Syngene International Limited

IPO Note

AVOID

Issue Open: July 27, 2015
Issue Close: July 29, 2015

Incorporated in 1993 as a subsidiary of Biocon Limited, Syngene is a leading custom research and manufacturing organization, which supports R&D programs from lead generation to clinical supplies. At the higher price band of ₹250/share, the implied P/E would be ~23x FY2017E compared to the average P/E of 17-22x for its global large peers. Thus, given little valuation comfort and the associated risks, **we recommend an Avoid on the IPO.**

Well placed in the CRO Industry: Since its formation, the company has emerged as a key player in the CRO Industry. The global CRO market for discovery and development services was estimated to be ~US$43.5bn in 2014 and is expected to reach US$67.3bn in 2018, reflecting a CAGR of ~11.6% (2014-2018), according to a report by IQ4I.

Syngene's operational track record, successful delivery of projects, responsiveness, process innovation, turnaround times, and productivity has facilitated the strengthening of its client base (mainly outside India with exports contributing 97.2% of sales in FY2014). Over the past 20 years, Syngene has built significant credibility and a regulatory track record in various therapeutic platforms and service models. It is now catering to 8 of the top 10 innovators globally including BMS, Abbott and Baxter. Syngene boasts of a healthy track record in the industry with a market share of ~2.0%. The company has been reporting a Sales and PAT CAGR of 28% and 59%, respectively, with healthy EBITDA margins of 30-33% over FY2011-2015. Going forward, with the industry growing at 11-12%, we believe the company can clock a healthy 18-20% growth given the Indian cost advantage (cost of conducting clinical trials in countries, such as China, India and Indonesia, is 25-40% less expensive than in western countries), though it needs a better diversification of clientele base to ensure a better consistency in the same.

Syngene to invest US$200mn: Syngene plans a US$200mn capex over the next three years. Of US$200mn, US$100mn will be incurred on the development of oral dosages, MAb facilities, phase 2 of Malaysia insulin facility and research lab in Bangalore, while the balance US$100mn will be utilized for Greenfield expansion in Mangalore. The company plans to evolve from a CRO to a CRAMS player. It has entered into three long term contracts with two clients for commercial manufacture of their novel small molecules, of which, one is under late stage development, while the other two are in various stages of clinical development.

Risk stems from overdependence on few clients: Around 45% of Syngene's total sales come from its top 3 clients - BMS, Abbott and Baxter, of which BMS alone contributed 30% in FY2015. Besides, its top 10 clients accounted for ~71% of its total sales in FY2015. However, the company has managed to scale up its client base from 103 in FY2012 to 221 in FY2015, indicating a gradual reduction in top 10 clients revenue contribution from 79% in FY2012 to 71% in FY2015.

Issue Details
Face Value: Rs10
Present Eq. Paid up Capital: ₹19.9cr
Offer Size: 528cr-550cr Shares*
Post Eq. Paid up Capital*: ₹22.1cr
Issue size (shares): 2.2cr
Price Band: ₹240-250
Promoters holding Pre-Issue: 85.5%
Promoters holding Post-Issue: 74.5%

Book Building	
QIBs	At least 50%
Non-Institutional	At least 15%
Retail	At least 35%

Post Issue Shareholding Pattern	
Promoters Group	0.745
MF/Banks/Indian FIs/FIIs/Public & Others	0.255

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Outlook and Valuation:

Syngene, given its leading position in the CRO industry, can continue to log in a robust growth, given that it is the leading Indian player in the industry. Thus, while the industry is expected to grow at 11-12% the company can log in around 18-20% growth in the near term. Also, the company plans to utilize its cash flows into the contract manufacturing segment, to emerge as a complete CRMAS player. Also, the company has been consistent in its growth and profitability profile, posting ROEs of 25.0% and ROIC upwards of 35.0%.

However, on the flip side the company has very high dependence on few clients, with around 45% of sales coming in from its top 3 clients, with one client contributing 30% of sales. This, coupled with the valuations of ~22-23.3x FY2017E (at ₹240-250), makes the IPO fairly valued. Its comparable peers in India and internationality, which are much larger in size with ROEs in the range of 20-27%, trade at ~17-22x FY2017E earnings. **Thus we recommend avoiding the issue.**

Key Financials

Y/E March (₹ cr)	FY2012	FY2013	FY2014	FY2015E
Net Sales	**417**	**550**	**700**	**860**
% chg	*29.5*	*32.0*	*27.2*	*23.0*
Net Profit	**71**	**102**	**135**	**166**
% chg	*161.0*	*43.8*	*32.0*	*23.2*
EBITDA (%)	32.9	30.6	30.6	30.6
EPS (₹)	**3.2**	**4.6**	**6.1**	**7.5**
P/E (x)	77.8	54.1	41.0	33.3
P/BV (x)	18.5	10.6	8.3	5.7
RoE (%)	27.4	25.0	22.9	20.5
RoCE (%)	31.3	23.1	20.7	20.7
EV/Sales (x)	13.2	9.7	7.3	5.5
EV/EBITDA (x)	40.2	31.7	23.9	18.0

Source: Company, Angel Research, Price at upper band of ₹250

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