

Focus on Pharma

We had an interaction with the management of IOL Chemicals & Pharmaceuticals (IOLCP), a pharmaceutical and speciality organic chemical company. In the past, the company has embarked upon various capacity expansions, product diversification, and cost cutting measures and de-bottlenecking projects. This has helped it diversify its product portfolio, integrate backward, achieve scale in bulk chemicals and enter into bulk drugs. The USFDA nod in July 2015 for its Ibuprofen manufacturing plant will facilitate the company's expansion into the US market. The US expansion coupled with its penetration into untapped and potential markets, we believe, should increase Pharma's share in the total revenue to ~65% in next couple of years. During the same period, the company intends to take the capacity utilization of this segment to about 90% levels, which will lead to expansion in margin to ~22-23% levels.

In the speciality organic chemical space, IOLCP produces Ethyl Acetate, IBB, MCA and Acetyl Chloride. The company is constantly working on making this business profitable. It's developing various products, striving hard to increase utilization levels and expanding its reach to other industries. This all-round effort has added big MNC giants to its customer portfolio. The margin for this business has improved from -29% in FY15 to -1.7% in Q1 FY17, which is further expected to rise to 11-12% in next two years. Management has guided an overall top line growth of ~30% CAGR over FY16-18E, on account of increased capacity utilisation. The company has a stretched balance sheet with D/E ratio of 2.4x and significant debt of Rs.4.4bn as of FY16. Although, management reckons that Debt would be more or less at similar levels, Interest as a percentage of revenues is expected to come down from current 10.6% to 7% by FY18.

Analyst: Ankit Tikmany, Rahul Jain

CMP (Rs) 132 Not rated

Stock data

Sensex:	27,942
52 Week h/l (Rs):	156 / 57
Market cap (Rs mn) :	7,433
Enterprise value (Rs mn):	11,402
6m Avg t/o (Rs mn):	7.6

Prices as on October 28, 2016

Company rating grid

	Low ← → High				
	1	2	3	4	5
Earnings Growth				4	
Cash Flow			3		
B/S Strength		2			
Valuation appeal			3		
Risk			2		

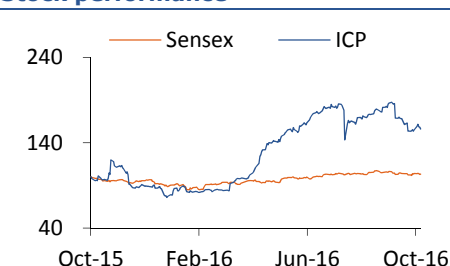
Shareholding pattern (%)

Promoter	39.9
FII+DII	0.2
Others	59.9

Sector: Pharmaceuticals

Bloomberg code:	ICP IB
BSE code:	524164
NSE code:	IOLCP
FV (Rs):	10
Div yield (%):	-

Stock performance



	1M	3M	1Y
Absolute return (%)	(14.0)	(13.9)	59.8

Financial summary

Y/e 31 Mar (Rs mn)	FY12	FY13	FY14	FY15	FY16
Revenues	4,707	4,815	5,635	3,847	5,804
yoy growth (%)	20.9	2.3	17.0	(31.7)	50.9
OPM (%)	14.6	18.5	17.0	2.9	8.9
Reported PAT	48	16	33	(666)	(400)
yoy growth (%)	(23.1)	(66.6)	107.8	(2,119.6)	(39.9)
EPS (Rs)	1.5	0.5	0.7	(14.0)	(7.1)
P/E (x)	85.5	259.4	195.7	-	-
Price/Book (x)	2.3	2.4	3.1	3.0	4.0
EV/EBITDA (x)	10.9	6.7	7.7	90.1	22.8
Debt/Equity (x)	2.0	2.2	1.5	1.9	2.4
RoE (%)	2.7	0.9	1.7	(32.0)	(20.4)

Source: Company, IIFL Research

Pharma Vertical

Over the years, IOLCP has established itself as a major player in Ibuprofen (total installed capacity- 6200 TPA) with 17% of the global capacity. It's the world's only backward-integrated Ibuprofen producer, manufacturing all intermediates stages and key starting materials at one location. The company has augmented its Pharma business by moving up the value-chain with entry into lifestyle drugs for pain management, anti-depressant, anti-diabetic, anti-platelet & anti-convulsion etc. It has presence in 56 countries and it regularly supplies products to major pharmaceutical players like Sanofi Aventis (India and Hungary), Aristo Pharmaceuticals, PratiDonaduzzi E Cia Ltda (Brazil), Cipla, BASF (USA), United Phosphorus, Abbot India and ZIBO XINUA-Perrigo Pharmaceutical (China) etc. IOLCP has recently received USFDA and EDQM certification for the Ibuprofen plant, which is the largest Ibuprofen plant by capacity. Ibuprofen contributes 85% of the total revenue of Pharma division.

Expanding into US market would be the key to future growth

IOLCP is exploring opportunities by diversifying its APIs product portfolio. This will bring in efficiencies in manufacturing processes and systems as also strengthen its relationships with major pharmaceutical generic companies in India and globally. IOLCP currently exports to Latin America, Africa, Europe, Korea, South America, Commonwealth of Independent States (CIS) countries and the Middle East. IOLCP have received USFDA nod in July 2015 for its Ibuprofen manufacturing plant. It intends to make the most of USFDA and EDQM certification and plans to take the capacity utilization above 90% levels in next 2 years. This will also facilitate the company to expand into US market, which is going to be a key driver for its future growth.

Table 1: Presence in life maintenance drug segment

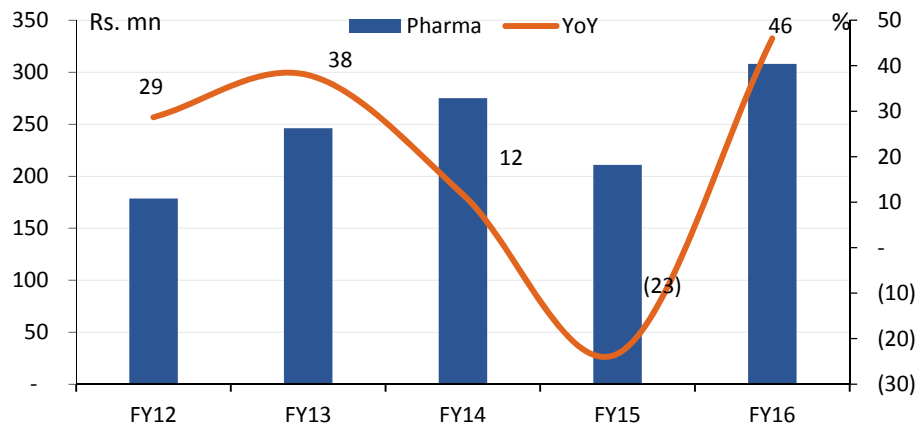
Products	Uses	Therapy segments
Ibuprofen	Pain management	Anti – Inflammatory
Clopidogrel	It is used to inhibit blood clots in a variety of conditions such as peripheral vascular disease, coronary artery disease, and cerebrovascular disease	Anti-platelet
Fenofibrate	Reduce cholesterol levels in patients at risk of cardiovascular disease	Cardiovascular
Lamotrigine	Treatment of partial seizures (Fits).	Anti – Convulsant
Metformin HCl	Used to improve blood sugar control in people with type 2 diabetes	Anti- Diabetes

Source: Company, IIFL Research

Focus on export market and increase in utilization levels to augur well for the segment

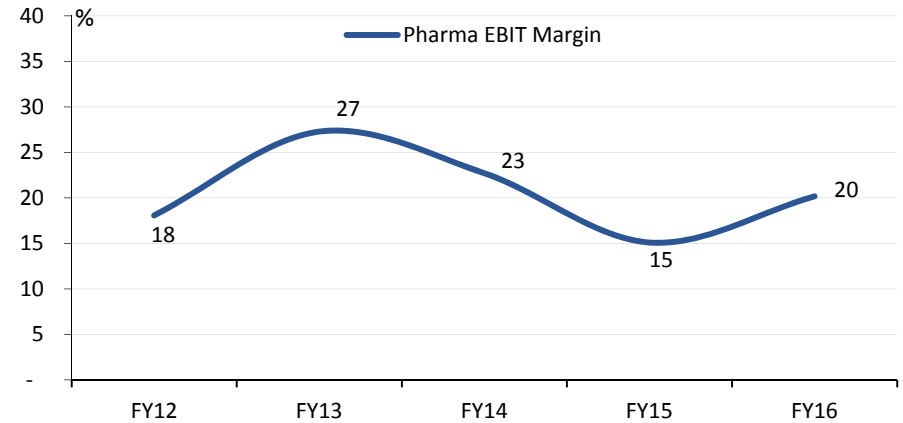
Over FY12-16, pharma business has reported revenue CAGR of 14.6%. Its share to the total revenue has expanded from 37.9% in FY12 to 53.1% in FY16, owing to increased focus on this business. With entry into US market and penetrating into untapped and potential markets of the world, we feel that Pharma's share to the total revenue would increase to ~65% in next couple of years. Margin from this segment had a moderate increase from 18.1% in FY11 to 20.2% in FY16. Management has guided the margin to be at the level of ~22-23% in the next couple of years owing to increase in utilization levels.

Chart 1. Pharma business over FY12-16



Source: Company, IIFL Research

Chart 2. Margin trend over FY12-16



Source: Company, IIFL Research

Other management comments on pharma segment

- Management commented that multipurpose plant that started in 2013 for API's, is flexible between different products. It provides significant opportunity that could be achieved in the next couple of years.
- IOLCP provides immediate access to Indian Pharmaceutical market for global pharmaceutical majors. Products are sold primarily to Branded Generic formulators.

Chemical Vertical

IOLCP is among the major manufacturers in the speciality organic chemical. The company has one of the largest producers of Ethyl Acetate in India and is the 2nd largest producer of Iso Butyl Benzene (IBB) in India with 30% global share. It has forward-integrated this vertical to the pharma segment with end products such as Ethyl Acetate, IBB, MCA and Acetyl Chloride used as key raw material for Ibuprofen. Chemical segment is majorly focused onto the pharmaceutical sector; however IOLCP is also looking to explore its presence in other industries such as paints, flexible packaging and glass. In line with this approach, the company has successfully added MNC giants to its customer base.

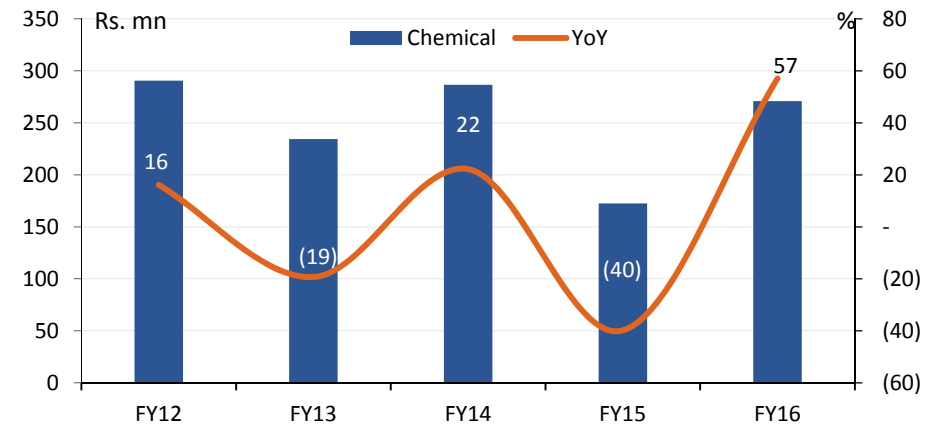
Table 2: Production capacities

Product segment	Capacity (TPA)
Ethyl Acetate	87,000
Iso Butyl Benzene (IBB)	9,000
MCA	7,200
Acetyl Chloride	5,200

Source: Company, IIFL Research

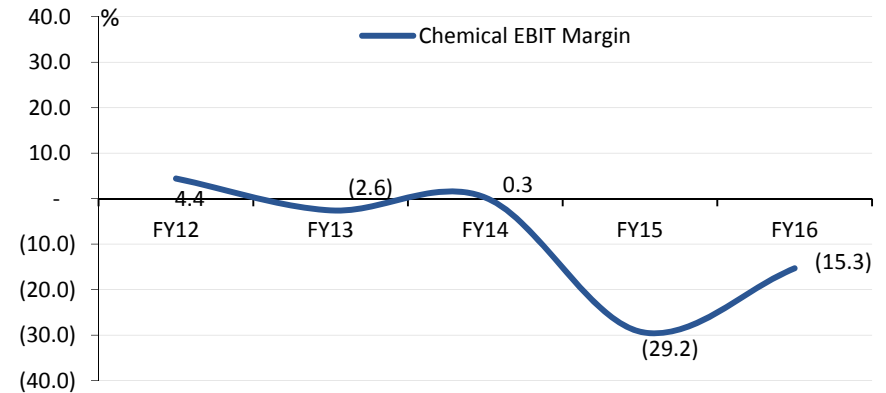
Over FY12-16, chemical segment has witnessed 1.7% de-growth in its revenue from Rs.290mn in FY12 to Rs.271mn in FY16. Its share to the total revenue has significantly come down from 61.7% in FY12 to 46.7% in FY16. 35% of the division's business comes from export market. During the period FY12-16, margin for this segment has either remained subdued or negative. IOLCP is constantly working on making this business profitable by developing various products and increasing the utilization levels. The margin for this business has improved from -29% in FY15 to -1.7% in Q1 FY17. The company has guided to touch 11-12% margin for this vertical in next two years.

Chart 3. Chemical business over FY12-16



Source: Company, IIFL Research

Chart 4. Margin trend over FY12-16

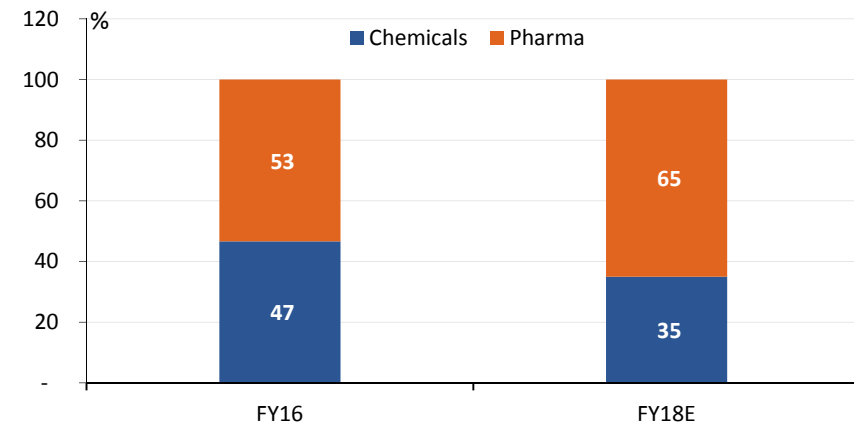


Source: Company, IIFL Research

Financials

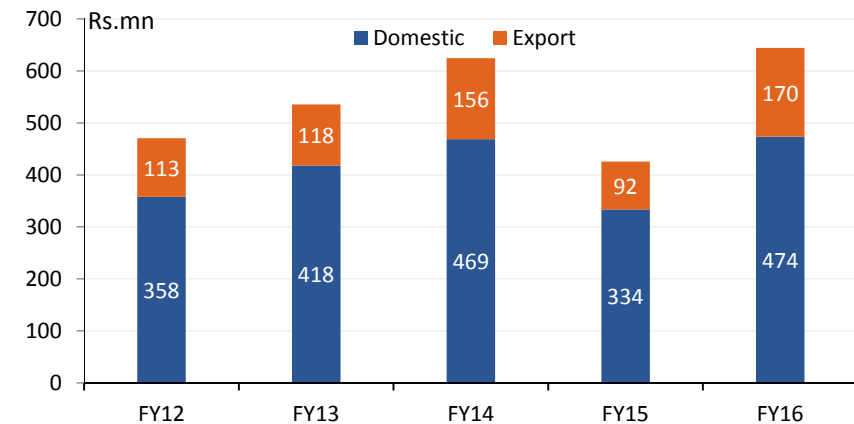
During FY16, the top line of the company increased from Rs.3,847mn to Rs.5,804mn, representing 51% yoy growth. Over FY12-16, it has reported a moderate growth in revenue of 5.4%. The company has guided for a top line growth of ~30% CAGR over FY16-18E, largely on account of increased focus on its Pharma division. Recent (July 2015) approval from USFDA for Ibuprofen manufacturing facilities will enable IOLCP to enter into the United States thereby leading to next leg of growth. Pharma division's contribution to the total top line is expected to rise from 53% in 2016 to 65% by FY18E. During FY12-16, overall EBITDA margins have been under pressure i.e. it contracted from 14.6% in FY12 to 8.9% in FY16. Management has guided for 22-23% EBITDA margins in Pharma segment and 11-12% in chemical segment for next 2 years. Blended EBITDA could touch 18-19% over the same period. IOLCP has been incurring losses from the last two years. Loss in FY15 stood at Rs.666mn and loss in FY16 reduced to Rs.400mn. From the last two quarters, the company has been making profits and the management has commented that the forthcoming quarters would see incremental profits taking the base as Q1FY16. The company has a stretched balance sheet with D/E ratio of 2.4x and debt of Rs.4.4bn as of FY16 which is quite significant. Management has guided that debt will remain more or less at Rs.4.5bn levels, however, D/E ratio should come down on account of expected profitability in next 2 years. Also interest cost as a percentage of sales should come down from 10.6% to 7% by FY18E. No major CAPEX is expected in next 2 years, just operational CAPEX would be incurred.

Chart 5. Pharma share to total revenue expand to 65%



Source: Company, IIFL Research

Chart 6. Geographical trend over FY12-16



Source: Company, IIFL Research

Financials

Balance sheet

Y/e 31 Mar (Rs m)	FY12	FY13	FY14	FY15	FY16
Equity capital	307	312	488	477	562
Reserves	1,429	1,418	1,604	1,595	1,289
Net worth	1,736	1,730	2,093	2,072	1,851
Other LT Liabilities	40	284	340	81	38
LT provision.	1	1	3	3	12
Borrowing	3,512	3,840	3,130	3,975	4,390
Deferred tax liab (net)	93	104	121	4	-
Total liabilities	5,382	5,959	5,687	6,135	6,291
Fixed assets	4,744	4,619	4,437	4,070	4,038
Investments	-	-	-	0.4	0.3
Other Non-current Asset	133	140	167	111	118
Net working capital	418	(828)	(1,117)	1,827	2,015
Current Assets					
Inventories	1,318	358	493	2,134	2,279
Sundry debtors	216	124	114	327	906
ST. Loans & advances	372	-	-	247	297
Cash	87	2,028	2,200	127	120
Current Liabilities					
Sundry creditors	(794)	(954)	(1,134)	(702)	(1,166)
Other current liabilities	(693)	(355)	(586)	(178)	(300)
Provision	(1)	(2)	(5)	(0)	(1)
Total assets	5,382	5,959	5,687	6,135	6,291

Income statement

Y/e 31 Mar (Rs m)	FY12	FY13	FY14	FY15	FY16
Revenue	4,707	4,815	5,635	3,847	5,804
Operating profit	686	890	957	113	514
Depreciation & Amortization	(239)	(314)	(316)	(289)	(297)
PBIT	447	577	641	(177)	217
Interest expense	(432)	(572)	(603)	(591)	(615)
Other income	23	25	13	13	12
Profit before tax	38	30	51	(754)	(385)
Taxes	10	(14)	(18)	88	(15)
Reported profit	48	16	33	(666)	(400)
Adj. Net profit	48	16	33	(666)	(400)

Cash flow

Y/e 31 Mar (Rs m)	FY12	FY13	FY14	FY15	FY16
Cash flow from operation					
Profit before tax	38	30	51	(754)	(385)
Depreciation	239	314	316	289	297
Tax paid	10	(14)	(18)	88	(15)
Working capital Δ	7	1,246	289	(2,944)	(188)
Other operating items					
Operating cashflow	294	1,576	638	(3,321)	(291)
Cash flow from Investing Activities					
Capital expenditure	(905)	(189)	(134)	77	(265)
Change in other non curr assets	36	(6)	(27)	57	(7)
Free cash flow	(575)	1,380	477	(3,188)	(563)
Cash flow from Financing activities					
Equity raised	(35)	(22)	330	646	180
Investments	-	-	-	(0.4)	0.1
Debt financing/disposal	529	328	(710)	846	414
Dividends paid	-	-	-	-	-
Other items	(13)	255	76	(377)	(38)
Net Δ in cash	(94)	1,941	172	(2,073)	(7)

Ratio analysis

Y/e 31 Mar (Rs m)	FY12	FY13	FY14	FY15	FY16
Growth matrix (%)					
Revenue growth	20.9	2.3	17.0	(31.7)	50.9
Op profit growth	1.3	29.8	7.5	(88.2)	356.2
EBIT growth	2.5	28.1	8.7	(125.0)	(240.3)
PBT growth	(58.0)	(22.1)	71.8	(1,584.3)	(48.9)
EPS growth	(23.1)	(67.1)	32.6	(2,169.1)	(49.1)
Profitability ratios (%)					
OPM	14.6	18.5	17.0	2.9	8.9
EBIT margin	10.0	12.5	11.6	(4.2)	3.9
Net profit margin	1.0	0.3	0.6	(17.3)	(6.9)
RoCE	9.2	10.6	11.2	(2.8)	3.7
RoNW	2.7	0.9	1.7	(32.0)	(20.4)
RoA	0.7	0.2	0.4	(9.2)	(5.4)
Per share ratios (Rs)					
EPS	1.5	0.5	0.7	(14.0)	(7.1)
Dividend per share	-	-	-	-	-
Cash EPS	9.3	10.6	7.2	(7.9)	(1.8)
Book value per share	56.5	55.5	42.9	43.5	32.9
Payout (%)					
Dividend payout	-	-	-	-	-
Tax payout	(25.2)	46.3	35.1	11.7	(3.8)
Liquidity ratios					
Debtor days	16.7	9.4	7.4	31.0	57.0
Inventory days	102.2	27.2	31.9	202.5	143.3
Creditor days	61.6	72.3	73.4	66.6	73.3
Leverage ratios (x)					
Interest coverage	1.1	1.1	1.1	(0.3)	0.4
Net debt / equity	2.0	1.0	0.4	1.9	2.3
Net debt / op. profit	5.1	4.3	1.0	34.2	8.3

Y/e 31 Mar (Rs m)	FY12	FY13	FY14	FY15	FY16
Valuation ratios (x)					
P/E	85.5	259.4	195.7	-	-
P/BV	2.3	2.4	3.1	3.0	4.0
EV/EBITDA	10.9	6.7	7.7	90.1	22.8
Net Cash Equiv./Mcap (x)	(0.8)	(0.4)	(0.1)	(0.6)	(0.6)
Dividend Yield	-	-	-	-	-
MCAP/Sales (x)	0.9	0.9	1.1	1.6	1.3
Component ratios (%)					
Raw material	63.7	62.3	65.6	72.6	71.3
Staff cost	4.3	4.6	4.8	6.4	6.1
Other operating exp	17.4	14.6	12.6	18.1	13.8

Du-Pont Analysis

Y/e 31 Mar (Rs m)	FY12	FY13	FY14	FY15	FY16
Tax burden (x)	1.3	0.5	0.6	0.9	1.0
Interest burden (x)	0.1	0.0	0.1	4.6	(1.7)
EBIT margin (x)	0.1	0.1	0.1	(0.0)	0.0
Asset turnover (x)	0.7	0.7	0.8	0.5	0.8
Financial leverage (x)	3.7	4.1	3.8	3.5	3.8
RoE (%)	2.7	0.9	1.7	(32.0)	(20.4)

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Prayesh Jain was conferred the Best Analyst Award for Auto sector and **Bhavesh Gandhi** bagged the Best Analyst Award for Pharma sector.

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Accumulate = 5% to 15%

Reduce = -10% to 5%

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