

28 July 2024

India | Equity Research | Q1FY25 results review

Dr Reddy's Laboratories

Pharma

Surging dependency on gRevlimid

Higher gRevlimid sales, in our view, formed the premise for Dr. Reddy's Laboratories' (DRL) Q1FY25 beat. US sales soared 20.3% YoY to USD 462mn riding on market share gains in existing products. Gross margins in the global generics segment expanded 80bps YoY (270bps QoQ) to 64.7%. We believe this surge was largely fuelled by market share improvement in gRevlimid (sales pegged at USD 140mn in Q1). Integration of Sanofi's vaccine portfolio boosted growth in India (15.4%) while the base business grew in mid-single-digit. Management envisages the base portfolio's double-digit growth continuing in FY25 and DRL further benefitting from a consolidation in Sanofi's vaccine portfolio and launch of the Nutraceutical-Nestle JV. While revenue traction may sustain in the near term, rising competition in key products in US, soaring R&D/marketing costs may restrain margins. We lower our rating to **REDUCE**, raise TP to INR 6,350 valuing the base business at 22x FY26E core EPS of INR 263 and INR 550 in NPV for gRevlimid.

US and India drive growth, overheads dent margins

DRL's Q1FY25 revenue grew 13.9% YoY (8.3% QoQ) to INR 76.7bn (I-Sec: INR 71.6bn). Gross margin, at 60.4%, expanded 170bps YoY/183bps QoQ. EBITDA rose 4.2% YoY at INR 21.3bn (I-Sec: INR 20.8bn). EBITDA margin slumped 256bps to 27.7% (+258bps QoQ) due to higher SG&A cost. R&D costs rose 24.3% YoY to INR 6.2bn and stood at 8.1% of revenue vs. 7.4% in Q1FY24 and 9.7% in Q4FY24. Adj. PAT declined 0.9% YoY to INR 13.9bn (I-Sec: INR 14.3bn).

Momentum in India and US likely to sustain in near term

US revenue surged 18% QoQ to USD 463mn (I-Sec: USD 404mn) led by better volumes for existing products. In Q1, it launched three new products and filed one product with the USFDA. DRL's biosimilar denosumab (collaborated with Alvotech) in FY26 and abatacept (in-licensed from Coya Therapeutics) in FY27. We expect US sales to grow at a CAGR of ~7% over FY24–26E. India biz grew a robust 15.4% YoY to INR 13.3bn. Excluding vaccine sales, India revenue grew in mid-single-digit. The JV with Nestle India, to launch consumer nutritional brands in India, is expected to become operational in Aug'24. We expect the India business to grow at a CAGR of ~15% over FY24–26E. EU grew 4% YoY to INR 5.3bn, driven by new launches. Russia sales declined 1.8% YoY due to unfavorable currency movement and CIS was down 5% YoY at INR 1.9bn due to dip in volumes. RoW business was up 13.3% YoY (-8.4% QoQ) at INR 4.5bn. PSAI revenue surged 14.1% YoY (-6.8% QoQ) to INR 7.7bn. DRL has filed 11 DMF globally in Q1FY25.

Financial Summary

Y/E March (INR mn)	FY23A	FY24A	FY25E	FY26E
Net Revenue	2,40,938	2,79,164	3,21,451	3,55,633
EBITDA	59,497	78,233	87,649	95,743
EBITDA Margin (%)	24.7	28.0	27.3	26.9
Net Profit	41,989	55,686	61,154	65,059
EPS (INR)	252.0	333.9	366.6	390.0
EPS % Chg YoY	91.0	23.4	9.8	6.4
P/E (x)	25.4	20.6	18.8	17.6
EV/EBITDA (x)	18.4	13.8	11.8	10.3
RoCE (%)	17.6	20.1	18.5	17.1
RoE (%)	19.9	21.8	19.9	18.1

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Market Data

Market Cap (INR)	1,148bn
Market Cap (USD)	13,715mn
Bloomberg Code	DRRD IN
Reuters Code	REDY.BO
52-week Range (INR)	6,966 /5,206
Free Float (%)	73.0
ADTV-3M (mn) (USD)	39.4

Price Performance (%)	3m	6m	12m
Absolute	10.0	17.5	25.6
Relative to Sensex	(0.3)	2.4	3.7

Earnings Revisions (%)	FY25E	FY26E
Revenue	5.7	4.8
EBITDA	6.0	4.6
EPS	6.6	5.2

Previous Reports

27-06-2024: [Company Update](#)

08-05-2024: [Q4FY24 results review](#)

Valuation and risks

Rise in market share in gRevlimid and in-licensed biosimilars are a few catalysts for driving growth in US in FY25–26E. Besides, India growth is expected to pick up in the quarters ahead as it will likely benefit from integration of Sanofi's vaccine portfolio and Nutraceuticals brands of Nestle (through JV). Windfall from the earnings of gRevlimid is being utilised to build a robust consumer health business (current size of USD 320mn). DRL had recently announced the acquisition of the Nicotinell brand from Haleon, which is expected to add revenues of USD 300mn to the consumer franchise in a couple of years; the company further aims to scale up consumer brand sales to USD 1bn through M&As and growth in the existing business. While its revenue growth will likely be supported by inorganic initiatives, the relatively higher spend on R&D and SG&A costs of the new business are expected to keep margins in check. Overall, we expect revenue/PAT CAGRs of 11.1%/8.1%, over FY24–26E, while EBITDA margins may see a 110bps dent to 26.9% in FY26E due to higher R&D and overheads.

At its CMP of INR 6,879, the stock trades at valuations of 30x FY25E and 26.2x FY26E ex-Revlimid earnings and EV/EBITDA multiples of 16.9x FY25E and 13.3x FY26E. We lower our rating to **REDUCE** (earlier *Hold*), though raise our target price to INR 6,350 (from INR 6,050), valuing the base business' FY26E earnings of INR 263 at 22x and NPV of INR 550 for gRevlimid.

Key upside risk: M&A in key areas of focus and cost optimisation to curtail overhead cost.

Q1FY25 conference call highlights

US

- US growth was driven by better volumes for existing products and new launches
- In Q1, DRL launched three new products and filed one product with the USFDA. It has 80 filings pending approval with the FDA, of which 23 are first to file products.
- The in-licensed biosimilar abatacept will be launched in CY27.
- It has collaborated with Alvotech for the commercialisation of their denosumab biosimilar candidate in US, Europe and UK. The product is expected to be commercialised in FY26.
- 20% of R&D spending is towards development of biosimilar products.

India

- Growth was mainly driven by 13 new launches in Q1FY25 and in-licensed vaccine portfolio from Sanofi.
- Base business grew in mid-single-digits (excluding vaccine biz). Management expects base business to grow in double-digits in FY25.

Europe

- In Europe, growth was driven by improvement in volumes and new product launches, which was partly offset by price erosion.
- It launched 12 new products in Europe in Q1.

Russia & CIS

- Sales from Russia declined due to unfavourable currency exchange rate movements, partially offset by price increases and higher base business volumes.
- CIS growth was impacted by low volumes for base business, partly offset by increase in prices.

PSAI

- It has filed 11 DMFs globally.

New Initiatives

- DRL is acquiring Nicotinell and its related brands in the Nicotine Replacement Therapy category in markets outside US from Haleon PLC for GBP 500mn (includes upfront cash payment of GBP 458mn and contingent payments of GBP 42mn), The transaction is expected to close in Q4CY24.
- DRL has entered into a JV with Nestle India to launch consumer nutritional brands in India. The JV is expected to become operational in Q2FY25.
- Partnered with Novartis Pharma LLC to distribute two anti-diabetes brands, Galvus and Galvus Met, in the Russia.
- Launched drug-free migraine management device, Nerivio in Germany, Spain, UK and South Africa.
- Inaugurated a 70,000sq.ft. biologics facility of Aurigene Pharmaceutical Services in Genome Valley, Hyderabad.

Guidance

- Management expects SG&A spending to be between 27.5–28% in FY25.
- Maintained tax rate guidance of 24–25%.
- Overall annual sales of consumer biz stood at USD 320mn post acquisition it will become a USD 600mn biz, which the company aims to scale up to USD 1bn in the near future through acquisition.
- Ahead, it would also focus on in-licensing novel brands and will also invest in building new capacities including a plant for injectables and peptides.

Q1FY25 performance

- It incurred capex of INR 4.9bn and generated cash of INR 2.3bn.
- Q1 cashflow was impacted by higher outgo of cash tax outgo in the overseas markets.
- Overall cash at end of Q1FY25 stood at INR 67.3bn, operating working capital at INR 115.5bn.
- Gross margin improvement was on account of product mix and overhead leverage.
- SG&A increase was due to new business initiatives, higher freight costs, business integration costs and annual increments.

Exhibit 1: Q1FY25 result review

Y/E Mar (INR mn)	Q1FY25	Q1FY24	YoY(%)	Q4FY24	QoQ (%)	FY24	FY23	YoY(%)
Net Sales	76,727	67,384	13.9	70,830	8.3	2,79,164	2,40,938	15.9
Gross Profit	46,344	39,553	17.2	41,483	11.7	1,63,607	1,34,402	21.7
Gross Margins (%)	60.4	58.7	170.3	58.6	183.4	58.6	55.8	
EBITDA	21,266	20,400	4.2	17,807	19.4	78,233	59,497	31.5
EBITDA Margins (%)	27.7	30.3	(255.8)	25.1	257.6	28.0	24.7	
Other Income	529	823	(35.7)	691	(23.4)	4,346	6,277	(30.8)
Interest	(837)	(784)		(1,022)		(3,994)	(2,853)	
Depreciation	3,806	3,533	7.7	3,677	3.5	14,700	12,502	17.6
Extraordinary expenses	5	11		(173)		3	(4,242)	
PBT	18,821	18,463	1.9	16,016	17.5	71,870	60,367	19.1
Tax	4,901	4,438	10.4	2,946	66.4	16,186	15,300	5.8
Tax Rate (%)	26.0	24.0		18.4		22.5	25.3	
PAT	13,920	14,025	(0.7)	13,070	6.5	55,684	45,067	23.6
Adj. PAT	13,915	14,036	(0.9)	12,929	7.6	55,686	41,900	32.9
NPM (%)	18.1	20.8		18.5		19.9	17.4	

Source: I-Sec research, Company data

Exhibit 2: Segmental break-up

INR mn	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24	Q3FY24	Q4FY24	Q1FY25	% YoY	% QoQ
Generics	44,323	55,946	59,241	54,257	60,083	61,159	63,095	61,190	68,857	14.6	12.5
North America	17,815	28,001	30,567	25,321	31,978	31,775	33,492	32,626	38,462	20.3	17.9
US (USD mn)	230	351	375	312	389	385	401	392	462	18.7	17.7
India	13,339	11,500	11,274	12,834	11,482	11,860	11,800	11,265	13,252	15.4	17.6
Europe	4,141	4,199	4,303	4,960	5,071	5,361	4,970	5,208	5,265	3.8	1.1
Russia	3,200	5,900	6,900	5,200	5,600	5,800	5,900	5,000	5,500	(1.8)	10.0
RoW	3,928	4,146	3,997	3,642	3,952	4,163	4,633	4,891	4,478	13.3	(8.4)
CIS	1,900	2,200	2,200	2,300	2,000	2,200	2,300	2,200	1,900	(5.0)	(13.6)
API	7,090	6,434	7,758	7,787	6,709	7,034	7,839	8,219	7,657	14.1	(6.8)
Proprietary products	740	677	701	924	592	684	1,214	1,420	212	(64.2)	(85.1)
Total	52,153	63,057	67,700	62,968	67,384	68,877	72,148	70,829	76,726	13.9	8.3

Source: I-Sec research, Company data

Exhibit 3: Key growth drivers of domestic business in Q1FY25

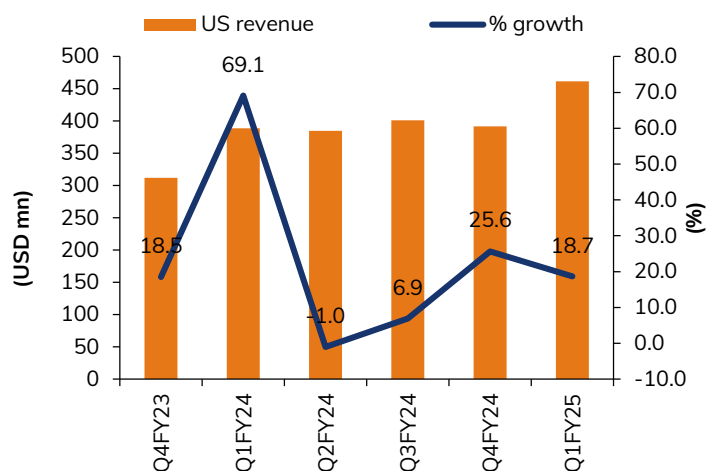
Brands (INR mn)	Q1FY25	Q1FY24	YoY (%)	Q4FY24	QoQ (%)	MAT Mar'24	MAT Mar'23	YoY (%)
Voveran	565	658	-14.1	608	-7.1	2,594	2,456	5.6
Omez	618	594	4.1	567	9.0	2,176	1,972	10.3
Atarax	542	476	13.7	505	7.2	2,039	1,919	6.2
Econorm	643	580	11.0	437	47.4	1,873	1,737	7.8
Ketorol	585	428	36.5	482	21.3	1,700	1,433	18.7
Hexaxim	371	362	2.4	413	-10.4	1,520	1,109	37.0
Venusia	354	268	32.3	389	-8.9	1,335	1,055	26.5
Razo-D	341	387	-11.9	333	2.6	1,394	1,392	0.2
Zedex	260	279	-6.8	371	-29.9	1,307	1,364	-4.2
Menactra	318	286	10.9	308	3.1	1,233	822	50.1

Source: IQVIA

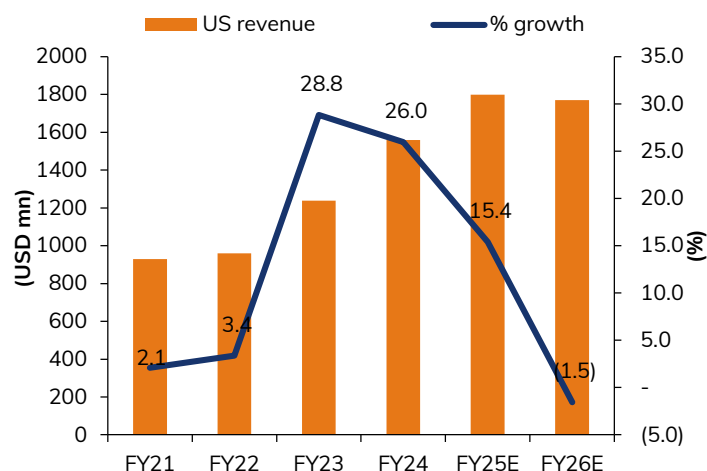
Exhibit 4: Growth profile across key therapies in India

Key therapies (INR mn)	Q1FY25	Q1FY24	YoY (%)	Q4FY24	QoQ (%)	MAT Mar'24	MAT Mar'23	YoY (%)
Gastro Intestinal	3,094	2,932	5.5	2,676	15.6	10,877	9,772	11.3
Respiratory	1,872	1,806	3.7	2,476	-24.4	9,288	8,667	7.2
Pain / Analgesics	1,914	1,760	8.8	1,790	6.9	7,152	6,457	10.8
Cardiac	1,783	1,785	-0.1	1,624	9.8	6,541	7,443	-12.1
Derma	1,304	1,087	20.0	1,242	5.0	4,822	4,196	14.9
Vaccines	1,342	1,215	10.5	1,205	11.4	4,839	3,444	40.5
Anti-Diabetic	1,019	956	6.6	927	10.0	3,740	3,389	10.4
Vitamins/Minerals/Nutrients	1,010	895	12.8	872	15.7	3,666	3,462	5.9
Stomatologicals	837	715	17.0	768	8.9	3,073	2,369	29.7
Anti-Infectives	649	576	12.8	756	-14.1	3,023	2,683	12.7

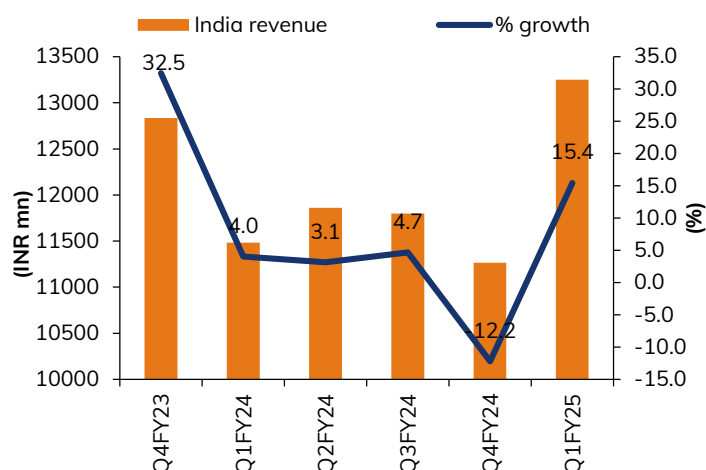
Source: IQVIA

Exhibit 5: US revenue surged due to market share improvement in existing products

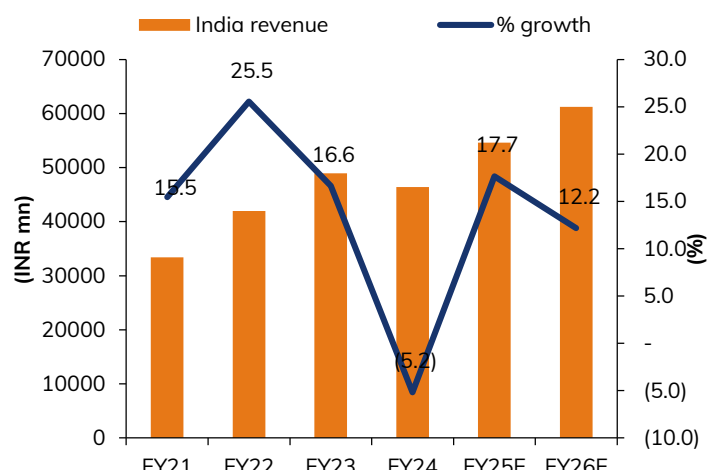
Source: I-Sec research, Company data

Exhibit 6: Limited growth visibility in US beyond FY24

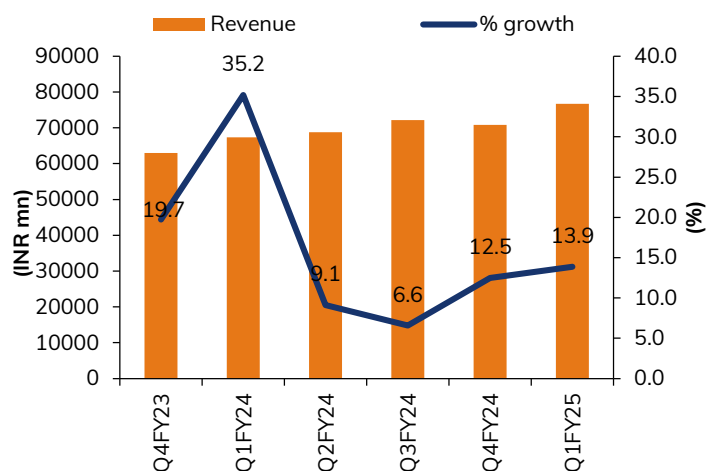
Source: I-Sec research, Company data

Exhibit 7: Domestic business grew a robust 15.4% YoY in Q1FY25

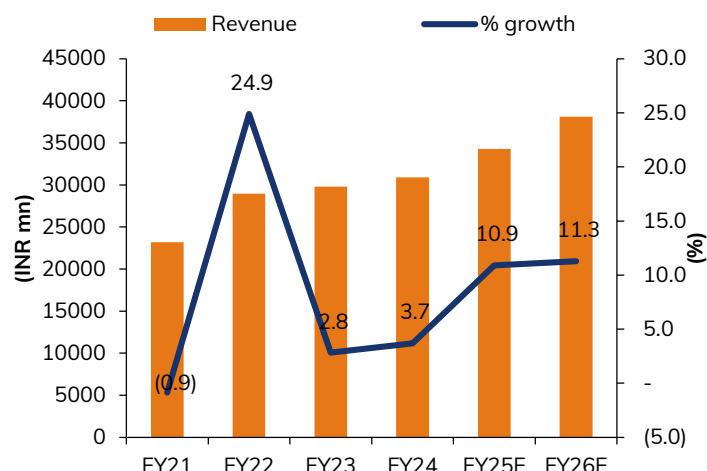
Source: I-Sec research, Company data

Exhibit 8: Double-digit growth expected in India from FY25E

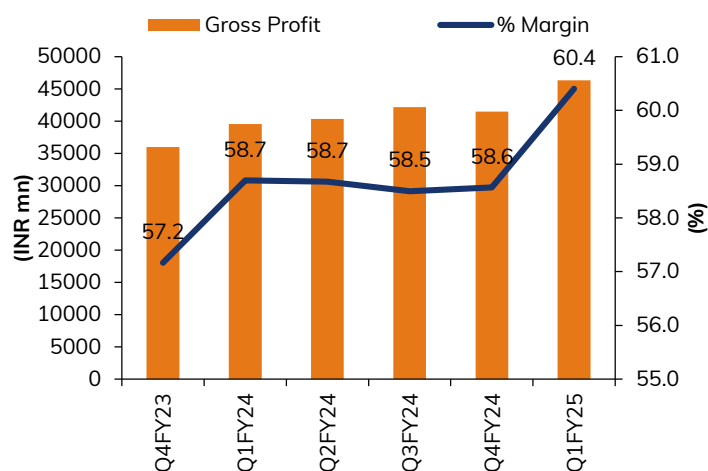
Source: I-Sec research, Company data

Exhibit 9: US and India markets boosted overall growth

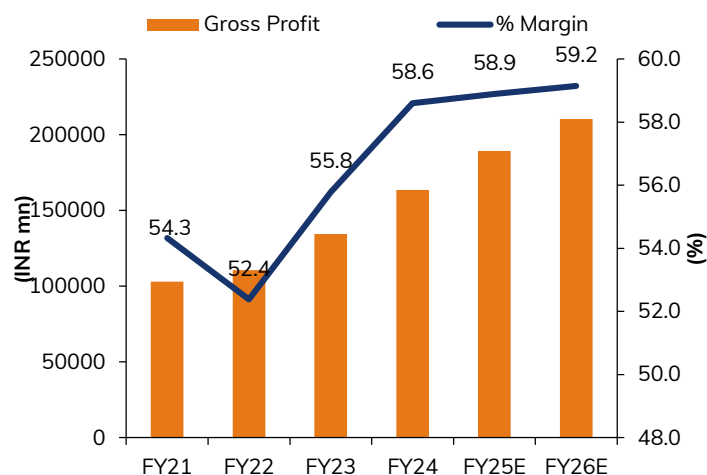
Source: I-Sec research, Company data

Exhibit 10: Revenue to grow at 11.1% CAGR over FY24-FY26E

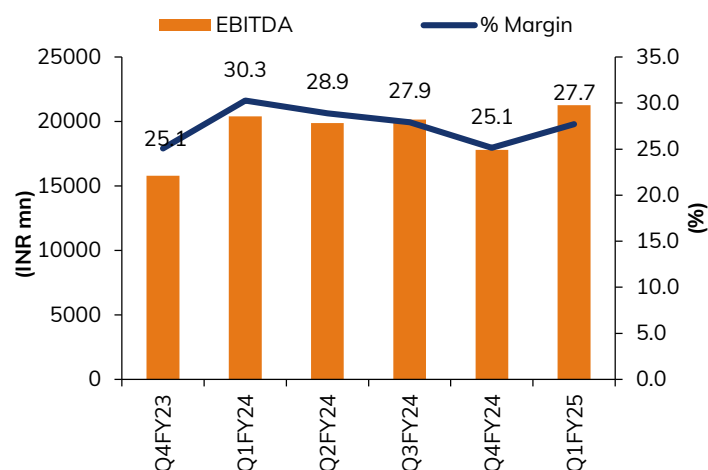
Source: I-Sec research, Company data

Exhibit 11: Gross margin improved on account of better product mix and overhead leverage

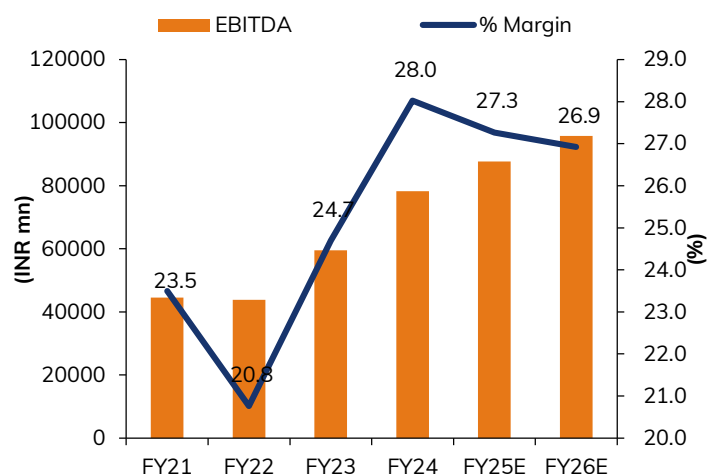
Source: I-Sec research, Company data

Exhibit 12: Gross margin to remain stable at ~59% going ahead

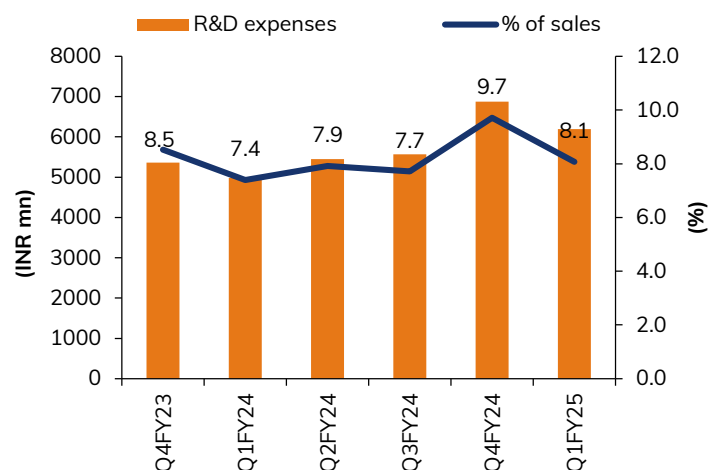
Source: I-Sec research, Company data

Exhibit 13: EBITDA margins slumped 256bps YoY due to higher SG&A cost

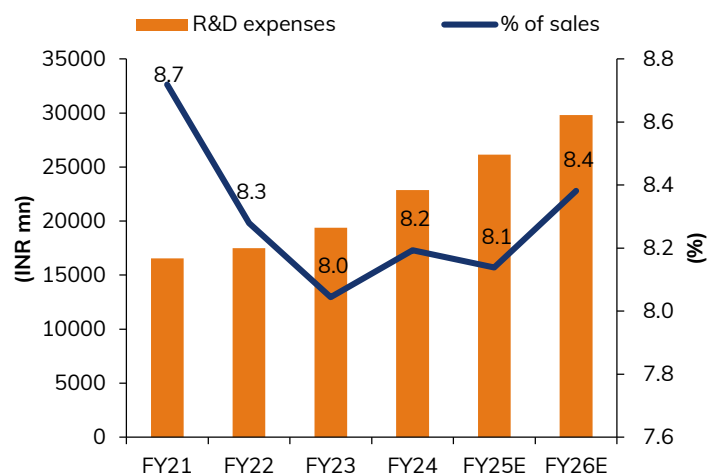
Source: I-Sec research, Company data

Exhibit 14: Higher spends in R&D and SG&A cost of new business to curb margins

Source: I-Sec research, Company data

Exhibit 15: R&D expense declined to ~8%

Source: I-Sec research, Company data

Exhibit 16: R&D spend to jump to ~8.5–9% in FY25E

Source: I-Sec research, Company data

Exhibit 17: Shareholding pattern

%	Dec'23	Mar'24	Jun'24
Promoters	26.7	26.7	26.7
Institutional investors	62.6	62.8	63.1
MFs and others	8.2	8.0	10.1
Insurance Cos	7.8	7.7	9.7
FII's	46.6	47.1	43.3
Others	10.7	10.5	10.2

Source: Bloomberg, I-Sec research

Exhibit 18: Price chart

Source: Bloomberg, I-Sec research

Financial Summary

Exhibit 19: Profit & Loss

(INR mn, year ending March)

	FY23A	FY24A	FY25E	FY26E
Net Sales	2,40,938	2,79,164	3,21,451	3,55,633
Operating Expenses	74,905	85,374	1,01,676	1,14,624
EBITDA	59,497	78,233	87,649	95,743
EBITDA Margin (%)	24.7	28.0	27.3	26.9
Depreciation & Amortization	12,502	14,700	15,777	16,904
EBIT	46,995	63,533	71,872	78,839
Interest expenditure	-	-	-	-
Other Non-operating Income	8,760	8,193	8,433	6,587
Recurring PBT	55,755	71,726	80,305	85,426
Profit / (Loss) from Associates	370	147	162	178
Less: Taxes	15,300	16,186	19,312	20,545
PAT	40,455	55,540	60,993	64,881
Less: Minority Interest	-	-	-	-
Extraordinaries (Net)	-	-	-	-
Net Income (Reported)	45,067	55,684	61,154	65,059
Net Income (Adjusted)	41,989	55,686	61,154	65,059

Source Company data, I-Sec research

Exhibit 20: Balance sheet

(INR mn, year ending March)

	FY23A	FY24A	FY25E	FY26E
Total Current Assets	2,06,940	2,51,767	3,10,866	3,74,338
of which cash & cash eqv.	61,797	81,470	1,28,428	1,72,913
Total Current Liabilities & Provisions	73,651	82,009	91,477	1,00,818
Net Current Assets	1,33,289	1,69,758	2,19,388	2,73,520
Investments	5,362	5,255	5,255	5,255
Net Fixed Assets	66,462	76,886	76,109	74,205
ROU Assets	-	-	-	-
Capital Work-in-Progress	-	-	-	-
Total Intangible Assets	35,094	41,204	41,204	41,204
Other assets	800	1,632	1,879	2,079
Deferred Tax Assets	7,196	10,774	10,774	10,774
Total Assets	2,48,203	3,05,509	3,54,610	4,07,037
Liabilities				
Borrowings	13,472	20,020	17,020	14,020
Deferred Tax Liability	833	909	909	909
provisions	59	61	61	61
other Liabilities	2,848	3,969	3,969	3,969
Equity Share Capital	3,172	2,367	2,367	2,367
Reserves & Surplus	2,27,819	2,78,183	3,30,284	3,85,711
Total Net Worth	2,30,991	2,80,550	3,32,651	3,88,078
Minority Interest	-	-	-	-
Total Liabilities	2,48,203	3,05,509	3,54,610	4,07,037

Source Company data, I-Sec research

Exhibit 21: Cashflow statement

(INR mn, year ending March)

	FY23A	FY24A	FY25E	FY26E
Operating Cashflow	58,873	45,433	74,011	72,117
Working Capital Changes	11,295	(1,809)	8,928	3,941
Capital Commitments	(41,371)	(40,283)	33,365	(10,565)
Free Cashflow	17,502	5,150	1,07,376	61,552
Other investing cashflow	-	-	-	-
Cashflow from Investing Activities	(41,371)	(40,283)	33,365	(10,565)
Issue of Share Capital	157	805	-	-
Interest Cost	(1,428)	(1,711)	-	-
Inc (Dec) in Borrowings	-	-	-	-
Dividend paid	(4,979)	(6,648)	(9,054)	(9,632)
Others	(20,611)	3,791	(3,000)	(3,000)
Cash flow from Financing Activities	(26,861)	(3,763)	(12,054)	(12,632)
Chg. in Cash & Bank balance	(9,359)	1,387	95,322	48,921
Closing cash & balance	5,493	7,166	1,02,429	1,51,350

Source Company data, I-Sec research

Exhibit 22: Key ratios

(Year ending March)

	FY23A	FY24A	FY25E	FY26E
Per Share Data (INR)				
Reported EPS	270.5	333.8	366.6	390.0
Adjusted EPS (Diluted)	252.0	333.9	366.6	390.0
Cash EPS	327.1	422.0	461.2	491.4
Dividend per share (DPS)	30.0	40.0	54.3	57.7
Book Value per share (BV)	1,386.5	1,682.0	1,994.3	2,326.6
Dividend Payout (%)	11.1	12.0	14.8	14.8
Growth (%)				
Net Sales	14.1	15.9	15.1	10.6
EBITDA	35.7	31.5	12.0	9.2
EPS (INR)	91.0	23.4	9.8	6.4
Valuation Ratios (x)				
P/E	25.4	20.6	18.8	17.6
P/CEPS	21.0	16.3	14.9	14.0
P/BV	5.0	4.1	3.4	3.0
EV / EBITDA	18.4	13.8	11.8	10.3
P / Sales	4.8	4.1	3.6	3.2
Dividend Yield (%)	0.4	0.6	0.8	0.8
Operating Ratios				
Gross Profit Margins (%)	55.8	58.6	58.9	59.2
EBITDA Margins (%)	24.7	28.0	27.3	26.9
Effective Tax Rate (%)	27.4	22.6	24.0	24.0
Net Profit Margins (%)	16.8	19.9	19.0	18.2
NWC / Total Assets (%)	-	-	-	-
Net Debt / Equity (x)	(0.2)	(0.2)	(0.4)	(0.4)
Net Debt / EBITDA (x)	(0.9)	(0.9)	(1.3)	(1.7)
Profitability Ratios				
RoCE (%)	17.6	20.1	18.5	17.1
RoE (%)	19.9	21.8	19.9	18.1
RoIC (%)	22.7	27.1	27.2	28.3
Fixed Asset Turnover (x)	3.9	4.1	4.4	4.7
Inventory Turnover Days	83	95	84	82
Receivables Days	-	-	-	-
Payables Days	45	46	43	41

Source Company data, I-Sec research

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