"Cipla Q3 FY17 Earnings Conference Call"

February 8, 2017

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Moderator: Ladies and Gentlemen, Good Day and Welcome to the Cipla Q3 FY17 Earnings Conference Call hosted by Kotak Securities Limited. 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 telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Chirag Talati from Kotak Securities. Thank you and over to you, Sir.

Chirag Talati: Hi, good evening, everyone. This is Chirag here, from Kotak Institutional Equities. I thank the Cipla Management Team for giving us the opportunity to host this call. From Cipla, we have with us today, Mr. Umang Vohra – MD & Global CEO, Mr. Kedar Upadhye – Global Chief Financial Officer and Mr. Alpesh Dalal – Head of Investor Relations at Cipla. I now hand over the call to Cipla Management Team for their opening remarks. Over to you, sir.

Alpesh Dalal: Good evening, everybody. This is Alpesh here and welcome to Cipla's Q3 earning call. Just a small disclaimer, that on this call, discussions will include certain forward-looking statements which are predictions, projections or other statements about our future events. These estimates reflect our current expectation of Cipla's future performance. Please note that these estimates involve a number of risks and uncertainties that could cause actual results to differ materially from what is expressed or implied. With that, I would now hand it over to Kedar to take us through the financial performance for the quarter.

Kedar Upadhye: Thank you, Alpesh. Good evening to all of you, and welcome to our Earnings Call for the Third Quarter of Fiscal 2016-17. I hope you have got a chance to go through the investor presentation that we have posted on our website. I will walk you through some of the key financial highlights of our performance this quarter. Our focus on reducing operational complexity and deepening our presence in priority markets which include India, US, South Africa, and key geographies within the emerging market territory has helped us deliver improved performance quarter-on-quarter. I am pleased to announce that our efforts on revenue growth and cost containment have helped us deliver strong base business profitability in Q3 FY 17. The performance trend from the last three quarters reflect our determination towards building an operational efficient and sustainable organization.

Coming to the quarter, overall income from operation stands at Rs. 3,647 crores, growing 16% year-on-year. As you know, the sales and profit spread on a year-on-year basis would not be fully comparable due to significant contribution of the US acquisition from this year Esomeprazole revenues last year. Margin after material cost grew to 64% from 61% same quarter last year. This approximately is 300 basis points increase in margins was driven by cost containment basis and a healthy product mix. Total expenses which include employee cost and other expenses for the quarter stand at Rs. 1668 crores, an increase of 14% year-on-year. Employee cost for this quarter is Rs. 633 crores an increase of 9% year-on-year largely attributable to consolidation impact of the acquisition. Excluding the impact of InvaGen and

Exelan acquisition, employee expenses largely remain flat. The other expenses for this quarter, which includes R&D, regulatory, quality, manufacturing and sales promotion expenses stood at Rs. 1035 crores which declined marginally on a sequential basis. The increase of 17% on a year-on-year basis was largely on the account of acquisition-related expenses and growth-enabling sales and marketing investments for our key markets.

You must have noticed the total R&D investment for this quarter at 6.2% of revenue, the spend for the quarter is below expectation on account of the some of the deferrers as well as efficiency-driven savings in the areas of cost within R&D. We continue to pursue our aggressive plans for US and other key markets. Our efforts on product and geography mix have resulted in improvement in the base business EBITDA which has grown by 21 percentage point post R&D in this year. As a reference, base business for us denotes the performance from our core operating markets without the benefit of acquisitions and excluding investments in new ventures as well as certain non-recurring items. Reported EBITDA for the quarter stands at Rs. 678 crores or 18.6% of revenues despite the impact of demonetization and pricing regulations in India, currency volatility in key markets and similar other headwinds. As we have spoken in the last quarterly call, the depreciation on amortization expenses now includes InvaGen related amortization of intangibles post the business combination accounting have been done under Ind-AS accounting standard. The quarter also includes a one-time charge of Rs. 27 crores towards an idle asset in depreciation line. Tax rate for the quarter was 25%, this increase in tax rate is a result of change in the mix of revenues from various jurisdiction, lower tax exempted income in India and lower weighted reduction on the R&D. The effective tax rate as on YTD December was about 19%. As you are aware, we had acquired a minority stake of about 16.7% in Chase Pharmaceutical in 2014 and made a meaningful contribution in advancing an Alzheimer's drug to an advanced stage of development where the product has now successfully concluded phase-2 studies.

This quarter, we divested our stake to Allergan, which has agreed to pay $125 million upfront plus potential regulatory and commercial milestones. We will realize this amount applicable to us to the extent of our shareholding in the entity. The results for this quarter of Cipla include gain on sale of investments in Chase of Rs. 121 crores, which is disclosed as part of other income. Profit After Tax is Rs. 375 crores and is up 44% versus last year. The PAT percentage for this quarter is 10.3 percentage. Our CAPEX stands at 7% of sales. In the last two years' period, we went through a heavy capital investment cycle and we will see a tapering down in the coming year. During this quarter, we invested about Rs. 246 crores on CAPEX in terms of cash flow. We continued our focus on operational efficiencies, which resulted in the improvement in our cash flow. Operating cash flow for the quarter stood at Rs. 620 crores.

Our long-term debt stands at USD 560 million which was mainly used to fund the US acquisition. We also have working capital loans of about USD 120 million, which act as anatural hedge towards our receivables. Our net debt to equity ratio improved from 0.25 in

September 2016 to 0.21 at the end of this quarter. Outstanding forward contracts as a hedge for receivables as on December 31, 2016, are USD 36 million, ZAR 366million and EURO 5 million. As we build our US franchisee and invest in building a differentiated product portfolio and counter various headwinds, as you would recollect the Board of Directors of the company in December had approved raising funds of up to Rs. 4000 crores by equity and debt instruments. Fundraising is subject to necessary permissions, sanctions, and approvals including shareholders and other statutory approvals as applicable.

I would now like to invite Umang to present the quarterly business operational performance.

Umang Vohra: Thank you, Kedar. Good evening to all of you, good evening, good morning depending on where you are joining from, thank you for being with us on the call today.

I would like to take you through the key events for the quarter. The first is the approval of Seroflo in the UK and our Albuterol filing in the US. These demonstrate Cipla's continued dominance in the respiratory space and our respiratory franchise in regulated market has kicked off. I am confident that we will be successful in building a strong and sustainable franchise in our key markets. We also monetized the first specialty pipeline asset through the divestment of our stake in Chase Pharmaceuticals Corporation to Allergan. Financial details of this transaction were shared earlier in the call by Kedar. As always, I would like to recapitulate some of the key priorities we set for ourselves at the beginning of this financial year and our progress so far. The first was our India business, where we had said that we would beat market growth. This quarter, our India business has grown by 19% despite the impact of demonetization. Adjusted growth for the base effect from last year is 12% and this is ahead of the IPM. We had given an EBITDA guidance of 16-18%. We have been sequentially improving our EBITDA margins with Quarter-3 closing at 18.6%. We are now confident that we will close the financial year within our guidance range. The third item we had mentioned to you was our R&D scale up and our investments in R&D. Along with our regular portfolio products, we are also investing in development of complex and differentiated products providing a right balance between the two and as you will see a YTD R&D percentage is considerably higher than the previous year and the number of filings which I will come to next as the point is also improved.

Our filing trajectory we said we would improve and we have filed almost 21 ANDAs so far. Of these nine were para 4, there is couple of them being first to five. We are on track as per our full year guidance of 20-25 ANDAs that would include a decent portion of limited competition products. As you are aware, we have considered Albuterol, Nanopaclitaxel, Fenofibrate caps and Esomeprazole DR capsule as limited competition opportunities. Our fifth goal was to integrate InvaGen, an acquisition we made and closed last year in February. I am happy to report that we are on track with all our internal targets on this acquisition.

I now come to the quarterly performance. For the quarterly performance of the total revenue of 3647 crores, 40% was contributed by the domestic business and 57% by our international

business. I will now take you through our business performance starting with the India business. Our domestic business recorded healthy growth of 19% year-on-year with most therapies retaining leadership position and growing strongly. When adjusted for the one time distribution policy change impact in the last year, our India business grew by 12% year-on-year. Cipla brand continued to outperform the market with 14 out of 22 Cipla brands from the top 300 IMS brands growing more than the respective market. We are working towards closing certain late stage in-licensing deals and we will continue to explore more opportunities going forward to benefit our therapies inkey brands and our ownership of some therapy segment in the market. Our generic business grew strongly year-on-year driven by focus on the large volume products, channel relationships, and strong on-field execution.

Our North America business has registered a robust growth of 21% compared to last year in dollar terms. This is excluding the impact of one-offs and acquisition. We now market 44 products in the US, out of which 8 products enjoy the Number one position in the market while 23 products feature in the top three position in the market. We are focusing on launching an interesting mix of products between InvaGen and Cipla including some limited competition opportunities in the coming quarters. During this year, we launched a couple of products which exhibit limited competition behavior such as Bupropion XL and Fenofibrate tabs. For this market in line with our full-year guidance of 20 to 25 ANDA filings, we filed nine products during this quarter including Albuterol, our first MDI in the US.

Coming to South Africa, our South Africa business continued to show growth across both private market and tender business with our Quarter-3 sales growing by 13% compared to last year in local currency terms. The quarter was the highest ever in revenue terms. As per IMS MAT, November 16, Cipla achieved a growth of 17.1% in the private market versus 7.5% growth and was the fastest growing company in the top 10 companies. Post the integration of the Actavis portfolio, Cipla became the fourth largest pharma company in South Africa. We continue our leadership position in focus therapies like Respiratory, CNS, Oncology and Musculoskeletal system with over 30% share in each segment. We will continue to aggressively explore in-licensing and partnership opportunities. In the tender market, our focus on high-margin tenders helped improve profitability significantly. As we alluded in our last quarterly call, in Europe we have reached the advanced stages of our business restructuring process and the business is back on the profitability curve. We are also happy as we mentioned earlier to have received approval for Seroflo in the UK and several other markets and are ready for launch in Quarter-4. In emerging market territory, outside of the global access business, our sales de-grew by 6% in dollar terms as we focused on reducing complexity and improving in market performance. You will recall at the beginning of the year, we mentioned that we would rationalize the couple of markets that has resulted in some amount of the de-growth in dollar terms. We continue to evaluate in licensing opportunities and furthering our own portfolio there in this region.

To summarize, the quarters recorded strong profitability in line with our overall guidance. We remain focused on significantly improving our overall margin profile in the future. We

will continue our impetus in strengthening our operation resulting in robust revenue growth and bring efficiencies in our cost structure while continuing our investments in R&D. I would like to thank you for your attention to Cipla and request the moderator to open the session for Q&A.

Moderator: Thank you. Ladies and Gentleman, we will now begin with the question-and-answer session. The first question is from the line of Saion Mukherjee from Nomura. Please go ahead.

Saion Mukherjee: Couple of questions on the US market, firstly, your comments on what you are seeing in the market in terms of pricing pressure, how do you see that going forward, and secondly, some of the limited competition, high-value launches, which were indicated before can come in fourth quarter onwards, how are we placed with respect to that and if you can give some color and what is happening with those files?

Umang Vohra: Happy to answer the second one first, Saion, on the limited competition I would probably say that they are out by about a quarter and slightly more than that and there is because of the new GDUFA etc., the process with the agency is a little slower than what we had thought. Maybe we were a little bit more aggressive in our anticipation of timelines, but I think there have been questions and we are responding to them, so that is out by a quarter and slightly more than that. On the first one, on pricing in the US actually, we are not noticing anything significant and that is probably because the type of products that InvaGen sells are mostly ones where the market is fairly saturated other than possibly the one or two where we believe that we have already seen the price being taken out. Overall, I do not think there is too much pressure, but I would say this that there is pressure in terms of number of people who are arriving on day 1 for any launch, would put that as a bigger deterrent to pricing than anything that we are hearing significantly from our customer.

Saion Mukherjee: On FY18 launches, how many launches should we build in and approximately how many you do consider as limited competition for FY18?

Umang Vohra: We will give more guidance little later at the end of the year, there are a few, but we will give you more guidance at that point in time for next year.

Moderator: Thank you. Next question is from the line of Anubhav Agarwal from Credit Suisse. Please go ahead.

Anubhav Agarwal: Good evening Umang, one question on this capital raise, enabling resolution for capital raising, you mentioned earlier that this was specialty pharma, have you already zeroed down on the therapeutic area you want to get in. If we were talking about capital raising now, you already identified the target or what is the progress here?

Umang Vohra: I think the resolution is enabling, Anubhav, and therefore, it is up to a certain amount which is the amount that we have determined considering that the company would be comfortable from various parameters like debt, equity etc. We have narrowed down on our areas of

specialty and there are in the areas of CNS, non-Psychiatry and it is the area of Respiratory, and the asset that we have monetized was also in the area of CNS, so if we do an acquisition in specialty, it will be in that space. I cannot comment on targets whether we have identified or not, like every other company we evaluate opportunities, but the enabling resolution was taken more just so that we are prepared if there is something that we would like to do.

Anubhav Agarwal: Just comment will be helpful because unlike some of our large peers, we already are in a stage where we are building the US generic pipeline as well, so what was the trade-off when you were deciding that to go for the specialty business, now let us say two years down the line, when you would have more than 100 ANDAs already in the pipeline?

Umang Vohra: It is a little of, I am not sure we want to make the OR decision, Anubhav, and the reason for that is that today Cipla is catching up on generics, two years later we do not want to be catching up on specialty, so I think we are trying to see what we can fund through our P&L and what needs to necessarily go through the balance sheet, that is the call that we are making right now and there will be more color as we go ahead. As of now, there is nothing that we are immediately very close to.

Anubhav Agarwal: I have one more question, now you have been with Cipla for more than a year, have you seen so far any benchmark study being done at Cipla comparing their cost structure overall versus peer, for example, let us say if I just broadly breakdown the cost structure into three parts, one being cost of manufacturing, second is R&D resources that today we are deploying versus output we are getting, so far nine months we are seeing good output but this year has been great but previous year was little tepid, third is total workforce that they have in the organization, any benchmarking you have done, the prime objective of asking this question is that we have been showing cost savings, I am just trying to understand that how much more cost saving can happen?

Umang Vohra: Maybe I will let Kedar answer this because internally we have a cost program running. We will be honest about it, we see opportunities for cost further, but I think what we need to get growth, we need to get growth to drive profitability, costs we will try and take out as much as we can from the system. R&D I can speak to. Our issue really in R&D was that we only really started focusing on the US market with our own filing something to the tune of 16-18 months back, so which is why while we had our teams in R&D, they were really focused on delivering R&D either for our partners or delivering R&D for some of our other markets, so the US focus is started only 16 to 18 months back which is why the filing upstick is happening this year and it will continue in the next year as well. Having said that, just because we file, it does not mean we will get approval. As an organization, we have to learn what the agency tells us through observations on our file etc., so that process is ongoing within Cipla right now. We like to believe that we have relatively well benchmarked based on what we are filing versus the resources that we are deploying there. On manufacturing, I think our cost structure is not bad, it is actually pretty good because Cipla's historical business has been pretty strong partnering or a CMO business as you may call it, but I think

the issue there is the relative value we get from what we manufacture, so if we do not have our own products in the US the equation of percentage etc., they will look really odd until the time you begin to have your own products in the US and then your ratios adjust well, but we have identified cost levers in procurement, we have identified cost levers in people cost, and Kedar can speak to some of these now, but there is a program ongoing on cost as well.

Kedar Upadhye: I agree, we continue to see opportunities, and our current state of profitability is both the function of the cost, opportunity in costs as well as the mix of revenues. In the next few years, we will work on both the levers addressing the mix of revenues in terms of footprint and the cost.

Anubhav Agarwal: Kedar, your comment on total workforce size that you have in organization today, because the reason I am asking is that personnel cost this quarter was flattish ex-InvaGen, and that was a surprise, is that like outside Europe also we have lost some people?

Kedar Upadhye: Europe was one reason. There has been some true-up of retirement-related provisions, which has resulted into some of the credits in this quarter and there is space there as well, but we will have to invest in people capabilities going forward. We would not hazard a guess at this point of time about future cost structure, but we continue to see opportunities. As we said, there is a program which is being run in the company now to address procurement, manufacturing, and various factory and corporate overheads.

Moderator: Thank you. Next question is from the line of Chirag Dagli from HDFC Mutual Fund. Please go ahead.

Chirag Dagli: Sir, can you indicate the number of pending ANDAs that we have at the moment with the agency and if you can split it between what we have with partners and what we have on your own?

Kedar Upadhye: The total number is, including the tentatively approved ANDAs, about 89 as of Dec'16. The tentatively approved ANDA is 24, the final waiting for approval is about 65.

Chirag Dagli: This split you will circle back. Can you also split the depreciation between amortization and actual depreciation?

Kedar Upadhye: We can do that.

Chirag Dagli: Fair point, and you mentioned about CAPEX coming off over the next two years, is there a ballpark number that you can indicate, is it going be in line with now your quarterly depreciation rate, how are you thinking about this and what are the key sort of areas where you think CAPEX is still required?

Kedar Upadhye: I think obviously, the maintenance CAPEX some of the product specific and enhancement in capacity is where still we will have to invest, but last two-three years we were in a heavy

investment cycle as we mentioned because of locations like Sikkim or Baddi or Goa, so part of that might continue into future.

Chirag Dagli: As we go along, what is the kind of bare minimum CAPEX that we should sort of pencil in for something?

Kedar Upadhye: Chirag, unlikely it will go below about maybe some 800 crores, that range between 800 to 1200, which we have been spending for the last three years is what we will have to think about.

Chirag Dagli: You will be in the lesser than 1200 is what you are obviously indicating, but more than 800?

Kedar Upadhye: Yes.

Chirag Dagli: Fair point, and just last point Sir, on the capital raising, is the capital raising tied to your ambition in the specialty effort?

Kedar Upadhye: Not only that, I think there are several use of proceeds, Chirag, we have in mind for enabling resolution, so be it capital expenditure, be it some of the trials in Respiratory, be it some of the inorganic initiatives, other ideas to pursue or in-licensing or business development in branded markets, there are several use of proceeds.

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

Prakash Agarwal: Just trying to understand the India growth, you said 12% on the base effect given demonetization, I think that growth is also great growth, so was that the generics grew faster or if you could just broadly give the split, Sir?

Umang Vohra: Actually the generic did grow faster, but the growth that we spoke to you about was actually the growth in our prescription business.

Prakash Agarwal: Which is 12%?

Umang Vohra: 12 and generics also grew faster than 12; 12% was just our India business prescription growth.

Prakash Agarwal: Where I am coming from is that if we look at while the gross margins where QOQ stable, we have seen lower EBITDA margin if we exclude R&D impact, I mean last quarter was 8%, this quarter is 6%, so if we exclude the R&D, we would be actually down on the EBITDA front, so the business mix could it be due to higher generic is what I am trying to understand?

Kedar Upadhye: Yes, I think Prakash, for the EBITDA margin there will be various factors in each expenditure and revenue line, so I would not probably ascribe pre-R&D EBITDA to only the

adjustment in India business revenues. There are several variables which will impact our EBITDA percentage other than only this reduction in R&D.

Umang Vohra: We had also guided last time on the call, that there could be some one-off in our results last quarter as well to a certain extent, so I think that offset a little bit of the R&D. At least sequentially, we are seeing the EBITDA to be marginally higher or than the previous quarter.

Prakash Agarwal: On the US, just trying to understand the chart that you have given and the statement, so flat QOQ, platform ready for Q4 and you mentioned that some of the key launches have pushed to another quarter by more than one quarter, so how do we read this platform ready for Q4?

Umang Vohra: Platform ready for Q4 in the sense that we are ready for key launches as they come in.

Prakash Agarwal: Launches expected from Q1 and onwards, is that the right understanding?

Umang Vohra: Some launches, for example, we have got some recent approvals which we are planning to get in to the market, so I think the platform really means that you should look at it more from a perspective of the acquisition of InvaGen that in eight months or nine months, we have got business ready to be able to launch products, not just in this product but the Cipla product, so it is more a reflection on the integration that has happened and the fact that our sales and marketing team now has the potential to launch almost two products a month, so that was what the comment was made.

Prakash Agarwal: Lastly Sir, on this Slide #8, North America base business growing by 21% and we are at about $98 million, so would that be fair to assume that InvaGen would have been less than $50 million?

Kedar Upadhye: InvaGen is around $54 million, Prakash, for the quarter.

Prakash Agarwal: So InvaGen remains flat and we are seeing improvement in the base US business of Cipla?

Kedar Upadhye: That is true, Yes.

Moderator: Thank you. Next question is from the line of Kartik Mehta from Deutsche Bank. Please go ahead.

Kartik Mehta: Is there any sort of one off in the depreciation, Kedar you mentioned that there was an asset which we have sold?

Kedar Upadhye: Yes, we have provided for an idle asset and the value is about 27 crore in the depreciation line.

Kartik Mehta: Is this on an annual basis?

Kedar Upadhye: Not on annual basis, this 257 crores in the consolidated financials for the quarter include 27 crore of idle asset provision.

Umang Vohra: Regular depreciation will be 27 crores lower.

Kartik Mehta: In case of your launch which we have in the UK market, can you help us with something like targeted market share or in terms of pricing, etc., because we already have one generic in that particular market?

Kedar Upadhye: We have spoken, as you are aware there is one generic in the market and we will offer this product through all the channels. As you know, there is a CCG channel, there is a retail channel in UK for this kind of products, and overtime, we will get to a fair share of the market, we will be responsible in pricing.

Kartik Mehta: Would you think that fair share would be there in a year from your launch or even actually more than that?

Kedar Upadhye: Probably, the products like this takes some time to scale up to this kind of fair share.

Kartik Mehta: Responsible pricing would also be a function of how much competition do you anticipate after that or would it be something which you would continue?

Kedar Upadhye: Competition, we do not want to comment, unlikely there will be commoditized kind of a scenario for this kind of a product, so we do not anticipate too many competitors going forward in the medium-term.

Moderator: Thank you. Next question is from the line of Neha Manpuria from JP Morgan. Please go ahead.

Neha Manpuria: Umang, on the US business, if I look at InvaGen, we have been in the $50-55 million range over the last three quarters despite product launches coming through, I understand there is some base business pressure, but given your comment that you have not seen anything significantly change, when do you see this revenue momentum picking up for InvaGen, if you are saying that our sales team is ready for two launches a month?

Umang Vohra: Let me put it this way, that InvaGen has a pipeline of launches Neha, depending on approval, we will begin to see that trend up and also it will benefit from the Cipla India products also which are up for approval, so it is all linked to approval at this point in time. I mentioned that we will begin to see it come as and when approval happens.

Neha Manpuria: Based on your visibility, I am assuming a lot of the products are not really limited competition that have been impacted by the change in GDUFA timelines, so when do you see this approval momentum taking up for InvaGen, is it still two-three quarters away?

Umang Vohra: I would think so, I would say if the question is specific to InvaGen, Yes, then that is fine, but if it is specific to launches in the US, then it would be as I mentioned one to two quarters.

Neha Manpuria: Secondly, on Advair, what is the status of Advair for the US, have we started trial there, we had indicated that we could probably start trials sometime in this fiscal and also, the DPI opportunity in Europe, could you give any color on Seretide DPI in Europe.

Umang Vohra: On trials, Neha, we are maintaining that. We are hoping to start the trial either late this fiscal or early next fiscal for Advair. DPI opportunity may be, Kedar if you speak.

Kedar Upadhye: From our point of view, European portfolio plans are largely surrounding India at this stage, but we will come back Neha in case there is any thought.

Moderator: Thank you. Next question is from the line of Sameer Baisiwala from Morgan Stanley. Please go ahead.

Sameer Baisiwala: Umang, can you tell us how much would the US clinical trial for Seretide cost us?

Umang Vohra: I am not sure we are going to give that level of guidance, we have a number, Sameer, based on informed and based on what we have done with Albuterol, and specifically what is that you are after, exact dollar number is it?

Sameer Baisiwala: My understanding is that it can cost around $30-40 million, so I just wanted to confirm if that is the kind of an outlay, and therefore, how it can impact your margins etc., for the next year?

Umang Vohra: I am not sure we are seeing that level of clinical spend on this, actually we would not want to comment on exactly how much it would, but it will be included, whatever we do will be included as part of our overall R&D numbers that we have mentioned which we think will trend somewhere closer to 8 or 8.5 next year.

Sameer Baisiwala: I was just curious, so do you think the number can be a lot lower than what I just saw?

Umang Vohra: No, not a lot lower.

Sameer Baisiwala: Couple more on the US side, Umang, you mentioned that now you see on a day 1 more competition, so I just for like for like, how much is the price erosion in a competitive market, does it go down 96% does it go down 98%?

Umang Vohra: If you have more than four guys showing up to the party Sameer, I would think it possibly is upwards of 97-98, because the number of customers now with meaningful share is barely four or five, so if you have four guys showing up, one guy takes one customer and then if it is a little bit more than that, that is when your erosion starts.

Sameer Baisiwala: Just on the approval timelines for the ANDA that you are filing now which is October onwards, what is your assessment, do you think and these are some of these MDIs that you have started filing, could it take the usual what it used to about 30 to 40 months, or do you think now it could be a lot earlier?

Umang Vohra: I do not think we have any precedence Sameer, but I think what happens is that by the time you get your first set of queries it is 9 months or 10 months, I would find it practically impossible to believe that anybody would get an approval for an MDI product in the first round itself, and therefore, I would think that it is not going to be less than 20 months that would be a safe bet. I do not know whether it could be 30, but I think there is a better chance that it would be somewhere closer to the 20-22 month time period.

Sameer Baisiwala: One last question with your permission, on GST if the government sticks with July 1st, do you think there is going to be a meaningful disruption in the supply chain in the preceding quarter and second, do you think your vendors and various people in supply chain are all IT ready for GST?

Umang Vohra: Not all, not necessarily the vendors and not necessarily our business partners, I do not think any of them are ready. I do think there will be a disruption for sure. I think that this disruption will last an amount of two to three quarters and probably start a quarter before it is implemented and run in well into two months after the GST is implemented.

Sameer Baisiwala: When you say disruption, you are saying destocking or much lower inventory levels so therefore it should impact?

Umang Vohra: Absolutely, destocking will happen and I also think that post implementation also there will be a huge amount of I would say people will not be very clear on what to file where, etc., how to link up tax and things like that, so there will be confusion.

Moderator: Thank you. Next question is from the line of Girish Bakhru from HSBC. Please go ahead.

Girish Bakhru: Actually, just following up on the last one, Umang you would say even Proventil can get queries and approval timeline can be more than 20 months?

Umang Vohra: Yes, could be because there is no precedence of this with the agency and I would find it very difficult to believe that a file would be approved in less than that period, I do not know, that is our feeling, but we could be pleasantly proved wrong, but I am not sure that this complexity of product that you would have an approval within the 12-14 month period.

Girish Bakhru: On the Advair side in UK, when you say fair share, what timeline would you say would that come in, would it reflect already in FY18 or it would be much longer than that?

Kedar Upadhye: It could be beyond the first 9 months or 12 months, Girish.

Girish Bakhru: Actually, I am bit also not sure, do you have another product which is different under different brand name called Zerodol or something in the market which is registered with UK?

Kedar Upadhye: The current marketing authorization which we will get commercialized that is called Sereflo.

Girish Bakhru: Okay, so that is the key product, and any particular reason why neither of the generics have low dose on this product in the market?

Alpesh Dalal: It is a very small portion and then there are certain challenges relating to its approving its equivalence and all.

Girish Bakhru: Okay, and just lastly, Kedar, tax rate on this 121 crore income will be full tax?

Umang Vohra: It was a tax friendly structure, it was structured with the IP in a different jurisdiction, so it will not be that. The tax rate increase you are saying is on account of a change in our ETR estimate.

Moderator: Thank you. Next question is from the line of Nimish Mehta from Research Delta Advisors. Please go ahead.

Nimish Mehta: Sir on the other expenses if I were to exclude the R&D expense that you mentioned at 6.2% of net sales, the other expense looks pretty high, if I am not wrong it is high by about 40% YOY and even on a QOQ basis, it is fairly high?

Kedar Upadhye: Nimish, the expenditure in this quarter includes the consolidation of our US acquisition, the line items be it people expense or depreciation or other expenditure, all these line includes the consolidation of the US acquisition, which is not there in the last year same period.

Nimish Mehta: By consolidation, what do you mean?

Kedar Upadhye: As you are aware, we acquired InvaGen and Exelan, so that has been merged.

Nimish Mehta: That is the only reason basically.

Kedar Upadhye: Yes.

Nimish Mehta: Second on the US business, on a QOQ basis, it is almost flattish $98-99 million and you mentioned that the own business of Cipla has done fairly well so does that mean that InvaGen sales have actually declined?

Umang Vohra: Not declined, I would say that they are static with absence of any big approvals, the sales there would be static because the US market behaves in that manner.

Nimish Mehta: Right but on one hand, we have the Cipla business growing healthy and on the other hand, we have the total sales being flat on a QOQ basis, which is where I am coming from?

Umang Vohra: Cipla business on a full year in terms of what we have launched is only one year old and it is not more than $30-40 million today, so if you were put that by quarter, it is barely 6-7 million and the delta will be far lesser than that, right so it is not going to compensate for anything on the InvaGen base.

Nimish Mehta: Lastly, what would you attribute this great domestic business growth which I understand if it is 12% even adjusted to the higher base, because the acute market has actually suffered this quarter, so what made Cipla grow so robustly and is it kind of sustainable?

Umang Vohra: I will just answer it by saying that the last three quarters we have shown the same amount of growth, it is not as if this quarter is higher at 12 even our Quarter-2 growth was there, so I do not think it is necessarily linked to acute, I think across therapies we are working on prescription and that is leading to the growth.

Nimish Mehta: Is there a split available between acute growth and chronic growth that will be helpful?

Kedar Upadhye: You can source it from public data, Nimish.

Moderator: Thank you. Next question is from the line of Anubhav Agarwal from Credit Suisse. Please go ahead.

Anubhav Agarwal: One question on this Albuterol filing that we have done, I just wanted to understand that what is the incremental complexity to file the other two ProAir and Ventolin, what changes because APIs are same, where does the complexity comes in here?

Umang Vohra: Clinical trials will be the complexity and the expenditure on the clinical trial will be the complexity.

Anubhav Agarwal: I agree like patient dosing etc., but how much of what you have done and let us say if we pursue both the drugs, ProAir and Ventolin, first are we pursuing that, and if you pursue them incrementally let us say have you already done in terms of 50% of the work because incrementally it is only clinical trial, drug wise we should already be there?

Umang Vohra: There are some differences in the product as well between the two, it is not as if all of them all are Albuterol, product characteristics differ. You have to have fundamentally a different product development thing. Our belief is and this is what we are trying to do is to try and see how single Albuterol could be an equivalent for all the three and that is not practically and I think that here it depends really on the customer strategy, and what the customers do with it. At this point in time, we are not going to divulge too much of details on this, but all three of them are different developments and then different clinics.

Anubhav Agarwal: When you say customer strategy, it means is this a partnered product for us?

Umang Vohra: Not, it is not a partnered product, I am saying customer as an end customer.

Anubhav Agarwal: Basically on the development phase, we have only done Albuterol. For Proventil, we have not started the clinical trial?

Umang Vohra: Yes, unlikely we will.

Anubhav Agarwal: Why would you say that, because market size for other two is also decent?

Umang Vohra: We are looking at how, as I mentioned to you that there could be therapeutic equivalence across the three Albuterols, that is what we are examining.

Anubhav Agarwal: I have other question the EM business, you mentioned that large part of decline was driven by global access business there, global access business decline were small, first of all out of this EM business of $110 million a quarter, how much is the global access business today?

Kedar Upadhye: Global access business, Anubhav, today per quarter is roughly $35-40 million about $160 billion annualized run rate.

Anubhav Agarwal: When this global access business have declined looks like if I may comment almost like 20%, which tender are we talking about, malaria or ARV, what led to the decline?

Umang Vohra: This is both, so as you know WHO and PEPFAR these are the two routes and there are several geographies within our data, so it would be tough to give the breakup, Anubhav.

Anubhav Agarwal: But would you say that this is like as you mentioned in the presentation, this is more phasing of the tender, so this is like just one off, it should come back next quarter or is malaria tender rebidding is still going to happen, I am trying to understand is it looks like one-off is not a structured decline, what is the status here?

Umang Vohra: I think it is a mix of a couple of factors Anubhav. The first factor is also we had some supply issues, some of the vendors who or some of our partners have had FDA issues at their site, and therefore, that is one of the reasons why we cannot supply as much as we were supplying earlier to the global fund. The second is that the global fund has also now restructured the way that they do business and that was the theme last year. This year that is coming into shape and it is not fully taken off in terms of the total capacity, so it is a just a mix of these two or three factors. If your question is have we lost any tender, we have not.

Anubhav Agarwal: Kedar just one clarify, interest cost also has spiked to 59 crore versus 35 crore, any change in net debt position or was it one-off here?

Kedar Upadhye: The FOREX movement on the dollarized debt, the portion beyond rupee rate needs to be clubbed as interest and there is some one-time element for about 10 crores or so, so I think going forward maybe you should model 10 crores lesser subject to the debt-equity position.

Anubhav Agarwal: In Quarter-2, we were 35 crore, now we are 59 crore, but you are saying that from here onwards we will be like 48-49 crore, but not back to 35 crore?

Kedar Upadhye: It could be, like what I said there is an element on the FOREX fluctuation, so subject to Forex and subject to debt equity probably we could possibly return.

Anubhav Agarwal: So if constant currency, we should still model 35, would you say that?

Kedar Upadhye: Yes, probably Yes.

Moderator: Thank you. Next question is from the line of Chirag Dagli from HDFC Mutual Fund. Please go ahead.

Chirag Dagli: Sir, have we seen Wellbutrin launch in the December quarter?

Umang Vohra: Yes, marginally we have.

Chirag Dagli: But you have not seen full scale launch?

Umang Vohra: Yes.

Chirag Dagli: Okay, and when you sort of think of each of your businesses and you look at the margins that these businesses enjoy, which of the businesses do you think has the maximum margin potential in terms of expansion potential, when you talk of an overall margin improvement trajectory?

Kedar Upadhye: What you are seeing Chirag from last year to this year, the improvement in our South Africa and India businesses from a percentage profitability standpoint is very significant, probably to expect this two businesses to grow on the top of where they standing now is not going to be easy, I think the traction would come from the mix improvement at a company level from a geography standpoint.

Chirag Dagli: You mean gross margins will improve?

Kedar Upadhye: Gross margin and net margin both, subject to how much we invest in R&D and subject to the mix of various geographies and primary factor being what is the mix of the US business and overall, that is how I think the margin hypothesis would play out for us, but within each region like what we said, India and South Africa have significantly expanded our margins year-on-year.

Chirag Dagli: When we look at our at the current consolidated US business, is this contributing meaningfully to profits pre-R&D, how should we, if you can share some light on how this business is doing?

Kedar Upadhye: Portfolio is commoditized for the current US business, pre R&D makes money but post R&D it is not a breakeven.

Chirag Dagli: This is InvaGen plus our own old business put together.

Kedar Upadhye: That is correct Chirag, Yes.

Moderator: Thank you. That was the last question. I now hand the floor over to the management for their closing comments.

Alpesh Dalal: Thank you everybody, thanks for joining in the call and expressing your interest in Cipla and we will speak to you again in three months' time.

Moderator: Thank you. Ladies and Gentleman, on behalf of Kotak Securities, that concludes this conference. Thank you for joining us, you may now disconnect your lines.