

October 22, 2010

Reco	Previous Reco
Buy	Buy
CMP	Target Price
Rs298	Rs336

EPS change FY11E/12E (%)	-
Target Price change (%)	-
Nifty	6,066
Sensex	20,166

Price Performance

(%)	1M	3M	6M	12M
Absolute	2	(1)	12	84
Rel. to Nifty	1	(11)	(2)	51

Source: Bloomberg

Relative Price Chart



Source: Bloomberg

Stock Details

Sector	Pharmaceuticals
Bloomberg	IPCA@IN
Equity Capital (Rs mn)	250
Face Value(Rs)	2
No of shares o/s (mn)	125
52 Week H/L	325/160
Market Cap (Rs bn/USD mn)	37/830
Daily Avg Volume (No of sh)	179188
Daily Avg Turnover (US\$m)	1.2

Shareholding Pattern (%)

	S'10	J'10	M'10
Promoters	46.2	46.2	46.2
FII/NRI	9.0	6.8	5.3
Institutions	23.2	29.0	30.4
Private Corp	9.8	5.8	5.9
Public	11.8	12.1	12.3

Source: Capitaline

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- **Robust revenue growth (up 20% YoY) and strong operating performance (up by 16%) resulted in 13% growth in APAT**
- **Strong revenue growth was driven by 29% growth in domestic formulation business and 27% growth in the exports formulations business**
- **High employee and SGA cost impacted operating performance of the company**
- **Addition in the field force has impacted short term profitability but long term growth visibility remains intact; maintain earnings and Buy rating**

Domestic growth led by uptick in anti-malarial business

Domestic formulation business grew by 29% (ahead of our expectations) to Rs2.6bn on the back of strong growth in branded formulation business. The strong growth in branded formulation was driven by higher contribution from the CVS, Pain management, Anti-Malarial portfolio and cough & cold segments. Strong growth in the anti-malarial segment (up 41% YoY) was mainly because of higher off-take in the anti-malarial products. Even after excluding the higher sales from the anti-malarial segment, domestic formulations grew strongly by 25%, which company should be able to maintain going forward. Company has added ~1000 sales representatives in last 6-9 months and now the total field force in the domestic market is approx. 3800-4000. We believe the ramp-up in sales force will contribute revenues from Q3FY11E onwards.

Generic business in regulated markets continued to drive export growth

Export formulation business during the quarter grew by 27% driven by a) 38% growth in generic formulation and b) 7% growth in branded formulation (company expect the performance to improve in 2HFY11E). This growth is commendable, as during the quarter average \$ realization declined from Rs48.6 to Rs46 and average sterling pound realization declined from Rs77.8 to Rs69.9. Generic formulation growth was driven by 46% growth in US generic market to Rs236mn and 96% growth in tender business (mainly driven by fixed dose combination of Artemether and Lumefantine) to Rs309mn. In the US, Atenelol (45% market share), Metoprolol (9%), Hydroxychloroquine (44%), Flucamide (38%) and Propanol (20%), were the major growth drivers for the company. The API business as a whole de-grew by 7%. The lower growth in API is mainly because of higher captive consumption in the formulation business. Formulation now contributes 77% of overall revenue. Management has indicated that in the US they are currently facing capacity constraints.

Revenue break-up

	Q2FY11	Q2FY10	Y-o-Y Gr.(%)	H1FY11	H1FY10	Q-o-Q Gr.(%)
Domestic	2628	2093	25.6%	4205	3918	7.3%
Formulation	2219	1715	29.4%	3450	3164	9.0%
API	408	378	8.1%	755	754	0.1%
Exports	2515	2195	14.6%	4222	3947	6.9%
Formulation	1751	1378	27.1%	2356	2324	1.4%
API	764	818	-6.6%	1866	1624	14.9%
Total	5143	4288	19.9%	8427	7866	7.1%

Financials

YE-	Net Sales	EBITDA (Core)	EBITDA (%)	APAT	EPS (Rs)	EPS % chg	RoE (%)	P/E	EV/ EBITDA	P/BV
Mar										
FY09	12,928	2,655	20.5	1,653	13.3	77.6	27.1	23.4	16.3	6.1
FY10	15,596	3,235	20.7	2,092	16.8	26.6	28.0	18.5	13.4	4.5
FY11E	18,872	3,963	21.0	2,487	20.0	18.9	25.7	15.6	10.8	3.6
FY12E	22,506	4,726	21.0	3,050	24.5	22.6	25.4	12.7	8.9	2.9

High employee and SGA cost impacted operating performance

Operating margins for the quarter declined by 97bps to 22.8% mainly because of 173bps increase in other expenditures and higher contribution of low margin anti-malarial and tender business. The increase in other expenditures is mainly on account of higher SGA cost (new people addition). Moreover, company is also incurring cost of Rs50mn per quarter on account of Indore SEZ which has yet to contribute in topline (UKMHRA inspection is over; production to commence by Dec'11) Going forward, as the new jointee will start contributing, we expect margins to improve gradually. Company has also guided EBITDA margins of 20-21% for FY11E.

APAT at Rs730mn is below our expectation

Despite lower interest cost (down by 36%), APAT was below our expectations at Rs730mn (we expected Rs762mn) because of a) 17% increase in depreciation cost and b) higher tax provision (26% of PBT vs. our assumption of 23.5% of PBT). The company has incurred forex gain of Rs288mn vs. forex loss of Rs6mn in Q2FY10. Going ahead, we believe net profit to grow at 21% CAGR to Rs3050mn over Fy10-12E, clocking an EPS of Rs24.5 in FY12E.

Maintain buy with a target price of Rs336

During H1FY11, the company has clocked adjusted EPS of Rs9.3 against our full estimation of Rs20 in FY11E. We continue to maintain our earning estimates of Rs20 and Rs24.5 for FY11E and FY12E respectively. We believe that this quarter performance is encouraging and expect the company to improve its earnings trajectory from next quarter onwards on account of incremental contribution because of field force expansion. Over the last 4 years, company has significantly reduced its dependency on one product or one market and has expanded its reach in key geographies. We are of the view that Ipca provides good visibility in terms of consistent CAGR growth of 20% over next few years on the back of its focus on branded formulations segment, geographical expansions in semi-regulated markets, new product launches in fast growing chronic segment and focus on European and US markets. We re-iterate our Buy rating with a price target of Rs336 (14x FY12E).

Key Financials – Quarterly

Rs mn

Rs mn	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11	YoY (%)	QoQ (%)
Revenue	4,303	3,957	3,678	4,145	5,183	20.5	25.0
Expenditure	3,281	3,054	2,992	3,468	4,003	22.0	15.4
<i>as % of sales</i>	76%	77%	81%	84%	77%		
Consumption of RM	1,737	1,604	1,577	1,748	2,044	17.7	16.9
<i>as % of sales</i>	40%	41%	43%	42%	39%		
Employee Cost	574	541	530	658	700	21.8	6.4
<i>as % of sales</i>	13%	14%	14%	16%	14%		
Other expenditure	971	909	885	1,062	1,259	29.7	18.5
<i>as % of sales</i>	23%	23%	24%	26%	24%		
EBITDA	1,021	903	686	678	1,180	15.6	74.2
Depreciation	117	119	117	129	137	16.9	6.2
EBIT	904	784	569	549	1,043	15.4	90.1
Other Income	5	9	-	41	8	43.4	(81.3)
Interest	71	53	59	49	62	(12.2)	27.6
PBT	839	740	510	541	989	17.9	82.9
Total Tax	195	141	152	123	337	73.3	174.0
Adjusted PAT	643	596	358	418	730	13.5	74.7
(Profit)/loss from JV's/Ass/MI							
APAT after MI	643	596	358	418	730	13.5	74.7
Extra ordinary items	-4	-14	18	-29	211		(818.5)
Reported PAT	639	583	376	388	940	47.2	142.1
AEPS	5.1	4.7	2.9	3.3	5.8	13.5	74.7

Margins (%)

(bps)

(bps)

EBIDTA	23.7	22.8	18.7	16.3	22.8	(97)	642
EBIT	21.0	19.8	15.5	13.2	20.1	(89)	689
EBT	19.5	18.7	13.9	13.0	19.1	(42)	603
PAT	14.9	15.1	9.7	10.1	14.1	(87)	400
Effective Tax rate	23.2	19.1	29.8	22.7	34.1	1,090	1133

Financials

Income Statement

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
Net Sales	12,928	15,596	18,872	22,506
Growth (%)	21.4	20.6	21.0	19.3
Expenditure	10,273	12,360	14,909	17,779
Raw Materials	5,073	6,456	7,398	8,822
SGA	3,318	3,697	4,812	5,739
Employee Cost	1,882	2,207	2,699	3,218
Other Exp	0	0	0	0
EBITDA	2,655	3,235	3,963	4,726
Growth (%)	46.0	21.9	22.5	19.3
EBITDA margin (%)	20.5	20.7	21.0	21.0
Depreciation	397	467	559	611
EBIT	2,258	2,768	3,404	4,115
EBIT margin (%)	17.5	17.7	18.0	18.3
Other Income	6	70	30	30
Interest expenses	318	264	286	285
PBT	1,185	2,593	3,149	3,860
Tax	233	627	661	811
Effective tax rate (%)	19.6	20.0	21.0	21.0
Adjusted PAT	1,711	2,110	2,487	3,050
(Profit)/loss from JV's/Ass/MI	57	18	0	0
Adjusted PAT after MI	1,653	2,092	2,487	3,050
Growth (%)	77.6	26.6	18.9	22.6
Net Margin (%)	12.8	13.4	13.2	13.6
E/O items	-762	0	0	0
Reported PAT	1,006	2,092	2,487	3,050
Growth (%)	-26.4	108.0	18.9	22.6

Cash Flow

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
PBT (Ex-Other income)	1,179	2,504	3,119	3,830
Depreciation	397	467	559	611
Interest Provided	318	264	286	285
Other Non-Cash items	0	0	0	0
Chg in working cap	-736	-1,664	-1,138	-1,518
Tax paid	-233	-485	-661	-811
Operating Cashflow	925	1,087	2,164	2,398
Capital expenditure	-889	-1,317	-617	-750
Free Cash Flow	36	-230	1,546	1,648
Other income	6	88	30	30
Investments	-316	86	0	0
Investing Cashflow	-1,199	-1,142	-587	-720
Equity Capital Raised	42	44	0	0
Loans Taken / (Repaid)	1,069	-54	-300	-900
Interest Paid	-318	-264	-286	-285
Dividend paid (incl tax)	-323	-409	-437	-437
Income from investments	0	0	0	0
Others	-177	662	0	0
Financing Cashflow	293	-21	-1,022	-1,622
Net chg in cash	19	-76	554	56
Opening cash position	94	113	108	662
Closing cash position	113	37	662	718

Balance Sheet

Y/E, Mar (Rs. mn)	FY09	FY10	FY11E	FY12E
Equity share capital	250	250	250	250
Reserves & surplus	6,063	8,398	10,449	13,062
Net worth	6,313	8,649	10,700	13,312
Minority Interest	-4	0	0	0
Secured Loans	3,408	3,791	3,591	3,091
Unsecured Loans	1,191	754	654	254
Loan Funds	4,599	4,545	4,245	3,345
Net deferred tax liability	651	793	793	793
Total Liabilities	11,560	13,987	15,738	17,451
Gross Block	7,790	8,812	9,812	10,562
Less: Depreciation	2,022	2,433	2,992	3,603
Net block	5,768	6,379	6,820	6,959
Capital work in progress	144	383	0	0
Investment	412	325	325	325
Current Assets	7,398	8,992	11,023	13,058
Inventories	3,062	3,802	4,511	5,364
Sundry debtors	3,391	3,880	4,718	5,626
Cash & bank balance	113	108	662	718
Loans & advances	832	1,201	1,132	1,350
Other current assets	0	0	0	0
Current lia & Prov	2,162	2,097	2,437	2,898
Current liabilities	1,962	1,850	2,191	2,605
Provisions	200	247	245	293
Net current assets	5,236	6,895	8,587	10,160
Misc. exp & Def. Assets	0	0	0	0
Total Assets	11,560	13,981	15,732	17,444

Key ratios

Y/E, Mar	FY09	FY10	FY11E	FY12E
Profitability (%)				
EBITDA Margin	20.5	20.7	21.0	21.0
Net Margin	12.8	13.4	13.2	13.6
ROCE	20.9	22.1	22.9	24.8
ROE	27.1	28.0	25.7	25.4
RoIC	23.2	22.9	24.3	26.4
Per Share Data (Rs)				
EPS	13.3	16.8	20.0	24.5
CEPS	22.6	20.6	24.5	29.4
BVPS	50.7	69.5	85.9	106.9
DPS	2.2	2.8	3.0	3.0
Valuations (x)				
PER	23.4	18.5	15.6	12.7
P/CEPS	13.8	15.1	12.7	10.6
P/BV	6.1	4.5	3.6	2.9
EV / Sales	3.4	2.8	2.3	1.9
EV / EBITDA	16.3	13.4	10.8	8.9
Dividend Yield (%)	0.7	0.9	1.0	1.0
Gearing Ratio (x)				
Net Debt/ Equity	0.7	0.5	0.2	0.1
Net Debt/EBIDTA	1.7	1.3	0.9	0.6
WC Cycle	145.8	159.2	163.8	162.5

Recommendation History: Ipca Laboratories – IPCA IN

Date	Reports	Reco	CMP	Target
30/07/2010	Ipca Laboratories Q1FY11 Result Update	Buy	274	336
31/05/2010	Ipca Laboratories Q4FY10 Result Update	Buy	263	336
22/01/2010	Ipca Laboratories Q3FY10 Result Update	Buy	1,183	1,440
17/12/2009	Ipca Laboratories Event Update	Buy	999	1,107

Recent Research Reports

Date	Reports	Reco	CMP	Target
20/10/2010	Cadila Healthcare Q2FY11 Result Update	Accumulate	680	720
18/10/2010	Unichem Labs Initiating Coverage	Buy	530	670
08/10/2010	Pfizer Q3CY10 Result Update	Hold	1,093	1,100
05/10/2010	Aurobindo Pharma Visit Note	Buy	1,066	1,242

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