

Institutional Equity Research

# Cadila Healthcare

Pharmaceuticals | India

3QFY19 Result Update | February 07, 2019

|                        |        |
|------------------------|--------|
| CMP* (Rs)              | 323    |
| Upside/ (Downside) (%) | 23.7   |
| Bloomberg Ticker       | CDH IN |
| Market Cap. (Rs bn)    | 331    |
| Free Float (%)         | 25     |
| Shares O/S (mn)        | 1,024  |

**BUY** 

Target Price: Rs400

## New Launches to Aid US Biz; Maintain BUY

Cadila Healthcare (CDH) has reported strong sequential growth in 3QFY19, exceeding our estimates on all metrics. Revenue grew by 10% YoY and 21% QoQ to Rs35.8bn on account of 44% QoQ and 11% YoY growth in the US sales to US\$ 272mn along with 14% YoY growth in Emerging market and API business. While India business declined by 8% YoY and 5% QoQ to Rs8.5bn due to lingering effect of GST-related re-stocking and restructuring and reallocations of resources. Gross margin declined by 336bps YoY and 430bps QoQ to 62.2% due to low-margin authorised generic (gAndroGel) launch in the US, weak India business and forex loss. Consequently, EBITDA margin fell by 249bps YoY (flat on QoQ basis) to 23.5% (vs. our estimate of 22.2%). EBITDA grew by 22% QoQ to Rs8.4bn led higher US sales. Its R&D expenses stood at 7.5% of sales vs. 9.5% in 2QFY19 and 6.5% in 3QFY19. PAT grew by 22% QoQ to Rs5.1bn due to strong QoQ sales and operating performance. CDH reported forex gain of Rs305mn during the quarter, which included in sales and raw material cost. Its US sales stood at US\$644mn in 9MFY19 and we expect the Company can achieve its target of ~US\$900mn in FY19E (vs. US\$905mn in FY18) driven by large number of new launches.

### Key Results Highlights

**US Biz (55% of Sales):** Sequential growth of 44% on CC terms primarily due to launch of authorised generic gAndroGel (1/3rd US sales impact) and ramp-up in recent launches (gToprol XL, Methylprednisolone), market share gain in own gAsacol HD, and better seasonality (gTamiflu). Price erosion in base business stood at 0.3% QoQ. CDH expects 1 trans-dermal product approval by FY19E-end, while 2-3 approvals expected in FY20E. It launched 15 new products (37 in 9MFY19), while filed 8 and received 23 approvals.

**India Biz (24% of Sales):** Decline in the domestic business due to high base (GST re-stocking) in 3QFY18 and rationalisation of product portfolio, restructuring of field force/therapies and re-allocation of resources (territories). The Management sees these initiatives will have some adverse impact on domestic sales in 4QFY19 too while expecting recovery from 1QFY20E onwards. Also, it indicated that these initiatives will have long-term positive impact on the business (already seen 5% improvement in 20% of territories in Jan'19; pan-India implementation soon). The Management expects to maintain its focus on key therapeutic segments i.e. Gynaecology, Respiratory, Pain Management, CVS and GI while focussing on super specialty therapies i.e. Oncology, Vaccines, Nephrology and Haematology going ahead.

**China Filings:** CDH has filed some API products, while evaluating formulation business. The Management maintained that no major resources allocated for China business.

**Other highlights** 1) CDH investment of Rs11.75bn in Heinz India acquisition (stake declined from 72% to 64%); (2) Capex of Rs8-10bn/annum; (3) looking inorganic opportunity in branded specialty side in the US (small size); (4) Other expenses increased in 3QFY19 due to disruption cost in the US, plant maintenance and advertisement cost.

### Outlook & Valuation

We believe that CDH's long-term fundamentals continue to remain intact on the back of rich pending product pipeline (including high-value products in the US). Looking ahead, we expect ramp-up in CDH's US business led by new product launches (including transdermal products). We are trimming down our earning estimates by 11% for FY20E to factor in lower India sales. **We maintain our BUY recommendation on the stock with a revised Target Price of Rs400 (from Rs450 earlier).**

| Quarterly Performance (Consolidated, Rs mn) |        |        |         |        |        |
|---|--------|--------|---------|--------|--------|
| (Rs mn)                                     | 3QFY19 | 3QFY18 | YoY, %  | 2QFY19 | QoQ, % |
| Revenue                                     | 35,779 | 32,475 | 10.2    | 29,612 | 20.8   |
| Operating Expenses                          | 27,380 | 24,042 | 13.9    | 22,734 | 20.4   |
| EBITDA                                      | 8,399  | 8,433  | -0.4    | 6,878  | 22.1   |
| EBITDA Margin (%)                           | 23.5   | 26.0   | -249bps | 23.2   | 25bps  |
| EBIT  | 7,172  | 7,374  | -2.7    | 5,707  | 25.7   |
| PBT   | 6,717  | 7,240  | -7.2    | 5,350  | 25.6   |
| Adj. PAT                                    | 5,107  | 5,458  | -6.4    | 4,175  | 22.3   |
| Adj EPS (Rs)                                | 5.0    | 5.3    | -6.0    | 4.1    | 22.3   |

Source: Company, RSec Research

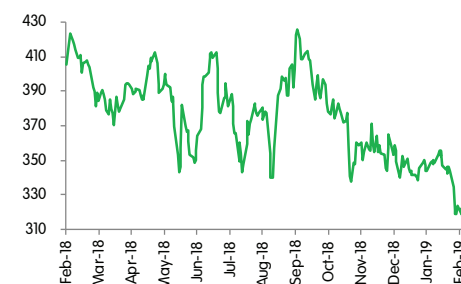
| Share price (%)      | 1 mth | 3 mth | 12 mth |
|----------------------|-------|-------|--------|
| Absolute performance | (7.6) | (9.3) | (18.8) |
| Relative to Nifty    | (4.8) | (4.9) | (13.1) |

| Shareholding Pattern (%) | Dec-18 | Sep-18 |
|--------------------------|--------|--------|
| Promoter                 | 74.8   | 74.8   |
| Public                   | 25.2   | 25.2   |

| Key Financials |         |         |         |
|----------------|---------|---------|---------|
| (Rs mn)        | FY19E   | FY20E   | FY21E   |
| Sales          | 125,803 | 139,197 | 148,363 |
| EBITDA         | 29,467  | 32,842  | 33,342  |
| Adj. PAT       | 16,977  | 20,467  | 22,650  |
| EPS (Rs)       | 16.6    | 20.0    | 22.1    |
| P/E (x)        | 19.5    | 16.2    | 14.6    |
| EV/Sales (x)   | 2.9     | 2.5     | 2.3     |
| EV/EBITDA (x)  | 12.4    | 10.8    | 10.2    |
| ROE (%)        | 16.9    | 17.6    | 17.0    |
| ROCE (%)       | 13.8    | 15.1    | 14.5    |

| Change of Estimates |        |        |
|---------------------|--------|--------|
| (% change)          | FY19E  | FY20E  |
| Revenue             | (3.0)  | (6.3)  |
| EBITDA              | (1.3)  | (8.1)  |
| PAT                 | (10.1) | (11.1) |

### 1 Year Stock Price Performance



Note: \* CMP as on February 07, 2019

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**BUY** 

Target Price: Rs400

## Risks to the View

- ▶ Delayed recovery in domestic business.
- ▶ Lower-than-expected growth in US revenue.

## Exhibit 1: Segment-wise sales performance

| (Rs mn)           | 3QFY19 | 3QFY18 | YoY, % | 2QFY19 | QoQ, % |
|-------------------|--------|--------|--------|--------|--------|
| India             | 8,457  | 9,168  | (7.8)  | 8,932  | (5.3)  |
| US                | 19,341 | 15,838 | 22.1   | 13,204 | 46.5   |
| Europe            | 595    | 649    | (8.3)  | 520    | 14.4   |
| JV                | 525    | 530    | (0.9)  | 167    | 214.4  |
| Emerging Market   | 2,243  | 1,964  | 14.2   | 2,034  | 10.3   |
| API               | 1300   | 1137   | 14.3   | 890    | 46.1   |
| Consumer & others | 2700   | 2513   | 7.4    | 2694   | 0.2    |
| Total             | 35,161 | 31,799 | 10.6   | 28,441 | 23.6   |
| US (USD mn)       | 272    | 245    | 11.2   | 188    | 44.4   |

Source: Company, RSec Research

## Exhibit 2: Quarterly Performance

| (Rs mn)                  | 3QFY19        | 3QFY18        | YoY, %       | 2QFY19        | QoQ, %      |
|--------------------------|---------------|---------------|--------------|---------------|-------------|
| <b>Net Sales</b>         | <b>35,779</b> | <b>32,475</b> | <b>10.2</b>  | <b>29,612</b> | <b>20.8</b> |
| Cost of Revenues         | 13,522        | 11,183        | 20.9         | 9,919         | 36.3        |
| Gross Profit             | 22,257        | 21,292        | 4.5          | 19,693        | 13.0        |
| % of net sales           | 62.2          | 65.6          | (336) bps    | 66.5          | (430) bps   |
| Employee expenses        | 5,240         | 4,655         | 12.6         | 5,212         | 0.5         |
| Other Expenses           | 8,618         | 8,204         | 5.0          | 7,603         | 13.3        |
| Total operating expenses | 27,380        | 24,042        | 13.9         | 22,734        | 20.4        |
| <b>EBITDA</b>            | <b>8,399</b>  | <b>8,433</b>  | <b>(0.4)</b> | <b>6,878</b>  | <b>22.1</b> |
| EBITDA margin (%)        | 23.5          | 26.0          | (249) bps    | 23.2          | 25 bps      |
| Depreciation             | 1,537         | 1,469         | 4.6          | 1,475         | 4.2         |
| <b>EBIT</b>              | <b>7,172</b>  | <b>7,374</b>  | <b>(2.7)</b> | <b>5,707</b>  | <b>25.7</b> |
| Other Income             | 310           | 410           | (24.4)       | 304           | 2.0         |
| Interest                 | 455           | 134           | 239.6        | 357           | 27.5        |
| <b>PBT</b>               | <b>6,717</b>  | <b>7,240</b>  | <b>(7.2)</b> | <b>5,350</b>  | <b>25.6</b> |
| Total tax                | 1,586         | 1,786         | (11.2)       | 1,247         | 27.2        |
| Tax Rate (%)             | 23.6          | 24.7          | (106) bps    | 23.3          | 30 bps      |
| Minority Interest        | 24            | (4)           | (700.0)      | (72)          | (133.3)     |
| <b>Adj PAT</b>           | <b>5,107</b>  | <b>5,458</b>  | <b>(6.4)</b> | <b>4,175</b>  | <b>22.3</b> |
| Adj. PAT margin (%)      | 14.3          | 16.8          | (253) bps    | 14.1          | 17 bps      |
| Extraordinary items      | 0             | (25)          |              | 0             |             |
| <b>Reported PAT</b>      | <b>5,107</b>  | <b>5,433</b>  | <b>(6.0)</b> | <b>4,175</b>  | <b>22.3</b> |
| <b>Adj. EPS (Rs)</b>     | <b>5.0</b>    | <b>5.3</b>    | <b>(6.0)</b> | <b>4.1</b>    | <b>22.3</b> |

Source: Company, RSec Research

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**Cadila Healthcare**

Pharmaceuticals | India

|                        |        |
|------------------------|--------|
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**BUY** 

Target Price: Rs400

**Profit & Loss Statement**

| Y/E March (Rs mn)           | FY18           | FY19E          | FY20E          | FY21E          |
|-----------------------------|----------------|----------------|----------------|----------------|
| <b>Net Sales</b>            | <b>119,049</b> | <b>125,803</b> | <b>139,197</b> | <b>148,363</b> |
| Total Expenditure           | 90,574         | 96,336         | 106,354        | 115,021        |
| Raw Material                | 41,220         | 43,402         | 48,719         | 51,927         |
| Staff cost                  | 18,545         | 21,141         | 23,890         | 27,115         |
| Other expenses              | 22,175         | 22,632         | 23,663         | 25,222         |
| R&D expense                 | 8,634          | 9,161          | 10,082         | 10,758         |
| <b>EBITDA</b>               | <b>28,475</b>  | <b>29,467</b>  | <b>32,842</b>  | <b>33,342</b>  |
| Margin                      | 23.9           | 23.4           | 23.6           | 22.5           |
| Depreciation & Amortisation | 5,388          | 5,855          | 6,284          | 6,713          |
| Other Income                | 1,132          | 1,930          | 2,135          | 2,276          |
| <b>EBIT</b>                 | <b>24,219</b>  | <b>23,612</b>  | <b>26,559</b>  | <b>26,629</b>  |
| Interest                    | 911            | 2,102          | 1,802          | 1,502          |
| <b>PBT</b>                  | <b>23,308</b>  | <b>21,510</b>  | <b>24,757</b>  | <b>27,403</b>  |
| Tax                         | 5,644          | 5,162          | 4,951          | 5,481          |
| Tax rate                    | 24.2           | 24.0           | 20.0           | 20.0           |
| Minority Interest           | (628)          | (630)          | (662)          | (728)          |
| <b>Adj. PAT</b>             | <b>18,292</b>  | <b>16,977</b>  | <b>20,467</b>  | <b>22,650</b>  |
| % chg                       | 31.5           | (7.2)          | 20.6           | 10.7           |
| Extraordinary item          | 188            | -              | -              | -              |
| <b>Reported PAT</b>         | <b>18,104</b>  | <b>16,977</b>  | <b>20,467</b>  | <b>22,650</b>  |
| <b>Adj. EPS (Rs)</b>        | <b>17.9</b>    | <b>16.6</b>    | <b>20.0</b>    | <b>22.1</b>    |

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Target Price: Rs400

## Balance Sheet

| Y/E March (Rs mn)           | FY18           | FY19E          | FY20E          | FY21E          |
|-----------------------------|----------------|----------------|----------------|----------------|
| <b>SOURCES OF FUNDS</b>     |                |                |                |                |
| Equity Share Capital        | 1,024          | 1,024          | 1,024          | 1,024          |
| Reserves & Surplus          | 86,421         | 99,396         | 115,037        | 132,348        |
| Shareholders Funds          | 87,445         | 100,420        | 116,061        | 133,372        |
| Minority Interest           | 1,910          | 2,540          | 3,202          | 3,929          |
| Deferred tax liability      | (6,425)        | (6,425)        | (6,425)        | (6,425)        |
| Total Loans                 | 54,067         | 70,067         | 60,067         | 50,067         |
| <b>Total Liabilities</b>    | <b>136,997</b> | <b>166,602</b> | <b>172,905</b> | <b>180,943</b> |
| <b>APPLICATION OF FUNDS</b> |                |                |                |                |
| Gross Block                 | 79,390         | 87,390         | 93,790         | 100,190        |
| Less: Acc. Depreciation     | 28,415         | 34,270         | 40,554         | 47,267         |
| Net Block                   | 50,975         | 53,120         | 53,236         | 52,923         |
| Capital Work-in-Progress    | 15,272         | 17,272         | 18,872         | 20,472         |
| Goodwill on consolidation   | 13,853         | 13,853         | 13,853         | 13,853         |
| Investments                 | 7,457          | 7,567          | 7,689          | 7,822          |
| Current Assets              | 79,549         | 106,421        | 114,284        | 123,030        |
| Inventories                 | 23,853         | 25,206         | 27,890         | 29,726         |
| Debtors                     | 32,063         | 33,882         | 37,489         | 39,958         |
| Cash & Bank                 | 13,149         | 36,253         | 36,647         | 40,281         |
| Other current assets        | 10,484         | 11,079         | 12,253         | 13,060         |
| Current liabilities         | 34,405         | 36,362         | 40,234         | 42,883         |
| Current liabilities         | 31,849         | 33,656         | 37,239         | 39,691         |
| Provisions                  | 2,561          | 2,706          | 2,994          | 3,192          |
| Other non-current assets    | 4,301          | 4,731          | 5,209          | 5,730          |
| <b>Total Assets</b>         | <b>136,997</b> | <b>166,602</b> | <b>172,905</b> | <b>180,943</b> |

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Target Price: Rs400

## Cash Flow Statement

| Y/E March (Rs mn)                        | FY18           | FY19E           | FY20E           | FY21E           |
|--|----------------|-----------------|-----------------|-----------------|
| Profit before tax                        | 23,120         | 21,510          | 24,757          | 27,403          |
| Depreciation                             | 5,405          | 5,855           | 6,284           | 6,713           |
| Interest provided                        | 1,468          | 2,102           | 1,802           | 1,502           |
| Change in Working Capital                | (13,964)       | (1,615)         | (3,411)         | (2,256)         |
| Tax Paid                                 | (6,206)        | (5,162)         | (4,951)         | (5,481)         |
| Others                                   | 334            | -               | -               | -               |
| <b>Cash Flow from Operations</b>         | <b>9,193</b>   | <b>22,689</b>   | <b>24,481</b>   | <b>27,881</b>   |
| (Inc.)/ Dec. in Fixed Assets             | (10,493)       | (10,000)        | (8,000)         | (8,000)         |
| Others                                   | 756            | (110)           | (121)           | (134)           |
| <b>Cash Flow from Investing</b>          | <b>(9,737)</b> | <b>(10,110)</b> | <b>(8,121)</b>  | <b>(8,134)</b>  |
| Issue of Equity                          | -              | -               | -               | -               |
| Inc./(Dec.) in loans                     | 1,575          | 16,000          | (10,000)        | (10,000)        |
| Dividend Paid (Incl. Tax)                | (10)           | (4,003)         | (4,825)         | (5,340)         |
| Interest provided                        | (1,049)        | (2,102)         | (1,802)         | (1,502)         |
| Others                                   | (1)            | 630             | 662             | 728             |
| <b>Cash Flow from Financing</b>          | <b>515</b>     | <b>10,525</b>   | <b>(15,966)</b> | <b>(16,114)</b> |
| Inc./(Dec.) in cash and cash equivalents | (29)           | 23,104          | 393             | 3,634           |
| Opening cash & cash equivalents balan.   | 15,435         | 13,149          | 36,253          | 36,647          |
| Closing cash & cash equivalents balances | 15,406         | 36,253          | 36,647          | 40,281          |
| Investment in Liquid MF                  | (2,257)        | -               | -               | -               |
| <b>Cash and cash equivalents</b>         | <b>13,149</b>  | <b>36,253</b>   | <b>36,647</b>   | <b>40,281</b>   |

## Key Ratios

| Y/E March                    | FY18 | FY19E | FY20E | FY21E |
|------------------------------|------|-------|-------|-------|
| <b>Valuation Ratio (x)</b>   |      |       |       |       |
| P/E                          | 18.1 | 19.5  | 16.2  | 14.6  |
| P/CEPS                       | 14.0 | 14.5  | 12.4  | 11.3  |
| P/BV                         | 3.8  | 3.3   | 2.9   | 2.5   |
| Dividend yield (%)           | 1.3  | 1.2   | 1.5   | 1.6   |
| EV/Sales                     | 3.1  | 2.9   | 2.5   | 2.3   |
| EV/EBITDA                    | 13.1 | 12.4  | 10.8  | 10.2  |
| <b>Per Share Data (Rs)</b>   |      |       |       |       |
| EPS                          | 17.9 | 16.6  | 20.0  | 22.1  |
| Cash EPS                     | 23.1 | 22.3  | 26.1  | 28.7  |
| DPS                          | 4.2  | 3.9   | 4.7   | 5.2   |
| Book Value (BV)              | 85.4 | 98.1  | 113.4 | 130.3 |
| <b>Returns (%)</b>           |      |       |       |       |
| RoCE                         | 17.1 | 13.8  | 15.1  | 14.5  |
| RoE                          | 20.9 | 16.9  | 17.6  | 17.0  |
| <b>Turnover ratios (x)</b>   |      |       |       |       |
| Asset Turnover (Gross Block) | 1.5  | 1.4   | 1.5   | 1.5   |
| Asset Turnover (Net Block)   | 2.3  | 2.4   | 2.6   | 2.8   |
| Inventory (days)             | 73   | 73    | 73    | 73    |
| Receivables (days)           | 98   | 98    | 98    | 98    |
| Payables (days)              | 98   | 98    | 98    | 98    |

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**BUY** 

Target Price: Rs400

## Rating History

| Date      | Reco | CMP | TP  |
|-----------|------|-----|-----|
| 05-Nov-18 | BUY  | 359 | 450 |
| 16-Aug-18 | BUY  | 343 | 450 |
| 28-May-18 | BUY  | 371 | 490 |
| 12-Feb-18 | BUY  | 418 | 540 |
| 16-Nov-17 | BUY  | 442 | 554 |
| 14-Aug-17 | BUY  | 486 | 554 |
| 30-May-17 | BUY  | 451 | 527 |
| 31-Jan-17 | BUY  | 352 | 422 |

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## Rating Guides

| Rating | Expected absolute returns (%) over 12 months |
|--------|--|
| BUY    | >10%   |
| HOLD   | -5% to 10%                                   |
| REDUCE | >-5%   |

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