

Industry Pharmaceuticals
Bloomberg DRRD IN
BSE CODE 500124

RATING	NEUTRAL
CMP	3189
Price Target	3073
Potential Upside	-4%

Rating Change	↔
Estimate Change	↑
Target Change	↑

STOCK INFO	
52wk Range H/L	3207/2065
Mkt Capital (Rs Cr)	52972
Free float (%)	73%
Avg. Vol 1M (,000)	469
No. of Shares (Crs)	17
Promoters Pledged %	0%

RESEARCH ANALYST

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Sales growth across geographies, PAT impacted due to a one-off impairment charges.

3QFY20 Result update

- Overall revenue grew by 14% YoY to Rs. 4384 crs (vs our estimate of Rs. 4021 crs) on account of growth across geographies especially Europe, US and India.
- The sales from North America increased by 7% YoY to US\$ 224 mn on account of higher volumes in some of its key molecules partly offset by price erosion in some of its key molecules.
- Revenue from Europe grew by 52% YoY primarily on account of new products and volume traction in base business partly offset by lower realizations as few key molecules entered tenders.
- Revenue from the Emerging market grew by 19% YoY to Rs.920; the growth was primarily driven by increase in volumes coupled with better realizations in some of the key molecules. The sales from India business grew by 13% YoY to Rs 764 crs.
- Gross margin for the quarter declined by 176 bps YoY to 67.8% and EBITDA margin expanded by 263 bps YoY to 23.5%.
- DRREDDY reported a loss of Rs. 538 crs as the company took an impairment charges of Rs. 1320 crs, of which Rs. 1114 crs is towards impairment of gNuvaring and the balance of Rs. 206 crs is towards other product related intangibles.

View and Valuation

DRREDDY reported strong numbers this quarter with sales improving across all geographies. The overall revenue rose 14% YoY with decent growth coming from US, India and Emerging markets. The cost optimization and productivity improvement initiatives being the major focus area of the company have led to margin expansion this quarter. However, the company reported loss in 3QFY20 based on the impairment charges of Rs. 1320 crs towards gNuvaring and other product related intangibles.

With the company's major focus being on growth across all geographies and cost efficiency, we expect to see traction in the margins going forward. The focus across all markets will reduce the dependency on one particular market and will help in revenue growth. Post result, based on the positive management commentary, we have increased our PAT estimate for FY21 by 11% though there is still a lack of clarity regarding how these markets will pan out going forward. Therefore, we maintain our NEUTRAL stance with a target price of Rs. 3073 (23x FY21E EPS).

Key Risks to our rating and target

- Re-inspection at API Srikakulam facility.
- gCopaxone launch.

Fig in Rs Cr

KEY FINANCIAL/VALUATIONS	FY17	FY18	FY19	FY20E	FY21E
Net Sales	14196	14281	15448	17396	18801
EBITDA	2221	2351	3178	3858	3827
EBIT	1194	1274	2043	2686	2590
PAT	1041	947	1950	1905	2217
EPS (Rs)	63	57	118	115	134
EPS growth (%)	-50%	-9%	106%	-2%	16%
ROE (%)	8.5%	7.5%	13.9%	12.3%	12.8%
ROCE (%)	9.3%	8.4%	12.6%	15.7%	13.6%
BV	740	758	845	936	1045
P/B (X)	3.5	2.7	3.3	3.4	3.1
P/E (x)	40.9	36.5	23.6	27.8	23.9

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3QFY20 Results

Fig in Rs Cr

FINANCIALS	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20	YoY %	QoQ%	FY18	FY19	YoY %
Net Sales	3,865	4,030	3,858	4,813	4,397	13.8%	-8.6%	14,281	15,448	8.2%
Other Income	102	83	430	54	67	-34.2%	24.6%	155	338	117.5%
COGS	1,176	1,262	1,207	1,401	1,415	20.4%	1.0%	4,040	4,495	11.3%
Gross Margin	69.6%	68.7%	68.7%	70.9%	67.8%	-1.8%	-3.1%	71.7%	70.9%	-0.8%
Employee Cost	805	842	862	826	838	4.0%	1.5%	3,215	3,356	4.4%
Other Expen.	1,079	1,107	1,048	1,522	1,113	3.2%	-26.9%	4,675	4,419	-5.5%
EBITDA	805	819	742	1,064	1,031	28.2%	-3.1%	2,351	3,178	35.2%
EBITDA Mar.	20.8%	20.3%	19.2%	22.1%	23.5%	2.6%	1.4%	16.5%	20.6%	4.1%
Depreciation	290	287	289	313	287	-1.2%	-8.4%	1,077	1,135	5.3%
EBIT	514	532	453	751	745	45%	-0.8%	79	89	12.8%
Interest	24	25	30	30	15	-37%	-49.8%	79	89	12.8%
PBT	593	591	853	774	797	34.4%	2.9%	912	1,906	109%
Exceptional Item					1,320					
Tax	101	151	193	(321)	33	-68%	-110%	438	386	-12%
PAT	500	455	677	1,107	(538)	-208%	-149%	947	1,950	106%
PAT Margin	12.9%	12.9%	12.9%	12.9%	-12.2%	-25%	-153%	6.6%	12.6%	6%

Concall Highlights

- The sales from North America increased by 7% YoY to US\$ 224 mn on account of higher volumes in some of its key molecules partly offset by price erosion in some of its key molecules
- Of the 30 products expected launch in USFDA in FY20, the company has launched 22 products so far and expects to launch the remaining this year itself.
- The company has filed 20 formulations across the global markets, with 3 ANDAs in the US; and has filed 20 DMFs across the markets, with 3 DMFs in the US.
- The company is focusing on increasing the market share of products like gSuboxone and other few products in the US market.
- Europe sales grew by 55% YoY and 12% sequentially to 12%, Revenue from the Emerging market and India business grew by 19% and 13% YoY respectively.
- The company launched 9 products in Europe, 17 products in EM and 8 new brands in India including Celevida (Nutrition segment).
- Among the Emerging markets, Russia grew strongly on account of retail growth and new tender.
- For the India business, the secondary sales as reported by IQVIA is 10.6% vs the market growth of 9.6%. According to the management, profitability in India business has grown much better than the topline and expects that there is more scope for improvement.
- The gross margin for global generics and PSAI grew by 270 bps and 540 bps to 58.2% and 30% respectively.
- Exception Item of Rs. 1320 crs: Total impairment charge for the quarter ended 31 December 2019 is Rs, 1320 crs, of which Rs. 1114 crs is towards impairment of gNuvaring and the balance of Rs. 206 crs is towards other product related intangibles.
- The R&D spends for the quarter was at 390 crs, 9% of sales in comparison to 9.5% of sales in Q3FY19. The management expects the R&D spend in the absolute terms to be in the range of Rs.1500- 1600 crs going forward.
- The free cash flow this quarter was 582crs, Capex for the quarter were at Rs. 120 crs and the net surplus cash stood at Rs. 414 crs as on 31 Dec 2019.
- On the regulatory front, the API manufacturing facilities in Srikakulam which received warning letter on 5 Nov 2015. As on 27 January 2020, the facility is undergoing inspection by the USFDA.
- The major focus of the company going ahead would be to focus on growth across markets especially the Emerging markets and cost efficiency, which would lead to faster growth of the bottomline than the topline.

Exhibit: Sales and Sales Growth

The overall revenue this quarter grew by 14% YoY to Rs. 4384 crs (vs our estimate of Rs. 4021 crs)

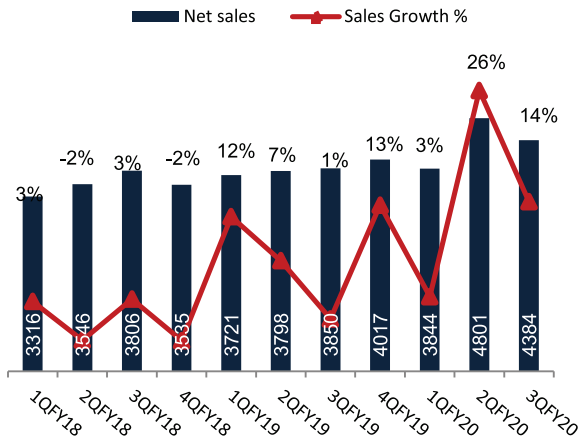


Exhibit: Domestic sales and YoY growth

The domestic sales grew by 13% YoY to Rs. 764 crs (vs our estimate of Rs. 762 crs)

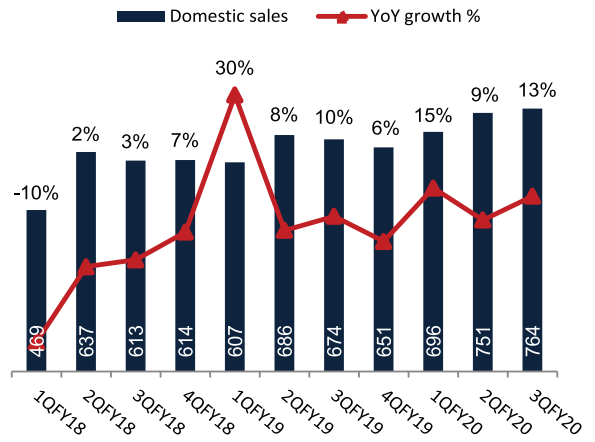


Exhibit: PAT and PAT margin

The company reported a loss of Rs. 538 crs on account of the impairment charges of Rs 1320 crs.

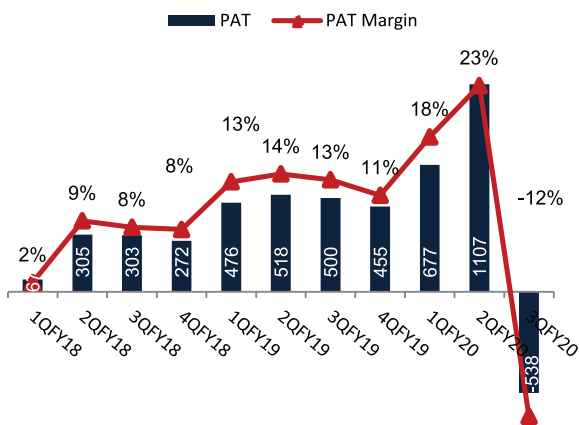


Exhibit: R&D cost and R&D as a % of sales

R&D expenses for quarter were at 390 crs, 9% of sales in comparison to 9.5% of sales in Q3FY19.

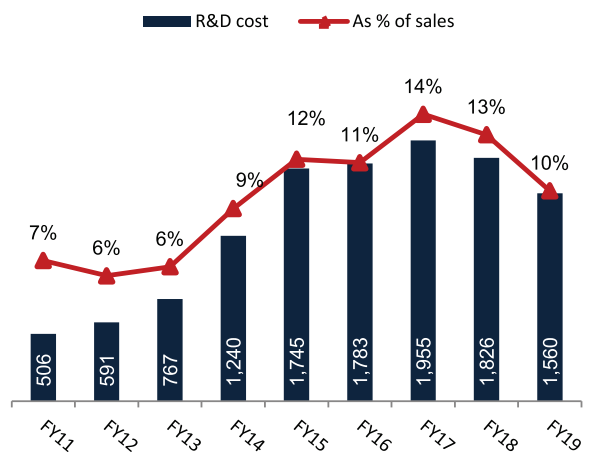
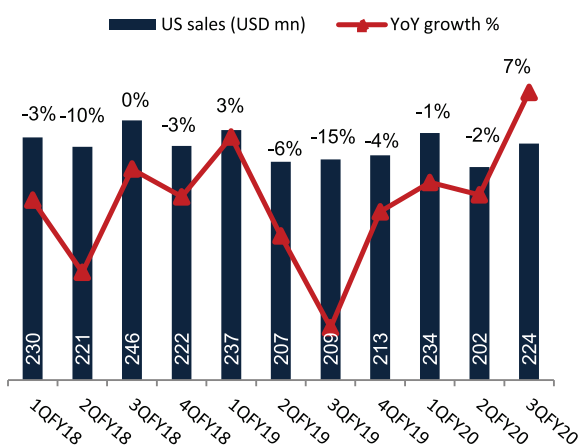


Exhibit: US sales and YoY growth

The US sales grew by 7% US\$ 224 on account of higher volumes in some of its key molecules



Operational Details

Fig in Rs Cr

GEOGRAPHY	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
North America	1607	1449	1590	1427	1483	1496	1632	1427	1600
Europe	201	171	202	192	203	191	240	276	309
India	613	614	607	686	674	651	696	751	764
Emerging Markets	590	550	664	749	774	701	730	828	920
PSAI	544	625	541	603	594	677	454	711	691
Proprietary products and others	252	126	116	141	122	302	91	809	101

REVENUE GR. %	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
North America	-3%	-6%	6%	0%	-8%	3%	3%	0%	8%
Europe	-7%	-17%	-3%	-21%	1%	12%	19%	44%	52%
India	3%	7%	30%	8%	10%	6%	15%	9%	13%
Emerging Markets	-1%	-9%	16%	36%	31%	27%	10%	10%	19%
PSAI	1%	16%	16%	7%	9%	8%	-16%	18%	16%
Proprietary products and others	145%	26%	10%	19%	-52%	139%	-21%	472%	-17%

REVENUE MIX%	3QFY18	4QFY18	1QFY19	2QFY19	3QFY19	4QFY19	1QFY20	2QFY20	3QFY20
North America	42%	41%	43%	38%	39%	37%	42%	30%	36%
Europe	5%	5%	5%	5%	5%	5%	6%	6%	7%
India	16%	17%	16%	18%	18%	16%	18%	16%	17%
Emerging Markets	16%	16%	18%	20%	20%	17%	19%	17%	21%
PSAI	14%	18%	15%	16%	15%	17%	12%	15%	16%
Proprietary products and others	7%	4%	3%	4%	3%	8%	2%	17%	2%

Financial Details

Balance Sheet

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Share Capital	85	85	85	83	83	83	83	83
Reserves	7,780	9,768	12,485	12,179	12,489	13,941	15,445	17,263
Networth	7,865	9,853	12,570	12,262	12,572	14,024	15,528	17,346
Debt	4,136	3,617	3,340	4,908	5,065	3,413	1,632	1,632
Other Non Current Liab	299	492	399	590	570	345	320	344
Total Capital Employed	12,001	13,470	15,910	17,170	17,637	17,436	17,160	18,978
Net Fixed Assets (incl CWIP)	5,280	5,906	7,335	10,255	10,439	10,125	9,064	10,386
Non Current Investments	0	146	330	683	465	334	334	334
Other Non Current Assets	424	670	925	1,195	1,142	897	1,404	1,414
Non Current Assets	5,704	6,721	8,590	12,133	12,046	11,356	10,802	12,134
Inventory	2,419	2,570	2,558	2,853	2,909	3,358	3,799	4,103
Debtors	3,325	4,101	4,125	3,799	4,053	3,987	4,892	5,283
Cash & Bank	2,301	1,872	492	387	264	223	420	547
Other Current Assets	2,281	3,333	4,619	2,646	3,273	3,543	2,948	3,061
Current Assets	10,326	11,877	11,794	9,684	10,498	11,110	12,059	12,995
Creditors	893	867	907	1,057	1,335	1,367	1,662	1,795
Provisions	816	1,144	529	513	439	479	496	535
Other Current Liabilities	2,021	2,624	2,640	2,488	2,564	2,839	3,223	3,477
Curr Liabilities	3,730	4,636	4,075	4,057	4,338	4,685	5,381	5,807
Net Current Assets	6,596	7,241	7,719	5,626	6,161	6,425	6,678	7,188
Total Assets	16,030	18,598	20,384	21,817	22,544	22,466	22,861	25,129

Income Statement

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
Revenue from Operation	13,415	15,023	15,568	14,196	14,281	15,448	17,396	18,801
Change (%)	13%	12%	4%	-9%	1%	8%	13%	8%
EBITDA	3251	3494	3585	2221	2351	3178	3858	3827
Change (%)	20%	7%	3%	-38%	6%	35%	21%	-1%
Margin (%)	24%	23%	23%	16%	16%	21%	22.2%	20.4%
Depr & Amor.	648	760	939	1027	1077	1135	1172	1237
EBIT	2603	2734	2646	1194	1274	2043	2686	2590
Int. & other fin. Cost	127	108	83	63	79	89	49	57
Other Income	170	274	295	172	155	338	593	232
EBT	2,646	2,900	2,859	1,302	1,350	2,292	3,230	2,764
Exp Item	-	-	-	-	-	-	1,320	-
Tax	683	563	751	297	438	386	66	608
Minority Int & P/L share of Ass.	-	-	23	35	34	44	61	61
Reported PAT	1,963	2,336	2,108	1,006	912	1,906	1,844	2,156
Adjusted PAT	1,963	2,336	2,131	1,041	947	1,950	1,905	2,217
Change (%)	29%	19%	-9%	-51%	-9%	106%	-2%	16%
Margin(%)	15%	16%	14%	7%	7%	13%	10.9%	11.8%

Financial Details

Key Ratios

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
ROE	25.0%	23.7%	17.0%	8.5%	7.5%	13.9%	12.3%	12.8%
ROCE	26.2%	24.2%	19.4%	9.3%	8.4%	12.6%	15.7%	13.6%
Asset Turnover	3	3	2	1	1	2	2	2
Debtor Days	91	100	97	98	104	95	103	103
Inv Days	66	63	60	74	75	80	80	80
Payable Days	25	21	21	27	34	32	35	35
Int Coverage	22	21	25	32	19	16	23	55
P/E	21.2	24.4	23.4	40.9	36.5	23.6	27.8	23.9
Price / Book Value	5.3	5.8	4.0	3.5	2.7	3.3	3.4	3.1
EV/EBITDA	13	16	14	19	16	15	14	14
FCF per Share	52	58	156	56	53	131	106	35
Div Yield	1%	1%	1%	1%	1%	1%	0.8%	0.8%

Cash Flow Statement

Fig in Rs Cr

Y/E March	FY14	FY15	FY16	FY17	FY18	FY19	FY20E	FY21E
PBT	2,646	2,900	2,675	1,554	1,350	2,292	3,290	2,825
(inc)/Dec in Working Capital	(1,005)	(1,484)	(18)	(525)	(897)	(577)	(1,341)	(368)
Non Cash Op Exp	648	760	971	1,027	1,077	1,135	1,172	1,237
Int Paid (+)	127	108	82	63	79	89	49	57
Tax Paid	(714)	(546)	(710)	(577)	(276)	(484)	(66)	(608)
others	269	786	1,047	603	469	(345)	(1,320)	-
CF from Op. Activities	1,970	2,524	4,048	2,144	1,803	2,870	1,785	3,143
(inc)/Dec in FA & CWIP	(1,083)	(1,532)	(1,388)	(1,223)	(929)	(696)	(27)	(2,559)
Free Cashflow	887	992	2,660	922	874	2,175	1,758	584
(Pur)/Sale of Inv	(2,509)	(3,701)	(5,516)	(4,972)	(6,829)	7,629	-	-
others	1,898	2,967	4,962	4,354	6,270	7,692	668	-
CF from Inv. Activities	(1,694)	(2,265)	(1,942)	(1,840)	(1,488)	(773)	641	(2,559)
inc/(dec) in NW				(1,569)				
inc/(dec) in Debt	390	34	(1,199)	1,631	88	(1,518)	(1,781)	-
Int. Paid	(116)	(109)	(92)	(92)	(133)	(161)	(49)	(57)
Div Paid (inc tax)	(298)	(359)	(411)	(339)	(399)	(400)	(400)	(400)
others	0	1	0	-	-	-	-	-
CF from Fin. Activities	(24)	(433)	(1,701)	(369)	(444)	(2,133)	(2,229)	(457)
Inc(Dec) in Cash	251	(174)	405	(65)	(129)	(35)	197	127
Add: Opening Balance	611	757	154	443	384	258	223	420
Closing Balance	862	583	559	378	254	223	420	547

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