"Laurus Labs Limited Q1 FY-23 Earnings Conference Call"

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MODERATOR: **MR. MONISH SHAH – ANTIQUE STOCK BROKING LIMITED**

Moderator: Ladies and gentlemen good day and welcome Laurus Labs Limited Q1 FY 2023 Earnings Conference Call hosted by Antique Stock Broking Limited. As a reminder, all participants' 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. Monish Shah from Antique Stock Broking. Thank you and over to you, Mr. Shah.

Moni Shah: Thank you, Neerav, good morning and welcome to Laurus' Q1 FY 2023 results conference call. We thank the management for giving us the opportunity to host this call. Today, we have with us Dr. Satyanarayana Chava – Founder and CEO, Mr. V. V Ravi Kumar – Executive Director and CFO and Mr. Vivek Kumar from the Investor Relation team.

I would like to hand the call over to Dr. Satya for his opening challenging comments. Thank you and over to you sir.

Dr. Satyanarayana Chava: Thank you Monish for this introduction. Thank you for joining us for our Q1 FY 2023 Results Conference Call. Since COVID-19 continued to cause challenges with increased infections with new subvariants. We hope everyone of you and your family members, colleagues and friends are keeping safe and healthy during the times.

We are pleased to have this opportunity to update you on the progress and answer your questions. Our Q1 results reflects, a very healthy start to our FY 2023. As we continue to improve on product mix and EBITDA was maintained at 30%. This was achieved despite ongoing disruption in the business environment due to COVID-19 and geopolitical scenario. Our CDMO division delivered exceptionally good performance offsetting pressure on our ARV business and growth in API division was modest but future business prospects appeared very encouraging. Imported RM prices have largely remained elevated in the light of supply chain conditions but we do anticipate some of these challenges to abate with gradual China lifting sanctions during COVID and also easing off, geopolitical situation across the globe.

We are progressively expanding our portfolio and new initiatives this along with our significant investment program should enable us to capture exciting and new business opportunities and reduce any concentration risk from a single product or a single therapy and deliver a broad-based sustainable growth in the long run. As a result, we retain our aspirational target of a billion sales and which will be partially supported by several approvals anticipated.

Moving on to our financial results for the quarter:

We achieved Rs.1539 crores in revenues, showcasing a very healthy growth of 20% year-on-year. Sequentially, we have substantially improved on our non-ARV revenue numbers. Formulation reported a revenue of Rs.349 crores for the quarter, a decline of 33% year-on-year.

Coming to LMIC business: While broader demand environment on ARV was softer the pricing as largely remained depressed in Q1 which is at already record low level. We are taking a calibrated biding approach to ensure better outcomes in the tenders for this business. Having said that we are very confident of sustaining our leadership position in ARV first-line treatment both APIs and formulation. During Q1, we launched lopi-rito combination in US. Additionally, we are awaiting few more approvals in the US which will drive our growth in the coming quarters and years.

As you are aware Laurus is a fully integrated player in ARV formulations and we believe we have the fair ability to whether pricing challenges and we are able to maintain our margins in the current quarter supported by performance in our divisions. Coming to the developed market our performances was stable as increase in the generic volumes more than offset by pricing pressure. We continue to leverage our front-end operations in US market for new product launches.

During the quarter, we filed one additional ANDA and received two approvals both tentative. We expect US filing pace to pick up during this financial year. Cumulatively, we have filed 30 ANDA to date, of which we have a total 11 final approvals and 14 tentative approvals so far. In Canada, we continue to have 11 product approvals of which we have launched 5 products and planning to launch more products in the next couple of quarters.

For European markets, we validated two products as part of the CMO opportunity. We expect a significant upside in this financial year from these products and we have a basket of 9 approved products, of which we have launched three on our own label and we will be launching two more products shortly.

Based on our healthy product pipeline progress, we continue to invest in non-ARV FDF infrastructure. As indicated in our last conference call, We have commissioned our brownfield expansion at unit 2, taking the total FDF capacity to handle 10 billion units now. We expect a more gradual ramp up of capacity utilization in the new block.

On the R&D front, we continue to allocate critical resources to our research initiatives and invest in portfolio with products specific approach based on complexity and scale economies. Additionally, we are implementing steps to bring more robustness in our overall product development processes including focus on bringing digital transformation within the R&D Infrastructure. We are happy to share that we have commissioned our sterile R&D labs and we have started working on a few priority projects. Overall, R&D spending to sales for the quarter was at 3%. We have a total 55 products in R&D pipeline either under review or under development having an addressable market size of over $40 billion.

When it comes to generic APIs, our anti-viral business during the quarter continued to witness sequential improvement and sales grew to Rs.383 crores, while overall demand environment stays softer, we expect volumes and prices are going to stabilize around these levels.

We continue to maintain a leading market share is current product line and also expect to increase, marginally in the developed market supplies of APIs. Onco APIs reported Rs. 63 cores sales during this quarter reflecting a marginal growth of 5% year-on-year. As we are mentioned, we have the largest high potent capabilities in the country and we are adding new capacity and we continue to see good offtake in onco APIs.

Our aim to strengthen global leadership in offering onco APIs not for generic customers but also for the innovator clinical based molecule. APIs other than oncology and ARV sales including diabetes, cardiovascular and asthma showed very good numbers for the quarter at Rs.138 crores growing significantly at almost 80% year-on-year. This was supported by new contract supplies and we believe this segment should return to healthy growth trajectory in FY 2023.

We filed one DMF in non-ARV during the quarter taking the total to 74 DMF files so far. We have also completed the validations of few APIs and we expect to file additional DMFs in the current financial year. Interestingly, we also have a very high order book visibility in the segment and accordingly adding additional manufacturing capacities to capture the opportunities in non-ARV and non-Onco API space.

Synthesis business delivered exceptionally good quarter delivering a robust growth of over 190% year-on-year and 60% quarter-on-quarter to Rs. 577 crores. The growth was supported by solid demand from new and existing customers. We remain quite excited about this division as we focused on both commercial execution as well as pipeline expansion and execution.

We continue to work with several and diversified customer base including several big pharma. Our Greenfield investment to set up a dedicated R&D center for synthesis division at Genome Valley, Hyderabad and three manufacturing units at Vizag under Laurus Synthesis Private Limited is progressing as per our expectations as we communicated to all our stakeholders. New sites for synthesis division will have capabilities to handle steroids, hormones, high potent molecules apart from other large volume products in animal health.

Laurus Bio revenues were largely stable at Rs.30 crores on quarter-on-quarter but we do anticipate pickup with the ramp up of new capacities, debottlenecking of R2 for our large scale CDMO partner.

We do believe alternate food industries likely to grow meaningfully over the coming decades and scale, cost and functionality will remain the core drivers for differentiation for the players. Schedule expansion at R1 including a new R&D block and installing downstream balancing equipment to enhance capacity at R2 is on track. This expansion will be completed before the Q2. We have zeroed in land parcels for another greenfield site for our large-scale fermentation capabilities and we are in the drawing board stage right now. We will invest to create capacities around may be 600 thousand liters to a million liters capacity in new site.

With that I would like to hand it over to Mr. Ravi to share some financial highlights.

V.V. Ravi Kumar: Thank you doctor and a very warm welcome to everyone on our first quarter FY 2023 Earnings Call.

Total income from operation for the quarter is Rs.1539 crores against Rs.1279 crores with a healthy growth of 20%. Gross margin for the quarter is at 57.6% almost improved like 90 bps on a better product mix.

Our EBITDA for the quarter 1 is at Rs.454 crores with a margin of 29.5% which is close to the full year guidance what we have provided. Our diluted EPS for the quarter is 4.6 not an annualize which grew over 4% over the corresponding quarter. Our ROCE improved to 29.4% on annualized basis based on the better product mix.

On the CAPEX front, we invested close to Rs.209 crores for the quarter and as we guided, we are expected to invest around Rs.2000 crores in the two years' time between FY 2023 and FY 2024. For any further details you may refer to IR presentation in this regard. We remained on course to strengthen our position as a cost effective integrated pharma player. We are investing in backward integration programs in creating more capacity in the non-ARV infrastructure.

On the tax rate, our effective tax rate was around 29% based on this year onwards, we are losing our exemption to 50% on the SEZ site that is the reason it is at a higher side but however, we are going to evaluate further at the end of the third quarter or beginning of the fourth quarter whether to shift to the new tax regime or not.

With I would request the moderator to open the lines for Q&A.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Sudarshan Padmanabhan from JM Financial. Please go ahead.

Sudarshan Padmanabhan: My question is on the synthesis business, I mean if I look at the run rate, honestly you have done a phenomenal job from where we were from two years ago to your run rate of almost Rs.600 crores. In the annual report we talked about two contracts, one is multi CDMO contracts with niche APIs and the other is global major Life Sciences. I would like to understand whether this run rate is sustainable going forward. I am not necessarily looking at quarter-to-quarter but directionally and is there any kind of to one-off supplies there we have booked to any of the contracts which might not recur probably going forward.

Dr. Satyanarayana Chava: I will answer this question in two parts you are mentioning on two contracts two pieces of information one is multi-year, multi product contracts signed with Global Life Science

Company. We are building a dedicated capacity to cater to the products and demands as per the contract right now we are developing products which will go into that manufacturing site and one NCE validation is going on the current site. So, the revenue coming from that contract is not that significant right now but it will become significant once we qualify the plant which will happen may be second half of next financial year that is question about part I of your question. The part two which we indicated, we got a major contract from another life science company and the supplies are ongoing. So, with that there is no one-off in Q1

Sudarshan Padmanabhan: And this will continue probably for the next year, I mean this is a longer-term contract it is not necessarily a short-term contract.

Dr. Satyanarayana Chava: These clinical programs commercial see it is difficult to predict, I think only as I mentioned in our last call numbers only will tell how we are doing.

Sudarshan Padmanabhan: The run rates will continue more or less directionally we should continue to do well on the CDMO is that right assumption sir?

Dr. Satyanarayana Chava: We will do very well in the CDMO part that is for sure, so lot of opportunity is ahead of us as Mr. Ravi mentioned, we are creating a three new greenfield sites for CDMO division that indicates how much of opportunities are in front of us.

Sudarshan Padmanabhan: Thanks a lot, and sir last question from my side is on the formulation side, we have the new capacity coming in, but on a quarter-on-quarter, we have seen a dip, somehow run rate that we usually do. Do you see the run rate kind of moving ahead and now when do we start optimally utilize the capacity, sir? Some color on how we look at it directional.

Dr. Satyanarayana Chava: You are asking formulations? Formulation capacity is fully qualified right now but it will be fully utilized by end of this calendar year.

Sudarshan Padmanabhan: Thanks a lot, sir. I will stand back in the queue.

Moderator: Thank you. Next question is from the line Krish Mehta from Enam Holdings. Please go ahead.

Krish Mehta: Thank you for taking my question and congratulations for good set of numbers the only question I have on the total break up of ARV versus non-ARV sales for this quarter?

Dr. Satyanarayana Chava: The ARV APIs is at 25% of our sales. If you recollect ARV APIs once upon a time in 4-5 years that used to constitute 80% of our sales. Now it is 25% of our sales and 17% sales came from ARV formulations. If you sum it up about 42% of sale came from ARV either APIs or formulations, put together.

Moderator: Thank you. Next question is Ameya Chalke from Haitong Securities. Please go ahead.

Ameya Chalke: Thank you for taking my question and congratulation for the management for the good set of numbers. Sir I have one question on the margin side. So, despite sizable increase into synthesis business our margin improvement sequentially has been minimal. So, is it fair to assume that the synthesis margins are not very far from the company level margins and if it is so, do not you think it is on the lower side, if you can clarify on that along with that also if you can explain the higher other expenses for this quarter compared to the Q4 of last year?

Dr. Satyanarayana Chava: There was price pressure on ARVs both APIs and formulations, that reduction in the margins in ARVs was offset by higher margin CDMO business. The CDMO business, the numbers are on par with any other CDMO focus player, that is one. Second, when it comes to the other businesses you are talking about EBITDA. EBITDA numbers for the entire company, we are not disclosing the division wise expenses. So, the other operating expenses, I will ask Mr. Ravi to clarify.

V.V. Ravi Kumar: The expenses side there is a power shortage in our manufacturing area in Andhra Pradesh. In the last quarter, we have sourced lot of power from the private sources and also, we used the diesel. We spent about Rs.33 crores additional expenditure towards power and some part of a foreign exchange loss also there. You are aware, the foreign exchange loss on account of not incurred loss, it is a restated loss. So, that is also reflected in the other expenses.

Ameya Chalke: Sure. So, going ahead, you expect these other expenses to normalize at least in the near term?

V.V. Ravi Kumar: We expect so, the power and fuel getting normalized already.

Ameya Chalke: If the GM remain at the similar level because of business mix do not you think the EBITDA margin has hope to improve going ahead.

V.V. Ravi Kumar: Our overall for the year, we gave an EBITDA margin guidance of around 30% that we are still retaining.

Ameya Chalke: Sure, and just question I have on the formulation sales drop on the TLE side how do you see the tenders going ahead and if the demands have gone down or the pricing has down substantially that is why the market size has shrunk. If you can elaborate on this

Dr. Satyanarayana Chava: The volume front there is no degrowth. Volume uptake remain robust for all players put together. In the last quarter, most of the tenders, except South Africa, winner takes all tenders. So, winners restricted to few players rather than spread across several players that is the case with global fund and PEPFAR where the volume split is evenly across all the players. So, we do expect the supplies to global fund and PEPFAR will start from Q2. So, we do hope the formulation sales in ARV segments will pickup from the next quarter.

Moderator: Thank you. Next question is from line Nikhil Mathur from HDFC Mutual Fund. Please go ahead.

Nikhil Mathur: I hope I am audible perfectly. Sir 2 or 3 questions I have, the first question is the CAPEX for the FY 2023 and FY 2024. You have guided towards the pros and cons of CAPEX can you help me with CAPEX which will be dedicated for the custom synthesis business mix Rs.2000 crores.

Dr. Satyanarayana Chava: The CAPEX number what guided by Ravi little while ago is Rs.2000 crores for FY 2023 and FY 2024. I would say 40-50% of the CAPEX is the CDMO space. If R&D or manufacturing put together it is about that number and nothing is going into ARV APIs or formulations. So, most of the remaining CAPEX say which is around another Rs1000 crores is going into non-ARV APIs and non-ARV formulations or backward integrations.

Nikhil Mathur: So, basically, what is gross today for the custom synthesis and if we add another Rs.1000 crores. So, what is the gross profit we are looking at for custom synthesis two years down the line.

Dr. Satyanarayana Chava: Currently except for one small facility we do not have a dedicated manufacturing facilities for custom synthesis. So, today our facilities are common for both generic and custom synthesis to remove that complexity and fight for capacity. We are creating dedicated capacities for a CDMO space. So, we cannot segregate right now. How much is used for CDMO or how much is used for generic we know, but there is no dedicated capacity for CDMO or generic both utilize the same capacity.

Nikhil Mathur: Sure sir, no problem. Sir, second question, as one of the participant's had already asked the question, I might just want to ask this question in a different way. In FY 2021, when sales rebound happened for the company in a big way. The company was not fully sure whether that particular sales momentum or the growth momentum will continue in FY 2022 or not and then in FY 2022 we saw destocking at various levels and in multiple business areas. Now whatever the sales that is happening FY 2023, a billion-dollar guidance that you are talking on multiple forums. What can be the externals led for several shocks to that number FY 2024 and FY 2025, I think it is very well understood, given that you are sounding so confident on this billion-dollar guidance. It should get realized in FY 2023, but as investors we are not fully sure of what kind of shocks can happen in the system whether in the company or outside. So, if you can get some more comfort whether this billion-dollar number sustain in FY 2024 and FY 2025 or not, that would be very helpful.

Dr. Satyanarayana Chava: See what the CAPEX we have announced FY 2023 and FY 2024. So, these capacities should give additional revenues in FY 2024 and FY 2025. So, by your question is while achieving our target of a billion will be growth in FY 2024 and how much will be growth in FY 2025. So, we can say our history also reveals. So, we grow significantly in one year, grow marginally in one year. So, it is not that we can grow as put a straight line is not possible. So, we have very exciting opportunities in front of us that is the reason we are doing CAPEX and now CAPEX is not being done in anticipation of something. So, at least we are moved away from creating capacities head of our requirement is gone, we are creating capacities to capture what opportunities we have in front of us. So, FY 2025 is going to be very good year, in our previous call also we have mentioned and FY 2024 we are not giving guidance but we will give guidance and appropriate stage what could be the growth opportunities FY 2024.

Nikhil Mathur: Sure, sir and one final question again of the custom synthesis side, we are broadly aware of the capability that Laurus brings in this particular segment specially on the high volumes manufacturing front but on the last 3-4 quarters the quarterly run rate on the sales of the segment continues to move up. Sir do you mind highlighting some 2-3 implementable capabilities that is now helping Laurus to continue to grow in this particular business, may be one or two case studies that you might want to share from your broad portfolio product in this business.

Dr. Satyanarayana Chava: This is very interesting question we have added significant capabilities apart from significant reactor volume. So, the company is in a position to do hydrogenations at very scale low cryogenic reactions at scale, Biocatalysis at scale, continuous flow reactions at scale. So, company added significant capabilities that is the reason we are able to attract retain new customers and insource several products at late-stage clinical phase are commercial because of our new enhanced capabilities in the company.

Nikhil Mathur: And if I may just squeeze one final one, for Laurus Bio can you share some outlook from where 2-3 year perspective what kind of ramp up we should expect from this kind of business?

Dr. Satyanarayana Chava: Laurus Bio where we did Rs.30 crore sale in this quarter and Q2 will similar. Q3-Q4, we expect debottlenecking of downstream processing will be over so some increase in revenue will come but FY 2024 is going to be a flat year for Bio because our capacities are full utilized by end of this year that is the reason, we are investing significantly or we are planning to invest significantly in the division and those capacities will come for commercial use in FY 2025. So, FY 2025 is a big leap for Bio but not FY 2024.

Moderator: Thank you. Next question is from the line of Binu from InCred Capital. Please go ahead.

Binu Pathiparambil: Congrats for a great set of numbers. Dr. Chava your guidance of billion-dollar for the year implies 50%-60% plus kind of growth for the year and in the first quarter, you have done 20% so which means for the next three quarters, you are looking at may be 70% odd kind of growth in revenues year-on-year, still that in full confidence or it is more aspirational, how confident are you about meeting yourself that?

Dr. Satyanarayana Chava: When we announced our goal, aspiration to become a billion dollar. The dollar was at Rs.70-Rs.73. So, we are very confident to achieve that number now. So, at that number, I think we have every arms and ammunitions available to reach there.

Binu Pathiparambil: Sounds great. Just to understand is there any one risk that you do not need to say what it is but if there that one risk in your mind which could impact achieving this may be some product developing some problem, or one client moving away from you. Is there one or two such key risk which can impact us or is it a well distributed business target?

Dr. Satyanarayana Chava: We have capacities, we have customers, we have visibility of orders and except one product approval in formulation all are in place, if we are scouting for customer, we are scouting for a capacity or a facility approval and all, it is a long goal. So, we are not at that, we are very close to our goal. We have all the actions required or abilities required to reach that number.

Binu Pathiparambil: Great. Thank you and best wishes.

Moderator: Thank you. Next question is from the line of Tushar Manudhane from Motilal Oswal. Please go ahead.

Tushar Manudhane: Thanks for the opportunity. Based on this brownfield capacity which has now come up in July so what could be the incremental operation cost associated with this which will come in the subsequent quarter.

Dr. Satyanarayana Chava: Our formulations expansion capacity is fully manned. So, those expenditures are already built-in in Q1 itself. So, we are going to recruit marginally more people in new block but those costs are already built-in in Q1 if there is a slight increase. It will be built in Q2. You are aware all these preoperative expenditures are expensed not capitalized in the company. So, all those are built-in in our numbers.

Tushar Manudhane: Interesting and just on other API segment where we have seen good traction over past few quarters. So, how do you see this in terms of the new products and the market share gaining the existing product the prospective here is that there has been good amount of inventory made disruption in API in industry per se may be on account COVID and or may be the China related lockdown. So, how do you see the prospects of non-ARV APIs?

Dr. Satyanarayana Chava: Non-ARV APIs will continue to grow and increase in our inventory is a conscious decision we took to weather the supplies and challenges. So, in one way, our increase in inventory helped us to sustain our growth. So, if we are very prudent in our inventory, we might have challenges also. So, higher inventory helped us to sustain the supplies to our partners during the challenging times.

Moderator: Thank you. Next question is from the line of Rithesh Rathod from Nippon India Mutual Fund. Please go ahead.

Rithesh Rathod: Can you quantify in terms of ARV pricing pressure which you mentioned significantly, how much it would be down on a year-on-year basis?

Dr. Satyanarayana Chava: It is both ARV APIs and formulation if you take together as I mentioned it is about Rs.550 crores. The margin impact was almost 15%. Average 15% both put together.

Rithesh Rathod: And in case of custom synthesis, you spoke about two contracts and the second one where you are ramping up. So, I presume, you would have ramped up in Q1 as well as in Q4 let to some extent. How sustainable that business would be after a year or so once it reached to steady state. You see any sort of risk over there after a year or so?

Dr. Satyanarayana Chava: These products are on the late stage or just launched. So, they have a very long patent life. So, these are not like generic molecules today company A will get market share, tomorrow company B get market share. Then we are not with A and B then we have no orders but with NCEs these innovators will have long rope I do not think these will vanish in a year. These are pretty long term in nature.

Rithest Rathod: This you are talking about the commercialized product, right?

Dr. Satyanarayana Chava: Yes.

Rithest Rathod: Ok and any kind of pricing pressure comes in this product on an annual basis or productivity benefits which needs to be passed on.

Dr. Satyanarayana Chava: We have not seen significant price pressure in this division unless we agree. See these contracts are long-term so do agree what kind improvements we make and pass it on to the partner but other than that this segment pricing is predictable and stable.

Rithesh Rathod: And excluding the two contracts which you spoke about excluding that custom synthesis business you will grow on that base. If you exclude those two contracts even over there you are confident of things ramping up?

Dr. Satyanarayana Chava: We do expect to grow.

Rithesh Rathod: Yes. And one final question on CAPEX. You have maintained your CAPEX guidance or even that has gone up or what is the number as of now because you mentioned about the rupee side and rupee being fluctuating on your revenue guidance. Just to reconfirm your CAPEX guidance.

Dr. Satyanarayana Chava: We indicated to around Rs.2000 crores CAPEX for FY 2023 and FY 2024. And in the Q1, we did spent around Rs. 208 crores CAPEX.

Moderator: Thank you. Next question is from the line of Nitin Agarwal from DAM Capital. Please go ahead.

Nitin Agarwal: Thanks for taking my question. Sir on the CDMO business how many commercial products are we supplying right now?

Dr. Satyanarayana Chava: We have 7 commercial products, 4 intermediates and 3 APIs.

Nitin Agarwal: And sir, how many late-stage products would we have that can be commercialized over the next 2-3 years.

Dr. Satyanarayana Chava: We do not want to give you a number but there are very good number candidates in the late stage because of those only we are expanding our capacities and capabilities in that division.

Nitin Agarwal: I was just curious rest of the seven that we have, do we see this number going 2x, 3x over the 3-5 years, 3 years rather.

Dr. Satyanarayana Chava: We do not want to comment on that.

Nitin Agarwal: Fair enough sir. Can you help us also with the split which is there between contract research and contract manufacturing in the CDMO business? The early-stage contract research that you do?

Dr. Satyanarayana Chava: We do not do any preclinical work so we do not do any MedChem work. So, most of our revenue coming from manufacturing only, so nothing is coming from research. We do not have any FTE programs.

Nitin Agarwal: Right and in terms of is there a work that you are doing with the innovator during clinical trial phase. May be doing pilot quantities and all in phase 2-3.

Dr. Satyanarayana Chava: Yes. Going back to your question. We do have a lot of programs coming from phase 1, phase 2. But phase 1 revenues are not that big to mention.

Nitin Agarwal: Right and sir, secondly on the formulation business sir how do we see the ex-ARV business in the formulations over the next couple of years. What should be the drivers for this business.

Dr. Satyanarayana Chava: Lot of filings done, lot of approvals anticipated and the growth in formulations will come from non-ARV now onwards.

Nitin Agarwal: Okay. Sir you mentioned a specific product around in Europe that will be a big driver, by when will that product start to kick in for this.

Dr. Satyanarayana Chava: Partly, this quarter but majority will come from next quarter onwards.

Nitin Agarwal: Okay and lastly on the CAPEX, you talked about a Rs.1000 odd crores on the non CDMO part of the business roughly, can you just help us understand what the areas where the areas where investing these, primary areas investment for on the ex-ARV size for the CDMO for the CAPEX.

Dr. Satyanarayana Chava: In the non-CDMO CAPEX. Two-thirds is going into APIs and one-third may go into formulation further.

Nitin Agarwal: And sir, formulation we adding more capacity beyond the brownfield that you have done which we commissioned this quarter.

Dr. Satyanarayana Chava: Not this financial year but next financial year may be yes.

Moderator: Thank you. The next question is from the line of Siddhartha Bhothika from Investment Trust of India. Please go ahead.

Siddhartha Bhothika: Sir, had couple of questions. one on the ARV tender side. Sir, three years ago, we received a large multi-year contract for the LMIC market. Just wanted to understand when will this would due for renewal. Is this done at a new round of tender for this.

Dr. Satyanarayana Chava: The South African tender was announced, we do not have any formulation sale there. So, API sales will go to South African contract and the Global Fund and other tenders will be announced soon for 2023 onwards. So, for 2023 allocations were already made and supplies will start from next quarter.

Siddhartha Bhothika: Okay and sir my second question is on the large CDMO product. Is it fair to say that if you exclude from this quarter then the synthesis business have led to single digit growth on a year-on-year basis?

Dr. Satyanarayana Chava: Large multi-year, multi-product contract has not given any significant revenues in Q1.

Siddhartha Bhothika: No, I am talking about commercialized large contract that we have been supplying since March.

Dr. Satyanarayana Chava: No still there is growth. This is not a one-month contract. So, if there is a quantum still, we need to execute fully.

Siddhartha Bhothika: So, meaning the follow up to this is that, is this contract a multi-year contract or is a renegotiable renewable single year kind sort of a contract.

Dr. Satyanarayana Chava: I think too early to comment on that.

Siddhartha Bhothika: And are the margins for this product will be similar to overall synthesis business.

Dr. Satyanarayana Chava: Yes.

Moderator: Thank you. The next question is from the line of Dhruv Bhatia from Bank of India. Please go ahead.

Dhruv Bhatia: Sir, my question is on the CDMO space, this quarter you have done about Rs. 577 crores of revenue. Is it fair to say that for full the year, this is a peak, capacity utilization you are running at, so on a full year, you could probably do Rs.2000 plus crores revenue from the segment?

Dr. Satyanarayana Chava: We want to reserve answering this question, right now.

Dhruv Bhatia: But you have the capacity to do further than this with current capacity available.

Dr. Satyanarayana Chava: Well capacity available yes.

Dhruv Bhatia: And the Rs. 1000 crores incremental CAPEX that you are planned for CDMO, what type of asset turns can we build in going forward?

Dr. Satyanarayana Chava: You could take our current average is asset 1.4-1.5, between 1 and 1.5 depending on how effectively utilize that CAPEX.

Dhruv Bhatia: And the capacity that you have put up is obviously for as you mentioned, the muti-year, multi-product contracts but over and

Moderator: Sir, the lines of the participant dropped. We move on to the next participant. The next question is from line of Manoj from Carnelian Asset Advisors Pvt Ltd. Please go ahead.

Manoj: Hi, this is Manoj from Carnelian. First of all, congratulations for good set of numbers. I have couple of questions, first one is on CDMO side, so just wanted to understand little bit more on CDMO. Since you mentioned that you have built some new capabilities to build this business so just wanted to understand two things, sir. A. what is our right to win here and secondly how do you pan down the opportunity size in the segments where you are working.

Dr. Satyanarayana Chava: Right to win, these opportunities is based on reputation regulatory track record, flexibility in offering volumes that is the right to win and the second question I could not get very clearly.

Manoj: Sir, if you can pen down the opportunity size in terms of the segments or therapies or in terms of the molecules where we are working, where we are putting the CAPEX. So, if you can, let us know the opportunity size overall for these segments where you are putting CAPEX.

Dr. Satyanarayana Chava: In the CDMO, we have little or no scope to choose what we should get so it all depends on what partner want us to make. See we are not making steroids, we are not making cephalosporin, penicillin other than that we are offering wide spectrum of things starting from steroids, hormones, high potent, prostaglandin, large volumes, small volumes. So, our offering is very extensive except cephalosporin and penicillin.

Manoj: Okay and whether this capacity which you are building are fungible, you are building up a particular capacity like you also mentioned in your PPT that you are putting a CAPEX on a multi-year contracts and molecule does not get the anticipated growth. So, whatever CAPEX, you are putting either it has to be protected by way of take or pay or is it fungible. So, if you can elaborate on this a bit, sir?

Dr. Satyanarayana Chava: One of the facility, we are building is for a specific therapy area, Animal Health. So, it is fungible within the animal health but not through human health can put there. So, that kind of fungibility is there and other than that other products are either advance intermediates or APIs. There are some equipment technology specific, which is not fungible but majority of the reactors are fungible. In the CDMO space, except few occasions, our partner do not use those vessels 365 days in a year. So, some kind of flexibility has to be there.

Manoj: Okay got it and one last question that I have mainly on Laurus Bio, you mentioned that you are evaluating a plan to create close to one million liters fermentation capacity in phase 1. If that goes through what kind of CAPEX we can think for building this kind of capacity and any color on timeline for this in terms of CAPEX as well as ramp up.

Dr. Satyanarayana Chava: We will get back to you on how much CAPEX we are going to spend may be in the next quarter or so. We are finalizing our numbers but we do expect this facility will up and running sometimes during FY 2025.

Manoj: FY 2025. Do you see enough opportunity size in this space right?

Dr. Satyanarayana Chava: There are opportunities, see the challenge right now is we do not have capacity to offer. So, that is reason we want to do this on a fast track more and we will get back to with the exact time length and also on how much we are going to spend on that.

Manoj: But sir on fermentation, I think world is overdependent on China and still I think India is not there. So, building this kind of capacity. So, if you can give us color in terms of the kind of capability or the kind of whether we will require some kind of pre-existing contracts or whether we will first build the capacity and then we will have to wait for the contract. So, some color on that may be this quarter or next quarter, I think that will be helpful for us.

Dr. Satyanarayana Chava: Sure, this capacity is being built for synthetic biology, alternate foods, recombinant food proteins. So, we are competing with conventional fermentation of steroids, or vitamins or any other large molecules. So, this is specifically for precision synthetic biology.

Moderator: Thank you. Next question is from the line of Bharath from Quest for Value Capitals. Please go ahead.

Bharath: My question is to Dr. Chava. Sir, you said that you want to see CDMO to be 25% of the sales in FY 2025 and if you see our numbers now, already in last quarter CDMO is 25% of the revenue and this quarter is already 37% of the revenue. So, I would like to know where do you see CDMO in percentage of sale in FY 2025?

Dr. Satyanarayana Chava: A very good observation, may have to revise our target to one-third by FY 2025. Yes, from 25 to one-third by FY 2025 may be.

Bharath: Yes, currently I can see in the PPT that is 25% by FY 2025 but already you are 37% so I think 33% is good number you gave.

Dr. Satyanarayana Chava: Yes.

Bharath: Yes, and my next question is that total capacity of Unit 2 is 15 billion.

Dr. Satyanarayana Chava: 10 billion right now.

Bharath: Yes, right now 10 billion is commissioned but the total capacity can be estimated to 15 billion, we can also do a brownfield extension of 5 billion more, right?

Dr. Satyanarayana Chava: Yes, you are right. The physical infrastructure was created to expand capacity by 10 billion but 5 billion capacity was installed and qualified. There is a room to expand by another 5 billion that may happen next year. FY 2024 depending on how we are doing in Europe and US.

Bharath: So, you mean to say once this 10 billion is completely utilized then you will do Brownfield capacity of 5 billion.

Dr. Satyanarayana Chava: Yes.

Bharath: Thank you and one more question is that in PPT you mentioned that you are taking calibrated tendering approach to ensure better profitability for this ARV formulations. So, do not you think that you would lose market share because of this calibrated tendering approach.

Dr. Satyanarayana Chava: See what we meant by calibrated approach is we do not want to participate aggressively in tender where winner takes all. So, there, people are very aggressive on pricing so do not want to participate in those tenders but still participate in tenders where the award is split among several people. But generally, it might get calibrated.

Bharath: Okay. But generally, I may be wrong but I think ARV tenders is not like winners takes all, right? It will be like 30% to the first guy and 30% to the second guy and 30% to the third guy, will be distributed, right? It is not like winner takes it all, I guess or I am wrong.

Dr. Satyanarayana Chava: There were some tenders may be, I will put up to 10% of the market is winner takes all kind of situation.

Bharath: Okay. Thank you and my question is like in the last con call you said, not last conference call, I think two quarters back, you said that you are planning to use this unit 4 capacity as interim to service this multi-year contract with animal health company till the dedicated plant is ready. May I know, like by when you will be able to do commercial supply from this interim capacity for this animal health company?

Dr. Satyanarayana Chava: Commercial supplies will start end of FY 2024.

Bharath: That is from the new capacity, new plant, right?

Dr. Satyanarayana Chava: Yes, once the new capacity comes up, I think we do not want to utilize the capacity in unit 4 for those products.

Bharath: Okay. So, you are not planning to commercialize in unit 4, you are planning to commercialize only in the new plant.

Dr. Satyanarayana Chava: You are right.

Moderator: Thank you. Next question is from the line of Pratik Kothari from Unique AMC. Please go ahead.

Pratik Kothari: Good morning and thank you for the opportunity. There are a couple of questions regarding ARV. Sir in the last con call, we did mention that our API and formulation prices were down 10% and you said this quarter it is down about 15% from price so there has been further deterioration of 5% odd.

Dr. Satyanarayana Chava: Yes, and we do believe that is the new base we do not expect further significant price drops.

Pratik Kothari: Fair enough and we also did say that going forward in the coming few quarters. We used to Rs.550-600 crores ARV APIs a quarter. We are at about 350 odd now or rather 400 odd now. This should go back but at the same margins that we used to see may be two years.

Dr. Satyanarayana Chava: ARVs both APIs and formulation put together. I think topline will grow but at a lesser gross margin what we enjoyed in the previous years.

Pratik Kothari: Ok fair enough. Sir two years back when we used do Rs.550-600 crores of ARV APIs did started a second line.

Dr. Satyanarayana Chava: No, we never did 600 crores. So, the peak, we did was Rs.1900 crores per year ARV API but broadly you can say Rs.1500-1600 crores APIs and another same number in the formulation. So, our new yearly base for ARVs will hover around Rs. 3000 crores, take early couple of hundreds on the positive side. so that will be new norm, so we do not expect that as the situation is evolving and we are trying to accommodate to the changed environment. We are growing in volumes but the price drops are pushing us downwards in our growth. So, around Rs.3000 crores is the new base for ARVs put together. I think we are very confident to retain that number and that number will also help us to retain our leadership position in both especially in APIs.

Pratik Kothari: Fair enough. Sir in your opinion what is causing this price because at one time we also saw that our solvent prices or input prices were going up and we were intending to pass that. Has new players come in, or has had market share seen in certain ways, if you can throw some light?

Dr. Satyanarayana Chava: It is a difficult one to answer no new player came under the market yet and it is not a growing for 10 people to jump in. It is declining market and incumbents are very strong. If the incumbents are weak then there is a scope for a new player but incumbents are very strong and market is stabilized, it is not growing. So, it is a natural phenomenon in the business. So, the era of high margins in this business has gone and it has become a cash cow. So, it is very important segment for us at 3000 crores and it is important business for us and we committed to that business and we do whatever course correction as needed to maintain our leadership position.

Moderator: Thank you. Next question is from the line of Jeevan from Sahasrar Capital. Please go ahead.

Jeevan Patwa: Congratulations sir, just few questions, first is last year, when we talked, we were having world leadership in 8 molecules and we aspiring to go for 15 molecules. So, where do we stand now.

Dr. Satyanarayana Chava: Couple of oncology, we increased our market share so that target is on Jeevan, on that. So, we are continuing to add portfolio where we have leadership position or ability to get to leadership position that goal is on track and in next two years may that number what you said will definitely more than 10.

Jeevan Patwa: Okay, perfect and on the CDMO side basically we were into human health, now we are getting into animal health, I think we are also getting into plant. I think looking at your CDMO it looks like more of a chemical company than a pharma company. And we have capacities, we have capabilities, we have credibility and we have clients. So, we have all four 'Cs'. So, how do we see the traction coming into CDMO. The kind of enquiry you are getting from the clients. So, are we looking to sign something similar multi-year, multi-product contract deal even in the future?

Dr. Satyanarayana Chava: We are not a chemical company; we are chemistry company. So, there is a lot of difference between that. So, we intend to use our chemistry capabilities and scale to offer value to our partners. So, I think we are adding more capabilities there are I mentioned previously to one question. What is the right to win here? We offer large scale chromatography, biocatalysis, fermentation, hydrogenation, continuous flow chemistry, very low temperature chemistry. So, I think our capabilities are also very enhanced, we can also do spray drying. So, because of those enhance capabilities coupled with our commitment to invest for a project. I think this division looks interesting for us.

Jeevan Patwa: So, are you seeing similar kind of enquiries for a multi-year, multi-product deal. So, large deal I am seeing basically.

Dr. Satyanarayana Chava: We are working on some at an appropriate time we will let you know. Yes, we are working on some.

Jeevan Patwa: Okay perfect and last question is on the Bio side actually, so last time when we spoke, you said that we have enough land acquired for 3–4-million-liter capacity.

Dr. Satyanarayana Chava: We did not acquire; we have chosen land parcel and now we have zeroed in where to build. So, we will close that land in this quarter and then start putting bricks as quickly as possible.

Jeevan Patwa: Yes, perfect and one more sir on the multi-year contract that we have for the CDMO. So, is it for intermediates or also for APIs and formulation?

Dr. Satyanarayana Chava: We cannot answer that, yes.

Jeevan Patwa: Okay perfect. Thanks a lot.

Moderator: Thank you. Next question is from the line of Nushad from Aditya Birla AMC. Please go ahead.

Nushad Chaudharu: Thanks for the opportunity, few clarifications. Firstly, on the CAPEX pipeline of Rs. 2000-2500 crores you mentioned 50% would go to CDMO business and you have shared an asset turnover of 1.5x. can you give us the asset turnover of the CDMO business, what one should expect?

Dr. Satyanarayana Chava: I think when I mentioned around 1.5, our CFO also corrected that. So, you can take between 1 and 1.5 asset turnover ratio when it is fully utilized. The gestation between our first two investment starts to getting to the peak commercial sale. We will take between 3-4 years. We invest and we go to the peak it does not happen. So, the day we complete our CAPEX. We need may be another 2 years to fully utilize that capacity.

Nushad Chaudharu: That I understand, so in both the businesses, we should expect on a full utilization it should give 1.5x.

Dr. Satyanarayana Chava: Between 1 and 1.5, you are free to choose either 1 or 1.5.

Nushad Chaudharu: Okay and how are we planning to fund this CAPEX sir, would it largely through internal accrual or any portion on debt we are planning.

Dr. Satyanarayana Chava: I will ask our CFO to answer that.

V.V. Ravi Kumar: Most internal accruals.

Nushad Chaudharu: Okay by any chance do you share your CDMO margins if do not quantify it qualitatively and you indicate would it be significantly higher than our API and formulation business or a marginally higher.

V.V. Ravi Kumar: We have been disclosing that on gross margin side CDMO is the highest followed by formulation, followed by API that is what disclosure we gave and it is still valid.

Nushad Chaudharu: And at the EBITDA level. The difference remains same or it becomes narrow.

V.V. Ravi Kumar: We cannot calculate the EBITDA level. So, it is not possible to calculate EBITDA level.

Nushad Chaudharu: And lastly in a CDMO business typically when we go for new client acquisition what is our value preposition to the client. Is it cost, the capabilities, what exactly we picture the differentiation to get the client?

Dr. Satyanarayana Chava: I think it is speed and flexibility.

Nushad Chaudharu: Perfect and thank you so much and sir all the best.

Moderator: Thank you. I now hand the conference over to Dr. Satya for closing comments.

Dr. Satyanarayana Chava: Thank you participants for your very intrigue questions and we continue to update you any further information in the next calls. Thanks, Monish for organizing this. Thank you everyone.

V.V. Ravi Kumar: Thank you everyone.

Moderator: Thank you very much. On behalf of Antique Stock Broking Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.