

Divi's Laboratories

Estimate change	↑
TP change	↑
Rating change	↔

CMP: INR4,122 TP: INR3,900 (-5%) Neutral

Custom Synthesis drives earnings

Efforts across CS and API segments to improve earnings outlook

Bloomberg	DIVI IN
Equity Shares (m)	265
M.Cap.(INRb)/(USD\$)	1094.4 / 13.2
52-Week Range (INR)	4175 / 3295
1, 6, 12 Rel. Per (%)	6/-6/-4
12M Avg Val (INR M)	1786

Financials & Valuations (INR b)

Y/E MARCH	FY24	FY25E	FY26E
Sales	78.5	91.4	106.2
EBITDA	22.2	28.0	33.8
Adj. PAT	15.9	21.3	25.6
EBIT Margin (%)	23.5	26.5	28.0
Cons. Adj. EPS (INR)	60.0	80.1	96.5
EPS Gr. (%)	-7.5	33.4	20.5
BV/Sh. (INR)	511.2	566.5	633.1

Ratios

Net D:E	-0.3	-0.3	-0.3
RoE (%)	12.1	14.9	16.1
RoCE (%)	12.1	14.9	16.1
Payout (%)	31.0	31.0	31.0

Valuations

P/E (x)	68.7	51.5	42.7
EV/EBITDA (x)	47.4	37.4	30.9
Div. Yield (%)	0.4	0.5	0.6
FCF Yield (%)	0.2	0.9	0.7
EV/Sales (x)	13.4	11.5	9.8

Shareholding pattern (%)

As On	Mar-24	Dec-23	Mar-23
Promoter	51.9	51.9	51.9
DII	22.2	21.9	21.1
FII	14.7	14.9	14.7
Others	11.2	11.3	12.3

FII Includes depository receipts

- Divi's Lab (DIVI) delivered a strong beat on earnings in 4QFY24, fueled by a revival in the Custom Synthesis (CS) business. Improved sales growth drove better profitability for the quarter as well. Having said these, FY24 would be the second consecutive year for YoY earnings decline, albeit at lower intensity, with improved traction in the CS business for the quarter.
- We raise our earnings estimates by 3% each for FY25/FY26, factoring in: 1) a better demand outlook in the CDMO segment, 2) the addition of new technologies, which will enhance the scope of contracts from the innovators, and 3) a higher number of product offerings in the generics segment. We value DIVI at 40x 12M forward earnings to arrive at our TP of INR3,900.
- DIVI has been making great strides in both the CS and API segments through a strong chemistry skill set. It is not only getting ready to supply APIs once they are off-patent, but also working on backward integration to gain market share/maintain profitability in the existing API portfolio. DIVI continues to improve services under the CDMO segment during product development and manufacturing stages. We expect a 27% earnings CAGR over FY24-26. The valuations, however, adequately capture the earnings upside (51x FY25E EPS of INR80 and 43X FY26E EPS of INR97). **Reiterate Neutral.**

Improved operating leverage drives profitability

- DIVI's revenue grew 18% YoY to INR23b (our est: INR19b) for the quarter.
- Gross margin expanded 330bp YoY to 60.8% due to a change in product mix.
- However, EBITDA margin expanded at a higher rate of 650bp YoY to 31.7% (our est: 26.8%), largely due to higher GM supported by lower employee costs/other expenses (-30bp/300bp as a % of sales)
- As a result, EBITDA grew 48.6% YoY to INR7.3b (our est: INR5.2b) for the quarter.
- Adjusted for INR20m in forex gain, PAT grew 65.7% YoY to INR5.4b (our est: INR3.9b).
- During FY24**, DIVI's revenue/ EBITDA/PAT declined 1%/6%/7.5% YoY to INR78.5b/INR22.2b/INR15.9b. Moreover, EBITDA margin contracted 220bp YoY to 28.3%.

Highlights from the management commentary

- Despite the decline in prices, DIVI has been able to maintain gross margin in the API segment due to a backward integration project in place and a higher volume share.
- With respect to the long-term supply agreement with one of the innovatory customers, DIVI would incur a capex of INR6.5b-INR7.0b at the existing manufacturing site. It would take about one year to build the facility and one year to get regulatory approvals. The product to be manufactured at this site would require regulatory approval for the innovator.

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Investors are advised to refer through important disclosures made at the last page of the Research Report.

Motilal Oswal research is available on www.motilaloswal.com/Institutional-Equities, Bloomberg, Thomson Reuters, Factset and S&P Capital.

Quarterly Performance

(INR m)

Y/E March	FY23				FY24				FY23	FY24	FY24	Var. (%)
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q				
Net Sales	22,545	18,545	17,077	19,508	17,780	19,090	18,550	23,030	77,675	78,450	19,250	19.6
YoY Change (%)	15.0	-6.7	-31.5	-22.5	-21.1	2.9	8.6	18.1	-13.3	1.0	-1.3	
Total Expenditure	14,078	12,335	12,994	14,590	12,740	14,100	13,660	15,720	53,997	56,220	14,084	
EBITDA	8,467	6,210	4,083	4,918	5,040	4,990	4,890	7,310	23,678	22,230	5,166	41.5
YoY Change (%)	-0.6	-24.7	-62.9	-55.5	-40.5	-19.7	19.8	48.6	-39.0	-6.1	5.0	
Margins (%)	37.6	33.5	23.9	25.2	28.3	26.1	26.4	31.7	30.5	28.3	26.8	
Depreciation	837	857	868	870	930	950	950	950	3,432	3,780	990	
EBIT	7,630	5,353	3,215	4,048	4,110	4,040	3,940	6,360	20,246	18,450	4,176	52.3
YoY Change (%)	-2.0	-28.4	-68.5	-60.4	-46.1	-24.5	22.5	57.1	-43.3	-8.9	3.2	
Interest	0	0	1	2	0	10	0	20	7	30	0	
Other Income	320	492	674	662	810	750	770	770	2,150	3,100	731	
PBT before EO Income	7,950	5,845	3,888	4,707	4,920	4,780	4,710	7,110	22,390	21,520	4,908	
Forex gain /(Loss)	564	308	467	-42	30	-90	180	20	1,297	140	0	
PBT	8,514	6,153	4,354	4,665	4,950	4,690	4,890	7,130	23,687	21,660	4,908	45.3
Tax	1,493	1,216	1,288	1,455	1,360	1,210	1,310	1,750	5,453	5,630	1,077	
Rate (%)	17.5	19.8	29.6	31.2	27.5	25.8	26.8	24.5	23.0	26.0	21.9	
PAT	7,021	4,937	3,066	3,210	3,590	3,480	3,580	5,380	18,234	16,030	3,828	40.5
Adj. PAT	6,556	4,690	2,738	3,239	3,568	3,547	3,448	5,365	17,222	15,928	3,829	40.1
YoY Change (%)	2.6	-23.9	-67.2	-61.5	-45.6	-24.4	25.9	65.7	-41.2	-7.5	18.2	
Margins (%)	31.1	26.6	18.0	16.5	20.2	18.2	19.3	23.4	23.5	20.4	19.9	
Adj. EPS	24.7	17.7	10.3	12.2	13.4	13.4	13.0	20.2	64.9	60.0	14.4	

Quarterly Performance

Y/E March	FY23				FY24				FY23	FY24	FY24
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q			
Cost Break-up											
RM Cost (% of Sales)	36.0	36.4	43.3	42.4	38.7	41.4	39.3	39.2	39.3	39.9	39.3
Staff Cost (% of Sales)	10.9	12.5	14.0	13.2	14.8	13.9	14.4	12.9	12.6	13.9	13.7
Other Expenses(% of Sales)	15.5	17.6	18.8	19.2	18.2	18.5	19.9	16.2	17.6	17.8	20.1
Tax rate (%)	17.5	19.8	29.6	31.2	27.5	25.8	26.8	24.5	23.0	26.0	26.0
Gross Margins(%)	64.0	63.6	56.7	57.6	61.3	58.6	60.7	60.8	60.7	60.1	60.7
EBITDA Margins(%)	37.6	33.5	23.9	25.2	28.3	26.1	26.4	31.7	30.5	28.3	26.8
EBIT Margins(%)	33.8	28.9	18.8	20.7	23.1	21.2	21.2	27.6	26.1	23.5	21.7



Key takeaways from the management commentary

- The two molecules going off-patent would provide a business opportunity to DIVI in FY25; seven molecules have gone off-patent in total over the next five years.
- The Kakinada facility will start operations in 2Q/3QFY25.
- It would incur a capex of INR15b apart from INR7b for a specific customer. The CWIP was INR7b.
- The generics:CS share was 49:51 for the quarter and 55:45 for FY24. This implies about 47% YoY growth in CS revenue for the quarter.
- It had a Nutraceutical business of INR1.9b/INR7.2b for 4QFY24/FY24.
- It had INR32b surplus cash at the end of FY24.
- Exports formed 89%/87% of total sales for 4QFY24/FY24. The US and EU formed 70% of total sales for FY24.

Focus on new growth levers in the CS/generics businesses

CS: Scale-up of existing contracts and gaining newer contracts

- In FY24, CS sales grew moderately by 2.8% YoY to INR35b, mainly affected by the high base of last year due to Molnupiravir-based contracts.
- However, DIVI has two major contracts from the innovator customer. These projects are expected to scale up in the coming quarters. The products are under patent and thus provide good visibility for the business.
- Given the complex nature of products (contrast media) and limited customers, DIVI is suitably placed given its capabilities.
- Further, DIVI is receiving inquiries about orders in the CS business due to the onset of Bio Secure Act in the US, especially in phase-2 and phase-3 clinical trials.
- Additionally, it has received a long-term contract from the Innovator for which DIVI is incurring a capex of INR7b, which would drive growth over the medium to long term.
- Accordingly, we expect a 22% CAGR in CS sales to INR52b over FY24-26.

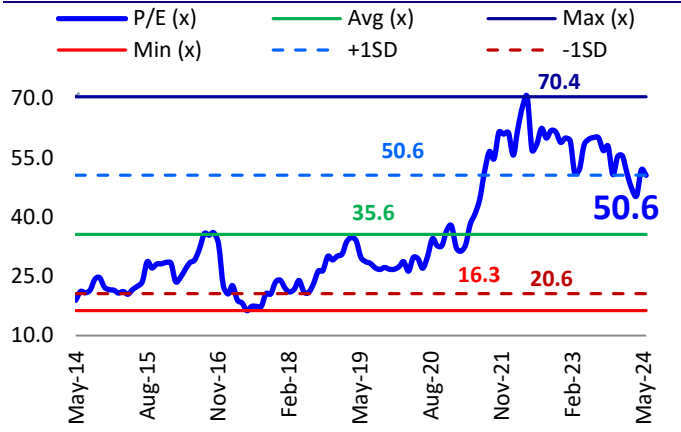
Generics: new launches/capacity enhancements to fuel growth

- In FY24, the generic API segment declined 3.4% YoY to INR36b as continued pricing pressure affected the growth. However, it was offset by increased volume off-take of key products.
- Interestingly, DIVI has gained market share in several large volume APIs. It has also increased capacity for several APIs.
- Moreover, there are multiple products that are coming off patent over the next four years. This provides a significant opportunity for DIVI.
- Further, DIVI is planning to supply seven molecules over the next 3-5 years, which would also drive growth.
- DIVI is also backward integrated, which is likely to be a key differentiator vs. peers.
- Accordingly, we expect DIVI to post a 115% revenue CAGR to INR45b over FY24-26.

Reiterate Neutral

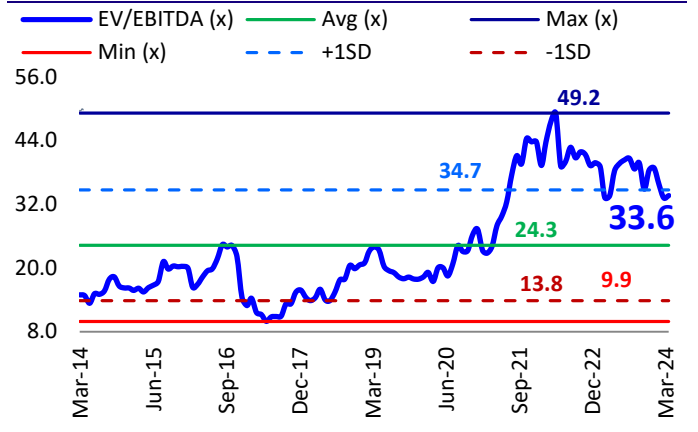
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Exhibit 1: P/E chart



Source: MOFSL, Company, Bloomberg

Exhibit 2: EV/EBITDA chart



Source: MOFSL, Company, Bloomberg

Story in charts

Exhibit 3: Revenue grew 18.1% YoY in 4QFY24

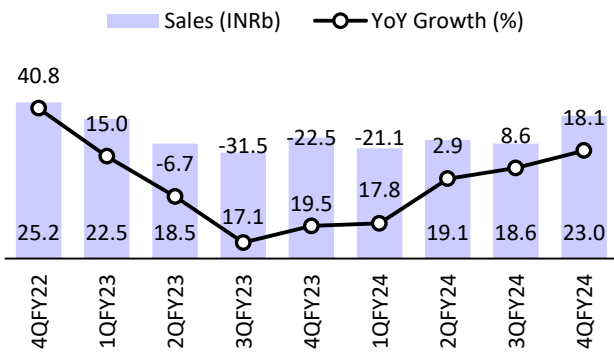


Exhibit 4: CS segment contributed 51% to revenue in 4Q

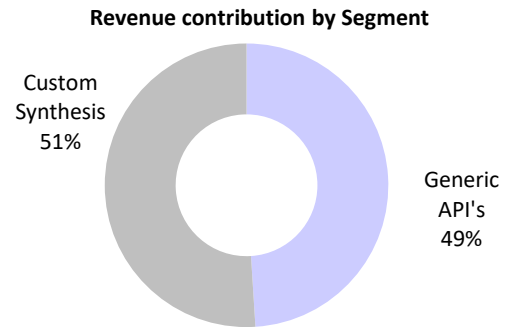


Exhibit 5: Gross margin up 330bp YoY in 4QFY24

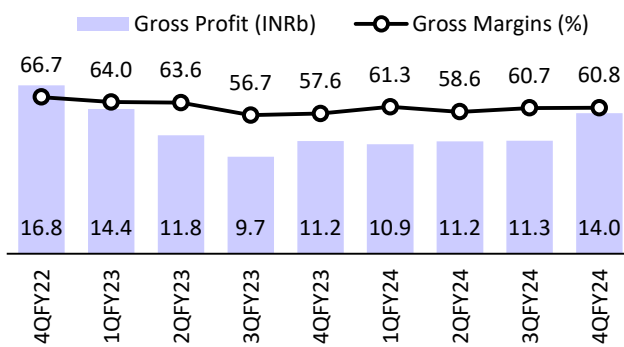


Exhibit 6: EBITDA margin expanded 650bp YoY in 4QFY24

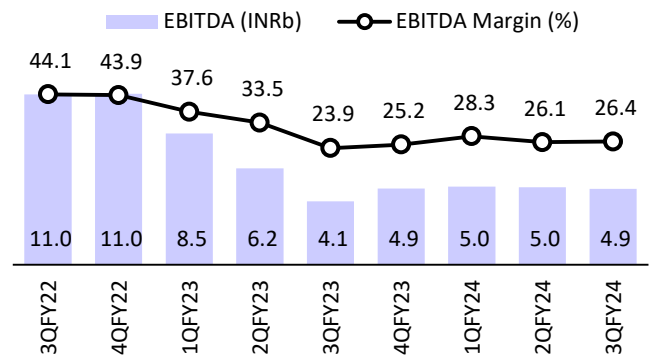


Exhibit 7: Expect ~16% revenue CAGR over FY24–26

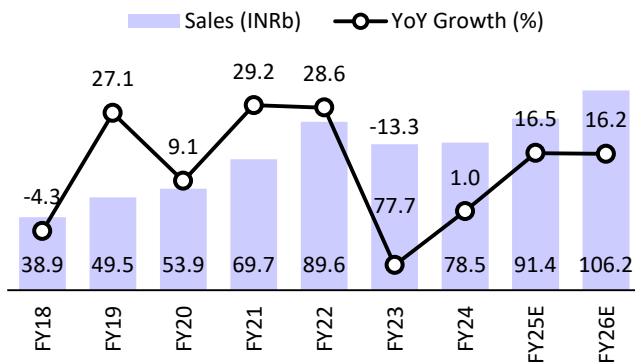


Exhibit 8: Expect margin to expand 350bp over FY24–26

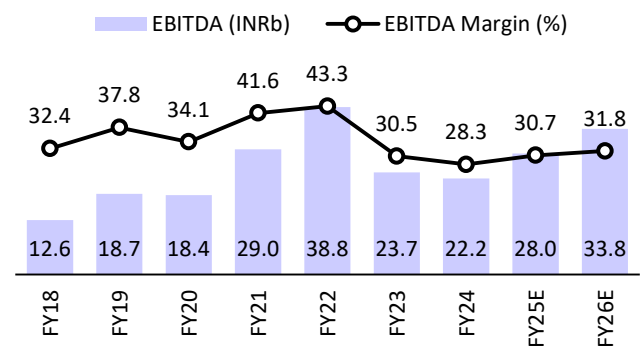
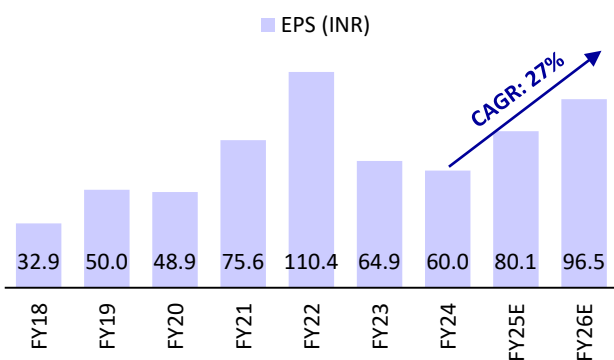
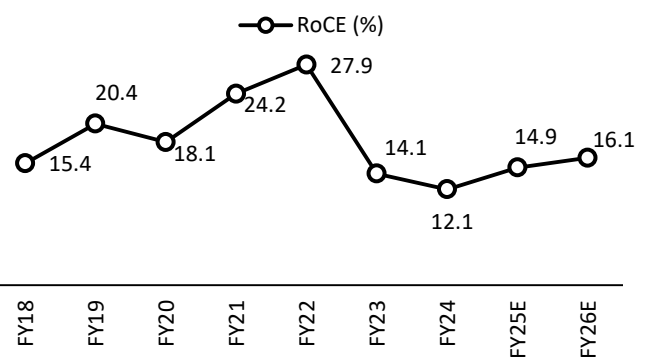


Exhibit 9: Expect 27% earnings CAGR over FY24–26



Source: Company, MOFSL

Exhibit 10: RoCE to reach ~16% by FY26



Source: Company, MOFSL

Financials and valuations

Income Statement								(INR m)
Y/E March	FY19	FY20	FY21	FY22	FY23	FY24	FY25E	FY26E
Total Income from Operations	49,463	53,944	69,694	89,598	77,675	78,450	91,355	1,06,195
Change (%)	27.1	9.1	29.2	28.6	-13.3	1.0	16.5	16.2
Total Expenditure	30,744	35,523	40,711	50,779	53,997	56,220	63,309	72,425
% of Sales	62.2	65.9	58.4	56.7	69.5	71.7	69.3	68.2
EBITDA	18,719	18,422	28,983	38,819	23,678	22,230	28,046	33,770
Margin (%)	37.8	34.1	41.6	43.3	30.5	28.3	30.7	31.8
Depreciation	1,689	1,862	2,556	3,115	3,432	3,780	3,826	4,012
EBIT	17,030	16,559	26,427	35,704	20,246	18,450	24,220	29,758
Int. and Finance Charges	35	61	9	8	7	30	0	0
Other Income	1,220	1,075	626	733	2,150	3,100	3,380	3,717
PBT bef. EO Exp.	18,215	17,573	27,044	36,429	22,390	21,520	27,600	33,475
EO Items	336	-621	-384	406	1,297	140	0	0
PBT after EO Exp.	18,551	16,952	26,660	36,835	23,687	21,660	27,600	33,475
Total Tax	5,023	4,429	6,818	7,231	5,453	5,630	6,348	7,867
Tax Rate (%)	27.1	26.1	25.6	19.6	23.0	26.0	23.0	23.5
Minority Interest	0	0	0	0	0	0	0	0
Reported PAT	13,527	12,523	19,843	29,605	18,234	16,027	21,252	25,608
Adjusted PAT	13,282	12,991	20,062	29,303	17,222	15,926	21,252	25,608
Change (%)	52.0	-2.2	54.4	46.1	-41.2	-7.5	33.4	20.5
Margin (%)	26.2	23.6	28.5	32.4	21.6	20.3	23.3	24.1

Balance Sheet								(INR m)
Y/E March	FY19	FY20	FY21	FY22	FY23	FY24	FY25E	FY26E
Equity Share Capital	531	531	531	531	531	531	531	531
Total Reserves	69,041	72,568	92,415	1,16,751	1,27,140	1,35,180	1,49,845	1,67,516
Net Worth	69,572	73,099	92,946	1,17,282	1,27,671	1,35,711	1,50,376	1,68,047
Total Loans	1,056	389	4	0	0	0	0	0
Deferred Tax Liabilities	2,188	2,696	3,348	4,069	5,230	5,720	5,720	5,720
Capital Employed	72,816	76,184	96,298	1,21,351	1,32,901	1,41,431	1,56,096	1,73,767
Gross Block	26,339	35,143	46,919	56,246	63,653	67,597	79,571	91,166
Less: Accum. Deprn.	5,462	7,324	9,880	12,995	16,427	20,207	24,033	28,046
Net Fixed Assets	20,878	27,819	37,039	43,251	47,226	47,390	55,538	63,120
Capital WIP	4,919	9,197	7,106	4,699	2,119	7,780	7,306	7,211
Total Investments	19,456	9,714	0	720	771	820	820	820
Curr. Assets, Loans&Adv.	35,106	38,584	63,563	84,933	94,130	99,011	1,09,448	1,22,187
Inventory	17,723	18,639	21,452	28,286	30,004	31,840	33,823	38,693
Account Receivables	11,634	14,134	16,765	24,239	17,925	21,560	22,276	25,894
Cash and Bank Balance	1,153	1,226	21,560	28,189	42,131	39,800	46,514	49,734
Loans and Advances	4,597	4,586	3,786	4,219	4,070	5,811	6,836	7,866
Curr. Liability & Prov.	7,543	9,130	11,411	12,251	11,345	13,570	17,015	19,571
Account Payables	5,320	6,626	7,632	7,957	7,625	8,640	11,274	12,898
Other Current Liabilities	2,039	2,174	3,501	3,986	3,364	4,490	5,229	6,078
Provisions	185	329	278	309	355	440	512	596
Net Current Assets	27,563	29,455	52,153	72,681	82,785	85,441	92,433	1,02,616
Appl. of Funds	72,816	76,184	96,298	1,21,351	1,32,901	1,41,431	1,56,096	1,73,767

E: MOSL Estimates

Financials and valuations

Ratios

Y/E March	FY19	FY20	FY21	FY22	FY23	FY24	FY25E	FY26E
Basic (INR)								
EPS	50.0	48.9	75.6	110.4	64.9	60.0	80.1	96.5
Cash EPS	56.4	56.0	85.2	122.1	77.8	74.2	94.5	111.6
BV/Share	262.1	275.4	350.1	441.8	481.0	511.2	566.5	633.1
DPS	10.0	16.0	20.0	29.9	17.0	15.5	20.6	24.8
Payout (%)	23.7	40.9	32.3	32.3	29.8	31.0	31.0	31.0
Valuation (x)								
P/E	82.4	84.2	54.5	37.3	63.5	68.7	51.5	42.7
Cash P/E	73.1	73.7	48.4	33.8	53.0	55.5	43.6	36.9
P/BV	15.7	15.0	11.8	9.3	8.6	8.1	7.3	6.5
EV/Sales	22.1	20.3	15.4	11.9	13.5	13.4	11.5	9.8
EV/EBITDA	58.4	59.4	37.0	27.5	44.4	47.4	37.4	30.9
Dividend Yield (%)	0.2	0.4	0.5	0.7	0.4	0.4	0.5	0.6
FCF per share	8.3	1.2	39.1	45.2	69.8	8.1	37.4	28.0
Return Ratios (%)								
RoE	20.6	18.2	24.2	27.9	14.1	12.1	14.9	16.1
RoCE	20.4	18.1	24.2	27.9	14.1	12.1	14.9	16.1
RoIC	28.3	23.7	31.8	36.9	17.7	15.1	19.2	20.9
Working Capital Ratios								
Asset Turnover (x)	0.7	0.7	0.7	0.7	0.6	0.6	0.6	0.6
Inventory (Days)	131	123	112	115	141	148	135	133
Debtor (Days)	86	96	88	99	84	100	89	89
Creditor (Days)	39	45	40	32	36	40	45	44
Leverage Ratio (x)								
Net Debt/Equity	-0.3	-0.1	-0.2	-0.25	-0.34	-0.3	-0.3	-0.3

Cash Flow Statement

Y/E March	FY19	FY20	FY21	FY22	FY23	FY24	FY25E	FY26E
(INR m)								
OP/(Loss) before Tax	18,551	16,952	26,660	36,835	23,687	21,660	27,600	33,475
Depreciation	1,689	1,862	2,556	3,115	3,432	3,780	3,826	4,012
Interest & Finance Charges	-40	-6	-564	4	-2,144	-3,070	-3,380	-3,717
Direct Taxes Paid	-4,844	-4,452	-6,443	-6,410	-5,453	-5,630	-6,348	-7,867
(Inc)/Dec in WC	-4,998	-2,183	-2,641	-13,705	3,838	-4,987	-278	-6,963
CF from Operations	10,357	12,174	19,569	19,840	23,360	11,753	21,420	18,941
Others	-814	-14	-100	-722	0	0	0	0
CF from Operating incl EO	9,543	12,160	19,469	19,118	23,360	11,753	21,420	18,941
(Inc)/Dec in FA	-7,331	-11,829	-9,101	-7,132	-4,827	-9,605	-11,500	-11,500
Free Cash Flow	2,213	331	10,368	11,986	18,534	2,148	9,920	7,441
(Pur)/Sale of Investments	-291	10,336	9,740	-15,990	-50	-50	0	0
Others	767	658	-668	1,173	2,150	704	3,380	3,717
CF from Investments	-6,854	-835	-29	-21,949	-2,727	-8,951	-8,120	-7,783
Issue of Shares	0	0	0	0	0	0	0	0
Inc/(Dec) in Debt	776	-612	-333	-4	0	0	0	0
Interest Paid	-35	-61	-9	-4	-7	-30	0	0
Dividend Paid	-3,200	-10,241	0	-5,309	-5,432	-4,968	-6,587	-7,937
CF from Fin. Activity	-2,459	-10,914	-349	8,676	-6,481	-5,133	-6,587	-7,937
Inc/Dec of Cash	230	411	19,091	5,844	14,152	-2,331	6,713	3,220
Opening Balance	1,124	1,153	1,227	21,560	28,189	42,131	39,800	46,514
Closing Balance	1,354	1,564	20,317	27,405	42,341	39,800	46,514	49,734
Forex and other adjustments	-201	-337	1,243	784	-210	0	0	0
Total Cash & Cash Eq	1,153	1,227	21,560	28,189	42,131	39,800	46,514	49,734

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NOTES

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Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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