

December 14, 2020

Intensifying competition for gRevlimid...

Cipla has announced the settlement of Revlimid (Lenalidomide) patent litigation with Celgene [Bristol Myers Squibb (BMS)] in the US. This makes Cipla the fourth player after Natco, Alvogen and Dr Reddy's (DRL) to sign a settlement agreement with the innovator for gRevlimid. Under the terms of the settlement, Celgene will provide Cipla with a license to sell generic volume-limited amounts of gRevlimid capsules in the US sometime after March 2022 subject to regulatory approval. This limited volume constraint will be applicable till January 2026. The oncology drug, indicated for treatment of multiple myeloma, had annual US sales of US\$9 billion in CY19 as per BMS report. For volume-limit assumptions, we expect similar terms and conditions as Natco for all companies i.e. not exceeding mid-single-digit percentage of gRevlimid dispensed in the US in the first year and a gradual increase to one-third share until January 2026.

Exhibit 1: Key Revlimid event timeline

Date	Details
Dec-05	Celgene gets Revlimid approval from USFDA
Dec-15	Celgene settles Revlimid patent litigation with Natco
Mar-19	Celgene settles Revlimid patent litigation with Alvogen
Sep-20	Celgene settles Revlimid patent litigation with Dr Reddy's
Dec-20	Celgene settles Revlimid patent litigation with Cipla
Dec-20	USFDA target action date for Natco's gRevlimid filing
Mar-22	Likely launch of gRevlimid capsules by Natco
FY 23	Launch of gRevlimid post Natco's launch by Alvogen, Dr Reddy's, Cipla
Mar'22-Jan'26	Volume-limited sales of gRevlimid by the four players
Post Jan'26	Unlimited volume sales of gRevlimid

Source: ICICI Direct Research

Valuation & Outlook

Cipla: Owing to competition, we expect Cipla to garner 1-7% market share for volume-limited period and 15% thereafter. Hence, with above market share and a 70-90% price erosion assumption, our gRevlimid NPV arrives at ₹ 41. We maintain **BUY** rating and arrive at a target price of ₹ 965, including base business value of ~₹ 924 (26x FY23E EPS of ₹ 35.5) + ₹ 41 NPV.

Natco Pharma: On the other hand, while the earlier settlement by Alvogen, Dr Reddy's (DRL) and now Cipla indicate increased competition, potential future entry by other players signal likely crowding in this lucrative space. Also, the volume-limit clause is likely to hinder Natco from gaining additional market share despite assuming early mover advantage. Subsequently, we maintain **HOLD** rating and revise our target price to ₹ 885, which includes base business value of ₹ 756 (28x FY23E EPS of 27) + NPV of ₹ 129.

Dr Reddy: Similarly, DRL's market share will also be impacted by increased competition and volume-limit clause in March 2022-January 2026. We maintain **BUY** at a revised TP of ₹ 5770, which includes base business value of ₹ 5558 (25x FY23E EPS of 222.3) + ~₹ 211 NPV for gRevlimid.

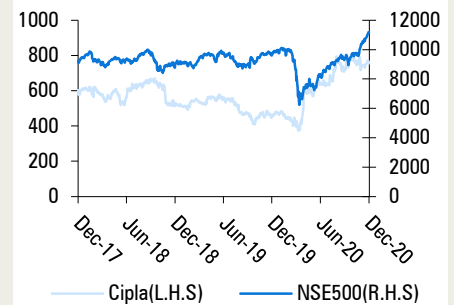
Note: Our NPV calculations are based on assumption that all three players receive USFDA approvals before March 2022 and subsequent launches.

Valuation Summary

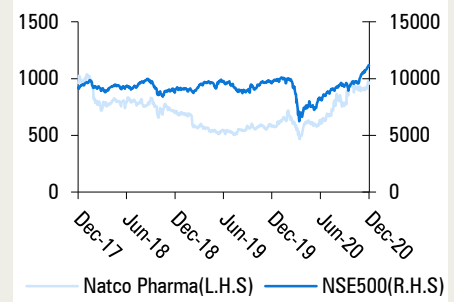
Company	CMP	FY23E Base business EPS	Multiple	NPV		Target Price		Rating	
				Old	New	Old	New	Old	New
Cipla	756	35.5	26	NA	41	925	965	Buy	Buy
Natco Pharma	951	27.0	28	294	129	970	885	Hold	Hold
Dr Reddy's	5,016	222.3	25	515	211	6,000	5,770	Buy	Buy

Source: ICICI Direct Research

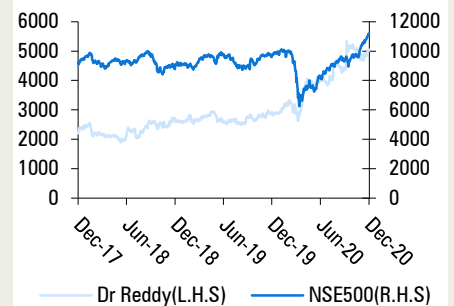
Price Performance - Cipla



Price Performance - Natco Pharma



Price Performance - Dr Reddy's



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Financial Summary - Cipla

Exhibit 2: Profit & Loss		₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E	
Revenues	17,132.0	19,516.9	20,959.8	22,598.0	
Growth (%)	4.7	13.9	7.4	7.8	
Raw Material Expenses	5,991.4	7,386.3	7,859.9	8,361.3	
Gross Profit	11,140.6	12,130.6	13,099.9	14,236.8	
Employee Expenses	3,027.0	3,287.2	3,489.3	3,704.6	
Other Expenditure	4,907.6	4,664.8	5,344.7	5,762.5	
Total Operating Expenditure	13,926.0	15,338.3	16,694.0	17,828.4	
EBITDA	3,206.0	4,178.6	4,265.8	4,769.6	
Growth (%)	3.5	30.3	2.1	11.8	
Depreciation	1,174.7	1,183.8	1,186.2	1,249.2	
Interest	197.4	166.4	109.0	79.0	
Other Income	344.2	274.0	398.2	440.7	
PBT	2,178.2	3,102.4	3,368.9	3,882.2	
Total Tax	631.2	884.2	909.6	1,009.4	
PAT before MI	1,547.0	2,218.2	2,459.3	2,872.8	
Minority Interest	-47.0	-32.7	-12.3	-14.4	
Adjusted PAT	1,546.5	2,225.1	2,445.7	2,861.2	
Growth (%)	3.4	43.9	9.9	17.0	
EPS (Adjusted)	19.2	27.6	30.4	35.5	

Source: ICICI Direct Research

Exhibit 3: Cash Flow Statement		₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E	
Profit/(Loss) after taxation	1,329.9	2,225.1	2,445.7	2,861.2	
Add: Depreciation	1,174.7	1,183.8	1,186.2	1,249.2	
(inc)/Dec in Current Assets	-114.3	-1,593.5	-871.4	-905.6	
inc/(Dec) in Current Liabilities	487.3	151.7	278.7	290.4	
Others	190.9	166.4	109.0	79.0	
CF from Operating activities	3,068.5	2,133.4	3,148.1	3,574.2	
(Purchase)/Sale of Fixed Assets	-985.7	-500.0	-500.0	-500.0	
Change in Investment	1,178.0	-500.0	-1,000.0	-1,000.0	
Others	73.2	-40.4	-20.4	-22.8	
CF from Investing activities	265.5	-1,040.4	-1,520.4	-1,522.8	
Change in Equity	0.1	0.0	0.0	0.0	
Change in Loan	-1,760.0	-500.0	-500.0	-500.0	
Dividend & Dividend tax	-664.2	-386.4	-556.3	-611.4	
Others	-524.7	-166.4	-109.0	-79.0	
CF from Financing activities	-2,948.8	-1,052.9	-1,165.2	-1,190.4	
Net Cash Flow	385.1	40.2	462.5	860.9	
Cash and Cash equ. at beginning	618.8	1,003.9	1,044.1	1,506.6	
Cash	1,003.9	1,044.1	1,506.6	2,367.5	
Free Cash Flow	2,082.8	1,633.4	2,648.1	3,074.2	

Source: ICICI Direct Research

Exhibit 4: Balance Sheet		₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E	
Equity Capital	161.3	161.3	161.3	161.3	
Reserve and Surplus	15,601.8	17,440.4	19,329.8	21,579.6	
Total Shareholders funds	15,763.0	17,601.6	19,491.0	21,740.9	
Total Debt	2,816.4	2,316.4	1,816.4	1,316.4	
Deferred Tax Liability	365.2	383.5	402.6	422.8	
Long Term Provision	133.3	139.9	146.9	154.3	
MI & Other Liabilities	638.7	623.2	628.9	633.6	
Source of Funds	19,716.6	21,064.6	22,486.0	24,267.9	
Gross Block - Fixed Assets	11,979.6	12,479.6	13,179.6	13,879.6	
Accumulated Depreciation	5,355.0	6,538.8	7,725.0	8,974.1	
Net Block	6,624.6	5,940.8	5,454.7	4,905.5	
Capital WIP	824.5	824.5	624.5	424.5	
Fixed Assets	7,449.1	6,765.4	6,079.2	5,330.0	
Investments	1,595.3	2,095.3	3,095.3	4,095.3	
Goodwill on Consolidation	2,934.0	2,934.0	2,934.0	2,934.0	
Long term Loans & Advances	52.4	55.0	57.8	60.6	
Other Non current assets	944.4	991.6	1,041.2	1,093.3	
Inventory	4,377.6	4,783.7	5,173.1	5,577.5	
Debtors	3,891.3	5,008.0	5,415.7	5,839.0	
Loans and Advances	5.6	5.9	6.2	6.5	
Other Current Assets	1,408.9	1,479.3	1,553.3	1,631.0	
Cash	1,003.9	1,044.1	1,506.6	2,367.5	
Total Current Assets	10,687.3	12,321.0	13,654.9	15,421.4	
Creditors	2,281.8	2,350.3	2,541.7	2,740.3	
Provisions	948.2	995.6	1,045.4	1,097.6	
Other current liabilities	716.0	751.8	789.4	828.8	
Total Current Liabilities	3,946.0	4,097.7	4,376.4	4,666.8	
Net Current Assets	6,741.3	8,223.3	9,278.5	10,754.6	
Application of Funds	19,716.6	21,064.6	22,486.0	24,267.9	

Source: ICICI Direct Research

Exhibit 5: Key Ratios					
(Year-end March)	FY20	FY21E	FY22E	FY23E	
Per share data (₹)					
Adjusted EPS	19.2	27.6	30.4	35.5	
BV per share	195.8	218.6	242.1	270.0	
Cash per Share	12.5	13.0	18.7	29.4	
Dividend per share	4.8	6.9	7.6	8.9	
Operating Ratios (%)					
Gross Margins	65.0	62.2	62.5	63.0	
EBITDA margins	18.7	21.4	20.4	21.1	
PAT Margins	9.0	11.4	11.7	12.7	
Inventory days	93.3	89.5	90.1	90.1	
Debtor days	82.9	93.7	94.3	94.3	
Creditor days	48.6	44.0	44.3	44.3	
Asset Turnover	0.9	0.9	0.9	0.9	
EBITDA conversion rate	95.7	51.1	73.8	74.9	
Return Ratios (%)					
RoE	9.8	12.6	12.5	13.2	
RoCE	12.0	15.5	15.5	16.3	
RoIC	12.0	16.9	17.3	19.6	
Valuation Ratios (x)					
P/E	39.4	27.4	24.9	21.3	
EV / EBITDA	19.2	14.5	13.7	11.8	
EV / Net Sales	3.6	3.1	2.8	2.5	
Market Cap / Sales	3.5	3.1	2.9	2.7	
Price to Book Value	3.9	3.5	3.1	2.8	
Solvency Ratios					
Debt / EBITDA	0.9	0.6	0.4	0.3	
Debt / Equity	0.2	0.1	0.1	0.1	
Current Ratio	2.5	2.8	2.8	2.8	

Source: ICICI Direct Research

Financial Summary – Natco Pharma

Exhibit 6: Profit & Loss		₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E	
Revenues	1,915.0	2,542.4	2,332.1	2,376.6	
Growth (%)	-8.6	32.8	-8.3	1.9	
Raw Material Expenses	381.6	632.7	489.7	475.3	
Employee Expenses	375.0	419.8	423.4	440.6	
Other expenses	575.8	668.6	697.7	752.5	
Total Operating Expenditure	1,332.4	1,721.1	1,610.8	1,668.4	
EBITDA	582.6	821.3	721.3	708.2	
Growth(%)	-26.7	41.0	-12.2	-1.8	
Depreciation	99.8	114.1	130.1	146.1	
Interest	21.5	14.3	15.8	15.8	
Other Income	107.4	95.5	104.2	109.7	
PBT	568.7	788.4	679.7	656.0	
Total Tax	110.6	189.1	163.1	157.4	
PAT before MI	458.1	599.3	516.5	498.6	
Minority Interest	-2.7	3.8	6.0	6.0	
Adjusted PAT	460.8	595.5	510.5	492.6	
Growth(%)	-28.5	29.2	-14.3	-3.5	
EPS (Adjusted)	25.3	32.7	28.0	27.0	

Source: ICICI Direct Research

Exhibit 7: Cash Flow Statement		₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E	
Profit/(Loss) after taxation	460.9	595.5	510.5	492.6	
Add: Depreciation	99.8	114.1	130.1	146.1	
(Inc)/dec in Current Assets	-151.2	0.2	91.7	-19.4	
Inc/(dec) in CL and Provisions	53.6	58.0	-15.2	16.0	
CF from operating activities	463.1	767.8	717.1	635.3	
(Purchase)/Sale of Fixed Assets	-336.5	-250.0	-250.0	-250.0	
(Increase)/Decrease in Investments	53.0	-171.6	-200.0	-200.0	
Others	-96.5	3.0	3.3	3.5	
CF from investing activities	-380.0	-418.6	-446.7	-446.5	
Inc / (Dec) in Equity Capital	0.1	0.0	0.0	0.0	
Inc / (Dec) in Loan	0.0	0.0	0.0	0.0	
Dividend & Dividend tax	-153.6	-118.4	-109.3	-109.3	
Others	-97.3	-14.3	-15.8	-15.8	
CF from financing activities	-250.8	-132.7	-125.1	-125.1	
Net Cash flow	-167.7	216.6	145.3	63.7	
Opening Cash	279.5	66.0	296.9	458.0	
Closing Cash	111.8	282.6	442.2	521.7	
Free Cash Flow	126.6	517.8	467.1	385.3	

Source: ICICI Direct Research

Exhibit 8: Balance Sheet		₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E	
Equity Capital	36.4	36.4	36.4	36.4	
Reserve and Surplus	3,737.1	4,214.2	4,615.4	4,998.7	
Total Shareholders funds	3,773.5	4,250.6	4,651.9	5,035.2	
Total Debt	315.9	315.9	315.9	315.9	
Deferred Tax Liability	25.9	28.0	30.2	32.6	
Minority Interest / Others	12.0	13.0	14.0	15.1	
Long Term Provisions	90.2	90.2	90.2	90.2	
Total Liabilities	4,217.5	4,697.7	5,102.2	5,489.0	
Gross Block - Fixed Assets	2,148.6	2,498.6	2,848.6	3,198.6	
Accumulated Depreciation	564.2	678.3	808.4	954.4	
Net Block	1,584.4	1,820.3	2,040.2	2,244.2	
Capital WIP	518.0	418.0	318.0	218.0	
Total Fixed Assets	2,102.4	2,238.3	2,358.2	2,462.2	
Investments	112.3	283.9	483.9	683.9	
Inventory	558.0	495.6	454.6	463.2	
Debtors	551.3	613.5	562.8	573.5	
Cash	66.0	296.9	458.0	537.5	
Other Current Assets	1,121.6	1,121.6	1,121.6	1,121.6	
Total Current Assets	2,296.9	2,527.5	2,596.9	2,695.8	
Creditors	255.4	304.2	279.0	284.4	
Provisions	10.5	11.3	12.2	13.2	
Other Current Liabilities	104.4	112.8	121.8	131.5	
Total Current Liabilities	370.3	428.3	413.0	429.1	
Net Current Assets	1,926.6	2,099.3	2,183.9	2,266.7	
LT L & A & Other Non CA	76.2	76.2	76.2	76.2	
Application of Funds	4,217.5	4,697.7	5,102.2	5,489.0	

Source: ICICI Direct Research

Exhibit 9: Key Ratios		₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E	
Per share data (₹)					
Adjusted EPS	25.3	32.7	28.0	27.0	
BV per share	207.1	233.3	255.3	276.4	
Dividend per share	6.8	6.5	6.0	6.0	
Cash Per Share	3.6	16.3	25.1	29.5	
Operating Ratios (%)					
Gross Profit Margins	80.1	75.1	79.0	80.0	
EBITDA Margins	30.4	32.3	30.9	29.8	
PAT Margins	24.1	23.4	21.9	20.7	
Inventory days	106.4	71.1	71.1	71.1	
Debtor days	105.1	88.1	88.1	88.1	
Creditor days	48.7	43.7	43.7	43.7	
Asset Turnover	0.9	1.0	0.8	0.7	
EBITDA Conversion Rate	79.5	93.5	99.4	89.7	
Return Ratios (%)					
RoE	12.2	14.0	11.0	9.8	
RoCE	14.0	17.1	13.6	12.2	
RoIC	13.4	18.7	15.1	13.6	
Valuation Ratios (x)					
P/E	37.6	29.1	33.9	35.2	
EV / EBITDA	30.1	20.9	23.3	23.3	
EV / Net Sales	9.2	6.7	7.2	6.9	
Market Cap / Sales	9.0	6.8	7.4	7.3	
Price to Book Value	4.6	4.1	3.7	3.4	
Solvency Ratios					
Debt / EBITDA	0.5	0.4	0.4	0.4	
Debt / Equity	0.1	0.1	0.1	0.1	
Current Ratio	6.0	5.2	5.2	5.0	

Source: ICICI Direct Research

Financial Summary – Dr Reddy's

Exhibit 10: Profit & Loss		₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E	
Revenues	17,517.0	19,187.9	22,132.4	24,579.1	
Growth (%)	13.4	9.5	15.3	11.1	
Raw Material Expenses	5,554.4	6,069.1	6,970.9	7,680.5	
Employee expenses	3,380.2	3,662.6	4,103.8	4,560.6	
Other expenses	6,116.4	4,992.5	5,754.4	6,390.6	
Total Operating Expenditure	15,051.0	14,724.3	16,829.1	18,631.7	
EBITDA	2,466.0	4,463.6	5,303.3	5,947.4	
Growth (%)	-21.8	81.0	18.8	12.1	
Interest	98.3	98.9	50.5	50.5	
Depreciation	1,163.1	1,241.8	1,281.3	1,354.0	
PBT before Exceptional It	1,829.6	3,364.2	4,327.8	4,955.8	
Share of profit/(loss) of e	0.0	0.0	0.0	0.0	
PBT	1,829.6	3,364.2	4,327.8	4,955.8	
Total Tax	-140.3	594.6	1,125.2	1,288.5	
PAT	2,026.0	2,799.3	3,231.8	3,696.5	
Adjusted PAT	2,026.0	2,799.3	3,231.8	3,696.5	
Growth (%)	6.3	38.2	15.4	14.4	
EPS	121.8	168.4	194.4	222.3	
EPS (Adjusted)	121.8	168.4	194.4	222.3	

Source: ICICI Direct Research

Exhibit 11: Cash Flow Statement		₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E	
Profit/(Loss) after taxation	1,175.2	2,799.3	3,231.8	3,696.5	
Add: Depreciation & Amortiz	1,163.1	1,241.8	1,281.3	1,354.0	
Net Increase in Current Ass	-1,393.3	-318.4	-1,411.4	-1,185.8	
Net Increase in Current Liabi	639.7	289.8	406.5	369.1	
CF from operating activitie	2,984.1	4,111.4	3,558.7	4,284.4	
(Inc)/dec in Fixed Assets	-572.5	-2,650.0	-1,400.0	-1,400.0	
(Inc)/dec in Investments	-21.4	600.0	-1,700.0	-2,000.0	
Others	108.2	-66.0	-68.6	-71.4	
CF from investing activitie	-485.7	-2,116.0	-3,168.6	-3,471.4	
Inc / (Dec) in Equity Capital	-47.0	0.0	0.0	0.0	
Inc / (Dec) in Loan	-1,868.3	-1,200.0	0.0	0.0	
Dividend & Dividend Tax	-391.6	-384.7	-444.1	-507.9	
Others	-209.0	-98.9	-50.5	-50.5	
CF from financing activitie	-2,515.9	-1,683.6	-494.6	-558.5	
Net Cash flow	-17.5	311.9	-104.5	254.6	
Opening Cash	222.8	205.3	517.2	412.7	
Closing Cash	205.3	517.2	412.7	667.2	
Free Cash Flow	2,411.6	1,461.4	2,158.7	2,884.4	

Source: ICICI Direct Research

Exhibit 12: Balance Sheet		₹ crore			
(Year-end March)	FY20	FY21E	FY22E	FY23E	
Equity Capital	83.1	83.1	83.1	83.1	
Net Network	15,515.7	17,930.3	20,718.0	23,906.5	
Total Shareholders fund	15,598.8	18,013.4	20,801.1	23,989.6	
Total Debt	2,210.2	1,010.2	1,010.2	1,010.2	
Deferred Tax Liability	2.0	2.1	2.2	2.2	
Other Non Current Liabilit	205.5	213.7	222.3	231.2	
Long term Provisions	74.5	77.5	80.6	83.8	
Source of Funds	18,091.0	19,316.9	22,116.3	25,317.0	
Gross Block - Fixed Ass	15,616.9	18,766.9	20,666.9	22,566.9	
Accumulated Depreciatio	9,257.9	10,499.7	11,781.0	13,135.1	
Net Block	6,359.0	8,267.2	8,885.9	9,431.8	
Capital WIP	1,535.1	1,035.1	535.1	35.1	
Net Fixed Assets	7,894.1	9,302.3	9,421.0	9,466.9	
Goodwill	491.3	491.3	491.3	491.3	
Investments	2,677.8	2,077.8	3,777.8	5,777.8	
Inventory	3,506.7	3,841.2	4,430.6	4,920.5	
Cash	205.3	517.2	412.7	667.2	
Debtors	5,027.8	4,952.1	5,712.0	6,343.4	
Loans & Advances & Oth	1,490.6	1,550.2	1,612.2	1,676.7	
Total Current Assets	10,230.4	10,860.7	12,167.5	13,607.8	
Creditors	1,524.8	1,670.2	1,926.6	2,139.5	
Provisions & Other CL	3,609.5	3,753.9	3,904.0	4,060.2	
Total Current Liabilities	5,134.3	5,424.1	5,830.6	6,199.7	
Net Current Assets	5,096.1	5,436.5	6,336.9	7,408.1	
LT L& A, Other Assets	711.8	740.3	769.9	800.7	
Deferred Tax Assets	1,219.9	1,268.7	1,319.4	1,372.2	
Application of Funds	18,091.0	19,316.9	22,116.3	25,317.0	

Source: ICICI Direct Research

Exhibit 13: Key Ratios					
(Year-end March)	FY20	FY21E	FY22E	FY23E	
Per share data (₹)					
EPS	121.8	168.4	194.4	222.3	
BV per share	938.1	1,083.3	1,251.0	1,442.8	
Operating Ratios (%)					
Gross Profit Margins	68.3	68.4	68.5	68.8	
EBITDA margins	14.1	23.3	24.0	24.2	
Net Profit margins	11.6	14.6	14.6	15.0	
Inventory days	73.1	73.1	73.1	73.1	
Debtor days	104.8	94.2	94.2	94.2	
Creditor days	31.8	31.8	31.8	31.8	
Asset Turnover	1.1	1.0	1.1	1.1	
EBITDA conversion Rate	121.0	92.1	67.1	72.0	
Return Ratios (%)					
RoE	13.0	15.5	15.5	15.4	
RoCE	9.6	17.5	19.3	19.5	
RoIC	11.5	24.4	27.1	28.3	
Valuation Ratios (x)					
P/E	41.2	29.8	25.8	22.6	
EV / EBITDA	33.6	18.3	15.1	13.1	
EV / Revenues	4.7	4.3	3.6	3.2	
Market Cap / Revenues	4.7	4.3	3.8	3.4	
Price to Book Value	5.3	4.6	4.0	3.5	
Solvency Ratios					
Debt / Equity	0.1	0.1	0.0	0.0	
Debt / EBITDA	0.9	0.2	0.2	0.2	
Current Ratio	2.0	1.9	2.0	2.1	

Source: ICICI Direct Research

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Hold: -5% to 15%;

Reduce: -5% to -15%;

Sell: <-15%



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