

COMPANY NOTE

Company Update

USA | Healthcare | Pharmaceutical Svcs.

October 30, 2015

Jefferies

INC Research (INCR) Solid Again: Key Insights from 3Q15

Key Takeaway

INCR's momentum should carry it to \$2.30+ in EPS next year. INCR's revenues, margins, and bookings exceeded expectations. Management has increased 2015 EPS guidance by 50% intra-year. The Trusted Process and therapeutic alignment have become very attractive to current and new clients, and continue to support future revenue and margin growth. Maintain Buy.

1. Impressive Operations. Revenue of \$234.5M exceeded consensus by \$4M (1.7%). Normalized operating margin expanded 460 bps YoY (165 bps FX benefit) and 70 bps sequentially to 21.8%. Higher btb and backlog burn rate has boosted revenue this year. Margins have benefited from faster progress on facility utilization and IT system consolidation. So far in 3Q, peers have reported modest BtBs due to heavy cancellations. INCR managed to avoid cancellations and posted a strong 1.4x BtB.

2. Diversify Client Base, Then Expand Share. ~90% of 2015 YTD new business awards have come from existing customers. INCR follows a "Land and Expand" strategy. Management remains focused on breaking into incremental Top 20 pharma customers with targeted strategies, then expanding wallet share with quality delivery. As trial complexity increases, INCR's therapeutic alignment and Trusted Process seem to be resonating with clients. Growth in INCR's 3-10 ranked clients has outpaced Otsuka and Astellas, such that they represent <10% of revenue. We think INCR's revenue growth will continue to lead the group.

3. Highlighting Technology More Prominently. INCR eliminated 2 of 5 CTMS systems YTD and may get rid of a third by YE15. We have debated the LT impact INCR faces by only utilizing 3rd party vendors. Peers have heavily invested in tech platforms (Infosario, ICONIK, Predictivv) designed to complement Medidata and other core technologies. INCR's strategy is aimed to allow access to top-notch tech talent and allows them to minimize software development investment. INCR works closely with 3rd parties to develop the most relevant, beneficial, and up to date systems. Best in group margins appear to indicate INCR is not missing any operational efficiencies.

Valuation/Risks

Our 12-month PT of \$51 reflects a 21.7x P/E (was 23x) on our \$2.35 '16 EPS_e (8% above consensus). INCR's high recent growth should moderate but continue to lead peers. That moderation should be more gradual than consensus now projects. Risks: 1) Project cancellations, 2) failure to penetrate new clients, 3) pricing pressure from new or existing clients, 4) scale investments.

USD	Prev.	2013A	Prev.	2014A	Prev.	2015E	Prev.	2016E
Rev. (MM)	--	652.4	--	809.7	907.0	912.5	1,032.3	1,050.7
EBITDA (MM)	--	103.1	--	150.9	202.7	215.3	231.2	248.4
Cons. EPS	--	--	--	--	1.77	1.88	2.09	2.18
EPS Non-GAAP								
Mar	--	(0.03)	--	0.13	--	0.41A	--	0.50
Jun	--	0.06	--	0.25	--	0.46A	--	0.56
Sep	--	0.15	--	0.33	0.47	0.53A	--	0.69
Dec	--	0.07	--	0.26	0.46	0.50	--	0.61
FY Dec	--	0.25	--	0.97	1.78	1.88	2.21	2.35
EV/Rev		4.1x		3.3x		2.9x		2.5x

BUY

Price target \$51.00

Price \$39.67

Financial Summary

Book Value (MM):	\$317.9
Net Debt (MM):	\$338.5
Long-Term Debt (MM):	\$475.0
Cash & ST Invest. (MM):	\$136.5
Backlog:	1,766

Market Data

52 Week Range:	\$51.69 - \$18.50
Total Entprs. Value (MM):	\$2,671.1
Market Cap. (MM):	\$2,332.6
Shares Out. (MM):	58.8
Float (MM):	26.1
Avg. Daily Vol.:	443,788

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Price Performance

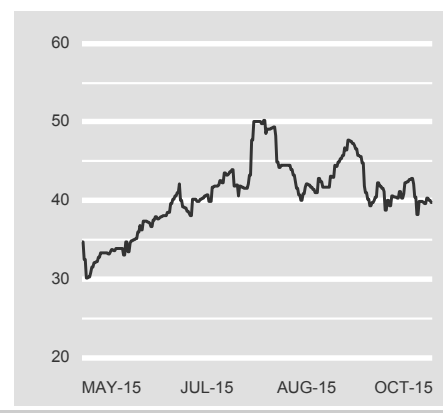


Chart 1: Summary of INC's Results

INC Research
Quarterly Results Comparison
3Q15

FY December (\$ in 000s, except for EPS)	Reported		Estimate	Actual	Consensus	Percentage Change		Difference		
	3Q14	2Q15	3Q15	3Q15	3Q15	Seq	Y/Y	Seq	Y/Y	Est.
Net service revenue	\$ 207,763	\$ 227,376	\$ 229,092	\$ 234,494	\$ 230,600	3.1%	12.9%	7,118	26,731	5,402
Direct costs	129,557	138,010	140,204	135,530		(1.8%)	4.6%	(2,480)	5,973	(4,674)
SG&A	37,763	37,014	38,258	40,315		8.9%	6.8%	3,301	2,552	2,057
FOREX	-	-	-	-		NA	NA	-	-	-
Adj EBITDA	40,443	52,352	50,629	58,649	48,100	12.0%	45.0%	6,297	18,206	8,020
Depreciation	4,734	4,420	4,590	4,357		(1.4%)	(8.0%)	(63)	(377)	(233)
Total expenses	172,054	179,444	183,052	180,202		0.4%	4.7%	758	8,148	(2,850)
Adj EBITA	35,709	47,932	46,039	54,292		13.3%	52.0%	6,360	18,583	8,253
Interest income (expense)	(12,903)	(4,188)	(2,569)	(3,037)		(27.5%)	(76.5%)	1,151	9,866	(468)
Other income (expense)	5,136	-	-	(1,003)		NA	(119.5%)	(1,003)	(6,139)	(1,003)
Pretax income	27,942	43,744	43,470	50,252		14.9%	79.8%	6,508	22,310	6,782
Taxes	10,665	16,077	15,629	19,052		18.5%	78.6%	2,975	8,387	3,423
Adj Net income	17,277	27,667	27,842	31,200		12.8%	80.6%	3,533	13,923	3,358
Adj EPS b/f charges	\$ 0.33	\$ 0.46	\$ 0.47	\$ 0.53	\$ 0.44	16.0%	61.4%	\$ 0.07	\$ 0.20	\$ 0.06
Diluted shares	52,514	60,464	58,774	58,764		(2.8%)	11.9%	(1,700)	6,250	(10)
Common Size:										
Net revenue	100.0%	100.0%	100.0%	100.0%				0 bps	0 bps	0 bps
Grow th										
Direct costs	62.4%	60.7%	61.2%	57.8%				(290 bps)	(460 bps)	(340 bps)
Gross margin	37.6%	39.3%	38.8%	42.2%				290 bps	460 bps	340 bps
SG&A	18.2%	16.3%	16.7%	17.2%				90 bps	(100 bps)	50 bps
Adj EBITDA	19.5%	23.0%	22.1%	25.0%				200 bps	550 bps	290 bps
Depreciation	2.3%	1.9%	2.0%	1.9%				(10 bps)	(40 bps)	(10 bps)
Total expenses	82.8%	78.9%	79.9%	76.8%				(210 bps)	(600 bps)	(310 bps)
Adj EBITA	17.2%	21.1%	20.1%	23.2%				210 bps	600 bps	310 bps
Interest income (expense)	-6.2%	-1.8%	-1.1%	-1.3%				50 bps	490 bps	(20 bps)
Other income (expense)	2.5%	0.0%	0.0%	-0.4%				(40 bps)	(290 bps)	(40 bps)
Pretax income	13.4%	19.2%	19.0%	21.4%				220 bps	800 bps	250 bps
Taxes	38.2%	36.8%	36.0%	37.9%				120 bps	(30 bps)	200 bps
Adjusted net income	8.3%	12.2%	12.2%	13.3%				110 bps	500 bps	120 bps
Metrics										
Net new business	249,300	295,900	318,093	327,700		10.7%	31.4%	31,800	78,400	9,608
Book-to-bill	1.20x	1.30x	1.39x	1.40x						
Ending backlog	1,505,973	1,675,996	1,714,102	1,800,000		7.4%	19.5%	124,004	294,027	85,898

Source: Company data and Jefferies LLC

INC Research Holdings, Inc. and Subsidiaries
Earnings Model

Source: Jefferies & Co.

FY December

(\$ in 000s, except for EPS)

	2014-A					2015E					2016E				
	Q1	Q2	Q3	Q4	2014	Q1-A	Q2-A	Q3-A	Q4	2015	Q1	Q2	Q3	Q4	2016
Net service revenue	\$ 184,700	\$ 203,540	\$ 207,763	\$ 213,725	\$ 809,728	\$ 211,514	\$ 227,376	\$ 234,494	\$ 239,162	\$ 912,546	\$ 246,415	\$ 263,160	\$ 275,602	\$ 265,535	\$ 1,050,712
Direct costs	120,764	130,781	129,557	133,957	515,059	125,448	138,010	135,530	142,302	541,290	152,308	161,045	158,600	155,338	627,292
SG&A	31,890	33,616	37,763	40,494	143,763	35,579	37,014	40,315	43,049	155,957	40,464	42,576	45,453	46,469	174,962
FOREX	-	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Adj EBITDA	32,046	39,143	40,443	39,274	150,906	50,487	52,352	58,649	53,812	215,300	53,643	59,538	71,549	63,728	248,458
Depreciation	6,869	5,025	4,734	4,991	21,619	4,766	4,420	4,357	4,521	18,064	4,686	4,860	5,036	5,207	19,789
Total expenses	159,523	169,422	172,054	179,442	680,441	165,793	179,444	180,202	189,872	715,311	197,458	208,481	209,090	207,013	822,042
Adj EBITA	25,177	34,118	35,709	34,283	129,287	45,721	47,932	54,292	49,291	197,236	48,957	54,678	66,512	58,522	228,670
Interest income (expense)	(15,901)	(12,823)	(12,903)	(11,160)	(52,787)	(5,305)	(4,188)	(3,037)	(2,522)	(15,052)	(2,467)	(2,392)	(2,307)	(2,225)	(9,391)
Other income (expense)	1,378	(337)	5,136	1,512	7,689	-	-	(1,003)	-	(1,003)	-	-	-	-	-
Pretax income	10,654	20,958	27,942	24,635	84,189	40,416	43,744	50,252	46,769	181,181	46,490	52,286	64,205	56,297	219,279
Taxes	4,138	8,085	10,665	9,509	32,397	14,805	16,077	19,052	17,304	67,238	17,201	19,085	23,114	19,985	79,385
Adj Net income	6,516	12,873	17,277	15,126	51,792	25,611	27,667	31,200	29,464	113,942	29,289	33,202	41,091	36,311	139,893
Adj EPS b/f charges	\$ 0.13	\$ 0.25	\$ 0.33	\$ 0.26	\$ 0.97	\$ 0.41	\$ 0.46	\$ 0.53	\$ 0.50	\$ 1.88	\$ 0.50	\$ 0.56	\$ 0.69	\$ 0.61	\$ 2.35
Diluted shares	51,947	52,185	52,514	57,504	53,538	63,103	60,464	58,764	58,851	60,683	58,794	59,643	59,475	59,319	59,575
Common Size:															
Direct costs	65.4%	64.3%	62.4%	62.7%	63.6%	59.3%	60.7%	57.8%	59.5%	59.3%	61.8%	61.2%	57.5%	58.5%	59.7%
Gross margin	34.6%	35.7%	37.6%	37.3%	36.4%	40.7%	39.3%	42.2%	40.5%	40.7%	38.2%	38.8%	42.5%	41.5%	40.3%
SG&A	17.3%	16.5%	18.2%	18.9%	17.8%	16.8%	16.3%	17.2%	18.0%	17.1%	16.4%	16.2%	16.5%	17.5%	16.7%
Adj EBITDA	17.4%	19.2%	19.5%	18.4%	18.6%	23.9%	23.0%	25.0%	22.5%	23.6%	21.8%	22.6%	26.0%	24.0%	23.6%
Depreciation	3.7%	2.5%	2.3%	2.3%	2.7%	2.3%	1.9%	1.9%	1.9%	2.0%	1.9%	1.8%	1.8%	2.0%	1.9%
Total expenses	86.4%	83.2%	82.8%	84.0%	84.0%	78.4%	78.9%	76.8%	79.4%	78.4%	80.1%	79.2%	75.9%	78.0%	78.2%
Adj EBITA	13.6%	16.8%	17.2%	16.0%	16.0%	21.6%	21.1%	23.2%	20.6%	21.6%	19.9%	20.8%	24.1%	22.0%	21.8%
Interest income (expense)	-8.6%	-6.3%	-6.2%	-5.2%	-6.5%	-2.5%	-1.8%	-1.3%	-1.1%	-1.6%	-1.0%	-0.9%	-0.8%	-0.8%	-0.9%
Other income (expense)	0.7%	-0.2%	2.5%	0.7%	0.9%	0.0%	0.0%	-0.4%	0.0%	-0.1%	0.0%	0.0%	0.0%	0.0%	0.0%
Pretax income	5.8%	10.3%	13.4%	11.5%	10.4%	19.1%	19.2%	21.4%	19.6%	19.9%	18.9%	19.9%	23.3%	21.2%	20.9%
Taxes	38.8%	38.6%	38.2%	38.6%	38.5%	36.6%	36.8%	37.9%	37.0%	37.1%	37.0%	36.5%	36.0%	35.5%	36.3%
Adjusted net income	3.5%	6.3%	8.3%	7.1%	6.4%	12.1%	12.2%	13.3%	12.3%	12.5%	11.9%	12.6%	14.9%	13.7%	13.3%

Company Description

INC Research (Nasdaq:INCR) is a leading global contract research organization (CRO) providing the full range of Phase I to Phase IV clinical development services for the biopharmaceutical and medical device industries. With significant breadth of service offerings and depth of therapeutic expertise across multiple patient populations, INC Research connects customers, clinical research sites and patients to accelerate the delivery of new medicines to market. The Company was ranked "Top CRO to Work With" among large global CROs in the 2015 CenterWatch Global Investigative Site Relationship Survey. INC Research is headquartered in Raleigh, N.C., with staff in 50 countries and experience spanning more than 100 countries.

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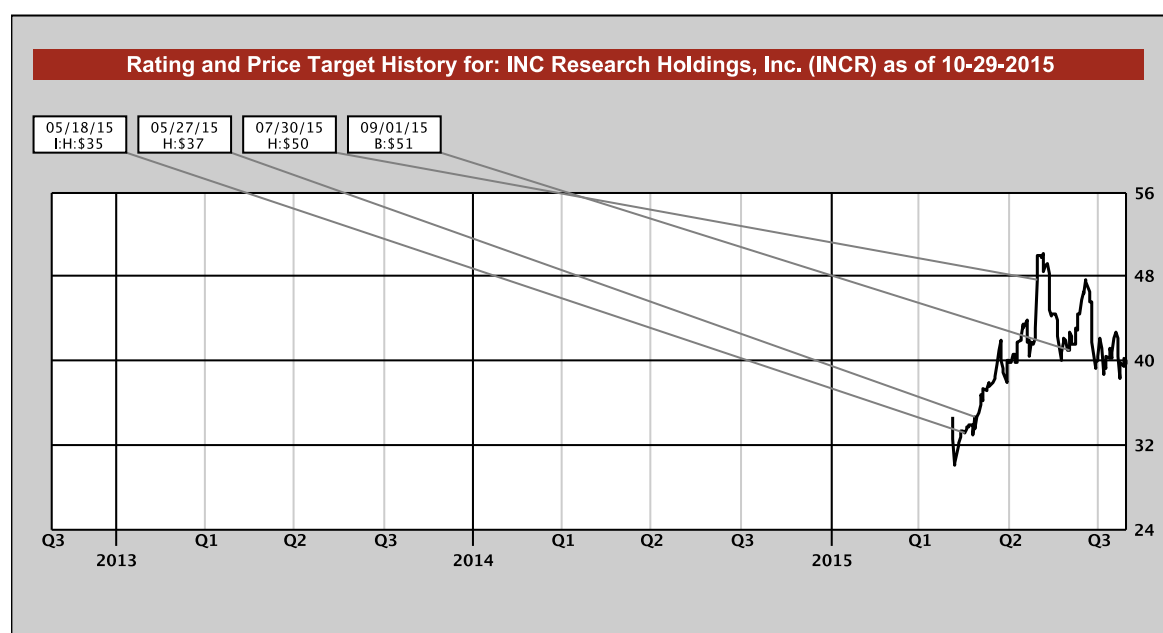
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Other Companies Mentioned in This Report

- Astellas Pharma (4503 JP: ¥1,765, BUY)
- Otsuka Corporation (4768 JP: ¥5,870, BUY)



Rating and Price Target History for: Astellas Pharma (4503 JP) as of 10-29-2015

Rating and Price Target History for: Otsuka Corporation (4768 JP) as of 10-29-2015

Distribution of Ratings

Rating	Count	Percent	IB Serv./Past 12 Mos.	
			Count	Percent
BUY	1128	53.54%	314	27.84%
HOLD	831	39.44%	163	19.61%
UNDERPERFORM	148	7.02%	17	11.49%

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