

Dr Reddy's Labs

Estimate change
TP change
Rating change

CMP: INR4,868
TP: INR4,500 (-8%)
Neutral

Earnings growth to moderate after superior show in FY23

Cash build-up to aid M&A opportunities

- Adj. for divestment of brands in the domestic formulation (DF) segment, Dr. Reddy's Labs (DRRD) recorded in-line sales in 4QFY23. However, it posted lower-than-expected EBITDA/PAT due to higher opex. DRRD delivered the highest-ever annual earnings in FY23, led by strong traction in g-Revlimid.
- We reduce our earnings estimates for FY24/FY25 by 7%/7.5%, factoring in 1) higher SGA expenses, 2) prolonged slowdown in the CIS business, and 3) some price erosion in export markets. We continue to value DRRD's base business at 22x 12M forward earnings and add INR170 as NPV of g-Revlimid to arrive at a TP of INR4,500.
- While DRRD delivered 39% YoY earnings growth in FY23, we expect moderation in the earnings CAGR to 3.6% over FY23-25 due to a high base of FY23 and limited visibility of potential products to deliver growth over the next two years. We believe the valuation already factors in the earnings upside, hence we maintain our Neutral rating on the stock.

Product mix benefit offset by higher opex on YoY basis

- Adj. for divestment of brands in the DF segment, 4QFY23 revenue grew 16% YoY to INR60b (est. INR60b).
- US sales rose 27% YoY to INR25.3b (~USD313m; 40% of sales), led by new launches and favourable FX movement. India sales grew 9.6% YoY to INR10b (20% of Sales). EU sales increased 12% YoY to INR5b. (8% of sales). EM sales grew 4% YoY to INR7.8b (12% of sales). Within EM, Russia sales declined 24% YoY. CIS sales remained flat YoY as pricing benefits were offset by lower volumes. PSAI revenue grew 3% YoY to INR7.8b. (12% of sales).
- Gross margin (GM) expanded 440bp YoY to 55.3% due to higher contribution from niche launches.
- EBITDA margin expanded 170bp YoY to 21.9% (est. 24.3%) as superior GM was offset to some extent by higher SG&A (+200bp YoY as % of sales).
- EBITDA grew 25% YoY to INR13b (est. INR14.6b).
- During the quarter, DRRD also recognized an impairment charge of INR540m and government grants of INR305m.
- Adj. for the same, DRRD had PAT of INR8b (est. INR9.5b), up 24% YoY.
- FY23 sales/EBITDA /PAT grew 14%/38%/39% to INR240b/INR62b/INR41b.

Highlights from the management commentary

- DRRD expects YoY growth in NA sales in FY24 on the back of robust launch momentum.
- The intensity of price erosion in the NA market is relatively milder compared to earlier quarters of FY23.
- DRRD completed trials for biosimilar Rituximab and has filed with US/EU/UK regulatory agencies.
- It has received approval for three products in the China market till date.
- DRRD has net surplus cash of INR50b at the end of FY23.

Bloomberg	DRRD IN
Equity Shares (m)	166
M.Cap.(INRb)/(USDb)	810.7 / 9.9
52-Week Range (INR)	4987 / 3788
1, 6, 12 Rel. Per (%)	-2/5/12
12M Avg Val (INR M)	1853

Financials & Valuations (INR b)

Y/E MARCH	FY23	FY24E	FY25E
Sales	240.9	266.1	292.8
EBITDA	62.1	62.8	69.7
Adj. PAT	40.8	39.5	43.7
EBITDA Margin (%)	25.8	23.6	23.8
Cons. Adj. EPS (INR)	244.7	237.0	262.6
EPS Gr. (%)	39.3	-3.2	10.8
BV/Sh. (INR)	1,387	1,598	1,836

Ratios

Net D:E	-0.3	-0.2	-0.4
RoE (%)	19.3	15.9	15.3
RoCE (%)	15.9	14.8	14.5
Payout (%)	9.0	10.6	9.6

Valuations

P/E (x)	19.9	20.5	18.5
EV/EBITDA (x)	12.1	12.0	10.3
Div. Yield (%)	0.4	0.4	0.4
FCF Yield (%)	2.5	0.7	4.5
EV/Sales (x)	3.1	2.8	2.4

Shareholding pattern (%)

As On	Mar-23	Dec-22	Mar-22
Promoter	26.7	26.7	26.7
DII	23.1	23.4	24.8
FII	38.8	38.1	25.4
Others	11.5	11.8	23.1

FII Includes depository receipts

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Investors are advised to refer through important disclosures made at the last page of the Research Report.

 Motilal Oswal research is available on www.motilaloswal.com/Institutional-Equities, Bloomberg, Thomson Reuters, Factset and S&P Capital.

Quarterly Performance - IFRS

(INRm)

Y/E March	FY22				FY23				FY22	FY23	Estimates	
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q			4QE	% Var
Sales	49,194	57,632	53,197	52,204	49,853	63,057	67,700	60,328	212,227	240,936	60,138	0.3
YoY Change (%)	11.4	17.7	9.9	10.4	1.3	9.4	27.3	15.6	11.9	13.5	15.2	
Total Expenditure	40,169	44,275	41,179	41,683	39,516	45,022	47,136	47,139	167,306	178,813	45,517	
EBITDA	9,025	13,357	12,018	10,521	10,337	18,035	20,564	13,189	44,921	62,123	14,622	-9.8
YoY Change (%)	-18.9	9.3	15.9	4.4	14.5	35.0	71.1	25.4	0.5	38.3	39.0	
Margins (%)	18.3	23.2	22.6	20.2	20.7	28.6	30.4	21.9	21.2	25.8	24.3	-245.1
Amortization	2,905	2,985	2,976	2,959	3,050	3,150	3,273	3,190	11,825	12,663	3,527	
EBIT	6,120	10,372	9,042	7,562	7,287	14,885	17,291	9,999	33,096	49,460	11,094	
YoY Change (%)	-23.4	16.0	26.4	9.4	19.1	43.5	91.2	32.2	3.8	49.4	46.7	
Other Income	1,305	2,309	714	1,255	2,829	318	180	1,156	5,583	4,483	288	
PBT before EO expenses	7,425	12,681	9,756	8,817	10,116	15,203	17,471	11,155	38,679	53,943	11,382	-2.0
One-off income/(expense)	0	0	-47	-6,334	4,537	908	-1,125	2,100	-6,381	6,420	0	
Profit before Tax	7,425	12,681	9,709	2,483	14,653	16,111	16,346	13,255	32,298	60,362	11,382	16.5
Tax	1,717	2,761	2,644	1,608	2,779	4,983	3,875	3,663	8,730	15,300	1,906	
Rate (%)	23.1	21.8	27.2	64.8	19.0	30.9	23.7	27.6	27.0	25.3	16.7	
Reported Profit	5,708	9,920	7,065	875	11,874	11,128	12,471	9,592	23,568	45,063	9,476	1.2
Adjusted PAT	5,708	9,920	7,112	6,525	8,197	11,402	13,103	8,072	29,265	40,775	9,476	-14.8
YoY Change (%)	-1.5	34.2	19.6	38.7	43.6	14.9	84.2	23.7	22.8	39.3	45.2	
Margins (%)	11.6	17.2	13.4	12.5	16.4	18.1	19.4	13.4	13.8	16.9	15.8	

E - MOFSL Estimates

Key performance Indicators (Consolidated)

Y/E March	FY22E				FY22E				FY22	FY23
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4Q		
INRm										
North America	17,390	18,909	18,645	19,971	17,815	28,001	30,567	25,321	74,915	101,704
YoY Change (%)	0.6	3.2	7.2	14.2	2.4	48.1	63.9	26.8	6.3	35.8
Europe	3,994	4,135	4,058	4,444	4,141	4,199	4,303	4,960	16,631	17,603
YoY Change (%)	12.5	10.1	-2.1	12.3	3.7	1.5	6.0	11.6	8.0	5.8
India	10,600	11,402	10,266	9,299	11,047	11,500	11,274	10,194	41,567	44,015
YoY Change (%)	69.3	25.0	7.0	10.1	4.2	0.9	9.8	9.6	24.4	5.9
Russia & Others CIS	4,900	7,890	7,100	7,426	5,074	8,100	9,100	7,500	27,426	29,774
YoY Change (%)	4.3	31.5	7.6	25.9	3.5	2.7	28.2	1.0	18.2	8.6
Others	4,229	5,095	4,439	2,813	3,954	4,146	3,997	3,642	16,500	15,729
YoY Change (%)	28.9	93.3	46.8	-4.5	-6.5	-18.6	-10.0	29.5	38.8	-4.7
PSAI	7,540	8,372	7,271	7,557	7,090	6,434	7,758	7,787	30,740	29,069
YoY Change (%)	-11.8	-1.6	3.7	-4.5	-6.0	-23.1	6.7	3.0	-3.9	-5.4
Cost Break-up										
COGS (% of Sales)	47.8	46.6	46.2	49.1	49.0	42.4	40.8	44.7	47.4	43.9
SG&A (% of Sales)	24.7	22.5	23.4	22.5	21.5	21.3	21.7	24.5	23.2	22.3
R&D Expenses(% of Sales)	9.2	7.7	7.8	8.3	8.7	7.7	7.1	8.9	8.2	8.0
Gross Margins(%)	52.2	53.4	53.8	50.9	51.0	57.6	59.2	55.3	52.6	56.1
EBITDA Margins(%)	18.3	23.2	22.6	20.2	20.7	28.6	30.4	21.9	21.2	25.8
EBIT Margins(%)	12.4	18.0	17.0	14.5	14.6	23.6	25.5	16.6	15.6	20.5

E: MOFSL Estimates

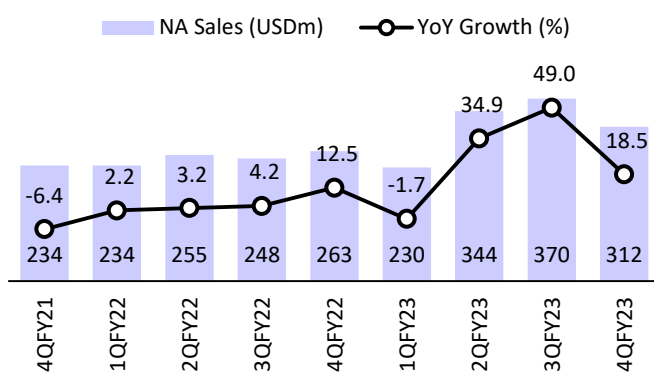


Management call highlights

- Adj. for Covid-related sales and divestment of brands, DRRD delivered 11% YoY growth in the DF segment in FY23.
- The pricing stability for its products and reduction in raw material costs helped the company improve profitability in the PSAI segment in 4QFY23.
- DRRD launched six products in the NA market in 4QFY23.
- Due to a higher base on account of divestment of certain brands and higher channel inventory in 4QFY22, Russia sales declined 24% YoY.
- DRRD filed 7 DMFs in the PSAI segment in 4QFY23.
- GM for global generics/PSAI segment stood at 61.7%/25.2% in 4QFY23.
- SG&A spending increased 15% YoY in 4QFY23 due to higher marketing/sales promotion expenses and adverse impact of forex rates.
- DRRD recorded an impairment charge of INR0.5b on account of 1) a decrease in market potential of products acquired from Nimbus health, and 2) adverse market conditions reducing the potential of certain products under development.

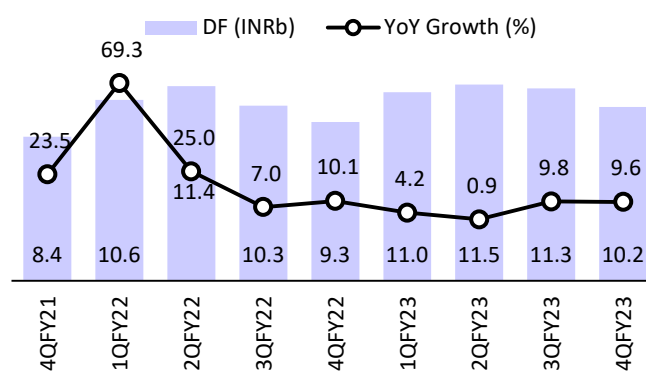
Key exhibits

Exhibit 1: In CC terms, NA sales grew 19% YoY in 4QFY23



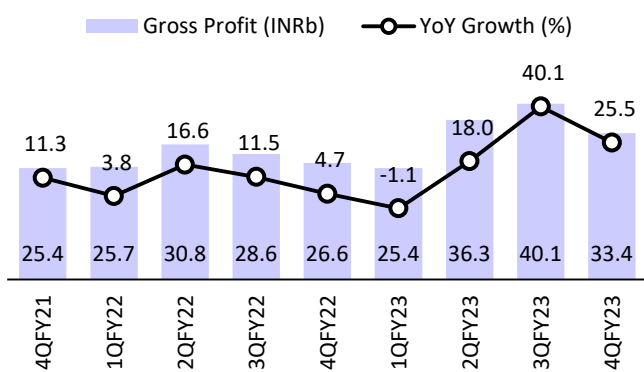
Source: MOFSL, Company

Exhibit 2: DF sales grew 10% YoY in 4QFY23



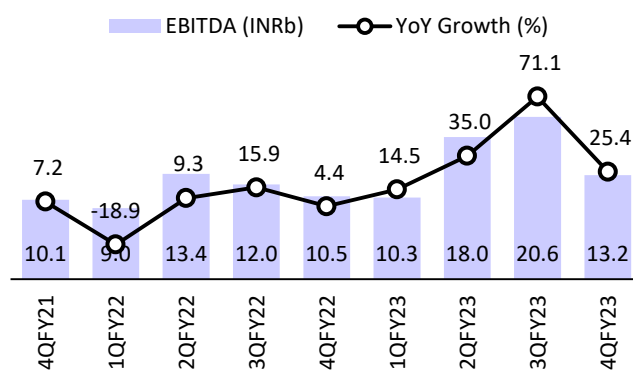
Source: MOFSL, Company

Exhibit 3: Gross profit increased 26% YoY in 4QFY23

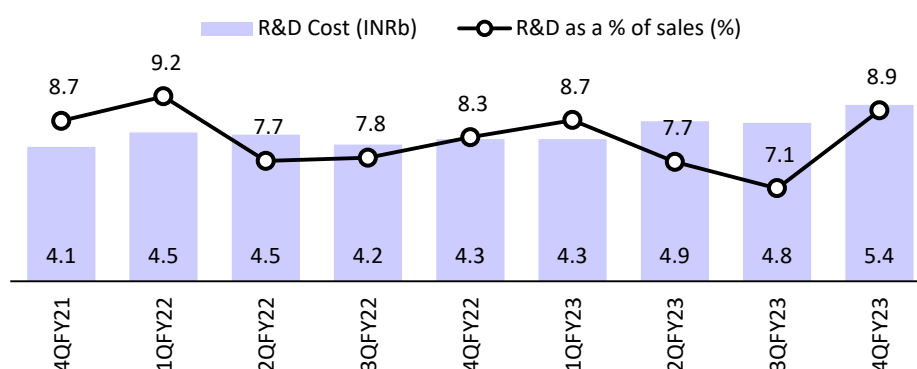


Source: Company, MOFSL

Exhibit 4: EBITDA grew 25% YoY in 4QFY23



Source: Company, MOFSL

Exhibit 5: R&D expense as a percentage of sales was 9% in 4QFY23

Source: MOFSL, Company

Efforts underway to sustain earnings momentum

US: Launch pace to support growth going forward

- In FY23, DRRD's sales witnessed robust YoY growth of 25% YoY to USD1.3b, led by new launches such as g-Revlimid, favourable movement of forex rates and scale-up of existing products.
- During FY23, DRRD launched 25 new products in the US such as Difluprednate, Lurasidone Tablets, Lubiprostone Capsules, Sunitinib Capsules.
- In FY24, DRRD is expected to sustain the launch momentum.
- DRRD has a robust pipeline of 81 ANDAs and 5 NDAs pending approval, which would support its long-term aspirations in the US.
- While the new launch momentum will continue in the US, we expect some tapering in g-Revlimid sales on account of a loss of exclusivity of certain strengths and increased competition going forward.
- We expect the US segment to witness an 11% sales CAGR over FY23-25 to ~INR125b (USD1.5b).

DF: efforts on multiple factors to drive growth

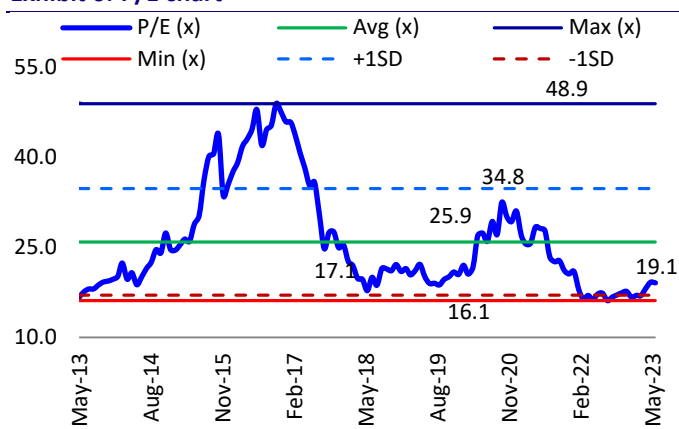
- During FY23, India sales grew 6% YoY to INR44b. However, adjusting for Covid-led sales in FY22, DRRD delivered healthy growth of 11% YoY in the DF segment.
- In FY23, DRRD witnessed robust growth in therapy areas of cardiac, derma, Gastro and Pain, led by price increases and new product launches, partly offset by reduction in volumes for certain products. DRRD continues to focus on select therapies and divest non-core brands to be among the top five companies in India.
- It also intends to build Nutraceuticals/OTC portfolio, enhance digital efforts, and build ecosystem for marketing/promotional activities.
- We expect a sales CAGR of 10% over FY23-25 to reach INR53b.

PSAI segment: Outlook on revival mode

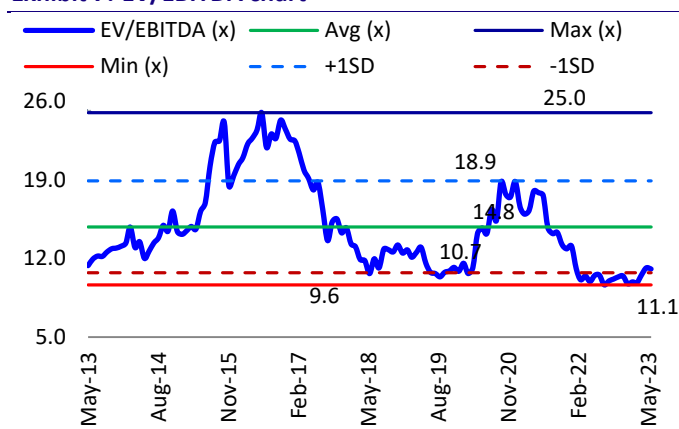
- During FY23, the PSAI segment's revenue declined 5% YoY to INR29b, due to a decline in base business volumes and price erosion, slightly offset by new launches and favourable forex movement.
- However, the outlook for PSAI is getting better on account of a volume uptick as well as reduction in raw material costs.
- We expect the PSAI business to post a 3% sales CAGR to INR35b over FY23-25.

Reiterate Neutral

- We reduce our earnings estimates for FY24/FY25 by 7%/7.5%, factoring in 1) higher SGA expenses, 2) prolonged slowdown in the CIS business, and 3) some price erosion across export markets. We continue to value DRRD's base business at 22x 12M forward earnings and add INR170 as NPV of g-Revlimid to arrive at a TP of INR4,500.
- While DRRD delivered 39% YoY earnings growth in FY23, we expect moderation in the earnings CAGR to 3.6% over FY23-25, due to a high base of FY23 and limited visibility of potential products to deliver growth over the next two years. We believe the valuation already factors in the earnings upside, hence we maintain our Neutral rating on the stock.

Exhibit 6: P/E chart

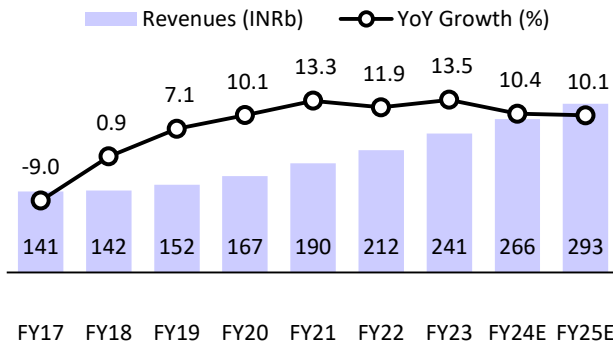
Source: MOFSL, Company, Bloomberg

Exhibit 7: EV/EBITDA chart

Source: MOFSL, Company, Bloomberg

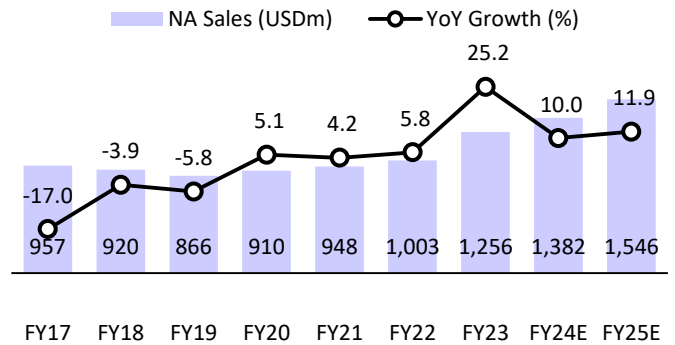
Story in charts

Exhibit 8: Expect sales CAGR of ~10% over FY23–25



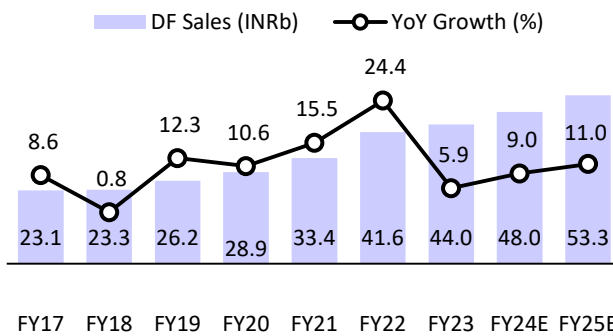
Source: Company, MOFSL

Exhibit 9: NA sales to see ~11% CAGR over FY23–25



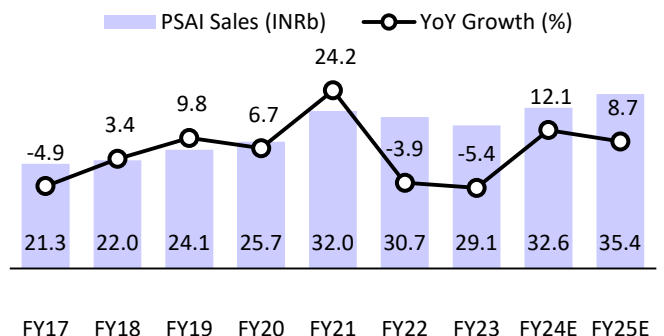
Source: Company, MOFSL

Exhibit 10: DF sales to exhibit 10% CAGR over FY23–25



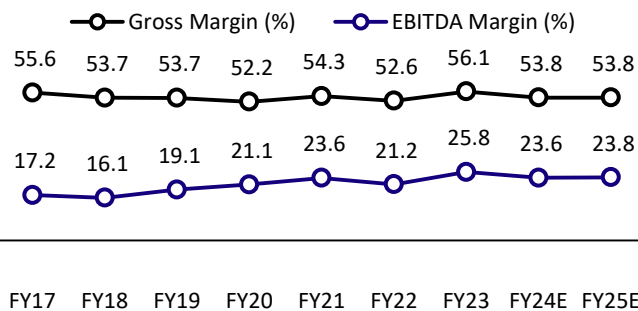
Source: Company, MOFSL

Exhibit 11: PSAI to see 10% sales CAGR over FY23–25



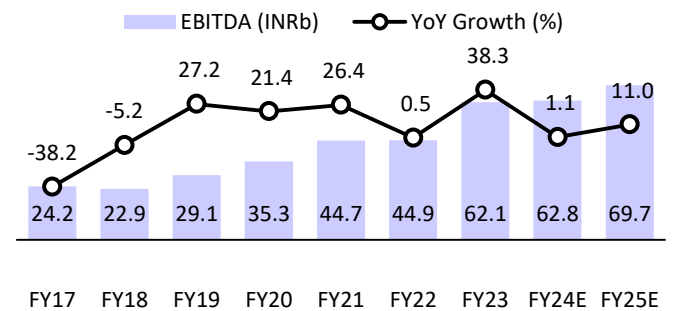
Source: Company, MOFSL

Exhibit 12: EBITDA margin to contract 200bp over FY23–25



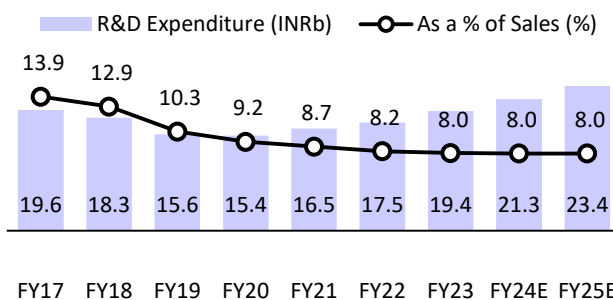
Source: Company, MOFSL

Exhibit 13: Expect EBITDA CAGR of ~6% over FY23–25



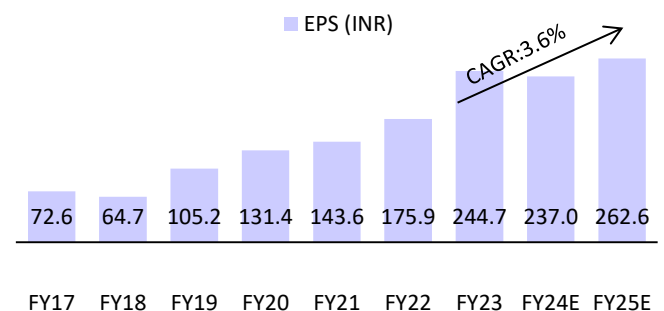
Source: Company, MOFSL

Exhibit 14: R&D expense to settle at ~8% of sales by FY25



Source: Company, MOFSL

Exhibit 15: Expect EPS CAGR of 3.6% over FY23–25



Source: Company, MOFSL

Financials and valuations

Income Statement									(INR m)
Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
Net Sales	140,809	142,028	152,051	167,400	189,722	212,227	240,936	266,053	292,805
Change (%)	-9.0	0.9	7.1	10.1	13.3	11.9	13.5	10.4	10.1
Total Expenditure	116,654	119,137	122,938	132,058	145,038	167,306	178,813	203,265	223,117
EBITDA	24,155	22,891	29,113	35,342	44,684	44,921	62,123	62,789	69,688
Change (%)	-38.2	-5.2	27.2	21.4	26.4	0.5	38.3	1.1	11.0
Margin (%)	17.2	16.1	19.1	21.1	23.6	21.2	25.8	23.6	23.8
Depreciation & Amort.	11,722	11,762	11,980	12,472	12,798	11,825	12,663	13,835	15,226
Net Interest Exp	0	817	1,163	983	-1,653	-2,119	-2,853	-1,095	-1,043
One-off (Gains)/Losses	0	0	-1,800	7,718	7,700	6,381	-5,445	0	0
PBT before EO Expense	14,653	14,341	22,443	25,749	35,001	38,679	53,943	51,950	57,406
Change (%)	-46.0	-2.1	56.5	14.7	35.9	10.5	39.5	-3.7	10.5
PBT after EO Expense	14,653	14,341	22,443	18,033	27,298	32,298	59,388	51,950	57,406
Tax	2,614	4,535	3,648	-1,466	9,175	8,730	15,300	12,468	13,663
Tax Rate (%)	17.8	31.6	16.3	-8.1	33.6	27.0	25.8	24.0	23.8
Reported PAT	12,039	9,806	18,795	19,499	18,123	23,568	44,088	39,482	43,743
Adjusted Net Profit	12,039	10,736	17,459	21,807	23,834	29,265	40,775	39,482	43,743
Change (%)	-46.7	-10.8	62.6	24.9	9.3	22.8	39.3	-3.2	10.8
Margin (%)	8.5	7.6	11.5	13.0	12.6	13.8	16.9	14.8	14.9

E: MOSFL Estimates

Balance Sheet									(INR m)
Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
Equity Share Capital	829	830	830	830	830	832	833	833	833
Reserves	121,792	124,886	139,406	155,158	175,587	189,695	230,158	265,461	305,026
Net Worth	122,621	125,716	140,236	155,988	176,417	190,527	230,991	266,294	305,859
Loans	49,075	50,651	34,125	17,836	29,444	33,845	13,472	12,472	11,472
Deferred Liabilities/Tax	-5,164	-3,455	-3,844	-12,179	-10,397	-12,721	-6,363	-6,363	-6,363
Capital Employed	166,532	172,912	170,517	161,645	195,464	211,651	238,100	272,403	310,968
Gross Block	92,605	99,286	115,385	126,148	143,664	160,797	177,753	190,841	199,703
Less: Accum. Deprn.	42,324	49,553	61,533	74,005	86,803	98,628	111,291	125,126	140,352
Net Fixed Assets	56,376	57,411	53,852	52,143	56,861	62,169	66,462	65,715	59,351
Investments	26,317	28,935	30,769	33,264	33,115	38,393	62,180	62,180	62,180
Goodwill/Intangibles	46,176	46,974	47,393	31,711	40,847	31,664	35,094	35,094	35,094
Curr. Assets	82,512	86,718	88,325	102,936	124,659	151,647	150,922	159,710	209,594
Inventory	28,528	29,089	33,579	35,067	45,412	50,884	48,670	54,083	60,874
Account Receivables	38,196	40,696	39,982	52,015	49,759	66,818	72,485	73,505	80,896
Cash and Bank Balance	3,865	2,638	2,228	2,053	14,829	14,852	5,779	8,177	41,471
Others	11,923	14,295	12,536	13,801	14,659	19,093	23,988	23,945	26,352
Curr. Liability & Prov.	44,849	47,126	49,822	58,409	60,018	72,222	76,558	50,295	55,251
Account Payables	10,569	13,345	13,671	15,248	18,109	25,572	26,444	19,790	21,779
Other Current Liabilities	34,280	33,781	36,151	43,161	41,909	46,650	50,114	30,506	33,471
Net Current Assets	37,663	39,592	38,503	44,527	64,641	79,425	74,364	109,415	154,343
Appl. of Funds	166,532	172,912	170,517	161,645	195,464	211,651	238,100	272,403	310,968

Financials and valuations

Ratios

Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
EPS	72.6	64.7	105.2	131.4	143.6	175.9	244.7	237.0	262.6
Cash EPS	143.3	135.5	177.3	206.5	220.7	246.9	320.8	320.0	354.0
BV/Share	739.6	757.3	844.8	939.7	1,062.8	1,145.0	1,386.5	1,598.4	1,835.9
DPS	20.0	20.0	20.0	23.6	25.0	20.4	20.4	21.4	21.4
Payout (%)	33.1	40.7	21.3	23.5	26.8	16.9	9.0	10.6	9.6
Valuation (x)									
P/E	67.1	75.3	46.3	37.1	33.9	27.7	19.9	20.5	18.5
PEG (x)	NA	-7	1	1	4	1.2	0.5	-6.5	1.7
P/BV	6.6	6.4	5.8	5.2	4.6	4.3	3.5	3.0	2.7
EV/Sales	5.9	5.8	5.3	4.7	4.2	3.7	3.1	2.8	2.4
EV/EBITDA	34.2	36.1	27.8	22.4	17.7	17.6	12.1	12.0	10.3
Dividend Yield (%)	0.4	0.4	0.4	0.5	0.5	0.4	0.4	0.4	0.4
Return Ratios (%)									
ROIC	8.9	5.8	10.8	21.9	17.0	18.0	23.1	21.0	21.5
RoE	9.7	8.6	13.1	14.7	14.3	16.0	19.3	15.9	15.3
RoCE	6.4	4.8	8.9	17.4	11.8	12.3	15.9	14.8	14.5
Working Capital Ratios									
Fixed Asset Turnover (x)	1.6	1.5	1.4	1.4	1.4	1.4	1.4	1.4	1.5
Debtor (Days)	103	101	97	100	98	100	106	100	96
Inventory (Days)	70	74	75	75	77	83	75	70	72
Leverage Ratio									
Net Debt/Equity (x)	0.1	0.1	0.0	-0.1	-0.2	-0.2	-0.3	-0.2	-0.4

Cash Flow Statement

Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
Op. Profit/(Loss) before Tax	14,653	14,341	22,443	25,749	35,001	38,679	53,943	51,950	57,406
Depreciation	11,722	11,762	11,980	12,472	12,798	11,825	12,663	13,835	15,226
Interest/Dividends Recd.	-2,220	-4,029	-6,473	4,839	6,238	2,917	-7,075	-1,901	-1,901
Direct Taxes Paid	-2,614	-4,535	-3,648	1,466	-9,175	-8,730	-15,300	-12,468	-13,663
(Inc)/Dec in WC	-192	-3,156	679	-6,199	-7,338	-14,761	-4,012	-32,653	-11,634
CF from Operations	21,349	14,383	24,981	38,327	37,524	29,930	40,219	18,763	45,434
EO Expense	0	0	0	0	-6,105	-4,559	0	0	0
CF from Operations	21,444	18,030	28,704	38,542	43,629	34,489	40,219	18,763	45,434
(inc)/dec in FA	-40,922	-13,595	-8,840	4,919	-26,652	-7,950	-20,386	-13,088	-8,863
Free Cash Flow	-19,573	788	16,141	43,246	10,872	21,980	19,833	5,675	36,572
(Pur)/Sale of Investments	17,757	1,411	2,839	-2,495	149	-5,278	-23,787	0	0
CF from Investments	-18,404	-14,883	-7,727	-4,923	-26,503	-26,387	-44,173	-13,088	-8,863
Change in net worth	-11,130	-2,719	-273	835	1,653	-5,479	355	0	0
(Inc)/Dec in Debt	15,672	1,576	-16,526	-16,289	11,608	4,401	-20,373	-1,000	-1,000
Dividend Paid	-3,986	-3,992	-4,002	-4,582	-4,852	-3,979	-3,877	-4,076	-4,076
CF from Fin. Activity	-3,692	-4,440	-21,326	-25,159	-4,545	3,959	-22,797	-3,278	-3,277
Inc/Dec of Cash	-652	-1,293	-349	8,460	12,581	12,061	-26,751	2,398	33,295
Add: Beginning Balance	4,921	3,865	2,638	2,228	2,053	14,829	14,852	5,779	8,177
Closing Balance	4,269	2,572	2,289	10,688	14,634	26,890	-11,899	8,177	41,471
FX impact net of bank balances	-404	66	-61	-8,635		-12,038	17,678	0	0
Closing Balance	3,865	2,638	2,228	2,053	14,829	14,852	5,779	8,177	41,471

E: MOFSL Estimates

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