

Strong operating performance

27 January 2009

BUY

Price	Target Price
Rs330	Rs637

Sensex –	8,674
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Price Performance

(%)	1M	3M	6M	12M
Absolute	(8)	(27)	(39)	(48)
Rel. to Sensex	1	(18)	0	3

Source: Bloomberg

Stock Details

Sector	Pharmaceuticals
Reuters	IPCA.BO
Bloomberg	IPCA@IN
Equity Capital (Rs mn)	252
Face Value (Rs)	10
No of shares o/s (mn)	25
52 Week H/L (Rs)	723/287
Market Cap (Rs bn /USD mn)	8/162
Daily Avg Vol (No of shares)	18504
Daily Avg Turnover (US\$ mn)	0.1

Shareholding Pattern (%)

	31/12/08	30/9/08	30/6/08
Promoters	46.0	46.1	46.1
FII/NRI	0.8	0.8	0.7
Institutions	37.5	37.1	33.3
Private Corp.	4.1	4.7	9.0
Public	11.7	11.4	11.0

Source: Capitaline

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Ipca's Q3FY09 revenues grew by 14% to Rs3.1bn (est. of 21%) on the back of 20% growth in export business. Branded formulation business in export market grew by 50%. Tender business of Rs190mn in Q3FY08 has restricted the domestic growth to 8.4% to Rs1436mn, however, excluding the tender business, the domestic formulation business has outpaced the industry growth and grew by 23% to Rs1156mn vs. the industry growth of 10.8%. The growth in domestic formulation business is on the back of increased contribution from life style segment. EBIDTA for the quarter was up by 40% to Rs712mn driven by 730 bps reduction in raw material cost (because of reduction in solvent prices due to crude oil) and increased contribution from formulation segment. Higher interest cost (up by 108%) and tax outgo (24% vs. 20.9% in Q3FY08) coupled with forex loss of Rs192mn vs. forex gain of Rs108mn in Q3FY08 resulting 40% decline in RPAT to Rs232mn. However after adjusting the Forex loss/gain, the APAT witnessed a growth of 27% to Rs378mn. At CMP of Rs354, the stock is trading at 4.4x FY10E earnings. We maintain our BUY with a target price of Rs637.

Branded formulation continue to grow at robust pace

Ipca's focus on high margin branded formulation segment continued to drive revenue and margin growth for the company. Though the overall revenue grew by only 14% because of tender business last year (contributed Rs190mn in Q3FY08), however branded formulation business in semi-regulated markets and domestic market grew by 50% and 23% respectively. Company's Russian business grew by 70% to Rs723mn in Q3FY09. In US, out of 11 ANDAs company has filed, 8 are already approved. Company has so far launched 4 products and 5th one is likely to be launched in Q4FY09. Management is confident of achieving US\$10mn revenue from US in FY10E.

EBIDTA margins expanded by 410bps

Operating margins during the quarter expanded by 410bps to 22.7% on the back of 730 bps reduction in raw material cost. The reduction in raw material cost was mainly because of softening of solvent prices driven by reduction in crude oil prices and improved product mix.

APAT grew by 27%

Higher interest cost (up by 108%) and tax out go (24% vs. 20.9% in Q3FY08) coupled with forex loss of Rs192mn vs. forex gain of Rs108mn in Q3FY08 resulting 40% decline in RPAT to Rs232mn. Out of Rs192mn forex loss, realized loss was Rs80mn on forward contracts. However adjusting to Forex loss/gain, the APAT grew by 27% to Rs 378mn (Rs 298mn in Q1FY08). During the quarter, total debt has increased from Rs3.5bn to Rs4.4bn, out of which foreign currency loan is US\$37mn.

Segment wise revenue break-up

Rs mn	Q3FY09	Q3FY08	Y-o-Y Gr.(%)	9MFY09	9MFY08	Y-o-Y Gr.(%)
Domestic	1411	1308	7.9%	4607	4073	13.1%
Formulation	1156	1137	2%	3820	3496	9%
Domestic Form Revenue from	1156	942	23%	3741	3146	19%
Tender	0	195		79	350	-77%
API	256	171	50%	787	578	36%
Exports	1697	1414	20.0%	4874	3889	25.3%
Formulation	1129	906	24.6%	3071	2480	23.8%
API	569	509	11.8%	1803	1409	28.0%
Total Sales	3109	2722	14.2%	9481	7962	19.1%

Buyback of share

Company has announced buy back of its share through open market operations at price not exceeding Rs600 per share. The total amount set aside for the buyback is Rs600mn. Assuming an average price of Rs400 per share (CMP Rs354/ share) for the buyback, the total number of shares bought back works out to 1.5mn. We believe this will lead to EPS accretion of 6.3% in FY10E (Rs84.6).

The table below presents various scenarios at which, depending upon the average buyback price, EPS accretion for FY10E will be

Average buyback price (Rs)	EPS accretion (%) FY10E
400	6.3%
375	6.8%
350	7.3%
325	7.9%

Management has announced that the buy-back will be done through internal accruals. So far company has bought 0.1mn shares from the market.

Outlook and Valuation

Ipca's focus on building brands through concentrating on branded formulation business in India as well as semi-regulated market has resulted steady growth in revenues and expansion in operating margins. Company has been consistently outpacing the industry growth in domestic formulation segment driven by increased focus on high growth life style segment. We believe this focus has resulted increased contribution from formulation business to 74% with a CAGR growth of 24% over last five years. We expect it to further improve with strategic focus on branded formulations segment, geographical expansions in semi-regulated markets (a 500+ sales people network across multiple semi-regulated markets (excluding India)), new product launches in fast growing life style segments and focus on European and US markets. Going forward, its focus in the US market will become growth driver from FY10E onwards. With strong visibility of an earning growth, 30% ROE, no fears of dilution, we believe that Ipca is an excellent investment opportunity. At CMP of Rs354, the stock is trading at 4.4x FY10E earnings. We maintain our BUY rating with a target price of Rs637. Key risk to our call remains the currency appreciation.

Key Financials

Income Statement	Standalone							Consolidated			
	Y/E, Mar (Rs. m)	Q3FY09	Q3FY08	Y-o-Y Gr.(%)	Q2FY09	Q-o-Q Gr.(%)	9MFY09	9MFY08	Y-o-Y Gr.(%)	FY08	FY09E
Net Sales (incl Operating income)	3133	2736	14%	3476	-10%	9558	8065	19%	10842	12671	14332
Expenses	2421	2229	9%	2643	-8%	7418	6596	12%	8660	9915	11195
Raw Materials	1183	1234	-4%	1288	-8%	3636	3552	2%	4639	5251	5879
% of sales	37.8	45.1	-16%	37	2%	38.0	44.0	-14%	42.8	41.4	41.0
Employee cost	434	345	26%	476	-9%	1349	1079	25%	1470	1691	1919
% of sales	13.8	12.6	10%	14	1%	14.1	13.4	5%	13.6	13.3	13.4
Other expenses	804	650	24%	879	-9%	2433	1964	24%	2551	2973	3396
% of sales	25.7	23.7	8%	25	1%	25.5	24.4	4%	24	23	24
EBIDTA (Reported)	712	508	40%	832.3	-14%	2140	1469	46%	2182	2757	3137
EBIDTA %	22.7	18.6	410 bps	23.9	-120bps	22.4	18.2	420bps	20.1	21.8	21.9
Other income	3	6	-45%	5	-36%	12	15	-22%	100	70	50
Interest	115	55	108%	71	62%	225	155	46%	204	258	226
Depreciation	104	81	27%	94	11%	287	237	21%	325	400	463
PBT	304.9	484.9	-37%	437.3	-30%	1036.7	1521.3	-32%	1753.5	2168.4	2497.4
Total Tax	73.1	101.5	-28%	72.2	1%	203.5	336.5	-40%	358.0	444.5	499.5
Effective tax rate (%)	24.0	20.9	15%	16.5	45%	19.6	22.1	-11%	20.4	20.5	20.0
RPAT	231.8	383.4	-40%	365.1	-37%	833.2	1184.8	-30%	1360.1	1120.6	1998.0
E/O items	-192.3	107.7		-235.9		-603.3	429.0		0.0	-603.3	0.0
Adjusted PAT	378.0	298.2	27%	520.3	-27%	1318.1	850.7	55%	1360.1	1723.9	1998.0
Net Margin (%)	12.1	10.9	120 bps	15.0	-290bps	13.8	10.5	325bps	12.5	13.6	13.9
EPS (diluted)	15.1	11.9	27%	20.8	-27%	52.7	34.0	55%	54.5	68.7	79.7

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