

Beat on earnings

- Natco's Q4FY24 results were above our estimates on account of higher-than-expected growth in export formulation. However, domestic and Crop Health Sciences (CHS) were below estimate due to a one-time charge of Rs900mn. Charge of Rs350mn on domestic business was on return of stock from super-stockist due to change in distribution model. Stock returns in CHS were worth Rs250mn due to poor crop season and Rs300mn provision for certain non-utilized assets.
- Management guided topline growth of 15-20% for FY25. Crop Health sciences is expected to be a Rs3bn business in the next three years. The company is looking for acquisitions in ROW markets to expand its business.
- We upgrade our FY25E/FY26E EPS estimates by 4.8%/5.1% assuming higher than expected export formulation sales. We like Natco Pharma's focus on niche drug filings and expect strong cash flows backed by low competitive launches. We believe cash flows will be utilized towards inorganic opportunities, dividend payouts and R&D bio-study activities. We maintain our 'Accumulate' rating with revised target price of Rs1,144 (earlier Rs1,004) on SOTP basis (Exhibit 4). Key risks: Higher competition in niche products, higher price erosion in the US and GMP compliance issues.

Complex and niche products to drive export growth

Exports increased 34.6%/56.9% YoY in Q4/FY24 driven by gRevlimid supplies. A good portion of the Q4FY24 revenue came from gRevlimid supplies. Semaglutide and Olaparib are some of the other large opportunities that will drive growth beyond the gRevlimid opportunity post FY26. Natco is focused on filing differentiated products in the US where it has ~24 Para IVs in the pipeline out of which 15 are approved. We project export revenue CAGR of 14% over FY24-26E including gRevlimid estimates in the US.

Decline in Agro and domestic sales on one time charge

Natco's Crop Health Sciences grew 164.8% in FY24 below estimates impacted by poor season. We expect the segment to become sizeable to Rs4-5bn in the long run. Domestic business declined 43.9% YoY in Q4FY24 due to a change in business model. We expect Natco's domestic business revenue to recover Q1FY25 onwards backed by new launches and show 12% CAGR over FY24-26E.

Q4FY24 Result (Rs Mn)

| Particulars | Q4FY24 | Q4FY23 | YoY (%) | Q3FY24 | QoQ (%) |
|-------------------|--------|--------|---------|--------|---------|
| Revenue | 10,683 | 8,979 | 19.0 | 7,586 | 40.8 |
| Total Expense | 5,710 | 5,588 | 2.2 | 4,905 | 16.4 |
| EBITDA | 4,973 | 3,391 | 46.7 | 2,681 | 85.5 |
| Depreciation | 555 | 410 | 35.4 | 442 | 25.6 |
| EBIT | 4,418 | 2,981 | 48.2 | 2,239 | 97.3 |
| Other Income | 420 | 290 | 44.8 | 370 | 13.5 |
| Interest | 62 | 27 | 129.6 | 46 | 34.8 |
| EBT | 4,776 | 3,244 | 47.2 | 2,563 | 86.3 |
| Tax | 913 | 486 | 87.9 | 436 | 109.4 |
| RPAT | 3,863 | 2,758 | 40.1 | 2,127 | 81.6 |
| APAT | 3,863 | 2,758 | 40.1 | 2,127 | 81.6 |
| | | | (bps) | | (bps) |
| Gross Margin (%) | 86.7 | 71.2 | 1543 | 78.6 | 803 |
| EBITDA Margin (%) | 46.6 | 37.8 | 878 | 35.3 | 1121 |
| NPM (%) | 36.2 | 30.7 | 544 | 28.0 | 812 |
| Tax Rate (%) | 19.1 | 15.0 | 413 | 17.0 | 211 |
| EBIT Margin (%) | 41.4 | 33.2 | 816 | 29.5 | 1184 |

| | |
|-----------------|----------------|
| CMP | Rs 1,029 |
| Target / Upside | Rs 1,144 / 11% |
| NIFTY | 22,957 |

Scrip Details

| | |
|------------------|-----------------|
| Equity / FV | Rs 358mn / Rs 2 |
| Market Cap | Rs 184bn |
| | USD 2.2bn |
| 52-week High/Low | Rs 1,108/ 609 |
| Avg. Volume (no) | 5,98,601 |
| Bloom Code | NTCPH IN |

| Price Performance | 1M | 3M | 12M |
|-------------------|-----|----|-----|
| Absolute (%) | 0 | 5 | 63 |
| Rel to NIFTY (%) | (2) | 0 | 39 |

Shareholding Pattern

| | Sep'23 | Dec'23 | Mar'24 |
|-----------------|--------|--------|--------|
| Promoters | 49.7 | 49.7 | 49.7 |
| MF/Banks/FIs | 14.0 | 11.3 | 9.7 |
| FIs | 12.8 | 13.7 | 16.1 |
| Public / Others | 23.5 | 25.3 | 24.5 |

Valuation (x)

| | FY24A | FY25E | FY26E |
|-----------|-------|-------|-------|
| P/E | 13.3 | 10.3 | 8.7 |
| EV/EBITDA | 9.9 | 7.6 | 5.9 |
| ROE (%) | 24.9 | 27.1 | 26.1 |
| RoACE (%) | 24.7 | 25.7 | 25.0 |

Estimates (Rs bn)

| | FY24A | FY25E | FY26E |
|-----------|-------|-------|-------|
| Revenue | 40.0 | 46.5 | 53.4 |
| EBITDA | 17.5 | 22.1 | 26.2 |
| PAT | 13.9 | 17.8 | 21.2 |
| EPS (Rs.) | 77.6 | 99.5 | 118.3 |

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Exhibit 1: Quarterly revenue mix

| Particulars (Rs mn) | Q4FY24 | Q4FY23 | YoY (%) | Q3FY24 | QoQ% | FY23 | FY24 | YoY (%) |
|------------------------|--------|--------|---------|--------|---------|--------|--------|---------|
| API | 500 | 728 | (31.3) | 463 | 8.0 | 2,103 | 2,492 | 18.5 |
| Domestic formulation | 524 | 918 | (42.9) | 994 | (47.3) | 3,749 | 3,867 | 3.1 |
| Export formulation | 9,549 | 7,092 | 34.6 | 6,056 | 57.7 | 20,632 | 32,369 | 56.9 |
| Other operating income | 534 | 261 | 104.6 | 302 | 76.8 | 178 | 177 | (0.6) |
| Crop health science | (40) | 270 | (114.8) | 141 | (128.4) | 409 | 1,083 | 164.8 |
| Total | 11,067 | 9,269 | 19.4 | 7,956 | 39.1 | 27,071 | 39,988 | 47.7 |

Source: Company, DART

Exhibit 2: Actual vs DART estimates

| Particulars (Rs mn) | Q4FY24 | Q4FY24E | Variance (%) | Comment |
|---------------------|--------|---------|--------------|--|
| Revenue | 10,683 | 9,449 | 13.1 | Higher than expected sales in exports |
| EBITDA | 4,973 | 4,063 | 22.4 | Higher than anticipated sales led to higher margin |
| EBITDA margin (%) | 46.6 | 43.0 | 355bps | |
| PAT | 3,863 | 3,242 | 19.2 | Higher than expected operating performance and other income. |
| EPS (Rs) | 21.6 | 18.1 | 19.2 | |

Source: Company, DART

Exhibit 3: Change in estimates

| Particulars (Rs mn) | FY25E | | | FY26E | | |
|---------------------|--------|--------|----------|--------|--------|----------|
| | Old | New | Chg. (%) | Old | New | Chg. (%) |
| Revenue | 44,403 | 46,524 | 4.8 | 50,838 | 53,407 | 5.1 |
| EBITDA | 21,136 | 22,146 | 4.8 | 24,911 | 26,169 | 5.1 |
| EBITDA Margin (%) | 47.6 | 47.6 | 0bps | 49.0 | 49.0 | 0bps |
| PAT | 16,995 | 17,807 | 4.8 | 20,157 | 21,179 | 5.1 |
| EPS (Rs) | 94.9 | 99.5 | 4.8 | 112.6 | 118.3 | 5.1 |

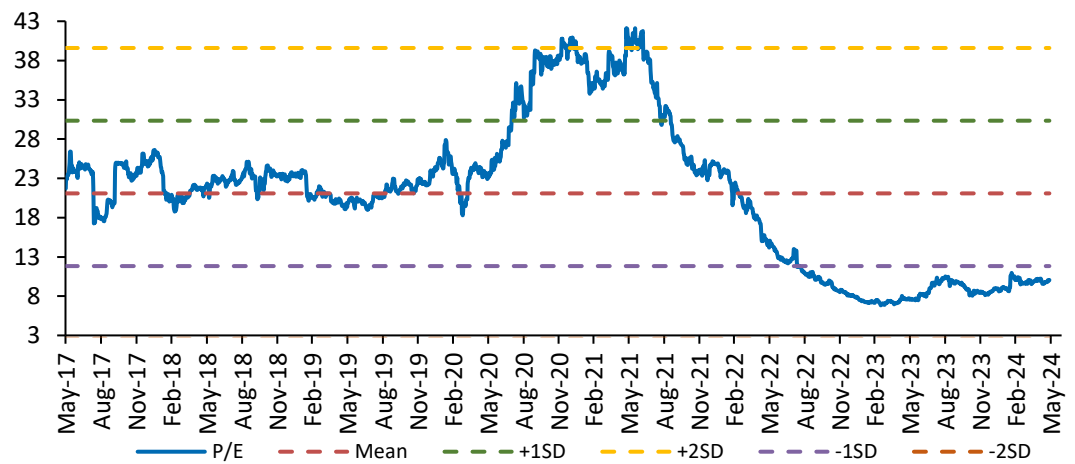
Source: Company, DART

Exhibit 4: SOTP based valuation

| Particulars | EPS Rs/share | P/E Multiple (x) | Value (Rs) |
|--------------------------|--------------|------------------|------------|
| Base Business EPS- FY26E | 36.4 | 24.4 | 889 |
| Key products opportunity | | | Value Rs |
| gRevlimid | | | 211 |
| gImbruvica | | | 44 |
| Target Price arrived | | | 1144 |

Source: Company, DART

Exhibit 5: One year forward P/E band



Source: Company, DART

Earnings call KTA's

Guidance

- Revenue growth to be around 15-20% for FY25.
- India business growth of 13-14% in FY25.
- PAT growth of 20%+ in FY25.
- Capex of Rs3.0-3.5bn for FY25 will be utilized for maintenance capex & expanding the capacity of existing facilities.

US

- In Q4FY24, the sales were mainly contributed by Revlimid.
- Natco has one NCE product in the early stage of phase 2 targeting oral cancer.
- Post gRevlimid, other big opportunities are –
 - Semaglutide, where the company has good filings on one particular strength in partnership with Viatris (filed from CMO site),
 - Olaparib is the other product in joint venture with Alembic where the company has sole FTF. Management believes it to be one of the important products after Semaglutide.
 - Imbruvica and Yondelis are other products where the company has sole FTF.
- The performance of Copaxone is consistent, and there are only two generics, Sandoz and Natco currently present in the market. There has been a slight decline in consumption, as many multiple sclerosis patients have transitioned to the oral formulation from the injectable formulation.
- The company has two sites for the US, located in Vizag and Hyderabad. Semaglutide will be manufactured through a CMO. For the top products, the company always maintains two sites as backup.
- Apart from Revlimid, Semaglutide is one of the biggest products, and Olaparib is expected to be the next biggest product, with Imbruvica expected within the next two to three years.
- The company recently filed Rimegepant from the Vizag plant.
- Natco expects key product launches in the next five years to include Semaglutide, Carfilzomib, Trabectedin, and Imbruvica.
- In the US, the focus is on complex generics or sole first-to-file (FTF) products, which are more profitable.

India

- In domestic formulations business, the company charged and accounted for a return of stock from super-stockist to C&Fs amounting to about Rs350mn due to a change in business model.
- MR count excluding contractors are 5000MR.

Agro

- In Crop Health Sciences Business (CHS), due to poor crop season the stock returns were more than expected at Rs250mn.
- Provision on assets of CHS division amounted to Rs300mn, due to non-utilization of certain assets used for manufacturing of Agro Intermediates.
- Expect First time generic launches in the CHS business.

- The CTPR combination has performed well. Due to high pricing, adoption was slow, prompting the expansion of the portfolio to capture a larger share of the market.

Other highlights

- During the quarter, good performance was achieved in Canada, Brazil, and the RoW business. Direct exports and subsidiary exports amount to almost US\$25mn to US\$26mn annually. The Canadian subsidiary has achieved nearly CAD40mn revenue.
- In FY25, the company plans to expand its business in Saudi Arabia and Egypt. Some very good orders have been received from these countries. The management plans to further diversify the RoW market.
- The company invested US\$2mn in Cellogen Therapeutics Private Ltd., with R&D programs involving Cell and Gene Therapy Solutions.
- The RoW business is quite similar to the domestic business, with a distribution arm and a presence in the branded market, providing broad-based and consistent earnings, and having valuations cheaper than those in India which is why the company is looking for M&A opportunities in the ROW market.
- The sustainability of the EBITDA margin depends upon the product mix.
- The other income includes Rs300mn from interest earned on deposits.
- The borrowings as of May'24 amounted to Rs11.6bn.
- Cash as of May'24 stood at Rs20.0bn.
- Majority of the company's shipments are through air route, as volumes are small owing to niche products.

Financial Performance

Profit and Loss Account

| (Rs Mn) | FY23A | FY24A | FY25E | FY26E |
|--|---------------|---------------|---------------|---------------|
| Revenue | 27,071 | 39,988 | 46,524 | 53,407 |
| Total Expense | 17,715 | 22,474 | 24,379 | 27,237 |
| COGS | 6,273 | 7,166 | 8,095 | 9,079 |
| Employees Cost | 4,867 | 5,250 | 6,048 | 6,409 |
| Other expenses | 6,575 | 10,058 | 10,235 | 11,749 |
| EBIDTA | 9,356 | 17,514 | 22,146 | 26,169 |
| Depreciation | 1,638 | 1,868 | 1,911 | 2,016 |
| EBIT | 7,718 | 15,646 | 20,234 | 24,153 |
| Interest | 145 | 192 | 189 | 186 |
| Other Income | 1,046 | 1,281 | 1,409 | 1,550 |
| Exc. / E.O. items | 0 | (510) | 0 | 0 |
| EBT | 8,619 | 16,225 | 21,454 | 25,517 |
| Tax | 1,466 | 2,852 | 3,647 | 4,338 |
| RPAT | 7,153 | 13,373 | 17,807 | 21,179 |
| Minority Interest | 0 | 0 | 0 | 0 |
| Profit/Loss share of associates | 0 | 0 | 0 | 0 |
| APAT | 7,153 | 13,883 | 17,807 | 21,179 |

Balance Sheet

| (Rs Mn) | FY23A | FY24A | FY25E | FY26E |
|-------------------------------|---------------|---------------|---------------|---------------|
| Sources of Funds | | | | |
| Equity Capital | 365 | 358 | 358 | 358 |
| Minority Interest | 0 | 0 | 0 | 0 |
| Reserves & Surplus | 48,373 | 58,173 | 72,419 | 89,362 |
| Net Worth | 48,738 | 58,531 | 72,777 | 89,720 |
| Total Debt | 1,667 | 3,712 | 3,662 | 3,612 |
| Net Deferred Tax Liability | 750 | 619 | 654 | 692 |
| Total Capital Employed | 51,155 | 62,862 | 77,093 | 94,023 |

Applications of Funds

| | | | | |
|---|---------------|---------------|---------------|---------------|
| Net Block | 24,269 | 24,908 | 26,002 | 26,991 |
| CWIP | 643 | 1,373 | 1,373 | 1,373 |
| Investments | 1,314 | 2,092 | 2,188 | 2,293 |
| Current Assets, Loans & Advances | 30,003 | 40,235 | 55,154 | 72,083 |
| Inventories | 7,429 | 7,005 | 12,767 | 14,656 |
| Receivables | 8,561 | 11,889 | 14,713 | 16,889 |
| Cash and Bank Balances | 5,463 | 9,529 | 15,345 | 27,647 |
| Loans and Advances | 102 | 90 | 90 | 90 |
| Other Current Assets | 5,398 | 7,287 | 7,360 | 7,433 |
| Less: Current Liabilities & Provisions | 5,074 | 5,746 | 7,623 | 8,716 |
| Payables | 2,638 | 2,355 | 3,630 | 4,056 |
| Other Current Liabilities | 2,436 | 3,391 | 3,993 | 4,660 |
| <i>sub total</i> | | | | |
| Net Current Assets | 24,929 | 34,489 | 47,531 | 63,367 |
| Total Assets | 51,155 | 62,862 | 77,093 | 94,023 |

E – Estimates

Important Ratios

| Particulars | FY23A | FY24A | FY25E | FY26E |
|---|----------|----------|----------|----------|
| (A) Margins (%) | | | | |
| Gross Profit Margin | 76.8 | 82.1 | 82.6 | 83.0 |
| EBIDTA Margin | 34.6 | 43.8 | 47.6 | 49.0 |
| EBIT Margin | 28.5 | 39.1 | 43.5 | 45.2 |
| Tax rate | 17.0 | 17.6 | 17.0 | 17.0 |
| Net Profit Margin | 26.4 | 33.4 | 38.3 | 39.7 |
| (B) As Percentage of Net Sales (%) | | | | |
| COGS | 23.2 | 17.9 | 17.4 | 17.0 |
| Employee | 18.0 | 13.1 | 13.0 | 12.0 |
| Other | 24.3 | 25.2 | 22.0 | 22.0 |
| (C) Measure of Financial Status | | | | |
| Gross Debt / Equity | 0.0 | 0.1 | 0.1 | 0.0 |
| Interest Coverage | 53.2 | 81.5 | 107.1 | 129.6 |
| Inventory days | 100 | 64 | 100 | 100 |
| Debtors days | 115 | 109 | 115 | 115 |
| Average Cost of Debt | 5.0 | 7.1 | 5.1 | 5.1 |
| Payable days | 36 | 21 | 28 | 28 |
| Working Capital days | 336 | 315 | 373 | 433 |
| FA T/O | 1.1 | 1.6 | 1.8 | 2.0 |
| (D) Measures of Investment | | | | |
| AEPS (Rs) | 40.0 | 77.6 | 99.5 | 118.3 |
| CEPS (Rs) | 49.1 | 88.0 | 110.2 | 129.6 |
| DPS (Rs) | 5.6 | 9.5 | 19.9 | 23.7 |
| Dividend Payout (%) | 14.0 | 12.2 | 20.0 | 20.0 |
| BVPS (Rs) | 272.3 | 327.0 | 406.6 | 501.2 |
| RoANW (%) | 15.7 | 24.9 | 27.1 | 26.1 |
| RoACE (%) | 14.7 | 24.7 | 25.7 | 25.0 |
| RoAIC (%) | 16.8 | 31.6 | 35.2 | 37.7 |
| (E) Valuation Ratios | | | | |
| CMP (Rs) | 1029 | 1029 | 1029 | 1029 |
| P/E | 25.8 | 13.3 | 10.3 | 8.7 |
| Mcap (Rs Mn) | 1,84,263 | 1,84,263 | 1,84,263 | 1,84,263 |
| MCap/ Sales | 6.8 | 4.6 | 4.0 | 3.5 |
| EV | 1,77,417 | 1,74,011 | 1,67,701 | 1,54,861 |
| EV/Sales | 6.6 | 4.4 | 3.6 | 2.9 |
| EV/EBITDA | 19.0 | 9.9 | 7.6 | 5.9 |
| P/BV | 3.8 | 3.1 | 2.5 | 2.1 |
| Dividend Yield (%) | 0.5 | 0.9 | 1.9 | 2.3 |
| (F) Growth Rate (%) | | | | |
| Revenue | 39.2 | 47.7 | 16.3 | 14.8 |
| EBITDA | 72.8 | 87.2 | 26.4 | 18.2 |
| EBIT | 93.5 | 102.7 | 29.3 | 19.4 |
| PBT | 326.3 | 88.2 | 32.2 | 18.9 |
| APAT | 77.2 | 94.1 | 28.3 | 18.9 |
| EPS | 77.2 | 94.1 | 28.3 | 18.9 |

E – Estimates

Cash Flow

| Particulars | FY23A | FY24A | FY25E | FY26E |
|--|----------------|----------------|----------------|----------------|
| Profit before tax | 7,573 | 14,944 | 20,045 | 23,967 |
| Depreciation & w.o. | 1,638 | 1,868 | 1,911 | 2,016 |
| Net Interest Exp | 145 | 192 | 189 | 186 |
| Direct taxes paid | (1,627) | (3,165) | (3,647) | (4,338) |
| Change in Working Capital | 1,237 | (4,574) | (6,747) | (3,009) |
| Non Cash | 0 | 0 | 0 | 0 |
| (A) CF from Operating Activities | 8,966 | 9,265 | 11,752 | 18,823 |
| Capex {(Inc.)/ Dec. in Fixed Assets n WIP} | (2,137) | (3,237) | (3,005) | (3,005) |
| Free Cash Flow | 6,829 | 6,028 | 8,747 | 15,818 |
| (Inc.)/ Dec. in Investments | 0 | 0 | 0 | 0 |
| Other | 1,046 | 1,281 | 1,409 | 1,550 |
| (B) CF from Investing Activities | (1,091) | (1,956) | (1,596) | (1,455) |
| Issue of Equity/ Preference | 0 | (7) | 0 | 0 |
| Inc./(Dec.) in Debt | (2,419) | 2,003 | (50) | (50) |
| Interest exp net | (145) | (192) | (189) | (186) |
| Dividend Paid (Incl. Tax) | (1,004) | (1,701) | (3,561) | (4,236) |
| Other | (905) | (3,347) | (539) | (593) |
| (C) CF from Financing | (4,473) | (3,243) | (4,340) | (5,065) |
| Net Change in Cash | 3,402 | 4,066 | 5,816 | 12,302 |
| Opening Cash balances | 2,061 | 5,463 | 9,529 | 15,345 |
| Closing Cash balances | 5,463 | 9,529 | 15,345 | 27,647 |

E – Estimates

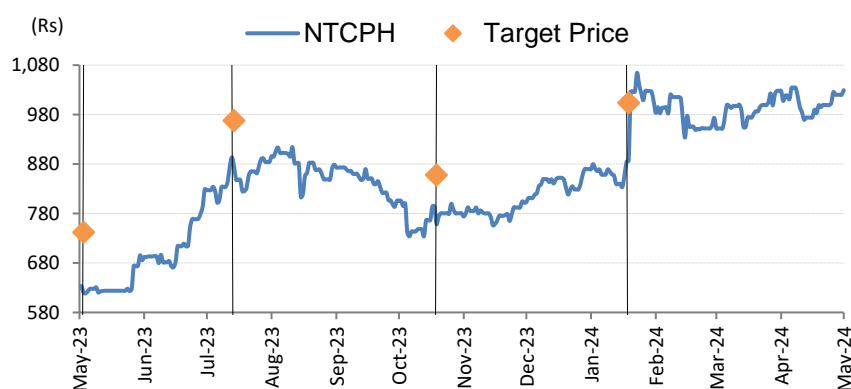
Notes

DART RATING MATRIX

Total Return Expectation (12 Months)

| | |
|------------|-----------|
| Buy | > 20% |
| Accumulate | 10 to 20% |
| Reduce | 0 to 10% |
| Sell | < 0% |

Rating and Target Price History



| Month | Rating | TP (Rs.) | Price (Rs.) |
|--------|------------|----------|-------------|
| May-23 | Accumulate | 742 | 620 |
| Aug-23 | Accumulate | 968 | 876 |
| Nov-23 | Accumulate | 858 | 759 |
| Feb-24 | Accumulate | 1,004 | 887 |

*Price as on recommendation date

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