

# Biocon (BIOCON)

Rs 272

## WHAT'S CHANGED...

PRICE TARGET ..... Changed from Rs 285 to Rs 335  
 EPS (FY10E) ..... Unchanged at Rs 17.6  
 EPS (FY11E) ..... Unchanged at Rs 20.3  
 RATING..... Unchanged

## Looking up...

Biocon's Q2FY10 results were ahead of our expectations. Consolidated net profit jumped ~200% YoY to Rs 74.2 crore (expected Rs 71.2 crore) on ~31% growth in net sales to Rs 580 crore (expected Rs 557 crore). The Axicorp integration led the EBITDA margin to fall by ~925 bps YoY to ~21.7% and net margin by ~593 bps YoY to ~12.8%. Excluding Axicorp, Biocon's EBITDA margin, expanded strongly by ~348 bps. The biopharma business grew by a robust 18% on standalone to Rs 294.2 crore on account of strong growth in the domestic formulation business while CRAMS grew ~37% YoY to Rs 73.1 crore. We continue to rate the stock **OUTPERFORMER** with a target price of Rs 335.

### ■ Highlights for the quarter

During Q2FY10, Biocon reported a strong operating performance with significant margin expansion. The company started to secure some tender business in Latin American countries and has also initiated supplies of its vials to key Latin American markets like Brazil. Biocon entered into an agreement to acquire the API manufacturing facility of IDL Specialty that will help it to expand its chemical synthesis capabilities and also manufacture advanced intermediates. The company has signed a joint development and commercialisation agreement with Amylin, for the development of a novel peptide hybrid. Biocon has booked Rs 10.6 crore of licensing income during the quarter as part of milestone from the Mylan deal.

## Valuations

We believe Biocon's strength lies in its strong Insulin franchise, position in biosimilars and increasing presence in niche areas like nephrology, diabetes, cardiovascular and oncology. Oral insulin for type-II diabetes is in Phase-III in India. An out-licensing deal in the area of insulin and bio-generics may act as a catalyst to the stock. Biocon is currently trading at 13.4x FY11E EPS. We continue to assign **OUTPERFORMER** rating to the stock with a target price of Rs 335, 16.5x FY11E EPS of Rs 20.

### Exhibit 1: Key Financials

	Q2FY10	Q2FY09	Q1FY10	YoY Gr.(%)	QoQ Gr.(%)	YTD FY10
Net Sales	580.0	442.3	495.9	31.1	17.0	1075.9
EBITDA	125.6	88.8	110.7	41.5	13.4	236.3
EBITDA Margin (%)	21.7	20.1	22.3			22.0
Depreciation	35.1	29.0	32.4	20.9	8.2	67.5
Interest	5.2	4.2	5.6	23.9	-6.6	10.8
Reported PAT	74.2	24.9	57.6	198.0	28.8	131.8
EPS (Rs)	5.4	1.8	4.2			9.5

Source: Company, ICICIdirect.com Research

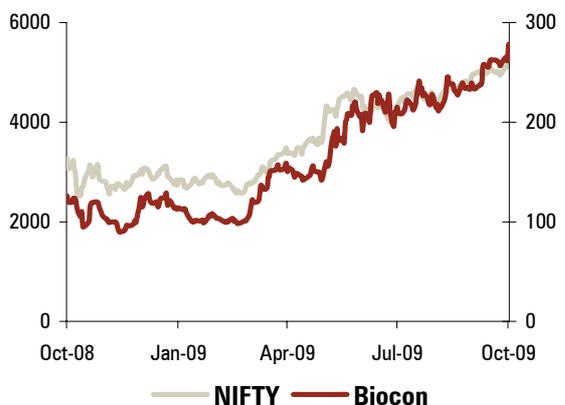
Rating Matrix	
Rating	: Outperformer
Target	: Rs 335
Target Period	: 12-15 months
Potential Upside	: 23%

Key Financials	(Rs Crore)			
	FY08	FY09	FY10E	FY11E
Net Sales	1108.2	1608.7	2430.9	2870.1
EBITDA	315.9	323.4	492.0	553.2
Net Profit	470.8	93.0	351.6	406.2

Valuation Summary	FY08	FY09	FY10E	FY11E
EPS (Rs)	23.2	12.0	17.6	20.3
PE (x)	11.7	22.6	15.5	13.4
Target PE (x)	14.5	27.9	19.1	16.5
EV to EBITDA (x)	9.2	18.5	11.3	11.4
Price to book (x)	1.8	3.6	2.9	3.5
RoNW (%)	14.8	11.4	17.0	19.1
RoCE (%)	13.8	13.2	19.7	23.4

Stock Data	
Market Capitalisation	Rs 5440 crore
Debt (FY09)	Rs 524 crore
Cash (FY09)	Rs -13 crore
EV	5977.1
52 week H/L	Rs 284/86
Equity capital	Rs 100 crore
Face value	Rs 5
MF Holding (%)	11.0
RI Holding (%)	4.7

### Price Movement (Stock vs. Nifty)



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## Result Analysis

### ■ Topline growth above our expectation (including Axicorp)

Biocon reported a robust 31% YoY growth in consolidated revenue buoyed by 30% YoY growth in biopharmaceuticals and 37% YoY growth in contract research. The robust growth in the bio-pharma business by 30% was recorded on account of integration of the Axicorp business, which contributed Rs 213 crore (~37% to the overall revenues and is growing by 52% YoY) to the consolidated sales in Q2FY10. Strong growth in the insulin franchise also led the biopharma business to perform better. The standalone bio-pharma business grew ~18% YoY to Rs 294.2 crore on account of robust performance in the domestic formulation business. The second largest revenue grosser to the company, CRAMS, grew at 37% YoY on account of a further ramp up in execution of the BMS contract in Q2FY10.

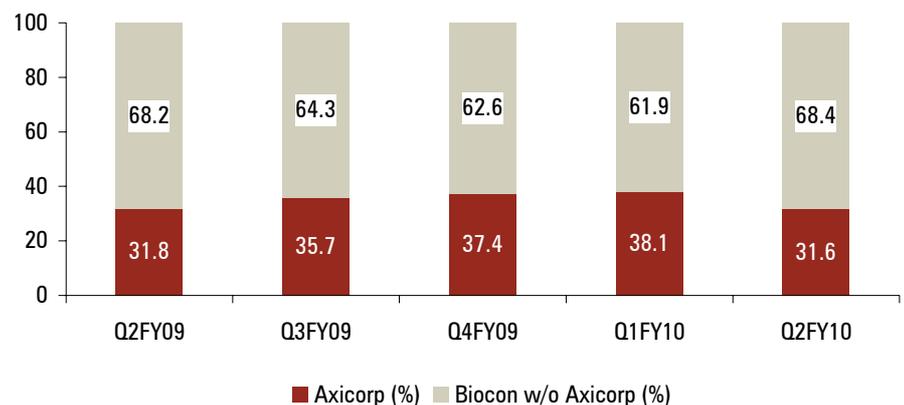
Growth in overall revenues was buoyed by 30% YoY growth in biopharmaceuticals and 37% YoY growth in the contract research business

### Exhibit 2: Business highlight

	Q2FY10	Q2FY09	YoY Growth (%)	Q1FY10	QoQ Growth (%)
Biopharma	294.2	249.5	17.9	240.5	22.3
% to sales	50.7	56.4		48.5	
Contract Research	73.1	53.2	37.4	66.7	9.6
% to sales	12.6	12.0		13.5	
Axicorp	212.69	139.62	52.3	188.7	12.7
% to sales	36.7	31.6		38.1	
<b>Total Sales</b>	<b>580.0</b>	<b>442.3</b>	<b>31.1</b>	<b>495.9</b>	<b>17.0</b>

Source: Company, ICICIdirect.com Research

### Exhibit 3: Percentage contribution to consolidated sales

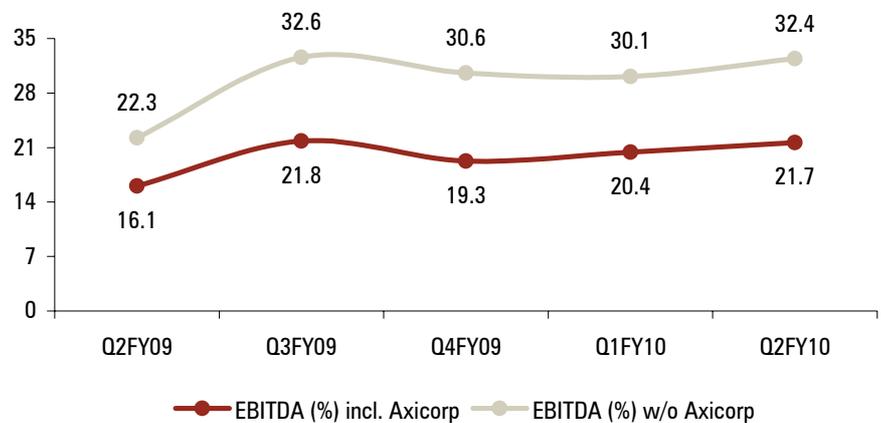


Source: Company, ICICIdirect.com Research

### ■ Expanding operating margin indicates improving business conditions

Biocon's operating profit for Q2FY10 grew at a robust rate of ~41% YoY, largely on account of 31% rise in top line. Biocon's overall EBITDA margin expanded by ~158bps YoY in Q2FY10. Consolidation of Axicorp dragged the overall EBITDA margin by ~925bps during Q2FY10 (due to ~37% revenue contribution from the low margin Axicorp subsidiary). Axicorp is in the business of distribution and generated an operating margin of ~5.5%, thereby a drag on the consolidated EBITDA margin by ~925 bps. Out of the total expenditure of Biocon of Rs 467 crore in Q2FY10, Axicorp's contribution was ~43%. Beside, employee costs have also seen a rise with Syngene beginning to ramp up its operations for the BMS contract. Employee cost rose 32% YoY to Rs 57 crore (including Axicorp). The R&D cost also increased due to increased spending on clinical development of novel biologics and bio-generics.

**Exhibit 4: EBITDA margin trend**



Source: Company, ICICIdirect.com Research

### ■ Net profit improves 47% YoY (adjusted for MTM)

For Q2FY10, Biocon's consolidated net profit was up ~200% YoY to Rs 74.2 crore. Even after adjusting for the MTM impact in Q2FY09, the bottomline in Q2FY10 grew ~47% YoY, indicating an improved profitability. Depreciation during the quarter rose by 21% due to further expansion in Syngene, which also led to a rise in interest cost by 24% YoY. The company earlier had a hedging position of US\$150 million (the contract which expired in April 2009). This quarter the company did not incur huge forex losses as was witnessed in the previous few quarters as a consequence of entering into an innovative option forward contract. With such an arrangement, we believe the forex loss provisions will not be significant in Biocon's numbers in the coming quarters.

**Exhibit 5: Common size profit and loss account**

	Q2FY09	Q3FY09	Q4FY09	Q1FY10	Q2FY10
Net Sales	100	100	100	100	100
Depreciation	6.6	6.2	6.6	6.5	6.0
Interest	1.0	0.8	1.3	1.1	0.9
PBT	12.7	18.5	15.7	14.7	14.7
Tax (% PBT)	10.5	7.2	2.2	18.8	11.0
Net Profit	5.7	6.5	5.3	11.6	12.8

Source: Company, ICICIdirect.com Research

Profitability was higher on account of 31% YoY increase in revenues

## Valuation

We believe Biocon is on track to generate robust revenues and net profit growth from FY10E onwards. Looking at the current quarter results, the company's performance has significantly improved. All the business segments are progressing well. Biocon's discovery R&D focus is reflected in its interesting discovery pipeline including two Monoclonal Antibodies (MAb) related to Oncology and Rheumatoid Arthritis along with the oral insulin. The company is looking to file an Investigational New Drug Application (IND) for its oral insulin in the EU by Q1FY11. It is looking for a potential partner for conducting Phase II and Phase III trials in regulated markets.

The Axicorp subsidiary will start contributing meaningfully to the bottomline once the commercialisation of the insulin kicks in the EU. Clingene and Syngene are showing a good ramp-up in operations. The immunosuppressant segment is likely to be another growth driver with Biocon looking to scale up the MMF supplies in the US market and Tacrolimus APIs over the next few quarters. Biocon has already captured 20% of the generic API market in MMF. We remain bullish on the company regarding its near to medium term prospects. An out-licensing deal in the area of insulin and bio-generics may act as a catalyst for the stock. Biocon is currently trading at 13.4x FY11E earnings. We are assigning an **OUTPERFORMER** rating on the stock with a target price of Rs 335, 16.5x FY11E EPS.

### Exhibit 6: Valuation Table

	Sales (Rs Cr)		EPS (Rs)	EPS Gr (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
		Gr (%)						
<b>FY08</b>	1108.2	12.4	23.2	15.7	11.7	9.2	14.8	13.8
<b>FY09</b>	1608.7	45.2	12.0	-48.2	18.2*	18.5	11.4	13.2
<b>FY10E</b>	2430.9	51.1	17.6	46.4	15.5	11.3	17.0	19.7
<b>FY11E</b>	2870.1	18.1	20.3	15.5	13.4	11.4	19.1	23.4

\* Adjusted EPS

Source: Company, ICICIdirect.com Research

**ICICIdirect.com Coverage Universe**

<b>Alembic</b>					<b>Sales (Rs Cr)</b>	<b>EPS (Rs)</b>	<b>PE(x)</b>	<b>EV/E* (x)</b>	<b>RoNW (%)</b>	<b>RoCE (%)</b>
<b>Idirect Code</b>	ALECHE	<b>CMP</b>	47	<b>FY08</b>	1003.2	8.0	5.8	7.2	32.6	19.1
		<b>Target</b>	57	<b>FY09</b>	1116.1	3.4	13.9*	8.8	14.0*	11.3
<b>MCap</b>	647.3	<b>Upside (%)</b>	22	<b>FY10E</b>	1165.7	4.5	10.3	6.4	12.4	11.5
				<b>FY11E</b>	1377.4	7.1	6.6	4.3	16.9	15.5
<b>Biocon</b>					<b>Sales (Rs Cr)</b>	<b>EPS (Rs)</b>	<b>PE(x)</b>	<b>EV/E* (x)</b>	<b>RoNW (%)</b>	<b>RoCE (%)</b>
<b>Idirect Code</b>	BIOCON	<b>CMP</b>	272	<b>FY08</b>	1108.2	23.2	11.7	9.2	14.8	13.8
		<b>Target</b>	335	<b>FY09</b>	1608.7	12.0	18.2*	18.5	11.4	13.2
<b>MCap</b>	5440.0	<b>Upside (%)</b>	23	<b>FY10E</b>	2430.9	17.6	15.5	11.3	17.0	19.7
				<b>FY11E</b>	2870.1	20.3	13.4	11.4	19.1	23.4
<b>Dishman</b>					<b>Sales (Rs Cr)</b>	<b>EPS (Rs)</b>	<b>PE(x)</b>	<b>EV/E* (x)</b>	<b>RoNW (%)</b>	<b>RoCE (%)</b>
<b>Idirect Code</b>	DISHPHA	<b>CMP</b>	242	<b>FY08</b>	803.1	14.9	16.2	16.0	21.6	9.7
		<b>Target</b>	325	<b>FY09</b>	1062.4	18.2	13.3	10.1	20.9	13.7
<b>MCap</b>	1952.9	<b>Upside (%)</b>	34	<b>FY10E</b>	1286.9	27.9	8.7	7.4	27.8	17.5
<b>IPCA Labs</b>					<b>Sales (Rs Cr)</b>	<b>EPS (Rs)</b>	<b>PE(x)</b>	<b>EV/E* (x)</b>	<b>RoNW (%)</b>	<b>RoCE (%)</b>
<b>Idirect Code</b>	IPCLAB	<b>CMP</b>	810	<b>FY08</b>	1051.3	54.4	14.9	14.1	23.1	15.2
		<b>Target</b>	694	<b>FY09</b>	1283.8	40.3	20.1	9.6	16.0	19.6
<b>MCap</b>	2025.0	<b>Upside (%)</b>	-14	<b>FY10E</b>	1488.2	75.4	10.7	8.1	24.1	22.1
				<b>FY11E</b>	1717.6	90.5	9.0	7.0	23.3	20.8
<b>Piramal Healthcare</b>					<b>Sales (Rs Cr)</b>	<b>EPS (Rs)</b>	<b>PE(x)</b>	<b>EV/E* (x)</b>	<b>RoNW (%)</b>	<b>RoCE (%)</b>
<b>Idirect Code</b>	NICPIR	<b>CMP</b>	366	<b>FY08</b>	2867.5	16.0	22.9	15.2	30.7	24.6
		<b>Target</b>	373	<b>FY09</b>	3281.1	15.1	24.2	15.3	24.0	17.7
<b>MCap</b>	7649.4	<b>Upside (%)</b>	2	<b>FY10E</b>	3448.7	20.9	17.5	12.1	26.3	20.2
				<b>FY11E</b>	3819.7	26.6	13.7	9.9	26.2	22.5
<b>Sun Pharma</b>					<b>Sales (Rs Cr)</b>	<b>EPS (Rs)</b>	<b>PE(x)</b>	<b>EV/E* (x)</b>	<b>RoNW (%)</b>	<b>RoCE (%)</b>
<b>Idirect Code</b>	SUNPHA	<b>CMP</b>	1322	<b>FY08</b>	3356.7	71.8	18.4	16.8	29.8	30.4
		<b>Target</b>	1344	<b>FY09</b>	4271.4	88.1	15.0	14.6	28.1	28.2
<b>MCap</b>	27381.0	<b>Upside (%)</b>	2	<b>FY10E</b>	3946.9	68.5	19.3	18.3	18.5	18.9
				<b>FY11E</b>	4468.2	83.2	15.9	15.3	19.0	19.3
<b>Glenmark</b>					<b>Sales (Rs Cr)</b>	<b>EPS (Rs)</b>	<b>PE(x)</b>	<b>EV/E* (x)</b>	<b>RoNW (%)</b>	<b>RoCE (%)</b>
<b>Idirect Code</b>	GLEPHA	<b>CMP</b>	240	<b>FY08</b>	2037.4	25.4	9.4	8.5	41.7	34.2
		<b>Target</b>	288	<b>FY09</b>	2093.0	7.7	31.4	18.6	19.4	16.4
<b>MCap</b>	6446.3	<b>Upside (%)</b>	20	<b>FY10E</b>	2435.7	14.1	17.0	11.6	16.1	17.3
				<b>FY11E</b>	2827.1	18.0	13.3	9.2	20.2	21.1

Source: Company, ICICIdirect.com Research

## RATING RATIONALE

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**Outperformer (OP):** 20% or more;

**Performer (P):** Between 10% and 20%;

**Hold (H):**  $\pm 10\%$  return;

**Underperformer (U):** -10% or more;

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