

06 November 2024

India | Equity Research | Q2FY25 results review

Dr Reddy's Laboratories

Pharma

Decent print; work on growth levers underway

Dr. Reddy's Laboratories' (DRL) Q2FY25 performance, adjusted for acquisition-related expenses (INR 561mn) and impairment charge of gNuvaring (INR 924mn), was ahead of our expectations. US sales posted growth of 15.6% YoY to USD 445mn, likely driven by gRevlimid (pegged at USD 145mn in Q2) as volumes for base portfolio tumbled. Q2FY25 performance was driven by sales from vaccine portfolio of Sanofi in India and healthy 33.4% growth in RoW markets. Acquisition of NRT business from Haleon, consolidation of Sanofi's vaccine portfolio coupled with the launch of the Nutraceutical portfolio with Nestle in India and steady new launches across key markets should drive growth in the near term while biologics and GLP-1 products are expected to boost growth from FY26E. The stock has corrected ~8% post Q1FY25 results. We raise our rating to **HOLD**; TP maintained at INR 1,270, valuing base business at 26x FY26E core EPS of INR 47 and INR 66 in NPV for gRevlimid.

Traction across all regions; higher R&D squeezes margin

DRL's Q2FY25 revenue grew by 16.5% YoY to INR 80.1bn (l-Sec: INR 76.5bn). Gross margin, at 59.6%, expanded 92bps YoY/contracted 81bps QoQ, mainly due to improvement in product mix and overhead leverage, partly offset by price erosion. Adjusted for acquisition-related cost, EBITDA rose 10.8% YoY at INR 22bn (l-Sec: INR 21.1bn). EBITDA margin slumped 142bps to 27.5% (+94bps QoQ) due to higher R&D costs, which rose 33.5% YoY to INR 7.3bn and stood at 9.1% of revenue vs. 7.9% in Q2FY24 and 8.1% in Q1FY25. Adj. PAT declined 2.1% YoY to INR 14.5bn (l-Sec: INR 13.8bn).

US and India on a strong footing

US revenue declined 3.6% QoQ to USD 445mn (l-Sec: USD 438mn), mainly due to rationalisation of channel inventory. In Q2, DRL launched four new products and filed two products with the USFDA. DRL's biosimilar, denosumab (collaborated with Alvotech), is expected to be commercialised in FY26 and abatacept (in-licensed from Coya Therapeutics) shall launch in early FY27. We expect US sales to grow at a CAGR of ~11.6% over FY24–26E. India biz grew a robust 17.2% YoY to INR 13.9bn. Base business revenue grew ~9.8% YoY (excluding sales from Sanofi's vaccine portfolio). We expect the India business to grow at a CAGR of ~15% over FY24–26E. EU grew 7.6% YoY to INR 5.8bn, driven by new launches. Russia sales grew 19.0% YoY, largely due to price increase in certain brands while CIS was down 4.5% YoY, at INR 2.1bn, due to dip in volumes. RoW business was up 33.4% YoY (+24% QoQ) at INR 5.6bn. PSAI revenue surged 19.5% YoY (+9.8% QoQ) to INR 8.4bn.

Financial Summary

Y/E March (INR mn)	FY24A	FY25E	FY26E	FY27E
Net Revenue	2,79,164	3,21,430	3,69,716	3,45,680
EBITDA	78,233	88,043	1,00,030	71,795
EBITDA Margin (%)	28.0	27.4	27.1	20.8
Net Profit	55,686	60,935	68,012	45,762
EPS (INR)	66.8	73.1	81.5	54.9
EPS % Chg YoY	23.4	7.4	13.7	(32.7)
P/E (x)	19.1	17.7	15.6	23.2
EV/EBITDA (x)	12.7	11.1	9.8	13.3
RoCE (%)	20.1	19.5	20.9	13.6
RoE (%)	21.8	21.1	22.3	14.3

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Market Data

Market Cap (INR)	1,061bn
Market Cap (USD)	12,622mn
Bloomberg Code	DRRD IN
Reuters Code	REDY.BO
52-week Range (INR)	1,421 / 1,057
Free Float (%)	73.0
ADTV-3M (mn) (USD)	29.5

Price Performance (%)	3m	6m	12m
Absolute	(6.6)	0.2	20.9
Relative to Sensex	(7.5)	(7.4)	(2.6)

ESG Score	2023	2024	Change
ESG score	74.6	74.9	0.3
Environment	68.3	72.3	4.0
Social	60.8	61.1	0.3
Governance	87.0	89.5	2.5

Note - Score ranges from 0 - 100 with a higher number indicating a higher ESG score.

Source: SES ESG, l-sec research

Earnings Revisions (%)	FY25E	FY26E
Revenue	(0.0)	4.0
EBITDA	0.4	4.5
EPS	(0.4)	4.5

Previous Reports

28-07-2024: [Q1FY25 results review](#)

27-06-2024: [Company Update](#)

Valuation and risks

DRL's US sales continues to be driven by gRevlimid sales while volume for base portfolio has taken a hit. In H1FY25, R&D spending soared 29.1% to INR 13.5bn, mainly towards development of GLP-1 products, complex injectables, biosimilars and novel drugs. It aims to launch 15–20 products in US annually and has a pipeline of 20 high-value products, which along with a rise in gRevlimid's market share will likely drive growth in the near term. The company is working on 16–17 GLP-1 products, including Liraglutide and Semaglutide, which can potentially be an important growth driver post the gRevlimid opportunity. Besides, India growth is expected to pick up due to integration of Sanofi's vaccine portfolio, and sales from Nestle's nutraceuticals brands should boost growth further. Windfall from the earnings of gRevlimid is being utilised to build a robust consumer health business (current size: USD 320mn). DRL has completed the acquisition of Nicotinell brand from Haleon, for an upfront cash payment of GBP 458mn in Sep'24, which is expected to add revenues of USD 300mn to the consumer franchise in a couple of years. The company further aims to scale up consumer brand sales to USD 1bn through M&As and growth in the existing business. While its revenue growth will likely be supported by inorganic initiatives, the relatively higher spend on R&D and SG&A costs of the new business may add pressure on margins. Overall, we expect revenue/PAT CAGRs of 15.1%/10.5%, over FY24–26E, while EBITDA margins may see a 97bps dent to 27.1% in FY26E due to higher R&D and overheads.

At CMP of INR 1,272, the stock trades at valuations of 28.0x FY25E and 27.3x FY26E ex-Revlimid earnings and EV/EBITDA multiples of 18.4x FY25E and 17.5x FY26E. We upgrade our rating to **HOLD** (earlier Reduce), and maintain our target price at INR 1,270 (adjusted for 1:5 share split), valuing the base business' FY26E earnings of INR 47 at 26x and NPV of INR 66 for gRevlimid.

Key upside risk: M&A in key focus areas; and cost optimisation to curtail overhead cost.

Q2FY25 conference call highlights

US

- US sales stood at USD 445mn in constant currency. Sequential decline was mainly due to rationalisation of channel inventory.
- It launched four products in Q2FY25 (seven in H1FY25). For FY25, it aims to launch 15–20 products.
- The company has a pipeline of over 20 high-value products.
- Apart from Liraglutide and Semaglutide, it is further working on 16–17 GLP-1 products. Aims to be one of the leading generic companies in these products. The company shall be manufacturing its API and formulation while device is to be sourced from CMOs.
- The company is also investing in setting up additional capacities for APIs of GLP-1 products.
- The in-licensed biosimilar abatacept is expected to be launched in early FY27.
- It has collaborated with Alvotech for the commercialisation of their denosumab biosimilar candidate in US, Europe and the UK. The product is expected to be commercialised in FY26.

India

- Base business (excluding vaccine biz of Sanofi) grew between 9–10% in Q2FY25.
- Overall, growth was driven by revenues from the vaccine portfolio in-licensed from Sanofi, new products launched as well as price increases.
- It launched three brands in Q2 (16 in H1FY25).
- The company has integrated the nutraceutical products under subsidiary, 'Dr. Reddy's and Nestle Health Science Limited' in Q2FY25.
- It has entered into a non-exclusive patent licensing agreement with Takeda to commercialise Vonoprazan (novel gastrointestinal drug) in India.

Europe

- It launched eight new products in Q2 (20 launched in H1FY25).
- In Europe, growth was driven by new launches, partly offset by price erosion.
- The company received marketing authorisation from European Commission for rituximab biosimilar. It aims to launch this product in Feb'25.
- In Sep'24, it completed acquisition of the Nicotine Replacement Therapy ('NRT') portfolio from Haleon UK (ex- US) for an upfront cash payment of GBP 458mn.
- The company aims to drive growth in NRT portfolio by increasing growth-related investments, launching the products in new countries, work on lifecycle management and packaging of the product.
- Intangibles pertaining to acquisition of the NRT portfolio shall be amortised over 22–23 years.

Russia & CIS

- It has launched 22 products across all emerging markets in Q2FY25.
- Russia biz growth was driven by higher sales volumes, better pricing and new product launches, partly offset by unfavourable currency exchange rate movements.
- Lower volumes fueled a 2% decline in revenues from CIS countries.

PSAI

- Growth was driven by better volumes for base business, traction in services business and new launches.
- In Q2FY25, it filed 22 DMFs (36 in H1FY25).

Guidance

- SG&A spending likely between 27.5–28% of sales in FY25.
- R&D spending likely between 8.5–9% for FY25.
- Effective tax rate is likely to be ~25% for FY25.

Q2FY25 performance

- Improvement in gross margins was mainly due to product mix and overhead leverage, partly offset by price erosion.
- It incurred one-time acquisition-related costs towards NRT portfolio (0.7% of sales); excluding this, SG&A spend was at 28% of sales.

- R&D was higher during the quarter and was mainly towards development of biosimilar (36% of spend), complex generics (50%) including peptides and complex injectables and novel oncology assets (14%).
- Other income was lower in the quarter on a high base of settlement income last year.
- It recorded a reversal of a deferred tax asset of INR 0.48bn; adjusting for it, effective tax rate for the quarter was at 25.9% of PBT.
- Adjusting for one-time acquisition related cost, impairment charge on non-current assets and one-time tax expense, PAT stood at 18% of sales.
- Operating working capital stood at INR 120.7bn
- It incurred capex of INR 7.4bn and generated FCF of INR 2.04bn.
- Net cash balance stood at INR 18.9bn post cash payment of GBP 458mn for NRT acquisition.
- The company has impaired the entire carrying value of gNuvaring intangible in Q2FY25.

Exhibit 1: Q2FY25 result review

Y/E Mar (INR mn)	Q2FY25	Q2FY24	YoY(%)	Q1FY25	QoQ (%)	H1FY25	H1FY24	YoY(%)
Net Sales	80,162	68,802	16.5	76,727	4.5	1,56,889	1,36,186	15.2
Gross Profit	47,769	40,368	18.3	46,344	3.1	94,113	79,921	17.8
Gross Margins (%)	59.6	58.7	92bps	60.4	(81bps)	60.0	58.7	
EBITDA	22,022	19,881	10.8	21,266	3.6	43,288	40,281	7.5
EBITDA Margins (%)	27.5	28.9	(142bps)	27.7	(24bps)	27.6	29.6	
Other Income	1,045	1,838	(43.1)	529	97.5	1,574	2,661	(40.8)
Interest	(1,555)	(1,225)		(837)		(2,392)	(2,009)	
Depreciation	3,970	3,755	5.7	3,806	4.3	7,776	7,288	6.7
Extraordinary expenses	1,485	55		5		1,490	66	
PBT	19,167	19,134	0.2	18,821	1.8	37,988	37,597	1.0
Tax	5,752	4,334	32.7	4,901	17.4	10,653	8,772	21.4
Tax Rate (%)	30.0	22.7		26.0		28.0	23.3	
PAT	13,415	14,800	(9.4)	13,920	(3.6)	27,335	28,825	(5.2)
Adj. PAT	14,529	14,843	(2.1)	13,924	4.3	28,453	28,876	(1.5)
NPM (%)	16.7	21.5		18.1		17.4	21.2	

Source: I-Sec research, Company data

Exhibit 2: Segmental break-up

INR mn	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24	Q3FY24	Q4FY24	Q1FY25	Q2FY25	% YoY	% QoQ
Generics	55,946	59,241	54,257	60,083	61,084	63,095	61,190	68,857	71,576	17.2	3.9
USA	28,001	30,567	25,321	31,978	31,775	33,492	32,626	38,462	37,281	17.3	(3.1)
India	11,500	11,274	12,834	11,482	11,860	11,800	11,265	13,252	13,971	17.8	5.4
Europe	4,199	4,303	4,960	5,071	5,286	4,970	5,208	5,265	5,770	9.2	9.6
Russia	5,900	6,900	5,200	5,600	5,800	5,900	5,000	5,500	6,900	19.0	25.5
RoW	4,146	3,997	3,642	3,952	4,163	4,633	4,891	4,478	5,554	33.4	24.0
CIS	2,200	2,200	2,300	2,000	2,200	2,300	2,200	1,900	2,100	(4.5)	10.5
API	6,434	7,758	7,787	6,709	7,034	7,839	8,219	7,657	8,407	19.5	9.8
Proprietary products	677	701	924	592	684	1,214	1,420	212	179	(73.8)	(15.6)
Total	63,057	67,700	62,968	67,384	68,802	72,148	70,829	76,726	80,162	16.5	4.5
US (USD mn)	351	375	312	389	385	401	392	462	445	15.6	(3.6)

Source: I-Sec research, Company data

Exhibit 3: Key growth drivers of domestic business in Q2FY25

Brands (INR mn)	Q2FY25	Q2FY24	YoY (%)	Q1FY25	QoQ (%)	MAT Sep'24	MAT Sep'23	YoY (%)
Voveran	586	698	-16.0	565	3.7	2,390	2,441	-2.1
Atarax	686	551	24.6	542	26.7	2,240	1,979	13.2
Omez	518	538	-3.7	618	-16.2	2,181	2,097	4.0
Econorm	637	477	33.6	643	-1.0	2,097	1,903	10.2
Ketorol	557	386	44.3	585	-4.8	2,027	1,568	29.3
Hexaxim	379	354	6.9	371	2.1	1,553	1,358	14.3
Venusia	360	297	21.5	354	1.7	1,485	1,194	24.3
Zedex	388	268	44.9	260	49.0	1,408	1,356	3.8
Razo-D	354	344	3.0	341	3.9	1,359	1,430	-5.0
Menactra	364	313	16.4	318	14.6	1,316	1,023	28.6

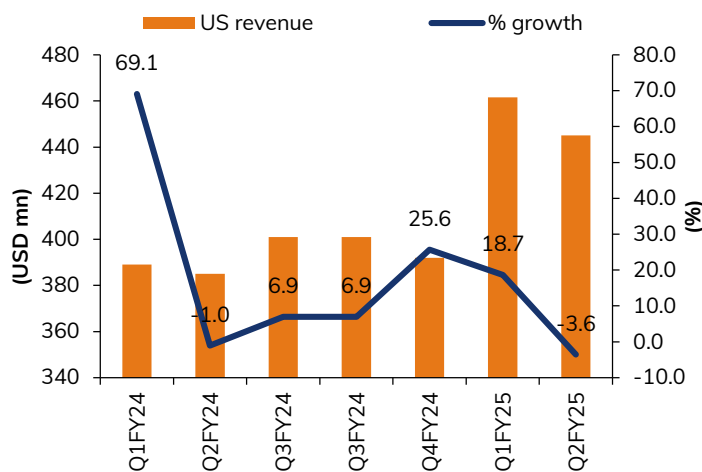
Source: IQVIA

Exhibit 4: Growth profile across key therapies in India

Therapies (INR mn)	Q2FY25	Q2FY24	YoY (%)	Q1FY25	QoQ (%)	MAT Sep'24	MAT Sep'23	YoY (%)
Gastro Intestinal	3,046	2,823	7.9	3,094	-1.5	11,263	10,571	6.5
Respiratory	2,614	2,318	12.8	1,872	39.6	9,651	8,947	7.9
Pain / Analgesics	1,963	1,849	6.2	1,914	2.5	7,420	6,726	10.3
Cardiac	1,730	1,604	7.9	1,783	-3.0	6,666	7,120	-6.4
Derma	1,488	1,247	19.3	1,304	14.1	5,280	4,485	17.7
Vaccines	1,364	1,234	10.5	1,346	1.4	5,116	4,211	21.5
Anti Diabetic	1,043	939	11.0	1,040	0.2	3,930	3,554	10.6
Vitamins/Minerals/Nutrients	992	979	1.3	1,010	-1.8	3,794	3,435	10.4
Stomatologicals	884	812	8.8	852	3.7	3,281	2,736	19.9
Anti-Infectives	939	810	15.9	649	44.6	3,225	2,851	13.1

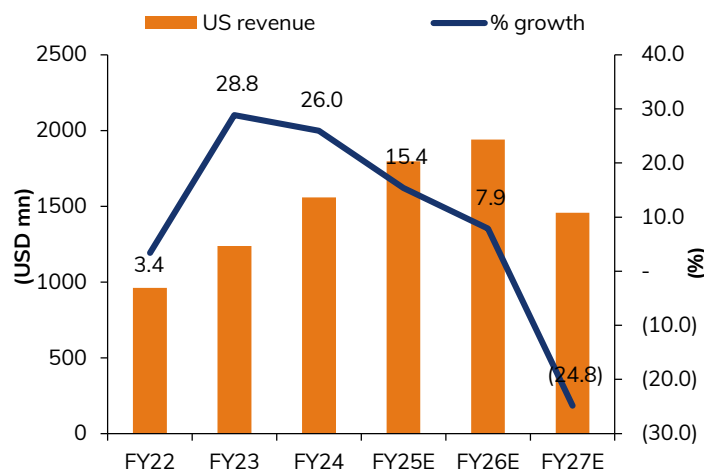
Source: IQVIA

Exhibit 5: US revenue declined due to rationalisation of channel inventory



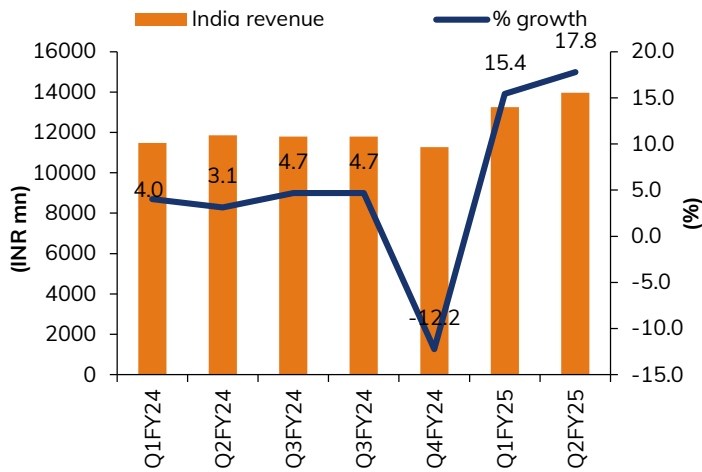
Source: I-Sec research, Company data

Exhibit 6: New launches coupled with market share gain in gRevlimid to drive growth



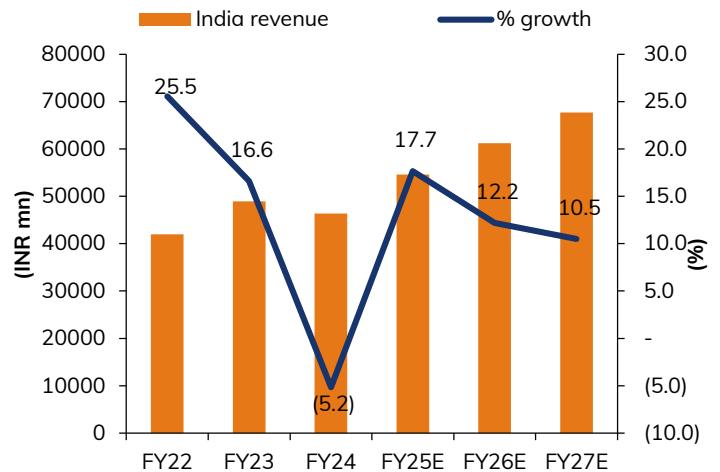
Source: I-Sec research, Company data

Exhibit 7: Domestic business grew a robust 17.8% YoY in Q2FY25



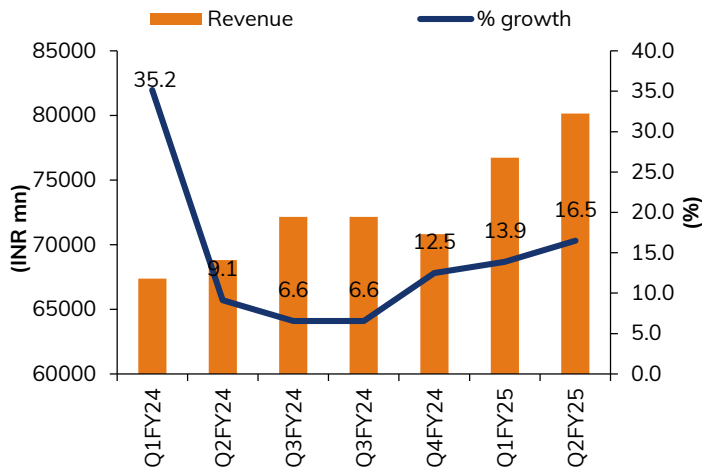
Source: I-Sec research, Company data

Exhibit 8: Double-digit growth expected in India from FY25E



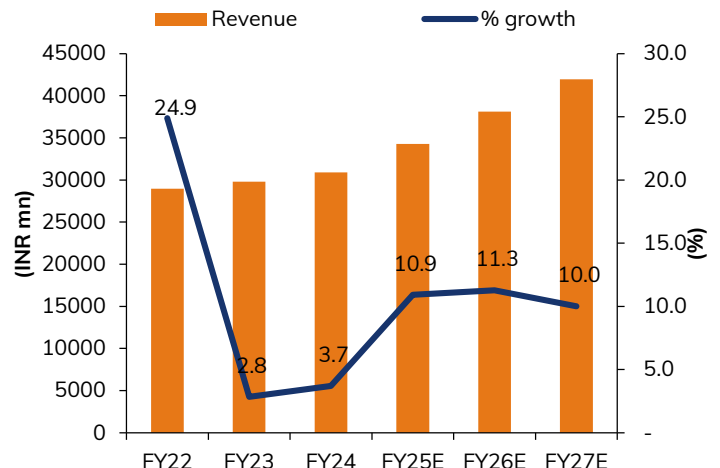
Source: I-Sec research, Company data

Exhibit 9: Traction across regions boosts overall growth



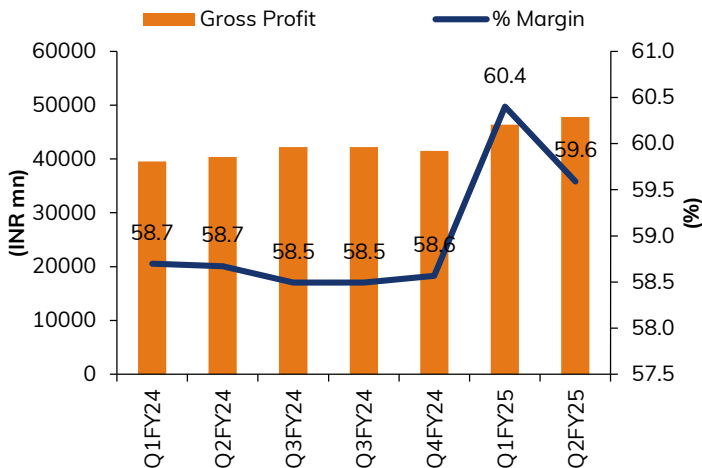
Source: I-Sec research, Company data

Exhibit 10: 15.1% revenue CAGR over FY24–26E



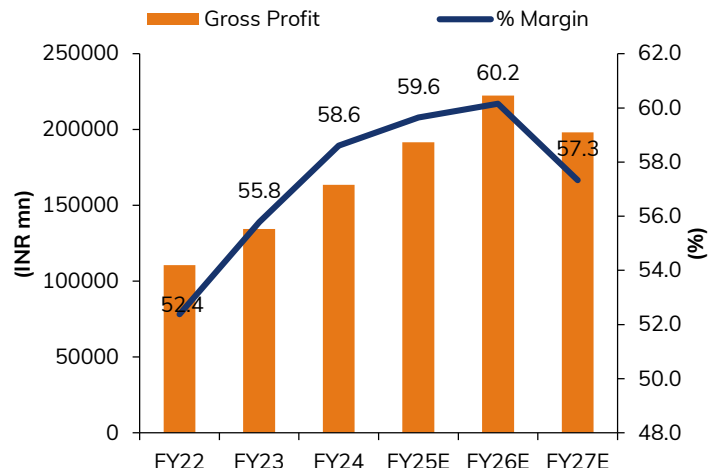
Source: I-Sec research, Company data

Exhibit 11: Gross margin improved on account of better product mix and overhead leverage



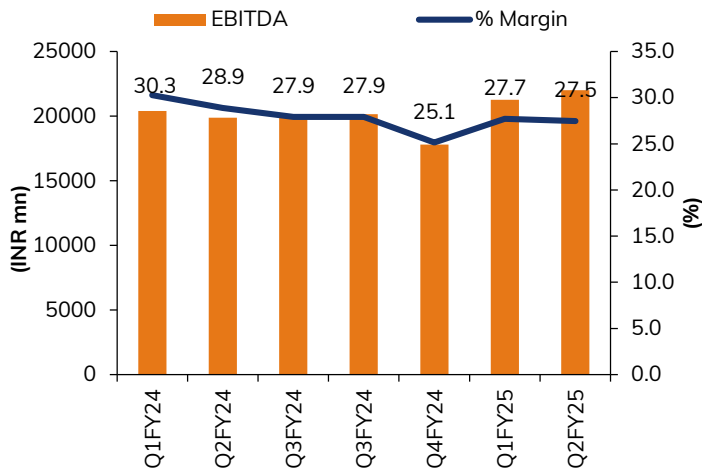
Source: I-Sec research, Company data

Exhibit 12: Gross margin to stay stable at ~60% till FY26E



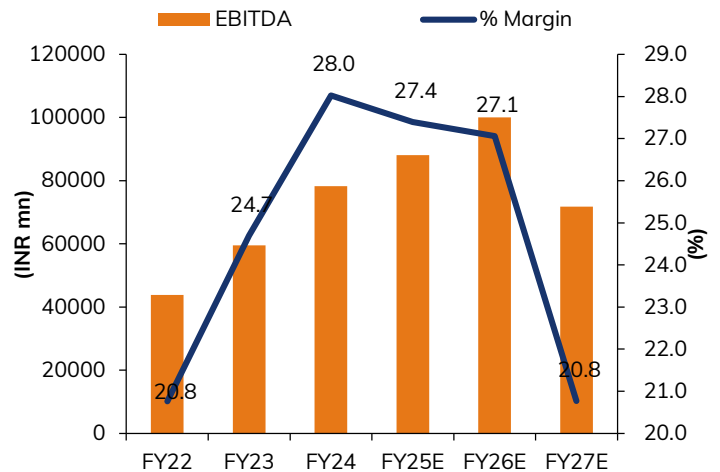
Source: I-Sec research, Company data

Exhibit 13: EBITDA margins slumped 142bps YoY due to higher R&D



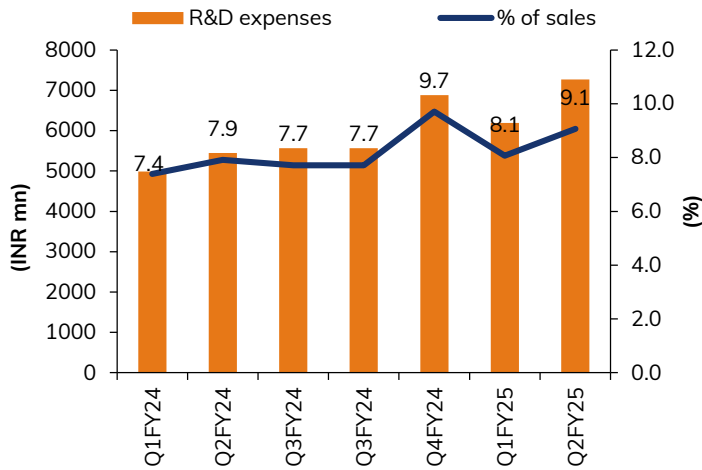
Source: I-Sec research, Company data

Exhibit 14: Higher spends in R&D and SG&A cost of new business to curb margins



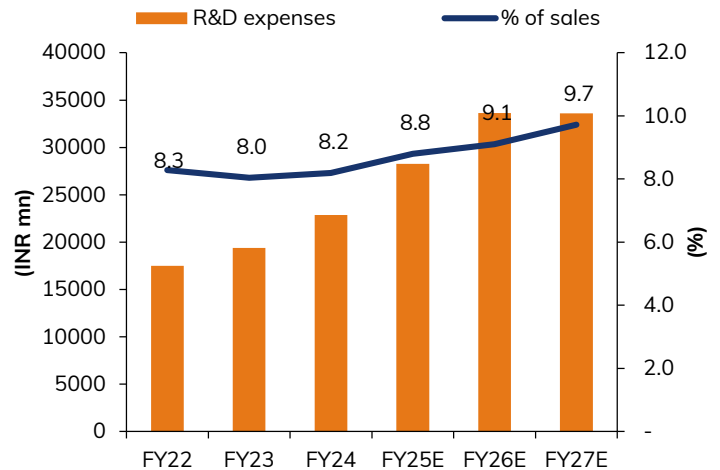
Source: I-Sec research, Company data

Exhibit 15: R&D expense rose 33.5% YoY to ~9.1% of sales



Source: I-Sec research, Company data

Exhibit 16: R&D spend to be in the range of ~8.5–9% in FY25E



Source: I-Sec research, Company data

Exhibit 17: Shareholding pattern

%	Mar'24	Jun'24	Sep'24
Promoters	26.7	26.7	26.6
Institutional investors	62.8	63.1	62.6
MFs and others	8.0	10.1	10.9
Insurance Cos	7.7	9.7	8.0
FII's	47.1	43.3	43.8
Others	10.5	10.2	10.8

Source: Bloomberg, I-Sec research

Exhibit 18: Price chart



Source: Bloomberg, I-Sec research

Financial Summary

Exhibit 19: Profit & Loss

(INR mn, year ending March)

	FY24A	FY25E	FY26E	FY27E
Net Sales	2,79,164	3,21,430	3,69,716	3,45,680
Operating Expenses	85,374	1,03,677	1,22,357	1,26,396
EBITDA	78,233	88,043	1,00,030	71,795
EBITDA Margin (%)	28.0	27.4	27.1	20.8
Depreciation & Amortization	14,700	15,920	16,904	17,744
EBIT	63,533	72,123	83,126	54,051
Interest expenditure	-	-	-	-
Other Non-operating Income	8,193	8,851	7,266	6,644
Recurring PBT	71,726	80,974	90,392	60,695
Profit / (Loss) from Associates	147	265	291	320
Less: Taxes	16,186	19,937	22,671	15,254
PAT	55,540	61,037	67,721	45,441
Less: Minority Interest	-	-	-	-
Extraordinaries (Net)	-	-	-	-
Net Income (Reported)	55,684	59,812	68,012	45,762
Net Income (Adjusted)	55,686	60,935	68,012	45,762

Source Company data, I-Sec research

Exhibit 20: Balance sheet

(INR mn, year ending March)

	FY24A	FY25E	FY26E	FY27E
Total Current Assets	2,51,767	2,73,868	3,03,188	3,09,876
of which cash & cash eqv.	81,470	91,441	93,941	1,13,980
Total Current Liabilities & Provisions	82,009	90,899	1,03,931	98,847
Net Current Assets	1,69,758	1,82,968	1,99,258	2,11,029
Investments	5,255	5,255	5,255	5,255
Net Fixed Assets	76,886	75,966	74,062	71,318
ROU Assets	-	-	-	-
Capital Work-in-Progress	-	-	-	-
Total Intangible Assets	41,204	41,204	41,204	41,204
Other assets	1,632	1,879	2,161	2,021
Deferred Tax Assets	10,774	10,774	10,774	10,774
Total Assets	3,05,509	3,18,046	3,32,714	3,41,601
Liabilities				
Borrowings	20,020	17,020	14,020	11,020
Deferred Tax Liability	909	909	909	909
provisions	61	61	61	61
other Liabilities	3,969	3,969	3,969	3,969
Equity Share Capital	2,367	2,367	2,367	2,367
Reserves & Surplus	2,78,183	2,93,720	3,11,388	3,23,275
Total Net Worth	2,80,550	2,96,087	3,13,755	3,25,642
Minority Interest	-	-	-	-
Total Liabilities	3,05,509	3,18,046	3,32,714	3,41,601

Source Company data, I-Sec research

Exhibit 21: Cashflow statement

(INR mn, year ending March)

	FY24A	FY25E	FY26E	FY27E
Operating Cashflow	45,433	72,246	70,845	71,913
Working Capital Changes	(1,809)	8,482	(1,642)	29,192
Capital Commitments	(40,283)	33,365	(10,565)	(10,565)
Free Cashflow	5,150	1,05,611	60,280	61,348
Other investing cashflow	-	-	-	-
Cashflow from Investing Activities	(40,283)	33,365	(10,565)	(10,565)
Issue of Share Capital	805	-	-	-
Interest Cost	(1,711)	-	-	-
Inc (Dec) in Borrowings	-	-	-	-
Dividend paid	(6,648)	(44,274)	(50,345)	(33,874)
Others	3,791	(3,000)	(3,000)	(3,000)
Cash flow from Financing Activities	(3,763)	(47,274)	(53,345)	(36,874)
Chg. in Cash & Bank balance	1,387	58,336	6,935	24,474
Closing cash & balance	7,166	65,443	72,378	96,852

Source Company data, I-Sec research

Exhibit 22: Key ratios

(Year ending March)

	FY24A	FY25E	FY26E	FY27E
Per Share Data (INR)				
Reported EPS	66.8	71.7	81.5	54.9
Adjusted EPS (Diluted)	66.8	73.1	81.5	54.9
Cash EPS	84.4	92.2	101.8	76.1
Dividend per share (DPS)	40.0	53.1	60.4	40.6
Book Value per share (BV)	336.4	355.0	376.2	390.5
Dividend Payout (%)	59.9	74.0	74.0	74.0
Growth (%)				
Net Sales	15.9	15.1	15.0	(6.5)
EBITDA	31.5	12.5	13.6	(28.2)
EPS (INR)	23.4	7.4	13.7	(32.7)
Valuation Ratios (x)				
P/E	19.1	17.7	15.6	23.2
P/CEPS	15.1	13.8	12.5	16.7
P/BV	3.8	3.6	3.4	3.3
EV / EBITDA	12.7	11.1	9.8	13.3
P / Sales	3.8	3.3	2.9	3.1
Dividend Yield (%)	3.1	4.2	4.7	3.2
Operating Ratios				
Gross Profit Margins (%)	58.6	59.6	60.2	57.3
EBITDA Margins (%)	28.0	27.4	27.1	20.8
Effective Tax Rate (%)	22.6	24.6	25.1	25.1
Net Profit Margins (%)	19.9	19.0	18.3	13.1
NWC / Total Assets (%)	-	-	-	-
Net Debt / Equity (x)	(0.2)	(0.3)	(0.3)	(0.3)
Net Debt / EBITDA (x)	(0.9)	(0.9)	(0.9)	(1.5)
Profitability Ratios				
RoCE (%)	20.1	19.5	20.9	13.6
RoE (%)	21.8	21.1	22.3	14.3
RoC (%)	27.1	27.0	29.2	19.6
Fixed Asset Turnover (x)	4.1	4.4	4.9	4.7
Inventory Turnover Days	95	84	84	73
Receivables Days	-	-	-	-
Payables Days	46	42	41	39

Source Company data, I-Sec research

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