

Industry	Pharmaceuticals
Bloomberg	LPC IN
BSE CODE	500257

Weak margins due to pricing pressures in major markets.

RATING	NEUTRAL
CMP	844
Price Target	868
Potential Upside	3%

Stock Info

52wk Range H/L	986/724
Mkt Capital (Rs Cr)	38174
Free float (%)	53%
Avg. Vol 1M (,000)	1687
No. of Shares	45
Promoters Pledged %	0%

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Key Highlights -

- ❑ US generic business witnessed volume growth and Price erosion stabilization for Glumetza and Fortamet as a result of supply chain issues among the peers.
- ❑ US Brand business has declined by 65% QoQ to US\$ 8 million as Methergine has gone generic.
- ❑ Japan was a challenging market on account of the biennial price cut.
- ❑ EBITDA margin has declined by 767 bps due to higher procurement prices in china and increased spend in the promotion of Solosec.
- ❑ Management guided for 18-19% margin based on the launch of Ranexa, Levothyroxine and ramp up Solosec in Q4FY19.

2Q FY19 Results-

In 2QFY19 Lupin's revenue remained flat YoY to Rs 3951 cr. Gross margin has declined on YoY by 270 bps due to higher procurement prices in China. US brand business revenue for the quarter were US\$ 8 million which declined by 65% YoY as Methergine has gone generic. Revenue from Japan has reduced by 6% on account of the biennial price cut. EBITDA margin has reduced YoY by 767 bps to 14% in comparison to the previous quarter due to increase in employee benefit expenses by 9% and increase in other expenses by 12%, Other expenses will continue to be higher for few coming quarters as it will include a recurring cost of around US\$ 12 crs for Solosec promotion in US. PAT has declined by 42% YoY to Rs 266 crs.

View and Valuation

Sales growth in Q2FY19 remained flat while gross margin contracted by 270 bps YoY. The US business continued to face the pricing pressure but gradually the market has started stabilizing and the management seems confident about the growth in the coming quarters. Japan business was impacted by biennial price cut last year, Japan would continue to be a challenging market as the country is getting ready for another price cut next year. Management has maintained its guidance of 14-15% growth for India business in FY19 based on the growing therapy areas. Going forward, we expect better performance in H2FY19 on account of Ranexa and levothyroxine launch in US, ramp up of Solosec and with flu season coming in, Tamiflu will be good contributor. We maintain our NEUTRAL stance with target price of Rs. 868 (27x FY20e EPS).

Key Risks to our rating and target

- ❑ Slow down in ANDA approvals.
- ❑ Biennial price cut in Japan.

KEY FINANCIAL/VALUATIONS	FY16	FY17	FY18	FY19E	FY20E
Net Sales	14256	17494	15804	17116	19556
EBITDA	3685	4493	3148	2899	3570
EBIT	3198	3581	2062	1913	2267
PAT	2261	2557	258	1488	1445
EPS (Rs)	50	57	6	33	32
EPS growth (%)	-6%	13%	-90%	476%	-3%
ROE (%)	20%	19%	2%	10%	9%
ROCE (%)	19%	19%	10%	9%	10%
BV	247	299	300	324	347
P/B (X)	6.0	4.8	2.5	2.6	2.4
P/E (x)	29.5	25.5	128.8	25.6	26.4

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2Q FY 19 Results

Weak margins YoY

Financials	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	YoY %	QoQ%	FY17	FY18	YoY %
Net Sales	3,952	3,976	4,034	3,856	3,951	0.0%	2.5%	17,494	15,804	-9.7%
Other Income	74	28	145	184	231	211.7%	25.2%	107	150	41.2%
COGS	1,287	1,393	1,363	1,444	1,393	8.3%	-3.6%	5,001	5,274	5.5%
Gross Margin	67%	65%	66%	63%	65%	-4.0%	3.5%	71%	67%	-6.7%
Employee Cost	725	693	729	749	794	9.5%	5.9%	2,850	2,865	0.5%
Other Expen.	1,087	1,202	1,234	1,135	1,215	11.7%	7.0%	5,150	4,518	-12.3%
EBITDA	853	688	709	527	550	-35.6%	4.3%	4,493	3,148	-29.9%
EBITDA Mar.	22%	17%	18%	14%	14%	-35.6%	1.8%	26%	20%	-22.5%
Depreciation	272	280	273	259	265	-2.5%	2.5%	912	1,086	19.0%
EBIT	581	408	436	268	284	-51%	6.0%	3,581	2,062	-42.4%
Interest	48	54	59	69	74	54%	7.4%	153	204	34.0%
PBT	607	382	522	383	441	-27.3%	15.0%	3,535	2,008	-43%
Exceptional			1,464						1,464	
Tax	154	161	(163)	181	173	12.2%	-4.5%	979	288	-71%
PAT	455	221	(784)	203	266	-41.5%	31.2%	2,557	258	-90%
PAT Margin	12%	6%	-19%	5%	7%	-41.5%	28.0%	15%	2%	-89%

Muted revenue growth

The company revenue growth was flat YoY but has increased QoQ by 2%. This sequential growth was due to growth in all major markets. On YoY basis, the US brand business has seen a decline of 65% as Methergine became generic. In the US generic business, the volume for Fortamet and Glumetza has increased as a result of supply chain issues among the peers. The Company has launched 5 products in the US market during the quarter which makes the total products in the US generic market to 162. Japan business has declined by 6% QoQ because of the price cut last year, and we believe revenue from Japan will continue to be depressed because the country is getting ready for another price cut next year. The performance in H2FY19 is expected to be better with launch of Ranexa, Levothyroxine and Ramp up of Solosec, Tamiflu will be a good contributor in Q4FY19 as flu season kicks in.

EBITDA has contracted YoY due to higher other expenses

EBITDA margin has reduced from 22% to 14% YoY due to increased spend on the promotion of Solosec and higher procurement prices in China. Other expenses will continue to be higher for coming few quarters as the company would continue to spend around US\$12 mn for Solosec. Management has guided for 18-19% margin for the full year as management is confident of better H2FY19 performance with the launch of Ranexa, Levothyroxine and ramp up Solosec.

Concall Highlights

- ❑ Volume has increased and price erosion has stabilized for Glumetza and Fortamet in US generic market.
- ❑ US revenue grew by 5% QoQ as base business on local currency grew by 3%
- ❑ Japan will continue to be a challenging market with next price cut scheduled next year.
- ❑ US branded sales were US\$ 8 million this quarter, of which Solosec sales were US\$ 3 million.
- ❑ There has been an impact of 26 crs because of FDC ban in India business this quarter.
- ❑ Other income includes Forex gain of 200 crs this quarter.
- ❑ Management is expecting 2HFY19 to be better with the launch of Ranexa, Levothyroxine, and ramp up of Solosec.
- ❑ US business- Tamiflu to be a good contributor in Q4FY19 as flu season kicks in.
- ❑ R&D expenditure is expected to be around Rs 1500-1600 crs for the full year.
- ❑ Management has guided for 14-15% India formulation growth in FY19.
- ❑ Management has guided for EBITDA margin 18-19% in FY19.
- ❑ Tax rate on standalone basis to be around 26%-27% and on consolidated basis to be around 32%-35% for the full year.

Exhibit: ANDA filings and ANDA pending

ANDA approvals were 7 this quarter while 4 ANDA were filed

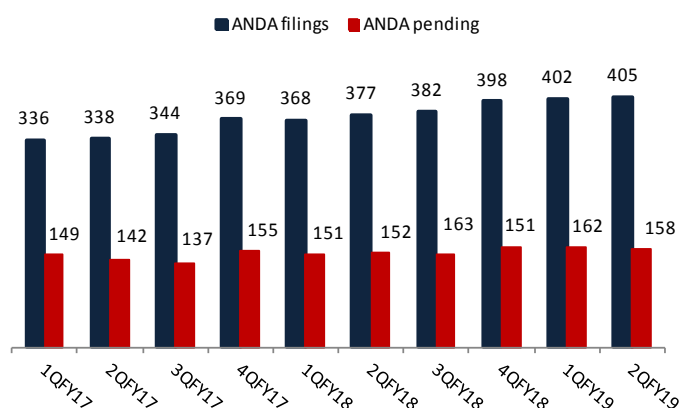


Exhibit: COGS and other expenses

COGS and other expenses for the quarter were 35% and 31% of the net sales.

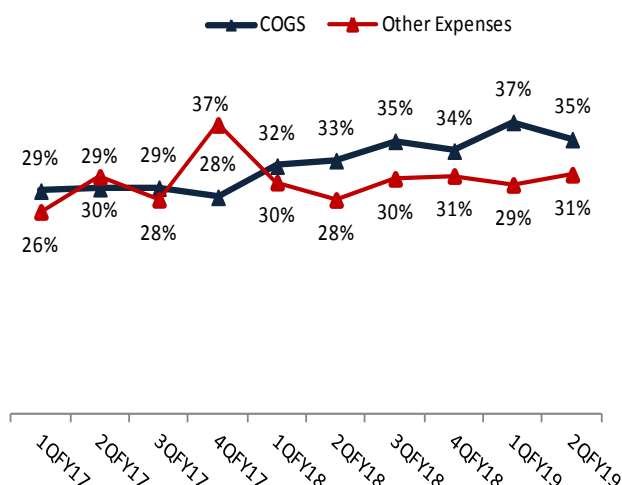


Exhibit: R&D spend and R&D expenses as % of sales

R&D expense for the quarter were Rs 376 crs, 9.5% of sales.

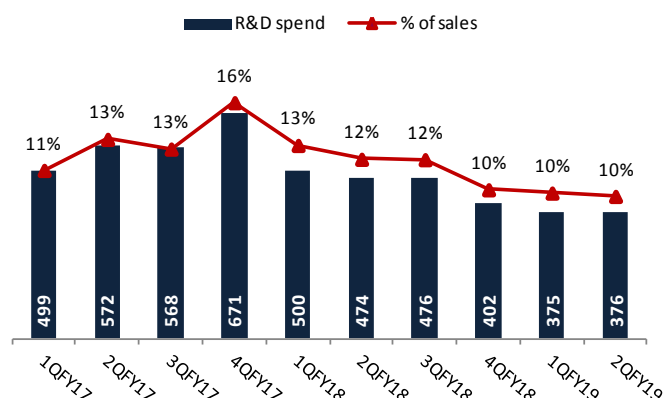


Exhibit: Sales and Sales Growth

Net sales for this quarter remained flat to 3951 crs (Vs our expectation of Rs 3825 crs)

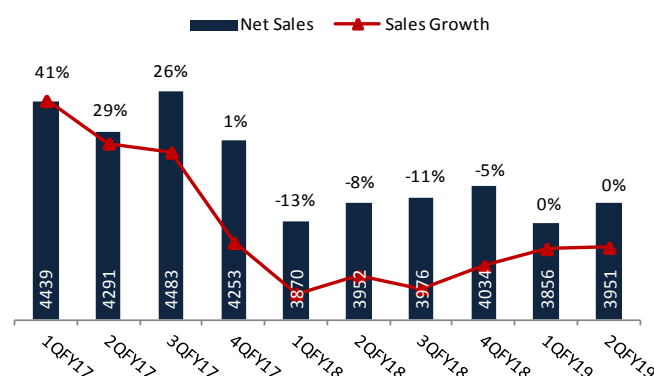


Exhibit: Gross and EBITDA Margin

Ebitda margin declined by 767 bps mainly led by higher COGS and other expenses.

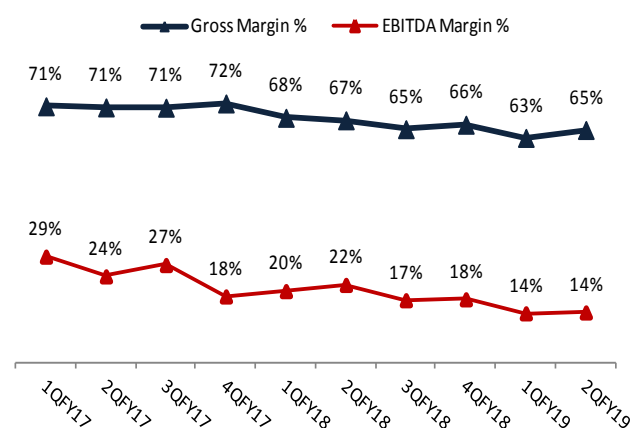
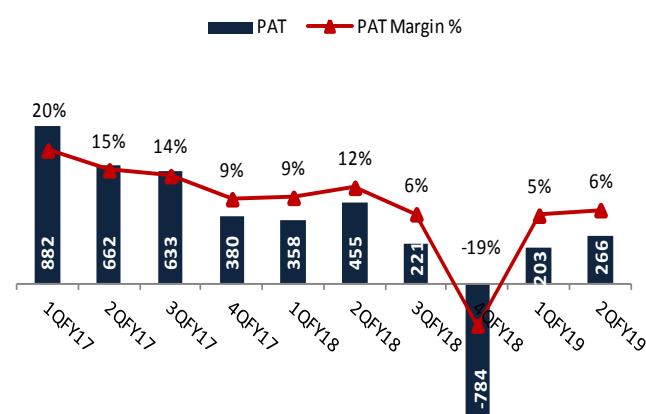


Exhibit: PAT and PAT Growth

PAT degrew by 42% YoY to 266 crs.



Operational Details

Geography	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19
<i>US</i>	1998	2176	1901	1602	1361	1432	1499	1186	1249
<i>India</i>	996	991	879	932	1159	1069	965	1192	1203
<i>APAC</i>	552	560	612	599	636	674	664	608	620
<i>EMEA</i>	236	256	301	226	276	272	351	276	295
<i>LATAM</i>	99	118	127	127	140	148	165	126	146
<i>ROW</i>	40	37	61	42	38	37	55	29	44
<i>API</i>	292	268	282	279	265	268	281	358	335

Revenue gr. %	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19
<i>US</i>	73%	58%	-13%	-27%	-32%	-34%	-21%	-26%	-8%
<i>India</i>	12%	12%	-11%	0%	16%	8%	10%	28%	4%
<i>APAC</i>	24%	21%	9%	11%	15%	20%	8%	1%	-2%
<i>EMEA</i>	6%	17%	18%	3%	17%	6%	17%	22%	7%
<i>LATAM</i>	-9%	33%	8%	17%	41%	26%	30%	-1%	5%
<i>ROW</i>	-4%	24%	66%	13%	-5%	1%	-11%	-30%	15%
<i>API</i>	-12%	-5%	5%	-3%	-9%	0%	0%	28%	26%

Revenue mix%	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19
<i>US</i>	47%	49%	46%	42%	35%	37%	38%	31%	32%
<i>India</i>	24%	23%	21%	24%	30%	27%	24%	32%	31%
<i>APAC</i>	13%	13%	15%	16%	16%	17%	17%	16%	16%
<i>EMEA</i>	6%	6%	7%	6%	7%	7%	9%	7%	8%
<i>LATAM</i>	2%	3%	3%	3%	4%	4%	4%	3%	4%
<i>ROW</i>	1%	1%	1%	1%	1%	1%	1%	1%	1%
<i>API</i>	7%	6%	7%	7%	7%	7%	7%	9%	9%

ANDA pipeline	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19
ANDA filings	338	344	369	368	377	382	398	402	405
ANDA approvals	196	207	214	217	225	231	235	240	247
ANDA pending	142	137	155	151	152	151	163	162	158

Financial Details

Balance Sheet

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Share Capital	90	90	90	90	90	90	90	90
Reserves	5,115	6,842	8,784	11,073	13,407	13,487	14,567	15,604
Networth	5,204	6,932	8,874	11,163	13,498	13,577	14,658	15,695
Debt	974	553	471	7,119	7,952	6,876	8,505	8,505
Other Non Current Liab	-	-	-	356	476	348	377	430
Total Capital Employed	6,178	7,485	9,345	18,283	21,450	20,453	23,162	24,199
Net Fixed Assets (incl CWIP)	2,804	3,002	3,296	9,154	10,856	10,512	11,906	12,206
Non Current Investments	2	2	3	14	22	27	6	6
Other Non Current Assets	-	-	0	65	105	159	172	197
Non Current Assets	3,771	4,106	5,305	12,737	14,653	14,096	15,230	15,567
Inventory	1,949	2,129	2,504	3,274	3,642	3,662	3,966	4,532
Debtors	2,187	2,464	2,657	4,549	4,307	5,192	4,689	5,358
Cash & Bank	435	798	481	793	682	1,394	1,660	1,526
Other Current Assets	233	231	193	1,191	1,076	1,246	1,350	1,542
Current Assets	5,143	6,100	7,832	9,887	11,954	12,201	13,791	15,150
Creditors	1,543	1,594	1,926	1,989	2,589	2,575	2,789	3,187
Provisions	112	132	162	190	309	357	361	383
Other Current Liabilities	381	288	830	898	566	1,283	1,007	1,124
Curr Liabilities	2,280	2,227	3,330	3,316	3,816	4,644	4,637	5,194
Net Current Assets	2,863	3,873	4,503	6,572	8,138	7,557	9,154	9,957
Total Assets	8,914	10,206	13,138	22,625	26,607	26,305	29,021	30,717

Income Statement

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
Revenue from Operation	9,641	11,287	12,770	14,256	17,494	15,804	17,116	19,556
Change (%)	36%	17%	13%	12%	23%	-10%	8%	14%
EBITDA	2,270	3,003	3,620	3,685	4,493	3,148	2,899	3,570
Change (%)	57%	32%	21%	2%	22%	-30%	-8%	23%
Margin (%)	24%	27%	28%	26%	26%	20%	17%	18%
Depr & Amor.	332	261	435	487	912	1,086	986	1,302
EBIT	1,938	2,742	3,185	3,198	3,581	2,062	1,913	2,267
Int. & other fin. Cost	41	27	10	59	153	204	230	230
Other Income	28	116	240	185	107	150	607	185
EBT	1,925	2,832	3,415	3,324	3,535	2,008	2,290	2,223
Exp Item	-	-	-	-	-	1,464		
Tax	584	962	970	1,059	979	288	801	778
Minority Int & P/L share of Ass.	26	33	41	9	7	-	-	-
Reported PAT	1,340	1,870	2,444	2,265	2,556	1,719	1,488	1,445
Adjusted PAT	1,314	1,836	2,403	2,261	2,557	258	1,488	1,445
Change (%)	51%	40%	31%	-6%	13%	-90%	476%	-3%
Margin(%)	14%	16%	19%	16%	15%	2%	9%	7%

Financial Details

Key Ratios

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
ROE	25%	26%	27%	20%	19%	2%	10%	9%
ROCE	36%	39%	35%	19%	19%	10%	9%	10%
Asset Turnover	1	1	1	1	1	1	1	1
Debtor Days	83	80	76	116	90	120	120	120
Inv Days	74	69	72	84	76	85	85	85
Payable Days	58	52	55	51	54	59	59	59
Int Coverage	47	103	325	54	23	10	8	10
P/E	21	23	38	30	26	129	26	26
Price / Book Value	5	6	10	6	5	2	3	2
EV/EBITDA	12	14	25	19	16	12	15	12
FCF per Share	16	33	41	(137)	33	4	15	11
Div Yield	0.5%	0.8%	0.3%	0.5%	0.5%	1.0%	0.9%	0.9%

Cash Flow Statement

Y/E March	FY13	FY14	FY15	FY16	FY17	FY18	FY19E	FY20E
PBT	1,925	2,832	3,415	3,329	3,543	547	2,290	2,223
(inc)/Dec in Working Capital	2,344	3,242	3,772	3,914	4,758	3,329	3,515	3,755
Non Cash Op Exp	332	261	435	487	912	1,086	986	1,302
Int Paid (+)	41	27	10	59	153	204	230	230
Tax Paid	(544)	(772)	(944)	(1,170)	(1,149)	(558)	(801)	(778)
others	207	59	313	3	799	92	7	659
CF from Op. Activities	1,251	2,004	2,733	(382)	4,115	1,751	3,079	2,105
(inc)/Dec in FA & CWIP	(551)	(529)	(871)	(5,822)	(2,637)	(1,553)	(2,381)	(1,602)
Free Cashflow	700	1,475	1,862	(6,204)	1,478	198	698	503
(Pur)/Sale of Inv	-	-	-	-	-	-	(1,382)	-
others	19	(334)	(187)	(1,184)	71	44	21	-
CF from Inv. Activities	(522)	(859)	(1,055)	(6,962)	(2,529)	(1,407)	(3,803)	(1,602)
inc/(dec) in NW								
inc/(dec) in Debt	(465)	(530)	(70)	6,208	605	(1,868)	1,628	-
Int. Paid	(42)	(28)	(11)	(58)	(151)	(204)	(230)	(230)
Div Paid (inc tax)	(143)	(321)	(134)	(337)	(338)	(338)	(339)	(339)
others	(26)	(2)	(23)	(69)	(69)	(69)	(69)	(69)
CF from Fin. Activities	(663)	(857)	(197)	5,836	433	(1,492)	990	(638)
Inc(Dec) in Cash	66	288	1,482	(1,508)	2,019	(1,148)	266	(135)
Add: Opening Balance	245	311	607	2,095	780	2,799	1,394	1,660
Closing Balance	311	607	2,108	780	2,799	1,651	1,660	1,526

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Analyst's ownership of the stocks mentioned in the Report	NIL
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*The name of the Company has been changed from “Microsec Capital Limited” to “Narnolia Financial Advisors Limited” pursuant to change of control. The change in name has been duly effected in the records of the Registrar of Companies (ROC). The application for fresh registration in the new name of “Narnolia Financial Advisors Limited” pursuant to change of control is under process with SEBI.

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Registered Office Address: Marble Arch, Office 201, 2nd Floor, 236B, AJC Bose Road, Kolkata 700 020; Tel No.: 033-4050 1500; www.narnolia.com

Compliance Officer: Manish Kr Agarwal, Email Id: mkagarwal@narnolia.com, Contact No.:033-40541700.

Registration details of Company: Narnolia Financial Advisors Ltd. (NFAL): SEBI Stock Broker Registration: INZ000166737 (NSE/BSE/MSEI); NSDL/CDSL: IN-DP-380-2018; Research Analyst: INH300002407, Merchant Banking: (Registration No.: INM000010791), PMS: (Registration No.: INP000002304), AMFIRegistered Mutual Fund distributor: ARN 3087

Registration Details of Group entities: G. Raj & Company Consultants Ltd (G RAJ)-BSE Broker INZ260010731; NSDL DP: IN-DP-NSDL-371-2014 || Narnolia Commerze Limited-MCX/NCDEX Commodities Broker: INZ000051636 || Narnolia Velox Advisory Ltd.- SEBI Registered PMS: INP000005109 || Eastwind Capital Advisors Pvt Ltd. (EASTWIND)-SEBI Registered Investment Adviser: INA300005439 || Narnolia Insurance Brokers Limited-IRDA Licensed Direct Insurance Broker (Life & Non-Life) License No.134 || Narnolia Securities Ltd. (NSL)-AMFI Registered Mutual Fund distributor: ARN 20558, PFRDA NPS POP: 27092018 || Narnolia Capital Advisors Pvt. Ltd. - RBI Registered NBFC:B.05.02568.

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