Dr. Reddy's

ANNUAL REPORT
2016-17

Accelerating Access to Good Health

In This Report

Our Promises

Our five promises clarify what we do, what we offer and the commitments we make to our stakeholders. Our patients trust our medicines. We focus our energies on renewing this trust every day. As we keep the interests of our patients at the centre of all that we do, our promises drive us to reach higher levels of excellence.

Bringing expensive medicine within reach

Addressing unmet patient needs

Helping patients manage disease better

Working with partners to help them succeed

Enabling and helping our partners ensure that our medicines are available where needed

Chairman's & Co-Chairman's Letter

Dear Shareholder,

It is useful to start with a summary of your company's performance in FY2017.

- Consolidated revenues were at ₹ 140.8 billion, which was less by almost 9% compared to the previous year.
- Gross profit margin was at 55.6% of consolidated revenues, or four percentage points lower than what it was in FY2016.
- EBITDA was at ₹ 25.5 billion versus ₹ 36.3 billion in FY2016, and accounted for 18.1% of consolidated revenues.
- Profit before tax (PBT) was at ₹ 14.7 billion compared to ₹ 27.1 billion in the previous year.
- Profit after tax (PAT) was at ₹ 12 billion or 8.5% of revenues. It was 40% less than FY2016.

What were the reasons of this unfortunate performance? Broadly speaking, your company went through what is called a 'perfect storm' when several negative factors simultaneously came into play. Let us briefly discuss each of these.

The first was related to the US Food and Drug Administration's (USFDA's) inspections. In November 2014 and March 2015, the regulator inspected three of our plants: two chemical units that manufacture active pharmaceutical ingredients (APIs) at Srikakulam and Miryalaguda, and our formulations plant at Duvadda, near Visakhapatnam, which is an oncological sterile injectable facility with the capacity to manufacture certain complex generics. Based on their inspection, the USFDA sent a warning letter to your company in November 2015. We responded with a comprehensive plan of corrective and remedial actions along with timelines.

Based on our corrective actions, the USFDA re-inspected these three plants between February 2017 and April 2017. We have received some observations from the regulator thereafter, and have subsequently submitted a detailed response. At present, we await the USFDA's views on our latest set of responses.

There is no doubt that the remedial actions triggered by the USFDA's observations is unmistakably beneficial to Dr. Reddy's in the long run and that it has helped us to accelerate the pace of quality reforms across our plants. We have, since November 2015, significantly invested in processes, automation, detailed documentation of each batch and standard operating procedures, and have further strengthened our quality management systems. We also believe that the shift in the US regulator's approach from 'what has gone wrong' to 'what can go wrong' is for the long term good of the industry. Equally, however, the warning letter put on hold the approval of several key drugs, including high value added injectables and complex generics, to the US from the last quarter of FY2016 and throughout FY2017. This pipeline blockage affected revenues, margins and profits. Additional costs of conducting remedial work, including the use of international consultants, also reduced profits.

The second factor was the intensive growth of competition in US from several other global generics players. This was on account of two reasons: new competitors launching some of our niche and high salience drugs and dramatically pushing prices down; and the significant consolidation of our key US trade channels which gave the buyers greater pricing power than before. Moreover, a high value multi-year supply contract from our US manufacturing facility, expired during the year.

Third, there were significant delays in USFDA approvals and the consequent launch of new products in the US. These have nothing to do with the warning letters regarding our three facilities. Instead, these are on account on several additional queries raised by the USFDA – not just to us but all global pharmaceutical companies. Added to these deferrals were intellectual property litigations on some of our complex generics products.

Fourth, as an industry, we are facing government inspired pricing pressures in emerging and even the developed markets. Regulators have become ever more vigilant of price increases taken by pharmaceutical companies. In India, for FY2017, your company's revenue growth was constrained by the notified decline of prices of a large number of drugs, including your company's leading brands, in the National

We have significantly invested in processes, automation, operating procedures, to strengthen our quality management systems.

We believe that there are enormous opportunities across emerging markets, and are playing actively to increase our presence through generics and biosimilars.

We have widened our European footprint from the UK and Germany to France, Italy and Spain, we expect more significant growth from the continent in the years to come.

List of Essential Medicines (NLEM) issued by the National Pharmaceutical Pricing Authority (NPPA). Elsewhere, global firms have been subpoenaed by lawmakers over price rises. In the US, the EU, China and Japan, governments are either considering or actively implementing policies that constrain price increases. This will only increase over time as more aged people need direct and indirect healthcare support from their governments.

The fifth has to do with what was once an excellently profitable emerging market, Venezuela.

Till two years ago, your company enjoyed a sound business in providing affordable medicine to that country. However, an increasingly severe economic crisis in Venezuela has led to the government imposing severe constraints on foreign exchange outflows. Those familiar with last year's annual report will know that we took a major write-down of the net monetary assets of our Venezuelan business in FY2016. Thereafter, we have consciously chosen to limit our business to supplying consignments only against remittance of funds from Venezuela. Since such repatriations are minuscule, so too is the size of our business.

Finally, our active pharmaceutical ingredients business was also impacted due to lower off-take of some key molecules.

These six factors came together; worked contemporaneously throughout FY2017; and severely affected both revenue and profits.

What are the bright spots? And where do we go from here?

We believe that the pricing pressures in the US market will be less severe and more calibrated in FY2018. We also have an excellent pipeline of complex generics to be introduced to the country in FY2018, and expect to do better through this effective upgrade of our portfolio mix.

We also believe that there are enormous opportunities across emerging markets, and are playing actively to increase our presence in these territories through complex generics and biosimilars.

The Russian and CIS markets are on a moderate upswing. Though threats of government-induced pricing pressure remain, we are seeing greater offtake of generics – both relatively simple and complex – and oncological biosimilars, the latter through greater hospital and institutional sales. We believe that emerging markets will again get back to double-digit growth.

Despite government induced pricing pressures on pharmaceutical products, India remains a high growth market. In FY2017, revenues grew by 9% over the previous year. The first quarter of FY2018 may witness a temporary decline in the sales due to de-stocking by trade on the implementation of Goods and Services Tax (GST). Post normalisation, we expect to grow at low double-digits in FY2018 and for the foreseeable future.

Having striven to widen our European footprint from the UK and Germany to France, Italy and Spain, we expect more significant growth from the continent in the years to come.

We are particularly proud of our relatively nascent proprietary products business. The focus in FY2017 was on the commercialization of our newly launched products: Zembrace™ SymTouch™ (a 3 mg sumatriptan injection for acute migraine) and Sernivo™ (a betamethasone dipropionate 0.05% spray to treat mild-to-moderate plaque psoriasis). We shall attempt to significantly drive the growth of these products while introducing new products from our healthy pipeline.

Perhaps the most significant aspect of the top-line crunch in FY2017 is that it forced us to carefully look at all elements of costs and administrative layers – items that inexorably build up in good times and are generally only confronted in periods of stress. We have started multiple, company-wide projects to lop off costs without affecting productivity and, in doing so, recreate a leaner and more nimble global enterprise.

No chairman of a company listed in India and the US should ever make forward-looking statements. Even so, we are tempted to believe that your company's performance in FY2018 will be better than what we saw in FY2017. Let us indeed hope that it will. We have a good of complex generics offerings and proprietary product. Our biosimilar products are gaining traction. So too are our over-the-counter portfolios in Russia and the CIS, the US and India. And the API business should to do better next year. Most importantly, the management is united in putting aside the results of FY2017 and in striving for higher growth and better profitability in FY2018.

We are, therefore, cautiously optimistic of your company's performance in FY2018.

Thank you for your support.

With best regards,

K Satish Reddy
Chairman

G V Prasad
Co-Chairman & CEO

Our Businesses

GLOBAL GENERICS

- Revenue from the GG segment declined by 10% to ₹ 115.4 billion.
- Revenue from North America declined by 16% to ₹ 63.6 billion.
- Revenue from Emerging Markets declined by 11% to ₹ 21.1 billion.
- Revenue from India grew by 9% to ₹ 23.1 billion.

GLOBAL GENERICS

Global Generics is our biggest business driver. We offer more than 200 high-quality generic drugs, keeping costs reasonable by leveraging our integrated operations. Our expertise in active ingredients, product development skills, a keen understanding of regulations and intellectual property rights, as well as our streamlined supply chain, makes us leaders in this segment.

BIOLOGICS

Our biosimilars portfolio comprises affordable yet high quality versions of originator products. Our product development capabilities and commercial reach have made us one of the global leaders in this rapidly growing area. We have four products commercialized in various markets and an industry-leading development pipeline focussing on oncology and auto-immune diseases.

PHARMACEUTICAL SERVICES & ACTIVE INGREDIENTS

- Revenue from the PSAI segment marginally declined to ₹ 21.2 billion.

ACTIVE PHARMACEUTICALS INGREDIENTS

We are one of the world's largest manufacturers of Active Pharmaceuticals Ingredients (APIs) and partner with several leading generic formulator companies in bringing their molecules first to the market. Our focus on innovation-led affordability gives our customers access to the most complex active ingredients, while maintaining a consistent global quality standard. Besides, our APIs development efforts enable our own generics business to be cost competitive and get to market faster.

CUSTOM PHARMACEUTICAL SERVICES

Dr. Reddy's has one of the largest Custom Pharmaceutical Services businesses in India. We offer end to end product development and manufacturing services and solutions to innovator companies. Further, our rich and extensive knowledge repository of various types of formulations helps shorten time to market and support lifecycle management.

PROPRIETARY PRODUCTS & OTHERS

- Revenue from Proprietary Products and others was ₹ 4.1 billion, decline of 3%.

PROPRIETARY PRODUCTS

Our Proprietary Products business focuses on developing differentiated formulations that present significantly enhanced benefits in terms of efficacy, ease of use and the resolution of unmet patient needs. The aim is to improve the patient's holistic experience with our medicines, so as to strengthen compliance with the therapeutic regimen and ensure positive outcomes.

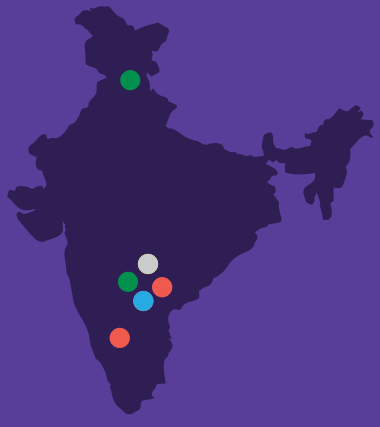
MORE THAN 200 HIGH-QUALITY GENERIC DRUGS

ONE OF THE WORLD'S LARGEST MANUFACTURERS OF APIs

DIFFERENTIATED FORMULATIONS THAT PRESENT ENHANCED BENEFITS

GLOBAL PRESENCE

- SALES & MARKETING OFFICES
- RESEARCH & DEVELOPMENT CENTRES
- MANUFACTURING FACILITIES
- HEADQUARTERS



FY2017 HIGHLIGHTS

REVENUES
₹ 140.8 bn

EBITDA
₹ 25.5 bn

PROFIT AFTER TAX
₹ 12.0 bn

DILUTED EPS
₹ 72.1

FY2017 FILINGS AND LAUNCHES

GENERAL FILINGS (26 ANDA FILINGS)
As on 31 March 2017, 101 generic filings are pending for approval (99 ANDAs and two NDAs). Of these, 99 ANDAs, 62 are Para IV filings and we believe 21 to have 'First-to-File' status.

82 DMF FILINGS
9 DMFs were filed in the US. As on 31 March 2017, there were 754 cumulative DMF filings.

93 NEW PRODUCTS
93 new products were launched in FY2017, of which 10 are in NAG, 22 in Europe, 39 in Emerging Markets and 22 in India.

GLOBAL WORKFORCE
+22,000

COMMERCIAL PRESENCE
26 COUNTRIES

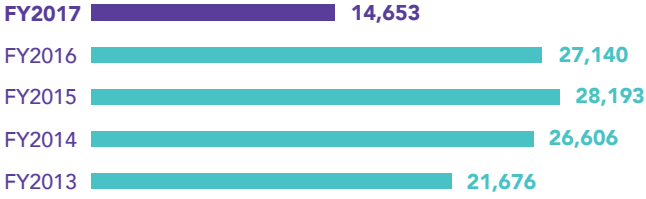
Key Performance Indicators

REVENUES (₹ MILLION)

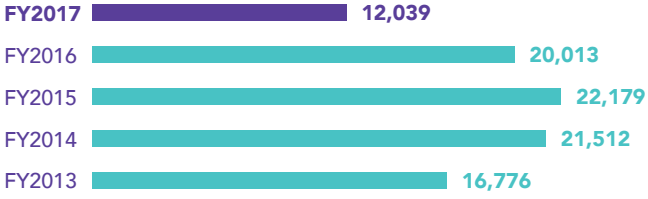
GROSS PROFIT (₹ MILLION)

EBITDA (₹ MILLION)

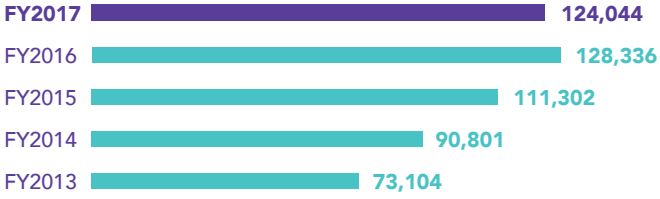
PBT (₹ MILLION)



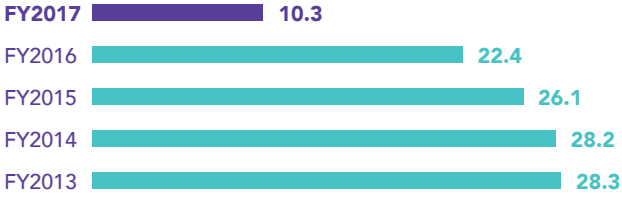
PAT (₹ MILLION)



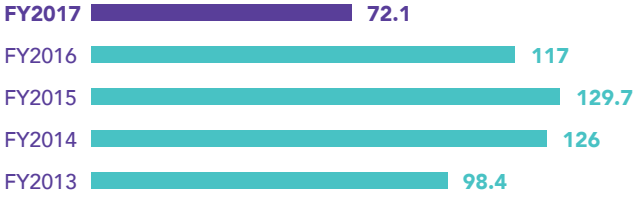
NET WORTH (₹ MILLION)



ROCE (%)



EPS (DILUTED) (₹)



Accelerating Access to Good Health

Accelerating access to affordable and innovative medicines is at the core of our work at Dr. Reddy's. The belief that Good Health Can't Wait inspires us to delve deep into understanding the needs of patients around the world and do all that it take to fulfill them.

Even as our medicines ensure good health for millions of people around the world every day, we are aware that there are millions more, in different countries, for whom high quality, affordable medicines continue to be out of reach. We realize that accelerating access to good health requires acting with alacrity on several fronts – developing products where affordable alternatives don't exist, working with all stakeholders in the healthcare systems across different countries to enable market access, manufacturing medicines of the highest quality in full adherence to the best global manufacturing practices, and ensuring their availability at all times through a robust, efficient and seamless supply chain.

We regard the good health of our patients as our responsibility and are committed to go the extra mile to ensure that they always have access to the medicines they need. In the following pages we share a few stories that illustrate our commitment to patients and our partners in the accelerated journey to good health.

Intelligent Packaging For Effective Treatment

Medicines work only when they are taken in the right dosage at the right time. And that is easier said than done. Dr. Reddy's deployed human-centred design thinking to help treatment become more effective, not just through better medicines, but through intelligent packaging.

At Dr. Reddy's, we do not see ourselves as a mere manufacturer of medicines. The concept of care and its proper delivery is as important to us as the quality of our drugs. We think beyond the molecule to ensure that we are empathetic to our patients' needs by experiencing their issues first hand.

Our Purple Health initiative was undertaken to do exactly this – improve the patients experience by identifying apparently minor issues that were a hindrance to the adherence or efficacy of a treatment.