

Natco Pharma

13 August 2019

Reuters: NATP.NS; Bloomberg: NTCPH IN

India and rest of the world should help ramp up performance

Natco Pharma's (NPL) revenue in 1QFY20 at Rs4,923mn is 4.5% above our estimate and 13.8% below consensus estimate. Net profit at Rs1,428mn increased 18.6% QoQ but declined 21.1% YoY and is above our estimate by 13.7% and below consensus estimate by 18.5%.

QoQ revenue growth (8.0%) was aided by higher profit share contribution from Copaxone, which is also reflected in a 70bps improvement in gross margins. Going forward, in the coming quarters new launches in India and Brazil will shape earnings growth. Recently in India, NPL launched first time generics - apixaban and rivaroxaban, which are globally mega blockbuster molecules. Prior to these, NPL had launched Valsac (first generic of Novartis Entresto). It should also launch Ticagrelor (gBrilinta) shortly as the court has vacated the interim injunction. These launches together position NPL strongly in cardiac segment (hospital setting). Each of these launched molecule represent best in class treatment options and an early mover advantage should allow NPL to ramp up to leadership position and scale up the market targeted by these molecules.. We estimate these opportunities can translate to Rs2000mn to Rs4000mn in sales for NPL over the next 3 years. In Brazil too, NPL is anticipating new approvals in the coming months which should allow it to double current run rate from Rs300mn per quarter.

We have retained Buy rating on the stock with a target price (TP) of Rs654, up 19% from the CMP.

Outlook and valuation: NPL has given guidance of high single-digit growth in net profit for FY20, which is expected to be largely driven by rest of the world markets (Canada and Brazil) and India. These markets put together should post high-teen growth. As regards limited competition portfolio in the US, the company does not assume incremental competition in Copaxone generic, at least until the end of CY20. Early entry of Copaxone generic may pose downside risk to our earnings estimate. The company expects to ramp up sales in India and rest of the world markets with an objective to replace sales erosion in its limited competition portfolio in the US. NPL has also initiated efforts to monetize its portfolio in Emerging Markets (EM) like China where new regulations have lowered the entry barriers. Successful entry in China can be highly meaningful as new product launches can potentially be as lucrative as the US market. In Canada, the focus is to launch the oncology product portfolio. In addition, the company is investing in the agrochemicals space and has identified a basket of niche difficult-to-make products (limited competition) that would give it a competitive advantage.

BUY

Sector: Pharmaceuticals

CMP: Rs552

Target Price: Rs654

Upside: 19%

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Key Data

Current Shares O/S (mn)	181.8
Mkt Cap (Rsbn/US\$bn)	100.2/1.4
52 Wk H / L (Rs)	849/480
Daily Vol. (3M NSE Avg.)	246,600

Price Performance (%)

	1 M	6 M	1 Yr
Natco Pharma	4.5	(13.3)	(28.0)
Nifty Index	(3.8)	2.6	(2.8)

Source: Bloomberg

Y/E March (Rsmn)	1QFY19	4QFY19	1QFY20	YoY (%)	QoQ (%)	FY18	FY19	YoY (%)
Revenues	5,386	4,557	4,923	(8.6)	8.0	22,020	20,945	(4.9)
Raw material expenses	873	670	760	(12.9)	13.4	4,283	3,542	(17.3)
%age of revenues	16.2	14.7	15.4	(77) bps	74 bps	19.5	16.9	(254) bps
Staff costs	887	813	932	5.1	14.6	3,256	3,559	9.3
%age of revenues	16.5	17.8	18.9	246 bps	109 bps	14.8	17.0	221 bps
Other expenses	1,450	1,591	1,318	(9.1)	(17.2)	5,197	5,896	13.5
%age of revenues	26.9	34.9	26.8	(15) bps	(814) bps	23.6	28.1	455 bps
EBITDA	2,176	1,483	1,913	(12.1)	29.0	9,284	7,948	(14.4)
EBITDA margin	40.4	32.5	38.9	(154) bps	632 bps	42.2	37.9	(421) bps
Other income	359	310	210	(41.5)	(32.3)	404	1,302	222.3
Interest	28	52	65	132.1	25.0	154	193	25.3
Depreciation	184	217	220	19.6	1.4	662	810	22.4
Exceptional item	0.0	0	0	-	-	0	0	
PBT	2,323	1,524	1,838	(20.9)	20.6	8,872	8,247	(7.0)
Tax	512	320	410	(19.9)	28.1	1,920	1,823	(5.1)
Tax rate (%)	22.0	21.0	22.3	27 bps	131 bps	21.6	22.1	46 bps
PAT	1,811	1,204	1,428	(21.1)	18.6	6,952	6,424	(7.6)
PAT Margin	33.6	26.4	29.0	(462) bps	259 bps	31.6	30.7	(90) bps

Source: Company, Nirmal Bang Institutional Equities Research

Earnings conference-call takeaways

Domestic business: There is a decline in Hep C portfolio on a YoY basis. On a QoQ basis, Hep C sales have declined from Rs420mn to Rs310mn. The Domestic Oncology business at Rs800mn is reflecting a decline of 30% QoQ, but the business is fundamentally strong and should continue to grow on a YoY basis. The Cardio and Diabetes portfolio (Rs300mn) grew significantly over the last quarter, driven by channel stocking done for recent new launches of Apixaban and Rivaroxaban (both launched in June). Management has guided for fast ramp-up in these products as the company is the first to the market.

Revlimid: Management has guided that all queries raised by the USFDA have been resolved and it is expecting the approval in the next few months.

Margin: Gross margin in the quarter was high, driven by higher profit share from gCopaxone and improving product mix in the domestic market.

Copaxone: Profit share in the current quarter reflects full contribution from a ramp-up in market share in the US.

Agrochem facility: Agrochem facility will be ready to commission by the end of the calendar year.

Brilinta: NPL has received a favourable court verdict on Brilinta and it should be able to launch the drug in domestic market. Currently, the market size of Brilinta is around Rs1,700mn.

Brazil: Expect the streak of new launches to continue in the current fiscal year.

CapEx: Management has guided for the capex of Rs3750mn to Rs4000mn during the year.

ANDA filing: Management has guided for 5-7 filings for the year.

Exhibit 1: Actual performance versus our/Bloomberg consensus estimates

(Rsmn)	Actual	NBIE estimate	Var. (%)	Consensus estimate	Var. (%)
Sales	4,923	4,710	4.5	5,713	(13.8)
EBITDA	1,913	1,572	21.7	2,216	(13.7)
EBITDA margin (%)	38.9	33.4	548 bps	38.8	7 bps
Reported PAT	1,428	1,256	13.7	1,752	(18.5)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 2: Key financials

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Net sales	20,202	22,020	20,945	21,916	21,403
EBITDA	6,834	9,284	7,948	8,435	7,224
Net profit	4,860	6,962	6,444	6,882	6,034
EPS (Rs)	27.9	38.8	34.9	37.3	32.7
EPS growth (%)	206.4	39.2	(10.0)	6.8	(12.3)
EBITDA margin (%)	33.8	42.2	37.9	38.5	33.8
P/E (x)	31.0	20.0	15.0	14.1	16.1
P/BV (x)	9.1	4.4	2.7	2.3	2.0
EV/EBITDA (x)	22.3	14.6	12.0	10.7	11.8
RoCE (%)	42.6	31.4	23.3	21.8	16.8
RoE (%)	29.5	22.7	18.5	16.6	12.8

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Change in our estimates

(Rsmn)	New estimates		Old estimates		Change (%)	
	FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Net sales	21,916	21,403	21,916	21,403	0.0	0.0
EBITDA	8,435	7,224	8,435	7,224	0.0	0.0
Margin (%)	38.5	33.8	38.5	33.8	0 bps	0 bps
PAT	6,882	6,034	6,882	6,034	0.0	0.0
Margin (%)	31.4	28.2	31.4	28.2	0 bps	0 bps
EPS	37.3	32.7	37.3	32.7	0.0	0.0

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Quarterly revenue break-up

Revenues (Rsmn)	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
Domestic formulations	2,180	1,821	2,134	1,658	1,585	1,910	1,939	1,640	1,859	1,640
<i>Oncology</i>	840	730	973	848	828	929	970	930	1,141	800
<i>Hepatitis C</i>	1,220	845	948	685	624	741	790	500	429	310
<i>Other</i>	120	246	213	125	133	242	179	210	289	530
Export formulations	2,890	1,338	1,268	2,890	4,920	2,140	2,478	2,570	1,662	2,130
Total formulations	5,070	3,159	3,402	4,548	6,505	4,052	4,417	4,210	3,521	3,770
API	560	863	584	811	1,337	670	668	990	702	720
Revenue mix (%)										
Domestic formulations	38.7	45.3	53.5	30.9	20.2	40.5	35.7	29.5	40.7	33.3
<i>Oncology</i>	14.9	18.1	24.4	15.8	10.6	19.7	17.8	16.7	25.0	16.3
<i>Hepatitis C</i>	21.7	21.1	23.8	12.8	8.0	15.7	14.5	9.0	9.4	6.3
<i>Other</i>	2.1	6.1	5.3	2.3	1.7	5.1	3.3	3.8	6.3	10.8
Export formulations	51.4	33.2	31.8	54.0	62.7	45.3	45.6	46.2	36.4	43.3
Total formulations	90.1	78.6	85.3	84.9	83.0	85.8	81.3	75.6	77.2	76.6
API	9.9	21.4	14.7	15.1	17.0	14.2	12.3	17.8	15.4	14.6
QoQ growth (%)										
Domestic formulations	(0.4)	(16.3)	16.9	(22.3)	(4.4)	20.6	1.4	(15.4)	13.4	(11.8)
<i>Oncology</i>	(4.9)	(13.1)	33.3	(12.8)	(2.4)	12.2	4.4	(4.1)	22.7	(29.9)
<i>Hepatitis C</i>	8.8	(30.4)	11.7	(27.7)	(8.9)	18.8	6.6	(36.7)	(14.2)	(27.7)
<i>Other</i>	(34.8)	105.0	(13.4)	(41.3)	6.4	82.0	(26.0)	17.3	37.6	83.4
Export formulations	(19.3)	(53.7)	(5.2)	128.7	69.7	(56.5)	15.8	3.7	(35.3)	28.2
Total formulations	(12.1)	(37.6)	7.6	34.0	42.7	(37.7)	9.0	(4.7)	(16.4)	7.1
API	9.9	54.9	(32.3)	38.7	65.1	(49.9)	(0.3)	48.2	(29.1)	2.6
YoY growth (%)										
Domestic formulations	-	-20.0	-1.3	-24.2	-27.3	4.8	-9.1	-1.1	17.3	-14.2
<i>Oncology</i>	-	0.0	26.2	-4.0	-1.4	27.3	-0.3	9.7	37.8	-13.9
<i>Hepatitis C</i>	-	-36.6	-15.4	-38.9	-48.9	-12.7	-16.7	-27.0	-31.3	-58.2
<i>Other</i>	-	17.1	-21.1	-32.1	10.8	-1.6	-16.0	68.0	117.3	119.0
Export formulations	-	162.4	-8.7	-19.0	70.2	59.9	95.4	-11.4	-66.2	-0.5
Total formulations	-	13.4	-4.2	-21.0	28.3	28.1	29.8	-7.6	-45.9	-7.0
API	-	115.8	22.7	59.8	140.0	-22.4	14.4	22.2	-47.5	7.5

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: Quarterly snapshot

Margins (%)	4QFY17	1QFY18	2QFY18	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20
Gross margin	79.7	71.6	73.5	88.3	84.0	83.8	82.5	81.1	85.3	84.6
EBITDA margin	41.7	30.7	28.6	51.0	49.9	40.4	40.6	37.4	32.5	38.9
PAT margin	30.5	21.0	19.8	38.7	39.0	33.6	33.4	28.6	26.4	29.0

Source: Company, Nirmal Bang Institutional Equities Research

Financial statements

Exhibit 6: Income statement

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Net sales	20,202	22,020	20,945	21,916	21,403
% growth	87.0	9.0	(4.9)	4.6	(2.3)
Raw material costs	5,991	4,283	3,542	3,577	3,935
Staff costs	2,432	3,256	3,559	3,986	4,464
Other expenditure	4,945	5,197	5,896	5,917	5,779
Total expenditure	13,368	12,736	12,997	13,480	14,178
EBITDA	6,834	9,284	7,948	8,435	7,224
% growth	157.3	35.9	(14.4)	6.1	(14.4)
EBITDA margin (%)	33.8	42.2	37.9	38.5	33.8
Other income	139	404	1,302	1,497	1,722
Interest costs	185	154	193	162	164
Gross profit	14,211	17,737	17,403	18,339	17,467
% growth	75.6	24.8	(1.9)	5.4	(4.8)
Depreciation	544	662	810	961	1,061
Profit before tax	6,244	8,872	8,247	8,809	7,720
% growth	206.5	42.1	(7.0)	6.8	(12.4)
Tax	1,395	1,920	1,823	1,947	1,707
Effective tax rate (%)	22.3	21.6	22.1	22.1	22.1
Net profit	4,860	6,962	6,444	6,882	6,034
% growth	209.3	43.3	(7.4)	6.8	(12.3)
EPS (Rs)	27.9	38.8	34.9	37.3	32.7
% growth	206.4	39.2	(10.0)	6.8	(12.3)

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 8: Balance sheet

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Equity	349	369	365	365	365
Reserves	16,144	30,353	34,525	41,145	46,917
Net worth	16,493	30,722	34,890	41,510	47,282
Net deferred tax liabilities	150	139	116	116	116
Total debt	2,216	1,732	3,863	1,946	1,970
Other non-current liabilities	268	370	738	738	738
Liabilities	19,127	32,963	39,607	44,310	50,106
Net block	8,272	10,127	12,185	13,691	14,629
Capital WIP	3,363	4,800	6,376	6,376	6,376
Intangible assets and goodwill	58	59	87	87	87
Other non-current assets	610	858	911	911	911
Inventories	3,489	4,384	5,290	2,083	2,292
Debtors	4,752	6,375	5,062	5,155	5,034
Cash	358	1,837	2,795	8,878	13,770
Other current assets	2,274	8,711	10,325	10,311	10,309
Total current assets	10,873	21,307	23,472	26,427	31,405
Creditors	2,627	2,691	2,170	1,568	1,726
Other current liabilities	1,422	1,497	1,254	1,613	1,577
Total current liabilities	4,049	4,188	3,424	3,182	3,303
Net current assets	6,824	17,119	20,048	23,246	28,102
Total assets	19,127	32,963	39,607	44,310	50,106

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 7: Cash flow

Y/E March (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
EBIT	6,429	9,026	8,440	8,972	7,885
(Inc.)/dec. in working capital	(2,495)	(8,816)	(1,971)	2,886	35
Cash flow from operations	3,934	210	6,469	11,857	7,920
Other income	(139)	(404)	(1,302)	(1,497)	(1,722)
Depreciation	544	662	810	961	1,061
Other non-cash expenses	3	(11)	(23)	0	0
Tax paid	(1,395)	(1,920)	(1,823)	(1,947)	(1,707)
Net cash from operations	2,947	(1,463)	4,131	9,374	5,552
Capital expenditure	(3,018)	(3,955)	(4,472)	(2,467)	(2,000)
Net cash after capex	(71)	(5,418)	(341)	6,907	3,552
Other investment activities	157	156	1,249	1,497	1,722
Cash from financial activities	(180)	6,741	50	(2,321)	(383)
Opening cash balance	452	358	1,837	2,795	8,878
Closing cash balance	358	1,837	2,795	8,878	13,770
Change in cash balance	(94)	1,479	958	6,083	4,891

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 9: Key ratios

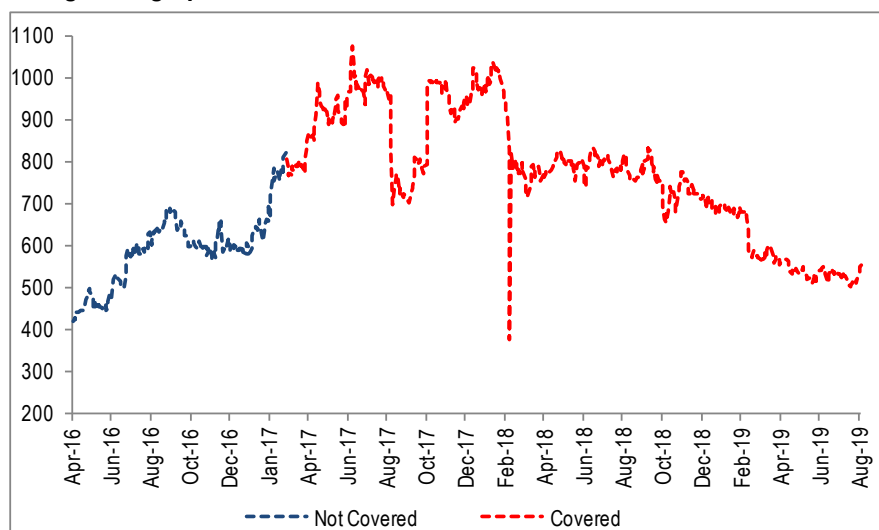
Y/E March	FY17	FY18	FY19	FY20E	FY21E
Profitability & return ratios					
EBITDA margin (%)	24.6	33.8	42.2	37.9	38.5
EBIT margin (%)	21.0	31.8	41.0	40.3	40.9
Net profit margin (%)	14.5	24.1	31.6	30.8	31.4
RoE (%)	12.1	29.5	22.7	18.5	16.6
RoCE (%)	22.0	42.6	31.4	23.3	21.8
Working capital & liquidity ratios					
Receivables (days)	88.4	85.9	105.7	88.2	85.9
Inventory (days)	481.9	212.6	373.6	545.1	212.6
Payables (days)	371.7	160.0	229.3	223.6	160.0
Current ratio (x)	2.1	2.7	5.1	6.9	8.3
Quick ratio (x)	1.2	1.8	4.0	5.3	7.7
Valuation ratios					
EV/sales (x)	13.0	7.5	6.1	4.8	4.3
EV/EBITDA (x)	53.0	22.3	14.6	12.6	11.2
P/E (x)	85.8	31.0	20.0	15.8	14.8
P/BV (x)	10.8	9.1	4.4	2.8	2.5

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price (Rs)	Target price (Rs)
28 February 2017	Sell	823	725
1 June 2017	Accumulate	933	940
8 August 2017	Accumulate	924	940
6 October 2017	Buy	953	1,102
7 February 2018	Buy	829	955
25 May 2018	Buy	790	915
10 August 2018	Buy	781	915
6 November 2018	Accumulate	752	813
14 February 2019	Buy	636	776
5 April 2019	Buy	556	779
28 May 2019	Buy	525	654
13 August 2019	Buy	552	654

Rating track graph



DISCLOSURES

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BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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