

# Divi's Laboratories

Estimate change	↑
TP change	↑
Rating change	↔

**CMP: INR3,507**      **TP: INR3,330 (-5%)**      **Neutral**

## Pricing pressure in API segment hurts profitability

### CS segment sales to pick up pace in the coming quarters

- Divi's Lab (DIVI) delivered a miss on 2QFY24 earnings. While revenue was in line with estimates, profitability was lower than expectation, partly due to lower pricing in the generic API segment.
- We reduce our earnings estimate by 5%/3% for FY24/FY25, factoring in a) increased competition in the API segment, and b) higher tax rate, partly offset by improved growth momentum in the Nutraceutical business. We value DIVI at 35x 12M forward earnings to arrive at a price target of INR3,330.
- We are building 25% earnings CAGR over FY23-25 (adjusting for COVID-led business in FY23). This is on the back of improved visibility for contracts in the custom synthesis segment as well as ramp-up in products in contrast media space. We believe the current valuation adequately factors the upside in earnings. We reiterate our Neutral stance on the stock.

### Product mix/reduced operating leverage lowered margin YoY

- DIVI's revenues grew 2.2% YoY to INR19.1b (our est: INR19.3b) for the quarter.
- Adjusting for COVID-related inventory write-off (INR200m), gross margin contracted 500bp YoY to 58.6% due to a change in product mix.
- EBITDA margin contracted at a higher rate by 740bp YoY to 26.1% (our est: 29.2%), largely due to lower GM and higher employee cost/other expenses (up 140bp/90bp as a % of sales).
- As a result, EBITDA was down 19.7% YoY to INR4.9b (our est: INR5.6b) for the quarter.
- Tax rate was 25.8% in 2QFY24 as compared to 27.5%/19.8% for 1QFY24/2QFY23.
- Adjusted for INR90m in Extra-ordinary expense, PAT was down 24.4% YoY to INR3.5b (our est: INR4.3b).
- During 1HFY24, Revenue/EBITDA/PAT declined 10%/32%/37% YoY to INR37b/INR10b/INR7b.

### Highlights from the management commentary

- On Ex-COVID basis, the YoY sales growth was at a healthy double digit for the quarter.
- The generics: CS ratio was 60:40 for the quarter. This implies 5% YoY growth in the generics segment for the quarter.
- While volume growth was robust in the generics segment, the pricing pressure negatively impacted YoY sales growth of this segment.
- The nutraceutical sales were INR2b during the quarter, up 11% YoY.
- The commercial benefits from the two major CS projects are anticipated to materialize starting 2HFY24 onwards.

Bloomberg	DIVI IN
Equity Shares (m)	265
M.Cap.(INRb)/(USD\$)	930.9 / 11.2
52-Week Range (INR)	3949 / 2730
1, 6, 12 Rel. Per (%)	-5/-1/-14
12M Avg Val (INR M)	1760

### Financials & Valuations (INR b)

Y/E MARCH	FY23	FY24E	FY25E
Sales	77.7	80.5	93.7
EBITDA	23.7	22.9	28.8
Adj. PAT	17.2	16.7	22.2
EBIT Margin (%)	26.1	23.7	26.7
Cons. Adj. EPS (INR)	64.9	63.0	83.7
EPS Gr. (%)	-41.2	-2.9	33.0
BV/Sh. (INR)	481.0	524.2	582.0

### Ratios

Net D:E	-0.3	-0.3	-0.3
RoE (%)	14.1	12.5	15.1
RoCE (%)	14.1	12.5	15.1
Payout (%)	29.8	31.1	31.0

### Valuations

P/E (x)	54.0	55.7	41.9
EV/EBITDA (x)	37.5	38.7	30.7
Div. Yield (%)	0.5	0.5	0.6
FCF Yield (%)	1.7	0.6	0.4
EV/Sales (x)	11.4	11.0	9.4

### Shareholding pattern (%)

As On	Sep-23	Jun-23	Sep-22
Promoter	51.9	51.9	51.9
DII	21.8	21.2	20.8
FII	14.6	14.7	15.4
Others	11.7	12.1	11.9

FII Includes depository receipts

## Quarterly Performance

(INRm)

Y/E March	FY23				FY24E				FY23	FY24E	FY24E	Var. (%)
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE				
<b>Net Sales</b>	<b>22,545</b>	<b>18,545</b>	<b>17,077</b>	<b>19,508</b>	<b>17,780</b>	<b>19,090</b>	<b>20,645</b>	<b>22,959</b>	<b>77,675</b>	<b>80,474</b>	<b>19,342</b>	<b>-1.3</b>
YoY Change (%)	15.0	-6.7	-31.5	-22.5	-21.1	2.9	20.9	17.7	-13.3	3.6	4.3	
Total Expenditure	14,078	12,335	12,994	14,590	12,740	14,100	14,906	15,874	53,997	57,619	13,694	
<b>EBITDA</b>	<b>8,467</b>	<b>6,210</b>	<b>4,083</b>	<b>4,918</b>	<b>5,040</b>	<b>4,990</b>	<b>5,739</b>	<b>7,085</b>	<b>23,678</b>	<b>22,855</b>	<b>5,648</b>	<b>-11.6</b>
YoY Change (%)	-0.6	-24.7	-62.9	-55.5	-40.5	-19.7	40.6	44.1	-39.0	-3.5	-9.1	
Margins (%)	37.6	33.5	23.9	25.2	28.3	26.1	27.8	30.9	30.5	28.4	29.2	
Depreciation	837	857	868	870	930	950	960	980	3,432	3,820	878	
<b>EBIT</b>	<b>7,630</b>	<b>5,353</b>	<b>3,215</b>	<b>4,048</b>	<b>4,110</b>	<b>4,040</b>	<b>4,779</b>	<b>6,105</b>	<b>20,246</b>	<b>19,035</b>	<b>4,770</b>	<b>-15.3</b>
YoY Change (%)	-2.0	-28.4	-68.5	-60.4	-46.1	-24.5	48.7	50.8	-43.3	-6.0	-10.9	
Interest	0	0	1	2	0	10	5	5	7	20	0	
Other Income	320	492	674	662	810	750	710	708	2,150	2,978	670	
<b>PBT before EO Income</b>	<b>7,950</b>	<b>5,845</b>	<b>3,888</b>	<b>4,707</b>	<b>4,920</b>	<b>4,780</b>	<b>5,484</b>	<b>6,808</b>	<b>22,390</b>	<b>21,992</b>	<b>5,440</b>	
Forex gain /(Loss)	564	308	467	-42	30	-90	0	0	1,297	-60	0	
<b>PBT</b>	<b>8,514</b>	<b>6,153</b>	<b>4,354</b>	<b>4,665</b>	<b>4,950</b>	<b>4,690</b>	<b>5,484</b>	<b>6,808</b>	<b>23,687</b>	<b>21,932</b>	<b>5,440</b>	<b>-13.8</b>
Tax	1,493	1,216	1,288	1,455	1,360	1,210	1,261	1,432	5,453	5,264	1,142	
Rate (%)	17.5	19.8	29.6	31.2	27.5	25.8	23.0	21.0	23.0	24.0	21.0	
<b>PAT</b>	<b>7,021</b>	<b>4,937</b>	<b>3,066</b>	<b>3,210</b>	<b>3,590</b>	<b>3,480</b>	<b>4,223</b>	<b>5,376</b>	<b>18,234</b>	<b>16,669</b>	<b>4,298</b>	<b>-19.0</b>
<b>Adj. PAT</b>	<b>6,556</b>	<b>4,690</b>	<b>2,738</b>	<b>3,239</b>	<b>3,568</b>	<b>3,547</b>	<b>4,223</b>	<b>5,376</b>	<b>17,222</b>	<b>16,714</b>	<b>4,298</b>	<b>-17.5</b>
YoY Change (%)	2.6	-23.9	-67.2	-61.5	-45.6	-24.4	54.2	66.0	-41.2	-3.0	-8.4	
Margins (%)	31.1	26.6	18.0	16.5	20.2	18.2	20.5	23.4	23.5	20.7	22.2	
<b>Adj. EPS</b>	<b>24.7</b>	<b>17.7</b>	<b>10.3</b>	<b>12.2</b>	<b>13.4</b>	<b>13.4</b>	<b>15.9</b>	<b>20.3</b>	<b>64.9</b>	<b>63.0</b>	<b>16.2</b>	

## Quarterly Performance

Y/E March	FY23				FY24E				FY23	FY24E	FY24E
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE			
<b>Cost Break-up</b>											
RM Cost (% of Sales)	36.0	36.4	43.3	42.4	38.7	41.4	40.5	39.4	39.3	40.0	38.6
Staff Cost (% of Sales)	10.9	12.5	14.0	13.2	14.8	13.9	13.4	12.2	12.6	13.5	13.8
Other Expenses(% of Sales)	15.5	17.6	18.8	19.2	18.2	18.5	18.3	17.5	17.6	18.1	18.4
Tax rate (%)	17.5	19.8	29.6	31.2	27.5	25.8	23.0	22.7	23.0	24.0	21.0
Gross Margins(%)	64.0	63.6	56.7	57.6	61.3	58.6	59.5	60.6	60.7	60.0	61.4
EBITDA Margins(%)	37.6	33.5	23.9	25.2	28.3	26.1	27.8	30.9	30.5	28.4	29.2
EBIT Margins(%)	33.8	28.9	18.8	20.7	23.1	21.2	23.1	26.6	26.1	23.7	25.0



## Key takeaways from the management commentary

- The capex at Unit 3 is progressing well and the production is expected to commence from 1QFY25. This would also increase operational cost for DIVI.
- DIVI had 87% of the business from exports. US/EU contributed 68% of exports.
- Overall CWIP FY24 till date was INR4b.
- It has a cash of INR36b at the end of 2QFY24.

## Improved visibility of new contracts/new molecules to drive profitability

### New compounds/contracts to drive CS business

- In 1HFY24, CS sales declined 23% YoY to INR14.7b. This decline was due to reduced number of molnupiravir-related contracts.
- Having said this, DIVI is expanding its sartan portfolio by leveraging backward integration and innovative technology.
- While DIVI has commercialized Iodine-based contrast media products, it is also actively developing gadolinium-based contrast media products, thereby enhancing its overall portfolio offerings.
- Given the complex nature of products (contrast media) and limited customers, DIVI is suitably placed, given its capabilities as well as capacities.
- Further, DIVI would also be executing other contracts in CS segments.
- However, considering the high COVID base of FY23, we expect CS sales to see a 6% CAGR to INR38.4b over FY23-25.

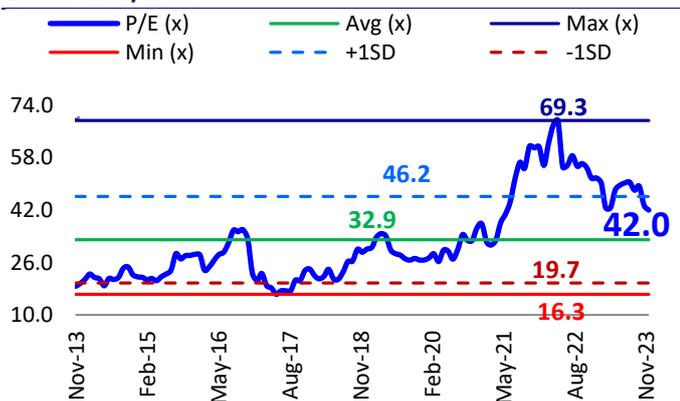
### Generics: New molecules/market share gain to fuel growth

- In 1HFY24, the generic API segment declined 3% YoY to INR18b. The pricing pressure continues to offset increased volume off-take of key products in this segment.
- In addition to backward integration for its existing products, DIVI is also building a portfolio that includes products with upcoming patent expirations within the next 2-3 years.
- Accordingly, we expect DIVI to post a 11.6% revenue CAGR to INR46.7b over FY23-25.

### Reiterate Neutral

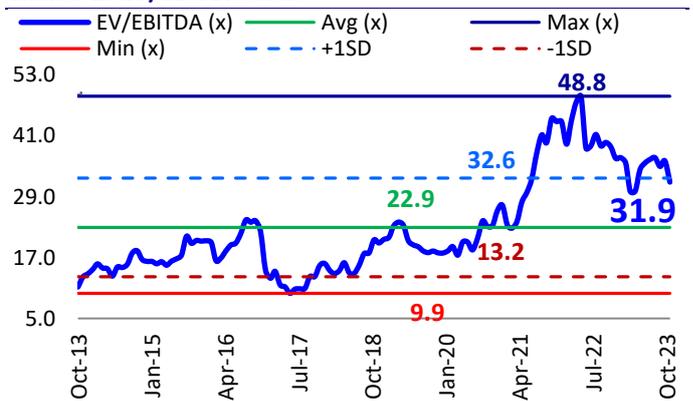
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Exhibit 1: P/E chart



Source: MOFSL, Company, Bloomberg

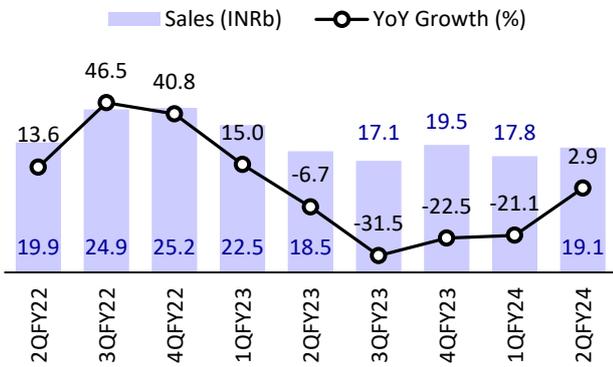
Exhibit 2: EV/EBITDA chart



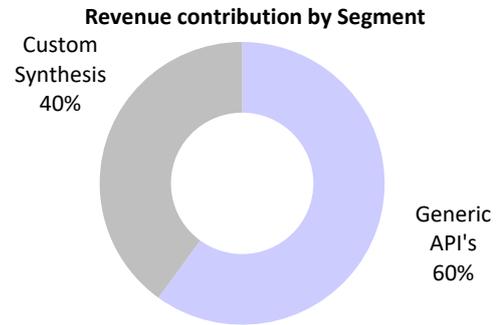
Source: MOFSL, Company, Bloomberg

## Story in charts

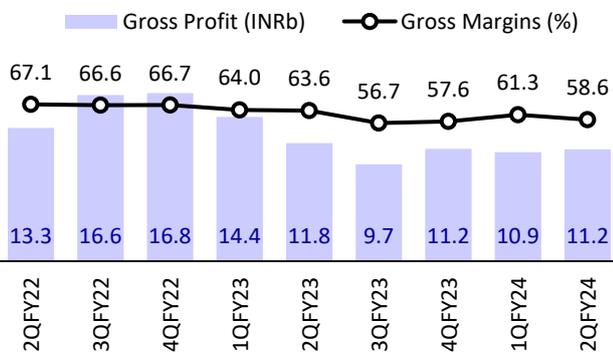
**Exhibit 3: Revenue growth declined 2.9% YoY in 2QFY24**



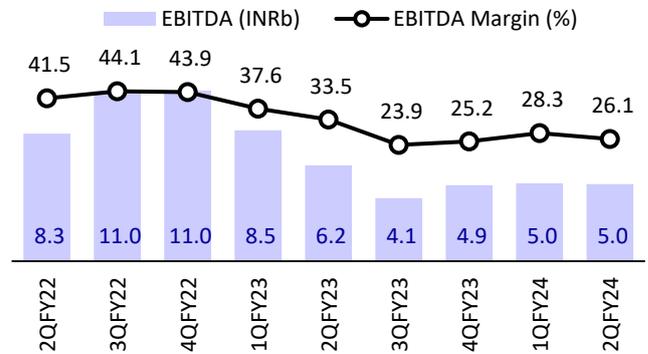
**Exhibit 4: Generic APIs segment contributes 60% to revenue in 2QFY24**



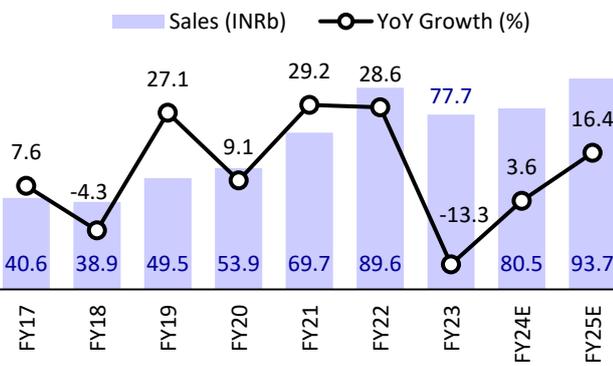
**Exhibit 5: Gross margin down 500bp YoY in 2QFY24**



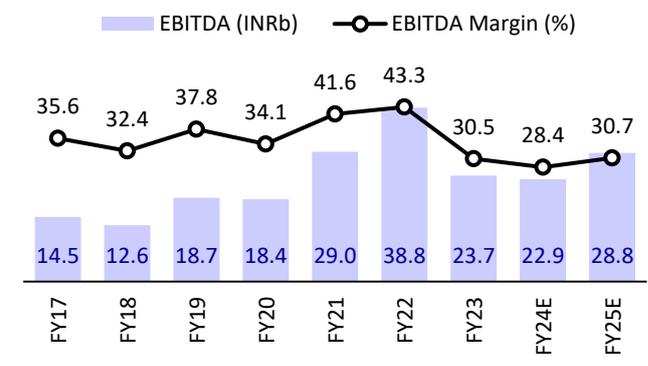
**Exhibit 6: EBITDA margin contracts 740bp YoY in 2QFY24**



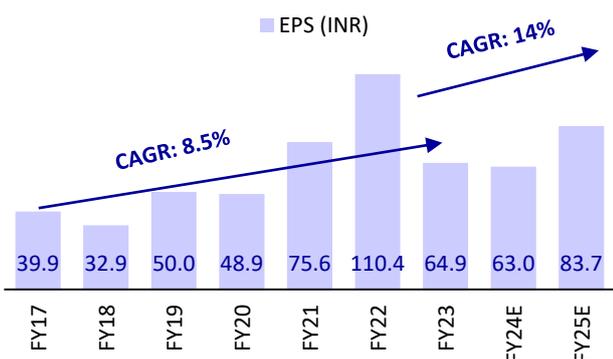
**Exhibit 7: Expect ~10% revenue CAGR over FY23–25**



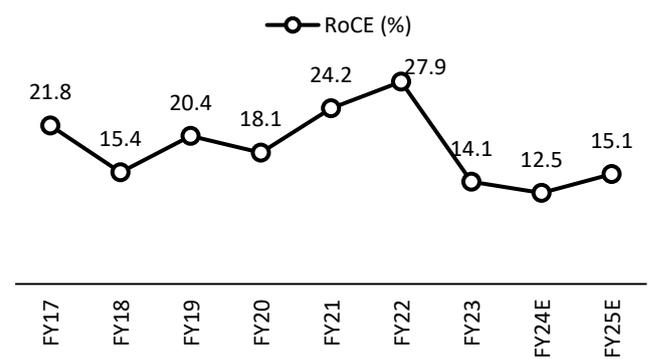
**Exhibit 8: Expect margin to expand 22bp over FY23–25**



**Exhibit 9: Expect 14% earnings CAGR over FY23–25**



**Exhibit 10: RoCE to reach ~15% by FY25**



Source: Company, MOFSL

Source: Company, MOFSL

## Financials and valuations

Income Statement							(INR m)	
Y/E March	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E	
<b>Total Income from Operations</b>	<b>49,463</b>	<b>53,944</b>	<b>69,694</b>	<b>89,598</b>	<b>77,675</b>	<b>80,474</b>	<b>93,688</b>	
Change (%)	27.1	9.1	29.2	28.6	-13.3	3.6	16.4	
<b>Total Expenditure</b>	<b>30,744</b>	<b>35,523</b>	<b>40,711</b>	<b>50,779</b>	<b>53,997</b>	<b>57,619</b>	<b>64,926</b>	
% of Sales	62.2	65.9	58.4	56.7	69.5	71.6	69.3	
<b>EBITDA</b>	<b>18,719</b>	<b>18,422</b>	<b>28,983</b>	<b>38,819</b>	<b>23,678</b>	<b>22,855</b>	<b>28,762</b>	
Margin (%)	37.8	34.1	41.6	43.3	30.5	28.4	30.7	
Depreciation	1,689	1,862	2,556	3,115	3,432	3,820	3,729	
<b>EBIT</b>	<b>17,030</b>	<b>16,559</b>	<b>26,427</b>	<b>35,704</b>	<b>20,246</b>	<b>19,035</b>	<b>25,034</b>	
Int. and Finance Charges	35	61	9	8	7	20	0	
Other Income	1,220	1,075	626	733	2,150	2,978	3,279	
<b>PBT bef. EO Exp.</b>	<b>18,215</b>	<b>17,573</b>	<b>27,044</b>	<b>36,429</b>	<b>22,390</b>	<b>21,992</b>	<b>28,313</b>	
EO Items	336	-621	-384	406	1,297	-60	0	
<b>PBT after EO Exp.</b>	<b>18,551</b>	<b>16,952</b>	<b>26,660</b>	<b>36,835</b>	<b>23,687</b>	<b>21,932</b>	<b>28,313</b>	
Total Tax	5,023	4,429	6,818	7,231	5,453	5,264	6,087	
Tax Rate (%)	27.1	26.1	25.6	19.6	23.0	24.0	21.5	
Minority Interest	0	0	0	0	0	0	0	
<b>Reported PAT</b>	<b>13,527</b>	<b>12,523</b>	<b>19,843</b>	<b>29,605</b>	<b>18,234</b>	<b>16,669</b>	<b>22,226</b>	
<b>Adjusted PAT</b>	<b>13,282</b>	<b>12,991</b>	<b>20,062</b>	<b>29,303</b>	<b>17,222</b>	<b>16,714</b>	<b>22,226</b>	
Change (%)	52.0	-2.2	54.4	46.1	-41.2	-2.9	33.0	
Margin (%)	26.2	23.6	28.5	32.4	21.6	20.8	23.7	

Balance Sheet							(INR m)	
Y/E March	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E	
Equity Share Capital	531	531	531	531	531	531	531	
Total Reserves	69,041	72,568	92,415	1,16,751	1,27,140	1,38,629	1,53,966	
<b>Net Worth</b>	<b>69,572</b>	<b>73,099</b>	<b>92,946</b>	<b>1,17,282</b>	<b>1,27,671</b>	<b>1,39,160</b>	<b>1,54,497</b>	
Total Loans	1,056	389	4	0	0	0	0	
Deferred Tax Liabilities	2,188	2,696	3,348	4,069	5,230	5,230	5,230	
<b>Capital Employed</b>	<b>72,816</b>	<b>76,184</b>	<b>96,298</b>	<b>1,21,351</b>	<b>1,32,901</b>	<b>1,44,389</b>	<b>1,59,726</b>	
Gross Block	26,339	35,143	46,919	56,246	63,653	70,848	81,337	
Less: Accum. Deprn.	5,462	7,324	9,880	12,995	16,427	20,247	23,975	
<b>Net Fixed Assets</b>	<b>20,878</b>	<b>27,819</b>	<b>37,039</b>	<b>43,251</b>	<b>47,226</b>	<b>50,601</b>	<b>57,362</b>	
Capital WIP	4,919	9,197	7,106	4,699	2,119	5,924	6,935	
Total Investments	19,456	9,714	0	720	771	771	771	
<b>Curr. Assets, Loans&amp;Adv.</b>	<b>35,106</b>	<b>38,584</b>	<b>63,563</b>	<b>84,933</b>	<b>94,130</b>	<b>1,00,103</b>	<b>1,10,707</b>	
Inventory	17,723	18,639	21,452	28,286	30,004	29,994	34,687	
Account Receivables	11,634	14,134	16,765	24,239	17,925	18,961	22,845	
Cash and Bank Balance	1,153	1,226	21,560	28,189	42,131	46,932	48,199	
Loans and Advances	4,597	4,586	3,786	4,219	4,070	4,216	4,978	
<b>Curr. Liability &amp; Prov.</b>	<b>7,543</b>	<b>9,130</b>	<b>11,411</b>	<b>12,251</b>	<b>11,345</b>	<b>13,010</b>	<b>16,049</b>	
Account Payables	5,320	6,626	7,632	7,957	7,625	9,156	11,562	
Other Current Liabilities	2,039	2,174	3,501	3,986	3,364	3,485	4,058	
Provisions	185	329	278	309	355	368	429	
<b>Net Current Assets</b>	<b>27,563</b>	<b>29,455</b>	<b>52,153</b>	<b>72,681</b>	<b>82,785</b>	<b>87,093</b>	<b>94,659</b>	
<b>Appl. of Funds</b>	<b>72,816</b>	<b>76,184</b>	<b>96,298</b>	<b>1,21,351</b>	<b>1,32,901</b>	<b>1,44,389</b>	<b>1,59,726</b>	

E: MOFSL Estimates

## Financials and valuations

### Ratios

Y/E March	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
<b>Basic (INR)</b>							
<b>EPS</b>	<b>50.0</b>	<b>48.9</b>	<b>75.6</b>	<b>110.4</b>	<b>64.9</b>	<b>63.0</b>	<b>83.7</b>
Cash EPS	56.4	56.0	85.2	122.1	77.8	77.4	97.8
BV/Share	262.1	275.4	350.1	441.8	481.0	524.2	582.0
DPS	10.0	16.0	20.0	29.9	17.0	16.2	21.5
Payout (%)	23.7	40.9	32.3	32.3	29.8	31.1	31.0
<b>Valuation (x)</b>							
P/E	70.0	71.6	46.4	31.8	54.0	55.7	41.9
Cash P/E	62.1	62.6	41.1	28.7	45.0	45.3	35.8
P/BV	13.4	12.7	10.0	7.9	7.3	6.7	6.0
EV/Sales	18.8	17.2	13.0	10.1	11.4	11.0	9.4
EV/EBITDA	49.7	50.5	31.4	23.2	37.5	38.7	30.7
Dividend Yield (%)	0.3	0.5	0.6	0.9	0.5	0.5	0.6
FCF per share	8.3	1.2	39.1	45.2	69.8	26.5	18.4
<b>Return Ratios (%)</b>							
RoE	20.6	18.2	24.2	27.9	14.1	12.5	15.1
RoCE	20.4	18.1	24.2	27.9	14.1	12.5	15.1
RoIC	28.3	23.7	31.8	36.9	17.7	16.2	20.2
<b>Working Capital Ratios</b>							
Asset Turnover (x)	0.7	0.7	0.7	0.7	0.6	0.6	0.6
Inventory (Days)	131	123	112	115	141	136	135
Debtor (Days)	86	96	88	99	84	86	89
Creditor (Days)	39	45	40	32	36	42	45
<b>Leverage Ratio (x)</b>							
Net Debt/Equity	-0.3	-0.1	-0.2	-0.25	-0.34	-0.3	-0.3

### Cash Flow Statement

Y/E March	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
<b>(INR m)</b>							
OP/(Loss) before Tax	18,551	16,952	26,660	36,835	23,687	21,932	28,313
Depreciation	1,689	1,862	2,556	3,115	3,432	3,820	3,729
Interest & Finance Charges	-40	-6	-564	4	-2,144	-2,958	-3,279
Direct Taxes Paid	-4,844	-4,452	-6,443	-6,410	-5,453	-5,264	-6,087
(Inc)/Dec in WC	-4,998	-2,183	-2,641	-13,705	3,838	493	-6,299
<b>CF from Operations</b>	<b>10,357</b>	<b>12,174</b>	<b>19,569</b>	<b>19,840</b>	<b>23,360</b>	<b>18,024</b>	<b>16,376</b>
Others	-814	-14	-100	-722	0	0	0
<b>CF from Operating incl EO</b>	<b>9,543</b>	<b>12,160</b>	<b>19,469</b>	<b>19,118</b>	<b>23,360</b>	<b>18,024</b>	<b>16,376</b>
(Inc)/Dec in FA	-7,331	-11,829	-9,101	-7,132	-4,827	-11,000	-11,500
<b>Free Cash Flow</b>	<b>2,213</b>	<b>331</b>	<b>10,368</b>	<b>11,986</b>	<b>18,534</b>	<b>7,024</b>	<b>4,876</b>
(Pur)/Sale of Investments	-291	10,336	9,740	-15,990	-50	0	0
Others	767	658	112	1,173	2,150	2,978	3,279
<b>CF from Investments</b>	<b>-6,854</b>	<b>-835</b>	<b>751</b>	<b>-21,949</b>	<b>-2,727</b>	<b>-8,022</b>	<b>-8,221</b>
Issue of Shares	0	0	0	0	0	0	0
Inc/(Dec) in Debt	776	-612	-333	-4	0	0	0
Interest Paid	-35	-61	-9	-4	-7	-20	0
Dividend Paid	-3,200	-10,241	0	-5,309	-5,432	-5,180	-6,889
Others	0	0	-7	13,992	-1,043	0	0
<b>CF from Fin. Activity</b>	<b>-2,459</b>	<b>-10,914</b>	<b>-349</b>	<b>8,676</b>	<b>-6,481</b>	<b>-5,200</b>	<b>-6,889</b>
<b>Inc/Dec of Cash</b>	<b>230</b>	<b>411</b>	<b>19,871</b>	<b>5,844</b>	<b>14,152</b>	<b>4,801</b>	<b>1,267</b>
Opening Balance	1,124	1,153	1,227	21,560	28,189	42,131	46,932
<b>Closing Balance</b>	<b>1,354</b>	<b>1,564</b>	<b>21,097</b>	<b>27,405</b>	<b>42,341</b>	<b>46,932</b>	<b>48,199</b>
Forex and other adjustments	-201	-337	463	784	-210	0	0
<b>Total Cash &amp; Cash Eq</b>	<b>1,153</b>	<b>1,227</b>	<b>21,560</b>	<b>28,189</b>	<b>42,131</b>	<b>46,932</b>	<b>48,199</b>

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