

October 9, 2017

PICK OF THE MONTH

VOL-3, NO-18

Cupid Limited

BUY

CMP: Rs.286

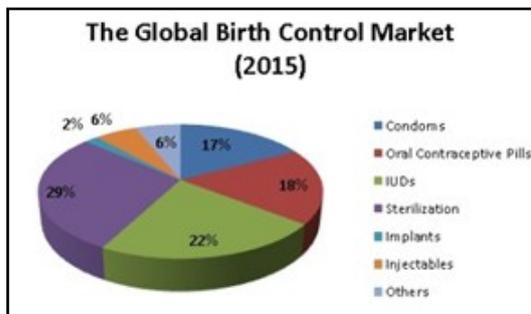
TARGET PRICE: Rs.340

TIME : 12 months

**OVERVIEW: Industry:
Contraception market:**

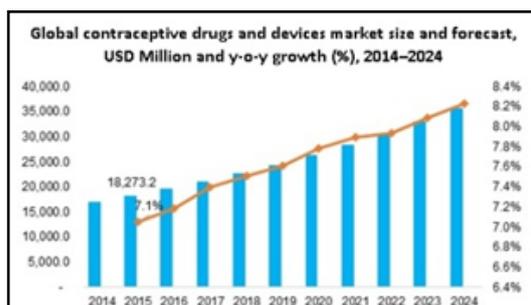
Contraception is an effective means of preventing pregnancy (by contraceptive methods), one of the apt ways to limit the size of the family. Thus, it is fair enough to say, that contraceptives segment represents a billion dollar market. The percentage of women using contraceptive methods has been increasing in the developed as well as developing countries. Many of the female contraceptives (especially the hormonal ones) which are readily available are also known to accompany higher costs and side-effects. Some of the side effects include nausea, weight gain and mood changes. Male contraceptives related to hormones are very hard to find in the existing market. Many pharmaceutical companies are reluctant to invest into male contraceptives. In order to mitigate the risk of side effects on the health of individuals; hormonal and non-hormonal, both the options may be used or advised.

Contraception options may have effects which are long term or short term. Some of the long acting options include the use of tubal ligation and fallopian tube inserts (permanent sterilization, effective rate 99.5%); intrauterine contraceptive devices (IUD) and hormonal implants. The effectiveness of these long lasting contraceptive options lasts for 3-10 years. Some of the short acting options include condoms, diaphragms, caps, spermicides, hormonal pills, hormonal patch etc. When one talks about the usage of condom as a measure to be used, some of the factors that will lead to increase in the usage include family planning, increase in unplanned pregnancy, increase in teen pregnancy, increasing investments in women's health and increase in awareness about topical contraceptives. As per some market research reports; globally there is huge demand for female condoms and it is expected to grow three times over the next five years. With increasing female literacy and growing women empowerment worldwide, the female condom product is expected to see a substantial uptick in sales.



Source: Transparency Market Research, Bloomberg

As per the recent annual report of Cupid limited (FY16-17), the usage of the condom is projected to reach nearly 44.7bn pieces by 2021 as compared to 26.5bn pieces in 2015. This converts the usage of condoms, which was at USD5.96bn in 2015 to be projected to reach USD9.55bn by 2021, growing at a CAGR of 9.12% during the forecast period (Report of Beige Market Intelligence on Global Condom Market).



Source: Coherent market insights analysis (2016)

SNAPSHOT				
52 week H / L	Mcap (INR mn)			
374 / 256	3178			
Face value: 10				
BSE Code	NSE CODE			
530843	CUPID			
Annual Performance				
(Rs mn)	FY15	FY16	FY17	FY18E
Sales (Net)	444	611	829	1037
EBITDA	128	253	323	384
EBITDA (%)	28.9	41.4	39.0	37.0
Other Income	7	17	23	25
Interest	3	2	1	1
Depreciation	18	19	21	22
PBT	114	248	324	385
PAT	77	159	205	260
Equity	111	111	111	111
EPS (INR)	7	14	18	23
Quarterly Performance				
Parameters (Rs mn)	Sept-16	Dec-16	Mar-17	Jun-17
Sales (Net)	215	284	185	197
EBITDA	85	109	82	74
EBITDA (%)	39	38	44	37
Other Income	6	0	0	0
Interest	0	0	0	1
Depreciation	5	5	5	5
PAT	54	64	49	43
Equity (Rs mn)	11	11	11	11
Ratio Analysis				
Parameters (Rs mn)	FY15	FY16	FY17	FY18E
EV/EBITDA (x)	24.7	12.2	9.2	7.8
EV/Net Sales (x)	7.1	5.1	3.6	2.9
M Cap/Sales (x)	7.2	5.2	3.8	3.1
M Cap/EBITDA (x)	24.8	12.6	9.8	8.3
Debt/Equity (x)	0.2	0.1	0.0	0.0
ROCE (%)	51	78	71	63
Price/Book Value (x)	13.1	8.8	6.2	4.7
P/E (x)	41.2	20.0	15.4	12.2
Share Holding Pattern as on 30th September 2017				
Parameters	No of Shares	%		
Promoters	4,986,800	44.9		
Institutions	475,187	4.3		
Public	5,653,013	50.9		
TOTAL	11,115,000	100.0		

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TIME : 12 months

OVERVIEW: Industry (contd.)

India is the second most populous nation in the world. With such a vast population, the fear for many lethal viral diseases arises; one of which is HIV. As per the research by United Nations, India ranks third in terms of number of people living with HIV in the world, where, HIV treatment coverage is only 36%, 51% of deaths occur due to AIDS and nearly 64% of Indians do not have access to antiretroviral treatment and drugs.

India is ranked number one as far as the process of sterilization of women is concerned. A large number of sterilization camps are organized across the nation, however, the question relates to safe and sanitary procedures used. For many, sterilization is also seen as a solution to curb population growth.

Some more factors which will brighten the expected growth in the contraceptive segment include:

- Increased usage of social media and social networking is seen as a very important tool for spreading awareness about the use of modern contraceptives, where the target audience is the youth and initiatives are to directly target the risk of unintended pregnancies.
- Many women are delaying pregnancies deliberately due to factors like focus on career, economic pressure etc. As a result of which the birth rates have declined among women in their 20s but increased among those aged between 30 and 44 years.
- According to WHO, everyday more than 1 million people across the globe are getting affected by sexually transmitted infections (STIs). In order to curb this issue, the growth of the contraceptive market is bound to happen.
- Where sterilization is the most effective route to prevent pregnancy (99.9%), contraceptive pills show an effective rate of nearly 97%. Contraceptive pills are very effective against unplanned pregnancy if used correctly.
- There are a large number of initiatives by the local governments to spread awareness as well.

Lubricant Market:

In the current market scenario for lubricants (sexual), water-based lubricant segment is the dominant segment. They have a wide customer base and are very popular amongst the end users. However, in times to come, silicone-based segment and the hybrid segment for lubricants is anticipated to grow at a faster rate as well. Growing at CAGR of 6.7% during 2016-2022, the market is expected to cross USD1.4bn. (As per Arizton Advisory & Intelligence). Some the major factors which contribute to this growth include, increasing demand from developing nations, acceptance of products among women, increased promotional and marketing activities, visibility of these products on the online and digital platforms, introduction of certain private brands etc. There are a large number of international and regional vendors in this domain. Some of the prominent vendors include Bodywise, Reckitt Benckiser, B. Cumming, HLL Lifecare, Cupid Limited, Empowered Products, Good Clean Love, Guy & O'Neill, Hathor Professional, ID Lubricants, Innovus Pharma, Live Well Brands etc. In the tiff between the two, regional vendors will definitely find it difficult to compete with the big fishes.

About the Company:

Cupid Limited (Cupid) is one of the few companies that manufacture male and female rubber contraceptives. It is one out of the four major players in the world which manufactures female condoms. Cupid, is the second company in the world to get pre-qualification from WHO for the female condoms. In September 2016, Cupid became the first company in the world to have been pre-qualified by WHO (World Health Organization)/UNFPA (United Nations Population Fund) for supplying both male and female condoms.

The company has established its brand name as a renowned manufacturer, exporter and supplier of male condoms and female condoms across the globe. Nearly 80% of the products are exported, while only 20% are used for local distributions in India. The company has expanded exports to nearly 40 countries (FY17-18) which were nearly 32 countries (in FY16-17). Cupid was featured in Forbes Asia's 200 best under a billion list which was again a rare achievement for an Indian company. The company is chaired by Mr Omprakash Garg and its state of the art plant is located in Nasik in Maharashtra.

INVESTMENT RATIONALE

(A) Core Business:

Cupid holds the recognition of being India's first and second in the world to have a pre-qualification accredited by WHO for worldwide public distribution of female condoms. The current geographical mix for the company includes domestic market at 20% while the exports are at nearly 80%. The manufacture of rubber contraceptives is approximately 95% of the total revenues earned by the company while the manufacture of water based lubricant (Jelly) contributes nearly 5% of the revenues. The company is contemplating and exploring the possibility of establishing a manufacturing plant in Africa. This is a long term project where the majority stake would be with the African authorities, while Cupid is estimated to hold 49%. The company will be investing time and money for creating awareness and exploring opportunities in the states of Gujarat, Bihar, Jharkhand, Karnataka, Tamil Nadu etc.

Cupid was featured in Forbes Asia's 200 best under a billion list which was again a rare achievement for a company on the Indian soil. The company is rightly capitalizing the opportunity and reaping revenues from the segment of female condoms. This segment has been growing at a faster rate as compared to the segment of male condoms. The margins earned in the segment of female condoms are much higher when compared to male condoms and thus, Cupid has been successful in maintaining the overall margins in the range of around 38-42%.

INVESTMENT RATIONALE (contd.)

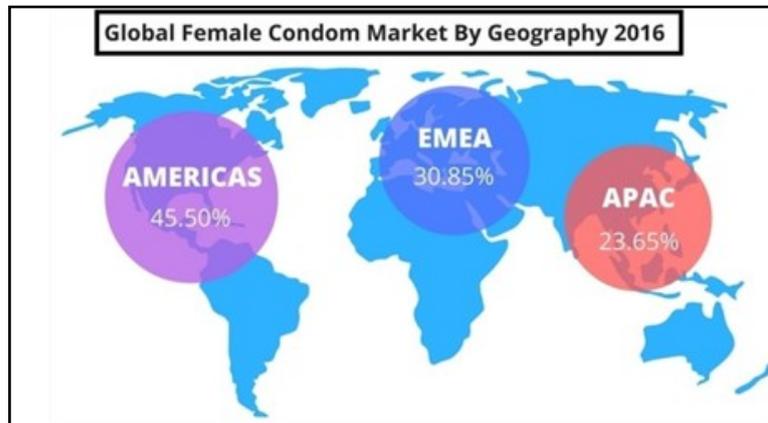
(A) Core Business (contd.)

The market of emergency contraceptive pills (ECP) will also grow going forward. However, as per market research, many of the users are skeptical about using ECP as the same leads to imbalances in the hormones. Many females prefer ECP only in case of extreme emergency. Thus, the risk of ECP overshadowing the condoms segment is very bleak. The company is working on the launch of our unique patented male condom giving extra pleasure to the user during safe sex.

In the survey conducted by Cupid Limited in Mumbai (sample size of 1000 females), some of the critical facts revealed included,

- only 36% of them were aware of female condoms
- a majority of participants aged between 18-50 believed condoms would be useful for preventing pregnancy and STDs
- for many, the most critical reasons to use condoms was to prevent unplanned and unwanted pregnancy
- around 70-74% participants purchased female condoms from a store, while 26-30% did online purchases

This clearly indicates that there is a need for awareness amongst the masses. The awareness appears to be slightly better in the cities; however, the same would not be the case in the rural parts of India and small towns. This provides a vision of the potential that the product will have if the same is promoted and marketed well. Realizing the potential of the demand and customers, Cupid has already started targeting the states of Bihar, Gujarat, Jharkhand, Karnataka and Tamil Nadu.



Source: http://mms.businesswire.com/media/20170209005066/en/568725/5/GLOBAL_FEMALE_CONDOM_MARKET.

(B) African opportunity:

The usage of condoms is going to grow on a constant rate. As per the recent annual report, the projected opportunity in the condoms market was 26.5bn pieces in 2015 which is expected to zoom to 44.7bn pieces in 2021. The demand for condoms is coming from Africa, Caribbean and CIS nations. The market size is improving as awareness about prevention of sexually transmitted infections including HIV and for prevention of unintended pregnancy is created.

Cupid is planning to launch its products in different developing countries like Brazil, Nigeria, Tanzania, Indonesia and other developing countries where there is significant demand for these products. All the countries mentioned above have a demography which is very much on the same lines where the demand for rubber contraceptives is bound to increase. The company has already initiated the process of acquiring product registration with the local authorities. The company is in the final stages of approvals in Brazil; while at the same time has initiated exploring opportunities in Tanzania. The market is not just restricted to Africa, but India too, has a huge potential market for female condoms.

(C) New Products launches:

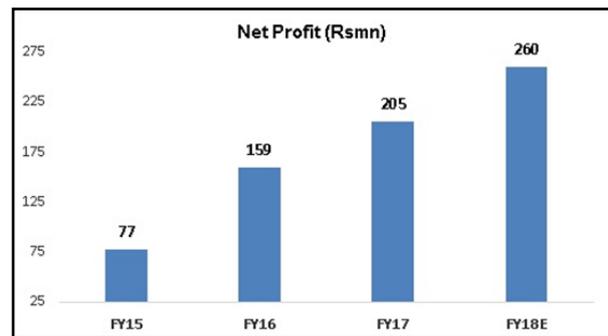
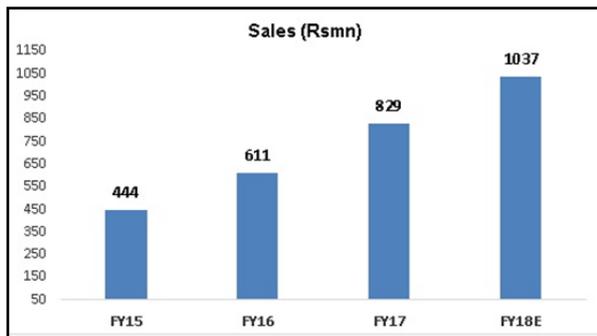
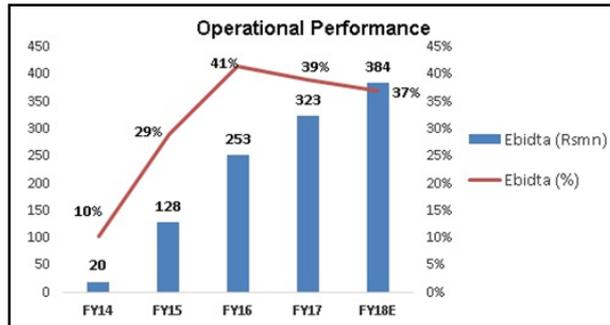
The company mainly deals in one segment i.e. male and female rubber contraceptives. However, during FY17, the company launched new product namely lubricant jelly. The product is currently not a significant contributor to the top line, but the management has ambitious plans to capitalize on the opportunity. The company has recently launched new products like hand sanitizers, vaginal creams and wipes etc. These new products fall in the comfortable margins range of 28-35%.

(D) B2C business foray:

Traditionally (in the B2B segment) the company has been catering to government and non-government organizations worldwide. The company has started taking baby steps with its plans to foray into B2C business. The same will also help provide brand recognition of Cupid and its products. Along with the brand promotion, creating awareness about the products offered and to strengthen this arm, the company has appointed nearly 50 distributors and hired an agency for sales and distribution. While the company will continue its progress on the B2B business, they will also focus on the B2C business to mitigate the risks associated to B2B business and dependence on the tenders for large orders.

Financials:

The male condoms contributed about 43% in value terms as against 52% for the female condoms and the newly launched water based lubricant jelly contributed around 5%. The company has the capability of switching the production lines between male and female condoms, as per the demand and requirement. The contract manufacturing business contributed close to 20% in overall sales. The company is debt free. Being cash rich it is looking for opportunities to be explored organically as well as inorganically. Cupid has been generous in rewarding the shareholders with incremental dividend over the last few years. Traditionally Q1 and Q4 are weaker quarters for the company while Q2 and Q3 are the stronger ones.



Source: Company

Risks and concerns:

Business continuity is one of the major concerns for the company. The CEO is still not identified, as the current management has not yet found a perfect match or an exact fit for the post; however, the company is currently run by a professional team. Since the company is a net exporter, forex fluctuation is a major concern for the company. Any fluctuations in the price of basic raw material i.e. latex rubber will affect the margins of the company. Going ahead, new competition will arise which can affect the margins to an extent; however, the same will be mitigated due to cost advantage for Cupid.

Outlook and valuations:

Cupid will continue its strategy in evaluating new growth opportunities (through organic and inorganic route). Some of the key initiatives planned by the company for the next couple of years include the launch of unique patented male condom, develop second generation hi-tech version of cupid female condom, foray into hand sanitizers, manufacture and launch vaginal creams, develop wipes that are used to slow down premature ejaculation. All these factors will help maintain growth in revenues and margins. Considering the strong growth with sound fundamentals, we recommend a Buy on the stock with a target price of Rs340 over a horizon of 12 months.

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