Dr. Reddy's Laboratories Limited presentation delivered at the 37th Annual J.P. Morgan Healthcare Conference on

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Neha Manpuria: Welcome to the emerging market track. We will start with the Indian pharmaceutical names. I am Neha Manpuria, the India Healthcare Analyst at JP Morgan. We have Dr. Reddy's presenting first. We have Mr. Erez Israeli from Dr. Reddy's, who is the COO.

Erez Israeli: Thank you so much. It's a great privilege and honor to represent Dr. Reddy's. My name is Erez. I am the Chief Operating Officer of Dr. Reddy's for the last nine months now, almost 10 months. In this presentation we will try to share with you the story. I want to thank everyone that took this slot, especially after the lunch slot, to listen to us. I hope it will be useful for you. I'll try to speak, let's say, 15 to 20 minutes, share the story and hopefully there will be some time to speak about, maybe to answer some Q&A.

When the company was formed 35 years ago by Dr. Anji Reddy, it was already about access to health and access to affordable medicines, back then. This purpose still exists. It's still alive and kicking. In the last couple of years, we even added the acceleration, that we cannot wait for that and this is where we came up with good health cannot wait. This is relevant. More than ever, we see the need. More than ever, we are committed for this purpose for Dr. Reddy.

In the last couple of years, especially in the last couple of months, we built ourselves to address the dynamics of this market. Naturally, you guys are well aware of all the dynamics, whether it's in the United States, or in India, or in China or elsewhere. We are well positioned to win in this game. We are well positioned to serve our customers well by first Dr. Reddy was always known for great science, great R&D. We are still there. We still are, and we are still committed to R&D. R&D will continue to be the main source of growth for the company for many, many years to come. As you can see, we have 1,200 scientists, 350 PhDs, and an amazing portfolio. We are normally being asked about products and naturally, we share certain information, either through litigation or through deals. But you are going to see in the future that most of our portfolio was not disclosed yet. Some of it is really differentiated, complex and a very, very interesting asset to come.

We are set in six spaces. I am going to elaborate about these six spaces, and where strategically we are planning to focus ourselves. In each one of these six spaces we are well set for growth.

Something that I would like to emphasize, and will emphasize more, it's about cost. We have a very low cost of operation. We will drive costs down even further than that. 90-plus percent of our expenses are in India. The rupee is relatively low. No tariffs, very, very low tax base, and naturally, giving the ability of getting a lot of talent in relatively low-cost environment is an advantage that we share.

With that respect, in the last couple of months and quarters, we were very busy to improve our business performance. We had couple of muted quarters prior to that. We changed certain activities. I'm going to elaborate about that. But as you can see, that our sales are in the right pattern, and what's more important, that it's well diverse. Actually, the last quarter is the first time that our sales into EM plus India were more than the United States. The growth that we have in this area will continue to be more significant than what we saw in the United States, although we do see that the United States will be a growth space for us, I will elaborate about that.

As you can see also that our margins are getting better. This is primarily by focusing on cost, and by facing the growth in the emerging markets. At the same time, a very big focus was on spend and the control of cost. You can see that despite the price erosion in the United States, we kept our margins. You can see our gross margin pattern.

You can see also that the level of spend is the same despite inflation, which means that we took out quite a lot of costs from the system to cover for this inflation and cover the cost in the places that we are growing. Naturally, when we grow, there is also growth in costs relatively to this area given that we control the spend and improve productivities significantly.

In terms of CAPEX, we are actually in a situation in which we do have enough capacity for the next to come. We will be able to cater for the growth without adding sites. Actually, we will even rationalize additional assets as they are going forward. You can see that the level of CAPEX is actually going down significantly, versus the $150 million to $200 million that you originally heard.

We have a very, very healthy balance sheet, 0.26 the last quarter that we have, which means that we have enough financial capacity. Our risk profile in terms of balance sheet is pretty healthy. It also was a good year in terms of TSR on both dividend and share price performance in general. The main message here is that we are focused on TSR. We are focused on shareholder returns. This is something that is at the top of our minds. How did we do that? This is where I'll spend a couple of minutes on some of these bullet points.

First, we are growing significantly in the emerging markets. Most of our emerging markets are based on hospital products. We are well positioned to be their solution for their unmet needs, because some of these markets are not being served well with hospital products. We are focusing more on India. India is very important to us. Maybe in the past, we were not as focused as we should be. We in Dr. Reddy's see India as very important to us. This is a home-based market. This is where Dr. Reddy came up. We used to be an important player in India. We are coming back with new management, with new brands, with a renewed brand into India. We actually now are growing faster than the market in India, the same we do in China, in Russia and in other markets. This is one bullet point.

Second, we have positioned ourselves well to customers. The customers naturally, and this is a message I know you heard from other companies bigger than us, but we also see stabilization in terms of price pressure. The discussion now is more about supply. It's about new products. We have a very healthy delivery of new products. In the last few months we launched 15 products. We are going to see two to three launches every month for the next months to come, as the portfolio was accumulated and yield the relevant results. Some of those products are exciting products. In that respect, we are positioned to our customers that if there is a supply issue, a disruption issue, we would love to help to cater to them, given the fact that we have the capacity and we have the right costs to address. We will continue to focus, we focused and we made certain steps on costs, as I mentioned it and we will continue to do that also in the future.

Improve efficiency, and being with the relevant costs structure in order to enable any pricing scenario in any of the markets is very, very important for us. I mentioned, for us, every product under any scenario needs to provide at least 20 percent EBITDA, no matter what is the scenario.

We started to divest non-strategic assets and we will continue to do so. It can be either the sites or the products that we do not believe that will achieve the relevant leadership, we will divest that. There is an effort. Already, you saw some of the announcements that we had in the last couple of months. We are going to see that also in the future.

We changed the management team. I am part of the change. Overall, about 70 percent of our management were changed in the last 18 months. This is a new management team, 100 percent professional. Very keen and very enthusiastic about the prospects of Dr. Reddy's and the growth opportunity that we have.

Last but not least, very important to us, we have some legacy quality issues with two of our sites. We are addressing them as I speak. Here, I would like to give an update as we are being asked on those. On our chemicals site we call it CTO 6, we submitted all the compliance responses to the FDA. Everything was submitted. Most of this, and this is why it took so long, we had to have third-party validation, as initially three-and-a-half years ago it was data integrity issue. We basically repeated all the relevant studies for a legacy of quite a few years with a third party to validate that the products are in the right place. We are awaiting re-inspection of the site, hopefully to finish with that. On the sterile plant we already got the re-inspection. We got 8 observations. We addressed the observations. We sent it over, and we're waiting for the response by the FDA. All the rest of the sites are with EIR, and are fully compliant and serving well all the countries. In our case, the approval for all the sites is by about 20 authorities.

Now, I want to go and elaborate a little bit on what we're going to do with each of the six spaces that we selected as a focus. The first one, naturally, in this conference is the US generics. This is a veteran space for us. Very important to us. We see ourselves growing also in that space. We do have a very, very exciting portfolio, which will be the main driver of our growth. 113 products to be exact, 32 out of them are first to file. Some of them really exciting, and some of them with very, very interesting IP position. In addition to that, we do see some nice potential OTC switch. In the OTC, we're primarily playing in the area of the private label. In this respect, we do see an opportunity for additional category to be launched, especially if the patient will be able to control the safety via digital or other means.

The next space is China. By the way, we are in China. We are in China, actually for the last 20 years. We are the largest foreign generic company in China, been there for the last 20 years selling about $100 million, about 10 products. We never left China, even when it was hard and hopefully now we can reap the benefit of it. The benefit will come, because on this infrastructure given the new regulation and especially the introduction of the GEA regulation, we saw that 70 products of our US portfolio can fit the GEA requirement of China, most of it, by the way, already in the stages of registrations, and some of it even going to be launched soon because we started registrations for them back. We do have sales force in China in some of the TAs. We do have a partnership with some other players, so we can choose whether to walk within the JV that we have in China, or outside of the JV. We have a great regulatory team that have a proof record of success, in registering products in China. For us, it's about going big into China by introducing much more product. 70 instead of 10 that we have right now, and to do it within the changes of the landscape in China.

Russia and India are both branded generic markets, so it's about playing in the retail, playing with mega brands. In both of them, we do have some legacy, big brands, for example, Omez, the omeprazole. Our planning to focus on extending those brands or launching additional brands in each one of these countries, about 5 or 6 therapeutic areas. In the case of Russia, it's including the OTC. They also fall especially for India, we do have a stream that we will also launch what we call specially or clinically differentiated product as well.

The API is in a way back to business. Two reasons for that. First of all, Dr. Reddy was always good with API. This was even the legacy, a franchise for Dr. Reddy's for many, many years. I remember in my Teva days competing against Dr. Reddy's and always respect very much the capability of Dr. Reddy's in the area of API. Now that I see from the Dr. Reddy's side, I can assure you that what we saw from the outside, we do also see from the inside that this are great capabilities. The recent changes in China in which there are less manufacturers and less, if you wish, desire to grow the API franchise in China actually bring the API back to India. Also, the notion that it's important to be back integrated. It was always important. May be when China was firming up and there were many suppliers out of China, it became less important to be back integrated. Now, it's going to be again there. We are well-positioned to do that. We are going to increase the level of back integration of the company plus serving others with third party, a model that was great for Dr. Reddy's, and I believe that will be great also going forward.

Global hospital: This is including the biologics, a market that is exciting. The beauty about this market for us, is that we can leverage product all over. Most of these businesses is a B2B business by participating in bids or tenders or you need relatively small force of account managers. It's not going to require a big investment in SGNA. This will allow us also to give and we do have a huge portfolio of injectables and focus on biosimilars in India, more of that will come. The composition of this portfolio is very, very attractive to many, many people around the world. This is where we want that our products will reach every town and every hospital that wish to have our product.

Six spaces, each one of them will grow. Each one of them will grow on it's own merit. There will be no cost subsidies between the spaces. Each one of them will have to stand on its own two feet. Each one of them will have to yield the return for investment and the KPI is naturally the profit, return on investment and growth.

With that, I would like to wrap up by basically giving the following message. We are focusing on execution in the short term. Profitable growth, shareholder returns, efficiency cost, quality compliance, this is in the short term. We are very busy with that. At the same time, we are gearing ourselves very, well for the long term. We will not shy away from inorganic. We will be an organic company in nature. The R&D will continue to be our bread and butter and our main meaningful growth. At the same time, there will be very, very attractive deals. We have the financial capacity and we have the ability to take it, but we will not go crazy. We will not pay any crazy multiples just to grow because for us, it's about being a great company, giving the right return for investment. It's not about the size in that respect.

With that, I think I have five minutes. If anyone wants to ask a question, please do.

Audience Member: I have a question. You have a slide where you showed 21 complex injectable/steriles filed, and 15 injectables filed. Are there any in those 36 that are long-acting injectables?

Erez: Yes, there are.

Audience Member: Thank you.

Audience Member: There was an [inaudible] better. Do you think it's going to be delayed because of government shut-down?

Erez: I don't know how to react to government shut-down.

Neha: One question, if I may ask.

Erez: Please.

Neha: You talked about not shying away from inorganic opportunities. The generic acquisitions have become pretty attractive as we have seen in the recent deals. Would you be open to doing more generic deals versus acquiring specialty assets? What's your view there?

Erez: We are going to focus on generic in general. We will have some specialty, but our main bread and butter is about affordable medicine, and giving accelerated access to affordable medicines. This is our bread and butter. This is where we are going to be. May be there was a perception in the past that we are becoming from a generic company to a specialty company. This is not the case. We are generic company and will stay generic company in that respect. May be here and there we will have a nice asset in specialty that can serve us well. In that respect, the main effort will be, if at all, complementary moves in the generic area.

Audience Member: This would be in the US market or are you open to others also ?

Erez: We are open for each one of the six spaces that I mentioned.

Neha: Since we’re discussing on, any update on generic Suboxone litigation?

Erez: Sure. Thank you for that. As you know, we are under PI. We won PI in November '18. We are still waiting for the mandate to be issued. The reason that the mandate was not issued is because the innovator asked for rehearing. This is now pending with the court. If this rehearing will be denied and if there are no other legal procedure like Supreme Court or something like that, we will launch the product, and for us, best case scenario is to launch it this month.

Neha: Any other questions?

Audience Member: [inaudible] work against you in the US market?

Erez: No, it will not. As OTCs, first of all, we don't have right now in India and China, the same portfolio the same as we have in the US, so we don't see that. This is one. Second, as odd as it sounds, the prices are not creating such a value that people believe they do. That's the way we see it.

Audience Member: Do you see the US generic market pricing eroding, continuing or stabilizing?

Erez: For us, in the last couple of months, it stabilized. In that respect, I can also add a little angle to what the other players in the industry are saying.

Audience Member: You talked about Europe, your approach in Europe.

Erez: We are under scaling Europe. We do have a franchise in Germany and the UK primarily on the retail side. The Germany is the legacy Betapharm and the UK was an organic move that we did through the years. We do want to scale better in those two countries but we are still very, very small, and I may say insignificant in Europe, as we speak. We need to improve that.

Neha: Thank you so much.

Erez: Thank you so much for listening to us.