MOTILAL OSWAL

Lupin

STOCK INFO.	BLOOMBERG
BSE Sensex: 8,510	LPC IN
	REUTERS CODE
S&P CNX: 2,524	LUPN.BO

Equity Shares (m)	82.1
52-Week Range	779/430
1,6,12 Rel. Perf. (%)	22/60/57
M.Cap. (Rs b)	51.7
M.Cap. (US$ b)	1.0

27 October 2008

Buy

Previous Recommendation: Buy

Rs630

YEAR END	NET SALES (RS M)	PAT (RS M)	EPS (RS)	EPS GROWTH (%)	P/E (X)	P/BV (X)	ROE (%)	ROCE (%)	EV/ SALES	EV/ EBITDA
03/07A	20,057	2,327	26.4	23.0	23.9	5.8	31.1	20.1	2.8	19.3
03/08A	27,064	3,334	37.8	43.3	16.7	4.0	31.0	22.0	2.3	14.0
03/09E	36,251	4,385	49.7	31.5	12.7	3.2	30.4	22.5	1.7	9.5
03/10E	42,694	5,628	63.8	28.3	9.9	2.6	31.0	24.6	1.4	7.4

Lupin's 2QFY09 results were above our estimates. Key highlights:

- Net sales grew by 42% to Rs9.3b (vs estimates of Rs8.3b) while adjusted PAT grew by 53% to Rs1.15b (vs estimates of Rs956m). Organic top-line growth (excluding Kyowa & Rubamin acquisitions) was 18%. EBITDA margins expanded by 200bp to 19% (vs estimate of 18%) led by better product-mix and currency depreciation.
- **Niche/IPR opportunities gaining visibility** – Lupin has a track record of launching low-competition IPR driven products in the US for the past few years. We expect this trend to continue in the future also with the company targeting to launch oral contraceptive products in the coming years.
- **Expect 30% EPS CAGR** – We expect Lupin's core operations (excluding one-off upsides) to record 25% sales and 30% earnings CAGR for FY08-10 led by traction in regulated markets, strong growth in domestic formulations and incremental savings from tax-exempt zones. The growth will be led by 23% CAGR for the regulated dosage form business and 21% CAGR for the domestic formulations business.

Lupin is likely to witness a gradual improvement in the underlying fundamentals led by an expanding US generics pipeline, niche / Para-IV opportunities in the US, strong performance from Suprax (branded product in US) and ramp-up in formulation revenues from its European initiative. Incremental benefits are likely to be visible from the Jammu facility which enjoys fiscal benefits. We expect the company to record EPS of Rs49.7 and Rs63.8 for FY09 and FY10 respectively. Given the strong earnings growth, valuations at 12.7x FY09E and 9.9x FY10E consolidated earnings are attractive. Reiterate **Buy.**

QUARTERLY PERFORMANCE (CONSOLIDATED) (Rs Million)

Y/E MARCH	FY08				FY09				FY08	FY09E
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE		
Net Sales	**5,757**	**6,590**	**7,213**	**7,504**	**8,624**	**9,343**	**9,066**	**9,219**	**27,064**	**36,251**
YoY Change (%)	*14.1*	*34.9*	*42.7*	*41.1*	*49.8*	*41.8*	*25.7*	*22.9*	*34.4*	*33.9*
Total Expenditure	4,936	5,464	5,998	6,307	7,097	7,555	7,437	7,625	22,705	29,713
EBITDA	**821**	**1,126**	**1,215**	**1,197**	**1,527**	**1,788**	**1,629**	**1,594**	**4,358**	**6,538**
Margins (%)	*14.3*	*17.1*	*16.8*	*16.0*	*17.7*	*19.1*	*18.0*	*17.3*	*16.1*	*18.0*
Depreciation	127	140	175	206	193	201	210	266	647	870
Interest	89	80	101	104	102	127	160	193	374	582
Other Income	159	188	1,389	328	202	13	100	150	2,065	465
PBT	**764**	**1,094**	**2,329**	**1,216**	**1,433**	**1,474**	**1,359**	**1,285**	**5,402**	**5,551**
Tax	206	338	520	255	313	312	285	255	1,318	1,166
Rate (%)	*26.9*	*30.9*	*22.3*	*20.9*	*21.8*	*21.2*	*21.0*	*19.9*	*24.4*	*21.0*
Reported PAT	**558**	**756**	**1,809**	**961**	**1,120**	**1,162**	**1,074**	**1,030**	**4,084**	**4,385**
Extra-Ordinary Exp/(Inc)	0	0	-748	0	0	0	0	0	-748	0
Recurring PAT	**559**	**756**	**1,060**	**959**	**1,121**	**1,156**	**1,074**	**1,030**	**3,334**	**4,385**
YoY Change (%)	*4.4*	*45.9*	*70.9*	*47.0*	*100.6*	*52.9*	*1.3*	*7.4*	*43.3*	*31.5*
Margins (%)	*9.7*	*11.5*	*14.7*	*12.8*	*13.0*	*12.4*	*11.8*	*11.2*	*12.3*	*12.1*

E: MOSt Estimates

Nimish Desai (Nimishdesai@MotilalOswal.com); Tel: +91 22 3982 5406

Formulations exports, currency depreciation drive revenue growth

Consolidated net sales of Lupin grew by 42% to Rs9.3b (vs estimate of Rs8.3b) while PAT grew by 53% to Rs1.15b (vs estimate of Rs956m). Adjusted for the one-time VRS charge of Rs297m, PAT growth was 88% to Rs1.4b. Organic topline growth (excluding acquisitions) is 18%; while acquired companies - Kyowa contributed Rs1b and Rubamin Rs160m to the topline.

Topline growth was led by 82% growth in formulation exports to regulated markets which contributed 29% (Rs2.7b) to revenues. Kyowa (Japan) has reported higher sales backed by 10 new launches in the Japanese market.

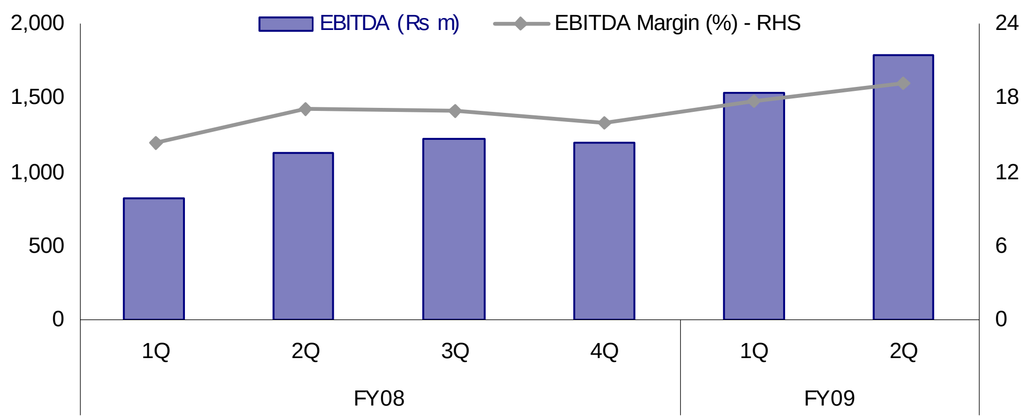
REVENUE BREAK-UP

GROSS SALES (RS M)	2QFY09	2QFY08	YOY (%)	1QFY09	QOQ (%)
India					
APIs	660	693	-4.8	642	2.8
Formulations	3,033	2,602	16.6	2,926	3.7
Total India Sales	**3,693**	**3,295**	**12.1**	**3,568**	**3.5**
% of sales	*39.0*	*48.8*		*40.6*	
Regulated markets					
APIs	210	216	-2.8	201	4.5
Formulations	2,719	1,570	73.2	2,530	7.5
Total regulated markets sales	**2,929**	**1,786**	**64.0**	**2,731**	**7.3**
% of sales	*30.9*	*26.4*		*31.1*	
Un-regulated markets					
APIs	1,050	1,422	-26.1	1,153	-8.9
Formulations	442	236	87.3	361	22.4
Total un-regulated markets sales	**1,492**	**1,658**	**-10.0**	**1,514**	**-1.5**
% of sales	*15.7*	*24.5*		*17.2*	
Kyowa (Japan)	**1,013**	**0**		**920**	
Others	**354**	**17**		**59**	
Total Gross Sales	**9,481**	**6,756**	**40.3**	**8,792**	**7.8**

Source: Company/Motilal Oswal Securities

EBITDA margins expanded by 200bp to 19% (vs estimate of 18%) led by better product-mix and currency depreciation.

TREND IN EBITDA MARGINS



Source: Company/Motilal Oswal Securities

Core business gaining strength

We expect Lupin to record 25% revenue CAGR for the core business in the FY08-10 period led by 23% CAGR for the regulated dosage form business and 21% CAGR for the domestic formulations business. We believe that the company is gaining critical mass in the US market while European market revenues are likely to gradually ramp-up beginning FY09E onwards.

US portfolio gaining critical mass

Lupin has adopted a pragmatic mix of normal, niche (low-competition) and Para-IV products for its US business. It also has Suprax – a branded product – in its portfolio which is likely to generate about US$40m in revenues for FY09E. Unlike many other generic companies, Lupin has focused on building a pipeline of niche, low-competition products for the US market rather than going in for a large number of filings. This strategy is evident from the successful launch of Ceftriaxone and Cefdinir over the last two years. Management has indicated that it has more such products in its pipeline to be launched over the next few years. Key focus segments for the company in the US include Cephalosporins (including injectables), CVS and CNS areas.

Suprax recording strong growth, but will face competition from FY10E onwards

Lupin is one of the few Indian companies to have a branded product in its portfolio in the US market. The company re-launched Suprax (a pediatric anti-infective) by licensing it from Fujisawa since its US partner (Wyeth) had stopped promoting the drug since 2003.

After facing some initial teething problems (in gaining doctor prescriptions), Suprax is now recording strong growth and contributes significantly to the company's margins. Suprax sales have grown at 80% CAGR (albeit on low base) to reach revenues of US$40m by FY08. We, however, believe that this product is likely to face competitive pressures in FY10E as some generic companies have already filed DMFs for the product. Our estimates take in to account this potential decline in revenues.

European sales to kick-in from FY09E onwards

Lupin is primarily targeting the French and UK markets for entering the EU markets. It is working on a combination strategy of forming partnerships with generic players in some geographies and entering the market directly in some others. It had launched Cefpodoxime Proxetil 100mg tablet in France (Euro 75m market) in FY08 and it expects to launch another 6-8 products in EU markets in FY09E.

Lupin has a pipeline of over 20 products filed with the UK regulatory authority and about 10 in France. This pipeline is likely to be commercialized over the next few years leading to a rapid ramp-up in EU revenues, albeit on a low base of US$20m in FY08.

Acquisitions as entry vehicle

Lupin has adopted a strategy of entering new markets through small-sized acquisitions of front-end companies which, gives the company access to the latter's distribution network. Expect for the Kyowa acquisition (Japan), all other acquisitions were small-sized. Lupin had announced two acquisitions in FY08 - Kyowa in Japan & Rubamin Labs in India - as entry vehicles for its Japanese and CRAMS initiatives respectively.

Kyowa's product portfolio and distribution network is likely to facilitate Lupin's entry into the Japanese generic market. The company has recently announced acquisition of Hormosan Pharma (Germany) and a minority stake in Generic Health Pty (Australia) as an entry strategy in these markets.

Japan – Kyowa acquisition to exploit unfolding opportunity

Lupin acquired a 79% stake in Kyowa Pharma (Japan) for US$60m (plus debt of about US$50m) in Oct-2007. Before the acquisition, it already had an arrangement with Kyowa wherein Lupin was involved in product development and manufacture whereas Kyowa brought in strengths in conducting biostudies, obtaining regulatory approvals and marketing.

Kyowa recorded revenues of US$60-70m for FY07 with ~15% EBITDA margins and has a strong presence in CNS, CVS and GI segments. While Lupin has not disclosed Kyowa's profits, it has indicated that the acquisition will be EPS accretive over the next 3 years.

The US$68b Japanese market is the second largest pharmaceutical market globally but suffers from low generic penetration (only 5%) as it was only in 2006 that the government has enacted regulations to encourage generics. Generic companies face formidable entry barriers in Japan owing to complex regulatory environment and strong patent framework (which allows multiple patent extensions), making it imperative to enter the market through a local partner (Ranbaxy and Cadila have also taken the partnership approach).

We do not expect any significant upside to Lupin's bottom-line in the short-term from the acquisition. However, we believe that Kyowa offers a good platform to Lupin for ramping-up its Japanese presence and is likely to bring in long-term benefits. Japan is likely to be the next big generic opportunity globally as the government has just commenced viewing generics favourably. Lupin management has guided the Kyowa sales are likely to record 12-15% growth in FY09E led by new launches. The company has recently received approval for 10 products from the Japanese authorities, which are likely to be launched in the coming quarters.

Expect 21% CAGR for the domestic formulations portfolio

From a predominantly anti-TB and malaria player, Lupin has undergone a significant transformation over the last few years by focusing more on chronic therapy segments like CVS, Asthma and Diabetology. The company has consistently out-performed the average industry growth for the past 3 years.

We expect Lupin to continue its strong momentum in the domestic formulations market led by increasing focus on life-style segments, aggressive new launches and increased penetration (it has almost doubled its field force in the last 3 years). We expect the company to record 21% CAGR for the domestic formulations business in the FY08-10 period.

Niche/IPR opportunities gaining more visibility

Lupin's strategy of focusing on niche, low-competition products for the US market has resulted in launch of Ceftriaxone, Cefdinir and Ramipril over the last few years. While competitive pressures are building up for Cefdinir and Ramipril, we believe that Lupin will have such niche, low-competition opportunities every year given its existing product pipeline. It also plans to file for oral contraceptive products for the US market in FY09E, which could again be potentially a low-competition, high-margin opportunity.

Patent challenges/settlements giving large one-time upsides

Lupin has commenced monetizing its patent challenge pipeline by entering into a settlement with Servier (France) for Perindopril. It has till date received Rs2.6b in settlement amount. The Para-IV pipeline includes some more such patent challenges, but given the uncertainty related to such filings, our estimates do not include any upsides from these patent challenges.

Valuations are attractive, Expect 30% earnings CAGR

Lupin is likely to witness a gradual improvement in the underlying fundamentals led by an expanding US generics pipeline, niche opportunities in the US and pick up in Suprax prescription share. Incremental benefits are likely to be visible from the recently commissioned Jammu facility which enjoys fiscal benefits.

We expect Lupin to record 30% earnings CAGR for FY08-10 period. We expect 20+% RoCE for the next few years led by traction in regulated and domestic formulations markets and incremental savings from tax-exempt zones. Lupin is currently valued at 12.7x FY09E and 9.9x FY10E consolidated earnings. We maintain **Buy** with a price target of Rs957. Earlier than expected competition for Suprax (in US) and significant currency appreciation are the key risks to our positive stance.

Lupin: an investment profile

Company description

Lupin is one of the second tier Pharma companies that is actively targeting the regulated generics markets. Historically very strong in the anti-TB segment, it has over the years built up expertise in fermentation-based products and segments like cephalosporins, prils and statins. Lupin is now a fully integrated company, with manufacturing capabilities in APIs and formulations and a direct marketing presence in the target markets.

Key investment arguments

- In the process of building a strong pipeline for the US market through aggressive filings – benefits expected to flow in over the next couple of years.
- Pediatric opportunity (Suprax), statins offer significant potential upsides that are not factored into our estimates.

Key investment risks

- Short-term financial performance would remain under pressure given slow scale up in US business and ramping up of R&D and regulatory filing costs.
- Commodity like nature of its developing markets business could lead to volatility in earnings.

Recent developments

- Acquired Hormosan Pharma (Germany) and a minority stake in Generic Health Pty (Australia)

Valuation and view

- Valuations at 12.7x FY09E and 9.9x FY10E EPS are attractive given EPS CAGR of 30% for FY08-10.
- Maintain **Buy** with price target of Rs957.

Sector view

- Regulated markets would remain the key sales and profit drivers in the medium term. Europe is expected to emerge as the next growth driver, particularly for companies with a direct marketing presence.
- We are overweight on companies that are towards the end of the investment phase, with benefits expected to start coming in from the next fiscal.

COMPARATIVE VALUATIONS

		LUPIN	SUN PHARMA	WOCKHARDT
P/E (x)	FY09E	12.7	26.1	6.7
	FY10E	9.9	21.3	5.5
P/BV (x)	FY09E	3.2	4.8	1.2
	FY10E	2.6	4.0	1.0
EV/Sales (x)	FY09E	1.7	7.2	1.4
	FY10E	1.4	6.0	1.2
EV/EBITDA (x)	FY09E	9.5	19.7	6.0
	FY10E	7.4	15.5	5.2

SHAREHOLDING PATTERN (%)

	SEP-08	JUN-08	SEP-07
Promoter	51.0	51.1	51.2
Domestic Inst	21.2	20.4	14.0
Foreign	16.2	17.2	20.7
Others	11.6	11.3	14.2

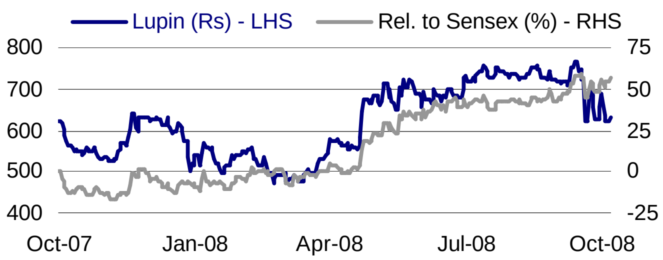
EPS: MOST FORECAST VS CONSENSUS (RS)

	MOST FORECAST	CONSENSUS FORECAST	VARIATION (%)
FY09	49.7	48.3	3.0
FY10	63.8	58.2	9.5

TARGET PRICE AND RECOMMENDATION

CURRENT PRICE (RS)	TARGET PRICE (RS)	UPSIDE (%)	RECO.
630	957	51.9	Buy

STOCK PERFORMANCE (1 YEAR)



INCOME STATEMENT (Rs Million)

Y/E MARCH	2006	2007	2008	2009E	2010E
Net Sales	**16,858**	**20,057**	**27,064**	**36,251**	**42,694**
Change (%)	*34.2*	*19.0*	*34.9*	*33.9*	*17.8*
Total Expenditure	14,623	17,135	22,705	29,713	34,363
EBITDA	**2,236**	**2,922**	**4,358**	**6,538**	**8,331**
Margin (%)	*13.3*	*14.6*	*16.1*	*18.0*	*19.5*
Depreciation	409	466	647	870	1,010
Int. and Finance Charges	313	372	374	582	861
Other Income - Rec.	741	847	937	465	593
PBT before EO item	2,255	2,931	4,275	5,551	7,052
EO Expense/(Income)	35	-1,143	-1,127	0	0
PBT after EO item	**2,221**	**4,075**	**5,402**	**5,551**	**7,052**
Tax	521	988	1,318	1,166	1,425
Tax Rate (%)	*23.5*	*24.0*	*25.0*	*21.0*	*20.2*
Reported PAT	**1,699**	**3,086**	**4,084**	**4,385**	**5,628**
PAT Adj for EO items	**1,726**	**2,327**	**3,336**	**4,385**	**5,628**
Change (%)	*87.1*	*34.9*	*43.3*	*31.5*	*28.3*
Less: Minority Interest	4	1	2	0	0
Adj Net Profit	**1722**	**2327**	**3334**	**4385**	**5628**

CONSOLDIATED BALANCE SHEET (Rs Million)

Y/E MARCH	2006	2007	2008	2009E	2010E
Equity Share Capital	401	803	821	821	821
Fully Diluted Equity Capital	*401*	*882*	*882*	*882*	*882*
Total Reserves	5,831	7,930	11,976	15,258	19,404
Net Worth	**6,233**	**8,733**	**12,797**	**16,079**	**20,225**
Minority Interest	-1	-1	95	95	95
Deferred liabilities	956	1,027	1,107	1,107	1,107
Total Loans	9,249	8,648	12,029	13,529	14,529
Capital Employed	**16,437**	**18,407**	**26,027**	**30,809**	**35,955**
Gross Block	8,561	9,528	14,859	17,359	19,359
Less: Accum. Deprn.	2,096	2,382	4,698	5,567	6,577
Net Fixed Assets	**6,466**	**7,146**	**10,161**	**11,791**	**12,782**
Capital WIP	252	826	964	250	250
Investments	28	28	58	58	58
Goodwill			1,872	2,772	2,772
Curr. Assets	**13,315**	**14,629**	**20,441**	**24,555**	**30,421**
Inventory	3,429	4,298	7,893	8,700	10,247
Account Receivables	3,112	4,039	7,439	9,063	11,527
Cash and Bank Balance	4,774	3,845	2,742	3,308	4,378
Others	2,000	2,448	2,367	3,484	4,269
Curr. Liability & Prov.	**3,624**	**4,222**	**7,470**	**8,618**	**10,328**
Account Payables	3,147	3,515	6,019	7,251	8,540
Provisions	477	707	1,451	1,367	1,788
Net Current Assets	**9,691**	**10,407**	**12,971**	**15,937**	**20,093**
Appl. of Funds	**16,437**	**18,407**	**26,027**	**30,809**	**35,955**

E: MOSt Estimates

RATIOS

Y/E MARCH	2006	2007	2008	2009E	2010E
Basic (Rs)					
EPS (Fully Diluted)	**21.4**	**26.4**	**37.8**	**49.7**	**63.8**
Cash EPS (Fully Diluted)	26.5	31.7	45.1	59.6	75.2
BV/Share	77.5	108.6	155.8	195.8	246.3
DPS	3.2	5.0	6.0	11.5	15.4
Payout (%)	17.5	15.2	14.1	25.2	26.3
Valuation (x)					
P/E (Fully Diluted)		23.9	16.7	12.7	9.9
Cash P/E (Fully Diluted)		19.9	14.0	10.6	8.4
P/BV		5.8	4.0	3.2	2.6
EV/Sales		2.8	2.3	1.7	1.4
EV/EBITDA		19.3	14.0	9.5	7.4
Dividend Yield (%)		0.8	1.0	1.8	2.4
Return Ratios (%)					
RoE	31.0	31.1	31.0	30.4	31.0
RoCE	20.6	20.1	22.0	22.5	24.6
Working Capital Ratios					
Asset Turnover (x)	1.0	1.1	1.0	1.2	1.2
Debtor (Days)	65	71	98	90	97
Inventory (Days)	74	78	106	88	88
Wkg. Capital Turnover (Days)	210	189	175	160	172
Leverage Ratio					
Debt/Equity (x)	1.5	1.0	0.9	0.8	0.7

CASH FLOW STATEMENT (Rs Million)

Y/E MARCH	2006	2007	2008	2009E	2010E
Oper. Profit/(Loss) before Tax	2,236	2,922	4,358	6,538	8,331
Interest/Dividends Recd.	741	847	937	465	593
Direct Taxes Paid	-500	-917	-1,238	-1,166	-1,425
(Inc)/Dec in WC	-1,128	-1,646	-3,667	-2,400	-3,086
EO expense	35	-1,143	-1,127	0	0
CF from Op. incl EO Exp.	**1,314**	**2,350**	**1,518**	**3,438**	**4,413**
(inc)/dec in FA	-800	-1,720	-5,674	-1,786	-2,000
(Pur)/Sale of Investments	-2	0	-30	-900	0
CF from Investments	**-801**	**-1,720**	**-5,704**	**-2,686**	**-2,000**
Issue of Shares	-76	-116	652	0	0
(Inc)/Dec in Debt	4,677	-601	3,381	1,500	1,000
Interest Paid	-313	-372	-374	-582	-861
Dividend Paid	-298	-470	-576	-1,103	-1,482
CF from Fin. Activity	**3,991**	**-1,560**	**3,083**	**-185**	**-1,343**
Inc/Dec of Cash	**4,503**	**-930**	**-1,103**	**566**	**1,070**
Add: Beginning Balance	271	4,774	3,845	2,742	3,308
Closing Balance	**4,774**	**3,845**	**2,742**	**3,308**	**4,378**

For more copies or other information, contact
Institutional: Navin Agarwal. **Retail:** Manish Shah
Phone: (91-22) 39825500 Fax: (91-22) 22885038. E-mail: inquire@motilaloswal.com

Motilal Oswal Securities Ltd, 3rd Floor, Hoechst House, Nariman Point, Mumbai 400 021

Disclosure of Interest Statement	Lupin
1. Analyst ownership of the stock	No
2. Group/Directors ownership of the stock	No
3. Broking relationship with company covered	No
4. Investment Banking relationship with company covered	No