

Indoco Remedies (INDREM)

Rs 426

WHAT'S CHANGED...

PRICE TARGET	Changed to Rs 403 from Rs 389
EPS (FY11E)	Changed from Rs 38.9 to Rs 42.6
EPS (FY12E)	Changed from Rs 44.3 to Rs 49.0
RATING.....	Unchanged

Fairly valued...

Indoco Remedies' (IRL) Q4FY10 results were better than our expectations but surprised us negatively on the EBITDA front. The topline grew 28% YoY to Rs 109 crore on account of 22% YoY domestic growth and 42% YoY growth in exports. The EBITDA margin expanded by 225 bps (lower than our expectation of 460 bps) as employee cost and other expenses as a percentage of sales declined YoY. The EBITDA (excluding other operating income) increase of 65% YoY to Rs 11 crore was below our expectation. The net profit improved by 110% YoY to Rs 8.2 crore (we expected Rs 7.9 crore) due to lower tax charge and interest cost. On strong 28% topline growth in Q4FY10, we are revising our estimates and target prices upwards. We rate Indoco as **REDUCE** with a target price of Rs 403.

■ Highlights for the quarter

During Q4FY10, Indoco signed deals with US based Watson Pharma and South-Africa based Aspen Pharma. The Watson deal encompasses a basket of six sterile products with an addressable market size of US\$679 million. The deal with Aspen consists of seven ophthalmic products addressing 30 emerging countries. Moreover, IRL bagged a tender in Costa Rica for supply of ibuprofen tablets valued at Rs 1.5 crore. On the cost front, raw material cost rose substantially by 37% YoY while interest cost declined 44% YoY on lower working capital borrowing.

Valuation

At Rs 426, Indoco Remedies is trading at 10x FY11E and 8.7x FY12E EPS of Rs 42.6 and Rs 49.0, respectively. On an EV/EBITDA basis, the stock is trading at 6.4x FY12E estimates. Historically, the stock has traded at a one-year forward P/E of ~8.8x during the last five years. We continue to value the stock at 8.8x average of FY11-12E EPS of Rs 45.8. This gives us a target price of Rs 403. We maintain our **REDUCE** rating on the stock. Earlier than expected revenues from the recently concluded deals pose an upside risk to our estimates and stock rating.

Exhibit 1: Performance Highlights

	(Rs Crore)					
	Q4FY10A	Q4FY10E	Q4FY09	Q3FY10	YoY Gr.(%)	QoQ Gr.(%)
Net Sales	108.9	95.1	85.0	95.7	28.1	13.8
EBITDA *	11.0	11.9	6.7	11.2	64.6	-1.3
EBITDA Margin (%)	10.1	12.5	7.9	11.7	224.8	-154.1
Depreciation	3.4	2.9	3.0	3.0	12.7	11.2
Interest	0.7	0.9	1.3	0.6	-43.8	20.7
Reported PAT	8.2	7.9	3.9	8.2	109.8	0.0
EPS (Rs)	6.7	6.4	3.2	6.7		

Source: Company, ICICIdirect.com Research

* Core EBITDA

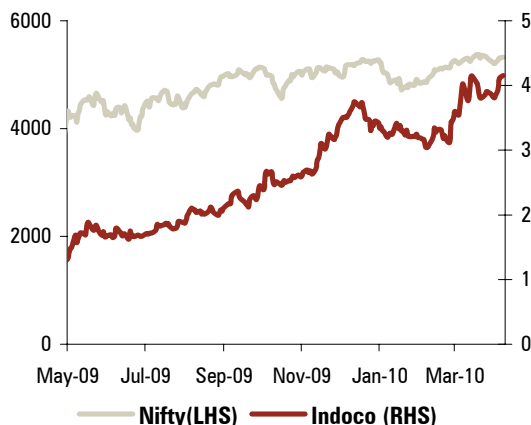
Rating matrix	
Rating	: Reduce
Target	: Rs 403
Target Period	: 12 months
Potential Upside	: -5%

Key Financials (Rs. crore)				
	FY09	FY10E	FY11E	FY12E
Net Sales	350.6	398.3	466.1	530.6
EBITDA	46.2	53.2	72.4	82.6
Net Profit	31.4	42.1	52.3	60.2

Valuation summary				
	FY09	FY10E	FY11E	FY12E
EPS (Rs)	25.6	34.2	42.6	49.0
PE (x)	16.6	12.4	10.0	8.7
Target PE (x)	15.7	11.8	9.5	8.2
EV to EBITDA (x)	11.9	10.0	7.5	6.4
Price to book (x)	1.9	1.7	1.4	1.2
RoNW (%)	11.3	13.3	14.3	14.3
RoCE (%)	10.9	11.1	13.5	13.8

Stock data	
Market Capitalisation	Rs 523.0 crore
Debt (FY09)	Rs 55.6 crore
Cash (FY09)	Rs 29.0 crore
EV	Rs 549.5 crore
52 week H/L	433/120
Equity capital	Rs 12.3 crore
Face value	Rs 10.0
MF Holding (%)	9.7
FII Holding (%)	3.0

Price movement (Stock vs. Nifty)



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Result Analysis

■ Sales growth above expectations

Indoco's topline grew 28% YoY in Q4FY10 to Rs 109 crore (we expected Rs 95 crore) buoyed by 22% growth in domestic revenue and 42% growth in exports revenue. The domestic segment, which is the largest revenue contributor, contributed 68% to the overall sales at Rs 75 crore, backed by 24% growth in the fixed dosage business. The company's key brands viz. Febrex Plus (Rs 31 crore, 18% YoY growth), Cyclopam (Rs 28 crore, 30% YoY growth), Sensodent (Rs 20 crore, 12% YoY growth) and Sensoform (Rs 11 crore, 60% YoY growth) led to the robust growth in the domestic formulation segment. The anti-infective, dental and respiratory therapies grew 46%, 6% and 33%, respectively, YoY in Q4FY10. The top five therapies contributed ~74% to the domestic formulation segment. The exports formulation business grew 34% YoY on 39% YoY growth from regulated markets contributing 29% to the overall sales and 77% to the export formulation business.

Exhibit 2: Revenue break-up						(Rs Crore)
	Q4FY10	Q4FY09	YoY %	FY09	FY08	YoY %
Domestic	74.6	60.9	22.5	279.5	250.4	11.6
% to Net Sales	68.5	71.6		70.2	71.4	
Formulations	71.8	57.7	24.5	270.7	239.5	13.0
% to Net Sales	65.9	67.8		67.9	68.3	
API	2.8	3.2	-12.8	8.8	10.9	-19.0
% to Net Sales	2.6	3.8		2.2	3.1	
Exports	34.3	24.1	42.2	118.8	100.3	18.5
% to Net Sales	31.5	28.4		29.8	28.6	
Formulations	31.2	23.3	34.2	109.1	94.8	15.1
% to Net Sales	28.7	27.4		27.4	27.0	
Regulated market	24.1	17.4	38.6	90.0	75.8	18.8
% to Net Sales	22.1	20.5		22.6	21.6	
Semi-reg market	7.1	5.9	21.3	19.1	19.1	0.2
% to Net Sales	6.5	6.9		4.8	5.4	
API	3.1	0.9	256.3	9.8	5.4	79.2
% to Net Sales	2.8	1.0		2.4	1.6	
Net Sales	108.9	85.0	28.1	398.3	350.6	13.6

Source: Company, ICICIdirect.com Research

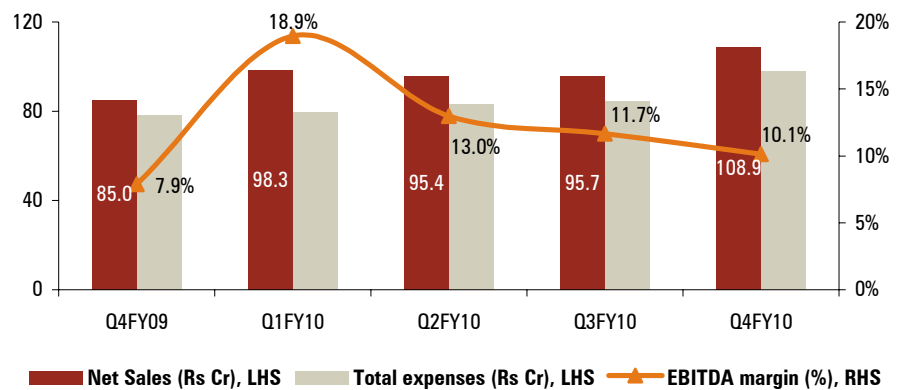
During FY10, the domestic market grew in line with the industry average. The formulation segment grew 13% YoY to Rs 271 crore contributing 68% to the overall sales. On the exports front, growth was led by ~23% contribution from regulated markets and ~5% contribution from semi-regulated markets.

EBITDA margin below expectation

The Q4FY10 EBITDA margin of ~11.6% (includes other operating income) was below our expectation of 12.5% on account of higher raw material cost. Raw material cost as a percentage of sales increased to 47% in Q4FY10 vis-à-vis 44% in Q4FY09 on account of strengthening of the US dollar as IRL's ~55-60% raw material requirement is subject to currency fluctuations as the company purchases raw materials from importers. Employee expenses also increased 15% YoY due to annual increments and recruitment of field force across two newly launched divisions in the semi-urban and chronic areas. However, there was a decline in employee and other expenses as a percentage of sales. This helped the company to prevent further erosion in margin.

During FY10, the EBITDA margin improved marginally by 42 bps on account of ~16.5% increase in raw material and ~18% increase in employee expenses. Going ahead, we expect the operating profit to grow at a CAGR of ~25% during FY10-12E. We expect an EBITDA margin of 15.6% in FY12E.

Exhibit 3: EBITDA margin trend



Source: Company, ICICIdirect.com Research
 EBITDA margins calculated on Core EBITDA

Higher net profit helped by lower interest cost

During Q4FY10, the net profit margin improved by 295 basis points to 7.6% on account of i) lower interest cost and ii) lower tax liability. During Q4FY10, Indoco borrowed working capital at ~5% rate vis-à-vis borrowings at higher rate in Q4FY09. This led the interest cost to decline ~44% YoY to Rs 0.72 crore during Q4FY10.

Exhibit 4: Common size statement (% of net sales)

	Q4FY09	Q1FY10	Q2FY10	Q3FY10	Q4FY10
Net Sales	100	100	100	100	100
Other Operating Income	1.7	2.4	0.8	0.3	1.5
EBITDA	7.9	18.9	13.0	11.7	10.1
Depreciation	3.5	2.8	3.0	3.2	3.1
Interest	1.5	0.9	0.7	0.6	0.7
PBT	4.5	17.6	10.0	8.2	7.8
Tax	-0.1	0.4	0.4	0.1	0.3
PAT	4.6	17.2	9.7	8.1	7.6

Source: Company, ICICIdirect.com Research

Valuations

We expect IRL's domestic sales to grow at a CAGR of ~12% during FY10-12E to Rs 350 crore on account of the continued focus on power brands and new launches. With new order execution, we believe IRL would be able to grow its sales and net profit at a CAGR of 15% and 20%, respectively, over FY10-12E.

At Rs 426, Indoco Remedies trades at 10x FY11E and 8.7x FY12E EPS of Rs 42.6 and Rs 49.0, respectively. On an EV/EBITDA basis, the stock is trading at 6.4x FY12E estimates. Historically, the stock has traded at a one-year forward P/E of ~8.8x over the last five years. We continue to value the stock at 8.8x average of FY11-12E EPS of Rs 45.8. This gives us a target price of Rs 403. We maintain our **REDUCE** rating on the stock. The risk to our call would be earlier than expected revenues from the recently concluded deals.

Exhibit 5: Valuation table

	Sales (Rs)		EPS Gr		PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
	Cr)	Sales Gr (%)	EPS (Rs)	(%)				
FY09	350.6	33.5	25.6	-1.5	16.6	11.9	11.3	10.9
FY10E	398.3	13.6	34.2	33.8	12.4	10.0	13.3	11.1
FY11E	466.1	17.0	42.6	24.3	10.0	7.5	14.3	13.5
FY12E	530.6	13.8	49.0	15.0	8.7	6.4	14.3	13.8

Source: Company, ICICIdirect.com Research

ICICIdirect.com Coverage Universe

Alembic					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	ALECHE	CMP	51	FY08	1003.2	8.0	6.3	7.6	32.6	19.1
		Target	49	FY09	1116.1	3.4*	14.9	9.2	14.0*	11.3
MCAp	704.7	Upside (%)	-4	FY10E	1169.0	4.0	12.7	7.0	11.1	10.8
				FY11E	1251.7	5.4	9.4	5.5	13.5	12.7
Biocon					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	BIOCON	CMP	296	FY08	1108.2	23.2	12.8	9.9	14.8	13.8
		Target	335	FY09	1608.7	12.0	18.2*	19.9	11.4	13.2
MCAp	5914.0	Upside (%)	13	FY10E	2345.0	15.1	19.6	12.9	14.8	18.6
				FY11E	2789.4	19.9	14.8	11.5	18.7	22.8
Dishman					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	DISHPHA	CMP	224	FY08	803.1	14.7	15.2	15.1	21.3	9.5
		Target	237	FY09	1062.4	18.2	12.3	9.5	20.8	13.6
MCAp	1806.8	Upside (%)	6	FY10E	911.9	15.8	14.2	11.2	18.0	9.5
				FY11E	1075.3	19.8	11.3	8.0	18.4	12.1
IPCA Labs					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	IPCLAB	CMP	269	FY08	1051.3	10.9	24.7	6.1	23.1	15.2
		Target	255	FY09	1284.0	8.1	33.2	4.4	16.0	19.6
MCAp	3358.8	Upside (%)	-5	FY10E	1516.3	17.3	15.5	3.1	26.7	24.1
				FY11E	1745.4	18.2	14.8	2.7	22.8	21.9
Piramal Health					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	NICPIR	CMP	518	FY08	2848.3	16.0	32.4	22.1	30.7	24.6
		Target	458	FY09	3281.1	15.1	34.2	20.8	24.0	17.7
MCAp	10826.2	Upside (%)	-12	FY10E	3668.8	21.0	24.6	17.4	26.4	17.8
				FY11E	3819.7	26.2	19.8	13.5	25.8	21.8
Sun Pharma					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	SUNPHA	CMP	1598	FY08	3356.7	71.8	22.3	20.5	29.8	30.4
		Target	1600	FY09	4271.4	88.1	18.1	17.0	25.9	28.5
MCAp	33097.4	Upside (%)	0	FY10E	3999.3	63.7	25.1	24.2	17.4	17.9
				FY11E	4920.7	84.2	19.0	17.4	19.3	20.8
Glenmark					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	GLEPHA	CMP	263	FY08	2037.4	25.4	10.3	9.2	41.7	34.2
		Target	288	FY09	2093.0	7.7	34.3	21.8	19.4	16.4
MCAp	7056.0	Upside (%)	10	FY10E	2373.3	10.9	24.2	14.5	12.8	14.1
				FY11E	2730.8	16.8	15.6	11.1	19.7	20.6
Lupin					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	LUPIN	CMP	1675	FY08	2706.4	49.8	33.7	33.7	31.9	22.2
		Target	1840	FY09	3775.9	61.3	27.3	23.2	35.6	23.6
MCAp	14850.6	Upside (%)	10	FY10E	4688.0	71.6	23.4	19.0	30.3	24.4
				FY11E	5968.8	92.2	18.2	13.9	27.3	26.4
				FY12E	7062.1	113.4	14.8	11.0	24.5	25.2
Unichem					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	LUPIN	CMP	427	FY09	735.2	30.0	14.3	10.9	22.3	23.2
		Target	486	FY10E	760.2	28.6	14.9	10.2	18.0	20.1
MCAp	1539.7	Upside (%)	14	FY11E	899.4	39.3	10.9	7.3	20.9	23.6
				FY12E	1050.6	47.6	9.0	5.8	21.4	24.5
Indoco Rem					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	LUPIN	CMP	426	FY09	350.6	25.6	16.6	11.9	11.3	10.9
		Target	403	FY10E	398.3	34.2	12.4	10.0	13.3	11.1
MCAp	523.0	Upside (%)	-5	FY11E	466.1	42.6	10.0	7.5	14.3	13.5
				FY12E	530.6	49.0	8.7	6.4	14.3	13.8

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 Buy: Between 10% and 20%;
 Add: Up to 10%;
 Reduce: Up to -10%
 Sell: -10% or more;

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