

INC Research Holdings, Inc.:

INCR: Off to a Strong Start

KeyBanc Capital Markets Inc.
 Member NYSE/FINRA/SIPC

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Rating	HOLD
Price	\$25.99
12- Mo. Price Target	NA
Dividend	\$0.00
Dividend Yield	0.0%
52- Wk. Range	\$20 - \$29
Trading Volume (000)	144
Market Cap. (M)	\$1,590.6
Shares Out. (M)	61.20
Book Value/Share	\$7.32

EPS (Net) Summary

FY Dec	2014A	2015E	2016E
1Q	0.14	0.29	0.35
Prior	0.14	0.29	0.33
2Q	0.18	0.30	0.35
Prior	0.26	0.29	0.34
3Q	0.26	0.31	0.37
Prior	0.35	0.30	0.36
4Q	0.26	0.33	0.38
Prior	0.21	0.31	0.37
YEAR	0.83	1.23	1.44
Prior	0.96	1.19	1.40
First Call	- -	\$0.90E	\$1.20E
P/E	31.3x	21.1x	18.0x

ACTION STATEMENT

We reiterate our **HOLD** rating on **INC Research (INCR-NASDAQ)** to reflect our balanced view of a strong finish to 2014 vs. an elevated valuation. This was the Company's first quarter following its IPO in November, so we suspect near-term investor expectations may still be a bit ahead of consensus.

Looking ahead, we are watching for updates on INCR's relationship with two large clients: **Otsuka Holdings (~14% of revenues)** and **Astellas Pharma (~12%)**. In December, Otsuka announced the acquisition of Avanir Pharmaceuticals, which we think could create new outsourcing opportunities for INCR. However, at the same time, INCR's three-year contract with Astellas is scheduled for renewal in April 2015.

- **2015E: \$1.23 from \$1.19**
- **2016E: \$1.44 from \$1.40**

KEY INVESTMENT POINTS

INCR reported 4Q14 net bookings of \$316 million (R4Q book- to- bill: ~1.2x; our estimate: \$260 million; consensus: \$270 million), translating to a year- end 2014 backlog of \$1.6 billion (+7% YOY). Project cancellations were low, which might have helped the bookings, and one client contributed \$50 million of bookings (across multiple areas). However, the 4Q14 bookings were otherwise reportedly diversified across a wide range of customers and there were no major renewals that inflated results.

Of note, management indicated that INCR entered into a strategic relationship with a large European biopharmaceutical sponsor in 2013. This sponsor has grown to now be a top five client (% of backlog) at year- end. Also, management referenced another large bookings opportunity in the first half of 2015. As INCR's bookings/backlog grow, we think it is notable that the composition of the Company's top clients is changing. For instance, two of INCR's top five clients in 2014 were not top five clients in 2013. And, based on the current pipeline, management indicated that INCR's top five clients will likely change again in 2015.

Looking ahead, we are not materially changing our **2015 revenue outlook of \$892 million** (guidance: \$870 million- \$900 million), implying constant currency growth of ~14% (after ~\$32 million of FX headwind). This implies ~56% backlog burn rate - - up from ~54% in 2013, ~49% in 2012 and ~47% in 2011. The increasing burn rate is consistent with the bookings strength seen in late 2013/early 2014. These studies have completed their start- up phases, and are entering the more revenue intensive periods of patient enrollment, monitoring and data management. Along with this, top- line growth appears to be accelerating (i.e., constant currency growth of ~24% in 2014 and ~14% expected in 2015).

We are modestly increasing our 2015 profitability estimates for adjusted EBITDA (to \$164 million from \$159 million) and for adjusted EPS (to \$1.23 from \$1.19) to reflect the carryover of the stronger than expected 4Q14 EBITDA margin of 17.9%. Our 2015 outlook implies another ~50 basis points of EBITDA margin expansion as revenue growth scale against fixed facility costs, despite ~50 basis points of margin headwind related to public company costs.

VALUATION

INCR's current intra-day trading price implies 19x multiple of our 2016 adjusted EPS estimate of \$1.44 (consensus: \$1.44), which is roughly in line with the current CRO group average (~19x). In our opinion, an in line trading multiple fairly reflects the balance of a higher growth offset by higher bookings volatility and balance sheet indebtedness.

Notably, INCR completed its IPO in November 2014, so there is not a significant trading history for this stock.

RISKS

INCR operates in a competitive industry against other providers that have similar services. The Company's ability to generate revenue and earnings growth is contingent on trends in global biopharmaceutical R&D spending and the propensity of biopharmaceutical firms to outsource R&D and sales activities to third parties. Furthermore, a significant portion of INCR's revenues are generated from clinical trials in central nervous system (CNS) disorders and oncology.

FINANCIAL MODELS

Figure 1: Projected Bookings and Backlog

INCR -- Bookings and Backlog Data (in millions)	2013A	Fiscal Year End, December 2014				2014A	Fiscal Year End, December 2015				2015E	2016E
		1QA	2QA	3QA	4QA		1QE	2QE	3QE	4QE		
Net New Business Wins (Bookings)	\$814.2	\$280.9	\$103.3	\$249.2	\$316.3	\$949.8	\$234.4	\$234.4	\$234.4	\$351.1	\$1,054.3	\$1,159.7
<i>Year-Over-Year Growth</i>	20.4%	107.0%	8.2%	-16.3%	10.9%	16.7%	11.0%	11.0%	11.0%	11.0%	11.0%	10.0%
<i>Net Book to Bill Ratio (Period)</i>	1.25x	1.52x	0.51x	1.20x	1.48x	1.17x	1.10x	1.08x	1.04x	1.49x	1.18x	1.18x
<i>Net Book to Bill Ratio (R4Q)</i>	1.25x	1.40x	1.32x	1.19x	1.17x	1.17x	1.08x	1.21x	1.17x	1.18x	1.18x	1.18x
Backlog, End of Period	\$1,490.8	\$1,594.0	\$1,493.0	\$1,506.0	\$1,589.0	\$1,589.0	\$1,611.0	\$1,627.6	\$1,635.6	\$1,751.6	\$1,751.6	\$1,930.6
<i>Year-Over-Year Growth (%)</i>	12.9%	22.3%	20.4%	9.7%	6.6%	6.6%	1.1%	9.0%	8.6%	10.2%	10.2%	10.2%
INCR -- Non-GAAP Operating Metrics												
Net Revenue	\$652.4	\$184.7	\$203.5	\$207.8	\$213.7	\$809.7	\$212.4	\$217.8	\$226.5	\$235.1	\$891.8	\$980.7
<i>Year-Over-Year Growth (%)</i>	12.7%	23.3%	27.9%	22.9%	22.6%	24.1%	15.0%	7.0%	9.0%	10.0%	10.1%	10.0%
Adjusted EBITDA	\$105.5	\$32.6	\$35.5	\$36.8	\$40.3	\$145.3	\$39.0	\$40.0	\$41.6	\$43.1	\$163.6	\$184.9
<i>Adjusted EBITDA Margin</i>	16.2%	17.6%	17.5%	17.7%	18.9%	17.9%	18.4%	18.4%	18.4%	18.4%	18.4%	18.9%
<i>Year-Over-Year Growth (%)</i>	25.1%	80.8%	43.5%	11.9%	35.2%	37.7%	19.6%	12.5%	12.8%	6.9%	12.6%	13.0%
Adjusted Earnings Per Share	\$0.30	\$0.14	\$0.18	\$0.26	\$0.26	\$0.83	\$0.29	\$0.30	\$0.31	\$0.33	\$1.23	\$1.44
<i>Year-Over-Year Growth (%)</i>	460.6%	-591.4%	182.2%	62.3%	159.0%	181.6%	111.9%	68.3%	20.4%	26.2%	47.3%	17.6%

Source: Company reports and KeyBanc Capital Markets Inc.

Figure 2: Projected Income Statements (GAAP and Non-GAAP)

INCR -- GAAP Income Statement (in millions)	2013A	Fiscal Year End, December 2014				2014A	Fiscal Year End, December 2015				2015E	2016E
		1QA	2QA	3QA	4QA		1QE	2QE	3QE	4QE		
Net Service Revenue	\$652.4	\$184.7	\$203.5	\$207.8	\$213.7	\$809.7	\$212.4	\$217.8	\$226.5	\$235.1	\$891.8	\$980.7
Year-Over-Year Growth, % (Services)	12.7%	17.0%	12.3%	15.4%	29.0%	24.1%	15.0%	7.0%	9.0%	10.0%	10.1%	10.0%
Less: Direct Costs	(432.3)	(120.8)	(130.8)	(129.6)	(134.0)	(515.1)	(136.4)	(139.8)	(145.4)	(150.9)	(572.5)	(628.6)
Gross Income	\$220.2	\$63.9	\$72.8	\$78.2	\$79.8	\$294.7	\$76.0	\$78.0	\$81.1	\$84.2	\$319.2	\$352.1
Gross Margin, % (Services)	33.7%	34.6%	35.7%	37.6%	37.3%	36.4%	35.8%	35.8%	35.8%	35.8%	35.8%	35.9%
less: Selling, General, and Admin	(117.9)	(32.2)	(34.0)	(38.2)	(40.8)	(145.1)	(38.0)	(39.0)	(40.5)	(42.1)	(159.6)	(171.6)
less: Depreciation	(19.2)	(6.9)	(5.0)	(4.7)	(5.0)	(21.6)	(5.7)	(5.7)	(5.9)	(6.1)	(23.4)	(25.5)
less: Amortization	(39.3)	(7.5)	(6.2)	(9.6)	(9.6)	(32.9)	(9.6)	(9.6)	(9.6)	(9.6)	(38.3)	(38.3)
less: Other	(12.3)	(2.8)	(19.7)	(3.0)	(5.9)	(31.3)	-	-	-	-	-	-
Operating Income	\$31.5	\$14.6	\$7.9	\$22.7	\$18.5	\$63.6	\$22.7	\$23.7	\$25.1	\$26.4	\$97.9	\$116.6
Operating Margin % (Services)	4.8%	7.9%	3.9%	10.9%	8.6%	7.9%	10.7%	10.9%	11.1%	11.2%	11.0%	11.9%
plus: Interest Income	0.3	0.2	0.0	0.0	0.0	0.2	0.0	0.0	0.0	0.0	0.2	0.2
less: Interest Expense	(60.8)	(16.1)	(12.8)	(12.9)	(11.2)	(53.0)	(5.2)	(5.2)	(5.2)	(5.2)	(21.0)	(21.0)
plus: Other Income (expense)	(1.6)	1.4	(0.3)	5.1	(45.2)	(39.1)	-	-	-	-	-	-
Pretax Income	(\$30.7)	\$0.1	(\$5.3)	\$15.0	(\$37.9)	(\$28.2)	\$17.5	\$18.5	\$19.9	\$21.2	\$77.0	\$95.8
less: Provision for Income Taxes	(10.8)	(1.6)	20.6	(2.4)	(11.8)	4.7	(6.3)	(6.7)	(7.1)	(7.6)	(27.7)	(33.5)
Net Earnings	(\$41.5)	(\$1.6)	\$15.3	\$12.6	(\$49.8)	(\$23.5)	\$11.2	\$11.9	\$12.7	\$13.6	\$49.3	\$62.3
less: Class C Stock Dividends	(0.5)	(0.1)	(0.1)	(0.1)	(3.4)	(3.8)	-	-	-	-	-	-
Net Earnings to Class A and B Shares	(\$42.0)	(\$1.7)	\$15.2	\$12.4	(\$53.2)	(\$27.2)	\$11.2	\$11.9	\$12.7	\$13.6	\$49.3	\$62.3
Diluted EPS (GAAP)	(\$0.81)	(\$0.03)	\$0.29	\$0.24	(\$0.92)	(\$0.51)	\$0.18	\$0.19	\$0.21	\$0.22	\$0.81	\$1.02
Diluted Share Count	52.0	51.9	52.2	52.5	57.5	53.5	61.2	61.2	61.2	61.2	61.2	61.2
Non-GAAP Metrics												
Net Services Revenue	\$652.4	\$184.7	\$203.5	\$207.8	\$213.7	\$809.7	\$212.4	\$217.8	\$226.5	\$235.1	\$891.8	\$980.7
Year-Over-Year Growth, % (Period)	12.7%	23.3%	27.9%	22.9%	22.6%	24.1%	15.0%	7.0%	9.0%	10.0%	10.1%	10.0%
Year-Over-Year Growth, % (R4Q)	12.7%	17.0%	21.0%	22.2%	24.1%	24.1%	21.8%	16.4%	13.0%	10.1%	10.1%	10.0%
Adjusted EBITDA	\$105.5	\$32.6	\$35.5	\$36.8	\$40.3	\$145.3	\$39.0	\$40.0	\$41.6	\$43.1	\$163.6	\$184.9
Adjusted EBITDA Margin %	16.2%	17.6%	17.5%	17.7%	18.9%	17.9%	18.4%	18.4%	18.4%	18.4%	18.4%	18.9%
Year-Over-Year Growth, % (Period)	25.1%	80.8%	43.5%	11.9%	35.2%	37.7%	19.6%	12.5%	12.8%	6.9%	12.6%	13.0%
Adjusted EPS	\$0.30	\$0.14	\$0.18	\$0.26	\$0.26	\$0.83	\$0.29	\$0.30	\$0.31	\$0.33	\$1.23	\$1.44
Year-Over-Year Growth, % (Period)	460.6%	-591.4%	182.2%	62.3%	159.0%	181.6%	111.9%	68.3%	20.4%	26.2%	47.3%	17.6%

Source: Company reports and KeyBanc Capital Markets Inc.

KeyBanc Capital Markets Inc. Disclosures and Certifications

INC Research Holdings, Inc. - INCR

We expect to receive or intend to seek compensation for investment banking services from INC Research Holdings, Inc. within the next three months.

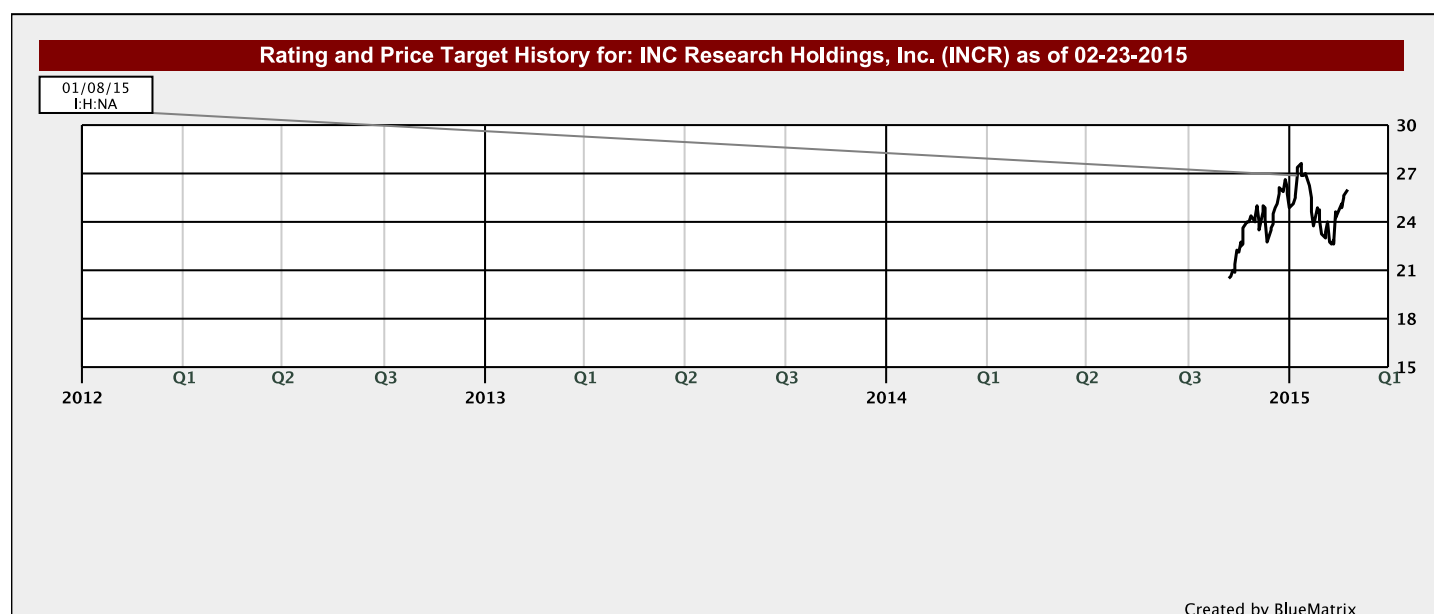
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As of the date of this report, we make a market in INC Research Holdings, Inc..

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Three- Year Rating and Price Target History



Rating Disclosures

Distribution of Ratings/IB Services Firmwide and by Sector									
KeyBanc Capital Markets					HEALTHCARE				
Rating	Count	Percent	IB Serv/Past 12 Mos.		Rating	Count	Percent	IB Serv/Past 12 Mos.	
			Count	Percent				Count	Percent
BUY [BUY]	259	44.81	61	23.55	BUY [BUY]	18	48.65	4	22.22
HOLD [HOLD]	301	52.08	56	18.60	HOLD [HOLD]	17	45.95	2	11.76
SELL [UND]	18	3.11	3	16.67	SELL [UND]	2	5.41	0	0.00

Rating System

BUY - The security is expected to outperform the market over the next six to 12 months; investors should consider adding the security to their holdings opportunistically, subject to their overall diversification requirements.

HOLD - The security is expected to perform in line with general market indices over the next six to 12 months; no buy or sell action is recommended at this time.

UNDERWEIGHT - The security is expected to underperform the market over the next six to 12 months; investors should reduce their holdings opportunistically.

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