

Dr Reddy's Labs

Estimate change



TP change



Rating change


CMP: INR5,397
TP: INR5,400
Neutral

Niche products lead to superior margins

Emerging markets and PSAI drag performance to some extent

- Dr. Reddy's Lab (DRRD) delivered better-than-expected 2QFY24, driven by higher North America (NA)/Europe sales and improved profitability. This was, however, offset to some extent by the subdued performance in emerging markets and Pharmaceutical services (PSAI) segments.
- We raise our earnings estimates by 6%/4% for FY24/FY25, factoring in: a) better traction in existing products and sustained launch momentum in the NA market, and b) superior growth in the European market. We value DRRD at 22x 12M forward earnings and add NPV of INR110 related to g-Revlimid to arrive at our TP of INR5,400.
- After a strong 31% earnings CAGR over FY21-23, we expect earnings growth momentum to moderate to 12% CAGR over FY23-25 due to the high base on account of g-Revlimid and gradual recovery in EM/PSAI sales. Further, the current valuation adequately factors in the earnings upside. **Reiterate Neutral.**

Superior product mix benefit offset by higher SG&A spending YoY

- DRRD's 2QFY24 revenue grew 9% YoY to INR69b (our est: INR67b). Sequentially, its sales stood stable for the quarter.
- The US sales rose 13% YoY to INR32b (~USD382m; 46% of sales), led by better traction in the existing portfolio, Mayne integration, and favorable FX movement. The EU sales jumped 26% YoY to INR5.3b (8% of sales). India sales grew 3% YoY to INR12b (17% of sales). The PSAI segment's revenue was up 9% YoY to INR7b (10% of sales). The EM sales stood flat YoY to INR12b (17% of sales). The business was hurt by currency devaluation (Russia), reduced volume off-take in CIS, and pricing pressure on the base portfolio in ROW.
- Gross margin (GM) expanded 110bp YoY to 58.7% due to a better product mix. The global generic/PSAI segments reported GM of 63.6%/17.8% in 2Q.
- EBITDA margin expanded at a lower rate of 40bp YoY to 29.0% (our est: 27.2%) due to higher SG&A/R&D spending (50bp/20bp YoY as a % of sales).
- Assuming USD110m sales from g-Revlimid and adjusting for the same, DRRD would have sales/EBITDA of INR60b/INR11b with an EBITDA margin of 19% for the quarter.
- EBITDA grew 11% YoY to INR20b (v/s est. of INR18b).
- Adj. for a one-time litigation settlement income (INR980m), DRRD reported a PAT of INR13.3b (our est: INR11.7b), up 17% YoY in 2QFY24.
- For 1HFY24, Revenue/EBITDA/PAT grew 21%/43%/37% YoY to INR136b/INR40b/INR27b.

Highlights from the management commentary

- Management guided for 25-30 launches in FY24 and about 65-70 launches over the next three years.
- DRRD will launch b-Rituximab through a partner in FY25. The biosimilar portfolio launch (without a partner) would commence from FY27 onwards.
- Adjusting for the impact of NLEM and discontinued products, India segment grew in mid-single-digit YoY for the quarter.

Bloomberg	DRRD IN
Equity Shares (m)	167
M.Cap.(INRb)/(USDb)	900.1 / 10.8
52-Week Range (INR)	5990 / 4175
1, 6, 12 Rel. Per (%)	2/3/13
12M Avg Val (INR M)	2143

Financials & Valuations (INR b)

Y/E MARCH	FY23	FY24E	FY25E
Sales	240.9	272.3	298.9
EBITDA	62.1	76.2	80.1
Adj. PAT	40.8	49.4	51.4
EBITDA Margin (%)	25.8	28.0	26.8
Cons. Adj. EPS (INR)	244.7	296.7	308.8
EPS Gr. (%)	39.2	21.2	4.1
BV/Sh. (INR)	1,387	1,658	1,942

Ratios

Net D:E	-0.3	-0.2	-0.5
RoE (%)	19.3	19.5	17.2
RoCE (%)	15.9	18.4	16.3
Payout (%)	9.0	8.5	8.1

Valuations

P/E (x)	22.1	18.2	17.5
EV/EBITDA (x)	13.5	11.0	9.8
Div. Yield (%)	0.4	0.4	0.4
FCF Yield (%)	2.2	0.3	6.1
EV/Sales (x)	3.5	3.1	2.6

Shareholding pattern (%)

As On	Sep-23	Jun-23	Sep-22
Promoter	26.7	26.7	26.7
DII	21.0	22.0	24.7
FII	42.4	39.8	36.6
Others	9.9	11.6	12.0

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

(INR b)

Y/E March	FY23				FY24E				FY23	FY24E	Estimates	
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE			2QE	% Var
Sales	49.9	63.1	67.7	60.3	67.4	68.8	68.7	67.4	240.9	272.3	66.7	3.1
YoY Change (%)	1.3	9.4	27.3	15.6	35.2	9.1	1.5	11.7	13.5	13.0	5.8	
Total Expenditure	39.5	45.0	47.1	47.1	46.9	48.8	49.6	50.7	178.8	196.1	48.6	
EBITDA	10.3	18.0	20.6	13.2	20.5	20.0	19.1	16.7	62.1	76.2	18.1	10.1
YoY Change (%)	14.5	35.0	71.1	25.4	97.8	10.7	-7.1	26.8	38.3	22.7	0.6	
Margins (%)	20.7	28.6	30.4	21.9	30.3	29.0	27.8	24.8	25.8	28.0	27.2	
Amortization	3.1	3.2	3.3	3.2	3.6	3.8	3.9	3.7	12.7	15.0	3.7	
EBIT	7.3	14.9	17.3	10.0	16.9	16.1	15.3	13.0	49.5	61.3	14.5	
YoY Change (%)	19.1	43.5	91.2	32.2	131.5	8.3	-11.8	30.3	49.4	23.9	-2.6	
Margins (%)	14.6	23.6	25.5	16.6	25.0	23.4	22.2	19.3	20.5	22.5	21.7	
Other Income	2.8	0.3	0.2	1.2	1.1	1.6	1.0	0.9	4.5	4.6	0.9	
PBT before EO expenses	10.1	15.2	17.5	11.2	18.0	17.7	16.2	14.0	53.9	65.9	15.4	15.0
One-off income/(expense)	4.5	0.9	-1.1	2.1	0.5	1.4	0.0	0.0	6.4	1.9	0.0	
Profit before Tax	14.7	16.1	16.3	13.3	18.5	19.1	16.2	14.0	60.4	67.8	15.4	24.3
PBT after EO Expenses	14.6	16.1	16.3	13.3	18.5	19.1	16.2	14.0	60.4	67.8	15.4	
Tax	2.8	5.0	3.9	3.7	4.4	4.3	4.1	3.6	15.3	16.5	3.7	
Rate (%)	19.0	30.9	23.7	27.6	24.0	22.7	25.3	25.7	25.3	24.3	24.2	
Reported Profit	11.9	11.1	12.5	9.6	14.0	14.8	12.1	10.4	45.1	51.3	11.7	26.8
Adjusted PAT	8.2	11.4	13.1	8.1	13.7	13.3	12.1	10.4	40.8	49.4	11.7	13.8
YoY Change (%)	43.6	14.9	84.2	23.7	66.6	16.5	-7.6	28.6	39.3	21.2	2.3	
Margins (%)	16.4	18.1	19.4	13.4	20.3	19.3	17.6	15.4	16.9	18.1	17.5	

E: MOFSL Estimates

Key performance Indicators (Consolidated)

Y/E March	FY23				FY24E				FY23	FY24E	FY24E
	1Q	2Q	3Q	4Q	1Q	2Q	3QE	4QE			
INRm											
North America	17.8	28.0	30.6	25.3	32.0	31.7	31.5	30.9	101.7	126.1	29.6
YoY Change (%)	2.4	48.1	63.9	26.8	79.5	13.2	12.0	22.2	35.8	24.0	5.7
Europe	4.1	4.2	4.3	5.0	5.1	5.3	4.9	4.3	17.6	19.6	4.8
YoY Change (%)	3.7	1.5	6.0	11.6	22.5	25.9	15.0	-12.9	5.8	11.5	15.0
India	11.0	11.5	11.3	10.2	11.5	11.9	12.0	10.9	44.0	46.2	12.5
YoY Change (%)	4.2	0.9	9.8	9.6	3.9	3.1	6.0	7.2	5.9	5.0	8.5
Russia & Others CIS	5.1	8.1	9.1	7.5	7.6	8.0	8.2	8.4	29.8	32.1	7.8
YoY Change (%)	3.5	2.7	28.2	1.0	49.8	-1.2	-10.3	11.7	8.6	7.9	-3.1
Others	4.0	4.1	4.0	3.6	4.0	4.2	4.4	4.8	15.7	17.3	4.2
YoY Change (%)	-6.5	-18.6	-10.0	29.5	-0.1	2.2	9.0	30.4	-4.7	10.0	2.0
PSAI	7.1	6.4	7.8	7.8	6.7	7.0	7.1	7.4	29.1	28.3	7.1
YoY Change (%)	-6.0	-23.1	6.7	3.0	-5.4	9.3	-8.0	-5.3	-5.4	-2.8	10.0
Cost Break-up											
COGS (% of Sales)	49.0	42.4	40.8	44.7	41.3	41.3	42.0	43.4	43.9	42.0	43.0
SG&A (% of Sales)	21.5	21.3	21.7	24.5	21.0	21.7	22.0	23.3	22.3	22.0	22.4
R&D Expenses(% of Sales)	8.7	7.7	7.1	8.9	7.4	7.9	8.2	8.5	8.0	8.0	7.4
Gross Margin (%)	51.0	57.6	59.2	55.3	58.7	58.7	58.0	56.6	56.1	58.0	57.0
EBITDA Margin (%)	20.7	28.6	30.4	21.9	30.3	29.0	27.8	24.8	25.8	28.0	27.2
EBIT Margin (%)	14.6	23.6	25.5	16.6	25.0	23.4	22.2	19.3	20.5	22.5	21.7

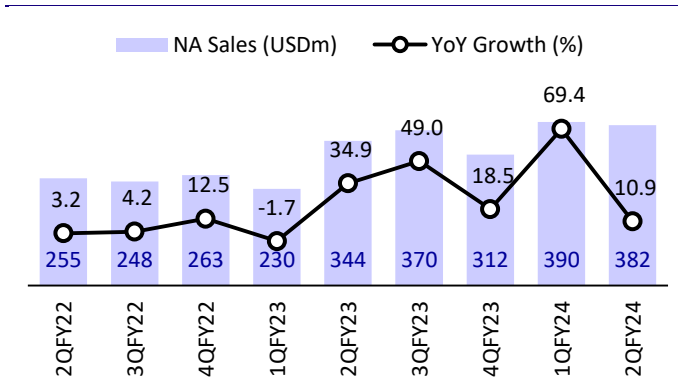


Management call highlights

- Management expects the India segment to reach double-digit growth in 4QFY24.
- DRRD has a sales force of 6K people to cater to the domestic formulation market.
- It expects the contribution from PLI scheme to be sustainable going forward.
- DRRD recently forayed into e-commerce for Nutraceutical, and OTC products.
- In China, the company expects to launch 15-18 new products. DRRD anticipates China to contribute meaningfully from FY25 onwards.
- DRRD is working on addressing the observations issued by the USFDA on its biologics facility.
- Its R&D expense stood at INR5.5b (7.9% of sales).
- DRRD expects ETR to be 24-25% for FY24.

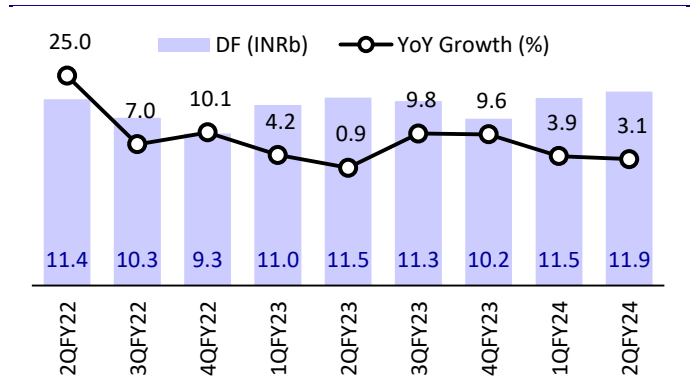
Key exhibits

Exhibit 1: In CC terms, NA sales grew 11% YoY in 2QFY24



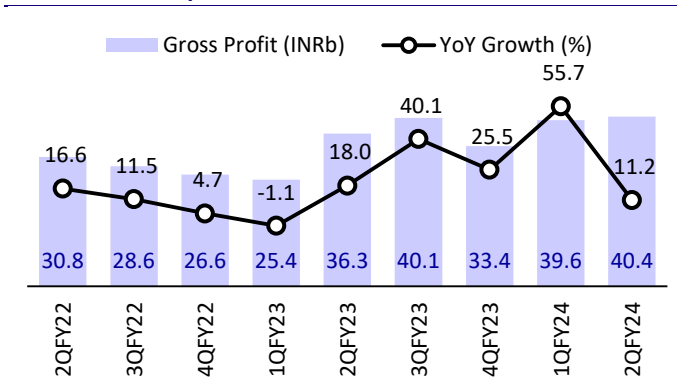
Source: MOFSL, Company

Exhibit 2: DF sales grew 3% YoY in 2QFY24



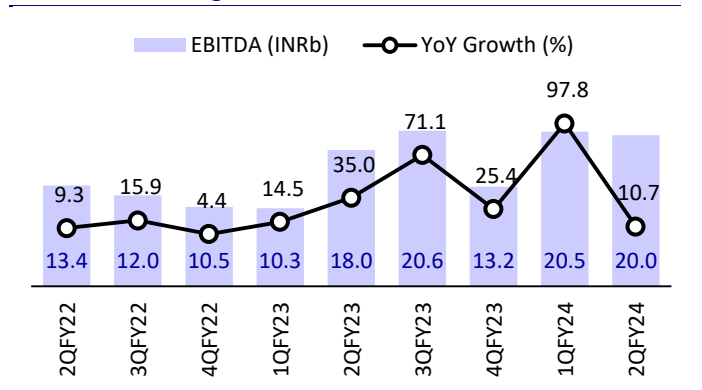
Source: MOFSL, Company

Exhibit 3: Gross profit increased 11% YoY

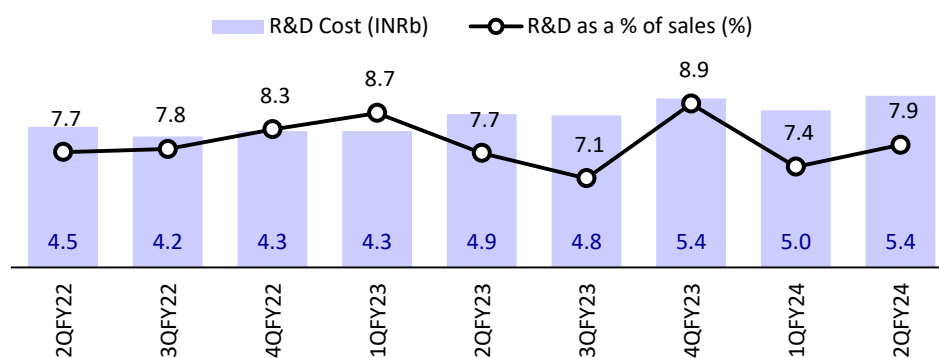


Source: Company, MOFSL

Exhibit 4: EBITDA grew 11% YoY in 2QFY24



Source: Company, MOFSL

Exhibit 5: R&D spending stable QoQ at ~INR5b

Source: MOFSL, Company

NA remains the key growth driver; the work-in-progress of other segments to drive future growth

Superior show sustained in the NA segment

- In 1HFY24, DRRD's NA sales posted a robust 34% YoY growth to USD771m. This was driven by higher volume off-take of differentiated products, addition of sales from Mayne portfolio, and reduced intensity of price erosion.
- DRRD launched 10 new products in the US in 1HFY24 and remains on track to launch 25-30 more products on a full-year basis.
- Going forward, DRRD has a robust pipeline of 75 ANDAs and 4 NDAs under the 505(b)(2) route awaiting approval, which is likely to bolster its US business significantly. Moreover, of these ANDAs, 41 are Para IVs, and 20 have the potential to secure 'First to File' status.
- We expect the US segment to report 17% sales CAGR over FY23-25 to ~INR139b (USD1.7b).

DF growth to pick-up in the coming quarters

- In 1HFY24, India sales grew 4% YoY to INR23.3b. After excluding the brand divestment income, sales of the divested portfolio, and NLEM-related adverse price impact, the DF business growth was modest for 1HFY24.
- In 2QFY24, as per IQVIA, Cardiac therapy declined 15% YoY. This affected overall growth in this segment adversely. This was offset by a healthy growth in therapy areas of gastro, derma, pain, et al.
- Moreover, price hikes/new product launches have remained key growth drivers.
- We expect a sales CAGR of 8% over FY23-25 to reach INR51b.

Multiple headwinds in the EM over near term; growth to revive gradually

- In 1HFY24, the EM sales grew 12% YoY to INR23.8b.
- While YoY growth was strong in EM in 1Q, DRRD posted a sharp deceleration in growth for 2QFY24, dragging the overall YoY sales growth for 1HFY24.
- The adverse currency impact in Russia and reduced base business in other emerging markets hurt 1HFY24 performance.
- We expect a sales CAGR of 8% over FY23-25 to reach INR35b.

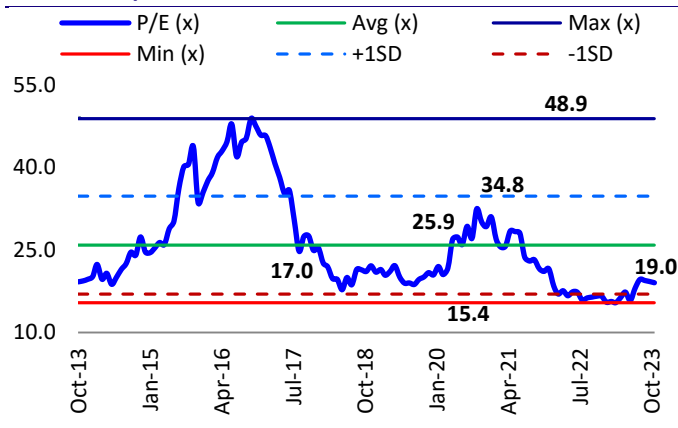
PSAI segment growth to be led by volume and new launches

- In 1HFY24, the PSAI segment’s revenue grew 2% YoY to INR13.7b. The price erosion in the base portfolio adversely impacted the performance of PSAI segment for 1HFY24.
- Considering the new launches and volume uptick in base business going forward, we expect the PSAI business to post a 3% sales CAGR to INR31b over FY23-25.

Reiterate Neutral

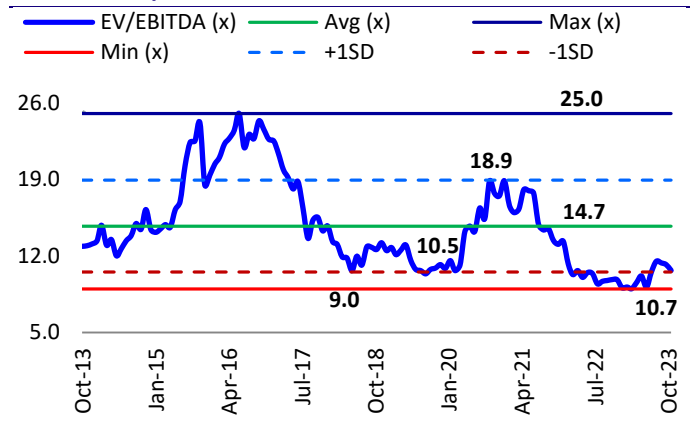
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- After a strong 31% earnings CAGR over FY21-23, we expect earnings growth momentum to moderate to 12% CAGR over FY23-25 due to the high base on account of g-Revlimid and gradual recovery in EM/PSAI sales. Further, the current valuation adequately factors in the earnings upside. **Reiterate Neutral.**

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 ~11% over FY23–25

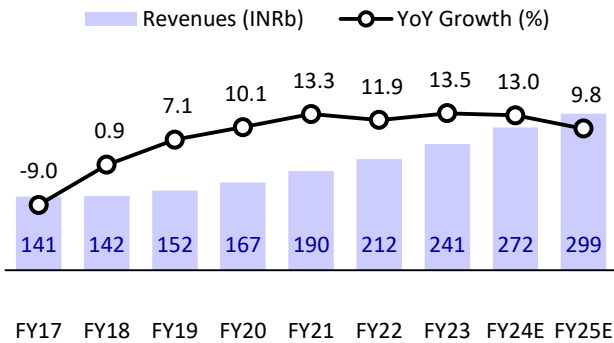


Exhibit 9: NA sales to report ~17% CAGR over FY23–25

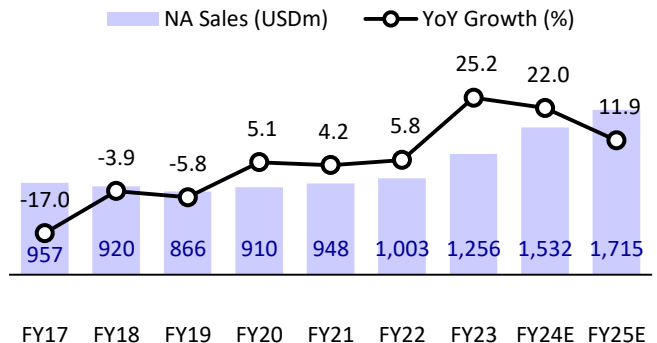


Exhibit 10: DF sales to exhibit 8% CAGR over FY23–25

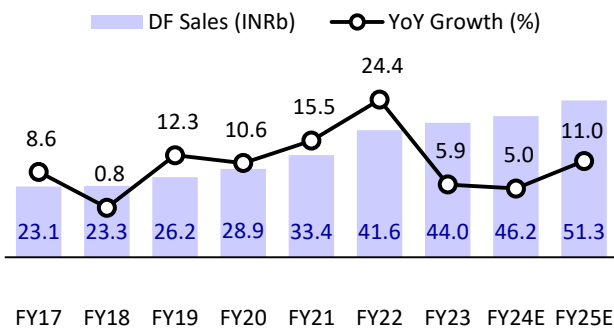


Exhibit 11: PSAI to post ~3% sales CAGR over FY23–25

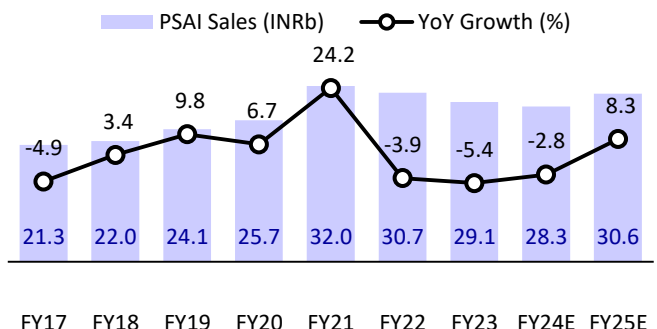


Exhibit 12: EBITDA margin to expand 100bp over FY23–25

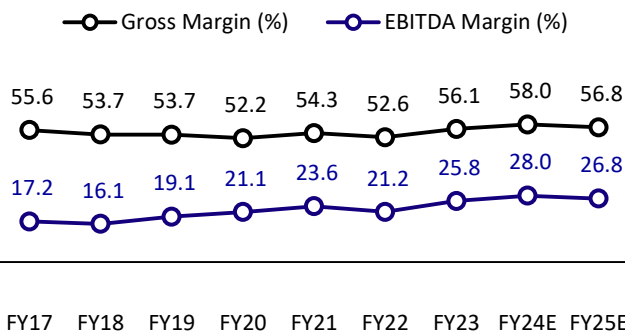


Exhibit 13: Expect EBITDA CAGR of ~14% over FY23–25

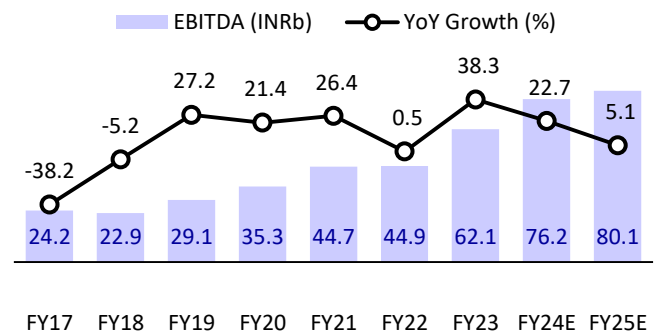


Exhibit 14: R&D expense to settle at ~8% of sales by FY25

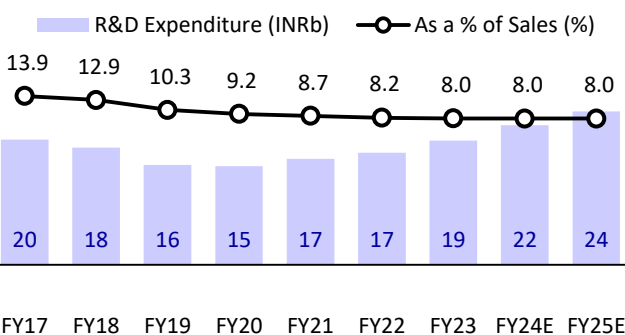
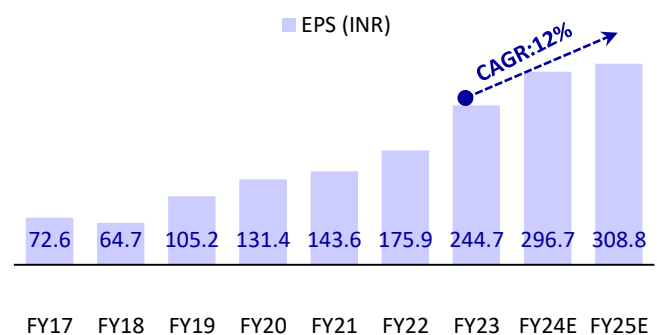


Exhibit 15: Expect EPS CAGR of 12% over FY23–25



Source: Company, MOFSL

Source: Company, MOFSL

Financials and valuations

Income Statement									(INR b)
Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
Net Sales	141	142	152	167	190	212	241	272	299
Change (%)	-9.0	0.9	7.1	10.1	13.3	11.9	13.5	13.0	9.8
Total Expenditure	117	119	123	132	145	167	179	196	219
EBITDA	24	23	29	35	45	45	62	76	80
Change (%)	-38.2	-5.2	27.2	21.4	26.4	0.5	38.3	22.7	5.1
Margin (%)	17.2	16.1	19.1	21.1	23.6	21.2	25.8	28.0	26.8
Depreciation & Amort.	12	12	12	12	13	12	13	15	16
EBIT	12	11	17	23	32	33	49	61	65
Net Interest Exp	0	1	1	1	-2	-2	-3	-1	-1
One-off (Gains)/Losses	0	0	-2	8	8	6	-5	0	0
PBT before EO Expense	12	10	18	14	26	29	58	62	66
Change (%)	-46.0	-2.1	56.5	14.7	35.9	10.5	39.5	22.1	2.5
PBT after EO Expense	12	10	18	14	26	29	58	62	66
Tax	3	5	4	-1	9	9	15	16	16
Tax Rate (%)	21.0	44.0	20.5	-10.3	35.5	30.3	26.5	26.4	24.5
Reported PAT	12	10	19	19	18	24	44	49	51
Adjusted Net Profit	12	11	17	22	24	29	41	49	51
Change (%)	-46.7	-10.8	62.6	24.9	9.3	22.8	39.3	21.2	4.1
Margin (%)	8.5	7.6	11.5	13.0	12.6	13.8	16.9	18.1	17.2

Balance Sheet									(INR b)
Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
Equity Share Capital	1	1	1	1	1	1	1	1	1
Reserves	122	125	139	155	176	190	230	275	323
Net Worth	123	126	140	156	176	191	231	276	323
Loans	49	51	34	18	29	34	13	12	11
Deferred Liabilities/Tax	-5	-3	-4	-12	-10	-13	-6	-6	-6
Capital Employed	167	173	171	162	195	212	238	282	329
Gross Block	93	99	115	126	144	161	178	191	200
Less: Accum. Deprn.	42	50	62	74	87	99	111	126	142
Net Fixed Assets	56	57	54	52	57	62	66	65	58
Investments	26	29	31	33	33	38	62	62	62
Goodwill/Intangibles	46	47	47	32	41	32	35	35	35
Curr. Assets	83	87	88	103	125	152	151	188	243
Inventory	29	29	34	35	45	51	49	61	58
Account Receivables	38	41	40	52	50	67	72	86	92
Cash and Bank Balance	4	3	2	2	15	15	6	17	66
Others	12	14	13	14	15	19	24	25	27
Curr. Liability & Prov.	45	47	50	58	60	72	77	75	77
Account Payables	11	13	14	15	18	26	26	23	26
Other Current Liabilities	34	34	36	43	42	47	50	52	51
Net Current Assets	38	40	39	45	65	79	74	120	173
Appl. of Funds	167	173	171	162	195	212	238	282	329

Financials and valuations

Ratios

Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
Basic (INR)									
EPS	72.6	64.7	105.2	131.4	143.6	175.9	244.7	296.7	308.8
Cash EPS	143.3	135.5	177.3	206.5	220.7	246.9	320.8	386.6	402.1
BV/Share	739.6	757.3	844.8	939.7	1,062.8	1,145.0	1,386.5	1,657.9	1,941.6
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	8.5	8.1
Valuation (x)									
P/E	74.3	83.4	51.3	41.1	37.6	30.7	22.1	18.2	17.5
PEG (x)	NA	-7.7	0.8	1.6	4.0	1.3	0.6	0.9	4.3
Cash P/E	37.7	39.8	30.4	26.1	24.5	21.9	16.8	14.0	13.4
P/BV	7.3	7.1	6.4	5.7	5.1	4.7	3.9	3.3	2.8
EV/Sales	6.5	6.4	5.9	5.2	4.6	4.1	3.5	3.0	2.6
EV/EBITDA	37.9	40.0	30.8	24.9	19.6	19.5	13.5	10.9	9.7
Dividend Yield (%)	0.4	0.4	0.4	0.4	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	26.3	25.7
RoE	9.7	8.6	13.1	14.7	14.3	16.0	19.3	19.5	17.2
RoCE	6.4	4.8	8.9	17.4	11.8	12.3	15.9	18.4	16.3
Working Capital Ratios									
Fixed Asset Turnover (x)	1.6	1.5	1.4	1.4	1.4	1.4	1.4	1.5	1.5
Debtor (Days)	103	101	97	100	98	100	106	106	108
Inventory (Days)	70	74	75	75	77	83	75	73	72
Payable (Days)	25	31	32	32	32	38	39	33	30
Leverage Ratio									
Current Ratio (x)	1.8	1.8	1.8	1.8	2.1	2.1	2.0	2.5	3.2
Net Debt/Equity (x)	0.1	0.1	0.0	-0.1	-0.2	-0.2	-0.3	-0.3	-0.6

Cash Flow Statement

Y/E March	FY17	FY18	FY19	FY20	FY21	FY22	FY23	FY24E	FY25E
(INR b)									
Op. Profit/(Loss) before Tax	15	14	22	26	35	39	54	66	68
Depreciation	12	12	12	12	13	12	13	15	16
Interest/Dividends Recd.	-2	-4	-6	5	6	3	-7	-4	-2
Direct Taxes Paid	-3	-5	-4	1	-9	-9	-15	-16	-16
(Inc)/Dec in WC	0	-3	1	-6	-7	-15	-4	-28	-3
CF from Operations	21	14	25	38	38	30	40	33	62
EO Expense	0	0	0	0	-6	-5	0	0	0
CF from Operations	21	18	29	39	44	34	40	33	62
(inc)/dec in FA	-41	-14	-9	5	-27	-8	-20	-13	-9
Free Cash Flow	-20	1	16	43	11	22	20	20	53
(Pur)/Sale of Investments	18	1	3	-2	0	-5	-24	0	0
Others	5	-3	-2	-7	0	-13	0	0	0
CF from Investments	-18	-15	-8	-5	-27	-26	-44	-13	-9
Change in net worth	-11	-3	0	1	2	-5	0	0	0
(Inc)/Dec in Debt	16	2	-17	-16	12	4	-20	-1	-1
Other Items	-4	1	-1	-5	-13	9	1	2	2
Dividend Paid	-4	-4	-4	-5	-5	-4	-4	-4	-4
CF from Fin. Activity	-4	-4	-21	-25	-5	4	-23	-3	-3
Inc/Dec of Cash	-1	-1	0	8	13	12	-27	17	50
Add: Beginning Balance	5	4	3	2	2	15	15	6	17
Closing Balance	4	3	2	11	15	27	-12	22	66
FX Impact	0	0	0	0	0	0	0	0	0
FX impact net of bank balances	0	0	0	-9	0	-12	18	-6	0
Closing Balance	4	3	2	2	15	15	6	17	66

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BUY	>=15%
SELL	< - 10%
NEUTRAL	< - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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