

Dr Reddy's Labs

BSE SENSEX

35,622

S&P CNX

10,818

CMP: INR2,351 TP: INR2,275 (-3%)
Neutral

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Bloomberg	DRRD IN
Equity Shares (m)	165.8
M.Cap.(INR b)/(USD b)	389.8 / 5.7
52-Week Range (INR)	2788 / 1888
1, 6, 12 Rel. Per (%)	17/-7/-28
Avg Val, (INR m)	1535.0
Free float (%)	73.2

Financials & Valuations (INR b)

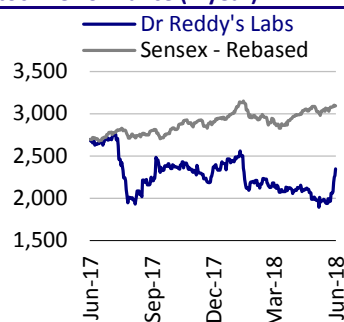
Y/E Mar	2018	2019E	2020E
Sales	142.0	166.6	190.6
EBITDA	22.9	36.3	43.3
Net Profit	10.7	17.1	20.9
Adj. EPS (INR)	64.7	102.9	125.7
EPS Gr. (%)	-10.9	59.1	22.1
BV/Sh. (INR)	757	864	972
RoE (%)	8.6	12.7	13.7
RoCE (%)	4.8	9.4	10.4
P/E (x)	36.4	22.8	18.7
P/BV (x)	3.1	2.7	2.4

Shareholding pattern (%)

As On	Mar-18	Dec-17	Mar-17
Promoter	26.8	26.8	26.8
DII	14.8	15.4	10.6
FII	30.3	29.3	32.4
Others	28.2	28.6	30.3

FII Includes depository receipts

Stock Performance (1-year)



Receives approval for gSuboxone; impact already priced in

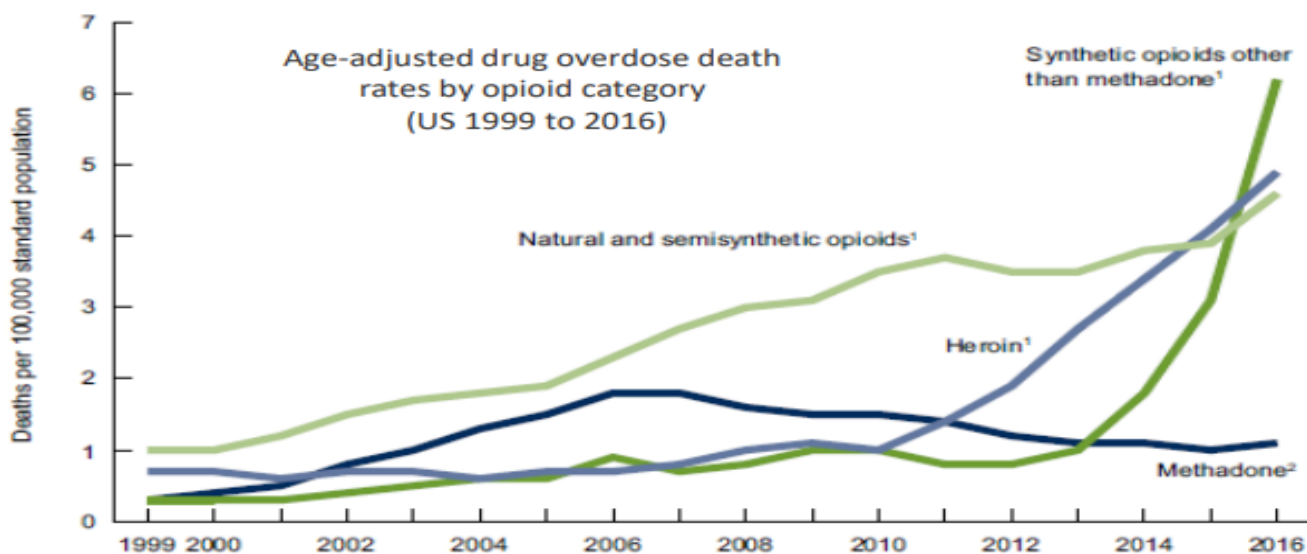
- Dr. Reddy's Labs (DRRD) today received final approval from the USFDA to launch Buprenorphine and Naloxone Sublingual Film, a generic version of Suboxone, in the the US market. Although the product is covered by seven patents until 2023, DRRD has got favorable ruling from the district court for four main patents. Indivior has challenged this ruling in the higher court and the decision is still pending. DRRD is doing an 'at risk' launch of gSuboxone based on the comfort it has on the patent litigation. The drug is indicated for the treatment of opioid addiction.
- **Competitive dynamics of gSuboxone:** Apart from DRRD, Mylan has received approval for gSuboxone. However, Mylan settled the patent dispute with Indivior (innovator) in Sep-17 – terms of the settlement were not disclosed. It is still unclear whether or not Mylan will launch the product immediately. Apart from DRRD and Mylan, three more players (Alvogen, Par Pharma and Teva) are in the race to launch gSuboxone. Par has settled the case with Indivior and can sell the product from 1st January 2023 or earlier under certain circumstances. In March 2018, the court ruled that Alvogen's version of gSuboxone does not infringe three patents ('514, '150 and '497); however, the company is yet to receive USFDA approval. Innovator had guided earlier that it will launch an authorized generic post the entry of a generic competitor.
- **Suboxone launch – a key growth driver:** According to IMS, secondary sales for Suboxone stood at ~USD1.86b for MAT April-18 in the US (primary sales: ~USD750-775m). Indivior's market share in Opioid Use Disorder (OUD) stood at ~54% at end-March 2018. Our base-case assumption is that at least two more players will enter the market soon. Based on that, we expect top-line contribution of ~USD60-65m on a 12-month basis (EPS contribution of ~INR14-15/share). However, if no other generic player enters the market for at least the next six months, then DRRD can generate revenue of greater than USD100m on an annualized basis.
- **Ramp-up of Sublocade can hurt Suboxone sales:** In March 2018, Indivior launched Sublocade in the US market for OUD. Sublocade is a once-a-month medicine, as against Suboxone film which is a daily medicine. Indivior expects this product to contribute revenue of ~USD1b at peak, which would mean a major shift in sales from Suboxone to Sublocade.
- **Key approvals awaited over next 12-18 months:** DRRD received complete response letter (CRL) for gNuvaring and gCopaxone in 4QFY18. The company is planning to respond to both the CRLs over the next two months. In the absence of further queries, we expect Nuvaring approval for DRRD by 2HFY19. Copaxone approval is expected only by 2HFY20.
- **Suboxone launch already factored in price; maintain Neutral:** Although the approval of gSuboxone is positive news for DRRD, the recent run-up in the stock already factors in this event. We maintain **Neutral** rating on the stock with a target price of INR2,275 @18x FY20E PER (v/s INR2,000 @18x FY20 PER). We have increased our EPS for FY19/20E by 16/14% as we build in the impact of early launch of Suboxone (earlier assumption of launch by 4QFY19E).

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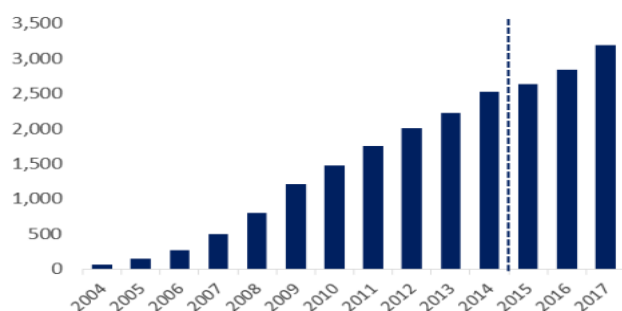
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Exhibit 1: Deaths due to drug overdose on the rise

Source: Indivior

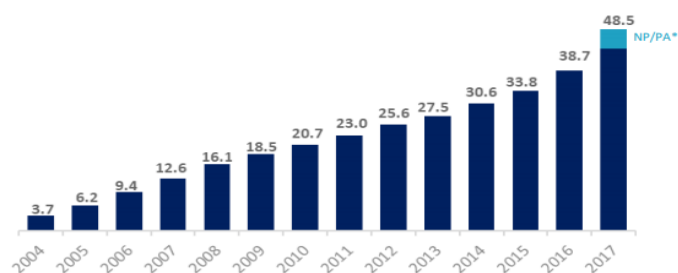
Exhibit 2: Strong, consistent market expansion...- Total buprenorphine market in mg⁽¹⁾ (millions) -

Source: Symphony Health Retail & Non-Retail TRx MG (IDV) ending Dec 2017

Source: Indivior

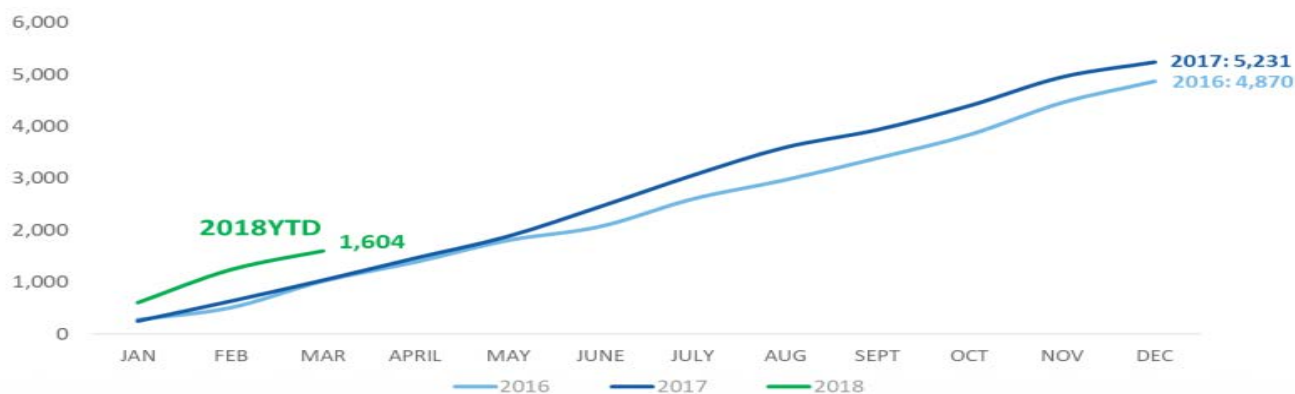
Exhibit 3: Driven by growing treatment capacity

- No. of HCP certifications (cumulative certifications in thousands) -

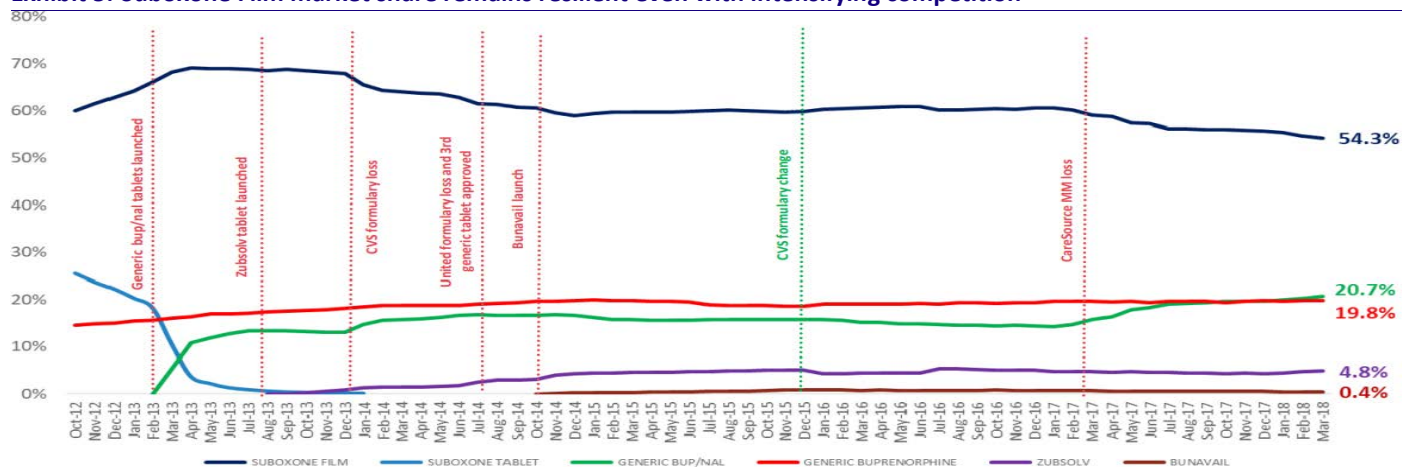


Source: NTIS DEA Certifications; Internal estimates

Source: Indivior

Exhibit 4: National Newly Waivered Treating MDs Continue on a Strong Pace**MD Waivers**

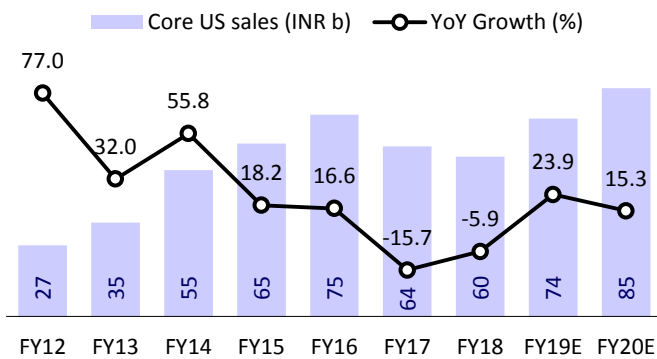
Source: Indivior

Exhibit 5: Suboxone Film market share remains resilient even with intensifying competition

Source: Indivior

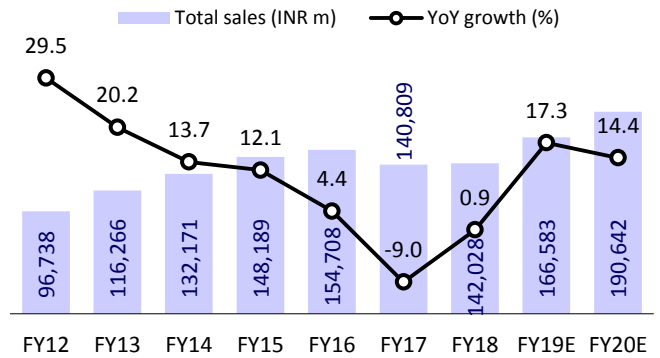
Story in charts

Exhibit 6: Ramp-up of key launches to boost US sales



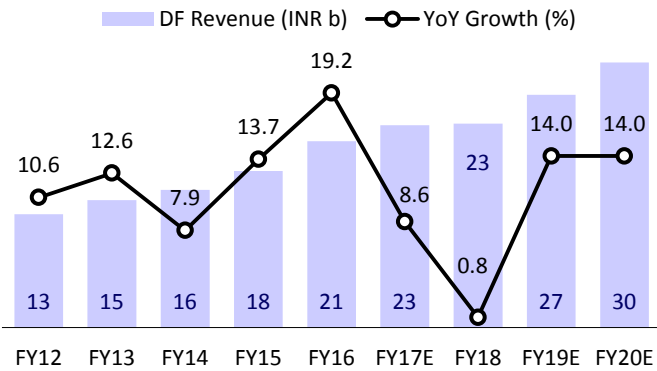
Source: Company, MOSL

Exhibit 7: Revenues to grow at CAGR 16% from FY18-20E



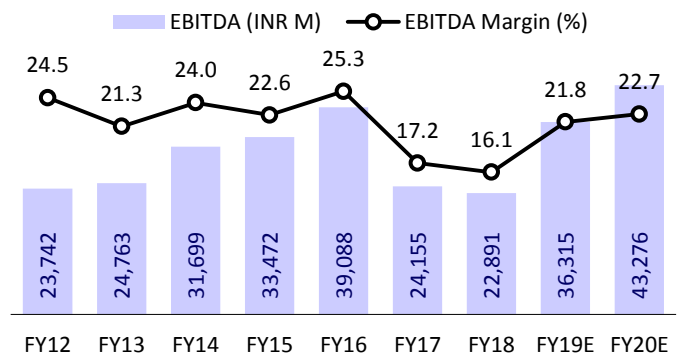
Source: Company, MOSL

Exhibit 8: Domestic biz to pick up in FY19 after GST implementation



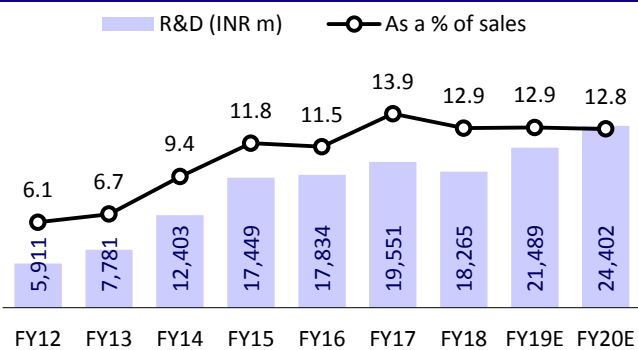
Source: Company, MOSL

Exhibit 9: EBITDA Margin to pick up FY19 onwards



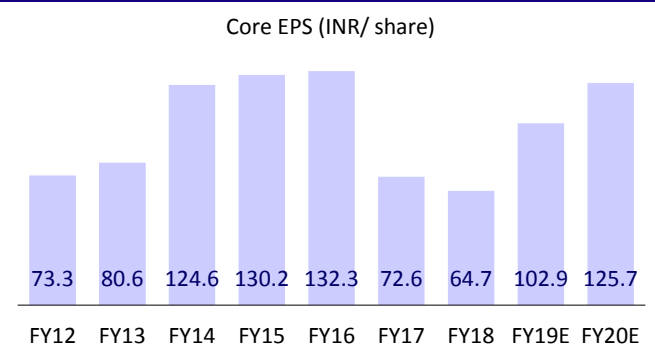
Source: Company, MOSL

Exhibit 10: R&D expense as % of sales



Source: Company, MOSL

Exhibit 11: EPS to grow at 39% CAGR from FY18-20E



Source: Company, MOSL

Financials and valuations

Income Statement						(INR m)	
Y/E March	2014	2015	2016	2017	2018	2019E	2020E
Net Sales	132,171	148,189	154,708	140,809	142,028	166,583	190,642
Change (%)	13.7	12.1	4.4	-9.0	0.9	17.3	14.4
Total Expenditure	100,472	114,717	115,620	116,654	119,137	130,268	147,367
EBITDA	31,699	33,472	39,088	24,155	22,891	36,315	43,276
Change (%)	28.0	5.6	16.8	-38.2	-5.2	58.6	19.2
Margin (%)	24.0	22.6	25.3	17.2	16.1	21.8	22.7
Depreciation & Amort.	7,085	8,103	10,343	11,722	11,762	13,826	15,957
EBIT	24,614	25,369	28,745	12,433	11,129	22,489	27,319
Int. and Finance Charges	0	0	0	0	0	0	0
Net Interest Exp	79	77	334	0	817	936	835
Forex (Gains)/Losses	-329	0	2,374	0	0	0	0
PBT & EO Expense	26,616	28,163	27,140	14,653	14,341	23,403	28,584
Change (%)	22.8	5.8	-3.6	-46.0	-2.1	63.2	22.1
PBT after EO Expense	26,616	28,163	27,140	14,653	14,341	23,403	28,584
Tax	5,093	5,984	7,127	2,614	4,535	6,319	7,718
Tax Rate (%)	19.1	21.2	26.3	17.8	31.6	27.0	27.0
Reported PAT	21,524	22,179	20,013	12,039	9,806	17,084	20,867
Adjusted Net Profit	21,188	22,179	22,577	12,039	10,736	17,084	20,867
Change (%)	54.9	4.7	1.8	-46.7	-10.8	59.1	22.1
Margin (%)	16.0	15.0	14.6	8.5	7.6	10.3	10.9

Balance Sheet						(INR m)	
Y/E March	2014	2015	2016	2017	2018	2019E	2020E
Equity Share Capital	851	852	853	829	830	830	830
Reserves	89,950	110,450	124,845	121,792	124,886	142,658	160,526
Net Worth	90,801	111,302	125,698	122,621	125,716	143,488	161,356
Loans	44,742	43,126	33,403	49,075	50,651	50,651	45,651
Deferred Liabilities/Tax	-3,310	-4,013	-5,368	-5,164	-3,455	-3,455	-3,455
Capital Employed	132,233	150,414	153,733	166,532	172,912	190,684	203,552
Gross Block	52,958	72,011	81,635	92,605	103,819	115,492	127,331
Less: Accum. Deprn.	21,213	30,040	35,505	42,324	54,086	67,912	83,869
Net Fixed Assets	37,814	48,090	52,756	56,376	57,411	55,257	51,139
Investments	26,384	38,871	41,854	26,317	28,935	28,935	28,935
Goodwill/Intangibles	14,697	16,430	20,596	46,176	46,974	46,974	46,974
Curr. Assets	78,664	85,580	82,730	82,512	86,718	98,568	120,597
Inventory	23,992	25,529	25,579	28,528	29,089	32,534	37,232
Account Receivables	33,037	40,755	41,250	38,196	40,696	41,026	46,951
Cash and Bank Balance	8,451	5,394	4,921	3,865	2,638	6,684	15,443
Others	13,184	13,901	10,980	11,923	14,295	18,324	20,971
Curr. Liability & Prov.	31,936	38,556	44,203	44,849	47,126	39,050	44,094
Account Payables	10,503	10,660	9,068	10,569	13,345	13,368	15,299
Other Current Liabilities	21,433	27,896	35,135	34,280	33,781	25,682	28,795
Net Current Assets	46,728	47,024	38,527	37,663	39,592	59,518	76,504
Appl. of Funds	125,623	150,415	153,733	166,532	172,912	190,684	203,552

E: MOSL Estimates

Financials and valuations

Ratios

Y/E March	2014	2015	2016	2017	2018	2019E	2020E
Basic (INR)							
EPS	124.6	130.2	132.3	72.6	64.7	102.9	125.7
Cash EPS	166.2	177.7	193.0	143.3	135.5	186.2	221.8
BV/Share	533.8	653.2	736.8	739.6	757.3	864.4	972.0
DPS	18.0	20.0	17.6	10.9	20.5	15.4	18.9
Payout (%)	16.6	17.9	17.6	17.6	39.9	17.6	17.6

Valuation (x)

P/E	18.9	18.1	17.8	32.4	36.4	22.8	18.7
PEG (x)	0.3	3.9	10	NA	-3	0.4	0.8
P/BV	4.4	3.6	3.2	3.2	3.1	2.7	2.4
EV/Sales	3.0	2.6	2.4	2.9	2.9	2.4	2.1
EV/EBITDA	12.6	11.6	9.6	16.9	17.9	11.1	9.0
Dividend Yield (%)	0.8	0.8	0.7	0.5	0.9	0.7	0.8

Return Ratios (%)

ROIC	23.6	20.9	21.2	8.9	5.8	11.7	13.3
RoE	25.9	21.9	19.1	9.7	8.6	12.7	13.7
RoCE	16.6	14.2	14.1	6.4	4.8	9.4	10.4

Working Capital Ratios

Fixed Asset Turnover (x)	2.7	2.4	2.0	1.6	1.4	1.5	1.6
Debtor (Days)	91	100	97	99	105	90	90
Inventory (Days)	66	63	60	74	75	71	71

Leverage Ratio

Debt/Equity (x)	0.5	0.4	0.3	0.4	0.4	0.4	0.3
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Cash Flow Statement

(INR m)

Y/E March	2014	2015	2016	2017	2018	2019E	2020E
Op. Profit/(Loss) before Tax	31,699	33,472	39,088	24,155	22,891	36,315	43,276
Interest/Dividends Recd.	2,003	2,793	-1,605	2,220	3,212	914	1,265
Direct Taxes Paid	-5,093	-5,984	-7,127	-2,614	-4,535	-6,319	-7,718
(Inc)/Dec in WC	-5,265	-3,353	8,024	-192	-3,156	-15,880	-8,227
CF from Operations	23,344	26,929	38,380	23,569	18,412	15,031	28,597
(inc)/dec in FA	-12,329	-20,112	-19,175	-40,922	-13,595	-11,673	-11,839
Free Cash Flow	11,015	6,817	19,205	-17,353	4,817	3,358	16,758
(Pur)/Sale of Investments	-8,253	-12,487	-2,983	15,537	-2,618	0	0
CF from Investments	-20,582	-32,599	-22,158	-25,385	-16,213	-11,673	-11,839
Change in net worth	-247	2,302	-2,104	-13,003	-2,800	3,686	664
(Inc)/Dec in Debt	8,064	-1,617	-9,723	15,672	1,576	0	-5,000
Other Items	-1,640	2,165	-219	204	0	0	0
Dividend Paid	-3,581	-3,979	-3,512	-2,113	-3,911	-2,998	-3,662
CF from Fin. Activity	2,596	-1,129	-15,558	760	-5,135	688	-7,998
Inc/Dec of Cash	5,357	-6,799	664	-1,056	-2,936	4,046	8,759
Add: Beginning Balance	5,136	8,451	5,394	4,921	3,865	2,638	6,684
Closing Balance	10,493	1,652	6,058	3,865	929	6,684	15,443

E: MOSL Estimates

NOTES

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	> - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

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Dr Reddy's Labs

Analyst ownership of the stock

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