

# INC Research Holdings, Inc.

## First Look at Strong Fourth-Quarter Results; 2015 Guidance Modestly Better Than Consensus

- Quarterly result overview.** INC reported strong fourth-quarter results on Tuesday morning, February 24—the company's first earnings release since its initial public offering. EPS exceeded our target by 7 cents on better revenues and an EBITDA margin 141 basis points above our target. We note that the adjusted EPS total of \$0.26 reported by the company excludes stock compensation expenses, and thus enhances the quarter's performance by roughly 1 cent. Relative to our model, better revenue (more than 1 cent) and gross margin (5 cents) drove the outperformance, with items below the operating line adding 1 cent. Full-year operating margin gains were also impressive, increasing nearly 280 basis points from a year ago, but 111 basis points of this improvement can be attributed to \$9 million (111 basis points of margin) of extra charge orders filled in the second and third quarter. We do not believe unusual change order activity affected the fourth-quarter results.
  - Bookings were \$70 million better.** Net new business was \$316.7 million, producing a book-to-bill ratio of 1.48 times. We had modeled \$246.9 million in bookings and a book-to-bill ratio of 1.20 times. The better awards total extends the trend of strong bookings delivered by clinical CROs so far this quarter. This level of bookings should support management's expectation for low-double-digit revenue growth in 2015. We look for additional detail on the mix of the new wins on Tuesday's 7:00 a.m. conference call.
  - Guidance for 2015 appears modestly better than consensus.** Guidance for calendar 2015 was introduced, calling for revenues of \$870 million to \$900 million, which implies a respectable 7.4% to 11.1% increase despite several points of currency-related headwind. Management's target is \$10 million above our estimate at the midpoint, and brackets the consensus of \$881 million (see exhibit 2, on page 2).
- Adjusted EPS guidance calls for a range of \$1.19 to \$1.29 (up 42% to 55%). The midpoint of the range is 11 cents above our \$1.13 target (excluding 4 cents of stock compensation expense) and 4 cents above consensus.
- Valuation and stock thoughts.** As of Monday's close, INC trades at 23.0 times our current 2015 EPS estimate of \$1.13 (up 21.1%). Currently, the clinical CRO peer group trades at 21.0 times [ICON [ICLR \$61.94; Outperform] at 19.7 times, Quintiles [Q \$46.99; Outperform] at 21.2 times, PRA Health Sciences [PRAH \$28.65; Outperform] at 21.1 times, and Parexel [PRXL \$64.75; Outperform] at 22.1 times). We believe these results are modestly above expectations despite the notable currency headwind. We are constructive on the CRO group and maintain our Outperform rating on INC given the company's industry leading growth profile. We will update our model following Tuesday's earnings call, and expect to increase our overall 2015 EPS estimates by 10 to 12 cents. Exhibits 1 and 3, on the following pages, break down the fourth quarter versus our expectations.

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.

John Kreger  
+1 312 364 8597  
jkreger@williamblair.com

Roberto Fatta  
+1 312 364 8797  
rfatta@williamblair.com

Matt Bacso, CFA  
+1 312 364 8996  
mbacso@williamblair.com

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February 24, 2015

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

Symbol: INCR (NASDAQ)  
Price: \$25.99 (52-Wk.: \$20-\$29)  
Market Value (mil.): \$1,560  
Fiscal Year End: December  
Long-Term EPS Growth Rate: 20%  
Dividend/Yield: None

		2013A	2014E	2015E
<b>Estimates</b>				
EPS	Q1	\$-0.03	A\$0.14	NA
	Q2	\$0.06	A\$0.26	NA
	Q3	\$0.16	A\$0.35	NA
	Q4	\$0.10	\$0.19	NA
	FY	\$0.30	\$0.93	\$1.13
	CY		\$0.93	\$1.13
<b>Valuation</b>				
FY P/E		86.6x	27.9x	23.0x
CY P/E			27.9x	23.0x

<b>Trading Data (FactSet)</b>	
Shares Outstanding (mil.)	60
Float (mil.)	23
Average Daily Volume	213,333

<b>Financial Data (FactSet)</b>	
Long-Term Debt/Total Capital (MRQ)	0.0
Book Value Per Share (MRQ)	0.0
Return on Equity (TTM)	-14.2

### Two-Year Price Performance Chart



Sources: FactSet, William Blair & Company estimates

**Exhibit 1. Fourth-Quarter EPS Performance Relative to William Blair Estimates**

Revenues	\$ 0.012
Gross Profit	\$ 0.037
Selling & Marketing	\$ (0.005)
Depreciation	\$ 0.015
Interest	\$ 0.005
Taxes	\$ -
Share Count	\$ 0.002
<b>Total</b>	<b>\$ 0.066</b>

Sources: Company reports and William Blair & Company, L.L.C. estimates

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

	2015 Guidance	2015 Estimates	
		WB - Prior to Call	Consensus - Prior to Call
Revenue (\$M)	\$870 to 900	\$870	\$881
Growth	7.4% to 11.1%	8.5%	10.0%
Adjusted EPS (excl. SBC)	\$1.19 to \$1.29	\$1.13	\$1.20
Growth (decline)	42% to 55%	21.1%	33.3%
Adjusted EPS (incl. SBC)	\$1.14 to \$1.24	\$1.09	NA
Growth (decline)	44% to 57%	21.4%	

Sources: Company reports, FactSet, and William Blair & Company, L.L.C. estimates

### Exhibit 3. Fourth Quarter 2014 EPS Variance Analysis

February 24, 2015

	<b>4Q 2014 (Actual)</b>	<b>4Q 2013 (Actual)</b>	<b>Year/Year % Change</b>	<b>4Q 2014 (Estimate)</b>	<b>Year/Year % Change</b>	<b>Act.-Est. Difference</b>
Total Net Revenue	213,725	174,365	22.6%	205,745	18.0%	7,980
Direct Costs	133,957	112,080	19.5%	132,294	18.0%	1,663
Selling, general, and administrative (incl options)	40,494	34,012	19.1%	38,474	13.1%	2,020
Stock-based comp expense	(1,065)	(1,566)	-32.0%	(960)	-38.7%	(105)
Total operating expenses	173,386	144,526	20.0%	169,808	17.5%	3,578
<b>EBITDA (excluding SBC)</b>	<b>40,339</b>	<b>29,839</b>	<b>35.2%</b>	<b>35,937</b>	<b>20.4%</b>	<b>4,402</b>
Depreciation	4,991	5,241	-4.8%	6,172	17.8%	(1,181)
Operating income (excluding SBC)	35,348	24,598	43.7%	29,765	21.0%	5,583
Interest and other income (expense)	(11,160)	(16,344)	-31.7%	(11,600)	-29.0%	440
Earnings before tax	24,188	8,254	193.0%	18,165	120.1%	6,023
Income taxes (expense) benefit	(8,950)	(3,054)	193.1%	(6,721)	120.1%	(2,229)
<b>Adjusted net income (excluding SBC)</b>	<b>15,238</b>	<b>5,200</b>	<b>193%</b>	<b>11,444</b>	<b>120.1%</b>	<b>3,794</b>
Shares outstanding	58,788	52,003	13.0%	59,189	13.8%	(401)
<b>EPS (excluding SBC)</b>	<b>\$0.26</b>	<b>\$0.10</b>	<b>159%</b>	<b>\$0.19</b>	<b>93.4%</b>	<b>0.07</b>
<b>EPS (including SBC)</b>	<b>\$0.25</b>	<b>\$0.08</b>	<b>206%</b>	<b>\$0.18</b>	<b>126.0%</b>	<b>0.06</b>
<b>% of Net Revenue:</b>			<b>Change</b>		<b>Difference</b>	
Gross profit	37.32	35.72	1.60	35.70	(0.02)	1.62
Selling, general and administrative	18.95	19.51	(0.56)	18.70	(0.81)	0.25
Stock-based comp expense	0.50	0.90	(0.40)	0.47	(0.43)	0.03
EBITDA	18.87	17.11	1.76	17.47	0.35	1.41
Depreciation	2.34	3.01	(0.67)	3.00	(0.01)	(0.66)
EBITA	16.54	14.11	2.43	14.47	0.36	2.07
Tax rate	37.00	37.00	0.00	37.00	(0.00)	0.00
Net Income	7.13	2.98	4.15	5.56	2.58	1.57
<b>Bookings</b>						
Net new business	316,700	285,200	31,500	246,894	(38,306)	69,806
Net Book-to-Bill	1.48	1.64		1.20		

Sources: Company reports, FactSet, and William Blair &amp; Company, L.L.C. estimates

William Blair & Company, L.L.C.

### **IMPORTANT DISCLOSURES**

William Blair was a manager or co-manager of a public offering of equity securities for INC Research Holdings, Inc. within the prior 12 months.

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

William Blair intends to seek investment banking compensation in the next three months from INC Research Holdings, Inc.

Within the past 12 months William Blair has provided or is providing investment banking services to or has an investment services relationship with INC Research Holdings, Inc.

Additional information is available upon request.

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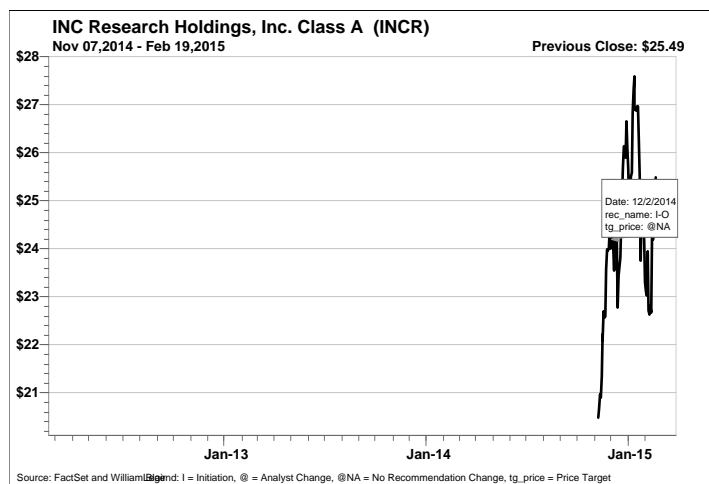
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DOW JONES: 18,116.84

S&P 500: 2,109.66

NASDAQ: 4,960.97



### **Current Rating Distribution (as of 01/31/15)**

Coverage Universe	Percent	Inv. Banking Relationships*	Percent
Outperform (Buy)	64	Outperform (Buy)	16
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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