

Orchid Chemicals

Performance Highlights

Y/E March (₹ cr)	4QFY2012	3QFY2012	%chg (qoq)	4QFY2011	%chg (yoy)
Net sales	485	482	0.6	528	(8.1)
Other income	44	15	197.6	63	(29.8)
Operating profit	45	111	(59.7)	49	(9.1)
Adjusted net profit	17	35	(49.8)	45	(61.1)

Source: Company, Angel Research

Orchid Chemicals (Orchid) reported lower-than-expected numbers for 4QFY2012. Going forward, for FY2013, management has guided for revenue growth of 15-20% and operating profit growth to be more than top-line growth. Although the stock has declined sharply post its 4QFY2012 results, given the valuations, **we maintain our Buy view on the stock.**

Lower-than-expected performance: For the quarter, on a consolidated level, Orchid reported net sales of ₹485cr, a decline of 8.1% yoy. The company's gross margin expanded by 638bp yoy to 52.5%; however, OPM remained flat at 9.2%, just in-line with 4QFY2011 OPM. The expansion in OPM came lower than the expansion in gross margin on account of lower growth in the top line. This along with higher interest expenditure led to net profit coming in lower than our expectation at ₹17cr vis-à-vis expectation of ₹36cr.

Outlook and valuation: We expect Orchid to post net sales of ₹2,434cr, with EBITDA margin of 17.7% in FY2014E. **The stock is currently trading at 7.6x FY2013E and 5.7x FY2014E earnings. We maintain our Buy rating on the stock with a revised target price of ₹178.**

Key financials (Consolidated)

Y/E March (₹ cr)	FY2011	FY2012E	FY2013E	FY2014E
Net sales	1,717	1,839	2,117	2,434
% chg	32.2	7.1	15.1	15.0
Recurring net profit	154	96	117	156
% chg	-	(38.0)	22.6	33.2
EBITDA margin (%)	20.5	16.3	17.7	17.7
Recurring EPS (₹)	22.2	13.6	16.7	22.2
P/E (x)	5.7	9.3	7.6	5.7
P/BV (x)	0.8	0.8	0.7	0.6
RoE (%)	15.2	8.5	9.5	11.5
RoCE (%)	7.4	4.8	6.8	7.9
EV/Sales (x)	1.5	1.2	1.1	0.9
EV/EBITDA (x)	7.2	7.6	6.1	5.0

Source: Company, Angel Research

BUY

CMP	₹126
Target Price	₹178

Investment Period	12 months
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Stock Info

Sector	Pharmaceutical
Market Cap (₹ cr)	886
Beta	1.4
52 Week High / Low	400 / 112
Avg. Daily Volume	1,031,256
Face Value (₹)	10
BSE Sensex	16,070
Nifty	4,870
Reuters Code	ORCD.BO
Bloomberg Code	OCP@IN

Shareholding Pattern (%)

Promoters	32.4
MF / Banks / Indian Fls	23.6
FII / NRIs / OCBs	18.5
Indian Public / Others	25.5

Abs.(%)	3m	1yr	3yr
Sensex	(12.1)	(11.4)	32.0
Orchid	(28.7)	(59.3)	25.4

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Exhibit 1: 4QFY2012 performance (Consolidated)

Y/E March (₹ cr)	4QFY2012	3QFY2012	%chg (qoq)	4QFY2011	%chg (yoy)	FY2012	FY2011	%chg (yoy)
Net Sales	485	482	0.6	528	(8.1)	1839	1717	7.1
Other Income	44	15	197.6	63	(29.8)	171	131	30.7
Total Income	529	497	6.5	590	(10.4)	2010	1847	8.8
Gross Profit	255	274	(6.8)	244	4.6	963	848	13.5
Gross Margin (%)	52.5	56.7		46.2		52.3	49.4	
Operating Profit	45	111	(59.7)	49	(9.1)	322	274	17.8
Operating Margin (%)	9.2	23.0	-	9.3	-	17.5	15.9	-
Interest	59	50	19.4	41	43.0	180	117	54.0
Depreciation & Amortization	42	38	10.0	36	17.5	154	134	15.2
PBT before Exceptional Items	(13)	38	-	35	-	159	154	-
Profit Before Tax	(2)	(46)	-	14	-	(84)	18	-
Provision for Taxation	(15)	(8)	89.2	48	-	75	172	(56.0)
Reported Net Profit	(30)	3		(10)	188.6	(22)	15	-
Exceptional Items (loss)/gain	15	(11)	-	59	(74.1)	97	156	(37.6)
Adjusted Net Profit	17	34.8	(49.8)	45	(61.1)	181	138	31.0
EPS (₹)	2.5	4.9		6.4		25.7	19.7	

Source: Company, Angel Research

Exhibit 2: Actual vs. estimates

(₹ cr)	Actual	Estimates	Variation (%)
Net sales	485	528	(8.1)
Other income	44	16	172.6
Operating profit	45	129	(65.4)
Tax	(30)	0	
Adjusted net profit	17	36	(51.7)

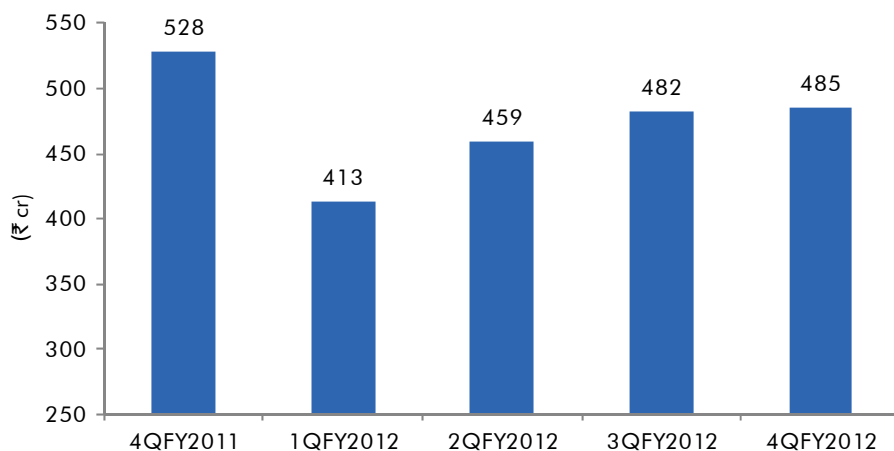
Source: Company, Angel Research

Below expectations revenue growth: For the quarter, on a consolidated level, Orchid reported net sales of ₹485cr, registering a decline of 8.1% yoy. Sales mainly declined on account of lower sales to Hospira, which contributes significantly to the overall top line of the company.

Going forward, for FY2013, the company has slated revenue guidance of ~₹2,000cr, 15.0% yoy growth. The company expects OPM of over ~20%. The key growth factor driving the same would be addition of new contracts by Hospira and other MNCs. While the Hospira contract is expected to grow at 10-15% during the contract, new API supplies from Hospira, for one of its products, are expected to contribute around US\$25mn in FY2013; the supplies for the same are expected to start from 2QFY2013. Apart from these, the company is expected to start API supplies for its new product for one of its MNC clients, which is expected to reflect from 3QFY2013 and 4QFY2013.

Overall, in FY2012, the company's sales mix was 75:25 of API:Formulation. Going forward, on the back of contract manufacturing activities, the company expects the ratio to be 50:50 in the next two years.

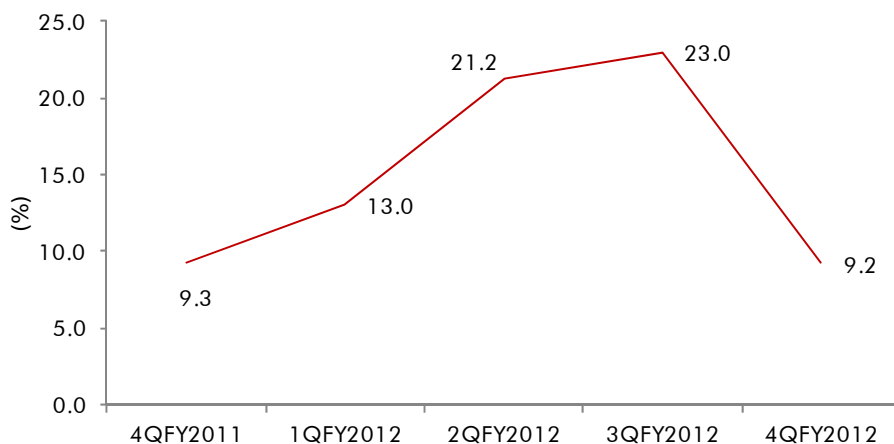
Exhibit 3: Sales trend



Source: Company, Angel Research

OPM stagnant despite gross margin expansion: The company's gross margin expanded by 638bp yoy to 52.5%; however, OPM remained flat at 9.2%, just in-line with 4QFY2011 OPM. The expansion in OPM came lower than the expansion in gross margin on account of lower top-line growth. Going into FY2013, top-line growth is expected to aid the company to report OPM of 23-24%.

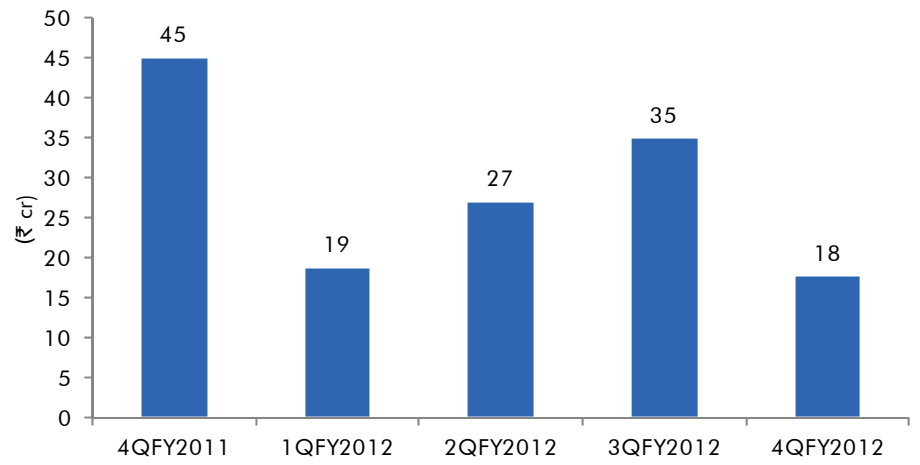
Exhibit 4: OPM trend (%)



Source: Company, Angel Research

Consequently, net profit came in lower than expectations: This along with higher interest expenditure led the net profit to come in lower than expected at ₹17cr vis-à-vis expectations of ₹36cr.

Exhibit 5: Adjusted net profit trend



Source: Company, Angel Research

Management takeaways

- For FY2013, management has guided towards revenue growth of 15% and EBITDA margin in excess of 20%.
- Tax rate is expected to be 20% of PBT in FY2013.
- API:Formulation mix to improve to 50:50 in the next two years.
- Targeted 1.1x Debt:Equity for FY2013.
- Plan to convert the rupee loan of ₹600cr into dollar to bring down its effective cost of funds to 5-6% in FY2013.
- Capex of around ₹200cr (including the maintenance capex) in FY2013.

Recommendation rationale

Supply agreements to drive growth: Growth for Orchid would be majorly led by its supply agreements with various players, with Hospira being the key contributor. In FY2010, Hospira took over the injectable business from Orchid. Subsequently, Orchid has entered into a 10-year exclusive agreement, wherein it would supply the API for the acquired generic injectable pharmaceuticals business to Hospira. Hospira contributed around 25% to total sales (FY2012), with the majority accruing through limited competition for products such as penems.

Besides Hospira, Orchid has entered into various supply agreements with other players in the regulated as well as non-regulated markets. The company has started supplying API to a leading Japanese company under a contract for the next five years. Orchid has also entered into an agreement with another company for the supply of API (Carbopenem). Apart from these, the company is expected to start supplies of API for a new product for one of its MNC clients, which is expected to reflect from 3QFY2013 and 4QFY2013.

These supply agreements are expected to boost the company's overall growth. We expect net sales to increase by 15.0% to ₹2,434cr in FY2014. While the contribution of API:Formulation has been around 75:25 in FY2012, management expects the contribution to be 50:50 by FY2015E.

Balance sheet in a healthy shape: Orchid faced debt pressure with interest cost rising to ₹242cr and losses on the operating front in FY2010. Repayment of debt through the proceeds received from Hospira led to net debt/equity dropping from 4.7x FY2009 to almost 1.5x in FY2012. Going forward, the company expects the company to further de-leverage its balance sheet and reduce its debt levels, making its debt/equity comfortable at 1.1x FY2013. The shift to a more sustainable and robust business model has helped the company significantly de-leverage its balance sheet with receivables reducing to 132 days (~180 days in FY2010) and inventory days reducing to 132 days (162 days in FY2010).

Outlook and valuation

Going forward, for FY2013, management has guided revenue growth of 15-20% and operating profit growth to be higher than top-line growth. We expect Orchid to post net sales of ₹2,434cr with EBITDA margin of 17.7% in FY2014E. **The stock is currently trading at 7.6x FY2013E and 5.7x FY2014E earnings. We maintain our Buy rating on the stock with a revised target price of ₹178.**

Exhibit 6: key assumptions

(₹ cr)	FY2013E	FY2014E
Net sales growth (%)	15.1	15.0
Operating margins (%)	17.7	17.7
Net profit growth (%)	22.6	33.2
Capex (₹ cr)	200	150

Source: Company, Angel Research

Exhibit 7: One-year forward EV/Sales



Source: Company, Angel Research

Exhibit 8: Recommendation summary

Company	Reco	CMP (₹)	Tgt. price (₹)	Upside %	PE (x)	FY2014E		FY12-14E	FY2014E	
						EV/Sales (x)	EV/EBITDA (x)	CAGR in EPS (%)	RoCE (%)	RoE (%)
Alembic Pharmaceuticals	Buy	50	91	82.0	5.5	0.7	4.7	14.6	29.4	29.2
Aurobindo Pharma	Buy	106	175	65.0	6.1	0.8	5.5	4.8	10.1	14.0
Aventis*	Reduce	2,148	1,937	(9.8)	20.6	2.7	17.2	12.0	16.1	17.0
Cadila Healthcare	Buy	789	953	20.7	16.5	2.1	10.9	22.3	23.0	27.5
Cipla	Buy	313	379	21.0	16.5	2.9	13.5	13.5	15.2	16.8
Dr Reddy's	Accumulate	1,662	1,859	11.9	17.3	3.0	11.9	22.5	22.2	25.3
Dishman Pharma	Buy	46	92	100.0	3.8	0.8	4.4	26.6	8.7	8.8
GSK Pharma*	Neutral	2,068	-	-	25.2	5.1	16.4	8.7	38.9	29.0
Indoco Remedies	Buy	58	89	53.4	6.6	0.9	5.8	25.1	13.8	16.9
Ipca labs	Buy	348	443	27.3	8.6	1.3	6.2	25.2	27.3	27.7
Lupin	Buy	544	646	18.8	16.8	2.1	10.8	29.1	28.0	25.2
Orchid Chemicals	Buy	126	178	41.3	5.7	0.9	5.0	27.8	11.5	7.9
Ranbaxy*	Neutral	488	-	-	16.4	1.6	10.4	44.8	15.6	28.1
Sun Pharma	Accumulate	580	635	9.4	20.9	6.0	13.2	8.3	24.0	20.8

Source: Company, Angel Research; Note: *December year ending; #Based on CY2012 estimates

Profit & loss statement (Consolidated)

Y/E March (₹ cr)	FY2009	FY2010	FY2011	FY2012E	FY2013E	FY2014E
Gross sales	1,273	1,312	1,731	1,857	2,136	2,456
Less: Excise duty	13	13	14	18	19	19
Net sales	1,260	1,299	1,717	1,839	2,117	2,434
Other operating income	33	44	69	63	81	81
Total operating income	1,293	1,342	1,786	1,902	2,198	2,515
% chg	(0.4)	3.8	33.0	6.5	15.5	14.4
Total expenditure	1,110	1,500	1,366	1,539	1,742	2,003
Net raw materials	586	840	869	876	847	974
Other mfg costs	149	116	155	214	251	288
Personnel	137	174	165	176	251	288
Other	238	370	332	272	394	453
EBITDA	150	(202)	351	300	375	431
% chg	(48.8)	(234.7)	(274.2)	(14.7)	25.0	15.0
(% of Net Sales)	11.9	(15.5)	20.5	16.3	17.7	17.7
Depreciation & amortisation	134	155	134	154	167	174
EBIT	16	(356)	218	146	208	256
% chg	(91.8)	(2,373.1)	(161.1)	(33.0)	42.3	23.4
(% of Net Sales)	1.2	(27.4)	12.7	7.9	9.8	10.5
Interest & other charges	156	242	117	180	156	156
Other Income	90	10	0	108	14	14
(% of PBT)	-	-	0.0	146.0	9.4	7.1
Share in profit of associates	-	-	-	-	-	-
Recurring PBT	(18)	(546)	170	74	147	195
% chg	-	-	-	(56.6)	99.1	33.2
Extraordinary expense/(Inc.)	15.9	(1,015.3)	1.9	-	-	-
PBT (reported)	(34)	470	172	74	147	195
Tax	15.2	130.6	15.4	(22.0)	29.3	39.1
(% of PBT)	0.0	27.8	9.0	(29.9)	20.0	20.0
PAT (reported)	(49)	339	156	96	117	156
PAT after MI (reported)	(49)	339	156	96	117	156
ADJ. PAT	(33)	(554)	154	96	117	156
% chg	-	-	-	(38.0)	22.6	33.2
(% of Net Sales)	-	-	9.1%	5.2%	5.5%	6.4%
Basic EPS (₹)	-	48.2	22.2	13.6	16.7	22.2
Adj Fully Diluted EPS (₹)	-	-	22.2	13.6	16.7	22.2
% chg	-	-	-	(38.7)	22.6	33.2

Balance sheet (Consolidated)

Y/E March (₹ cr)	FY2009	FY2010	FY2011	FY2012E	FY2013E	FY2014E
SOURCES OF FUNDS						
Equity share capital	70	70	70	70	70	70
Reserves & surplus	480	885	999	1,110	1,213	1,356
Shareholders' funds	550	955	1,069	1,181	1,284	1,426
Minority interest	-	-	2	3	3	3
Total loans	2,616	1,644	1,856	1,556	1,721	1,721
Deferred tax liability	128	203	194	170	170	170
Total liabilities	3,295	2,802	3,120	2,910	3,178	3,320
APPLICATION OF FUNDS						
Gross block	2,601	2,250	2,526	3,138	3,338	3,488
Less: acc. depreciation	688	741	872	1,026	1,192	1,367
Net block	1,913	1,508	1,654	2,113	2,146	2,121
Capital work-in-progress	547	469	602	215	215	215
Goodwill	95	95	99	99	99	99
Investments	1	1	1	1	1	1
Current assets	1,595	1,700	1,716	1,340	1,704	2,018
Cash	53	335	222	179	349	461
Loans & advances	102	206	362	380	444	511
Other	1,441	1,160	1,131	782	910	1,047
Current liabilities	856	972	950	858	986	1,134
Net current assets	740	729	766	483	718	884
Mis. Exp. not written off	-	-	-	-	-	-
Total Assets	3,295	2,802	3,120	2,910	3,178	3,320

Cash flow statement (Consolidated)

Y/E March (₹ cr)	FY2009	FY2010	FY2011	FY2012E	FY2013E	FY2014E
Profit before tax	(34)	470	172	74	147	195
Depreciation	134	155	134	154	167	174
(Inc)/Dec in Working Capital	(129)	294	(150)	239	(64)	(55)
Less: Other income						
Direct taxes paid	(3)	(66)	(31)	22	(29)	(39)
Cash Flow from Operations	(31)	852	124	489	220	275
(Inc.)/Dec.in Fixed Assets	(524)	429	(408)	(226)	(200)	(150)
(Inc.)/Dec. in Investments	-	-	-	-	-	-
Other income						
Cash Flow from Investing	(524)	429	(408)	(226)	(200)	(150)
Issue of Equity	110	-	-	-	-	-
Inc./(Dec.) in loans	546	(780)	212	(299)	165	-
Dividend Paid (Incl. Tax)	(23)	(8)	(14)	(14)	(14)	(14)
Others	(56)	(211)	(27)	7	-	-
Cash Flow from Financing	577	(998)	171	(307)	151	(14)
Inc./(Dec.) in Cash	21	283	(113)	(44)	171	111
Opening Cash balances	31	53	335	222	179	349
Closing Cash balances	53	335	222	179	349	461

Key ratios

Y/E March	FY2009	FY2010	FY2011	FY2012E	FY2013E	FY2014E
Valuation Ratio (x)						
P/E (on FDEPS)	-	-	5.7	9.3	7.6	5.7
P/CEPS	8.8	-	3.1	3.6	3.1	2.7
P/BV	1.6	0.9	0.8	0.8	0.7	0.6
Dividend yield (%)	1.0	10.0	1.4	1.4	1.4	1.4
EV/Sales	2.7	1.7	1.5	1.2	1.1	0.9
EV/EBITDA	23.1	(10.9)	7.2	7.6	6.0	5.0
EV / Total Assets	1.0	0.8	0.8	0.8	0.7	0.6
Per Share Data (₹)						
EPS (Basic)	-	48.2	22.2	13.6	16.7	22.2
EPS (fully diluted)	-	-	22.2	13.6	16.7	22.2
Cash EPS	14.3	-	40.8	35.4	40.3	46.9
DPS	1.3	12.6	1.7	1.7	1.7	1.7
Book Value	78.1	135.6	151.8	167.6	182.2	202.4
Dupont Analysis						
EBIT margin	1.2	-	12.7	7.9	9.8	10.5
Tax retention ratio	-	-	91.0	129.9	80.0	80.0
Asset turnover (x)	0.4	-	0.7	0.7	0.8	0.9
ROIC (Post-tax)	-	-	7.7	7.0	6.2	7.5
Cost of Debt (Post Tax)	-	-	6.1	13.7	7.6	7.2
Leverage (x)	3.8	-	1.4	1.3	1.1	1.0
Operating ROE	-	-	10.0	(2.1)	4.6	7.7
Returns (%)						
RoCE (Pre-tax)	0.5	-	7.4	4.8	6.8	7.9
Angel RoIC (Pre-tax)	0.7	-	10.6	6.3	8.4	10.1
RoE	-	-	15.2	8.5	9.5	11.5
Turnover ratios (x)						
Asset Turnover (Gross Block)	0.6	0.6	0.7	0.7	0.7	0.7
Inventory / Sales (days)	200	162	106	128	142	146
Receivables (days)	171	179	128	132	144	149
Payables (days)	109	83	98	105	107	107
WC cycle (ex-cash) (days)	176	147	96	81	56	57
Solvency ratios (x)						
Net debt to equity	4.7	1.4	1.5	1.2	1.1	0.9
Net debt to EBITDA	17.1	(6.5)	4.6	4.6	3.7	2.9
Interest Coverage (EBIT / Int.)	0.1	(1.5)	1.9	0.8	1.3	1.6

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Disclosure of Interest Statement	Orchid Chemicals
1. Analyst ownership of the stock	No
2. Angel and its Group companies ownership of the stock	No
3. Angel and its Group companies' Directors ownership of the stock	No
4. Broking relationship with company covered	No

Note: We have not considered any Exposure below ₹ 1 lakh for Angel, its Group companies and Directors.

Ratings (Returns):	Buy (> 15%)	Accumulate (5% to 15%)	Neutral (-5 to 5%)
	Reduce (-5% to 15%)	Sell (< -15%)	