# Glenmark Pharmaceuticals

04 March 2020

Reuters: GLEN.NS; Bloomberg: GNP IN

Initiating Coverage

## Strategic maneuvers and R&D discipline to drive outperformance

**We initiate coverage on Glenmark Pharma with a Buy rating and a target price of Rs390, based on 11x FY22 EPS. The target valuation multiple represents a steep discount to peers given that for more than a decade the company has been incurring a disproportionately large investment in NCE R&D - a high risk investment avenue. The stock can rerate and trade at higher multiples depending on the company's execution on its guidance of containing R&D spend and reducing debt. Currently, the combination of financial risk and business risk (NCE development) is suppressing valuation multiples.**

**The company is pursuing strategic initiatives (stake sale) for its NCE business (hived off into a new entity - Ichnos Sciences). A potential deal is largely contingent on the quality of clinical data emerging from its Phase 2b drug candidate – ISB 830 (OX 40 antagonist) in atopic dermatitis. The Phase 2b trial should report clinical data by the middle of 2020. The Phase 2a data has been encouraging and bodes well for a favorable outcome. In addition, Glenmark is seeking partners for further development of its other specialty assets like biosimilar Xolair.**

**Also, Glenmark is now sharply focused on improving free cash flow generation from the business. Over the decade (FY10-20), Glenmark has expanded its R&D investment at 33% CAGR, which has depressed earnings performance and free cash flows. Over this same period, net profit growth (9% CAGR) has lagged revenue growth (15% CAGR). However, going forward, reduction in R&D spend is expected on account of closure / completion of majority of ongoing Phase 2 trials on its NCE projects (ISB 830, ISC 27864, GSP 304). About US$20mn to US$30mn saving can accrue from the closure of such clinical trials.**

**From a growth standpoint, we see earnings growth outpacing revenue growth over FY20-FY22, led by the curtailment in R&D spend and 6% revenue CAGR. Revenue growth will be led by domestic sales, which have been outpacing IPM growth for the past decade. The domestic business is built around high growth therapy areas – dermatology, respiratory and cardiology. The recent launch of Remogliflozin (SGLT2) inhibitor will ensure that its presence in diabetes therapy also becomes profound.**

**The US business, which is its second largest segment, has also rebased due to price decline in limited competition assets. Hence, price erosion pressures in the US will be milder going forward. New ANDA launches (10-15 every year) should more than offset price erosion pressures and aid mid single digit growth. The API business, which is 10% of Glenmark sales, is also well placed in a favorable environment and can grow in mid to high single digits.**

**Defensive valuation:** Inability to reduce net debt has led to the valuation multiples being compressed to historically low levels. At CMP, the stock trades at 8x FY22 EPS, and less than 1x revenue. The risk-reward profile is favorable at this juncture as earnings growth, if accompanied by net debt reduction, can lead to a rerating in valuation multiple, which can add to the potential returns. A successful outcome from the atopic dermatitis drug candidate also remains a free call option.

| Y/E March (Rsmn) | FY18 | FY19 | FY20E | FY21E | FY22E |
|---|---|---|---|---|---|
| Net sales | 91,031 | 98,655 | 104,062 | 111,150 | 118,725 |
| EBITDA | 16,154 | 15,858 | 15,834 | 17,961 | 19,672 |
| Net profit | 8,039 | 9,250 | 7,240 | 8,655 | 9,997 |
| EPS (Rs) | 28.5 | 32.8 | 25.7 | 30.7 | 35.5 |
| *EPS growth (%)* | *(27.5)* | *15.1* | *(21.7)* | *19.5* | *15.5* |
| *EBITDA margin (%)* | *17.7* | *16.1* | *15.2* | *16.2* | *16.6* |
| PER (x) | 18.5 | 19.7 | 11.0 | 9.2 | 8.0 |
| P/BV (x) | 2.9 | 3.2 | 1.3 | 1.1 | 1.0 |
| EV/EBITDA (x) | 11.2 | 13.3 | 6.8 | 5.8 | 5.0 |
| *RoCE (%)* | *18.0* | *19.0* | *16.8* | *18.3* | *19.2* |
| *RoE (%)* | *15.6* | *16.5* | *11.6* | *12.3* | *12.5* |

*Source: Company, Nirmal Bang Institutional Equities Research*

## BUY

**Sector:** Pharmaceuticals

**CMP:** Rs282

**Target Price:** Rs390

**Upside:** 38%

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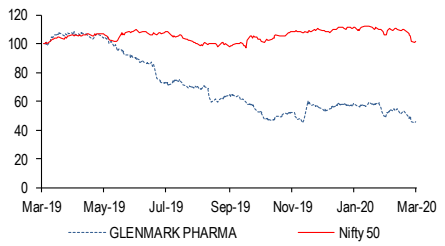
**Key Data**

| | |
|---|---|
| Current Shares O/S (mn) | 282.2 |
| Mkt Cap (Rsbn/US$bn) | 77.8/1.1 |
| 52 Wk H / L (Rs) | 667/267 |
| Daily Vol. (3M NSE Avg.) | 2,113,434 |

| Share holding (%) | 1QFY20 | 2QFY20 | 3QFY20 |
|---|---|---|---|
| Promoter | 46.6 | 46.6 | 46.6 |
| Public | 53.4 | 53.4 | 53.4 |
| Others | - | - | - |

**One-Year Indexed Stock Performance**




**Price Performance (%)**

| | 1 M | 6 M | 1 Yr |
|---|---|---|---|
| Glenmark Pharma | (8.2) | (29.5) | (54.0) |
| Nifty Index | (4.4) | 3.7 | 3.0 |

*Source: Bloomberg*

## Glenmark Investment Thesis – Opportunities and Risks

| OPPORTUNITY | RISK |
|---|---|
| R&D spend expected to subside as % of sales and help earnings growth outpace revenue growth | Specialty R&D investments will not yield earnings contribution in the near to medium term investment horizon. About 15 years of investment in NCE development w/o a meaningful commercial success is testing investors' patience |
| Multiple strategic initiatives to deleverage balance sheet which includes<br>1) **Potential Out-licensing Deals** – *ISB 830*, *Ryaltris* and *Xolair biosimilar*<br>2) **Stake sale in Ichnos Sciences** | Management failure to address debt concerns of investors in the past |
| Stock trades at a steep discount to its intrinsic value | Dividend payments have not meaningfully grown over the last 10 years and unlikely to change meaningfully in the near term as free cash flow would rather be used for debt repayment |
| Potential for EPS growth and rerating in valuation multiple Rerating would be driven by reduction in net debt | Capex needs might turn out to be higher and absorb any benefit of earnings growth on FCF generation |
| A positive outcome from ongoing Phase 2b trials on atopic dermatitis candidate (ISB 830) can be a game changer | A negative outcome may affect Glenmark's ability to raise capital by way of stake sale in Ichnos Sciences |
| Improving outlook for API business, led by greater management focus by carving the business out into a new entity | Adverse market conditions |
| Glenmark's domestic business growth has consistently outperformed IPM growth | DPCO related price cuts can take away any benefit of growth in sales |
| US business has rebased and should grow in low single digits to high single digits depending on execution of limited competition ANDA launches | Delay in approvals and regulatory risk remain the key risks to execution of US business growth |
| A fast growing consumer business in India, which is gaining critical mass and should improve profitability on gaining critical mass | - |

*Source: Company, Nirmal Bang Institutional Equities Research*

**ISB 830 clinical data in atopic dermatitis crucial for monetization of stake in Ichnos Sciences**

A Phase 2b trial is currently underway for ISB 830 in atopic dermatitis. The trial should report clinical data in a couple of months (by the end of 1QFY21). Existing evidence from Phase 2a studies suggests that the drug has benefits. The trial demonstrated that just two doses of IV administration of ISB830 led to an improvement in EASI (Eczema Area and Severity Index) and IGA score. ISB830 works through a unique mechanism of action and is believed to provide durability of response. There are only two other companies (Kyowa Hakko Kirin and Kymab) that are developing an OX40 antagonist for atopic dermatitis. A successful outcome in Phase 2b should raise confidence on Glenmark's efforts on the NCE front and more importantly ensure a successful stake sale in Ichnos Sciences.

**Phase 2a clinical data suggests ISB 830 appears to hold promise in Atopic Dermatitis**

A phase 2 proof-of-concept clinical trial on ISB 830 (OX 40 Antagonist) showed that only 2 intravenous doses of the drug, administered 4 weeks apart, induced significant improvement of tissue and clinical measurements until day 71 (42 days after the last dose). The study was primarily designed to assess safety and validate mechanism of action in atopic dermatitis. Signs of clinical efficacy were observed, as more patients achieved EASI-50 in the ISB 830 treated group vs. the placebo group. ISB 830 was well tolerated and tissue analysis showed significant reductions of Th1, Th2 and Th17/Th22-related markers as well as that of epidermal hyperplasia. This study provides first evidence for the pathogenic role of OX40 in AD and highlights the potential benefits of OX40 antagonism for the disease.

## PERFORMANCE ON KEY EFFICACY ENDPOINTS

**1. % Change in EASI (Eczema Area and Severity Index) Score**

On day 71, the percentage change from baseline indicated greater mean improvement with ISB 830 relative to placebo (56% and 38%, respectively). EASI scores between ISB 830–treated and placebo-treated subjects showed even greater separation through day 71 in severe subjects. On day 71 (final skin biopsy assessment visit), ITT response rates for ISB 830–treated subjects (EASI50, 76.9% [20/26]; EASI75, 42.3% [11/26]) were greater than response rates in placebo-treated subjects (EASI50, 37.5% [3/8]; EASI75, 25.0% [2/8]). All 5 subjects who achieved EASI75 on day 29 maintained their improvement until day 71.

| ISB 830 Versus Dupixent - Efficacy Comparison | | | | | |
|---|---|---|---|---|---|
| **Drug Name** | **Company** | **Status** | **EASI 50 Reduction** | **EASI 75 Reduction** | **IGA 0 or 1** |
| ISB 830 | Glenmark | Phase 2b | 40% | 17% | 12% |
| Dupixent | Sanofi | Launched | 50% | 47% | 33% |
| Lebrikuzumab | - | - | - | 35% | 30% |
| ISB 830 at week 10 – Dosed every 4 weeks. 3 doses administered at week 10.<br>Dupixent data at week 12 – Dosed every fortnight – 7 doses administered<br>Lebrikuzumab at week 16 – once every fortnight – 10 doses administered | | | | | |

**2. Patients with an IGA response**

The number of subjects with an IGA response (score of 0 or 1) on day 71 (week 10) was 6 (23.1%) of 26 for ISB 830 treated subjects compared to 1 (12.5%) of 8 for placebo-treated subjects.

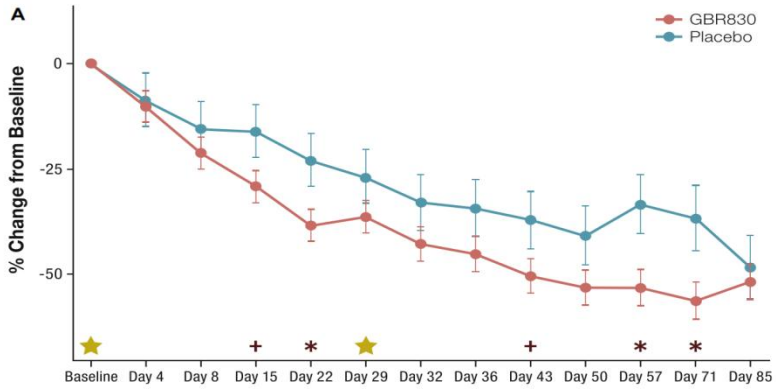
**3. % change in IGA score in severe patients**

Notably, the proportion of subjects with severe/very severe IGA scores at baseline was greater in the ISB 830 group (20/46[43.5%]) compared to the placebo group (5/16 [31.2%]). This finding is in line with the observation that EASI score improvement in subjects with severe disease at baseline (SCORAD score >50) might benefit more compared to the ITT population.

**4. % change in BSA and Pruritus NRS score**

The reduction in body surface area involvement and Pruritus NRS score demonstrated meaningful improvement versus baseline but was numerically comparable to the placebo group. The Phase 2b study outcome (expected around mid June 2020) should be more relevant to look at as the study is adequately powered to detect clinical significance.

**Exhibit 1: GBR 830 – Reduction in EASI score from Baseline**




*Source: Company, Nirmal Bang Institutional Equities Research*

### Competing OX40 antagonists in clinical pipeline

Kyowa Hakko Kirin – A Japanese pharmaceutical player is also working on an OX40 antagonist – KHK4083 - currently in Phase 2 studies. In a small Japanese study, KHK4083 has shown encouraging data. The study involved 22 patients with severe AD receiving only 3 intravenous doses, with sustained reductions in EASI.

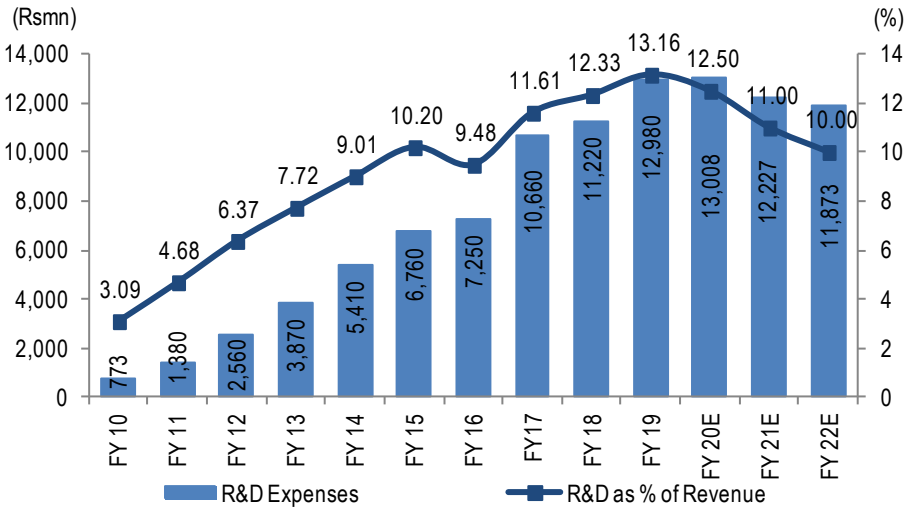
| OX 40 ANTAGONISTS PIPELINE | | | |
|---|---|---|---|
| **Company** | **Drug name** | **Indication** | **Clinical status** |
| Glenmark | ISB 830 | Atopic Dermatitis | Phase 2b |
| Kyowa Hakko Kirin | KHK4083 | Atopic Dermatitis | Phase 2a |
| Kymab | KY1005 | Atopic Dermatitis | Phase 2a |

| ATOPIC DERMATITIS PIPELINE IS CROWDED - CAN GLENMARK DIFFERENTIATE | | | | | |
|---|---|---|---|---|---|
| **Name** | **Status** | **Phase** | **n** | **Target type** | **Primary End Point** |
| **Biologics** | | | | | |
| Fevipiprant | Completed | II | 103 | CRTH2 mAb | Change in EASI week 12 |
| Timapiprant | Completed | II | 142 | CRTH2 mAb | Change in EASI week 16 |
| Omalizumab | Recruiting | IV | 62 | IgE mAb | Improvement AD week 24 |
| Ligelizumab (QGE031) | Completed | II | 22 | IgE mAb | Change in EASI week 12 |
| Ustekinumab | Completed | II | 79 | IL-12/IL-23 mAb | Change in EASI week 12 |
| Lebrikizumab (3 doses) | Completed | II | 212 | IL-13 mAb | EASI50 week 12 |
| Tralokinumab | Not Yet Recruiting | III | 780 | IL-13 mAb | IGA, EASI75 week 16 |
| Secukinumab 300mg | Recruiting | II | 44 | IL-17 mAb | Change in Epidermal Thickness |
| Nemolizumab | Not Yet Recruiting | II | 250 | IL-31 mAb | Change in EASI week 24 |
| Dupilumab | Completed | III | 240 | IL-4Ra mAb | IGA, EASI75 week 16 |
| Mepolizumab 100mg | Recruiting | II | 56 | IL-5 mAb | IGA week 16 |
| Fezakinumab | Not Yet Recruiting | II | 60 | IL-22 mAb | SCORAD, safety |
| ISB 830 | Recruiting | II | 64 | OX40 mAb | TEAE, improvement in pathology week 12 |
| Tezepelumab | Completed | II | 155 | TSLP mAb | EASI50 week 12 |
| **Small Molecules** | | | | | |
| Baricitinib | Completed | II | 124 | JAK1 + 2 antagonist | EASI90 week 16 |
| AQX-1125 | Completed | II | 54 | SHIP1 activator | TLSS |
| Aprimelast 30 or 40mg | Completed | II | 191 | PDE4 antagonist | Change in EASI week 12 |
| Serlopitant (2 doses) | Recruiting | II | 450 | NK1 receptor antagonist | Itch intentsity week 6 |
| Tradipitant | Recruiting | II | 150 | NK1 receptor antagonist | Pruritus VAS week 2 |
| Asimadoline | Recruiting | II | 200 | k-opiod receptor antagonist | number of patients with AE |
| Upadacitinib (3 doses) | Recruiting | II | 167 | JAK1 antagonist | Change in EASI week 16 |
| PF-04965842 | Recruiting | II | 268 | JAK1 antagonist | IGA week 12 |

**Large ongoing clinical trials should close by end of 4QFY20/1QFY21 translating into a reduction in R&D spend –** 60% of the R&D spend by Glenmark is on specialty R&D. Lately, there has been efforts to restrict this spend and prioritize efforts. The ongoing Phase 2 trial on its lead asset ISB 830 is nearing completion (4QFY20) and Glenmark should save about US$15mn annually in R&D spend post completion of this trial. In addition, ongoing Phase 2 studies on GRC 27864 have recently concluded. The drug is likely to be discontinued as it has not demonstrated clinical benefit. Likewise, ongoing Phase 2 trials on GSP304, which is a nebulized version of Tiotropium (Spiriva) for the treatment of COPD, also stands completed, which should allow savings to be reflected from 4QFY20 onwards. In our view, Glenmark may not be taking this project further.

In case ISB 830 is successful in ongoing Phase 2b trial, the company would look to out-license the same and hence incremental spend on the product will not be out of Glenmark P&L. The company has also concluded Phase 1 trials on its biosimilar version of Xolair (Omalizumab) and is looking to out-license the same.

**Exhibit 2: R&D Expenses Trend**

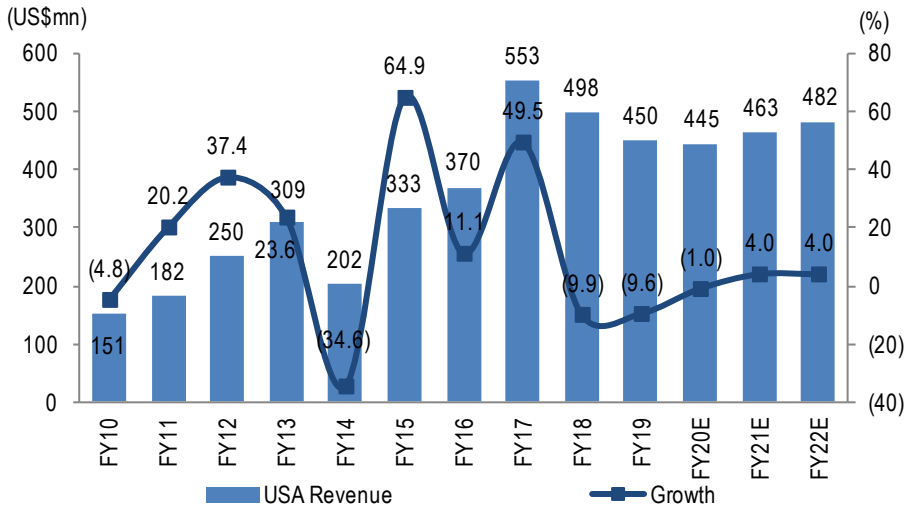



*Source: Company, Nirmal Bang Institutional Equities Research*

## US business highlights

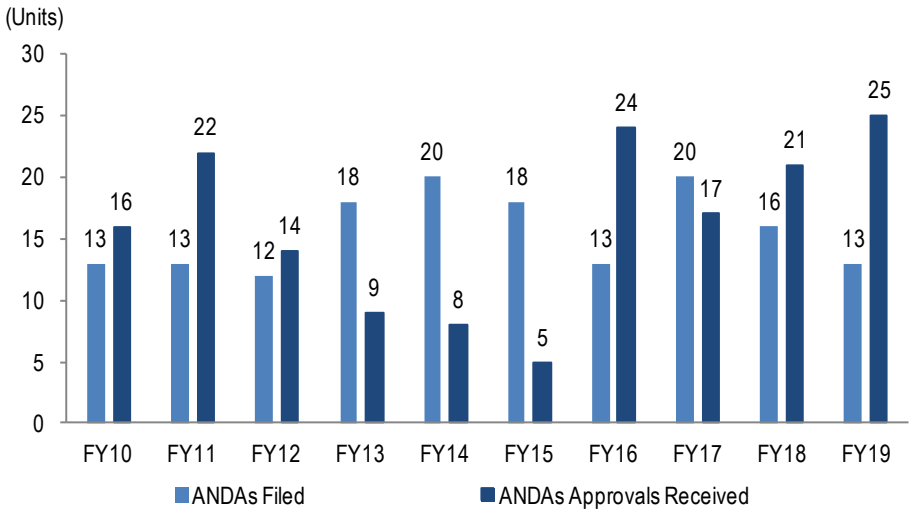
- Glenmark is the 14th largest generics manufacturer by prescription volume and the products are used to fill about 83mn scrips each year in the US. Over the last 10 years, the company has grown the US business at 16% CAGR but due to recent cost pressures, the revenue has seen a decline of 9.9% and 9.6% in the last two years.
- The company has shifted focus from vanilla generic oral solids to value-added niche generics in relatively high barrier-to-entry segments such as oral contraceptives and skin treatments.
- In the US, the company continues to seek approvals for new products while improving cost efficiency and defending the market share. The company has consistently gained market share in Naproxen, Mupirocin, Omeprazole, Olmesartan, Verapamil ER and Clobetasol propionate.
- The Baddi formulations facility remains under warning letter and the resolution of the same is critical in order for Glenmark to sustain its base business in the US.

**Exhibit 3: US business revenue growth**



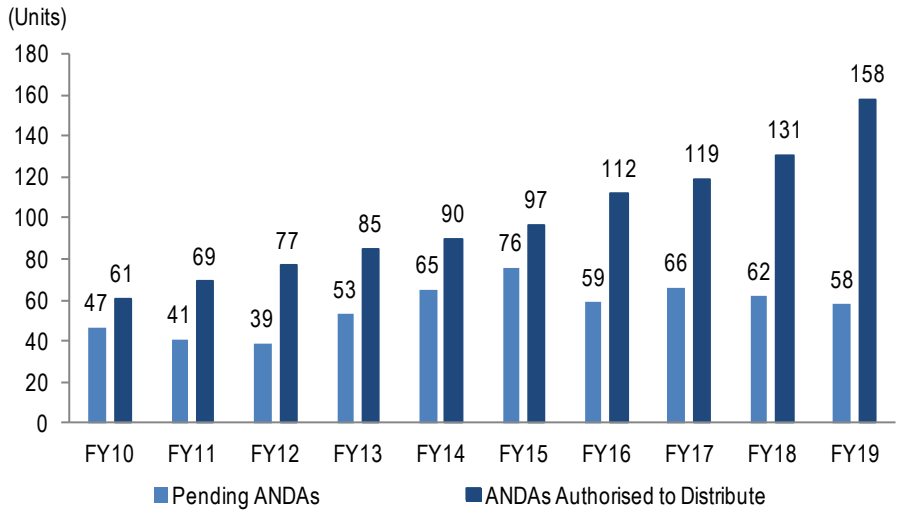

*Source: Company, Nirmal Bang Institutional Equities Research*

**Exhibit 4: US ANDAs filed and approvals received**




*Source: Company, Nirmal Bang Institutional Equities Research*

**Exhibit 5: US ANDAs pending and authorised to distribute**




*Source: Company, Nirmal Bang Institutional Equities Research*

**Exhibit 6: Products where Glenmark has above 10% market share**

| Glenmark Market Share (%) | 2014 | 2015 | 2016 | 2017 | 2018 | 2019 |
|---|---|---|---|---|---|---|
| Omeprazole | 0.0 | 3.6 | 10.7 | 12.8 | 16.9 | 16.5 |
| Pravastatin Sodium | 23.7 | 24.5 | 23.1 | 19.2 | 15.8 | 15.9 |
| Fluconazole | 21.6 | 20.3 | 22.1 | 17.6 | 13.4 | 16.7 |
| Ondansetron Odt | 25.4 | 34.4 | 22.7 | 14.3 | 11.5 | 13.1 |
| Naproxen | 6.3 | 18.9 | 39.6 | 40.5 | 44.3 | 45.3 |
| Ondansetron Hcl | 34.1 | 35.0 | 36.4 | 31.2 | 25.4 | 24.2 |
| Topiramate | 12.9 | 14.4 | 16.6 | 17.7 | 14.9 | 11.7 |
| Mupirocin | 13.3 | 15.0 | 35.0 | 36.2 | 34.6 | 33.8 |
| Clobetasol Propionate | 0.0 | 0.0 | 0.0 | 0.2 | 7.5 | 12.5 |
| Ropinirole Hcl | 22.9 | 21.6 | 20.7 | 19.0 | 18.4 | 22.8 |
| Olmesartan Medoxomil | 0.0 | 0.0 | 0.0 | 0.0 | 5.2 | 19.1 |
| Levocetirizine Dihydrochloride | 17.5 | 33.2 | 36.4 | 33.9 | 24.6 | 29.3 |
| Oxcarbazepine | 34.4 | 31.7 | 28.1 | 29.1 | 27.5 | 26.7 |
| Pramipexole Dihydrochloride | 43.3 | 48.2 | 45.2 | 40.6 | 42.3 | 47.6 |
| Verapamil Er | 25.2 | 41.6 | 40.6 | 45.2 | 45.6 | 80.2 |
| Drospirenone-Ethinyl Estradiol | 0.0 | 6.6 | 48.5 | 46.3 | 36.4 | 49.6 |
| Norgestimate-Ethinyl Estradiol | 100.0 | 100.0 | 70.4 | 62.8 | 60.9 | 71.4 |

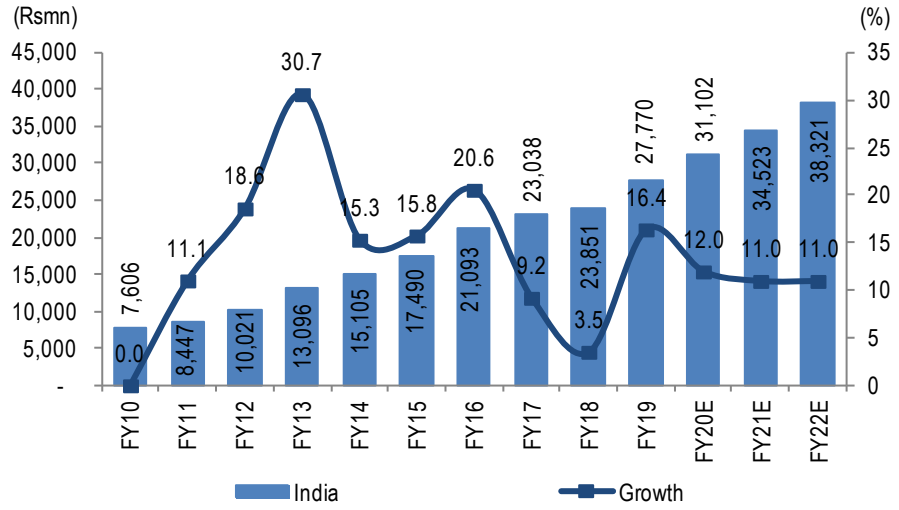
*Source: Bloomberg, Nirmal Bang Institutional Equities Research*

## Ryaltris™

- Ryaltris™ [Olopatadine hydrochloride (665 mcg) and Mometasone Furoate (25 mcg)], developed by Glenmark, is a novel fixed-dose combination nasal spray of an anti-histamine and a steroid, indicated for the treatment of symptoms associated with seasonal allergic rhinitis (SAR) in patients over 12 years of age.
- Ryaltris™ is currently under review with the USFDA as a treatment for seasonal allergic rhinitis in the US. During 3QFY20, the company filed an application for Ryaltris approval in the European Union.
- The company has entered into an exclusive licensing deal with Hikma for the commercialization of the product in the US. Under the terms of the agreement, Glenmark will be responsible for the continued development and regulatory approval of Ryaltris™ by the USFDA, while Hikma will be responsible for the commercialization of Ryaltris™ in the US. Hikma would also have the ability to produce the product utilizing its nasal manufacturing capabilities in Columbus, Ohio.
- Glenmark will receive an upfront payment, regulatory approval and commercial milestone payments as well as royalties from Hikma for Ryaltris™.
- The agreement with Hikma is Glenmark's fourth regional licensing deal for Ryaltris™. Glenmark has already signed licensing deals for commercialising Ryaltris™ in China (Grand Pharma Co. Ltd), Australia (Seqiris), New Zealand and South Korea (Yuhan Corporation).

## India business

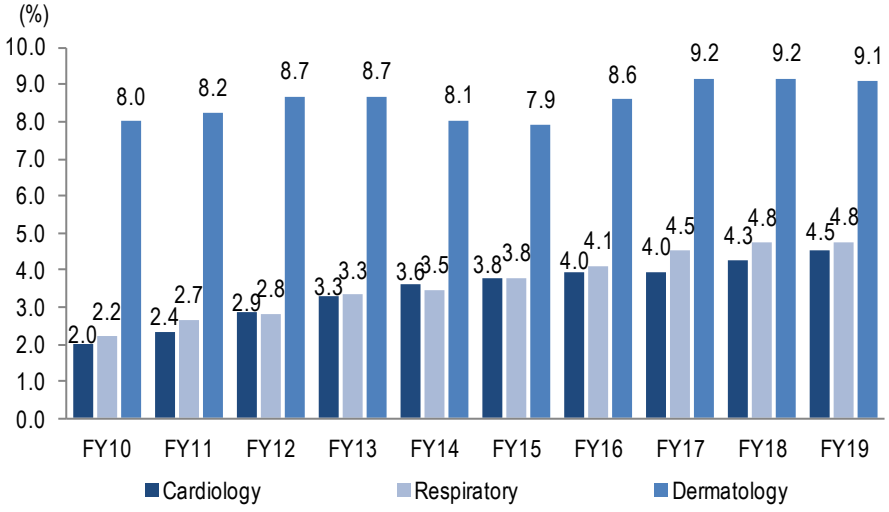
**Exhibit 7: India business revenue growth**




*Source: Company, Nirmal Bang Institutional Equities Research*

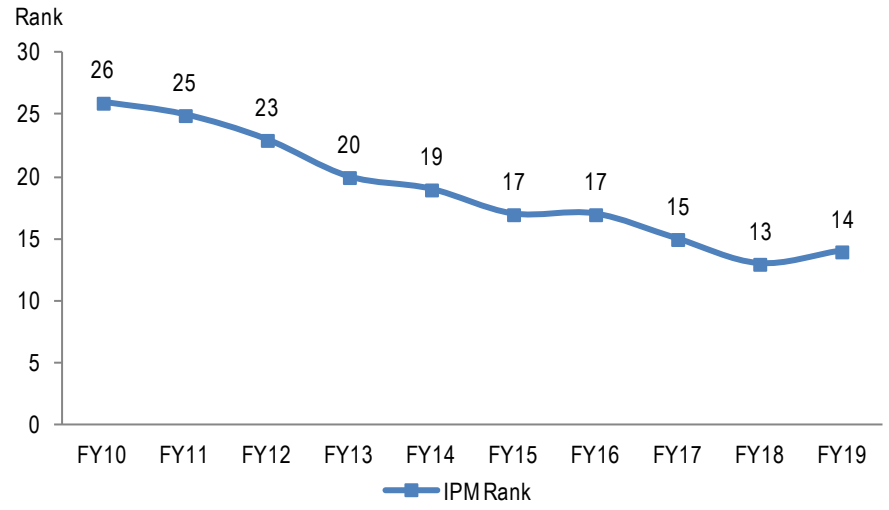
- In India, the company has shown consistent growth over the last 10 years, growing faster than the Indian Pharmaceutical Market (IPM). The company has grown at 17% CAGR from FY2010 to FY2019 against market growth of low double digits over the same period. As a result, the company's market share has risen from 1.46% to 2.18%. The Indian business is concentrated in few chronic therapies, making the company immune to seasonal fluctuations.
- The company was ranked 26 in FY2010, but consistently outgrowing the market has enabled it to gain market share and was ranked 14th in FY2019. Going forward, the company is expected to outperform the market with new launches. The company has 9 products in the Top 300 products in IPM.
- The company has three key focus therapeutic areas viz., Dermatology, Respiratory and Cardiology, which are ranked 2nd, 4th and 6th in IPM. The company has consistently grown the market across these three therapies. In Anti-Diabetics segment, Glenmark became the first company to launch the novel patent-protected and globally researched SGLT2 inhibitor Remogliflozin Etabonate 100 mg for Type 2 diabetes.
- The company has a strong presence across OTC segments as well with Candid Dusting Powder (DP) and Scalpe+. Candid DP is a 30 year-old flagship and a prescription leader in the category of fungal skin infection. Scalpe+ is a 17-year old brand with a proven track record in dandruff treatment.

**Exhibit 8: India business mix trend**



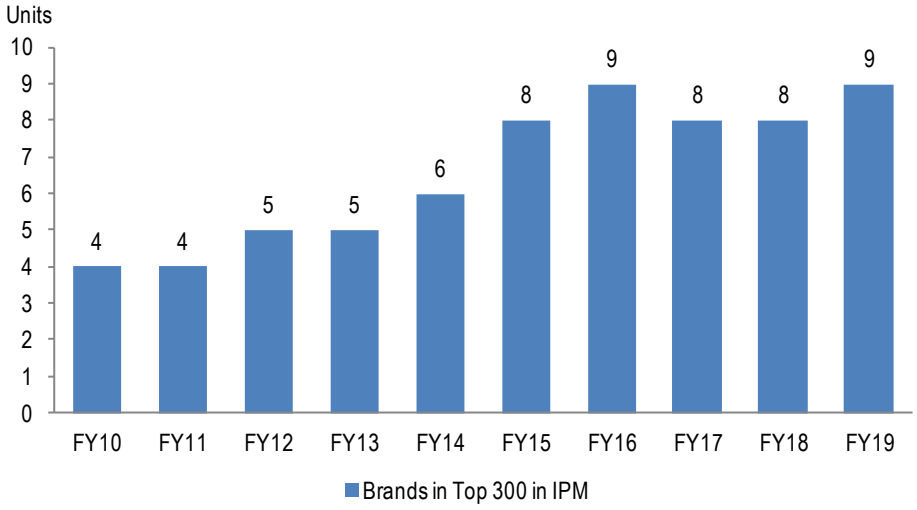

*Source: Company, Nirmal Bang Institutional Equities Research*

**Exhibit 9: India business rank in IPM**



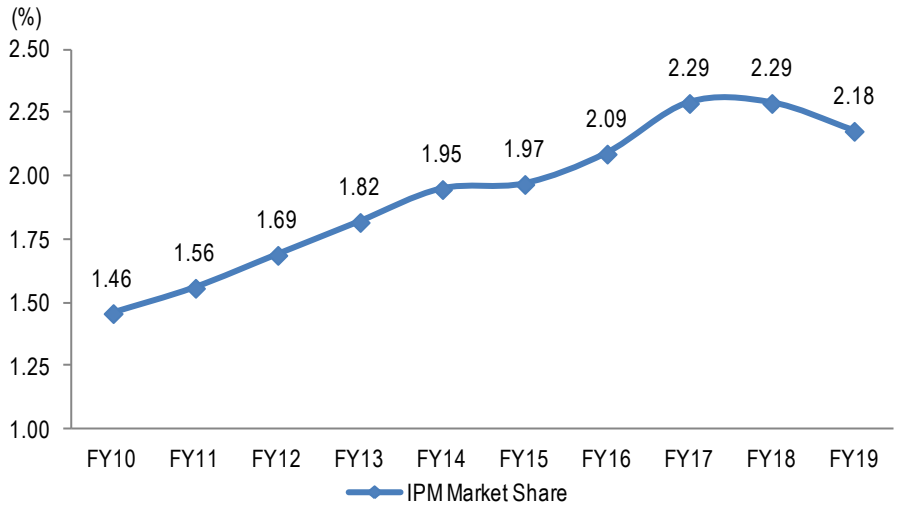

*Source: Company, Nirmal Bang Institutional Equities Research*

**Exhibit 10: Glenmark's brands in Top 300 brands in IPM**




*Source: Company, Nirmal Bang Institutional Equities Research*

**Exhibit 11: Glenmark's market share in IPM**




*Source: Company, Nirmal Bang Institutional Equities Research*

**Remogliflozin should help Glenmark build a strong diabetes platform**

Glenmark is the first company in the world to launch Remogliflozin and India is the first country to get access to this innovative drug. Remogliflozin Etabonate is a novel SGLT2 Inhibitor: Glenmark in-licensed Remogliflozin from BHV Pharma and has gained approval for marketing in India based on Phase 3 trials.

**Exhbit 12: SGLT2 Drugs Marketed in India**

| Molecule – SGLT2 inhibitors | Innovator | Marketing Partners | Daily cost | Dosing |
|---|---|---|---|---|
| Empagliflozin | Boehringer Ingelheim | Lupin | 57 | Once daily |
| Cannagliflozin | Johnson & Johnson | Cipla, USV | 55 | Once daily |
| Dapagliflozin | AstraZeneca | Sun Pharma | 55 | Once daily |
| Remofliflozin | Glenmark and BHV Pharma | Mankind Pharma and Torrent Pharma | 25 | Twice Daily |

## SGLT2 Inhibitor Market

SGLT2 Inhibitor represents a Rs6,000-7,000mn market opportunity in India and continues to expand rapidly. The key attributes of this class that is translating into rapid acceptance being

1) *Effective Glycemic Control*
2) *Complementary mechanism of action*
3) *Weight loss benefit*
4) *Does not raise hypoglycaemia risk*
5) *Offers renal protective effect*
6) *Mild reduction in blood pressure*
7) *Proven benefit in reducing cardiovascular risk*

**Current market share of SGLT2 inhibitors in the diabetes market and potential market opportunity**

The SGLT2 class is a relatively new treatment modality in the diabetes space and hence the market penetration is low (about 1% in volume terms). However, evidence of superior cardiovascular benefit and renal protection that has emerged from several large outcome studies conducted on this class of drugs is pushing physicians to use the class of drugs more often.

**Renal protection benefits are unique and not associated with any other class of drugs for diabetes**

A Meta analysis of clinical data on the most widely used SGLT2 inhibitors suggests renal protective effect of SGLT2 inhibitors. The meta-analysis suggests that the use of SGLT2 inhibitors cuts the risk for the primary composite end point of dialysis, kidney transplant or mortality from kidney disease by 33% with consistent benefit observed across trials. In addition, they also reduced the risks of End Stage Renal disease and Acute Kidney Injury by 35% and 25%, respectively, allaying earlier concerns that SGLT2 inhibitors increase AKI risk.

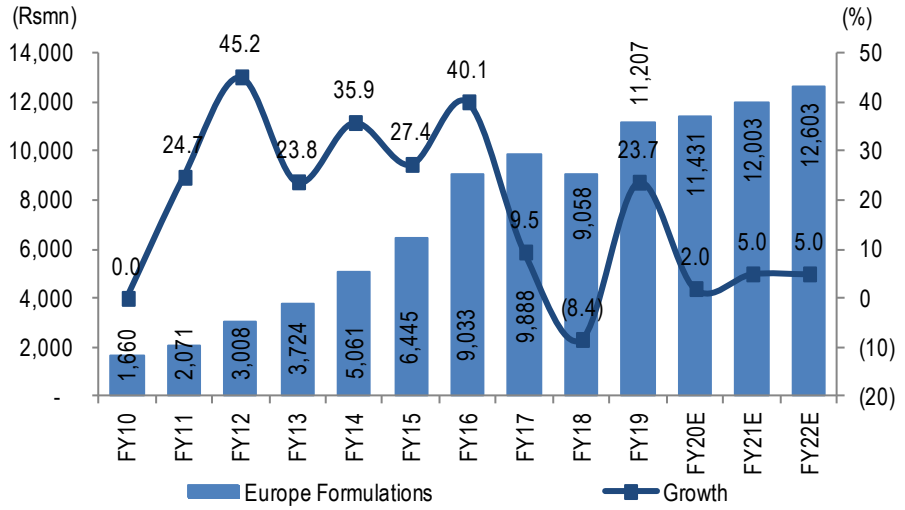
**About 20-25% of diabetes patients have concomitant chronic kidney disease (CKD)**

Assuming one third penetration of SGLT2 inhibitors in the diabetes patients having concomitant CKD, the market share of SGLT2 inhibitors can expand multi-fold from here on. Assuming the build-up happens over the next five years, SGLT2 opportunity can expand to a Rs5000 crore market. Remogliflozin by virtue of its affordability benefit can gain a fair share of the pie.

## Europe

- Glenmark is one of the fastest-growing mid-size/large players in Europe. This has been achieved through a combination of portfolio expansion and geographical spread.
- The company's geographical footprint covers all major markets in Western Europe (WEU) and Central and Eastern Europe (CEE).
  - In WEU, the company has a third party out-licensing business commercializing key molecules developed in-house via partners across several markets.
  - In CEE, along with prescription drugs, over-the-counter (OTC) medicines are a key growth driver for Glenmark with almost 40% of the CEE business being brought in by the OTC franchise.
- The business has leveraged not just its in-house pipeline, but also added a significant component of in-licensing partnerships to develop a robust portfolio, delivering strong growth over the last decade.
- Glenmark has clocked a growth of 24% over the last 10 years, which is significantly higher than the market growth. We expect the company to clock a growth of mid single digits over the next two years.

**Exhibit 13: Europe business revenue growth**



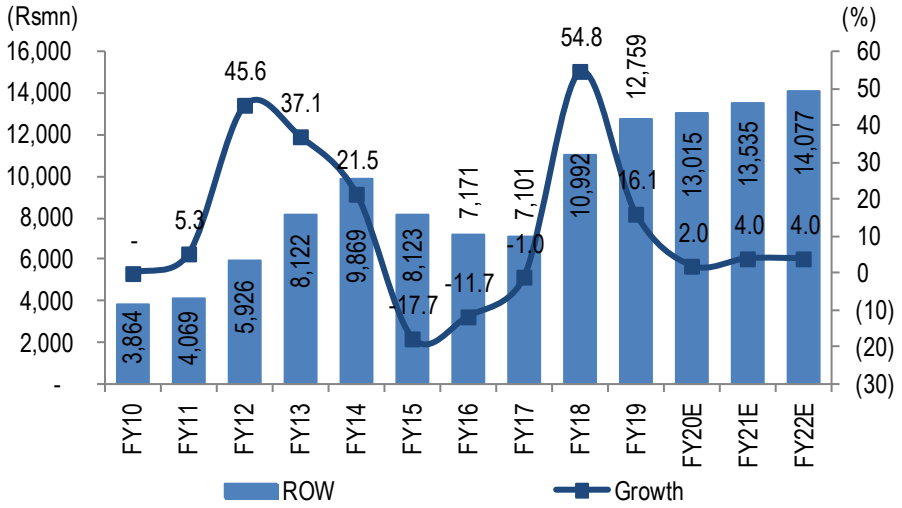

*Source: Company, Nirmal Bang Institutional Equities Research*

## ROW and LATAM

### RoW

- Glenmark started its business in Russia-CIS region in 1980 and is currently ranked 44 in the retail segment in Russia. According to the IQVIA data for MAT (March 2019), Glenmark Russia recorded a growth of 8.3% in value vis-á-vis overall retail market growth of 5.8%. In the dermatology segment, Glenmark showed growth of 1.6% in value vis-á-vis overall dermatology market growth of 2.2% in value.
- As a result of the strong position of Glenmark Russia in the dermatology segment (retail), the company continues to rank in the Top-15 of all derma companies present in the market, with MAT March 2019 rank being 11. Among the companies present in the expectorants market (retail segment) of the local pharmaceutical market, Glenmark has a strong position and ranks 4th as of MAT March 2019.
- Other key markets across the CIS region include Ukraine and Kazakhstan. In other CIS markets, Glenmark Ukraine showed secondary sales growth of 26% in value in FY2018-19.
- The Africa region performed well in FY2018-19, recording growth in excess of 30%. The subsidiaries in South Africa and Kenya grew in excess of 30% for the financial year. The Africa business launched 56 products in the region for the entire financial year. The company will look to consolidate its position in the African markets with growth coming via in-licensing of complex generics that provide first-to-file opportunities.

**Exhibit 14: RoW business revenue growth**

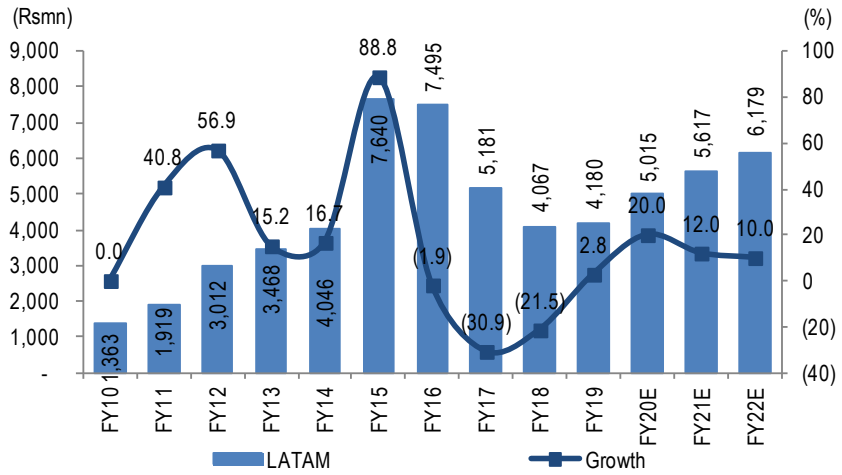



*Source: Company, Nirmal Bang Institutional Equities Research*

## LATAM

- The LATAM business contributes 4% to the total business for Glenmark and the overall performance for the overall region continued to remain subdued. The company has launched unique offerings such as Nebzmart handheld nebulizer, nasal sprays and MDI devices in the respiratory segment and a microsphere formulation of adapalene + clindamycin in dermatology, which offer benefits and more choice for prescribers and patients.
- In Brazil, Glenmark has entered into an exclusive partnership with Novartis to promote and distribute three of its respiratory brands.
- In the Caribbean region, Glenmark launched Momate AZ in the respiratory franchise. It has been a key game changer for Glenmark in the Rhinitis Allergis segment and has helped to position the company as a differentiated player with a unique product in the market.
- In Colombia, Glenmark launched Glemont to complement the respiratory portfolio.
- We foresee 10-12% growth in revenue in the next two years.

**Exhibit 15: LATAM business revenue growth**

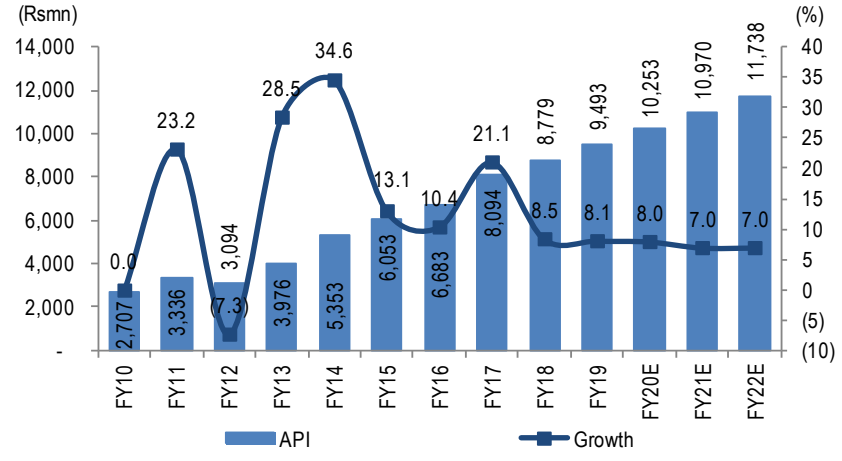



*Source: Company, Nirmal Bang Institutional Equities Research*

## API:

- Glenmark entered the API business in 2003 and built a large business based on strong product selection, focus on key regulated markets, maintaining high operational efficiencies and strong compliance culture. The API business has grown at a CAGR of 15% over the last 10 years while maintaining consistently high EBITDA margin. Overall EBITDA margin recorded for the business in FY19 was in excess of 30%.
- Glenmark transferred its API business to a wholly-owned subsidiary, Glenmark Life Sciences Ltd (GLS), which became operational on January 1, 2019. Over 75% of GLS revenue is supplied to regulated markets of Europe, USA and Japan. The top 10 molecules contribute 60% to the overall revenue of GLS.

**Exhibit 16: API business revenue growth**




*Source: Company, Nirmal Bang Institutional Equities Research*

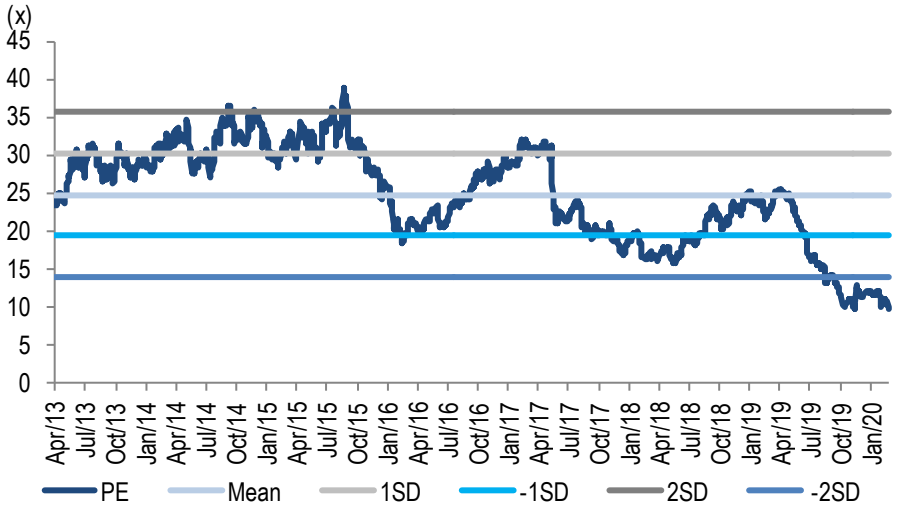
## Valuation

We value Glenmark at 11x FY22E EPS and arrive at a target price of Rs390. The valuation multiple is in line with its current valuation, which has seen a steep correction from its historical average (25x). The correction reflects investor impatience with respect to the company's inability to reduce net debt meaningfully and ongoing disproportionate investment in high risk NCE R&D. Most therapeutic targets that Glenmark is chasing are not validated in terms of proof of concept studies and the track record is also not supportive.

We estimate the FY22 EPS at 35.5, a growth of CAGR 2% over FY19 base earnings. Key assumptions for earnings growth being

1) India domestic business should grow faster than IPM, driven by selective presence in high growth therapies such as dermatology, respiratory and cardiology. Recent launch of Remogliflozin (SGLT2) inhibitor will ensure its presence in diabetes therapy also becomes profound, which it can leverage for further augmenting growth.
2) The US business will exhibit subdued growth trend (mid single digits) as we risk adjust our forecasts for any adverse regulatory action and mild price erosion pressures.
3) European and ROW businesses are expected to grow in low to mid single digits.
4) The API business is expected to grow at high single digits whereas the LATAM business is expected to grow in double digits on favorable bases and new launches in the region.

**Exhibit 17: Historical price/earnings ratio of Glenmark Pharmaceuticals**



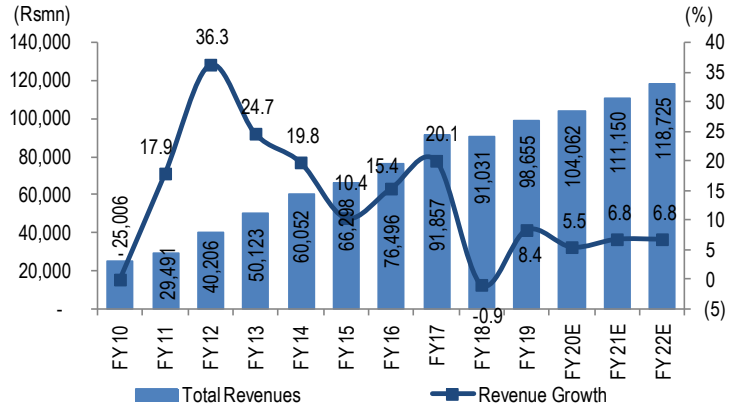

*Source: Bloomberg, Nirmal Bang Institutional Equities Research*

## Risks to our recommendation

1) **Regulatory compliance** remains the key risk. Warning letters remain key issues to be resolved. The company has received a warning letter for its Baddi facility.
2) **Exchange rate** – Depreciation/appreciation of USD versus INR can have an adverse/favorable impact on earnings versus our forecasts.
3) **Execution and commercialization capabilities** for new as well as existing products are a key risk. With a large NCE pipeline, the company faces a lot of risk in terms of successful trials and marketing. The company in the past has dropped a lot of NCEs due to failure in clinical trials.
4) **DPCO risk –** The risk of additional drugs coming under price control, which is expected to be announced next year, is a major risk to the India business of Glenmark. The value growth of India business will largely depend on the extent of price control on drugs marketed by Glenmark.
5) **CapEx needs -** Higher than anticipated CapEx needs will affect net debt reduction - higher than anticipated CapEx adversely impacts free cash flows and hence reduction in net debt.

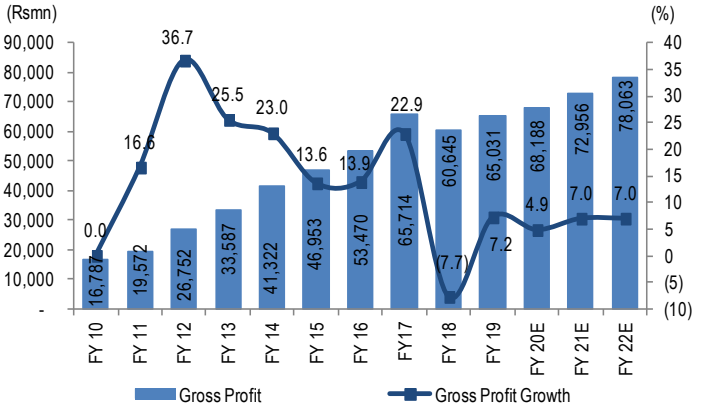
# Ratio charts

### Exhibit 18: Revenue and revenue growth



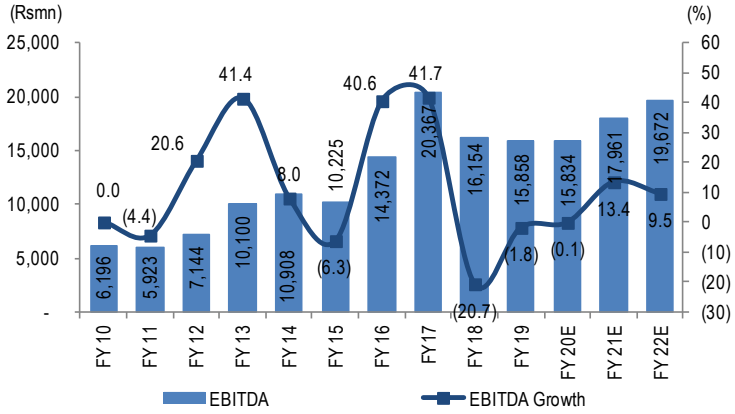

*Source: Company, Nirmal Bang Institutional Equities Research*

### Exhibit 19: Gross profit and growth



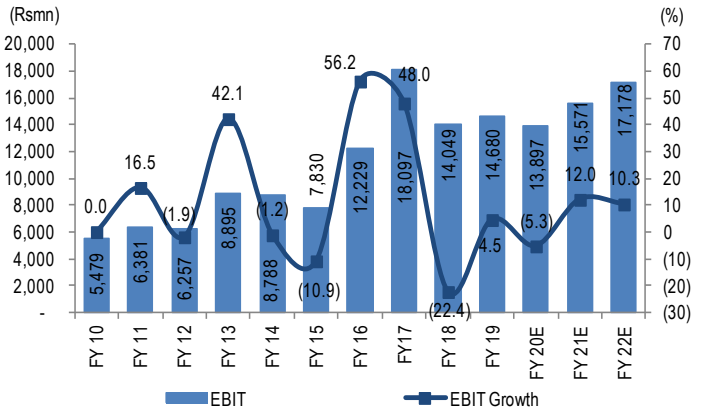

*Source: Company, Nirmal Bang Institutional Equities Research*

### Exhibit 20: EBITDA and EBITDA growth



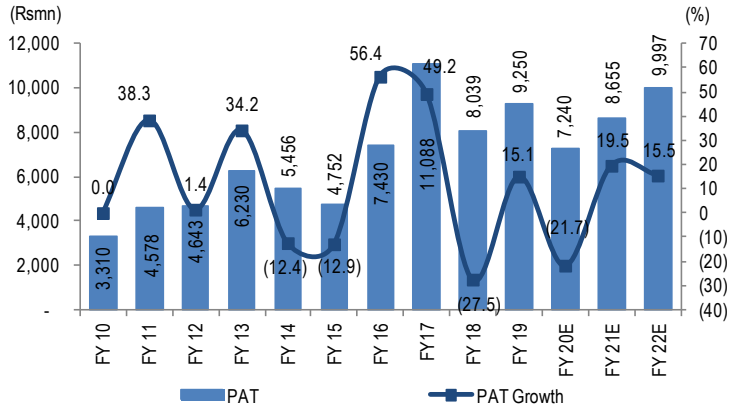

*Source: Company, Nirmal Bang Institutional Equities Research*

### Exhibit 21: EBIT and EBIT growth



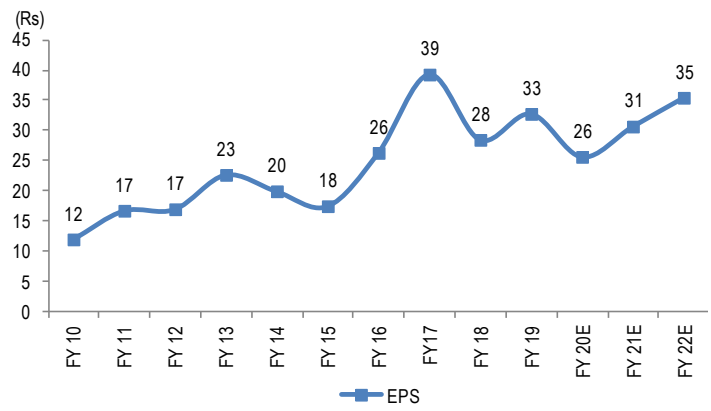

*Source: Company, Nirmal Bang Institutional Equities Research*

### Exhibit 22: PAT and PAT growth



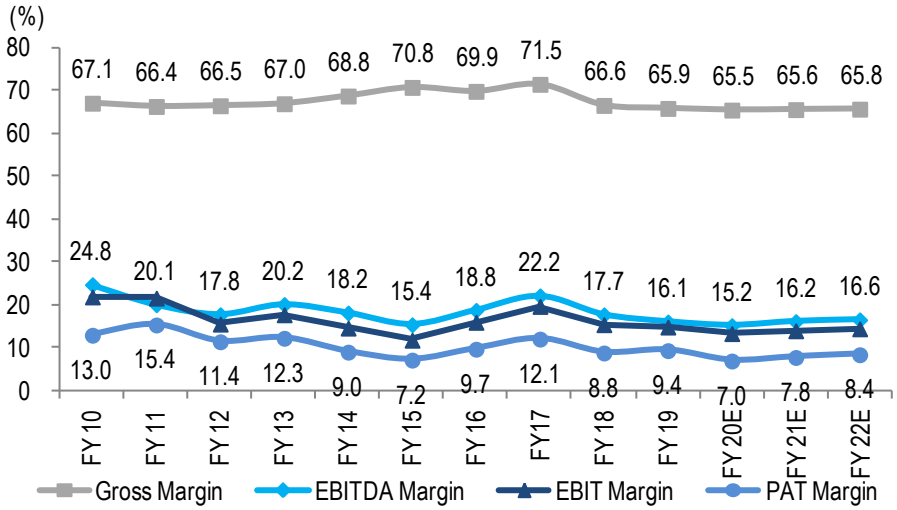

*Source: Company, Nirmal Bang Institutional Equities Research*

### Exhibit 23: EPS



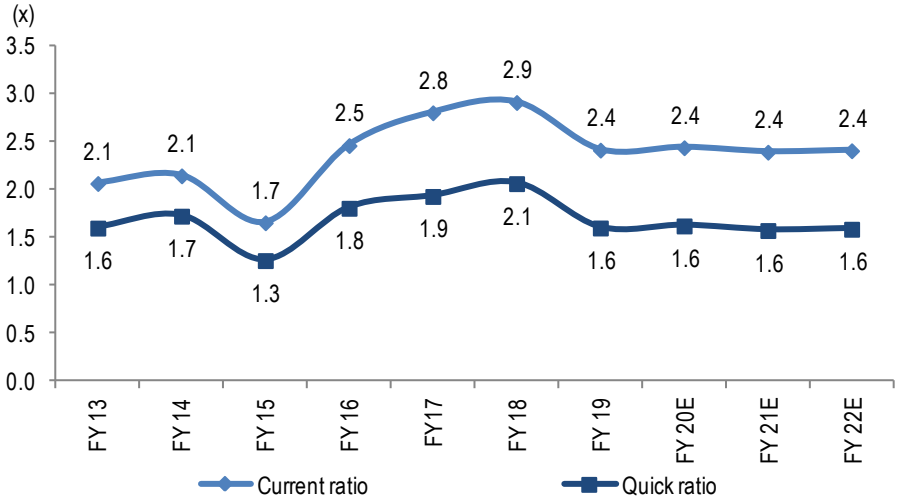

*Source: Company, Nirmal Bang Institutional Equities Research*

**Exhibit 24: Margin profile**



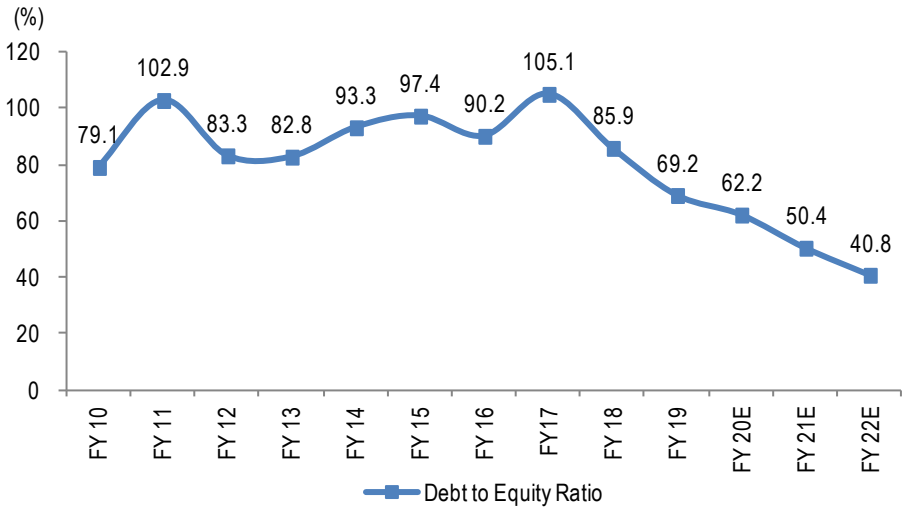

*Source: Company, Nirmal Bang Institutional Equities Research*

**Exhibit 25: Current ratio and cash ratio**



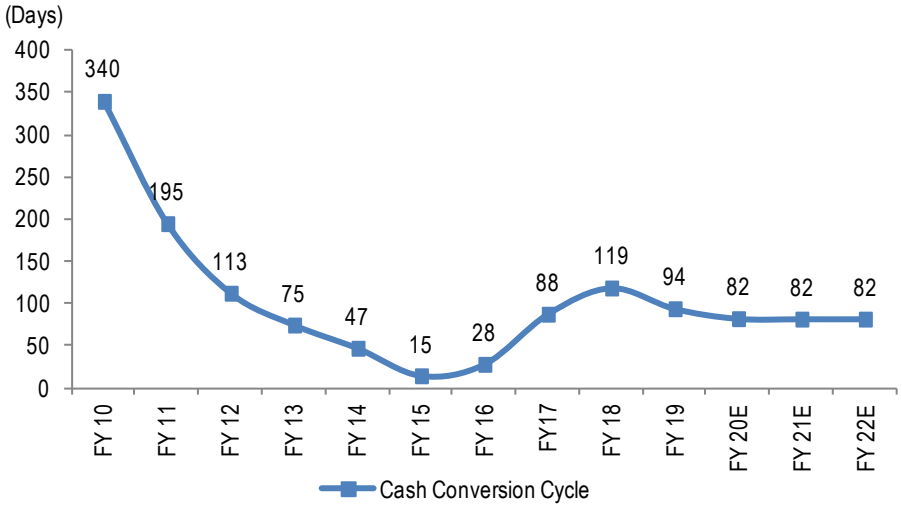

*Source: Company, Nirmal Bang Institutional Equities Research*

**Exhibit 26: Debt-to-equity ratio**



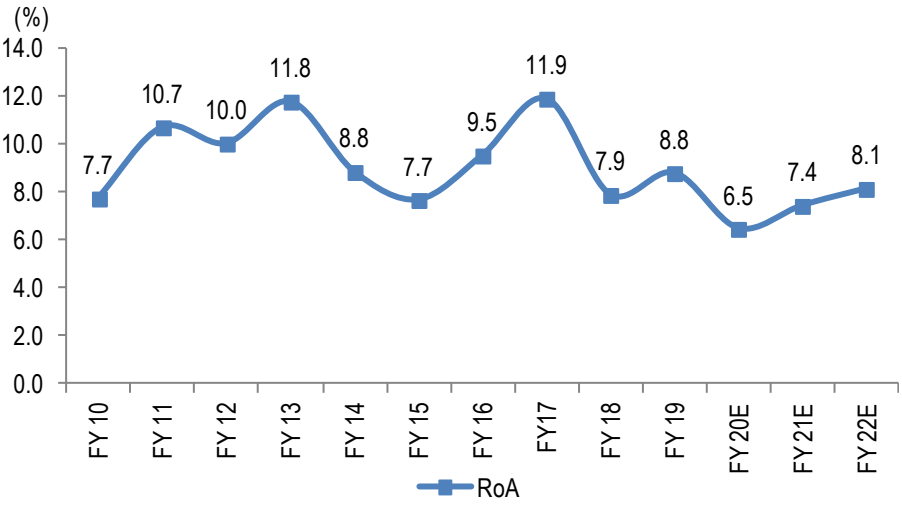

*Source: Company, Nirmal Bang Institutional Equities Research*

**Exhibit 27: Cash conversion cycle**



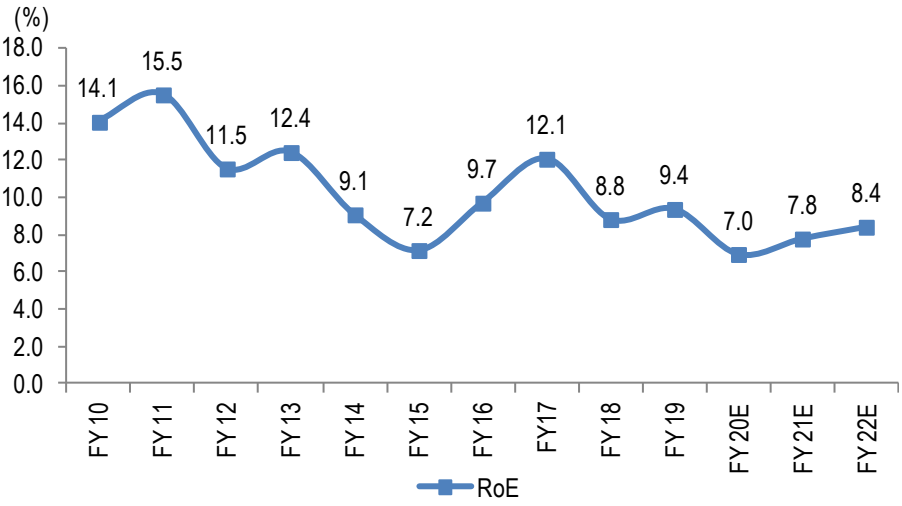

*Source: Company, Nirmal Bang Institutional Equities Research*

**Exhibit 28: Return on Assets**



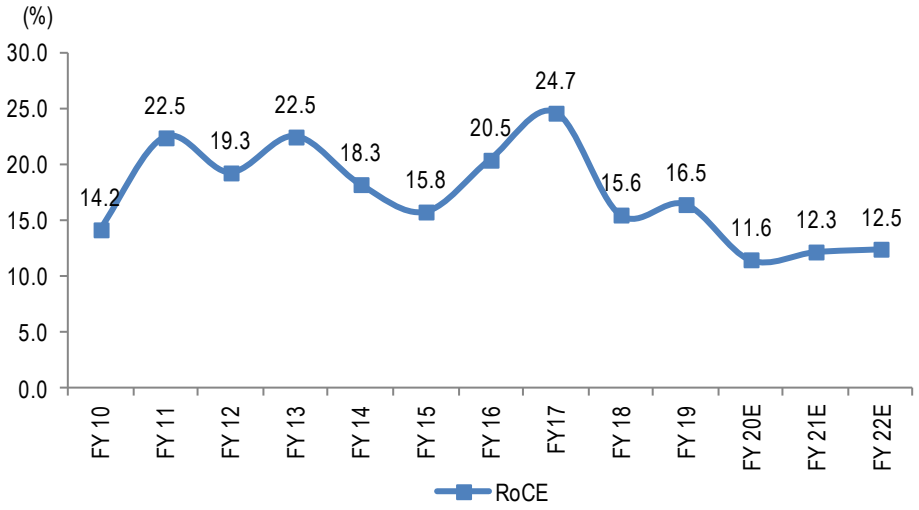

*Source: Company, Nirmal Bang Institutional Equities Research*

**Exhibit 29: Return on Equity**




*Source: Company, Nirmal Bang Institutional Equities Research*

**Exhibit 30: Return on Capital Employed**




*Source: Company, Nirmal Bang Institutional Equities Research*

## Glenmark Pharmaceuticals - Overview

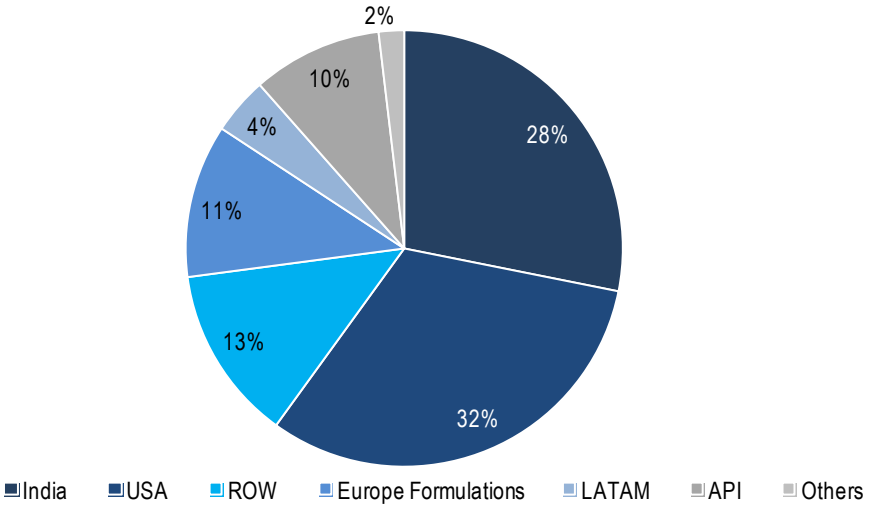
Glenmark Pharmaceuticals Ltd has a significant presence in the branded generics markets across emerging economies, including India. The company entered into the dermatology market through the launch of its Candid Cream. Glenmark's ground-breaking drug discovery effort is primarily focused in the areas of inflammation [asthma/COPD, rheumatoid arthritis etc.], metabolic disorders [diabetes, obesity, etc.] and pain [neuropathic pain and inflammatory pain]. The formulations business focuses on therapeutic areas such as dermatology, anti-infective, respiratory, cardiac, diabetes, gynaecology, CNS and oncology. India is the second largest market in terms of revenue. Glenmark was an early entrant into the US generics market and has established itself as a leading generics player. The company is now the 14th largest generics manufacturer by prescription and its products are used to fill about 83mn scrips each year in the US. The US business is the largest revenue contributor by geography. Glenmark has a strong presence across Europe with the company being one of the fastest-growing mid-size/large players. This has been achieved through a combination of portfolio expansion and geographical spread. The business has leveraged not just its in-house pipeline but has also added a significant component of in-licensing partnerships to develop a robust portfolio, delivering strong growth over the last decade. ROW business includes markets in CIS and other Asian markets, contributing 13% to the revenue. The company expects to consolidate its position in key markets in the Middle East and African regions. An important growth lever will be the in-licensing of complex generics that provide first-to-file opportunities. As part of the company's attempts to boost growth in the Latin America region, Glenmark's Brazilian subsidiary entered into an exclusive partnership in June 2019 with Novartis to promote and distribute three of the latter's respiratory brands in that market.

**Exhibit 31: Shareholding pattern**

| Particulars | No. of shares (mn) | % held |
|---|---|---|
| **Promoter & promoter group** | **131.5** | **46.59** |
| **Mutual funds** | **11.5** | **4.07** |
| Franklin Templeton | 9.1 | 3.24 |
| **Foreign portfolio investors** | **85.1** | **30.16** |
| HSBC Pooled Investment Fund | 9.3 | 3.29 |
| Franklin Templeton Investment Funds | 5.3 | 1.87 |
| **Financial institutions/banks** | **8.4** | **2.97** |
| LIC | 4.9 | 1.75 |
| **Others** | **45.7** | **16.21** |

*Source: BSE, Nirmal Bang Institutional Equities Research*

**Exhibit 32: Revenue break-up**




*Source: Company, Nirmal Bang Institutional Equities Research*

## Financials

### Exhibit 33: Income statement

| Y/E March (Rsmn) | FY18 | FY19 | FY20E | FY21E | FY22E |
|---|---|---|---|---|---|
| **Net sales** | **91,031** | **98,655** | **104,062** | **111,150** | **118,725** |
| *% growth* | *(0.9)* | *8.4* | *5.5* | *6.8* | *6.8* |
| Raw material costs | 30,386 | 33,623 | 35,874 | 38,194 | 40,662 |
| Staff costs | 18,718 | 20,561 | 23,028 | 25,561 | 28,373 |
| R&D Expenses | 11,220 | 12,980 | 13,008 | 12,227 | 11,873 |
| Other expenditure | 14,553 | 15,633 | 16,318 | 17,207 | 18,145 |
| Total expenditure | 74,877 | 82,797 | 88,228 | 93,189 | 99,053 |
| **EBITDA** | **16,154** | **15,858** | **15,834** | **17,961** | **19,672** |
| *% growth* | *(20.7)* | *(1.8)* | *(0.1)* | *13.4* | *9.5* |
| *EBITDA margin (%)* | *17.7* | *16.1* | *15.2* | *16.2* | *16.6* |
| Other income | 914 | 2,081 | 2,000 | 2,200 | 2,420 |
| Interest costs | 2,856 | 3,346 | 3,700 | 3,381 | 3,097 |
| **Gross profit** | **60,645** | **65,031** | **68,188** | **72,956** | **78,063** |
| *% growth* | *(7.7)* | *7.2* | *4.9* | *7.0* | *7.0* |
| Depreciation | 3,019 | 3,259 | 3,937 | 4,590 | 4,915 |
| **Profit before tax & Exceptional Items** | **11,193** | **11,334** | **10,197** | **12,190** | **14,080** |
| Exceptional Items | 0 | 1,672 | 0 | 0 | 0 |
| **Profit before tax** | 11,193 | 13,006 | 10,197 | 12,190 | 14,080 |
| *% growth* | *-28.8* | *1.3* | *-10.0* | *19.5* | *15.5* |
| Tax | 3,155 | 3,756 | 2,957 | 3,535 | 4,083 |
| *Effective tax rate (%)* | *28* | *33* | *29* | *29* | *29* |
| **PAT before Minority Interest** | **8,039** | **9,250** | **7,240** | **8,655** | **9,997** |
| Share of MI and Associates | 0 | 0 | 0 | 0 | 0 |
| **PAT after Minority Interest** | **8,039** | **9,250** | **7,240** | **8,655** | **9,997** |
| *% growth* | *(27.5)* | *15.1* | *(21.7)* | *19.5* | *15.5* |
| EPS (Rs) | 28.5 | 32.8 | 25.7 | 30.7 | 35.5 |
| % growth | *(27.5)* | *15.1* | *(21.7)* | *19.5* | *15.5* |

*Source: Company, Nirmal Bang Institutional Equities Research*

### Exhibit 35: Balance sheet

| Y/E March (Rsmn) | FY18 | FY19 | FY20E | FY21E | FY22E |
|---|---|---|---|---|---|
| Equity | 282 | 282 | 282 | 282 | 282 |
| Reserves | 51,353 | 55,770 | 62,331 | 70,307 | 79,625 |
| Net worth | 51,635 | 56,052 | 62,613 | 70,589 | 79,907 |
| Minority Interest | (4) | (4) | (4) | (4) | (4) |
| Net deferred tax liabilities | 284 | 458 | 458 | 458 | 458 |
| Total Loans | 44,368 | 38,768 | 38,952 | 35,592 | 32,603 |
| Other Financial Liabilities | 5,684 | 9,898 | 9,898 | 9,898 | 9,898 |
| Other Long Term Liabilities | 0 | 6 | 6 | 6 | 6 |
| **Liabilities** | **101,967** | **105,177** | **111,923** | **116,539** | **122,868** |
| Net Block | 18,958 | 20,978 | 28,308 | 34,979 | 37,831 |
| CWIP | 9,933 | 12,344 | 9,125 | 5,907 | 5,907 |
| Intangible Assets and Goodwill | 12,623 | 17,370 | 17,321 | 17,279 | 17,512 |
| Other Non Current Assets | 14,406 | 14,931 | 14,429 | 14,429 | 14,429 |
| Non-Current Investments | 147 | 297 | 297 | 297 | 297 |
| Inventories | 20,306 | 22,521 | 24,028 | 25,582 | 27,235 |
| Debtors | 23,318 | 21,946 | 23,149 | 24,726 | 26,411 |
| Cash | 12,347 | 9,378 | 11,579 | 11,501 | 13,373 |
| Other current assets | 13,916 | 13,124 | 13,124 | 13,124 | 13,124 |
| Total current assets | 69,887 | 66,968 | 71,879 | 74,933 | 80,143 |
| Creditors | 18,698 | 22,208 | 23,694 | 25,226 | 26,856 |
| Other current liabilities | 5,289 | 5,503 | 5,743 | 6,058 | 6,395 |
| Total current liabilities | 23,986 | 27,710 | 29,437 | 31,284 | 33,251 |
| Net current assets | 45,901 | 39,258 | 42,442 | 43,648 | 46,892 |
| **Total assets** | **101,967** | **105,177** | **111,923** | **116,539** | **122,868** |

*Source: Company, Nirmal Bang Institutional Equities Research*

### Exhibit 34: Cash flow

| Y/E March (Rsmn) | FY18 | FY19 | FY20E | FY21E | FY22E |
|---|---|---|---|---|---|
| EBIT | 14,049 | 16,352 | 13,897 | 15,571 | 17,178 |
| (Inc.)/dec. in working capital | 133 | 3,673 | (984) | (1,284) | (1,371) |
| **Cash flow from operations** | **14,182** | **20,026** | **12,914** | **14,288** | **15,806** |
| Other income | (914) | (2,081) | (2,000) | (2,200) | (2,420) |
| Other Expenses | 28 | 1,845 | 0 | 0 | 0 |
| Depreciation | 3,019 | 3,259 | 3,937 | 4,590 | 4,915 |
| Tax paid (-) | (3,155) | (3,756) | (2,957) | (3,535) | (4,083) |
| **Net cash from operations** | **13,160** | **19,292** | **11,894** | **13,143** | **14,218** |
| Capital expenditure (-) | (9,901) | (12,437) | (8,000) | (8,000) | (8,000) |
| **Net cash after CapEx** | **3,259** | **6,855** | **3,894** | **5,143** | **6,218** |
| **Other Investing activities** | **622** | **1,406** | **2,502** | **2,200** | **2,420** |
| **Cash from Financial Activities** | **(2,098)** | **(11,231)** | **(4,195)** | **(7,420)** | **(6,765)** |
| Opening cash | 10,564 | 12,347 | 9,378 | 11,579 | 11,501 |
| Closing cash | 12,347 | 9,378 | 11,579 | 11,501 | 13,373 |
| Change in cash | 1,783 | (2,969) | 2,201 | (78) | 1,873 |

*Source: Company, Nirmal Bang Institutional Equities Research*

### Exhibit 36: Key ratios

| Y/E March | FY18 | FY19 | FY20E | FY21E | FY22E |
|---|---|---|---|---|---|
| **Profitability & return ratios** | | | | | |
| EBITDA margin (%) | 17.7 | 16.1 | 15.2 | 16.2 | 16.6 |
| EBIT margin (%) | 15.4 | 14.9 | 13.4 | 14.0 | 14.5 |
| Net profit margin (%) | 8.8 | 9.4 | 7.0 | 7.8 | 8.4 |
| RoE (%) | 15.6 | 16.5 | 11.6 | 12.3 | 12.5 |
| RoCE (%) | 18.0 | 19.0 | 16.8 | 18.3 | 19.2 |
| **Working capital & liquidity ratios** | | | | | |
| Receivables (days) | 95 | 84 | 79 | 79 | 79 |
| Inventory (days) | 250 | 232 | 237 | 237 | 237 |
| Payables (days) | 227 | 222 | 234 | 234 | 234 |
| Current ratio (x) | 2.9 | 2.4 | 2.4 | 2.4 | 2.4 |
| Quick ratio (x) | 2.1 | 1.6 | 1.6 | 1.6 | 1.6 |
| **Valuation ratios** | | | | | |
| EV/sales (x) | 2.0 | 2.1 | 1.0 | 0.9 | 0.8 |
| EV/EBITDA (x) | 11.2 | 13.3 | 6.8 | 5.8 | 5.0 |
| P/E (x) | 18.5 | 19.7 | 11.0 | 9.2 | 8.0 |
| P/BV (x) | 2.9 | 3.2 | 1.3 | 1.1 | 1.0 |

*Source: Company, Nirmal Bang Institutional Equities Research*

## DISCLOSURES

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## Disclaimer

**Stock Ratings Absolute Returns**

BUY > 15%

ACCUMULATE -5% to15%

SELL < -5%

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