Investor's Eye

August 03, 2017

Index

Stock Update

To regain momentum with double-digit volume growth ahead

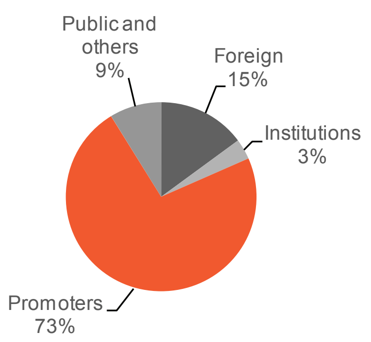
Emami

Reco: Buy | CMP: Rs1,137

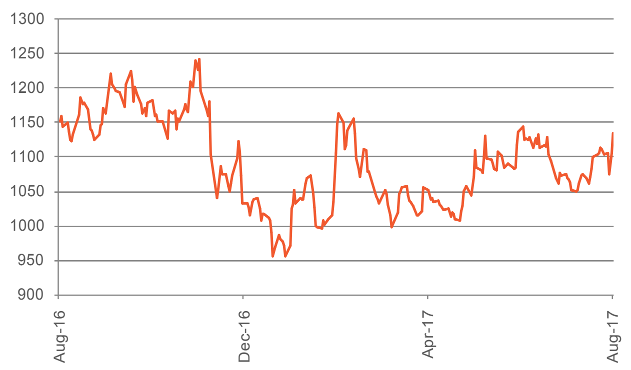
Company details

Price target:	Rs1,245
Market cap:	Rs25,806 cr
52-week high/low:	Rs1260/935
NSE volume: (No of shares)	1.7 lakh
BSE code:	531162
NSE code:	EMAMILTD
Sharekhan code:	EMAMILTD
Free float: (No of shares)	6.2 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	3.2	6.4	-3.1	-2.8
Relative to Sensex	-2.0	-2.7	-16.6	-17.4

Key points

- **Q1 performance affected by down-stocking in domestic market and inventory correction in international market:** In Q1FY2018, Emami's revenue declined by 16.1% YoY to Rs.541.1 crore, significantly impacted by down-stocking in domestic business and a 19% decline in the international business revenue (due to inventory correction in key markets). Domestic business volumes declined by 18% during the quarter. With higher input prices, gross margin decreased by 91BPS YoY to 63.6%. The company did higher promotional spends behind new launches, resulting in a 300BPS increase in advertisement and promotional spends to 26.4% in Q1FY2018. This, along with lower operating leverage, resulted in a 45.5% decline in operating profit and a 53.7% decline in adjusted PAT in Q1FY2018.

- **Key brands witnessed sales decline; *Boroplus Cream* and *7-in-one* oils registered double-digit growth:** Emami's Balm range, *Navratna cooling oil*, *Kesh King* range of products, *Fair & Handsome* and Zandu Healthcare range of products witnessed decline of 21%, 15%, 28%, 21% and 23%, respectively, as wholesale trade channels and canteen stores department (CSD) stood out of business in June 2017. *Boroplus Cream* and *7-in-one oil* registered growth of 41% and 16%, respectively, mainly on account of good demand and lesser dependence on wholesale channels. Revenue of the international business declined by 19%, affected by slowdown in Middle East market and reduction in stock levels in key markets.

- **Outlook – Domestic volume growth likely to get back to double digits; International business to grow:** Management is confident of re-gaining the double-digit growth momentum with wholesale trade channels (50% of Emami sales) back in business in some of the key markets. The company's management is expecting revenue growth of 18-19% (volume growth of 14-15%) for the remaining period of the current fiscal. Also, the second half of the year will be boosted by increased rural demand on account of better monsoons. The company expects to maintain OPM of 28-29% for FY2018. In the long run, the increase in direct distribution (targeting to reach 8 lakh outlets by the end of FY2018) and sustenance of new product additions will drive performance. Further, performance of the international business is expected to pick up post the required pipeline correction.

- **Growth levers in place; Retain Buy:** We have revised downwards our earnings estimates for FY2018 and FY2019 by 11% and 6%, respectively, to factor in lower sales and margins in Q1FY2018. Going ahead, the sustenance of new product additions in key categories, lower dependence on wholesale channels and enhancing direct distribution reach would help Emami to achieve better earnings growth in the medium to long run. Further, the stock is trading at discounted valuations of 32x its FY2019E earnings, which provides limited downside risk. Hence, we maintain our Buy rating on the stock with an unchanged price target of Rs.1,245.

Valuation (Consolidated) Rs cr

Particulars	FY16	FY17	FY18E	FY19E
Net Sales	2397.6	2532.6	2728.4	3269.5
Operating Profit	687.3	759.1	783.9	978.3
Adjusted PAT	533.7	549.8	611.9	803.4
EPS (Rs.)	23.5	24.2	27.0	35.4
OPM (%)	28.7	30.0	28.7	29.9
PE(X)	48.4	46.9	42.2	32.1
EV/EBIDTA (X)	38.4	34.5	32.7	25.8
RoE(%)	37.5	32.6	33.0	37.5
RoCE(%)	38.2	31.9	35.2	43.9

Result (Consolidated) Rs cr

Particulars	Q1FY18	Q1FY17	YoY%	Q4FY17	QoQ%
Total revenues	541.1	645.2	-16.1	577.7	-6.3
Total expenditure	460.9	498.2	-7.5	399.6	15.3
Operating profit	80.2	147.1	-45.5	178.1	-55.0
Other income	6.5	5.1	27.6	9.2	-29.4
interest expenses	7.9	12.5	-36.6	16.8	-52.8
depreciation	15.3	10.6	43.9	14.0	8.7
Profit before tax	63.5	129.0	-50.8	156.5	-59.4
Tax	14.7	23.9	-38.3	23.3	-36.7
Adjusted PAT	48.7	105.1	-53.7	133.2	-63.4
extra-ordinary gain / loss	-47.8	-48.7	-	-49.9	
Reported PAT	0.9	56.4	-98.4	83.3	-98.9
Adjusted EPS (Rs)	2.1	4.6	-53.7	5.9	-63.4
Gross margins (%)	63.6	64.6	-91BPS	62.2	144BPS
OPM (%)	14.8	22.8	-797BPS	30.8	-

Other key highlights

- **Distribution shift to direct retail from wholesale:** In line with its strategy of reducing dependency on the wholesale channel, Emami has increased its direct retail reach by 23,000 outlets in Q1FY2018 and reached a total of 7.5 lakh direct retail outlets by Q1FY2018-end. The company wants to reach about 8 lakh direct retail outlets by FY2018-end from the current level of 7.5 lakh outlets. By doing so, Emami wants to reduce business generated from the wholesale channel from 50% currently to 40% by FY2018.

- **New product launches continue:** Emami had launched HE *On* the *Go* (India's first waterless face wash), *Zandu Spray, Zandu Gel* and *Zandu Roll* at the end of FY2017. All these products are performing well and have seen good consumer traction. Also, during Q1FY2018, the company launched few SKUs in its *Navratna* range of products (cool oil and cool talc) and introduced a new variant in the cool talc segment named as *i-COOL Dynamite*. Going ahead, management aims that these new products (in the coming quarters also there can be some new product launches) would add 2-3% to the company's overall FY2018 consolidated revenue.

- **International business declined by 19%, but likely to see recovery in the coming quarters:** Slowdown and political instability in Middle East countries impacted the overall performance of the international business. During Q1FY2018, Emami had undertaken reduction of stock levels across key markets (about Rs.18crore-19crore of inventory correction) to bridge the gap between the actual demand and inventory hold on by trade channels. With fixing of pipeline, management expects the international business to gain traction and grow in double digits in the coming quarters.

Stock Update

Sunshine ahead: Performance to improve in H2FY2018

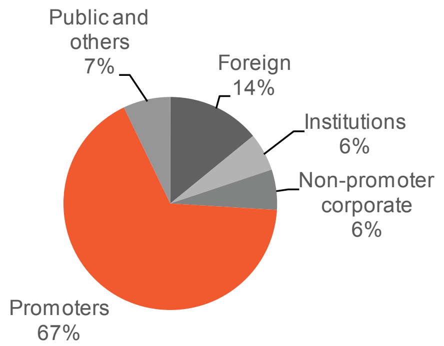
Jyothy Laboratories

Reco: Buy | CMP: Rs390

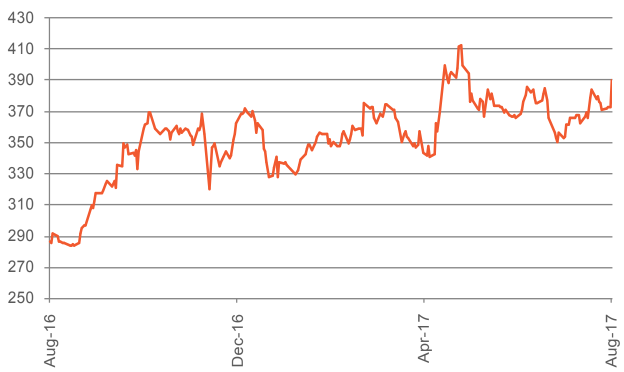
Company details

Price target:	Rs435
Market cap:	Rs7,086 cr
52-week high/low:	Rs427/281
NSE volume: (No of shares)	1.5 lakh
BSE code:	532926
NSE code:	JYOTHYLAB
Sharekhan code:	JYOTHYLAB
Free float: (No of shares)	6.0 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	7.2	-2.8	9.5	33.9
Relative to Sensex	1.7	-11.1	-5.7	13.9

Key points

- **Q1FY2018 performance marred by GST led de-stocking:** Like other FMCG companies, Jyothy Laboratories Ltd (JLL) performance for Q1FY2018 was marred by GST led de-stocking undertaken by various trade channels in the month of June 2017. The consolidated revenues declined by 14.8% to Rs385.8 crore with its key categories such as Fabric Whitener, Dishwash and household insecticide witnessing a dip of 15-20% in sales. The overall sales volume declined by 17% during the quarter. The gross margins improved by 261BPS yoy to 50.3% mainly on account of price hikes undertaken in FY2017. Higher advertisement spend and other fixed costs led to a 694BPS decline in OPM to 10.9% in Q1FY2018. The operating profit and the PAT was down by 47.9%yoy and 47.7%yoy respectively during the quarter.

- **Outlook – 10-12 % revenue growth for the rest of the fiscal and OPM likely to be maintained in the range of 15-16%:** JLL's management has indicated that with South India and west India recovering , about sixty percent of the business has attained normalcy. Billing with the canteen store department has resumed and modern trade is also back in trade post the negotiation on trade margin front. It expects revenues to grow in high single in Q2FY2018 and expect it to improve to 10-12% in H2FY2018. The gross margins at consolidated levels are expected to sustain at about 50% and the OPM will be maintained in the range of 15-16%.

- **Regional benefits to mark early recovery; Retain Buy:** We have reduced our earnings estimates for FY2018 and FY2019 by 6% and 2% to factor in the below par performance in Q1FY2018. JLL has a strong portfolio of brands, which can be key revenue drivers in a normal business environment. Further, the company will be one of the key beneficiaries of improvement in demand in the rural India . The stock is currently trading at discounted valuation 28.3x its FY2019E earnings to some of the large FMCG stocks. Thus in view of future growth prospects and decent valuations, we maintain our Buy recommendation on the stock with the unchanged price target of Rs435.

Valuation (Consolidated) Rs cr

Particulars	FY16	FY17	FY18E	FY19E
Net sales	1659.5	1749.1	1873.2	2216.3
Operating profit	222.1	254.4	278.6	335.1
Adjusted PAT	73.8	204.1	260.1	250.0
EPS (Rs.)	4.3	11.3	14.3	13.8
OPM (%)	13.4	14.5	14.9	15.1
PE (x)	91.5	34.5	27.2	28.3
EV/EBIDTA (x)	34.1	29.5	26.5	21.3
RoE (%)	8.8	20.5	22.0	18.4
RoCE (%)	14.8	16.5	17.3	21.2

Result (Consolidated) Rs cr

Particulars	Q1FY18	Q1FY17	YoY%	Q4FY17	QoQ%
Total Revenues	385.8	452.9	-14.8	446.2	-13.5
Total expenditure	343.7	372.0	-7.6	385.6	-10.9
Operating profit	42.2	80.9	-47.9	60.6	-30.5
Other income	2.1	2.9	-26.3	2.1	0.0
Depreciation	7.8	7.1	9.9	8.3	-6.5
Interest cost	10.1	15.7	-36.0	9.9	1.6
PBT	26.5	61.0	-56.7	44.6	-40.6
Tax	2.2	14.6	-85.2	-62.9	-103.5
Reported PAT	24.3	47.4	-48.7	107.4	-77.4
EPS (Rs.)	1.3	2.6	-47.7	5.9	-77.4
Gross margins (%)	50.3	47.7	261BPS	43.9	-
OPM(%)	10.9	17.9	(694) BPS	13.6	(266) BPS

Other key highlights

- **Issue with Kerala wholesalers association resolved; business to get back to normalcy:** Kerala is amongst the top markets for Jyothy (contributing 17% of general trade business). The All Kerala Distributors Association (AKDA) claimed an increase in their cost of business after the implementation of GST for demanding a higher margin. AKDA issued a diktat to all members in the first week of June to stop purchase. These distributors under their association unilaterally decided on up-charging — increasing their selling price to retailers — as a condition to resume billing. The distributors were demanding an increase in margins, which would be ultimately detrimental to consumers. This issue resulted in sales loss of Rs40 crore to Jyothy during Q1FY2018, but is now getting back to normalcy.

- **Most of the categories/brands in portfolio saw double digit dip:**

  - The fabric care category de-grew by 15.1% to Rs. 175.8 crore. All the products under this category declined due to the de-stocking effect. Ujala Fabric Whitener, having pan India presence was down by 12.6% YoY, Ujala Fabric Stiffener which is available only in Kerala and Tamil Nadu was down by 45.2% YoY and Ujala Detergent which is available only in Kerala was down by 34.4% YoY.

  - In the premium laundry segment, the Henko franchisee de-grew by 5.7% to Rs. 46.2 crore. The contribution from Modern Trade is higher in this product and hence the decline in sales was lesser than the other categories.

  - The dish wash category recorded de-growth of 14.2% YoY to Rs. 115 crore. The Exo franchisee was down by 16.8% to Rs. 84.2 crore while Pril was down by 5.7% YoY at Rs. 31.2 crore (as the brand is largely a modern trade/retail brand).

  - The home insecticide category de grew by 19.2% YoY to Rs. 30.1 crore in Q1FY2018. The performance of Maxo is expected to revive due to favourable season in north and east during August/September prior to the onset of winter

  - The personal care category de-grew by 18.8% YoY to Rs. 45.3 crore.

Segment-wise - revenue growth Rs cr

Particulars	Q1FY18	Q1FY17	YoY%	Q4FY17	QoQ%
Fabric care	175.8	207.0	-15.1	182.0	-3.4
Dish washing	115.0	134.1	-14.2	120.9	-4.9
Mosquito Repellant	30.1	37.3	-19.2	111.1	-72.9
Personal care	45.3	55.8	-18.8	33.2	36.3
Other Products	8.8	8.1	8.6	7.2	22.4
Total Consumer	375.0	442.3	-15.2	454.4	-17.5
Laundry Services	10.2	11.1	-8.4	11.3	-10.1
Total Revenues	385.0	452.6	-14.9	465.7	-17.3

Product-wise revenue growth Rs cr

Particulars	Q1FY18	Q1FY17	YoY %
Ujala	93.2	118.2	-21.2
Exo	84.2	101.2	-16.8
Maxo	30.1	37.3	-19.3
Henko	46.2	49.0	-5.7
Margo	40.4	49.7	-18.7
Pril	31.2	33.1	-5.7
Other	49.5	53.0	-6.6
Laundry	10.2	11.1	-8.1
Total Revenues	385.0	452.6	-14.9

Stock Update

Regional challenges with higher operational expenses affect profitability in Q1FY18

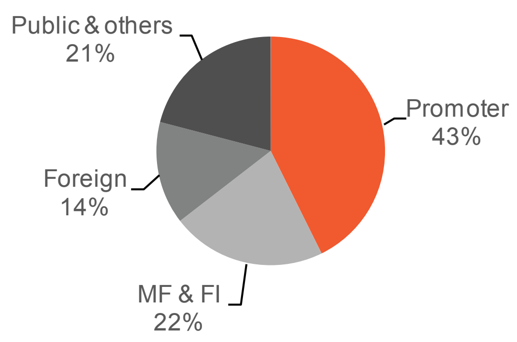
The Ramco Cements

Reco: Hold | CMP: Rs689

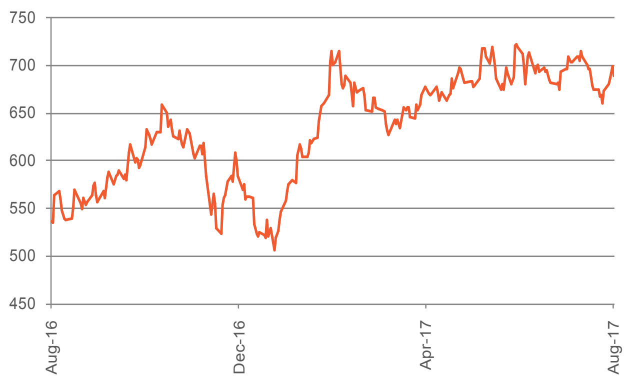
Company details

Price target:	Rs750
Market cap:	Rs16,250 cr
52-week high/low:	Rs750/479
NSE volume: (No of shares)	2.3 lakh
BSE code:	500260
NSE code:	RAMCOCEM
Sharekhan code:	RAMCOCEM
Free float: (No of shares)	13.5 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	1.1	2.1	-0.2	26.9
Relative to Sensex	-4.0	-6.6	-14.1	7.9

Key points

- **Challenges in the southern region with erosion of low fuel cost advantage affects operational performance:** The Ramco cements posted 6.7% YoY growth in net sales (net of excise duty) to Rs1,029 crore during Q1FY2018 on account of a 4.1% YoY growth in cement volume while the blended realization was flat YoY for the quarter. The volume growth was impacted due to drought and sand scarcity in Tamil Nadu while the company witnessed growth in Eastern region. The Operating Profit Margin (OPM) for the quarter contracted by 252basis points YoY to 28.2% on account of higher power & fuel cost (up 25% YoY on per tonne basis due to exhaustion of low cost pet coke inventory) and higher freight expenses (up 8.4% YoY on per tonne basis). Hence, the blended EBITDA per tonne for the quarter declined 19.8% YoY to Rs989. Decline in interest cost (down 47% YoY, earlier repayment of borrowings) and lower effective tax rate (down 79bps YoY) resulted in an almost flat PAT YoY at Rs156 crore.

- **Capacity to be expanded by 3.1MTPA to strengthen geographical reach:** The company is mulling over the expansion of its satellite grinding capacity from 4MTPA to 7.1MTPA at a cost of Rs1,095 crore. The slated expansion which is to be completed in 18 months (post statuary clearances) is expected to take its aggregate cement capacity from 16.5MTPA to 19.6MTPA. The expansion aims to strengthen reach in Andhra Pradesh, West Bengal and North Eastern states.

- **Outlook:** Ramco's operational performance is expected to be under pressure in the near term considering lower utilisation in the Southern region and benefits of low cost petcoke inventory getting totally eroded from the current quarter. Moreover, any pressure on cement prices in Southern region can further affect its operational performance. We would be keenly monitoring demand revival in Southern region post monsoon, cement price trends and measures taken by the company to improve operational efficiency (to contain increased power and freight costs).

- **Valuation - maintain Hold with revised PT of Rs750:** We have lowered our earnings estimates for FY2018 and FY2019 to factor in higher power & fuel cost in 1QFY2018. We believe that benefit of the capacity expansion would be back ended in FY2019. The near term challenges persist on the containment of cost pressure and the ability to increase prices to sustain margins. Hence, we maintain our Hold rating on the stock with revised price target of Rs750 due to downward revision in operating margins.

Result Rs cr

Particulars	Q1FY18	Q1FY17	YoY %	Q4FY17	QoQ %
Net Sales	1028.8	964.4	6.7	1026.2	0.3
Total Expenditure	738.4	667.9	10.6	773.7	-4.6
Operating profits	290.4	296.5	-2.0	252.5	15.0
Other Income	5.2	9.6	-45.2	5.8	-9.0
EBIDTA	295.7	306.1	-3.4	258.3	14.5
Interest	15.5	29.1	-47.0	20.1	-23.2
PBDT	280.2	276.9	1.2	238.2	17.6
Depreciation	72.0	66.3	8.6	66.4	8.4
PBT	208.2	210.6	-1.1	171.8	21.2
Tax	52.4	54.7	-4.1	37.3	40.5
Extraordinary items	0.0	0.0		0.0	
Reported Profit After Tax	155.8	155.9	-0.1	134.5	15.9
Adjusted PAT	155.8	155.9	-0.1	134.5	15.9
EPS	6.5	6.6	-0.1	5.7	15.9
OPMs (%)	28.2	30.7	-252 bps	24.6	362 bps
PAT (%)	15.1	16.2	-102 bps	13.1	204 bps
Tax rate (%)	25.2	26.0	-79 bps	21.7	345 bps

Valuation Rs cr

Particulars	FY2015	FY2016	FY2017	FY2018E*	FY2019E*
Net sales	3,594	3,573	3,950	4,333	4,707
Growth YoY (%)	-1.1	-0.6	10.5	9.7	8.6
EBITDA	662	1,072	1,176	1,243	1,362
EBITDA margin (%)	18.4	30.0	29.8	28.7	28.9
Adjusted PAT	236	518	649	710	804
Growth YoY (%)	91.8	119.6	25.3	9.4	13.2
EPS diluted (Rs)	9.9	21.8	27.3	30.2	34.1
P/E (x)	70.2	32.0	25.5	23.1	20.4
P/BV (x)	6.3	5.4	4.4	3.9	3.3
EV/EBITDA (x)	28.5	17.2	15.1	14.0	12.5
EV/Sales (x)	5.2	5.2	4.5	4.0	3.6
RoE (%)	9.2	18.1	19.0	17.9	17.6
RoCE (%)	7.4	12.0	12.9	13.3	13.8

*Factoring in buy-back of 25lakh shares which is currently underway by the company

Per tonne analysis (blended basis) Rs per tonne

Particulars	Q1FY17	Q2FY17	Q3FY17	Q4FY17	Q1FY18	YoY %	QoQ %
Volume	2,066,000	2,034,000	1,988,000	2,277,000	2,150,000	4.1	-5.6
Realisation	4,467	4,560	4,648	4,435	4,487	0.4	1.2
Total RM	810	777	830	862	803	-0.9	-6.8
Employee Expense	342	344	351	295	349	1.9	18.0
Power & Fuel	626	591	645	617	782	25.0	26.7
Transportation & Handling	858	879	891	901	930	8.4	3.2
Other Expenses	597	669	645	722	634	6.2	-12.2
Total Expenditure per tonne	3,233	3,260	3,362	3,398	3,497	8.2	2.9
EBDITA per tonne	1,234	1,300	1,286	1,037	989	-19.8	-4.6

Stock Update

Near-term pain to weigh on operating margins

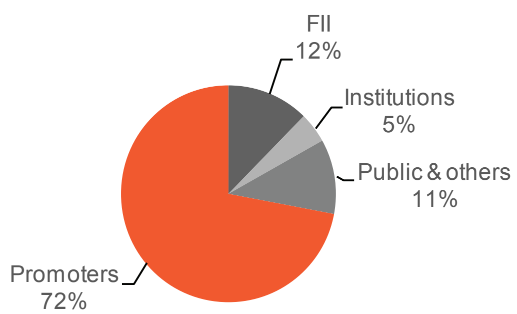
Century Plyboards (India)

Reco: Hold | CMP: Rs275

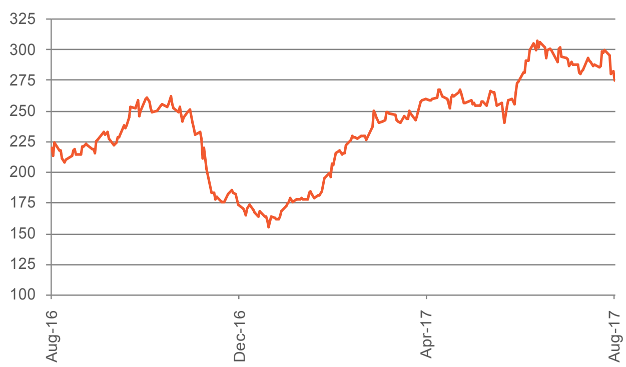
Company details

Price target:	Rs280
Market cap:	Rs6,114 cr
52-week high/low:	Rs313/155
NSE volume: (No of shares)	2.4 lakh
BSE code:	532548
NSE code:	CENTURYPLY
Sharekhan code:	CENTURYPLY
Free float: (No of shares)	6.2 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-3.2	10.4	38.6	26.8
Relative to Sensex	-8.1	0.9	19.3	7.8

Key points

- **GST-related initial issues along with raw-material supply constraints affects overall operating performance:** Century Plyboards (India) Limited (Century Plyboards) reported standalone net sales growth of 8.1% YoY to Rs.438.6 crore in Q1FY2018. The topline was supported by the plywood division (revenue up 10.0% YoY), led by higher volume. The laminate division's revenue was flat YoY on account of reduction in tax rate due to GST (from 29-30% to 18%), resulting in channel destocking. The company's OPM contracted by 238BPS on account of lower gross profit margin in plywood and laminate divisions. The laminate division suffered due to lower capacity utilisation (production issues faced in April and May 2017), while the plywood division suffered on account of higher raw-material costs (chemicals and veneer), which were not passed on to customers. Further, higher depreciation charge (up 42.5% YoY due to commissioning of particle board plant) and higher effective tax rate (19.0% as against 14.4%) led to an 18.4% YoY decline in adjusted net profit.
- **Capacity expansion across units during FY2018-FY2019:** The MDF unit is expected to commence commercial operations by early October 2017, which has the potential to generate revenue of Rs.170 crore with an OPM of over 30% in H2FY2018. Further, expansion in laminates (two additional lines) is expected to be operational in the current fiscal. The company is also planning the doors venture with a Chinese company. The company is planning to set up rooftop solar panel on its plants (at a cost of Rs.35 crore), which can save 5-10% of its electricity cost (first to be implemented at its Chennai plant of 1.06MW at a cost of ~Rs.5 crore.)
- **Outlook – Near-term pressure on operating margin to remain:** Century Plyboards' operating margin is expected to be under pressure in the near term, with raw-material supply constraints faced in Myanmar and Laos leading to contraction in gross profit margin. Further, the inability to pass on the increase in cost to consumers with the unorganised sector benefitting from GST-related initial issues (e-way bills yet to be implemented) can further pressurise margins in the near term. The scaling of particle board unit, commencement of MDF unit during H2FY2018 and easing of raw-material supply from Q4FY2018 are expected to ease pressure on margins.
- **Valuation – Downgrade to hold with unchanged PT of Rs.280:** We have adjusted earnings estimates for FY2018-FY2019, factoring in delay in commencement of MDF unit and increased raw-material price affecting overall operating margins. Considering the above-mentioned, challenges in the near term, we have downgraded the stock to Hold with an unchanged price target of Rs.280.

Result (standalone) Rs cr

Particulars	Q1FY18	Q1FY17	YoY %	Q4FY17	QoQ %
Income from operations	438.6	405.8	8.1	488.5	(10.2)
COGS	233.9	204.5	14.4	253.1	(7.6)
Gross profit	204.7	201.2	1.7	235.5	(13.1)
Gross margin (%)	46.7	49.6	(292)	48.2	(152.8)
Employee cost	68.9	63.8	8.0	66.7	3.2
Other expenditure	74.7	71.3	4.8	85.0	(12.0)
Total expenditure	377.5	339.6	11.2	404.8	(6.7)
Operating profit	61.1	66.1	-7.7	83.8	(27.1)
OPM (%)	13.9	16.3	(238)	17.1	(322.5)
Finance cost	6.3	8.9	-29.0	4.7	33.6
Depreciation	13.2	9.3	42.5	15.6	(15.2)
Other income	0.5	0.8	-32.1	0.1	268.3
Forex loss/(gain)	-	(1.5)		(10.8)	
PBT	42.1	50.3	-16.2	74.5	(43.4)
Tax	8.0	7.2	10.7	18.6	(56.8)
Reported PAT	34.1	43.1	-20.8	55.9	(39.0)
Adjusted PAT	34.1	41.8	-18.4	45.1	(24.3)

Segmental performance Rs cr

Particulars	Q1FY18	Q1FY17	YoY %	Q4FY17	QoQ %
Plyboards					
Revenue	342.7	311.6	10.0	374.3	(8.4)
EBIT	38.5	43.6	(11.8)	74.0	(48.1)
EBIT margin (%)	11.2	14.0	(278)	19.8	856
Capital employed	542.7	523.2	3.7	539.7	0.6
RoCE (%)	28.3	33.3	(500)	54.9	(2,653)
Laminates					
Revenue	89.1	89.1	0.1	109.9	(18.9)
EBIT	9.2	11.5	(20.4)	11.0	(16.9)
EBIT margin (%)	10.3	12.9	(265)	10.0	(25)
Capital employed	174.1	159.4	9.2	160.3	8.6
RoCE (%)	21.1	28.9	(783)	27.5	(646)
CFS					
Revenue	23.9	23.5	1.6	23.5	1.8
EBIT	6.7	7.9	(14.6)	6.0	12.1
EBIT margin (%)	28.1	33.5	(535)	25.5	(258)
Capital employed	44.6	53.1	(16.0)	49.5	(10.0)
RoCE (%)	60.2	59.2	99	48.4	1,186
MDF Boards					
Revenue	0.6	1.4	(56.2)	0.6	3.4
EBIT	(0.2)	0.2	-	(0.6)	-
EBIT margin (%)	(29.9)	17.4	-	(108.1)	-
Capital employed	325.8	58.7	455.1	264.5	23.2
RoCE (%)	(0.2)	1.6		(1.0)	
Particle Boards					
Revenue	11.1	-	-	11.7	(5.3)
EBIT	(3.7)	-	-	(3.3)	12.4
EBIT margin (%)	(33.6)	-	-	(28.3)	530
Capital employed	54.2	55.9	(3.0)	56.7	(4.5)
RoCE (%)	(27.6)	-		(23.4)	

Valuation (consolidated) **Rs cr**

Particulars	FY15	FY16	FY17	FY18E	FY19E
Net sales	1,588	1,641	1,819	2,135	2,583
Growth YoY (%)	18	3	11	17	21
Adjusted EBITDA	274	295	315	384	509
EBITDA margin (%)	17.2	18.0	17.3	18.0	19.7
Adjusted PAT	149	181	178	192	271
Growth YoY (%)	145	21	(1)	8	41
Adjusted EPS (Rs)	6.7	8.1	8.0	8.6	12.2
P/E (x)	41.1	36.2	32.2	31.9	22.6
RoCE (%)	23.0	21.9	19.7	16.9	18.8
RoE (%)	44.0	37.0	31.1	24.4	27.3

Stock Update

Disappointing performance and weak guidance; Downgrade to Reduce with downward revised TP of Rs.950

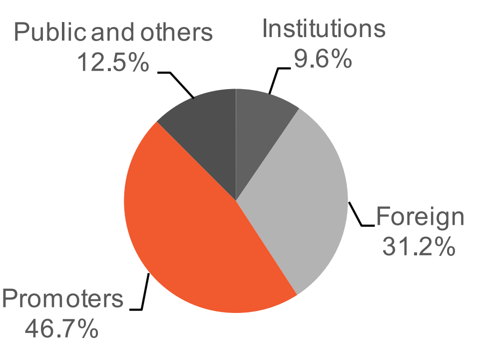
Lupin

Reco: Reduce | CMP: Rs995

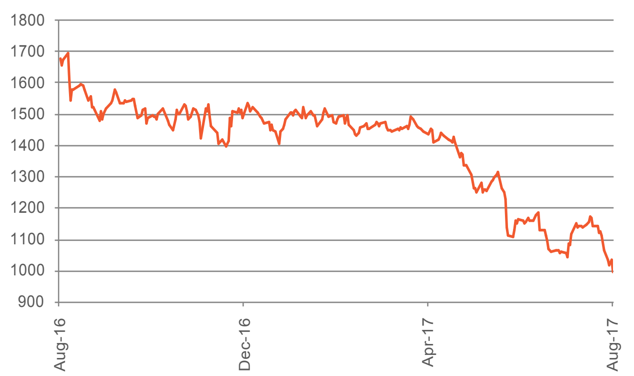
Company details

Price target:	Rs950
Market cap:	Rs44,924 cr
52-week high/low:	Rs1734/986
NSE volume: (No of shares)	14.8 lakh
BSE code:	500257
NSE code:	LUPIN
Sharekhan code:	LUPIN
Free float: (No of shares)	24.06 cr

Shareholding pattern



Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	-1.7	-20.1	-29.7	-38.8
Relative to Sensex	-6.7	-26.9	-39.5	-48.0

Key points

- **Disappointing performance:** During Q1FY2018, Lupin's total sales (including operating income) declined by 12.8% to Rs.3,869.6 crore. Operating profit declined by 41.3% to Rs.768.4 crore and adjusted profit declined by 59.3% to Rs.359.1 crore. Disappointing performance for the quarter was mainly on account of a 26.8% decline in US revenue due to increased competition in gGlumetza and gFortamet and GST transition impact on the Indian business (declined by 2%).

- **Weak guidance:** Management has indicated that the next 12-15 months will be difficult as US, Japan and India businesses are undergoing structural changes. Increasing pricing pressure due to channel consolidation, increased competition in gFortamet and gGlumetza, delay in key product approvals, slow ramp up of Gavis portfolio and appreciating rupee will add to the pressure on US business. Further, transition to GST in India is likely to weigh down on the domestic business. gRenvela opportunity for the US market is also lost due to entry of another generic player, with many other players in fray. Therefore, we feel Lupin will continue to witness pressure on its business and margins for FY2018 and FY2019. Moreover, management has further reduced its already-weak operating margin guidance of 24-26% to 21-23% for FY2018.

- **Downgrade to Reduce with downward revised TP of Rs.950:** Considering the weak outlook and guidance, rupee appreciation and the change in regulatory environment across key markets such as US, India and Japan, we have revised downward our sales estimates by 10% each for FY2018 and FY2019, while earnings estimates are revised downward by 30% and 22% for FY2018 and FY2019, respectively. Consequently, we downgrade our rating to Reduce and revise downward our target price (TP) to Rs.950 (valuing the stock at 16x FY2019 earnings estimates).

Results Rs cr

Particulars	Q1 FY18	Q1 FY17	YoY (%)	Q4 FY17	QoQ (%)
Total sales	3869.6	4439.4	-12.8	4253.3	-9.0
Expenditure	3101.2	3131.4	-1.0	3148.0	-1.5
Operating profit	768.4	1308.0	-41.3	1105.3	-30.5
Other income	32.0	82.6	-61.3	45.3	-29.5
EBIDTA	800.3	1390.7	-42.4	1150.6	-30.4
Interest	43.9	32.0	37.3	40.6	8.1
Depreciation	260.5	202.7	28.5	267.4	-2.6
PBT	495.9	1156.0	-57.1	842.6	-41.1
Tax	136.8	273.4	-50.0	136.7	0.1
Adjusted PAT	359.1	882.6	-59.3	705.9	-49.1
OCI	-1.1	-0.6	65.6	-1.8	-39.8
Net profit (Reported)	358.1	881.9	-59.4	704.1	-49.1
Adj. EPS	8.0	19.6		15.7	
Reported EPS (Rs)	8.0	19.6	-59.4	15.6	-49.1
OPM (%)	19.9	29.5	-961	26.0	-613
EBIDTA margin (%)	20.7	31.3	-1064	27.1	-637
Net profit margin (%)	9.3	19.9	-1061	16.6	-730
Effective tax rate (%)	27.6	23.7	393	16.2	1136

Key concall highlights

- US base business (excluding gFortamet and gGlumetza) continues to witness high single-digit pricing pressure. gFortamet and gGlumetza are also losing market share due to new competition that entered during the quarter. During the quarter, Lupin launched four new products in the US. Further, channel consolidation and appreciating rupee will add to woes over the next few quarters.

- The Indian market is also witnessing structural changes, as the government takes new initiatives to reduce generic prices by starting jan-aushadhi stores and curtailing brand prescription. NLEM list continues to widen, thereby adding to pressure.

- Japanese government has recently proposed to take price cut for generic products every two years, adding to the existing problems in other geographies. The company had recently acquired 21 generic brands from Shionogi (~$90 million sales), covering therapeutic areas such as central nervous system (CNS), oncology, cardiovascular and anti-infectives, which helped maintain growth in Japan.

- R&D spends for Q1FY2018 were Rs.500 crore, 13.1% of sales, and will continue to be in the same range for the next two years.

- Lupin filed one ANDA and received three approvals from the USFDA during the quarter. Cumulative ANDA filings with the USFDA were 368 as of 30th June 2017, with the company having received 217 approvals to date. The company now has 45 First-to-Files (FTF) filings, including 23 exclusive FTF opportunities.

- Operating working capital increased to Rs.5,407 crore in Q1FY2018 compared to Rs.4,896 crore in Q4FY2017. The working capital number of days stood at 119 days at the end of Q1FY2018 (up from 105 days in Q4FY2017).

- Capex for the quarter was Rs.283 crore. Net Debt-Equity ratio for the company stands at 0.37:1.

Geography wise Sales Rs cr

Particulars	Q1 FY18	Q1 FY17	YoY (%)	Q4 FY17	QoQ (%)
Formulations	3527.5	4045.2	-12.8	3880.4	-9.1
North America	1601.8	2188.6	-26.8	1900.7	-15.7
India	932.4	949.9	-1.8	878.8	6.1
APAC	598.9	541.6	10.6	611.8	-2.1
EMEA	225.9	219.4	3.0	301.2	-25.0
LATAM	126.9	108.9	16.5	126.9	0.0
ROW	41.6	36.8	13.0	61.0	-31.8
API	279.3	296.6	-5.8	281.5	-0.8
Other operating income	62.8	125.9	-50.1	91.4	-31.4
Total	**3869.6**	**4467.7**	**-13.4**	**4253.3**	**-9.0**

Downgrade to Reduce with downward revised TP of Rs.950: Considering the weak outlook and guidance, rupee appreciation and the change in regulatory environment across key markets such as India and Japan, we have revised downward our sales estimates by 10% each for FY2018 and FY2019, while earnings estimates are revised downward by 30% and 22% for FY2018 and FY2019, respectively. Consequently, we downgrade our rating to Reduce and revise downward our TP to Rs.950 (valuing the stock at 16x FY2019 earnings estimates).

Valuation Rs cr

Particulars	FY16	FY17	FY18E	FY19E
Net sales	14,255.6	17,494.3	17,586.3	20,330.1
Adjusted net profit	2,260.8	2,713.4	2,062.6	2,698.6
Shares in issue (cr)	45.1	45.2	45.2	45.2
Adj. EPS (Rs)	50.2	60.1	45.7	59.8
PER (x)	19.8	16.5	21.7	16.6
EV/Ebidta (x)	13.8	11.2	12.2	9.5
Book value (Rs/ share)	247.7	298.9	355.9	415.7
P/BV (x)	4.0	3.3	2.8	2.4
Mcap/sales	3.3	2.6	2.5	2.2
RoCE (%)	17.0	16.8	12.2	14.8
RoNW (%)	20.3	20.1	12.8	14.4

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