

DR.REDDYS LABORATORIES

FY17 Annual Report Analysis

India Equity Research | Pharmaceuticals

FY17 was a forgettable year for Dr. Reddy's Laboratories (DRRD) as increased competition in key products, channel consolidation and delay in approval for new products in US (45% of business) impacted top line and bottom line by 9% and 40%, respectively. Weak business performance led to operating cash flow plummeting 48%. The company acquired 8 ANDAs from Teva for USD350mn and also bought back its shares worth INR15bn from the secondary market to boost investor sentiments in these uncertain times, which led to net debt burgeoning by INR37bn. R&D expenses increased to 14.0% of sales compared to 11.5% in FY16 and RoCE tumbled to 8.1% compared to 18.8% last year. Going forward, management's key priorities are: (1) launch of complex pipeline like Copaxone & Nuvaring in US; and (2) remediate issues raised in the USFDA warning letter. Maintain 'HOLD' with TP of INR2,660.

US declined by sharp 17%

DRRD is grappling with delays in USFDA approvals for its complex pipeline coupled with delay in launches from its 3 plants that received a warning letter in November 2015. Higher price erosion due to intense competition in key products like *Valganciclovir*, *Decitabine* and *Azacitidine* and termination of the contract with McNeil Consumer Healthcare (PAT impact of US\$25mn) also affected US revenues. Key positives for the year were: 1) 26 new product filings in US, taking cumulative filings to 101 including 62 Para IVs and 21 FTFs; 2) DRRD acquired 8 ANDAs from Teva for USD350mn and 6 OTC brands from Ducere Pharma for INR1,148mn; 3) the company entered into a strategic collaboration with Gland Pharma to market its 8 injectable ANDAs.

Buyback, dip in operating cash flow led to increase in debt

In FY17, DRRD bought back INR15bn worth of shares (~3% of market cap) from the secondary market at an average price of INR3,090/share. Capex for the year stood at INR17bn versus INR15bn in previous year. Operating cash flow declined by 48% to INR21bn, while net debt increased by INR37bn. RoCE declined to 8% in FY17 from peak of 21.5% in FY14 and 18.8% in FY16.

Outlook and valuations: Earnings under pressure; maintain 'HOLD'

In our opinion, there are several downside risks to DRRD's earnings. At CMP, the stock trades at 18.5x FY19E EPS. We maintain 'HOLD/SP' with TP of INR2,660.

Financials Matrix	(INR mn)			
Year to March	FY16	FY17	FY18E	FY19E
Net Revenues (INR mn)	154,708	140,809	156,429	181,939
EBITDA (INR mn)	39,088	24,155	30,256	41,124
Adjusted Diluted EPS (INR)	135.0	72.6	96.1	147.7
Diluted P/E (x)	20.2	37.6	28.4	18.5
EV/EBITDA (x)	11.8	20.0	15.9	11.6
ROAE (%)	19.2	9.5	12.3	17.1

EDELWEISS 4D RATINGS	
Absolute Rating	HOLD
Rating Relative to Sector	Performer
Risk Rating Relative to Sector	Medium
Sector Relative to Market	Equalweight

MARKET DATA (R: REDY.BO, B: DRRD IN)	
CMP	: INR 2,732
Target Price	: INR 2,660
52-week range (INR)	: 3,690 / 2,380
Share in issue (mn)	: 165.7
M cap (INR bn/USD mn)	: 453 / 7,015
Avg. Daily Vol.BSE/NSE('000)	: 392.3

SHARE HOLDING PATTERN (%)			
	Current	Q3FY17	Q2FY17
Promoters *	26.8	26.8	26.7
MF's, FI's & BK's	10.6	8.2	6.5
FII's	32.4	36.3	37.2
Others	30.3	28.7	29.7
* Promoters pledged shares (% of share in issue)			1.2

PRICE PERFORMANCE (%)			
	Stock	Nifty	EW Pharma Index
1 month	3.7	1.1	2.2
3 months	3.7	5.8	(5.0)
12 months	(24.8)	15.4	(10.5)

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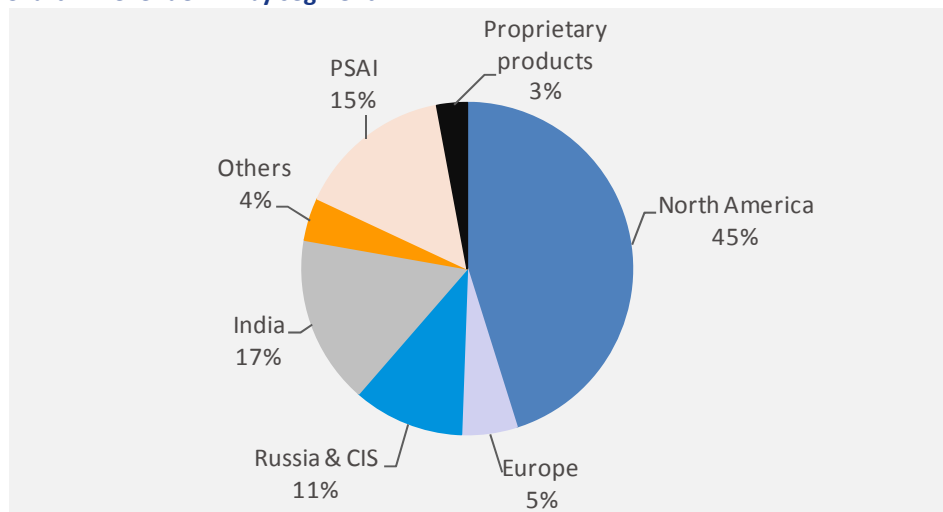
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July 10, 2017

Revenues declined 9%

DRRD's total revenue, at INR140.8bn, declined 9%. Except Russia and India, revenue declined across segments. The company's generics business (82% of total revenue) was subdued due to lower contribution from North America, Venezuela and lacklustre growth in India, though offset by better growth in Russia. PSAI segment and proprietary business also posted weak performance.

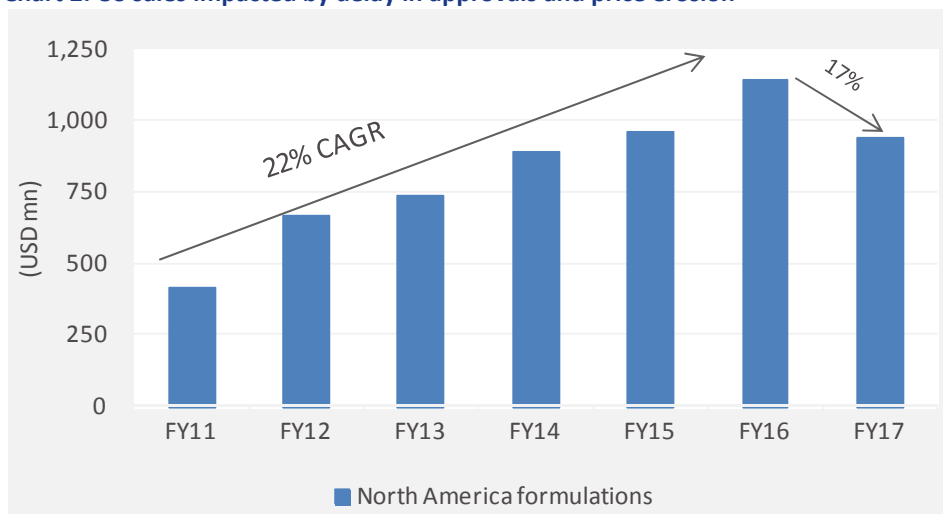
Chart 1: Revenue mix by segment



Source: Company, Edelweiss research

North America Formulations

Chart 2: US sales impacted by delay in approvals and price erosion



Source: Company, Edelweiss research

North America Formulations segment (45% of total revenue) declined 17% in CC terms largely attributable to: (1) delay in approvals from USFDA and launch delays (*Esomeprazole*, *Imatinib*, some injectables as well as certain APIs) from its 3 plants that received the USFDA warning letter; (2) significant price erosion following heightened competition in key products, such as, *Valganciclovir*, *Decitabine* and *Azacitidine*; (3) end of supply agreements

with McNeil Consumer Healthcare (annualised PAT impact of ~USD25mn); and (4) price erosion in base business.

In FY17, DRRD launched 10 products with the major ones being *Omeprazole Sodium Bicarbonate*, *Nitroglycerin SLT (sublingual tablets)*, *Paricalcitol injection* and *Naproxen Sodium IR (immediate-release)*. The company also garnered high market share in certain products like *Esomeprazole DR* and *Habitrol* (OTC nicotine patch). DRRD has also de-risked its near term major launches by listing alternative sites for products filed from facilities under warning letter.

During FY17, DRRD acquired 8 ANDAs from Teva/ Allergan across various dosage forms for USD350mn. Of these, the first product *Vytorin* was launched in April 2017. They also acquired 6 well known OTC brands in cough, cold, pain and dermatological categories from Ducere Pharma and entered into a strategic collaboration with Gland Pharma to market and distribute a portfolio of 8 injectable ANDAs in the US market.

Table 1: Eight ANDAs acquired from Teva

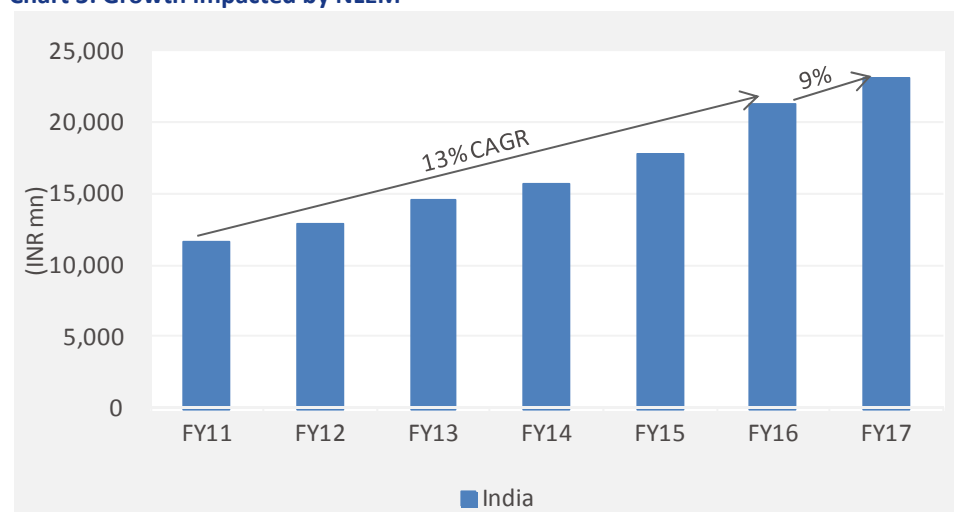
Product	Consideration (USD mn)
gNuvaRing (Ethinyl estradiol/Ethonogestrel Vaginal Ring)	185
gSuboxone (Buprenorphine HCl/Naloxone HCl Sublingual Film)	70
gRozerem (Ramelteon Tablets)	34
Others	61
Total	350

Source: SEC filings, Edelweiss research

During FY17, 26 ANDAs were being filed (including 11 Para IV filings) with 8 final approvals were received. Cumulatively, 101 generic filings — 99 ANDAs (including 62 Para IVs) and 2 NDAs under 505(b)(2) are currently awaiting approval from the USFDA. Of these, 21 are believed to have 'First to File' status. In FY17, the company in-licensed 20 ANDAs in the US, of which 13 are Para IV filings. As of March 31, 2017, cumulatively DRRD had in-licensed 30 ANDAs in the US, out of which 24 are pending USFDA approval.

India

Chart 3: Growth impacted by NLEM



Source: Company, Edelweiss research

India formulations business (17% of total revenue) grew 9%. However, growth was partially impacted by the 4% decline in sales of certain drugs forming part of NLEM for which NPPA had notified price declines. As per IMS, for DRRD growth at 4.5% was lower than market growth of 9% due to higher impact of NLEM on its portfolio.

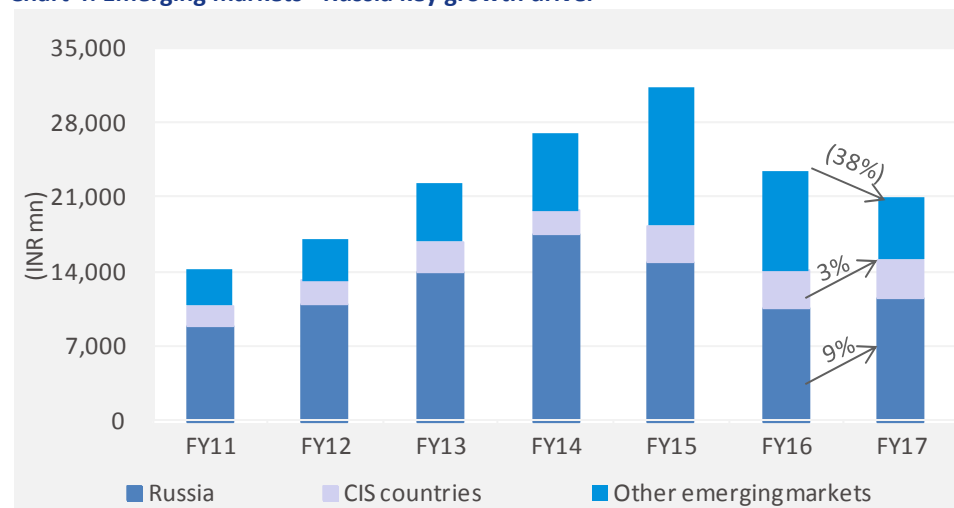
During the year, DRRD expanded its collaboration with Amgen to market and distribute 3 of its products in India, namely, *XGEVA* (Denosumab), *Vectibix* (Panitumumab) and *Prolia* (Denosumab) in the therapeutic areas of oncology and osteoporosis. The company also entered into an agreement with Integra LifeSciences to market and distribute *DuraGen Plus* and *Suturable DuraGen* dural regeneration matrices in India.

DRRD had 5,778 sales representatives in India, including managers. Also, the company believes that if the FDC ban becomes effective it could impact revenues by 0.5% annually.

Emerging markets

Overall, emerging markets (EM) business grew 7% largely attributable to increased revenues from Russia. However, DRRD discontinued its drug supply business in Venezuela due to the ongoing economic crisis in the country.

Chart 4: Emerging markets - Russia key growth driver



Source: Company, Edelweiss research

- Russia:** Revenues grew 8% in CC terms. According to IMS, DRRD's Russia sales-value/volume growth stood at 4.5%/5.1% for FY17, versus overall market's 5.6%/-3.9% growth. Improving macros and currency stability during the year aided growth. The growth was also driven by increased marketing and pharmacy chain activities for OTC business (40% of revenues, grew 17%). Despite this growth, Russian business has yet to achieve its previous peak.

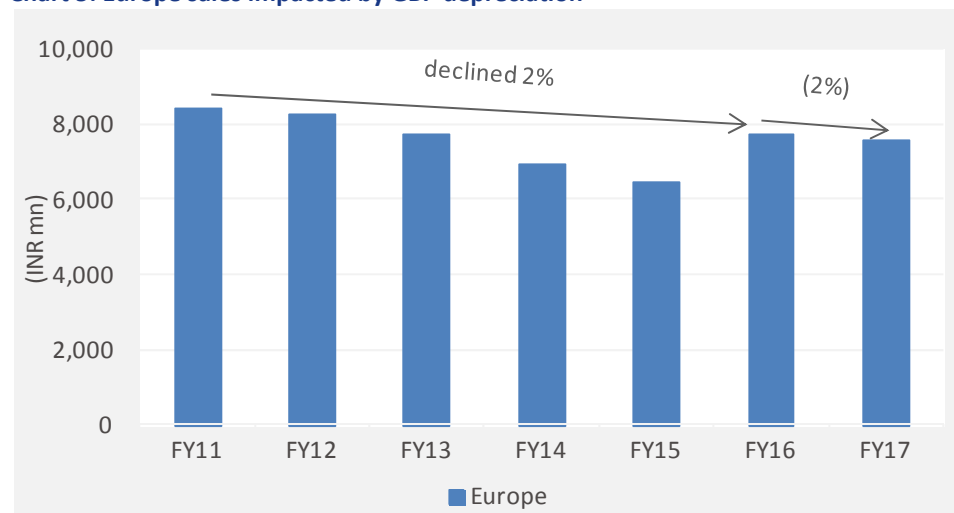
Table 2: Russia operations

	FY12	FY13	FY14	FY15	FY16	FY17
RUB-INR average	1.62	1.75	1.83	1.42	1.04	1.00
IMS (%)						
Industry sales value growth	N/A	4.9	7.7	10.1	8.4	5.6
Industry volume growth	N/A	2.7	4.1	(2.7)	(4.0)	(3.9)
DRRD sales value growth	N/A	8.5	1.9	12.3	5.6	4.5
DRRD volume growth	N/A	0.7	5.0	(1.3)	(3.9)	5.1
DRRD's field-force in Russia						
Rx Medical representatives	400	396	275	284	268	288
Rx Managers	77	65	44	48	38	38
OTC medical representatives	141	146	181	226	216	212
OTC Managers	N/A	N/A	N/A	40	31	30
Hospital specialists	39	35	38	41	38	40
Hospital account managers	17	16	17	17	17	17

Source: Company, Edelweiss research

- **Other CIS countries:** CIS markets, including Romania, grew 3%. This growth was triggered by higher off-take in Ukraine and Romania, though partially offset by devaluation of the Ukrainian Hryvnia. In Kazakhstan, currency devaluation and generally unfavourable macroeconomic environment dampened growth.
- **Other EM's:** Revenue from rest of EM's declined 38%, largely due to severely constrained operations in Venezuela.

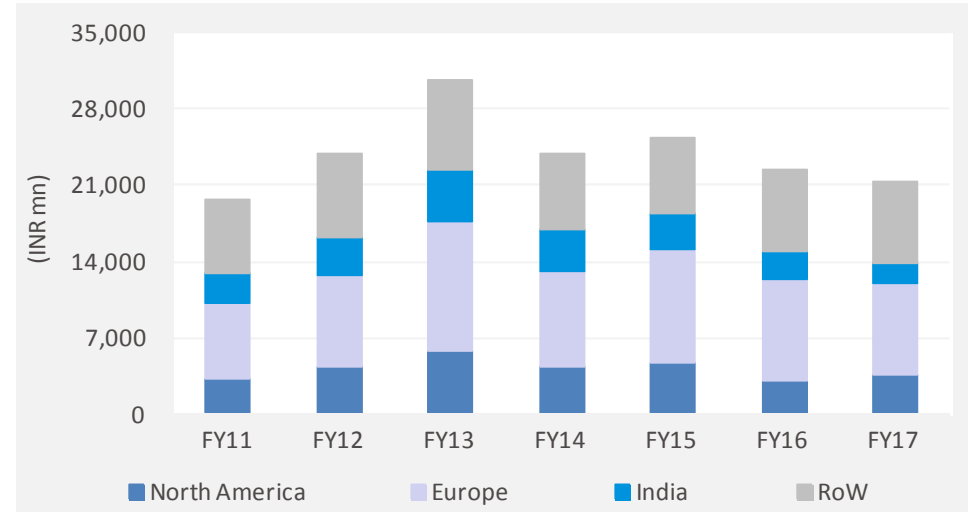
Europe

Chart 5: Europe sales impacted by GBP depreciation

Source: Company, Edelweiss research

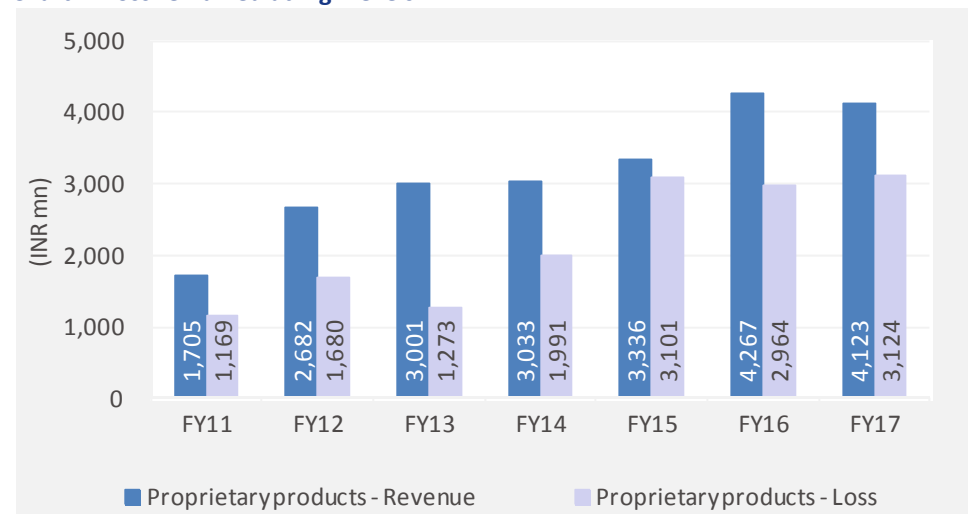
Europe (5% of total revenue) revenue, primarily derived from Germany, UK and out-licensing across Europe, declined 2% following depreciation in GBP post Brexit. While DRRD faced pricing pressures on products like *Pregabalin* and *Arpiprazole*, it launched new products like *Imatinib*, *Voriconazole* and *Buprenorphine* patch and benefitted from volume gains in *Pregabalin*.

PSAI

Chart 6: PSAI segment declined 5%


Source: Company, Edelweiss research

API business (15% of total revenue) declined 5% impacted by warning letter at 2 API facilities and lower off-take of some key molecules. During FY17, DRRD filed 85 DMFs worldwide, of which 11 were filed in the US, 5 in Europe and 69 in other countries. Cumulatively, total DMFs filed worldwide (as of March 31, 2017) were 830, including 275 DMFs filed in the US.

Proprietary products
Chart 7: Loss remained at high levels


Source: Company, Edelweiss research

Proprietary products' revenue declined 3% due to temporary supply issues in one of its drugs and re-prioritisation of portfolio to accelerate market uptake of new products. Meanwhile, loss from this business was still at high levels as DRRD launched its approved products – *Zembrace SymTouch* and *Sernivo*, during the year.

- **Zembrace SymTouch (launched in April 2016):** The product is a 3mg Sumatriptan Auto injector filed through 505(b)(2) pathway. It has a better safety profile due to its lower strength (3 versus 6mg). The product is indicated for patients with migraine and severe nausea. Market for Sumatriptan in US is USD250mn for oral and USD120mn for Injections. DRRD achieved 500 prescriptions per week and 75% coverage with insurance by end FY17. One injectable Sumatriptan of 4mg is already available in the market, which is not doing too well. DRRD has a field force of 40-50 personnel to reach ~7,000 neurologists in US markets.
- **Sernivo spray (launched in May 2016):** The product is indicated for treatment of mild to moderate plaque psoriasis in patients 18 years of age or older. DRRD had 850 prescriptions per week and 75% coverage with insurance by end FY'17.

As of March 31, 2017, DRRD had 16 active product development programs in its pipeline. In January and February 2016, it received USFDA approval for its NDAs –Sernivo and Zembrace, which were launched during the year. The company also received tentative approval of its NDA for its dermatology product, *Zenavod*.

Table 3: DRRD's proprietary pipeline

Compound	Therapy area	Status	Clinical work done
DFN-11 (Zembrace)	Neurology (Migraine)	NDA approved Feb 16, launched Apr 16	3 BE studies
DFD-01 (Sernivo)	Derma (Psoriasis)	NDA approved Jan 16, launched Jun 16	Ph-3 study
DFD-09 (Zenavod) - doxycycline	Dermatology (rosacea)	Tentative approval Feb 16, court case ongoing against Galderma	BE study
DFN-02	Neurology (Migraine)	Submission planned for 2018	Ph-3 completed. BE and patient safety studies completed; efficacy studies in progress.
DFD-06	Dermatology (Plaque Psoriasis)	NDA submitted in Jan 17	Ph-3 completed.
DFD-10	Dermatology (Acne)	NDA approval received in May 17	2 BE studies completed
DFD-11 (Xeglyze)	Pediatrics (head lice)	NDA filed in Sep 15 by Hatchtech, DRRD bought in Dec 15. received a CRL in Aug 16. Expect to respond in July 2017.	N/A
XP 23829 (NCE inlicensed from Xenoport)	Derma (Psoriasis)	-	Ph-2 study completed in Sep 2015. Phase 2b/3 studies being planned.
E7777 (orphan product)	Haematology-Oncology (Skin Cancer)	BLA submission planned for 2019	Ph-3 study ongoing

Source: Company, Edelweiss research

Price erosion, higher R&D impacted profitability

Gross margin was hit by higher price erosion, unfavourable product mix, provision for new product inventory, one-off impairment charge and operational de-leveraging. While gross margin declined ~400bps, the dip in EBITDA margin was almost double due to higher R&D and SG&A expenses. DRRD benefitted from lower effective tax rate, higher other income and lower forex loss (loss of INR4.6bn in FY16 due to Venezuela).

Gross margin:
Global generics - 61.6%
(FY16 – 65.9%)
PSAI - 21% (FY16- 22%)

Higher spend due to:

- (1) focus on complex generics and differentiated products;
- (2) spends on in-licensed ANDAs from Teva; and
- (3) acquisition of R&D assets from XenoPort and Eisai

DRRD benefitted from lower remediation expenses, but EBITDA margin declined impacted by higher investment and rise in costs due to price controls under NLEM

Chart 8: Gross margin declined ~400bps

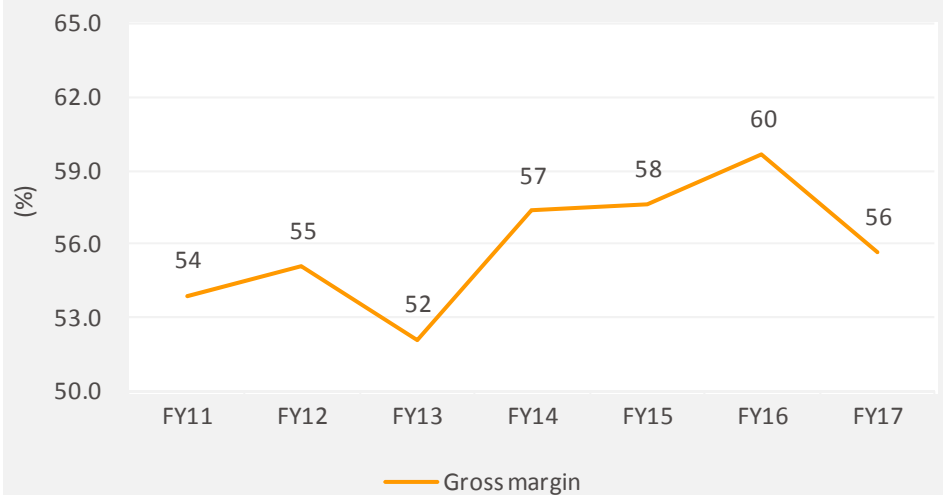


Chart 9: R&D spend highest at 14% of sales

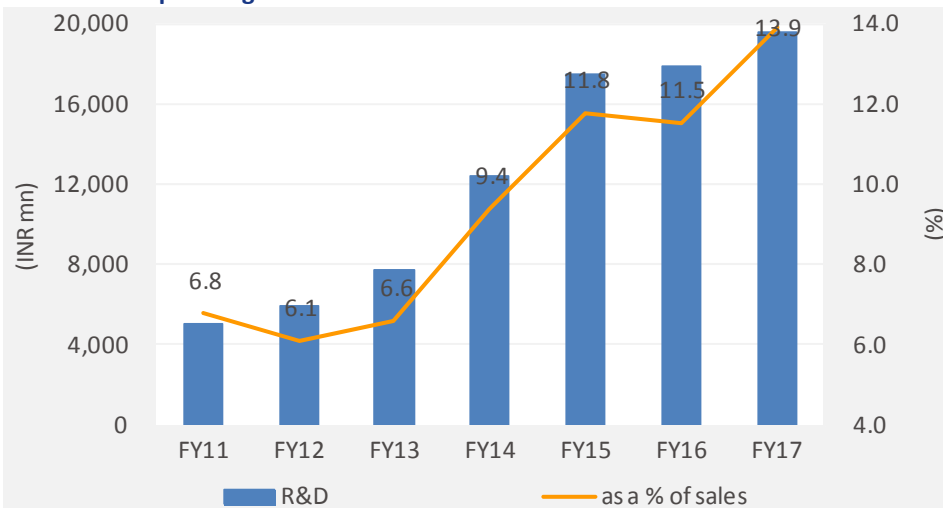
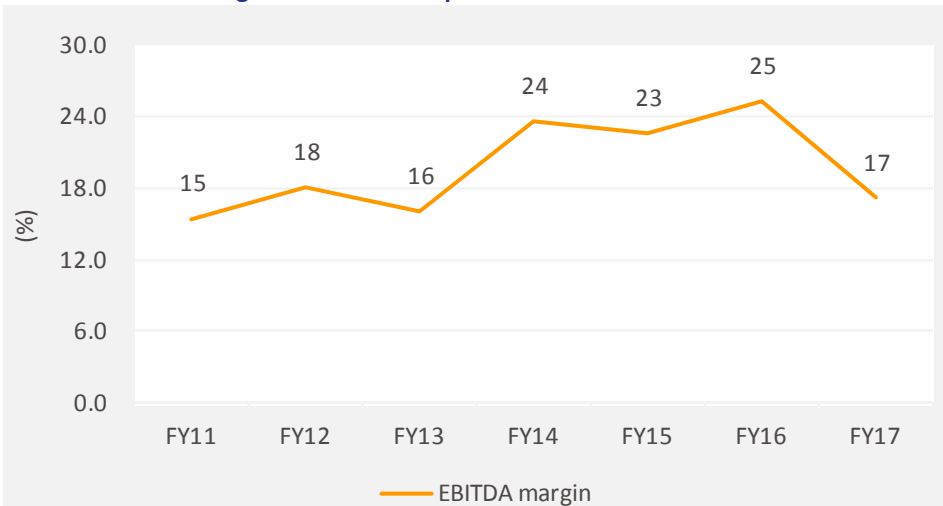


Chart 10: EBITDA margin declined ~800bps



Source: Company, Edelweiss research

Table 4: Tax expenses

	FY11	FY12	FY13	FY14	FY15	FY16	FY17	Comments
Cash tax paid	2,952	4,548	5,573	7,087	5,396	7,014	5,770	The effective tax rate for FY17 was lower by 8% compared to FY16 due to resolution of tax matter resulting in a reversal of INR1,370mn in income tax expense pertaining to earlier years.
cash tax rate (%)	23.7	24.6	25.7	26.6	19.2	25.8	39.4	
reported tax	1,403	4,204	4,900	5,094	5,984	7,127	2,614	
effective tax rate (%)	11.3	22.8	22.6	19.1	21.2	26.3	17.8	
deferred tax asset balance	(87)	833	1,814	3,310	4,013	4,230	4,373	

Source:

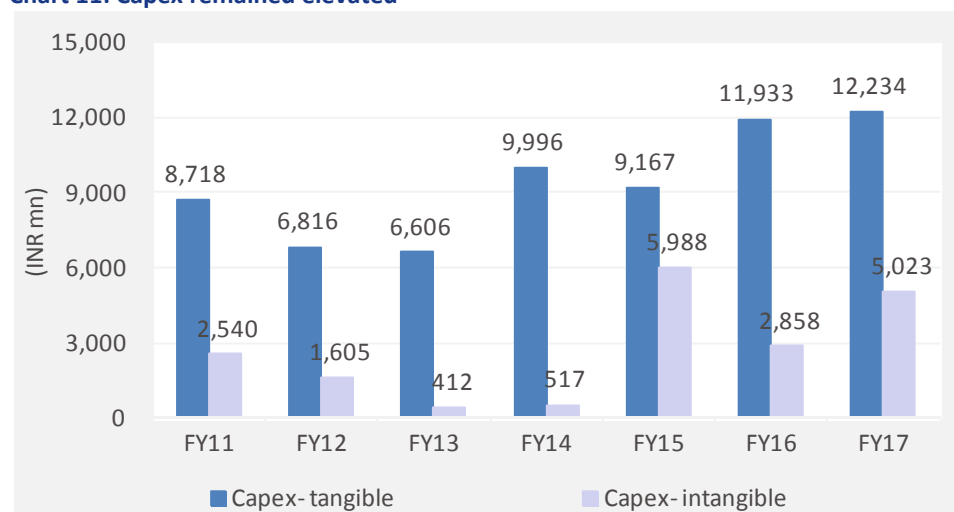
Table 5: Foreign Currency Translation reserve movement

	FY11	FY12	FY13	FY14	FY15	FY16	FY17
FCTR balance	2,921	3,737	3,928	4,477	4,455	4,424	4,233
adjustments during the year	362	816	191	549	(22)	(31)	(191)

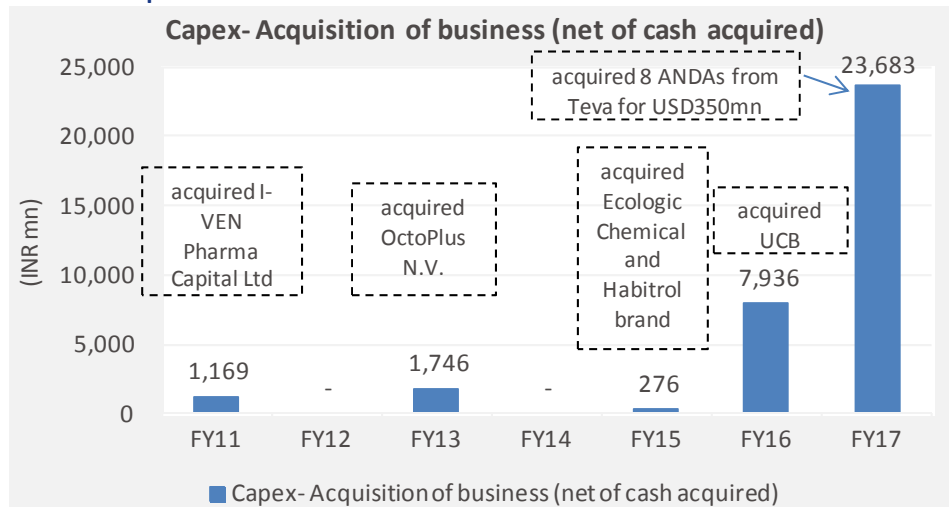
Source:

Capex remained elevated, working capital increased

In FY17, DRRD's high gestation organic capex continued. The company also acquired ANDAs from Teva for a consideration of USD350mn. As such, DRRD's capital efficiency trend-line continued to fall in FY17, primarily impacted by declining asset turnover ratio. In past few years, apart from high capital investments on R&D, the company has also sought to build its manufacturing capability for complex generics like sterile injectables that has seen low asset turnover ratio. DRRD's working capital, as a proportion to revenue, rose from 24.5% in FY16 to 29% in FY17, while the cash conversion cycle continued to rise during FY17.

Chart 11: Capex remained elevated

Source: Company, Edelweiss research

Chart 12: Acquired 8 ANDAs from Teva for USD350mn


Source: Company, Edelweiss research

Table 6: Working capital analysis

	FY11	FY12	FY13	FY14	FY15	FY16	FY17
Inventory days	170	149	134	148	144	149	158
Debtors days	86	81	90	90	91	97	103
Payable days	90	76	70	72	62	67	75
Cash Conversion Cycle	166	154	154	165	173	179	186
Working capital	19,048	24,218	33,577	40,152	45,009	37,915	40,888
Working capital to sales (%)	25.5	25.0	28.9	30.4	30.4	24.5	29.0

Source: Company, Edelweiss research

Debt jumps on buyback, acquisitions and lower operating cash flows

In FY17, DRRD's cash balance halved while debt increased to fund the company's cash deployment activities. Net debt increased by INR37,404mn. In addition to its usual capex and working capital investment, the company undertook 2 major capital deployment activities (aggregating to INR39bn) during FY17:

- Share buyback worth INR15,695mn (5mn equity shares); and
- Acquisition of 8 ANDAs worth USD350mn (INR23,666mn) from Teva, which was mainly funded via debt.

However, DRRD continued to generate positive free cash before considering acquisition of ANDAs.

DRRD's debt increased by INR15.6bn to fund buyback and acquire ANDAs

Debt to equity ratio at 0.4x
(FY16 - 0.26x)

Chart 13: Jump in debt to fund acquisition of ANDAs from Teva, and buyback

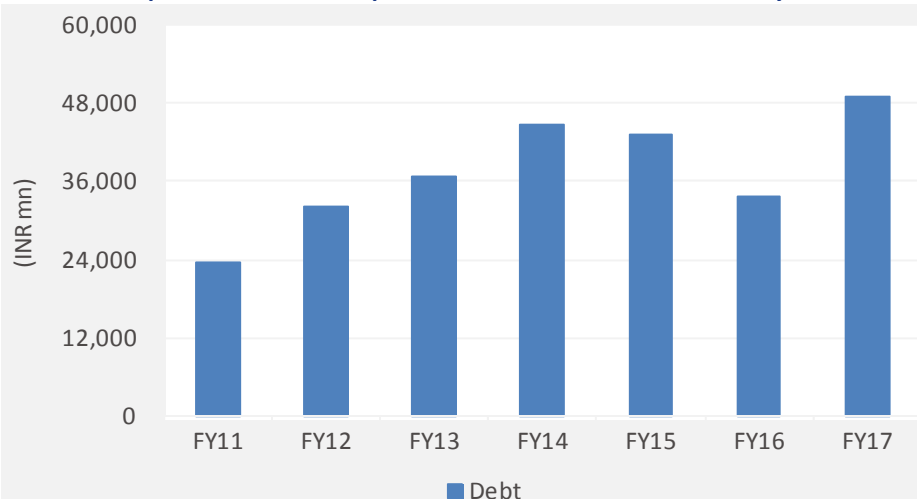


Chart 14: Cash balance halves

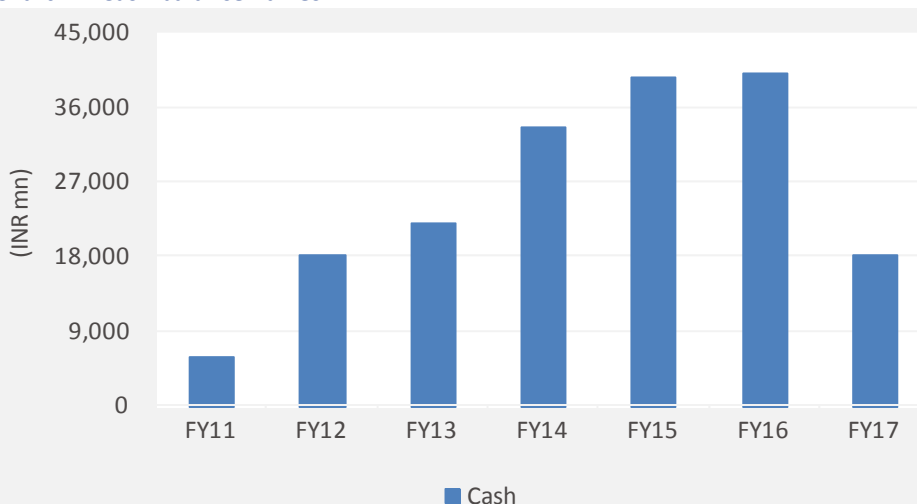


Table 7: Cash flow analysis

	FY11	FY12	FY13	FY14	FY15	FY16	FY17	Cumulative	%
Cash Profits generated	17,699	29,658	32,000	36,939	45,471	48,449	32,633	242,849	97.6
Change in debt (in CC)	3,548		2,293	3,957	352	(11,979)	16,316	14,487	5.8
Proceeds from issue of equity	29	7,054	1	2	206	1	(15,693)	(8,400)	(3.4)
Total funds generated	21,276	36,712	34,294	40,898	46,029	36,471	33,256	248,936	100.0
Less:									
Capex- Acquisition of business (net)	1,169		1,746		276	7,936	17	11,144	4.5
Capex- tangible	8,718	6,816	6,606	9,996	9,167	11,933	12,234	65,470	26.3
Capex- intangible	2,540	1,605	412	517	5,988	2,858	28,706	42,626	17.1
Purchase of investments	(3,642)	10,576	6,028	7,090	8,290	(1,021)	(21,858)	5,463	2.2
Working capital	6,738	8,960	13,146	10,389	15,040	188	5,350	59,811	24.0
Interest and dividend paid	3,302	2,993	3,127	3,168	3,860	3,740	3,687	23,877	9.6
Exchange rate differences	(141)	(499)	(94)	(771)	1,068	4,296	492	4,351	1.7
taxes paid	2,952	4,548	5,573	7,087	5,396	7,014	5,770	38,340	15.4
others	525		111	25				661	0.3
Total funds utilised	22,161	34,999	36,655	37,501	49,085	36,944	34,398	251,743	101.1
Increase in cash	(885)	1,713	(2,361)	3,397	(3,056)	(473)	(1,142)	(2,807)	(1.1)
Cash balance at year end	5,660	7,379	5,054	8,451	5,394	4,921	3,779		

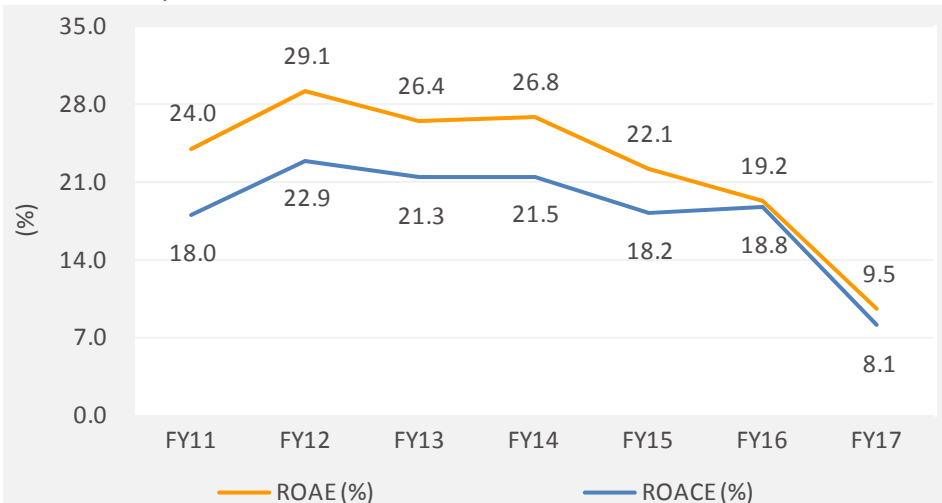
Source: Company, Edelweiss research

Table 8: Free cash flow analysis

	FY11	FY12	FY13	FY14	FY15	FY16	FY17
Operating cash flow	8,009	16,150	13,281	19,463	25,035	41,247	21,513
Capex	11,258	8,421	7,018	10,513	15,155	14,791	17,274
Free cash flow	(3,249)	7,729	6,263	8,950	9,880	26,456	4,239
acquisition	1,169	-	1,746	-	276	7,936	23,683
Free cash flow (after acquisitions)	(4,418)	7,729	4,517	8,950	9,604	18,520	(19,444)
Change in debt (in CC)	3,548	-	2,293	3,957	352	(11,979)	16,316

Source: Company, Edelweiss research

Chart 15: RoAE, RoACE continued to slide



Source: Company, Edelweiss research

Company Description

Dr. Reddy's is one of the largest Indian generic companies in the world with presence in more than 40 countries. USA is its largest market and contributes more than 40% of its revenues. It has one of the largest portfolios among Indian generic players and has enabled it to become a prominent generic player in the US. Russia and India are the two other key geographies, where it has significant presence. Apart from strengths in developing niche generic products, vertical integration into APIs has enabled it to become a global generic powerhouse. It operates 30 facilities (10 USFDA approved) and is actively supported by an extensive R&D programme. It also has one of the deepest pipelines of bio-similars amongst leading global generic companies, addressing global brand sales of USD30bn.

Investment Theme

Dr. Reddy's stands out with its world class R&D skills in developing technically complex/niche products which attract limited competition and is well set to capture the less-explored world of higher complexity generic products in the US. It is also among the leading players globally with a strong pipeline in the high potential biosimilars space which will be a long term growth driver. We believe that higher contribution from niche pipeline in US, strong growth in Russia & bounce back in India should drive strong earnings growth.

Key Risks

- Slowdown in ANDA approvals and USFDA related regulatory risks are part of the generics business
- Delay in bounce back in the PSAI business
- Failure to get approvals for Biosimilars and niche derma pipeline

Financial Statements

Key Assumptions

Year to March	FY16	FY17	FY18E	FY19E
Macro				
GDP(Y-o-Y %)	7.4	6.5	7.1	7.7
Inflation (Avg)	4.8	4.8	5.0	5.2
Repo rate (exit rate)	6.8	6.3	6.3	6.3
USD/INR (Avg)	65.0	67.5	67.0	67.0
Sector				
IPM growth (Y-o-Y) %	12.0	12.0	12.0	13.0
Company				
India sales (INR mn)	21,293	23,131	25,907	29,016
% change	19.2	8.6	12.0	12.0
US generics (USD mn)	1,139	942	1,030	1,300
Growth (YoY)%	18.7	(17.3)	9.3	26.2
Russia/ CIS growth(YoY)%	5.2	11.5	20.0	10.0
PSAI growth (YoY) %	(17.3)	(8.4)	5.9	3.0
EBITDA margins (%)	25.3	17.2	19.3	22.6
R&D (% of sales)	11.5	13.9	13.0	13.0
USD/INR (Avg)	65.0	67.5	67.0	67.0
Net debt to equity (x)	(0.1)	0.3	0.2	0.1

Income statement

(INR mn)

Year to March	FY16	FY17	FY18E	FY19E
Net revenue	154,708	140,809	156,429	181,939
Income from operations	154,708	140,809	156,429	181,939
Materials costs	62,427	62,453	69,454	78,234
R&D Cost	17,834	19,551	20,336	23,652
Total SG&A expenses	35,359	34,650	36,383	38,929
EBITDA	39,088	24,155	30,256	41,124
Operating profit	39,088	24,155	30,256	41,124
EBIT	28,745	12,433	18,506	29,349
Add: Other income	874.00	1,065.00	827.62	1,030.71
Less: Interest Expense	2,708	(806)	(1,000)	(1,000)
Add: Exceptional items	4,133	-	-	-
Profit Before Tax	26,911	14,304	20,334	31,380
Less: Provision for Tax	7,127	2,614	4,757	7,309
Associate profit share	229	349	350	400
Reported Profit	20,013	12,039	15,927	24,470
Exceptional Items	4,133	-	-	-
Adjusted Profit	23,061	12,039	15,927	24,470
Shares o /s (mn)	171	166	166	166
Adjusted Basic EPS	135.0	72.6	96.1	147.7
Diluted shares o/s (mn)	171	166	166	166
Adjusted Diluted EPS	135.0	72.6	96.1	147.7
Adjusted Cash EPS	195.5	143.4	167.0	218.7
Dividend per share (DPS)	20.0	20.0	26.4	40.6
Dividend Payout Ratio(%)	17.0	27.5	27.5	27.5

Common size metrics

Year to March	FY16	FY17	FY18E	FY19E
Operating expenses	74.7	82.8	80.7	77.4
Materials costs	40.4	44.4	44.4	43.0
S G & A expenses	22.9	24.6	23.3	21.4
R & D cost	11.5	13.9	13.0	13.0
Depreciation	6.7	8.3	7.5	6.5
Interest Expense	1.8	(0.6)	(0.6)	(0.5)
EBITDA margins	25.3	17.2	19.3	22.6
Net Profit margins	14.9	8.6	10.2	13.4

Growth ratios (%)

Year to March	FY16	FY17	FY18E	FY19E
Revenues	4.4	(9.0)	11.1	16.3
EBITDA	16.8	(38.2)	25.3	35.9
PBT	(3.8)	(46.8)	42.2	54.3
Adjusted Profit	3.1	(47.8)	32.3	53.6
EPS	3.1	(46.2)	32.3	53.6

Balance sheet		(INR mn)			
As on 31st March	FY16	FY17	FY18E	FY19E	
Share capital	853	828	828	828	
Reserves & Surplus	127,483	123,216	133,885	150,277	
Shareholders' funds	128,336	124,044	134,713	151,105	
Short term borrowings	22,828	43,649	43,649	43,649	
Long term borrowings	10,685	5,449	5,449	5,449	
Total Borrowings	33,513	49,098	49,098	49,098	
Long Term Liabilities	3,216	4,124	4,124	4,124	
Def. Tax Liability (net)	(4,230)	(4,376)	(4,376)	(4,376)	
Sources of funds	160,835	172,890	183,559	199,951	
Depreciation	10,343	11,722	11,750	11,775	
Net Block	53,961	57,160	57,410	57,636	
Intangible Assets	24,644	48,677	48,677	48,677	
Total Fixed Assets	78,605	105,837	106,087	106,313	
Non current investments	3,297	6,840	3,500	3,500	
Cash and Equivalents	39,955	18,136	20,690	25,768	
Inventories	25,578	28,529	31,727	35,738	
Sundry Debtors	41,306	38,065	42,287	49,184	
Loans & Advances	12,849	15,645	17,380	20,215	
Current Assets (ex cash)	79,733	82,239	91,395	105,136	
Trade payable	12,300	13,417	14,921	16,807	
Other Current Liab	29,518	27,934	24,693	25,458	
Total Current Liab	41,818	41,351	39,614	42,265	
Net Curr Assets-ex cash	37,915	40,888	51,781	62,871	
Uses of funds	160,835	172,890	183,559	199,951	
BVPS (INR)	751.1	748.5	812.9	911.8	

Free cash flow		(INR mn)			
Year to March	FY16	FY17	FY18E	FY19E	
Reported Profit	20,013	12,039	15,927	24,470	
Add: Depreciation	10,343	11,722	11,750	11,775	
Interest (Net of Tax)	1,991	(659)	(766)	(767)	
Others	9,940	(182)	(16,774)	(19,343)	
Less: Changes in WC	1,040	1,407	(5,917)	(9,021)	
Operating cash flow	41,247	21,513	16,053	25,155	
Less: Capex	22,727	40,957	12,000	12,000	
Free Cash Flow	18,520	(19,444)	4,053	13,155	

Cash flow metrics		FY16	FY17	FY18E	FY19E
Year to March					
Operating cash flow		41,247	21,513	16,053	25,155
Investing cash flow		(20,423)	(18,471)	(8,660)	(12,000)
Financing cash flow		(17,001)	(3,692)	(5,569)	(8,078)
Net cash Flow		3,823	(650)	1,824	5,077
Capex		(22,727)	(40,957)	(12,000)	(12,000)
Dividend paid		(3,740)	(3,687)	(5,258)	(8,078)

Profitability and efficiency ratios		FY16	FY17	FY18E	FY19E
Year to March					
ROAE (%)		19.2	9.5	12.3	17.1
ROACE (%)		18.8	8.1	10.8	15.8
Inventory Days		149	158	158	157
Debtors Days		97	103	94	92
Payable Days		67	75	74	74
Cash Conversion Cycle		179	186	178	175
Current Ratio		2.9	2.4	2.8	3.1
Gross Debt/EBITDA		0.9	2.0	1.6	1.2
Gross Debt/Equity		0.3	0.4	0.4	0.3
Adjusted Debt/Equity		0.3	0.4	0.4	0.3
Net Debt/Equity		(0.1)	0.2	0.2	0.2
Interest Coverage Ratio		10.6	(15.4)	(18.5)	(29.3)

Operating ratios		FY16	FY17	FY18E	FY19E
Year to March					
Total Asset Turnover		1.0	0.8	0.9	0.9
Fixed Asset Turnover		2.2	1.5	1.5	1.7
Equity Turnover		1.3	1.1	1.2	1.3

Valuation parameters		FY16	FY17	FY18E	FY19E
Year to March					
Adj. Diluted EPS (INR)		135.0	72.6	96.1	147.7
Y-o-Y growth (%)		3.1	(46.2)	32.3	53.6
Adjusted Cash EPS (INR)		195.5	143.4	167.0	218.7
Diluted P/E (x)		20.2	37.6	28.4	18.5
P/B (x)		3.6	3.6	3.4	3.0
EV / Sales (x)		2.8	3.3	2.9	2.5
EV / EBITDA (x)		11.8	20.0	15.9	11.6
Dividend Yield (%)		0.7	0.7	1.0	1.5

Peer comparison valuation

Name	Market cap (USD mn)	Diluted P/E (X)		EV / EBITDA (X)		ROAE (%)	
		FY18E	FY19E	FY18E	FY19E	FY18E	FY19E
Dr.Reddys Laboratories	7,015	28.4	18.5	15.9	11.6	12.3	17.1
Aurobindo Pharma	6,445	19.7	17.8	13.0	11.3	20.3	18.8
Cipla	6,857	25.1	21.7	15.1	12.1	13.1	13.6
Lupin	8,048	22.6	18.8	14.0	11.6	15.9	16.7
Sun Pharmaceuticals Industries	20,930	23.2	18.2	14.2	10.8	14.8	16.2
Median	-	23.2	18.5	14.2	11.6	14.8	16.7
AVERAGE	-	23.8	19.0	14.4	11.5	15.3	16.5

Source: Edelweiss research

Additional Data

Directors Data

Satish Reddy	Chairman	G V Prasad	Co-Chairman & CEO
Dr. Omkar Goswami	Independent Director	Ravi Bhoothalingam	Independent Director
Anupam Puri	Independent Director	J. P. Moreau	Independent Director
Kalpana Morparia	Independent Director	Bruce LA Carter	Independent Director
Ashok Ganguly	Independent Director	Sridar Iyengar	Independent Director

Auditors - B S R & Co., Chartered Accountants, and KPMG India

**as per last annual report*

Holding – Top10

	Perc. Holding		Perc. Holding
Commonwealth Bank of Australia	9.65	Franklin Resources	1.42
Blackrock	7.27	Teluk Kamang Invest	1.25
Massachusetts Mutual Life	3.26	Vanguard group	1.03
Templeton asset management	1.76	ICICI Prudential Life Insurance	0.97
GIC Private Ltd	1.44	Reliance Capital Trustee	0.93

**in last one year*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
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No Data Available

**in last one year*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
17 Jan 2017	G V Prasad	Sell	212000.00
17 Jan 2017	K Satish Reddy	Sell	212000.00
17 Jan 2017	Dr. Reddy's Holdings Limited	Buy	424000.00
10 Oct 2016	G V Prasad	Buy	20800.00
05 Oct 2016	G V Prasad	Buy	66000.00

**in last one year*

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Aurobindo Pharma	HOLD	SP	H	Cadila Healthcare	BUY	SO	M
Cipla	HOLD	SP	L	Divi's Laboratories	HOLD	SO	M
Dr.Reddys Laboratories	HOLD	SP	M	Glenmark Pharmaceuticals	HOLD	SP	M
Ipca Laboratories	REDUCE	SU	M	Lupin	HOLD	SP	M
Natco Pharma	BUY	SO	M	Sun Pharmaceuticals Industries	BUY	SO	M
Torrent Pharmaceuticals	BUY	SO	H				

ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return

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Aditya Narain

Head of Research

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Coverage group(s) of stocks by primary analyst(s): Pharmaceuticals

Aurobindo Pharma, Cadila Healthcare, Cipla, Divi's Laboratories, Dr.Reddys Laboratories, Glenmark Pharmaceuticals, Ipca Laboratories, Lupin, Natco Pharma, Sun Pharmaceuticals Industries, Torrent Pharmaceuticals

Recent Research

Date	Company	Title	Price (INR)	Recos
05-Jul-17	Pharma	INR appreciation further mars lethargic performance; Q1FY18 Result Preview		
07-Jun-17	Cadila Healthcare	gLiAlda approved, strong tailwind ahead; Event Update	490	Buy
01-Jun-17	Fortis Healthcare	Demonetisation dent; Result Update	198	Buy

Distribution of Ratings / Market Cap

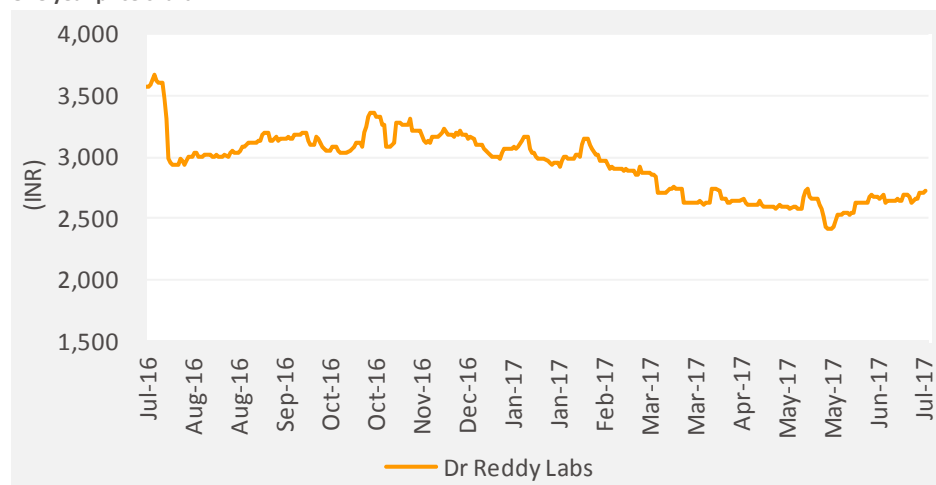
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart



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