

# DR. REDDY'S LABORATORIES

## Overboard on guidance

India Equity Research | Pharmaceuticals



Dr. Reddy's (DRRD) Q3FY13 adjusted PAT of INR3.87bn was lower than INR4.7bn estimate. Revenue grew 3.5%YoY (core growth of 23% versus 32% estimated). EBITDA margin of 20.5% plunged 350bps QoQ, lower than estimated 23.0%, due to increase in fixed costs build in our estimate. Overall performance reflects lower execution overlapped by price erosion in base business and delayed approvals in US. DRRD is likely to miss its FY13 US sales guidance of USD800mn, which will partly spill over to FY14. Hence, we expect FY14 growth to improve due to the spillover effect. However, execution risk will loom over valuations. Maintain 'HOLD' with TP of INR1,951 (18x NTM EPS and assign NPV of INR42 for Para IVs).

### Weak US decelerates operating performance

DRRD's core sales (ex-Olanzapine base) grew 23%, while PBT surged 17% YoY due to lower margin of 20.5% (down 350bps QoQ). While India grew 12%, Russia/CIS reported strong growth of 26%. US declined 5% QoQ due to price erosion, which resulted in lower gross realisations. R&D cost of 7.1% of sales rose from 6.1% in Q2FY13.

### Propecia/MS ramp up in Toprol to boost US

Despite MS ramp up in Atorvastain (15% MS), Toprol, Montelukast etc., US sales at USD178mn were lower than USD187mn in Q2FY13 due to higher price erosion and lack of new approvals. However, with launch of Finasteride and ramp up in Toprol (15% MS from earlier 4-5%), US is likely to post USD220-230mn sales during Q4 and USD725mn during FY13E (7% below prior estimate). We expect 13% CAGR in US over FY13-15E.

### Revising down FY13-14E earnings on higher tax, R&D costs

We revise down our FY13E and FY14E EPS 4% and 2%, respectively, factoring in lower growth in US, higher R&D costs and higher tax rate. We expect some spill over of sales in US from approvals that will add USD30-50mn to FY14 sales. We thus expect earnings CAGR of 14% (12% base business) over FY13-15E versus earlier estimate of 11%.

### Outlook and valuations: Premium swing; maintain 'HOLD'

We believe DRRD's growth pace will moderate, which, coupled with execution risk, could shift valuation premium to pharma stocks that have strong growth visibility. We prefer Lupin over DRRD owing to the former's growth visibility (25% earnings CAGR).

#### Financials (Consolidated)

(INR mn)

Year to March	Q3FY13	Q3FY12	% change	Q2FY13	% change	FY12	FY13E	FY14E
Net revenue	28,652	27,692	3.5	28,809	(0.5)	97,139	116,115	132,182
EBITDA	5,878	8,689	(32)	6,910	(15)	20,515	21,481	24,922
Adj. net profit	3,870	4,941	(21.7)	4,599	(15.9)	14,556	16,774	19,404
Adj. diluted EPS	22.9	29.3	(21.7)	27.2	(15.9)	85.6	98.7	114.2
Diluted P/E (x) on recurring EPS						28.5	20.8	17.6
EV/EBITDA (x)						13.7	12.6	10.7
ROAE (%)						28.1	26.4	25.2

#### EDELWEISS 4D RATINGS

Absolute Rating	HOLD
Rating Relative to Sector	Performer
Risk Rating Relative to Sector	Medium
Sector Relative to Market	Underweight

#### MARKET DATA (R: REDY.BO, B: DRRD IN)

CMP	: INR 1,874
Target Price	: INR 1,951
52-week range (INR)	: 1,970 / 1,526
Share in issue (mn)	: 169.8
M cap (INR bn/USD mn)	: 318/ 5,900
Avg. Daily Vol.BSE/NSE('000)	: 352.0

#### SHARE HOLDING PATTERN (%)

	Current	Q2FY13	Q1FY13
Promoters *	25.6	25.6	25.6
MF's, FI's & BK's	14.0	15.2	14.4
FII's	26.2	24.5	25.9
Others	34.3	34.7	34.1
* Promoters pledged shares (% of share in issue)	:		Nil

#### PRICE PERFORMANCE (%)

	Stock	Nifty	EW Pharma Index
1 month	0.6	(1.0)	(0.4)
3 months	5.7	4.4	11.3
12 months	13.7	11.8	50.0

#### Manoj Garg

+91 22 6623 3302  
manoj.garg@edelweissfin.com

#### Perin Ali

+91 22 6620 3032  
perin.ali@edelweissfin.com

February 14, 2013

Table 1: Actual Versus Estimates

(INR mn)

	Q3FY13 Actual	YoY (%)	Edel estimates	YoY (%)	Deviation from Actual (%)	Comments
Net Revenue	28,652	3.5	30,608	10.5	(6.4)	Lower growth in US, EU and PSAI business
Cost of revenue	13,559	22.0	14,263	28.3	(4.9)	
Gross profit	15,092	(8.9)	16,344	(1.4)	(7.7)	
Gross margin (%)	52.7		53.4			Margins impacted from price erosion in key products in US
S,G&A	7,189	12.8	7,346	15.3	(2.1)	
R&D	2,025	33.8	1,867	23.3	8.5	Increased to 7.1% of sales from increased investments into biosimilars and complex products in US
EBITDA	5,878	(32.4)	7,132	(17.9)	(17.6)	
EBITDA margin (%)	20.5		23.3			Lower margins from increase in R&D costs and lower gross margins
Depreciation	971	8.0	990	10.1	(1.9)	
Amortization	411	0.7	450	10.3	(8.7)	
Total operating expenses	10,596	15.3	10,653	15.9	(0.5)	
Operating profit	4,496	(39.1)	5,692	(22.9)	(21.0)	
Operating margin (%)	15.7		18.6			
Other income	233.1	41.4	200.0	21.4	16.6	
Net finance expense (income)	(13)	(82.0)	20	(82.0)	(82.0)	
PBT	4,742	(36.2)	5,872	(21.0)	(19.2)	
Income tax expense	827	(68.4)	1,174	(55.1)	(29.6)	Tax rate lower than estimated; guidance of 20-22% for FY13
Tax rate (%)	17.4		20.0			
PAT	3,916	(18.7)	4,697	(2.5)	(16.6)	
Share of profit(loss) in investees	31	22.7	28	9.8	11.8	
Extraordinaries (incl fx gain/ loss)	314.0		-			AP fuel surcharge levied during the quarter
Net profit	3,633	(29.2)	4,725	(7.9)	(23.1)	
Adjusted PAT	3,870	(21.7)	4,725	(4.4)	(18.1)	
Adjusted EPS	22.9	(21.7)	28.0	(4.4)	(18.1)	

Source: Company, Edelweiss research

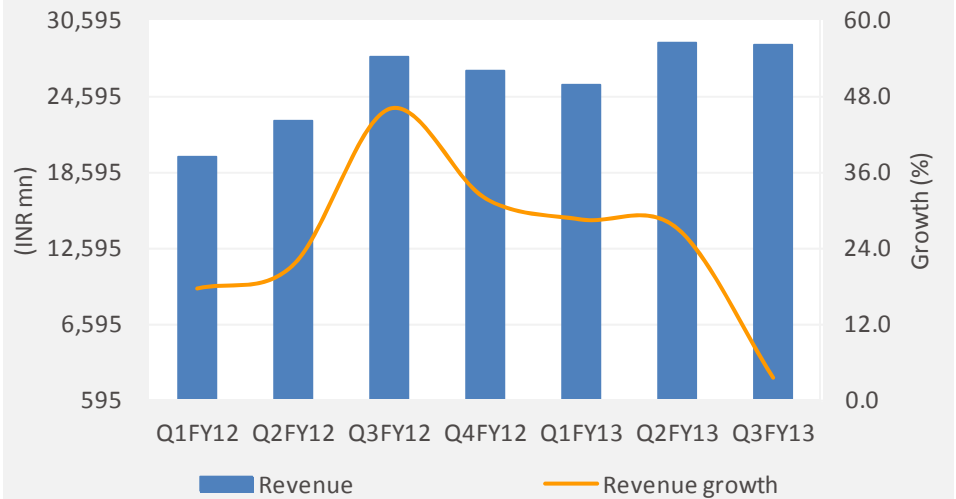
Table 2: Revenue mix by segment - Consolidated

Year to March	Q3FY13	Q3FY12	% change	Q2FY13	% change	Comments
Global generics	20,828	21,287	(2.2)	20,103	3.6	
North America	9,243	11,114	(16.8)	9,270	(0.3)	Lack of new launches and price erosion in base business; Olanzapine sales of USD99mn last year resulted in negative growth
Europe	1,931	2,426	(20.4)	1,777	8.7	
India	3,718	3,333	11.6	3,879	(4.2)	Growth to track overall market
Russia & CIS	4,380	3,317	32.0	3,841	14.0	26% growth in constant currency; strong ramp-up in Russia including other CIS markets such as Ukraine
Others	1,556	1,097	41.8	1,336	16.5	
PSAI	7,127	5,563	28.1	7,876	(9.5)	
Proprietary products/Others	696	842	(17.3)	830	(16.1)	
<b>Net Sales</b>	<b>28,651</b>	<b>27,692</b>	<b>3.5</b>	<b>28,809</b>	<b>(0.5)</b>	

Source: Company, Edelweiss research

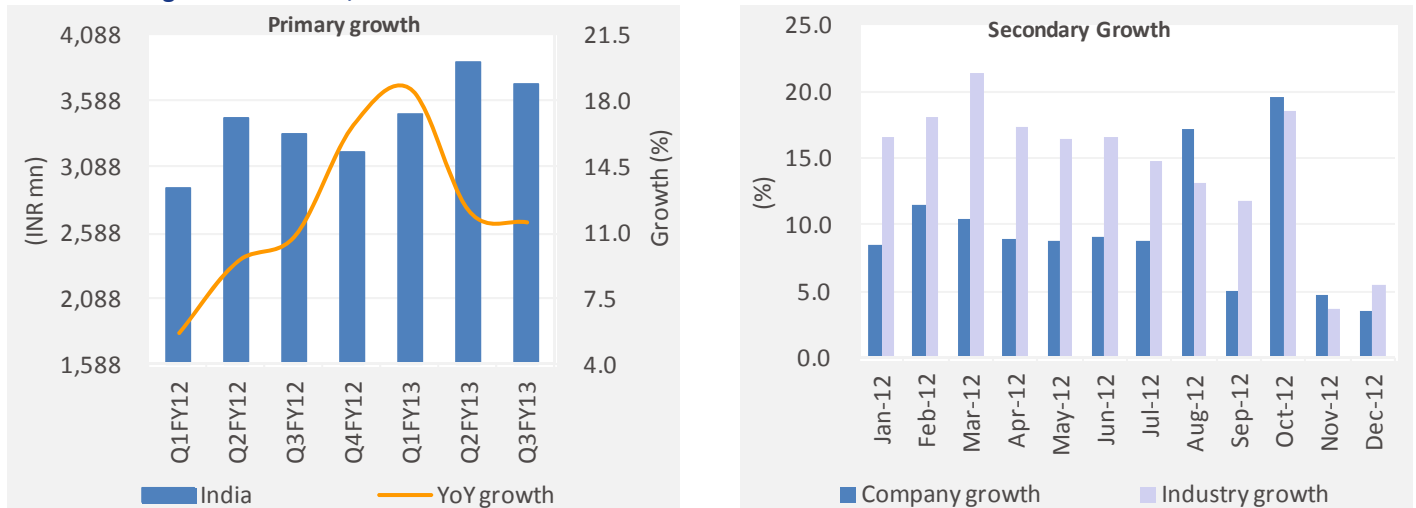
Slower ramp-up versus the strong growth expectations build for H2FY13; stated guidance of sales will be unmet and some spill over will benefit growth over FY14

**Chart 1: Revenue growth slowed on back of higher base and slower ramp-up in US**



Source: Company, Edelweiss research

**Chart 2: India growth stabilized; traction to move in-line with market**



Source: AIOCD, Edelweiss research

**Table 3: Top 10 brands performance – flattish**

Brands	Therapy	% of total	Market share	Dec-12		Q3FY13	
				Growth rate	Cont. to growth	Growth rate	Cont. to growth
Omez	Acute	7.6	11.8	(5.2)	(11.9)	0.8	0.8
Stamlo	Chronic	4.4	16.2	(0.6)	(0.8)	6.8	3.4
Nise	Acute	3.9	15.5	(1.8)	(2.0)	1.3	0.7
Omez D	Acute	3.6	45.7	7.8	7.5	14.6	5.6
Stamlo Beta	Chronic	2.8	5.3	(8.3)	(7.3)	(3.9)	(1.3)
Razo	Acute	3.0	-	11.6	8.8	18.3	5.6
Econorm	Acute	2.8	-	15.8	10.9	27.2	6.5
Mintop	Chronic	2.4	38.5	(14.7)	(11.9)	3.1	1.0
Atocor	Chronic	2.8	56.6	(0.7)	(0.6)	(0.3)	(0.1)
Razo D	Acute	2.6	100.0	19.5	12.1	25.1	6.3
<b>Total</b>		<b>36.0</b>		<b>0.5</b>	<b>4.9</b>	<b>7.0</b>	<b>28.5</b>

Source: AIOCD, Edelweiss research

**Table 4:Therapy wise Performance- strong growth in respiratory and dema segment**

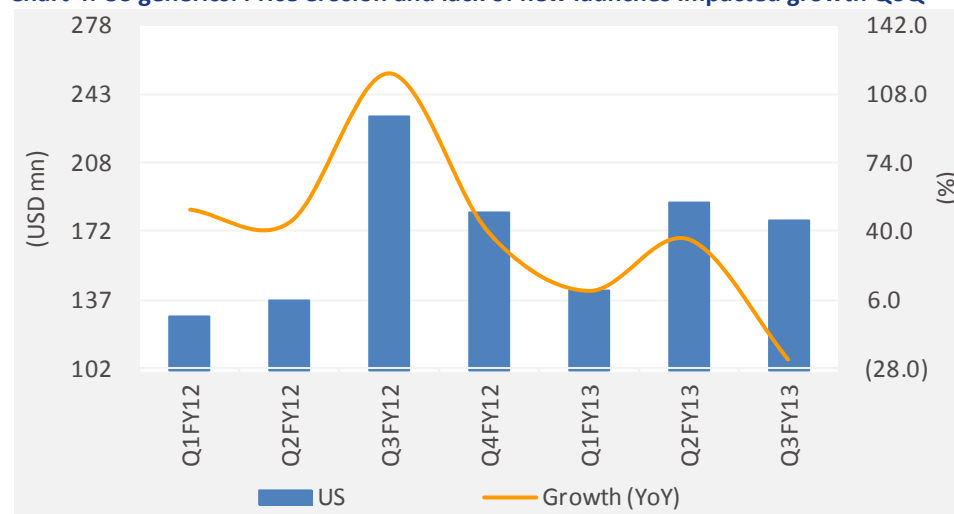
Therapeutic area	% of total	Market share	Dec-12			Q3FY13				
			Dr. Reddy's growth	Industry Growth	Cont. to growth	Dr. Reddy's growth	Industry Growth	Cont. to growth		
Gastro	24.6	4.8	6.4	4.0	↑	41.9	13.1	8.1	↑	34.1
CVS	20.3	3.0	0.4	11.0	↓	2.0	4.3	11.7	↓	9.8
Pain Management	9.2	2.6	4.0	1.3	↑	10.1	6.9	4.2	↑	7.5
Anti-Infectives	8.2	1.0	(5.2)	0.3	↓	(12.9)	5.8	8.0	↓	5.7
Dermatology	7.4	2.8	(3.3)	5.9	↓	(7.1)	21.0	9.0	↑	17.1
Respiratory	7.2	1.7	13.1	0.7	↑	23.7	17.4	8.0	↑	12.5
Diabetics	6.7	2.0	10.9	9.6	↑	18.7	10.3	13.8	↓	7.3
Urology	4.4	1.1	9.2	9.1	↑	10.6	9.1	10.8	↓	4.2
Multi-vitamins	4.0	5.7	(7.1)	5.2	↓	(8.7)	3.9	8.9	↓	1.9
<b>Chronic cont.</b>	<b>26.9</b>					<b>20.8</b>				<b>17.1</b>

Source: AIOCD, Edelweiss research

NAM at USD178mn grew 32% (ex-Olanzapine);

MS improved in Atorvastatin (15%), Metoprolol (15%) and Montelukast; however it was a subdued quarter in terms of approvals, which could not offset compression in prices of couple of large products

**Chart 4: US generics: Price erosion and lack of new launches impacted growth QoQ**



Source: Company, Edelweiss research

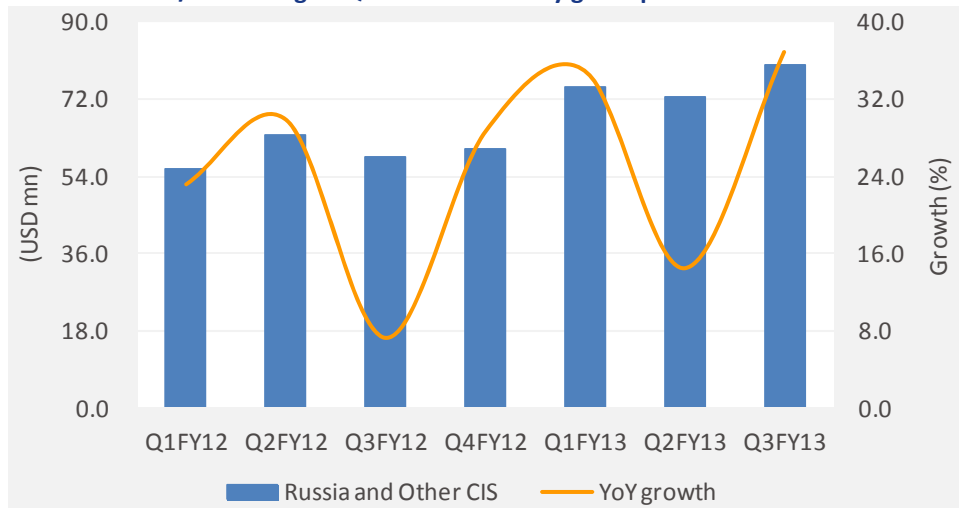
**Table 5: Key product opportunities and US sales projections over FY13-15**

USD mn	FY10	FY11	FY12	FY13E	FY14E	FY15E				
Core sales	283	355	459	538	696	762				
New launches	67	72	104	79	158	66				
No of products launched	12	14	16	14	11	10				
Key launches			Allegra OTC	14	Olanzapine	11	Singulair	13	Copaxone	38
			Augumentin	40	Quetiapine	9	Diovan	7	Dacogen	11
			Lansoprazole	38	Geodon	12	Propecia	7	Xeloda	10
			Lotrel	11	Clopidogril	15	Dacogen	7	Cymbalta	6
					Vidaza	9	Vidaza	41	Nexium	6
					Toporol XL	14	Toporol XL	42		
					Lipitor	16				
					Montelukast (granules)	9				
							Non disclosed limited competition	10	Non disclosed limited competition	10
	Para IV/ one-offs	60	40	153	82	21	65			
Key one-offs			Geodon	13	Geodon	26				
			Zyprexa	100	Propecia	16	Propecia	8		
					Boniva	1	Telmisartan	13	Telmisartan	7
					Calrinex	5			Lunesta	8
			Tacrolimus	40	Tacrolimus	34			Avelox	30
								Vimovo	18	
								Namenda	3	
Fondaparinux	-	-	14	51	51	48				
Omeprazole OTC	7	31	44	52	55	53				
<b>Total US sales</b>	<b>350</b>	<b>426</b>	<b>670</b>	<b>724</b>	<b>823</b>	<b>930</b>				
Growth (%)		21.6	57.3	8.0	13.7	13.0				

Source: Company, Edelweiss research

Apart from US, Russia / CIS would emerge as key pillars of future growth

**Chart 5: Russia / CIS strong as Q3 was a seasonally good quarter**



Source: Company, Edelweiss research

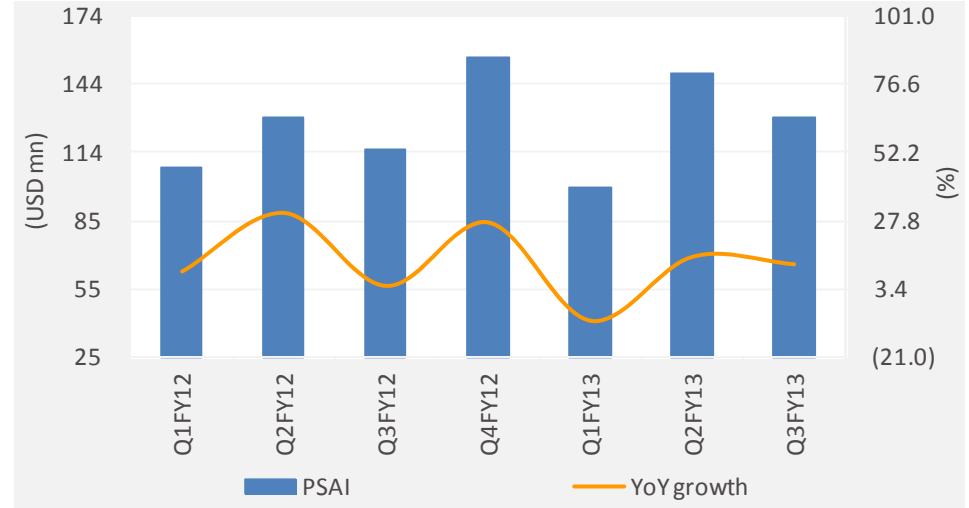
Expect higher traction on back of few high value orders

Higher S,G&A – OTC launched side coupled with some rationalization in Germany

GUDUFA fees of USD1mn included in S,G&A costs

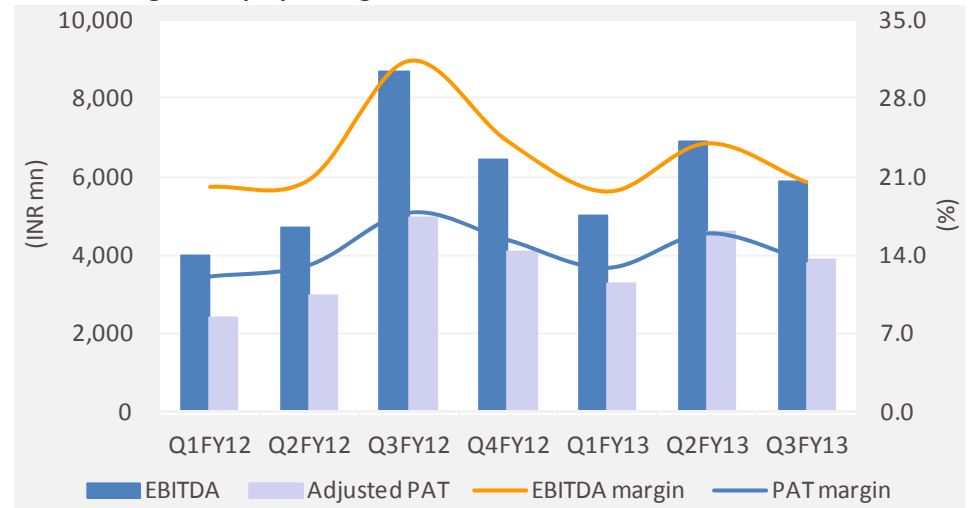
R&D costs increased to 7.1% from 6.1% in Q2FY13; Management expects R&D to increase to north of 7% on back of clinical development of biosimilars, complex injectibles and niche products in US

**Chart 6: PSAI declined QoQ due to pricing pressure in couple of products**



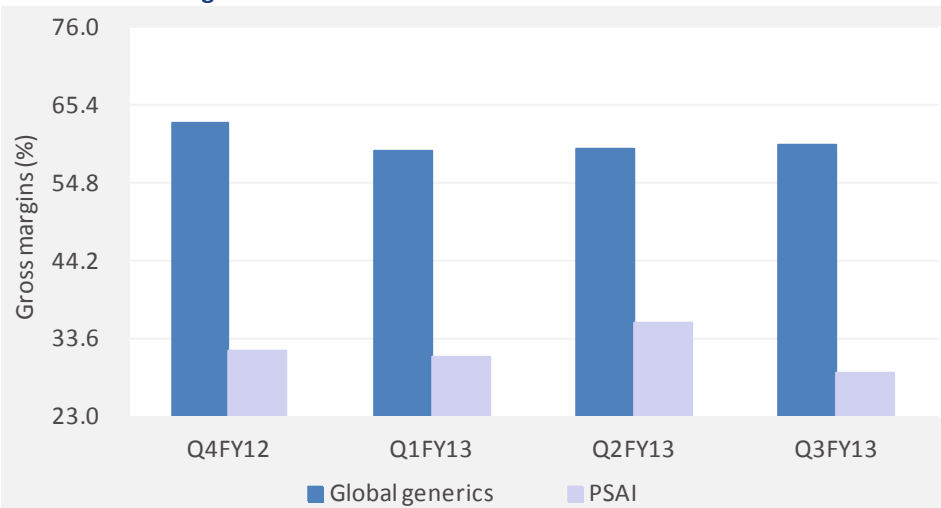
Source: Company, Edelweiss research

**Chart 7: Margins ramp-up during could not be sustained**



Source: Company, Edelweiss research

**Chart 8: Gross margins declined in PSAI business due to lower mix**



Source: Company, Edelweiss research

**Other key highlights from the Earnings call for Q3FY13**

- DRRD reported revenue of USD422mn (3% YoY); excl base of Olanzapine sales of USD99mn Normalized growth was 23% during the quarter
- Global generics at USD380mn; Ex-olanzapine growth of 24%YoY
- **US generics** at USD178mn (versus USD187mn in Q2FY13) depicted growth of 32% YoY (ex-olanzapine). Price erosion in base business and lack of new launches impacted growth in US QoQ. DRRD saw MS improvement in Atorvastatin, Metoprolol and Montelukast, however it faced delay in regulatory approvals which could not replace price erosion in key products  
  
MS of Key products: Metoprolol MS has ramped-up from 4-5% to 15% but revenue has been accrued form January, hence the same is not reflected during the quarter; Lasoprazole Rx – price erosion seen post incremental competition from entry of two competitors; Atorvastatin – DRRD is holding 15% MS; Finasteride launch - MS of 70%
- Going forward, next quarter to likely to benefit from new launches
- **India** reported satisfactory growth of 12% (MAT growth at 14.5%). Biosimilars growth in India has been strong and management expects it to scale-up to INR1bn by end FY13
- **Russia/CIS** depicted strong growth of 26% (constant currency) as Q3 has been a seasonally strong quarter; CIS markets are ramping-up and depicted strong growth
- Gross Margin at 53% led by Global generics - 60% and PSAI 29%, respectively
- **R&D spend** – expect to increase going forward (7% and above) on back of clinical development of biosimilars; **The** external R&D partnerships, Octopus acquisition, complex injectibles, niche products, biosimilars are peptides as few areas that company is working on and it aims to have incrementally 30% of filings in unique and complex molecules
- **Capex guidance** - YTD INR5bn
- Effective tax rate at 20-22%; current quarter tax at 19%
- WC increased by USD24mn, in-line with increase in sales; Capex for the quarter at USD27mn
- Hedges at USD600mn around USD/INR rate of 55-57; BS hedges of USD408mn

## Financial snapshot

(INR mn)

Year to March	Q3FY13	Q3FY12	% change	Q2FY13	% change	YTD13	FY13E	FY14E
Net revenues	28,652	27,692	3.5	28,809	(0.5)	82,866	116,115	132,182
Cost of revenue	13,559	11,117	22.0	13,504	0.4	38,929	53,297	60,177
Gross profit	15,092	16,575	(8.9)	15,305	(1.4)	43,938	62,818	72,005
SG&A	7,189	6,371	12.8	6,637	8.3	20,808	29,835	33,977
R&D	2,025	1,514	33.8	1,758	15.2	5,347	7,664	8,988
Amortization expenses	411	408	0.7	433	(5.1)	1,244	1,642	1,762
Other expenses	233	165	41.4	396	(41.2)	848	1,040	1,000
Total expenditure	10,596	9,192	15.3	9,771	8.4	30,209	42,979	48,845
EBITDA	5,878	8,689	(32.4)	6,910	(14.9)	17,783	21,481	24,922
EBITDA margin	20.5	31.4		24.0		21.5	18.5	18.9
Depreciation	971	899	8.0	943	3.0	2,810	3,838	4,118
Net finance expense	(13)	111	NA	(33)	NA	(242)	(67)	(432)
Profit before tax	4,742	7,436	(36.2)	5,963	(20.5)	14,819	20,946	24,591
Tax	827	2,617	(68.4)	1,392	(40.6)	2,890	4,041	5,287
Core profit	3,916	4,819	(18.7)	4,571	(14.3)	11,929	16,905	19,304
Extraordinary items	314	(285)	(210.2)	525	(40.1)	742	(19)	-
Share of profit(loss) in investees	31	26	22.7	28	10.2	79	-	-
Net profit	3,633	5,130	(29.2)	4,074	(10.8)	11,266	16,924	19,304
Adjusted net profit	3,870	4,941	(21.7)	4,599	(15.9)	11,731	16,774	19,404
Adj. EPS (INR)	22.9	29.3		27.2		69.5	98.7	114.2

## As % of net revenues

Cost of revenue	47.3	40.1		46.9		47.0	45.9	45.5
Gross profit	52.7	59.9		53.1		53.0	54.1	54.5
SG&A	25.1	23.0		23.0		25.1	25.7	25.7
R&D	7.1	5.5		6.1		6.5	6.6	6.8
Total expenses	37.0	33.2		33.9		36.5	37.0	37.0
Operating profit	15.7	26.7		19.2		16.6	17.1	17.5
Reported net profit	12.7	18.5		14.1		13.6	14.6	14.6
Tax rate	17.4	35.2		23.4		19.5	19.3	21.5



### Company description

Promoted by Dr. K Anji Reddy, Dr. Reddy's Laboratories (DRRD) is a professionally managed company with revenue of USD 2bn in FY12. Operating in 40 plus countries, revenue from international operations has gone up to 84% currently from 40% in FY08 with US/Russia contributing 40% of FY12 sales. The company has set itself an internal target of USD 2.5 bn revenue and ROCE of 30% by FY13E. The company's key strength has been its vertical integration through its Pharmaceutical Services & Active Ingredients (PSAI) operations and 16 manufacturing bases (10 USFDA approved) which enable it to have one of the best gross margin ratios in the Indian pharmaceutical industry. This is actively supported by an extensive R&D programme which spans CRAMs to drug discovery. It also has one of the deepest pipelines of bio-similars amongst leading global generic companies, addressing global brand sales of USD30bn.

### Investment theme

DRRD's base business is expected to grow at 12% CAGR in FY13-15E, on back of 12% CAGR in US core sales. Domestic formulation growth is expected to post ~12.5% CAGR, while Russian operations are expected to post 14% CAGR in FY13-15E. US is likely to report strong growth in FY12/13E, driven by strong Para IV as well as limited competition products such as Fondaparinux, Olanzapine, Allegra 24D OTC, among others. However, beyond, FY13, we expect US revenue to come down to 11.6% over FY13-15, because of higher base effect and fewer block buster opportunities.

### Key risks

- Pricing policy impact is expected to be 2.8% on FY14E earnings
- Slow ramp-up on new launches in US.
- Delay in key approvals.

## Financial Statements

### Key Assumptions

Year to March	FY12	FY13E	FY14E	FY15E
<b>Macro</b>				
GDP(Y-o-Y %)	6.5	5.5	6.5	7.0
Inflation (Avg)	8.8	7.8	6.0	6.0
Repo rate (exit rate)	8.5	7.5	6.8	6.0
USD/INR (Avg)	47.9	54.5	54.0	52.0
<b>Sector</b>				
India pharma market growth (Y-o-Y) %	16.0	14.1	13.0	15.0
<b>Company</b>				
India sales (INR mn)	12,931	14,695	16,600	19,055
% change	10.6	13.6	13.0	14.8
Gastro Intestinal	3,235	3,753	4,316	4,963
% change	13.2	16.0	15.0	15.0
Cardiovascular	2,771	3,103	3,538	4,068
% change	16.0	12.0	14.0	15.0
Pain management	1,318	1,450	1,624	1,852
% change	(6.8)	10.0	12.0	14.0
Anti-infectives	1,017	1,139	1,276	1,442
% change	(6.5)	12.0	12.0	13.0
Dermatology	852	1,005	1,186	1,400
% change	31.6	18.0	18.0	18.0
US generics (USD mn)	670	724	823	930
Growth (YoY)%	57.3	8.0	13.7	13.0
US base business	499	572	696	762
No of launches	16	14	11	10
Fondaparinaux	14	51	51	48
Omeprazole OTC	44	52	55	53
Para IV and one-offs	113	48	21	65
Russia and CIS growth (YoY) %	22.4	24.0	19.2	17.5
Top 5 brands	23	13	13	13
Others	57	49	30	24
PSAI growth (YoY) %	13.6	9.4	6.3	11.6
EBITDA margins (%)	24.9	21.8	22.0	22.3
India	25.0	24.9	25.0	0.3
Russia	27.0	27.0	26.0	0.3
US (Base business)	25.0	25.0	25.0	0.2
Para-IV/FTFs	80.0	60.0	80.0	0.8
ROW	24.0	24.0	25.0	0.3
PSAI	13.3	12.3	12.3	0.1
R&D (% of sales)	6.1	6.6	6.8	7.0
USD/INR (Avg)	47.6	53.0	54.0	52.0
Capex (USD mn)	207	154	153	171
Net debt to equity ratio(x)	0.3	0.1	(0.0)	(0.1)

### Income statement

(INR mn)

Year to March	FY12	FY13E	FY14E	FY15E
Income from operations	97,139	116,115	132,182	146,895
Materials costs	43,432	53,297	60,177	66,323
R&D Cost	5,911	7,664	8,988	10,283
Total SG&A expenses	27,282	33,673	38,095	41,968
EBITDA	20,515	21,481	24,922	28,321
Depreciation and amortisation	2,626	1,642	1,762	1,881
EBIT	17,889	19,839	23,159	26,441
Other income	365	1,059	1,000	1,000
Interest expenses	603	(67)	(432)	(647)
Profit before tax	17,651	20,965	24,591	28,087
Provision for tax	4,204	4,041	5,287	6,460
Net profit	13,447	16,924	19,304	21,627
Extraordinary income/ (loss)	(904)	(761)	-	-
Profit After Tax	14,351	17,685	19,304	21,627
Adjusted PAT	14,556	16,774	19,404	21,727
Diluted EPS (INR)	85.6	98.7	114.2	127.8
Recurring EPS (INR) fully diluted	64.3	88.3	104.4	110.6
CEPS (INR)	94.8	109.5	124.2	138.6
Dividend per share (INR)	16.0	23.1	26.7	29.9

### Common size metrics

Year to March	FY12	FY13E	FY14E	FY15E
Materials costs	44.7	45.9	45.5	45.1
R & D cost	6.1	6.6	6.8	7.0
Operating margins	21	19	19	19
Net profit margins	13.9	14.6	14.6	14.8

### Growth ratios (%)

Year to March	FY12	FY13E	FY14E	FY15E
Revenues	28.6	19.5	13.8	11.1
EBITDA	51.4	4.7	16.0	13.6
Net profit	31.3	15.2	15.7	12.0
EPS	16.2	37.4	18.2	5.9

Balance sheet		(INR mn)			
As on 31st March	FY12	FY13E	FY14E	FY15E	
Equity capital	848	848	848	848	
Reserves & surplus	56,596	68,834	83,597	100,140	
Shareholders funds	57,444	69,682	84,445	100,988	
Borrowings	32,210	27,210	22,210	17,210	
Deferred tax (net)	(833)	(833)	(833)	(833)	
Other term liabilities	1,059	1,059	1,059	1,059	
<b>Sources of funds</b>	<b>89,880</b>	<b>97,118</b>	<b>106,881</b>	<b>118,424</b>	
Net block	33,246	35,908	38,290	40,895	
Intangible assets	13,529	11,887	10,124	8,244	
Investments	785	785	785	785	
Cash and equivalents	18,152	25,062	30,056	37,072	
Inventories	19,352	22,269	25,350	28,172	
Sundry debtors	25,339	26,086	29,696	33,001	
Other current assets	7,109	7,109	7,109	7,109	
Total current assets	69,952	80,525	92,210	105,353	
Sundry creditors and others	25,660	30,015	32,556	34,880	
Provisions	1,973	1,973	1,973	1,973	
Total current liabilities &	27,633	31,988	34,529	36,853	
Net current assets	42,320	48,538	57,681	68,500	
<b>Uses of funds</b>	<b>89,880</b>	<b>97,118</b>	<b>106,881</b>	<b>118,424</b>	
Book value per share (INR)	338.8	410.9	497.9	595.5	

Free cash flow		(INR mn)			
Year to March	FY12	FY13E	FY14E	FY15E	
Net profit	14,351	17,685	19,304	21,627	
Depreciation	2,626	1,642	1,762	1,881	
Others	3,628	2,316	4,118	4,395	
Gross cash flow	20,605	21,643	25,184	27,903	
Less: Changes in WC	5,092	(691)	4,150	3,802	
Operating cash flow	15,513	22,335	21,034	24,100	
Less: Capex	9,858	8,142	8,262	8,881	
<b>Free cash flow</b>	<b>5,655</b>	<b>14,192</b>	<b>12,772</b>	<b>15,220</b>	

Cash flow metrics		FY12	FY13E	FY14E	FY15E
Year to March					
Operating cash flow		15,513	22,335	21,034	24,100
Investing cash flow		(8,337)	(6,500)	(6,500)	(7,000)
Financing cash flow		5,629	(8,925)	(9,541)	(10,084)
Net cash flow		12,805	6,910	4,994	7,016
Capex		(9,858)	(8,142)	(8,262)	(8,881)
Dividends paid		(2,728)	(3,925)	(4,541)	(5,084)

Profitability & efficiency ratios		FY12	FY13E	FY14E	FY15E
Year to March					
ROAE (%)		28.1	26.4	25.2	23.4
ROACE (%)		30.4	30.2	33.8	36.2
Inventory day		149	143	144	147
Debtors days		81	81	77	78
Payable days		198	191	190	186
Cash conversion cycle (days)		32	33	32	40
Current ratio		2.5	2.5	2.7	2.9
Debt/EBITDA		1.6	1.3	0.9	0.6
Debt/Equity		0.6	0.4	0.3	0.2
Adjusted debt/equity		0.6	0.4	0.3	0.2

Operating ratios		FY12	FY13E	FY14E	FY15E
Year to March					
Total asset turnover		1.2	1.2	1.3	1.3
Fixed asset turnover		3.1	3.3	3.6	3.7
Equity turnover		1.9	1.8	1.7	1.6

Valuation parameters		FY12	FY13E	FY14E	FY15E
Year to March					
Y-o-Y growth (%)		16.2	37.4	18.2	5.9
Core EPS (INR)		64.3	88.3	104.4	110.6
Diluted PE (x)		28.5	20.8	17.6	16.6
Price/BV (x)		5.5	4.6	3.8	3.1
EV/Sales (x)		3.4	2.8	2.3	2.0
EV/EBITDA (x)		13.7	12.6	10.7	9.1
Dividend yield (%)		0.9	1.2	1.4	1.6
Market Capitalisation		318,534	318,534	318,534	318,534

Peer comparison valuation

Name	Market cap (USD mn)	Diluted PE (X)		EV/EBITDA (X)		ROAE (%)	
		FY13E	FY14E	FY13E	FY14E	FY13E	FY14E
Dr.Reddys Laboratories	5,902	20.8	17.6	12.6	10.7	26.4	25.2
Cadila Healthcare	2,814	24.6	19.1	15.0	12.1	22.0	23.8
Cipla	5,685	20.1	18.5	13.4	12.2	19.2	17.6
Lupin	4,899	21.0	18.2	12.6	9.8	27.9	28.8
Sun Pharmaceuticals Industries	14,939	26.7	22.4	15.3	13.8	26.7	24.6
Median	-	20.8	18.5	14.1	12.1	26.7	24.6
AVERAGE	-	21.3	18.2	14.1	12.0	24.6	24.0

Source: Edelweiss research

## Additional Data

### Directors Data

Dr. K. Anji Reddy	Chairman	G V Prasad	Vice Chairman and Chief Executive Officer
Satish Reddy	Managing Director & Chief Operating Officer	Dr. Omkar Goswami	Independent and non whole time director
Ravi Bhoothalingam	Independent and non whole time director	Dr. Bruce LA Carter	Independent and non whole time director
Anupam Puri	Independent and non whole time director	Ms.Kalpana Morparia	Independent and non whole time director
J.P. Moreau	Independent and non whole time director	Sridar Iyengar	Independent and non whole time director
Dr. Ashok Ganguly	Independent and non whole time director		

Auditors - B S R & Co., Chartered Accountants, and KPMG India

*\*as per last annual report*

### Holding – Top10

	Perc. Holding		Perc. Holding
Genesis Investment Management LLP	3.16	Life Insurance Corp. of India	2.44
Matthews International Capital Management LLC	0.94	The Vanguard Group, Inc.	0.81
JF Asset Management Ltd.	0.80	OppenheimerFunds, Inc.	0.60
UTI Asset Management Co. Ltd.	0.58	Hansberger Global Investors, Inc.	0.54
BlackRock Fund Advisors	0.42	Vontobel Asset Management, Inc.	0.42

*\*as per last available data*

### Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
No Data Available				

*\*in last one year*

### Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
No Data Available			

*\*in last one year*

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Apollo Hospitals Enterprise	HOLD	None	None	Aurobindo Pharma	BUY	SP	H
Cadila Healthcare	BUY	SO	L	Cipla	BUY	SO	L
Divi's Laboratories	BUY	SP	M	Dr.Reddys Laboratories	HOLD	SP	M
Glenmark Pharmaceuticals	BUY	SO	H	Ipca Laboratories	BUY	SO	L
Jubilant Life Sciences	BUY	SP	M	Lupin	BUY	SO	M
Ranbaxy Laboratories	REDUCE	SU	H	Sun Pharmaceuticals Industries	HOLD	SO	L
Torrent Pharmaceuticals	BUY	SO	H				

## ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

## RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

## RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

## SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return



**Edelweiss Securities Limited**, Edelweiss House, off C.S.T. Road, Kalina, Mumbai – 400 098.  
Board: (91-22) 4009 4400, Email: [research@edelcap.com](mailto:research@edelcap.com)

Vikas Khemani	Head Institutional Equities	vikas.khemani@edelweissfin.com	+91 22 2286 4206
Nischal Maheshwari	Co-Head Institutional Equities & Head Research	nischal.maheshwari@edelweissfin.com	+91 22 4063 5476
Nirav Sheth	Head Sales	nirav.sheth@edelweissfin.com	+91 22 4040 7499

### Coverage group(s) of stocks by primary analyst(s): Pharmaceuticals

Apollo Hospitals Enterprise, Aurobindo Pharma, Cadila Healthcare, Cipla, Divi's Laboratories, Dr.Reddys Laboratories, Glenmark Pharmaceuticals, Ipca Laboratories, Jubilant Life Sciences, Lupin, Ranbaxy Laboratories, Sun Pharmaceuticals Industries, Torrent Pharmaceuticals

#### Recent Research

Date	Company	Title	Price (INR)	Recos
09-Feb-13	Sun Pharma	Strong to stronger; <i>Result Update</i>	746	Hold
09-Feb-13	Cadila Healthcare	An aberration; <i>Result Update</i>	791	Buy
08-Feb-13	Aurobindo Pharma	Gathering pace; <i>Result Update</i>	184	Buy

#### Distribution of Ratings / Market Cap

Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	118	46	17	181
* - stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	117	57	7	

#### Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

## DISCLAIMER

### General Disclaimer:

This document has been prepared by Edelweiss Securities Limited (Edelweiss). Edelweiss, its holding company and associate companies are a full service, integrated investment banking, portfolio management and brokerage group. Our research analysts and sales persons provide important input into our investment banking activities. This document does not constitute an offer or solicitation for the purchase or sale of any financial instrument or as an official confirmation of any transaction. The information contained herein is from publicly available data or other sources believed to be reliable, but we do not represent that it is accurate or complete and it should not be relied on as such. Edelweiss or any of its affiliates/ group companies shall not be in any way responsible for any loss or damage that may arise to any person from any inadvertent error in the information contained in this report. This document is provided for assistance only and is not intended to be and must not alone be taken as the basis for an investment decision. The user assumes the entire risk of any use made of this information. Each recipient of this document should make such investigation as it deems necessary to arrive at an independent evaluation of an investment in the securities of companies referred to in this document (including the merits and risks involved), and should consult his own advisors to determine the merits and risks of such investment. The investment discussed or views expressed may not be suitable for all investors. We and our affiliates, group companies, officers, directors, and employees may: (a) from time to time, have long or short positions in, and buy or sell the securities thereof, of company (ies) mentioned herein or (b) be engaged in any other transaction involving such securities and earn brokerage or other compensation or act as advisor or lender/borrower to such company (ies) or have other potential conflict of interest with respect to any recommendation and related information and opinions. This information is strictly confidential and is being furnished to you solely for your information. This information should not be reproduced or redistributed or passed on directly or indirectly in any form to any other person or published, copied, in whole or in part, for any purpose. This report is not directed or intended for distribution to, or use by, any person or entity who is a citizen or resident of or located in any locality, state, country or other jurisdiction, where such distribution, publication, availability or use would be contrary to law, regulation or which would subject Edelweiss and affiliates/ group companies to any registration or licensing requirements within such jurisdiction. The distribution of this document in certain jurisdictions may be restricted by law, and persons in whose possession this document comes, should inform themselves about and observe, any such restrictions. The information given in this document is as of the date of this report and there can be no assurance that future results or events will be consistent with this information. This information is subject to change without any prior notice. Edelweiss reserves the right to make modifications and alterations to this statement as may be required from time to time. However, Edelweiss is under no obligation to update or keep the information current. Nevertheless, Edelweiss is committed to providing independent and transparent recommendation to its client and would be happy to provide any information in response to specific client queries. Neither Edelweiss nor any of its affiliates, group companies, directors, employees, agents or representatives shall be liable for any damages whether direct, indirect, special or consequential including lost revenue or lost profits that may arise from or in connection with the use of the information. Past performance is not necessarily a guide to future performance. The disclosures of interest statements incorporated in this document are provided solely to enhance the transparency and should not be treated as endorsement of the views expressed in the report. Edelweiss Securities Limited generally prohibits its analysts, persons reporting to analysts and their dependents from maintaining a financial interest in the securities or derivatives of any companies that the analysts cover. The information provided in these reports remains, unless otherwise stated, the copyright of Edelweiss. All layout, design, original artwork, concepts and other Intellectual Properties, remains the property and copyright Edelweiss and may not be used in any form or for any purpose whatsoever by any party without the express written permission of the copyright holders.

### Analyst Certification:

The analyst for this report certifies that all of the views expressed in this report accurately reflect his or her personal views about the subject company or companies and its or their securities, and no part of his or her compensation was, is or will be, directly or indirectly related to specific recommendations or views expressed in this report.

### Analyst holding in the stock: No.

### Additional Disclaimer for U.S. Persons

This research report is a product of Edelweiss Securities Limited, which is the employer of the research analyst(s) who has prepared the research report. The research analyst(s) preparing the research report is/are resident outside the United States (U.S.) and are not associated persons of any U.S. regulated broker-dealer and therefore the analyst(s) is/are not subject to supervision by a U.S. broker-dealer, and is/are not required to satisfy the regulatory licensing requirements of FINRA or required to otherwise comply with U.S. rules or regulations regarding, among other things, communications with a subject company, public appearances and trading securities held by a research analyst account.

This report is intended for distribution by Edelweiss Securities Limited only to "Major Institutional Investors" as defined by Rule 15a-6(b)(4) of the U.S. Securities and Exchange Act, 1934 (the Exchange Act) and interpretations thereof by U.S. Securities and Exchange Commission (SEC) in reliance on Rule 15a 6(a)(2). If the recipient of this report is not a Major Institutional Investor as specified above, then it should not act upon this report and return the same to the sender. Further, this report may not be copied, duplicated and/or transmitted onward to any U.S. person, which is not the Major Institutional Investor.

In reliance on the exemption from registration provided by Rule 15a-6 of the Exchange Act and interpretations thereof by the SEC in order to conduct certain business with Major Institutional Investors, Edelweiss Securities Limited has entered into an agreement with a U.S. registered broker-dealer, Enclave Capital, LLC ("Enclave").

Transactions in securities discussed in this research report should be effected through Enclave or another U.S. registered broker dealer.

### Additional Disclaimer for U.K. Persons

The contents of this research report have not been approved by an authorised person within the meaning of the Financial Services and Markets Act 2000 ("FSMA").

In the United Kingdom, this research report is being distributed only to and is directed only at (a) persons who have professional experience in matters relating to investments falling within Article 19(5) of the FSMA (Financial Promotion) Order 2005 (the "Order"); (b) persons falling within Article 49(2)(a) to (d) of the Order (including high net worth companies and unincorporated associations); and (c) any other persons to whom it may otherwise lawfully be communicated (all such persons together being referred to as "relevant persons").

This research report must not be acted on or relied on by persons who are not relevant persons. Any investment or investment activity to which this research report relates is available only to relevant persons and will be engaged in only with relevant persons. Any person who is not a relevant person should not act or rely on this research report nor any of its contents. This research report must not be distributed, published, reproduced or disclosed (in whole or in part) by recipients to any other person.

Edelweiss shall not be liable for any delay or any other interruption which may occur in presenting the data due to any reason including network (Internet) reasons or snags in the system, break down of the system or any other equipment, server breakdown, maintenance shutdown, breakdown of communication services or inability of the Edelweiss to present the data. In no event shall the Edelweiss be liable for any damages, including without limitation direct or indirect, special, incidental, or consequential damages, losses or expenses arising in connection with the data presented by the Edelweiss through this report.

Copyright 2009 Edelweiss Research (Edelweiss Securities Ltd). All rights reserved

Access the entire repository of Edelweiss Research on [www.edelresearch.com](http://www.edelresearch.com)