

IPO Note: Syngene International Ltd.

Industry: Contract Research (CRO)
Recommendation: Subscribe
Date: July 20, 2015

Issue Snapshot

Company Name	Syngene International Ltd.
Issue Opens	July 27, 2015 to July 29, 2015
Price Band	Rs. 240 to Rs. 250
Bid Lot	60 Equity Shares and in multiples of 60 Equity Shares thereafter.
The Offer	Public issue of 22,000,000 Equity shares of Face value Rs.10 each, (Comprising of Offer for Sale of 22,000,000 Equity Shares by Selling Shareholder (Biocon Ltd.).
Issue Size	Rs. 528 - 550 Crore
IPO Process	100% Book Building
Face Value	Rs. 10.00
IPO Grading	NA
Exchanges	NSE & BSE
BRLM	Axis Capital Limited, Credit Suisse Securities (India) Private Limited, Jefferies India Private Limited
Registrar	Karvy Computershare Private Limited

Equity Shares offered through this Offer

	Nos. of Share	As a % of total
Equity Shares offered through this Offer	20000000	100.0%
A. Fresh Issue	0	
B. Offer for Sale	22000000	
Less: Biocon Shareholders Reservation Portion	2000000	
I. QIB Portion (Not more than)	10000000	50.0%
- Anchor Investor Portion		
- Mutual Funds only (5% of the QIB Portion)		
- QIBs including Mutual Funds		
II. Non-Institutional Portion (Not less than)	3000000	15.0%
III. Retail Portion (Not less than)	7000000	35.0%

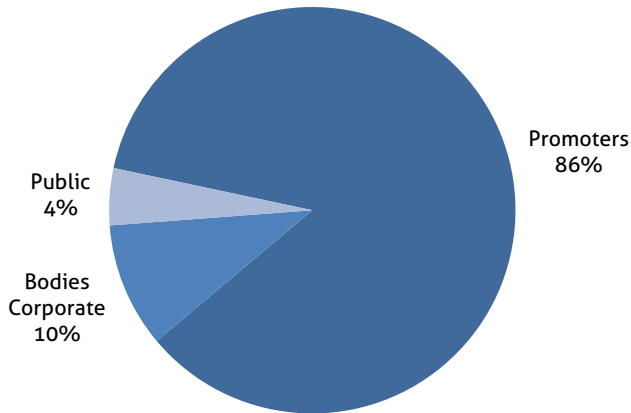
Pre and post Issue Equity Shares

	Nos. of Share
Equity Shares outstanding prior to the Issue	20,000,000
Equity Shares outstanding after the Issue	20,000,000

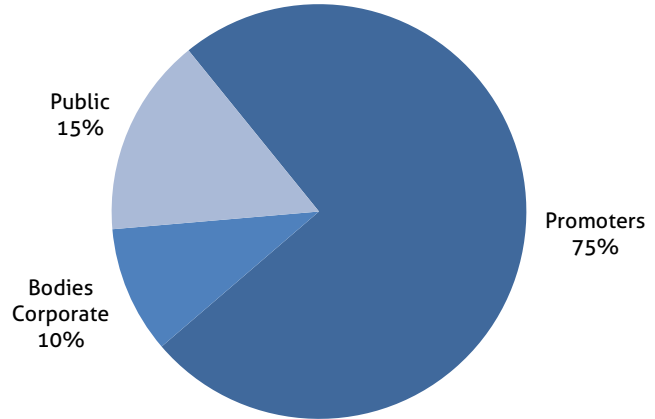
Objects of the Offer

The objects of the Offer are to achieve the benefits of listing the Equity Shares on the Stock Exchanges and for the sale of 22,000,000 Equity Shares by the Selling Shareholder (Biocon Ltd.). Further, the Company expects that the listing of the Equity Shares will enhance the visibility and brand image among existing and potential clients and provide liquidity to the existing shareholders. The Company will not receive any proceeds of the Offer and all the proceeds will go to the Selling Shareholder.

Pre-Issue



Post-Issue



Background

Company

Incorporated in 1993, Syngene International Limited is a subsidiary of Biocon Limited ("Biocon"), a global biopharmaceutical enterprise focused on delivering affordable formulations and compounds. Biocon has been listed on the Indian stock exchanges since 2004 and as of May 31, 2015 had a market cap of Rs.90.3 billion on the BSE as well as the NSE. Over the years, Biocon has successfully brought to the market several affordable and alternative therapeutic drugs in the areas of diabetes, oncology and autoimmune diseases. Biocon is currently focused on bringing its portfolio of generic insulins and bio-similar monoclonal antibodies to global markets.

Promoters

Smt. Kiran Mazumdar Shaw is the Managing Director of the Company. She is also the Chairperson and Managing Director of Biocon. She is a first generation entrepreneur with more than 39 years of experience in the field of biotechnology. Shri Peter Bains is a Director and Chief Executive Officer of the Company and has almost three decades of experience in the global pharmaceutical space. He is responsible for the daily operations and takes strategic decisions for the Company. Shri Manoj Nerurkar is the Chief Operating Officer of the Company. He has over 19 years of experience in pharmaceutical industry. Shri MB Chinappa is the Chief Financial Officer of the Company. He has over 22 years of experience in the field of finance.

About the company

Syngene International Ltd ("Syngene") is one of the leading India-based contract research organisations ("CRO"), offering a suite of integrated, end-to-end discovery and development services for novel molecular entities ("NMEs") across industrial sectors including pharmaceutical, biotechnology, agrochemicals, consumer health, animal health, cosmetic and nutrition companies. Syngene's service offerings in discovery and development cover multiple domains across small molecules, large molecules, antibody-drug conjugates ("ADC") and oligonucleotides. Their integrated discovery and development platforms help organisations conduct discovery (from hit to candidate selection), development (including pre-clinical and clinical studies, analytical and bio-analytical evaluation, formulation development and stability studies) and pilot manufacturing (scale-up, pre-clinical and clinical supplies) under one roof with a distinctive economic advantage. Company's service offerings also support the development of bio-similar and generic molecules. In the near term, Syngene intend to forward integrate into commercial-scale manufacturing of NMEs.

Outsourcing discovery and development work is an established alternative to in-house development among multinational organisations. While traditionally multinational organisations had looked at outsourcing as a way to reduce their research and development expenditures, the R&D outsourcing industry is evolving from a mere leveraging of cost arbitrage to enhancing R&D productivity and reducing the time to market.

As an experienced CRO with a proven track record of providing quality NME discovery, development and manufacturing services and continued focus on reliability, responsiveness and protection of client's intellectual property, Syngene is well-positioned to benefit from the expected growth in the CRO industry. Company offer an attractive variable cost alternative to the traditionally fixed cost, in-house, resource intensive business model of R&D focused organisations.

Syngene offers services through flexible business models that are customised to their client's requirements. These range from a full-time equivalent ("FTE") to a fee-for-service ("FFS") model, or a combination thereof. During Fiscal 2015, Syngene serviced 221 clients, ranging from multinational corporations to start-ups, including 8 of the top 10 global pharmaceutical companies by sales for 2014. Syngene has several long-term relationships and multi-year contracts with their clients, including three long-duration multidisciplinary partnerships, each with a dedicated research centre, with three of the world's leading global healthcare organisations Bristol-Myers Squibb Co. ("BMS"), Abbott Laboratories (Singapore) Pte. Ltd. ("Abbott") and Baxter International Inc. ("Baxter").

Syngene delivers the services through a combination of scientific talent, globally accredited systems and R&D infrastructure. As of March 31, 2015, it's tangible fixed assets (gross block) were Rs.931.1 Crores. Syngene has laboratory and manufacturing facilities that are spread over more than 900,000 sq. ft. and located in Bengaluru. As of May 31, 2015, Syngene has 2,122 scientists, including 258 Ph.Ds. and 1,665 scientists with a Master's degree.

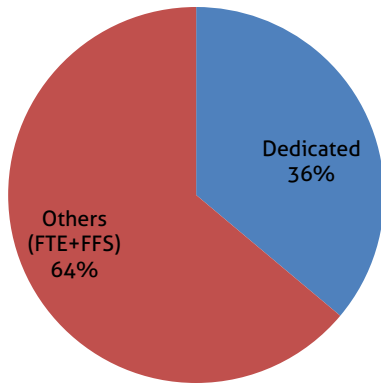
For the Financial Years 2015 and 2014, Syngene generated Total Revenue of Rs. 871.6 Crores and Rs.707.7 Crores, EBITDA of Rs. 292.8 Crores and Rs. 222.6 Crores and Restated profit for Rs. 175 Crores and Rs. 134.8 Crores respectively. For the three fiscal years ended March 31, 2015, the Total Revenue, Restated Profit and EBITDA grew at a CAGR of 27.7%, 35.1% and 28.3% respectively.

Effective April 1, 2014, company's subsidiary Clinigene International Limited ("Clinigene"), through which they have provided the clinical research and clinical trial services, was amalgamated with syngene. Prior to this date, company's results did not include the results of Clinigene.

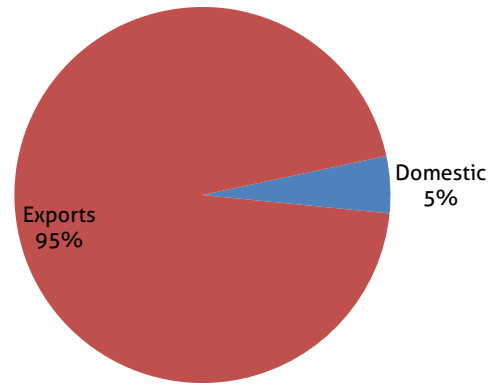
For the fiscal year ended March 31, 2015, Company's revenue from the sale of services was Rs.842.7 Crores. For the fiscal year ended March 31, 2015, company derived 36.1% and 63.9% of their revenue from the sale of services from long-term contracts with dedicated infrastructure and other contracts, respectively. For the fiscal year ended March 31, 2015, they derived 95.1% and 4.9% of the revenue from the sale of services to customers outside India and from customers in India, respectively.

The charts below present the split of the revenue from the sale of services for the fiscal year ended March 31, 2015 between long-term contracts with dedicated infrastructure and other contracts and between customers outside India and customers in India, respectively:

Revenue from sale of services in Fiscal 2015 by contract type



Revenue from sale of services in Fiscal 2015 by geography

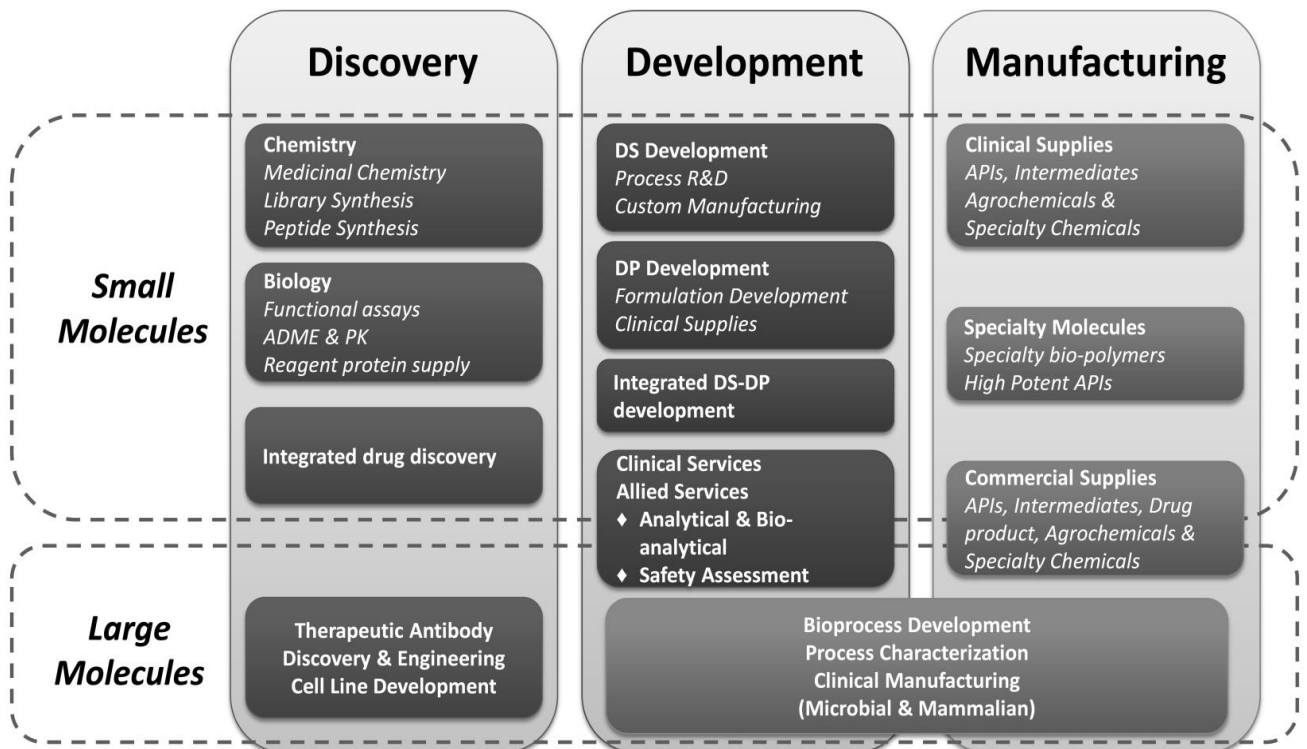


Fully Integrated Services Platform

Syngene's core operations are grouped into the following service platforms:

- Discovery Chemistry
- Discovery Biology
- Chemical Development
- Formulation
- Safety Assessment
- Clinical Services
- Stability Services
- Large Molecule Development
- Manufacturing

The following chart depicts Syngene's comprehensive suite of discovery and development and manufacturing services:



The service offerings initially consisted of simpler discovery chemistry and discovery biology services. As the company established credibility and delivery track record on various technologies, they have expanded their offerings extensively across multiple service platforms in line with the changing requirements of the global pharmaceutical industry. Their clients value the company's ability to offer a wide breadth of quality services to meet their R&D needs, and syngene intend to continue to expand their service offerings in line with the evolving requirements of their clients in the future.

Key Points

World-class infrastructure, systems and processes that comply with quality standards to serve international markets and successful audits by regulatory authorities such as the FDA and EMA

As of March 31, 2015, company's tangible fixed assets (gross block) were Rs.931.1 Crores. Their laboratory and manufacturing facilities are spread over more than 900,000 sq. ft. and are located in Bengaluru. Their infrastructure, along with high standards of regulatory compliance and quality services, provides the sustainable competitive advantage. Syngene operate their laboratory and manufacturing facilities to high standards that are consistent with the requirements of the large global clients. Their research facilities and systems are certified with ISO standards. The pre-clinical research facilities are Good Laboratory Practices ("GLP") certified and accredited by Association for Assessment and Accreditation of Laboratory Animal Care ("AAALAC"). The clinical facilities are GLP compliant, National Accreditation Board for Testing and Calibration Laboratories ("NABL"), College of American Pathologists ("CAP") and Central Drugs Standard Control Organisation ("CDSCO") accredited and have undergone multiple FDA audits. In 2014, they successfully completed an FDA pre-approval inspection of one of their manufacturing facilities. In 2010 and 2013, they also successfully completed EMA audits of their bioanalytical and clinical facilities. In addition to regulatory inspections, their facilities and systems are regularly inspected by their clients.

Talented and qualified pool of scientists and an experienced management

Syngene has an experienced and qualified team of scientists across multiple disciplines. As of May 31, 2015, 90.6% of their scientist pool of 2,122 scientists had a Master's degree or a Ph.D. Their position as an industry leader represents a significant competitive advantage in attracting and retaining high-quality scientists required to successfully execute the innovative business model and to differentiate the service offerings from those of other CROs. They recruit primarily from the large scientific talent pool in India as well as from overseas. For the three fiscal years ended March 31, 2013, March 31, 2014 and March 31, 2015, Syngene has an average attrition rate of 14.3%, which is a low rate for this industry in India.

Integrated service offerings across multiple domains with a proven track-record of successful delivery, reliability, cost efficiency and client satisfaction

Syngene has evolved from being a discovery chemistry and discovery biology-focused CRO to an integrated provider of discovery and development services for NMEs across a range of domains including small molecules, large molecule biologics, ADCs and oligonucleotides. The depth and breadth of their scientific capabilities and service offerings provide them multiple entry points during the life cycle of the clients'

molecules across the discovery and development process. Syngene's broad discovery and development capabilities also enable them to serve a number of industrial sectors beyond the pharmaceutical and biotechnology sectors.

Their operational track record in successful delivery of projects, responsiveness, process innovation, turnaround times, and productivity has facilitated the strengthening of their client base. Over the years, Syngene has built significant credibility and a regulatory track record in various therapeutic platforms and service models. This has helped them to attract a wider range of new clientele as well as deepen the existing client collaborations through successive renewal and expansion of contractual arrangements.

The flexible business models allow company to meet the discovery and development needs of a wide range of clients, from small biotechnology companies to large pharmaceutical companies. Through more than 20 years of experience, Syngene has developed significant expertise managing large integrated collaborations and executing complex projects. In addition, they have been able to take advantage of India's large, low-cost scientific talent pool to deliver their services to multinational companies at competitive rates, especially when compared with costs for comparable services in developed countries.

Attractive and diversified client base with several client collaborations

During fiscal 2015, Syngene has serviced 221 clients including 8 of the top 10 global pharmaceutical companies by sales for 2014. They have longstanding, extensive relationships with multinational clients such as BMS, Baxter, and Merck & Co, as well as emerging small- to mid-sized companies such as Achillion Pharmaceuticals, Inc., Aquinox Pharmaceuticals, Inc. and Saniona AB. Syngene continually strived towards strengthening the client relationships by ensuring that their service offerings keep pace with the clients' requirements. For example, in fiscal 2009, Syngene established a dedicated centre for BMS to support their R&D across multiple disciplines. Over time, this dedicated centre has become their largest R&D presence in Asia with more than 400 scientists. The capabilities and therapeutic focus of this R&D centre have evolved in line with the shift in BMS' R&D strategy. BMS has also recently extended this engagement to 2020. The integrated service offerings coupled with consistent performance and delivery has helped them continuously renew the client engagements as well.

Commitment to protection of the clients' intellectual property and data confidentiality

Protection of intellectual property and data confidentiality is integral to the success of R&D outsourcing. Syngene has made it a strategic priority to safeguard their clients' proprietary rights by using well established and strictly enforced intellectual property protection procedures. They have a zero-tolerance policy for confidentiality breaches and data leakages and implement this policy through a combination of solutions including technology, work-flow and information segregation as well as legal remedies. The entire physical infrastructure is access controlled, with access granted only on a need-to-work basis. Information regarding the projects being undertaken is segregated and shared on a need-to know-basis post discussion with the clients. The physical separation of client projects ensures enhanced security and protection of the clients' intellectual property.

Financial stability and stable cash flows

Discovery and development is an extensive process which builds a composite of information drawn from multiple disciplines. Syngene has the financial stability and steady operational cash flows to enable the extension of the platforms in line with the present and future needs of their clientele. The long term collaborations with certain clients lead to predictable and stable cash flows. Their strong balance sheet and financial performance has helped them in reassuring clients that company will be able to support their NME development with dedicated investments in terms of both capabilities and capacities. Over the years, Syngene has invested in specialised services and equipment and dedicated infrastructure to support these growing needs. Their ability to make these investments helps strengthen trust and engagement with the clients, which enhances their ability to retain client and extend the engagement across multiple platforms.

Company's Strategy going forward

- "Follow the molecule" by providing the clients with integrated services
- Expand capabilities and capacities while enhancing efficiencies in R&D services
- Scale-up the manufacturing capabilities
- Engage, expand and extend client collaborations

Key Concern

- **Client growth:** Growth in sales from existing clients and the acquisition of new clients have been the key drivers of their historical growth, and these factors will remain critical going forward as well.
- **Introducing new drugs:** Pressure to introduce new drugs into the market rapidly with lower development costs.
- **Fluctuations in the exchange rate:** The company derives almost all of the revenue in U.S. dollars and incurs certain costs in U.S. dollars, and hence is exposed to the risks associated with fluctuations in foreign exchange rates which could negatively impact the profitability and financial condition.
- **Material costs:** The company has mixed of FTE contracts and FFS contracts. FFS contracts means fixed-price contracts, so any increases in material costs are generally not billed to the clients. So any increase in material cost could negatively impact the profitability and financial condition

Valuation

Syngene International Ltd, a subsidiary of Indian pharmaceutical major, Biocon, is one of the leading contract research organizations offering a suite of integrated, end-to-end discovery and development services for novel molecular entities ("NMEs") across the sectors including pharmaceutical, biotechnology, agrochemicals, consumer health, animal health, cosmetic and nutrition companies. Over the years, Syngene has earned a global reputation in the area of integrated discovery and development services for novel small molecules and biologics. During the last fiscal year (FY15), the company has serviced 221 clients globally, including 8 of the top 10 global pharmaceutical companies by sales. Syngene contributes about 28% of total Biocon's revenue, thus one of the key revenue drivers for the pharma major. Biocon holds 84% stake in Syngene and post 11% equity sale, the promoter shareholding would reduce to 74%. As the equity offering is through "offer for sale", hence there would be no equity dilution and the EPS would remain intact.

As per Frost & Sullivan estimates, the global R&D expenditure for the pharmaceutical industry in 2014 was pegged at USD 139 billion, of which USD 105 billion could have potentially been outsourced, thus have immense growth opportunities for research and development firm like Syngene. Even IQ4I Research and Consultancy report states that contract research organization for discovery services market was at USD 14.7 billion at 2014 and is expected to grow at whopping 11.5% CAGR by 2018 to reach at USD 22.7 billion. Thus operating in such lucrative sector, Syngene has good long term growth story ahead. Further, Syngene has several long term relationships and multiyear contracts with the clients, thus have strong revenue growth visibility going ahead. Backed by 900,000 sq ft of laboratory as well as manufacturing facility at Bangalore, Syngene is well placed to ride on the growth potential in global pharma research and development segment.

*On financial front, the company has shown exponential growth on all fronts. During the period between FY10-FY15, revenue grew at a CAGR of 26%, while EBITDA has shown a growth of 28% CAGR over the same period. Higher revenue growth and improving operating efficiencies led PAT growth, which witnessed 42% CAGR between FY10-FY15. Apart from strong financial growth, company has also maintained healthy margins over the years and thus helped the company to report strong RoE of 18-20% in past years. Given its healthy financial growth, strong global client base and backing of strong parent Biocon, we believe that the IPO is fairly valued. At the upper price band, the company is valued at P/E multiple of 28x of FY15 earnings. We believe that Syngene has the ability to become a long term wealth creator for the investor and also a value investing from long term perspective. Hence, we suggest our investors to **SUBSCRIBE** the issue.*

Financial Statement

Income Statement

(In Rs. Cr)	FY11	FY12	FY13	FY14	FY15
Revenue from operations	3,219	4,167	5,500	6,995	8,599
Other income	10	15	42	82	117
Total revenue	3,229	4,182	5,542	7,077	8,716
Total expenses	2,229	2,796	3,815	4,851	5,788
Operating Profit	990	1,371	1,685	2,144	2,811
OPM (%)	30.8%	32.9%	30.6%	30.7%	32.7%
Depreciation	515	547	599	656	814
Finance cost	210	102	65	4	79
Tax expense	3	27	42	218	285
Net Profit	272	710	1,021	1,348	1,750

Source: RHP

Asset Liability Statement

(In Rs. Cr)	FY11	FY12	FY13	FY14	FY15
Equity & Liabilities					
Shareholders' funds	2,207	2,968	5,186	6,593	8,449
Share Capital	29	241	261	261	1,991
Reserves and Surplus	2,178	2,727	4,925	6,332	6,458
Non - Current Liabilities	501	696	566	692	1,014
Long -Term Borrowings	-	42	-	-	186
Deferred tax liability (net)	101	82	65	51	49
Other long-term liabilities	388	560	473	583	647
Long-Term Provisions	12	12	28	58	132
Current Liabilities	2,333	2,202	1,490	4,624	4,752
Short- Term Borrowings	1,450	926	-	1,549	1,364
Trade Payables	280	643	827	766	692
Other Current Liabilities	565	566	575	2,212	2,602
Short-Term Provisions	38	67	88	97	94
Total Equity & Liabilities	5,041	5,866	7,242	11,909	14,215
Assets					
Non - Current Assets	4,277	4,487	4,872	5,569	8,357
Tangible Assets	3,876	3,830	3,810	3,941	4,976
Intangible Assets	-	-	-	-	57
CapitalWork-In-Progress	9	108	88	453	1,051
Non - Current Investments	-	1	1	1	-
Long-Term Loans and Advances	392	497	863	1,031	1,142
Other Non-Current Assets	-	51	110	143	1,131
Current Assets	764	1,379	2,370	6,340	5,858
Current investments	26	-	691	3,520	1,460
Inventories	63	149	179	149	384
Trade Receivables	384	434	766	943	1,799
Cash and Bank Balances	59	377	118	916	1,157
Short-Term Loans and Advances	64	74	160	269	338
Other Current Assets	168	345	456	543	720
Total Assets	5,041	5,866	7,242	11,909	14,215

Cash Flow Statement

(In Rs. Cr)	FY11	FY12	FY13	FY14	FY15
Cash flow from Operations Activities	798	1222	1035	2995	185
Cash flow from Investing Activities	(184)	(226)	(1501)	(3742)	120
Cash flow from Financing Activities	(621)	(699)	207	1554	(101)
Net increase/(decrease) in cash and cash equivalents	(7)	297	(259)	807	204
Cash and cash equivalents at the beginning of the year	66	59	377	118	916
Cash and cash equivalents at the end of the year	59	377	118	916	1157

Source: RHP

Ratios

	FY11	FY12	FY13	FY14	FY15
Earning per share (EPS) (Rs.)	1.4	3.6	5.8	7.0	8.9
Net Asset Value per share (Rs.)	13.0	17.3	27.8	35.4	43.7
Return on Net Worth (RONW) (%)	12.3	23.9	19.7	20.5	20.7

Source: RHP

Peer Comparison

There are no listed entities in India which are similar to the line of business and comparable to the scale of operations.

Disclosure

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