

**EMPLOYEE STOCK OPTION SCHEME***Dr. Reddy's Employees Stock Option Plan-2002 ("the DRL 2002 Plan"):*

The Company instituted the DRL 2002 Plan for all eligible employees in pursuance of the special resolution approved by the shareholders in the Annual General Meeting held on 24 September 2001. The DRL 2002 Plan covers all employees of DRL and its subsidiaries and directors (excluding promoter directors) of DRL and its subsidiaries (collectively, "eligible employees"). Under the Scheme, the Nomination, Governance and Compensation Committee of the Board ('the Committee') shall administer the Scheme and grant stock options to eligible directors and employees of the Company and its subsidiaries. The Committee shall determine the employees eligible for receiving the options, the number of options to be granted, the exercise price, the vesting period and the exercise period. The vesting period is determined for the options issued on the date of the grant. The options issued under the DRL 2002 Plan vest in periods ranging between one and four years and generally have a maximum contractual term of five years.

The DRL 2002 Plan, as amended at Annual General Meetings of shareholders held on 28 July 2004 and on 27 July 2005, provides for stock option grants in two categories:

**Category A:** 300,000 stock options out of the total of 2,295,478 reserved for grant of options having an exercise price equal to the fair market value of the underlying equity shares on the date of grant; and

**Category B:** 1,995,478 stock options out of the total of 2,295,478 reserved for grant of options having an exercise price equal to the par value of the underlying equity shares (i.e., ₹ 5 per option).

The fair market value of a share on each grant date falling under Category A above is defined as the average closing price (after adjustment of Bonus issue) for 30 days prior to the grant, in the stock exchange where there was highest trading volume during that period. Notwithstanding the foregoing, the Committee may, after getting the approval of the shareholders in the Annual General Meeting, grant options with a per share exercise price other than fair market value and par value of the equity shares.

After the issue of bonus shares by the Company in August 2006, the DRL 2002 Plan provides for stock options granted in the above two categories as follows:

PARTICULARS	NUMBER OF OPTIONS UNDER CATEGORY A	NUMBER OF OPTIONS UNDER CATEGORY B	TOTAL
Options reserved under original plan	300,000	1,995,478	2,295,478
Options exercised prior to issue of bonus shares (A)	94,061	147,793	241,854
Balance of shares that can be allotted on exercise of options (B)	205,939	1,847,685	2,053,624
Options arising from issue of bonus shares (C)	205,939	1,847,685	2,053,624
<b>Total options after bonus shares (A+B+C)</b>	<b>505,939</b>	<b>3,843,163</b>	<b>4,349,102</b>

In the case of termination of employment, all unvested options would stand cancelled. Options that have vested but have not been exercised can be exercised within the time prescribed under each option agreement by the Committee or if no time limit is prescribed, within three months of the date of employment termination, failing which they would stand cancelled.

The term of the DRL 2002 Plan was extended for a period of 10 years with effect from 29 January 2012 by the shareholders at the Company's Annual General Meeting held on 20 July 2012.

During the year ended 31 March 2016, the Company under the DRL 2002 Plan has issued 102,224 Category B options to eligible employees. The vesting period for the options granted varies from 12 to 48 months.

The date of grant, number of options granted, exercise price fixed by the Committee for respective options and the market price of the shares of the Company on the day prior to the date of grant are given below:

DATE OF GRANT	NUMBER OF OPTIONS GRANTED	EXERCISE PRICE ₹	MARKET PRICE ₹ (AS PER SEBI GUIDELINES)
11 May 2015	102,224	5.00	3,350.45

**EMPLOYEE STOCK OPTION SCHEME (CONTINUED)**

Stock option activity under the DRL 2002 Plan for the two categories of options was as follows:

**CATEGORY A - FAIR MARKET VALUE OPTIONS**

There is no stock option activity under this category during the year 31 March 2016 and there were no options outstanding under this category as of 31 March 2016.

CATEGORY A - FAIR MARKET VALUE OPTIONS	YEAR ENDED 31 MARCH 2015			
	PARTICULARS	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE
Outstanding at the beginning of the year	10,000	₹ 448.00	₹ 448.00	44
Granted during the year	-	-	-	-
Expired / forfeited during the year	-	-	-	-
Exercised during the year	(10,000)	₹ 448.00	₹ 448.00	-
Outstanding at the end of the year	-	-	-	-
Exercisable at the end of the year	-	-	-	-

CATEGORY B - PAR VALUE OPTIONS	YEAR ENDED 31 MARCH 2016			
	PARTICULARS	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE
Outstanding at the beginning of the year	585,454	₹ 5.00	₹ 5.00	71
Granted during the year	102,224	5.00	5.00	90
Expired / forfeited during the year	(66,319)	5.00	5.00	-
Exercised during the year	(194,011)	5.00	5.00	-
Outstanding at the end of the year	427,348	₹ 5.00	₹ 5.00	72
Exercisable at the end of the year	53,801	₹ 5.00	₹ 5.00	42

CATEGORY B - PAR VALUE OPTIONS	YEAR ENDED 31 MARCH 2015			
	PARTICULARS	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE
Outstanding at the beginning of the year	641,674	₹ 5.00	₹ 5.00	78
Granted during the year	230,840	5.00	5.00	90
Expired / forfeited during the year	(59,148)	5.00	5.00	-
Exercised during the year	(227,912)	5.00	5.00	-
Outstanding at the end of the year	585,454	₹ 5.00	₹ 5.00	71
Exercisable at the end of the year	43,425	₹ 5.00	₹ 5.00	40

**Dr. Reddy's Employees ADR Stock Option Plan-2007 ("the DRL 2007 Plan"):**

The Company instituted the DRL 2007 Plan for all eligible employees in pursuance of the special resolution approved by the shareholders in the Annual General Meeting held on 27 July 2005. The DRL 2007 Plan came into effect on approval of the Board of Directors on 22 January 2007. The DRL 2007 Plan covers all employees of DRL and its subsidiaries and directors (excluding promoter directors) of DRL and its subsidiaries (collectively, "eligible employees"). Under the DRL 2007 Plan, the Nomination, Governance and Compensation Committee of the Board (the 'Committee') shall administer the DRL 2007 Plan and grant stock options to eligible employees of the Company and its subsidiaries. The Nomination, Governance and Compensation Committee shall determine the employees eligible for receiving the options, the number of options to be granted, the exercise price, the vesting period and the exercise period. The vesting period is determined for all options issued on the date of the grant. The options issued under the DRL 2007 Plan vest in periods ranging between one and four years and generally have a maximum contractual term of five years.

The Committee may, after obtaining the approval of the shareholders in the Annual General Meeting, grant options with a per share exercise price other than fair market value and par value of the equity shares.

During the year ended 31 March 2016, the Company has issued 40,184 Category B options to eligible employees under the DRL 2007 Plan. The vesting period for the options granted varies from 12 to 48 months.

**EMPLOYEE STOCK OPTION SCHEME (CONTINUED)**

The date of grant, number of options granted, exercise price fixed by the Committee for respective options and the market price of the shares of the Company on the day prior to the date of grant is given below:

DATE OF GRANT	NUMBER OF OPTIONS GRANTED	EXERCISE PRICE ₹	MARKET PRICE ₹ (AS PER SEBI GUIDELINES)
11 May 2015	40,184	5.00	3,350.45

Stock option activity under the DRL 2007 Plan was as follows:

CATEGORY B - PAR VALUE OPTIONS	YEAR ENDED 31 MARCH 2016			
	PARTICULARS	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE
Outstanding at the beginning of the year	98,350	₹ 5.00	₹ 5.00	72
Granted during the year	40,184	5.00	5.00	90
Expired / forfeited during the year	(14,023)	5.00	5.00	-
Exercised during the year	(32,468)	5.00	5.00	-
Outstanding at the end of the year	<b>92,043</b>	<b>₹ 5.00</b>	<b>₹ 5.00</b>	<b>79</b>
Exercisable at the end of the year	<b>7,141</b>	<b>₹ 5.00</b>	<b>₹ 5.00</b>	<b>45</b>

CATEGORY B - PAR VALUE OPTIONS	YEAR ENDED 31 MARCH 2015			
	PARTICULARS	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE
Outstanding at the beginning of the year	97,463	₹ 5.00	₹ 5.00	79
Granted during the year	45,796	5.00	5.00	90
Expired / forfeited during the year	(10,515)	5.00	5.00	-
Exercised during the year	(34,394)	5.00	5.00	-
Outstanding at the end of the year	<b>98,350</b>	<b>₹ 5.00</b>	<b>₹ 5.00</b>	<b>72</b>
Exercisable at the end of the year	<b>6,730</b>	<b>₹ 5.00</b>	<b>₹ 5.00</b>	<b>42</b>

The Company has not granted any options under Category A of "the DRL 2007 Plan".

In addition to the above, during the year ended 31 March 2015, the Company adopted a new program to grant performance linked stock options to certain employees under the DRL 2002 Plan and the DRL 2007 Plan. Under this program, performance targets are measured each year against pre-defined interim targets over the three year period ending on 31 March 2017 and eligible employees are granted stock options upon meeting such targets. The stock options so granted are ultimately vested with the employees who meet subsequent service vesting conditions which range from 1 to 4 years. After vesting, such stock options generally have a maximum contractual term of five years. The details of grants made under this program are included in the above tables under the respective plans.

Till 30 September 2015, the Company accounted for employee stock options using the intrinsic method of accounting available under Securities and Exchange Board of India (Employee Stock Option Scheme and Employee Stock Purchase Scheme) Guidelines, 1999. Effective 1 October 2015, the Company applied Securities and Exchange Board of India (Share Based Employee Benefits) Regulations, 2014, which require the employee stock options to be accounted under the Guidance note on Accounting for Employee Share-based Payments issued by the Institute of Chartered Accountants of India (ICAI). Consequent to such change, deferred employee stock compensation account has been de-recognised to conform to the new accounting pronouncement.

The Company followed intrinsic method of accounting based on which a compensation expense of ₹ 455 (previous year: ₹ 519) was recognized in the statement of profit and loss. Had the Company used the fair value method, the compensation expense would have been ₹ 471. The differential stock compensation expense of ₹ 16 does not have any significant effect on the net results and EPS of the Company for the year ended 31 March 2016.

*Valuation of stock options under fair value method:*

The fair value of stock options granted under the DRL 2002 Plan and the DRL 2007 Plan has been measured using the Black-Scholes-Merton model at the date of the grant.

**EMPLOYEE STOCK OPTION SCHEME (CONTINUED)**

The Black-Scholes-Merton model includes assumptions regarding dividend yields, expected volatility, expected terms and risk free interest rates. In respect of par value options granted under category B, the expected term of an option (or "option life") is estimated based on the vesting term, contractual term, as well as expected exercise behavior of the employees receiving the option. In respect of fair market value options granted under category A, the option life is estimated based on the simplified method. Expected volatility of the option is based on historical volatility, during a period equivalent to the option life, of the observed market prices of the Company's publicly traded equity shares. Dividend yield of the options is based on recent dividend activity. Risk-free interest rates are based on the government securities yield in effect at the time of the grant. These assumptions reflect management's best estimates, but these assumptions involve inherent market uncertainties based on market conditions generally outside of the Company's control. As a result, if other assumptions had been used in the current period, stock-based compensation expense could have been materially impacted. Further, if management uses different assumptions in future periods, stock based compensation expense could be materially impacted in future years.

The estimated fair value of stock options is charged to income on a straight-line basis over the requisite service period for each separately vesting portion of the award as if the award was, in-substance, multiple awards.

The weighted average inputs used in computing the fair value of options granted were as follows:

Expected volatility	25.98%
Exercise price	₹ 5.00
Option life	2.5 Years
Risk-free interest rate	7.87%
Expected dividends	0.60%
Grant date share price	₹ 3,359.70

Details of weighted average grant date fair values and exercise prices of options granted during the year ended 31 March 2016:

PARTICULARS	DRL 2002 PLAN	DRL 2007 PLAN
Weighted average grant date fair value of options granted - Par value	₹ 3,350	₹ 3,465
Weighted average share price on the date of exercise of options	₹ 3,504	₹ 3,575

Employee wise details of options granted during the year to senior management personnel to be exercised at par value:

Name	Designation	No of options granted	
		2002 Plan	2007 Plan
Mr. Abhijit Mukherjee	Chief Operating Officer	4,500	
Mr. Saumen Chakraborty	President, Chief Financial Officer and Global Head - IT & BPE	3,000	
Mr. Umang Vohra*	Executive Vice President and Head - North America Generics	3,000	
Dr. Cartikeya Reddy	Executive Vice President and Head - Biologics	2,800	
Mr. M V Ramana	Executive Vice President and Head - Branded Markets (India & Emerging markets)	3,000	
Mr. Samiran Das	Executive Vice President and Head - Global Manufacturing Operations	2,500	
Dr. Amit Biswas	Executive Vice President and Head - Integrated Product Development	2,500	
Dr. K V S Ram Rao	Senior Vice President and Head - PSAI Commercial Organisation	2,000	
Mr. Alok Sonig	Executive Vice President and Head - North America Generics	3,000	
Dr. Chandrasekhar Sripada	President and Global Head - Human Resources	2,500	
Dr. Raghav Chari	Executive Vice President and Head - Proprietary Products		3,000

\* Mr. Umang Vohra was in service till 25 September 2015.

No employee of the Company received grant of options during the year amounting to 5% or more of options granted or exceeding 1% of issued capital of the Company.