Glenmark Lifesciences – IPO Note (Subscribe)

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Leveraging API base towards CDMO

Glenmark life sciences (GLS, a spin-off from Glenmark Pharma), operates in 2 segments – Generic APIs (91% of sales) and CDMO (8% of sales) with dominance in chronic therapies such as CVS and CNS. It currently has 120 molecules and 65% of customer base which is repeat in nature. Major customers are Glenmark (contributes 35% of sales), Torrent Pharma, Teva, Aurobindo and Krka. With 65% of revenue coming from US/EU, GLS intends to expand to expand presence in regions that are moving towards becoming well-regulated markets such as South Korea, Taiwan, Russia, Brazil, Mexico and Saudi Arabia. Apart from APIs, company plans to expand its CDMO business which is in nascent stage focusing on lifecycle management and specialty products. GLS intends to spend Rs6bn+ towards building its greenfield capacity with a capacity of 800KL. Besides, capex is also underway for oncology pipeline expected to be operational by 4QFY23. It also plans to bid for PLI 2.0 under category A.

Outlook and valuation

GLS' FY21 P&L reflects benefits from Favipiravir (EBITDA margin 31%). Interestingly in past 6 months (Jan-Jun'21), exports have largely been towards EM and sales have seen a declining trend. Also, Glenmark's contribution has been negligible during this period. We expect revenue contribution from newly-commercialized products to increase over the next five years. In addition, we see the complex API business as a key growth opportunity where GLS could leverage expertise in synthetic chemistry and analytical characterization to expand its existing technology platforms and complex API portfolio in oncology, peptides and iron compounds, thereby expanding existing portfolio of API products. Profit share clause in the CDMO segment could add profit optionality to this business. At the upper end of price band of Rs720, Glenmark is valued currently at 22x FY21 earnings which is in-line with industry peers. Subscribe.

Investment Rationale

Leadership in select high value, non-commodity chronic API: GLS' portfolio comprises of 120 products (10 products in development; 4 products in validation and 106 products being commercialized) ranging across various therapy areas like CVS, CNS, diabetes, anti-infective, etc. It has strong market share in select specialized APIs such as Telmisartan, Perindopril (anti-hypertensive), Atovaquone (anti-parasitic), Teneligliptin (diabetes), Adapalene (derma). GLS is working towards developing 8-10 molecules each year, which include both high value and high volume APIs. As of FY21, it has filed 403 DMF/CEPs across major markets (US, Europe, Japan, Russia, Brazil, South Korea, Taiwan, Canada, China and Australia).

Share Data	Rs mn	Mn
Fresh issue	10,600	14.7
Offer for Sale	4,537	6.3
Issue Size	15,137	21.0
Issue Open/Close	27th July'21 to 29th July'21	
Face Value (Rs)		2/-
Lot Size (shares)		20 Shares
Price Band (Rs)		695 - 720
Pre-issue paid up Capital		19.6
Post-issue paid up Capital		49
Post-issue market Cap (at upper price band)		17,640
BRLM: Citigroup, Kotak Mahindra Capital, Nomura Financial Advisory, Haitong Securities		
Registrar	Link In-time India Private Ltd	

Pre-issue pattern	%
Promoter	100%
Public	0%

Post-issue pattern	%
Promoter	83%
Public	17%

Offer for different categories	%
QIB	50%
NII	15%
Retail	35%

Promoters	Pre offer (%)	Post Offer (%)
Glenmark Pharma	100%	83%

Objects of the issue	Amt (mn)
(i) Payment of outstanding purchase consideration to the Promoter for the spin-off of the API business; (ii) Funding capex requirements; (iii) General corporate purposes.	Rs 8000 Rs1,527.64

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Strong relationship with leading global generic companies: It works with 16 of the 20 largest generic companies globally. With higher compliance rate it has been able to maintain high customer loyalty and a high rate of repeat customers, ~65%. Its top customers include Teva, Krka, Torrent, Aurobindo and Glenmark Pharma. Glenmark constitutes ~35% of total sales. In the past 6 months, regulated markets such as US/UK contributed only 14% of sales.

High-quality product manufacturing with R&D infrastructure: It currently operates through 4 facilities with an annual capacity of 725.8KL. Since 2015, its facilities had been inspected ~37 times by regulators across USFDA, PMDA, EDQM, etc. It has maintained strong compliance and not received any warning letter or import alert till date. The manufacturing facilities at Ankleshwar and Dahej are certified ISO 14001:2015 and ISO 45001:2018 for environment management and occupational health and safety management systems.

CDMO business an optionality: In the last 3 years, GLS has started working with innovator pharma companies in the area of CDMOs. It currently operates in 2 segments (1) Lifecycle management (2) Specialty business – such as 505(b) (2). Right now the company has only 4 clients but it believes that of its portfolio of 120 molecules there could be many such molecules for new set of customers. Greenfield capacity expansion of 40 acres with plan to manufacture both API and intermediates will have capacity of 800KL over the next 3-4 years. Royalty and profit clause can act as potential optionality for future business.

Proven track record of strong financial performance: Regulated markets comprise 65% of sales. Its sales grew 26% CAGR and PAT by 12% CAGR over FY18-21 with strong EBITDA margins at ~30%.

Risk

Competition: The API market is highly fragmented with ~1,500 API manufacturing plants. As of 2017, the top 14-16 API players comprised just 16-17% of the total market share. Key players playing in the API market include Laurus Labs, Divis, Glenmark Life Sciences, Shilpa Medicare, Aarti Drugs and Solara Active Pharma Sciences. The products are chemistry based and hence easy to replicate.

Customer dependency: Top 5 customers contribute 57% of sales and Glenmark is the largest customer. If other players decide to backward integrate then it becomes a risk to the business.

Interruption in supply of raw materials: Three largest suppliers account for 40% of total KSMs as on FY21. Pricing pressure or inadequate supply could impact profitability.

Capex plans

It intends to increase its API manufacturing capabilities by enhancing the existing production capacities at its Ankleshwar facility during FY22 and its Dahej facility during FY22 and FY23 by an aggregate annual total installed capacity of 200 KL. This additional production capacity is expected to help further expand its generic API production and also grow its oncology product pipeline. The company intends to develop a new manufacturing facility in India for the manufacture of generic APIs from FY22 which is expected to become operational by 4QFY23. The new facility will also provide a platform for the growth of our CDMO business and also add capacity for our generic API business. This facility will be a greenfield project built on a 40-acre footprint with a plan to manufacture both APIs and intermediates and will house several multi-purpose manufacturing blocks with mid to high-volume capacity.

About the Company

In 2001-2002, Glenmark launched the API manufacturing business by setting up a manufacturing facility in Kurkumbh. In 2019, the API manufacturing business of Glenmark was sold and spun off as part of a broader reorganization designed to place Glenmark on an accelerated trajectory to attain its objectives in three different verticals. Following the spin-off, it operates as an independent, professionally-managed global API business.

The company develops, manufactures, and supplies APIs for cardiovascular disease (CVS), central nervous system disease (CNS), pain management, and diabetes, gastrointestinal disorders, anti-infective and other therapeutic areas. It further operates in Contract Development and manufacturing operations (CDMO) to offer services to specialty Pharmaceutical companies.

Its products are being sold in India and also exported to multiple countries i.e. Europe, North America, Latin America, Japan, etc. Currently, it has 4 manufacturing facilities at Ankleshwar and Dahej in Gujarat and Mohol and Kurkumbh in Maharashtra State with an aggregate annual installed capacity of 725.8 KL as of 9MFY21. Since 2015, the facilities have been subject to 37 inspections and audits by regulators including the USFDA, PMDA, COFEPRIS, Health Canada, MFDS (Korea), EDQM, other European regulatory agencies and CDSCO conducted on a periodic basis. It has not received any warning letters or import alerts from such regulatory authorities. Its facilities have also been subject to 416 inspections and audits by customers during this period.

As on FY21, it had a portfolio of 120 molecules globally. As of FY21, it had filed 403 Drug Master Files (“DMFs”) and Certificates of suitability to the monographs of the European Pharmacopoeia (“CEPs”) across various major markets. It works with 16 of the 20 largest generic companies globally as of FY21.

About the Industry

Globally, India is one of the top suppliers of bulk drugs and formulations. The country has the highest number of USFDA approved plants outside the US as well as 44% of global ANDA. The Indian generics industry can benefit substantially from the patent cliff as patents for branded molecules with cumulative global sales of ~US$251bn are expected to expire between 2018 and 2024, opening new opportunities for the industry.

India supplies almost 40% of the total US generic drug demand and addresses as much as 25% of the total drug demand in the UK. India also accounts for 60% of global vaccine production, contributing 40-70% of the WHO demand. This success can be attributed to the advanced capabilities in the formulation development and the vision of the industry to establish India's footprint in large international markets. However, within the APIs and bulk drug manufacturing segment, India lags behind China. Currently, India imports ~68% of its API consumption by value from China and is highly reliant on China for fermentation-based APIs (antibiotics), feedstock and many key starting materials ("KSMs"). The COVID-19 pandemic has shed light on India's excessive dependence on China for APIs and KSMs.

India's pharma sector is now trying to reinvent itself and move forward from its long standing dependence on export of generics towards enabling the industry to become an end-to-end drug manufacturer. This includes a parallel thrust on localizing API and bulk drug manufacturing. The Indian government has set up a production linked incentive ("PLI") package focusing on APIs and the API Parks scheme to boost competitiveness of India's manufacturing and promote domestic manufacturing of critical intermediates and APIs.

The global API market was estimated to be ~US$181bn in 2020 and is expected to grow at a CAGR of 6.2% to reach to ~US$259bn by 2026. The market is likely to exhibit a positive outlook with the growing trend towards the development of innovative therapeutic drugs by various pharmaceutical and biotechnology companies. The rising prevalence of chronic disorders, increasing demand for personalized medicine and emergence of novel drug delivery devices are some of the key factors expected to drive the API market over the next five years. Currently, a large number of manufacturers have their robust footprints in China and India which is propelling many biopharmaceutical industries to seek partnerships with CDMOs. These possess the technical know-how and capabilities for largescale manufacturing, which is anticipated to upsurge the market growth of APIs during the forecast period. The Indian API market has shown steady growth of 9.2% since FY18 and is expected to further grow owing to an increased focus on newer geographies in the global pharmaceutical industry, transition to specialty segments and strong domestic demand.

Key trends

Rising prevalence of chronic and lifestyle diseases and changing demographic mix – The population above 65 years constitutes a large percentage of the total global population. Individuals in this group (baby boomers) typically have at least one chronic disorder such as cardiovascular diseases, diabetes, cancer and other chronic conditions, which creates pressure on the healthcare system to look for cost-effective options in the form of affordable, high-quality generic drugs. The prevalence of chronic diseases has drastically increased in the last few years compared to acute therapies leading to a shift in focus from lower-cost commoditized therapies to higher value non-commodity drugs which are usually orally administered allowing the healthcare system to handle an increasing patient pool effectively while also managing overall treatment costs.

The newest generation of APIs is extremely complex, such as peptides, high potency API, oligonucleotides, and sterile API. Thus, the R&D and certification processes are expected to become longer and more complicated. 4. 5% of the global supply of API's are produced in Asia and this trend is expected to grow at a faster pace than the overall pace of market growth. A multitude of small producers, specializing in manufacturing niche segments of API have led to intense competition despite growing market.

The rising volume of API production from Asia has also led to issues related to quality assurance and compliance to standards. This trend has led to increased regulatory demands from the United States, European and Japanese authorities.

Exhibit 1: Revenue break-up segment wise

Particulars (%)	FY21
Generic API's	90.6
CDMO	8.1
Others	1.3
Total	**100.0**

Source: DART, Company

Exhibit 2: Revenue break-up geography-wise

API Business	(%)
Regulated market	65.6
Emerging market	33.1
Others	1.3

Source: DART, Company

Exhibit 3: Filings

Region	No of DMF / CEP Filing	Approx No. of Customer Serviced in FY20
North America	142	30+
Europe	79	50+
India	-	100+
Japan	15	10+
Latin America	59	50+
ROW	108	300+

Source: DART, Company

Exhibit 4: Revenue break-up therapy wise

Generic APIs	FY18	FY19	FY20	FY21
CVS Therapeutic Area	4,677	5,439	6,682	7,763
% of Sales	41.8	43.1	51.6	45.4
CNS Therapeutic Area	962	1,220	1,280	1,677
% of Sales	8.6	9.7	9.9	9.8
Diabetes Therapeutic Area	975	795	571	619
% of Sales	8.7	6.3	4.4	3.6
Pain Management Therapeutic Area	727	685	727	706
% of Sales	6.5	5.4	5.6	4.1
Others	3,840	4,489	3,679	6,319
% of Sales	34.4	35.6	28.4	37.0
Total API sales	**11,180**	**12,627**	**12,939**	**17,084**
CDMO	**487**	**981**	**2,005**	**1,530**
Total Revenue	**11,667**	**13,608**	**14,943**	**18,614**

Source: DART, Company

Exhibit 5: Volume and Value of key APIs

Market Share Range	Volume contribution in FY21	Value Contribution in FY21	Key Products
<10%	27%	36%	Olmesartan, Rosuvastatin, Oxcarbazepine
10-20%	31%	18%	Telmisartan, Etoricoxib, Voriconazole
20-30%	1%	3%	Teneligliptin, Desloratadine, Riluzole
>30%	41%	44%	Atovaquone, Perindopril, Adapalene, Zonisamide

Source: DART, Company

Exhibit 6: Manufacturing facilities

Location	Description	Top Products (Therapeutic Area)	Approvals	Last Inspection
Ankleshwar, Gujarat	API manufacturing facility with manpower of 955 personnel Annual total installed capacities as of December 31, 2020 – 511.0 KL	Amiodarone (CVS), Olmesartan (CVS), Perindopril (CVS), Oxcarbazepine (CNS)	USFDA	Jul-19
			MHRA (UK)	Nov-06
			FIMEA (Finland)	Jul-14
			Romania (Europe)	Feb-14
			PMDA (Japan)	Aug-19
			COFEPRIS (Mexico)	Feb-16
			Health Canada	Jul-19
			KFDA (South Korea)	Apr-11
Dahej, Gujarat	API manufacturing facility with manpower of 260 personnel Annual total installed capacities as of December 31, 2020 – 141.1 KL	Amiodarone (CVS), Etoricoxib (Pain management), Omeprazole (Gastro-intestinal), Fluconazole (antiinfective), Cilostazol (CVS)	USFDA	Oct-18
			EDQM (Europe)	Mar-18
			PMDA (Japan)	Dec-16
			KFDA (South Korea)	May-17
Mahol, Maharashtra	API manufacturing facility with manpower of 77 personnel Annual total installed capacities as of December 31, 2020 – 49.1 KL	Telmisartan (CVS), Rosuvastatin (CVS), Vildagliptin (diabetes)	USFDA	Mar-18
			Maharashtra FDA	Jan-21
Kurkumbh, Maharashtra	API manufacturing facility with manpower of 71 personnel Annual total installed capacities as of December 31, 2020 – 24.6 KL	Glimepiride (diabetes), Sertaconazole (dermatology), Adapalene (dermatology)	Maharashtra FDA	Jan-21

Source: DART, Company

Production Capacity, Production Volumes and Capacity Utilization

Ankleshwar

Particulars	Financial Year			
	FY21	2020	2019	2018
Annual Production Capacity (M/T)	301	246	251.2	209.6
Actual Production Volumes (M/T)	259	214	206	174
Capacity Utilization (%)	86	87	82	83

Source: DART, Company

Dahej

Particulars	Financial Year			
	FY21	2020	2019	2018
Annual Production Capacity (M/T)	151	111.5	121.7	94.9
Actual Production Volumes (M/T)	133	97	101	75
Capacity Utilization (%)	88	87	83	79

Source: DART, Company

Mohol

Particulars	Financial Year			
	FY21	2020	2019	2018
Annual Production Capacity (M/T)	55	43.2	42.7	41.2
Actual Production Volumes (M/T)	47	32.4	31.6	30.5
Capacity Utilization (%)	86	75	74	74

Source: DART, Company

Kurkumbh

Particulars	Financial Year			
	FY21	2020	2019	2018
Annual Production Capacity (M/T)	56.3	43.2	42.7	41.2
Actual Production Volumes (M/T)	38	32.4	31.6	30.5
Capacity Utilization (%)	68	75	74	74

Source: DART, Company

Management details

No. of directors	FY21
Promoter Director	1
Non-Executive director	2
Independent director	4
Executive director	1
Total	**8**
% of Promoter director	**13%**
% of independent director	**50%**

Source: DART, Company

Profile of independent directors (Rs mn)

Name	Qualification	Appointment date	Directorship in any other public company	FY21 Remuneration (Rs mn)	% of PBT
Sridhar Gorthi	Law Degree	30-Oct-20	3	0.2	0.00%
Manju Agarwal	Post Graduate	30-Oct-20	5	0.2	0.00%
Taruvai Laxminarayanan Easwar	Chemical Engineer	8-Jan-21	-	-	-
Gita Nayyar	Master's in business Admin	17-Feb-21	4	0.2	0.00%

Source: DART, Company

Remuneration of other key personnel

Name	Position	FY21 (Rs mn)
Glenn Saldhana	Promoter & Non-Executive Director	-
V.S Mani	Non-Executive Director	-
Yasir Rawjee	MD & CEO	45.71
Sumantra Mitra	Executive Director	8.02
Ruchita Gandhi	CFO	9.02
Bhavesh Pujara	CFO	1.15

Peer comparison

Company (Rs mn)	Sales	EBITDA	PAT	ROE (%)	ROCE (%)	P/E (x)	D/E (x)	EV/EBITDA (x)
Glenmark	**18,852**	**5,911**	**3,516**	**60.9**	**93.6**	**22.1**	**(0.2)**	**12.9**
Laurus Lab	48135	15,507	9,838	45.1	36.8	35.6	0.6	23.6
Solara	16,169	3,859	2,214	16.6	15.4	26.9	0.2	16.3
Aarti drugs	22,723	4,427	2,797	34.7	31.4	24.0	0.2	15.6
Granules	32,375	8,552	5,495	27.4	25.8	14.8	0.2	10.1

Source: DART, Company

BALANCE SHEET (Rs mn)

Year ending March	FY18	FY19	FY20	9MFY21
SOURCES OF FUNDS				
Share Capital	0.1	19.6	19.6	19.6
Reserves	(14)	862	3,997	6,459
Total Shareholders' Funds	(14)	881	4,017	6,479
Long-term Debt	0	0	0	0
Short-term Debt	0	0	0	0
Total Debt	0	0	0	0
Deferred Taxes	0	69	164	216
Other LT Liabilities	0	0	0	0
Minority Interest	0	0	0	0
TOTAL SOURCES OF FUNDS	**(14)**	**950**	**4,182**	**6,695**
APPLICATION OF FUNDS				
Net Block	0	4,564	5,462	5,286
CWIP	0	803	107	434
Good will	0	0	0	0
LT Investments	0	1	1	1
LT Loans & Advances	0	79	84	88
Inventories	0	4,008	4,128	5,081
Debtors	0	4,481	6,386	7,208
Cash & Equivalents	0	21	100	111
Other Current Assets	0	797	987	1,356
Total Current Assets	1	9,307	11,601	13,757
Creditors	0	1,829	2,011	2,882
Other Current Liabilities	15	11,975	11,064	9,989
Total Current Liabilities	15	13,804	13,074	12,870
Net Current Assets	(14)	(4,497)	(1,473)	886
TOTAL APPLICATION OF FUNDS	**(14)**	**950**	**4,182**	**6,695**

INCOME STATEMENT (Rs mn)

Year ending March	FY18	FY19	FY20	9MFY21
Revenues	2	8,864	15,373	14,180
Growth (%)	-	357328	73	(8)
Material Expenses	(1)	(3,523)	(6,905)	(7,130)
Employee Expenses	2	1,063	1,423	1,116
Other Operating Expenses	0	1,561	2,095	1,574
R&D	333	376	400	304
EBITDA	2	9,763	18,760	18,620
EBITDA Margin (%)	62	110	122	131
Growth (%)	-	633884	92	(1)
Depreciation	0	193	294	250
EBIT	2	9,571	18,467	18,371
Other Income	0	4	120	5
Interest	0	6	335	664
PBT	2	9,569	18,251	17,712
Tax	4	327	1,080	834
PAT	(3)	9,242	17,172	16,877
EO items (net of tax)	0	0	0	0
Share of Profits from JV/Associates	0	0	0	0
APAT	(3)	9,242	17,172	16,877
Growth (%)	-	(346245)	86	(2)
AEPS	(7.9)	24.6	29.0	22.9
Growth (%)	-	(412)	18	(21)

CASH FLOW STATEMENT (Rs mn)

Year ending March	FY18	FY19	FY20	9MFY21
Reported PAT	(4)	1,956	3,131	2,469
Non-operating & EO items	0	0	0	0
PAT from Operations	(4)	1,956	3,131	2,469
Depreciation	0	193	294	250
Interest expenses	0	6	335	664
Working Capital Change	10	4,245	(3,928)	(3,131)
OPERATING CASH FLOW (a)	**(5)**	**104**	**1,950**	**4,330**
Capex	0	(5,560)	(496)	(400)
Free cash flow (FCF)	(5)	14	1,445	3,907
Investments	0	(1)	0	0
INVESTING CASH FLOW (b)	**0**	**(89)**	**(505)**	**(423)**
Debt Issuance	0	0	0	0
Interest expenses	0	(6)	(335)	(664)
FCFE	(5)	5,668	2,696	5,226
Share capital Issuance	0	20	0	0
Dividend	0	0	0	0
Others	0	0	0	0
FINANCING CASH FLOW (c)	**5**	**5**	**(1,366)**	**(1,670)**
NET CASH FLOW (a+b+c)	**0**	**20**	**79**	**2,237**
Closing Cash & Equivalents	0	21	100	111

Source: DART, Company

KEY RATIOS

	FY18	FY19	FY20	9MFY21
PROFITABILITY %				
Gross Margin	66.1	60.3	55.1	49.7
EBITDA Margin	(6.0)	29.1	31.6	30.1
EBIT Margin	(6.0)	26.9	30.4	28.4
APAT Margin	(186.7)	23.0	21.0	17.7
RoE	62.2	451.1	127.8	47.0
Core RoCE	2.1	3466.3	194.9	74.5
RoCE	2.0	489.1	177.2	72.9
EFFICIENCY	-			
Tax rate %	(3007.1)	14.3	25.6	25.3
Fixed Asset Turnover (x)	496.0	3.3	2.8	2.5
Inventory (days)	60	172	101	133
Debtor (days)	49	192	156	188
Other Current Assets (days)	-	-	-	-
Payables (days)	18	105	69	106
Other Current Liab & Provns (days)				
Cash Conversion Cycle (days)	90	259	188	215
Net Debt/EBITDA (x)	0.5	0.0	0.0	0.0
Net D/E	0.0	0.0	0.0	0.0
Interest Coverage		378.4	13.6	6.0
PER SHARE DATA (Rs/sh)	-			
EPS	(7.9)	24.6	29.0	22.9
CEPS	(7.9)	27.1	31.8	25.2
DPS	0.0	0.0	0.0	0.0
BV	(25.4)	11.1	37.3	60.1

***DART* RATING MATRIX**

Total Return Expectation (12 Months)

Buy	**> 20%**
Accumulate	**10 to 20%**
Reduce	**0 to 10%**
Sell	**< 0%**

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