Sharekhan by BNP PARIBAS

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Stock Update

Result Update

Aurobindo Pharma Ltd

Eugia unit III WL to not hit financials much

Pharmaceuticals	Sharekhan code: AUROPHARMA

Reco/View: Hold ↑	CMP: Rs. 1,502	Price Target: Rs. 1,663 ↑

↑ 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		↔	

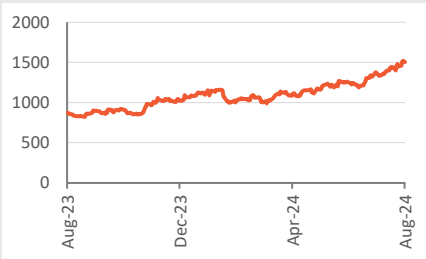
Company details

Market cap:	Rs. 61,497 cr
52-week high/low:	Rs. 1,177 / 443
NSE volume: (No of shares)	0.2 lakh
BSE code:	524804
NSE code:	AUROPHARMA
Free float: (No of shares)	28.1 cr

Shareholding (%)

Promoters	51.8
FII	1.0
DII	17.9
Others	29.3

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	9.5	29.5	46.3	72.0
Relative to Sensex	9.7	20.1	33.8	49.1

Sharekhan Research, Bloomberg

Summary

- Q1 numbers were in-line on all fronts, where sales grew by 10.5% y-o-y to Rs 7567 crore (0.5% above our estimates), EBITDA grew by 40% y-o-y to Rs. 1,658 crore (1.8% above our estimates) and adjusted PAT grew by 84% y-o-y to Rs. 907 crore (-0.8% below our estimates).
- Surge in sales was led by a 25% y-o-y growth in the US (CC sales of $ 426 million), followed by a 27% y-o-y growth in the Emerging business (CC sales of $85 million).
- Healthy product mix owing to growth across geographies drove up gross margins by 530 bps y-o-y to 58.8% and subsequently EBITDA margin rose by 460 bps to 21.4% in Q1FY2025.
- We believe Eugia warning letter would have no impact on injectable sales and no pricing pressure in Oral solids to spurt US growth, hence we upgrade our EPS by 7% and 15% for FY25E and FY26E respectively. Thus we upgrade our recommendation to Hold. At CMP, the stock trades at a premium valuation of ~22.6x/19x its FY2025E/FY2026E EPS, we would like to allot a P/E of 21x to arrive at a price target of Rs. 1663 (earlier PT 1014).

Q1FY25 numbers were in-line set on all fronts. Revenues rose 9.8% y-o-y to Rs. 7457 crore, led by a stronger-than-anticipated growth in all markets like the US sales which reported a 13% growth at Rs. 3,555 crore, driven by stability in price erosion in oral solids and product launches, rise in specialty and Injectables sales to $102 million (24% of US sales) and gRevlimid sales. In CC terms, sales fell 1% due to lower supplies from the Eugia-III unit. The company incurred a $2 million remediation costs over and above $9 million cost incurred in 4QFY24. Europe too continued to grow by 7% y-o-y to Rs 1982 crore and Euro 221 million led by new product launches and deeper penetration into newer geographies. The healthy product mix resulted in EBITDA growth of 41.5% y-o-y to Rs. 1619 crore and a 460 bps increase in EBITDA margin to 21.4%. Healthy operations led to PAT growth of 61% y-o-y after adjusting for forex. Going forward, key triggers to watch would be 1) Pick-up in sales of Pen G, 2) growth in Eugia injectables sales and 3) commercialization of Chinese unit 4) commission of Pen G sales and 5) Signing of a letter of intent with MSD for CMO. Company's Eugia unit-3, which was under an OAI has received a warning letter (WL). There are 20+ ANDAs which were expected to be filed from this unit can be shifted to USFDA approved plant in Vizag. As the WL does not possess a material risk, we upgrade our recommendation to Hold.

Key positives

- Margins were above estimates where gross and EBITDA margins stood at 58.8% and 21.4%, respectively.
- European CC revenue was highest-ever at Euro 221 million.

Key negatives

- Sales & PAT all lagged our estimates by 0.5% and -0.8%, respectively.
- US sales in CC terms were lower at $ 426 million due to supplies that got hit from the Eugia plant.

Management Commentary

- Eugia unit-3 has 20 pending (mostly injectables) ANDAs, which constitute 20% of company's total pending ANDAs, Eugia III is one of the most important facilities for ARBP with respect to new launches.
- About $40 million of launches were scheduled from this facility over FY2025-26E, which will now be delayed. Back-up facility to Eugia III, ARBP's Vizag injectable plant, is expected to go live from H1FY25E.
- Vizag facility has a footprint of seven lines. Capacities are fungible to some extent. ARBP has filed two products from the Vizag plant and expects a USFDA inspection in the coming quarters.

Revision in estimates – The company has indicated of no pricing pressure in the oral solids and Eugia sales to resume swiftly from Q2FY25E, hence we have upgraded our EPS estimates by 7% and 15% for FY25E and FY26E to Rs 66 and Rs 79 per share respectively.

Our Call

Valuation – Upgrade to Hold with a revised PT of Rs. 1,663: Q1FY25 numbers were in-line in Q1FY25 primarily driven by lower sales in US which offset growth in the European and growth markets. During the quarter, the company incurred a hit of lower supplies from the Eugia unit hurting lower US sales. We believe the company to report EBITDA Margin of 22% by FY26E driven by double digit growth rate ex of US, through Pen-G plant commission and benign RM cost. However, Eugia's unit-3 would lead to lower injectable and specialty sales. The company's unit 3 which was under OAI has received a WL. There are 20+ ANDAs which were expected to be filed from this unit can be shifted to USFDA approved plant in Vizag. As the WL does not pose a material risk to the company, hence we upgrade our recommendation to Hold. At CMP, the stock trades at a PE of 22.6x and 19x its FY25E and FY26E EPS and we would like to ascribe a PE of 21x to arrive at a PT of Rs 1663 (earlier Rs 1014).

Key Risks

Delay in the resolution of USFDA issues and product approvals; change in the regulatory landscape; and negative outcome of key facility inspection by the USFDA can affect earnings prospects.

Valuation (Consolidated) Rs cr

Particulars	FY2022	FY2023	FY2024	FY2025E	FY2026E
Total Income	23455.5	24855.4	28704.5	32096.0	35611.2
Operating profits	4386.8	3758.2	5545.6	6740.2	8012.5
OPM (%)	18.7	15.1	19.3	21.0	22.5
Adj. PAT	2737.5	1978.8	3084.6	3901.9	4641.0
EPS (Rs)	46.7	33.8	52.6	66.6	79.2
PER (x)	32.1	44.5	28.5	22.6	19.0
EV/Ebidta (x)	19.8	23.2	12.6	9.7	7.4
P/BV (x)	3.6	3.3	2.9	2.6	2.3
ROCE (%)	12.9	9.3	13.4	15.2	16.1
RONW (%)	11.8	7.7	10.9	12.3	13.0

Source: Company; Sharekhan estimates

Q1FY2025 Conference Call Highlights

- **US (ex-Puerto Rico) (48% of sales):** US sales stood at $426 million (+11% y-o-y, -1% q-o-q). Eugia revenues in the US, which includes generic injectables & specialty OSD, stood at $102 million in 1QFY24 (24% of the total US revenue). Global Specialty & Injectables revenue on a pro-forma basis stood at $141 million. Given the reported print, we believe gRevlimid sales were in line with our estimates. The company received 10 approvals (including an injectable and specialty products) and launched 10 products (including 1 specialty and injectables) during Q1FY25. As on June 30, 2024, on a cumulative basis, the company has filed 838 ANDAs with US FDA and received approval for 668 ANDAs and 26 tentative approvals.
- **Europe (23% of sales):** Europe revenues in Q1FY25 stood at Rs19.8 bn. In euro terms, revenues stood at EUR202 million. The management expects Euro CC sales to sustain at Euro 220 million.
- **Eugia unit-3 facility update:** Sales remained flat at $141 million in Q1FY25 due to lack of optimum supplies from the Eugia unit due to remediation measures. In FY2024, Eugia's global sales stood at $541 million, while Eugia's US sales stood at $397 million. All the lines have since been operational. ARBP reported ~$160. However, with 29 pending (mostly injectables) ANDAs, which constitute 20% of ARBP's total pending ANDAs, Eugia III is one of the most important facilities for ARBP with respect to new launches. ~$40 million of new launches were scheduled from this facility over FY2025-26E, which will now be delayed. The back-up facility to Eugia III, ARBP's Vizag injectables plant, is expected to go live from 1HFY25, with supply to ROW markets to begin with. ARBP expects revenues from US and EU from this plant by FY2026E. ARBP intends to tech transfer products, as required. Vizag facility has a footprint of 7 lines. Capacities are fungible to some extent. million US sales from this facility in FY2024, which constituted ~10% of ARBP's overall US sales in FY2024.

Results (Consolidated) **Rs cr**

Particulars	Q1FY25	Q1FY24	Y-o-Y (%)	Q4FY24	Q-o-Q (%)
Total Income	7,567.0	6,850.5	10.5	7,551.9	0.2%
Operating expenditure	5,947.5	5,699.2	4.4	5,893.1	0.9%
EBITDA	1,619.6	1,151.4	40.7	1,658.9	-2.4%
Depreciation	404.2	326.6	23.8	354.3	14.1%
EBIT	1,215.4	824.8	47.4	1,304.5	-6.8%
Interest	111.0	56.6	96.4	89.4	24.2%
Other income	220.9	78.7	180.9	135.6	62.9%
PBT ex forex	1,325.3	846.9	56.5	1,350.8	-1.9%
Tax	405.7	242.3	67.4	322.6	25.8%
MI and Income from Associates	-2.4	-1.8	NM	-12.7	NM
Adjusted PAT	917.2	533.0	72.1	907.7	1.0%
Exceptional Items	0.0	-37.7	NM	0.0	NM
Reported PAT	**917.2**	**492.0**	**86.4**	**757.0**	**21.2%**
Margins			**BPS**		**BPS**
EBIDTA margin (%)	21.4	16.8	460	22.0	-56
EBIT (%)	16.1	12.0	402	17.3	-121
Adj PAT margin (%)	12.1	7.8	434	12.0	10
Tax rate (%)	30.6	28.6	200	23.9	673

Source: Company; Sharekhan Research

Revenue mix **Rs cr**

Particulars	Q1FY25	Q1FY24	Y-o-Y (%)	Q4FY24	Q-o-Q (%)
USA	3,756.0	3,001.2	25.1	3,385.0	11.0
Europe	1,728.0	1,701.2	1.6	1,769.0	(2.3)
Emerging Markets	627.0	498.9	25.7	564.0	11.2
ARV	179.0	251.2	(28.7)	250.0	(28.4)
Formulations	**6,290**	**5,453**	**15.4**	**5,968**	**5.4**
Betalactums	737	623	18.3	816	(9.7)
Non Betalactums	285	332	(14.0)	350	(18.6)
API	**1,022**	**955**	**7.1**	**1,166**	**(12.3)**
Gross Sales	**7,312**	**6,407**	**14.1**	**7,134**	**2.5**
Dossier Income	0.0	0.0	-	0.0	-
Net Sales	**7,312**	**6,407**	**14.1**	**7,134**	**2.5**

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 should 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 companies. The sector is primarily a low-debt sector with increasing operational profit and the benefit of a low tax rate due to its operations in the SEZ sector, so we remain optimistic about the sector overall.

■ Company Outlook – Uncertainties likely to stay in the near term

Over the long term, a healthy growth outlook exists for the US business, driven by improving traction from the generic injectables space (with comparatively low competition), a sturdy product pipeline, and expected traction in the recently launched products. However, headwinds for the US business are in the form of price erosion and inventory buildup across channels in the industry, which the management believes would ease out gradually in the subsequent quarters. While the strong product pipeline planned for the US could partly enable mitigation of price erosion, higher channel stocks are likely to pressurise topline growth until the stocks normalise. The European business has a healthy growth outlook, backed by product portfolio expansion and expanding geographic reach. However, some moderation in growth is expected and FY2024 is expected to post strong growth, backed by product portfolio expansion and tapping new geographies. However, Aurobindo is awaiting USFDA clearance for its plants and a successful resolution of USFDA observations would be a key monitorable and trigger for an earnings upgrade. Over the long term, Aurobindo is looking to build its presence in the specialty segment, which includes areas of injectables, biosimilars, oncology inhalers, and transdermal patches among others, which is likely to support growth. Moreover, a possible demerger of the injectables business could provide a value-unlocking opportunity. However, in the medium term, challenges in the form of price erosion and cost pressures are likely to stay and could overweigh margin performance.

■ Valuation – Upgrade to Hold with a revised PT of Rs. 1,663.

Q1FY25 numbers were in-line in Q1FY25 primarily driven by lower sales in US which offset growth in the European and growth markets. During the quarter, the company incurred a hit of lower supplies from the Eugia unit hurting lower US sales. We believe the company to report EBITDA Margin of 22% by FY26E driven by double digit growth rate ex of US, through Pen-G plant commission and benign RM cost. However, Eugia's unit-3 would lead to lower injectable and specialty sales. The company's unit 3 which was under OAI has received a WL. There are 20+ ANDAs which were expected to be filed from this unit can be shifted to USFDA approved plant in Vizag. As the WL does not pose a material risk to the company, hence we upgrade our recommendation to Hold. At CMP, the stock trades at a PE of 22.6x and 19x its FY25E and FY26E EPS and we would like to ascribe a PE of 21x to arrive at a PT of Rs 1663 (earlier Rs 1014).

About company

Hyderabad-based Aurobindo was incorporated in 1986 and manufactures generic formulations and APIs. Aurobindo generates 90% of its sales from international markets. The company currently holds a strong position in the U.S., where it is the fifth largest generic pharmaceutical company as per the IMS National Prescription Audit, measured by total prescriptions dispensed for 12 months ending June 2018. The company also holds a strong position in many European countries, including France and Italy, where it ranks among the largest generic companies. Aurobindo is a vertically integrated company, meeting around 70% of its API requirements in-house. Aurobindo has 26 manufacturing facilities for its API and formulations businesses, which have requisite approvals from various regulatory authorities, including the USFDA, U.K. MHRA, Japan PMDA, WHO, Health Canada, MCC South Africa, and ANVISA Brazil. Recently, Aurobindo entered Poland and the Czech Republic with the acquisition of Apotex's commercial operations. The company also strengthened its U.S. presence with the acquisition of dermatology and oral solid businesses from Sandoz.

Investment theme

Aurobindo is one of the largest pharma players with a large share of revenue from the U.S. having one of the highest ANDA filings. However, the company is grappling with the pricing pressure in its OSD segment, wherein it has a stronghold. Nevertheless, it is seeing an uptick in its complex and specialty injectables revenue share in the U.S. With an increased share of the injectables and biosimilar products revenue, it should be able to stabilise its margins over the medium term. However, currently, it is experiencing margin pressures due to increased expenses and uneven sales growth.

Key Risks

Delay in product approvals, change in regulatory landscape, and negative outcome of key facility inspections by the USFDA can affect earnings prospects.

Additional Data

Key management personnel

K. Ragunathan	Chairperson
K. Nithyananda Reddy	Managing Director
P.V. Ramaprasad Reddy	Non-Executive Director, Promoter
Santhanam Subramanian	Chief Financial Officer

Source: Company Website

Top shareholders

Sr. No.	Holder Name	Holding (%)
1	LIFE INSURANCE CORPORATION OF INDIA	5.57
2	HDFC TRUSTEE COMPANY LTD.	2.94
3	MIRAE ASSET EMERGING BLUECHIP FUND	1.69
4	BNP PARIBAS ARBITRAGE	1.22
5	INVESCO PACIFIC FUND (U.K.)	1.05

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

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