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STOCK BROKING PVT. LTD.

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Result update@ Dalal & Broacha

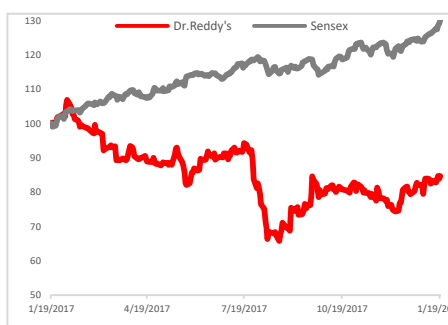
Buy on Dips

Current Price	2352
Target Price	2800
Upside/Downside	19%
52 Week Range	3175/1902

Key Share Data

Market Cap (Rs.bn)	415
Market Cap (US\$ mn)	6431
No of o/s shares (mn)	170.6
Face Value	5
Monthly Avg. vol (BSE+NSE) Nos'000	449
BSE Code	500124
NSE Code	DRREDDY
Bloomberg	DRRD IN Equity

Price performance



Dr. Reddy's Labs Q3FY18 results were in line with expectations. While revenues were in line with estimates, the profits were lower than estimates. Sequentially performance improved considerably with a 300 bps improvement in gross margins, due to milestone payment from Encore Dermatology and 3 new launches in US and 2 in Canada.

Sequential performance improves, betters margins

Revenues grew 3% to Rs 38060 mn (+7% qoq), due to 2% de-growth in Global Generics to Rs 30105 mn and flat performance in PSAI (CRAMS) to Rs 5436 mn. Proprietary Products grew 10% to Rs 2519 mn. Gross margins were 280 bps lower yoy (up 290 bps qoq) to 56.1%. EBITDA decreased 8% to Rs 8055 mn due to increase in SG &A spends. EBITDA margins were 260 bps lower yoy (up 170 bps qoq) to 21.2%. After significantly higher taxes, PAT de-grew 29% to Rs 3344 mn (increased 17% qoq).

Key takeaways from the concall

- In Global Generics, US de-grew 3% (up 12% qoq) to Rs 16073 mn due to pricing pressure on account of channel consolidation. Going forward, the company expects annualized price erosion in low double digits.
- During the quarter DRL launched Sevelamer Carbonate and gained market share.
- The company launched 3 new products during the quarter. DRL was also the first to launch gAzacitidine injectable in Canada.
- India revenues grew 3% yoy to Rs 6136 mn. Post GST adjustments, it works out to a 11% yoy growth.
- In Proprietary products, DRL's IMPOYZ cream received USFDA approval, which triggered a milestone payment of Rs 1300 mn from its partner Encore Dermatology Inc.
- DRL's focus is on strengthening its manufacturing and quality management systems.
- During the quarter, the company received and Establishment Inspection Report (EIR) for 2 sites at Srikakulam.
- DRL also received clearance from the German regulator which will help ramp up supplies to EU.
- DRL expects to invite USFDA for re-inspection of Duvvada in a quarter or two.
- In the US, DRL plans a larger proportion of high value products in FY19.
- Copaxone approval is expected to be delayed by 4-5 months.

% Shareholding	Dec-17	Sep-17
Promoters	26.76	26.77
FII	29.27	29.65
DII	15.36	13.49
Others	28.61	30.09
Total	100	100

Outlook & Valuation

We are positive on the developments at Dr. Reddy's. Although the much awaited re-inspection at Duvvada may be in a quarter or two, the company is catching up pace through high value launches. Although there have been delays, DRL still has significant value with a high contribution to US generics. At Rs 2352, DRL trades at 19x FY20E EPS of Rs 136.9. We recommend investors to BUY on DIPS with a target price of Rs 2800.

Key Financials

Year	Net sales	% Growth	EBIDTA	OPM (%)	PAT	% Growth	EPS	PE (x)	RoE (%)	RoCE (%)
FY16	155,683.0	4.4	35,853.0	23.0	21,306.0	(8.8)	124.9	20.5	17.0	16.3
FY17	141,961.0	(8.8)	24,722.0	17.4	12,921.0	(39.4)	77.9	32.9	10.5	8.2
FY18E	156,346.1	10.1	27,975.1	17.9	14,079.5	9.0	84.9	30.2	10.8	9.3
FY19E	176,827.8	13.1	35,610.5	20.1	19,212.2	36.5	115.9	22.1	12.8	12.1
FY20E	198,994.4	12.5	42,734.1	21.5	22,704.3	18.2	136.9	18.7	13.1	13.6



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Particulars	Q3FY18	Q2FY18	Q3FY17	% yoy	% qoq	FY17	FY16	% Change
Net Income from Sales & Services	38060	35460	37065	3%	7%	140809	154708	-9%
Gross Profit	21411	18901	21899			78356	92281	
GPM (%)	56.3%	53.3%	59.1%			55.6%	59.6%	
SG&A expenses	-12048	-11032	-11341			-46372	-45702	
R&D Expenses	-4667	-4175	-4956			-19551	-17834	
EBIDTA	8055	6888	8793	-8%	17%	25495	36252	-30%
EBIDTA (%)	21.2%	19.4%	23.7%			18.1%	23.4%	
Other Income	313	114	187			1065	874	
EBIT	5009	3808	5789	-13%	32%	13498	29619	-54%
Interest	851	-24	44			806	-2708	
Profit before tax	5860	3784	5833	0%	55%	14304	26911	-47%
Tax	-2601	-1027	-1221			-2614	-7127	
Profit After tax before MI	3259	2757	4612	-29%	18%	11690	19784	-41%
Minority Interest (MI)	0	0	0			0	0	
Share of Profit	85	92	89			349	229	
Profit After Tax	3344	2849	4701	-29%	17%	12039	20013	-40%
NPM (%)	8.79%	8.03%	12.68%			8.55%	12.94%	
Equity	829	829	853			853	853	
EPS -(Rs)	20.17	17.18	27.56			72.61	117.3	



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Dr Reddy's Laboratories Limited											
P&L (Rs mn)	FY16	FY17	FY18E	FY19E	FY20E	Cash Flow St. (Rs. mn)	FY16	FY17	FY18E	FY19E	FY20E
Net Sales	155,683.0	141,961.0	156,346.1	176,827.8	198,994.4	Net Profit		12,921.0	14,079.5	19,212.2	22,704.3
						Add: Dep. & Amort.		10,266.0	11,095.4	11,761.5	12,871.5
Raw materials	(37,585.0)	(34,449.0)	(37,456.4)	(41,566.0)	(46,842.4)	Cash profits		23,187.0	25,174.9	30,973.6	35,575.8
Employee costs	(31,174.0)	(31,068.0)	(34,796.2)	(40,015.6)	(46,017.9)	(Inc)/Dec in					
Other Expenses	(39,260.0)	(38,788.0)	(41,891.0)	(43,985.6)	(46,184.9)	-Sundry debtors		3,264.0	(1,805.5)	(5,285.8)	(5,722.1)
Selling Expenses	(11,811.0)	(12,934.0)	(14,227.4)	(15,650.1)	(17,215.2)	-Inventories		(2,949.0)	1,302.2	(3,616.6)	(3,915.1)
Cost of sales	(119,830.0)	(117,239.0)	(128,371.0)	(141,217.3)	(156,260.3)	-Loans/advances		(188.0)	(169.6)	(186.6)	(205.2)
Operating Profit	35,853.0	24,722.0	27,975.1	35,610.5	42,734.1	-Sundry creditors		1,501.0	(307.0)	1,125.9	1,445.6
Depreciation	(9,389.0)	(10,266.0)	(11,095.4)	(11,761.5)	(12,871.5)	-Others		(55.0)	763.1	824.4	891.2
PBIT	26,464.0	14,456.0	16,879.7	23,849.0	29,862.6	Change in working capital		1,573.0	(216.8)	(7,138.6)	(7,505.6)
Other income	2,950.0	1,715.0	2,229.5	2,898.4	3,767.9	CF from Oper. activities		24,760.0	24,958.1	23,835.0	28,070.2
Interest	(826.0)	(634.0)	(941.5)	(851.5)	(801.5)	CF from Inv. activities		(24,051.0)	(14,262.5)	(18,000.0)	(30,000.0)
Profit before tax	28,588.0	15,537.0	18,167.7	25,895.9	32,828.9	CF from Fin. activities		809.0	(9,296.9)	(4,420.9)	642.1
Provision for tax	(7,511.0)	(2,965.0)	(4,541.9)	(7,250.8)	(10,833.5)	Cash generated/(utilised)		1,518.0	1,398.6	1,414.2	(1,287.7)
PAT Bfr Exp Items	21,077.0	12,572.0	13,625.8	18,645.0	21,995.4	Cash at start of the year		4,921.0	3,865.0	5,263.6	6,677.8
Share of Profit	229.0	349.0	453.7	567.1	708.9	Cash at end of the year		3,865.0	5,263.6	6,677.8	5,390.1
Net Profit	21,306	12,921	14,079	19,212	22,704	Ratios	FY16	FY17	FY18E	FY19E	FY20E
Balance Sheet	FY16	FY17	FY18E	FY19E	FY20E	OPM	23.0	17.4	17.9	20.1	21.5
Equity capital	853.0	829.0	829.0	829.0	829.0	NPM	13.4	9.0	8.9	10.7	11.2
Reserves	124,845.0	121,792.0	130,051.4	149,263.6	171,967.8	Tax rate	(26.3)	(19.1)	(25.0)	(28.0)	(33.0)
Net worth	125,698.0	122,621.0	130,880.4	150,092.6	172,796.8	Growth Ratios (%)					
Def. Tax Liab.+Minority Int.	537.0	1,620.0	1,782.0	1,960.2	2,156.2	Net Sales	4.4	(8.8)	10.1	13.1	12.5
Secured loans	10,685.0	5,449.0	5,449.0	5,449.0	5,449.0	Operating Profit	6.1	(31.0)	13.2	27.3	20.0
Unsecured loans	22,718.0	43,626.0	39,626.0	34,626.0	34,626.0	PAT	(8.8)	(39.4)	9.0	36.5	18.2
Total debt	33,403.0	49,075.0	45,075.0	40,075.0	40,075.0	Per Share (Rs.)					
Other Liabilities	2,503.0	3,434.0	3,795.7	4,197.2	4,643.3	Net Earnings (EPS)	124.9	77.9	84.9	115.9	136.9
CAPITAL EMPLOYED	162,141.0	176,750.0	181,533.1	196,325.0	219,671.4	Cash Earnings (CPS)	179.9	139.8	151.8	186.8	214.6
Gross block	131,518.0	145,935.0	153,935.0	163,935.0	183,935.0	Dividend	25.0	20.0	30.0	30.0	30.0
Accumulated depreciation	(85,388.0)	(95,654.0)	(106,749.4)	(118,510.9)	(131,382.4)	Book Value	736.8	739.6	789.4	905.3	1,042.2
Net block	46,130.0	50,281.0	47,185.6	45,424.1	52,552.6	Free Cash Flow	-	4.3	64.5	35.2	(11.6)
Capital WIP	6,626.0	6,095.0	5,000.0	5,000.0	5,000.0	Valuation Ratios					
Total fixed assets	52,756.0	56,376.0	52,185.6	50,424.1	57,552.6	P/E(x)	20.5	32.9	30.2	22.1	18.7
Intangible assets	15,946.0	41,413.0	42,770.5	42,770.5	42,770.5	P/B(x)	3.5	3.5	3.2	2.8	2.5
Goodwill	4,650.0	4,763.0	4,763.0	4,763.0	4,763.0	EV/EBIDTA(x)	13.0	19.0	16.6	12.9	10.8
Investments	38,331.0	21,097.0	27,097.0	35,097.0	45,097.0	EV/SALES(x)	3.0	3.3	3.0	2.6	2.3
Other non current assets	3,347.0	5,166.0	5,166.0	5,166.0	5,166.0	Div. Yield(%)	1.0	0.8	1.2	1.2	1.2
Inventories	25,579.0	28,528.0	27,225.8	30,842.4	34,757.5	FCF Yield(%)	-	0.2	2.5	1.4	(0.5)
Sundry debtors	41,250.0	37,986.0	39,791.5	45,077.3	50,799.4	Return Ratios (%)					
Cash & bank	4,921.0	3,865.0	5,263.6	6,677.8	5,390.1	ROE	17.0	10.5	10.8	12.8	13.1
Loans & advances	1,508.0	1,696.0	1,865.6	2,052.2	2,257.4	ROCE	16.3	8.2	9.3	12.1	13.6
Other current assets	9,648.0	10,491.0	10,491.0	10,491.0	10,491.0						
Sundry creditors	(9,068.0)	(10,569.0)	(10,262.0)	(11,388.0)	(12,833.5)						
Acceptances	(3,589.0)	(4,647.0)	(5,111.7)	(5,622.9)	(6,185.2)						
Provisions	(6,237.0)	(5,967.0)	(6,265.4)	(6,578.6)	(6,907.5)						
Working capital	41,206.0	41,151.0	42,766.5	51,319.2	57,537.1						
Deferred tax assets	5,905.0	6,784.0	6,784.6	6,785.2	6,785.2						
CAPITAL DEPLOYED	162,141.0	176,750.0	181,533.1	196,325.0	219,671.4						

Note: Annual numbers based on IND AS



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