

**Milind Bhargale**

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**Shareholding (%)**

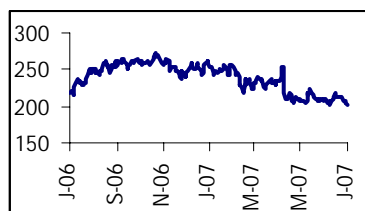
Promoters	39.4
FII's	15.7
MF/FI's/banks	3.1
Insurance Co.	9.5
Others	32.3

**Share price performance**

52-week high/low (Rs)	280/180		
	-1m	-3m	-12m
Abs (%)	-1.6	-4.7	-7.7
Rel* (%)	-8.8	-16.4	-58.8

\*to Nifty

**Stock chart**



**Results below expectation**

Cipla Ltd's Q1FY08 numbers were significantly below our estimates. During the quarter, the company's net sales were marginally up 4.9% YoY at Rs9bn; however, EBITDA and PAT declined by 29.8% and 29.7% YoY at Rs1.6bn and Rs1.2bn respectively. Sales were below our expectation on account of lower domestic formulations growth and lower export revenue, which were partially affected by rupee appreciation. Cipla's EBITDA margin declined by 880bps YoY at 17.8% during the quarter. The company has given a guidance of 10-12% growth in sales.

We are reducing FY08E and FY09E EPS estimates by 14% and 15.4% respectively, on account of appreciating rupee and change in product-mix. At revised earnings, Cipla trades at 23.3x FY08E EPS of Rs8.6 and 19.4x FY09E EPS of Rs10.4. We recommend 'Reduce' rating on the stock.

**Key highlights of Q1FY08 results are:**

- During Q1FY08, domestic formulation sales grew modestly by 7% YoY at Rs4.8bn, which is significantly below the market growth rate. This was mainly on account of lower stocking of certain older brands at the primary level.
- Cipla's gross margin reduced from 55.2% to 50.2%, due to change in product-mix and appreciation of Indian rupee. Staff costs and other expenses have also gone up significantly on YoY basis, resulting in lower EBITDA margin of 17.8% (26.6% in Q1FY07).
- In Q1FY08, formulation export sales grew marginally by 2.1% YoY to Rs4bn, which was mainly on account of rupee appreciation and lower formulation exports to regulated markets. In our opinion, the company is facing challenges in sustaining historical growth rates on a much larger export base, and increase in formulation exports seems to come from lower margin products. API exports have grown by 8.5% YoY at Rs816mn.
- Valuation:** We are reducing FY08E and FY09E EPS estimates by 14% and 15.4% respectively, and expect the stock to be under pressure for the next couple of quarters. Cipla has given a guidance of 10-12% growth in sales. At revised earnings, the company trades at 23.3x FY08E EPS of Rs8.6 and 19.4x FY09E EPS of Rs10.4. We recommend 'Reduce' rating on the stock.

**Reduce  
Rs201**

July 23, 2007

**Market cap**

Rs bn 156  
US\$ mn 3,858

**Avg 3m daily volume**

2,933,936

**Avg 3m daily value**

USD mn 15

**Shares outstanding (mn)**

777

**Reuters**

CIPL.BO/CIPLA.NA

**Bloomberg**

CIPLA IN

**Sensex**

15,566

**Nifty**

4,566

**Table 1. Sales mix**

Rs mn	Q1FY08	Q4FY07	QoQ(%)	Q1FY07	YoY(%)
Domestic sales (net of excise) (a)	4783.5	3778.1	26.6	4460.5	7.2
% to sales	54.3	41.6		53.1	
Exports					
Formulations	3203.4	3878.7	(17.4)	3186.5	0.5
Formulations/Total Sales %	79.7	73.3		80.9	
APIs	815.8	1414.6	(42.3)	751.7	8.5
Total Exports (b)	4019.2	5293.3	(24.1)	3938.2	2.1
% of exports to sales	45.7	58.4		46.9	
<b>Total Sales (a+b)</b>	<b>8802.7</b>	<b>9071.4</b>	<b>(3.0)</b>	<b>8398.7</b>	<b>4.8</b>
Other operating income					
Technology Knowhow/Fees	113.4	242.0		90.2	
Technology Knowhow fees/Sales %		77.2		44.6	
Others	102.2	71.3		112.1	
Total (c)	215.6	313.3	(31.2)	202.3	6.6
<b>Total operating income (a+b+c)</b>	<b>9018.3</b>	<b>9384.7</b>	<b>(3.9)</b>	<b>8601</b>	<b>4.9</b>

Source: IISL research, company

**Table 2. Quarterly result table**

Rs mn	Q1FY08	Q4FY07	QoQ%	Q1FY07	YoY%
Gross Sales	9288.3	9603.8	-3.3	8869.1	4.7
Excise Duty	270	219.1		268.1	
(%) of Gross sales	2.9	2.3		3.0	
Net Sales	9018.3	9384.7	(3.9)	8601.0	4.9
Total Expenses	7411.4	7914.8		6312.3	
(%) of net sales	82.2	84.3		73.4	
EBITDA	1606.9	1469.9	9.3	2288.7	(29.8)
Depreciation	302.5	260.8		260.0	
EBIT	1304.4	1209.1	7.9	2028.7	(35.7)
Interest	8.2	12.9		27.9	
Other Income	185.4	220.6		219.5	
PBT	1481.6	1416.8	4.6	2220.3	(33.3)
Provision for tax(including deferred tax)	284	159.5		516.0	
PAT	1197.6	1257.3	(4.7)	1704.3	(29.7)
Equity (Face value 2)	1554.6	1554.6		1554.6	
EPS (Rs.)	1.5	1.6		2.2	
<b>Key Ratios (%)</b>					
EBITDA Margin	17.8	15.7		26.6	
Interest/ Sales	0.1	0.2		0.3	
Tax/PBT	19.2	13.0		23.2	
Other Income/Sales	2.1	2.8		2.6	
NPM	13.3	13.4		19.8	

Source: IISL research, company

## Financials

### Profit & Loss

In Rs million	FY06	FY07E	FY08E	FY09E
Net sales	29,858.8	35,721.4	40,433.8	47,796.0
YoY (%)	32.4	19.6	13.2	18.2
Total expenses	23,060.7	27,493.8	32,136.4	37,787.3
Inc/dec in stock	(943.5)	338.2	(508.8)	(852.4)
Raw material cost	15,059.2	16,941.7	20,574.5	24,066.1
Staff cost	1,507.6	1,842.9	2,395.8	3,114.5
Power and fuel cost	630.8	738.0	845.5	1,004.7
Other manufacturing expenses	2,790.5	3,104.5	3,595.5	4,234.8
Selling Expenses	2259.3	2473.1	2818.3	3349.0
Other expenses	1,756.8	2,055.5	2,415.7	2,870.6
EBIDTA	6,798.1	8,227.6	8,297.4	10,008.8
YoY (%)	34.1	21.0	0.8	20.6
EBIDTA (%)	22.8	23.0	20.5	20.9
Other income	1,216.3	891.3	931.4	931.4
PBIDT	8,014.4	9,118.9	9,228.8	10,940.1
Interest	114.2	69.6	77.0	99.1
Gross profit	7,900.2	9,049.3	9,151.7	10,841.1
Depreciation	801.8	1,040.8	1,107.0	1,206.3
PBT and extra ordinary	7,098.4	8,008.5	8,044.8	9,634.8
Extra ordinary items	941.9	0.0	0.0	0.0
PBT	8,040.3	8,008.5	8,044.8	9,634.8
(-) Tax	1,022.0	1,400.1	1,325.8	1,589.7
Tax/ PBT	12.7	17.5	16.5	16.5
PAT	7,018.3	6,608.4	6,719.0	8,045.0
Adjusted net profit	7,018.3	6,608.4	6,719.0	8,045.0
YoY (%)	66.5	(5.8)	1.7	19.7

### Key Ratios

	FY06	FY07E	FY08E	FY09E
EPS (Rs)	23.4	8.5	8.6	10.4
CEPS (Rs)	26.7	10.0	10.1	12.1
Book value (Rs)	66.1	41.7	46.3	52.7
Dividend per share (Rs)	5.9	3.4	4.0	4.0
Debt-equity (x)	0.2	0.0	0.1	0.0
ROCE	24.5	21.8	19.0	20.9
ROE	35.4	20.4	18.6	19.6

### Valuations

	FY06	FY07E	FY08E	FY09E
PE (x)	8.6	23.6	23.3	19.4
Cash PE (x)	7.5	20.1	19.9	16.6
Price/book value (x)	3.0	4.8	4.3	3.8
Dividend yield	2.9	1.7	2.0	2.0
Market cap/sales	2.0	4.4	3.9	3.3
EV/sales (x)	2.2	4.4	3.9	3.3
EV/EBDITA (x)	9.5	18.9	18.9	15.6

### Balance Sheet

In Rs million	FY06	FY07E	FY08E	FY09E
Equity capital	599.7	1,554.6	1,554.6	1,554.6
Preference capital	0.0	0.0	0.0	0.0
Reserves	19,233.0	30,854.9	34,472.5	39,416.1
Net worth	19,832.7	32,409.5	36,027.0	40,970.7
Total borrowings	4,689.1	576.1	1,831.8	1,139.4
Deferred tax	979.5	1,104.5	1,143.1	1,287.6
Total liabilities	25,501.3	34,090.1	39,001.9	43,397.7
Gross block	13,666.7	16,141.1	18,141.1	20,141.1
Less: Acc. depreciation	3,100.6	4,141.4	5,248.4	6,454.7
Net block	10,566.1	11,999.7	12,892.7	13,686.4
CWIP	870.1	400.0	400.0	400.0
Investments	224.3	6,892.1	9,498.0	9,514.2
Current assets	22,922.8	26,135.3	30,376.0	35,596.1
Inventories	9,570.0	9,139.5	10,628.7	12,432.6
Debtors	8,759.6	10,647.5	12,298.9	14,615.1
Cash	444.8	1,000.0	1,000.0	1,000.0
Loans and advances	4,148.4	5,348.4	6,448.4	7,548.4
Current liabilities	6,358.9	7,788.8	10,173.5	11,807.7
Provisions	2,723.1	3,548.3	3,991.4	3,991.4
Net current assets	13,840.8	14,798.2	16,211.1	19,797.0
Miscellaneous expenses	0.0	0.0	0.0	0.0
Total assets	25,501.3	34,090.0	39,001.9	43,397.6

### Cash Flow

In Rs million	FY06	FY07E	FY08E	FY09E
Net profit	7,124.1	6,608.4	6,719.0	8,045.0
Depn and w/o	801.8	1,040.8	1,107.0	1,206.3
Deferred tax	90.0	125.0	38.6	144.5
Change in working cap	(3,802.0)	(402.2)	(1,413.0)	(3,585.9)
Other income	1,216.3	891.3	931.4	931.4
Operating cash flow	2,997.6	6,480.7	5,520.2	4,878.6
Other income	1,216.3	891.3	931.4	931.4
Capex	(3,789.3)	(2,004.3)	(2,000.0)	(2,000.0)
Investments	(41.3)	(6,667.8)	(2,605.9)	(16.2)
Investing cash flow	(2,614.3)	(7,780.8)	(3,674.5)	(1,084.8)
Dividend	(1,772.6)	(2,658.3)	(3,101.4)	(3,101.4)
Fresh equity	(1,055.1)	7,671.8	0.0	0.0
Debt	2,777.1	(4,113.0)	1,255.7	(692.4)
Financing cash flow	(50.6)	900.4	(1,845.7)	(3,793.8)
Others	0.1	954.8	0.0	0.0
Net change in cash	332.8	555.2	0.0	(0.0)
Opening cash	112.0	444.8	1,000.0	1,000.0
Closing cash	444.8	1,000.0	1,000.0	1,000.0

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