

29<sup>th</sup> May 2009**BUY**

Price	Target Price
<b>Rs487</b>	<b>Rs660</b>

Sensex –	<b>14,296</b>
----------	---------------

**Price Performance**

(%)	1M	3M	6M	12M
Absolute	13	39	36	(21)
Rel. to Sensex	(8)	(12)	(13)	(5)

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 )	624/285
Market Cap (Rs bn /USD mn)	12/285
Daily Avg Vol (No of shares)	19673
Daily Avg Turnover (US\$ mn)	0.1

**Shareholding Pattern (%)**

	31/03/09	31/12/08	30/9/08
Promoters	46.4	46.0	46.1
FII/NRI	1.2	0.8	0.8
Institutions	35.4	37.5	37.1
Private Corp.	5.0	4.1	4.7
Public	12.1	11.7	11.4

Source: Capitaline

**Manoj Garg**

manoj.garg@emkayshare.com

+91 22 6612 1257

**Akshat Vyas**

akshat.vyas@emkayshare.com

+91 22 6612 1491

Ipca's focus on building brands through concentrating on branded formulation business 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. In Q4FY09, revenues grew by 29% to Rs3.1bn on the back of a) 38% growth in export formulation business, & b) 34% growth in domestic formulation business. On the operating front, the company reported a growth of 63% to Rs 533mn in Q4FY09, driven by a) 140 bps reduction in raw material cost & b) 300bps reduction in other expenses. Higher interest cost (up by 71%), tax out go (26.8% vs. 8.5% in Q4FY08) and MTM losses of Rs154mn, the company reported a decline of 65% in the bottom line to Rs 79mn. However adjusting to Forex loss of Rs 154mn and Rs 102mn for provision for investment/ loan in subsidiary, the APAT grew by 30% to Rs 296mn. For FY09, revenue was up by 22% to Rs 12.8bn and APAT was up by 64% to Rs1655mn. At CMP of Rs487, the stock is trading at 6.2x FY10E earnings. We upgrade our price target from Rs637 to Rs660 (8x one year forward rolling EPS of Rs82.5). We reiterate our BUY rating.

**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 tender business for FY09 declined significantly from Rs 470mn to Rs 79mn, the overall domestic formulation business grew on the back of significant growth from lifestyle segments like CVS, CNS and Pain management. For FY09 the branded formulation business in export markets and domestic market grew by 49% and 24% respectively. The contribution of high margin branded formulation business in India and other semi-regulated market has increased to 51% in FY08 from 48% of sales in FY09. Management has given a guidance of 18-20% growth in the topline in FY10E.

**Segment wise revenue break-up**

	Q4FY09	Q4FY08	Y-o-Y Gr.(%)	FY09	FY08	Y-o-Y Gr.(%)
<b>Domestic</b>	<b>1257</b>	<b>1038</b>	<b>21.0%</b>	<b>5952</b>	<b>5070</b>	<b>17.4%</b>
Formulation	940	703	34%	4803	3850	24%
Tender	-	120	-	79	470	
API	317	297	7%	1070	750	43%
<b>Exports</b>	<b>1929</b>	<b>1474</b>	<b>30.9%</b>	<b>6800</b>	<b>5364</b>	<b>26.8%</b>
Formulation	1300	940	38.3%	4370	3421	27.8%
API	629	534	17.9%	2430	1943	25.1%
	<b>3186</b>	<b>2512</b>	<b>26.8%</b>	<b>12752</b>	<b>10434</b>	<b>22.2%</b>

**EBIDTA margins expanded by 420bps for FY09**

Operating margins during the year expanded by 420bps to 20% on the back of 460 bps reduction in raw material cost. The reduction in raw material cost was mainly because of improved product mix and softening of solvent prices driven by reduction in crude oil prices. Going forward we expect, company to maintain similar operating margins.

**Adjustment of Forex loss & Provisions**

During the year, the company has reported a MTM loss of Rs 756.9mn out of which Rs 495 mn was on account of realized losses on forward contracts and Rs 262mn on account of MTM losses on forward contracts, maturing in next 6 months. The company has transferred Rs305mn in the 'Foreign Currency Hedging Reserve' account as MTM losses for the contracts which are maturing beyond 6 months. This amount will be charged to P&L account when this contracts will materialized depending upon the currency movement. Company has sold forward contracts worth \$80mn at Rs47.5/USD, which is 43% of the projected export sales in FY10E. The company has also made a provision of Rs 101.9mn for investment/ loan in Brazilian subsidiary.

## APAT grew by 64% for FY09

Higher interest cost (up by 56%) coupled with forex loss resulted in a 26% decline in RPAT to Rs 1008mn. However adjusting to Forex loss/gain, the APAT grew by 64% to Rs 1655mn (Rs 1010mn in FY08). During the quarter, total debt has increased from Rs3.5bn to Rs4.5bn, out of which foreign currency loan is US\$ 25mn. The average debt cost is around 6.25- 6.5%.

## Revised Table

On the back of strong growth in branded formulation business and improved performance of APIs segment, we are revising our revenue estimates for FY10E and FY11E upwards by 6% and 7% respectively. However because of appreciation in Rupees, higher R&D expenses and increased SG&A cost, we have moderated our operating margins by 160 bps and 180 bps for FY10E and FY11E respectively. Our earning estimate remain unchanged because of impact of higher revenue growth will be negated by contraction in operating margins.

	FY10E	FY11E
<b>Revenue (Rs mn)</b>		
Old Estimate	14332	16244
New Estimate	15129	17414
% Change	6%	7%
<b>EBIDTA Margins</b>		
Old Estimate	21.9	22.1
New Estimate	20.3	20.3
% Change	-160 bps	-180 bps
<b>PAT</b>		
Old Estimate	1998	2358.2
New Estimate	1971	2360
% Change	-1%	0%
<b>EPS (Rs)</b>		
Old Estimate	79.7	94
New Estimate	78.6	94.1
% Change	-1%	0%

## Outlook and Valuation

Ipca's focus on branded formulation business has resulted 20% growth and 420 bps expansion in operating margins in FY09. We believe 20% growth in revenue is more credible because of the fact that during the year company has closed down its low margins intermediary business (contribution of Rs100mn vs. Rs300mn in FY08) and its tender business has come down from Rs470mn in FY08 to Rs79mn in FY09. In the last five years, its formulation business has grown at a CAGR of 25%. 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 Rs487, the stock is trading at 6.2x FY10E and 5.2x FY11E earnings. We are rolling our target price to one year forward rolling PE and upgrade our target price from Rs637 to Rs660 (8 years average one year forward PE multiple) and reiterate BUY rating. Key risk to our call remains the currency appreciation.

Income Statement Y/E, Mar (Rs. m)	Standalone					Consolidated				
	Q4FY09	Q4FY08	Y-o-Y Gr.(%)	Q3FY09	Q-o-Q Gr.(%)	FY09	FY08	Y-o-Y Gr.(%)	FY10E	FY10E
Net Sales (incl Operating income)	3171	2460	29%	3133	1%	12838	10513	22%	15129	17414
Expenses	2638	2132	24%	2421	9%	10274	8835	16%	12065	13888
Raw Materials	1345	1079	25%	1183	14%	5073	4639	9%	5931	6826
% of sales	42.4	43.8	-3%	38	12%	39.5	44.1	-10%	39.2	39.2
Employee cost	494	360	37%	434	14%	1882	1470	28%	2254	2595
% of sales	15.6	14.6	6%	14	13%	14.7	14.0	5%	14.9	14.9
Other expenses	798	693	15%	804	-1%	3319	2726	22%	3881	4467
% of sales	25.2	28.2	-11%	26	-2%	25.9	25.9	0%	26	26
EBIDTA (Reported)	533	328	63%	712.2	-25%	2565	1678	53%	3064	3526
EBIDTA %	16.8	13.3	410 bps	22.7	-120 bps	20.0	16.0	420 bps	20.3	20.3
Other income	15	52	-71%	3	369%	95	167	-43%	6	6
Interest	79	46	71%	115	-31%	318	204	56%	276	231
Depreciation	106	85	25%	104	3%	397	325	22%	475	526
PBT	107.9	248.2	-57%	304.9	-65%	1183.2	1752.4	-32%	2319.0	2776.2
Total Tax	28.9	21.0	38%	73.1	-60%	175.2	393.3	-55%	347.9	416.4
Effective tax rate (%)	26.8	8.5	217%	24.0	12%	14.8	22.4	-34%	15.0	15.0
RPAT	79.0	227.2	-65%	231.8	-66%	1008.0	1359.1	-26%	1971.2	2359.7
E/O items	-255.5	-1.0		-192.3		-761.5	436.3		0.0	
Adjusted PAT	296.2	228.0	30%	317.2	-7%	1655.3	1010.1	64%	1971.2	2359.7
Net Margin (%)	9.3	9.3	120 bps	10.1	-290 bps	12.9	9.6	325 bps	13.0	13.6
EPS (diluted)	11.9	9.1	30%	12.7	-7%	66.2	40.4	64%	78.6	94.1

**DISCLAIMER:** This document is not for public distribution and has been furnished to you solely for your information and may not be reproduced or redistributed to any other person. The manner of circulation and distribution of this document may be restricted by law or regulation in certain countries, including the United States. Persons into whose possession this document may come are required to inform themselves of, and to observe, such restrictions. This material is for the personal information of the authorized recipient, and we are not soliciting any action based upon it. This report is not to be construed as an offer to sell or the solicitation of an offer to buy any security in any jurisdiction where such an offer or solicitation would be illegal. No person associated with Emkay Global Financial Services Ltd. is obligated to call or initiate contact with you for the purposes of elaborating or following up on the information contained in this document. The material is based upon information that we consider reliable, but we do not represent that it is accurate or complete, and it should not be relied upon. Neither Emkay Global Financial Services Ltd., nor any person connected with it, accepts any liability arising from the use of this document. The recipient of this material should rely on their own investigations and take their own professional advice. Opinions expressed are our current opinions as of the date appearing on this material only. While we endeavor to update on a reasonable basis the information discussed in this material, there may be regulatory, compliance, or other reasons that prevent us from doing so. Prospective investors and others are cautioned that any forward-looking statements are not predictions and may be subject to change without notice. We and our affiliates, officers, directors, and employees world wide, including persons involved in the preparation or issuance of this material may; (a) from time to time, have long or short positions in, and buy or sell the securities thereof, of company (ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the company (ies) discussed herein or may perform or seek to perform investment banking services for such company(ies) or act as advisor or lender / borrower to such company(ies) or have other potential conflict of interest with respect to any recommendation and related information and opinions. The same persons may have acted upon the information contained here. No part of this material may be duplicated in any form and/or redistributed without Emkay Global Financial Services Ltd.'s prior written consent. No part of this document may be distributed in Canada or used by private customers in the United Kingdom. In so far as this report includes current or historical information, it is believed to be reliable, although its accuracy and completeness cannot be guaranteed.

Emkay Global Financial Services Ltd.,  
Paragon Center, H -13 -16, 1st Floor, Pandurang Budhkar Marg, Worli, Mumbai – 400 013.  
Tel: +91-22-66121212, Fax: +91-22-66242410