

Robust growth across key markets, niche research assets differentiator



Dr. Reddy's Q2FY22 results were better than estimates. Robust demand for Covid and non Covid products across markets, aided revenue growth and profitability.

- Adj. Sales came in at Rs 57.6 bn, +18% yoy/+17% qoq. Sales include income from sale of rights for E7777 - anti cancer molecule to Citius Pharmaceuticals Inc.
- Sales by segment, Global Generics Rs 47.4 bn (+19% yoy/+15% qoq).
- PSAI Rs 8.4 bn (-2% yoy/+11% qoq).
- PP Rs 1.8 bn +198% includes license fee relating to sale of US & Canada rights of ELYXYB to BioDelivery Sciences Inc.
- Sales growth was from ROW, India, Russia, US and Europe.
- EBITDA came in at Rs 12.7 bn +31% yoy/+49% qoq.
- EBITDA margins at 27%, highest in last 7 quarters (+270 bps yoy/+570 bps qoq).
- Adjusted PAT came in at Rs 9.9 bn, +30% yoy/+74% qoq.
- EPS for the quarter was at Rs 59.6.

Key Triggers & monitorables

- Niche launches (gREVLIMID, SPIRIVA and more) across markets.
- Normalization of SPUTNIK supplies and EUA for Sputnik Lite.
- USFDA observations to DUVVADA plant. The management indicated that the observations are product related and are addressable. The company plans to reply to USFDA within the stipulated time.

Financial Summary

Y/E Mar (Rs mn)	FY19	FY20	FY21	FY22E	FY23E
Net sales	1,54,482	1,75,170	1,90,475	2,24,032	2,52,475
EBITDA	31,782	41,945	45,467	52,889	64,444
Adjusted net profit	19,500	20,340	19,516	31,786	39,903
Free cash flow	23,797	31,830	14,073	25,675	26,273
EPS (Rs)	117.5	122.4	117.3	191.0	239.8
growth (%)	106	4	(4)	63	26
P/E (x)	39.8	38.2	39.8	24.4	19.5
P/B (x)	5.5	5.0	4.4	3.9	3.2
EV/EBITDA (x)	25.3	18.8	17.4	14.9	12.1
D/E	0.2	0.1	0.2	0.1	0.1
RoIC (%)	13.6	14.5	12.2	18.9	21.6
RoE (%)	13.9	13.0	11.1	15.9	16.7
Dividend yield (%)	0.6	1.0	1.0	1.0	1.0

Source: Company

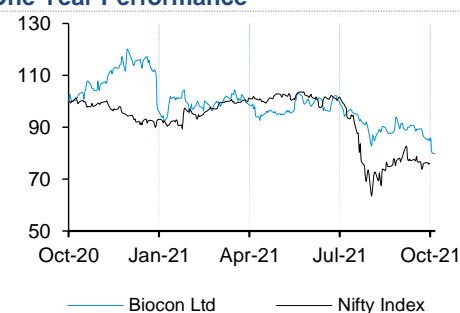
Rating	TP (Rs)	Up/Dn (%)
BUY	5,809	25

Market data

Current price	Rs	4,659
Market Cap (Rs.Bn)	(Rs Bn)	775
Market Cap (US\$ Mn)	(US\$ Mn)	10,345
Face Value	Rs	5
52 Weeks High/Low	Rs	5,649 / 4,135
Average Daily Volume	('000)	275
BSE Code		500124
Bloomberg		DRRD.IN

Source: Bloomberg

One Year Performance



Source: Bloomberg

(%) Shareholding	Sep-21	Jun-21
Promoter	26.72	26.73
Public	72.99	72.92
Total	0.29	0.32

Source: Bloomberg

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Conference Call Highlights

A. North America

- **US:** Rs 18.9 bn (+9% yoy/+3% qoq), due to volume growth, new launches which was offset by price erosion in some molecules.
- 4 new launches including gREVLIMID in Canada and 2 ANDA filings during the quarter.
- Healthy growth in existing products like gVASCEPA, Suboxone film.
- USFDA approval for gREVLIMID with 180 days exclusivity for 2.5 mg and 20 mg segment. The product has a market size of \$5bn each. Dr. Reddy's has settled with BMS (Celgene) for the same.

B. India

- **India:** Rs 11.4 bn (+25% yoy/+8% qoq) due to higher volumes, Covid related products (Sputnik, 2 deoxy -D-glucose) and price increase in some products.
- The company launched 2 new products (Melotryl and Baricax) during the quarter.
- The quarter saw limited growth from SPUTNIK during Q2, in view of lack of supplies for the 2nd dose.
- Currently Sputnik and Sputnik Lite is under trials for children aged 2-12 and adolescents aged 12-18 years, for the export markets.
- In India, Dr. Reddy's is along with other pharma companies conducting trials for Molnupiravir, for the Indian market. The company expects data in the current quarter.

C. Russia & CIS

- **Russia & CIS:** Rs 7.9 bn (+32% yoy/+61% qoq), driven by higher volumes, price increase and new launches.
- The company launched Bevacizumab in Russia during the quarter.
- CIS growth was mainly from new launches as CIS had lower volumes and price erosion on high base. Sequential growth was from higher volumes and price increases.

D. ROW

- **ROW:** Rs 5.1 bn (+90% yoy/+22% qoq), due to Covid portfolio, new launches and volume growth partially offset by price erosion in some products.

E. Europe

- Europe Rs 4.1 bn (+10% yoy/+1% qoq), due to volume growth in base business, new launches partially offset by price erosion in some products.

F. PSAI

- PSAI Rs 8.4 bn (-2% yoy/+11% qoq), due to growth from Covid portfolio offset by lower volumes and prices partially offset by new products. The company filed 2 DMFs during Q2FY22.

G. Proprietary Products

- Proprietary Products Rs 1.8 bn, +195% yoy/+238% qoq.
- Includes license fee from sale of US and Canada rights of ELYXYB (Celecoxib oral solution) to BioDelivery Sciences International Inc.

Quarterly Financials

Particulars	Q2FY22	Q1FY22	Q2FY21	% yoy	% qoq	H1FY22	H1FY21	% Change
Net Income from Sales & Services	57632	49194	48967	18%	17%	106826	93142	15%
Gross Profit	30786	25699	26409	17%	20%	56485	51164	
GPM (%)	53.4%	52.2%	53.9%			52.9%	54.9%	
SG&A expenses	-15951	-15045	-13107	22%	6%	-30996	-25893	
R&D Expenses	-4463	-4534	-4359			-8997	-8339	
EBIDTA excl one offs	15573	10472	12673	23%	49%	26045	24296	7%
EBIDTA (%)	27.0%	21.3%	25.9%			24.4%	26.1%	
Other Income	1743	487	149			2230	267	735%
Impairment	0	0	-781			0	-781	
EBIT	12115	6607	8311			18722	16418	14%
Interest	319	652	237			971	842	
PBT excl. one offs	12434	7259	8548	45%	71%	19693	19684	
Profit before tax	12434	7259	8548	45%	71%	19693	17260	14%
Tax	-2761	-1717	-998			-4478	-3994	
Profit After tax before MI	9673	5542	7550			15215	13266	15%
Share of Profit	247	166	73			413	150	
Profit After Tax	9920	5708	7623	30%	74%	15628	13416	16%
NPM (%)	17.21%	11.60%	15.57%			14.63%	14.40%	
Adjusted Net Profit	9920	5708	7623			15628	13416	
Equity	832	832	830.6			832	830.6	
Number of shares	166.4	166.4	166.12			166.4	166.12	
EPS excl exceptional	59.62	34.30	45.89			117.21	155.94	
EPS -(Rs)	59.62	34.30	45.89			115.31	117.38	

Robust revenue growth driven by strong demand across geographies

US price erosion and lower export incentives reduce gross margins

Other income includes gain on sale of E7777 rights

Cost Analysis	Q1FY23	Q1FY22	Q2FY21	% yoy	% qoq	H1FY22	H1FY21	% Change
Raw Materials	46.6%	47.8%	46.1%			47.1%	45.1%	
SG&A	-27.7%	-30.6%	-26.8%			-29.0%	-27.8%	
R & D	-7.7%	-9.2%	-8.9%			-8.4%	-9.0%	

% profitability	Q1FY23	Q1FY22	Q2FY21	% yoy	% qoq	H1FY22	H1FY21	% Change
Gross margin	53.4%	52.2%	53.9%			52.9%	54.9%	
EBITDA margin	27.0%	21.3%	25.9%			24.4%	26.1%	
PBT margin	21.6%	14.8%	17.5%			18.4%	18.5%	
PAT margin	17.2%	11.6%	15.6%			14.6%	14.4%	

Valuation & Outlook

Dr. Reddy's has robust growth across markets, both including and excluding Covid. The company has niche launches like gVASCEPA, Suboxone film and also has USFDA approvals for large assets like GREVLIMID, gSPIRIVA.

The company's niche research pipeline includes 46 Para IVs and 23 First to files for North America (Developed markets).

We believe Dr. Reddy's will continue to grow across geographies. We have increased our estimates for both FY22E and FY23E for Sales/Ebitda/PAT by 1%/3%/4%.

At Rs 4670, Dr. Reddy's trades at 19x FY23E EPS of Rs 249.8 and 12x EV/EBITDA. We have valued Dr. Reddy's as a weighted average (50:50) of 24x P/E and 15x EV/EBITDA and arrived at a target price of Rs 5809, indicating a 24% upside from current levels.

We upgrade our rating from BUY on Dips to BUY.

Financials

P&L (Rs mn)	FY19	FY20	FY21	FY22E	FY23E	Cash Flow St. (Rs. mn)	FY19	FY20E	FY21E	FY22E	FY23E
Net Sales	1,54,482	1,75,170	1,90,475	2,24,032	2,52,475	Net Profit	19,500	20,340	19,516	31,786	39,903
Other operating income						Add: Dep. & Amort.	11,348	11,631	12,288	12,938	13,913
Raw materials	(44,948)	(55,070)	(60,789)	(76,106)	(83,490)	Cash profits	30,848	31,971	31,804	44,724	53,816
Employee costs	(33,562)	(33,802)	(36,299)	(39,929)	(43,922)	(Inc)/Dec in					
Other Expenses	(44,190)	(44,353)	(47,920)	(55,108)	(60,619)	-Sundry debtors	714	(12,033)	2,256	(8,980)	(7,594)
Cost of sales	(1,22,700)	(1,33,225)	(1,45,008)	(1,71,143)	(1,88,031)	-Inventories	(4,490)	(1,488)	(10,345)	(2,090)	(6,142)
Operating Profit	31,782	41,945	45,467	52,889	64,444	-Loans/advances	(834)	(2,010)	1,406	(154)	(161)
Depreciation	(11,348)	(11,631)	(12,288)	(12,938)	(13,913)	-Sundry creditors	326	1,577	2,861	2,772	2,026
Impairment	-	(17,160)	(6,768)	-	-	-Others	3,636	2,409	(1,282)	(94)	(117)
PBIT	20,434	13,154	26,411	39,951	50,531	Change in working capita	(648)	(11,545)	(5,104)	(8,546)	(11,989)
Other income	3,375	6,206	2,914	3,205	3,526	CF from Oper. activities	30,200	20,426	26,700	36,179	41,828
Interest	(889)	(983)	(970)	(883)	(883)	CF from Inv. activities	(10,954)	4,989	(27,514)	(23,749)	(30,831)
Profit before tax	22,920	18,377	28,355	42,273	53,174	CF from Fin. activities	(22,647)	(46,498)	7,097	(10,708)	(2,355)
Provision for tax	(3,858)	1,402	(9,319)	(10,991)	(13,825)	Cash generated/(utilise	(3,401)	(21,083)	6,283	1,721	8,641
PAT Bfr Excp Items	19,062	19,779	19,036	31,282	39,349	Cash at start of the year	7,205	5,628	6,432	17,574	19,295
Share of Profit	438	561	480	504	554	Cash at end of the year	5,628	6,432	17,574	19,295	27,936
Net Profit	19,500	20,340	19,516	31,786	39,903	Ratios	FY19	FY20	FY21	FY22E	FY23E
Balance Sheet						OPM	20.6	23.9	23.9	23.6	25.5
Equity capital	830	831	832	832	832	NPM	12.4	11.2	10.1	14.0	15.6
Reserves	1,39,406	1,55,157	1,75,585	1,98,609	2,38,512	Tax rate	(16.8)	7.6	(32.9)	(26.0)	(26.0)
Net worth	1,40,236	1,55,988	1,76,417	1,99,441	2,39,344	Growth Ratios (%)					
Def. Tax Liab.+Minority Ir	473	20	289	318	350	Net Sales	8.2	13.4	8.7	17.6	12.7
Secured loans	22,000	1,304	6,299	6,299	6,299	Operating Profit	35.2	32.0	8.4	16.3	21.8
Unsecured loans	12,125	16,532	23,145	23,145	23,145	PAT	106.0	4.3	(4.1)	62.9	25.5
Total debt	34,125	17,836	29,444	29,444	29,444	Per Share (Rs.)					
Other Liabilities	2,181	2,055	1,617	1,779	1,957	Net Earnings (EPS)	117.5	122.38	117.3	191.0	239.8
CAPITAL EMPLOYED	1,77,015	1,75,899	2,07,767	2,30,982	2,71,095	Cash Earnings (CPS)	185.8	192.4	191.1	268.8	323.4
Gross block	1,66,901	1,77,184	1,89,015	1,99,015	2,14,015	Dividend	30.0	45.0	45.0	45.0	46.0
Accumulated depreciati	(1,17,774)	(1,29,405)	(1,41,693)	(1,54,631)	(1,68,544)	Book Value	844.8	938.6	1,060.2	1,198.6	1,438.4
Net block	49,127	47,779	47,322	44,384	45,471	Free Cash Flow	115.9	152.9	(4.9)	74.7	66.1
Capital WIP	4,725	4,364	9,539	9,539	9,539	Valuation Ratios					
Total fixed assets	53,852	52,143	56,861	53,923	55,010	P/E(x)	40	38	40	24	19
Intangible assets	42,734	26,798	35,248	35,859	36,532	P/B(x)	6	5	4	4	3
Goodwill	4,659	4,913	5,599	5,599	5,599	EV/EBIDTA(x)	25	19	17	15	12
Investments	25,871	26,778	28,077	41,077	56,078	EV/SALES(x)	5	4	4	4	3
Other non current assets	1,138	1,002	1,075	1,213	1,371	Div. Yield(%)	1	1	1	1	1
Inventories	33,579	35,067	45,412	47,502	53,643	FCF Yield(%)	2	3	(0)	2	1
Sundry debtors	39,982	52,015	49,759	58,739	66,334	Return Ratios (%)					
Cash & bank	5,628	6,432	17,574	19,295	27,936	ROE	13.9	13.0	11.1	15.9	16.7
Loans & advances	2,472	4,482	3,076	3,230	3,391	ROCE	11.5	7.5	12.7	17.3	18.6
Other current assets	10,424	10,424	12,801	14,081	15,489	ROA	11.8	11.3	9.6	14.0	15.0
Sundry creditors	(13,671)	(15,248)	(18,109)	(20,881)	(22,907)	ROIC	13.6	14.5	12.2	18.9	21.6
Acceptances	(5,537)	(8,114)	(9,100)	(10,010)	(11,011)						
Provisions	(5,582)	(5,414)	(5,523)	(5,799)	(6,089)						
Working capital	44,444	52,066	70,221	80,488	1,01,117						
Deferred tax assets	4,317	12,199	10,686	12,823	15,388						
CAPITAL DEPLOYED	1,77,015	1,75,899	2,07,767	2,30,982	2,71,095						

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