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Ipca Laboratories Ltd

Brighter Growth prospects

Stock Update

Pharmaceuticals	Sharekhan code: IPCALAB	Company Update

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

What has changed in 3R MATRIX

	Old		New
RS		↔	
RQ		↔	
RV		↔	

Reco/View	Change
Reco: **Buy**	↔
CMP: **Rs. 2,524**	
Price Target: **Rs. 2,850**	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

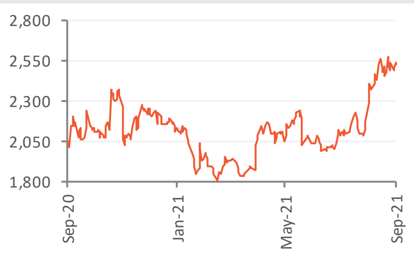
Company details

Market cap:	Rs. 32,012 cr
52-week high/low:	Rs. 2,664 / 1,786
NSE volume: (No of shares)	5.04 lakh
BSE code:	524494
NSE code:	IPCALAB
Free float: (No of shares)	6.8 cr

Shareholding (%)

Promoters	46.3
FII	13.2
DII	28.1
Others	12.5

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	9.9	23.7	30.2	23.5
Relative to Sensex	2.8	11.5	15.9	-29.2

Sharekhan Research, Bloomberg

Summary

- IPCA laboratories (IPCA) domestic formulations business is on a strong footing and is expected to be a key growth driver with a likely double digit growth for FY22.
- IPCA's presence in the fast growing therapies coupled with positive rub off effect of a strong IPM growth could be the key drivers for domestic formulations business.
- For the API segment, completion of Dewas greenfield (expected to add 25% of capacities) by FY2023 and a strong demand outlook would be the key drivers.
- At CMP the stock trades at 27.2x /24.1x its FY22E and FY23E EPS. Strong earnings prospects, a sturdy balance sheet, and healthy return ratios augur well for IPCA. We maintain Buy recommendation with a revised PT of Rs 2850.

Ipca Laboratories Limited's (IPCA) domestic formulations segment is on a strong footing and the company has outperformed the IPM growth over the recent three months, attributable to a strong presence in the fast growing therapy areas and low base in previous year. The sturdy growth momentum is expected to sustain going ahead as well. Over the long term the easing of capacity constraints for the API segment backed by commissioning of Dewas greenfield provides ample visibility on growth.

- **Sturdy IPM growth likely to have a positive rub off effect:** IPCA derives around 40% of the revenues from the domestic markets, which is substantial. The IPM is expected to grow in high single digit to double digit for FY2022 backed by a pick up in volumes while the strong pricing growth and share of new products growth is likely to sustain. This is expected to have a positive rub-off effect on the performance of the companies such as IPCA laboratories.
- **Domestic formulations on a strong footing to clock a double-digit growth:** IPCA's domestic formulations segment is expected to be a key growth driver for the company and the revenues are likely to stage a double digit growth over 20% CAGR over FY21-FY23E on the back of improvement in the acute therapy areas and presence in the fast growing segments such as pain / analgesics, gastro intestinal amongst others.
- **Ratlam expansion to be ready in 2HFY22; while covid delays Dewas greenfield:** Over the long term, IPCA's API segment growth would be driven by easing capacity constraints due to the commissioning of Dewas greenfield, which would add on ~25% of the capacity. The Ratlam expansion is expected to be ready by 2HFY22. IPCA has lined up a capex of Rs. 400 crores over next 2-3 years and this provides comfort on the future growth prospects.

Our Call

Maintain Buy with revised PT of Rs 2,850: IPCA's domestic formulations, which account for ~40% of the company's overall topline, is expected to be a key growth driver and management has guided for double-digit growth in FY2022. Consistent outperformance to the IPM over the past 3 months, presence in fast growing therapy areas, provides visibility on the growth ahead. Over the long term, the easing capacity constraints backed by commissioning of the Dewas Greenfield could be the growth drivers for the API segment. At CMP the stock trades at 27.2x /24.1x its FY22E and FY23E EPS and we have also introduced FY24 estimates in this note. We maintain our Buy recommendation on the stock with revised PT of Rs 2,850.

Key risk

1) A delay in regulatory clearance of its plants and 2) adverse changes in the regulatory landscape could have an adverse impact on profitability.

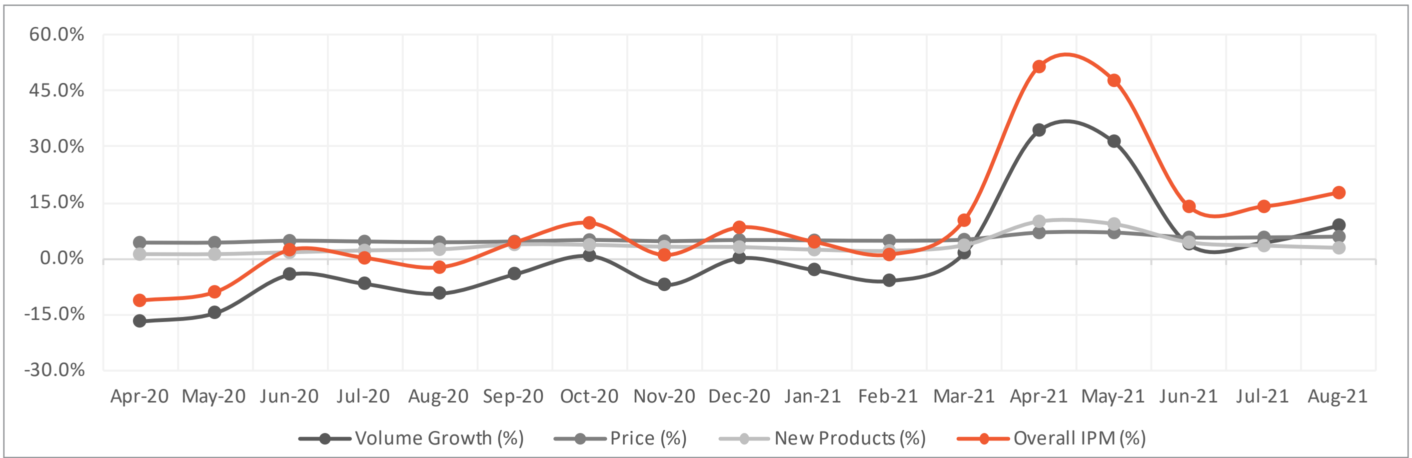
Valuation (Consolidated) Rs cr

Particulars	FY2020	FY2021	FY2022E	FY2023E	FY2024E
Net sales	4,648.7	5,420.0	5,984.8	6,689.7	7,482.6
Operating Profit	906.7	1,544.4	1,585.7	1,802.6	2,039.8
OPM (%)	19.5	28.5	26.5	26.9	27.3
PAT	603.6	1,141.1	1,170.6	1,321.5	1,482.2
EPS (Rs)	47.8	90.5	92.8	104.8	117.5
PER (x)	52.8	27.9	27.2	24.1	21.5
EV/Ebidta (x)	35.6	20.7	19.6	16.7	14.2
RoCE (%)	18.6	29.3	24.9	23.5	22.3
RoNW (%)	18.1	27.6	22.3	20.3	18.8

Source: Company; Sharekhan estimates

Double digit growth in IPM over April – August 2021; strong outlook bodes well for IPCA: IPCA's revenues from the domestic markets is sizeable around 40% of the total and so the performance reflects the growth of the IPM (Indian Pharmaceutical markets). After modest 1.6% y-o-y growth for FY2021, IPM growth has bounced back; and for YTD April – August 2021, IPM grew by ~29% y-o-y, largely backed by a low base in the corresponding period of the previous year. A major chunk of IPM growth can be attributed to strong growth in April and May 2021 of ~51.5% and 47.8% y-o-y, respectively. YTD growth is supported by ~17% growth in volumes, while the share of pricing and new products stand at ~6.3% and 6%, respectively. Further, in August 2021, IPM growth normalized to 17.7% with volume, pricing, and new products growth at 9%, 5.9%, and 2.9% y-o-y, respectively. Going ahead, industry reports point that strong pricing growth and share of new products are expected to sustain, which is likely to be complemented by pick-up in volume growth. Moreover, with doctors commencing OPD consultations and elective surgeries likely to increase, patient footfalls are likely to improve leading to a higher prescription, which bodes well. Overall, industry reports indicate that IPM is expected to report a high single digit to double-digit growth in FY2022. This compares with almost flat growth reported in FY2021. This is expected to have a positive rub-off effect on the performance of the companies such as IPCA laboratories.

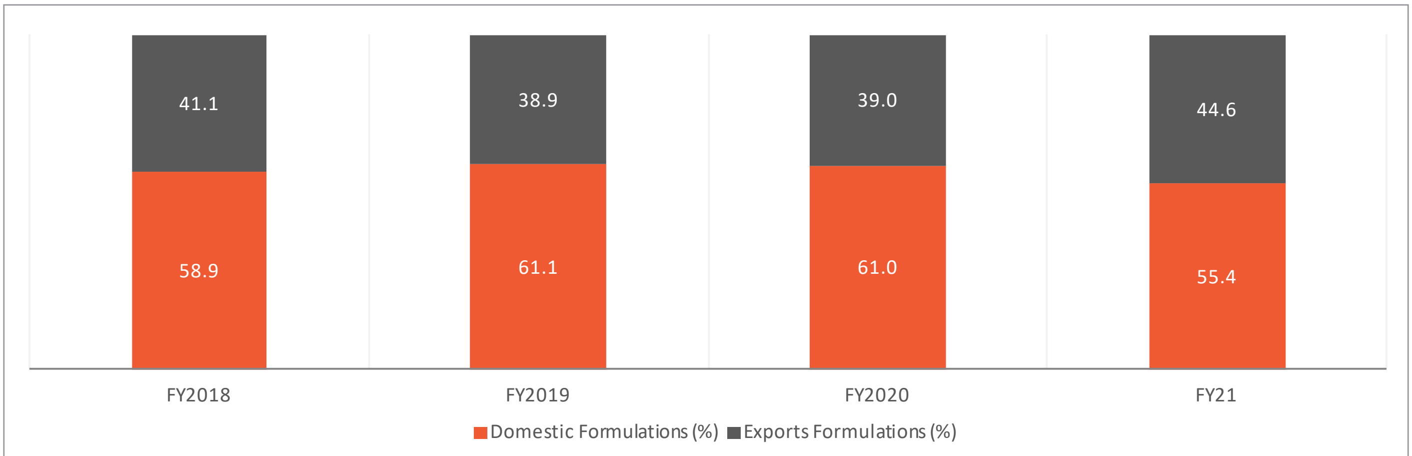
IPM Growth Trends (% y-o-y)



Source: Industry, Sharekhan Research

Domestic formulations on a strong footing to clock a double digit growth: Ipca is largely a formulations player and derives around 70% of revenues (FY2021) from the formulations segment. The balance is constituted by the API segment. In the formulations segment Ipca caters to the domestic as well as exports markets, with the domestic business constituting around 55% of the total formulations sales. The balance, is derived from the exports markets. The revenue mix of the formulations segment is largely constant thus pointing at the leading position in the Indian markets.

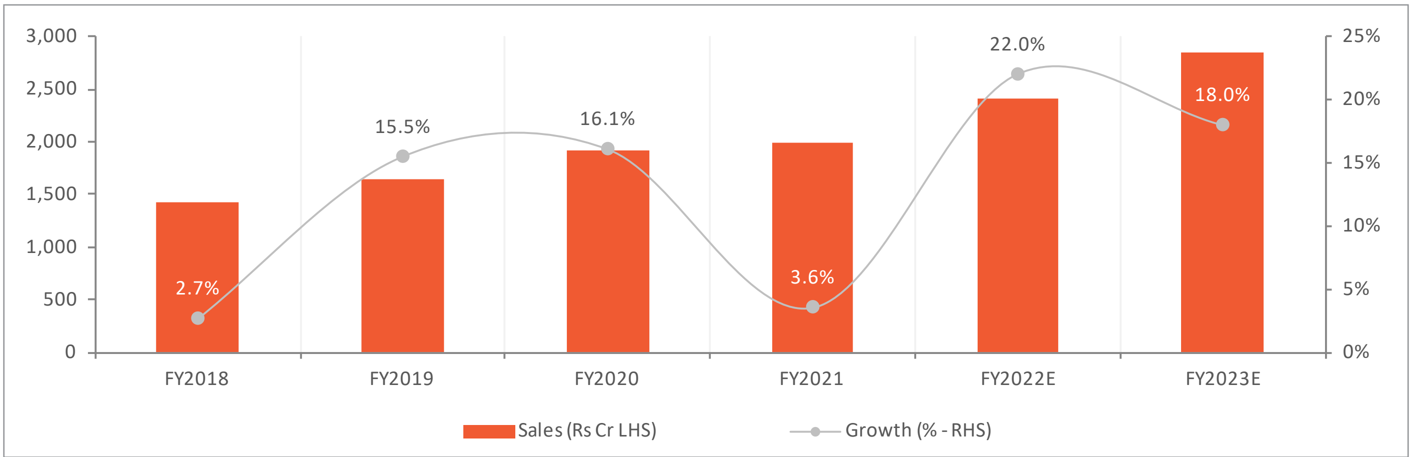
Formulations Segment - Sales Mix



Source: Industry, Sharekhan Research

Going ahead, the management expects the formulations segment to be a key growth driver for the company in FY2022, largely driven by strong growth in the India formulations segment. In FY2021, the India formulations business had a one-time incremental business due to HCQS sales on account of COVID-led higher demand; and despite this, Ipca has guided for 16-18% revenue growth from the domestic formulations business for FY2022. To pass on the higher cost pressures, the company has been able to successfully implement a price hike of 6% in the quarter ending June 2021, thus pointing at its strong position. In Indian markets, the company has a strong presence in the pain/analgesics, gastrointestinal segments followed by cardiology. For the period April to August the Pain / analgesic segment has grown by ~ 35% yoy, while the gastro intestinal segment has staged a growth of 33% over the same period. The cardiac segment has also staged a double digit growth of 15%. One of its strong brands, Zerodol (pain management) has reported 30% growth in Q1FY2022 and is expected to sustain the strong growth trajectory. In domestic markets, a likely pick-up in therapies such as pain management, cardiac, neuro, and derma would drive growth, while anti-malarial, cough, and cold segments would catch up gradually. For the recent three months of June July and August IPCA has outperformed the growth of the IPM staging a 22%. 24% and 39% YoY growth and the overall, the domestic business is expected to stage double-digit growth for FY2022.

Domestic Formulations - Sales trends

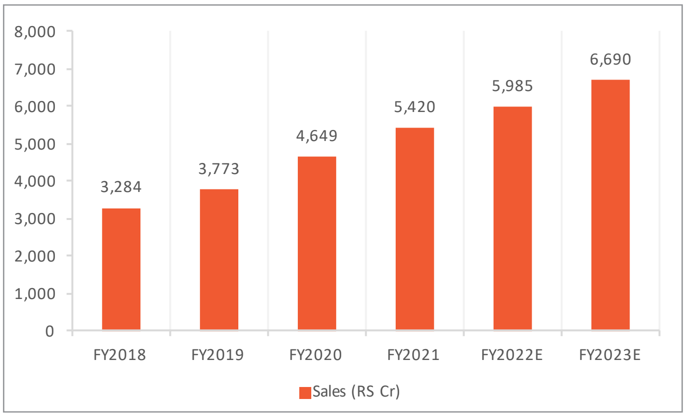


Source: Industry, Sharekhan Research

Ratlam expansion to be ready in 2HFY22; while covid delays Dewas greenfield: Ipca is expanding its API facilities at Dewas as it looks to reduce dependence on others for APIs and intermediaries. The company is setting up a new Greenfield plant at Dewas at an outlay of Rs. 300 crore-350 crore. The company has commenced civil work for the plant, but due to COVID-led delays, the work is progressing at a slower-than-expected pace, leading to delay of three months as per the schedule. Consequently, the Dewas plant is expected to be ready in FY2023; and post this, the plant would undergo inspections for regulators before the company starts API exports from the plant. In addition to Dewas, Ipca is in the process of setting up a small API plant at its Ratlam facility, which is likely to be ready in Q3FY2022 and is likely to contribute to Q4FY2022 topline. Overall, the company expects to incur capex of Rs. 400 crore over the next 2-3 years and this provides comfort on future growth prospects.

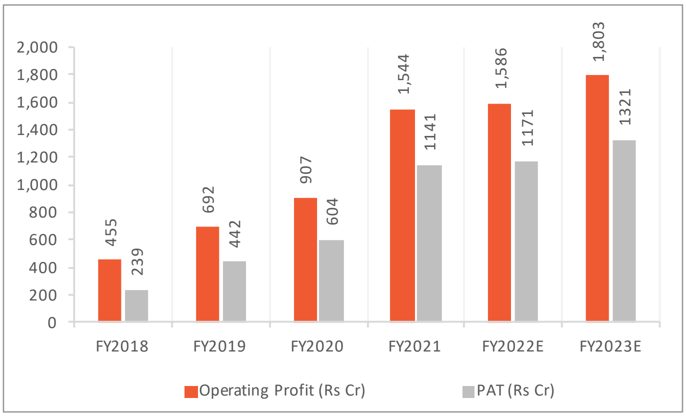
Financials in charts

Sales Trends



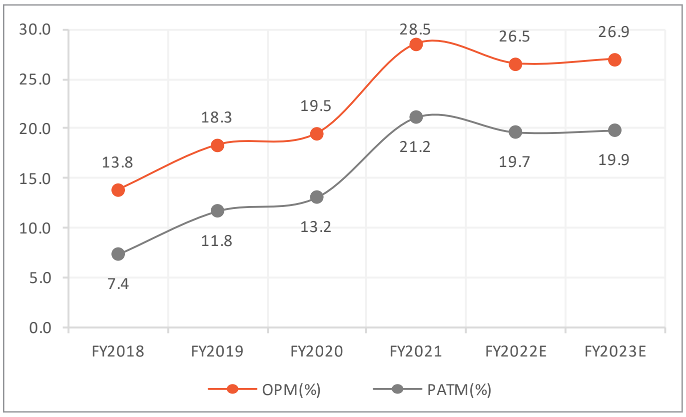
Source: Company, Sharekhan Research

Operating Profit - PAT Trends



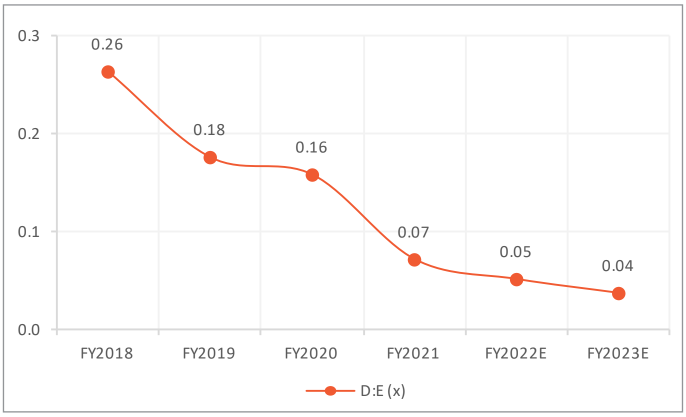
Source: Company, Sharekhan Research

Margin Trends



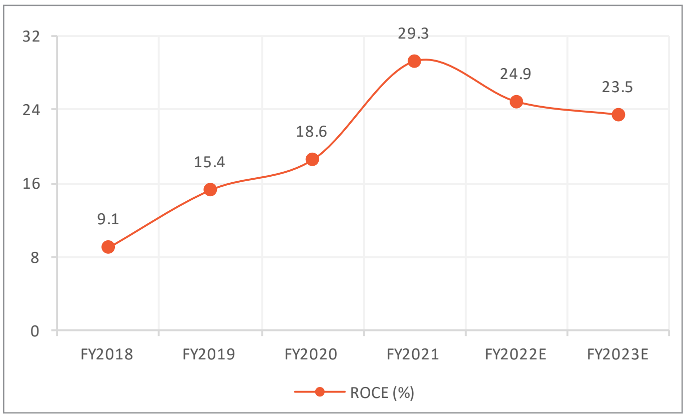
Source: Company, Sharekhan Research

Improving Leverage (D:E)



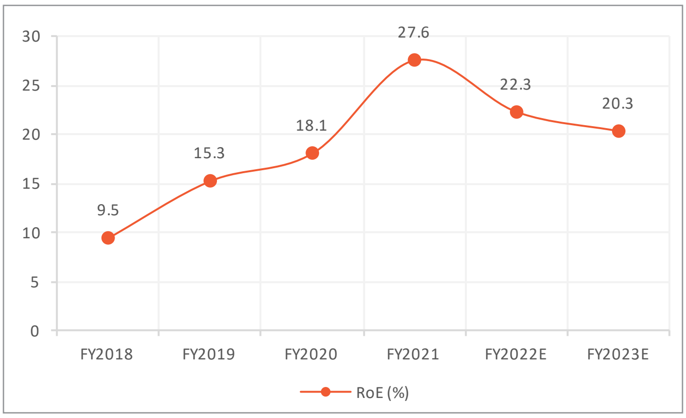
Source: Company, Sharekhan Research

RoCE Trend (%)



Source: Company, Sharekhan Research

RoE (%) Trends



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector View – Growth momentum to improve

Indian pharmaceutical companies are better placed to harness opportunities and report healthy growth going ahead. Indian companies are among the most competitive ones globally and hold a sizeable market share in most developed as well as other markets. Moreover, other factors such as easing of pricing pressures (especially in the US generics market), rise in product approvals, plant resolutions by the USFDA, strong growth prospects in domestic markets, and emerging opportunities in the API space would be key growth drivers. This would be complemented by strong capabilities developed by Indian companies (leading to a shift towards complex molecules and biosimilars) and commissioning of expanded capacities by select players over the medium term. Collectively, this indicates a strong growth potential going ahead for pharma companies.

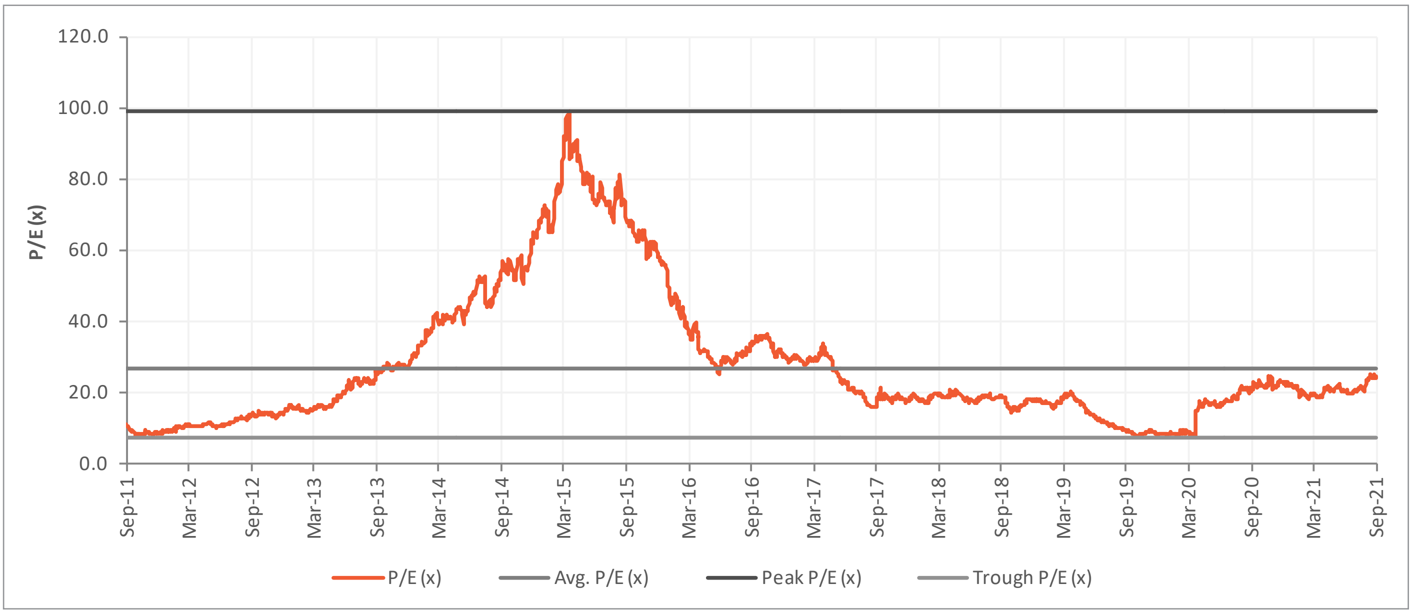
■ Company Outlook – Strong earnings prospects

Ipca is a fully integrated Indian pharmaceutical company, manufacturing more than 350 formulations and 80 APIs for various therapeutic segments. The formulations business is expected to grow at a healthy pace and is likely to be a key growth driver for the company. In the formulations segment, the domestic segment is expected to grow at a healthy pace. There are many growth opportunities ahead for the API segment. The company is witnessing strong demand traction in the API segment and is implementing de-bottlenecking to ease out capacity constraints. This would fuel growth over the next two years, while over the long term, Dewas expansion would come on stream and drive the topline. Moreover, the company is in the process of setting up a new API plant at Ratlam facility with a 50 MT capacity, which is likely to commence operations in FY2022. The expected improvement in the formulation business and increased opportunities in the API space and additional business from the institutional segment indicate strong earnings potential for the company. In the near term, due to capacity constraints and high base in FY2021, the API segment's sales growth is expected to moderate, though long-term growth levers are intact.

■ Valuation – Maintain Buy with a revised PT of Rs. 2,850

Ipca's domestic formulations, which account for ~40% of the company's overall topline, is on a strong footing and the management expects a double-digit growth in FY2022E. The expected strong growth in the IPM, which is expected to stage a high single digit to double digit growth in FY22 and a strong presence in fat growing therapy areas are key growth drivers for the domestic formulations segment. Over the long term, commissioning of Dewas plant and a robust growth outlook for APIs would drive the API segment's performance, though in the near term some moderation in growth could be expected. Further, for the recent three months of June July and August IPCA has outperformed the growth of the IPM staging a 22%. 24% and 39% y-o-ygrowth respectively. Given the strong demand currents in domestic formulations, management is contemplating an upward revision for FY2022 growth guidance, though this could be after Q2FY2022 results. At the CMP, the stock is trading at valuation of 27.2x/24.1x its FY2022E/FY2023E EPS and we have also introduced FY24E EPS in this note. Strong earnings prospects, a sturdy balance sheet, and healthy return ratios augur well for Ipca. We maintain our Buy recommendation on the stock with revised price target (PT) of Rs. 2,850.

One-year forward P/E (x) band



Source: Sharekhan Research

Peer valuation

Particulars	CMP (Rs / Share)	O/S Shares (Cr)	MCAP (Rs Cr)	P/E (x)			EV/EBITDA (x)			RoE (%)		
				FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
IPCA Labs	2,173	12.6	27,555	27.9	27.2	24.1	20.7	19.6	16.7	27.6	22.3	20.3
Torrent Pharma	3106	16.92	52566	42.2	37.6	29.4	23.1	20.6	16.9	23.5	22.0	23.3
Cipla	950.0	80.6	76,596.0	31.9	24.7	19.9	18.3	15.4	12.5	13.9	14.6	16.7

Source: Company, 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-malaria with a market share of over 34% and 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, UK-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 the institutional segment indicate strong earnings potential over the next 2-3 years. We feel most headwinds that impacted the company's sales and profitability (except for import alert from USFDA) are now behind it. Management is also evaluating new therapeutic areas that would boost the company's overall growth. In addition, Ipca is implementing de-bottlenecking plans for its API facilities to ease capacity constraints. Further, Ipca is setting up new API capacities at Dewas and is looking to build the Nobel Expochem plant in to a KSM plant. Collectively, incremental capacities are coming on stream and would fuel growth, though over the long term.

Key Risks

1) Delay in regulatory clearance for two of its plants at Pipariya and Pithampur 2) Addition of drugs in NLEM list could hurt the domestic business.

Additional Data

Key management personnel

Premchand Godha	Chairman and Managing Director
Ajit Kumar Jain	Joint Managing Director
Harish Kamath	Corporate Counsel and Company Secretary

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Chandurkar Investments Pvt Ltd	5.52
2	DSP Investment Managers Pvt Ltd	4.41
3	Paschim Chemicals Pvt Ltd	3.98
4	HDFC Asset Management Co Ltd	3.63
5	L&T Mutual Fund Trustee Ltd/India	3.26
6	Lavender Investments Ltd	2.88
7	UTI Asset Management Co Ltd	2.04
8	Axis asset Management Co Ltd	1.7
9	IDFC Mutual Fund	1.31
10	Canara Robeco Asset Management Company	1.14

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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