DR. REDDY'S

Creating a Global Enterprise

ANNUAL REPORT 2005–06 DR. REDDY'S LABORATORIES LIMITED

CREATING A GLOBAL ENTERPRISE

In the world of matter, a drop of liquid diffuses slowly in another and forms a pattern that it is distinctive, reflective of its nature.

Through more than a decade of steady effort and guided by an unswerving original vision, Dr. Reddy's Laboratories has been growing into a business that has earned the right to be called global. When a business evolves, rather than changes suddenly, its growth is likely to endure.

This year's cover images, as a whole, tell the story of this transformation. The front shows how an enterprise, like a drop of reagent, can take a global shape in its own distinctive way, guided by its inherent nature. The back cover reflects our focus on three continental geographies and in the inside covers are images of diffusion, reflective of our creative energy.

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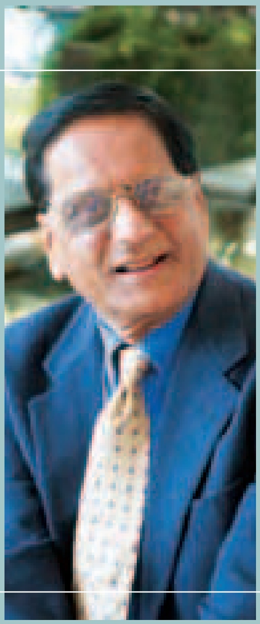
chairman's letter

Dear Shareholders

2005-06 has been a momentous transformational year in the history of your Company. The transformation is not just of the company coming out of its financial and operation trough of 2004-05. It is about thinking out of the box, aggressively growing its businesses, making landmark deals and completing two significant global acquisitions.

2005-06 has proved to me that your Company has it in its DNA to quickly overcome adversity and get back on to the path of rapid and broad-based growth to realise its vision of becoming a discovery-led global pharmaceutical company.



DR. K ANJI REDDY
CHAIRMAN

> In my last year's letter to you, I had written, "There is nothing like a year of adversity to strengthen, re-focus and re-channel entrepreneurial drives." That is exactly what has happened in 2005-06 — and has occurred across various businesses of your Company.

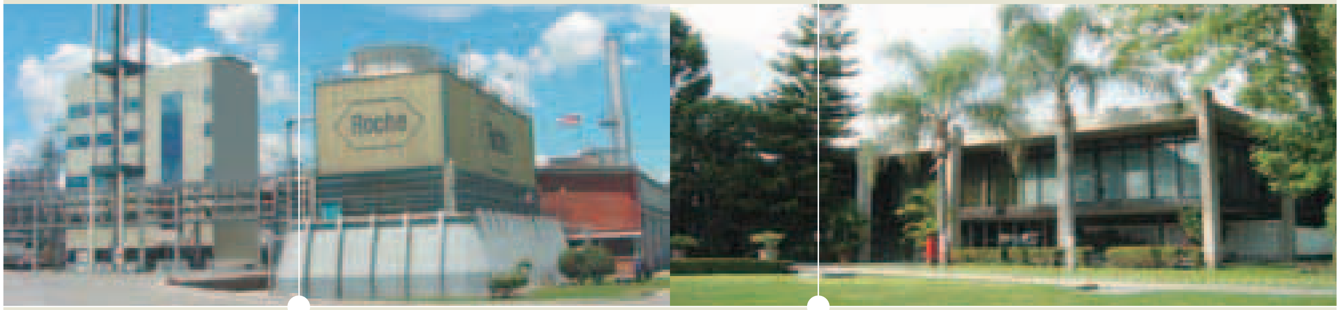
If you will recollect, 2004-05 was a difficult and challenging year. Consolidated revenues had declined; and profits had fallen precipitously. In my last year's letter to you, I had written, "There is nothing like a year of adversity to strengthen, re-focus and re-channel entrepreneurial drives." That is exactly what has happened in 2005-06 — and has occurred across various businesses of your Company.

Let me share with you some of the major developments of the year.

On a consolidated basis and as per U.S.GAAP, your Company's revenues have grown by almost 24 per cent to Rs.24.3 billion in 2005-06. Thus, for the first time in its history, it has comfortably crossed the U.S.$500 million mark. Net profits have increased from a mere Rs.211 million in 2004-05 to Rs.1.6 billion in 2005-06. And earning per share has increased from Rs.2.76 to Rs.21.24.

These numbers reflect fundamental changes in your Company's ways of doing business. I would like to touch upon a few of these.

To begin with, we have become more aggressive in growing our businesses. The Branded Formulations team has succeeded in increasing its revenues by 27 per cent to Rs.9.9 billion — and has done so in international markets as well as in India. Revenue from Active Pharmaceutical Ingredients (API) has grown by 19 per cent to Rs.8.2 billion.



In March 2006, we completed the acquisition of the betapharm Group, Germany's fourth largest Generics pharmaceutical company for an all cash deal of €483 million — which, I am told is largest international acquisition made by an Indian company up to date. It has a portfolio of 145 marketed products and several more in the pipeline.

Sustained efforts of the Generics business in Europe have helped overcome difficult market conditions in the U.S.; and revenues have grown by 13 per cent to Rs.4.1 billion. Customs Pharmaceutical Services (CPS) has grown its stand-alone business by 68 per cent to Rs.523 million; with its Mexican acquisition — which I will share with you shortly — revenues have grown to Rs.1.3 billion. These are examples of the re-discovered energy of your Company's employees.

But there is more. Instead of purely focusing on organic growth and cost cutting, your Company's senior management decided that it was time to leverage the cash in its balance sheet to actively scout for international acquisitions.

In November 2005, your Company purchased Roche's API business, its order books and its state of the art manufacturing plant at Cuernavaca in Mexico for U.S.$61 million. This acquisition alone increased Dr. Reddy's fourth quarter revenue by Rs.804 million and will help the Company's CPS business to grow from around U.S.$12 million to U.S.$100 million in the next 15 months.

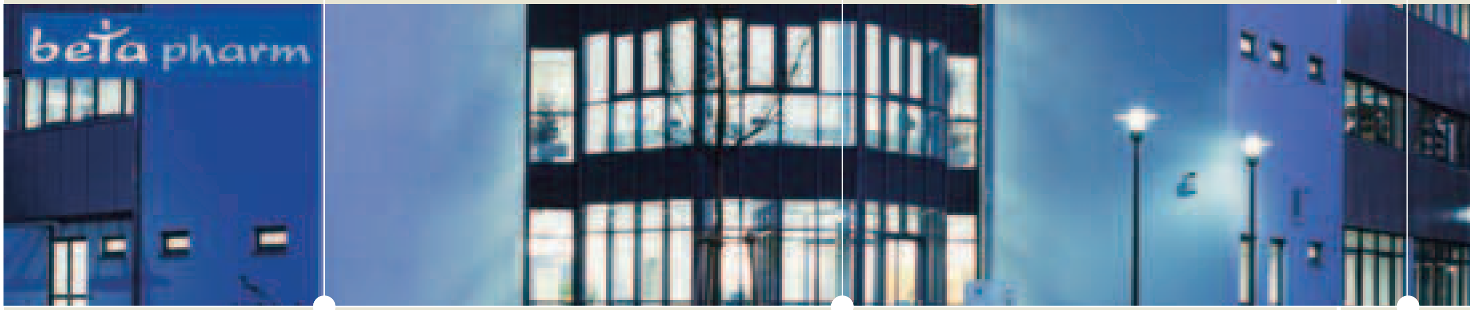
In March 2006, your Company completed the acquisition of the betapharm Group, Germany's fourth largest Generics pharmaceutical company for an all cash deal of €483 million — which, I am told is largest international acquisition made by an Indian company up to date. With a portfolio of 145 marketed products and several more in the pipeline, betapharm had a turnover of €164 million in 2005. This is expected to increase in the future. More significantly it gives your Company a strong foothold in the large German Generics market.

Given the way in which your Company's management is charged up and its successes in integrating these international entities, something tells me that you may well be seeing more global acquisitions in the coming years.

The scientist in me is delighted in the way your Company has re-engineered its R&D and has built an even stronger pipeline for the future. Last year, I wrote about the need for 'smart R&D'. We are seeing that happen at Dr. Reddy's on several fronts.

In March 2006, your Company concluded a landmark deal in discovery research where Dr. Reddy's, Citigroup Venture and ICICI Venture joined hands to form an integrated drug development company called Perlecan Pharma Private Limited with an equity capital commitment of U.S.$52.5 million. In this deal, Dr. Reddy's has transferred to Perlecan all rights and titles of four discovery molecules in the area of cardiovascular and metabolic disorders. Perlecan's priority is to accelerate the development of these molecules and thereafter seek out-licensing, co-development or joint commercialisation opportunities.

Also in the year, Dr. Reddy's and Rheoscience A/S have agreed to co-partner the development of balaglitazone (DRF 2593) a partial PPAR-gamma agonist for the treatment of Type 2 diabetes, which is expected to move to Phase III clinical trials. The



arrangement allows Dr. Reddy's to keep its full rights for North America, Japan and the rest of the world, except Europe (excluding Russia and CIS) and China.

Today, five of the Company's seven key NCEs have advanced to clinical development. And there are a few in pre-clinical that are showing considerable promise.

In addition, we have significantly strengthened our Generics and API pipelines. In 2005-06, your Company filed 12 Abbreviated New Drug Applications (ANDAs), taking the total number of ANDA filings to 70. As of March 31, 2006, our U.S. Generics pipeline comprised 49 ANDAs pending with the U.S. Food and Drugs Administration, including 29 Para IVs. As far as APIs are concerned, the Company increased the number of products in its Drug Master File (DMF) by 30 during 2005-06, of which 17 were U.S. DMFs, 8 Canadian and 5 European. The total number of DMFs now stand at 151 — 81 filed in the U.S., 28 in Canada and 42 in Europe.

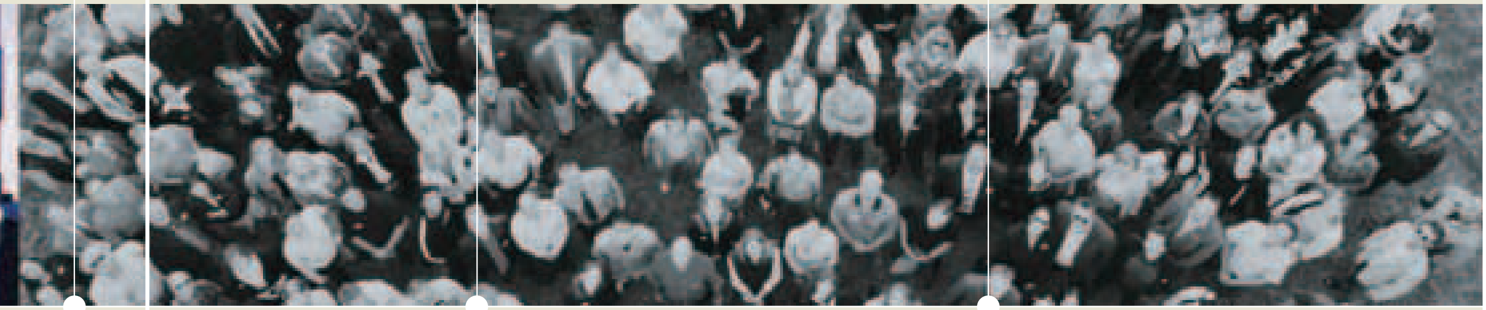
Thus, 2005-06 has seen growth in revenues, increase in profitability, two significant global acquisitions and a fundamental re-engineering of its R&D and product pipeline. Something else has also occurred which I need to share with you.

As you know, we are a company that is also listed on the New York Stock Exchange and thus, subject to the laws and regulations of the U.S. Securities and Exchanges Commission (SEC). In 2002 the U.S. passed the Sarbanes-Oxley Act (SOX), which imposed stringent corporate governance conditions and internal control over financial reporting on all companies registered with the SEC. As a foreign registrant, your Company had to comply with Section 404 of SOX by March 31, 2007.

Instead of waiting for the deadline, we took the view that this is a worthy exercise which needed to be fast-forwarded. Therefore, 18 months ago, we began an all-out effort to comply with the provisions of SOX-404 of the Sarbanes Oxley Act, 2002.

I am delighted to inform you that your Company has become SOX-404 compliant 10 months before the mandated deadline. That makes us one of the earliest Asian companies to be SOX compliant — and demonstrates our commitment to having global

+The scientist in me is delighted in the way in which your Company has re-engineered its R&D and has built an even stronger pipeline for the future. Last year, I wrote about the need for 'smart R&D'. We are seeing that happen at Dr. Reddy's on several fronts.



I am delighted to inform you that your Company has become SOX-404 compliant 10 months before the mandated deadline. That makes us one of the earliest Asian companies to be SOX compliant — and demonstrates our commitment to having global best-in-class internal control processes and corporate governance procedures.

best-in-class internal control processes and corporate governance procedures.

Adversity brings with it optimism. Successful growth ought to be accompanied with a few words of warning. We have done well. However, there are many challenges ahead. There is a challenge of successful integration; of being a global company with over 2,000 employees at international locations; of creating global managerial talent pools; of dealing with increasing competitive pressures in the Generics and API businesses; of systematically making successful launches across the entire produce space; of further developing the Company's NCE pipeline; and of maintaining the momentum of rapid transformation to become a globally recognised, discovery-led international pharmaceutical player.

These are the challenges of growth. I am confident that your Company's employees — both within and outside India — will surmount each of them. And, with your support, deliver even better therapeutic solutions while generating superior shareholder value.

Yours sincerely,

K anji reddy

DR. K ANJI REDDY
CHAIRMAN

key highlights

BASED ON U.S.GAAP FINANCIALS

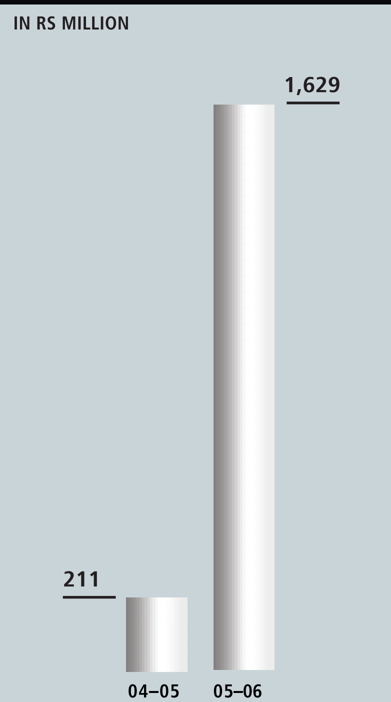
ACQUISITIONS

- **ACQUISITION OF BETAPHARM,** the fourth largest generics company in Germany, for €483 million ($584 million) in cash. The combination of Dr. Reddy's and betapharm offers an excellent opportunity to build on the unique strengths of each company to emerge as a leading generics player in Europe.
- **ACQUISITION OF ROCHE'S API BUSINESS** at the manufacturing site in Cuernavaca, Mexico including all employees and business supply contracts for U.S.$61.5 million. This will help Dr. Reddy's to emerge as a leading player in Customs Pharmaceutical Services (CPS) segment and position itself as a partner of choice for strategic outsourcing needs of global innovator companies.

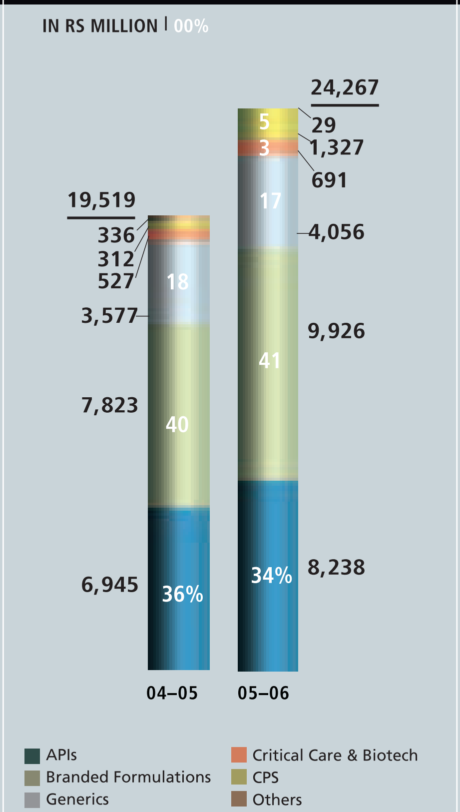
FINANCIALS HIGHLIGHTS

- **REVENUES CROSS** the milestone of U.S.$500 million driven by a well diversified business and market growth
- **TOTAL CONSOLIDATED** revenues rises by 24.3 per cent — from Rs.19,519 million in 2004-05 to Rs.24,267 million in 2005-06.
- **REVENUES FROM** Active Pharmaceutical Ingredients and Intermediates **(API)** grows by 19 per cent to Rs.8,238 million.
- **REVENUES FROM BRANDED FORMULATIONS** increases by 27 per cent to Rs.9,926 million.
- **REVENUES FROM GENERICS** grows by 13 per cent to Rs.4,056 million, including 28 days revenue from betapharm — Dr. Reddy's German acquisition.
- **REVENUES FROM CUSTOMS PHARMACEUTICAL SERVICES** rises from Rs.312 million to Rs.1,327 million, including fourth quarter revenue from Dr. Reddy's Mexican acquisition.
- **R&D SPEND** net of income under the ICICI Venture Capital Funds Management Company – Generics deal at Rs.2,153 million, reflecting a decline of 23 per cent over 2004-05.
- **PROFIT AFTER TAX** increases to Rs.1,629 million from Rs.211 million in 2004-05. This growth also includes the profit from the sale of formulations facility in Goa, India.
- **FULLY DILUTED EARNINGS PER SHARE** (EPS) grows from Rs.2.76 in 2004-05 to Rs.21.24 in 2005-06.

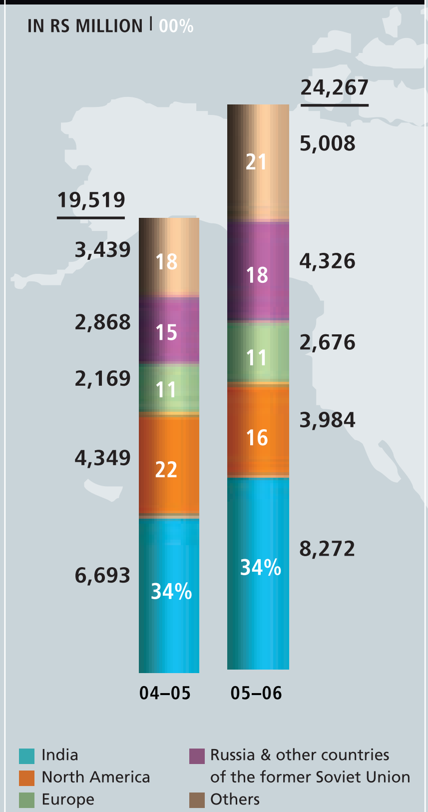
PROFIT AFTER TAX



BUSINESS REVENUE MIX



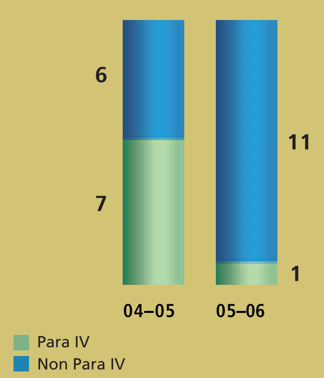
GEOGRAPHIC REVENUE MIX



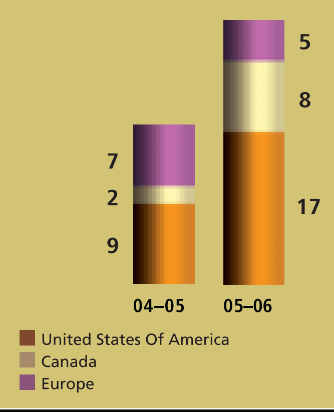
CORPORATE ALLIANCES

- **PROMOTED INDIA'S FIRST** integrated drug development company, Perlecan Pharma Private Limited, together with ICICI Venture Capital Funds Management Company and Citigroup Venture Capital International Growth Partnership Mauritius Limited. Perlecan will be engaged in the clinical development and out-licencing of New Chemical Entities (NCEs) assets. As part of agreement, Dr. Reddy's has assigned all rights in respect of four NCEs.
- **AGREEMENT WITH RHEOSCIENCE A/S** for joint development and commercialisation of balaglitazone (DRF 2593) for the treatment of type 2 diabetes.
- **COLLABORATION WITH ARGENTA DISCOVERY LIMITED** for joint development and commercialisation of a novel approach to the treatment of Chronic Obstructive Pulmonary Disease.
- **AGREEMENT WITH MERCK & CO., INC.,** allowing the company to distribute and sell authorised generic versions of Proscar® and Zocor® provided there is 180-day exclusivity for the first-to-filer for either product.

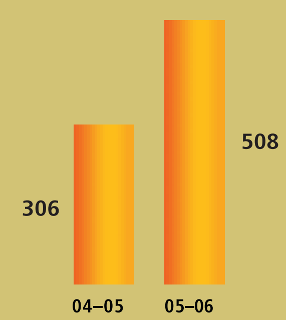
ANDAs IN U.S.



DMFs

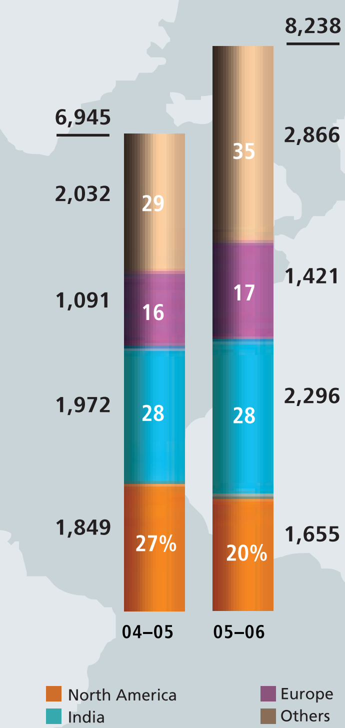


FORMULATIONS INTERNATIONAL DOSSIERS



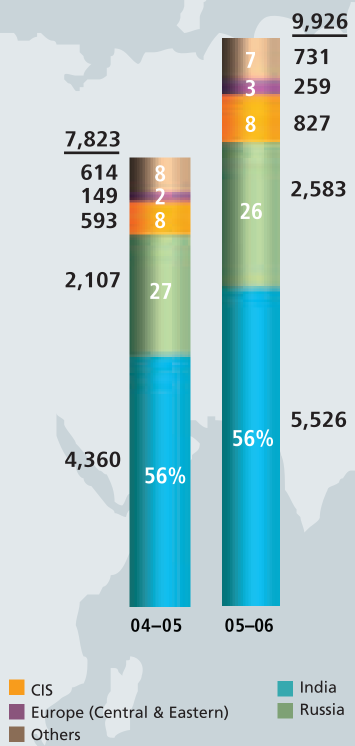
GEOGRAPHIC MIX OF APIs

IN RS MILLION | 00%



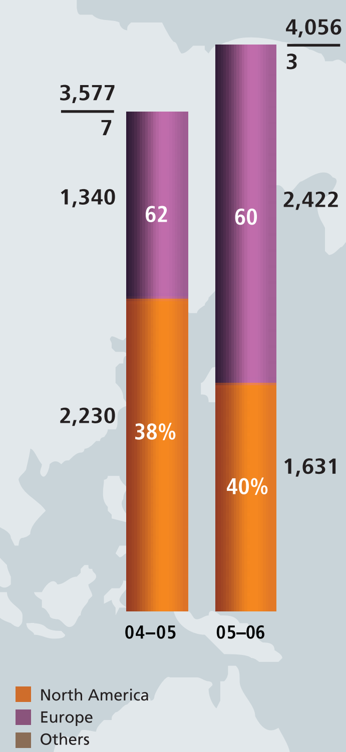
OF BRANDED FORMULATIONS

IN RS MILLION | 00%



OF GENERICS

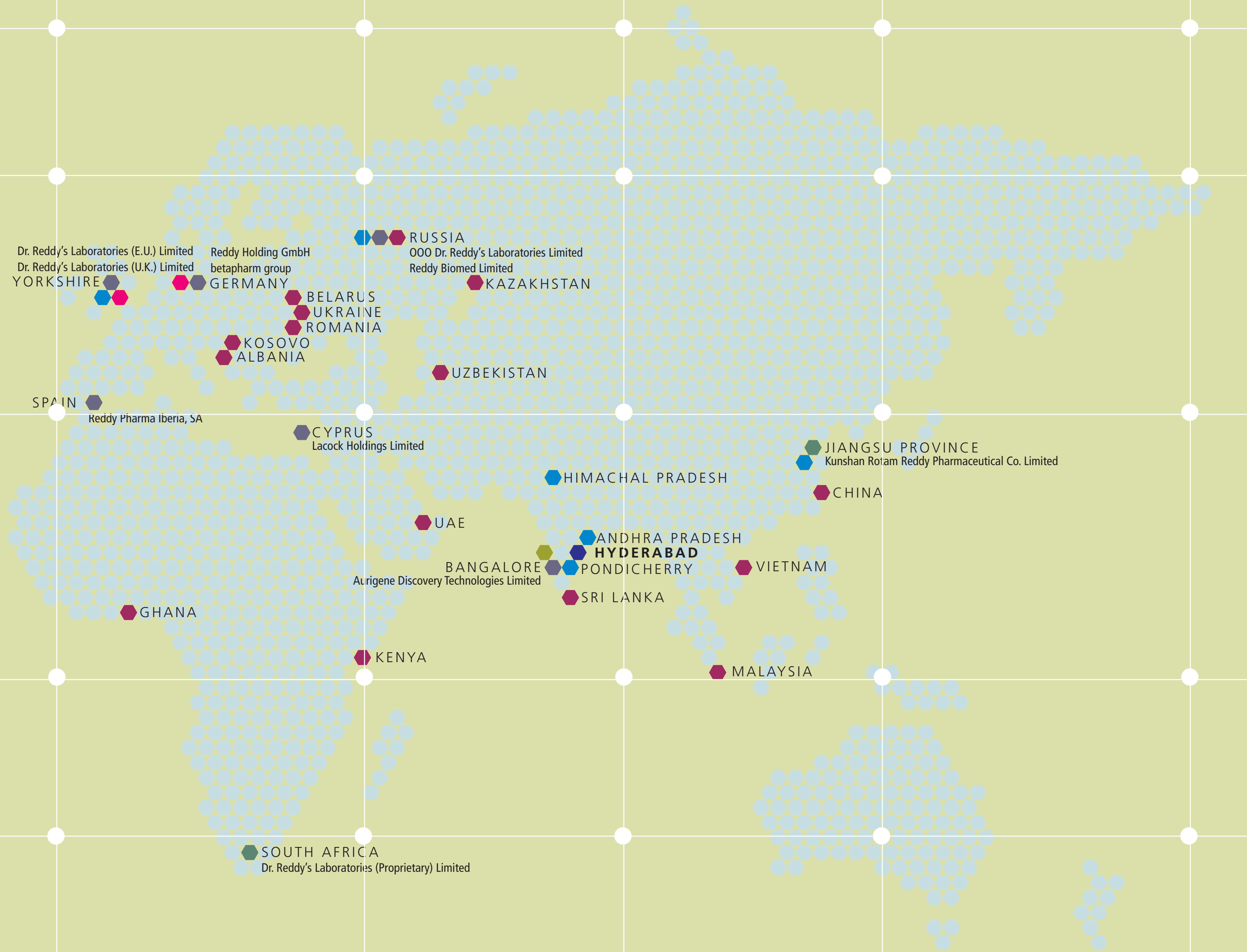
IN RS MILLION | 00%



Dr. Reddy's transformational journey

On March 3, 2006, Dr. Reddy's Laboratories (or Dr. Reddy's) fully acquired the betapharm Group, Germany's fourth largest generics pharmaceuticals company with over 370 employees and a turnover of €164 million. This closely followed Dr. Reddy's purchase of Roche's state-of-the-art active pharmaceuticals ingredients (API) manufacturing facility in Mexico along with its order books in November 2005.

Thus, by the end of 2005-06, Dr. Reddy's effectively became a global pharmaceutical player — one that not only supplied medicine throughout the world but also owned manufacturing bases and full fledged business



organisations in different parts of the globe. International operations accounted for 66 per cent of the Company's revenues in 2005-06. With betapharm and the Mexican facility fully coming into the fold, we believe that almost 80 per cent of the Company's consolidated revenues in 2006-07 will come from international operations. That will clearly make Dr. Reddy's a global player in the true sense of the term and bring it even closer to its vision of becoming a discovery-led global pharmaceutical Company.

That wasn't so even a year ago. 2004-05 saw a 3 per cent decline in the Company's revenues over the previous year, accompanied by a very sharp reduction in profit after tax. However, instead of concentrating only on cutting down costs, Dr. Reddy's chose to re-commit its businesses, strategies and organisational architecture to becoming a shareholder value enhancing global pharmaceutical player.

At a broad strategy level, Dr. Reddy's intends to achieve its vision of becoming a discovery-led global pharmaceutical Company by building on two distinct business models — that of being a global generics player covering Active Pharmaceutical Ingredients (API) and Finished Dosages; and of being an innovation-based player that focuses on Specialty Pharmaceutical and Drug Discovery.

achieving record sales

build critical mass that can create a sustainable growth engine

greater level of customer engagement

actively pursuing several business development opportunities

Growth in the near-to-medium term will be driven by the global generics model, as we maximize the opportunities in our established businesses of APIs and Branded Formulations and acquire critical mass in our generics businesses in the U.S. and Europe through organic and inorganic routes. At the same time, we will continue with our calibrated investments and strategic collaborations in making the innovation-based businesses self-sustaining — one that creates powerful patent protected product franchises for the longer term.

This strategy has six key components — all of which have been revealed in the course of 2005-06.

PUSHING REVENUE GROWTH AND PROFIT MARGINS

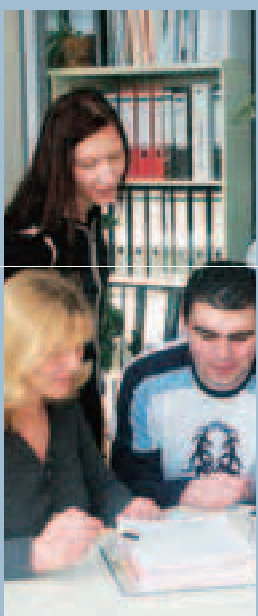
With severe pricing pressures in the increasingly competitive U.S. generics market, it was essential for Dr. Reddy's to increase its sales of APIs, Generics and Branded Formulations in more profitable geographies to offset the decline in U.S. revenues. The Company achieved this objective in 2005-06: total consolidated U.S.GAAP revenue increased by 24 per cent to Rs.24.3 billion. And post-tax profits grew from Rs.211 million in 2004-05 to Rs.1.6 billion in 2005-06. There were four elements of this growth.

First, achieving record sales of its more profitable offerings of Branded Formulations — which grew by 27 per cent to Rs.9.9 billion, driven by significant sales growth in Russia and CIS as well as an impressive upturn in the Indian market.

Second, pushing API sales, which grew by 19 per cent to Rs.8.2 billion in 2005-06.

Third, creating a niche market for Generics in Europe, which saw a 81 per cent sales growth to Rs.2.4 billion — driven by both greater volumes and higher prices in the U.K., as well as 28-days of revenue from betapharm.

Fourth, leveraging the Mexico acquisition to rapidly grow Customs Pharmaceuticals Services from Rs.312 million in 2004-05 to Rs.1.3 billion in 2005-06.



+T o sustain the growth momentum, we have expanded our sales force in India and Russia to drive market shares and maintain a steady flow of new product launches. Today, new products contribute about 5-6 per cent of total Branded Formulations revenue.

GROWING THE API, BRANDED FORMULATIONS, GENERICS AND CUSTOMS PHARMACEUTICALS SERVICES BUSINESSES

In the **GLOBAL API BUSINESS,** the Company is driving significantly greater level of customer engagement in key markets — which has resulted in the deepening of its product portfolio with major customers, and in creating global leadership for its key products. Moreover, the strategy also involves identifying unique product opportunities in major geographies, and protecting them through a strong patenting strategies. In API alone, Dr. Reddy's has a pipeline of over 81 cumulative drug master filings (DMF) in the U.S., 42 in Europe and 28 in Canada. With patent expiries in several markets in the next few years, the API business has its growth trajectory well laid out.

In **BRANDED FORMULATIONS BUSINESS,** Dr. Reddy's is investing in the key markets of India and Russia. To sustain the growth momentum, it has expanded its sales force in India and Russia to drive market shares and maintain a steady flow of new product launches. Today, new products contribute about 5-6 per cent of total Branded Formulations revenues, which the company aspires to ramp up to around 20 per cent in the next few years. We expect to sustain our growth momentum in Russia in the medium term. We also intend to build a sizeable presence in other key markets of South Africa, Brazil and China.

The **GENERICS BUSINESS** is best understood in terms of two key segments: the U.S. and Europe. In the U.S. Generics segment, our key priority is to build critical mass that can create a sustainable growth engine for the long-term. We believe that we now have a strong generics pipeline that help to start achieving this objective from 2006-07. Today, Dr. Reddy's generics pipeline is not only well populated but is also a judicious mix between relatively simple products that would


de-risking R&D
creating new discovery platforms
seven new chemical entities
accelerate clinical development of NCEs

be easy to launch and, therefore, subject to greater competition, and those that were complex, needed greater development and stronger IPR fencing to stave off competition and, thus, command greater post-launch pricing power.

Dr. Reddy's filed 12 abbreviated new drug applications (ANDAs) in 2005-06, taking the total number of ANDA filings to 70. More significantly, the year saw a record number of approvals for the company's ANDA filings: 5 final approvals and 7 tentative. As of March 31, 2006, the Company's U.S. Generics pipeline comprised 49 ANDAs pending with the U.S. Food and Drugs Administration, including 29 Para IVs.

In the U.S., we are also actively pursuing several business development initiatives to create additional growth opportunities: in-market product acquisitions, development alliances to complement Dr. Reddy's in-house pipeline expansion, and authorized generics deals. In 2005-06, we acquired three off-patent brands from Protein Design Labs. We also entered into development alliances for expanding our pipeline in oral solids as well as alternate dosage forms. Finally, we entered into a deal with Merck & Co., Inc. — the first of its kind from India — to sell the authorised generic versions of Zocor® and Proscar® if the 180-day marketing exclusivity is granted to the first filer on either product.

The two-year carcinogenicity studies have been completed, and the preliminary findings appear promising and should support its further development.

Driven by the betapharm acquisition, **EUROPEAN GENERICS BUSINESS** assumes significance to our long-term growth. Europe, now is our single largest geography and we have put in place a new leadership team to design and implement a pan-European strategy focused on building a significant presence in key markets. We intend to further build on betapharm's business in Germany, drive scale in the U.K., and expand our presence in other important markets of Europe. We are also exploring various business development opportunities in Spain, Italy and France. In May, we entered Spain with the acquisition of a small portfolio of in-market generic products and pending marketing authorisations.

In the **CUSTOMS PHARMACEUTICALS SERVICES (CPS) BUSINESS,** the integration of the Mexico acquisition has been completed successfully and we are already beginning to see the benefits. This business is well positioned to achieve the annual revenue mark of U.S.$100 million in the near term.

GROWING RESEARCH BY DE-RISKING R&D

In Drug Discovery, we have seven new chemical entities (NCEs), with four in clinical development and three in the pre-clinical stages. On the research side, the strategy is to continue expanding our discovery pipeline with greater focus on creating new discovery platforms in the chosen therapeutic areas of cardiovascular and metabolic disorders. On the development side, the objective is to advance the development of our NCE assets through a combination of in-house and co-development initiatives.

Our most advanced asset in clinical development is balaglitazone (DRF 2593), a partial PPAR-gamma agonist for the treatment of Type 2 diabetes. The two-year carcinogenicity studies have been completed and the preliminary findings appear promising and should support its further development.

With an increasing number of NCEs moving into clinical development, the key priority is to create a roadmap for commercialising these assets in key territories. This includes building the clinical development organisation, commercialisation capabilities and strategic partnerships and alliances for de-risking R&D while simultaneously unlocking the asset value of each NCE.

2005-06 saw two landmark deals in Discovery.

In March 2006, Dr. Reddy's, ICICI Venture Capital Fund Management Company and Citigroup Venture Capital International Growth Partnership Mauritius Limited concluded a deal to form an integrated drug development company called Perlecan Pharma Private Limited with an equity capital commitment of U.S.$52.5 million. In this deal, Dr. Reddy's

cost-effective
end-to-end global
supply chain

invest in
capacity
expansion

attain process
excellence

SOX–404 compliant

has transferred to Perlecan all rights and titles of four NCEs in the area of cardiovascular and metabolic disorders. Managed by an independent Board of Directors and a dedicated management team, Perlecan's priority is to accelerate the development of these assets up to Phase IIa and thereafter seek out-licensing, co-development or joint commercialisation opportunities.

Dr. Reddy's and Rheoscience A/S have agreed to co-partner the development of balaglitazone which appears to be set to move to Phase III clinical trials. The arrangement allows Dr. Reddy's to keep its full rights for North America, Japan and the rest of the world, except Europe (excluding Russia and CIS) and China.

Going forward, one can expect similar innovative deals.

CAPACITY EXPANSION

The fourth leg of Dr. Reddy's transformation and growth strategy has been rapid building of plant capacities. This involved de-bottlenecking of existing capacities and adding new lines, especially to meet the growing international demand for generics and Customs Pharmaceuticals Services. Within the first half of 2006-07, the Company will have enough capacity to produce over 10 billion tablets and capsules. Even that will not be enough. Therefore, the future will see more capacity expansion to further ramp up the production of API and finished dosages globally.

The growth strategy involves de-bottlenecking of existing capacities and adding new lines, especially to meet the growing international demand for branded formulations and generics.

GREATER SYSTEMIC FOCUS ON INTERNAL CONTROLS AND SUPPLY CHAIN

When businesses grow rapidly across many geographies, they typically strain internal control systems. Realising this fairly early on, Dr. Reddy's has executed several initiatives over the last few years, three of which need mentioning.

The first has been the setting up of the Company's GLOBAL BUSINESS SERVICES ORGANISATION in March 2004 to leverage people, processes and technology to attain process excellence in finance, SAP management, internal controls, insurance and employee services. The initiative uses the Six-Sigma approach. Today, most of Dr. Reddy's metrics for the Global Business Services Organisation have surpassed 4-sigma, signifying over 99 per cent transactional accuracy.

The second initiative is called Project DISHA, which aims at creating an even more efficient, cost-effective end-to-end global supply chain solution across all its businesses. The process is being implemented and when fully operational, is expected to significantly reduce logistics costs of the company.

The third and perhaps most significant, initiative has been Project SURAKSHA, which involves company-wide implementation of best-in-class internal control requirement for ensuring accuracy of financial reporting as required by Section 404 of the Sarbanes Oxley Act, 2002 (or SOX). Although compliance with Section 404 was mandatory for Dr. Reddy's only as on March 31, 2007, the company consciously decided to fast track the process. Consequently, all key control elements that constitute SOX 404 compliance have been documented, tested and remediated wherever necessary. On May 31, 2006, the Company became complaint with SOX 404. That makes Dr. Reddy's one of the earliest foreign SEC registrants to have met the stringent SOX 404 criteria, and first manufacturing company in India.

ACQUISITIONS

Even in the difficult days of 2004-05, Dr. Reddy's realised that organic growth was not enough. In order to become a mid-sized global pharmaceutical player, required a concerted focus on acquisitions. Fortunately, the Company had a strong balance sheet with hardly any long term debt, and cash and cash equivalents to the tune of U.S.$209 million on March 31, 2005. It therefore had the financial ability to make major acquisitions.

The first of 2005-06 was the purchase of Roche's API business, its order books and its

financial ability
to make overseas
acquisitions

truly global
company today

create a dynamic
and nurturing
cross-cultural
environment

accelerate
transformation

manufacturing plant at Cuernavaca in Mexico at an investment of U.S.$61 million. The plant, approved by the U.S.FDA and other international regulatory agencies, employs around 340 people and has a current portfolio comprising 18 products including mature APIs as well as a range of intermediates and steroids. This acquisition will facilitate Dr. Reddy's CPS business to grow from around U.S.$12 million to U.S.$100 million in the next 15 months.

The second acquisition during the year was that of the betapharm Group, Germany's fourth largest generics pharmaceuticals company. Dr. Reddy's entirely bought out betapharm in an all cash deal for €483 million. The company currently has a portfolio of 145 marketed products; has been the fastest growing large-sized generics company in Germany over the last five years; employs 370 people with a dedicated sales force of 250; and achieved a turnover of €164 million in 2005. betapharm has given Dr. Reddy's a strong foothold in the large German generics market.

2005-06, therefore, has been a year of accelerated transformation: of pulling out of the lows of the previous two years; of putting all the key long term initiatives in place; of de-risking R&D; of growing revenues through a healthier and diversified portfolio of businesses and geographies; and of leveraging the strength of the Company's balance sheet to make strategic acquisitions.

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All these initiative bring with them challenges that Dr. Reddy's will have to address and surmount in the future — the greatest being to orchestrate the next phase of growth in each of its businesses and to create the right organisational architecture to enable the Company to become a mid-sized global pharmaceutical Company in the medium-term.

There is the challenge of organisational integration in all its diverse aspects. Today, there are 1,300 international employees within Dr. Reddy's; another 340 in Mexico; and 370 people in betapharm. Thus, over 2,000 employees out of 7,525 are at other parts of the world. Dr. Reddy's needs to create a dynamic yet a nurturing cross-cultural environment that gets the best out of everyone.

Then there is the challenge of creating and growing managerial talent pools throughout its businesses and empowering them with the entrepreneurial drive that is needed to succeed in global operations.

There is the challenge of sustaining and further developing each of our key business process initiatives — to ensure that these become a part of the DNA of the organisation.

There is the challenge of maintaining the momentum of rapid transformation and also creating the excitement needed to further accelerate the process of change.

There are challenges of seeking newer business opportunities wherever they arise and opening up hitherto untapped geographies either organically or through other acquisitions.

For a multi-faceted company like Dr. Reddy's, there is also the challenge of consistently scaling up the organisation — API, Generics, Branded Formulations, Customs Pharmaceutical Services, Biotechnology, the Specialty business, Tech-ops, R&D, and IPR creation and management. And to do so in a coherent and integrated way that generates greater revenues, higher profits, provides better therapeutic solutions, and creates a rapidly transforming corporation that can deliver consistently superior shareholder value.

All these are happy challenges. The challenges of growth and opportunity. The challenges of being a global pharmaceutical company. Which is what Dr. Reddy's has become.

inspired people, breakthrough performance

A person is often judged by the company she keeps. An organization is often judged by the people it keeps. As Dr. Reddy's moves into its 22nd year of existence, we can only reiterate that our people have made all the difference to us. From our humble beginnings, through all our appointments and disappointments, we have been proud of our people and the way we have earned their sense of engagement.

Today Dr. Reddy's has a widespread presence across the globe - with direct presence in across 40 geographies and intensifying that presence by major acquisitions in the past year. Today we have over 7,500 associates working with us in different corners of the world. Over 2,000 of them, including more than a quarter of our Management Council, are at international locations. **Truly, the sun never sets on Dr. Reddy's!**

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This leads to a challenge that has not been faced by many science led Indian companies- diversity integration.This, however, is not new to us, as we have been working towards this in various ways over a period of time. Diversity in our talent gene pool has been a conscious choice for us. As we spread our wings, we are trying to help integrate such diversity to build a truly global organization. We have used our strong people-centric ethic and values as an integrating lever, both in our organic and inorganic growth.

As we build our business, we are conscious of the need to derisk it and also to make our people infrastructure scalable. From a Human Resources viewpoint, it means constantly keeping the talent pipeline flowing. We continue to have an excellent employer brand. Our recruitment engine has been revved up substantially. We have been able to attract talent globally, especially in the cutting edge areas of R&D. Our innovative and technology-supported efforts have not only helped us develop a very cost effective hiring process but also earned us prestigious accolades. We received the internationally reputed RECRUITING AND STAFFING BEST IN CLASS (RASBIC) AWARD for 2005, the first time these have been given in India.

We have successfully institutionalized TALENT MANAGEMENT BOARDS in all our Businesses. These have helped us identify and track high potential to facilitate building pipelines to all key positions. We have also initiated a high-focus mentoring, initiative driven by the members of the Management Council. We have sustained our 'equal opportunity' approach to careers by internally advertising all positions. We have made appropriate interventions in our organization design at different slices to create more focussed responsibility centers, a higher collaborative environment and quicker turnaround times to ensure that the organization spots and converts all meaningful business opportunities.

ANKUR, our "virtual corporate university" continues to spearhead customized skill building initiatives. This year, apart from our previous tie up with BITS for the M.Sc program, we have also collaborated with the Narsee Monjee Institute of Management and Higher Studies, Mumbai, one of the top 10 business schools in India, to offer an MBA program to our employees with an exclusive focus on Pharma. We expect that this will not only foster the learning environment we have but also provide us the talent that we need a couple of years down the line.

We hosted two Technical Conclaves to continually keep our scientific community abreast of cutting edge technology and also the opportunity to interact with thought leaders in our interest areas of science. Over the course of the year we have invested in 9000 man-days of training.

We hosted two TECHNICAL CONCLAVES to continually keep our scientific community abreast of cutting edge technology and also the opportunity to interact with thought leaders in our interest areas of science. Over the course of the year we have invested in 9,000 man-days of training. We have also improved our own internal capability to deliver greater learning. External certification for internal trainers has added sinew to our capability to deliver more relevant and customized in-house programmes across different functional areas.

All these strategic initiatives, we are confident, will sustain our LEADERSHIP DEVELOPMENT ENGINE, that is critical as we build a strong organization to sustain our ambition.

Nursing this aspiration also entails setting high performance standards. Excellence in performance cannot remain a mere buzzword. We are convinced that a strong performance ethic is the way to manage performance. As we strive towards execution excellence, we have suitably adapted our performance management processes. This year, we implemented a variant of the BALANCED SCORE CARD for all our Businesses and Corporate functions. The focus has been on clear outcomes: financial, customer, business building and organization building. This approach has helped us consolidate an immediate term performance while not neglecting our long-term interests.

As a high performing organization, we aligned the rewards distribution with these scorecards. We have introduced a very innovative VARIABLE PAY PLAN that aggressively rewards better performers, bring in substantial differentiation in rewards and motivates our employees for higher performance outcomes. Our robust review systems, practised meritocracy, a fair and transparent integrated rewards strategy in line with our organizational strategy and values nourishes and sustains a high performance culture, committed to entrepreneurship and innovation.

Best-in-class technology is another focus as we tone up our people processes to substantially improve our employee transaction processing. The Employee Services Team in our Global Business Services group has evolved this year into a robust support group, driven by Six Sigma metrics. We have now embarked on a huge organization wide initiative to reconfigure our ERP and are implementing mySAP BUSINESS Suite. This will enable end-to-end process support to Human Capital Management modules that, in turn, shall improve operational efficiency, enable execution excellence and to speed up processes. And of course give our employees a more real-time support to make our workplace even more reassuring.This year, we have integrated our entire India operations sales force on a platform called DRLINTOUCH. This enables the field force of 1650 employees view and operate a single integrated platform, helping increase the service levels of all the employee-related processes and queries by reducing the transit time. Most importantly, we have improved the levels of transparency and accountability in the processes.

In Dr. Reddy's, we believe that our associates must have real time information about our strategy, performance, challenges and victories. We have thus institutionalized a multiple-channel communication approach. The Quarterly Communication Session to the top 100 Managers helps explain business performance and challenges. The concomitant cascade down the line is reinforced by a bimonthly communiqué from the CEO to all. Unit level group sessions, skip level meets, factory level 'Get to know your colleague' sessions, ELIXIR, the house magazine of the corporation, specific business newsletters and even the maiden web cast of the Celebrations Awards Nite help a fast growing organization connect with a vast and diverse workforce.

Celebrating successes, big or small, sustains a performance driven culture. We have institutionalized the element of recognition in our way of life. Whether these are spot recognition actions on the ground or various levels of awards at the Business or Corporate level, we acknowledge extraordinary effort. In many of these, we involve the families, who are often the inspiration behind the effort and toil that builds a great organization. And we know that inspired people deliver breakthrough performance.

different locations. We have rolled out the CODE OF BUSINESS CONDUCT AND ETHICS (COBE) globally to ensure that every one in the organization is strongly committed to our values. Our OMBUDSMAN PROCESS, with the WHISTLEBLOWER provision, has strengthened our resolve to build accountability at all levels even as it has enabled both employees and external stakeholders to point out any omissions without fear.

Success to us is about Vision- ours. It is the ability to rise above the immediacy of any situation. It is

One of the key drivers in our business is our adherence to our core values. This is not just any document that gets displayed and referred to at important occasions- it is a way of life for us. To reinforce it, we have continued to leverage it in all our people processes (hiring, performance reviews, rewards management and career development) and built further on the concept of Values Week in

about imagination. It is about sensitivity to people. It is about building inclusion. It is about connectedness to a larger world existence. It is about personal tenacity. It is about giving back more to life than you take out of it. It is about creating extra-ordinary success with ordinary lives. And that is what we at Dr. Reddy's strive for - everyday - all the time - all over the world.

safety, health and environment

As a part of our commitment towards the principles of sustainable development, the safety, health and environment continue to be the priority areas.

We published the Sustainability Report for the last two years giving the full account of our activities in the area of safety, health and environment going much beyond the statutory requirements. The sustainability report is prepared as per the internationally accepted guidelines issued by Global Reporting Initiatives, commonly known as GRI guidelines. GRI is an official collaborating center of United Nations Environment Program (UNEP) and works in cooperation with UN Secretary-General Kofi Annan's Global compact. Out of about 823 companies worldwide, who currently publish the sustainability reports, only 8 are Indian companies and we are the first Indian company from Health Care Product Sector to be registered on GRI database. We will continue with this initiative of publishing the sustainability report in the future as well.

Some of the major activities in the area of safety, health and environment are as follows:

1. With the commissioning of the wastewater recycling plants at three locations of API units, most of the effluent from API units is now treated and recycled back into the plant. Continuous improvements are being done in these plants.
2. FTO Unit 2 obtained ISO 14001 – 2004 certification.
3. Generics (FTO–3) earlier obtained the ISO 14001-1996 certification. During the financial year, this was renewed to ISO 14001-2004.
4. At Discovery Research, Hyderabad, well-designed effluent treatment plant was commissioned. The plant design is based on technology known as Chemo Autotropic Activated Carbon Oxidation (CACCO Technology), developed by Central Leather Research Institute, Chennai
5. Regular workplace monitoring at strategic locations within all plants is being carried out to ensure that the exposures of the chemicals are well below the limits prescribed. Periodical medical check ups of the employees are also carried out as a part of safety activity.
6. Mock drills for training the staff to efficiently handle the emergency situation are being carried out

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regularly at all locations. On certain occasions, the local fire brigade personals are also involved.

7. Continuous training of the staff at all levels in the different areas of SHE forms an important activity in the area of safety and environment.
8. To foster the SHE culture across the organization, the National Safety Day & the World Environment Day were celebrated on 4th March and 5th June respectively. On the occasion of the National Safety Day, the Gold Star Helmets were awarded to six safety champions in API units, who contributed significantly in the area of SHE during the year.
9. Tree plantation drive is an ongoing activity for all units. During the year, API Unit 5, planted more than 10,000 saplings in and around the plant.

Although we make all efforts to ensure safe operations, we are pained to report that during the financial year, we had an unfortunate incidence of a fatal accident of a contract worker at one of our units. We have a well-defined corporate guideline for the contractors' safety & the requisite systems are in place to train the contract workers. However, after this accident, we once again reviewed our systems and further strengthen the training and monitoring activities for the contract workers.

Our efforts in the area of safety, health and environment are appreciated by various organizations and during the year we received the following five awards:

1. Confederation of Indian Industry (CII) Southern Region – First Position Award for the Leadership and Excellence in Safety and Environment Management. This award was conferred on us for the innovative work we have done in the area of SHE.
2. Greentech Foundation Silver Award for the Environmental Excellence in pharmaceutical sector.
3. CII Shorabji Godrej Green Business Center (CII-GBS) – National Award for the Excellence in Water Management for the year 2005 to API Unit 2
4. Appreciation Certificate to API Unit 5, from Andhra Pradesh Pollution Control Board on the occasion of the World Environment Day in appreciation of the work done by the unit in the area of environmental protection.
5. CII Shorabji Godrej Green Business Center (CII-GBS) – National Award for the Excellence in Water Management for the year 2005 to API Unit 6.

social responsibility – Dr. Reddy's Foundation

Committed to serve the communities in which we live and work, Dr Reddy's has consistently supported Dr. Reddy's Foundation in finding breakthrough solutions to enhance livelihoods and education. As a result, in the year 2005-06, Dr. Reddy's Foundation's Livelihood Advancement Business School (LABS) provided sustainable livelihoods to more than 60,000 economically backward youth and the School Community Partnership in Education (SCOPE) reached out to more than 14,000 children by bringing quality education in schools.

Under the special project of Swarna Jayanthi Gram Swarozgar Yojana (SGSY) we aim to generate 35,000 livelihoods across 7 states of India.

LIVELIHOODS

NEW DEVELOPMENTS IN LABS

GRAMEEN LABS- Partnership with the **MINISTRY OF RURAL DEVELOPMENT (MORD), GOVERNMENT OF INDIA,** under the special project of Swarna Jayanthi Gram Swarozgar Yojana (SGSY) for generating 35,000 Livelihoods across 7 states of India. Under this project, starting from August 2005, 3,000 livelihoods have been achieved in the three states of Gujarat, Tamil Nadu & Jammu and Kashmir.

NEW PARTNERSHIPS

- Aide ET Action an INGO for implementing LABS for equitable rehabilitation of Tsunami victims focusing on dalits, women and other marginalized communities in Tamil Nadu & Pondicherry.
- Mineral Foundation of Goa and Dr. Reddy's Foundation for implementing LABS in Goa.
- ICICI One Source and Dr. Reddy's Foundation for I One LABS in Bangalore.
- Housing Environment, Urban Development & Dr. Reddy's Foundation in Chattisgarh for SPM LABS.
- International Labour Organisation & Dr. Reddy's Foundation for ILO LABS in Uttar Pradesh for the child labour.
- Victims Plan International and Dr. Reddy's Foundation in Indonesia.
- New Academies @ LABS: BPO, Micro Irrigation, Teaching and Retail sectors. The new academies resulted in more than 200 new economy livelihoods.
- Project Disha, which works towards career development for LABS alumni spread across the country.

LABS—MILESTONES ACHIEVED IN THE YEAR 2005-06

- GRAMEEN LABS (JAMMU AND KASHMIR, TAMIL NADU AND GUJARAT)— (3,051) in partnership with Ministry of Rural Development, Government of India.
- ANDHRA PRADESH— (14,231) in partnership with A.P. Urban Services for the poor, society for elimination of rural poverty, Municipal Corporation of Hyderabad & Department of Youth Services.

- KARNATAKA— (409) in partnership with KUIDFC, ICICI Onesource.
- TAMIL NADU— (317) in partnership with SST, Aide ET Action, Other corporates.
- CHATTISGARH— (2,448) in partnership with Housing Environment & Urban Development.
- UTTAR PRADESH— (754) in partnership with International Labour Organisation.
- GOA & MAHARASHTRA—in partnership with Mineral Foundation of Goa & Forbes Marshall respectively trained a total of 168 trainees.
- INTERNATIONAL—In Vietnam, LABS was operational in Hue in association with a Government Organisation, Center for Population, Family and Children (CPFC), LABS center was also operational in Da Nang, Hung Yen, Thanh Nhoa, and Ha Long in association with various local and international partners. Sri Lanka LABS was operational in partnership with Plan and 222 aspirants were trained in total.

NEW PROGRAMS IN LIVELIHOODS

- PROJECT AAROGYA—is a project with 100 mobile eateries in Karimnagar District, Andhra Pradesh to bring in hygienic practices and safe water provision. This was the first step towards bringing enterprise focus to LABS.
- CORNBYTES—is a Micro Entrepreneurial Project targeting

25 partially disabled youth of Ranga Reddy District, Andhra Pradesh. This unique project is being conceptualized looking into the on going demand for Sweet Corn Vending as an enterprise opportunity.

NEW DEVELOPMENTS IN EDUCATION

- SCOPE—intervention reached out to tribal children by setting up 28 schools and 4 tribal welfare residential hostels in 30 tribal villages in Khammam District, Andhra Pradesh.
- NEW PARTNERS—Quality Education for Skilled Training (QUEST): The QUEST Alliance works towards effective use of education technology for the underprivileged in India. QUEST is a consortium formed by U.S.AID in association with Dr. Reddy's Foundation, Azim Premji Foundation (APF), Pratham Educational Initiatives & WIPRO Foundation. Other partners include Microsoft, International Youth Foundation (IYF), ICICI Community Initiatives, Lucent Technologies, Nokia Enterprises and GE Foundation.

UNICEF and Dr. Reddy's Foundation worked with Tsunami affected children in Andaman and Nicobar Islands by implementing a small grant funding project that addressed access to education.

MILESTONES ACHIEVED IN 2005-06

School Community Partnership in Education is a program funded by European Commission (EC) and Aga Khan Foundation. SCOPE creates access to quality education to all children irrespective of their age through school community partnership. DRF is implementing this project with Department of School Education, District Institute of Education Training (DIET), State Center for Education Research and training (SCERT), Department of Tribal Welfare, Sarva Shiksha Abhiyan, & Director Municipal Administration.

- REACH—15,000 non-school going and working children, 64 Government schools in and around Hyderabad, 130 urban basties and 45,000 families.
- 5,000 ADOLESCENT youth mainstreamed into education and more than 600 youth have been trained for employment.
- TRAINING ON BEST teaching practices and Education leadership to 250 school teachers and 50 school principals respectively.
- SCHOOL VISION for 64 Government schools across Hyderabad.
- COMMUNITY PARTNERSHIP with Basti School Committee, School Development Committee and Class Committees in 53 schools.
- 1,000 FAMILIES accessed better employment opportunities.

KALLAM ANJI REDDY VIDYALAYA (KARV) CAMPUS, CHANDANAGAR

The KARV campus is an integrated education model for aspirants from the age group of 3 to 25. The components of the model are: Pre-school center, Bridge school, School, 2 years certified vocational courses (college) and short term vocational courses.

- PRE-SCHOOL—caters to the age group of 3 to 6. In the year 2005-06 the strength of pre school was 75.
- BRIDGE SCHOOL—school drop out and working children in the age group of 6 to 13 attend this school. 140 students were benefited in 2005-06.
- KARV SCHOOL—Students of the age group of 6 to 17 study in the school. 1,050 students studied in KARV school in the year 2005-06.
- KARV VOCATIONAL JUNIOR COLLEGE—2 years certified vocational training particularly aims at adolescents in the age group of 15 to 21 years. 200 students were benefited from this junior college in the year 2005-06.
- LABS (3 MONTHS—Three batches have been conducted in the LABS center for youth of the age group 18 to 25 in Chandanagar Campus in 2005-06 with a total 400 LABS aspirants.

RESPONDING TO EMERGENCY

UNICEF and Dr. Reddy's Foundation worked with Tsunami affected children in Andaman and Nicobar Islands by implementing a small grant funding project that addressed access to education.

board of directors

DR. K ANJI REDDY
CHAIRMAN

DR. K ANJI REDDY is the founder Chairman of Dr. Reddy's Laboratories Limited. Prior to founding Dr. Reddy's in 1984, he was the founder-Managing Director of Uniloids Ltd. and Standard Organics Limited and also served in the state-owned Indian Drugs and Pharmaceuticals Limited.

Under his leadership, Dr. Reddy's has become a pioneer in the Indian Pharmaceutical industry. It has transformed the Indian bulk drug industry from import-dependent in mid-80s to self-reliant in mid-90s and finally into the export-oriented industry that it is today. Under his guidance, Dr. Reddy's became the first Indian company to embark upon drug discovery research in India in 1993 and the first non-Japanese Asia Pacific pharmaceutical company to list on NYSE in April 2001.

Dr. K. Anji Reddy has a Bachelor of Science degree in Pharmaceuticals and Fine Chemicals from Bombay University and a Ph.D., in Chemical Engineering from National Chemical Laboratory, Pune.

GV PRASAD
VICE CHAIRMAN & CEO

MR. G V PRASAD joined the Company in 1986 and leads the core team that is driving the Company's growth and transformation from a Company predominantly selling APIs, Branded Formulations & Generics to achieving its vision of becoming a discovery-led global pharmaceutical Company. As Chief Executive Officer, Mr. Prasad has championed the globalization of the Company and has played a crucial role in its evolution. He has been the architect of the Company's global generics strategy. He has helped create new platforms of growth for Dr. Reddy's, in the Customs Pharmaceutical Services, Discovery Services & Specialty Pharmaceutical segments.

He has built a diverse, talented and experienced senior management team in India, Europe and the U.S. Currently, he is focused on driving Dr. Reddy's growth in the two largest geographies—U.S. and Europe.

Mr. Prasad has a Bachelors degree in Chemical Engineering from Illinois Institute of Technology, Chicago, and a Masters degree in Industrial Administration from Purdue University, U.S.

SATISH REDDY
MANAGING DIRECTOR & COO

MR. SATISH REDDY joined the Company as Executive Director in 1993, responsible for manufacturing operations of APIs, formulations, research & development activities and new product development. He presided over the Company's successful transition from a predominantly APIs manufacturer to a more value-added, finished dosages producer.

In year 1995, he was appointed as Managing Director of Dr. Reddy's Laboratories with primary focus on finished dosage forms (formulations), in the national and international markets. He was the major force behind the successful acquisition of American Remedies Limited (1999), a Chennai-based pharmaceutical company. Besides, he was instrumental in setting up wholly owned subsidiaries in Russia and Latin America and joint ventures in China and South Africa.

Mr. Satish Reddy has a B. Tech. degree in Chemical Engineering from Osmania University, Hyderabad and M.S. degree in Medicinal Chemistry from Purdue University, U.S.

ANUPAM PURI
INDEPENDENT DIRECTOR

MR. ANUPAM PURI joined the Company as Director in 2002. From 1970 to 2000, Mr. Puri was with McKinsey & Company. He worked globally with corporate clients in several industries on strategy and organizational issues, and also served several governments and multilateral institutions on public policy. Mr. Anupam Puri spearheaded the development of McKinsey's India practice, oversaw the Asian and Latin American offices, and was an elected member of the Board. He is currently a Special Advisor for General Atlantic Partners.

Mr. Anupam Puri holds a M. Phil in Economics, Nuffield College, Oxford University, 1969; an MA in Economics from Balliol College, Oxford University,1967; and a BA in Economics from Delhi University, India, 1965.

He is also on the Boards of ICICI Bank Limited, Mahindra & Mahindra Limited and Tech Mahindra Limited, Godrej Consumer Products Limited and ICICI Bank Limited.

DR. KRISHNA G PALEPU
INDEPENDENT DIRECTOR

DR. KRISHNA G PALEPU joined the Company as Director in 2002. Dr. Palepu is the Ross Graham Walker Professor of Business Administration at the Harvard Business School. He holds the title of Senior Associate Dean for International Development. Dr. Palepu's current teaching and research activities focus on Globalization and Corporate Governance. He has published numerous research papers and is also the co-author of the book titled 'Business Analysis & Valuation: Text and Cases.'

Dr. Palepu has a Masters degree in physics from Andhra University, a Post-graduate Diploma in Management from the Indian Institute of Management and a Ph.D., from the Massachusetts Institute of Technology. He is also a recipient of an honorary MA from Harvard and an honorary Doctorate from the Helsinki School of Economics.

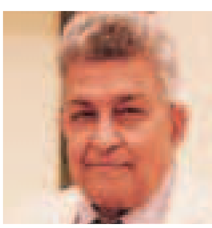
He serves as a consultant to a wide variety of businesses and is also on the boards of Satyam Computer Services Limited, Brooks Automation, and Enamics Inc.

DR. OMKAR GOSWAMI
INDEPENDENT DIRECTOR

DR. OMKAR GOSWAMI joined the Company as Director in 2000. Dr. Goswami is the Founder and Chairperson of CERG Advisory Private Limited. In March 1997, he moved away from formal academics to become the Editor of Business India, one of India's prestigious business magazines. From August 1998 to March 2004, Dr. Goswami served as the Chief Economist of the Confederation of Indian Industry — the premier apex industry organization in India.

A professional economist, Dr. Goswami did his Masters in Economics from the Delhi School of Economics and his D.Phil (Ph.D) from Oxford University. He taught and researched economics for 18 years at Oxford, Delhi School of Economics, Harvard, Tufts, Jawaharlal Nehru University, Rutgers University and the Indian Statistical Institute, New Delhi.

He is also a Director of Infosys Technologies Limited, DSP-Merrill-Lynch Investment Managers Limited, Crompton Greaves Limited, Infrastructure Development Finance Company Limited, SRF Limited and Sona Koyo Steering Systems Limited.



P N DEVARAJAN
INDEPENDENT DIRECTOR

MR. P N DEVARAJAN joined the Company as Director in 2000. Mr. Devarajan was Director in Cheminor Drugs Limited, a Company that merged with Dr. Reddy's in 2000. He was also member of the Planning Board of Madhya Pradesh, Chairman of Research at the Council of National Environment Engineering Research Institute, member of the Assessment Committee of Council of Scientific and Industrial Research and member of the Research Council of National Chemical Laboratory. He was also a Director of the Bank of Baroda, member of the Central Board of Directors of the Reserve Bank of India and Group President and consultant of Reliance Industries Limited.

He is also a Director on the Board of Kothari Sugars and Chemicals Limited, Chairman of Sriram EPC Limited and Chairman of Pollution Monitoring Mitigation Systems and Devises.

RAVI BHOOTHALINGAM
INDEPENDENT DIRECTOR

MR. RAVI BHOOTHALINGAM joined the Company as Director in 2000. Mr. Bhoothalingam has served as the President of The Oberoi Group of Hotels and was responsible for the operations of the Group worldwide. He has also served as Head of Personnel at BAT Plc, Managing Director of VST Industries Limited and as a Director of ITC Limited.

Mr. Bhoothalingam holds a Bachelor of Science degree in Physics from St. Stephens College, Delhi and an M.A. in Experimental Psychology from Gonville and Caius College, Cambridge University.

He is also a Director of Nicco Internet Ventures Limited and Sona Koyo Steering Systems Limited.

DR. V MOHAN
INDEPENDENT DIRECTOR

DR. V MOHAN joined the Company as Director in 1996. Dr. Mohan is also the Chairman and Managing Director of Dr. Mohan's Diabetes Specialities Centre Private Limited and President of the Madras Diabetes Research Foundation, Chennai. He is also a Visiting Professor of Diabetology at Sri Ramachandra Medical College. He was awarded the prestigious Dr. B. C. Roy award by the Medical Council of India in 2005.

Dr. Mohan holds a Bachelor of Medicine degree, Doctor of Medicine Degree, Ph.D. and a Doctor of Science degree from the Madras University.

management discussion & analysis

Note: Analysis of the financial performance for 2005-06 in this part of the Management Discussion & Analysis is based on the consolidated U.S.GAAP financials

OVERVIEW

2005-06 has been a momentous — indeed defining — year for Dr. Reddy's Laboratories ("Dr. Reddy's" or "the Company"). To understand why, it is necessary to touch upon the situation of the Company a year earlier, at the end of 2004-05.

2004-05 was probably the most challenging year in the history of Dr. Reddy's. Due to severe pricing pressure on its Generics business, consolidated revenues had declined year-on-year by 3 per cent to Rs.19,519 million. Post-tax profit fell by almost 91 per cent to Rs.211 million.

Instead of concentrating only on cutting costs, Dr. Reddy's decided to re-commit its strategies and organisational architecture to aggressively growing all its businesses and increasing profitability. In the course of 2005-06, the Company significantly de-risked its drug discovery process by forming an integrated drug development Company called Perlecan Pharma Private Limited with Citigroup Venture and ICICI Venture. It acquired Roche's API business, its order-book and its U.S. FDA-approved manufacturing plant at Cuernavaca in Mexico, with a portfolio of 18 products as well as a range of intermediates and steroids. Thereafter, it acquired betapharm, Germany's fourth largest generics pharmaceuticals Company, with a portfolio of 145 marketed products.

All this was carried out even as the Company actively pushed the sale of its pharmaceutical products throughout the world to grow revenues and profits, while creating a more robust API and generics pipeline for the future. These and other initiatives have resulted in a rebound in growth and profitability. The Company crossed the historical milestone of U.S.$500 million in revenues.

Simultaneously, the Company whole-heartedly focused on having its internal controls over financial reporting in line with the stringent requirements of Section 404 of the U.S. Sarbanes-Oxley ("SOX") Act. The objective was to complete this task well before the mandatory deadline of March 31, 2007 for foreign US Securities and Exchange Commission ("SEC") registrants, such as Dr. Reddy's. We are delighted to inform you that, thanks to the unremitting efforts of the various cross-functional teams, Dr. Reddy's is now compliant with Section 404 of the U.S. Sarbanes Oxley Act. That makes Dr. Reddy's the first manufacturing Company in India, and one of the earliest foreign filers, to become SOX compliant — testimony to the strong internal controls over financial reporting and corporate governance standards and practices of the Company.

Given below are some key financial highlights:

- **Revenues increased by 24.3 per cent from Rs.19,519 million in 2004-05 to Rs.24,267 million in 2005-06.**
- **Profits after tax increased from Rs.211 million in 2004-05 to Rs.1,629 million in 2005-06.**
- **Earnings per share on a fully diluted basis rose from Rs.2.76 in the previous year to Rs.21.24 in 2005-06.**

While these are discussed in detail in the sections that follow, the drivers of performance in 2005-06 were:

- **Well-diversified revenue growth of 17 per cent (excluding acquisitions) across key markets and for key** product segments, which demonstrated the strength of the Company's underlying businesses.

- Initiatives to de-risk R&D investments— specifically, the initiatives with ICICI Venture Funds Management Company towards the product development for U.S. Generics and co-promotion of Perlecan Pharma for Discovery Research.
- Decrease in foreign exchange loss compared to 2004-05.
- One-time income from the profit on the sale of the Company's formulations manufacturing facility at Goa.

Briefly, the revenue growth for each of the key businesses in 2005-06 was :

a) API: 19 per cent growth to Rs.8,238 million, mainly due to a better combination of products and markets.

b) FORMULATIONS: 27 per cent growth to Rs.9,926 million, led by excellent performance across markets, particularly, India, Russia and the CIS countries.

c) GENERICS BUSINESS (excluding acquisition): Grew by 28 per cent in Europe. However, because of heavy pricing pressure, revenues in North America, declined by 27 per cent to Rs.1,631 million.

d) CUSTOMS PHARMACEUTICAL SERVICES (CPS): Excluding acquisition, the CPS business grew by 68 per cent to Rs.523 million in 2005-06.

e) ACQUISITIONS: The Company's acquisitions in Mexico and Germany contributed to Rs.1,509 million to the revenues of 2005-06.

In the following sections, we discuss acquisitions, markets, business-wise revenues, R&D and financials in greater detail.

ACQUISITIONS

Dr. Reddy's had realised that in order to rapidly grow its businesses it had to focus on acquisitions. Fortunately, the Company had a strong balance sheet with the value of cash and cash equivalents to the tune of U.S.$209 million and hardly any long-term debt as on March 31, 2005. It therefore had the financial strength to make major acquisitions. Two significant ones were concluded in 2005-06.

- The first was the purchase of Roche's API business, its order-book and its manufacturing plant at Cuernavaca in Mexico at an investment of U.S.$61 million. The plant, approved by the U.S. FDA and other international regulatory agencies, employs around 340 people, with the current portfolio comprising 18 products including mature APIs as well as a range of intermediates and steroids.
- The second acquisition during the year was that of betapharm, Germany's fourth largest generics pharmaceuticals Company. Dr. Reddy's entirely bought out betapharm in an all cash deal for approximately €483 million. The Company currently has a portfolio of 145 marketed products; employs 370 people with a dedicated revenues force of 250; and achieved a turnover of €164 million in 2005. betapharm gives Dr. Reddy's access to a broad portfolio and a strong foothold in the large German generics market.

MARKETS

GLOBAL TRENDS[1]

In 2005, global pharmaceutical revenues was estimated at U.S.$602 billion. In the ten major markets that account for 81 per cent of the total global revenues, the average growth was 6 per cent in 2005, compared with 7 per cent the previous year. However, emerging markets — including China, Korea, Mexico, Russia and Turkey — experienced double-digit growth and, by consistently out-pacing global performance, have begun to signal important shifts in the market place. With improving patient access to prescription drugs, the emerging markets of Asia, Latin America and Eastern Europe have gained in strength.

Global growth in pharmaceutical revenues was driven by increased longevity of the populations, rising wealth, innovative new products, and new applications for existing products. In 2005 alone, 40 per cent of total market growth was fuelled by the introduction of new products, including 30 new molecular entities launched in key markets.

North America, which accounts for 47 per cent of global pharmaceutical revenues, grew 5 per cent, to U.S.$266 billion, while Europe experienced somewhat higher growth of 7 per cent, to U.S.$170 billion. Japan, the world's second largest market and one which had been posting slower growth rates, performed strongly in 2005 — growing 7 per cent to U.S.$60 billion, its highest year-on-year growth since 1991. Revenues in Latin America grew at an exceptional rate of 19 per cent to U.S.$24 billion, while Asia Pacific (excluding Japan) and Africa grew 11 per cent to U.S.$46 billion. China continued showing spectacular growth — of 20 per cent to almost U.S.$12 billion in 2005. This is the third consecutive year that China has achieved over 20 per cent growth. In fact, IMS estimates that China will be the world's seventh largest pharmaceutical market by 2009.

The number of blockbuster products (those with revenues exceeding U.S.$1 billion per year) reached 94 in 2005, vis-à-vis just 36 in 2000. These included 17 new members of the billion-dollar club. While six blockbusters are expected to lose their patents in 2006, the launch of new products and continued growth of those already on the market will result in an increasing number of blockbusters over the next five years.

CHART A Global Distribution of Audited Pharmaceutical Revenue in 2005

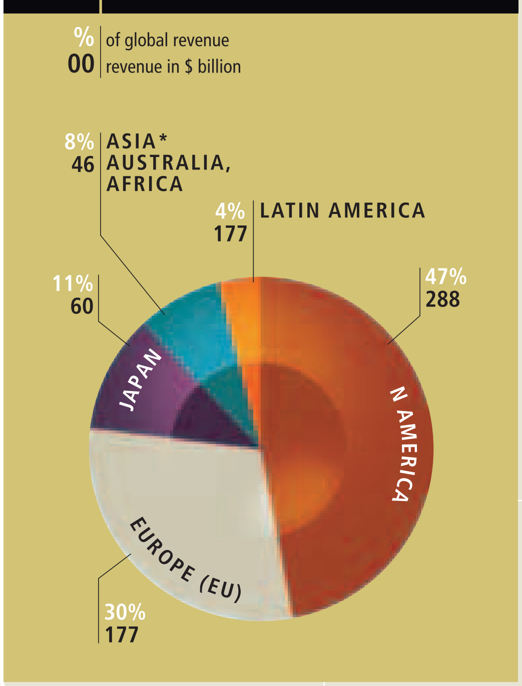


Chart A plots the geographical spread of audited pharmaceutical revenues in 2005.

TRENDS IN INDIA[2]

With 2005 witnessing the advent of the product patent regime, both MNCs and Indian pharmaceutical companies have begun to adapt their strategies. The MNCs are now preparing to bring in their research molecules to the country to leverage India's strength of knowledge workers, while Indian companies are trying to focus on developing brands and exploring in-licensing and marketing alliances.

In 2005, the Indian pharmaceutical market grew by 7 per cent in volume and 9 per cent in value to Rs.230 billion. New product launches contributed to almost 90 per cent of this 9 per cent value growth. All the top-10 new products crossed the milestone revenues figure of Rs.100 million. Overall growth, however, occurred more in the second half of the year compared to first half — when it was affected by the uncertainty over the impact of implementation of the VAT regime.

Some of the key trends in the market during 2005 were:

- Revenues of acute therapy products grew by 8 per cent in 2005 compared to 6 per cent in 2004. Chronic therapy revenues grew by 11 per cent in 2005 — in line with the 2004 growth rate.
- Except pain and cardiac therapeutic segments, most therapy areas observed higher growth in 2005 compared to 2004.
- Share of the top 10 companies declined from 38 per cent of the Indian market in 2003 to 36 per cent in 2005, indicating higher market penetration by the mid-sized and smaller pharmaceutical companies.

[1] Source: IMS Health: MIDAS, MAT December 2005

[2] Source: ORG IMS Annual Report January to December 2005

DR. REDDY'S MARKET PERFORMANCE

REVENUES

Revenues increased by almost 24 per cent to Rs.24,267 million in 2005-06. This was primarily due to increase in revenues of APIs, Formulations, Generics in Europe, as well as the revenue contribution from Mexico (with effect from December 30, 2005) and Germany (from March 3, 2006). Excluding the two acquisitions, revenues grew by 17 per cent.

India contributed 34 per cent of total revenues in 2005-06. International operations accounted for the remaining 66 per cent, which was distributed as follows:

- 16 per cent of total revenues from North America (United States and Canada).
- 15 per cent from Russia and other countries in the Commonwealth of Independent States ("CIS").

- 18 per cent from Europe, and 17 per cent from other countries.

Formulations and API segments. **Table 1** gives Dr. Reddy's consolidated financial performance by businesses under U.S.GAAP.

01 TABLE Consolidated business-wise performance under U.S.GAAP

IN RS. MILLION

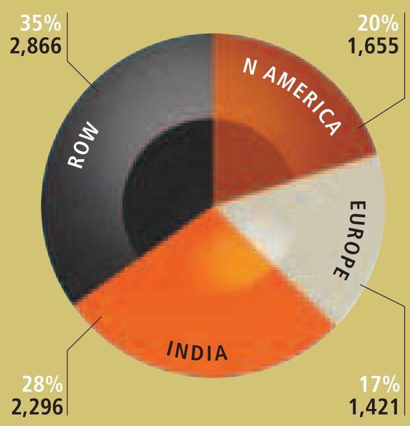
	2005-06			2004-05		
	REVENUE	GROSS PROFITS(1)	% TO REVENUE	REVENUE	GROSS PROFITS(1)	% TO REVENUE
Formulations	9,926	6,842	69	7,823	5,330	68
API	8,238	2,321	28	6,945	1,931	28
Generics	4,056	1,887	46	3,577	1,957	55
Biotechnology & Critical Care	691	455	66	527	351	67
CPS	1,327	328	29	312	229	73
Others	29	17	71	335	335	100
TOTAL	**24,267**	**11,850**	**49**	**19,519**	**10,133**	**52**

Note: (1) does not include selling, research and development costs, and exchange gains and losses

Some of the details are worth highlighting:

- Revenues from Russia and other former CIS countries grew by 28 per cent to Rs.3,559 million in 2005-06. The increase was primarily due to the growth in revenues of major brands such as Nise, Keterol, Ciprolet and Omez.
- Revenues from Europe increased by 51 per cent to Rs.4,326 million in 2005-06, primarily on account of the Company's growing revenues of Generics, APIs and Formulations. This revenue includes Rs.686 million from betapharm, which was acquired in March 2006.
- Revenues from North America decreased by 8 per cent to Rs.3,984 million in 2005-06, largely because of severe pricing pressure in Generics and lower revenues in API.
- Revenues from India increased by 24 per cent to Rs.8,272 million in 2005-06, thanks to significantly better performance in the

CHART B Geographical Distribution of API Revenue during 2004–05



ACTIVE PHARMACEUTICAL INGREDIENTS AND INTERMEDIATES ("API")

In 2005-06, revenue from API increased by 19 per cent to Rs.8,238 million, with international revenues accounting for 72 per cent of this segment's revenue.

International revenues grew by 20 per cent to Rs.5,942 million in 2005-06. Several markets showed high growth. For instance, revenues from Europe grew by 30 per cent primarily due to key product such as terbinafine, montelukast and sertraline, which more than offset the decline in revenues of ramipril due to pricing pressure. The Company performed very well in emerging markets, especially in Israel, Turkey and Mexico. Robust growth in other international markets more than offset the decline in North American revenues, which fell by 11 per cent to Rs.1,654 million in 2005-06 — largely because of the lack of significant new product launches coupled with revenues decline in the existing portfolio.

Revenues from India grew by 16 per cent to Rs.2,296 million in 2005-06. Ciprofloxacin, sparfloxacin and ranitidine drove this growth.

Chart B gives the geographical distribution of API revenues during 2005-06. **Table 2** gives the revenues earned from the top-15 products. It shows that ten of these fifteen products achieved higher revenues in 2005-06 compared to the previous year; and that, in the aggregate, revenues of the top-15 grew by 21 per cent in value terms.

BRANDED FORMULATIONS

2005-06 saw a resurgence in Formulations revenues in India as well as across Dr. Reddy's key international markets, which resulted in revenues increasing by 27 per cent to Rs.9,926 million.

Revenues in India increased by 26.7 per cent to Rs.5,526 million in 2005-06, and this was primarily driven by growth in top 10 brands backed up by an increase in the sales force and a sharper marketing focus. Higher re-stocking by dealers in 2005-06 after the drawing down of stocks because of uncertainties that accompanied the introduction of VAT in April 2005 also had a positive impact. The Company's Top-10 brands put together grew by 31 per cent and contributed to revenue worth Rs.2,848 million. **Table 3** gives the revenues performance of the Top-10 Formulations in India in 2005-06 and the previous year.

Revenue from international markets increased by 27 per cent to Rs.4,400 million in 2005-06. Russia was the key revenue driver, and grew at 23 per cent. Dr. Reddy's new marketing initiatives in Russia — getting listed in federal programme and special campaigns for key products — played their role in

TABLE 02 Revenue from key API products

IN RS. MILLION

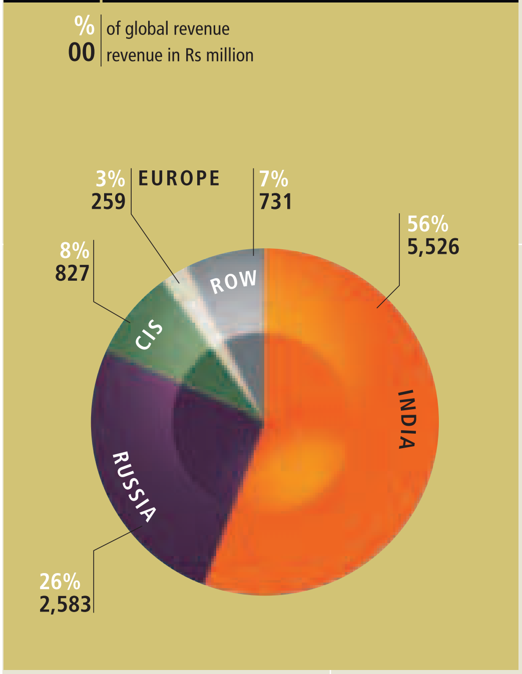
KEY PRODUCTS	2005-06	2004-05	GROWTH
Ciprofloxacin Hydrochloride	778	619	26%
Ramipril	643	783	(18%)
Terbinafine HCl	537	194	177%
Ibuprofen	502	460	9%
Sertraline Hydrochloride	494	138	258%
Ranitidine HCl Form 2	404	282	43%
Naproxen Sodium	380	470	(19%)
Naproxen	375	230	63%
Atorvastatin	321	252	27%
Montelukast	241	53	355%
Losartan Potassium	173	181	(4%)
Sparfloxacin	168	118	42%
Nizatidine	161	217	(26%)
Ranitidine Hydrochloride Form 1	149	452	(67%)
Clopidogrel	140	80	75%
TOP-15 API REVENUES	**5,466**	**4,529**	**21%**

TABLE 03 Revenues from Top-10 brands in India

IN RS. MILLION

KEY DOMESTIC PRODUCTS	2005-06	2004-05	GROWTH
Nise	736	538	37%
Omez	691	528	31%
Stamlo	340	298	14%
Stamlo Beta	263	187	41%
Enam	173	162	7%
Atocor	167	116	44%
Razo	127	65	95%
Reclimet	124	79	57%
Clamp	118	101	17%
Mintop	109	98	11%
TOTAL	**2,848**	**2,172**	**31%**

CHART C **Geographical Distribution of Formulations Revenues 2005–06**



driving revenue growth. This was supplemented by increases in revenues in key markets in CIS countries, Central and Eastern Europe, Latin America, South Africa and Middle East.

Chart C gives the geographical distribution of Formulations revenues during 2005-06.

GENERICS

The Company's revenues from Generics increased by 13 per cent to Rs.4,056 million in 2005-06. The main factors were increases in the U.K. and the contribution of revenues from betapharm in Germany from March 3, 2006, which helped offset the decrease in North American revenues. Excluding betapharm, however, revenues reduced by 6 per cent to Rs.3,351 million in 2005-06.

Revenues from Europe grew by 81 per cent to Rs.2,422 million in 2005-06 — both due to volume growth as well as price increase in key products such as omeprazole and amlodipine maleate in the U.K. and betapharm revenues. Excluding betapharm, European revenues grew by 28 per cent.

Revenue in North America declined by 27 per cent to Rs.1,631 million in 2005-06, largely due to reduced revenues and acute pricing pressures of products such as fluoxetine and tizanidine, which are facing intense competition in the market place. In 2005-06, these two products contributed Rs.438 million in revenues, compared to Rs.1,135 million a year earlier. To an extent, the fall in U.S. Generics revenue was offset by the contribution of Rs.140 million from new product launches of glimpiride and zonisamide. Both these launches helped increase the breadth of products under Dr. Reddy's own label; also their market shares were encouraging.

To better leverage the U.S. Generics market, the Company has begun to create a broad and more favourably positioned pipeline to reap maximum benefits of patent expiries that are to occur in subsequent years. In 2005-06, the Company filed 12 Abbreviated New Drug Applications ("ANDA"), taking the total number of ANDA filings to 70. More significantly, the year saw a record number of approvals for the Company's ANDA filings: 5 final approvals and 7 tentative.

Chart D gives the geographical distribution of Generics revenue for 2005-06.

CUSTOMS PHARMACEUTICAL SERVICES

Revenue in this segment increased from Rs.311 million in 2004-05 to Rs.1,327 million in 2005-06 — thanks largely to the contribution from the Company's acquisition in Mexico. Excluding the acquisition, revenues increased by 68 per cent. With the Mexican facility, Dr. Reddy's expects even greater success in establishing its franchise among the large as well as emerging pharmaceutical companies that want to partner with it for their innovation development needs.

CRITICAL CARE AND BIOTECHNOLOGY

Revenue in this segment increased by 31 per cent to Rs.691 million in 2005-06. Growth was driven by the performance of key products in India as well as Russia.

REGULATORY ACTIVITY

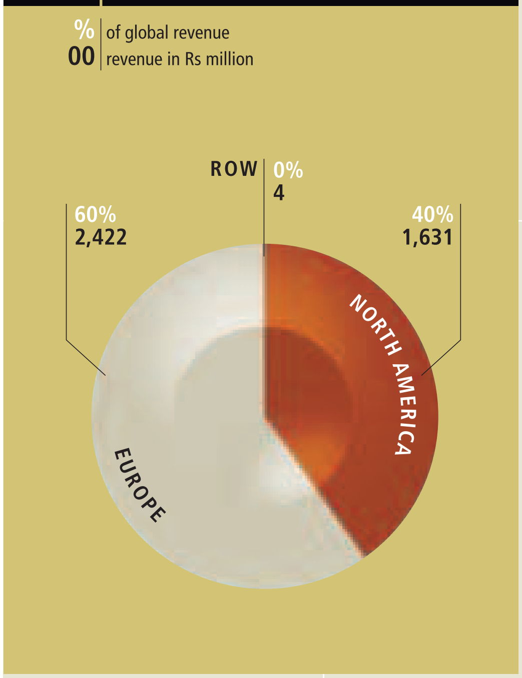
As early as 2003-04, the Company realised that a source of competitiveness in the international markets was a robust generics and API pipeline. The Company has been aggressively investing in expanding its pipeline of APIs and finished dosages. The Company continued the investments in 2005-06 as well.

As a result, Dr. Reddy's has filed 12 ANDAs in 2005-06, including 11 non-Para IV filings, taking the total number of ANDA filings to 70. These 12 ANDAs address innovator IMS revenues of about U.S.$13 billion [MAT, December 2005]. The year also saw a record number of approvals for the Company's ANDA filings: 5 final approvals and 7 tentative. As of March 31, 2006, the Company's U.S. Generic pipeline comprises 49 ANDAs pending with the U.S. FDA, including 10 tentative approvals and 29 Para-IVs.

As far as APIs are concerned, during 2005-06, the Company increased the number of products in its Drug Master File ("DMF") by 30, of which 17 were U.S. DMFs, 8 Canadian and 5 European. The total number of DMFs now stand at 151 — 81 filed in the U.S., 28 in Canada and 42 in Europe. The Company is also developing APIs in the oncology segment.

During 2005-06, the Company submitted seven national licences, 34 duplicate licences and 5 MRP applications to the U.K. Medicines and Healthcare products Regulatory Agency ("MHRA"). It also continued the development of a portfolio of biogenerics.

CHART D Geographical Distribution of Generic Revenues 2005–06



DRUG DISCOVERY

In Drug Discovery, Dr. Reddy's has seven molecules or new chemical entities ("NCE"), of which five are in clinical development and two in the pre-clinical phase. On the research side, the Company will continue to extend its discovery pipeline with greater focus on creating new platforms in its chosen therapeutic segments of cardiovascular and metabolic disorders. On the development side, it will continue to advance the development of the NCE assets through a combination of in-house, partnerships and co-development initiatives.

Dr. Reddy's most advanced NCE in clinical development is balaglitazone (DRF 2593), a partial PPAR-gamma agonist for the treatment of Type 2 diabetes. The 2 year carcinogenicity studies have been completed. The preliminary findings appear to be promising and should support further development of balaglitazone. We are waiting for the final report to come by the end of this year. We are also making good progress with the clinical development efforts on DRF 10945, RUS 3108 and DRL 11605.

With five of the Company's NCEs having advanced to clinical development, the key priority is to create a roadmap for commercialising these assets. In addition to further building the R&D organisation and its IPR-protecting commercialisation capabilities, it requires strategic partnerships and alliances for not only de-risking the cost of research but also unlocking the value of these assets.

This is why Dr. Reddy's has been actively pursuing collaborative mechanisms in its Discovery R&D. During 2005-06, three key R&D deals were finalised.

Table 4 gives the details of Dr. Reddy's development pipeline in discovery research.

1. PERLECAN PHARMA PRIVATE LIMITED

Dr. Reddy's promoted India's first integrated drug development Company, Perlecan Pharma Private Limited ("Perlecan"), together with Citigroup Venture Capital International Growth Partnership Mauritius Limited and ICICI Venture Funds Management

TABLE 04 Dr. Reddy's development pipeline in discovery research

COMPOUND	THERAPEUTIC AREA	STATUS	DEVELOPMENT PARTNER	REMARKS
DRF 2593	Metabolic disorders	Phase II completed	Rheoscience	• Long-term carcinogenicity studies completed. Results expected by end of calendar year.
DRF 10945	Metabolic disorders	Phase II in progress	Assigned to Perlecan	• Non-fibrate predominantly PPAR alpha agonist for the treatment of dyslipidemia • Phase II safety & efficacy studies in patients commercially in Canada.
RUS 3108	Cardiovascular	Phase I in progress	Assigned to Perlecan	• Perlecan inducer for the treatment of atherosclerosis • Phase I studies (U.K.) have shown good tolerability and safety profile for the drug
DRL 11605	Metabolic disorders	Phase I initiated	Assigned to Perlecan	• Pan PPAR (α,δ,γ) agonist for the treatment of obesity • Initiated Phase I in Canada
DRL 16536	Metabolic disorders	Pre-clinical	Assigned to Perlecan	• AMPK modulator for the treatment of diabetes • Regulatory toxicity studies initiated
DRF 1042	Oncology	Phase I	Dr. Reddy's	• Single isomer in Phase I trials in India
DRL 12424	Cardiovascular	Pre-clinical	Dr. Reddy's	• Pre-clinical development

Company. Total equity commitment towards Perlecan of all three promoting entities aggregates U.S.$53 million. Four NCEs were assigned to the new Company — DRL 10945, RUS 3108, DRL 11605 and DRL 16536 — with the specific task of furthering clinical development and out-licensing of these molecules.

2. RHEOSCIENCE A/S

The Company has entered into an agreement for joint development and commercialisation of balaglitazone (DRF 2593), in which Rheoscience will fund all the costs associated with the Phase III clinical trials. Dr. Reddy's will pay Rheoscience a pre-determined amount towards its share of the development costs. This arrangement allows Dr. Reddy's to keep its full rights for North America, Japan, and the rest of the world, except Europe (excluding Russia and CIS) and China.

3. ARGENTA DISCOVERY LIMITED

This involves an agreement to jointly develop and commercialise a novel approach to the treatment of Chronic Obstructive Pulmonary Disease ("COPD"). Both parties will collaborate to identify clinical candidates from a certain class of Dr. Reddy's compounds for use as potential treatments for COPD. Both will jointly develop the selected candidates from the pre-clinical stage up to Phase IIa (proof-of-concept). On successful completion of Phase IIa trials, the companies may either license-out the candidate for further development and commercialisation to a larger pharmaceutical Company, or jointly pursue further co-development.

FINANCIALS

INCOME STATEMENT

Table 5 gives the abridged U.S.GAAP financial performance of Dr. Reddy's for 2005-06 on a consolidated basis.

Revenues

Revenues increased by 24 per cent from Rs.19,519 million in 2004-05 to Rs.24,267 million in 2005-06. Revenue growth was broad based, occurred across all divisions and was well diversified across all key markets in the world — except North America, where the severe pricing pressure on existing Generics products continued. Excluding the acquisitions, revenues grew by 17 per cent.

Gross profit

The Company's gross profits increased by 17 per cent to Rs.11,850 million for 2005-06 from Rs.10,134 million in 2004-05. Gross profit as a percentage of revenues was 49 per cent in 2005-06 as compared to 52 per cent in 2004-05. This drop in gross margin was largely on account of decline in revenues of Generics segment.

Selling, general and administrative expenses

Selling, General and Administrative ("SG&A") expenses increased by 19 per cent to Rs.8,029 million in 2005-06, compared to Rs.6,775 million in 2004-05. Despite this increase, as a share of total revenues, SG&A expenses were 33 per cent in 2005-06, versus 35 per cent in the previous year. The rise in absolute SG&A expenses was largely as a result of increase in employee costs — which increased by 18 per cent in 2005-06, primarily due to market corrections and increase in the headcount. This was, however, partially offset by an 11 per cent decrease in legal and professional expenses. SG&A costs also rose because of marketing expenses — which increased by 36 per cent in 2005-06, mostly on account of higher selling expenses and higher shipping cost. SG&A expenses for the year include those of the acquisitions in Mexico and Germany.

R&D expenses

R&D costs decreased by 23 per cent to Rs.2,153 million for 2005-06. As a share of total revenue, R&D expenditure was at 9 per cent in 2005-06, compared to 14 per cent in the previous year. The decrease in absolute value of R&D expenses was largely on account of lower costs in the Drug Discovery and in Generics business segments.

Under the terms of the R&D partnership agreement with I-VEN Pharma Capital Fund Limited ("I-VEN"), Dr. Reddy's received U.S.$23 million in March 2005, of which U.S.$8.6 million (Rs.384 million) was recorded as a reduction in the R&D expense in 2005-06, compared to the U.S.$2.1 million (Rs.96 million) recognised in 2004-05.

Amortization expenses

Amortization expenses, including acquisitions, increased by 20 per cent to Rs.420 million from Rs.350 million. The increase is primarily on account of amortization of intangibles acquired in the acquisition of Falcon, Trigenesis & betapharm.

05 TABLE

Abridged consolidated statement of operations 2005-06 U.S.GAAP

IN RS. MILLION

PARTICULARS	2005-06	%	2004-05	%
TOTAL REVENUES	**24,267**	**100.0%**	**19,519**	**100.0%**
Cost of revenues	12,417	51.2%	9,386	48.2%
GROSS PROFIT	**11,850**	**48.8%**	**10,134**	**51.8%**
Selling, General & Administrative Expenses	8,029	33.1%	6,775	35.0%
R&D Expenses (1)	2,153	8.9%	2,803	14.4%
Amortization Expenses	420	1.7%	350	1.8%
Other operating (income)/expense net (2)	(320)	(1.3%)	(6)	0.0%
OPERATING INCOME BEFORE FOREX LOSS/(GAIN)	**1,568**	**6.5%**	**200**	**0.6%**
Forex Loss/ (Gain)	126	0.5%	489	2.5%
OPERATING INCOME/(LOSS)	**1,442**	**5.9%**	**(289)**	**(1.9%)**
Equity in loss of affiliates	(88)	(0.4%)	(58)	(0.3%)
Other (expenses)/income net	533	2.2%	454	2.3%
INCOME BEFORE INCOME TAXES AND MINORITY INTEREST	**1,887**	**7.8%**	**107**	**0.5%**
Income tax benefit/(expense)	(258)	(1.1%)	94	(0.5%)
Minority interest	–	0.0%	(10)	(0.1%)
NET INCOME	**1,629**	**6.7%**	**211**	**1.1%**
DILUTED EPS (RS. PER SHARE)	**21.24**	**–**	**2.76**	**–**

Notes: : (1) Including income from ICICI Venture towards Generics R&D partnership fund, amounting to Rs.384 million.

(2) Includes profit from the sale of finished dosages facility at Goa for Rs.388 million.

Other operating expense/(income)

Other operating expense/(income) amounted to Rs.320 million in year 2005-06 as compared to Rs.6 million in 2004-05. This primarily includes profit on sale of finished dosages facility at Goa amounting to Rs.388 million in 2005-06.

Other Income

For 2005-06 our other income was Rs.534 million, as compared to Rs.454 million for 2004-05. This includes net interest income of Rs.507 million in 2005-06.

Net Income

As a result of the above, our net income increased to Rs.1,629 million in 2005-06, as compared to Rs.211 million in 2004-05. Net income as a percentage of total revenues increased to 6.7 per cent in 2005-06 from 1.1 per cent in 2004-05.

BALANCE SHEET

The overall balance sheet size of the Company as on March 31, 2006 more than doubled compared to March 31, 2005. The total value of assets (and liabilities including Equity) was Rs.29,288 million as on March 31, 2005 which increased to Rs.68,768 million as on March 31, 2006. The increase is in line with a) the high value acquisitions made by the Company during 2005-06 in Germany and Mexico and b) increase in the scale of activities compared to previous year. On the asset side, a major share of the increase has been observed in Goodwill & Intangibles and Inventories. On the Liability side, the external funding obtained for the acquisitions reflected in the increase in Long term debt (both current and non-current portions). Movements in key balance sheet items have been briefly discussed below.

Cash, Cash Equivalents & Restricted Cash (current & non-current portions)

Cash and cash equivalents (including restricted cash) marginally increased by Rs.442 million from Rs.9,346 million as on March 31, 2005 to Rs.9,787 million as on March 31, 2006. The cash flows generated from operating and financing activities were used to fund the acquisitions, capital expenditure, increase in working capital and dividend payment by the Company.

Property, Plant and Equipment (net)

During the year 2005-06, the Property, Plant and Equipment (net) increased by Rs.2,028 million from Rs.7,058 million as on March 31, 2005 to Rs.9,086 million as on March 31, 2006. The increase is primarily due to the assets taken over during the acquisitions in Mexico and Germany. The increase also includes the investment in the Company's new formulations facility set up at Baddi, Himachal Pradesh. These increases were partially offset by the sale of formulations manufacturing facility at Goa.

Goodwill & Intangibles

Goodwill & intangibles increased by Rs.31,080 million from Rs.2,588 million as on March 31, 2005 to Rs.33,669 million as on March 31, 2006. This increase is primarily on account of the purchase price accounting of the two acquisitions.

Inventory

Increase in inventory by Rs.3,395 million from Rs.3,500 million as on March 31, 2005 to Rs.6,895 million as on March 31, 2006 is due partly to the acquisitions and partly to cater to the build-up for planned new product launches in U.S. and expected increase in the production activity.

Long Term Debt (current & non-current portions)

The long-term debt increased by Rs.21,832 million from Rs.31 million as on March 31, 2005 to Rs.21,863 million as on March 31, 2006. The increase was primarily due to foreign currency denominated term loan obtained to fund the acquisition in Germany.

Bank Borrowings

The bank borrowing as on March 31, 2006 increased by Rs.6,336 million from Rs.2,796 million as on March 31, 2005 to Rs.9,132 million as on March 31, 2006. During the year, the Company availed the foreign currency denominated packing credit and other loans to fund the working capital requirements, which increased as an impact of the increase in the scale of operations during 2005-06.

INDIAN GAAP FINANCIAL PERFORMANCE FOR 2005-06, STAND-ALONE

Note: Analysis of the financial performance for 2005-06 in this part of the Management Discussion and Analysis is based on the Indian GAAP Standalone financials

REVENUE MIX 2005-06

Table 6 gives the business wise breakup of revenues (Gross of excise duty and other similar duties).

06 TABLE Business-wise performance under Indian GAAP standalone

IN RS. MILLION

	2005-06	2004-05	INC./ (DEC.)
API	7,449	5,947	25%
Formulations	9,915	7,642	30%
Generics	2,187	2,184	0%
Critical Care and Biotechnology	484	366	32%
Custom Pharmaceutical Services	920	112	721%
TOTAL	**20,955**	**16,251**	**29%**

KEY PERFORMANCE HIGHLIGHTS

Net Revenues

Net revenues increased by 29 per cent from Rs.16,251 million in 2004-05 to Rs.20,955 million in 2005-06 due to the following reasons

- Revenues from Formulations increased by 30 per cent from Rs.7,642 million in 2004-05 to Rs.9,915 million in 2005-06. Revenues from India increased by 27 per cent to Rs.5,532 million primarily due to growth in top brands. The growth was also positively impacted by higher off take by trade in Q1 2005-06 following implementation of Value added tax system in India from April 2005. Revenues from international markets increased by 34 per cent to Rs.4,383 million in 2005-06, driven by growth across key markets including Russia and CIS markets.
- Revenues from API grew by 25 per cent to Rs.7,449 million in 2005-06 from Rs.5,947 million in 2004-05. This growth was well diversified across

key markets. Revenues from India grew by 17 per cent, primarily driven by increase in sales of key products. Revenues from international markets grew by 29 per cent, primarily led by Europe and Rest of the World due to growth of key products of terbinafine, montelukast and sertraline. This growth was partially offset by decrease in sales of new products as well as decline in key commercialized products in North America.

- In Generics, revenues more or less remained flat at Rs.2,187 million in 2005-06 as compared to Rs.2,184 million in 2004-05. Revenue growth in Europe was led by higher pricing of omeprazole and amlodipine maleate. Revenues from North America declined due to continued pricing pressure on fluoxetine and tizanidine partially offset by revenues from new product launches of glimpiride and zonisamide.
- Revenues from Custom Pharmaceutical Services increased from Rs.112 million in 2004-05 to Rs.920 million in 2005-06. This increase was primarily led by increase in customers and product portfolio as well as contribution from business acquired in Mexico.

Material Costs

Material Costs increased by 39 per cent from Rs.5,444 million in 2004-05 to Rs.7,562 million in 2005-06. As a per cent of revenues, material costs increased from 34 per cent to 36 per cent, which was primarily due to decrease in average price realization in generics.

Personnel Costs

Personnel costs increased by 17 per cent from Rs.1,824 million in 2004-05 to Rs.2,128 million in 2005-06 due to annual increments, increase in employee base and the full year impact of the market correction announced in the fourth quarter of 2004-05. As a per cent of revenues, personnel costs decreased from 12 per cent in 2004-05 to 11 per cent in 2005-06.

Operating & Other Expense

Operating and other expense increased by 17 per cent from Rs.4,462 million in 2004-05 to Rs.5,201 million in 2005-06 due to the following reasons –

- Increase in selling expense by 34 per cent to Rs.1,454 million on account of higher marketing activities in line with increase in sales in formulations.
- Increase in carriage outwards by 24 per cent to Rs.748 million on account of increase in sales

The above increase was offset by

- Decrease in Forex loss by Rs.360 million.

As per cent of revenues, the expense decreased to 26 per cent in 2005-06 from 29 per cent in 2004-05.

Depreciation & Amortisation

Depreciation & amortization increased by 20 per cent from Rs.925 million in 2004-05 to Rs.1,113 million in 2005-06, in line with increase in gross block and intangibles. The additional investments were incurred towards normal capital expenditure as well as new projects in formulations and generics. Increase in amortization by Rs.25 million was due to amortization related to the acquisition in Mexico.

Research & Development

Research & development expenses decreased by 29 per cent from Rs.2,422 million in 2004-05 to Rs.1,725 million in 2005-06. As a percent of revenues, the expense decreased to 8.6 per cent per cent in 2005-06 from 15.5 per cent due to the following reasons –

- Decrease in expenses at drug discovery by Rs.416 million primarily due to lower expenses on clinical trials.
- Decrease in research and development expenses in generics.
- During the year, the Company recognized an income of Rs.384 million as against Rs.96 million under the R&D partnership with ICICI venture.

Other income

Other income for 2005-06 amounted to Rs.1,231 million as compared to Rs.696 million in financial year 2004-05. This includes profit on sale of finished dosages facility at Goa for Rs.388 million as well as increase in interest income by Rs.351 million.

It was partially offset by decrease in profit on sale of investments of Rs.69 million.

Income Tax

Provision for income tax (inclusive of fringe benefit tax) for the financial year 2005-06 amounted to Rs.526 million as compared to benefit of 211 million in financial year 2004-05. This was due to overall increase in profits.

Profit After Tax

Net income increased from Rs.655 million in 2004-05 to Rs.2,111 million in 2005-06. Net income was 11 per cent of net revenues in 2005-06 compared to 4 per cent in 2004-05.

07 TABLE Business-wise performance under Indian GAAP consolidated

IN RS. MILLION

	2005-06		2004-05	
	REVENUES	PBIT*	REVENUES	PBIT*
Formulations	10,182	3,343	7,914	2,335
API	8,301	1,540	6,942	997
Generics	4,009	(569)	3,516	(712)
Developing businesses	692	59	527	58
Drug discovery	–	(675)	–	(993)
CPS	1,390	64	314	43
Others	31	31		
TOTAL	**24,605**	**3,793**	**19,213**	**1,728**

*Note: *: Does not include costs, which cannot be allocated, and unallocable exchange rate gains and losses.*

08 TABLE Revenues by geographic markets (Gross of excise and other similar duties)

IN RS. MILLION

	2005-06	2004-05	INCR./(DECR.)
India	8,222	6,689	23%
North America	4,103	4,349	-6%
Russia and other CIS countries	3,654	2,402	52%
Europe	4,310	2,868	50%
ROW	4,316	2,905	49%
TOTAL	**24,605**	**19,213**	**28%**

INDIAN GAAP FINANCIAL PERFORMANCE FOR 2005-06, CONSOLIDATED

Note: Analysis of the financial performance for 2005-06 in this part of the Management Discussion and Analysis is based on the Indian GAAP Consolidated financials

REVENUES MIX 2005-06

Table 7 gives the Company's Strategic Business Unit ("SBU") wise financial performance on a consolidated basis.

Table 8 gives the region wise distribution of the Company's revenues in 2004-05 and 2003-04 respectively.

KEY PERFORMANCE HIGHLIGHTS

Net Revenues (gross of excise and other similar duties)

Net revenues increased by 28 per cent from Rs.19,213 million in 2004-05 to Rs.24,605 million in 2005-06 due to the following reasons

- Revenues from formulations increased by 29 per cent to Rs.10,182 million. This growth was primarily driven by well-diversified growth across key geographies. Revenues from India were driven growth in top brands. The growth was also positively impacted by higher off take by trade in Q1 2005-06 following implementation of Value added tax system in India from April 2005. Revenues from the international markets were driven by growth in key markets including Russia and CIS markets.
- Revenues from API have increased by 20 per cent to 8,301 million. This growth was driven by increase in revenues across markets. Growth in revenues from India was led by increase in sales of key products. Revenues from international markets were driven by Europe and Rest of the World due to growth of key products such as terbinafine, montelukast and sertraline partially offset by decrease in sales in North America due to decline in key products.
- Revenues from Generics have increased by 14 per cent to Rs.4,009 million. Excluding acquisitions, revenues declined by 6 per cent to Rs.3,302 million. The decline in North America driven by pricing pressure on fluoxetine and tizanidine more than offset growth in Europe led by higher pricing of omeprazole and amlodipine maleate in the U.K.

- Revenues from Customs Pharmaceuticals Services increased from Rs.314 million in 2004-05 to Rs.1,390 million in 2005-06. Excluding acquisitions, the revenues grew by 88 per cent to Rs.586 million primarily due to increase in customer and product portfolio.

Material Costs

Material Costs increased by 36 per cent from Rs.6,015 million in 2004-05 to Rs.8,165 million in 2005-06. As a per cent of revenues, material costs increased to 35 per cent in 2005-06 from 33 per cent. This increase was primarily due to decline in margin in North America generics segment on account of pricing pressure on key products.

Personnel Costs

Personnel Costs increased by 19 per cent to Rs.3,495 million in 2005-06 from Rs.2,938 million in 2004-05. This increase was primarily due to annual increments, increase in number of employees as well as the full year impact of the market correction announced in the fourth quarter of 2004-05. As a per cent of revenues, personnel costs decreased to 15 per cent in 2005-06 from 16 per cent in 2004-05.

Operating & Other expense

Operating and other expense increased by 10 per cent from Rs.5,905 million in 2004-05 to Rs.6,503 million in 2005-06 due to the following reasons –

- Increase in selling expenses by 43 per cent to Rs.1,691 million in 2005-06 from 1,186 million in 2004-05 on account of higher marketing activities in line with increased sales of formulations.
- Increase in carriage outwards by 28 per cent to Rs.824 million in 2005-06 from Rs.643 million in 2004-05 in line with increase in sales.

The above increase was partially offset by

- Decrease in legal expense by Rs.106 million due to lower litigation activity during the year.

As a per cent of revenues, the expense decreased to 28 per cent in 2005-06 from 32 per cent in 2004-05.

Depreciation & Amortisation

Depreciation & amortization expense increased by 29 per cent from Rs.1,256 million in 2004-05 to Rs.1,617 million in 2005-06 in line with increase in gross block and intangibles. The additional investments were incurred towards normal capital expenditure as well as new projects in formulations and generics. Amortization expense increased to Rs.436 million in 2005-06 primarily due to amortization related to the acquisition in Mexico and betapharm.

Research & Development

Research & development expenses decreased by 24 per cent from Rs.2,297 million in 2004-05 to Rs.1,737 million in 2005-06. As per cent of revenues, the expense decreased to 9 per cent in 2005-06 from 13 per cent due to the following reasons –

- Decrease in expenses at drug discovery by Rs.340 million primarily due to lower expenses on clinical trials.
- Decrease in research and development expenses in generics.
- During the year, the Company recognized an income of Rs.384 million as against Rs.96 million under the R&D partnership with ICICI Venture.

Other income

Other income for the financial year 2005-06 amounted to Rs.1,206 million as compared to Rs.657 million in financial year 2004-05. This includes profit on sale of finished dosages facility at Goa for Rs.388 million as well as increase in interest income by Rs.319 million. It was partially offset by decrease in profit on sale of investments by Rs.69 million.

Income Tax

Provision for income tax (inclusive of fringe benefit tax) for the financial year 2005-06 amounted to Rs.546 million as compared to benefit of Rs.181 million in financial year 2004-05. This was due to overall increase in profits.

Profit After Tax

Net income increased from Rs.329 million in 2004-05 to Rs.1,467 million in 2005-06. Net income was 6 per cent of net revenues in 2005-06 compared to 2 per cent in 2004-05.

HUMAN RESOURCES

People have made all the difference to us. From our humble beginnings, through all our appointments and disappointments, we have been proud of our people and the way we have earned their sense of engagement. We continue to build our people processes based on the three pillers of Innovation, Entrepreneurship and Globalization.

Diversity in our talent gene pool has been a conscious choice for us. As we spread our wings, we are trying to help integrate such diversity to build a truly global organisation. We have used our strong people-centric ethic and values as an integrating lever, both in our organic and inorganic growth.

As on March 31, 2006, the Company and its subsidiaries had 7,525 employees working throughout the globe. During the year, we witnessed smooth and peaceful industrial relations with increased participation from all employees in various management initiatives. For more details on the Human Resources, please refer page 20 in this annual report.

INTERNAL CONTROLS AND RISK MANAGEMENT

Dr. Reddy's has designed a system of internal control with the objective of safeguarding the Company's assets, ensuring that transactions are properly authorized, and providing significant assurance at reasonable cost, of the integrity, objectivity and reliability of financial information. The management of Dr. Reddy's duly considers and takes appropriate action on recommendations made by the statutory auditors, internal auditors, and the audit committee of the Board. Details of internal controls are given in the chapter on corporate governance.

It is testimony to the quality of Dr. Reddy's internal control systems for financial reporting that the Company is now SOX-404 compliant in May 2006 — a full ten months before the mandated date for foreign SEC registrants. It makes Dr. Reddy's one of the earliest foreign compliants of SOX-404, and the first of its kind among manufacturing companies in India. Getting the SOX-404 certification was a mammoth across-the-Board task that was kicked off 18 months ago. Driven by the Company's Audit Committee, its internal audit team, its systems integration team, Business heads as well as finance team, the Company succeeded in getting the certification well before the SEC deadline. Thanks to the systems and documentation put in place because of SOX-404, Dr. Reddy's today can claim to have global best-in-class internal controls, especially those that relate to financial reporting.

The Company has a detailed risk management framework, which is not only integrated to the key controls under SOX-404 but also evaluate other strategic, business, operational and reporting risks. The risk management team at Dr. Reddy's regularly prepares risk reports that identify and quantify various risks, assign risk owners, set out mitigating mechanisms and actions taken thereto, and evaluate the residual risks. Reports of the risk management team are fully discussed with the Audit Committee of the Company's Board of Directors.

OPPORTUNITIES, THREATS, RISKS AND CONCERNS

Given its objective of becoming a discovery-led global pharmaceutical Company, Dr. Reddy's long-term operations will depend, to a large extent, upon its ability to successfully patent and commercialise its own Discovery molecules and Specialty products. The process of development and commercialisation of new molecules is time consuming as well as costly. On an average, it takes between nine to 12 years to develop a new molecule from the laboratory stage to a form ready for patented commercial launch. The Company's inability to obtain necessary regulatory approvals for its products or failure of a product at any stage may disturb its future revenue projections. Even in the Specialty business in the U.S., delays or denial of regulatory approvals may affect future revenue projections. In view of the number of patent expiries coming up in the near future, sales of patent expiry drugs in the U.S. as well as Europe represents significant opportunity for all generic and API manufacturers. However, obtaining 180-days exclusivity is getting increasingly difficult in the U.S., and the generics market is becoming rapidly commoditised. The Company's Generics business could be affected if branded pharmaceutical companies are successful in limiting the use of generics through aggressive legal defence tactics as well as authorised generics deals, development of combination products and over-the-counter switching. In addition, there is increasing competition from companies from India and Eastern Europe, which may put pressure on price realisations. The Company continues to carry risks of competition, litigations, regulatory and legislative reforms in its global Generics business. In India, the Government of India through the Drugs (Prices Control) Order, 1995 (DPCO) imposes price controls for specified pharmaceutical products under certain circumstances. Adverse changes in the DPCO list or in the span of price control can affect pricing, and hence, Indian revenues. Similarly, the German government passed the Economic Optimization of the Pharmaceutical Care Act (Arzneimittelversorgungs-Wirtschaftlichkeisgestz, AVWG) which became effective May 1, 2006, which again tries to contain the cost increase in the area of pharmaceuticals. Measures taken are, amongst others, forbiddance of free goods to pharmacists, limitation of rebates to wholesaler and pharmacists, forbiddance of price increases for generics for 2 years, implementation of additional mandatory rebates of 10 per cent if pharmaceutical prices are not 30 per cent below the fixed prices, reduction of fixed prices as of July 1, 2006, possibility to waive co-payments of patients by the SHI organizations. The impact of these changes on the competitive landscape will unfold in 2006-07. Also, with the introduction of product patent protection in India with effect from January 1, 2005, it is expected that the new product launch opportunity for Indian manufacturers of API and finished dosages will narrow over the next few years.

OUTLOOK

The Company looks forward to a healthy financial performance in 2006-07. The Company expects to maintain the growth momentum in the established businesses of APIs and Formulations. The Company expects significant increase in revenues in the U.S. Generics segment driven by the launch of several new products. 2006-07 also represents the first full year of consolidation of financials of the two acquisitions – betapharm in Germany and acquisition of Roche’s API business at Cuernevaca in Mexico. The Company will continue to actively pursue business development opportunities in all key geographies in terms of partnerships, alliances and acquisitions to further accelerate future growth opportunities.

CAUTIONARY STATEMENT

The management of Dr. Reddy’s has prepared and is responsible for the financial statements that appear in this report. These financial statements are in conformity with accounting principles generally accepted in India and in the U.S., and therefore include amounts based on informed judgments and estimates. The management also accepts responsibility for the preparation of other financial information that is included in this report.

This presentation includes some forward-looking statements, as defined in the U.S. Private Securities Litigation Reform Act of 1995. The management has based these forward-looking statements on its current expectations and projections about future events. Such statements involve known and unknown risks, uncertainties and other factors that may cause actual results to differ materially. These factors include, but are not limited to, changes in local and global economic conditions, the Company’s ability to successfully implement its strategy, the market’s acceptance of and demand for its products, growth and expansion, technological change and exposure to market risks. By their nature, these expectations and projections are only estimates and could be materially different from actual results in the future.

corporate governance

Dr. Reddy's Laboratories Limited's ("Dr. Reddy's" or the "Company") long-standing commitment to high standards of corporate governance and ethical business practices is a fundamental shared value of its Board of Directors, management and employees. The Company's philosophy of corporate governance stems from its belief that timely disclosures, transparent accounting policies, and a strong and independent Board go a long way in preserving shareholders trust while maximising long-term corporate value.

RECENT DEVELOPMENTS

Securities and Exchange Board of India ("SEBI"), vide circular SEBI/CFD/DIL/CG/1/2004/ 12/10 dated October 29, 2004, issued the revised Clause 49 of the listing agreement, which was to come into effect on April 1, 2005. Since it was brought to SEBI's notice that a large number of companies were still not in a state of preparedness to be fully compliant with the requirements as contained in the revised Clause 49, SEBI vide its circular no. SEBI/CFD/DIL/CG/1/2005/29/3 dated March 29, 2005 extended the date for ensuring compliance with the revised Clause 49 of the listing agreement up to December 31, 2005. The revised Clause 49 thus has come into effect from January 1, 2006.

This section of the Annual Report discusses the compliance with the erstwhile Clause 49 of the listing agreement till December 31, 2005 and with the new Clause 49 with effect from January 1, 2006 to March 31, 2006

This section of the Annual Report, the information given under 'Management Discussion and Analysis' and 'Additional Shareholders' Information' constitutes the compliance report of the Company on corporate governance during the year 2005-06.

BOARD OF DIRECTORS

COMPOSITION

As on March 31, 2006, the Board of Dr. Reddy's had nine Directors, comprising three executive Directors, including the Chairman, and six independent Directors as defined under listing agreement with Indian Stock Exchanges and Corporate Governance Guidelines of New York Stock Exchange Inc. ("NYSE"). Detailed profile of Directors have been discussed in this annual report on page no.28.

The Directors bring in expertise in the fields of medicinal chemistry, medical research, human resource development, strategy, management, finance and economics. The Board provides leadership, strategic guidance, objective and independent view to the Company's management while discharging its fiduciary responsibilities, thereby ensuring that the management adheres to high standards of ethics, transparency and disclosure.

Every Director informs the Company annually about the Board and Board Committee positions he occupies in other companies including Chairmanships and notifies changes as and when they take place.

Table 1 gives the composition of Dr. Reddy's Board, their positions, relationship with other Directors, date of joining the Board, other Directorships and memberships of Committees held by each of them.

MEMBERSHIP TERM

As per the provisions of the Companies Act, 1956 one-third of the Board members (other than executive Directors) who are subject to retire by rotation shall retire every year, and the approval of the shareholders is sought for the re-appointment of the retiring members, if found eligible. Executive Directors are appointed by the shareholders

TABLE 01 Composition of Dr. Reddy's Board as on March 31, 2006

NAME	POSITION	RELATIONSHIP WITH OTHER DIRECTORS	DATE OF JOINING	DIRECTORSHIPS IN INDIA U/S 275 OF THE COMPANIES ACT, 1956	OTHER DIRECTORSHIPS[1]	COMMITTEE MEMBERSHIP[2]	CHAIRMANSHIP IN COMMITTEES[2]
Dr. K Anji Reddy	Chairman	Father of Mr. Satish Reddy & father-in-law of Mr. G V Prasad	February 24, 1984	4	36	–	–
Mr. G V Prasad	Vice Chairman & CEO	Son-in-law of Dr. K Anji Reddy & brother-in-law of Mr. Satish Reddy	April 8, 1986	8	35	–	–
Mr. Satish Reddy	Managing Director & COO	Son of Dr. K Anji Reddy & brother-in-law of Mr. G V Prasad	January 18, 1993	5	37	–	–
Mr. Anupam Puri	Independent Director	None	June 4, 2002	6	–	2	–
Dr. Krishna G Palepu	Independent Director	None	January 29, 2002	2	2	1	–
Dr. Omkar Goswami	Independent Director	None	October 30, 2000	7	1	7	2
Mr. P N Devarajan	Independent Director	None	October 30, 2000	3	1	2	1
Mr. Ravi Bhoothalingam	Independent Director	None	October 30, 2000	3	–	2	1
Dr. V Mohan	Independent Director	None	March 8, 1996	1	2	–	–

(1) Other Directorships are those, which are not covered under Section 275 of the Companies Act, 1956.

(2) Membership / Chairmanship in Audit and Shareholders' Grievance Committees of all public limited companies, whether listed or not, including Dr. Reddy's. Private limited companies, foreign companies and companies under Section 25 of the Companies Act, 1956 have been excluded.

for a maximum period of five years at a time, but are eligible for re-appointment upon completion of their term. The appointments and re-appointments of Directors are considered by the Board on the recommendations of the Nomination Committee.

SELECTION AND APPOINTMENT OF NEW DIRECTORS

The Board, on the recommendations of the Nomination Committee appoints a new Director. The charter of the Nomination Committee provides evaluation of the current composition and organization of the Board and review of the composition and size of the Board in order to ensure that the Board comprises of members reflecting the proper expertise, skills, attributes and personal and professional backgrounds for service as a Director of the Company.

SHAREHOLDING IN THE COMPANY

Table 2 gives details of the shares and stock options held by each of the Directors as on March 31, 2006.

MEETINGS

The Company prepares the schedule of the Board and Board Committee meetings a year in advance to assist the Directors in scheduling their program.

The schedule of meetings and agenda for meeting is finalized in consultation with lead independent Director. The agenda of the meeting is pre-circulated with detailed notes, supporting documents and executive summary.

Under Indian laws, the Board of Directors must meet at least four times a year, with a maximum time gap of four months between any two Board meetings. Dr. Reddy's Board met six times during the year under review – on May 6, 2005, July 26, 2005, August 31, 2005, October 29, 2005, January 24, 2006 and March 14, 2006. The Company

02 TABLE Shares and stock options held by Directors

AS ON MARCH 31, 2006

NAME	NO. OF SHARES HELD	STOCK OPTIONS HELD[2]
Dr. K Anji Reddy [1]	400,478	Nil
Mr. G V Prasad	675,720	Nil
Mr. Satish Reddy	597,916	Nil
Mr. Anupam Puri	2,000	3,000
Prof Krishna G Palepu	1,000	3,000
Dr. Omkar Goswami	Nil	3,000
Mr. P N Devarajan	Nil	3,000
Mr. Ravi Bhoothalingam	Nil	3,000
Dr. V Mohan	Nil	2,000

[1] *Shares held in individual capacity. In addition Dr. K Anji Reddy owns 40% of Dr. Reddy's Holdings Private Limited, which in turn owns 18,893,245 shares of Dr. Reddy's Laboratories Limited. Various members of his family own the balance shares in Dr. Reddy's Holdings Private Limited.*

[2] *Stock Options were granted to independent Directors in the Compensation Committee meeting held on May 6, 2005.*

held one Board meeting in each quarter as required under the Companies Act, 1956. The Company is in compliance with the provision of the listing agreement on the gap between two Board meetings.

Details of Directors and their attendance in Board meetings and Annual General Meeting are given in **Table 3.**

The Board and Board Committee meetings at Dr. Reddy's generally extend for two days. In the course of these meetings, the business unit heads and key management personnel made presentations to the Board.

03 TABLE Directors' attendance at Dr. Reddy's Board meetings and AGM

DURING THE FINANCIAL YEAR 2005-06

NAME	MEETINGS HELD IN DIRECTOR'S TENURE	NUMBER OF BOARD MEETINGS ATTENDED	ATTENDANCE IN LAST AGM ON JULY 27, 2005
Dr. K Anji Reddy[1]	6	4	Present
Mr. G V Prasad[1]	6	5	Present
Mr. Satish Reddy	6	6	Present
Mr. Anupam Puri[1]	6	4	Absent
Prof. Krishna G Palepu[1][2]	6	3	Absent
Dr. Omkar Goswami[1]	6	5	Present
Mr. P N Devarajan[1]	6	4	Present
Mr. Ravi Bhoothalingam	6	6	Present
Dr. V Mohan[1]	6	4	Present

[1] *Were given leave of absence on request.*

[2] *Prof. Krishna G Palepu attended one meeting by way of video conference. However he was considered absent in that meeting.*

INFORMATION GIVEN TO THE BOARD

The Company provides the following information to the Board or the Board Committees as and when required. Such information is submitted either as part of the agenda papers in advance of the meetings or are presented by way of presentations during the meetings of the Board or the Board Committees.

- Annual operating plans and budgets, capital budgets, updates, and all variances;
- Quarterly, half yearly and annual results of the Company and its operating divisions or business segments;
- Detailed presentations on the progress

in Research and Development and new drug discoveries;
- Minutes of meetings of Audit Committee and other Committees;
- Information on recruitment and remuneration of key executives below the Board level;
- Significant regulatory matters concerning Indian or Foreign regulatory authorities;
- Issue which involves possible public or product liability claims of a substantial nature;
- Risk analysis of various products, markets and businesses;
- Detailed analysis of potential acquisition targets, or possible divestments;
- Details of any Joint Venture or collaboration agreements;
- Transactions that involve substantial payment towards goodwill, brand equity or intellectual property;
- Significant sale of investments, subsidiaries assets, which are not in the normal course of business;
- Contracts in which Director(s) are deemed to be interested;
- Materially important show cause, demand, prosecution and penalty notices;
- Fatal or serious accidents or dangerous occurrences
- Significant effluent or pollution problems;
- Materially relevant default in financial obligations to and by the Company or substantial non-payment for goods sold by the Company;
- Significant labour problems and their proposed solutions;
- Significant development in the human resources and industrial relations fronts;
- Quarterly details of foreign exchange exposure and the steps taken by management to limit the risks of adverse exchange rate movement;
- Non-compliance of any regulatory or statutory nature or listing requirements as well as shareholder services such as non-payment of dividend and delays in share transfer; and
- Subsidiary companies minutes, financial statements, significant investments and significant transactions and arrangements.

BOARD ONLINE

The Company has created an online portal exclusively for the Board of Directors. The portal called "Board Online" keeps the Board members updated on all key information related to the Company. The Directors can access presentations, documents, agenda notes and minutes of all previous meetings online for their reference. They can also access key reports posted periodically at this portal. The portal also keeps them updated on the industry and the Company news.

REVIEW MEETINGS

The initiative undertaken last year to convene review meetings of Directors in addition to the regular Board and Board Committee meetings was continued during the year. The Company facilitates review meetings between the Board meeting dates wherein a group of Directors meet and review select topics in greater detail. This practice enables the Directors to get involved in comprehensive analysis of key themes and areas of work, and allows them to give their detailed inputs. During 2005-06, there were two review meetings conducted on August 31, 2005 and December 27, 2005. The minutes of such meetings are made part of the agenda of the ensuing Board meeting.

The Company also organizes meetings of various business and functional heads (Management Council members) with the Directors during the Board meeting dates. The Management Council members look forward to Directors on their inputs and suggestions on various strategic and operational matters in their respective business / functional areas. In addition, the Company organizes periodic visits by Directors to its research and manufacturing locations to enable them to understand better the business operations and also to provide an opportunity to employees to interact with Directors.

MEETINGS IN EXECUTIVE SESSION

During the financial year, the independent Directors of Dr. Reddy's met twice without the management in an executive session. The Company intends to further facilitate such sessions as and when required by the independent Directors. Executive sessions generate ideas for improvements in Board processes. A lead Director among the independent Directors has been identified to provide structured feedback to the management to encourage healthy discussions and openness amongst the members of the Board.

REVIEW OF PERFORMANCE OF BOARD AND BOARD COMMITTEES

During the year, the independent Directors discussed and reviewed, in an executive session, the time invested by them in the Company in the context of the reviews and decisions taken at the Board and Committee meetings. The time investment was estimated based on agenda analysis. They also reviewed the time invested in strategy reviews, internal controls review, new investment proposals, human resource matters, financial analysis and operational matters and the major outcomes of the decisions taken thereat. An independent Director led the analysis and later briefed the Board on the outcome of the analysis.

DIRECTOR'S REMUNERATION

The remuneration, including the commission based on the net profits of the Company for the three executive Directors is recommended by the Compensation Committee of the Board and is then approved by the Board. The independent Directors receive sitting fees for attending the meeting of Board and Board Committees and commission based on the net profits of the Company. The remuneration including commission payable to the Directors during the year under review was in conformity with the applicable provisions of the Companies Act, 1956 and duly approved by the Board and the shareholders.

The remuneration paid or payable to the Directors for their services rendered during 2005-06 is given in **Table 4**.

The executive Directors of the Company are appointed by the shareholders' resolution for a period of 5 years. No severance fees is payable to the executive Directors. Except the Commission payable to the executive Directors all other components of remuneration are fixed and are in line with the Company's policies.

The Company granted stock options to independent Directors on May 6, 2005. The exercise price of the options is Rs.5 each. The options have graded vesting of 25% options vesting each year for 4 years and the exercise period is 5 years from the date of vesting.

Following is the criteria for making payments to the independent Directors:

1. The independent Directors are paid sitting fees for each meeting of the Board or Board Committee @ Rs.5,000 per meeting attended by them.
2. The shareholders of the Company approved the payment of commission up to 0.5% of net profits calculated in accordance with Section 198 of the Companies Act, 1956 to all the independent Directors collectively. The Board decides the amount of commission payable to these independent Directors every year within the overall limit of 0.5% of the net profit.
3. The Remuneration paid to the independent Directors is determined keeping in view the industry benchmarks and also on the basis of their memberships in various committees of the Board.

04 TABLE

Remuneration paid / payable to the directors for Financial Year 2005-06

IN RS. THOUSANDS

NAME OF DIRECTORS	SITTING FEES[1]	COMMISSIONS[2]	SALARIES	PERQUISITES[3]	TOTAL	STOCK OPTIONS
Dr. K Anji Reddy	NA	23,051	1,800	144	24,995	NA
Mr. G V Prasad	NA	12,488	1,514	195	14,197	NA
Mr. Satish Reddy	NA	12,457	1,500	195	14,152	NA
Mr. Anupam Puri	75	1,785	NA	NA	1,860	3,000
Prof. Krishna G Palepu	50	1,785	NA	NA	1,835	3,000
Dr. Omkar Goswami	80	1,785	NA	NA	1,865	3,000
Mr. P N Devarajan	60	1,785	NA	NA	1,845	3,000
Mr. Ravi Bhoothalingam	75	1,785	NA	NA	1,860	3,000
Dr. V Mohan	20	892	NA	NA	912	2,000

[1] Sitting fees include fees for Board as well as Board Committee meetings @ Rs.5,000 per meeting.

[2] Commissions are variable, and based on percentage of net profit calculated according to Section 198 of the Companies Act, 1956. The commissions would be paid after the approval of shareholders at the Annual General Meeting.

[3] Perquisites include house rent allowance, medical reimbursement for self and family according to the rules of the Company, leave travel assistance, personal accident insurance, Company's vehicle for official use with driver, telephone at residence and mobile phone, contribution to Provident Fund and Superannuation Scheme. All these benefits are fixed in nature.

Following is the criteria for making payments to the executive Directors:

1. The executive Directors are paid salary as recommended by the Compensation Committee and approved by the shareholders. The perquisites and retirement benefits are also paid as per the HR compensation policies of the Company as applicable to all employees.
2. The shareholders of the Company approved the payment of commission on the net profits calculated in accordance with Section 198 of the Companies Act, 1956 to all executive Directors. The Compensation Committee decides the amount of commission every year within the overall limit.
3. The Remuneration paid to the executive Directors is determined keeping in view the industry benchmarks.

LEAD INDEPENDENT DIRECTOR

The independent Directors of the Company have identified the following lead independent Directors for various matters:

MR. RAVI BHOOTHALINGAM—Board and Board Committee meetings agenda and its development / improvement;

PROF. KRISHNA G PALEPU—Board processes and their improvement / optimisation and giving structured feedback to Board on the outcome of executive sessions of independent Directors meetings;

MR. ANUPAM PURI—Strategy matters;

DR. OMKAR GOSWAMI—Finance, internal controls, risk and compliance matters;

MR. P N DEVARAJAN—Chief Ombudsman for the Whistle Blower Policy of the Company.

RISK MANAGEMENT

The Company has a detailed enterprise-wide risk management system in place. During the year, detailed presentations were made to the Board on the enterprise-wide risk management system and a process was set up to inform Board members about the risk assessment and minimization procedures. These procedures shall be periodically reviewed to ensure that management controls risk through means of a properly defined framework.

COMPLIANCE REVIEWS

Dr. Reddy's has a dedicated team and a defined framework to review the compliances with all laws applicable to the Company. The compliance status is periodically updated to the senior management team. Presentations are scheduled every quarter in the Audit Committee Meetings on compliance status.

CODE OF BUSINESS CONDUCT AND ETHICS AND OMBUDSMAN PROCEDURE

The Company has adopted a Code of Business Conduct and Ethics (the "Code"), which applies to all employees and Directors of the Company, its subsidiaries and affiliates. It is the responsibility of all employees and Directors to familiarize themselves with this Code and comply with its standards.

An Ombudsman Procedure has also been made under this Code, which describes the Ombudsman framework and procedures for investigation and communication of any report on any violation or suspected violation of Code, appeal against any decision taken by Ombudsman, and submission of complaint against any retaliation action against any employee. An independent Director has been appointed as Chief Ombudsman, and the reports and complaints submitted to the Company are reported to the Audit Committee.

The Code of Business Conduct and Ethics and Ombudsman Procedure has been posted on the Company's website www.drreddys.com

The Board and the Senior Management affirms compliance with the Code of Business Conduct and Ethics annually. A certificate of the Chief Executive Officer of the Company to this effect is enclosed as Exhibit 1 to this section.

RELATED PARTY TRANSACTIONS

The details of related party transactions are discussed in detail in page no.112 of this Annual Report.

All related party transactions during the year, whether in the ordinary course of business or not, were placed before the Audit Committee. All related party transactions were on arm's length basis.

SUBSIDIARY COMPANIES

The Audit Committee of the Company reviews the financial statements of the subsidiary companies. During the year the Audit Committee of the Company also reviewed the investments made by the subsidiary companies, minutes of the Board meetings of the subsidiary companies and statement of all significant transactions and arrangements entered into by the subsidiary companies. No Indian subsidiary of the Company falls under the term "material non listed Indian subsidiary" as defined under amended Clause 49 of the listing agreement.

DISCLOSURE ON ACCOUNTING TREATMENT

In the preparation of financial statements for the financial year 2005-06, there is no treatment of any transaction different from that prescribed in Accounting Standards.

COMMITTEES OF THE BOARD

The Board Committees appointed by the Board focus on specific areas and make informed decisions within the authority delegated. Each Committee of the Board is guided by its Charter, which defines the composition, scope and powers of the committee. The Committees also make specific recommendations to the Board on various matters from time-to-time. All decisions and recommendations of the Committees are placed before the Board for information or for approval. The Company has seven Board-level Committees, namely:

- Audit Committee
- Compensation Committee
- Nomination Committee
- Strategy Committee
- Shareholders' Grievance Committee
- Investment Committee
- Management Committee

a) Audit Committee

The management is responsible for the Company's internal controls and the financial reporting process while the statutory auditors are responsible for performing independent audits of the Company's financial statements in accordance with generally accepted auditing practices and for issuing reports based on such audits. The Board of Directors has entrusted the Audit Committee to supervise these processes and thus ensure accurate and timely disclosures that maintain the transparency, integrity and quality of financial control and reporting.

The primary responsibilities of the Audit Committee are to:

- Supervise the financial reporting process;
- Review the financial results before placing them to the Board along with related disclosures and filing requirements;
- Review the adequacy of internal controls in the Company, including the plan, scope and performance of the internal audit function;
- Discuss with management the Company's major policies with respect to risk assessment and risk management;
- Hold discussions with statutory auditors on the nature and scope of audits, and any views that they have about the financial control and reporting processes;
- Ensure compliance with accounting standards, and with listing requirements with respect to the financial statements;
- Recommend the appointment and removal of external auditors and their fees;
- Review the independence of auditors;
- Ensure that adequate safeguards have been taken for legal compliance both for the Company and its other Indian as well as foreign subsidiaries;
- Review related party transactions;
- Review the functioning of Whistle Blower mechanism and
- Implementation of the applicable provisions of the Sarbanes Oxley Act, 2002.

The Audit Committee is entirely composed of independent Directors and all members of the Audit Committee are financially literate and bring in expertise in the fields of finance, economics, human

05 TABLE

Audit Committee attendance

DURING THE FINANCIAL YEAR 2005-06

COMMITTEE MEMBERS	POSITION	MEETINGS HELD	MEETINGS ATTENDED
Dr. Omkar Goswami(1)	Chairman	5	4
Mr. Anupam Puri(1)	Member	5	4
Prof. Krishna G Palepu(1)	Member	5	3
Mr. P N Devarajan(1)	Member	5	3
Mr. Ravi Bhoothalingam	Member	5	5

(1) *Were given leave of absence on request.*

resource development, strategy and management. Mr. Ravi Bhoothalingam, independent Director on the Board has accounting or related financial management expertise.

The Audit Committee met five times during the year – on May 5, 2005, July 26, 2005, October 29, 2005, January 24, 2006 and March 14, 2006. The Company is in compliance with the provisions of the amended Clause 49 of the listing agreement on the gap between two Audit Committee meetings. In addition, the Chairman of the Audit Committee and some other members of the Audit Committee met additionally to review other processes, particularly the progress on internal control mechanisms to prepare for certification under Section 404 of the Sarbanes Oxley Act, 2002. **Table 5** gives the composition and attendance record of Audit Committee.

The Chief Executive Officer, Chief Financial Officer and Chief Internal Auditor are permanent invitees to all Audit Committee meetings. The statutory auditors of the Company were present in all the Audit Committee meetings during the year. The Company Secretary is the Secretary of the Committee.

The Audit Committee meetings were generally half a day sessions, except in the case of half-yearly and annual results, where they extend to full day sessions. The agenda for the Audit Committees, inter-alia, included the following items:

- Review of financial performance, including business level financial performance;
- Internal audit, control matters and risk management, including action-taken reports;
- Status on the implementation of the compliance with Section 404 of the Sarbanes Oxley Act, 2002;
- Discussion with statutory auditors, including new accounting policies relating to Indian as well as U.S. accounting principles and practices; and
- Detailed operational and financial risk appraisals, as well as risks relating to legal compliance.

The internal and statutory auditors of the Company discuss their audit findings and updates with the Audit Committee and submit their views directly to the Committee. Meetings with internal auditors focus on detailed reviews of the processes and internal controls in the Company. This practice enables the Directors in smaller groups to devote more time towards business and financial performance during the Audit Committee meetings.

The report of the Audit Committee is enclosed as Exhibit 2 to this section.

b) Compensation Committee

The Compensation Committee reviews the performance and considers and recommends to the Board the compensation of the executive Directors and executives above Vice-President level, and also reviews the remuneration package offered by the Company to different grades/levels of its employees.

While reviewing the remuneration of senior management personnel, the Committee takes into account the following:

- Financial position of the Company;
- Trends in the industry;
- Appointee's qualification;
- Experience;
- Past performance;
- Past remuneration; etc.

The Compensation Committee also administers Dr. Reddy's Employee Stock Option Scheme, 2002. The details of stock options granted by the Committee have been discussed in detail in the Directors' Report.

The Executive Vice President and Global Chief of Human Resources, IT and Business Process Excellence makes periodic presentations to the Compensation Committee on performance appraisals, increments and performance bonus recommendations. The discussions and presentations keep the Directors updated on various Human Resources matters.

06 TABLE

Compensation Committee attendance

DURING THE FINANCIAL YEAR 2005-06

COMMITTEE MEMBERS	POSITION	MEETINGS HELD	MEETINGS ATTENDED
Mr. Ravi Bhoothalingam	Chairman	3	3
Mr. Anupam Puri[(1)]	Member	3	2
Prof. Krishna G Palepu[(1)]	Member	3	1
Dr. Omkar Goswami	Member	3	3
Mr. P N Devarajan[(1)]	Member	3	2

[(1)] *Were given leave of absence on request.*

The Compensation Committee is entirely composed of independent Directors.

The Compensation Committee met three times during the year on May 6, 2005, August 31, 2005 and January 24, 2006. **Table 6** gives the composition and attendance record of the Compensation Committee.

The Executive Vice President and Global Chief of Human Resource, IT and BPE is the Secretary of the Committee.

The report of the Compensation Committee is enclosed as Exhibit 3 to this section.

07 TABLE — Nomination Committee attendance

DURING THE FINANCIAL YEAR 2005-06

COMMITTEE MEMBERS	POSITION	MEETINGS HELD	MEETINGS ATTENDED
Mr. Anupam Puri	Chairman	1	1
Prof. Krishna G Palepu[1]	Member	1	–
Dr. Omkar Goswami	Member	1	1
Mr. P N Devarajan[1]	Member	1	–
Mr. Ravi Bhoothalingam	Member	1	1

[1] *Were given leave of absence on request.*

c) Nomination Committee

The role of the Nomination Committee is to:

- Shortlist nominees for induction to the Board of the Company;
- Selection of nominees on the Board of the Company;
- Recommend appointment of members to the Board for its consideration; and
- Review principles of corporate governance of the Company.

The Nomination Committee is entirely composed of independent Directors. The Company Secretary is the Secretary of the Committee.

The Nomination Committee met once during the year on May 6, 2005. **Table 7** gives the composition and attendance record of the Nomination Committee.

d) Strategy Committee

The role of this Committee is to:

- Participate with management to develop or modify the Company's strategies;
- Recommend to the Board the adoption or modification of the Company's strategies;
- Participate with management to develop or modify the Company's merger and acquisition plans;
- Oversee the development of plans to implement different strategies;
- Review progress and implementation of the strategies; and
- Assess and provide guidance on internal and external trends and developments that impact both the strategy and its execution.

The Strategy Committee is composed of independent Directors and executive Directors. The Chairman of the Committee is an independent Director.

The Committee held four meetings during the year on May 6, 2005, July 26, 2005, October 29, 2005 and January 23, 2006. **Table 8** gives the composition and attendance record of the Strategy Committee. The Company Secretary is the Secretary of the Committee.

08 TABLE — Strategy Committee attendance

DURING THE FINANCIAL YEAR 2005-06

COMMITTEE MEMBERS	POSITION	MEETINGS HELD	MEETINGS ATTENDED
Prof. Krishna G Palepu[1]	Chairman	4	3
Mr. Anupam Puri	Member	4	4
Mr. G V Prasad	Member	4	4
Dr. Omkar Goswami[1]	Member	4	3
Mr. Satish Reddy	Member	4	4

[1] *Were given leave of absence on request.*

e) Shareholders' Grievance Committee

The Shareholders' Grievance Committee is empowered to perform all the functions of the Board in relation to handling of Shareholders' Grievances.

The Committee primarily focuses on:

- Review of investor complaints and their redressal;
- Review of the queries received from investors;
- Review of the work done by Share Transfer Agent; and
- Review of the corporate actions related work.

The Shareholders' Grievance Committee consists of three Directors including two executive Directors. The Chairman of the Committee is an independent Director.

The Committee met three times during the year on May 6, 2005, October 29, 2005 and January 24, 2006. **Table 9** gives the composition and attendance record of the Shareholders' Grievance Committee. The Company Secretary is the Secretary of the Committee who is designated as Compliance Officer of the Company.

An analysis of investor queries and complaints received during the year and pending disposal is given in the Additional Shareholders' Information section of this annual report.

f) Investment Committee

The Investment Committee reviews the Company's capital investment proposals and ongoing projects.

The Investment Committee consists of three Directors including two executive Directors. The Chairman of the Committee is an executive Director.

The Committee held two meetings during the year on December 27, 2005 and February 15, 2006

Table 10 gives the composition and attendance record of the Investment Committee.

The Company Secretary is the Secretary of the Committee.

During the year, the Committee approved the investments in the subsidiary companies and approved new projects for Integrated Product Development Organization, Generics, Customs Pharmaceutical Services facilities at Hyderabad and Visakhapatnam.

09 TABLE — Shareholders' Grievance Committee attendance

DURING THE FINANCIAL YEAR 2005-06

COMMITTEE MEMBERS	POSITION	MEETINGS HELD	MEETINGS ATTENDED
Mr. P N Devarajan[1]	Chairman	3	2
Mr. G V Prasad	Member	3	3
Mr. Satish Reddy	Member	3	3

[1] *Was granted leave of absence on request.*

g) Management Committee

The role of Management Committee is to authorise Directors and officers of the Company to deal with day to day business operations such as banking, treasury, insurance, excise, customs, administrative and dealing with other Government / Non Government authorities; approve loans to subsidiaries or other entities / persons up to an overall limit of Rs.250 million; and approve borrowings from any person up to an overall limit of Rs.250 million.

The Management Committee consists of three Directors including two executive Directors. The Chairman of the Committee is an executive Director.

The Committee held nine meetings during the year on April 8, 2005, May 13, 2005, July 14, 2005, August 3, 2005, September 6, 2005, November 11,

10 TABLE — Investment Committee attendance

DURING THE FINANCIAL YEAR 2005-06

COMMITTEE MEMBERS	POSITION	MEETINGS HELD	MEETINGS ATTENDED
Mr. G V Prasad	Chairman	2	2
Mr. P N Devarajan[1]	Member	2	1
Mr. Satish Reddy	Member	2	2

[1] *Was granted leave of absence on request.*

11 TABLE	Management Committee attendance DURING THE FINANCIAL YEAR 2005-06		
COMMITTEE MEMBERS	**POSITION**	**MEETINGS HELD**	**MEETINGS ATTENDED**
Mr. Satish Reddy	Chairman	9	9
Mr. G V Prasad	Member	9	9
Mr. P N Devarajan[1]	Member	9	–

[1]Was granted leave of absence on request.

2005, December 8, 2005, February 6, 2006 and March 2, 2006. **Table 11** gives the composition and attendance record of the Management Committee. The Company Secretary is the Secretary of the Committee.

MANAGEMENT

The management of Dr. Reddy's has developed and implemented policies, procedures and practices that attempt to translate the Company's core purpose and mission into reality. The management also identifies, measures, monitors and minimizes the risk factors in the business and ensures safe, sound and efficient operation. These are internally supervised and monitored through the Management Council.

MANAGEMENT COUNCIL

Dr. Reddy's Management Council consists of all senior management members from the business units and corporate centre of the Company. It has a balanced representation from the Indian as well as its overseas offices. **Table 12** gives the details of the members of Management Council as on March 31, 2006:

PHOTOGRAPH TAKEN AT THE MANAGEMENT COUNCIL MEETING HELD ON JANUARY 22, 2006 AT HYDERABAD

STANDING LEFT TO RIGHT Raghu Cidambi, Alan Sheppard, Arun Sawhney, K Sankara Rao, Saumen Chakraborty, Mark Hartman, Andrew J Miller, Dr. Uday Saxena, Dr. R Rajagopalan, Abhijit Mukherjee, Ashwani Kumar Malhotra

SITTING LEFT TO RIGHT Satish Reddy, V S Vasudevan, G V Prasad, Jaspal Singh Bajwa, Jeffrey Wasserstein

TABLE 12

Details of Management Council Members

AS ON MARCH 31, 2006

SR. NO.	NAME AND DESIGNATION	QUALIFICATION	AGE	EXPERIENCE IN YEARS	DATE OF COMMENCEMENT OF EMPLOYMENT	PARTICULARS OF LAST EMPLOYMENT
1	G V PRASAD Vice Chairman and Chief Executive Officer	B.Sc. (Chem. Eng.), M.S. (Indl. Admn.)	45	22	30.06.1990	Promoter Director, Benzex Labs Private Limited
2	SATISH REDDY Managing Director and Chief Operating Officer	B.Tech., M.S.	38	14	18.01.1993	Director, Globe Organics Limited
3	ABHIJIT MUKHERJEE President – Developing Businesses	B.Tech. (Chem.)	47	25	15.01.2003	President, Atul Limited
4	ALAN SHEPPARD Executive Vice President – Europe Generics	B.Tech. (Hons.)	58	35	01.11.2004	Vice President, Global Corporate Strategy, Pliva
5	ANDREW J MILLER Executive Vice President and General Counsel	B.A., J.D.	50	26	08.01.2002	Partner, Budd Larner
6	ARUN SAWHNEY President – Global API	B.Com. PGDBM	50	29	01.06.2001	Chief Executive, Max-GB Limited
7	ASHWANI KUMAR MALHOTRA Senior Vice President – Formulations TechOps	M.Pharma., PGD-IE&M, PGD-CS	50	26	08.02.2001	Unit Head, Cipla Limited
8	JASPAL SINGH BAJWA President – Branded Formulations (ROW)	MBA	54	29	10.04.2003	Executive Director and COO, Marico Industries Limited
9	JEFFREY WASSERSTEIN Executive Vice President – Specialty Operations	B.A., J.D.	47	23	31.01.2005	EVP & Chief Business Officer, Avigenics, Inc.
10	K SANKARA RAO Executive Vice President – Integrated Product Development	M.Pharma.	52	28	29.09.1986	Production Executive, Cipla Limited
11	MARK HARTMAN Executive Vice President – North America Generics	B.Sc. Dairy Science, Virginia Tech.	47	21	04.01.2002	VP Sales & Marketing, Generics, Watson Laboratories
12	DR. R RAJAGOPALAN President – Discovery Research	M.Sc., Ph.D.	56	33	18.04.1994	Principal Research Scientist, Hoechst India Limited
13	RAGHU CIDAMBI Advisor	B.Sc., PGDBM, LLB.	55	36	01.10.2001	Director, Eenadu, Margadarsi Group
14	SAUMEN CHAKRABORTY Executive Vice President & Global Chief of HR, IT & BPE	B.Sc.(H), PGDM	45	22	02.07.2001	Vice President, Tecumseh
15	DR. UDAY SAXENA Chief Scientific Officer	Ph.D.	48	16	03.03.2003	Vice President, Preclinical Research, AtheroGenics Inc.
16	V S VASUDEVAN President & Chief Financial Officer	B.Com., ACA	54	32	01.04.1986	Finance Head, Standard Equity Fund Limited

For further details on Management Council members please visit the corporate website of the Company www.drreddys.com

The Management Council meets once in a quarter for two to four full day sessions. The background notes for the meetings are circulated in advance to facilitate decision-making. Listed below are some of the key issues that were considered by the management council in the year under review:

- Company's long term strategy, growth initiatives and priorities;
- Monitoring overall Company performance, including the performance of various business units;
- Decision on major corporate policies;
- Discussion and sign off on annual plans, budgets and investments and any other major initiatives; and
- Discussion on business alliances proposals.

MANAGEMENT DISCUSSION AND ANALYSIS

This annual report has a detailed section on management discussion and analysis.

MANAGEMENT DISCLOSURES

Senior management of the Company (Employees at General Managers and above levels and certain identified key employees) make annual disclosures to the Board relating to all material financial and commercial transactions, where they have personal interest, if any, that may have a potential conflict with the interest of the Company at large. Such transactions have been discussed in detail in financials sections of this Annual Report under Related Party Transactions.

PROHIBITION OF INSIDER TRADING

The Company has implemented a policy prohibiting Insider Trading in conformity with applicable rules of the Securities Exchange Board of India (SEBI) and Securities Exchange Commission (SEC) of United States of America. The necessary procedures have been laid down for employees, connected persons and persons deemed to be connected for trading in the securities of the Company. The blackout periods, when the employees are not expected to trade in the securities of the Company, are intimated to all employees from time to time.

INTERNAL CONTROL SYSTEMS

Effective governance consists of competent management; implementation of standard policies and processes; maintenance of an appropriate audit program and internal control environment and effective risk monitoring and management information systems.

Dr. Reddy's has both external and internal audit systems in place. Auditors have access to all records and information of the Company. The Board and the management periodically review the findings and recommendations of the auditors and take necessary corrective actions wherever necessary. The Board recognises the work of the auditors as an independent check on the information received from the management on the operations and performance of the Company.

INTERNAL CONTROLS

The Company maintains a system of internal controls designed to provide reasonable assurance regarding the achievement of objectives in following categories:

- Effectiveness and efficiency of operations;
- Adequacy of safeguards for assets;
- Reliability of financial controls; and
- Compliance with applicable laws and regulations.

The integrity and reliability of the internal control systems are achieved through clear policies and procedures, process automation, careful selection, training and development of employees and an organization structure that segregates responsibilities.

An effective internal control system has inherent limitations no matter how well designed, and therefore, may mitigate but cannot eliminate risks. In addition, there are areas of the Group's business where it is necessary to take risks to achieve a satisfactory return for shareholders, such as investment in development of new products or acquisition of businesses. In these cases the Company applies its expertise for prudent risk management rather than risk elimination.

Internal Audit at Dr. Reddy's is an independent, objective and assurance function responsible for evaluating and improving the effectiveness of risk management, control, and governance processes. The function prepares annual audit plans based on risk assessment and conducts extensive reviews covering financial, operational and compliance controls and risk mitigation. Areas requiring specialized knowledge are reviewed in partnership with external experts. Improvement opportunities identified during reviews are communicated to the management on an ongoing basis.

The Audit Committee monitors performance of internal Audit on a periodic basis through review of the audit plans, audit findings & promptness of issue resolution through follow ups.

STATUTORY AND U.S.GAAP AUDITS

For the financial year 2005-06, BSR & Co. audited the financial statements prepared under the Indian GAAP. The Company had also appointed KPMG as independent auditors for the purpose of issuing opinion on the financial statements prepared under the U.S.GAAP.

While auditing the operations of the Company, the external auditors recorded their observations and findings with the management. These were then discussed by the management, Audit Committee members and the auditors at Audit Committee meetings. Corrective actions suggested by the auditors and the Audit Committee were implemented or taken up for implementation by the management.

The independent auditors render an opinion regarding the fair presentation in the financial statements of the Company's financial condition and operating results. Their audit was made in accordance with generally accepted auditing standards and included a review of the internal controls to the extent, considered necessary to determine the audit procedures required to support their opinion.

AUDITORS' FEES

During the year, the Company paid Rs.6.55 million to the statutory auditors of the Company BSR & Co. as auditors' remuneration.

The Company also paid Rs.1.45 million to the statutory auditors of the Company BSR & Co. as non-audit fees.

INFORMATION TO STAKEHOLDERS

DISSEMINATION OF INFORMATION

The Company has established systems and procedures to disseminate, in a planned way, relevant information to its stakeholders, including shareholders, analysts, suppliers, customers, employees and the society at large.

Audit Committee Chairman reviews the earnings press releases, SEC filings and annual reports of the Company.

TABLE 13 Details of communication made during the financial year 2005-06.

MEANS OF COMMUNICATION	NOS.
Press releases / statements	22
Earnings calls	4
Publication of results	4
Analysts meet	1

The primary source of information regarding the operations of the Company is the corporate website of the Company www.drreddys.com

All official news releases and presentations made to institutional investors and analysts are posted on the Company's website. An analysis of the various means of dissemination of information in the year under review is produced in **Table 13**.

All communications referred above are available on Company's website www.drreddys.com for reference of the stakeholders.

The quarterly results of the Company are published in widely circulated national newspapers such as The Economic Times, Business Line, The Hindu and The Times of India and the local daily Andhra Bhoomi. Also the same is disseminated internationally through Business Wire.

In addition to the corporate website, the Company maintains various portals such as www.vikreta2drl.com, www.customer2drl.com, www.livizi.com, www.housecallsindia.com, www.drlintouch.com, which have proved to be effective tools for information dissemination and have been widely appreciated.

INFORMATION TO SHAREHOLDERS

Re-appointment of Director

MR. P N DEVARAJAN

INDEPENDENT DIRECTOR

Mr. P N Devarajan joined the Company as Director in 2000. He was Director in Cheminor Drugs Limited, a Company that merged with Dr. Reddy's in 2000. He is currently member of the Planning Board of Madhya Pradesh, Chairman of Research at the Council of National Environment Engineering Research Institute, member of the Assessment Committee of Council of Scientific and Industrial Research and member of the Research Council of National Chemical Laboratory. He was also a Director of the Bank of

Baroda, member of the Central Board of Directors of the Reserve Bank of India and Group President and consultant of Reliance Industries Limited. He is also a Director on the Board of Kothari Sugars and Chemicals Limited. He was not holding any equity share in the Company as on March 31, 2006.

Dr. V Mohan the other retiring Director has expressed his intention not to opt for re-appointment in the ensuing Annual General Meeting of the Company.

COMPLIANCE REPORT ON NYSE CORPORATE GOVERNANCE GUIDELINES

Pursuant to Section 303A.11 of the NYSE Listed Companies Manual, Dr. Reddy's which is a foreign private issuer as defined by Securities and Exchange Commission, must make its U.S. investors aware of the significant ways in which the corporate governance practices differ from those required of domestic companies under NYSE listing standards. A detailed analysis of the same has been posted on Dr. Reddy's website www.drreddys.com

COMPLIANCE REPORT ON NON-MANDATORY REQUIREMENTS UNDER CLAUSE 49

1. The Board

The Chairman of Dr. Reddy's is an executive Director and he maintains the Chairman's office at the Company's expenses.

Dr. V Mohan, independent Director completed 10 years as Director on the Board of the Company. He has expressed his intention not to opt for re-appointment in the ensuing Annual General Meeting of the Company. The tenure of all other independent Directors on the Board is less than 9 years.

2. Remuneration Committee

The Board of Directors has constituted a Compensation Committee, which is composed of independent Directors. This Committee also discharges the duties and responsibilities of Remuneration Committee as contemplated under non-mandatory requirements of Clause 49. The details of the Compensation Committee and its powers have already been discussed in this section of the Annual Report.

3. Shareholders rights

The Company did not send half yearly results to each household of the shareholders in the financial year 2005-06. However the Company displays its quarterly and half yearly results on its website www.drreddys.com and published in widely circulated news papers.

4. Audit Qualifications

The auditors have not qualified the financial statements of the Company any time.

5. Training of Board members

The Company believes that for the able discharge of the responsibilities of the Board it is essential that Board be continuously empowered with the knowledge of the latest developments in the Company's businesses and the external environment affecting the industry as a whole. In pursuit of achieving this goal, during the year, the Directors were given presentations on global business environment, all business areas of the Company including business strategy, risks and opportunities. The Directors visited various manufacturing and research locations of the Company. The Company also sponsored some of its Directors for attending seminars.

6. Mechanism for evaluating independent Board members

During the year, the independent Directors of the Company discussed the decisions taken by the Board and various Committees during last three financial years and the time allocated by the Directors towards the Company. A lead Director amongst the independent Directors has been identified to provide structured feedback to the Board to encourage healthy discussions and openness amongst the members of the Board.

7. Whistle Blower Policy

The Company has framed and implemented a Whistle Blower policy in 2005, details of which have been discussed earlier in this section.

ADDITIONAL SHAREHOLDER INFORMATION

The detailed "additional shareholder information" section is part of this Annual Report.

EXHIBIT 1

DECLARATION OF THE CHIEF EXECUTIVE OFFICER ON COMPLIANCE WITH CODE OF BUSINESS CONDUCT AND ETHICS

Dr. Reddy's Laboratories Limited has adopted a Code of Business Conduct and Ethics ("the Code"), which applies to all employees and Directors of the Company, its subsidiaries and affiliates. Under the code, it is the responsibility of all employees and Directors to familiarize themselves with the Code and comply with its standards.

I hereby certify that the Board members and senior management personnel of Dr. Reddy's have affirmed compliance with the Code for the financial year 2005-06.

Sd.

G V PRASAD

VICE CHAIRMAN &

CHIEF EXECUTIVE OFFICER

HYDERABAD

MAY 31, 2006

EXHIBIT 2

REPORT OF THE AUDIT COMMITTEE

TO THE SHAREHOLDERS OF

DR. REDDY'S LABORATORIES LIMITED

The Audit Committee of the Board of Directors comprises five Directors. Each member of the Committee is an independent Director as defined under Indian Laws and New York Stock Exchange Corporate Governance Guidelines. The Committee operates under a written charter adopted by the Board of Directors, and has been vested with all the powers necessary to effectively discharge its responsibilities.

Dr. Reddy's management has primary responsibility for the financial statements and reporting process including the systems of internal controls. During the year, the Committee discussed with the Company's internal auditors and statutory auditors the overall scope and plans for their respective audits. The Committee also discussed the results of their examination, their evaluations of the Company's internal controls, and the overall quality of the Company's financial reporting.

In fulfilling its oversight responsibilities, the Committee has reviewed and discussed the Company's audited financial statements with the management. BSR & Co., the Company's independent auditors for Indian GAAP financial statements and KPMG, Company's independent auditors for U.S.GAAP financial statements are responsible for expressing their opinion on the conformity of the Company's audited financial statements with Generally Accepted Accounting Principles.

Relying on the review and discussions with the management and the independent auditors, the Audit Committee believes that the Company's financial statements are fairly presented in conformity with Generally Accepted Accounting Principles in all material aspects.

During the year, the Committee devoted considerable time and efforts towards compliance with Section 404 of the U.S. Sarbanes-Oxley Act (SOX) of 2002. We are pleased to report that the Company became the first Indian manufacturing company to comply with Section 404 of the U.S. Sarbanes-Oxley Act (SOX), well in advance of the mandatory deadline of March 31, 2007.

The Audit Committee has recommended that the Board accept the audited financial statements prepared in accordance with Indian GAAP and U.S.GAAP as true and fair statements of the financial health of the Company. Further, the Committee has recommended that for the year 2005-06 the Board re-appoint BSR & Co. and KPMG as statutory independent auditors for Indian GAAP and U.S.GAAP respectively.

The Company's Code of Business Conduct and Ethics has the mechanism whereby no personnel intending to make a compliant relating to Securities and Financial reporting shall be denied access to the Audit Committee.

Sd.

DR. OMKAR GOSWAMI

CHAIRMAN, AUDIT COMMITTEE

HYDERABAD

MAY 31, 2006

EXHIBIT 3

REPORT OF THE COMPENSATION COMMITTEE

TO THE SHAREHOLDERS OF DR. REDDY'S LABORATORIES LIMITED

The Compensation Committee of the Board of Directors comprises five Directors. Each member of the Committee is an independent Director as defined under Indian Laws and New York Stock Exchange Corporate Governance Guidelines. The Committee operates under a written Charter adopted by the Board of Directors. The Committee has been vested with all the powers necessary to effectively discharge its responsibilities.

The Committee believes that its principal objective is to reward executive performance that will lead to long-term enhancement of shareholder value. The Compensation policies of the Company are vital elements in the Company's drive to identify, develop and motivate high-potential leaders to create and sustain outstanding performance. The Compensation Committee is responsible for overseeing performance evaluation, approving compensation levels for all senior executives and oversight of the administration of the Employee Stock Option Scheme.

During the year, the Committee discussed the Company's performance appraisal systems, the outcome of the performance assessment programs and compensation policies for national and international employees. A particular point of focus was the alignment of HR costs with business performance. Accordingly, the Committee advised the introduction of a new variable pay plan and an outcome – focussed balanced scorecard approach to annual goal setting across the Company.

As on March 31, 2006, the Company has 482,234 outstanding stock options, which amounts to 0.62% of total equity capital. The stock options have been granted to 254 employees of the Company and its subsidiaries under Dr. Reddy's Employee Stock Options Scheme, 2002. Out of the total 482,234 stock options, 117,250 stock options are exercisable at Fair Market Value and 364,984 stock options are exercisable at Par Value i.e. Rs.5.

Sd.

RAVI BHOOTHALINGAM
CHAIRMAN, COMPENSATION COMMITTEE

HYDERABAD
MAY 31, 2006

CERTIFICATE OF COMPLIANCE

TO THE MEMBERS OF DR. REDDY'S LABORATORIES LIMITED

We have examined the compliance of conditions of Corporate Governance by Dr. Reddy's Laboratories Limited ("the Company"), for the year ended on March 31, 2006, as stipulated in Clause 49 of the Listing Agreement of the said Company with the Bombay Stock Exchange and the National Stock Exchange. The compliance of conditions of Corporate Governance is the responsibility of the management. Our examination was limited to procedures and implementation thereof, adopted by the Company for ensuring the compliance of the conditions of the Corporate Governance. It is neither an audit nor an expression of opinion on the financial statements of the Company.

In our opinion and to the best of our information and according to the explanations given to us, we certify that the Company has complied with the conditions of Corporate Governance as stipulated in the above mentioned listing agreement.

We further state that such compliance is neither an assurance as to the future viability of the Company nor the efficiency or effectiveness with which the management has conducted the affairs of the Company.

for BSR & CO.
CHARTERED ACCOUNTANTS
SANJAY AGGARWAL
PARTNER

HYDERABAD
MAY 31, 2006

additional shareholders' information

CONTACT INFORMATION

REGISTERED AND CORPORATE OFFICE

DR. REDDY'S LABORATORIES LIMITED
7-1-27, Ameerpet, Hyderabad 500 016
Andhra Pradesh, India
T +91-40-2373 1946
F +91-40-2373 1955
W http://www.drreddys.com

REPRESENTING OFFICERS

Correspondence to the following officers may be addressed at the registered and corporate office of the Company.

CHIEF COMPLIANCE OFFICER

V S VASUDEVAN
PRESIDENT & CHIEF FINANCIAL OFFICER
T +91-40-2373 1946
F +91-40-2373 1955
E vasudevan@drreddys.com

COMPLIANCE OFFICER

V VISWANATH
COMPANY SECRETARY
T +91-40-23734504
F +91-40-23731955
E viswanathv@drreddys.com

ADR INVESTORS / INSTITUTIONAL INVESTORS / FINANCIAL ANALYSTS

NIKHIL SHAH
INVESTOR RELATIONS
T +91-40-6651 1532
F +91-40-2373 1955
E nikhilshah@drreddys.com

MEDIA

M MYTHILI
CORPORATE COMMUNICATIONS
T +91-40-6651 1620
F +91-40-6651 1621
E mythilim@drreddys.com

INDIAN RETAIL INVESTORS

GIRISH TEKCHANDANI
ASSISTANT COMPANY SECRETARY
T +91-40-2374 5274
F +91-40-2373 1955
E girisht@drreddys.com

EVENTS FOR FINANCIAL YEAR 2005-06

ANNUAL GENERAL MEETING

DATE	Friday, July 28, 2006
TIME	11.30 AM
VENUE	Grand Ball Room Hotel Taj Krishna Road No. 1, Banjara Hills Hyderabad 500 034
LAST DATE FOR RECEIPT OF PROXY FORMS	July 26, 2006 before 11.30 AM

FINANCIAL CALENDAR

The tentative calendar for declaration of financial results in financial year 2006-07 is as follows:

For the quarter ending June 30, 2006	Last week of July, 2006
For the quarter and half year ending September 30, 2006	Last week of October, 2006
For the quarter and nine months ending December 31, 2006	Last week of January, 2007
For the year ending March 31, 2007	Last week of May, 2007
AGM for the year ending March 31, 2007	Second fortnight of July, 2007

DIVIDEND

The Board of Directors of the Company has proposed a dividend of Rs.5 on equity shares of Rs.5 each. The dividend will be paid on or after August 3, 2006, if approved by the shareholders at the Annual General Meeting scheduled on July 28, 2006.

BOOK CLOSURE DATE

The dates of book closure are from July 11, 2006 to July 14, 2006 (both days inclusive) for the purpose of payment of dividend.

CIN NUMBER

The Corporate Identity Number ("CIN") of the Company, as allotted by Ministry of Company Affairs is **L8519AP1984PLC004507.**

DEPOSITORIES

Overseas depository of ADRs

J P Morgan Chase Bank, N.A.
P.O. Box 43013, Providence, RI 02940-3013
T (781) 5754325
E shareholder@adr.com

LISTING ON STOCK EXCHANGES AND STOCK CODES

EQUITY SHARES	STOCK CODES
The Bombay Stock Exchange Limited ("BSE")	500124
National Stock Exchange of India Limited ("NSE")	DRREDDY
AMERICAN DEPOSITORY RECEIPTS ("ADR")	
New York Stock Exchange Inc. ("NYSE")	RDY

Notes:

1. Listing fees for the year 2006-07 has been paid to the Indian Stock Exchanges.

2. Listing fees to NYSE for listing of ADRs has been paid for the calendar year 2006.

3. Shares are also traded at other stock exchanges as permitted securities.

4. The Stock Code on Reuters is REDY.BO and on Bloomberg is DRRD@IN.

INTERNATIONAL SECURITIES IDENTIFICATION NUMBER ("ISIN")

ISIN is a unique identification number of traded scrip. This number has to be quoted in each transaction relating to the dematerialised equity shares of the Company. The ISIN number of the equity shares of the Company is **INE089A01023.**

CUSIP NUMBER FOR ADRS

The Committee on Uniform Security Identification Procedures ("CUSIP") of the American Bankers Association has developed a numbering system for securities. A CUSIP number uniquely identifies a security and its issuer and this is recognised globally by organisations adhering to standards issued by the International Securities Organization ("ISO"). The Company's ADRs carry the CUSIP number **256135203.**

Indian custodian of ADRs

ICICI Limited
ICICI Towers, Bandra-Kurla Complex,
Mumbai 400 051, Maharashtra, India
T +91-22-26531414
F +91-22-26531122

Registrar for Indian shares (Common agency for demat and physical shares)

Bigshare Services Private Limited
G-10 Left Wing, Amrutha Ville, Opp. Yashodha Hospital, Raj Bhavan Road, Hyderabad 500 082
T +91-40-23374967
F +91-40-23370295
E hyd2_bigshare@yahoo.com
Contact Person–Mr. G S Dharma Veer

EQUITY HISTORY OF THE COMPANY

Table 1 gives the equity history of the Company from incorporation of the Company till March 31, 2006.

01 TABLE

Equity history of the Company

TILL MARCH 31, 2006

DATE	PARTICULARS	ISSUED	CANCELLED	CUMULATIVE
February 24, 1984	Issue to promoters	200	–	200
November 22, 1984	Issue to promoters	243,300	–	243,500
June 14, 1986	Issue to promoters	6,500	–	250,000
August 9, 1986	Issue to public	1,116,250	–	1,366,250
September 30, 1988	Forfeiture of 100 shares	–	100	1,366,150
August 9, 1989	Rights Issue	819,750	–	2,185,900
December 16, 1991	Bonus Issue	1,092,950	–	3,278,850
January 17, 1993	Bonus Issue	3,278,850	–	6,557,700
May 10, 1994	Bonus Issue	13,115,400	–	19,673,100
May 10, 1994	Issue to promoters	2,250,000	–	21,923,100
July 26, 1994	GDR underlying Equity Shares	4,301,076	–	26,224,176
September 29, 1995	SEFL shareholders on merger	263,062	–	26,487,238
January 30, 2001	CDL Shareholders On merger	5,142,942	–	31,630,180
January 30, 2001	Cancellation of shares held in CDL	–	41,400	31,588,780
April 11, 2001 & April 24, 2001	ADR underlying Equity Shares	6,612,500	–	38,201,280
July 9, 2001	GDR conversion into ADR	–	–	38,201,280
September 24, 2001	ARL Shareholders on merger	56,694	–	38,257,974
October 25, 2001	Sub division of equity shares	–	–	76,515,948
January 30, 2004	Allotment pursuant to exercise of Stock Options	3,001	–	76,518,949
April 29, 2005	Allotment pursuant to exercise of Stock Options	20,000	–	76,538,949
February 13, 2006	Allotment pursuant to exercise of Stock Options	68,048	–	76,606,997
March 24, 2006	Allotment pursuant to exercise of Stock Options	12,573	–	76,619,570
March 31, 2006	Allotment pursuant to exercise of Stock Options	75,000	–	76,694,570

DESCRIPTION OF VOTING RIGHTS

All shares issued by the Company carry equal voting rights.

PERSONS HOLDING MORE THAN 1% OF THE SHARES

Table 2 gives the names of the persons who hold more than 1 per cent shares of the Company as on March 31, 2006.

STOCK DATA

Table 3 gives the monthly high, low and the total number of shares/ADRs traded per month on the BSE, NSE and the NYSE during the financial year 2005-06.

Chart 1 gives the movement of the Company's share price on NSE vis-a-vis S&P CNX Nifty during the financial year 2005-06.

Chart 2 gives the movement of Dr. Reddy's ADR prices on NYSE vis-à-vis S&P ADR index during the financial year 2005-06 and **Chart 3** gives premium in per cent on ADR traded at NYSE compared to price quoted at NSE.

02 TABLE

Persons holding 1 per cent or more of the shares in the Company

AS ON MARCH 31, 2006

SR. NO.	NAME	NO. OF SHARES HELD[1]	% OF PAID UP CAPITAL
1	Dr. Reddy's Holdings Private Limited	18,893,245	24.64%
2	Life Insurance Corporation of India	5,156,011	6.74%
3	FID Funds (Mauritius) Limited	3,689,905	4.82%
4	HSBC Global Investment Funds	2,750,000	3.59%
5	JP Morgan Fleming Asset Management	2,186,573	2.86%

[1] Does not include ADR holdings

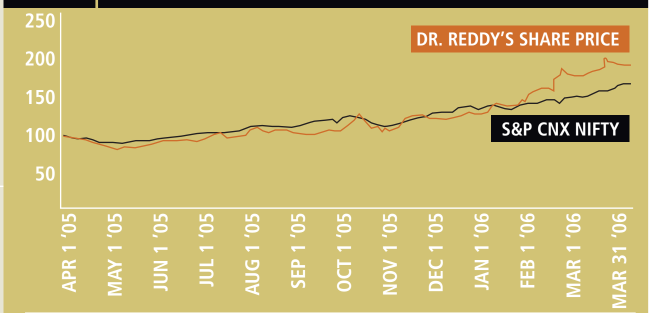
03 TABLE

High, low and number of shares traded per month on BSE, NSE and NYSE in the financial year 2005-06

MONTH	BSE			NSE			NYSE		
	HIGH (RS.)	LOW (RS.)	NO. OF SHARES	HIGH (RS.)	LOW (RS.)	NO. OF SHARES	HIGH (USD)	LOW (USD)	NO. OF ADRS
Apr-05	758.90	634.90	818,330	758.00	639.05	2,908,654	17.59	15.11	3,003,700
May-05	730.00	613.00	1,584,433	735.00	605.00	5,183,133	16.35	14.91	3,614,700
Jun-05	762.00	703.00	1,040,395	770.40	701.50	3,201,781	17.00	16.00	2,764,500
Jul-05	842.75	725.00	901,785	844.75	735.00	3,096,809	19.26	17.00	2,579,500
Aug-05	862.00	755.00	632,525	862.00	755.65	2,509,138	19.69	17.87	1,854,800
Sep-05	865.00	765.00	1,030,592	862.40	765.95	3,126,547	19.46	17.63	1,584,700
Oct-05	975.00	781.50	2,020,622	975.00	781.05	5,237,835	22.20	17.61	3,572,400
Nov-05	968.00	811.00	1,330,341	967.45	823.50	4,980,274	21.99	18.66	2,665,000
Dec-05	990.00	900.00	1,524,281	999.90	900.00	4,442,104	21.94	20.19	2,210,500
Jan-06	1,149.00	950.00	1,421,902	1145.00	941.55	4,357,252	25.70	21.79	3,829,600
Feb-06	1,408.00	1,125.00	2,692,693	1410.00	1082.40	8,721,624	30.41	25.83	8,313,200
Mar-06	1,513.00	1,290.00	2,825,379	1517.00	1250.20	6,770,508	33.34	28.27	7,042,800

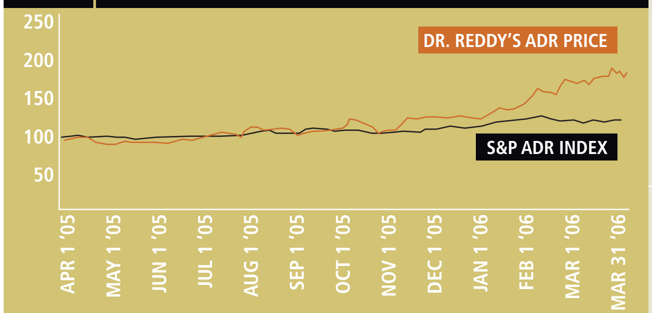
Note: 1 ADR = 1 Equity share

CHART 1 Movement of the Company's share price in 2005-06 on NSE



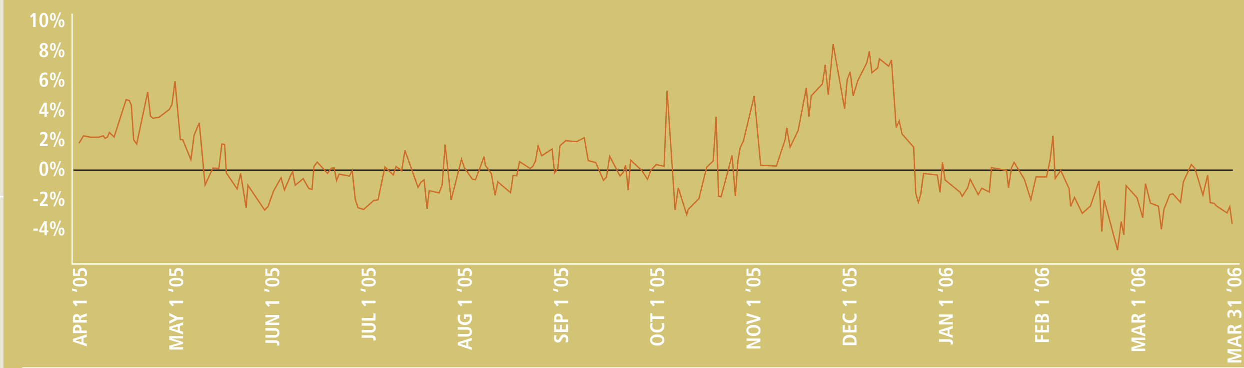
NOTES:
1. All values are indexed to 100 as on April 1, 2005.
2. S&P CNX Nifty is a diversified 50 stock index accounting for 23 sectors of the Indian corporates. It is owned and managed by India Index Services and Products Ltd. (IISL), which is a joint venture between NSE and CRISIL.

CHART 2 Movement of Company's ADR prices in financial year 2005-06 on NYSE



NOTES:
1. All values are indexed to 100 as on April 1, 2005
2. The S&P ADR Index is based on the non-U.S. stocks comprising the S&P Global 1200. For details of the methodology used to compute this index please visit www.adr.com

CHART 3 Premium (in per cent) on ADR traded at NYSE compared to share price quoted at NSE



NOTE:
1. Premium has been calculated on a daily basis using RBI reference exchange rate

04 TABLE

Distribution of shareholding on the basis of ownership

AS ON MARCH 31

	2006		2005		% CHANGE
	NO. OF SHARES	% OF TOTAL	NO. OF SHARES	% OF TOTAL	
PROMOTER'S HOLDING					
Individuals	2,232,542	2.91	2,243,594	2.93	-0.02
Companies	18,893,245	24.64	17,877,730	23.36	1.30
SUB TOTAL	**21,125,787**	**27.55**	**20,121,324**	**26.30**	**1.27**
Indian Financial Institutions	**5,536,530**	**7.22**	**7,971,748**	**10.42**	-3.20
Banks	**24,750**	**0.03**	**606,592**	**0.79**	-0.76
Mutual Funds	**1,679,347**	**2.19**	**1,583,330**	**2.07**	0.12
FOREIGN HOLDINGS					
Foreign Institutional Investors	21,829,357	28.46	12,282,463	16.05	12.41
Non Resident Indians	1,711,228	2.23	1,911,826	2.50	-0.27
American Depository Receipts	15,441,327	20.13	20,271,793	26.49	-6.36
Overseas Corporate Bodies	1,000	0.00	1,245	0.00	0.00
SUB TOTAL	**38,982,912**	**50.82**	**34,467,327**	**45.04**	**5.79**
Indian Public and Corporate	**9,345,244**	**12.19**	**11,768,628**	**15.38**	-3.19
TOTAL	**76,694,570**	**100.00**	**76,518,949**	**100.00**	

05 TABLE

Distribution of shareholding according to shareholder class

AS ON MARCH 31, 2006

SHARES HELD	NO. OF SHAREHOLDERS	% OF SHAREHOLDERS	NO. OF SHARES HELD	% OF SHARE HOLDING
1–5,000	48,606	95.54	4,507,642	5.88
5,001–10,000	1,155	2.27	1,714,580	2.24
10,001–20,000	609	1.20	1,753,949	2.29
20,001–30,000	180	0.35	900,430	1.17
30,001– 40,000	93	0.18	633,573	0.83
40,001–50,000	51	0.10	461,959	0.60
50,001–100,000	67	0.13	921,333	1.20
100,001 and above	116	0.23	50,436,027	65.76
TOTAL, EXCLUDING ADRS	**50,877**	**100.00**	**61,329,493**	**79.97**
Equity shares underlying ADRs(1)	1	0.00	15,365,077	20.03
TOTAL	**50,878**	**100.00**	**76,694,570**	**100.00**

(1) *Held by beneficial owners outside India*

SHAREHOLDING PATTERN AS ON MARCH 31, 2006

Table 4 and **Table 5** give the data on shareholding classified on the basis of ownership and shareholder class respectively.

DIVIDEND HISTORY

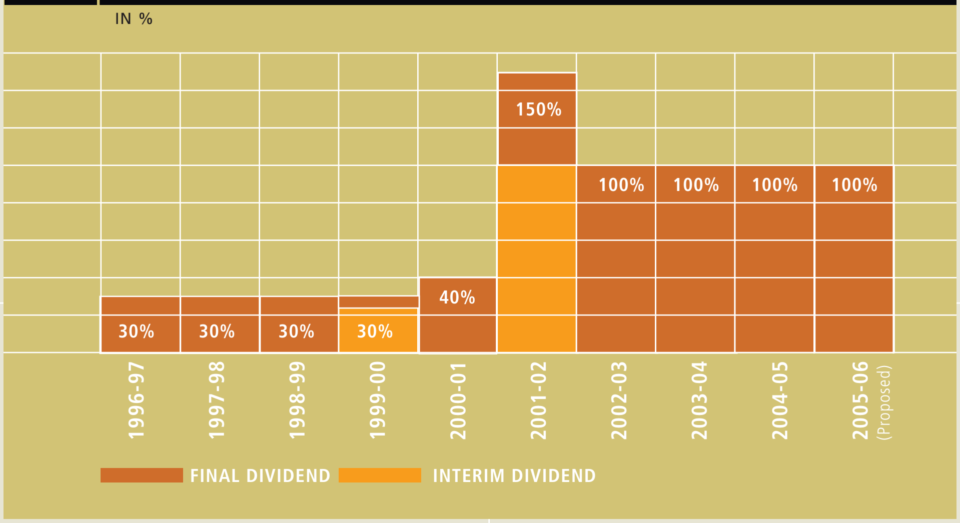
Chart 4 gives the dividend history of the Company from 1996-97.

The dividend proposed for declaration by shareholders for the financial year 2005-06 is Rs.5 per share of Rs.5 face value, which is 100%.

NOMINATION FACILITY

Shareholders holding physical shares may, if they so want, send their nominations in prescribed Form 2B of the Companies (Central Government's) General Rules and Forms, 1956 to the Registrars & Transfer Agents of the Company. Those

CHART 4 Dividend History of the Company



holding shares in dematerialised form may contact their respective Depository Participant (DP) to avail the nomination facility.

SHARE TRANSFER SYSTEM

All services relating to share transfers / transmissions and information may be addressed to:
M/s Bigshare Services Private Limited
G-10 Left Wing, Amrutha Ville, Opp. Yashodha Hospital, Raj Bhavan Road, Hyderabad 500 082
T +91-40-23374967
F +91-40-23370295
E hyd2_bigshare@yahoo.com
Contact Person–Mr. Dharma Veer, Branch Manager

The Company periodically audits the operations of Share Transfer Agent. The number of shares transferred / transmitted in physical form during the last two financial years is given in **Table 6**.

DEMATERIALISATION OF SHARES

The Company's scrip forms part of the compulsory dematerialisation segment for all investors with effect from February 15, 1999. To facilitate easy access of dematerialised system to the investors, the Company has signed up with both the depositories, namely, National Securities Depository Limited (NSDL) and Central Depository Services (India) Limited (CDSL), and has established connectivity with the depositories through our Registrars – Bigshare Services Private Limited.

Chart 5 gives the break up of dematerialized shares and shares in certificate form as on March 31, 2006 as compared with that of March 31, 2005.

Dematerialisation of shares is done through Bigshare Services Private Limited and on an average the dematerialisation process is completed within 10 days from the date of receipt of a valid dematerialisation request along with the relevant documents.

SECRETARIAL AUDIT

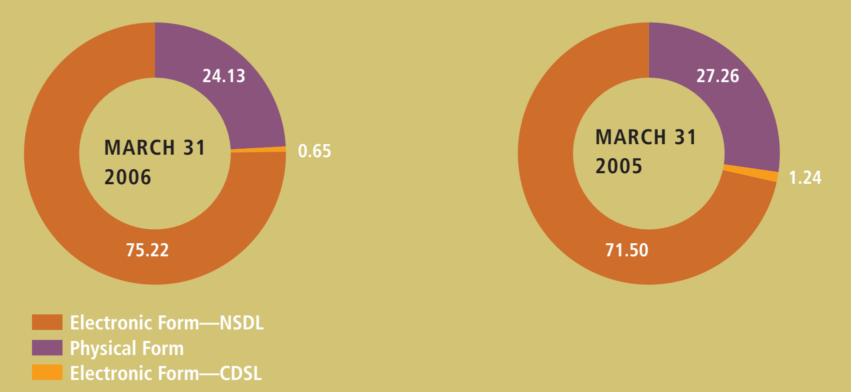
Each of the quarter in the financial year 2005-06, a qualified practicing Company Secretary carried out secretarial audits to reconcile the total admitted capital with National Securities Depository Limited (NSDL) and Central Depository Services (India) Limited

06 TABLE

Shares transferred / transmitted in physical form

	2005-06	2004-05
Number of transfers / transmissions	223	251
Number of shares	31,213	73,016

CHART 5 Break up of dematerialized shares and shares in certificate form as on March 31, 2006 and March 31, 2005



07 TABLE

Shareholder queries and requests received and replied to in 2005-06

SL. NO.	NATURE OF LETTERS	OPENING BALANCE	RECEIVED	REPLIED	CLOSING BALANCE[1]
1	Change of address	–	421	421	–
2	Revalidation and issue of duplicate dividend warrants	40	646	614	72
3	Sub-division of shares	32	763	795	–
4	Share transfers	10	282	285	7
5	Transmission of shares	–	29	29	–
6	Split of shares	–	11	11	–
7	Stop transfer	–	26	26	–
8	Change of bank mandate	–	55	55	–
9	Dematerialization of Shares	13	1,509	1,516	6
10	Rematerialization of Shares	–	7	7	–
11	Issue of duplicate share certificates of Dr. Reddy's	4	32	33	3
12	Issue of duplicate share certificates of ARL/SEFL/CDL	3	57	60	–
13	Letters and emails received from Shareholders	7	411	395	23
14	Complaints received from Stock Exchanges/SEBI etc.	1	19	20	–

[1] *The Company has resolved all the shareholders' complaints as on March 31, 2006. The above table does not include those shareholders' complaints, which are pending in various courts.*

(CDSL) and total issued and listed capital. The audit reports confirm that the total issued/ paid up capital is in agreement with the total number of shares in physical form and the total number of dematerialized shares held with NSDL and CDSL.

OUTSTANDING ADR WARRANTS AND IMPACT ON EQUITY SHARES

The Company's ADRs are traded in the U.S. on New York Stock Exchange Inc. (NYSE) under the ticker symbol "RDY". Each ADR is presented by one equity share. As on March 31, 2006, there were approximately 12,550 record holders of ADRs evidencing 15,365,077 ADRs.

TABLE 08 Last three Annual General Meetings

YEAR	DATE AND TIME	LOCATION	SPECIAL RESOLUTION(S) PASSED
2002-03	August 25, 2003 at 11.30 am	Hotel Viceroy, Tank Bund Road, Hyderabad – 500 080	• De-listing of equity shares from four stock exchanges
2003-04	July 28, 2004 at 11.30 am	Hotel Viceroy, Tank Bund Road, Hyderabad – 500 080	• Approval to the Employee Stock Option Scheme • Amendment in the Employee Stock Option Scheme Amendment in Articles of Association of the Company
2004-05	July 27, 2005 At 11.30 am	Hotel Viceroy, Tank Bund Road, Hyderabad – 500 080	• Amendment in Dr. Reddy's Laboratories Limited Stock Options Scheme, 2002 • Approval to the ADR linked Employee Stock Option Scheme

QUERIES AND REQUESTS RECEIVED FROM SHAREHOLDERS IN 2005-06

Table 7 gives details on all types of shareholder queries received and replied to during 2005-06. The pending queries and requests were either received during the last week of March 2006 or were pending due to non-receipt of information / documents from the respective shareholders.

During the year under review, the Company obtained the approval of the members, through postal ballot on certain matters on September 1, 2005 and March 6, 2006. Some of the resolutions were passed as special resolution. The details of postal ballot, resolutions and voting pattern are given in **Table 9**.

The Board of Directors of the Company appointed Mr. B Satya Reddy as scrutinizer for conducting postal ballot in fair and transparent manner. The printed postal ballot forms and resolutions with explanatory statement were dispatched under certificate of posting to all shareholders alongwith the pre-paid envelop and they were given 30 days to submit their mandate to the scrutinizer. Mr. B Satya Reddy scrutinized the responses and submitted his report to the Chairman of the Company. The results were informed to Stock Exchanges and posted on the Company's website.

There is no proposal to conduct postal ballot for any matter in ensuing annual general meeting.

TABLE 09 Details of the resolution passed through postal ballot in 2005-06

SR. NO.	RESOLUTION	ORDINARY /SPECIAL	DATE OF PASSING	RESOLUTION PASSED BY(%)
1	Disposal of manufacturing facility of the Company at Goa under Section 293(1)(a)	Ordinary	September 1, 2005	77.38%
2	Borrowings in excess of the Board powers under Section 293(1)(d)	Ordinary	March 6, 2006	98.88%
3	Creation of charges Section 293(1)(a)	Ordinary	March 6, 2006	97.91%
4	Investments under Section 372A	Special	March 6, 2006	99.01%
5	Issue of securities under Section 81	Special	March 6, 2006	98.40%

DATES AND VENUE OF LAST THREE ANNUAL GENERAL MEETINGS

Table 8 gives the date, time, location and business transacted at last three Annual General Meetings.

All special resolutions in the Annual General Meetings held in 2003, 2004 and 2005 were passed through show of hands. An ordinary resolution relating to disposal of Company's Formulations factory (Formulations – III) situated at Pondicherry was passed by postal ballot in 2003. There was no other occasion of postal ballot in these Annual General Meetings.

DISCLOSURE ON LEGAL PROCEEDINGS PERTAINING TO SHARES

There are six pending cases relating to disputes over title of the shares, in which Company has been made a party. These cases however are not material in nature.

UNCLAIMED DIVIDENDS

Pursuant to section 205A of the Companies Act, 1956, unclaimed dividends up to and including for the financial year 1997-98 have been transferred to the general revenue account of the Central Government / Investor Education and Protection Fund.

The dividends for the following years, which remain unclaimed for seven years will be transferred to Investor Education and Protection Fund established by the Central Government under Section 205C of the Companies Act, 1956. **Table 10** gives the transfer dates in this regard. Shareholders who have not claimed these dividends are, therefore, requested to do so before they are statutorily transferred to the Investor Education and Protection Fund. Shareholders who have not encashed their dividend warrants relating to the dividends specified in Table 10 are requested to immediately approach M/s Bigshare Services Private Limited, Hyderabad for the issue of duplicate warrants/ demand drafts in lieu of the dividend warrants.

TABLE 10 Dates of transfer of unclaimed dividend

FINANCIAL YEAR	TYPE OF DIVIDEND	DATE OF DECLARATION	AMOUNT OUTSTANDING AS ON MARCH 31, 2006	DUE FOR TRANSFER ON
1998-1999	Final	24.09.1999	639,657	12.11.2006
1998-1999	Final (erstwhile Cheminor)	25.09.1999	408,464	13.11.2006
1999-2000	Interim	23.03.2000	541,253	11.05.2007
1999-2000	Final	29.09.2000	166,511	17.11.2007
1999-2000	Interim (erstwhile Cheminor)	23.03.2000	339,275	11.05.2007
1999-2000	Final (erstwhile Cheminor)	06.07.2000	111,772	24.08.2007
2000-2001	Final	24.09.2001	1,157,444	31.10.2008
2001-2002	Interim	31.10.2001	1,825,370	07.12.2008
2001-2002	Final	26.08.2002	1,166,598	02.10.2009
2002-2003	Final	25.08.2003	1,626,380	01.10.2010
2003-2004	Final	28.07.2004	2,117,810	03.09.2011
2004-2005	Final	27.07.2005	2,009,350	02.09.2012

NON-COMPLIANCE ON MATTERS RELATING TO CAPITAL MARKETS FOR LAST THREE YEARS

There has been no instance of non-compliance relating to capital markets for the last three years.

FINANCIAL RESULTS ON COMPANY'S WEBSITE

The quarterly, half yearly and annual results of the Company are displayed on its website www.drreddys.com. Presentations to analysts, as and when made, are immediately posted on the website for the benefit of the shareholders and public at large. Apart from the above, the Company also regularly provides relevant information to the stock exchanges as per the requirements of the listing agreements.

PLANT LOCATIONS (IN INDIA)

BULK DRUGS

Bulk Drugs – I
Plot No. 137,138 & 146, IDA Bollaram, Jinnaram Mandal, Medak Dist., A P 502 320

Bulk Drugs – II
Plot No.110&111, IDA Bollaram, Jinnaram Mandal, Medak Dist., A P 502 320

Bulk Drugs – III
Plot No.116, IDA Bollaram, Jinnaram Mandal, Medak Dist., A P 502 320

Bulk Drugs – IV
Plot No.9/A, Phase – III, IDA Jeedimetla, Ranga Reddy Dist., A P 500 055

Bulk Drugs – V
Peddadevulapally, Tripuraram Mandal, Nalgonda Dist., AP 508 207

Bulk Drugs – VI
IDA Pydibheemavaram, Ransthal Mandal, Srikakulam Dist., AP 532 409

Bulk Drugs – IX
IDA Pydibheemavaram, Ransthal Mandal, Srikakulam Dist., AP 532 409

FORMULATIONS

Formulation – I
IDA Bollaram, Jinnaram Mandal, Medak Dist., AP 502 320

Formulation – II
S Y No.42 Bachupally, Quthbullapur Mandal, Ranga Reddy Dist., AP 500 123

Formulation – III
Ward-F, Block-4, Adavipolam, Yanam, Pondicherry 533 464

Formulation – V
Khol, Nalagarh,Solan, Nalagarh Road, Baddi 173205, Himachal Pradesh

GENERICS

Survey No.41 Bachupally, Quthbullapur Mandal, Ranga Reddy Dist., A P 500 043

BIOTECH

Survey No.47 Bachupally, Quthbullapur Mandal, Ranga Reddy Dist, A P 500 043

CUSTOM PHARMACEUTICALS SERVICES

Bollaram Road, Miyapur, Hyderabad, A P 500 050

CRITICAL CARE

Survey No.47 Bachupally, Quthbullapur Mandal, Ranga Reddy Dist., A P 500 043

DISCOVERY RESEARCH

Bollaram Road, Miyapur, Hyderabad, A P 500 050

PLANT LOCATIONS (OUTSIDE INDIA)

DR. REDDY'S LABORATORIES (UK) LIMITED
Riverview Road, Beverly, East Yorkshire, HU 17 Old, United Kingdom.

Dr. Reddy's Laboratories (EU) Limited
208-214, York Road, Battersea, London, Sw11 3sd, United Kingdom.

Kunshan Rotam Reddy Pharmaceutical Co. Limited
Huangpujiangzhonglu Kunshan Economic and Technological Development Zone, Jiangsu province, China.

Industrias Quimicas Falcon de Mexico S.A. de C.V.
Km 4.5 Carr. Fed. Cuernavaca-Cuautla, 62578 CIVAC, Jiutepec, Morelos, Mexico

INFORMATION ABOUT DIRECTORS PROPOSED FOR REAPPOINTMENT

The information is given in the Section on 'Corporate Governance'.

QUERIES AT ANNUAL GENERAL MEETING

Shareholders desiring any information with regard to the accounts are requested to write to the Company at an early date so as to enable the management to keep the information ready. The queries relating to operational and financial performance may be raised at the Annual General Meeting.

The Company provides the facility of Investor-Helpdesk at the Annual General Meeting. Shareholders may post their queries relating to shares, dividends etc., at this Investor-Helpdesk.

PROCEDURE FOR CONVENING EXTRA-ORDINARY GENERAL MEETING

The Extra Ordinary General Meeting of the Company may be called on by the requisition of the shareholders. The requisition shall set out the matters of consideration for which the meeting is to be called on, signed by the requisitionists, and deposited at the registered office of the Company.

Pursuant to the provisions of the Companies Act, 1956, the members entitled to the requisition of an Extra-Ordinary General Meeting with regard to any matter shall be those who hold not less than one-tenth of the paid-up capital of the Company as at the date of the deposit of the requisition and carry the right to vote in that matter.

PROCEDURE FOR NOMINATING DIRECTOR ON THE BOARD

Pursuant to Section 257 of the Companies Act, 1956, any member intending to propose a person for appointment on the Board of the Company shall, leave a notice in writing under his hand signifying candidature to the office of Director along with a deposit of five thousand rupees at the registered office of the Company, atleast fourteen days before the meeting. All nominations are considered by the Nomination Committee of the Board of Directors entirely consisting of independent Directors.

INFORMATION ON MEMORANDUM AND ARTICLES OF ASSOCIATION

The Memorandum and Articles of Association of the Company are available at the corporate website of the Company www.drreddys.com

CERTIFICATE FROM THE COMPANY SECRETARY

I, **V VISWANATH**, Company Secretary of Dr. Reddy's Laboratories Limited, hereby confirm that the Company has:

a. Maintained all the books of account and statutory registers prescribed under the Companies Act, 1956;

b. Filed all forms and returns and furnished all necessary particulars to the Registrar of Companies and/or Authorities as required under the Companies Act, 1956;

c. Conducted the Board Meetings and Annual General Meetings as per the Companies Act, 1956 and the minutes thereof were properly recorded in the minutes books;

d. Effected share transfers and despatched the certificates within the time limit prescribed by various authorities;

e. Not exceeded the borrowing powers;

f. Paid dividend to the shareholders within the time limit prescribed and has also transferred the unpaid dividend to the Investor Education and Protection Fund within the time limit; and

g. Complied with the regulations prescribed by the Stock Exchanges, SEBI and other Statutory Authorities and also the statutory requirements under the Companies Act, 1956 and other applicable statutes in force.

The certificate is given by the undersigned according to the best of his knowledge and belief, knowing fully well that on the faith and strength of what is stated above, the shareholders of the Company will place full reliance on it.

Sd.

V VISWANATH
COMPANY SECRETARY

HYDERABAD
MAY 31, 2006

five years at a glance

based on consolidated
U.S.GAAP financials

ALL FIGURES IN RS. MILLION EXCEPT EPS

YEAR ENDING MARCH 31	2006	2005	2004	2003	2002
INCOME STATEMENT DATA					
Product sales	24,077	19,126	20,081	18,070	16,409
Service Income	142	47	22	–	–
License fees	48	346	–	–	125
Other	–	–	–	–	89
Total revenues	**24,267**	**19,519**	**20,104**	**18,070**	**16,623**
Cost of revenues	12,417	9,386	9,337	7,848	6,869
Gross profit	**11,850**	**10,134**	**10,767**	**10,222**	**9,754**
as a % of revenues	49	52	54	57	59
OPERATING EXPENSES					
Selling, general and administrative expenses	8,029	6,774	6,543	5,103	3,674
Research and development expenses	2,153	2,803	1,992	1,412	742
Amortization expenses	420	350	383	419	488
Foreign exchange (gain)/loss	126	489	(282)	70	(209)
Other Operating (income) / expenses, net	(320)	6	83	–	–
TOTAL OPERATING EXPENSES	**10,408**	**10,422**	**8,718**	**7,004**	**4,695**
Operating income	**1,442**	**(289)**	**2,049**	**3,218**	**5,059**
as a % of revenues	6	(1)	10	18	30
Equity in loss of affiliate	(88)	(58)	(44)	(92)	(131)
Other (expense) / income, net	534	454	536	683	154
INCOME BEFORE INCOME TAX AND MINORITY INTEREST	**1,887**	**107**	**2,540**	**3,809**	**5,083**
Income tax benefit/(expense)	(258)	94	(69)	(398)	(154)
Minority interest	(0)	10	3	(7)	(15)
NET INCOME/(LOSS)	**1,629**	**211**	**2,474**	**3,404**	**4,914**
as a % of revenues	7	1	12	19	30
Net income/(loss) per equity share – basic	21.28	2.76	32.34	44.49	64.63
Net income/(loss) per equity share – diluted	21.24	2.76	32.32	44.49	64.53
Dividend declared per share of Rs.5 (Rs.)	5.00	5.00	5.00	5.00	7.50
BALANCE SHEET DATA					
Cash and cash equivalents	3,713	9,288	4,376	7,273	5,109
Working capital	1,345	10,771	11,103	12,024	9,519
Total assets	68,768	29,288	26,619	23,092	18,967
Total long-term debt, excluding current portion	20,937	25	31	41	47
Total stockholders' equity	22,272	20,953	21,039	18,832	15,457
ADDITIONAL DATA					
Net cash provided by / (used in)					
Operating activities	1,643	2,292	3,999	4,367	4,653
Investing activities	(34,524)	633	(6,506)	(1,955)	(1,533)
Financing activities	27,211	1,931	(376)	(153)	1,422
Effect of exchange rate changes on cash	95	55	(14)	(95)	89
Expenditure on property, plant and equipment	(1,873)	(1,749)	(2,416)	(1,516)	(1,090)

intangible accounting

EVA – Economic Value Added ®

AS AT MARCH 31 (IN RS. MILLION)

	2006	2005	2004	2003	2002
Shareholders Funds	22,272	20,953	21,039	18,832	15,457
Debt - LT	19	25	31	41	47
TOTAL CAPITAL EMPLOYED	**22,291**	**20,978**	**21,070**	**18,873**	**15,504**
Earnings before Interest & Tax - EBIT	2,186	173	2,555	3,944	5,095
Tax on EBIT*	362	2	205	398	423
NOPAT (A)	**1,823**	**171**	**2,350**	**3,546**	**4,672**
Cost of Debt	2.1%	2.3%	1.9%	1.9%	1.9%
Cost of Equity & Retained Earnings	13.7%	12.3%	10.8%	11.9%	12.8%
WEIGHTED AVERAGE COST OF CAPITAL	**13.7%**	**12.3%**	**10.8%**	**11.9%**	**12.7%**
CAPITAL CHARGES (B)	**3,052**	**2,571**	**2,267**	**2,238**	**1,973**
Economic Value added (a-b)	(1,228)	(2,400)	83	1,307	2,699

® EVA is a registered trademark of Stern Stewart & Co.

*Notes: **1.** The cost of equity is calculated by using the following formula: Return on risk-free investment + expected risk premium on equity investment adjusted for the beta variant for Dr. Reddy's in India **2.** 10-year G-Sec yield taken as the risk-free rate of investment (7.50%) **3.** Beta value of 0.72 used for calculation of cost of equity **4.** Taxes on EBIT calculated at the Effective Tax Rate (excluding deferred taxes) **5.** All the calculations are based on U.S.GAAP Consolidated Financials **6.** Long term debt of Rs.21.6 billion taken in March 2006 has been ignored for the workings.*

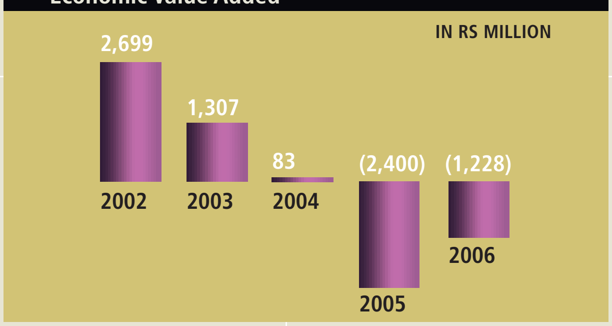
MVA – Market Value Added

AS AT MARCH 31 (IN RS. MILLION)

	2006	2005	2004	2003	2002
Current Market Value of Debt(1)	20,937	25	31	41	47
No of o/s shares (Mn)	77	77	77	77	77
SHARE PRICE DETAILS(2)					
High for the year	1,517	1,004	1,461	1,150	1,150
Low for the year	605	650	816	675	432
AVERAGE PRICE	**1,061**	**827**	**1,139**	**912**	**791**
Average Market Value of Equity	81,216	63,302	87,124	69,821	60,527
Market Value of Debt & Equity	102,153	63,327	87,156	69,862	60,574
Book Value of Debt & Equity	43,209	20,978	21,070	18,873	15,504
MARKET VALUE AT END OF YEAR	**58,944**	**42,349**	**66,085**	**50,989**	**45,070**
NET MVA ADDED DURING THE YEAR	**16,595**	**(23,736)**	**15,096**	**5,919**	**8,327**

(1) Book values, excluding current portion (2) Share prices in 2002 adjusted for stock split

Economic Value Added



Market Value Added

ratio analysis

based on consolidated U.S.GAAP financials

RATIOS (AS ON MARCH 31)	2006	2005	2004
PERFORMANCE RATIOS			
International revenue / total revenue %	65.9	65.7	64.5
Domestic revenue / total revenue %	34.1	34.3	35.5
Gross profit / total revenue %	48.8	51.9	53.6
– API %	28.2	27.8	33.1
– Formulations %	68.9	68.1	65.7
– Generics %	46.5	54.7	69.5
– Critical care & biotechnology %	65.9	66.5	49.6
Selling, General and Administrative expenses / total revenue %	33.1	34.7	32.5
R&D Expenses / total revenue %	8.9	14.4	9.9
– Drug Discovery / Total R&D %	37.8	31.0	36.6
Operating profit / total revenue %	5.9	(1.5)	10.2
Depreciation and amortization / total revenue %	6.5	6.7	5.6
Other income / total revenue %	2.2	2.3	2.7
Profit before tax / total revenue %	7.8	0.5	12.6
Profit after tax / total revenue %	6.7	1.1	12.3
BALANCE SHEET RATIOS			
Fixed Assets turnover ratio	3.0	2.9	3.6
Working Capital Turnover ratio (1)	4.9	4.6	4.2
Debtors turnover (Days)	63	68	67
Inventory turnover ratio (Days)	153	127	114
Capital expenditure / total revenue %	7.7	9.0	12.0
Total Debt / Equity	1.39	0.13	0.02
Cash and cash equivalents / total assets (2)	14.2	31.9	16.8
Investments securities (current + non-current) / total assets	1.6	4.5	15.4
GROWTH RATIOS			
Total revenue %	24.3	(2.9)	11.3
– API %	18.6	(9.0)	20.3
– Formulations %	26.9	4.2	9.4
– Generics %	13.4	(17.5)	1.2
– Critical care & biotechnology %	31.1	28.2	(4.0)
International revenue %	24.7	(1.2)	11.9
Selling, General and Administrative expenses %	18.5	3.5	28.2
R&D Expenses %	(23.2)	40.8	41.1
SHARE DATA			
Book Value (Rs. per Share)	290.4	273.8	275.0
Dividend %	100.00	100.00	100.00
Dividend per share (Rs)	5.00	5.00	5.00
Price / earnings, end of year	66.78	282.77	35.67
Basic earnings per share	21.3	2.8	32.3
Diluted earnings per share	21.2	2.8	32.3

2005-06 numbers include the results of the aquisitions in Germany for 28 days and in Mexico for 3 months. Hence, the ratios may not be comparable with those of earlier years.

Notes: (1) Working Capital is calculated as (Accounts Receivables; Inventories & Other Current Assets) Less (Trade Accounts Payables; Accrued Expenses & Other Current liabilities). (2) Cash & Cash Equivalents includes Restricted Cash (current and non-current portion)

directors' report

DEAR MEMBERS,

Your Directors are pleased to present the 22nd Annual Report for the year ended March 31, 2006. The financial highlights of the year are–

FINANCIAL HIGHLIGHTS

Table 1 gives the financial highlights of the Company in the financial year 2005-06 as compared to previous financial year on Indian GAAP standalone basis.

01 TABLE Financial highlights for the financial year ended March 31

IN RS. THOUSANDS

	2006	2005
Income	**21,365,711**	**16,290,422**
Gross profit	**3,750,983**	**1,368,152**
Depreciation	1,113,337	924,575
Profit before tax	2,637,646	443,578
Taxation	–	–
Current tax	(526,407)	(211,010)
Net profit for the year	**2,111,239**	**654,588**
Add: Profit and loss brought forward	1,815,464	1,663,130
TOTAL AVAILABLE FOR APPROPRIATION	**3,926,703**	**2,317,718**
APPROPRIATIONS		
Proposed dividend on equity shares	383,473	382,595
Tax on proposed dividend	53,782	53,659
Dividend of previous year	114	–
Transfer to general reserve	211,124	66,000
Balance carried forward	3,278,210	1,815,464

DIVIDEND

Your Directors are pleased to recommend a dividend of Rs.5 per equity share of Rs.5 for the financial year 2005-06. The dividend, if approved at the ensuing Annual General Meeting, will be paid to those shareholders whose name appear on the register of members of the Company as on July 10, 2006.

The dividend would be tax-free in the hands of the shareholders.

EMPLOYEE STOCK OPTION SCHEME

Pursuant to the provisions of Guideline 12 of the Securities and Exchange Board of India (Employee Stock Option Scheme and Employee Stock Purchase Scheme), Guidelines, 1999, as amended, the details of stock options as on March 31, 2006 under the Dr. Reddy's Employee Stock Option Scheme, 2002 are set out in the Annexure –1 to the Directors' Report.

SHARE CAPITAL

The paid up Share Capital of your Company increased by Rs.878,105 in the financial year ended March 31, 2006, due to exercise of Stock Options by the eligible employees under Dr. Reddy's Stock Option Scheme, 2002.

The Board of Directors have recommended issue of bonus shares to the shareholders in the ratio of 1:1 (one equity share for each equity share held) for all existing shares including American Depository Shares on the record date to be fixed by the Board.

CORPORATE GOVERNANCE AND ADDITIONAL INFORMATION TO SHAREHOLDERS

A detailed report on the Corporate Governance system and practices of the Company are given in a separate section in this annual report. Detailed information for the shareholders is given in Additional Shareholders' Information section.

MANAGEMENT DISCUSSION AND ANALYSIS

A detailed Management Discussion and Analysis is provided in the annual report.

SUBSIDIARY COMPANIES

The Company had 28 subsidiary companies as on March 31, 2006. The members may refer to the Statement under Section 212 of the Companies Act, 1956 and information on the financials of subsidiaries appended to the above statement under Section 212 of the Companies Act, 1956 in this Annual Report for further information on these subsidiaries.

The Ministry of Company Affairs vide its letter No. 47/55/2006 – CL-III dated May 4, 2006 granted approval to the Company for not attaching the financials of subsidiary companies to the financials of the Company for the financial year 2005-06.

The members, if they desire, may write to the Company Secretary at Dr. Reddy's Laboratories Ltd., 7-1-27, Ameerpet, Hyderabad – 500 016 to obtain a copy of the financials of the subsidiary companies.

DIRECTORS' RESPONSIBILITY STATEMENT

In terms of Section 217 (2AA) of the Companies Act, 1956, your Directors confirm as under:

1. In preparation of annual accounts, the applicable accounting standards have been followed along with proper explanation relating to material departures;
2. We have selected such accounting policies and applied them consistently and made judgments and estimates that are reasonable and prudent so as to give a true and fair view of the state of affairs of the Company at the end of the financial year 2005-06 and of profit of the Company for that period;
3. We have taken proper and sufficient care for the maintenance of adequate accounting records in accordance with the provisions of this Act for safeguarding the assets of the Company and for preventing and detecting fraud and other irregularities; and
4. We have prepared the annual accounts on an on going concern basis.

FIXED DEPOSITS

Your Company has not accepted any fixed deposits under Section 58A of the Companies Act, 1956 and hence no amount of principal or interest was outstanding as on the Balance Sheet date.

DIRECTORS

Mr. P N Devarajan retire by rotation at the ensuing Annual General Meeting scheduled on July 28, 2006. The other retiring Director Dr. V Mohan has expressed his intention not to opt for re-appointment at the ensuing Annual General Meeting. The brief profile of Mr. P N Devarajan is given in the Corporate Governance section for the reference of members.

It is proposed to re-appoint Dr. K Anji Reddy as Executive Chairman (Whole Time Director) of the Company for a further period of 5 years commencing July 13, 2006 and Mr. G V Prasad as Vice Chairman and Chief Executive Officer (Whole Time Director) of the Company for a further period of 5 years commencing on January 31, 2006. It is also proposed to revise the terms and conditions of appointment of Mr. Satish Reddy as Managing Director and Chief Operating Officer. The resolutions for the same have been included in the notice of the Annual General Meeting scheduled on July 28, 2006.

AUDITORS

The Statutory Auditors of the Company M/s BSR & Co., Chartered Accountants, retire at the ensuing Annual General Meeting and have confirmed their eligibility and willingness to accept office of Auditors, if reappointed. The Audit Committee and the Board of Directors recommend M/s BSR & Co. as Statutory Auditors of the Company for the financial year 2006-07.

COST AUDIT

Pursuant to Section 233B of the Companies Act, 1956, the Central Government has prescribed Cost Audit of the Company's Bulk Drugs Division and Formulation Division.

Subject to the approval of the Central Government, the Board has appointed M/s Sagar & Associates as Cost Auditors of the Company for the Financial Year 2005-06. The Cost Audit is under process and the Company will submit the Cost Auditors' report to the Central Government within the stipulated statutory period.

PARTICULARS OF EMPLOYEES

Pursuant to the provisions of Section 217(2A) of the Companies Act, 1956 read with Companies (Particulars of Employees) Rules, 1975 as amended, the names and other particulars of employees are set out in the Annexure–2 to the Directors' Report.

CONSERVATION OF ENERGY RESEARCH AND DEVELOPMENTS, TECHNOLOGY ABSORPTION, FOREIGN EXCHANGE EARNING AND OUTGO

The particulars as prescribed under Section 217(1)(e) of the Companies Act, 1956, read with the Companies (Disclosure of particulars in the report of Board of Directors) Rule, 1988 are set out in the Annexure–3 to the Directors' Report.

ACKNOWLEDGEMENT

Your Directors place on record their sincere appreciation for significant contribution made by the employees through their dedication, hard work and commitment and the trust reposed on us by the medical fraternity and the patients.

We also acknowledge the support and wise counsel extended to us by the analysts, bankers, government agencies, shareholders and investors at large. We look forward to having the same support in our endeavour to help people lead healthier lives.

for Dr. Reddy's Laboratories Limited

sd.

DR. K ANJI REDDY

CHAIRMAN

HYDERABAD

MAY 31, 2006

ANNEXURE TO THE DIRECTORS' REPORT

ANNEXURE 1

Pursuant to the provisions of Guideline 12 of the Securities and Exchange Board of India (Employee Stock Option Scheme and Employee Stock Purchase Scheme), Guidelines, 1999, as amended, the details of stock options as on March 31, 2006 under Dr. Reddy's Employee Stock Option Scheme 2002 are as under:

SL. NO.	DESCRIPTION	DETAILS
1	Options granted	2,081,128
2	The pricing formula	Dr. Reddy's Employee Stock Option Scheme, 2002 provides for the grant of options 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., Rs.5 per option). The fair market value of a share on each grant date falling under Category A above is defined as the weighted average closing price for 30 days prior to the grant, in the stock exchange where there is highest trading volume during that period.
3	Options vested and not exercised	56,018
4	Options exercised	178,622
5	The total number of shares arising as a result of exercise of option	178,622
6	Options lapsed	1,425,272
7	Variation of terms of options	1. Members of the Company approved the amendment in Dr. Reddy's Employee Stock Option Scheme, 2002 at the Annual General Meeting held on July 28, 2004. The amendment enabled the Company to grant Stock Options in two categories as discussed below. Before this amendment Dr. Reddy's Employee Stock Option Scheme, 2002 provided for grant of options at fair market value only. **Category A** 1,721,700 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** 573,778 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., Rs.5 per option). 2. Members of the Company further approved the amendment in Dr. Reddy's Employee Stock Option Scheme, 2002 at the Annual General Meeting held on July 27, 2005. The amendment enabled the Company to grant Stock Options in two categories as discussed below: **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., Rs.5 per option).
8	Money realised by exercise of options	893,110
9	Total number of options in force	482,234

10	Employee wise details as on March 31, 2006 of options granted to	
	(i) Senior managerial personnel	(see table below)

NAME	EXERCISE PRICE	NO. OF OPTIONS
Mr. V.S. Vasudevan	Fair Market Value	50,740
Mr. Abhijit Mukherjee	Par Value	7,400
Mr. Andrew Miller	Par Value	9,200
Mr. Arun Sawhney	Par Value	10,855
Mr. Ashwani Kumar Malhotra	Par Value	8,003
Mr. Jaspal Singh Bajwa	Par Value	13,000
Mr. Jeff Wasserstein	Par Value	10,000
Mr. K.B. Sankara Rao	Par Value	8,620
Mr. Mark Hartman	Fair Market Value	16,000
	Par Value	6,000
Dr. R. Rajagopalan	Par Value	8,430
Mr. Raghu Cidambi	Par Value	10,250
Mr. Saumen Chakraborty	Fair Market Value	5,000
	Par Value	8,825
Dr. Uday Saxena	Par Value	9,250

	(ii) Any other employee who receives a grant in any one year of option amounting to 5% or more of option granted during that year.	During the year Mr. V S Vasudevan, President of Chief Financial Officer of the Company was granted 25,000 Stock Options exercisable at Fair Market Value, which constitutes 10.03% of total options granted during the year.
	(iii) Identified employees who were granted option, during any one year, equal to or exceeding 1% of the issued capital (excluding outstanding warrants and conversions) of the Company at the time of grant;	Nil
11	Diluted Earnings Per Share (EPS) pursuant to issue of shares on exercise of option calculated in accordance with Accounting Standard (AS) 20 'Earnings Per Share'	27.44
12	The difference between the employee compensation cost computed under Intrinsic Value Method and the employee compensation cost that shall have been recognized if the Company had used the Fair Value Methods and its impact on profits and on EPS of the Company	The employee Compensation Cost on account of ESOP in the financial year 2005-06 based on Intrinsic Value Method is Rs.133.07 million. Had the Company used the Fair Value Method, the ESOP cost in the financial year 2005-06 would have been Rs.162.25 million. There would have been reduction in the Profit and EPS, on using fair value method of accounting by Rs.29.18 million and Rs.0.38 respectively.
13	Weighted-average exercise prices and weighted-average fair values of options for options whose exercise price either equals or exceeds or is less than the market price of the stock	Weighted average exercise price of the outstanding Fair Market Value options as on March 31, 2006 was Rs.878.85. Weighted average exercise price of the outstanding Fair Market Value options as on March 31, 2006 was Rs.5. The weighted average fair value of the outstanding options as on March 31, 2006 was Rs.747.69.

14	Description of the method and significant assumptions used during the year to estimate the fair values of options: (i) Risk-free interest rate, (ii) Expected life, (iii) Expected volatility, (iv) Expected dividends, and (v) The price of the underlying share in market at the time of option grant	The Company has opted Intrinsic Value Method for accounting of Compensation Cost arising out of ESOP. However for disclosures in para 12 above the following assumptions have been used: 5.7% - 7.5% 12 months to 78 months 23.4% to 36.9% 0.5% Rs.672 to Rs.1,349

ANNEXURE 2

Pursuant to the provisions of Section 217(2A) of the Companies Act, 1956 read with Companies (Particulars of Employees) Rules, 1975 as amended, the names and other particulars of employees are as under:

SL. NO.	NAME OF THE EMPLOYEE	AGE	DESIGNATION / NATURE OF DUTY	GROSS REMUNERATION
	EMPLOYED FOR THE FULL YEAR			
1	Dr. K. Anji Reddy	66	Executive Chairman	6,281,677
2	Mr. G. V. Prasad	45	Executive Vice Chairman and CEO	3,877,386
3	Mr. K. Satish Reddy	38	Managing Director and COO	3,863,838
4	Mr. V. S. Vasudevan	54	President and Chief Financial Officer	7,844,918
5	Mr. Abhijit Mukherjee	47	President	6,358,655
6	Mr. Arun Sawhney	50	President	9,053,022
7	Mr. Jaspal Singh Bajwa	54	President	8,763,583
8	Dr. R. Rajagopalan	56	President	5,627,265
9	Mr. K. B. Sankara Rao	52	Executive Vice President	5,527,308
10	Mr. Saumen Chakraborty	45	Executive Vice President	7,435,692
11	Mr. Ashwani Kumar Malhotra	50	Senior Vice President	5,645,643
12	Dr. N. R. Srinivas	46	Senior Vice President	4,460,719
13	Mr. S. Venkatraman	59	Senior Vice President	3,633,052
14	Mr. Vilas Dholye	56	Senior Vice President	4,315,606
15	Dr. Kashi Nath Singh	54	Senior Vice President	3,949,053
16	Mr. J. N. G. G. Shankar	47	Vice President	2,783,048
17	Mr. K. N. Reddy	52	Vice President	2,696,882
18	Mr. K. Ramesh	45	Vice President	2,579,795
19	Mr. K. S. R. Krishna Reddy	47	Vice President	2,671,600
20	Mr. M. S. Mohan	42	Vice President	3,626,703
21	Mr. Prabir Kumar Jha	39	Vice President	3,251,136
22	Dr. Ranjan Chakraborty	48	Vice President	3,030,488
23	Ms. Ritha Chandrachud	42	Vice President	2,950,396
24	Mr. Singhai Sunil Chand	50	Vice President	3,103,012
25	Mr. T. S. Rangan	41	Vice President	2,841,220
26	Mr. V. K. Chandrasekharan	53	Vice President	2,711,879
27	Mr. V. V. S. Murthy	50	Vice President	2,577,588
28	Mr. B. Madhusudan Rao	38	Vice President	3,306,883
29	Dr. R. Ezhil Arasan	47	Senior Director	2,967,802
	EMPLOYED FOR THE PART OF THE YEAR			
1	Mr. C. Raghuraman	46	Senior Vice President	259,014
2	Dr. Javed Iqbal	59	Distinguished Research Scientist	1,887,048
3	Mr. Chandan Kumar	48	Vice President	2,612,533
4	Mr. G. Subramanyam	51	Vice President	2,309,726
5	Dr. P. Sairam	56	Vice President	2,817,723
6	Mr. Sandeep Sahney	42	Executive Vice President	4,725,676
7	Dr. Ravi Pillai	45	Senior Director	1,434,780
8	Mr. K. Ganesh	43	Senior Director	944,685
9	Dr. Apurba Bhattacharya	53	Vice President	712,403

1. All the above employments are contractual.

2. Dr. K Anji Reddy, Mr. G V Prasad and Mr. Satish Reddy are relatives within the meaning of Section 6 of the Companies Act, 1956.

3. Dr. K Anji Reddy, Mr. G V Prasad and Mr. Satish Reddy are also eligible for commission on the net profits of the Company. The Commission has been included in the remuneration specified above.

	QUALIFICATION	EXPERIENCE IN YEARS	DATE OF COMMENCEMENT OF EMPLOYMENT	PARTICULARS OF LAST EMPLOYMENT
	B.Sc. (Tech.), Ph.D.	36	01.09.1986	Managing Director, Standard Organics Limited
	B.Sc., (Chem. Eng.), MS (Indl. Admn.)	22	30.06.1990	Promoter Director, Benzex Labs Private Limited
	B.Tech., M.S.	14	18.01.1993	Director, Globe Organics Limited
	B.Com., ACA	32	01.04.1986	Finance Head, Standard Equity Fund Limited
	B.Tech. (Chem.)	25	15.01.2003	President, Atul Limited
	B.Com., PGDBM	23	01.06.2001	Chief Executive, Max-GB Limited
	B.Sc., MBA	29	10.04.2003	Executive Director and COO, Marico Industries Limited
	M.Sc., Ph.D.	33	18.04.1994	Principal Research Scientist, Hoechst India Limited
	M.Pharma.	28	29.09.1986	Production Executive, Cipla Limited
	B.Sc.(H), MBA-IIM	22	02.07.2001	Vice President, Tecumsesh
	M.Pharma., PGD-IEM, PGD-CS	26	08.02.2001	Unit Head, Cipla Limited
	B.Pharma., Ph.D.	16	01.06.2001	Senior Research Investigator, Bristol Myers Squibbs Company
	M.Sc.	32	25.03.1987	GM-Tech, Uniloids Limited
	B.Tech. (Chem.)	27	18.12.2000	VP, Pidilite Industries Limited
	M.Sc., Ph.D.	33	08.08.2003	President - Alkem Laboratories Limited
	M.Pharma., MBA	26	28.02.1996	General Manager - John Wyeth (India) Limited
	M.Sc.	28	16.05.1994	Manager - Ranbaxy Laboraoties Limited
	B.E. (Mech.), MMS	22	25.01.2002	General Manager - Max India Limited
	B.Com.	21	05.11.1984	Resident Executive, Cheminor Drugs Limited
	M.Pharma.	18	01.03.2000	Asst Manager - Astra IDL Limited
	M.A., PGDM(XLRI)	14	29.11.2002	Regional Head HR - Mahindra British Telecom
	M.Sc., Ph.D.	23	08.08.1985	Research Associate, University of Massachusetts Medical Centre
	B.Sc., MMS	20	14.07.2003	Sr. Director - Fulford (India) Limited
	M.Pharma.	28	19.02.2001	General Manager - Ranbaxy Laboratories Limited
	MBA, MS(IS)	19	07.12.1999	Manager - Finance & IT - Zeneca Agrochemicals Limited
	B.Sc.	28	17.04.1992	Divisional Manager - Fyto Chem Formulations
	B.Com., ACA	26	23.08.1995	Manager Accounts - Coromandel Fertilizers Limited
	M.Sc., M.Phil.	13	09.07.1993	—
	MBBS, MD	19	27.09.2004	Vice President - USV Limited
	M.Tech., M.Sc.	22	22.03.2004	Vice President - Polaris Software
	M.Sc., Ph.D.	27	02.01.2003	Director, Regional Research Laboratory
	M.Sc.	25	07.12.1998	Deputy Manager - Darshal Limited
	B.A., ACA	27	09.07.2003	Director - Indian School of Business
	M.Sc., Ph.D.	27	19.12.1994	Manager - Cipla Limited
	MBA	20	04.04.2005	Eli Lilly & Co (I) Private Limited, Director – Sales & Marketing
	MS, Ph.D.	12	04.07.2005	Ranbaxy Research Laboratories (Associate Director)
	B.Com., ACA	14	14.10.2005	Philips Electronics (Country Treasurer)
	M.Sc., Ph.D.	23	30.12.2005	Texas A & M Kingsville (Associate Professor)

ANNEXURE 3

FORM A

Form for Disclosure of Particulars with respect to Conservation of Energy.

A. POWER AND FUEL CONSUMPTION

1. ELECTRICITY

(i) PURCHASED

	2005-06	2004-05
Unit	89,957,682	75,349,924
Total amount (Rs.)	306,829,107	273,605,462
Rate/unit (Rs.)	3.41	3.63

(ii) OWN GENERATION—THROUGH DIESEL GENERATOR SET

	2005-06	2004-05
Unit	2,010,367	6,736,259
Units per ltr. of diesel oil	3.54	3.42
Cost/unit (Rs.)	9.12	7.76

2. COAL (USED IN BOILER)

	2005-06	2004-05
Quantity (tonnes)	32,835	29,823
Total Cost (Rs.)	83,150,579	67,836,781
Average Rate (Rs.)	2,532	2,275

3. FURNACE OIL

	2005-06	2004-05
Quantity (K Lts.)	4,084	4,732
Total Cost (Rs.)	60,354,195	59,804,678
Cost/unit (Rs.)	14,780	12,638

B. CONSUMPTION PER UNIT OF PRODUCTION

The Company manufactures APIs and finished dosages in various forms and pack sizes. It is therefore impractical to apportion the consumption and cost of utilities to each unit.

FORM B

RESEARCH AND DEVELOPMENT (R & D)

1. Specific areas in which R & D carried out by the Company.

Our research and development activities can be classified into several categories, which run parallel to the activities in our principal areas of operations:

- Formulations, where our research and development activities are directed at the development of product formulations, process validation, bio-equivalency testing and other data needed to prepare a growing list of drugs that are equivalent to numerous brand name products for sale in the emerging markets.
- Active pharmaceutical ingredients and intermediates, where our research and development activities concentrate on development of chemical processes for the synthesis of active pharmaceutical ingredients for use in our generics and formulations segments and for sales in the emerging and developed markets to third parties.
- Generics, where our research and development activities are directed at the development of product formulations, process validation, bio-equivalency testing and other data needed to prepare a growing list of drugs that are equivalent to numerous brand name products whose patents and regulatory exclusivity periods have expired or are nearing expiration in the regulated markets of the United States and Europe.

  During fiscal 2004, we integrated the product development capabilities in our API, generics and formulations segments to increase our focus on productivity and product delivery, by combining technical excellence with process excellence. We also strengthened our technical, intellectual property and legal skills to enhance our new product development process. This will help us leverage our core technology strengths in chemistry and formulation development with legal, regulatory and intellectual property management expertise to expand our product pipeline.
- Critical care and biotechnology, where research and development activities are directed at the development of oncology and biotechnology products for the emerging as well as regulated markets.
- Custom pharmaceuticals, where we intend to leverage the strength of our process chemistry skills to cater to the niche segment of the specialty chemical industry targeting innovator pharmaceutical companies. The research and development is directed toward supporting the business to focus on marketing of process development and manufacturing services to emerging and established pharmaceutical companies.
- Drug discovery, where we are actively pursuing discovery and development of NCEs. Our research programs focus on the following therapeutic areas:
  - — Metabolic disorders;
  - — Cardiovascular disorders;
  - — Cancer; and
  - — Bacterial infections.

  We are pursuing an integrated research strategy with our laboratories in the U.S. focusing on discovery of new molecular targets and designing of screening assays to screen for promising lead molecules. Discovery is followed by selection and optimisation of lead molecules and further clinical development of those optimised leads at our laboratories in India.

2. Benefits derived as a result of the R&D

- Commercial production of the new products
- Modification of existing manufacturing processes for some of the products and significant savings in cost of production
- Modification of existing manufacturing processes to reduce the time cycle
- Indian patents and U.S. patents filings
- Development of analytical methods for the products in various therapeutic areas

3. Future plan of action

- Commercialisation of new products for which the products are under trials at development stage. Several new products have been identified after a thorough study of the market and the processes to manufacture these products will be developed in the R&D lab.
- Development of Analytical methods for the new products and method validations.

4. Expenditure on R & D

		FOR THE YEAR ENDED MARCH 31 2006	2005
A	Capital (Rs. thousand)	205,164	459,689
B	Recurring (Rs. thousand)	2,334,285	2,518,184
	Total (Rs. thousand)	**2,539,449**	**2,977,873**
	TOTAL R & D EXPENDITURE AS A PERCENTAGE OF TOTAL TURNOVER	**11.89%**	**18.29%**

1	Efforts, in brief, made towards technology absorption, adaptation and innovation	The Company has a full-fledged R&D Division continuously engaged in research on new products and on process development of existing products. The Company has developed indigenous technology in respect of the products manufactured by it. As soon as the technology is developed for a product, it is tested in Pilot Plant and thereafter commercial production is taken up. It is our philosophy to continuously upgrade the technology.
2	Benefits derived as a result of the above efforts, e.g., product improvement, cost reduction, product development, import substitution, etc.	Product quality improvement, cost reduction, product development, import substitution etc. The continuous up gradation and adoption of new technology has benefited the Company in the form of better production process, better yields, better quality of the end product and cost reduction.
3	In case of imported technology (imported during the last 5 years reckoned from the beginning of the financial year), following information may be furnished: a) Technology imported; b) Year of import; c) Has technology been fully absorbed; and d) If not fully absorbed, areas where this has not taken place, reasons there for and future plans of action.	No Imported technology

Technology, absorption, adaptation and innovation

FORM C

FOREIGN EXCHANGE EARNINGS AND OUTGO

Please refer information given in the notes to the annual accounts of the Company in Schedule 19 Notes to accounts item No.15 to item No.18.

IGAAP standalone financials

auditors' report to the members of Dr. Reddy's Laboratories Limited

We have audited the attached Balance Sheet of Dr.Reddy's Laboratories Limited ("the Company") as at 31 March 2006, the Profit and Loss Account of the Company for the year ended on that date annexed thereto and the Cash Flow Statement for the year ended on that date. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

1 We conducted our audit in accordance with auditing standards generally accepted in India. Those Standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

2 As required by the Companies (Auditor's Report) Order, 2003 ("the Order"), as amended by the Companies (Auditor's Report) (Amendment) Order 2004, issued by the Central Government of India in terms of sub-section (4A) of Section 227 of the Companies Act, 1956, we enclose in the Annexure a statement on the matters specified in paragraphs 4 and 5 of the said Order.

3 Further to our comments in the Annexure referred to in paragraph 2 above, we report that:

(a) we have obtained all the information and explanations, which to the best of our knowledge and belief were necessary for the purposes of our audit;

(b) in our opinion, proper books of account as required by law have been kept by the Company so far as appears from our examination of those books;

(c) the Balance Sheet, Profit and Loss Account and the Cash Flow Statement dealt with by this report are in agreement with the books of account;

(d) in our opinion, the Balance Sheet, Profit and Loss account and Cash Flow Statement dealt with by this report comply with the accounting standards referred to in sub-section (3C) of Section 211 of the Companies Act, 1956 to the extent applicable;

(e) on the basis of written representations received from the directors, as on 31 March 2006, and taken on record by the Board of Directors, we report that none of the directors is disqualified as on 31 March 2006 from being appointed as a director in terms of clause (g) of sub-section (1) of Section 274 of the Companies Act, 1956; and

(f) in our opinion and to the best of our information and according to the explanations given to us, the said accounts give the information required by the Companies Act, 1956, in the manner so required and give a true and fair view in conformity with the accounting principles generally accepted in India:

(i) in the case of the Balance Sheet, of the state of affairs of the Company as at 31 March 2006;

(ii) in the case of the Profit and Loss Account, of the profit of the Company for the year ended on that date; and

(iii) in the case of Cash Flow Statement, of the cash flows of the Company for the year ended on that date.

for **BSR & Co**
Chartered Accountants

Place: Hyderabad
Date: 31 May 2006

Sanjay Aggarwal
Partner
Membership No: 40780

annexure to the auditors' report

Annexure referred to in paragraph 2 of our report of eve n date to the members of Dr. Reddy's Laboratories Limited:

1. The Company has maintained proper records showing full particulars, including quantitative details and situation of fixed assets.
2. The Company has a phased programme of physical verification of its fixed assets which, in our opinion, is reasonable having regard to the size of the Company and the nature of its assets. In accordance with this programme, certain fixed assets were physically verified by management during the year and no discrepancies were identified during such verification.
3. During the year, the Company has disposed of one of its manufacturing facilities located in Goa. In our opinion and according to the information and explanations given to us, the aforesaid disposal has not affected the going concern assumption.
4. The inventories have been physically verified by management at reasonable intervals during the year.
5. In our opinion, the procedures of physical verification of inventories followed by management are reasonable and adequate in relation to the size of the Company and the nature of its business.
6. The Company is maintaining proper records of inventory. The discrepancies noticed during the physical verification of inventories as compared to book records were not material and have been properly dealt with in the books of account.
7. The Company has neither granted nor taken any loans, secured or unsecured to / from companies, firms or other parties covered in the register maintained under Section 301 of the Companies Act, 1956. Consequently, clauses 4(iii)(a) to 4(iii)(g) of the Order are not applicable to the Company.
8. In our opinion and according to the information and explanations given to us, there is an adequate internal control system commensurate with the size of the Company and the nature of its business for purchase of fixed assets and inventories and for the sale of goods and services. In our opinion and according to information and explanation given to us, there is no continuing failure to correct major weaknesses in internal controls.
9. In our opinion, and according to the information and explanations given by the management, we are of the opinion that contracts and arrangements referred to in Section 301 of the Companies Act, 1956 have been entered in the register required to be maintained under that section and such transactions have been made at prices which are reasonable having regard to the prevailing market prices at the relevant time.
10. The Company has not accepted any deposits from the public and consequently, the directives issued by the Reserve Bank of India and the provisions of Section 58 A, 58 AA or any other relevant provisions of the Companies Act, 1956 and the rules framed there under are not applicable to the Company.
11. In our opinion, the Company has an internal audit system commensurate with the size and nature of its business.
12. We have broadly reviewed the books of accounts maintained by the Company pursuant to the rules prescribed by the Central Government for maintenance of cost records under Section 209(1)(d) of the Companies Act, 1956, and are of the opinion that prima facie the prescribed accounts and records have been made and maintained. We, have not however made a detailed examination of records with a view to determining whether they are accurate and complete.
13. According to the information and explanations given to us and on the basis of our examination of books of account, the Company has been regular in depositing undisputed statutory dues including Provident Fund, Investor Education Protection Fund, Employees' State Insurance, Income Tax, Sales Tax, Wealth Tax, Customs Duty, Excise Duty, Cess and any other material statutory dues during the year with the appropriate authorities. Except for minor delays in some cases, the Company has been regular in depositing undisputed dues in respect of Service Tax.
14. According to the information and explanations given to us, no undisputed amounts payable in respect of Provident Fund, Employees' State Insurance, Sales Tax, Income Tax, Service tax, Wealth Tax, Customs Duty, Excise Duty, Cess and other material statutory dues were in arrears as at 31 March 2006 for a period of more than six months from the date they became payable.
15. According to the information and explanations given to us, there are no amounts in respect of Provident Fund, Income tax, Sales Tax, Wealth Tax, Service Tax, Customs Duty, Excise Duty and Cess that have not been deposited with the appropriate authorities on account of any dispute other than those mentioned in Annexure I to this report.
16. The Company does not have accumulated losses at the end of the financial year and has not incurred any cash losses in the financial year and in the immediately preceding financial year.
17. In our opinion and according to the information and explanations given to us, the Company has not defaulted in repayment of dues to its bankers or to any financial institutions. The Company did not have any outstanding debentures during the year.
18. The Company has not granted any loans and advances on the basis of security by way of pledge of shares, debentures and other securities. Accordingly, clause 4(xii) of the Order is not applicable.
19. In our opinion and according to the information and explanations given to us, the Company is not a chit fund/nidhi/mutual benefit fund/society. Accordingly, clause 4(xiii) of the Order is not applicable.

20. According to the information and explanations given to us, the Company is not dealing or trading in shares, securities, debentures and other investments. Accordingly, clause 4(xiv) of the Order is not applicable.

21. In our opinion and according to information and explanations given to us, the terms and conditions on which the Company has given guarantees for loans taken by a subsidiary and the joint venture from banks or financial institutions are not prejudicial to the interests of the Company.

22. In our opinion and according to information and explanations given to us and on the basis of examination of books of accounts, the term loans obtained by the Company were applied for the purpose for which such loans were obtained.

23. According to information and explanation given to us and on an overall examination of the balance sheet of the Company, we are of the opinion that the funds raised on short term basis have not been used for long term investment.

24. The Company has not made any preferential allotment of shares to companies / firms / parties covered in the register maintained under Section 301 of the Companies Act, 1956. Accordingly, clause 4(xviii) of the Order is not applicable.

25. The Company did not have any outstanding debentures during the year. Accordingly, clause 4(xix) of the Order is not applicable to the Company.

26. We have verified the end-use of money raised by public issues as disclosed in the notes to the financial statements.

27. According to information and explanations given to us, no fraud on or by the Company has been noticed or reported during the course of our audit.

for **BSR & Co**
Chartered Accountants

Place: Hyderabad
Date: 31 May 2006

Sanjay Aggarwal
Partner
Membership No: 40780

annexure I as referred to in para 15 of annexure to the auditors' report

Name of the Statute	Nature of the Dues	Amount (Rs.'000)	Period to which amount relates	Forum where dispute is pending
Sales Tax (Including Central Sales Tax and Local Sales Tax)				
Andhra Pradesh General Sales Tax Act, 1957	Tax	599	2002-03	Appellate Deputy Commissioner
Andhra Pradesh Central Sales Tax Act, 1956	Tax	1,434	2002-03	Appellate Deputy Commissioner
Bihar Finance Act, 1981	Tax	119	2002-03	Appellate Deputy Commissioner
Kerala Central Sales Tax Act, 1956	Tax	245	1997-98	Tax revision case filed with High Court
Kerala Central Sales Tax Act, 1956	Tax	66	1998-99	Assessing Officer
West Bengal Sales Tax Act, 1994	Tax, interest and penalty	445	1994-95	Assessing Officer
West Bengal Sales Tax Act, 1994	Tax	122	2002-03	Appellate Deputy Commissioner
Kerala General Sales Tax Act, 1963	Tax and surcharge	262	1997-98	Tax revision case filed with High Court
Gujarat Central Sales Tax Act, 1969	Tax	732	2003-04	Applellate deputy Commissioner
Delhi Sales Tax Act, 1975	Tax & Interest	691	2002-03	Applellate deputy Commissioner
Excise Duty				
Central Excise Act, 1944	Duty	89	2004-05	Commissioner Appeals
Central Excise Act, 1944	Duty	20	2004-05	Commissioner Appeals
Central Excise Act, 1944	Duty	181	2000-01	Assistant Commissioner
Central Excise Act, 1944	Duty	575	1999-00	Assistant Commissioner
Central Excise Act, 1944	Duty	79	1999-00	Assistant Commissioner
Central Excise Act, 1944	Duty	113	1999-00	Assistant Commissioner
Central Excise Act, 1944	Duty	154	2001-02	Assistant Commissioner
Central Excise Act, 1944	Duty	85	2003-04	Assistant Commissioner
Central Excise Act, 1944	Duty	121	2003-04	Assistant Commissioner
Central Excise Act, 1944	Duty	21	2002-03	Assistant Commissioner
Central Excise Act, 1944	Duty	52	2002-03	Assistant Commissioner
Central Excise Act, 1944	Duty	34	2003-04	Assistant Commissioner
Central Excise Act, 1944	Duty	38	2005-06	Assistant Commissioner
Central Excise Act, 1944	Duty	45	2004-05	CESTAT
Central Excise Act, 1944	Duty	24	2005-06	CESTAT
Central Excise Act, 1944	Duty	70	2005-06	Commissioner Appeals
Central Excise Act, 1944	Duty	2,959	2003-04	Additional Commissioner
Central Excise Act, 1944	Duty	4,729	2003-04	Commissioner Appeals
Central Excise Act, 1944	Duty	2,024	2004-05	
Central Excise Act, 1944	Duty	891	2002-03	Assistant Commissioner
Central Excise Act, 1944	Duty	106	2003-04	CESTAT
Central Excise Act, 1944	Duty	29	2005-06	Assistant Commissioner
Central Excise Act, 1944	Duty	26,743	2005-06	Commissioner
Central Excise Act, 1944	Duty	442	2003-04	Commissioner, Appeals
Central Excise Act, 1944	Interest	59	2003-04	Assistant Commissioner
Central Excise Act, 1944	Duty	288	2005-06	Assistant Commissioner
Central Excise Act, 1944	Duty	4,124	2005-06	Additional Commissioner
Central Excise Act, 1944	Duty	2,723		Commissioner
Central Excise Act, 1944	Duty	4,349	2002-03	Commissioner
Central Excise Act, 1944	Duty	1,476	2005-06	Assistant Commissioner
Central Excise Act, 1944	Duty	194	1993-94 & 1996-97	Commissioner, Appeals
Central Excise Act, 1944	Duty	478,217	2003-04	CESTAT
Central Excise Act, 1944	Duty	368	2004-05	Assistant Commissioner
Central Excise Act, 1944	Duty	4,684	2003-04	Commissioner, Appeals
Central Excise Act, 1944	Duty	466	1995-00	CESTAT
Central Excise Act, 1944	Duty	965	1998-02	CESTAT
Central Excise Act, 1944	Duty & Interest	87	2004-05	Commissioner, Appeals
Central Excise Act, 1944	Duty	241	2000-02	CESTAT
Income Tax				
Income Tax Act, 1961	Tax & Interest	5,884	1998-99	ITAT
Income Tax Act, 1961	Tax & Interest	34,566	2000-01	ITAT
Income Tax Act, 1961	Tax & Interest	20,162	1993-94 & 1994-95	Andhra Pradesh High Court
Income Tax Act, 1961	Tax & Interest	309	1991-92	Andhra Pradesh High Court
Income Tax Act, 1961	Tax & Interest	1,140	1992-93	Andhra Pradesh High Court
Income Tax Act, 1961	Tax & Interest	1,491	1993-94	Andhra Pradesh High Court
Income Tax Act, 1961	Tax & Interest	3,620	1994-95	Andhra Pradesh High Court
Income Tax Act, 1961	Tax & Interest	591	1993-94	ITAT
Income Tax Act, 1961	Tax & Interest	48,385	2003-04	ITAT
Income Tax Act, 1961	Tax & Interest	43,179	2002-03	ITAT
Income Tax Act, 1961	Tax & Interest	77,761	2003-04	C.I.T (A)
Customs Duty				
Customs Act, 1962	Duty	258	2003-04	Deputy Commissioner
Customs Act, 1962	Duty	17,911	1999-00	Supreme Court
Customs Act, 1962	Duty	16,600	2002-03	Supreme Court

balance sheet AS AT 31 MARCH 2006

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	SCHEDULE	As at 31 MARCH 2006	As at 31 MARCH 2005
SOURCES OF FUNDS			
Shareholders' funds			
Share capital	1	383,473	382,595
Reserves and surplus	2	22,237,944	20,358,243
		22,621,417	**20,740,838**
Loan funds			
Secured loans	3	1,451,285	32,729
Unsecured loans	4	7,787,410	2,699,642
		9,238,695	**2,732,371**
Deferred tax liability, net	19(3)	530,847	211,572
		32,390,959	**23,684,781**
APPLICATION OF FUNDS			
Fixed assets	5		
Gross block		10,528,977	10,042,244
Less: Accumulated depreciation		(4,910,826)	(4,416,829)
Net block		5,618,151	5,625,415
Capital work-in-progress (including capital advances)		1,129,160	601,253
		6,747,311	**6,226,668**
Investments	6	8,217,937	3,584,573
Current assets, loans and advances			
Inventories	7	4,430,968	3,038,108
Sundry debtors	8	5,812,160	4,176,411
Cash and bank balances	9	6,509,429	8,917,227
Loans and advances	10	6,776,456	2,152,021
		23,529,013	**18,283,767**
Current liabilities and provisions			
Current liabilities	11	5,532,648	3,776,474
Provisions	12	570,654	633,753
		6,103,302	4,410,227
Net current assets		**17,425,711**	**13,873,540**
		32,390,959	**23,684,781**
Significant accounting policies	19 (1)		
Notes to accounts	19		
The schedules referred to above form an integral part of the Balance Sheet			

As per our report attached
for BSR & CO.
Chartered Accountants
SANJAY AGGARWAL — PARTNER
Membership No.: 40780

HYDERABAD — 31 MAY 2006

for DR. REDDY'S LABORATORIES LIMITED

DR. K ANJI REDDY — CHAIRMAN
G V PRASAD — VICE CHAIRMAN & CEO
K SATISH REDDY — MANAGING DIRECTOR & COO
V S VASUDEVAN — CHIEF FINANCIAL OFFICER
V VISWANATH — COMPANY SECRETARY

profit and loss account FOR THE YEAR ENDED 31 MARCH 2006

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	SCHEDULE	For the year ended 31 MARCH 2006		For the year ended 31 MARCH 2005	
INCOME					
Sales, gross			20,955,141		16,250,756
Less: Excise duty on sales			(910,673)		(673,810)
Sales, net			20,044,468		15,576,946
License fees			29,982		12,229
Service income			60,550		4,816
Other income	13		1,230,711		696,431
			21,365,711		16,290,422
EXPENDITURE					
Material costs	14		7,561,526		5,444,264
Conversion charges			514,234		247,563
Excise duty			76,454		94,193
Personnel costs	15		2,128,442		1,823,643
Operating and other expenses	16		5,200,993		4,461,828
Research and development expenses		2,340,915		2,518,184	
Less: Amount reimbursed as per the research and development arrangements (Refer Note 19, Schedule 19)		(615,511)	1,725,404	(96,239)	2,421,945
Loss on sale of non-trade investments, net			18,434		26,398
Provision for decline in the value of long-term investments			175,000		302,864
Investment written off		134,103		–	
Less: Provision for decline in the value of long-term investments written back		(134,103)	–	–	–
Finance charges	17		214,241		99,571
Depreciation			1,113,337		924,575
			18,728,065		15,846,844
Profit before taxation			2,637,646		443,578
Income tax (expense) / benefit	18		(526,407)		211,010
Profit after taxation			2,111,239		654,588
Balance in profit and loss account brought forward			1,815,464		1,663,130
Amount available for appropriation			3,926,703		2,317,718
Appropriations:					
Proposed dividend on equity shares			383,473		382,595
Tax on proposed dividend			53,782		53,659
Dividend of previous years			114		–
Transfer to general reserve			211,124		66,000
Balance carried forward			3,278,210		1,815,464
			3,926,703		2,317,718
Earnings per share	19(4)				
Basic – Par value Rs.5 per share			27.58		8.55
Diluted – Par value Rs.5 per share			27.44		8.54
Notes to accounts	19				

The Schedules referred to above form an integral part of the Profit and Loss Account

As per our report attached
for BSR & CO.
Chartered Accountants
SANJAY AGGARWAL PARTNER
Membership No.: 40780

HYDERABAD 31 MAY 2006

for DR. REDDY'S LABORATORIES LIMITED

DR. K ANJI REDDY CHAIRMAN
G V PRASAD VICE CHAIRMAN & CEO
K SATISH REDDY MANAGING DIRECTOR & COO
V S VASUDEVAN CHIEF FINANCIAL OFFICER
V VISWANATH COMPANY SECRETARY

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

		As at 31 MARCH 2006		As at 31 MARCH 2005
SCHEDULE 1: SHARE CAPITAL				
Authorised				
100,000,000 (previous year: 100,000,000) equity shares of Rs.5 each		500,000		500,000
Issued				
76,694,770 (previous year: 76,519,149) equity shares of Rs.5 each fully paid-up		383,474		382,596
Subscribed and paid-up				
76,694,570 (previous year: 76,518,949) equity shares of Rs.5 each fully paid-up	383,472		382,594	
Add: Forfeited share capital (Note 2)	1	383,473	1	382,595
		383,473		**382,595**

NOTES:

1. Subscribed and paid-up share capital includes:

   (a) 34,974,400 (previous year: 34,974,400) equity shares of Rs.5 each fully paid-up, allotted as bonus shares by capitalisation of General Reserve.

   (b) 526,124 (previous year: 526,124) equity shares of Rs.5 each allotted pursuant to a scheme of amalgamation with Standard Equity Fund Limited without payments being received in cash.

   (c) 10,285,884 (previous year: 10,285,884) equity shares of Rs.5 each allotted and 82,800 (previous year: 82,800) equity shares of Rs.5 each extinguished pursuant to a scheme of amalgamation with erstwhile Cheminor Drugs Limited (CDL) without payments being received in cash.

   (d) 13,225,000 (previous year: 13,225,000) equity shares of Rs.5 each allotted against American Depository Shares (ADS).

   (e) 8,602,152 (previous year: 8,602,152) equity shares of Rs.5 each allotted against Global Depository Receipts (GDR) that were converted into ADS during the year ended 31 March 2002.

   (f) 113,388 (previous year: 113,388) equity shares of Rs.5 each allotted to the erstwhile members of American Remedies Limited (ARL) pursuant to a scheme of amalgamation with ARL without payments being received in cash.

   (g) 175,621(previous year: Rs.Nil) equity shares of Rs.5 each allotted to the employees of the Company on exercise of the vested stock options in accordance with the terms of exercise under the "Dr. Reddy's Employees Stock Option Plan, 2002".

2. Represents 200 (previous year: 200) equity shares of Rs.5 each, amount paid-up Rs.500/-, forfeited due to non-payment of allotment money.

schedules to the balance sheet (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 2: RESERVES AND SURPLUS		
Capital reserve		
Balance at the beginning and end of the year	7,276	7,276
Securities premium account		
Balance at the beginning of the year	7,734,005	7,734,005
Add: Received during the year on exercise of		
stock options issued to employees	143,807	–
	7,877,812	7,734,005
Employee stock options outstanding		
Balance at the beginning of the year	275,402	564
Add: Options granted during the year (including grants issued in exchange of surrendered options)	155,600	277,949
Less: Options forfeited during the year	(98,900)	(3,111)
Less: Options excercised during the year	(71,049)	–
Balance at the end of the year (A)	261,053	275,402
Deferred stock compensation cost		
Balance at the beginning of the year	222,965	470
Add: Options granted during the year (including grants in exchange for surrendered options)	155,600	277,949
Less: Amortisation during the year, net of forfeiture	(133,073)	(52,343)
Less: Options forfeited during the year	(98,900)	(3,111)
Balance at the end of the year (B)	146,592	222,965
(A-B)	114,461	52,437
General reserve		
Balance at the beginning of the year	10,749,061	10,683,061
Add: Transferred from profit and loss account	211,124	66,000
	10,960,185	10,749,061
Profit and loss account		
Balance in profit and loss account	3,278,210	1,815,464
	22,237,944	**20,358,243**
SCHEDULE 3: SECURED LOANS		
Loan from Indian Renewable Energy Development Agency Limited (Note 1)	25,145	31,065
Short-term loans from banks		
Cash credit (Note 2)	–	1,664
Loan from State Bank of India (Note 3)	1,426,140	–
	1,451,285	**32,729**

NOTES:

1. Loan from Indian Renewable Energy Development Agency Limited is secured by way of hypothecation of specific movable assets pertaining to the Solar Grid Interactive Power Plant. The loan is repayable in quarterly instalments of Rs.1,480 each and carries an interest rate of 2% per annum.

2. The Company has working capital facilities with a consortium of bankers and has created a charge, on a pari-passu basis, by hypothecation of the whole of the current assets, both present and future, and a first charge on immovable properties, pertaining to certain factories of the Company.

3. Short term loan from State Bank of India, Hyderabad carrying an interest rate of 8.8% per annum is fully secured by way of pledge of fixed deposits, (Refer Schedule 9).

schedules to the balance sheet (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 4: UNSECURED LOANS		
Sales tax deferment loan from the Government of Andhra Pradesh (interest free)	70,980	74,942
Short-term loans from banks		
Foreign currency packing credit loan (Note 1)	6,893,018	2,624,700
Bank overdraft (Note 2)	823,412	–
	7,787,410	**2,699,642**

NOTES:

1. Foreign currency packing credit loans are from State Bank of India, HSBC, Citi Bank, Standard Chartered Bank, Bank of America and ABN Amro Bank carrying an interest of LIBOR plus 50 – 70 bps, repayable on expiry of 6 months from the date of drawdown.
2. Bank overdraft is on the current accounts with Citi Bank and HDFC, which carry an interest rate of 11% and 9% per annum respectively.

SCHEDULE 5: FIXED ASSETS

DESCRIPTION	GROSS BLOCK				DEPRECIATION				NET BLOCK	
	AS AT 1 APRIL 2005	ADDITIONS	DELETIONS	AS AT 31 MARCH 2006	AS AT 1 APRIL 2005	FOR THE YEAR	DELETIONS	AS AT 31 MARCH 2006	AS AT 31 MARCH 2006	AS AT 31 MARCH 2005
Land – freehold (Note 1)	130,245	13,090	–	143,335	–	–	–	–	143,335	130,245
Buildings	1,655,128	150,671	139,009	1,666,790	277,934	70,306	10,822	337,418	1,329,372	1,377,194
Plant and machinery (Note 2)	4,528,623	676,728	471,692	4,733,659	2,205,210	526,015	305,550	2,425,675	2,307,984	2,323,413
Electrical equipment	606,691	66,343	124,909	548,125	310,062	58,486	103,802	264,746	283,379	296,629
Laboratory equipment	1,427,480	133,554	138,579	1,422,455	599,178	198,846	117,430	680,594	741,861	828,302
Furniture, fixtures and office equipment	648,458	90,414	66,397	672,475	417,598	100,829	59,834	458,593	213,882	230,860
Vehicles	216,303	78,827	33,521	261,609	81,812	45,268	19,091	107,989	153,620	134,491
Library	3,506	–	2,811	695	3,506	–	2,811	695	–	–
Intangibles										
Customer contracts	–	243,424	–	243,424	–	24,911	–	24,911	218,513	–
Technical know-how	522,310	–	–	522,310	282,804	52,231	–	335,035	187,275	239,506
Non-compete fees	227,500	–	–	227,500	182,000	22,750	–	204,750	22,750	45,500
Patents, trademarks and designs	76,000	10,600	–	86,600	56,725	13,695	–	70,420	16,180	19,275
(including marketing know-how)										
	10,042,244	**1,463,651**	**976,918**	**10,528,977**	**4,416,829**	**1,113,337**	**619,340**	**4,910,826**	**5,618,151**	**5,625,415**
Previous year	8,109,506	1,985,957	53,219	10,042,244	3,528,523	924,575	36,269	4,416,829	5,625,415	

NOTES:

1. Land located at Pydibheemavaram allotted by the Andhra Pradesh Industrial Infrastructure Corporation Limited having a book value of Rs.7,893 (previous year: Rs.7,893) is yet to be registered in the name of the Company.
2. The Company owns treated effluent discharge pipeline with the cost of Rs.9,257 (previous year: Rs.9,257) and net book value of Rs.2,551 (previous year: Rs.3,509) in equal proportion jointly with a third party in Pydibheemavaram pursuant to a mutual agreement.
3. Depreciation for the year includes depreciation amounting to Rs.211,639 (previous year: Rs.211,631) on assets used for Research and Development.

schedules to the balance sheet (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 6: INVESTMENTS		
Long-term at cost, unless otherwise specified		
I. QUOTED INVESTMENTS		
Non-trade		
(a) Equity shares (fully paid-up)		
12,000 (previous year: 12,000) equity shares of Rs.10 each of State Bank of India (Note 1)	3,096	3,096
(b) Units		
2,000 (previous year: 2,000) Units of UTI Master Gain' 92	20	20
Total quoted investments	**3,116**	**3,116**
II. UNQUOTED INVESTMENTS		
Trade		
Equity and preference shares (fully paid-up)		
In Subsidiary Companies		
50,000 (previous year: 50,000) equity shares of Rs.10 each of DRL Investments Limited	500	500
11,625,000 (previous year: 11,625,000) ordinary shares of HK$ 1 each of Reddy Pharmaceuticals Hong Kong Limited	58,021	58,021
Equity shares of OOO JV Reddy Biomed Limited (Note 2)	6,635	6,635
500,000 (previous year: 500,000) equity shares of US$ 1 each of Reddy Antilles N.V.	17,969	17,969
6,059,231 (previous year: 6,059,231) shares of Real $ 1 each of Dr. Reddy's Farmaceutica Do Brasil Ltd.	97,085	97,085
400,750 (previous year: 400,750) ordinary shares of Dr. Reddy's Laboratories Inc.	175,038	175,038
134,513 (previous year: 134,513) equity shares of Rs.10 each of Cheminor Investments Limited	1,345	1,345
2,500 (previous year: 2,500) ordinary shares of FF 100 each of Reddy Cheminor S.A.	1,558	1,558
88,644,161 (previous year: 88,644,161) equity shares of Rs.10 each of Aurigene Discovery Technologies Limited	886,442	886,442
34,476 (previous year: 34,476) ordinary A shares of GBP 0.01 each of Dr. Reddy's Laboratories (EU) Limited	141,502	141,502
98,124 (previous year: 98,124) ordinary shares of GBP 0.01 each of Dr. Reddy's Laboratories (EU) Limited	493,324	412,190
360,000 (previous year: 360,000) preference shares of GBP 0.0001 each of Dr. Reddy's Laboratories (EU) Limited	22,546	22,546
34,022,070 (previous year: 34,022,070) equity shares of Rs.10 each of Dr. Reddy's Bio-sciences Limited	266,388	266,388
Equity shares of OOO Dr.Reddy's Laboratories Limited, Russia (Note 2)	71,843	5,139
60 (previous year: 60) ordinary shares of Rand 1 each of Dr. Reddy's Laboratories (Proprietory) Limited	3	3
206 (previous year: 206) equity shares of US $ 0.01 each of Trigenesis Therapeutics Inc, USA	496,715	496,715
5,000 (previous year : nil) equity shares of CYP 1 each of Lacock Holdings Limited, Cyprus (Note 4)	3,952,700	–
50,000 (previous year: nil) Series "A" shares of Industrias Quimicas Falcon de Mexico, S.A. de. C.V. (Falcon) (Note 5)	657,025	–
In associates		
Nil (previous year: 2,870,502) ordinary shares of Real $ 1 each of Aurantis Farmaceutica Limited (Note 6)	–	85,099
Nil (previous year: 4,899,995) equity shares of Rs.10 each of Pathnet India Private Limited (Pathnet) (Note 6)	–	49,000
1,482,352 (previous year: nil) equity shares of Re. 1 each of Perlecan Pharma Private Limited (Refer Note 19, Schedule 19)	100,800	–
Nil (previous year: 300) equity shares of Rs.10 each of Dr. Reddy's Exports Limited	–	3
CARRIED FORWARD	**7,447,439**	**2,723,178**

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 6: INVESTMENTS (CONTINUED)		
Brought forward	7,447,439	2,723,178
Unquoted trade investments (continued)		
In joint venture		
Equity shares held in Kunshan Rotam Reddy Pharmaceutical Co. Limited (Note 2)	339,774	339,774
In other companies		
28,693 (previous year: 28,693) ordinary shares of Roubles 1,000 each of Biomed Russia Limited (Note 3)	65,557	65,557
In capital of partnership firm (a subsidiary)		
Globe Enterprises	2,396	2,396
(A partnership firm with Dr. Reddy's Holdings Limited organised under the Indian Partnership Act, 1932 wherein the Company and Dr. Reddy's Holdings Limited share the profits in the ratio of 95:5 respectively)		
Partners capital account:		
Dr. Reddy's Laboratories Limited – Rs.2,396		
Dr. Reddy's Holdings Private Limited – Rs.101		
Non-trade		
Nil (previous year: 500), 9% minus US$12 month LIBOR or 0% whichever is higher, Non convertible debentures of Rs.1,000,000 of Citicorp Finance (India) Limited	–	500,000
Nil (previous year: 5), 8-13% based on offer side fixed rate of 12 month Mibor Interbank Overnight Index Swap (MIOIS), convertible debentures of Rs.100,000,000 each of Citicorp Finance (India) Limited	–	500,000
5 (previous year: Nil), 0-9% based on offer side fixed rate of 12 month MIOIS, convertible debentures of Rs.50,000,000 each of Citicorp Finance (India) Limited	250,000	–
10 (previous year: Nil), 0-9.5% based on offer side fixed rate of 12 month MIOIS, convertible debentures of Rs.50,000,000 each of Citicorp Finance (India) Limited	500,000	–
5 (previous year: Nil), 0-12.35% based on offer side fixed rate of 12 month Mibor Interbank Overnight Index Swap (MIOIS), convertible debentures of Rs.100,000,000 each of Citicorp Finance (India) Limited	500,000	–
200,000 (previous year: 200,000) ordinary shares of Rs.10 each of Altek Engineering Limited	2,000	2,000
8,859 (previous year: 8,859) equity shares of Rs.100 each of Jeedimetla Effluent Treatment Limited	965	965
24,000 (previous year: 24,000) equity shares of Rs.100 each of Progressive Effluent Treatment Limited	2,400	2,400
II. TOTAL UNQUOTED INVESTMENTS	**9,110,531**	**4,136,270**
Current Investment, at lower of cost or market value		
In Mutual Funds		
Alliance Cash Manager – Nil (previous year : 3,066,713 units of NAV of Rs.16.3041 each)	–	50,000
Birla Liquid Plus – Nil (previous year : 2,804,434 units of NAV of Rs.17.8289 each)	–	50,000
Standard Chartered Grindlays Fixed Maturity – Nil (previous year : 20,000,000 units of NAV of Rs.10 each)	–	200,000
III. TOTAL INVESTMENT IN MUTUAL FUNDS	**–**	**300,000**
Aggregate cost of investments (I + II + III)	9,113,647	4,439,386
Less: Provision for decline, other than temporary, in the value of long term investments	(895,710)	(854,813)
TOTAL INVESTMENTS, NET	**8,217,937**	**3,584,573**

schedules to the balance sheet (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 6: INVESTMENTS (CONTINUED)		
Aggregate cost of quoted investments	3,116	3,116
Aggregate cost of unquoted investments	9,110,531	4,136,270
Aggregate cost of current investments	–	300,000
Market value of quoted investments	11,636	7,903
Market value of current investments	–	310,886

NOTES:

1. In respect of shares of State Bank of India, the share certificates were misplaced during transfer/lost in transit. The Company has initiated necessary legal action at the appropriate courts.
2. Equity shares held in Kunshan Rotam Reddy Pharmaceutical Co. Limited, China (Reddy Kunshan), OOO JV Reddy Biomed Limited and OOO Dr. Reddy's Laboratories Limited, Russia are not denominated in number of shares as per the laws of the respective countries.
3. In October 2004, the Company signed an agreement to sell the shares in Biomed, Russia to KT&T, a Russian Company for a total consideration of U.S.$5 million. Under the terms of the agreement, the transfer of shares was to be completed by 30 September 2005. However, the Company is currently involved in a litigation with a shareholder of Biomed, the outcome of which will determine the Company's ability to complete the sale. The company's investment in Biomed Russia has been fully provided for.
4. On March 3, 2006, the Company invested Rs.3,952,700 in Lacock Holding Limited ("Lacock") a newly floated subsidiary to acquire the entire share capital of Beta Group of Companies, Germany through Reddy Holding GmbH (subsidiary of Lacock).
5. On December 30, 2005 the Company acquired 100% of the share capital of Industrias Quimicas Falcon de Mexico,S.A.de.C.V ("Falcon"), a Roche group company for a total consideration of Rs.2,320,246 of which an amount of Rs.657,025 was paid towards shares and the balance Rs.1,663,221 as loan. (Refer Schedule 19)
6. During the current year, the Company sold its stake in Pathnet India Private Limited and wrote of its investment in Aurantis Farmaceutica Limited upon liquidation of that subsdiary.

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 7: INVENTORIES		
Stores and spares	344,463	304,547
Raw materials	1,978,164	992,425
Work-in-process	1,278,837	1,008,575
Finished goods	829,504	732,561
	4,430,968	**3,038,108**
SCHEDULE 8: SUNDRY DEBTORS		
(Unsecured)		
Debts outstanding for a period exceeding six months		
Considered good	144,267	313,763
Considered doubtful	169,340	156,488
Other debts		
Considered good	5,667,893	3,862,648
	5,981,500	4,332,899
Less: Provision for doubtful debts	(169,340)	(156,488)
	5,812,160	**4,176,411**

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 9: CASH AND BANK BALANCES		
Cash in hand	9,333	6,335
Balances with scheduled banks		
In current accounts	160,581	161,905
In EEFC current accounts	40,185	182,268
In deposit accounts	6,254,412	7,714,950
In unclaimed dividend accounts	12,110	11,307
In unclaimed fractional share pay order accounts	669	670
Balances with non-scheduled banks		
Current account with Sri Visakha Grameena Bank Limited	–	9
Balances with non-scheduled banks outside India		
In current accounts	32,139	48,375
In deposit accounts	–	791,408
	6,509,429	**8,917,227**
NOTES:		
1. Maximum amount outstanding at any time during the year with non-scheduled banks: Sri Visakha Grameena Bank Limited	9	143
2. Deposits with scheduled and non-scheduled banks include Rs.2,051 (previous year: Rs.2,051) representing margin money for letters of credit and bank guarantees.		
3. Deposits with scheduled banks include Nil (previous year: Rs.962,733) representing balance of unutilised money out of ADS issue.		
4. Fixed deposits amounting to Rs.4,468,870 (previous year: Rs.Nil) have been pledged against a loan taken by the Company's subsidiary, Reddy Holding GmbH		
5. The Company has taken a short term loan of Rs.1,426,140 from State Bank of India, Hyderabad which is secured by way of pledge of fixed deposits. (Refer Schedule 3)		
6. Deposits with banks outside India represent balance of unutilised money out of ADS issue: ABN Amro Bank, Netherlands	–	256,046
[Maximum amount outstanding at any time during the year: Rs.256,046 (previous year: Rs.262,982)]		
Citibank, Singapore	–	535,362
[Maximum amount outstanding at any time during the year: Rs.535,362 (previous year: Rs.549,862)]		
	–	**791,408**

schedules to the balance sheet (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	Maximum Balance		Balance As at	
	31 MARCH 2006	31 MARCH 2005	31 MARCH 2006	31 MARCH 2005
7. Closing balances and maximum amounts outstanding at any time during the year on current accounts with banks outside India:				
Citibank, New York	54,204	39,999	10,837	39,999
Credit Bank of Moscow, Moscow	10,964	26,182	310	945
ABN Amro Bank, Romania	7,392	3,218	3,031	1,038
ABN Amro Bank, Kazakhstan	3,440	7,422	3,355	1,000
Golden Taler Bank, Belarus	1,927	2,302	1,927	59
Societe Generale Yugoslav Bank Ad, Yugoslavia	1,109	2,071	145	199
Exim Bank HCMC, Vietnam	8,984	1,344	1,132	2
Standard Chartered Grindlays Bank, Sri Lanka	382	301	43	15
Citibank, Malaysia	537	1,076	256	156
Commercial Bank of Africa Ltd., Kenya	1,081	789	393	402
Ukreximbank, Ukraine	12,253	6,779	4,519	4,395
HSBC, U.A.E	1,420	3,954	848	161
Standard Chartered Bank, Ghana	396	308	–	4
Union Bank of Switzerland, Basel	3,419	–	3,419	–
National Bank for Foreign Economic Activity, Uzbekistan	383	–	383	
Agricultural bank of China	2,441	–	1,541	–
			32,139	**48,375**

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 10: LOANS AND ADVANCES		
(Unsecured)		
Considered good		
Loans and advances to wholly owned subsidiary companies, step down subsidiary companies, Joint venture and associates	4,600,342	651,072
Share application money pending allotment to subsidiary company	–	65,180
Advance recoverable from Perlecan Pharma Private Limited (Refer Note 19, Schedule 19)	234,541	–
Advances to material suppliers	310,483	97,351
Staff loans and advances	20,339	29,035
Interest accrued on investments	–	15,620
Other advances recoverable in cash or in kind or for value to be received	670,728	624,274
Advance tax (net of provision for current taxes Rs.280,674, previous year: Rs.1,198,033)	334,536	403,913
MAT credit entitlement	141,082	–
Balances with customs, central excise etc.	371,539	175,180
Deposits	92,866	90,396
Considered doubtful		
Advance towards investment	8,056	8,056
Share application money pending allotment in respect of an associate company	–	15,310
Staff loans and advances	6,500	6,500
Loans and advances to a wholly owned subsidiary company and associate	183,431	168,678
Other advances recoverable in cash or in kind or for value to be received	29,268	16,918
	7,003,711	2,367,483
Less: Provision for doubtful advances	(227,255)	(215,462)
	6,776,456	**2,152,021**

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

Staff loans and advances include:
Loans to an officer of the Company Rs.Nil (previous year: Nil)
[Maximum amount outstanding at anytime during the year Nil (previous year: Rs.90)]
Loans and advances in the nature of loans to wholly owned subsidiary companies, step down subsidiary companies, joint venture and associate comprise:

	BALANCE AS AT		MAXIMUM AMOUNT OUTSTANDING AT ANY TIME DURING THE YEAR	
	31 MARCH 2006	31 MARCH 2005	31 MARCH 2006	31 MARCH 2005
Dr. Reddy's Laboratories Inc.	262,719	136,842	262,719	141,945
Aurigene Discovery Technologies Limited	333,344	249,244	333,344	249,244
DRL Investments Limited	8,534	8,534	8,534	8,534
Cheminor Investments Limited	7	7	7	9
Reddy Antilles N.V.	110,020	107,875	113,251	113,559
Aurigene Discovery Technology Inc.	–	–	–	115,125
Dr. Reddy's Farmaceutica Do Brasil Ltda.	178,460	153,108	180,200	194,170
Dr. Reddy's Bio-sciences Limited	31,910	31,611	31,910	31,611
Kunshan Rotam Reddy Pharmaceutical Co. Limited	30,750	30,151	31,050	99,312
Dr. Reddy's Laboratories (Proprietary) Limited, South Africa	23,832	22,954	23,832	25,354
Pathnet India Private Limited, India	–	–	20,802	–
APR LLC	81,003	79,424	83,382	79,424
Reddy Holding GmbH	61,563	–	61,563	–
Lacock Holdings Limited	1,954,814	–	1,954,814	–
Industrias Quimicas Falcon de Mexico, S.A.de.C.V. (Falcon)	1,706,817	–	2,613,293	–
	4,783,773	**819,750**		

NOTES:

1. The loans and advances in the nature of loans to the subsidiaries and step down subsidiaries specified above have repayment schedule below seven years, except for the loan given to Dr. Reddy's Laboratories Inc., which has been extended for a further period of 3 years thereby increasing the total repayment period to 10 years. All these loans are interest free loans except for the following loans:

Loan to	Interest rate per annum
Dr. Reddy's Laboratories Inc.	London Inter Bank offer Rate (LIBOR) plus 0.7%
Dr. Reddy's Laboratories (Proprietary) Limited, South Africa	6%
Kunshan Rotam Reddy Pharmaceutical Co. Limited	6%
Lacock Holdings Limited	6 months EURO LIBOR plus 1.75%
Industrias Quimicas Falcon de Mexico, S.A de.C.V. (Falcon)	12 months USD LIBOR plus 1.5.%

2. There are no investments made by the loanees in the Company and in any of its subsidiaries except in respect of Aurigene Discovery Technologies Limited, Dr. Reddy's Laboratories Inc., Reddy Antilles N.V., Reddy Holding GmbH and Lacock Holdings Limited which have made investments in their wholly owned subsidiaries.

schedules to the balance sheet (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 11: CURRENT LIABILITIES		
Sundry creditors		
Due to small scale industrial undertakings	27,569	22,670
Others	5,210,379	3,491,039
Payable to subsidiary companies and joint venture	226,187	65,309
Book overdraft	–	143,891
Interest accrued but not due on loan	15,162	–
Unclaimed dividends *	12,110	11,307
Trade deposits	41,241	42,258
	5,532,648	**3,776,474**

* Investor Protection and Education Fund is being credited by the amounts of unclaimed dividends after seven years from the due date.

NOTES:

The names of the small scale industrial (SSI) undertakings to whom the company is indebted for a period of more than thirty days as at 31 March 2006:

Ability Engineering equipments
Ami Polymer Private Limited
Esjay Poly Products Private Limited
Godavari Plasto Containers Private Limited
Hyderabad Security Offset Printers
IndTech Systems & Mfg. Co. Private Limited
Lisa Ampoules & Vials Private Limited
Milan Art Printers
Murthy's Lab Glass Works
Paper Pack Industries
Pec Electricals Private Limited
Rohit Interlocks & Automation
Santhosh Engineering Works
Secunderabad Printed Cartons
Shivshakti Timber Industries
Sigachi Chloro Chemicals Private Limited
Sree Deepthi Packaging Industries
Super Olefins Private Limited
Susheel Enterprises
Temple Packaging Private Limited
Thejaswini Energy Chemicals Private Limited
Tirumala Comprints Private Limited
Veer-Chemie & Aromatics
Walnut Packaging Private Limited

The list of SSI undertakings was determined by the Company on the basis of information available with the Company and relied upon by the auditors.

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 12: PROVISIONS		
Proposed dividend	383,473	382,595
Tax on proposed dividend (including dividend tax)	53,782	53,659
Provision for		
Gratuity	–	82,083
Leave encashment	133,399	115,416
	570,654	**633,753**
Movement of provisions during the year:		
Gratuity		
Balance at the begining of the year	82,083	71,220
Add : Provision made during the year	13,655	40,935
Less: Amount paid / adjusted during the year	(95,738)	(30,072)
Balance at the end of the year	**–**	**82,083**
Leave encashment		
Balance at the begining of the year	115,416	78,478
Add: Provision made during the year	33,244	49,837
Less: Amount paid / adjusted during the year	(15,261)	(12,899)
Balance at the end of the year	**133,399**	**115,416**

schedules to the profit and loss account

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
SCHEDULE 13: OTHER INCOME		
Dividends		
Non-trade investments	29	98
Interest income		
On fixed deposits (gross, tax deducted at source:	567,380	252,005
Rs.131,599 ; previous year: Rs.47,990)		
On loans to subsidiaries and joint venture	36,213	4,308
On non-trade investments (gross, tax deducted at source :	85,874	72,445
Rs.19,270 ; previous year: Rs.21,450)		
On others	26,433	35,756
Gain on redemption of mutual fund units	14,510	83,273
Sale of spent chemicals	101,589	85,014
Profit on sale of fixed assets, net	330,148	26,813
Royalty income from subsidiary	3,982	–
Miscellaneous income	64,553	136,719
	1,230,711	**696,431**

		2006	2006	2005	2005
SCHEDULE 14: MATERIAL COSTS					
(a)	**Opening**				
	Work-in-process	1,008,575		954,440	
	Finished goods	732,561	1,741,136	490,546	1,444,986
	Closing				
	Work-in-process	1,278,837		1,008,575	
	Finished goods	829,504	2,108,341	732,561	1,741,136
	Net increase		(367,205)		(296,150)
(b)	**Raw materials consumed**				
	Opening stock of raw materials	992,425		885,173	
	Add: Purchases	5,980,521		3,486,031	
		6,972,946		4,371,204	
	Less: Closing stock	(1,978,164)	4,994,782	(992,425)	3,378,779
(c)	**Stores, chemicals, spares and packing material consumed**		762,062		700,873
(d)	**Purchase of traded goods**		2,171,887		1,660,762
			7,561,526		**5,444,264**

Raw materials consumed include Rs.14,393 (previous year: Rs.51,205) being stocks written-off/written-down, Rs.100,059 (previous year: Rs.69,366) being cost of samples issued and is net of Rs.390,541 (previous year: Rs.26,688) being sale of raw materials.

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
SCHEDULE 15: PERSONNEL COSTS		
Salaries, wages and bonus	1,690,864	1,436,171
Contribution to provident and other funds	84,825	103,510
Workmen and staff welfare expenses	219,680	231,619
Amortisation of deferred stock compensation cost	133,073	52,343
	2,128,442	**1,823,643**

schedules to the profit and loss account (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
SCHEDULE 16: OPERATING AND OTHER EXPENSES		
Power and fuel	482,293	432,058
Repairs and maintenance		
Buildings	22,373	29,799
Plant and machinery	235,264	226,774
Others	186,524	217,187
Rent	68,338	51,904
Rates and taxes	58,885	31,371
Insurance	167,904	220,784
Travelling and conveyance	209,627	177,522
Communication	69,335	75,668
Advertisements	39,785	16,134
Commission on sales	189,848	118,794
Carraige outwards	747,926	604,065
Other selling expenses	1,453,909	1,082,241
Printing and stationery	55,739	56,833
Donations	60,039	87,761
Legal and professional	628,969	171,298
Bad debts written off	27,349	44,618
Provision for doubtful advances	11,793	177,259
Provision for doubtful debts, net	12,852	(39,279)
Directors' sitting fees	360	392
Directors' remuneration	63,159	15,338
Auditors' remuneration	8,602	7,850
Bank charges	32,015	27,772
Exchange loss, net	103,574	463,492
Sundry expenses	264,531	164,193
	5,200,993	**4,461,828**
SCHEDULE 17: FINANCE CHARGES		
Interest on foreign currency loan notes issued on acquisition of Dr. Reddy's Laboratories (EU) Limited	323	513
Interest on packing credit loan	175,477	37,064
Other finance charges	38,441	61,994
	214,241	**99,571**
SCHEDULE 18: INCOME TAXES		
Current taxes		
Domestic taxes	279,418	–
MAT credit entitlement	(141,082)	–
Deferred taxes		
Domestic taxes	319,275	(211,010)
Fringe benefit tax	68,796	–
	526,407	**(211,010)**

SCHEDULE 19: NOTES TO ACCOUNTS

1. SIGNIFICANT ACCOUNTING POLICIES

a) Basis of preparation

The financial statements of Dr. Reddy's Laboratories Limited ("Dr. Reddy's" or "the Company") have been prepared and presented under the historical cost convention on the accrual basis of accounting in accordance with the accounting principles generally accepted in India ("GAAP") and comply with the mandatory Accounting Standards ("AS") issued by the Institute of Chartered Accountants of India to the extent applicable and with the relevant provisions of the Companies Act, 1956. The financial statements are presented in Indian rupees rounded off to the nearest thousand.

b) Use of estimates

The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities on the date of the financial statements and reported amounts of revenues and expenses for the year. Actual results could differ from these estimates. Any revision to accounting estimates is recognised prospectively in the current and future periods.

c) Fixed assets and depreciation

Fixed assets are carried at the cost of acquisition or construction less accumulated depreciation. The cost of fixed assets includes taxes, duties, freight and other incidental expenses related to the acquisition and installation of the respective assets. Borrowing costs directly attributable to acquisition or construction of those fixed assets which necessarily take a substantial period of time to get ready for their intended use are capitalised. The cost of fixed assets also includes the exchange differences arising in respect of foreign currency loans or other liabilities incurred for the purpose of their acquisition or construction.

Advances paid towards the acquisition of fixed assets outstanding at each balance sheet date and the cost of fixed assets not ready for their intended use before such date are disclosed under capital work-in-progress.

Depreciation on fixed assets is provided using the straight-line method based on the useful life of the assets as estimated by Management. Depreciation is calculated on a pro-rata basis from the date of installation till the date the assets are sold or disposed. Individual assets costing less than Rs. 5,000 are depreciated in full in the year of acquisition.

Management's estimates of the useful lives for various categories of fixed assets are given below:

	YEARS
Buildings	
– Factory and administrative buildings	30
– Ancillary structures	3 to 10
Plant and machinery	3 to 15
Electrical equipment	5 to 15
Laboratory equipment	5 to 15
Furniture, fixtures and office equipment (other than computer equipment)	4 to 8
Computer equipment	3
Vehicles	4 to 5
Library	2

d) Intangible assets and amortisation

Intangible assets are recorded at the consideration paid for acquisition. Intangible assets are amortised over their estimated useful lives on a straight-line basis, commencing from the date the asset is available to the Company for its use. The management estimates the useful lives for the various intangible assets as follows:

	YEARS
Customer contracts	2 to 5
Technical know-how	10
Non compete fees	1.5 to 10
Patents, trademarks and designs	6 to 10
(including marketing know-how)	

e) Investments

Long-term investments are carried at cost less any other-than-temporary diminution in value, determined separately for each individual investment.

Current investments are carried at the lower of cost and fair value. The comparison of cost and fair value is done separately in respect of each category of investment.

f) Inventories

Inventories are valued at the lower of cost and net realisable value. Cost of inventories comprises all cost of purchase, cost of conversion and other costs incurred in bringing the inventories to their present location and condition.

The methods of determining cost of various categories of inventories are as follows:

Raw materials	First-in-first out (FIFO)
Stores and spares	Weighted average method
Work-in-process and finished goods (manufactured)	FIFO and including an appropriate share of production overheads
Finished goods (traded)	Actual cost of purchase
Goods in transit	Actual cost of purchase

g) Research and development

Revenue expenditure on research and development is expensed as incurred. Capital expenditure incurred on research and development is capitalised as fixed assets and depreciated in accordance with the depreciation policy of the Company.

h) Retirement benefits

Contributions payable to an approved gratuity fund (a defined benefit plan), determined by an independent actuary at the balance sheet date, are charged to the profit and loss account. Leave encashment cost which is a defined benefit, is accrued based on an actuarial valuation at the balance sheet date, carried out by an independent actuary.

Contributions payable to the recognised provident fund and approved superannuation scheme, which are defined contribution schemes, are charged to the profit and loss account.

i) Foreign currency transactions and balances

Foreign currency transactions are recorded using the exchange rates prevailing on the dates of the respective transactions. Exchange differences arising on foreign currency transactions settled during the year are recognised in the profit and loss account except that exchange differences related to acquisition of fixed assets are adjusted in the carrying amount of the related fixed assets.

Monetary assets and liabilities denominated in foreign currencies as at the balance sheet date, not covered by forward exchange contracts, are translated at year-end rates. The resultant exchange differences (except those related to acquisition of fixed assets) are recognised in the profit and loss account. Non-monetary assets are recorded at the rates prevailing on the date of the transaction.

Income and expenditure items at representative offices are translated at the respective monthly average rates. Monetary assets at representative offices at the balance sheet date are translated using the year-end rates. Non-monetary assets are recorded at the rates prevailing on the date of the transaction.

Forward contracts are entered into to hedge the foreign currency risk of the underlying outstanding at the balance sheet date and also to hedge the foreign currency risk of firm commitments or highly probable forecast transactions. The premium or discount on all such contracts is amortised as income or expense over the life of the contract. Any profit or loss arising on the cancellation or renewal of forward contracts is recognised as income or expense for the period.

In relation to the forward contracts entered into to hedge the foreign currency risk of the underlying outstanding at the balance sheet date, the exchange difference is calculated and recorded in accordance with paragraphs 36 and 37 of AS-11 (revised). The exchange difference on such a forward exchange contract is calculated as the difference the foreign currency amount of the contract translated at the exchange at the reporting date, or the settlement date where the transaction is settled during the reporting period, and the corresponding foreign currency amount translated at the later of the date of inception of the forward exchange contract and the last reporting date. Such exchange differences are recognized in the profit and loss account in the reporting period in which the exchange rates change.

j) Revenue recognition

Revenue from sale of goods is recognised when significant risks and rewards in respect of ownership of products are transferred to customers. Revenue from domestic sales of formulation products is recognised on despatch of products to stockists by clearing and forwarding agents of the Company. Revenue from domestic sales of active pharmaceutical ingredients and intermediates is recognised on despatch of products from the factories of the Company. Revenue from export sales is recognised on shipment of products.

Revenue from product sales is stated exclusive of returns, sales tax and applicable trade discounts and allowances.

Service income is recognised as per the terms of contracts with customers when the related services are performed or the agreed milestones are achieved.

Dividend income is recognised when the unconditional right to receive the income is established. Income from interest on deposits, loans and interest bearing securities is recognised on the time proportionate method.

Export entitlements under the Duty Entitlement Pass Book ("DEPB") scheme are recognised as income when the right to receive credit as per the terms of the scheme is established in respect of the exports made and where there is no significant uncertainty regarding the ultimate collection of the relevant export proceeds.

The Company enters into certain dossier sales, licensing and supply arrangements with certain third parties. These arrangements include certain performance obligations by the Company. Revenue from such arrangements is recognised in the period in which the Company completes all its performance obligations.

k) Income-tax expense

Income tax expense comprises current tax and deferred tax charge or credit.

Current tax

The current charge for income taxes is calculated in accordance with the relevant tax regulations applicable to the Company.

Deferred tax

Deferred tax charge or credit reflects the tax effects of timing differences between accounting income and taxable income for the period. The deferred tax charge or credit and the corresponding deferred tax liabilities or assets are recognised using the tax rates that have been enacted or substantially enacted by the balance sheet date. Deferred tax assets are recognised only to the extent there is reasonable certainty that the assets can be realised in future; however, where there is unabsorbed depreciation or carry forward of losses, deferred tax assets are recognised only if there is a virtual certainty of realisation of such assets. Deferred tax assets are reviewed at each balance sheet date and is written-down or written-up to reflect the amount that is reasonably/virtually certain (as the case may be) to be realised.

The break-up of the major components of the deferred tax assets and liabilities as at balance sheet date has been arrived at after setting off deferred tax assets and liabilities where the Company has a legally enforceable right to set-off assets against liabilities and where such assets and liabilities relate to taxes on income levied by the same governing taxation laws.

l) Earnings per share

The basic earnings per share ("EPS") is computed by dividing the net profit after tax for the year by the weighted average number of equity shares outstanding during the year. For the purpose of calculating diluted earnings per share, net profit after tax for the year and the weighted average number of shares outstanding during the year are adjusted for the effects of all dilutive potential equity shares. The dilutive potential equity shares are deemed converted as of the beginning of the period, unless they have been issued at a later date. The diluted potential equity shares have been adjusted for the proceeds receivable had the shares been actually issued at fair value (i.e. the average market value of the outstanding shares).

m) Employee stock option schemes

In accordance with the Securities and Exchange Board of India guidelines, the excess of the market price of shares, at the date of grant of options under the Employee stock option schemes, over the exercise price is treated as employee compensation and amortised over the vesting period.

n) Provisions and contingent liabilities

The Company creates a provision when there is a present obligation as a result of a past event that probably requires an outflow of resources and a reliable estimate can be made of the amount of the obligation. A disclosure for a contingent liability is made when there is a possible obligation or a present obligation that may, but probably will not, require an outflow of resources. Where there is possible obligation or a present obligation in respect of which the likelihood of outflow of resources is remote, no provision or disclosure is made.

o) Impairment of assets

The Company assesses at each balance sheet date whether there is any indication that an asset may be impaired. If any such indication exists, the Company estimates the recoverable amount of the asset. If such recoverable amount of the asset or the recoverable amount of the cash generating unit to which the asset belongs is less than its carrying amount, the carrying amount is reduced to its recoverable amount. The reduction is treated as an impairment loss and is recognised in the profit and loss account. If at the balance sheet date there is an indication that if a previously assessed impairment loss no longer exists, the recoverable amount is reassessed and the asset is reflected at the recoverable amount subject to a maximum of depreciated historical cost.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO ACCOUNTS (CONTINUED)

2. COMMITMENTS AND CONTINGENT LIABILITIES

		As at 31 MARCH 2006	As at 31 MARCH 2005
i)	Commitments / contingent liabilities:		
(a)	Guarantees issued by banks	45,330	92,932
(b)	Guarantees issued by the Company on behalf of subsidiaries, associates and joint venture	22,397,602	942,661
(c)	Letters of credit outstanding	224,484	183,914
(d)	Contingent consideration payable in respect of subsidiaries acquired	12,463	84,662
(e)	Commitment towards research funding to a third party	–	34,470
ii)	Claims against the Company not acknowledged as debts in respect of:		
(a)	Income tax matters, pending decisions on various appeals made by the Company and by the Department	468,730	272,382
(b)	Excise matters, under dispute	483,089	478,928
(c)	Custom matters, under dispute	34,511	–
(d)	Sales tax matters, under dispute	14,117	4,753
(e)	Other matters, under dispute	9,457	950

(f) Demand for payment to the credit of the Drug Prices Equalisation Account under Drugs (Price Control) Order,1995 which is being contested by the Company in respect of its product "Norfloxacin". During the previous year, the Hon'ble High Court of Andhra Pradesh dismissed the review petition filed by the Company against the original order passed by the same Court. Subsequently, the Company had filed a Special Leave Petition with the Supreme Court of India appealing against the High Court Order.

During the year ended March 31, 2006 the Company received a further demand notice from the authorities for a total of Rs.284,984 towards the overcharged sale price (principal) and interest thereon. The Company filed a fresh writ petition in the High Court of Andhra Pradesh challenging the demand notice. The High Court whilst admitting the writ petition, granted an interim order wherein it ordered the Company to deposit 50% of the principal amounting to Rs.77,149. The Company deposited this amount with the authorities under protest on November 14, 2005, whilst it awaits the outcome of its appeal with the Supreme Court. The Company has provided fully against the potential liability in respect of the principal amount demanded in earlier years. However, based on an external legal opinion, the Company believes that no interest can be levied on such a demand and hence department's contention is not tenable. In the event the Company is unsuccessful in its appeal with the Supreme Court, there could be penalties and interest, the amount of which cannot be ascertained at this stage

		As at 31 MARCH 2006	As at 31 MARCH 2005
iii)	Estimated amount of contracts remaining to be executed on capital account and not provided for (net of advances)	685,163	192,161

iv) The Employee Provident Fund Organisation (EPFO) has on 9 September 2005 issued a clarification as per which provident fund contributions should be deducted on leave encashment from 1 May 2005 onwards. It has also been stated that the claims between 1 October 1994 and 30 April 2005 should be kept in abeyance till this matter is decided by the Central Board of Trustees. Based on this notification, the Company has deducted and paid provident fund on leave encashment for the period from May 2005. However, the Company is in the process of quantifying the liability with respect to the period 1 October 1994 till 30 April 2005, which it believes would not be material.

v) The Company is also involved in other lawsuits, claims, investigations and proceedings, including patent and commercial matters, which arise in the ordinary course of business. However, there are no such matters pending that the Company expects to be material in relation to its business.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO ACCOUNTS (CONTINUED)

3. DEFERRED TAXATION

Deferred tax liability, net included in the balance sheet comprises the following:

	As at 31 MARCH 2006	As at 31 MARCH 2005
Deferred tax assets		
Sundry debtors	62,192	57,867
Operating losses carried forward	–	301,812
Capital losses carried forward	–	36,890
Provisions	98,370	120,758
Other current assets	18,018	9,244
Current liabilities	404	404
	178,984	**526,975**
Deferred tax liability		
Excess of depreciation allowable under Income tax law over depreciation provided in accounts	709,831	738,547
Deferred tax liability, net	**(530,847)**	**(211,572)**

4. EARNINGS PER SHARE (EPS)

The computation of EPS is set out below:

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
	Basic & Diluted EPS	Basic & Diluted EPS
Earnings		
Net profit for the year	2,111,239	654,588
Shares		
Number of shares at the beginning of the year	76,518,949	76,518,949
Equity shares issued on exercise of vested stock options	175,621	–
Total number of equity shares outstanding at the end of the year	76,694,570	76,518,949
Weighted average number of equity shares outstanding during the year – Basic	76,546,658	76,518,949
Add: Weighted average number of equity shares arising out of outstanding stock options (net of the stock options forfeited) that have dilutive effect on the EPS	386,138	175,964
Weighted average number of equity shares outstanding during the year – Diluted	76,932,796	76,694,913
Earnings per share of par value Rs. 5 – Basic (Rs.)	27.58	8.55
Earnings per share of par value Rs.5 – Diluted (Rs.)	27.44	8.54

5. RELATED PARTY DISCLOSURES

a. The related parties where control exists are the subsidiaries, step down subsidiaries and the partnership firm. There are no other parties over which the Company has control.

b. Related parties where control / significant influence exists or with whom transactions have taken place during the year:

Subsidiaries including step-down subsidiaries

- OOO JV Reddy Biomed Limited, Russia;
- Reddy Pharmaceuticals Hong Kong Limited, Hong Kong;
- Dr. Reddy's Laboratories Inc., USA;
- Reddy Cheminor S.A., France;
- Reddy Antilles N.V., Netherlands;
- Dr. Reddy's Farmaceutica Do Brasil Ltda., Brazil;
- Aurigene Discovery Technologies Limited, India;
- Aurigene Discovery Technology Inc., USA;
- Cheminor Investments Limited, India;
- DRL Investments Limited, India;
- Reddy Netherlands B.V., Netherlands;

SCHEDULE 19: NOTES TO ACCOUNTS (CONTINUED)

- Trigenesis Therapeutics Inc, USA;
- Reddy US Therapeutics Inc., USA;
- Dr. Reddy's Laboratories (EU) Limited, UK;
- Dr. Reddy's Laboratories (UK) Limited, UK;
- Dr. Reddy's Laboratories (Proprietary) Limited, South Africa;
- OOO Dr. Reddy's Laboratories Limited, Russia;
- Reddy Pharmaceuticals Inc, USA;
- Dr. Reddy's Bio-sciences Limited, India;
- Globe Enterprises (a partnership firm in India);
- Industrias Quimicas Falcon de Mexico, S.A.de.C.V. (Falcon), Mexico;
- Lacock Holdings Limited, Cyprus;
- Reddy Holding GmbH, Germany;
- beta Holding GmbH, Germany;
- beta Healthcare Verwaltungs, Germany;
- betapharm Arzneimittel GmbH, Germany;
- beta Healthcare Solutions GmbH, Germany;
- beta Institut GmbH, Germany;

Associates

Pathnet India Private Limited, India ("Pathnet")	Enterprise over which the Company had significant influence through 49% shareholding. (The Company sold its stake in Pathnet during the year)
Aurantis Farmaceutica Ltda., Brazil ("Aurantis")	Enterprise over which the Company had significant influence through 50% shareholding. (Aurantis was liquidated during the year)
Dr. Reddy's Exports Limited, India ("DREL")	Enterprise over which the Company has significant influence through 22% shareholding. (DREL was liquidated during the year)
Perlecan Pharma Private Limited, India ("Perlecan")	Enterprise over which the Company has significant influence through 14.28% shareholding and through representation on the Board of Directors of Perlecan.

Joint venture

Kunshan Rotam Reddy Pharmaceutical Company Limited ("Reddy Kunshan"), China	Enterprise over which the Company exercises joint control with other joint venture partners and holds 51.2% equity stake.

Enterprises where principal shareholders have control or significant influence ("Significant interest entities")

Dr. Reddy's Research Foundation ("Research Foundation")	Enterprise over which the principal shareholders have significant influence
Dr. Reddy's Holdings Private Limited	Enterprise owned by principal shareholders

Others

Diana Hotels Limited	Enterprise owned by relative of a director
Ms K Samrajyam	Spouse of Chairman
Ms G Anuradha	Spouse of Vice Chairman and Chief Executive Officer
Ms Deepti Reddy	Spouse of Managing Director and Chief Operating Officer
Madras Diabetes Research Foundation	Enterprise promoted by a director
Dr. Reddy's Heritage Foundation	Enterprise in which the Chairman is a director
Dr. Reddy's Foundation for Human and Social development	Enterprise where principal shareholders are trustees
Manava Seva Dharma Samvardhani Trust	Enterprise in which a director is a Managing trustee

Key Management Personnel represented on the Board

Dr. K Anji Reddy	Chairman
Mr G V Prasad	Vice Chairman and Chief Executive Officer
Mr K Satish Reddy	Managing Director and Chief Operating Officer

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO ACCOUNTS (CONTINUED)

Non-Executive and Independent Directors on the Board

- Mr Anupam Puri
- Dr Krishna G Palepu
- Dr. Omkar Goswami
- Mr P N Devarajan
- Mr Ravi Bhoothalingam
- Dr. V Mohan

c. Particulars of related party transactions
The following is a summary of significant related party transactions:

	PARTICULARS	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
i.	Sales to:		
	Subsidiaries and joint ventures	4,960,683	4,804,697
	Significant interest entities	32,198	–
ii.	Interest income from subsidiary	36,213	4,308
iii.	Royalty income from subsidiary	3,982	–
iv.	Purchases from:		
	Subsidiaries	24,230	33,323
	Significant interest entities	30,527	49,879
	Joint venture entity	–	39,278
v.	Lease rentals and other service charges paid to significant interest entities	17,526	25,319
vi.	Contributions made to others	21,550	21,788
vii.	Contribution made to subsidiaries and step-down subsidiary for research	371,160	365,770
viii.	Hotel expenses paid to an enterprise owned by relative of a director	7,426	4,649
ix.	Rent paid to:		
	Key management personnel	9,971	9,208
	Spouses of key management personnel	8,956	7,936
x.	Directors' sitting fees	360	392
xi.	Donation to an enterprise in which a director is a Managing trustee	730	100
xii.	Investment in subsidiaries, joint venture and associates during the year:		
	Dr. Reddy's Laboratories (EU) Limited	81,134	–
	Dr. Reddy's Bio-sciences Limited	–	15,000
	OOO Dr.Reddy's Laboratories Limited	66,704	–
	Trigenesis Therapeutics Inc., USA	–	496,718
	Kunshan Rotam Reddy Pharmaceutical Company Limited	–	83,037
	Industrias Quimicas Falcon de Mexico, SA de CV (Falcon)	657,025	–
	Lacock Holdings Limited	3,952,700	–
	Perlecan Pharma Private Limited	100,800	–
xiii.	Provision for decline in the value of long-term investments and investments written-off, net of write back	175,000	239,679
xiv.	Provision for loans given to subsidiary and associate	14,753	168,669
xv.	Share application money paid to:		
	OOO Dr. Reddy's Laboratories Limited	–	65,180
xvi.	Interest free deposit adjusted against loan to associate	–	53,000
xvii.	Contract manufacturing charges paid to a subsidiary	218,525	–
xviii.	Guarantee given on behalf of a subsidiary	21,602	–
xix.	Guarantee given on behalf of a joint venture	31,500	–

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO ACCOUNTS (CONTINUED)

d. The Company has the following amounts due from / to related parties:

PARTICULARS	As at 31 MARCH 2006	As at 31 MARCH 2005
i. Due from related parties (included in loans and advances and sundry debtors):		
Subsidiaries (included in sundry debtors)	2,457,307	2,190,084
Key management personnel and relatives (included in loans and advances)	2,261	3,680
ii. Deposit with related parties (included in loans and advances)	3,000	3,000
iii. Due to related parties (included in current liabilities):		
Subsidiaries	226,187	59,908
Joint Venture entity	–	5,401
Significant interest entities	20,145	15,572
Enterprise owned by relative of a director	522	170

e. Details of remuneration paid to the whole-time and non-whole-time directors are given in Note 6 of Schedule 19.

f. Equity held in subsidiaries, associates and a joint venture have been disclosed under "Investments", (Schedule 6). Share application money paid to subsidiary and joint venture by the Company for which shares are yet to be allotted and loans to subsidiaries, joint venture and an associate have been disclosed under "Loans and advances", (Schedule 10).

6. PARTICULARS OF MANAGERIAL REMUNERATION

The remuneration paid to managerial personnel during the year:

	CHAIRM AN		VICE-CHAIRMAN & CEO		MANAGING DIRECTOR & COO		NON-EXECUTIVE / INDEPENDENT DIRECTORS	
	For the year ended 31 MARCH		For the year ended 31 MARCH		For the year ended 31 MARCH		For the year ended 31 MARCH	
	2006	2005	2006	2005	2006	2005	2006	2005
Salaries and allowances	1,800	1,800	1,514	1,080	1,500	1,080	–	–
Commission	23,051	4,337	12,488	2,169	12,457	2,169	9,815	2,169
Other perquisites	144	144	195	195	195	195	–	–
	24,995	**6,281**	**14,197**	**3,444**	**14,152**	**3,444**	**9,815**	**2,169**

The executive directors are covered under the Company's gratuity policy along with the other employees of the Company. Proportionate amount of gratuity and leave encashment is not included in the aforementioned disclosure.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO ACCOUNTS (CONTINUED)

Computation of net profit and directors' commission under Section 309(5) of the Companies Act, 1956 and commission payable to directors.

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
Profit after taxation as per profit and loss account	2,111,239	654,588
Add:		
Provision for taxation	457,611	(211,010)
Provision for wealth tax	1,505	1,274
Directors' sitting fees	360	392
Managerial remuneration to directors	63,159	15,338
Depreciation as per books of accounts	1,113,337	924,575
	3,747,211	**1,385,156**
Less:		
Depreciation as envisaged under section 350 of the Companies Act, 1956 (Refer Note 1 below)	1,113,337	924,575
Profit on sale of fixed assets, net	330,148	26,813
Profit for the purpose of calculating directors' commission as per the provisions of the Companies Act, 1956	2,303,726	433,768
Commission payable to whole-time directors @ 2.5% (previous year: 2%) (Refer Note 2 below)	47,996	8,675
Commission payable to non-whole-time directors: Maximum allowed as per the Companies Act, 1956 (1%)	23,037	4,337
Maximum approved by the shareholders (0.5%)	11,518	2,169
Commission approved by the Board (Refer Note 3 below)	9,815	2,169

NOTE:

1. The Company depreciates fixed assets based on estimated useful lives that are lower than those implicit in Schedule XIV to the Companies Act, 1956. Accordingly, the rates of depreciation used by the Company are higher than the minimum rates prescribed by Schedule XIV.
2. During the current year the Board of directors of the Company approved an increase in the commission payable to whole time directors by 0.5% effective 30 January 2006 for the CEO and 1 February 2006 for the COO, which is subject to the approval of the shareholders. The increase is accordingly accounted proportionately from the effective date to 31 March 2006.
3. Stock compensation cost amounting to Rs.5,317 thousands (previous year: Rs.Nil) pertaining to stock options issued to non-whole time directors have not been considered as remuneration in the table above. The stock options were issued pursuant to a shareholders' resolution dated 24 September 2001.

7. AUDITORS' REMUNERATION

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
a) Audit fees	6,550	6,050
b) Other charges		
Taxation matters	500	50
Other matters	950	1,625
c) Reimbursement of out of pocket expenses	602	125
	8,602	**7,850**

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO ACCOUNTS (CONTINUED)

8. INTEREST IN JOINT VENTURE

The Company has a 51.2 percent interest in Reddy Kunshan, a joint venture in China. Reddy Kunshan is engaged in manufacturing and marketing of active pharmaceutical ingredients and intermediates and formulations in China. The contractual arrangement between shareholders of Reddy Kunshan indicates joint control as the minority shareholders, along with the company, have significant participating rights such that they jointly control the operations of Reddy Kunshan. The aggregate amounts of the assets, liabilities, income and expenses related to the Company's share in Reddy Kunshan as at and for the year ended 31 March 2006 are given below:

PARTICULARS	As at 31 MARCH 2006	As at 31 MARCH 2005
BALANCE SHEET		
Secured loan	91,315	69,859
Unsecured loan	105,751	94,603
Foreign currency translation reserve	358	4,058
Fixed assets, net	90,385	91,892
Deferred tax assets, net	–	9,277
Current assets, loans and advances		
Inventories	37,425	35,403
Sundry debtors	45,096	40,921
Cash and bank balances	8,947	10,389
Loans and advances	11,062	8,608
Current liabilities and provisions		
Current liabilities	35,839	12,606
Net current assets	66,691	82,715
Estimated amount of contracts remaining to be executed on capital account and not provided for (net of advances)	62	1,237

PARTICULARS	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
INCOME STATEMENT		
Income		
Sales	194,805	146,244
Other income	4,985	–
Expenditure		
Material costs	95,450	67,679
Personnel costs	51,227	46,432
Operating and other expenses	79,548	76,002
Research and development expenses	4,331	7,513
Finance charges	7,289	4,700
Depreciation	11,189	4,806
Loss before taxation	(49,244)	(60,888)
Provision for taxation		
– Current tax	–	–
– Deferred tax (expense) / benefit	(9,810)	4,449
Loss after taxation	(59,054)	(56,439)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO ACCOUNTS (CONTINUED)

9. EMPLOYEE STOCK OPTION SCHEME

Dr. Reddy's Employees Stock Option Plan-2002 (the 2002 Plan): The Company instituted the 2002 Plan for all eligible employees in pursuance of the special resolution approved by the shareholders in the Annual General Meeting held on September 24, 2001. The Scheme covers all directors and employees of Dr. Reddy's and directors and employees of all its subsidiaries. Under the Scheme, the 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 2002 Plan was amended on July 28, 2004 at the annual general meeting of shareholders to provide for stock options grants in two categories:

Category A: 1,721,700 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: 573,778 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., Rs.5 per option).

The DRL 2002 Plan was further amended on July 27, 2005 at the annual general meeting of shareholders to provide 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., Rs.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 for 30 days prior to the grant, in the stock exchange where there is highest trading volume during that period. Notwithstanding the foregoing, the Compensation 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.

As the number of shares that an individual employee is entitled to receive and the price of the option are known at the grant date, the scheme is considered as a fixed grant.

In the case of termination of employment, all non-vested 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.

During the current year, the Company under the 2002 Plan has issued 249,360 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 date of grant is given below:

DATE OF GRANT	NUMBER OF OPTIONS GRANTED	EXERCISE PRICE (RUPEES)	MARKET PRICE (RUPEES) (AS PER SEBI GUIDELINES)
5-Apr-05	1,000	5.00	744.50
6-May-05	17,000	5.00	671.95
27-May-05	32,500	725.00	724.50
27-May-05	178,560	5.00	724.50
13-Jun-05	12,000	5.00	713.85
31-Aug-05	8,300	5.00	793.15
	249,360		

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO ACCOUNTS (CONTINUED)

CATEGORY A – FAIR MARKET VALUE OPTIONS	YEAR ENDED MARCH 31, 2006			
	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE	WEIGHTED- AVERAGE REMAINING CONTRACTUAL LIFE (MONTHS)
Outstanding at the beginning of the year	298,950	Rs.747.00-1,149.00	Rs.977.31	50
Granted during the year	32,500	725.00-725.00	725.00	81
Expired / forfeited during the year	(46,700)	725.00-1,149.00	994.35	–
Surrendered by employees during the year	(90,000)	977.30-1,063.02	1,034.45	–
Exercised during the year	(77,500)	883.00-977.30	943.84	–
Outstanding at the end of the year	117,250	725.00-1,063.02	878.85	64
Exercisable at the end of the year	37,882	Rs.725.00-1,063.02	Rs.943.85	45

CATEGORY B – PAR VALUE OPTIONS	YEAR ENDED MARCH 31, 2006			
	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE	WEIGHTED- AVERAGE REMAINING CONTRACTUAL LIFE (MONTHS)
Outstanding at the beginning of the year	379,549	Rs.5	Rs.5	84
Granted during the year	216,860	5	5	81
Forfeited during the year	(133,304)	5	5	–
Exercised during the year	(98,121)	5	5	–
Outstanding at the end of the year	364,984	5	5	81
Exercisable at the end of the year	18,136	Rs.5	Rs.5	59

The Company has followed intrinsic method of accounting based on which a compensation expense of Rs.133,073 (previous year : Rs.52,343 thousands) has been recognized in the profit and loss account (refer Schedule 2 – Deferred stock compensation cost)

CATEGORY A – FAIR MARKET VALUE OPTIONS	YEAR ENDED MARCH 31, 2005			
	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE	WEIGHTED- AVERAGE REMAINING CONTRACTUAL LIFE (MONTHS)
Outstanding at the beginning of the year	911,038	Rs.883.00-1,396.00	Rs.968.95	66
Granted during the year	466,500	747.00-885.00	872.82	82
Expired / forfeited during the year	(352,657)	765.00-1,063.02	918.84	–
Surrendered by employees during the year in exchange for category B options	(725,931)	747.00-1,396.00	928.07	–
Exercised during the year	–	–	–	–
Outstanding at the end of the year	298,950	747.00-1149.00	977.31	50
Exercisable at the end of the year	188,538	Rs.883.00-1,149.00	Rs.996.54	35

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO ACCOUNTS (CONTINUED)

CATEGORY B – PAR VALUE OPTIONS	YEAR ENDED MARCH 31, 2005			
	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE	WEIGHTED- AVERAGE REMAINING CONTRACTUAL LIFE (MONTHS)
Outstanding at the beginning of the year	–	–	–	–
Granted during the year				
In exchange for Category A surrendered options	280,873	Rs.5	Rs.5	84
New options	102,650	5	5	84
Forfeited during the year	(3,974)	5	5	–
Exercised during the year	–	–	–	–
Outstanding at the end of the year	379,549	Rs.5	Rs.5	84
Exercisable at the end of the year	–	–	–	–

10. UTILISATION OF FUNDS RAISED ON ADS ISSUE

The net proceeds from the ADS offering after underwriting discounts and commissions were approximately United States Dollar (USD) 125.4 million. The Company had liquidated USD 74.1 million of its liabilities, thereby reducing its interest outflows substantially and the balance of USD 51.3 million has been primarily utilised towards acquisitions and for providing loans to subsidiaries and an associate.

The utilisation during the current year is as follows:

PARTICULARS	AMOUNT IN USD MILLION
Expenses during the year	0.01
Loan to subsidiary	1.00
Acquisition of Falcon during the year	34.53
Total utilisation during the year	**35.54**

The information required as per clause 4C and 4D and notes thereon of part II of Schedule VI to the Companies Act, 1956

11. CAPACITY AND PRODUCTION

a) Licensed capacity, installed capacity and production

		As at 31 MARCH 2006			As at 31 MARCH 2005		
CLASS OF GOODS	UNIT	LICENSED CAPACITY (I)	INSTALLED CAPACITY (I)	ACTUAL PRODUCTION	LICENSED CAPACITY (I)	INSTALLED CAPACITY (I)	ACTUAL PRODUCTION
Formulations (ii)	Million units	1,907*	1,907*	2,816	2,806.95*	2,806.95*	2,426.29
Active pharmaceutical ingredients and intermediates (API)	Tonnes	6,941	3,833	3,101	6,941	4,068	2,994
Generics	Million Units	5,500	5,500	1,939	5,500	5,500	1,519
Biotechnology	Grams	370	370	73	370	370	38.73

* On single shift basis

NOTES:

(i) Licensed and installed capacities are as certified by Management and have not been verified by the auditors as this is a technical matter.

(ii) Actual production of Formulations includes 427.3 (previous year: 356.96) million units produced on loan licensing basis from outside parties. During the current year, the company sold one of its Formulations manufacturing facilities.

(iii) Actual production of API includes 625.24 (previous year: 238.94) tonnes produced on loan licensing basis from outside parties.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO ACCOUNTS (CONTINUED)

12. PARTICULARS OF PRODUCTION, SALE AND STOCK

	OPENING STOCK		PRODUCTION	PURCHASES		SALES **		CLOSING STOCK	
	QUANTITY	VALUE	QUANTITY	TRADED GOODS (UNITS)	VALUE	QUANTITY	VALUE	QUANTITY	VALUE
Formulations (million units)	300.98	521,191	2,816	453.15	708,176	3,092.32	9,955,557	477.81	462,444
	(305.13)	(329,947)	(2,426)	(430.85)	(706,592)	(2,861)	(8,106,935)	(300.98)	(521,191)
Active pharmaceutical ingredients and intermediates (tonnes)	245	188,919	3,101	979	1,224,368	4,102*	8,873,273	223	221,159
	(126)	(148,461)	(2,994)	(714)	(954,170)	(3,589)*	(6,866,368)	(245)	(188,919)
Generics (million units)	19.82	22,451	1,939.48	–	–	1,932.87	2,186,688	26.43	11,274
	(28.82)	(12,138)	(1,519)	–	–	(1,528)	(2,184,488)	(19.82)	(22,451)
Biotechnology (grams)	–	–	73	–	–	73	649,555	–	37,669
			(39)			(39)	(33,485)		(Nil)
Custom Pharmaceutical Services (Kilograms)	–	–	219,200	79,685	239,343	285,971	934,967	12,914	96,958
	–	–	(Nil)	(Nil)	(Nil)	(Nil)	(Nil)	(Nil)	(Nil)
TOTAL		**732,561**			**2,171,887**		**22,600,040**		**829,504**
							(17,191,276)		
Less: Inter segmental Sales							1,644,899		
							(940,520)		
Sales (Gross of excise duty) as per profit and loss account							20,955,141		
Previous year		(490,546)			(1,660,762)		(16,250,756)		(732,561)

* Includes captive consumption of active pharmaceutical ingredients 537 tonnes (previous year: 464 tonnes)
** Sales are net of samples, rejections and damages but include intersegmental sales.

Figures in brackets represent the numbers for the previous year.

13. RAW MATERIALS CONSUMED DURING THE YEAR

RAW MATERIALS	2006		2005	
	QUANTITY (KGS)	VALUE	QUANTITY (KGS)	VALUE
Recemiac-2-azabicyclo (3,3,0) Octane	10,547	151,451	10,490	180,235
2 4-Dichloro-5-Fluoro Acetophenone	522,786	228,750	648,420	232,206
Isobutyl Aceto Phenone (HVD)	1,883,588	273,761	1,581,880	239,971
2-Acetyl-6-Methoxy Naphthalene	659,142	203,698	549,600	177,138
Methanol	7,031,238	121,938	5,936,301	105,957
Toluene	3,632,997	133,811	2,839,106	101,791
Isopropyl Alcohol IP	1,620,026	89,080	2,144,915	112,509
Fluoro Quinolonic Acid	321,200	259,204	238,972	157,934
(4R-Cis-1,1Dimethylethyl,1-6-Cynaomethyl)	6,007	151,530	3,715	134,931
Others		3,381,559		1,936,107
TOTAL		**4,994,782**		**3,378,779**

'Others' include no item which in value individually accounts for 10 percent or more of the total value of the raw materials consumed.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO ACCOUNTS (CONTINUED)

14. DETAILS OF IMPORTED AND INDIGENOUS RAW MATERIALS, SPARE PARTS, CHEMICALS, PACKING MATERIALS AND COMPONENTS CONSUMED

PARTICULARS	For the year ended 31 MARCH 2006		For the year ended 31 MARCH 2005	
	VALUE	% OF TOTAL CONSUMPTION	VALUE	% OF TOTAL CONSUMPTION
Raw materials				
Imported	2,833,062	57%	1,847,049	55%
Indigenous	2,161,720	43%	1,531,730	45%
	4,994,782		3,378,779	
Stores, Chemicals, Spares and Packing materials				
Imported	154,536	20%	96,282	14%
Indigenous	607,526	80%	604,591	86%
	762,062		700,873	
	5,756,844		**4,079,652**	

15. CIF VALUE OF IMPORTS

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
Raw materials	2,331,109	1,899,439
Capital equipment (including spares and components)	413,426	383,433
	2,744,535	**2,282,872**

16. EARNINGS IN FOREIGN CURRENCY

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
Exports on FOB basis	11,966,591	9,139,041
Interest on deposits with banks	2,723	41,777
Interest on loan to subsidiaries	36,213	4,308
Service income and license fees	90,532	12,229
Royalty income	3,982	–
	12,100,041	**9,197,355**

17. EXPENDITURE IN FOREIGN CURRENCY

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
Travelling	23,901	38,757
Interest on loan note	323	513
Legal and professional fees	394,079	46,564
Bio-studies expenses	182,174	497,952
Other expenditure	1,304,715	1,374,281
	1,905,192	**1,958,067**

18. DIVIDEND REMITTANCE IN FOREIGN CURRENCY

The Company does not make any direct remittances of dividends in foreign currencies to ADS holders. The Company remits the equivalent of the dividends payable to the ADS holders in Indian Rupees to the depositary bank, which is the registered shareholder on record for all owners of the Company's ADS. The depositary bank purchases the foreign currencies and remits dividends to the ADS holders.

SCHEDULE 19: NOTES TO ACCOUNTS (CONTINUED)

19. RESEARCH AND DEVELOPMENT ARRANGEMENT

I – Ven Pharma arrangement

During the year ended 31 March 2005, the Company entered into a joint development and commercialisation agreement with I-VEN Pharma Capital Limited ("I-VEN"). As per the terms of the agreement, I-VEN will fund up to fifty percent of the project costs (development, registration and legal costs) related to the specified generic product filings made by the Company for the United States of America market. The terms of the arrangement do not require the Company to repay the funds or purchase I-VEN's interest in the event of the failure of the research and development. However, on successful commercialisation of these products, the Company would pay I-VEN royalty on sales for a period of 5 years for each product. The first tranch advanced by I-VEN of Rs. 985,388 was received on 28 March 2005.

The amount received from I-VEN will be recognised in the income statement upon completion of specific milestones as detailed in the agreement. Accordingly, an amount of Rs. 384,488 (previous year: Rs.96,239) has been recognised in the current year representing the proportionate costs relating to the completion of specified filings as a credit to research and development expenses.

Perlecan Pharma arrangement

In September 2005, the Company announced the formation of an integrated drug development company, Perlecan Pharma Private Limited ("Perlecan Pharma"), with a total equity of U.S.$52,500 to be contributed jointly by the Company, Citigroup Venture Capital International Growth Partnership Mauritius Limited ("Citigroup Venture") and ICICI Venture Funds Management Company ("ICICI Venture"). Perlecan Pharma will be engaged in the clinical development and out-licensing of New Chemical Entity ("NCE") assets. As part of this arrangement, the Company has transferred all rights and title, including the development and commercialization rights, of four NCE assets to Perlecan Pharma, on March 27, 2006 ("the closing date"). As per the arrangement, Citigroup Venture and ICICI Venture will contribute U.S.$22,500 each and the Company will contribute U.S.$7,500 towards Perlecan Pharma's initial equity capital. As a result, the Company will initially own approximately 14.28% of the equity of Perlecan Pharma. In addition, Perlecan Pharma will issue to the Company warrants to purchase 45 million equity shares of Perlecan Pharma, at Re 1.00 per warrant, the exercise of which will be contingent upon the success of certain research and development milestones. If the warrants are fully exercised, then the Company will own approximately 62.5% of the equity shares of Perlecan Pharma.

As of March 31, 2006, the three investors have invested Rs.705,700 (US.$ 15,818) in Perlecan Pharma. The Company's share of equity was Rs.100,800 (US.$2,259). The Company has also committed to invest an additional amount of Rs.170,000 as its equity contribution in the future. Further, three out of seven directors on the board of Perlecan will be from the Company.

As per the terms of the arrangement, the Company will have the first right to conduct product development and chemical trials on behalf of Perlecan Pharma on an arm's length basis subject to the final decision by the board of directors of Perlecan Pharma. Moreover, the research and development expenses incurred by the Company from 1 April 2005 till the closing date of the arrangement will be reimbursed by Perlecan Pharma. Accordingly, an amount of Rs.231,023 (previous year: Rs.Nil) receivable from Perlecan Pharma has been recognised in the current year representing cost relating to product development and chemical trials as a credit to research and development cost.

20. SEGMENT INFORMATION

In accordance with AS 17 – Segment Reporting, segment information has been given in the consolidated financial statements of Dr. Reddy's and therefore no separate disclosure on segment information is given in these financial statements.

21. COMPARATIVE FIGURES

Previous year's figures have been regrouped / reclassified wherever necessary to conform to current year's classification.

cash flow statement FOR THE YEAR ENDED 31 MARCH 2006

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
CASH FLOWS FROM OPERATING ACTIVITIES		
Profit before taxation	2,637,646	443,578
Adjustments:		
Depreciation	1,113,337	924,575
Provision for wealth tax	1,505	1,274
Bad debts written off	27,349	44,618
Income from redemption of mutual funds units	(14,510)	(83,273)
Amortisation of Deferred stock compensation expense, net	133,073	52,343
Unrealised foreign exchange loss	64,192	39,041
Loss on sale of non-trade invetsments, (net)	18,434	26,398
Provision for decline in the value of long-term investments and investments written off, net of write back	175,000	302,864
Interest income	(689,467)	(328,758)
Dividend income	(29)	(98)
Finance charges	214,241	99,571
(Profit)/loss on sale of fixed assets, net	(330,148)	(26,813)
Provision for doubtful debts	12,852	(39,279)
Provision for doubtful advances	11,793	177,259
Operating cash flows before working capital changes	3,375,268	1,633,300
(Increase)/decrease in sundry debtors	(1,698,293)	191,900
(Increase) in inventories	(1,392,860)	(457,998)
(Increase)/decrease in loans and advances	(762,117)	102,948
Increase in current liabilities and provisions	1,483,140	990,443
Cash generated from operations	1,005,138	2,460,593
Income taxes (paid)/refunded	(208,411)	44,809
NET CASH PROVIDED BY OPERATING ACTIVITIES	**796,727**	**2,505,402**
Cash flows from investing activities		
Purchase of fixed assets	(1,873,207)	(1,604,048)
Proceeds from sale of fixed assets	687,727	43,763
Purchase of investments	(10,020,482)	(10,761,720)
Sale of investments	5,274,899	13,114,902
Loans and advances given to subsidiaries, joint ventures & associates	(3,913,477)	(449,882)
Interest received	705,087	350,430
Dividend received	29	98
NET CASH PROVIDED BY/(USED) IN INVESTING ACTIVITIES	**(9,139,424)**	**693,543**
Cash flows from financing activities		
Proceeds from issue of share capital	73,638	–
Repayment of long-term borrowings	(9,882)	(156,824)
Repayment of short-term borrowings	(7,700,859)	(317,730)
Proceeds from short-term borrowings	14,202,482	2,624,700
Interest paid	(199,079)	(99,571)
Dividend paid (including dividend tax)	(436,368)	(431,615)
NET CASH PROVIDED BY FINANCING ACTIVITIES	**5,929,932**	**1,618,960**

cash flow statement (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
Net increase/(decrease) in cash and cash equivalents	(2,412,765)	4,817,905
Cash and cash equivalents at the beginning of the period (Note 1)	8,917,227	4,080,832
Effect of exchange gain on cash and cash equivalents	4,967	18,490
Cash and cash equivalents at the end of the period (Note 1)	6,509,429	8,917,227

As per our report attached
for BSR & CO.
Chartered Accountants
SANJAY AGGARWAL PARTNER
Membership No.: 40780

HYDERABAD 31 MAY 2006

for DR. REDDY'S LABORATORIES LIMITED

DR. K ANJI REDDY CHAIRMAN
G V PRASAD VICE CHAIRMAN & CEO
K SATISH REDDY MANAGING DIRECTOR & COO
V S VASUDEVAN CHIEF FINANCIAL OFFICER
V VISWANATH COMPANY SECRETARY

NOTES:

1. Cash and cash equivalents comprise:

	As at 31 MARCH 2006	As at 31 MARCH 2005
Cash in hand	9,333	6,335
Balances with banks		
In current accounts	192,720	210,289
In deposit accounts	6,252,361	8,504,307
In EEFC current accounts	40,185	182,268
In unclaimed dividend account	12,110	11,307
In unclaimed fractional share pay order accounts	669	670
In margin money	2,051	2,051
	6,509,429	**8,917,227**

2. The Company has undrawn borrowing facilities of Rs.3,043,730. These facilities are essentially for funding working capital requirements of the Company.

3. The Company has taken a short term loan of Rs.1,426,140 from State Bank of India, Hyderabad which is secured by way of pledge of fixed deposits.

4. Previous year's figures have been regrouped/reclassified, wherever necessary to conform to the current year's classification.

balance sheet abstract and company's general business profile

1. Registration details

Registration No.:	4507	State Code:	01
Balance Sheet Date:	31 03 06 (Date Month Year)		

2. Capital raised during the year (Amount in Rs. thousands)

Public Issue:	NIL	Rights Issue:	NIL
Bonus Issue:	NIL	Private Placement:	NIL

3. Position of moblisation and deployment of funds (Amount in Rs. thousands)

Total Liabilities:	32390959	Total Assets:	32390959
Sources of Funds:			
Paid – up Capital:	383473	Reserves and Surplus:	22237944
Secured Loans:	1451285	Unsecured Loans:	7787410
Application of Funds:			
Net Fixed Assets:	5618151	Investments:	8217937
Net Current Assets:	17425711	Miscellaneous Exp.:	NIL

4. Performance of the Company (Amount in Rs. thousands)

Turnover:	20044468	Total Expenditure:	18728065
Profit Before Tax:	2637646	Profit After Tax:	2111239
Earning Per Share in Rs.	27.58	Dividend Rate %	100

5. Generic names of three principal products/services of company (as per the monetary terms)

Item Code No.: (ITC Code)	29420090
Product Description:	Ramipril
Item Code No.: (ITC Code)	29420001
Product Description:	Ciprofloxacin Hydrochloride
Item Code No.: (ITC Code)	29420012
Product Description:	Ibuprofen

IGAAP consolidated financials

AUDITORS' REPORT
TO THE BOARD OF DIRECTORS OF DR. REDDY'S LABORATORIES LIMITED
ON THE CONSOLIDATED FINANCIAL STATEMENTS OF DR. REDDY'S LABORATORIES LIMITED AND ITS SUBSIDIARIES

1 We have audited the attached consolidated balance sheet of Dr. Reddy's Laboratories Limited ("the Company") and its subsidiaries [collectively referred to as the "Dr. Reddy's Group"] as at 31 March 2006 and also the consolidated profit and loss account for the year ended on that date annexed thereto and the consolidated cash flow statement for the year ended on that date. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

2 We conducted our audit in accordance with auditing standards generally accepted in India. Those Standards require that we plan and perform the audit to obtain reasonable assurance whether the consolidated financial statements are free of material misstatement. An audit includes, examining on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall consolidated financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

3 The consolidated financial statements have been prepared by the Company's management in accordance with the requirements of Accounting Standard 21 - Consolidated Financial Statements, issued by the Institute of Chartered Accountants of India.

4 In our opinion and to the best of our information and according to the explanations given to us, the consolidated financial statements give a true and fair view in conformity with the accounting principles generally accepted in India:

(i) in the case of the Consolidated Balance Sheet, of the consolidated state of affairs of Dr. Reddy's Group as at 31 March 2006;

(ii) in the case of Consolidated Profit and Loss Account, of the consolidated results of operations of Dr. Reddy's Group for the year ended on that date; and

(iii) in the case of Consolidated Cash Flow Statement, of the consolidated cash flows of Dr. Reddy's Group for the year ended on that date.

for **BSR & Co**
Chartered Accountants

Place: Hyderabad
Date: 31 May 2006

Sanjay Aggarwal
Partner
Membership No: 40780

consolidated balance sheet AS AT 31 MARCH 2006

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	SCHEDULE	As at 31 MARCH 2006	As at 31 MARCH 2005
SOURCES OF FUNDS			
Shareholders' funds			
Share capital	1	383,473	382,595
Reserves and surplus	2	20,305,323	19,035,159
		20,688,796	19,417,754
Loan funds			
Secured loans	3	23,381,665	104,563
Unsecured loans	4	7,787,410	2,699,642
		31,169,075	2,804,205
Deferred tax liabilities	19(7)	781,491	218,172
		52,639,362	22,440,131
APPLICATION OF FUNDS			
Fixed assets	5		
Gross block		42,012,771	13,052,133
Less: Accumulated depreciation		(8,095,598)	(5,253,208)
Net block		33,917,173	7,798,925
Capital work-in-progress (including capital advances)		1,398,202	616,032
		35,315,375	8,414,957
Deferred tax assets	19(7)	26,584	9,615
Investments	6	1,337,248	1,319,714
Current assets, loans and advances			
Inventories	7	6,665,211	3,526,922
Sundry debtors	8	5,104,357	3,821,185
Cash and bank balances	9	9,796,156	9,354,954
Loans and advances	10	5,051,942	2,795,653
		26,617,666	19,498,714
Current liabilities and provisions			
Current liabilities	11	8,527,625	4,947,468
Provisions	12	2,129,886	1,855,401
		10,657,511	6,802,869
Net current assets		15,960,155	12,695,845
		52,639,362	22,440,131
Significant accounting policies	19 (1)		
Notes to consolidated accounts	19		

The schedules referred to above form an integral part of the Consolidated Balance Sheet

As per our report attached
for BSR & CO.
Chartered Accountants
SANJAY AGGARWAL PARTNER
Membership No.: 40780

HYDERABAD 31 MAY 2006

for DR. REDDY'S LABORATORIES LIMITED

DR. K ANJI REDDY CHAIRMAN
G V PRASAD VICE CHAIRMAN & CEO
K SATISH REDDY MANAGING DIRECTOR & COO
V S VASUDEVAN CHIEF FINANCIAL OFFICER
V VISWANATH COMPANY SECRETARY

consolidated profit and loss account FOR THE YEAR ENDED 31 MARCH 2006

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	SCHEDULE	For the year ended 31 MARCH 2006		For the year ended 31 MARCH 2005	
INCOME					
Sales, gross			24,605,247		19,212,597
Less: Excise duty and other similar duties and taxes on sales			(1,139,473)		(853,837)
Sales, net			23,465,774		18,358,760
Service income			113,403		4,816
License fees			47,521		57,441
Other income	13		1,205,517		656,927
			24,832,215		19,077,944
EXPENDITURE					
Material costs	14		8,164,634		6,014,891
Conversion charges			514,234		247,563
Excise duty and other similar duties and taxes			76,454		94,193
Personnel costs	15		3,495,337		2,938,329
Operating and other expenses	16		6,503,386		5,904,969
Research and development expenses		2,352,824		2,393,335	
Less: Amount reimbursed as per the research and development arrangements (Refer Note 13, Schedule 19)	19(13)	(615,511)	1,737,313	(96,239)	2,297,096
Loss on sale of investments			18,434		26,398
Finance charges	17		644,242		108,083
Equity in loss of associates, net (Refer Note 4, Schedule 19)	19(4)		47,968		51,908
Depreciation			1,616,859		1,255,982
			22,818,861		18,939,412
Profit before taxation and minority interest			2,013,354		138,532
Income tax	18		545,980		(180,920)
Profit before minority interest			1,467,374		319,452
Minority interest			(76)		9,664
Profit for the year			1,467,298		329,116
Balance in profit and loss account brought forward			366,548		539,686
Amount available for appropriation			1,833,846		868,802
Appropriations:					
Proposed dividend on equity shares		–	383,473	–	382,595
Tax on proposed dividend		–	53,782	–	53,659
Dividend of previous years (including tax)			114		–
Transfer to general reserve			211,124		66,000
Balance carried forward			1,185,353		366,548
			1,833,846		868,802
Earnings per share	19(8)				
Basic – Par value Rs.5 per share			19.17		4.30
Diluted – Par value Rs.5 per share			19.07		4.29
Significant accounting policies	19(1)				
Notes to consolidated accounts	19				

The schedules referred to above form an integral part of the Consolidated Profit and Losss Account

As per our report attached
for BSR & CO.
Chartered Accountants
SANJAY AGGARWAL PARTNER
Membership No.: 40780

HYDERABAD 31 MAY 2006

for DR. REDDY'S LABORATORIES LIMITED

DR. K ANJI REDDY CHAIRMAN
G V PRASAD VICE CHAIRMAN & CEO
K SATISH REDDY MANAGING DIRECTOR & COO
V S VASUDEVAN CHIEF FINANCIAL OFFICER
V VISWANATH COMPANY SECRETARY

schedules to the consolidated balance sheet

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006		As at 31 MARCH 2005	
SCHEDULE 1: SHARE CAPITAL				
Authorised				
100,000,000 (previous year: 100,000,000) equity shares of Rs.5 each		500,000		500,000
Issued				
76,694,770 (previous year: 76,519,149) equity shares of Rs.5 each fully paid-up		383,474		382,596
Subscribed and paid-up				
76,694,570 (previous year: 76,518,949) equity shares of Rs.5 each fully paid-up	383,472		382,594	
Add: Forfeited share capital (Note 2)	1		1	
		383,473		382,595
		383,473		**382,595**

NOTES:

1. Subscribed and paid-up share capital includes:

   (a) 34,974,400 (previous year: 34,974,400) equity shares of Rs.5 each fully paid-up, allotted as bonus shares by capitalisation of General reserve.

   (b) 526,124 (previous year: 526,124) equity shares of Rs.5 each allotted pursuant to a scheme of amalgamation with Standard Equity Fund Limited with out payments being received in cash.

   (c) 10,285,884 (previous year: 10,285,884) equity shares of Rs.5 each allotted and 82,800 (previous year: 82,800) equity shares of Rs.5 each extinguished pursuant to a scheme of amalgamation with erstwhile Cheminor Drugs Limited without payments being received in cash.

   (d) 13,225,000 (previous year: 13,225,000) equity shares of Rs.5 each allotted against American Depository Shares (ADS).

   (e) 8,602,152 (previous year: 8,602,152) equity shares of Rs.5 each allotted against Global Depository Receipts, that were converted into ADS during the year ended 31 March 2002.

   (f) 113,388 (previous year: 113,388) equity shares of Rs.5 each allotted to the erstwhile members of American Remedies Limited (ARL) pursuant to a scheme of amalgamation with ARL without payments being received in cash.

   (g) 178,622 (Previous year: Nil) equity shares of Rs.5 each allotted to the employees of the Company on exercise of the vested stock options in accordance with the terms of exercise under the "Dr. Reddy's Employees Stock Option Plan, 2002".

2. Represents 200 (previous year: 200) equity shares of Rs.5 each, amount paid-up Rs.500/-, forfeited due to non-payment of allotment money.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 2: RESERVES AND SURPLUS		
Capital reserve		
Balance as at the end of the year	13,769	13,769
	13,769	**13,769**
Securities premium account		
Balance at the beginning of the year	7,734,005	7,734,005
Add: Received during the year on exercise of stock options issued to employees	143,807	–
	7,877,812	**7,734,005**
Employee stock options outstanding		
Balance at the beginning of the year	275,402	564
Add: Options granted during the year (including grants issued in exchange of surrendered options)	155,600	277,949
Less: Options forfeited during the year	(98,900)	(3,111)
Less: Options excercised during the year	(71,049)	–
Balance at the end of the year (A)	**261,053**	**275,402**
Deferred stock compensation cost		
Balance at the beginning of the year	222,965	470
Add: Options granted during the year (including grants in exchange for surrendered options)	155,600	277,949
Less: Amortisation during the year, net of forfeiture	(133,073)	(52,343)
Less: Options forfeited during the year	(98,900)	(3,111)
Balance at the end of the year (B)	146,592	222,965
(A-B)	**114,461**	**52,437**
General reserve		
Balance at the beginning of the year	10,787,577	10,721,577
Add: Transferred from profit and loss account	211,124	66,000
	10,998,701	**10,787,577**
Foreign currency translation reserve		
Opening balance	80,823	57,321
Additions/(deductions) for the year	34,404	23,502
	115,227	**80,823**
Profit and loss account		
Balance in consolidated profit and loss account	1,185,353	366,548
	20,305,323	**19,035,159**

schedules to the consolidated balance sheet (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 3: SECURED LOANS		
Loans from banks		
Cash credit (Note 1)	–	1,664
Long term Euro loan (Note 2)	21,602,000	–
Short-term loan from State Bank of India (Note 3)	1,426,140	–
Others (Note 4 and 5)	92,632	71,834
Finance lease obligation (Note 6)	235,748	–
Loan from Indian Renewable Energy Development Agency Limited (Note 7)	25,145	31,065
	23,381,665	**104,563**

NOTES:

1. The Company has working capital facilities with a consortium of bankers and has created a charge, on a pari-passu basis, by hypothecation of the whole of the current assets, both present and future, and a first charge on immovable properties, pertaining to certain factories of the Company.
2. Long term Euro loan has been guaranteed by the Company and certain subsidiaries of the Group. This loan carries an interest rate of EURIBOR plus 150 basis points.
3. Short term loan from State Bank of India carrying an interest rate of 8.8% per annum is fully secured by way of pledge of fixed deposits.
4. Loan from the ICICI Bank taken by Aurigene Discovery Technologies Limited ("Aurigene") is secured by way of hypothecation of vehicles acquired by Aurigene. The loan carries an interest rate of 8.015%.
5. Loan from the Agricultural Bank of China taken by Kunshan Rotam Reddy Pharmaceutical Company Limited ("Reddy Kunshan"), a consolidated joint venture, is secured by way of hypothecation of leasehold land, buildings and equipment of Reddy Kunshan. This loan carries an interest rate of 5.742%.
6. Finance lease obligation represents present value of minimum lease rental payable for the building taken by the Group's subsidiary. (Refer note 15, Schedule 19).
7. Loan from Indian Renewable Energy Development Agency Limited is secured by way of hypothecation of specific movable assets pertaining to the Solar Grid Interactive Power plant. This loan carries an interest rate of 2% per annum.

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 4: UNSECURED LOANS		
Sales tax deferment loan from the Government of Andhra Pradesh (interest free)	70,980	74,942
Foreign currency packing credit loan (Note 1)	6,893,018	2,624,700
Bank Overdraft (Note 2)	823,412	–
	7,787,410	**2,699,642**

NOTES:

1. Foreign currency packing credit loan is from State Bank of India, HSBC, Citi Bank, Standard Chartered Bank, Bank of America and ABN Amro Bank carrying an interest of LIBOR plus 50 – 70 basis points, repayable on expiry of 6 months from date of drawdown.
2. Bank overdraft is on the current accounts with Citi Bank and HDFC, which carry an interest rate of 11% and 9% per annum respectively.

schedules to the consolidated balance sheet (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 5: FIXED ASSETS

	GROSS BLOCK						DEPRECIATION						NET BLOCK	
DESCRIPTION	AS AT 1 APRIL 2005	ADDITIONS	ADDITIONS ON ACQUISITION OF FALCON AND BETAPHARM [NOTE 5]	DELETIONS	FOREIGN EXCHANGE ADJUSTMENTS	AS AT 31 MARCH 2006	AS AT 1 APRIL 2005	FOR THE YEAR	ADDITIONS ON ACQUISITION OF FALCON AND BETAPHARM [NOTE 5]	DELETIONS	FOREIGN EXCHANGE ADJUSTMENTS	AS AT 31 MARCH 2006	AS AT 31 MARCH 2006	AS AT 31 MARCH 2005
Land – freehold (Note 1)	353,462	12,561	415,190	609	–	780,604	–	–	–	–	–	–	780,604	353,462
Land – leasehold (Note 2)	61,865	–	–	–	823	62,688	1,245	474	–	–	46	1,765	60,923	60,620
Buildings	2,082,374	169,050	152,534	139,009	424	2,265,373	326,796	97,350	1,674	9,953	(2,240)	413,627	1,851,746	1,755,578
Plant and machinery (Note 3)	4,734,185	683,039	343,407	471,692	(1,874)	5,287,065	2,302,952	563,972	213	306,416	(3,927)	2,556,794	2,730,271	2,431,233
Electrical equipment	706,041	67,022	–	124,909	–	648,154	338,930	70,680	–	103,802	–	305,808	342,346	367,111
Laboratory equipment	1,669,443	152,451	–	144,039	(981)	1,676,874	659,970	231,174	–	118,911	(1,099)	771,134	905,740	1,009,473
Furniture, fixtures and office equipment	891,233	102,657	226,886	77,109	(64)	1,143,603	531,095	154,819	1,02,004	65,032	(839)	722,047	421,556	360,138
Vehicles	231,693	79,957	12,127	39,114	119	284,782	91,238	48,893	378	20,584	(163)	119,762	165,020	140,455
Library	3,506	–	–	2,811	–	695	3,506	–	–	2,811	–	695	–	–
Intangibles														
Customer contracts	–	243,424	–	–	–	243,424	–	24,911	–	–	–	24,911	218,513	–
Goodwill (Note 4 and 5)	1,255,854	114,245	19,513,360	1,410	(24,936)	20,857,113	475,680	290,531	–	146	(10,654)	755,411	20,101,702	780,174
Patents, trademarks and designs	312,667	40,987	7,378,737	–	–	7,732,391	56,992	58,382	1,734,375	–	421	1,850,170	5,882,221	255,675
Technical know-how	522,310	–	–	–	–	522,310	282,804	52,231		–	–	335,035	187,275	239,506
Non-compete fees	227,500	–	–	–	–	227,500	182,000	22,750		–	–	204,750	22,750	45,500
	13,052,133	1,665,393	28,042,241	1,000,702	(26,489)	41,732,576	5,253,208	1,616,167	1,838,644	627,655	(18,455)	8,061,909	33,670,667	7,798,925
Assets taken on lease														
Buildings	–	–	280,195	–	–	280,195	–	692	32,997	–	–	33,689	246,506	–
TOTAL	**13,052,133**	**1,665,393**	**28,322,436**	**1,000,702**	**(26,489)**	**42,012,771**	**5,253,208**	**1,616,859**	**1,871,641**	**627,655**	**(18,455)**	**8,095,598**	**33,917,173**	**7,798,925**
Previous year	10,407,635	2,674,457		(95,042)	65,083	13,052,133	4,045,673	1,255,982		46,112	2,335	5,253,208	7,798,925	

NOTES:

1. Land located at Pydibheemavaram alloted by the Andhra Pradesh Industrial Infrastructure Corporation Limited having book value of Rs.7,893 (previous year: Rs.7,893) is yet to be registered in the name of the Company.
2. In pursuance of an allotment letter ("the letter") dated 16 October 2001, received from Karnataka Industrial Area Development Board, Aurigene Discovery Technologies Limited, a consolidated subsidiary, acquired land located at Electronics City, Bangalore, on a lease-cum-sale basis. In terms of the letter, the lease shall be converted into a sale at the end of six years subject to fulfillment of all the terms and conditions of the allotment. Pending completion of the period of six years and fulfillment of the terms and conditions of the allotment, the amount incurred on the land acquisition aggregating to Rs.49,729 (previous year: Rs.49,729) has been accounted as leasehold land.
3. The Company owns treated effluent discharge pipeline with the cost of Rs.9,257 (previous year: Rs.9,257) and net book value of Rs.2,551 (previous year: Rs.3,509) in equal proportion jointly with a third party in Pydibheemavaram pursuant to a mutual agreement.
4. For additions to goodwill, refer note 6 of Schedule 19.
5. The Company on 30 December 2005 acquired the entire share capital of Industrias Quimicas Falcon de Mexico, S.A.de.C.V. (Falcon) which has been fully described in Note 6a) of schedule 19. Further, on 3 March 2006 the Company also acquired the entire share capital of beta Holding GmbH, which has been fully described in note 6c) of Schedule 19.

schedules to the consolidated balance sheet (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
SCHEDULE 6: INVESTMENTS		
(Long term, unless otherwise specified)		
Investment in associates		
Aurantis Farmaceutica Ltda	–	85,099
Perlecan Pharma Private Ltd	66,464	–
APR LLC	–	13,632
Other investments (at cost)		
Aggregate cost of quoted investments	3,116	3,116
Aggregate cost of unquoted investments	1,320,922	1,070,923
Current Investments, at the lower of cost or market value		
Mutual funds	14,703	300,000
	1,405,205	1,472,770
Less: Provision for decline, other than temporary, in the value of investments	(67,957)	(153,056)
	1,337,248	**1,319,714**
Market value of quoted investments	11,636	7,903
Market value of current investments	14,703	310,886
SCHEDULE 7: INVENTORIES		
Stores and spares	428,381	317,421
Raw materials	2,334,552	1,025,844
Work-in-process	1,436,810	1,076,609
Finished goods	2,465,468	1,107,048
	6,665,211	**3,526,922**
SCHEDULE 8: SUNDRY DEBTORS		
(Unsecured)		
Debts outstanding for a period exceeding six months		
Considered good	98,733	159,890
Considered doubtful	261,251	248,399
Other debts		
Considered good	5,005,624	3,661,295
	5,365,608	4,069,584
Less: Provision for doubtful debts	(261,251)	(248,399)
	5,104,357	**3,821,185**
SCHEDULE 9: CASH AND BANK BALANCES		
Cash in hand	13,519	10,916
Balances with banks		
In current accounts	3,467,511	513,713
In EEFC current accounts	40,185	182,268
In deposit accounts	6,262,162	8,636,080
In unclaimed dividend accounts	12,110	11,307
In unclaimed fractional share pay order accounts	669	670
	9,796,156	**9,354,954**

schedules to the consolidated balance sheet (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
Deposits with banks include:		
(i) Margin money for letters of credit and bank guarantees	2,051	2,051
(ii) Balance of unutilised money out of ADS issue	–	1,754,141
(iii) Fixed deposits amounting to Rs.4,468,840 (previous year: Rs.Nil) have been pledged against a loan taken by the Company's subsidiary		
(iv) Short term loan from State Bank of India amounting to Rs.1,426,140 is fully secured by way of pledge of fixed deposits.		

SCHEDULE 10: LOANS AND ADVANCES

	As at 31 MARCH 2006	As at 31 MARCH 2005
(Unsecured)		
Considered good		
Advances to associate	234,541	–
Advances to material suppliers	359,950	116,564
Staff loans and advances	21,320	29,687
Interest accrued on investments	–	15,620
Other advances recoverable in cash or in kind or for value to be received	1,462,029	725,478
Advance tax, net of provision for current taxes	1,810,911	1,624,052
MAT credit entitlement	141,082	–
Balances with statutory authorities	791,893	181,944
Deposits	230,216	102,308
	5,051,942	2,795,653
Considered doubtful		
Share application money pending allotment in respect of Pathnet	–	15,310
Staff loans and advances	6,500	6,500
Other advances recoverable in cash or in kind or for value to be received	29,268	16,918
Advances towards investment	8,056	8,056
	5,095,766	2,842,437
Less: Provision for doubtful advances	(43,824)	(46,784)
	5,051,942	**2,795,653**

SCHEDULE 11: CURRENT LIABILITIES

Sundry creditors	8,459,112	4,750,012
Book overdraft	–	143,891
Interest accrued but not due on loan	15,162	
Unclaimed dividends	12,110	11,307
Trade deposits	41,241	42,258
	8,527,625	**4,947,468**

SCHEDULE 12: PROVISIONS

Proposed dividend	383,473	382,595
Tax on proposed dividend	53,782	53,659
Provision for		
Gratuity	1,036	83,122
Leave encashment	140,654	115,968
Pension, Seniority and Severence Indemnity Plan	33,395	–
Taxation, net of advances taxes	1,517,546	1,220,057
	2,129,886	**1,855,401**

schedules to the consolidated profit & loss account

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 13: OTHER INCOME

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
Interest on fixed deposits	581,038	264,679
Interest on investments	85,874	72,445
Interest others	26,433	36,777
Dividends from investments	29	98
Profit on sale of fixed assets, net	320,218	1,263
Income from redemption of mutual fund units	14,510	83,273
Sale of spent chemicals	101,589	85,014
Miscellaneous income	75,826	113,378
	1,205,517	**656,927**

NOTE: Fixed deposits and interest income are stated at gross values. The value of income tax deducted at source is Rs.153,622 (previous year: Rs.69,485)

SCHEDULE 14: MATERIAL COSTS

		For the year ended 31 MARCH 2006		For the year ended 31 MARCH 2005	
(a)	**Opening**				
	Work-in-process	1,076,609		989,865	
	Finished goods	1,107,048		857,326	
	Add: Stocks acquired on acquisition of Falcon and betapharm (Note 6 of Schedule 19)	1,296,336	3,479,993	–	1,847,191
	Closing				
	Work-in-process	1,436,810		1,076,609	
	Finished goods	2,465,468	3,902,278	1,107,048	2,183,657
	Net (increase)		(422,285)		(336,466)
(b)	**Raw materials consumed**				
	Opening stock of raw materials	1,025,844		911,867	
	Add: Stocks acquired on acquisition of Falcon and betapharm (Note 6 of Schedule 19)	191,521		–	
	Add: Purchases	6,681,553		3,893,944	
		7,898,918		4,805,811	
	Less: Closing stock	(2,334,552)	5,564,366	(1,025,844)	3,779,967
(c)	**Stores, chemicals, spares and packing material consumed**		769,943		706,455
(d)	**Purchase of traded goods**		2,252,610		1,864,935
			8,164,634		**6,014,891**

Raw materials consumed include Rs.15,646 (previous year: Rs.51,205) being stocks written-off/written-down, Rs.100,059 (previous year: Rs.69,366) being cost of samples issued and is net of Rs.390,541 (previous year: Rs.26,688) being sale of raw materials.

SCHEDULE 15: PERSONNEL COSTS

	For the year ended 31 MARCH 2006	for the year ended 31 MARCH 2005
Salaries, wages and bonus	2,842,537	2,458,729
Contribution to provident and other funds	181,692	149,974
Workmen and staff welfare expenses	338,035	277,283
Amortisation of deferred stock compensation cost	133,073	52,343
	3,495,337	**2,938,329**

schedules to the consolidated profit & loss account (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
SCHEDULE 16: OPERATING AND OTHER EXPENSES		
Power and fuel	535,316	436,629
Rent	173,271	183,517
Rates and taxes	122,362	117,508
Repairs and maintenance		
Buildings	22,373	29,837
Plant and machinery	239,162	231,123
Others	233,573	237,173
Insurance	194,481	242,521
Travelling and conveyance	329,690	298,140
Communication	105,983	106,857
Advertisements	64,755	30,607
Commission on sales	189,883	123,025
Carraige outwards	823,883	642,508
Other selling expenses	1,690,958	1,185,998
Printing and stationery	67,918	72,698
Legal and professional charges	890,399	996,509
Donations	60,039	87,761
Bad debts written off	27,349	44,618
Provision for doubtful advances	(2,960)	8,581
Provision for doubtful debts	12,852	(36,040)
Directors' sitting fees	360	392
Directors' remuneration	63,159	15,338
Auditors' remuneration	8,827	8,043
Bank charges	39,416	34,555
Exchange loss, net	144,862	537,292
Sundry expenses	465,475	269,779
	6,503,386	**5,904,969**
SCHEDULE 17: FINANCE CHARGES		
Interest on loan note in respect of acquisition of Dr. Reddy's Laboratories (EU) Limited	323	5,367
Interest on packing credit loan	175,477	37,064
Interest on long term Euro loan	76,409	–
Other finance charges	392,033	65,652
	644,242	**108,083**
SCHEDULE 18: INCOME TAX		
Current taxes		
Domestic taxes	279,536	249
MAT credit entitlement	(141,082)	–
Foreign taxes	34,080	1,070
	172,534	**1,319**
Deferred taxes		
Domestic taxes	319,275	(211,009)
Foreign taxes	(15,572)	28,770
Fringe benefit tax	69,743	–
	373,446	**(182,239)**
	545,980	**(180,920)**

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS

1. SIGNIFICANT ACCOUNTING POLICIES

a) Basis of preparation of consolidated financials statements

The consolidated financial statements have been prepared and presented under the historical cost convention on the accrual basis of accounting in accordance with the accounting principles generally accepted in India ("GAAP") and comply with the mandatory Accounting Standards ("AS") issued by the Institute of Chartered Accountants of India ("ICAI") to the extent applicable. The consolidated financial statements are presented in Indian rupees rounded off to the nearest thousand.

b) Use of estimates

The preparation of the consolidated financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities on the date of the consolidated financial statements and reported amounts of income and expenditure for the year. Actual results could differ from these estimates. Any revision to accounting estimates is recognised prospectively in the current and future periods.

c) Principles of consolidation

The consolidated financial statements include the financial statements of Dr. Reddy's Laboratories Limited ("Dr. Reddy's" or "the Company"), the parent company and all of its subsidiaries (collectively referred to as "the Group" or "Dr. Reddy's Group"), in which Dr. Reddy's has more than one-half of the voting power of an enterprise or where Dr. Reddy's controls the composition of the board of directors. In accordance with AS 27 – "Financial Reporting of Interes ts in Joint Ventures", issued by the ICAI, the Group has accounted for its proportionate share of interest in a joint venture by the proportionate consolidation method. The joint venture arrangement has been more fully described in Note 5 below.

The consolidated financial statements have been prepared on the following basis:

- The financial statements of the parent company and the subsidiaries have been combined on a line-by-line basis by adding together the book values of like items of assets, liabilities, income and expenses after eliminating intra-group balances / transactions and resulting unrealised profits in full. Unrealised losses resulting from intra-group transactions have also been eliminated except to the extent that recoverable value of related assets is lower than their cost to the group. The amounts shown in respect of reserves comprise the amount of the relevant reserves as per the balance sheet of the parent company and its share in the post-acquisition increase in the relevant reserves of the subsidiaries.

- The Group accounts for investments by the equity method of accounting where it is able to exercise significant influence over the operating and financial policies of the investee. Inter company profits and losses have been proportionately eliminated until realised by the investor or investee.

- Pursuant to the adoption of AS 27 "Financial Reporting of Interest in Joint Ventures" the Group does not consolidate entities where, regardless of the share of capital contributions, the minority shareholders have significant participating rights jointly with the Group, that provide for effective involvement in significant financial and operating decisions in the ordinary course of business.

- The proportionate share of Group's interest in Joint Ventures is combined on a line-by-line basis by adding together the book values of like items of assets, liabilities, income and expenses after eliminating intra-group transactions and resulting unrealised profits, to the extent it pertains to the group.

- The excess / deficit of cost to the parent company of its investment in the subsidiaries, joint ventures and associates over its portion of equity at the respective dates on which investment in such entities were made is recognised in the financial statements as goodwill / capital reserve. The parent company's portion of equity in such entities is determined on the basis of the book values of assets and liabilities as per the financial statements of such entities as on the date of investment and if not available, the financial statements for the immediately preceding period adjusted for the effects of significant transactions, up to the date of investment. Goodwill / capital reserve arising on the acquisition of an associate by the parent company is included in the carrying amount of investment in the associate but is disclosed separately.

- The consolidated financial statements are presented, to the extent possible, in the same format as that adopted by the parent company for its separate financial statements.

- The consolidated financial statements are prepared using uniform accounting policies for like transactions and other events in similar circumstances.

d) Fixed assets and depreciation

Fixed assets are carried at the cost of acquisition or construction, less accumulated depreciation. The cost of fixed assets includes taxes, duties, freight and other incidental expenses related to the acquisition and installation of the respective assets. Borrowing costs directly attributable to acquisition or construction of those fixed assets which necessarily take a substantial period of time to get ready for their intended use are capitalised. The cost of fixed assets also includes the exchange differences arising in respect of foreign currency loans or other liabilities incurred for the purpose of their acquisition or construction.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

Advances paid towards the acquisition of the fixed assets outstanding at each balance sheet date and the cost of fixed assets not ready for their intended use before such date are disclosed under capital work-in-progress. Pre-operative expenses directly attributable to fixed assets pending capitalisation are included under capital work-in-progress.

Depreciation on fixed assets is provided using the straight-line method based on the useful lives of the assets as estimated by Management. Depreciation is calculated on a pro-rata basis from the date of installation till the date the assets are sold or disposed off. Individual assets costing less than Rs. 5,000 are depreciated in full in the year of acquisition.

Management's estimates of the useful lives for various categories of fixed assets are given below:

	YEARS
Buildings	
– Factory and administrative buildings	20 to 30
– Ancillary structures	3 to 10
Plant and machinery	3 to 15
Electrical equipment	5 to 15
Laboratory equipment	5 to 15
Furniture, fixtures and office equipment (other than computer equipment)	4 to 8
Computer equipment	3
Vehicles	4 to 5
Library	2

Leasehold land is being amortised over the primary period of the lease.

e) Intangible assets and amortisation

Intangible assets are recorded at the consideration paid for acquisition. Intangible assets are amortised over their estimated useful lives on a straight-line basis, commencing from the date the asset is available to the Group for its use. The Management estimates the useful lives for the various intangible assets as follows:

	YEARS
Goodwill	5 to 20
Patents, trademarks and designs (including marketing know-how)	6 to 10
Customer contracts	2 to 5
Technical know-how	10
Non-compete fees	1.5 to 10

f) Investments

Long-term investments, other than investments in associates, are stated at cost. A provision for diminution is made to recognise a decline, other than temporary, in the value of long-term investments. Current investments are carried at the lower of cost and fair value. The comparison of cost and fair value is done separately in respect of each category of investment.

Investments in associates, accounted under the equity method of accounting, are initially recorded at cost, identifying any goodwill / capital reserve at the time of acquisition. The carrying amount of such investments is adjusted thereafter for the post acquisition change in the Group's share of net assets of the investee unless there is an agreement to the contrary. The carrying amount of investment in an associate is reduced to recognise a decline, other than temporary, in the value of the investment, such reduction being determined and made for each investment individually.

g) Inventories

Inventories are valued at the lower of cost and net realisable value. Cost of inventories comprises all costs of purchase, cost of conversion and other costs incurred in bringing the inventories to their present location and condition.

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

The methods of determining cost of various categories of inventories are as follows:

Raw materials	First in first out (FIFO)
Stores and spares	Weighted average method
Work-in-process and finished goods (manufactured)	FIFO and including an appropriate share of production overheads
Finished goods (traded)	Actual cost of purchase
Goods in transit	Actual cost of purchase

h) Research and development

Revenue expenditure on research and development is expensed as incurred. Capital expenditure incurred on research and development is capitalised as fixed assets and depreciated in accordance with the depreciation policy of the Group.

i) Retirement benefits

Contributions payable to an approved gratuity fund (a defined benefit plan), and certain defined benefit plans at overseas subsidiaries determined by independent actuaries at the balance sheet date, are charged to the profit and loss account. Leave encashment cost which is a defined benefit, is accrued based on an actuarial valuation at the balance sheet date, carried out by an independent actuary.

Contributions payable to recognised provident funds, approved superannuation scheme and employee pension and social security schemes in certain overseas subsidiaries, which are defined contribution schemes, are charged to the profit and loss account.

j) Foreign currency transactions, balances and translation of financial statements of foreign subsidiaries and joint venture

Foreign currency transactions are recorded using the exchange rates prevailing on the dates of the respective transactions. Exchange differences arising on foreign currency transactions settled during the year are recognised in the profit and loss account except that exchange differences related to acquisition of fixed assets are adjusted in the carrying amount of the related fixed assets.

Monetary assets and liabilities denominated in foreign currencies as at the balance sheet date not covered by forward exchange contracts are translated at year-end rates. The resultant exchange differences (except those related to acquisition of fixed assets) are recognised in the profit and loss account. Non-monetary assets are recorded at the rates prevailing on the date of the transaction.

Forward contracts are entered into to hedge the foreign currency risk of the underlying outstanding at the balance sheet date. The premium or discount on all such contracts arising at the inception of each contract is amortised as expense or income over the life of the contract. Any profit or loss arising on the cancellation or renewal of forward contracts is recognised as income or expense for the period.

In relation to the forward contracts entered into to hedge the foreign currency risk of the underlying outstanding at the balance sheet date, the exchange difference is calculated and recorded in accordance with paragraphs 36 and 37 of AS – 11 (revised). The exchange difference on such a forward exchange contract is calculated as the difference the foreign currency amount of the contract translated at the exchange at the reporting date, or the settlement date where the transaction is settled during the reporting period, and the corresponding foreign currency amount translated at the later of the date of inception of the forward exchange contract and the last reporting date. Such exchange differences are recognized in the profit and loss account in the reporting period in which the exchange rates change.

The financial statements of the foreign integral subsidiaries, representative offices and (collectively referred to as the 'foreign integral operations') are translated into Indian rupees as follows:

- Revenue items, except opening and closing inventories and depreciation are translated at the respective monthly average rates. Opening and closing inventories are translated at the rates prevalent at the commencement and close respectively of the accounting period. Depreciation is translated at the rates used for the translation of the values of the assets on which depreciation is calculated.
- Monetary items are translated using the closing rate.
- Non-monetary items, other than inventories and fixed assets, are translated using the exchange rate at the date of transaction i.e., the date when they were acquired.
- Fixed assets are translated using the exchange rate at the date of their acquisition. Where there has been an increase or decrease in the liability of the Group, as expressed in Indian rupees by applying the closing rate, for making payment towards the whole or a part of the cost of a fixed asset or for repayment of the whole or a part of the monies borrowed, in foreign currency specifically for the purpose of acquiring a fixed asset, the amount by which the liability is so increased or reduced during the year, is added to, or reduced from, the cost of the fixed asset concerned.
- The net exchange difference resulting from the translation of items in the financial statements of foreign integral operations is recognised as income or as expense for the year, except to the extent adjusted in the carrying amount of the related fixed assets as stated above.
- Contingent liabilities are translated at the closing rate.

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

- The consolidated foreign subsidiaries Reddy US, DREU, DRUK, AI, Falcon, Lacock, RHG, Beta group and joint venture KRRP have been identified as non integral operations in accordance with the requirements of AS –11 (Revised 2003) "The Effect of Changes in Foreign Exchange rates" issued by ICAI which is effective for the accounting periods commencing on or after 1 April 2004. In accordance with AS –11 (Revised 2003) "The Effect of Changes in Foreign Exchange rates", the financial statements of non-integral foreign operations are translated into Indian rupees as follows:
- All assets and liabilities, both monetary and non-monetary, are translated using the closing rate.
- Revenue items are translated at the respective monthly average rates.
- The resulting net exchange difference is credited or debited to a foreign currency translation reserve. However, an exchange difference arising out of intragroup monetary item, whether short term or long term is recognised in the profit and loss account.
- Contingent liabilities are translated at the closing rate.

k) Revenue recognition

Revenue from sale of goods is recognised when significant risks and rewards in respect of ownership of products are transferred to customers. Revenue from domestic sales of formulation products is recognised on dispatch of products to stockists by clearing and forwarding agents of the Group. Revenue from domestic sales of active pharmaceutical ingredients and intermediates is recognised on dispatch of products from the factories of the Group. Revenue from export sales is recognised on shipment of products.

Revenue from product sales is stated exclusive of returns, sales tax and applicable trade discounts and allowances.

Service income is recognised as per the terms of contracts with customers when the related services are performed, or the agreed milestones are achieved.

Dividend income is recognised when the unconditional right to receive the income is established. Income from interest on deposits, loans and interest bearing securities is recognised on the time proportionate method.

Export entitlements under the Duty Entitlement Pass Book ("DEPB") scheme are recognised as income when the right to receive credit as per the terms of the scheme is established in respect of the exports made and where there is no significant uncertainty regarding the ultimate collection of the relevant export proceeds.

The Group has entered into marketing arrangements with certain marketing partners for sale of goods in certain overseas territories. Under such arrangements, the Group sells generic products to the marketing partners at a price agreed in the arrangement. Revenue is recognized on these transactions upon delivery of products to the marketing partners. An additional amount representing profit share is recognised as revenue on the basis of ultimate net sale proceeds realised by such marketing partners from the end customer. Such amount is determined as per the terms of the arrangment and recognised by the Group when the realisation is certain.

The Group enters into certain dossier sales, licensing and supply arrangements with certain third parties. These arrangements include certain performance obligations by the Group. Revenue from such arrangements is recognised in the period in which the Group completes all its performance obligations.

l) Income-tax expense

Income tax expense comprises current tax and deferred tax charge or credit.

Current tax

The current charge for income taxes is calculated in accordance with the relevant tax regulations applicable to the entities in the Group.

Deferred tax

Deferred tax charge or credit reflects the tax effects of timing differences between accounting income and taxable income for the period. The deferred tax charge or credit and the corresponding deferred tax liabilities or assets are recognised using the tax rates that have been enacted or substantially enacted by the balance sheet date. Deferred tax assets are recognised only to the extent there is reasonable certainty that the assets can be realised in future; however, where there is unabsorbed depreciation or carry forward of losses, deferred tax assets are recognised only if there is a virtual certainty of realisation of such assets. Deferred tax assets are reviewed at each balance sheet date and written-down or written-up to reflect the amount that is reasonably / virtually certain (as the case may be) to be realised.

The break-up of the major components of the deferred tax assets and liabilities as at the balance sheet date have been arrived at after setting off deferred tax assets and liabilities where the Group has a legally enforceable right to set-off assets against liabilities, and where such assets and liabilities relate to taxes on income levied by the same governing taxation laws.

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

m) Earnings per share

The basic earnings per share ("EPS") is computed by dividing the net profit after tax for the year by the weighted average number of equity shares outstanding during the year. For the purpose of calculating diluted earnings per share, net profit after tax for the year and the weighted average number of shares outstanding during the year are adjusted for the effects of all dilutive potential equity shares. Dilutive potential equity shares are deemed converted as of the beginning of the year, unless they have been issued at a later date. The diluted potential equity shares have been adjusted for the proceeds receivable had the shares been actually issued at fair value (i.e. the average market value of the outstanding shares).

n) Employee stock option schemes

In accordance with the Securities and Exchange Board of India guidelines, the excess of the market price of shares, at the date of grant of options under the Employee stock option schemes, over the exercise price is treated as employee compensation and amortised over the vesting period.

o) Impairment of assets

The Group assesses at each balance sheet date whether there is any indication that an asset may be impaired. If any such indication exists, the Group estimates the recoverable amount of the asset. If such recoverable amount of the asset or the recoverable amount of the cash generating unit to which the asset belongs is less than its carrying amount, the carrying amount is reduced to its recoverable amount. The reduction is treated as an impairment loss and is recognised in the profit and loss account. If at the balance sheet date there is an indication that if a previously assessed impairment loss no longer exists, the recoverable amount is reassessed and the asset is reflected at the recoverable amount subject to a maximum of depreciated historical cost.

p) Provisions and contingent liabilities

The Group creates a provision when there is a present obligation as a result of a past event that probably requires an outflow of resources and a reliable estimate can be made of the amount of the obligation. A disclosure for a contingent liability is made when there is a possible obligation or a present obligation that may, but probably will not, require an outflow of resources. Where there is possible obligation or a present obligation in respect of which the likelihood of outflow of resources is remote, no provision or disclosure is made.

q) Leases

Assets taken on lease where the Group acquires substantially the entire risks and rewards incidental to ownership are classified as finance leases. The amount recorded is the lesser of the present value of the minimum lease rental and other incidental expenses during the lease term or the asset's fair value. The rental obligations, net of interest charges, are reflected in secured loan.

Leases that do not transfer substantially all of the risks and rewards of ownership are classified as operating leases and recorded as expenses as and when payments are made over the lease term.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

2. DESCRIPTION OF THE GROUP

Dr. Reddy's Laboratories Limited ("Dr. Reddy's" or "the Company") together with its subsidiaries (collectively referred to as "the Group" or "Dr. Reddy's Group") is a leading India-based pharmaceutical group headquartered in Hyderabad, India. The Group's principal areas of operation are formulations, active pharmaceutical ingredients and intermediates, generics, critical care and biotechnology, custom pharmaceutical services and drug discovery. The Group's principal research and development and manufacturing facilities are located in Andhra Pradesh, India with principal marketing facilities in India, Russia, the United States, the United Kingdom, Brazil, Germany and South Africa. The Company's shares trade on several stock exchanges in India and on the New York Stock Exchange in the United States from April 11, 2001.

DRL's subsidiaries, step-down subsidiaries, associates and joint venture are listed below:

	COUNTRY OF INCORPORATION	PERCENTAGE HOLDING (%)
Subsidiaries		
OOO JV Reddy Biomed Limited ("RBL")	A Company organised under the laws of Russia	10
Reddy Pharmaceuticals Hong Kong Limited	A Company organised under the laws of Hong Kong	100
Dr. Reddy's Laboratories Inc. ("DRLI")	A Company organised under the laws of New Jersey, USA	100
Reddy Cheminor S.A.	A Company organised under the laws of Chartres, France	100
Reddy Antilles N.V. ("RANV")	A Company organised under the laws of Antilles, Netherlands	100
Dr. Reddy's Farmaceutica Do Brazil Ltda.	A Company organised under the laws of Brazil	100
Aurigene Discovery Technologies Limited	A Company organised under the laws of India	100
Dr. Reddy's Laboratories (EU) Limited ("DREU")	A Company organised under the laws of the United Kingdom	100
Cheminor Investments Limited	A Company organised under the laws of India	100
DRL Investments Limited	A Company organised under the laws of India	100
OOO Dr. Reddy's Laboratories Limited	A Company organised under the laws of Russia	100
Dr. Reddy's Laboratories (Proprietary) Limited	A Company organised under the laws of the Republic of South Africa	60
Dr. Reddy's Bio-Sciences Limited	A Company organised under the laws of India	100
Trigenesis Therapeutics Inc.	A Company organised under laws of New Jersey, USA	100
Industrias Quimicas Falcon de Mexico S.A. de.C.V. ("Falcon")	A Company organised under laws of Mexico	100
Lacock Holdings Limited	A Company organised under laws of Cyprus	100
Step-down subsidiaries		
Reddy Netherlands B.V.	A subsidiary of Reddy Antilles N.V., organised under the laws of Netherlands	100
Reddy US Therapeutics Inc. ("Reddy US")	A subsidiary of Reddy Antilles N.V., organised under the laws of Atlanta, USA	100
Reddy Pharmaceuticals Inc.	A subsidiary of Dr. Reddy's Laboratories Inc., organised under the laws of Delaware, USA	100
Dr. Reddy's Laboratories (UK) Limited ("DRUK")	A subsidiary of Dr. Reddy's Laboratories (EU) Limited, organised under the laws of the United Kingdom	100
Aurigene Discovery Technologies Inc ("AI").	A subsidiary of Aurigene Discovery Technologies Limited, organised under the laws of Massachusetts, USA	100
Reddy Holding GmbH ("RHG")	A subsidiary of Lacock Holdings Limited organised under the laws of Germany	100
beta Holding GmbH	A subsidiary of Reddy Holding GmbH organised under the laws of Germany	100
beta Healthcare Verwaltungs GmbH	A subsidiary of beta Healthcare GmbH & Co. KG organised under the laws of Germany	100
betapharm Arzneimittel GmbH	A subsidiary of beta Healthcare GmbH & Co. KG organised under the laws of Germany	100
beta Healthcare Solutions GmbH	A subsidiary of beta Healthcare GmbH & Co. KG organised under the laws of Germany	100
beta Institut GmbH	A subsidiary of beta Healthcare GmbH & Co. KG organised under the laws of Germany	100

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

	COUNTRY OF INCORPORATION	PERCENTAGE HOLDING (%)
Partnership firms		
Globe Enterprises	A partnership from with Dr. Reddy's Holding Private Limited organised under the laws of India, wherein DRL and Dr. Reddy's Holdings Private Limited share the profits in the ratio of 95:5	95
beta Healthcare GmbH & Co.KG	A partnership firm organised under the laws of Germany	100
Joint Venture		
Kunshan Rotam Reddy Pharmaceutical Company Limited ("Reddy Kunshan" or KRRP)	A Company organised under the laws of China	51.2
Associates		
Pathnet India Private Limited ("Pathnet")	A Company organised under the laws of India, (Disposed during the year)	49
Aurantis Farmaceutica Ltda ("Aurantis")	A Company organised under the laws of Brazil, (Liquidated during the year)	50
Dr. Reddy's Exports Limited	A Company organised under the laws of India, (Liquidated during the year)	22
APR LLC	A Limited Liability Company (LLC) oranised under the laws of Delaware, USA	100 of Class B interest in the LLC
Perlecan Pharma Private Limited	A Company organised under the laws of India	14.28

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

3. COMMITMENTS AND CONTINGENT LIABILITIES

			As at 31 MARCH 2006	As at 31 MARCH 2005
(i)		Commitments / contingent liabilities:		
	(a)	Guarantees issued by banks	61,835	106,432
	(b)	Guarantees issued by the Company on behalf of its subsidiaries, joint venture and associates	22,397,602	942,661
	(c)	Letters of credit outstanding	224,484	183,914
	(d)	Contingent consideration payable in respect of subsidiaries acquired	12,463	84,662
	(e)	Bonds executed in favour of customs and excise authorities by a subsidiary	–	445,078
(ii)		Claims against the Group not acknowledged as debts in respect of:		
	(a)	Income tax matters, pending decisions on various appeals made by the Group and by the Department	468,730	272,382
	(b)	Excise matters, under dispute	483,089	478,928
	(c)	Sales tax matters, under dispute	15,877	5,513
	(d)	Customs matter under dispute	34,511	–
	(e)	Other matters, under dispute	9,457	950
	(f)	Commitment towards research funding to third party	–	34,470

(g) Demand for payment to the credit of the Drug Prices Equalisation Account under Drugs (Price Control) Order,1995 which is being contested by the Company in respect of its product "Norfloxacin". During the previous year, the Hon'ble High Court of Andhra Pradesh dismissed the review petition filed by the Company against the original order passed by the same Court. Subsequently, the Company had filed a Special Leave Petition with the Supreme Court of India appealing against the High Court Order.

During the year ended 31 March 2006 the Company received a further demand notice from the authorities for a total of Rs.284,984 towards the overcharged sale price (principal) and interest thereon. The Company filed a fresh writ petition in the High Court of Andhra Pradesh challenging the demand notice. The High Court whilst admitting the writ petition, granted an interim order wherein it ordered the Company to deposit 50% of the principal amounting to Rs.77,149. The Company deposited this amount with the authorities under protest on 14 November 2005, whilst it awaits the outcome of its appeal with the Supreme Court. The Company has provided fully against the potential liability in respect of the principal amount demanded in earlier years. However, based on an external legal opinion, the Company believes that no interest can be levied on such a demand and hence department's contention is not tenable. In the event the Company is unsuccessful in its appeal with the Supreme Court, there could be penalties and interest, the amount of which cannot be ascertained at this stage

(h) The Employee Provident Fund Organisation (EPFO) has on 9 September 2005 issued a clarification as per which provident fund contributions should be deducted on leave encashment from 1 May 2005 onwards. It has also been stated that the claims between 1 October 1994 and 30 April 2005 should be kept in abeyance till this matter is decided by the Central Board of Trustees. Based on this notification, the Group has deducted and paid provident fund on leave encashment for the period from May 2005. However, the Group is in the process of quantifying the liability with respect to the period 1 October 1994 till 30 April 2005, which it believes would not be material.

		As at 31 MARCH 2006	As at 31 MARCH 2005
(iii)	Estimated amount of contracts remaining to be executed on capital account and not provided for (net of advances)	744,068	193,398

(iv) The Group is also involved in other lawsuits, claims, investigations and proceedings, including patent and commercial matters, which arise in the ordinary course of business. However, there are no such matters pending that the Group expects to be material in relation to its business.

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

4. ACCOUNTING FOR ASSOCIATES

Pursuant to the adoption of AS 23 – "Accounting for Investments in Associates in Consolidated Financial Statements", the Group has accounted for its investments in Pathnet India Private Limited, Aurantis Farmaceutica Ltda, APR LLC and Perlecan Pharma Private Limited (part of the year) under the equity method, as the Group exercises significant influence over the financial and operating policy decisions of these entities.

Perlecan Pharma Private Limited ("Perlecan Pharma")

The Group, during the year invested Rs 100,800 in Perlecan Pharma for an equity stake of 14.28%. As more fully described in Note 13 of Schedule 19, the Company as per the terms of the agreement will have 3 out of the 7 directors on the Board of Perlecan Pharma and will have continuing involvement in the operations of Perlecan Pharma. The Group has therefore concluded that it has a significant influence in the financial and operating policies of Perlecan Pharma and has accounted for its investment in Perlecan Pharma under the equity method. The Group's losses of Perlecan Pharma amounting to Rs.34,336 has been recognised in these financial statements.

Pathnet India Private Limited ("Pathnet")

The Group, in earlier years acquired a 49% interest in Pathnet for a consideration of Rs.64,310. Pathnet is engaged in the business of setting up of medical pathology laboratories. The carrying value of the Group's investement in Pathnet had been reduced to Rs.Nil through loss pick ups in prior years. The Group during the year sold its entire equity stake in Pathnet.

APR LLC (''APR")

On 30 January 2004, the Group invested Rs.21,859 in the Class B Interest of APR. APR is a development stage Company in the process of developing an active pharmaceutical ingredient. In accordance with a Development and Supply Agreement between the Group and APR, the Group has agreed to fund APR's development expenses, provided certain milestones are achieved. Such funding is repayable by APR upon successful commercialisation of the product in the future. In addition to its equity investment of Rs.21,859 the Group has advanced Rs.78,500 to APR through 31 March 2005.

During the current year, the balance carrying value of the investment and advance amounting to Rs 13,632 has been adjusted against the Group's share of losses thereby reducing the Group's investment in APR to Rs.Nil at 31 March 2006.

Aurantis Farmaceutica Ltda ("Aurantis")

During the financial year ended 31 March 2002, the Group discontinued its association with Aurantis. The operations of this entity are being phased out and the Group does not expect to recover the carrying amount of its investment in Aurantis. Accordingly, during the financial year ended 31 March 2002, the Group had provided for the carrying value of the entire investment of Rs. 85,099 thousands to recognise this other than temporary diminution in value. During the current year, this company has been liquidated and accordingly this investment has been entirely written off.

5. ACCOUNTING FOR INTEREST IN A JOINT VENTURE (JV)

Kunshan Rotam Reddy Pharmaceuticals Company Limited ("Reddy Kunshan")

The Company has a 51.2 % interest in Reddy Kunshan, a joint venture (JV) in China. Reddy Kunshan is engaged in manufacturing and marketing of active pharmaceutical ingredients and intermediates and formulations in China. The contractual arrangement between shareholders of Reddy Kunshan indicates joint control as the minority shareholders, along with the Group, have significant participating rights such that they jointly control the financial and operating policies of Reddy Kunshan in the ordinary course of business.

The Group has, in accordance with AS 27 – "Financial Reporting of Interests in Joint Ventures" issued by the ICAI, accounted for its 51.2 % interest in the JV by the proportionate consolidation method. Thus the Group's income statement, balance sheet and cash flow statement incorporate the Group's share of income, expenses, assets, liabilities and cash flows of the JV on a line-by-line basis.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

The aggregate amount of the assets, liabilities, income and expenses related to the Group's share in the JV included in these financial statements as of and for the year ended 31 March 2006 are given below:

PARTICULARS	As at 31 March 2006	As at 31 March 2005
Balance Sheet		
Secured loan	91,315	69,859
Unsecured loan	105,751	94,603
Foreign currency translation reserve	358	4,058
Fixed assets, net	90,385	91,892
Deferred tax assets, net	–	9,277
Current assets, loans and advances		
Inventories	37,425	35,403
Sundry debtors	45,096	40,921
Cash and bank balances	8,947	10,389
Loans and advances	11,062	8,608
Current liabilities and provisions		
Current liabilities	35,839	12,606
Net current assets	66,691	82,715
Estimated amount of contracts remaining to be executed on capital account and not provided for (net of advances)	62	1,237

PARTICULARS	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
Income statement		
Income		
Sales	194,805	146,244
Other income	4,985	–
Expenditure		
Material costs	95,450	67,679
Personnel costs	51,227	46,432
Operating and other expenses	79,548	76,002
Research and development expenses	4,331	7,513
Finance charges	7,289	4,700
Depreciation	11,189	4,806
Loss before taxation	(49,244)	(60,888)
Provision for taxation		
– Current tax	–	–
– Deferred tax (expense) / benefit	(9,810)	4,449
Loss after taxation	(59,054)	(56,439)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

6. ACQUISITIONS

a) Industrias Quimicas Falcon de Mexico S.A.de.C.V. ("Falcon")

On 30 December 2005 the Group acquired the entire share capital of Falcon a Roche group company for a total purchase consideration of Rs.2,320,246. Additionally, the Company has paid Rs.243,424 for acquisition of customer relationships which has been accounted as an intangible asset.

Falcon was acquired with an intent to add unique steroid manufacturing capabilities and to emerge as a partner of choice with innovator companies across the globe with service offerings spanning the entire value chain of pharmaceutical services.

The total purchase consideration has been allocated to acquired assets and liabilites at book values on the date of acquisition as follows:

Fixed assets net of accumulated depreciation (includes Capital Work In Progress Rs 46,324)	967,610
Current assets	1,249,458
Goodwill	115,164
Total assets	**2,332,232**
Less: Current liabilities	11,986
Purchase consideration	**2,320,246**

b) Brands from PDL Pharma

On 13 March 2006, the Company acquired three trademarks along with all the physical inventories of the related products from PDL Biopharm, Inc (PDL) for a total consideration of Rs 122,691.

PDL is a U.S. based fully integrated biopharmaceutical company focused in the development and commercialization of novel therapies for treatment of inflammation and autoimmune diseases, acute cardiac conditions and cancer. As a result of the acquisition, the company has got an opportunity to continue selling these products through generics sales and marketing organization and leverage the NDA filing.

The total purchase consideration has been allocated to the acquired assets as of March 31, 2006 as follows:

Inventory	115,845
Acquired intangibles	6,846
Purchase consideration	**122,691**

The values attributable to the brands are amortized over the period over which the intangible assets are expected to contribute directly or indirectly to the future cash flows.

c) beta Holding GmbH

On 3 March 2006, the Company, through its wholly owned subsidiary Reddy Holding GmbH, acquired 100% of the outstanding common shares of beta Holding GmbH. betapharm is a leading generics pharmaceuticals company in Germany. Under the 'beta' brand, the Company markets a broad and diversified portfolio comprising 140 drugs incorporating a broad range of formulations, primarily solid dose, focused on medical conditions requiring long-term therapy that are typically prescribed by primary care physicians. The strategic investment in betapharm is a step towards realising the Company's intention of building a global generics business in key European markets.

The aggregate purchase price of Rs.26,063,321 including the direct acquisition cost of Rs.201,548 was paid in cash. The agreement included the payment of a contingent consideration amounting up to Rs.518,400 which was paid into an escrow account. This amount is subject to set-off for certain indemnity claims in respect of legal and tax matters that might arise, pertaining to the periods prior to the acquisition. The escrow will lapse and be time barred at the end of the year 2013. Since the maximum amounts pertaining to such claims are determinable at the date of acquisition, the same has been included as part of the purchase price.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

The total purchase consideration has been allocated to acquired assets and liabilites at book values on the date of acquisition as follows:

Fixed assets net of accumulated depreciation (includes Capital Work in Progress of Rs.595)	372,382
Current assets	3,212,791
Intangibles	5,644,362
Goodwill	19,398,196
Total assets	**28,627,731**
Less: Current liabilities	2,082,269
Less: Finance lease obligation	239,447
Loss: Deferred tax liability	242,694
Purchase consideration	**26,063,321**

d) Trigenesis Therapeutics Inc.

On 27 April 2004 the Group acquired the entire share capital of Trigenesis Therapeutics Inc. (“Trigenesis”) for a total consideration of Rs.496,715 (U.S.$11 million). Trigenesis is a US based research company specializing in dermatology field. As a result of the acquisition, the Group acquired certain technology platforms and marketing rights.

The total purchase consideration has been allocated as follows:

Patents, trademarks and licenses	228,037
Goodwill	268,678
Purchase consideration	**496,715**

e) Dr. Reddy’s Laboratories (EU) Limited (DREU)

On 11 April 2002, DRL acquired the entire share capital of DREU and its consolidated subsidiary Dr. Reddy’s Laboratories (UK) Limited (“DRUK”) for a total consideration of Rs.644,413 (UK Pound Sterling 9.16 million). The purchase consideration consisted of:

Cash	438,216
Loan notes	128,108
Direct acquisition cost	7,739
	574,063
Contingent consideration	70,350
Purchase consideration	**644,413**

At the date of acquisition, the Group has recorded the cost of acquisition as Rs. 574,063 consisting of the cash paid, loan notes issued, and the direct acquisition cost. Contingent consideration amounting to Rs. 70,350 was held in an escrow account which was subject to set-off for indemnity claims in respect of tax and legal matters that might be made by the Group. Therefore, this amount was not included in the determination of cost of acquisition initially, but was to be included as purchase consideration upon expiration of the escrow period in 2007. As per the agreement, during the year, the balance of the escrow amount of Rs.81,133 was paid to the sellers on resolution of the contingency.

f) Dr. Reddy’s Laboratories Inc. (DRLI)

In March 2000, DRLI, a consolidated subsidiary, acquired 25% of its common stock held by a minority shareholder, for a cash consideration of Rs.1,072. This acquisition has resulted in goodwill of Rs.1,072. The terms of the purchase also provide for contingent consideration not exceeding U.S.$14 million over the next ten years payable to the minority shareholders based on achievement of certain specified targets. Such payments would be recorded as goodwill in the periods in which the contingency is resolved. During the year ended 31 March 2006, as certain specified targets have been met, DRLI has paid/accrued Rs.33,112 (U.S.$0.75 million) [previous year Rs.38,950 (U.S.$0.88 million)] which has been recorded as goodwill.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

7. DEFERRED TAXATION

	As at 31 MARCH 2006	As at 31 MARCH 2005
Deferred tax assets		
Losses carried forward	–	338,422
Sundry debtors	62,520	66,482
Provisions	95,603	114,807
Inventories	–	745
Other current assets	18,018	9,500
Current liabilities	–	2,952
	176,141	532,908
Deferred tax liability		
Inventories	(10,765)	–
Current liabilities	(220,487)	–
Excess of depreciation allowable under Income tax law over depreciation provided in accounts	(699,796)	(741,465)
Deferred tax liability, net	**(754,907)**	**(208,557)**

The net deferred tax liability of Rs.754,907 thousands (previous year: Rs. 208,557 thousands) has been presented in the balance sheet as follows:

	As at 31 MARCH 2006	As at 31 MARCH 2005
Deferred tax assets	26,584	9,615
Deferred tax liabilities	(781,491)	(218,172)
	(754,907)	**(208,557)**

[Refer Note 1(l) to Schedule 19]

8. EARNINGS PER SHARE (EPS)

The computation of EPS is set out below:

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
Earnings		
Net profit for the year	1,467,298	329,116
Shares		
Number of shares at the beginning of the year	76,518,949	76,518,949
Add: No of equity shares issued on exercise of vested stock options	175,621	–
Total number of equity shares outstanding at the end of the year	76,694,570	76,518,949
Weighted average number of equity shares outstanding during the year – Basic	76,546,658	76,518,949
Add: Weighted average number of equity shares arising out of outstanding stock options (net of stock options forfeited) that have dilutive effect on EPS	386,138	175,964
Weighted average number of equity shares outstanding during the year – Diluted	76,932,796	76,694,913
Earnings per share of face value Rs.5-Basic (Rs.)	19.17	4.30
Earnings per share of face value Rs.5-Diluted (Rs.)	19.07	4.29

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

9. RELATED PARTY DISCLOSURES

a. The related parties where control exists, are the subsidiaries, step down subsidiaries and partnership firms as described in Note 2. There are no otherparties over which the Group has control.

b. Other related parties with whom transactions have taken place during the year:

Associates

■ Pathnet India Private Limited, India	Enterprise over which the Group has significant influence, through 49% shareholding. (Equity shares in this Company were sold during the year)
■ Aurantis Farmaceutica Ltda, Brazil	Enterprise over which the Group has significant influence, through 50% shareholding. (Company liquidated during the year)
■ Dr. Reddy's Exports Limited, India	Enterprise over which the Group has significant influence, through 22% shareholding. (Company liquidated during the year)
■ APR LLC, USA	Enterprise over which the Group has significant influence, through 100% of Class B interest.
■ Perlecan Pharma Private Limited, India	Enterprise over which the Group has significant influence, through 14.28% shareholding and through representation on Board of Directors of the Company.

Joint Venture

Kunshan Rotam Reddy Pharmaceutical Company Limited – China (" Reddy Kunshan" or KRRP)	Enterprise over which the group exercises joint control with other joint venture partners and holds 51.2% equity stake.

Enterprises where principal shareholders have control or significant influence ("Significant interest entities")

■ Dr. Reddy's Research Foundation ("Research Foundation")	Enterprise over which the principal shareholders have significant influence
■ Dr. Reddy's Holdings Private Limited	Enterprise owned by principal shareholders

Others

■ Diana Hotels Limited	Enterprise owned by relative of a director
■ Ms K Samrajyam	Spouse of the Chairman
■ Ms G Anuradha	Spouse of the Vice-Chairman and Chief Executive Officer
■ Ms Deepti Reddy	Spouse of the Managing Director and Chief Operating Officer
■ Madras Diabetes Research Foundation	Enterprise promoted by a director
■ Dr. Reddy's Heritage Foundation	Enterprise in which the Chairman is a director
■ Dr. Reddy's Foundation for Human and Social development	Enterprise where principal shareholders are trustees
■ Manava Seva Dharma Samvardhani Trust	Trust in which a director is a Managing trustee

Key management personnel represented on the board of the Company

■ Dr. K Anji Reddy	Chairman
■ Mr G V Prasad	Vice-Chairman and Chief Executive Officer
■ Mr K Satish Reddy	Managing Director and Chief Operating Officer

Non-executive and independent directors on the board of the Company

- Mr Anupam Puri
- Dr. Krishna G Palepu
- Dr. Omkar Goswami
- Mr P N Devarajan
- Mr Ravi Bhoothalingam
- Dr. V Mohan

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

c. Particulars of related party transactions
The following is a summary of significant related party transactions:

PARTICULARS	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
i. Sales to:		
Significant interest entities	32,198	–
ii. Purchases from:		
Significant interest entities	30,527	49,879
Joint venture entity	–	39,278
iii. Lease rentals and other service charges paid to significant interest entities	17,526	25,319
iv. Contributions made to others:	21,550	21,788
Research and development to Others		
v. Hotel expenses paid for:		
Enterprise owned by relative of a director	7,426	4,649
vi. Rent paid to:		
Key management personnel	9,971	9,208
Spouses of key management personnel	8,956	7,936
vii. Directors' sitting fees	360	392
viii. Donation to an enterprise in which a director is a Managing trustee	730	100
ix. Investments in associate	100,800	–
x. Investments in Joint venture	–	83,037
xi. Loan / advance to an associate	–	49,209
xii. Interest free deposit adjusted against loan to associate	–	53,000

d. The Group has the following amounts due from/to related parties:

PARTICULARS	As at 31 MARCH 2006	As at 31 MARCH 2005
i. Due from key management personnel (included in loans and advances)	2,261	3,680
ii. Deposit with significant interest entity (included in loans and advances)	3,000	3,000
iii. Due to related parties (included in current liabilities):		
Significant interest entities	20,145	15,572
Joint venture entity	–	5,401
Enterprise owned by relative of a director	522	170

e. Details of remuneration paid to the whole-time and non-whole-time directors are given in Note 11 to Schedule 19.

10. SEGMENTAL INFORMATION

The primary and secondary reportable segments are business segments and geographic segments respectively.

Business segments:

For management purposes, the Group is organised on a worldwide basis into six strategic business units (SBUs), which are the reportable segments:

- Formulations;
- Active Pharmaceutical Ingredients and Intermediates (API);
- Generics;
- Critical Care and Biotechnology;
- Drug Discovery; and
- Customs Pharmaceutical Services (CPS)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

The Group reports its primary segment information on the basis of strategic business units (SBUs). Formulations also referred to as finished dosages, consist of finished pharmaceutical products ready for consumption by the patient marketed under brand name. Active pharmaceutical ingredients and intermediates, also known as active pharmaceutical products or bulk drugs, are the principal ingredients for formulations. Active pharmaceutical ingredients and intermediates become formulations when the dosage is fixed in a form ready for human consumption such as a tablet, capsule or liquid using additional inactive ingredients. Generics are generic finished dosages with therapeutic equivalence to innovator products. Drug Discovery involves the discovery of new chemical entities meant for subsequent commercialisation or out licensing. Critical Care and Biotechnology business relates to diagnostic pharmaceuticals and equipment and specialist products produced and marketed by the Group primarily for anti cancer and critical care. Custom Pharmaceutical Services business caters to the strategic outsourcing needs of large innovator as well as emerging pharmaceutical companies, spanning the entire value chain of pharmaceutical services.

Geographic segments:

The Group's business is organised into five key geographic segments. Revenues are attributable to individual geographic segments based on the location of the customer.

Segment revenues and expenses:

All segment revenues and expenses are directly attributable to the segments.

Segment assets and liabilities:

According to the internal organisation and management structure of the Group and its system of internal financial reporting, the Chief Operating Decision Maker does not review the total assets and liabilities for each reportable segment.

The assets and liabilities are not fully identifiable with / allocable to individual reportable segments. as certain assets are interchangeable between segments. Consequently, the Management believes that it is not practicable to provide segmental disclosures relating to assets and liabilities by primary segments.

Inter-segment transfers:

Segment revenue, segment expenses and segment result include transfers between business segments. Inter-segment transfers are accounted for at cost to the transferring segment. Such transfers are eliminated on consolidation.

Accounting policies:

The accounting policies consistently used in the preparation of the financial statements are also applied to items of revenues and expenditure in individual segments.

Unallocable and Head office expenses:

General administrative expenses, head-office expenses, and other expenses that arise at the corporate level and relate to the Group as a whole, are shown as unallocable items.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

	FORMULATIONS	ACTIVE PHARMACEUTICAL INGREDIENTS AND INTERMEDIATES	GENERICS	CRITICAL CARE AND BIOTECHNOLOGY	DRUG DISCOVERY	CUSTOM PHARMACEUTICAL SERVICES	OTHERS	ELIMINATIONS	UNALLOCABLE ITEMS	TOTAL
External sales (Gross)	10,182,493	8,300,503	4,009,426	691,906	–	1,390,469	30,450	–	–	24,605,247
Inter-segment sales	40,426	1,424,592	–	40,770	–	15,056	–	(1,520,844)	–	–
Less: Excise duty and other similar duties and taxes on sales	(507,300)	(379,500)	(228,800)	(23,873)	–	–	–	–	–	(1,139,473)
TOTAL SALES	**9,715,619**	**9,345,595**	**3,780,626**	**708,803**	**–**	**1,405,525**	**30,450**	**(1,520,844)**	**–**	**23,465,774**
Income from services	–	–	–	–	–	113,403	–	–	–	113,403
License fees	–	–	47,521	–	–	–	–	–	–	47,521
Sale of spent chemicals	–	100,034	–	1,555	–	–	–	–	–	101,589
Miscellaneous income	17,153	45,799	2,235	1,452	875	862	–	–	7,450	75,826
SEGMENT REVENUES	**9,732,772**	**9,491,428**	**3,830,382**	**711,810**	**875**	**1,519,790**	**30,450**	**(1,520,844)**	**7,450**	**23,804,113**
Interest	–	–	–	–	–	–	–	–	693,345	693,345
Dividend	–	–	–	–	–	–	–	–	29	29
Other unallocable income	–	–	–	–	–	–	–	–	334,728	334,728
Total revenues	–	–	–	–	–	–	–	–	–	24,832,215
SEGMENT RESULT	**3,344,913**	**1,562,214**	**(568,559)**	**59,189**	**(674,697)**	**63,142**	**30,450**			**3,816,652**
Unallocated expenses									1,159,056	1,159,056
Finance charges									644,242	644,242
Profit before taxation and minority interest										2,013,354
Income tax expense										545,980
Profit after taxation, but before minority interest										1,467,374
Minority interest										(76)
PROFIT FOR THE YEAR										**1,467,298**

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

	FORMULATIONS	ACTIVE PHARMACEUTICAL INGREDIENTS AND INTERMEDIATES	GENERICS	CRITICAL CARE AND BIOTECHNOLOGY	DRUG DISCOVERY	CUSTOM PHARMACEUTICAL SERVICES	OTHERS	ELIMINATIONS	UNALLOCABLE ITEMS	TOTAL
External sales (Gross)	7,914,432	6,942,366	3,515,904	527,230	–	312,665	–	–	–	19,212,597
Inter-segment sales	17,702	807,104	–	115,714	–	–	–	(940,520)	–	–
Less: Excise duty and other similar duties and taxes on sales	(367,095)	(296,367)	(169,445)	(20,930)	–	–	–	–	–	(853,837)
TOTAL SALES	**7,565,039**	**7,453,103**	**3,346,459**	**622,014**	**–**	**312,665**	**–**	**(940,520)**	**–**	**18,358,760**
Income from services	–	–	57,441	–	–	4,816	–	–	–	4,816
License fees	–	–	47,521	–	–	–	–	–	–	57,441
Sale of spent chemicals	–	83,310	–	1,704	–	–	–	–	–	85,014
Miscellaneous income	33,975	24,927	8,830	2,005	650	364	–	–	42,627	113,378
SEGMENT REVENUES	**7,599,014**	**7,561,340**	**3,412,730**	**625,723**	**650**	**317,845**	**–**	**–**	**42,627**	**18,619,409**
Interest	–	–	–	–	–	–	–	–	373,901	373,901
Dividend	–	–	–	–	–	–	–	–	98	98
Other unallocable income	–	–	–	–	–	–	–	–	84,536	84,536
Total revenues	–	–	–	–	–	–	–	–	–	19,077,944
SEGMENT RESULT	**2,335,211**	**997,012**	**(712,468)**	**57,936**	**(992,613)**	**42,581**				**1,727,659**
Unallocated expenses									1,481,044	1,481,044
Finance charges									108,083	108,083
Profit before taxation and minority interest										138,532
Income tax epxense										(180,920)
Profit after taxation, but before minority interest										319,452
Minority interest										9,664
PROFIT FOR THE YEAR										**329,116**

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

Sales by markets:

The following table shows the distribution of the Group's sales by geographical markets, based on the location of the customer:

Sales revenues by geographic markets (Gross of excise and other similar duties)

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
India	8,221,665	6,688,532
North America	4,103,033	4,349,191
Russia and other CIS countries	3,654,468	2,401,512
Europe	4,310,557	2,868,233
Others	4,315,524	2,905,129
	24,605,247	**19,212,597**

Analysis of assets by geography

	As at 31 MARCH 2006	As at 31 MARCH 2005
India	23,043,680	21,378,867
North America	45,19,804	2,245,780
Russia and other CIS countries	698,002	750,243
Europe	31,494,219	1,455,869
Others	1,703,673	1,778,573
	61,459,378	**27,609,332**

Cost of tangible and intangible fixed assets acquired by geography

	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
India	1,673,593	2,088,449
North America	983,195	540,919
Russia and other CIS countries	459	5,929
Europe	25,454,608	18,761
Others	4,333	19,830
	28,116,188	**2,673,888**

11. PARTICULARS OF MANAGERIAL REMUNERATION

The remuneration paid to managerial personnel during the year:

PARTICULARS	For the year ended 31 MARCH 2006	For the year ended 31 MARCH 2005
Remuneration and Commission to whole-time directors		
Salaries and allowances	4,814	3,960
Commission	47,996	8,675
Other perquisites	534	534
	53,344	**13,169**
Commission to non-whole-time directors	9,815	2,169
	63,159	**15,338**

The executive directors are covered under the Company's gratuity policy along with the other employees of the Company. Proportionate amount of gratuity and leave encashment is not included in the aforementioned disclosure.

Note: Computation of Net Profits under Section 309(5) of the Companies Act, 1956 ("the Act") and the computation of limit on commission payable to non-whole-time directors have not been disclosed as the limits prescribed under the Act do not apply at consolidated level.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

12. EMPLOYEE STOCK OPTION SCHEME

Dr. Reddy's Employees Stock Option Plan-2002 (the 2002 Plan): The Company instituted the 2002 Plan for all eligible employees in pursuance of the special resolution approved by the shareholders in the Annual General Meeting held on September 24, 2001. The Scheme covers all directors and employees of Dr. Reddy's and directors and employees of all its subsidiaries. Under the Scheme, the 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 2002 Plan was amended on July 28, 2004 at the annual general meeting of shareholders to provide for stock options grants in two categories:

Category A: 1,721,700 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: 573,778 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., Rs.5 per option).

The DRL 2002 Plan was further amended on July 27, 2005 at the annual general meeting of shareholders to provide 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., Rs.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 for 30 days prior to the grant, in the stock exchange where there is highest trading volume during that period. Notwithstanding the foregoing, the Compensation 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.

As the number of shares that an individual employee is entitled to receive and the price of the option are known at the grant date, the scheme is considered as a fixed grant.

In the case of termination of employment, all non-vested 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.

During the current year, the Company under the 2002 Plan has issued 249,360 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 date of grant is given below:

DATE OF GRANT	NUMBER OF OPTIONS GRANTED	EXERCISE PRICE (RUPEES)	MARKET PRICE (RUPEES) (AS PER SEBI GUIDELINES)
5-Apr-05	1,000	5.00	744.50
6-May-05	17,000	5.00	671.95
27-May-05	32,500	725.00	724.50
27-May-05	178,560	5.00	724.50
13-Jun-05	12,000	5.00	713.85
31-Aug-05	8,300	5.00	793.15
	249,360		

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

CATEGORY A – FAIR MARKET VALUE OPTIONS	YEAR ENDED MARCH 31, 2006			
	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE	WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE (MONTHS)
Outstanding at the beginning of the year	298,950	Rs.747-1,149	Rs.977.31	50
Granted during the year	32,500	725	725	81
Expired / forfeited during the year	(46,700)	725-1,149	994.35	–
Surrendered by employees during the year	(90,000)	977.30-1,063.02	1,034.45	–
Exercised during the year	(77,500)	883-977.30	943.84	–
Outstanding at the end of the year	117,250	725-1,063.02	878.85	64
Exercisable at the end of the year	37,882	Rs.725-1,063.02	Rs.943.85	45

CATEGORY B – PAR VALUE OPTIONS	YEAR ENDED MARCH 31, 2006			
	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE	WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE (MONTHS)
Outstanding at the beginning of the year	379,549	Rs.5	Rs.5	84
Granted during the year	216,860	5	5	81
Forfeited during the year	(133,304)	5	5	–
Exercised during the year	(98,121)	5	5	–
Outstanding at the end of the year	364,984	5	5	81
Exercisable at the end of the year	18,136	Rs.5	Rs.5	59

CATEGORY A – FAIR MARKET VALUE OPTIONS	YEAR ENDED MARCH 31, 2005			
	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE	WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE (MONTHS)
Outstanding at the beginning of the year	911,038	Rs.883-1,396	Rs.968.95	66
Granted during the year	466,500	747-885	872.82	82
Expired / forfeited during the year	(352,657)	765-1,063.02	918.84	–
Surrendered by employees during the year in exchange for category B options	(725,931)	747-1,396	928.07	–
Exercised during the year	–	–	–	–
Outstanding at the end of the year	298,950	747-1149	977.31	50
Exercisable at the end of the period	188,538	Rs.883-1,149	Rs.996.54	35

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

CATEGORY B – PAR VALUE OPTIONS	YEAR ENDED MARCH 31, 2005			
	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE	WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE (MONTHS)
Outstanding at the beginning of the year	–	–	–	–
Granted during the year				
In exchange for category A surrendered options	280,873	Rs.5	Rs.5	84
New options	102,650	5	5	84
Expired/forfeited during the year	(3,974)	5	5	–
Exercised during the year	–	–	–	–
Outstanding at the end of the year	379,549	Rs.5	Rs.5	84
Exercisable at the end of the year	–	–	–	–

The Company has followed intrinsic method of accounting based on which a compensation expense of Rs.133,073 (previous year: Rs.52,343) has been recognized in the profit and loss account (refer Schedule 15 – Deferred stock compensation expense)

Aurigene Discovery Technologies Ltd. Employee Stock Option Plan (the "Aurigene ESOP Plan"):
In fiscal 2004, Aurigene Discovery Technologies Limited ("Aurigene"), a consolidated subsidiary, adopted the Aurigene ESOP Plan to provide for issuance of stock options to employees. Aurigene has reserved 4,550,000 of its ordinary shares for issuance under this plan. Under the Aurigene ESOP Plan, stock options may be granted at a price per share as may be determined by the Compensation Committee. The options vest at the end of three years from the date of grant of option.

Stock option activity under the Aurigene ESOP Plan was as follows:

	YEAR ENDED MARCH 31, 2006			
	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE	WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE (MONTHS)
Outstanding at the beginning of the year	197,178	Rs.10	Rs.10	59
Granted during the year	500,000	10	10	70
Expired / forfeited during the year	(168,271)	10	10	–
Outstanding at the end of the year	528,907	Rs.10	Rs.10	67
Exercisable at the end of the year	–	–	–	–

	YEAR ENDED MARCH 31, 2005			
	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE	WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE (MONTHS)
Outstanding at the beginning of the year	169,188	Rs.10	Rs.10	65
Granted during the year	342,381	10	10	61
Expired / forfeited during the year	(314,391)	10	10	–
Outstanding at the end of the year	197,178	Rs.10	Rs.10	59
Exercisable at the end of the year	–	–	–	–

Aurigene Discovery Technologies Ltd. Management Group Stock Grant Plan (the "Management Plan"):
In fiscal 2004, Aurigene adopted the Management Plan to provide for issuance of stock options to management employees of Aurigene and its subsidiary Aurigene Discovery Technologies Inc. Aurigene has reserved 2,950,000 ordinary shares for issuance under this plan. Under the Management Plan, stock options may be granted at a price per share as may be determined by Aurigene's compensation committee. The options vest on the date of grant of the options.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

Stock option activity under the Management Plan was as follows:

	YEAR ENDED MARCH 31, 2006			
	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE	WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE (MONTHS)
Outstanding at the beginning of the year	100,000	Rs.10	Rs.10	65
Granted during the year	–	–	–	–
Expired during the year	(100,000)	10	10	–
Outstanding at the end of the year	–	–	–	–
Exercisable at the end of the year	–	–	–	–

	YEAR ENDED MARCH 31, 2005			
	SHARES ARISING OUT OF OPTIONS	RANGE OF EXERCISE PRICES	WEIGHTED-AVERAGE EXERCISE PRICE	WEIGHTED-AVERAGE REMAINING CONTRACTUAL LIFE (MONTHS)
Outstanding at the beginning of the year	616,666	Rs.10	Rs.10	77
Granted during the year	616,667	10	10	73
Expired during the year	(1,133,333)	10	10	–
Outstanding at the end of the year	100,000	Rs.10	Rs.10	65
Exercisable at the end of the year	100,000	Rs.10	Rs.10	65

13. RESEARCH AND DEVELOPMENT ARRANGEMENT

The Group undertakes significant portion of the research and development activities relating to drug discovery through its research facilities located in the United States and India.

During the year ended 31 March 2005, the Group entered into a joint development and commercialisation agreement with I-VEN Pharma Capital Limited ("I-VEN"). As per the terms of the agreement, I-VEN will fund up to fifty percent of the project costs (development, registration and legal costs) related to the specified generic product filings made by the Group for the United States of America market. The terms of the arrangement do not require the Group to repay the funds or purchase I-VEN's interest in the event of the failure of the research and development. However, on successful commercialisation of these products, the Group would pay I-VEN royalty at agreed rates on sales for a period of 5 years for each product. The first tranch advanced by I-VEN of Rs. 985,388 was received on 28 March 2005.

The amount received from I-VEN will to be recognised in the income statement upon completion of specific milestones as detailed in the agreement. Accordingly, an amount of Rs. 384,488 (previous year Rs.96,239) has been recognised in the current year representing the proportionate costs relating to the completion of specified filings as a credit to research and development expenses.

Perlecan Pharma arrangement

In September 2005, the Company announced the formation of an integrated drug development company, Perlecan Pharma Private Limited ("Perlecan Pharma"), with a total equity of U.S.$52,500 to be contributed jointly by the Company, Citigroup Venture Capital International Growth Partnership Mauritius Limited ("Citigroup Venture") and ICICI Venture Funds Management Company ("ICICI Venture"). Perlecan Pharma will be engaged in the clinical development and out-licensing of New Chemical Entity ("NCE") assets. As part of this arrangement, the Company has transferred all rights and title, including the development and commercialization rights, of four NCE assets to Perlecan Pharma, on March 27, 2006 ("the closing date"). As per the arrangement, Citigroup Venture and ICICI Venture will contribute U.S.$22,500 each and the Company will contribute U.S.$7,500 towards Perlecan Pharma's initial equity capital. As a result, the Company will initially own approximately 14.28% of the equity of Perlecan Pharma. In addition, Perlecan Pharma will issue to the Company warrants to purchase 45 million equity shares of Perlecan Pharma, at Re 1.00 per warrant, the exercise of which will be contingent upon the success of certain research and development milestones. If the warrants are fully exercised, then the Company will own approximately 62.5% of the equity shares of Perlecan Pharma.

As of March 31, 2006, the three investors have invested Rs.705,700 (U.S.$15,818) in Perlecan Pharma. The Company's share of equity was Rs.100,800 (U.S.$2,259). The Company has also committed to invest an additional amount of Rs.170,000 as its equity contribution in the future. Further, three out of seven directors on the board of Perlecan will be from the Company.

As per the terms of the arrangement, the Company will have the first right to conduct product development and chemical trials on behalf of Perlecan Pharma on an arm's length basis subject to the final decision by the board of directors of Perlecan Pharma. Moreover, the research and development expenses incurred by the Company from 1 April 2005 till the closing date of the arrangement will be reimbursed by Perlecan Pharma. Accordingly, an

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

SCHEDULE 19: NOTES TO CONSOLIDATED ACCOUNTS (CONTINUED)

amount of Rs.231,023 (previous year: Rs.Nil) receivable form Perlecan Pharma has been recognised in the current year representing cost relating to product development and chemical trials as a credit to research and development cost.

14. OPERATING LEASE

The Group leases office and residential facilities under operating lease agreements that are renewable on a periodic basis at the option of both the lessor and the lessee. Rental expense under those leases was Rs.173,271 thousands (previous year Rs.183,517 thousands).

The schedule of future minimum rentals payments in respect of non-cancellable operating leases is set out below:

LEASE OBLIGATIONS	31 MARCH 2006	31 MARCH 2005
Within one year of the balance sheet date	150,051	74,546
Due in a period between one year and five years	373,232	289,363
Due after five years	154,033	227,300
	677,316	**591,209**

15. FINANCE LEASE

A subsidiary of the Group has taken buildings under finance lease. Future minimum lease payments under finance leases as at 31 March 2006 are as follows:

	PRESENT VALUE OF MINIMUM LEASE PAYMENTS	FUTURE INTEREST	MINIMUM LEASE PAYMENTS
Not later than 1 year	19,758	–	19,758
Later than 1 year and not later than 5 years	215,990	13,054	229,044
	235,748	**13,054**	**248,802**

16. COMPARATIVE FIGURES

Previous year's figures have been regrouped / reclassified wherever necessary, to conform to current year's classification.

The consolidated financial statements of the current year include the financial statements of the newly acquired subsidiaries Falcon and Beta group companies from the dates of their acquisition. Accordingly, the current year figures are not directly comparable with those of the previous year.

consolidated cash flow statement FOR THE YEAR ENDED 31 MARCH 2006

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
CASH FLOWS FROM OPERATING ACTIVITIES		
Profit before taxation and minority interest	2,013,354	138,532
Adjustments:		
Depreciation	1,616,859	1,255,982
Provision for wealth tax	1,505	1,274
Bad debts written-off	27,349	44,618
Loss on sale of investments	18,434	26,398
Income on redemption of mutual fund units	(14,510)	(83,273)
Unrealised foreign exchange loss	99,471	26,464
Amortisation of deferred stock compensation expese, net	133,071	52,343
Equity in loss of associates	47,968	51,908
Interest income	(666,912)	(337,124)
Dividend income	(29)	(98)
Finance charges	644,242	108,083
Profit on sale / retirement of fixed asset, net	(320,218)	(1,263)
Provision for doubtful debts	12,852	(36,040)
Provision for doubtful advances	(2,960)	8,581
Operating cash flows before working capital changes	**3,610,476**	**1,256,385**
(Increase)/decrease in sundry debtors	(881,980)	103,651
(Increase)/decrease in inventories	(1,646,475)	(504,983)
(Increase)/decrease in loans and advances	(2,065,070)	118,377
Increase/(decrease) in current liabilities and provisions	2,278,807	1,282,223
Cash generated from operations	**1,295,758**	**2,255,653**
Income taxes refunded/paid	(190,770)	43,460
NET CASH PROVIDED BY OPERATING ACTIVITIES	**1,104,988**	**2,299,113**
Cash flows from investing activities		
Purchase of fixed assets	(1,894,271)	(1,741,329)
Investment in affiliate	(100,800)	–
Proceeds from sale of fixed assets	693,264	50,193
Purchase of investments	(5,243,525)	(10,294,411)
Sale of investments	5,274,899	13,061,903
Interest received	682,532	358,796
Dividends received	29	98
Cash paid for acquisition, net of cash acquired	(27,025,960)	(496,715)
NET CASH (USED) IN/PROVIDED BY INVESTING ACTIVITIES	**(27,613,832)**	**938,535**
Cash flows from financing activities		
Proceeds from issuance of share capital (net of share issue expenses)	73,638	–
Proceeds from long-term borrowings	21,622,798	–
Repayment of long-term borrowings	(9,881)	(182,462)
Repayment of short-term borrowings	(1,664)	(324,038)
Proceeds from short-term borrowing	6,263,840	2,624,700
Interest paid	(628,060)	(108,083)
Dividends paid	(436,368)	(431,615)
NET CASH PROVIDED BY FINANCING ACTIVITIES	**26,882,303**	**1,578,502**

consolidated cash flow statement (CONTINUED)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	As at 31 MARCH 2006	As at 31 MARCH 2005
Net increase in cash and cash equivalents	375,459	4,816,150
Cash and cash equivalents at the beginning of the year	9,354,954	4,495,555
Effect of exchange gain / (loss) on cash and cash equivalents	65,743	43,249
Cash and cash equivalents at the end of the year (Note 1)	9,796,156	9,354,954

As per our report attached
for BSR & CO.
Chartered Accountants
SANJAY AGGARWAL PARTNER
Membership No.: 40780

HYDERABAD 31 MAY 2006

for DR. REDDY'S LABORATORIES LIMITED

DR. K ANJI REDDY CHAIRMAN
G V PRASAD VICE CHAIRMAN & CEO
K SATISH REDDY MANAGING DIRECTOR & COO
V S VASUDEVAN CHIEF FINANCIAL OFFICER
V VISWANATH COMPANY SECRETARY

NOTES:

1. Cash and cash equivalents comprise:

	As at 31 MARCH 2006	As at 31 MARCH 2005
Cash in hand	13,519	10,916
Balances with banks		
In current accounts	3,467,511	513,713
In EEFC current accounts	40,185	182,268
In deposit accounts	6,262,162	8,636,080
In unclaimed dividend accounts	12,110	11,307
In unclaimed fractional share pay order accounts	669	670
	9,796,156	**9,354,954**
Deposits with banks include:		
(i) Margin money for letters of credit and bank guarantees	2,051	2,051
(ii) Balance of unutilised money out of ADS issue	–	1,754,141

(iii) Fixed deposits amounting to Rs.4,468,840 (previous year: Rs.Nil) have been pledged against a loan taken by the Company's subsidiary.

(iv) Fixed deposits amounting to Rs.1,584,600(previous year: Rs.Nil) have been pledged against the short term loan availed from State Bank of India.

2. Previous year's figures have been regrouped/reclassified, wherever necessary to conform to the current year's classification.

US GAAP consolidated financials

Report of Independent Registered Public Accounting Firm

The Board of Directors and Stockholders
Dr. Reddy's Laboratories Limited

We have audited the accompanying consolidated balance sheets of Dr. Reddy's Laboratories Limited and subsidiaries ("the Company") as of March 31, 2006 and 2005, and the related consolidated statements of operations, stockholders' equity and comprehensive income, and cash flows for each of the years in the three-year period ended March 31, 2006. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of March 31, 2006 and 2005, and the results of their operations and their cash flows for each of the years in the three-year period ended March 31, 2006, in conformity with U.S. generally accepted accounting principles.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the effectiveness of Dr. Reddy's Laboratories Limited's internal control over financial reporting as of March 31, 2006, based on criteria established in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated May 31, 2006 expressed an unqualified opinion on management's assessment of, and the effective operation of, internal control over financial reporting.

KPMG
Hyderabad, India
May 31, 2006

consolidated balance sheets AS OF MARCH 31, 2006

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	MARCH 31 2005	MARCH 31 2006	MARCH 31 2006
ASSETS			Convenience translation in US$ (unaudited)
Current assets			
Cash and cash equivalents	Rs.9,287,864	Rs.3,712,637	U.S.$83,468
Investment securities	310,887	14,703	331
Restricted cash	57,866	1,606,245	36,112
Accounts receivable, net of allowances	3,587,289	4,801,794	107,954
Inventories	3,499,606	6,894,712	155,007
Deferred income taxes and deferred charges	236,931	173,750	3,906
Due from related parties	10,812	246,360	5,539
Other current assets	1,361,578	2,639,818	59,348
Total current assets	**18,352,833**	**20,090,019**	**451,664**
Property, plant and equipment, net	7,058,308	9,086,331	204,279
Due from related parties	11,067	6,182	139
Investment securities	995,431	1,090,202	24,510
Investment in affiliates	180,894	132,659	2,982
Goodwill	1,561,499	16,634,509	373,977
Intangible assets, net	1,026,882	17,034,555	382,971
Restricted cash	-	4,468,840	100,469
Other assets	101,446	224,772	5,053
Total assets	**Rs.29,288,360**	**Rs.68,768,069**	**U.S.$. 1,546,045**
LIABILITIES AND STOCKHOLDERS' EQUITY			
Current liabilities			
Borrowings from banks	2,796,330	9,132,462	205,316
Current portion of long-term debt	5,920	925,761	20,813
Trade accounts payable	1,415,648	3,639,217	81,817
Due to related parties	139,503	151,678	3,410
Accrued expenses	2,375,087	3,083,120	69,315
Other current liabilities	849,434	1,812,623	40,751
Total current liabilities	**7,581,922**	**18,744,861**	**421,422**
Long-term debt, excluding current portion	25,145	20,937,132	470,709
Deferred revenue	58,255	56,466	1,269
Deferred income taxes	551,789	6,346,174	142,675
Other liabilities	118,090	411,703	9,256
Total liabilities	**Rs.8,335,201**	**Rs.46,496,336**	**U.S.$. 1,045,331**
STOCKHOLDERS' EQUITY:			
Equity shares at Rs.5 par value; 100,000,000 shares authorized; Issued and outstanding; 76,518,949 shares and 76,694,570 shares as of March 31, 2005 and 2006 respectively	382,595	383,473	8,621
Additional paid-in capital	10,089,152	10,261,783	230,706
Equity-options outstanding	400,749	463,128	10,412
Retained earnings	10,009,305	11,201,794	251,839
Equity shares held by a controlled trust: 41,400 shares	(4,882)	(4,882)	(110)
Accumulated other comprehensive income	76,240	(33,563)	(755)
Total stockholders' equity	**20,953,159**	**22,271,733**	**500,713**
Total liabilities and stockholders' equity	**Rs.29,288,360**	**Rs.68,768,069**	**U.S.$. 1,546,045**

See accompanying notes to the consolidated financial statements.

consolidated statements of operations FOR THE YEAR ENDED MARCH 31,

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	2004	2005	2006	2006
REVENUES				Convenience translation in US$ (unaudited)
Product sales, net of allowances for sales returns (includes excise duties of Rs.870,079, Rs.815,007, and Rs.1,153,273 for the years ended March 31, 2004, 2005 and 2006 respectively)	Rs.20,081,249	Rs.19,126,188	Rs.24,077,209	U.S.$541,304
Service income	22,273	47,441	142,317	3,200
License fees	–	345,737	47,521	1,068
	20,103,522	**19,519,366**	**24,267,047**	**545,572**
Cost of revenues	**9,337,255**	**9,385,820**	**12,417,413**	**279,168**
Gross profit	**10,766,267**	**10,133,546**	**11,849,634**	**266,404**
Operating expenses, net:				
Selling, general and administrative expenses	6,542,501	6,774,563	8,028,884	180,505
Research and development expenses, net	1,991,629	2,803,311	2,152,950	48,403
Amortization expenses	382,857	349,991	419,867	9,439
Foreign exchange (gain)/loss	(282,419)	488,819	126,342	2,840
Other operating (income)/expenses, net	83,208	5,969	(320,361)	(7,202)
Total operating expenses, net	**8,717,776**	**10,422,653**	**10,407,682**	**233,988**
Operating income/(loss)	2,048,491	(289,107)	1,441,952	32,418
Equity in loss of affiliates	(44,362)	(58,101)	(88,235)	(1,984)
Other income, net	535,909	454,237	533,606	11,997
Income before income taxes and minority interest	**2,540,038**	**107,029**	**1,887,323**	**42,431**
Income taxes (expense)/benefit	(69,249)	94,277	(258,390)	(5,809)
Minority interest	3,364	9,942	(76)	(2)
Net income	**Rs.2,474,153**	**Rs.211,248**	**Rs.1,628,857**	**U.S.$ 36,620**
Earnings per equity share				
Basic	32.34	2.76	21.28	0.48
Diluted	32.32	2.76	21.24	0.48
Weighted average number of equity shares used in computing earnings per equity share				
Basic	76,513,764	76,518,949	76,546,658	76,546,658
Diluted	76,549,598	76,559,801	76,701,923	76,701,923

See accompanying notes to the consolidated financial statements

statements of stockholders equity and comprehensive income

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

FOR THE YEAR ENDED MARCH 31, 2004, 2005 AND 2006

	Equity Shares					Equity Shares held by a Controlled Trust				
	No. of shares	Amount	Additional Paid In Capital	Comprehen–sive Income	Accumulated Other Comprehen-sive Income	No. of shares	Amount	Equity – Options Outstanding	Retained Earnings/	Total Stockholders' Equity
Balance as of March 31, 2003	**76,515,948**	**Rs.382,580**	**10,085,004**		**46,328**	**41,400**	**(4,882)**	**135,694**	**8,187,117**	**Rs.18,831,841**
Issuance of equity shares on exercise of options	3,001	15	4,148	–	–	–	–	(1,123)		3,040
Dividends	–	–	–	–	–	–	–	–	(431,598)	(431,598)
Comprehensive income	–	–	–	–	–	–	–	–	–	–
Net income	–	–	–	2,474,153	–	–	–	–	2,474,153	2,474,153
Translation adjustment	–	–	–	24,725	24,725	–	–	–	–	24,725
Unrealized gain on investments, net of tax	–	–	–	15,020	15,020	–	–	–	–	15,020
Comprehensive income	–	–	–	2,513,898	–	–	–	–	–	–
Application of SFAS 123	–	–	–		–	–	–	122,177	–	122,177
Balance as of March 31, 2004	**76,518,949**	**382,595**	**10,089,152**	**–**	**86,073**	**41,400**	**(4,882)**	**256,748**	**10,229,672**	**21,039,358**
Dividends	–								(431,615)	(431,615)
Comprehensive income	–	–	–	–	–	–	–	–	–	
Net income	–			211,248					211,248	211,248
Translation adjustment	–	–	–	13,512	13,512	–		–	–	13,512
Unrealized loss on investments, net of tax	–	–	–	(23,345)	(23,345)	–		–	–	(23,345)
Comprehensive income	–	–	–	201,415	–	–	–	–	–	–
Application of SFAS 123	–	–	–	–	–	–	–	144,001	–	144,001
Balance as of March 31, 2005	**76,518,949**	**382,595**	**10,089,152**		**76,240**	**41,400**	**(4,882)**	**400,749**	**10,009,305**	**20,953,159**
Dividend paid	–	–	–	–	–	–	–	–	(436,368)	(436,368)
Issuance of equity shares on exercise of options	175,621	878	172,631					(99,870)		73,639
Comprehensive income	–	–	–		–	–	–	–	–	–
Net income	–	–	–	1,628,857	–	–	–		1,628,857	1,628,857
Translation adjustment	–	–	–	11,041	11,041	–	–	–	–	11,041
Unrealized loss on investments, net of tax	–	–	–	(120,844)	(120,844)	–	–	–	–	(120,844)
Comprehensive income	–	–	–	1,519,054	–	–	–	–	–	–
Application of SFAS 123								162,249		162,249
Balance as of March 31,2006	**76,694,570**	**Rs.383,473**	**10,261,783**		**(33,563)**	**41,400**	**(4,882)**	**463,128**	**11,201,794**	**Rs.22,271,733**
Convenience translation into U.S.$ (unaudited)		US$ 8,621	US$ 230,706		US$ 755		US$ (110)	US$ 10,412	US$ 251,839	US$ 500,713

See accompanying notes to the consolidated financial statements.

consolidated statements of cash flows FOR THE YEAR ENDED MARCH 31,

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	2004	2005	2006	2006
Cash flows from operating activities				Convenience translation in US$ (unaudited)
Net income	Rs.2,474,153	Rs.211,248	Rs.1,628,857	U.S.$. 36,620
Adjustments to reconcile net income to net cash from operating activities:				
Deferred tax benefit	(134,867)	(95,580)	(55,157)	(1,240)
(Gain)/ loss on sale of available for sale securities, net	(24,786)	(64,997)	3,924	88
Depreciation and amortization	1,128,453	1,309,290	1,567,090	35,231
In-process research and development expensed	–	277,343	–	–
Loss/(gain) on sale of property, plant and equipment	29,319	(1,810)	(320,361)	(7,202)
Provision for doubtful accounts receivable	19,871	79,442	33,629	756
Allowance for sales returns	169,511	105,245	239,462	5,384
Inventory write-downs	31,898	52,692	100,783	2,266
Equity in loss of affiliates.	44,362	58,101	88,235	1,984
Unrealized exchange (gain)/loss	(109,602)	105,227	67,650	1,521
Employees Stock based compensation	122,177	144,001	162,249	3,648
Loss on sale of subsidiary interest	58,473	8,122	–	–
Minority interest	(3,364)	(9,942)	76	2
Changes in operating assets and liabilities:				
Accounts receivable	(379,413)	77,368	(781,607)	(17,572)
Inventories	(335,092)	(514,187)	(1,851,724)	(41,630)
Other assets	(276,467)	142,486	(1,123,076)	(25,249)
Due to / from related parties, net	148,576	(40,249)	15,223	342
Trade accounts payable	690,182	(763,523)	1,511,074	33,972
Accrued expenses	510,768	1,094,768	243,625	5,477
Deferred revenue	–	(247,604)	(16,277)	(366)
Taxes payable	(115,375)	42,513	84,794	1,906
Other liabilities	(49,547)	321,657	44,684	1,005
Net cash provided by operating activities	**3,999,230**	**2,291,611**	**1,643,153**	**36,941**
Cash flows from investing activities				
Restricted cash	(67,221)	49,304	(6,017,219)	(135,279)
Expenditure on property, plant and equipment	(2,415,638)	(1,749,172)	(1,873,268)	(42,115)
Proceeds from sale of property, plant and equipment	33,558	44,673	691,273	15,541
Investment in affiliate	(63,238)	(49,935)	(100,800)	(2,266)
Purchase of investment securities	(13,178,735)	(10,226,471)	(5,074.184)	(114,078)
Proceeds from sale of investment securities	9,167,150	13,079,463	5,274,899	118,590
Expenditure on intangible assets	(105)	(8,299)	(41,517)	(933)
Cash paid towards contingent consideration	–	–	(114,244)	(2,568)
Proceeds from sale of subsidiary	81,464	29,000	–	–
Cash paid for acquisition, net of cash acquired	(63,290)	(535,665)	(27,269,382)	(613,071)
Net cash provided by / (used in) in investing activities	**(6,506,055)**	**632,898**	**(34,524,442)**	**(776,179)**
Cash flows from financing activities:				
Proceeds from issuance of equity	3,040	–	73,639	1,656
Proceeds from issuance of equity, in subsidiary	2,435	–	–	–
Purchase of treasury stock	(115,990)	–	–	–
Proceeds from borrowing from banks, net	177,071	2,520,409	6,322,206	142,136
Proceeds from issuance from long-term debt	–	–	21,598,301	485,573
Repayment of long-term debt	(11,072)	(157,476)	(6,577)	(148)
Debt issuance costs	–	–	(340,243)	(7,649)
Dividends	(431,598)	(431,615)	(436,368)	(9,810)
Net cash provided by/(used in) financing activities	**(376,114)**	**1,931,318**	**27,210,958**	**611,757**

See accompanying notes to the consolidated financial statements

consolidated statements of cash flows FOR THE YEAR ENDED MARCH 31,

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	2004	2005	2006	2006
Effect of exchange rate changes on cash and cash equivalents	(14,224)	55,802	95,104	2,138
Net increase / (decrease) in cash and cash equivalents during the year	(2,897,163)	4,911,629	(5,575,227)	(125,342)
Cash and cash equivalents at the beginning of the year	7,273,398	4,376,235	9,287,864	208,810
Cash and cash equivalents at the end of the year	**Rs.4,376,235**	**Rs.9,287,864**	**Rs.3,712,637**	**U.S.$. 83,468**
Supplemental disclosures:				
Cash paid for:				
Interest	Rs.11,234	Rs.98,337	Rs.225,284	U.S.$.5,065
Income taxes	425,144	–	Rs.223,000	U.S.$.5,013
Supplemental schedule of non-cash investing activities:				
Property, plant and equipment purchased on credit during the year	36,710	22,827	54,276	1,220
Treasury stock issued on acquisition of minority interest including compensation cost	115,990	–		
Promissory notes issued on acquistion	–	–	209,456	4,708

See accompanying notes to the consolidated financial statements

notes to the consolidated financial statements

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

1. OVERVIEW

Dr. Reddy's Laboratories Limited ("Dr. Reddy's") together with its subsidiaries (collectively, the "Company") is a leading India-based pharmaceutical company headquartered in Hyderabad, India. The Company's principal areas of operation are formulations, active pharmaceutical ingredients and intermediates, generics, custom pharmaceutical services, critical care and biotechnology, and drug discovery. The Company's principal research and development and manufacturing facilities are located in Andhra Pradesh, India and Cuernavaca-Cuautla, Mexico with principal marketing facilities in India, Russia, the United States, the United Kingdom,Brazil and Germany. The Company's shares trade on several stock exchanges in India and, since April 11, 2001, on the New York Stock Exchange in the United States. As of March 31, 2006, the list of subsidiaries is as follows:

• DRL Investments Limited ("DRL Investments")	• OOO JV Reddy Biomed Limited ("Reddy Biomed " or "RBL")
• Reddy Pharmaceuticals Hong Kong Limited ("RPHL")	• Reddy Netherlands B.V. ("RNBV")
• Reddy Antilles N.V. ("RANV")	• Reddy Cheminor SA ("RCSA")
• Reddy US Therapeutics Inc. ("Reddy US")	• Aurigene Discovery Technologies Inc. ("ADTI")
• Dr. Reddy's Laboratories Inc. ("DRLI")	• Dr. Reddy's Laboratories (U.K.) Limited ("DRL U.K.")
• Dr. Reddy's Farmaceutica Do Brazil Ltda. ("DRFBL")	• Cheminor Investment Limited ("CIL")
• Aurigene Discovery Technologies Limited ("ADTL")	• Dr. Reddy's Bio-sciences Limited ("RBSL")
• Dr. Reddy's Laboratories (EU) Limited ("DRL EU")	• Trigenesis Therapeutics Inc. ("Trigenesis")
• Dr. Reddy's Laboratories (Proprietary) Limited ("DRSA")	• Industrias Quimicas Falcon De Mexico S.A.de.C.V. ("FALCON")
• Reddy Pharmaceuticals, Inc. USA ("RPI")	• beta Healthcare Verwaltungs GmbH ("Beta HVG")
• Reddy Holding GmbH ("RHG")	• beta Holding GmbH ("Beta HG")
• beta Healthcare GmbH & Co KG ("Beta KG")	• betapharm Arzneimittel GmbH ("Beta AG")
• beta Healthcare Solutions GmbH ("Beta HSG")	• beta Institut gGmbH ("Beta IG")
• OOO Dr. Reddy's Laboratories Limited, Russia ("OOO DRL")	• Lacock Holdings Limited ("LHL")

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

2. SIGNIFICANT ACCOUNTING POLICIES

a) Basis of preparation

The accompanying consolidated financial statements have been prepared in accordance with the accounting principles generally accepted in the United States (U.S. GAAP). The preparation of consolidated financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, revenues and expenses and disclosure of contingent assets and liabilities. Actual results could differ from these estimates.

b) Functional currency

The functional currency of the Company is the Indian rupee, being the currency of the primary economic environment in which the Company operates. The functional currencies of the subsidiaries have been determined as follows based on an individual and collective evaluation of economic factors described in Statament of Financial Accounting Standards ("SFAS") SFAS 52, "Foreign currency translation":

Name of the Subsidiary	Functional Currency
DRL Investments, RPHL, RANV, DRLI, DRFBL, ADTL, DRSA, RPI, OOO DRL, RBL, RNBV, RCSA, CIL, RBSL, Trigenesis, LHL	Indian Rupee
Reddy US and ADTI	U.S. Dollar
DRL EU and DRL U.K.	Pound Sterling
FALCON	Mexican Peso
RHG, Beta KG, Beta HSG, Beta HG, Beta AG, Beta HVG, Beta IG and LHL	Euro

In respect of all foreign subsidiaries that operate as marketing arms of the parent company in their respective countries/regions, the functional currency has been determined to be the functional currency of the parent company, i.e. Indian Rupee. Accordingly, the operations of these entities are largely restricted to import of finished goods from the parent company in India, sale of these products in the foreign country and remittance of the sale proceeds to the parent. The cash flows realized from sale of goods are readily available for remittance to the parent company and cash is remitted to the parent company on a regular basis. The costs incurred by these entities are primarily the cost of goods imported from the parent. The financing of these subsidiaries is done directly or indirectly by the parent company.

In respect of the subsidiaries whose operations are self contained and integrated within their respective countries / regions, the functional currency has been determined to be the currency of those countries / regions. The assets and liabilities of such subsidiaries are translated into Indian rupees at the rate of exchange prevailing as at the balance sheet date. Revenues and expenses are translated into Indian rupees at average monthly exchange rates prevailing during the year. Resulting translation adjustments are included in accumulated other comprehensive income.

c) Foreign currency transactions

Foreign currency transactions are converted into Indian rupees at the rates of exchange prevailing on the date of the respective transactions. Assets and liabilities in foreign currency are converted into Indian rupees at the exchange rate prevailing on the balance sheet date. The resulting exchange gains/ losses are included in the statement of income. For entities that operate in a higly inflationary economy, the functional currency is determined as the Indian Rupee.

d) Convenience translation

The accompanying financial statements have been prepared in Indian rupees, the national currency of India. Solely for the convenience of the reader, the financial statements as of and for the year ended March 31, 2006 have been translated into United States dollars at the noon buying rate in New York City on March 31, 2006 for cable transfers in Indian rupees, as certified for customs purposes by the Federal Reserve Bank of New York of U.S.$1 = Rs.44.48. No representation is made that the Indian rupee amounts have been, could have been or could be converted into United States dollars at such a rate or any other rate.

e) Principles of consolidation

The consolidated financial statements include the financial statements of Dr. Reddy's, all of its subsidiaries, which are more than 50% owned and controlled, entities where the Company has variable interest. Dr. Reddy's Research Foundation (the "Research Foundation"), a special purpose entity that is funded by and carries out research activities on behalf of and for the benefit of the Company and beta Institut Gmbh, a special purpose entity which is engaged in development of patient pathways, case management, disease management, health systems management and psychological health. The Company does not consolidate entities where the minority shareholders have certain significant participating rights which provide for effective involvement in significant decisions in the ordinary course of business. Such investments are accounted by the equity method of accounting. All inter–company balances and transactions are eliminated on consolidation.

The Company accounts for investments by the equity method of accounting where it is able to exercise significant influence over the operating and financing policies of the investee. The Company's equity in the income / loss of equity method affiliates, Reddy Kunshan, Pathnet India Private Limited ("Pathnet") and Perlecan Pharma Private Limited is included in the statement of operations. Inter company profits and losses have been eliminated until realized by the investor or investee.

Newly acquired subsidiaries have been included in the consolidated financial statements from the dates of acquisition. Effective January 2004, the Company adopted FASB Interpretation ("FIN") No. 46 (revised December 2003 "FIN 46R"), Consolidation of Variable Interest Entities ("VIE"), which addresses how a business enterprise should evaluate whether it has a controlling financial interest in an entity through means other than voting rights and accordingly should consolidate the entity.

For any VIEs that must be consolidated under FIN 46R that were created after January 1, 2004, the interpretation generally requires the primary beneficiary initially to measure the assets, liabilities and noncontrolling interests of the newly consolidated VIE at their fair values at the date the enterprise first becomes the primary beneficiary.

Based on the evaluation on FIN 46R, the Company has consolidated the financial statements of APR LLC, a VIE.

f) Cash equivalents

The Company considers all highly liquid investments with remaining maturities, at the date of purchase / investment, of three months or less to be cash equivalents.

g) Revenue recognition

Product sales

Revenue is recognized when significant risks and rewards in respect of ownership of products are transferred to customers, generally, the stockists or formulations manufacturers and when the following criteria are met:

- Persuasive evidence of an arrangement exists;
- The price to the buyer is fixed and determinable; and
- Collectibility of the sales price is reasonably assured.

Revenue from domestic sales of formulation products is recognized on dispatch of the product to the stockist by the consignment and clearing and forwarding agent of the Company. Revenue from domestic sales of active pharmaceutical ingredients and intermediates is recognized on dispatch of products to customers, from the factories of the Company. Revenue from export sales is recognized when significant risks and rewards are transferred to customers, which is based on terms of contract.

Revenue from product sales includes excise duty and is shown net of sales tax and applicable discounts and allowances.

Sales of formulations in India are made through clearing and forwarding agents to stockists. Significant risks and rewards in respect of ownership of formulation products is transferred by the Company when the goods are shipped to stockists from clearing and forwarding agents. Clearing and forwarding agents are generally compensated on a commission basis as a percentage of sales made by them.

Sales of active pharmaceutical ingredients and intermediates in India are made directly to the end customers generally, formulation manufacturers, from the factories. Sales of formulations and active pharmaceutical ingredients and intermediates outside India are made directly to the end customers, generally stockists or formulations manufacturers, from the Company or its consolidated subsidiaries.

The Company has entered into marketing arrangements with certain marketing partners for sale of goods. Under such arrangements, the Company sells generic products to the marketing partners at a price agreed in the arrangement. Revenue is recognized on these transactions upon delivery of products to the marketing partners as all the conditions under Staff Accounting Bulletin No.104 ("SAB 104") are met. Subsequently, the marketing partners remit an additional amount based on the ultimate sale proceeds upon further sales made by them to the end customer. Such amount is determined as per the terms of the arrangement and is recognized by the Company when the realization is certain under the guidance given in SAB 104.

The Company has entered into certain dossier sales, licensing and supply arrangements that include certain performance obligations. Based on an evaluation of whether or not these obligations are inconsequential or perfunctory, the Company defers the upfront payments received towards these arrangements. Such deferred amounts are recognized in the income statement in the period in which the Company completes its remaining performance obligations.

Sales of generic products is recognized as revenue when products are shipped and title and risk of loss passes on to the customeRs.Provisions for chargeback, rebates and medicaid payments, are estimated and provided for in the year of sales. Such provisions are estimated based on average charge back rate actually claimed over a period of time and average inventory holding by the wholesaler. A charge back claim is a claim made by the wholesaler for the differential price at which the product is sold to customers and the price at which it is procured from the Company.

The Company accounts for sales returns in accordance with SFAS 48, " Revenue Recognition when Right to Return Exists" by establishing an accrual in an amount equal to the Company's estimate of sales recorded for which the related products are expected to be returned.

The Company deals in various products and operates in various markets and the Company's estimate is determined primarily by its experience in these markets for the products. For returns of established products, the Company determines an estimate of the sales returns accrual primarily based on historical experience regarding sales returns. Additionally other factors that the Company considers in its estimate of sales returns include levels of inventory in the distribution channel, estimated shelf life, product discontinuances, price changes of competitive products, introductions of generic products and introductions of competitive new products to the extent each of them has an impact on the Company's business and its markets. The Company considers all of these factors and adjusts the accrual to reflect actual experience.

With respect to new products that the Company introduces, they are either extensions of an existing line of products or in a generally therapeutic category where the Company has historical experience. The Company's new product launches have historically been in therapeutic categories where established products exist and are sold either by the Company or its competitoRs.The Company has not yet introduced products in any new therapeutic category where the acceptance of such products is not known. The amount of sales returns for the Company's newly launched products are not significantly different from current products marketed by the Company or its competitors and hence the Company does not expect sales returns for new products to be significantly different than expected sales returns of current products. The Company evaluates the sales returns of all of the products at the end of each reporting period and necessary adjustments, if any, are made. However, to date, no significant revision has been determined to be necessary.

License fees

Non-refundable milestone payments are recognized in the statement of income when earned, in accordance with the terms prescribed in the license agreement, and where the Company has no future obligations or continuing involvement pursuant to such milestone payments. Non-refundable up-front license fees are deferred and recognized when the milestones are earned, in proportion that the amount of each milestone earned bears to the total milestone amounts agreed in the license agreement. As the upfront license fees are a composite amount and cannot be attributed to a specific molecule, they are amortized over the development period. The milestone payments during the development period increase as the risk involved decreases. The agreed milestone payments reflect the progress of the development of the molecule and may not be spread evenly over the development period. Further, the milestone payments are a fair representation of the extent of progress made in the development of these molecules. Hence, the upfront license fees are amortized over the development period in proportion to the milestone payments received. In the event, the development is discontinued, the corresponding amount of deferred revenue is recognized in the income statement in the period in which the project is effectively terminated.

h) Shipping and handling costs

Shipping and handling costs incurred to transport products to customers are included in selling, general and administrative expenses.

i) Inventories

Inventories are stated at the lower of cost or market value. Cost is determined using the first-in-first-out method for all categories of inventories except stores and spares, where cost is determined using the weighted average method. Stores and spares comprise engineering spares such as machinery spares and consumables such as lubricants, cotton waste and oils, which are used in operating machines or consumed as indirect materials in the manufacturing process. Cost in the case of raw materials and stores and spares comprises the purchase price and attributable direct costs, less trade discounts. Cost in the case of work-in-process and finished goods comprises direct labor, material costs and production overheads.

A write-down of inventory to the lower of cost or market value at the close of a fiscal period creates a new cost basis and is not marked up based on changes in underlying facts and circumstances.

Inventories are reviewed on a monthly basis for identification and write-off of slow-moving, obsolete and impaired inventory. Such write-downs, if any, are included in cost of goods sold.

j) Investment securities

Investment securities consist of available for sale debt and equity securities and non-marketable equity securities accounted for by the cost method.

Available for sale securities are carried at fair value based on quoted market prices. For debt securities where quoted market prices are not available, fair value is determined using pricing techniques such as discounted cash flow analysis or at the swap rates and forward rate agreements on the date of the valuation, obtained from market sources. Unrealized holding gains and losses, net of the related tax effect, on available for sale securities are excluded from earnings and are reported as a separate component of stockholders' equity until realized. Decline in the fair value of any available for sale security below cost that is determined to be other than temporary, results in reduction in the carrying amount to fair value. Such impairment is charged to the statement of operations. Realized gains and losses from the sale of available for sale securities are determined on a first-in-first-out method and are included in earnings.

Non-marketable equity securities accounted for by the cost method are stated at cost, less provision for any other than temporary decline in value.

k) Derivative financial instruments

On April 1, 2001, the Company adopted SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities" as amended, when the rules became effective for companies with period ending March 31, 2006 and adopted SFAS 149 "Amendment of Statement 133 on Derivative Instruments and Hedging Activities", which is effective for all contracts entered into or modified after June 30, 2003. The Company enters into forward foreign exchange contracts and options where the counterparty is generally a bank. The Company purchases forward foreign exchange contracts and options to mitigate the risk of changes in foreign exchange rates on accounts receivable and foreign currency loans and deposits. Although these contracts are effective as hedges from an economic perspective, they do not qualify for hedge accounting under SFAS No. 133, as amended. Any derivative that is either not designated as a hedge, or is so designated but is ineffective per SFAS No. 133, is marked to market and recognized in income immediately. No initial transition adjustments were required to adopt SFAS No. 133.

l) Property, plant and equipment

Property, plant and equipment including assets acquired under capital lease agreements are stated at cost less accumulated depreciation. The Company depreciates property, plant and equipment over the estimated useful life using the straight-line method. Assets under capital leases are amortized over their estimated useful life or the lease term as appropriate. The estimated useful lives of assets are as follows:

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

Buildings	
– Factory and administrative buildings	25 to 40 years
– Ancillary structures	3 to 15 years
Plant and machinery	3 to 15 years
Furniture, fixtures and office equipment	4 to 10 years
Vehicles	4 to 5 years
Computer equipment	3 to 5 years

Advances paid towards the acquisition of property, plant and equipment outstanding at each balance sheet date and the cost of property, plant and equipment not put to use before such date are disclosed under capital work-in-progress. The interest cost incurred for funding an asset during its construction period is capitalized based on the actual investment in the asset and the average cost of funds. The capitalized interest is included in the cost of the relevant asset and is depreciated over the estimated useful life of the asset.

m) Goodwill

Goodwill represents the excess of purchase cost over the fair value of the net tangible and identified intangable assets of businesses acquired. Goodwill is not amortized but is tested for impairment at least annually.

n) Intangible assets

Intangible assets consist of goodwill and other acquired intangibles, which include core-technology rights, trademarks, customer related intangibles, marketing rights, marketing know-how, beneficial toll manufacturing contracts and non-compete arrangements. All intangible assets with definite life are amortized over the expected benefit period or the legal life, whichever is lower. Such periods are as follows:

Trademarks	
– Trademarks with indefinite life	Tested for impairment at least annually
– Trademarks with definite life	5 to 10 years
Core technology rights and licenses	10 to 15 years
Product related intangibles	12 to 14 years
Marketing rights	11 to 16 years
Non-compete arrangements	1.5 to 10 years
Marketing know-how	6 months
Customer-related intangibles including customer contracts	2 to 5 years
Beneficial toll manufacturing contract	58 months
Other intangibles	5 to 15 years

0) Impairment or disposal of long-lived assets and long-lived assets to be disposed of

Long-lived assets and finite life intangibles are reviewed for impairment whenever events or changes in business circumstances indicate that the carrying amount of assets may not be fully recoverable. Each impairment test is based on a comparison of the undiscounted cash flows expected to be generated from the use of the asset to its recorded value. If impairment is indicated, the asset is written down to its fair value. Long-lived assets to be disposed are reported at the lower of the carrying value or fair value, less cost to sell.

p) Start-up costs

Costs of start-up activities including organization costs are expensed as incurred.

q) Research and development

Research and development cost is expensed as incurred. In-process technologies used in research and development projects and having no alternate future uses are expensed upon purchase. Capital expenditure incurred on equipment and facilities acquired or constructed for research and development activities and having alternative future uses, is capitalized as property, plant and equipment when acquired or constructed.

r) Stock-based compensation

The Company uses the Black-Scholes option pricing model to determine the fair value of each option grant. The Black-Scholes model includes assumptions regarding dividend yields, expected volatility, expected lives and risk free interest rates. These assumptions reflect management's best estimates, but these assumptions involve inherent market uncertainties based on market conditions generally outside of the control of the Company. As a result, if other assumptions had been used in the current period, stock-based compensation expense could have been materially impacted. Furthermore, if management uses different assumptions in future periods, stock based compensation expense could be materially impacted in future years.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

The fair value of each option is estimated on the date of grant using the Black-Scholes model with the following assumptions:

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Dividend yield	0.5%	0.5%	0.5%
Expected life	42-78 months	12-78 months	12-78 months
Risk free interest rates	5.2 – 6.8%	4.5-6.7%	5.7-7.5%
Volatility	45.7-50.7%	39.4-44.6%	23.4-36.9%

At March 31, 2006, the Company had three stock-based employee compensation plans, which are described more fully in Note 23. Prior to April 1, 2003, the Company accounted for its plans under the recognition and measurement provisions of Accounting Principle Board Opinion ('APB'). APB Opinion No. 25, "Accounting for Stock Issued to Employees", and related interpretations. No stock-based employee compensation cost was reflected in previously reported results, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant. During the first quarter of fiscal 2004, the Company adopted the fair value recognition provisions of SFAS No. 123, "Accounting for Stock- Based Compensation", for stock-based employee compensation. The Company has selected the retroactive method of adoption described in SFAS No. 148 "Accounting for Stock Based Compensation – Transition and Disclosure" for all options granted after January 1, 1995. Consequently, for the years ended March 31, 2004, 2005 and 2006, an amount of Rs.122,177, Rs.144,001 and Rs.162,249 respectively, has been recorded as total employee stock based compensation expense.

During fiscal 2004, Aurigene Discovery Technologies Limited adopted two stock based employee compensation plans, which are described more fully in Note 23. The Company has accounted for these plans under SFAS 123 Accounting for Stock-Based Compensation", using the Black Scholes option pricing model to determine the fair value of each option grant.

s) Income taxes

Income taxes are accounted for using the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss carry-forwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in the statement of operations in the period that includes the enactment date. The measurement of deferred tax assets is reduced, if necessary, by a valuation allowance for any tax benefits the future realization of which is not considered more likely than not.

t) Leases

Leases of property plant and equipment where the Company has substantially all of the risks and rewards of ownerships are classified as capital lease. The amount recorded is the lesser of the present value of the rental and other lease payments during the lease term, excluding that portion of the payments representing executory costs paid to the lessor or the asset's fair value. The rental obligations, net of interest charges, are reflected in long term debt.

Leases that do not transfer substantially all of the benefits or risks of ownership are classified as operating leases and recorded as expenses as payments are made over the lease term.

u) Earnings per share

In accordance with SFAS No.128, "Earnings per Share", basic earnings per share is computed using the weighted average number of common shares outstanding during the period. Diluted earnings per share is computed using the weighted average number of common and dilutive common equivalent shares outstanding during the period, using the treasury stock method for options and warrants, except where the results would be anti-dilutive.

v) Recent accounting pronouncements

In November 2004, the FASB issued SFAS No. 151, "Inventory costs", an amendment of Accounting Research Bulletin ("ARB"), ARB No. 43, and Chapter 4. SFAS 151, amends and clarifies financial accounting and reporting for inventory costs. This statement amends current guidance to clarify the accounting for abnormal amounts of idle facility expense, freight, handling costs, and wasted material. This statement requires that those items be recognized as current-period charges. In addition, this statement requires that allocation of fixed production overheads to the costs of conversion be based on the normal capacity of the production facilities. This statement becomes effective on April 1, 2006 and the provisions of this statement shall be applied prospectively. The Company does not expect this statement to have a material effect on the Company's financial statements or its results of operations.

In December 2004, the FASB issued SFAS No. 123 (revised 2004), "Share-Based Payment" ("SFAS 123R"). SFAS 123R is an amendment of SFAS 123, "Accounting for Stock-Based Compensation". This statement also supersedes APB Opinion No. 25, "Accounting for Stock Issued to Employees". SFAS 123R focuses primarily on accounting for transactions in which an entity obtains employee services in share-based payment transactions. Pursuant to the Securities and Exchange Commission Release No. 33-8568, the Company is required to adopt SFAS 123R from April 1, 2006. Adoption of SFAS No. 123R will not have any material impact on the consolidated financial statements, as the Company has already adopted fair value accounting under SFAS 123.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

In June2005, the FASB issued SFAS No. 154, "Accounting changes and error corrections". SFAS 154 is a replacement is Accounting Pronouncement Board ("APB") No. 20 and SFAS No. 3 "Reporting Accounting Changes in Interim Financial Statements", the statement applies to all voluntary changes in accounting principle, and changes the requirements for accounting for and reporting of a change in accounting principle. SFAS 154 requires retrospective application to prior periods' financial statements of a voluntary change in accounting principle unless it is impracticable. APB 20, previously required that most voluntary changes in accounting principle be recognised by including in net income of the period of the change the cumulative effect of changing to the new accouting principle. SFAS 154, is effective for accounting changes and corrections of errors made in fiscal years beginning after December 15, 2005. The statement does not change the transition provisions foamy existing accounting pronouncements including those that are in a transition phase as of the effective date of the statement.

w) Reclassifications

The Company has reclassified certain expenses/income for the year ended March 31, 2004 and 2005, between costs of revenues, operating expenses, product sales, other (expense) / income and other operating expense/(income) respectively, to confirm to the current presentation. These reclassifications increased the previously reported gross profit by Rs.31,135 and Rs.47,441 respectively and reduced the previously reported operating income for the year ended March 31, 2004 by Rs.31,718 and reduced the previously reported operating loss for the year ended March 31, 2005 by Rs.77,343, which is not material. The above reclassification had no impact on reported net income or stockholder's equity.

3. BUSINESS COMBINATIONS

All of the Company's acquisitions have been accounted for using the purchase method of accounting. Revenues and expenses of the acquired businesses have been included in the acompanying consolidated financial statements beginning on the respective dates of acquisition. Contingent transaction consideration pursuant to earnout agreements is accrued as an additional cost of the transaction when payment thereof is deemed to be probable by the Company.

Industrias Quimicas Falcon de Mexico, S.A. de C.V ("Falcon")

On December 30, 2005 the Company acquired 100% of the share capital of Industrias Quimicas Falcon de Mexico, S.A.de C.V ("Falcon"), a Roche group company for a total purchase consideration of Rs.2,773,126 (U.S.$ 61,233).

Falcon was acquired with an intent to add unique steroid manufacturing capabilities and to partner with innovator companies across the globe with service offerings spanning the entire value chain of pharmaceutical services. The operations of Falcon relate to the manufacture and sale of active pharmaceutical ingredients and steroids as per innovator's requirements.

The Company has accounted for the acquisition under the purchase method as defined in SFAS No. 141, "Business combinations. Accordingly, the financial results for the period December 30, 2005 through March 31, 2006 have been included in the consolidated financial statements of the Company. The purchase cost of Rs.2,773,126 has been allocated as follows:

CURRENT ASSETS	
Cash and cash equivalents	Rs. 215
Accounts receivable	39,353
Inventories	1,139,509
Other current assets	256,937
Property, plant and equipment	1,404,987
Intangible assets	–
Customer contracts	50,992
Non-competition agreement	20,045
Total assets	–
Liabilities assumed	(13,207)
Deferred tax liability	(125,705)
Purchase cost	**Rs. 2,773,126**

The weighted average useful lives of intangibles acquired are as follows:-

Customer contracts	2.6 years
Non competition agreement	3 years

beta Holding GmbH

On March 3, 2006, the Company, through its wholly owned subsidiary Lacock Holdings Limited, acquired 100% of the outstanding common shares of beta Holding GmbH. Accordingly, the financial results of beta Holding GmbH have been included in the consolidated financial statements since that date. beta Holding GmbH is a leading generics pharmaceuticals Company in Germany. Under the 'beta' brand, the Company markets a broad and diversified portfolio comprising formulations, primarily solid dose, focused on medical conditions requiring long-term therapy that are typically prescribed by primary care physicians. This strategic investment in beta Holding GmbH is a step towards realizing the Company's intention of building a global generics business in key markets.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

The aggregate purchase price of Rs.26,063,321 (Euro 482,654) includes direct acquisition cost amounting to Rs.201,548 (Euro 3,732). The agreement included the payment of a contingent consideration amounting up to Rs.518,400 (Euro 9,600), which was paid into an escrow account. This amount is subject to set-off for certain indemnity claims in respect of legal and tax matters that might arise, pertaining to the periods prior to the acquisition. The escrow will lapse and be time barred at the end of the year 2013. Since the maximum amounts pertaining to such claims are determinable at the date of acquisition, the same has been included as part of the purchase price.

The following table summarizes the estimated fair values of the assets acquired and liabilities assumed at the date of acquisition. The Company is in the process of obtaining third-party valuations of certain intangible assets and accordingly, the allocation of the purchase price is preliminary and may be prospectively revised when additional information is obtained based on third party valuation. The final purchase price allocation is expected to be completed by September 30, 2006. The initial purchase price of beta Holding GmbH, has been allocated based on management's estimate of fair values as follows:

CURRENT ASSETS	
Cash and cash equivalents	Rs.1,357,395
Inventories	538,860
Other current assets	552,938
Property, plant and equipment	372,382
Intangibles	
Trademarks	3,970,118
Product related intangibles	11,734,422
Toll manufacturing agreement	621,058
Other assets	142,541
Goodwill	14,958,766
Total assets	34,248,480
Deferred tax liability, net	(5,825,388)
Liabilities assumed	(2,359,771)
Purchase cost	**Rs.26,063,321**

Trademarks have an indefinite useful life and are therefore not subject to amortization but will be tested for impairment annually. The weighted average useful lives of other intangibles acquired are as follows:

Products related intangibles	11.6 years
Toll manufacturing agreement	5 years

All of goodwill arising on beta Holding GmbH acquisition was assigned to the Generics segment.

Proforma Information: The table below reflects unaudited pro forma consolidated results of operations as if both Falcon and beta Holding GmbH acquisitions had been made at the beginning of the periods presented below:

	YEAR ENDED MARCH 31,	
	2005 (unaudited)	2006 (unaudited)
Revenues	Rs.28,658,645	Rs.33,766,668
Net income	Rs.1,227,528	1,991,090
Earning per equity share		
Basic	16.04	26.01
Diluted	16.03	25.96
Weighted average number of equity shares used in computing earnings per share		
Basic	76,518,949	76,546,658
Diluted	76,559,801	76,701,923

notes to the consolidated financial statements

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

4. ASSET PURCHASE

Trigenesis Therapeutics Inc.

On April 27, 2004, the Company acquired the entire share capital of Trigenesis Therapeutics Inc. ("Trigenesis") for a total consideration of Rs.496,715 (U.S.$11,000).

Trigenesis is a U.S. based research company specializing in dermatology field. As a result of the acquisition, DRL has acquired certain technology platforms and marketing rights. The acquisition has been accounted for as a purchase of intangible assets as Trigenesis did not meet the definition of a business as described in EITF Issue No. 98-3 Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business and accordingly the transaction did not meet the definition of a business combination.

The total purchase consideration had been allocated to the acquired assets as of March 31, 2005 based on a valuation carried out by an independent valuer.

Core-technology rights and licenses	Rs.132,753
Marketing rights	Rs.86,619
In-process technology	Rs.277,343
	Rs.496,715

The Company expensed the amount allocated towards in-process technology being research and development projects having no future alternate uses as research and development expenses during the year ended March 31, 2005. The core-technology rights and licenses and marketing rights have been capitalized as intangible assets to be amortized over the period such assets are expected to contribute directly or indirectly to the future cash flows.

PDL Pharma Biopharm, Inc

On March 13, 2006, the Company acquired three trademarks along with all the physical inventories of the related products from PDL Biopharm, Inc (PDL) for a total consideration of Rs.122,691 (U.S.$ 2,750).

PDL is a U.S. based fully integrated biopharmaceutical company focused in the development and commercialization of novel therapies for treatment of inflammation and autoimmune diseases, acute cardiac conditions and cancer. As a result of the acquisition, the company acquired an opportunity to continue selling these products through generics sales and marketing organization and leverage the NDA filing.

The acquisition has been accounted for as a purchase of intangible assets as PDL did not meet the definition of a business as described in EITF Issue No. 98-3, Determining Whether a Nonmonetary Transaction Involves Receipt of Productive Assets or of a Business.

The total purchase consideration has been allocated to the acquired assets as of March 31, 2006 based on a fair valuation carried out by the Management as follows:

Inventory	Rs.115,845
Trademarks	Rs.6,846
	Rs.122,691

The value attributable to the brands are amortized over the period over which the intangible assets are expected to contribute directly or indirectly to the future cash flows.

5. GOODWILL

The Company follows SFAS No. 142, "Goodwill and Other Intangible Assets" and accordingly tests goodwill for impairment, at least annually. The carrying value of the goodwill (including goodwill arising on investment in affiliates of Rs.181,943) on the date of adoption of SFAS No. 142 was Rs.1,473,605.

The following table presents the changes in goodwill during the years ended March 31, 2005 and 2006:

	YEAR ENDED MARCH 31,	
	2005	2006
Balance at the beginning of the period	Rs.1,704,492	Rs.1,743,442
Acquired during the period	38,950	15,073,010
Balance at the end of the period	**Rs.1,743,442**	**Rs.16,816,452**

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

Goodwill acquired during the period ended March 31, 2005 and 2006 represents the following:

	YEAR ENDED MARCH 31,	
	2005	2006
Cash paid towards contingent consideration in purchase business combinations	Rs.38,950	Rs.114,244
Excess of cost over the fair value of acquired, net assets, in a purchase business combination (beta Holding GmbH)	–	14,958,766
	Rs.38,950	Rs.15,073,010

The following table presents the allocation of Goodwill to the following segments:

	AS OF MARCH 31, 2006	
	2005	2006
Formulations	Rs.349,774	Rs.349,774
Active pharmaceutical Ingredients and Intermediates	997,025	997,025
Generics	306,206	15,379,216
Drug Discovery	90,437	90,437
	Rs.1,743,442	Rs.16,816,452

6. **INTANGIBLE ASSETS, NET**

The Company follows SFAS No.142, "Goodwill and other intangible assets" and accordingly intangible assets are amortized over the expected benfit period or the legal life, whichever is lower. The carrying value of intagible assets on the date of adoption was Rs.1,276,397.

The following table presents acquired and amortized intangible assets as at March 31, 2005 and 2006:

	AS OF MARCH 31, 2005		AS OF MARCH 31, 2006	
	Gross carrying amount	Accumulated amortization	Gross carrying amount	Accumulated amortization
Trademarks	Rs.2,570,242	Rs.1,833,303	Rs.2,575,224	Rs.2,113,374
Trademarks not subject to amortisation	–	–	3,970,118	–
Product related intangibles	–	–	11,759,317	77,326
Toll manufacturing contract	–	–	621,058	10,708
Core–technology Rights	132,753	–	132,753	–
Non-compete arrangements	111,289	98,602	128,883	105,019
Marketing know-how	80,000	80,000	80,000	80,000
Marketing rights	94,852	3,659	94,369	9,222
Customer related intangibles including customer contracts	125,156	73,908	167,233	98,799
Others	8,027	5,965	7,556	7,508
	Rs.3,122,319	Rs.2,095,437	Rs.19,536,511	Rs.2,501,956

The aggregate amortization expense for the years ended March 31, 2004, 2005 and 2006 was Rs.382,857, Rs.349,991 and Rs.419,867 respectively.

Estimated amortization expense for the next five years with respect to such assets is as follows:

	YEAR ENDED MARCH 31,
2007	Rs.1,463,808
2008	1,358,792
2009	1,239,464
2010	1,175,376
2011	1,159,714
Thereafter	6,667,283
Total	Rs.13,064,437

The intangible assets (net of amortization) as of March 31, 2006 have been allocated to the following segments:

notes to the consolidated financial statements

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	Formulations	Generics	Customs Pharmaceutical Services	Total
Trademarks	Rs.412,346	Rs.4,019,622	–	Rs.4,431,968
Product related intangibles	–	11,681,991	–	11,681,991
Toll manufacturing contract	–	610,350	–	610,350
Core-technology rights	–	132,753	–	132,753
Non-compete arrangements	–	6,052	17,812	23,864
Customer related intangibles	–	24,082	44,352	68,434
Marketing rights	–	85,147	–	85,147
Others	–	48	–	48
	Rs.412,346	**Rs.16,560,045**	**Rs.62,164**	**Rs.17,034,555**

The intangible assets (net of amortization) as of March 31, 2005 have been allocated to the following segments:

	Formulations	Generics	Total
Trademarks	Rs.647,369	Rs.89,570	Rs.736,939
Core-technology rights	–	132,753	132,753
Non-compete arrangements	–	12,687	12,687
Customer related intangibles	–	51,248	51,248
Marketing rights	–	91,193	91,193
Others	–	2,062	2,062
	Rs.647,369	**Rs.379,513**	**Rs.1,026,882**

7. INCORPORATION OF PERLECAN PHARMA PRIVATE LIMITED

In September 2005, the Company announced the formation of an integrated drug development company, Perlecan Pharma Private Limited ("Perlecan Pharma"), with a total equity of U.S.$52,500 to be contributed jointly by the Company, Citigroup Venture Capital International Growth Partnership Mauritius Limited ("Citigroup Venture") and ICICI Venture Funds Management Company ("ICICI Venture"). Perlecan Pharma will be engaged in the clinical development and out-licensing of New Chemical Entity ("NCE") assets. As part of this arrangement, the Company has transferred all rights and title, including the development and commercialization rights, of four NCE assets to Perlecan Pharma, on March 27,2006 ("the closing date")

As per the arrangement, Citigroup Venture and ICICI Venture will contribute U.S.$22,500 each and the Company will contribute U.S.$7,500 towards Perlecan Pharma's initial equity capital. As a result, the Company will initially own approximately 14.28% of the equity of Perlecan Pharma. In addition, Perlecan Pharma will issue to the Company warrants to purchase 45 million equity shares of Perlecan Pharma, at Re 1.00 per warrant, the exercise of which will be contingent upon the success of certain research and development milestones. If the warrants are fully exercised, then the Company will own approximately 62.5% of the equity shares of Perlecan Pharma.

As of March 31, 2006, the three investors have invested Rs.705,700 (U.S.$ 15,818) in Perlecan Pharma. The Company's share of equity was Rs.100,800 (U.S.$2,259). The Company has also committed to invest an additional amount of Rs.170,000 as its equity contribution in the future. Further, three out of seven directors on the board of Perlecan will be from the Company.

As per the terms of the arrangement, the Company will have the first right to conduct product development and clinical trials on behalf of Perlecan Pharma on an arms length basis subject to the final decision by the board of directors of Perlecan Pharma. The Company's equity in the loss of Perlecan Pharma for the year ended March 31, 2006 amounted to Rs.40,000. Moreover, the research and development expenses incurred by the Company from 1 April 2005 till the closing date of arrangement amounting to Rs.231,023 will be reimbursed by Perlecan Pharma.

However, due to the company's continuing involvement in Perlecan Pharma and its unconditional obligation to fund additional equity to meet its future R & D project cost, the receivable from Perlecan Pharma has been utilized to reduce the carrying value of the Company's investment in equity of Perlecan Pharma as of March 31, 2006 to Rs.Nil, and the balance amount of the receivable aggregating to Rs.170,223 has been recorded as a deferred liability in the balance sheet.

8. CASH, CASH EQUIVALENTS AND RESTRICTED CASH

Cash and cash equivalents as of March 31, 2005 and 2006 amounted to Rs.9,287,864 and Rs.3,712,637 respectively. This excludes restricted cash included in current assets of Rs.57,866 and Rs.1,606,245 as of March 31, 2005 and 2006 respectively and restricted cash included in non-current assets of Rs.Nil and Rs.4,468,840 as on March 31, 2005 and 2006 respectively against the following obligations or commitments of the Company:

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	AS OF MARCH 31	
	2005	2006
Restricted cash – current		
Against performance guarantees issued by the Company	Rs.16,157	Rs.1,394
Against short term loan from State Bank of India	–	1,584,600
Against unclaimed dividend	11,831	12,633
Against other obligations	29,878	7,618
	Rs.57,866	Rs.1,606,245
Restricted cash – non current		
Against long term loan from Citibank	–	4,468,840
Total restricted cash	**Rs.57,866**	**Rs.6,075,085**

The fair values of cash and cash equivalents approximate their carrying values.

9. ACCOUNTS RECEIVABLE

Accounts receivable as of March 31, 2005 and 2006 are stated net of allowance for doubtful accounts. The Company maintains an allowance for doubtful accounts on all accounts receivable, including receivables sold with recourse, based on present and prospective financial condition of the customer and ageing of the accounts receivable after considering historical experience and the current economic environment. Accounts receivable are generally not collateralized.

The activity in the allowance for doubtful accounts receivable is given below:

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Balance at the beginning of the year	Rs.141,949	Rs.139,569	Rs.171,154
Additional provision	19,871	79,442	33,629
Bad debts charged to provision	(22,251)	(47,857)	(16,782)
Balance at the end of the year	**Rs.139,569**	**Rs.171,154**	**Rs.188,001**

10. INVENTORIES

Inventories consist of the following:

	AS OF MARCH 31,	
	2005	2006
Raw materials	Rs.1,008,729	Rs.2,002,246
Stores and spares	316,915	450,658
Work-in-process	1,068,115	1,421,151
Finished goods	1,105,847	3,020,657
	Rs.3,499,606	**Rs.6,894,712**

During the years ended March 31, 2004, 2005 and 2006 the Company recorded an inventory write-down of Rs.31,898, Rs.52,692 and Rs.100,783 respectively, resulting from a decline in the market value of certain finished goods and write down of certain raw materials and these amounts are included in the cost of goods sold.

11. OTHER ASSETS

Other assets consist of the following:

	AS OF MARCH 31,	
	2005	2006
Prepaid expenses	Rs.124,972	Rs.432,680
Advances to suppliers	135,352	367,485
Balances with statutory authorities	193,806	928,423
Deposits	99,896	223,409
Export benefits receivable	215,750	291,210

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	AS OF MARCH 31,	
	2005	2006
Others	693,248	621,383
	1,463,024	2,864,591
Less: Current assets	1,361,578	2,639,818
	Rs.101,446	Rs.224,772

Balances with the statutory authorities represent amounts deposited with the excise authorities and the unutilized excise input credits on purchases. These are regularly utilized to offset the excise liability on the goods produced. Accordingly, these balances have been classified as current assets.

Deposits mainly comprise telephone, premises and other deposits. Others mainly represent receivables of duties and income tax deducted at source on interest received by the Company.

12. PROPERTY, PLANT AND EQUIPMENT, NET

Property, plant and equipment consist of the following:

	AS OF MARCH 31,	
	2005	2006
Land	Rs.519,902	Rs.861,951
Buildings	2,064,956	2,470,029
Plant and machinery	6,947,490	7,966,645
Furniture, fixtures and equipment	734,721	826,370
Vehicles	238,556	288,162
Computer equipment	429,266	514,935
Capital work-in-progress	567,974	1,135,905
	11,502,865	14,063,997
Accumulated depreciation	(4,444,557)	(4,977,666)
	Rs.7,058,308	Rs.9,086,331

Depreciation expense for the years ended March 31, 2004, 2005 and 2006 was Rs.745,596, Rs.959,299 and Rs.1,147,223 respectively.

13. INVESTMENT SECURITIES

Investment securities consist of the following:

	AS OF MARCH 31, 2005				AS OF MARCH 31, 2006			
	Carrying value	Gross unrealized holding gains	Gross unrealized holding losses	Fair value	Carrying value	Gross unrealized holding gains	Gross unrealized holding losses	Fair value
Equity securities	Rs.3,096	Rs.4,787	–	Rs.7,883	Rs.3,096	Rs.8,520	–	Rs.11,617
Debt securities	1,009,785	–	(24,965)	984,820	1,250,020	–	(174,163)	1,075,857
	1,012,881	4,787	(24,965)	992,703	1,253,116	8,520	(174,163)	1,087,474
Non-marketable equity securities	2,728	–	–	2,728	2,728	–	–	2,728
	Rs.1,015,609	Rs.4,787	Rs.(24,965)	Rs.995,431	Rs.1,255,844	Rs.8,520	Rs.(174,163)	Rs.1,090,202
Current								
Mutual fund units	300,000	10,887	–	310,887	14,703	–	–	14,703
	Rs.300,000	Rs.10,887	–	Rs.310,887	Rs.14,703	–	–	Rs.14,703

Dividends from equity securities available for sale, during the years ended March 31, 2004, 2005 and 2006 were Rs.53, Rs.98 and Rs.29 respectively, and are included in other income.

(Gain)/loss on sale of securities during the years ended March 31, 2004, 2005 and 2006 was Rs.(24,786), Rs.(64,997) and Rs.3,924 respectively. Proceeds from sale of available for sale securities were Rs.9,167,150, Rs.13,079,463 and Rs.5,274,899 during the years ended March 31, 2004, 2005 and 2006 respectively.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

14. LEASES

Capital leases

Property, plant and equipment includes Rs.Nil and Rs.222,701 in respect of assets acquired under capital lease and other beneficial right of use, during the years ended March 31, 2005 and 2006.

The amortization charge of Rs.Nil and Rs.678 during the years ended March 31, 2005 and 2006 respectively is included within depreciation. The financial obligations arising from these contractual arrangements are reflected in long-term debt.

Operating leases

The Company leases office and residential facilities under operating lease agreements that are renewable on a periodic basis at the option of both the lessor and the lessee. Rental expense under those leases was Rs.101,845, Rs.198,692 and Rs.229,956 for the years ended March 31, 2004, 2005 and 2006 respectively.

The schedule of future minimum rentals payments in respect of non-cancellable operating leases is set out below:

	Year ended March 31,
2007	Rs.150,051
2008	133,844
2009	95,699
2010	78,482
2011	65,207
Thereafter	154,033
	Rs.677,316

15. INVESTMENT IN AFFILIATES

Reddy Kunshan: Reddy Kunshan is engaged in manufacturing and marketing of active pharmaceutical ingredients and intermediates and formulations in China. During the year ended March 31, 2002, the Company acquired an additional 4.9% interest in Reddy Kunshan for a cash consideration of Rs.47,532. Consequently, the Company's interest in Reddy Kunshan increased to 51%.

Three of the directors of the Company are on the board of directors of Reddy Kunshan, which comprises seven directoRs.Under the terms of the agreement, all decisions with respect to operating activities, significant financing and other activities are taken by the majority approval of at least five of the seven directors of the board. These significant decisions include amendments to the Articles, suspensions of the operations, alterations to the registered capital etc. As the Company does not have the control over the board and as the other partners have significant participating rights, acting on its own, the Company is not in a position to control or take any significant operating decisions of Reddy Kunshan and would require approval of other shareholdeRs.Therefore, the Company has accounted for its interest in Reddy Kunshan under the equity method.

During the year ended March 31, 2005 the Company further invested Rs.49,935 along with one of its other joint venture partners in Reddy Kunshan. Consequently, the Company's interest in Reddy Kunshan increased to 51.2%.

The Company's equity in the loss of Reddy Kunshan for the years ended March 31, 2004, 2005 and 2006 was Rs.44,362 Rs.58,101 and Rs.48,235 respectively. The carrying value of the investment in Reddy Kunshan as of March 31, 2005 and 2006 was Rs.180,894 and Rs.132,659 respectively.

Pathnet: Pathnet is engaged in the business of setting up medical pathology laboratories. The Company acquired a 49% interest in Pathnet on March 1, 2001 for a consideration of Rs.4,000. During the year ended March 31, 2002 the Company further invested Rs.60,310 and has accounted for its 49% interest in Pathnet under the equity method. The carrying value of the investment in Pathnet as of March 31, 2005 was Rs.Nil. During the year ended March 31, 2006, the Company sold its stake in Pathnet and settled the guarantee issued to ICICI bank by paying its share of the outstanding loan amount granted by ICICI to Pathnet.

16. VARIABLE INTEREST ENTITIES

On January 30, 2004, the Company along with two individuals formed APR LLC, a Delaware limited liability company. APR LLC is a development stage enterprise, which is in the process of developing an active pharmaceutical ingredient ("API"). Equity capital of APR LLC consists of Class A equity interests, which are held by two individuals and Class B equity interests held by Dr. Reddy's. The initial contribution for the Class A interests was U.S.$400 (Rs.17,487) in cash. Class A interests carry voting rights and participate in the profits and losses of APR LLC in the normal course of business. Dr. Reddy's contributed U.S.$500 (Rs.21,859) in cash for Class B interests, which was used to acquire intellectual property rights. Class B interests carry certain protective rights only.

Further, Dr. Reddy's has entered into a development and supply agreement under which Dr. Reddy's and APR will collaborate in the development, marketing and sale of API and generic dosages. Under the terms of the agreement, Dr. Reddy's is committed to fund the entire research and development of API. This amount is repayable by APR LLC upon successful commercialization of the product. Under this agreement, the Company has paid U.S.$670 (Rs.29,291), U.S.$ 900 (Rs.39,346) and U.S.$ Nil (Rs.Nil) during the years ended March 31, 2004, 2005 and 2006 respectively to fund ongoing research and development.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

The Company has evaluated this transaction and believes that APR meets the criteria to be a variable interest entity and that the Company, being the primary beneficiary, is required to consolidate APR under the requirements of FIN 46R. Accordingly, on January 30, 2004, the Company recorded the assets, liabilities and the non-controlling interest at a fair value of U.S.$900 (Rs.39,346).

17. FINANCIAL INSTRUMENTS AND CONCENTRATION OF RISK

Concentration of risk: Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of cash equivalents, accounts receivable, investment securities and marketable securities. The Company's cash resources are invested with financial institutions with high investment grade credit ratings. Limits have been established by the Company as to the maximum amount of cash that may be invested with any such single entity. To reduce credit risk, the Company performs ongoing credit evaluations of customeRs.

Pursuant to the terms of an agreement with Par Pharmaceuticals Inc. ("PAR"), the Company supplies certain generic formulations to PAR for further sale to customers in the United States. Under this arrangement the Company sells its products to PAR at an agreed price. Subsequently, PAR remits additional amount based on the ultimate sale proceeds realized from further sales made by it to the end customeRs.As of March 31, 2005 and 2006, receivables from PAR under this arrangement aggregated to Rs.210,463 and Rs.113,684 representing 5.9% and 2.4% of the total receivables and revenues during the years ended March 31, 2004, 2005 and 2006 aggregated to Rs.3,224,647, Rs.1,638,939 and Rs.529,252, representing 16.0%, 8.4% and 2.2% of the total revenues of the Company.

Derivative financial instruments.

The Company enters into certain forward foreign exchange contracts and certain derivative arrangements where the counterparty is generally a bank. The Company does not consider the risk of non-performance by the counterparty to be significant.

The following table presents the aggregate contracted principal amounts of the Company's derivative financial instruments outstanding:

	AS OF MARCH 31,	
	2005	2006
Forward exchange contracts (U.S.$-INR) (sell)	U.S.$30,000	US $ 105,000
Forward exchange contracts (U.S.$-INR) (buy)	U.S.$40,000	US $ 79,500
Forward exchange contracts (GBP/U.S.$) (sell)	GBP 2,000	–
Forwards exchange contracts (EUR / U.S.$) (sell)	–	EUR 36,000
Interest rate swap	–	EUR 75,000

The foreign forward exchange contracts mature between one to six months.

18. RESEARCH AND DEVELOPMENT ARRANGEMENT

The Company undertakes significant portion of the research and development activities relating to drug discovery through its research facilities located in the United States and India. The Company under an existing arrangement also undertakes research and development activities through the Research Foundation, a special purpose entity, organized as a Section 25 company under the Indian Companies Act, to avail certain tax benefits under the Indian Income Tax Rules. At present, the Research Foundation does not undertake research and development activity for any other entity. The operations of the Research Foundation are funded by the Company and as a result this entity has been consolidated in the financial statements. The Company has the first right to use the intellectual property rights relating to patents, copyrights, trademarks and know-how discovered or developed by the Research Foundation.

During the year ended March 31, 2005, the Company entered into an agreement with I-VEN Pharma Capital Limited ("I-VEN") for the joint development and commercialization of generic drug products. As per the terms of the agreement, I-VEN will have the right to fund up to fifty percent of the project costs (development, registration and legal costs) related to these products and the related U.S. Abbreviated New Drug Applications ("ANDA") filed or to be filed in the fiscal years ended March 31, 2005 and March 31, 2006, subject to a maximum contribution of U.S.$56 million. The terms of the arrangement do not require the Company to repay the funds or purchase I-VEN's interest in the event that the Company is not able to develop or commercialize one or more of the products subject to this agreement. However, upon successful commercialization of these products, the Company will pay I-VEN a royalty on net sales at agreed rates for a period of 5 years from the date of commercialization of each product. The first tranche advanced by I-VEN of Rs.985,388 (U.S.$22,500 million) was received on March 28, 2005.

The amount received from I-VEN has been treated as an advance and is being recognized in the income statement as a credit to research and development expenses upon completion of specific milestones as detailed in the agreement. A milestone (i.e. a product filing as per the terms of the agreement) will be completed once the appropriate ANDA has been submitted to the U.S. FDA. Achievement of a milestone entitles the Company to take a credit to the research and development expenses in a fixed amount equal to I-VEN's share of the research and development costs of the product, which share varies depending on whether the ANDA is a Paragraph III or Paragraph IV filing. Accordingly, an amount of Rs.96,239 and Rs.384,488 has been recognized as a reduction to research and development expenses during the years ended March 31, 2005 and 2006 respectively.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

19. BORROWINGS FROM BANKS

The Company had a line of credit of Rs.5,319,000 and Rs.10,760,000 as of March 31, 2005 and 2006, respectively from its bankers for working capital requirements. The line of credit is renewable annually. The credit bears interest at the prime rate of the banks, which averaged 10.25% and 10.5% for rupee borrowings and LIBOR+65 basis points for foreign currency borrowing during the years ended March 31, 2005 and 2006 respectively. As of March 31, 2006, the Company had partly drawn down upon such facilities, for packing credit loans, cash credit and as temporary overdraft facilities, all of which are repayable within one year from the balance sheet date. These borrowings, except for the foreign currency packing credit loan, are secured by inventories, accounts receivable and certain property. The Company has an option to draw down the balance of the line of credit based on its requirements.

20. LONG-TERM DEBT

Long-term debt consists of the following:

	AS OF MARCH 31,	
	2005	2006
Rupee term loan	Rs.31,065	Rs.25,145
Euro loan	–	21,602,000
Obligation under capital lease	–	235,748
	31,065	21,862,893
Less: Current portion		
– Rupee term loan	5,920	5,920
– Euro loan	–	900,083
– Obligation under capital lease	–	19,758
	5,920	925,761
Non Current Portion		
– Rupee term loan	25,145	19,225
– Euro Loan	–	20,701,917
– Obligation under capital lease transaction	–	215,990
	Rs.25,145	Rs.20,937,132

Rupee term loan represents a loan from Indian Renewable Energy Development Agency Limited which is secured by way of hypothecation of specific movable assets pertaining to the Company's solar grid interactive power plant located in Bachupally, Hyderabad.
Euro loan represents a loan from Citibank, N.A., Hong Kong to fund the acquisition of beta Holding GmbH during the year, which is guaranteed by the Company and its wholly owned subsidiaries, OOO DRL, DRLI and DRL U.K. The loan is also subject to certain financial covenants which are in the nature of maintaining certain financial ratios within defined limits.

An interest rate profile of long-term debt is given below:

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Foreign currency loan notes	4 %	4.8%	–
Rupee term loan	2%	2.0%	2.0%
Euro loan	–	–	EURIBOR + 150 bps

A maturity profile of the long-term debt outstanding is as follows:

Maturing in the year ending March 31,	Rupee loan	Euro loan	Capital lease	Total
2007	5,920	900,083	19,758	925,761
2008	5,920	3,600,333	19,761	3,626,014
2009	5,920	3,600,333	19,761	3,626,014
2010	5,920	6,300,583	19,761	6,326,264
2011	1,465	7,200,668	19,761	7,221,894
Thereafter	–	–	136,946	136,946
	Rs.25,145	Rs.21,602,000	Rs.235,748	Rs.21,862,893

The fair value of outstanding payments on the Rupee term loan were Rs.23,573 and Rs.19,953 as of March 31, 2005 and 2006. The fair value of outstanding payments on the Euro loans were Rs.21,602,000 as of March 31, 2006.

21. SHAREHOLDERS EQUITY

Equity shares and dividend

The Company presently has only one class of equity shares. For all matters submitted to vote in the shareholders meeting, every holder of equity shares, as reflected in the records of the Company on the date of the shareholders meeting shall have one vote in respect of each share held.

Indian statutes mandate that the dividends shall be declared out of the distributable profits only after the transfer of up to 10% of net income computed in accordance with current regulations to a general reserve. Should the Company declare and pay dividends, such dividends will be paid in Indian rupees to each holder of equity shares in proportion to the number of shares held by him to the total equity shares outstanding as on that date. Indian statutes on foreign exchange govern the remittance of dividend outside India.

In the event of liquidation of the affairs of the Company, all preferential amounts, if any, shall be discharged by the Company. The remaining assets of the Company, after such discharge, shall be distributed to the holders of equity shares in proportion to the number of shares held by them.

Dividends on common stock are recorded as a liability at the point of their approval by the shareholders in the annual general meeting. The shareholders approved and the Company paid dividends of Rs.431,598, Rs.431,615 and Rs.436,368 during the years ended March 31, 2004, 2005 and 2006 respectively. The dividend per share was Rs.5.00, Rs.5.00 and Rs.5.00 during the years ended March 31, 2004, 2005 and 2006 respectively.

22. DEFERRED REVENUE

The Company had, pursuant to an agreement entered into with Novartis Pharma AG ("Novartis"), agreed to provide Novartis with an exclusive license to develop, promote, distribute, market and sell certain products to be further developed into drugs for the treatment of specified diseases. Pursuant to the terms of the agreement, during the year ended March 31, 2002, the Company received Rs.235,550 (U.S.$5,000) as an up-front license fee. As the up-front license fee did not represent the culmination of a separate earning process, the up-front license fee had been deferred to be recognized in accordance with the Company's accounting policy proportionately upon the receipt of stated milestones payments. The agreement with Novartis for the further development of the compound expired on May 30, 2004 and Novartis has determined to discontinue further development and, accordingly, the Company recognized the entire amount of deferred revenue of Rs.235,550 (U.S.$5,000) as license fees during the year ended March 31, 2005.

The Company had entered into a licensing arrangement with Novo Nordisk A/S in February 1997, whereby the Company had licensed two molecule compounds for further development and conducting clinical trials. Under the arrangement, the Company received a non-refundable upfront license fee upon signing of the agreement and was also entitled to receive certain additional non-refundable payments upon the achievement of certain defined milestones. As of March 31, 2004, the Company had unamortized non-refundable upfront license fees of Rs.52,832 (U.S.$1,273) on account of the second molecule compound. On October 22, 2004, Novo Nordisk announced that it had suspended clinical trials on the second compound also due to unsatisfactory results. Accordingly, the Company has recognized the entire amount of deferred revenue of Rs.52,832 (U.S.$1,273) as license fees during the year ended March 31, 2005.

The Company has entered into certain dossier sales, licensing and supply arrangements in Europe and Japan. These arrangements include certain performance obligations and based on an evaluation that these obligations are not inconsequential or perfunctory, the Company has deferred the upfront payments of Rs.33,757 received towards these arrangements. These amounts will be recognized in the income statement in the period in which the Company completes all its performance obligations.

Upon completion of all its performance obligation for some of the contracts, the Company recognized an amount of Rs.7,355 and Rs.47,521 in the income statement during the years ended March 31, 2005 and 2006 respectively. The balance amounts aggregating to Rs.58,255 and Rs.56,466 as of March 31, 2005 and 2006 respectively represent the deferred revenue relating to these arrangements.

23. EMPLOYEES STOCK INCENTIVE PLANS

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 September 24, 2001. The DRL 2002 Plan covers all employees of Dr. Reddy's and all employees and directors of its subsidiaries. Under the DRL 2002 Plan, the Compensation Committee of the Board (the "Compensation Committee") shall administer the DRL 2002 Plan and grant stock options to eligible employees of the Company and its subsidiaries. The 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 DRL 2002 Plan was amended on July 28, 2004 at the annual general meeting of shareholders to provide for stock option grants in two categories:

Category A: 1,721,700 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: 573,778 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., Rs.5 per option).

The DRL 2002 Plan was further amended on July 27, 2005 at the annual general meeting of shareholders to provide 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

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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., Rs.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 for 30 days prior to the grant in the stock exchange where there is highest trading volume during that period. Notwithstanding the foregoing, the Compensation 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.

Stock option activity under the DRL 2002 Plan in the two categories of options (i.e. fair market value and par value options) was as follows:

CATEGORY A – FAIR MARKET VALUE OPTIONS — YEAR ENDED MARCH 31, 2005

	Shares arising out of options	Range of exercise prices	Weighted-average exercise price	Weighted-average remaining contractual life (months)
Outstanding at the beginning of the period	911,038	Rs.883-1,396	Rs.968.95	66
Granted during the period	466,500	747-885	872.82	82
Expired / forfeited during the period	(352,657)	765-1,063.02	918.84	–
Surrendered by employees during the period in exchange of category B options	(725,931)	747-1,396	928.07	–
Exercised during the period	–	–	–	–
Outstanding at the end of the period	298,950	747-1149	977.31	50
Exercisable at the end of the period	188,538	Rs.883-1,149	Rs.996.54	35

CATEGORY B – PAR VALUE OPTIONS — YEAR ENDED MARCH 31, 2005

	Shares arising out of options	Range of exercise prices	Weighted-average exercise price	Weighted-average remaining contractual life (months)
Outstanding at the beginning of the period	–	–	–	–
Granted during the period				
In exchange for category A surrendered options	280,873	Rs.5	Rs.5	84
New options	102,650	5	5	84
Forfeited during the period	(3,974)	5	5	–
Exercised during the period	–	–	–	–
Outstanding at the end of the period	379,549	Rs.5	Rs.5	84
Exercisable at the end of the period	–	–	–	–

CATEGORY A – FAIR MARKET VALUE OPTIONS — YEAR ENDED MARCH 31, 2006

	Shares arising out of options	Range of exercise prices	Weighted-average exercise price	Weighted-average remaining contractual life (months)
Outstanding at the beginning of the period	298,950	Rs.747-1,149	Rs.977.31	50
Granted during the period	32,500	725	725	81
Expired / forfeited during the period	(46,700)	725-1,149	994.35	–
Surrendered by employees during the period	(90,000)	977.30-1,063.02	1,034.45	–
Exercised during the period	(77,500)	883-977.30	943.84	–
Outstanding at the end of the period	117,250	725-1,063.02	878.85	64
Exercisable at the end of the period	37,882	Rs.725-1,063.02	Rs.943.85	45

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

CATEGORY B – PAR VALUE OPTIONS

YEAR ENDED MARCH 31, 2006	Shares arising out of options	Range of exercise prices	Weighted-average exercise price	Weighted-average remaining contractual life (months)
Outstanding at the beginning of the period	379,549	Rs.5	Rs.5	84
Granted during the period	216,860	5	5	81
Forfeited during the period	(133,304)	5	5	–
Exercised during the period	(98,121)	5	5	–
Outstanding at the end of the period	364,984	5	5	81
Exercisable at the end of the period	18,136	Rs.5	Rs.5	59

The weighted average grant date fair value of options granted under the DRL 2002 Plan at fair market value during the years ended March 31, 2005 and March 31, 2006 was Rs.377.60 and Rs.293.42 respectively. The weighted average grant date fair value for options granted under the DRL 2002 Plan at par value during the years ended March 31, 2005 and March 31, 2006 was Rs.707.40 and Rs.705.88 respectively.

Aurigene Discovery Technologies Ltd. Employees Stock Option Plan (the "Aurigene ESOP Plan"):

In fiscal 2004, Aurigene Discovery Technologies Limited ("Aurigene"), a consolidated subsidiary, adopted the Aurigene ESOP Plan to provide for issuance of stock options to employees. Aurigene has reserved 4,550,000 of its ordinary shares for issuance under this plan. Under the Aurigene ESOP Plan, stock options may be granted at a price per share as may be determined by the Compensation Committee. The options vest at the end of three years from the date of grant of option.

Stock option activity under the Aurigene ESOP Plan was as follows:

YEAR ENDED MARCH 31, 2005	Shares arising out of options	Range of exercise prices	Weighted-average exercise price	Weighted-average remaining contractual life (months)
Outstanding at the beginning of the period	169,188	Rs.10	Rs.10	65
Granted during the period	342,381	10	10	61
Expired / forfeited during the period	(314,391)	10	10	–
Outstanding at the end of the period	197,178	Rs.10	Rs.10	59
Exercisable at the end of the period	–	–	–	–

YEAR ENDED MARCH 31, 2006	Shares arising out of options	Range of exercise prices	Weighted-average exercise price	Weighted-average remaining contractual life (months)
Outstanding at the beginning of the period	197,178	Rs.10	Rs.10	59
Granted during the period	500,000	10	10	70
Expired / forfeited during the period	(168,271)	10	10	–
Outstanding at the end of the period	528,907	Rs.10	Rs.10	67
Exercisable at the end of the period	–	–	–	–

The weighted average grant date fair value for options granted under the Aurigene ESOP Plan during the years ended March 31, 2005 and March 31, 2006 was Rs.4.29 and Rs.4.01 respectively.

Aurigene Discovery Technologies Ltd. Management Group Stock Grant Plan (the "Management Plan"):

In fiscal 2004, Aurigene adopted the Management Plan to provide for issuance of stock options to management employees of Aurigene and its subsidiary Aurigene Discovery Technologies Inc. Aurigene has reserved 2,950,000 ordinary shares for issuance under this plan. Under the Management Plan, stock options may be granted at a price per share as may be determined by Aurigene's compensation committee. The options vest on the date of grant of the options.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

Stock option activity under the Management Plan was as follows:

YEAR ENDED MARCH 31, 2005	Shares arising out of options	Range of exercise prices	Weighted average exercise price	Weighted average remaining contractual life (months)
Outstanding at the beginning of the period	616,666	Rs.10	Rs.10	77
Granted during the period	616,667	10	10	73
Expired during the period	(1,133,333)	10	10	–
Outstanding at the end of the period	100,000	Rs.10	Rs.10	65
Exercisable at the end of the period	100,000	Rs.10	Rs.10	65

YEAR ENDED MARCH 31, 2006	Shares arising out of options	Range of exercise prices	Weighted average exercise price	Weighted average remaining contractual life (months)
Outstanding at the beginning of the period	100,000	Rs.10	Rs.10	65
Granted during the period	–	–	–	–
Expired during the period	(100,000)	10	10	–
Outstanding at the end of the period	–	–	–	–
Exercisable at the end of the period	–	–	–	–

The weighted average grant date fair value for options granted under the Aurigene Management Plan during the year ended March 31, 2005 was Rs.3.76.

24. ALLOWANCES FOR SALES RETURNS

Product sales are net of allowances for sales returns. The activity in the allowance for sales returns is given below:

YEAR ENDED MARCH 31,	2004	2005	2006
Balance at the beginning of the year	Rs.89,026	Rs.99,919	Rs.95,123
Acquired during the year	–	–	51,251
Additional provision	169,511	105,245	239,462
Sales returns charged to the provision	(158,618)	(110,041)	(217,480)
Balance at the end of the year	**Rs.99,919**	**Rs.95,123**	**Rs.168,356**

25. OTHER (EXPENSE)/INCOME, NET

Other (expense)/ income consists of the following:

YEAR ENDED MARCH 31,	2004	2005	2006
Interest expense,	Rs.(14,970)	Rs.(103,027)	Rs.(298,603)
Interest income	421,763	374,928	717,410
Gain / (loss) on sale of available for sale securities, net	24,786	64,997	(3,924)
Other	104,330	117,339	118,723
	Rs.535,909	**Rs.454,237**	**Rs.533,606**

26. SHIPPING COSTS

Selling, general and administrative expenses include shipping and handling costs of Rs.557,969, Rs.642,508 and Rs.823,883 for the years ended March 31, 2004, 2005 and 2006 respectively.

notes to the consolidated financial statements

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

27. INCOME TAXES

Income taxes consist of the following:

	YEAR ENDED MARCH 31,		
	2004	**2005**	**2006**
Pre-tax income			
Domestic	Rs.3,021,098	Rs.562,343	Rs.2,144,176
Foreign	(481,060)	(455,314)	(256,853)
	Rs.2,540,038	**Rs.107,029**	**Rs.1,887,323**
Income tax benefit / (expense) attributable to continuing operations:			
Current taxes:			
Domestic	Rs.(202,364)	Rs.(250)	Rs.(279,466)
Foreign	(1,752)	(1,053)	(34,081)
	(204,116)	**(1,303)**	**(313,547)**
Deferred taxes:			
Domestic	20,126	190,087	(48,503)
Foreign	114,741	(94,507)	103,660
	134,867	**95,580**	**55,157**
	Rs.(69,249)	**Rs.94,277**	**Rs.(258,390)**
Deferred tax benefit / (expense) attributable to other comprehensive income.	**Rs.(3,873)**	**Rs.5,206**	**Rs.35,079**

The reported income tax expense differed from amounts computed by applying the enacted tax rates to income / (loss) before income taxes as a result of the following:

	YEAR ENDED MARCH 31,		
	2004	**2005**	**2006**
Income before income taxes and minority interest	Rs.2,540,038	Rs.107,029	Rs.1,887,323
Enacted tax rate in India	35.875%	36.5925%	33.66%
Computed expected tax benefit expense	Rs.(911,239)	Rs.(39,164)	Rs.(635,272)
Effect of:			
Differences between Indian and foreign tax rates	(2,325)	13,362	(8,546)
Valuation allowance	(149,805)	(254,243)	(142,206)
In-process technology written-off	–	(110,771)	–
Expenses not deductible for tax purposes	(39,149)	(36,552)	(67,403)
ESOP cost not deductible for tax purpose	(43,831)	(52,694)	(54,614)
Income exempt from income taxes	856,317	333,310	538,151
Foreign exchange (loss) / gain	64,008	(5,300)	8,335
Incremental deduction allowed for research and development expenses	172,259	254,245	166,308
Indexation of capital assets	907	8,275	1,413
Tax rate change	12,111	(9,466)	12,534
Minimum alternate tax	(639)	(3,910)	(3,019)
Tax provision for earlier years	–	–	(73,970)
Others	(27,863)	(2,815)	(101)
Income tax benefit / (expense)	**Rs.(69,249)**	**Rs.94,277**	**Rs.(258,390)**

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

The tax effects of significant temporary differences that resulted in deferred tax assets and liabilities and a description of the items that create these differences is given below:

	AS OF MARCH 31,	
	2005	2006
Deferred tax assets:		
Inventory	Rs.62,644	47,407
Deferred revenue	5,868	7,957
Minimum Alternate Tax	–	140,400
Accounts payable	46,300	47,655
Investments	93,762	169,737
Operating loss carry-forward	874,187	1,320,961
Capital loss carry forward	36,890	44,622
Expenses deferred for tax purposes		
Research and development expenses	52,026	47,787
Employee costs	62,009	34,062
Legal costs	66,647	33,269
Start-up costs	42,138	37,460
Others	31,824	15,464
Other current liabilities	96,265	179,178
	1,470,560	2,125,959
Less: Valuation allowance	(781,392)	(923,598)
Deferred tax assets	**689,168**	**1,202,361**
Deferred tax liabilities		
Property, plant and equipment	(876,483)	(824,174)
Intangible assets	(134,054)	(6,425,661)
Investment securities	(14,094)	(12,964)
Others	(45,518)	(162,691)
Deferred tax liabilities	**(1,070,149)**	**(7,425,490)**
Net deferred tax assets / (liabilities)	(380,981)	(6,223,129)
Deferred charges	66,123	50,705
	Rs.(314,858)	**Rs.(6,172,424)**

In assessing the realizability of deferred tax assets, management considers whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. The ultimate realization of the deferred tax assets and tax loss carry forwards is dependent upon the generation of future taxable income during the periods in which the temporary differences become deductible. Management considers the scheduled reversal of the projected future taxable income and tax planning strategy in making this assessment. Based on the level of historical taxable income and projections for future taxable incomes over the periods in which the deferred tax assets are deductible, management believes that it is more likely than not the Company will realize the benefits of those deductible differences and tax loss carry forwards, net of the existing valuation allowances. The amount of the deferred tax assets considered realizable, however, could be reduced in the near term if estimates of future taxable income are reduced.

Operating loss carry forward comprises business losses and unabsorbed depreciation. The period for which such losses can be carried forward differs from five years to indefinite.

The company has during the year, set up a full valuation allowance against the deferred tax asset on account of tax effect of operating and capital losses carry forward and other net deferred tax assets of AMPNH, RNBV, RPI, RANV, RPS, RBL, RCSA, DRSA, DRFBL, Reddy US and others amounting to Rs.110,510 as the management based on future profit projections believes that the likelihood of not realizing these deferred tax assets is more likely than not.

Valuation allowance has been created with regard to operating losses and other net deferred tax assets arising out of ADTL, ADLINC, RUSTI amounting to Rs.33,355 as these subsidiaries specializes in research activities and the Company believes that the likelihood of not realizing these deferred tax assets is more likely than not.

Income exempt from tax represents export earnings exempt for tax purposes and earnings derived from units set up in backward areas for which the Company is eligible for tax concessions under the local laws.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

Incremental deduction allowed for research and development expenses represents tax incentive provided by the Government of India for carrying out such activities.

As of March 31, 2006 the Company had operating and capital loss carry-forward of Rs.3,558,808 that expires as follows:

Expiring in the year ending March 31:	
2007	21,931
2008	217,651
2009	14,576
2010	–
2011	–
Thereafter (2012 – 2024)	1,007,767
Thereafter (indefinite)	2,296,883
	Rs.3,558,808

Operating loss carry forward includes unabsorbed depreciation of Rs.107,832, which can be carried forward indefinitely. Further, as of March 31, 2006 the Company had capital loss carry forward of Rs.176,422 that expires on March 31, 2013 and Rs.22,430 that expires on March 31, 2014 and the valuation allowance has been created for the same.

Undistributed earnings of the Company's foreign subsidiaries and unrecognized deferred tax liability on the same amounted to approximately Rs.245,906 Rs.273,274, Rs.307,012 and Rs.88,219, Rs.100,163, Rs.103,340 as of March 31, 2004, 2005 and 2006 respectively. Such earnings are considered to be indefinitely reinvested and, accordingly no provision for income taxes has been recorded on the undistributed earnings.

28. EARNINGS PER SHARE

A reconciliation of the equity shares used in the computation of basic and diluted earnings per equity share is set out below:

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Basic earnings per equity share – weighted average number of equity shares outstanding	76,513,764	76,518,949	76,546,658
Effect of dilutive equivalent shares-stock options outstanding	35,834	40,852	155,265
Diluted earnings equity share – weighted average number of equity shares and equivalent shares outstanding	76,549,598	76,559,801	76,701,923

29. EMPLOYEE BENEFIT PLANS

Gratuity benefits: In accordance with applicable Indian laws, the Company provides for gratuity, a defined benefit retirement plan (the "Gratuity Plan") covering certain categories of employees. The Gratuity Plan provides a lump sum payment to vested employees, at retirement or termination of employment, an amount based on the respective employee's last drawn salary and the years of employment with the Company. Effective September 1, 1999, the Company established Dr. Reddy's Laboratories Gratuity Fund (the "Gratuity Fund"). Liabilities with regard to the Gratuity Plan are determined by an actuarial valuation, based upon which the Company makes contributions to the Gratuity Fund. Trustees administer the contributions made to the Gratuity Fund. The amounts contributed to the Gratuity Fund are invested in specific securities as mandated by law and generally consist of federal and state government bonds and the debt instruments of government-owned corporations.

In respect of certain other employees of the Company, the gratuity benefit is provided through annual contribution to separate funds managed by the Life Insurance Corporation of India ("LIC") and ICICI Prudential Life Insurance Company Limited ("ICICI Pru"). Under this scheme, the settlement obligation remains with the Company, although the LIC and ICICI Pru administer the funds and determines the contribution premium required to be paid by the Company.

The following table sets out the funded status of the Gratuity Plan and the amounts recognized in the Company's financial statements:

	AS OF MARCH 31,	
	2005	2006
Change in the benefit obligations		
Projected Benefit Obligations (PBO) at the beginning of the year	Rs.147,309	Rs.200,039
Service cost	20,379	26,926
Interest cost	10,217	15,255

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	AS OF MARCH 31,	
	2005	2006
Actuarial (gain)/ loss	34,362	(14,384)
Benefits paid	(12,228)	(19,800)
PBO at the end of the year	**Rs.200,039**	**Rs.208,036**
Change in plan assets		
Fair value of plan assets at the beginning of the year	Rs.130,939	Rs.127,122
Actual return on plan assets	(26,003)	11,066
Employer contributions	34,414	101,882
Benefits paid	(12,228)	(19,800)
Plan assets at the end of the year	**Rs.127,122**	**Rs.220,270**
Funded status	Rs.(72,917)	12,234
Unrecognized actuarial loss	92,014	68,560
Unrecognized transitional obligation	12,146	–
Net amount recognized	**Rs.31,243**	**Rs.80,794**

Amounts recognized in the statement of financial position consist of:

	YEAR ENDED MARCH 31,	
	2005	2006
Prepaid benefit cost	Rs.35,231	Rs.85,991
Accrued benefit liability	(3,988)	(5,197)
Net amount recognized	**Rs.31,243**	**Rs.80,794**

The accumulated benefit obligation for the Gratuity Plan was Rs.105,931 and Rs.112,873 as at March 31, 2005 and 2006 respectively.

Components of net periodic benefit cost:

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Service cost	Rs.16,061	Rs.20,379	Rs.26,926
Interest cost	8,992	10,217	15,255
Expected return on plan assets	(8,831)	(10,468)	(9,211)
Amortization of transition obligation / (assets)	770	770	12,146
Recognized net actuarial (gain) / loss	881	288	7,215
Net amount recognized	**Rs.17,873**	**Rs.21,186**	**Rs.52,331**

Summary of the actuarial assumptions: The actuarial assumptions used in accounting for the Gratuity Plan are:
Weighted-average assumptions used to determine benefit obligations:

	AS AT MARCH 31,	
	2005	2006
Discount rate	8.0%	8%
Rate of compensation increase	7.0%	8% p.a. for first 5 years and 6% p.a. thereafter.

Weighted-average assumptions used to determine net periodic benefit cost:

	YEAR ENDED MARCH 31,	
	2005	2006
Discount rate	8.0%	8%
Rate of compensation increase	7.0%	8% p.a. for first 5 years and 6% p.a. thereafter
Expected long-term return on plan assets	7.5%	7.50%

The expected long-term return on plan assets is based on the expectation of the average long-term rate of return expected to prevail over the next 15 to 20 years on the types of investments prescribed as per the statutory pattern of investment.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

Plan assets: The Company's gratuity plan weighted-average asset allocations at March 31, 2005 and 2006, by asset category are as follows:

	YEAR ENDED MARCH 31,	
	2005	2006
Debt	100%	63%
Funds managed by LIC	–	37%

Contributions: The Company expects to contribute Rs.10,098 to its gratuity plan during the year ending March 31, 2007

Estimated future benefit payments: The following benefit payments are expected to be paid:

Year ended March 31,	
2007	Rs.18,828
2008	20,166
2009	25,495
2010	23,692
2011	27,513
2012 to 2015	174,756

Superannuation benefits: Apart from being covered under the Gratuity Plan described above, the senior officers of the Company also participate in a superannuation, a defined contribution plan administered by the LIC. The Company makes annual contributions based on a specified percentage of each covered employee's salary. The Company has no further obligations under the plan beyond its annual contributions. The Company contributed Rs.24,192, Rs.26,994 and Rs.24,832 to the superannuation plan during the years ended March 31, 2004, 2005 and 2006 respectively.

Provident fund benefits: In addition to the above benefits, all employees receive benefits from a provident fund, a defined contribution plan. Both the employee and employer each make monthly contributions to the plan each equal to 12% of the covered employee's salary. The Company has no further obligations under the plan beyond its monthly contributions. The Company contributed Rs.58,685, Rs.64,223 and Rs.64,443 to the provident fund plan during the years ended March 31, 2004, 2005and 2006 respectively.

Pension plan: All the employees of Falcon are governed by a Defined Benefit Plan in the form of Pension Plan. The pension plan provides a payment to vested employees at retirement or termination of the employment. This payment is based on the employee's integrated salary and is paid in the form of a monthly pension over a period of 20 years computed based on a predefined formula. Liabilities with regard to the Pension Plan are determined by an actuarial valuation, based upon which the company makes contributions to the Pension Fund. This fund is administered by a third party who is provided guidance by a technical committee formed by senior employees of the company.

The following table sets out the funded status of the Pension Plan and the amounts recognized in the Company's financial statements:

	AS OF MARCH 31,
	2006
Change in the benefit obligations	
Projected Benefit Obligations (PBO) as on January 1, 2006	Rs.275,001
Service cost	4,173
Interest cost	3,490
Actuarial (gain)/ loss	892
Benefits paid	–
Inflationary effect over initial balance	2,383
PBO at the end of the year	**285,939**
Change in plan assets	
Fair value of plan assets at the beginning of the year	246,173
Actual return on plan assets	2,947
Employer contributions	–
Benefits paid	–
Inflationary effect over initial balance	2,134
Plan assets at the end of the year	**251,254**
Funded status	(34,685)
Unrecognized actuarial gain	(711)
Unrecognized transitional obligation	–
Net amount recognized	**Rs.(35,396)**

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

Amounts recognized in the statement of financial position consist of:

	AS OF MARCH 31, 2006
Prepaid pension cost	Rs.–
Accrued benefit liability	(35,396)
Net amount recognized	**Rs.(35,396)**

Components of net periodic benefit cost:

	YEAR ENDED MARCH 31, 2006
Service cost	Rs.4,137
Interest cost	3,460
Expected return on plan assets	(3,725)
Amortisation of unrecognized net transition obligation / (assets)	–
Cost price inflation index adjustment over net periodic pension cost	43
Net periodic pension cost adjusted by cost price inflation index	**Rs.3,915**

Summary of the actuarial assumptions: The actuarial assumptions used in accounting for the Pension Plan are:
Weighted-average assumptions used to determine benefit obligations:

	AS AT MARCH 31, 2006
Discount rate	5.25%
Rate of compensation increase	0.75%

Weighted-average assumptions used to determine net periodic benefit cost:

	YEAR ENDED MARCH 31, 2006
Discount rate	5.25%
Rate of compensation increase	2.00%
Expected long-term return on plan assets	7.75%
Inflation rate of fiscal year	0.87%

Plan assets: The Company's pension plan weighted-average asset allocations, by asset category are as follows:

	YEAR ENDED MARCH 31, 2006
Equity	27%
Debt	73%

Estimated future benefit payments: The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

	Year ended March 31,
2007	Rs.23,473
2008	28,118
2009	28,490
2010	26,143
2011	28,391
2012 to 2017	Rs.150,502

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

30. RELATED PARTY TRANSACTIONS

The Company has entered into transactions with the following related parties:

- Diana Hotels Limited for availing hotel services
- AR Chlorides for availing processing services of raw materials and intermediates
- Dr. Reddy's Holdings Private Limited for purchase and sale of active pharmaceutical ingredients and intermediates
- Madras Diabetes Research Foundation for undertaking research on behalf of the Company
- Dr. Reddy's Heritage Foundation for purchase of services
- SR Enterprises for transportation services
- Manava Seva Dharma Samvardhani Trust for social contribution to which the Company has made contribution.

The directors of the Company have either a significant ownership interest, controlling interest or exercise significant influence over these entities ("significant interest entities").

The Company has carried out transactions with its two affiliates Perlecan Pharma and Reddy Kunshan. These transactions are in the nature of reimbursement of research and development expenses by Perlecan Pharma and purchase of active pharmaceutical ingredients by the Company from Reddy Kunshan. The Company has also entered into transactions with employees, directors of the Company and their relatives.

One of the Company's executives and U.S. general counsel, hired on July 15, 2002, is a partner of a law firm that the Company engages for provision of legal services. Legal fees paid by the Company to the concerned law firm were Rs.423,137, Rs.468,758 and Rs.466,567 during the years ended March 31, 2004, 2005 and 2006 respectively.

The following is a summary of significant related party transactions:

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Purchases from:			
Significant interest entities	Rs.59,889	Rs.45,239	Rs.182,870
Affiliates	107,801	39,278	5,410
Sales to:			
Significant interest entities	1,185	1,055	32,255
Lease rental paid under cancelable operating leases to: Directors and their relatives	16,891	17,144	18,927
Administrative expenses paid to: Significant interest entities	4,793	4,649	7,401

The Company has the following amounts due from related parties:

	AS OF MARCH 31,	
	2005	2006
Significant interest entities	–	Rs.6,084
Directors and their relatives	Rs.3,680	4,380
Employee loans (interest free)	18,199	7,537
Affiliates	–	234,541
	Rs.21,879	Rs.252,542

The Company has the following amounts due to related parties:

	AS OF MARCH 31,	
	2005	2006
Significant interest entities	Rs.16,397	Rs.18,958
Payable towards legal fees	123,106	131,392
Directors and their relatives	–	1,328
	Rs.139,503	Rs.151,678

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

As of March 31, 2006, the required repayments of employee loans are given below:

Repayable in the year ending March 31:	
2007	Rs.5,735
2008	1,448
2009	296
2010	58
2011	–
Thereafter	–
	Rs.7,537

31. COMMITMENTS AND CONTINGENCIES

Capital Commitments: As of March 31, 2005 and 2006, the Company had committed to spend approximately Rs.192,161 and Rs.744,006 respectively, under agreements to purchase property and equipment. The amount is net of capital advances paid in respect of such purchases.

Guarantees: The Company adopted the provisions of FASB Interpretation No. 45, Guarantor's Accounting and Disclosure Requirements for Guarantees, including Indirect Guarantees of Indebtedness of OtheRs.The Interpretation requires that the Company recognize the fair value of guarantee and indemnification arrangements issued or modified by the Company after December 31, 2002, if these arrangements are within the scope of that Interpretation. In addition, under previously existing generally accepted accounting principles, the Company continues to monitor the conditions that are subject to the guarantees and indemnifications to identify whether it is probable that a loss has occurred, and would recognize any such losses under the guarantees and indemnifications when those losses are estimable.

The Company has entered into a guarantee arrangement which arose in transactions related to enhancing the credit standing and borrowings of its affiliate Pathnet.

Pathnet, an equity investee accounted for by the equity method, secured a credit facility of Rs.250 million from ICICI Bank Ltd. ("ICICI Bank"). To enhance the credit standing of Pathnet, on December 14, 2001 the Company issued a corporate guarantee amounting to Rs.122.5 million in favor of ICICI Bank. In July 2005, the Company was released by ICICI Bank from this guarantee when its share of the outstanding loan amount, Rs.21.0 million, was repaid. During the year ended March 31, 2006 the Company sold its stake in Pathnet and settled the guarantee issued to ICICI bank by paying its share of the envoked guarantee by ICICI.

KRRP secured a financial assistance of Rs.32 million from Citi Bank,N.A. To enhance the credit standing of KRRP the Company issued during the year a corporate guarantee amounting to Rs.45,000 in favor of Citibank. The guarantee has to be renewed every year and the liability of the Company may arise in case of non-payment or non-performance of other obligations of KRRP under its facilities agreement with Citi Bank. As of March 31, 2006, it is not probable that the company will be required to make payments under the guarantee. Hence, no liability has been accrued for a loss related to company's obligation under this guarantee arrangement.

Litigations / Contingencies: The Company manufactures and distributes Norfloxacin, a formulations product. Under the Drugs Prices Control Order (the "DPCO"), the Government of India has the authority to designate a pharmaceutical product as a "specified product" and fix the maximum selling price for such product. In 1995, the Government of India notified Norfloxacin as a "specified product" and fixed the maximum selling price. In 1996, the Company filed a statutory Form III before the Government of India for the upward revision of the price and a legal suit in the Andhra Pradesh High Court (the "High Court") challenging the validity of the notification on the grounds that the applicable rules of the DPCO were not complied with while fixing the ceiling price. The High Court had earlier granted an interim order in favor of the Company, however it subsequently dismissed the case in April 2004. The Company filed a review petition in the High Court in April 2004 which was also dismissed by the High Court in October 2004. Subsequently the Company appealed to the Supreme court of India by filing a Special Leave Petition. The appeal is currently pending with the Supreme Court.

During the year ended March 31, 2006 the Company received a demand from the Government of India amounting to Rs.284,984 towards the overcharged amount and interest thereon. The Company filed a writ petition in the High Court challenging the Government of India's demand order. The High Court has admitted the writ petition and granted an interim order, however it ordered the Company to deposit 50% of the principal amount claimed by the Government of India, which amounts to Rs.77,149. The Company deposited this amount with the Government of India on November 14, 2005 whilst it awaits the outcome of its appeal with the Supreme Court. The Company has provided fully against the potential liability in respect of the principal amount demanded and believes that the possibility of any liability that may arise on account of interest and penalty is remote.

During the year ended March 31, 2003, the Central Excise Authorities of India (the "Authorities") issued a demand notice on one of the Company's vendors with regard to the assessable value of its products supplied to the Company. The Company has been named as a co-defendant in the notice. The Authorities demanded payment of Rs.175,718 from the vendor including a penalty of Rs.90,359. The Authorities, through the same notice, issued a penalty claim of Rs.70,000 against the Company.

During the year ended March 31, 2005, the Authorities issued an additional notice on the vendor demanding Rs.225,999 from the vendor including a penalty of Rs.51,152. The Authorities, through the same notice, issued a penalty claim of Rs.6,500 against the company. Further, during the year ended March 31, 2006, the Authorities issued an additional notice on the vendor demanding payment of Rs.33,549. The Company has filed appeals against these notices. Pending resolution of these appeals, the Company believes that the possibility of any liability that may arise on account of these notices is remote.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

The Indian Council for Environmental Legal Action filed a writ in 1989 under Article 32 of the Constitution of India against the Union of India and others in the Supreme Court of India for the safety of people living in the Patancheru and Bollarum areas of Medak district of Andhra Pradesh. The Company has been named in the list of polluting industries.

In 1996, the Andhra Pradesh District Judge proposed that the polluting industries compensate farmers in the Patancheru, Bollarum and Jeedimetla areas for discharging effluents which damaged the farmers' agricultural land. The compensation was fixed at Rs.1.3 per acre for dry land and Rs.1.7 per acre for wet land over the following three yeaRs.Accordingly, the Company has paid a total compensation of Rs.2,013. The matter is still pending in the courts and the possibility of additional liability is remote. The Company would not be able to recover the compensation paid, even if the decision of the court is in its favor.

Additionally, the Company is also involved in other lawsuits, claims, investigations and proceedings, including patent and commercial matters, which arise in the ordinary course of business. However, there are no such matters pending that the Company expects to be material in relation to its business.

32. SEGMENT REPORTING AND RELATED INFORMATION

a) Segment information

The Chief Operating Decision Maker ("CODM") evaluates the Company's performance and allocates resources based on an analysis of various performance indicators by product segments. The product segments and the respective performance indicators reviewed by the CODM are as follows:

- Formulations – Revenues by therapeutic product category; Gross profit
- Active pharmaceutical ingredients and intermediates – Gross profit, revenues by geography and revenues by key products;
- Generics– Gross profit;
- Critical care and biotechnology – Gross profit;
- Drug discovery – Revenues and expenses; and
- Customs Pharmaceutical Services- Gross profit

The CODM of the Company does not review the total assets for each reportable segment. The property and equipment used in the Company's business, depreciation and amortization expenses, are not fully identifiable with/ allocable to individual reportable segments, as certain assets are used interchangeably between segments. The other assets are not specifically allocable to the reportable segments. Consequently, management believes that it is not practicable to provide segment disclosures relating to total assets since allocation among the various reportable segments is not possible.

Formulations

Formulations, also referred to as finished dosages, consist of finished pharmaceutical products ready for consumption by the patient. An analysis of revenues by therapeutic category of the formulations segment is given below:

	YEAR ENDED MARCH 31,		
	2004	**2005**	**2006**
Gastro Intestinal	Rs.1,624,811	Rs.1,740,087	Rs.2,252,528
Pain Control	1,386,362	1,540,665	1,873,921
Cardiovascular	1,444,055	1,494,701	1,707,223
Anti-Infectives	1,013,595	1,001,797	1,118,631
Dermatology	313,076	338,016	427,165
Others	1,732,039	1,526,753	2,535,664
	Rs.7,513,938	Rs.7,642,019	Rs.9,915,132
Intersegment revenues[1]	19,519	17,702	40,426
Adjustments[2]	(25,979)	163,192	(29,603)
Total revenues	**Rs.7,507,478**	**Rs.7,822,913**	**Rs.9,925,955**
Cost of revenues	2,450,906	2,280,473	3,024,070
Intersegment cost of revenues[3]	211,182	259,727	242,080
Adjustments[2]	(84,424)	(47,397)	(182,012)
	Rs.2,577,664	**Rs.2,492,803**	**Rs.3,084,138**
Gross profit	4,871,369	5,119,521	6,689,408
Adjustments[2]	58,445	210,589	152,409
	Rs.4,929,814	**Rs.5,330,110**	**Rs.6,841,817**

(1) Intersegment revenues is comprised of transfers to the active pharmaceutical ingredients and intermediates segment and is accounted for at cost to the transferring segment.

(2) The adjustments represent reconciling items to conform the segment information to U.S. GAAP. Such adjustments primarily relate to elimination of sales made to subsidiaries and other adjustments.

(3) Intersegment cost of revenues is comprised of transfers from the active pharmaceutical ingredients and intermediates segment to formulations and is accounted for at cost to the transferring segment.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

Active pharmaceutical ingredients and intermediates

Active pharmaceutical ingredients and intermediates, also known as active pharmaceutical products or bulk drugs, are the principal ingredients for formulations. Active pharmaceutical ingredients and intermediates become formulations when the dosage is fixed in a form ready for human consumption such as a tablet, capsule or liquid using additional inactive ingredients.

An analysis of gross profit for the segment is given below.

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Revenues from external customers	Rs.6,973,891	Rs.5,946,765	Rs.7,448,681
Intersegment revenues[1]	602,060	742,294	1,064,816
Adjustments[2]	52,552	255,469	(275,440)
Total revenues	**Rs.7,628,503**	**Rs.6,944,528**	**Rs.8,238,057**
Cost of revenues	Rs.4,666,757	Rs.4,499,140	5,462,935
Intersegment cost of revenues	19,519	17,702	40,426
Adjustments[2]	416,082	496,713	413,239
	Rs.5,102,358	**Rs.5,013,555**	**Rs.5,916,600**
Gross profit	Rs.2,889,675	Rs.2,172,217	Rs.3,010,135
Adjustments[2]	(363,530)	(241,244)	(688,679)
	Rs.2,526,145	**Rs.1,930,973**	**Rs.2,321,456**

(1) Intersegment revenues is comprised of transfers to formulations, generics and custom pharamaceutical services and are accounted for at cost to the transferring segment.

(2) The adjustments represent reconciling items to conform the segment information to U.S. GAAP. Such adjustments primarily relate to elimination of sales made to subsidiaries and other adjustments.

An analysis of revenue by geography is given below:

	YEAR ENDED MARCH 31,		
	2004	2005	2006
North America	Rs.1,902,922	Rs.1,848,963	Rs.1,654,953
India	2,160,297	1,988,134	2,302,434
Europe	1,626,890	1,091,190	1,420,930
Others	1,983,551	2,032,258	2,865,743
	7,673,660	6,960,545	8,244,060
Adjustments[1]	(45,157)	(16,017)	(6,003)
	Rs.7,628,503	**Rs.6,944,528**	**Rs.8,238,057**

(1) The adjustments represent reconciling items to conform the segment information to U.S. GAAP. Such adjustments primarily relate to elimination of sales made to subsidiaries and other adjustments.

An analysis of revenues by key products is given below:

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Ciprofloxacin Hydrochloride	Rs.959,773	Rs.619,112	Rs.778,458
Ramipril	1,314,164	783,362	642,538
Terbinafine HCl	124,923	194,482	537,155
Ibuprofen	394,634	460,490	502,263
Sertraline Hydrochloride	178,537	138,158	494,101
Ranitidine HCl Form 1 & 2	711,445	734,265	552,845
Naproxen Sodium	437,339	470,044	380,409
Naproxen	233,835	229,553	374,997
Atorvastatin	211,192	252,466	321,139

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Montelukast	29,825	52,626	241,090
Losartan Potassium	214,231	180,528	172,682
Sparfloxacin	197,055	117,520	168,200
Nizatidine	159,592	216,757	160,857
Clopidogrel	140,310	79,586	139,941
Dextromethorphan HBr	182,775	165,836	134,884
Others	2,138,872	2,249,743	2,636,498
Total	**Rs.7,628,502**	**Rs.6,944,528**	**Rs.8,238,057**

Generics

Generics are generic finished dosages with therapeutic equivalence to branded formulations. The Company entered the global generics market during the year ended March 31, 2001 with the export of ranitidine 75mg and oxaprozin to the United States.

An analysis of gross profit for the segment is given below.

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Revenues	Rs.4,337,525	Rs.3,577,421	Rs.4,055,764
Less:			
Cost of revenues	989,125	1,222,401	1,464,479
Intersegment cost of revenues[1]	335,342	397,969	704,321
	1,324,467	1,620,370	2,168,800
Gross Profit	**Rs.3,013,058**	**Rs.1,957,051**	**Rs.1,886,964**

(1) Intersegment cost of revenues is comprised of transfers from the active pharmaceutical ingredients and intermediates segment to the generics segment and are accounted for at cost to the transferring segment.

An analysis of revenues by key products for the year ended March 31, 2004, 2005, and 2006 is given below:

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Omeprazole	Rs.325,304	Rs.434,090	Rs.786,341
Fluoxetine	1,825,546	857,927	381,265
Amlodipine	7,797	200,459	384,411
Ranitidine	205,799	194,003	235,621
Ibuprofen	183,973	198,666	251,430
Ciprofloxacin	28,057	196,010	158,158
Others	1,761,049	1,496,266	1,858,538
	Rs.4,337,525	**Rs.3,577,421**	**Rs.4,055,764**

Critical care and biotechnology

Diagnostic pharmaceuticals and equipment and specialist products are produced and marketed by the Company primarily for anti-cancer and critical care. An analysis of gross profit for the diagnostics, critical care and biotechnology segment is given below:

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Revenues	Rs.411,028	Rs.527,108	Rs.691,074
Cost of revenues	206,974	176,534	235,869
Gross profit	**Rs.204,054**	**Rs.350,574**	**Rs.455,205**

(1) Intersegment cost of revenues is comprised of transfers from the active pharmaceutical ingredients and intermediates segment to the critical care and biotechnology segment and are accounted for at cost to the transferring segment.

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

Customs pharmaceutical services ("CPS")

Customs pharmaceutical services caters to innovator companies across the globe with service offerings spanning the entire value chain of pharmaceutical services. The operations relate to the manufacture and sale of active pharmaceutical ingredients and steroids as per innovator's requirements. The Company's acquisition of Roche's manufacturing facility in Mexico, during the current year has been assigned to this segment.

An increase in the revenues of customs pharmaceutical services business coupled with the acquisition of Roche's manufacturing facility in Mexico, has resulted in disclosure of CPS as a separate segment. Segment data for the previous periods has been reclassified on a comparable basis. In earlier periods the result of CPS business was grouped under "Others" in segment information.

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Revenues	Rs.113,094	Rs.311,574	Rs.1,326,828
Less:			
Cost of revenues	2,213	–	829,302
Intersegment cost of revenues[1]	55,339	82,559	118,415
Adjustments	–	–	51,717
	57,552	82,559	999,434
Gross Profit	**Rs.55,542**	**Rs.229,015**	**Rs.327,394**

(1) Intersegment cost of revenues is comprised of transfers from the active pharmaceutical ingredients and intermediates segment to the custom pharmaceutical services and are accounted for at cost to the transferring segment

Drug discovery

The Company is involved in drug discovery through the research facilities located in the United States and India. The Company commercializes drugs discovered with other products and also licenses these discoveries to other companies. An analysis of the revenues and expenses of the drug discovery segment is given below:

	YEAR ENDED MARCH 31,		
	2004	2005	2006
Revenues	Rs.–	Rs.288,382	–
Adjustments[1]	–	–	–
	–	Rs.288,382	–
Research and development expenses	Rs.729,434	Rs.868,992	Rs.814,485

(1) The adjustments represent reconciling items to conform the segment information with U.S. GAAP. Such adjustments primarily relate to deferral of up-front non-refundable license fees.

a) Reconciliation of segment information to entity total

	YEAR ENDED MARCH 31					
	2004		2005		2006	
	Revenues	Gross profit	Revenues	Gross profit	Revenues	Gross profit
Formulations	Rs.7,507,478	Rs.4,929,814	Rs.7,822,913	Rs.5,330,110	Rs.9,925,955	Rs.6,841,817
Active pharmaceutical ingredients and intermediates	7,628,503	2,526,145	6,944,528	1,930,973	8,238,057	2,321,456
Generics	4,337,525	3,013,058	3,577,421	1,957,051	4,055,764	1,886,964
Critical care and biotechnology	411,028	204,054	527,108	350,574	691,074	455,205
Drug discovery	–		288,382	288,382	–	–
Custom pharmaceutical services	113,094	55,542	311,573	229,015	1,326,828	327,394
Others	105,894	37,654	47,441	47,441	29,369	16,798
	Rs.20,103,522	**Rs.10,766,267**	**Rs.19,519,366**	**Rs.10,133,546**	**Rs.24,267,047**	**Rs.11,849,634**

notes to the consolidated financial statements

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

b) Analysis of revenue by geography

The Company's business is organized into five key geographic segments. Revenues are attributable to individual geographic segments based on the location of the customer.

	YEAR ENDED MARCH 31,		
	2004	**2005**	**2006**
India	Rs.7,143,798	Rs.6,693,042	Rs.8,272,468
North America	5,319,160	4,349,191	3,983,860
Russia and other countries of the former Soviet Union	2,285,838	2,782,171	3,559,477
Europe	2,788,648	2,868,233	4,326,366
Others	2,566,078	2,826,729	4,124,876
	Rs.20,103,522	**Rs.19,519,366**	**Rs.24,267,047**

c) Analysis of property, plant and equipment by geography

Property, plant and equipment (net) attributed to individual geographic segments are given below:

	AS OF MARCH 31,	
	2005	**2006**
India	Rs.6,723,966	Rs.7,063,595
North America	157,549	1,511,068
Russia and other countries of the former Soviet Union	34,681	30,118
Europe	122,449	468,314
Others	19,663	13,236
	Rs.7,058,308	**Rs.9,086,331**

information on the financial of subsidiaries (PREPARED AS PER IGAAP)

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

Name of the Subsidiary	Capital	Reserves	Total Assets	Total Liabilities	investments	Turnover	Profit Before Tax	Provision for Tax	Profit after Tax	Proposed dividend
DRL Investments Limited	500	171,946	9,217	9,217	–	–	(20)	–	(20)	–
Reddy Pharmaceuticals Hongkong Limited	58,021	23,291	150,843	150,843	–	–	1,491	–	1,491	–
OOO JV Reddy Biomed Limited	4,509	686	37,081	37,081	–	7,758	(1,277)	2,413	(3,690)	–
Reddy Antilles N.V.	17,969	187,977	317,863	317,863	205,648	2,014	1,866	(25)	1,841	–
Dr. Reddy's Farmaceutica Do Brasil Ltda.	97,085	(157,901)	41,848	41,848	–	20,392	(65,284)	–	(65,284)	–
Dr. Reddy's Laboratories Inc.	175,118	(754,158)	1,800,367	1,800,367	139,101	146	67,952	2,227	70,179	–
Reddy US Therapeutics Inc.	954	(36,648)	90,020	90,020	–	282,099	13,915	–	13,915	–
Reddy Cheminor S.A.	1,958	(7,419)	1,349	1,349	–	316	(450)	(288)	(738)	–
Cheminor Investments Limited	1,346	(101)	1,273	1,273	–	–	(2)	–	(2)	–
Aurigene Discovery Technologies Ltd.	866,442	(467,844)	780,943	780,943	208,282	87,812	(121,023)	–	(121,023)	–
Kunshan Rotam Reddy Pharmaceutical Co. Ltd.	620,617	(360,244)	192,915	192,915	–	199,789	(49,243)	(9,810)	(59,053)	–
Reddy Netherlands BV	754	(8,797)	4,320	4,320	–	18	(2,091)	–	(2,091)	–
Aurigene Discovery Technologies Inc.	208,282	(223,525)	2,404	2,404	–	19,575	(4,082)	–	(4,082)	–
Dr. Reddy's Laboratories (EU) Ltd.	96	170,732	190,851	190,851	70	–	(72,802)	–	(72,802)	–
Dr. Reddy's Laboratories (UK) Ltd.	70	59,824	738,779	738,779	–	2,201,922	(106,041)	12,650	(93)	
Dr. Reddy's Laboratories (Proprietary) Ltd.	–	(32,354)	61,909	61,909	–	142,635	394	(176)	218	–
Reddy Pharmaceuticals Inc.	122,692	6,768	132,669	132,669	–	16,017	6,807	–	6,807	–
OOO Dr. Reddy's Laboratories Limited	71,843	54,706	508,937	508,937	–	1,151,297	45,891	(12,235)	33,656	–
Dr. Reddys Bio–Sciences Limited	361,596	(155,298)	230,405	230,405	14,703	286,542	132	(116)	16	–
Trigenesis Theraputics Inc.	9	(31,353)	226,948	226,948	–	–	(1,279)	–	(1,279)	–
Industrias Quimicas falcon de Mexico, SA de CV	541,865	(18,132)	2,819,783	2,819,783	–	508,889	(17,302)	(830)	(18,132)	–
Lacock Holdings Ltd.	460	–	5,858,116	5,858,116	5,806,125	–	(12,695)	–	(12,695)	–
beta Holding GmbH	8,128	(165,047)	17,058,329	17,058,329	17,049,120	–	(146)	–	(146)	–
beta Healthcare Verwaltungs GmbH	1,350	147	1,597	1,597	–	–	(7,829)	–	(7,829)	–
betapharm Arzneimittel GmbH	55,225	(52,841)	1,967,524	1,967,524	–	707,792	82,564	–	82,564	–
beta Healthcare Solutions GmbH	1,350	(2,495)	1,533	1,533	–	–	(607)	–	(607)	–
beta Institut GmbH	5,400	–	44,744	44,744	–	16,768	–	–	–	–
Reddy Holding GmbH	1,319	(447,045)	27,400,607	27,400,607	26,063,322	–	(439,437)	(7,608)	(447,045)	–

statement pursuant to Section 212 of the Companies Act, 1956

(ALL AMOUNTS IN INDIAN RUPEES THOUSANDS, EXCEPT SHARE DATA AND WHERE OTHERWISE STATED)

Name of the Subsidiary	The Financial Year of the subsidiary company ended on	Number of shares in the subsidiary company held by Dr. Reddy's Laboratories Limited at the above date				The net Aggregate of profits (losses) of the subsidiary company for it's financial year so far as they concern the members of Dr. Reddy's Laboratories Limited		The net Aggregate of profits (losses) of the subsidiary company for it's previous financial year so far as they concern the members of Dr. Reddy's Laboratories Limited		Changes in the interest of Dr. Reddy's Laboratories Limited, between the end of the last financial year and 31st March 2006	Material changes between the end of the last financial year and 31st March 2006
		Equity Shares	Preference Shares	Equity Holding %	Preference Holding %	a) Dealt with in the account of Dr. Reddy's Laboratories Limited for the year ended 31.03.2006	b) Not dealt with in the account of Dr. Reddy's Laboratories Limited for the year ended 31.03.2006	a) Dealt with in the account of Dr. Reddy's Laboratories Limited for the year ended 31.03.2005	b) Not dealt with in the account of Dr. Reddy's for the year ended 31.03.2005		
DRL Investments Limited	31.03.2006	50,000	–	100	–	Nil	(20)	Nil	(21)	–	–
Reddy Pharmaceuticals Hongkong Limited	31.03.2006	11,625,000	–	100	–	Nil	1,491	Nil	55,651	–	–
OOO JV Reddy Biomed Limited	31.03.2006	500,000	–	100	–	Nil	(3,690)	Nil	(14,903)	–	–
Reddy Antilles N.V.	31.03.2006	500,000	–	100	–	Nil	1,841	Nil	(447)	–	–
Dr. Reddy's Farmaceutica Do Brasil Ltda.	31.03.2006	6,059,231	–	100	–	Nil	(65,284)	Nil	(116,298)	–	–
Dr. Reddy's Laboratories Inc.	31.03.2006	410,000	–	100	–	Nil	70,179	Nil	(173,274)	–	–
Reddy US Therapeutics Inc.	31.03.2006	(1)	–	–	–	Nil	13,915	Nil	18,915	–	–
Reddy Cheminor S.A.	31.03.2006	2,500	–	100	–	Nil	(738)	Nil	(1,635)	–	–
Cheminor Investments Limited	31.03.2006	134,513	–	100	–	Nil	(2)	Nil	(2)	–	–
Aurigene Discovery Technologies Ltd.	31.03.2006	88,644,161	–	100	–	Nil	(121,023)	Nil	(418,322)	–	–
Kunshan Rotam Reddy Pharmaceutical Co. Ltd.	31.03.2006	(2)	–	51.2	–	Nil	(59,053)	Nil	(109,903)	–	–
Reddy Netherlands BV	31.03.2006	(1)	–	–	–	Nil	(2,091)	Nil	(315)	–	–
Aurigene Discovery Technologies Inc.	31.03.2006	(1)	–	–	–	Nil	(4,082)	Nil	747	–	–
Dr.Reddy's Laboratories (EU) Ltd.	31.03.2006	132,600	360000	100	100	Nil	(72,802)	Nil	(76,932)	–	–
Dr.Reddy's Laboratories (UK) Ltd.	31.03.2006	(1)	–	–	–	Nil	(93)	Nil	42,040	–	–
Dr. Reddy's Laboratories (Proprietary) Ltd.	31.03.2006	60	–	60	–	Nil	218	Nil	(24,161)	–	–
Reddy Pharmaceuticals Inc.	31.03.2006	(1)	–	–	–	Nil	6,807	Nil	(7)	–	–
OOO Dr. Reddy's Laboratories Limited	31.03.2006	3,319,000	–	–	–	Nil	33,656	Nil	36,566	Capital increased	–
Dr. Reddys Bio–Sciences Limited	31.03.2006	34,022,070	–	100	–	Nil	16	Nil	255	–	–
Trigenesis Therapeutics Inc.	31.03.2006	9	–	100	–	Nil	(1,279)	Nil	6	–	–
Industrias Quimicas falcon de Mexico, SA de CV	31.03.2006	5,000	–	100	–	Nil	(18,132)	Nil	NA	New subsidiary	–
Lacock Holdings Limited	31.03.2006	5,000	–	100	–	Nil	(12,695)	Nil	NA	New subsidiary	–
beta Holding GmbH	31.03.2006	(1)	–	–	–	Nil	(146)	Nil	NA	New subsidiary	–
beta Healthcare Verwaltungs GmbH	31.03.2006	(1)	–	–	–	Nil	(7,829)	Nil	NA	New subsidiary	–
betapharm Arzneimittel GmbH	31.03.2006	(1)	–	–	–	Nil	82,564	Nil	NA	New subsidiary	–
beta Healthcare Solutions GmbH	31.03.2006	(1)	–	–	–	Nil	(607)	Nil	NA	New subsidiary	–
beta Institut GmbH	31.03.2006	(1)	–	–	–	Nil	–	Nil	NA	New subsidiary	–
Reddy Holding GmbH	31.03.2006	(1)	–	–	–	Nil	(447,045)	Nil	NA	New subsidiary	–

(1) Step Down subisdiary

(2) No concept of number of shares

For DR. REDDY'S LABORATORIES LIMITED

DR. K. ANJI REDDY	G V PRASAD	K SATISH REDDY	V S VASUDEVAN	V VISWANATH
CHAIRMAN	VICE CHAIRMAN & CEO	MANAGING DIRECTOR & COO	CHIEF FINANCIAL OFFICER	COMPANY SECRETARY

Hyderabad

31 MAY 2006

notice

Notice is hereby given that the 22nd Annual General Meeting of the Company will be held on Friday, the 28th day of July, 2006 at 11.30 AM at the Grand Ball Room, Taj Krishna, Road No.1 Banjara Hills, Hyderabad - 500 034 to transact the following business:

ORDINARY BUSINESS:

1. To receive, consider and adopt the Profit & Loss Account for the year ended March 31, 2006; Balance Sheet as on that date along with the Reports of the Directors' and Auditors' thereon and the consolidated financials along with the Auditors' Report thereon.
2. To declare dividend for the financial year 2005-06.
3. To appoint a Director in place of Mr. P. N. Devarajan who retires by rotation, and being eligible, offers himself for re-appointment.
4 To resolve not to fill the vacancy, for the time being, caused by the retirement of Dr. V Mohan, who retires by rotation and does not seek re-appointment.
5. To appoint the Statutory Auditors and fix their remuneration. The retiring Auditors M/s BSR & Co. are eligible for re-appointment.

SPECIAL BUSINESS:

6. To consider and if thought fit, to pass the following resolution as an ordinary resolution:

Re-appointment of Dr. K Anji Reddy as Executive Chairman

"RESOLVED THAT subject to the provisions of Sections 198, 269, 309, 310 and other applicable provisions, if any, of the Companies Act, 1956 read with Schedule XIII there of, Dr. K Anji Reddy be and is hereby re-appointed as Executive Chairman of the Company for a period of five years with effect from July 13, 2006 on the following terms and conditions:

The remuneration payable by way of salary, perquisites and commission be as follows:

(A) SALARY: Rs.300,000 per month

(B) PERQUISITES:

Category A:

1. Housing: Rent free accommodation or house rent allowance of Rs.150,000 per month.
2. Medical reimbursement for self and family as per the rules of the Company, value not exceeding Rs.15,000 per annum.
3. Leave travel allowance, as per the rules of the Company; value not exceeding Rs.150,000 per annum.

Category B:

Contribution to Provident Fund, Superannuation Fund or Annuity Fund. This will not be included in the computation of the ceiling on perquisites to the extent these either singly or put together are not taxable under the Income Tax Act, 1961. Gratuity payable shall not exceed half-a-month's salary for each completed year of service as per applicable provisions of Payment of Gratuity Act, 1972.

Encashment of leave at the end of the tenure will not be included in the computation of the ceiling on perquisites.

Category C:

Car, telephone at residence and mobile phone for use on Company's business.

(C) COMMISSION:

In addition to the salary and perquisites, commission will also be payable up to 1% of the net profits of the Company calculated as per the provisions of Section 198 of the Companies Act, 1956, as may be decided by the Board of Directors of the Company."

7. To consider and if thought fit, to pass the following resolution as an ordinary resolution:

Re-appointment of Mr. G V Prasad as Vice Chairman and Chief Executive Officer

"RESOLVED THAT subject to the provisions of Sections 198, 269, 309, 310 and other applicable provisions, if any, of the Companies Act, 1956 read with Schedule XIII there of Mr. G. V. Prasad be and is hereby re-appointed as Vice Chairman and Chief Executive Officer of the Company for a period of five years with effect from January 30, 2006 on the following terms and conditions:

The remuneration payable by way of salary, perquisites and commission be as follows:

(A) SALARY: Rs.200,000 per month

(B) PERQUISITES:

Category A:

1. Housing: Rent free accommodation or house rent allowance of Rs.100,000 per month.
2. Medical reimbursement for self and family as per the rules of the Company, value not exceeding Rs.15,000 per annum.
3. Leave travel allowance, as per the rules of the Company; value not exceeding Rs.100,000 per annum.

Category B:

Contribution to Provident Fund, Superannuation Fund or Annuity Fund. This will not be included in the computation of the ceiling on perquisites to the extent these either singly or put together are not taxable under the Income Tax Act, 1961. Gratuity payable shall not exceed half-a-month's salary for each completed year of service as per applicable provisions of Payment of Gratuity Act, 1972.

Encashment of leave at the end of the tenure will not be included in the computation of the ceiling on perquisites.

Category C:

Car, telephone at residence and mobile phone for use on Company's business.

(C) COMMISSION:

In addition to the salary and perquisites, commission will also be payable up to 0.75% of the net profits of the Company calculated as per the provisions of Section 198 of the Companies Act, 1956, as may be decided by the Board of Directors of the Company."

8. To consider and if thought fit, to pass the following resolution as an ordinary resolution:

Revision in terms of appointment of Mr. Satish Reddy as Managing Director and Chief Operating Officer

"RESOLVED THAT subject to the provisions of Sections 198, 269, 309, 310 and other applicable provisions, if any, of the Companies Act, 1956 read with Schedule XIII there of, the terms of appointment of Mr. Satish Reddy as Managing Director and Chief Operating Officer of the Company be and is hereby amended with effect from February 1, 2006 as under:

The remuneration payable by way of salary, perquisites and commission be as follows:

(A) SALARY: Rs.200,000 per month

(B) PERQUISITES:

Category A:

1. Housing: Rent free accommodation or house rent allowance of Rs.100,000 per month.

2. Medical reimbursement for self and family as per the rules of the Company, value not exceeding Rs.15,000 per annum.
3. Leave travel allowance, as per the rules of the Company; value not exceeding Rs.100,000 per annum.

Category B:

Contribution to Provident Fund, Superannuation Fund or Annuity Fund. This will not be included in the computation of the ceiling on perquisites to the extent these either singly or put together are not taxable under the Income Tax Act, 1961. Gratuity payable shall not exceed half-a-month's salary for each completed year of service as per applicable provisions of Payment of Gratuity Act, 1972.

Encashment of leave at the end of the tenure will not be included in the computation of the ceiling on perquisites.

Category C:

Car, telephone at residence and mobile phone for use on Company's business.

(C) COMMISSION:

In addition to the salary and perquisites, commission will also be payable up to 0.75% of the net profits of the Company calculated as per the provisions of Section 198 of the Companies Act, 1956, as may be decided by the Board of Directors of the Company.

9. To consider and, if thought fit, to pass with or without modification, the following resolution as a special resolution.

Remuneration to Directors other than the Managing / Whole-time Director(s)

(a) "RESOLVED THAT pursuant to Section 309 and other applicable provisions of the Companies Act, 1956, the Directors of the Company other than the Managing / Whole-time Director(s) be collectively paid a commission up to 0.5% of the net profit as may be decided by the Board of Directors of the Company for each of the financial years starting from financial year 2006-07 and ending with financial year 2010-11."

(b) "RESOLVED THAT the Directors of the Company other than the Managing / Whole-time Director(s) be collectively granted up to 200,000 stock options in aggregate at any point of time during the financial years starting from financial year 2006-07 and ending with financial year 2010-11 and out of which up to 60,000 stock options be granted in a financial year to all the above Directors collectively under any of the stock option plans, either existing or to be framed in future, on such terms and conditions as the Compensation Committee / Board of Directors may in its absolute discretion think fit."

10. To consider and, if thought fit, to pass with or without modification, the following resolution as an ordinary resolution.

Increase in the Authorized Share Capital of the Company

"RESOLVED THAT pursuant to Section 16 and Section 94 of the Companies Act, 1956 and other applicable provisions of the Companies Act, 1956, the Authorized Share Capital of the Company be and is hereby increased from Rs.50,00,00,000 (Rupees Fifty Crores only) divided into 10,00,00,000 (Ten Crores only) equity shares of Rs.5 each (Rupees five only) to Rs.100,00,00,000 (Rupees Hundred Crores only) divided into 20,00,00,000 (Twenty Crores only) equity shares of Rs.5 each (Rupees five only), and consequently the existing Clause V.a. of the Memorandum of Association of the Company be and is hereby altered by substituting the existing Clause V.a. there of by the following Clause V.a.:

V.a. The authorized share capital of the Company is Rs.100,00,00,000/- (Rs. One Hundred Crores only) divided into 20,00,00,000 equity shares of Rs.5/- (Rupees Five only) each."

11. To consider and, if thought fit, to pass with or without modification, the following resolution as an ordinary resolution.

Capitalization of the reserves of the Company

"RESOLVED THAT in accordance with the relevant provisions of the Memorandum and Articles of Association of the Company and recommendation of the Board of Directors, and subject to the guidelines issued by the Securities and Exchange Board of India and such approvals as may be required in this regard, consent of the members be and is hereby accorded to the Board of Directors of the Company (herein after referred to as the Board, which expression shall include a Committee of Directors duly authorized in this behalf), for capitalization of such sum standing to the credit of the general reserves / share premium account of the Company, as may be considered necessary by the Board, for the purpose of issue of bonus shares of Rs.5 each, credited as fully paid up shares to the holders of the existing equity shares of the Company, whose names appear in the Register of Members, on such date as may be fixed in this regard by the Board of Directors, in the proportion of one equity share for every one existing equity share held by them."

"RESOLVED FURTHER THAT consequent to the issue of bonus shares, herein before resolved, in accordance with the relevant provisions of the Memorandum and Articles of Association of the Company and subject to any registration statement to be filed with the Securities and Exchange Commission, USA, and any other requirement under any law, consent of the shareholders be and is hereby accorded to the Board of Directors of the Company for the purpose of issue of stock dividend (Bonus), credited as fully paid up American Depository Shares to the holders of the American Depository Shares of the Company whose names appear on such date as may be fixed in this regard by the Board of Directors, in the proportion of one American Depository Share for every one existing American Depository Share held by them."

"RESOLVED FURTHER THAT no allotment letters shall be issued to the allottees of the bonus shares and that the certificate(s) in respect of bonus shares shall be dispatched to the allottees there of within the period prescribed or that may be prescribed in this behalf, from time to time, except in respect of those allottees who hold shares in dematerialized form."

"RESOLVED FURTHER THAT the issue and allotment of the said bonus shares to the extent they relate to Non-Resident Indians (NRIs), Persons of Indian Origin (PIO) and other foreign investors of the Company will be subject to the approval of the Reserve Bank of India (RBI), as may be necessary."

"RESOLVED FURTHER THAT for the purposes of giving effect to the bonus issue of Equity Shares and American Depository Shares resolved hereinbefore, the issuance of Equity Shares and / or American Depository Shares or Instruments or Securities representing the same, the Board of Directors of the Company be and are hereby authorized on behalf of the Company to do all such acts, deeds, matters and things as it may at its discretion deem necessary or desirable for such purpose, including without limitation, filing a registration statement, if any, and other documents with the Securities and Exchange Commission, USA and / or the Securities and Exchange Board of India, listing the additional Equity Shares and / or American Depository Shares on the Bombay Stock Exchange Limited, National Stock Exchange of India Limited and the New York Stock Exchange Inc. as it may in its absolute discretion deem fit."

"RESOLVED FURTHER THAT the Board be and is hereby authorized to take all the other steps as may be necessary to give effect to the aforesaid resolution and determine all other terms and conditions of the issue of bonus shares as the Board may in its absolute discretion deem fit."

12. To consider and, if thought fit, to pass with or without modification, the following resolution as a special resolution.

Further issue of shares

"RESOLVED THAT pursuant to Section 81(1A) and all other applicable provisions of the Companies Act, 1956 (including any statutory modification or re-enactment there of, for the time being in force) and enabling provisions of the Memorandum and Articles of Association of the Company and the Listing Agreements entered into by the Company with the Stock Exchanges where the securities of the Company are listed and subject to any guidelines, regulations, approval, consent, permission or sanction of the Central Government, Reserve Bank of India, Securities and Exchange Board of India and any other appropriate authorities, institutions or Bodies (hereinafter collectively referred to as "the appropriate authorities"), and subject to such conditions as may be prescribed by any one of them while granting any such approval, consent, permission, and / or sanction (hereinafter referred to as "the requisite approvals"), which may be agreed to by the Board of Directors of the Company (hereinafter called "the Board" which term shall be deemed to include any Committee which the Board may have constituted or hereinafter constitute to exercise its powers including the powers conferred by this resolution), the Board be and is hereby authorised to issue, offer and allot, any securities in Indian or international markets including equity shares, Global Depository Receipts and / or American Depository Receipts convertible into equity shares, preference shares whether Cumulative or Non-Cumulative / Redeemable / Convertible at the option of the Company and / or at the option of the holders of the security and / or securities linked to equity shares / preference shares and / or any instrument or securities representing convertible securities such as convertible debentures, bonds or warrants convertible into equity shares / preference shares (hereinafter referred to as "Securities") to be subscribed by foreign investors / institutions and / or corporate bodies, mutual funds, banks, insurance companies, trusts and / or individuals or otherwise, whether or not such persons / entities / investors are Members of the Company, whether in Indian currency or foreign currency and such issue and allotment shall be made at such time or times in one or more tranche or tranches, at par or at such price or prices, and on such terms and conditions including with the differential rights as to dividend, voting or otherwise and in such manner as the Board may, in its absolute discretion think fit, in consultation with the Lead Managers, Underwriters, Advisors or other intermediaries; provided however that the issue of Securities as above shall not result in increase of the issued and subscribed equity share capital of the Company by more than 23,000,000 equity shares (Post Bonus issue) of the face value of Rs.5 each."

"RESOLVED FURTHER THAT without prejudice to the generality of the above, the aforesaid issue of Securities may have all or any terms or combination of terms including as to conditions in relation to payment of interest, additional interest, premia on redemption, prepayment and any other debt service payments whatsoever, and all such matters as are provided in Securities offerings of this nature including terms for issue of such Securities or variation of the conversion price of the Security during the tenure of the Securities and the Company is also entitled to enter into and execute all such arrangements as the case may be with any lead managers, underwriters, bankers, financial institutions, solicitors, advisors, guarantors, depositories, custodians and other intermediaries in such offerings of Securities and to remunerate all such agencies including the payment of commissions, brokerage, fees or payment of their remuneration for their services or the like, and also to seek the listing of such Securities on one or more Stock Exchanges including international Stock Exchanges, wherever permissible."

"RESOLVED FURTHER THAT the Company may enter into any arrangement with any agency or body authorised by the Company for the issue of Securities in registered or bearer form with such features and attributes as are prevalent in capital markets for instruments of this nature and to provide for the tradability or free transferability there of as per the international practice and regulations, and under the forms and practices prevalent in securities markets."

"RESOLVED FURTHER THAT the Securities issued in foreign markets shall be deemed to have been made abroad and / or in the market and / or at the place of issue of the Securities in the international market and may be governed by applicable laws."

"RESOLVED FURTHER THAT such of these Securities to be issued as are not subscribed may be disposed off by the Board to such persons and in such manner and on such terms as the Board in its absolute discretion thinks fit in the best interest of the Company and as is permissible at law."

"RESOLVED FURTHER THAT for the purpose of giving effect to any issue or allotment of Securities or instruments representing the same, as described in paragraph (a) above, the Board or any Committee there of be and is hereby authorized on behalf of the Company to do all such acts, deeds, matters and things as it may at its discretion deem necessary or desirable for such purpose, including without limitation, entering into of underwriting, marketing and depository arrangement and institution / trustees / agents and similar agreements and to remunerate the Managers, underwriters and all other agencies / intermediaries by way of commission, brokerage, fees and the like as may be involved or connected in such offerings of securities, with power on behalf of the Company to settle any questions, difficulties or doubts that may arise in regard to any such issue or allotment as it may in its absolute discretion deem fit."

NOTES:

1. An explanatory statement pursuant to Section 173 (2) of the Companies Act, 1956 in respect of the special business is annexed hereto.
2. **A member entitled to attend and vote is entitled to appoint a proxy to attend and vote instead of himself/herself and the proxy need not be a member of the Company. The instrument of proxy in order to be effective, must be deposited at the registered office of the Company, duly completed and signed not less than 48 hours before the meeting.**
3. The register of members and the share transfer books of the Company will remain closed from July 11, 2006 to July 14, 2006 (both days inclusive) in connection with the payment of dividend for the financial year 2005-06.
4. The Register of Members and Share Transfer Books shall be closed from Tuesday, July 11, 2006 to Friday, July 14, 2006 (both days inclusive) for determining the names of Members eligible for dividend on Equity Shares, if declared at the Meeting. The Dividend on Equity Shares, if declared at the Meeting will be paid to those Members whose names appeared on the Company's Register of Members on Monday, July 10, 2006. In respect of shares held in dematerialized form, the dividend will be paid on the basis of particulars of beneficial ownership furnished by depositories as at the end of business on Monday, July 10, 2006
5. The Shareholders are requested to intimate immediately any change in their address or bank mandates to their depository participants with whom they are maintaining their demat accounts or to the Company's Share Transfer Agent, M/s Bigshare Services Private Limited, if the shares are held in certificate form.
6. For the convenience of members and for proper conduct of the meeting, entry to the place of meeting will be regulated by attendance slip, which is part of the annual report. Members are requested to sign at the place provided on the attendance slip and hand it over at the entrance to the venue.
7. Shareholders desiring any information relating to the accounts are requested to write to the Company at an early date so as to enable the management to keep the information ready.

By order of the Board

Place: Hyderabad
Date: May 31, 2006

V VISWANATH
COMPANY SECRETARY

annexure to notice

Explanatory statement pursuant to Section 173 (2) of the Companies Act, 1956

ITEM NO. 6

Dr. K. Anji Reddy is the Founder Chairman of Dr. Reddy's Laboratories Limited. Prior to founding Dr. Reddy's in 1984, he was the Founder Managing Director of Uniloids Limited. and Standard Organics Limited and also served in the state-owned Indian Drugs and Pharmaceuticals Limited.

Under Dr. K. Anji Reddy's leadership, Dr. Reddy's has become a pioneer in the Indian Pharmaceutical industry. It has transformed the Indian bulk drug industry from import-dependent in mid-80s to self-reliant in mid-90s and finally into the export-oriented industry that it is today. Under his guidance, Dr. Reddy's became the first Indian Company to embark upon drug discovery research in India in 1993 and the first non-Japanese Asia Pacific pharmaceutical Company to list on NYSE in April 2001.

Dr. K. Anji Reddy has a Bachelor of Science degree in Pharmaceuticals and Fine Chemicals from Bombay University and a Ph.D. in Chemical Engineering from National Chemical Laboratory, Pune.

Dr. K. Anji Reddy holding 400,478 equity shares in the Company is also a Director in the following Companies in terms of Section 275 of the Companies Act, 1956:

1) DRL Investments Limited.
2) Cheminor Investments Limited.
3) Diana Hotels Limited.

Dr. K. Anji Reddy was re-appointed as Executive Chairman (Whole Time Director) of the Company at the 17th Annual General Meeting of the Company held on September 24, 2001, for a period of 5 years ending July 13, 2006. It is now proposed to re-appoint Dr. K. Anji Reddy as Executive Chairman (Whole Time Director) of the Company for a further period of 5 years commencing July 13, 2006 on the terms and conditions as specified in the resolution no.6.

Your Directors recommend the resolution for your approval.

None of the Directors other than Dr. K. Anji Reddy, Mr. Satish Reddy and Mr. G V Prasad are deemed to be concerned or interested in the above resolution.

ITEM NO. 7

Mr. G V Prasad joined the Company in 1986 and leads the core team that is driving the Company's growth and transformation from a Company predominantly selling APIs, Branded Formulations & Generics to achieving its vision of becoming a discovery-led global pharmaceutical Company. As CEO, Mr. Prasad has championed the globalization of the Company and has played a crucial role in the Company's evolution. He has been the architect of the Company's global generics strategy. He has helped create new platforms of growth for Dr. Reddy's, in the Customs Pharmaceutical Services, Discovery Services and Specialty Pharmaceutical segments.

Mr. Prasad has a Bachelors degree in Chemical Engineering from Illinois Institute of Technology, Chicago, and a Masters degree in Industrial Administration from Purdue University, USA.

Mr. G V Prasad holding 675,720 equity shares in the Company is also a Director in the following Companies in terms of Section 275 of the Companies Act, 1956:

1) DRL Investments Limited.
2) Cheminor Investments Limited.
3) Aurigene Discovery Technologies Limited.
4) Nipuna Services Limited.
5) Diana Hotels Limited.
6) Dr. Reddy's Bio Sciences Limited.
7) Ocimum Bio-solutions Limited.
8) Infotech Enterprises Limited.

Mr. G V Prasad was re-appointed as Vice Chairman and Chief Executive Officer (Whole Time Director) of the Company at the 17th Annual General Meeting of the Company held on September 24, 2001, for a period of 5 years ending January 30, 2006. It is now proposed to re-appoint Mr. G V Prasad as Vice Chairman and Chief Executive Officer (Whole Time Director) of the Company for a further period of 5 years commencing on January 30, 2006 on the terms and conditions as specified in the resolution no. 7.

Your Directors recommend the resolution for your approval.

None of the Directors other than Dr. K Anji Reddy, Mr. Satish Reddy and Mr. G V Prasad are deemed to be concerned or interested in the above resolution.

ITEM NO. 8

Mr. Satish Reddy joined the Company as Executive Director in 1993, responsible for manufacturing operations of active pharmaceutical ingredients (APIs), formulations, research and development activities and new product development. He presided over the Company's successful transition from a predominantly API manufacturer to a more value-added, finished dosages producer.

He was the major force behind the successful acquisition of American Remedies Limited. (1999), a Chennai-based pharmaceutical company. Besides, he was instrumental in setting up our wholly owned subsidiaries in Russia and Latin America and joint ventures in China and South Africa.

Mr. Satish Reddy was re-appointed as Managing Director and Chief Operating Officer of the Company at the 18th Annual General Meeting of the Company held on August 26, 2002, for a period of 5 years ending October 1, 2007. It is now proposed to revise the terms and conditions of appointment of Mr. Satish Reddy as specified in the resolution no.8.

Your Directors recommend the resolution for your approval.

None of the Directors other than Dr. K Anji Reddy, Mr. Satish Reddy and Mr. G V Prasad are deemed to be concerned or interested in the above resolution.

ITEM NO. 9(a) AND 9(b)

With the constitution of various committees and the increasing demand over the time of the independent and professional Directors on various issues relating to the Company, it would be advisable to put in place an appropriate mechanism to compensate, attract and retain professionals on the Board. Thus it is proposed to remunerate the non-executive Directors based on the performance of the Company on yearly basis by way of commission on the net profits and grant of stock options. The remuneration proposed for the independent Directors is set out in the resolution.

The Company has Employee Stock Option Scheme, which covers employees, and Directors of the Company and its subsidiaries.

As per the revised Clause 49 of the listing agreement, which has come into effect from January 1, 2006, it is now mandatory for the Companies to seek approval of the shareholders to specify the limit on the number of stock options that can be granted to non-executive Directors, including independent Directors, in any financial year and in aggregate. The present Resolution 9(b) specifies the limits for the maximum number of stock options that can be granted to independent Directors of the Company, in any financial year and in aggregate.

Your Directors recommend the resolution for your approval.

None of the Directors other than Mr. Anupam Puri, Prof. Krishna G. Palepu, Dr. Omkar Goswami, Mr. P N Devarajan, Mr. Ravi Bhoothalingam and Dr. V Mohan as independent Directors of the Company are deemed to be interested in this resolution except as members.

ITEM NO. 10

The present Authorized Share Capital of the Company is Rs.50 Crores. In view of the proposal for issue of Bonus Shares, and further issue of shares as contemplated in item Nos. 11 and 12 it is proposed to increase the Authorized Share Capital of the Company from Rs.50,00,00,000 (Rupees Fifty Crores only) divided into 10,00,00,000 equity shares of Rs.5 each to Rs.100,00,00,000 (Rs. Hundred Crores only) divided into 20,00,00,000 equity shares of Rs.5 each.

Increase in Authorized Share Capital would necessitate amendment to the Clause V.a. of the Memorandum of Association by passing an ordinary Resolution.

Your Directors recommend the resolution for your approval.

None of the Directors of the Company is, in any way, concerned or interested in the said resolution.

ITEM NO. 11

The Board of Directors at their meeting held on May 31, 2006, recommended issue of bonus shares in proportion of one share for every one equity share held by the members on a date to be fixed by the Board, by capitalizing a part of the amount standing to the credit of the general reserve account / share premium account. Consequently, the Board has also recommended stock dividend of one American Depository Share for every one existing American Depository Share held by the holders of the American Depository Shares as on a date to be fixed by the Board.

Pursuant to the provisions of the Articles of Association of the Company and in terms of Guidelines of Securities Exchange Board of India (SEBI) the capitalization of reserves and bonus issue thereof require approval of the members in general meeting. Further, it is necessary to authorize the Board of Directors of the Company to complete all the regulatory formalities prescribed by the Securities and Exchange Commission, USA, Securities and Exchange Board of India, the stock exchanges on which the Company's securities are listed and any other regulatory authority including without limitation, the filing of any registration statement and / or other filings, with the Securities and Exchange Commission, USA, in connection with the bonus issue.

Accordingly, the resolution seeks the approval of the members for capitalization of amount standing to the credit of general reserves / share premium account and issue of bonus shares on the terms and conditions set out in the resolution.

Your Directors recommend the resolution for your approval.

None of the Directors of the Company is concerned or interested in the said resolution, except as member.

ITEM NO. 12

The Company needs to augment long-term resources to strengthen its financial position, to meet its growth objectives. It is accordingly proposed to issue securities in the national/international markets as contemplated in the resolution set out above, as may be decided by the Board and found to be expedient and in the interests of the Company. The detailed terms and conditions of the Issue as and when made will be determined by the Board of Directors in consultation with the Merchant Bankers, Lead Managers, Advisors, Underwriters and other experts in accordance with the terms of approval of the Government of India, Reserve Bank of India, Securities and Exchange Board of India, Financial Institutions who have lent or agreed to lend monies to the Company and such other authorities as may be required. The proposed issue of Securities as above may be made in one or more tranches, which may result in an increase of the issued and subscribed equity and/or Preference share capital of the Company by not more than 23,000,000 equity shares of the face value of Rs.5 each of the Company. The issue price of the securities to be issued in the proposed offerings will be determined by the Board of Directors at the time of the offer depending on the then prevailing market conditions. The Securities will be listed on such international / Indian Stock Exchanges as the Board may be advised.

Section 81 of the Companies Act, 1956, provides, inter-alia, that where it is proposed to increase the Subscribed Share Capital of the Company by allotment of further shares, such further shares shall be offered to the persons who at the date of the offer are holders of the Equity Shares of the Company, in proportion to the capital paid up on those shares as of that date unless the Shareholders decide otherwise. The Listing Agreements executed by the Company with the various Stock Exchanges also provide that the Company shall issue or offer in the first instance all Securities to the existing Equity Shareholders of the Company unless the Shareholders decide otherwise.

The Special Resolution seeks the consent of the Shareholders authorizing the Board of Directors to make the proposed issue of Securities and in the event it is decided to issue Securities convertible into Equity and/or Preference Shares, to issue to the holders of such Convertible Securities in such manner and such number of Equity and / or Preference Shares on conversion as may be required to be issued in accordance with the terms of the issue.

This Special Resolution gives (a) adequate flexibility and discretion to the Board to finalise the terms of the issue, in consultation with the Lead Managers, Underwriters, Legal Advisors and experts or such other authority or authorities as need to be consulted including in relation to the pricing of the issue which will be a free market pricing and may be at premium or discount to the market price in accordance with the normal practice and (b) powers to issue and market any securities issued pursuant to the international offer including the power to issue such Securities in such tranche or tranches with / without voting rights or with differential voting rights. The Board of Directors recommends the resolution set out in the accompanying notice for the approval of the Members.

Your Directors recommend the resolution for your approval.

None of the Directors of the Company is, concerned or interested in the said resolution, except as members.

By order of the Board

Place: Hyderabad
Date: May 31, 2006

V VISWANATH
COMPANY SECRETARY

Glossary

ADR	American Depository Receipts
ADS	American Depository Shares
ANDA	Abbreviated New Drug Application
API	Active Pharmaceutical Ingredients
ARL	American Remedies Limited
BSE	Bombay Stock Exchange Limited
CPS	Customs Pharmaceutical Services
CDL	Cheminor Drugs Limited
CDSL	Central Depository Services (India) Limited
CEO	Chief Executive Officer
CFO	Chief Financial Officer
cGMP	Current Good Manufacturing Practices
CIA	Chief Internal Auditor
COO	Chief Operating Officer
DMF	Drug Master File
DP	Depository Participant
DPCO	Drugs (Prices Control) Order, 1995
DRF	Dr. Reddy's Research Foundation
DRL	Dr. Reddy's Laboratories Limited
EPS	Earning Per Share
ESOP	Employees Stock Option Plan
ESOS	Employees Stock Option Scheme
GDR	Global Depository Receipts
HR	Human Resources
ICAI	Institute of Chartered Accountants of India
Indian GAAP	Indian Generally Accepted Accounting Principles
IPM	Intellectual Property Management
IPR	Intellectual Property Rights
IREDA	Indian Renewable Energy Development Agency
M&A	Mergers and Acquisition
NCE	New Chemical Entity
NSDL	National Securities Depository Limited
NSE	National Stock Exchange of India Limited
NYSE	New York Stock Exchange, Inc.
R&D	Research and Development
ROW	Rest of the world
RUSTI	Reddy US Therapeutics, Inc.
SBU	Strategic Business Unit
SEBI	Securities and Exchange Board of India
SEC	Securities and Exchange Commission
SEFL	Standard Equity Fund Limited
TDC	Technology Development Centre
US GAAP	United States Generally Accepted Accounting Principles
USFDA	United States Food and Drug Administration
VAT	Value Added Tax
WTO	World Trade Organisation

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DR.REDDY'S

Dr. Reddy's Laboratories Limited
Regd. Office: 7-1-27, Ameerpet, Hyderabad – 500 016

Attendance Slip

Regd. Folio No./ Client ID :

Name & Address
of First/Sole Shareholder :

No. of Shares held :

I hereby record my presence at the 22nd Annual General Meeting of the Company on Friday, the July 28, 2006 at 11.30 AM at Grand Ball Room, Hotel Taj Krishna, Banjara Hills, Hyderabad – 500 034.

Signature of Member / Proxy

Note: Member / Proxy wish to attend the meeting must bring this Attendance Slip to the meeting and handover at the entrance duly signed.

— — — Please tear here — — —

DR.REDDY'S

Dr. Reddy's Laboratories Limited
Regd. Office: 7-1-27, Ameerpet, Hyderabad – 500 016

Proxy Form

Regd. Folio No./Client ID :

No. of Shares Held :

I/We ____

of ______________________________________ being a member/members of

the above named Company, hereby appoint ______________________________

of ____ or

failing him/her ____________________ of ____________________

as my/our Proxy to attend and vote for me/us on my/our behalf at the 22nd Annual General Meeting of the Company on Friday, the July 28, 2006 at 11.30 AM at Grand Ball Room, Hotel Taj Krishna, Banjara Hills, Hyderabad – 500 034, and at any adjournment thereof.

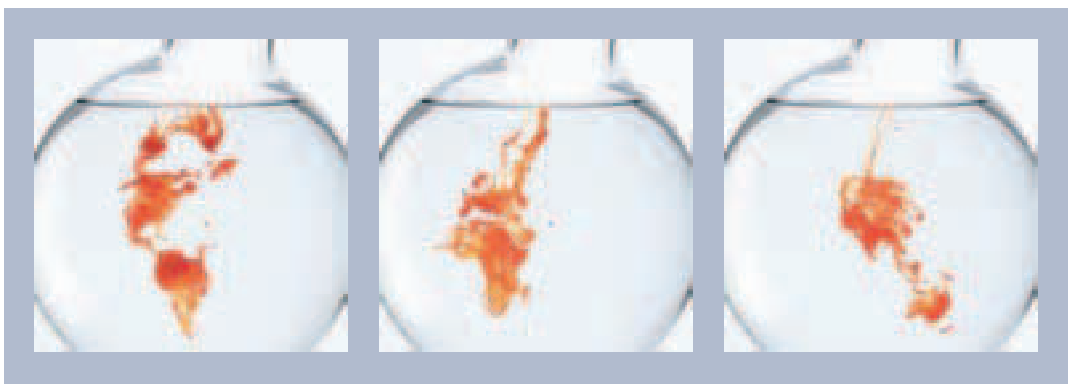
Revenue Stamp

Signed this __________ day of ___________ 2006.

Notes:

a) Proxy need not be a member.

b) The Proxy form duly signed by the member(s) across Revenue Stamp should reach the Company's Registered Office: Dr. Reddy's Laboratories Ltd., 7-1-27, Ameerpet, Hyderabad – 500 016, at least 48 hours before the time fixed for the meeting.



Dr. Reddy's Laboratories Limited | 7-1-27, Ameerpet, Hyderabad 500 016, India

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