

HOLD
 TP: Rs 765 | ▼ 4%

GLENMARK LIFE SCIENCES

Pharmaceuticals

24 January 2024

Strong margins make up for subdued revenue growth

- Q3 revenue growth a miss at 6% YoY but robust 670bps expansion in gross margin helped mitigate the impact on bottomline
- EBITDA/PAT grew 19%/13% YoY on higher margins – in line with consensus
- Our DCF-based TP stands revised to Rs 765 (vs. Rs 620) as we raise FY24-FY26 EPS 4-8%; maintain HOLD as valuations look fair post rally

Saad Shaikh

research@bobcaps.in

External business fares well; GPL declines: GLS reported 6% YoY growth in Q3FY24 revenue to Rs 5.7bn, a miss of 5% compared to Bloomberg consensus. The subdued topline growth stemmed from lower sales in its Glenmark Pharma (GPL) business which declined 2% YoY (-23% QoQ), whereas external business reported a healthy 9% YoY (+6% QoQ) uptick. Management highlighted that the slowdown in GPL business is temporary and was mainly on account of a few developed markets (including Japan which had inventory issues), while emerging markets led the growth. The company did not see any decline in volumes for Q3.

CDMO business rebounds; new multi-year contract to begin in FY25: The CDMO business reported strong revenue growth of 27% YoY and 40% QoQ to Rs 355mn on account of recovery in demand. GLS signed a definitive multi-year agreement with an innovator for the supply of APIs, which is scheduled to be commercialised in FY25. In addition, management indicated that multiple discussions are ongoing with companies globally for further business opportunities in the CDMO space.

Better product mix and favourable input costs lift gross margin: GLS’s gross margin expanded 670bps YoY to 57.7% due to a better product mix tilted towards the high-margin CDMO business. Input costs too were favourable as well as the Chinese supply chain has improved and shipments are on track. Employee cost, however, was on the higher side at 13% of sales vs. an average of 9% because of incentive disbursement. Management expects costs to normalise from Q1FY25 onwards. EBITDA margin increased 320bps YoY to 30.1%, supporting EBITDA/PAT growth of 19%/13% YoY to Rs 1.7bn/Rs 1.2bn for the quarter.

Fully valued; maintain HOLD: We raise our FY24 earnings estimate by 6% to reflect the sharp uptick in gross and EBITDA margins and our expectations of a similar trend in Q4FY24. We also raise FY25/FY26 earnings by 8%/4% to factor in the new CDMO contract. Our two-step DCF model yields a revised TP of Rs 765 (from Rs 620), but still offers only 4% upside following the recent stock rally. We thus maintain our HOLD rating.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	GLS IN/Rs 800
Market cap	US\$ 1.2bn
Free float	17%
3M ADV	US\$ 1.3mn
52wk high/low	Rs 808/Rs 370
Promoter/FPI/DII	83%/5%/1%

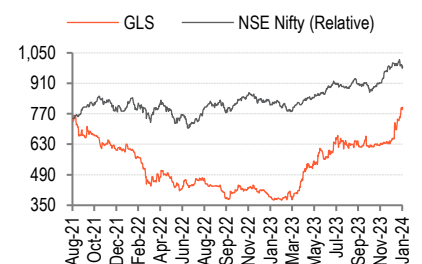
Source: NSE | Price as of 24 Jan 2024

Key financials

Y/E 31 Mar	FY23A	FY24E	FY25E
Total revenue (Rs mn)	21,613	24,495	27,847
EBITDA (Rs mn)	6,424	7,638	9,098
Adj. net profit (Rs mn)	4,691	5,545	6,551
Adj. EPS (Rs)	38.3	45.3	53.5
Consensus EPS (Rs)	38.3	41.8	50.5
Adj. ROAE (%)	22.0	23.4	23.4
Adj. P/E (x)	20.9	17.7	15.0
EV/EBITDA (x)	15.5	12.3	10.3
Adj. EPS growth (%)	12.0	18.2	18.1

Source: Company, Bloomberg, BOBCAPS Research

Stock performance



Source: NSE



Fig 1 – Quarterly performance

(Rs mn)	Q3FY24	Q3FY23	YoY (%)	Q2FY24	QoQ (%)	9MFY24	9MFY23	YoY (%)
Total Income	5,728	5,407	5.9	5,954	(3.8)	17,467	15,400	13.4
EBITDA	1,726	1,455	18.6	1,671	3.2	5,329	4,360	22.2
Depreciation	132	108	-	131	-	389	306	-
EBIT	1,594	1,347	18.3	1,540	3.5	4,940	4,054	21.8
Interest	4	2	-	4	-	12	4	-
Other Income	17	66	-	54	-	89	261	-
PBT	1,607	1,411	13.8	1,590	1.1	5,017	4,311	16.4
Less: Taxation	419	361	--	402	-	1,287	1,104	-
Less: Minority Interest	0	0	-	0	-	0	0	-
Recurring PAT	1,188	1,050	13.1	1,188	0.0	3,730	3,207	16.3
Exceptional items	0	0	-	0	-	0	0	-
Reported PAT	1,188	1,050	13.1	1,188	0.0	3,730	3,207	16.3
Key Ratios (%)								
			(bps)		(bps)			(bps)
Gross Margin	57.7	51.0	669	54.1	358	56.3	52.4	394
EBITDA Margin	30.1	26.9	322	28.1	206	30.5	28.3	220
Tax / PBT	26.1	25.6	-	25.3	-	25.6	25.6	-
NPM	21.8	20.7	108	20.9	84	22.4	21.9	46
EPS	9.7	8.6	13.1	9.7	0.0	30.4	26.2	16.3

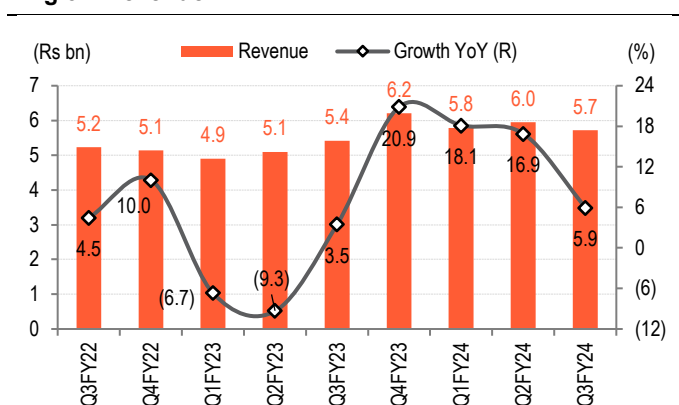
Source: Company, BOBCAPS Research

Fig 2 – Revenue mix

(Rs mn)	Q3FY24	Q3FY23	YoY (%)	Q2FY24	QoQ (%)	9MFY23	9MFY23	YoY (%)
Generic API	5,105	4,799	6.4	5,428	(6.0)	15,575	13,781	13.0
CDMO	355	279	27.1	253	40.3	1,072	832	28.9
Net Sales	5,460	5,078	7.5	5,681	(3.9)	16,647	14,612	13.9
OOI	268	329	(18.5)	273	(1.8)	820	788	4.1
Revenues	5,728	5,407	5.9	5,954	(3.8)	17,467	15,400	13.4

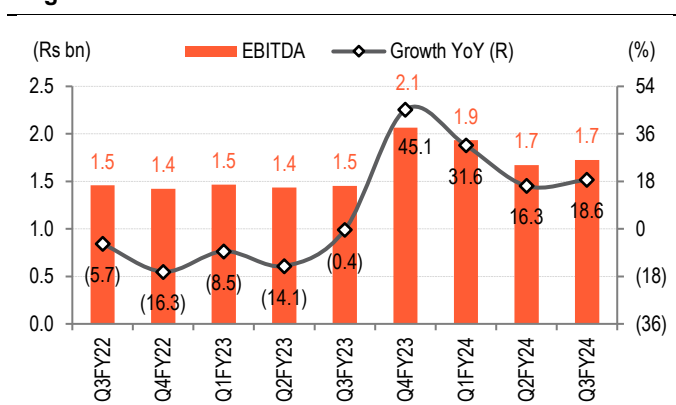
Source: Company, BOBCAPS Research

Fig 3 – Revenue



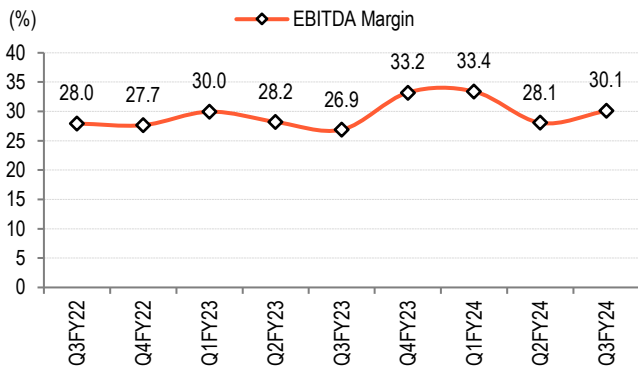
Source: Company, BOBCAPS Research

Fig 4 – EBITDA



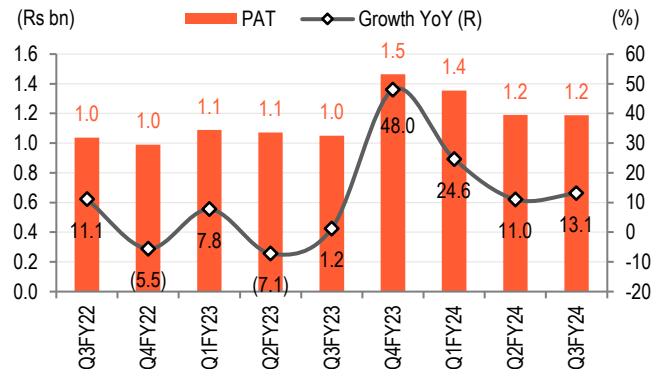
Source: Company, BOBCAPS Research

Fig 5 – EBITDA Margin



Source: Company, BOBCAPS Research

Fig 6 – PAT

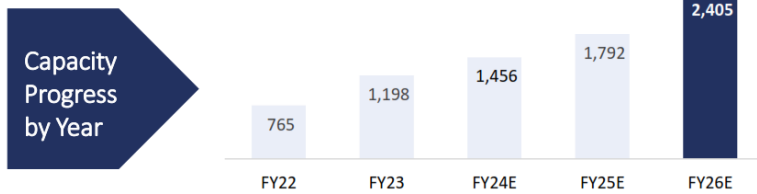


Source: Company, BOBCAPS Research

Fig 7 – Capacity expansion plan

Expansion Type	Division	Location	Status & Planned Capacity	Operational Timelines
Brownfield	API / Intermediate	Ankleshwar	208 KL (Under Construction)	Q4 FY24
			Planned addition of 280KL-300KL	FY25-FY26
Brownfield	API	Dahej	Planned addition of 220KL-240KL	FY25-FY26
Greenfield	API	Solapur	CTE received for 1,000MT ~500 KL capacity will be operational by FY26	FY26

Total Reactor Capacity Expansion Plan (KL)



- ✓ **Backward Integration plant at Ankleshwar of 208KL is under construction.**
- ✓ **Engineering work started for construction at Solapur Plant of 200KL (Phase 1).**
- ✓ **Solapur's further capacity expansion will be calibrated as per the volume demand**

Source: Company, BOBCAPS Research

Valuation methodology

We raise our FY24 earnings estimate for GLS by 6% to reflect the sharp uptick in gross and EBITDA margins and our expectations of a similar trend in Q4FY24. We also raise FY25/FY26 earnings by 8%/4% to factor in the new CDMO contract which is to be commercialised from FY25. Our two-step DCF model yields a revised TP of Rs 765 (from Rs 620), but still offers only 4% upside following the recent stock rally. We thus maintain our HOLD rating.

Fig 8 – Revised estimates

(Rs bn)	New			Old			Change (%)		
	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E	FY24E	FY25E	FY26E
Sales	24.5	27.8	30.6	24.5	27.5	30.0	(0.0)	1.3	1.7
EBITDA	7.6	9.1	9.8	7.3	8.4	9.7	4.7	8.5	1.6
EBITDA margin (%)	31.2	32.7	32.2	29.8	30.5	32.3	140bps	215bps	(6bps)
EPS (Rs)	45.3	53.5	57.0	42.7	49.3	55.0	6.0	8.4	3.5

Source: BOBCAPS Research

Fig 9 – Key assumptions

Revenue (Rs bn)	FY23	FY24E	FY25E	FY26E
Generic API	19.1	21.9	24.8	27.3
CDMO	1.4	1.5	1.9	2.1
OOI	1.1	1.1	1.1	1.2

Source: Company, BOBCAPS Research

Fig 10 – DCF valuation summary

Variables	Assumptions	Basis
Risk Free Rate (%) (A)	7.4	10Y Average GIND10Y Index
Equity Risk Premium (%) (B)	6.1	(Rm-Rf)
Beta (C)	0.7	5Y Average Beta of Nifty Pharma
Cost of Equity (%) (D) = A + B x C	11.5	
Cost of Debt (%) (E)	NA	Debt-free
Marginal Tax Rate (%) (F)	25	
Post-Tax Cost of Debt (%) (G) = E x (1-F)	0	Debt-free
Current Debt to Equity (2023) (H)	0	
WACC (%) (I) = (1 x D + H x G)/(1 + H)	11.5	
	Stage 1	Stage 2 (Terminal)
FCF CAGR (FY23-FY33E) (%)	26	3

Source: BOBCAPS Research

Key risks

Key upside risks to our estimates are:

- **CDMO resolution:** CDMO is a lumpy business and faster than anticipated ramp-up could take revenue above our estimates.
- **Higher volumes:** Increased volume offtake from formulation companies given ongoing drug shortages in the US represents an upside risk to our assumptions.

Key downside risks to our estimates are:

- **Regulatory lapses:** The US and the EU are key geographies for GLS's clientele, implying a potential risk of lapses in maintaining the strict cGMP standards required by regulators in these markets. There have, however, been no regulatory lapses at the company's manufacturing plants to date.
- **Customer concentration:** GLS derives more than half of its revenue from its top 5 customers, pointing to potential revenue concentration risk.
- **Raw material supply disruptions:** Periodic uncertainty regarding the supply chain out of China and other geographies due to various factors, including geopolitical tensions, poses risks to our assumptions of growth and raw material costs in the near-to-medium term.
- **Pricing pressure:** Pricing pressure from customers may affect gross margins, profitability, and the ability to increase prices.

Glossary

Glossary of Abbreviations			
API	Active Pharmaceutical Ingredient	cGMP	Current Good Manufacturing Practices
CDMO	Contract Development and Manufacturing Operations	LATAM	Latin America
CNS	Central Nervous System	PLI	Production Linked Incentives
CVS	Cardiovascular		

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Total revenue	21,232	21,613	24,495	27,847	30,563
EBITDA	6,160	6,424	7,638	9,098	9,845
Depreciation	379	401	466	524	717
EBIT	5,782	6,023	7,173	8,574	9,127
Net interest inc./(exp.)	(280)	(5)	(15)	0	0
Other inc./(exp.)	147	290	120	160	176
Exceptional items	0	0	0	0	0
EBT	5,649	6,307	7,279	8,734	9,304
Income taxes	1,462	1,616	1,733	2,184	2,326
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	4,187	4,691	5,545	6,551	6,978
Adjustments	0	0	0	0	0
Adjusted net profit	4,187	4,691	5,545	6,551	6,978

Balance Sheet

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Accounts payables	3,077	3,966	3,205	3,659	4,026
Other current liabilities	602	901	702	801	294
Provisions	144	155	178	203	223
Debt funds	29	194	0	0	0
Other liabilities	0	0	0	0	0
Equity capital	245	245	245	245	245
Reserves & surplus	20,613	21,561	25,443	30,028	34,913
Shareholders' fund	20,858	21,806	25,688	30,273	35,158
Total liab. and equities	24,710	27,021	29,772	34,936	39,700
Cash and cash eq.	5,122	3,094	4,942	7,389	10,058
Accounts receivables	6,735	8,068	8,012	9,147	10,064
Inventories	5,162	6,042	6,410	7,317	8,051
Other current assets	823	1,395	1,404	1,602	1,763
Investments	1	1	1	1	1
Net fixed assets	5,846	7,749	8,334	8,818	9,102
CWIP	970	616	616	616	616
Intangible assets	51	57	53	45	44
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	24,710	27,021	29,772	34,936	39,700

Cash Flows

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24E	FY25E	FY26E
Cash flow from operations	6,230	3,512	4,766	5,412	5,763
Capital expenditures	(588)	(2,257)	(1,018)	(1,000)	(1,000)
Change in investments	0	0	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(588)	(2,257)	(1,018)	(1,000)	(1,000)
Equities issued/Others	225	0	0	0	0
Debt raised/repaid	(9,522)	165	(194)	0	0
Interest expenses	(280)	(5)	(15)	0	0
Dividends paid	(2,579)	(1,407)	(1,664)	(1,965)	(2,093)
Other financing cash flows	10,480	(2,034)	(28)	0	0
Cash flow from financing	(1,675)	(3,282)	(1,900)	(1,965)	(2,093)
Chg in cash & cash eq.	3,966	(2,027)	1,848	2,447	2,669
Closing cash & cash eq.	5,122	3,094	4,942	7,389	10,058

Per Share

Y/E 31 Mar (Rs)	FY22A	FY23A	FY24E	FY25E	FY26E
Reported EPS	34.2	38.3	45.3	53.5	57.0
Adjusted EPS	34.2	38.3	45.3	53.5	57.0
Dividend per share	21.1	11.5	13.6	16.0	17.1
Book value per share	170.2	178.0	209.7	247.1	286.9

Valuations Ratios

Y/E 31 Mar (x)	FY22A	FY23A	FY24E	FY25E	FY26E
EV/Sales	5.1	4.6	3.8	3.4	3.0
EV/EBITDA	17.4	15.5	12.3	10.3	9.3
Adjusted P/E	23.4	20.9	17.7	15.0	14.0
P/BV	4.7	4.5	3.8	3.2	2.8

DuPont Analysis

Y/E 31 Mar (%)	FY22A	FY23A	FY24E	FY25E	FY26E
Tax burden (Net profit/PBT)	74.1	74.4	76.2	75.0	75.0
Interest burden (PBT/EBIT)	97.7	104.7	101.5	101.9	101.9
EBIT margin (EBIT/Revenue)	27.2	27.9	29.3	30.8	29.9
Asset turnover (Rev./Avg TA)	27.8	25.2	25.7	24.9	23.4
Leverage (Avg TA/Avg Equity)	1.3	1.0	1.0	1.0	1.0
Adjusted ROAE	29.3	22.0	23.4	23.4	21.3

Ratio Analysis

Y/E 31 Mar	FY22A	FY23A	FY24E	FY25E	FY26E
YoY growth (%)					
Revenue	12.6	1.8	13.3	13.7	9.8
EBITDA	4.2	4.3	18.9	19.1	8.2
Adjusted EPS	4.8	12.0	18.2	18.1	6.5
Profitability & Return ratios (%)					
EBITDA margin	29.0	29.7	31.2	32.7	32.2
EBIT margin	27.2	27.9	29.3	30.8	29.9
Adjusted profit margin	19.7	21.7	22.6	23.5	22.8
Adjusted ROAE	29.3	22.0	23.4	23.4	21.3
ROCE	31.0	29.4	30.6	31.2	28.4
Working capital days (days)					
Receivables	118	144	125	125	125
Inventory	90	108	100	100	100
Payables	54	71	50	50	50
Ratios (x)					
Gross asset turnover	3.0	2.3	2.4	2.4	2.5
Current ratio	4.7	3.7	5.1	5.5	6.6
Net interest coverage ratio	20.7	1,101.1	494.1		
Adjusted debt/equity	(0.2)	(0.1)	(0.2)	(0.2)	(0.3)

Source: Company, BOBCAPS Research | Note: TA = Total Assets

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Registered office Address: **1704, B Wing, Parinee Crescenzo, G Block, BKC, Bandra East, Mumbai 400051**

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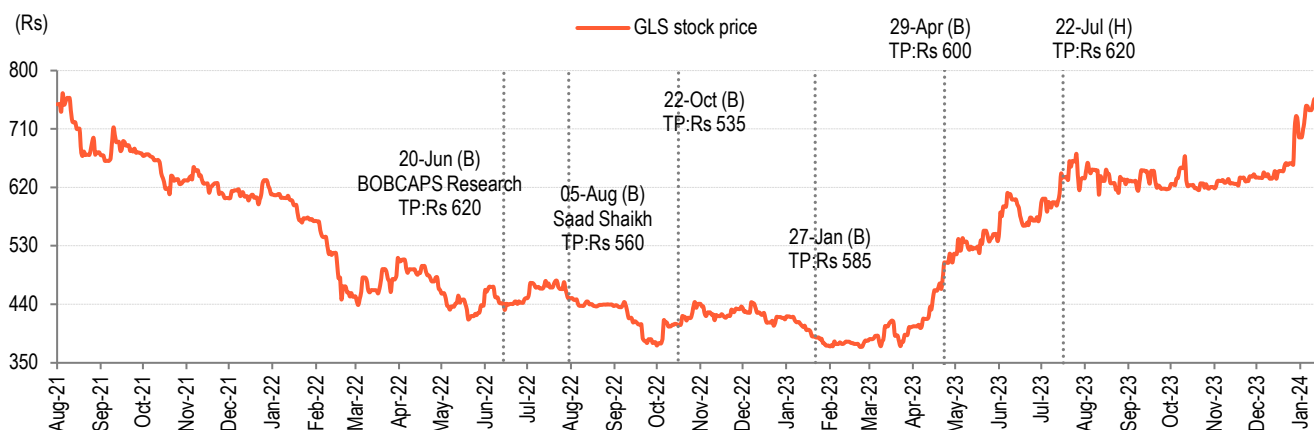
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SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

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Ratings and Target Price (3-year history): GLENMARK LIFE SCIENCES (GLS IN)



B – Buy, H – Hold, S – Sell, A – Add, R – Reduce

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