

Ipca Laboratories

Performance Highlights

Y/E March (₹ cr)	3QFY2017	2QFY2017	% chg (QoQ)	3QFY2016	% chg (YoY)
Net sales	731	853	(14.3)	675	8.3
Other income	15	33	(55.2)	16	(8.0)
Operating profit	102	109	(6.7)	79	29.3
Tax	22	37	(40.6)	18	21.3
Adj. net profit/(loss)	41	55	(24.7)	27	54.6

Source: Company, Angel Research

IPCA Labs posted results lower than expected for 3QFY2017 on both sales and net profit fronts, however OPM's were in-line with expectations. In sales, the company posted sales of ₹731cr, a yoy growth of 8.3% v/s ₹815cr expected. On EBITDA front, the company posted EBITDA of 13.9% (v/s 13.5% expected) v/s 11.6% in 3QFY2016. Consequently, PAT came in at ₹40.5cr (v/s ₹61.6cr expected) v/s ₹27cr in 3QFY2016, growth of 54.6% yoy. The Tax as % of PBT was 34.9% of PBT v/s 40.5% of PBT in 3QFY2016. **We maintain our Accumulate.**

OPM in-line with expectations: In sales, the company posted sales of ₹731cr, up 8.3% yoy v/s ₹815cr expected. Formulations at ₹569cr, posted a yoy growth of 6.0% and API at ₹162cr, posted a yoy growth of 16.0%. On EBITDA front, the company posted EBITDA of 13.9% (v/s 13.5% expected) v/s 11.6% in 3QFY2016. Consequently, PAT came in at ₹40.5cr (v/s ₹61.6cr expected) v/s ₹27cr in 3QFY2016, growth of 54.6% yoy. The Tax as % of PBT was 34.9% of PBT v/s 40.5% of PBT in 3QFY2016.

Outlook and Valuation: We expect net sales to post a CAGR of 14.8% to ₹3,747cr and EPS to register a CAGR of 34.8% to ₹19.2 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 inexpensive valuations, **we maintain our Accumulate rating.**

Key financials (Consolidated)

Y/E March (₹ cr)	FY2015	FY2016	FY2017E	FY2018E
Net sales	3,117	2,844	3,258	3,747
% chg	(2.6)	(8.7)	14.5	15.0
Adj. Net profit	254	133	152	242
% chg	(48.6)	(47.6)	14.4	58.9
EPS	20.1	10.6	12.1	19.2
EBITDA margin (%)	16.2	10.6	12.8	15.3
P/E (x)	27.5	52.5	45.8	28.8
RoE (%)	12.2	5.9	6.4	9.5
RoCE (%)	10.9	4.1	5.7	8.6
P/BV (x)	3.2	3.0	2.9	2.6
EV/Sales (x)	2.4	2.6	2.2	2.0
EV/EBITDA (x)	15.1	24.4	17.0	13.1

Source: Company, Angel Research; Note: CMP as of February 21, 2017

ACCUMULATE

CMP	₹544
Target Price	₹613

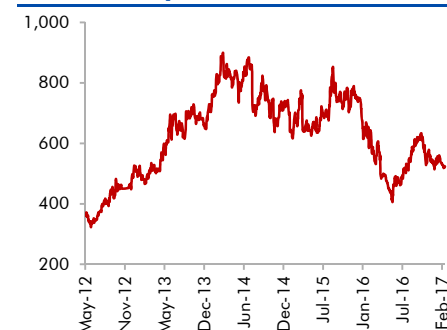
Investment Period	12 Months
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Stock Info	
Sector	Pharmaceutical
Market Cap (₹ cr)	6,988
Net Debt (₹ cr)	337
Beta	0.5
52 Week High / Low	643/402
Avg. Daily Volume	44,244
Face Value (₹)	2
BSE Sensex	28,762
Nifty	8,908
Reuters Code	IPCA.BO
Bloomberg Code	IPCA@IN

Shareholding Pattern (%)	
Promoters	46.1
MF / Banks / Indian Fls	25.3
FII / NRIs / OCBs	16.3
Indian Public / Others	12.3

Abs. (%)	3m	1yr	3yr
Sensex	10.8	21.3	38.9
Ipca	3.3	(13.9)	(37.6)

3-Year Daily Price Chart



Source: Company, Angel Research

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Exhibit 1: 3QFY2017 – Standalone performance

Y/E March (₹ cr)	3QFY2017	2QFY2017	% chg (QoQ)	3QFY2016	% chg (YoY)	9MFY2017	9MFY2016	% chg (yoy)
Net sales	731	853	(14.3)	675	8.3	2405	2160	11.4
Other income	15	33	(55.2)	16	(8.0)	66	45	44.9
Total income	746	886	(15.8)	691	8.0	2471	2205	12.1
Gross profit	488	511	(4.5)	424	15.2	1530	1331	15.0
Gross margins (%)	66.8	59.9		62.8		63.6	61.6	
Operating profit	102	109	(6.7)	79	29.3	318	224	41.8
Operating margin (%)	13.9	12.8		11.6		13.2	10.4	
Interest	10	7	41.9	10	(0.9)	19	22	(13.8)
Depreciation	43	43	0.5	40	7.9	128	117	9.7
PBT	64	92	(31.0)	45	-	237	131	80.9
Provision for taxation	22	37	(40.6)	18		89	36	144.8
Less: Excep. Items (gains)/ loss	41	0		0		4	35	
Reported Net profit	41	55	(24.7)	26	57.2	144	60	141.5
Adj. Net profit/(loss)	41	55	(24.7)	26	57.2	147	85	72.5
EPS (₹)	3.2	4.3		2.1		11.4	6.6	

Source: Company, Angel Research, FY numbers are consolidated

Exhibit 2: 3QFY2017 – Actual vs Angel estimates

(₹ cr)	Actual	Estimates	Variation (%)
Net sales	731	815	(10.3)
Other income	15	15	0.3
Operating profit	102	110	(7.7)
Interest	10	9	5.0
Tax	22	8	163.7
Adjusted Net profit/(loss)	41	62	(33.7)

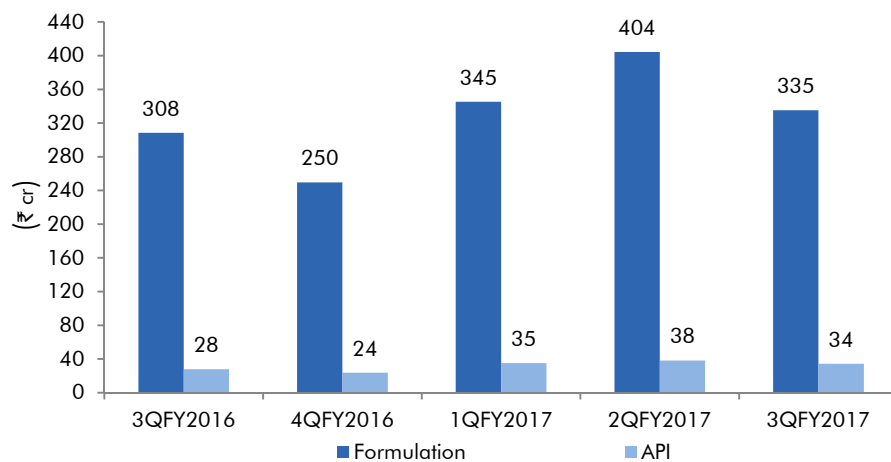
Source: Company, Angel Research

Revenue below our estimates; up 8.3% yoy: The formulation sales (₹569cr) posted a yoy growth of 6.0%, while API (₹162cr) posted a yoy growth of 16.0%. The formulation sales growth was driven by Domestic Formulation (₹335cr), posting a yoy growth of 9.0%.

Domestic formulation sales (₹335cr) posted a yoy growth of 9.0%, while exports formulation sales (₹233cr) posted a yoy growth of 3.0%. Domestic API sales (₹34cr) posted a growth of 23% yoy and export API sales posted yoy growth of 14% yoy to end the period at ₹128cr.

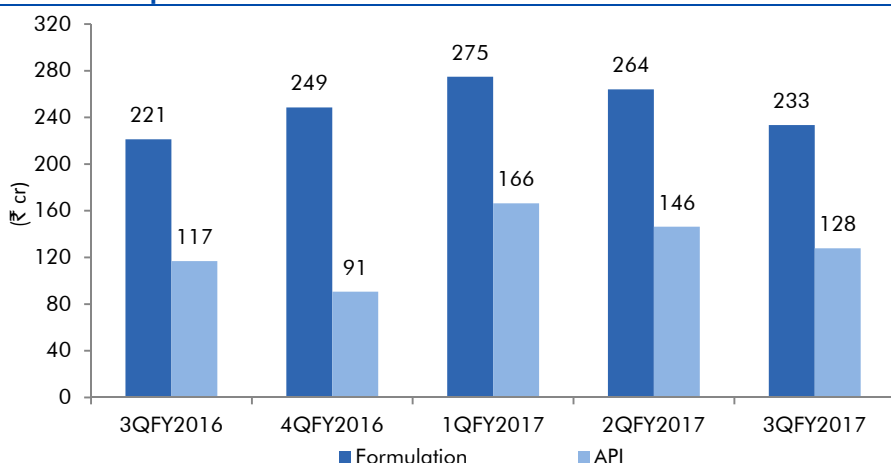
Overall, for 3QFY2017 exports contributed 49.4% to the top-line, while the domestic business contributed the rest. The overall contribution of formulations was at 77.8% of total sales during the quarter. This is against 78.6% in 3QFY2016.

Exhibit 3: Domestic sales trend



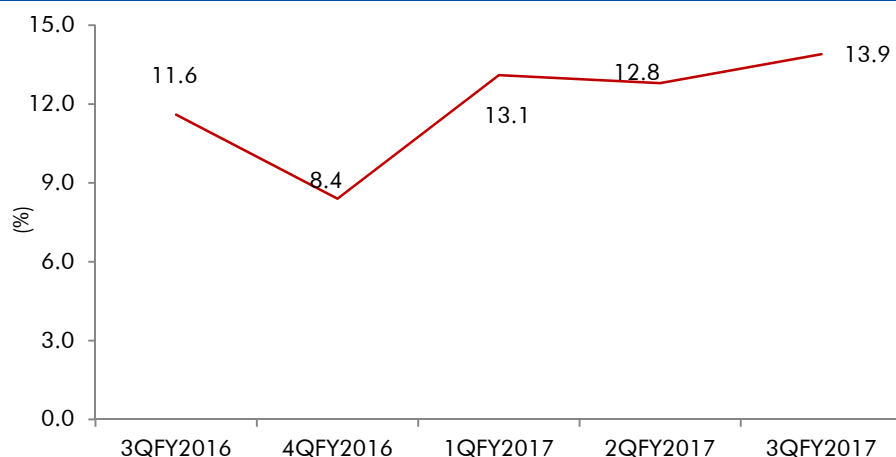
Source: Company, Angel Research

Exhibit 4: Exports sales trend



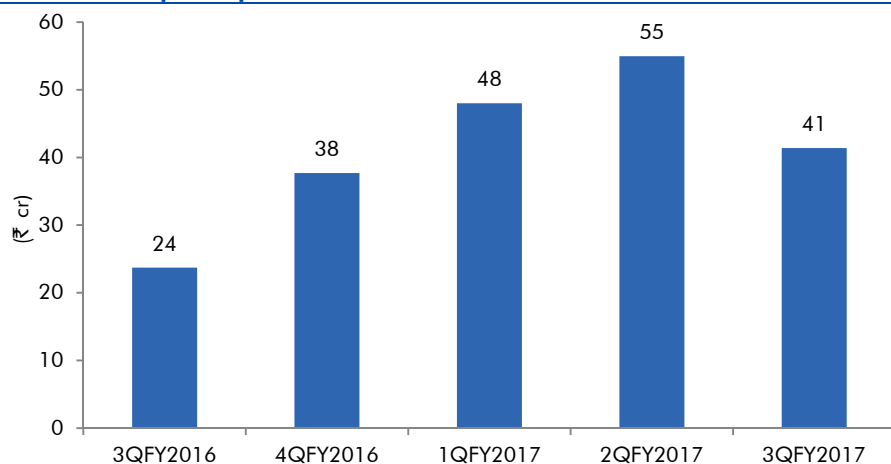
Source: Company, Angel Research

OPM expands yoy; higher than expected: On the operating front, the EBITDA margin came in at 13.9% (v/s. 13.5% expected) v/s. 11.6% in 3QFY2016. While the GPM's (which came in at 66.8% in 3QFY2017 v/s. 62.8% in 3QFY2016), higher expenses during the quarter aided the lower OPM expansion in comparison to the GPM expansion. Other expenses posted a yoy growth of 14.8%.

Exhibit 5: OPM trend


Source: Company, Angel Research

Reported net profit lower than estimates: Consequently, the Adj. PAT came in at ₹41cr (v/s. ₹62cr expected) v/s. ₹24cr in 3QFY2016. Moreover better than expected OPM coupled with lower interest expenses lead the company to post a robust growth during the period.

Exhibit 6: Adj. Net profit trend


Source: Company, Angel Research

Concall Highlights

- IPCA plans to invite USFDA in 4QFY2017 to inspect its two formulations plants (Piparia and Pithampur), Ratlam-based API plant will be offered for re-inspection in 1HFY2018. The company expects remediation cost to decline significantly from 2QFY2018 onwards.
- Plans to file 8-10 ANDAs in FY2018.
- Anti-malaria business in institutional segment is expected to start in FY2018.
- R&D as % of sales stands at 4%; likely to increase to 4.7% in FY2018.
- HCQS production can restart in six months.

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 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. These developments impacted FY2015 sales, while FY2018 should see some revival. We expect exports to grow at a CAGR of 15.0% over FY2016-18E.

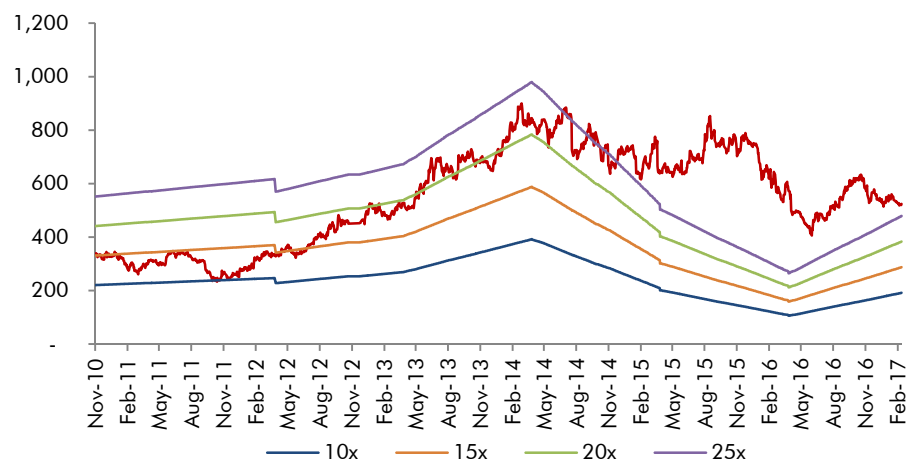
Outlook & Valuation:

We expect net sales to post a CAGR of 14.8% to ₹3,747cr and EPS to register a CAGR of 34.8% to ₹19.2cr 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. However, given the valuations, **we maintain our Accumulate rating on the stock with a target price 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 (%)	12.8	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 (%)	FY2018E			FY16-18E	FY2018E	
					PE (x)	EV/Sales (x)	EV/EBITDA (x)	CAGR in EPS (%)	RoCE (%)	RoE (%)
Alembic Pharma	Neutral	593	-	-	19.5	2.6	12.2	(10.8)	27.5	25.3
Aurobindo Pharma	Buy	686	877	27.9	14.5	2.4	10.1	18.1	22.5	26.1
Cadila Healthcare	Neutral	440	-	-	22.9	3.6	16.6	13.5	23.6	27.1
Cipla	Sell	593	465	(21.5)	24.2	2.7	16.3	14.2	12.2	13.9
Dr Reddy's	Neutral	2,899	-	-	22.1	2.6	11.4	(2.7)	15.3	15.2
Dishman Pharma	Neutral	229	-	-	20.3	2.3	10.0	13.3	10.3	10.9
GSK Pharma*	Neutral	2,683	-	-	44.5	6.8	32.8	16.9	37.5	34.5
Indoco Remedies	Reduce	272	240	(11.8)	17.0	2.0	10.9	33.2	19.1	20.1
Ipca labs	Accumulate	554	613	10.7	28.8	2.0	12.9	34.8	8.6	9.5
Lupin	Buy	1,469	1,809	23.1	21.2	4.0	13.1	17.2	24.4	20.9
Sanofi India	Neutral	4,186	-	-	24.3	3.2	17.4	22.2	25.6	28.8
Sun Pharma	Buy	673	847	25.8	19.1	4.0	12.2	26.5	18.9	20.1

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)	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
Gross sales	2,778	3,232	3,157	2,891	3,310	3,807
Less: Excise duty	25	33	40	47	52	60
Net Sales	2,754	3,199	3,117	2,844	3,258	3,747
Other operating income	59	82	40	41	41	41
Total operating income	2,813	3,282	3,157	2,885	3,299	3,788
% chg	19.3	16.7	(3.8)	(8.6)	14.3	14.8
Total expenditure	2,190	2,471	2,613	2,543	2,843	3,175
Net raw materials	1,097	1,137	1,155	1,058	1,238	1,330
Other mfg costs	245	250	277	253	290	333
Personnel	392	498	565	627	718	826
Other	456	587	616	606	596	686
EBITDA	564	728	504	301	416	572
% chg	19.5	29.1	(30.8)	(40.2)	38.0	37.5
(% of Net Sales)	20.5	22.8	16.2	10.6	12.8	15.3
Depreciation & amortisation	87	103	180	172	233	268
EBIT	477	625	324	129	183	304
% chg	17.8	31.1	(48.1)	(60.2)	41.8	66.2
(% of Net Sales)	17.3	19.5	10.4	4.5	5.6	8.1
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	8.1	5.1
Recurring PBT	517	703	364	155	209	330
% chg	24.0	35.9	(48.2)	(57.5)	34.8	58.0
Extraordinary expense/(Inc.)	63.3	72.2	-	39.5	-	-
PBT (reported)	454	631	364	115	209	330
Tax	129.9	152.4	101.9	18.6	52.2	82.4
(% of PBT)	28.6	24.2	28.0	16.1	25.0	25.0
PAT (reported)	324	478	262	97	156	247
Add: Share of earnings of asso.	-	0	(5)	(3)	-	-
PAT after MI (reported)	324	478	254	94	152	242
ADJ. PAT	340	495	254	133	152	242
% chg	18.4	45.6	(48.6)	(47.6)	14.4	58.9
(% of Net Sales)	11.8	14.9	8.2	3.3	4.7	6.5
Basic EPS (₹)	26.9	39.2	20.1	10.6	12.1	19.2
Fully Diluted EPS (₹)	26.9	39.2	20.1	10.6	12.1	19.2
% chg	18.4	45.6	(48.6)	(47.6)	14.4	58.9

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	2,419	2,646
Shareholders Funds	1,554	1,960	2,208	2,306	2,444	2,671
Minority interest	-	-	-	-	-	-
Total loans	523	603	829	595	725	867
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	3,338	3,708
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	123	142
Current assets	1,397	1,602	1,614	1,522	1,743	2,005
Cash	58	76	125	162	184	220
Loans & advances	42	67	47	43	50	50
Other	1,297	1,459	1,442	1,317	1,509	1,735
Current liabilities	477	485	579	729	835	960
Net Current Assets	921	1,117	1,035	793	908	1,044
Other Non current Assets	-	9	-	-	.	.
Total Assets	2,220	2,726	3,233	3,094	3,338	3,708

Cash flow statement (Consolidated)

Y/E March (₹ cr)	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
Profit before tax	454	631	364	115	209	330
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)	(52)	(82)
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)	130	142
Dividend Paid (Incl. Tax)	(59)	(74)	(15)	(15)	(15)	(15)
Others	72	1	47	(69)	270	(1,314)
Cash Flow from Financing	8	10	264	(316)	385	(1,187)
Inc./Dec.) in Cash	46	18	49	37	22	35
Opening Cash balances	12	58	76	125	162	184
Closing Cash balances	58	76	125	162	184	220

Key Ratios

Y/E March	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
Valuation Ratio (x)						
P/E (on FDEPS)	20.6	14.1	27.5	52.5	45.8	28.8
P/CEPS	16.4	11.7	16.1	22.9	18.1	13.7
P/BV	4.5	3.6	3.2	3.0	2.9	2.6
Dividend yield (%)	0.7	0.9	0.2	0.2	0.2	0.2
EV/Sales	2.7	2.3	2.4	2.6	2.2	2.0
EV/EBITDA	13.1	10.2	15.1	24.4	17.0	13.1
EV / Total Assets	3.3	2.7	2.4	2.4	2.1	2.0
Per Share Data (₹)						
EPS (Basic)	26.9	39.2	20.1	10.6	12.1	19.2
EPS (fully diluted)	26.9	39.2	20.1	10.6	12.1	19.2
Cash EPS	33.8	47.4	34.4	24.2	30.5	40.4
DPS	4.0	5.0	1.0	1.0	1.0	1.0
Book Value	123.1	155.3	175.0	182.7	193.6	211.7
DuPont Analysis						
EBIT margin	17.3	19.5	10.4	4.5	5.6	8.1
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	1.1
ROIC (Post-tax)	17.2	20.2	8.2	3.6	4.5	6.6
Cost of Debt (Post Tax)	4.5	3.6	2.9	3.7	3.6	3.0
Leverage (x)	0.4	0.3	0.3	0.3	0.2	0.3
Operating ROE	21.8	24.9	9.8	3.6	4.6	7.6
Returns (%)						
RoCE (Pre-tax)	23.2	25.3	10.9	4.1	5.7	8.6
Angel RoIC (Pre-tax)	25.0	27.7	12.0	4.5	6.2	9.2
RoE	24.2	28.2	12.2	5.9	6.4	9.5
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	59	60
WC cycle (ex-cash) (days)	106	106	113	97	82	89
Solvency ratios (x)						
Net debt to equity	0.3	0.3	0.3	0.2	0.3	0.2
Net debt to EBITDA	0.8	0.7	1.4	1.4	1.5	1.1
Int. Coverage (EBIT / Int.)						

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Ipca Laboratories

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)