

CMP: ₹ 1300

Target: ₹ 1570(20%)

Target Period: 12 months

BUY

November 6, 2024

Decent numbers; Optimistic commentary...

About the stock: Dr Reddy's (DRL) business encompasses generic formulations sales across US, Europe, RoW markets and branded generics in India and Russia CIS. The business also comprises of API sales under the head PSAI. The company is increasingly looking to expand its global portfolio with biosimilar and complex formulation offerings.

- Revenue breakup Q2FY25: US (~47%), India (~17%), Russia and CIS (11%), Europe (~7%), RoW (~7%), PSAI (~11%)
- It owns 14 formulation facilities, 9 API manufacturing facilities, one biologics facility and several R&D centres across the globe.

Investment Rationale:

- Q2FY25- Sales upbeat but one offs / higher R&D dent margins- Revenues grew ~17% YoY to ₹ 8038 crore driven by 17% growth in the US to ₹ 3728 crore and 18% growth in India to ₹ 1397 crore. Other geographies also did well with Russia growth of 18% to ₹ 690 crore and RoW growth of 32% to ₹ 560 crore. Growth in Europe was subdued at 9% to ₹ 580 crore due to decline in the UK. EBITDA grew 3% YoY to ₹ 2077 crore and margins declined 326 bps to 27.7% surpassing marginal 42 bps decline in GPM (70.6%) mainly due to significant jump in SG&A expenses (up 22%) on account of costs related to NRT business acquisition, impairment of Hallette besides higher R&D spend (up 120 bps to 9.1).
- US launches, in-licensing deals, acquisitions to determine the growth path The growth across geographies was mainly driven by new launches, a strategy spelled out by the management few years ago that the company will keep the launch momentum simultaneously across global markets. The management has guided for 20 launches in the next two years in the US, many of which will be complex launches. 50% of the new launches would be from Peptides / Injectables / Oncology / Biosimilars category and the idea is to fill the possible void after the complete genericization of gRevlimid. India growth was mainly on account of acquisition of Sanofi vaccines portfolio (ex of which the growth was 9-10%). The management expects double digit growth excluding acquisitions. R&D is expected to be around ~8.5-9% of the revenues with ~36% earmarked for biosimilars and innovative arm Aurigene. For GLP-1 opportunities globally, the company is targeting entire value chain starting from API manufacturing. Overall, we believe DRL's capability of complex launches on a consistent basis across geographies to be the key determinant for overall performance. Recent acquisition of Nicotine Replacement Therapy brands, launch drug-free migraine device in Europe and JV with Nestle for nutraceuticals are some unique deals the success of which would be keenly watched for. Also in focus would be the margins trajectory especially in post Revlimid era.

Rating and Target price

- Our target price is ₹ 1570 based on 20x FY26E EPS of 78.5.

Key Financial Summary

Key Financials (₹ crore)	FY20	FY21	FY22	FY23	3 year CAGR (FY20-23)	FY24	FY25E	FY26E	2 year CAGR (FY24-26E)
Revenues	17517.0	19047.5	21545.2	24669.7	12.1	28011.1	33538.2	36284.5	13.8
EBITDA	2466.0	3869.9	3767.7	6348.9	37.1	7924.7	8630.6	9252.5	8.1
EBITDA Margins (%)	14.1	20.3	17.5	25.7		28.3	25.7	25.5	
Adjusted PAT	2026.0	1951.6	2112.2	4470.2	30.2	5563.2	5921.4	6542.9	8.4
EPS (Adjusted)	24.3	23.4	25.3	53.6		66.7	71.0	78.5	
PE (x)	53.5	54.2	49.7	24.1		19.5	18.3	16.6	
RoE (%)	13.0	11.1	11.0	19.2		19.7	19.3	19.3	
RoCE (%)	9.6	13.1	12.5	23.9		23.0	19.8	20.5	

Source: Company, ICICI Direct Research

Dr.Reddy's

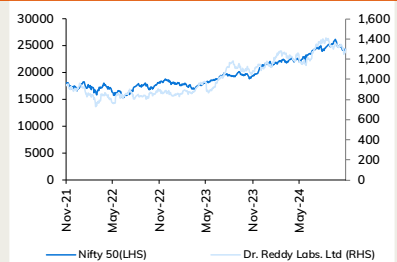
Particulars

Particular	Amount
Market Capitalisation	₹108420 crore
Debt (FY24)	₹2002 crore
Cash & equivalents (FY24)	₹711 crore
EV	₹109711 crore
52 week H/L (₹)	1420/1065
Equity capital	₹83.4 crore
Face value	₹1

Shareholding pattern

(in %)	Dec-23	Mar-24	Jun-24	Sep-24
Promoter	26.7	26.7	26.7	26.6
FIs	28.6	29.1	27.7	27.5
DIs	18.7	18.3	20.7	21.5
Others	26.1	25.9	25.0	24.4

Price Chart



Key risks

- Slower ramp up in new launches especially in the US
- Increasing intangible component on the balance sheet due to licensing deals

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Exhibit 1: Quarterly Summary

₹ Crore	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24	Q3FY24	Q4FY24	Q1FY25	Q2FY25	YoY (%)	QoQ (%)
Total Operating Income	5786.9	5338.3	5474.9	5232.9	6331.8	6789.8	6315.2	6757.9	6902.6	7236.8	7113.8	7696.1	8038.3	16.5	4.4
Raw Material Expenses	2027.6	1814.7	1897.8	1911.3	1847.0	2001.4	1898.1	1937.6	2003.0	2176.0	2092.1	2181.7	2366.7	18.2	8.5
% of Revenues	35.0	34.0	34.7	36.5	29.2	29.5	30.1	28.7	29.0	30.1	29.4	28.3	29.4	42 bps	109 bps
Gross Profit	3759.3	3523.6	3577.1	3321.6	4484.8	4788.4	4417.1	4820.3	4899.6	5060.8	5021.7	5514.4	5671.6	15.8	2.9
Gross Profit Margins (%)	65.0	66.0	65.3	63.5	70.8	70.5	69.9	71.3	71.0	69.9	70.6	71.7	70.6	-42 bps	-109 bps
Employee expenses	1010.4	956.3	972.6	1045.7	1151.7	1173.2	1276.0	1189.7	1280.3	1276.4	1283.6	1413.7	1399.2	9.3	-1.0
% of Revenues	17.5	17.9	17.8	20.0	18.2	17.3	20.2	17.6	18.5	17.6	18.0	18.4	17.4	-114 bps	-96 bps
Other expenses	1389.1	1351.6	2153.5	1334.7	1434.2	1663.3	1607.2	1568.5	1611.0	1761.3	1906.9	1970.3	2195.8	36.3	11.4
% of Revenues	24.0	25.3	39.3	25.5	22.7	24.5	25.4	23.2	23.3	24.3	26.8	25.6	27.3	398 bps	172 bps
Total Expenditure	4427.1	4122.6	5023.9	4291.7	4432.9	4837.9	4781.3	4695.8	4894.3	5213.7	5282.6	5565.7	5961.7	21.8	7.1
% of Revenues	76.5	77.2	91.8	82.0	70.0	71.3	75.7	69.5	70.9	72.0	74.3	72.3	74.2	326 bps	185 bps
EBITDA	1359.8	1215.7	451.0	941.2	1898.9	1951.9	1533.9	2062.1	2008.3	2023.1	1831.2	2130.4	2076.6	3.4	-2.5
EBITDA Margins (%)	23.5	22.8	8.2	18.0	30.0	28.7	24.3	30.5	29.1	28.0	25.7	27.7	25.8	-326 bps	-185 bps
Total Depreciation	294.1	294.2	293.0	301.8	309.2	323.7	315.5	353.3	375.5	373.5	367.7	381.1	397.0	5.7	4.2
Interest	23.4	21.6	31.5	34.7	30.9	41.8	35.4	37.1	35.3	39.4	59.3	59.8	75.7	114.4	26.6
Share of profit/ (loss) of equity accounted investees	0.0	0.0	0.0	0.0	0.0	0.0	-7.6	-4.3	-4.2	-2.7	-3.5	-5.9	-6.1		
Other income	205.5	55.8	121.9	853.9	40.8	58.7	138.5	174.0	315.0	216.2	197.5	187.2	307.4		
EBT	1247.8	955.7	248.4	1458.6	1599.6	1645.1	1329.1	1850.0	1916.7	1829.1	1605.2	1882.6	1917.4	0.0	1.8
Total Tax	276.7	264.9	161.9	279.0	499.4	393.8	369.0	445.0	434.5	448.2	295.4	490.2	575.5	32.5	17.4
Tax %	25.9	28.8	118.2	45.4	31.8	24.9	27.8	24.1	22.7	24.5	18.4	26.0	30.0		
PAT	971.1	690.8	325.6	607.0	1100.2	1251.3	960.1	1405.0	1482.2	1380.9	1309.8	1392.4	1341.9	-9.5	-3.6
No. of Equity Shares	83.4	83.4	83.4	83.4	83.4	83.4	83.4	83.4	83.4	83.4	83.4	83.4	83.4		
EPS (Diluted)	11.9	8.5	1.2	14.3	13.4	15.1	11.5	16.8	17.8	16.6	15.7	16.7	16.1		

Q2FY25 Results / Conference call highlights

US Business –

- DRL launched four products this quarter and expects a total of 15-20 launches by year-end. The High-value launches with limited competition in the US are anticipated later in FY26.
- The in-licensed biosimilar Abatacept is expected to be launched in early FY27.
- DRL’s subsidiary Aurigene Oncology reported positive results for its CAR-T cell therapy Phase 1 study. The company received European Commission authorization for a biosimilar of Rituximab, with European launch expected in February 2025 and U.S. launch anticipated in FY26 upon regulatory approval.
- The U.S. FDA classified three DRL facilities as VAI, ensuring compliance and supporting future product approvals.
- gRevlimid (lenalidomide) Sales are expected to remain healthy through the second half of FY25, with continued demand anticipated into FY26.

Domestic Business –

- Double-digit growth in India at 18% was driven by new launches and additional revenues from the licensed Sanofi vaccine portfolio. The additional brand introduction is expected to sustain double-digit growth in India.
- Company has entered into a non-exclusive patent licensing agreement with Takeda to commercialise Vonoprazan (novel gastrointestinal drug) in India.

Other Geographies –

- For Russia, the management anticipates high double-digit growth due to market share expansion and limited peer investment in the region.
- The management expects the European generics growth to continue with a focus on new product introductions across the region, especially through biosimilar launches like Rituximab
- DRL completed the acquisition of a portfolio in the Nicotine Replacement Therapy (NRT) category from Haleon UK for an upfront cash payment of GBP 458 million and expects market penetration to scale in key geographies over the next 12-14 months.

- Intangibles pertaining to acquisition of the NRT portfolio shall be amortised over 22–23 years.

Other aspects–

- Going forward DRL's Key focus will be GLP-1 products and is also investing in setting up additional capacities for APIs of GLP1 products.
- R&D spending has increased to 9.1% of sales, focusing on complex generics, with guidance for FY25 at 8.5%-9%.
- The management is prioritizing high-value, limited-competition launches across generics, biologics, and oncology. Approximately 36% of R&D spending is focused on biologics and oncology, with the remaining primarily for generics and APIs.
- Growth in SG&A was driven by investments in new business initiatives, one-time costs related to acquisitions, and increased freight costs. These are expected to be in the range of 27.5%-28% of revenue for the fiscal year.
- DRL entered a voluntary license agreement with Gilead Sciences for an HIV treatment (Lenacapavir), aiming to expand its portfolio in over 120 countries.
- Effective tax rate is likely to be ~25% for FY25
- The company has impaired the entire carrying value of Hallette (gNuvaring intangible).
- Company to infuse up to ₹ 600 crore in its step-down wholly-owned subsidiary in Russia for working capital requirements.
- 50-60% capex for APIs will be earmarked for GLP-1 projects.

Financial Tables

Exhibit 3: Profit and loss statement				₹ crore
(Year-end March)	FY23	FY24	FY25E	FY26E
Revenues	24,669.7	28,011.1	33,538.2	36,284.5
Growth (%)	14.5	13.5	19.7	8.2
Raw Material Expenses	7,657.8	8,208.7	10,023.7	10,885.3
Employee expenses	4,646.6	5,030.0	6,088.8	6,712.6
Other expenses	6,016.4	6,847.7	8,795.1	9,434.0
Total Operating Expenditure	18,320.8	20,086.4	24,907.6	27,031.9
EBITDA	6,348.9	7,924.7	8,630.6	9,252.5
Growth (%)	68.5	24.8	8.9	7.2
Interest	142.8	171.1	286.9	217.7
Depreciation	1,250.2	1,470.0	1,572.1	1,637.3
PBT before Exceptional Item	6,011.4	7,186.3	7,942.7	8,776.3
Share of profit/ (loss) of equity	-37.0	0.0	0.0	0.0
PBT	6,048.4	7,186.3	7,942.7	8,776.3
Total Tax	1,541.2	1,623.1	2,021.3	2,233.4
PAT	4,507.2	5,563.2	5,921.4	6,542.9
Adjusted PAT	4,470.2	5,563.2	5,921.4	6,542.9
Growth (%)	111.6	24.5	6.4	10.5
EPS	54.0	66.7	71.0	78.5
EPS (Adjusted)	53.6	66.7	71.0	78.5

Source: Company, ICICI Direct Research

Exhibit 4: Cash flow statement				₹ crore
(Year-end March)	FY23	FY24	FY25E	FY26E
Profit/(Loss) after taxation	4,977.1	5,196.3	5,921.4	6,542.9
Add: Depreciation & Amortization	1,250.2	1,470.0	1,572.1	1,637.3
Net Increase in Current Assets	-840.6	-2,649.9	-1,054.1	-2,612.2
Net Increase in Current Liabilities	55.1	631.7	617.7	640.3
CF from operating activities	5,887.3	4,543.3	7,344.0	6,426.1
(Inc)/dec in Fixed Assets	-1,878.2	-2,637.1	-8,067.6	-1,820.0
(Inc)/dec in Investments	-2,336.6	-1,570.4	1,267.9	-780.0
Others	77.6	179.2	618.1	-11.0
CF from investing activities	-4,137.2	-4,028.3	-6,181.6	-2,611.0
Inc / (Dec) in Equity Capital	36.8	80.5	0.0	0.0
Inc / (Dec) in Loan	-2,039.7	434.6	2,852.1	-500.0
Dividend & Dividend Tax	-497.9	-664.8	-3,336.0	-3,336.0
Others	-185.3	-226.6	-286.9	-217.7
CF from financing activities	-2,686.1	-376.3	-770.8	-4,053.7
Net Cash flow	-907.3	132.8	422.3	-238.7
Opening Cash	1,485.2	577.9	710.7	1,133.0
Closing Cash	577.9	710.7	1,133.0	894.4
Free Cash Flow	4,009.1	1,906.2	-723.6	4,606.1
FCF Yield	3.7%	1.8%	-0.7%	4.2%

Source: Company, ICICI Direct Research

Exhibit 5: Balance Sheet				₹ crore
(Year-end March)	FY23	FY24	FY25E	FY26E
Equity Capital	83.3	83.4	83.4	83.4
Net Network	23,202.8	28,171.4	31,059.2	33,872.8
Total Shareholders fund	23,286.1	28,254.8	31,142.6	34,349.5
Total Debt	1,347.2	2,002.0	4,854.1	4,354.1
Deferred Tax Liability	76.0	84.1	1,376.2	1,431.2
Other Non Current Liabilities	203.2	314.0	519.1	539.9
Long term Provisions	19.9	23.9	34.1	35.4
Source of Funds	24,932	30,679	37,926	40,710
Gross Block - Fixed Assets	21,586.4	24,260.2	31,826.5	33,146.5
Accumulated Depreciation	12,914.7	14,384.7	15,956.8	17,594.1
Net Block	8,671.7	9,875.5	15,869.7	15,552.4
Capital WIP	1,030.1	1,419.3	1,920.6	2,420.6
Net Fixed Assets	9,701.8	11,294.8	17,790.3	17,973.0
Goodwill	547.4	550.1	1,315.9	1,315.9
Investments	4,985.8	4,930.5	3,662.6	4,442.6
Inventory	4,867.0	6,355.2	7,203.9	7,157.5
Cash	577.9	710.7	1,133.0	894.4
Debtors	7,248.5	8,029.8	8,439.8	10,935.0
Loans & Advances & Other	2,130.2	4,287.6	4,083.0	4,246.3
Total Current Assets	15,975.9	20,400.3	21,755.1	24,128.6
Creditors	2,268.4	2,614.4	3,020.6	3,429.6
Provisions & Other CL	5,084.3	5,570.6	5,782.1	6,013.4
Total Current Liabilities	7,352.7	8,185.0	8,802.7	9,443.0
Net Current Assets	8,623.2	12,215.3	12,952.4	14,685.6
LT L&A, Other Assets	369.0	630.3	475.0	494.0
Deferred Tax Assets	705.2	1,057.8	1,729.5	1,798.7
Application of Funds	24,932	30,679	37,926	40,710

Source: Company, ICICI Direct Research

Exhibit 6: Key ratios				₹ crore
(Year-end March)	FY23	FY24	FY25E	FY26E
Per share data (₹)				
EPS	53.6	66.7	71.0	78.5
BV per share	279.2	338.8	368.7	407.1
Operating Ratios (%)				
Gross Profit Margins	69.0	70.7	70.1	70.0
EBITDA margins	25.7	28.3	25.7	25.5
Net Profit margins	18.1	19.9	17.7	18.0
Inventory days	232.0	282.6	262.3	240.0
Debtor days	107.2	104.6	91.9	110.0
Creditor days	108.1	116.2	110.0	115.0
Asset Turnover	1.1	1.2	1.1	1.1
EBITDA conversion Rate	92.7	57.3	85.1	69.5
Return Ratios (%)				
RoE	19.2	19.7	19.3	19.3
RoCE	23.9	23.0	19.8	20.4
RoIC	32.6	31.5	26.2	26.7
Valuation Ratios (x)				
P/E	24.1	19.5	18.3	16.6
EV / EBITDA	2.8	2.3	2.6	16.6
EV / Revenues	0.7	0.7	0.7	0.6
Market Cap / Revenues	0.9	0.8	0.6	0.6
Price to Book Value	4.7	3.8	3.5	3.2
Solvency Ratios				
Debt / Equity	0.1	0.1	0.2	0.1
Debt / EBITDA	0.2	0.3	0.6	0.5
Current Ratio	1.9	2.3	2.2	2.4
Quick Ratio	1.3	1.5	1.4	1.6
Working Capital Cycle	231.1	271.0	244.2	235.0

Source: Company, ICICI Direct Research

ANALYST CERTIFICATION

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