

IPCA Labs - BUY

Healthy outlook

Strong revenue and margin performance yoy

IPCA reported strong topline growth driven by robust traction in APIs, 13% growth in domestic business and 20% rise in branded exports. IPCA is the largest producer of Losartan globally and sartans supplies helped API business in Q1, even as obviously such high growth will not sustain. Company indicated that although gross margin might come in lower than earlier expected due to faster API sales, it would not have any impact on EBIDTA margin as API business does not involve additional costs. Despite weak malarial sales, healthy growth in pain management brands like Zerodol, 11% rise in cardiac drove domestic business. Institutional anti-malaria revenues declined 40% yoy as offtake was slow though company expects incremental Rs900mm orders to be executed over next 1 year. With API share at 28% vs 25% in base quarter, gross margin declined, accentuated by higher COGS due to increase in raw material prices.

One of the better bets in pharma; BUY stays

IPCA management expects inspection for all three affected plants in the current fiscal while UK revenues would expand on low FY19 base of Rs1.3bn as distributor issues are now behind. Domestic business guidance of 13-15% is ahead of prior indication while API growth has surprised on the upside. This leads to a cut in margin due to rise in API share even as the reduction is cushioned by larger base of absolute EBIDTA. We like the revenue visibility coupled with lack of margin volatility due to absence of US business. Retain BUY based on 21x FY21 PE, at a premium to the sector valuation with unchanged 1-year PT of Rs1,100.

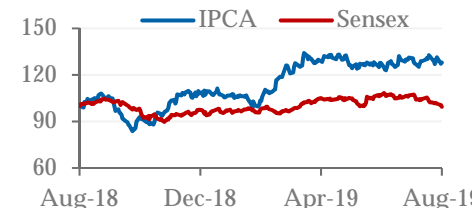
CMP (Rs) 937		12-mts Target (Rs) 1,100		Upside 17.4%	
Stock data (As on Aug 14, 2019)			Sector: Pharmaceuticals		
Sensex:	37,311	Stock performance			
52 Week h/l (Rs)	1,042/590				
Market cap (Rs mn)	118,390				
Enterprise value (Rs mn)	113,988				
6m Avg t/o (Rs mn):	116				
FV (Rs):	2				
Div yield (%):	0.3				
Bloomberg code:	IPCA IN	Shareholding pattern (As of Jun'19 end)			
BSE code:	524494	Promoter	46.1%		
NSE code:	IPCALAB	FII+DII	39.7%		
		Others	14.2%		

Exhibit 1: Result table

(Rs mn)	Q1 FY20	Q4 FY19	% qoq	Q1 FY19	% yoy
Revenues	10,782	8,796	22.6	8,754	23.2
RM + inventory	(3,211)	(2,145)	49.7	(2,456)	30.7
Purchase of stocks	(849)	(922)	(8.0)	(358)	136.9
Staff	(2,157)	(1,871)	15.3	(2,026)	6.5
Other expenses	(2,578)	(2,212)	16.5	(2,728)	(5.5)
OPM (%)	18.4	18.7	(28) bps	13.5	489 bps
Depreciation	(461)	(448)	3.0	(466)	(1.0)
Interest	(46)	(64)	(28.7)	(49)	(6.9)
Other income	203	153	33.3	143	42.0
Tax	(374)	(317)	18.0	(131)	185.8
Effective tax rate (%)	22.2	24.6	(242) bps	16.1	612 bps
PAT	1,294	960	34.8	685	88.8

Source: Company, YES Sec – Research

CONCALL HIGHLIGHTS

- ✓ Remediation cost of Rs60mn in Q1 and not more than Rs100mn in FY20
- ✓ Sartans supplies have helped in APIs; do not foresee Q1 growth to be repeated but expect strong momentum to continue. Largest global producer of Losartan and did not have the kind of impurities regulators found in other manufacturers' products
- ✓ Institutional business was slow and trim earlier guidance of Rs2.5bn to Rs2.3bn-2.5bn
- ✓ India growth of 13-15% in FY20; grew 22% in pain management in Q1. Cardiac grew 11% while malaria declined by 23%. CNS and anti-bacterial also recorded good growth.
- ✓ Pain accounts for 45% of domestic sales. Most of the rheumatoid arthritis brands are leaders in the market. About 1,000 MRs promoting Zerodol and anti-bacterial product. Price growth contributed 3-4% and rest is volumes in Q1
- ✓ Rheumatoid Arthritis: enjoy high market share of 50% and IPCA practically created this segment. Osteoarthritis has 2 brands Zerodol and Etova.
- ✓ Gross margin larger impact due to higher share of APIs followed by higher prices of COGS
- ✓ UK used to do Rs2.6bn and last year was Rs1.3bn so a 20% jump would still leave sales well below peak; UK Q1 revenues back on track at Rs400mn vs Rs340mn last year
- ✓ API revenue guidance of 20% growth in FY20 and not like 49% done in Q1

Exhibit 2: Cost analysis

As a % of net sales	Q1 FY20	Q4 FY19	bps qoq	Q1 FY19	bps yoy
RM + inventory	29.8	24.4	540	28.1	172
Staff	7.9	10.5	(261)	4.1	378
Other expenses	20.0	21.3	(126)	23.1	(314)
Total costs	23.9	25.2	(125)	31.2	(725)
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Gross profit Rs mn	6,722	5,729	17.3	5,940	13.2
GM (%)	62.3	65.1	(279)	67.8	(550)

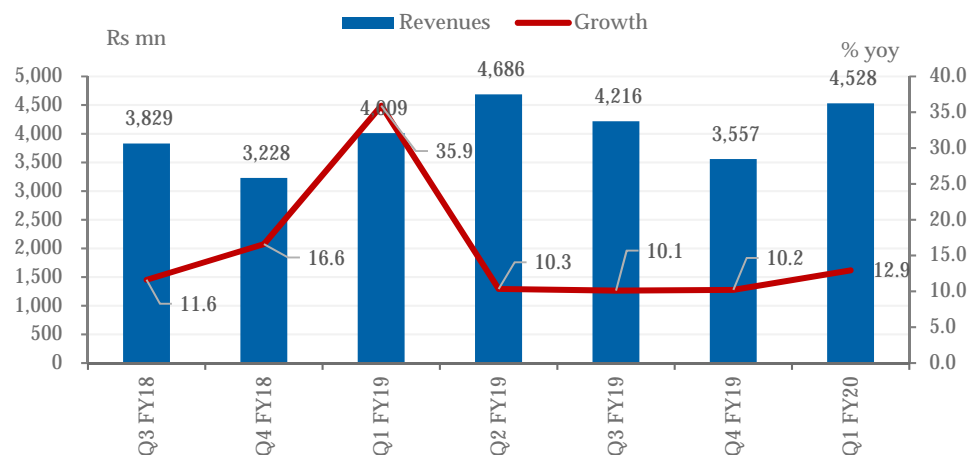
Source: Company, YES Sec – Research

Exhibit 3: Geographic breakup

Rs mn	Q1 FY20	Q4 FY19	% qoq	Q1 FY19	% yoy
India	4,528	3,557	27.3	4,009	12.9
Exports	2,448	2,536	(3.5)	2,240	9.3
Branded	916	946	(3.1)	785	16.7
Institutional	273	408	(33.1)	415	(34.1)
Generics	1,259	1,182	6.5	1,040	21.0
APIs	2,983	2,116	41.0	2,178	37.0
Domestic	657	460	42.7	600	9.5
Exports	2,326	1,656	40.5	1,577	47.5
Total	9,960	8,209	21.3	8,427	18.2

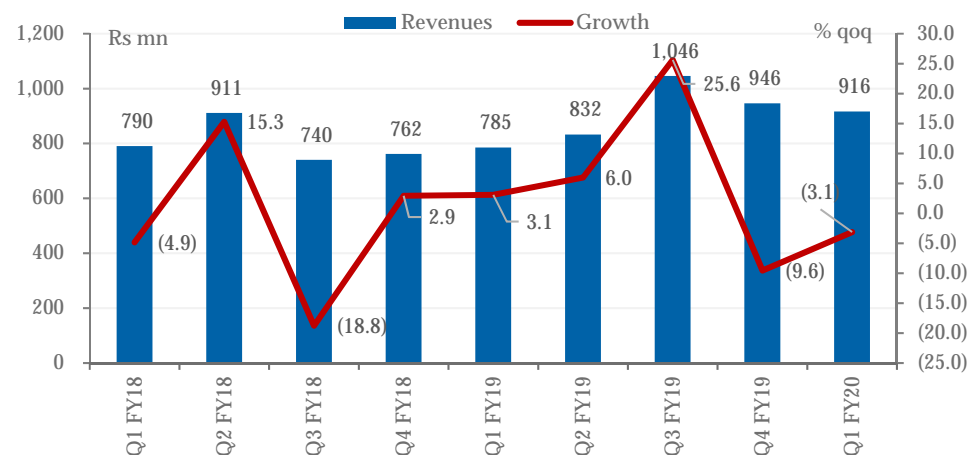
Source: Company, YES Sec – Research

Exhibit 4: India sales grew 13%



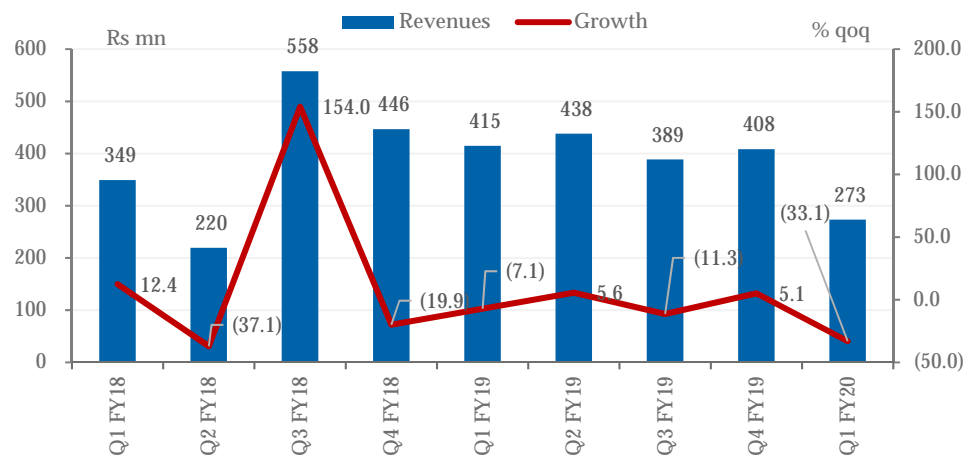
Source: Company, YES Sec – Research

Exhibit 6: Branded exports displayed strong traction yoy



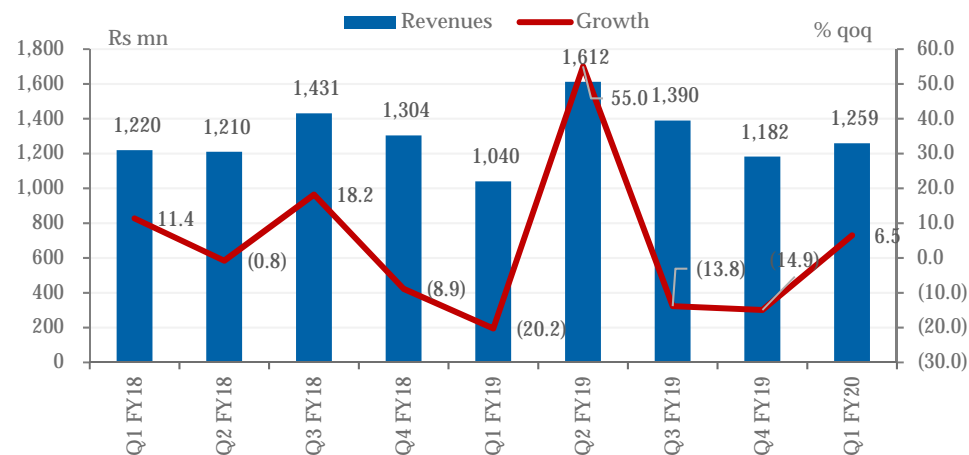
Source: Company, YES Sec – Research

Exhibit 5: Institutional business guidance trimmed in FY20



Source: Company, YES Sec – Research

Exhibit 7: Generics business jumped 21% yoy



Source: Company, YES Sec – Research

Exhibit 8: Financial summary

Y/e 31 Mar (Rs mn)	FY17	FY18	FY19	FY20E	FY21E
Revenues	31,582	32,192	36,332	41,106	45,422
yoy growth (%)	9.5	1.9	12.9	13.1	10.5
Operating profit	4,319	4,416	6,932	8,129	9,928
OPM (%)	13.7	13.7	19.1	19.8	21.9
Reported PAT	1,883	2,331	4,549	5,372	6,748
yoy growth (%)	101.9	23.8	95.1	18.1	25.6
EPS (Rs)	14.9	18.5	36.0	42.5	53.4
P/E (x)	62.8	50.7	26.0	22.0	17.5
P/BV (x)	4.8	4.4	3.8	3.3	2.8
EV/EBITDA (x)	27.9	26.9	16.8	14.1	11.0
Debt/Equity (x)	0.2	0.1	0.1	0.0	0.0
ROE (%)	7.9	9.0	15.6	15.9	17.1
ROCE (%)	9.9	10.4	17.5	18.1	19.3

Source: Company, YES Sec – Research

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