

Dr. Reddy's Laboratories

18 September 2020

Reuters: REDY.BO; Bloomberg: DRRD IN

Dr. Reddy announce settlement of Revlimid Litigation with Bristol Myers

Dr. Reddy has announced that they have settled the ongoing Revlimid (lenalidomide) Litigation with Bristol Myers. The settlement gives DRL a license to sell limited volumes of gRevlimid from an undisclosed date which is post March 2022 (post settlement date with Natco Pharma). The details on volume and exact timelines are not disclosed. There are now 3 players – Natco Pharma, Dr. Reddy and Alvogen which have entered into a settlement agreement with the innovator.

Will Bristol Myers also settle with other Litigants and potential timelines: Other generic players like Cadila healthcare Sun Pharma, Hetero and Apotex are currently into litigation on Revlimid and there is a chance that we can see the innovator enter into a settlement with these players as well. In case of Natco and DRL, the settlement happened closer to trial hearing dates. It took about five years to reach trial hearing post litigation initiation. Assuming similar timelines for the other litigants, we expect a settlement to happen around FY24 time frame.

How much gRevlimid could be worth for Dr. Reddy: Although the detailed terms of the settlement are not disclosed, the settlement terms would at best be comparable to Natco or in the base case comparable to terms offered to Alvogen (upto high single digit volume share). Revlimid is a \$7bn drug and the sales continue to grow annually even at the existing revenue base. We assume that other generic players which are currently into litigation with innovator would also enter post FY24. Until then DRL, Natco and Alvogen would be the only players. Entry of other generic players (if settled) should not impact the potential opportunity for the incumbents as the innovator will reduce its share of volumes on a prorata basis. Assuming that DRL will garner an average 5% volume every year at an average 30% price discount over exclusivity period (FY23-FY27), we estimate the NPV of the opportunity at \$900mn which translates to Rs. 400 per share.

Upward revise our estimates, incorporate gVascepa in FY22, introduce FY23 estimates and Roll over target price: We slightly tweak our FY21 estimates, incorporate gVascepa launch into our FY22 earnings estimates and introduce FY23 estimates to our forecasts. We add about \$72mn on account of gVascepa and incorporate addition from gRevlimid in FY23 in our base case estimates. While DRL has an approval for gVascepa, they have not been able to launch it as they have some constraints on the manufacturing front. They expect to launch gVascepa over the next 3 to 9 months. We currently factor in an early FY22 launch. Vascepa represents a \$600mn market and we expect this to be a four player market (Hikma, Teva, Apotex and Dr. Reddy). We also expect the gVascepa market to expand (two fold by volume) on the current base as they have recently been granted approval for reduction in risk of cardiovascular morbidity and mortality in Hypertriglyceridemia patients. Vascepa would gain market share from Lovaza and fenofibrates which are other alternatives to the treatment of hypertriglyceridemia. We roll over our price target to average of FY22 and FY23 earnings and assign a 22x PE multiple. The higher multiple is to account for greater resilience in base earnings led by an improving base business in US, option value of vaccine deal with Russian direct investment fund, strong cash generation allows inorganic opportunities and potential upside from a scale up in China. Our revised target price on DRL stands at Rs. 5656 and recommend a buy rating at current market price.

Key Financials

Y/E March (Rsmn)	FY19	FY20	FY21E	FY22E	FY23E
Net sales	1,53,851	1,74,600	1,82,006	2,05,562	2,37,347
EBITDA	34,189	46,431	49,649	62,237	78,314
Net profit	18,795	19,498	27,014	36,538	48,797
EPS (Rs)	113.3	117.5	162.8	220.2	294.0
EPS growth (%)	91.7	3.7	38.5	35.3	33.6
EBITDA margin (%)	22.2	26.6	27.3	30.3	33.0
PER (x)	39.1	37.7	27.2	20.1	15.1
P/BV (x)	5.2	4.7	4.2	3.5	2.9
EV/EBITDA (x)	21.9	15.7	14.4	11.1	8.5
RoCE (%)	13.5	23.2	20.5	24.2	27.4
RoE (%)	14.1	13.2	16.3	19.0	21.4

Source: Company, Nirmal Bang Institutional Equities Research

BUY

Sector: Pharmaceuticals

CMP: Rs4,827

Target Price: Rs5,656

Upside: 17%

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Key Data

Current Shares O/S (mn)	166.2
Mkt. Cap (Rsbm/US\$bn)	802.5/10.9
52 Wk H / L (Rs)	4,850/2,495
Daily Vol. (3M NSE Avg.)	1,308,633

Price Performance (%)

	1 M	6 M	1 Yr
Dr Reddy's Labs.	6.8	80.9	75.9
Nifty Index	2.4	28.4	6.5

Source: Bloomberg

Exhibit 1: Change in Estimates

(Rsmn)	New estimates		Old estimates		Change (%)	
	FY21E	FY22E	FY21E	FY22E	FY21E	FY22E
Net sales	1,82,006	2,05,562	1,87,288	2,06,543	(2.8)	(0.5)
EBITDA	49,649	62,237	49,948	55,557	(0.6)	12.0
Margin (%)	27.3	30.3	26.7	26.9	61 bps	338 bps
PAT	27,014	36,538	27,236	31,595	(0.8)	15.6
Margin (%)	14.8	17.8	14.5	15.3	30 bps	248 bps
EPS	162.8	220.2	164.1	190.4	(0.8)	15.6

Source: Company, Nirmal Bang Institutional Equities Research

Financial statements
Exhibit 2: Income statement*

Y/E March (Rsmn)	FY19	FY20	FY21E	FY22E	FY23E
Net sales	153,851	174,600	182,006	205,562	237,347
% growth	8.3	13.5	4.2	12.9	15.5
Cost of Sales	70,421	80,591	81,995	88,117	93,982
R&D Expenditure	15,607	15,410	16,836	18,501	21,361
SG&A Expenditure	48,890	50,129	50,962	54,474	61,710
Impairment of Non-Current Assets	0	16,767	0	0	0
Other (Income) / Expense	(1,955)	(4,290)	(1,955)	(1,955)	(1,955)
Total expenditure	132,963	158,607	147,837	159,136	175,099
Operating Profit	20,888	15,993	34,169	46,426	62,248
% growth	75.3	(23.4)	113.6	35.9	34.1
Operating Profit margin (%)	13.6	9.2	18.8	22.6	26.2
Finance (Expense) / Income	1,117	1,478	1,608	1,930	2,316
Share of Profit in Equity Investments	438	561	729	1,021	1,378
Gross profit	83,430	94,009	100,011	117,445	143,365
% growth	9.3	12.7	6.4	17.4	22.1
Profit before tax	22,443	18,032	36,506	49,376	65,942
% growth	56.5	(19.7)	102.5	35.3	33.6
Tax	3,648	(1,466)	9,492	12,838	17,145
Effective tax rate (%)	16.3	(8.1)	26.0	26.0	26.0
Net profit	18,795	19,498	27,014	36,538	48,797
% growth	91.7	3.7	38.5	35.3	33.6
EPS (Rs)	113.3	117.5	162.8	220.2	294.0
% growth	91.7	3.7	38.5	35.3	33.6

*In IFRS format

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 4: Balance sheet

Y/E March (Rsmn)	FY19	FY20	FY21E	FY22E	FY23E
Equity	830	831	831	831	831
Reserves	139,367	154,157	175,855	206,544	248,908
Net worth	140,197	154,988	176,686	207,375	249,739
Net deferred tax liabilities	610	275	275	275	275
Short-term loans	12,125	16,441	32,634	15,133	17,473
Long-term loans	22,000	1,304	913	639	447
Other Non Current Liabilities	2,920	2,860	2,860	2,860	2,860
Liabilities	225,427	232,241	270,605	291,082	345,822
Intangible Assets and Goodwill	50,798	34,416	30,873	28,149	26,258
Net block	54,088	52,332	55,638	58,640	61,134
Other Non Current Assets	6,040	15,123	15,123	15,123	15,119
Inventories	33,579	35,066	37,277	42,101	48,611
Debtors	39,869	50,278	52,050	58,786	67,876
Cash	2,228	2,053	30,973	34,403	66,124
Loans and advances	12,536	13,802	14,387	16,249	18,762
Other current assets	26,289	29,171	34,284	37,630	41,937
Total current assets	114,501	130,370	168,971	189,170	243,311
Creditors	14,553	16,659	17,366	19,613	22,646
Other current liabilities	45,147	56,155	72,506	60,319	69,855
Total current liabilities	59,700	72,814	89,871	79,932	92,500
Net current assets	54,801	57,556	79,100	109,237	150,810
Total assets	225,427	232,241	270,604	291,082	345,822

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 3: Cash flow

Y/E March (Rsmn)	FY19	FY20	FY21E	FY22E	FY23E
PAT	18,795	19,498	27,014	36,538	48,797
(Inc.)/Dec in working capital	(6,110)	(7,256)	(4,942)	(9,090)	(12,110)
Cash flow from operations	12,685	12,242	22,073	27,448	36,688
Other income	(438)	(560)	(729)	(1,021)	(1,377)
Other expenses	3,648	(1,466)	9,492	12,838	17,152
Depreciation	12,400	12,471	14,751	14,790	14,687
Tax paid	(3,648)	1,466	(9,492)	(12,838)	(17,145)
Net cash from operations	24,647	24,153	36,094	41,218	50,005
Capital expenditure	(14,292)	(14,355)	(13,784)	(14,047)	(13,912)
Net cash after capex	10,355	9,798	22,310	27,170	36,093
Other investing activities	(1,736)	(485)	0	0	(4)
Cash from Financial Activities	(9,029)	(9,489)	6,610	(23,741)	(4,367)
Opening cash	2,638	2,228	2,053	30,973	34,403
Closing cash	2,228	2,053	30,973	34,403	66,124
Change in cash	(410)	(175)	28,920	3,429	31,721

Source: Company, Nirmal Bang Institutional Equities Research

Exhibit 5: Key ratios

Y/E March	FY19	FY20	FY21E	FY22E	FY23E
Profitability & return ratios					
EBITDA margin (%)	13.6	9.2	18.8	22.6	26.2
EBIT margin (%)	14.2	21.6	19.2	23.1	26.8
Net profit margin (%)	12.2	11.2	14.8	17.8	20.6
RoE (%)	14.1	13.2	16.3	19.0	21.4
RoCE (%)	13.5	23.2	20.5	24.2	27.4
Working capital & liquidity ratios					
Receivables (days)	95	94	103	98	97
Inventory (days)	162	155	161	164	176
Payables (days)	79	71	76	77	82
Current ratio (x)	1.9	1.8	1.9	2.4	2.6
Quick ratio (x)	1.4	1.3	1.5	1.8	2.1
Valuation ratios					
EV/sales (x)	4.9	4.2	3.9	3.4	2.8
EV/EBITDA (x)	21.9	15.7	14.4	11.1	8.5
P/E (x)	39.1	37.7	27.2	20.1	15.1
P/BV (x)	5.2	4.7	4.2	3.5	2.9

Source: Company, Nirmal Bang Institutional Equities Research

P/E Chart

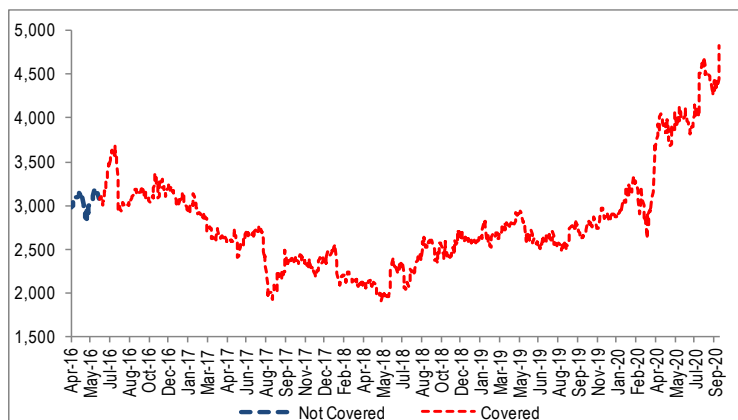


Source: Bloomberg, Company, Nirmal Bang Institutional Equities Research

Rating track

Date	Rating	Market price	Target price (Rs)
10 June 2016	Buy	3,160	3,950
27 July 2016	Buy	3,300	3,950
6 February 2017	Buy	3,142	3,950
15 May 2017	Buy	2,584	3,366
28 July 2017	Buy	2,620	3,020
1 November 2017	Buy	2,428	3,216
29 January 2018	Buy	2,508	3,077
23 May 2018	Buy	2,004	2,898
23 July 2018	Buy	2,059	2,898
27 July 2018	Buy	2,110	2,898
29 October 2018	Buy	2,405	3,122
4 February 2019	Accumulate	2,791	3,122
5 April 2019	Buy	2,772	3,348
20 May 2019	Buy	2,748	3,281
30 July 2019	Buy	2,653	3,281
23 September 2019	Accumulate	2,829	3,138
4 November 2019	Buy	2,755	3,138
28 January 2020	Accumulate	3,189	3,188
27 March 2020	Accumulate	2,945	3,333
23 April 2020	Sell	4,056	3,647
20 May 2020	Sell	3,911	3,647
30 July 2020	Sell	4,300	3,808
18 September 2020	Buy	4,827	5,656

Rating track graph



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Stock Ratings Absolute Returns

BUY > 15%

ACCUMULATE -5% to 15%

SELL < -5%

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