

Indoco Remedies

Performance Highlights

Y/E March (` cr)	1QFY18	4QFY17	% chg (qoq)	1QFY17	% chg (yoy)
Net sales	204	266	(23.1)	253	(19.1)
Other operating income	6	13	(56.7)	5	13.9
Gross profit	133	168	(20.9)	164	(18.7)
Operating profit	(3)	21	-	37	-
Net profit	(22)	18	-	20	-

Source: Company, Angel Research

For 1QFY2018 Indoco Remedies posted poor set of numbers. Sales came in at `204cr (`214cr expected) v/s. `253cr in 1QFY2017, a yoy de-growth of 19.1%. The company witnessed a disruptive 1QFY2018, with domestic as well International sales getting affected adversely due to GST implementation in India and voluntary stoppage of ophthalmic product supplies to US respectively. On operating front, the EBITDA margins came in at (1.7%) ((0.9%) expected) v/s. 14.7% in 1QFY2017, mainly on the back of lower than expected sales during the quarter. Thus, the PAT came in at `(21.7)cr (`13.8)cr expected) v/s. `19.7cr in 1QFY2017. **We maintain our sell rating on the stock, with a price target of `153.**

Results lower than expected: Sales came in at `204cr (`214cr expected) v/s. `253cr in 1QFY2017, a yoy de-growth of 19.1%. The company witnessed a disruptive 1QFY2018, with domestic as well International sales getting affected adversely due to GST implementation in India and voluntary stoppage of ophthalmic product supplies to US respectively. The formulation sales (`185.7cr; 90.9% of sales in 1QFY2018) posted a dip of 20.7% yoy. The domestic formulation sales (`99.7cr) registered a dip of 29.7% yoy. The International formulation sales (`86.0cr) posted a yoy dip of 6.9%. The API sales (`14.9cr) posted a yoy dip of 15.1%. On operating front, the EBITDA margins came in at (1.7%) ((0.9%) expected) v/s. 14.7% in 1QFY2017, mainly on the back of lower than expected sales during the quarter. Gross margins came in at 65.2% v/s. 64.8% in 1QFY2017; while R&D expenses were 6.6% of sales in 1QFY2018 v/s. 4.7% of sales in 1QFY2017. Thus, the PAT came in at `(21.7)cr (`13.8)cr expected) v/s. `19.7cr in 1QFY2017.

Outlook and valuation: We expect net sales to post a CAGR of 10.8% to `1,310cr and EPS to post a CAGR of 23.0% to `12.7 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	1124	1310
% chg	14.6	9.2	5.4	16.5
Net profit	83.0	77.5	71.4	117.3
% chg	0.2	(6.7)	(7.8)	64.3
EPS (`)	9.0	8.4	7.7	12.7
EBITDA margin (%)	14.9	12.1	11.9	14.9
P/E (x)	21.2	22.7	24.7	15.0
RoE (%)	15.1	12.6	10.6	15.6
RoCE (%)	11.9	7.9	6.2	11.3
P/BV (x)	3.0	2.7	2.5	2.2
EV/Sales (x)	1.9	1.8	1.8	1.5
EV/EBITDA (x)	12.9	15.1	15.0	10.0

Source: Company, Angel Research; Note: CMP as of August 11, 2017

SELL

CMP	`191
Target Price	`153

Investment Period -

Stock Info

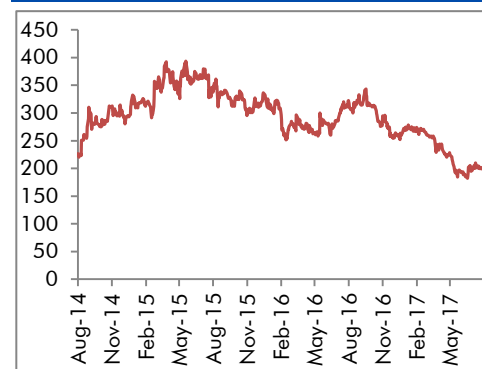
Sector	Pharmaceutical
Market Cap (` cr)	1,760
Net Debt (` cr)	188
Beta	0.2
52 Week High / Low	360/179
Avg. Daily Volume	13,718
Face Value (`)	2
BSE Sensex	31,214
Nifty	9,711
Reuters Code	INRM.BO
Bloomberg Code	INDR@IN

Shareholding Pattern (%)

Promoters	59.1
MF / Banks / Indian Fls	12.1
FII / NRIs / OCBs	11.9
Indian Public / Others	17.0

Abs. (%)	3m	1yr	3yr
Sensex	4.8	12.0	22.3
Indoco	(18.7)	(39.9)	(15.8)

3-Year Daily Price Chart



Source: Company, Angel Research

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Exhibit 1: 1QFY2018 (Consolidated) performance

Y/E March (` cr)	1QFY2018	4QFY2017	% chg (qoq)	1QFY2017	% chg (yoy)	FY2017	FY2016	% chg (yoy)
Net sales	204	266	(23.1)	253	(19.1)	1067	981	8.8
Other income	5.7	13.1	(56.7)	5	13.9	32	28	12.7
Total income	210	279	(24.7)	257	(18.5)	1098	1009	8.9
Gross profit	133	168	(20.9)	164	(18.7)	685	635	7.9
Gross margins (%)	65.2	63.4		64.8		64.2	64.7	
Operating profit	(3.5)	21.2	-	37.2	-	129.2	145.2	(11.0)
OPM (%)	(1.7)	8.0		14.7		12.1	14.8	
Interest	6	(2)	(492.9)	2	149.6	5	13	(61.5)
Dep & amortisation	17	15	9.5	17	0.4	63	60	5.0
PBT	(21)	20	-	23	-	93	100	(7.4)
Provision for taxation	0.9	2.4	(62.3)	3	(70.1)	14	18	(22.2)
Reported Net profit	(22)	18	-	20	-	77	82	(5.9)
Less : Exceptional items	0	0	-	(0)	-	0	0	
PAT after exceptional items	(22)	18	-	20	-	77	82	(5.9)
EPS (`)	-	1.9		2.2		8.4	8.9	

Source: Company, Angel Research

Exhibit 2: 1QFY2018 – Actual vs. Angel estimates

(` cr)	Actual	Estimate	Variation (%)
Net sales	204	214	(4.8)
Other operating income	6	5	13.9
Operating profit	(3)	(2)	-
Tax	1	0	
Net profit	(22)	(14)	-

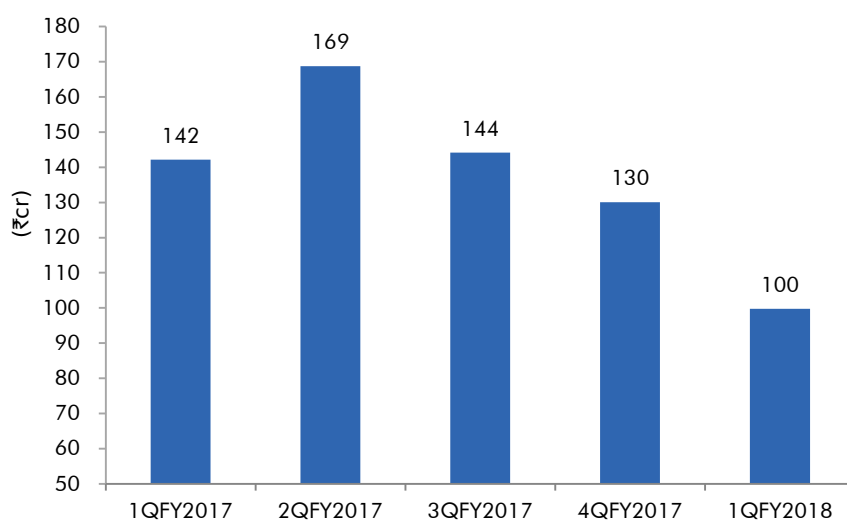
Source: Company, Angel Research

Revenues below expectations: Sales came in at `204cr (`214cr expected) v/s. `253cr in 1QFY2017, a yoy de-growth of 19.1%. The company witnessed a disruptive 1QFY2018, with domestic as well International sales getting affected adversely due to GST implementation in India and voluntary stoppage of ophthalmic product supplies to US respectively. The formulation sales (`185.7cr; 90.9% of sales in 1QFY2018) posted a dip of 20.7% yoy. The domestic formulation sales (`99.7cr) registered a dip of 29.7% yoy. The International formulation sales (`86.0cr) posted a yoy dip of 6.9%. The API sales (`14.9cr) posted a yoy dip of 15.1%.

In US, during the quarter, the revenues de-grew by 6.8% at `86.0cr as against `92.3cr for the same period last year. In terms of filings, the company (through partners or by itself), filed 32 ANDAs, which are pending approvals with 10 ANDAs approved till date, with 2 tentative approvals.

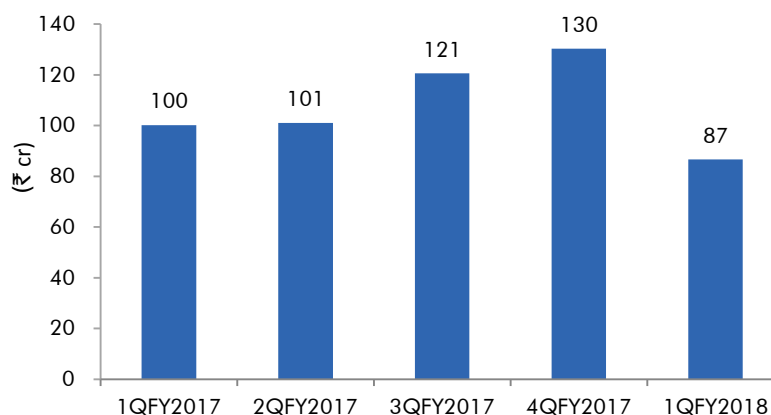
With reference to warning letter from USFDA for the company's Goa Plant II & III, the remediation process is going on in co-ordination with a US based consultant and the packaging component manufacturer from Europe. After sending the comprehensive response in May 2017, the company has sent the first update to USFDA in July 2017 & the second and final update will be sent soon.

Exhibit 3: Domestic Formulation sales trend



Source: Company, Angel research

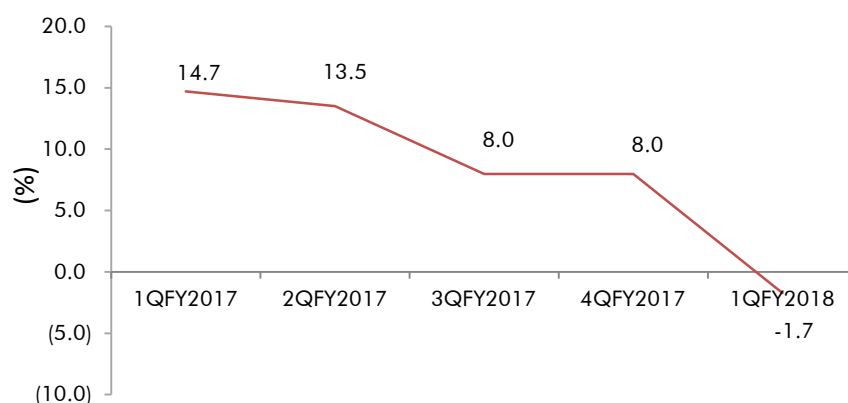
Exhibit 4: Export sales trend



Source: Company, Angel research

OPM negative: On operating front, the EBITDA margins came in at (1.7%) ((0.9% expected) v/s. 14.7% in 1QFY2017, mainly on the back of lower than expected sales during the quarter. Gross margins came in at 65.2% v/s. 64.8% in 1QFY2017; while R&D expenses were 6.6% of sales in 1QFY2018 v/s. 4.7% of sales in 1QFY2017.

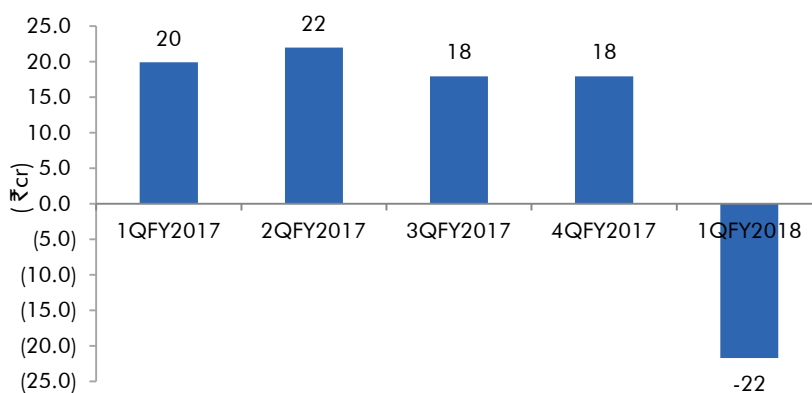
Exhibit 5: OPM trend



Source: Company, Angel Research

Net profit lower than expectation: Consequently, PAT came in at ₹ (21.7)cr (₹ (13.8)cr expected) v/s. ₹ 19.7cr in 1QFY2017. The lower than expected net profit was on the back of lower than expected sales and OPM. Also, the interest expenses during the quarter were higher, which accentuated the dip in the net profit. However, the other income came in at ₹ 6cr v/s. ₹ 5cr during the corresponding period last year.

Exhibit 6: Net profit trend



Source: Company, Angel Research

Concall takeaways

- Management expects that stoppage of export its ophthalmic solution to US, & sluggish growth in the unregulated markets are one-offs. All these markets are expected to deliver robust growth going ahead.
- The company has incurred one time one-off expense of `2.5cr in the quarter, which is an expense incurred on the US consultant.
- Domestic Formulations likely to bounce back in 2QFY2018.

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 CAGR 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. 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.

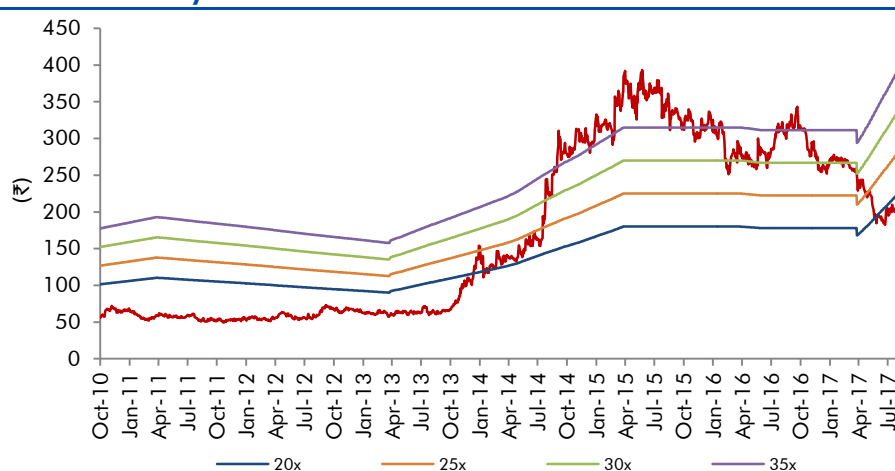
Valuation: We expect net sales to post a CAGR of 10.8% to ₹1,310cr and EPS to post a CAGR of 23.0% to ₹12.7 over FY2017-19E. At the current market price, the stock is trading at 24.7x and 15.0x its FY2018E and FY2019E earnings respectively. **We recommend a SELL rating on the stock considering the valuations.**

Exhibit 7: Key assumptions

	FY2018E	FY2019E
Domestic sales growth (%)	13.0	13.0
Exports growth	15.0	15.0
Operating margins (%)	11.9	14.9
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 (%)	FY2019E			FY17-19E		FY2019E
					PE (x)	EV/Sales (x)	EV/EBITDA (x)	CAGR in EPS (%)	RoCE (%)	RoE (%)
Alembic Pharma	Buy	512	600	17.3	18.8	2.1	11.0	12.8	24.3	20.6
Aurobindo Pharma	Buy	705	823	16.8	13.7	2.1	9.6	14.2	25.3	22.7
Cadila Healthcare	Reduce	483	420	(13.0)	22.7	3.7	18.0	21.0	17.3	22.9
Cipla	Sell	543	461	(15.1)	22.4	2.4	14.5	39.2	11.0	13.2
Dr Reddy's	Accumulate	2,011	2,219	10.4	19.0	2.3	12.3	23.6	11.2	13.0
Dishman Pharma	Under Review	301	-	-	18.9	1.3	10.1	(7.2)	2.9	2.5
GSK Pharma	Neutral	2,368	-	-	40.4	5.4	30.3	30.6	28.9	26.5
Indoco Remedies	Sell	191	153	(20.0)	15.0	1.5	10.0	23.0	11.3	15.6
Ipca labs	Buy	412	620	50.5	16.3	1.3	8.4	27.9	12.8	11.2
Lupin	Buy	942	1,467	55.7	14.1	1.9	8.2	8.2	20.5	17.5
Sanofi India*	Reduce	4,104	3,845	(6.3)	26.7	2.8	16.4	9.2	23.9	25.8
Sun Pharma	Buy	451	712	57.8	13.9	2.5	10.0	1.2	15.1	18.8

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)	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
Gross sales	735	863	987	1,078	1,137	1,325
Less: Excise duty	13	11	10	12	13	15
Net sales	722	852	977	1,067	1,124	1,310
Other operating income	10	5	27	27	27	27
Total operating income	733	857	1,004	1,094	1,152	1,338
% chg	16.2	17.0	17.1	9.0	5.3	16.1
Total expenditure	612	691	831	937	991	1,115
Net raw materials	272	300	341	382	416	485
Other mfg costs	42	50	57	62	66	77
Personnel	130	140	183	216	228	265
Other	168	201	250	277	281	288
EBITDA	110	161	145	129	134	195
% chg	23.5	46.1	(9.7)	(11.0)	3.6	45.9
(% of Net Sales)	15.2	18.9	14.9	12.1	11.9	14.9
Depreciation & amortisation	31	47	60	63	75	83
EBIT	79	114	85	66	59	113
% chg	21.0	43.7	(25.4)	(22.2)	(11.2)	92.2
(% of Net Sales)	11.0	13.3	8.7	6.2	5.2	8.6
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	4.9	3.0
Share in profit of Associates	-	-	1.0	2.0	3.0	4.0
Recurring PBT	72	110	101	91	84	138
PBT (reported)	72	110	101	91	84	138
Tax	14	27	18	14	13	21
(% of PBT)	19.6	24.3	17.5	15.2	15.0	15.0
PAT (reported)	58	83	83	77	71	117
Add: Share of earnings of asso.	-	-	-	-	-	-
Less: Minority interest (MI)	-	-	-	-	-	-
Prior period items	-	-	-	-	-	-
PAT after MI (reported)	58	83	83	77	71	117
ADJ. PAT	58	83	83	77	71	117
% chg	36.5	42.3	0.2	(6.7)	(7.8)	64.3
(% of Net Sales)	8.1	9.7	8.5	7.3	6.3	9.0
Basic EPS (`)	6.3	9.0	9.0	8.4	7.7	12.7
Fully Diluted EPS (`)	6.3	9.0	9.0	8.4	7.7	12.7
% chg	36.5	42.3	0.2	(6.7)	(7.8)	64.3

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	684	781
Shareholders funds	457	519	583	651	702	798
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	974	1,021
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	110	128
Current assets	305	385	448	572	597	693
Cash	13	15	15	63	49	55
Loans & advances	42	85	78	107	112	131
Other	249	285	355	403	435	507
Current liabilities	144	187	201	265	277	323
Net current assets	160	199	247	307	319	370
Mis. Exp. not written off	-	-	-	-	-	-
Total assets	585	659	762	903	974	1,021

Cash Flow Statement (Consolidated)

Y/E March (` cr)	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
Profit before tax	72	110	101	91	84	138
Depreciation	31	47	60	63	75	83
(Inc)/Dec in working capital	(18)	(39)	(62)	(8)	(70)	(63)
Less: Other income	2	2	1	4	4	4
Direct taxes paid	14	27	18	14	13	21
Cash Flow from Operations	69	90	81	128	73	133
(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	(14)	6
Opening Cash balances	12	13	15	15	63	49
Closing Cash balances	13	15	15	63	49	55

Key Ratios

Y/E March	FY2014	FY2015	FY2016	FY2017	FY2018E	FY2019E
Valuation Ratio (x)						
P/E (on FDEPS)	30.2	21.2	21.2	22.7	24.7	15.0
P/CEPS	19.7	13.5	12.3	12.5	12.0	8.8
P/BV	3.9	3.4	3.0	2.7	2.5	2.2
Dividend yield (%)	0.5	1.0	1.0	1.0	1.0	1.0
EV/Sales	2.5	2.2	1.9	1.8	1.8	1.5
EV/EBITDA	16.5	11.4	12.9	15.1	15.0	10.0
EV / Total Assets	3.1	2.8	2.5	2.2	2.1	1.9
Per Share Data (₹)						
EPS (Basic)	6.3	9.0	9.0	8.4	7.7	12.7
EPS (fully diluted)	6.3	9.0	9.0	8.4	7.7	12.7
Cash EPS	9.7	14.1	15.6	15.3	15.9	21.7
DPS	1.0	2.0	2.0	2.0	2.0	2.0
Book Value	49.6	56.3	63.3	70.6	76.1	86.6
Dupont Analysis						
EBIT margin	11.0	13.3	8.7	6.2	5.2	8.6
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	5.8	10.3
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	7.0	12.9
Returns (%)						
ROCE (Pre-tax)	13.9	18.3	11.9	7.9	6.2	11.3
Angel ROIC (Pre-tax)	15.3	20.2	14.0	10.0	7.9	14.0
ROE	13.4	17.0	15.1	12.6	10.6	15.6
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	62	62
Receivables (days)	64	62	68	80	79	79
Payables (days)	40	46	42	49	48	50
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	0.2
Net debt to EBITDA	0.5	0.5	0.8	1.5	1.9	1.0
Interest Coverage (EBIT / Int.)	4.2	10.7	6.8	10.7	9.5	18.3

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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)