

## Equities

17 November 2011 | 7 pages

# Lupin (LUPN.BO)

## Alert: Adding Muscle in Japan

We expect Lupin's acquisition of I'rom Pharma to strengthen its presence in Japan by providing exposure to injectables & the growing DPC hospitals segment. While financial details are sketchy, the management has indicated that the deal would be earnings accretive from the outset. Lupin remains one of our top picks in the sector.

- **The deal** – Lupin's Japanese subsidiary (Kyowa) entered into an agreement with I'rom Holdings of Japan to acquire up to 100% stake in the latter's subsidiary I'rom Pharmaceuticals. This is Lupin's second acquisition in the Japanese market.
- **About I'rom Pharmaceuticals** – I'rom Pharma is a specialty injectables company in Japan, established in 1947 and has its headquarters in Tokyo. It primarily caters to the Diagnosis Procedure Combination (DPC) hospitals in Japan. DPC hospitals are fixed rate/flat sum reimbursement hospitals and hence more likely to promote generics. These account for over 35% of overall hospital beds in the country. It had revenues of JPY5,361m (cUS\$69m) in FY11 (year to March), with single-digit margins.
- **Consolidating its presence in Japan** – With this acquisition, Lupin further strengthens its presence in the high potential Japanese market. The combined entity (Kyowa + I'rom) would have revenues of cUS\$230-240m in Japan – c15% of Lupin's overall turnover. I'rom's injectables portfolio is complementary to Kyowa's oral portfolio. Besides, Lupin can now seek to leverage I'rom's strong position in Japan's hospitals to introduce injectables from its own product basket in this market. Lupin remains the only Indian play, with any degree of scale, on the Japanese generics opportunity.
- **What is the financial impact?** – Very few financial details are available, making it difficult for us to independently ascertain the financial impact at this stage. The management has indicated that the transaction would be accretive to earnings from the outset. We understand that margins are well below Lupin's corporate average (would improve going forward) but this is offset by the valuation (undisclosed) and low cost of funds (possible low cost debt raised in Japan). Lupin's track record on inorganic initiatives also gives us comfort on this front.

### Company Update

<b>Buy</b>	<b>1</b>
Price (17 Nov 11)	Rs446.65
Target price	Rs565.00
Expected share price return	26.5%
Expected dividend yield	0.9%
<b>Expected total return</b>	<b>27.4%</b>
Market Cap	Rs199,447M US\$3,930M

### Price Performance (RIC: LUPN.BO, BB: LPC IN)



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# Lupin

## Valuation

Given that pharma is a growth sector, we use P/E as our primary method to value the base business of pharma companies. Lupin has historically (last six to seven years) traded in a band of 10-34x one-year forward earnings. We value Lupin at 20x 12m forward earnings, in line with the sector leaders such as Cipla and Dr Reddy's, due to its leadership in key markets/products & robust financial metrics. At 20x Dec12E recurring FDEPS, we arrive at a target price of Rs565.

## Risks

Key risks to our target price include: 1) Earlier than expected generic competition in Suprax; 2) INR appreciation would hurt, given its exposure to global markets; 3) Reasonable exposure to the domestic formulations market (c31% of sales) leaves Lupin vulnerable to any significant widening of the price control net or slow down in industry growth. 4) Inability to effectively scale up the Kyowa operations or Antara sales.

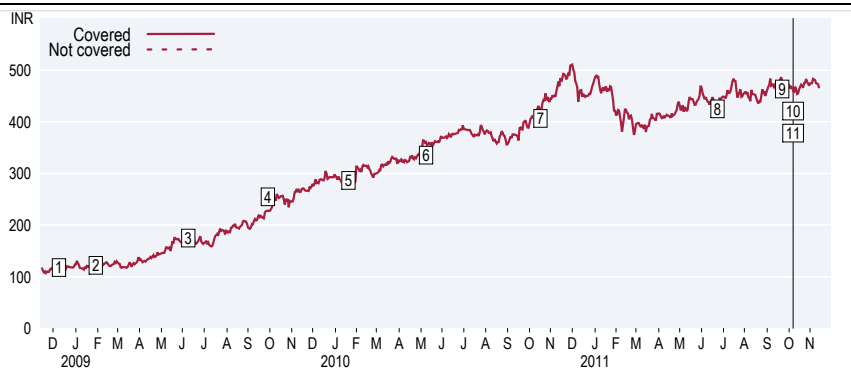
## Appendix A-1

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Ratings and Target Price History  
Fundamental Research  
Analyst: Prashant Nair, CFA



	Date	Rating	Target Price	Closing Price
1	9-Dec-08	1M	*164.60	111.40
2	29-Jan-09	1M	*178.80	112.23
3	9-Jun-09	1M	*213.00	167.80
4	29-Sep-09	1M	*283.00	227.96

	Date	Rating	Target Price	Closing Price
5	20-Jan-10	1M	*340.00	284.82
6	9-May-10	*1L	*420.00	359.42
7	17-Oct-10	1L	*500.00	425.80
8	23-Jun-11	1L	*525.00	430.15

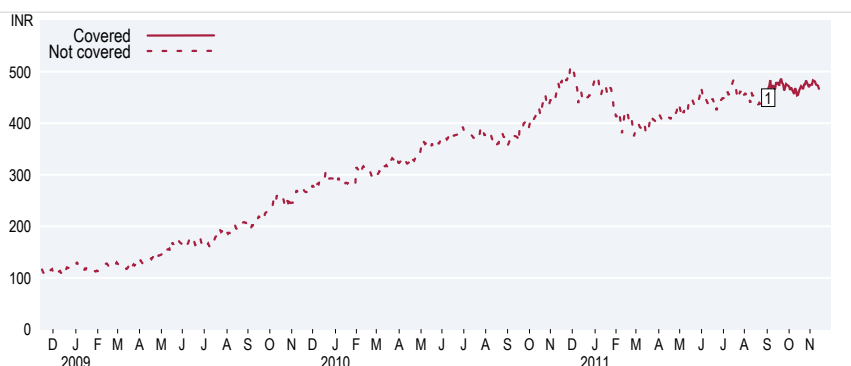
	Date	Rating	Target Price	Closing Price
9	22-Sep-11	1L	*565.00	478.20
10	7-Oct-11	Stock rating system changed		
11	7-Oct-11	*1	565.00	461.00

\* Indicates change

Rating/target price changes above reflect Eastern Standard Time

**Lupin (LUPN.BO)**  
**Ratings and Target Price History**  
**Best Ideas Research**  
**Relative Call (3 Month)**

Analyst: Prashant Nair, CFA



Date	Rating	Target Price	Closing Price
2-Sep-11	*ADD MP	-	467.60

\* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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	59%	34%	7%	10%	79%	10%
	45%	42%	37%	50%	43%	46%

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