

July 30, 2015

## INC Research Holdings, Inc.

### First Look at Very Strong Second-Quarter Results

- Quarterly result overview.** INC reported very strong second-quarter results on Thursday morning, July 30—the company's third earnings release since its initial public offering. EPS exceeded our target by \$0.13 on better revenues and much better margins. EBITDA margin was 450 basis points above our target, driven mainly by gross margins that were 280 basis points better than our target. We note that the adjusted EPS total of \$0.47 reported by the company excludes stock compensation expenses, and thus enhances quarterly performance by roughly \$0.01. Relative to our model, better revenue (about \$0.02) and gross margin (about \$0.07) drove the outperformance. While foreign exchange rates had a negative impact on net service revenues (roughly \$11.3 million), INC also realizes a margin benefit as a higher percentage of costs are denominated in local currencies as compared with revenue. Net revenue increased 17.3% on a constant-currency basis, compared with our 13.3% estimate.
- Bookings were \$34.1 million better.** Net new business was \$295.9 million, producing a book-to-bill ratio of 1.3 times. We had modeled \$261.8 million in bookings and a book-to-bill ratio of 1.20 times. According to the release, growth continues to be strong within CNS, oncology, and other complex therapeutic areas. This level of bookings should support management's expectation for low-double-digit revenue growth in 2015.
- Updated 2015 guidance.** Given strong quarterly results, management updated calendar 2015 guidance, calling for revenues of \$900 million to \$910 million, which implies an increase of 11.1% to 12.4% despite several points of currency-related headwind. Management's guidance is roughly \$13 million and \$11 million above our estimate and consensus, respectively, at the midpoint and is \$12.5 million above prior guidance despite the headwind from a stronger dollar. Management also increased its 2015 EPS target to a range of \$1.69 to \$1.80 (up 104% to 117%). Guidance was increased an impressive \$0.23.
- Valuation and stock thoughts.** As of Wednesday's close, INC trades at 24.8 times our current 2016 EPS estimate of \$1.74 (up 16.7%), which includes stock based comp. Currently, the clinical CRO peer group trades at 19.9 times (ICON [ICLR \$78.58; Outperform] 16.9 times, Quintiles [Q \$79.10; Outperform] 22.1 times, PRA [PRAH \$41.83; Outperform] 20.9 times, and Parexel [PRXL \$69.22; Outperform] 19.9 times). While revenues continue to be hampered by currency headwinds, we maintain our Outperform rating on INC given the company's industry-leading organic growth profile and impressive margin improvement of late. We will update our model following Thursday's earnings call, and expect to increase our overall 2015 EPS estimate by \$0.20-\$0.25. Exhibits 1 and 3, on the following page, break down the second quarter versus our expectations.

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Stock Rating: **Outperform**  
Company Profile: **Aggressive Growth**

Symbol: INCR (NASDAQ)  
Price: \$43.16 (52-Wk.: \$20-\$44)  
Market Value (mil.): \$2,428  
Fiscal Year End: December  
Long-Term EPS Growth Rate: 20%  
Dividend/Yield: None

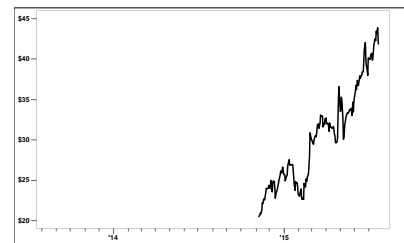
	2014A	2015E	2016E
<b>Estimates</b>			
EPS Q1	\$0.12	A\$0.42	NA
Q2	\$0.27	\$0.34	NA
Q3	\$0.28	\$0.37	NA
Q4	\$0.26	\$0.39	NA
FY	\$0.93	\$1.52	\$1.78
CY		\$1.52	\$1.78

<b>Valuation</b>			
FY P/E	46.4x	28.4x	24.2x
CY P/E		28.4x	24.2x

<b>Trading Data (FactSet)</b>			
Shares Outstanding (mil.)			61
Float (mil.)			5
Average Daily Volume			307,191

<b>Financial Data (FactSet)</b>			
Book Value Per Share (MRQ)			6.7
Return on Equity (TTM)			-8.1

#### Two-Year Price Performance Chart



Sources: FactSet, William Blair & Company estimates

INC Research is one of the top 10 largest CROs, with an annual revenue base exceeding \$800 million. Founded in 1985 as a niche CRO focused on central nervous system disorders, INC now employs 5,400 associates across 50 countries, and its focus has broadened to include oncology and other complex diseases.

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### Exhibit 1. Second-Quarter EPS Performance Relative to William Blair Estimates

Revenues	\$ 0.016
Gross Profit	\$ 0.067
Selling & Marketing	\$ 0.041
Depreciation	\$ 0.011
Interest	\$ (0.004)
Taxes	\$ -
Share Count	\$ 0.001
<b>Total</b>	<b>\$ 0.132</b>

Sources: Company reports and William Blair estimates

### Exhibit 2. Current 2015 Guidance Relative to William Blair Estimates and Consensus

	2015 Guidance		2015 Estimates	
	Updated	Prior to Call	WB - Prior to Call	Consensus - Prior to Call
Revenue (\$M)	\$900 to 910	\$880 to 905	\$892	\$894
Growth	11.1% to 12.4%	8.7% to 11.8%	10.2%	10.5%
Adjusted EPS (excl. SBC)	\$1.69 to \$1.80	\$1.45 to \$1.57	\$1.52	\$1.53
Growth (decline)	104% to 117%	75% to 89%	83.1%	84.3%
Adjusted EPS (incl. SBC)	\$1.64 to \$1.75	\$1.40 to \$1.52	\$1.49	NA
Growth (decline)	108% to 122%	77% to 92%	88.6%	

Sources: Company reports, FactSet, and William Blair estimates

### Exhibit 3. Second Quarter 2015 EPS Variance Analysis

July 30, 2015	2Q 2015 (Actual)	2Q 2014 (Actual)	Year/Year % Change	2Q 2015 (Estimate)	Year/Year % Change	Act.-Est. Difference
Total Net Revenue	227,376	203,540	11.7%	218,147	7.2%	9,229
Direct Costs	138,010	130,781	5.5%	138,524	5.9%	(514)
Selling, general, and administrative (incl options)	37,014	33,616	10.1%	39,048	16.2%	(2,034)
Stock-based comp expense	(913)	(893)	2.2%	(707)	-20.8%	(206)
Total operating expenses	174,111	163,504	6.5%	176,865	8.2%	(2,754)
<b>EBITDA (excluding SBC)</b>	<b>53,265</b>	<b>40,036</b>	<b>33.0%</b>	<b>41,282</b>	<b>3.1%</b>	<b>11,983</b>
Depreciation	4,420	5,025	-12.0%	5,236	4.2%	(816)
Operating income (excluding SBC)	48,845	35,011	39.5%	36,046	3.0%	12,799
Interest and other income (expense)	(4,188)	(12,823)	-67.3%	(3,799)	-70.4%	(389)
Earnings before tax	44,657	22,188	101.3%	32,247	45.3%	12,410
Income taxes (expense) benefit	(16,077)	(8,210)	95.8%	(11,609)	41.4%	(4,468)
<b>Adjusted net income (excluding SBC)</b>	<b>28,580</b>	<b>13,978</b>	<b>104%</b>	<b>20,638</b>	<b>47.6%</b>	<b>7,942</b>
Shares outstanding	60,464	52,185	15.9%	60,614	16.2%	(150)
<b>EPS (excluding SBC)</b>	<b>\$0.47</b>	<b>\$0.27</b>	<b>76%</b>	<b>\$0.34</b>	<b>27.1%</b>	<b>0.13</b>
<b>EPS (including SBC)</b>	<b>\$0.46</b>	<b>\$0.26</b>	<b>80%</b>	<b>\$0.33</b>	<b>29.5%</b>	<b>0.13</b>
<u>% of Net Revenue:</u>			<u>Change</u>		<u>Difference</u>	
Gross profit	39.30	35.75	3.56	36.50	0.75	2.80
Selling, general and administrative	16.28	16.52	(0.24)	17.90	1.38	(1.62)
Stock-based comp expense	0.40	0.44	(0.04)	0.32	(0.11)	0.08
EBITDA	23.43	19.67	3.76	18.92	(0.75)	4.50
Depreciation	1.94	2.47	(0.52)	2.40	(0.07)	(0.46)
EBITA	21.48	17.20	4.28	16.52	(0.68)	4.96
Tax rate	36.00	37.00	(1.00)	36.00	(1.00)	0.00
Net Income	12.57	6.87	5.70	9.46	2.59	3.11
<u>Bookings</u>						
Net new business	295,900	103,400	192,500	261,777	158,377	34,123
Net Book-to-Bill	1.30	0.51		1.20		

Sources: Company reports, FactSet, and William Blair estimates

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William Blair or an affiliate is a market maker in the security of INC Research Holdings, Inc.

William Blair or an affiliate expects to receive or intends to seek compensation for investment banking services from INC Research Holdings, Inc. within the next three months.

William Blair or an affiliate received compensation for investment banking services from INC Research Holdings, Inc. within the last 12 months. INC Research Holdings, Inc. is or was, within the last 12 months, an investment banking client of William Blair & Company and/or one or more of its affiliates.

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DOW JONES: 17,751.39

S&P 500: 2,108.57

NASDAQ: 5,111.73



## **Current Rating Distribution (as of 06/30/15)**

Coverage Universe	Percent	Inv. Banking Relationships*	Percent
Outperform (Buy)	66	Outperform (Buy)	15
Market Perform (Hold)	32	Market Perform (Hold)	2
Underperform (Sell)	2	Underperform (Sell)	0

\*Percentage of companies in each rating category that are investment banking clients, defined as companies for which William Blair has received compensation for investment banking services within the past 12 months.

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