



Top Sector Ideas: *Pharmaceutical*

Q3FY24 Pharma Review – Higher Profitability with Easing Price Erosion, New Launches, & Lower RM Prices

✓ *Key Highlights & Financial Performance*

- In Q3FY24, the Pharma Coverage universe demonstrated robust revenue growth of 12.7% YoY and 2.8% QoQ, primarily driven by volume gains, stable demand, and the introduction of new products such as gRevlimid, gSpiriva, and gPrezista. Additionally, there has been a stabilization of pricing pressure in the US base business.
- EBITDA margin witnessed a healthy improvement of 220bps YoY and 55bps QoQ, attributed to normalizing cost inflation and stabilizing prices. US price erosion remains benign, mostly in the low to mid-single digits for most players, with benefits derived from drug shortages and supply issues. There is an increasing focus on complex molecules, with Indian companies advancing up the value chain.
- India's growth has exceeded expectations, and expansion of the field force is expected to drive further volume growth in the country. Softening input costs and reduced freight expenses have contributed to margin improvement.
- While hospitals experienced a seasonally weak quarter, brownfield expansion initiatives are anticipated to drive growth without significant dilution in Return on Capital Employed (RoCE).

Pharma Back on Growth Track

- **In FY24, high single-digit domestic growth is anticipated.** Furthermore, the US market is poised for robust growth, supported by the normalization of prices in the base business and the ongoing ramp-up of gRevlimid, along with new product launches such as gSpiriva and gPrezista.
- In the US business, **supply constraints have prompted most business leaders to anticipate a significant decrease in price erosion**, with expectations that it will remain low for the remainder of FY24.
- In India, growth has primarily been fueled by price increases and robust expansion in chronic therapies, with **all major companies projecting high single-digit growth for FY24.**
- **Margins will also improve as RM and freight costs normalize, US price erosion eases, and a better mix is achieved.**
- However, **USFDA inspections remain an overhang and price erosion in the US is expected to increase once supply normalize.**
- Therefore, we continue to eye on companies that are focused on launching niche products in the US market and a strong product mix (Chronic Portfolio) in the Indian market.
- **LUPIN, CIPLA, and Aurobindo are our top picks in the Pharma universe.**

Short and Medium-term Outlook

Short Term

Trend in Price Erosion after the normalization of drug shortages supply in the US

India: Weak acute season and NLEM impacted growth

Better sales growth was led by gRevlimid and the launch of new products gSpiriva, gPrtezista

Field force expansion to drive growth in India


Better margins for full year due to normalized cost inflation and moderation in US Price Erosion

Medium Term


Key monitorables – Price Erosion, Margins Expansion, and Launch of New Products

Stock	Reco.	TP	Recommendation Rationale
 <p>Lupin Ltd</p>	<p>BUY</p>	<p>Rs 1,770*</p>	<ul style="list-style-type: none"> ✓ The company's US business recorded revenue of \$212 Mn, representing a modest 0.5% increase QoQ. Encouragingly, new launches such as Darunavir and gSpiriva continue to gain traction, with the company achieving market shares (MS) of up to 30% and 32% respectively, despite experiencing low single-digit price erosion in its base business. ✓ The company's India business exhibited a robust YoY growth of 13.4%, surpassing the industry performance measured by IPM (Indian Pharmaceutical Market) growth. This outperformance was particularly notable in key therapy areas such as CVS (Cardiovascular System) and anti-diabetic treatments. The other segment reported growth as follows: EMEA (+36% YoY), and RoW business (+71.4% YoY). ✓ The company's gross margins increased by 60bps QoQ to 66.8% due to a better product mix and strong growth in the US and Indian markets. Reported PAT increased to Rs 613 Cr (+25.1% QoQ) due to the low tax rate. ✓ 1) New launches in the US market like Darunavir and gSpiriva have gained MS upto 30% and 32% respectively; 2) Recent approvals for Tolvaptan (MS \$287 MN) and Xyway (MS \$958 Mn) – 180 days exclusivity could add business in the second half; 3) Double-digit growth in India business as the company has already increased MR numbers to 1,000; 4) An uptick in the API business as the API industry is witnessing demand revival.

* Note: Target Price is based on our Q3FY24 Result Update Report

Stock	Reco.	TP	Recommendation Rationale
 <p>CIPLA LTD</p>	<p>BUY</p>	<p>Rs 1,515*</p>	<ul style="list-style-type: none"> ✓ The US revenue stood at \$230 Mn (vs. exp \$220 Mn), led by improvement in the base business pricing and higher MS in Lenotirade, while Albuterol has stable MS. The company has filed gSymbicort (MS \$3.3 bn) and one other respiratory product. ✓ Gross margins improved by 90bps YoY to 66.4% due to a high proportion of gRevlimid and low other expenses, while stable R&D expenses led to EBITDA margins of 26.5%. ✓ The company’s Reported PAT stood at Rs 1,220 Cr, which grew by 40.5% on a YoY basis. ✓ The base business in the US reported better-than-expected results (\$190-\$200 Mn). This was driven by the following factors: 1) Only a few distributors buying locally manufactured drugs, 2) Channel readjusting, 3) Shortage of drugs in a few segments, and 4) The company launching new products in the market. gSynbicort and one Peptide (\$300-400 Mn) product have been already launched in the last quarter and the company has planned to launch 4 more peptides in FY25E.

* Note: Target Price is based on our Q3FY24 Result Update Report

Stock	Reco.	TP	Recommendation Rationale
 <p>Aurobindo Pharma Ltd</p>	<p>BUY</p>	<p>Rs 1,160*</p>	<ul style="list-style-type: none"> ✓ Aurobindo reported EBITDA/PAT beat estimates by +1.7%/+12.6%. The company's consolidated revenue grew by 14.7%/1.8% YoY/QoQ, and Gross Margins improved by 253bps/198bps YoY/QoQ. EBITDA margins improved by 689bps/275bps YoY/QoQ. ✓ The growth was mainly driven by volume gains, stable demand, and new product launches. The wide range of approved baskets has helped the company optimally manage the price erosion, which remains neutral. ✓ Production in Eugia-3 has stopped temporarily as the company is filing its response to the USFDA for its 9 observations following the inspection visit in Jan'24. This could lead to a loss of \$20 Mn in Q4FY24. ✓ ABRP has a number of levers to grow its topline: 1) Generic injectibles, Eugia (USD\$520 Mn sales) may grow at low double-digit rate based on value-added approval, 2) The launch of Trastuzumab biosimilars in H1FY25E, 3) The launch of Pen-G injectible in H1FY25E, and 4) One-time opportunity in gRevlimid in the next 2-3 years.

* Note: Target Price is based on our Q3FY24 Result Update Report

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