

Dr. Reddy's Laboratories (DRRD IN)

Rating: ACCUMULATE | CMP: Rs5,160 | TP: Rs5,648

gKuvan in US: Silent launch, strong potential

Quick Pointers:

- Kuvan to remain a three player market in US at least until FY24E, as there are no pending ANDA's.
- Global sales of US\$463m as on CY-19 with likely US sales of US\$360-380m.

DRRD and Endo (Par) pharma recently launched gKuvan as per their settlement agreement with the innovator BioMarin Pharmaceuticals. We believe gKuvan's contribution to DRRD earnings will be sustainable over FY21-FY24E as there are no generic filers and pending ANDA's. While Endo launched both Tab and PFOS (powder) form, DRRD launched only the tab form and we assume the PFOS form to be also launched soon. The US market of Kuvan is equally divided between Tab and PFOS forms. Following BioMarin's co-pay assistance program, DRRD also offered co-pay assistance while Endo is yet to offer a similar strategy after its launch on 1st Oct CY20. However, considering the early days of launch there is still limited information on their co-pay strategy. We anticipate Kuvan to remain a three-player market and DRRD may likely capture gradually 20-40% market share with 50-80% price erosion from the branded market and may reach its peak sales up to US\$45m. This leads to an EPS contribution of Rs2.0/9.90/7.30 for FY21/22/23E. With limited information on the co-pay program and strategy to gain Rx traction for gKuvan, we wait for further clarity on their strategy (profitability in co-pay program) for US and EU (market size US\$80-100m) before discounting in our earnings estimates. We have an Accumulate rating with TP of Rs5,648 based on 24x(PE) of FY23E and Rs 262/share benefit from gRevlimid (using NPV method) over FY23-26E.

Genesis of drug: KUVAN (Sapropterin dihydrochloride) is available in two dosing forms (tablets and powder) and it's prescribed to lower blood Phe levels in adults and children over one month of age with a certain type of Phenylketonuria (PKU). It is the first and only FDA-approved medication for PKU.

Approval history and competitive scenario: In CY-07 (December) Kuvan tablet dosage received marketing approval from the US Food and Drug Administration making it the first specific therapy for treatment of PKU patients, similarly powder form was approved in CY-13 (December). Kuvan was developed by BioMarin Pharmaceutical in partnership with Merck Serono, a division of Merck while in CY-15 BioMarin acquired the global rights to Kuvan Merck.

Kuvan last patents expires in CY-24 and CY-32 (its dry blend formulations) but between CY-14 and CY-16, DRRD and Endo Pharma filed generic applications with the FDA to market their copycats. BioMarin sued filers for patent infringement. However, between CY-15 and CY-17 the innovator settled patent infringement case and granted licenses to launch generic in CY-20 (Oct).

October 5, 2020

Event Update

■ Change in Estimates | ■ Target | ■ Reco

Change in Estimates

	Current		Previous	
	FY22E	FY23E	FY22E	FY23E
Rating	ACCUMULATE		ACCUMULATE	
Target Price	5,648		5,648	
Sales (Rs. m)	2,06,129	2,29,269	2,06,129	2,29,269
% Chng.	-	-	-	-
EBITDA (Rs. m)	50,502	57,890	50,502	57,890
% Chng.	-	-	-	-
EPS (Rs.)	191.2	224.4	191.2	224.4
% Chng.	-	-	-	-

Key Financials - Consolidated

Y/e Mar	FY20	FY21E	FY22E	FY23E
Sales (Rs. bn)	168	182	206	229
EBITDA (Rs. bn)	34	43	51	58
Margin (%)	20.3	23.6	24.5	25.3
PAT (Rs. bn)	26	27	32	38
EPS (Rs.)	157.2	161.4	191.2	224.4
Gr. (%)	33.8	2.7	18.4	17.4
DPS (Rs.)	23.6	31.5	38.1	44.8
Yield (%)	0.5	0.6	0.7	0.9
RoE (%)	17.6	16.1	17.1	17.5
RoCE (%)	12.8	17.1	18.9	20.0
EV/Sales (x)	5.1	4.6	4.0	3.5
EV/EBITDA (x)	25.0	19.4	16.3	14.0
PE (x)	32.8	32.0	27.0	23.0
P/BV (x)	5.5	4.8	4.2	3.7

Key Data

REDY.BO | DRRD IN

52-W High / Low	Rs.5,515 / Rs.2,495
Sensex / Nifty	38,974 / 11,503
Market Cap	Rs.858bn/ \$ 11,703m
Shares Outstanding	166m
3M Avg. Daily Value	Rs.20783.53m

Shareholding Pattern (%)

Promoter's	26.74
Foreign	29.33
Domestic Institution	14.87
Public & Others	29.06
Promoter Pledge (Rs bn)	-

Stock Performance (%)

	1M	6M	12M
Absolute	19.4	64.0	97.1
Relative	19.7	18.9	93.7

Surajit Pal

surajitpal@plindia.com | 91-22-66322259

Tausif Shaikh

tausifshaikh@plindia.com | 91-22-66322246

Exhibit 1: Key launches for DRRD over FY21-23E

Drug(API)	Market Size (US\$)	Potential Launch Date	Market share	Limited competition period	EPS Contribution in FY23E	NPV/Share	Competitive Status
Revlimid (Lenalidomide)	7.8b	FY23E	5-12%	FY23-26	-	262	Natco/Teva would be first to launch in CY22-March followed by Alvogen and DRRD. Many filers are also seeking approval for Revlimid which could change competitive environment at a fast pace.
Copaxone (Glatiramer acetate)	1.5b	FY22E	15-20%	FY22-23E	8.20	-	Currently it a 3 player market (Teva, Novartis and Natco/Mylan) with innovator having market share of 55-60% in 40mg. DRRD submitted response (of CRL) to FDA. Expected launch in Q1FY22E. Synthon / Pfizer, Amneal and Biocon are few known filers.
Nuvaring (etonogestrel/ethinyl estradiol vaginal ring)	742m	FY22E	15%	FY22-23E	7.70	-	Anmeal launched 1st generic post approval in Dec (CY-19) followed up by launch of own generic by Merck. DRRD response to CRL (received in CY19) is in W-I-P. Post submission of response, final approval is expected in 8-10 months. Expect approval/launch in FY22E though it may compete with improved medicine Annovera (new approved).
Vascepa (icosapent ethyl)	429m	FY21E(3Q)	15%	FY21-22E	0.50	-	Hikma and DRRD recently received favorable outcome from the higher court. Hikma, DRRD and Teva received approval and expect planned launch in FY21E.

Source: Company, PL

Financials

Income Statement (Rs m)

Y/e Mar	FY20	FY21E	FY22E	FY23E
Net Revenues	1,67,684	1,82,253	2,06,129	2,29,269
YoY gr. (%)	8.5	8.7	13.1	11.2
Cost of Goods Sold	55,544	55,295	63,900	71,073
Gross Profit	1,12,140	1,26,957	1,42,229	1,58,196
Margin (%)	66.9	69.7	69.0	69.0
Employee Cost	33,802	35,448	37,103	39,549
Other Expenses	15,410	15,947	17,521	19,488
EBITDA	33,985	43,085	50,502	57,890
YoY gr. (%)	6.9	26.8	17.2	14.6
Margin (%)	20.3	23.6	24.5	25.3
Depreciation and Amortization	11,631	11,867	12,498	13,086
EBIT	22,354	31,218	38,004	44,804
Margin (%)	13.3	17.1	18.4	19.5
Net Interest	983	922	709	527
Other Income	2,793	3,308	3,440	3,543
Profit Before Tax	24,164	33,603	40,734	47,821
Margin (%)	14.4	18.4	19.8	20.9
Total Tax	(1,403)	7,393	8,961	10,521
Effective tax rate (%)	(5.8)	22.0	22.0	22.0
Profit after tax	25,567	26,210	31,773	37,300
Minority interest	(561)	(617)	(679)	(747)
Share Profit from Associate	-	-	-	-
Adjusted PAT	26,128	26,827	32,451	38,047
YoY gr. (%)	34.0	2.7	21.0	17.2
Margin (%)	15.6	14.7	15.7	16.6
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	26,128	26,827	32,451	38,047
YoY gr. (%)	34.0	2.7	21.0	17.2
Margin (%)	15.6	14.7	15.7	16.6
Other Comprehensive Income	-	-	-	-
Total Comprehensive Income	26,128	26,827	32,451	38,047
Equity Shares O/s (m)	166	166	166	166
EPS (Rs)	157.2	161.4	191.2	224.4

Source: Company Data, PL Research

Balance Sheet Abstract (Rs m)

Y/e Mar	FY20	FY21E	FY22E	FY23E
Non-Current Assets				
Gross Block	1,56,149	1,76,225	1,96,972	2,18,345
Tangibles	1,10,619	1,31,486	1,52,984	1,75,070
Intangibles	45,530	44,739	43,988	43,275
Acc: Dep / Amortization	92,559	1,04,426	1,16,924	1,30,010
Tangibles	62,840	74,707	87,205	1,00,291
Intangibles	29,719	29,719	29,719	29,719
Net fixed assets	63,590	71,799	80,048	88,335
Tangibles	47,779	56,779	65,779	74,779
Intangibles	15,811	15,020	14,269	13,556
Capital Work In Progress	15,351	11,513	8,635	6,476
Goodwill	4,913	4,176	3,550	3,017
Non-Current Investments	5,621	3,389	3,514	3,757
Net Deferred tax assets	12,179	11,936	11,698	11,464
Other Non-Current Assets	4,588	4,359	4,141	3,934
Current Assets				
Investments	23,687	27,240	31,326	36,025
Inventories	35,067	39,951	42,013	44,305
Trade receivables	50,278	45,554	51,768	57,791
Cash & Bank Balance	2,053	8,693	9,706	12,431
Other Current Assets	10,424	10,945	11,492	12,067
Total Assets	2,32,253	2,44,506	2,63,332	2,85,586
Equity				
Equity Share Capital	831	831	831	831
Other Equity	1,55,157	1,76,209	2,01,764	2,31,801
Total Network	1,55,988	1,77,040	2,02,595	2,32,632
Non-Current Liabilities				
Long Term borrowings	1,304	978	734	-
Provisions	745	842	842	842
Other non current liabilities	2,055	1,541	1,156	867
Current Liabilities				
ST Debt / Current of LT Debt	16,532	12,399	7,439	3,720
Trade payables	15,248	15,663	17,168	18,492
Other current liabilities	40,361	35,771	33,104	28,712
Total Equity & Liabilities	2,32,253	2,44,505	2,63,333	2,85,586

Source: Company Data, PL Research



Cash Flow (Rs m)

Y/e Mar	FY20	FY21E	FY22E	FY23E
PBT	18,857	34,220	41,413	48,567
Add. Depreciation	11,631	11,867	12,498	13,086
Add. Interest	983	922	709	527
Less Financial Other Income	2,793	3,308	3,440	3,543
Add. Other	14,011	(449)	(3,349)	(3,573)
Op. profit before WC changes	45,482	46,560	51,272	58,607
Net Changes-WC	(8,536)	(5,276)	(10,451)	(12,475)
Direct tax	(7,105)	(7,393)	(8,961)	(10,521)
Net cash from Op. activities	29,841	33,892	31,859	35,611
Capital expenditures	(5,725)	(16,239)	(17,869)	(19,214)
Interest / Dividend Income	1,12,720	3,308	3,440	3,543
Others	(1,11,918)	(3,619)	(4,165)	(4,793)
Net Cash from Invt. activities	(4,923)	(16,550)	(18,594)	(20,464)
Issue of share cap. / premium	(470)	-	-	-
Debt changes	(19,165)	(4,459)	(5,204)	(4,453)
Dividend paid	(3,916)	(5,229)	(6,339)	(7,442)
Interest paid	(1,608)	(922)	(709)	(527)
Others	(25)	-	-	-
Net cash from Fin. activities	(25,184)	(10,611)	(12,253)	(12,422)
Net change in cash	(266)	6,731	1,013	2,725
Free Cash Flow	24,116	17,653	13,990	16,397

Source: Company Data, PL Research

Quarterly Financials (Rs m)

Y/e Mar	Q2FY20	Q3FY20	Q4FY20	Q1FY21
Net Revenue	40,899	43,971	44,489	44,265
YoY gr. (%)	7.1	13.8	10.4	14.7
Raw Material Expenses	14,011	14,153	15,311	13,196
Gross Profit	26,888	29,818	29,178	31,069
Margin (%)	65.7	67.8	65.6	70.2
EBITDA	6,969	10,313	9,499	11,213
YoY gr. (%)	(8.2)	28.2	16.0	51.2
Margin (%)	17.0	23.5	21.4	25.3
Depreciation / Depletion	3,131	2,869	2,748	2,923
EBIT	3,838	7,444	6,751	8,290
Margin (%)	9.4	16.9	15.2	18.7
Net Interest	303	152	230	233
Other Income	540	673	736	871
Profit before Tax	4,075	7,965	7,257	8,928
Margin (%)	10.0	18.1	16.3	20.2
Total Tax	(3,207)	325	(449)	3,059
Effective tax rate (%)	(78.7)	4.1	(6.2)	34.3
Profit after Tax	7,282	7,640	7,706	5,869
Minority interest	(117)	(176)	(105)	(77)
Share Profit from Associates	-	-	-	-
Adjusted PAT	7,399	7,816	7,811	5,946
YoY gr. (%)	42.8	56.2	71.5	79.7
Margin (%)	18.1	17.8	17.6	13.4
Extra Ord. Income / (Exp)	-	-	-	-
Reported PAT	7,399	7,816	7,811	5,946
YoY gr. (%)	42.8	56.2	71.5	79.7
Margin (%)	18.1	17.8	17.6	13.4
Other Comprehensive Income	-	454	1,263	782
Total Comprehensive Income	7,399	8,270	9,074	6,728
Avg. Shares O/s (m)	166	166	166	166
EPS (Rs)	44.6	47.1	47.1	35.8

Source: Company Data, PL Research

Key Financial Metrics

Y/e Mar	FY20	FY21E	FY22E	FY23E
Per Share(Rs)				
EPS	157.2	161.4	191.2	224.4
CEPS	227.2	232.8	270.5	307.7
BVPS	938.6	1,065.2	1,219.0	1,399.7
FCF	145.1	106.2	84.2	98.7
DPS	23.6	31.5	38.1	44.8
Return Ratio(%)				
RoCE	12.8	17.1	18.9	20.0
ROIC	10.8	15.0	17.1	18.9
RoE	17.6	16.1	17.1	17.5
Balance Sheet				
Net Debt : Equity (x)	(0.1)	(0.1)	(0.2)	(0.2)
Net Working Capital (Days)	153	140	136	133
Valuation(x)				
PER	32.8	32.0	27.0	23.0
P/B	5.5	4.8	4.2	3.7
P/CEPS	22.7	22.2	19.1	16.8
EV/EBITDA	25.0	19.4	16.3	14.0
EV/Sales	5.1	4.6	4.0	3.5
Dividend Yield (%)	0.5	0.6	0.7	0.9

Source: Company Data, PL Research

Key Operating Metrics

Y/e Mar	FY20	FY21E	FY22E	FY23E
India Formulations	28,946	30,393	34,040	38,466
US formulations	64,659	74,393	86,120	94,799
Russia	23,424	20,683	23,663	27,144
PSAI	25,747	31,411	33,610	35,963

Source: Company Data, PL Research

Price Chart
Recommendation History


No.	Date	Rating	TP (Rs.)	Share Price (Rs.)
1	24-Sep-20	Accumulate	5,648	5,108
2	29-Jul-20	Hold	4,326	4,306
3	08-Jul-20	Accumulate	4,326	3,887
4	21-May-20	Accumulate	4,326	3,915
5	18-Apr-20	Accumulate	4,030	3,930
6	14-Apr-20	Accumulate	3,331	3,622
7	27-Jan-20	Accumulate	3,331	3,200
8	03-Jan-20	Accumulate	2,910	2,884
9	01-Nov-19	Accumulate	2,910	2,757
10	22-Oct-19	Accumulate	2,997	2,820

Analyst Coverage Universe

Sr. No.	Company Name	Rating	TP (Rs)	Share Price (Rs)
1	Aurobindo Pharma	Hold	838	881
2	Cadila Healthcare	Sell	329	396
3	Cipla	Reduce	657	729
4	Dr. Lal PathLabs	Sell	1,006	1,892
5	Dr. Reddy's Laboratories	Accumulate	5,648	5,108
6	Eris Lifesciences	BUY	576	511
7	Glenmark Pharmaceuticals	Sell	365	481
8	Indoco Remedies	Hold	243	262
9	Ipca Laboratories	Hold	1,962	2,013
10	Jubilant Life Sciences	Sell	446	830
11	Lupin	BUY	1,085	1,007
12	Sun Pharmaceutical Industries	Reduce	479	532
13	Thyrocare Technologies	Sell	307	677

PL's Recommendation Nomenclature (Absolute Performance)

Buy	: > 15%
Accumulate	: 5% to 15%
Hold	: +5% to -5%
Reduce	: -5% to -15%
Sell	: < -15%
Not Rated (NR)	: No specific call on the stock
Under Review (UR)	: Rating likely to change shortly



ANALYST CERTIFICATION

(Indian Clients)

We/I, Mr. Surajit Pal- PGDBA, CFA, M.Com, Mr. Tausif Shaikh- BA, Major in Economics, Financial Management Research Analysts, authors and the names subscribed to this report, hereby certify that all of the views expressed in this research report accurately reflect our views about the subject issuer(s) or securities. We also certify that no part of our compensation was, is, or will be directly or indirectly related to the specific recommendation(s) or view(s) in this report.

(US Clients)

The research analysts, with respect to each issuer and its securities covered by them in this research report, certify that: All of the views expressed in this research report accurately reflect his or her or their personal views about all of the issuers and their securities; and No part of his or her or their compensation was, is or will be directly related to the specific recommendation or views expressed in this research report.

DISCLAIMER

Indian Clients

Prabhudas Lilladher Pvt. Ltd, Mumbai, India (hereinafter referred to as "PL") is engaged in the business of Stock Broking, Portfolio Manager, Depository Participant and distribution for third party financial products. PL is a subsidiary of Prabhudas Lilladher Advisory Services Pvt Ltd. which has its various subsidiaries engaged in business of commodity broking, investment banking, financial services (margin funding) and distribution of third party financial/other products, details in respect of which are available at www.plindia.com.

This document has been prepared by the Research Division of PL and is meant for use by the recipient only as information and is not for circulation. This document is not to be reported or copied or made available to others without prior permission of PL. It should not be considered or taken as an offer to sell or a solicitation to buy or sell any security.

The information contained in this report has been obtained from sources that are considered to be reliable. However, PL has not independently verified the accuracy or completeness of the same. Neither PL nor any of its affiliates, its directors or its employees accepts any responsibility of whatsoever nature for the information, statements and opinion given, made available or expressed herein or for any omission therein.

Recipients of this report should be aware that past performance is not necessarily a guide to future performance and value of investments can go down as well. The suitability or otherwise of any investments will depend upon the recipient's particular circumstances and, in case of doubt, advice should be sought from an independent expert/advisor.

Either PL or its affiliates or its directors or its employees or its representatives or its clients or their relatives may have position(s), make market, act as principal or engage in transactions of securities of companies referred to in this report and they may have used the research material prior to publication.

PL may from time to time solicit or perform investment banking or other services for any company mentioned in this document.

PL is in the process of applying for certificate of registration as Research Analyst under Securities and Exchange Board of India (Research Analysts) Regulations, 2014

PL submits that no material disciplinary action has been taken on us by any Regulatory Authority impacting Equity Research Analysis activities.

PL or its research analysts or its associates or his relatives do not have any financial interest in the subject company.

PL or its research analysts or its associates or his relatives do not have actual/beneficial ownership of one per cent or more securities of the subject company at the end of the month immediately preceding the date of publication of the research report.

PL or its research analysts or its associates or his relatives do not have any material conflict of interest at the time of publication of the research report.

PL or its associates might have received compensation from the subject company in the past twelve months.

PL or its associates might have managed or co-managed public offering of securities for the subject company in the past twelve months or mandated by the subject company for any other assignment in the past twelve months.

PL or its associates might have received any compensation for investment banking or merchant banking or brokerage services from the subject company in the past twelve months.

PL or its associates might have received any compensation for products or services other than investment banking or merchant banking or brokerage services from the subject company in the past twelve months

PL or its associates might have received any compensation or other benefits from the subject company or third party in connection with the research report.

PL encourages independence in research report preparation and strives to minimize conflict in preparation of research report. PL or its analysts did not receive any compensation or other benefits from the subject Company or third party in connection with the preparation of the research report. PL or its Research Analysts do not have any material conflict of interest at the time of publication of this report.

It is confirmed that Mr. Surajit Pal- PGDBA, CFA, M.Com, Mr. Tausif Shaikh- BA, Major in Economics, Financial Management Research Analysts of this report have not received any compensation from the companies mentioned in the report in the preceding twelve months

Compensation of our Research Analysts is not based on any specific merchant banking, investment banking or brokerage service transactions.

The Research analysts for this report certifies that all of the views expressed in this report accurately reflect his or her personal views about the subject company or companies and its or their securities, and no part of his or her compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this report.

The research analysts for this report has not served as an officer, director or employee of the subject company PL or its research analysts have not engaged in market making activity for the subject company

Our sales people, traders, and other professionals or affiliates may provide oral or written market commentary or trading strategies to our clients that reflect opinions that are contrary to the opinions expressed herein, and our proprietary trading and investing businesses may make investment decisions that are inconsistent with the recommendations expressed herein. In reviewing these materials, you should be aware that any or all of the foregoing, among other things, may give rise to real or potential conflicts of interest.

PL and its associates, their directors and employees may (a) from time to time, have a long or short position in, and buy or sell the securities of the subject company or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as a market maker in the financial instruments of the subject company or act as an advisor or lender/borrower to the subject company or may have any other potential conflict of interests with respect to any recommendation and other related information and opinions.

US Clients

This research report is a product of Prabhudas Lilladher Pvt. Ltd., which is the employer of the research analyst(s) who has prepared the research report. The research analyst(s) preparing the research report is/are resident outside the United States (U.S.) and are not associated persons of any U.S. regulated broker-dealer and therefore the analyst(s) is/are not subject to supervision by a U.S. broker-dealer, and is/are not required to satisfy the regulatory licensing requirements of FINRA or required to otherwise comply with U.S. rules or regulations regarding, among other things, communications with a subject company, public appearances and trading securities held by a research analyst account.

This report is intended for distribution by Prabhudas Lilladher Pvt. Ltd. only to "Major Institutional Investors" as defined by Rule 15a-6(b)(4) of the U.S. Securities and Exchange Act, 1934 (the Exchange Act) and interpretations thereof by U.S. Securities and Exchange Commission (SEC) in reliance on Rule 15a 6(a)(2). If the recipient of this report is not a Major Institutional Investor as specified above, then it should not act upon this report and return the same to the sender. Further, this report may not be copied, duplicated and/or transmitted onward to any U.S. person, which is not the Major Institutional Investor.

In reliance on the exemption from registration provided by Rule 15a-6 of the Exchange Act and interpretations thereof by the SEC in order to conduct certain business with Major Institutional Investors, Prabhudas Lilladher Pvt. Ltd. has entered into an agreement with a U.S. registered broker-dealer, Marco Polo Securities Inc. ("Marco Polo").

Transactions in securities discussed in this research report should be effected through Marco Polo or another U.S. registered broker dealer.

Prabhudas Lilladher Pvt. Ltd.

3rd Floor, Sadhana House, 570, P. B. Marg, Worli, Mumbai-400 018, India | Tel: (91 22) 6632 2222 Fax: (91 22) 6632 2209

www.plindia.com