

# Divi's Laboratories

Estimate change

TP change

Rating change



Bloomberg	DIVI IN
Equity Shares (m)	265
M.Cap.(INRb)/(USDb)	989.7 / 12.4
52-Week Range (INR)	5425 / 3365
1, 6, 12 Rel. Per (%)	-9/-15/-32
12M Avg Val (INR M)	2415

## Financials & Valuations (INR b)

Y/E MARCH	FY22	FY23E	FY24E
Sales	89.6	93.1	106.4
EBITDA	38.8	36.6	43.7
Adj. PAT	29.3	28.5	34.2
EBIT Margin (%)	39.8	35.8	38.0
Cons. Adj. EPS (INR)	110.4	107.2	128.8
EPS Gr. (%)	46.1	-2.9	20.1
BV/Sh. (INR)	441.8	517.1	605.9

## Ratios

Net D:E	-0.2	-0.4	-0.4
RoE (%)	27.9	22.4	22.9
RoCE (%)	27.9	22.4	22.9
Payout (%)	32.3	29.3	31.0

## Valuations

P/E (x)	33.8	34.8	29.0
EV/EBITDA (x)	24.8	25.7	21.2
Div. Yield (%)	0.8	0.7	0.9
FCF Yield (%)	1.1	2.7	1.8
EV/Sales (x)	10.7	10.1	8.7

## Shareholding pattern (%)

As On	Jun-22	Mar-22	Jun-21
Promoter	51.9	51.9	52.0
DII	20.0	18.3	16.6
FII	16.5	18.5	20.6
Others	11.6	11.3	10.9

FII Includes depository receipts

CMP: INR3,728

TP: INR4,340 (+16%)

Buy

## Short-term hiccups in margin; outlook remains intact

### Kakinada project key to major capex in the near term

- DIVI delivered an in-line earnings in 1QFY23. While traction in Custom Synthesis (CS) has toned down in 1QFY23, there has been a pick-up in the sale of Nutraceuticals. Also, the completion of additional capacity will drive a better sales run-rate in the Generics segment.
- We cut our FY23/FY24 EPS estimate by 6%/3% to factor in: a) a higher operating cost due to an inflation-linked increase in raw material cost and elevated freight cost, and b) some moderation in the CS segment. We continue to value DIVI at 33x 12M forward earnings to arrive at our TP of INR4,340.
- While the high base in FY22 may cap earnings growth in the near term, DIVI continues to strengthen its skill sets in newer technology like peptides, HiPo conjugate drugs, and contrast media products. It is also building up its commercial capability to tap future business opportunities. We maintain our Buy rating.

## Higher sales growth was outweighed by lower profitability on a YoY basis

- Revenues grew 15% YoY to INR22.5b (est. INR22.1b) in 1QFY23.
- Gross margin (GM) contracted by 330bp YoY to 64% due to the change in the segmental mix.
- EBITDA margin contracted at a higher rate by 590bp YoY to 37.6% (est. 40.6%) largely due to lower GM and higher other expenses (up 300bp as a percentage of sales).
- As a result, EBITDA was flat YoY at INR8.5b (est. INR9b) in 1QFY23.
- Adjusted for INR564m in forex gains, PAT rose 3% YoY to INR6.6b (est. INR6.7b) due to a lower tax rate in 1QFY23.

## Highlights from the management commentary

- The management reiterated its EBITDA margin guidance of 40%, including other income, for FY23.
- With capacity expansion in the Generics segment in place, it expects sales to pick up going forward.
- One of the capacity expansion projects, related to CS, is complete.
- DIVI had a Generics-to-CS share of 47:53 in 1QFY23.
- It garnered sales of INR1.9b in the Nutraceuticals segment in 1QFY23.
- CWIP stands at INR5b. The management expects capital expenditure of not more than INR5-6b in FY23, unless the Kakinada project kick starts.
- DIVI is working towards peptide chemistry and HiPo conjugate drug-related technology, which will drive opportunities over the next three-to-four years.

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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&amp;P Capital.

## Quarterly Performance

(INR m)

Y/E March	FY22E				FY23E				FY22	FY23E	FY23E	Var.
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE			1QE	(%)
<b>Net Sales</b>	<b>19,606</b>	<b>19,875</b>	<b>24,932</b>	<b>25,184</b>	<b>22,545</b>	<b>22,177</b>	<b>23,428</b>	<b>24,958</b>	<b>89,598</b>	<b>93,109</b>	<b>22,127</b>	<b>1.9</b>
YoY Change (%)	13.3	13.6	46.5	40.8	15.0	11.6	-6.0	-0.9	28.6	3.9	12.9	
Total Expenditure	11,086	11,623	13,930	14,140	14,078	13,683	14,151	14,605	50,779	56,517	13,144	
<b>EBITDA</b>	<b>8,521</b>	<b>8,252</b>	<b>11,003</b>	<b>11,044</b>	<b>8,467</b>	<b>8,494</b>	<b>9,278</b>	<b>10,353</b>	<b>38,819</b>	<b>36,592</b>	<b>8,984</b>	<b>-5.8</b>
YoY Change (%)	21.7	9.0	51.7	54.2	-0.6	2.9	-15.7	-6.3	33.9	-5.7	5.4	
Margins (%)	43.5	41.5	44.1	43.9	37.6	38.3	39.6	41.5	43.3	39.3	40.6	
Depreciation	733	774	799	810	837	833	840	730	3,115	3,240	809	
<b>EBIT</b>	<b>7,788</b>	<b>7,478</b>	<b>10,204</b>	<b>10,234</b>	<b>7,630</b>	<b>7,661</b>	<b>8,438</b>	<b>9,623</b>	<b>35,704</b>	<b>33,352</b>	<b>8,174</b>	<b>-6.7</b>
YoY Change (%)	21.0	7.5	55.3	58.4	-2.0	2.4	-17.3	-6.0	35.1	-6.6	5.0	
Interest	3	2	2	1	0	0	0	-1	8	0	0	
Other Income	163	191	166	212	320	330	350	350	733	1,350	200	
<b>PBT before EO Income</b>	<b>7,948</b>	<b>7,667</b>	<b>10,368</b>	<b>10,446</b>	<b>7,950</b>	<b>7,991</b>	<b>8,787</b>	<b>9,974</b>	<b>36,429</b>	<b>34,702</b>	<b>8,374</b>	
Forex gain /(Loss)	196	-71	-31	312	564	0	0	0	406	564	0	
<b>PBT</b>	<b>8,145</b>	<b>7,596</b>	<b>10,337</b>	<b>10,757</b>	<b>8,514</b>	<b>7,991</b>	<b>8,787</b>	<b>9,974</b>	<b>36,835</b>	<b>35,266</b>	<b>8,374</b>	<b>1.7</b>
Tax	2,574	1,532	1,314	1,811	1,493	1,438	1,626	1,791	7,231	6,348	1,675	
Rate (%)	31.6	20.2	12.7	16.8	17.5	18.0	18.5	18.0	19.6	18.0	20.0	
<b>PAT</b>	<b>5,571</b>	<b>6,065</b>	<b>9,022</b>	<b>8,946</b>	<b>7,021</b>	<b>6,552</b>	<b>7,162</b>	<b>8,182</b>	<b>29,605</b>	<b>28,918</b>	<b>6,699</b>	<b>4.8</b>
<b>Adj. PAT</b>	<b>6,391</b>	<b>6,165</b>	<b>8,336</b>	<b>8,413</b>	<b>6,556</b>	<b>6,552</b>	<b>7,162</b>	<b>8,182</b>	<b>29,303</b>	<b>28,453</b>	<b>6,699</b>	<b>-2.1</b>
YoY Change (%)	32.6	16.0	68.8	68.5	2.6	6.3	-14.1	-2.7	46.1	-2.9	4.8	
Margins (%)	28.4	30.5	36.2	35.5	31.1	29.5	30.6	32.8	33.0	31.1	30.3	

## Quarterly Performance

Y/E March	FY22				FY23E				FY22	FY23E	FY23E
	1Q	2Q	3Q	4Q	1Q	2QE	3QE	4QE			1QE
<b>Cost Break-up</b>											
RM Cost (% of Sales)	32.8	32.9	33.4	33.3	36.0	35.5	35.2	34.2	33.1	35.2	34.2
Staff Cost (% of Sales)	11.3	11.3	9.8	10.2	10.9	11.2	11.0	9.8	10.6	10.7	10.7
Other Expenses(% of Sales)	12.5	14.3	12.7	12.7	15.5	15.0	14.2	14.6	13.0	14.8	14.5
Tax rate (%)	31.6	20.2	12.7	16.8	17.5	18.0	18.5	18.0	19.6	18.0	20.0
Gross Margins (%)	67.2	67.1	66.6	66.7	64.0	64.5	64.8	65.8	66.9	64.8	65.8
EBITDA Margins (%)	43.5	41.5	44.1	43.9	37.6	38.3	39.6	41.5	43.3	39.3	40.6
EBIT Margins (%)	39.7	37.6	40.9	40.6	33.8	34.5	36.0	38.6	39.8	35.8	36.9



## Key takeaways from management commentary

- DIVI has capacity utilization of 83% and thus there is sufficient capacity available for medium term requirements.
- DIVI is working towards peptide chemistry, hi-po conjugate drugs related technology, which would drive opportunities for next 3-4 years.
- DIVI has completed all the orders related to Molnupiravir as of now.
- DIVI is experiencing elevated cost pressures on account of raw material and logistics.
- With capacity expansion in place, sartans and contrast media products are expected to drive growth over medium term. Further, the product patent expiries over next two years are going to drive opportunities in generics API segment over next 3-4 years.

## Moderate Outlook

### Custom Synthesis – High base drags sales growth; Outlook remains robust

- DIVI had a moderate 3% YoY revenue growth of INR10b in 1QFY23. DIVI has enjoyed a high growth period for custom synthesis business driven by its chemistry skills, manufacturing scale as well as regulatory compliance, and project execution. DIVI's has capability to fast-track projects is reflected in Molnupiravir opportunity executed in the recent past.
- The R&D cost for innovators remains at escalated level with reducing probability of success for new chemical entities. Further, the period of strong business is also decreasing with rising Para-IV litigations. This compels innovators to outsource manufacturing during research/commercial activities to reduce the operational cost as much as possible. With long term relationship, consistent track record, DIVI has large headroom for growth.
- We expect flattish sales due to high base of FY22 in CS to INR56b over FY22–24.

### Generics - Growth on the back of Patent expiries/Sartans

- The Generic API segment grew 26% YoY at INR10.6b in 1QFY23. DIVI is working on complex APIs (contrast media/Hi-Po APIs) linked to patent expiries worth USD20b over FY23-25. Subsequently, the dossiers filing is also underway in across geographies. Notably, DIVI has also taken product validation batches for 3 Sartans products in its new dedicated facility which would be filed in due course.
- We expect the generics API business to exhibit 16% revenue CAGR to INR50b over FY22–24 vs moderate 4% YoY growth in sales for FY22.

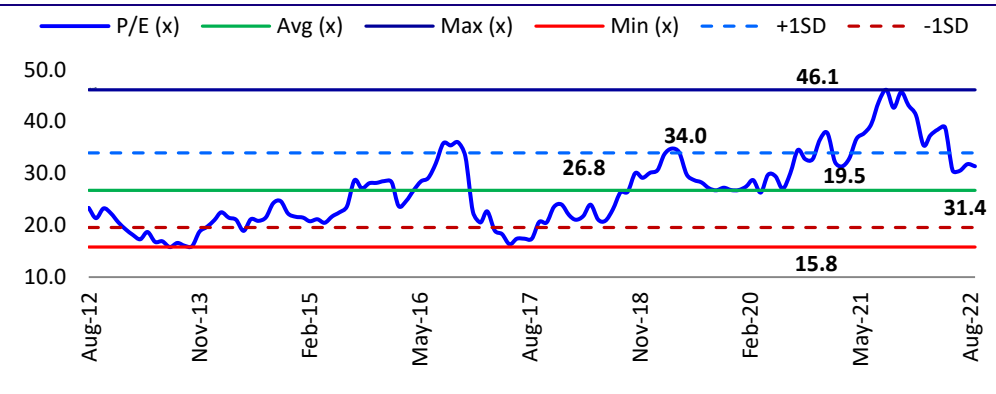
### Existing capacities to cater near term requirements; Kakinada project crucial for further growth

- DIVI's has 20% headroom in existing capacities which will drive growth in the near term. At the same time, there are two new capacities commercialized in 1QFY23 which will provide further impetus for growth in both generics as well as CS business.
- However, the progress on Kakinada project remains crucial from major capex perspective.

### We expect 8% earnings CAGR over FY22–24

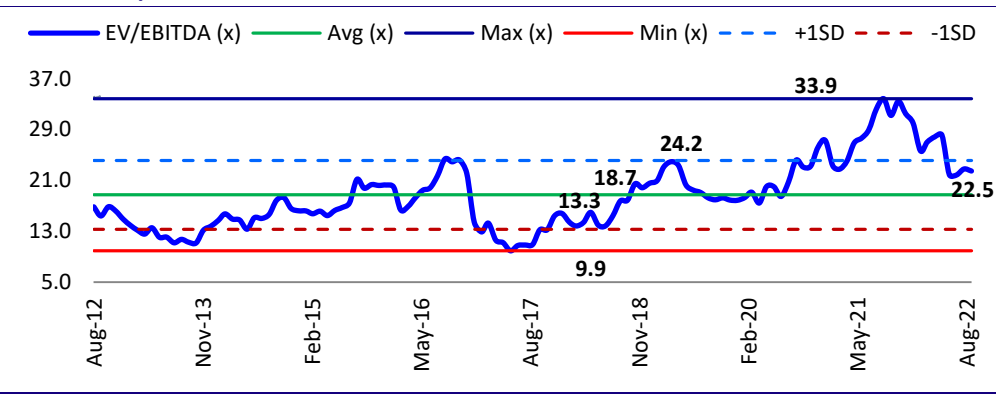
- We cut our EPS estimate by 6%/3% for FY23/FY24 to factor a) higher operational cost due to inflation linked increased raw material cost and elevated freight cost, and b) some moderation in CS segment.
- We continue to value DIVI at 33x 12M forward earnings to arrive at price target of INR4,340.
- While high base of past year may cap growth in earnings over near term, DIVI's remain on track to strengthen its skill-sets in newer technology like peptides, hipo conjugate drugs, contrast media products and also build commercial capability to tap business opportunities going forward. Maintain BUY

Exhibit 1: P/E chart



Source: MOFSL, Company, Bloomberg

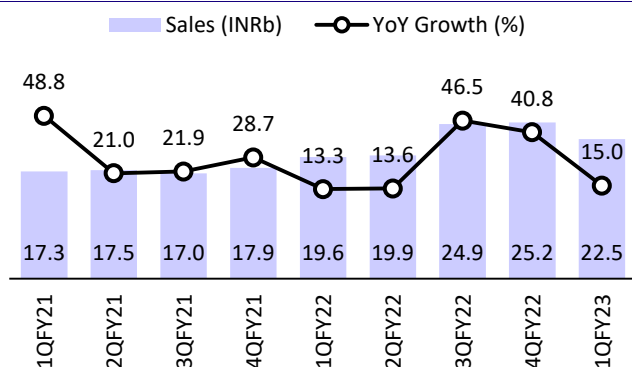
Exhibit 2: EV/EBITDA chart



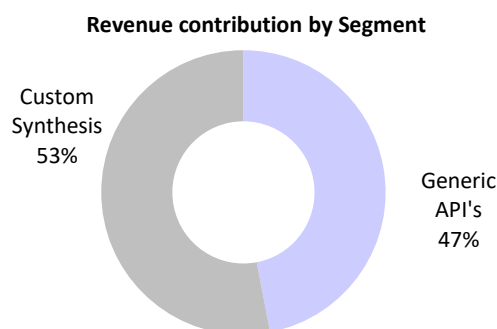
Source: MOFSL, Company, Bloomberg

## Story in charts

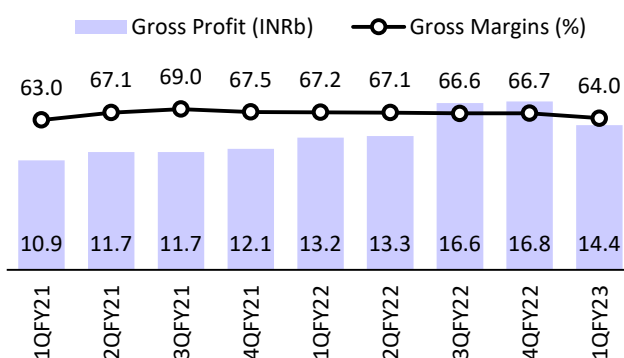
**Exhibit 3: Revenue growth moderates to 15% YoY**



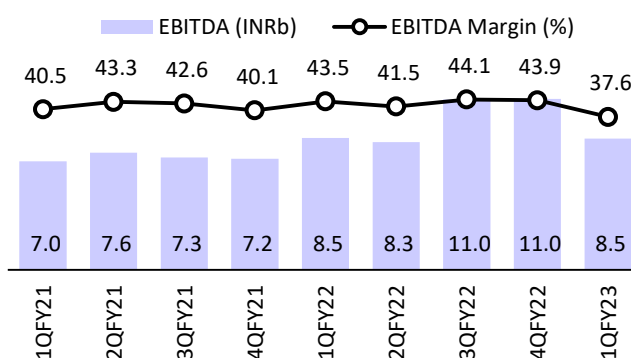
**Exhibit 4: CS segment contributes 53% to revenue in 1QFY23**



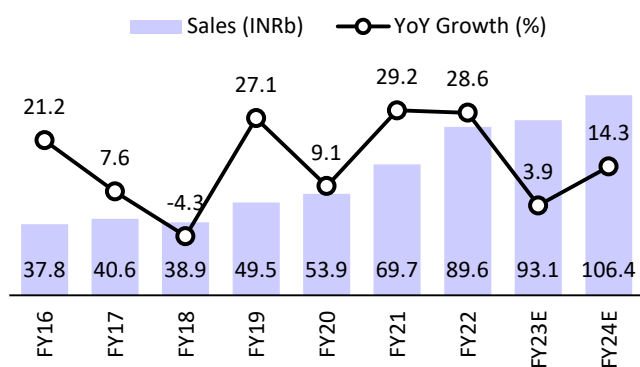
**Exhibit 5: Gross margin down 330bp YoY in 1QFY23**



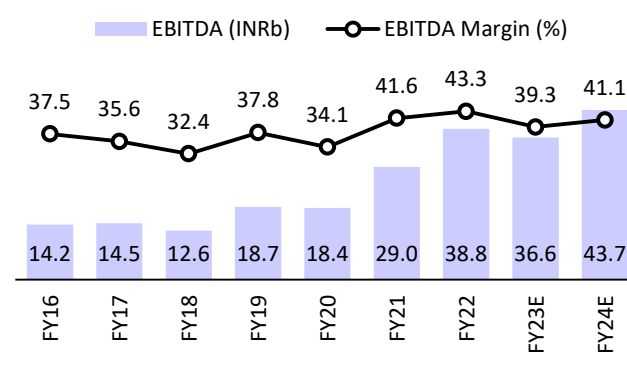
**Exhibit 6: EBITDA margin contracts 590bp YoY in 1QFY23**



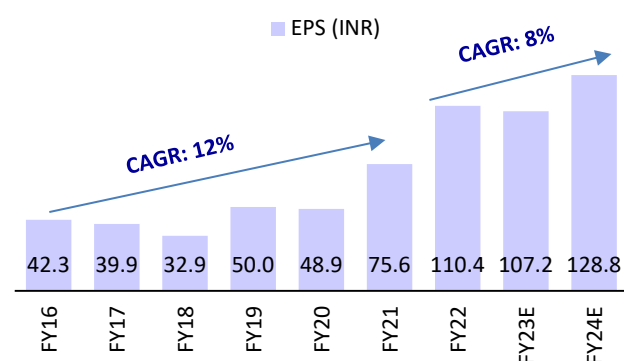
**Exhibit 7: Expect ~9% revenue CAGR over FY22–24**



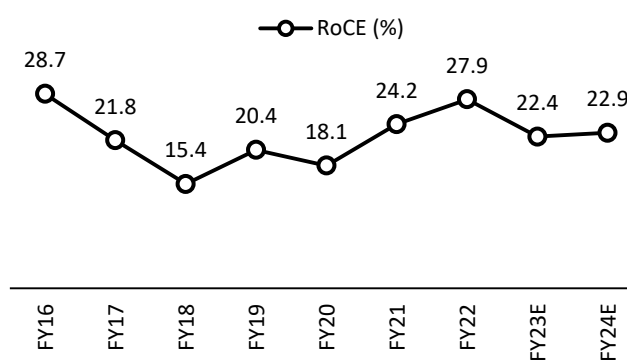
**Exhibit 8: Expect margin to contract 220bp over FY22–24**



**Exhibit 9: Expect 8% earnings CAGR over FY22–24**



**Exhibit 10: RoCE to moderate over FY22–24**



Source: Company, MOFSL

Source: Company, MOFSL

## Financials and valuations

Income Statement							(INR m)	
Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Total Income from Operations	40,643	38,915	49,463	53,944	69,694	89,598	93,109	1,06,382
Change (%)	7.6	-4.3	27.1	9.1	29.2	28.6	3.9	14.3
Total Expenditure	26,183	26,298	30,744	35,523	40,711	50,779	56,517	62,659
% of Sales	64.4	67.6	62.2	65.9	58.4	56.7	60.7	58.9
EBITDA	14,460	12,617	18,719	18,422	28,983	38,819	36,592	43,723
Margin (%)	35.6	32.4	37.8	34.1	41.6	43.3	39.3	41.1
Depreciation	1,233	1,425	1,689	1,862	2,556	3,115	3,240	3,319
EBIT	13,227	11,192	17,030	16,559	26,427	35,704	33,352	40,404
Int. and Finance Charges	23	13	35	61	9	8	0	0
Other Income	737	1,090	1,220	1,075	626	733	1,350	1,277
PBT bef. EO Exp.	13,942	12,269	18,215	17,573	27,044	36,429	34,702	41,681
EO Items	12	44	336	-621	-384	406	564	0
PBT after EO Exp.	13,953	12,313	18,551	16,952	26,660	36,835	35,266	41,681
Total Tax	3,349	3,543	5,023	4,429	6,818	7,231	6,348	7,502
Tax Rate (%)	24.0	28.8	27.1	26.1	25.6	19.6	18.0	18.0
Reported PAT	10,604	8,770	13,527	12,523	19,843	29,605	28,918	34,178
Adjusted PAT	10,595	8,739	13,282	12,991	20,062	29,303	28,453	34,178
Change (%)	-5.7	-17.5	52.0	-2.2	54.4	46.1	-2.9	20.1
Margin (%)	25.6	21.8	26.2	23.6	28.5	32.4	30.1	32.1

Balance Sheet							(INR m)	
Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23E	FY24E
Equity Share Capital	531	531	531	531	531	531	531	531
Total Reserves	53,043	58,717	69,041	72,568	92,415	1,16,751	1,36,730	1,60,315
Net Worth	53,574	59,248	69,572	73,099	92,946	1,17,282	1,37,261	1,60,846
Total Loans	357	631	1,056	389	4	0	0	0
Deferred Tax Liabilities	1,228	1,917	2,188	2,696	3,348	4,069	4,069	4,069
Capital Employed	55,160	61,796	72,816	76,184	96,298	1,21,351	1,41,330	1,64,915
Gross Block	17,940	23,735	26,339	35,143	46,919	56,246	60,505	67,157
Less: Accum. Deprn.	2,348	3,773	5,462	7,324	9,880	12,995	16,235	19,554
Net Fixed Assets	15,592	19,962	20,878	27,819	37,039	43,251	44,270	47,603
Capital WIP	4,436	1,198	4,919	9,197	7,106	4,699	1,440	5,788
Total Investments	16,307	18,893	19,456	9,714	0	720	720	720
Curr. Assets, Loans&Adv.	25,215	27,796	35,106	38,584	63,563	84,933	1,08,963	1,25,859
Inventory	13,199	13,507	17,723	18,639	21,452	28,286	30,194	33,475
Account Receivables	9,009	10,144	11,634	14,134	16,765	24,239	24,234	26,814
Cash and Bank Balance	787	1,125	1,153	1,226	21,560	28,189	50,152	60,561
Loans and Advances	2,220	3,021	4,597	4,586	3,786	4,219	4,384	5,009
Curr. Liability & Prov.	6,390	6,053	7,543	9,130	11,411	12,251	14,063	15,056
Account Payables	4,713	4,327	5,320	6,626	7,632	7,957	9,600	9,957
Other Current Liabilities	1,511	1,540	2,039	2,174	3,501	3,986	4,142	4,732
Provisions	166	186	185	329	278	309	321	366
Net Current Assets	18,825	21,743	27,563	29,455	52,153	72,681	94,901	1,10,804
Appl. of Funds	55,160	61,796	72,816	76,184	96,298	1,21,351	1,41,330	1,64,915

## Financials and valuations

<b>Ratios</b>	<b>(INR m)</b>							
<b>Y/E March</b>	<b>FY17</b>	<b>FY18</b>	<b>FY19</b>	<b>FY20</b>	<b>FY21</b>	<b>FY22</b>	<b>FY23E</b>	<b>FY24E</b>
<b>Basic (INR)</b>								
<b>EPS</b>	<b>39.9</b>	<b>32.9</b>	<b>50.0</b>	<b>48.9</b>	<b>75.6</b>	<b>110.4</b>	<b>107.2</b>	<b>128.8</b>
Cash EPS	44.6	38.3	56.4	56.0	85.2	122.1	119.4	141.3
BV/Share	201.8	223.2	262.1	275.4	350.1	441.8	517.1	605.9
DPS	10.0	10.0	10.0	16.0	20.0	29.9	26.5	33.1
Payout (%)	30.1	36.4	23.7	40.9	32.3	32.3	29.3	31.0
<b>Valuation (x)</b>								
P/E	93.4	113.2	74.5	76.2	49.3	33.8	34.8	29.0
Cash P/E	83.7	97.4	66.1	66.6	43.8	30.5	31.2	26.4
P/BV	18.5	16.7	14.2	13.5	10.6	8.4	7.2	6.2
EV/Sales	24.3	25.4	20.0	18.3	13.9	10.7	10.1	8.7
EV/EBITDA	68.4	78.4	52.9	53.7	33.4	24.8	25.7	21.2
Dividend Yield (%)	0.3	0.3	0.3	0.4	0.5	0.8	0.7	0.9
FCF per share	29.1	18.9	8.3	1.2	39.1	45.2	111.3	74.3
<b>Return Ratios (%)</b>								
RoE	22.0	15.5	20.6	18.2	24.2	27.9	22.4	22.9
RoCE	21.8	15.4	20.4	18.1	24.2	27.9	22.4	22.9
RoIC	30.3	21.5	28.3	23.7	31.8	36.9	30.9	35.5
<b>Working Capital Ratios</b>								
Asset Turnover (x)	0.7	0.6	0.7	0.7	0.7	0.7	0.7	0.6
Inventory (Days)	119	127	131	123	112	115	118	115
Debtor (Days)	81	95	86	96	88	99	95	92
Creditor (Days)	42	41	39	45	40	32	38	34
<b>Leverage Ratio (x)</b>								
Net Debt/Equity	-0.3	-0.3	-0.3	-0.1	-0.2	-0.25	-0.4	-0.4

<b>Cash Flow Statement</b>	<b>(INR m)</b>							
<b>Y/E March</b>	<b>FY17</b>	<b>FY18</b>	<b>FY19</b>	<b>FY20</b>	<b>FY21</b>	<b>FY22</b>	<b>FY23E</b>	<b>FY24E</b>
OP/(Loss) before Tax	13,953	12,313	18,551	16,952	26,660	36,835	35,266	41,681
Depreciation	1,233	1,425	1,689	1,862	2,556	3,115	3,240	3,319
Interest & Finance Charges	-32	-30	-40	-6	-564	4	-1,350	-1,277
Direct Taxes Paid	-3,017	-2,686	-4,844	-4,452	-6,443	-6,410	-6,348	-7,502
(Inc)/Dec in WC	-371	-2,191	-4,998	-2,183	-2,641	-13,705	-257	-5,494
<b>CF from Operations</b>	<b>11,766</b>	<b>8,831</b>	<b>10,357</b>	<b>12,174</b>	<b>19,569</b>	<b>19,840</b>	<b>30,551</b>	<b>30,727</b>
Others	-262	-1,073	-814	-14	-100	-722	0	0
<b>CF from Operating incl EO</b>	<b>11,504</b>	<b>7,759</b>	<b>9,543</b>	<b>12,160</b>	<b>19,469</b>	<b>19,118</b>	<b>30,551</b>	<b>30,727</b>
(Inc)/Dec in FA	-3,767	-2,738	-7,331	-11,829	-9,101	-7,132	-1,000	-11,001
<b>Free Cash Flow</b>	<b>7,737</b>	<b>5,021</b>	<b>2,213</b>	<b>331</b>	<b>10,368</b>	<b>11,986</b>	<b>29,551</b>	<b>19,726</b>
(Pur)/Sale of Investments	-8,289	-2,559	-291	10,336	9,740	-15,990	0	0
Others	659	513	767	658	112	1,173	1,350	1,277
<b>CF from Investments</b>	<b>-11,396</b>	<b>-4,784</b>	<b>-6,854</b>	<b>-835</b>	<b>751</b>	<b>-21,949</b>	<b>350</b>	<b>-9,724</b>
Inc/(Dec) in Debt	0	0	776	-612	-333	-4	0	0
Interest Paid	-23	-13	-35	-61	-9	-4	0	0
Dividend Paid	0	-3,192	-3,200	-10,241	0	-5,309	-8,476	-10,593
<b>CF from Fin. Activity</b>	<b>24</b>	<b>-3,142</b>	<b>-2,459</b>	<b>-10,914</b>	<b>-349</b>	<b>8,676</b>	<b>-8,938</b>	<b>-10,593</b>
<b>Inc/Dec of Cash</b>	<b>132</b>	<b>-167</b>	<b>230</b>	<b>411</b>	<b>19,871</b>	<b>5,844</b>	<b>21,963</b>	<b>10,409</b>
Opening Balance	734	787	1,124	1,153	1,227	21,560	28,189	50,152
<b>Closing Balance</b>	<b>866</b>	<b>620</b>	<b>1,354</b>	<b>1,564</b>	<b>21,097</b>	<b>27,405</b>	<b>50,152</b>	<b>60,561</b>
Forex and other adjustments	-79	504	-201	-337	463	784	0	0
<b>Total Cash &amp; Cash Eq</b>	<b>787</b>	<b>1,124</b>	<b>1,153</b>	<b>1,227</b>	<b>21,560</b>	<b>28,189</b>	<b>50,152</b>	<b>60,561</b>

## NOTES



Explanation of Investment Rating	
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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