

Indoco Remedies

Performance Highlights

Y/E March (` cr)	2QFY18	1QFY18	% chg (qoq)	2QFY17	% chg (yoy)
Net sales	280	204	37.1	276	1.3
Other operating income	7	6	25.8	6	26.1
Gross profit	180	133	35.1	179	0.3
Operating profit	36	(3)	-	37	(3.1)
Net profit/(loos)	20	(22)	-	22	(10.7)

Source: Company, Angel Research

For 2QFY2018 Indoco Remedies sales came in at `280cr, in line with expectations, posting a yoy growth of 1.3%. The growth was impacted by lower exports, mainly on the back of US (` post a 69.5% yoy dip in sales). Indian Formulation sales posted 11.5% yoy growth. On operating front, the EBITDA margins came in at 12.9% (11.8% expected) v/s. 13.5% in 2QFY2017, following lower than expected other expenses during the quarter. Thus, the PAT came in at `20cr (`13cr expected) v/s. `22cr in 2QFY2017. **We maintain our sell rating on the stock, with a price target of `136.**

Results better than expected: Sales came in at `280cr v/s. `276cr in 2QFY2017, a yoy growth of 1.3%. The growth was impacted by lower exports, mainly on the back of US (` post a dip of 69.5% yoy dip in sales). Indian Formulation sales posted a 11.5% yoy growth. The formulation sales (`262.5cr accounting for 92.2% of total sales in 2QFY2018) posted a flat growth of 0.4% yoy. The domestic formulation sales (`188cr) registered a growth of 11.5% yoy. The International formulation sales (`74cr) posted a yoy dip of 19.8%. The API sales (`14.7cr) posted a yoy grow of 8.3%. On operating front, the EBITDA margins came in at 12.9% (11.8% expected) v/s. 13.5% in 2QFY2017, following lower than expected other expenses during the quarter. Gross margins came in at 64.2% v/s. 64.9% in 2QFY2017, while R&D expenses were 4.9% of sales in 2QFY2018 v/s. 4.4% of sales in 2QFY2017. Thus, the PAT came in at `20cr (`13cr expected) v/s. `22cr in 2QFY2017.

Outlook and valuation: We expect net sales to post a CAGR of 10.3% to `1,297cr and EPS to post a CAGR of 16.2% to `11.4 over FY2017-19E. **We maintain our SELL rating on back of the valuations and the corresponding lower profitability.**

Key financials (Consolidated)

Y/E March (` cr)	FY2016	FY2017	FY2018E	FY2019E
Net sales	977	1067	1114	1297
% chg	14.6	9.2	4.4	16.5
Net profit	83.0	77.5	51.3	104.6
% chg	0.2	(6.7)	(33.7)	103.7
EPS (`)	9.0	8.4	5.6	11.4
EBITDA margin (%)	14.9	12.1	9.9	13.9
P/E (x)	29.7	31.8	47.9	23.5
RoE (%)	15.1	12.6	7.7	14.5
RoCE (%)	11.9	7.9	3.8	10.1
P/BV (x)	4.2	3.8	3.6	3.2
EV/Sales (x)	2.6	2.5	2.4	2.1
EV/EBITDA (x)	17.7	20.5	24.7	14.9

Source: Company, Angel Research; Note: CMP as of November 22, 2017

SELL

CMP `280
 Target Price `136

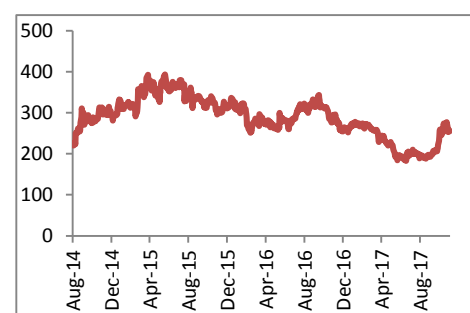
Investment Period -

Stock Info	
Sector	Pharmaceutical
Market Cap (` cr)	2,579
Net Debt (` cr)	188
Beta	0.2
52 Week High / Low	287/179
Avg. Daily Volume	19,371
Face Value (`)	2
BSE Sensex	33,562
Nifty	10,342
Reuters Code	INRM.BO
Bloomberg Code	INDR@IN

Shareholding Pattern (%)	
Promoters	58.9
MF / Banks / Indian FIs	12.9
FII / NRIs / OCBs	11.4
Indian Public / Others	16.8

Abs. (%)	3m	1yr	3yr
Sensex	6.3	29.3	17.8
Indoco	(18.7)	(39.9)	(15.8)

3-Year Daily Price Chart



Source: Company, Angel Research

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Exhibit 1: 2QFY2018 (Consolidated) performance

Y/E March (` cr)	2QFY2018	1QFY2018	% chg (qoq)	2QFY2017	% chg (yoy)	1HFY2018	1HFY2017	% chg (yoy)
Net sales	280	204	37.1	276	1.3	484	529	(8.4)
Other income	7.1	5.7	25.8	5.6	26.1	13	12	8.7
Total income	287	210	36.8	282	1.8	497	541	(8.1)
Gross profit	180	133	35.1	179	0.3	313	635	(50.7)
Gross margins (%)	64.2	65.2		64.9		64.6	64.8	
Operating profit	36.2	(3.5)	-	37.3	(3.1)	32.7	74.5	(56.1)
OPM (%)	12.9	(1.7)		13.5		6.7	14.1	
Interest	7	6		2	343.9	13	5	153.6
Dep & amortisation	17	17	2.0	17	3.2	34	33	1.8
PBT	19	(21)	-	25	-	(2)	48	
Provision for taxation	(0.7)	0.9		2.6		0	6	
Reported Net profit	20	(22)	-	22	(10.7)	(2)	42	
Less : Exceptional items	0	0	-	0		0	0	
PAT after exceptional items	20	(22)	-	22	(10.7)	(2)	42	
EPS (`)	2.1	-		2.4		-	4.5	

Source: Company, Angel Research

Exhibit 2: 2QFY2018 – Actual vs. Angel estimates

(` cr)	Actual	Estimate	Variation (%)
Net sales	280	280	0.0
Other operating income	7	6	27.0
Operating profit	36	33	9.7
Tax	(1)	3	-
Net profit	20	13	49.7

Source: Company, Angel Research

Revenues just in-line with expectations: Sales came in at `280cr (`280cr expected) v/s. `276cr in 2QFY2017, a yoy growth of 1.3%. The growth was impacted by lower exports mainly on the back of US (`post a dip of 69.5% yoy dip in sales). Indian Formulation sales posted a 11.5% yoy growth.

The formulation sales (`262.5cr; 92.2% of total sales in 2QFY2018) posted a growth of 0.4% yoy. The domestic formulation sales (`188.2cr) registered a growth of 11.5% yoy. The International formulation sales (`74cr) posted a yoy dip of 19.8%. The API sales (`14.7cr) posted a yoy growth of 8.3%.

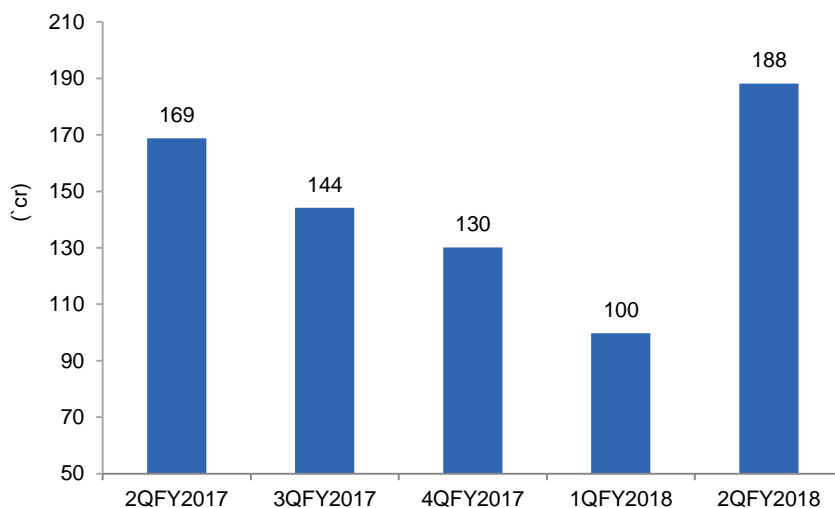
In US, during the quarter, the revenues de-grew by 69.5% at `8.0cr as against `26.2cr for the same period last year. In terms of filings, the company (through partners or by itself), filed 35 ANDAs, which are pending approvals with 10 ANDAs approved till date, with 2 tentative approvals.

On the progress of remediation measures, the Company has sent its final response to USFDA with all the supporting documentation and updates of completed actions. Detailed investigations were performed to identify root cause of the observations and to have an effective Corrective and Preventive action (CAPA) plan.

Consequent to the responses, Indoco continues to work with the US based consultant to assess all GMP systems at site and ensure upgradations as per latest GMP trends. The Company informed that it is on track in sending all its responses and will seek an audience with USFDA. The Company will soon

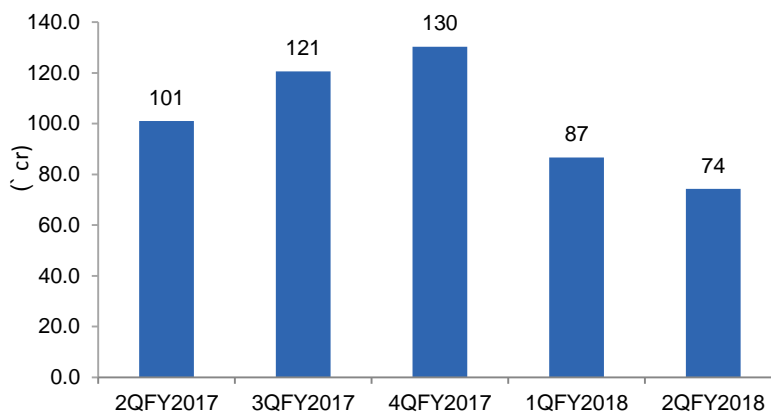
commence production of some of the existing ophthalmic products from Goa plant II for US market.

Exhibit 3: Domestic Formulation sales trend



Source: Company, Angel research

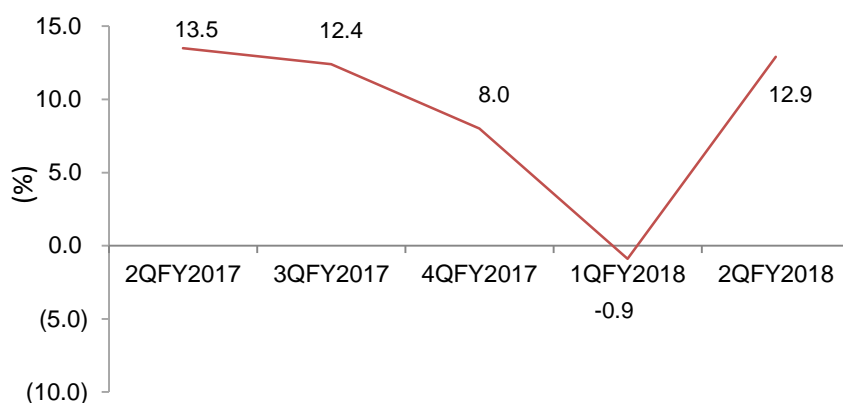
Exhibit 4: Export sales trend



Source: Company, Angel research

OPM dips yoy, but better than expected: On operating front, the EBITDA margins came in at 12.9% (11.8% expected) v/s. 13.5% in 2QFY2017, mainly on the back of lower than expected other expenses during the quarter. Gross margins came in at 64.2% v/s. 64.9% in 2QFY2017, while R&D expenses were 4.9% of sales in 2QFY2018 v/s. 4.4% of sales in 2QFY2017. On yoy basis, the decline was mainly on back of 13.0% yoy rise in the R&D expenses.

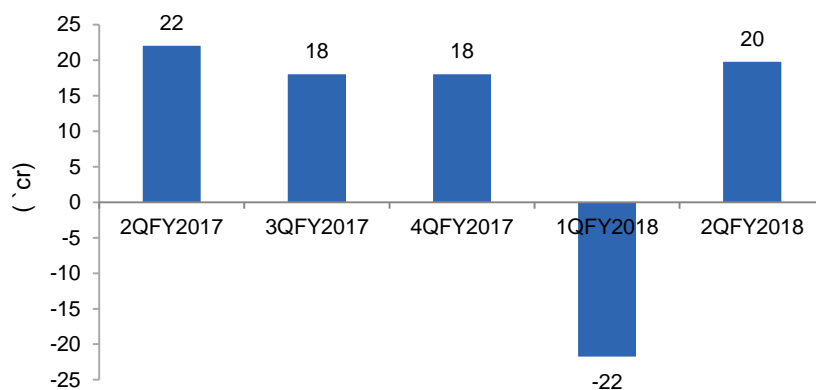
Exhibit 5: OPM trend



Source: Company, Angel Research

Net profit better than expectation: Consequently, PAT came in at `20cr (`13cr expected) v/s. `22cr in 2QFY2017. The higher than expected net profit was on the back of higher other income and lower than expected taxes. Other income came in at `7.1cr v/s. `5.6cr during the corresponding period last year. On yoy basis, the PAT dipped by 10.7%, following lower OPM.

Exhibit 6: Net profit trend



Source: Company, Angel Research

Concall takeaways

- Management expects that stoppage of exports of its ophthalmic solution to US, and sluggish growth in the unregulated markets are one-offs. All these markets are expected to deliver robust growth going ahead.
- Company's exports also remain lackluster with lower supply from its OSD plant in Goa Unit-I. EU sales declined by 6% qoq due to lower offtake in tender business in Germany. EM sales also declined down by 15% due to volatile currencies in South Africa and New Zealand.

Investment arguments

Focus on domestic formulations- Aiming for a higher-than-industry growth:

Indoco has a strong brand portfolio of 135 products and a base of ~2,800 MRs. It operates in various therapeutic segments, including anti-infective, anti-diabetic, CVS, ophthalmic, dental care, pain management and respiratory. Prominent Indoco brands include *Cyclopam*, *Vepan*, *Febrex Plus*, *ATM*, *Sensodent-K* and *Sensoform*. The company has seen strong growth across the respiratory, anti-infective, ophthalmic and alimentary therapeutic segments. Further, the company is investing to enhance the share of the chronic segment, which constitutes 10% of overall sales. With a market share of 0.7% and overall rank of 31, the company is still a marginal player with some top brands in smaller categories such as stomatologicals. We expect the domestic formulation segment to grow at a 11.5CAGR of 13.0% over FY2017-19E.

Scaling-up on the exports front: Indoco has also started focusing on regulated markets by entering into long-term supply contracts. The company is currently executing several contract-manufacturing projects, and covering a number of products for its clients in the UK, Germany and Slovenia. Indoco has received a nod from the USFDA for two of its facilities in Goa. The company derived ~49% of its revenues from exports in 2016-17. The US cumulative ANDA filings stood at 42 with 29 pending approvals (including 3 tentative approvals). Of these, 18 were filed under the Actavis deal. The Goa plant warning letter is likely to weigh on company's US business, as most of the pending ANDAs are from this unit. Watson deal, which is at the core of US business prospects, is also likely to witness a slowdown, as the development may lead to a delay in approval for products that are part of the deal. The deal covers 18 pending ANDAs. We expect the exports segment to grow at 15.0% CAGR over FY2017-19E.

Partnering with pharmaceutical majors: The Company has a large customer base of small and medium sized generic companies across the globe and has major tie-ups with generic companies for certain territories and products. It has a deal with Watson Pharmaceuticals to develop and manufacture a number of sterile (ophthalmic) products for marketing in the USA. The agreement with South Africa's largest pharmaceutical company,

Aspen Pharmacare, encompasses a number of solid dosages and ophthalmic products, extending to 30 emerging market countries, while the contract signed with DSM, Austria is for marketing 8 of Indoco's APIs in various geographies. These deals have further strengthened Indoco's image in the international arena.

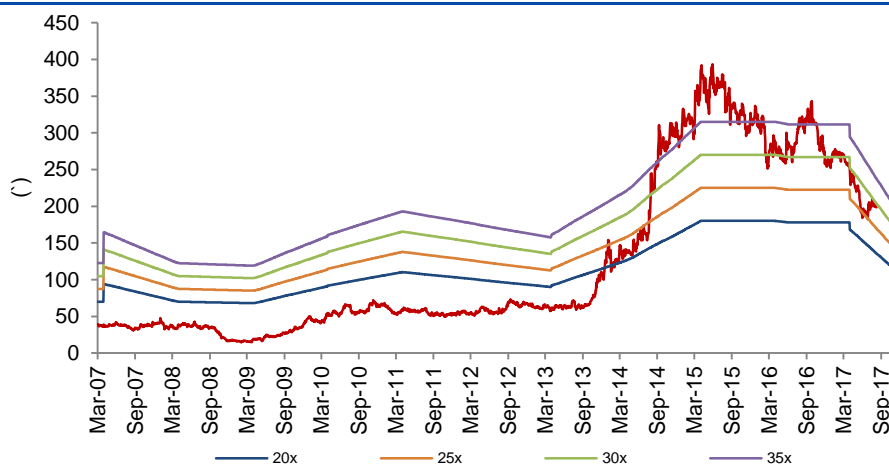
Valuation: We expect net sales to post a CAGR of 10.3% to `1,297cr and EPS to post a CAGR of 16.2% to `11.4 over FY2017-19E. At the current market price, the stock is trading at 47.9x and 16.7x its FY2018E and FY2019E earnings respectively. **We maintain a SELL rating on the stock considering the valuations.**

Exhibit 7: Key assumptions

	FY2018E	FY2019E
Domestic sales growth (%)	6.0	18.0
Exports growth	15.0	15.0
Operating margins (%)	9.9	13.9
Capex (` cr)	90.0	60.0

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)	FY2019E		FY17-19E	FY2019E	
						EV/Sales (x)	EV/EBITDA (x)	CAGR in EPS (%)	RoCE (%)	RoE (%)
Alembic Pharma	Buy	511	600	17.3	21.4	2.9	13.0	5.7	20.6	18.4
Aurobindo Pharma	Buy	699	823	17.8	13.6	2.5	9.9	14.2	25.3	22.7
Cadila Healthcare	Reduce	443	411	(7.2)	21.6	4.1	17.6	18.9	16.5	22.2
Cipla	Sell	619	462	(25.3)	25.5	3.2	16.2	39.3	10.9	13.1
Dr Reddy's	Reduce	2,361	2,040	(13.6)	23.2	3.1	13.3	18.5	10.3	12.4
Dishman Pharma	Under Review	301	-	-	19.3	2.7	10.1	23.3	4.5	4.4
GSK Pharma	Sell	2,496	2,000	(19.9)	53.9	6.9	39.3	19.3	25.8	23.5
Indoco Remedies	Sell	280	136	(49.0)	23.5	2.1	14.9	16.2	10.1	14.5
Ipca labs	Neutral	535	-	-	21.2	1.9	13.5	24.7	12.4	11.0
Lupin	Buy	828	1,091	31.8	16.7	2.4	9.3	(6.6)	13.7	13.7
Sanofi India*	Neutral	4,434	-	-	27.1	3.8	17.0	12.8	25.8	27.5
Sun Pharma	Buy	535	615	15.0	24.0	3.7	16.3	(17.5)	11.3	14.0

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

Company Background

Indoco has a strong brand portfolio of 135 products and a base of 2,300 MRs. The company operates in various therapeutic segments including anti-infective, anti-diabetic, CVS, ophthalmic, dental care, pain management and respiratory areas. Prominent Indoco brands include Cyclopam, Vepan, Febrex Plus, ATM, Sensodent-K and Sensiform. The company's top-10 brands contribute over 50% of its domestic sales. Indoco now proposes to scale up its exports through higher exposure to the regulated markets.

Profit & loss statement (Consolidated)

Y/E March (₹ cr)	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
Gross sales	735	863	987	1,078	1,126	1,312
Less: Excise duty	13	11	10	12	12	15
Net sales	722	852	977	1,067	1,114	1,297
Other operating income	10	5	27	27	27	27
Total operating income	733	857	1,004	1,094	1,141	1,325
% chg	16.2	17.0	17.1	9.0	4.3	16.1
Total expenditure	612	691	831	937	1,003	1,117
Net raw materials	272	300	341	382	412	480
Other mfg costs	42	50	57	62	65	76
Personnel	130	140	183	216	226	263
Other	168	201	250	277	301	298
EBITDA	110	161	145	129	110	180
% chg	23.5	46.1	(9.7)	(11.0)	(14.7)	63.6
(% of Net Sales)	15.2	18.9	14.9	12.1	9.9	13.9
Depreciation & amortisation	31	47	60	63	75	83
EBIT	79	114	85	66	35	98
% chg	21.0	43.7	(25.4)	(22.2)	(46.9)	178.9
(% of Net Sales)	11.0	13.3	8.7	6.2	3.1	7.5
Interest & other charges	19	11	13	6	6	6
Other income	2	2	1	4	4	4
(% of PBT)	2.4	1.6	1.1	4.5	6.9	3.4
Share in profit of Associates	-	-	1.0	2.0	3.0	4.0
Recurring PBT	72	110	101	91	60	123
PBT (reported)	72	110	101	91	60	123
Tax	14	27	18	14	9	18
(% of PBT)	19.6	24.3	17.5	15.2	15.0	15.0
PAT (reported)	58	83	83	77	51	105
Add: Share of earnings of asso.	-	-	-	-	-	-
Less: Minority interest (MI)	-	-	-	-	-	-
Prior period items	-	-	-	-	-	-
PAT after MI (reported)	58	83	83	77	51	105
ADJ. PAT	58	83	83	77	51	105
% chg	36.5	42.3	0.2	(6.7)	(33.7)	103.7
(% of Net Sales)	8.1	9.7	8.5	7.3	4.6	8.1
Basic EPS (₹)	6.3	9.0	9.0	8.4	5.6	11.4
Fully Diluted EPS (₹)	6.3	9.0	9.0	8.4	5.6	11.4
% chg	36.5	42.3	0.2	(6.7)	(33.7)	103.7

Balance Sheet (Consolidated)

Y/E March (` cr)	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
SOURCES OF FUNDS						
Equity share capital	18	18	18	18	18	18
Reserves & surplus	439	500	566	633	664	748
Shareholders funds	457	519	583	651	681	765
Minority Interest	-	-	-	-	-	-
Total loans	72	88	127	251	300	250
Other Long Term Liab.	9	9	10	10	10	10
Long Term Provisions	16	16	17	19	19	19
Deferred tax liability	31	27	24	(28)	(28)	(28)
Total liabilities	585	659	762	903	954	988
APPLICATION OF FUNDS						
Gross block	481	561	560	715	805	865
Less: acc. depreciation	156	203	264	327	402	485
Net block	325	358	296	388	403	380
Capital work-in-progress	44	44	44	44	44	44
Goodwill	-	0	88	98	98	98
Investments	0	0	15	0	0	0
Long Term Loans And Adv.	55	58	71	66	109	127
Current assets	305	385	448	572	575	659
Cash	13	15	15	63	33	27
Loans & advances	42	85	78	107	111	130
Other	249	285	355	403	431	502
Current liabilities	144	187	201	265	275	320
Net current assets	160	199	247	307	301	339
Mis. Exp. not written off	-	-	-	-	-	-
Total assets	585	659	761	903	954	988

Cash Flow Statement (Consolidated)

Y/E March (` cr)	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
Profit before tax	72	110	101	91	60	123
Depreciation	31	47	60	63	75	83
(Inc)/Dec in working capital	(18)	(39)	(62)	(8)	(66)	(62)
Less: Other income	2	2	1	4	4	4
Direct taxes paid	14	27	18	14	9	18
Cash Flow from Operations	69	90	81	128	56	121
(Inc.)/Dec.in fixed assets	(41)	(80)	1	(155)	(90)	(60)
(Inc.)/Dec. in investments	-	-	-	-	-	-
Other income	2	2	1	4	4	4
Cash Flow from Investing	(39)	(78)	3	(151)	(86)	(56)
Issue of equity	-	-	(1)	-	-	-
Inc./Dec.) in loans	(9)	16	41	126	49	(50)
Dividend Paid (Incl. Tax)	(12)	(22)	(21)	(21)	(21)	(21)
Others	(7)	(4)	(103)	(35)	(29)	-
Cash Flow from Financing	(28)	(10)	(83)	70	(0)	(71)
Inc./Dec.) in Cash	2	2	(0)	48	(30)	(5)
Opening Cash balances	12	13	15	15	63	33
Closing Cash balances	13	15	15	63	33	27

Key Ratios

Y/E March	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
Valuation Ratio (x)						
P/E (on FDEPS)	42.3	29.7	29.7	31.8	47.9	23.5
P/CEPS	27.6	18.9	17.2	17.5	19.4	13.1
P/BV	5.4	4.7	4.2	3.8	3.6	3.2
Dividend yield (%)	0.4	0.7	0.7	0.7	0.7	0.7
EV/Sales	3.5	3.0	2.6	2.5	2.4	2.1
EV/EBITDA	22.9	15.8	17.7	20.5	24.7	14.9
EV / Total Assets	4.3	3.8	3.4	2.9	2.9	2.7
Per Share Data (₹)						
EPS (Basic)	6.3	9.0	9.0	8.4	5.6	11.4
EPS (fully diluted)	6.3	9.0	9.0	8.4	5.6	11.4
Cash EPS	9.7	14.1	15.6	15.3	13.7	20.3
DPS	1.0	2.0	2.0	2.0	2.0	2.0
Book Value	49.6	56.3	63.3	70.6	74.0	83.1
Dupont Analysis						
EBIT margin	11.0	13.3	8.7	6.2	3.1	7.5
Tax retention ratio	80.4	75.7	82.5	84.8	85.0	85.0
Asset turnover (x)	1.3	1.4	1.4	1.4	1.3	1.4
ROIC (Post-tax)	11.6	14.2	10.3	7.2	3.5	9.0
Cost of Debt (Post Tax)	18.7	10.0	9.6	2.8	1.9	1.9
Leverage (x)	0.2	0.1	0.2	0.2	0.3	0.3
Operating ROE	10.4	14.8	10.5	8.3	4.0	11.4
Returns (%)						
ROCE (Pre-tax)	13.9	18.3	11.9	7.9	3.8	10.1
Angel ROIC (Pre-tax)	15.3	20.2	14.0	10.0	4.7	12.2
ROE	13.4	17.0	15.1	12.6	7.7	14.5
Turnover ratios (x)						
Asset Turnover (Gross Block)	1.6	1.6	1.8	1.7	1.5	1.6
Inventory / Sales (days)	50	55	54	63	61	60
Receivables (days)	64	62	68	80	77	76
Payables (days)	40	46	42	49	47	49
WC cycle (ex-cash) (days)	68	70	75	79	82	80
Solvency ratios (x)						
Net debt to equity	0.1	0.1	0.2	0.3	0.4	0.3
Net debt to EBITDA	0.5	0.5	0.8	1.5	2.4	1.2
Interest Coverage (EBIT / Int.)	4.2	10.7	6.8	10.7	5.7	15.9

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Disclosure of Interest Statement	Indoco Remedies
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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