Sharekhan
by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Update

Result Update

Divis Laboratories Ltd

Company set for continued growth

Pharmaceuticals	Sharekhan code: DIVISLAB

Reco/View: Buy	↔	CMP: Rs. 5,899	Price Target: Rs. 6,812	↑

↑ Upgrade ↔ Maintain ↓ Downgrade

Summary

- Divis Labs' revenue for the quarter amounted to Rs. 2,238 crore, marking a 17% y-o-y increase and a 6% q-o-q rise, which was 4% above estimates.
- EBITDA stood at Rs. 616 crore, reflecting a 29% y-o-y increase but a slight decline of 1% q-o-q, falling short of our expectations by 4%. Margins stood at 28%, indicating a 243 bps y-o-y improvement but a 184 bps q-o-q decrease.
- PAT reached Rs. 510 crore, showing a 47% increase y-o-y and a 19% q-o-q rise, exceeding our estimates by 15%.
- We observe a consistent increase across all key financial metrics, indicating a significant potential for stock. Therefore, we maintain BUY. Currently, at the CMP, the stock is priced at 70x the FY2026E EPS of Rs. 83.89 and 59x the FY2027E EPS of Rs. 100.30. Given the sustained growth in the custom synthesis business, we have established a PT of Rs. 6,812.

Divis Labs reported revenue of Rs. 2,238 crore in Q2FY2025, which represents a robust 17% y-o-y increase and a 6% q-o-q rise, exceeding our estimates by 4%. EBITDA for the quarter was recorded at Rs. 616 crore, reflecting a significant y-o-y growth of 29%, although it experienced a minor decline of 1% q-o-q, which fell short of our expectations by 4%. Profit margin for this quarter stood at 28%, demonstrating a substantial y-o-y improvement of 243 bps, despite a decrease of 184 bps q-o-q. Additionally, PAT reached Rs. 510 crore, marking an impressive 47% y-o-y increase and a 19% q-o-q rise, thereby surpassing our estimates by 15%.

Key positives

- The company holds a dominant market share in its key product categories.
- The company has achieved a notable increase in its market share for the molecules introduced over the past two to three years.
- The company is experiencing growing demand from both its existing and new customers within the custom synthesis market.

Key negatives

- The company is facing supply chain disruptions stemming from ongoing attacks on commercial vessels in the Red Sea, which have resulted in increased transit times from 45 days to 70 days.
- Global inflation is significantly impacting companies, creating pressure to make medicines more affordable.

Management Commentary

- The demand for solid-phase peptide synthesis is steadily increasing, leading the company to further expand its facilities.
- To manage inventory effectively, the company has taken a proactive approach that involves advancing shipments by 3-4 weeks, maintaining higher safety stock levels, and diversifying its supply sources whenever possible.
- The shipping timeframe has lengthened to approximately 70 days as a result of the need to reroute around Africa.
- Additionally, the company is experiencing pricing pressure in the generic markets, which poses a challenge faced across the entire industry.

Revision in estimates: Numbers were below our estimates due to the Red Sea crisis resulting in freight cost, price erosion pressure in API, and delays in commencing of new capacities in generic APIs due to uncertainty of USFDA inspection, which we have all factored in; hence, there is no revision in our estimates.

Our Call

Valuation – Maintain BUY with a revised PT of Rs. 6,812: Divis is poised for significant growth across several key areas, including the custom synthesis (CS) business, where there is an anticipated ramp-up in the production of Entresto and Rivoq. Additionally, the contrast media segment is expected to expand with increased production of Iopamidol and Iohexol, alongside the commercialisation of Gadolinium products. The company is also preparing for the commercialisation of GLP-1 in FY2026, which presents further growth potential. Furthermore, the generics business is set to benefit from loss of exclusivity (LOE) opportunities starting in 2026. In addition to these developments, there are promising prospects stemming from the Biosecure Act and the Kakinada project, among others. Given these factors, we believe Divis is exceptionally well-positioned to capitalise on these opportunities for expansion. As a result, we are raising our target price to Rs. 6,812. Currently, the stock is trading at 58x its estimated earnings per share (EPS) for FY2026, projected at Rs. 102.13, and 50x its estimated EPS for FY2027, projected at Rs. 117.45.

Key Risks

1) Adverse regulatory changes; 2) Unfavourable forex movements.

Valuation (Consolidated) Rs cr

Particulars	FY2023	FY2024	FY2025E	FY2026E	FY2027E
Net sales	7768	7845	9022	10826	13533
EBITDA	2368	2205	2752	3464	4466
EBITDA (%)	30%	28%	31%	32%	33%
PAT	1823	1600	2030	2598	3383
EPS (Rs)	68.70	60.30	76.60	98.05	127.67
PER (x)	86x	98x	77x	60x	46x
EV/EBITDA(x)	65x	70x	54x	43x	33x
ROCE (%)	15%	17%	19%	19%	20%
RONW (%)	12%	13%	16%	16%	17%

Source: Company; Sharekhan estimates

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. 1,56,600 cr
52-week high/low:	Rs. 6276/3350
NSE volume: (No of shares)	4.47 lakh
BSE code:	532488
NSE code:	DIVISLAB
Free float: (No of shares)	12.8 cr

Shareholding (%)

Promoters	51.9
FII	17.3
DII	21.0
Others	9.88

Price chart

Price performance

(%)	1m	3m	6m	12m
Absolute	-32.9	-15.7	5.8	17.2
Relative to Sensex	-26.1	-11.0	2.0	0.9

Sharekhan Research, Bloomberg

Key conference call highlights

- There is no specific guidance available regarding metrics such as revenue, earnings, or capital expenditures.
- Several generic products have submitted their NDAs and are currently awaiting approval from various regulatory authorities.
- Capital expenditure (Capex) expansion for the next year is anticipated to be slightly lower than this year's due to the brownfield nature of the expansion.
- Global inflation is significantly impacting companies, creating pressure to make medicines more affordable.
- The company is facing supply chain disruptions stemming from ongoing attacks on commercial vessels in the Red Sea, which have led to increased transit times from 45 days to 70 days.
- Despite experiencing volume-based growth, the generic business is not performing as anticipated due to pricing pressures.
- The company's future product pipeline is strong, with a variety of generic products progressing toward customer qualifications and regulatory approvals in the U.S. and Europe.
- The company has developed amino acids and protected amino acids, and it is now expanding into solid-phase and liquid-phase peptide synthesis to produce fragments for tetramers, octamers, and decamers, which are currently in the qualification process.
- The company is also working on developing generic products that are set to come off patent starting in 2026, with some already having filed NDAs and awaiting regulatory approvals.
- At Unit 3, the company is focused on qualifying regulatory products, although obtaining regulatory approvals is expected to take time.
- Initially, Unit 3 will concentrate on producing backward-integrated products to free up capacity in existing plants for regulatory products.

Results Rs cr

Particulars	Q2FY25	Q2FY24	YoY (%)	Q1FY25	QoQ (%)
Revenue	**2,338**	**1,909**	**22%**	**2,118**	**10%**
Total Expenditure	1,622	1,430	13%	1,496	8%
Operating profit	**716**	**479**	**49%**	**622**	**15%**
Other Income	106	86	23%	79	34%
Interest	1	1	0%	0	-
Depreciation	99	95	4%	97	36%
PBT	**722**	**469**	**54%**	**604**	**20%**
Tax	212	121	75%	174	22%
Adjusted PAT	**499**	**348**	**43%**	**430**	**16%**
EPS (Rs.)	18.7	10.76		17.58	
Margins (%)			**BPS**		**BPS**
OPM	31%	25%	553bps	29%	126bps
NPM	21%	18%	311bps	20%	103bps
Tax rate	29%	26%	356bps	29%	55bps

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 – of raw material, freight, and power, which are likely to aid the sector in expanding margins. The sector is also witnessing an easing of price erosion followed by increasing contribution from product launches. We believe that 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 the advantage of a low tax rate due to its operations in the SEZ sector; hence, overall, we stay positive on the sector.

■ **Company outlook - Company Outlook – Earnings prospects to stay weak in the near to medium term**

Divis' long-term growth opportunities are robust and the company is well-placed to capitalise on the same. Similarly, growth levers in the generic API space are also promising in the long term, though concerns in the near term could drag growth. The hunt by global companies for alternative procurement sources for API/intermediates drugs is expected to benefit API-centric players such as Divis. New areas of contrast media manufacturing and focus on molecules going off patent in the next two years offering an addressable market size of USD20 billion, could fuel growth going ahead. Consequently, the company has completed a substantial capacity expansion plan across its facilities for both the API as well as custom synthesis business. With expanded capacities going onstream, Divis could be best placed to cater to increased demand. Moreover, the company has entered the contract media manufacturing space recently, which is growing annually by 10-15%. With a substantial global addressable market size of USD4-6 billion, this space has the potential to provide considerable growth opportunities. Moreover, management has defined its six pillars or focus areas, which are expected to propel growth in the times to come. However, escalating costs with lower revenue could lead to margin pressures in the near term, though backward integration and expanded capacities could be long-term levers.

■ **Valuation - Maintain BUY with a revised PT of Rs. 6,812**

Divis is poised for significant growth across several key areas, including the custom synthesis (CS) business, where there is an anticipated ramp-up in the production of Entresto and Rivoq. Additionally, the contrast media segment is expected to expand with increased production of Iopamidol and Iohexol, alongside the commercialisation of Gadolinium products. The company is also preparing for the commercialisation of GLP-1 in FY2026, which presents further growth potential. Furthermore, the generics business is set to benefit from loss of exclusivity (LOE) opportunities starting in 2026. In addition to these developments, there are promising prospects stemming from the Biosecure Act and the Kakinada project, among others. Given these factors, we believe Divis is exceptionally well-positioned to capitalise on these opportunities for expansion. As a result, we are raising our target price to Rs. 6,812. Currently, the stock is trading at 58x its estimated earnings per share (EPS) for FY2026, projected at Rs. 102.13, and 50x its estimated EPS for FY2027, projected at Rs. 117.45.

About company

Divis, based in Hyderabad, India, has two manufacturing units and is among the top pharmaceutical companies in India. Divis is the leading manufacturer of APIs, intermediates, and registered starting materials offering high-quality products with the highest level of compliance and integrity to over 95 countries. Advanced manufacturing facilities, both in Hyderabad and Vizag, have been inspected multiple times by USFDA, EU GMP (U.K., Slovenia, German, and Irish authorities), HEALTH CANADA, TGA, ANVISA, COFEPRIS, PMDA, and MFDS health authorities.

Investment theme

Divis' long-term growth opportunities are intact and the company is well placed to capitalise on the same. Immense opportunities lie ahead in the contract research and manufacturing space (CRAMS). Similarly, growth levers in the generic API space are promising. With expanded capacities having been ready while new product opportunities are yet to fully commercialise fully untill FY2025, Divis's business prosepcts weaken over the short–medium term.

Key Risks

1) Adverse regulatory change

2) Regulatory compliance risk

3) Forex volatility

Additional Data

Key management personnel

Dr. Murali K. Divi	Managing Director
Kishore Babu	CFO
Dr. Kiran S. Divi	Wholetime Director and CEO

Source: Company

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	SBI Funds Management	6.70
2	Life Insurance Corp India	5.53
3	Axis Asset Management	3.06
4	Government Pension Fund Global	1.20

Source: BSE

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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

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by BNP PARIBAS

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