

Sector: Pharmaceuticals  
Result Update

	Change
Reco: <b>Buy</b>	↔
CMP: <b>Rs. 1,069</b>	
Price Target: <b>Rs. 1,220</b>	↑

↑ Upgrade   ↔ No change   ↓ Downgrade

## Company details

Market cap:	Rs. 13,509 cr
52-week high/low:	Rs. 1,103/681
NSE volume: (No of shares)	1.7 lakh
BSE code:	524494
NSE code:	IPCALAB
Sharekhan code:	IPCALAB
Free float: (No of shares)	6.8 cr

## Shareholding (%)

Promoters	46.1
FII	16.9
DII	24.1
Others	13.0

## Price chart



## Price performance

(%)	1m	3m	6m	12m
Absolute	21.5	14.2	11.6	55.2
Relative to Sensex	12.0	2.9	4.1	33.0

Sharekhan Research, Bloomberg

Ipca Laboratories Limited (Ipca) reported impressive results for Q2FY2020. Numbers were ahead of estimates. Aided by a strong double-digit growth across the formulations and API business, topline was up 29% y-o-y to Rs 1284 crore. On the back of improved product mix and favorable raw material prices, operating profit jumped 52.5% y-o-y to Rs 263.5 cr while the adjusted PAT rose 62% y-o-y to Rs 193.5 cr. Expected traction across the formulation and API business, improved product mix and a substantial drop in the remedial cost are expected to be the key earnings drivers. We Expect Ipca's sales and profits to grow at a CAGR of 19% and 32% over FY2019-FY2021. Further a successful inspection outcome from the USFDA would be a key trigger for earnings upgrades.

## Key positives

- ◆ Sturdy double digit growth across all verticals
- ◆ OPM's expanded sharply by 320 bps to 20.5% attributable to better product mix.
- ◆ Operating profit and adjusted PAT grow impressively by 52.5% and 62% y-o-y respectively.
- ◆ Remediation costs have reduced and the management expects no major remedial cost to come up.

## Key negatives

- ◆ Global Fund business offtake delayed; Anti-malarial drug prices softening.

## Our Call

**Valuation – Maintain Buy with revised PT of Rs. 1,220:** IPCA is on a strong footing and is well placed to capitalize on the growth opportunities across the domestic and exports markets. Performance across the Formulation and API segment is expected to improve as most headwinds that impacted the performance are behind. Management has maintained its sales and profitability guidance. However, given the robust performance in Q2FY2020, we have revised our earnings estimates upwards for FY2020 / FY2021. We expect the company to report sales/profit CAGR of 19%/32% over FY2019-FY2021. At CMP the stock is trading at an attractive P/E multiple of 17.6x its FY2021 earnings. We maintain our Buy recommendation on the stock with a revised PT of Rs. 1,220. Successful resolution of the USFDA regulatory issues could provide further upside with the potential for upgrade of earnings estimates.

## Key Risks

- ◆ A lack/delay of clearance by other drug regulators would impact the export business outlook
- ◆ Addition of drugs in NLEM list could hurt the domestic business; and
- ◆ Weakness in emerging market currencies could affect the growth prospects.

## Valuation (Consolidated)

Particulars	Rs cr			
	FY2018	FY2019	FY2020E	FY2021E
Net sales	3,283.6	3,773.2	4,522.9	5,380.9
OPM (%)	13.8	18.3	20.8	22.4
PAT	239.4	442.2	645.7	768.1
EPS (Rs)	19.0	35.1	51.2	60.9
PER (x)	56.3	30.5	20.9	17.6
EV/Ebitda (x)	30.9	19.9	14.8	11.5
RoCE (%)	9.1	15.4	19.9	23.0
RoNW (%)	9.5	15.3	18.8	18.5

Source: Company; Sharekhan estimates

**Impressive results; PAT beat estimates:** Ipca reported an impressive set of numbers for Q2FY20. Numbers were ahead of estimates. Sales for the quarter grew by 29% y-o-y to Rs 1284 crore. A strong double-digit growth across the formulations and a sturdy growth in the API business aided the robust topline growth. Operating profit was up remarkably by 52.5% y-o-y to Rs 263.5 crores. Operating margins improved 320 bps y-o-y to 20.5%. A favorable product mix (higher share of formulations business) drove margin expansion. Adjusted PAT at Rs 193.5 crore grew strongly by 62% y-o-y, comfortably beating our estimates of Rs 157.7 cr. The forex loss stood at Rs 2.33 crore as against Rs 30.33 cr loss in the corresponding quarter of the previous year.

**Strong growth outlook:** A Strong growth in domestic formulation business coupled with increased opportunities in the API space and additional business from institutional anti-malaria segment indicates strong growth potential over the next 2-3 years. In the formulations business the management expects to comfortably outpace the market growth by clocking a 1.5x growth rate. In the API space, alternative sourcing opportunities (as most of the companies look to India as alternative sourcing destination to China) is expected to be a key growth driver. For FY2020, the management has maintained its conservative guidance for ~20% sales growth and OPM improvement guidance of 150 bps y-o-y. OPM improvement is likely to be on account of low remedial costs (Management expects Rs 15 cr remedial cost for FY2020 vs. Rs. 50 crores in FY2019), improved product mix along with increasing operational efficiencies. On an overall basis, we expect sales and profit CAGR to be 19% and 32%, respectively between FY2019-FY2020.

**Remediation measures completed; Await USFDA re-inspection:** Ipca has submitted response to all queries of USFDA-related to all its three sites, with no queries pending currently. We expect the USFDA to re-inspect facilities anytime in the near term. Successful inspection outcome would be the key positive factor that will lead to an earnings upgrade.

#### **Q2FY2020 Conference Call Highlights:**

- ◆ Remedial cost incurred for Q2FY2020 is Rs 4 cr, Q1FY2020 is Rs 6cr. The management has guided for a remedial cost of Rs 15 cr for Fy2020
- ◆ Ipca has incurred a capex of Rs 85 cr in 1HFY2020 while it expects to spend a similar amount in 2HFY2020. For FY2021 Ipca has guided for Rs 250 to Rs 300 cr capex, towards the API business.
- ◆ Ipca has guided for effective tax rate to be in the territory of 17.5-18% for the next 2-3 years as it has huge unutilized MAT credit.

**Results (Consolidated)**

						Rs cr
Particulars	Q2FY2020	Q2FY2019	YoY %	Q1FY2020	QoQ %	
Net sales	1283.9	997.8	28.7	1078.2	19.1	
Expenditure	1020.4	825.0	23.7	870.3	17.2	
Operating profit	263.5	172.8	52.5	207.9	26.8	
Other income	14.8	13.8	7.6	20.3	-27.1	
EBIDTA	278.3	186.5	49.2	228.2	22.0	
Interest	4.2	2.4	77.7	4.6	-8.0	
Depreciation	49.6	43.2	15.0	46.1	7.7	
PBT	224.5	141.0	59.2	177.5	26.5	
Tax	31.9	21.3	50.0	37.4	-14.7	
Adjusted PAT (ex-forex)	192.6	119.7	60.8	140.1	37.5	
Excep. Items	-1.0	0.0		10.7	-109.0	
Net profit (reported)	193.5	119.7	61.6	129.4	49.6	
EPS (Rs)	15.4	9.5	61.6	10.3	49.6	
			<b>bps</b>		<b>bps</b>	
OPM (%)	20.5	17.3	321	19.3	124	

Source: Sharekhan Research

**Geographical Sales Break-Up – Quarterly**

						Rs cr
Formulation	Q2FY2020	Q2FY2019	YoY %	Q1FY2020	QoQ %	
Domestic	543.2	468.6	15.9	452.8	20.0	
<b>Exports</b>	<b>340.8</b>	<b>288.3</b>	<b>18.2</b>	<b>244.8</b>	<b>39.2</b>	
Branded Generics	100.2	83.2	20.4	91.6	9.4	
Institutional	61.5	43.8	40.3	27.3	125.0	
Generics	179.2	161.2	11.1	125.9	42.3	
<b>Total Formulation</b>	<b>884.0</b>	<b>756.9</b>	<b>16.8</b>	<b>697.6</b>	<b>26.7</b>	
<b>APIs</b>						
Domestic	67.2	51.4	30.6	65.7	2.2	
Exports	247.2	173.7	42.3	232.6	6.3	
<b>Total APIs</b>	<b>314.4</b>	<b>225.2</b>	<b>39.6</b>	<b>298.3</b>	<b>5.4</b>	
Subsidiaries	71.3	14.2	403.1	67.2	6.2	
OOI	14.2	15.8	-10.3	15.1	-6.0	
<b>Total Sales</b>	<b>1283.9</b>	<b>1012.0</b>	<b>26.9</b>	<b>1078.2</b>	<b>19.1</b>	

Source: Company, Sharekhan Research, Industry Reports

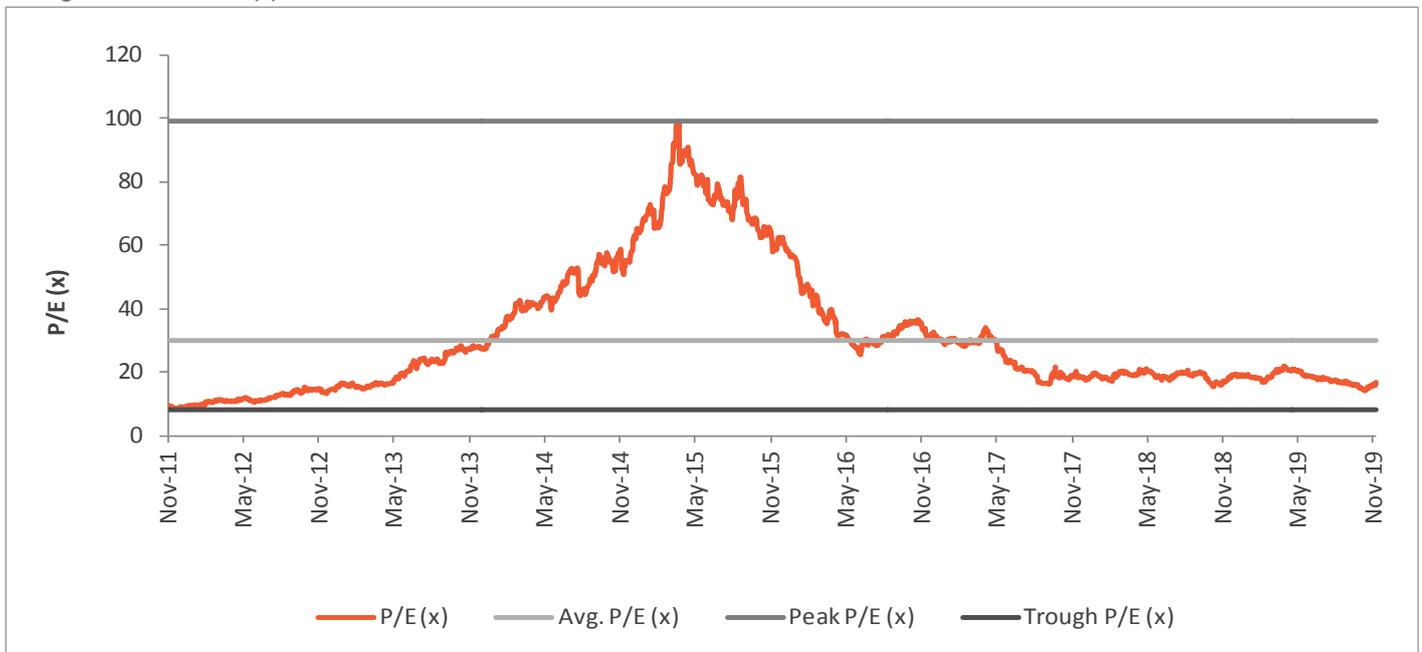
**Outlook**

Strong growth in the domestic formulation business coupled with increased opportunities in the API space and additional business from institutional anti-malaria segment indicates strong earnings potential for the company over the next 2-3 years.

**Valuation**

**Maintain Buy with revised PT of Rs. 1,220:** IPCA is on a strong footing and is well placed to capitalize on the growth opportunities across the domestic as well as exports markets. Performance across the Formulation and API segment is expected to improve as most headwinds that impacted the performance are behind. The management has maintained its sales and profitability guidance. However, given the robust performance in Q2FY2020, we have revised our earnings estimates upwards for FY2020 / FY2021. We expect the company to report sales/profit CAGR of 19%/32% over FY2019-FY2021. At CMP, the stock is trading at an attractive P/E multiple of 17.6x its FY2021 earnings. We maintain our Buy recommendation on the stock with a revised PT of Rs. 1,220. Successful resolution of the USFDA regulatory issues could provide further upside with potential for upgrade of earnings estimates.

One-year forward P/E (x) band



Source: Sharekhan Research

## About company

Ipca is a fully integrated Indian pharmaceutical company, manufacturing more than 350 formulations and 80 APIs for various therapeutic segments. Ipca is a therapy leader in India for anti-malarias with a market share of over 34% with a fast-growing presence in the international market as well. The company has leading brands in five therapeutic areas, with three of its branded formulations being ranked among the top-300 Indian brands by ORG-IMS. Ipca's APIs and formulations are produced at manufacturing facilities approved by leading drug regulatory authorities, including USFDA, U.K.-Medicines and Healthcare Regulatory Agency (MHRA), South Africa-Medicines Control Council (MCC), Brazil-Brazilian National Health Vigilance Agency (ANVISA) and Australia-Therapeutic Goods Administration (TGA) with operations in more than 100 countries.

## Investment theme

Strong growth in the domestic formulation business coupled with increased opportunities in the API space and additional business from institutional anti-malaria segment indicates strong earnings potential over the next 2-3 years. We feel most headwinds that impacted sales and profitability of the company (except for import alert from USFDA) are behind. Management has maintained its sales and profitability guidance, We expect the company to report sales/profit CAGR of 19%/32% over FY2019-FY2021.

## Key Risks

- ◆ A lack/delay of clearance by other drug regulators would impact the export business outlook
- ◆ Addition of drugs in NLEM list could hurt the domestic business; and
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## Additional Data

### Key management personnel

Premchand Godha	Chairman and Managing Director
Ajit Kumar Jain	Joint Managing Director
Dr. Ashok Kumar	President - R&D (Chemical)
E. J. Babu	President - API
Dr. Goutam Muhuri	President - R&D (Formulations)
Kavita Sehwan	President - Generics
Sunil Ghai	President – Marketing
Harish Kamath	Corporate Counsel & Company Secretary

Source: Company Website

### Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Kaygee Investments Pvt Ltd	21.4
2	DSP Investment Managers Pvt Ltd	6.6
3	KAYGEE LABORATORIES PVT LT	6.6
4	Chandurkar Investments Pvt Ltd	5.5
5	Paschim Chemicals Pvt Ltd	4.0
6	HDFC Asset Management Co Ltd	3.8
7	Lavender Investments Ltd	2.9
8	Godha Premchand	2.1
9	Norges Bank	2.1
10	UTI Asset Management Co Ltd	2.0

Source: Bloomberg

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by BNP PARIBAS

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