

November 09, 2017

Surajit Pal
surajitpal@plindia.com
+91-22-66322259

Rating	Accumulate
Price	Rs832
Target Price	Rs963
Implied Upside	15.7%
Sensex	33,251
Nifty	10,309

(Prices as on November 09, 2017)

Trading data

Market Cap. (Rs bn)	69.1
Shares o/s (m)	83.1
3M Avg. Daily value (Rs m)	159.1

Major shareholders

Promoters	59.76%
Foreign	10.75%
Domestic Inst.	11.17%
Public & Other	18.32%

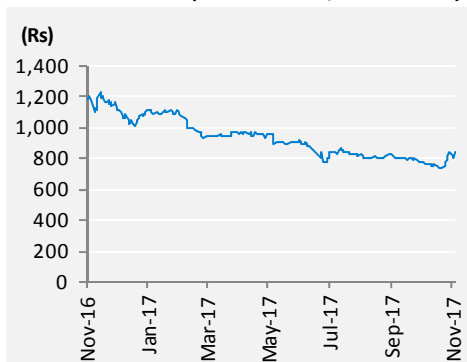
Stock Performance

(%)	1M	6M	12M
Absolute	6.9	(12.9)	(29.8)
Relative	2.4	(23.9)	(51.8)

How we differ from Consensus

EPS (Rs)	PL	Cons.	% Diff.
2018	22.0	20.7	6.3
2019	27.4	25.0	9.4

Price Performance (RIC: DLPA.NS, BB: DLPL IN)



Source: Bloomberg

■ **Sales in line; margin, earnings beat consensus:** DLPL's revenue grew 6% YoY to Rs2.8bn in Q2FY18, in line with our estimates. Adj. EBITDA (adjusted for ESOP charges) and PAT declined by 1.5% and 3% YoY to Rs808m and Rs507m respectively. With favourable product mix, seasonal tailwind of Dengue outbreak and higher B-2-C contribution, Adj. EBITDA margin was 29%, 220bps lower YoY due to delayed and weaker outbreak of vector borne diseases. We however expect delayed Dengue outbreak will have spill over benefits in Q3FY18E, which is conventionally weaker for DLPL.

■ **Volumes growth driver in revenue growth:** DLPL's revenue growth of 6.1% was contributed by 6.7% volume growth with Rs699 revenues/patient. DLPL's revenues/patient decreased due to rationalisation of certain tests at local markets in non-NCR region. Delhi remain major growth center with 11% growth and consolidated patient base was 4m in Q2FY18. The seasonal revenue boosts in Q2FY18 from the breakout of Vector borne diseases (chikungunya, Dengue) occur typically in the month of August and September.

■ **HLM contributes 14% revenues:** Currently, Hospital Lab management (HLM) contributed 13% of revenues in Q2FY18. Though the business contributes high sales, relative margins are lower and DLPL is cautiously optimistic in expansion of this lower margin business due to volatile receivable management.

■ **Valuation-Downgrade to 'Accumulate', reduce TP to Rs963:** While cash flow remain strong in pathology business, the scalability of growth remain a challenger given that PE-backed new competitors, intensity of price disruption and eroding margin in high-end specimen test in B-2-B segment. With guidance for margin dilution (by Rs70-80m) due to commissioning of Kolkata CPL and continued pressure from labs like Thyrocare Technologies challenging DLPL's B-2-B revenues through their benefit of lower operating cost structure with single central lab (CPL), we believe the premium valuation may not sustain. The stock trades at PER of 38x and 30x FY18E and FY19E and we downgrade our assigned PER to 35x (from 45x) of FY19E. We downgrade our recommendation to 'ACCUMULATE' and reduce TP to Rs963 (from Rs1,202).

Key financials (Y/e March)	2016	2017	2018E	2019E
Revenues (Rs m)	7,913	9,124	10,998	13,442
Growth (%)	20.0	15.3	20.5	22.2
EBITDA (Rs m)	2,097	2,365	2,805	3,387
PAT (Rs m)	1,322	1,542	1,830	2,274
EPS (Rs)	16.0	18.6	22.0	27.4
Growth (%)	(8.7)	16.1	18.7	24.2
Net DPS (Rs)	2.5	1.3	4.4	5.5

Profitability & Valuation

	2016	2017	2018E	2019E
EBITDA margin (%)	26.5	25.9	25.5	25.2
RoE (%)	32.2	26.4	25.3	26.0
RoCE (%)	29.7	25.4	24.3	25.1
EV / sales (x)	8.4	7.3	6.0	4.8
EV / EBITDA (x)	31.8	28.2	23.5	19.0
PE (x)	52.0	44.8	37.8	30.4
P / BV (x)	13.6	10.5	8.8	7.2
Net dividend yield (%)	0.3	0.2	0.5	0.7

Source: Company Data; PL Research

Exhibit 1: Q2FY18 Result Overview (Rs m)

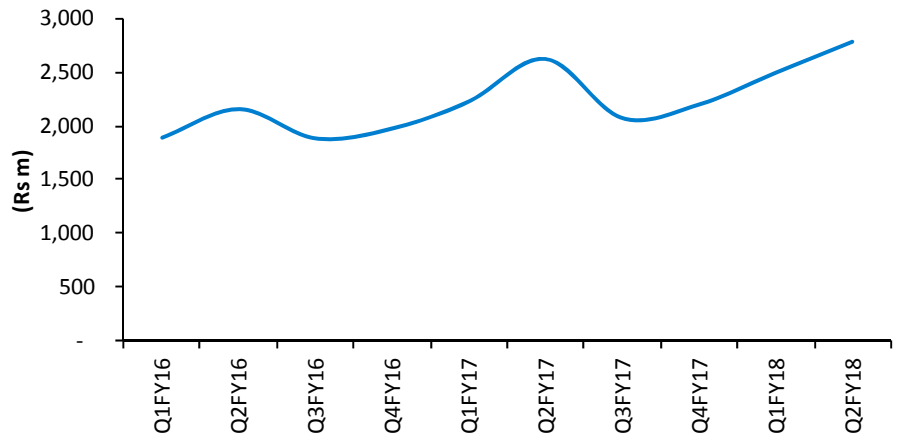
Y/e March	Q2FY18	Q2FY17	YoY gr. (%)	Q1FY18	H1FY18	H1FY17	YoY gr. (%)
Net Sales	2,781	2,622	6.1	2,493	5,274	4,850	8.7
Raw Material	594	596	(0.3)	521	1,115	1,080	3.3
<i>% of Net Sales</i>	<i>21.4</i>	<i>22.7</i>		<i>20.9</i>	<i>21.1</i>	<i>22.3</i>	
Personnel Cost	446	393	13.5	436	882	743	18.7
<i>% of Net Sales</i>	<i>16.0</i>	<i>15.0</i>		<i>17.5</i>	<i>16.7</i>	<i>15.3</i>	
Others	962	833	15.5	881	1,843	1,622	13.6
<i>% of Net Sales</i>	<i>34.6</i>	<i>31.8</i>		<i>35.3</i>	<i>34.9</i>	<i>33.4</i>	
Total Expenditure	2,002	1,822	9.9	1,838	3,840	3,445	11.5
EBITDA	779	800	(2.6)	655	1,434	1,406	2.0
<i>Margin (%)</i>	<i>28.0</i>	<i>30.5</i>		<i>26.3</i>	<i>27.2</i>	<i>29.0</i>	
Depreciation	75	65	15.4	69	144	128	12.5
EBIT	704	735	(4.2)	586	1,290	1,278	1.0
Other Income	77	69	11.6	75	152	133	14.3
Interest	3	1		1	4	2	
PBT	778	803	(3.1)	660	1,438	1,409	2.1
Extra-Ord. Inc./Exps.	-	-		-	-	-	
Total Taxes	269	273	(1.5)	216	485	478	1.5
<i>ETR (%)</i>	<i>34.6</i>	<i>34.0</i>		<i>32.7</i>	<i>33.7</i>	<i>33.9</i>	
Reported PAT	509	530	(4.0)	444	953	931	2.4
Minority Interest	3	3		3	6	6	
Reported PAT	506	527	(4.0)	441	947	925	2.4

Source: Company Data, PL Research

Conference call takeaways:

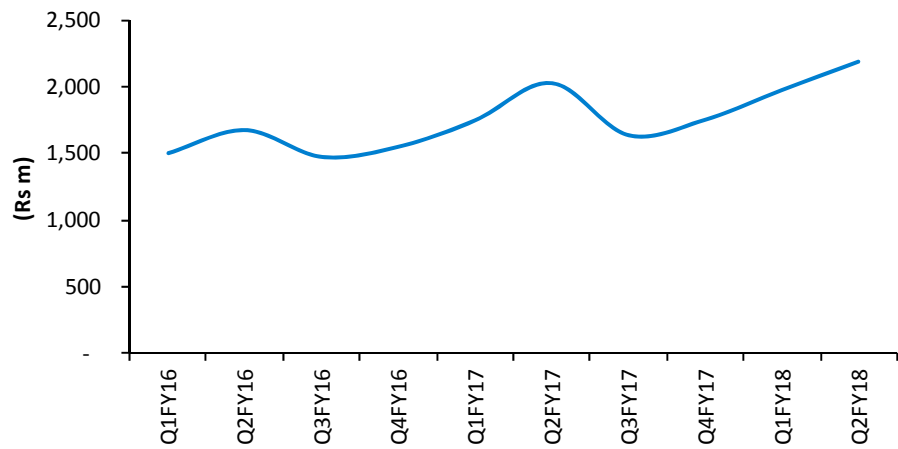
- Management guided for 14-15% volume growth in FY18E. Management expect to maintain EBITDA margins at 25-27% going forward and gross margin at the current levels, i.e. 79% of revenues. Revenue increased by 6.1% YoY in Q2FY18 on account of increase in volumes by 6.7%.
- Management guided that Kolkata Reference Lab (KRL) project is on schedule and expects it to be operational by Dec 2017. This will help DLPL to increase their presence in Eastern India, North-East India and Bangladesh. Management expects additional operating costs of Rs90-100m (constituting around 1% of sales) post commisioning of KRL. DLPL expects to achieve cash break-even in KRL in next 3-4 years of operations
- Management guided that DLPL faced pricing pressures in B-2-B segments in Q2FY18 due to aggressive pricing from the limited number of single-lab operators. DLPL guided for strong promotion for its new pckage in all its channel aimed at preventive care business and branded as 'Swasth'.
- DLPL had a gradual increase in number of patients tested from 3.7m in Q2FY17 to 4m in Q2FY18. Realisation per patient declined to Rs699 in Q2FY17 due to price rationalisation in certain geography of non-NCR region of DLPL's pathology business.
- Revenues from northern geography (specifically Delhi/NCR) witnessed strong growth of 13% YoY in Q2FY18
- The tests/patient decreased to 2.24 in Q2FY18 from 2.28 in Q2FY17 due to introducton of many package testing.
- DLPL guided for capex of Rs600m in FY18E, of which Rs250m is maintenance capex and Rs350m for setting up of KRL. Management guided for commencement of capex for Lucknow reference lab (Rs500-600m) gradually subject to learning from operations of new KRL center

Exhibit 2: Revenue - Diagnostics



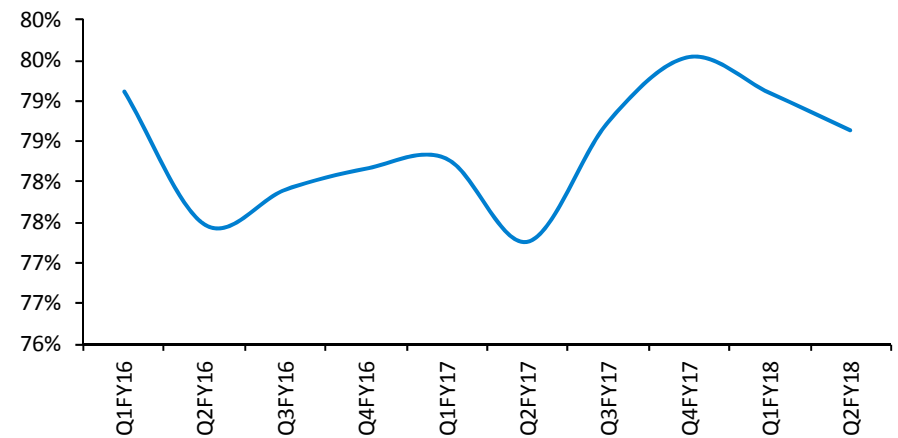
Source: Company Data, PL Research

Exhibit 3: Gross Profits



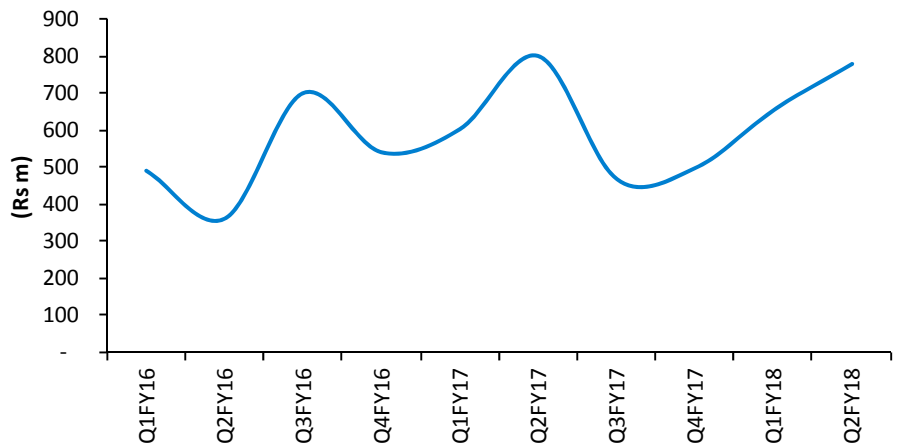
Source: Company Data, PL Research

Exhibit 4: Gross Profit Margin



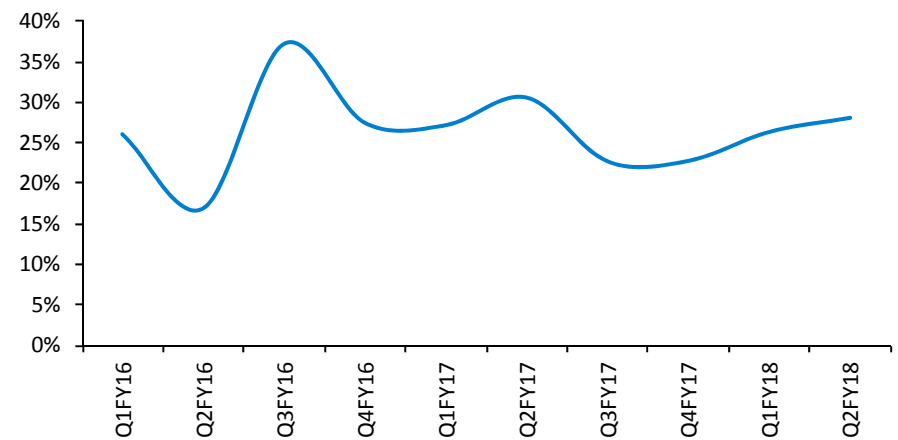
Source: Company Data, PL Research

Exhibit 5: EBITDA



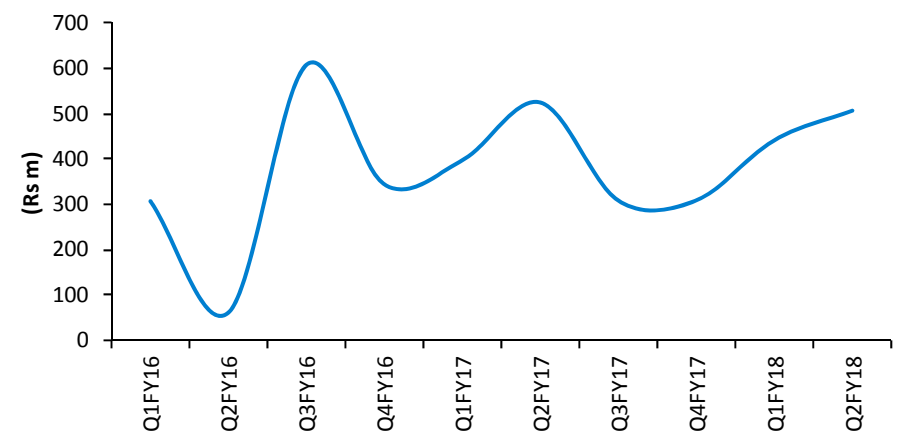
Source: Company Data, PL Research

Exhibit 6: EBITDA Margins



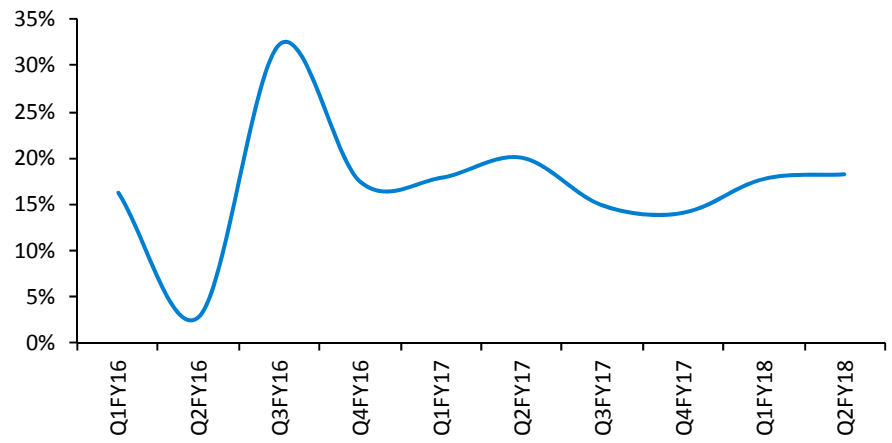
Source: Company Data, PL Research

Exhibit 7: PAT



Source: Company Data, PL Research

Exhibit 8: PAT Margins



Source: Company Data, PL Research

Income Statement (Rs m)

Y/e March	2016	2017	2018E	2019E
Net Revenue	7,913	9,124	10,998	13,442
Raw Material Expenses	1,729	1,971	2,376	2,904
Gross Profit	6,184	7,153	8,623	10,539
Employee Cost	1,368	1,634	2,018	2,446
Other Expenses	2,718	3,154	3,800	4,705
EBITDA	2,097	2,365	2,805	3,387
Depr. & Amortization	283	282	399	355
Net Interest	5	2	1	—
Other Income	198	251	264	282
Profit before Tax	2,007	2,333	2,669	3,315
Total Tax	675	781	827	1,028
Profit after Tax	1,332	1,552	1,842	2,287
Ex-Od items / Min. Int.	10	10	11	13
Adj. PAT	1,322	1,542	1,830	2,274
Avg. Shares O/S (m)	82.7	83.1	83.1	83.1
EPS (Rs.)	16.0	18.6	22.0	27.4

Cash Flow Abstract (Rs m)

Y/e March	2016	2017	2018E	2019E
C/F from Operations	1,469	1,716	1,720	2,286
C/F from Investing	(1,518)	(1,407)	(373)	(355)
C/F from Financing	4	(344)	(445)	(553)
Inc. / Dec. in Cash	(46)	(35)	901	1,379
Opening Cash	233	187	152	1,053
Closing Cash	187	152	1,053	2,432
FCFF	183	802	1,392	1,879
FCFE	183	802	1,392	1,879

Key Financial Metrics

Y/e March	2016	2017	2018E	2019E
Growth				
Revenue (%)	20.0	15.3	20.5	22.2
EBITDA (%)	34.5	12.8	18.6	20.8
PAT (%)	38.2	16.7	18.7	24.2
EPS (%)	(8.7)	16.1	18.7	24.2
Profitability				
EBITDA Margin (%)	26.5	25.9	25.5	25.2
PAT Margin (%)	16.7	16.9	16.6	16.9
RoCE (%)	29.7	25.4	24.3	25.1
RoE (%)	32.2	26.4	25.3	26.0
Balance Sheet				
Net Debt : Equity	(0.4)	(0.4)	(0.4)	(0.5)
Net Wrkng Cap. (days)	(42)	(47)	(40)	(41)
Valuation				
PER (x)	52.0	44.8	37.8	30.4
P / B (x)	13.6	10.5	8.8	7.2
EV / EBITDA (x)	31.8	28.2	23.5	19.0
EV / Sales (x)	8.4	7.3	6.0	4.8
Earnings Quality				
Eff. Tax Rate	33.6	33.5	31.0	31.0
Other Inc / PBT	9.9	10.8	9.9	8.5
Eff. Depr. Rate (%)	9.6	8.8	10.3	7.9
FCFE / PAT	13.9	52.0	76.1	82.6

Source: Company Data, PL Research.

Balance Sheet Abstract (Rs m)

Y/e March	2016	2017	2018E	2019E
Shareholder's Funds	5,074	6,598	7,871	9,592
Total Debt	2	3	3	3
Other Liabilities	148	145	223	307
Total Liabilities	5,224	6,745	8,097	9,901
Net Fixed Assets	1,281	1,502	1,754	2,069
Goodwill	417	578	578	578
Investments	643	1,046	1,099	1,154
Net Current Assets	3,329	4,369	5,458	6,937
<i>Cash & Equivalents</i>	<i>2,099</i>	<i>2,383</i>	<i>3,284</i>	<i>4,662</i>
<i>Other Current Assets</i>	<i>2,138</i>	<i>2,724</i>	<i>2,977</i>	<i>3,217</i>
<i>Current Liabilities</i>	<i>908</i>	<i>737</i>	<i>803</i>	<i>943</i>
Other Assets	197	297	307	318
Total Assets	5,224	6,745	8,097	9,901

Quarterly Financials (Rs m)

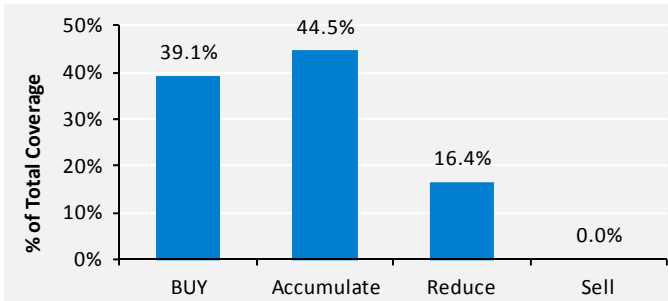
Y/e March	Q3FY17	Q4FY17	Q1FY18	Q2FY18
Net Revenue	2,074	2,199	2,493	2,781
EBITDA	469	499	655	779
<i>% of revenue</i>	<i>22.6</i>	<i>22.7</i>	<i>26.3</i>	<i>28.0</i>
Depr. & Amortization	71	78	69	75
Net Interest	1	2	1	3
Other Income	68	68	75	77
Profit before Tax	465	487	660	778
Total Tax	155	172	216	269
Profit after Tax	309	313	441	506
Adj. PAT	309	313	441	506

Source: Company Data, PL Research.

Prabhudas Lilladher Pvt. Ltd.

3rd Floor, Sadhana House, 570, P. B. Marg, Worli, Mumbai-400 018, India

Tel: (91 22) 6632 2222 Fax: (91 22) 6632 2209

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Accumulate	:	Outperformance to Sensex over 12-months
Reduce	:	Underperformance to Sensex over 12-months
Sell	:	Over 15% underperformance to Sensex over 12-months
Trading Buy	:	Over 10% absolute upside in 1-month
Trading Sell	:	Over 10% absolute decline in 1-month
Not Rated (NR)	:	No specific call on the stock
Under Review (UR)	:	Rating likely to change shortly

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