



# Biocon

DOLAT CAPITAL

CMP: ₹ 319

Target Price: ₹ 421

Buy

Biocon has shifted its focus from statins to branded biotech formulations and contract research services. We estimate Biopharma division to grow at 17% CAGR over FY11-13E with increasing contribution from domestic branded formulations and ramp up in bulk supplies for products going off patent. The company is gearing up its product pipeline to leverage on the Biosimilar opportunity in key regulated markets (products going off-patent in 2014-2018E). We estimate 18% revenue growth in its CRO segment over FY11-13E with increased focus on integrated drug development services. Favourable data on Oral insulin IN105 (Phase I trials ongoing in US) shall be a key valuation driver, given the potential size of the opportunity and the status as a novel product.

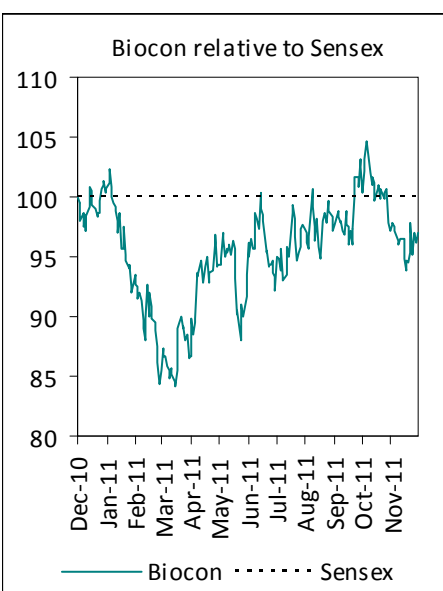
BSE Sensex	16,123
NSE Nifty	4,832

### Scrip Details

Equity	₹ 1000mn
Face Value	₹ 5/-
Market Cap	₹ 64bn
	USD 1251mn
52 week High / Low	₹ 430 / 299
Avg. Volume (no)	233,278
Bloomberg Code	BIOS IN
Reuters Code	BION.BO

### Shareholding Pattern as on Sept'11 (%)

Promoter	60.9
MF/Banks/FIs	10.9
FII's	4.8
Public / Others	23.4



### Key takeaways from the meeting

#### Biopharma Segment (82% of sales) – To sustain growth momentum.

- The management guides for a stable outlook in its statins business as Atorvastatin goes off patent while dependency on the statins business is anyways expected to decline over the years. It has signed up with four partners in EU and shall have two clients (currently one) in the US for Atorvastatin supplies.
- The company commenced Fidaxomicin bulk supplies in June 2011 to Optimer and this will aid topline growth in subsequent quarters. Optimer has revised its revenue forecast on 'DIFICID' upwards to USD 2bn — to be attained over three years. This augurs well for Biocon.
- The management has guided the branded formulations business to grow 35% YoY during FY12E (FY11: ₹ 1.8bn) and reach a revenue mark of ₹ 5bn over the next three years. Its diabetic portfolio currently generates half of the total domestic branded business revenues.
- Biocon launched 'Insupen' (reusable insulin pen device) in Q2, competitively priced at ₹ 675. Rivals' products are priced in the ₹ 450-1,350 range. Insupen is unique in being able to deliver both Basalog (glargine) and Insugen (insulin), thus maximising patient convenience. We expect it to aid growth.
- Updates on the Pfizer deal:
  - The aggregate cost of development for all four products (Rh insulin, glargine, aspart and lispro) is expected to be approx. USD 200mn which shall be met by upfront licensing income and other timely milestone payments.
  - The upcoming facility at Malaysia is not completely dedicated to meet Pfizer supply requirements. Its first phase (which entails a capital investment of USD 160mn) will commence in 2014E.
  - We anticipate significant value creation from this deal post launch of Insulin biosimilar portfolio in regulated markets which is yet time away – 2015-16E (post patent expiries). Its Recombinant Insulin is undergoing Ph-III trials in EU and it looks forward to initiate registration in US (under 505b (2) route).

### Financials (Consolidated)

Year	Net Sales	Growth-%	EBITDA	OPM-%	Adj. PAT	Growth-%	Adj.EPS (₹)	Growth-%	PER (X)	ROANW-%	ROACE-%
FY10	23,748	46.0	4,784	20.1	2,933	22.0	14.7	22.0	21.8	18.0	16.5
FY11	27,767	16.9	5,926	21.3	3,675	25.3	18.4	25.3	17.4	19.4	19.7
FY12E	21,095	(24.0)	5,907	28.0	3,601	(2.0)	18.0	(2.0)	17.7	16.7	17.8
FY13E	24,872	17.9	7,089	28.5	4,402	22.2	22.0	22.2	14.5	18.1	19.7

Figure in ₹ mn

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- The partnership with Mylan for co-development of five biologics is on-track. While entry into regulated markets is expected only by CY15-16E (post patent expirations), it would in the interim explore opportunities in emerging markets.

#### **Contract Research segment (18% of sales) – Gaining scale.**

The BMS contract (7 year contract), with 450 FTE's, contributes 30% of Syngene sales. Syngene is anticipated to record revenue growth of 20% YoY during FY12E. It has reported PAT of ₹ 240mn during H1FY12. The company intends to gain scale in this vertical and shall consequently work out the modalities of getting Syngene listed.

#### **R&D Pipeline: Progress Update**

- IN105 (Oral Insulin) Phase 1 trials are ongoing in US. The company is in active discussions with several potential partners for the global development and launch of the insulin. A deal is expected to be concluded by FY12E.
- Anti-CD6 antibody (T1h) has concluded Phase III trials for Psoriasis and is expected to be out-licensed next year.

#### **Valuation**

Fidaxomicin bulk and Atorvastatin supplies coupled with incremental revenues from the Pfizer deal ensure near-term revenue visibility. We expect the growth trajectory to sustain with gradual scale up in domestic formulations and ramp up in bulk supplies for products going off-patent. We anticipate higher R&D costs (as the product pipeline advances) to restrict margin expansion. Higher contribution from contract research and certainty over milestone payments further add to the growth momentum.

At CMP of ₹319, the stock trades at 17.7x FY12E and 14.5x FY13E earnings. We maintain **Buy** recommendation with target price of ₹ 421 (16x FY13E EPS and inclusive of NPV of ₹ 69 per share from Pfizer deal). This price target does not include any upside potential from the oral insulin molecule.

INCOME STATEMENT					CASH FLOW				
	₹ mn								
Particulars	Mar10	Mar11	Mar12E	Mar13E	Particulars	Mar10	Mar11	Mar12E	Mar13E
<b>Net Sales</b>	<b>23,748</b>	<b>27,767</b>	<b>21,095</b>	<b>24,872</b>	<b>Profit before tax</b>	<b>3,515</b>	<b>4,472</b>	<b>4,392</b>	<b>5,369</b>
Other income	301	370	350	350	Depreciation & w.o.	1,401	1,568	1,725	1,920
Total Income	24,048	28,137	21,445	25,222	Net Interest Exp	169	257	140	150
Total Expenditure	18,963	21,840	15,189	17,784	Direct taxes paid	(487)	(721)	(790)	(966)
<b>Operating Profit (excl. Other Income)</b>	<b>4,784</b>	<b>5,926</b>	<b>5,907</b>	<b>7,089</b>	Chg in Working Capital (Non Cash)	(291)	4,102	597	(2,476)
<b>Operating Profit (incl. Other Income)</b>	<b>5,085</b>	<b>6,296</b>	<b>6,257</b>	<b>7,439</b>	<b>(A) CF from Opt Activities</b>	<b>4,307</b>	<b>9,677</b>	<b>6,063</b>	<b>3,996</b>
Interest	169	257	140	150	Capex {Inc./ (Dec.) in FA n WIP}	(1,452)	(2,622)	(3,500)	(3,500)
<b>Gross Profit</b>	<b>4,916</b>	<b>6,039</b>	<b>6,117</b>	<b>7,289</b>	<b>Free Cash Flow</b>	<b>2,856</b>	<b>7,055</b>	<b>2,563</b>	<b>496</b>
Depreciation	1,401	1,568	1,725	1,920	(Inc)/ Dec. in Investments	(630)	(299)	(795)	0
Profit Before Tax & EO Items	3,515	4,472	4,392	5,369	Others (Bal Fig)	101	(700)	(287)	184
Extra Ordinary Exps/(Income)					<b>(B) CF from Investing Activities</b>	<b>(1,980)</b>	<b>(3,621)</b>	<b>(4,582)</b>	<b>(3,316)</b>
Profit Before Tax	3,515	4,472	4,392	5,369	Issue of Equity/ Preference	0	0	0	0
Tax	487	721	790	966	Inc./ (Dec.) in Debt	(103)	(1,794)	(453)	(89)
<b>Net Profit</b>	<b>3,028</b>	<b>3,751</b>	<b>3,601</b>	<b>4,402</b>	Interest exp net	(169)	(257)	(140)	(150)
Minority Interest	(96)	(75)	0	0	Dividend Paid (Incl. Tax)	(774)	(991)	(1,101)	(1,321)
<b>Net Profit After Minority Interest</b>	<b>2,933</b>	<b>3,675</b>	<b>3,601</b>	<b>4,402</b>	<b>(C) Cash Flow from Financing</b>	<b>(1,046)</b>	<b>(3,041)</b>	<b>(1,694)</b>	<b>(1,560)</b>
					Net Change in Cash	1,281	3,015	(213)	(880)
					<b>Opening Cash balances</b>	<b>118</b>	<b>1,399</b>	<b>4,414</b>	<b>4,201</b>
					<b>Closing Cash balances</b>	<b>1,399</b>	<b>4,414</b>	<b>4,201</b>	<b>3,320</b>
					E-estimates				
<b>BALANCE SHEET</b>					<b>IMPORTANT RATIOS</b>				
Particulars	Mar10	Mar11	Mar12E	Mar13E	Particulars	Mar10	Mar11	Mar12E	Mar13E
<b>Sources of Funds</b>					<b>(A) Measures of Performance (%)</b>				
Equity Capital	1,000	1,000	1,000	1,000	Operating Profit Margin (excl. O.I.)	20.1	21.3	28.0	28.5
Preference Capital	0	0	0	0	Operating Profit Margin (incl. O.I.)	21.4	22.7	29.7	29.9
Reserves (excl Rev Res)	16,569	19,318	21,809	24,881	Interest / Sales	0.7	0.9	0.7	0.6
Net Worth	17,569	20,318	22,809	25,881	Gross Profit Margin	20.7	21.8	29.0	29.3
Revaluation reserve	9	9	9	9	Tax/PBT	13.8	16.1	18.0	18.0
Minority Interest	338	377			Net Profit Margin	12.3	13.2	17.1	17.7
Secured Loans	3,315	2,039	1,539	1,500					
Unsecured Loans	1,821	1,303	1,350	1,300	<b>(B) Measures of Financial Status</b>				
Loan Funds	5,136	3,342	2,889	2,800	Debt / Equity (x)	0.3	0.2	0.1	0.1
Deferred Tax Liability	508	497	655	848	Interest Coverage (x)	30.1	24.5	44.7	49.6
<b>Total Capital Employed</b>	<b>23,561</b>	<b>24,544</b>	<b>26,362</b>	<b>29,539</b>	Average Cost Of Debt (%)	3.3	7.7	4.5	5.3
					Debtors Period (days)	69	67	85	90
<b>Applications of Funds</b>					Closing stock (days)	57	54	60	70
Gross Block	16,515	18,096	21,892	25,392	Inventory Turnover Ratio (x)	6.4	6.7	6.1	5.2
Less: Accumulated Depreciation	4,862	6,328	8,053	9,973	Fixed Assets Turnover (x)	2.0	2.4	1.5	1.6
<b>Net Block</b>	<b>11,653</b>	<b>11,769</b>	<b>13,839</b>	<b>15,419</b>	Working Capital Turnover (x)	4.6	6.9	6.5	5.2
Capital Work in Progress	755	1,796	1,500	1,500					
<b>Intangibles</b>	<b>1,726</b>	<b>2,342</b>	<b>2,400</b>	<b>2,400</b>	<b>(C) Measures of Investment</b>				
<b>Investments</b>	<b>4,306</b>	<b>4,605</b>	<b>5,400</b>	<b>5,400</b>	Earnings Per Share (₹) (excl EO)	14.7	18.4	18.0	22.0
Current Assets, Loans & Advances					Earnings Per Share (₹)	14.7	18.4	18.0	22.0
Inventories	3,716	4,137	3,468	4,770	Cash Earnings Per Share (₹)	21.7	26.2	26.6	31.6
Sundry Debtors	4,461	5,124	4,913	6,133	Dividend Per Share (₹)	3.5	4.5	5.0	6.0
Cash and Bank Balance	1,399	4,414	4,201	3,320	Dividend Payout (%)	23.9	24.5	27.8	27.3
Loans and Advances	1,344	1,355	1,755	2,255	Profit Ploughback (%)	76.1	75.5	72.2	72.7
Other Current Assets					Book Value (₹)	87.8	101.6	114.0	129.4
<i>sub total</i>	<i>10,921</i>	<i>15,030</i>	<i>14,336</i>	<i>16,478</i>	RoANW (%)	18.0	19.4	16.7	18.1
Less : Current Liabilities & Provisions					RoACE (%)	16.5	19.7	17.8	19.7
Current Liabilities	4,909	9,855	9,262	9,488	RonCE (%) (Excl Cash & Invest.)	20.6	30.5	27.0	26.5
Provisions	891	1,141	1,851	2,171					
<i>sub total</i>	<i>5,800</i>	<i>10,997</i>	<i>11,113</i>	<i>11,659</i>	<b>(D) Valuation Ratios</b>				
Net Current Assets	5,121	4,033	3,223	4,819	Market Price - Average (₹)	319	319	319	319
Misc Expenses	0	0	0	0	Price / Earnings Ratio - Average (x)	21.8	17.4	17.7	14.5
<b>Total Assets</b>	<b>23,561</b>	<b>24,544</b>	<b>26,362</b>	<b>29,539</b>	Average Market Cap. (₹ Cr.)	63,800	63,800	63,800	63,800
E-estimates					Market Capitalisation to Sales (x)	2.7	2.3	3.0	2.6
					Enterprise Value (₹ Cr.)	67,537	62,729	62,488	63,280
					EV/Sales (x)	2.8	2.3	3.0	2.5
					EV/EBDITA (x)	13.3	10.0	10.0	8.5
					Market Price to Book Value (x)	3.6	3.1	2.8	2.5
					Dividend Yield (%)	1.1	1.4	1.6	1.9
					E-estimates				

BUY	Upside above 20%
ACCUMULATE	Upside above 5% and up to 20%
REDUCE	Upside up to 5%
SELL	Negative Returns

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