

## Glenmark Pharmaceuticals

 BSE code: 532296  
 NSE code: GLENMARK

**CMP: Rs 625**
**Target: Rs 700** ↑

**BUY**
**Alok Dalal**

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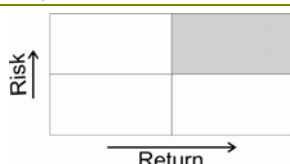
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**Company data**

Particulars	
Market cap (Rs bn / US\$ bn)	155.4/3.9
Outstanding equity shares (mn)	248.1
52-week high/low (Rs)	627/351
3-month average daily volume	136,524

**Financial snapshot**

Particulars	FY08	FY09E	FY10E
Sales (Rs mn)	19,783.4	25,667.2	35,183.4
Growth (%)	58.1	29.7	37.1
Adj net inc (Rs mn)	6,312.7	8,122.0	10,594.0
Growth (%)	103.6	28.7	30.4
FDEPS (Rs)	23.9	30.8	40.2
Growth (%)	103.6	28.7	30.4
P/E (x)	26.1	20.3	15.6
ROE (%)	63.4	47.8	40.5

**Risk-return profile**

**Shareholding pattern**

(%)	Mar-08	Dec-07
Promoters	52.4	52.5
FIIIs	27.9	26.5
Banks & FIs	3.9	4.2
Public	15.8	16.8

**Stock performance**

Returns (%)	CMP	1-mth	3-mth	6-mth
Glenmark	625	23.0	20.2	40.2
Sensex	17,016	3.9	(5.9)	(14.8)
BSEHC	4,216	9.4	14.9	7.4

**Company website** [www.glenmarkpharma.com](http://www.glenmarkpharma.com)
**Robust quarter; we upgrade estimates on upbeat guidance**

Glenmark Pharma's Q4FY08 results are broadly in line with our estimates. All-round growth in key geographies, barring Latin America, has fuelled a 64% YoY growth in sales to Rs 5.7bn. The company received US\$ 15mn as out-licensing revenue from Forest Labs during the quarter for its lead candidate, Oglemilast, which led to a 1,050bps YoY expansion in the EBITDA margin. A strong operational performance, higher other income and lower tax outgo led to a 252% jump in PAT to Rs 2.2bn.

FY08 has been a very strong year for Glenmark across geographies, both in terms of sales and profitability. The year also witnessed traction on the NCE R&D front. Based on the robust performance, the management has raised its sales and profit guidance by ~10% for FY09 and ~18% for FY10. We believe the guidance is attainable considering Glenmark's established infrastructure in key markets. The management guidance factors in only US\$ 69mn from out-licensing revenue, which could yield a significant positive upside. Rupee appreciation presents a key risk to the guidance.

We have incorporated the revised management outlook into our estimates and raised our FY09 and FY10 FDEPS by 15.3% and 23.6% to Rs 30.8 and Rs 40.2 respectively. We thus have a revised target price of Rs 700 for the stock arrived at as follows: a) non-R&D business valued at Rs 479.1/share based on 18x FY10E FDEPS of Rs 26.6, and b) NCE research valued at Rs 220.4/share. We maintain a Buy rating.

**Actual vs estimated performance**

(Rs mn)	Actual	Estimated	% Variance
Net sales	5,726.9	6,052.0	(5.4)
EBITDA	2,233.4	2,404.5	(7.1)
Adj net income	2,189.7	2,078.4	5.4
FDEPS (Rs)	8.3	7.9	5.4

Source: Company, Religare Research

**Quarterly results**

(Rs mn)	Q4FY08	Q4FY07	Growth (%)	FY08	FY07	Growth (%)
Net sales	5,726.9	3,486.1	64.3	19,783.4	12,165.3	62.6
Expenditure	3,493.5	2,493.2	40.1	11,752.5	7,902.2	48.7
Operating profit	2,233.4	992.9	124.9	8,030.9	4,263.1	88.4
Other income	340.9	73.1	366.3	445.6	156.9	184.0
Interest	160.3	127.1	26.1	637.1	384.0	65.9
Depreciation	241.7	119.9	101.6	715.8	422.6	69.4
PBT	2,172.3	819.0	165.2	7,123.6	3,613.4	97.1
Tax	(17.4)	197.0	-	810.9	512.5	58.2
APAT	2,189.7	622.0	252.0	6,312.7	3,100.9	103.6
OPM (%)	39.0	28.5	1,050bps	40.6	35.0	560bps
FDEPS (Rs)	8.3	2.4	252.0	23.9	11.8	103.6

Source: Company, Religare Research

## Result highlights

### Growth across key geographies except Latin America

Glenmark witnessed strong growth from key geographies, barring Latin America, which led to a 64% YoY increase in net sales for the quarter. In Latin America, sales were affected by the de-stocking of products – a one-quarter phenomenon. We present a detailed overview of growth drivers across each market in the table below.

#### Geographical revenue break-up

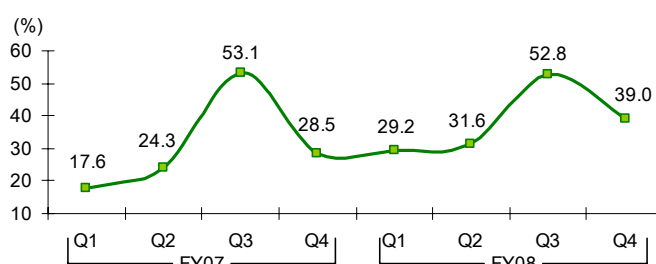
(Rs mn)	QFY08	Q4FY07	% Chg	FY08	FY07	% Chg	Comments
<b>Generics business</b>							
US	1,962.5	803.4	144.3	5,640.3	2,207.5	155.5	Launch of derma products, Oxcarbazepine exclusivity
Europe	9.2	-	-	9.2	-	-	
Latin America	60.2	55.5	8.5	309.9	265.2	16.9	New product introductions
API	590.9	355.9	66.0	1,959.3	1,318.4	48.6	Strong volume growth in domestic and export markets
<b>Total generics</b>	<b>2,622.8</b>	<b>1,214.8</b>	<b>115.9</b>	<b>7,918.7</b>	<b>3,791.1</b>	<b>108.9</b>	
<b>Specialty business</b>							
Latin America	432.7	620.4	(30.3)	1,917.6	1,155.4	66.0	Sales affected by de-stocking of products – a one-quarter phenomenon
Semi-regulated markets	532.6	454.4	17.2	2,045.7	1,884.0	8.6	Strong performance from Africa and CIS
Europe	83.5	0.0	-	368.6	0	-	Contribution from the recently-acquired Medicamenta
India	1,540.9	1,292.0	19.3	5,453.5	4,289.7	27.1	New product launches and volume growth in existing products, growth ahead of industry
Specialty formulations	2,589.7	2,366.8	9.4	9,785.4	7,329.1	33.5	
Out-licensing revenue	609.8	-	-	2,402.7	1,395.1	72.2	US\$ 15mn received from Forest Labs
Specialty business	3,199.5	2,366.8	35.2	12,188.1	8,724.2	39.7	
<b>Consolidated revenue</b>	<b>5,822.3</b>	<b>3,581.6</b>	<b>62.6</b>	<b>20,106.8</b>	<b>12,515.3</b>	<b>60.7</b>	

Source: Company

### EBITDA margin surges on out-licensing income and strong growth in key markets

The company's EBITDA margin has expanded significantly by 1,050bps to 39% driven by the robust performance from key geographies like the US, India and semi-regulated markets. In addition, the margins were boosted by out-licensing income of US\$ 15mn received from Forest Labs during the quarter. The operating margin came in slightly lower than estimates due to an inventory write-off of Rs 250mn–280mn owing to a process change on a key product, which raised material costs.

#### Trend in EBITDA margins



Source: Company, Religare Research

### Out-licensing income of US\$ 15mn boosts EBITDA margin

### Forex gains, lower tax outgo lead to sharp 252% rise in PAT

### PAT jumps 252% to Rs 2.2bn

Other income increased nearly 5-fold to Rs 341mn driven by foreign exchange gains as well as Rs 60.1mn recorded from the sale of investments in its wholly owned subsidiary. The company reported Rs 17.4mn as tax benefits for the quarter as against a Rs 197mn tax outgo in the same-year ago period, on account of higher tax payment during 9mFY08. Consequently, PAT increased by 252% to Rs 2.2bn for the quarter.

## Other highlights

- ❖ The listing of Glenmark Generics, a subsidiary of Glenmark Pharma, will be completed in FY09. Glenmark is looking at diluting a 25–30% stake in the subsidiary and deploying the proceeds towards inorganic growth.
- ❖ The company has presented an update on its NCE (new chemical entity) pipeline, which now has 13 molecules as against 11 earlier, including 5 NBEs (new biologic entities).
- ❖ The company is actively looking at a partner for Melogliptin (GRC 8200) which could crystallise over the next 12–18 months. Further, a partner for Oglemilast for the European market could be finalised before December 2008
- ❖ The management highlighted that the data from Phase II studies of acute infectious diarrhea drug Crofelemer being conducted by Napo was positive. It expects a launch over the next 18–24 months. Glenmark has exclusive marketing rights for this drug in 140 countries (semi-regulated markets), an opportunity worth US\$ 80mn–100mn.

## Valuation

### Strong FY08 performance, management revises guidance

FY08 has been a very strong year for Glenmark across geographies, both in terms of sales and profitability. The year also witnessed traction on the NCE R&D front, which saw significant progress on pre-clinical molecules moving into clinics, the out-licensing of GRC 6211 to Eli Lilly, as well as receipt of the US\$ 15mn milestone payment from Forest Labs.

Based on the robust performance, the management has raised its sales and profit guidance by ~10% for FY09 and ~18% for FY10. We believe the guidance is attainable considering Glenmark's established infrastructure in key markets. The guidance factors in only US\$ 69mn from out-licensing revenue, which could yield a significant positive upside. Rupee appreciation presents a key risk to the guidance.

### Revenue break-up over FY08-FY10

(Rs mn)	FY08	FY09E	FY10E	% CAGR FY08-FY10	Growth drivers
<b>Generics</b>					
USA	5,640.1	7,823.4	11,434.2	42.4	Focus on niche categories and new launches
Europe	9.2	152.2	380.0	542.7	Niche products, partnering EU companies
Latin America (Argentina)	309.5	600.5	936.1	73.9	File dossiers, expand in other markets using Argentina as a hub
API	1,959.9	2,700.0	3,420.0	32.1	Ramping up supplies to regulated markets, file over 15 DMFs
<b>Total generics (a)</b>	<b>7,918.7</b>	<b>11,276.1</b>	<b>16,170.4</b>	<b>42.9</b>	
<b>Specialty formulations</b>					
Latin America	1,917.9	2,325.8	3,014.0	25.4	New product launches, entry into key markets
Semi-regulated markets	2,045.4	2,931.5	5,284.2	60.7	New product launches, brand acquisitions, entry into key markets
Europe	368.1	739.8	1,477.4	100.4	Focus on Eastern Europe, build or acquire front end
India	5,454.1	6,054.1	7,022.7	13.5	Consolidate position in key therapies, new product launches
<b>Total specialty formulations (b)</b>	<b>9,785.4</b>	<b>12,051.2</b>	<b>16,798.4</b>	<b>31.0</b>	
Out-licensing revenue (c)	2,402.7	2,691.0	2,622.0	4.5	Target five molecules in Phase II trials, identify out-licensing partner for Oglemilast and Melogliptin
Specialty business (b+c) = (d)	12,188.1	14,742.2	19,420.4	30.6	
<b>Consolidated revenue (a+d)*</b>	<b>20,106.8</b>	<b>26,018.3</b>	<b>35,590.7</b>	<b>33.0</b>	

Source: Company, Religare Research, \* Gross revenue

### Based on positive guidance, we upgrade our FY09 and FY10 estimates

#### We upgrade estimates

We have incorporated the revised management outlook into our estimates and raised our FY09 and FY10 FDEPS by 15.3% and 23.6% to Rs 30.8 and Rs 40.2 respectively. We have assumed Re/\$ rate of 39.0 and 38.0 for FY09 and FY10 respectively.

#### Revised estimates

(Rs mn)	FY09E			FY10E		
	Earlier	Revised	% Chg	Earlier	Revised	% Chg
Net sales	23,392.3	25667.2	9.7	28,882.2	35183.4	21.8
Adj net income	7,046.3	8,122.0	15.3	8,568.1	10,594.0	23.6
FDEPS (Rs)	26.7	30.8	15.3	32.5	40.2	23.6

Source: Religare Research

#### SOTP-based target price of Rs 700, Buy

As Glenmark's research income is volatile in nature, the P/E methodology which is the preferred valuation method for most pharma companies will not be appropriate. We have therefore used the sum-of-the-parts (SOTP) approach for Glenmark wherein we have assessed the company's base business and NCE pipeline separately.

### Upgrade target to Rs 700, Buy

We have valued the non-R&D business at 18x FY10E earnings, in line with its peers, which yields a revised fair value of Rs 479.1/share from Rs 327 previously. We maintain our valuation of the three lead molecules of Glenmark's NCE pipeline at Rs 220.4/share. We thus arrive at a revised target price of Rs 700 from Rs 548. At our target price, the stock would trade at 22.7x FY09E and 17.4x FY10E earnings. We believe valuations are attractive and maintain a Buy on the stock.

#### SOTP valuation for Glenmark

Parameter	FY10E EPS (Rs)	P/E (x)	Value per share (Rs)
Base business	26.6	18.0	479.1
R&D pipeline	220.4	-	220.4
<b>Total</b>			<b>699.5</b>

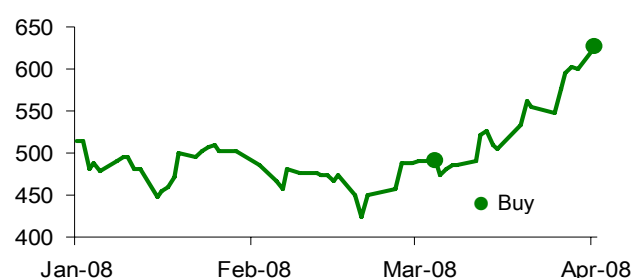
Source: Religare Research

#### Recommendation history

Date	Event	Reco price	Tgt price	Reco
1-Apr-08	Initiating Coverage	485	548	Buy
29-Apr-08	Results Update	625	700	Buy

Source: Religare Research

#### Stock performance



Source: Religare Research

## Consolidated financials

### Profit and Loss statement

(Rs mn)	FY07	FY08	FY09E	FY10E
Revenues	12,515.3	19,783.4	25,667.2	35,183.4
Growth (%)	65.2	58.1	29.7	37.1
EBITDA	4,262.9	8,030.9	10,266.9	13,123.4
Growth (%)	210.7	88.4	27.8	27.8
Depreciation	422.6	715.8	824.3	963.7
EBIT	3,840.3	7,315.1	9,442.6	12,159.7
Growth (%)	236.9	90.5	29.1	28.8
Interest	384.1	637.1	583.6	624.8
Other income	157.0	445.6	308.0	422.2
EBT	3,613.2	7,123.6	9,167.0	11,957.1
Income taxes	512.6	810.9	1,045.0	1,363.1
Effective tax rate (%)	14.2	11.4	11.4	11.4
Adjusted net income	3,100.6	6,312.7	8,122.0	10,594.0
Growth (%)	252.4	103.6	28.7	30.4
Reported net income	3,100.6	6,312.7	8,122.0	10,594.0
Growth (%)	252.4	103.6	28.7	30.4
Shares outstanding (mn)	263.7	263.7	263.7	263.7
Basic EPS (Rs) (adj)	11.8	23.9	30.8	40.2
FDEPS (Rs) (adj)	11.8	23.9	30.8	40.2
DPS (Rs)	0.4	0.5	0.7	0.9

Source: Company, Religare Research

### Cash flow statement

(Rs mn)	FY07	FY08E	FY09E	FY10E
Net income	3,100.6	6,312.7	8,122.0	10,594.0
Depreciation	422.6	715.8	824.3	963.7
Other adjustments, net	300.0	187.6	574.8	749.7
Changes in working capital	(2,970.3)	(2,584.1)	(3,060.7)	(5,894.9)
Cash flow from operations	852.9	4,632.0	6,460.3	6,412.5
Capital expenditure	(2,722.2)	(1,839.8)	(1,941.7)	(1,979.6)
Change in investments	9.8	-	-	-
Other investing inc/(exp)	15.9	(0.1)	-	-
Cash flow from investing	(2,696.6)	(1,839.9)	(1,941.7)	(1,979.6)
Free cash flow	(1,843.6)	2,792.1	4,518.6	4,432.9
Issue of equity	2.7	8.6	-	-
Issue/repay debt	2,013.1	(2,543.2)	500.0	500.0
Dividends paid	(109.2)	(147.7)	(190.1)	(247.9)
Other financing cash flow	(61.5)	-	-	-
Cash flow from financing	1,845.1	(2,682.3)	309.9	252.1
Change in cash & cash eq	1.5	109.8	4,828.6	4,685.0
Opening cash & cash eq	1,056.0	1,057.5	1,167.3	5,995.9
Closing cash & cash eq	1,057.5	1,167.3	5,995.9	10,680.9

Source: Company, Religare Research

### Balance sheet

(Rs mn)	FY07	FY08E	FY09E	FY10E
Cash and cash eq	1,057.5	1,167.3	5,995.9	10,680.9
Accounts receivable	5,711.6	8,431.6	9,363.1	13,873.7
Inventories	2,697.1	4,060.9	5,008.8	7,511.4
Others current assets	1,588.0	2,275.1	3,336.7	5,277.5
Current assets	11,054.3	15,935.0	23,704.6	37,343.5
Long-term investments	187.2	187.2	187.2	187.2
Net fixed assets	5,930.4	7,497.9	8,947.9	10,213.2
CWIP	2,173.9	1,730.4	1,397.8	1,148.4
Intangible assets	-	-	-	-
Total assets	19,345.9	25,350.5	34,237.5	48,892.3
Accounts payable	2,328.6	4,320.2	4,148.4	7,137.3
Others	66.6	261.7	313.8	383.8
Current liabilities	2,395.1	4,581.9	4,462.2	7,521.2
Debt funds	9,367.0	6,823.8	7,323.8	7,823.8
Other liabilities	720.0	907.6	1,482.4	2,232.1
Equity capital	240.1	248.7	248.7	248.7
Reserves	6,623.5	12,788.5	20,720.5	31,066.5
Shareholder's funds	6,863.6	13,037.2	20,969.2	31,315.2
Total liabilities	19,345.8	25,350.5	34,237.5	48,892.3
BVPS (Rs)	26.0	49.4	79.5	118.8

Source: Company, Religare Research

### Financial ratios

	FY07	FY08E	FY09E	FY10E
EBITDA margin (%)	34.1	40.6	40.0	37.3
EBIT margin (%)	30.7	37.0	36.8	34.6
Net profit margin (%)	24.8	31.9	31.6	30.1
FDEPS growth (%)	217.3	103.6	28.7	30.4
Receivables (days)	138.9	130.5	126.5	120.5
Inventory (days)	94.5	104.9	107.5	103.6
Payables (days)	89.5	103.2	100.4	93.4
Current ratio (x)	4.6	3.5	5.3	5.0
Quick ratio (x)	3.5	2.6	4.2	4.0
Interest coverage ratio (x)	9.1	10.9	14.9	18.0
Debt / equity (x)	1.4	0.5	0.3	0.2
ROE (%)	57.4	63.4	47.8	40.5
ROA (%)	18.9	28.2	27.3	25.5
ROCE (%)	26.8	38.8	37.4	34.2
EV/Sales (x)	12.9	8.1	6.3	4.6
EV/EBITDA (x)	37.8	20.1	15.7	12.3
P/E (x)	53.2	26.1	20.3	15.6
P/BV (x)	24.0	12.6	7.9	5.3

Source: Company, Religare Research

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Recommendation parameters

Large-caps*	> 10%	< - 5%	Returns	Absolute
	BUY	SELL		
Mid-caps**	> 25%	< 10%		

\*Market cap over US\$ 1bn \*\*Market cap less than US\$ 1bn

**Religare Securities**

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