

5th May 2020

IPCA Laboratories–BUY

CMP : Rs.1,615.0
Target Price : Rs.1,939.0
Upside : 20%+
Stop Loss : Rs.1,415.0 (Closing basis)

Investment Thesis

IPCA Laboratories is a fully integrated Indian pharmaceutical company, manufacturing more than 350 formulations and 80 APIs for various therapeutic segments. It is one of the world's largest manufacturers and suppliers of over a dozen APIs. IPCA Laboratories is a therapy leader in India for anti-malarials with a market share of over 34% with a fast-growing presence in the international market as well. It 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 Laboratories' APIs and formulations are produced at manufacturing facilities approved by leading drug regulatory authorities, including USFDA, UK's Medicines and Healthcare Regulatory Agency (MHRA), South Africa's Medicines Control Council (MCC) and Brazil's Brazilian National Health Vigilance Agency (ANVISA) with operations in more than 120 countries.

Strong growth in domestic formulation business coupled with increased opportunities in the API space and additional business from institutional anti-malaria segment indicates IPCA Laboratories' strong growth potential over the next 2-3 years. In the API space, alternative sourcing opportunities (as most of companies look to India as alternative sourcing destination to China) is expected to be a key growth driver. For FY20E, the management has maintained its conservative guidance for ~20% sales growth and OPM improvement guidance of 150bps YoY. OPM improvement is likely to be on account of low remedial costs (Rs.150mn remedial cost for FY20E as against Rs.500mn in FY19), improved product mix along with increasing operational efficiencies.

Financials

- During the past 5 years, revenue of IPCA Laboratories grew at CAGR of 2.7% while PAT de-grew at CAGR of 1.4% in the same period.

Consol. (Rs.Mn.)	FY17	FY18	FY19	FY20E	FY21E
Revenue	31,562	32,578	37,457	44,199	50,829
EBITDA	4,154	4,420	6,783	7,970	9,165
% growth	51.8	6.4	53.5	17.5	15.0
PAT	1,945	2,394	4,456	5,837	6,713
EPS (INR)	15.4	19.0	35.3	46.2	53.1
P/E (x)	105.0	85.3	45.9	35.0	30.5
RoE (%)	7.9%	8.9%	14.3%	17.0%	17.8%

- IPCA Laboratories has reported 20.5% YoY growth in revenue to Rs.12,129mn in Q3FY20 mainly due to 25.2% YoY growth in export formulations to Rs.3,534mn.

Stock Data

Market Cap (Rs. Mn)	2,04,476
Market Cap (\$ Mn)	2,722.4
Shares O/S (in Mn)	126.4
Avg. Volume (3 month)	610,000
52-Week Range (Rs.)	1,825.00/ 844.65

Shareholding Pattern

Promoters	46.07%
FII's	13.99%
Institutions	25.93%
Others (incl. body corporate)	14.01%

Performance (%)	1M	6M	1Yr
Absolute	24.8%	66.1%	69.9%
BSE Healthcare	35.3%	19.3%	-0.8%

Key Ratios

Div Yield	0.2%
TTM PE	33.1x
ROE	16.3%
TTM EPS (Rs.)	49.0/-

- IPCA Laboratories' domestic revenues grew 15.2% YoY to Rs.4,856mn whereas API segment grew 24.0% YoY to Rs.2,854mn in Q2FY20.
- IPCA Laboratories' EBITDA grew by 16.7% YoY in Q3FY20 to Rs.2,737mn mainly due to better revenue growth and better-than-expected operational performance. However, EBITDA margin declined by 74.0bps YoY to 22.6% in Q3FY20.
- IPCA Laboratories' PAT grew by 24.1% YoY to Rs.1,976mn due to 35.9% higher Other Income and lower interest outgo in the quarter.

Key Business Highlights

- Established in 1949, IPCA Laboratories is known for its dominance in the anti-malarial business. It has come a long way from being an anti-malarial player to a player offering a gamut of other therapeutic products. It has been partnering healthcare globally in over 120 countries and in markets as diverse as Africa, Asia, Australia, Europe and the US.
- IPCA Laboratories' domestic formulations comprise 44% of FY19 revenues. And its major therapies in domestic formulations are pain management, anti-malarial, cardiovascular (CVS) and gastrointestinal (GI).
- In domestic formulations, IPCA Laboratories owns a field force of 4000 MRs covering 12 therapy focused marketing divisions.

Valuation

- IPCA Laboratories has recently acquired Nobel Explochem with the intention to manufacture key starting materials, APIs and thus reduce dependency on external sourcing. Nobel Explochem assets consist of free-hold land of 690 acres, leasehold land of 180 acres and forest land of 239 acres. It also provides access to nitration chemistry to be used for developing/commercializing APIs. We believe, it will take about two years for production to begin from this site.
- IPCA Laboratories has incurred a capex of Rs.850mn in H1FY20 while it has guided to spend a similar amount in H2FY20E also. Considering increasing demand for captive consumption and external sales, the company has earmarked capex of Rs.2,500mn for FY21E to enhance API and intermediates capacity. Most of the capex (excluding maintenance capex) is contingent on Dewas API plant environment clearance, which is expected to be commercialized by FY22E.
- IPCA Laboratories 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. We believe, a successful inspection outcome will be the key positive factor for IPCA Laboratories.
- With fully integrated Indian pharmaceutical company, manufacturing more than 350 formulations and 80 APIs, alternative sourcing opportunities in API space, recently acquired Nobel Explochem to reduce dependency on external sourcing, capex of Rs.2,500mn for FY21E to enhance API and intermediates capacity and submitted response to all queries of USFDA, we value IPCA Laboratories at 36.50x FY21E EPS of Rs.53.10 to arrive at target price of Rs.1,939.00, an upside of ~20%.

Risk & Concern

- Any delay or lack of clearance by other drug regulators will impact the export business outlook of IPCA Laboratories.
- Any addition of drugs in NLEM list may hurt the domestic business of IPCA Laboratories.
- IPCA Laboratories' major part of revenue comes through export, hence any weakness in emerging market currencies may affect the growth prospects of the company.

Graphs & Charts

Figure 1: Net Sales Trend

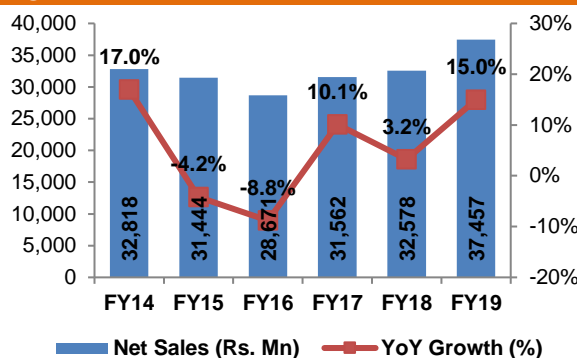


Figure 2: EBITDA & EBITDA Margin Trend

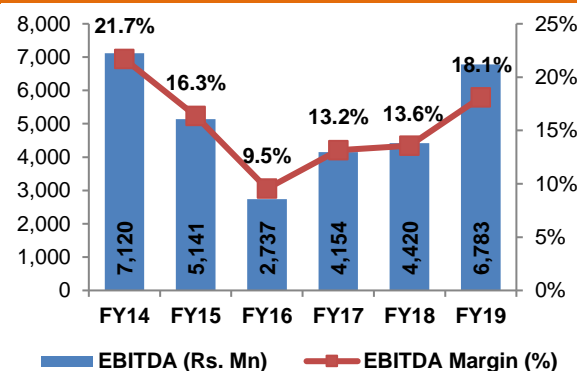


Figure 3: PAT Trend

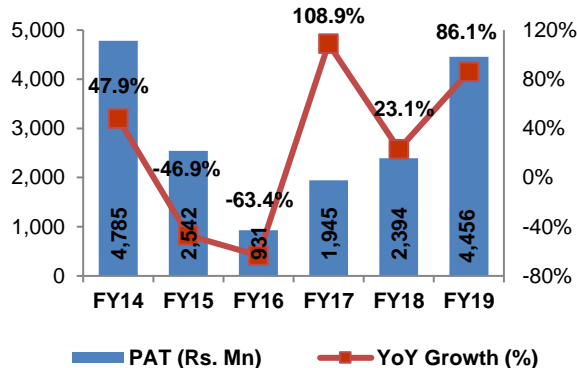
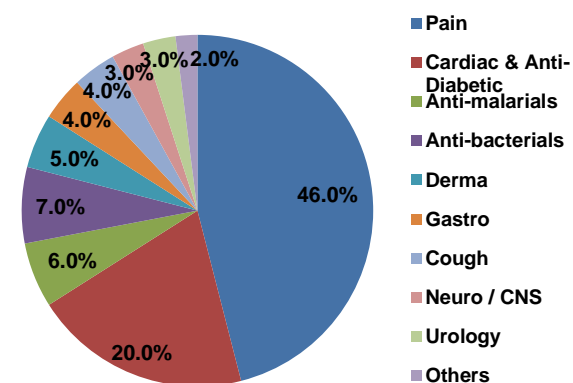


Figure 4: Disease-wise Domestic Formulation



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