



Dr. Reddy's Q1FY22 results were below estimates. Higher contribution from India (22% Vs 16-18%) due to severe second Covid19 wave and marginally lower US sales impacted profitability. The management is confident of restoring profitability in the coming quarters.

- **Adj. Sales came in at Rs 49.1 bn**, +11% yoy/+4% qoq, 2% lower than our estimate.
- Sales growth was from India, ROW, Europe, Russia and US.
- **EBITDA came in at Rs 10.47 bn** -10% yoy/-8% qoq due to higher material costs, SG&A and R & D spend.
- **EBITDA margins at 21.3%**, -500 bps yoy/-270 bps qoq
- **Adjusted PAT came in at Rs 5.7 bn**, -1% yoy/-29% qoq.
- **EPS for the quarter was at Rs 34.3.**

Revenue by geographies

- **US:** Rs 17.4 bn (+1% yoy/+1% qoq), due to volume growth, new launches which was offset by price erosion in some molecules and adverse forex rates. 2 ANDA filings during the quarter.
- **India:** Rs 10.6 bn (+69% yoy/+26% qoq) due to higher volumes, new Covid related launches (Sputnik, 2 deoxy -D-glucose) and price increase in some products.
- **Russia & CIS:** Rs 4.9 bn (+4% yoy/-17% qoq).
- **ROW:** Rs 4.2 bn (+25% yoy/+43% qoq), due to new launches and volume growth partially offset by price erosion in some products.
- **Europe** Rs 4 bn (+12% yoy/+1% qoq), due to volume growth in base business, new launches partially offset by price erosion in some products.
- **PSAI** Rs 7.5 bn (-12% yoy/-5% qoq), due to lower volumes and prices partially offset by new products, also on high base. The company filed 2 DMFs during Q1FY22.
- **Proprietary Products** Rs 541 mn, -1% yoy/-14% qoq.

Y/E Mar (Rs mn)	FY19	FY20	FY21	FY22E	FY23E
Net sales	1,54,482	1,75,170	1,90,475	2,21,390	2,49,568
EBITDA	31,782	41,945	45,467	51,172	62,526
Adjusted net profit	19,500	20,340	19,516	30,516	38,483
Free cash flow	23,797	31,830	14,073	25,441	24,966
EPS (Rs)	117.5	122.4	117.3	183.4	231.3
growth (%)	106	4	(4)	56	26
P/E (x)	41.2	39.6	41.3	26.4	20.9
P/B (x)	5.7	5.2	4.6	4.1	3.4
EV/EBITDA (x)	26.2	19.5	18.0	16.0	12.9
D/E	0.2	0.1	0.2	0.1	0.1
RoIC (%)	13.6	14.5	12.2	18.2	21.0
RoE (%)	13.9	13.0	11.1	15.4	16.3
Dividend yield (%)	0.6	0.9	0.9	0.9	0.9

Source: Company

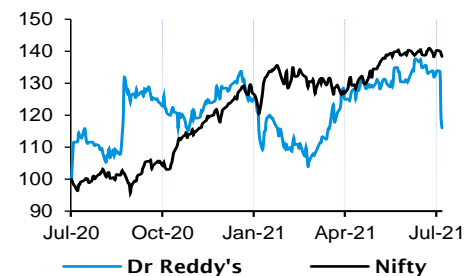
Rating	TP (Rs)	Up/Dn (%)
BUY ON DIPS	5621	19

Market data

Current price	Rs	4730
Market Cap (Rs.Bn)	(Rs Bn)	787
Market Cap (US\$ Mn)	(US\$ Mn)	10584
Face Value	Rs	5
52 Weeks High/Low	Rs	5614/4020
Average Daily Volume	('000)	6110
BSE Code		500124
Bloomberg		DRRD:IN

Source: Bloomberg

One Year Performance



Source: Bloomberg

% Shareholding	Jun-21	Mar-21
Promoters	26.73	26.74
FII	29.04	29.03
DII	15.74	14.90
Others	28.49	29.33
Total	100	100

Source: BSE

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Key Highlights

1. **Gross margins:** 52.2% (-380 bps yoy/-150 bps qoq) due to lower margins across Global Generics, PSAI and PP segments.
2. **R & D spend:** Rs 4.5 bn +14% yoy, 9% of sales. The management expects higher spend in view of biosimilar trials for the Russian market.
3. Capex Rs 3.2 bn.
4. Net cash Rs 451 mn.
5. Free Cash Flow Rs 6.8 bn. Strong CF generation.
6. **Lower EBITDA peculiar in the current quarter due to price erosion in some products in the US.** The company expects improvement (24-25%) over the coming quarters with value added launches, increased market share in recent launches (gVASCEPA, gKUVAN and many more), increased PSAI sales and growth in India branded sales.
7. In the US, the company has planned for 26-28 new launches, in line with FY21.
8. **Russia & ROW** – the management is confident of growth with new launches.
9. **Higher SG&A spend to continue in view of OTC launches in India and other markets.** The company has launched CurHealth- a nutritional product and has a pipeline of OTC products for the Indian market. The management also plans to widen its network into rural India.
10. **Dr. Reddy's has 93 ANDAs pending USFDA approval, of which 47 are Para IVs and the company believes 24 have FTF status.**
11. R & D spend higher in view of trials for 4 biosimilars for the Russian market.
12. **Dr. Reddy's has Invested in digitization for India** – a healthcare platform combining the entire ecosystem for faster execution and break even.
13. Dr. Reddy's has received an anonymous complaint and received a subpoena from SEC. The complaint alleges that healthcare professionals in Ukraine and potentially in other countries were provided improper payments by or on behalf of the company, in violation of US anti-corruption laws, specifically the U.S. Foreign Corrupt Practices Act. A U.S. law firm is conducting the investigation at the instruction of a committee of Company's Board of Directors. The investigation is ongoing. The Company has disclosed the matter to the U.S. Department of Justice, Securities and Exchange Commission ("SEC") and Securities Exchange Board of India, and on 6 July 2021 the Company received a subpoena from the SEC for the production of documents pertaining to certain CIS geographies, and the Company is in the process of responding to the same. While the matter may result in government enforcement actions against the Company in the United States and/or foreign jurisdictions, which could lead to civil and criminal sanctions under relevant laws, the probability of such action and the outcome are not reasonably ascertainable at this time.

Margin impact due to unfavourable sales mix, higher SG & A and R & D spend

The company expects supplies of SPUTNIK V from September-November.

Plans to launch OTC brands in India

Quarterly Financials

Particulars	Q1FY22	Q4FY21	Q1FY21	% yoy	% qoq	FY21	FY20	% Change
Net Income from Sales & Services	49194	47284	44175	11%	4%	189742	174601	9%
Gross Profit	25699	25375	24755	4%	1%	103097	94010	
GPM (%)	52.2%	53.7%	56.0%			54.3%	53.8%	
SG&A expenses	-15045	-14279	-12786	18%	5%	-54559	-50129	
R&D Expenses	-4534	-4094	-3980			-16541	-15410	
EBITDA excl one offs	10472	11330	11623	-10%	-8%	47565	28471	67%
EBITDA (%)	21.3%	24.0%	26.3%			25.1%	16.3%	
Other Income	487	587	118			982	4290	-77%
Impairment	0	0	0			-6753	-16767	
EBIT	6607	7589	8107			26226	15994	64%
Interest	652	318	605			1653	1478	
PBT excl. one offs	7259	7907	11136	-35%	-8%	27879	17472	
Profit before tax	7259	7907	8712	-17%	-8%	27879	17472	60%
Tax	-1717	-2536	-2996			-9175	1466	
Profit After tax before MI	5542	5371	5716			18704	18938	-1%
Share of Profit	166	179	77			800	561	
Profit After Tax	5708	5550	5793	-1%	3%	19504	19499	0%
NPM (%)	11.60%	11.74%	13.11%			10.28%	11.17%	
Adjusted Net Profit	5708	8086				19484	25904	
Equity	832	832	830.6			832	830.6	
Number of shares	166.4	166.4	166.12			166.4	166.12	
EPS excl exceptional	34.30	48.59	34.87			117.21	155.94	
EPS -(Rs)	34.30	33.35	34.87			115.31	117.38	
Cost Analysis	Q1FY22	Q4FY21	Q1FY21	% yoy	% qoq	FY21	FY20	% Change
Raw Materials	47.8%	46.3%	44.0%			45.7%	46.2%	
SG&A	-30.6%	-30.2%	-28.9%			-28.8%	-28.7%	
R & D	-9.2%	-8.7%	-9.0%			-8.7%	-8.8%	
% profitability	Q1FY22	Q4FY21	Q1FY21	% yoy	% qoq	FY21	FY20	% Change
Gross margin	52.2%	53.7%	56.0%			54.3%	53.8%	
EBITDA margin	21.3%	24.0%	26.3%			25.1%	16.3%	
PBT margin	14.8%	16.7%	19.7%			14.7%	10.0%	
PAT margin	11.6%	11.7%	13.1%			10.3%	11.2%	

Source: Dalal & Broacha Research, Company

In view of the increased SG&A and R & D spends, we have revised our estimates of Sales/EBITDA/PAT by 3%/-16%/-15% for FY22 and 4%/-13%/-11% for FY23.

Valuation & Outlook

The stock has seen a sharp correction in view of the subpoena from SEC. The matter is under investigation and any adverse event poses a downside risk. In view of the lower profitability, the management is confident of restoring profitability with value added launches in the US, increase in market share in recent launches, growth in branded products in India and the PSAI segment.

At Rs 4844, Dr. Reddy trades at 21x FY23E EPS of Rs 231. We have valued Dr. Reddy's at 24x FY23E EPS and 15x EV/EBITDA and arrived at a target price of Rs 5621.

We maintain BUY on Dips.

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	2,21,390	2,49,568	Net Profit	19,500	20,340	19,516	30,516	38,483
Other operating income						Add: Dep. & Amort.	11,348	11,631	12,288	12,938	13,913
Raw materials	(44,948)	(55,070)	(60,789)	(75,181)	(82,502)	Cash profits	30,848	31,971	31,804	43,454	52,396
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	(8,267)	(7,523)
Cost of sales	(1,22,700)	(1,33,225)	(1,45,008)	(1,70,218)	(1,87,042)	-Inventories	(4,490)	(1,488)	(10,345)	(1,513)	(6,083)
Operating Profit	31,782	41,945	45,467	51,172	62,526	-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	2,518	2,008
Impairment	-	(17,160)	(6,768)	-	-	-Others	3,636	2,409	(1,282)	(94)	(117)
PBIT	20,434	13,154	26,411	38,234	48,612	Change in working capita	(648)	(11,545)	(5,104)	(7,509)	(11,876)
Other income	3,375	6,206	2,914	3,205	3,526	CF from Oper. activities	30,200	20,426	26,700	35,945	40,520
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	40,556	51,255	CF from Fin. activities	(22,647)	(46,498)	7,097	(10,708)	(2,355)
Provision for tax	(3,858)	1,402	(9,319)	(10,545)	(13,326)	Cash generated/(utilise	(3,401)	(21,083)	6,283	1,487	7,333
PAT Bfr Excp Items	19,062	19,779	19,036	30,012	37,929	Cash at start of the year	7,205	5,628	6,432	17,574	19,061
Share of Profit	438	561	480	504	554	Cash at end of the year	5,628	6,432	17,574	19,061	26,395
Net Profit	19,500	20,340	19,516	30,516	38,483	Ratios	FY19	FY20	FY21	FY22E	FY23E
						OPM	20.6	23.9	23.9	23.1	25.1
						NPM	12.4	11.2	10.1	13.6	15.2
						Tax rate	(16.8)	7.6	(32.9)	(26.0)	(26.0)
						Growth Ratios (%)					
						Net Sales	8.2	13.4	8.7	16.2	12.7
						Operating Profit	35.2	32.0	8.4	12.5	22.2
						PAT	106.0	4.3	(4.1)	56.4	26.1
						Per Share (Rs.)					
						Net Earnings (EPS)	117.5	122.38	117.3	183.4	231.3
						Cash Earnings (CPS)	185.8	192.4	191.1	261.1	314.9
						Dividend	30.0	45.0	45.0	45.0	46.0
						Book Value	844.8	938.6	1,060.2	1,190.9	1,422.2
						Free Cash Flow	115.9	152.9	(4.9)	73.3	58.2
						Valuation Ratios					
						P/E(x)	41	40	41	26	21
						P/B(x)	6	5	5	4	3
						EV/EBIDTA(x)	26	19	18	16	13
						EV/SALES(x)	5	5	4	4	3
						Div. Yield(%)	1	1	1	1	1
						FCF Yield(%)	2	3	(0)	2	1
						Return Ratios (%)					
						ROE	13.9	13.0	11.1	15.4	16.3
						ROCE	11.5	7.5	12.7	16.6	18.1
						ROA	11.8	11.3	9.6	13.6	14.6
						ROIC	13.6	14.5	12.2	18.2	21.0

Balance Sheet	FY19	FY20	FY21	FY22E	FY23E
Equity capital	830	831	832	832	832
Reserves	1,39,406	1,55,157	1,75,585	1,97,339	2,35,822
Net worth	1,40,236	1,55,988	1,76,417	1,98,171	2,36,654
Def. Tax Liab.+Minority Ir	473	20	289	318	350
Secured loans	22,000	1,304	6,299	6,299	6,299
Unsecured loans	12,125	16,532	23,145	23,145	23,145
Total debt	34,125	17,836	29,444	29,444	29,444
Other Liabilities	2,181	2,055	1,617	1,779	1,957
CAPITAL EMPLOYED	1,77,015	1,75,899	2,07,767	2,29,711	2,68,404
Gross block	1,66,901	1,77,184	1,89,015	1,99,015	2,14,015
Accumulated depreciation	(1,17,774)	(1,29,405)	(1,41,693)	(1,54,631)	(1,68,544)
Net block	49,127	47,779	47,322	44,384	45,471
Capital WIP	4,725	4,364	9,539	9,539	9,539
Total fixed assets	53,852	52,143	56,861	53,923	55,010
Intangible assets	42,734	26,798	35,248	35,859	36,532
Goodwill	4,659	4,913	5,599	5,599	5,599
Investments	25,871	26,778	28,077	41,077	56,078
Other non current assets	1,138	1,002	1,075	1,213	1,371
Inventories	33,579	35,067	45,412	46,925	53,008
Sundry debtors	39,982	52,015	49,759	58,026	65,548
Cash & bank	5,628	6,432	17,574	19,061	26,395
Loans & advances	2,472	4,482	3,076	3,230	3,391
Other current assets	10,424	10,424	12,801	14,081	15,489
Sundry creditors	(13,671)	(15,248)	(18,109)	(20,627)	(22,636)
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	79,217	98,427
Deferred tax assets	4,317	12,199	10,686	12,823	15,388
CAPITAL DEPLOYED	1,77,015	1,75,899	2,07,767	2,29,711	2,68,404

Source: Dalal & Broacha Research, Company

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