Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Granules India Ltd

Plants Resuming Operations and Upcoming Product Launches

Pharmaceuticals	Sharekhan code: GRANULES

Reco/View: **Buy**	⇔	CMP: **Rs. 576**	Price Target: **Rs. 700**	⇔

↑ Upgrade ⇔ Maintain ↓ Downgrade

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral – Negative

What has changed in 3R MATRIX

	Old		New
RS		⇔	
RQ		⇔	
RV		⇔	

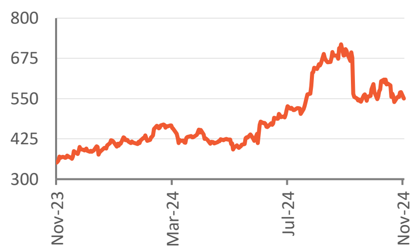
Company details

Market cap:	Rs. 12,168 cr
52-week high/low:	Rs. 724 / 348
NSE volume: (No of shares)	66.89 lakh
BSE code:	532482
NSE code:	GRANULES
Free float: (No of shares)	15.2 cr

Shareholding (%)

Promoters	38.9
FII	19.5
DII	14.9
Others	26.8

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	3.0	-8.5	43.6	67.4
Relative to Sensex	3.1	-11.2	31.0	41.8

Sharekhan Research, Bloomberg

Summary

- Revenues stood at Rs. 957 crore, falling 19% y-o-y and 18% q-o-q, falling 5% short of our estimates.
- EBITDA was Rs. 193 crore, down 9% y-o-y and 22% q-o-q, and 6% below our estimates. Margins stood at 20%, reflecting an 11bps decrease q-o-q, a 24 bps increase y-o-y, and 4 bps below our estimates.
- Company voluntarily halted production at the Gagillapur plant in September 2024 to reevaluate any potential risks related to observations from the USFDA. Production was subsequently resumed in a staggered manner in October.
- Company has meaningful products in its portfolio, like Metoprolol, Ibuprofen, etc., and backward integration of its key products, which will continue to increase margins. Hence, we maintain a Buy on the stock. At CMP, the stock trades at valuation of ~21x/18x its FY2026E/FY2027E earnings and arrive at a PT of Rs 700 per share.

Q2FY25 revenues stood at Rs. 957 crore, falling 19% y-o-y and 18% q-o-q, missing our estimates by 5%, primarily due to the voluntary pause in operations at the Gagillapur facility in response to the USFDA inspection. The company reported EBITDA of Rs. 193 crore, representing a 9% decrease y-o-y and a substantial 22% decline q-o-q, which is also 6% below our projections. Operating margins were recorded at 20%, indicating an 11 basis point (bps) reduction from the previous quarter, although there was a 24 bps increase as compared to the same period last year; nonetheless, this was still 4 bps lower than our estimates. Better margins were driven by increased sales of finished dosage forms (FD) and a strategic emphasis on higher-margin products within our formulations, alongside reduced raw material costs. Profit after tax (PAT) amounted to Rs. 97 crore, marking a 5% decline y-o-y and a 28% drop q-o-q, but this figure was 2% higher than our estimates, demonstrating some resilience despite the challenges faced.

Key positives

- Production at Gagillapur plant has resumed.
- Raw material prices have decreased.
- Four products have already received approval and are set to be launched.

Key negatives

- API and PFI segments continue to decline by 37% y-o-y and 33% y-o-y, while Geographically, Europe continues to decline and reported a fall of 38% y-o-y due to lower prices of Paracetamol price erosion led by stocking of inventory.

Management Commentary

- Company has recently launched Pantoprazole in the US.
- Robust margins for the quarter were fueled by sales of formulations and the product mix.
- Ongoing growth in share of formulations within the business.
- Received approvals for Trazodone HCl tablets and Glycopyrrolate oral solution.

Revision in estimates – Management has retained its guidance of higher formulation contribution led by value added products, which we have factored in, hence, there are no changes in estimates.

Our Call

Valuation – Maintain Buy Rating with a PT of Rs. 700: Granules has reported improved margins, driven by increased demand for value-added products. Management anticipates that the contribution from the Finished Dosage Form (FDF) segment will rise to 75%, fuelled by a higher share of value-added products and new product launches. In the near term, growth is expected to be led by the North American market, which is projected to grow by 20% in FY25E. The European market is expected to rebound next year as demand for paracetamol picks up starting in FY26E. Additionally, management has raised its EBITDA margin guidance to 22%, supported by several factors: 1) new product launches in high-value categories, 2) an increase in Phase 3 and 4 clinical trials from previous Phase 2 trials, 3) the commercialization of pilot projects for DCDA and PAP, and 4) A reduction in input costs. Therefore, we are maintaining our Buy rating on the stock. At CMP, the stock is trading at approximately 21x and 18x its FY2026E and FY2027E earnings of Rs. 27.91 and Rs. 31.14, respectively, resulting in a price target of Rs. 700 per share.

Key Risks

Delay in product approvals or the negative outcome of facility inspections by the USFDA can affect future earnings prospects.

Valuation (Consolidated) Rs cr

Particulars	FY2023	FY2024	FY2025E	FY2026E	FY27E
Net Sales	4512	4506	5092	5703	6388
EBIDTA	914	856	1069	1255	1405
EBITDA M (%)	20%	19%	21%	22%	22%
Adjusted PAT	517	405	547	676	755
EPS (Rs)	21.34	16.72	22.55	27.91	31.14
PER (x)	27	34	26	21	18
EV/EBITDA (x)	16	17	14	12	10
ROCE (%)	18%	14%	17%	18%	19%
RONW (%)	18%	13%	15%	16%	15%

Source: Company; Sharekhan estimates

Key conference call highlights

- The company anticipates reaching a run rate of approximately $1 billion within the next two months and plans to scale it up, in reference to the 2.5 billion capacity.
- Better margins can be attributed to the product mix within formulations, as more profitable products were sold.
- Company is making steady progress toward its R&D objectives, resulting in an expanding list of product approvals worldwide.
- Granules is also concentrating on fermentation and biocatalysis, aiming to develop environmentally friendly processes.
- Four products are currently being assessed and developed using fermentation technology.
- The company continues to supply products, with the launch quantities reflected in IMS data.
- It faced price erosion in the API and PFI segments due to decreased demand and elevated customer inventory levels.
- New launches from the GPI site are expected to mitigate the impact of the Gagillapur slowdown in Q2, which also has a minor spillover effect into Q3.
- Phase 2 of the formulation facility, which will add an additional 7.5 billion dosage capacity, is projected to be completed by Q4 FY25, with validation and commercialization activities set to commence in Q1 FY26.
- The company is developing CNS products with an emphasis on ADHD therapies at its Shantanuli facility.
- The company currently has four products under feasibility and development utilizing its fermentation technology.

Results (Consolidated) Rs cr

Particulars	Q2FY25	Q2FY24	Y-o-Y (%)	Q1FY25	Q-o-Q (%)
Revenue	**957**	**1,188**	**-19%**	**1,169**	**-18%**
Total Expenditure	763	977	-22%	921	-17%
Operating profit	**193**	**211**	**-9%**	**249**	**-22%**
Other Income	3	2	113%	2	58%
Interest	26	26	-1%	27	-5%
Depreciation	53	53	0%	53	36%
PBT	**118**	**135**	**-12%**	**171**	**-31%**
Tax	31	34	-8%	47	-33%
Adjusted PAT	**76**	**101**	**-24%**	**124**	**-39%**
EPS (Rs.)	4.01	4.22		5.56	
Margins (%)			**BPS**		**BPS**
OPM	20%	18%	240	21%	-106
NPM	8%	8%	-53	11%	-265

Source: Company; Sharekhan Research

Outlook and Valuation

■ Sector View – Input cost easing with companies focusing on complex product launches

Over the years, Indian pharmaceutical companies have established themselves as a dependable source for global peers. A confluence of other factors, including a focus on specialty/complex products in addition to emerging opportunities in the API space, would be key growth drivers over the long term. The sector is witnessing an easing of input costs – raw material, freight and power- expected to aid the sector in expanding margins. The sector is also witnessing an easing of price erosion followed by increasing contributions from new product launches. We believe the sector is in a sweet spot, where it is experiencing a healthy product mix and cost rationalisation, which increases operational profit of the companies. The sector is mainly a low-debt sector with increasing operational profit followed by experiencing advantages of a low tax rate due to its operations in the SEZ sector; hence, overall, we stay positive on the sector.

■ Company Outlook – Cost pressures to continue; to be partially offset by strong sales growth and productivity measures

Granules is a fully integrated pharmaceutical company present across the API-PFI-FD value chain. Over the long term, but growth levers are intact. As FY2025 could stage an improvement, regaining normalcy i.e., previous period margins and growth, apparently is likely over the medium term. Nevertheless, raw material and freight costs are easing q-o-q. Measures taken to reduce dependence on China and initiate a price hike across customers will help offset any concerns around China, leading to API price hikes. Positives continue to be commissioning of the MUPS block and a strong product pipeline across regions to support growth. We believe given the recent unfavourable change in product mix and an expected rise in R&D spending coupled with increased finance and depreciation costs, and continued price erosions seen in the formulations segment together with the increase in the share of regulated markets, the outlook on profitability weakens; nevertheless, strong sales growth coupled with productivity measures should help it offset its impact partially over the short to medium term.

■ Valuation – Maintain Buy Rating with a PT of Rs. 700

Granules has reported improved margins, driven by increased demand for value-added products. Management anticipates that the contribution from the Finished Dosage Form (FDF) segment will rise to 75%, fuelled by a higher share of value-added products and new product launches. In the near term, growth is expected to be led by the North American market, which is projected to grow by 20% in FY25E. The European market is expected to rebound next year as demand for paracetamol picks up starting in FY26E. Additionally, management has raised its EBITDA margin guidance to 22%, supported by several factors: 1) new product launches in high-value categories, 2) an increase in Phase 3 and 4 clinical trials from previous Phase 2 trials, 3) the commercialization of pilot projects for DCDA and PAP, and 4) A reduction in input costs. Therefore, we are maintaining our Buy rating on the stock. At CMP, the stock is trading at approximately 21x and 18x its FY2026E and FY2027E earnings of Rs. 27.91 and Rs. 31.14, respectively, resulting in a price target of Rs. 700 per share.

About company

Granules is a vertically integrated pharmaceutical company, headquartered in Hyderabad, India. The company manufactures Active Pharmaceutical Ingredients (APIs) – 29.7% of sales, Pharmaceutical Formulation Intermediates (PFIs) – 20.2% of sales and Finished Dosages (FDs) – 50.1% of sales and supplies them to both regulated and semi-regulated markets. The regulated markets constitute around 73% of revenue, LATAM accounts for 11%, and RoW markets constitute around 16% of revenue.

Investment theme

Granules is a fully integrated pharmaceutical company present across the API-PFI-FD value chain. Over a long-term period, the company's growth levers are intact, and this bodes well. However, in the near term, severe headwinds could substantially outweigh the financial performance. Though FY2023 could stage an improvement, but regaining normalcy i.e. previous period margins and growth, apparently is a challenge. As raw material prices are looking up, coupled with higher and firm logistics costs, the price increase is inevitable, though channel de-stocking across the segments could act as a dampener. Therefore, as markets open and Covid cases ease out, the business would evolve towards a new normal, and this could moderate the growth prospects. Though Granules is taking measures to reduce dependence on China and initiating a price hike across customers, these could take a while to be reflected in the financials, clearly pointing at near-term challenges. We believe the revival remains a key monitorable. However, positives such as the commissioning of the MUPS block and product pipeline across regions could support growth. We believe new product launches in the U.S., tapping new geographies, and augmented capacities will support the base business as well as the emerging business.

Key Risks

- Delays in product approvals or negative outcomes of facility inspections by the USFDA can affect future earnings prospects.
- Delay in product launches in the U.S.
- Adverse outcome of USFDA inspection at the manufacturing facility also poses a risk.

Additional Data

Key management personnel

Krishna Prasad Chigurupati	Chairman and Managing Director
Kandiraju Venkata Sitaramrao	Chief Executive Officer and Managing Director
Chaitanya Tummala	Company Secretary & Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Life Insurance Corp of India	4.26
2	FIL Ltd	3.65
3	Axis Asset Management Co Ltd/India	2.79
4	Vanguard Group Inc/The	2.18
5	Dimensional Fund Advisors LP	1.74
6	Blackrock Inc	1.41
7	Aditya Birla Sun Life Asset Manage	1.07
8	Tata Asset Management Pvt Ltd	0.94
9	Nippon Life India Asset Management	0.64
10	Edelweiss Asset Management Ltd	0.52

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/ weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

Sharekhan

by BNP PARIBAS

DISCLAIMER

Registration and Contact Details: Name of Research Analyst - Sharekhan Limited, Research Analyst Regn No.: INH000006183. CIN: - U99999MH1995PLC087498.

Registered Office: The Ruby, 18th Floor, 29 Senapati Bapat Marg, Dadar (West), Mumbai – 400 028, Maharashtra, INDIA. Tel: 022-6115000.

Correspondence/Administrative Office Address - Gigaplex IT Park, Unit No 1001, 10th Floor, Building No.9, TTC Industrial Area, Digha, Airoli-West, Navi Mumbai – 400708. Tel: 022 61169000 / 61150000, Fax No. 61169699.

Other registrations of Sharekhan Ltd.: SEBI Regn. Nos.: BSE / NSE (CASH / F&O / CD) / MCX - Commodity: INZ000171337; BSE – 748, NSE – 10733, MCX – 56125, DP: NSDL/CDSL-IN-DP-365-2018; PMS: INP000005786; Mutual Fund: ARN 20669 (date of initial registration: 03/07/2004, and valid till 02/07/2026); IRDAI Registered Corporate Agent (Composite) License No. CA0950, valid till June 13, 2027.

Compliance Officer: Ms. Binkle R. Oza; Tel: 022-62263303; email id: complianceofficer@sharekhan.com

For any complaints/grievance, email us at igc@sharekhan.com or you may even call Customer Service desk on - 022- 41523200/022-69920600.