

Biocon reported 15% growth in its consolidated revenues to Rs.730 crore, primarily led by 22% growth in the biopharma business and 339% jump in licensing income. With improving product mix towards higher licensing income, the OPM expanded by 310bps to 23.3%, resulting in 25% growth in net profit to Rs.101 crore. The reported profits were a bit lower, as Biocon expensed an one-off R&D cost worth Rs.35 crore relating to prior period and provided higher taxes during the quarter.

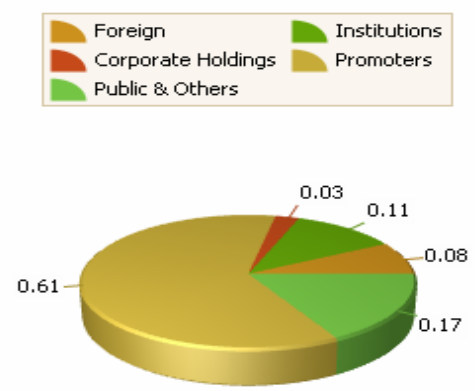
Q3FY11 Snapshot

- **Biopharma leads to revenue growth:** Higher sales in Biopharma (+22% YoY; +15% QoQ) & higher licensing income (up 339% YoY – largely from Pfizer) led to good revenue growth of more than 15% YoY. Launch of tacrolimus earlier in FY11, continued growth in the India branded biz & a pickup in statins were the main factors aiding strong growth in Biopharma. Research services (+14%) also grew well following a pickup in fortunes at Syngene.
- **Axicorp puts pressure:** Axicorp (German Subsidiary) has posted a top line de growth 15.6% y-o-y during Q3FY11 which was due to German government’s decision to offer 16% rebate to customers for next 3 years. Axicorp is currently revamping its product portfolio by moving towards higher margin segments wherein its growth is sustainable.
- **Improvement seen in Research services business:** Research services business gained slight momentum during the quarter posting growth of 14% y-o-y. The restructuring exercise in Syngene and Clinigene is now heading towards closure. The EBIDTA margin for the first time showed improvement after the change in business model. The company is changing its business model from fee based to higher margin risk-reward based model. Net Profit growth (+22% YoY) was subdued due to unusually higher tax rate (22% vs. 15%).
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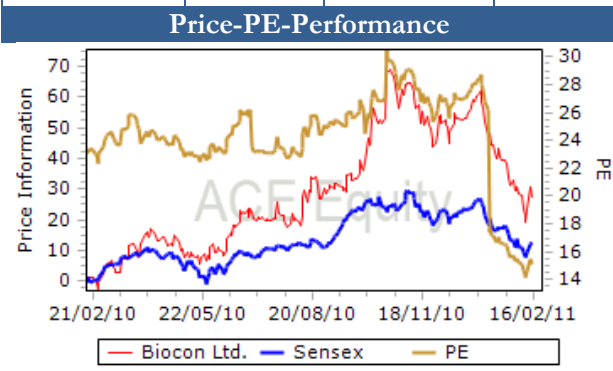
Outlook & Recommendation

We continue to hold positive outlook on the Biocon. Since our recommendation the stock has corrected close to 24%, in line with the market. At the CMP of Rs.336, stock trades at a TTM PE of 15.14x and we are of the view that the valuation has become quite attractive to accumulate the stock. **Looking at the multiple triggers, in terms of value unlocking of Biocon’s R&D pipeline, likely deals in the field of research services and its global commercialisation pact with Pfizer, we maintain our ACCUMULATE recommendation with a target of Rs.510 (target P/E of 27x) over the next 10-12 months.**

Recommendation - Accumulate	
CMP	Rs.336
Target Price	Rs.510
Investment Horizon	10-12 months
Basic Details	
BSE Code/NSE Symbol	532523/BIOCON
Bloomberg/Reuters	BIOS IN/BION.BO
Industry	Pharmaceuticals
Face Value	5.00
BSE 52 Wk High/Low	464.60/253.15
Key Indicators	
Shares Outstanding	20 Cr.
Market cap. (Rs Cr)	6721.00
Average 2 wk volume	96.58
Latest Book Value	98.40
TTM EPS	17.89
TTM PE (x)	18.78
Industry PE	10.42
Price/BV (x)	3.42
Dividend Yield %	1.04
EV / EBITDA (TTM)	11.62
Mcap / Sales (TTM)	2.47
Share Holding Pattern (%)	



Performance (in % terms)			
	3m	6m	12m
Industry	-11.04	7.06	23.91
Company	-18.94	-1.74	29.40
Sensex	-10.02	0.59	13.94



Q3FY11 Snapshot

Particular	Q2FY11	Q2FY10	Var (%)	Q1FY11	Var (%)
Net Sales	728.05	635.12	14.63	678.77	7.26
Total Expenditure	559.73	508.42	10.09	535.18	4.59
Raw Materials	331.13	355.61	-6.88	393.04	-15.75
<i>% Net Sales</i>	45.48	55.99		57.90	
Employee Cost	81.11	63.74	27.25	75.11	7.99
<i>% Net Sales</i>	11.14	10.04		11.07	
PBIDT (Excl OI)	170.04	128.58	32.24	144.76	17.46
Other Income	7.91	4.54	74.23	7.77	1.80
Operating Profit	177.95	133.12	33.68	152.53	16.67
Interest	6.56	2.72	141.18	6.51	0.77
PBDT	171.39	130.40	31.43	146.02	17.37
<i>PBDTM (%)</i>	<i>23.54</i>	<i>20.53</i>		<i>21.51</i>	
Depreciation	40.58	35.96	12.85	39.04	3.94
PBT	130.81	94.44	38.51	106.98	22.28
Tax	29.07	11.20	159.55	15.60	86.35
PAT	101.74	83.24	22.22	91.38	11.34
<i>PATM (%)</i>	<i>13.97</i>	<i>13.11</i>		<i>13.46</i>	

Comparative Sales Break Up and Analysis

Segmental Sales	Q3FY11	Q3FY10	% Growth
Bio Pharmaceutical	354	289.5	22.28
<i>% of sales</i>	<i>48.63</i>	<i>45.59</i>	
Contract Research	78.8	69.4	13.54
<i>% of sales</i>	<i>10.82</i>	<i>10.93</i>	
Axi-Corp	218.4	258.7	-15.58
<i>% of sales</i>	<i>30</i>	<i>40.74</i>	
Licensing Income	76.8	17.5	338.86
<i>% of sales</i>	<i>10.55</i>	<i>2.76</i>	
<i>Total</i>	<i>728</i>	<i>635</i>	14.65

Concall Takeaways

- Encouraged by the oral insulin (IN 105) trial results and hopes to be able to shortlist a potential licensing partner in the next 6 months
- Revenues from India and other emerging markets under the insulin deal with Pfizer to commence in FY12
- Plans to bolster immunosuppressants pipeline with 3 new products (one filed, two under development for the US)
- Expects to launch reusable pen for insulin in mid-2011
- Expects to file human insulin in Europe in mid CY12. Glargine trials for EU to also start in CY11

Key Investment Arguments

- ❑ Biocon and Pfizer have entered into a strategic agreement for global commercialization of Biocon's biosimilar versions of insulin and insulin analogues. The potential global opportunity for the above said biosimilar products amount to about \$14 billion
- ❑ Going forward, the company will be focusing on chronic segments and embark on its brand building exercise for its larger brands. It also plans to launch 'Advacan', a drug for renal and heart transplant recipients in Q3FY11.
- ❑ The management expects a CAGR of 25-30% for next 2-3 years resulting into sales of Rs.500 crore by 2015 in domestic formulations business.
- ❑ Biocon is gradually shifting its focus from low margin statins business to high margin insulin business.
- ❑ Biocon's established capabilities along with the drug value chain business model make it a strong player to take advantage of emerging opportunities in the biopharmaceutical space
- ❑ The company is developing an oral form of insulin as a part of its NCE research, thus offering the potential for an "option value" (if successful) over the core business

Investment Concerns

- ❑ Significant capex and investment to fund future initiatives may temper earnings growth in the short-term
- ❑ Higher R&D costs and higher expenses linked to the scale-up of the domestic formulations business will continue to pare earnings growth

Future Outlook

Going ahead, incremental revenues flowing from Critical care operation, supply to Biocon's focus going forward will be on insulin, immunosuppressant, and branded formulations, which will be critical in driving growth in the future. The company has also been active in inking deals with innovator companies such as Mylan and Amylin for developing biotech products, which will augur well from a long-term perspective. Besides this, there are some biologics programs in the pipeline which will enhance revenues in the longer term and could translate into licensing opportunities. Though Next few quarters appear to be challenging for Biocon as core business growth seems muted. Given the high R&D spending in H2 FY11 (FY11 guidance of Rs.150 crore, incurred Rs.40 crore in H1 FY11), pressure on margins is likely to continue. Biocon's deal with Pfizer is a long term positive (beyond 2015 when products are launched in US/EU) though nothing much may accrue in the short term (emerging markets). Of the US\$ 200 mn upfront payment, Biocon would receive US\$ 100 mn in Q3 FY11 while US\$ 100 mn would be kept in an escrow account and accrue to Biocon over a period of 3-5 years. Development cost of US\$ 200mn (4-5 years) and capex of US\$ 170mn (next 3 years) would be funded entirely by Biocon.

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Anexure Consolidated Annual Results

Description (Rs. Cr.)	FY10	FY09	FY08	FY07	FY06
Total Income	2439.03	1673.23	1092.86	999.43	796.82
Growth (%)	45.77	53.11	9.35	25.43	8.85
Total Expenditure	1930.53	1285.31	757.67	712.01	561.98
Growth (%)	50.20	69.64	6.41	26.70	14.25
EBIDT	508.51	387.91	335.20	287.42	234.84
EBITDA Margin (%)	20.85	23.18	30.67	28.76	29.47
PBIT	368.37	277.66	241.27	220.87	205.19
PBT	351.47	260.00	230.91	211.00	202.55
PAT	302.81	248.16	218.02	194.08	171.98
Growth (%)	22.02	13.82	12.33	12.85	-12.48
Sources of Funds					
Equity Paid Up	100.00	100.00	50.00	50.00	50.00
Reserves and Surplus	1595.96	1369.32	1397.80	992.55	827.55
Net Worth	1695.01	1468.37	1446.85	1041.44	876.28
Total Debt	513.61	523.92	255.06	186.77	105.05
Capital Employed	2304.30	2058.48	1730.93	1253.47	995.10
Application of Funds					
Gross Block	1837.13	1581.70	1182.39	1066.11	407.05
Investments	430.58	367.62	474.77	79.09	100.23
Cash and Bank balance	139.93	11.81	9.62	8.73	2.02
Net Current Assets	512.06	354.85	234.12	254.60	98.86
Total Current Liabilities	579.99	437.54	300.52	274.94	261.26
Total Assets	2305.25	2059.43	1731.88	1254.58	996.37
Key Ratios					
Debt to Equity(x)	0.33	0.27	0.18	0.15	0.11
Current Ratio(x)	2.22	2.22	2.32	2.28	1.65
ROCE(%)	16.89	14.65	16.17	19.65	22.66
RONW(%)	19.14	17.03	17.52	20.24	21.40
PBIDTM(%)	20.91	23.53	31.02	28.13	28.46
PATM(%)	12.45	15.05	20.18	18.99	20.84

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