

Indoco Remedies

Performance Highlights

Y/E March (₹ cr)	3QFY17	2QFY17	% chg (qoq)	3QFY16	% chg (yoy)
Net sales	272	276	(1.5)	256	6.2
Other operating income	7	6	26.2	4	68.7
Gross profit	174	179	(3.0)	162	7.6
Operating profit	34	37	(9.2)	39	(13.4)
Net profit	18	22	(20.5)	19	(7.3)

Source: Company, Angel Research

Indoco Remedies posted lower than expected numbers for 3QFY2017. In sales, the company posted revenues of ₹272cr (₹276cr expected) v/s ₹256cr in 3QFY2016, growth of 6.2% yoy. The lower growth was on the back of the formulation business at ₹252.2cr, up 4.5% yoy, API at ₹18.2cr up 32.8% yoy. The domestic formulation at ₹144.2cr recorded a yoy growth of 5.2%. On EBITDA front, the company posted an EBITDA of 12.4% (14.5% expected) v/s 15.4% in 3QFY2016. The dip came in on the back of the high R&D expenses, which came in at 5.1% of sales v/s 3.5% of sales in 3QFY2016. Consequently, PAT came in at ₹18cr (lower than expectations) v/s ₹19cr in 3QFY2016, de-growth of 7.3% yoy.

On the back of valuations, we maintain our Reduce stance on the stock.

Results lower than expected: Indoco Remedies posted numbers lower than expectations. In sales, the company posted revenues of ₹272cr (₹276cr expected) v/s ₹255cr in 3QFY2016, growth of 6.2% yoy. The low growth was on back of the formulation business at ₹252.2cr, up 4.5% yoy, API at ₹18.2cr up 32.8% yoy. The domestic formulation at ₹144.2cr recorded a yoy growth of 5.2%. On EBITDA front, the company posted an EBITDA of 12.4% (14.5% expected) v/s 15.4% in 3QFY2016. The dip came in on the back of the high R&D expenses, which came in at 5.1% of sales v/s 3.5% of sales in 3QFY2016. Consequently, PAT came in at ₹18cr (lower than expectations) v/s ₹19cr in 3QFY2016, de-growth of 7.3% yoy.

Outlook and valuation: We expect net sales to post a CAGR of 14.9% to ₹1,289cr and EPS to post a CAGR of 33.2% to ₹16 over FY2016-18E. At the current market price, the stock is trading at 23.8x and 17.2x its FY2017E and FY2018E earnings, respectively. **We maintain our reduce rating on back of the valuations.**

Key financials (Consolidated)

Y/E March (₹ cr)	FY2015	FY2016	FY2017E	FY2018E
Net sales	852	977	1112	1289
% chg	18.0	14.6	13.8	16.0
Net profit	82.8	83.0	106.6	147.1
% chg	42.3	0.2	28.4	38.0
EPS (₹)	9.0	9.0	11.6	16.0
EBITDA margin (%)	18.9	14.9	16.2	18.2
P/E (x)	30.6	30.5	23.8	17.2
RoE (%)	17.0	15.1	17.0	20.1
RoCE (%)	18.3	11.9	14.4	19.1
P/BV (x)	4.9	4.3	3.8	3.2
EV/Sales (x)	3.1	2.7	2.4	2.0
EV/EBITDA (x)	16.2	18.2	14.8	11.0

Source: Company, Angel Research; Note: CMP as of January 27, 2017

REDUCE

CMP	₹275
Target Price	₹240

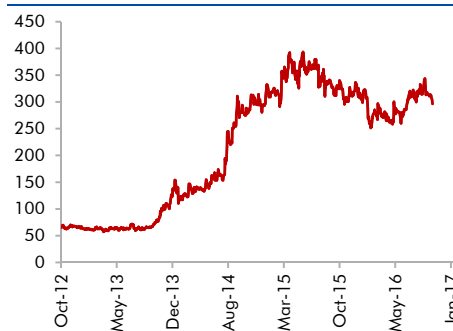
Investment Period	-
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Stock Info	
Sector	Pharmaceutical
Market Cap (₹ cr)	2,533
Net Debt (₹ cr)	73
Beta	0.4
52 Week High / Low	360/244
Avg. Daily Volume	10,283
Face Value (₹)	2
BSE Sensex	27,882
Nifty	8,641
Reuters Code	INRM.BO
Bloomberg Code	INDR@IN

Shareholding Pattern (%)	
Promoters	59.2
MF / Banks / Indian Fls	11.3
FII / NRIs / OCBs	13.0
Indian Public / Others	16.5

Abs. (%)	3m	1yr	3yr
Sensex	(0.1)	13.8	34.6
Indoco	(4.8)	(13.8)	126.9

3-Year Daily Price Chart



Source: Company, Angel Research

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Exhibit 1: 3QFY2017 (Consolidated) performance

Y/E March (₹ cr)	3QFY2017	2QFY2017	% chg (qoq)	3QFY2016	% chg (yoy)	9MFY2017	9MFY2016	% chg (yoy)
Net sales	272	276	(1.5)	256	6.2	801	723	10.8
Other income	7.1	5.6	26.2	4	68.7	18	19	(8.5)
Total income	279	282	(1.0)	261	7.2	819	742	10.3
Gross profit	174	179	(3.0)	162	7.6	517	459	12.6
Gross margins (%)	63.9	64.9		63.0		64.5	63.5	
Operating profit	33.9	37.3	(9.2)	39.1	(13.4)	108.0	111.4	(3.1)
OPM (%)	12.4	13.5		15.3		13.5	15.4	
Interest	3	2	86.6	6	(47.9)	7	10	(28.4)
Dep & amortisation	14	17	(13.8)	15	(5.6)	48	45	6.1
PBT	24	25	(4.2)	22	5.4	71	76	(6.7)
Provision for taxation	5.8	2.6	122.8	3	84.3	11	15	(22.1)
Reported Net profit	18	22	(20.5)	19	(7.3)	60	61	(3.0)
Less : Exceptional items	0	0	-	0		0	0	
PAT after exceptional items	18	22	(20.5)	19	(7.3)	60	61	(3.0)
EPS (₹)	1.9	2.4		2.1		6.5	6.7	

Source: Company, Angel Research

Exhibit 2: 3QFY2017 – Actual vs. Angel estimates

(₹ cr)	Actual	Estimate	Variation (%)
Net sales	272	276	(1.5)
Other operating income	7	6	27.1
Operating profit	34	40	(15.5)
Tax	6	3	121.9
Net profit	18	25	(29.1)

Source: Company, Angel Research

Revenues below expectations: In sales, the company posted revenues of ₹272cr (₹276cr expected) v/s ₹255cr in 3QFY2016, growth of 6.9% yoy. The lower growth was on the back of the formulation business at ₹252.2cr, up 4.5% yoy, API at ₹18.2cr up 32.8% yoy. The domestic formulation at ₹144.2cr recorded a yoy growth of 5.2%.

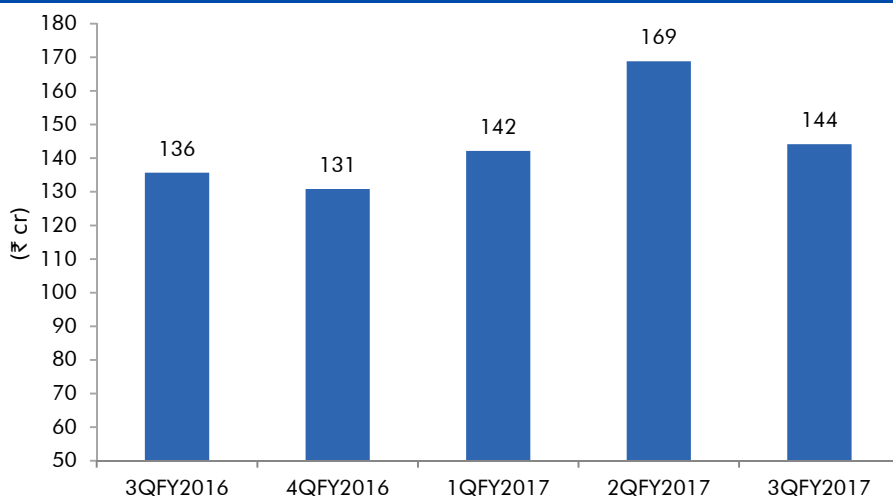
Domestic Formulation markets (₹144cr) posted a growth of 5.2% yoy, mainly, while API sales (₹5.7cr) posted a dip of 11.6% yoy. Exports Formulations (₹108cr) grew 3.6% yoy, while API exports (₹12.5cr) grew 72.4% yoy. Europe contributed 34.9% of International formulation sales, followed by US at 31.5%, South Africa, Australia & New Zealand at 18.4% and Emerging markets at 15.3%.

During the quarter, the revenues grew by 27.5 % at ₹37.8cr as against ₹29.7cr for the same period last year. YTD, the revenue grew by 17.9% at ₹92.1cr as against ₹78.2cr for the same period last year. The company is awaiting Establishment Inspection Report (EIR) from the USFDA for its Goa Plant II & III for the audit conducted in the month of September 2016.

In terms of filings, the company (through partners or by itself), filed 25 ANDAs which are pending approvals with 10 ANDAs approved till date.

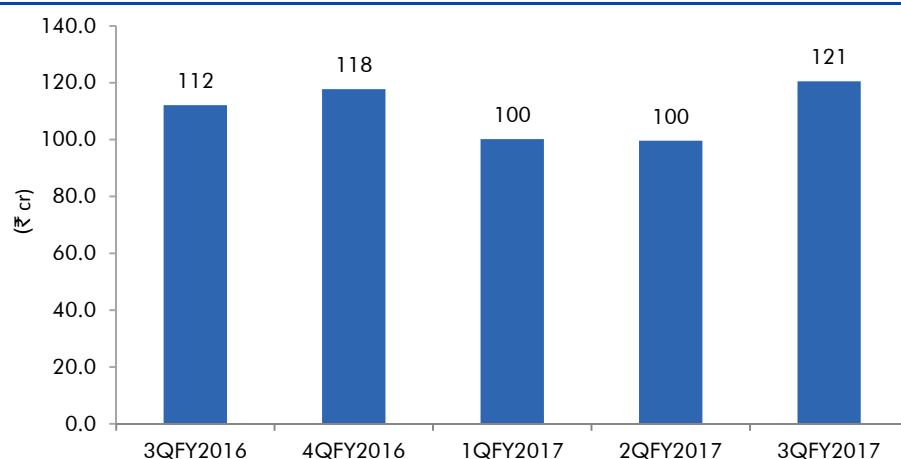
The revenues for the quarter grew by 18.1% at ₹16.4cr, as against ₹13.9cr for the same period last year. YTD to date, the revenues grew by 32.7% at ₹44.7cr as against ₹ 33.7cr.

Exhibit 3: Domestic Formulation sales trend



Source: Company, Angel research

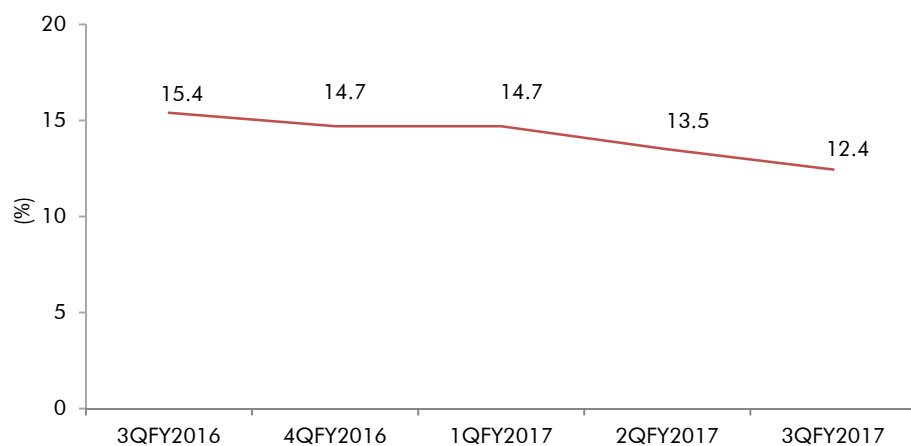
Exhibit 4: Export sales trend



Source: Company, Angel research

OPM lower than estimated: On EBITDA front, the company posted an EBITDA of 12.4% (14.5% expected) v/s 15.4% in 3QFY2016. The dip came in on back of the high R&D expenses, which came in at 5.1% of sales v/s 3.5% of sales in 3QFY2016.

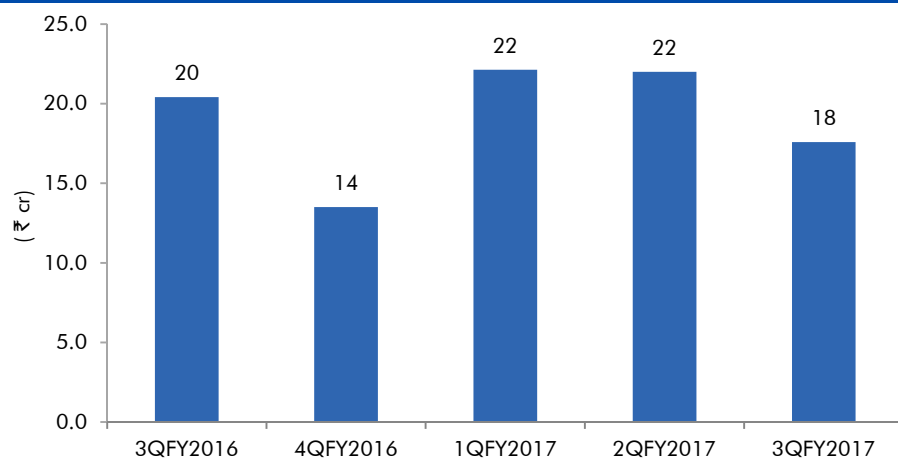
Exhibit 5: OPM trend



Source: Company, Angel Research

Net profit lower than expectation: Consequently, PAT came in at ₹18cr (lower than expectations) v/s ₹20.4cr in 3QFY2016, de-growth of 7.3% yoy. The lower than expected net profit is on back of lower than expected sales and OPM.

Exhibit 6: Net profit trend



Source: Company, Angel Research

Concall takeaways

- The company has re-structured some of its marketing divisions in domestic markets with addition to the field force to accelerate growth and build on its core strengths in the mass speciality segments.
- Going forward, the company's business from US and EU territory is expected to grow at a fast pace, as ANDAs and Dossiers will be commercialized at regular intervals.
- While surging ahead in the regulated markets, Indoco is also consolidating its position in the emerging markets through active brand promotion. Part of the emerging market is exploited through distributors appointed by Indoco and part through alliances.

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.

Post the restructuring of the domestic business in FY2009, which has resulted in an improvement in the working capital cycle, Indoco is back on the growth trajectory with its domestic formulation business growing at 15.1% in FY2015. We expect the domestic formulation segment to grow at a CAGR of 15.0% over FY2016-18E, factoring in a muted FY2016, restructuring, and low monsoon.

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 ~46% of its revenues from exports in 2015-16.

The US cumulative ANDA filings stood at 34 with 26 pending approvals (including 3 tentative approvals). 54 products are under the development pipeline for the US. The company has launched 8 products in the US market (five ophthalmic, one solid dosage and two products supplied by Watson). A total of 14 products have been filed through Watson. We expect the exports segment to grow at an 18.1% CAGR over FY2016-18E.

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. The company 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.

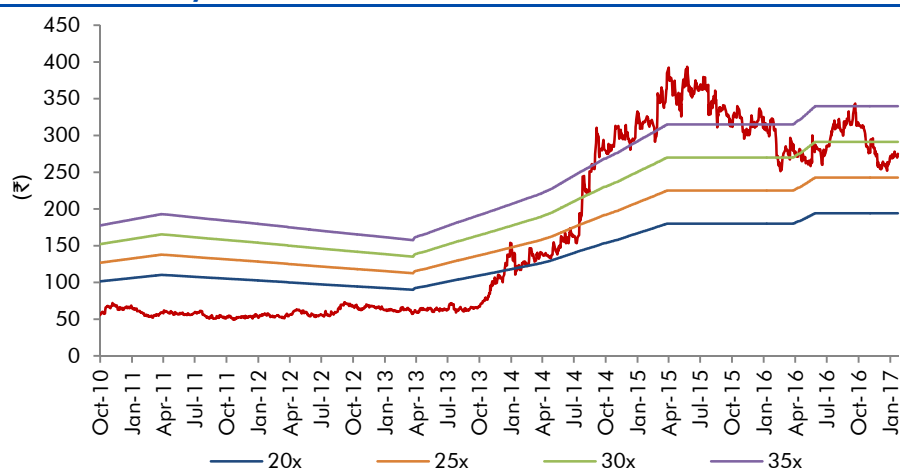
Valuation: We expect net sales to post a CAGR of 14.9% to ₹1,289cr and EPS to post a CAGR of 33.2% to ₹16.0 over FY2016-18E. At the current market price, the stock is trading at 23.8x and 17.2x its FY2017E and FY2018E earnings, respectively. **We recommend a reduce rating on back of the valuations.**

Exhibit 7: Key assumptions

	FY2017E	FY2018E
Domestic sales growth (%)	15.0	15.0
Exports growth	18.0	18.0
Operating margins (%)	18.2	18.2
Capex (₹ cr)	60.0	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 (%)	FY2017E			FY15-17E	FY2017E	
					PE (x)	EV/Sales (x)	EV/EBITDA (x)	CAGR in EPS (%)	RoCE (%)	RoE (%)
Alembic Pharma	Neutral	575	-	-	18.9	2.5	11.8	(10.8)	27.5	25.3
Aurobindo Pharma	Accumulate	713	877	22.9	15.1	2.5	10.5	18.1	22.5	26.1
Cadila Healthcare	Accumulate	363	400	10.3	18.9	2.9	13.2	13.4	22.7	25.7
Cipla	Sell	580	490	(15.6)	21.3	2.7	14.7	20.4	13.5	15.2
Dr Reddy's	Neutral	2,999	-	-	21.0	2.7	10.2	1.7	16.2	15.9
Dishman Pharma	Neutral	234	-	-	20.7	2.3	10.2	13.3	10.3	10.9
GSK Pharma	Neutral	2,732	-	-	44.9	6.8	33.0	17.3	35.3	32.1
Indoco Remedies	Reduce	275	240	(12.7)	17.2	2.0	11.0	33.2	19.1	20.1
Ipsca labs	Accumulate	537	613	14.2	27.3	1.9	12.4	36.5	8.8	9.4
Lupin	Buy	1,492	1,809	21.3	21.5	3.5	13.3	17.2	24.4	20.9
Sanofi India*	Neutral	4,181	-	-	24.3	3.2	17.3	22.2	25.6	28.8
Sun Pharma	Buy	640	847	32.4	18.1	3.5	11.5	26.5	18.9	20.1

Source: Company, Angel Research; Note: *December year ending, Price as of January 27, 2017

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 Sensoform. 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)	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
Gross sales	638	735	863	987	1,124	1,303
Less: Excise duty	11	13	11	10	12	14
Net sales	626	722	852	977	1,112	1,289
Other operating income	4	10	5	27	27	27
Total operating income	630	733	857	1,004	1,139	1,316
% chg	10.4	16.2	17.0	17.1	13.5	15.6
Total expenditure	537	612	691	831	932	1,055
Net raw materials	262	272	300	341	434	477
Other mfg costs	37	42	50	57	65	75
Personnel	100	130	140	183	199	231
Other	138	168	201	250	234	272
EBITDA	89	110	161	145	180	234
% chg	5.4	23.5	46.1	(9.7)	23.7	30.3
(% of Net Sales)	14.2	15.2	18.9	14.9	16.2	18.2
Depreciation & amortisation	24	31	47	60	65	70
EBIT	65	79	114	85	114	164
% chg	0.1	21.0	43.7	(25.4)	34.7	43.3
(% of Net Sales)	10.4	11.0	13.3	8.7	10.3	12.7
Interest & other charges	22	19	11	13	13	13
Other income	1	2	2	1	1	1
(% of PBT)	1.8	2.4	1.6	1.1	0.9	0.6
Share in profit of Associates	-	-	-	1.0	2.0	3.0
Recurring PBT	48	72	110	101	130	179
PBT (reported)	48	72	110	101	130	179
Tax	6	14	27	18	23	32
(% of PBT)	11.8	19.6	24.3	17.5	18.0	18.0
PAT (reported)	43	58	83	83	107	147
Add: Share of earnings of asso.	-	-	-	-	-	-
Less: Minority interest (MI)	-	-	-	-	-	-
Prior period items	-	-	-	-	-	-
PAT after MI (reported)	43	58	83	83	107	147
ADJ. PAT	43	58	83	83	107	147
% chg	(7.9)	36.5	42.3	0.2	28.4	38.0
(% of Net Sales)	6.8	8.1	9.7	8.5	9.6	11.4
Basic EPS (₹)	4.6	6.3	9.0	9.0	11.6	16.0
Fully Diluted EPS (₹)	4.6	6.3	9.0	9.0	11.6	16.0
% chg	(7.9)	36.5	42.3	0.2	28.4	38.0

Balance Sheet (Consolidated)

Y/E March (₹ cr)	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
SOURCES OF FUNDS						
Equity share capital	18	18	18	18	18	18
Reserves & surplus	396	439	500	566	652	778
Shareholders funds	414	457	519	583	669	796
Minority Interest	0	-	-	-	-	-
Total loans	90	72	88	127	130	70
Other Long Term Liab.	9	9	9	9	9	9
Long Term Provisions	7	16	16	18	18	18
Deferred tax liability	35	31	27	24	24	24
Total liabilities	555	585	659	762	824	890
APPLICATION OF FUNDS						
Gross block	447	481	561	649	709	769
Less: acc. depreciation	126	156	203	264	329	399
Net block	321	325	358	386	380	370
Capital work-in-progress	38	44	44	44	44	44
Goodwill	0	-	0	-	-	-
Investments	0	0	0	15	15	15
Long Term Loans And Adv.	57	55	58	71	109	126
Current assets	273	305	385	448	549	653
Cash	12	13	15	14	8	25
Loans & advances	41	42	85	78	111	129
Other	220	249	285	356	430	499
Current liabilities	134	144	187	201	274	318
Net current assets	139	160	199	247	275	335
Mis. Exp. not written off	0	-	-	-	-	-
Total assets	555	585	659	762	824	890

Cash Flow Statement (Consolidated)

Y/E March (₹ cr)	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
Profit before tax	48	72	110	101	130	179
Depreciation	24	31	47	60	65	70
(Inc)/Dec in working capital	13	(18)	(39)	(63)	(73)	(60)
Less: Other income	1	2	2	1	1	1
Direct taxes paid	6	14	27	18	23	32
Cash Flow from Operations	79	69	90	80	98	156
(Inc.)/Dec.in fixed assets	(49)	(41)	(80)	(88)	(60)	(60)
(Inc.)/Dec. in investments	-	-	-	-	-	-
Other income	1	2	2	1	1	1
Cash Flow from Investing	(48)	(39)	(78)	(87)	(59)	(59)
Issue of equity	-	-	-	(1)	-	-
Inc./Dec.) in loans	(22)	(9)	16	41	3	(60)
Dividend Paid (Incl. Tax)	(12)	(12)	(22)	(21)	(21)	(21)
Others	3	(16)	(3)	(15)	9	-
Cash Flow from Financing	(30)	(37)	(9)	5	(9)	(81)
Inc./Dec.) in Cash	1	(7)	3	(2)	30	17
Opening Cash balances	10	12	13	15	14	8
Closing Cash balances	12	13	15	14	8	25

Key Ratios

Y/E March	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
Valuation Ratio (x)						
P/E (on FDEPS)	59.4	43.5	30.6	30.5	23.8	17.2
P/CEPS	38.2	28.4	19.5	17.7	14.7	11.6
P/BV	6.1	5.5	4.9	4.3	3.8	3.2
Dividend yield (%)	0.4	0.4	0.7	0.7	0.7	0.7
EV/Sales	4.2	3.6	3.1	2.7	2.4	2.0
EV/EBITDA	29.3	23.6	16.2	18.2	14.8	11.0
EV / Total Assets	4.7	4.4	4.0	3.5	3.2	2.9
Per Share Data (₹)						
EPS (Basic)	4.6	6.3	9.0	9.0	11.6	16.0
EPS (fully diluted)	4.6	6.3	9.0	9.0	11.6	16.0
Cash EPS	7.2	9.7	14.1	15.6	18.7	23.6
DPS	1.1	1.0	2.0	2.0	2.0	2.0
Book Value	44.9	49.6	56.3	63.3	72.6	86.4
Dupont Analysis						
EBIT margin	10.4	11.0	13.3	8.7	10.3	12.7
Tax retention ratio	88.2	80.4	75.7	82.5	82.0	82.0
Asset turnover (x)	1.2	1.3	1.4	1.4	1.5	1.6
ROIC (Post-tax)	10.8	11.6	14.2	10.3	12.3	16.3
Cost of Debt (Post Tax)	18.9	18.7	10.0	9.6	8.0	10.3
Leverage (x)	0.2	0.2	0.1	0.2	0.2	0.1
Operating ROE	8.9	10.4	14.8	10.5	13.1	17.0
Returns (%)						
ROCE (Pre-tax)	11.9	13.9	18.3	11.9	14.4	19.1
Angel ROIC (Pre-tax)	13.0	15.3	20.2	13.0	15.5	20.5
ROE	10.7	13.4	17.0	15.1	17.0	20.1
Turnover ratios (x)						
Asset Turnover (Gross Block)	1.5	1.6	1.6	1.7	1.7	1.8
Inventory / Sales (days)	52	50	55	54	58	60
Receivables (days)	66	64	62	68	74	76
Payables (days)	43	40	46	42	50	52
WC cycle (ex-cash) (days)	78	68	70	76	80	80
Solvency ratios (x)						
Net debt to equity	0.2	0.1	0.1	0.2	0.2	0.1
Net debt to EBITDA	0.9	0.5	0.5	0.8	0.7	0.2
Interest Coverage (EBIT / Int.)	3.0	4.2	10.7	6.8	9.1	13.1

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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)