

OAI status for Gagillapur; but correction overdone...

About the stock: Granules is a large-scale vertically integrated company that manufactures API, intermediates and finished dosages. It owns eight manufacturing facilities catering mainly for export markets (~94% of sales).

- ANDA and Dossiers filed and approved- US- 83, Europe- 12, Canada- 7, UK- 2, Others – 15.
- Top five products (Paracetamol, Ibuprofen, Metformin, Methocarbamol, Guaifenesin) contributed 65% to H1FY25 revenues (across segments).
- Revenue mix Q2FY25: Formulations (FD) - 77%, API - 15%, PFI - 8%.

Investment Rationale

- Granules India Q2FY25- Voluntary production stoppage hurt numbers- Revenues de-grew ~19% YoY to ₹ 967 crore, due to voluntary stoppage at the Gagillapur facility to reassess the potential risk on account of the USFDA observations. On segmental front, Formulations grew 1% YoY to ₹ 749 crore, driven by new products in the US and other geographies. APIs (APIs + PFIs), on the other hand declined ~51% to ₹ 218 crore led primarily by higher customer inventory and price erosion. Gross Profit, however was down just 2% YoY to ₹ 599 crore (margins stood at 62%, up 1036 bps YoY) driven by better product mix (high-value formulations sales) and prioritized sales of high-margin products within formulations. EBITDA de-grew ~5% YoY to ₹ 203 crore due to lower sales and higher fixed overheads and EBITDA margins stood at 21% (313 bps improvement).
- Proactive measures; future looks promising- As per management, 45 days of production was hampered at Gagillapur facility and the production was resumed in October. Currently, ~80% of the remediation is complete and the full completion is expected by Q4 given that the USFDA classification status is OAI (warning letter almost eminent). Hence Q3 and Q4 numbers are also likely to get impacted. The Gagillapur facility is the largest for Granules but it is already operating at ~90% capacity and the company over the years has added other facilities as well. It plans to file 6-7 products in the US every year. The company is also focusing on Oncology as a segment with dedicated API and formulations block at Vizag. It has already announced an aggressive Capex which includes manufacturing of Paracetamol and Metformin KSMs and intermediates via green route. We believe the quest for transformation to high value formulations and increasing the product basket with significant focus on vertical integration to continue to drive investor's interest. We believe the negativity is fully priced in.

Rating and Target price

- We value Granules India at 24x FY26E EPS of ₹ 27.2 with a target of ₹ 650. Downwards revision incorporates reduction in estimates post OAI.



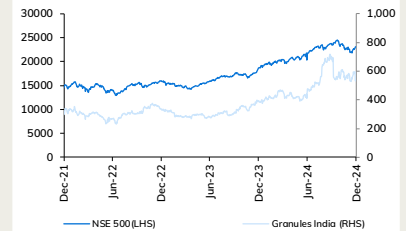
Particulars

Particular	Amount
Market Capitalisation	₹ 13068 crore
Debt (FY24)	₹ 1315 crore
Cash (FY24)	₹ 381 crore
EV	₹ 14002 crore
52 week H/L	724/365
Equity capital	₹ 24.2 crore
Face value	₹ 1

Shareholding pattern

(in %)	Dec-23	Mar-24	Jun-24	Sep-24
Promoters	42.0	42.0	38.9	38.9
FII	18.8	19.6	20.4	19.5
DII	10.2	10.7	14.1	14.9
Others	29.1	27.8	26.6	26.8

Price Chart



Key risks

- (i) Higher than expected remediation cost
- (ii) Pricing pressure in the regulated markets especially the US

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Key Financial Summary

Key Financials ₹ Crore)	FY20	FY21	FY22	FY23	3 year CAGR (FY20-23)	FY24	FY25E	FY26E	2 year CAGR (FY24-26E)
Revenues	2598.6	3237.5	3764.9	4511.4	20.2	4506.4	4541.3	5208.9	7.5
EBITDA	525.3	853.6	722.2	913.3	20.2	856.0	906.7	1173.5	17.1
EBITDA Margins (%)	20.2	26.4	19.2	20.2		19.0	20.0	22.5	
Net Profit	309.9	549.5	412.8	516.1	18.5	405.3	455.9	658.1	27.4
EPS (Adjusted)	12.7	22.7	17.1	21.3		16.7	18.8	27.2	
PE (x)	39.0	23.8	31.7	25.3		32.2	28.7	19.9	
EV to EBITDA (x)	26.0	16.0	19.4	15.2		16.4	15.6	11.8	
RoCE (%)	15.2	24.0	15.6	18.5		14.3	14.9	18.9	
RoE (%)	16.7	25.3	16.0	18.2		12.6	13.3	16.3	

Exhibit 1: Quarterly Summary

(₹ crore)	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24	Q3FY24	Q4FY24	Q1FY25	Q2FY25	YoY (%)	QoQ (%)
Net Sales	888.3	996.8	1030.0	1019.6	1150.7	1145.6	1195.5	985.5	1189.5	1155.6	1175.7	1179.9	966.6	-18.7	-18.1
Raw Material Expenses	436.6	531.9	526.0	513.5	578.5	591.8	623.5	479.2	575.1	497.3	469.6	484.4	367.2	-36.2	-24.2
% of Revenue	49.1	53.4	51.1	50.4	50.3	51.7	52.2	48.6	48.3	43.0	39.9	41.1	38.0	-1036 bps	-307 bps
Gross Profit	451.7	464.8	503.9	506.0	572.2	553.9	572.0	506.3	614.4	658.3	706.1	695.5	599.4	-2.4	-13.8
Gross Profit Margin (%)	50.9	46.6	48.9	49.6	49.7	48.3	47.8	51.4	51.7	57.0	60.1	58.9	62.0	1036 bps	307 bps
Employee Expenses	92.5	105.3	108.2	108.7	117.7	119.2	126.7	140.3	148.8	157.0	151.7	163.6	159.4	7.1	-2.6
% of Revenue	10.4	10.6	10.5	10.7	10.2	10.4	10.6	14.2	12.5	13.6	12.9	13.9	16.5	398 bps	263 bps
Other Expenditure	208.0	185.8	203.1	185.8	211.6	203.9	217.3	229.2	252.6	250.8	298.8	272.5	236.7	-6.3	-13.2
% of Revenue	23.4	18.6	19.7	18.2	18.4	17.8	18.2	23.3	21.2	21.7	25.4	23.1	24.5	325 bps	138 bps
Total Expenditure	737.2	823.0	837.3	808.1	907.8	914.8	967.4	848.7	976.5	905.1	920.1	920.6	763.3	-21.8	-17.1
% of Revenue	83.0	82.6	81.3	79.3	78.9	79.9	80.9	86.1	82.1	78.3	78.3	78.0	79.0	-313 bps	94 bps
EBITDA	151.2	173.7	192.7	211.5	242.9	230.8	228.1	136.8	213.0	250.5	255.6	259.3	203.3	-4.5	-21.6
EBITDA Margin (%)	17.0	17.4	18.7	20.7	21.1	20.1	19.1	13.9	17.9	21.7	21.7	22.0	21.0	313 bps	-94 bps
Depreciation	39.8	39.2	40.2	43.4	44.1	48.4	48.7	49.2	52.5	52.4	53.2	52.9	52.5	0.0	-0.7
Interest	5.5	4.6	6.4	6.9	13.2	17.0	18.8	22.5	26.0	28.6	28.8	27.0	25.7	-1.1	-5.0
Other Income	4.4	4.9	4.0	4.7	4.8	0.9	3.4	0.3	1.5	0.7	1.9	2.1	3.3	112.7	57.7
Less: Exceptional Items	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
PBT	110.2	134.8	150.1	165.9	190.4	166.4	164.0	65.5	136.0	170.1	175.6	181.5	128.4	-5.6	-29.3
Total Tax	29.6	33.9	39.1	38.3	45.3	42.6	44.4	17.6	33.9	44.4	46.0	46.8	31.1	-8.1	-33.4
Tax rate (%)	26.8	25.2	26.1	23.1	23.8	25.6	27.1	26.9	24.9	26.1	26.2	25.8	24.3	-66 bps	-152 bps
PAT before MI	80.7	100.9	111.0	127.6	145.1	123.8	119.6	47.9	102.1	125.7	129.6	134.7	97.2	-4.8	-27.8
Minority Interest	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0		
Adjusted PAT	80.7	100.9	111.0	127.6	145.1	123.8	119.6	47.9	102.1	125.7	129.6	134.6	97.2	-4.8	-27.8
PAT Margin (%)	9.1	10.1	10.8	12.5	12.6	10.8	10.0	4.9	8.6	10.9	11.0	11.4	10.1	147 bps	-135 bps
EPS (Rs)	3.3	4.1	4.5	5.1	5.9	5.0	4.9	2.0	4.2	5.2	5.4	5.6	4.0		

Q2FY25 Results / Conference call highlights

- Company expects near future growth from new product launches from GPAC site in the US market, especially the CNS and ADHD segment and finished dosage sales in Europe.
- Company at present has 17 ANDAs in the US and four applications in Europe and eight applications in rest of the world under review for approval whereas three approvals are pending from Gagillapur facility.
- It has started dispatches from the Gagillapur facility from October onwards.
- Company has onboarded third party consultant for resolving issues related to cross-contamination, data management, and investigational studies. The company expects additional burden of \$2 million on other expenses for the same.
- Granules has seen some easing of inventory levels related to paracetamol and expects normalcy in the PFI/API business from Q4FY25 onwards.
- Granules expects to launch 4 new products in second half in the US market.
- Company's is focusing its R&D on fermentation and Bio-Catalysis.
- Company is doing better than expectation on Metoprolol succinate.
- Granules has completed integration for manufacturing of Pantoprazole with the receipt of API approval
- Granules new formulations facility at Genome Valley have been commissioned with Phase 1 capacity of 2.5 billion doses and commercial dispatches of monograph products have commenced.
- Overall impact due to voluntary shutdown- Revenues- ~₹ 200 crore; Profit- ₹ 50-60 crore.

Financial Tables

Exhibit 1: Profit and loss statement					₹ crore
(Year-end March)	FY23	FY24	FY25E	FY26E	
Total Operating Income	4,511.4	4,506.4	4,541.3	5,208.9	
Growth (%)	19.8	-0.1	0.8	14.7	
Raw Material Expenses	2,307.3	2,021.3	1,821.0	2,160.2	
Gross Profit	2,204.1	2,485.1	2,720.3	3,048.8	
Gross Profit Margins (%)	48.9	55.1	59.9	58.5	
Employee Expenses	472.2	597.9	718.1	781.3	
Other Expenditure	818.6	1,031.3	1,095.6	1,093.9	
Total Operating Expenditure	3,598.1	3,650.4	3,634.7	4,035.4	
EBITDA	913.3	856.0	906.7	1,173.5	
Growth (%)	26.5	-6.3	5.9	29.4	
Interest	55.9	105.8	104.0	86.2	
Depreciation	184.5	207.3	210.4	224.1	
Other Income	13.8	4.4	13.4	26.0	
PBT before Exceptional Item:	686.7	547.2	605.6	889.3	
Less: Exceptional Items	0.0	0.0	0.0	0.0	
PBT after Exceptional Items	686.7	547.2	605.6	889.3	
Total Tax	170.6	141.9	149.7	231.2	
PAT before MI	516.1	405.3	455.9	658.1	
PAT	516.1	405.3	455.9	658.1	
Growth (%)	25.0	-21.5	12.5	44.4	
EPS (Adjusted)	21.3	16.7	18.8	27.2	

Source: Company, ICICI Direct Research

Exhibit 2: Cash flow statement					₹ crore
(Year-end March)	FY23	FY24	FY25E	FY26E	
Profit/(Loss) after taxation	511.3	356.9	455.9	658.1	
Add: Depreciation & Amortization	184.5	207.3	210.4	224.1	
Net Increase in Current Assets	-119.5	-242.5	127.5	-198.7	
Net Increase in Current Liabilities	109.2	-3.9	-89.1	101.1	
Others	53.2	121.5	104.0	86.2	
CF from Operating activities	738.7	439.4	808.7	870.7	
(Purchase)/Sale of Fixed Assets	-410.7	-378.8	-600.7	-400.0	
Investments	203.5	15.9	-0.1	0.0	
Others	15.8	2.8	-24.0	-3.8	
CF from Investing activities	-191.4	-360.2	-624.8	-403.8	
(inc)/Dec in Loan	-60.0	-113.0	2.1	-240.0	
Dividend & Dividend tax	-18.6	-36.3	-36.3	-36.3	
Other	-361.6	157.0	-104.0	-86.2	
CF from Financing activities	-440.3	7.7	-138.2	-362.5	
Net Cash Flow	107.1	89.5	-172.3	104.5	
Cash and Cash Equivalent	184.7	291.6	381.1	208.8	
Cash	291.8	381.1	208.8	313.3	
Free Cash Flow	328.1	60.6	208.0	470.7	

Source: Company, ICICI Direct Research

Exhibit 3: Balance Sheet					₹ crore
(Year-end March)	FY23	FY24	FY25E	FY26E	
Equity Capital	24.2	24.2	24.2	24.2	
Reserve and Surplus	2,810.7	3,201.3	3,403.0	4,024.8	
Total Shareholders funds	2,834.9	3,225.5	3,427.2	4,049.1	
Minority Interest	0.0	0.0	0.0	0.0	
Total Debt	1,136.2	1,315.1	1,317.2	1,077.2	
Net Deferred Tax Liability	11.3	-14.0	-19.6	-20.0	
Long-Term Provisions	0.0	0.0	0.0	0.0	
Other Non Current Liabilities	29.3	37.9	44.0	44.8	
Source of Funds	4,011.6	4,564.5	4,768.8	5,151.1	
Gross Block - Fixed Assets	3,015.9	3,408.0	3,859.8	4,109.8	
Accumulated Depreciation	1,105.1	1,312.4	1,522.9	1,746.9	
Net Block	1,910.8	2,095.6	2,336.9	2,362.9	
Capital WIP	239.3	271.7	420.6	570.6	
Fixed Assets	2,150.1	2,367.3	2,757.6	2,933.5	
Investments	21.2	21.5	21.6	21.6	
Other non-Current Assets	162.6	195.1	219.7	224.0	
Inventory	1,149.4	1,300.5	1,395.4	1,035.7	
Debtors	948.5	985.8	726.7	1,279.7	
Other Current Assets	184.6	232.5	269.1	274.6	
Cash	291.6	381.1	208.8	313.3	
Total Current Assets	2,574.2	2,899.9	2,600.1	2,903.3	
Creditors	782.1	749.5	635.1	732.4	
Provisions	14.6	11.8	11.8	12.1	
Other Current Liabilities	99.8	158.0	183.3	186.9	
Total Current Liabilities	896.5	919.4	830.3	931.4	
Net Current Assets	1,677.6	1,980.6	1,769.9	1,972.0	
Application of Funds	4,011.6	4,564.5	4,768.8	5,151.1	

Source: Company, ICICI Direct Research

Exhibit 4: Key ratios				
(Year-end March)	FY23	FY24	FY25E	FY26E
Per share data (₹)				
Reported EPS	21.3	16.7	18.8	27.2
Cash EPS	27.4	23.8	26.0	35.0
BV per share	117.1	133.3	141.6	167.3
Cash per Share	12.0	15.7	8.6	12.9
Dividend per share	1.5	1.5	1.5	1.5
Operating Ratios (%)				
Gross Profit Margins	48.9	55.1	59.9	58.5
EBITDA margins	20.2	19.0	20.0	22.5
PAT Margins	11.4	9.0	10.0	12.6
Cash Conversion Cycle	135	179	211	141
Asset Turnover	1.5	1.3	1.2	1.3
EBITDA conversion Rate	80.9	51.3	89.2	74.2
Return Ratios (%)				
RoE	18.2	12.6	13.3	16.3
RoCE	18.5	14.3	14.9	18.9
RoIC	20.9	16.6	16.8	22.3
Valuation Ratios (x)				
P/E	25.3	32.2	28.7	19.9
EV / EBITDA	15.2	16.4	15.6	11.8
EV / Net Sales	3.1	3.1	3.1	2.7
Market Cap / Sales	2.9	2.9	2.9	2.5
Price to Book Value	4.6	4.1	3.8	3.2
Solvency Ratios				
Debt / EBITDA	1.2	1.5	1.5	0.9
Debt / Equity	0.4	0.4	0.4	0.3
Current Ratio	2.5	2.7	2.9	2.8
Quick Ratio	1.3	1.3	1.2	1.7
Inventory days	182	235	280	175
Debtor days	77	80	58	90
Creditor days	124	135	127	124
Long term debt/Equity	0.1	0.1	0.0	0.1

Source: Company, ICICI Direct Research

ANALYST CERTIFICATION

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