

IPCA Laboratories

Performance Highlights

Y/E March (₹ cr)	4QFY2016	3QFY2016	% chg (QoQ)	4QFY2015	% chg (yoy)
Net sales	612	674	(9.2)	623	(1.7)
Other income	18	15	22.9	20	(7.0)
Operating profit	51	79	(35.6)	28	80.1
Tax	(16)	16	(199.2)	(3)	349.6
Adj. net profit/(loss)	38	24	58.9	(10)	-

Source: Company, Angel Research

IPCA Laboratories (Ipcal)'s results for 4QFY2016 have come in much lower than our expectations on the sales and the operating front, while a tax write-back led the net profit to outperform our estimates. Sales for the quarter de-grew 1.7% yoy to ₹612cr (V/s ₹680cr expected). On the operating front, the gross margin came in at 64.4% V/s 58.8% in 4QFY2015, while the EBDITA margin came in at 8.4% V/s 4.6% in 4QFY2015. The reported net profit for the quarter thus came in at ₹38cr V/s ₹8cr in 4QFY2015 while the Adj. net profit stood at ₹38cr V/s a loss of ₹10cr in 4QFY2015. While the current performance of the company is being impacted due to its key plants being under the USFDA scanner, we believe once out of it, the company can bounce back to its normalized ROE of 25%. **Thus, we maintain our Buy on the stock.**

Results lower than expectations: For the quarter, the company's sales declined by 1.7% yoy to ₹612cr (V/s ₹680cr expected). The dip in the sales was owing to a 26% yoy decline in API sales (₹114cr), while Formulations (₹498cr) posted a yoy growth of 6.0%. Within formulations, domestic formulations posted a yoy growth of 9%. On the operating front, the gross margin came in at 64.4% V/s 58.8% in 4QFY2015, while the EBDITA margin came in at 8.4% V/s 4.6% in 4QFY2015. The reported net profit for the quarter thus came in at ₹38cr V/s ₹8cr in 4QFY2015 while the, Adj. net profit stood at ₹38cr V/s a loss of ₹10cr in 4QFY2015.

Outlook and Valuation: We expect net sales to post a 15.6% CAGR to ₹3,799cr, and EPS to register a 36.5% CAGR to ₹19.7 over FY2016–18E. The company's financials will be impacted by the USFDA import alert on the Ratlam, Indore and Silvassa facilities. While the problems are likely to persist for a while, we expect the company's performance to witness a gradual pick-up going forward. Given the valuations, **we maintain our Buy rating on the stock with a price target of ₹613.**

Key financials (Consolidated)

Y/E March (₹ cr)	FY2015	FY2016	FY2017E	FY2018E
Net sales	3,117	2,844	3,303	3,799
% chg	(2.6)	(8.7)	16.1	15.0
Adj. Net profit	254	133	219	248
% chg	(48.6)	(47.6)	64.2	13.5
EPS	20.1	10.6	17.3	19.7
EBITDA margin (%)	16.2	10.6	15.3	15.3
P/E (x)	21.2	40.4	24.6	21.7
RoE (%)	12.2	5.9	9.1	9.4
RoCE (%)	10.9	4.1	8.4	8.8
P/BV (x)	2.4	2.3	2.1	2.0
EV/Sales (x)	1.9	2.0	1.7	1.5
EV/EBITDA (x)	11.9	19.0	11.4	10.1

Source: Company, Angel Research; Note: CMP as of June 7, 2016

BUY

CMP	₹431
Target Price	₹613

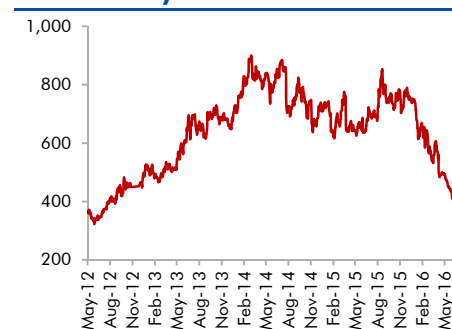
Investment Period	12 Months
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Stock Info	
Sector	Pharmaceutical
Market Cap (₹ cr)	5,846
Net Debt (₹ cr)	337
Beta	0.6
52 Week High / Low	888/402
Avg. Daily Volume	49,999
Face Value (₹)	2
BSE Sensex	26,636
Nifty	8,170
Reuters Code	IPCA.BO
Bloomberg Code	IPCA@IN

Shareholding Pattern (%)	
Promoters	45.9
MF / Banks / Indian Fls	19.8
FII / NRIs / OCBs	22.1
Indian Public / Others	12.2

Abs. (%)	3m	1yr	3yr
Sensex	8.2	(0.8)	37.0
Ipcal	(15.0)	(27.8)	(23.3)

3-Year Daily Price Chart



Source: Company, Angel Research

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Exhibit 1: 4QFY2016 – Standalone performance

Y/E March (₹ cr)	4QFY2016	3QFY2016	% chg (qoq)	4QFY2015	% chg (yoy)	FY2016	FY2015	% chg (yoy)
Net sales	612	674	(9.2)	623	(1.7)	2844	3060	(7.0)
Other income	18	15	22.9	20	(7.0)	57	65	(11.6)
Total income	630	689	(8.5)	642	(1.8)	2902	3125	(7.1)
Gross profit	395	423	(6.8)	366	7.8	1787	1917	(6.8)
Gross margins (%)	64.4	62.8		58.8		62.8	62.6	
Operating profit	51	79	(35.6)	28	80.1	262	495	(47.1)
Operating margin (%)	8.4	11.8		4.6		9.2	16.2	
Interest	8	9	(11.4)	8	(2.2)	32	26	21.6
Depreciation	39	45	(12.5)	58	(32.0)	172	177	(2.7)
PBT	22	40	(45.2)	(18)	-	112	352	(68.2)
Provision for taxation	(16)	16	(199.2)	(3)	349.6	19	102	(81.8)
Less: Exceptional Items (gains)/ loss	0	1		(23)		0	0	
Reported Net profit	38	23	62.6	8	-	93	254	(63.3)
Adj. Net profit/(loss)	38	24	58.9	(10)	-	93	254	(63.3)
EPS (₹)	2.9	1.8		(0.8)		7.3	19.8	(63.3)

Source: Company, Angel Research, FY numbers are consolidated

Exhibit 2: 4QFY2016 – Actual vs Angel estimates

(₹ cr)	Actual	Estimates	Variation (%)
Net sales	612	680	(10.0)
Other income	18	18	(0.1)
Operating profit	51	83	(38.5)
Interest	8	8	(0.1)
Tax	(16)	11	-
Adjusted Net profit/(loss)	38	28	33.5

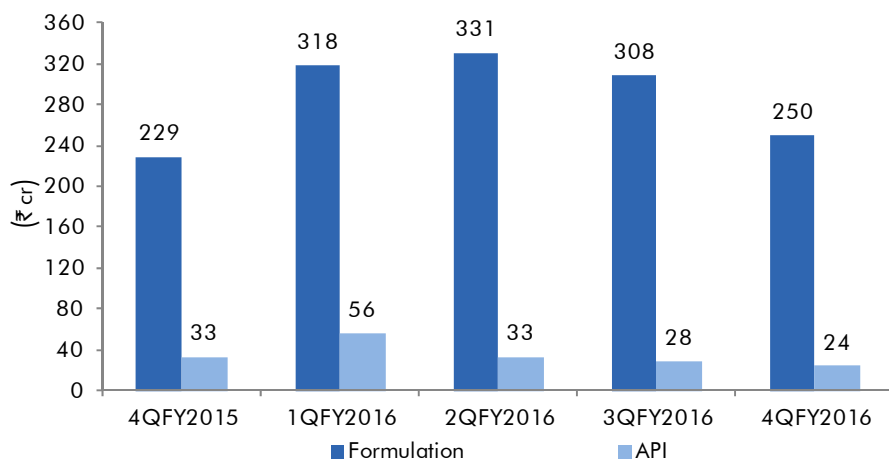
Source: Company, Angel Research

Revenue below our estimate; dips 1.7% yoy: For the quarter, the company's sales declined by 1.7% yoy to ₹612cr (V/s ₹680cr expected). The dip in the sales was owing to a 26% yoy decline in API sales (₹114cr), while Formulations (₹498cr) posted a yoy growth of 6.0%. Within formulations, domestic formulations posted a yoy growth of 9%.

Domestic markets (₹273cr) posted a growth of 4.4% yoy. API sales at ₹24cr de-grew by 27.6% yoy, while Formulation sales at ₹250cr grew by 9.0% yoy. Exports (₹339cr) dipped by 6.1% yoy; API exports dipped by 25.1% yoy (₹91cr), while Formulation exports (₹249cr) posted a yoy growth of 3.5%.

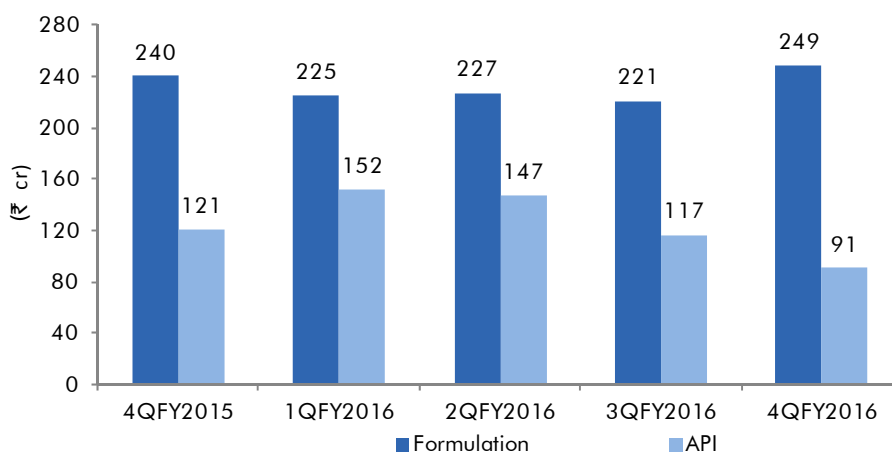
Overall, for 4QFY2016, exports contributed 55.4% to the top-line while the domestic business contributed by around 44.6%. The overall contribution of formulation sales is at 81.3% of total sales, for the quarter.

Exhibit 3: Domestic sales trend



Source: Company, Angel Research

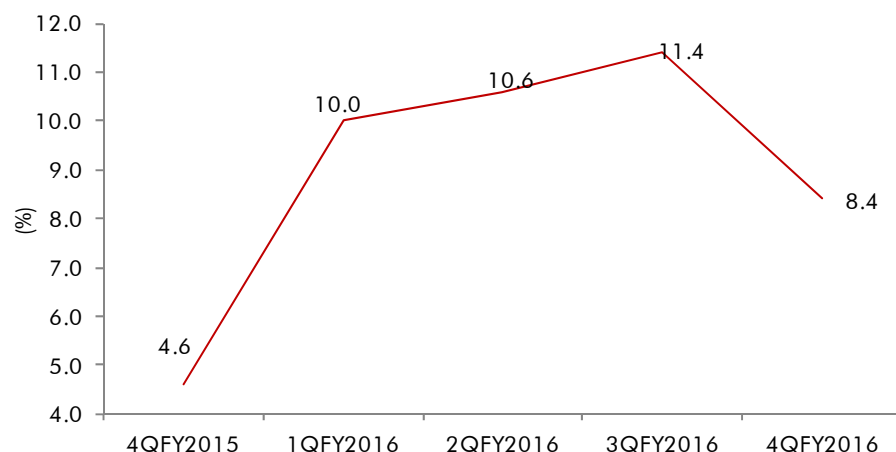
Exhibit 4: Exports sales trend



Source: Company, Angel Research

OPM falls sharply: On the operating front, the gross margin came in at 64.4% V/s 58.8% in 4QFY2015 on back of an improved sales mix, while the EBDITA margin came in at 8.4% V/s 4.6% in 4QFY2015. The margins growth during the quarter was restricted by the dip in sales. The company had posted an OPM of 11.8% in 3QFY2016. The decline was also owing to a large amount of fixed costs in the US and the Institutional business remaining unabsorbed, and remediation cost on US facilities also continued to be incurred during the quarter. Overall, the base business' margin remained muted at ~14-15% in 4QFY2016. The margins are likely to improve once the US business picks up, which would be hopefully by FY2018.

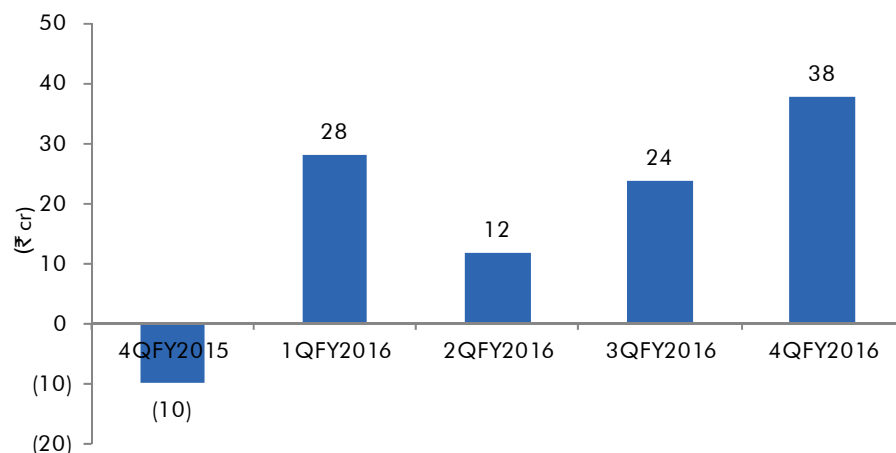
Exhibit 5: OPM trend



Source: Company, Angel Research

Reported net profit outperforms our estimates: The reported net profit thus came in at ₹38cr V/s ₹8cr in 4QFY2015 while the Adj. net profit stood at ₹38cr V/s a loss of ₹10cr in 4QFY2015.

Exhibit 6: Adj. Net profit trend



Source: Company, Angel Research

Investment arguments

- **Domestic formulations business – the cash cow:** Ipca has been successful in changing its business focus to the high-margin chronic and lifestyle segments from the low-margin anti-malarial segment. The chronic and lifestyle segments, comprising CVS, anti-diabetics, pain-management, CNS and dermatology products, constitute more than 50% of the company’s domestic formulation sales. The Management has ramped up its field force significantly with addition of divisions in the domestic formulations segment, taking the current total strength to nearly 4,000MRs. With an expected pick-up in sales in FY2017, we expect the domestic formulation business to grow at a CAGR of 16.2% over FY2016-18E.
- **Exports currently under pressure; should pickup only by FY2018:** On the formulations front, Ipca has been increasing its penetration in regulated

markets, viz Europe and the US, by expanding the list of generic drugs backed by its own API. In the emerging and semi-regulated markets, the company plans to focus on building brands in the CVS, CNS, pain-management and anti-malarial segments along with tapping new geographies. On the API front, where the company is among the low-cost producers, it is aggressively pursuing supply tie-ups with pharmaceutical MNCs.

After the USFDA inspection at the company's API manufacturing facility at Ratlam (Madhya Pradesh), the company has received certain inspection observations in Form 483, consequent to which the company had voluntarily decided to temporarily suspend API shipments from this manufacturing facility to the US markets until the issue getting resolved. However, the 483 was converted into an import alert, except for 4 APIs which constituted around 45% of US sales in FY2014.

The company's Silvassa and Indore facilities (formulation facilities) are also under import alert. These developments impacted FY2015 sales, while FY2017/FY2018 should see some revival. We expect exports to grow at a CAGR of 15.0% over FY2016-18E.

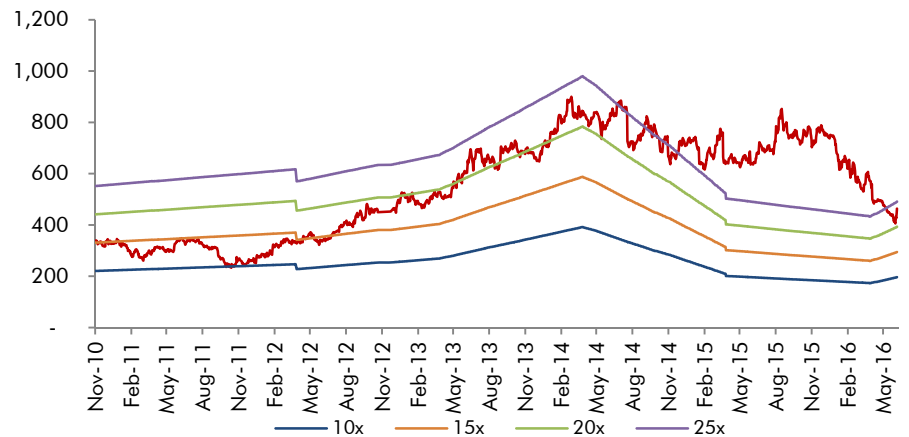
Outlook & Valuation:

We expect net sales to post a 15.6% CAGR to ₹3,799cr, and EPS to register a 36.5% CAGR to ₹19.7 over FY2016–18E. The company's financials will be impacted by the USFDA import alert on the Ratlam, Indore and Silvassa facilities. While the problems are likely to persist for a while, we expect a gradual pick-up in performance only by FY2018. Still, given the valuations, **we maintain our Buy rating on the stock with a price target of `613.**

Exhibit 7: Key Assumptions

	FY2017E	FY2018E
Sales growth (%)	16.1	15.0
Domestic growth (%)	17.4	15.0
Exports growth (%)	15.0	15.0
Operating margins (%)	15.3	15.3
R&D Exp (% of sales)	4.0	4.0
Capex (₹ cr)	500	500

Source: Company, Angel Research

Exhibit 8: One-year forward PE band


Source: Company, Angel Research

Exhibit 9: Recommendation summary

Company	Reco.	CMP (₹)	Tgt Price (₹)	Upside (%)	PE (x)	EV/Sales (x)	FY2017E	FY15-17E	FY2017E	
							EV/EBITDA (x)	CAGR in EPS (%)	RoCE (%)	RoE (%)
Alembic Pharma	Neutral	557	-	-	29.8	3.0	18.2	11.4	22.0	20.1
Aurobindo Pharma	Accumulate	773	768	10.8	20.1	3.1	14.5	11.4	21.4	27.7
Cadila Healthcare	Buy	320	400	25.0	18.7	2.9	13.2	22.9	24.2	28.8
Cipla	Neutral	469	-	-	21.6	2.7	15.3	4.9	11.1	13.7
Dr Reddy's	Accumulate	3,158	3,476	10.1	20.7	3.0	12.3	6.8	19.2	18.7
Dishman Pharma	Neutral	152	-	-	15.2	1.6	7.7	15.9	9.4	11.0
GSK Pharma	Neutral	3,515	-	-	58.4	8.1	43.0	0.0	33.0	29.9
Indoco Remedies	Neutral	282	-	-	20.7	2.2	12.4	23.0	19.7	19.7
Ipca labs	Buy	431	613	42.2	24.9	1.8	11.5	7.8	8.4	9.1
Lupin	Buy	1,435	1,809	26.1	24.7	4.1	15.6	13.1	29.6	24.7
Sanofi India*	Accumulate	4,300	4,738	10.2	28.0	3.9	22.3	34.2	21.0	25.6
Sun Pharma	Buy	739	950	28.6	26.4	5.4	17.9	10.5	17.7	18.7

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

Company background

Formed in 1949, IPCA Labs is a market leader in the anti-malarials and rheumatoid arthritis segments. The company is a notable name in the domestic formulations category with 150 formulations across major therapeutic segments like cardiovascular (CVS), anti-diabetes, anti-malaria, pain-management (NSAID), anti-bacterial, central nervous system (CNS) and gastro-intestinal. The company has 7 production units which are approved by most of the discerning regulatory authorities including USFDA, UKMHRA, Australia-TGA, South Africa-MCC and Brazil-ANVISA.

Profit & loss statement (Consolidated)

Y/E March (₹ cr)	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
Gross sales	2,778	3,232	3,157	2,891	3,356	3,859
Less: Excise duty	25	33	40	47	53	61
Net Sales	2,754	3,199	3,117	2,844	3,303	3,799
Other operating income	59	82	40	41	41	41
Total operating income	2,813	3,282	3,157	2,885	3,344	3,839
% chg	19.3	16.7	(3.8)	(8.6)	15.9	14.8
Total expenditure	2,190	2,471	2,613	2,543	2,799	3,219
Net raw materials	1,097	1,137	1,155	1,058	1,173	1,349
Other mfg costs	245	250	277	253	294	338
Personnel	392	498	565	627	728	837
Other	456	587	616	606	604	695
EBITDA	564	728	504	301	504	580
% chg	19.5	29.1	(30.8)	(40.2)	67.4	15.0
(% of Net Sales)	20.5	22.8	16.2	10.6	15.3	15.3
Depreciation & amortisation	87	103	180	172	233	268
EBIT	477	625	324	129	271	312
% chg	17.8	31.1	(48.1)	(60.2)	110.3	15.0
(% of Net Sales)	17.3	19.5	10.4	4.5	8.2	8.2
Interest & other charges	33	27	28	32	32	32
Other Income	14	22	28	17	17	17
(% of PBT)	2.8	3.2	7.8	10.9	5.7	5.0
Recurring PBT	517	703	364	155	297	338
% chg	24.0	35.9	(48.2)	(57.5)	91.8	13.7
Extraordinary expense/(Inc.)	63.3	72.2	-	39.5	-	-
PBT (reported)	454	631	364	115	297	338
Tax	129.9	152.4	101.9	18.6	74.2	84.4
(% of PBT)	28.6	24.2	28.0	16.1	25.0	25.0
PAT (reported)	324	478	262	97	223	253
Add: Share of earnings of asso.	-	0	(5)	(3)	-	-
PAT after MI (reported)	324	478	254	94	219	248
ADJ. PAT	340	495	254	133	219	248
% chg	18.4	45.6	(48.6)	(47.6)	64.2	13.5
(% of Net Sales)	11.8	14.9	8.2	3.3	6.6	6.5
Basic EPS (₹)	26.9	39.2	20.1	10.6	17.3	19.7
Fully Diluted EPS (₹)	26.9	39.2	20.1	10.6	17.3	19.7
% chg	18.4	45.6	(48.6)	(47.6)	64.2	13.5

Balance sheet (Consolidated)

Y/E March (₹ cr)	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
SOURCES OF FUNDS						
Equity share capital	25	25	25	25	25	25
Reserves & surplus	1,529	1,934	2,183	2,281	2,485	2,718
Shareholders Funds	1,554	1,960	2,208	2,306	2,510	2,743
Minority interest	-	-	-	-	-	-
Total loans	523	603	829	595	671	809
Other Long Term Liabilities	1	1	-	-	-	-
Long Term Provisions	12	15	22	23	23	23
Deferred tax liability	130	147	174	169	169	169
Total Liabilities	2,220	2,726	3,233	3,094	3,350	3,722
APPLICATION OF FUNDS						
Gross block	1,537	1,882	2,626	2,828	3,328	3,828
Less: Acc. depreciation	475	578	758	930	1,163	1,431
Net Block	1,063	1,303	1,868	1,898	2,165	2,397
Goodwill	42	50	34	34	34	34
Capital work-in-progress	129	165	165	165	165	165
Investments	9	9	16	96	96	96
Long Term Loans and Adv.	57	71	115	108	125	144
Current assets	1,397	1,602	1,614	1,522	1,767	2,032
Cash	58	76	125	162	189	223
Loans & advances	42	67	47	43	50	50
Other	1,297	1,459	1,442	1,317	1,529	1,759
Current liabilities	477	485	579	729	847	974
Net Current Assets	921	1,117	1,035	793	920	1,058
Other Non current Assets	-	9	-	-	.	.
Total Assets	2,220	2,726	3,233	3,094	3,350	3,722

Cash flow statement (Consolidated)

Y/E March (₹ cr)	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
Profit before tax	454	631	364	115	297	338
Depreciation	87	103	180	172	233	268
(Inc)/Dec in working capital	(116)	(193)	88	286	(411)	1,088
Direct taxes paid	(130)	(152)	(102)	(19)	(74)	(84)
Cash Flow from Operations	295	389	530	555	137	1,722
(Inc.)/Dec.in fixed assets	(257)	(380)	(745)	(202)	(500)	(500)
(Inc.)/Dec. in Investments	-	-	-	-	-	-
Cash Flow from Investing	(257)	(380)	(745)	(202)	(500)	(500)
Issue of Equity	0	-	-	-	-	-
Inc./Dec.) in loans	(5)	83	232	(232)	76	138
Dividend Paid (Incl. Tax)	(59)	(74)	(15)	(15)	(15)	(15)
Others	72	1	47	(69)	419	(72)
Cash Flow from Financing	8	10	264	(316)	480	51
Inc./Dec.) in Cash	46	18	49	37	27	38
Opening Cash balances	12	58	76	125	162	189
Closing Cash balances	58	76	125	162	189	223

Key Ratios

Y/E March	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
Valuation Ratio (x)						
P/E (on FDEPS)	16.0	11.0	21.4	40.8	24.9	21.9
P/CEPS	12.7	9.1	12.5	17.8	12.0	10.5
P/BV	3.5	2.8	2.5	2.4	2.2	2.0
Dividend yield (%)	0.9	0.9	0.9	0.9	0.9	0.9
EV/Sales	2.1	1.8	1.9	2.0	1.8	1.6
EV/EBITDA	10.4	8.1	12.0	19.2	11.5	10.2
EV / Total Assets	2.6	2.2	1.9	1.9	1.7	1.6
Per Share Data (₹)						
EPS (Basic)	26.9	39.2	20.1	10.6	17.3	19.7
EPS (fully diluted)	26.9	39.2	20.1	10.6	17.3	19.7
Cash EPS	33.8	47.4	34.4	24.2	35.8	40.9
DPS	4.0	5.0	1.0	1.0	1.0	1.0
Book Value	123.1	155.3	175.0	182.7	198.9	217.4
DuPont Analysis						
EBIT margin	17.3	19.5	10.4	4.5	8.2	8.2
Tax retention ratio	71.4	75.8	72.0	83.9	75.0	75.0
Asset turnover (x)	1.4	1.4	1.1	1.0	1.1	1.2
ROIC (Post-tax)	17.2	20.2	8.2	3.6	6.8	7.1
Cost of Debt (Post Tax)	4.5	3.6	2.9	3.7	3.7	3.2
Leverage (x)	0.4	0.3	0.3	0.3	0.2	0.2
Operating ROE	21.8	24.9	9.8	3.6	7.3	7.9
Returns (%)						
RoCE (Pre-tax)	23.2	25.3	10.9	4.1	8.4	8.8
Angel RoIC (Pre-tax)	25.0	27.7	12.0	4.5	9.4	9.9
RoE	24.2	28.2	12.2	5.9	9.1	9.4
Turnover ratios (x)						
Asset Turnover (Gross Block)	2.0	1.9	1.4	1.1	1.1	1.1
Inventory / Sales (days)	92	88	103	111	96	97
Receivables (days)	49	48	46	46	52	52
Payables (days)	42	45	43	90	60	60
WC cycle (ex-cash) (days)	106	106	113	97	74	74
Solvency ratios (x)						
Net debt to equity	0.3	0.3	0.3	0.2	0.2	0.2
Net debt to EBITDA	0.8	0.7	1.4	1.4	1.0	1.0
Interest Coverage (EBIT / Int.)	14.3	23.3	11.4	4.1	8.6	9.9

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Disclosure of Interest Statement	Ipca Laboratories
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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