

BSE SENSEX

32,310

S&P CNX

10,015

CMP: INR390 TP: INR330(-15%)
Sell

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Bloomberg	BIOS IN
Equity Shares (m)	600
M.Cap.(INR b)/(USD b)	234.1 / 3.6
52-Week Range (INR)	424 / 256
1, 6, 12 Rel. Per (%)	16/-1/27
Avg Val, (INR m)	1082
Free float (%)	39.3

Financials & Valuations (INR b)

Y/E Mar	2017	2018E	2019E
Net Sales	40.8	50.6	63.5
EBITDA	11.4	12.2	16.3
PAT	6.0	5.8	8.5
EPS (INR)	10.2	9.7	14.2
Gr. (%)	31.8	-4.8	45.9
BV/Sh (INR)	80.6	87.5	97.5
RoE (%)	12.3	11.1	14.5
RoCE (%)	9.4	8.8	14.9
P/E (x)			
P/BV (x)	38.2	40.1	27.5
P/BV (x)	4.8	4.5	4.0
EV/EBITDA (x)	20.5	19.3	14.2
Div. Yield (%)	0.7	0.6	0.9

Estimate change



TP change



Rating change



Quarterly performance (Consolidated)

Y/E March	FY17				FY18E				FY17	FY18E	(INR Million)	
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE			1QE	vs Est
Net Sales	9,920	9,400	10,290	9,250	9,337	10,939	12,033	17,948	40,787	50,603	10,076	-7.3%
YoY Change (%)	22.4	19.6	24.2	-2.1	-5.9	16.4	16.9	94.0	18.2	24.1	2.7	
Total Expenditure	7,289	7,150	7,680	7,430	7,416	8,313	9,145	13,552	29,421	38,426	7,738	
EBITDA	2,631	2,250	2,610	1,820	1,921	2,625	2,888	4,397	11,366	12,177	2,338	-17.8%
Margins (%)	26.5	23.9	25.4	19.7	20.6	24.0	24.0	24.5	27.9	24.1	23.2	
Depreciation	661	680	710	730	988	1,000	1,050	2,034	2,772	5,072	950	
Interest	57	70	90	50	161	68	68	-61	260	236	68	
Other Income	409	520	630	653	540	500	500	460	0	2,000	500	
PBT	2,322	2,020	2,440	1,693	1,312	2,057	2,270	2,884	8,334	8,870	1,820	-27.9%
Tax	552	420	550	110	376	494	545	714	1,616	2,129	437	
Rate (%)	23.8	20.8	22.5	6.5	28.7	24.0	24.0	24.8	19.4	24.0	24.0	
Minority Interest	104	130	180	150	123	175	175	439	760	912	175	
PAT	1,666	1,470	1,710	1,433	813	1,389	1,550	1,731	5,958	5,829	1,208	-32.7%
YoY Change (%)	34.6	51.5	66.0	-56.6	-51.2	-5.5	-9.3	20.8	28.3	-2.2	32.0	
Margins (%)	16.8	15.6	16.6	15.5	8.7	12.7	12.9	9.6	14.6	11.5	12.0	

Malaysian plant commercialization impacts profits

- Biocon (BIOS) reported weak 1QFY18 results. Revenue declined 5% YoY to INR9.3b (est. of INR10b), mainly due to weak performance in the Small molecules (-17% YoY) and Branded formulations (-13% YoY) segments. With commercialization of the Malaysian plant, operational expense and fixed cost (depreciation and interest cost) increased ~USD12m, leading to a 27% YoY decline in EBITDA to INR1.9b (est. of INR2.3b). Margin for the quarter came in at 20.6% (-530bp YoY), with employee expenses up ~400bp YoY (as % of sales).
- **Branded business impacted by GST; Syngene showing signs of recovery:** Small molecules sales declined 17% YoY due to pricing pressure. Branded formulations sales fell 13% YoY due to destocking in trade channels ahead of GST implementation. BIOS, however, expects growth to bounce back in 2Q. The company has guided for mid-to-high-teens growth in India business in the coming quarters. Biologics business grew 15% YoY in 1Q. Syngene business (~29% of revenue) grew 6% YoY.
- **Concall takeaways:** 1) Maintained USD200m of revenue guidance from Biologics in FY19E; substantial portion will come from EMs. 2) Tender business from the Malaysian plant is worth USD20m annualized (USD5m in 1Q). 3) Peg Filgrastim TAD is 9th Oct. 4) Malaysian facility was inspected by EU regulator in Mar/Apr-17. Observations were issued, and Biocon has replied to it. 5) Syngene signed a multi-year agreement with Japanese manufacturer to produce a novel drug.
- **Biosimilars pipeline progressing well:** The recent run-up in the stock price is primarily led by positive developments in the Biosimilars portfolio. Although the progress is impressive, there are still uncertainties that cap the upside potential. In the near term, commissioning of the Malaysia plant would exert pressure on profits. We thus cut our FY18E EPS by 6.7%. However, we have increased our TP multiple on the back of enhanced visibility of Biologics launch in the EU and US markets. Maintain **Sell** with a TP of INR330 @ 23x FY19E EPS (v/s INR300 @ 20x FY19E EPS).

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Muted performance due to de-growth in Syngene

Biocon posted muted growth during the quarter on back of weak performance in Small molecules and Branded formulation segment, declining 14%YoY and 22%YoY respectively. Fire incident at Syngene facility continued to impact its performance, which posted 6%YoY growth as against 23% growth in 1QFY17. Biologics segment posted robust growth of 15%YoY to INR1.8b on back of increased market share of Insulin in Emerging Market.

Exhibit 1: Quarterly performance (sales mix) (IND AS format)

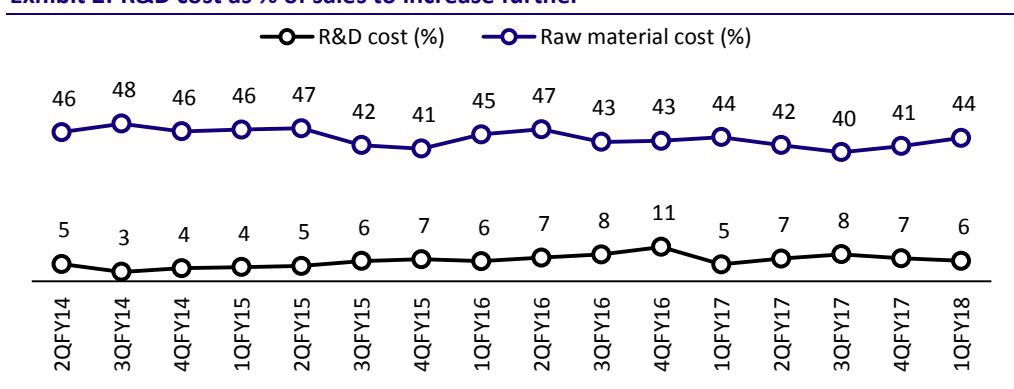
(INR m)	1QFY18	1QFY17	% YoY	4QFY17
Small Molecules	3,629	4,354	-17.0	3,870
% of sales	38.9	43.9		41.8
Biologics	1,839	1,606	15.0	1,190
% of sales	19.7	16.2		12.9
Branded Formulations	1,227	1,408	-13.0	1,310
% of sales	13.1	14.2		14.2
Licensing Income	77	172	-55.0	160
% of sales	0.8	1.7		1.7
Research-Syngene	2,911	2,754	6.0	2,720
% of sales	31.2	27.7		29.4
Total Revenues	9,337	9,920	-6.0	9,250

Source: Company, MOSL

Higher R&D coupled with commissioning of Malaysia plant to limit margins expansion

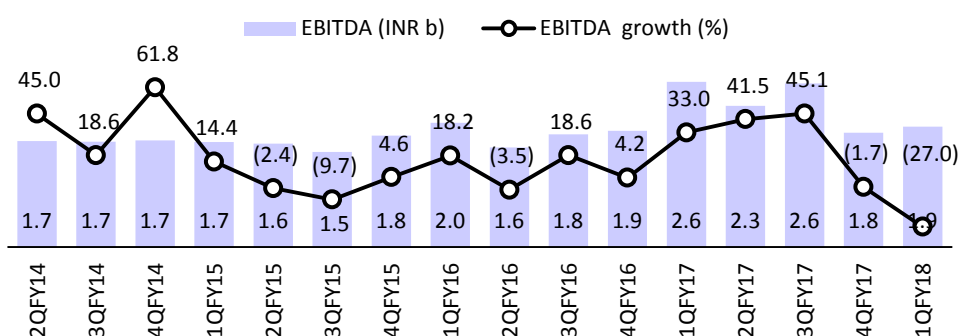
Gross R&D spend for the quarter was INR960 million of which INR580 million was in P&L (~6% of sales excluding Syngene). Going ahead R&D spend will be around 11% of revenues on back of novel development programs and also some of other biosimilar and insulin which will progress further into the clinic.

Exhibit 2: R&D cost as % of sales to increase further



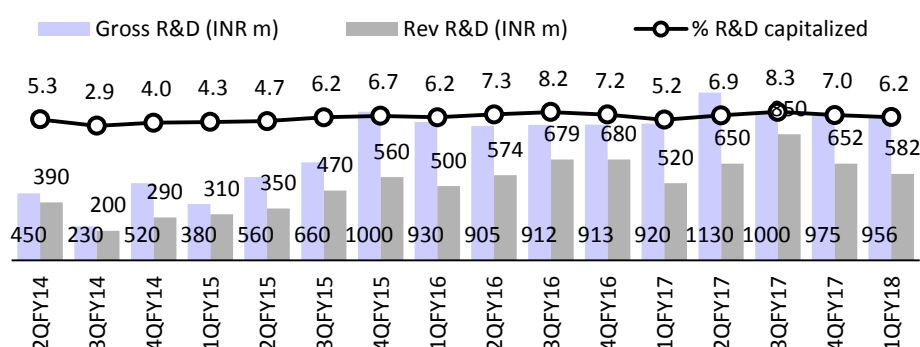
Source: Company, MOSL

Exhibit 3: EBITDA growth quarterly trend (INR b)



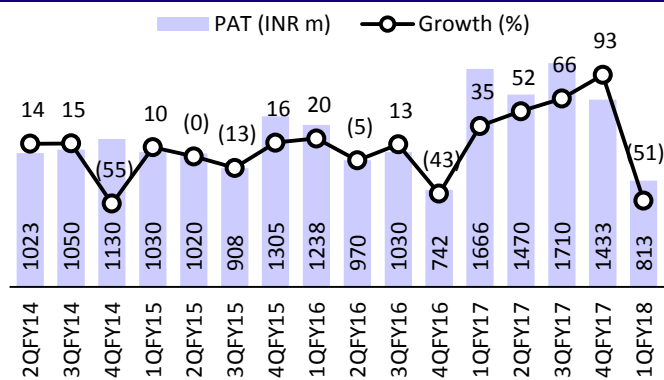
Source: Company, MOSL

Exhibit 4: Higher R&D cost being capitalized



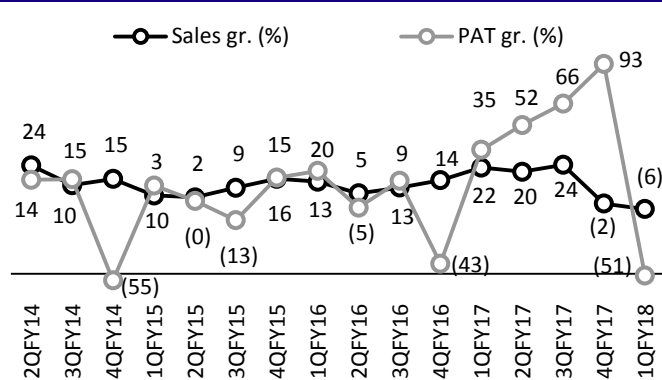
Source: Company, MOSL

Exhibit 5: Quarterly earnings trend



Source: Company, MOSL

Exhibit 6: Sales growth v/s PAT growth



Source: Company, MOSL

Other key highlights

- **Malaysia facility:** Tender business from the Malaysian plant is worth USD20m annualized (USD5m in 1Q). The facility was inspected by the EU regulator in Mar-17/Apr-17. Observations were issued and Biocon has replied to it.
- **Branded Formulations:** The segment declined 13% YoY to INR1.2b on the back of low licensing income and channel de-stocking due to GST implementation.
- **Biologics:** The company maintained its FY19E guidance of USD200m of revenue (v/s USD75m in FY17). Majority of revenue contribution will come from emerging markets, while revenue related to initial supply to developed markets can come in FY19.

- **R&D guidance:** Biocon will be spending 11% of revenue on R&D. Out of this, ~10% will be expensed through P&L, and the rest will be capitalized.
- **Partnered products:** Biocon has target action date of Sep/ Oct-17 for Trastuzumab (Herceptin) and Pegfilgrastim (Neulasta) from the US FDA. The company is on track to file other two key molecules – Adalimumab (Humira) and Glargine (Lantus) – in FY18 in developed markets.

Operating metrics

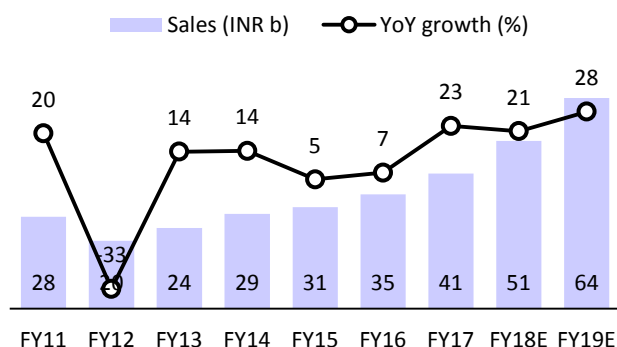
Exhibit 7: Key operating metrics

	1QFY15	2QFY15	3QFY15	4QFY15	1QFY16	2QFY16	3QFY16	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18
Cost of sales (%)													
Raw material	46.5	46.9	41.7	40.7	45.0	46.6	42.7	43.0	44.2	41.7	39.6	41.4	43.9
Staff cost	16.2	16.7	17.9	16.4	16.7	16.5	17.6	16.3	16.6	17.7	17.4	19.2	20.7
R&D cost	4.3	4.7	6.2	6.7	6.1	7.3	8.2	10.5	5.2	6.9	8.3	7.0	6.2
Other expenses	9.8	9.7	14.3	14.7	7.8	9.4	9.8	10.6	7.6	9.8	9.4	12.6	8.6
Tax Rate	22.4	16.9	10.3	12.8	22.8	145.0	16.6	14.6	23.8	20.8	22.5	6.5	28.7
Margins (%)													
Gross Margins	53.5	53.1	58.3	59.3	55.0	53.4	57.3	57.0	55.8	58.3	60.4	58.6	56.1
EBITDA Margins	23.3	22.0	19.9	21.4	24.4	20.2	21.7	19.6	26.5	23.9	25.4	19.7	20.6
EBIT Margins	16.1	14.8	12.5	14.4	17.1	12.5	14.2	12.8	19.9	16.7	18.5	11.8	10.0
PAT margins	14.3	13.6	11.9	24.3	15.3	(1.4)	12.4	35.0	16.8	15.6	16.6	15.5	8.7

Source: MOSL, Company

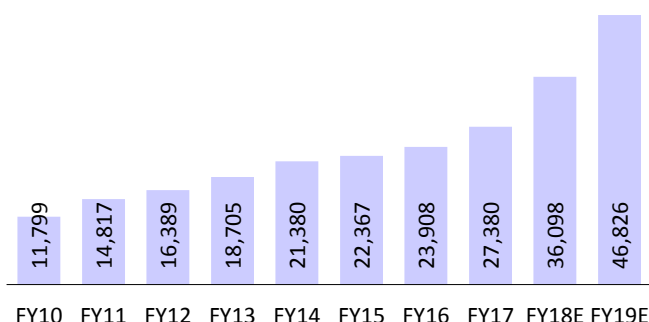
Story in charts

Exhibit 1: Revenue growth to pick up in FY17-18E



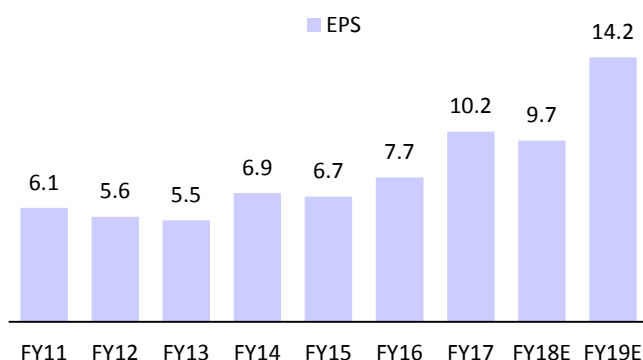
Source: Company, MOSL

Exhibit 2: Biopharma sales trend (In INR m)



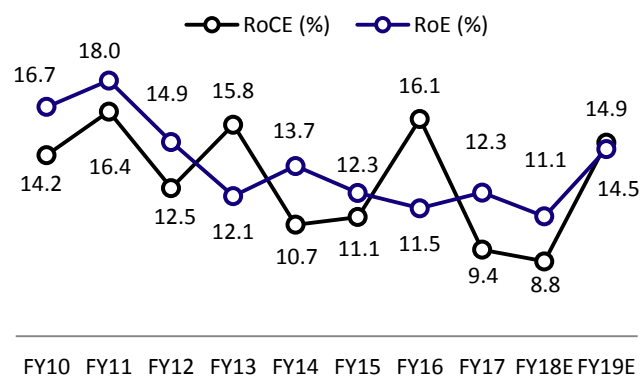
Source: Company, MOSL

Exhibit 3: EPS to grow at 18% CAGR from FY17-19E



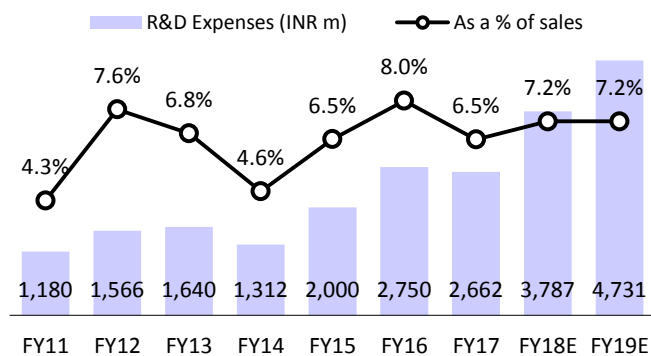
Source: Company, MOSL

Exhibit 4: Return ratios trending lower with high capex



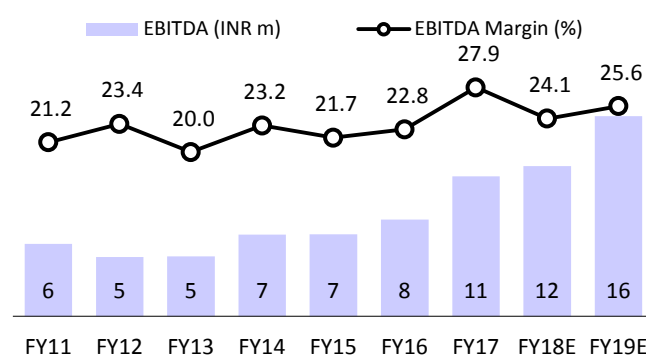
Source: Company, MOSL

Exhibit 5: R&D expenses (annual trend)



Source: Company, MOSL

Exhibit 6: EBITDA margin trend



Source: Company, MOSL

Financials and Valuations

Income Statement (Consolidated)						(INR Million)	
Y/E March	2013	2014	2015	2016	2017	2018E	2019E
Net Sales	18,704	21,390	22,367	23,908	29,407	35,628	45,572
Contract Research	5,572	7,137	8,225	10,599	11,380	14,975	17,934
Net Income	24,276	28,527	30,592	34,507	40,787	50,603	63,506
Change (%)	18.5	17.5	7.2	12.8	18.2	24.1	25.5
Total Expenditure	19,423	21,902	23,940	26,654	29,421	38,426	47,255
EBITDA	4,853	6,625	6,652	7,853	11,366	12,177	16,251
Change (%)	1.1	36.5	0.4	18.1	44.7	7.1	33.5
Margin (%)	20.0	23.2	21.7	22.8	27.9	24.1	25.6
Depreciation	1,793	2,036	2,210	2,423	2,772	5,072	5,408
EBIT	3,060	4,589	4,442	5,430	8,594	7,105	10,843
Int. & Finance Charges	81	17	89	102	260	236	241
Other Income - Rec.	3,123	805	1,888	6,946	0	2,000	2,200
PBT	6,101	5,377	6,241	12,274	8,334	8,870	12,802
Tax	975	1,069	957	2,569	1,616	2,129	3,201
Tax Rate (%)	16.0	19.9	15.3	20.9	19.4	24.0	25.0
Minority Interest	38	170	310	744	760	912	1094
Adjusted PAT	3,271	4,137	4,023	4,646	5,958	5,829	8,507
PAT	5,088	4,137	4,974	8,961	5,958	5,829	8,507
Change (%)	50.3	-18.7	20.2	80.2	-33.5	-2.2	45.9
Margin (%)	21.0	14.5	16.3	26.0	14.6	11.5	13.4

Consolidated Balance Sheet						(INR Million)	
Y/E March	2013	2014	2015	2016	2017	2018E	2019E
Equity Share Capital	1,000	1,000	1,000	1,000	3,000	3,000	3,000
Other Reserves	25,937	29,258	31,697	39,329	45,368	49,492	55,511
Net Worth	26,946	30,267	32,706	40,338	48,377	52,501	58,520
Loans	2,488	8,497	10,306	24,673	22,054	23,054	24,054
Minority Interest	653	823	1,722	2,658	3,761	4,673	5,767
Deferred liabilities	4689	6558	5934	3489	1964	624	-600
Capital Employed	34,776	46,145	50,667	71,158	76,156	80,852	87,741
Gross Block	24,961	27,218	29,750	33,113	53,269	61,269	66,769
Less: Accum. Deprn.	9,672	11,711	13,943	16,302	17,740	22,812	28,220
Net Fixed Assets	15,289	15,507	15,807	16,811	35,529	38,457	38,549
Capital WIP	2,054	10,831	14,939	20,597	5,327	5,327	5,327
Investments	5,866	7,649	2,303	9,015	12,538	8,224	9,182
Intangibles	1,290	1,442	2,320	2,470	3,787	4,166	4,582
Curr. Assets	19,662	22,077	28,384	34,973	34,786	42,978	53,067
Inventory	3,984	3,766	4,527	5,424	6,353	7,625	9,569
Account Receivables	5,097	5,998	7,705	7,145	8,832	11,091	13,919
Cash and Bank Balance	6,729	8,044	9,375	15,386	10,443	13,864	17,399
Loans & Advances	3,852	4,269	6,777	7,018	9,158	10,398	12,179
Curr. Liability & Prov.	9,385	11,361	13,087	12,708	15,811	18,300	22,967
Account Payables	6,920	9,595	11,355	12,334	15,343	15,250	19,139
Provisions	2,465	1,766	1,732	374	468	3,050	3,828
Net Current Assets	10,277	10,716	15,297	22,265	18,975	24,678	30,100
Appl. of Funds	34,776	46,145	50,667	71,158	76,156	80,852	87,741

E: MOSL Estimates

Financials and Valuations

Ratios

Y/E March	2013	2014	2015	2016	2017	2018E	2019E
Basic (INR)							
EPS	5.5	6.9	6.7	7.7	10.2	9.7	14.2
Cash EPS	11.5	10.3	12.0	19.0	14.6	18.2	23.2
BV/Share	44.9	50.4	54.5	67.2	80.6	87.5	97.5
DPS	2.5	1.7	1.7	1.7	2.6	2.4	3.5
Payout (%)	34.5	28.3	23.5	13.4	30.1	29.3	29.3
Valuation (x)							
P/E	71.5	56.6	58.2	50.4	38.2	40.1	27.5
Cash P/E	34.0	37.9	32.6	20.6	26.8	21.5	16.8
P/BV	8.7	7.7	7.2	5.8	4.8	4.5	4.0
EV/Sales	9.2	8.0	7.6	6.8	5.7	4.6	3.6
EV/EBITDA	46.1	34.2	35.0	29.8	20.5	19.3	14.2
Dividend Yield (%)	0.6	0.4	0.4	0.4	0.7	0.6	0.9
Return Ratios (%)							
RoE	12.1	13.7	12.3	11.5	12.3	11.1	14.5
RoCE	15.8	10.7	11.1	16.1	9.4	8.8	14.9
RoIC	13.7	18.5	17.2	17.1	18.7	10.7	14.9
Working Capital Ratios							
Fixed Asset Turnover (x)	1.7	1.9	2.0	2.1	1.6	1.4	1.6
Debtor (Days)	77	77	92	76	79	80	80
Inventory (Days)	60	48	54	57	57	55	55
Working Capital (Days)	53	34	71	73	76	78	73
Leverage Ratio (x)							
Current ratio	2.1	1.9	2.2	2.8	2.2	2.3	2.3
Debt/Equity	0.1	0.3	0.3	0.6	0.5	0.4	0.4

Consolidated Cash Flow Statement

(INR Million)

Y/E March	2013	2014	2015	2016	2017	2018E	2019E
Oper. Profit/(Loss) before Tax	4,853	6,625	6,652	7,853	11,366	12,177	16,251
Interest/Dividends Recd.	3,123	805	937	2,630	0	2,000	2,200
Direct Taxes Paid	-2,040	800	-1,581	-5,014	-3,141	-3,469	-4,425
(Inc)/Dec in WC	-1,910	876	-3,251	-956	-1,653	-2,282	-1,887
CF from Operations	4,025	9,106	2,758	4,513	6,572	8,426	12,139
(Incr)/Dec in FA	-3,535	-11,031	-6,618	-9,085	-6,220	-8,000	-5,500
Free Cash Flow	490	-1,925	-3,861	-4,572	352	426	6,639
(Pur)/Sale of Investments	-358	-1,935	4,468	-6,862	-4,840	3,935	-1,375
CF from investments	-3,893	-12,966	-2,151	-15,946	-11,060	-4,065	-6,875
Change in Net Worth	2,706	354	-414	4,190	3,871	0	0
(Inc)/Dec in Debt	494	6,009	2,397	14,559	-2,276	1,000	1,000
Interest Paid	-81	-17	-89	-102	-260	-236	-241
Dividend Paid	-1,755	-1,170	-1,170	-1,204	-1,790	-1,705	-2,488
CF from Fin. Activity	1,364	5,175	724	17,444	-455	-941	-1,729
Inc/Dec of Cash	1,496	1,315	1,331	6,011	-4,943	3,421	3,535
Add: Beginning Balance	5,233	6,729	8,044	9,375	15,386	10,443	13,864
Closing Balance	6,729	8,044	9,375	15,386	10,443	13,864	17,399

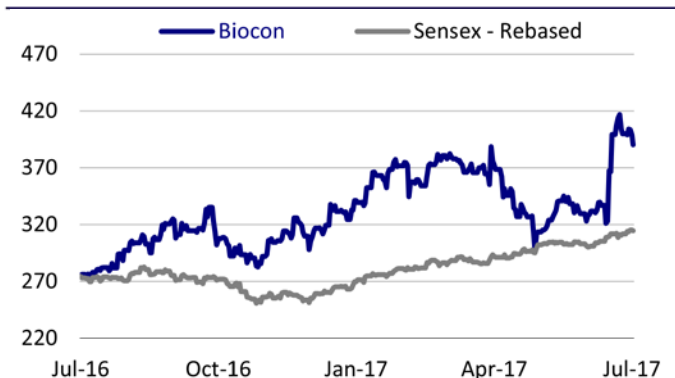
E: MOSL Estimates

Corporate profile

Company description

Biocon is an integrated biotechnology company encompassing all the three critical stages of drug development - drug discovery, development and manufacturing, and commercialization of bio-pharmaceuticals. With over 25 years of expertise in fermentation technology, the company has built a strong presence in lucrative high-growth segments like statins, immuno-suppressants and anti-diabetes.

Exhibit 1: Sensex rebased



Source: MOSL/Bloomberg

Exhibit 2: Shareholding pattern (%)

	Jun-17	Mar-17	Jun-16
Promoter	60.7	60.7	60.7
DII	3.7	3.7	5.1
FII	16.9	19.5	17.1
Others	18.8	16.1	17.2

Note: FII Includes depository receipts

Source: Capitaline

Exhibit 3: Top holders

Holder Name	% Holding
OPPENHEIMER DEVELOPING MARKETS FUND	2.6
FRANKLIN TEMPLETON INVESTMENT FUNDS	1.7
NATIONAL WESTMINSTER BANK PLC AS TRUSTEE OF THE JUPITER INDIA FUND	1.4
Arun Suresh Chandavarkar	1.1

Source: Capitaline

Exhibit 4: Top management

Name	Designation
Kiran Mazumdar Shaw	Chairperson & Managing Direct
John Shaw	Vice Chairman
Arun Suresh Chandavarkar	Joint Managing Director & CEO
Kiran Kumar	Company Secretary

Source: Capitaline

Exhibit 5: Directors

Name	Name
Kiran Mazumdar Shaw	Mary Harney*
John Shaw	Ravi Mazumdar
Arun Suresh Chandavarkar	Russell Walls*
Daniel M Bradbury*	Vijay Kumar Kuchroo*
Jeremy Levin*	M Damodaran*

*Independent

Exhibit 6: Auditors

Name	Type
Rao & Murty	Cost Auditor
S R Batliboi & Associates LLP	Statutory

Source: Capitaline

Exhibit 7: MOSL forecast v/s consensus

EPS (INR)	MOSL forecast	Consensus forecast	Variation (%)
FY18	9.7	9.9	-1.8
FY19	14.2	13.0	8.9

Source: Bloomberg

NOTES

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