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GOVERNMENT OF INDIA
भारत सरकार

Business Standard, Delhi
Tuesday 2nd June 2015, Page: 16
Width: 8.07 cms, Height: 22.82 cms, a4, Ref: pmin.2015-06-02.28.69

Cipla: Higher costs offset strong revenue show

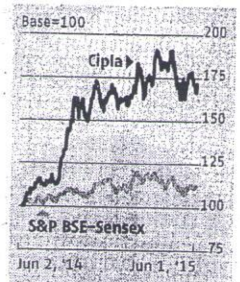
Management's conservative forecast makes analysts cautious

UJJVAL JAUHARI

On a day when major pharmaceuticals stocks ended in the red, Cipla made gains of 1.8 per cent to ₹662, on the back of strong revenue growth in the March quarter. However, analysts maintain a cautious stance on the stock, given a conservative growth forecast by the management. The company has said it expects 100-150 bps improvement in margins and sales growth in the mid-teens, which analysts say are on the lower side.

Growth in the domestic market, which contributes 36 per cent to sales, at 20.7 per cent, has outperformed the domestic sector growth of 12 per cent. The respiratory, cardiovascular, gastrointestinal and anti-infective portfolio continues to do well and momentum is expected to continue.

Exports grew 25 per cent, with the strategy of having own front-end operations yielding results. However, this has a bearing on margins, given the higher fixed costs. Nevertheless, in this backdrop and also the fact there were no one-off benefits seen a year ago (supply of Dymista nasal spray), margin improvement by about 30 bps to 16.4 per cent is positive. In store are benefits from supply of gastric drug Nexium to Teva, both on revenue and margins, starting in the current (June) quarter. With other contenders for generic launch of Nexium are unlikely to get approvals or launch before the second half of FY16, Cipla is likely to reap the benefits for at least one quarter.



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Analysts still see the benefits on margins to be partly offset by increased costs. Analysts at HSBC believe Cipla remains conservative, as they forecast higher sales growth and build in continued higher expenses, although staff costs are expected to moderate. On margins, analysts indicate 200 basis points improvement in FY16.

The respiratory opportunities, especially for the US, will depend on approvals and might not come soon, though some analysts expect faster approvals. Europe is unfolding well and approval of generic Seretide inhaler in the UK is a big catalyst in the near medium term, feel analysts. Surajit Pal at Prabhudas Lilladher expects better traction in respiratory sales in Germany, along with new approvals in UK and the US in FY16. Pal has a target price of ₹781. However, others such as Barclays Research are more circumspect due to near-term margin concerns. They peg target price at ₹655. Most analysts hold this view, as the consensus target price, according to Bloomberg, stands at ₹665.

Company