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Cipla - Margin Improvement - A Healthy Sign.

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Abstracts

We reiterate our Market Perform rating on CIPLA after its Q1 FY12 result that was lower than our sales expectations, but higher than our earnings estimate owing to the sharp improvement in gross margin. The improvement in gross margin (up by 330 bps, Y-o-Y) is largely due to the commissioning of the Indore facility operating at a breakeven level this quarter. The muted sales growth at 7.5% was partly due to the decline in sales from ARV.

Although we continue believe that CIPLA's structural issues are yet not over, we expect drastic upside in the near term owing to (1) $100m of EBITDA from supply of API of generic Zyprexa to Teva under 180-day exclusivity and (2) improvement in margin as contribution from Indore facility increases. For the longer term, CIPLA's traditional business model with back ended focus in regulated markets remains a major bottleneck.

We keep our estimates unchanged and reiterate our Positive Investment Alert on CIPLA. Our target price remains at Rs.306.

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