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Investor's Delight

31st December, 2010

Company	IPCA Labs Ltd.
BSE Code	524494
FV	Rs.2
Equity Capital (Rs in mn)	250
Reserves (Rs in mn)	8,398
Market Capitalization (Rs in mn)	43,320
CMP	Rs. 345
Target Price	Rs. 400
Upside	15.9%

A) About the company

Background

Incorporated in 1949, IPCA is a fully integrated pharmaceutical company engaged in producing Branded and Generic formulations, APIs etc. It has over 1,000 formulations registered in 38 countries and 32 (APIs), across therapeutic segments: Anti-malarials, Anti-emetics, Antibiotics, Analgesics, Anti-arthritics, Anti-diabetics, Cardiac Care, Cough and Cold therapy, Dermatology and Neuropsychiatry segments.

With over 20 years of experience in the Anti-malarial and Antihypertensive therapeutic segments, it has been leading in the domestic APIs and Drug Intermediaries (DIs) market. The company is one of the biggest manufacturers in the world of APIs Atenolol (Antihypertensive), Chloroquine Phosphate (Anti-malarial), Furosemide (Diuretic) and Pyrantel Salts (Anthelmintic) and one of the largest suppliers of these APIs and their intermediates world over.

Manufacturing facilities

The company has six formulation plants – two each at Silvassa and Madhya Pradesh (MP), one each at Gujarat and Uttaranchal. It has recently completed Indore SEZ plant at MP.

B) Investment Rationale

1) **Strong domestic formulation business:** This space contributes ~80-83% of the total sales. In the domestic business, the company has been successful in changing its business focus from low margin anti-malaria segment to high margin chronic and lifestyle segments. In FY10, it introduced eight new products in the domestic market. Historically, new products introduced in the last five years have constituted ~15% of sales. As per management, domestic formulation business is expected to witness a CAGR of 18% over the next two years.

2) **Expansion plans in place:** The company is facing capacity constraints for export markets as most of its plants are operating at over 90% of capacities. It recently modified its USFDA approved formulation plant at Silvassa. The company has planned a capex of Rs.2 bn for Sikkim, Ratlam plant and routine capex of Rs. ~1.5 bn for FY12E. To cater the US markets, the company has invested ~Rs. 1.5 bn to setup a new plant at Indore SEZ.

3) **Indore SEZ approval to act as a key trigger:** The company expects UKMHRA approval to be received by Q3FY11 as the inspection of the same was done in Q2FY11. USFDA inspection is expected in Feb-Mar 2011 which would act as a key trigger to the stock.

4) **Exports to drive growth:** Currently, the company exports to 110 countries. Exports accounted for 52% of total Revenue. Revenue from exports has clocked a CAGR of 22.6% over FY08-10. Going forward, we expect exports to register a CAGR of 18% over FY10-12E on the back of scale up in its US business, branded formulation exports to emerging economies and revival in UK operations.

C) Outlook and Valuation: The company witnessed revenue CAGR of 22% over the period FY08-10. We expect revenue CAGR of 18% over the period FY10-12E which translates into an EPS of Rs.28.4 for FY12E. As on Q2FY11, the company had healthy OPM of 20.8% and PAT margin of 18.3%.

At CMP, the stock currently trades at a P/E of 12.1x at estimated FY12EPS. We believe that the company is well placed to tap the opportunity presented by US generics market and is strongly placed in domestic formulations business. With due consideration to factors like a) strong presence in domestic formulation business, b) expected USFDA inspection for Indore SEZ plant by fiscal end, we recommend a 'BUY' with a target price of Rs.400 (14x at estimated FY12 EPS) for investors with a six months horizon.

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