"SeQuent Scientific Limited Q4 FY20 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day. And a welcome to SeQuent Scientific Limited Q4 FY20 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Abhishek Singhal. Thank you. And over to you, sir.

Abhishek Sighal: Hello. Very good evening. And thank you for joining us today for SeQuent Scientific's earnings conference call for the fourth quarter and financial year ended 2020. Today we have with us Manish – SeQuent's Managing Director; Sharat – Joint Managing Director; and Tushar – CFO, to share the highlights of business and financials of the quarter.

I hope you have gone through our results release, and the quarterly investor presentation which have been uploaded on our website, as well as the stock exchange website. Please note that today's discussion will be forward looking in nature and must be viewed in relation to the risk pertaining to our business. After the end of this call, in case you have any further questions, please feel free to reach out to the investor relations team.

I now hand over the call to Manish to make the opening comments.

Manish Gupta: Thank you, Abhishek. Good evening and a very warm welcome to all. I would like to thank you all for joining us for the earnings call for the fourth quarter and financial year 2020. I also would like to apologies once again for this rescheduling which we had to do from 3pm to 6pm, which was purely on account of technical challenges that we faced in uploading the results on the stock exchange website. I hope all of you are safe and hale and hearty in the confines of your home.

Joining me on this call are my colleague Sharat Narasapur, our Joint Managing Director; and our CFO, Tushar Mistry. I will start with a brief overview followed by the highlights of our financial performance for the quarter and the full year, as well as the other corporate developments. Post which we shall open the call for Q&A session.

This time is different from the previous quarters and the interactions that we had been having in the past, primarily for two reasons, one is external and faced by all of us, the COVID pandemic and its impact on the world. And the second is the internal at SeQuent, which is going through an ownership change, something that I will touch upon later in the call. Given the recent developments, I presume there could be a few new participants in the call today. And I will take a few minutes to set the stage on how SeQuent reached where it is today, before talking about the business.

Stepping back to 2014, SeQuent was a Rs. 400 crore company with two distinct businesses, human API and animal health business. We also had a small specialty chemical business then. A strategic call was taken by the promoters to create the first powerhouse of animal health business firm in India, giving birth to Alivira, our animal health focused vertical. This was followed by a series of structural moves in the animal health space, including investing in the new veterinary focused API facility at Vizag, and a string of inorganic acquisitions across the world in select geographies of Europe, Turkey, India, and Latin America, to build a strong foundation of formulation business.

Along the way, we divested our non-core businesses to channelize our energy on core business. The specialty chemical business was sold in 2014, while the human API business was demerged into Solara in early 2018. We are now a pure play animal health company with an annual turnover in the region of Rs. 1,180 crores or $165 million, making us the largest in India. And as we speak, the 20th largest animal health company across the globe. We have a track record of consistent performance over last 12 quarter ever since we became a pure play animal health company.

I will now spend some time on how the company has coped with the COVID challenges. While we did give some of a detailed business update to the stock exchanges on 8th April, 2020, on the COVID impact, I would like to take this opportunity to reiterate a few points. Pharmaceuticals and animal health industries, which we cater to, have been categorized as essential industry across the globe. And hence, we are generally exempt from the lockdowns that have impacted most industries. Further, within the animal health industry, we cater to the production animal segment, which is not a discretionary spend, and hence we see little impact on the demand side of the business as well.

In response to the evolving COVID-19 pandemic, and related execution challenges, we put in place a business continuity plan to deal with the challenges across all operations. As part of the plan, manufacturing operations across locations worldwide are working with reduced staff, while all non-essential employees are working remotely. We made alternate logistic arrangements for both men and material across all facilities to ensure continued operation as well as supplies to our customers. The swift implementation of business continuity plan allowed us to shield our operations, in India specifically, from significant disruption in a very challenging environment. All our global businesses also showed great resilience during these times with facilities in Spain, Turkey and Brazil are also operating at normal levels, while all non-manufacturing staff work from home. We did, however, face some shortfall in Germany, as our QC, quality control staff struggled to make it to factory. As a result of some of these proactive measures, we could largely achieve our plan for the quarter, say, for goods worth approximately Rs. 8 crores which we could not ship to our customers, even though ready at our end.

Let me now turn attention to our performance for the year. We set out a target for ourselves when we started the year to grow the revenues in high teens, and increase the EBITDA by about 200 bps. I am pleased to state that despite the various challenges in the last quarter, we saw a growth of 16.5% in constant currency terms as far as our top-line is concerned. While our API business grew 21.2%, our formulations business recovered quite smartly in the second half, and grew at 14.1% for the year. Turkey and Latin America stood out with growth of 67% and 26% in the respective geographies. We also had a strong second half in Europe, driven by our nutrition facility in Spain. Overall, we feel good about the way the revenue growth has panned out, which clearly demonstrates a well-diversified portfolio mix between products and geographies. I am not going to call out the Q4 numbers as it is already in the Investor Deck as also on our website. But suffice to say, that performance in Q4 mostly mirrored our full year numbers.

Operational Excellence has been at the core of our strategy ever since we embarked on this journey of consolidation. I am extremely delighted to state that we have been able to achieve the guidance of improvement in EBITDA margins by 200 bps on a year-on-year basis. While the year-end EBITDA stood at 14.9%, 210 bps improvement over the last year, the highest ever EBITDA of 17% in Q4 keeps us confident for the future. Portfolio mix, scale, and right markets were key variables that drove the margin. Even though we are conscious or cautious about the environment we are operating in, we expect the momentum to continue in FY21. We expect to maintain robust growth in both LATAM and Turkey, while Europe is rebounding, and we shall also benefit from the launch of the new injectable in the second half. We shall continue to adopt a cautious stance in emerging markets, where we believe collection risk could be a significant variable.

API continues to grow well supported by focus on regulated markets and regulated customers, as well as high value products, which continue to drive our fixed asset turn for the business, which now stands at 2.7x on Q4 annualized basis, and 2.4x for the full year of FY20. This quarter, we achieved actually the highest every API sale as well, in spite of losing out on about Rs. 8 crores of revenue. Our contribution from top 10 customers is close to 55% of our API sales, while our top 10 products contribute close to 88% of our API sales. We now have 26 commercial APIs, along with 19 U.S. filing and 11 CEP filings, with about 14-odd products in the pipeline.

On the Formulation side, we recently filed the first injectable for the U.S. market. As you all know, we are targeting about 10 new filings in the U.S. for the next three years. And U.S. will be a market that we will be increasingly looking forward to make our presence felt. Overall, we believe we are in a strong position on the Formulation side of business too. And this will drive the business momentum going forward.

The ratios on the balance sheet continue to improve as well. With our ROCE or return on capital employed now very close to 15% as compared to 3% four years back. This is almost a 5x jump in four years. Our Net debt-to-EBITDA is at 1.23 compared to 3.75 in FY17, a 3x improvement. Cash from operations improved to Rs. 127 crores during the year as compared to Rs. 2 crores in FY17. And the Net debt to Equity finished the year at 0.29. You would also notice that our net debt is moving in the right direction and is reflective of the strong cash flows that we derive from the business. In effect, all the ratios are moving in the right direction. And this again is a testimony to the single minded focus and relentless execution of the management team, backed by unflinching support from the promoters to execute the strategy.

You would notice that the audit report carries the remark around physical verification of inventories in Europe. This is on account of the inability of the respective auditors to carry out such verification at the peak of COVID pandemic in those territories. However, the auditor has been able to carry out alternative procedures in India, as guided by the Indian regulatory body. Such alternate procedures were not available for the auditors in other geographies. However, as a pharmaceutical organization, we have complete internal control on inventory management, and we see no challenge around this once the verification is undertaken.

Recently, AnimalPharm Awards recognized Alivira as the top company from India, Middle East and Africa. This global recognition does provide us both impetus and motivation continue to do well.

This brings me to address an important corporate action that all of you might have seen and would be eager to ask questions about. Global investment firm, The Carlyle Group has entered into a definitive agreement with the existing promoters of SeQuent Scientific to acquire a majority stake and up to 74% in the company, including up to 26% equity shares from public shareholders. This is an inflection point in the journey of the company as a SeQuent can now leverage Carlyle's global network and resources to move to the next bit of growth and innovation. Carlyle is no stranger to the Indian healthcare market, with a history of investing in the healthcare sector, both in India and globally, fueled by deep understanding of the market, and an ability to create value through its operational expertise and close partnership with management. This transaction is their largest control deal in India and is reflective of their confidence, both on the sector, as well as the business model of SeQuent. I believe with Carlyle as the new promoter group, we are well poised to the new phase of development, where we together with Carlyle will work to grow the company into one of the top global animal health care company.

I take this opportunity to place on record my sincere thanks to Arun Kumar and KR Ravishankar, our current promoters, for their vision and support which took SeQuent to where it is today, which is India's largest animal health company, and also amongst the top 20 global animal health companies in the world. We are confident of treading the path of continued growth to the benefit of all stakeholders.

With those few words, let me throw open the floor for question and answers.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from the line of Rajesh Kumar, an individual investor. Please go ahead.

Rajesh Kumar: I have two questions. The first question is, based on the COVID situation that is evolving, how do we see the situation for API as well as pharmaceutical in terms of the working capital? Are we seeing any stretch on the working capital cycle?

Manish Gupta: What is your second question?

Rajesh Kumar: And the second question is related to the formulations in the European business. The Jan to March quarter has been excellent, it's been a wonderful work done in that area. Are we seeing any challenges or, let's say, any COVID related issues in the first quarter of the new financial year, which is April, May, June?

Manish Gupta: Okay. So let me address the demand side of business and its potential impact. So basically, as I mentioned earlier, we are in animal health, and within that production animals, and within that also a generic company, which fundamentally offers a better price proposition to the customers. So, as we speak not only for Q4, but even Q1 we see our business to be certainly on in the normal course of business, both in terms of order book as also working capital management. We are not seeing any challenges thus far. Having said that, it's evolving world and it's very difficult to predict the future, because every country is struggling to kind of respond to this challenge. So the way I look at it is, we are taking one quarter at a time. As we speak Q1 looks good. We shall evaluate the year as it rolls by. As a company, we are extremely cautious on the cash flow management, that has been our single most strength as a company I would like to believe. And there is nothing we will allow to take risk on those counts. So, we are very cognizant of collections and cash flows. And that is also one of the reasons why we are playing very cautious on the emerging market.

Rajesh Kumar: Understood. Just a follow-up, if you would please allow me. Would there be any impact on the new launches? Let's see, I know it’s a little forward-looking statement, so please feel free to disregard this question.

Manish Gupta: I don't see any reason for any change at this point of time.

Rajesh Kumar: Okay. And any disruptions in terms of intermediate supplies from China?

Manish Gupta: None at all. We have been very proactive in this regard. Second, our dependence on China is very limited, especially on the API side of business. So, certainly, again, I would like to reiterate that we do not foresee any challenges to the business

Moderator: Thank you. The next question is from the line of Alankar Garude from Macquarie. Please go ahead.

Alankar Garude: Sir, my first question is on our medium-term goal where we had said that we are targeting high-teens growth and margins about 20% in the next three years. So with this COVID-19 situation and even otherwise, are you sticking to this goal? And secondly, if you could also provide some idea as far as the FY21 outlook is concerned, that would be helpful.

Manish Gupta: So, Alankar, this one is a very difficult question to respond, because nobody can predict the world as we see it today. I keep getting new update from all the management consultants every week, and they are very different from each other. Having said that, given just the nature of industry and the strength of our business model, currently, we do not believe any reason to change our medium-term objectives. So we stay confident of largely achieving the medium-term goals. Having said that, for the current year, I am looking at business one quarter at a time. Q1 certainly looks robust for us despite the peak of the challenges. And I do believe, again, as we roll forward, things will get better and not worse from here.

Alankar Garude: Understood, sir. And secondly, I wanted to ask you on the Carlyle deal. Can you throw some light on whether Carlyle has any investments on the animal health side anywhere else in the world? You mentioned about them having presence on the pharma side, I think. So firstly that. And secondly, how can they help us grow further from these levels and help us achieve our objective of being amongst the top players globally within the animal health space?

Manish Gupta: Yes. So there are a couple of areas wherein they can certainly add value. First is, of course, Carlyle has fairly strong healthcare practice around the world, significant investments on the pharmaceuticals and healthcare side, and they do have some investments on the animal care side, not so much in the pharmaceutical side, but more on the nutrition side of business, including, I believe, some stake in very big CP group in China. So as they have explained us, we are looking at two or three areas of contribution. One is fast-tracking our growth in the U.S., and also China, which is the second largest animal health market in the world. So, while we had our own plans for U.S., clearly Carlyle can help us fast-track that. And while we had no plans for China, clearly, again, Carlyle can help us build up a plan for China.

The other element is vaccines. Again, on our own there was nothing we could have gone or done to build that technological gap. But we believe with Carlyle's expertise and global network, we will be able to do that. So these are the couple of areas where I believe Carlyle can get very clear value to our growth platform.

Alankar Garude: Sure. And finally one last question from my side. If I just look at the emerging markets performance, specifically in this quarter, it's almost a 15% decline. And even in constant currency terms, it's a pretty sharp 13% decline. And I think in your opening remarks, you also mentioned about being slightly cautious over there. So can you just highlight what exactly are the issues you are facing in these emerging markets?

Manish Gupta: Yes. So, for our case, emerging market includes India, wherein we do have a business. And just for information, our Indian business did about minus 25% in Q4, simply because there is no money available to collect. So selling is very easy, but money is not available to collect. And that's not a space we want to get into, because for such a small business if we get into collection issues, I think it will not be good for the organization. So, we have chosen to take a step back and unless the collection concerns are addressed, we will not take aggressive stance in these markets, including the other emerging markets which are also oil dependent. Now, with the global crash in oil prices, obviously, we do expect payment challenges even in those countries. So, we will certainly follow a wait and watch policy as far as emerging markets are concerned. Having said that, our dependence on this business is very limited.

Alankar Garude: Right. And just one quick follow-up. When you said collection issues are specifically in India, who will be the counterparties?

Manish Gupta: No, this is like a pharmaceutical business, so you have to deal with stockiest and the retailers. And the final consumer is farmers, so you can understand the rural distress that we have in our country today.

Moderator: Thank you. The next question is from the line of Vishal Manchanda from Nirmal Bang. Please go ahead.

Vishal Manchanda: Sir, I have a question pertaining to this injectable launch that is scheduled in FY21 in Europe. So would this launch happen pan-Europe? Or would this kind of be a staggered launch first in specific geographies and then other geographies?

Manish Gupta: So it would not be certainly pan-Europe, but it will be definitely in the key geographies of Europe. So we have undertaken a decentralized procedure for this, a DCP, with some 10 or 11 countries, which are critical and relevant for this product. So that's how we have gone about it. And obviously, it will be ethical approval and therefore the product will be launched in all those geographies.

Vishal Manchanda: So each individual approval will come at a separate point in time, but it will come in the second half of FY21, is that correct?

Manish Gupta: No, the approval will be single approval, it's a DCP procedure as it is called in Europe, which is slightly misunderstood, but because it is one approval for the countries we participate in. So approval will come in one shot. The launch will be based on the patent expiry. So the patent expiration date is also, of course, common across Europe. Somewhere in November or December is when we expect to launch the product, end of November.

Vishal Manchanda: So you will be launching in all those 11 territories that you have applied for in that fourth quarter of FY21, can that be a fair assumption?

Manish Gupta: That's correct.

Vishal Manchanda: So will France be also one of those territories where you would have applied for approval?

Manish Gupta: That's correct.

Vishal Manchanda: And since you don't have a very significant presence in France, so would this approval kind of help you build a presence or it will be kind of still difficult for you to launch this in France? And will France be the largest geography for this product?

Manish Gupta: No, France is not the largest geography for this product. So, certainly in all the countries where we have our own front-end, we will be launching through our own front-end. In some markets like France wherein we are at a very early stage, we may look at option of launching ourselves and also appointing a larger company as a distributor.

Vishal Manchanda: Okay. So we will partner that product in geographies where you don't have a front-end?

Manish Gupta: Absolutely.

Vishal Manchanda: So there will be some distribution fees that will go, but should not be significant?

Manish Gupta: Yes. I mean, fundamentally, it will be in our interest to maximize our revenue, which is what we will do.

Vishal Manchanda: And any sense of competition that you are expecting, what sort of competition would come in?

Manish Gupta: So, it's difficult to predict at this point of time. But having said that, it will certainly have handful of competitors, because no generic animal health company worth its while can ignore this product. So I do foresee between three to four companies, more or less at the time of launch.

Vishal Manchanda: Okay. And would this product have any complexity which will reflect the competition to an extent?

Manish Gupta: See, irrespective, animal health industry is not as competitive as one pharma. And plus, it is an injectable. So obviously, you will need injectable capabilities for you to be able to launch this. So that further restrict the competition.

Vishal Manchanda: We have limited companies with injectable capabilities in the animal health category.

Manish Gupta: Absolutely. Yes.

Vishal Manchanda: And sir, during the quarter we have seen a strong margin expansion at the gross level. So is this on account of API sales becoming more prominent during the quarter?

Manish Gupta: So, it's really a mix of API sales and also Turkey business, because Turkey is also one of our better margin business, and so is our API business.

Vishal Manchanda: So, this gross margin at 50%, it should be around this number, closer to this number going forward?

Manish Gupta: The idea is always to make it better. But difficult to predict exact numbers. But given our focus on regulated markets and better priced higher priced products, my belief is we will be improving our gross margins as we build our business.

Vishal Manchanda: And on the exchange loss of Rs. 6.5 crores, how would you explain that?

Manish Gupta: Tushar, if you can respond to that.

Tushar Mistry: Yes. So, as you know that we operate into multiple geographies, some of the geographies have currencies which are pretty volatile, like Brazil and Mexico. Due to this COVID-19 pandemic hitting during the month of March, by the end of March these currencies moved in a very volatile manner and they depreciated more than 25%. And we had certain creditors sitting on the balance sheet on dollar terms, and this hit was on account of that. While having said that, the way this geography manages, they peg their pricelist to the dollar movement and all their selling prices will undergo change for the market, but that will be all prospective. So, on a near-term perspective, the impact will be all absorbed positively in the financials. But for the quarter there is an impact that will hit us.

Moderator: Thank you. The next question is from the line of Nisarg Vakharia from Lucky Investment Managers. Please go ahead.

Nisarg Vakharia: Congratulations on a very consistent and a stable performance. Manishji, I wanted to ask you that, you know, we have a working capital of about Rs. 300 crores for this year. Is it possible to give a small breakup between the two businesses, formulations and API? I wanted to understand which business is more heavy on working capital.

Manish Gupta: I don't have this handy. Maybe Nisarg we will have to connect again on this. But at a broad level, the working capital across both the businesses are not very different in terms of number of days.

Nisarg Vakharia: Okay. Second question, this Rs. 400 crores of API business which has grown at 20% Y-o-Y, what sort of capacity are we sitting on to take it what sort of revenue over the next two years?

Manish Gupta: Yes. So, at a broad level we are targeting similar growth rates in the medium-term. In terms of capacity, we certainly do have capacities to cater to FY21 requirements. But as we speak, we are working on an expansion plan and my colleague Sharat can provide more colour on that, which will be useful for fulfilling the demands from FY22 onwards. So Sharat, if you can give some colour on the expansion that we are undertaking.

Sharat Narsapur: Yes. So, this expansion is basically at our Vizag site, wherein historically we already have the construction of the civil building ready. So what we are trying to do is equip them and also build a couple of clean rooms. And they should be ready by December of this year. So there has been a small impact due to COVID, we are slow at the moment. But we will go ahead with that,. So in terms of capacity, our plans are quite clear.

Nisarg Vakharia: Okay. And lastly on the API side, again. Manishji, has there been any one-off pricing advantages that we have seen in the API business last year? Because normally a lot of API companies enjoy some pricing advantages which does appear later.

Manish Gupta: Not really. So if we look at our business model, we do not have large products. And we are not a commodity API player, we are fundamentally multiple products with multiple customers. And regulated market is our strategy. So we are not working or seeing any one-offs kind of thing in our API strategy. These are long-term arrangements, because even qualifying our API takes a couple of years.

Nisarg Vakharia: Okay. So out of Rs. 400 crores what would be the maximum contribution from a single molecule?

Manish Gupta: I think the only big molecule which we have is Albendazole, which is, of course, a product which goes for both human and animal health purposes. And that is doing well as well. And that's where we have taken about 20% capacity increase, which has also helped us grow that business. I don't have off-hand numbers, but my guess is it will be accounting for about 25% of our API revenues, 25% to 30%.

Moderator: Thank you. The next question is from the line of Manish Gupta from Solidarity. Please go ahead.

Manish Gupta (Solidarity): Hi, Manish. I had two questions. The first one is, can you provide some colour about how the opportunity for our API business has changed based on whatever we read in the press between what's going on between the U.S. and China? So that was the first question. The second question was that, is our formulation business globally, does it have any advantage at all with our India back-end? And I had a third question as well, which is that, I guess, you said that we are a generic player. But as we are trying to build our front-end in many markets, for example, the U.S. and all that, at what scale in these markets will be bottom-line start contributing meaningfully to the business?

Manish Gupta: Okay. So first question, China and U.S. Too early to predict based on the recent developments, but some of the movements we have been seeing over last one or two years. So clearly, just like we were derisking ourselves from China, many of the bigger companies have also been doing that. And this was one of the reasons why our API business has been growing, because companies are looking at second options for all the key APIs. Also, I think the bigger benefit we are enjoying is from the segregation of animal health businesses from their parent human organization, so the likes of Merck and all, some are making it a separate vertical, and Zoetis, Elanco have created separate companies. And therefore, we are seeing a fairly good traction on our API side of business. I can only give you some colour on what things we see changing in last couple of weeks, which is where -- and I don't know whether it is right or wrong, we are seeing that some of the Chinese employees who were marked on emails are no longer been marked on those emails by our customers. So, I definitely foresee some kind of move that is happening towards derisking from China, internally across all the global companies.

Your second question was on formulations and the India back-end advantage. The only back-end advantage which we see is in the R&D side of business as far as animal health is concerned. We do not foresee much advantage on manufacturing side of formulation, simply because of too many formats and too few or too little volumes in animal health. So India advantage really comes in when there are volumes. That does not really work in animal health. But on the R&D side, clearly there are India advantages and that's why some of our value added products, especially injectables, are all getting developed in India.

The third question was the scale and when do we see the scale benefit on the formulation side of business? I think we are still two years away. And the scale advantage will start showing up when our value added products start getting launched. The first one gets launched in Europe towards the end of the year. But the first commercial benefit in U.S. is at least two years away. So the formulation business will drive our margins only from FY23 onwards. And most of our margin expansion between now till FY22, I foresee would be coming from the API side of business.

Moderator: Thanks you. The next question is from the line of Sachin S from Swan Investment. Please go ahead.

Sachin S: Sir, two, three questions. One, what is the CAPEX plan for the current year?

Manish Gupta: I can give you a two year CAPEX plan. We would be spending about Rs. 90 crores between India and Germany for expanding capacities at Vizag and also the injectable capacity in Germany.

Sachin S: Okay. And is there going to be any maintenance CAPEX other than this Rs. 90 crores over the next two years across other sites?

Manish Gupta: This largely includes the maintenance CAPEX as well.

Sachin S: Okay. So does it mean that the net debt, which has seen a reduction of around Rs. 30 crores, Rs. 35 crores this year, we could see further reduction in the next two years?

Manish Gupta: Absolutely. Unless we do any inorganic strategy, the net debt should keep coming down.

Sachin S: Okay. Secondly, now that we have this investment in Solara and in Strides, and now that we are no longer going to be part of that group, so what is the strategy on the investment in Solara and Stdires for the change in management?

Manish Gupta: Yes. See, we have been always mentioning and maintaining that these are treasury investments for us and will be used as growth capital going forward. And the same situation state we shall use it as a growth capital as and when required, and as and when we feel the pricing is right.

Sachin S: Sir, this European injectable launch, any sense which quarter we could look at? Is it like first half or second half, what is your sense on the likely time of the launch?

Manish Gupta: No. So the European launch will happen in end November or early December, kind of launch based on patent expiry. And the U.S. launch will be another one year after that.

Sachin S: Okay. Sir, you mentioned in one of your opening remarks that with the entry of Carlyle, it could help you in terms of the U.S. market. So you had also mentioned that you are looking at some sort of doing an inorganic front-end acquisition in the U.S. So does Carlyle coming in helping way of accelerating that or getting a more suitable candidate? If you could just comment on that.

Manish Gupta: Yeah, absolutely. I think that goes without saying. See, what Carlyle brings in a lot of bench strength around managing partners, and these are ex-CEOs of various pharmaceutical companies, including animal health companies. So the network that Carlyle brings to the table is very different from what we had in the past. But more importantly, even the cheque size, so if you look at historically, all our deals were very, very small. And it was purely coming out of our ability to take risk and our ability to write the cheques. Now that certainly will change, because Carlyle, while they have bought the company for our business plan, but they definitely would add to this business plan to accelerate it further and faster. I clearly foresee that whatever we were aspiring to do, both in terms of scale, and also speed, Carlyle will fast track that.

Sachin S: Sure. And just lastly again on U.S., we still remain on plan for starting U.S. formulation in FY22, that's the way we should look at it?

Manish Gupta: Correct.

Moderator: Thank you. Next question is from the line of Anubhav Saho from MC Research. Please go ahead.

Anubhav Saho: If I understand from your comments, the CAPEX budget for medium-term remains intact, that is Rs. 90 crores which you highlighted. But in your early communication, you mentioned that the injectable plant in Germany would be kept on hold for some time. So has the situation improved from there? And what are the challenges there on that side?

Manish Gupta: Yes. So that's why I mentioned this Rs. 90 crore investment is over two years and not over one year. The expansion plan in Bremer, the project was to start in July, which meant obviously all our vendors had to be ready with the equipment. And you can understand that currently it is impossible to undertake any project in Europe, because the vendors have not been working for a couple of months or at least between four to eight weeks. So therefore, rather than starting a project and then you are stuck with it in an incomplete form, we decided that we will defer it and only start the project towards the end of the year. So, as we speak, we are targeting that instead of July we will start the project in December. It will take about three to four months to complete the project, so on an overall basis it does not have any impact. But a part of this CAPEX flows into the next year.

Anubhav Saho: Got it. And in case of Vizag any change in timeline? You mentioned some moderation plan, so does it change any way as per the scope of expansion?

Manish Gupta: So, Vizag impact is comparatively very limited. So we were to place purchase orders when the COVID pandemic hit. So obviously, we didn't want to be stuck in that situation wherein you give advances and then the vendor may or may not deliver. Now that we know who all are doing well and who are not doing well, so we are now ready to place an order. So at best, in Vizag there will be a delay of one month or so. Is that right, Sharat?

Sharat Narsapur: A couple of months, yes.

Anubhav Saho: Okay. And sir wanted a couple of more details on your early update. One is that on the CDMO business model which we probably are initiating or have initiated. If you could spell out what is the opportunity size we are looking at? And if you can spell out some more details vis-à-vis geography or any other details, which would be helpful.

Manish Gupta: Yes. So I will have Sharat speak on this better than me.

Sharat Narsapur: So, we have initiated the CDMO business. And the first couple of contracts we are working on right now. And as I speak, there is a proposal for a dozen products which has already gone in, and they are under evaluation. And we expect at least about 70%, 80% of them to fructify. So, in terms of size, it would be too early to comment. I think we need to wait till things shape up. But having said that, we have made a beginning for sure.

Anubhav Saho: Okay. And sir, I have one more question, regarding our India business, again, one of your recent update was that we are trying to establish a distribution partnership with a global leader. So though this plan having a rethink now, because we want to wait and watch as far as few of the markets are concerned or is it on track?

Manish Gupta: It is certainly on track, and right now we cannot communicate anything in this regard. But by June we should be able to unveil everything around that.

Moderator: Thank you. The next question is from the line of Anurag Patil from Roha Asset Managers. Please go ahead.

Anurag Patil: So in terms of receivables, are we seeing any stress? Because in a FY19 and FY20 our revenue has increased by around Rs. 140 crores and incremental receivables are also up by around 30% to 35%. So relatedly it seems a bit higher side. So that was my question, issue on the receivable side for us, particular.

Manish Gupta: See, as a business structure, certainly we are not seeing any stretch or collection delays. But I think Tushar, if you are on the line, if you can give it better or deeper color to it.

Tushar Mistry: Yes. So if we look at year-on-year comparison of debtors, they are in line with the business that has expanded. So we don't see any big challenge on this front. And all of our debtors are pretty well monitored and evaluated almost on a monthly basis.

Anurag Patil: Okay. So can you just clarify the numbers, because they are not clear in the result? So absolute increase in the receivable, if you can just clarify.

Tushar Mistry: So, receivable last year were Rs. 278 crores, or Rs. 2,782 million. They are at Rs. 3,188 million in the current year.

Moderator: Thank you. The next question is from the line of Vipul Shah from RW Equity. Please go ahead.

Vipul Shah: So, in the press release on 8th of April, company had mentioned that they are actually looking out to consolidate their holdings and pursue consolidation of the minority interest. So just wanted to understand what is the plan on that?

Manish Gupta: Yes. So this largely pertains to Turkey wherein the existing promoter also had a put option at the end of 2019, which is what he has exercised. Also, the new shareholder wants us to consolidate because, obviously, that has a better benefit in the long run. So as we speak, we are negotiating and finalizing our buying out of the Turkish minority stake. And that can further accelerate to other geographies as well.

Vipul Shah: Because if you see, the proportion of minority interest to PAT, actually has deviated quite on a quarter basis and a full year basis. So how should we look at these numbers going forward? Because we have, I guess, some minority interest in Spain as well. What is sustainable, whether it is 10% of PAT is attributable to minority? And going forward do you foresee that we will be able to consolidate all our shareholdings in all the subsidiaries?

Manish Gupta: See, technically answer is yes. It also partly depends on what the new shareholder wants us to achieve. Because everything has a cost to it. And it all depends on where you want to invest the capital. So we have been guiding in the status quo basis to about 15% of our PAT to be attributable to minority interest. I don't know the numbers offhand, but I am sure at an annual level we won't be very different from that. A lot of our growth in profitability is coming from our API business. So obviously, the minority interest will continue to reduce in the medium-term in terms of percentage of the overall profitability. And any further consolidation of my notice stake will further reduce that minority interest.

Vipul Shah: So if we say some of that 15% of PAT ballpark is attributable to minority interest, and with the Turkish transaction being in consideration as we speak, and if it is completed and consummated, what is the change in the minority interest, I mean, as a percentage of our PAT?

Manish Gupta: Tushar, would you have a guess there?

Abhishek Sighal: Sir, Tushar has dropped out. We will just drag him back in.

Manish Gupta: So we will get him back in. But basically I can guide you that Turkey is obviously a significant part of the minority interest because of the higher profitability that we enjoy there. So, I am sure that more than 50% of the minority interest would be on account of that.

Vipul Shah: Which you say probably in this, as we move ahead in this year we will be able to consolidate this?

Manish Gupta: Certainly.

Vipul Shah: Sir, if I may, I had one more question on the tax rates. It's very volatile, it's very difficult to ascertain what is the percentage of tax which we should budget, the company would budget or rather forecast?

Manish Gupta: Tushar, if you can. There is a question around tax rate that we should consider in the model.

Tushar Mistry: Yes. So we have been guiding, I would suggest that you don't look at the quarter-on-quarter tax numbers, because they may vary. But we had also spoken about this last time that you look at over annualized tax cost, and should assume between 15% to 18% as tax rates going forward.

Vipul Shah: Sir,, thank you so much. If I may ask one last question, with the Turkish currency hitting all time low, does it have a negative impact on our business?

Manish Gupta: See, they are all made in Turkey for Turkey, or made in Brazil for Brazil. So, while there are translation impacts on currencies which any global company will have to face. But by itself, it does not have any negative impact on the structural solidity of those businesses. So that's all I can say. I mean, our individual businesses, whether it is Brazil or Turkey, they are rock solid and doing very, very well. Currencies are dealt in a particular manner in all the geographies, so most geographies have moved to a dollar linked prices, which is how they operate. But at the quarter end or year end, if there is a very dramatic shift, then there is always some translation losses that come and hit us.

Moderator: Thank you. Next question is from the line of Vishal Bora from MK Ventures. Please go ahead.

Vishal Bora: Sir, congratulations for the transaction with Carlyle.

Manish Gupta: I think that you have to convey to the promoter.

Vishal Bora: Sir, but the performance of the management would be a key driver, right, for the transaction, so take my compliments. Sir, a couple of points. First, what is the behavioral shifts you perceive with the entire COVID thing? In terms of, say, the animal health market as a whole, whether it's the buying behavior of end clients or whether it is from a B2B perspective or a clients' perspective, what are the trends you perceive that there will be dramatic shifts in this business, can you tell me?

Manish Gupta: I am not an economist to predict this broadly, but typically the only thing I can say is whenever there is a downturn, people become more value conscious. Which means, in the animal health parlance, it will be that we will look for cheaper protein, which is poultry vis-à-vis beef. And within the way you treat your animals, you will look for cheaper products which is branded generics vis-à-vis the innovator products. So that is a broad theme I can see. The demand for protein is not going to go away because the population is in debt. So, largely, I see the environment to be more conducive for a company like us, which represents a better value proposition value opportunity for the customer. Is that clear?

Vishal Bora: Yes. In fact, just as a follow-up on that, like you have at times of, let's say, when a disease is around or things like that, people suddenly become more conscious about even other health issues or medicines in general the consumption goes up. You think that something like that could happen from an animal feed perspective or animal medicines perspective as well, that people may just become more conscious about the entire animal health aspect?

Manish Gupta: Not really that much, because in animal health it's very commercial decision making, unlike human pharma wherein it's a very emotive decision, let's say. If Trump said Azithromycin is working or HCQ is working, then suddenly everything flew off the shelf, such things don't happen in animal health. So I don't see an emotive impact in the animal health business.

Vishal Bora: Great. And if you can help us understand the U.S. business a little bit better in terms of what drivers or what are monitorable over the next, say, 18 to 24 months?

Manish Gupta: Obviously, all deliverables for next 18 months for sure will be on the API side of business. And that's what is going to gain traction as we go along. And most of our API growth will actually come out of U.S. Starting end of 18 months to 24 months, that's where our first formulation sales in U.S. should start with the commercialization of the first injectable. Having said that, I think we will be back to drawing board along with our new promoter and we will be working on fast tracking our U.S. program.

Vishal Bora: Including the acquisition which you have hinted at in previous quarters?

Manish Gupta: Absolutely.

Vishal Bora: One last questions, because you mentioned Carlyle as well, overall what are the changes we can expect? Are there any changes in terms of the overall strategy or in terms of resources, or anything that you can sort of hint at? I know it's quite early, but still.

Manish Gupta: As of now and based on what we are told, obviously, the couple of growth engines they will be looking to add is, one is U.S. in terms of acquisition, maybe China and vaccines. And they will be hopefully able to help us attract some key talent, which we might not have been able to do on our own. But in terms of strategy, I do not foresee any deviation from what we have been doing.

Moderator: Thank you. We take the next question from the line of Sarvesh Gupta from Maximal Capital. Please go ahead.

Sarvesh Gupta: First of all, congratulations on having this deal closed. And I am sure that the incoming promoters would have seen the good work done by the management team. So, it's good to hear that. Secondly, for quarter if I take out the revenues for emerging markets, which are definitely under some sort of a turmoil, we definitely see some sort of a slowdown in our API business, even if I add back Rs. 8 crores which we have lost. And now when you say that Q1 is looking to be robust, are we reverting back to our previous growth rates in API and in formulation ex of emerging markets or is it Q4 growth rates are going to be the new normal?

Manish Gupta: No. So see, we have been guiding to mid-teens growth on our API business. You have to bear in mind that we bought back Mahad and there was just full year benefit of Mahad facility that helped us grow our business a bit faster. But the second half growth rate, if you adjust it for that Rs. 8 crores, would be more reflective of the medium-term growth rate that we should be able to deliver on the API side of business. Also, this does not take into account the CDMO model which we have just initiated. We are yet to develop numbers around it because it's our first foray in that sector. And that should further accelerate our API business going forward. So all in all, I do foresee mid-teens to high-teens growth rate for our API business in the medium-term.

Sarvesh Gupta: Understood. And with this Carlyle coming in, are there any key management changes as well as cost structure changes because we are, I think, operating on a slightly lower cost model in terms of our operating overheads that you foresee with the coming change in promoter?

Manish Gupta: So I don't foresee any changes immediately, certainly. Carlyle, obviously, has acquired us for the business plan that we have, plus something more that they want to add. Now, what they add and how they add is yet to be kind of determined, because these are largely inorganic and something which we have not been doing. So very difficult to answer that question in that context. But certainly, there would be some additions, both in terms of cost, but more importantly revenue opportunities as we go along once Carlyle is able to bring in the value that they are looking at.

Sarvesh Gupta: Okay. And finally in Q1 I think you mentioned that, at least the European capacities are all working up to 90% and things are becoming better with time. But, there are some logistical problem that we keep hearing about. So, net, net, apart from the emerging markets is this business as usual for our formulation business as well for our ex of emerging market formulations business?

Manish Gupta: Yes. So I will have Sharat respond to some part of it. But at a broad level, one of the things we take humongous pride in SeQuent is speed and nimble footedness. And I believe we are one of the few companies who have managed the COVID situation very well, not only in our India operations but also in our global operations. Sharat, if you can throw more color whether in terms of do you see any impact?

Sharat Narsapur: Yes. So, obviously, during the first few days of the lockdown, there was a turmoil. And logistics, as you rightly pointed out, was impacted heavily. But then as clarity emerged, things have come back on track. And today we are almost 50 days into lockdown now, and things are only getting better day by day. So, there are still few issues to be ironed out in terms of small, small issues on logistics. But by and large ports have started operating. There are a cost issues associated with it. But in terms of achieving the goals, I don't see challenges.

Manish Gupta: In this context, let me explain you the ways we thought about it. First thing we said is, let's secure our plant operation. Because if we produce we can sell, but if we cannot produce there is nothing to sell. So the biggest effort we undertook as far as our response to COVID was concerned was to ring fence our plant operation, both from a supply chain perspective and also from an operations perspective. And I believe we have been much better than most of our counterparts in the industry in securing that. Now, coming to eventually logistics and sales, as I said, as we lost Rs. 8 crores this quarter, but this effectively means that instead of selling on 31st March, it will go sometime in April. But that's about it. But if you do not produce there is no way you can sell. So our entire effort has been on ring fencing and securing production in these challenging times, which we have achieved very well.

Sarvesh Gupta: Thanks, Manish, Sharat, and Tushar, all of you have done a great job. And I am sure that you will take the company to new heights under the new promoters. Thank you.

Moderator: Thank you. We take the last question from the line of Vishal Manchanda from Nirmal Bang. Please go ahead.

Vishal Manchanda: Thanks for the follow-up. Can you share some colour on how would the numbers be in effect FY21 in terms of the formulation business and API business?

Manish Gupta: Vishal, I will ask you a counter question. When does the lockdown open up in India? And I will give you the number. I mean, this is going to be the most challenging aspect to respond. I think because world is evolving, and none of us have a clear view. Having said that, I can assure you that we as a management team are committed to deliver the objectives that we have set for ourselves. And unless there is some unforeseen circumstances that evolved over the year, we stay confident as of now to deliver the objective.

Vishal Manchanda: Okay. So even on the API side would it be difficult to give a colour on the growth rate?

Manish Gupta: See, we do foresee high teens growth rate on API front as well, which I have been alluding to. But fact is, see today suddenly Mr. Modi announces that no production to be done across the country, I can't do anything thereafter. Okay? So it is a lot to do with the flip-flops and whims-and-fancies that are happening in the country. Because somewhere we are not accepting the reality, I mean, right now no state wants to take the lead in opening the lockdown. While the world is now accepting that this is the new reality, and we have to start working in this environment. So we stay cautiously optimistic is the kind of word I will use at this point of time.

Vishal Manchanda: But like in terms of what you would have in terms of launches, assuming things don't become worse from here and the lockdown opens, you would have enough launches to sustain the growth that we have been seeing over the last few years. So you have, kind of, organically you have a pipeline basically to deliver if at all things don't go bad, the pipeline will deliver for you and you can expect mid-teens type of growth?

Manish Gupta: So, let me put it this way, unless things get worse from what it is today, or much worse from what it is today, I think our business plan for the year would stay intact.

Vishal Manchanda: Okay. And sir just one more on the API side. There are six API's that you are the sole player for. So how many of these you already have commercialized and how many won't be commercialized whenever your partner launches?

Manish Gupta: I think most of them will get commercialized, none of them would have been commercialized in terms of commercial sales, they would have been all validation supplies made to the partner.

Vishal Manchanda: Okay. Sir, is Albendazole not a product where you are the sole API manufacturer?

Manish Gupta: So we are not participating on the U.S. market for Albendazole at all. Because your question on Albendazole must be U.S. specific, so that's why I am saying.

Vishal Manchanda: Because what I go see, in Albendazole probably you are the only DMF filer with an active status, others probably are not active on the DMF.

Manish Gupta: Our DMF went to Solara in the demerger.

Vishal Manchanda: Not the DMF, VMF.

Manish Gupta: VMF, yes. But not the DMF. VMF we are in the process of commercializing in U.S., but probably in the coming year.

Vishal Manchanda: Okay. So all these six APIs are yet to add to your number basically?

Manish Gupta: That’s correct.

Moderator: Thank you. I now hand the conference over to Mr. Manish Gupta for closing comments.

Manish Gupta: Thanks once again to everyone for your insightful questions and comments. Should you have any follow-on question, please do call our Investor Relations team or reach out to management team for setting up a meeting. As we continue our journey with the new promoter, I would like to use cliched statement that says, "Change is a constant", and this is more apt for the Arum Kumar Group of companies. Yes, we now have a new promoter, but everything else remains constant. And you can expect the same level of focus and executional excellence. We look forward to interacting with you in the near future. Thank you once again. And have a good evening.

Moderator: Thank you. Ladies and gentlemen, on behalf of SeQuent Scientific, that concludes this conference. Thank you for joining us.