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# Dr Reddy's: Growth in small doses

## US growth in FY15 will be driven by existing niche and recently launched low-competition products

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The scrip of Dr Reddy's Laboratories has risen six per cent over the past month, due to three Abbreviated New Drug Application (ANDA) approvals from the US Food and Drug Administration, with a combined market size of $500 million. All three face limited competition, from three to four entities, which should translate into higher margins.

Although there are short-term hurdles such as the Russia-Ukraine standoff and 2014-15 might not see any blockbuster product launches by it in the US, analysts believe the valuations are fair. Motilal Oswal Financial Services' (MOSL) Alok Dalal and Hardick Bora say though the near-term outlook on the US seems muted, the company deserves at least sector-average valuations, given its established research and development capabilities, lean balance sheet and well-balanced geographic presence. Hence, the price to earning (PE) valuations of 18.9 times the FY15 estimates and 16.9 times those of FY16 are undemanding.

According to Bloomberg, of the 55 analysts who track the company, 46 have a 'Buy', nine have a 'Hold' and there are no 'Sell' calls.

However, given the 40 per cent outperformance over the past year and short-term pressures, investors can consider the stock on any weakness.

Analysts believe Dr Reddy's niche product portfolio will drive US revenues in FY14-16 and forecast 11-12 per cent annual growth in dollar terms. PHOTO: BLOOMBERG

**Stability from US base biz**

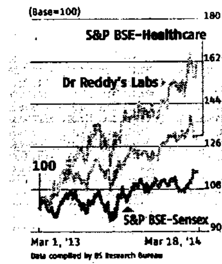
The three drugs launched recently are Imitrex Statdose, Avelox and Caduet, used in the treatment of migraine, bacterial infections and high cholesterol, respectively. Edelweiss Securities analysts estimate these will add four to six per cent to US sales in FY15, on a large US base which contributes over $1 billion revenue to Dr Reddy's annually. Anshuman Gupta and Perin Ali of the research firm say the full-year impact from launches in the second half of FY14, ramp-up in niche products and new launches bolster confidence on the US growth.

While prospects for the US market are robust over the long term, the momentum is likely to come from limited competition products, market share gains from existing products (In the base business) and smaller value products, as there are no blockbuster drug launches in FY15, believe analysts. Launches in the injectable space were the key reason for good performance in the US market over the past year. Two of its launches, Vidaza and Dacogen, used for treating cancer, contributed to nearly 20 per cent of US sales in the December quarter.

The company also launched two other limited competition products in FY14 — Reclast for osteoporosis and Imitrex for migraine headaches. It is expected to launch eight to 10 products in FY15 in that market and would hope limited-competition product approvals continue. Edelweiss Securities' analysts believe Dr Reddy's niche product portfolio will drive US revenues in FY14-16 and forecast 11-12 per cent annual growth in dollar terms.

The next big launch is likely to be Copaxone (around mid-2015), a drug which helps in the treatment of multiple sclerosis and has estimated sales of $3.5 billion in the US market. Overall, for the US market, the company has a pipeline of 62 ANDAs pending approval, of which 39 are filed under Paragraph IV, with eight being first-to-file, giving it 180 day exclusivity on these.

**LIMITED UPSIDE**




**HOLDING STEADY**

| In ₹ crore | FY14E | FY15E |
|---|---|---|
| **Revenues** | **13,648** | **15,597** |
| % chg y-o-y | 15.2 | 14.3 |
| **Ebitda** | **2,485** | **2,790** |
| % chg y-o-y | 10.9 | 12.3 |
| Margin (%) | 18.2 | 17.9 |
| **Net profit** | **2,065** | **2,444** |
| % chg y-o-y | 23.9 | 18.4 |

E: Estimates Source: Edelweiss Securities

**Domestic show to improve**

While pricing issues, as well as a maturing portfolio, have been responsible for the sub-market numbers, growth in India is likely to be led by biotech products and launches in the chronic space. MOSL analysts say higher dependence on mature products is hampering overall growth. While the company is expected to close FY14 with six per cent growth, this is likely to improve to 10-12 per cent starting FY15, in line with the market.

**Russia: Blips & opportunity**

Sales in the Russian market will continue to be a worry due to political tensions but analysts believe the world's 10th largest market, growing at 20 per cent annually in recent years, is a key market for Dr Reddy's. Russian operations accounted for 12 per cent of overall revenue in the December 2013 quarter. While the management, according to MOSL, says the underlying growth will remain unaffected despite the ongoing political issues, there could be an impact due to currency volatility.

For a 10 per cent change in the rouble, MOSL analysts estimate a two per cent impact on FY15 earnings per share. They maintain that Russia and CIS sales could remain soft in the near to medium term. Analysts say with Russia importing three quarters of its medicines, sales might remain unaffected. Positively, with Indian companies barely accounting for three per cent of the Russian market, there is scope to increase its share.

Company.