

Dr Reddys Laboratories | BUY

Strong 1Q; attractively priced

Dr Reddy's reported strong performance, with both topline and EBITDA exceeding our expectations by 5 to 6%. In 1QFY25, Revenue/EBITDA/PAT grew 14%/4%/-1% YoY respectively, driven largely by ramp-up of gRevlimid. Despite higher revenue in the US (USD 463 million, +19% YoY), the EBITDA margin of 27.6% was slightly below expectations due to a significant increase in SG&A expenses – this was led by a sharp rise in freight costs. In other segments, India posted a 15% growth, aided by Sanofi vaccine portfolio. Adjusted for Sanofi vaccines, it grew in mid-single digit. Unlike peers, Dr. Reddy's US pipeline remains relatively opaque to investors. Despite having 23 pending FTF filings and expectations for 25 annual launches, our growth expectations for the US market, excluding Revlimid, appear modest. We believe there could be potential upside here. Additionally, gRevlimid sales estimates are likely to be underestimated as DRRD could have achieved at least USD 150 mn this quarter, reflecting a ~50% QoQ increase. Given this performance, Dr. Reddy's is expected to generate USD 650mn+ in free cash flow annually over the next three years, potentially raising its cash balance to over USD 1.5 bn by FY27. With a focus on earnings-accretive transaction (such as the recent NRT brands acquisition), we see positive potential for core earnings. At CMP, it trades at ~21-22x on FY27 EPS and remains attractive as compared to large-cap peers. Therefore, we maintain a BUY rating on the stock, valuing it based on core EPS and Rs 628 Revlimid NPV, with a target price of Rs 8,010.

- **US delivers stellar performance:** US business reported stellar sales of INR 38.5bn (13% beat) growing 20% YoY and 18% QoQ. The improvement was largely on account of increase in volumes, contribution from new launches, partly offset by price erosion. During the quarter, the company launched 3 new products and filed one new ANDA with the U.S. FDA. As of June 30, 2024, 80 generic filings were approvals pending from the U.S. FDA in the U.S.
- **Nicotinell acquisition from Haleon:** DRRD acquired Haleon's global Nicotine Replacement Therapy ('NRT') OTC brands for GBP 500mn (2.3x sales) of which GBP 42mn is contingent consideration payable in CY25/26. This acquisition will help leverage customer relationships and give an opportunity to cross-sell. The acquisition alleviates concerns around managing gRevlimid cliff. Recent initiatives like Nestle JV, biosimilars, innovation, licensing deals, etc. pinpoint towards DRRD's focus on growing its new businesses. With domestic growth catching up with market growth and Haleon brand acquisitions enhancing ex-Revlimid EPS, we believe there is an opportunity to unlock value here. We highlighted additional details about this acquisition in our [recent note](#).
- **Vaccine portfolio helps drive India beat:** Domestic sales grew 15%YoY (5% beat) to INR 13.3bn. Growth was supported by the Sanofi vaccine portfolio, adjusted for the acquisition, it grew in mid-single digit. This is in line with management's guidance of IPM outperformance. We believe India business will continue to deliver IPM-beating growth over the next few years (~12% CAGR). The company launched 13 new brands in the country, in addition to exclusive rights to promote and distribute Sanofi's vaccine brands.



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Recommendation and Price Target

Current Reco.	BUY
Previous Reco.	BUY
Current Price Target (12M)	8,010
Upside/(Downside)	16.4%
Previous Price Target	7,390
Change	8.4%

Key Data – DRRD IN

Current Market Price	INR6,879
Market cap (bn)	INR1,147.5/US\$13.7
Free Float	67%
Shares in issue (mn)	166.5
Diluted share (mn)	166.5
3-mon avg daily val (mn)	INR3,253.2/US\$38.9
52-week range	6,966/5,206
Sensex/Nifty	81,333/24,835
INR/US\$	83.7

Price Performance

%	1M	6M	12M
Absolute	7.4	17.5	23.2
Relative*	4.4	3.9	0.2

* To the BSE Sensex

Financial Summary					(INR mn)
Y/E March	FY23A	FY24A	FY25E	FY26E	FY27E
Net Sales	245,879	279,164	312,326	353,491	338,375
Sales Growth (%)	14.7	13.5	11.9	13.2	-4.3
EBITDA	70,479	82,587	88,076	98,977	80,195
EBITDA Margin (%)	28.7	29.6	28.2	28.0	23.7
Adjusted Net Profit	35,348	33,371	33,988	45,366	53,009
Diluted EPS (INR)	212.3	200.5	204.2	272.5	318.4
Diluted EPS Growth (%)	18.7	-5.6	1.9	33.5	16.8
ROIC (%)	20.0	23.6	24.2	26.6	19.9
ROE (%)	16.8	13.0	11.1	12.5	12.7
P/E (x)	32.4	34.3	33.7	25.2	21.6
P/B (x)	5.0	4.1	3.4	2.9	2.6
EV/EBITDA (x)	16.1	13.2	11.8	10.0	11.7
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0

Source: Company data, JM Financial. Note: Valuations as of 26/Jul/2024

JM Financial Institutional Securities Limited

JM Financial Research is also available on:
Bloomberg - JMFR <GO>,
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S&P Capital IQ, FactSet and Visible Alpha

Please see Appendix I at the end of this report for Important Disclosures and Disclaimers and Research Analyst Certification.

- **Russia growth weak due to forex impact:** EM revenue grew of 3% YoY/ -2% QoQ to INR 11.9bn with Russia revenues declining 2% YoY majorly due to unfavorable currency exchange rate movements, partially offset by price increases and higher base business volumes. Revenue from RoW territories grew 11% YoY largely attributable to increase in volumes of base business, contribution from new products, partly offset by price erosion. Europe grew 4% YoY (9% miss) to INR 5.3bn. PSAl gross margin came in at 23.1% (vs. 15%YoY; 28.6%QoQ)with revenue increasing 14%YoY /-7%QoQ (9% beat) to INR 7.7bn with YoY growth driven by improved volumes in base business, and contribution from new products.
- **Biosimilars:** The biosimilars opportunity is going to be meaningful from 2027. The management guided for Denosumab launch in next year and Abatacept launch likely by early CY27 (filing by end CY25). The company is investing in their Bachupally facility and are increasing capacity to 50kl (currently 15kl) within the next two years.
- **Key financials:**
 - Revenue/EBITDA/APAT of INR 76.7bn/21.2bn/13.9bn grew +14%/+4%/-1% YoY respectively and were +6%/+5%/+1% vs. our expectations and +5%/+6%/+6% vs. Street expectations.
 - Gross margin was 60% (vs. 59% YoY; vs. 59% QoQ) due to better product mix.
 - EBITDA margin declined to 27.6% vs. 30.3% YoY/25.2% QoQ (JMFe: 27.9%).
 - Capex for the quarter was INR 4.9bn while FCF was INR 2.3bn.
 - The R&D expenses were at 8.1% of sales
 - Net cash surplus as of 30th Jun'24 was INR 67.3bn. This cash surplus will be used to drive inorganic growth to achieve short-term and long-term objectives.
 - ETR guidance remains 24-25%.

Exhibit 1. 1QFY25 review

Dr. (INR mn)	Reddy's	P&L	1QFY24A	1QFY25A	% YoY	1QFY25E	% Delta vs JMFe	1QFY25E (cons.)	% Delta vs cons	4QFY24A	% QoQ
Net Sales			67,384	76,727	14%	72,606	6%	72,780	5%	70,830	8%
Cost of goods sold			27,831	30,383	9%	30,131	1%			29,347	4%
Gross Profit			39,553	46,344	17%	42,474				41,483	
% Margin			59%	60%	170 bps	59%				59%	
SG&A (excl. amort)			16,400	21,389	30%	18,514	16%			19,185	11%
Amortization			1,302	1,302	0%	1,350	-4%			1,291	1%
R&D			4,984	6,193	24%	6,171	0%			6,877	-10%
Impairment charges			11	5		0				-173	
EBITDA*			20450	21212	4%	20238	5%			17842	
% Margin			30.3%	27.6%		27.9%				25.2%	
Adjusted EBITDA**			20450	21212	4%	20238	5%	19,930	6%	17842	19%
% Margin			30.3%	27.6%	-270 bps	27.9%	-23 bps	27.4%	26 bps	25.2%	246 bps
D&A			2,281	2,450	7%	2,450	0%			2,421	1%
Op. Income			16,867	17460	4%	16,438	6%			14,130	24%
% Margin			25.0%	22.8%	-228 bps	22.6%	12 bps			19.9%	281 bps
Equity in affiliates			43	59	37%	46				35	69%
Other Income/(Expenses)			780	470	-40%	700				656	-28%
Net Finance Expense/(Income)			(784)	(837)		(900)				(1022)	
Profit Before Tax			18463	18821	2%	18084				16016	18%
Tax			4438	4901		4340				2946	
Adj. Net Profit			14025	13,920	-1%	13744	1%	13,170	6%	13070	7%
Adj. EPS			84.5	83.9		82.8				78.8	
% Cost Ratios			1QFY24A	1QFY25A	% YoY	1QFY25E	% Delta vs JMFe	1QFY25E (cons.)	% Delta vs cons	4QFY24A	% QoQ
COGS			41.3	39.6	-170 bps	41.5	-190 bps			41.4	-183 bps
SG&A			24.3	27.9	354 bps	25.5	238 bps			27.1	79 bps
R&D			7.4	8.1	68 bps	8.5	-43 bps			9.7	-164 bps
Sales Break-up			1QFY24A	1QFY25A	% YoY	1QFY25E	% Delta vs JMFe	1QFY25E (cons.)	% Delta vs cons	4QFY24A	% QoQ
Global Generics			60,083	68,857	15%	64,880	6%	66,230	4%	61,190	13%
North America			32,002	38,462	20%	34,160	13%			32,626	18%
Europe			5,047	5,265	4%	5,771	-9%			5,208	1%
India			11,482	13,252	15%	12,630	5%			11,265	18%
Russia & CIS			7,600	7,400	-3%	7,893	-6%			7,200	3%
Others			3,952	4,478	13%	4,426	1%			4,891	-8%
PSAI			6,709	7,657	14%	7,044	9%			8,219	-7%
Prop products and Others			592	212	-64%	681	-69%			1,420	-85%

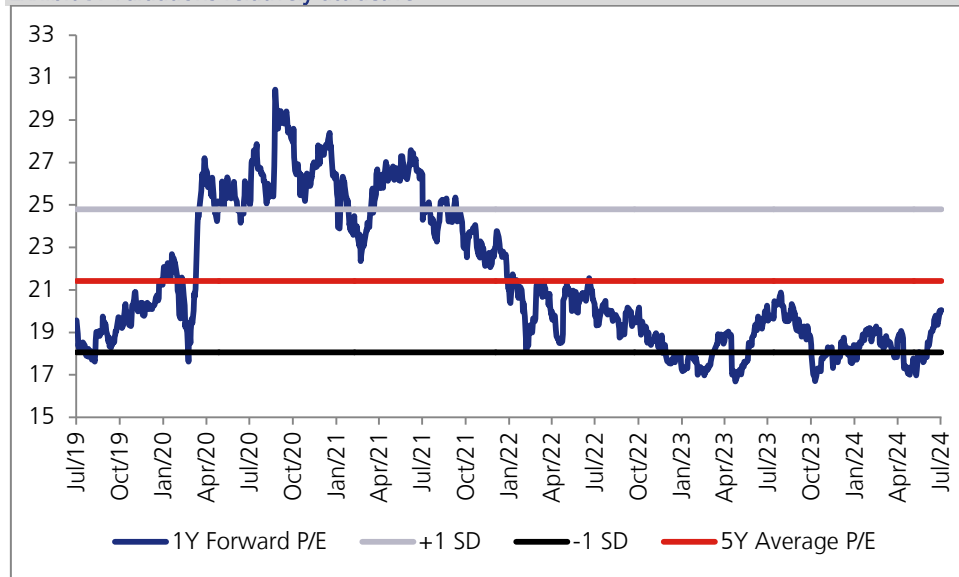
Source: Company, Bloomberg, JM Financial

Exhibit 2. Recent initiatives

Date	Notable events in Specialty/Specialty generics
Jan-24	Launched inhouse PRIMCYV (Breast Cancer Drug taken from Pfizer) in India
Feb-24	Acquired Mayne Pharma US generic portfolio
Jun-24	Completed Phase 1 studies of Tocilizumab Biosimilar
Jul-24	Submitted Trastuzumab dossier in US, UK and Europe
Nov-24	Launched Nerivio (US FDA approved Path breaking Migraine treatment) in India
Dec-24	Enters into exclusive agreement for Coya 302 (ALS product)
Jan-24	Announces the acquisition of MenoLabs in US (women healthcare & Nutra)
Jan-24	Forayed into the consumer health market of UK with the launch of allergy medication, Histallay
Mar-24	Launches Versavo (Bevacizumab biosimilar) in UK
Mar-24	In licensed first in class Cethaquine for Hypovolemic shock in India
Mar-24	Exclusive distribution partnership for Sanofi's Vaccines brands in India
Apr-24	Partnered with Bayer to distribute Vericiguat, a heart failure management drug, in India
Apr-24	Launched migraine management wearable device, Nerivio®, in Germany and South Africa
Apr-24	Launched 'DailyBloom IBS' digital integrated care plan to manage Irritable Bowel Syndrome
Apr-24	Announced JV with Nestle for health science nutraceutical portfolio
May-24	Acquired Haleon's global consumer OTC brands for NRT

Source: Company

Exhibit 3. Valuations relatively attractive



Source: Bloomberg, JM Financial

Financial Tables (Consolidated)

Income Statement		(INR mn)				
Y/E March	FY23A	FY24A	FY25E	FY26E	FY27E	
Net Sales	245,879	279,164	312,326	353,491	338,375	
Sales Growth	14.7%	13.5%	11.9%	13.2%	-4.3%	
Other Operating Income	0	0	0	0	0	
Total Revenue	245,879	279,164	312,326	353,491	338,375	
Cost of Goods Sold/Op. Exp	106,536	115,557	125,867	143,164	147,193	
Personnel Cost	0	0	0	0	0	
Other Expenses	68,864	81,020	98,383	111,350	110,987	
EBITDA	70,479	82,587	88,076	98,977	80,195	
EBITDA Margin	28.7%	29.6%	28.2%	28.0%	23.7%	
EBITDA Growth	44.2%	17.2%	6.6%	12.4%	-19.0%	
Depn. & Amort.	13,335	14,858	15,334	15,907	16,411	
EBIT	57,144	67,729	72,742	83,070	63,784	
Other Income	2,853	3,994	3,000	5,500	7,000	
Finance Cost	0	0	334	373	301	
PBT before Excep. & Forex	59,997	71,723	75,408	88,198	70,483	
Excep. & Forex Inc./Loss(-)	0	0	0	0	0	
PBT	59,997	71,723	75,408	88,198	70,483	
Taxes	15,300	16,186	18,892	22,094	17,670	
Extraordinary Inc./Loss(-)	0	0	0	0	0	
Assoc. Profit/Min. Int.(-)	370	147	162	178	196	
Reported Net Profit	45,067	55,684	56,677	66,282	53,009	
Adjusted Net Profit	35,348	33,371	33,988	45,366	53,009	
Net Margin	14.4%	12.0%	10.9%	12.8%	15.7%	
Diluted Share Cap. (mn)	166.5	166.5	166.5	166.5	166.5	
Diluted EPS (INR)	212.3	200.5	204.2	272.5	318.4	
Diluted EPS Growth	18.7%	-5.6%	1.9%	33.5%	16.8%	
Total Dividend + Tax	0	0	0	0	0	
Dividend Per Share (INR)	0.0	0.0	0.0	0.0	0.0	

Source: Company, JM Financial

Cash Flow Statement		(INR mn)				
Y/E March	FY23A	FY24A	FY25E	FY26E	FY27E	
Profit before Tax	60,367	71,870	75,570	88,375	70,679	
Depn. & Amort.	12,636	14,855	15,304	15,907	16,411	
Net Interest Exp. / Inc. (-)	3,846	0	334	373	301	
Inc (-) / Dec in WCcap.	-28,742	-7,416	-6,049	-15,648	134	
Others	0	3	30	0	0	
Taxes Paid	-15,619	-16,545	-19,296	-22,546	-18,175	
Operating Cash Flow	32,489	62,767	65,892	66,461	69,349	
Capex	-7,204	-9,000	-11,000	-11,001	-11,001	
Free Cash Flow	25,285	53,767	54,892	55,460	58,348	
Inc (-) / Dec in Investments	8,529	-2,098	-2,308	-2,539	-2,793	
Others	0	0	0	0	0	
Investing Cash Flow	1,325	-11,098	-13,308	-13,540	-13,794	
Inc / Dec (-) in Capital	0	0	0	0	0	
Dividend + Tax thereon	-4,869	-4,869	-4,869	-5,064	-5,064	
Inc / Dec (-) in Loans	-19,000	-1,804	-1,804	-1,804	-1,804	
Others	-3,527	358	37	79	205	
Financing Cash Flow	-27,396	-6,315	-6,636	-6,789	-6,663	
Inc / Dec (-) in Cash	6,418	45,354	45,948	46,132	48,892	
Opening Cash Balance	14,852	21,270	66,624	112,572	158,704	
Closing Cash Balance	21,270	66,624	112,572	158,704	207,597	

Source: Company, JM Financial

Balance Sheet		(INR mn)				
Y/E March	FY23A	FY24A	FY25E	FY26E	FY27E	
Shareholders' Fund	230,725	281,540	333,348	394,566	442,511	
Share Capital	832	832	832	832	832	
Reserves & Surplus	229,893	280,708	332,516	393,734	441,679	
Preference Share Capital	0	0	0	0	0	
Minority Interest	0	0	0	0	0	
Total Loans	14,845	13,041	11,237	9,433	7,629	
Def. Tax Liab. / Assets (-)	-8,144	-8,144	-8,144	-8,144	-8,144	
Total - Equity & Liab.	237,426	286,437	336,441	395,855	441,996	
Net Fixed Assets	96,392	90,537	86,233	81,327	75,917	
Gross Fixed Assets	149,593	157,593	167,593	177,593	187,593	
Intangible Assets	34,664	35,664	36,664	37,664	38,664	
Less: Depn. & Amort.	92,365	107,220	122,524	138,431	154,842	
Capital WIP	4,500	4,500	4,500	4,501	4,502	
Investments	4,318	4,318	4,318	4,318	4,318	
Current Assets	195,753	255,582	315,481	391,814	443,711	
Inventories	49,539	53,734	58,528	67,287	69,181	
Sundry Debtors	80,225	85,502	89,412	101,197	96,869	
Cash & Bank Balances	21,270	66,624	112,572	158,704	207,597	
Loans & Advances	0	0	0	0	0	
Other Current Assets	44,719	49,723	54,969	64,626	70,064	
Current Liab. & Prov.	59,037	63,998	69,590	81,604	81,949	
Current Liabilities	25,906	27,900	30,179	34,001	34,892	
Provisions & Others	33,130	36,098	39,412	47,603	47,058	
Net Current Assets	136,716	191,584	245,890	310,210	361,761	
Total - Assets	237,426	286,439	336,441	395,855	441,996	

Source: Company, JM Financial

Dupont Analysis		FY23A	FY24A	FY25E	FY26E	FY27E
Net Margin		14.4%	12.0%	10.9%	12.8%	15.7%
Asset Turnover (x)		1.0	1.0	1.0	0.9	0.8
Leverage Factor (x)		1.1	1.1	1.0	1.0	1.0
RoE		16.8%	13.0%	11.1%	12.5%	12.7%

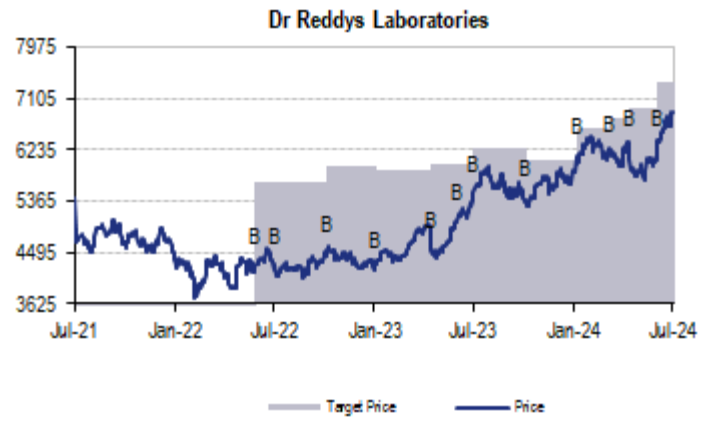
Key Ratios		FY23A	FY24A	FY25E	FY26E	FY27E
BV/Share (INR)		1,386.0	1,691.3	2,002.5	2,370.2	2,658.3
ROIC		20.0%	23.6%	24.2%	26.6%	19.9%
ROE		16.8%	13.0%	11.1%	12.5%	12.7%
Net Debt/Equity (x)		0.0	-0.2	-0.3	-0.4	-0.5
P/E (x)		32.4	34.3	33.7	25.2	21.6
P/B (x)		5.0	4.1	3.4	2.9	2.6
EV/EBITDA (x)		16.1	13.2	11.8	10.0	11.7
EV/Sales (x)		4.6	3.9	3.3	2.8	2.8
Debtor days		119	112	104	104	104
Inventory days		74	70	68	69	75
Creditor days		49	47	45	45	46

Source: Company, JM Financial

History of Recommendation and Target Price

Date	Recommendation	Target Price	% Chg.
22-Jun-22	Buy	5,685	
28-Jul-22	Buy	5,685	0.0
29-Oct-22	Buy	5,960	4.8
26-Jan-23	Buy	5,890	-1.2
11-May-23	Buy	5,980	1.5
25-Jun-23	Buy	5,980	0.0
26-Jul-23	Buy	6,260	4.7
29-Oct-23	Buy	6,055	-3.3
31-Jan-24	Buy	6,585	8.8
31-Mar-24	Buy	6,780	3.0
7-May-24	Buy	6,935	2.3
27-Jun-24	Buy	7,390	6.6

Recommendation History



APPENDIX I

JM Financial Institutional Securities Limited

Corporate Identity Number: U67100MH2017PLC296081

Member of BSE Ltd. and National Stock Exchange of India Ltd.

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Rating	Meaning
Buy	Total expected returns of more than 10% for stocks with market capitalisation in excess of INR 200 billion and REITs* and more than 15% for all other stocks, over the next twelve months. Total expected return includes dividend yields.
Hold	Price expected to move in the range of 10% downside to 10% upside from the current market price for stocks with market capitalisation in excess of INR 200 billion and REITs* and in the range of 10% downside to 15% upside from the current market price for all other stocks, over the next twelve months.
Sell	Price expected to move downwards by more than 10% from the current market price over the next twelve months.

* REITs refers to Real Estate Investment Trusts.

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