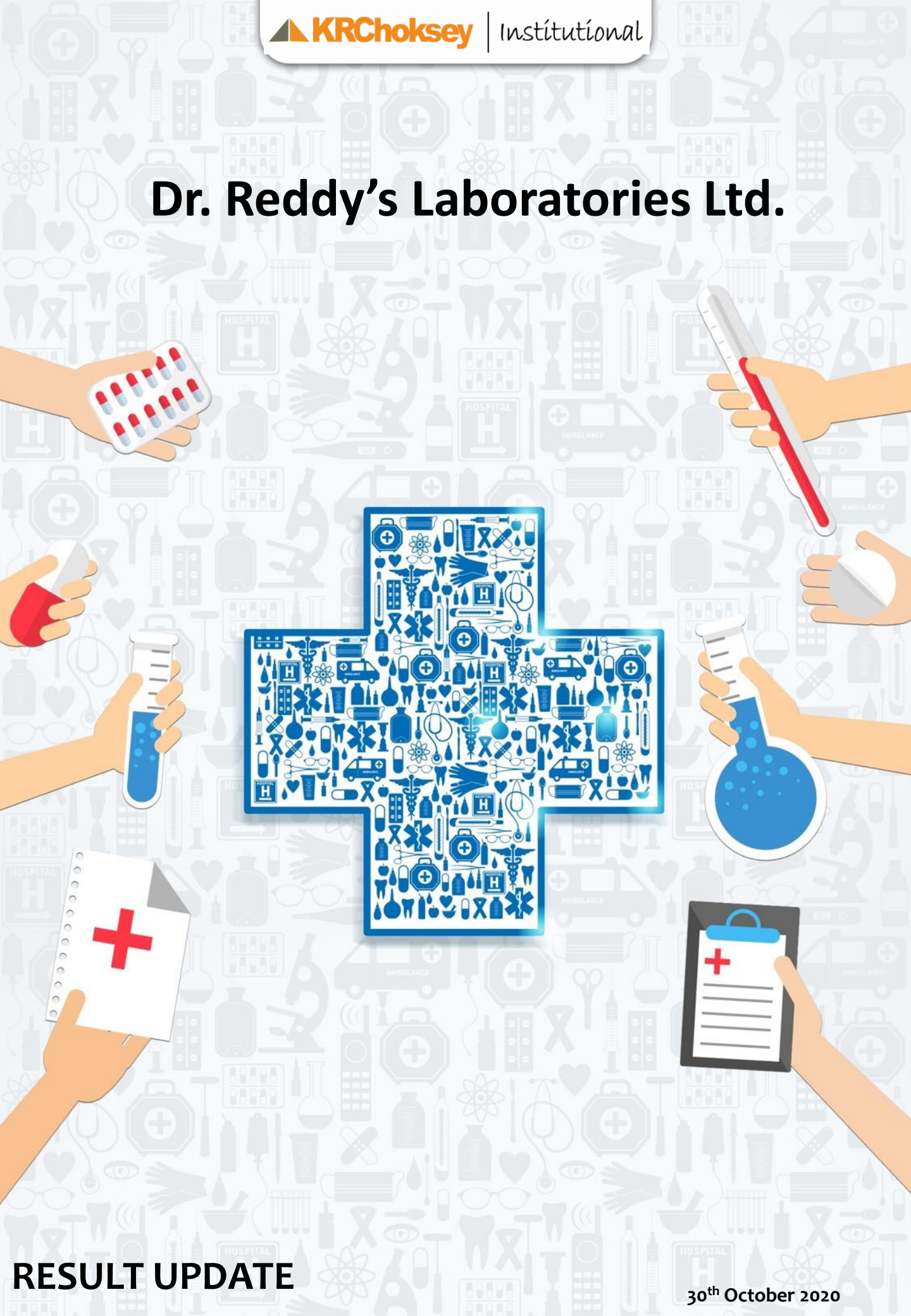


Dr. Reddy's Laboratories Ltd.



Dr. Reddy's Laboratories Ltd.

Continued broad based growth; margin contraction on high base

CMP INR 4,942	Target INR 5,418	Potential Upside 10.0%	Market Cap (INR Mn) INR 8,21,352	Recommendation ACCUMULATE	Sector Pharmaceuticals
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Result Highlights of Q2FY21

- Dr. Reddy's laboratories reported Revenue growth of 2.0% YoY (up 10.9% QoQ) to INR 49,109 mn in Q2FY21.
- EBITDA declined 13.1% YoY (up 10.1% QoQ) to INR 12,342 mn while EBITDA margin contracted by 437 bps YoY to 25.1% in Q2FY21 (from 29.5% in Q2FY20).
- Company reported PAT of INR 7,718 mn, a decline of 30.3% YoY (up 29.8% QoQ). Net Profit Margin contracted 728bps YoY (+228 bps QoQ).
- R&D expenses were 8.9% of revenue (INR 4.4 bn) in Q2FY21 as against 7.6% (INR 4.5 bn) in Q2FY20. Capex for the quarter was INR 2.5 bn.

MARKET DATA

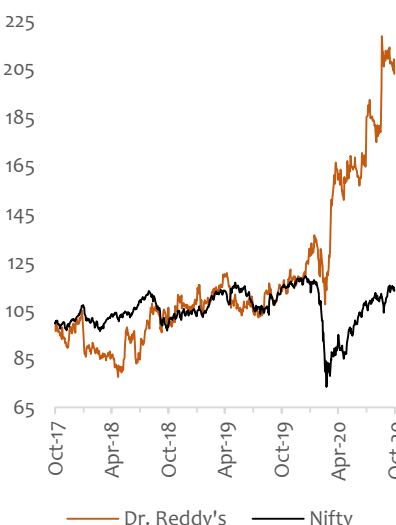
Shares outs (Mn)	166
Equity Cap (INR Mn)	1,55,988
Mkt Cap (INR Mn)	8,21,352
52 Wk H/L (INR)	5,513/2,495
Volume Avg (3m K)	2,523
Face Value (INR)	5
Bloomberg Code	DRRD IN

KEY FINANCIALS

INR Millions	FY18	FY19	FY20	FY21E	FY22E
Revenue	1,42,810	1,54,482	1,75,170	1,92,737	2,18,227
EBITDA	23,512	31,898	41,471	48,955	52,375
PAT	9,468	19,500	20,260	29,625	32,745
Adjusted PAT	9,468	19,500	38,313	30,234	32,745
EPS (INR)	57.1	117.5	121.9	178.2	197.0
Adj EPS (INR)	57.0	117.5	230.5	181.9	197.0
EBITDA Margin	16.5%	20.6%	23.7%	25.4%	24.0%
NPM	6.6%	12.6%	11.6%	15.4%	15.0%
Adjusted NPM	6.6%	12.6%	21.9%	15.7%	15.0%

Source: Company, KRChoksey Research

SHARE PRICE PERFORMANCE



SENSEX	39,750
NIFTY	11,671

Strong broad-based growth; led by mix of new launches/volume growth & COVID-19 drugs: Dr. Reddy's beat our Q2FY21 estimates with positive deviation of 6%/15%/36% in Revenue/EBITDA/Adj PAT. Revenue growth was seen across the geographies with North America (+28%/+6.1% YoY/QoQ, 37% of revenue), India (+21%/+46% YoY/QoQ, 19% of revenue), and Europe (+36%/+5.7% YoY/QoQ, 8% of revenue) leading the growth.

Growth in North America was driven by contribution from new products launches (Ciprofloxacin & Dexamethasone Otic Suspension, Fulvestrant Injection, OTC Diclofenac and OTC Olapatadine), increase in volumes of the base products and further supported by a favorable currency rate, which was partially offset by price erosion. Europe grew on the back of foraying into a new country (Austria) in addition to new launches and favorable forex movement. India business grew on account of revenues from the acquired business of Wockhardt and contribution from new products including the Avigan (Favipiravir) and Remdesivir launched for treatment of Covid-19.

Muted growth in Emerging Markets of 4.3%/8.2% YoY/QoQ was due to 3% YoY decline in Russia business on account of weakening Ruble, offset by 19% YoY growth in CISR countries (driven by both base business and new product launches) & 7% YoY growth in ROW markets driven by new products.

Lower export incentive impacts GPM; higher employee cost offsets savings in SG&A: Gross Profit Margin (GPM) for the quarter was lower by ~200bps QoQ on account of lower export incentive, adverse forex movement and product mix while on YoY basis GPM was lower as base quarter had higher GPM compared to other quarters. Accordingly, EBITDA margin contracted by 430bps YoY despite savings in SG&A (23.4% of revenue in Q2FY21 vs 24.2% in Q2FY20).

The decline in Net Profit was on account of positive effective tax rate at 11.7% (vs -41.4% in Q2FY20). D&A cost rose 1.1% YoY, while other income & finance cost declined by 5.2%/16.8% YoY, respectively. Net Profit Margin contracted 728bps YoY (+228 bps QoQ).

SHARE HOLDING PATTERN (%)

Particulars	Sep-20 (%)	Jun-20 (%)	Mar-20 (%)
Promoters	26.7	26.7	26.8
FIIIs	29.6	29.3	30.2
DIIIs	13.9	14.7	14.3
Others	29.8	29.3	28.7
Total	100	100	100

11.6%

Revenue CAGR between FY20 and FY22E

27.1%

PAT CAGR between FY20 and FY22E

Dr. Reddy's Laboratories Ltd.

Key Concall Highlights: (i) Dr. Reddy's filed two new ANDAs during the quarter. Cumulatively company has 94 generic filings which are pending for USFDA approval (92 ANDAs and 2 NDAs). Of the 92 ANDAs, 50 are Para IV and 26 are estimated to have "First to File" status (ii) R&D Spend to increase in H2FY21 due to Sputnik trials (iii) Company revised its guidance on new product launches to 30+ products in FY21 (from 25+ earlier) (iv) Growth momentum to continue in Europe due to low base. Company added Austrian market during the quarter. It also launched 3 products in Germany, 1 each in UK, Spain and Austria (v) Company continues to focus on improving productivity. It is also planning to increase digital marketing practices to save cost & improve EBITDA margin (vi) Wockhardt business was integrated from June-20 & company expects synergies soon at topline & bottom line level.

Valuation and view

Second quarter of FY21 was a strong quarter for DRL on the back of superior performance in the US & domestic markets. This superior performance is expected to continue in FY21 aided by COVID-19 drugs (Remdesivir & Favipiravir). Moreover, key products like gNuvaring, gCopaxone & gVascepa provide earnings visibility in the US market, and these products to contribute substantially in FY22 if approval goes through. **Since our last update on the stock in Sep-20 (CMP: INR 5,108/share), the stock has corrected 3.3% & currently trading at FY21/FY22 P/E of 27.2/25.1x. We continue to apply a P/E multiple of 27.5x on FY22E EPS of INR 197/share and maintain our target price of INR 5,418/ share, an upside potential of 10% over CMP. Accordingly, we reiterate an "ACCUMULATE" rating on the shares of Dr. Reddy's Laboratories.**

Segments Result (INR Mn)	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21
Total Sales	48,009	43,838	44,319	44,175	48,967
Global Generics	32,816	35,927	36,399	35,075	39,841
North America	14,265	15,999	18,072	17,282	18,328
Europe	2,764	3,093	3,446	3,551	3,754
India	7,511	7,636	6,839	6,260	9,123
Emerging Markets	8,276	9,199	8,042	7,982	8,636
PSAI	7,107	6,906	7,195	8,553	8,505
PP & Others	8,086	1,005	725	547	621

Segments Result (% YoY)	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21
Total Sales	26.4%	13.9%	10.3%	14.9%	2.0%
Global Generics	7.5%	14.6%	19.8%	6.3%	21.4%
North America	0.0%	7.9%	20.8%	5.9%	28.5%
Europe	44.3%	52.4%	80.2%	47.7%	35.8%
India	9.4%	13.3%	5.1%	-10.1%	21.5%
Emerging Markets	10.5%	18.8%	14.7%	9.4%	4.3%
PSAI	17.9%	16.3%	6.4%	88.4%	19.7%
PP & Others	472.3%	-17.4%	-76.0%	-40.2%	-92.3%

Revenue Mix (%)	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21
Total Sales	100.0%	100.0%	100.0%	100.0%	100.0%
Global Generics	68.4%	82.0%	82.1%	79.4%	81.4%
North America	29.7%	36.5%	40.8%	39.1%	37.4%
Europe	5.8%	7.1%	7.8%	8.0%	7.7%
India	15.6%	17.4%	15.4%	14.2%	18.6%
Emerging Markets	17.2%	21.0%	18.1%	18.1%	17.6%
PSAI	14.8%	15.8%	16.2%	19.4%	17.4%
PP & Others	16.8%	2.3%	1.6%	1.2%	1.3%

Source: Company, KRChoksey Research

Dr. Reddy's Laboratories Ltd.

KEY FINANCIALS

Exhibit 1: Profit & Loss Statement

INR Millions	FY 18	FY 19	FY 20	FY 21E	FY 22E
Revenues	1,42,810	1,54,482	1,75,170	1,92,737	2,18,227
COGS	40,395	44,948	55,544	64,760	72,015
Gross profit	1,02,415	1,09,534	1,19,626	1,27,977	1,46,212
Employee cost	32,149	33,562	33,802	36,620	43,645
Other expenses	46,754	44,074	44,353	42,402	50,192
EBITDA	23,512	31,898	41,471	48,955	52,375
EBITDA Margin	16.46%	20.65%	23.67%	25.40%	24.00%
Depreciation & amortization	10,772	11,348	11,631	11,885	12,336
EBIT	12,740	20,550	29,840	37,070	40,039
Interest expense	788	889	983	1,016	1,054
Other income	1,552	3,375	6,206	1,927	2,182
PBT	13,504	22,920	18,296	37,201	41,167
Tax	4,380	3,858	-1,403	8,184	9,057
Share of Profit/(Loss) of Associates	344	438	561	608	635
PAT	9,468	19,500	20,260	29,625	32,745
EPS (INR)	57.1	117.5	121.9	178.2	197.0
Adj. PAT	9,468	19,500	38,313	30,234	32,745
Adj EPS (INR)	57.0	117.5	230.5	181.9	197.0

Source: Company, KRChoksey Research

Exhibit 2: Cash Flow Statement

INR Millions	FY18	FY19	FY20	FY21E	FY22E
Net Cash Generated From Operations	18,030	28,704	29,841	22,269	22,924
Net Cash Flow from/(used in) Investing Activities	(14,883)	(7,727)	(4,923)	(11,574)	(13,722)
Net Cash Flow from Financing Activities	(4,440)	(21,326)	(25,159)	(9,192)	(10,050)
Net Inc/Dec in cash equivalents	(1,293)	(349)	(241)	1,503	(848)
Opening Balance	3,778	2,542	2,228	1,962	3,465
Closing Balance Cash and Cash Equivalents	2,638	2,228	2,053	3,556	2,708

Source: Company, KRChoksey Research

Exhibit 3: Key Ratios

Key Ratio	FY18	FY19	FY20	FY21E	FY22E
EBITDA Margin (%)	16.5%	20.6%	23.7%	25.4%	24.0%
Tax rate (%)	32.4%	16.8%	-7.7%	22.0%	22.0%
Net Profit Margin (%)	6.6%	12.6%	11.6%	15.4%	15.0%
Adj. Net Profit Margin (%)	6.6%	12.6%	21.9%	15.7%	15.0%
RoE (%)	7.5%	13.9%	24.6%	17.1%	16.4%
RoCE (%)	7.2%	11.8%	17.2%	19.0%	18.3%
Current Ratio (x)	1.52	1.88	1.75	1.94	2.10
EPS (INR)	57.1	117.5	121.9	178.2	197.0
Adj. EPS (INR)	57.0	117.5	230.5	181.9	197.0

Source: Company, KRChoksey Research

Dr. Reddy's Laboratories Ltd.

Exhibit 4: Balance Sheet

INR Millions	FY18	FY19	FY20	FY21E	FY22E
EQUITY AND LIABILITIES					
Equity					
Equity share capital	830	830	831	831	831
Other equity	1,24,886	1,39,406	1,55,157	1,76,010	1,99,059
Shareholders Fund	1,25,716	1,40,236	1,55,988	1,76,841	1,99,890
Total Debt	50,651	34,125	17,836	18,432	19,132
Deferred tax liabilities, net	1,950	473	20	20	20
Other NCL & Provisions	3,750	2,974	2,800	3,081	3,488
Trade payables	13,345	13,671	15,248	21,468	23,873
OCL & Provisions	30,031	33,177	40,361	40,475	45,828
Total equity and liabilities	2,25,443	2,24,656	2,32,253	2,60,317	2,92,232
Assets					
Property, plant and equipment	49,733	49,127	47,779	47,903	48,494
Capital work-in-progress	7,678	4,725	4,364	4,364	4,364
Goodwill	5,331	4,659	4,913	4,913	4,913
Other intangible assets	14,616	18,124	15,811	13,439	11,423
Intangible assets under development	27,027	24,610	10,987	10,987	10,987
Investment in joint ventures	2,104	2,529	2,763	2,763	2,763
Investments	2,549	813	328	328	328
Other non-current assets	11,421	8,968	19,317	21,254	24,065
Total No-current assets	1,20,459	1,13,555	1,06,262	1,05,951	1,07,338
Inventories	29,089	33,579	35,067	60,324	82,867
Investments	18,330	22,529	23,687	23,687	23,687
Trade receivables	40,527	39,869	50,278	47,524	53,809
Other Current Assets	14,400	12,896	14,906	19,274	21,823
Cash and cash equivalents	2,638	2,228	2,053	3,556	2,708
Total Current Assets	1,04,984	1,11,101	1,25,991	1,54,365	1,84,894
Total Assets	2,25,443	2,24,656	2,32,253	2,60,317	2,92,232

Source: Company, KRChoksey Research

Dr. Reddy's Laboratories Ltd.

Dr. Reddy's Laboratories Ltd.				Rating Legend (Expected over a 12-month period)	
Date	CMP (INR)	TP (INR)	Recommendation	Our Rating	Upside
29-10-20	4,942	5,418	Accumulate	Buy	More than 15%
24-09-20	5,108	5,418	Accumulate		
21-05-20	3,839	4,254	Accumulate	Accumulate	5% – 15%
29-01-20	3,189	3,389	Accumulate		
04-11-19	2,757	2,928	Accumulate	Hold	0 – 5%
31-07-19	2,575	2,896	Accumulate		
21-05-19	2,665	2,962	Accumulate	Reduce	-5% – 0
				Sell	Less than – 5%

ANALYST CERTIFICATION:

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