

Ipca Laboratories

Performance Highlights

Y/E March (` cr)	1QFY2018	4QFY2017	% chg (QoQ)	1QFY2017	% chg (YoY)
Net sales	713	666	7.1	855	(16.6)
Other income	6	5	18.4	5	26.9
Operating profit	22	68	(68.2)	120	(82.0)
Tax	(1)	(19)	-	29	-
Adj. net profit/(loss)	(20)	44	-	48	-

Source: Company, Angel Research

IPCA Labs posted results lower than expected for 1QFY2018 mainly on the OPM front, which lead the company to report losses during the period. In sales, the company posted sales of ₹713cr, a yoy de-growth of 16.6%, but mostly in-line with the expected ₹700cr. On EBITDA front, the company posted EBITDA of 3.0% (v/s. 8.0% expected) v/s. 14.0% in 1QFY2017. Consequently, the company posted a loss of ₹20cr (v/s. PAT of ₹21cr expected) v/s. PAT of ₹48cr in 1QFY2017. **We maintain our BUY.**

Results below expectations: On the sales front, the company posted sales of ₹713cr, down 16.6% yoy v/s. ₹700cr expected. Formulations at ₹531cr were down 16% and API at ₹171cr posted a yoy de-growth of 16%. On the EBITDA front, the company posted EBITDA of 3.0% (v/s. 8.0% expected) v/s. 14.0% in 1QFY2017. Consequently, net loss came in at ₹21cr (v/s. PAT of ₹21cr expected) v/s. PAT of ₹48cr in 1QFY2017. The other income came in at ₹6.0cr v/s. ₹5.0cr in 1QFY2017.

Outlook and Valuation: We expect net sales to post a CAGR of 11.0% to ₹3,952cr and EPS to register a CAGR of 24.7% to ₹24.0 over FY2017–19E. The company's financials will be impacted by the USFDA import alert on its 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; mostly in FY2019E. Given the inexpensive valuations, **we maintain our Buy rating.**

Key financials (Consolidated)

Y/E March (` cr)	FY2016	FY2017	FY2018E	FY2019E
Net sales	2,844	3,211	3,532	3,952
% chg	(8.7)	12.9	10.0	11.9
Adj. Net profit	133	195	158	303
% chg	(47.6)	46.0	(18.7)	91.2
EPS	10.6	15.4	12.5	24.0
EBITDA margin (%)	10.6	13.9	11.3	15.3
P/E (x)	39.2	26.9	33.0	17.3
RoE (%)	5.9	8.2	6.3	11.0
RoCE (%)	4.1	8.7	6.6	12.4
P/BV (x)	2.3	2.1	2.0	1.8
EV/Sales (x)	2.0	1.8	1.6	1.3
EV/EBITDA (x)	18.5	12.6	13.8	8.8

Source: Company, Angel Research; Note: CMP as of August 24, 2017

BUY

CMP	₹414
Target Price	₹540

Investment Period	12 Months
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Stock Info

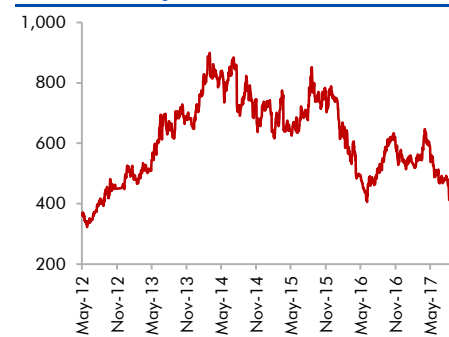
Sector	Pharmaceutical
Market Cap (₹ cr)	5,228
Net Debt (₹ cr)	357
Beta	0.8
52 Week High / Low	656/400
Avg. Daily Volume	13,073
Face Value (₹)	2
BSE Sensex	31,596
Nifty	9,857
Reuters Code	IPCA.BO
Bloomberg Code	IPCA@IN

Shareholding Pattern (%)

Promoters	46.1
MF / Banks / Indian Fls	24.9
FII / NRIs / OCBs	16.9
Indian Public / Others	12.1

Abs. (%)	3m	1yr	3yr
Sensex	6.5	12.6	19.5
Ipca	(30.3)	(23.8)	(43.6)

3-Year Daily Price Chart



Source: Company, Angel Research

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Exhibit 1: 1QFY2018 – Standalone performance

Y/E March (` cr)	1QFY2018	4QFY2017	% chg (QoQ)	1QFY2017	% chg (YoY)	FY2017	FY2016	% chg (yoy)
Net sales	713	666	7.1	855	(16.6)	3157	2843	11.0
Other income	6	5	18.4	5	26.9	22	28	(19.7)
Total income	719	671	7.2	860	(16.3)	3179	2871	10.7
Gross profit	445	434	2.6	541	(17.7)	2049	1796	14.1
Gross margins (%)	62.5	65.2		63.3		64.9	63.2	
Operating profit	22	68	(68.2)	120	(82.0)	430	274	57.3
Operating margin (%)	3.0	10.2		14.0		13.6	9.6	
Interest	6	4	26.8	6	(9.0)	23	29	(18.4)
Depreciation	43	43	1.3	42	2.8	171	161	6.1
PBT	(21)	26	(182.5)	76	-	258	111	131.7
Provision for taxation	(1)	(19)	(94.8)	29	-	70	19	269.3
Less: Excep. Items (gains)/ loss	0	0		0		0	0	
Reported Net profit	(20)	44	-	48	-	188	93	103.5
Adj. Net profit/(loss)	(20)	44	-	48	-	188	93	103.5
EPS (`)	-	3.5		3.8		14.9	7.3	

Source: Company, Angel Research, FY numbers are consolidated

Exhibit 2: 1QFY2018 – Actual Vs Angel estimates

(` cr)	Actual	Estimates	Variation (%)
Net sales	713	700	1.9
Other income	6	17	(64.4)
Operating profit	22	56	(61.6)
Interest	6	4	26.8
Tax	(1)	5	-
Adjusted Net profit/(loss)	(20)	21	-

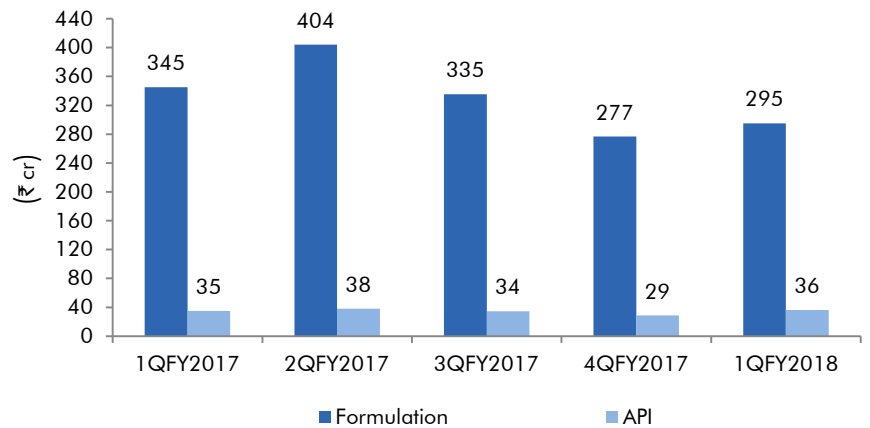
Source: Company, Angel Research

Revenue mostly in-line with our estimates down 16.6% yoy: The formulation sales (`531cr) posted a yoy de-growth of 16.0%, while API (₹171cr) posted a yoy de-growth of 16.0%.

Domestic formulation sales (₹295cr) posted a yoy de-growth of 17%, while exports formulation sales (₹236cr) posted a yoy de-growth of 14.0%. Domestic API sales (₹36cr) posted a de-growth of 4% yoy and export API sales posted yoy de-growth of 19% yoy to end the period at ₹135cr.

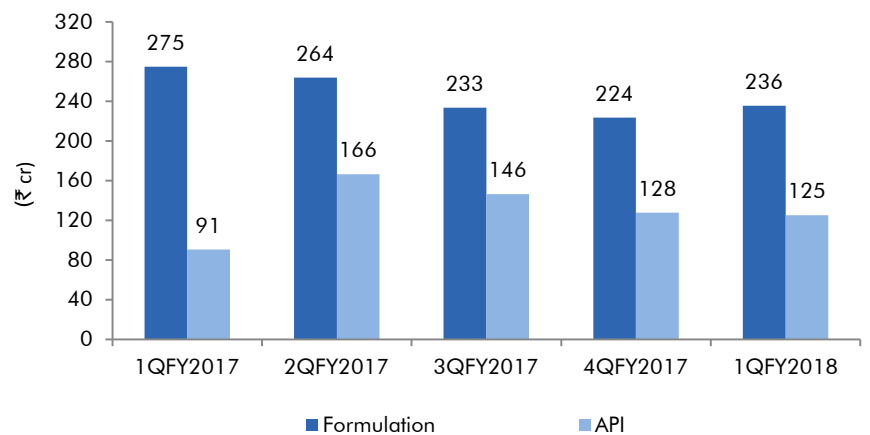
Overall, for 1QFY2018, exports contributed 52.8% to the top-line, while the domestic business contributed the rest. The overall contribution of formulations was at 75.5% of total sales during the quarter. This was against the 75.5% in 1QFY2017.

Exhibit 3: Domestic sales trend



Source: Company, Angel Research

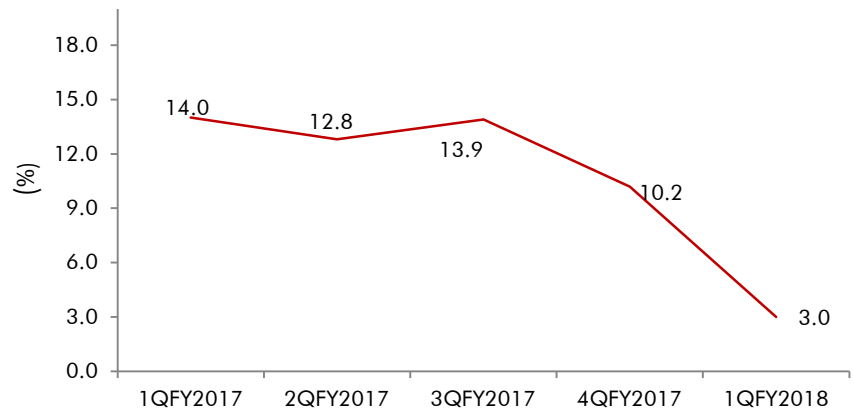
Exhibit 4: Exports sales trend



Source: Company, Angel Research

OPM dips yoy, lower than expected: On EBITDA front, the company posted EBITDA of 3.0% (v/s. 8.0% expected) v/s. 14.0% in 1QFY2017. While the GPM's were flat, (which came in at 62.5% in 1QFY2018 v/s. 63.3% in 1QFY2017), lower sales and other expenses, which rose by 2.8% yoy aided the dip in the OPM.

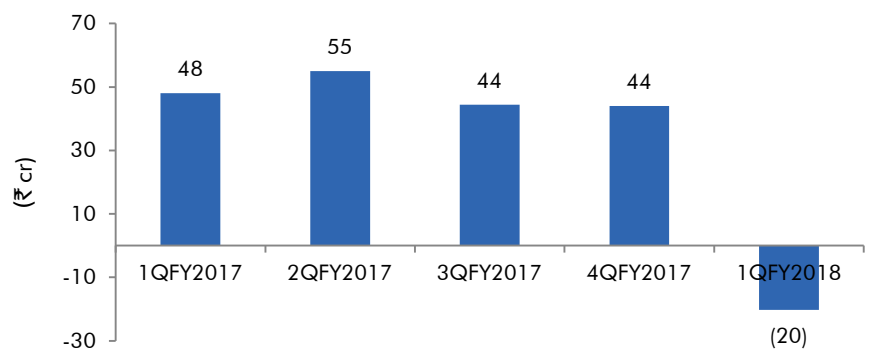
Exhibit 5: OPM trend



Source: Company, Angel Research

Reported net loss: Consequently, the Adj. net loss came in at `20cr (v/s. `21cr PAT expected) v/s. PAT of `48cr in 1QFY2017. The other income came in at `6.2cr v/s. `4.9cr in 1QFY2017.

Exhibit 6: Adj. Net profit trend



Source: Company, Angel Research

Concall Highlights

- Management expects FY2018 revenue to grow in the range of 8-10% yoy.
- Invite for Pithampur inspection is expected by September 2017. Currently >90% of ANDAs are linked to API from Ratlam. Given that the remediation process at Ratlam will only get over by end October 2018, we do not expect full regulatory resolution in the next 12 months.
- The company expects an impact of ~`15cr on EBITDTA due to GST.

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 4,000 MRs. With an expected pick-up in sales in 2HFY2018 (after the GST impact reduces), we expect the domestic formulation business to grow at a CAGR of 11.9% over FY2017-19E.
- **Exports currently under pressure; should pickup only by FY2019:** 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 is resolved. However, the Form 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. IPCA Labs has already invited the USFDA for Piparia inspection. Invite for Pithampur inspection is expected by September 2017. Currently >90% of ANDAs are linked to API from Ratlam. Given that the remediation process at Ratlam will only get over by end October 2018, we do not expect full regulatory resolution in the next 12 months. Thus, FY2019 should see some revival. We expect exports to grow at a CAGR of 10.0% over FY2017-19E.

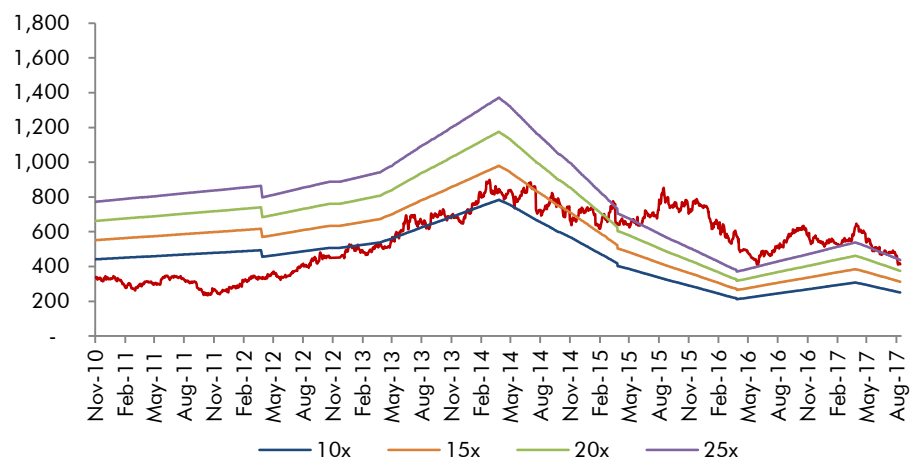
Outlook & Valuation:

We expect net sales to post a CAGR of 11.0% to ₹3,952cr and EPS to register a CAGR of 24.7% to ₹24.0cr over FY2017–19E. 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 FY2019. However, given the valuations, **we maintain our buy rating on the stock with a target price of ₹540.**

Exhibit 7: Key Assumptions

	FY2018E	FY2019E
Sales growth (%)	10.0	11.9
Domestic growth (%)	10.0	10.0
Exports growth (%)	10.0	14.0
Operating margins (%)	11.3	15.3
R&D Exp (% of sales)	4.0	4.0
Capex (₹ cr)	200	200

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		FY2019E		FY17-19E	FY2019E	
				(%)	PE (x)	EV/Sales (x)	EV/EBITDA (x)	CAGR in EPS (%)	RoCE (%)	RoE (%)
Alembic Pharma	Buy	510	600	17.4	18.7	2.1	10.9	12.8	24.3	20.6
Aurobindo Pharma	Accumulate	733	823	12.3	14.2	2.2	10.0	14.2	25.3	22.7
Cadila Healthcare	Reduce	495	426	(13.9)	23.3	3.8	18.4	21.0	17.3	22.9
Cipla	Sell	573	458	(20.1)	23.8	2.5	15.3	38.7	10.9	13.1
Dr Reddy's	Accumulate	2,088	2,219	6.3	18.8	2.1	11.7	23.6	11.2	13.0
Dishman Pharma	Under Review	301	-	-	18.9	1.3	10.1	(7.2)	2.9	2.5
GSK Pharma	Neutral	2,385	-	-	40.7	5.5	30.5	30.6	28.9	26.5
Indoco Remedies	Sell	190	153	(19.6)	14.9	1.5	10.0	23.0	11.3	15.6
Ipca labs	Buy	414	540	30.3	17.3	1.3	8.8	24.7	12.4	11.0
Lupin	Buy	992	1,467	47.8	14.9	2.0	8.7	8.2	20.5	17.5
Sanofi India*	Neutral	4,007	-	-	26.1	2.7	16.0	9.2	23.9	25.8
Sun Pharma	Buy	483	558	16.0	19.5	3.2	14.3	8.0	12.3	15.2

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

Company background

Formed in 1949, Ipca Laboratories 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)	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
Gross sales	3,232	3,157	2,891	3,262	3,588	4,016
Less: Excise duty	33	40	47	51	57	63
Net Sales	3,199	3,117	2,844	3,211	3,532	3,952
Other operating income	82	40	41	23	23	23
Total operating income	3,282	3,157	2,885	3,233	3,554	3,975
% chg	16.7	(3.8)	(8.6)	12.1	9.9	11.8
Total expenditure	2,471	2,613	2,543	2,766	3,132	3,347
Net raw materials	1,137	1,155	1,058	1,110	1,221	1,367
Other mfg costs	250	277	253	286	320	358
Personnel	498	565	627	696	778	871
Other	587	616	606	674	812	751
EBITDA	728	504	301	445	400	605
% chg	29.1	(30.8)	(40.2)	47.7	(10.1)	51.4
(% of Net Sales)	22.8	16.2	10.6	13.9	11.3	15.3
Depreciation & amortisation	103	180	172	173	187	199
EBIT	625	324	129	272	213	406
% chg	31.1	(48.1)	(60.2)	110.8	(21.7)	90.8
(% of Net Sales)	19.5	10.4	4.5	8.5	6.0	10.3
Interest & other charges	27	28	32	24	24	18
Other Income	22	28	17	-	-	-
(% of PBT)	3.2	7.8	10.9	-	-	-
Recurring PBT	703	364	155	270	211	411
% chg	35.9	(48.2)	(57.5)	74.6	(21.9)	95.0
Extraordinary expense/(Inc.)	72.2	-	39.5	-	-	-
PBT (reported)	631	364	115	270	211	411
Tax	152.4	101.9	18.6	67.5	52.8	102.8
(% of PBT)	24.2	28.0	16.1	25.0	25.0	25.0
PAT (reported)	478	262	97	203	158	309
Add: Share of earnings of asso.	0	(5)	(3)	(8)	-	-
PAT after MI (reported)	478	254	94	195	158	303
ADJ. PAT	495	254	133	195	158	303
% chg	45.6	(48.6)	(47.6)	46.0	(18.7)	91.2
(% of Net Sales)	14.9	8.2	3.3	6.1	4.5	7.7
Basic EPS (₹)	39.2	20.1	10.6	15.4	12.5	24.0
Fully Diluted EPS (₹)	39.2	20.1	10.6	15.4	12.5	24.0
% chg	45.6	(48.6)	(47.6)	46.0	(18.7)	91.2

Balance sheet (Consolidated)

Y/E March (` cr)	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
SOURCES OF FUNDS						
Equity share capital	25	25	25	25	25	25
Reserves & surplus	1,934	2,183	2,281	2,430	2,574	2,861
Shareholders Funds	1,960	2,208	2,306	2,455	2,599	2,887
Minority interest	-	-	-	-	-	-
Total loans	603	829	595	529	450	250
Other Long Term Liabilities	1	-	-	-	-	-
Long Term Provisions	15	22	23	26	26	26
Deferred tax liability	147	174	169	170	170	170
Total Liabilities	2,726	3,233	3,094	3,181	3,245	3,333
APPLICATION OF FUNDS						
Gross block	1,882	2,626	2,760	2,914	3,114	3,314
Less: Acc. depreciation	578	758	930	1,103	1,290	1,489
Net Block	1,303	1,868	1,830	1,811	1,824	1,825
Goodwill	50	34	102	102	102	102
Capital work-in-progress	165	165	165	165	165	165
Investments	9	16	96	136	136	136
Long Term Loans and Adv.	71	115	108	125	134	150
Current assets	1,602	1,614	1,522	1,620	1,790	1,969
Cash	76	125	162	36	44	21
Loans & advances	67	47	38	43	50	50
Other	1,459	1,442	1,322	1,542	1,696	1,898
Current liabilities	485	579	729	779	905	1,013
Net Current Assets	1,117	1,035	793	842	884	956
Other Non current Assets	9	-	-	-	-	-
Total Assets	2,725	3,233	3,094	3,181	3,245	3,333

Cash flow statement (Consolidated)

Y/E March (₹ cr)	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
Profit before tax	631	364	115	270	211	411
Depreciation	103	180	172	173	187	199
(Inc)/Dec in working capital	(193)	88	286	(193)	(43)	(110)
Direct taxes paid	(152)	(102)	(19)	(68)	(53)	(103)
Cash Flow from Operations	389	530	555	183	302	397
(Inc.)/Dec.in fixed assets	(380)	(745)	(134)	(154)	(200)	(200)
(Inc.)/Dec. in Investments	-	-	-	-	-	-
Cash Flow from Investing	(380)	(745)	(134)	(154)	(200)	(200)
Issue of Equity	-	-	-	-	-	-
Inc./[Dec.] in loans	83	232	(232)	(63)	(79)	(200)
Dividend Paid (Incl. Tax)	(74)	(15)	(15)	(15)	(15)	(15)
Others	1	47	(69)	(77)	-	(6)
Cash Flow from Financing	10	264	(316)	(155)	(94)	(221)
Inc./[Dec.] in Cash	18	49	37	(126)	8	(23)
Opening Cash balances	58	76	125	162	36	44
Closing Cash balances	76	125	162	36	44	21

Key Ratios

Y/E March	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
Valuation Ratio (x)						
P/E (on FDEPS)	10.6	20.6	39.2	26.9	33.0	17.3
P/CEPS	8.7	12.1	17.1	14.2	15.2	10.4
P/BV	2.7	2.4	2.3	2.1	2.0	1.8
Dividend yield (%)	1.2	0.2	0.2	0.2	0.2	0.2
EV/Sales	1.8	1.9	2.0	1.8	1.6	1.3
EV/EBITDA	7.8	11.6	18.5	12.6	13.8	8.8
EV / Total Assets	2.1	1.8	1.8	1.8	1.7	1.6
Per Share Data (₹)						
EPS (Basic)	39.2	20.1	10.6	15.4	12.5	24.0
EPS (fully diluted)	39.2	20.1	10.6	15.4	12.5	24.0
Cash EPS	47.4	34.4	24.2	29.1	27.3	39.7
DPS	5.0	1.0	1.0	1.0	1.0	1.0
Book Value	155.3	175.0	182.7	194.6	205.9	228.7
DuPont Analysis						
EBIT margin	19.5	10.4	4.5	8.5	6.0	10.3
Tax retention ratio	75.8	72.0	83.9	75.0	75.0	75.0
Asset turnover (x)	1.4	1.1	1.0	1.1	1.1	1.2
ROIC (Post-tax)	20.2	8.2	3.6	6.8	5.1	9.4
Cost of Debt (Post Tax)	3.6	2.9	3.7	3.2	3.8	3.8
Leverage (x)	0.3	0.3	0.3	0.2	0.2	0.1
Operating ROE	24.9	9.8	3.6	7.4	5.3	10.1
Returns (%)						
RoCE (Pre-tax)	25.3	10.9	4.1	8.7	6.6	12.4
Angel RoIC (Pre-tax)	27.7	12.0	4.5	9.5	7.1	13.2
RoE	28.2	12.2	5.9	8.2	6.3	11.0
Turnover ratios (x)						
Asset Turnover (Gross Block)	1.9	1.4	1.1	1.1	1.2	1.2
Inventory / Sales (days)	88	103	111	91	92	90
Receivables (days)	48	46	46	49	50	49
Payables (days)	45	43	90	61	57	62
WC cycle (ex-cash) (days)	106	113	97	81	85	81
Solvency ratios (x)						
Net debt to equity	0.3	0.3	0.2	0.2	0.2	0.1
Net debt to EBITDA	0.7	1.4	1.4	1.1	1.0	0.4
Int. Coverage (EBIT / Int.)	23.3	11.4	4.1	11.3	8.7	23.2

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1. Financial interest of research analyst or Angel or his Associate or his relative	No
2. Ownership of 1% or more of the stock by research analyst or Angel or associates or relatives	No
3. Served as an officer, director or employee of the company covered under Research	No
4. Broking relationship with company covered under Research	No

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)