

Indoco Remedies (INDREM)

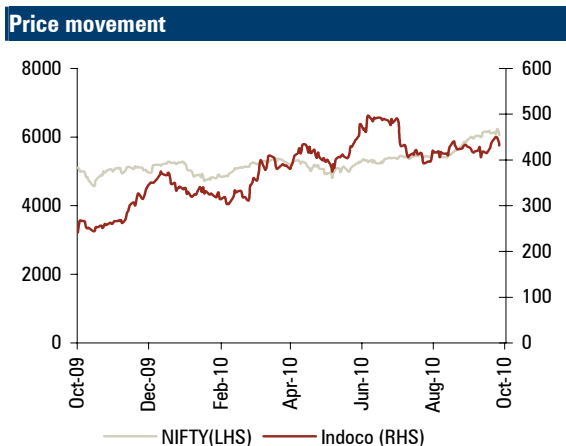
Rs 490

Rating matrix	
Rating	: Buy
Target	: Rs 546
Target Period	: 12 months
Potential Upside	: 11%

Key Financials (in Rs crore)				
(Rs Crore)	FY09	FY10	FY11E	FY12E
Net Sales	350.6	398.3	490.3	565.8
EBITDA	46.2	53.2	78.1	103.3
Net Profit	31.4	42.1	55.6	67.1

Valuation summary				
	FY09	FY10	FY11E	FY12E
EPS (Rs)	25.6	34.4	45.3	54.6
PE (x)	19.1	14.2	10.8	9.0
Target PE (x)	21.4	15.9	12.1	10.0
EV to EBITDA (x)	13.6	11.8	8.4	6.0
Price to book (x)	2.2	1.9	1.7	1.5
RoNW (%)	11.3	13.6	15.6	16.2
RoCE (%)	10.9	11.5	13.6	16.9

Stock data	
Market Capitalisation	Rs 602 crore
Debt (FY10)	Rs 66.0 crore
Cash (FY10)	Rs 37.9 crore
EV	Rs 630.3 crore
52 week H/L	523/240
Equity capital	Rs 12.3 crore
Face value	Rs 10.0
MF Holding (%)	10.0
FII Holding (%)	3.3



Analyst's name	
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WHAT'S CHANGED...

PRICE TARGET	Changed from Rs 432 to Rs 546
EPS (FY11E)	Changed from Rs 43.3 to Rs 45.3
EPS (FY12E)	Changed from Rs 49.1 to Rs 54.6
RATING.....	Buy

Strong Show...

Indoco Remedies' (IRL) Q2 FY11 results were above our expectations. The net sales increased by ~39% YoY to Rs 132.3 crore (we estimated Rs 114 crore) on the back of strong growth registered by all business segments. EBITDA margins grew by 200 bps on YoY basis due to fall in the other expenditure as a percentage to sales by 160 bps. EBITDA increased ~ 59% to Rs 20.8 crore. Thanks to dip in the interest cost by ~20% the net profit grew by ~ 65% to Rs 15.3 crore. With the key divisions Indoco and Spade coming back to growth track, we have revised our target price upwards to Rs 546 with Buy rating.

■ Highlights for the quarter

The domestic formulation business rose ~ 37% on YoY to 88.4 crore and international formulations increased by ~35% to Rs 35.3 crore. Indoco launched 7 new products in the domestic market. The key divisions Indoco and Spade witnessed a growth of 17% and 50% respectively on a YoY basis. It has filed two ANDAs with the USFDA. Under the supply agreement with Watson, it has agreed to develop 4 more products taking to total number of products under deal for development to 12. Overall exports grew by ~30% on account of robust growth registered both in regulated as well as semi-regulated markets.

Valuation

We have adjusted our forward multiple from 8-9x to 10x on account of strong showing in Q2FY11 and fair visibility based upon management guidance. We believe the strong showing will sustain going forward on account of conscious re-strategising of the product focus and selection of the geographies. Although there remains a sizable delta between Indoco and other companies which are strong in more than one geography like Lupin, Cadila or Torrent, we believe the company is on the right track to follow these players. We expect the margins concern to recede further once the newly added sales force completes the learning curve. We have arrived at a price target of Rs 546, based upon 10x FY12E EPS of Rs 54.6. We recommend Buy for 11% upside from the current level.

Exhibit 1: Financial Performance

(Rs Crore)	Q2FY11A	Q2FY11E	Q2FY10	Q1FY11	YoY Gr.(%)	QoQ Gr.(%)
Net Sales	132.3	113.6	95.4	111.4	38.7	18.8
EBITDA *	20.8	16.9	13.1	19.1	59.3	9.2
EBITDA Margin (%)	15.7	14.9	13.7	17.1	14.8	-8.1
Depreciation	3.4	3.5	2.9	3.2	15.5	4.4
Interest	0.5	0.6	0.7	0.7	-19.7	-18.5
Reported PAT	15.3	12.3	9.3	14.8	65.0	3.0
EPS (Rs)	12.4	10.0	7.5	12.1		

Source: Company, ICICIdirect.com Research

■ Sales grew by 39%

The net sales grew by ~39% on YoY basis to Rs 132 crore as against our estimate of Rs 114 crore. The growth was driven by all the therapeutic segments except Diabetic and Cardiac. The domestic formulation business increased by ~ 37% to Rs 88.4 crore on the back of 17% and 50% growth registered by its flagship divisions Indoco and Spade respectively. Sales from these two segments were impacted in Q1 FY11 due to change in strategy which did not work. So this time around the company again adopted the old strategy with some modification and it has given the best results. Sales from international formulation business rose by ~35% on the back of ~140% rise in the sales from the Semi-regulated markets. Sales from Metformin tender (Anti-Diabetic) in South Africa stood at Rs 4.62 crore and Paracetamol tender in New Zealand stood at Rs 2.06 crore. Sales from domestic APIs jumped by ~ 85% to 3.6 crore and export APIs by ~70% to Rs 5.1 crore.

The growth in Indoco and Spade division drives the growth in domestic formulation revenues

Exhibit 2: Revenue break-up

(Rs Crore)	Q2FY11	Q2FY10	YoY %	Q1FY11	QoQ %
Domestic	92.0	66.4	38.6	75.5	21.8
% to Net Sales	69.5	69.6		1489.9	
Formulations	88.4	64.5	37.2	72.6	21.9
% to Net Sales	66.8	67.6		1431.6	
API	3.6	1.9	85.4	3.0	20.3
% to Net Sales	2.7	2.0		58.4	
Exports	40.3	29.0	39.0	35.8	12.6
% to Net Sales	30.5	30.4		706.9	
Formulations	35.3	26.0	35.4	32.8	7.4
% to Net Sales	26.7	27.3		647.5	
Regulated market	27.1	22.7	19.7	25.0	8.3
% to Net Sales	20.5	23.7		493.7	
Semi-reg market	8.2	3.4	140.4	7.8	4.5
% to Net Sales	6.2	3.6		153.8	
API	5.1	3.0	69.6	3.0	68.4
% to Net Sales	3.8	3.1		59.4	
Net Sales	132.3	95.4	38.7	111.4	18.8

Source: Company, ICICIdirect.com Research

Exhibit 3: Therapeutic Segment Performance (Rs crore)

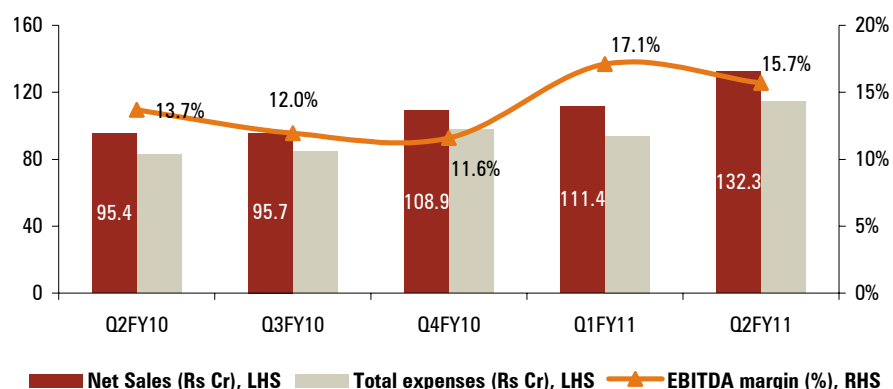
Therapeutic Segment	Q2FY11	Q2FY10	Gr. (%)
Respiratory	21.29	13.9	53.2
Anti-Infective	18.28	13.72	33.2
Gastro-Intestinal	12.44	8.75	42.2
Stomatologicals	11.78	9.16	28.6
Pain/Analgesics	5.13	3.39	51.3
Ophthal/Otologicals	4.62	3.03	52.5
Gynaec	4.21	3.8	10.8
Dermatology	4.27	3.31	29.0
Diabetic & Cardiac	3.96	3.8	4.2
Vitamins	2.65	1.76	50.6
Anti-Malarials	0.55	0.32	71.9

Source: Company, ICICIdirect.com Research

■ EBITDA up 200 bps

EBITDA margins expanded by 200 bps YoY on account of decline in the other expenditure. The margins would have been better but for increase in the raw material cost by ~310 bps and lower realization in exports on account of appreciation of rupee vis-à-vis major currencies. EBITDA increased by ~59% to Rs 20.83 crore.

Exhibit 4: EBITDA margin trend



Source: Company, ICICIdirect.com Research

■ Net profit grew by 65% YoY

The net profit rose by 65% YoY to Rs 15.26 crore (above our expectations Rs 12 crore). Increase in sales coupled with expansion in margins drove the growth in net profits. The interest cost declined further on account better working capital fund management.

Exhibit 5: Common size P&L statement

	Q2FY10	Q3FY10	Q4FY10	Q1FY11	Q2FY11
Net Sales	100	100	100	100	100
Other Operating Income	0.8	0.3	1.5	1.3	2.34
EBITDA	13.0	11.7	10.1	17.1	15.7
Depreciation	3.0	3.2	3.0	2.9	2.5
Interest	0.7	0.6	0.6	0.7	0.4
PBT	10.0	8.2	8.0	13.6	12.8
Tax	0.4	0.1	0.3	0.4	1.3
PAT	9.7	8.1	7.7	13.4	11.5

Source: Company, ICICIdirect.com Research

Other Key Developments

- Company expects Capex of Rs 80 crore for the current fiscal and Rs 50 crore for next fiscal.
- It is setting up formulation manufacturing facility at Goa with Capex of Rs 48 crore. The facility is expected to commence by February 2011.
- During the quarter, the company has expanded supply agreement with Watson by 4 more products taking total products under the agreement to 12.
- It has filed two ANDAs with US FDA during the quarter.
- It has launched 7 products in domestic market.
- The receivable hedging position as on 31st September 2010 are USD 5.6 million @ 46.88 per dollar and Euro 2.5 million @ 62.50 per Euro. This accounts for almost 55% of the likely exports for FY11.

Valuation

We expect IRL's formulations sales to grow at a CAGR 18.4% during FY10-12E. The two key segments Indoco and spade will be driving the growth in domestic formulation business while supply deal with Aspen will bring growth in export formulation business. Overall, we expect sales to grow at a CAGR 19.2% during FY10-12E and net profit to grow at 26%. On the EBITDA margins front the management has guided for at least 150-200 bps improvement from its historical range of 14-15%. The tax outgo however will go up in the next fiscal from 8-9% to almost 20% in FY12 putting some pressure on the bottomline.

The scrip is currently trading at 9x of FY12E EPS of Rs 54.6. We have upgraded the multiple to 10 on account of greater visibility in the domestic formulations business and division rationalisation. On the exports front the deals with Aspen and Watson (from FY13 onwards) have given the company a new identity. On the other hand low EBITDA margins, negligible presence in branded formulations and low return ratios will still act as deterrence for higher multiple. Our fair value for the company is Rs 546, based on 10x FY12E EPS of Rs 54.6.

Exhibit 6: Valuation Matrix

	Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
FY09	350.6	25.6	19.1	13.6	11.3	10.9
FY10E	398.3	34.4	14.2	11.8	13.6	11.5
FY11E	490.3	45.3	10.8	8.4	15.6	13.6
FY12E	565.8	54.6	9.0	6.0	16.2	16.9

Source: Company, ICICIdirect.com Research

ICICIdirect.com coverage universe (Pharma)

Alembic					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	ALECHE	CMP	46	FY08	1003.2	8.0	5.7	7.1	32.6	19.1
		Target	46	FY09	1116.1	3.4	14.6	8.7	14.0*	11.3
MCap	634.8	Upside (%)	1	FY10E	1141.7	3.6	12.8	7.3	8.1	8.8
				FY11E	1222.9	4.6	9.9	5.6	12.2	11.4
Biocon					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	BIOCON	CMP	321	FY09	1608.7	12.0	18.2	19.8	11.4	13.2
		Target	335	FY10E	2367.8	14.7	21.9	13.3	12.4	15.6
MCap	6420.0	Upside (%)	4	FY11E	2701.9	17.1	18.7	12.2	13.2	16.7
				FY12E	3085.7	20.2	15.9	10.3	13.9	17.5
Dishman					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	DISHPHA	CMP	206	FY09	1062.4	18.2	11.3	8.9	20.9	13.6
		Target	189	FY10	915.4	14.6	14.1	11.6	15.0	9.1
MCap	1662.4	Upside (%)	-8	FY11E	969.3	16.0	12.9	10.6	14.4	8.9
				FY12E	1102.1	17.2	12.0	9.2	14.0	9.7
IPCA Labs					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	IPCLAB	CMP	280	FY09	1283.8	8.1	34.7	15.4	16.0	19.6
		Target	302	FY10	1559.6	16.4	17.0	12.2	23.7	20.5
MCap	3500.0	Upside (%)	8	FY11E	1812.5	17.7	15.8	10.7	21.1	20.9
				FY12E	2165.9	23.2	12.1	8.3	22.3	23.9
Piramal Health					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	NICPIR	CMP	480	FY09	3281.1	15.1	31.7	19.4	24.0	17.7
		Target	526	FY10E	3671.1	23.1	20.8	15.2	28.3	18.8
MCap	10032.0	Upside (%)	10	FY11E	4019.5	23.9	20.1	14.0	24.4	19.6
				FY12E	4542.8	29.8	16.1	11.4	25.2	22.5
Sun Pharma					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	SUNPHA	CMP	1947	FY09	4271.4	88.1	22.1	20.8	25.9	28.5
		Target	1805	FY10	4019.8	65.2	29.8	28.3	17.8	19.6
MCap	40325.8	Upside (%)	-7	FY11E	4906.5	83.9	23.2	20.9	19.2	21.2
				FY12E	5324.2	86.9	22.4	19.6	17.1	19.1
Glenmark					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	GLEPHA	CMP	285	FY09	2093.0	7.7	35.5	20.6	19.4	16.4
		Target	325	FY10	2484.9	12.2	22.3	14.6	13.9	14.6
MCap	7678.2	Upside (%)	14	FY11E	2876.5	15.4	18.6	12.1	18.0	17.2
				FY12E	3345.2	20.7	13.8	9.7	20.3	19.7
Lupin					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	LUPIN	CMP	1951	FY08	2706.4	49.8	39.2	38.9	31.9	22.2
		Target	2101	FY09	3775.9	61.3	31.8	26.7	35.6	23.6
MCap	17350.4	Upside (%)	8	FY10E	4740.5	78.7	24.8	21.4	27.3	22.4
				FY11E	5883.6	94.6	20.6	16.2	27.5	25.7
				FY12E	6943.2	117.0	16.7	13.1	24.9	23.8
Unichem Labs					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	UNILAB	CMP	217	FY09	735.2	12.0	18.1	13.8	22.3	23.2
		Target	242	FY10E	765.5	14.7	14.7	10.6	23.3	25.7
MCap	1956.0	Upside (%)	12	FY11E	851.4	14.7	14.8	9.5	19.5	22.9
				FY12E	1001.6	18.6	11.7	7.5	20.9	24.6
Indoco Remedies					Sales (Rs Cr)	EPS (Rs)	PE(x)	EV/E (x)	RoNW (%)	RoCE (%)
Idirect Code	INDREM	CMP	490	FY09	350.6	25.6	19.1	13.6	11.3	10.9
		Target	546	FY10E	398.3	34.4	14.2	11.8	13.6	11.5
MCap	602.2	Upside (%)	11	FY11E	490.3	45.3	10.8	8.4	15.6	13.6
				FY12E	565.8	54.6	9.0	6.0	16.2	16.9

RATING RATIONALE

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 Add: Up to 10%;
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