Stock Idea

Sector: Pharmaceuticals February 26, 2021

Gland Pharma Limited

A giant in the making

Sharekhan
by BNP PARIBAS

Powered by Sharekhan's 3R Research Philosophy

Gland Pharma Limited

A giant in the making

Pharmaceuticals	Sharekhan code: GLAND	Initiating Coverage

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral - Negative

Reco
Reco: **Buy**
CMP: **Rs. 2,412**
Price Target: **Rs. 3,040**

Company details

Market cap:	Rs. 39,432 cr
52-week high/low:	Rs. 2509 / 1701
NSE volume: (No of shares)	6.7 lakh
BSE code:	543245
NSE code:	GLAND
Free float: (No of shares)	6.8 cr

** Company listed on 20 Nov 2020*

Shareholding (%)

Promoters	58.4
FII	12.7
DII	10.8
Others	18.10

Summary

- We Initiate coverage on Gland Pharma Limited (Gland) with a Buy recommendation and a price target of Rs. 3,040.
- Gland is an established player in Injectables space and is well-placed to harness the growth opportunities in this space. It has a strong compliance record with nil observations from the USFDA across all its plants.
- Gland has a unique B2B business model, which enables it grow its market share while maintaining cost leadership.
- Strong domain expertise, robust growth prospects, sturdy & consistent earnings track record, and healthy return ratios make Gland an ideal long-term investment pick.

Gland Pharma Limited (Gland) is an established player in the injectables space, which is one of the fastest-growing drug delivery formats across markets. Injectables are being preferred over oral delivery formats due to certain benefits offered such as convenience of administration. Hence,Injectables find applications in treatment of new ailments/chronic diseases, thus pointing to possibilities of robust demand traction. Further, the sterile nature of injectables warrants adherence to relatively stringent compliance norms and higher investments, which act as entry barriers and could keep competitive pressures lower. Gland follows a unique B2B business model (~96% of FY2020 sales) across global markets, which comprises an IP-led model(69% of B2B revenue) and the technology transfer model (27% of B2B revenue). The B2B model helps the company achieve economies of scale at the product level, leading to cost leadership and enables market share gains. This coupled with a strong compliance track record,(reflected in zero observations from the USFDA for all plants) augurs well for Gland's growth. Consistent shortage of Injectables in the US offers substantial growth opportunities. Further, entry in the Chinese generic injectable markets is expected to be a key growth driver, as Gland plans to file 60 products in China going ahead (already filed 6 dossiers). Gland's strong capabilities (reflected in commercialization of various niche products) are well supported by a sturdy R&D muscle, which alludes to a robust product pipeline. Cumulatively, this points at the company's ability to consistently commercialise its product pipeline and gain market share. Geographically, the US forms a strong base for the company's growth while RoW markets are expected to grow at a sturdy pace. Further, Gland has a higher degree of vertical integration across its product categories, which would enhance operational efficiencies, leading to margin expansion. We expect sales and PAT to report a 23.7% and 25.7% CAGR over FY2020 to FY2023.

Our Call

Valuation Initiate Coverage with a Buy recommendation and PT of Rs.3040: Gland is in a sweet spot, well-placed to harness growth opportunities in the generic Injectables space. Being an established player in the space globally, it is slated to benefit from increasing preference for Injectables, while a high entry barrier would ensure lower competitive pressures and sustained growth momentum. Gland has a unique B2B business model, which enables it to gain market share while maintaining its cost leadership. Being largely a B2B player, it is exposed to frequent plant inspections by clients, which ensures consistent adherence to strict compliance norms. The fact that the company has nil observations from USFDA for its plants is testimony to the stringent compliance standards followed. The US market accounts for 67% of the revenue and a clean compliance track record is a key strength. This coupled with consistent shortage of Injectables paves the way for a strong growth going ahead. Moreover, strong capabilities, entry in new geographies like China, an extensive product portfolio backed by strong R&D and vertical integration for APIs, are key growth driver. Potential opportunities in the vaccine space, if accrued could complement growth. Gland's topline and PAT are expected to register a 23.7% and 25.7% CAGR over FY2020 to FY2023. At CMP, the stock trades at valuation of 31.9x/25.7x its FY2022E/FY2023E EPS. Strong domain expertise and growth prospects, sturdy and consistent earnings track record, healthy return ratios and cashflows make Gland an ideal long-term investment pick. We initiate coverage on the stock with a Buy recommendation and a price target (PT) of Rs. 3,040.

Key risks

- Any adverse change in the regulatory landscape and delay in procuring product approvals can impact growth prospects.
- Product concentration risk exists as top 5 products constitute around 45% of US sales.
- Adverse forex movement.

Valuation Rs cr

Particulars	FY2019	FY2020	FY2021E	FY2022E	FY2023E
Total Sales	2044.2	2633.2	3338.2	4102.2	4988.6
Operating Profits	792.1	1094.6	1388.2	1706.7	2106.0
OPM (%)	34.6	36.3	37.0	37.5	38.3
Reported PAT	471.8	772.8	997.3	1233.4	1535.4
EPS (Rs)	28.9	47.3	61.1	75.5	94.0
PER (x)	83.5	51.0	39.5	31.9	25.7
EV/Ebidta (x)	48.8	34.8	26.2	20.8	16.4
P/BV (x)	13.8	10.8	6.7	5.6	4.6
ROCE (%)	23.7	26.8	21.6	22.3	23.0
RONW (%)	16.5	21.2	17.0	17.5	18.0

Source: Company, Sharekhan Research

Executive Summary

3R Research Positioning Summary

- **Right Sector:** Competitive nature of Indian Pharma Companies, Strong manufacturing capabilities, shift in favor of complex / specialty molecules and Capacity expansion by select players to support growth.
- **Right Quality:** Presence in the lucrative Injectables space, Strong compliance track record with zero observations, unique B2B IP led business model.
- **Right Valuation:** Gland is available at a valuation of 31.9x / 25.7x its FY2022E/FY2023E EPS. Given the strong domain expertise, consistent earnings track record and healthy return ratios, the premium valuations would sustain.

Valuation and return potential

- Gland is trading premium valuations of 39.5x/31.9x/25.7x its FY 2021E/FY2022E/FY2023E EPS.
- We initiate Coverage on Gland with a Buy recommendation and a PT of Rs 3040 (upside of 26%).

Catalysts

Triggers

- Increasing share of Injectables in the overall industry coupled with high entry barriers.
- Unique B2B model enabling market share growth, whilst maintaining cost leadership.
- Extensive product portfolio backed by a strong R&D leading to consistent filling / commercializing of new products
- Vertical integration for all the key API's leading to better operation efficiencies.
- Entry in new geographies such as china & strengthening capability in complex injectables.

Key Risks:

- Adverse changes in regulatory landscape, delay in receiving product approvals

Earnings and Balance sheet highlights

- **Consistent earnings growth:** Revenues and PAT grew at a CAGR of 27.4% and 55%, over FY2018-20.
- **Key regions:** US and India are the key geographies accounting for 66.7% and 17.7% of the overall FY2020 sales.
- **Healthy balance sheet and cash flows:** Gland has a almost zero debt – equity position; Cash flow from operations stood at Rs. 754 crore as of FY2020, as against Rs 193 cr in FY2019.
- **Healthy return profile:** RoE and RoCE stood at 21.2% and 26.8%, respectively, in FY2020.

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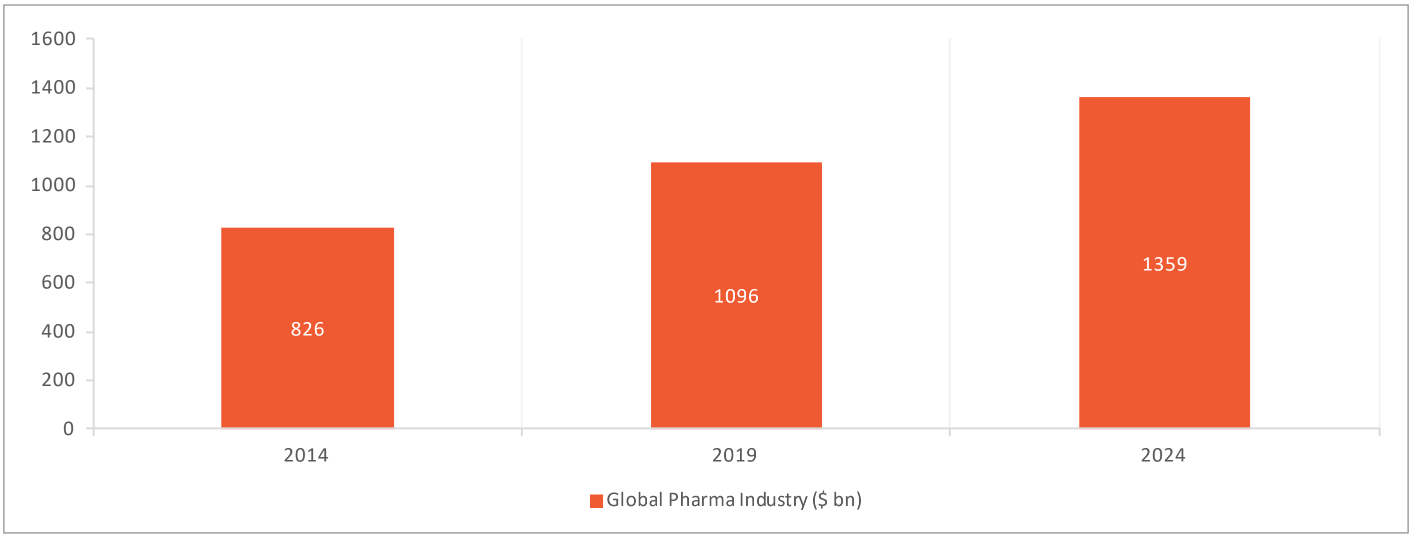
Investment Rationale

Why we like the space: Robust growth outlook

The global pharma industry is slated to report healthy growth over 2019-2024. In the pharma industry, injectables are one of the fastest growing drug delivery formats and the injectables pie in the overall industry increased to 39% as of 2019 as compared to 32% as of 2014. Outlook for the injectables segment is robust given the benefits offered over orals across therapies.

Global pharma market to register healthy growth over 2019-2024: The global formulations market reported a CAGR of ~5.8% from 2014 to reach $1,096 billion in 2019, as per IQVIA. The market is estimated to register a CAGR of 4.4% to reach $1,359 billion by 2024. Among global markets, North America is expected to contribute ~47% to the overall market by value in 2024 and register a CAGR of approximately 3.9% from 2019 to 2024. India and China are expected to contribute approximately 2% and 9%, respectively, of the market, by value, with India expected to grow at a faster rate of approximately 9.3% and China to register a CAGR of approximately 5.2% from 2019 to 2024.

Global pharmaceutical market size



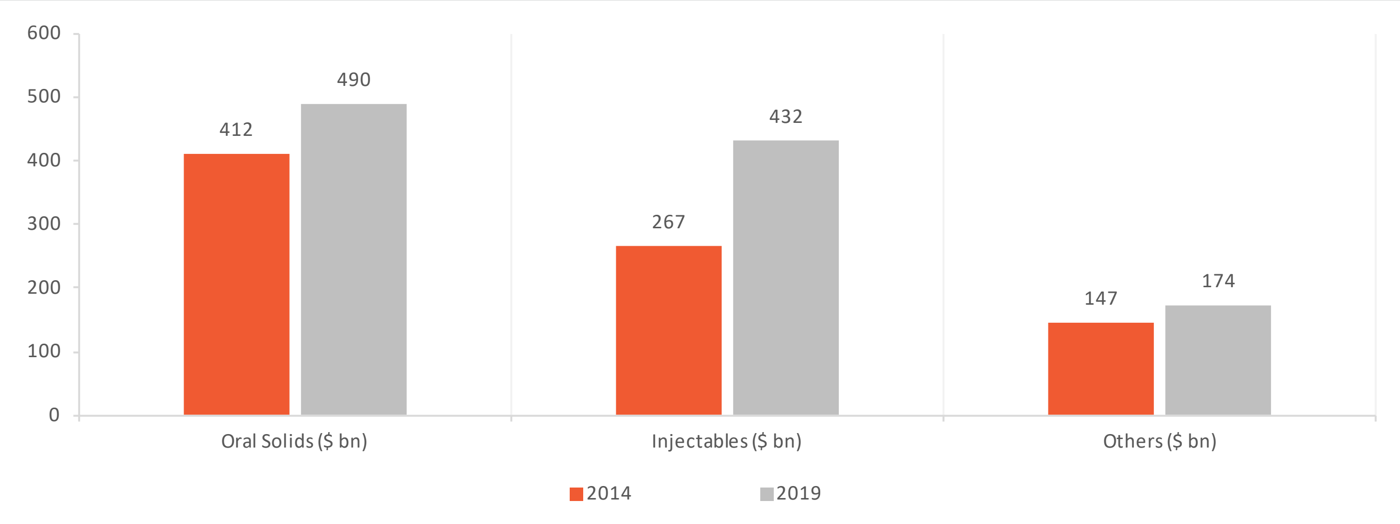
Source: DRHP; Sharekhan Research

Further, oral solids, which is the largest delivery format in the market by value, were estimated to be $490 billion in 2019, registering a CAGR of approximately 3.5% from 2014 to 2019. However, the market share by value of oral solids declined from 50% in 2014 to 45% in 2019. Injectables are the second-largest delivery format in the global pharmaceutical market. IQVIA estimated that the global injectables market reported a CAGR of ~10.1% from 2014 to reach $432 billion in 2019. Market share by value of injectables increased from 32% in 2014 to approximately 39% in 2019.

Global injectables markets gaining traction

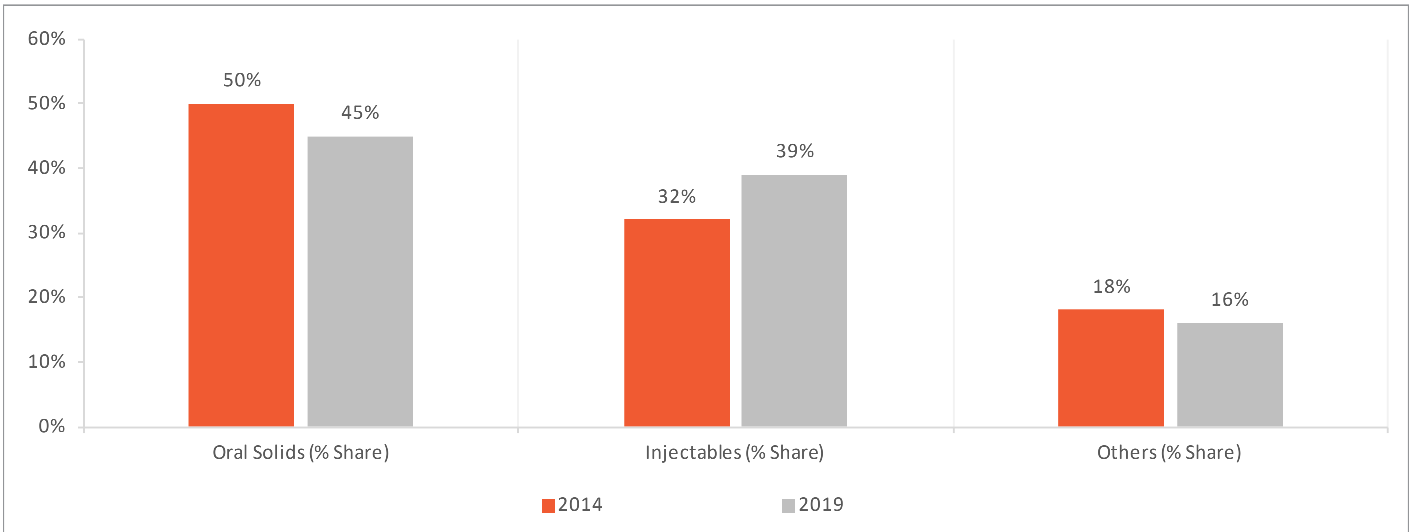
The global injectables markets is the second largest form of delivery systems, next only to oral solids. The share of injectables in the total has increased to 39% as of 2019 compared to 32% in 2014. Injectables have numerous advantages over other traditional dosage forms. Injectables in particular are useful to unconscious or comatose patients who are otherwise not capable of consuming medication. Moreover, development of self-injection devices such as pen injectors and auto injectors has made administering drugs convenient and easy for patients, right from their homes. Further, the increase in number of new drug formulations, which are not water soluble and/or have low effectiveness through the oral delivery route are usually given through the injectables route.

Trends in global sales of injectables compared to other dosage formats



Source: DRHP; Sharekhan Research

Market share of injectables versus other dosage formats

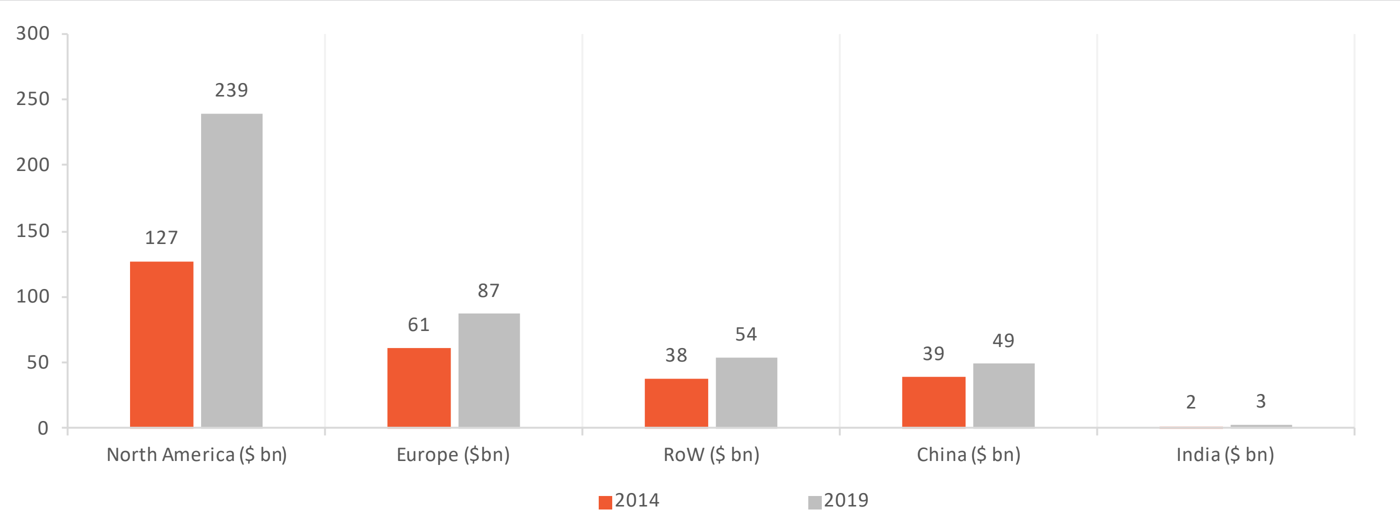


Source: DRHP; Sharekhan Research

Geographic segmentation of the injectables markets; North America commands a lion's share

The North American market is one of the leading markets globally for injectables. As per IQVIA, US accounted for the largest share by value of 55% in 2019 and was estimated to be worth of $239 billion, followed by Europe with a market share of 20% with an estimated value of $87 billion. China accounted for 11% of market share with an estimated market of $49 billion in 2019, while India had 1% market share with a $3 billion market. The remaining 13% was contributed by RoW, estimated at $54 billion. Japan, Russia, Korea, and Saudi Arabia are the key markets contributing to approximately 68% of overall ROW injectables market. India's injectables market witnessed growth primarily on account of rising prevalence of chronic diseases such as diabetes and growth in demand of insulin and certain therapeutic areas (i.e., nervous system, musculoskeletal system, gastro intestinal system, respiratory system, and systemic anti-infective), which constituted approximately 67% of the generic injectables market in India in 2019.

Geographic segmentation of global injectables market

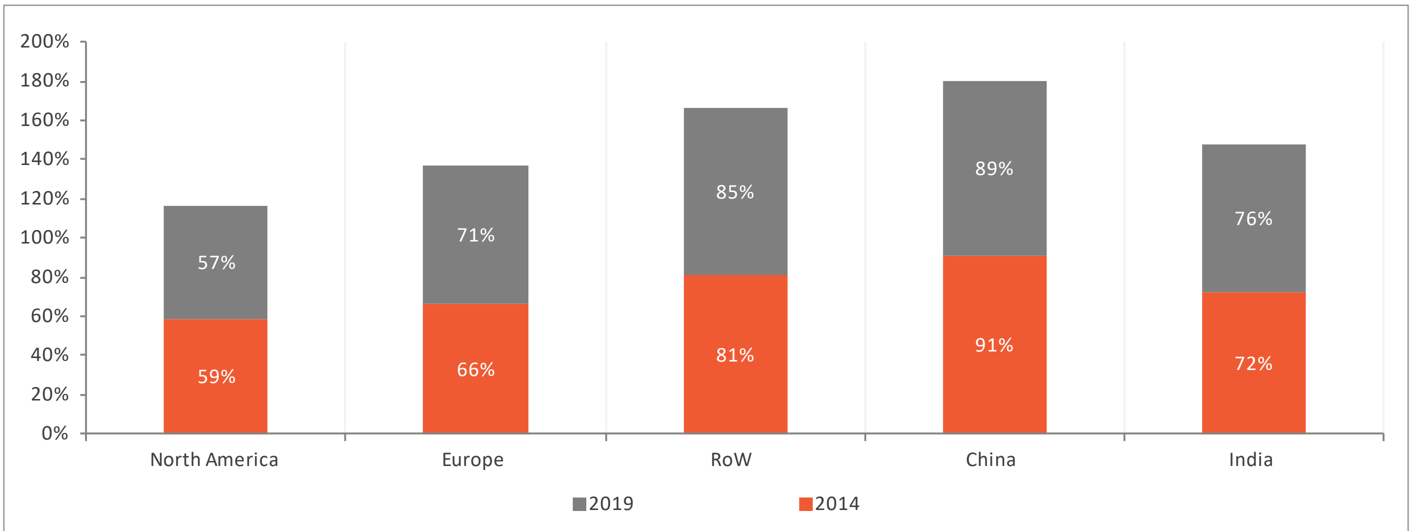


Source: DRHP; Sharekhan Research

Improving Geographic Market penetration of injectables

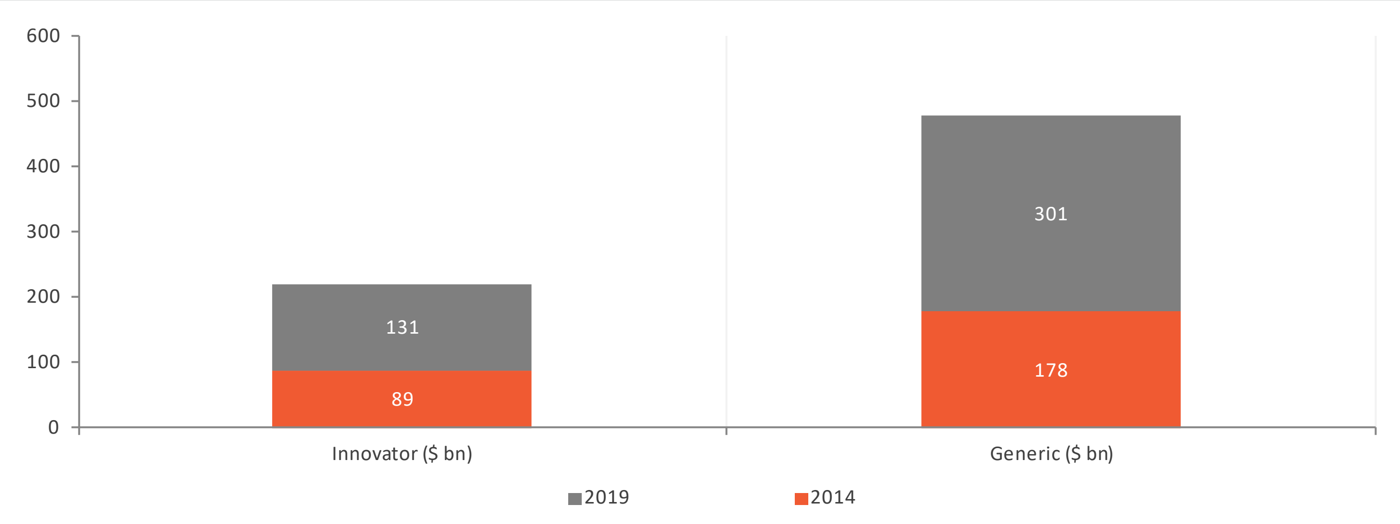
Amongst markets globally, China had the highest generic penetration by volume in the injectables form as of 2019, while North America had the lowest percentage. Generic penetration mostly increased across geographies during the past few years, except for North America and China, where the value of the market has, however, increased and grown by 12.5% and 3.0%, respectively. North America had the lowest generic penetration of approximately 57% across geographies. China and India had the highest generic injectables market share estimated at 89% and 76%, respectively. Europe had injectables generic contribution by volumes estimated at 71%.

Penetration of generics in injectables form (% volume share)



Source: DRHP; Sharekhan Research

Global Injectables Market Mix - Innovator and Generic Players



Source: DRHP; Sharekhan Research

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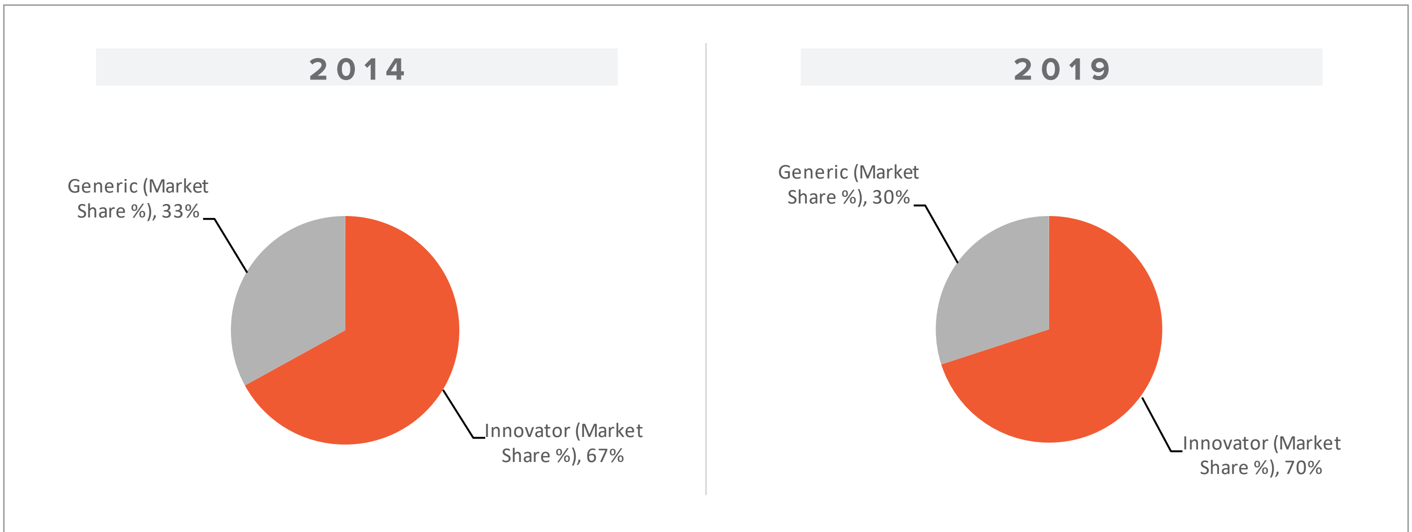
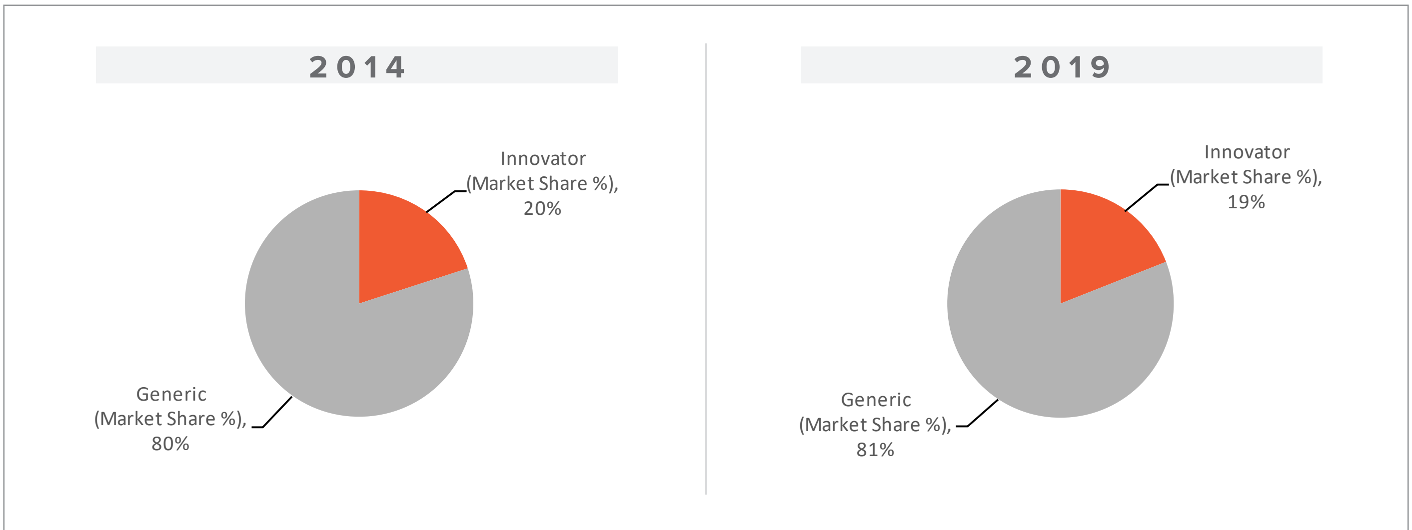


Source: DRHP; Sharekhan Research

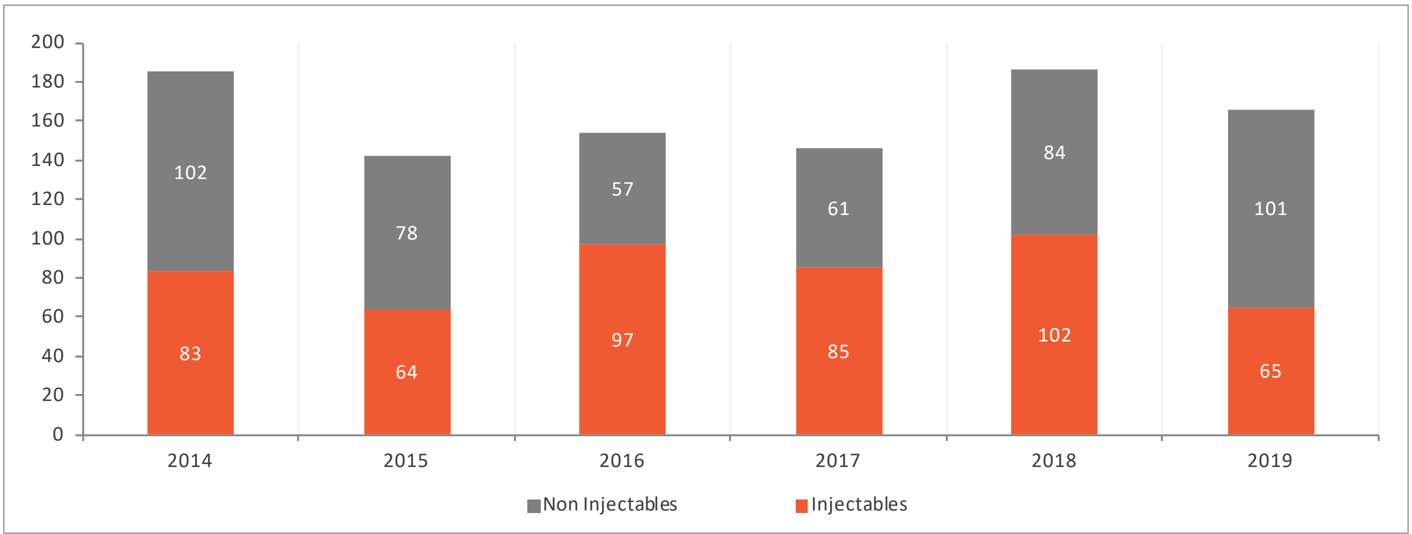
Segmental Volumes mix – Global Injectables Market



Source: DRHP; Sharekhan Research

Multiple factors to fuel growth in Injectables space: Injectables have been one of the fastest growing formats of drug delivery systems across as they offer certain advantages over oral systems. Rising prevalence of chronic diseases such as cardiac, diabetes, and cancer amongst others is better administered through injectables. Moreover, new market opportunities including new ailments - rheumatoid arthritis, multiple sclerosis, cancers, and autoimmune disorders are now being treated through injectables solutions. Further, over the years, injectables continue to form a major portion of drug shortages in the US (which is a major market globally) and USFDA reported an increase in the number of injectables shortages over 2014 to 2018. Approximately, 40% of the overall drug shortage in the US is in the injectables category.

Form-wise Drug Shortages in the US (Nos)



Source: DRHP; Sharekhan Research

Cumulatively, this points at a possibly better traction for injectables. As per IQVIA, the global injectables market was estimated to be $432 billion in 2019, registering a CAGR of approximately 10.1% over 2014-2019. Consequently, the market share by value of injectables grew from 32% in 2014 to approximately 39% in 2019. Companies such as Gland, which have been predominantly injectables focused players, are likely to be substantial beneficiaries of the situation.

Company Rationales

Why we like Gland: Injectables-focused player with a unique business model and strong compliance track record

Gland is an injectables-focused company with a unique B2B business model that enables market share growth, whilst enhancing operational efficiencies. A strong compliance track record with zero observation points towards robust capabilities. An Extensive Product portfolio and strong R&D muscle ensure consistent filling/ commercialising of new products, while vertical integration for the APIs enables better operational efficiencies. The high entry barrier for the injectables space ensures limited competitive pressures.

Extensive and vertically integrated manufacturing facilities with a consistent regulatory compliance track record: Gland has seven manufacturing facilities, including two sterile injectables facilities, one dedicated Penems facility, one oncology facility, and three API facilities. The manufacturing process across plants is designed to facilitate production flexibility and deliver high and consistent product quality. This allows the company to quickly adapt to changes in product specifications, market demand, and production requirements.

Manufacturing Facilities Details and Regulatory approvals

Location	Facility	Key Products	Key regulatory Approvals
Dundigal, Hyderabad	Sterile Injectables	Enoxaparin Sodium, Caspofungin, Levetiracetam, Daptomycin	USFDA (US), MHRA (UK), ANVISA (Brazil), TGA (Australia), BGV Hamburg (Germany)
Pashamylaram, Hyderabad	Sterile Injectables	Heparin Sodium, Vancomycin	USFDA (US), GUB Munich (Germany)
Pashamylaram, Hyderabad	Penems	-	USFDA (US)
Visakhapatnam	Oncology	Paclitaxel, Bortezomib	USFDA (US), AGES (Austria), TGA (Australia)

Source: DRHP; Sharekhan Research

In addition, diversification of product approvals across multiple manufacturing units for key products mitigates regulatory risk with respect to any particular unit and provides increased certainty of supply. All manufacturing facilities have established a consistent record of regulatory compliance with the USFDA, highlighting focus on quality assurance and quality control. Gland has had no warning letters from the USFDA since the inception of each facility. Certain facilities are also compliant with MHRA (UK), ANVISA (Brazil), AGES (Austria), TGA (Australia), and BGV Hamburg (Germany). Gland has three API plants that manufacture critical APIs as well. Of the three facilities, one is an R&D pilot plant and the other two have an annual capacity of 3,000 kg and 8,000 kg, respectively. The company's 24 ANDAs covering key products are supported by in-house APIs. The key APIs that are manufactured by the company include - Atracurium Besylate, Cisatracurium Besylate, Dexrazoxane, Enoxaparin Sodium, Heparin Sodium and Rocuronium Bromide. Vertical integration allows Gland to achieve greater control over manufacturing processes to meet required standards, increase operating efficiencies, accelerate product development, strengthen product quality control, and improve supply chain efficiencies. Therefore, a strong vertical integration across products with fully compliant facilities point at strong manufacturing capabilities with a focus on quality.

Extensive & Vertically Integrated Manufacturing Capabilities

Source: Company

Unique B2B-led model across markets complemented by a B2C model in India bodes well from growth perspective

Gland primarily follows a unique B2B business model in global markets. The B2B model covers IP-led, technology transfers and contract manufacturing models, complemented by B2C model in the home market of India. Gland has a successful track record of operating a B2B business model with leading global pharma companies.

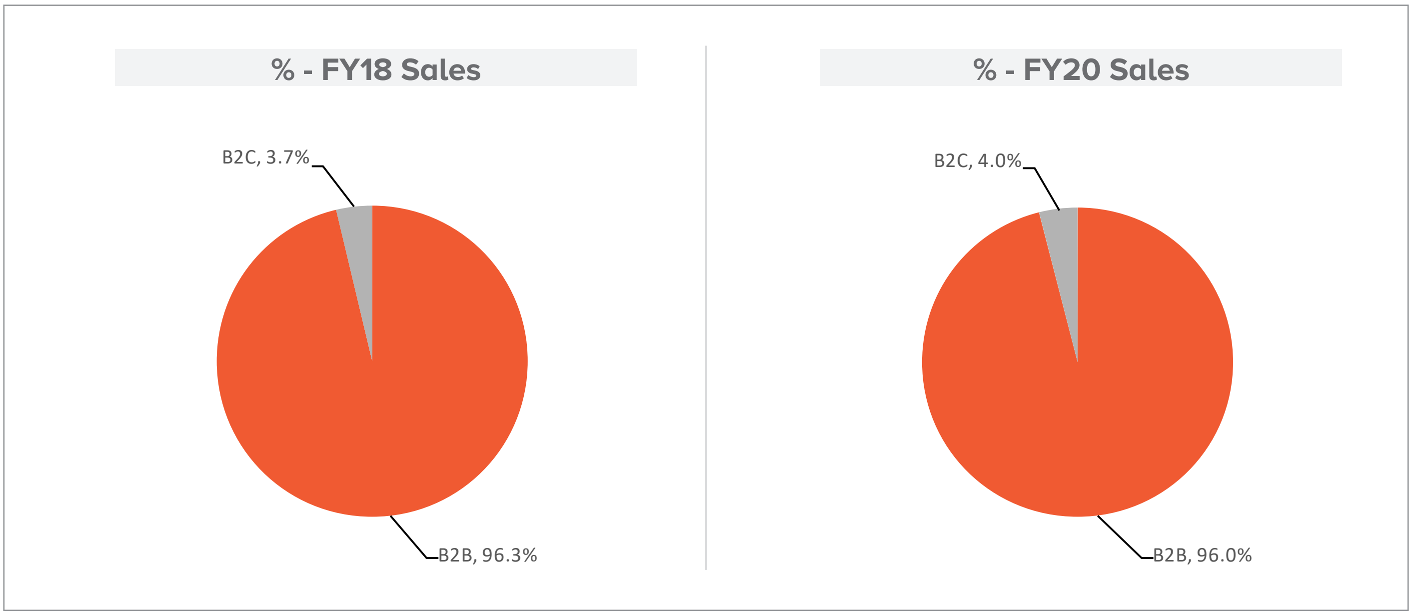
Diversified Business Model Details

	B2B Global				B2C (India)
	B2B IP Led		B2B Tech Transfer	B2B CMO	B2C
	Own Filling	Partner Filling			
Overview	Out-license to Marketing partners.		Co Development with Partner	Fill & Finish Service	Direct Marketing of Products
	Long Term Product Supply Contract		Manufacturing by Gland	Loan & License Agreement	
Revenues Model	License & Milestone Payment		Tech Transfer Fee	Fixed per unit price	Direct Sale of Products
	Selling Price Per unit Dose + profit Share		Selling price per unit Dose + Royalty	-	
ANDA - Ownership	Yes	NA	NA	NA	Yes
IP ownership	Yes	Co-owned	NA	NA	Yes

Source: Company Presentation; Sharekhan Research

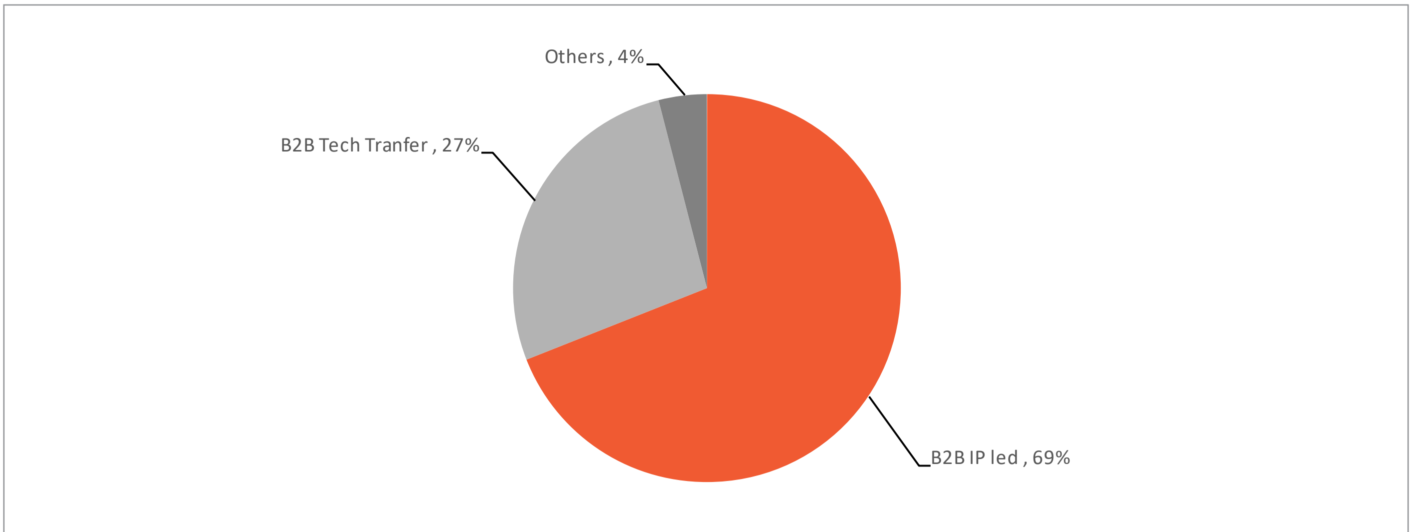
Under the B2B model, the company operates in two different arrangements – B2B Technology transfer and B2B – IP-led model. Under the IP-led model, Gland enters in to long-term development, licensing and manufacturing, and supply agreements with leading pharmaceutical companies, which have strong and independent sales and distribution networks. Gland gets licensing fees together with milestone payments tied to completion of specific product development stages; and once the product is commercialised, the company is entitled to receive selling price (per unit dose) and may additionally receive a profit share or royalties based on net profit or net sales of the product. Under the tech transfer model, the client partially develops the technology and Gland is engaged in certain studies. Under the tech transfer model, partner/client retains ownership of the relevant dossier as well as intellectual property and marketing rights of the product, while Gland has manufacturing rights during the term of the technology transfer agreement.

Overall Revenue Mix



Source: Company Presentation; Sharekhan Research

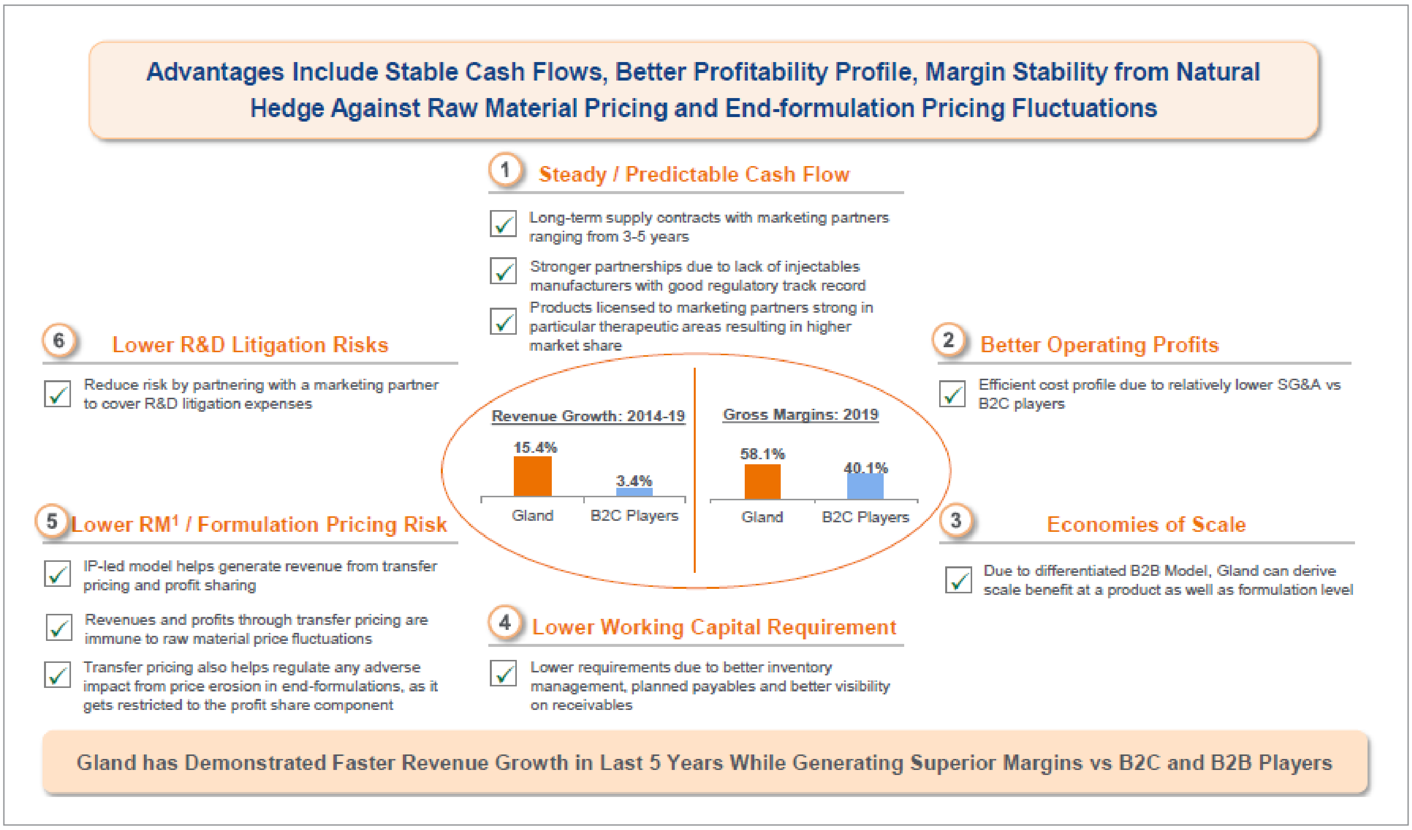
B2B Revenue Mix



Source: Company; Sharekhan Research

The unique B2B model enables the company to grow its market share in key developed markets - US, Europe, Canada, and Australia with reduced investments towards marketing. It also helps leverage the reputation of marketing partners in their home markets to build Gland's presence and supports to build the company's reputation as a complex injectables manufacturer with a consistent compliance record attracting confidence from other potential marketing partners. Further, under the B2B model, customers also undertake plant inspections from time to time, which enable the company to identify affected areas and take corrective actions, thus enabling compliance of regulatory norms across plants.This would support growth going ahead. The B2B model constitutes a sizeable chunk of the company's revenue and constitutes 96.3%, 95.6%, and 96% of sales, respectively, for FY2018/FY2019/FY2020.For the Indian markets, the company operates a B2B CMO model as well as B2C model. Under the B2B CMO model, the company provides fill and finish services for aseptically or terminally sterilised injectables to other pharmaceutical companies. Under this model, the client retains the ownership of the relevant dossier as well as development, intellectual property, and marketing rights of a product, while Gland has the manufacturing right during the term of the agreement. While under the B2C model, the company leverages its brand strength to drive growth in the injectables space. As on March 31, 2020, Gland had a sales force of over 200 employees and an extensive countrywide distribution network covering 2,000 corporate hospitals, nursing homes, and government facilities.Collectively, strong brand strength andwell-penetrated distribution reach augur well and would support topline growth.

Gland's B2B Model: Salient Features



Source: IQVIA Report. *Note: (1) RM Raw Material.*

Extensive portfolio of complex products backed by strong R&D muscle: Gland is a vertically-integrated company with a demonstrated ability to advance a product from the R&D stage through commercialisation. The company's capabilities include internal research &development expertise, robust manufacturing capabilities, a strict quality assurance system, extensive regulatory experience, and established marketing and distribution relationships. Gland is present in sterile injectables, including oncology and ophthalmics and a focus on high-value generics, such as complex molecules, First-to-File products, and 505(b)(2) filings for new drug applications. The company has established a portfolio of injectable products across various therapeutic areas and has delivery systems such as liquid vials, lyophilised vials, pre-filled syringes, ampoules, bags, and drops. Gland is also expanding its development and manufacturing capabilities in the complex injectables space such as peptides, long-acting injectables, suspensions, and hormonal products as well as new delivery systems such as pens and cartridges.The injectables segment appears to have high entry barriers as it is inherently complex resulting in limited competition. Gland has a strong product pipeline. As on December 31, 2020, Gland along with its partners has282 ANDA filings in the US, of which 226 were approved and 56 pending approvals. The 282 ANDA filings comprise 204 ANDA filings for sterile injectables, 51 for oncology, and 27 for ophthalmic related products. Further, for 9MFY21, the company has filed for a total of 19 ANDA's while it has received approval for 24 including five tentative approvals. Also, during 9MFY21, the company has filed for 5 DMF's. The strong product pipeline is supported by an in-house R&D expertise, which is engaged in the development of key processes such as formulation development, analytical method development, API process development, and stability studies, thus supporting the required regulatory filings worldwide. Therefore, a strong base and a sturdy new product launch pipeline would aid topline growth. The share of revenue from new products stood at 13% and 9% as of FY2019 and FY2020, respectively, and this is expected to increase going ahead because of a strong product pipeline. Strong R&D capabilities indicates Gland's ability to consistently commercialise the product pipeline to achieve market penetration, while a well-diversified product pipeline across multiple therapeutic areas would unfold gradually going ahead and would support growth.

Complex Product Portfolio Supported by Strong R&D

Extensive Portfolio of Complex Products

Present in sterile injectables, oncology and ophthalmics, and focus on complex injectables, NCE-1s, First-to-File products and 505(b)(2) filings

Delivery Systems:

- Liquid vials
- Lyophilized vials
- Pre-filled syringes
- Ampoules
- Bags
- Drops

Therapeutic Areas:

- Anti-diabetic
- Anti-infectives
- Anti-malarials
- Anti-neoplastics (Oncology)
- Blood-related
- Cardiac
- Gastro-intestinal
- Hormones
- Neurological and Central Nervous System
- Ophthalmics and Otologicals
- Pain, neuro-muscular blocking agents & analgesics
- Respiratory
- Vitamins, minerals & nutrients

Internal R&D & Regulatory Capabilities

Centralized R&D Laboratory located at Dundigal, Hyderabad facility, with supporting personnel at each manufacturing facility

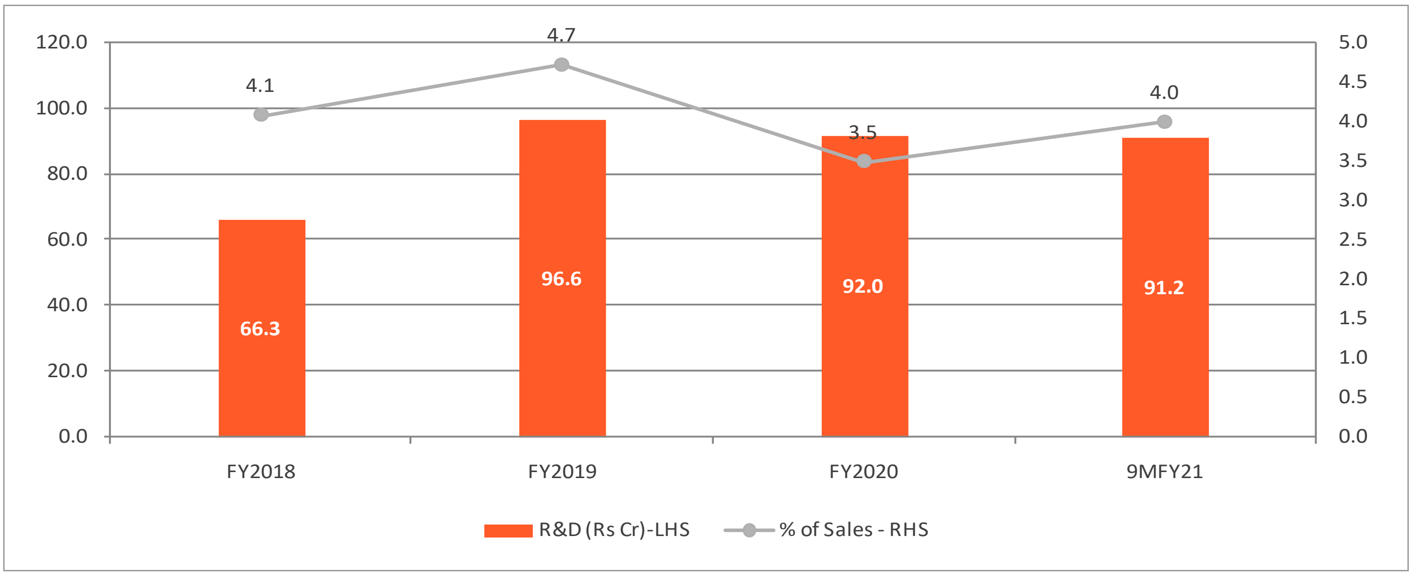
- ~265 personnel team including PhDs, pharmacy post graduates and chemists
- Plan to set up a new R&D building at Pashamylaram, Hyderabad
- R&D expertise supports regulatory filings globally

Regulatory Track Record

- 282 ANDA Filings in US – 226 approved; 56 pending (1)
  - Of 282, 113 owned by Gland Pharma out of which 79 are approved and 34 are pending for approval
  - 204 for sterile injectables, 51 for oncology and 27 for ophthalmics related products
- 1,478 product registrations globally, of which 387 in United States, Europe, Canada and Australia, 69 in India and 1022 in Rest of the world (1)

Source: Company, Sharekhan Research

Trends in R&D Spends (% of sales)



Source: Company; Sharekhan Research

Over the years, Gland has been incurring healthy R&D investments, which has helped it grow. The company incurred R&D spends to the tune of 4% and 3.5% for 9MFY21 and FY20, respectively. Going ahead the management expects to the R&D spends to be around the same levels, which largely would be directed towards building a product pipeline. In addition to this, the company is looking to build a new R&D center at Hyderabad (Pashamylaram) and also to expand the team size with an objective to sustain the momentum of development of complex molecules. A healthy R&D spend would also result in improvement in the quality of fillings, which is likely to be apparent in the next 3-4 years.

Focus on RoW Markets to fuel revenue growth, though over the long term

Currently, Gland is focused on the developed markets of the US, EU, Australia and Canada. Of this, the US is a major contributor to the company's topline accounting for 66.7% of the overall FY2020 sales. While the Rest of the World markets (including China) account for around 8.8%. Going ahead the company also intends to ramp-up its presence in India, China, Brazil and RoW markets with a strategy to reduce the dependence on US and also the leverage US products portfolio in other markets. The generic injectables market in China is around $34bn as compared to $44bn in the US market. China could hence become a big potential market for Gland, wherein the company can leverage its relationship with the parent entity to better penetrate the market, given the drug regulations in China still give preference to the domestic Chinese companies. It is essential for generic players to have a tie-up with a local Chinese company to make a foray in the market. As Gland has a parentage with Shanghai Fosun Pharma, it well placed to enter the Chinese markets and has an edge above as compared to the peers.

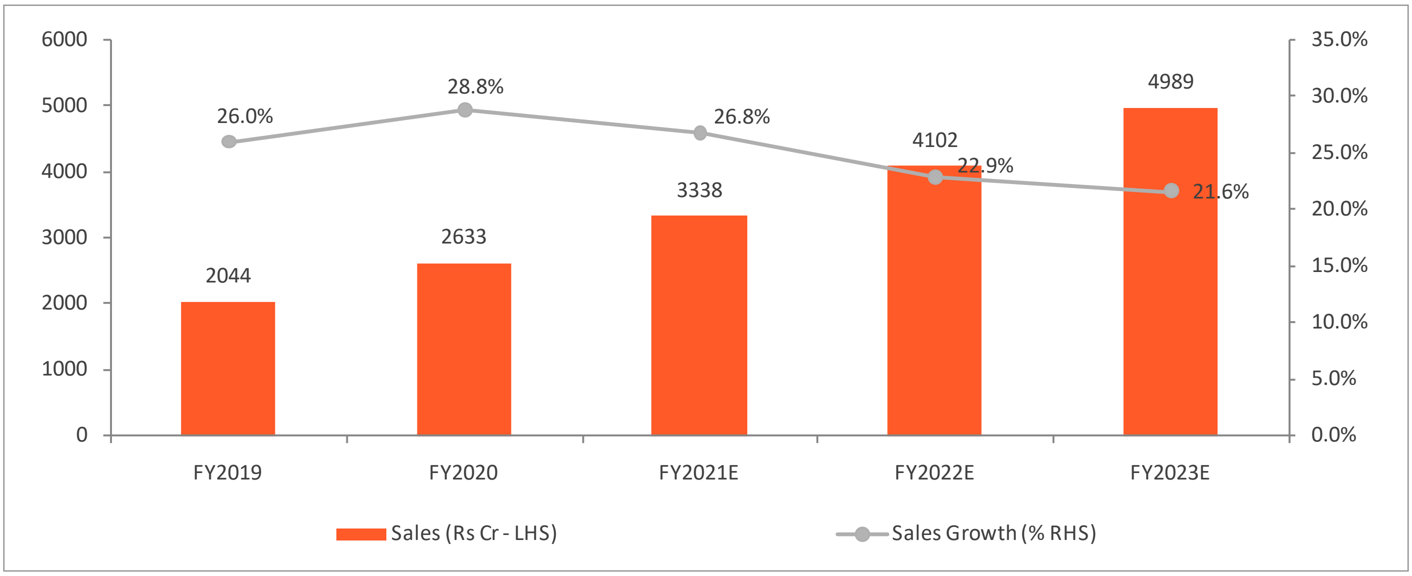
Potential opportunities in the Vaccines space, if accrued to complement existing growth drivers

With the onset of the Covid pandemic there has been a strong need for vaccines to combat the pandemic. Various players across the globe have been in the race with few of them awarded an emergency use authorisation by various countries. The concluding stage in the vaccine manufacturing process is the fill and finish stage, post which the vaccines are distributed. This stage of fill and finish is ideally a non-technology intensive step, albeit at times proves to be a bottleneck for distribution / availability of the vaccines. Gland being an established player in the vaccine space, has a vial capacity of around 380 million units spread across two sterile plants and these could be utilized for the fill and the finish process. Further, the promoter Shanghai Fosun Pharma has inked a deal with a leading vaccine manufacturer and this is likely to positively rub off on Gland as well as it is one of the major injectable facilitiesof the parent. In addition to this the vaccine manufacturers world over are in a fray to supply as many vaccines as possible to various countries, thus pointing at a strong demand potential. Gland has one of the largest vial bottling capacity, with a strong compliance track record and it may look to tie up with vaccine innovators / manufacturers to speed up the process, which in turn would enable to cater to the incremental demand for vaccines.

Exploring inorganic growth avenues - Strategic acquisitions and partnerships: To complement its organic growth and internal expertise, Gland may also pursue strategic acquisitions of companies, products, and technologies to add to its capabilities and technical expertise or enter into partnerships to strengthen its product and technology infrastructure in areas, including steroidal hormonal products, suspensions, anti-neoplastic, and nasal and inhalation products. The company looks to identify API suppliers that complement its business with niche capabilities, including fermentation technology, corticosteroid APIs, and hormonal APIs as well as partners with USFDA-approved facilities to reduce market entry time. In certain markets, where there is preference for local manufacturers, the company may partner with or acquire suitable local manufacturers with manufacturing, R&D, and marketing capabilities to complement its product development capabilities. Gland currently has kept its doors open to explore any inorganic opportunity or partnership. Healthy cashflow generation would enable the company to pursue the above-stated objectives, which would further add to growth.

Strong track record of topline growth and profitability: Gland has a proven track record of a strong performance delivered over FY2018 to FY2020. The topline has staged a sturdy 27.4% CAGR over FY2018 to FY2020 backed by a well-diversifiedbusiness model as well as key customer base and markets. The company's top five customers account for almost half of its overall revenue, with the share almost stable over the said period. Further,a few customers have contracted for products sold across multiple markets and alsohave long-term contracts, which has boosted topline growth. In addition to this the strong capabilities developed in house coupled with a healthy product pipeline have also been the contributors to the revenue growth. Backed by benefits of in-house R&D arm and cost advantages due to operating leverage, EBITDA reported growth of ~37%, while the margins have expanded by 330 bps to 36.3% over the similar time frame. Consequently, earnings have stagedan impressive 55% growth.

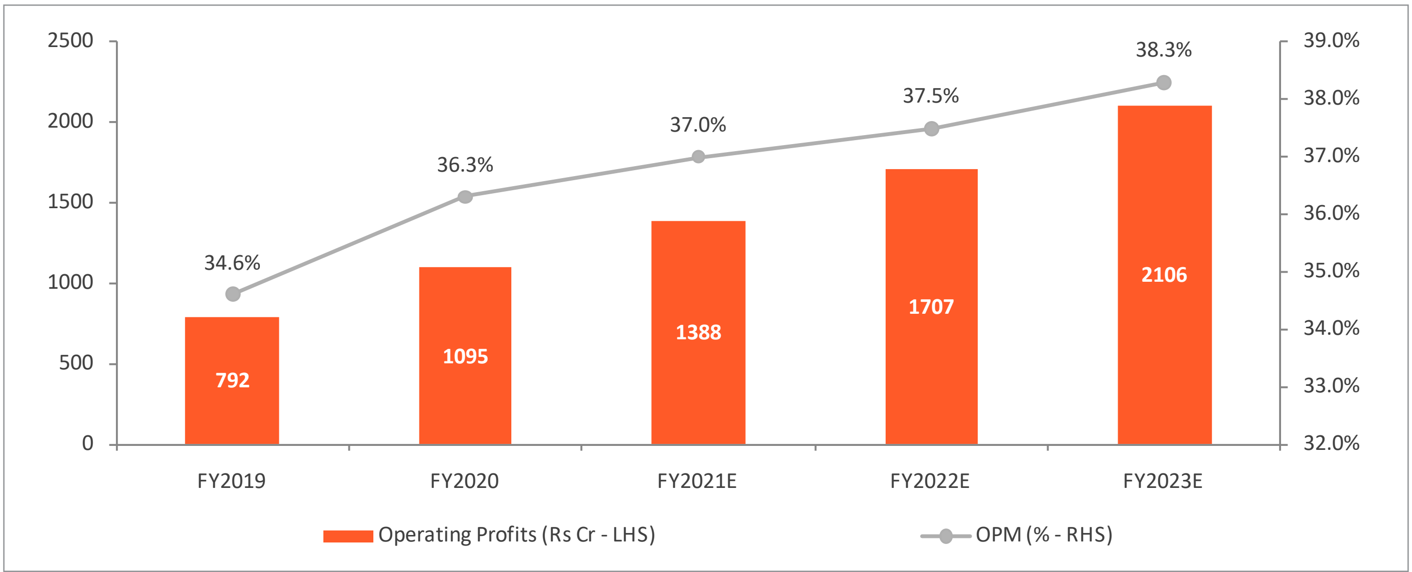
Revenue to sustain the double-digit growth trajectory



Source: Company; Sharekhan Estimates

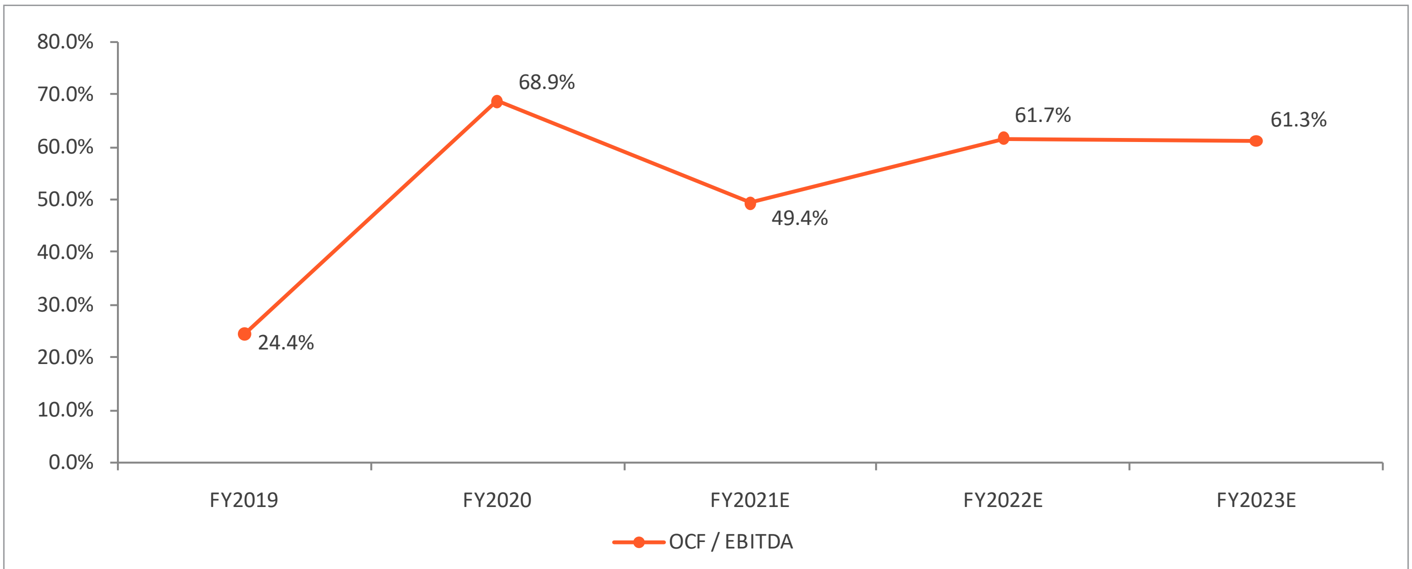
Going ahead, Gland Pharma is expected to continue its strong double-digit topline growth backed by an expected strong demand environment for Injectables being fortified by the company's strong client connects. This would be complemented by a sturdy product pipeline, which would continue to provide new growth avenues. Further, benefits of operating leverage and cost advantages due to vertical integration would result in margin expansion. Consequently, earnings are expected to report a strong 25.9% CAGR over FY2020 to FY2023. Further, Gland's debt levels are almost nil, while capex plans of around Rs.200 crore (for FY2022 and FY2023) would be completely met through proceeds of the IPO as well as through internal accruals. The company's strong earnings performance and a sturdy balance sheet position with almost nil debt would result in healthy return ratios. RoE is expected to be at ~18% levels by FY2023 as compared to 16.5% as of FY2019. Further the company has consistently generated healthy cashflows in the past, however stretched working capital cycles is expected to stress the cashflow generation for FY2021, which is expected to normalize going ahead. Consequently, the OCF/EBITDA ratio is expected to improve to around 61% in FY22 & FY23 as compared to 49% expected in FY21.

OPMs Expanding



Source: Company; Sharekhan Estimates

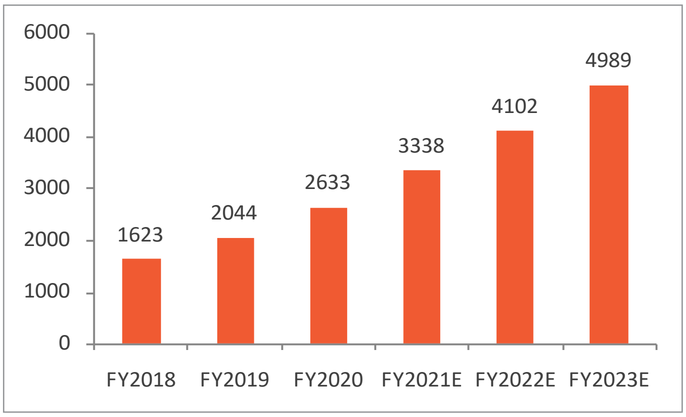
OCF / EBITDA (%)



Source: Company; Sharekhan Estimates

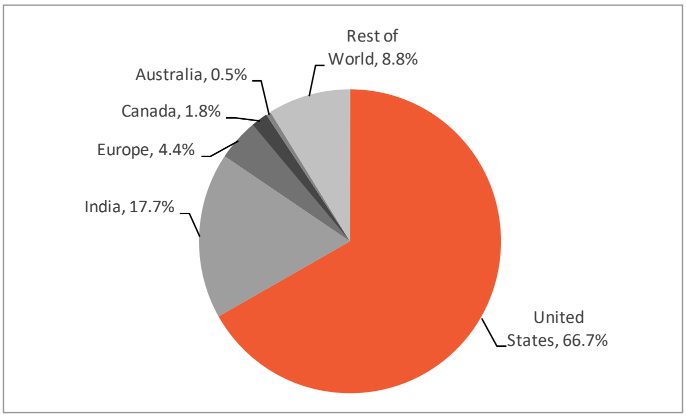
Financials in charts

Sales Trends (Rs Cr)



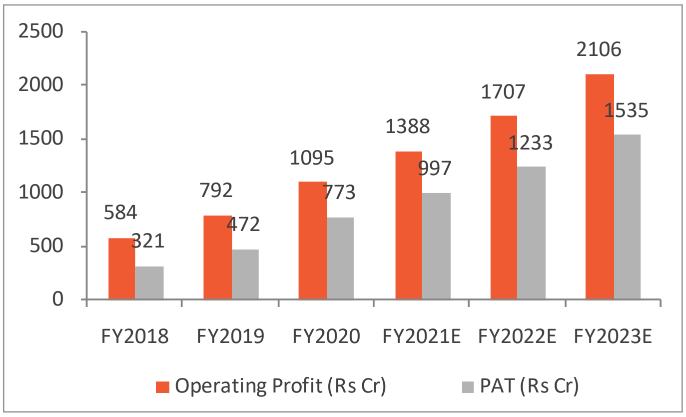
Source: Company, Sharekhan Research

Geography wise Revenue Mix



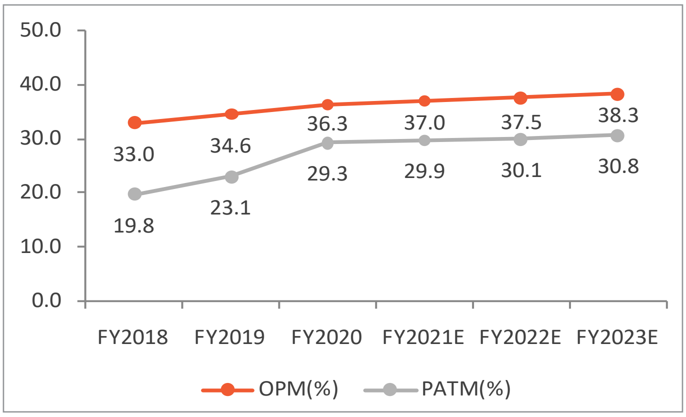
Source: Company, Sharekhan Research

Operating Profit - PAT Trends



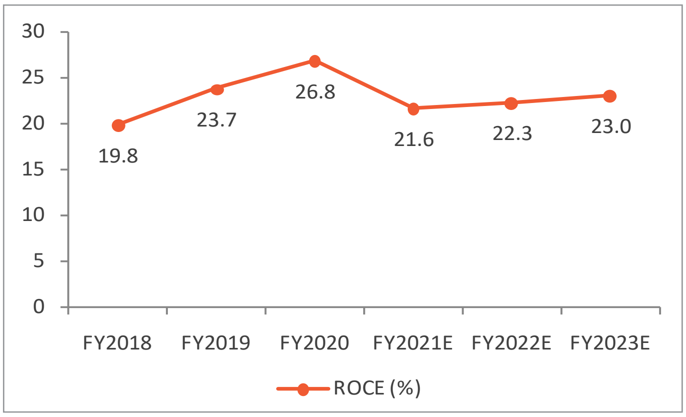
Source: Company, Sharekhan Research

OPM's to improve



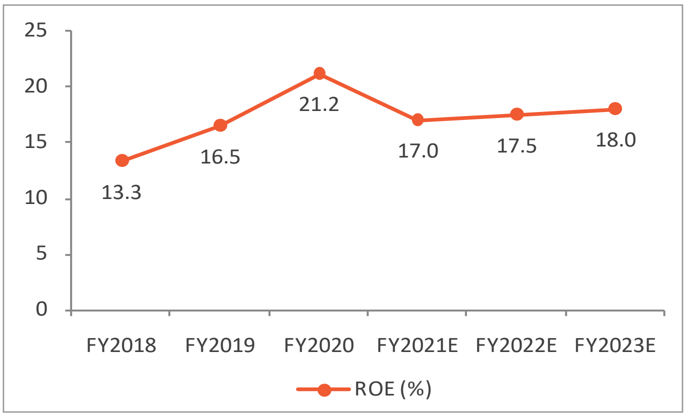
Source: Company, Sharekhan Research

ROCE Trends (%)



Source: Company, Sharekhan Research

Healthy RoE (%)



Source: Company, Sharekhan Research

Outlook and Valuation

■ Sector view - Healthier growth prospects

Indian pharmaceutical companies are better placed to harness opportunities and report healthy growth going ahead. Indian companies are among the most competitive ones globally and hold a sizeable market share in most developed as well as other markets. Moreover, other factors such as easing of pricing pressures (especially in the US generics market), improving product approvals, and plant resolutions by the USFDA coupled with strong growth prospects in domestic markets and emerging opportunities in the API space would be key growth drivers. This would be complemented by the strong capabilities developed by Indian companies (leading to a shift towards complex molecules, biosimilars, and injectables) and commissioning of expanded capacities by select players over the medium term. Collectively, this indicates a strong growth potential going ahead for Indian pharma companies.

■ Company outlook - Well placed to harness growth opportunities

Gland is an established player globally in sterile Injectables and is one of the fastest-growing generic injectable-focused companies.The injectables space inherently has high entry barriers, thus pointing to relatively low competition. Gland has extensive and vertically integrated Injectables manufacturing capabilities and has a consistent regulatory compliance track record, with no observations received from the USFDA. US markets constitute a lion's share of 67% of sales and, hence, a strong compliance track record augurs well.Improved demand traction and incremental capacities coming on-stream, provide ample visibility on growth ahead. Further,the company follows a unique diversified B2B-led model across markets globally, which partially lowers the compliance risk, thus paving the way for faster growth. In the domestic markets, Gland follows a B2C model. Gland has an extensive portfolio of complex products (which are well supported by internal R&D), awaiting to be commercialised across markets. Gland has an experienced management team and is promoted by Shanghai Fosun Pharma. This coupled with focus on the injectables space and strong compliance track record are key positives for Gland. Gland's financial performance over FY2018-FY2020 is impressive and the same is expected to sustain going ahead. We expect sales and the PAT to report a 23.7% and 25.9% CAGR, respectively, over FY2020-FY2023.

■ Valuation - Initiate Coverage with a Buy recommendation and PT of Rs. 3,040

Gland is in a sweet spot, well-placed to harness growth opportunities in the generic injectables space. Being an established player in the injectables space globally, it is slated to benefit from increasing preference for Injectables, while a high entry barrier would ensure lower competitive pressures and sustained growth momentum. Gland has a unique B2B business model, which enables it to gain market share while maintaining its cost leadership. As Gland is largely a B2B player, it is exposed to frequent plant inspections by clients, which ensures consistent adherence to strict compliance norms. The fact that the company has nil observations from USFDA for its plants is testimony to the stringent compliance standards followed. The US market accounts for 67% of the revenue and a clean compliance track record is a key strength. This coupled with consistent shortage of Injectables paves the way for a strong growth going ahead. Moreover, strong capabilities, entry in new geographies like China, an extensive product portfolio backed by strong R&D and vertical integration for APIs, are key growth driver. Potential opportunities in the vaccine space, if accrued would complement growth. Gland's topline and PAT are expected to register a 23.7% and 25.7% CAGR over FY2020 to FY2023. At CMP, the stock trades at valuation of 31.9x/25.7x its FY2022E/FY2023E EPS. Strong domain expertise and growth prospects, sturdy and consistent earnings track record, healthy return ratios and cashflows make Gland an ideal long-term investment pick. We initiate coverage on the stock with a Buy recommendation and a price target (PT) of Rs. 3,040.

Peer comparison

Particulars	CMP (Rs / Share)	O/S Shares (Crs)	Mcap (Rs Cr)	P/E			EV / EBITDA			RoE (%)		
				FY21E	FY22E	FY23E	FY21E	FY22E	FY23E	FY21E	FY22E	FY23E
Aurobindo Pharma	863.0	58.6	50,575.0	15.5	13.3	11.1	8.7	7.1	5.4	16.3	15.1	15.6
Lupin	1,023.0	45.3	46,423.0	42.8	25.1	20.1	16.7	11.5	9.1	8.0	11.9	13.0
Laurus Labs	357.0	53.2	19,175.0	20.6	17.4	14.7	14.1	11.8	10.0	34.2	28.8	25.5
Granules	327.0	24.7	8,090.0	15.0	12.5	10.3	9.6	7.7	6.2	23.3	22.4	22.5
Gland Pharma	2,412.0	16.3	39,431.0	39.5	31.9	25.7	26.2	20.8	16.4	17.0	17.5	18.0
Divis Labs	3,439.0	26.5	91,294.0	46.5	35.5	28.1	31.6	24.4	19.3	22.1	23.2	23.2
PI Industries	2,217	15.2	33,642	50.7	40.1	31.4	34.7	27.5	21.7	17	15.1	16.7

Source: Company, Sharekhan estimates

Financials

Profit & Loss Rs cr

Particulars	FY2019	FY2020	FY2021E	FY2022E	FY2023E
Total Revenues	2,044.2	2,633.2	3,338.2	4,102.2	4,988.6
Raw material Cost	(857.0)	(1,102.0)	(1,385.4)	(1,690.1)	(2,035.4)
Employee Cost	(222.9)	(277.7)	(340.5)	(410.2)	(488.9)
Other Expenses	(257.7)	(298.1)	(377.2)	(463.5)	(553.7)
Total Operating Expense	(1,337.7)	(1,677.8)	(2,103.1)	(2,563.8)	(3,078.0)
Operating Profits	792.1	1,094.6	1,388.2	1,706.7	2,106.0
Other Income	85.6	139.2	153.1	168.4	195.3
Interest	(3.7)	(7.2)	(6.5)	(6.5)	(6.5)
Depreciation	(82.1)	(94.6)	(103.1)	(118.8)	(123.4)
Profit Before tax	706.2	992.8	1,278.6	1,581.3	1,976.1
Tax Expense	(234.4)	(220.0)	(281.3)	(347.9)	(440.7)
Reported PAT	471.8	772.8	997.3	1,233.4	1,535.4

Source: Company; Sharekhan estimates

Balance Sheet Rs cr

Particulars	FY2019	FY2020	FY2021E	FY2022E	FY2023E
Sources Of Funds					
Equity Capital	15.5	15.5	16.3	16.3	16.3
Reserves & Surplus	2846.5	3630.7	5839.9	7027.5	8507.9
Net Worth	**2862.0**	**3646.2**	**5856.2**	**7043.8**	**8524.2**
Non Controlling interest	0.0	0.0	0.0	0.0	0.0
Total Borrowings	5.0	4.1	4.1	4.1	4.1
Deferred Tax liabiities	107.6	74.1	74.1	74.1	74.1
Capital Employed	**2990.8**	**3727.0**	**5937.0**	**7124.6**	**8605.0**
Application of Funds					
Net Block	929.6	968.1	1115.0	1196.2	1272.8
Capital WIP	123.2	188.5	150.0	90.0	50.0
Investments	6.4	6.9	7.3	7.6	8.0
Goodwill	0.0	0.0	0.0	0.0	0.0
Current assets	**2357.4**	**2836.8**	**5001.5**	**6244.3**	**7774.1**
Inventories	911.9	756.3	1051.8	1258.7	1503.4
Debtors	506.1	601.8	777.4	932.8	1134.4
Cash & Bank Balance	753.3	1325.2	3011.2	3878.7	4948.4
Loans & advances	0.3	0.5	0.5	0.5	0.5
Other Current Assets	185.9	153.0	160.7	173.5	187.4
Current Liabilities & Provisions	**532.8**	**359.0**	**403.4**	**478.2**	**562.5**
Trade Payables	446.2	249.1	303.6	370.4	446.1
Other current Liabilities	83.7	92.4	99.8	107.8	116.4
Provisions	2.9	17.5	19.2	21.1	23.3
Net Assets	**2990.8**	**3727.0**	**5937.0**	**7124.6**	**8605.0**

Source: Company; Sharekhan estimates

Cash Flow Statement Rs cr

Particulars	FY2019	FY2020	FY2021E	FY2022E	FY2023E
Cash flow from operating activities	193	754	685	1054	1285
Cash flow from investing activities	-90	-193	-212	-140	-160
Cash flow from financing activities	-21	11	1213	-46	-55
Net Change in cash and cash equivalents	83	572	1686	868	1070
Opening Cash	671	753	1325	3011	3879
Closing Cash	753	1325	3011	3879	4948
Free Cash Flows (FCF)	104	562	474	914	1125

Source: Company; Sharekhan estimates

Key Ratios

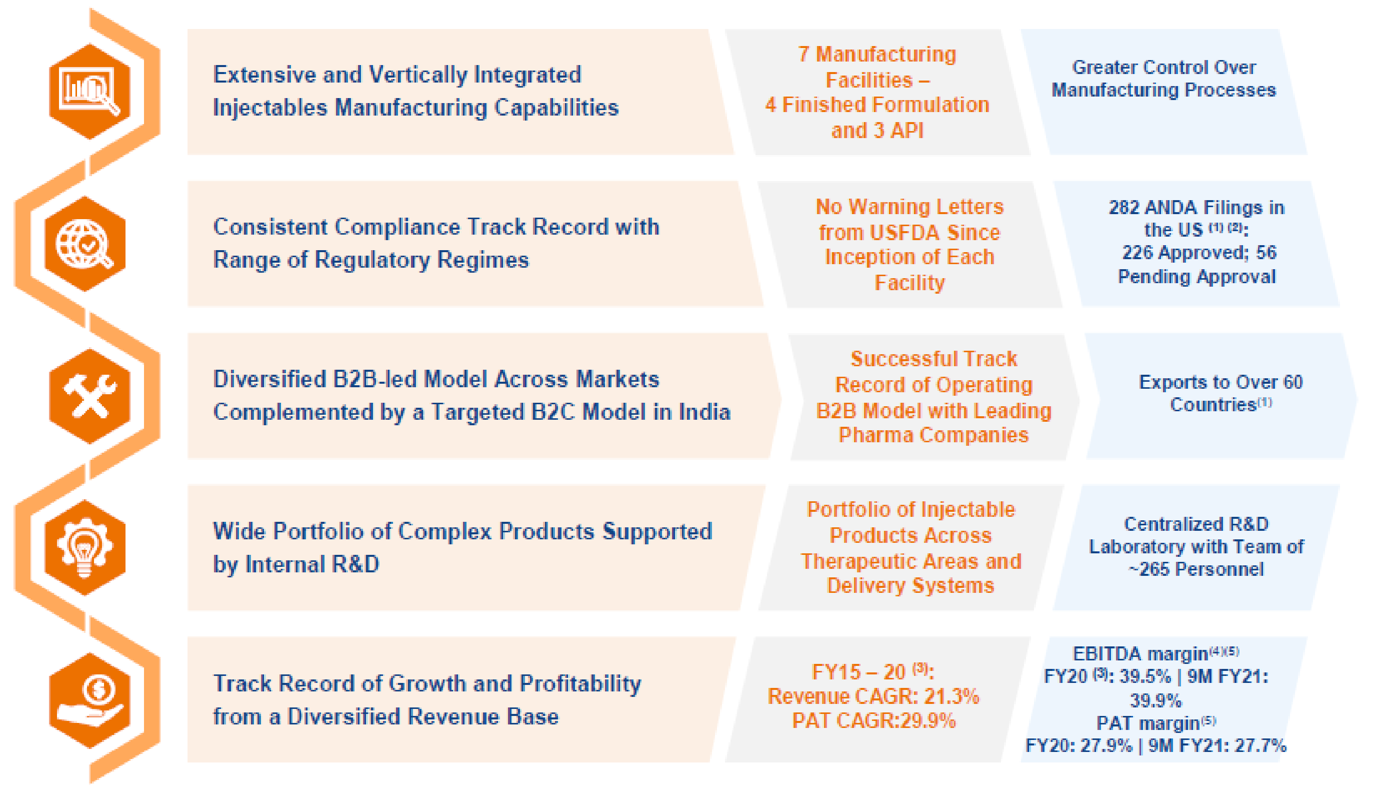
Particulars	FY2019	FY2020	FY2021E	FY2022E	FY2023E
Margins (%)					
Gross Profit Margin	58.1	58.1	58.5	58.8	59.2
Operating Margin	34.6	36.3	37.0	37.5	38.3
EBIT Margin	33.3	36.1	36.8	37.2	38.2
Tax Rate	(33.2)	(22.2)	(22.0)	(22.0)	(22.3)
As a percentage of revenue (%)					
Raw Material Expenses	(41.9)	(41.9)	(41.5)	(41.2)	(40.8)
Employee Expenses	(10.9)	(10.5)	(10.2)	(10.0)	(9.8)
Other Expenses	(12.6)	(11.3)	(11.3)	(11.3)	(11.1)
Financial Ratios					
Debt/Equity (x)	0.0	0.0	0.0	0.0	0.0
Inventory Days	162.8	104.8	115.0	112.0	110.0
Debtor Days	90.4	83.4	85.0	83.0	83.0
Payable Days	190.0	82.5	80.0	80.0	80.0
Working Capital Days	63.2	105.7	120.0	115.0	113.0
AEPS (Rs)	28.9	47.3	61.1	75.5	94.0
CEPS (Rs)	33.9	53.1	67.4	82.8	101.6
DPS (Rs)	0.0	0.0	2.0	2.4	2.9
BVPS (Rs)	175.3	223.3	358.6	431.4	522.0
RoNW (%)	16.5	21.2	17.0	17.5	18.0
RoCE (%)	23.7	26.8	21.6	22.3	23.0
Valuation Ratios					
CMP	2,412.0	2,412.0	2,412.0	2,412.0	2,412.0
P/E (x)	83.5	51.0	39.5	31.9	25.7
Market Cap (Rs Crore)	39,385.2	39,385.2	39,385.2	39,385.2	39,385.2
Market Cap / Sales (x)	19.3	15.0	11.8	9.6	7.9
Enterprise Value (Rs Crore)	38,630.4	38,057.1	36,370.8	35,502.9	34,432.8
EV / Sales (x)	18.9	14.5	10.9	8.7	6.9
EV / EBITDA (x)	48.8	34.8	26.2	20.8	16.4
P/BV (x)	13.8	10.8	6.7	5.6	4.6
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0
Growth Ratios (%)					
Revenue	26.0	28.8	26.8	22.9	21.6
EBITDA	34.6	36.3	37.0	37.5	38.3
EBIT	33.3	36.1	36.8	37.2	38.2
PBT	40.8	40.6	28.8	23.7	25.0
APAT	46.9	63.8	29.0	23.7	24.5
EPS	46.9	63.8	29.0	23.7	24.5

Source: Company; Sharekhan estimates

Company Background

Gland Pharma Limited (Gland) was established in Hyderabad in 1978. The company is a vertically integrated company with capabilities including internal research and development expertise, robust manufacturing capabilities, a stringent quality assurance system, extensive regulatory experience, and established marketing and distribution relationships. The company has expanded from liquid parenterals to cover other elements of the injectables value chain, including contract development, own development, dossier preparation and filing, technology transfer, and manufacturing across a range of delivery systems. Predominantly, Gland has been focusing on the injectables space with negligible or no presence in orals. The company focuses on meeting diverse injectables needs with a stable supply of affordable and high-quality products. Gland follows a unique B2B business model and has a successful track record of operating this model across multiple geographies. Gland has a total of 7 manufacturing plants with 3 of them being API plants. Of the balance 2 are sterile injectables plant while one each for oncology and opthalmolgy.

Company Snapshot



Note: (1) As of December 31, 2020. (2) Filed by Gland Pharma, along with partners. (3) Based on Financial Information prepared in accordance with Ind AS (4) EBITDA stands for earnings before interest, taxes, depreciation and amortization which has been arrived at by adding finance expense, depreciation expense, exceptional items and total tax expense to the profit for the year or period. (5) EBITDA margin = EBITDA / Total Income; PAT margin = PAT / Total Income.

Source: Company; Sharekhan Estimates

Investment Thesis

Gland is an established player globally in sterile injectables and is one of the fastest growing generic injectable-focused companies. Due to the inherent nature of injectables, the space has high entry barriers, thus pointing at relatively low competition. Gland has extensive and vertically integrated injectables manufacturing capabilities and has a consistent regulatory compliance track record, with no observations received from the USFDA. US markets constitute a lion's share of 67% of sales and, hence, a strong compliance track record augurs well. Improved demand traction and incremental capacities coming on stream provide ample visibility on growth ahead. Further, the company follows a unique diversified B2B-led model across markets globally, which partially lowers the compliance risk, thus paving way for faster growth. In domestic markets, Gland follows a B2C model. Gland has an extensive portfolio of complex products (which are well supported by internal R&D), awaiting to be commercialised across markets. Gland has an experienced management team and is promoted by Shanghai Fosun Pharma. This coupled with focus on the injectable space and strong compliance track record are key plus points for Gland.

Key risk

- Any adverse change in the regulatory landscape and delay in procuring product approvals can impact growth prospects.
- Product concentration risk exists as top five products constitute around 45% of US sales.
- Adverse forex movement.

Additional Data

Key management personnel

Mr Srinivas Sadu	Managing Director & Chief Executive Officer
Mr Ravi Mitra	Chief Financial Officer
KVGK Raju	Chief Technology Officer

Source: Company website

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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Registered Office: Sharekhan Limited, 10th Floor, Beta Building, Lodha iThink Techno Campus, Off. JVLR, Opp. Kanjurmarg Railway Station, Kanjurmarg (East), Mumbai – 400042, Maharashtra. Tel: 022 - 61150000. Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE / MSEI (CASH / F&O / CD) / MCX - Commodity: INZ000171337; DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669; Research Analyst: INH000006183;