Dr. Reddys(RDY)

$42.45 (As of 01/17/20)

Price Target (6-12 Months): **$45.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 01/07/20) Prior Recommendation: Underperform	**Neutral**
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**5-Strong Sell**
	Zacks Style Scores:	VGM:B
	Value: C | Growth: A | Momentum: C	

Summary

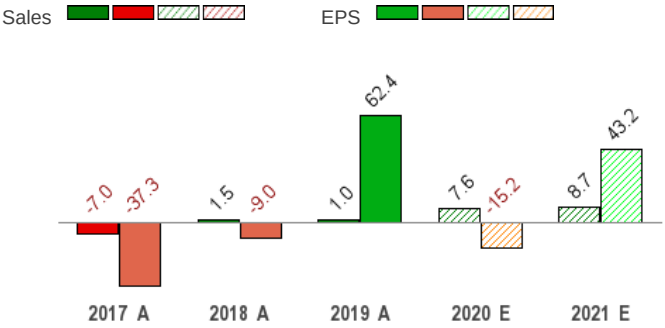
In second-quarter fiscal 2020, Dr. Reddy's top and bottom lines recorded year-over-year growth. This was supported by strength in Europe, emerging markets and India, and pickup in product launches. As of Sep 30, the company had 99 generic filings (96 abbreviated New Drug Applications and three new drug applications) pending FDA approval. Approval of new generics should further bolster the portfolio. The company has started to divest non-core assets to channelize its sources to increase profitability. Shares of the company have outperformed the industry in the past year. However, price erosion in the North America generics market will impact sales from that region. Moreover, the European market is also witnessing high price erosion in some of the key molecules.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	**$42.82 - $34.67**
20 Day Average Volume (sh)	**135,648**
Market Cap	**$7.0 B**
YTD Price Change	**4.6%**
Beta	**0.18**
Dividend / Div Yld	**$0.26 / 0.6%**
Industry	**Medical - Generic Drugs**
Zacks Industry Rank	**Top 43% (110 out of 254)**
Last EPS Surprise	**NA**
Last Sales Surprise	**NA**
EPS F1 Est- 4 week change	**-7.9%**
Expected Report Date	**01/27/2020**
Earnings ESP	**0.0%**
P/E TTM	**18.5**
P/E F1	**30.5**
PEG F1	**NA**
P/S TTM	**3.0**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2021					2,603 E
2020	558 A	680 A			2,394 E
2019	543 A	524 A	535 A	581 A	2,225 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021					$1.99 E
2020	$0.58 A	$0.93 A			$1.39 E
2019	$0.40 A	$0.42 A	$0.41 A	$0.38 A	$1.64 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 01/17/2020. The reports text is as of 01/20/2020.

Overview

India-based Dr. Reddy's Laboratories Ltd. is an integrated global pharmaceutical company engaged in providing affordable and innovative medicines since 1984.

The company markets its products in countries like the U.S., the UK, Germany, India, Russia, Venezuela, Romania and South Africa. Dr. Reddy's operates through three segments:

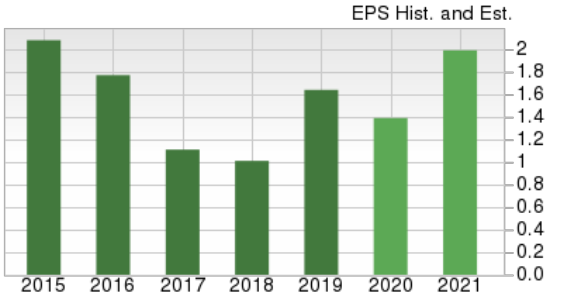
- ***Global Generics*** – This segment consists of branded and unbranded prescription drugs along with over-the-counter (OTC) drugs. It includes the operations of the company's biologics business.

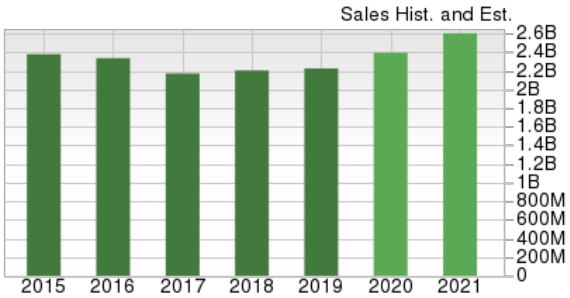
- ***Pharmaceutical Services & Active Ingredients (PSAI)*** – This segment is composed of active pharmaceutical ingredients (API) and custom pharmaceutical services.

- ***Proprietary Products and Others*** – This segment involves the new chemical entities, the differentiated formulations business and a dermatology specialty business.

Global Generics contributed 79.9%, PSAI contributed 15.7% and Proprietary Products and Others contributed 4.4% to total revenues in fiscal 2019.

The company has a strategic partnership with Glaxo to market selected products across emerging markets outside India.





Dr. Reddy's reported fiscal 2019 (ending Mar 31, 2019) revenues of $2.2 billion (up 8% year over year).

Reasons To Buy:

▲ **Strong Generic Pipeline:** Dr. Reddy's enjoys a strong position in the generics market. As of Sep 30, 2019, Dr. Reddy's had 99 generic filings (96 abbreviated New Drug Applications [ANDAs] and three new drug applications) pending FDA approval. Of these 96 ANDAs, 55 were Para IV filings and 31 have first-to-file status. New product launches, especially complex generics, should help drive the generics business over regular intervals. In the second quarter of fiscal 2020, the company launched eight products (Carboprost, Ramelteon, Fosaprepitant, Pregabalin, Vigabatrin, Docetaxel 160mg, Bupropion SR and OTC Guaif / Psuedo).

> Dr. Reddy's enjoys a strong position in the generics market. Efforts on strengthening its presence in the biosimilars market have been commendable too.

In April 2019, Dr. Reddy's entered a definitive agreement to acquire the yet-to-be-marketed portfolio of 42 non-marketed ANDAs in the United States. The portfolio includes more than 30 generic injectable products. These products will be technology transferred and ready for launch within the next one to two years. The deal is in sync with the company's strategy to strengthen its portfolio in its chosen growth markets. This transaction will help the company expand its injectable products portfolio in the U.S. market and globally.

▲ **Biosimilars Market to Boost Revenues:** Dr. Reddy's is working with Merck Serono to develop and commercialize a portfolio of biosimilar compounds in oncology, primarily focused on MAbs. Dr. Reddy's has already expanded its biosimilars facility in India to meet growing demand in emerging markets. Dr. Reddy's in July 2018 launched Hervycta (Trastuzumab), a biosimilar of Roche's Herceptin in India, indicated for the treatment of HER2-positive cancers (early breast cancer, metastatic breast cancer and metastatic gastric cancer).

▲ **Strategic Initiatives:** The company is undertaking some strategic measures to combat the ongoing challenges. It plans to modernize some of its infrastructure, systematically implement its new quality management system and automate some of the critical manufacturing and quality related processes.

In order to revitalize growth, Dr. Reddy's remains focused on accelerating the development of its complex generics portfolio and also making efforts to ensure that the approvals come in time through appropriate risk management and proactive measures to deal with possible deficiencies.

Reasons To Sell:

Persisting macroeconomic issues in some territories in emerging markets and negative impact of a depreciating ruble remain a concern. The FDA warning letter for some manufacturing facilities is also a concern.

- **Pricing pressure on North America business:** The company's North America base business is witnessing pricing pressures since the last few quarters due to enhanced channel consolidation and increased competitive pressure on sales of some of its key generic products.

  In-fact, the United States' generics industry is facing significant competitive and pricing pressure. The ongoing consolidation of customers in the industry has led to increasing price erosion and decreasing volume. The consolidation in the industry has increased the ability to negotiate lower prices for generic drugs. A sharp decline in generic drug prices is proving to be a major challenge for generic drugmakers as well as drug distributors. Moreover, the FDA is speeding up the approval of generic drugs, which means more competition, increasing price cuts and decreasing volume. The pricing and competitive pressures are expected to continue.

  The implementation of general sales tax (GST) in India is also hurting its topline to an extent.

- **Warning Letter for Manufacturing Facilities:** In November 2015, Dr. Reddy's received a warning letter from the FDA regarding a couple of API manufacturing facilities in India as well as its Oncology Formulation manufacturing facility in India. In December 2015, the company submitted a comprehensive, corrective and preventive action plan, to address all the issues raised, which includes manufacturing network and quality/compliance issues. The company has completed its remedial measures and submitted the same as of Mar 2017. The FDA conducted reinspection of the aforementioned manufacturing facilities in March and April 2017. During the re-inspections, the FDA issued three observations with respect to the company's API facility at Miryalaguda, two observations with respect to its API facility at Srikakulam and thirteen observations with respect to its oncology formulation manufacturing facility. With respect to API manufacturing facility at Srikakulam, the company was asked to carry out certain detailed investigations and analyses. The company has completed a portion of this investigation.

  In June 2018, the company requested the FDA to schedule a re-inspection of the oncology formulation manufacturing facility at Duvvada. In October 2018, the re-inspection for the injectable plant in Duvvada was completed and the FDA issued eight observations. The company comprehensively responded to this observation and received certain specific questions from the agency, seeking further clarification on some of the company's responses. With respect to the API manufacturing facility in Srikakulam, the company submitted the results of the investigation, and responded to all the queries asked by the FDA. The company is awaiting re-inspection of the facility.

  Consequent to this warning letter, the company has been facing a number of challenges that includes price erosion and delay in product launches. These challenges are adversely affecting the company's top-line growth.

- **Competition in Generics Segment:** The generic market is highly crowded and Dr. Reddy's faces competition from players like Mylan, Teva, Endo and Sandoz among others. Competition is fierce as generic companies strive to be the first to launch a generic version once a brand product loses exclusivity so that they can capture significant market share. Once additional generic companies enter the market, market share, revenues and gross profit typically decline. Therefore, it is very important for generic companies to develop and introduce new products in a timely and cost-effective manner to maintain revenues and gross profit. In addition to competition from other generic players, brand name companies also provide competition by marketing their own generic version (authorized generics) of their brand products.

Last Earnings Report

Dr. Reddy's Q2 Earnings and Revenues Increase Y/Y

Quarter Ending	09/2019
Report Date	**Nov 01, 2019**
Sales Surprise	**NA**
EPS Surprise	**NA**
Quarterly EPS	**0.93**
Annual EPS (TTM)	**2.30**

Dr. Reddy's reported second-quarter fiscal 2020 earnings of 93 cents per share, up from 43 cents in the year-ago quarter, per American Depositary Share (ADS).

Moreover, revenues grew 26% year over year to $680 million.

Quarter in Detail

Dr. Reddy's reported revenues under three segments — Global Generics, Pharmaceutical Services & Active Ingredients ("PSAI"), and Proprietary Products and Others.

Global Generics revenues were INR32.8 billion ($464.6 million), up 7% year over year in the fiscal second quarter. Growth was led by contributions from Europe, emerging markets and India, primarily owing to volume gains and product launches.

PSAI revenues were INR7.1 billion ($100.6 million), up 18% from the year-ago quarter.

Revenues at the Proprietary Products segment came in at INR8.09 million ($0.11 million), surging 472% year over year.

Research and development expenses were down 11% year over year to $52 million.

Selling, general and administrative expenses were $238 million, up 36% year over year.

As of Sep 30, 2019, Dr. Reddy's had 99 generic filings (96 abbreviated New Drug Applications [ANDAs] and three new drug applications) pending FDA approval. Of these 96 ANDAs, 55 were Para IV filings and 31 have first-to-file status.

Recent News

Launch of Sodium Nitroprusside Injection, Single-dose Vial in the U.S. Market-Dec 30

Dr. Reddy's announced the launch of Sodium Nitroprusside Injection, 50 mg/2 mL (25 mg/mL) Single-dose Vial, the therapeutic generic equivalent of Nitropress (sodium nitroprusside) Injection, 50 mg/2mL vial, approved by the FDA. Nitropress is a trademark of Hospira, Inc.

Launch of Deferasirox Film-Coated Tablets, in the U.S. Market-Dec 6

Dr. Reddy's announced the launch of Deferasirox Film-Coated Tablets, 90 mg and 360 mg, a therapeutically equivalent generic version of Jadenu (deferasirox) Film-Coated Tablets, 90 mg, 180 mg, and 360 mg, approved by the FDA.

Launch of Deferasirox Tablets for Oral Suspension, in the U.S. Market-Dec 6

Dr. Reddy's announced the launch of Deferasirox Tablets for Oral Suspension, a therapeutically equivalent generic version of Exjade (deferasirox) Tablets for Oral Suspension, approved by the FDA. Dr. Reddy's Deferasirox Tablets for Oral Suspension, are available in 125 mg, 250 mg, and 500 mg dosage strengths in bottle count sizes of 30.

Launch of Bortezomib for Injection 3.5 mg/vial for Intravenous use only in the U.S. Market-Dec 4

Dr. Reddy's announced the launch of Bortezomib for Injection 3.5 mg/vial, approved by the FDA via a 505(b)(2) new drug application (NDA) pathway for intravenous use only.

Dr. Reddy's Bortezomib for Injection 3.5 mg/vial is for intravenous use only and is indicated for the treatment of adult patients with multiple myeloma and for the treatment of adult patients with mantle cell lymphoma who have received at least one prior therapy.

Launch of Doxercalciferol Injection in the U.S. Market-Nov 22

Dr. Reddy's announced the launch of Doxercalciferol Injection, 4 mcg/2 mL (2 mcg/mL) multiple-dose Vials, the therapeutic generic equivalent of Hectorol (doxercalciferol) Injection 4 mcg/2 mL (2 mcg/mL) MultipleDose Vials, approved by the FDA.

Hectorol is a trademark of Sanofi-Aventis US LLC

Enters Nutrition Segment with Celevida in India-Nov 14

Dr. Reddy's announced the entry into the nutrition segment with the launch of its diabetes nutrition drink 'Celevida' in India. It's a first-of-its-kind under Dr. Reddy's nutrition portfolio and clinically proven to help manage blood glucose levels among Indian patients.

Confirmed its Voluntary Nationwide Recall of all Ranitidine Products in the U.S. Market-Oct 23

Dr. Reddy's confirmed that it initiated a voluntary nationwide recall on Oct 1, 2019, (at the retail level for over-the-counter products and at the consumer level for prescription products) of all of its ranitidine medications sold in the United States due to confirmed contamination with N-Nitrosodimethylamine (NDMA) above levels established by the FDA. This recall follows the USFDA's caution note alerting patients and health care professionals that NDMA was found in certain samples of ranitidine. To date, Dr. Reddy's has not received any reports of adverse events related to the recall of these products. The recall includes all quantities in the United States within the expirydate.

Launch of Over-the-Counter, Store-Brand equivalent of Prevacid 24HR Capsules-Sep 16

Dr. Reddy's announced the launch of Lansoprazole Delayed-Release Capsules USP, 15 mg, an over-the-counter (OTC) store-brand equivalent of Prevaci® 24HR Capsules, in the U.S. market, as approved by the FDA.

Dr. Reddy's OTC Lansoprazole Delayed-Release Capsules USP, 15 mg, is an over-the-counter, Proton Pump Inhibitor (PPI) used to treat frequent heartburn occurring two or more days a week.

Prevacid is a registered trademark of Takeda Pharmaceuticals North America, Inc

Launch of Fosaprepitant for Injection in the U.S. Market -Sep 11

Dr.Reddy's announced the launch of Fosaprepitant for Injection, the therapeutic generic equivalent of EMEND (fosaprepitant) for injection, approved by the FDA.

EMEND is a trademark of Merck Sharp & Dohme Corp.

Launch of Bupropion Hydrochloride Extended-Release Tablets in the U.S. Market- Sep 5

Dr.Reddy's announced the launch of Bupropion Hydrochloride extended-release tablets, USP (SR), a therapeutically equivalent generic version of Zyban (Bupropion Hydrochloride) extended-release tablets, approved by the FDA.

Valuation

Dr. Reddy's shares are up 14.6% over the trailing 12-month period. Over the past year, the Zacks sub-industry is down 6.9% while the sector is up 4.5%.

The S&P 500 index is up 23.8% in the past year.

The stock is currently trading at 22.66X forward 12-month earnings per share, which compares to 8.99X for the Zacks sub-industry, 21.79X for the Zacks sector and 19.20X for the S&P 500 index.

Over the past five years, the stock has traded as high as 34.23X and as low as 16.19X, with a 5-year median of 21.49X. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our $45.00 price target reflects 24.02X forward 12-month earnings per share.

The table below shows summary valuation data for RDY

Valuation Multiples - RDY

		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	22.66	8.99	21.79	19.2
	5-Year High	34.23	16.24	21.79	19.34
	5-Year Low	16.19	6.55	15.85	15.17
	5-Year Median	21.49	9.87	18.91	17.44
P/S F12M	Current	2.75	1.59	2.88	3.57
	5-Year High	4.28	4.31	3.82	3.57
	5-Year Low	1.79	1.14	2.43	2.54
	5-Year Median	2.7	1.93	2.94	3
P/B TTM	Current	3.23	1.32	4.61	4.55
	5-Year High	6.23	3.7	5.03	4.55
	5-Year Low	2.43	0.86	3.43	2.85
	5-Year Median	3.47	1.32	4.29	3.61

As of 01/17/2020

Industry Analysis **Zacks Industry Rank:** Top 43% (110 out of 254)

Top Peers

Bausch Health Cos Inc. **(BHC)**	Neutral
Endo International plc **(ENDP)**	Neutral
GlaxoSmithKline plc **(GSK)**	Neutral
Mallinckrodt public limited company **(MNK)**	Neutral
Mylan N.V. **(MYL)**	Neutral
Novartis AG **(NVS)**	Neutral
Sanofi **(SNY)**	Neutral
Teva Pharmaceutical Industries Ltd. **(TEVA)**	Neutral

Industry Comparison Industry: Medical - Generic Drugs

Industry Peers

	RDY Neutral	X Industry	S&P 500	MYL Neutral	NVS Neutral	TEVA Neutral
VGM Score	B	-	-	B	B	B
Market Cap	7.03 B	386.32 M	24.65 B	11.18 B	219.85 B	11.14 B
# of Analysts	1	4	13	9	5	13
Dividend Yield	0.62%	0.00%	1.73%	0.00%	1.92%	0.00%
Value Score	C	-	-	A	B	A
Cash/Price	0.06	0.18	0.04	0.03	0.04	0.13
EV/EBITDA	13.20	-1.46	14.11	8.20	10.75	-45.23
PEG Ratio	NA	0.98	2.08	1.11	1.98	0.98
Price/Book (P/B)	3.23	2.96	3.39	0.97	4.18	0.75
Price/Cash Flow (P/CF)	15.73	4.57	13.81	2.50	11.78	2.20
P/E (F1)	30.54	7.78	19.19	4.83	16.92	4.07
Price/Sales (P/S)	2.99	3.07	2.69	0.98	4.55	0.64
Earnings Yield	3.27%	-8.28%	5.21%	20.73%	5.91%	24.61%
Debt/Equity	0.10	0.08	0.72	1.17	0.42	1.62
Cash Flow ($/share)	2.70	-0.17	6.94	8.68	8.15	4.63
Growth Score	A	-	-	D	C	D
Hist. EPS Growth (3-5 yrs)	-5.32%	3.58%	10.56%	3.79%	0.15%	-17.10%
Proj. EPS Growth (F1/F0)	-15.24%	2.24%	7.57%	4.05%	8.41%	4.99%
Curr. Cash Flow Growth	29.21%	-0.81%	14.73%	5.27%	6.18%	-26.03%
Hist. Cash Flow Growth (3-5 yrs)	-0.91%	4.21%	9.00%	22.00%	2.20%	-4.41%
Current Ratio	1.96	2.91	1.24	1.43	0.95	0.89
Debt/Capital	9.03%	8.22%	42.99%	53.87%	29.33%	61.86%
Net Margin	16.20%	-56.06%	11.14%	0.42%	24.43%	-22.88%
Return on Equity	18.44%	-42.85%	17.16%	18.80%	20.86%	15.41%
Sales/Assets	0.72	0.29	0.55	0.36	0.37	0.29
Proj. Sales Growth (F1/F0)	9.63%	2.73%	4.16%	3.94%	2.86%	-1.01%
Momentum Score	C	-	-	B	C	C
Daily Price Chg	2.88%	-0.59%	0.27%	-1.41%	0.87%	-3.95%
1 Week Price Chg	1.99%	0.00%	0.39%	3.22%	-0.98%	-0.88%
4 Week Price Chg	4.61%	2.34%	2.95%	11.76%	1.76%	2.31%
12 Week Price Chg	8.40%	14.36%	7.76%	18.69%	9.96%	25.00%
52 Week Price Chg	13.81%	-19.05%	22.29%	-26.70%	8.24%	-45.63%
20 Day Average Volume	135,648	481,489	1,536,375	6,294,218	1,073,944	13,784,133
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-7.95%	0.00%	0.00%	0.29%	-0.11%	0.00%
(F1) EPS Est 12 week change	-32.52%	-4.57%	-0.40%	0.29%	-1.60%	0.37%
(Q1) EPS Est Mthly Chg	NA%	0.00%	0.00%	5.75%	NA	0.00%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	C
Growth Score	A
Momentum Score	C
VGM Score	B

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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