

Lupin

Performance Highlights

Y/E March (₹ cr)	1QFY2016	4QFY2015	% chg qoq	1QFY2015	% chg yoy
Net sales	3,074	3,054	0.7	3,284	(6.4)
Other income	152	41	266.8	85	78.0
Operating profit	745	766	(2.7)	1,058	(29.6)
Interest	2	3	(4.0)	3	(7.7)
Net profit	526	547	(4.0)	624	(15.8)

Source: Company, Angel Research

Lupin announced lower-than-expected numbers for 1QFY2016. Its sales for the quarter dipped by 6.4% yoy to ₹3,074cr V/s an expected ₹3,600cr. Overall formulations posted a sales dip of 8.0% yoy to ₹2,748.6cr and APIs posted an 11% yoy growth to ₹325.7cr. On the operating front, the gross margin came in at 68.0% V/s an expected 65.5% and V/s 67.9% in the corresponding previous year period. EBITDA margin came in at 24.2% V/s an expected 27.0% and V/s 32.2% in 1QFY2015. Consequently, the PAT came in at ₹525.5cr V/s an expected ₹749cr and V/s ₹624cr in 1QFY2015, ie a decline of 15.8% yoy. **We are Neutral on the stock, given the valuations.**

Below expectation numbers: Lupin's sales for the quarter dipped by 6.4% yoy to ₹3,074cr V/s an expected ₹3,600cr. Overall formulations posted a sales dip of 8.0% yoy to ₹2,748.6cr and APIs posted an 11% yoy growth to ₹325.7cr. Formulation sales dipped as US posted a decline of 26% yoy to ₹1,109.6cr, owing to the base impact and on account of a few launches during the quarter. On the operating front, the gross margin came in at 68.0% V/s an expected 65.5% and V/s 67.9% in the corresponding previous year period. EBITDA margin came in at 24.2% V/s an expected 27.0% and V/s 32.2% in 1QFY2015. The decline in EBITDA margin is mainly owing to lower sales and higher R&D expenditure. During the quarter, R&D expenditure as a percentage of sales rose to 10.2% V/s 7.4% in 1QFY2015. Consequently, the PAT came in at ₹525.5cr V/s an expected ₹749cr and V/s ₹624cr in 1QFY2015, ie a yoy de-growth of 15.8%.

Outlook and valuation: We expect Lupin to post a CAGR of 9.5% in net sales to ₹15,110cr and earnings to report a 9.7% CAGR to ₹64.3/share over FY2015–17E. Currently, the stock is trading at 32.1x and 25.2 its FY2016E and FY2017E earnings, respectively. **We remain Neutral on the stock.**

Key financials (Consolidated)

Y/E March (₹ cr)	FY2014	FY2015	FY2016E	FY2017E
Net sales	11,087	12,600	13,092	15,110
% chg	17.2	13.6	3.9	15.4
Net profit	1,836	2,403	2,266	2,891
% chg	39.7	30.9	-5.7	27.6
EPS (₹)	41.0	53.5	50.4	64.3
EBITDA margin (%)	25.3	27.4	25.0	27.9
P/E (x)	39.5	30.3	32.1	25.2
RoE (%)	30.3	30.4	22.8	23.4
RoCE (%)	34.7	34.3	26.1	27.9
P/BV (x)	10.5	8.2	6.6	5.3
EV/sales (x)	6.5	5.7	5.4	4.5
EV/EBITDA (x)	25.7	20.8	21.5	16.2

Source: Company, Angel Research; Note: CMP as of July 27, 2015

NEUTRAL

CMP ₹1,618
Target Price -

Investment Period -

Stock Info

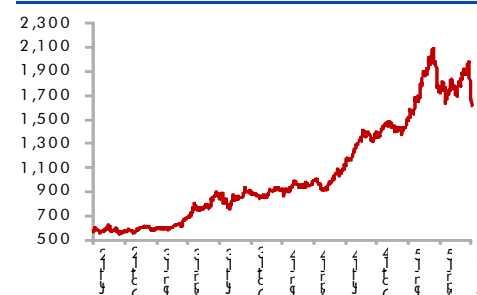
Sector	Pharmaceutical
Market Cap (₹ cr)	72,771
Net Debt (₹ cr)	(629)
Beta	0.7
52 Week High / Low	2,112 / 1,113
Avg. Daily Volume	78,879
Face Value (₹)	2
BSE Sensex	27,561
Nifty	8,361
Reuters Code	LUPN.BO
Bloomberg Code	LPC@IN

Shareholding Pattern (%)

Promoters	46.6
MF / Banks / Indian Fls	7.9
FII / NRIs / OCBs	37.2
Indian Public / Others	8.3

Abs. (%)	3m	1yr	3yr
Sensex	1.4	5.5	63.7
Lupin	(6.1)	43.3	185.6

3-year price chart



Source: Company, Angel Research

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Exhibit 1: 1QFY2016 – Consolidated performance

Y/E March (₹ cr)	1QFY2016	4QFY2015	% chg (qoq)	1QFY2015	% chg (yoy)	FY2015	FY2014	% chg (yoy)
Net sales	3,074	3,054	0.7	3,284	(6.4)	12,529	11,087	13.0
Other income	152	41	266.8	85	78.0	445	316	40.7
Total income	3,226	3,096	4.2	3,369	(4.3)	12,974	11,403	13.8
Gross profit	2,091	2,098	(0.3)	2,230		8,412	7,269	15.7
Gross margin	68.0	68.7		67.9		67.1	65.6	
Operating profit	744.5	765.5	(2.7)	1,058	(29.6)	3,344	2,803.0	19.3
OPM (%)	24.2	25.1		32.2		26.7	25.3	
Interest	2	3	(4.0)	3	(7.7)	10	27	(64.3)
Dep. & amortisation	101	107	(6.0)	109	(7.3)	425	261	62.9
PBT	793	697	13.7	1,032	(23.2)	3,354	2,832	18.4
Provision for taxation	264	136	94.0	403	(34.4)	996	962	3.6
Reported net profit	529	561	(5.8)	629	(16.0)	2,358	1,870	26.1
Less : exceptional items	-	-		-		-	-	
MI & share in associates	3	14	(78.1)	5	(38.8)	31	33	(6.2)
PAT after exceptional items	526	547	(4.0)	624	(15.8)	2,327	1,837	26.7
EPS (₹)	11.7	12.2		13.9		51.9	41.0	

Source: Company, Angel Research

Exhibit 2: 1QFY2016 – Actual vs Angel estimates

₹ cr	Actual	Estimates	Variation
Net Sales	3,074	3,600	(14.6)
Other Income	152	85	78.0
Operating Profit	745	972	(23.4)
Depreciation	101	107	(6.0)
Tax	264	185	43.2
Net Profit	526	749	(29.8)

Source: Company, Angel Research

Revenue dips 6.4% yoy: Lupin's sales for the quarter dipped by 6.4% yoy to ₹3,074cr V/s an expected ₹3,600cr. Overall formulations posted a sales dip of 8.0% yoy to ₹2,748.6cr and APIs posted an 11% yoy growth to ₹325.7cr.

Formulation sales dipped as US posted a decline of 26% yoy to ₹1,109.6cr, owing to the base impact and on account of a few launches during the quarter. Another export destination – Japan, posted a yoy dip of 5.0% to ₹323.1cr, mainly on back of the currency impact. Sales in JPY terms grew 6% yoy to JPY6,178mn during the quarter. Lupin's sales in Europe (₹85.6cr) and India (₹885.1cr) posted a yoy growth of 21% and 16%, respectively. ROW (₹182.6cr) posted a strong growth of 44% in 1QFY2016.

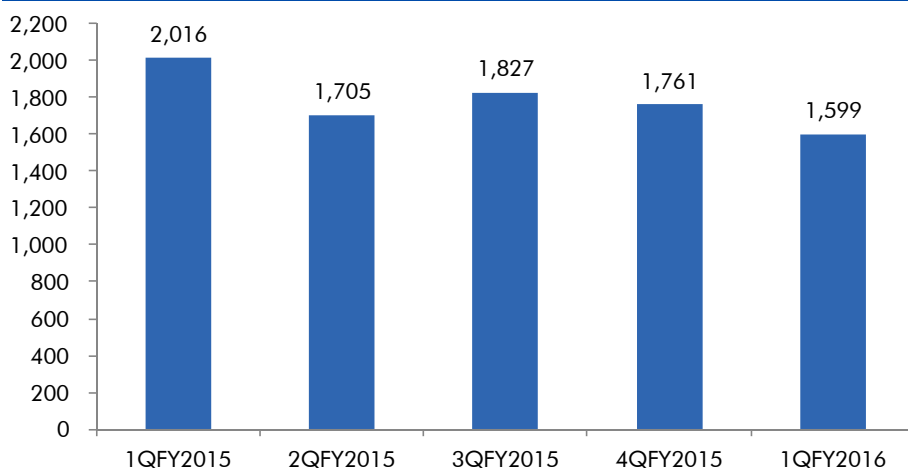
Formulations posted a dip of 8.0% (~89% of sales), while API grew by 11.0% yoy (~11% of sales).

Lupin's Japan sales (Kyowa + I'rom) de-grew by 5.4% yoy, clocking net sales of ₹323.1cr for the quarter. Total revenues increased to JPY6,178mn in 1QFY2016, up from JPY5,823mn in 1QFY2015, a yoy growth of 6% in JPY terms. For the quarter, Kyowa revenues (excluding I'rom) de-grew by 5.9% yoy to ₹248.3cr from ₹264.0cr in 1QFY2015. In JPY terms, Kyowa revenues grew by 5% yoy to JPY4,747mn from JPY4,502mn in 1QFY2015.

Pharma Dynamics clocked in revenues of ₹81.6cr during 1QFY2016, a de-growth of 6.1% yoy, while growing by 2% in ZAR terms to end the quarter at ZAR155mn. The company remains the fastest growing and the 4th largest generic company in the South African market with clear leadership in the cardiovascular space.

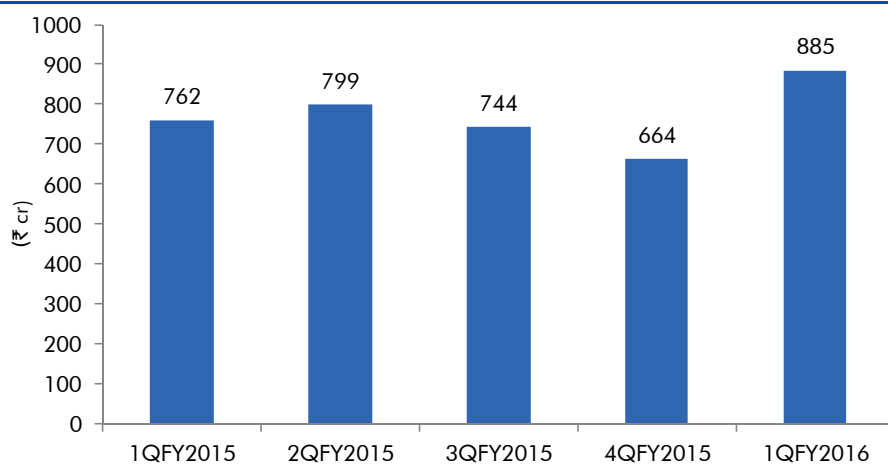
On the regulatory front, Lupin received 6 approvals from the USFDA during the quarter. Cumulative ANDA filings with the USFDA as of June 30, 2015 stood at 215 (35 FTFs) with the company having received 117 approvals to date.

Exhibit 3: Advanced markets – Sales trend



Source: Company, Angel Research

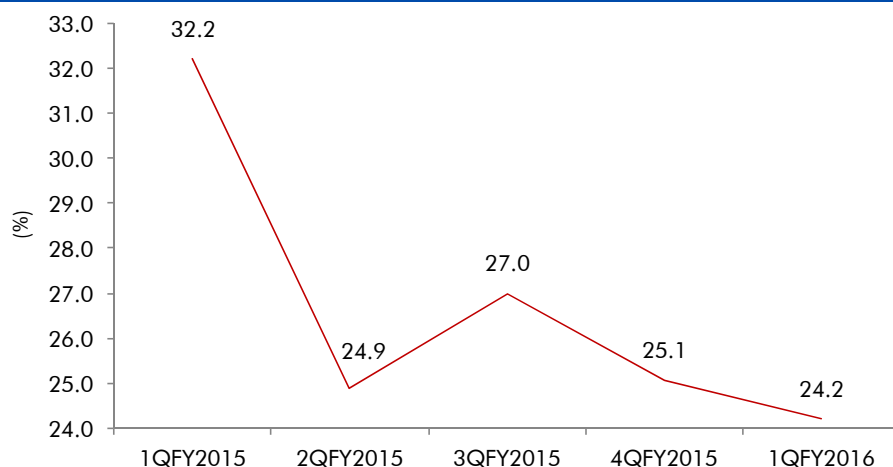
Exhibit 4: Domestic Formulation Market



Source: Company

OPM lower than expectation at 24.2%: On the operating front, the gross margins came in at 68.0% V/s an expected 65.5% and V/s 67.9% in the corresponding previous year period. EBITDA margin came in at 24.2% V/s an expected 27.0% and V/s 32.2% in 1QFY2015. This was mainly on account of lower sales, and higher R&D expenditure as a percentage of sales which rose to 10.2% in 1QFY2016 V/s 7.4% in 1QFY2015.

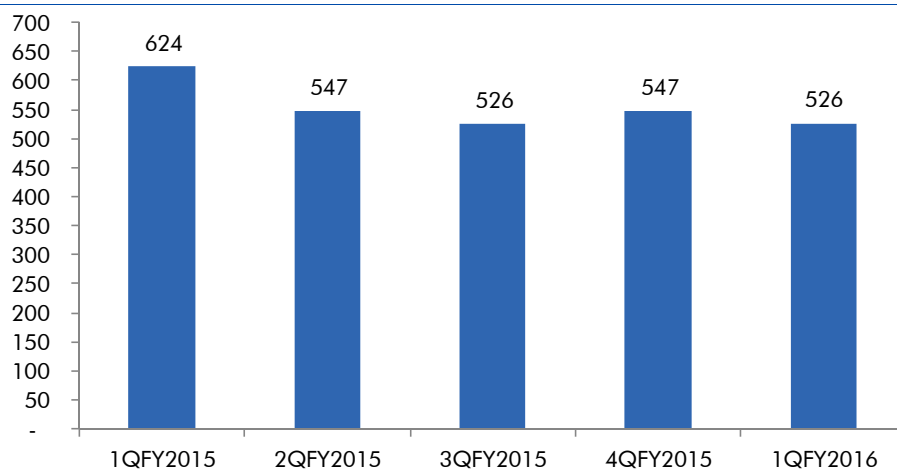
Exhibit 5: OPM trend



Source: Company, Angel Research

Net profit growth lower than our estimate: The other income during the quarter rose to ₹151.1cr V/s 85.1cr in 1QFY2015. Also, tax as a percentage of PBT rose by 33.3% V/s 39.0% in 1QFY2015. Consequently, the PAT came in at ₹525.5cr V/s an expected ₹749cr and V/s ₹624cr in 1QFY2015, ie a yoy de-growth of 15.8%.

Exhibit 6: Net profit trends



Source: Company, Angel Research

Conference call takeaways

- The Management expects the domestic formulation business to grow higher than the industry growth rate in FY2016.
- Overall, we believe FY2016 would be a year of consolidation for Lupin with the organic and inorganic initiatives for Lupin likely to kick start earnings only from FY2017 onwards.
- Also, the company entered into a definitive agreement to acquire privately held GAVIS Pharmaceuticals LLC and Novel Laboratories Inc (GAVIS), subject to certain closing conditions, in a transaction valued at US\$880mn, cash free and debt free. The acquisition enhances Lupin’s scale in the US generic

market and also broadens Lupin's pipeline in dermatology, controlled substance products and other high-value and niche generics. New Jersey based GAVIS is a privately held company specializing in formulation development, manufacturing, packaging, sales, marketing, and distribution of pharmaceuticals products. GAVIS recorded sales of US\$96mn in FY2014 (coming from around 20 products) and has over 250 New Jersey based employees.

- The acquisition looks very costly, coming in at 9.2x Market Cap/Sales, given the size of the company, though funding will not be a problem given that the company has very little debt on its books.

Recommendation rationale

- **US market – the key driver:** The high-margin branded generic business has been the key differentiator for Lupin in the Indian pharmaceuticals space. On the generic turf, Lupin is currently the fifth largest generic player in the US, with 5.3% market share in prescription. Lupin is now the market leader in 28 products marketed in the US generics market and is amongst the Top 3 by market share in 55 products.

Currently, the company's cumulative filings stand at 215, of which 117 have been approved, with 35 FTFs valued at more than US\$13bn. Lupin plans to launch 15-20 products in the US in FY2017. Another driver, the OC segment, is expected to contribute US\$100mn to the company's top-line over the next 2-3 years. Another significant portion of the company's US business, Branded segment which is around ~10% of its US sales (FY2015), is expected to increase to 30% of sales by FY2018, through acquisitions. We expect the region to post a CAGR of 7.9% during FY2015-17.

- **Domestic formulations on a strong footing:** Lupin continues to make strides in the Indian market. Currently, Lupin ranks No 3, and is the fastest growing company among the top five companies in the domestic formulation space, registering a strong CAGR of 20.0% over the last few years. Six of Lupin's products are among the top 300 brands in the country. Lupin introduced 54 new products in the Indian market in FY2014 and has a strong field force of ~5,400MRs (as of FY2015). We expect the domestic formulation market to grow at a CAGR of 16.0% over FY2015-17E.
- **First-mover advantage in Japan:** Lupin figures among the few Indian companies with a formidable presence in the world's second largest pharma market (ranked as the 8th largest as per IMS MAT March 2014). The Management believes there will be patent expiries (US\$14-16bn) in the next two years in the Japanese market, which along with increased generic penetration, would drive growth in the market. For FY2015, the market posted a moderate growth after a dip in FY2014; however going forward the company expects a healthy growth, with double digit growth (15% in constant currency) in the Kyowa business and a single digit growth in the I'rom business. The Management expects improvement in growth in the next 3-4 years. On a conservative basis, we expect the market to post a CAGR of 9.5% over FY2015-17E.

Valuation

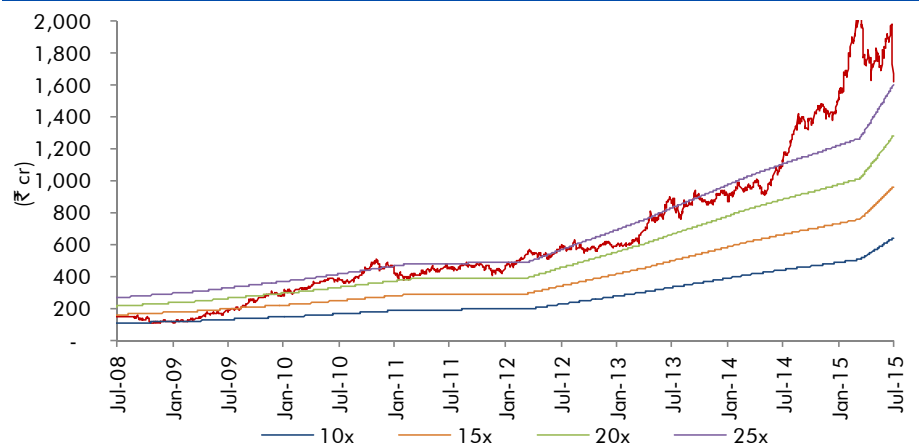
We expect Lupin to post a CAGR of 9.5% in net sales to ₹15,110cr and earnings to report a 9.5% CAGR to ₹64.3/share over FY2015–17E. Currently, the stock is trading at 32.1x and 25.2x FY2016E and FY2017E earnings, respectively. **We remain Neutral on the stock.**

Exhibit 7: Key Assumptions

	FY2016E	FY2017E
Sales growth (%)	18.0	16.0
Domestic growth (%)	16.0	16.0
Exports growth (%)	4.5	15.4
Operating margins (%)	25.0	27.9
R&D Exp (% of sales)	10.0	10.0
Capex (₹ cr)	1000	1000

Source: Company, Angel Research

Exhibit 8: One-year forward PE



Source: Company, Angel Research

Exhibit 9: Recommendation summary

Company	Reco	CMP (₹)	Tgt. price (₹)	Upside (%)	FY2017E			FY15-17E		FY2017E
					PE (x)	EV/Sales (x)	EV/EBITDA (x)	CAGR in EPS (%)	RoCE (%)	RoE (%)
Alembic Pharma.	Neutral	740	-	-	33.6	4.8	23.7	21.1	30.6	30.9
Aurobindo Pharma	Accumulate	739	824	11.5	17.9	2.8	12.6	14.1	22.5	29.2
Cadila Healthcare	Neutral	1,915	-	-	23.6	3.3	16.5	19.6	22.8	27.3
Cipla	Neutral	675	-	-	23.4	3.2	17.2	21.2	16.9	16.9
Dr Reddy's	Neutral	3,856	-	-	21.4	3.1	14.1	18.6	21.1	20.5
Dishman Pharma	Buy	181	254	40.0	8.4	0.8	4.0	42.8	14.8	14.3
GSK Pharma*	Neutral	3,383	-	-	57.7	9.0	47.8	2.5	30.7	32.2
Indoco Remedies	Neutral	360	-	-	23.2	2.7	14.7	31.4	20.1	21.1
Ipca labs	Accumulate	696	736	6.1	19.9	2.3	11.9	31.5	14.0	15.9
Lupin	Neutral	1,618	-	-	25.2	4.5	16.2	9.7	27.9	23.4
Sanofi India*	Neutral	3,782	-	-	28.2	3.1	18.5	25.1	22.0	22.5
Sun Pharma	Buy	824	950	15.3	30.6	5.1	17.1	10.7	14.3	14.6
Alembic Pharma.	Neutral	740	-	-	33.6	4.8	23.7	21.1	30.6	30.9

Source: Company, Angel Research; Note: * December year ending

Company Background

Lupin, established in 1968, is primarily engaged in the manufacture and global distribution of active pharmaceutical ingredients (APIs) and finished dosages. Over the years, the company forayed into US markets through a differentiated export strategy of tapping branded generics and consequently gaining a large share of the US prescription market. Further, to expand its foot-print in the global market, Lupin has prudently adopted the inorganic growth route. In line with this, over the last two years, the company made small acquisitions across geographies, prominent among these being the acquisition of Kyowa in the growing Japanese market.

Profit & Loss Statement (Consolidated)

Y/E March (₹ cr)	FY2012	FY2013	FY2014	FY2015	FY2016E	FY2017E
Gross sales	7,002	9,524	11,167	12,684	13,171	15,202
Less: Excise duty	42	62	80	84	79	91
Net sales	6,960	9,462	11,087	12,600	13,092	15,110
Other operating income	123	180	200	170	170	170
Total operating income	7,083	9,641	11,287	12,770	13,262	15,281
% chg	21.4	36.1	17.1	13.1	3.9	15.2
Total expenditure	5,638	7,371	8,284	9,150	9,819	10,890
Net raw materials	2,604	3,548	3,817	4,157	4,189	4,835
Other mfg costs	906	757	887	1,008	1,047	1,209
Personnel	970	1,249	1,465	1,747	2,053	1,964
Other	1,159	1,818	2,115	2,238	2,529	2,882
EBITDA	1,322	2,090	2,803	3,449	3,273	4,220
% chg	24.0	58.2	34.1	23.1	(5.1)	28.9
(% of Net Sales)	19.0	22.1	25.3	27.4	25.0	27.9
Depreciation & amortisation	228	332	261	435	468	548
EBIT	1,094	1,758	2,542	3,015	2,805	3,672
% chg	22.3	60.7	44.6	18.6	-7.0	30.9
(% of Net Sales)	15.7	18.6	22.9	23.9	21.4	24.3
Interest & other charges	35	41	27	10	10	10
Other Income	14	28	116	240	240	240
(% of PBT)	1	1	4	7	7	6
Share in profit of associates	-	-	-	-	-	-
Recurring PBT	1,196	1,925	2,832	3,415	3,205	4,072
% chg	20.0	60.9	47.1	20.6	-6.1	27.1
Extraordinary expense/(Inc.)	-	-	-	-	-	-
PBT (reported)	1,196	1,925	2,832	3,415	3,205	4,072
Tax	309	584	962	970	897	1,140
(% of PBT)	25.8	30.4	34.0	28.4	28.0	28.0
PAT (reported)	888	1,340	1,870	2,444	2,307	2,932
Add: Share of earnings of asso.	-	-	-	-	-	-
Less: Minority interest (MI)	20	26	33	41	41	41
Prior period items	-	-	-	-	-	-
PAT after MI (reported)	868	1,314	1,836	2,403	2,266	2,891
ADJ. PAT	868	1,314	1,836	2,403	2,266	2,891
% chg	0.6	51.5	39.7	30.9	(5.7)	27.6
(% of Net Sales)	12.5	13.9	16.6	19.1	17.3	19.1
Basic EPS (₹)	19.4	29.4	41.0	53.5	50.4	64.3
Fully Diluted EPS (₹)	19.4	29.4	41.0	53.5	50.4	64.3
% chg	0.6	51.0	39.5	30.5	(5.7)	27.6

Balance Sheet (Consolidated)

Y/E March (₹ cr)	FY2012	FY2013	FY2014	FY2015	FY2016E	FY2017E
SOURCES OF FUNDS						
Equity share capital	89	90	90	90	90	90
Reserves & surplus	3,924	5,115	6,842	8,784	10,882	13,605
Shareholders funds	4,013	5,204	6,932	8,874	10,972	13,695
Minority interest	72	59	67	24	65	106
Total loans	1,640	1,164	553	471	471	471
Other Long-Term Liabilities	73	50	46	74	75	76
Long-Term Provisions	67	112	132	132	69	70
Deferred tax liability	144	163	178	118	118	118
Total liabilities	6,010	6,754	7,908	9,693	11,771	14,536
APPLICATION OF FUNDS						
Gross block	3,627	4,114	4,564	5,355	6,355	7,355
Less: Acc. depreciation	1,442	1,684	1,928	2,363	2,831	3,380
Net block	2,185	2,430	2,635	2,992	3,524	3,975
Capital work-in-progress	444	311	304	304	304	304
Goodwill	564	570	720	1,648	1,648	1,648
Investments	3	2	178	1,658	1,658	1,658
Long-Term Loans and Adv.	394	387	373	275	284	328
Current assets	4,297	5,143	5,924	6,176	7,844	10,652
Cash	402	435	798	1,306	2,783	4,811
Loans & advances	309	340	302	671	697	805
Other	3,586	3,154	4,825	4,199	4,364	5,036
Current liabilities	1,878	2,089	2,227	3,360	3,491	4,030
Net current assets	2,420	3,054	3,697	2,816	4,352	6,622
Mis. Exp. not written off	-	-	-	-	-	-
Total assets	6,010	6,754	7,908	9,693	11,771	14,536

Cash Flow Statement (Consolidated)

Y/E March (₹ cr)	FY2012	FY2013	FY2014	FY2015	FY2016E	FY2017E
Profit before tax	1,196	1,925	2,832	3,415	3,205	4,072
Depreciation	228	332	261	435	468	548
(Inc)/Dec in working capital	(724)	620	(1,481)	1,487	(69)	(286)
Direct taxes paid	(309)	(584)	(962)	(970)	(897)	(1,140)
Cash Flow from Operations	391	2,293	649	4,367	2,707	3,195
(Inc.)/Dec.in Fixed Assets	(997)	(353)	(443)	(791)	(1,000)	(1,000)
(Inc.)/Dec. in Investments	-	-	-	-	-	-
Cash Flow from Investing	(997)	(353)	(443)	(791)	(1,000)	(1,000)
Issue of equity	-	-	-	-	-	-
Inc./Dec.) in loans	550	(476)	(611)	(82)	0	-
Dividend Paid (Incl. Tax)	(165)	(209)	(157)	(168)	(168)	(168)
Others	204	499	(795)	(2,816)	(62)	2
Cash Flow from Financing	589	(186)	(1,564)	(3,067)	(230)	(166)
Inc./Dec.) in Cash	(18)	1,753	(1,358)	509	1,477	2,028
Opening Cash balances	420	402	435	798	1,306	2,783
Closing Cash balances	402	435	798	1,306	2,783	4,811

Key Ratios

Y/E March (₹ cr)	FY2012	FY2013	FY2014	FY2015	FY2016E	FY2017E
Valuation Ratio (x)						
P/E (on FDEPS)	83.2	55.1	39.5	30.3	32.1	25.2
P/CEPS	65.9	44.0	34.6	25.6	26.6	21.1
P/BV	18.0	13.9	10.5	8.2	6.6	5.3
Dividend yield (%)	0.2	0.2	0.2	0.2	0.2	0.2
EV/Sales	10.5	7.7	6.5	5.7	5.4	4.5
EV/EBITDA	55.4	34.9	25.7	20.8	21.5	16.2
EV / Total Assets	12.2	10.8	9.1	7.4	6.0	4.7
Per Share Data (₹)						
EPS (Basic)	19.4	29.4	41.0	53.5	50.4	64.3
EPS (fully diluted)	19.4	29.4	41.0	53.5	50.4	64.3
Cash EPS	24.5	36.8	46.8	63.1	60.8	76.5
DPS	3.4	4.0	4.0	4.0	4.0	4.0
Book Value	89.9	116.3	154.6	197.4	244.1	304.7
Dupont Analysis						
EBIT margin	15.7	18.6	22.9	23.9	21.4	24.3
Tax retention ratio	74.2	69.6	66.0	71.6	72.0	72.0
Asset turnover (x)	1.4	1.6	1.7	1.6	1.5	1.6
ROIC (Post-tax)	16.8	20.9	25.4	28.2	23.5	28.6
Cost of Debt (Post Tax)	1.9	2.0	2.0	1.4	1.5	1.5
Leverage (x)	0.3	0.0	0.0	0.0	0.0	0.0
Operating ROE	20.6	20.9	25.4	28.2	23.5	28.6
Returns (%)						
ROCE (Pre-tax)	20.5	27.5	34.7	34.3	26.1	27.9
Angel ROIC (Pre-tax)	27.5	35.0	44.1	48.2	41.6	49.6
ROE	23.8	28.5	30.3	30.4	22.8	23.4
Turnover ratios (x)						
Asset Turnover (Gross Block)	2.3	2.5	2.6	2.6	2.3	2.2
Inventory / Sales (days)	76	70	66	62	69	80
Receivables (days)	77	75	75	66	74	85
Payables (days)	156	72	84	78	89	89
WC cycle (ex-cash) (days)	87	88	89	63	42	40
Solvency ratios (x)						
Net debt to equity	0.3	0.1	(0.0)	(0.1)	(0.2)	(0.3)
Net debt to EBITDA	0.9	0.3	(0.1)	(0.2)	(0.7)	(1.0)
Interest Coverage	30.8	42.9	95.4	307.3	285.9	374.3

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Disclosure of Interest Statement	Lupin
1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

Note: We have not considered any Exposure below ₹1 lakh for Angel, its Group companies and Directors

Ratings (Based on expected returns over 12 months investment period):	Buy (> 15%)	Accumulate (5% to 15%) Reduce (-5% to -15%)	Neutral (-5 to 5%) Sell (< -15)
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