Dr. Reddy's Laboratories Limited

Q1 FY13 Earnings Call Transcript

Kedar Upadhye *(Investor Relations)*

Good morning and good evening to all, and thank you for joining us today for Dr. Reddy's Earnings Call for Q1 of Fiscal 13. Earlier during the day, we have released our results and the same are also posted on our website. We are conducting a live webcast of this call and a transcript shall be available on our website soon. The discussion and analysis in this call will be based on the IFRS consolidated financials. To discuss the business performance and outlook, we have today Satish Reddy – our Chief Operating Officer; Umang Vohra – our Chief Financial Officer; Abhijit Mukherjee – President & Head of Global Generics and the Investor Relations team. Please note that today's call is copyrighted material of Dr. Reddy's and cannot be rebroadcast or attributed in press or media outlet without the company's expressed written consent.

Before we proceed with the call, I would like to remind everyone that the Safe Harbor language contained in today's press release also pertains to this conference call and the webcast. After the end of the call, in case, any additional clarifications are required, please feel free to get in touch with the IR team. Now, I would like to turn the call over to Mr. Umang for his opening remarks.

Umang Vohra *(Chief Financial Officer)*

Thank you, Kedar. Good morning and good evening to all. Let me begin with the key financial highlights. For this section, all the figures are translated to US dollars at a convenience translation rate of Rs.55.57 to the dollar.

Our consolidated revenues are at $457 million for the quarter and grew by 28%YoY. Revenues from our Global Generics segment are at $343 million for the quarter and grew by 32% YoY driven largely by US, Russia and India. Revenues from the Pharmaceutical Services and Active Ingredients segment (PSAI) are at $99 million and grew by 14% YoY.

Consolidated gross profit margin for the quarter is at 53.3%. Gross profit margin for Global Generics and PSAI are at 59% and 31% respectively. SG&A expenses including amortization for the quarter are at $149 million and represent an increase of 23% over the previous year, largely attributable to YoY salary increments, higher sales and marketing costs and effect of rupee depreciation against multiple currencies. Without the impact of exchange rate, this increase in SG&A is approximately 16.5%. R&D costs are at $28 million for the quarter and are approximately 6% of the revenues; and grew by 31%YoY. This time, due to the volatility of exchange rate our forex line contains a loss of Rs.30 crores attributed to time value of -options. 'Time value' is a function of volatility and time-to-maturity and is likely to reverse over the balance period of the year.

The effective tax rate for this year is at 18%. However, due to our dispatches to the US market the unrealized profit impact of the inventory has reduced this rate to 10% this quarter. As a reminder, the normalized effective tax rate for Q1 of the previous year was 16% against the reported 4% for the same period. This was primarily on account of the tax benefit on the unrealized profits on shipments made to the United States in that quarter which was primarily olanzapine.

Profit after tax for the year is at $60 million, 13% of sales and shows a YoY growth of 28%. Similarly, adjusted profit after tax for the quarter is at $55 million and shows a YoY growth of 26%.

Key balance sheet highlights are as follows: Our working capital increased by $29 million and is largely in line with the increase in sales and its mix across the markets. Capital expenditure for the quarter is at $33 million. Foreign currency cash flow hedges for the next 18 months in the form of derivatives and loans are at approximately $620 million, largely hedged around Rs. 51.3 to Rs. 53.4 to a dollar rate. In addition, we have balance sheet hedges of $225 million which are more or less at current rates.

Our mark-to-market losses and hedge reserve account in the balance sheet on account of the cash flow hedges is approximately $51 million and this is a figure which will spread over the next 18 months if the dollar rates stay the same as they are at the current moment. Net debt at $253 million, represents a net debt to equity ratio of 0.24 and this ratio is consistent versus the sequential quarter as well.

With this I now request Satish to take us through the key business highlights.

Satish Reddy (Chief Operating Officer)

Thank you, Umang. Overall, this has been a relatively good quarter for us. Performance in US generics, emerging markets and India demonstrated steady growth. On the other hand, there was a lower off-take by some of our key customers of PSAI business. In addition, atorvastatin generic launch got delayed a bit. As you are aware, we have launched it in this week and we will attempt to build the desired level of market share during the coming months. During this quarter we launched clopidogrel and the OTC version of lansoprazole in the US market. Towards the end of the quarter we also launched ibandronate sodium. Q2 FY13 will see the full benefit of atorvastatin and ibandronate launches. With this, our product offering in the US generics market is getting broader.

Our partnership with Merck Serono which we entered into in the month of June increases the visibility of monetization from biosimilars opportunity. We believe that this is a win-win partnership wherein Merck Serono will benefit from our proven early stage product development capabilities and commercialization experience in some of the emerging markets. In turn, we will benefit from their expertise in late-stage development, production and global commercialization.

I will now cover some of the specific business highlights for each of our markets. Please note that in this section the revenue numbers referred to are in the local currencies at respective period average exchange rates.

Revenues for the North American Generics for this quarter are at $159 million, reflecting a YoY growth of 27% largely driven by products such as ziprasidone, fondaparinux, clopidogrel, quetiapine, lansoprazole OTC and products from our Shreveport facility. This growth was marginally offset by the pricing pressures. New product launches at regular intervals, coupled with the increased focus on the OTC limited competition product lines helped us strengthen our portfolio and enhance customer franchise.

Moving on to India, I am happy to note that specific interventions made over the past several quarters are showing the desired results. Revenues for the quarter are at Rs. 348 crores which represents a YoY growth of 19%. This growth was driven by a healthy revival of volumes across most of our top 15 brands and also partly due to a low base effect. Improvement of prescription share across key brands and sales force excellence has helped us in this endeavor.

Russian market with revenues of $65 million, the growth in Ruble terms was 30% over the previous year. Growth for the quarter was driven by volume increase across key prescription brands and OTC portfolio.

Moving on to the PSAI business. Revenues for Active Ingredients segment for the quarter are marginally lower than the previous year due to deferment of launches by some of our key customers. We expect a relatively strong revival in the next quarter.

With this I would now like to open the call for questions.

Balaji Prasad: My first question is on the Indian market. You had two quarters of industry level growth showing a strong recovery. Can you just give us some clarity on how sustainable you see this is going to be; is it the trend rate that we can expect going forward?

Abhijit Mukherjee: This is the branded generics market and is largely dependent on sales force excellence and execution. Last few quarters, we have been working on some of the actions which are showing results. Going ahead I think these are reasonably sustainable. There would be seasonal fluctuations in Indian market as it happens every year, but it is not a flash in the pan performance.

Balaji Prasad: Would you at all be concerned with any of the newer changes been proposed by the government in terms of generics drugs for the population?

Satish Reddy This will affect the entire industry in terms of the pricing policy in whichever form it comes out. So, I think we will have to wait to see how it affects any specific brands belonging to the company but in case this pricing policy comes out which it will at some point of time, it is bound to affect the entire industry.

Balaji Prasad: My second question is on basically your operating profile going forward. You highlighted a couple of key launches in the coming quarters. Now, if these launches do happen, can you give us some thought or throw some color on what this has do to the operating margin profile?

Umang Vohra: This quarter we have not seen the full effect of either ibandronate or atorvastatin, since it was launched only very recently. We have not seen the effect of new products conclusively kicking into this quarter. Q4 in Generics was 58%, and Q1 this year is 59%. So, sequentially there has been an improvement in Generics margins. I would expect that as new products momentum gains, margins would probably be better than 59% going forward, but there is price compression we are seeing in the market as well.

Balaji Prasad: It is at 59% right?

Umang Vohra: This quarter it is 59%, the previous sequential quarter was 58% on the Global Generics gross margins spectrum.

Nimish Mehta: First of all, can you just let us know the constant currency growth in key markets; the US, Europe and CIS, Russia?

Umang Vohra: The US, constant currency growth is 27% in dollar terms, Germany, Euro terms is 17%, if you look at India that is constant at 19% in the rupee terms, if you look at Russia, constant growth is 30% in Ruble terms.

Nimish Mehta: Now that we have this OTC business significant in US, is it fair to assume that it is profitable to the level of your average margins or can you just throw some light on its profitability although you may not - give me exact numbers?

Umang Vohra: We do not disclose profitability by segment, but all I can say is that the margin profile for OTC is slightly lower than our regular Rx but it has stabilized at a level which we are pretty happy with.

Nimish Mehta: You are likely to see any significant increase in margins here or it will continue?

Umang Vohra: Unlikely. OTC is a fairly stable business.

Arvind Bothra: I just wanted to understand the steep jump in SG&A. Is there any particular reason or is there any forex translation loss? We just wanted to have a color on how can we project it going forward. Are we going to see such spikes going ahead?

Umang Vohra: The SG&A growth is 23% over the previous year and this includes the forex impact. Without the forex impact, the growth is 16.5%.

Arvind Bothra: And what kind of forex are we looking at, Umang?

Umang Vohra: Last year the rate was at Rs.44 to a dollar and this year it is approximately Rs. 54 to the dollar on the cost basis. So, there is an almost 20-25% jump in exchange rate translation. If you take that forex impact out the growth in SG&A is only 16.5% and that growth is largely on account of increments that happened in the first quarter for us as well as some selling and marketing expenditure that has happened in our rest of the world and Russia market. The other thing that I will also add here is that we have also accrued a user fee in line with the Generic Drug User Fee Act which came into existence on the 9th of July and that accrual is close to about Rs. 7 crores.

Arvind Bothra: But if I am to look at the profile going forward, 30% of top-line is a fair assumption for SG&A or we would see that to moderate as a percentage of sales?

Umang Vohra: We do not guide to that. All I would say is that we should hopefully see a lesser amount of SG&A growth, compared to sales. So, if we were to take this quarter, because of the forex the translation has happened, but other than that I think continuously going forward maybe a 15-20% range is the best for a SG&A growth including possibly inflationary impact of forex.

Arvind Bothra: Secondly, I just wanted to understand on the gross margins front. Of course, on a YoY basis we are at a flat level whereas we had some favorable impact of a) currency, b) India and Russia growth being much stronger and c) partially, there could be impact of -ziprasidone as well. But despite all these three factors playing out the gross margins did not improve significantly. Any particular reason you can ascribe to that?

Umang Vohra: As I mentioned earlier, the sequential quarter on Generics had a margin of 58%. This quarter the margins up by a percent, it is come in at 59%. The margin could have been a little higher but we are witnessing some amount of price compression in the market. Also, from a pure US quarter perspective this has not really been a good quarter for product launches. We did not get the effect of -ibandronate because it was launched after a cutoff period for sale and atorvastatin got launched only recently. So, we have not really seen the quantum of new product launches which generally helps offset price compression.

Arvind Bothra: Final question on the US market, products like clopidogrel or atorvastatin post the patent expiration and exclusivity, the price erosion has been as high as 97-98%. Do you still think that these can be material contributors to an incremental margin or would they enjoy a similar margin to your normal US business?

Abhijit Mukherjee: You are right; I think most of the recent big launches have seen 97-98% erosion from the innovator prices. So, any big product would see a similar sort of erosion. But one is backward integrated, it is not a big business but it is still a reasonably healthy business to go after.

Arvind Bothra: And we are not seeing a significant loss of Simvastatin post atorvastatin?

Abhijit Mukherjee: Too early to comment.

Ravi Agarwal: A couple of questions. First, when we are talking of our biosimilars business, you were alluding to this deal which you have done with Merck Serono, I do believe we also had something going with GSK regarding the emerging markets for the biosimilars. Is there some product breakup which has happened across these two partners or it is just like a different strategy altogether now?

Satish Reddy: For the emerging markets, one of the deals that we had done with GSK, also included a discussion on product specific biosimilar, which was much earlier. So, Merck Serono is a separate deal primarily targeted towards the regulated markets. That is how we need to visualize this deal.

Ravi Agarwal: And just carrying this forward, what is the status on the Reditux filing for the European market?

Umang Vohra: We are still in the process of having discussions with the regulator and there will be studies which will be kicked off. And now, I think whatever we will do, will be in conjunction with the new partner.

Ravi Agarwal: Any kind of timelines we could look at?

Umang Vohra: So we are not divulging that. I think internally we are aware of some rough timelines but at this point in time we do not want to give that out.

Ravi Agarwal: Second question is on OTC, could you just tell us about some of the initiatives we are taking for OTC in India and would that entail any additional meaningful cost in terms of your cost base for the next couple of quarters?

Abhijit Mukherjee: OTC in India is very early. Currently, we just have two products in the market, somewhat in an experimental stage and it is going well. So, we want to feel the business and then we will slowly scale up over the next few years.

Ravi Agarwal: Final question, if I just look at the sequential numbers for the US part of the business, last quarter we were roughly tracking around $170-175 million, this quarter we seem to be tracking somewhere around $145-odd million and we had ibandronate coming at the end, possibly we'll not get that benefit as yet, but we still had a couple of key products as you mentioned. What could really explain this big decline from say Q4 to Q1?

Umang Vohra: Let me just first give you the numbers. What happens is in the reported numbers you also have the impact of hedge. So the reported number in Q4 was $176 million for the US and the same in Q1 is $159 million. So, it is a $16 million sequential decline. But you really got to look at this with respect of where we were in Q1 of last year, we were $125 million, we moved up to $135 million in Q2, we moved up significantly because of olanzapine at $235 million and then we moved up to $176 million. So, US has been on a very significant sequential QoQ growth perspective. It has taken a small break this quarter and that is probably because we have not been able to have those many number of new product launches which is the reason that we are explaining even the fact that price compression is not possibly set off completely with new product launches and that is why you are seeing this difference.

Ravi Agarwal: You also mentioned I think in the press conference earlier that there are some deferment of sales which has happened. If you could just explain that?

Umang Vohra: The deferment of sale is largely linked to PSAI. This quarter has been a little weaker than what we expected. That is probably because a large portion of the sales linked to the customer selling the product will happen possibly in Q2. So, we are expecting a much better Q2 for the PSAI segment.

.**Manoj Garg**: Since we have done around $450 million in this quarter and looking at the kind of guidance which we have for this year as a whole of around $2.5 billion. That means the asking run rate for the next three quarters would be in the range from $650 million to $670 million. So can you give us some color on that and how we are likely to go up? And do we still hold that $2.5 billion kind of aspiration number?

Umang Vohra: I would say that we have articulated earlier a goal of about directionally moving to $2.7 billion. I do not believe that the scale up to $650 million to $670 million is not possible QoQ and actually, we are pretty confident about the scale up happening in the balance three quarters and it is linked largely to new product launches. But having said that, I would also say that there are events such as approval delays possibly in some products, that would hit us, like it did for atorvastatin, and those could be some variability that we could see. But the trajectory for the Q2, Q3 and Q4 is significantly higher than what we have seen in Q1.

Manoj Garg: And most of those launches which you are anticipating going forward, they are more of sustainable kind of nature or there could be some one-off elements?

Umang Vohra: They are mixed. Some of them would be sustainable some of them would not. When you say one-off, it means that you entered the market with the others, and some of them are sustainable, some of them are regular markets.

Manoj Garg: Second thing, on a sequential basis like, I think depreciation has come down around 12% to 13% from Rs 102 crores, which was there in Q4FY12 to Rs 89-90 crores. Any specific reason on that?

Umang Vohra: No, I do not think there is any specific reason for depreciation. There is generally an interest capitalization charge that happens in accounting. And I think this interest capitalization charge would possibly have made the difference. But I do not believe there is any significant decrease in the depreciation.

Manoj Garg: There are rumours in the market like there is some leadership change which will happen in the US business. Any color on that?

Satish Reddy: We were talking about leadership change, where our Head of North America operations, Amit Patel, is moving on. Having said that, there is sufficient management bandwidth in the North American market and there is enough leadership in place and talent.

Sameer Baisiwala: I just wanted to check on the US pricing. Is it a portfolio-wide pricing pressure that you are facing or is it just a couple of products where there has been a incremental competition which is driving down the prices for the US business?

Abhijit Mukherjee: No, it is not portfolio-wide, Like in any product, it depends on how many people are getting into the product on day one. For example in Plavix, the number of players were far too many, so also in the case of Seroquel. In atorvastatin as well that is when compared to such a big molecule with five players in, the erosion is rather drastic. In fact, from what we have envisaged the erosion is much more. But having said that, I am saying that if one gets a good product, I think essentially the generic gain is going to shift into what are your launches rather than the question being that what is the erosion, the product would see more erosion than what it has been witnessing in the past. But what is more important is what would be the product for the future and which company gets those products to the market.

Sameer Baisiwala: And just in that context, do you think Metroprolol XL i.e. Toprol XL is going to be a credible opportunity for the current fiscal year?

Abhijit Mukherjee: So it is in an evaluation with USFDA at the moment. Depends on how it goes.

Sameer Baisiwala: Is that part of your aspiration to grow 30% ($2.5 billion)?

Abhijit Mulherji: Yes, to an extent.

Anubhav Agarwal: I just wanted to understand this decline in the US business a bit better. I have not understood it because the decline is almost -about more than 10% decline from $177 million to $159 million. Just one clarification here. When you recorded ziprasidone last quarter, I am not asking the number here, but would majority of it have been recorded in the fourth quarter and has this quarter been a very low number?

Umang Vohra: No, I think what we have seen on ziprasidone, it is a little bit of equal for both. I think this quarter is marginally lower than the previous quarter, but it is not significantly off on ziprasidone. On the rest of the margins, if you apply a 10% price erosion across some selective products, you will come to the rough number that we are talking about. Generally, this is 3-5%. The other thing is that we have also seen some higher OTC in the mix as well. And as a result of that, the cumulative value would get represented from a mix effect.

Anubhav Agarwal: And just a question to follow here is, if Ziprasidone was a part of your sales this quarter, then even despite that, margins are still at 59%. I am assuming that in Ziprasidone you are still earning much higher margins. So I have been asking this question for the last two quarters now. I structurally see that margins, what we are earning, gross margins in the Global Generics now are much, much lower, even excluding the DEPB impact versus first half that we earned in the last year. This quarter having such a significant favorable mix from India and Russia.

Umang Vohra: Let me put it this way. The margins in any of our emerging markets are not under pressure. India, Russia, or API are showing better margins, so it is isolated possibly to what we have seen in this quarter in the US. And the fact is that last quarter we were 58% in Global Generics, this quarter, we have gone up to 59%. So we have seen some margin improvement on account of emerging markets and the mix. But yes, we will agree that there is margin pressure and that is happening because of the price compression that we have seen in Q1. We certainly think that this is probably one of the most severe price compressions we have seen in some while now.

Anubhav Agarwal: And just one more question, in Russia, you had two very, very strong quarters, this one and the last one. Do you think that this could impact the growth of Dr. Reddy’s in Russia in the next quarter? I am just asking that can you keep growing at, let us say, 20% plus growth rate even in the next two quarters?

Abhijit Mukherjee: This is again a branded market. There is a seasonal factor. Each of the branded markets in each part of the world has its own peculiarities in terms of season. So it would be not fair to say that we will have uniform growth in all the four quarters. But having said that, there is some growth in Russia on both

Rx as well as OTC products. Both have registered a very, very significant growth, the story is strong, but difficult to put a figure on a quarter-on-quarter basis.

Bino Pathiparampil: Just a clarification on the US revenue accounting. If I correlate the numbers given in INR and USD the revenue seems to be booked at about a rate less than Rs. 50 to the dollar whereas the average rate was about Rs.54 a dollar. So my understanding was that most of the hedging related accounting happens in the financial expenses part. So why this has been the case? Could you please explain that?

Umang Vohra: There are two types of hedges we take. The first type of hedges is hedges over forecasted cash flows which we call 'cash flow hedging'. The accounting treatment for this cash flow hedging is that it gets booked to the revenue line at the rate of the hedge. Our rates of hedges roughly are in the Rs. 49 to 50 to a dollar range. This quarter we booked revenues at Rs.50.2 to the dollar. What comes in the P&L in the forex line is the balance sheet hedges that we take to protect all our assets on the balance sheet, which means our receivables and things like that.

Bino Pathiparampil: So all balance sheet hedges are directly on the forex line item?

Umang Vohra: That is right. All balance sheet hedges are on the forex line item. All P&L hedges, which mean forecasted cash flow hedges are booked to sale directly.

Bino Pathiparampil: In which case, may I also know what rate you have consolidated Betapharm revenues at?

Umang Vohra: I think it is about Rs. 69 to the Euro.

Bino Pathiparampil: Do you have hedges there?

Umang Vohra: No, we do not. We only hedge on the dollar, on the cash flow side.

Bino Pathiparampil: So continuing with the US, earlier within that 2.7 direction you had roughly $900 million direction in the US. Is that directionally looking sound even now?

Umang Vohra: I think it would be marginally lower from the $900 million number.

Bino Pathiparampil: In Betapharm, after several quarters of revenue declines, we have seen some stabilization and in fact growth. So is that an indication that we are kind of bottoming out there and we can look to at least a stable revenue and profitability there?

Umang Vohra: We would like to believe that, but it is too early to call.

Bino Pathiparampil: On the PSAI front, would you be able to give some constant currency growth?

Umang Vohra: Constant currency PSAI has been flattish versus the previous year and that is because a large portion of the revenues are deferred to Q2 and Q3 based on customer orders.

Bino Pathiparampil: For the full year, what kind of growth are you expecting in PSAI?

Umang Vohra: I do not think we want to guide to any number.

Bino Pathiparampil: Would be a decent growth?

Umang Vohra: Yes, it would be a fairly decent growth.

Bino Pathiparampil: At constant currency?

Umang Vohra: At constant currency, yes.

Bhavin Shah: OTC has been about 21% of US, would that be a reflection of what we probably would do at the end of the year?

Abhijit Mukherjee: Somewhat in a similar range. I think there is no other major launch, but there is some organic growth in some of the assets.

Bhavin Shah: And could you share what Bristol would have done in this quarter specifically?

Abhijit Mukherjee: Specifically, we would not be able to give you a figure, but this is an antibiotics business – seasonal in nature and so it varies from quarter-to-quarter.

Bhavin Shah: But it is trailing your expectations?

Umang Vohra: It is meeting our expectations.

Abhijit Mukherjee: Yes, probably.

Ranjit Kapadia: My question relates to Biosimilars. Can you guide how many numbers of products are there in the pipeline and when you can reach a critical mass in this business?

Satish Reddy: I think the pattern on the growth on biosimilars will follow largely the same sequence that we have been saying before, which is, launches will take place in India and there will be significant revenue coming out of that. Besides the products that we will launch, the products that are currently in the market, also will see a significant growth. Then the next wave of growth would come from the emerging markets. So this is something which is now scaling up and again, this all depends on when we get approvals in those emerging markets. If you are really looking at a sizable business size coming in from this space, this will really be a few years away because it is more dependant on the launch timelines for the regulated markets. So that is a few years away.

Ranjit Kapadia: And this Glaxo and Merck deals, do you feel that it will start contributing from FY14 onwards?

Satish Reddy: No, it will be further than that.

Nitin Agarwal: Umang, just following up on the question about the gross margins which one of the earlier participants asked. You sort of referred to the margins - in Q4 and Q1 at 59%, 58% -respectively. But if I remember, we were 64%, 65% margins at the gross level for the Global Generics business in H1 of last year, and then there was no Zyprexa. So what has really led to a compression on a YoY basis, when the currency has been in our favor ?

Umang Vohra: So I would answer it in two ways. I think last year we had export benefits to the extent of almost 3% in net margin and thus the 64%. Having said that, the currency depreciation should have affected us, should have given us an impact. However sequentially the real change from 64% to a more normal range already happened in Q2 of last year. In Q4, we reported 58%. In Q3, because of olanzapine we reported higher. But if you look at it, the change had already happened in Q3 of last year. Now this quarter, we could have seen a little bit of higher margin but for the price compression. So I think we are going to wait to see what Q2, Q3 and Q4 delivers, but this quarter certainly we have seen more price compression than we have ever seen in any other quarter before.

Nitin Agarwal: And this is what, as you sort of discussed, has been on specific two or three products where it has come through or it has been where certainly competition came in much stronger than what you anticipated or is that the way to look at it?

Umang Vohra: Multiple players on products, which have gone generic, that is one and maybe one or two selective products other than that.

Nitin Agarwal: And on the US sales, you said you booked a sales net of the hedges which sort of crystallized. So essentially from a reported perspective, has there been a big impact on the numbers which have been reported for the quarter for the US growth?

Umang Vohra: At dollar-to-dollar level, before we book the number, on account of hedge accounting, the US numbers are close to $160 million this quarter. So after we book the hedge, I think there would be a hedge impact of roughly about $10 million to $12 million on US revenues.

Nitin Agarwal: And what would have been that number for Q4, roughly?

Umang Vohra: Q4 was $176 million.

Nitin Agarwal: And we have talked about the $800, $900 million number for the US business, and we are at about $160-odd million for the quarter and we sort of right now have visibility say on atorva and Boniva, which are sizable products, and they can contribute to a certain amount. But clearly, this will not fill up the gap, which we are looking at as far as the full year numbers are concerned. So how does one look at this whole gap getting filled out in terms of the numbers that we have in our mind or have been sort of looking at for the year?

Abhijit Mukherjee: There are quite a few products, which specifically we would not be able to provide in this call. There are quite a few products which are in an approval stage and going through various levels of scrutiny. They would be coming in between now and Q4. As you all must be aware that Propecia launch is in Q4 as this is in the public domain. The story in the US market is going to be which product one is able to launch rather than just sort of fighting out for market share in me-too.

Nitin Agarwal: And do we see some of these products coming through in the current quarter or it is all going to be completely back into the second half of the year?

Abhijit Mukherjee: Difficult to say. It will be unfair to comment on the FDA's approval timeline.

Nitin Agarwal: Umang, on the SG&A, we are about 27.5% of sales for the current quarter. Is there a number as a percentage of sales that we should use or it could be probably a little lower , is it a number that we are generally comfortable with, is it a long, medium term, sustainable number for us?

Umang Vohra: No, I think as the business grows a percentage, the SG&A percentage to sales should reduce. But reduce does not mean that it will go back to, say, 15%. I think it should stabilize as business grows to somewhere around the 25%, 26% range. So it would not be a very significant reduction from where we are today. But we will say this that the growth in SG&A will be lower than the growth in sales.

Nitin Agarwal: So we should be looking at a potentially lower trend, 27.5% as a new sales number in the coming quarters?

Umang Vohra: Yes, we could say that.

Balaji Prasad: Congratulations on getting the clearance on your Mexican plant. Just wanted to get a sense of how this will impact your business now. Can we expect an incremental $30 million or so, which I believe was the sales being done from this plant earlier, can we expect that to come on board now?

Satish Reddy: Basically, the import alert will be lifted. So that is a consequence of what we have just disclosed. Now, the sales have to resume. So it will not be exactly the same level as what we indicated earlier that we lost because there has been time lag and customers are not going to accept that long, hence it will take time to build it up again.

Balaji Prasad: Any thoughts on the timelines that we can say before it reaches like the sales of earlier levels?

Satish Reddy: Let us give it sometime because we also need to see the pattern of build up price, so I do not want to commit myself to a certain timeline. We actually need to see the volumes build up and get the customer first.

Ravi Agarwal: Umang just to understand the concept of hedging, which you were mentioning, you were talking about the fact that your cash flow hedging you have taken your revenues and the quarter, you booked at around Rs. 50.2 to a dollar on an average. And you also in your opening comments mentioned that your current hedges are between Rs. 51 and 53.5 odd to a dollar range. How long are these hedges going to be for? And for how many more months should we expect these hedges to play out?

Umang Vohra: Our policy, Ravi, is to have hedges for 18 months. We cover 60% of our net exposures. Now what happens is that if the sales fall off, that 60% started becoming larger and this is what happened in this quarter. The Rs.51 to 53 to a dollar range that you are talking about is the hedge rate for the balance period, let us say four to five quarters which is the next 18 months.

Ravi Agarwal: In a very simplistic way if I have to assume, I could possibly assume that our US revenues would be booked within this range at least for the next nine months?

Umang Vohra: That is right. You could assume a booking rate between Rs.52 and Rs.53 to a dollar because there will be open element also to the US trade. We only hedge 60% of it.

Ravi Agarwal: The other thing I just wanted to understand from your balance sheet is I see that you have a very large amount of cash and cash equivalents with you. I mean, obviously, some part of it is because of working capital loans which you might have taken. But any rationale for keeping such a large amount on hand, $400-odd-million in your books?

Umang Vohra: Our capex programs there, that is about $150 million. We also went out last year to raise money before the Euro crisis hit and we got a competitive rate there. And also we had this mismatch between short-term and long-term. So if you take out the short-term funding, there is not too much of cash then on the balance sheet. So if you take out the impact of short-term loans of working capital, right, and if you were to pay all of those off, you would not have a loan balance of more than $150 million, $200 million.

Ravi Agarwal: And just my final question here, when you talk of margins, between PSAI and your Generics, obviously, one big delta for at least for next quarter should come from the PSAI business because that I believe would be a growing part of your business. But just on a gross thing how much could one see in terms of an improvement? I am not asking for your formal guidance, the range last year for the remaining three quarters have been from 53 to almost up to 60% at a current level. So what do you think is a fair number to look at from a company perspective given whatever we are seeing in terms of pricing and everything else that you have discussed?

Kedar Upadhye: Excluding the olanzapine benefit in Q3 of last year, we have been at 53%, 54%. And even in this quarter also we are tracking at that percentage. So as an approximation I think one could take that percentage.

Ravi Agarwal: Even for the remaining three quarters?

Kedar Upadhaye: Possibly. Again, it is a function of the business mix, it is a function of the product mix, currency, etc. So, we would not want to take a guess at that. But I think unlikely that we will see a drastic upsurge or a drastic weakening from this trend.

Anubhav Agarwal: Yes, just one clarification. You provided for the GDUFA. Is there any ANDA which you dropped or your pending ANDAs will remain the same?

Umang Vohra: The provision is made on the basis of the pending ANDAs. I am not sure we would drop any ANDAs or anything at this stage.

Anubhav Agarwal: Okay, and second question on the Allegra D12. Can you just update on the status of that product?

Abhijit Mukherjee: At the end of the exclusivity, we -would be launching. Currently, there is still an exclusivity period running and beyond that we will launch.

Abhay Shanbhag: Getting back on the gross margins, with the revenue growth expected to come from OTC partly in US, and as you had indicated earlier, PSAI is also expected to grow quite robustly in the current year, do we see the gross margins remaining under pressure?

Umang Vohra: Abhay, the pressure part I do not know, because I think what we are saying is that we will be in the range of the 53%-odd number that we had given. And that is being by the way the margin that we have seen over the last three quarters at a consolidated company level. So I think we are going to stick with that range. The Global Generics business will possibly be in the range of 59%, 60%, depending on the launches that we have. So I think we are not seeing too much of variability in the company level on margins, it is at 53% and it has been there for the past three, four quarters.

Abhay Shanbhag: And in terms of Russia, as per the guidance earlier, do you see the growth coming down a bit with the pricing policy being implemented from April?

Abhijit Mukherjee: Russia, we are not aware of any pricing policy as such. So, there is no pricing policy being implemented at the moment.

Abhay Shanbhag: So, do you expect this growth in Russia to continue at this rate or do you expect it to come down going forward?

Abhijit Mukherjee: As I just mentioned, responding to another question that being a branded market, there is seasonality to this market; winter is the strong season. But otherwise, barring the seasonal factor, the story is quite strong. All the major Rx as well as the OTC brands is growing. There are more launches coming, there is good BD traction, we are taking products from a few companies and launching. So overall, I think it would be a good growth story.

Sameer Baisiwala: I just wanted to understand your thrust from other emerging markets. I saw your latest presentation on the website. Looks like you are going to focus on Venezuela and South Africa. So could you just take us through what exactly is the plan over here, when should we start seeing the ramp-up and product launches in these two markets?

Abhijit Mukherjee: In both of these markets and a couple of other markets as well, we are now taking a very focused approach. We have decided which therapy we will play on. We are taking advantage of our Global Generics pipeline to handpick those specific products, which are relevant for those markets, providing a lot of sales force excellence efficiency, which is the way we know it, should be played out. So overall, we are seeing in both these markets and a few other markets, growth well ahead of the market growth. So I think as a company, we are very bullish about the emerging markets and we will put all due focus. We have the right steps. We are providing a great deal of development efforts as well to make these markets very relevant, there is a business development traction as well as I was mentioning. As we have grown scale, you get more products.

Sameer Baisiwala Just a follow-up on this. What would be the size of the portfolio, what is the timeline that you are looking at in terms of ramping up the sales?

Abhijit Mukherjee: So in the first quarter as well, we had a very healthy growth, but these markets today are not huge markets. Within South Africa and Venezuela are combined in the range of about $50 million, $60 million. And there is very good growth. While else this is a good mid-term story, this is not likely to make a substantial change to the financial year.

Saion Mukherjee: Umang, is it possible to share the quantum of cash flow hedge which is there in the P&L for the quarter? That is on your revenue line. That is where you book your cash flow?

Umang Vohra: On the revenue line, it is $90 million roughly. For the quarter, it is $90 million, book to revenue.

Saion Mukherjee: So that is the kind of loss you have in the P&L.

Umang Vohra: No, no, no, that is the value of the hedge is booked. The booking at the sales line is approximately Rs.70 crores.

Saion Mukherjee: So basically, if the currency were to be at an average rate for the quarter, your EBITDA would have been higher by Rs.70 crores?

Umang Vohra: That is right.

Chirag Talati: Just a couple of questions. Firstly, can you provide some update on what is happening with your autoinjector partnership with Consort? I believe they have indicated that it is likely to be delayed by 12 more months?

Abhijit Mukherjee: On Sumatriptan front, we are still pursuing that. There were some problems in the entire value chain, which came up with some partners. So overall, it is again getting back on track and we should be there, depending on how the rest of the approval process goes through.

Chirag Talati: Were the problems relating to the device or could you throw some light?

Satish Reddy: I would not be able to share but we are sorting it out.

Chirag Talati: Secondly, can you comment on the attrition rate in terms of field force for the domestic market?

Abhijit Mukherjee: It is normally inversely proportional to the growth witnessed in markets. So certainly, the very fact that we are getting good growth, hopefully will result in a lower attrition in the coming quarters.

Chirag Talati: Because last year, you had gone up as high as 25%, so I am just trying to get a sense whether it has gone down materially from that now and are you seeing that stability?

Abhijit Mukherjee: Yes, as I said, it takes a while for growth to have an impact on attrition and we have seen early signs of stabilization. And certainly, this year we are quite confident that we will see a reduction in attrition.

Kedar Upadhye: Thank you, all for joining Dr. Reddy's senior management for the earnings conference call for the first quarter of this fiscal. In case of any additional clarifications, please feel free to get in touch with the IR team.