India

Neutral *(no change)*

Highlighted Companies

Sun Pharmaceutical Industries
ADD, TP Rs1095, Rs995 close
Long growth runway for specialty products.

Torrent Pharmaceuticals Ltd
ADD, TP Rs2135, Rs1868 close
Margins have more levers to expand.

Aurobindo Pharma
ADD, TP Rs793, Rs721 close
Improving product mix in the US

Summary Valuation Metrics

P/E (x)	Mar23-A	Mar24-F	Mar25-F
Sun Pharmaceutical Industries	28.17	26.67	22.48
Torrent Pharmaceuticals Ltd	50.77	38.39	38.39
Aurobindo Pharma	21.93	17.18	17.18

P/BV (x)	Mar23-A	Mar24-F	Mar25-F
Sun Pharmaceutical Industries	4.26	3.84	3.84
Torrent Pharmaceuticals Ltd	10.2	8.9	8.9
Aurobindo Pharma	1.57	1.47	1.47

Dividend Yield	Mar23-A	Mar24-F	Mar25-F
Sun Pharmaceutical Industries	1.16%	1.16%	1.16%
Torrent Pharmaceuticals Ltd	1.18%	0.8%	0.8%
Aurobindo Pharma	1.04%	0.83%	0.83%

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Pharmaceuticals

Margin recovery to support outperformance

- Improved near-term US generics macroeconomic environment and margin recovery should support near-term outperformance, although valuations of some companies are now approaching the exuberance zone.
- Indian companies better positioned now (vs. the past) to tackle the challenges backed by a leaner business model, portfolio optimization, better leverage position and an improving branded market presence in the overall mix.
- Stay selective. We prefer companies with strong India/branded market presence, robust manufacturing capabilities and a track record in complex generics in the US market. Top picks: SUNP, TRP & ARBP.

FY24F should be a strong year for the industry

After a challenging FY23, FY24F is likely to be a strong year for the industry, as elevated inventory level in the channel normalizes in the US, logistic cost declines and high-cost raw material inventory depletes. The US generics macroeconomic environment has improved too, given high shortage/competitor exits, although we believe the opportunity will be short-lived and limited to a few players. We expect the companies under our coverage to post an earnings CAGR of 13% over FY23-25F, driven by a stable domestic/branded market, relatively stable US pricing, specialty launches, continued traction in gRevlimid and margin improvement. News flow on the USFDA audits of plants would be a key monitorable as these can drive a meaningful upside/ downside to estimates.

US generics macro improving, but benefits limited to a few players

Despite some indications of stability in the current pricing environment, it's important to acknowledge that the benefits have been limited and primarily favoured specific players like Aurobindo Pharma, rather than being widespread. Industry commentary suggests that high single-digit price erosion is likely to persist. In the past, portfolio rationalization efforts by major companies did not lead to significant advantages for incumbents, as newer entrants displayed aggressive strategies. Additionally, compliance challenges faced by large players like Sun Pharma further impede their ability to fully capitalize on the prevailing trends.

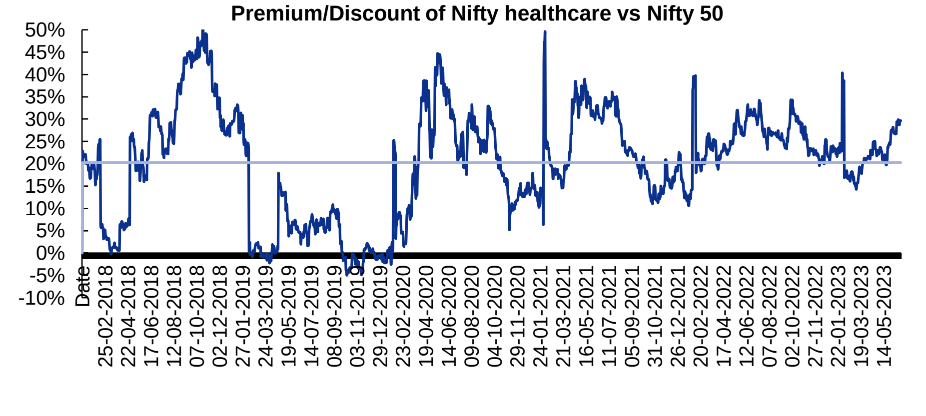
Improving mix with a higher share of India/branded markets

The share of India/other branded markets and specialty complex products in the US is gradually going up in the overall revenue mix, thereby reducing the dependance on the US generics segment and ensuring consistency in earnings with better profitability margins. Especially, we note a renewed aggression in the domestic market, with most companies expanding their medical representative or MR strength in recent times and expanding into hitherto untapped areas like trade generics and consumer health business.

Valuations and outlook

The sector's outperformance (200bp vs. Nifty) so far in FY24 has pushed the valuations of some companies into the exuberance zone. The average sector premium is now at 30% (vs. 5-year average of 20%). We, thus, stay selective. Top picks: Sun Pharma, Torrent Pharma and Aurobindo Pharma.

Figure 1: Nifty Pharma now trades at a 30% premium to Nifty versus a five-year mean of 20%, but still far away from 45-50% witnessed during the Covid-19 pandemic



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 2: Our healthcare sector coverage universe

Company	Bloomberg Ticker	Rec	MktCap (US$bn)	Price	Target Price	Up/down (%)	EPS			PER (x)			P/Bk (x)			EV/EBITDA (x)			ROE			ROCE		
							FY23A	FY24F	FY25F	FY23A	FY24F	FY25F	FY23A	FY24F	FY25F	FY23A	FY24F	FY25F	FY23A	FY24F	FY25F	FY23A	FY24F	FY25F
Ajanta Pharma Ltd	AJP IN	HOLD	2.6	1,472	1,515	2.9%	45.9	56.7	63.4	32.1	25.9	23.2	5.6	4.7	4.0	22.9	17.7	15.3	17.7%	19.6%	18.5%	19.6%	22.9%	21.9%
Alkem Laboratories Ltd	ALKEM IN	HOLD	5.6	3,402	3,542	4.1%	82.3	124.6	147.7	41.3	27.3	23.0	4.5	4.1	3.6	24.3	19.7	16.6	12.0%	15.7%	16.7%	11.7%	14.7%	15.6%
Aurobindo Pharma	ARBP IN	ADD	5.8	721	793	9.9%	32.9	42.0	50.5	21.9	17.2	14.3	1.6	1.5	1.3	10.8	8.6	7.2	7.5%	8.8%	9.8%	8.5%	10.3%	11.6%
Divi's Laboratories	DIVI IN	HOLD	12.9	3,534	3,487	-1.3%	68.6	73.1	91.8	51.5	48.4	38.5	7.3	6.7	5.9	37.8	31.6	25.0	14.9%	14.5%	16.4%	16.5%	18.2%	20.8%
Dr Reddy's Laboratories Ltd	DRRD IN	REDUCE	11.6	5,042	4,656	-7.6%	270.8	248.0	263.8	18.6	20.3	19.1	3.6	3.2	2.8	12.3	12.4	11.3	21.4%	16.8%	15.7%	21.9%	19.0%	17.3%
Gland Pharma Ltd	GLAND IN	HOLD	2.3	1,021	1,056	3.4%	47.4	55.6	62.6	21.5	18.4	16.3	2.1	1.9	1.7	12.7	11.3	9.5	10.9%	10.9%	11.0%	11.6%	12.3%	12.0%
Laurus Labs	LAURUS IN	REDUCE	2.7	362	263	-27.3%	14.7	9.7	13.3	24.7	37.4	27.3	4.8	4.5	3.9	13.4	17.3	13.9	21.4%	12.4%	15.4%	22.8%	13.9%	16.2%
Sun Pharmaceutical Industries	SUNP IN	ADD	32.9	995	1,095	10.1%	35.3	37.3	43.7	28.2	26.7	22.8	4.3	3.8	3.4	19.8	17.7	15.2	16.6%	15.1%	15.9%	15.7%	15.1%	16.0%
Torrent Pharmaceuticals Ltd	TRP IN	ADD	8.7	1,868	2,135	14.3%	36.8	48.6	57.9	50.8	38.4	32.3	10.2	8.9	7.4	23.8	20.3	17.6	20.5%	24.8%	25.0%	19.8%	22.1%	24.7%
Zydus Lifesciences	ZYDUSLIF IN	REDUCE	7.8	562	517	-8.0%	19.4	27.4	29.6	28.9	20.5	19.0	3.2	2.9	2.6	15.0	13.7	12.3	14.1%	14.9%	14.4%	14.2%	15.8%	15.7%

PRICES AS ON 26TH JUN 2023
SOURCE: INCRED RESEARCH, COMPANY REPORTS

US generics market recovery is structural or cyclical?

The US journey of Indian pharmaceutical players can be broadly divided into four distinct phases. From 2005 to 2010, major Indian companies made substantial investments in their US plants and R&D, thereby impacting their return ratios. They also focused on establishing strong relationships with distributors. The period between 2011 and 2015 witnessed a significant growth for Indian generic players, driven by expiring product patents. Margins expanded as operating leverage and higher capacity utilization improved the return ratios. However, from 2016 to 2019, intense competition and customer consolidation resulted in sharp price erosion. The US Food and Drug Administration or USFDA introduced guidelines that shortened product approval timeline, causing challenges for incumbents. Compliance issues also arose, impacting growth. To address these challenges, generic players underwent portfolio rationalization, exited economically unviable products, and focused on cost-control measures.

From 2019 to 2021, as larger players exited unviable products, prices began to stabilize, reducing average price erosion from 15-20% to high single digits. Additionally, the Covid-19 pandemic shifted distributor negotiations towards supply consistency rather than demanding lower pricing, further supporting pricing dynamics in the market. Throughout these phases, Indian pharmaceutical companies adapted their strategies to navigate changing market conditions and optimize their portfolios, focusing on cost efficiency to ensure growth and profitability.

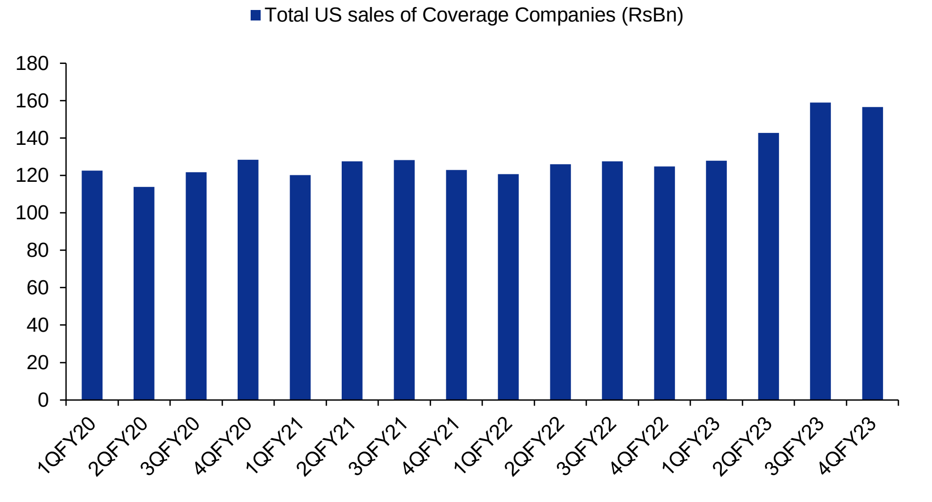
Post Covid-19 pandemic, US generic (Gx) players found themselves grappling with elevated inventory levels, necessitating the disposal of stock at reduced prices as its shelf-life approached expiry. This further intensified pricing pressure throughout the first half of FY23. However, in the past six months, there have been encouraging indications of stability emerging in the US Gx pricing landscape. Several factors have contributed to this trend, such as another round of market exits as well as bankruptcy filings by some players, and a few grappling with non-compliance issues leading to supply disruption. Consequently, a surge in product shortage instilled a sense of rationality in pricing. The crucial question now remains as to whether the current pricing dynamics prove to be sustainable or transient in nature.

Figure 3: List of players existing/ pulling out their products from the US market in recent times

Impacted player	Reason
Teva Pharmaceuticals	Pulled out large part of its products from US market around 2018-19.
Purdue Pharma	Filed for bankruptcy due to lawsuits from around the country related to its marketing of Oxycontin.
Insys Therapeutics	Filed for bankruptcy in 2019. Insys went to trial for accusations that the company gave kickbacks to doctors who prescribed the company's powerful fentanyl spray, Subsys, to patients who didn't necessarily need it.
Novum Pharma	Price hike, bad press and having coverage dropped by insurance companies created a financial hole.
Akorn Pharmaceuticals	Regulatory and financial troubles.
Endo International	Opioid litigation and scrutiny from FDA.
Lannet Pharmaceuticals	High debt.
Mallinckrodt	High debt.
Teligent	Failed USFDA inspection and product recall.
Intas Pharma	Import alert on Metoda plant led to disruption in injectable supplies.
Sun Pharma	Import alert on Halol plant led to disruption in supplies.

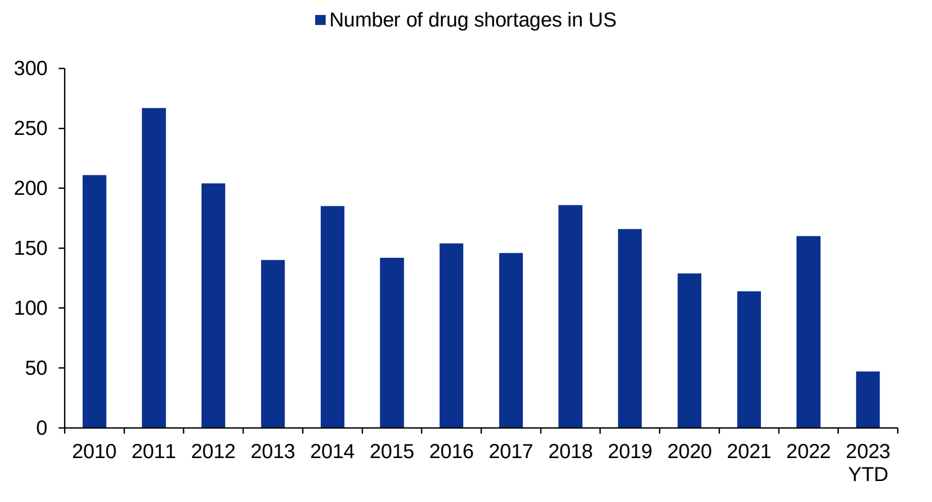
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 4: Cumulative US revenue of coverage companies – pick-up in 2HFY23 was largely on account of gRevlimid opportunity



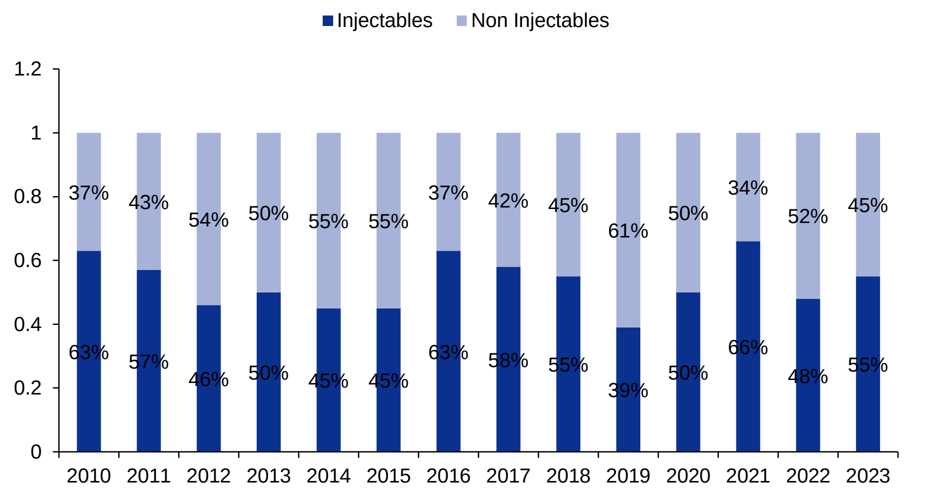
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 5: Number of drug shortages in the US market



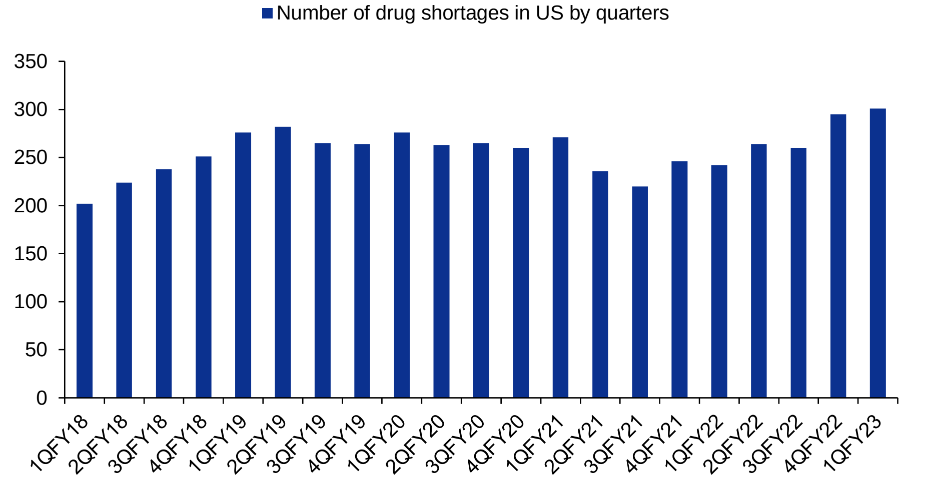
SOURCE: ASHP.ORG, INCRED RESEARCH, COMPANY REPORTS

Figure 6: Number of drug shortages - injectables and non-injectables in the US market



SOURCE: ASHP.ORG, INCRED RESEARCH, COMPANY REPORTS

Figure 7: Number of drug shortages in the US market by quarters



SOURCE: ASHP.ORG, INCRED RESEARCH, COMPANY REPORTS

Despite some indications of stability in the current pricing environment, it's important to acknowledge that the benefits have been limited and have primarily favoured specific players like Aurobindo Pharma or ARBP, rather than being widespread. The current improvements are primarily driven by exclusive opportunities for certain products, with gRevlimid being a notable example. Industry observations suggest that high single-digit price erosion is likely to persist.

It's worth noting that previous instances, such as in 2019, have demonstrated that portfolio rationalization efforts by major companies did not lead to significant advantages for incumbents, as newer entrants deployed aggressive strategies. Additionally, compliance challenges faced by prominent Indian players like Sun Pharma or SUNP further impede their ability to fully capitalize on prevailing trends.

Structurally, there are no anticipated substantial changes in US pricing trends, and the generics market there is expected to maintain its flat-to-declining trajectory due to a combination of volume growth and price declines. This presents a challenging landscape for industry players, requiring them to navigate through a market environment characterized by limited pricing improvement.

Figure 8: Commentaries from industry leaders suggest that while price erosion has abated versus FY23, it is still expected to be in high single digits

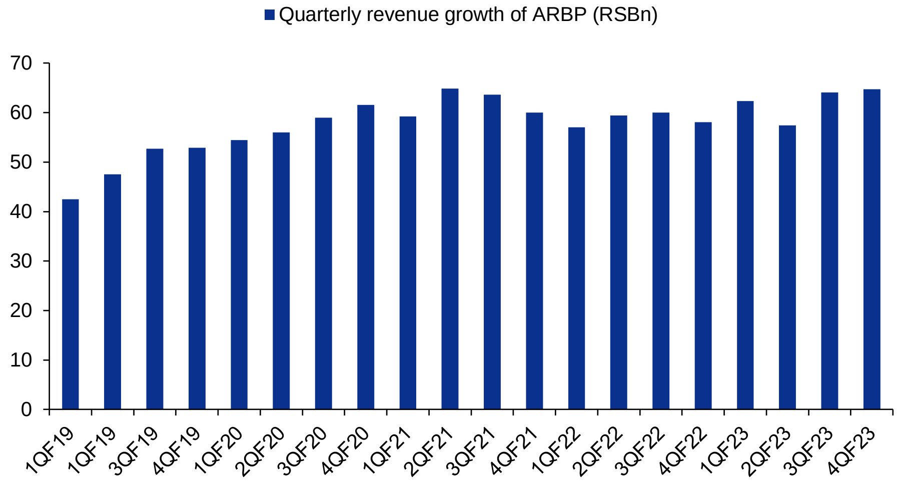
Price erosion as guided by companies in 4QFY23

Companies	Commentary
AJP	Stabilized and down to high single digit.
ARBP	On a yoy basis, in the first three quarters, we had a fair amount of price erosion, and then the fourth quarter was somewhat stable.
DRL	Price erosion was lower in this quarter as compared to previous quarters.
SUNP	Price stabilization not seen just from Sun Pharma's perspective, but also from an industry perspective.
ZYUSLIF	Mid- to high single-digit price erosion.

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Meanwhile, Aurobindo Pharma has emerged as a standout performer, leveraging an aggressive filing strategy, broad product portfolio, cost-effective manufacturing setup, strong compliance record (excluding one plant under watchlist), and a robust supply chain which has been positioned to substantially benefit from product shortage in the market.

Figure 9: Revenue of Aurobindo Pharma seems to have stabilized in the past two quarters, reflecting the benefits of the current US pricing situation



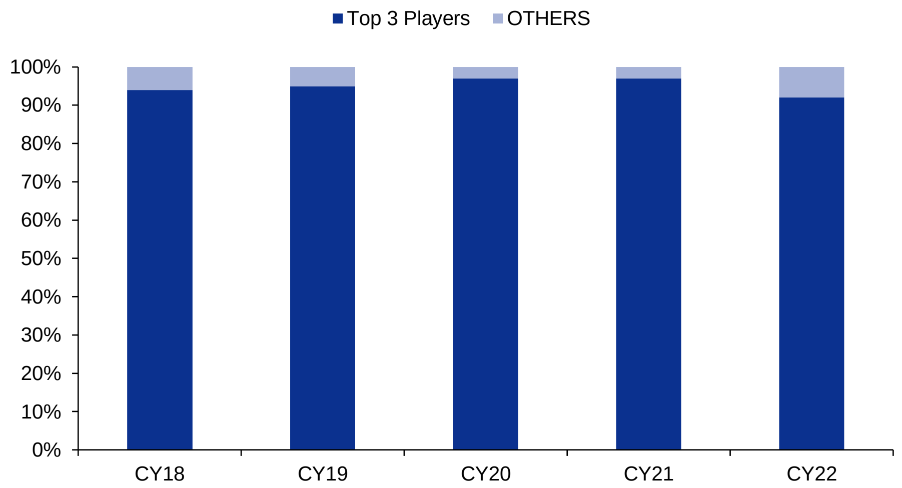
SOURCE: INCRED RESEARCH, COMPANY REPORTS

What are the factors ailing the US Gx market?

Customer consolidation

Three major buyers, namely Walgreens Boots Alliance Development (WBAD), Red Oak, and ClaurusONE, hold a dominant position, accounting for over 90% of drug distribution in the US market. Their consolidated purchasing power and negotiating strength had a notable impact on US generic pricing. The consolidated buyers can demand more competitive pricing terms from generic drug manufacturers, leading to intensified price competition and lower prices for generic drugs. Barring an event like the Covid-19 pandemic, where product availability takes precedence over pricing, we believe generic players will continue to be price-takers.

Figure 10: US distribution channel dominated by top-3 players



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Implementation of GDUFA

The implementation of GDUFA-1 in 2012 had a profound impact on the generics market, significantly accelerating the approval process and triggering deflationary pressure. In the first five years of the GDUFA program (2013-2017), the USFDA approved 2,829 new generic drugs, marking a substantial 21% increase compared to the 2008-2012 period.

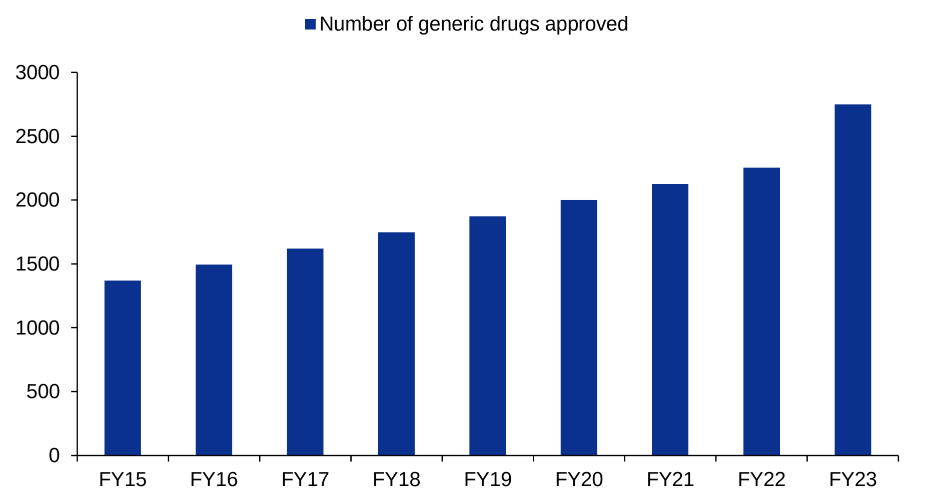
The pace of approval for subsequent generics was even more rapid, leading to substantial price erosion, particularly following the approval of the third and fourth players in a specific generic category. On an average, the price of the second generic launch was discounted by 50% compared to the brand, while the third and fourth launches experienced discounts of 75% and 90%, respectively.

The impact of GDUFA on Indian companies became apparent in 2015, after the clearance of backlogged applications and the USFDA's priority review of second and third generics.

Established Indian players such as Sun Pharma, Zydus, and Dr. Reddy's Labs suffered significant setbacks due to the implementation of GDUFA (The Generic Drug User Fee Act). However, not all companies were disadvantaged by the situation.

Late entrants to the US market, including Torrent Pharma, Alkem and Caplin benefited from the expedited approvals, allowing them to scale up more quickly. It is worth noting that the total number of exclusive first generics remained relatively stable, ranging from 72 to 102 ANDAs (abbreviated new drug applications) between 2015 and 2020. The inability of Indian companies to fully capitalize on these approvals can be attributed to deficiency in their applications and regulatory issues at their manufacturing plants.

Figure 11: Generic drug approvals increase every year post implementation of GDUFA



SOURCE: FDA.GOV, INCRED RESEARCH, COMPANY REPORTS

Non-compliance at manufacturing plants dents growth further

Along with sharp price erosion, Indian companies have also been reeling under heightened compliance issues with the USFDA. India has the highest number of USFDA-approved plants outside the US and, therefore, witnessed more intense scrutiny vis-à-vis other countries. While the inspections halted briefly during the Covid-19 pandemic due to travel restrictions, they have resumed in full swing in the last one year, with priority accorded to plants under compliance issues and ready for re-inspection. This can prove to be either a boon or bane – a successful re-inspection of plants with compliance issues will pave the way for faster approval of stuck product filings; however, plants which are currently clear may draw the USFDA's observations if compliance is found not up to the mark. So far, the results have been mixed – while Zydus Lifesciences have cleared their Moraiya plant, others like Sun Pharma/Intas/Glenmark Pharma (with import alerts) have been pulled up for non-compliance at their plants. To de-risk, companies are now filing products from dual sites or doing site transfers for their large products.

Figure 12: Indian pharma companies' facilities facing USFDA problems

Company	Facility	Status
Sun Pharma	Halol, Gujarat	Import alert
Sun Pharma	Mohali	Under consent decree
Aurobindo Pharma	Aurobindo Pharma's Unit I, Telangana	Warning letter
Aurobindo Pharma	Aurobindo Pharma's Unit IX, Telangana	OAI
Aurobindo Pharma	Dayton, USA	Warning letter
Torrent Pharma	Indrad plant, Gujarat	Warning letter
Torrent Pharma	Dahej plant	OAI
Glenmark	Goa	Warning letter
Glenmark	Baddi	Import Alert
Glenmark	Monroe, USA	OAI

SOURCE: INCRED RESEARCH, COMPANY REPORTS

In response, companies are moving up the value chain

Amid the sharp price decline and regulatory challenges in the US market, Indian companies are strategically focusing on scaling up their product offerings with increased complexity. This involves allocating more resources towards areas such as injectables, oncology, hormones, and respiratory products, which face barriers related to complexity, manufacturing, or technology. Encouraging progress has already been made by companies like Dr. Reddy's Labs, Aurobindo Pharma, and Sun Pharma in injectables, and specialty portfolios.

These efforts reflect a positive direction for Indian companies, with Sun Pharma specifically aiming to bolster its global specialty franchise through significant capital allocation. Zydus has also outlined plans for increased investments in its innovation portfolio, while Dr. Reddy's Labs is shifting its capital allocation away from the specialty business towards aggressive investments in India and non-US markets like China. Additionally, Aurobindo Pharma is strengthening its injectables and biosimilars franchise while committing significant capital to the active pharmaceutical ingredient or API segment.

These product expansions not only diversify companies' portfolios but also serve as a safeguard against margin erosion in the commodity segment, thanks to lower competition and higher profitability associated with these complex offerings.

Figure 13: Companies present in various complex filings

	Complex Injectables	Biosimilars	Penem	Peptides
Alkem Pharma	N	Y	N	Y
Aurobindo Pharma	Y	Y	Y	Y
Dr Reddy's Labs	Y	Y	N	Y
Gland Pharma	Y	Y	Y	Y
Sun Pharma	Y	Y	N	Y
Zydus Lifesciences	Y	Y	N	N

NOTE-Y-YES, N-NO.
SOURCE: INCRED RESEARCH, COMPANY REPORTS

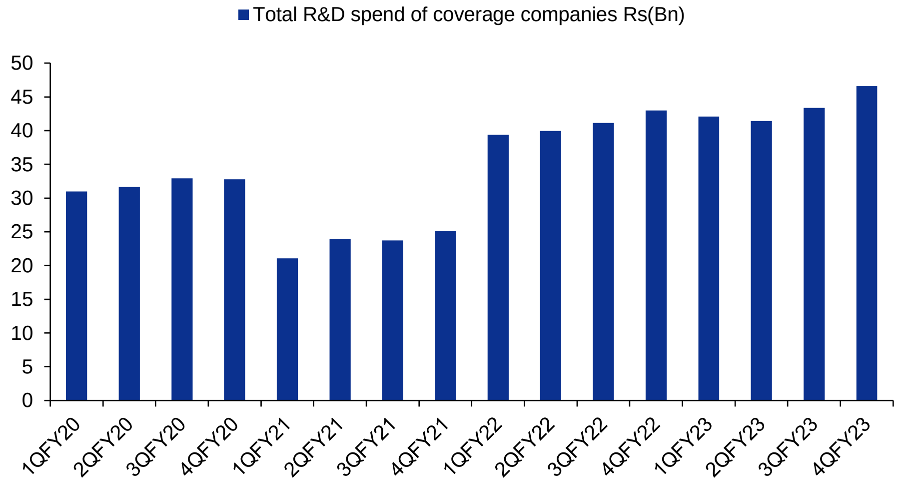
Moving towards leaner cost models

Prior to the Covid-19 pandemic, Indian pharma industry embarked on a balance sheet clean-up mission, reducing debt, optimizing costs, and divesting non-core assets and products. This departure from the past reflects a shift from the constraints of leveraged balance sheets and profitability pressure that hindered decision-making capabilities.

In the current cycle, there is a clear emphasis on strategic capital allocation, with companies focusing on their R&D strengths and investing in assets and markets that offer sustained growth opportunities. This approach provides them with greater flexibility to pursue organic and inorganic strategic options for medium- to long-term growth.

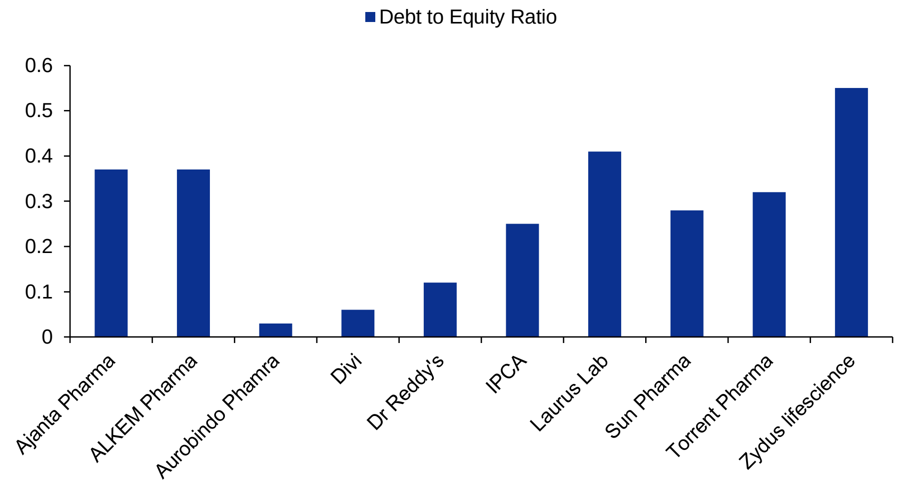
Today, the pharma sector is in a significantly improved state compared to a few years ago, with a stronger foundation. While robust earnings remain crucial for sustaining momentum, the industry's transformation has positioned it for a brighter future.

Figure 14: R&D spending is increasing largely due to investments in complex generics/specialty segment



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 15: Current leverage position is very comfortable and allows flexibility to undertake opportunistic acquisitions



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 16: Divestment of non-core assets by coverage companies in the past three years

Asset	Company	Date of Sale	Amount (Rsm)
Divestment of dietary supplements business Natrol.	Aurobindo	2022	
Divested some of the brands belonging to proprietary products, a few from India and a few from EMs.	Dr Reddy's	2022	
Sold CDMO division of custom pharmaceutical service.	Dr Reddy's	2022	4,772
In proprietary products business, sold US and select territory rights for the commercialized portfolio of dermatology and neurology therapies that were being marketed in the US by Dr. Reddy's Labs.	Dr Reddy's	2021	
Sold US and selected territory rights of commercialized neurology products of the proprietary products (PP) business.	Dr Reddy's	2020	
Sold one of its API manufacturing business units located at Jeedimetla in Hyderabad to Therapiva Private Limited.	Dr Reddy's	2020	
Divestment of entire interests of the company in Kyowa Pharmaceuticals, Japan.	Dr Reddy's	2020	
Sold animal healthcare emerging market business.	Zydus Lifesciences	2021	29,210

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 17: Inorganic acquisitions done by pharma companies in recent times

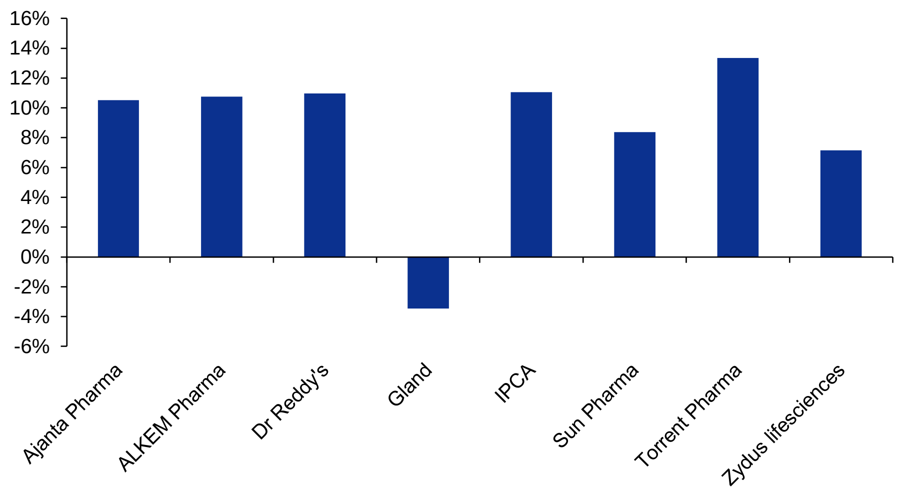
Date	Deal	Seller / out-licensor	Buyer / in-licensor	Type of deal	Consideration paid upfront
Dec-22	JB Chemicals- Glenmark deal	Glenmark	JB Chemicals	Business buyout	3,140 Rsm
Sep-22	Torrent-Curatio deal	Curatio	Torrent Pharmaceuticals	Company buyout	20,000 Rsm
Jun-22	JB Chemicals-Dr. Reddy's deal	Dr. Reddy's	JB Chemicals	Product buyout	980 Rsm
May-22	Eris- Oaknet healthcare	Oaknet Heakthcare	Eris	Company buyout	6,500 Rsm
Apr-22	JB Chemicals-Novartis deal	Novartis	JB Chemicals	Product buyout	2,460 Rsm
Mar-22	Dr Reddy's-Novartis deal	Novartis	Dr. Reddy's	Product buyout	4,560 Rsm
Jan-22	JB Chemicals- Sanzyme deal	Sanzyme	JB Chemicals	Product buyout	6,280 Rsm
Dec-21	Eris- MJ Biopharm Pvt. Ltd.			Joint venture (product licensing)	-
Sep-21	Citius Pharmaceuticals-Dr Reddy's deal	Dr. Reddy's	Citius Pharmaceuticals	Product buyout	40mUD$
Aug-20	JB Chemicals-Lekar Pharma deal	Lekar Pharma	JB Chemicals	Business buyout	85Rsm
Jun-20	Dr Reddy's-Wockhardt deal	Wockhardt	Dr. Reddy's	Product buyout	15,500 Rsm
Dec-19	Eris-Novartis deal	Novartis	Eris	Product buyout	13mUD$
Jan-18	Dr Reddy's- UCB deal	UCB	Dr. Reddy's	Business buyout	8,000 Rsm
Nov-17	Torrent-Unichem deal	Unichem	Torrent Pharmaceuticals	Business buyout	36,000 Rsm
Dec-14	Torrent- Elder deal	Elder	Torrent Pharmaceuticals	Business buyout	2,0040 Rsm

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Domestic formulations shine amid challenges

The domestic formulations business, valued at ~US$24bn, stands as a cornerstone of the Indian generics industry and ranks among the world's most rapidly expanding markets, with an annual growth rate of 9-10%. For most Indian companies, a robust domestic business, contributing 35-40% to their revenue, has served as a stabilizing force, bolstering their earnings and facilitating investments overseas. Notably, this market primarily consists of branded generics, offering elevated profitability with margins of 25-50%, high asset turns, low working capital and high ROCEs. As regulated markets witnessed a reversal in the growth trend from FY15, the domestic formulations business emerged as a silver lining for these companies.

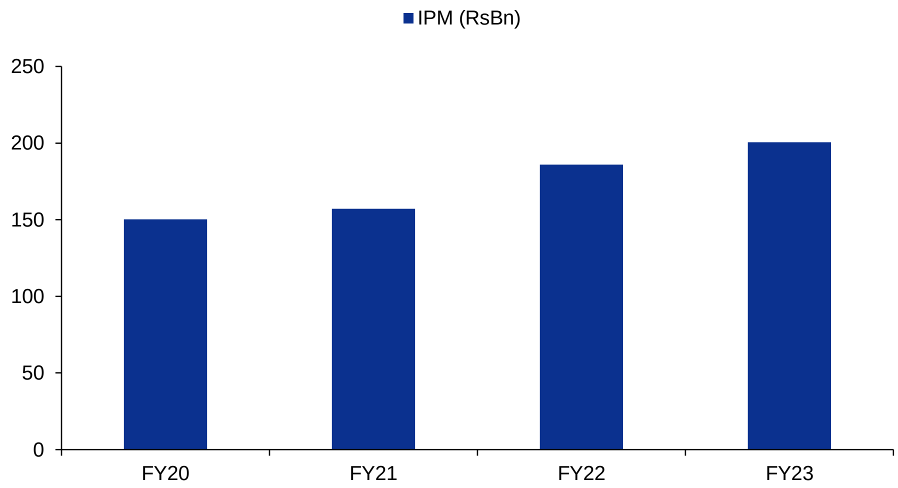
Figure 18: CAGRs of leading domestic players from FY16 to FY23



SOURCE: INCRED RESEARCH, COMPANY REPORTS

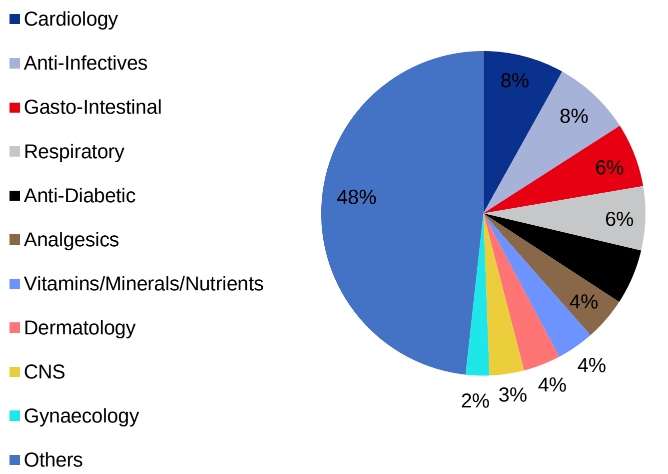
The IPM (Indian Pharmaceutical Market) has navigated through a series of formidable challenges over the FY15-21 period, including disruptive events like demonetization, Goods and Services Tax or GST implementation, price controls, and Covid-induced lockdowns, all of which hampered growth. Despite these obstacles, the industry has demonstrated remarkable resilience, achieving a commendable 9% compounded annual growth rate (CAGR) during the period.

Figure 19: IPM growth has been consistent between 8-10%



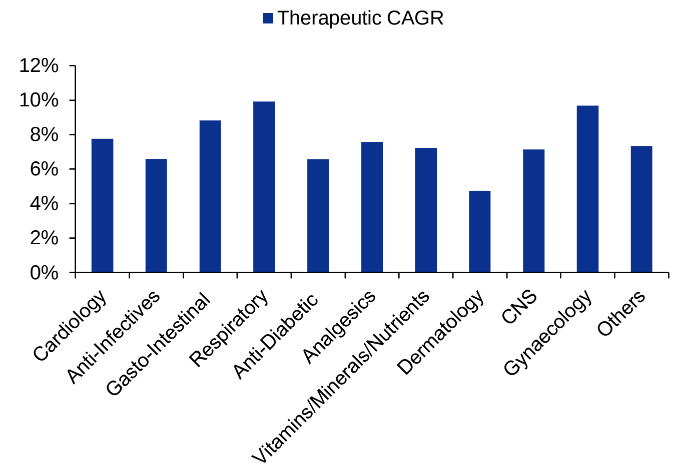
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 20: Therapy-wise revenue break-up in IPM – Market dominated by acute therapies, but chronic therapies fast catching up



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 21: Therapy-wise CAGRs of the past four years in IPM



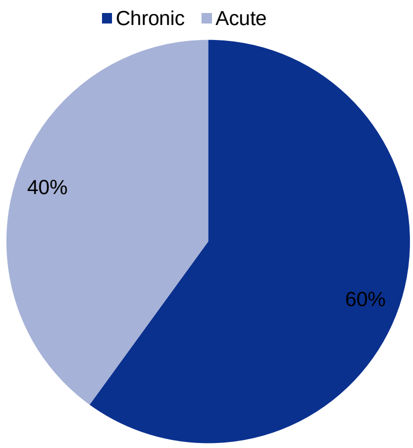
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Notably, India-focused companies have surpassed not only the Nifty Index but also their pharmaceutical peers over the past five years, demonstrating their superior performance. Companies with a greater proportion of EBITDA derived from the Indian market, such as IPCA Labs and Alkem Labs, have notably reported higher Return on Capital Employed (RoCE) compared to their export-oriented counterparts. This consistent outperformance of the IPM by India-focused companies has played a crucial role in mitigating the challenges faced in regulated markets.

Navigating change: The gradual transformation towards chronic therapies

In recent years, chronic therapies have exhibited remarkable growth, outperforming the acute segment by a notable margin of 200-300bp compared to the industry average. Although the gap between the two is narrowing, acute and sub-chronic therapies consistently maintain a substantial market share of 67-68% in IPM sales. Despite this trend, most new product launches continue to target the chronic segment. This strategic emphasis is driven by the intense competition and lower price realization typically associated with the acute segment, incentivizing companies to prioritize the chronic market. Notably, the chronic segment has long been dominated by a select group of formidable players, including Sun Pharma and Torrent Pharma.

Figure 22: Chronic-acute mix in IPM in FY23



SOURCE: INCRED RESEARCH, COMPANY REPORTS

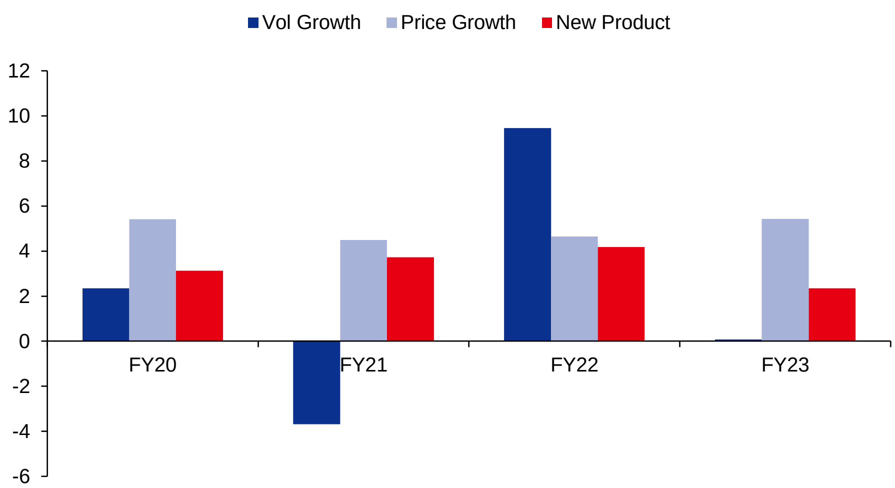
Given the advantages of better price realization, enhanced sales force productivity (with a leaner sales force often required for chronic therapies, primarily targeting urban areas), and greater revenue sustainability, pharmaceutical companies are diligently working towards optimizing their product mix. This is being achieved through strategic initiatives such as in-licensing, acquisitions, and in-house product development, with the aim of enhancing their market position and driving long-term growth.

While we acknowledge the mounting competition in the chronic segment from new market entrants and the influence of e-pharmacies, we remain optimistic about its long-term growth prospects. This optimism stems from ongoing lifestyle and demographic changes that are poised to drive sustained demand within the segment.

Price hikes power IPM growth

With the three components of growth for pharma companies—volume, new product launch and price—it's clear that price growth has taken the lead as the primary catalyst. Volume growth's contribution to overall IPM has notably diminished, declining to 20% in Mar 2020 from 34% in Mar 2016 (and to 1% in Mar 2023, although FY21-23 data is erratic due to the Covid-19 pandemic), whereas price growth surged to 55% during the same period.

Figure 23: Domestic market growth drivers show price growth as the driving force in FY23



SOURCE: INCRED RESEARCH, COMPANY REPORTS

The slowdown in volume growth can be attributed to rising prominence of trade-generics and Jan Aushadhi medical stores in recent times. However, the impact of this deceleration has been counterbalanced by the robust performance of price growth. Going ahead, we expect the IPM to maintain a healthy annual growth rate of 9-10%, driven primarily by price hikes. It is noteworthy that only 18% of the IPM falls under price control regulations stipulated by the National List of Essential Medicines (NLEM), restricting price hikes to Wholesale Price Index (WPI) inflation levels. Consequently, the remaining 82% holds the potential for a maximum price hike of 10%.

MR productivity is a crucial performance metric

In the pharmaceutical industry, the performance of a company hinges on two critical factors: the size of its medical representative (MR) team and their productivity. A key metric used to gauge productivity is sales per MR, which is influenced by various factors, including the company's acute/chronic mix, therapy mix of its product offerings, portfolio size, and the pace of new product launches.

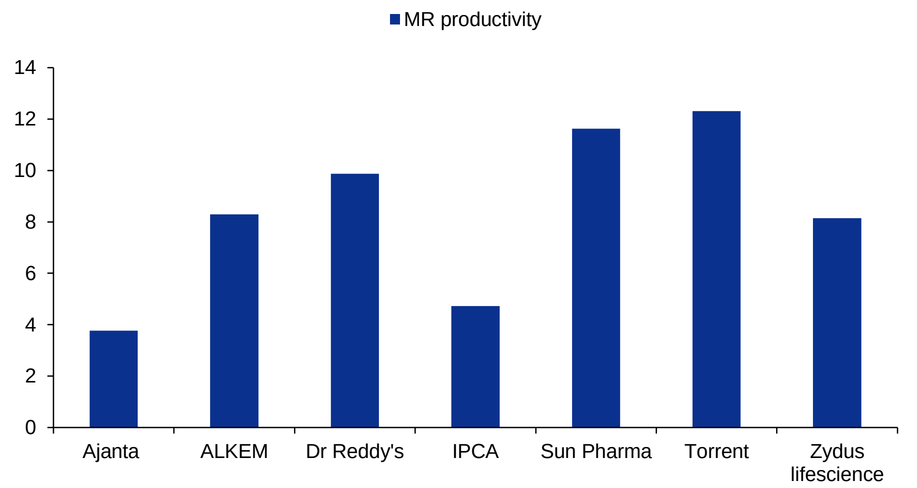
To understand the relationship between these factors and MR team productivity, we have analyzed the chronic/acute mix. Our findings reveal that companies with a higher contribution from chronic/sub-chronic products, such as Torrent Pharma and Sun Pharma, boasting an average revenue contribution of 69%, achieve exceptional MR productivity of Rs0.92m per month, setting the industry benchmark.

Figure 24: Comparing Eris and Abbott with Alkem Labs and Indoco Remedies (Rsm)

	Eris	Abbott	Alkem	Indoco
Chronic Revenue	15,672	33,697	57,997	3,504
Acute Revenue	1,180	19,790	57,997	13,182
Marketing Expenses	8%	10%	26%	25%

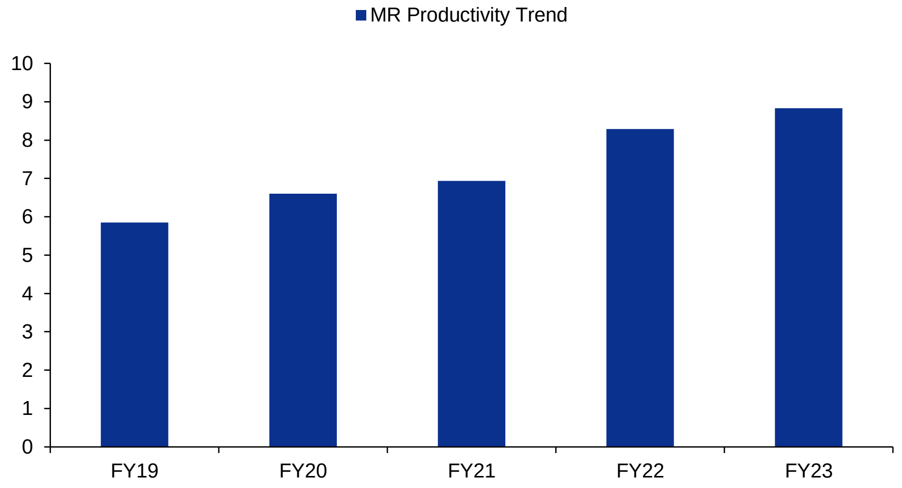
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 25: Medical representatives' productivity in India (per month)



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 26: Medical representatives' productivity trend for the past five years for the industry



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 27: Field force strength of companies

	Field force as of FY23-end
Ajanta Pharma	4,100
Alkem Labs	12,000
Sun Pharma	12,692
Torrent Pharma	5,500
Zydus Lifesciences	7,000

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Conversely, companies with a greater reliance on acute products, representing an average revenue contribution of 38% from chronic products, such as Indoco Remedies, Alkem Labs, Ipca Labs, and Alembic, experience significantly lower MR productivity, averaging Rs0.36m per month. However, there is a notable exception in the form of Ajanta Pharma. Despite generating 63% of its revenue from chronic/sub-chronic products, the company's MR productivity stands at Rs0.26m per month. This deviation can be attributed to its dominant position in the ophthalmology segment, where productivity levels inherently differ.

To summarize, the chronic/acute mix of a company's product portfolio plays a pivotal role in shaping the MR team's productivity, with those focusing on chronic/sub-chronic products consistently leading the industry in terms of performance.

With the domestic formulations segment offering substantial revenue opportunities, companies are actively positioning themselves to capitalize on this by further expanding their presence in this segment, adopting strategies such as augmenting their medical representative (MR) teams or pursuing inorganic growth opportunities.

Trade generics: Reshaping the volume landscape

Trade generics (Gx) represent a cost-effective alternative to branded drugs, offering the same active molecule but marketed under a different or nominal brand name. Unlike branded drugs, Gx products are directly supplied to distributors and retailers, bypassing the need for a dedicated field force. Retailers, in turn, promote these products to customers in pursuit of higher profit margins. This volume-centric segment operates on relatively lower profit margin for manufacturers, as Gx drugs are sold at a substantial discount compared to their branded counterparts.

Figure 28: Trade generics' business getting more prominent

Company Name	Trade generics revenue as % of total revenue
Alkem Labs	21%
Dr Reddy's Labs	Launched in 1QFY24
Torrent Pharma	Launched in 4QFY23

SOURCE: INCRED RESEARCH, COMPANY REPORTS

While sales through the Gx channel are not captured in IPM revenue, as the segment primarily targets tier-3 and tier-4 cities, industry estimates suggest that it accounts for around 5% of IPM value but potentially represents 25-30% of industry volume. A significant growth driver for this segment is the government's push through Jan Aushadhi stores, which further enhances its market potential.

Recognizing the robust growth potential in the Gx segment, many companies have shifted their focus towards it. For eg, Alkem Labs a major player in the industry, have witnessed Gx products accounting for 15-20% of its domestic sales. Ajanta Pharma, JB Chemicals, and Eris Lifesciences also have a presence in this segment, albeit with a lower revenue contribution.

As the Gx segment continues to witness strong growth, companies are increasingly directing their attention and resources towards capturing opportunities in this market. With its cost-effective appeal and expanding customer base, Gx presents an attractive avenue for growth and market expansion for pharmaceutical companies.

Emerging markets: India-like dynamics, currency plays a big role

Emerging markets (EMs) share similarities with the Indian market, as they primarily consist of branded generics markets driven by out-of-pocket expenses. These markets offer high profitability, require lower capital expenditure, and generate returns that are accretive. Key focus regions for Indian companies within EMs include Asian countries, LATAM, Africa, and Russia/CIS.

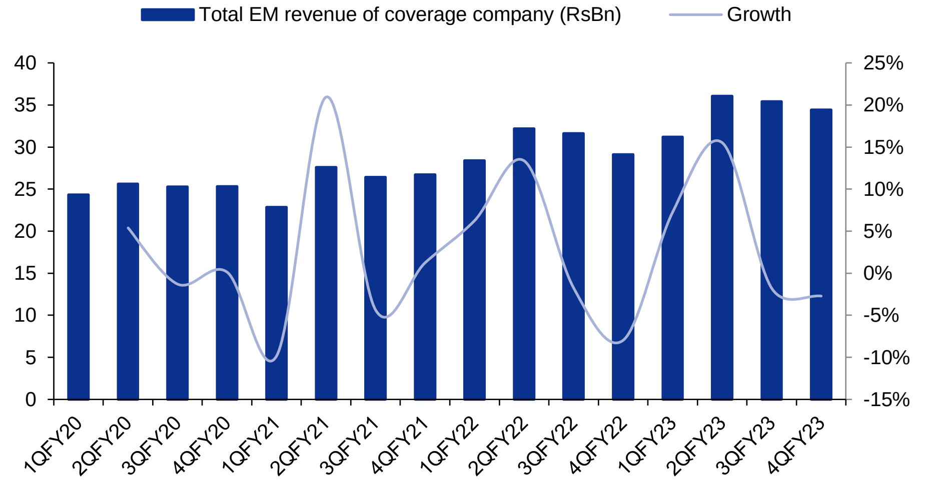
Indian companies, on an average, derived approximately 15% of their global sales in FY21 from these regions, experiencing a compounded annual growth rate (CAGR) of 8% from FY16 to FY21. Sun Pharma and Dr. Reddy's Labs have notably high contributions in absolute value from these EMs.

Indian players have expanded their presence in these markets through various approaches, including establishing their own field-force-driven front ends, adopting distributor-led models, or participating in institutional tenders. Many of these EMs exhibit dynamics like India, with branded generic markets driven by out-of-pocket expenses.

In tender-driven markets, Indian companies have leveraged their existing product portfolios from established markets or engaged in in-licensing deals. In some cases, they have pursued inorganic growth by acquiring brands or entire entities. Indian companies have employed diverse strategies to scale up in these markets. However, the success has been limited to one or two large markets, at best, primarily due to macroeconomic concerns such as pricing deflation, rising generic drug usage coverage, or currency volatility.

In response to rising pricing pressure and greater generic drug coverage in specific countries, Indian players have also focused on developing specialty product portfolios through front-end partnerships and in-licensing deals. Companies like Cadila Healthcare and Dr. Reddy's Labs have established biosimilars pipelines in EMs, while Sun Pharma and Glenmark Pharma have entered into out-licensing agreements for their specialty products, Ilumya and Ryaltris, respectively, as partners for launch in multiple countries.

Figure 29: Emerging markets' contribution to revenue of our coverage companies declines in 4QFY23



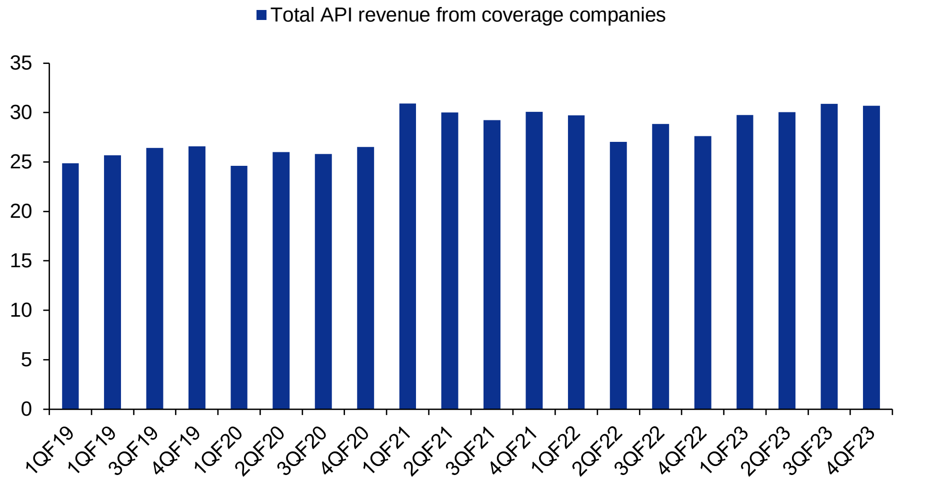
SOURCE: INCRED RESEARCH, COMPANY REPORTS

API segment – all set for a recovery

We maintain our bullish stance on the API segment, anticipating the conclusion of the recent downturn. The Covid-19 pandemic resulted in raw material shortages and logistical challenges, forcing formulation companies to maintain unusually high levels of API inventory. Consequently, API manufacturers were able to command significantly higher prices due to the urgent need for uninterrupted supplies. As the effects of the pandemic gradually subside, formulation companies find themselves burdened with excessive inventory, adversely affecting the offtake of API companies. Additionally, as the final products near their shelf-life, formulators are seeking to dispose them at significantly lower prices, further exacerbating the pressure on API companies. Also, API companies themselves had to maintain elevated level of raw material inventory, acquired at higher prices, to meet the heightened demand during the pandemic. Although the situation has since normalized, these API companies are now burdened with high-cost inventory that needs to be consumed. These factors had a significant impact on the operating profitability of API companies over the past two years. However, we anticipate a reversal of these trends. The high channel inventory is expected to deplete soon, as confirmed by numerous managements in their quarterly con-calls while the high-cost raw material inventory held by API companies should also diminish in the next three-to-six months, thereby driving a robust rebound in margins starting from 2HFY24F.

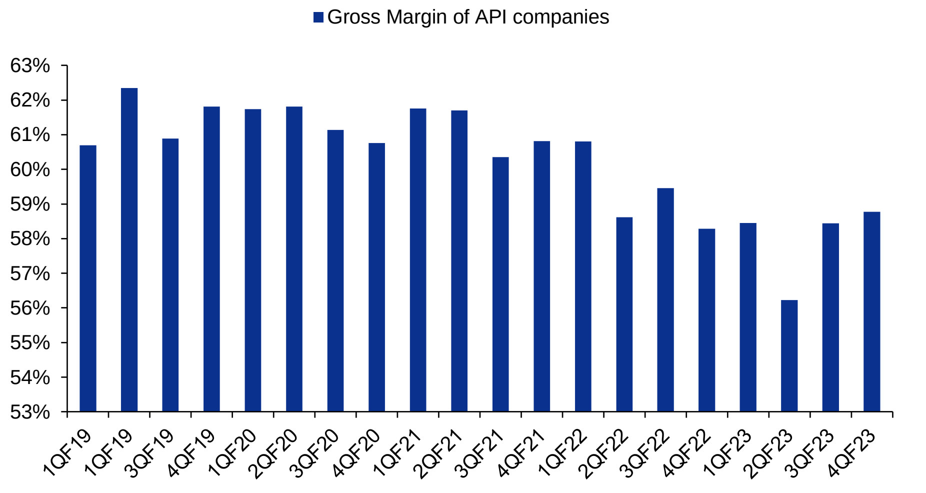
Structurally, the dynamics of the API business diverge significantly from that of the formulations business. While prices in the formulations market exhibit a substantial variation across end-markets, API prices remain relatively consistent, placing immense importance on manufacturing capability, timely supplies, compliance track record, and process chemistry to gain market share. Those players with scale advantages and cost efficiency tend to outperform their competitors. In the Indian market, most suppliers possess a significant global market share in a select few products (one-to-five products), where they excel as the lowest-cost manufacturers with the benefits of scale. Indian generics companies are proactively investing in back-end capabilities such as intermediates and key starting materials (KSMs) to reduce their reliance on China for larger products. Additionally, leading companies like Divi's Labs and Granules India are embracing green chemistry practices to minimize resource consumption, subsequently reducing costs while adopting technological solutions to prevent pollution. With favourable tailwinds from the schemes like the Production-Linked Incentive (PLI) program and an increasing shift away from China, along with depletion of channel inventory, we firmly believe that the industry is set to experience robust volume growth over the next few years.

Figure 30: API companies saw strong growth during Covid (Q1FY21-Q1FY22) and a sharp decline thereafter; some green shoots visible from 2HFY23



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 31: Gross margin of API players' revenue during the Covid-19 pandemic and the post-Covid phase



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 32: API companies' commentary in 4QFY23

Companies	4QFY23 con-call comments
Laurus Labs	GM impact was due to depressed pricing in ARV APIs and formulations. API prices have already bottomed out and are expected to bounce back.
Divi's Labs	In some generic API products, the company doesn't see any pressure on pricing, sales price or on demand. But in some of the generic APIs because after the Covid-19 impact, there are huge stocks of dosage forms and the dosage form companies' generics, it's fighting for getting rid of the stocks before the expiry date. But once that happens, companies will need APIs again. So, it expects the prices to stabilize, and they should see improvement in the coming quarters.
Neuland	The company has the highest gross margin in the API space in India. On the pricing side, the company has consistently de-risked its procurement positions from China to other suppliers. And therefore, as far as their solvents or raw materials are concerned, it is seeing volatility, but it's not extreme volatility as you see reflected in the performance numbers as well.
IOL	API manufacturers in India faced severe margin pressure earlier, with significant correction in raw material prices, that is over for the sector as domestic API manufacturers resume their investments and increase their capacity gradually to capitalize on robust domestic demand.
Aarti Drugs	Company expects a fall in input prices as well as selling prices has stopped, in coming quarters
Glenmark Lifesciences	API pricing pressure exists - more driven by the US market, and as costs ease, customers expect the prices to go up.

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 33: Highlights of the government's PLI scheme for the sector

The Government of India has introduced a Production-Linked Incentive (PLI) scheme for the promotion of domestic manufacturing of critical key starting materials (KSMs)/drug intermediates and active pharmaceutical ingredients (APIs) in India. The scheme aims to boost domestic manufacturing of APIs, reduce import dependency, and create jobs.
The PLI scheme for APIs was announced in Jul 2020 and was notified in Oct 2020. The scheme has a budget of Rs69.4bn (US$940m) and will run for a period of six years.
Under the PLI scheme, eligible companies will be provided an incentive of 20% for fermentation-based APIs and 10% for chemically synthesized APIs, on incremental sales over the base year (2019-20). The incentive will be available for a period of six years.
The PLI scheme for APIs is open to both existing and new manufacturers. To be eligible for the scheme, companies must meet certain criteria, such as having a minimum annual production capacity of 100t for fermentation-based APIs and 500t for chemically synthesized APIs.
The PLI scheme for APIs is expected to boost domestic manufacturing of APIs, reduce import dependency, and create jobs. The scheme is also expected to help India become a global hub for API manufacturing.

SOURCE: PHARMACEUTICALS.GOV.IN, INCRED RESEARCH, COMPANY REPORTS

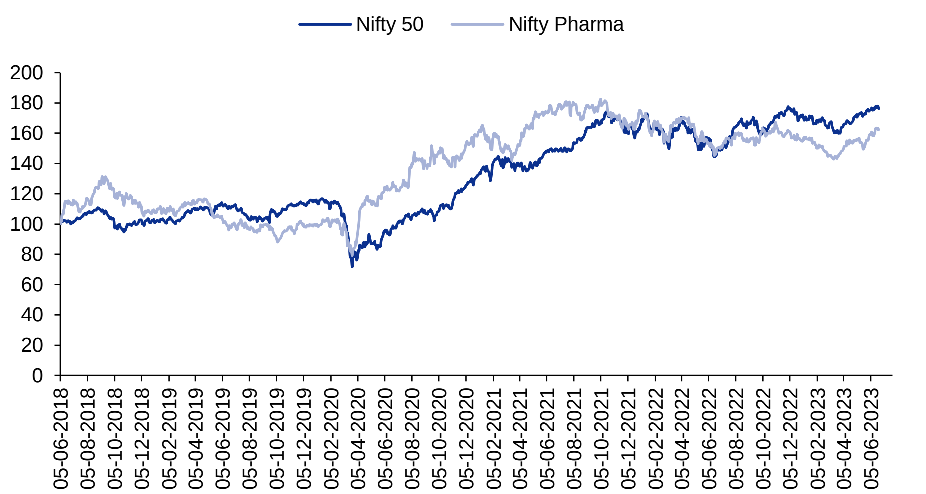
Valuation

After navigating through three turbulent years marked by strong Covid-19 tailwinds in FY21 and a sharp price erosion thereafter in FY22/1HFY23, IPM now presents select investment opportunities. Since FY24, Nifty Pharma Index has outperformed the broader Nifty Index by around 200 bp and pushed valuations of some companies in the exuberance zone. Average sector premium vs. Nifty is now at 30% against a five-year average of 20%, but still away from the 45-50% observed during Covid.

We expect a significant improvement in RoCE for our coverage companies, with an expected gain of 147 bp over the next two years. While these levels may not match the peak returns witnessed during the FY14-15 cycle, the current RoCE levels are robust for a mature business model. Companies possessing a well-diversified portfolio, flexibility in their balance sheets, a robust pipeline of product launches, and sustainable earnings are expected to outperform the sector.

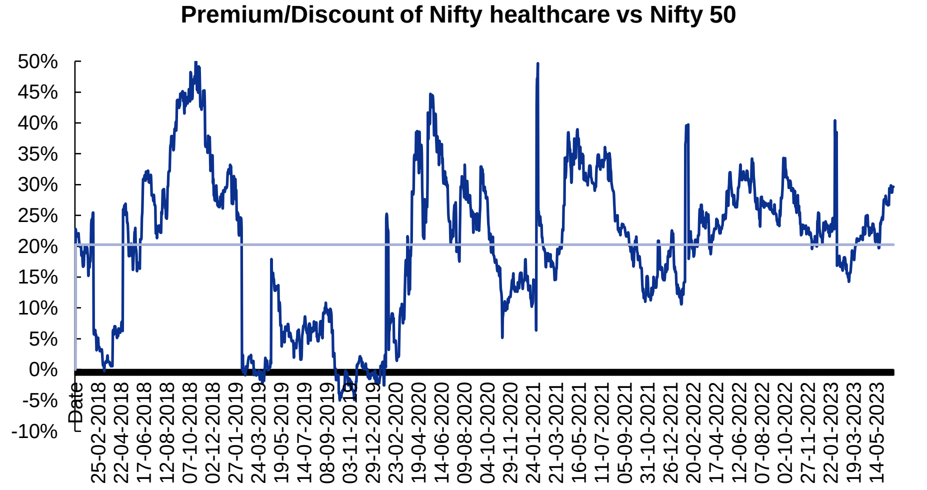
Despite the challenges faced, the IPM presents an attractive landscape for discerning investors, with the potential for healthy returns and growth prospects among companies that exhibit the above characteristics.

Figure 34: Nifty Pharma Index's outperformance vs. Nifty Index



SOURCE: INCRED RESEARCH, COMPANY REPORTS, BLOOMBERG

Figure 35: Premium/discount of Nifty Healthcare Index vs. Nifty-50 Index



SOURCES: INCRED RESEARCH, COMPANY REPORTS, BLOOMBERG

Margin expansion should support the sector's outperformance

4QFY23 was one of the worst quarters for the industry, in terms of margins, and we expect a strong recovery in FY24F, as high channel inventory as well as high-cost raw material inventory depletes, and logistic cost normalize. Further, with a favourable US pricing in the interim (although short-lived) and raw material prices deflating/stabilizing along with rising contribution of large products like gRevlimid, we expect gross margin to also exhibit a good recovery. For API companies and CDMOs, we believe a revenue growth-led recovery is very important, which should reflect largely from 2HFY24F. Because of their huge manufacturing capacities and thus, high operating leverage, margin recovery should follow the recovery in revenue. Overall, we expect the margins to improve by 143 bp in FY24F.

Selective opportunities still exist

Following a period of rapid expansion from FY10-15, the Indian pharma market faced challenges in FY16-20 due to consolidation among buyers in the US market and a surge in product approvals. This led to significant decline in the US portfolio of most companies. However, companies responded wisely by streamlining their cost structure, resulting in a leaner operational model. In the post-Covid era, additional savings are expected as marketing events shift from physical to digital platforms, to some extent.

With a reset cost base, the industry is now focusing on elevating its position in the value chain by emphasizing product complexity. Rationalization of R&D spending is underway, prioritizing high-value assets over a larger number of product filings.

We favour stocks that offer strong earnings visibility and possess a competitive advantage that is capable of navigating through various business cycles.

Resume coverage with:

ADD rating on

Sun Pharma: Shift in the business mix away from US generics, long growth runway for specialty products.

Aurobindo Pharma: Strong US positioning, improving product mix.

Torrent Pharma: Strong branded market presence, price hikes to drive margin expansion

HOLD rating on

Alkem Laboratories: Await better visibility on margins, domestic presence provides valuation cushion.

Divi's Laboratories: Biggest beneficiary of improving outsourcing trend, valuation is rich.

Ajanta Pharma: Margin expansion ahead, branded mix to cushion valuation.

Gland Pharma: Tough to map near-term recovery; await more clarity.

REDUCE rating on:

Zydus Lifesciences: High product concentration risk, large part of US improvement factored in.

Dr. Reddy's Laboratories: Weak core business profitability.

Laurus Labs: Front-loaded cost base, muted near-term revenue growth to keep margins under pressure.

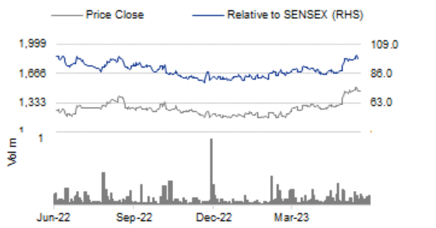
India

HOLD *(previously ADD)*

Consensus ratings*: Buy 14 Hold 1 Sell 0

Current price:	Rs1,472
Target price: ▲	Rs1,515
Previous target:	Rs1,360
Up/downside:	2.9%
InCred Research / Consensus:	1.0%
Reuters:	AJPH.NS
Bloomberg:	AJP IN
Market cap:	US$2,259m
	Rs185,348m
Average daily turnover:	US$1.5m
	Rs125.3m
Current shares o/s:	128.1m
Free float:	33.8%

**Source: Bloomberg*



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	13.8	24.3	18.0
Relative (%)	13.0	13.8	(0.4)

Major shareholders	% held
Promoters	66.2
UTI MF	4.6
Nippon MF	3.2

Ajanta Pharma Ltd

Stock is priced fairly

- Ajanta Pharma's large and diversified presence in the branded generics markets (BGx) of India, Asia and Africa (~72% of revenue) provides revenue stability/visibility and mitigates business risks.
- Margins have hit a trough in FY23. The recovery should be sharp with a ~300bp expansion in FY24F and a gradual build-up thereafter.
- The stock is priced fairly. We resume coverage on it with a HOLD rating (ADD earlier) and a target price of Rs1,515.

Large BGx presence provides high visibility to profitability & returns

Ajanta Pharma or AJP's strategy of focusing on niche, first-to-market products gives it an early-mover advantage and has led to its outperformance in India. The first-to-market launches have either been with a differentiated delivery system or combinations of existing molecules. This allows AJP to command premium pricing over its peers. Nearly 63% of AJP's portfolio is skewed towards chronic/sub-chronic therapies which are growing faster than the industry. AJP is focused on four key therapies - cardiology, ophthalmology, dermatology and pain - and ranks among the Top-10 in its coverage markets with a second rank in ophthalmology. Ex-India, AJP has around 40% contribution from branded markets of Asia and Africa, where market dynamics are broadly like in India (branded generics markets, out-of-pocket expenses, field force-driven markets) and have strong RoIs. These markets are growing between 8-10%. With a focused approach, we expect AJP to continue outperforming in these markets.

Margins hit a trough in FY23; FY24F should see a good recovery

AJP's profitability was impacted in FY23 due to high-cost inventory (which should deplete by 1QFY24F), higher freight cost (normalized now) and a decline in its high-margin Africa branded business (impacted due to pension-related strikes in France which led to delayed supplies). With normalization of these factors, AJP has given guidance of FY24F margins recovering to 25% against 17% in 4QFY23 and 21% in FY23; we directionally concur but believe a 400bp margin expansion guidance may be a little aggressive, especially as 1QFY24F should still see some impact of the high-cost inventory and the full-year impact of field force expansion in international geographies (+50% in FY23) gets factored in (our estimate: 23.9%). Structurally, we believe AJP's margins should tread the historical average of 27-28% in the next few years, led by outperformance in BGx markets.

Best-in-class operating/financial metrics, but stock is priced fairly

AJP has a strong margin profile, a debt-free balance sheet, consistently generated free cash, and a strong, consistent returns profile (RoE/RoCE of 20-25%); which has historically driven its valuation premium over peers. We expect this to continue, but at a valuation of 24x, we believe the stock is priced fairly and it's better to wait for a better entry point. We resume coverage on the stock with a HOLD rating (ADD earlier) and a target price of Rs1,515. Slower-than-expected margin improvement is a downside risk and vice-versa.

Financial Summary	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue (Rsm)	28,897	33,410	37,426	41,799	45,703
Operating EBITDA (Rsm)	9,986	9,294	7,833	9,986	11,283
Net Profit (Rsm)	6,538	7,128	5,880	7,269	8,122
Core EPS (Rs)	51.0	55.6	45.9	56.7	63.4
Core EPS Growth	39.8%	9.0%	(17.5%)	23.6%	11.7%
FD Core P/E (x)	28.84	26.45	32.07	25.94	23.22
DPS (Rs)	6.3	6.3	6.7	7.0	7.0
Dividend Yield	0.43%	0.43%	0.45%	0.48%	0.48%
EV/EBITDA (x)	18.64	19.90	22.95	17.68	15.27
P/FCFE (x)	19.19	18.98	13.29	21.28	17.63
Net Gearing	(7.1%)	(10.2%)	(25.3%)	(29.3%)	(33.8%)
P/BV (x)	6.29	5.78	5.57	4.68	3.97
ROE	23.4%	22.8%	17.7%	19.6%	18.5%
% Change In Core EPS Estimates				7.58%	7.22%
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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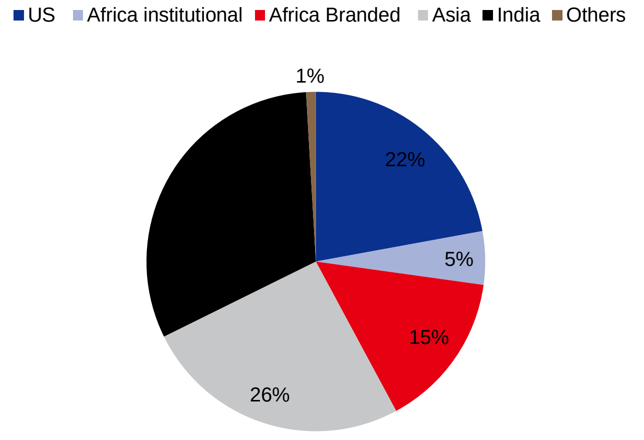
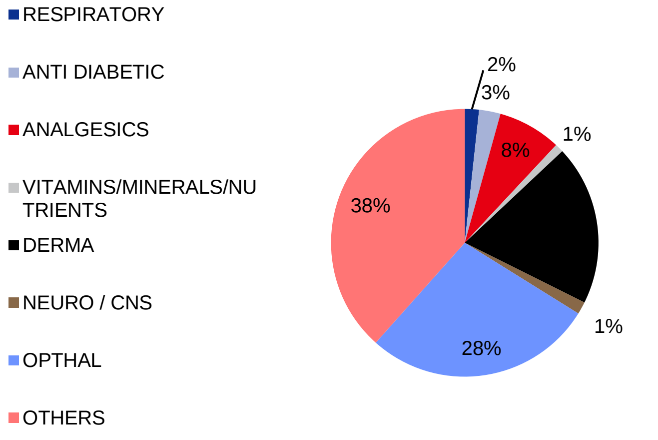
Figure 36: AJP's revenue breakup – large branded business presence



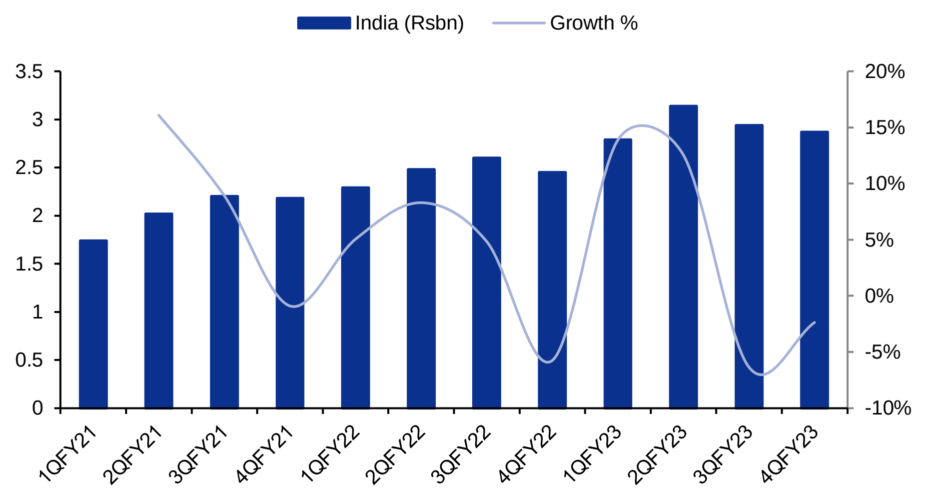
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 37: Therapeutic-wise break-up of AJP



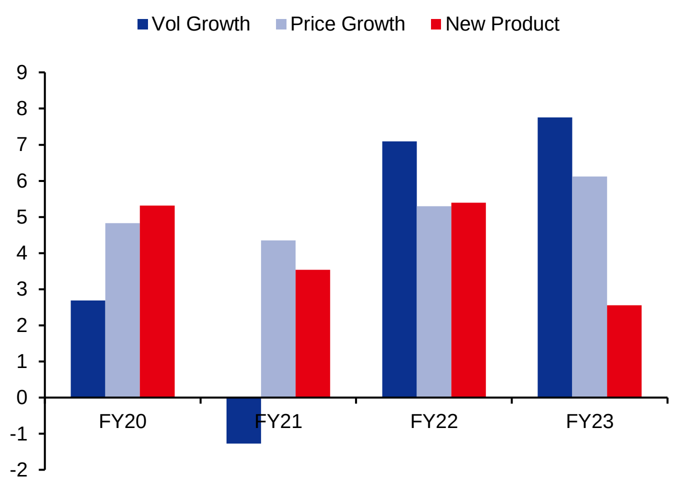
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 38: Domestic revenue has been scaling up steadily



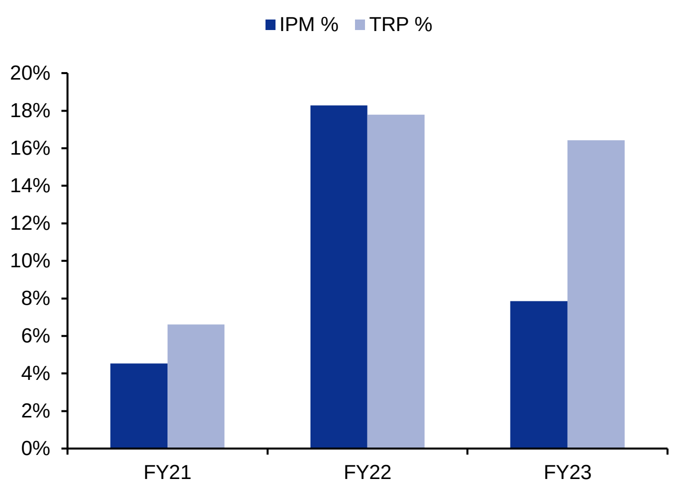
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 39: Growth drivers of domestic market – all three components contributing well



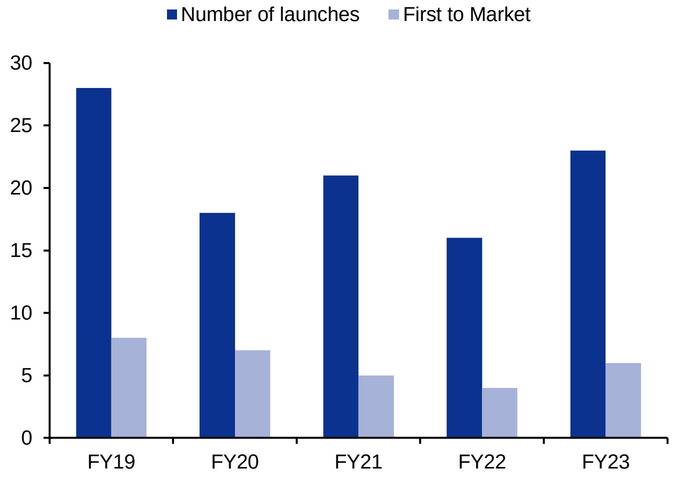
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 40: Consistently outperforming IPM growth



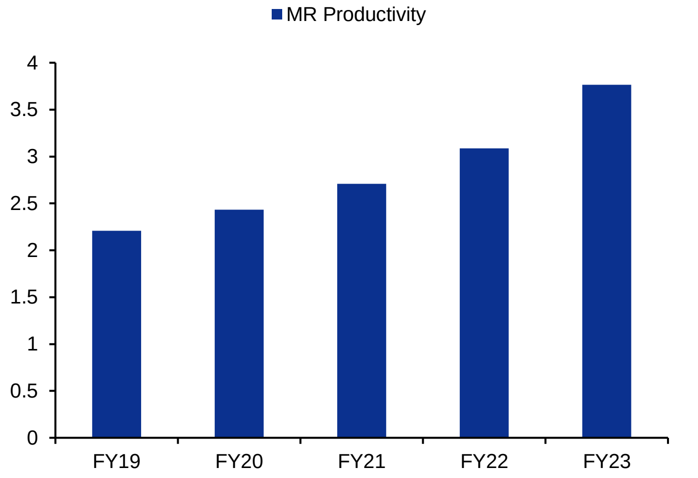
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 41: First-to-market launches in India have been a key driver of India business growth



SOURCE: INCRED RESEARCH, COMPANY REPORTS

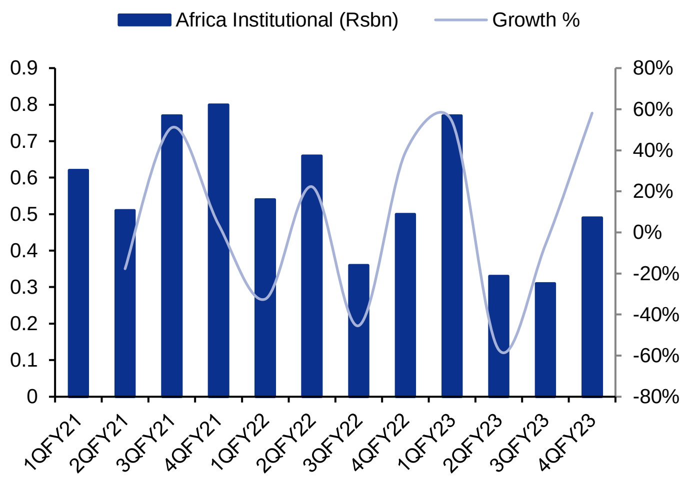
Figure 42: MR productivity – looks low as the covered market is relatively small



SOURCE: INCRED RESEARCH, COMPANY REPORTS

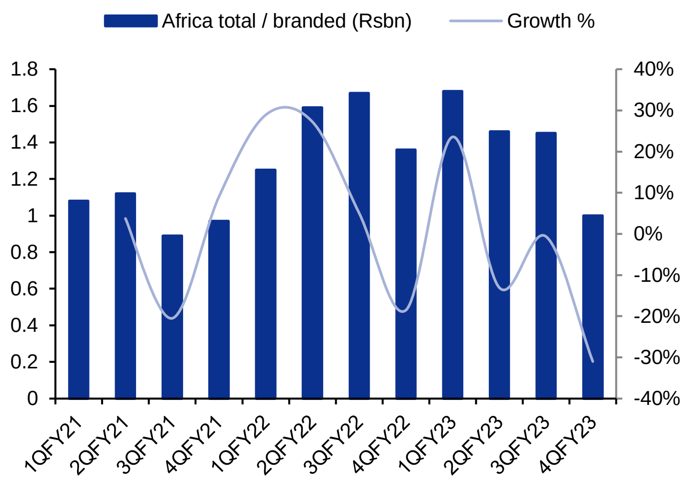
Africa institutional business is no more a focus area, but the focus is on Africa branded business.

Figure 43: Not a focus area given it's a tender-driven business, expect flat-to-declining revenue



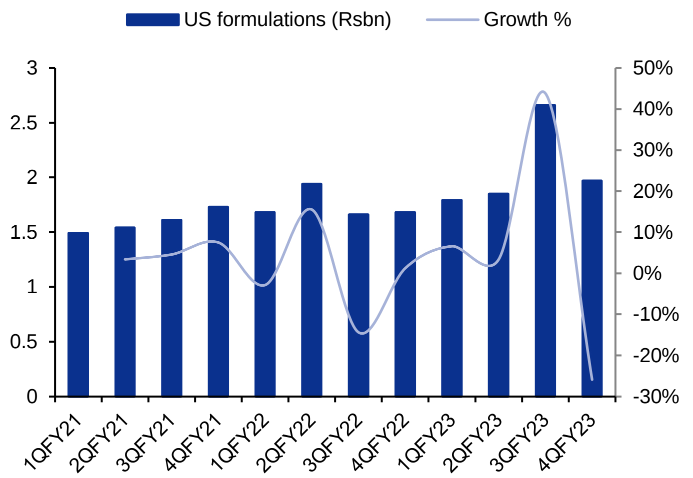
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 44: Africa branded business – relatively steady



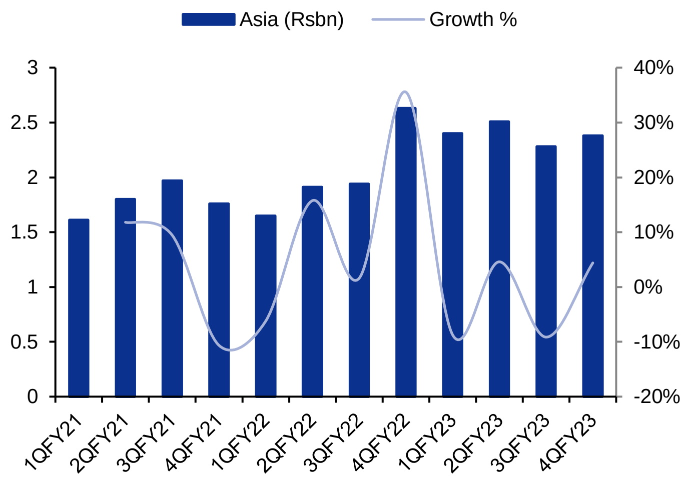
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 45: US business - steady growth on a low base



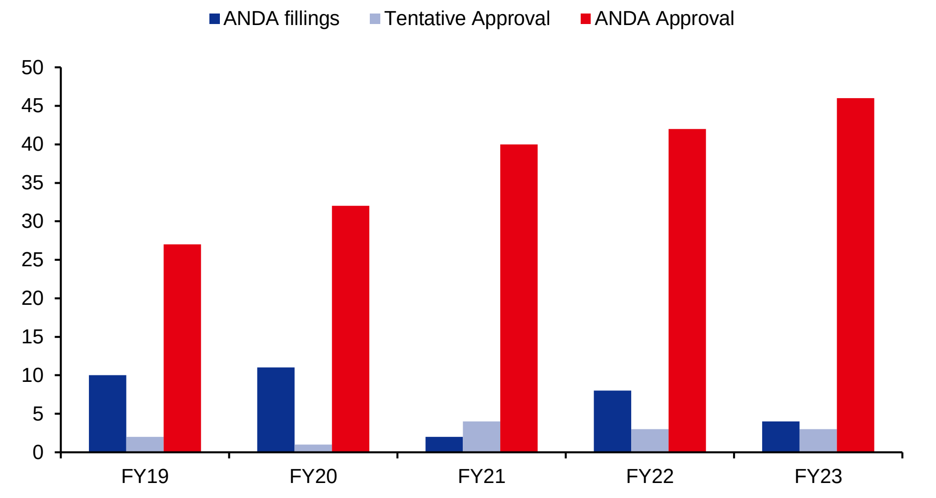
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 46: Asia revenue – fairly consistent



SOURCE: INCRED RESEARCH, COMPANY REPORTS

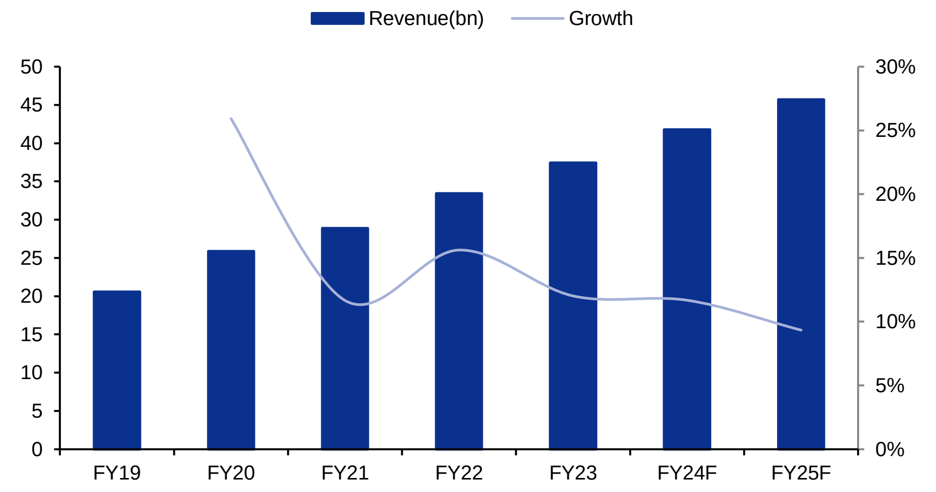
Figure 47: ANDA filings and approvals over the year



SOURCE: INCRED RESEARCH, COMPANY REPORTS

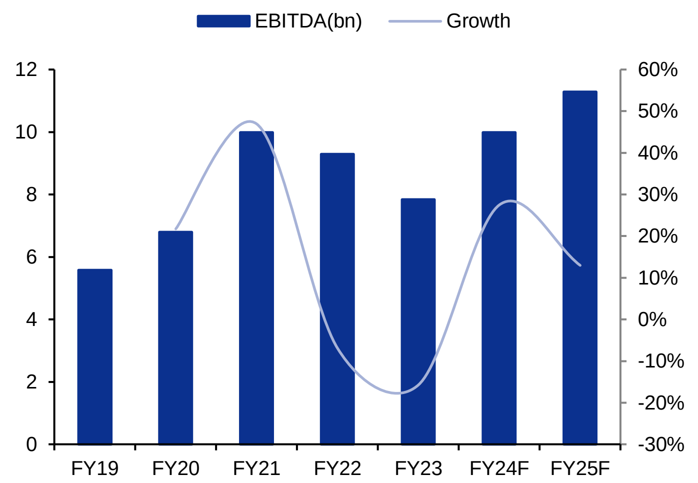
High branded Gx presence has ensured a strong profitability profile.

Figure 48: Steady revenue growth backed the large branded generics franchise



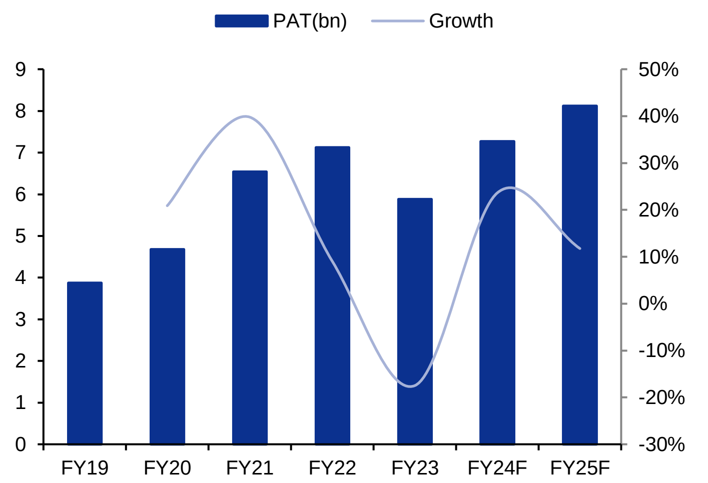
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 49: FY23 margins hit a trough



SOURCE: INCRED RESEARCH, COMPANY REPORTS

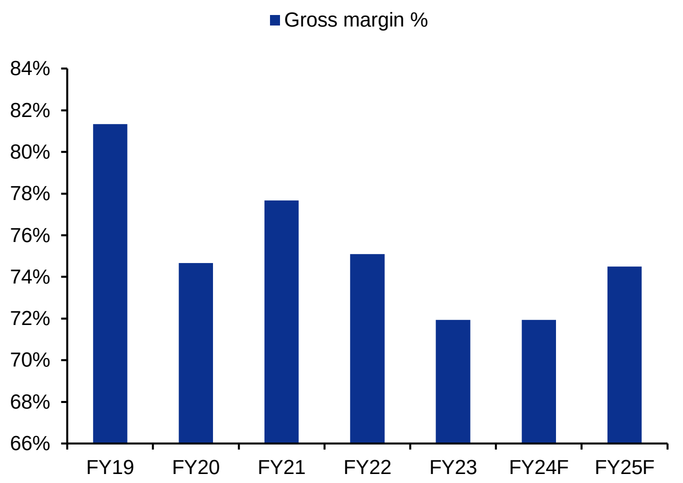
Figure 50: PAT follows suit



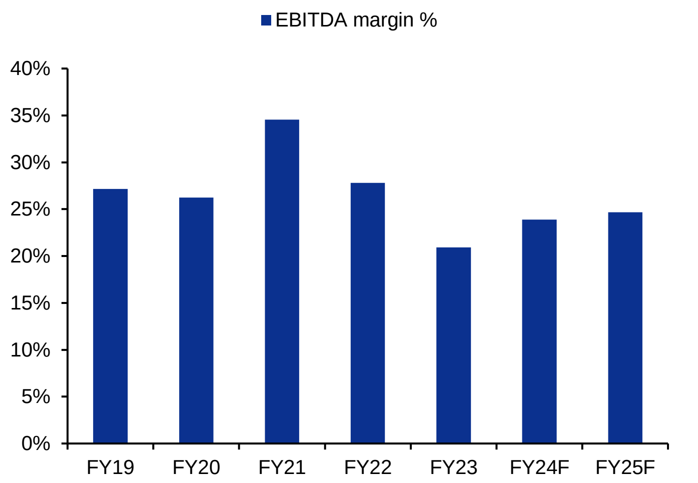
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 51: Gross margin trend

Figure 52: EBITDA margin trend



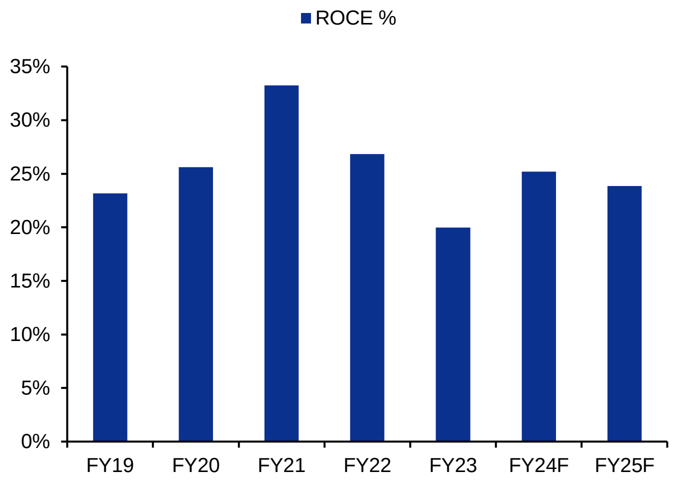
SOURCE: INCRED RESEARCH, COMPANY REPORTS



SOURCE: INCRED RESEARCH, COMPANY REPORTS

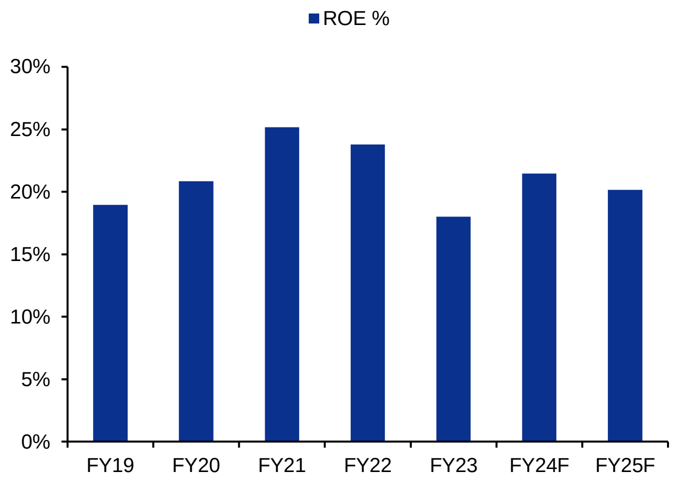
Strong return ratios...

Figure 53: RoCE of AJP



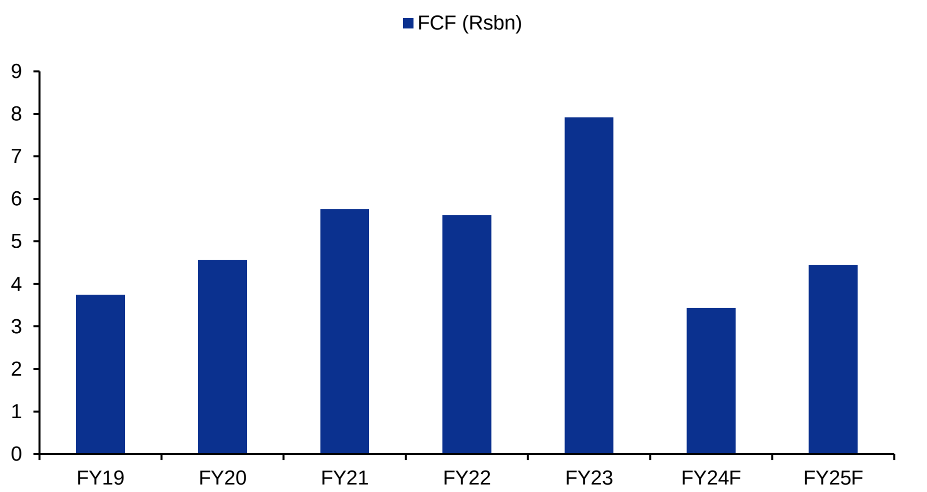
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 54: RoE of AJP



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 55: Strong history of FCF generation

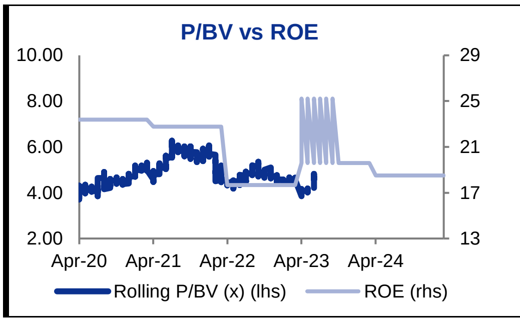


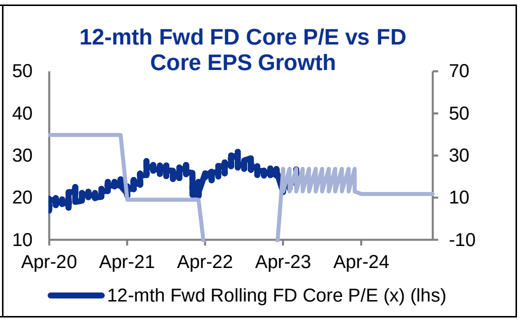
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 56: One-year forward P/E of Ajanta Pharma

SOURCE: INCRED RESEARCH, COMPANY REPORTS, BLOOMBERG

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Net Revenues	**28,897**	**33,410**	**37,426**	**41,799**	**45,703**
Gross Profit	**22,447**	**25,088**	**26,922**	**31,140**	**34,277**
Operating EBITDA	**9,986**	**9,294**	**7,833**	**9,986**	**11,283**
Depreciation And Amortisation	(1,161)	(1,253)	(1,308)	(1,440)	(1,575)
Operating EBIT	**8,825**	**8,041**	**6,525**	**8,546**	**9,708**
Financial Income/(Expense)	(83)	(102)	(58)	(45)	(45)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	260	1,157	986	700	750
Profit Before Tax (pre-EI)	**9,002**	**9,096**	**7,453**	**9,201**	**10,413**
Exceptional Items					
Pre-tax Profit	**9,002**	**9,096**	**7,453**	**9,201**	**10,413**
Taxation	(2,463)	(1,968)	(1,573)	(1,932)	(2,291)
Exceptional Income - post-tax					
Profit After Tax	**6,538**	**7,128**	**5,880**	**7,269**	**8,122**
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**6,538**	**7,128**	**5,880**	**7,269**	**8,122**
Recurring Net Profit	6,538	7,128	5,880	7,269	8,122
Fully Diluted Recurring Net Profit	**6,538**	**7,128**	**5,880**	**7,269**	**8,122**

Cash Flow

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
EBITDA	9,986	9,294	7,833	9,986	11,283
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(2,088)	(2,004)	575	(2,623)	(2,744)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	(2,135)	(1,670)	(490)	(1,932)	(2,291)
Net Interest (Paid)/Received	(83)	(102)	(58)	(45)	(45)
Tax Paid	(2,312)	(2,724)	(1,418)	(2,587)	(2,996)
Cashflow From Operations	**5,763**	**5,620**	**7,918**	**5,431**	**6,248**
Capex	(1,699)	(1,304)	(1,649)	(2,000)	(1,800)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments					
Other Investing Cashflow					
Cash Flow From Investing	**4,064**	**4,316**	**6,268**	**3,431**	**4,448**
Debt Raised/(repaid)					
Proceeds From Issue Of Shares	(1,678)	(3,541)	(14)		
Shares Repurchased					
Dividends Paid	(83)	(822)	(897)	(854)	(897)
Preferred Dividends					
Other Financing Cashflow	(2,201)	1,229	(108)	1,045	777
Cash Flow From Financing	**(3,962)**	**(3,134)**	**(1,019)**	**191**	**(120)**
Total Cash Generated	102	1,182	5,249	3,622	4,329
Free Cashflow To Equity	**9,827**	**9,936**	**14,186**	**8,862**	**10,697**
Free Cashflow To Firm	**9,910**	**10,038**	**14,245**	**8,907**	**10,742**

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Cash And Equivalents	2,155	3,337	8,586	12,208	16,537
Total Debtors	7,384	10,198	10,569	12,540	13,711
Inventories	7,665	7,911	8,156	9,196	10,055
Total Other Current Assets	3,072	1,199	1,029	1,254	1,371
Total Current Assets	**20,276**	**22,645**	**28,340**	**35,197**	**41,673**
Fixed Assets	15,374	15,856	16,173	16,733	16,958
Total Investments	253	251	251	251	251
Intangible Assets	108	793	886	886	886
Total Other Non-Current Assets	1,777	1,012	1,140	1,140	1,140
Total Non-current Assets	**17,511**	**17,912**	**18,450**	**19,010**	**19,235**
Short-term Debt		3	2	2	2
Current Portion of Long-Term Debt					
Total Creditors	3,739	3,272	4,228	4,346	4,697
Other Current Liabilities	2,748	3,199	7,163	7,657	6,710
Total Current Liabilities	**6,486**	**6,474**	**11,393**	**12,005**	**11,408**
Total Long-term Debt	16	16	13	403	475
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	1,329	1,422	1,505	1,505	1,505
Total Non-current Liabilities	**1,345**	**1,439**	**1,518**	**1,908**	**1,980**
Total Provisions					
Total Liabilities	**7,831**	**7,912**	**12,910**	**13,913**	**13,388**
Shareholders Equity	29,956	32,644	33,880	40,295	47,520
Minority Interests					
Total Equity	**29,956**	**32,644**	**33,880**	**40,295**	**47,520**

Key Ratios

	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue Growth	11.7%	15.6%	12.0%	11.7%	9.3%
Operating EBITDA Growth	47.0%	(6.9%)	(15.7%)	27.5%	13.0%
Operating EBITDA Margin	34.6%	27.8%	20.9%	23.9%	24.7%
Net Cash Per Share (Rs)	16.70	25.90	66.91	92.14	125.37
BVPS (Rs)	233.85	254.83	264.48	314.56	370.96
Gross Interest Cover	106.32	78.83	111.72	189.92	215.74
Effective Tax Rate	27.4%	21.6%	21.1%	21.0%	22.0%
Net Dividend Payout Ratio					
Accounts Receivables Days	95.60	96.04	101.27	100.90	104.82
Inventory Days	357.09	341.57	279.15	297.10	307.48
Accounts Payables Days	208.29	153.73	130.30	146.80	144.44
ROIC (%)	22.8%	19.7%	18.4%	21.5%	22.2%
ROCE (%)	31.2%	25.7%	19.6%	22.9%	21.9%
Return On Average Assets	18.6%	18.4%	13.6%	14.5%	14.2%

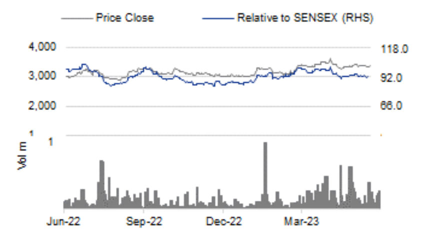
SOURCE: INCRED RESEARCH, COMPANY REPORTS

India

HOLD *(no change)*

Consensus ratings*:	Buy 11 Hold 7 Sell 7
Current price:	Rs3,402
Target price: ▲	Rs3,542
Previous target:	Rs3,434
Up/downside:	4.1%
InCred Research / Consensus:	5.9%
Reuters:	ALKE.NS
Bloomberg:	ALKEM IN
Market cap:	US$4,957m
	Rs406,700m
Average daily turnover:	US$5.6m
	Rs458.0m
Current shares o/s:	119.6m
Free float:	42.9%

**Source: Bloomberg*



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	1.7	7.9	14.0
Relative (%)	0.9	(1.2)	(3.7)

Major shareholders	% held
Promoters	57.1
LIC	3.9
DSP MF	3.2

Alkem Laboratories Ltd

Margins to remain under pressure

- Barring the two Covid-19 years (FY21-22), Alkem Labs' margins have always fallen short of the 20% threshold throughout the past decade, despite its India-heavy revenue base, indicating inherent inefficiency in its cost structure.
- This is an opportunity as well as a cause for concern. We find FY24F margin guidance of ~16% (+200bp on a low FY23 base) disappointing, particularly as it includes the benefit of ~Rs800m from the shutdown of its US plant.
- We await a more comprehensive plan to revive margins. Mankind Pharma's valuation implies the market is willing to assign a higher multiple to India-heavy franchises. Resume coverage with a HOLD rating and a TP of Rs3,542.

Close proxy of India pharmaceutical market (IPM)

Alkem Laboratories' (Alkem) India business is representative of IPM – an acute-dominated portfolio (~58% of India business), a fast-growing chronic business (on a small base) and trade generics portfolio (second-largest player, 21% of India business). Alkem has broadly maintained its market share at ~3.4% over the last five years. It is the largest player in anti-infectives (9.4% market share or MS), the second-largest in vitamins/nutrients (5.6% MS) and the third-largest in gastro-intestinal (5.8% MS) and pain/analgesics (3.5% MS). While the acute segment broadly tracks industry growth, it is witnessing strong growth in the chronic segments of cardio, diabetes, respiratory and neuro/CNS (on a low base). It is especially doing well in the anti-diabetec segment backed by successful launches of recently off-patent molecules like dapagliflozin, sitagliptin & vildagliptin (in top-5 across these). We expect the acute segment to grow at 8-9%, while the chronic segment should grow much faster at 20-22%, driving overall India growth of 10-11% over FY23-25F.

Margins fail to reflect the strong India trajectory

Despite an India-heavy portfolio (~90% of profits), Alkem's margins have failed to top the 20% threshold (barring Covid years). This underpins the inefficiency in its cost structure; for e.g., despite one of the largest field forces in India (17,000 MRs), Alkem's India revenue is 20-25% lower than that of peers. Its US portfolio largely comprises commoditized products and we don't expect a material turnaround in its profitability anytime soon. A 200bp margin improvement guidance in FY24F (~16% vs. 17-18% guidance earlier) is dismal as well, especially as Alkem is likely to benefit (~Rs800m) from the shutdown of its US plant.

Mankind's valuation implies market favours India-driven franchises

The valuation of recently listed Mankind Pharma (currently at 31x FY25F consensus EPS) implies the market's fervour towards India-driven franchises. On most counts, Alkem compares well with Mankind Pharma, and we thus feel that Alkem should trade at the higher end of its average P/E band of 20-25x. We resume coverage on the stock with a HOLD rating and a target price of Rs3,542. Slowdown in India is a key downside risk while better-than-expected margins is an upside risk.

Financial Summary	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue (Rsm)	88,765	106,342	115,993	127,429	139,345
Operating EBITDA (Rsm)	19,539	20,380	16,095	19,809	22,896
Net Profit (Rsm)	15,850	16,456	9,842	14,897	17,655
Core EPS (Rs)	132.6	137.6	89.0	124.6	147.7
Core EPS Growth	40.6%	3.8%	(35.4%)	40.1%	18.5%
FD Core P/E (x)	25.66	24.71	38.24	27.30	23.04
DPS (Rs)	28.0	34.0	54.0	35.0	35.0
Dividend Yield	0.82%	1.00%	1.59%	1.03%	1.03%
EV/EBITDA (x)	20.67	19.91	24.31	19.69	16.65
P/FCFE (x)	17.42	21.47	12.97	24.70	14.77
Net Gearing	(4.2%)	(0.8%)	(17.3%)	(17.1%)	(22.9%)
P/BV (x)	5.51	4.71	4.50	4.12	3.63
ROE	23.4%	20.6%	12.0%	15.7%	16.7%
% Change In Core EPS Estimates				(0.22%)	8.52%
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Analyst(s)

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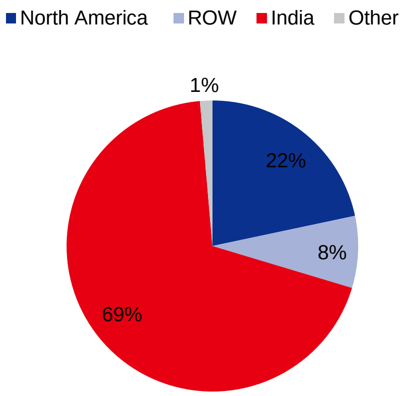
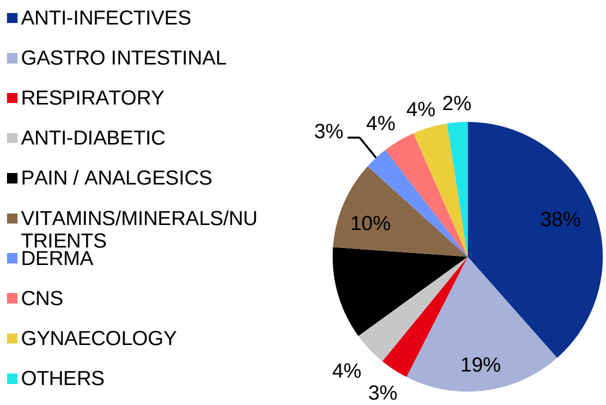
Figure 57: Geographical break-up of revenue



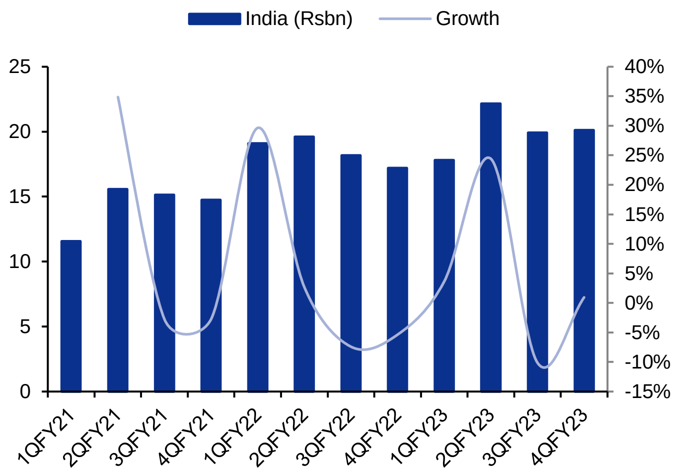
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 58: Therapy-wise break-up of India revenue



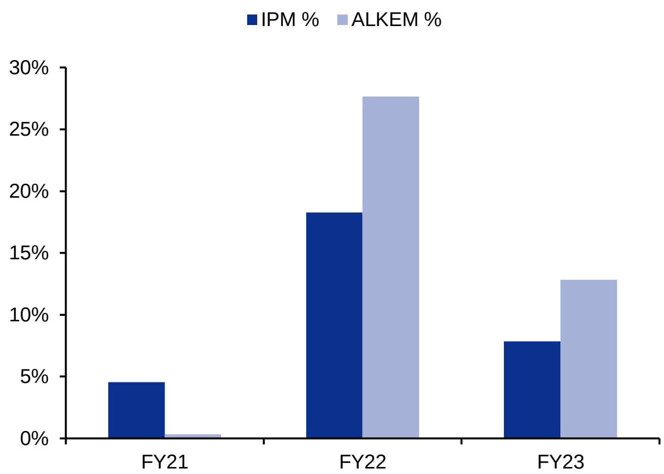
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 59: Domestic business performance over the past few quarters – FY23 saw some moderation after a strong FY22



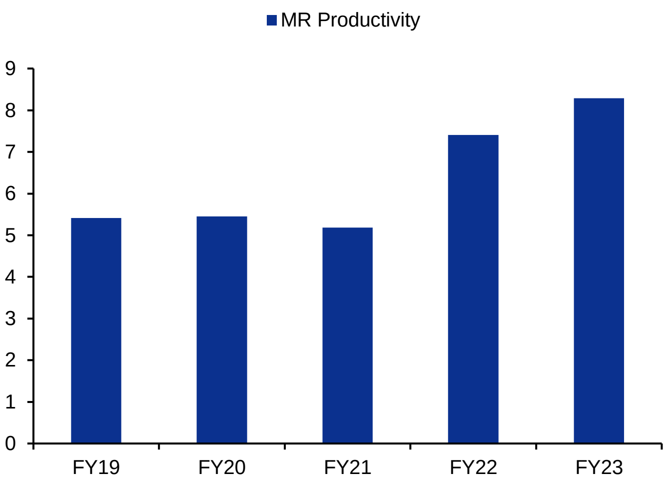
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 60: Alkem's growth vs. IPM growth



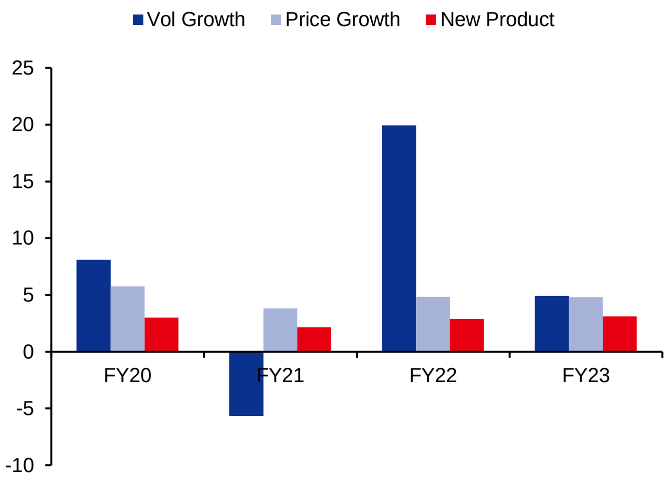
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 61: MR productivity – good scale-up in the past two years



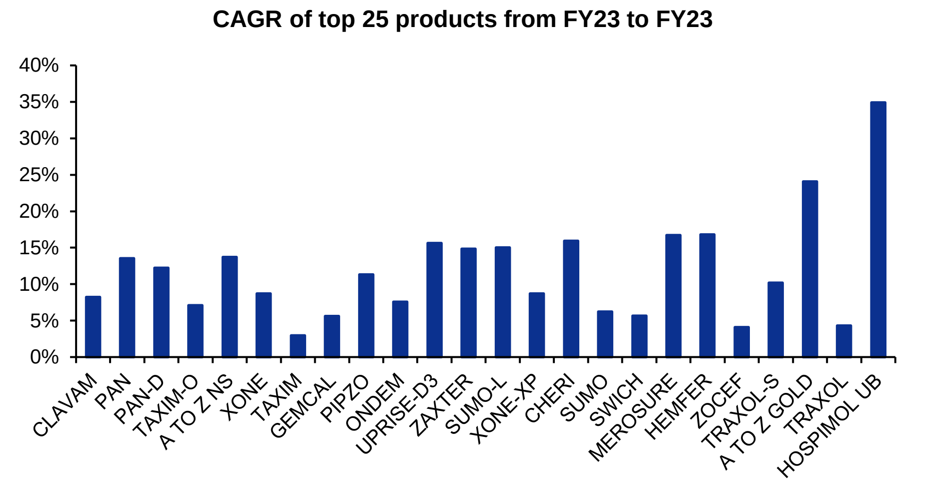
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 62: Growth drivers of domestic market – volume growth has picked up in recent years



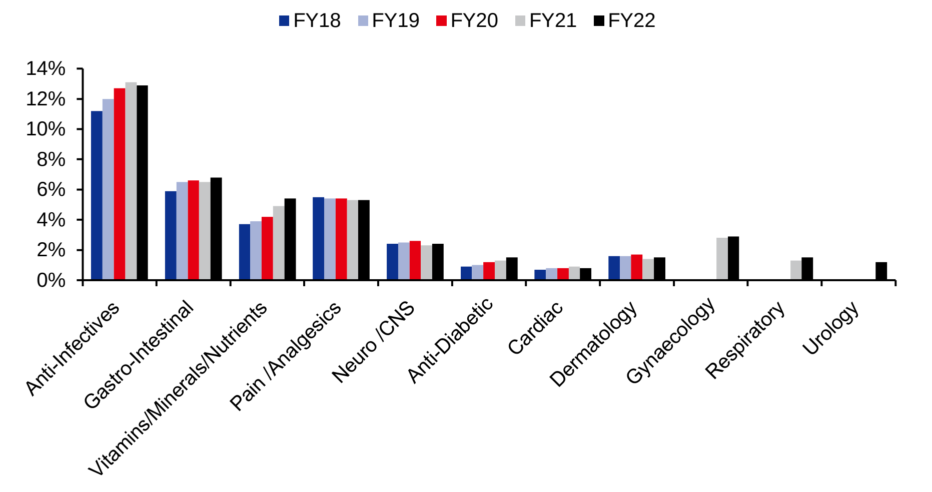
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 63: CAGRs of top-25 products over FY20 to FY23 - large products have shown a good momentum



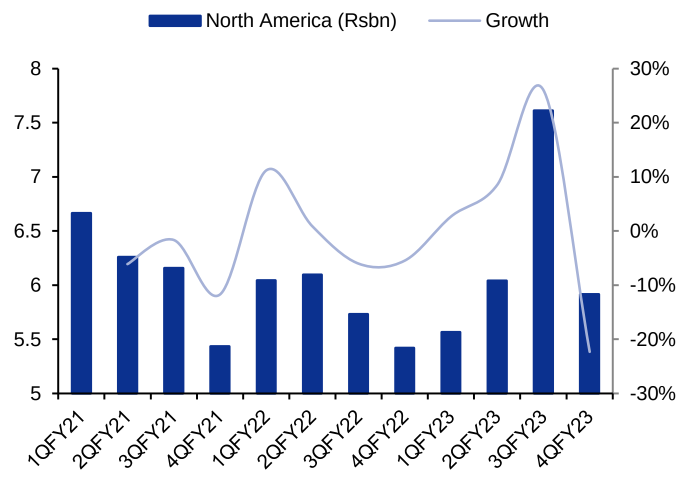
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 64: Market share in key therapies – enjoys a large market share in acute therapies and have sustained it



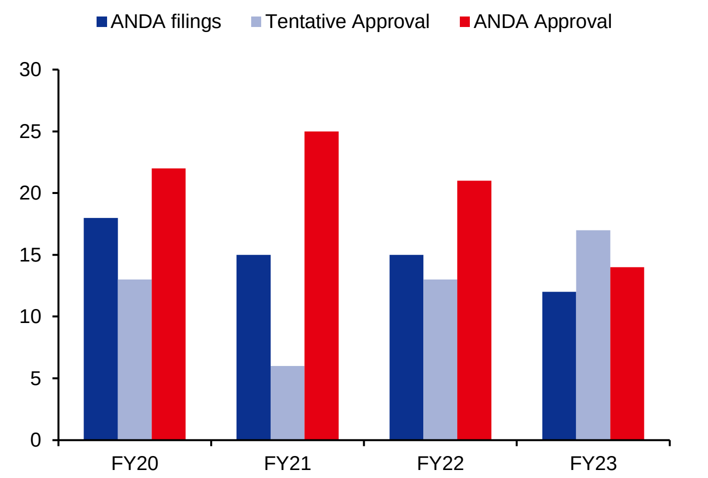
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 65: US business performance over the past few quarters – sharp jump in 3QFY23 was on account of the flu season



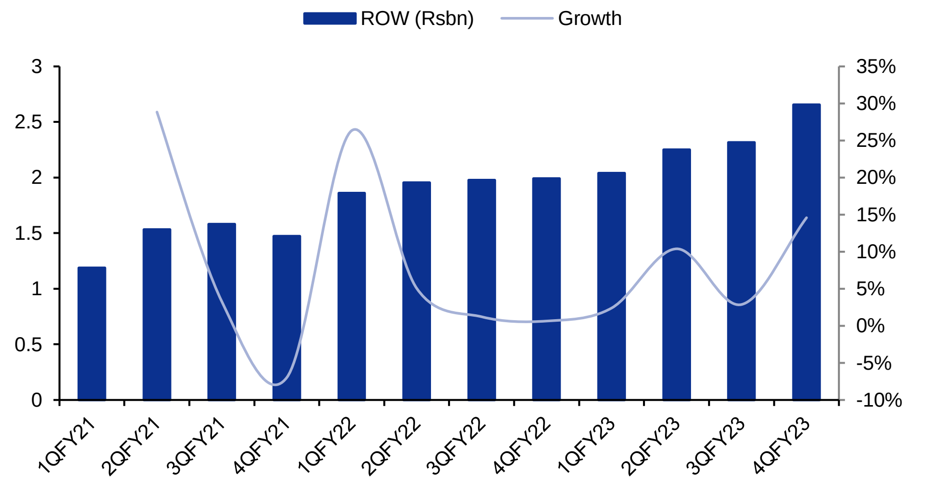
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 66: ANDA approvals and filings over the past four years



SOURCE: INCRED RESEARCH, COMPANY REPORTS

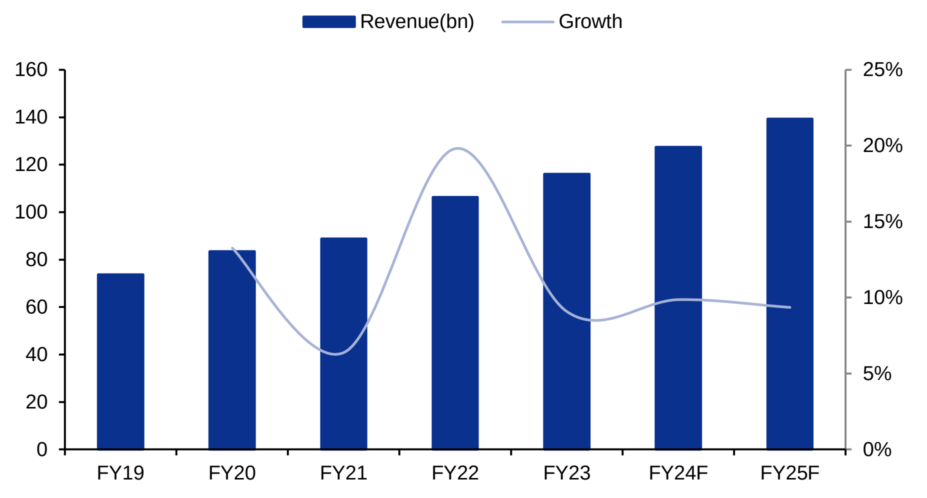
Figure 67: RoW performance over the past few quarters – steady scale-up



SOURCE: INCRED RESEARCH, COMPANY REPORTS

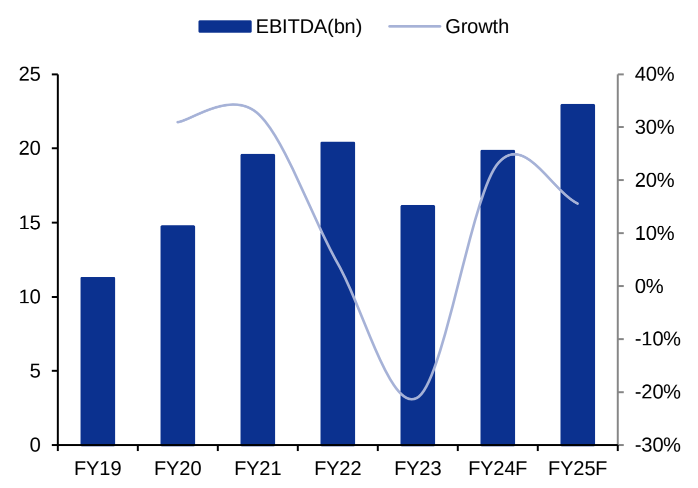
Despite an India heavy portfolio, margins have failed to cross the 20% threshold.

Figure 68: High contribution from India has ensured consistent revenue growth in the past



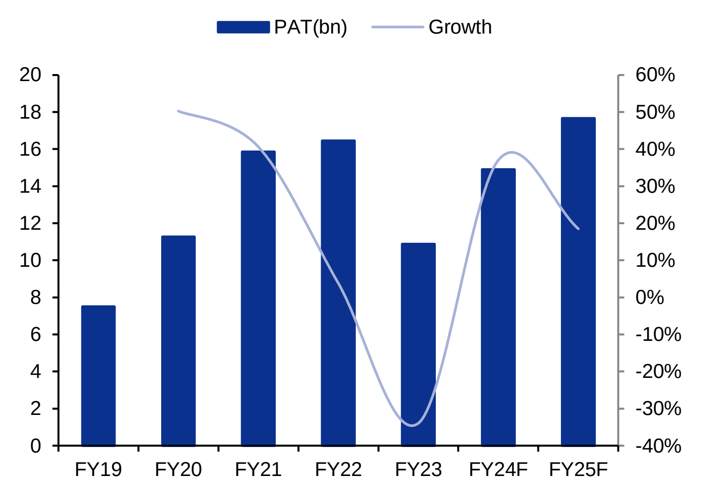
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 69: EBITDA growth has been strong in Covid years due to low marketing expenses, but lag sales growth now



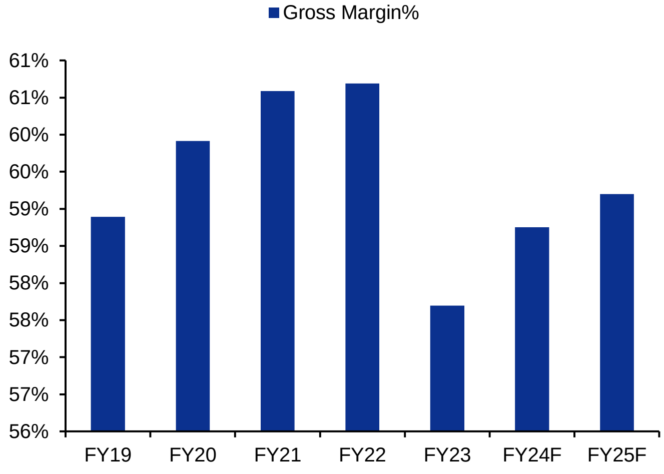
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 70: PAT has also largely followed this trend



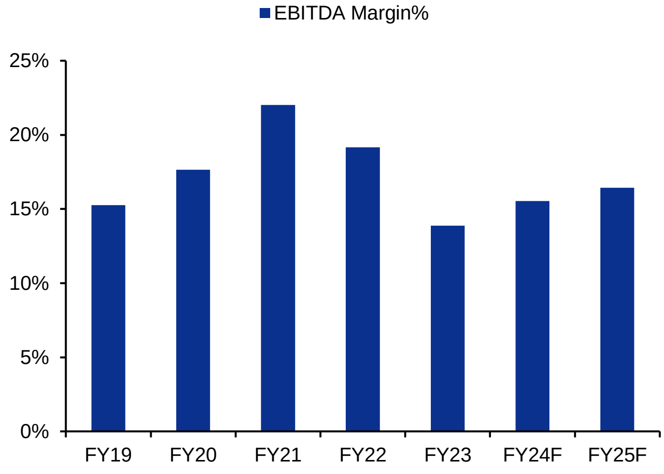
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 71: Gross margin trend



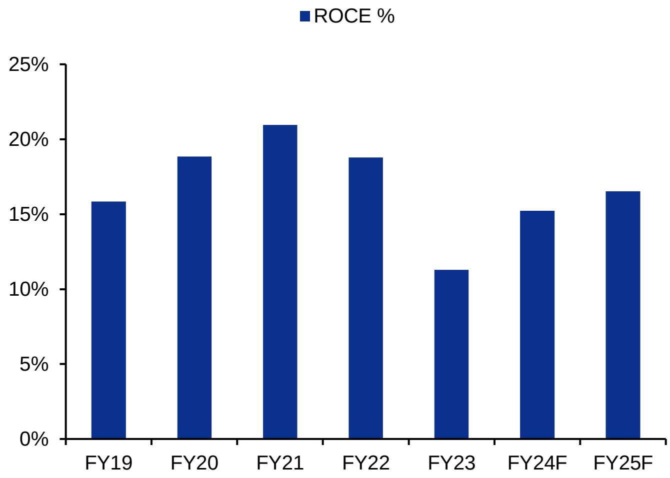
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 72: EBITDA margin trend



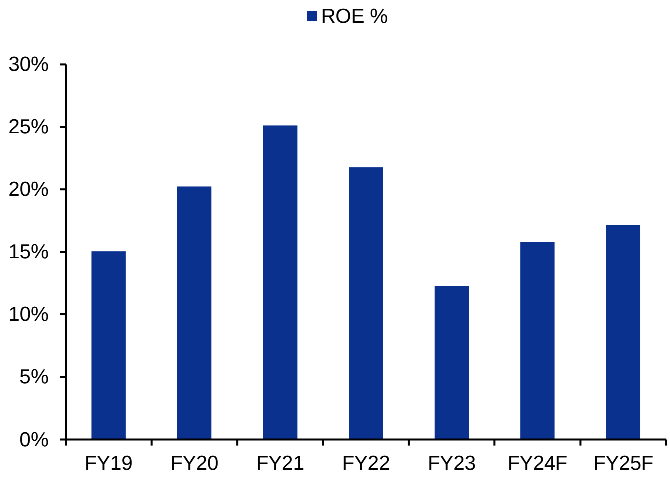
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 73: ROCE of ALKEM



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 74: ROE of ALKEM



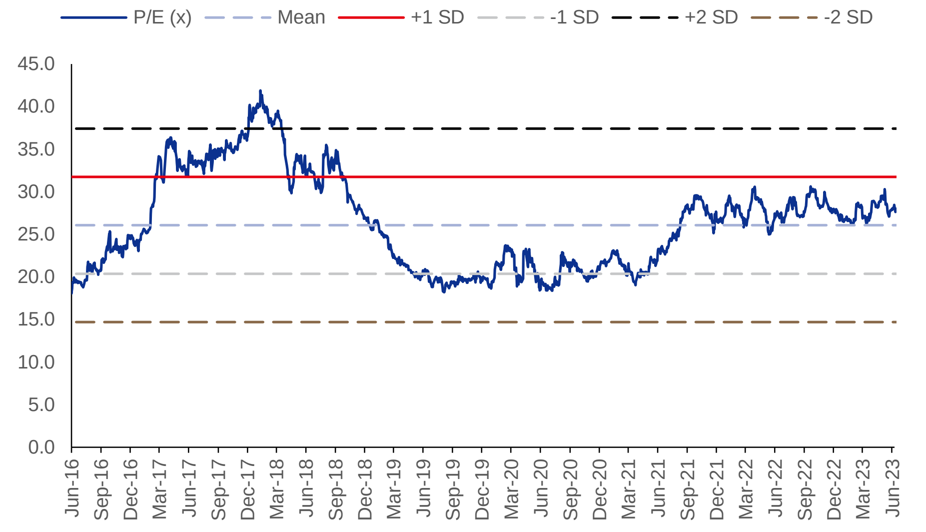
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 75: Alkem's comparison with Mankind Pharma (Rsm)

Contents (FY23)	Mankind Pharma	Alkem Laboratories
Revenue	87,490	1,15,993
Gross margin	67%	58%
EBITDA	19,130	16,095
EBITDA margin	22%	14%
PAT	13,100	10,872
EPS	32.0	76.6
Cash flow from operations	18,130	16,825
Domestic business	84,530	80,011
% of total business	97%	69%
Chronic segment's contribution	34%	50%
Market cap.	682.4bn	405.6bn
P/E	31x FY25F	

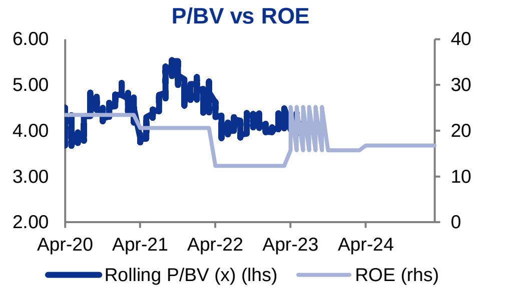
SOURCE: INCRED RESEARCH, COMPANY REPORTS

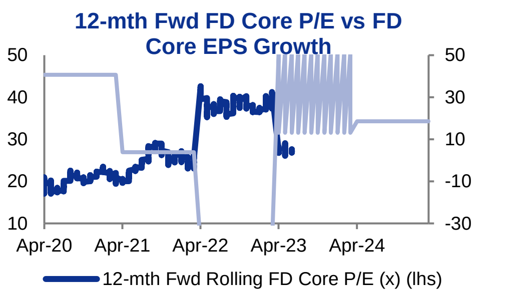
Figure 76: One-year forward P/E of Alkem



SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Net Revenues	**88,765**	**106,342**	**115,993**	**127,429**	**139,345**
Gross Profit	**53,780**	**64,539**	**66,924**	**74,865**	**82,492**
Operating EBITDA	**19,539**	**20,380**	**16,095**	**19,809**	**22,896**
Depreciation And Amortisation	(2,746)	(3,040)	(3,104)	(3,450)	(3,750)
Operating EBIT	**16,793**	**17,340**	**12,990**	**16,359**	**19,146**
Financial Income/(Expense)	(589)	(524)	(1,074)	(920)	(500)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	2,217	1,627	2,161	2,000	2,000
Profit Before Tax (pre-EI)	**18,421**	**18,443**	**14,078**	**17,439**	**20,646**
Exceptional Items			(1,030)		
Pre-tax Profit	**18,421**	**18,443**	**13,048**	**17,439**	**20,646**
Taxation	(2,243)	(1,640)	(2,980)	(2,441)	(2,890)
Exceptional Income - post-tax					
Profit After Tax	**16,178**	**16,803**	**10,068**	**14,997**	**17,755**
Minority Interests	(328)	(347)	(226)	(100)	(100)
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**15,850**	**16,456**	**9,842**	**14,897**	**17,655**
Recurring Net Profit	15,850	16,456	10,636	14,897	17,655
Fully Diluted Recurring Net Profit	**15,850**	**16,456**	**10,636**	**14,897**	**17,655**

Cash Flow

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
EBITDA	19,539	20,380	16,095	19,809	22,896
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(3,412)	(5,450)	24	(7,410)	(4,141)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	(3,478)	(3,820)	706	(2,541)	(2,990)
Net Interest (Paid)/Received	(589)	(524)	(1,074)	(920)	(500)
Tax Paid	(5,106)	(4,923)	649	(3,621)	(4,490)
Cashflow From Operations	**12,649**	**11,110**	**16,825**	**9,857**	**15,764**
Capex	(1,949)	(3,280)	(2,297)	(3,250)	(4,000)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments					
Other Investing Cashflow					
Cash Flow From Investing	**10,700**	**7,830**	**14,528**	**6,607**	**11,764**
Debt Raised/(repaid)					
Proceeds From Issue Of Shares			1,615		
Shares Repurchased					
Dividends Paid	(3,348)	(4,219)	5,295	(6,457)	(4,185)
Preferred Dividends					
Other Financing Cashflow	1,630	3,866	(19,411)	1,080	1,500
Cash Flow From Financing	**(1,718)**	**(354)**	**(12,501)**	**(5,377)**	**(2,685)**
Total Cash Generated	8,982	7,477	2,027	1,231	9,079
Free Cashflow To Equity	**23,349**	**18,941**	**31,353**	**16,465**	**27,528**
Free Cashflow To Firm	**23,938**	**19,464**	**32,427**	**17,385**	**28,028**

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Cash And Equivalents	19,905	27,381	29,409	30,639	39,719
Total Debtors	16,072	18,846	21,322	24,212	26,476
Inventories	23,124	30,055	26,075	29,309	32,049
Total Other Current Assets	10,187	8,072	10,491	11,469	12,541
Total Current Assets	**69,288**	**84,354**	**87,297**	**95,629**	**110,785**
Fixed Assets	22,339	26,266	25,135	24,935	25,185
Total Investments	1,540	2,317	3,046	3,046	3,046
Intangible Assets	5,591	6,227	4,926	4,926	4,926
Total Other Non-Current Assets	16,435	21,529	17,163	17,163	17,163
Total Non-current Assets	**45,904**	**56,338**	**50,270**	**50,070**	**50,320**
Short-term Debt	16,360	25,923	13,072	13,072	13,072
Current Portion of Long-Term Debt					
Total Creditors	10,694	11,734	11,650	12,040	13,023
Other Current Liabilities	8,987	10,396	12,350	11,651	12,603
Total Current Liabilities	**36,041**	**48,053**	**37,072**	**36,762**	**38,698**
Total Long-term Debt	343	759			
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	3,230	3,407	6,145	6,145	6,145
Total Non-current Liabilities	**3,572**	**4,165**	**6,145**	**6,145**	**6,145**
Total Provisions					
Total Liabilities	**39,613**	**52,219**	**43,217**	**42,907**	**44,843**
Shareholders Equity	73,767	86,379	90,453	98,794	112,164
Minority Interests	1,813	2,094	3,897	3,997	4,097
Total Equity	**75,580**	**88,473**	**94,350**	**102,791**	**116,261**

Key Ratios

	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue Growth	6.4%	19.8%	9.1%	9.9%	9.4%
Operating EBITDA Growth	32.6%	4.3%	(21.0%)	23.1%	15.6%
Operating EBITDA Margin	22.0%	19.2%	13.9%	15.5%	16.4%
Net Cash Per Share (Rs)	26.78	5.85	136.64	146.93	222.87
BVPS (Rs)	616.96	722.44	756.52	826.28	938.10
Gross Interest Cover	28.50	33.11	12.10	17.78	38.29
Effective Tax Rate	12.2%	8.9%	22.8%	14.0%	14.0%
Net Dividend Payout Ratio					
Accounts Receivables Days	66.95	59.93	63.20	65.21	66.38
Inventory Days	215.51	232.17	208.77	192.29	196.96
Accounts Payables Days	105.56	97.91	86.97	82.25	80.45
ROIC (%)	17.0%	14.6%	12.0%	13.9%	15.4%
ROCE (%)	19.5%	16.7%	11.7%	14.7%	15.6%
Return On Average Assets	15.5%	13.4%	8.6%	11.1%	11.8%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

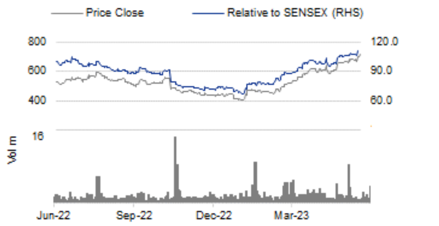
India

ADD *(no change)*

Consensus ratings*:	Buy 23	Hold 6	Sell 1

Current price:	Rs721
Target price:	Rs793
Previous target:	Rs553
Up/downside:	10.0%
InCred Research / Consensus:	19.6%
Reuters:	
Bloomberg:	ARBP IN
Market cap:	US$5,152m
	Rs422,667m
Average daily turnover:	US$14.6m
	Rs1194.1m
Current shares o/s:	585.9m
Free float:	4,817.0%

Source: Bloomberg



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	17.3	44.1	37.0
Relative (%)	16.4	32.0	15.7

Major shareholders	% held
Promoters	51.8
LIC	5.6
HDFC MF	3.1

Aurobindo Pharma

US product mix is improving

- Aurobindo Pharma is best positioned to benefit from improving US generic market dynamics; the share of complex products is improving in the US mix.
- Margins should recover by ~280bp from the FY23 base over the next two years. Improving US mix, receding raw material prices and gRevlimid launch are key growth drivers.
- The valuation is still at a discount to its five-year average. Resume coverage on the stock with an ADD rating and a target price of Rs793.

Successful US generics franchise; mix shifts to complex generics

In an era marked by diminishing fortunes for many industry players, Aurobindo Pharma or ARBP has emerged as a standout success story in the last decade, growing at an 8% CAGR since FY15, despite a large base. A robust but still a low-cost manufacturing base, one of the best R&D productivity levels in the industry, a robust supply chain and one of the widest product baskets have been some of the pillars of this strong growth. Further, ARBP's ability to compete and gain market share in the commodity generics segment and low product concentration profile have also protected it against any large-scale price erosion in the past. The company is now fast graduating into complex generics, led by its filings in injectables, peptides, biosimilars and penems. These, along with the recent PLI-related capex for PenG (US$250m in total), should start contributing meaningfully and lead to positive FCF from FY25F.

Margins likely to improve by ~280bp over FY23-25F

ARBP is one of the biggest beneficiaries of the current US generic market dynamics, given its strong presence in injectables where there is a significant shortage in the market, and a wide product basket which helps it get opportunistic business opportunities. These opportunities are medium-term in nature and come with a much better margin profile. Further, Eugia, which houses its injectables portfolio, is likely to witness strong double-digit growth in FY24F; Eugia has a gross margin of 60-70% and an EBITDA margin of 25-35%, much above company-level margins. Receding raw material cost, gRevlimid launch in Oct 2023F and biosimilar launches by the end of FY24F and FY25F should further support margins, driving a likely improvement of ~280bp over FY23-25F.

Resume coverage on the stock with an ADD rating

ARBP trades at 14.5x FY25F EPS, at a significant discount to peers. While a US-driven base warrants discount to peers, we believe ARBP is at an inflection point with its complex generics portfolio about to take off, which should drive a sharp improvement in profitability/return ratios. Further, culmination of the production-linked incentive or PLI-linked capex by FY25F should lead to a positive FCF. We value the stock at 16x FY25F EPS and resume coverage on it with an ADD rating and a target price of Rs793. Any marked slowdown in the US business or a spike in price erosion are key downside risks.

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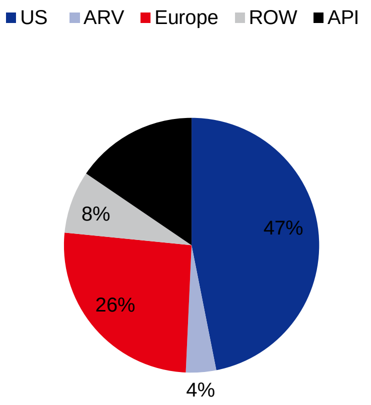
Financial Summary	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue (Rsm)	247,746	234,555	248,554	273,617	296,069
Operating EBITDA (Rsm)	53,334	43,867	37,582	46,358	52,870
Net Profit (Rsm)	53,444	26,481	19,275	24,609	29,568
Core EPS (Rs)	55.2	47.4	32.9	42.0	50.5
Core EPS Growth	12.7%	(14.2%)	(30.6%)	27.7%	20.2%
FD Core P/E (x)	13.07	15.23	21.93	17.18	14.29
DPS (Rs)	2.5	9.0	7.5	6.0	7.0
Dividend Yield	0.35%	1.25%	1.04%	0.83%	0.97%
EV/EBITDA (x)	7.81	9.10	10.78	8.59	7.20
P/FCFE (x)	6.24	9.37	26.71	(44.88)	13.44
Net Gearing	(2.3%)	(7.0%)	(5.2%)	(7.2%)	(12.3%)
P/BV (x)	1.93	1.72	1.57	1.47	1.35
ROE	16.7%	11.9%	7.5%	8.8%	9.8%
% Change In Core EPS Estimates				1.75%	12.72%
InCred Research/Consensus EPS (x)					

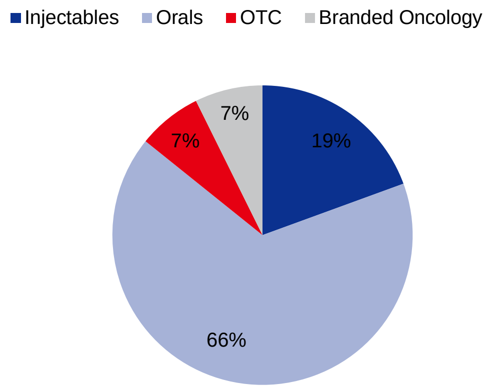
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 77: Geographical revenue break-up



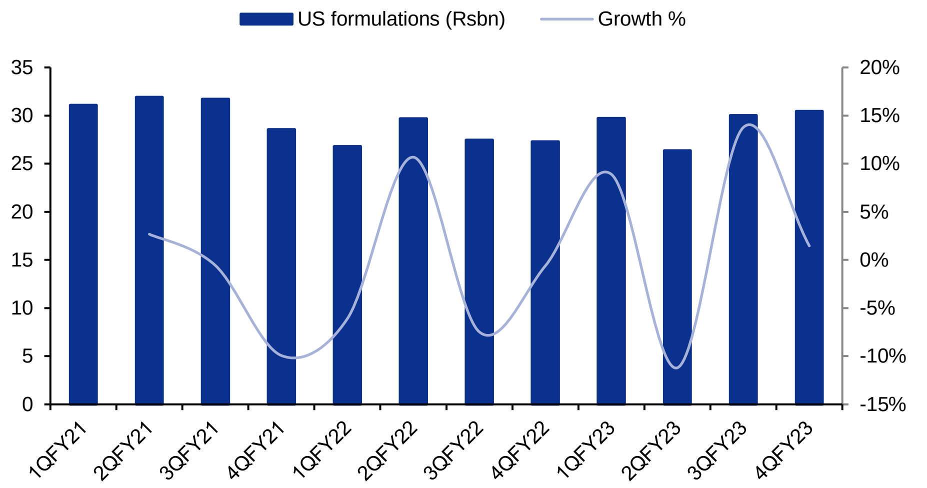
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 78: US business dominated by oral dosage



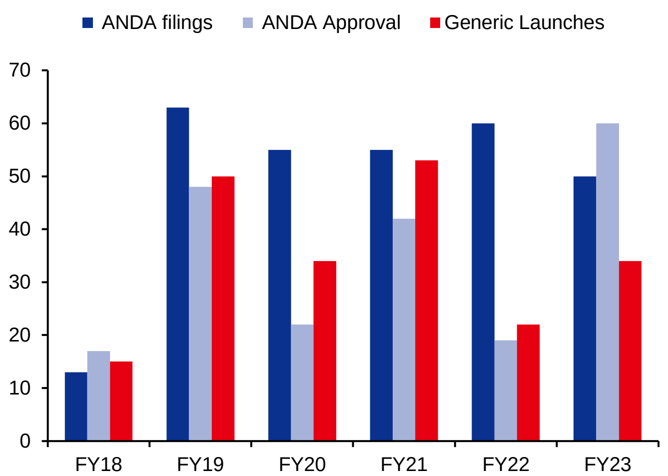
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 79: ARBP's US revenue is gradually picking up pace again post channel inventory ramp-down by customers after the Covid-19 pandemic



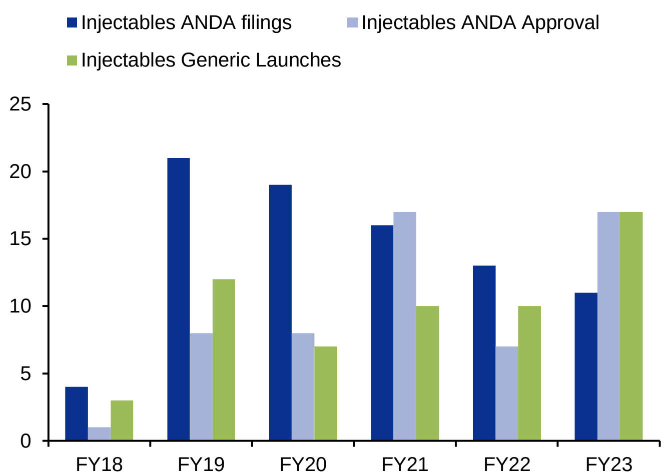
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 80: US ANDA filings data – one of the most aggressive product filings and high approval rate



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 81: US injectable filings – focusing heavily on the US injectables segment



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 82: Therapy-wise breakdown of ANDA filings

Therapy	ANDAs	Addressable market Size (US$ Bn)
CNS	140	26.7
ARV	38	0.6
CVS	109	38.8
SSP & Cephs	33	0.8
Anti-Diabetic	23	30.9
Oncology & Hormones	65	15.8
Gastroenterological	43	4
Controlled Substances	16	0.9
Respiratory (incl. Nasal)	1	1.5
Ophthalmic	17	4.7
Dermatology	9	1
Penem injectables	2	0.2
Others	264	23.8
	774	149.7

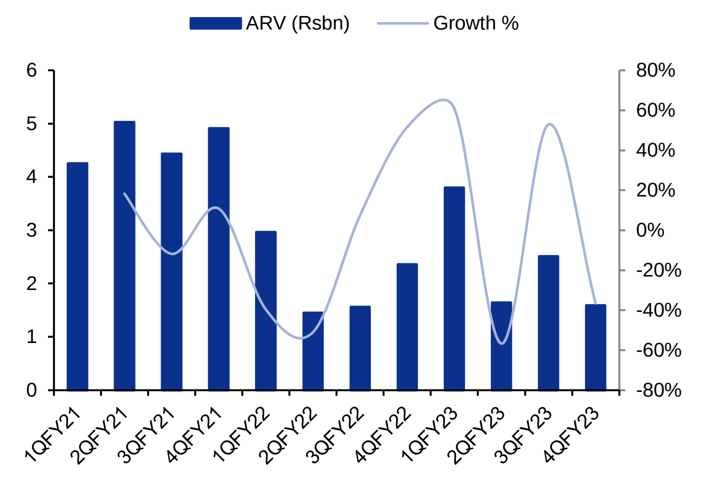
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 83: Plant-wise details of filings

Site	Details	Final Approval	Tentative Approval	Under Review	Total
Unit III	Oral Formulations	118	7	7	132
Unit VIB	Cephalosphorins Oral	11	0	2	13
Unit VII (SEZ)	Oral Formulations	147	10	17	174
Unit XII	Penicillin Oral & Injectables	21	0	1	22
Aurolife & Aurolife – II	Orals & topicals	24	0	11	35
APL HC I	Oral Formulations	15	2	16	33
APL HC III	Orals & topicals	1	0	3	4
APL HC IV	Oral Formulations	49	6	56	111
Eugia I	Oral & Injectable Formulations	31	6	20	57
Eugia II	Penem Injectables	2	0	0	2
Eugia III	Injectables & Ophthalmics	98	3	39	140
Wytells	Injectable	0	0	1	1
Others		48	0	2	50
Total		565	34	175	774

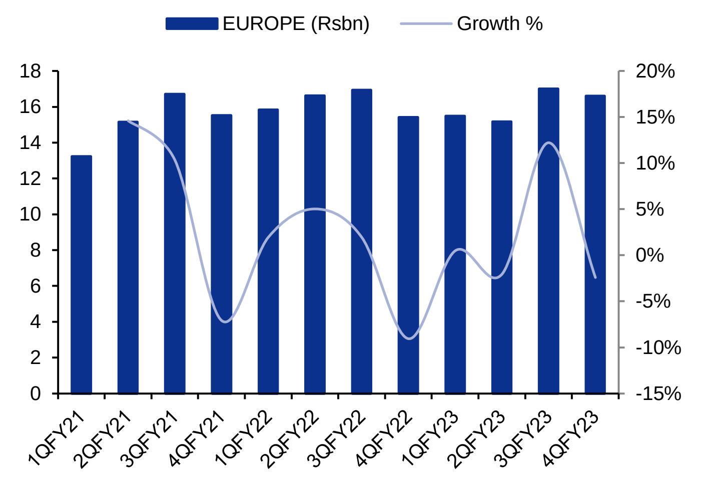
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 84: ARV revenue is tender-driven and volatile



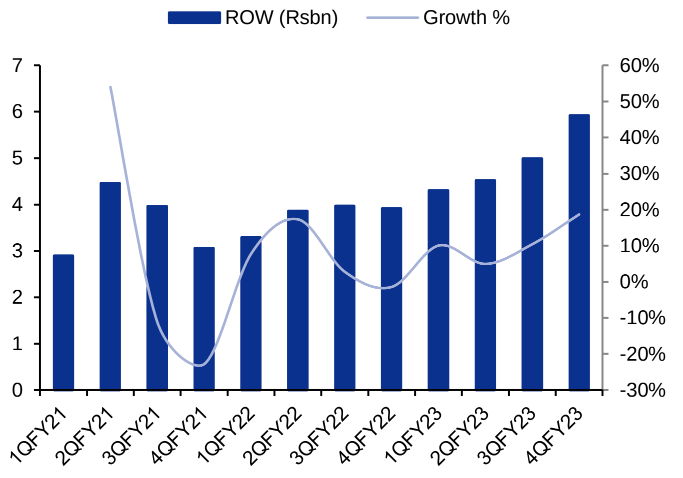
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 85: Europe revenue is steady and gradually ramping up



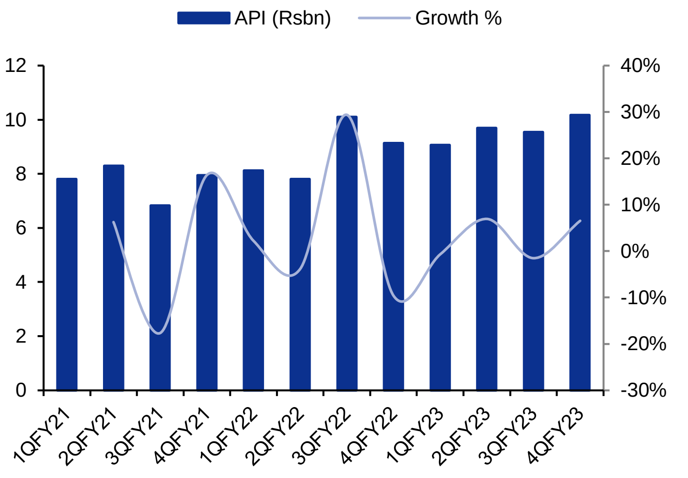
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 86: ROW revenue – steady improvement



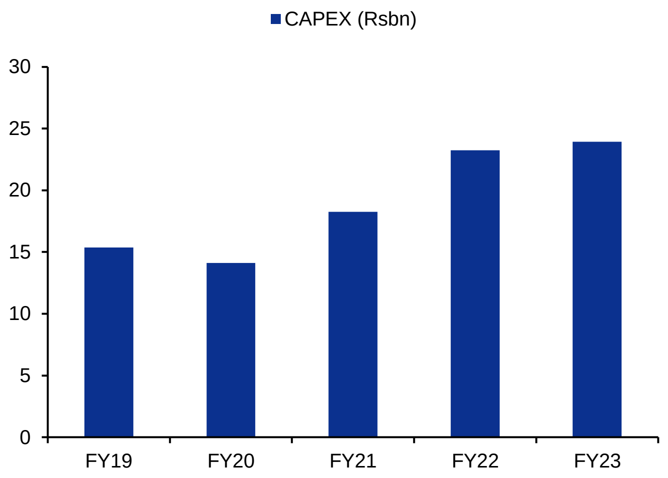
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 87: API revenue – mostly for captive consumption



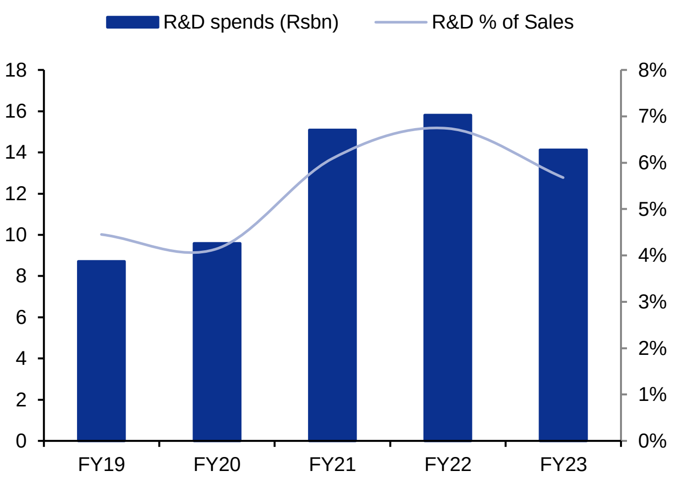
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 88: Capex trend – high intensity in recent times due to PLI-related capex of US$250-260m which should get over by early FY25F



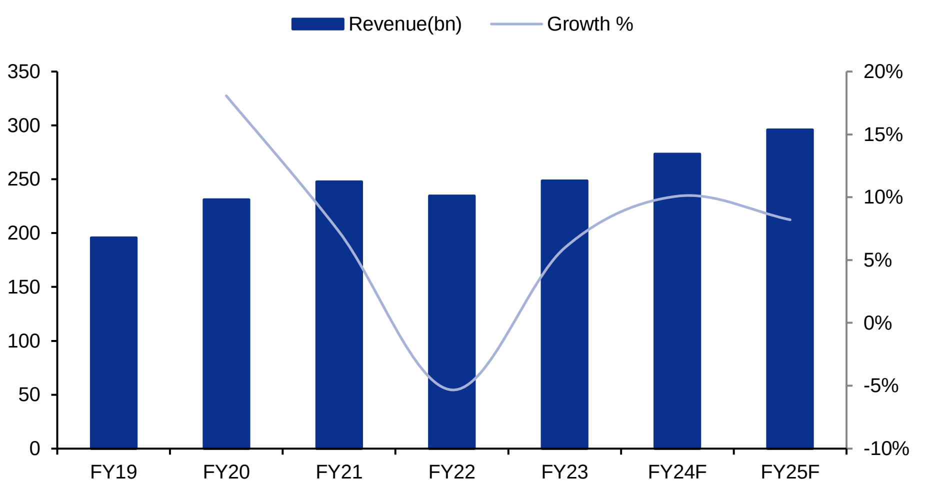
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 89: R&D spending trend – one of the best R&D productivities in the industry



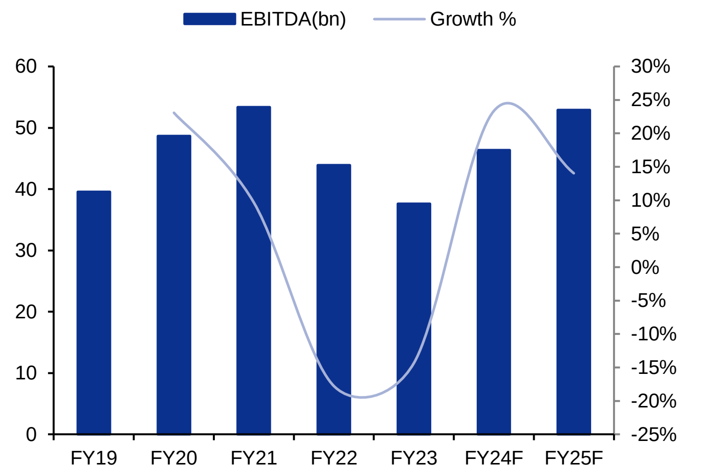
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 90: A solid success story in the US, with consistent scale-up despite a high base



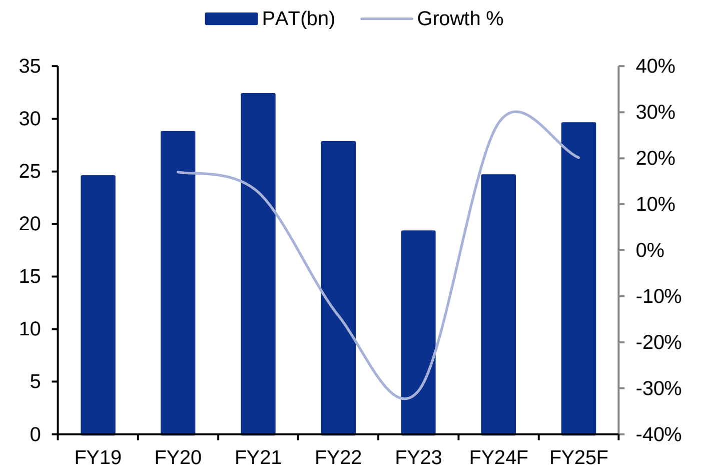
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 91: FY23 was impacted by high price erosion in 1H, but this has now reversed



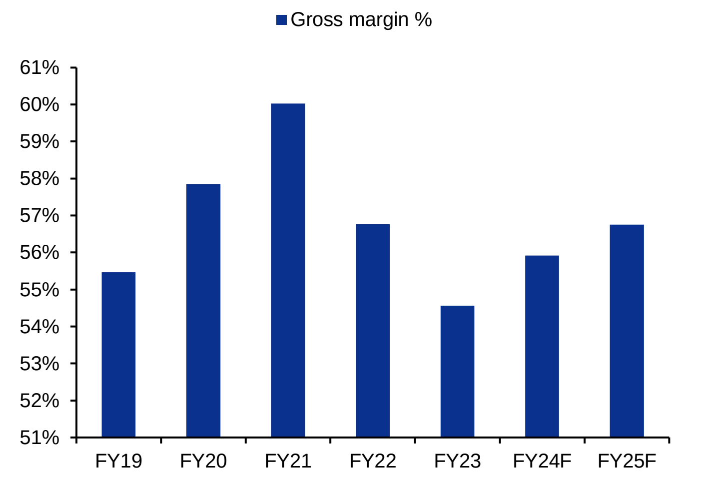
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 92: PAT declined in FY23 due to high price erosion in the US; expect strong growth in FY24F-25F



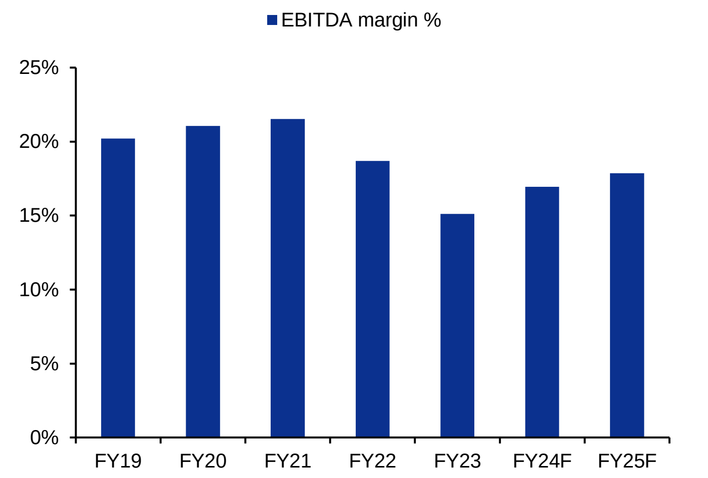
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 93: Gross margin – FY21 was an aberrational year due to the Covid-19 pandemic



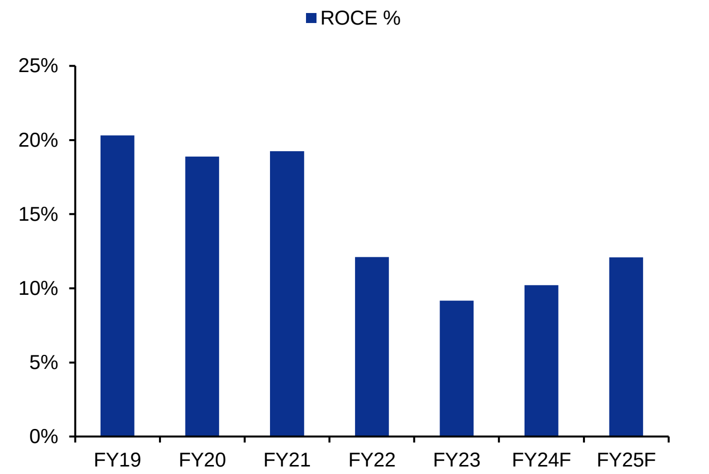
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 94: EBITDA margin trend – FY23 was impacted due to high price erosion in the US in 1H



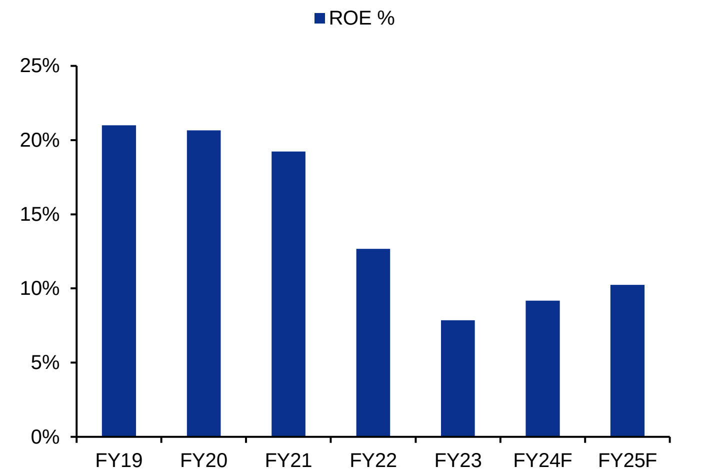
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 95: RoCE trend – PLI-related capex yet to pay off



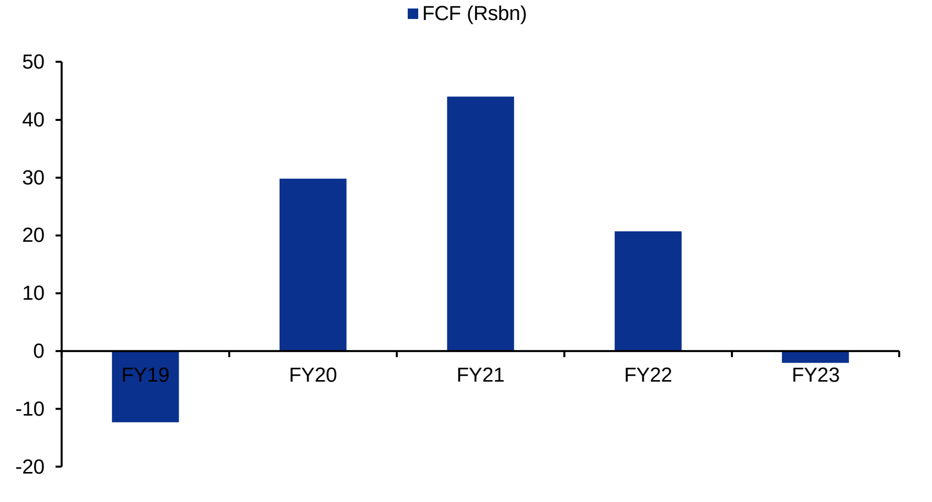
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 96: RoE trend of ARBP



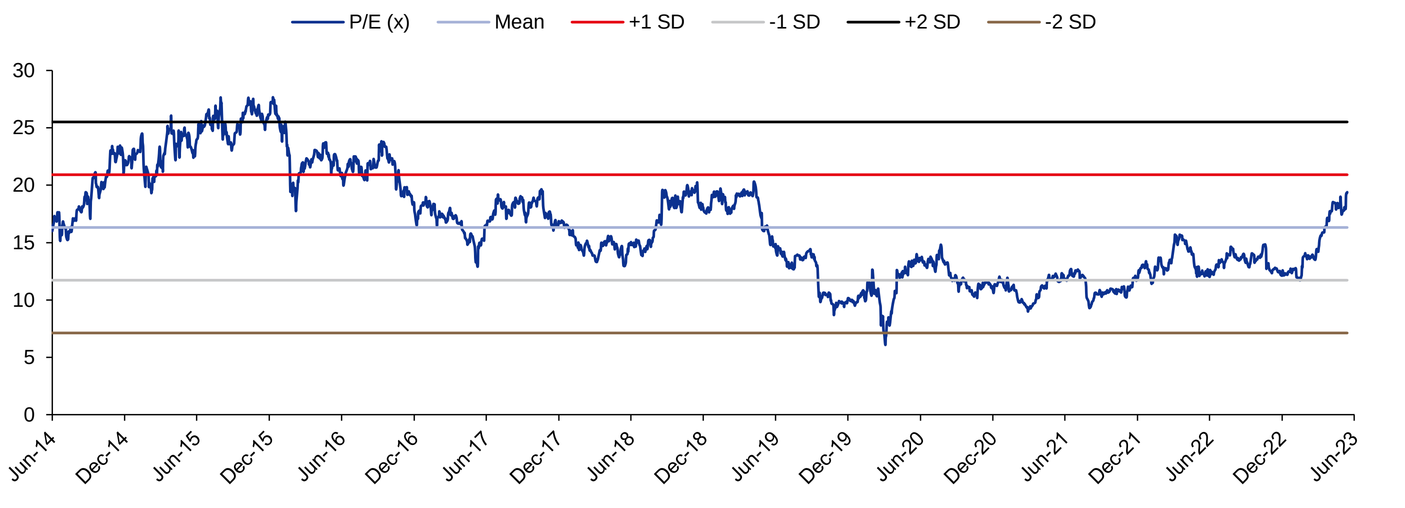
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 97: FCF generation trend – one of the key focus areas now



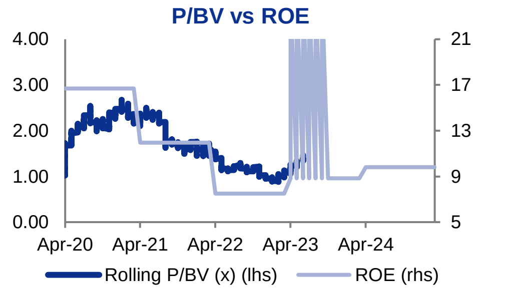
SOURCE: INCRED RESEARCH, COMPANY REPORTS

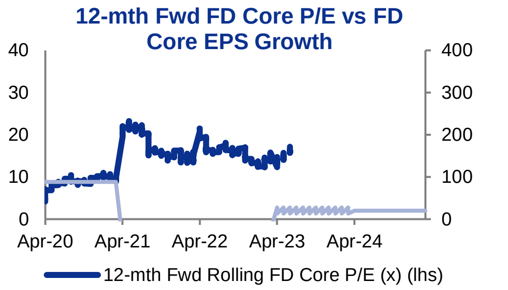
Figure 98: One-year forward P/E of Aurobindo Pharma



SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Net Revenues	**247,746**	**234,555**	**248,554**	**273,617**	**296,069**
Gross Profit	**148,722**	**133,152**	**135,621**	**152,992**	**168,035**
Operating EBITDA	**53,334**	**43,867**	**37,582**	**46,358**	**52,870**
Depreciation And Amortisation	(10,554)	(11,265)	(12,446)	(14,000)	(15,000)
Operating EBIT	**42,780**	**32,602**	**25,136**	**32,358**	**37,870**
Financial Income/(Expense)	(745)	(486)	(1,405)	(1,200)	(600)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	3,807	3,204	2,510	2,000	2,500
Profit Before Tax (pre-EI)	**45,843**	**35,319**	**26,242**	**33,158**	**39,770**
Exceptional Items					
Pre-tax Profit	**45,843**	**35,319**	**26,242**	**33,158**	**39,770**
Taxation	(13,057)	(7,256)	(6,849)	(8,290)	(9,943)
Exceptional Income - post-tax	21,105	(1,280)			
Profit After Tax	**53,891**	**26,783**	**19,393**	**24,869**	**29,828**
Minority Interests	(447)	(302)	(118)	(260)	(260)
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**53,444**	**26,481**	**19,275**	**24,609**	**29,568**
Recurring Net Profit	32,339	27,761	19,275	24,609	29,568
Fully Diluted Recurring Net Profit	**32,339**	**27,761**	**19,275**	**24,609**	**29,568**

Cash Flow

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
EBITDA	53,334	43,867	37,582	46,358	52,870
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(10,666)	15,578	(10,950)	(5,754)	(8,244)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	31,401	1,612	(7,305)	(9,225)	(9,712)
Net Interest (Paid)/Received	(745)	(486)	(1,405)	(1,200)	(600)
Tax Paid	(40,033)	(10,406)	(9,350)	(12,103)	(10,619)
Cashflow From Operations	**33,291**	**50,165**	**8,573**	**18,077**	**23,697**
Capex	(18,256)	(23,237)	(23,927)	(21,500)	(15,000)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments	28,997	(6,248)	(1,970)		
Other Investing Cashflow					
Cash Flow From Investing	**44,031**	**20,680**	**(17,323)**	**(3,423)**	**8,697**
Debt Raised/(repaid)	(9,601)	(25,724)	24,576	(24,073)	(933)
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid	(2,343)	(2,637)	(4,395)	(4,395)	(3,516)
Preferred Dividends					
Other Financing Cashflow	(5,764)	(1,246)	(1,491)	800	1,900
Cash Flow From Financing	**(17,709)**	**(29,607)**	**18,690**	**(27,667)**	**(2,549)**
Total Cash Generated	26,323	(8,927)	1,367	(31,090)	6,148
Free Cashflow To Equity	**67,721**	**45,121**	**15,826**	**(9,418)**	**31,460**
Free Cashflow To Firm	**78,067**	**71,332**	**(7,345)**	**15,855**	**32,993**

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Cash And Equivalents	54,743	45,816	62,476	45,364	62,239
Total Debtors	35,033	40,123	44,664	46,515	50,332
Inventories	90,266	75,539	85,112	98,502	106,585
Total Other Current Assets	18,194	19,750	23,204	19,153	20,725
Total Current Assets	**198,235**	**181,227**	**215,457**	**209,534**	**239,881**
Fixed Assets	93,155	106,660	124,918	132,418	132,418
Total Investments	947	6,183	3,917	3,917	3,917
Intangible Assets	31,196	36,133	39,219	39,219	39,219
Total Other Non-Current Assets	15,007	9,014	15,389	15,389	15,389
Total Non-current Assets	**140,305**	**157,990**	**183,443**	**190,943**	**190,943**
Short-term Debt	48,027	22,835	42,426	42,426	42,426
Current Portion of Long-Term Debt					
Total Creditors	27,947	27,031	38,713	43,305	46,209
Other Current Liabilities	30,678	31,695	33,799	34,644	36,967
Total Current Liabilities	**106,651**	**81,560**	**114,938**	**120,374**	**125,602**
Total Long-term Debt	1,684	5,678	6,190	(17,883)	(18,817)
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	10,915	6,239	9,254	9,254	9,254
Total Non-current Liabilities	**12,599**	**11,917**	**15,444**	**(8,629)**	**(9,563)**
Total Provisions					
Total Liabilities	**119,250**	**93,477**	**130,381**	**111,745**	**116,039**
Shareholders Equity	219,299	245,760	268,399	288,353	314,145
Minority Interests	(9)	(19)	120	380	640
Total Equity	**219,290**	**245,741**	**268,519**	**288,733**	**314,785**

Key Ratios

	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue Growth	7.3%	(5.3%)	6.0%	10.1%	8.2%
Operating EBITDA Growth	9.7%	(17.8%)	(14.3%)	23.4%	14.0%
Operating EBITDA Margin	21.5%	18.7%	15.1%	16.9%	17.9%
Net Cash Per Share (Rs)	8.59	29.53	23.66	35.54	65.93
BVPS (Rs)	374.27	419.43	458.07	492.12	536.14
Gross Interest Cover	57.43	67.03	17.89	26.97	63.12
Effective Tax Rate	28.5%	20.5%	26.1%	25.0%	25.0%
Net Dividend Payout Ratio					
Accounts Receivables Days	57.59	58.48	62.25	60.82	59.70
Inventory Days	308.26	298.41	259.61	277.80	292.33
Accounts Payables Days	98.41	98.94	106.24	124.09	127.59
ROIC (%)	14.3%	10.7%	7.2%	8.9%	10.1%
ROCE (%)	17.4%	12.0%	8.5%	10.3%	11.6%
Return On Average Assets	10.6%	8.4%	5.5%	6.4%	7.3%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

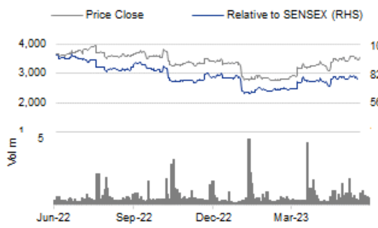
India

HOLD *(previously REDUCE)*

Consensus ratings*:	Buy 8	Hold 7	Sell 9

Current price:	Rs3,534
Target price: ▲	Rs3,487
Previous target:	Rs2,218
Up/downside:	-1.3%
InCred Research / Consensus:	15.1%
Reuters:	
Bloomberg:	DIVI IN
Market cap:	US$11,436m
	Rs938,259m
Average daily turnover:	US$24.7m
	Rs2026.0m
Current shares o/s:	265.5m
Free float:	48.0%

Source: Bloomberg



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	0.6	25.9	(4.0)
Relative (%)	(0.2)	15.3	(18.9)

Major shareholders	% held
Promoters	52.0
SBI MF	7.8
LIC	5.6

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Divi's Laboratories

Revenue recovery + cost normalization

- FY23F-25F to see a sharp recovery, as a couple of custom synthesis projects take shape, sartans portfolio picks up pace and raw material cost pressure subsides.
- Structurally, best positioned to benefit from the rising outsourcing trend; recent capex intensity is a testimony of the opportunities that lie ahead.
- Current valuation bakes in the recovery. Await a better entry point. Resume coverage with a HOLD rating (REDUCE earlier) and a target price of Rs3,487.

FY24F-25F should stage a strong comeback after a dismal FY23

FY23 was a washout year for Divi's Laboratories (DLL), hit by a large Covid-driven base, high-cost raw material inventory, rise in freight cost and increased pricing pressure as customers disposed high-channel inventory before shelf-life expiry. We see most of these problems subsiding and FY24F-25F should see a strong comeback led by depletion of high-cost inventory, normalization of logistics costs and reduced pricing pressure. More importantly, DLL should see revenue recovery led by a sartans contract with a big pharma company and commercialization of a couple of projects in the CCS business. We expect its earnings to post a 16% CAGR over FY23F-25F.

Strongly positioned to benefit from increased outsourcing

Over the last couple of years, DLL has a) invested in the back-end (intermediates/KSMs for larger products, thereby reducing its dependency on China), b) expanded capacity for sartans (DLL believes its sartans have a lower impurity level than peers), contrast media products (niche, but a large opportunity) and in products where it has a 20-30% market share currently but has the potential to achieve a 60-70% global market share, and c) invested in technologies/processes (upgradation of older plants, green chemistry, etc). This should allow it to have much better control of the supply chain, reduce manufacturing costs with better processes and gain market share with enhanced capacity. All this, combined with an almost clean compliance record (barring an import alert, which got resolved in a record nine months) and strong customer relationships, we believe, will make DLL strongly positioned to benefit from an increased outsourcing environment.

Margins should regain historical high level

We notice a sharp divergence in consensus margin estimates, ranging from 30% to 35% for FY25F and understandably so, given the limited information on key business variables. While the pace of margin recovery will depend on how fast DLL is able to monetize its recent capex, we feel, structurally, margins may head back to the historical level of 35%+.

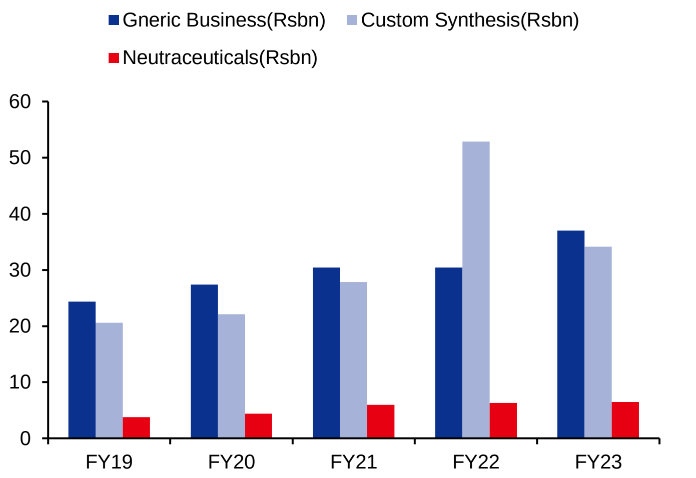
Fairly valued; resume coverage with a HOLD rating

Current valuation at 38x FY25F EPS fairly prices in the recovery. Wait for a better entry point. Resume coverage with a HOLD rating (REDUCE earlier) and a target price of Rs3,487. Slower-than-expected margin recovery is a downside risk. Large order in custom synthesis business is an upside risk.

Financial Summary	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue (Rsm)	69,694	89,598	77,675	84,192	94,916
Operating EBITDA (Rsm)	28,599	38,819	23,669	28,124	35,232
Net Profit (Rsm)	19,843	29,605	18,225	19,401	24,364
Core EPS (Rs)	74.7	111.5	68.6	73.1	91.8
Core EPS Growth	44.2%	49.2%	(38.4%)	6.5%	25.6%
FD Core P/E (x)	47.29	31.70	51.49	48.37	38.51
DPS (Rs)	0.0	0.0	0.0	0.0	0.0
Dividend Yield	0.00%	0.00%	0.00%	0.00%	0.00%
EV/EBITDA (x)	32.06	23.43	37.83	31.62	24.96
P/FCFE (x)	32.54	30.17	21.10	29.68	27.74
Net Gearing	(23.2%)	(24.0%)	(33.0%)	(34.7%)	(36.7%)
P/BV (x)	10.10	8.00	7.35	6.75	5.93
ROE	23.9%	28.2%	14.9%	14.5%	16.4%
% Change In Core EPS Estimates				1.08%	17.22%
InCred Research/Consensus EPS (x)					

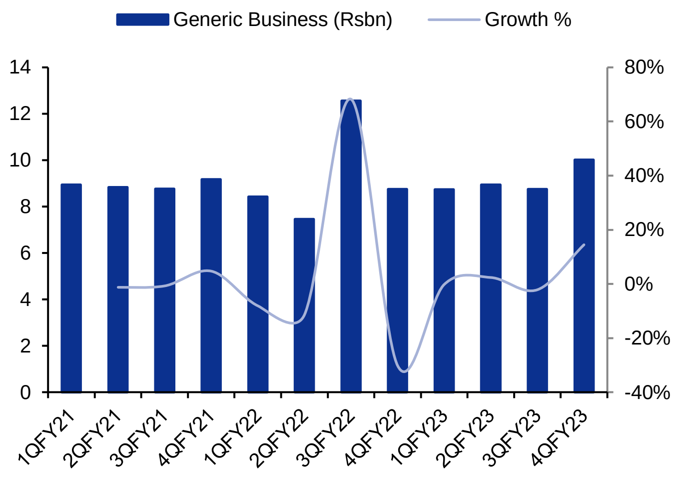
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 99: Business breakup – steady growth in all segments



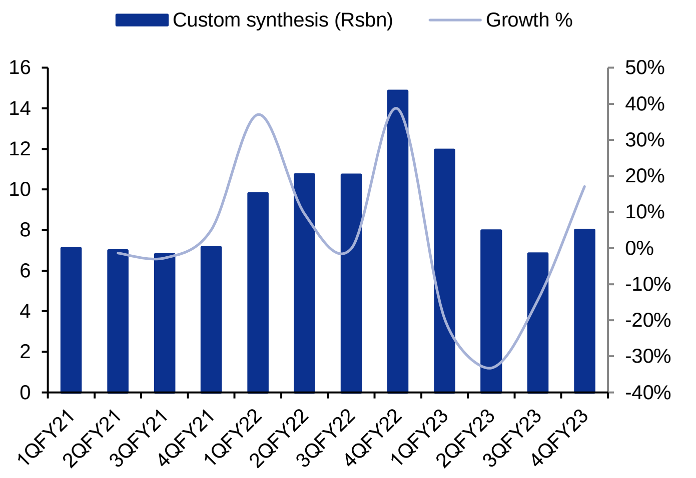
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 100: Generic business – impacted in FY23 due to high channel inventory



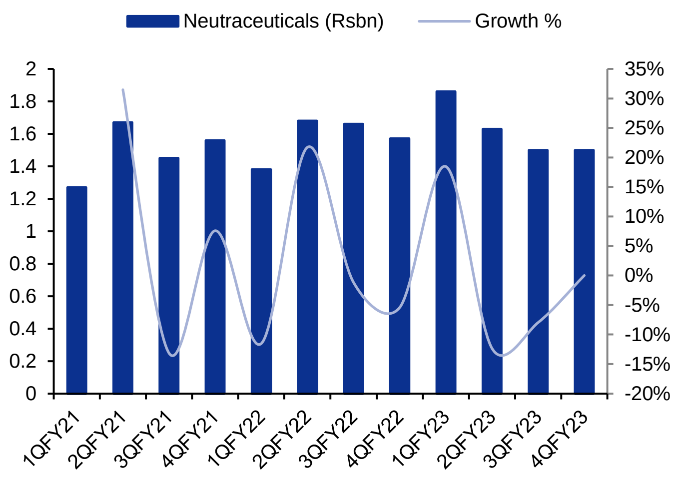
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 101: Custom synthesis business – cools off after a strong FY22 due to supply of Covid drug



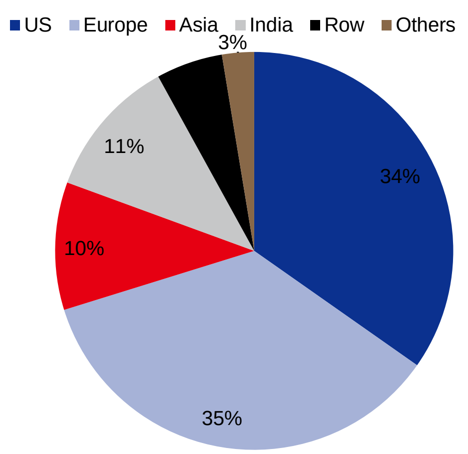
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 102: Nutraceuticals' performance – largely steady



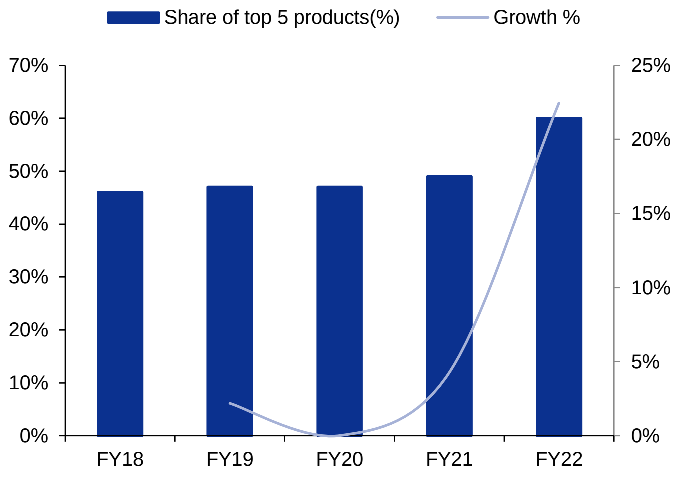
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 103: Geography-wise revenue break-up



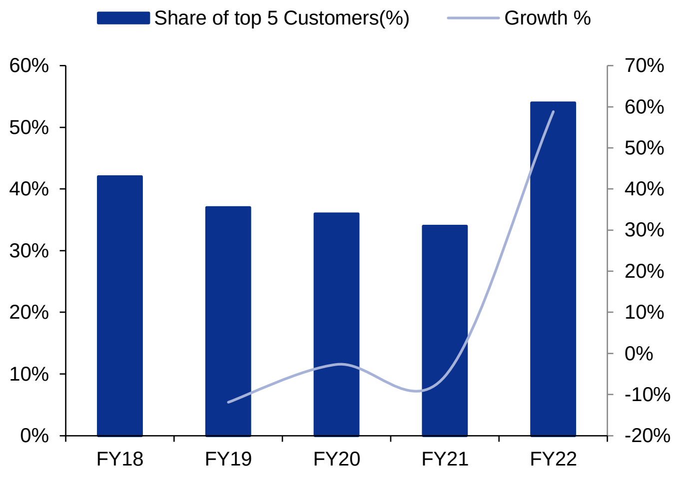
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 104: Share of top-5 products



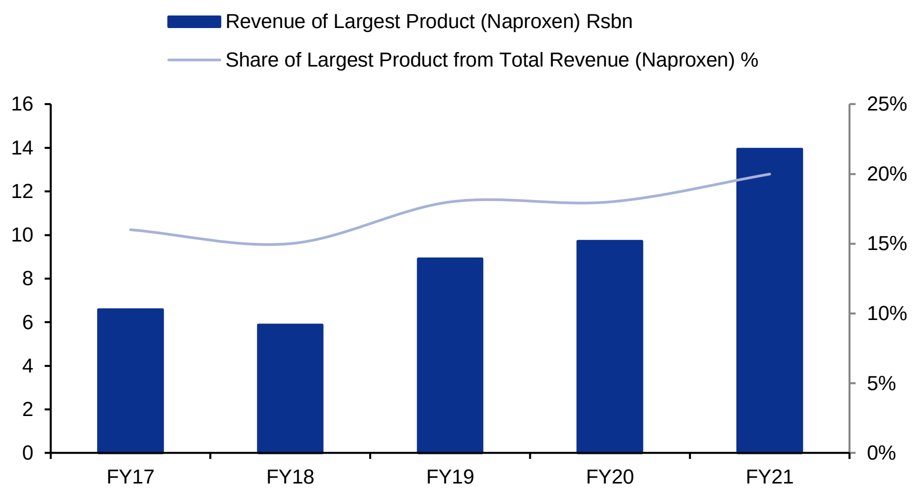
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 105: Share of top-5 customers



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 106: Performance of Naproxen, DLL's top product



NOTE- DLL HAS NOT GIVEN THE DATA ON ITS LARGEST PRODUCT FOR FY23
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 107: Contrast media capacity

API	Existing capacity (MTA) - Unit 1	Upcoming capacity (MTA) - Unit 3	Details
Iopromide	200	-	Included product to the list during FY19-21 capex plan.
Iopamidol	180	300	Old capacity of 180 mtpa mainly for exports to the EU and US clients for past several years. Another 300 mtpa to be added post Unit-3 completion in FY23-24F.
Iohexol	-	300	Had capacity of 15 mtpa in Unit 1 but was discontinued in FY19-20. New larger capacity to come on stream in Unit-3 from FY23-24F.

SOURCE: INCRED RESEARCH, COMPANY REPORTS

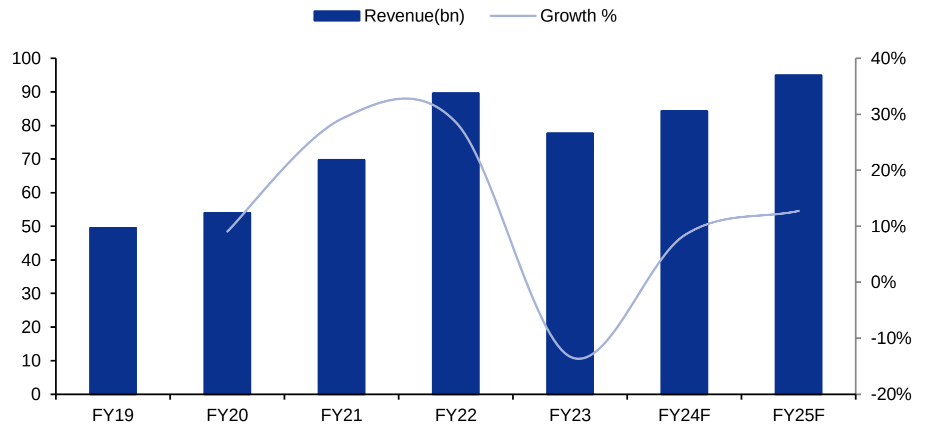
Figure 108: Key products in contrast media in the less competitive US market

API	Innovator	US DMF filers	API suppliers for Ex-US region
Iohexol	GE	Hovione and Zhejiang Starry	More than 10
Iopamidol	Bracco	Total 9 DMFs filed with USFDA including DLL, Abbott and Zhejiang Starry	More than 10
Iodixanol	GE	Imax Diagnostic and Jiangsu Hengrui	More than 10
Iopromide	Bayer	Daewoong Bio and Alp Pharma	More than 10

SOURCE: INCRED RESEARCH, COMPANY REPORTS

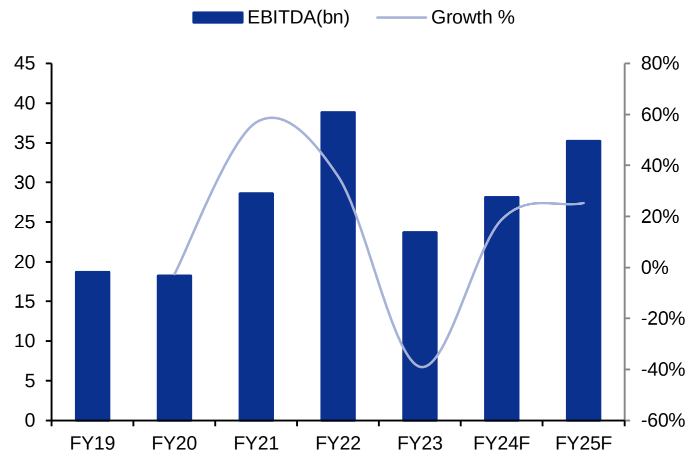
Expect the company to head back to its historical margin range of 35%+.

Figure 109: Steady scale-up in revenue; FY22 revenue was propped up by one-time supply of Covid drug



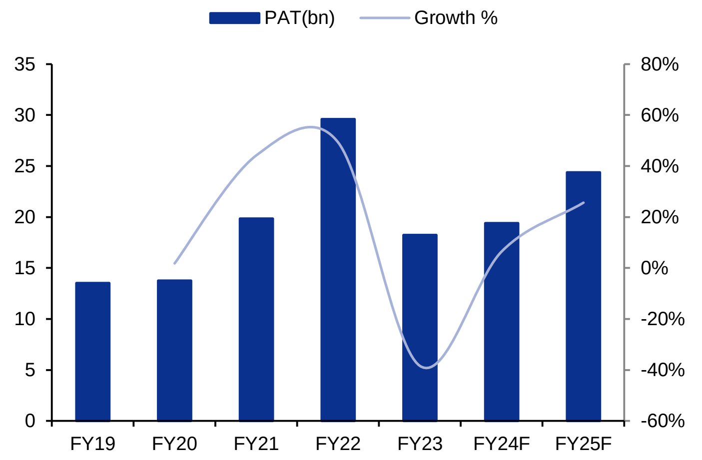
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 110: EBITDA impacted in FY23 due to high channel inventory - this is transient in nature and should normalize



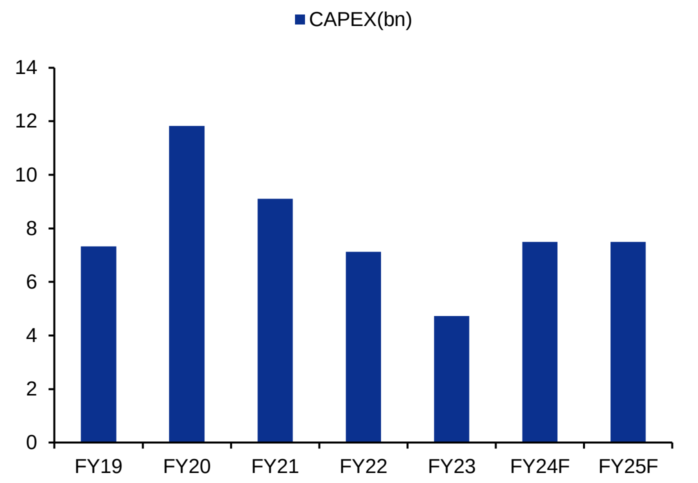
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 111: FY22 base impacted PAT growth in FY23



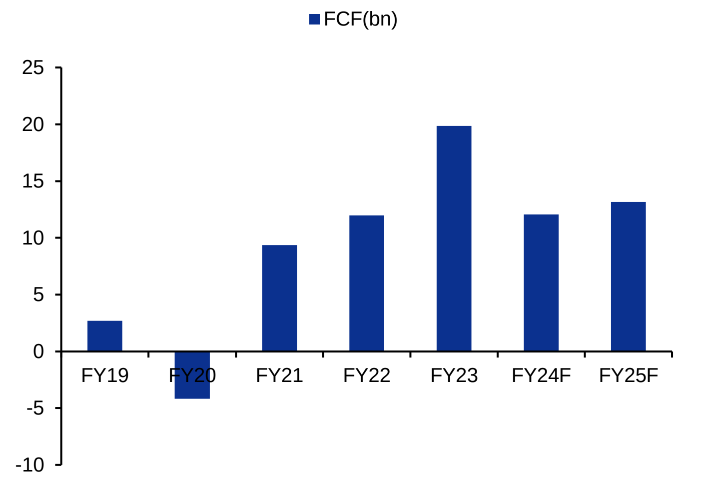
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 112: Huge capex intensity over the past five years



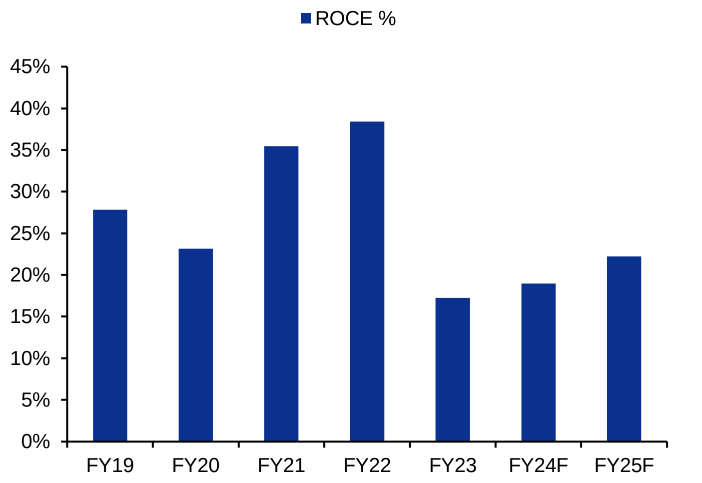
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 113: FCF generation over the past five years



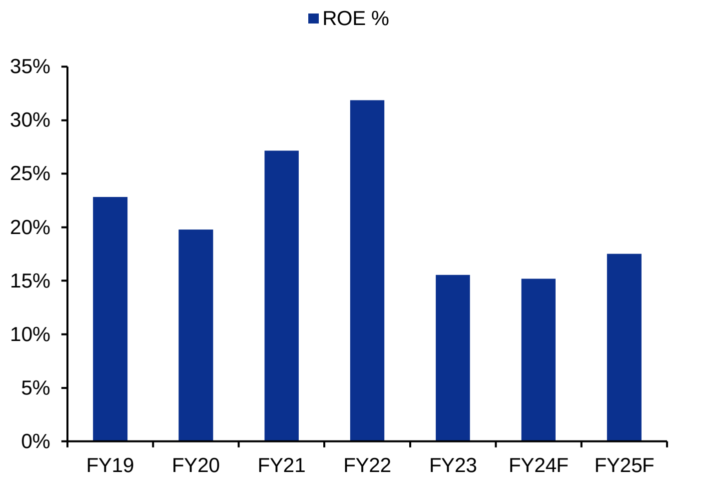
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 114: RoCE trend



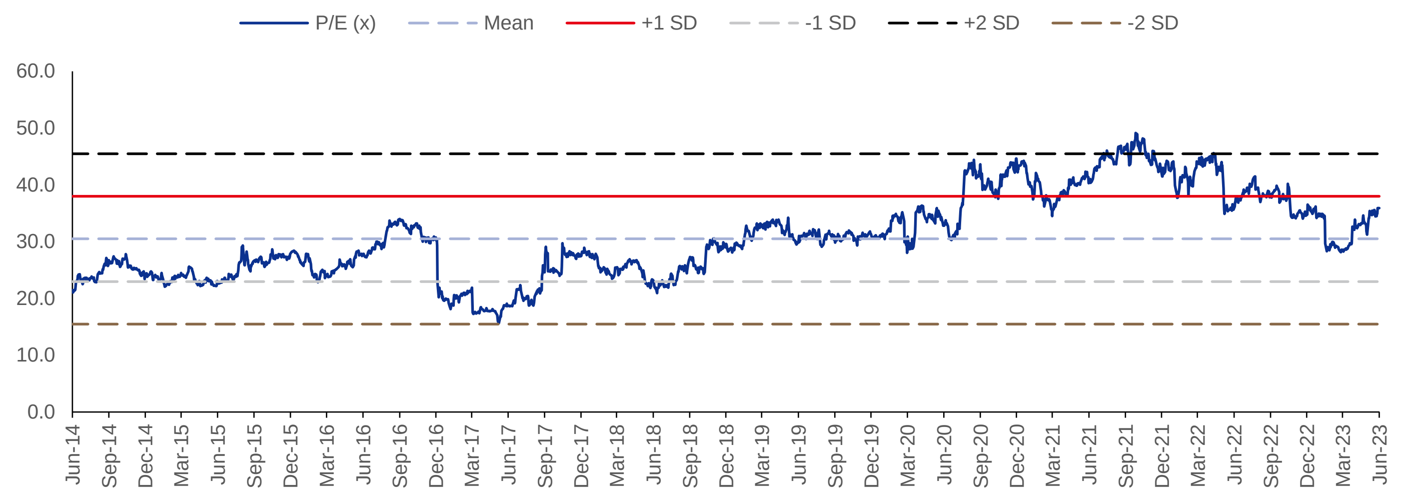
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 115: RoE trend



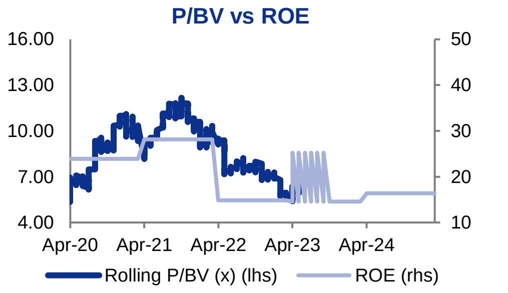
SOURCE: INCRED RESEARCH, COMPANY REPORTS

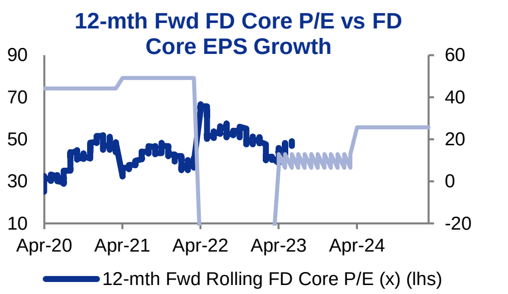
Figure 116: One-year forward P/E of Divi's Laboratories



SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Net Revenues	**69,694**	**89,598**	**77,675**	**84,192**	**94,916**
Gross Profit	**46,453**	**59,927**	**47,138**	**53,506**	**62,644**
Operating EBITDA	**28,599**	**38,819**	**23,669**	**28,124**	**35,232**
Depreciation And Amortisation	(2,556)	(3,115)	(3,432)	(3,900)	(4,300)
Operating EBIT	**26,044**	**35,704**	**20,237**	**24,224**	**30,932**
Financial Income/(Expense)	(9)	(8)	(7)	(7)	(7)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	626	1,139	3,447	2,000	2,000
Profit Before Tax (pre-EI)	**26,660**	**36,835**	**23,677**	**26,217**	**32,925**
Exceptional Items					
Pre-tax Profit	**26,660**	**36,835**	**23,677**	**26,217**	**32,925**
Taxation	(6,818)	(7,231)	(5,453)	(6,816)	(8,560)
Exceptional Income - post-tax					
Profit After Tax	**19,843**	**29,605**	**18,225**	**19,401**	**24,364**
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**19,843**	**29,605**	**18,225**	**19,401**	**24,364**
Recurring Net Profit	19,843	29,605	18,225	19,401	24,364
Fully Diluted Recurring Net Profit	**19,843**	**29,605**	**18,225**	**19,401**	**24,364**

Cash Flow

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
EBITDA	28,599	38,819	23,669	28,124	35,232
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(2,641)	(13,705)	4,188	(1,750)	(6,011)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	(6,489)	(5,997)	(3,260)	(6,816)	(8,560)
Net Interest (Paid)/Received	(9)	(8)	(7)	(7)	(7)
Tax Paid	(6,443)	(7,128)	(6,709)	(8,809)	(10,553)
Cashflow From Operations	**19,469**	**19,118**	**24,597**	**19,558**	**20,661**
Capex	(9,102)	(7,130)	(4,730)	(7,500)	(7,500)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	(1,000)				
Cash Flow From Investing	**9,367**	**11,988**	**19,867**	**12,058**	**13,161**
Debt Raised/(repaid)					
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid		(5,309)	(7,964)	(7,964)	(5,309)
Preferred Dividends					
Other Financing Cashflow	1,252	(50)	2,039	2,132	2,012
Cash Flow From Financing	**1,252**	**(5,360)**	**(5,925)**	**(5,832)**	**(3,298)**
Total Cash Generated	10,620	6,629	13,942	6,226	9,863
Free Cashflow To Equity	**28,837**	**31,106**	**44,465**	**31,616**	**33,822**
Free Cashflow To Firm	**28,845**	**31,114**	**44,471**	**31,623**	**33,829**

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Cash And Equivalents	21,560	28,189	42,131	48,357	58,220
Total Debtors	16,765	24,239	17,925	20,206	22,780
Inventories	21,452	28,286	30,004	28,625	32,271
Total Other Current Assets	1,969	2,801	3,057	3,368	3,797
Total Current Assets	**61,747**	**83,515**	**93,117**	**100,556**	**117,068**
Fixed Assets	44,053	47,875	49,292	52,892	56,092
Total Investments		720	771	771	771
Intangible Assets	92	75	53	53	53
Total Other Non-Current Assets	1,849	1,562	1,155	1,155	1,155
Total Non-current Assets	**45,994**	**50,232**	**51,270**	**54,870**	**58,070**
Short-term Debt	11	8			
Current Portion of Long-Term Debt					
Total Creditors	7,632	7,957	7,625	7,286	7,730
Other Current Liabilities	3,481	3,990	3,386	3,188	3,382
Total Current Liabilities	**11,125**	**11,956**	**11,011**	**10,474**	**11,112**
Total Long-term Debt		29		139	158
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	3,670	4,481	5,706	5,706	5,706
Total Non-current Liabilities	**3,670**	**4,510**	**5,706**	**5,845**	**5,864**
Total Provisions					
Total Liabilities	**14,795**	**16,465**	**16,717**	**16,319**	**16,976**
Shareholders Equity	92,946	117,282	127,671	139,108	158,162
Minority Interests					
Total Equity	**92,946**	**117,282**	**127,671**	**139,108**	**158,162**

Key Ratios

	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue Growth	29.2%	28.6%	(13.3%)	8.4%	12.7%
Operating EBITDA Growth	57.0%	35.7%	(39.0%)	18.8%	25.3%
Operating EBITDA Margin	41.0%	43.3%	30.5%	33.4%	37.1%
Net Cash Per Share (Rs)	81.16	106.03	158.69	181.61	218.69
BVPS (Rs)	350.08	441.74	480.87	523.95	595.72
Gross Interest Cover	2,993.51	4,463.04	3,020.51	3,318.42	4,237.24
Effective Tax Rate	25.6%	19.6%	23.0%	26.0%	26.0%
Net Dividend Payout Ratio					
Accounts Receivables Days	80.91	83.52	99.07	82.66	82.65
Inventory Days	314.82	305.93	348.36	348.69	344.38
Accounts Payables Days	106.32	95.88	93.12	88.68	84.92
ROIC (%)	26.0%	28.8%	16.7%	18.9%	22.0%
ROCE (%)	31.3%	34.0%	16.5%	18.2%	20.8%
Return On Average Assets	20.6%	24.5%	13.1%	12.9%	14.7%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

India

REDUCE *(previously HOLD)*

Consensus ratings*:	Buy 20 Hold 11 Sell 10
Current price:	Rs5,042
Target price: ▲	Rs4,656
Previous target:	Rs4,556
Up/downside:	-7.7%
InCred Research / Consensus:	-6.7%
Reuters:	REDY.NS
Bloomberg:	DRRD IN
Market cap:	US$10,234m
	Rs839,652m
Average daily turnover:	US$20.0m
	Rs1641.1m
Current shares o/s:	166.4m
Free float:	73.3%

Source: Bloomberg

Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	11.3	12.9	17.0
Relative (%)	10.4	3.4	(1.2)

Major shareholders	% held
Promoters	26.7
LIC	9.7
First State	2.5

Dr Reddy's Laboratories Ltd

Weak core profitability

- The 4QFY23 results, post expiry of gRevlimid marketing exclusivity, gave some sense on core EBITDA margin which, in our view, is at ~15-16% (ex-gRevlimid and one-time divestment-related income), much below expectations.
- gRevlimid contributes around one-third to our FY25F EPS. While the medium-term performance will continue to remain elevated due to gRevlimid, there is limited visibility on turnaround triggers in the base business profitability.
- We value the stock at 22x FY25F base EPS & gRevlimid earnings at 10x multiple to arrive at a TP of Rs4,656. Resume coverage with a REDUCE rating.

Base business profitability under pressure

Dr. Reddy's Laboratories or DRL's FY23 performance was supported by strong contribution from gRevlimid (180-day marketing exclusivity in two strengths) but 4QFY23 margins, post incremental competition in the product, gave some clear sense on the base business profitability which, we believe, is at ~15-16% margin (ex-gRevlimid and one-time brand divestment income), much weaker than what we expected. FY23 saw a meaningful increase in R&D/SG&A spending, which should broadly continue. Further, likely incremental competition in high-value products like gVascepa and gCiprodex should keep margins under pressure. Adjusted for one-time brand divestment income, we expect a 70bp decline in margins over FY23-25F.

Thrust on non-US franchise encouraging, but the shift to be gradual

DRL is gradually shifting away from US generics with its incremental capital allocation largely happening in emerging markets, thereby attempting to have a more sustainable and a more profitable franchise. It is probably the only Indian company to have a meaningful presence in two large emerging markets outside India, i.e., Russia and China. This is a key change in strategy - where growth was dependent on select high-risk assets historically, efforts are now directed to have a more broad-based growth approach across markets with specific focus on India and other emerging markets. We like the thrust on non-US franchise, but also acknowledge that the US will continue to remain a meaningful contributor to earnings in the medium term with a meaningful shift in the geography mix still three-to-five years away.

Resume coverage with a REDUCE rating

After an elongated period of cost rationalization/reduced investments (flat SG&A spending from FY15-21), the spending is picking up pace again, thereby exerting pressure on the base business profitability. While strong gRevlimid sales will mask weak base business profitability in the medium term, we await signs of improvement in core margins before turning constructive. We value the stock at 22x FY25F core EPS – in line with its historical range, and gRevlimid earnings at 10x multiple to arrive at our target price of Rs4,656. We resume coverage with a REDUCE rating (HOLD earlier) on the stock. Faster-than-expected improvement in the base business profitability is an upside risk.

Financial Summary	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue (Rsm)	189,722	214,391	245,879	263,503	279,036
Operating EBITDA (Rsm)	44,775	46,054	63,873	63,308	66,299
Net Profit (Rsm)	19,149	23,568	45,067	41,276	43,899
Core EPS (Rs)	155.7	186.8	270.8	248.0	263.8
Core EPS Growth	(20.4%)	19.9%	45.0%	(8.4%)	6.4%
FD Core P/E (x)	32.38	27.00	18.62	20.33	19.11
DPS (Rs)	25.0	30.0	70.0	35.0	40.0
Dividend Yield	0.50%	0.60%	1.39%	0.69%	0.79%
EV/EBITDA (x)	18.55	17.87	12.28	12.36	11.26
P/FCFE (x)	12.76	18.46	10.54	17.99	10.10
Net Gearing	(2.9%)	(6.5%)	(21.5%)	(19.6%)	(28.9%)
P/BV (x)	4.80	4.40	3.63	3.22	2.80
ROE	15.7%	17.0%	21.4%	16.8%	15.7%
% Change In Core EPS Estimates				(5.64%)	(8.16%)
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Analyst(s)

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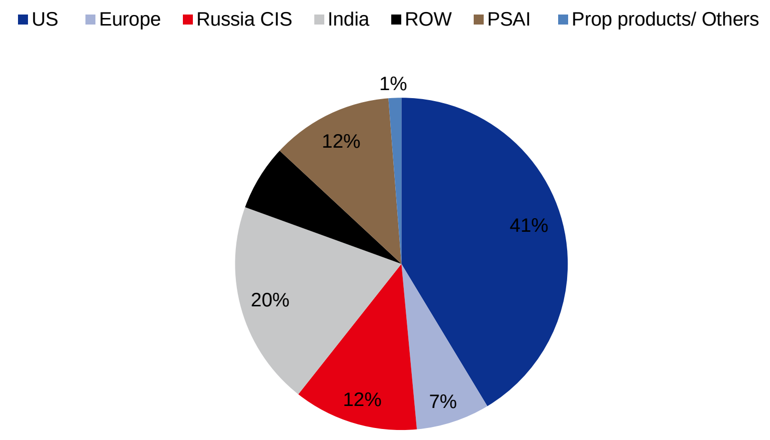
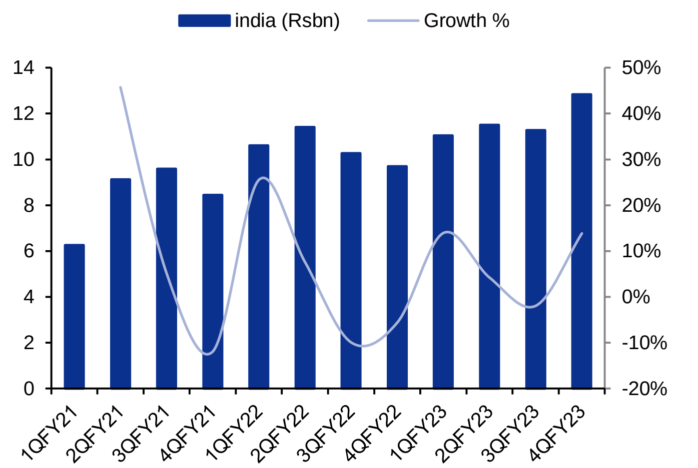
Figure 117: Geography-wise revenue breakup – gradually moving away from US generics, but it is still a meaningful contributor



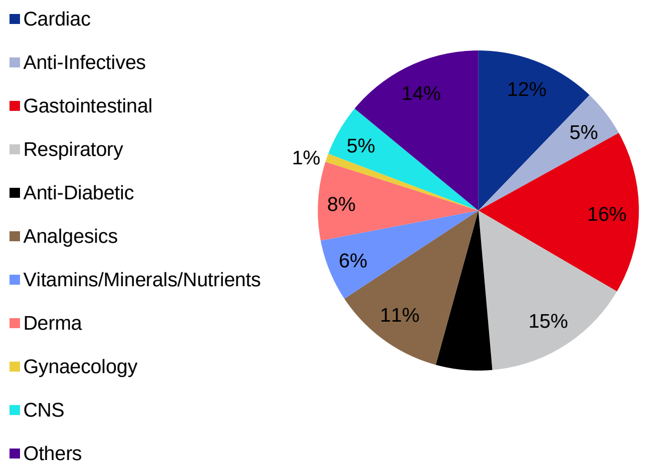
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 118: DRL's domestic business has been doing well off late with increased focus



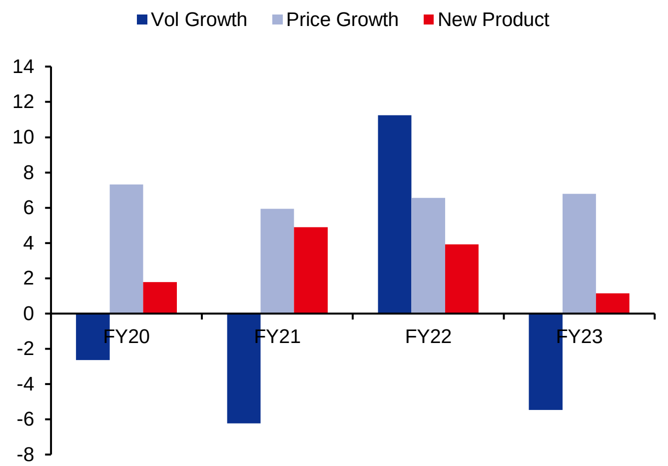
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 119: Therapy-wise revenue break-up of DRL



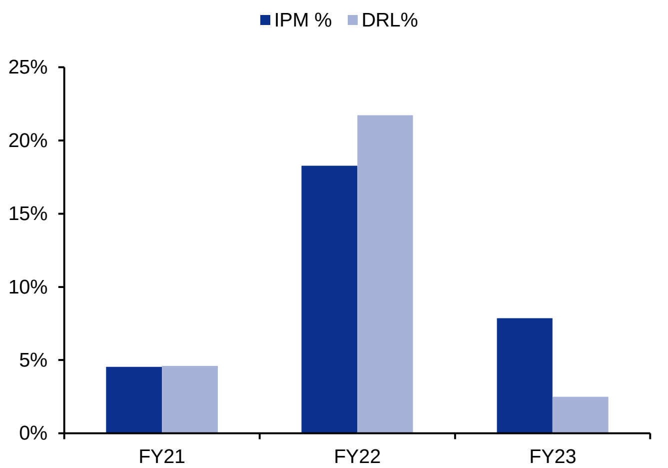
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 120: Domestic business growth drivers – volume yet to show a pick-up



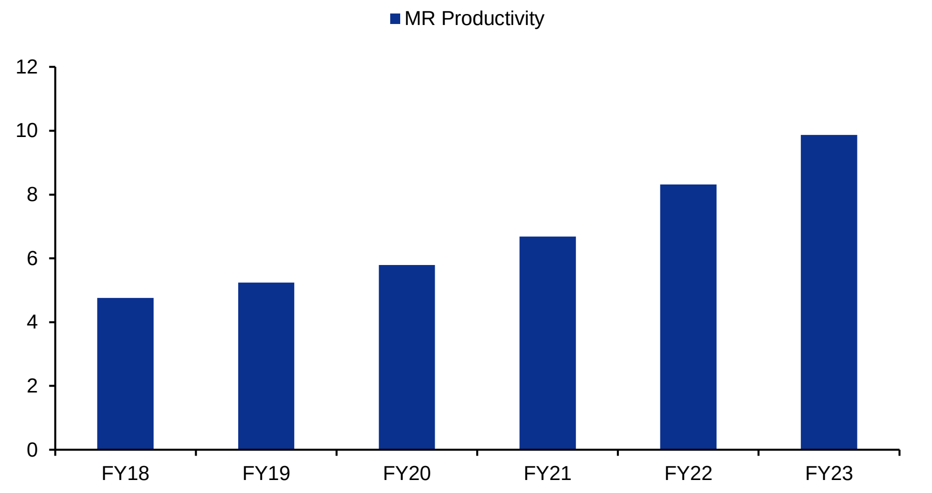
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 121: Fast catching up with IPM growth



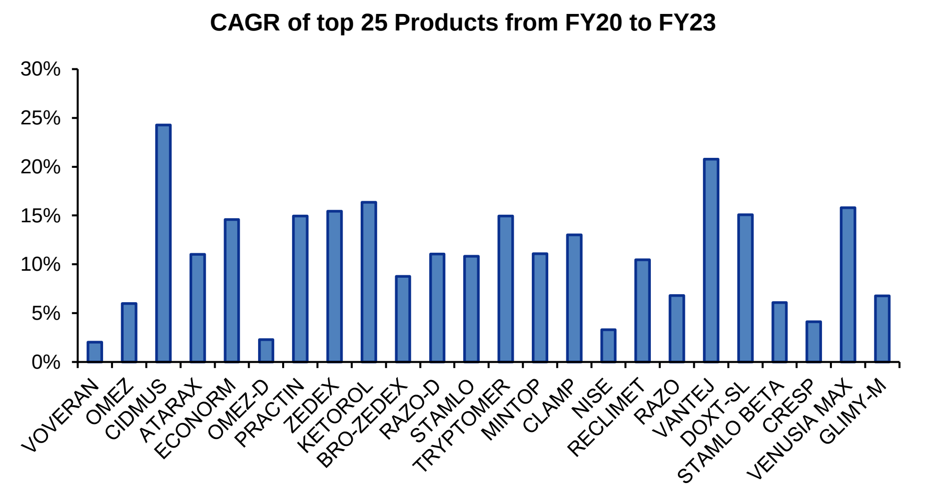
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 122: MR productivity – steadily picking up



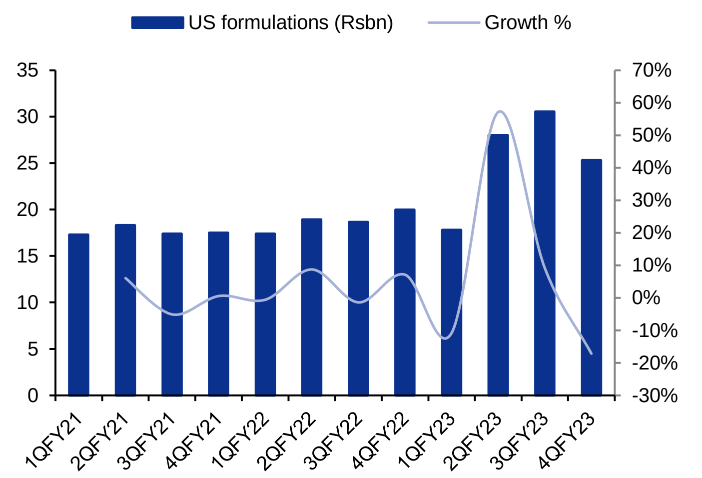
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 123: CAGR of top-25 products from FY20 to FY23 - increased focus on top products



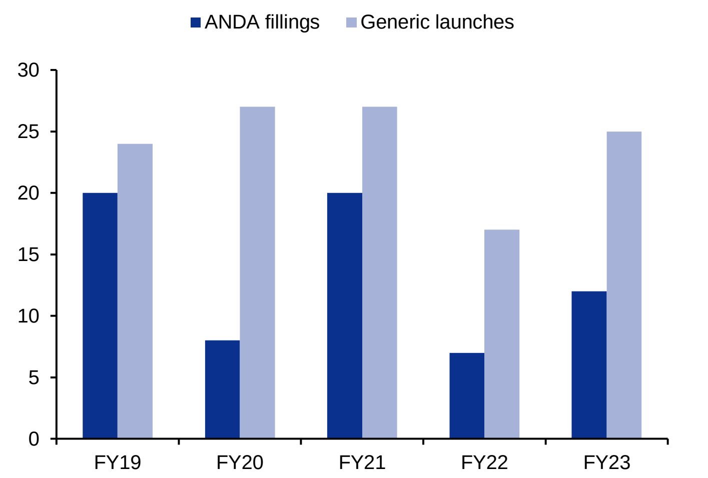
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 124: US market performance over the past few quarters – pick-up reflects in gRevlimid sales



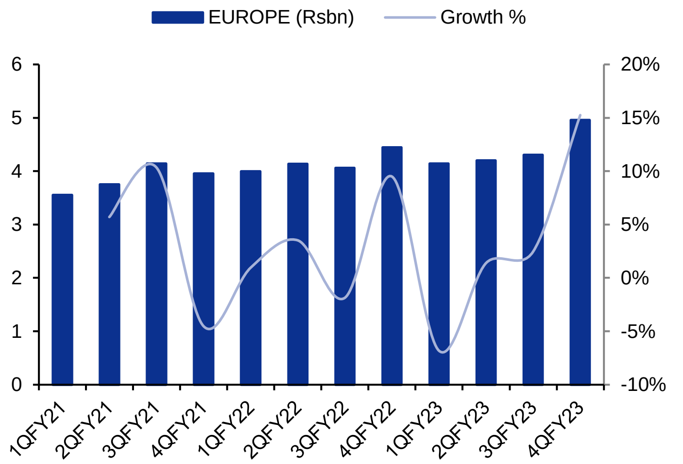
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 125: Historical ANDA filings and generic launches in the US market



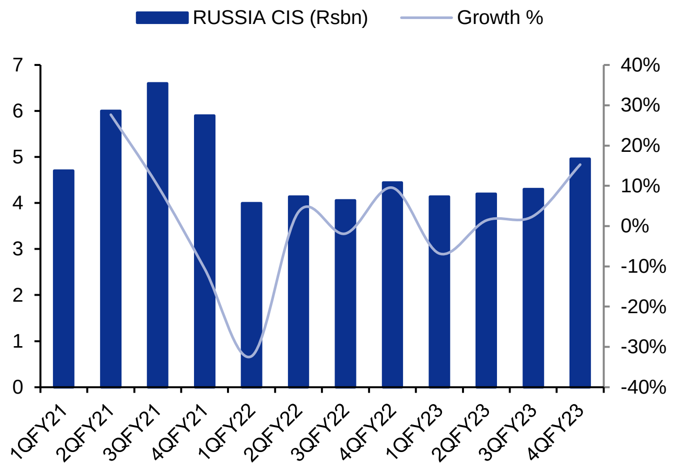
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 126: Europe revenue performance of DRL



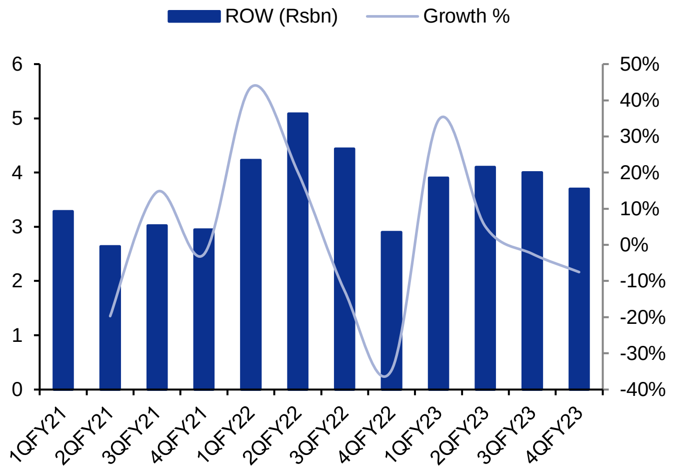
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 127: Russia-CIS revenue performance of DRL



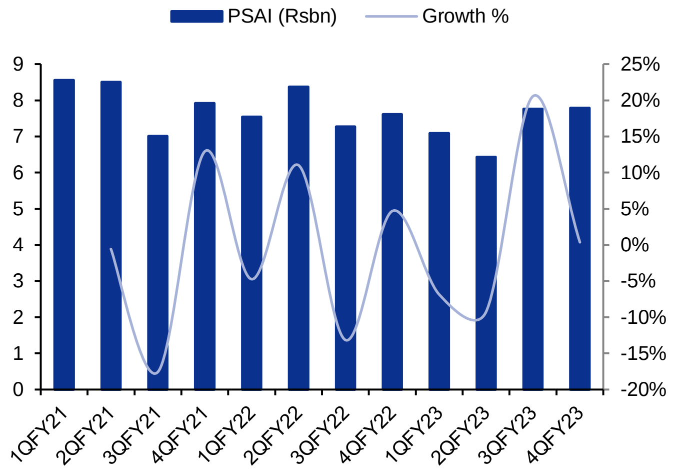
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 128: RoW revenue performance has been steady



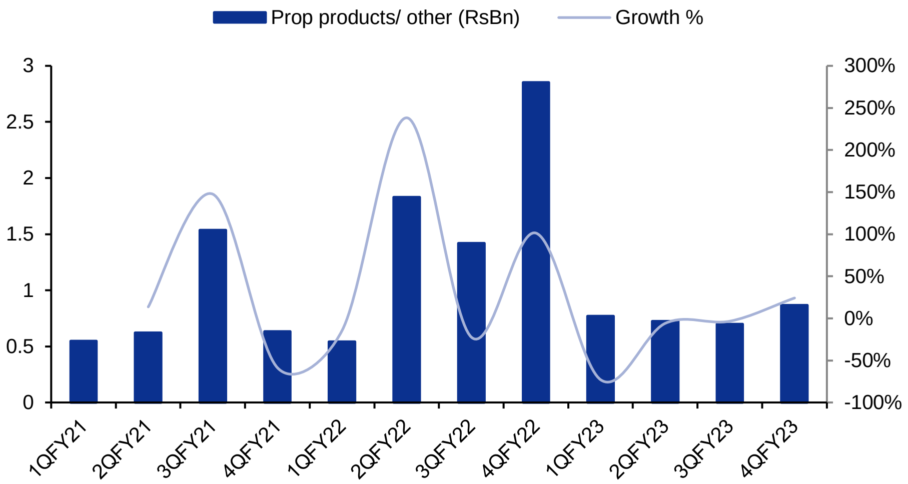
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 129: PSAI – mostly consumed captively



SOURCE: INCRED RESEARCH, COMPANY REPORTS

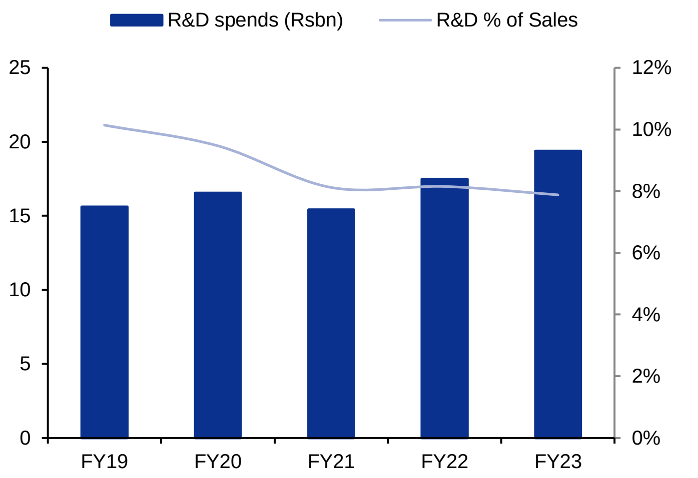
Figure 130: Proprietary products/ others revenue – see the occasional bump-up due to milestone incomes



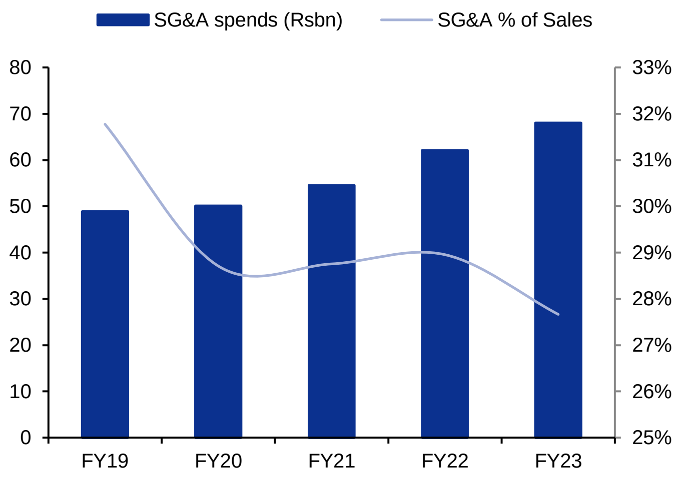
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 131: R&D spending has been maintained largely

Figure 132: SG&A spending – low in the past but expected to pick up now

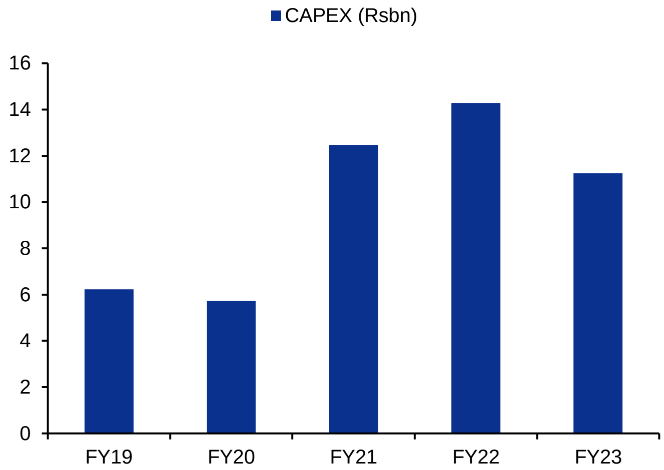


SOURCE: INCRED RESEARCH, COMPANY REPORTS



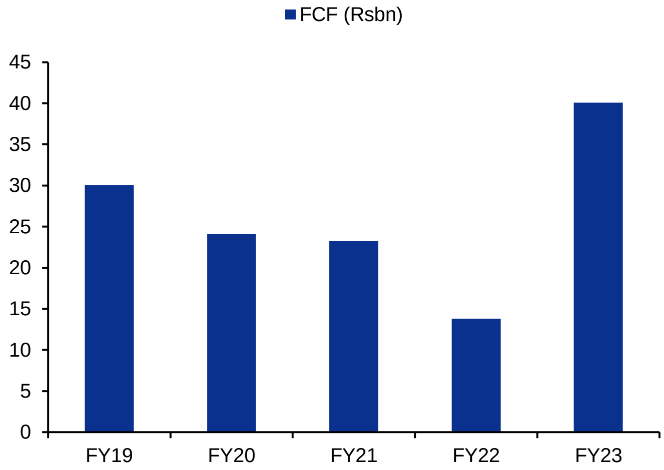
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 133: Capex trend



SOURCE: INCRED RESEARCH, COMPANY REPORTS

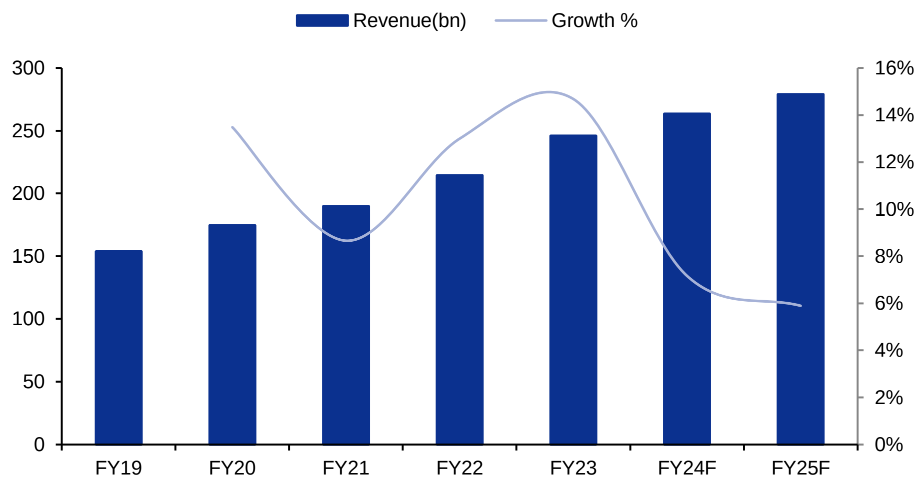
Figure 134: FCF generation – picked up well in FY23 due to gRevlimid sales



SOURCE: INCRED RESEARCH, COMPANY REPORTS

We believe core margins are weak at 15-16%, as reflected in 4QFY23 earnings.

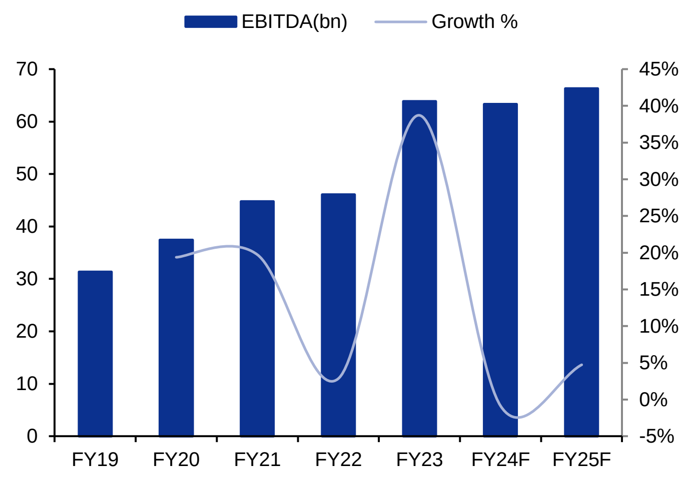
Figure 135: FY23 was a big year for US revenue with marketing exclusivity for gRevlimid



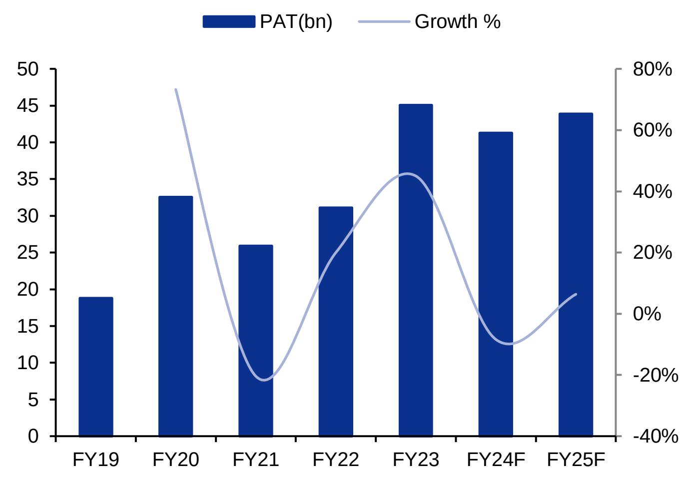
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 136: FY23 margins were propped up by marketing exclusivity of gRevlimid…

Figure 137: …and PAT followed suit

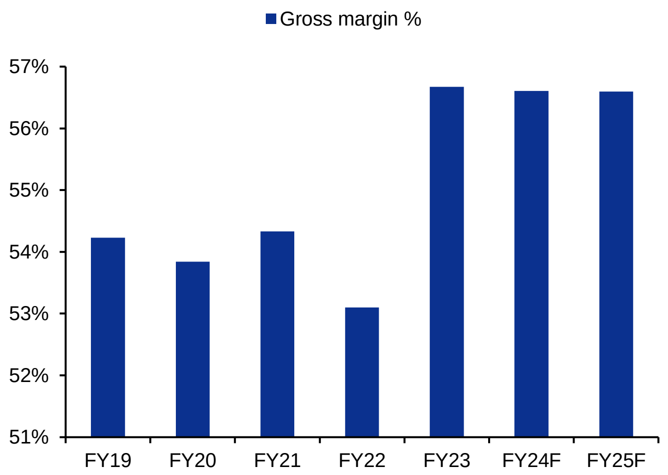


SOURCE: INCRED RESEARCH, COMPANY REPORTS



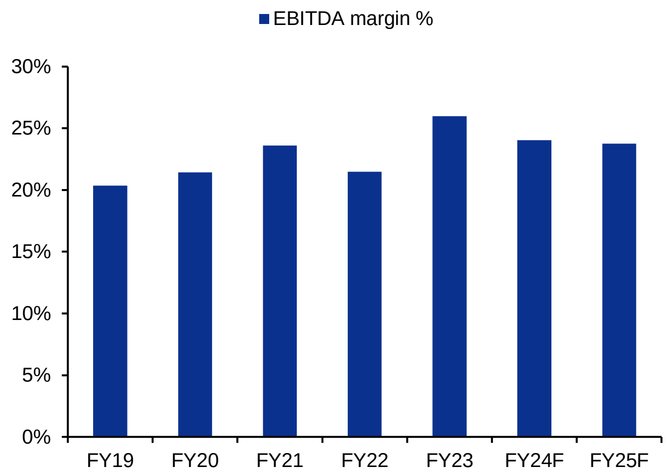
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 138: Gross margin trend



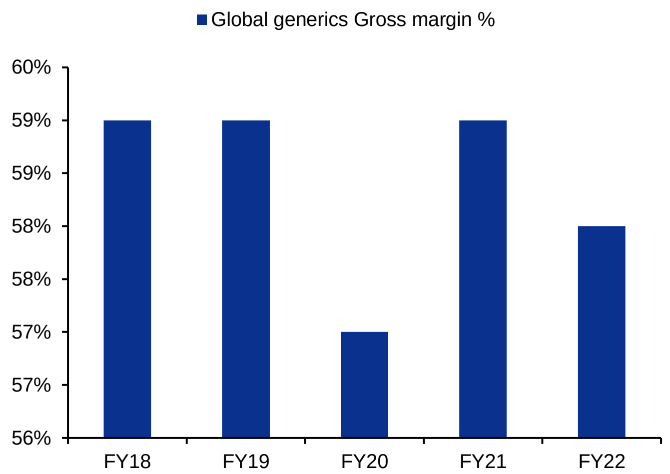
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 139: EBITDA margin



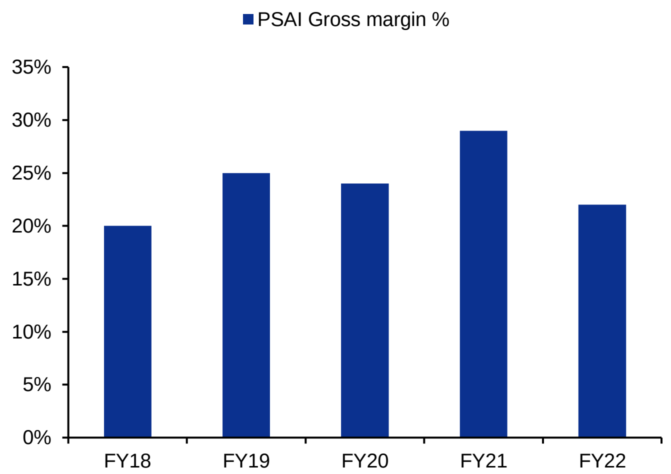
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 140: Global generics gross margin trend



SOURCE: INCRED RESEARCH, COMPANY REPORTS

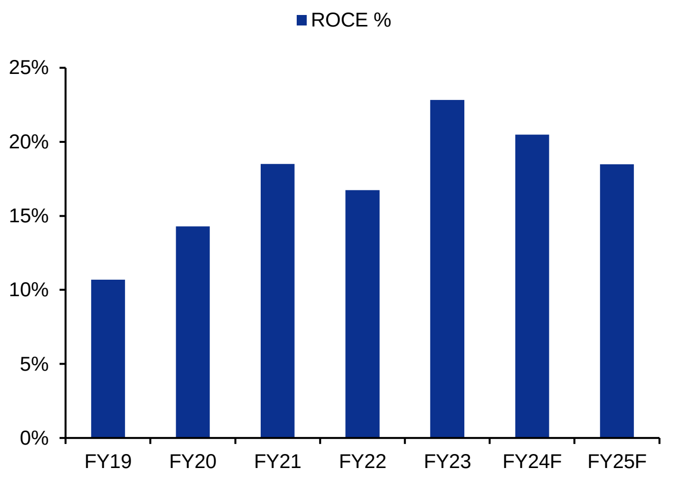
Figure 141: PSAI gross margin trend



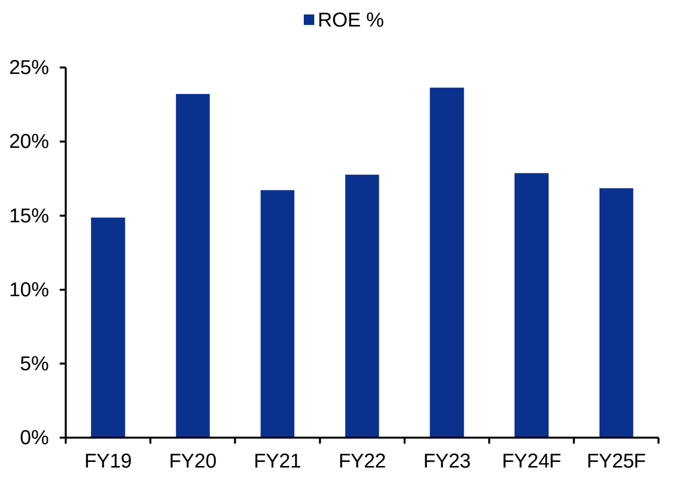
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 142: RoCE trend

Figure 143: RoE trend

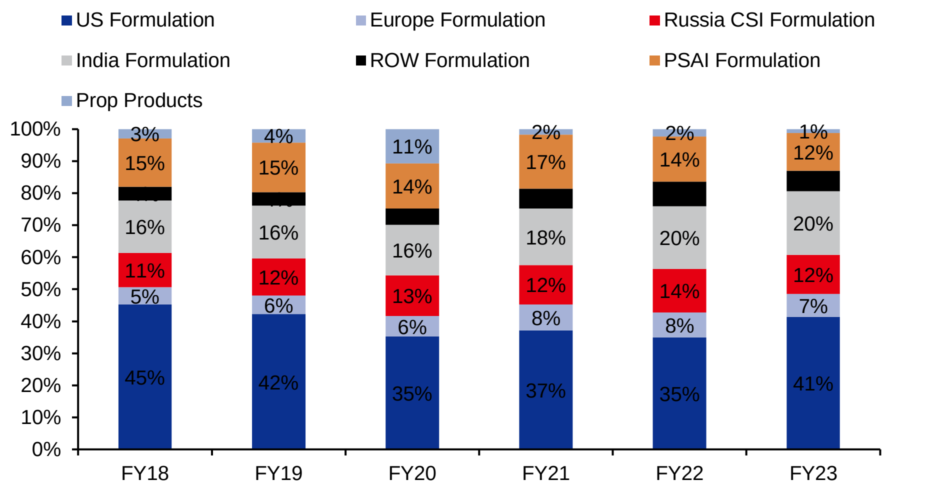


SOURCE: INCRED RESEARCH, COMPANY REPORTS



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 144: Business composition over the past five years



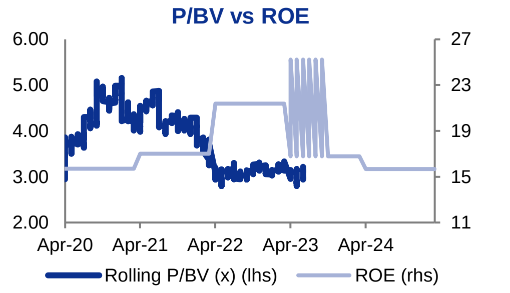
SOURCE: INCRED RESEARCH, COMPANY REPORTS

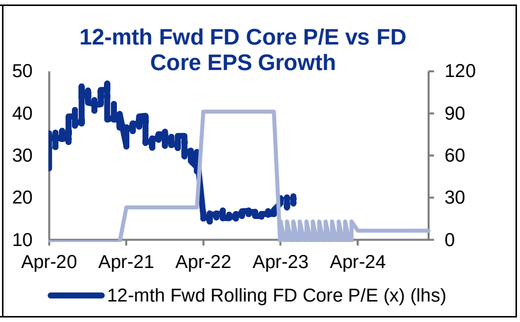
Figure 145: One-year forward P/E of DRL

SOURCE: INCRED RESEARCH, COMPANY REPORTS

InCred Equities

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Net Revenues	**189,722**	**214,391**	**245,879**	**263,503**	**279,036**
Gross Profit	**103,077**	**113,840**	**139,343**	**149,168**	**157,921**
Operating EBITDA	**44,775**	**46,054**	**63,873**	**63,308**	**66,299**
Depreciation And Amortisation	(12,798)	(11,824)	(12,636)	(13,200)	(13,800)
Operating EBIT	**31,977**	**34,230**	**51,237**	**50,108**	**52,499**
Financial Income/(Expense)	(970)	(958)	(1,428)	(1,500)	(1,500)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	3,605	5,838	10,188	6,000	7,000
Profit Before Tax (pre-EI)	**34,612**	**39,110**	**59,997**	**54,608**	**57,999**
Exceptional Items					
Pre-tax Profit	**34,612**	**39,110**	**59,997**	**54,608**	**57,999**
Taxation	(9,175)	(8,730)	(15,300)	(13,652)	(14,500)
Exceptional Income - post-tax	(6,768)	(7,515)			
Profit After Tax	**18,669**	**22,865**	**44,697**	**40,956**	**43,499**
Minority Interests	480	703	370	320	400
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**19,149**	**23,568**	**45,067**	**41,276**	**43,899**
Recurring Net Profit	25,917	31,083	45,067	41,276	43,899
Fully Diluted Recurring Net Profit	**25,917**	**31,083**	**45,067**	**41,276**	**43,899**

Cash Flow

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
EBITDA	44,775	46,054	63,873	63,308	66,299
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(8,288)	(13,894)	(7,845)	(21,993)	(5,142)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	24,627	22,456	51,286	47,315	68,158
Net Interest (Paid)/Received	(970)	(958)	(1,428)	(1,500)	(1,500)
Tax Paid	12,046	6,610	9,017	(17,832)	(19,600)
Cashflow From Operations	**35,703**	**28,108**	**58,875**	**27,983**	**47,058**
Capex	(12,476)	(14,290)	(11,241)	(11,000)	(11,500)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments				(8,300)	
Other Investing Cashflow			(7,543)		
Cash Flow From Investing	**23,227**	**13,818**	**40,091**	**8,683**	**35,558**
Debt Raised/(repaid)	6,848	3,520	(19,382)	9,983	440
Proceeds From Issue Of Shares	(924)	334	368		
Shares Repurchased					
Dividends Paid	(4,147)	(4,146)	(4,146)	(11,657)	(5,828)
Preferred Dividends					
Other Financing Cashflow	(16,171)	(1,828)	(173)	4,500	5,500
Cash Flow From Financing	**(14,394)**	**(2,120)**	**(23,333)**	**2,826**	**111**
Total Cash Generated	8,833	11,698	16,758	11,509	35,669
Free Cashflow To Equity	**65,778**	**45,446**	**79,584**	**46,649**	**83,055**
Free Cashflow To Firm	**59,900**	**42,884**	**100,394**	**38,166**	**84,115**

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Cash And Equivalents	34,573	46,271	63,029	74,538	110,207
Total Debtors	49,641	66,764	72,485	76,416	80,920
Inventories	45,412	50,884	48,670	60,606	64,178
Total Other Current Assets	18,623	17,187	22,756	26,350	27,904
Total Current Assets	**148,249**	**181,106**	**206,940**	**237,910**	**283,209**
Fixed Assets	57,111	62,169	66,462	64,262	61,962
Total Investments	3,375	3,668	5,362	5,362	5,362
Intangible Assets	40,216	36,036	35,094	43,394	43,394
Total Other Non-Current Assets	16,540	13,675	7,996	7,996	7,996
Total Non-current Assets	**117,242**	**115,548**	**114,914**	**121,014**	**118,714**
Short-term Debt	23,136	28,099	12,194	12,194	12,194
Current Portion of Long-Term Debt					
Total Creditors	21,916	25,572	26,444	24,892	26,463
Other Current Liabilities	36,420	44,171	47,207	46,227	49,145
Total Current Liabilities	**81,472**	**97,842**	**85,845**	**83,313**	**87,801**
Total Long-term Debt	6,299	5,746	1,278	11,261	11,700
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	2,739	2,539	3,740	3,740	3,740
Total Non-current Liabilities	**9,038**	**8,285**	**5,018**	**15,001**	**15,440**
Total Provisions					
Total Liabilities	**90,510**	**106,127**	**90,863**	**98,314**	**103,242**
Shareholders Equity	174,981	190,527	230,991	260,930	299,401
Minority Interests				(320)	(720)
Total Equity	**174,981**	**190,527**	**230,991**	**260,610**	**298,681**

Key Ratios

	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue Growth	8.7%	13.0%	14.7%	7.2%	5.9%
Operating EBITDA Growth	19.7%	2.9%	38.7%	(0.9%)	4.7%
Operating EBITDA Margin	23.6%	21.5%	26.0%	24.0%	23.8%
Net Cash Per Share (Rs)	30.87	74.66	297.75	306.91	518.58
BVPS (Rs)	1,051.31	1,144.71	1,387.82	1,567.70	1,798.84
Gross Interest Cover	32.97	35.73	35.88	33.41	35.00
Effective Tax Rate	26.5%	22.3%	25.5%	25.0%	25.0%
Net Dividend Payout Ratio					
Accounts Receivables Days	96.12	99.09	103.36	103.13	102.90
Inventory Days	169.51	174.78	170.54	174.42	188.03
Accounts Payables Days	81.25	86.19	89.11	81.94	77.38
ROIC (%)	14.1%	14.5%	21.3%	18.0%	18.6%
ROCE (%)	17.0%	16.0%	21.9%	19.0%	17.3%
Return On Average Assets	10.5%	11.1%	14.8%	12.4%	11.7%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

India

HOLD *(previously ADD)*

Consensus ratings*:	Buy 7	Hold 2	Sell 10

Current price:	Rs1,021
Target price: ▼	Rs1,056
Previous target:	Rs1,564
Up/downside:	3.4%
InCred Research / Consensus:	-17.9%
Reuters:	
Bloomberg:	GLAND IN
Market cap:	US$2,050m
	Rs168,160m
Average daily turnover:	US$15.0m
	Rs1229.7m
Current shares o/s:	164.7m
Free float:	42.1%

Source: Bloomberg

Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	9.9	(20.4)	(61.4)
Relative (%)	9.1	(27.1)	(67.4)

Major shareholders	% held
Promoters	57.9
Mirae MF	4.7
ICICI Pru MF	4.4

Analyst(s)

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Gland Pharma Ltd

Tough to map near-term recovery

- Gland Pharma's near-term recovery is tough to map as it has several moving parts – price erosion in key products (Heparin/Enoxaparin), bankruptcy filing by a key client (~5% of revenue) and a customer shifting out of its products.
- Gland Pharma has high operating leverage in the business, and margin recovery should follow revenue recovery. Structurally, we see risks to margin with rising competition in the injectables segment.
- We factor in a recovery in 2HFY24F but await more clarity before being constructive. The stock trades at 16x FY25F EPS; we value it at 17x and resume coverage on it with a HOLD rating (ADD earlier) and a TP of Rs1,056.

FY23 was a tough year; near-term outlook is uncertain

FY23 was one of the toughest years for Gland Pharma (Gland) led by temporary shutdown of its insulin and penem lines, a sharp decline in gMicafungin post loss of 180-day marketing exclusivity in the US, pricing pressure in two of its largest products, Heparin and Enoxaparin (~27% of FY23 revenue), bankruptcy filing by a key client and another customer shifting out of its products. While the insulin/penem lines have resumed operations, a lot of uncertainty still surrounds Heparin (high pricing pressure, market share loss; company yet to decide whether to participate in low-margin tenders or not), Enoxaparin (high channel inventory), customer shift (14-15 products impacted, company trying to transfer its products to other clients) and customer bankruptcy (awaits clarity). While the near-term outlook is uncertain, we are building in a recovery from 2HFY24F. Management refrained from giving guidance, given uncertain industry dynamics.

Margin recovery should follow revenue recovery

Gland's business has high operating leverage, and margins usually follow revenue recovery. Over the past four quarters, while the cost base has broadly remained stable, margins have swung from 21% to 31%, in line with revenue swings. FY24F-25F margins will also be influenced by whether Gland decides to aggressively bid for Heparin tenders or not as well as on when its Enoxaparin channel inventory depletes. New launches are witnessing more competition and contributed <5% to growth for the last two years (vs. 10%+ in the past). In the near term, the injectables portfolio should do well, given the ongoing shortage, but structurally we believe the higher competitive intensity will keep its margins under check. Already, the profit share from its partners has come off by ~300bp to 7% (vs. 10-11% historically) although Gland expects it to recover to 10% going ahead.

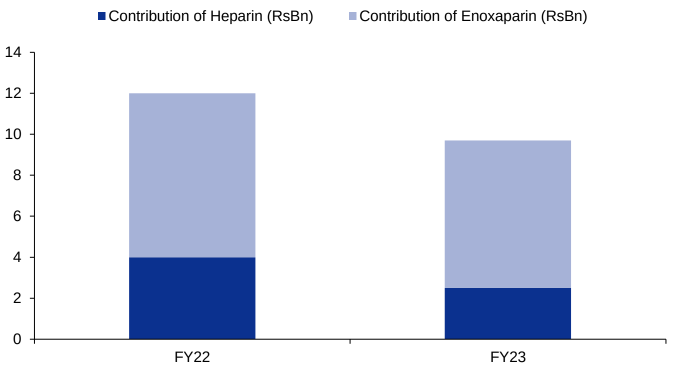
Resume coverage on the stock with a HOLD rating

While we bake in a recovery in 2HFY24F, a lot of it depends on how the industry dynamics play out in key products (Heparin/Enoxaparin) and the fate of product contracts with key customers. We await more clarity on the same, and resume coverage on Gland with a HOLD rating and a target price of Rs1,056, valuing it at 17x FY25F EPS. Faster-than-expected recovery is a key upside risk while a delayed recovery is a key downside risk.

Financial Summary	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue (Rsm)	34,629	44,007	36,246	54,146	58,834
Operating EBITDA (Rsm)	13,022	15,102	10,248	13,394	15,241
Net Profit (Rsm)	9,970	12,117	7,811	9,153	10,313
Core EPS (Rs)	60.5	73.6	50.0	55.6	62.6
Core EPS Growth	29.0%	21.5%	(32.1%)	11.2%	12.7%
FD Core P/E (x)	16.87	13.88	20.43	18.37	16.30
DPS (Rs)	0.0	0.0	0.0	0.0	0.0
Dividend Yield	0.00%	0.00%	0.00%	0.00%	0.00%
EV/EBITDA (x)	10.61	8.99	12.73	11.30	9.48
P/FCFE (x)	17.13	15.87	33.16	(7.73)	11.73
Net Gearing	(50.9%)	(45.3%)	(47.3%)	(19.0%)	(24.0%)
P/BV (x)	2.85	2.35	2.11	1.89	1.70
ROE	20.9%	18.6%	10.9%	10.9%	11.0%
% Change In Core EPS Estimates				(10.40%)	(7.85%)
InCred Research/Consensus EPS (x)					

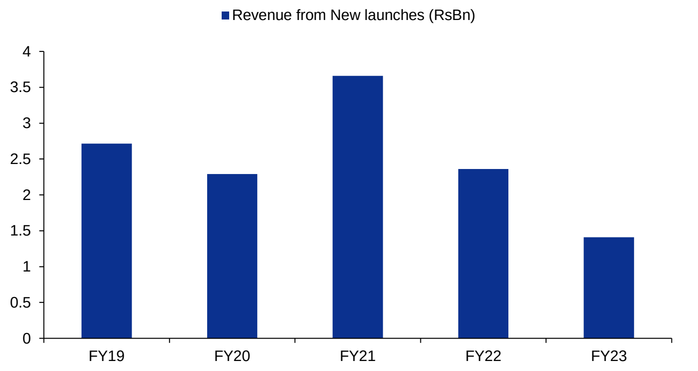
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 146: Heparin and Exoparin contributed nearly 27% each for FY22 and FY23 revenue



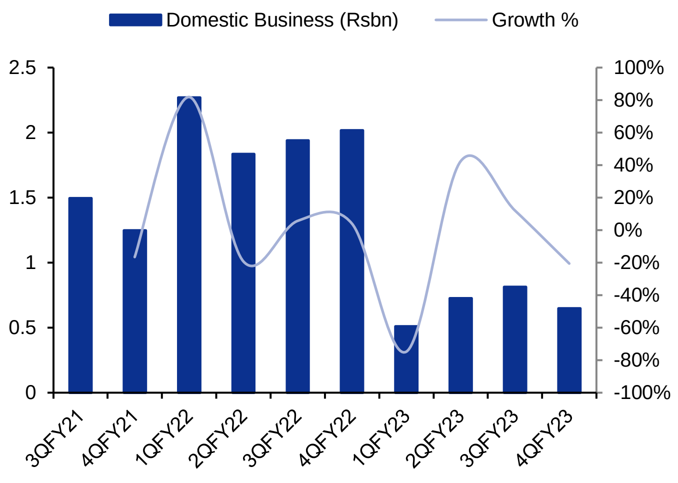
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 147: Revenue contribution from new products continues to decline; contribution is now down from an average of 20%+ to <5% of growth, implying higher competitive intensity



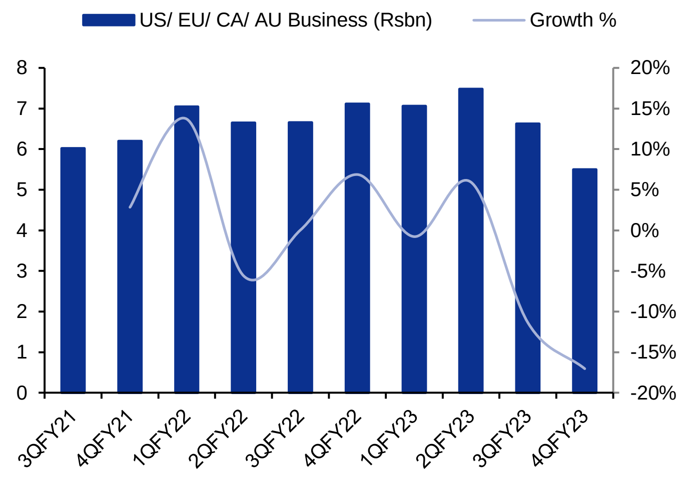
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 148: Domestic performance was boosted by sale of Covid products in FY22, which came off in FY23



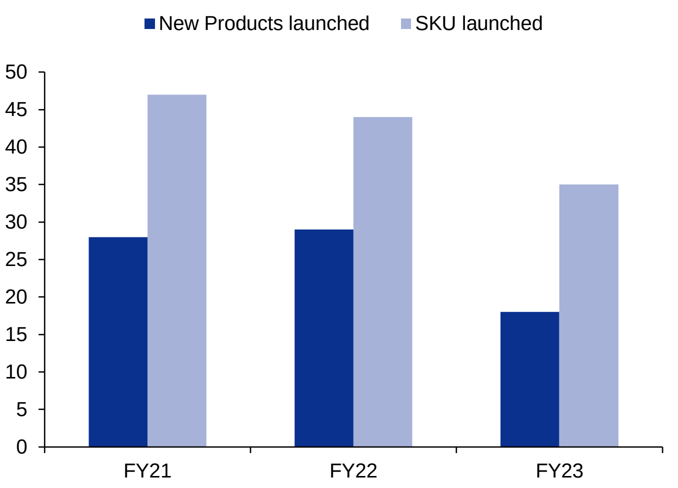
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 149: Higher channel inventory impacted sales in US/EU/CA/AU business



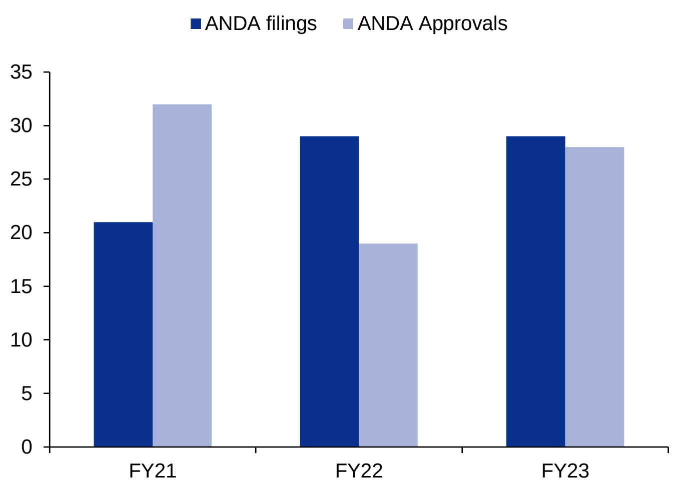
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 150: Reduced number of products launched in FY23



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 151: ANDA filings and approvals remain on track



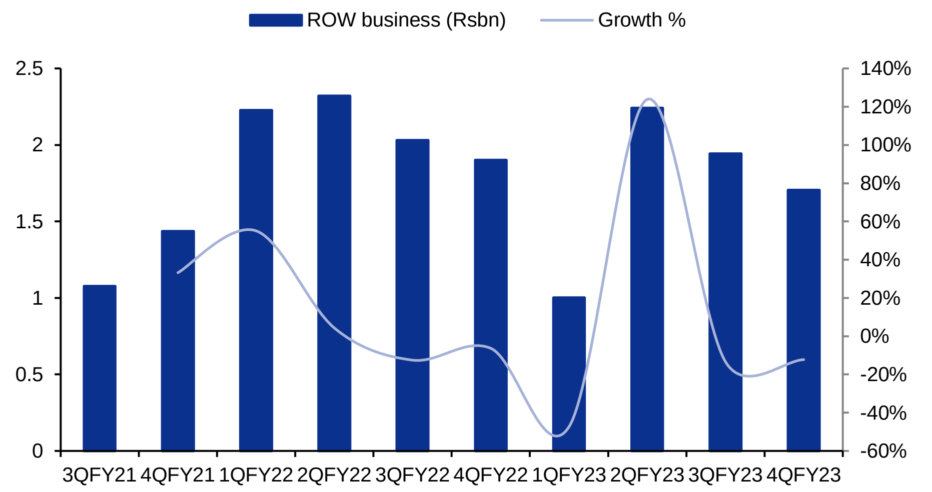
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 152: US complex injectables pipeline

Complex Injectables Pipeline	Total Projects	FY22	FY23	FY24F	FY25F
Complex-Peptide	4	1			3
Emulsion	1			1	
Hormone	7	3	3	1	
Microsphere	2				2
Nano Suspension	1				1
Suspension	4			2	2
Grand Total	19	4	3	4	8

SOURCE: INCRED RESEARCH, COMPANY REPORTS

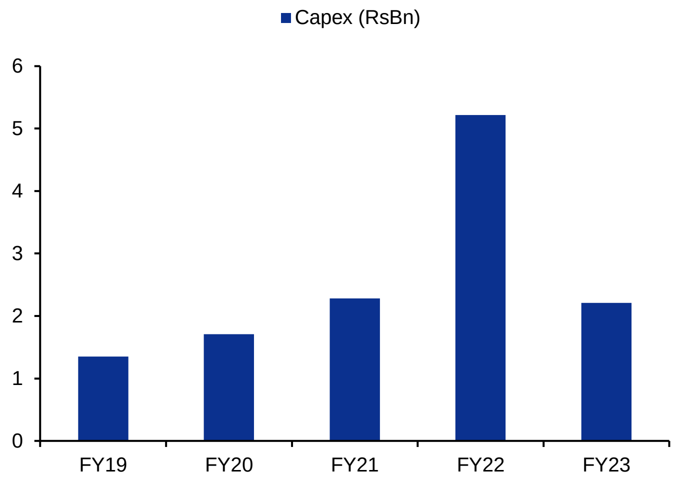
Figure 153: RoW revenue impacted by lower ARV sales in 4QFY23



SOURCE: INCRED RESEARCH, COMPANY REPORTS

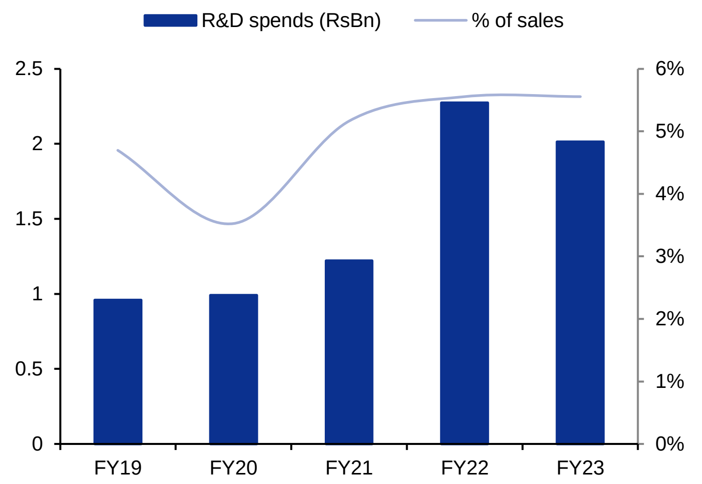
Financials

Figure 154: Capex to remain in the range of Rs2.5-3bn going ahead



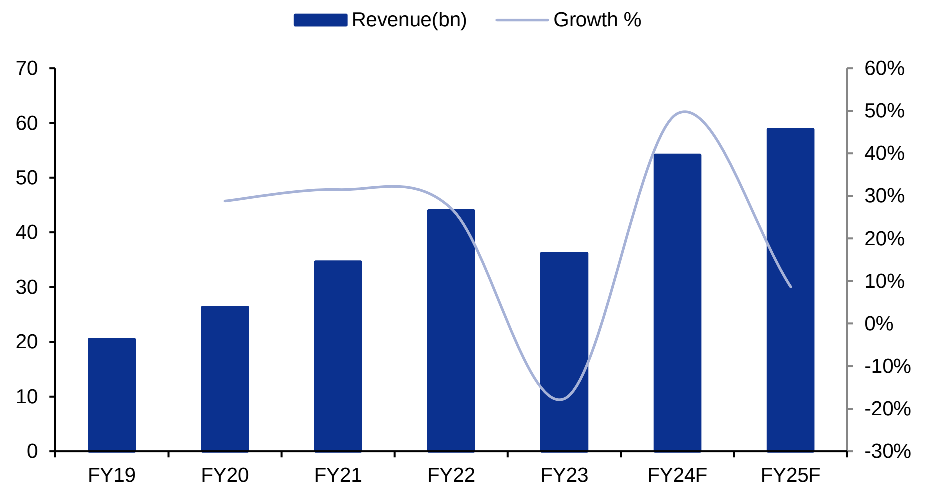
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 155: R&D spending fell in FY23, but R&D spending as a % of sales remained consistent with FY22 level



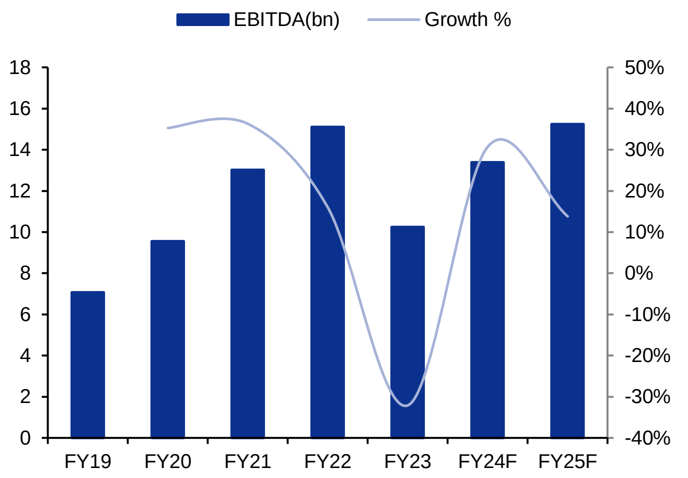
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 156: Revenue performance significantly weakened in FY23 due to multiple issues



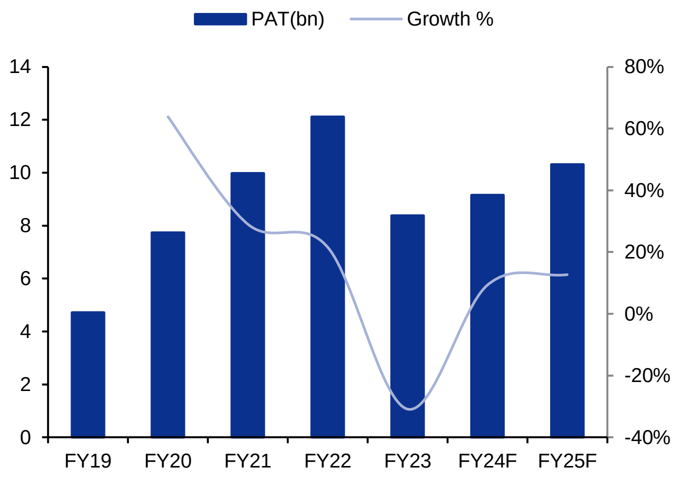
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 157: Negative operating leverage impacted EBITDA



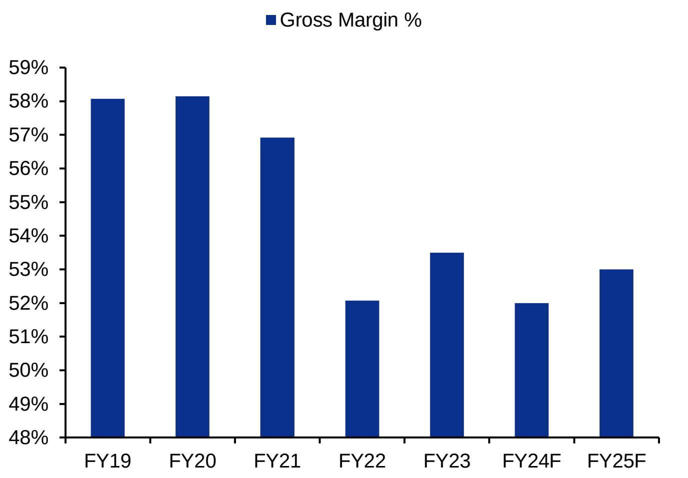
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 158: PAT was further impacted by a provision of Rs565m in FY23 related to a client filing for bankruptcy



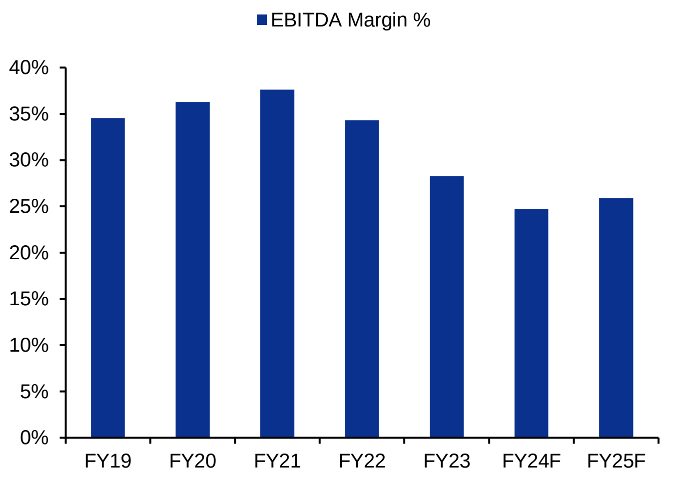
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 159: Gross margin impacted due to pricing pressure in large products



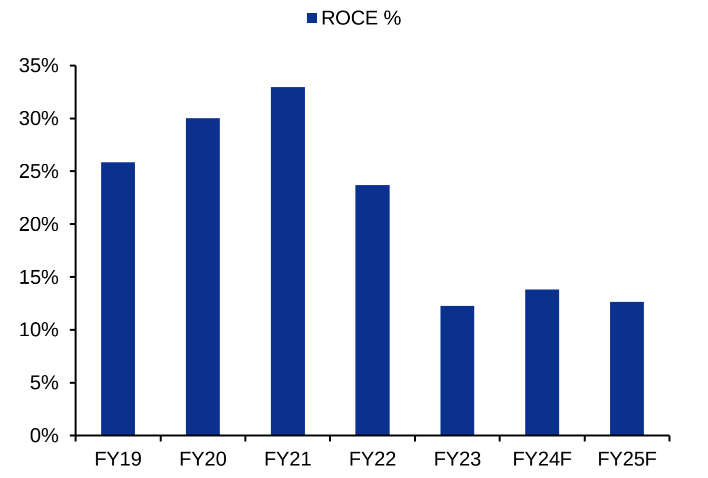
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 160: EBITDA swings have been wide, largely following revenue trajectory



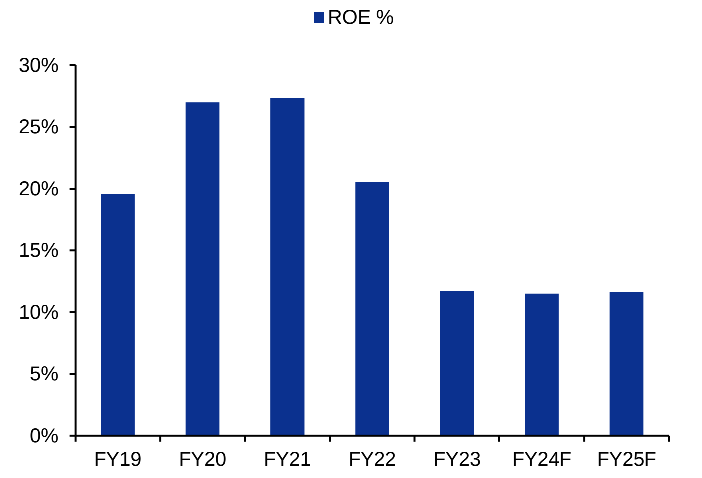
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 161: Weak operating performance impacted RoCE…



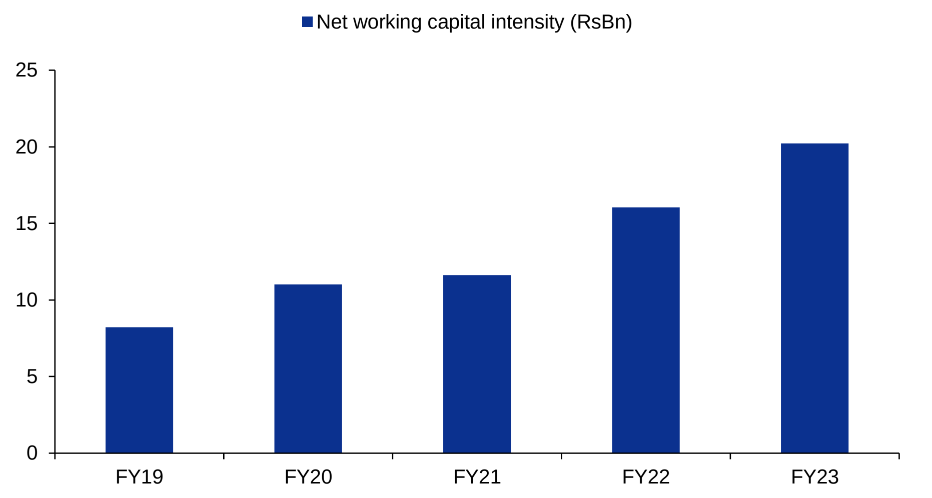
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 162: …and RoE in FY23



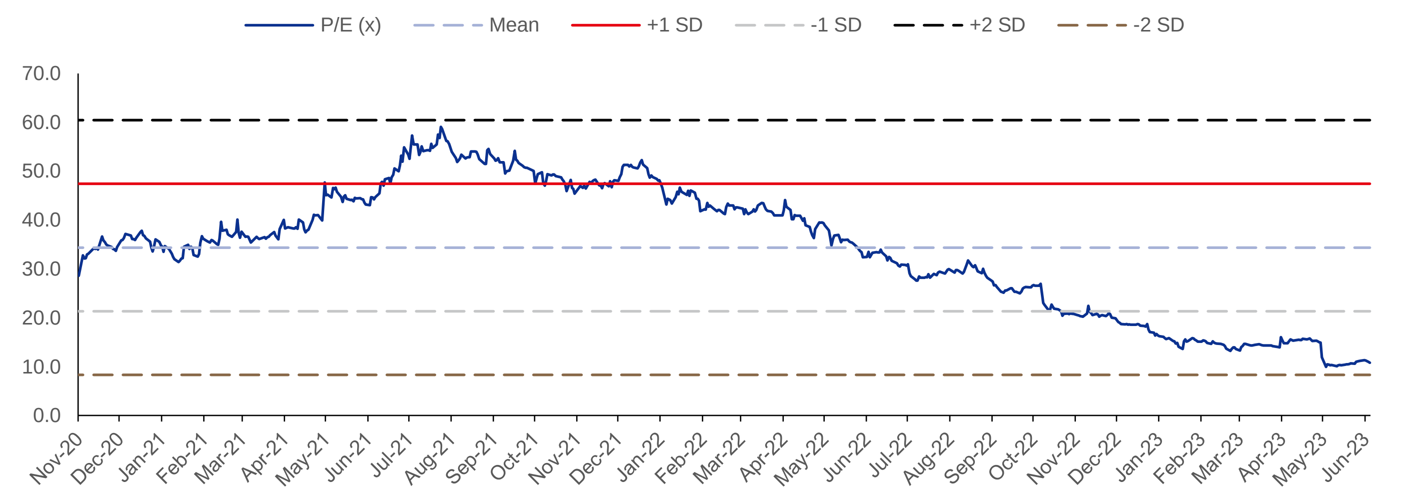
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 163: Net working capital shot up due to higher inventory



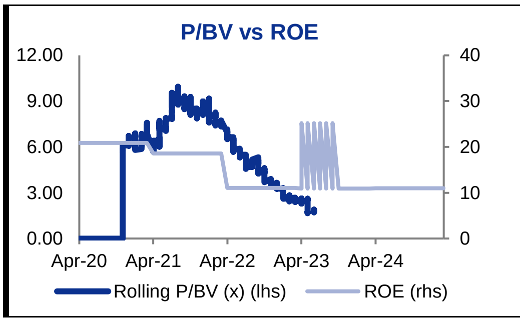
SOURCE: INCRED RESEARCH, COMPANY REPORTS

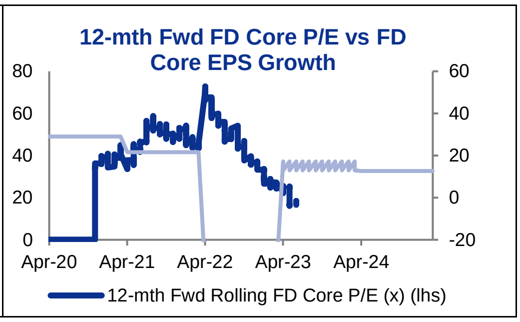
Figure 164: One-year forward P/E of Gland Pharma



SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Net Revenues	**34,629**	**44,007**	**36,246**	**54,146**	**58,834**
Gross Profit	**19,710**	**22,915**	**19,392**	**28,156**	**31,182**
Operating EBITDA	**13,022**	**15,102**	**10,248**	**13,394**	**15,241**
Depreciation And Amortisation	(988)	(1,103)	(1,467)	(2,400)	(2,700)
Operating EBIT	**12,034**	**13,999**	**8,780**	**10,994**	**12,541**
Financial Income/(Expense)	(34)	(52)	(74)	(90)	(90)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	1,348	2,239	2,405	1,300	1,300
Profit Before Tax (pre-EI)	**13,348**	**16,186**	**11,111**	**12,204**	**13,751**
Exceptional Items			(565)		
Pre-tax Profit	**13,348**	**16,186**	**10,546**	**12,204**	**13,751**
Taxation	(3,378)	(4,069)	(2,735)	(3,051)	(3,438)
Exceptional Income - post-tax					
Profit After Tax	**9,970**	**12,117**	**7,811**	**9,153**	**10,313**
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**9,970**	**12,117**	**7,811**	**9,153**	**10,313**
Recurring Net Profit	9,970	12,117	8,229	9,153	10,313
Fully Diluted Recurring Net Profit	**9,970**	**12,117**	**8,229**	**9,153**	**10,313**

Cash Flow

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
EBITDA	13,022	15,102	10,248	13,394	15,241
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(4,358)	(3,931)	(4,179)	(10,086)	(3,134)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	(2,615)	(3,263)	(2,429)	(3,051)	(3,438)
Net Interest (Paid)/Received	(34)	(52)	(74)	(90)	(90)
Tax Paid	(3,929)	(5,450)	(4,194)	(4,261)	(4,648)
Cashflow From Operations	**6,049**	**7,908**	**3,640**	**257**	**8,669**
Capex	(2,283)	(5,217)	(2,208)	(2,500)	(3,000)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments				(19,780)	
Other Investing Cashflow					
Cash Flow From Investing	**3,766**	**2,690**	**1,432**	**(22,023)**	**5,669**
Debt Raised/(repaid)					
Proceeds From Issue Of Shares	12,418	386	214		
Shares Repurchased					
Dividends Paid					
Preferred Dividends					
Other Financing Cashflow	622	(646)	3,573	11,530	1,210
Cash Flow From Financing	**13,040**	**(260)**	**3,787**	**11,530**	**1,210**
Total Cash Generated	16,806	2,430	5,219	(10,493)	6,879
Free Cashflow To Equity	**9,815**	**10,598**	**5,071**	**(21,766)**	**14,338**
Free Cashflow To Firm	**9,849**	**10,651**	**5,146**	**(21,676)**	**14,428**

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Cash And Equivalents	30,058	32,488	37,707	27,214	34,093
Total Debtors	6,710	11,988	8,714	12,995	14,120
Inventories	12,752	11,857	19,453	27,073	29,417
Total Other Current Assets	1,718	2,188	3,133	4,332	4,707
Total Current Assets	**51,236**	**58,521**	**69,007**	**71,614**	**82,337**
Fixed Assets	12,913	16,804	17,362	27,782	28,082
Total Investments					
Intangible Assets	10	125	117	9,577	9,577
Total Other Non-Current Assets	802	2,886	1,290	1,290	1,290
Total Non-current Assets	**13,724**	**19,815**	**18,769**	**38,649**	**38,949**
Short-term Debt		3	6	6	6
Current Portion of Long-Term Debt					
Total Creditors	4,007	4,629	5,873	8,046	8,601
Other Current Liabilities	1,118	1,189	1,412	2,253	2,408
Total Current Liabilities	**5,125**	**5,820**	**7,291**	**10,305**	**11,015**
Total Long-term Debt	39	45	33	10,353	10,353
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	764	895	864	864	864
Total Non-current Liabilities	**803**	**940**	**897**	**11,217**	**11,217**
Total Provisions					
Total Liabilities	**5,928**	**6,760**	**8,188**	**21,521**	**22,232**
Shareholders Equity	59,032	71,576	79,587	88,740	99,054
Minority Interests					
Total Equity	**59,032**	**71,576**	**79,587**	**88,740**	**99,054**

Key Ratios

	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue Growth	31.5%	27.1%	(17.6%)	49.4%	8.7%
Operating EBITDA Growth	36.3%	16.0%	(32.1%)	30.7%	13.8%
Operating EBITDA Margin	37.6%	34.3%	28.3%	24.7%	25.9%
Net Cash Per Share (Rs)	182.27	196.98	228.72	102.35	144.12
BVPS (Rs)	358.45	434.61	483.25	538.83	601.46
Gross Interest Cover	353.95	267.05	118.02	122.16	139.34
Effective Tax Rate	25.3%	25.1%	25.9%	25.0%	25.0%
Net Dividend Payout Ratio					
Accounts Receivables Days	67.08	77.54	104.23	73.17	84.11
Inventory Days	248.50	212.92	339.02	326.70	372.83
Accounts Payables Days	79.48	74.72	113.72	97.74	109.87
ROIC (%)	30.2%	26.2%	15.4%	11.3%	12.3%
ROCE (%)	25.2%	21.4%	11.6%	12.3%	12.0%
Return On Average Assets	18.9%	17.0%	10.2%	9.3%	9.0%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

India

REDUCE *(previously ADD)*

Consensus ratings*:	Buy 9	Hold 3	Sell 3

Current price:	Rs362
Target price: ▼	Rs263
Previous target:	Rs449
Up/downside:	-27.3%
InCred Research / Consensus:	-22.7%
Reuters:	
Bloomberg:	LAURUS IN
Market cap:	US$2,376m
	Rs194,965m
Average daily turnover:	US$12.3m
	Rs1005.1m
Current shares o/s:	538.7m
Free float:	72.8%

**Source: Bloomberg*

Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	8.1	20.9	(22.4)
Relative (%)	7.3	10.7	(34.5)

Major shareholders	% held
Promoters	27.2
Capital group	9.1
Amansa	4.1

Laurus Labs

Margins to remain under pressure

- Some signs of a recovery in the anti-retroviral or ARV formulations business, with the commencement of supplies for global ARV tender & additional capacity on stream. High CDMO base should keep overall FY24F revenue flat.
- The front-loaded cost base (due to capacity expansion) and muted revenue growth in the near term should, in our view, keep the company's margins under pressure. We expect its margins to decline by 160bp over FY23-25F.
- Valuation at 26x FY25F EPS is higher than the historical five-year average and more than factors in a recovery. Resume coverage on the stock with a REDUCE rating & a target price of Rs263, valuing the stock at 20x FY25F EPS.

FY23 was a tough year for core business

While the supply of Paxlovid intermediates drove strong growth in overall revenue in FY23 (we estimate US$170-180m total sales spread over 4QFY22-9MFY23), the core business weakened considerably, led by significant pricing pressure in the ARV business, given high inventory in the channel. There are some signs of stability now, with formulation (FDF) sales recovering in 4QFY23, as supplies relating to the global ARV tender commenced. This should continue in FY24F, which along with higher utilization in recently added capacities (+50% addition in last two years; management expects 70% utilization by the year-end vs. 55-60% currently) should lead to a recovery in the overall FDF business. CDMO business should benefit from the commencement of animal health contract in 2HFY24F, but a high FY23 CDMO base will still drive a marginal fall in overall revenue.

Front-loaded costs and muted revenue to result in flat earnings

Laurus Labs has expanded its API/formulations capacity by 30%/50%, respectively, over FY22-23 and is spending Rs20bn over FY23-24F of which Rs8bn is towards its custom synthesis/bio-ingredients business. The new capacities will start contributing from 2HFY24F; huge capacity addition is a strong show of confidence in the long-term potential of the company, but a front-loaded cost base will keep margins under pressure in the interim, till the time the capacities are optimally utilized. Management expects the capacity utilization rate to pick up from 55-60% in FY23 to around 70% in FY24F and expects margins to not fall below the 20-21% level witnessed in 4QFY23. We factor in a 160bp decline in margins over FY23-25F.

Resume coverage on the stock with a REDUCE rating

Laurus Labs has brought down the salience of its ARV segment over the years through aggressive investments/ramp-ups in the non-ARV business. While the ARV segment's contribution will decline further with the recent capacity addition in the non-ARV formulation business, it is still meaningful at 36% of sales and will drag down overall revenue growth. The stock price has rallied in anticipation of a pick-up in the overall API industry, and its current valuation at 26x FY25 EPS leaves little room for error. We resume coverage on the stock with a REDUCE rating (ADD earlier) and a target price of Rs263, valuing the business at 20x FY25F EPS. Better-than-expected margins are a key upside risk.

Financial Summary	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue (Rsm)	48,135	49,356	60,406	56,497	64,089
Operating EBITDA (Rsm)	15,507	14,224	15,922	12,548	15,738
Net Profit (Rsm)	9,836	8,275	7,901	5,211	7,153
Core EPS (Rs)	18.3	15.4	14.7	9.7	13.3
Core EPS Growth	285.3%	(15.9%)	(4.5%)	(34.0%)	37.3%
FD Core P/E (x)	19.82	23.56	24.68	37.42	27.26
DPS (Rs)	1.2	1.6	4.0	2.0	2.0
Dividend Yield	0.33%	0.44%	1.11%	0.55%	0.55%
EV/EBITDA (x)	13.39	14.86	13.43	17.30	13.91
P/FCFE (x)	37.22	21.24	19.94	15.32	17.29
Net Gearing	48.7%	49.3%	47.5%	51.5%	49.1%
P/BV (x)	7.51	5.82	4.83	4.49	3.94
ROE	45.0%	27.8%	21.4%	12.4%	15.4%
% Change In Core EPS Estimates				(46.52%)	(35.65%)
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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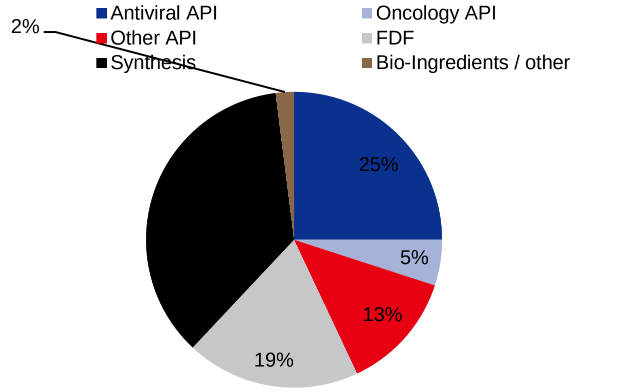
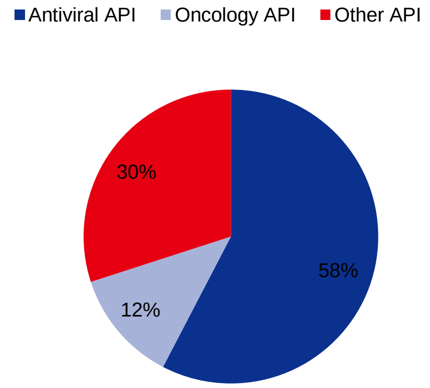
Figure 165: Synthesis business dominates revenue growth in FY23, largely on account of Paxlovid supplies



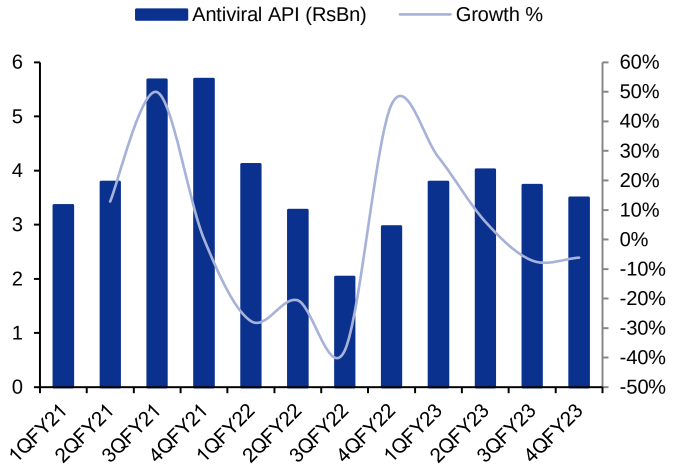
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 166: API sales break-up – while Gland is trying to bring down the contribution of ARV APIs, it is still meaningful



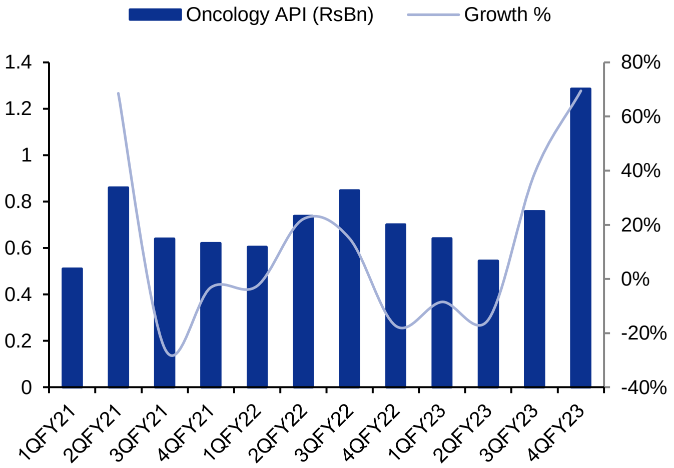
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 167: ARV sales witnessed a dip from 3QFY23 due to high price erosion



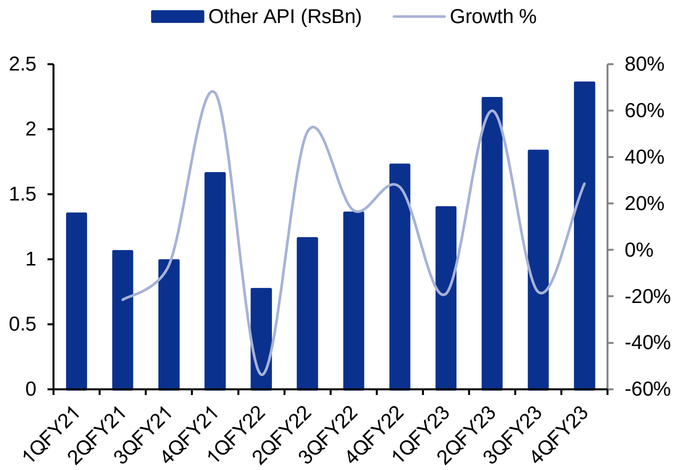
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 168: Oncology API outperforms in 4QFY23 led by higher offtake of one product



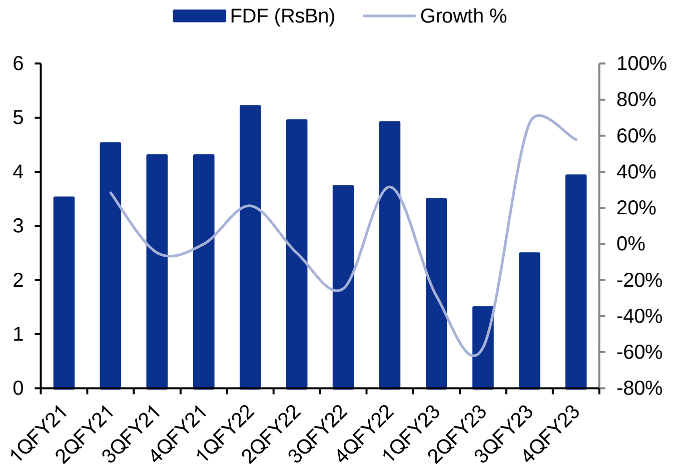
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 169: Other API segment had the best quarter in recent times



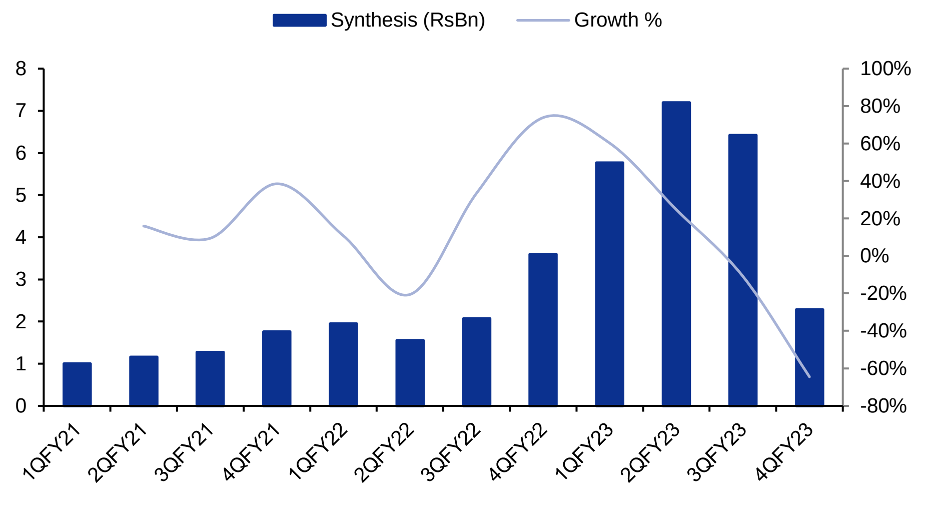
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 170: Recovery in FDF business in 4QFY23, led by commencement of global ARV tender



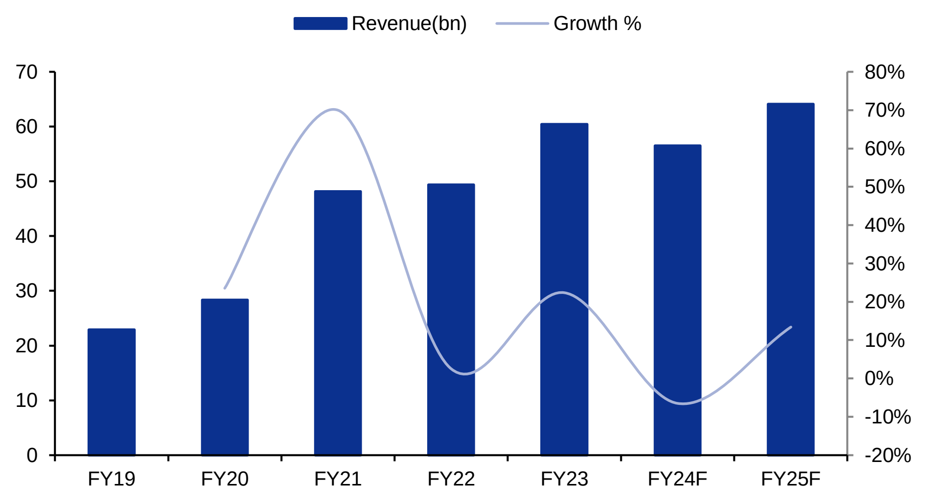
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 171: Synthesis segment declined significantly post Paxlovid supplies in 9MFY23 - this should continue in FY24F



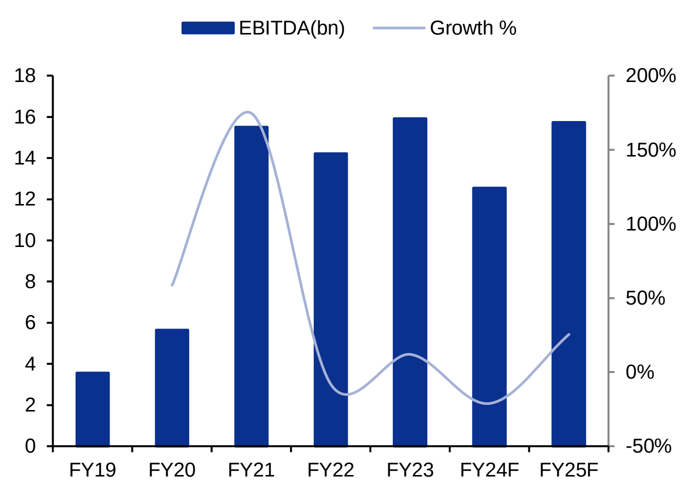
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 172: FY23 growth led by one-time Paxlovid supplies



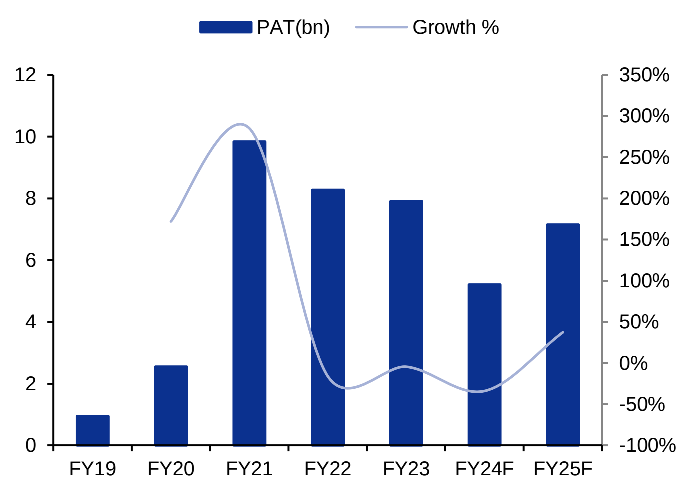
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 173: Paxlovid supplies positively influenced EBITDA…



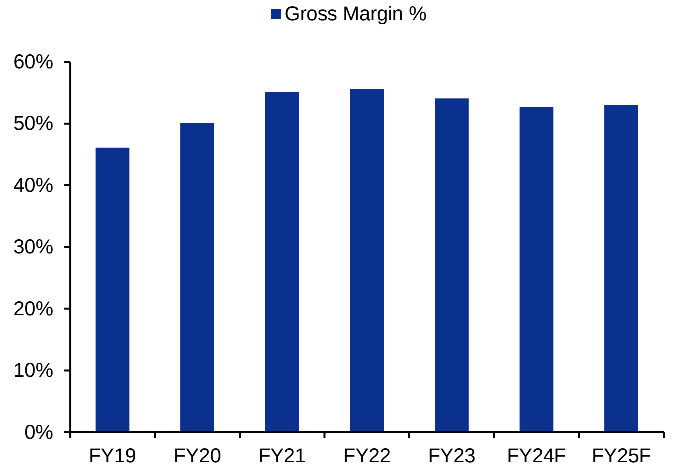
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 174: …but PAT declined on account of higher depreciation due to recent capex



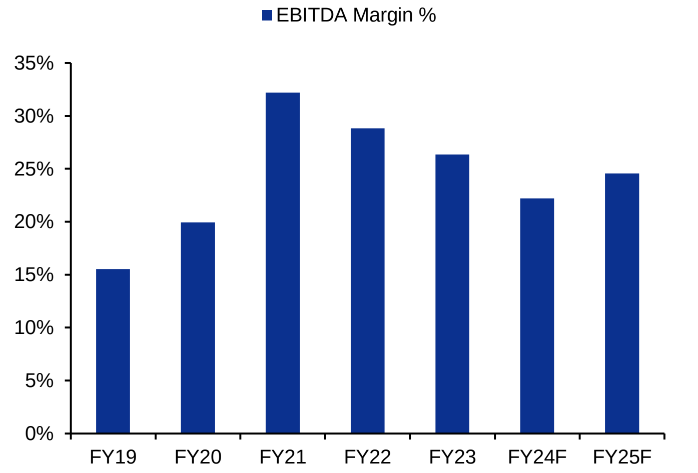
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 175: Gross margin declined in FY23 due to price erosion in the ARV segment…



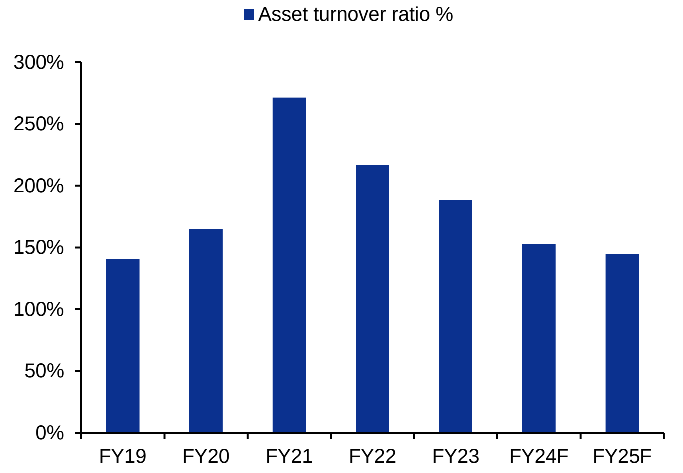
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 176: …and EBITDA margin followed suit



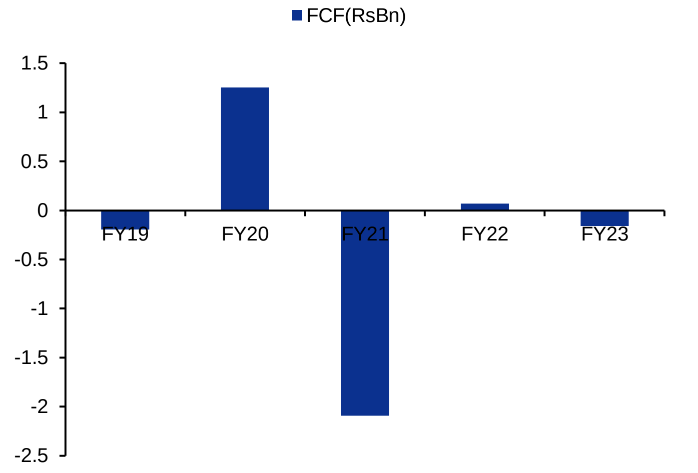
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 177: Asset turnover continues to decline with lesser utilization of recently added capacities



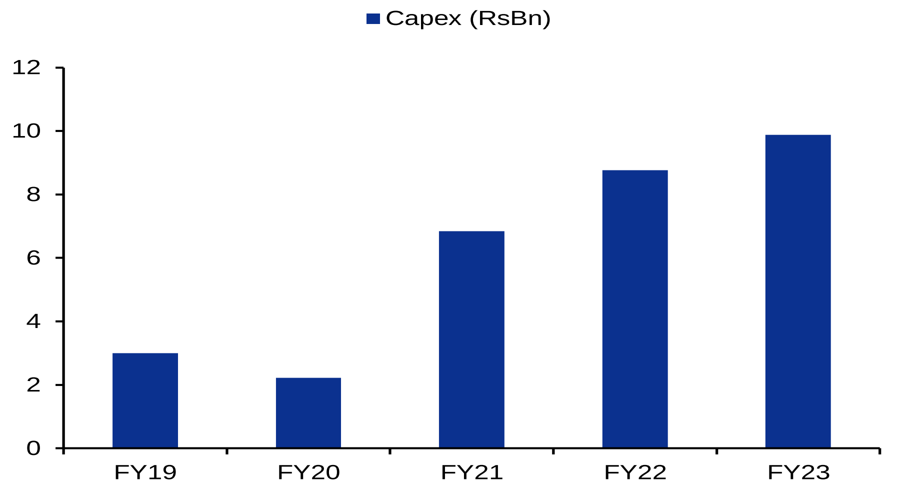
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 178: FCF generation has been weak



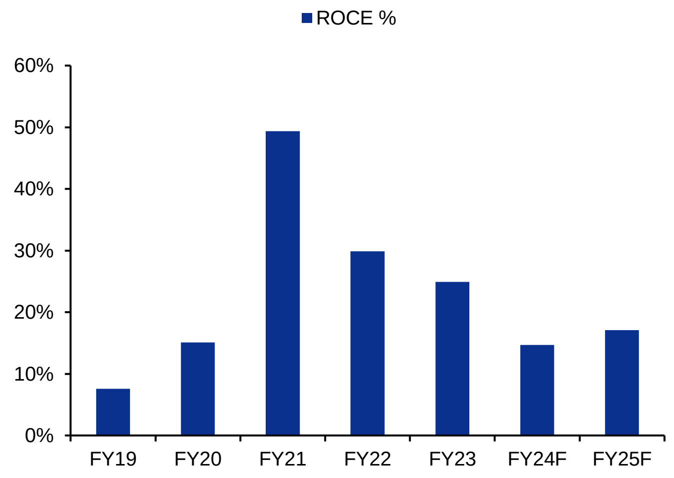
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 179: Capex trend – huge capex intensity over the last three years with API/FDF capacities expanded by 30%/50%, respectively, and spending another Rs800m in FY24F on expansion of synthesis/bio-ingredients capacity



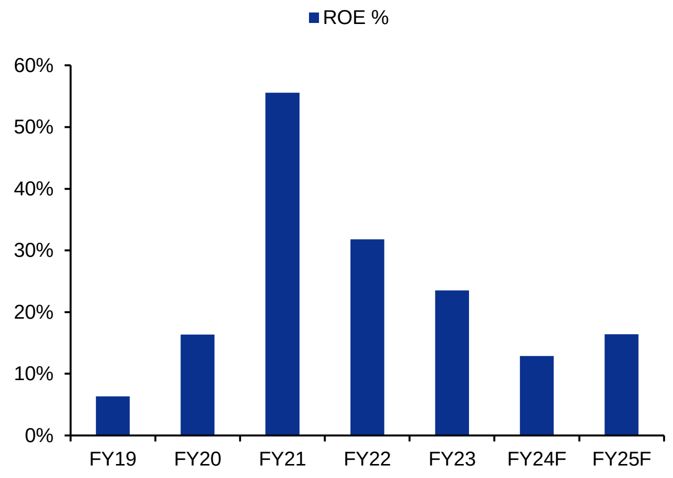
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 180: RoCE on a declining trend



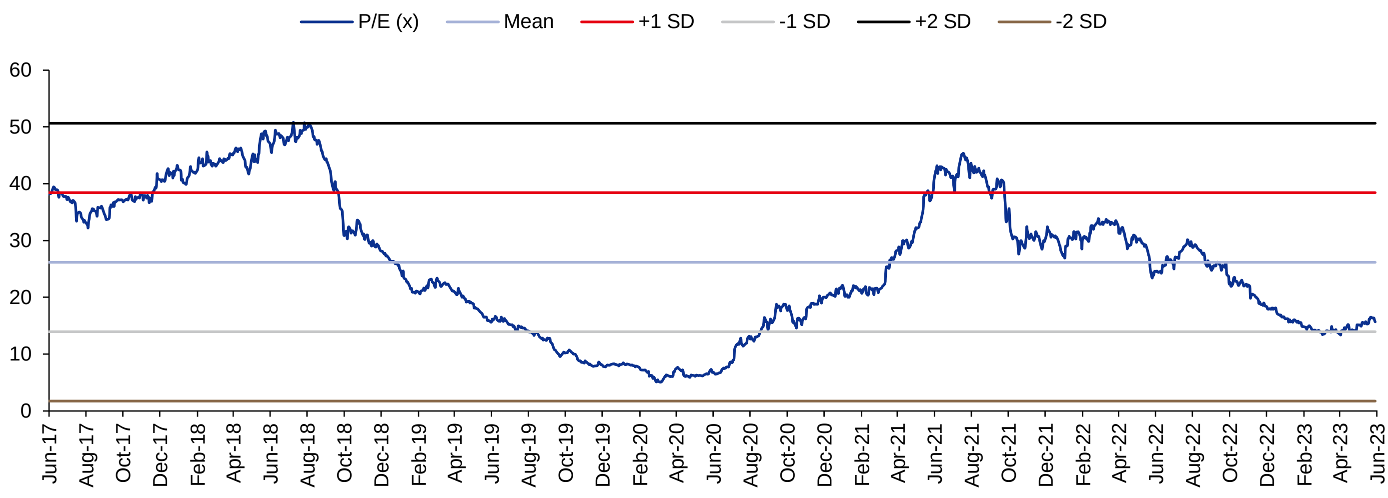
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 181: RoE on a declining trend as well



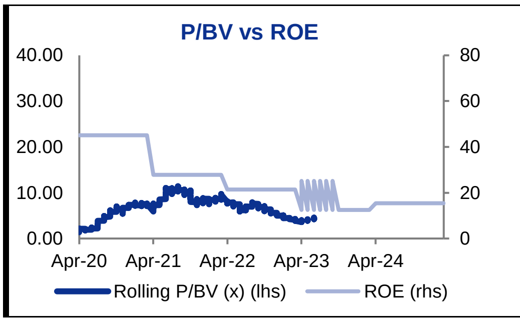
SOURCE: INCRED RESEARCH, COMPANY REPORTS

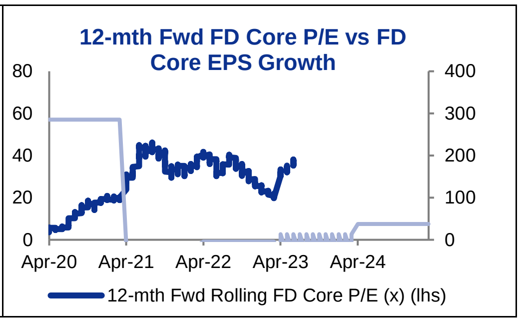
Figure 182: One-year forward P/E



SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Net Revenues	**48,135**	**49,356**	**60,406**	**56,497**	**64,089**
Gross Profit	**26,553**	**27,418**	**32,662**	**29,748**	**33,967**
Operating EBITDA	**15,507**	**14,224**	**15,922**	**12,548**	**15,738**
Depreciation And Amortisation	(2,051)	(2,515)	(3,241)	(3,700)	(4,200)
Operating EBIT	**13,456**	**11,709**	**12,681**	**8,848**	**11,538**
Financial Income/(Expense)	(682)	(1,024)	(1,652)	(2,000)	(2,100)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	237	153	60	100	100
Profit Before Tax (pre-EI)	**13,011**	**10,839**	**11,089**	**6,948**	**9,538**
Exceptional Items					
Pre-tax Profit	**13,011**	**10,839**	**11,089**	**6,948**	**9,538**
Taxation	(3,173)	(2,515)	(3,123)	(1,737)	(2,384)
Exceptional Income - post-tax					
Profit After Tax	**9,838**	**8,324**	**7,966**	**5,211**	**7,153**
Minority Interests	(2)	(49)	(65)		
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**9,836**	**8,275**	**7,901**	**5,211**	**7,153**
Recurring Net Profit	9,836	8,275	7,901	5,211	7,153
Fully Diluted Recurring Net Profit	**9,836**	**8,275**	**7,901**	**5,211**	**7,153**

Cash Flow

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
EBITDA	15,507	14,224	15,922	12,548	15,738
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(5,941)	(3,416)	(3,153)	1,054	(3,215)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	(2,236)	(1,697)	(2,830)	(1,737)	(2,384)
Net Interest (Paid)/Received	(682)	(1,024)	(1,652)	(2,000)	(2,100)
Tax Paid	(1,791)	(826)	(1,239)	163	(384)
Cashflow From Operations	**7,330**	**9,111**	**9,939**	**11,865**	**10,138**
Capex	(6,839)	(8,767)	(9,875)	(11,000)	(9,000)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments	(2,583)	(276)	(223)		
Other Investing Cashflow					
Cash Flow From Investing	**(2,092)**	**68**	**(159)**	**865**	**1,138**
Debt Raised/(repaid)					
Proceeds From Issue Of Shares	74	43	74		
Shares Repurchased					
Dividends Paid	(750)	(859)	(1,404)	(2,155)	(1,080)
Preferred Dividends					
Other Financing Cashflow	3,237	1,022	1,207	2,329	(644)
Cash Flow From Financing	**2,561**	**207**	**(122)**	**174**	**(1,724)**
Total Cash Generated	469	274	(281)	1,040	(586)
Free Cashflow To Equity	**5,238**	**9,179**	**9,780**	**12,731**	**11,277**
Free Cashflow To Firm	**5,920**	**10,203**	**11,432**	**14,731**	**13,377**

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Cash And Equivalents	491	766	485	1,524	938
Total Debtors	13,061	13,542	15,804	15,819	17,945
Inventories	15,755	17,603	16,848	18,079	20,508
Total Other Current Assets	1,442	1,536	1,480	1,977	2,243
Total Current Assets	**30,749**	**33,446**	**34,617**	**37,400**	**41,635**
Fixed Assets	22,772	32,086	37,002	44,302	49,102
Total Investments	34	308	499	499	499
Intangible Assets	2,556	2,571	2,592	2,592	2,592
Total Other Non-Current Assets	1,396	1,269	1,894	1,894	1,894
Total Non-current Assets	**26,758**	**36,234**	**41,987**	**49,287**	**54,087**
Short-term Debt	8,861	11,357	12,106	12,106	12,106
Current Portion of Long-Term Debt					
Total Creditors	11,787	8,764	7,107	8,937	9,893
Other Current Liabilities	3,923	6,690	5,111	6,077	6,727
Total Current Liabilities	**24,572**	**26,810**	**24,323**	**27,120**	**28,726**
Total Long-term Debt	4,292	5,963	7,614	11,843	13,199
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	2,637	3,316	4,181	4,181	4,181
Total Non-current Liabilities	**6,928**	**9,280**	**11,795**	**16,024**	**17,380**
Total Provisions					
Total Liabilities	**31,500**	**36,090**	**36,117**	**43,144**	**46,105**
Shareholders Equity	25,976	33,512	40,375	43,432	49,505
Minority Interests	32	79	111	111	111
Total Equity	**26,007**	**33,591**	**40,487**	**43,543**	**49,617**

Key Ratios

	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue Growth	70.0%	2.5%	22.4%	(6.5%)	13.4%
Operating EBITDA Growth	174.7%	(8.3%)	11.9%	(21.2%)	25.4%
Operating EBITDA Margin	32.2%	28.8%	26.4%	22.2%	24.6%
Net Cash Per Share (Rs)	(23.50)	(30.73)	(35.71)	(41.63)	(45.23)
BVPS (Rs)	48.22	62.21	74.95	80.62	91.90
Gross Interest Cover	19.74	11.44	7.68	4.42	5.49
Effective Tax Rate	24.4%	23.2%	28.2%	25.0%	25.0%
Net Dividend Payout Ratio					
Accounts Receivables Days	79.52	98.37	88.66	102.15	96.15
Inventory Days	209.77	277.50	226.63	238.30	233.79
Accounts Payables Days	151.73	170.96	104.40	109.46	114.09
ROIC (%)	24.4%	16.5%	15.0%	9.5%	11.1%
ROCE (%)	40.5%	26.0%	22.8%	13.9%	16.2%
Return On Average Assets	21.8%	14.3%	12.6%	8.2%	9.6%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Sun Pharmaceutical Industries

Strong all the way, but faces minor hurdles

- FY24F results would be marred by import alert at Halol plant, gradual sales recovery at Mohali plant and higher R&D spending (Sun Pharma gave guidance of +250bp higher spending YoY). FY25F to be the year of recovery.
- We like the company's increasing shift towards the non-US generics business, with specialty/branded businesses now contributing 85% to its sales. This provides a more sustainable revenue stream, and a better profitability profile.
- Resume coverage on the stock with an ADD rating and a TP of Rs1,095.

Specialty segment has a long runway for growth

Over the past few years, Sun Pharma or SUNP has silently graduated to a specialty-focused/brand-driven business. The specialty segment now contributes 16% to its overall sales (vs. ~10% in FY21), with Ilumya spearheading the segment's growth (Ilumya's share has doubled from 27% in FY20 to 55% in FY23 in the specialty segment's revenue). SUNP has further expanded its portfolio inorganically with acquisitions of Levulan, Absorica, Bromsite, Odomzo, Yonsa, Xelpros, Cequa, Winlevi, Sezaby and Deuroxolinib. We believe that Ilumya still has a significant potential for growth, particularly in its approved indication for treating psoriasis. By improving patient footfalls and enhancing access to payor channels, Ilumya can further expand its market share. Also, the recent acquisition of Deuroxolinib, a Phase-3 drug for alopecia areata disease, via the Concert deal, has provided SUNP with growth opportunities beyond Ilumya's peak sales. In addition to its specialty segment, the contribution of branded businesses (India/RoW/EMs) is also large at ~70% and has been largely stable over the past five years. With 85%+ now coming from specialty/branded businesses, SUNP has a much consistent earnings profile with strong profitability, which should further expand as the specialty segment's sales ramp up further.

Wild swings in profitability no more an area of concern

SUNP's margins have ranged between 20%-44% over FY12-20, when they relied more on the US generics business. They are now in a more stable range of 25-26%, despite absorbing the competition in gAbsorica, normalization of SG&A expenses and a sharp fall in Taro's margins (from 41% in FY20 to 8.5% in FY23) over the past three years. We feel SUNP's US specialty portfolio is now close to breakeven and further ramp-up should keep margins sanguine in the medium term. We bake in higher R&D spending (+Rs10bn in FY24, +150bp YoY at the lower end of management guidance of 7-8%) in FY24F, factoring in clinical trials for psoriatic arthritis in case of Ilumya and long-term studies for Deuroxolinib). Despite this, we expect overall margins to rise by ~80bp over FY23-25F.

Resume coverage with an ADD rating; Taro buyout is a potential +ve

Resume coverage on SUNP with an ADD rating and a TP of Rs1,095, valuing the stock at 25x FY25F EPS. SUNP has made a non-binding offer to acquire Taro at US$38/share (US$300m deal value). If successful, SUNP will get access to Taro's US$1.3bn cash surplus – a key near-term trigger. Slowdown in specialty portfolio is a key downside risk.

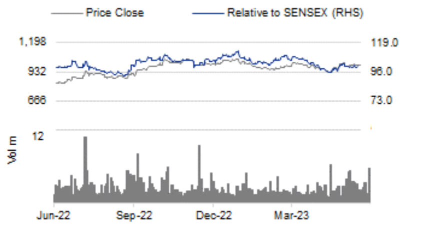
India

ADD *(no change)*

Consensus ratings*:	Buy 39	Hold 0	Sell 2

Current price:	Rs995
Target price: ▼	Rs1,095
Previous target:	Rs1,187
Up/downside:	10.1%
InCred Research / Consensus:	-3.8%
Reuters:	SUN.NS
Bloomberg:	SUNP IN
Market cap:	US$29,097m
	Rs2,387,162m
Average daily turnover:	US$28.4m
	Rs2329.5m
Current shares o/s:	2,399.3m
Free float:	45.5%

**Source: Bloomberg*



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	2.6	2.3	20.7
Relative (%)	1.8	(6.4)	1.9

Major shareholders	% held
Promoters	54.5
ICICI Pru MF	3.3
LIC	3.2

Financial Summary	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue (Rsm)	334,981	386,545	438,857	480,740	521,868
Operating EBITDA (Rsm)	84,677	102,438	117,729	128,389	144,130
Net Profit (Rsm)	29,038	32,727	84,736	89,513	104,730
Core EPS (Rs)	30.1	32.4	36.0	37.3	43.7
Core EPS Growth	79.1%	7.7%	11.4%	3.5%	17.0%
FD Core P/E (x)	33.11	30.75	27.61	26.67	22.79
DPS (Rs)	5.5	10.0	11.5	11.5	11.5
Dividend Yield	0.55%	1.01%	1.16%	1.16%	1.16%
EV/EBITDA (x)	28.15	21.97	19.76	17.65	15.16
P/FCFE (x)	35.22	25.13	28.32	17.77	11.03
Net Gearing	(6.3%)	(22.6%)	(15.2%)	(22.9%)	(31.6%)
P/BV (x)	5.14	4.97	4.26	3.84	3.41
ROE	15.7%	16.4%	16.6%	15.1%	15.9%
% Change In Core EPS Estimates				3.07%	3.34%
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Analyst(s)

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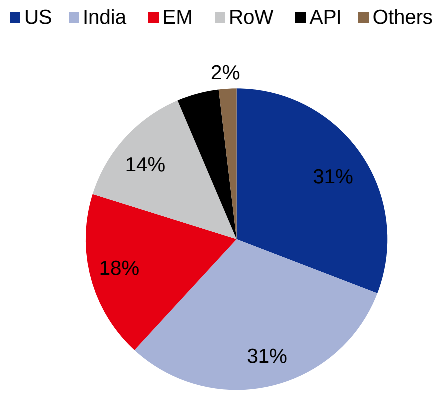
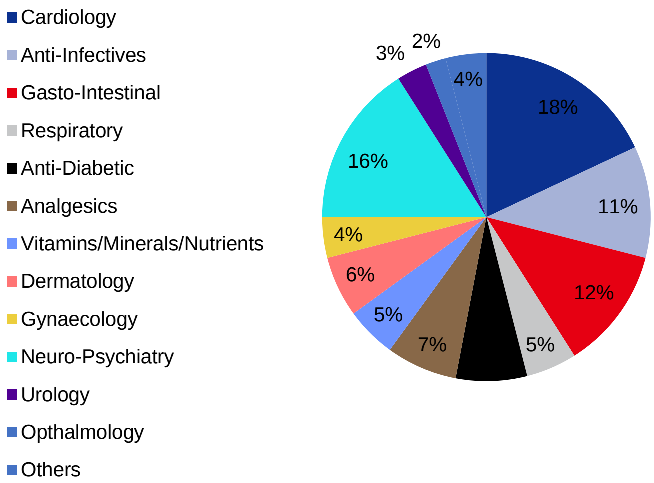
E kashish.thakur@incredcapital.com

Figure 183: Geographical breakup of SUNP's overall business – rising share of non-US generic businesses



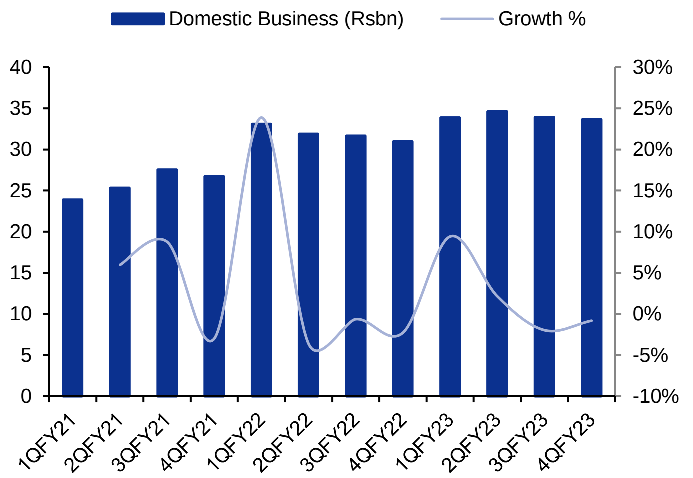
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 184: Therapy-wise break-up of SUNP's India business



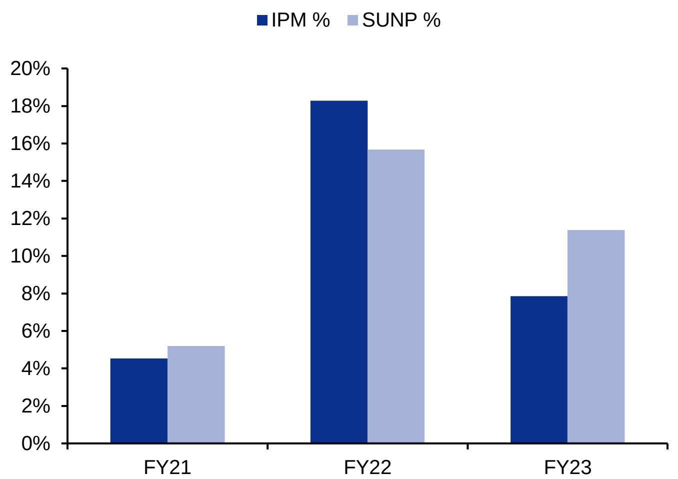
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 185: Domestic revenue growth – maintains dominant position in India



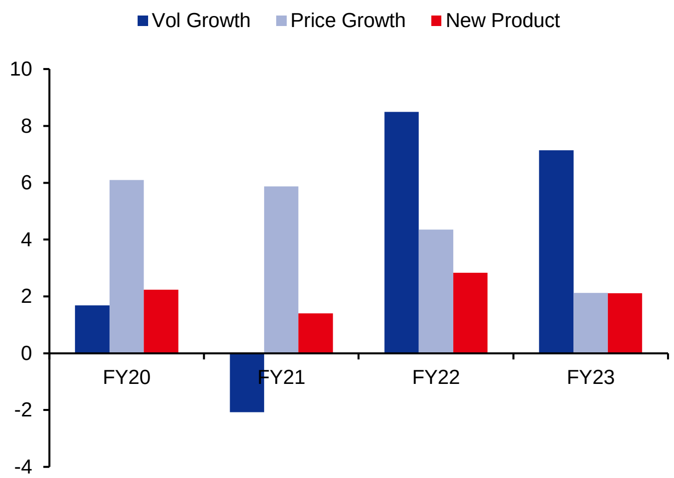
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 186: SUNP's India growth has broadly treaded IPM



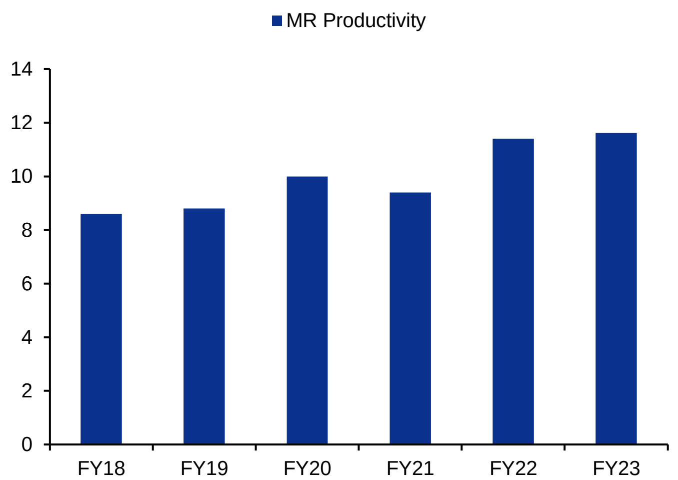
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 187: Growth drivers of India business – volumes have picked up well in last two years, which is a very healthy sign



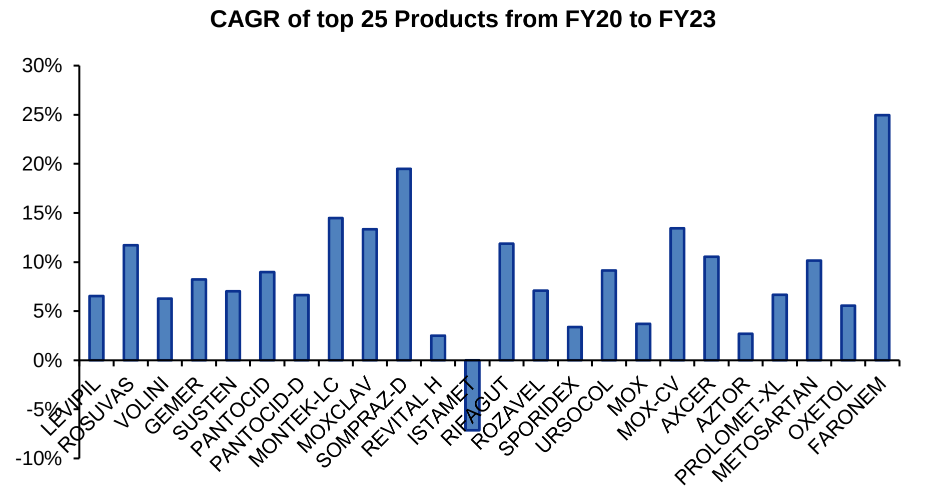
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 188: Growth drivers of India business – volumes have picked up well in last two years, which is a very healthy sign



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 189: CAGR of top-25 products – most recent launches have been doing well



SOURCE: INCRED RESEARCH, COMPANY REPORTS

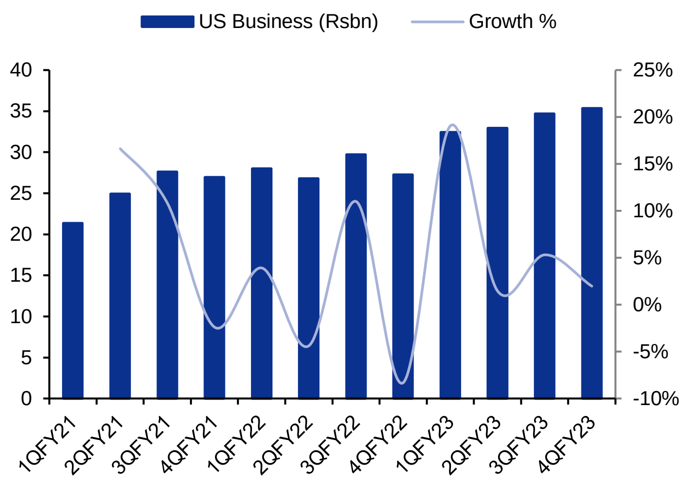
Figure 190: Prescription data of key therapeutic areas of SUNP

	Oct'18	Oct'19	Oct'20	Oct'21	Oct'22
Specialists	1	1	1	1	1
Psychiatrists	1	1	1	1	1
Neurologists	1	1	1	1	1
Cardiologists	1	1	1	1	1
Orthopaedics	1	1	1	1	1
Gastroenterologists	1	1	1	1	1
Diabetologists	1	1	1	1	1
Dermatologists	1	1	1	1	1
Urologists	1	1	1	1	1
Consulting Physicians	2	1	1	1	1
ENT	2	2	2	1	1
Chest Physicians	3	2	2	1	1
Nephrologists	1	1	2	2	1
Ophthalmologists	1	2	2	2	2

SOURCE: INCRED RESEARCH, COMPANY REPORTS

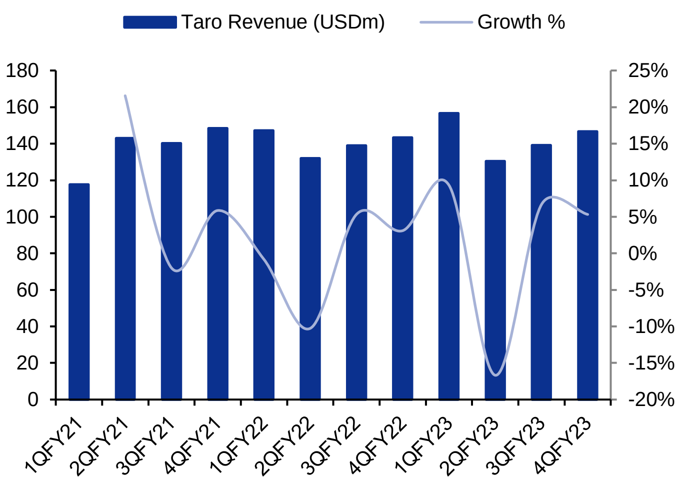
US business has been a mix of declining generics revenue and Improving specialty business,

Figure 191: US revenue – declining generics business, improving specialty revenue



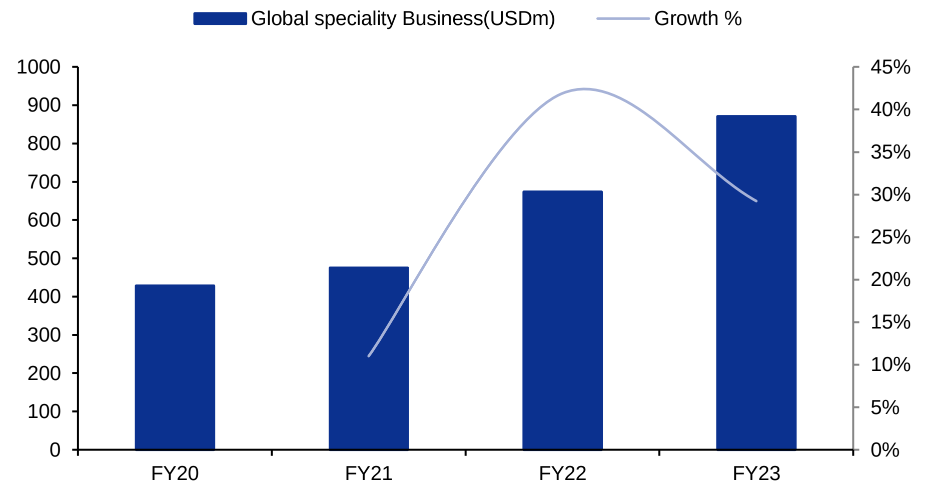
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 192: Taro's revenue has been on a declining trend



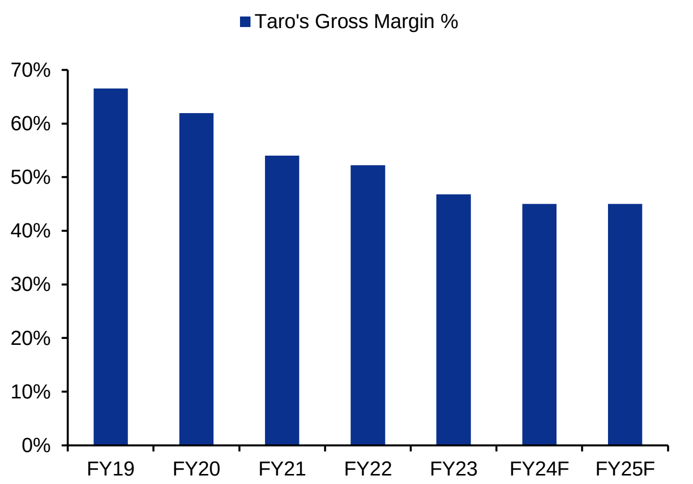
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 193: Global specialty business – revenue ramp-up has been encouraging…



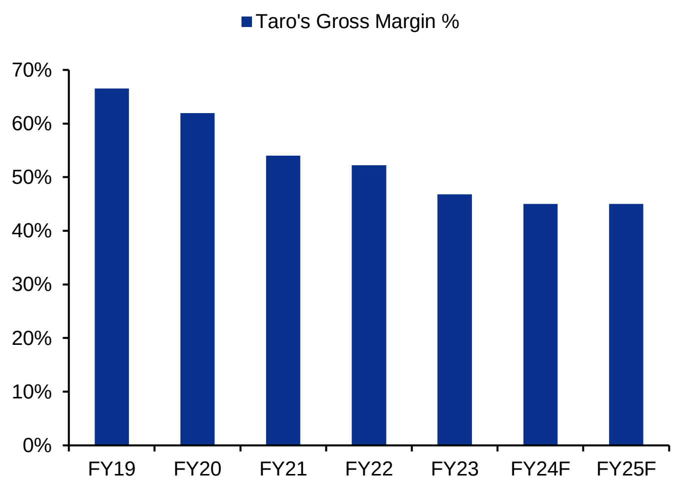
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 194: …and so is its gross margin…



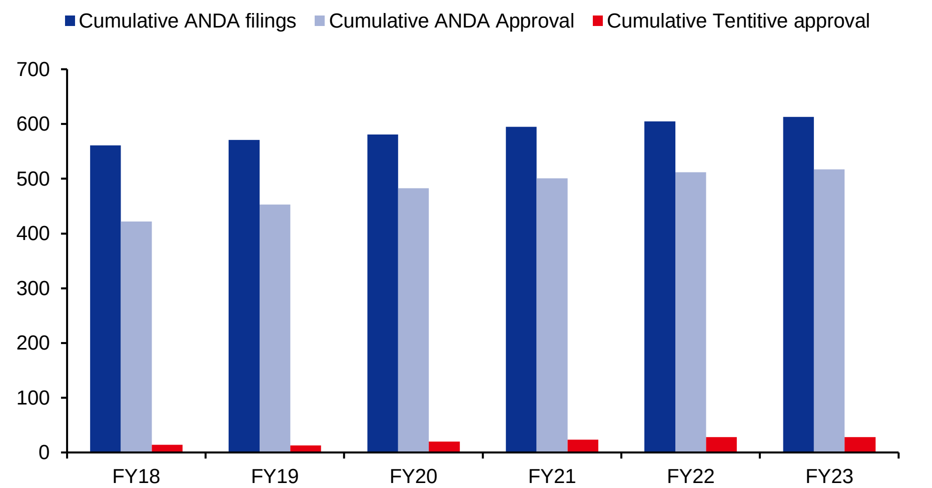
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 195: …and EBITDA margin



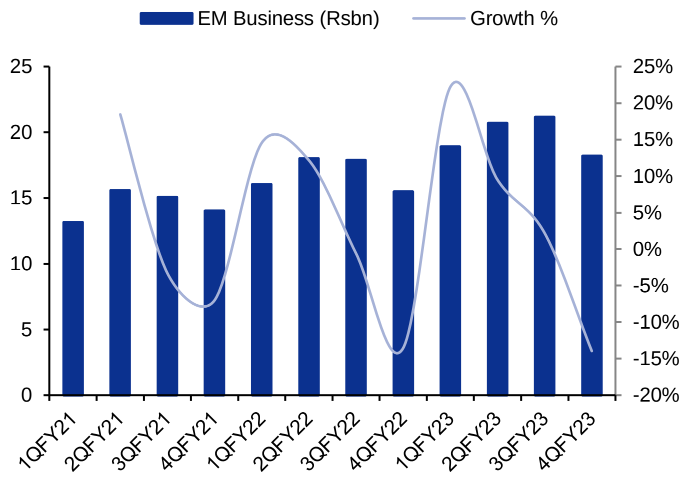
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 196: ANDA filings and approvals data



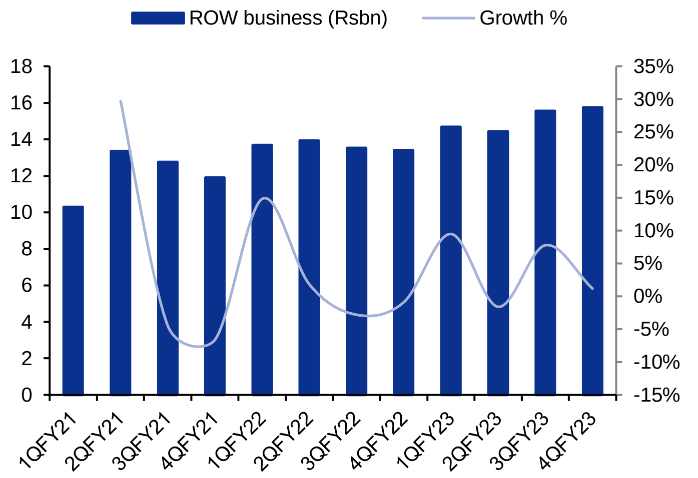
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 197: Steady growth in Ems



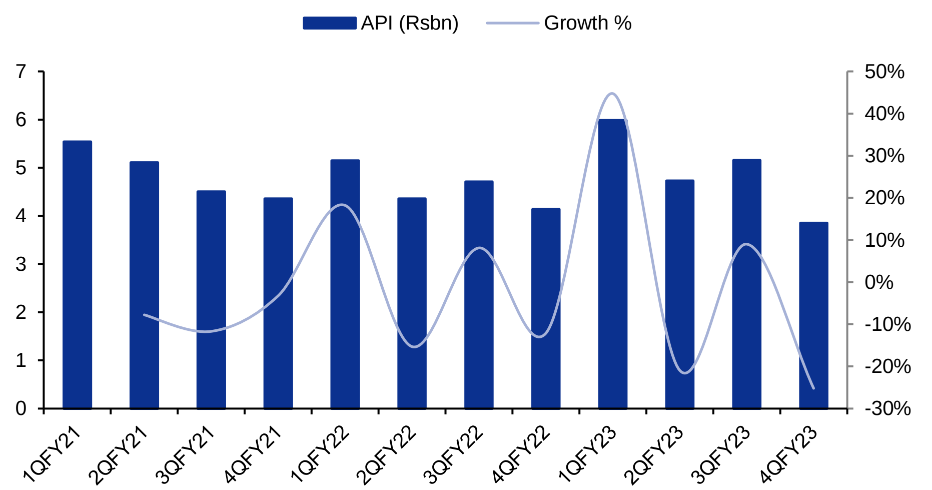
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 198: Steady growth in RoW market



SOURCE: INCRED RESEARCH, COMPANY REPORTS

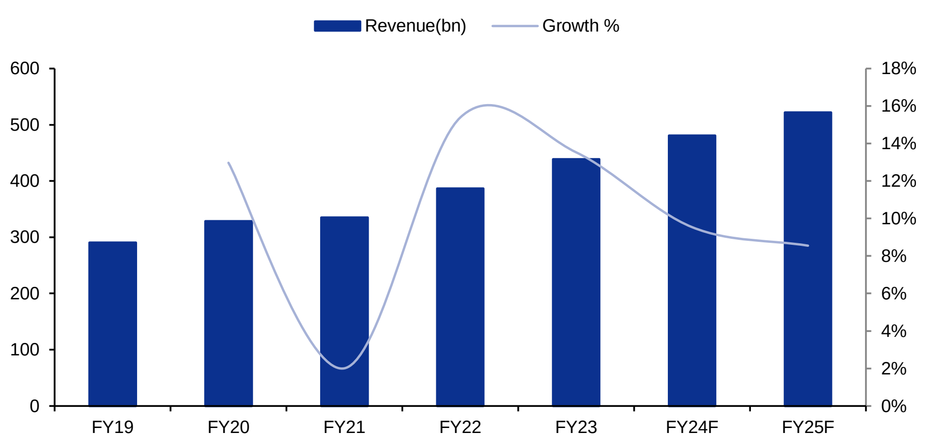
Figure 199: API is mostly used for captive consumption



SOURCE: INCRED RESEARCH, COMPANY REPORTS

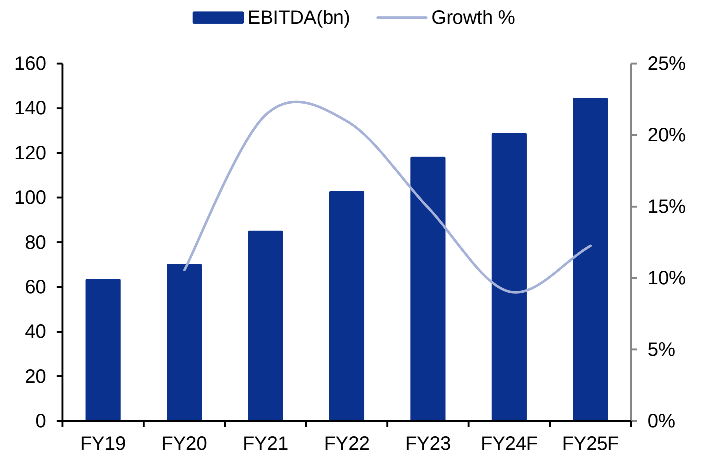
Rising contribution of specialty business and other branded businesses have lent stability to margins.

Figure 200: Revenue growth has been mixed with declining US generics revenue and improvement in rest of the business



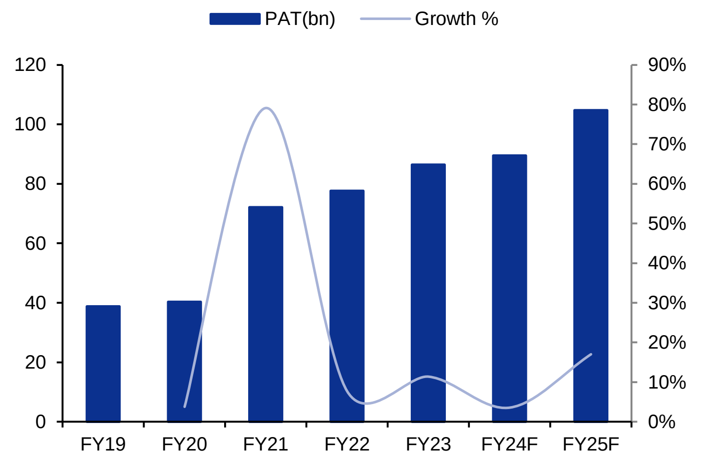
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 201: EBITDA improvement led by ramp-up in specialty portfolio



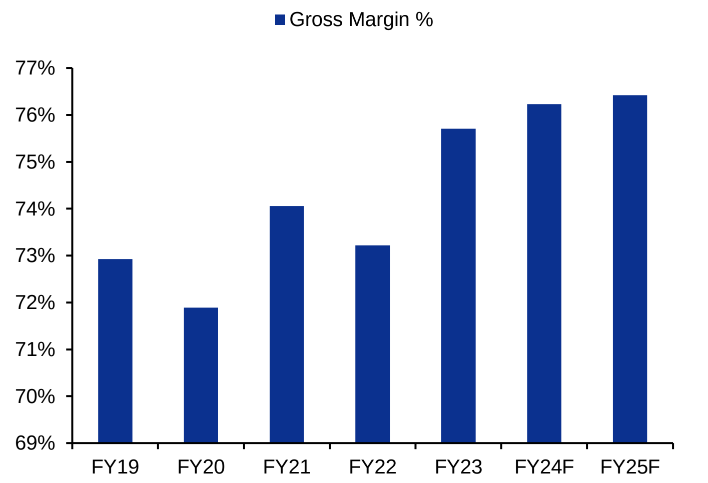
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 202: PAT growth has been steady



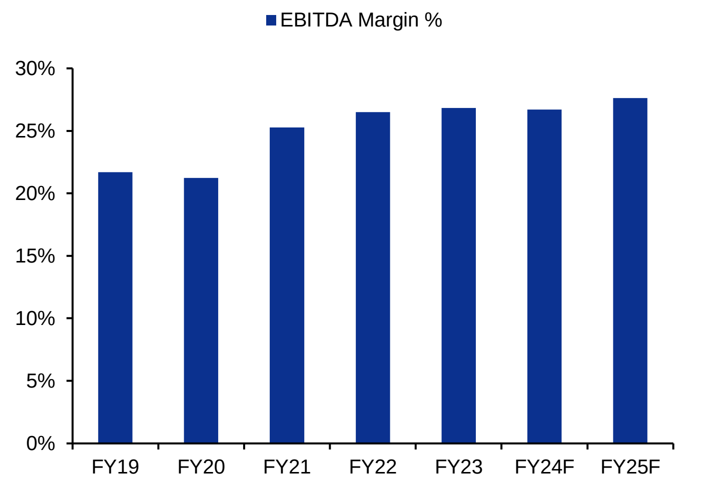
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 203: Gross margin over the past five years



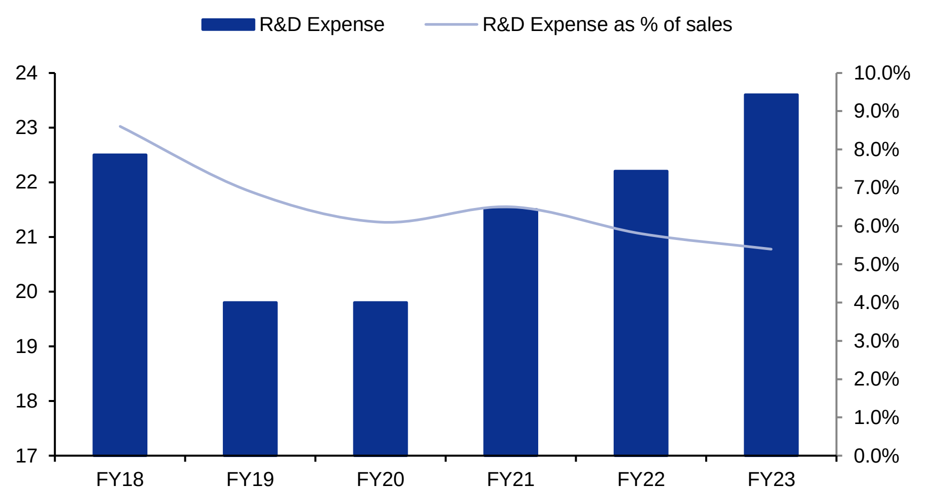
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 204: EBITDA margin over the past five years



SOURCE: INCRED RESEARCH, COMPANY REPORTS

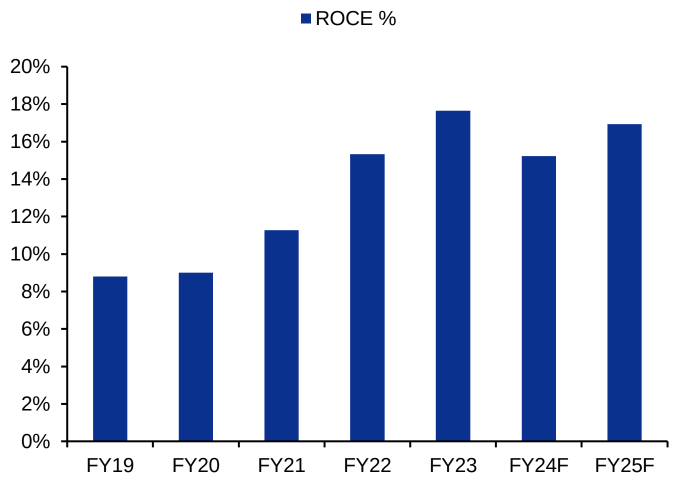
Figure 205: R&D spending moving up on clinical trials for specialty products



SOURCE: INCRED RESEARCH, COMPANY REPORTS

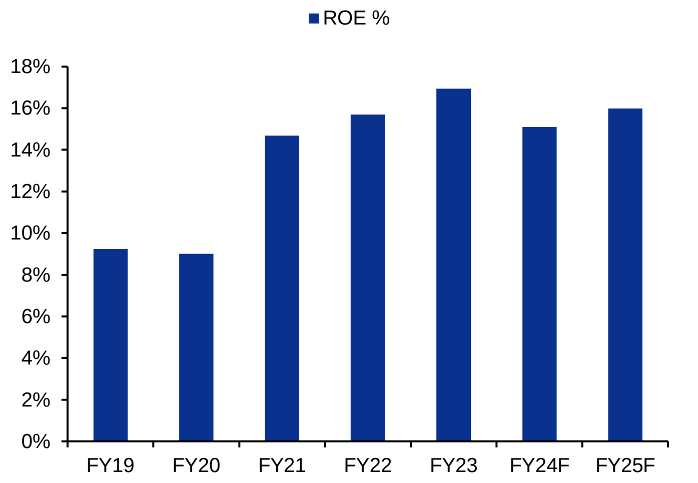
InCred Equities

Figure 206: RoCE trend of SUNP



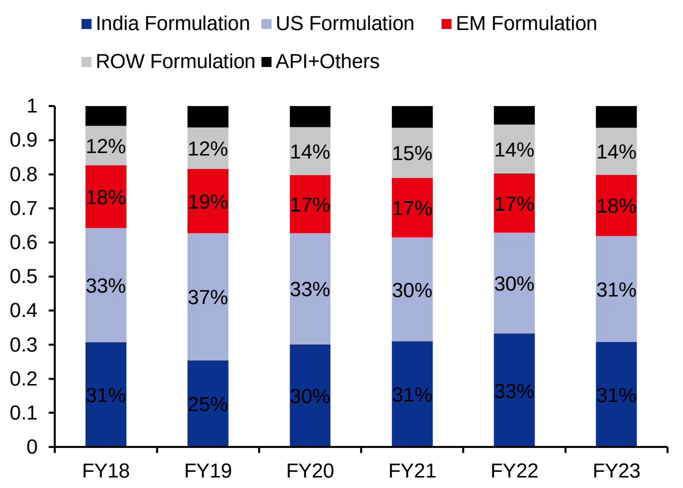
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 207: RoE trend of SUNP



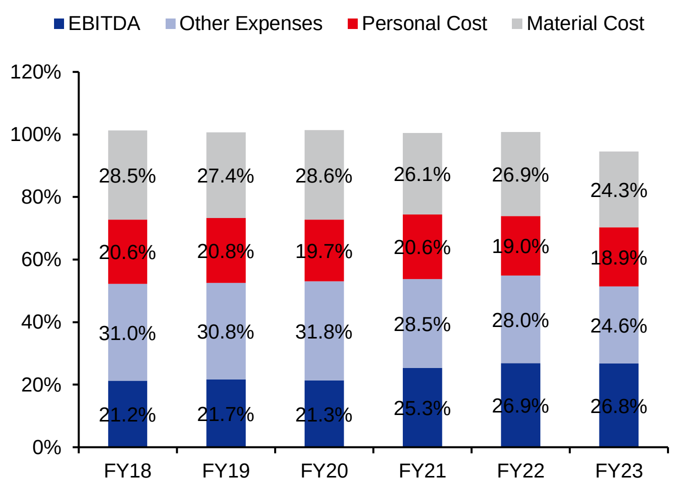
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 208: Business composition – share of non-US generics going up in the overall pie



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 209: Cost break-up – improving gross margin and declining operating expenses with ramp-up in specialty portfolio

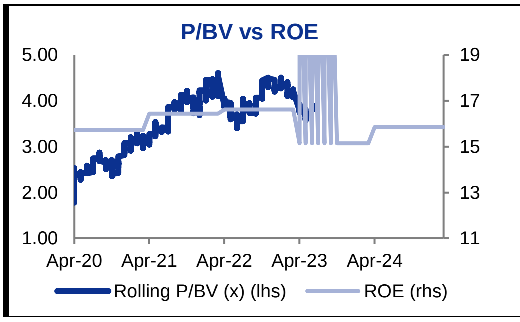


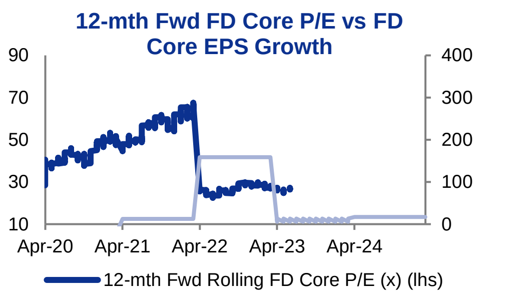
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 210: One-year forward P/E of SUNP

SOURCE: COMPANY REPORTS, INCRED RESEARCH

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Net Revenues	**334,981**	**386,545**	**438,857**	**480,740**	**521,868**
Gross Profit	**248,080**	**283,030**	**332,235**	**366,478**	**398,843**
Operating EBITDA	**84,677**	**102,438**	**117,729**	**128,389**	**144,130**
Depreciation And Amortisation	(20,800)	(21,437)	(25,294)	(28,617)	(30,946)
Operating EBIT	**63,878**	**81,000**	**92,435**	**99,773**	**113,184**
Financial Income/(Expense)	(1,414)	(1,274)	(1,720)	(3,000)	(2,000)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	8,592	10,755	5,084	6,000	9,000
Profit Before Tax (pre-EI)	**71,055**	**90,481**	**95,799**	**102,773**	**120,184**
Exceptional Items					
Pre-tax Profit	**71,055**	**90,481**	**95,799**	**102,773**	**120,184**
Taxation	(5,147)	(11,519)	(8,476)	(13,360)	(15,624)
Exceptional Income - post-tax	(43,061)	(44,904)	(1,715)		
Profit After Tax	**22,847**	**34,058**	**85,608**	**89,412**	**104,560**
Minority Interests	6,191	(1,331)	(873)	101	170
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**29,038**	**32,727**	**84,736**	**89,513**	**104,730**
Recurring Net Profit	72,099	77,631	86,450	89,513	104,730
Fully Diluted Recurring Net Profit	**72,099**	**77,631**	**86,450**	**89,513**	**104,730**

Cash Flow

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
EBITDA	84,677	102,438	117,729	128,389	144,130
Cash Flow from Invt. & Assoc.					
Change In Working Capital	25,641	15,591	(56,618)	(16,531)	(11,895)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	75,848	83,115	64,480	117,858	141,235
Net Interest (Paid)/Received	(1,414)	(1,274)	(1,720)	(3,000)	(2,000)
Tax Paid	(12,730)	8,004	(13,167)	(16,259)	(22,454)
Cashflow From Operations	**61,704**	**89,845**	**49,593**	**98,599**	**116,781**
Capex	(10,730)	(14,344)	(20,646)	(14,000)	(15,000)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments		(41,643)	(46,858)		
Other Investing Cashflow					
Cash Flow From Investing	**50,973**	**33,858**	**(17,911)**	**84,599**	**101,781**
Debt Raised/(repaid)	(44,896)	(28,718)	52,602	(48,877)	(2,118)
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid	(15,862)	(21,692)	(25,197)	(27,592)	(27,592)
Preferred Dividends					
Other Financing Cashflow	9,364	80,469	13,976	3,000	7,000
Cash Flow From Financing	**(51,394)**	**30,059**	**41,380**	**(73,469)**	**(22,710)**
Total Cash Generated	(420)	63,918	23,470	11,130	79,071
Free Cashflow To Equity	**67,781**	**94,986**	**84,284**	**134,321**	**216,444**
Free Cashflow To Firm	**114,091**	**124,977**	**33,403**	**186,199**	**220,562**

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Cash And Equivalents	64,455	128,373	151,842	162,972	242,043
Total Debtors	90,614	105,929	114,385	129,800	140,904
Inventories	89,970	89,968	105,131	115,378	125,248
Total Other Current Assets	59,382	25,880	27,476	31,248	33,921
Total Current Assets	**304,421**	**350,150**	**398,833**	**439,398**	**542,117**
Fixed Assets	111,715	111,689	113,537	98,921	82,975
Total Investments	2,327	52,147	3,894	3,894	3,894
Intangible Assets	119,483	125,777	180,396	180,396	180,396
Total Other Non-Current Assets	138,721	58,237	110,776	110,776	110,776
Total Non-current Assets	**372,247**	**347,849**	**408,603**	**393,986**	**378,040**
Short-term Debt	24,449	8,086	61,979	61,979	61,979
Current Portion of Long-Term Debt					
Total Creditors	39,737	44,793	56,815	57,690	62,211
Other Current Liabilities	97,271	119,126	80,276	92,304	99,537
Total Current Liabilities	**161,456**	**172,006**	**199,070**	**211,973**	**223,727**
Total Long-term Debt	8,981	4,817		(48,877)	(50,996)
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	11,431	10,515	15,211	15,211	15,211
Total Non-current Liabilities	**20,413**	**15,332**	**15,211**	**(33,666)**	**(35,784)**
Total Provisions					
Total Liabilities	**181,869**	**187,338**	**214,281**	**178,307**	**187,942**
Shareholders Equity	464,628	480,112	559,954	621,977	699,285
Minority Interests	30,171	30,549	33,201	33,100	32,930
Total Equity	**494,798**	**510,661**	**593,155**	**655,076**	**732,215**

Key Ratios

	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue Growth	2.0%	15.4%	13.5%	9.5%	8.6%
Operating EBITDA Growth	21.4%	21.0%	14.9%	9.1%	12.3%
Operating EBITDA Margin	25.3%	26.5%	26.8%	26.7%	27.6%
Net Cash Per Share (Rs)	12.93	48.13	37.45	62.46	96.30
BVPS (Rs)	193.65	200.11	233.38	259.23	291.45
Gross Interest Cover	45.17	63.60	53.74	33.26	56.59
Effective Tax Rate	7.2%	12.7%	8.8%	13.0%	13.0%
Net Dividend Payout Ratio					
Accounts Receivables Days	100.69	92.79	91.62	92.70	94.67
Inventory Days	354.33	317.24	333.94	352.20	356.95
Accounts Payables Days	169.42	149.03	173.92	182.89	177.87
ROIC (%)	10.1%	17.1%	13.4%	14.4%	16.5%
ROCE (%)	11.7%	15.4%	15.7%	15.1%	16.0%
Return On Average Assets	9.9%	11.6%	11.8%	11.2%	12.1%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Torrent Pharmaceuticals Ltd

Margins have more levers to expand

- One of the most successful chronic therapy-driven India franchise, with industry-leading profitability and operating metrics.
- A resilient and diverse business mix - with 70% contribution from branded generic markets, empowering the company to implement price hikes and lay a strong foundation for potential margin expansion in the future.
- Resume coverage on the stock with an ADD rating and a TP of Rs2,135.

One of the most successful domestic franchises over the last decade

TRP has built one of the most successful chronic therapy-driven domestic franchises in India (70%+ contribution), leveraging its strong relationships with specialist doctors, and is now the sixth-largest player in India (vs. 17th a decade ago). It is among the top-5 players in India in cardiovascular, CNS, gastro-intestinal and vitamin segments. TRP has leveraged this by impeccably integrating strategic acquisitions (Elder/Unichem/Curatio). Given its large chronic therapy-driven portfolio, TRP has been able to consistently outpace IPM growth and has one of the best MR productivity (at Rs900,000 pcpm). The ability to take large price hikes (7-8% annually) and improving productivity from the recently-added field force (+15% YoY) should, in our view, continue to drive the outperformance vs. IPM.

Brazil market recovers well, US should follow suit from FY25F

After a tepid performance in FY18-21, we see strong signs of a recovery in Brazil market (six-to-seven new launches p.a, increase in coverage with field force addition) over the last two years which, in our view, should continue. The US business outlook is still uncertain in the near term given compliance issues at key plants (Dahej/Indrad), although we expect it to recover from FY25F, assuming positive clearance by the USFDA (Dahej plant received two observations in a re-inspection). Notably, TRP has significantly scaled down its investments in the US (R&D rationalization, plant shutdown) to contain the cash burn.

Industry-leading margins; more levers for expansion

At ~30%, TRP's margins are one of the best in the industry. A large, branded generics franchise (70%+ contribution) empowers TRP to implement price hikes and sustain this profitability even as its export business faced headwinds over the last three years. We believe its margins have further levers for expansion led by a) price hikes in India/Brazil, b) improving profitability of the Curatio portfolio (300-400bp improvement already since integration; can go to TRP's India-level margins), and c) potential cut in plant-related remediation cost by 2HFY24F and likely launch of new products from affected plants (assuming clearance by end-FY24F), which should help absorb costs fixed better.

Resume coverage with an ADD rating

We resume coverage on TRP with an ADD rating (HOLD earlier) and a target price of Rs2,135, valuing it at 20x FY25 EV/EBITDA (to adjust for high amortization cost due to acquisitions in India), in line with its 5-year avg. Downside risk: Slowdown in India growth.

Financial Summary	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue (Rsm)	80,050	85,080	96,200	107,468	118,320
Operating EBITDA (Rsm)	24,850	24,310	28,420	33,010	37,232
Net Profit (Rsm)	12,520	7,770	12,450	16,464	19,587
Core EPS (Rs)	37.0	32.0	36.8	48.6	57.9
Core EPS Growth	22.1%	(13.4%)	14.8%	32.2%	19.0%
FD Core P/E (x)	50.49	58.29	50.77	38.39	32.27
DPS (Rs)	10.0	24.0	22.0	15.0	17.5
Dividend Yield	0.54%	1.28%	1.18%	0.80%	0.94%
EV/EBITDA (x)	26.66	27.42	23.84	20.30	17.55
P/FCFE (x)	17.69	18.54	27.24	17.35	12.88
Net Gearing	52.1%	58.5%	73.7%	54.2%	25.5%
P/BV (x)	10.83	10.62	10.20	8.90	7.39
ROE	23.5%	18.4%	20.5%	24.8%	25.0%
% Change In Core EPS Estimates				13.86%	13.71%
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

India

ADD *(previously HOLD)*

Consensus ratings*: Buy 25 Hold 5 Sell 4

Current price:	Rs1,868
Target price: ▲	Rs2,135
Previous target:	Rs1,509
Up/downside:	14.3%
InCred Research / Consensus:	15.3%
Reuters:	TORP.NS
Bloomberg:	TRP IN
Market cap:	US$7,705m
	Rs632,103m
Average daily turnover:	US$6.1m
	Rs503.7m
Current shares o/s:	338.4m
Free float:	29.0%

Source: Bloomberg

Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	9.9	23.0	30.2
Relative (%)	9.0	12.7	9.9

Major shareholders	% held
Promoters	71.0
ICICI Pru Life	1.3
BlackRock	1.2

Analyst(s)

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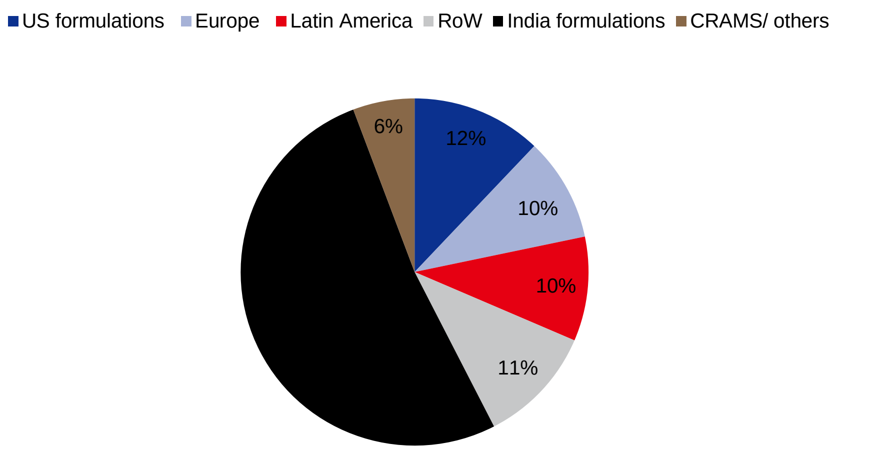
E kashish.thakur@incredcapital.com

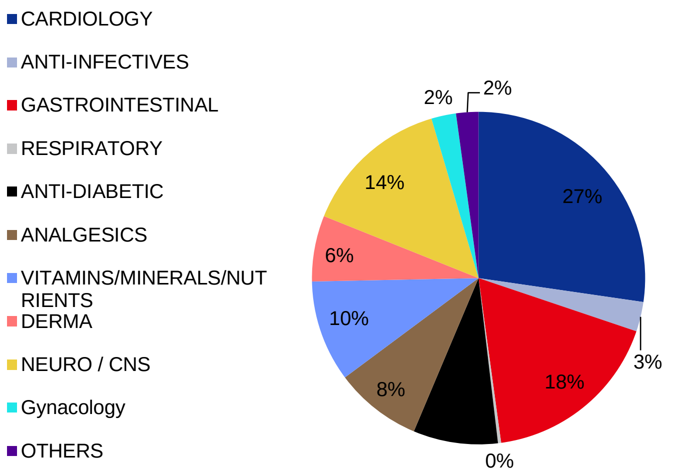
Figure 211: Revenue composition – India/RoW markets (branded generic markets) contribute 60%+ to revenue



SOURCE: INCRED RESEARCH, COMPANY REPORTS

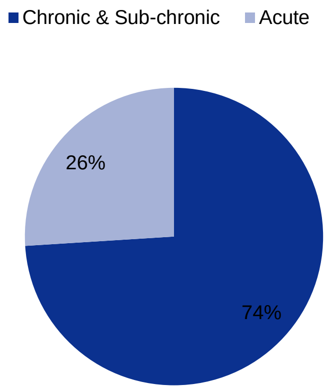
One of the most successful domestic franchises over the last decade.

Figure 212: Cardiology is the biggest contributor in TRP revenue



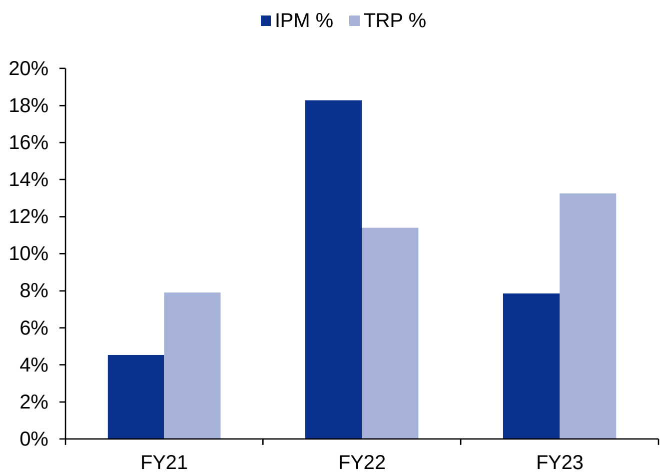
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 213: Sales driven by chronic and sub-chronic segments



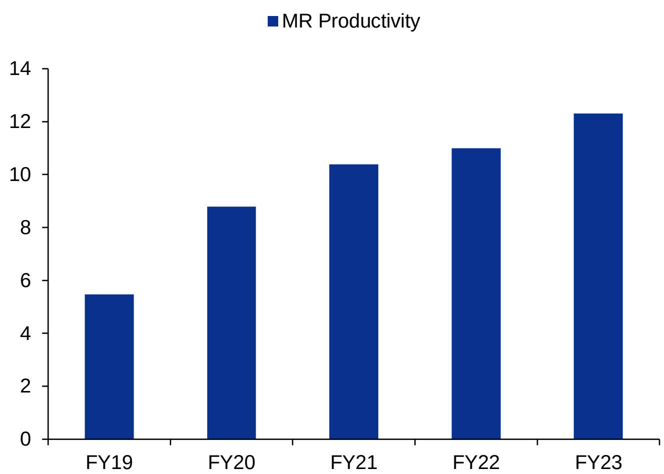
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 214: Consistently outperforms IPM growth



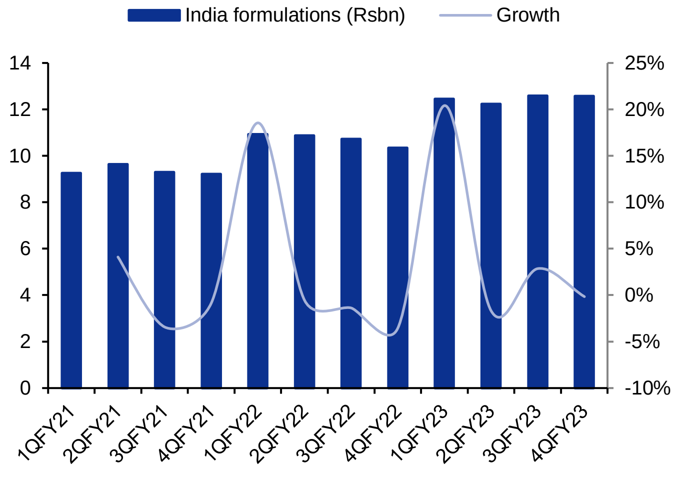
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 215: MR productivity – best in the industry



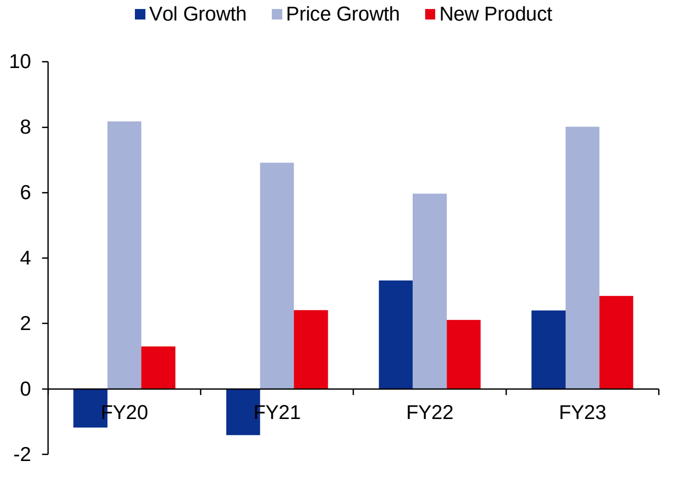
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 216: India business has been steadily growing



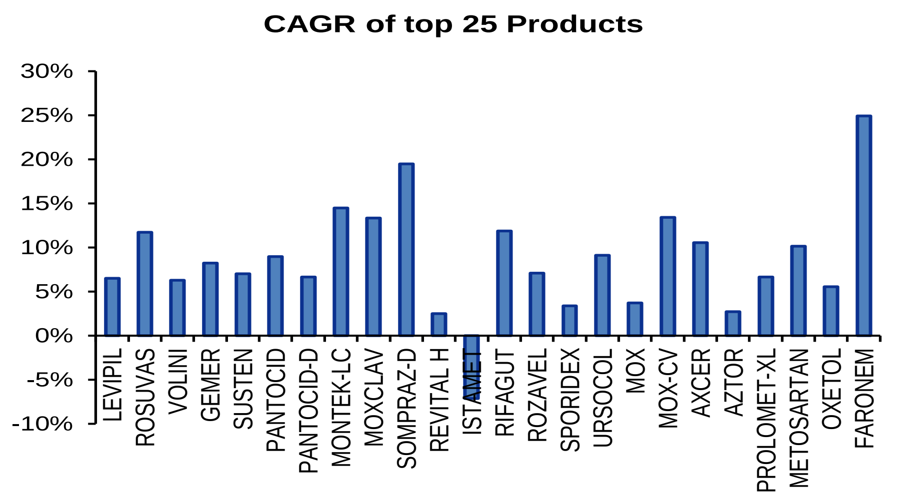
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 217: Price hikes have been a key driver of India business growth



SOURCE: INCRED RESEARCH, COMPANY REPORTS

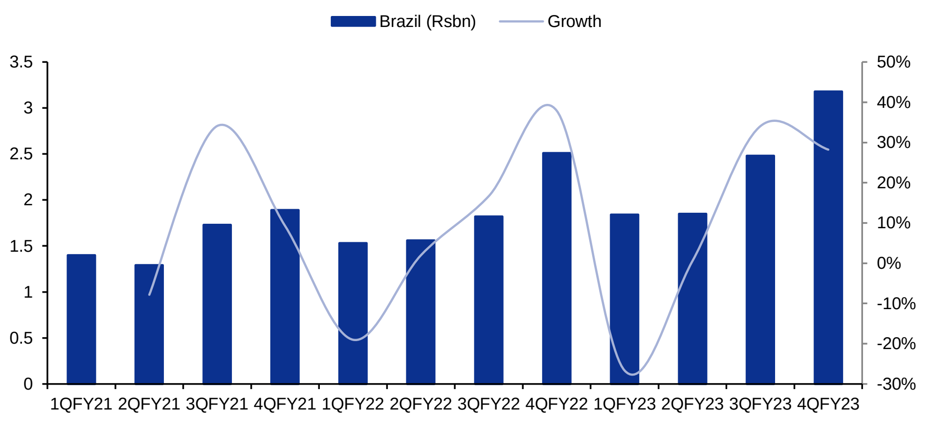
Figure 218: CAGR of top-25 products of TRP from FY20 to FY23



SOURCE: INCRED RESEARCH, COMPANY REPORTS

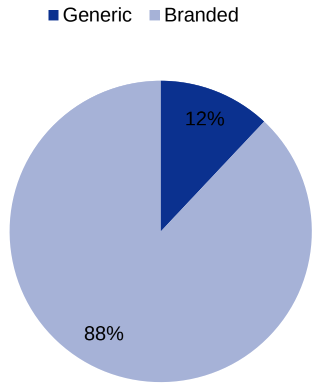
Brazil business is on the recovery path

Figure 219: Brazil business recovering post weak FY21/22



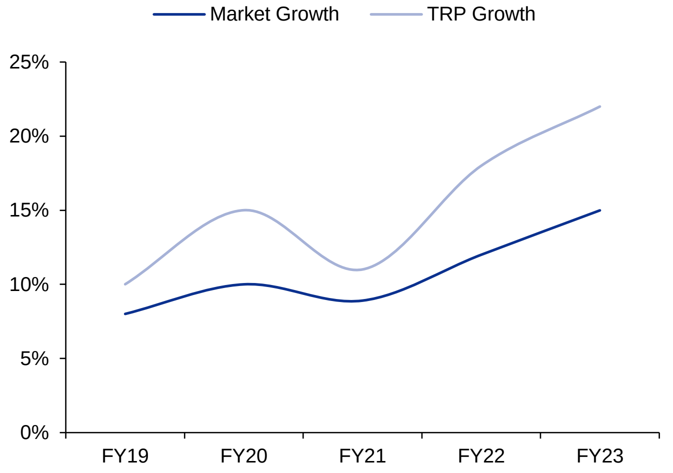
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 220: Brazil's revenue break-up – replicating India model



SOURCE: INCRED RESEARCH, COMPANY REPORTS

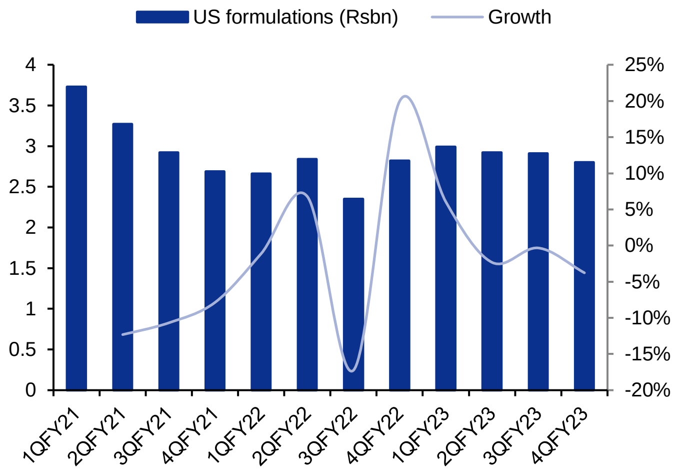
Figure 221: TRP has consistently grown ahead of the market in Brazil



SOURCE: INCRED RESEARCH, COMPANY REPORTS

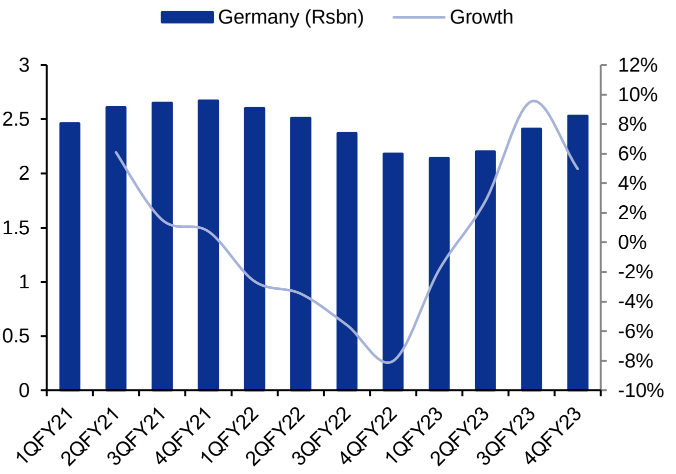
US performance impacted by warning letters at key plants. Germany has been volatile due to the tender-driven nature of the market.

Figure 222: US market performance impacted by warning letters for Indrad and Dahej plants



SOURCE: INCRED RESEARCH, COMPANY REPORTS

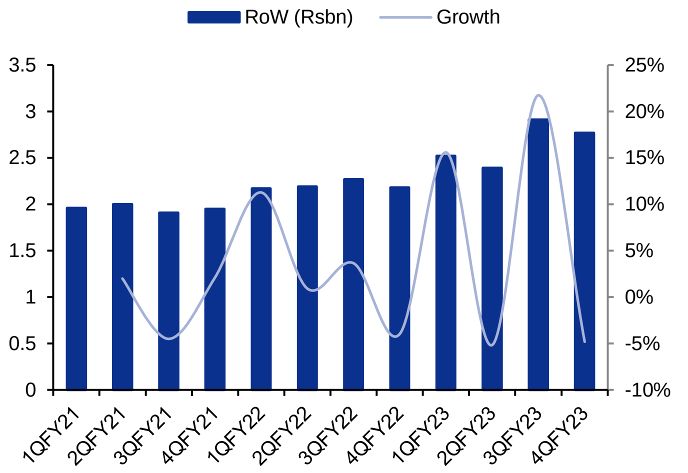
Figure 223: German market – been through a rough patch but now recovering



SOURCE: INCRED RESEARCH, COMPANY REPORTS

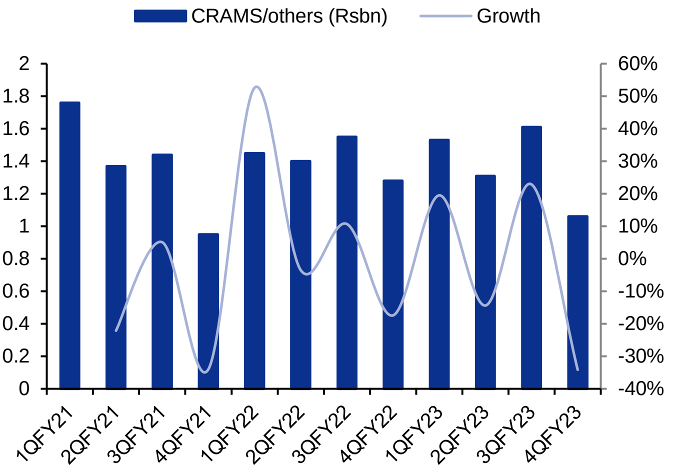
Steady performance in ROW markets and CRAMS business.

Figure 224: TRP's RoW performance has been steady



SOURCE: INCRED RESEARCH, COMPANY REPORTS

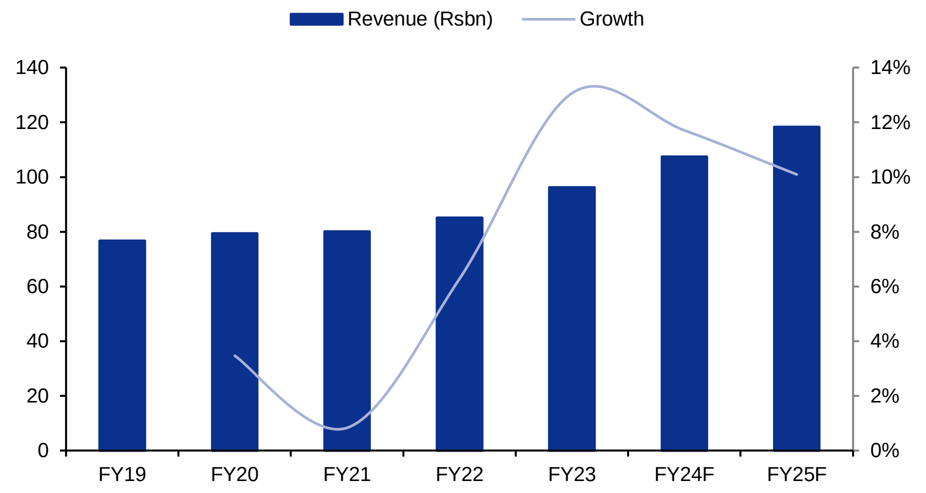
Figure 225: TRP's CRAMS business is small and growing at 5-6% annually



SOURCE: INCRED RESEARCH, COMPANY REPORTS

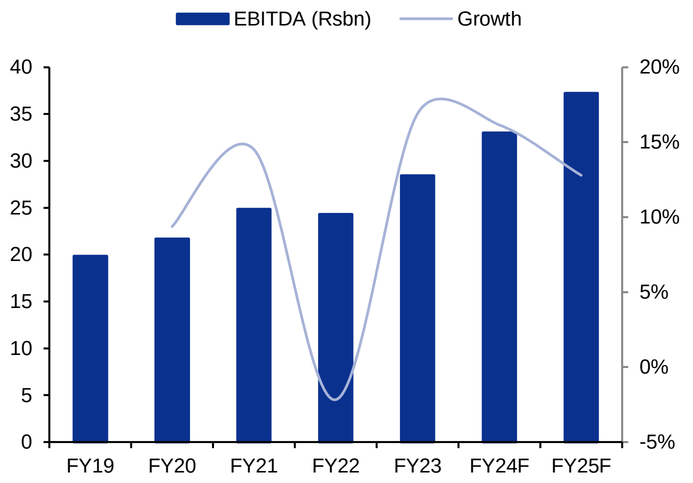
Strong operating metrics

Figure 226: Strong branded franchise has cushioned revenues even as exports business has faced headwinds in last three years



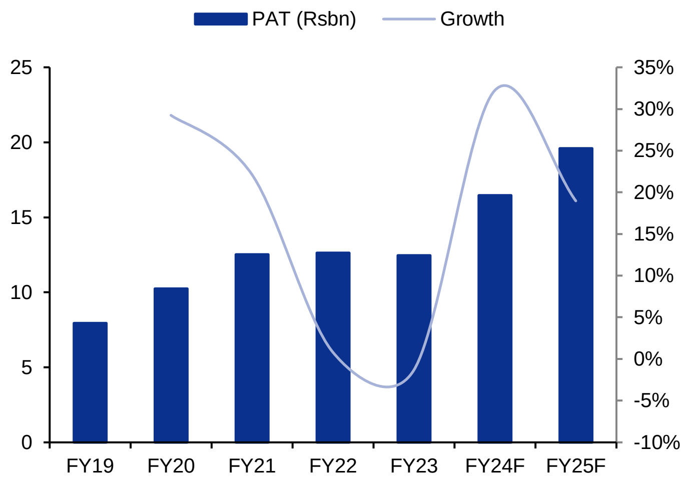
SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 227: EBITDA performance has largely been resilient despite export headwinds



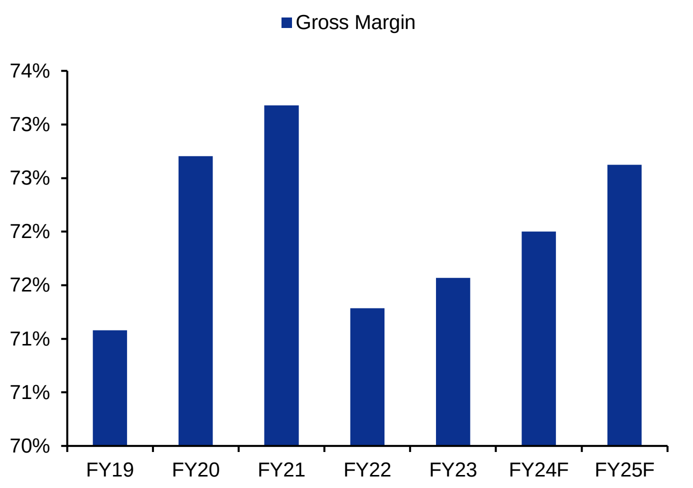
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 228: PAT has been impacted due to high depreciation cost from domestic acquisitions



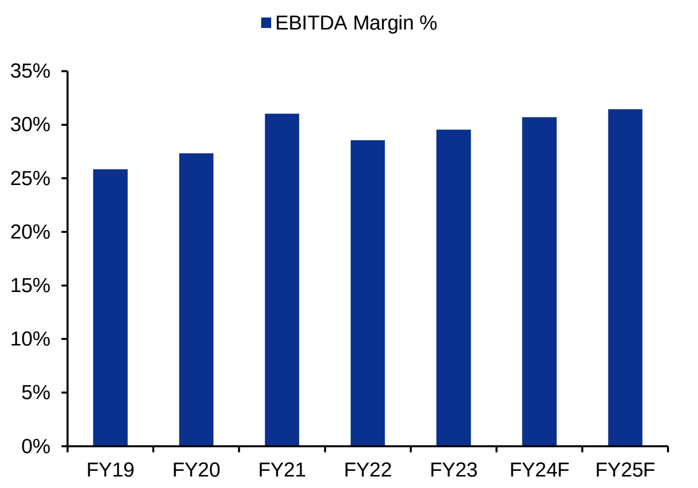
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 229: Price hikes power strong gross margin



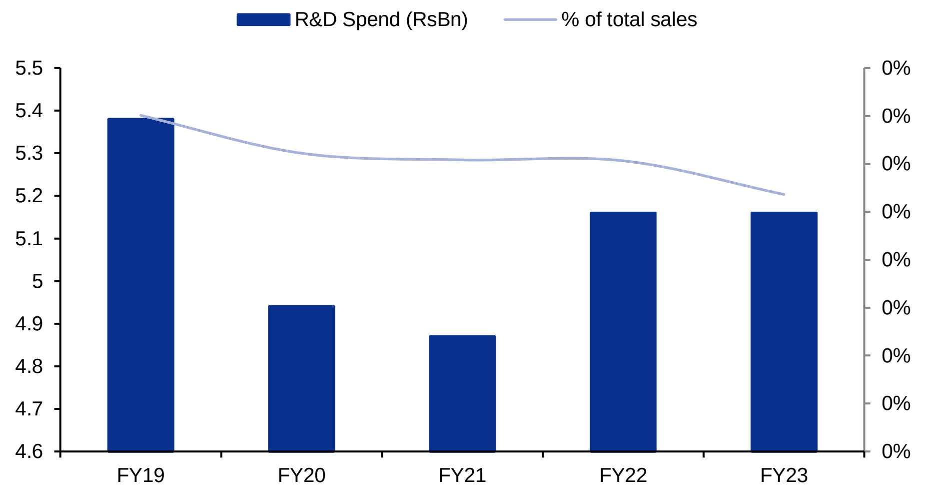
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 230: Despite export headwinds, EBITDA margin sustains



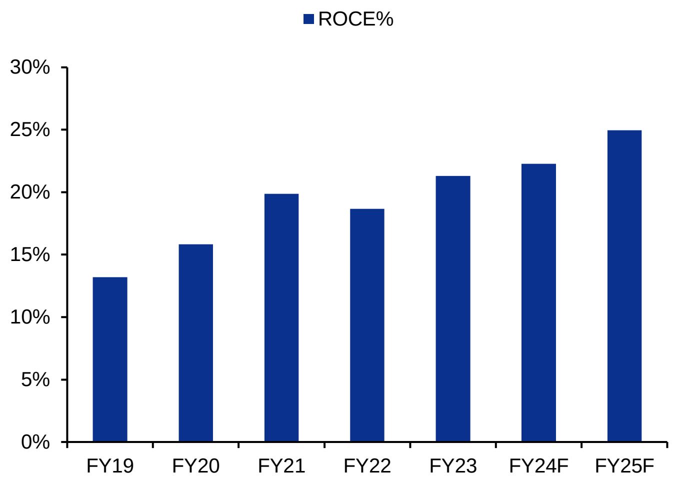
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 231: R&D spending – moving in a tight range



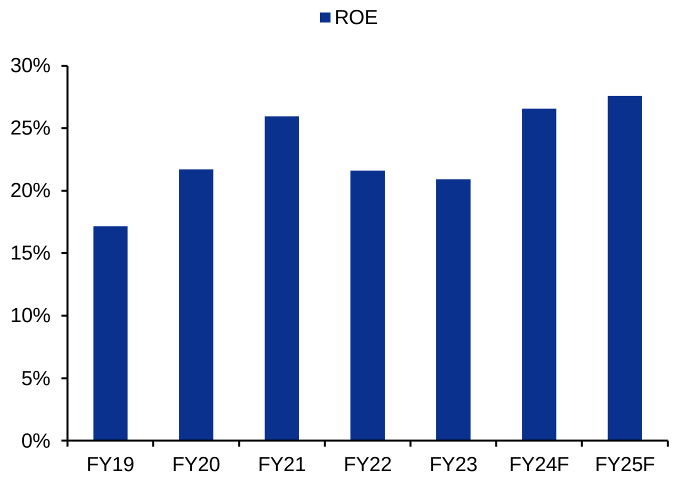
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 232: Strong branded market presence has led to strong RoCE…



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 233: …and RoE

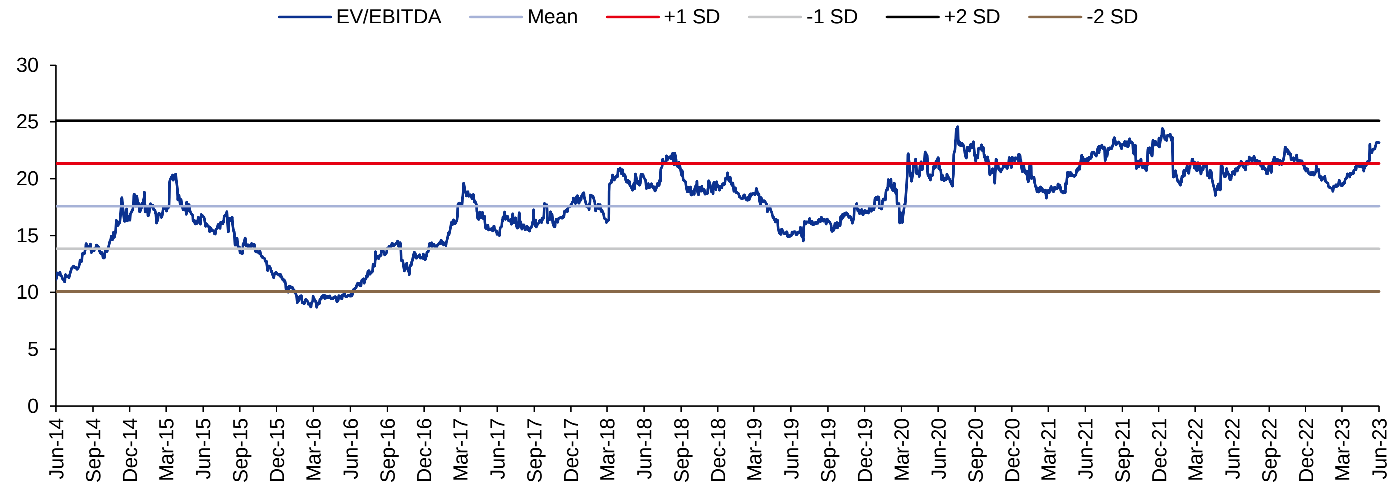


SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 234: One-year forward P/E

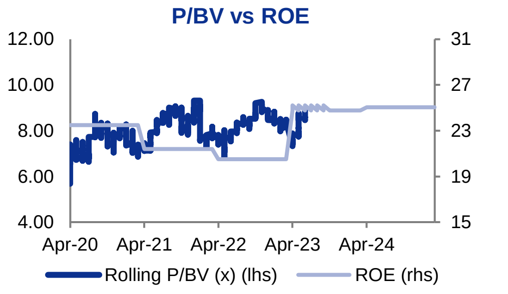
SOURCE: INCRED RESEARCH, COMPANY REPORTS

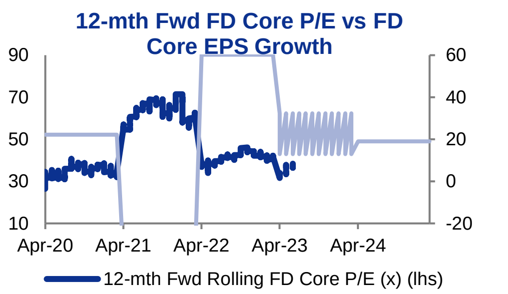
Figure 235: One-year forward EV/EBITDA



SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Net Revenues	**80,050**	**85,080**	**96,200**	**107,468**	**118,320**
Gross Profit	**58,580**	**60,650**	**68,850**	**77,377**	**85,929**
Operating EBITDA	**24,850**	**24,310**	**28,420**	**33,010**	**37,232**
Depreciation And Amortisation	(6,580)	(6,620)	(7,070)	(7,400)	(8,000)
Operating EBIT	**18,270**	**17,690**	**21,350**	**25,610**	**29,232**
Financial Income/(Expense)	(3,580)	(2,550)	(3,330)	(2,750)	(2,000)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	570	1,970	450	660	750
Profit Before Tax (pre-EI)	**15,260**	**17,110**	**18,470**	**23,520**	**27,982**
Exceptional Items		(4,850)			
Pre-tax Profit	**15,260**	**12,260**	**18,470**	**23,520**	**27,982**
Taxation	(2,740)	(4,490)	(6,020)	(7,056)	(8,394)
Exceptional Income - post-tax					
Profit After Tax	**12,520**	**7,770**	**12,450**	**16,464**	**19,587**
Minority Interests					
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**12,520**	**7,770**	**12,450**	**16,464**	**19,587**
Recurring Net Profit	12,520	10,844	12,450	16,464	19,587
Fully Diluted Recurring Net Profit	**12,520**	**10,844**	**12,450**	**16,464**	**19,587**

Cash Flow

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
EBITDA	24,850	24,310	28,420	33,010	37,232
Cash Flow from Invt. & Assoc.					
Change In Working Capital	(3,383)	(3,519)	(180)	(6,234)	(2,794)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	(1,358)	(2,762)	(4,560)	(7,056)	(8,394)
Net Interest (Paid)/Received	(3,580)	(2,550)	(3,330)	(2,750)	(2,000)
Tax Paid	1,640	2,669	(1,680)	(4,966)	(7,144)
Cashflow From Operations	**20,110**	**18,030**	**23,680**	**19,720**	**26,043**
Capex	(3,340)	(1,970)	(4,150)	(3,000)	(3,000)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments			(20,000)		
Other Investing Cashflow	(1,150)				
Cash Flow From Investing	**15,620**	**16,060**	**(470)**	**16,720**	**23,043**
Debt Raised/(repaid)					
Proceeds From Issue Of Shares					
Shares Repurchased					
Dividends Paid	(3,610)	(6,770)	(8,630)	(7,446)	(5,077)
Preferred Dividends					
Other Financing Cashflow	(12,630)	(9,430)	10,470	(8,911)	(13,195)
Cash Flow From Financing	**(16,240)**	**(16,200)**	**1,840**	**(16,357)**	**(18,272)**
Total Cash Generated	(620)	(140)	1,370	363	4,771
Free Cashflow To Equity	**35,730**	**34,090**	**23,210**	**36,440**	**49,085**
Free Cashflow To Firm	**39,310**	**36,640**	**26,540**	**39,190**	**51,085**

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Cash And Equivalents	6,040	5,900	7,270	7,633	12,403
Total Debtors	15,230	16,330	19,440	21,494	23,664
Inventories	26,810	24,620	22,300	26,867	29,580
Total Other Current Assets	7,140	4,800	4,280	5,373	5,916
Total Current Assets	**55,220**	**51,650**	**53,290**	**61,367**	**71,564**
Fixed Assets	36,290	32,470	34,600	30,200	25,200
Total Investments		420	430	430	430
Intangible Assets	43,250	38,050	54,270	54,270	54,270
Total Other Non-Current Assets	5,990	8,410	7,530	7,530	7,530
Total Non-current Assets	**85,530**	**79,350**	**96,830**	**92,430**	**87,430**
Short-term Debt	7,040	19,100	28,010	28,010	28,010
Current Portion of Long-Term Debt					
Total Creditors	20,490	16,740	16,790	17,780	19,455
Other Current Liabilities	21,380	8,310	9,670	10,160	11,117
Total Current Liabilities	**48,910**	**44,150**	**54,470**	**55,950**	**58,582**
Total Long-term Debt	29,410	21,600	24,960	18,139	6,193
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	4,050	5,720	8,710	8,710	8,710
Total Non-current Liabilities	**33,460**	**27,320**	**33,670**	**26,849**	**14,903**
Total Provisions					
Total Liabilities	**82,370**	**71,470**	**88,140**	**82,799**	**73,485**
Shareholders Equity	58,380	59,530	61,980	70,998	85,509
Minority Interests					
Total Equity	**58,380**	**59,530**	**61,980**	**70,998**	**85,509**

Key Ratios

	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue Growth	0.8%	6.3%	13.1%	11.7%	10.1%
Operating EBITDA Growth	14.5%	(2.2%)	16.9%	16.2%	12.8%
Operating EBITDA Margin	31.0%	28.6%	29.5%	30.7%	31.5%
Net Cash Per Share (Rs)	(89.85)	(102.82)	(135.03)	(113.80)	(64.41)
BVPS (Rs)	172.49	175.89	183.13	209.78	252.65
Gross Interest Cover	5.10	6.94	6.41	9.31	14.62
Effective Tax Rate	18.0%	36.6%	32.6%	30.0%	30.0%
Net Dividend Payout Ratio					
Accounts Receivables Days	72.32	67.70	67.86	69.51	69.65
Inventory Days	410.48	384.20	313.09	298.19	318.04
Accounts Payables Days	348.25	278.12	223.74	209.66	209.79
ROIC (%)	14.7%	13.3%	13.8%	16.3%	18.9%
ROCE (%)	19.6%	18.1%	19.8%	22.1%	24.7%
Return On Average Assets	10.8%	10.7%	10.6%	12.2%	13.5%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

India

REDUCE *(previously ADD)*

Consensus ratings*:	Buy 24	Hold 8	Sell 4

Current price:	Rs562
Target price: ▼	Rs517
Previous target:	Rs593
Up/downside:	-8.0%
InCred Research / Consensus:	-6.2%
Reuters:	
Bloomberg:	ZYDUSLIF IN
Market cap:	US$6,931m
	Rs568,656m
Average daily turnover:	US$6.7m
	Rs548.7m
Current shares o/s:	1,012.2m
Free float:	25.0%

**Source: Bloomberg*

Source: Bloomberg

Price performance	*1M*	*3M*	*12M*
Absolute (%)	10.5	16.9	59.0
Relative (%)	9.7	7.0	34.2

Major shareholders	% held
Promoters	75.0
LIC	6.2
Kotak Mahindra MF	2.4

Zydus Lifesciences

Rising risks to core earnings

- We believe a large part of the rerating linked to its improving US outlook is now behind; at current valuation, the risk-reward ratio is unfavourable.
- While a strong US performance may continue for another quarter, we note that product concentration risk is rising – especially in the wake of looming competition in gAsacol HD (25-30% of EBITDA, as per our estimate).
- Resume coverage with a REDUCE rating (ADD earlier) and a TP of Rs517.

Recent outperformance linked to improving US outlook is factored in

India and the US combined make up for 83% of overall revenue and thus, Zydus Lifesciences' (Zydus) performance is largely linked to its performance in these geographies. Over the past six months, Zydus has significantly outperformed peers led by improving US pricing environment and a spike in approvals (63 in FY23) post clearance of its Moraiya plant. While a strong US growth may continue in 1QFY24F, we believe the risk-reward is unfavourable now, especially given the rising product concentration, with its top-2 products contributing 40% to EBITDA and looming competition in its largest product, gAsacol HD. Zydus has given guidance of a high single-digit growth in the US market in FY24F, which implies the quarterly run-rate moderating to US$250m/quarter (vs. US$274m in 4QFY23). It has a strong near-term launch calendar – with around 32 launches including gVascepa, two REMS products, three transdermal products and a few other high-value launches. Beyond FY24F, Zydus has a strong pipeline of oncology, injectables, vaccines and transdermal products, though we believe that these may not be enough to sustain the momentum on a concentrated US base. The new chemical entity business is still far off, with the earliest commercial opportunity likely only in FY26F.

India business should largely tread industry growth

Zydus' domestic formulations (DF) business underwent a restructuring a couple of years ago, with divestment of non-core brands and division of India business into three clusters viz. specialty business, chronic business and mass business to ensure better focus and distribution efficiency. The strategy has played off well and DF business is now broadly treading/outperforming industry growth. The wellness business has been mired by slower growth in discretionary spending and Zydus hopes to mitigate the impact via calibrated price hikes and a reduction in input prices. The recent WHO guidelines on non-sugar sweeteners - against their use to control body weight or reduce the risk of non-communicable diseases, we believe, can be a key risk for its Sugar-free product.

Valuation ignores high concentration risk

We believe the street is overtly focused on the near-term US momentum, ignoring the increasing concentration risk. Our calculations suggest that gAsacol/gRevlimid/gTrokendi together contributed nearly half of FY23 EBITDA; while gTrokendi has already seen incremental competition, gAsacol HD can witness competition in 2HFY24F. Resume coverage on Zydus with a REDUCE rating and a target price of Rs517, valuing the base business at 20x FY25F EPS and gRevlimid at 10x. Delay in competition in gAsacol HD is an upside risk.

Financial Summary	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue (Rsm)	151,022	152,652	175,218	193,294	203,862
Operating EBITDA (Rsm)	31,359	33,407	38,599	42,364	45,870
Net Profit (Rsm)	21,336	44,873	19,649	27,774	29,989
Core EPS (Rs)	21.1	23.4	24.0	27.4	29.6
Core EPS Growth	81.3%	10.9%	2.8%	14.2%	8.0%
FD Core P/E (x)	26.65	24.03	23.38	20.47	18.96
DPS (Rs)	3.5	6.0	6.0	7.0	7.0
Dividend Yield	0.62%	1.07%	1.07%	1.25%	1.25%
EV/EBITDA (x)	19.53	17.58	15.05	13.66	12.26
P/FCFE (x)	9.91	9.46	12.96	22.08	9.96
Net Gearing	18.7%	4.0%	(0.1%)	(1.3%)	(8.1%)
P/BV (x)	4.38	3.35	3.25	2.89	2.60
ROE	18.3%	15.8%	14.1%	14.9%	14.4%
% Change In Core EPS Estimates				(5.51%)	(13.86%)
InCred Research/Consensus EPS (x)					

SOURCE: INCRED RESEARCH, COMPANY REPORTS

Analyst(s)

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Kashish THAKUR
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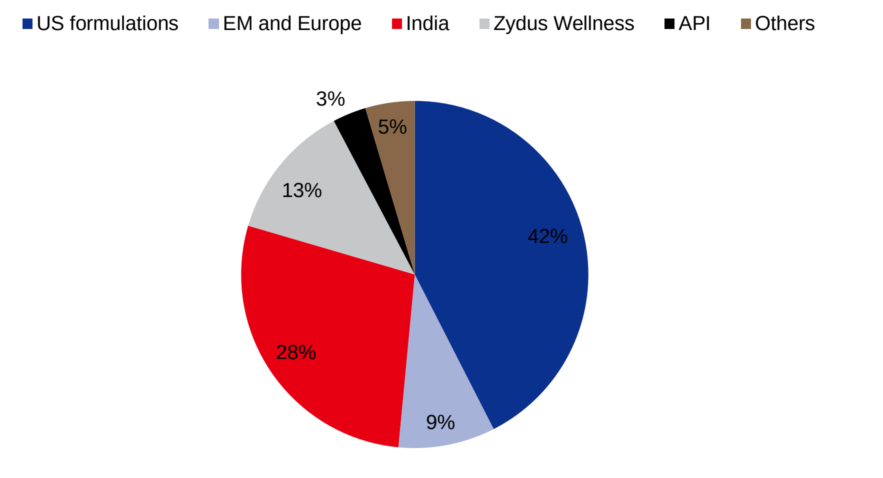
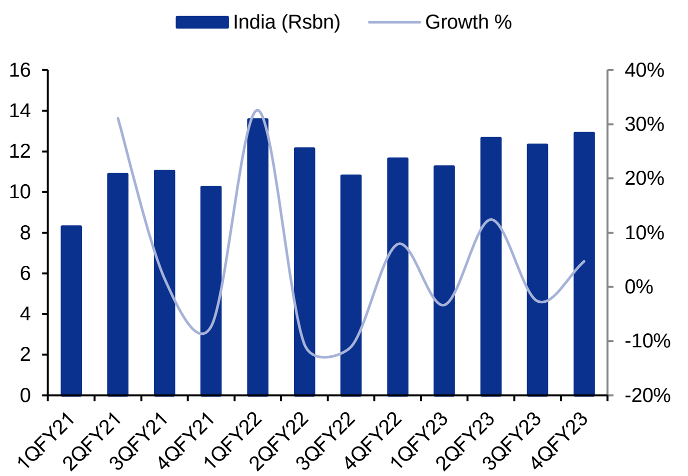
Figure 236: Geographic revenue break-up



SOURCE: INCRED RESEARCH, COMPANY REPORTS

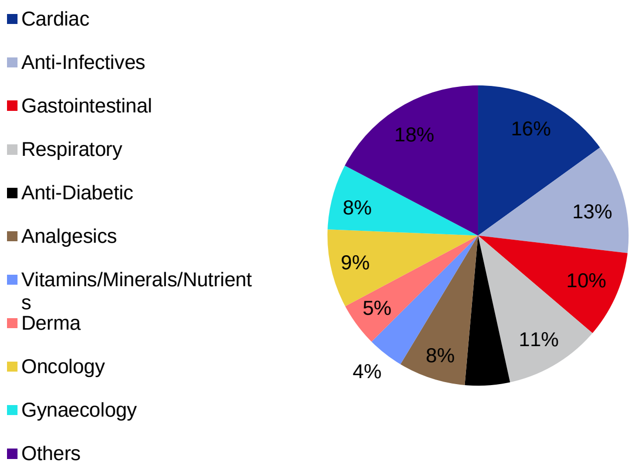
India business is back on track post restructuring

Figure 237: Domestic revenue – growth has picked up in last few quarters



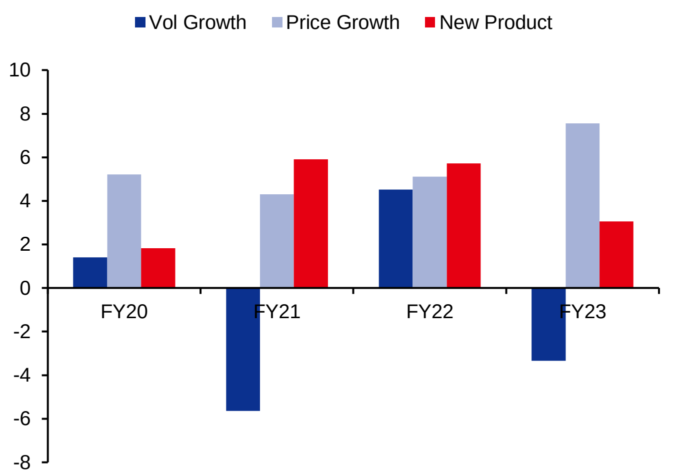
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 238: Therapy-wise revenue break-up



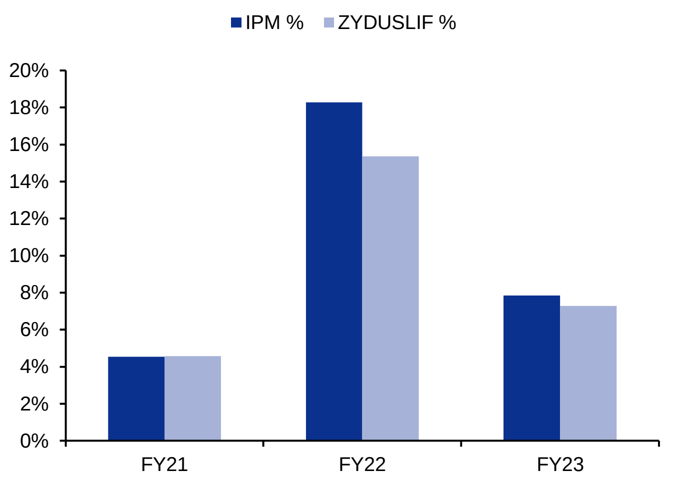
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 239: Price hikes, new launches have been consistent drivers of India growth



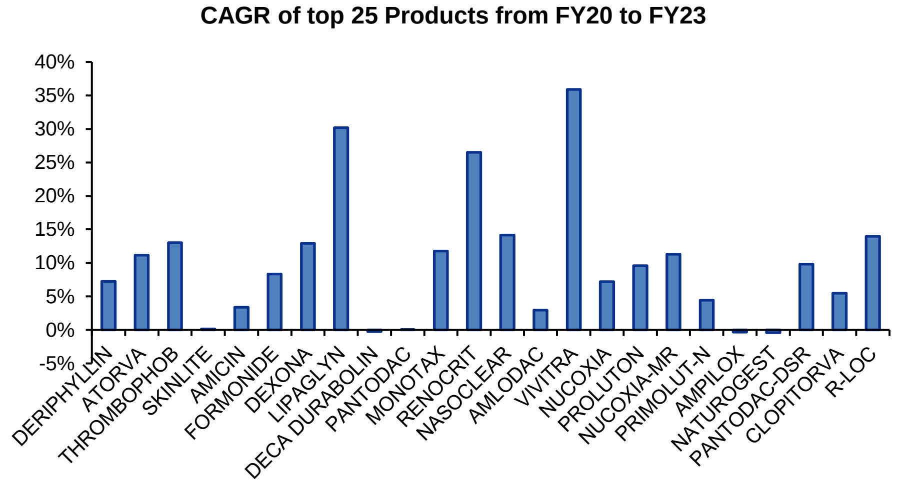
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 240: Zydus' India business has largely treaded IPM growth



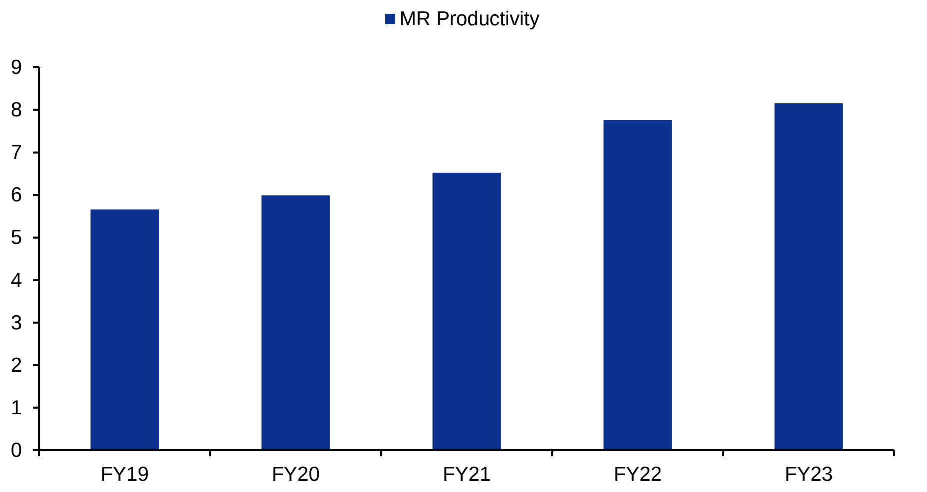
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 241: Top-25 product CAGRs from FY20 to FY23 – new launches like Lipaglyn have done extremely well



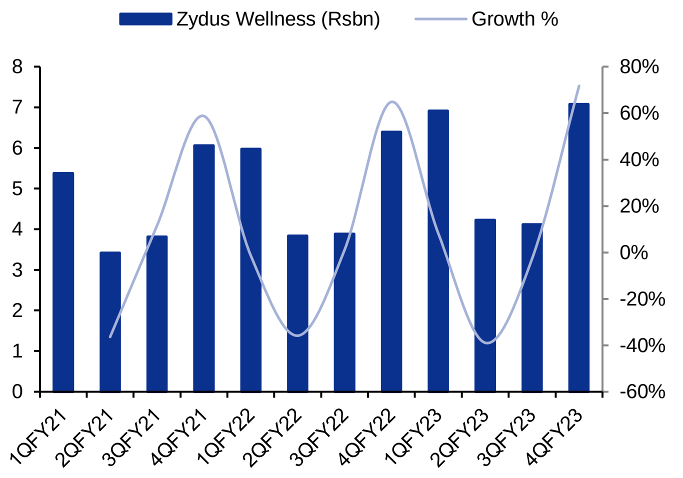
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 242: MR productivity continues to increase



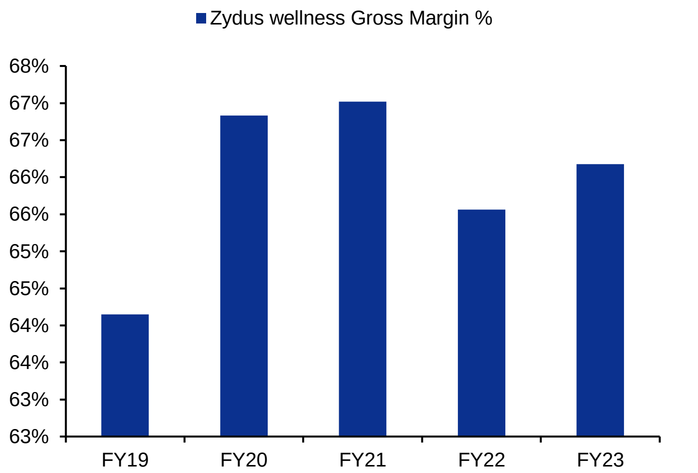
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 243: Zydus Wellness' has been rather struggling



SOURCE: INCRED RESEARCH, COMPANY REPORTS

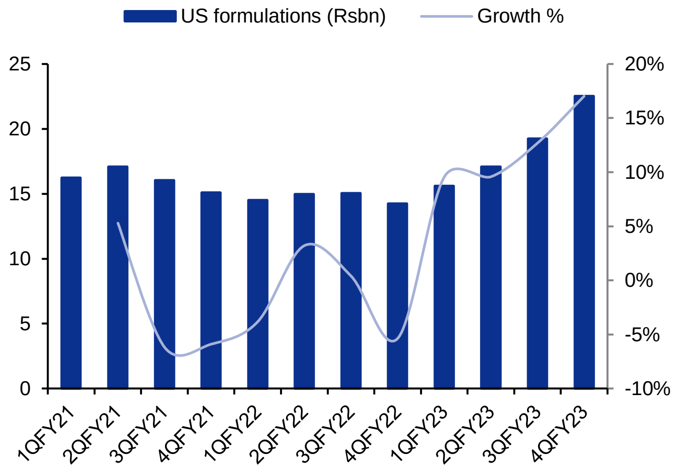
Figure 244: Gross margin in Zydus Wellness business has been volatile



SOURCE: INCRED RESEARCH, COMPANY REPORTS

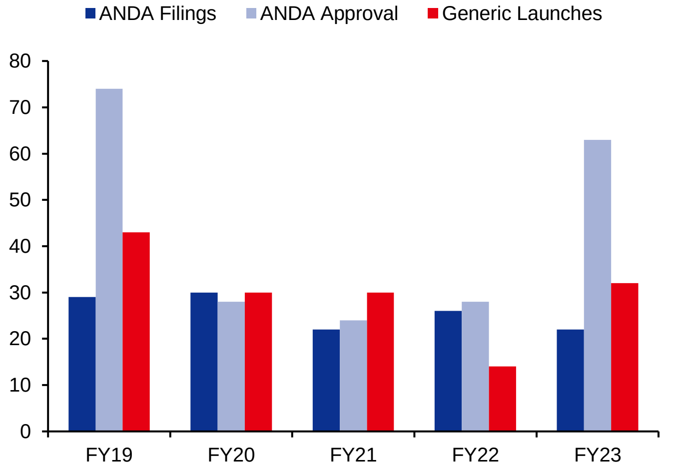
Steadily improving US business

Figure 245: US business has been steadily improving



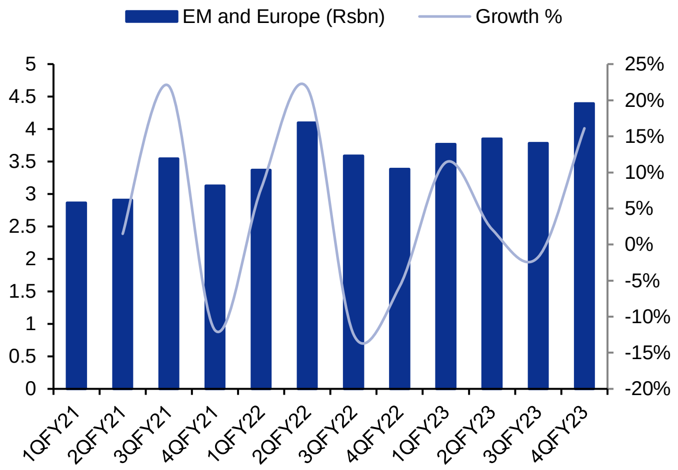
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 246: Historical ANDA filings and approvals – one of the highest approval rates in the industry



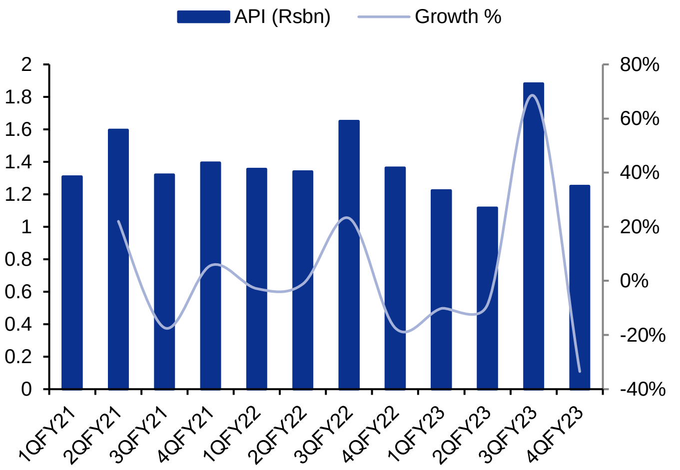
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 247: EM's and Europe – slow and steady



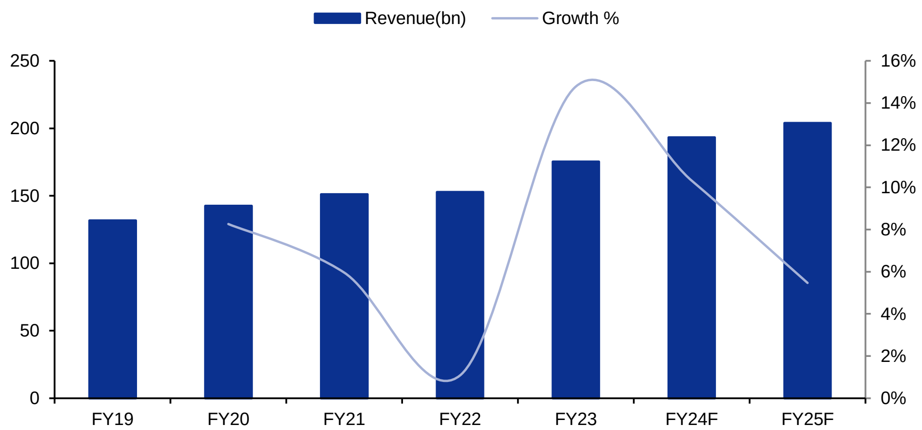
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 248: API business – largely used for captive consumption



SOURCE: INCRED RESEARCH, COMPANY REPORTS

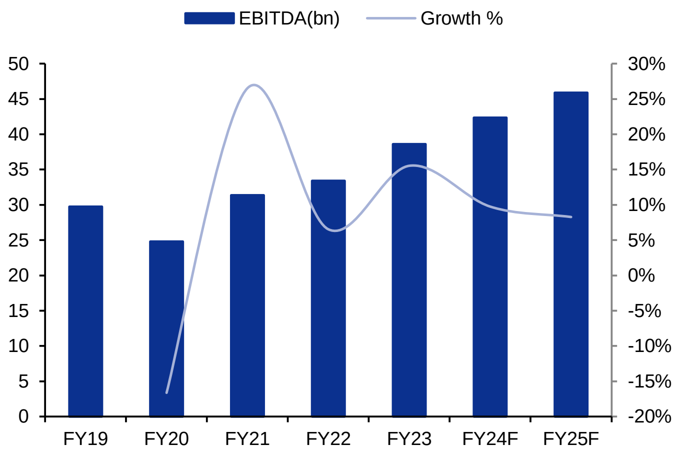
Figure 249: Revenue growth – steady India business and strong scale-up in the US business, but now concentration risks are rising



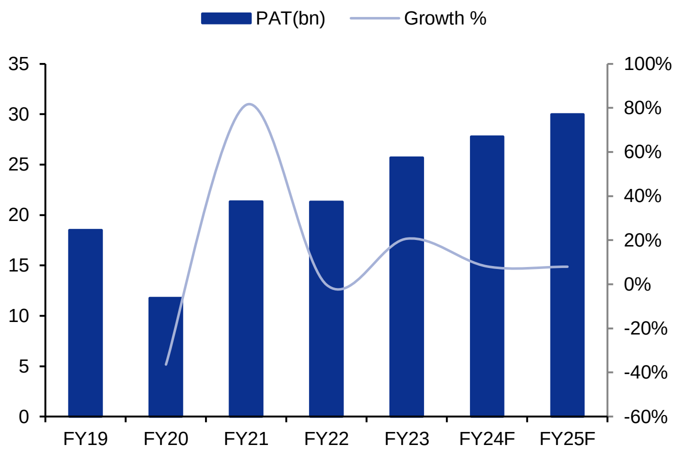
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 250: EBITDA – largely sustained in the 20-22% range

Figure 251: PAT – expect marginal growth in next two years

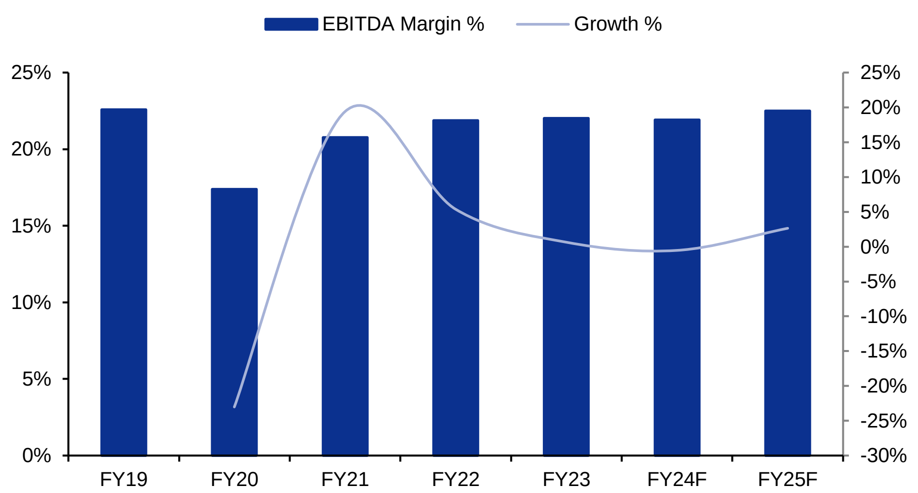


SOURCE: INCRED RESEARCH, COMPANY REPORTS



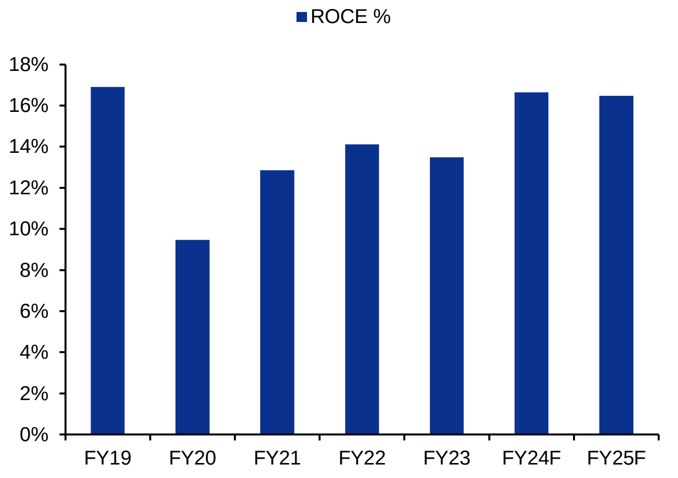
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 252: EBITDA margin – largely sustained in the 20-22% range



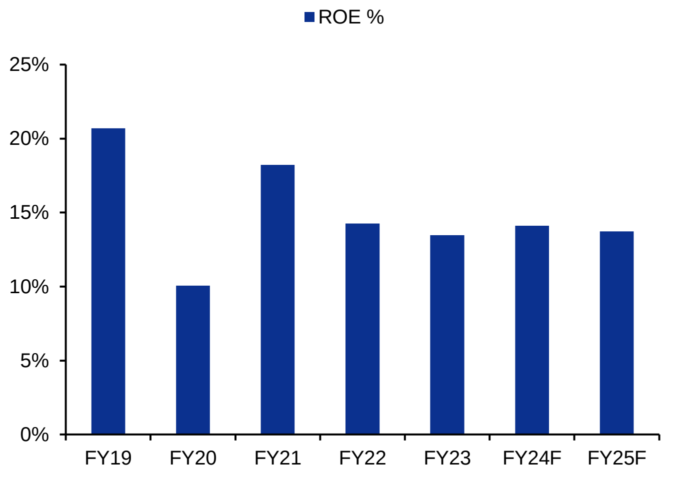
SOURCES: INCRED RESEARCH, COMPANY REPORTS

Figure 253: RoCE trend of Zydus Lifesciences



SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 254: RoE trend of Zydus Lifesciences

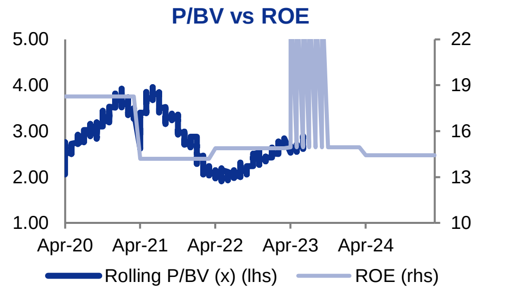


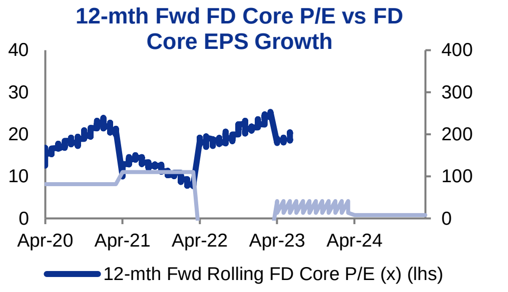
SOURCE: INCRED RESEARCH, COMPANY REPORTS

Figure 255: One-year forward P/E of Zydus Lifesciences

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS





Profit & Loss

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Net Revenues	**151,022**	**152,652**	**175,218**	**193,294**	**203,862**
Gross Profit	**98,921**	**97,200**	**112,117**	**124,724**	**134,560**
Operating EBITDA	**31,359**	**33,407**	**38,599**	**42,364**	**45,870**
Depreciation And Amortisation	(7,248)	(7,130)	(7,227)	(7,650)	(7,950)
Operating EBIT	**24,111**	**26,277**	**31,372**	**34,714**	**37,920**
Financial Income/(Expense)	(1,635)	(1,270)	(1,299)	(1,000)	(1,000)
Pretax Income/(Loss) from Assoc.					
Non-Operating Income/(Expense)	372	2,247	1,866	1,400	1,000
Profit Before Tax (pre-EI)	**22,848**	**27,254**	**31,939**	**35,114**	**37,920**
Exceptional Items		23,584	(6,042)		
Pre-tax Profit	**22,848**	**50,838**	**25,897**	**35,114**	**37,920**
Taxation	(1,472)	(5,117)	(5,878)	(7,023)	(7,584)
Exceptional Income - post-tax					
Profit After Tax	**21,376**	**45,721**	**20,019**	**28,091**	**30,336**
Minority Interests	(40)	(848)	(370)	(317)	(347)
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	**21,336**	**44,873**	**19,649**	**27,774**	**29,989**
Recurring Net Profit	21,336	23,663	24,320	27,774	29,989
Fully Diluted Recurring Net Profit	**21,336**	**23,663**	**24,320**	**27,774**	**29,989**

Cash Flow

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
EBITDA	31,359	33,407	38,599	42,364	45,870
Cash Flow from Invt. & Assoc.					
Change In Working Capital	1,911	(3,515)	(2,358)	(17,395)	(4,633)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	(331)	(8,851)	(9,353)	(7,340)	(7,931)
Net Interest (Paid)/Received	(1,635)	(1,270)	(1,299)	(1,000)	(1,000)
Tax Paid	932	(35,128)	(3,808)	(7,740)	(7,931)
Cashflow From Operations	**32,939**	**21,041**	**26,888**	**17,628**	**33,306**
Capex	(8,469)	(11,672)	(9,915)	(9,500)	(9,500)
Disposals Of FAs/subsidiaries					
Acq. Of Subsidiaries/investments		29,712			
Other Investing Cashflow					
Cash Flow From Investing	**24,470**	**39,081**	**16,973**	**8,128**	**23,806**
Debt Raised/(repaid)					
Proceeds From Issue Of Shares			(8,632)		
Shares Repurchased					
Dividends Paid	(15)	(3,722)	(2,671)	(6,073)	(7,085)
Preferred Dividends					
Other Financing Cashflow	(25,221)	(9,641)	(28,347)	400	
Cash Flow From Financing	**(25,236)**	**(13,363)**	**(39,650)**	**(5,673)**	**(7,085)**
Total Cash Generated	(766)	25,718	(22,677)	2,455	16,720
Free Cashflow To Equity	**57,409**	**60,122**	**43,861**	**25,757**	**57,112**
Free Cashflow To Firm	**59,044**	**61,392**	**45,160**	**26,757**	**58,112**

SOURCE: INCRED RESEARCH, COMPANY REPORTS

BY THE NUMBERS…cont'd

Balance Sheet

(Rs mn)	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Total Cash And Equivalents	8,883	34,601	11,924	14,379	31,099
Total Debtors	31,273	33,403	44,168	48,324	50,966
Inventories	32,362	37,194	34,133	38,659	40,772
Total Other Current Assets	14,642	15,754	9,939	19,329	20,386
Total Current Assets	**87,160**	**120,952**	**100,164**	**120,691**	**143,224**
Fixed Assets	63,332	64,226	68,267	70,117	71,667
Total Investments	3,570	9,348	9,273	9,273	9,273
Intangible Assets	53,465	64,918	58,949	58,949	58,949
Total Other Non-Current Assets	31,320	18,510	20,911	20,911	20,911
Total Non-current Assets	**151,687**	**157,002**	**157,400**	**159,250**	**160,800**
Short-term Debt	30,709	38,427	11,632	11,632	11,632
Current Portion of Long-Term Debt					
Total Creditors	22,059	21,378	21,250	21,120	21,681
Other Current Liabilities	25,845	18,589	22,425	23,232	23,849
Total Current Liabilities	**78,613**	**78,394**	**55,307**	**55,984**	**57,162**
Total Long-term Debt	6,095	3,782			
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	4,843	5,240	5,374	5,374	5,374
Total Non-current Liabilities	**10,938**	**9,022**	**5,374**	**5,374**	**5,374**
Total Provisions					
Total Liabilities	**89,551**	**87,416**	**60,681**	**61,358**	**62,536**
Shareholders Equity	129,923	169,996	175,158	196,542	219,098
Minority Interests	19,373	20,542	21,725	22,042	22,389
Total Equity	**149,296**	**190,538**	**196,883**	**218,584**	**241,487**

Key Ratios

	Mar-21A	Mar-22A	Mar-23A	Mar-24F	Mar-25F
Revenue Growth	6.0%	1.1%	14.8%	10.3%	5.5%
Operating EBITDA Growth	26.5%	6.5%	15.5%	9.8%	8.3%
Operating EBITDA Margin	20.8%	21.9%	22.0%	21.9%	22.5%
Net Cash Per Share (Rs)	(27.58)	(7.52)	0.29	2.71	19.23
BVPS (Rs)	128.36	167.95	173.05	194.17	216.46
Gross Interest Cover	14.75	20.69	24.15	34.71	37.92
Effective Tax Rate	6.4%	10.1%	22.7%	20.0%	20.0%
Net Dividend Payout Ratio					
Accounts Receivables Days	82.06	77.32	80.79	87.33	88.88
Inventory Days	211.05	228.92	206.29	193.73	209.17
Accounts Payables Days	148.41	142.96	123.29	112.77	112.71
ROIC (%)	10.1%	10.1%	12.2%	12.3%	13.0%
ROCE (%)	12.9%	12.5%	14.2%	15.8%	15.7%
Return On Average Assets	9.5%	8.9%	10.1%	10.7%	10.6%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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