

Indoco Remedies

Performance Highlights

Y/E March (₹ cr)	4QFY16	3QFY16	% chg (qoq)	4QFY15	% chg (yoy)
Net sales	255	255	0.1	212	20.5
Other operating income	9	4	113.7	(1)	(788.5)
Gross profit	173	162	6.3	143	20.6
Operating profit	32	39	(17.3)	39	(17.0)
Net profit	20	20	(2.0)	19	6.7

Source: Company, Angel Research

Indoco Remedies (Indoco) results for 4QFY2016 have come in much below our expectations. The company posted a 20.5% yoy growth in sales to ₹255cr, although the same is lower than our expectation of ₹300cr. The growth was mainly driven by exports (₹117.8cr), which grew by 43.8% yoy, while domestic sales (₹136.3cr) rose 5.6% yoy. On the operating front, the EBDITA margin for the quarter came in at 12.7% V/s 18.4% in 4QFY2015. The reported net profit came in at ₹20cr V/s ₹18.8cr in 4QFY2015, registering a yoy growth of 6.7%. **We recommend a SELL on the stock, on back of the valuations.**

Results lower than expected: The company posted a 20.5% yoy growth in sales for the quarter to ₹255cr, although the same is lower than our expectation of ₹300cr. The growth was mainly driven by exports (₹117.8cr), which grew by 43.8% yoy, while domestic sales (₹136.3cr) rose 5.6% yoy. Export sales were driven by a 47.3% yoy growth in Formulation exports (₹110.5cr) while domestic formulation sales (₹130.8cr) rose 6.4% yoy. On the operating front, the gross margin for the quarter came in at 67.7% V/s 67.6% in 4QFY2015, while the EBDITA margin came in at 12.7% V/s 18.4% in 4QFY2015. The reported net profit came in at ₹20cr V/s ₹18.8cr in 4QFY2015, i.e. a yoy growth of 6.7%. This was however lower than our expectation of a net profit of ₹35cr for the quarter.

Outlook and valuation: We expect net sales to post a 14.9% CAGR to ₹1,289cr and EPS to post a 31.5% CAGR to ₹15.6 over FY2016-18E. At the current market price, the stock is trading at 21.3x and 18.1x its FY2017E and FY2018E earnings, respectively. **We recommend a SELL, given the expensive valuations.**

Key financials (Consolidated)

Y/E March (₹ cr)	FY2015	FY2016	FY2017E	FY2018E
Net sales	852.2	976.6	1111.7	1289.2
% chg	18.0	14.6	13.8	16.0
Net profit	82.8	83.0	121.8	143.5
% chg	42.3	0.2	46.7	17.9
EPS (₹)	9.0	9.0	13.2	15.6
EBITDA margin (%)	18.9	14.9	18.2	18.2
P/E (x)	31.4	31.3	21.3	18.1
RoE (%)	17.0	15.1	19.2	19.2
RoCE (%)	18.3	11.9	17.1	19.1
P/BV (x)	5.0	4.5	3.8	3.2
EV/Sales (x)	3.1	2.8	2.4	2.0
EV/EBITDA (x)	16.6	18.7	13.4	11.2

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

Please refer to important disclosures at the end of this report

SELL

CMP	₹282
Target Price	₹225

Investment Period	-
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Stock Info	
Sector	Pharmaceutical
Market Cap (₹ cr)	2,597
Net Debt (₹ cr)	113
Beta	0.7
52 Week High / Low	396/244
Avg. Daily Volume	15,102
Face Value (₹)	2
BSE Sensex	27,010
Nifty	8,266
Reuters Code	INRM.BO
Bloomberg Code	INDR@IN

Shareholding Pattern (%)	
Promoters	59.3
MF / Banks / Indian Fls	11.5
FII / NRIs / OCBs	12.2
Indian Public / Others	17.0

Abs. (%)	3m	1yr	3yr
Sensex	9.6	0.9	39.0
Indoco	1.9	(22.6)	343.9

3-Year Daily Price Chart



Source: Company, Angel Research

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Exhibit 1: 4QFY2016 (Consolidated) performance

Y/E March (₹ cr)	4QFY2016	3QFY2016	% chg (qoq)	4QFY2015	% chg (yoy)	FY2016	FY2015	% chg (yoy)
Net sales	255	255	0.1	212	20.5	977	849	15.0
Other income	9.0	4.2	113.7	(1)	(788.5)	28	7	304.4
Total income	264	259	2.0	210	25.5	1,005	856	17.4
Gross profit	173	162	6.3	143	20.6	635	550	15.5
Gross margins (%)	67.7	63.7		67.6		65.0	64.8	
Operating profit	32.3	39.1	(17.3)	39.0	(17.0)	145.2	160.4	(9.5)
OPM (%)	12.7	15.4		18.4		14.9	18.9	
Interest	5	3	64.7	2	110.9	13	10	25.1
Dep & amortisation	15	15	0.1	13	21.9	60	47	28.4
PBT	21	25	(15.2)	23	(6.5)	101	110	(8.9)
Provision for taxation	1.4	4.9	(70.4)	4	(65.6)	18	27	(34.8)
Reported Net profit	20	20	(2.0)	19	6.7	83	83	0.6
Less : Exceptional items	0	0	-	0		0	0	
PAT after exceptional items	20	20	(2.0)	19	6.7	83	83	0.6
EPS (₹)	2.2	2.2		2.0		9.0	9.0	

Source: Company, Angel Research

Exhibit 2: 4QFY2016 – Actual vs. Angel estimates

(₹ cr)	Actual	Estimate	Variation (%)
Net sales	255	300	(15.1)
Other operating income	4	4	0.5
Operating profit	39	57	(31.4)
Tax	5	9	(43.8)
Net profit	20	35	(40.9)

Source: Company, Angel Research

Revenues below our expectation: For 4QFY2016, Indoco Remedies posted a 20.5% yoy growth in sales to ₹255cr, although the same is lower than our expectation of ₹300cr. The growth was mainly driven by exports (₹117.8cr), which grew by 43.8% yoy, while domestic sales (₹136.3cr) rose 5.6% yoy. Export sales were driven by a 47.3% yoy growth in Formulation exports (₹110.5cr) while domestic formulation sales (₹130.8cr) rose 6.4% yoy.

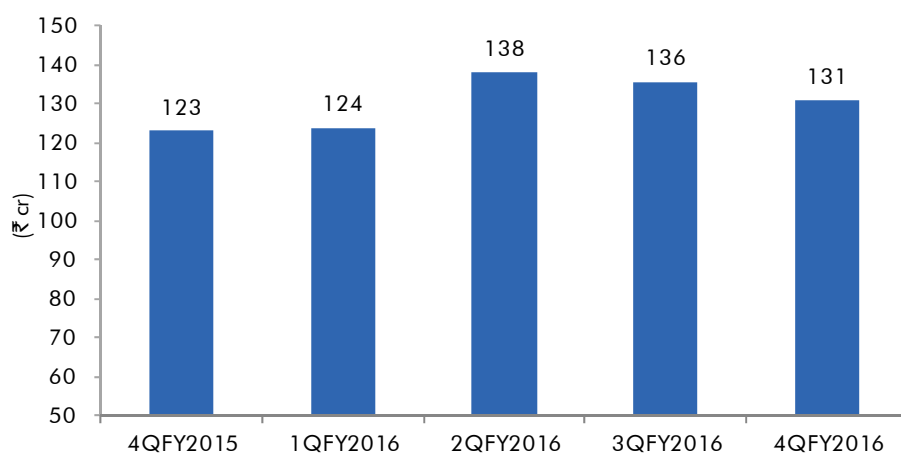
Domestic markets (₹136.3cr) posted a growth of 5.6% yoy, mainly driven by formulation sales (₹130.8cr; up 6.4% yoy), while API sales (₹5.49cr) posted a dip of 10.6% yoy. The top-10 therapies of the company contributed by 88.3% to the IPM market.

Exports (₹118cr) grew 43.8% yoy on back of formulation exports (₹110cr; up 47.3% yoy), while API exports (₹6.5cr) de-grew by 5.0% yoy. The regulated markets grew by 52.5% yoy to ₹95.1cr during the quarter as against ₹62.4cr during the same quarter last year.

During the quarter, the company's US business grew by 69.5% yoy with revenues at ₹28.4cr. The company (through partners or by itself) filed 23 ANDAs with 8 ANDAs approved till date. There are 54 under the pipeline for the company.

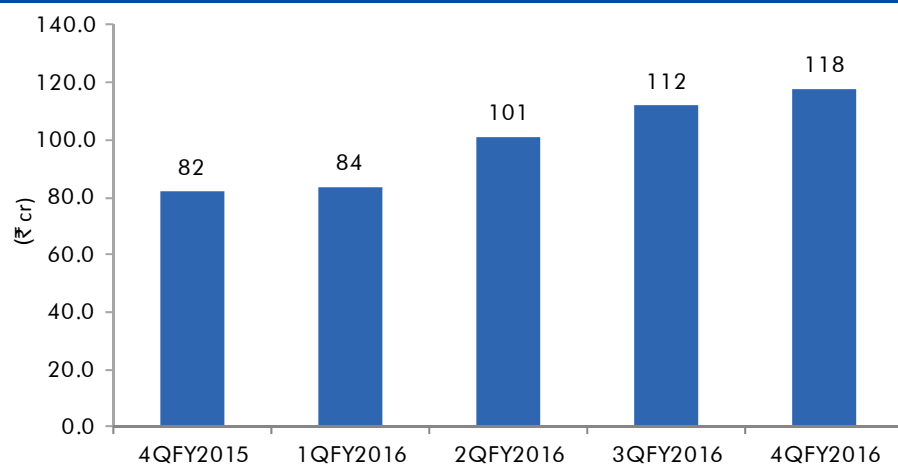
For the quarter, the emerging markets grew by 22.0% to ₹15.4cr as against ₹12.6cr during the same quarter last year. Kenya, French West Africa, Uganda, Tanzania and Myanmar drove sales during the quarter.

Exhibit 3: Domestic Formulation sales trend



Source: Company, Angel research

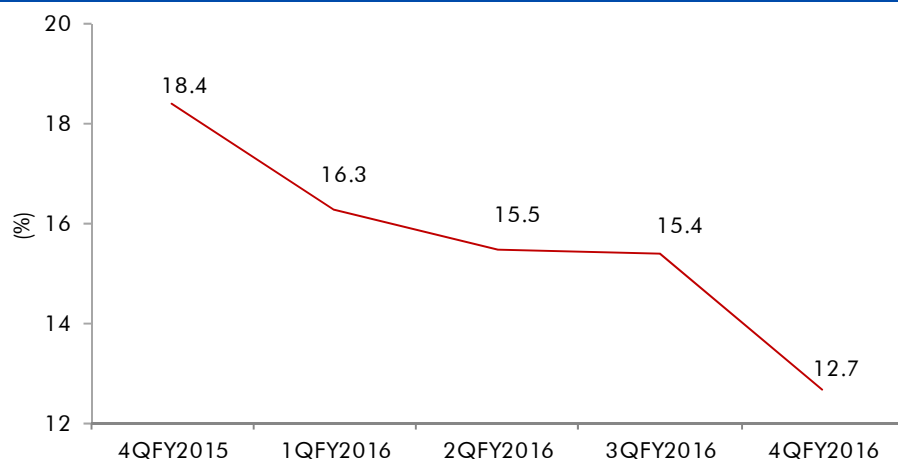
Exhibit 4: Export sales trend



Source: Company, Angel research

OPM lower than estimated: On the operating front, the gross margin for the quarter came in at 67.7% V/s 67.6% in 4QFY2015, while the EBDITA margin came in at 12.7% V/s 18.4% in 4QFY2015. The margins came under pressure owing to a 153.7% yoy rise in the R&D expenditure.

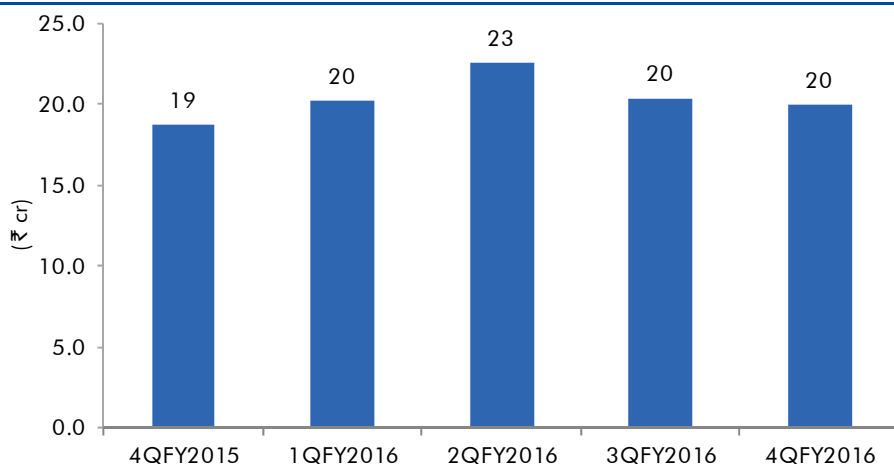
Exhibit 5: OPM trend



Source: Company, Angel Research

Net profit lower than expectation: The reported net profit grew 6.7% yoy to ₹20cr V/s ₹18.8cr in 4QFY2015.

Exhibit 6: Net profit trend



Source: Company, Angel Research

Concall Highlights

- As per the Management, the proposed ban on fixed dose combinations (FDCs; accounting for 2-3% of domestic sales) would have an minimal impact on the company’s sales.
- 9.5-10% of the company’s domestic portfolio is currently under NLEM.
- The company has guided for ~15% growth in the domestic market for FY2017.
- Watson contributed ~US\$3mn to the company’s revenues in FY2016; Aspen has filed for 22 products with MCC, the regulatory authority of South Africa. For FY2016, Aspen generated sales of ₹20cr.
- The company received the Establishment Inspection Report (EIR) on 25th May, 2016 from the USFDA for its sterile and solid dosage facility (Goa Plant II).

The company also received the EIR from USFDA for its Goa Plant I (solid dosages facility) and Goa Plant III.

- The company expects US revenues to be ~₹150cr for FY2017.
- As per the company, the approvals expected in FY2017 have an addressable market size of ~US\$800mn.
- The company expects international sales to grow at 30-35% in FY2017.
Overall, the company expects a high teen growth in revenues in FY2017.

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 (5 Ophthalmic, 1 solid dosage and 2 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 14.9% CAGR to ₹1,289cr and EPS to post a 31.5% CAGR to ₹15.6 over FY2016-18E. At the current market price, the stock is trading at 21.3x and 18.1x its FY2017E and FY2018E earnings, respectively. **We recommend a SELL rating on the stock, given 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 (%)	PE (x)	FY2017E		FY15-17E		FY2017E	
						EV/Sales (x)	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	Accum.	773	850	10.0	18.7	3.1	13.1	6.9	24.0	29.6	
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	Accum.	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	SELL	282	225	(20.2)	21.3	2.4	13.4	8.6	17.1	19.2	
Ipca labs	Buy	431	750	74.0	15.4	1.6	8.8	17.9	11.8	14.9	
Lupin	Buy	1,435	1,809	26.1	24.7	4.1	15.6	13.1	29.6	24.7	
Sanofi India*	Accum.	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

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	910	1,055
Net raw materials	262	272	300	341	411	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	202	234
% chg	5.4	23.5	46.1	(9.7)	39.0	16.0
(% of Net Sales)	14.2	15.2	18.9	14.9	18.2	18.2
Depreciation & amortisation	24	31	47	60	65	70
EBIT	65	79	114	85	136	164
% chg	0.1	21.0	43.7	(25.4)	60.9	20.0
(% of Net Sales)	10.4	11.0	13.3	8.7	12.3	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	0.7	0.6
Share in profit of Associates	-	-	-	1.0	2.0	3.0
Recurring PBT	48	72	110	101	152	179
PBT (reported)	48	72	110	101	152	179
Tax	6	14	27	18	30	36
(% of PBT)	11.8	19.6	24.3	17.5	20.0	20.0
PAT (reported)	43	58	83	83	122	144
Add: Share of earnings of asso.	-	-	-	-	-	-
Less: Minority interest (MI)	-	-	-	-	-	-
Prior period items	-	-	-	-	-	-
PAT after MI (reported)	43	58	83	83	122	144
ADJ. PAT	43	58	83	83	122	144
% chg	(7.9)	36.5	42.3	0.2	46.7	17.9
(% of Net Sales)	6.8	8.1	9.7	8.5	11.0	11.1
Basic EPS (₹)	4.6	6.3	9.0	9.0	13.2	15.6
Fully Diluted EPS (₹)	4.6	6.3	9.0	9.0	13.2	15.6
% chg	(7.9)	36.5	42.3	0.2	46.7	17.9

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	667	790
Shareholders funds	414	457	519	583	685	808
Minority Interest	0	-	-	-	-	-
Total loans	90	72	88	127	120	50
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	829	882
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	554	644
Cash	12	13	15	14	13	16
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	280	326
Mis. Exp. not written off	0	-	-	-	-	-
Total assets	555	585	659	762	829	882

Cash Flow Statement (Consolidated)

Y/E March (₹ cr)	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
Profit before tax	48	72	110	101	152	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	30	36
Cash Flow from Operations	79	69	90	80	113	153
(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	(7)	(70)
Dividend Paid (Incl. Tax)	(12)	(12)	(22)	(21)	(21)	(21)
Others	3	(16)	(3)	(15)	9	9
Cash Flow from Financing	(30)	(37)	(9)	5	(19)	(82)
Inc./Dec.) in Cash	1	(7)	3	(2)	35	12
Opening Cash balances	10	12	13	15	14	13
Closing Cash balances	12	13	15	14	13	16

Key Ratios

Y/E March	FY2013	FY2014	FY2015	FY2016	FY2017E	FY2018E
Valuation Ratio (x)						
P/E (on FDEPS)	60.9	44.6	31.4	31.3	21.3	18.1
P/CEPS	39.1	29.1	20.0	18.1	13.9	12.1
P/BV	6.3	5.7	5.0	4.5	3.8	3.2
Dividend yield (%)	0.4	0.4	0.7	0.7	0.7	0.7
EV/Sales	4.3	3.7	3.1	2.8	2.4	2.0
EV/EBITDA	30.0	24.1	16.6	18.7	13.4	11.2
EV / Total Assets	4.8	4.5	4.1	3.6	3.3	3.0
Per Share Data (₹)						
EPS (Basic)	4.6	6.3	9.0	9.0	13.2	15.6
EPS (fully diluted)	4.6	6.3	9.0	9.0	13.2	15.6
Cash EPS	7.2	9.7	14.1	15.6	20.3	23.2
DPS	1.1	1.0	2.0	2.0	2.0	2.0
Book Value	44.9	49.6	56.3	63.3	74.3	87.6
Dupont Analysis						
EBIT margin	10.4	11.0	13.3	8.7	12.3	12.7
Tax retention ratio	88.2	80.4	75.7	82.5	80.0	80.0
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	14.3	15.9
Cost of Debt (Post Tax)	18.9	18.7	10.0	9.6	8.1	11.8
Leverage (x)	0.2	0.2	0.1	0.2	0.2	0.1
Operating ROE	8.9	10.4	14.8	10.5	15.4	16.3
Returns (%)						
ROCE (Pre-tax)	11.9	13.9	18.3	11.9	17.1	19.1
Angel ROIC (Pre-tax)	13.0	15.3	20.2	13.0	18.5	20.5
ROE	10.7	13.4	17.0	15.1	19.2	19.2
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	59	59
Receivables (days)	66	64	62	68	75	75
Payables (days)	43	40	46	42	52	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	0.0
Net debt to EBITDA	0.9	0.5	0.5	0.8	0.5	0.1
Interest Coverage (EBIT / Int.)	3.0	4.2	10.7	6.8	10.9	13.1

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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)