

HOLD
TP: Rs 790 | ▼ 3%

GLENMARK LIFE SCIENCES

| Pharmaceuticals

| 26 April 2024

Weak quarter; maintain HOLD

- Lower-than-expected 4Q due to Red Sea disruptions. EBITDA/PAT were 17% below consensus estimates
- Changes in accounting policies with new promoters and lower PLI benefit impacted margins. Confident of 28-30% EBITDA margin in FY25
- FY25-FY26 earnings tweaked; move to EV/EBITDA valuation. Raise TP to Rs 790 (from Rs 765). Retain HOLD.

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Generic API business impacted by supply chain disruptions: GLS reported 14% YoY decline in Q4 revenue to Rs 5.4bn (-6% QoQ) owing to delayed shipments due to the ongoing disruption in the Red Sea and, to some extent changes, in revenue recognition patterns with the change in ownership in Nirma. Management maintained that the orderbook remains strong and there is demand visibility. The Glenmark Pharma (GPL) business recovered sequentially with QoQ growth of 8.1% (-28% YoY). Generic API revenues declined by 9% YoY and by (-5.1% QoQ), impacted by the Red Sea crisis in external business and degrowth in GPL's business. Regions like Europe and LATAM contributed to growth YoY. External business saw de-growth of 5.2% YoY and 11.7% QoQ on delayed shipments due to the Red Sea conflict. External business saw positive YoY growth in Europe and LATAM.

New CDMO contract to commercialise from Q3FY25; growth and margin to remain intact: The CDMO business was stable sequentially but last year's high base resulted in a YoY decline of 38%. The multi-year definitive agreement with an innovator for supply of API will commercialise in Q3FY25. Management expects sales growth of low-to-mid teens, while maintaining EBITDA margin at 28-30% in FY25. The company's fourth CDMO project is to go commercial by 2HFY25 or a bit earlier. The company's fifth CDMO project in its pipeline will commercialise from 4QFY25.

Reduced PLI benefit and one-time impact of bonus on margin: Change in product mix as well as high employee cost on account of the one-time bonus to employees impacted EBITDA margin of 26.4% by 700bps YoY. The company also saw reduced productivity-linked incentive (PLI) benefit impacting gross margins and expects 100-150bps impact on gross margins going forward due to lack of PLI benefit.

Retain HOLD; raise TP to Rs 790: We have tweaked our FY25-FY26 earnings assumptions and move to an EV/EBITDA valuation. Thus, we raise our TP to Rs 790 (Rs 765 earlier) based on 10x FY26E EV/EBITDA, with an implied P/E of 14x.

Key changes

Target	Rating
▲	◀ ▶

Ticker/Price	GLS IN/Rs 815
Market cap	US\$ 1.2bn
Free float	17%
3M ADV	US\$ 1.6mn
52wk high/low	Rs 906/Rs 465
Promoter/FPI/DII	83%/5%/1%

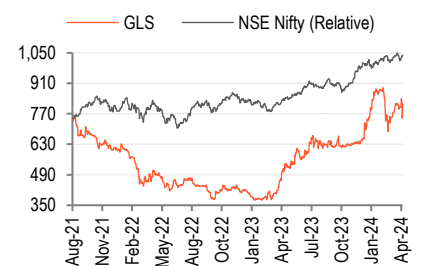
Source: NSE | Price as of 26 Apr 2024

Key financials

Y/E 31 Mar	FY24P	FY25E	FY26E
Total revenue (Rs mn)	22,833	26,584	29,838
EBITDA (Rs mn)	6,743	8,804	9,837
Adj. net profit (Rs mn)	4,710	6,224	6,806
Adj. EPS (Rs)	38.4	50.8	55.5
Consensus EPS (Rs)	38.4	50.5	55.1
Adj. ROAE (%)	20.6	23.9	22.3
Adj. P/E (x)	21.2	16.0	14.7
EV/EBITDA (x)	14.2	11.0	9.8
Adj. EPS growth (%)	0.4	32.2	9.4

Source: Company, Bloomberg, BOBCAPS Research | P – Provisional

Stock performance



Source: NSE



Fig 1 – Quarterly performance

(Rs mn)	Q4FY24	Q4FY23	YoY (%)	Q3FY24	QoQ (%)	FY24	FY23	YoY (%)
Revenue	5,366	6,213	(13.6)	5,728	(6.3)	22,833	21,613	5.6
EBITDA	1,414	2,064	(31.5)	1,726	(18.0)	6,743	6,424	5.0
Depreciation	145	115	-	132	-	535	421	-
EBIT	1,269	1,949	(34.9)	1,594	(20.4)	6,209	6,003	3.4
Interest	4	1	-	4	-	15	5	-
Other Income	31	28	-	17	-	120	290	-
PBT	1,297	1,976	(34.4)	1,607	(19.3)	6,314	6,287	0.4
Less: Taxation	317	513	-	419	-	1,604	1,616	-
Less: Minority Interest	0	0	-	0	-	0	0	-
Recurring PAT	979	1,463	(33.1)	1,188	(17.5)	4,710	4,671	0.8
Exceptional items	0	0	-	0	-	0	0	-
Reported PAT	979	1,463	(33.1)	1,188	(17.5)	4,710	4,671	0.8
Key Ratios (%)			(bps)		(bps)			(bps)
Gross Margin	55.5	54.9	64	57.7	(220)	54.1	50.5	365
EBITDA Margin	26.4	33.2	(686)	30.1	(376)	29.5	29.7	(19)
Tax / PBT	24.5	25.9	-	26.1	-	25.4	25.7	-
NPM	18.8	24.9	(611)	21.8	(292)	21.6	22.8	(125)
EPS	8.0	11.9	(33.1)	9.7	(17.5)	43.3	38.1	0.1

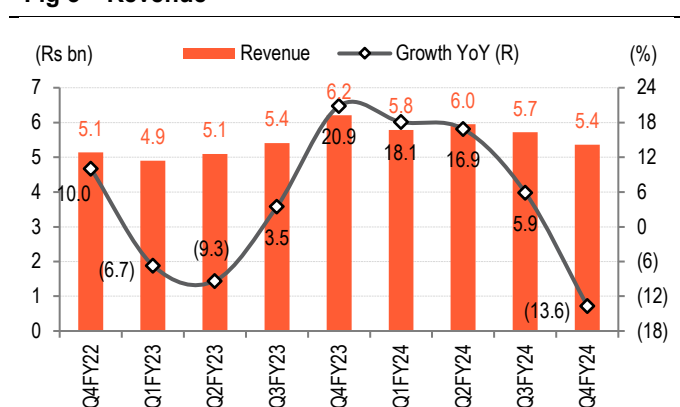
Source: Company, BOBCAPS Research

Fig 2 – Revenue mix

(Rs mn)	Q4FY24	Q4FY23	YoY (%)	Q3FY24	QoQ (%)	FY24	FY23	YoY (%)
Generic API	4,846	5,299	(8.5)	5,105	(5.1)	20,421	19,080	7.0
CDMO	354	568	(37.7)	355	(0.3)	1,426	1,400	1.9
Net Sales	5,200	5,867	(11.4)	5,460	(4.8)	21,847	20,479	6.7
OOI	166	346	(52.0)	268	(38.1)	986	1,134	(13.0)
Revenues	5,366	6,213	(13.6)	5,728	(6.3)	22,833	21,613	5.6

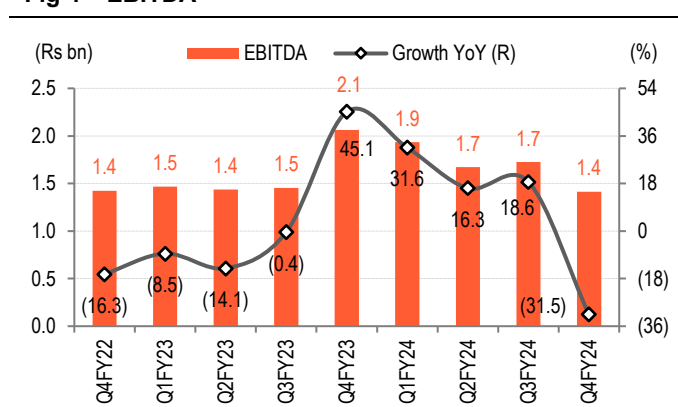
Source: Company, BOBCAPS Research

Fig 3 – Revenue



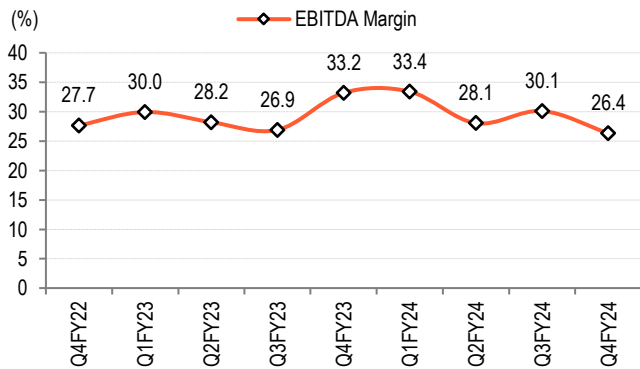
Source: Company, BOBCAPS Research

Fig 4 – EBITDA



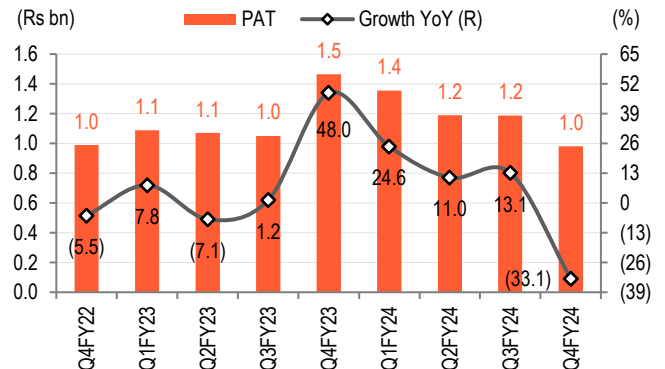
Source: Company, BOBCAPS Research

Fig 5 – EBITDA margin



Source: Company, BOBCAPS Research

Fig 6 – PAT



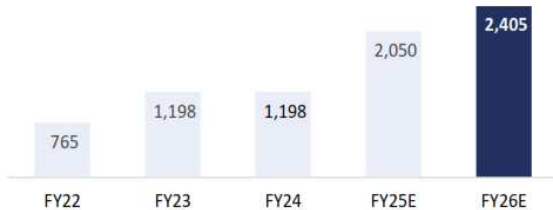
Source: Company, BOBCAPS Research

Fig 7 – Capacity expansion plans

Expansion Type	Division	Location	Status & Planned Capacity	Operational Timelines
Brownfield	API / Intermediate	Ankleshwar	208 KL (Construction Completed)	Q1 FY25
			Planned addition of 280KL-300KL	FY25-FY26
Brownfield	API	Dahej	18 KL (Construction Completed)	Q1 FY25
			Planned addition of 100 KL-120 KL	FY25-FY26
Greenfield	API	Solapur	Phase 1 – 200 KL (Construction started)	FY26
			Phase 2 - Planned addition of 400 KL	FY27

Total Reactor Capacity Expansion Plan (KL)

Capacity Progress by Year



- ✓ Backward Integration plant at Ankleshwar of 208 KL construction is completed and will be operational in Q1FY25
- ✓ Construction work started at Solapur Plant of 200 KL (Phase 1)
- ✓ Solapur's further capacity expansion will be calibrated as per the volume demand

Source: Company, BOBCAPS Research | KL = Kilo Litre

Earnings call takeaways:

- **Nirma's completes GLS acquisition:** Nirma has completed its acquisition of GLS but will continue the existing strategies for growth with greater availability of capital to be deployed in new ventures.
- **R&D pipeline:** GLS has six new products in the development grid, of which four products are highly potent API / Oncology class of drugs and two are synthetic small molecules. The HP API portfolio now extends to 17 products with an addressable market of US\$ 37bn. Three products are validated, and four are in advanced stages of development. Development is progressing for iron complexes in the grid. Filing has been completed for one iron complex with two others in advanced stages of development.
- **Employee cost:** High employee cost mainly on account of the one-time bonus to employees.
- **PLI benefit:** Company to see 100-150bps impact on gross margins going forward.
- **Capex:** Investment on capex to be ~Rs 3.4bn in FY25, of which ~Rs 1.4bn is to be deployed at Solapur greenfield site.
 - Backward integration plant at Ankleshwar of 208 kilo litre (KL) construction has been completed and will be operational in Q1FY25.
 - Construction work started at Solapur Plant of 200 KL (Phase 1).
 - Solapur's further capacity expansion will be calibrated as per volume demand.
- **Working capital:** Working capital days at 170 days – maintaining slightly high inventories due to Red Sea crisis.
- **Robust balance sheet:** Strong free cash flow of Rs 2.8bn, leading to cash and cash equivalents of Rs 3.0bn as of 31 Mar 2024 (post payment of interim dividend of Rs 2.8bn).

Valuation methodology

We remain optimistic about growth prospects and margin trajectory of GLS as we believe the external factors affecting the performance in recent quarters are transitory. Management has guided for sales growth of low-to-mid teens, while maintaining EBITDA margin at 28-30% in FY25. It intends to spend ~Rs 3.4bn on capex in FY25, a large part of which is to be invested in the Solapur greenfield facility.

On the back of new capacities coming up, commercialisation of new CDMO projects and strong track record of operating margins, we expect GLS to post 21% earnings CAGR over FY24-26.

We have tweaked our FY25-FY26 earnings assumptions and move to an EV/EBITDA valuation. Our TP thus gets revised to Rs 790 (Rs 765 earlier) based on 10x FY26 EV/EBITDA, an implied P/E of 14x.

Fig 8 – Revised estimates

(Rs bn)	New		Old		Change (%)	
	FY25E	FY26E	FY25E	FY26E	FY25E	FY26E
Sales	26.5	29.7	27.8	30.6	(4.7)	(2.7)
EBITDA	8.8	9.7	9.1	9.8	(3.8)	(1.0)
EBITDA margin (%)	33.0	32.8	32.7	32.2	32bps	54bps
EPS (Rs)	50.9	56.2	53.5	57.0	(4.9)	(1.3)

Source: BOBCAPS Research

Fig 9 – Key assumptions

Revenue (Rs bn)	FY24A	FY25E	FY26E
Generic API	20.4	23.5	26.5
CDMO	1.4	1.9	2.1
OOI	1.0	1.1	1.2

Source: Company, BOBCAPS Research

Key risks

Key upside risks to our estimates are:

- **CDMO resolution:** CDMO is a lumpy business and the 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 five 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, pose risks to our assumptions of growth and raw material costs in the near-to-medium term.
- **Pricing pressure:** Pricing pressure in API may affect gross margins, profitability, and the ability to increase prices.

Sector recommendation snapshot

Company	Ticker	Market Cap (US\$ bn)	Price (Rs)	Target (Rs)	Rating
Alembic Pharma	ALPM IN	2.4	990	970	HOLD
Alkem Labs	ALKEM IN	7.1	4,910	4,800	SELL
Aurobindo Pharma	ARBP IN	8.1	1,131	1,100	HOLD
Cipla	CIPLA IN	13.8	1,409	1,576	BUY
Divi's Labs	DIVI IN	13.0	4,016	3,000	SELL
Dr Reddy's Labs	DRRD IN	12.7	6,252	5,900	HOLD
Eris Lifesciences	ERIS IN	1.5	893	955	BUY
Glenmark Life Sciences	GLS IN	1.2	815	790	HOLD
Laurus Labs	LAURUS IN	2.9	437	305	SELL
Lupin	LPC IN	8.9	1,616	1,560	HOLD
Sun Pharma	SUNP IN	44.0	1,507	1,550	HOLD

Source: BOBCAPS Research, NSE | Price as of 26 Apr 2024

Glossary

Glossary of Abbreviations			
API	Active Pharmaceutical Ingredient	LATAM	Latin America
HP API	High Performance API	PLI	Production Linked Incentives
CDMO	Contract Development and Manufacturing Operations	cGMP	Current Good Manufacturing Practices
OOI	Other Operating Income		

Financials

Income Statement

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24P	FY25E	FY26E
Total revenue	21,232	21,613	22,833	26,584	29,838
EBITDA	6,160	6,424	6,743	8,804	9,837
Depreciation	379	401	534	652	934
EBIT	5,782	6,023	6,209	8,152	8,903
Net interest inc./(exp.)	(280)	(5)	(15)	(5)	0
Other inc./(exp.)	147	290	120	152	171
Exceptional items	0	0	0	0	0
EBT	5,649	6,307	6,314	8,299	9,075
Income taxes	1,462	1,616	1,604	2,075	2,269
Extraordinary items	0	0	0	0	0
Min. int./Inc. from assoc.	0	0	0	0	0
Reported net profit	4,187	4,691	4,710	6,224	6,806
Adjustments	0	0	0	0	0
Adjusted net profit	4,187	4,691	4,710	6,224	6,806

Balance Sheet

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24P	FY25E	FY26E
Accounts payables	3,077	3,966	3,687	3,828	4,306
Other current liabilities	602	901	557	762	286
Provisions	144	155	278	323	364
Debt funds	29	194	171	0	0
Other liabilities	0	0	0	0	0
Equity capital	245	245	245	245	245
Reserves & surplus	20,613	21,561	23,566	27,923	32,687
Shareholders' fund	20,858	21,806	23,811	28,168	32,932
Total liab. and equities	24,710	27,021	28,504	33,081	37,887
Cash and cash eq.	5,122	3,094	3,016	3,719	4,314
Accounts receivables	6,735	8,068	7,654	8,699	9,785
Inventories	5,162	6,042	6,666	6,959	7,828
Other current assets	823	1,395	2,057	1,524	1,714
Investments	1	1	1	1	1
Net fixed assets	5,846	7,749	7,950	11,050	13,099
CWIP	970	616	1,060	1,060	1,060
Intangible assets	51	57	101	69	86
Deferred tax assets, net	0	0	0	0	0
Other assets	0	0	0	0	0
Total assets	24,710	27,021	28,504	33,081	37,887

Cash Flows

Y/E 31 Mar (Rs mn)	FY22A	FY23A	FY24P	FY25E	FY26E
Cash flow from operations	6,230	3,512	3,887	6,467	5,636
Capital expenditures	(588)	(2,257)	(1,058)	(3,400)	(3,000)
Change in investments	0	0	0	0	0
Other investing cash flows	0	0	0	0	0
Cash flow from investing	(588)	(2,257)	(1,058)	(3,400)	(3,000)
Equities issued/Others	225	0	0	0	0
Debt raised/repaid	(9,522)	165	(22)	(171)	0
Interest expenses	(280)	(5)	(15)	(5)	0
Dividends paid	(2,579)	(1,407)	(1,413)	(1,867)	(2,042)
Other financing cash flows	10,480	(2,034)	(1,457)	(320)	0
Cash flow from financing	(1,675)	(3,282)	(2,907)	(2,364)	(2,042)
Chg in cash & cash eq.	3,966	(2,027)	(78)	703	595
Closing cash & cash eq.	5,122	3,094	3,016	3,719	4,314

Per Share

Y/E 31 Mar (Rs)	FY22A	FY23A	FY24P	FY25E	FY26E
Reported EPS	34.2	38.3	38.4	50.8	55.5
Adjusted EPS	34.2	38.3	38.4	50.8	55.5
Dividend per share	21.1	11.5	22.5	22.5	22.5
Book value per share	170.2	178.0	194.3	229.9	268.8

Valuations Ratios

Y/E 31 Mar (x)	FY22A	FY23A	FY24P	FY25E	FY26E
EV/Sales	5.2	4.7	4.2	3.6	3.2
EV/EBITDA	17.8	15.8	14.2	11.0	9.8
Adjusted P/E	23.8	21.3	21.2	16.0	14.7
P/BV	4.8	4.6	4.2	3.5	3.0

DuPont Analysis

Y/E 31 Mar (%)	FY22A	FY23A	FY24P	FY25E	FY26E
Tax burden (Net profit/PBT)	74.1	74.4	74.6	75.0	75.0
Interest burden (PBT/EBIT)	97.7	104.7	101.7	101.8	101.9
EBIT margin (EBIT/Revenue)	27.2	27.9	27.2	30.7	29.8
Asset turnover (Rev./Avg TA)	27.8	25.2	24.8	25.5	24.4
Leverage (Avg TA/Avg Equity)	1.3	1.0	1.0	1.0	1.0
Adjusted ROAE	29.3	22.0	20.6	23.9	22.3

Ratio Analysis

Y/E 31 Mar	FY22A	FY23A	FY24P	FY25E	FY26E
YoY growth (%)					
Revenue	12.6	1.8	5.6	16.4	12.2
EBITDA	4.2	4.3	5.0	30.6	11.7
Adjusted EPS	4.8	12.0	0.4	32.2	9.4
Profitability & Return ratios (%)					
EBITDA margin	29.0	29.7	29.5	33.1	33.0
EBIT margin	27.2	27.9	27.2	30.7	29.8
Adjusted profit margin	19.7	21.7	20.6	23.4	22.8
Adjusted ROAE	29.3	22.0	20.6	23.9	22.3
ROCE	31.0	29.4	27.5	31.8	29.7
Working capital days (days)					
Receivables	118	144	128	125	125
Inventory	90	108	111	100	100
Payables	54	71	62	55	55
Ratios (x)					
Gross asset turnover	3.0	2.3	2.2	1.9	1.8
Current ratio	4.7	3.7	4.3	4.3	4.8
Net interest coverage ratio	20.7	1,101.1	401.6	1,584.6	
Adjusted debt/equity	(0.2)	(0.1)	(0.1)	(0.1)	(0.1)

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

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BUY – Expected return >+15%

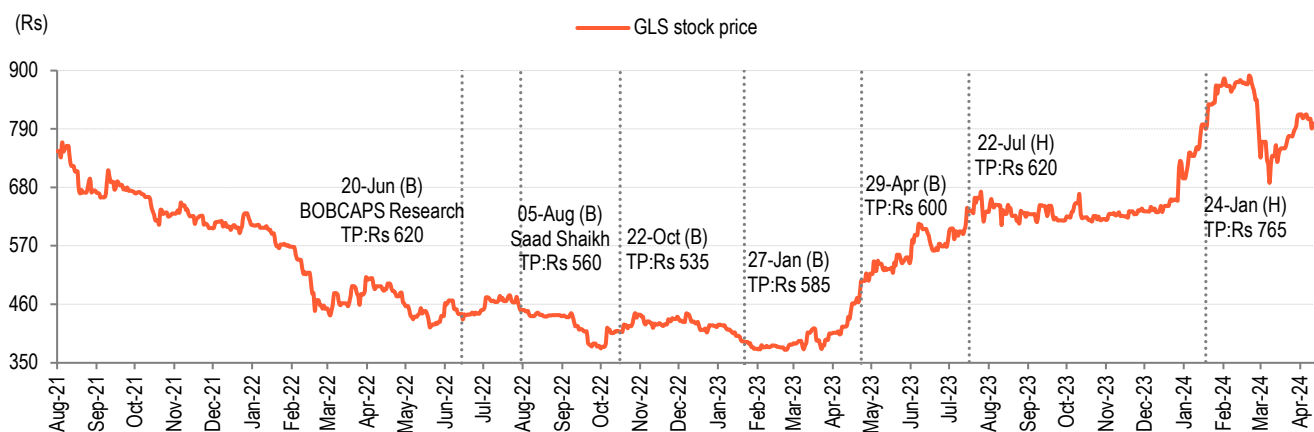
HOLD – Expected return from -6% to +15%

SELL – Expected return <-6%

Note: Recommendation structure changed with effect from 21 June 2021

Our recommendation scale does not factor in short-term stock price volatility related to market fluctuations. Thus, our recommendations may not always be strictly in line with the recommendation scale as shown above.

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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