

India

**Neutral** (no change)**Highlighted Companies****Ajanta Pharma Ltd**

ADD, TP Rs2800, Rs2995 close

A play on branded generics.

**Aurobindo Pharma**

ADD, TP Rs1610, Rs1503 close

Top-notch generics player.

**Zydus Lifesciences**

ADD, TP Rs1434, Rs1188 close

A play on the US generics market.

**Summary Valuation Metrics**

P/E (x)	Mar24-A	Mar25-F	Mar26-F
Ajanta Pharma Ltd	47.01	38.6	32.86
Aurobindo Pharma	27.76	21.99	17.91
Zydus Lifesciences	31.33	25.76	23.32

P/BV (x)	Mar24-A	Mar25-F	Mar26-F
Ajanta Pharma Ltd	10.76	10.59	9.26
Aurobindo Pharma	2.95	2.63	2.32
Zydus Lifesciences	6.06	5.06	4.26

Dividend Yield	Mar24-A	Mar25-F	Mar26-F
Ajanta Pharma Ltd	1.7%	1.67%	1.67%
Aurobindo Pharma	0.4%	0.47%	0.53%
Zydus Lifesciences	0.59%	0.59%	0.59%

# Pharmaceuticals

## 1QFY25 results review

- 1QFY25 results/outlook were overall strong. Downgrades on Torrent Pharma (to HOLD) and Ipca Labs (to REDUCE) were more on the risk-reward ratio.
- Strong US business, and steady India & margin tailwinds should continue to drive the outperformance. The CDMO segment could be a dark horse.
- ADD ratings: Ajanta Pharma, Aurobindo Pharma, Divi's Labs, Lupin, and Zydus Lifesciences. REDUCE ratings: Gland Pharma, Laurus Labs, and Ipca Labs.

### Strong start to FY25

The 1QFY25 earnings report card was in line-to-better for our coverage universe, with only two misses and two downgrades. Our coverage companies' revenue grew by 11.7% YoY and 5% QoQ while the margins expanded by 240bp sequentially and YoY. Except for Gland Pharma and Laurus Laboratories (both REDUCE-rated), the performance of our coverage companies was in line or above our estimates. Our broader thesis on the coverage universe remains intact, with the US business largely holding up its strong momentum, reduced raw material prices leading to improved gross margin & sustenance of operating margin, and the domestic business recovery on the cards in FY25F.

### New launches & stable price erosion in US sustains positive outlook

During 1QFY25, our coverage universe's US revenue grew by 12.6% YoY (7.6% QoQ) led by new launches, stable price erosion as well as gRevlimid sales. While gMirabegron was a significant product launch in 1Q, benefitting Lupin and Zydus Lifesciences big time, the other US generics-driven companies witnessed gRevlimid-driven growth. We understand that gMirabegron may not see a typical generic competition post 180-day marketing exclusivity while gRevlimid should contribute higher than what it did in FY24. The price erosion during 1Q was in mid-high single digits and is believed to remain stable for the next three-to-four quarters due to continuance of drug shortage. Our coverage companies have given guidance of a high single-digit to double-digit growth in the US market for FY25F.

### Lower input costs – key lever for margin improvement

During 1QFY25, our coverage universe's gross margin and EBITDA margin witnessed healthy improvement (on an average 100bp YoY /50bp QoQ growth in gross margin and 100bp YoY/QoQ rise in the EBITDA margin), mostly led by benign raw material prices. Going ahead, raw material prices are expected to remain stable at the current levels which, we believe, should keep the gross and EBITDA margins buoyant at the current levels.

### Hits and misses

Post 1QFY25, we have two downgrades - Ipca Laboratories' rating to REDUCE (from ADD) and Torrent Pharma's rating to HOLD (from ADD) - due to adverse risk-reward ratios and valuations (Ipca Laboratories trading at +2SD). Enthused by the strong earnings as well as positive outlook, we continue to maintain our high-conviction ADD rating on Ajanta Pharma, Aurobindo Pharma, and Zydus Lifesciences. In the CDMO space, while we are optimistic on Divi's Laboratories due to a pick-up in the custom synthesis or CS business and order inflow due to the ongoing speculation regarding the Biosecure Act, we maintain our negative stance on Laurus Laboratories and Gland Pharma due to earnings miss & soft management commentary. We maintain our HOLD rating on Cipla, Dr. Reddy's Laboratories and Sun Pharmaceutical Industries due to the delay in key launches/lack of product visibility /moderate earnings, respectively. Conversely, we continue our ADD rating on Lupin on account of its strong US market growth backed by new launches & margin expansion.

### Sector outlook

We remain broadly optimistic on the sector and expect the outperformance to largely continue, with the momentum sustaining in India/US markets as well as on the margins front. We prefer stocks having earnings momentum likely staying strong in the medium term. We remain bullish on Aurobindo Pharma, Ajanta Pharma, Lupin and Zydus Lifesciences, while Divi's Laboratories can be a dark horse with optionality from the Biosecure Act.

**Research Analyst(s)****Praful BOHRA**

T (91) 22 4161 1552

E praful.bohra@incredresearch.com

**Yogesh SONI**

T (91) 8850099267

E yogesh.soni@incredresearch.com

**Figure 1: Management commentary indicates sustenance of the current favourable pricing dynamics for next few quarters**

Company	Speaker	Comments
Ajanta Pharma	Mr Yogesh Agrawal - MD	"Price erosion is stable. It remains to be in high-single digits. There are no aggressive price erosions or any kind of things up there. So, for now, I think the market seems to have stabilized quite well."
Alkem Labs	Mr Vikas Gupta - CEO	"The US generics are seeing a single-digit price erosion, and the trend continues even for this quarter. So, we are seeing that kind of price erosion in our US businesses."
Aurobindo Pharma	Mr Yugandhar Puvvala - CEO Eugia Pharma	"The price erosion is in low single digits."
Cipla	Mr Ashish Adukia - Global CFO	"Going forward, I don't... we don't think that it will be touching double digit."
Ipca Labs	Mr Ajit Kumar Jain - MD & CEO	"Erosions are now very limited. Price erosion was there, but now it's very, very limited. Now it's not maybe 2%, 3% here and there, but price erosion trend has stopped now."
Lupin	Ms Vinita Gupta - CEO	"It's (sic. base price erosion) a mid-single digit price erosion."
Torrent Pharma	Mr Sanjay Gupta - Executive Director	"So (sic. price erosion), similar to previous quarters, I would say mid-single digit type of price erosion continues and now we are able to compensate for it by increased market share and some small launches here and there."

SOURCE: INCRED RESEARCH, COMPANY REPORTS

**Figure 2: Benign raw material costs led to an improvement in gross margin, and they are likely to continue in medium term**

Company	Speaker	Comments
Aurobindo Pharma	Mr. S. Subramanian - CFO	"The raw material costs continued to be at benign levels and are in line with the previous quarter, supporting our gross margins."
Alkem Labs	Mr Vikas Gupta - CEO	"We are committed to maximizing our EBITDA margin by carefully managing our product mix, controlling costs and taking advantage of the favourable raw material pricing environment." "So I see the API pricing remaining more or less stable now. So, I'm not foreseeing any significant change in the API environment."
Ipca Labs	Mr Ajit Kumar Jain - MD & CEO	"And I would say that input costs are also not moving up to that extent. There is a marginal improvement here and there in solvents and others, but by and large margin... your material costs are also very stable."

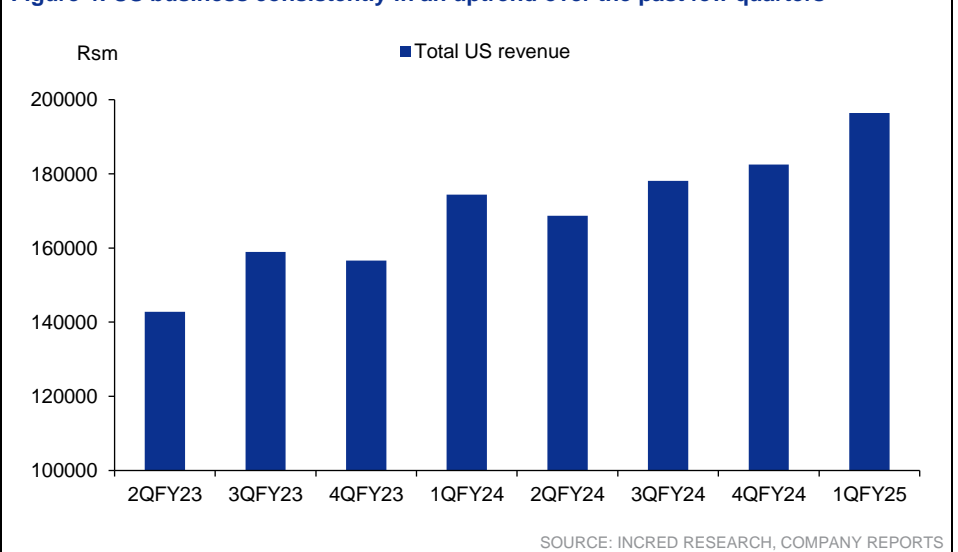
SOURCE: INCRED RESEARCH, COMPANY REPORTS

**Figure 3: Gross margin and EBITDA margin improvement due to lower input costs**

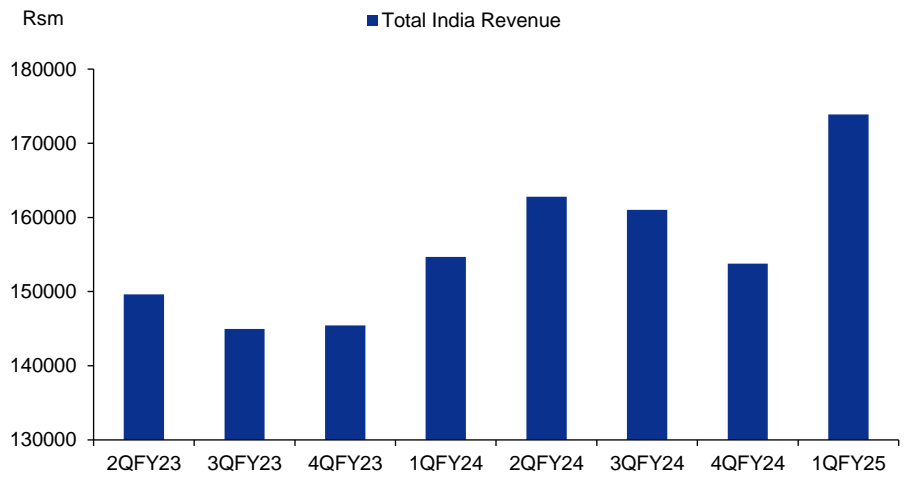
	Gross Margin	Changes		EBITDA Margin	Changes	
		YoY (bp)	QoQ (bp)		YoY (bp)	QoQ (bp)
Ajanta Pharma	76.6%	128	169	28.9%	228	245
Alkem Labs	64.5%	490	223	20.1%	696	638
Cipla	67.2%	258	50	25.6%	203	428
Divi's Labs	59.7%	-158	-111	29.4%	102	-237
Dr. Reddy's Labs	60.4%	170	183	27.7%	-262	228
Gland Pharma	59.7%	-278	-127	18.9%	-546	-447
Laurus Labs	55.1%	448	522	14.3%	22	-245
Lupin	68.8%	445	57	24.3%	1018	422
Torrent Pharma	75.7%	81	46	31.6%	109	-55
Ipca Labs	69.2%	171	299	18.8%	-61	293
Aurobindo Pharma	59.4%	544	-23	21.4%	460	-85
Zydus Lifesciences	74.4%	720	357	33.6%	413	411
Sun Pharmaceutical Industries	78.9%	195	-128	28.9%	103	311

SOURCE: INCRED RESEARCH, COMPANY REPORTS

**Figure 4: US business consistently in an uptrend over the past few quarters**

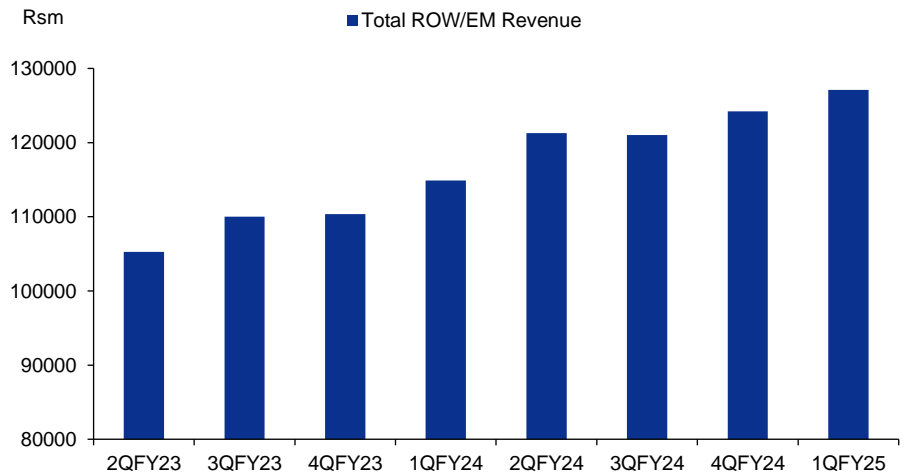


**Figure 5: India business posts strong performance after a seasonally weak 4Q**



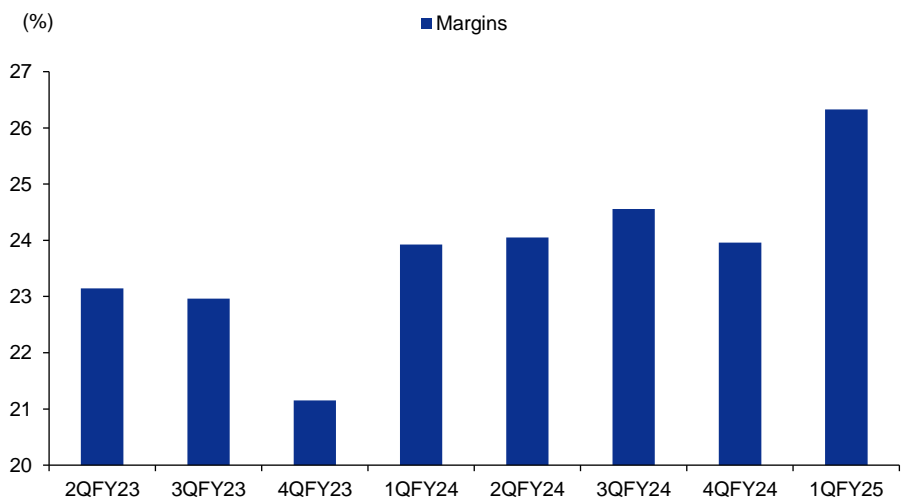
SOURCE: INCRED RESEARCH, COMPANY REPORTS

**Figure 6: Consistent sharp upturn in the ex-US international market in the past four quarters**
















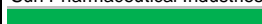


SOURCE: INCRED RESEARCH, COMPANY REPORTS

**Figure 7: Lower input costs give a significant boost to margins in 1QFY25**



SOURCE: INCRED RESEARCH, COMPANY REPORTS

**Figure 8: Rating changes post 1QFY25 results**

	Current Rating	Previous rating	Earnings	Commentary
Ajanta Pharma	ADD	ADD		
Alkem Labs	HOLD	HOLD		
Cipla	HOLD	HOLD		
Dr. Reddy's Labs	HOLD	HOLD		
Divi's Labs	ADD	ADD		
Gland Pharma	REDUCE	REDUCE		
Laurus Labs	REDUCE	REDUCE		
Lupin	ADD	ADD		
Torrent Pharma	HOLD	ADD		
Ipca Labs	REDUCE	ADD		
Aurobindo Pharma	ADD	ADD		
Zydus Lifesciences	ADD	ADD		
Sun Pharmaceutical Industries	HOLD	HOLD		
	Positive			
	Neutral			
	Weak			

SOURCE: INCRED RESEARCH, COMPANY REPORTS

**Figure 9: Earnings revision summary post 1QFY25 results**

	FY25F	FY26F
Ajanta Pharma	4.6%	8.1%
Alkem Labs	5.2%	3.4%
Cipla	3.9%	2.3%
Divi's Labs	-	-
Dr. Reddy's Labs	2.9%	0.8%
Gland Pharma	-	7.0%
Laurus Labs	-33.1%	-15.6%
Lupin	11.4%	15.0%
Torrent Pharma	-1.4%	-0.3%
Ipca Labs	-2.0%	1.0%
Aurobindo Pharma	-	-
Zydus Lifesciences	4.0%	9.0%
Sun Pharmaceutical Industries	-	-1.0%

SOURCE: INCRED RESEARCH, COMPANY REPORTS

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Hold	The stock's total return is expected to be between 0% and positive 10% over the next 12 months.
Reduce	The stock's total return is expected to fall below 0% or more over the next 12 months.
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Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.
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Underweight	An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.