

India

ADD (no change)

Consensus ratings*: Buy 7 Hold 5 Sell 3

Current price:	Rs829
Target price:	Rs1,235
Previous target:	Rs1,290
Up/downside:	49.0%
InCred Research / Consensus:	11.5%
Reuters:	NATP.NS
Bloomberg:	NTCPH IN
Market cap:	US\$2,030m
	Rs151,103m
Average daily turnover:	US\$7.3m
	Rs544.7m
Current shares o/s:	182.5m
Free float:	51.1%

*Source: Bloomberg

Key changes in this note

- Cut FY22F/23F revenue by 4.8%/11.4%
- Cut FY22F/23F EBITDA by 14.4%/10.4%
- Cut FY22F/23F EPS by 14.5%/8.9%



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	(7.2)	(20.4)	(8.6)
Relative (%)	(7.9)	(28.1)	(34.7)

Major shareholders	% held
Promoter & Promoter Group	48.9
Mirae Asset Bluechip Fund	4.0
Life Insurance Corporation of India	4.0

Analyst(s)



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Natco Pharma Ltd

Weak quarter; long-term outlook intact

- Natco's 2QFY22 earnings were below our estimates, mainly due to lower-than-expected operating performance.
- Management expects a strong rebound in 2HFY22 with many low competitive launches to gain traction and recovery in the domestic segment.
- We reiterate our Add rating and roll forward our SOP-based TP to FY24F.

2QFY22 earnings below our estimates

Revenue de-grew by 53% yoy in 2Q to Rs3.77bn (our estimate Rs4.3bn). EBITDA declined by 74% yoy /36% qoq to Rs705m (our estimate Rs1.1bn), and EBITDA margin contracted by 1580bp yoy and 800bp qoq to 18.7% in 2Q. PAT of Rs651m (our estimate Rs738m) de-grew 68% yoy/13%qoq. Revenue and profits declined yoy mainly on a high base which included settlement income of gRevlimid in Canada and higher gTamiflu supplies.

Recovery seen in Oncology sales in domestic business

India revenue declined 8% in 2QFY22. The Oncology segment, which was impacted by Covid-19 in the last few quarters due to lower patient footfalls for hospital therapies, is seeing recovery with a decline in Covid cases and management believes pricing pressure will decline in oncology. Management is looking for new launches in oncology and its Cardio-Diabeto segment. Management highlighted that the domestic business is pivoted towards the Covid-19 portfolio like anti-fungal drugs and anticoagulants and expects the Drugs Controller General of India's (DCGI) approval for Molnupiravir soon. We expect Natco's domestic business revenue CAGR to be 14% over FY21-FY24F, assuming a recovery in the oncology segment, ramp-up in the Covid portfolio and new launches.

High base impacted export business growth

Export formulations, including subsidiaries, fell by 60% yoy, mainly impacted by higher gTamiflu supplies on Covid demand and settlement income for gRevlimid included in 2QFY21. However, we expect a recovery from 2HFY22 with the ramp-up of new launches in the US like gAfitinor, gZortress to support sales growth in FY22F/23F. gRevlimid's launch would have the most impact, supporting Natco's revenue growth in the US beyond FY22F, in our view.

Reiterate Add rating with lower TP of Rs1,235

We introduce FY24 estimates and lower our EPS estimates for FY22F/FY23F by 15%/9% assuming lower-than-expected export formulation sales and operating performance. We believe Natco has a strong PARA-IV product pipeline, while execution remains key. We reiterate our Add rating and roll forward our target valuation to FY24F with lower SOP-based TP of Rs1,235 (from Rs1,290) ascribing P/E of 23x FY24F to its base business EPS of Rs46.3 plus NPV of Rs170/share for its key products opportunity. Downside risk: Delay in any high-value launches estimated in the US. Key catalyst: Earlier-than-expected high-value product launches.

Financial Summary	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Revenue (Rsm)	19,150	20,521	25,118	41,867	47,841
Operating EBITDA (Rsm)	5,826	6,062	8,038	19,677	24,877
Net Profit (Rsm)	4,608	4,409	5,963	15,148	19,384
Core EPS (Rs)	25.3	24.2	32.7	83.0	106.2
Core EPS Growth	(28.0%)	(4.3%)	35.1%	154.0%	28.0%
FD Core P/E (x)	32.78	34.26	25.36	9.98	7.80
DPS (Rs)	7.0	6.2	6.0	6.0	0.0
Dividend Yield	1.05%	0.74%	0.72%	0.72%	0.72%
EV/EBITDA (x)	26.37	24.89	18.78	7.34	5.24
P/FCFE (x)	(107.73)	31.04	58.63	19.30	9.74
Net Gearing	6.6%	(0.4%)	(0.7%)	(11.2%)	(26.6%)
P/BV (x)	4.00	3.67	3.28	2.51	1.93
ROE	12.7%	11.2%	13.7%	28.5%	28.0%
% Change In Core EPS Estimates			(14.53%)	(8.92%)	
InCred Research/Consensus EPS (x)			1.31	1.31	1.35

SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS, PRICED AS AT 12 NOV 2021

Weak quarter; long-term outlook intact

Key takeaways from the results conference call

On the domestic business ➤

- The company has good launches lined up in the oncology segment, including Azacitidine.
- The oncology segment, impacted by Covid in FY21, is now stable and management expects price erosion to decline. It expects steady revenue from this segment now.
- Management added that Molnupiravir will be a big launch in the domestic and exports markets. It expects to launch the drug in Nov 2021 if it obtains the required licence. The company already has a tie-up in place for Molnupiravir's supply chain.
- Products Ticagrelor and Dabigatran did very well as they were used in Covid treatment but have now settled to normalised sales.
- The company launched Eltrombopag (Novartis) and is the only generic player in India.
- On product Coragen litigation, management said the next court hearing is on 15-16 Dec 2021.

On the exports business ➤

- Management is confident its product Revlimid will do well in Canada (market size US\$400m-500m). Currently there are four generic approvals. Sandoz and Natco Pharma are on the innovators Risk Evaluation and Mitigation Strategy (REMS) program, while Dr Reddy's and Apotex are on their own REMS program.
- Natco has a first-to-file (FTF) and final approval on 5mg, 15mg, 25mg strengths of gRevlimid in the US, while Dr Reddy's has FTF and approval on 2.5 and 20mg. Management highlighted that 90% of the market size is covered by Natco Pharma.
- The Imbruvica litigation may continue for a further 18-24 months.
- The company is doing well in the product Copaxone and has seen a steady market share, while Afinitor 10mg has done very well.
- Regarding Zortress, management said that it is a three-player market (Hikma, Natco and one more player) and the market size is lower than US\$200m.
- The company has made a product filing for Yondelis in the US and Europe in partnership with Sun Pharma.

On the agro-chem business ➤

- The agro-chem business's Rs35m revenue in 2QFY22 was primarily driven by the pheromones product used to control pink bollworm in cotton crops.
- Management highlighted that the company could launch chlorantraniliprole (CTPR) in Aug 2022 and could do more interesting filings in this business.

On capex ➤

- The company incurred maintenance capex of Rs720m in 1HFY22. It plans to spend 60-70% of the budgeted capex of Rs3.4bn in FY22. It does not expect any large capex spend in the next 2-3 years as there are enough capacities available.

Figure 1: Quarterly consolidated summary

YE 31 March	2QFY21	2QFY22	% yoy	1QFY22	%qoq	1HFY21	1HFY22	% yoy
Sales (Rsm)	8,022	3,772	(53.0)	4,103	(8.1)	13,656	7,875	(42.3)
Gross Profit (Rsm)	6,073	2,847	(53.1)	3,312	(14.0)	9,918	6,159	(37.9)
Gross Margin (%)	75.7	75.5	-23bps	80.7	-524bps	72.6	78.2	558bps
EBITDA (Rsm)	2,764	705	(74.5)	1,098	(35.8)	4,475	1,803	(59.7)
EBITDA margin (%)	34.5	18.7	-1576bps	26.8	-807bps	32.8	22.9	-987bps
Interest (Rsm)	27	40	48.1	20	100.0	64	60	(6.3)
Depreciation (Rsm)	287	347	20.9	338	2.7	567	685	20.8
Other income (Rsm)	257	380	47.9	170	123.5	444	550	23.9
PBT before extra-ordinary items (Rsm)	2,707	698	(74.2)	910	(23.3)	4,288	1,608	(62.5)
Extraordinary income	-	-	-	-	-	-	-	-
Extraordinary expenses	-	-	-	-	-	-	-	-
PBT after extra-ordinary items (Rsm)	2,707	698	(74.2)	910	(23.3)	4,288	1,608	(62.5)
Tax (Rsm)	718	161	(77.6)	156	3.2	1,143	317	(72.3)
Effective tax rate (%)	24.7	6.7	NM	17.6	NM	24.0	12.9	NM
Reported PAT (Rsm)	2,024	651	(67.8)	750	(13.2)	3,252	1,401	(56.9)
Adjusted PAT (Rsm)	2,024	651	(67.8)	750	13.2)	3,252	1,401	(56.9)

SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 2: Natco's quarterly sales breakdown

YE March (Rsm)	2QFY21	2QFY22	% yoy	1QFY22	%qoq	1HFY21	1HFY22	% yoy
Formulations	5,903	2,903	-50.8	3,460	-16.1	9,902	6,363	-35.7
Domestic	1,083	998	-7.8	2,006	-50.2	2,340	3,004	28.4
Exports (incl. subsidiaries)	4,820	1,905	-60.5	1,454	31.0	7,562	3,359	-55.6
API	1,995	763	-61.8	616	23.9	3,434	1,379	-59.8
Other Operating Income	124	71	-42.7	22	222.7	320	93	-70.9
Crop Health Sciences	0	35	NM	5	600.0	0	40	NM
Total	8,022	3,772	-53.0	4,103	-8.1	13,656	7,875	-42.3

SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 3: Revised earnings estimates

Rsm	Old estimates		New estimates		Change (%)	
	FY22F	FY23F	FY22F	FY23F	FY22F	FY23F
Revenue	26,386	47,240	25,118	41,867	-4.8	-11.4
EBITDA	9,394	21,966	8,038	19,677	-14.4	-10.4
EBITDA Margin (%)	35.6	46.5	32.0	47.0	-360bps	50bps
PAT	6,978	16,632	5,963	15,148	-14.5	-8.9
EPS (Rs)	38.2	91.1	32.7	83.0	-14.5	-8.9

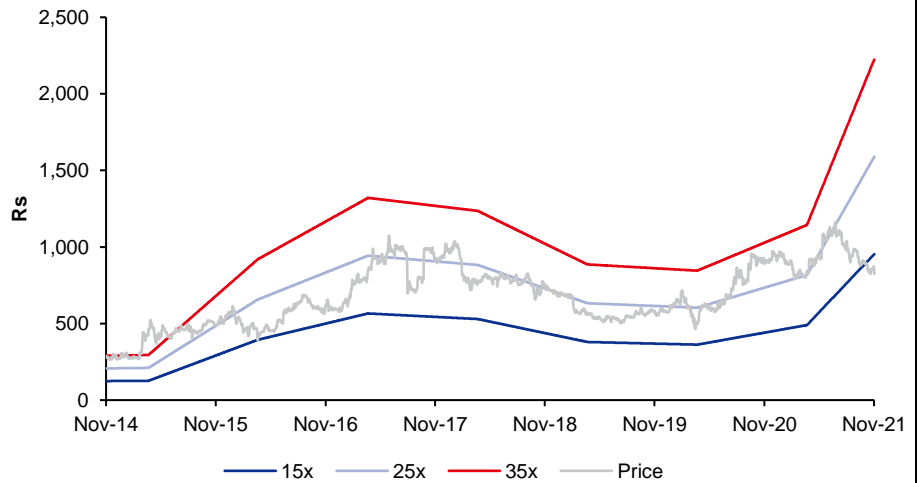
SOURCES: INCRED RESEARCH ESTIMATES

Figure 4: Annual revenue breakdown assumptions

Particulars (Rsm)	FY21	FY22F	FY23F	FY24F
Domestic formulations	4,102	4,971	5,260	6,074
% sales	20.0	19.8	12.6	12.7
% yoy	(24.1)	21.2	5.8	15.5
Export formulations (incl. subsidiaries)	10,771	17,027	33,059	37,730
% sales	52.5	67.8	79.0	78.9
% yoy	(18.1)	72.9	118.5	18.1
API	5,120	2,714	3,121	3,589
% sales	25.0	10.8	7.5	7.5
% yoy	44.1	(47.0)	15.0	15.0
Other Operating Income	507	355	373	391
% sales	2.5	1.4	0.9	0.8
% yoy	269.7	33.1	40.9	0.5
Crop Health Sciences	21	52	55	57
% sales		0.2	0.1	0.1
% yoy		147.6	5.0	5.0
Total	20,521	25,118	41,867	47,841

SOURCES: INCRED RESEARCH ESTIMATES, COMPANY REPORTS

Figure 5: P/E band: One-year forward

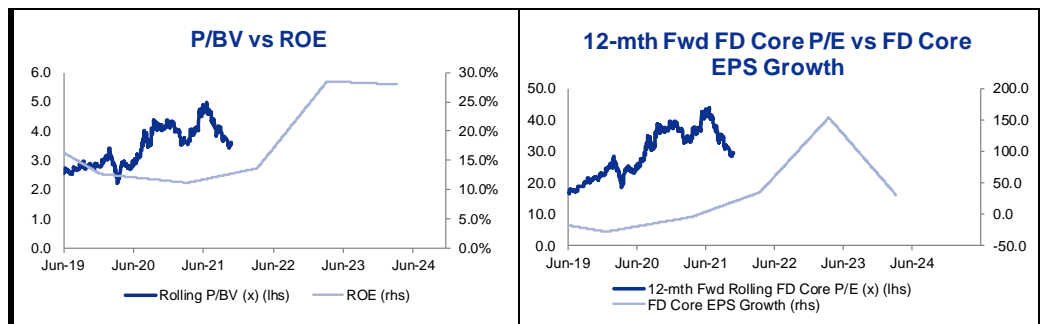


SOURCES: INCRED RESEARCH, BLOOMBERG

Figure 6: P/E standard deviation: One-year forward



SOURCES: INCRED RESEARCH, BLOOMBERG

BY THE NUMBERS

Profit & Loss

(Rs mn)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Net Revenues	19,150	20,521	25,118	41,867	47,841
Gross Profit	15,334	15,407	19,843	33,912	39,708
Operating EBITDA	5,826	6,062	8,038	19,677	24,877
Depreciation And Amortisation	(998)	(1,169)	(1,255)	(1,342)	(1,428)
Operating EBIT	4,828	4,893	6,783	18,336	23,449
Financial Income/(Expense)	(215)	(133)	(158)	(182)	(179)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	1,074	1,036	1,140	1,538	1,923
Profit Before Tax (pre-EI)	5,687	5,796	7,764	19,693	25,193
Exceptional Items					
Pre-tax Profit	5,687	5,796	7,764	19,693	25,193
Taxation	(1,106)	(1,372)	(1,786)	(4,529)	(5,794)
Exceptional Income - post-tax					
Profit After Tax	4,581	4,424	5,978	15,163	19,399
Minority Interests	27	(15)	(15)	(15)	(15)
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	4,608	4,409	5,963	15,148	19,384
Recurring Net Profit	4,608	4,409	5,963	15,148	19,384
Fully Diluted Recurring Net Profit	4,608	4,409	5,963	15,148	19,384

Cash Flow

(Rs mn)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
EBITDA	5,826	6,062	8,038	19,677	24,877
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(2,689)	2,473	(3,649)	(6,614)	(3,243)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow					
Net Interest (Paid)/Received	(215)	(133)	(158)	(182)	(179)
Tax Paid	(1,311)	(1,478)	(1,786)	(4,529)	(5,794)
Cashflow From Operations	1,611	6,924	2,445	8,352	15,661
Capex	(3,374)	(2,611)	(2,005)	(2,005)	(2,005)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	1,074	1,036	1,140	1,538	1,923
Cash Flow From Investing	(2,300)	(1,575)	(865)	(467)	(82)
Debt Raised/(repaid)	(713)	(483)	1,000	(50)	(50)
Proceeds From Issue Of Shares	(1)	1			
Shares Repurchased					
Dividends Paid	(1,536)	(1,138)	(1,095)	(1,095)	(1,095)
Preferred Dividends					
Other Financing Cashflow	804	(1,554)	(319)	(349)	(382)
Cash Flow From Financing	(1,446)	(3,174)	(414)	(1,494)	(1,527)
Total Cash Generated	(2,135)	2,175	1,166	6,391	14,051
Free Cashflow To Equity	(1,402)	4,866	2,579	7,835	15,529
Free Cashflow To Firm	(474)	5,482	1,737	8,067	15,758

SOURCES: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS...cont'd

Balance Sheet					
(Rs mn)	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Total Cash And Equivalents	660	2,835	4,001	10,392	24,443
Total Debtors	5,513	4,129	6,882	9,176	10,486
Inventories	5,580	7,982	9,290	14,338	16,384
Total Other Current Assets	11,216	6,984	7,053	7,122	7,192
Total Current Assets	22,969	21,930	27,225	41,028	58,504
Fixed Assets	20,936	22,372	23,117	23,775	24,347
Total Investments	1,123	3,037	3,341	3,675	4,042
Intangible Assets	88	94	99	104	109
Total Other Non-Current Assets	762	486	521	541	571
Total Non-current Assets	22,909	25,989	27,078	28,095	29,069
Short-term Debt	3,150	2,667	3,667	3,617	3,567
Current Portion of Long-Term Debt					
Total Creditors	2,554	1,462	1,872	2,432	2,517
Other Current Liabilities	1,149	1,127	1,183	1,387	1,460
Total Current Liabilities	6,853	5,256	6,722	7,436	7,543
Total Long-term Debt	8	11	11	11	11
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	9	9	9	9	9
Total Non-current Liabilities	17	20	20	20	20
Total Provisions	1,161	1,409	1,459	1,511	1,566
Total Liabilities	8,031	6,685	8,201	8,967	9,129
Shareholders Equity	37,735	41,216	46,084	60,138	78,426
Minority Interests	112	18	18	18	18
Total Equity	37,847	41,234	46,102	60,156	78,444

Key Ratios					
	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Revenue Growth	(8.6%)	7.2%	22.4%	66.7%	14.3%
Operating EBITDA Growth	(26.7%)	4.1%	32.6%	144.8%	26.4%
Operating EBITDA Margin	30.4%	29.5%	32.0%	47.0%	52.0%
Net Cash Per Share (Rs)	(13.73)	0.86	1.77	37.06	114.33
BVPS (Rs)	207.34	225.84	252.52	329.52	429.73
Gross Interest Cover	22.46	36.79	42.95	100.96	130.91
Effective Tax Rate	19.4%	23.7%	23.0%	23.0%	23.0%
Net Dividend Payout Ratio	27.8%	19.3%	14.1%	5.6%	4.3%
Accounts Receivables Days	100.78	85.75	80.00	70.00	75.01
Inventory Days	519.86	483.98	597.59	542.09	689.39
Accounts Payables Days	225.93	143.32	115.34	98.73	111.04
ROIC (%)	12.0%	12.4%	15.4%	35.8%	42.5%
ROCE (%)	12.0%	11.4%	14.4%	32.1%	32.0%
Return On Average Assets	13.3%	12.6%	15.5%	32.2%	32.4%

Key Drivers					
	Mar-20A	Mar-21A	Mar-22F	Mar-23F	Mar-24F
Unit sales grth (% , main prod./serv.)	(8.6%)	7.2%	22.4%	66.7%	14.3%
R&D Cost/sales(%)	8.6%	7.8%	8.0%	6.0%	6.0%

SOURCES: INCRED RESEARCH, COMPANY REPORTS

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Corporate Governance Report of Thai Listed Companies (CGR). CG Rating by the Thai Institute of Directors Association (Thai IOD) in 2021, Anti-Corruption 2021

ADVANC – Excellent, Certified, **AMATA** – Excellent, Certified, **ANAN** – Excellent, n/a, **AOT** – Excellent, n/a, **AP** – Excellent, Certified, **ASP** – Excellent, n/a, **AWC** – Excellent, Declared, **AU** – Good, n/a, **BAM** – Very Good, Certified, **BAY** – Excellent, Certified, **BBL** – Excellent, Certified, **BCH** – Very Good, Certified, **BCP** – Excellent, Certified, **BCPG** – Excellent, Certified, **BDMS** – Excellent, n/a, **BEAUTY** – Good, n/a, **BEM** – Excellent, n/a, **BH** – Good, n/a, **BJC** – Very Good, n/a, **BLA** – Very Good, Certified, **BTS** – Excellent, Certified, **CBG** – Very Good, n/a, **CGET** – n/a, n/a, **CENEL** – Excellent, Certified, **CHAYO** – Very Good, n/a, **CHG** – Very Good, n/a, **CK** – Excellent, n/a, **COM7** – Excellent, Certified, **CPALL** – Excellent, Certified, **CPF** – Excellent, Certified, **CPN** – Excellent, Certified, **CPNREIT** – n/a, n/a, **CRC** – Excellent, Declared, **DELTA** – Excellent, Certified, **DDD** – Excellent, n/a, **DIF** – n/a, n/a, **DOHOME** – Very Good, Declared, **DREIT** – n/a, n/a, **DTAC** – Excellent, Certified, **ECL** – Excellent, Certified, **EGCO** – Excellent, Certified, **EPG** – Excellent, Certified, **ERW** – Very Good, Certified, **GFPT** – Excellent, Certified, **GGC** – Excellent, Certified, **GLOBAL** – Excellent, n/a, **HANA** – Excellent, Certified, **HMPRO** – Excellent, Certified, **HUMAN** – Good, n/a, **ICHI** – Excellent, Certified, **III** – Excellent, Declared, **INTUCH** – Excellent, Certified, **IRPC** – Excellent, Certified, **ITD** – Very Good, n/a, **IVL** – Excellent, Certified, **JASIF** – n/a, n/a, **JKN** – n/a, Certified, **JMT** – Very Good, n/a, **KBANK** – Excellent, Certified, **KCE** – Excellent, Certified, **KEX** – Very Good, Declared, **KKP** – Excellent, Certified, **KSL** – Excellent, Certified, **KTB** – Excellent, Certified, **KTC** – Excellent, Certified, **LH** – Excellent, n/a, **LPN** – Excellent, Certified, **M** – Very Good, Certified, **MAKRO** – Excellent, Certified, **MC** – Excellent, Certified, **MEGA** – Very Good, n/a, **MINT** – Excellent, Certified, **MTC** – Excellent, Certified, **NETBAY** – Very Good, n/a, **NRF** – Very Good, Declared, **OR** – Excellent, n/a, **ORI** – Excellent, Certified, **OSP** – Excellent, n/a, **PLANB** – Excellent, Certified, **PRINC** – Very Good, Certified, **PR9** – Excellent, Declared, **PSH** – Excellent, Certified, **PTT** – Excellent, Certified, **PTTEP** – Excellent, n/a, **PTTGC** – Excellent, Certified, **QH** – Excellent, Certified, **RAM** – n/a, n/a, **RBF** – Very Good, n/a, **RS** – Excellent, Declared, **RSP** – Good, n/a, **S** – Excellent, n/a, **SAK** – Very Good, Declared, **SAPPE** – Very Good, Certified, **SAWAD** – Very Good, n/a, **SCB** – Excellent, Certified, **SCC** – Excellent, Certified, **SCGP** – Excellent, Declared, **SECURE** – n/a, n/a, **SHR** – Excellent, n/a, **SIRI** – Excellent, Certified, **SPA** – Very Good, n/a, **SPALI** – Excellent, Certified, **SPRC** – Excellent, Certified, **SSP** – Good, Certified, **STEC** – Excellent, n/a, **SVI** – Excellent, Certified, **SYNEX** – Very Good, Certified, **TCAP** – Excellent, Certified, **THANI** – Excellent, Certified, **TIDLOR** – n/a, Certified, **TISCO** – Excellent, Certified, **TKN** – Very Good, n/a, **TOP** – Excellent, Certified, **TRUE** – Excellent, Certified, **TTB** – Excellent, Certified, **TU** – Excellent, Certified, **TVO** – Excellent, Certified, **VGI** – Excellent, Certified, **WHA** – Excellent, Certified, **WHART** – n/a, n/a, **WICE** – Excellent, Certified, **WORK** – Good, n/a.

- CG Score 2021 from Thai Institute of Directors Association (IOD)

- Companies participating in Thailand's Private Sector Collective Action Coalition Against Corruption programme (Thai CAC) under Thai Institute of Directors (as of August 5, 2021) are categorised into: companies that have declared their intention to join CAC, and companies certified by CAC.

Recommendation Framework

Stock Ratings

Definition:

Add	The stock's total return is expected to exceed 10% over the next 12 months.
Hold	The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
Reduce	The stock's total return is expected to fall below 0% or more over the next 12 months.

The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.

Sector Ratings

Definition:

Overweight	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

Country Ratings

Definition:

Overweight	An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
Neutral	A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
Underweight	An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.