

Dr. Reddy's Laboratories

24 November, 2022

Reuters: REDY.BO; Bloomberg: DRRD IN

Dr. Reddy's – Management Meet Update

We hosted the management of Dr. Reddy's Laboratories Ltd (DRL) at our Annual Investor Conference to discuss the business outlook. The company has reiterated its guidance of single-digit growth in the US and double-digit growth in other markets with 25% margins. But, growth and margins would not be linear. In the US, the company continues to face annual double-digit price erosion. In the domestic market too, due to its acute-heavy portfolio, the company is growing at lower than industry rate. However, excluding covid, the company is growing in double digits in almost all other markets. Also, the company is working on its domestic business to deliver market-beating growth in the medium term. We like DRL management's strategic decision-making ability and its enhanced focus on the branded business. However, restructuring and shift in focus from Gx to BRx markets are likely to weigh on near to medium term base business growth. Also, capital allocation is still high towards Developed Markets (DM) complex products and the innovative pipeline. Spending on Horizon 2 opportunity (mainly due to innovation) and Biosimilars is likely to drag DRL's overall financials. We maintain ACCUMULATE on DRL with a revised target price (TP) of Rs4,640, valuing it at 24x PE on Sept'24E base EPS of Rs188 and NPV of Rs122 for the Revlimid opportunity.

US

- The company believes that Revlimid antitrust lawsuit has no merit since the settlement took place in the court of law. Additionally, it is difficult to comment on the outcome as litigation in the US tends to drag on for many years.
- gKuvan with launch of branded product Javygtor along with a partner in the US is showing strong traction.
- Base business continues to see double-digit price erosion, with a few large products getting impacted. This includes Vasopressin, which saw enhanced competition on account of new generic launches over the last few months. The company was able to maintain market share in most of the products.
- The company is seeing some easing in pricing pressure, but it believes that it is too early to comment on the trend.
- There is no plan for any mass product restructuring of the US product portfolio, but, products are continuously evaluated on an ongoing basis.
- US business is expected to grow in single digit over a multi-year horizon.
- Out of the current US pipeline of 170 products, 40% are injectables and 15% complex high value products. 11-12 biosimilars are under development. The company has filed 80-85 products, of which 50% are Para IV's.
- OTC Products constitute ~15-16% US sales, which are mostly private labels. The company has also ventured into branded OTC, but its contribution is negligible. OTC is a relatively stable business but does see Rx level price erosion. The company continues to add more products to the OTC business and growth in OTC is more linear compared to the Rx business.
- The company expects to launch 20-25 products each year.

ACCUMULATE

Sector: Pharmaceuticals

CMP: Rs4,407

Target Price: Rs4,640

Upside: 5.3%

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Key Data

Current Shares O/S (mn)	166.5
Mkt. Cap (Rsbn/US\$bn)	733.5/9.0
52 Wk H / L (Rs)	4,931/3,654
Daily Vol. (3M NSE Avg.)	433,118

Price Performance (%)

	1 M	6 M	1 Yr
Dr. Reddy's	0.6	1.3	(4.2)
Nifty Index	3.0	13.3	4.9

Source: Bloomberg

[FY22 Annual Report](#)
[2QFY23 Results](#)

Y/E March (Rsmn)	FY21	FY22	FY23E	FY24E	FY25E
Net sales	1,89,722	2,12,617	2,36,746	2,57,611	2,68,135
EBITDA	44,582	45,311	50,948	58,235	60,493
Net profit	25,826	28,475	31,617	37,140	38,648
EPS (Rs)	155.6	171.5	190.5	223.7	232.8
EPS growth (%)	38.9	10.3	11.0	17.5	4.1
EBITDA margin (%)	23.5	21.3	21.5	22.6	22.6
PER (x)	28.3	25.7	23.1	19.7	18.9
EV/Sales (x)	3.8	3.4	2.9	2.6	2.4
EV/EBITDA (x)	16.3	15.9	13.7	11.6	10.7
RoCE (%)	13.4	13.2	13.3	14.4	13.8
RoE (%)	15.7	15.7	15.3	15.6	14.4
RoIC (%)	15.8	16.1	16.9	19.2	19.4

Source: Company, Nirmal Bang Institutional Equities Research

India

- The last couple of quarters were a bit subdued for the domestic business, but the company has identified areas for improvement.
- Slower than industry growth could mainly be attributable to its acute-heavy portfolio. The company expects to deliver market-beating performance going forward.
- The company expects to launch several new products (especially in OTC and Nutraceuticals) with a renewed focus on a better go-to market strategy and portfolio enhancement.
- The company expects to launch 15-20 products in the domestic market with focus on 10 therapies, including anti-diabetics, oncology, CVS and GI.
- The current MR strength stands at 6500 spread across the country. The company does not intend to add new MRs. Improvement in MR productivity would be led by sales growth.

Europe

- Europe business remains stable and has not faced any significant disruption. Growth would be led by new product launches and geographical expansion. The aim is to establish presence in 12 European countries.
- In constant currency terms, the European business delivered double-digit growth in 2QFY23.

Margins

- There has been some bit of normalization in raw material costs. Additionally, solvent and freight rates have also eased.

Others

- Emerging Markets – Adjusted for covid-related sales, most countries have grown in double digits.
- PS&I business remains volatile and the company continues to face some near term challenges. However, it expects double-digit growth in the medium term.

Exhibit 1: One Year Rolling Forward P/E Chart



Source: BSE, Bloomberg, Company, Nirmal Bang Institutional Equities Research

Financial statements

Exhibit 2: Income statement

Y/E March (Rsmn)	FY21	FY22	FY23E	FY24E	FY25E
Net sales	1,89,722	2,12,617	2,36,746	2,57,611	2,68,135
% growth	13.4	12.1	11.3	8.8	4.1
Cost of Sales	86,645	1,00,551	1,10,688	1,19,226	1,23,672
R&D Expenditure	16,541	17,482	18,940	20,609	21,451
SG&A Expenditure	41,954	49,273	56,171	59,541	62,519
Extraordinary Items	(8,588)	(6,724)	7,878	-	-
Other Income	982	2,761	1,320	1,386	1,455
Total expenditure	1,45,140	1,67,306	1,85,799	1,99,376	2,07,641
Operating Profit	44,582	45,311	50,948	58,235	60,493
% growth	26.2	1.6	12.4	14.3	3.9
Operating Profit margin (%)	23.5	21.3	21.5	22.6	22.6
Finance (Expense) / Income	1,653	2,119	2,367	3,091	3,486
Depreciation & Amortisation	12,696	11,872	13,218	13,968	14,718
Share of Profit in Equity Investments	480	703	738	775	814
Gross profit	1,03,077	1,12,066	1,26,059	1,38,385	1,44,463
% growth	17.9	8.7	12.5	9.8	4.4
Profit before tax	26,413	32,298	50,034	49,520	51,531
% growth	7.8	22.3	54.9	(1.0)	4.1
Tax	9,175	8,730	12,508	12,380	12,883
Effective tax rate (%)	34.7	27.0	25.0	25.0	25.0
Reported PAT	17,238	23,568	37,525	37,140	38,648
Adjusted PAT	25,826	28,475	31,617	37,140	38,648
% growth	38.9	10.3	11.0	17.5	4.1

*In IFRS format

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Cash flow

Y/E March (Rsmn)	FY21	FY22	FY23E	FY24E	FY25E
PBT	26,413	32,298	50,034	49,520	51,531
Depreciation	12,696	11,872	13,218	13,968	14,718
Net Chg in WC	(4,939)	(17,929)	(9,302)	(9,068)	(4,559)
Taxes	(5,716)	7,437	(12,508)	(12,380)	(12,883)
Others	5,338	(6,540)	3,093	3,323	1,439
CFO	33,792	27,138	44,533	45,363	50,246
Capex	(27,990)	(16,059)	(15,000)	(15,000)	(15,000)
Net Investments made	4,110	(11,201)	(10,000)	(10,000)	(10,000)
Others	1,220	873	-	-	-
CFI	(22,660)	(26,387)	(25,000)	(25,000)	(25,000)
Change in Share capital	269	334	-	-	-
Change in Debts	1,947	2,735	(11,000)	(11,000)	(3,000)
Div. & Div Tax	-4,147	-4,146	-4,980	-7,848	-8,166
Others	3,575	349	-	-	-
CFF	1,644	(728)	(15,980)	(18,848)	(11,166)
Total Cash Generated	12,776	23	3,553	1,515	14,079
Cash Opening Balance	2,053	14,829	14,852	18,405	19,920
Cash Closing Balance	14,829	14,852	18,405	19,920	34,000

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Balance sheet

Y/E March (Rsmn)	FY21	FY22	FY23E	FY24E	FY25E
Equity	832	832	832	832	832
Reserves	1,72,230	1,89,695	2,22,240	2,51,532	2,82,014
Net worth	1,73,062	1,90,527	2,23,072	2,52,364	2,82,846
Net deferred tax liabilities	-10,292	-12,721	-12,721	-12,721	-12,721
Short-term loans	24,000	28,099	18,099	8,099	6,099
Long-term loans	6,299	5,746	4,746	3,746	2,746
Other non-current liabilities	2,401	2,479	2,479	2,479	2,479
Liabilities	1,95,470	2,14,130	2,35,675	2,53,967	2,81,449
Intangible assets and goodwill	40,216	31,664	31,664	31,664	31,664
Net block	57,111	62,169	63,951	64,984	65,266
Other non-current assets	9,436	8,934	9,042	9,135	9,182
Inventories	45,412	50,884	51,890	56,463	58,769
Debtors	49,641	66,764	61,619	67,049	69,789
Cash	14,829	14,852	18,405	19,920	34,000
Loans and advances	20,962	31,419	41,419	51,419	61,419
Other current assets	17,254	17,187	18,765	20,129	20,817
Total current assets	1,48,098	1,81,106	1,92,098	2,14,980	2,44,794
Creditors	23,744	25,572	12,130	13,066	13,553
Other current liabilities	35,647	44,171	48,949	53,729	55,903
Total current liabilities	59,391	69,743	61,079	66,795	69,456
Net current assets	88,707	1,11,363	1,31,018	1,48,185	1,75,337
Total assets	1,95,470	2,14,130	2,35,675	2,53,967	2,81,449

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: Key ratios

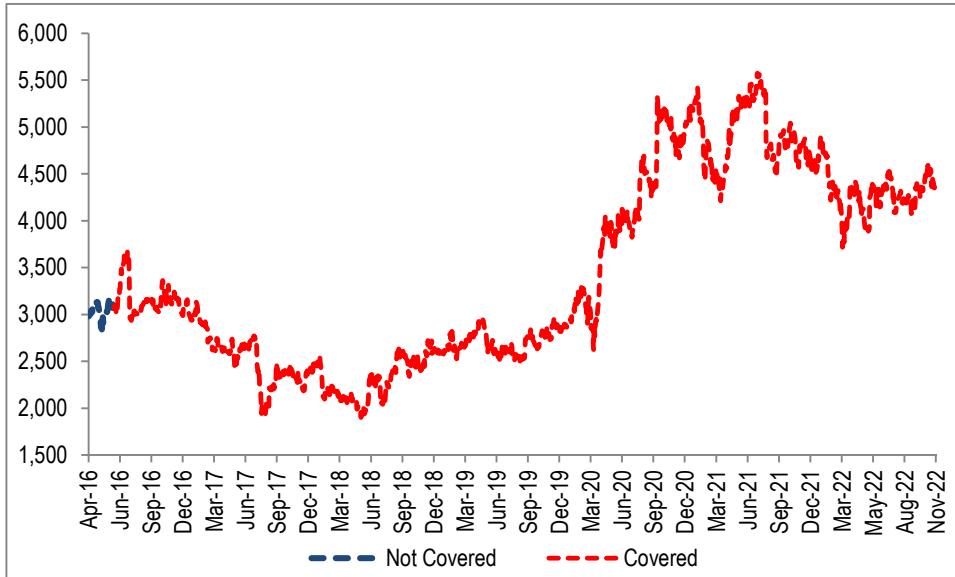
Y/E March	FY21	FY22	FY23E	FY24E	FY25E
Profitability & return ratios					
EBITDA margin (%)	23.5	21.3	21.5	22.6	22.6
Net profit margin (%)	13.6	13.4	13.4	14.4	14.4
RoE (%)	15.7	15.7	15.3	15.6	14.4
RoCE (%)	13.4	13.2	13.3	14.4	13.8
Working capital & liquidity ratios					
Receivables (days)	96	100	95	95	95
Inventory (days)	77	83	80	80	80
Payables (days)	39	42	40	40	40
Current ratio (x)	2.5	2.6	3.1	3.2	3.5
Quick ratio (x)	1.7	1.9	2.3	2.4	2.7
Valuation ratios					
EV/sales (x)	3.8	3.4	2.9	2.6	2.4
EV/EBITDA (x)	16.3	15.9	13.7	11.6	10.7
P/E (x)	28.3	25.7	23.1	19.7	18.9
P/BV (x)	4.2	3.8	3.3	2.9	2.6

Source: Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price	Target price (Rs)
10 June 2016	Buy	3,160	3,950
27 July 2016	Buy	3,300	3,950
6 February 2017	Buy	3,142	3,950
15 May 2017	Buy	2,584	3,366
28 July 2017	Buy	2,620	3,020
1 November 2017	Buy	2,428	3,216
29 January 2018	Buy	2,508	3,077
23 May 2018	Buy	2,004	2,898
23 July 2018	Buy	2,059	2,898
27 July 2018	Buy	2,110	2,898
29 October 2018	Buy	2,405	3,122
4 February 2019	Accumulate	2,791	3,122
5 April 2019	Buy	2,772	3,348
20 May 2019	Buy	2,748	3,281
30 July 2019	Buy	2,653	3,281
23 September 2019	Accumulate	2,829	3,138
4 November 2019	Buy	2,755	3,138
28 January 2020	Accumulate	3,189	3,188
27 March 2020	Accumulate	2,945	3,333
23 April 2020	Sell	4,056	3,647
20 May 2020	Sell	3,911	3,647
30 July 2020	Sell	4,300	3,998
18 September 2020	Buy	4,827	5,656
23 September 2020	Accumulate	5,168	5,656
29 October 2020	Buy	4,950	5,737
27 November 2020	Buy	4,899	5,648
7 January 2021	Buy	5,292	6,231
1 February 2021	Buy	4,603	5,594
10 March 2021	Buy	4,448	5,594
5 April 2021	Buy	4,588	5,594
17 May 2021	Accumulate	5,197	5,782
28 July 2021	Accumulate	4,844	5,240
26 September 2021	Buy	4,777	5,515
31 October 2021	Buy	4,670	5,644
30 January 2022	Buy	4,218	5,689
21 February 2022	Buy	4,321	5,710
31 March 2022	Buy	4,351	5,349
20 May 2022	Buy	3,928	5,424
29 July 27, 2022	Buy	4,259	5,587
29 September 2022	Accumulate	4,267	4,468
29 October 2022	Accumulate	4,461	4,640
24 November 2022	Accumulate	4,407	4,640

Rating track graph



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ACCUMULATE -5% to 15%

SELL < -5%

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