

India Research

Dr. Reddys Lab

RESULT REVIEW

 Bloomberg: DRRD IN
 Reuters: REDY.BO

HOLD

Margins move up on back of lower SG&A and R & D

Dr. Reddys Lab's (DRL) revenue, increased by 13.6% YoY to Rs40.2 bn, is higher than our estimates of Rs 38.9bn; primarily due to good growth in Europe and Emerging market business. EBITDA margins grew to 21.2% in-line with our estimates of 21.0% on account of lower SGA and R & D expenses. Net profit increased by 44% to Rs4344mn (higher than our estimate of Rs 4063 mn in Q4FY19).

Muted US and Domestic revenue, good traction in Emerging market: North American revenue has increased by 3.2% YoY to Rs14.9bn (lower than our estimates of Rs 16.4 bn) mainly due to increase in base business market share gains and new product launches. The Russia market grew by 41% YoY on account of better volume uptake. Overall PSAI business has grown by 8.2% YoY to Rs 6765 mn as against our estimate of Rs 6185 mn for the quarter. Proprietary business showed robust growth of 139.1% to Rs 3017 mn for the quarter which includes Rs 1.8 bn due to sale of Derma brands.

Improved margins: EBITDA margins increased from 16.1% to 21.2% for the quarter mainly on account of decrease in SG&A and R& D (9.1%) which more than offset decline in gross margins for the quarter. Net profit increased by 44% YoY to Rs 4344 mn.

Outlook and Valuation: We downgrade our Revenues for FY20E by 1% while we upgrade by 1.2% for FY 21E. We downgrade EBITDAM by 50 bps for FY20E while we maintain our FY21E at 21.8 % mainly on account of higher R & D. We upgrade our EPS estimates for FY20E by 9.5% to Rs 135.8 mainly due to Celegene settlement income being factored in FY20E while we upgrade by 2.1% to Rs 144.9 for FY 21E. We maintain our price target at Rs 3122 based on 21.5x FY21E and maintain our **HOLD** rating on the stock.

Key Financials

RsMn	FY17	FY18	FY19	FY20E	FY21E
Net sales	140,809	142,028	153,851	174,543	195,852
EBITDA	24,950	23,679	33,288	37,349	42,740
Net Profit	12,039	9,806	18,795	22,535	24,051
EPS(Rs)	72.6	59.1	113.2	135.8	144.9
EPS growth (%)	(38.1)	(18.6)	91.7	19.9	6.7
EBITDA margin (%)	17.7	16.7	21.6	21.4	21.8
PER(x)	37.8	46.5	24.2	20.2	18.9
EV/EBITDA (x)	19.6	20.6	14.0	12.2	10.3
P/S (x)	3.2	3.2	3.0	2.6	2.3
RoCE (x)	9.0	8.4	13.1	16.7	16.4
RoE (%)	9.5	7.8	14.1	15.1	14.2

Source: Company, Karvy Stock Broking..... IFRS Consolidated

Recommendation

CMP:	Rs2,745
Target Price:	Rs3,122
Previous Target Price	Rs3122
Upside (%)	13.7%

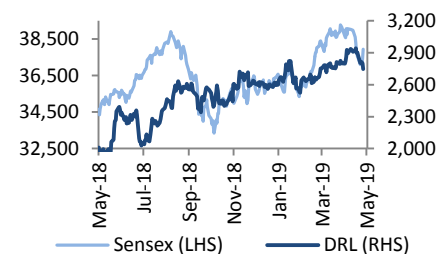
Stock Information

Market Cap. (Rsbn / US\$ mn)	456/6,563
52-week High/Low (Rs)	2,965/1,873
3m ADV (Rsmn /US\$ mn)	2211/32
Beta	0.8
Sensex/ Nifty	37,931/11,407
Share outstanding (mn)	166

Stock Performance (%)

	1M	3M	12M	YTD
Absolute	(1.9)	8.7	38.5	4.9
Rel. to Sensex	1.2	2.5	27.2	0.2

Performance



Source: Bloomberg

Earnings Revision

(%)	FY20E	FY21E
Revenue	↓ 1.0	↑ 1.2
EBITDA	↓ 3.0	↑ 1.2
EPS	↑ 9.5	↑ 2.1

Source: Company, Karvy Stock Broking

Analysts Contact

Rahul Sharma
 022 - 6176 0817
 rahul.sharma@karvy.com

Key Takeaways

During the year company had launched 7 new products including some limited competition products. Propofol injection, Tadalafil and Testosterone Gel were good launches. During the quarter, company filed 10 ANDAs, Dr Reddys has 110 cumulative ANDA filings pending for approval out of which 34 are FTFs and 3 are NDAs. The company plans to launch 30 products in FY 20E in the US markets.

The company has successfully re-launched gSuboxone and divested brands in the Derma space, the same is accounted in Proprietary products business.

Generic Nuvaring: The Company continues to work with US FDA on scheduled launch in the H1CY2019.

Generic Copaxone: The Company received additional queries from the US FDA and is in the process of assessing the requirements and potential timeline. Launch would be deferred to FY21E.

The sterile injectable facility in Duvvada has finally received its EIR from US FDA. This plant is classified as Voluntary Action Initiated (VAI) status.

The company has continued to work towards the resolution of warning letter for API site at Srikakulam facility and is hopeful of positive outcome in the near term.

Cash flow hedges include USD 363 mn at Rs72 – Rs74.4 to a dollar while 1800mn Ruble has been hedged at Rs 1.066 which would be exhumed over the next 12 months.

During the quarter, company launched 6 products in Germany, 4 products in UK and 4 in France; with these launches, company expects to sustain growth in these markets going forward.

Company has realigned its six key areas of business for future growth and made some changes in leadership team for all the six areas. Key priorities include market leadership status, high impact products in proprietary products and key areas.

Company has focused on global cost optimization and divestment of non-core assets.

R & D guidance for FY20 is USD 250 mn – USD 300 mn and Tax rate would be in the range of 20% - 22%.

Exhibit 1: Quarterly Performance

Y/E Mar (Rsmn)	Q4FY19	Q3FY19	Q4FY18	QoQ %	YoY %
Total Revenues	40,166	38,500	35,349	4.3	13.6
Cost of Revenues	19,113	17,748	16,454	7.7	16.2
Gross Profit	21,053	20,752	18,895	1.5	11.4
Total Expenditure	12,525	11,915	13,218	5.1	(5.2)
EBITDA	8,528	8,837	5,677	(3.5)	50.2
EBITDA Margin (%)	21.2	23.0	16.1		
Depreciation	2,136	2,073	2,109	3.0	1.3
Amortization	1,047	1,035	921	1.2	13.7
Finance Income / (expense)	349	(13)	1,032	n/a	(66.2)
Equity Profit / (Loss) in Affiliates	157	89	69	76.4	127.5
Profit before Tax	5,851	5,805	3,748	0.8	56.1
Tax	1,507	953	726	58.1	107.6
Tax rate (%)	25.8	16.4	19.4		
Reported Net Profit	4,344	4,852	3,022	(10.5)	43.7

Source: Company, KarvyStock Broking; n/a - not applicable

Exhibit 2: Actual vs Estimates

Y/E Mar (Rs. mn)	Q4FY19	Q4FY19E	Deviation %
Total Revenues	40,166	38,931	3.2%
EBITDA	8,528	8,160	4.5%
EBITDA Margin (%)	21.2%	21.0%	27bps
Profit before Tax	5,851	5,143	13.8%
Reported Net Profit	4,344	4,063	6.9%

Source: Company, Karvy Stock Broking

Exhibit 3: Change in Estimates

Y/E Mar (Rs. mn)	FY20E			FY21E			Comments
	New	Old	(%) change	New	Old	(%) change	
Domestic business	28,797	29,027	(0.8)	31,677	31,929	(0.8)	marginal downgrade in business
US business	69,600	73,859	(5.8)	78,726	78,723	0.0	lowered US business in FY20 in lieu of Copaxone
EU	8,660	8,783	(1.4)	9,526	9,661	(1.4)	in lieu of lower base
Russia and other markets	32,740	31,984	2.4	37,115	36,283	2.3	upgrade in lieu of higher base
PSAI	26,554	25,916	2.5	29,271	29,271	-	
Revenues	174,543	176,265	(1.0)	195,852	193,456	1.2	
SGA	41,017	42,303	(3.0)	46,025	46,429	(0.9)	lower SGA factored
R & D	18,327	17,626	4.0	19,585	19,346	1.2	higher R & D factored for FY 20 and FY 21
Other expense / (income)	(1,955)	(1,925)	1.6	(1,955)	(1,925)	1.6	
EBITDA	37,349	38,523	(3.0)	42,740	42,271	1.1	
EBITDA margin (in %)	21.4	21.9		21.8	22		
Net Finance Charges/(Income)	(5,577)	(1,844)	202.5	(3,107)	(2,955)	5.1	
Depreciation	8,869	8,852	0.2	9,265	9,248	0.2	
Amortization	4,448	4,435	0.3	4,952	4,939	0.3	
Tax	7,512	6,862	9.5	8,017	7,852	2.1	
Tax Rate (%)	25%	25%		25%	25%		
Net Profit	22,535	20,587	9.5	24,051	23,557	2.1	
EPS (in Rs.)	135.8	124.0	9.5	144.9	141.9	2.1	

Source: Company, KarvyStock Broking

Financials

Exhibit 4: Profit & Loss Statement

Y/E Mar (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Net Revenues	140,809	142,028	153,851	174,543	195,852
% growth	(9.0)	0.9	8.3	13.4	12.2
Cost of revenues (COGS)	62,453	65,724	70,421	79,804	89,456
SGA	34,920	35,148	36,490	41,017	46,025
Research & Development	19,551	18,265	15,607	18,327	19,585
Other expenses/(income)	(1,065)	(788)	(1,955)	(1,955)	(1,955)
EBITDA	24,950	23,679	33,288	37,349	42,740
EBITDA Margin (%)	17.7	16.7	21.6	21.4	21.8
Depreciation	7,593	8,285	8,456	8,869	9,265
AmortisationExps	3,859	3,477	3,944	4,448	4,952
Impairment of Intangibles	0	0	0	0	0
Equity in loss of affiliates	0	344	438	438	438
Net Finance Charges/ (Income)	(806)	(2,080)	(1,117)	(5,577)	(3,107)
Others	(349)	0	0	0	0
Profit before Tax and Minority	14,653	14,341	22,443	30,047	32,068
Tax	2,614	4,535	3,648	7,512	8,017
Effective Tax Rate %	17.8	31.6	16.3	25.0	25.0
Reported Net Profit	12,039	9,806	18,795	22,535	24,051

Source: Company, KarvyStock Broking.....IFRS Consolidated

Exhibit 5: Balance sheet

Y/E Mar (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
Equity	829	830	830	830	830
Net worth	124,044	126,460	140,197	159,273	179,331
Minority Interest	0	0	0	0	0
Short-term Loans	47,616	29,046	14,993	15,959	17,557
Long-term Loans	5,449	25,089	22,000	17,000	10,000
Total Loans	53,065	54,135	36,993	32,959	27,557
Provision (Non Current)	47	53	52	52	52
Deferred Payment Laibilities	1,204	730	610	610	610
Liabilities	178,360	181,378	177,852	192,894	207,549
Net Fixed Assets	60,912	61,814	57,990	61,164	63,899
Intangible Assets	45,131	44,665	44,367	39,919	34,967
Long-term Investments	6,840	4,653	3,342	3,342	3,342
Inventories	28,529	29,089	33,579	38,053	42,656
Debtors	38,065	40,786	39,982	45,359	50,897
Cash and Cash Equivalents	18,136	20,968	24,757	33,185	43,266
Other Current assets	16,628	20,001	17,242	18,928	20,664
Total Current assets	101,358	110,844	115,560	135,526	157,483
Creditors	13,417	16,052	14,553	16,492	18,487
Other current liabilities	28,044	28,174	33,022	34,733	37,823
Total current liabilities	41,461	44,226	47,575	51,225	56,309
Net current assets	59,897	66,618	67,985	84,301	101,174
Deferred Income taxes	5,580	3,628	4,168	4,168	4,168
Total Assets	178,360	181,378	177,852	192,894	207,549

Source: Company, KarvyStock Broking.....IFRS Consolidated

Exhibit 6: Cash Flow Statement

Y/E Mar (Rsmn)	FY17	FY18	FY19	FY20E	FY21E
EBIT	15,949	11,917	20,888	24,032	28,523
Change in working capital	(3,099)	(3,889)	2,422	(7,888)	(6,792)
Cash flow from operations	12,850	8,028	23,310	16,144	21,731
Depreciation and amortization	11,452	11,762	12,400	13,317	14,217
Net Finance Charges/(Income)	(806)	(2,080)	(1,117)	(5,577)	(3,107)
Dividends paid	(3,990)	(3,994)	(3,994)	(3,994)	(3,994)
Tax paid	(2,614)	(4,535)	(3,648)	(7,512)	(8,017)
Deferred payment liabilities	437	(474)	(120)	0	0
Deferred tax asset	(583)	1,952	(540)	0	0
Equity loss in affiliates	(349)	(344)	(438)	(438)	(438)
Other provisions	(8)	6	(1)	0	0
Forex gain/loss	0	0	0	0	0
Impairment of goodwill and amortization	0	0	0	0	0
Net cash from operations	17,993	14,487	28,085	23,095	26,606
Capital Expenditure	(10,792)	(8,994)	(4,675)	(12,043)	(12,000)
Intangibles	(24,129)	466	298	4,448	4,952
Free Cash Flow	(16,928)	5,959	23,708	15,500	19,558
Changes in short term borrowing	20,821	(18,073)	(13,341)	966	1,598
Change in long-term borrowing	(4,320)	19,143	(3,801)	(5,000)	(7,000)
Change in borrowings	16,501	1,070	(17,142)	(4,034)	(5,402)
Change in Investments	(3,543)	2,187	1,311	0	0
Equity issue/buyback	(12,966)	(3,398)	(509)	0	0
Cash from Financial Activities	(8)	(141)	(16,340)	(4,034)	(5,402)
Others	(4,883)	(2,986)	(3,579)	(3,037)	(4,076)
Opening cash	39,955	18,136	20,968	24,757	33,185
Closing cash	18,136	20,968	24,757	33,185	43,266
Change in Cash	-21819	2832	3789	8428	10081

Source: Company, KarvyStock Broking.....IFRS Consolidated

Exhibit 7: Ratios

Y/E Mar	FY17	FY18	FY19	FY20E	FY21E
EV/EBDITA(x)	19.6	20.6	14.0	12.2	10.3
ROE (%)	9.5	7.8	14.1	15.1	14.2
ROCE (%)	9.0	8.4	13.1	16.7	16.4
PE(x)	37.8	46.5	24.2	20.2	18.9
P/BV(x)	3.7	3.6	3.3	2.9	2.5
P/S(x)	3.2	3.2	2.5	2.2	2.0

Source: Company, KarvyStock Broking.....IFRS Consolidated

Stock Ratings		Absolute Returns
Buy	:	> 15%
Hold	:	5-15%
Sell	:	< 5%

For further enquiries please contact:

research@karvy.com

Tel: +91-22-61491500

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Office No. 701, 7th Floor, Hallmark Business Plaza, Opp.-Gurunanak Hospital, Mumbai 400 051
 RegdOff :Plot No.31, 6th Floor, Karvy Millennium Towers, Financial District, Nanakramguda, Hyderabad, 500 032, India
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