

May 04, 2010

Recommendation	BUY
CMP	303
Target	340
Stock Return	12.2%

Nifty	5,223
Sensex	17,386

Key Stock Data

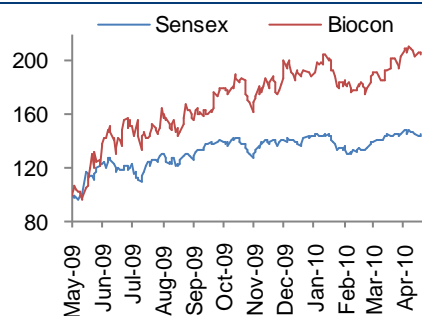
Sector	Pharma
Reuters Code	BION.BO
BLOOMBERG Code	BIOS IN
No. of Shares (mn)	200
Market Cap (Rs bn)	60.6
Market Cap (\$ mn)	1,362
Avg. 6m Vol. (mn)	0.87

Stock Performance (%)

52 - Week high / low	Rs 311/140		
	3M	6M	12M
Absolute (%)	11.3	28.1	113.6
Relative (%)	4.9	14.1	59.6

Shareholding Pattern (%)

Promoters	60.9
FIs & Local MFs	13.2
FII	3.9
Public & Others	22.0

Source: Company
Sensex and Stock Movement

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Biocon results for the Q4FY10 were affected by lower other income and higher tax rate. Total income grew by 36%YoY from Rs4.68bn to Rs6.58bn. The company's EBIDTA margin improved by 40bps from 19.6% to 20.0% mainly due to the decline in personnel and other expenses. Material cost increased by 100bps from 56.4% to 57.4% of total revenues due to the change in product mix. Personnel cost declined by 70bps from 10.4% to 9.7% of total income due to strong sales growth. Other expenses declined by 80bps from 13.6% to 12.8% of total income due to strong sales growth. Biocon's other income declined by 60% from Rs185m to Rs75m. Its interest cost was lower by 56% from Rs61m to Rs33m due to debt repayment and reduction in working capital. The company's tax rate has gone up from -2.2% to 11.3% of PBT due to increase in tax rate. Net profit declined by 3% from Rs829m to Rs806m.

Net profit to rise by 25% over next two years

We expect Biocon to report 19% growth in total income for FY11 and 16% in FY12. We expect 29% increase in net profit for FY11 and 21% rise in net profit for FY12. We expect EBIDTA margin to improve from 20.2% in FY10 to 21.0% in FY11 and further improve to 22.0% in FY12 due to the reduction in material cost and other expenses. We expect the company's RoCE to improve from 14.2% in FY10 to 19.1% in FY12. Its RoE is also likely to improve from 18.1% to 20.9% during the similar period.

On a strong growth path

Biocon's various businesses reported good YoY growth during FY10 as follows: insulins 11%, immunesuppressants 28%, statins 26%, and domestic formulations 36%. In the domestic formulations segment the company has reported the following YoY growth rates: diabetology, 24%, oncology 59%, cardiology 26% and nephrology 57%. We expect the company to maintain the growth momentum in future. The German subsidiary Axicorp reported 93% YoY growth although it is not comparable as in FY09 the sales were for three quarters only.

BUY with a target price of Rs340

At the CMP of Rs303, the stock trades at 16.0x FY11E EPS of Rs18.9 and 13.3 FY12E EPS of Rs22.8. We have BUY rating for the scrip with the target price of Rs340 (18x FY11 earnings) with an upside of 12.2% over the next 12 months.

Particulars (Rs mn)	FY08	FY09	FY10E	FY11E	FY12E
Revenues	10,538	16,087	23,749	28,268	32,762
Growth (%)	7%	53%	48%	19%	16%
EBIDTA	2,974	3,234	4,787	5,940	7,210
EBIDTA margin (%)	28.2%	20.1%	20.2%	21.0%	22.0%
Net profit	2,233	2,402	2,933	3,776	4,558
Net profit Growth (%)	12%	8%	22%	29%	21%
EPS Rs.	11.2	12.0	14.7	18.9	22.8
P/E (x)	27.1	25.2	20.7	16.0	13.3
D/E (x)	0.2	0.3	0.3	0.1	0.1
RoCE (%)	14.7	13.6	14.2	17.2	19.1
RoE (%)	17.5	16.0	18.1	20.3	20.9

Source: Company, HDFC Securities Institutional Research

Table 1: Valuations

Particulars	FY08	FY09	FY10A/E	FY11E	FY12E
P/E (x)	27.1	25.2	20.7	16.0	13.3
Dividend yield %	1.7	1.0	1.2	1.3	1.5
P/BV (x)	2.0	4.0	3.5	3.0	2.6
EV/EBIDTA (x)	21.2	20.3	13.8	10.7	8.7
EV/Sales (x)	6.0	4.1	2.8	2.2	1.9
Market cap/sales (x)	5.8	3.8	2.6	2.1	1.8

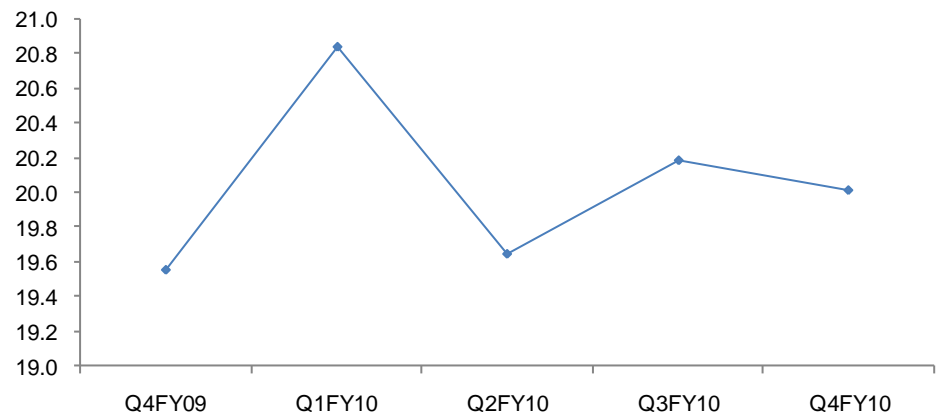
Source: HDFC Securities Institutional Research

Result Highlights

- During the quarter, Biocon's total income grew by 36%YoY from Rs4.69bn to Rs6.58bn due to strong growth across various segments.
- EBITDA margin improved by 40bps from 19.6% to 20.0% mainly due to the reduction in personnel and other expenses.
- Material cost increased by 100bps from 56.4% to 57.4% of total income due to the change in product mix. Personnel cost declined by 70bps from 10.4% to 9.7% of total income due to strong sales growth. Other expenses declined by 80bps from 13.6% to 12.8% of total income due to strong sales growth.
- Other income declined by 60% from Rs185m to Rs75m. Interest expenses declined by 56% from Rs61m to Rs33m.
- Biocon's tax rate increased from -2.2% to 11.3% of PBT due to the increase in MAT rate.
- The company's net profit before EO items declined by 3%YoY from Rs829m to Rs806m. Its net margin dropped by 550bps from 17.7% to 12.2% due to the drop in EBITDA margin, lower other income and higher tax rate.
- Net profit after EO items was up by 95% from Rs414m to Rs806m.

EBIDTA margin improved by 40bpsYoY to 20.0%

Biocon's EBITDA grew by 44%YoY from Rs916m to Rs1,318m. EBITDA margin improved by 40bps mainly due to the decline in personnel and other expenses. The company's EBITDA margin for the last 5 quarters is indicated in the following graph:

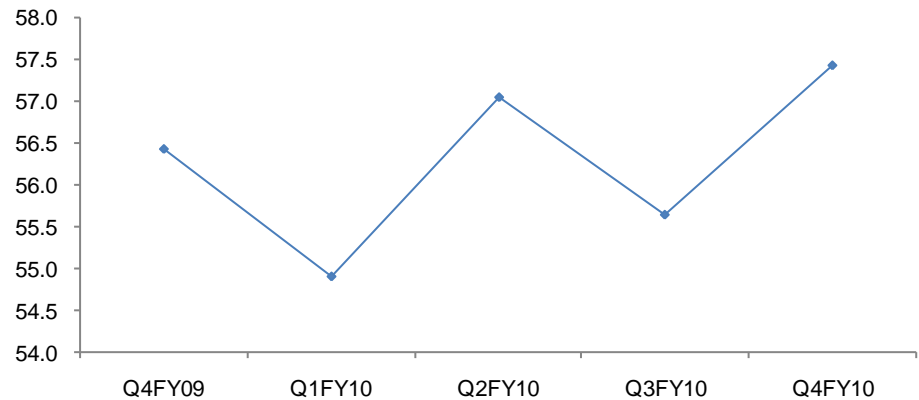
Chart 1: EBITDA margin (%)


Source : HDFC Securities Institutional Research

As seen from the above graph, the company's EBIDTA margin improved from 19.6% in Q4FY09 to 20.8% in Q1FY10 and then declined to 19.6% in Q2FY10. The margin then improved to 20.2% in Q3FY10 and then declined to 20.0% in Q4FY10 indicating a 20bps decline on QoQ basis.

Biocon's material cost for last 5 quarters has been shown in the following chart:

Chart 2 : Material cost (%)



Source : HDFC Securities Institutional Research

The company's material cost declined from 56.4% in Q4FY09 to 54.9% in Q1FY10. It further increased to 57.0% in Q2FY10 and then declined to 55.6% in Q3FY10. The material cost increased to 57.4% in Q4FY10 indicating an 180bps increase on QoQ basis.

Adjusted PAT declined by 3%YoY

Biocon's PAT before EO items declined by 3%YoY from Rs829m to Rs806m due to decline in EBIDTA margin, lower other income and higher tax rate. PAT after EO items was up by 95% from Rs414m to Rs806m.

Outlook

Strong growth across segments

Biocon's various businesses reported good YoY growth during FY10 as follows: insulins 11%, immunesuppressants 28%, statins 26%, and domestic formulations 36%. In the domestic formulations segment the company has reported the following YoY growth rates: diabetology, 24%, oncology 59%, cardiology 26% and nephrology 57%. We expect the company to maintain the growth momentum in future. The German subsidiary Axicorp reported 93% YoY growth although it is not comparable as in FY09 the sales were for three quarters only.

R & D pipeline

Biocon's oral insulin molecule IN105 is currently undergoing phase III clinical trials in India. Its other molecule T1h for psoriasis is likely to enter into Phase III clinical trials during CY10. Biocon has plans to out licence these molecules and will start negotiating for the same from Q3CY10.

Biocon has plans to launch insulin pen in CY10 in the domestic market.

Capex for FY11

Biocon has plans to spend Rs2.5bn on capex in FY11 in creating a biological manufacturing facility and R & D centre.

Concerns

Axicorp margin- on decline

Axicorp has reported EBIDTA margin of 4.8% during Q4FY10 against 5.9% in FY10. Its net margin also declined to 1.6% during Q4FY10 compared to 2.5% in FY10. The details of the same have been indicated in the following table:

Table 2: Axicorp results

PARTICULARS (Rs mn)	Q4FY10	FY10
Sales	2,510	9,120
EBIDTA	120	540
EBIDTA margin %	4.8	5.9
Net profit	40	230
Net margin %	1.6	2.5

Source: Company, HDFC Securities Institutional Research

ORG IMS data reports lower growth

As per ORG IMS MAT data of MARch'10, Biocon had sales of Rs704.7m and growth rate of 3.4%. However, the company has reported sales of about Rs1.25bn and growth rate of 36%. Hence, there is a large discrepancy in the two sets of data.

Valuation

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At the CMP of Rs303, the stock trades at 16.0x FY11E EPS of Rs18.9 and 13.3 FY12E EPS of Rs22.8. We have BUY rating for the scrip with the target price of Rs340 (18x FY11 earnings) with an upside of 12.2% over the next 12 months.

Institutional Research
Table 3: Q4FY10 and FY10 results-consolidated

PARTICULARS	Q4FY10	Q4FY09	YoY	Q3FY10	QoQ	FY10	FY09	YoY
(Rs mn)	Mar'09	Mar'08	Growth %	Dec'09	Growth %	Mar'09	Mar'08	Growth %
Total income	6,582	4,681	36.1	6,370	3.3	23,748	16,124	47.3
Expenditure								
Raw materials	3,781	2,642	34.2	3,544	6.7	13,377	8,367	59.9
as % of total income	57.4	56.4		55.6		56.3	51.9	
Personnel expenses	639	486	31.1	637	0.2	2,450	1,787	37.1
as % of total income	9.7	10.4		10.0		10.3	11.1	
Other expenses	845	637	41.7	903	-6.4	3,137	2,772	13.2
as % of total income	12.8	13.6		14.2		13.2	17.2	
Total Expenditure	5,265	3,765	39.8	5,084	3.5	18,963	12,926	46.7
EBIDTA	1,318	916	43.9	1,286	2.5	4,784	3,198	49.6
<i>EBIDTA Margin (%)</i>	<i>20.0</i>	<i>19.6</i>		<i>20.2</i>		<i>20.1</i>	<i>19.8</i>	
Other income	75	185	(59.7)	45	64.1	301	609	(50.6)
PBDIT	1,392	1,101	26.5	1,331	4.6	5,085	3,806	33.6
Depreciation	367	306	17.4	360	2.0	1,401	1,120	25.1
Interest	33	61	(55.6)	27	22.1	169	177	(4.4)
PBT	992	733	35.3	944	5.1	3,515	2,510	40.0
Prov. For tax	144	(16)	(808.9)	112	28.1	487	118	311.8
Tax rate	11.3	(2.2)		11.9		13.8	4.7	
PAT	849	749	13.3	832	1.9	3,028	2,392	26.6
Minority Interest	-42.4	82.8		-23.5		-95.6	83.9	
Share of Profit & Loss of Asso	0	-2.9		0		0	-7.3	
PAT after MI & share of P&L Asso.	806	829	(2.7)	809	-0.3	2,932	2,468	18.8
Extraordinary item	-	(414)		-		-	(1,382)	
Reported PAT (after EO)	806	414	94.5	809	-0.3	2,932	1,086	169.9
Equity capital	1,000	1,000	-	1,000	0.0	1,000	1,000	-
EPS Rs.(Rs. 5 Paid up)	4.0	4.1	(2.7)	4.0	-0.3	14.7	12.3	18.8

Source: Company, HDFC Securities Institutional Research