

12 November 2010

MF Global Quarterly Report

Cipla

| Turning the corner

PHARMACEUTICALS

CIPLA IN: UPGRADE TO BUY

RS 332

We upgrade Cipla to BUY from Neutral with a price target of Rs 373, valuing the stock at 23x FY12 earnings. After successive quarters of subdued growth in the domestic formulations, Cipla has reported a strong 20% growth this quarter. We believe growth in this space of around 15% (management guidance of 20%) is sustainable for Cipla over the next few quarters as new product launches, recent addition in field force start kicking in. Export formulations witnessed a strong growth of 14% for the quarter and we believe this momentum is likely to sustain going forward as new partnerships are formed (like the recent one with Dr Reddy's for CIS markets). Licensing income, an integral part of Cipla's profits was weak this quarter (de-growth of 76%) but given the shape the core business is taking, reliance on this income to drive profits would be low in the future.

Core EBITDA margins for the quarter (excluding the forex gain of Rs 150-200mn) were marginally below estimates on account of overheads costs at the newly commissioned facility at Indore. Given that the facility is currently not profitable (cost of Rs 250-300mn per quarter, insignificant revenues), we believe operating margins may see a sharp improvement in H2 FY12 when the facility starts generating revenue (recently approved by WHO and South Africa recently, awaiting inspection by UK, Australian agencies over the next few months).

We believe Cipla's management is being conservative with a 8-10% topline growth guidance for FY12. Our estimates do not include potential launch of basket of inhalers in EU over the next 2 years (NPV Rs 35-40) and any outsourcing deal with an MNC pharma company. Strong balance sheet makes Cipla an attractive investment opportunity with a long term perspective.

TARGET RS 374 (+13%)

SECTOR RATING

OW	N	UW

STOCK RATING

BUY	NEUTRAL	SELL
> 15%	-15% TO +15%	< -15%

COMPANY DATA

O/S SHARES:	803MN
MARKET CAP (RS):	266BN
MARKET CAP (USD):	6BN
52 - WK HI/LO (RS):	364 / 299
AVG. DAILY VOL. (3MTH):	1.9MN
FACE VALUE (RS):	2

SHARE HOLDING PATTERN, %

PROMOTERS:	36.8
FII / NRI:	20.3
FI / MF:	17.5
NON PROMOTER CORP. HOLDINGS:	3.9
PUBLIC & OTHERS:	21.5

PRICE PERFORMANCE, %

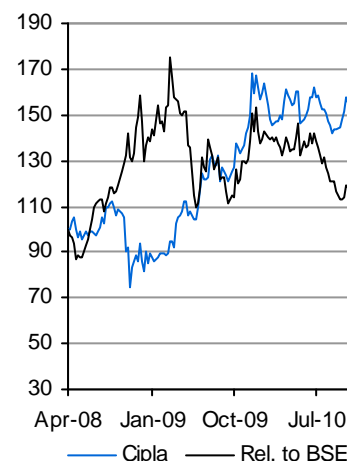
	1MTH	3MTH	1YR
ABS	-2.1	6.0	9.2
REL TO BSE	-3.3	-7.9	-13.0

VALUATION SUMMARY

Y/E MAR, RS MN	FY2008	FY2009	FY2010	FY2011E	FY2012E
NET SALES	40,103	49,601	53,595	60,384	68,056
GROWTH, %	16.6	23.7	8.1	12.7	12.7
EBIDTA	8,317	12,215	13,330	14,294	16,804
EBIDTA MARGINS, %	20.7	24.6	24.9	23.7	24.7
CORE EBIDTA	8,317	12,215	13,330	14,294	16,804
NET PROFIT	6,678	8,932	10,355	10,567	12,496
NET PROFIT MARGIN, %	16.7	18.0	19.3	17.5	18.4
EPS, RS	8.6	11.5	12.9	13.2	15.6
EPS GROWTH, %	2.5	33.8	12.2	2.0	18.3
PER, X	38.5	28.8	25.7	25.2	21.3
EV/EBIDTA, X	31.5	21.8	19.9	18.3	15.5
EV/NET SALES, X	6.5	5.4	4.9	4.3	3.8
PRICE/BOOK VALUE, X	6.9	5.9	4.5	3.9	3.4
ROIC, %	17.2	17.9	19.2	18.2	19.1
ROE, %	19.1	22.0	20.2	16.7	17.1
DIVIDEND YIELD, %	0.6	0.6	0.6	0.6	0.6

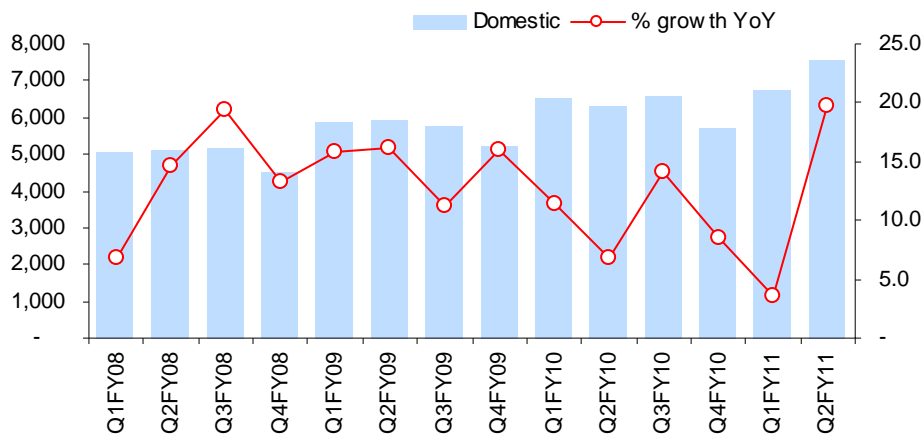
Source: Company, MF Global India Research Estimates

PRICE VS. SENSEX



Source: Bloomberg, MF Global India Research

TREND IN DOMESTIC FORMULATION SALES



Source: Company

REVENUE BREAKUP

RS MN	Q2 FY11	Q2 FY10	% CHANGE
DOMESTIC FORMULATIONS	7,564	6,314	19.8
EXPORTS - FORMULATIONS	6,639	5,819	14.1
EXPORTS - APIS	1,683	1,706	(1.3)
TOTAL EXPORTS	8,322	7,525	10.6
TOTAL SALES (A)	15,886	13,839	14.8
TECHNOLOGY KNOWHOW/FEES	120	508	(76.4)
EXPORT INCENTIVE /OTHERS	235	209	12.4
OTHER OPERATING INCOME (B)	355	717	-50.5
TOTAL OPERATING INCOME (A+B)	16,241	14,556	11.6

Source: Company

QUARTERLY RESULT

RS MN	Q2 FY11	Q2 FY10	% CHANGE
NET SALES & INCOME FROM OPERATIONS	16,154	14,429	12.0
A) RAW MATERIAL COST	7,487	6,396	17.1
B) STAFF COST	1,376	864	59.2
C) OTHER EXPENDITURE	3,625	3,436	5.5
TOTAL EXPENDITURE	12,488	10,695	16.8
EBITDA	3,666	3,733	(1.8)
DEPRECIATION	639	478	33.7
OTHER INCOME	166	128	29.8
INTEREST	3	84	(96.7)
PBT	3,190	3,300	-3.3
PBT MARGIN	20.2	24.1	-16.1
FX (GAIN) / LOSS	0	-75	(100.0)
TOTAL TAXATION	560	618	(9.3)
TAX RATE, %	17.6	18.7	-
REP PAT	2,630	2,757	-4.6
ADJ. PAT	2,630	2,565	2.5
BASIC & DILUTED EPS	3.3	3.2	2.5

Source: Company

COMMON SIZE (%)

	Q2 FY11	Q2 FY10	% CHANGE
A) RAW MATERIAL COST	46.3	44.3	202BPS
B) STAFF COST	8.5	6.0	253BPS
C) OTHER EXPENDITURE	22.4	23.8	-137BPS
TOTAL EXPENDITURE	77.3	74.1	318BPS
EBITDA	22.7	25.9	-318BPS

Source: Company

FINANCIALS

INCOME STATEMENT

Y/E MAR, RS MN	FY2008	FY2009	FY2010	FY2011E	FY2012E
NET SALES	40,103	49,601	53,595	60,384	68,056
<i>GROWTH, %</i>	17	24	8	13	13
OTHER INCOME	2,054	2,737	2,654	1,898	1,959
TOTAL INCOME	42,157	52,338	56,249	62,282	70,015
OPERATING EXPENSES	-33,840	-40,123	-42,919	-47,988	-53,211
EBITDA (CORE)	8,317	12,215	13,330	14,294	16,804
<i>GROWTH, %</i>	1.2	46.9	9.1	7.2	17.6
<i>MARGIN, %</i>	20.7	24.6	24.9	23.7	24.7
DEPRECIATION	-1,163	-1,518	-1,671	-2,120	-2,468
EBIT	7,154	10,697	11,659	12,174	14,335
<i>GROWTH, %</i>	1.2	46.9	9.1	7.2	17.6
<i>MARGIN, %</i>	20.7	24.6	24.9	23.7	24.7
INTEREST PAID	-113	-329	-230	0	0
OTHER NON-OPERATING INCOME	672	918	881	872	904
NON-RECURRING ITEMS	334	-1,109	470	0	0
PRE-TAX PROFIT	8,047	10,177	12,780	13,045	15,239
TAX PROVIDED	-1,036	-2,354	-1,955	-2,479	-2,743
PROFIT AFTER TAX	7,011	7,823	10,825	10,567	12,496
NET PROFIT	7,011	7,823	10,825	10,567	12,496
MF NET PROFIT	6,678	8,932	10,355	10,567	12,496
<i>GROWTH, %</i>	3.6	33.8	15.9	2.0	18.3
NET PROFIT (ADJUSTED)	6,678	8,932	10,355	10,567	12,496
EXTRAORDINARY ITEMS: GAINS/(LOSSES)	334	-1,109	470	0	0
UNADJ. SHARES (M)	777	777	803	803	803
WTD AVG SHARES (M)	777	777	803	803	803

CASH FLOW

Y/E MAR, RS MN	FY2008	FY2009	FY2010	FY2011E	FY2012E
PRE-TAX PROFIT	8,047	10,177	12,780	13,045	15,239
DEPRECIATION	1,163	1,518	1,671	2,120	2,468
CHG IN WORKING CAPITAL	-2,016	-1,429	-8,741	-4,218	-8,725
TOTAL TAX PAID	-724	-2,411	-3,755	-991	-2,089
CASH FLOW FROM OPERATING ACTIVITIES	6,470	7,854	1,955	9,956	6,894
CAPITAL EXPENDITURE	-1,494	-4,627	-3,571	-4,482	-4,000
CHG IN INVESTMENTS	230	135	-1,664	0	0
OTHER INVESTING ACTIVITIES	-4,000	-1,512	0	0	0
CASH FLOW FROM INVESTING ACTIVITIES	-5,264	-6,004	-5,235	-4,482	-4,000
FREE CASH FLOW	1,206	1,850	-3,280	5,474	2,894
EQUITY RAISED/(REPAID)	0	0	6,691	0	0
DEBT RAISED/(REPAID)	96	-194	-24	0	0
DIVIDEND (INCL. TAX)	-1,819	-1,819	-1,825	-1,873	-1,879
OTHER FINANCING ACTIVITIES	0	0	0	0	0
CASH FLOW FROM FINANCING ACTIVITIES	-1,724	-2,012	4,842	-1,873	-1,879
NET CHG IN CASH	-518	-163	1,562	3,601	1,015

BALANCE SHEET

AS AT 31ST MAR, RS MN	FY2008	FY2009	FY2010	FY2011E	FY2012E
CASH & BANK	797	534	621	4,222	5,237
MARKETABLE SECURITIES AT COST	0	0	0	0	0
DEBTORS	14,065	18,529	15,666	18,498	23,595
INVENTORY	11,205	13,983	15,126	16,011	17,605
LOANS & ADVANCES	11,035	10,899	11,682	13,435	15,450
OTHER CURRENT ASSETS	345	234	578	636	700
TOTAL CURRENT ASSETS	37,446	44,179	43,673	52,801	62,586
INVESTMENTS	935	801	2,464	2,464	2,464
GROSS FIXED ASSETS	22,018	26,933	28,973	36,376	41,836
LESS: DEPRECIATION	-5,404	-7,008	-8,861	-10,981	-13,449
ADD: CAPITAL WIP	2,331	3,663	6,842	3,921	2,461
NET FIXED ASSETS	18,945	23,588	26,954	29,316	30,848
NON-CURRENT ASSETS	0	0	0	0	0
TOTAL ASSETS	57,326	68,568	73,091	84,581	95,898
CURRENT LIABILITIES	13,687	19,290	9,809	11,052	11,066
PROVISIONS	4,374	4,130	2,381	3,445	3,582
TOTAL CURRENT LIABILITIES	18,061	23,420	12,190	14,497	14,647
NON-CURRENT LIABILITIES	1,713	1,669	1,796	2,291	2,840
TOTAL LIABILITIES	19,774	25,090	13,986	16,788	17,487
PAID-UP CAPITAL	1,555	1,555	1,606	1,606	1,606
RESERVES & SURPLUS	35,997	41,923	57,500	66,188	76,805
SHAREHOLDERS' EQUITY	37,552	43,478	59,106	67,793	78,411
TOTAL EQUITY & LIABILITIES	57,326	68,568	73,091	84,581	95,898

PER-SHARE DATA

	FY2008	FY2009	FY2010	FY2011E	FY2012E
MF EPS (INR)	8.6	11.5	12.9	13.2	15.6
GROWTH, %	2.5	33.8	12.2	2.0	18.3
BOOK NAV/SHARE (INR)	48.3	55.9	73.6	84.4	97.7
FDEPS (INR)	8.6	11.5	12.9	13.2	15.6
CEPS (INR)	9.7	14.9	14.4	15.8	18.6
CFPS (INR)	2.1	2.6	13.5	11.4	7.5
DPS (INR)	2.0	2.0	2.0	2.0	2.0

FINANCIAL STRUCTURE

	FY2008	FY2009	FY2010	FY2011E	FY2012E
TOTAL DEBT/EQUITY (%)	15.5	21.6	0.1	0.0	0.0
NET DEBT/EQUITY (%)	13.3	20.4	(1.0)	(6.2)	(6.7)

PROFITABILITY, PRODUCTIVITY, LIQUIDITY AND VALUATION RATIOS

	FY2008	FY2009	FY2010	FY2011E	FY2012E
RETURN ON ASSETS (%)	14.0	12.8	15.5	13.4	13.8
RETURN ON EQUITY (%)	19.1	22.0	20.2	16.7	17.1
RETURN ON INVESTED CAPITAL (%)	17.2	17.9	19.2	18.2	19.1
ROIC/COST OF CAPITAL (X)	2.1	2.1	2.4	2.3	2.4
ROIC - COST OF CAPITAL (%)	9.0	9.5	11.3	10.3	11.2
RETURN ON CAPITAL EMPLOYED (%)	19.3	18.9	20.5	16.0	16.4
COST OF CAPITAL (%)	8.3	8.4	7.9	7.9	7.9
ROCE - COST OF CAPITAL (%)	11.0	10.5	12.6	8.1	8.5
ASSET TURNOVER (X)	1.0	0.9	0.9	1.0	0.9
SALES/TOTAL ASSETS (X)	0.8	0.8	0.8	0.8	0.8
SALES/NET FA (X)	2.4	2.3	2.1	2.1	2.3
RECEIVABLE DAYS	128.0	136.3	106.7	111.8	126.5
INVENTORY DAYS	102.0	102.9	103.0	96.8	94.4
PAYABLE DAYS	57.5	41.5	68.5	53.9	47.4
CURRENT RATIO (X)	2.1	1.9	3.7	3.8	4.5
QUICK RATIO (X)	1.5	1.3	2.4	2.6	3.2
INTEREST COVER (X)	63.1	32.5	50.8	-	-
DIVIDEND COVER (X)	4.3	5.7	6.4	6.6	7.8
PER (X)	38.5	28.8	25.7	25.2	21.3
PEG (X) - Y-O-Y GROWTH	15.3	0.9	2.1	12.3	1.2
PRICE/BOOK (X)	6.9	5.9	4.5	3.9	3.4
YIELD (%)	0.6	0.6	0.6	0.6	0.6
EV/NET SALES (X)	6.5	5.4	4.9	4.3	3.8
EV/EBITDA (X)	31.5	21.8	19.9	18.3	15.5
EV/EBIT (X)	31.5	21.8	19.9	18.3	15.5
EV/NOPLAT (X)	36.0	27.0	23.3	22.1	18.5
EV/CE	6.6	5.8	4.3	3.7	3.2
EV/IC (X)	6.2	5.1	4.5	4.1	3.6

Source: Company, MF Global India Research Estimates

RECOMMENDATION HISTORY

RECOMMENDATION	TARGET, RS	CMP, RS	DATE
BUY	374	332	12 NOVEMBER 2010
NEUTRAL	339	342	7 MAY 2010
BUY	373	319	28 JANUARY 2010
NEUTRAL	323	290	29 OCTOBER 2009
NEUTRAL	260	269	27 AUGUST 2009
NEUTRAL	258	253	30 JUNE 2009

VINEET BHATNAGAR	MANAGING DIRECTOR	91-22-2300 2999	VBHATNAGAR@MFGLOBAL.COM
SAJID KHALID	HEAD – INSTITUTIONAL EQUITIES	91-22-6667 9972	SAKHALID@MFGLOBAL.COM
JIGNESH SHAH	HEAD – EQUITY DERIVATIVES	91-22-6667 9735	JSHAH@MFGLOBAL.COM

Equity Research

AMBRISH MISHRA	VP - AUTOMOBILES, AUTO COMPONENT	91-22-6667 9758	AMISHRA@MFGLOBAL.COM
MANISH AGARWALLA	VP - BANKING	91-22-6667 9962	MAGARWALLA@MFGLOBAL.COM
ABHISHEK RANGANATHAN, CFA	RETAIL, REAL ESTATE	91-22-6667 9952	ABHISHEKR@MFGLOBAL.COM
ALOK DALAL	PHARMACEUTICALS	91-22-6667 9950	ALDALAL@MFGLOBAL.COM
ANJALI VERMA	ECONOMIST	91-22-6667 9969	ANVERMA@MFGLOBAL.COM
DHAWAL DOSHI	METALS, POWER	91-22-6667 9769	DDOSHI@MFGLOBAL.COM
DIPESH SOHANI	REAL ESTATE	91-22-6667 9756	DSOHANI@MFGLOBAL.COM
GAURI ANAND	OIL & GAS, FERTILISER	91-22-6667 9943	GANAND@MFGLOBAL.COM
KAPIL BAGARIA	MIDCAP, SUGAR	91-22-6667 9965	KBAGARIA@MFGLOBAL.COM
NAVEEN KULKARNI, FRM	TELECOM, FMCG, MEDIA	91-22-6667 9947	NKULKARNI@MFGLOBAL.COM
VAIBHAV AGARWAL	CEMENT	91-22-6667 9966	VAGARWAL@MFGLOBAL.COM
VIHANG NAIK	IT SERVICES, MIDCAP	91-22-6667 9768	VNAIK@MFGLOBAL.COM
DHARMESH SHAH	RESEARCH ASSOCIATE	91-22-6667 9974	DHSHAH@MFGLOBAL.COM
ENNETTE FERNANDES	RESEARCH ASSOCIATE	91-22-6667 9764	EFERNANDES@MFGLOBAL.COM
JISHAR THOOMBATH	RESEARCH ASSOCIATE	91-22-6667 9986	JTHOOMBATH@MFGLOBAL.COM
NEHA GARG	RESEARCH ASSOCIATE	91-22-6667 9992	NGARG@MFGLOBAL.COM
SAPNA SHAH	RESEARCH ASSOCIATE	91-22-6667 9996	SAPSHAH@MFGLOBAL.COM
SAURABH RATHI	RESEARCH ASSOCIATE	91-22-6667 9951	SRATHI@MFGLOBAL.COM
SHUBHANGI AGRAWAL	RESEARCH ASSOCIATE	91-22-6667 9964	SAGRAWAL@MFGLOBAL.COM
VARUN VIJAYAN	RESEARCH ASSOCIATE	91-22-6667 9759	VVIJAYAN@MFGLOBAL.COM
GANESH DEORUKHKAR	PRODUCTION	91-22-6667 9999	GDEORUKHKAR@MFGLOBAL.COM
ROSHNI KALLOOR	RESEARCH COMPLIANCE OFFICER	91-22-6667 9762	RKALLOOR@MFGLOBAL.COM

Technical & Quant Research

NEPPOLIAN PILLAI	CHIEF TECHNICAL STRATEGIST	91-22-6667 9989	PNEPPOLIAN@MFGLOBAL.COM
SHIKHA KHURANA	QUANT ANALYST	91-22-6667 9948	SKHURANA@MFGLOBAL.COM

Institutional Cash Equity Sales

SUDHIR PADIYAR	VP - EQUITY SALES (ASIAPAC)	91-22-6667 9991	SPADIYAR@MFGLOBAL.COM
KINSHUK TIWARI	EQUITY SALES	91-22-6667 9946	KTIWARI@MFGLOBAL.COM
NASIR MOHAMED	EQUITY SALES	91-22-6667 9973	NMOHAMED@MFGLOBAL.COM
SHEETAL GANDHI	EQUITY SALES (US)	91-22-6667 9944	SGANDHI@MFGLOBAL.COM
PAYAL PANCHAL	ASSOCIATE SALES (DMA)	91-22-6667 9949	PPANCHAL@MFGLOBAL.COM
ROSIE FERNS	SR. EXEC. – EQUITIES SALES SUPPORT	91-22-6667 9971	RFERNS@MFGLOBAL.COM

Institutional Cash Equity Sales Trading

SUNIL KAMATH	VP - SALES TRADER	91-22-6667 9747	SKAMATH@MFGLOBAL.COM
CHETAN SAVLA	SALES TRADER	91-22-6667 9749	CSAVLA@MFGLOBAL.COM
RAJESH ASHAR	SALES TRADER	91-22-6667 9746	RASHAR@MFGLOBAL.COM

Institutional Cash Equity Dealing

CHETAN BABARIA	DEALER	91-22-6667 9945	CBABARIA@MFGLOBAL.COM
MAYUR SHAH	DEALER	91-22-6677 9945	M SHAH@MFGLOBAL.COM

Rating Rationale

BUY and SELL recommendations are used to draw attention to stocks, which we believe are under-priced or over-priced by circa 15%, that is, price differential of +/- 15% between our price target and the market price. Stocks which do not achieve this price differential are NEUTRAL. Price targets are established in the context of a flat market.

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2nd Floor, C-Block, Modern Centre
Mahalaxmi, Mumbai
400 011

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