

October 30, 2023

RESULT REPORT Q2 FY24 | Sector: Pharmaceuticals & Healthcare

Dr Reddys'

Triggers & headwinds cancel out

Result Synopsis

Dr Reddys' management alluded to few growth drivers in H2 and FY25 namely 1) acceleration to double digit growth by Q4 exit in India followed by improved outlook next fiscal on back of in-licensing deals and 2) ramp up in acquired Mayne Pharma products like Nuvaring. Albeit two opposing forces – Revlimid peak and higher R&D in H2 may offset some of these triggers leaving margin in the same ballpark as what has been delivered in H1 FY24. Indeed, next fiscal reckon DRL could be looking at lower OPM as peak Revlimid sales and associated margin would be behind and unlikely to be offset by any such large product. What we had outlined 1-2 quarters back about all eyes on traction in ex-Revlimid growth still remains relevant where we do not notice any incremental change; ramp up of material launches as outlined in call amidst a benign pricing environment is key to better growth in US though we note nothing is likely to accrue at least over next 6-12 months. Biosimilars and China scale up also appear to be longer term triggers leaving no change to our Neutral stance on the stock with unchanged estimates, multiple and TP Rs5,580.

Result Highlights

- A largely in-line growth of 2% QoQ driven by ex-US markets
- US business flat QoQ vs expectation of modest growth; YoY growth of 13% on account of Mayne integration and FX tailwind
- Domestic business weak at +3% YoY due to now well-known muted acute season specifically gastro in our view; excluding NLEM impact, growth in mid-single digit YoY
- Russia sales down 3% YoY on currency devaluation sans which underlying growth of 4% YoY; overall EM growth tepid due to Russia impact YoY
- Europe up 26% YoY on favourable forex and contribution of new products
- Margin at 29% lower than our estimate of 31% on back of flat US business QoQ coupled with higher R&D
- Other income included Rs984mn from settlement of product litigation in UK; margin would have been lower but for Rs1.6bn in PLI grant in Q2 and Rs2.3bn in H1

Exhibit 1: Actual vs estimates

Rsmn	Actual	Estimate		% Variation		Remarks
		YES Sec	Consensus	YES Sec	Consensus	
Sales	69,026	68,425	68,993	0.9	0.0	In-line Q with tad weaker margin on tepid US performance QoQ
EBITDA	20,138	21,197	18,655	-5.0	7.9	
EBITDA Margin (%)	29.2	31.0	27.0	-180 bps	214 bps	
Adjusted PAT	14,877	14,252	12,673	4.4	17.4	

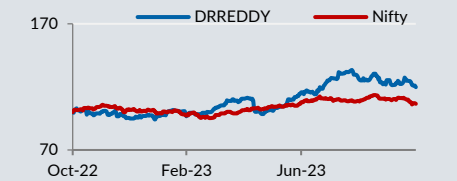
Source: Company, YES Sec

Reco	: NEUTRAL
CMP	: Rs 5,339
Target Price	: Rs 5,580
Potential Return	: +4.5%

Stock data (as on October 27, 2023)

Nifty	18,959
52 Week h/l (Rs)	5990 / 4175
Market cap (Rs/USD mn)	898322 / 10789
Outstanding Shares (mn)	166
6m Avg t/o (Rs mn):	2,124
Div yield (%):	0.7
Bloomberg code:	DRRD IN
NSE code:	DRREDDY

Stock performance



	1M	3M	1Y
Absolute return	-4.4%	-4.4%	19.7%

Shareholding pattern (As of Sep '23 end)

Promoter	26.7%
FII+DII	63.3%
Others	9.9%

Δ in stance

(1-Yr)	New	Old
Rating	NEUTRAL	NEUTRAL
Target Price	5,580	5,580

Δ in earnings estimates

	FY24e	FY25e
EPS (New)	326.7	292.9
EPS (Old)	321.0	293.7
% change	1.8%	-0.3%

Financial Summary

(Rs mn)	FY23	FY24E	FY25E
Revenue	246,697	271,634	278,412
YoY Growth	14.5	10.1	2.5
EBIDTA	64,189	79,687	74,651
YoY Growth	36.6	24.1	-6.3
PAT	45,073	54,234	48,627
YoY Growth	106.5	20.3	(10.3)
ROE	21.4	21.0	16.0
EPS	270.5	326.7	292.9
P/E	19.7	16.3	18.2
BV	1397.7	1689.5	1942.4
EV/EBITDA	12.9	9.9	10.1

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Exhibit 2: Quarterly snapshot (Consolidated)

Rs mn	Q1 FY23	Q2 FY23	Q3 FY23	Q4 FY23	Q1 FY24	y/y (%)	q/q (%)
Revenue	63,318	67,898	63,152	67,579	69,026	9.0	2.1
Expenditure	44,304	48,379	47,273	46,947	48,888	10.3	4.1
- RM	10,381	10,854	11,314	10,605	8,652	(16.7)	(18.4)
- Purchase of goods	8,089	9,160	7,667	8,771	11,378	40.7	29.7
- Staff Cost	11,517	11,732	12,760	11,897	12,803	11.2	7.6
- Other exp	14,317	16,633	15,532	15,674	16,055	12.1	2.4
Operating Profit	19,014	19,519	15,879	20,632	20,138	5.9	(2.4)
OPM(%)	30.0	28.7	25.1	30.5	29.2	-85 bps	-136 bps
Other Income	408	587	1,385	1,740	3,150	672	81
Depreciation	3,092	3,237	3,155	3,533	3,755	21	6
Interest	309	418	354	371	353	14	(5)
PBT	16,021	16,451	13,755	18,468	19,180	19.7	3.9
Tax	4,994	3,938	3,690	4,450	4,345	(13.0)	(2.4)
PAT	11,027	12,513	10,065	14,018	14,835	34.5	5.8
Exceptional	25	134	540	11	55	-	-
Minority Int	(140)	(60)	(76)	(43)	(42)	(70.0)	(2.3)
Reported PAT	11,142	12,439	9,601	14,050	14,822	33.0	5.5

Source: Company, YES Sec

KEY CON-CALL HIGHLIGHTS

- Expect PSAI sales to improve in next 2 quarters on back of imported volumes
- In-licensing is the most important focus for India along with performance of core portfolio
- Targeting cardiac, CNS and oncology in domestic therapies where there is unmet need
- Do not see decline in API prices unlike previous years. What is seen is the impact of new portfolio vs old portfolio earlier
- Price erosion - affected certain products but moderate compared to earlier years. Shortages persist in US market
- Most of US growth came from main portfolio and new launches. On track for 25 launches in current year. About 25-30 material launches in 3 years with at least single digit USD mn sales
- R&D spending range may be higher than what it is today
- Believe Mayne portfolio products could see growth in H2 as customers launch RFPs
- Domestic business - takes about 12-18 months since announcement of in-licensing a year ago and also in some cases may require clinical trials
- Not a big investment on consumer platform
- At the end of year should see double digit growth and then continue in quarters afterwards. Going after products that can be Rs1bn each and 10 such products for in-licensing
- Not looking at any transformative deals in India. 2x debt/ebidta is the limit beyond which may not venture
- Payouts are good in in-licensing as not much of down payment involved and also have good margin
- Chronic is 35% of India business. Total MR strength of 6000.
- SG&A - investments on brands, digital key reason behind the rise. See at 28-29% of sales range for FY24
- PLI incentives to be marginally higher than last year. Expect to be meaningful in next several quarters
- Rituximab - got pre approval inspection and should be able to launch by partner in early FY25 in US
- Main ramp up in biosimilars from FY27 which would require sales force. To launch 5 biosimilars in 2 years
- Europe - new launches and volume growth in base business. Participation in more injectable tenders also a driver
- China market - total 6 approvals so far. Filing 15 products and most of filings are amongst first wave of launches. To start contribution next fiscal
- ETR lower due to adoption of lower tax regime and expected ETR is 24-25%

FINANCIALS

Exhibit 3: Balance Sheet

Y/e 31 Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E
Equity capital	832	832	833	830	830
Reserves	175,585	191,292	232,028	279,622	321,610
Net worth	176,417	192,124	232,861	280,452	322,440
Debt	8,424	7,673	3,509	3,509	3,509
Deferred tax liab (net)	289	14	760	760	760
Total liabilities	185,130	199,811	237,130	284,721	326,709
Fixed Asset	97,708	94,150	102,492	101,248	101,866
Investments	12,271	12,727	9,052	9,052	9,052
Net Working Capital	64,465	80,164	118,534	167,369	208,739
Inventories	45,412	50,884	48,670	53,590	54,927
Sundry debtors	49,641	66,764	72,485	79,812	81,803
Cash	34,573	44,364	61,852	99,542	138,940
Other current assets	15,877	15,810	21,302	23,089	23,665
Sundry creditors	(18,109)	(22,662)	(22,738)	(25,036)	(25,661)
Other CL	(62,929)	(74,996)	(63,037)	(63,627)	(64,935)
Misc exp	10,686	12,770	7,052	7,052	7,052
Total Assets	185,130	199,811	237,130	284,721	326,709

Source: Company, YES Sec

Exhibit 4: Income statement

Y/e 31 Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E
Revenue	190,475	215,452	246,697	271,634	278,412
Operating profit	45,467	46,981	64,189	79,687	74,651
Depreciation	(12,288)	(11,652)	(12,502)	(13,942)	(15,382)
Interest expense	(970)	(958)	(1,428)	(1,426)	(1,426)
Other income	2,914	4,844	10,555	7,500	6,500
Profit before tax	35,123	39,215	60,814	71,819	64,343
Taxes	(9,319)	(8,789)	(15,412)	(17,955)	(16,086)
Adj. profit	25,804	30,426	45,402	53,864	48,257
Exceptional items	(6,768)	(9,304)	(699)	0	0
Associate share	480	703	370	370	370
Net profit	19,516	21,825	45,073	54,234	48,627

Source: Company, YES Sec

Exhibit 5: Cashflow Statement

Y/e 31 Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E
Profit before tax	35,123	39,215	60,814	71,819	64,343
Depreciation	12,288	11,652	12,502	13,942	15,382
Misc exp w/o	1,513	(2,084)	5,718	-	-
Def tax assets (net)	269	(275)	746	-	-
Tax paid	(9,319)	(8,789)	(15,412)	(17,955)	(16,086)
Working capital Δ	(1,780)	(5,908)	(20,882)	(11,145)	(1,971)
Other operating items	480	703	370	370	370
Operating cashflow	38,574	34,514	43,856	57,031	62,038
Capital expenditure	(26,142)	(8,094)	(20,844)	(12,698)	(16,000)
Free cash flow	12,432	26,420	23,012	44,333	46,038
Equity raised	(2,054)	(10,430)	1,629	(3)	(0)
Investments	(2,062)	(456)	3,675	-	-
Debt financing/disposal	4,320	(751)	(4,164)	-	-
Dividends paid	(4,160)	(4,992)	(6,664)	(6,640)	(6,640)
Net Δ in cash	8,476	9,791	17,488	37,690	39,398

Source: Company, YES Sec

Exhibit 6: Du-pont analysis

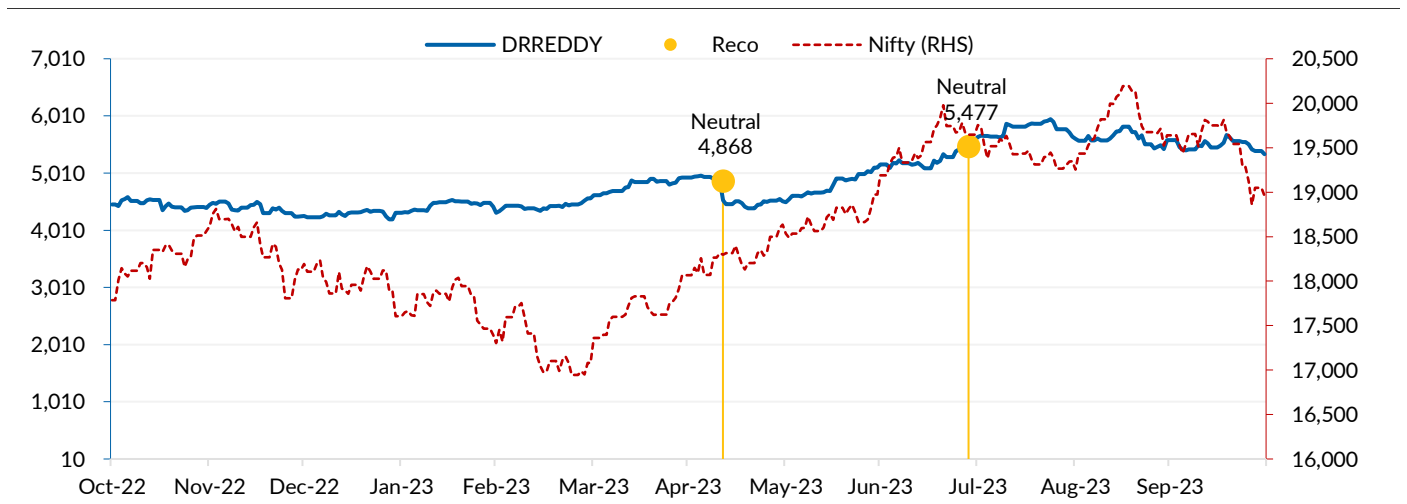
Y/e 31 Mar (Rs mn)	FY21	FY22	FY23	FY24E	FY25E
Tax burden (x)	0.73	0.78	0.75	0.75	0.75
Interest burden (x)	0.97	0.98	0.98	0.98	0.98
EBIT margin (x)	0.19	0.19	0.25	0.27	0.24
Asset turnover (x)	0.80	0.80	0.82	0.80	0.72
Financial leverage (x)	1.43	1.47	1.41	1.33	1.29
RoE (%)	15.5	16.5	21.4	21.0	16.0

Exhibit 7: Ratio analysis

Y/e 31 Mar	FY21	FY22	FY23	FY24E	FY25E
Growth matrix (%)					
Revenue growth	8.7	13.1	14.5	10.1	2.5
Op profit growth	9.6	3.3	36.6	24.1	(6.3)
EBIT growth	0.1	11.3	54.9	17.7	(10.2)
Net profit growth	(3.7)	11.8	106.5	20.3	(10.3)
Profitability ratios (%)					
OPM	23.9	21.8	26.0	29.3	26.8
EBIT margin	18.9	18.6	25.2	27.0	23.6
Net profit margin	13.5	14.1	18.4	19.8	17.3

Y/e 31 Mar	FY21	FY22	FY23	FY24E	FY25E
RoCE	20.9	20.9	28.5	28.1	21.5
RoNW	15.5	16.5	21.4	21.0	16.0
RoA	10.8	11.3	15.1	15.8	12.4
Per share ratios					
EPS	117.3	131.2	270.5	326.7	292.9
Dividend per share	25.0	30.0	40.0	40.0	40.0
Cash EPS	228.9	252.9	347.6	408.5	383.4
Book value per share	1,060.2	1,154.6	1,397.7	1,689.5	1,942.4
Valuation ratios					
P/E	45.5	40.7	19.7	16.3	18.2
P/CEPS	5.0	4.6	3.8	3.2	2.7
P/B	4.7	4.1	3.6	3.3	3.2
EV/EBIDTA	19.0	18.1	12.9	9.9	10.1
Payout (%)					
Dividend payout	26.5	22.4	25.3	25.0	25.0
Tax payout	21.3	22.9	14.8	12.2	13.7
Liquidity ratios					
Debtor days	95	113	107	107	107
Inventory days	87	86	72	72	72
Creditor days	35	38	34	34	34

Recommendation Tracker



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