



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 | ✗ | ↔ | ✓ |

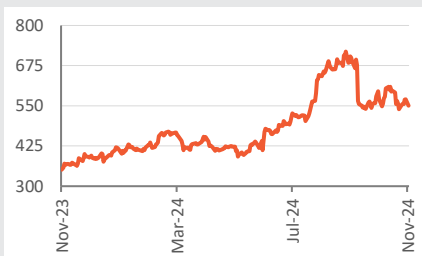
Company details

| | |
|-------------------------------|---------------|
| 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

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 | |

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 | FY2027E |
| 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

Sharekhan Limited, its analyst or dependant(s) of the analyst might be holding or having a position in the companies mentioned in the article.

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 deteriorating 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

DISCLAIMER

This information/document has been prepared by Sharekhan Ltd. (SHAREKHAN) and is intended for use only by the person or entity to which it is addressed to. This Document may contain confidential and/or privileged material and is not for any type of circulation and any review, retransmission, or any other use is strictly prohibited. This information/ document is subject to changes without prior notice.

Recommendation in reports based on technical and derivatives analysis is based on studying charts of a stock's price movement, trading volume, outstanding positions, as opposed to focusing on a company's fundamentals and as such, may not match with a report on a company's fundamentals. However, this would only apply for information/document focused on technical and derivatives research and shall not apply to reports/documents/information focused on fundamental research.

This information/document does not constitute an offer to sell or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. Though disseminated to all customers who are due to receive the same, not all customers may receive this report at the same time. SHAREKHAN will not treat recipients as customers by virtue of their receiving this information/report.

The information contained herein is obtained from publicly available data or other sources believed to be reliable and SHAREKHAN has not independently verified the accuracy and completeness of the said data and hence it should not be relied upon as such. While we would endeavour to update the information herein on reasonable basis, SHAREKHAN, its subsidiaries and associated companies, their directors and employees ("SHAREKHAN and affiliates") are under no obligation to update or keep the information current. Also, there may be regulatory, compliance, or other reasons that may prevent SHAREKHAN and affiliates from doing so. This document is prepared for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. Recipients of this report should also be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigations as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved) and should consult its own advisors to determine the merits and risks of such an investment. The investment discussed or views expressed may not be suitable for all investors. We do not undertake to advise you as to any change of our views. Affiliates of Sharekhan may have issued other recommendations/ reports that are inconsistent with and reach different conclusions from the information presented in this recommendations/report.

This information/recommendation/report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject SHAREKHAN and affiliates to any registration or licensing requirement within such jurisdiction. The securities described herein may or may not be eligible for sale in all jurisdictions or to certain category of investors. Persons in whose possession this document may come are required to inform themselves of and to observe such restriction.

The analyst certifies that the analyst might have dealt or traded directly or indirectly in securities of the company and that all the views expressed in this document accurately reflect his or her personal views about the subject company or companies and its or their securities and do not necessarily reflect those of SHAREKHAN. The analyst and SHAREKHAN further certifies that either he or his relatives or Sharekhan associates might have direct or indirect financial interest or might have actual or beneficial ownership of 1% or more in the securities of the company at the end of the month immediately preceding the date of publication of the research report. The analyst and SHAREKHAN encourages independence in research report/ material preparation and strives to minimize conflict in preparation of research report. The analyst and SHAREKHAN does not have any material conflict of interest or has not served as officer, director or employee or engaged in market making activity of the company. The analyst and SHAREKHAN has not been a part of the team which has managed or co-managed the public offerings of the company, and no part of the analyst's compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this document. Sharekhan Ltd or its associates or analysts have not received any compensation for investment banking, merchant banking, brokerage services or any compensation or other benefits from the subject company or from third party in the past twelve months in connection with the research report.

Either SHAREKHAN or its affiliates or its directors or employees / representatives / clients or their relatives may have position(s), make market, act as principal or engage in transactions of purchase or sell of securities, from time to time or may be materially interested in any of the securities or related securities referred to in this report and they may have used the information set forth herein before publication. SHAREKHAN may from time to time solicit from, or perform investment banking, or other services for, any company mentioned herein. Without limiting any of the foregoing, in no event shall SHAREKHAN, any of its affiliates or any third party involved in, or related to, computing or compiling the information have any liability for any damages of any kind.

Forward-looking statements (if any) are provided to allow potential investors the opportunity to understand management's beliefs and opinions in respect of the future so that they may use such beliefs and opinions as one factor in evaluating an investment. These statements are not a guarantee of future performance and undue reliance should not be placed on them. Such forward-looking statements necessarily involve known and unknown risks and uncertainties, which may cause actual performance and financial results in future periods to differ materially from any projections of future performance or result expressed or implied by such forward-looking statements. Sharekhan/its affiliates undertakes no obligation to update forward-looking statements if circumstances or management's estimates or opinions should change except as required by applicable securities laws. The reader/investors are cautioned not to place undue reliance on forward-looking statements and use their independent judgement before taking any investment decision.

Investment in securities market are subject to market risks, read all the related documents carefully before investing. The securities quoted are for illustration only and are not recommendatory. Registration granted by SEBI, and certification from NISM in no way guarantee performance of the intermediary or provide any assurance of returns to investors.

Client should read the Risk Disclosure Document issued by SEBI & relevant exchanges and the T&C on www.sharekhan.com

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.