

ADD

TP: Rs 3,350 | ▼ 13%

DR REDDY'S LABS

Pharmaceuticals

08 May 2020

EIR for Srikakulam (CTO-VI) API unit

Event: Dr Reddy's Labs (DRRD) announced that it has received an EIR (establishment inspection report) from the USFDA for its Srikakulam (CTO-VI) API facility. This plant was last inspected in Feb'20 (warning letter status since Nov'15), wherein the FDA issued six observations. These observations are now classified under VAI (voluntary action indicated) status. The EIR implies closure of both the observations and the warning letter.

Implications: The site accounted for US\$ 100mn in end product sales (~4% of revenues) in FY16, which should have moderated to some extent in our view. Copaxone is one of the key products from the plant pending approval (CRL or complete response letter submission is in progress on the queries raised by USFDA on DMF). As the regulatory issues at CTO-VI have now been resolved, we believe supplies of new APIs and ANDAs that were held back would recommence.

DRRD should also be able to gradually increase sales for the current portfolio as backward linkages to key raw materials get restored, including supplies for products which were outsourced over the last five years. This would provide a greater cushion to margins.

View: Site clearance comes as good surprise to the street. However, we do not expect any material swing in our FY21/FY22 EPS estimates which are at Rs 158/Rs 186. Following the recent stock rally, valuations appear stretched and we see limited upside potential at the current P/E of 21x and EV/EBITDA of 13x on FY22E (close to the five-year mean). Considering the uncertain environment due to Covid-19, we will review our rating and target price once more clarity emerges after the Q4FY20 results.

Vivek Kumar

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Ticker/Price	DRRD IN/Rs 3,838
Market cap	US\$ 8.4bn
Shares o/s	166mn
3M ADV	US\$ 53.0mn
52wk high/low	Rs 4,094/Rs 2,351
Promoter/FPI/DII	27%/27%/18%

Source: NSE

KEY FINANCIALS

Y/E 31 Mar	FY20E	FY21E	FY22E
Total revenue (Rs bn)	174	185	203
EBITDA (Rs bn)	42	41	47
Adj. net profit (Rs bn)	28	26	31
Adj. EPS (Rs)	168.1	157.7	185.8
Adj. EPS growth (%)	56.0	(6.2)	17.9
Adj. ROAE (%)	19.1	15.7	16.1
Adj. P/E (x)	22.8	24.3	20.7
EV/EBITDA (x)	15.8	15.6	13.2

Source: Company, BOBCAPS Research

STOCK PERFORMANCE



Source: NSE

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Recommendations and Absolute returns (%) over 12 months

BUY – Expected return >+15%

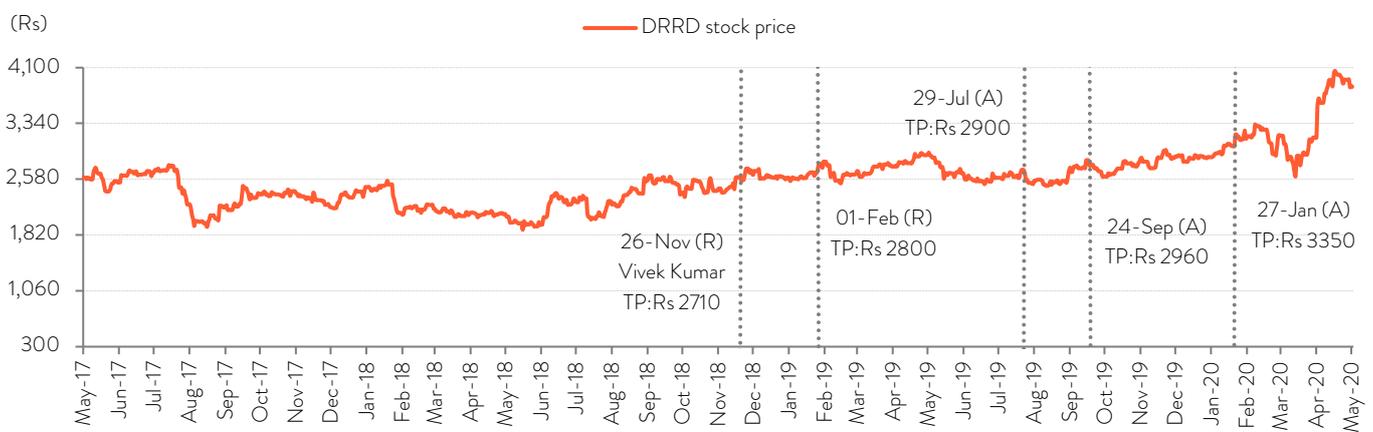
ADD – Expected return from >+5% to +15%

REDUCE – Expected return from -5% to +5%

SELL – Expected return <-5%

Note: Recommendation structure changed with effect from 1 January 2018 (Hold rating discontinued and replaced by Add / Reduce)

HISTORICAL RATINGS AND TARGET PRICE: DR REDDY'S LABS (DRRD IN)



Note: B – Buy, A – Add, R – Reduce, S – Sell

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