



Divi's Laboratories Limited

Date: February 08, 2023

To
The Secretary
National Stock Exchange of India Limited
Exchange Plaza,
Bandra-Kurla Complex, Bandra (East)
MUMBAI – 400 051

To
The Secretary
BSE Limited
Phiroze Jeejeebhoy Towers,
Dalal Street
MUMBAI – 400 001

Stock Code: DIVISLAB

Stock Code: 532488

Dear Sir/ Madam,

Sub: Transcript of Q3FY23 earnings conference call held on February 03, 2023

Ref: Regulation 30 of the SEBI (Listing Obligations and Disclosure Requirements), Regulations, 2015

We hereby submit the transcript of the earnings conference call for the quarter and nine months ended on December 31, 2022, held on February 03, 2023 at 14.00 Hrs IST. The transcript is also available on the website of the Company i.e. www.divislabs.com, under Investor Relations section.

This is for your information and records.

Thanking you,

Yours faithfully,
For **Divi's Laboratories Limited**

M. Satish Choudhury
Company Secretary & Compliance Officer



“Divi's Laboratories Limited
Q3 FY '23 Earnings Conference Call”

February 03, 2023



MANAGEMENT: DR. MURALI K. DIVI – MANAGING DIRECTOR – DIVI'S LABORATORIES LIMITED
MS. NILIMA PRASAD DIVI – WHOLE-TIME DIRECTOR, COMMERCIAL – DIVI'S LABORATORIES LIMITED
MR. L. KISHORE BABU – CHIEF FINANCIAL OFFICER - DIVI'S LABORATORIES LIMITED
MR. VENKATESA PERUMALLU – GENERAL MANAGER - FINANCE AND ACCOUNTS – DIVI'S LABORATORIES LIMITED
MR. M. SATISH CHOUDHURY – COMPANY SECRETARY AND CHIEF INVESTOR RELATIONS OFFICER – DIVI'S LABORATORIES LIMITED



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Moderator: Ladies and gentlemen, good day, and welcome to the Earnings Conference Call of Divi's Laboratories Limited for Q3 FY 2023. 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 star and then zero on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. M. Satish Choudhury. Thank you, and over to you, sir.

M. Satish Choudhury: Good afternoon to all of you. I am M. Satish Choudhury, Company Secretary and Chief Investor Relations Officer of Divi's Laboratories Limited. I welcome you all to the earnings call of the company for the quarter and 9 months ended December 31, 2022. From Divi's Lab, we have with us today, Dr. Murali K. Divi, Managing Director; Ms. Nilima Prasad Divi, Whole-Time Director (Commercial); Mr. L. Kishore Babu, Chief Financial Officer; Mr. Venkatesa Perumallu, General Manager (Finance and Accounts). During the day, our Board has approved unaudited financial results for the quarter and 9 months ended December 31, 2022, and we have released the same to the stock exchanges as well as updated the same in our website. Please note that this conference call is being recorded and a transcript of the same will be made available on the website of the company.

Please note that the audio of the conference call is the copyright material of Divi's Laboratories Limited and cannot be copied, re-broadcasted or attributed in the press or media without the specific and written consent of the company.

Let me draw your attention to the fact that on this call, our discussion will include certain forward-looking statements, which are projections or other estimates about future events. These estimates reflect management's current expectations of the future performance of the company. Please note that these estimates involve several risks and uncertainties that could cause our actual results to differ materially from what is expressed or implied. Divi's Labs or its officials does not undertake any obligation to publicly update any forward-looking statements, whether as a result of future events or otherwise. Now I hand over the conference to Dr. Murali K. Divi, Managing Director for opening remarks. Over to you, sir.

Dr. Murali K. Divi: Good morning, ladies and gentlemen. Welcome to our earnings call for the quarter 3 of financial year 2023. I hope that all of you, your family and your friends are in good health.

I am pleased to report that our manufacturing operations has been running smoothly despite the volatile global market scenarios, including the global recession, energy crisis and geopolitical uncertainty. After having a great opportunity to service COVID products during last year, we are seeing normalization of our core API product portfolio, which is growing and with addition of new product opportunities that continue to grow further.

We have implemented various strategies to ensure uninterrupted supply and maintain normal operations despite COVID surge in various parts of the world. We are continuing to maintain



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leadership position in our core products. Our top generic products continue to grow. This growth is primarily driven by volume despite pricing pressures. INR 275 crores has been capitalized for the first 9 months of this financial year. We have a capital work-in-progress of about INR 575 crores as at the end of the quarter.

We would like to inform you that the Unit 3 facility near Kakinada has received the necessary clearances from government officials and we are prepared for the prospective development of the same. We are currently finalizing the plan and we will give you an update in the coming quarters.

We are happy to report that Divi's has continued to operate responsibly and make a positive impact in the communities where our business operates. During the last quarter, we implemented various CSR and sustainability initiatives, including infrastructure improvement in the areas surrounding our manufacturing facilities, which benefited thousands of people. With that, I'll hand over to Ms. Nilima to share some operational and financial highlights of the quarter. Thank you.

Nilima Divi:

Ladies and gentlemen, a very good afternoon to all of you and thank you very much for joining us today to discuss the results for the third quarter FY '23. I hope that everyone, along with your friends and family is in good health.

Considering the operational front, we had no disruptions to our customer shipments during the quarter and we are operating with a commitment to fulfilling all our customer requirements on time. The global logistics scenario showed improvement with respect to sea and air freight costs during the quarter. However, minor disruptions in matters pertaining to manpower shortages continued and we are being cautious about inbound and outbound logistics management to keep our operations smooth and meet our customer commitments.

Raw material procurement and availability have been stabilized and the material prices have slightly softened compared to the last quarter. However, the prices for some base metals like lithium and iodine have increased over the past quarters and we are expecting this trend to continue. We also continue to monitor the ever-changing energy situation. With a strong and reliable supply base and inventory control, we are confident in facing challenges that may come our way.

As the world continues to change, our team stays vigilant. We are mindful of the global developments, tracking geopolitical tensions and energy prices. We are diversifying our supply base and working to mitigate risks, so that we can keep our customer shipments on track and our supply chain stable.

I would now brief you on financial performance for the third quarter of financial year 2022-23. We have achieved a consolidated total revenue of INR 1,822 crores for the current quarter as against a revenue of INR 2,510 crores for the corresponding quarter of previous year. Material



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consumption for this quarter came to be about 43% of the sales revenue due to change in product mix. Profit before tax for the quarter amounted to INR 436 crores. Our effective tax rate for the quarter is 29%. We have a profit after tax of INR 307 crores for this quarter. For the 9-month period, we have a consolidated revenue of about INR 6,100 crores and profit after tax of INR 1,502 crores.

Exports for the quarter continue to be around 87% and export to Europe and America is about 69% of our revenue for the quarter and 70% for the 9-month period. Product mix for generics to custom synthesis is 55% and 45% for 9 months and it is 60% to 40% for the quarter. We have a forex gain of INR 47 crores for the quarter and a gain of INR 134 crores for the 9-month period. As we have a lower sales revenue during the quarter, our constant currency growth for the quarter has been negative 40%, while it has been negative 17% for 9-month period. Our nutraceutical business amounted to INR 160 crores for the quarter and INR 509 crores for 9 months. As of 31st December, we have cash on books of INR 3,849 crores, receivables of INR 1,659 crores and inventories of INR 2,981 crores. Thank you.

- M. Satish Choudhury:** Thank you, Madam. With this, we would request the moderator to open the line for Q&A.
- Moderator:** The first question is from the line of Tushar Manudhane from Motilal Oswal Financial Services.
- Tushar Manudhane:** Yes. First on the gross margin thing -- so the kind of product mix that is there. So is it softness in gross margins to look for going forward and which is significantly down if we look at the historical trend rate, if you could elaborate on that?
- Nilima Divi:** Could you please repeat the question again?
- Tushar Manudhane:** The gross margin for the quarter has been significantly lower, while you alluded to the change in product mix being one of the reasons. But if I look at it the historical trend rate, it has been significantly down. So again, considering the product mix should the 3Q gross margin to be taken as a sustainable rate going forward? Or is - there more one-off or inventory write-off for the quarter?
- Dr. Murali K. Divi:** It will improve in the coming quarters. It so happened in this quarter, the raw material prices have gone up and there were pressures on the sales prices of the API. And we anticipate in the coming quarters, it should be better. There should be a growth and also a profitability growth. And also, I think you said gross, even when it came to the net, because of the high tax rate of 29%, EPS impacted naturally the profit after tax.
- Tushar Manudhane:** Sir, and secondly, if you can highlight further in terms of the role played by Nilima madam and Kiran sir in terms of given -- in terms of shifting of gears of growth in the second generation?
- Dr. Murali K. Divi:** Somehow, the voice is not clear. Can you please repeat?



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Tushar Manudhane: Yes, Sir, my question was, while considering your age and considering the second generation also into the business, Nilima Madam and Kiran, so would like to understand in further details in terms of the roles taken up by each of this and how to look at this going forward?

Dr. Murali K. Divi: I think the roles are clear that the finance, accounting, the material purchases or supply chain management will be done by Nilima. The production planning, marketing, sales, technology development what we call R&D will be handled by Kiran S. Divi. It is also being followed like this has been happening for the last 5 years. They both are heavily involved. And I just foresee the new products, new pipelines, new chemistries, what else can be introduced, like the vapor-phased chemistry, continuous flow chemistry, photochemistry, gadolinium compounds, peptides, these are the new chemistry. I am trying to see what can be introduced in addition to the regular generic custom synthesis. That's all being handled by both Kiran and Nilima and we are also having the professionals who are experts and who have been with us for a number of years.

Tushar Manudhane: And just lastly, if I -- so when do we expect Kakinada basically the construction to sort of start or, let's say, over the next 12 to 15 months, how much money you plan to invest at Kakinada?

Dr. Murali K. Divi: Finally, after 5 years since we started the first attempt to start our work in Kakinada, we got all the clearances and the land of 500 acres is handed over to us, the project planning is under progress, products planning, some of them are starting materials, some of them are intermediates, some of them are APIs. And an investment of about INR 1,000 crores and I think we will update in the very near future because we have been handed over the land in the last couple of weeks. So we are protecting the land by constructing the wall around. We have moved the teams, construction teams and fabrication teams. So the whole...., I think we will be updating in the coming -- going forward.

Moderator: The next question is from the line of Prakash Agarwal from Axis Capital.

Prakash Agarwal: Sir, trying to understand, definitely the product mix has changed, the generics has gone up. But within generics, is there a pricing pressure that you are seeing because this kind of gross margin and EBITDA margin we have never seen before. I mean, we have -- you've talked about raw material pressures in the past. But is it more related to pricing in the generics that you are seeing or that is fairly stable?

Dr. Murali K. Divi: It is mainly from the generic compounds where we have seen the price pressures, because during the COVID, several of the companies probably with generics did not get opportunity to sell. Now the growth is there, but there is price pressure. So -- but going forward, we see the price pressure will ease up and probably the raw material prices also may ease up; and come down. We are seeing that so the profitability should increase. We cannot compare with the previous 5, 6 quarters, where we had exceptional opportunity. We used the speed, took challenges and executed. So it resulted in the upside during the last 6, 7 quarters, the anti-COVID drug. But if



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you see the pre-COVID business, I think we are seeing normal growth in the coming quarters and profitability should improve quarter-on-quarter.

Prakash Agarwal: Okay. Just one point on the generics. So you mentioned there is some pricing pressure, but you're also saying that you would see pricing to improve. So what gives us confidence? Are we seeing it already? Or I mean, what gives us the confidence that generic pricing will improve?

Dr. Murali K. Divi: We are already seeing the prices improving and also the volumes improving. In several of the generics, we have seen even a 50%, 60%, 70% of volumes improving. Naturally, when volumes improve, prices also improve. There is a change and also our new generics and the contrast media, where there are no price pressures, I think we should look better in the coming quarters.

Prakash Agarwal: Fair enough. And secondly, sir, given the cash pile we have, are we considering any large buyout, especially in the contrast manufacturing side, injectables, something like that?

Dr. Murali K. Divi: We are not planning to buy any injectable or anything like that. We are planning to invest in new technologies, as I mentioned few minutes ago in the vapor-phased chemistry, continuous flow chemistry, photochemistry and in some of the newer compounds called Gadolinium compounds, which are the MRI contrast media agents, where we already developed process, we are trying to tag with some big name people in that. And again, the large interest in the peptide building block and there is good demand in the expanded contract media business. I think we are going to be very busy in the coming 6 to 8 quarters in implementing all these projects.

Prakash Agarwal: That's great to know. Lastly, on the Kakinada, you said INR 1,000 crores yet to be invested or within the CWIP, what is the share of Kakinada, sir?

Dr. Murali K. Divi: We have planned Kakinada almost in the last 5 years, at least 5, 6 times as if we are going ahead, but there was always a road block not getting the full clearances. Now we got full clearances, based on our current requirements or demand for starting materials, intermediates and API, we are grouping them and creating the infrastructure or utilities, and I think in the next quarter, 2 quarters, we should be totally -- the project should be going to full swing of construction.

Prakash Agarwal: The INR 1,000 crores is the capex we want to do going ahead?

Dr. Murali K. Divi: That is what we plan initially, a INR 1,000 crores investment as a Phase 1 because we waited long time, we have substantially invested in both Unit 1 and Unit 2. Those projects where we invested in the new blocks, they are getting occupied, validations being completed and commercial production will be starting. Some of them just started. Some of them are planned in a phased manner, as we get regulatory clearances. So we don't immediately need such capacity, but we see post these capacity requirements as we have the new projects coming in.

Prakash Agarwal: I understand, sir. I was asking on the INR 575 crores CWIP how much is Kakinada? That's what I wanted to understand.



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- Dr. Murali K. Divi:** Kakinada is not in that INR 575 crores, it's a small amount that is there in the -- it is in the existing SEZ and EOU that is where the investment is.
- Prakash Agarwal:** Okay. Which will give us more capacity in the near to medium term?
- Dr. Murali K. Divi:** Yes. I think in the growth engines, I have described about, that some of the big CS projects, some of the products where they're expiring, some of the sartans, we have been -- we planned with 3, 4 quarters ago, that is what is the work in progress, CWIP.
- Moderator:** The next question is from the line of Damayanti Kerai from HSBC.
- Damayanti Kerai:** Sir, can you update us on your progress in the iodine-based contrast media projects, which you are working for few last quarters? When we are expecting notable sales to come from these products?
- Dr. Murali K. Divi:** Yes. I think going -- as I mentioned in the last quarters that projects are under implementation. Now 2 of the products are our own generic products. And the contrast media where we are doing custom synthesis, that project is already implemented. The quantification is done. Now we just entered into commercial production and you will see good numbers in the Q1 2024 onwards by which time all the regulatory clearances would happen. And the strength again, I would stress that is the capability of iodine recovery to the maximum, where it used to be \$25 per kilo, it is \$75 a kilo. Also, we have excellent relationships with the customers as well as the big pharma where this contrast media are being used.
- Damayanti Kerai:** Okay. So just to clarify, by first quarter of FY '24, you should be starting commercial supply, both for the custom synthesis project as well as for your own generic, right?
- Dr. Murali K. Divi:** That is correct.
- Damayanti Kerai:** Okay. Sir, my second question is on demand scenario for overall generics portfolio. So you mentioned that you are seeing good volume for some of the products where 50%, 70% increase has come on demand side. But on very broad basis, are you seeing a recovery in demand from the customer for some of the base generics, which are like large product for you?
- Dr. Murali K. Divi:** Yes. We are seeing a double-digit growth in some of the generics, that's the minimum. And the products are expanding as well as the customers who probably were -- some of the customers who are buying from elsewhere probably have issues and that's where we are also getting a lot of demand from.
- Damayanti Kerai:** So in coming quarters, we should be expecting better volume growth on the generic part of your business?
- Dr. Murali K. Divi:** That's correct.



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- Moderator:** The next question is from the line of Ashish Thavkar from IIFL Asset Management.
- Ashish Thavkar:** Sir, you mentioned about Gadolinium compounds. And I believe you're also on the iodine contrast media. So given that this is a \$7 billion market globally and market is growing at 10%, what kind of say are we -- will we be having in this entire market? How are we planning to move ahead with the commercialization of the molecules?
- Dr. Murali K. Divi:** There are not many customers who would consume the contrast media, both iodine compound, gadolinium compounds. There are only a handful in the whole world. And with the majority of them..... we are discussing for long-term agreement for supply of these APIs.
- Ashish Thavkar:** Okay. So it's not intermediate, but you will be directly into APIs. So that's a fair understanding, right?
- Dr. Murali K. Divi:** In most of the cases, they are direct APIs. In few of the cases, they are like N minus 1, N minus 2.
- Ashish Thavkar:** Okay. Sir, but would it be fair to assume that some of the bigger names, they would also be doing in-house, are they willing to shift the entire like 7 to 8 step process to us? Is that a fair way to understand?
- Dr. Murali K. Divi:** I wouldn't say that they will shift the entire..., but we will get a decent portion of the business, either a part of the.... see, the contrast media is growing in the world at the rate of a minimum of 10%. And each of this contrast media is there about 2,500 to 3,000 tons. Every year, they need about 300 tons extra quantity. So in the last couple of years, if we count, they need about 600 to 1,000 tons planning for the next 4 years.
- So that is the kind of opportunity we are looking at, number one, get some quantities from the existing market. And going forward, instead of these big pharmas expanding, we'll be expanding in India, number one. So with reference to these new gadolinium compounds or other compounds where they are used for MRI and also some of the newer ones, we are looking at supplying the N minus 1 N minus 2.
- Ashish Thavkar:** Okay. Sir, last question on the new pipeline, the NCE-based molecules that we spoke about in the second quarter commentary, you said there are like a couple of projects which are there and could see FY '24 launch. Any update on those lines would be helpful.
- Dr. Murali K. Divi:** That's right. This is the sixth growth engine where there's a \$20 billion products expiring between '23, '25. Yes, we have submitted for some of them drug master files, some of them are getting ready to be submitted. So as soon as the customers have sampled, customers have purchased some quantities for their formulation purposes and stability study to submit to the FDA. And I think going forward, it looks good as and when the patents expire, I think we should have the opportunity.



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- Ashish Thavkar:** Okay. So you're confident of FY '24 launch?
- Dr. Murali K. Divi:** '25 for sure. Even if it starts in '24. I don't think on day 1, we'll get very big volume. But in '25, we should get good volumes.
- Moderator:** The next question is from the line of Neha Manpuria from Bank of America.
- Neha Manpuria:** Okay. Sir, could you give us some color on the extent of pricing pressure that we've seen in the quarter? And also just trying to understand the gross margin a little better. Is there some impact from, let's say, high-cost inventory for raw materials that we used in the quarter as raw material costs are coming down, we could probably see improvement in gross margins. Is that one of the factors that we should consider?
- Dr. Murali K. Divi:** Yes, one of the factors could be that. If you recall in the last 2 years, I think some of the raw materials, how I think the prices went up by 2x, just Nilima was mentioning a while ago on the lithium, the same thing goes for several other materials where we have procured them at high prices and some of them still we are procuring at high prices. And we see now a drop in prices, or at least price pressures are just coming down. So across industry, I think people faced the price pressures. Now it's loosening and we should expect better margins in the coming quarters.
- Neha Manpuria:** And sir, what about the API price realization decrease, how much would have been on an average, let's say, over the last year or quarter-on-quarter? If you could give us some color?
- Dr. Murali K. Divi:** It is surprising that several of the API.... some of the APIs had price pressures where the prices came down by 5%, 10%, whereas some of the APIs where we just entered, we were able to maintain good prices and even prices have gone up, depending on, I think, how many suppliers are there. I think what will happen finally is that if there is a supplier who would continuously supply without interruption and maintaining the quality, I think customers have no choice but to buy from them. So that's where we see that we are positioned and we should be able to get better prices.
- Neha Manpuria:** Sir, is the API realization pressure more on the older products that we are selling rather than the new launches? Is that a fair assessment?
- Dr. Murali K. Divi:** I think if I have to say that I would say it is across portfolio, but naturally, in some of the new products, there could be a little more pressure depending upon how long several people have been with stock, waiting when they may disappear after the stock is being disposed into the market. Then the prices will stabilize.
- Neha Manpuria:** Understood. And sir, on Kakinada, now that we are starting work, by when should we start seeing the facility being ready for, let's say, validation, regulatory approvals and eventually, commercial production? Would it be more 2 years, 3 years? What sort of timeline should we look at?



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- Dr. Murali K. Divi:** I think we should be able to look in 2 to 3 years, any time after 2 years.
- Neha Manpuria:** Commercial production or validation?
- Dr. Murali K. Divi:** No. These are two things. I think I said that we'll be doing some starting material with the difficult chemistry, some advance intermediates and some APIs. For API, definitely initially, we'll be selling to the other markets while we are qualifying for the regulatory market. But the raw material, starting materials and intermediates, we should be able to consume them for our existing products to increase our further capacity.
- Moderator:** The next question is from the line of Surya Patra from PhillipCapital.
- Surya Patra:** I just wanted to understand the pricing situation in the APIs and intermediates better. So is it anything to do with the China open-up or it is a good correction or inventory rationalization, now what we would be seeing post the strong demand situation during COVID, few quarters that we have been witnessing? So anything to do with that, the current price situation that we have within for the APIs and intermediates?
- Nilima Divi:** Can you just repeat the question again, please?
- Surya Patra:** Yes. So just to understand this price erosion or price correction in the API, I'm just trying to understand whether this correction what we are witnessing in suddenly in this quarter is because of the China open-up scenario, what we are witnessing, is that -- or the recent crash or the sharp correction in the crude prices that we have witnessed? Or that we are witnessing any kind of inventory rationalization situation at the customer's end, after seeing a kind of inventory buildup situation during COVID over last many quarters? So what is really impacting these prices because we have not seen this kind of a broad-based price erosion in case of APIs in many of the names.
- Dr. Murali K. Divi:** The pricing pressures, I think it's not only with us, it is across the industry and across products. Now yes, you are right that the pre-COVID, during COVID, post-COVID, there is a difference in the consumption of the therapeutic segment and now slowly therapeutic segments are coming back. So we don't know the real stocks at each of the either API manufacturers or dosage manufacturers, but we felt the pricing pressures. I'm sure everybody is feeling across industry. And we see the raw material prices getting better right now what contracts we are entering. So we expect that in the coming quarters, not only we have the volume growth, I think we should be having a profitability growth as well.
- Surya Patra:** Okay. And sir, in fact, the margins for the quarter is the lowest ever. And this is not because of the gross margin slippage. It is also because of the spike in the other expenses. So there also, what is that has that, whether it is the energy cost element or it is the freight cost one? What is really has -- see, can you tell, sir, what is the share of this freight cost element in your overall cost?



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Dr. Murali K. Divi:

I think it is not just one. I think one is the planned maintenance costs went up because several of the buildings or several of the utilities, we built them in the 1995, we started implementing rebuilding some of those plants, material plant structures. And also, we have invested heavily in replacing some of the old safety systems with new safety systems. You must have heard recently popping up here and there, few accidents. And we are making sure that we are removing all those old pipelines, old electrical cables, which we installed in the early years. That's probably one of the reasons. Two, also, you must have seen the taxation went up. When it comes to the profit after tax, the tax was it used to be 15%, 18%, this is the highest, I think, 29%, 30% almost. That's what we have paid tax.

Surya Patra;

Okay. Sir, just if I try to ask slightly differently, let's say, the sequential 10% correction in the margin, what we had witnessed, what portion of this would be quarter-specific for this quarter, which may not be there in the following quarters, either because of the improvement in the pricing scenario, or few of the cost element which will be there, like maintenance and all that? So this is really a lower number and this is a big negative surprise to the streets. So that's why I'm trying to understand a bit more better.

Dr. Murali K. Divi:

I think we are -- after we have seen the COVID drug, where we have high margin, high productivity where we achieved, coming back to the pre-COVID production schedules, all modifications and getting into the new -- utilizing those -- some of those assets, the reorientation, reorienting them to make the current again generic products or these products, this is where some of the costs went into them and fully geared up and we should be able to see not only double-digit growth in terms of business, but also profitability.

Surya Patra:

Sure, sir, just last question about the new capacities what we had added both in the 2 sides, so around 15-odd units that we had added incrementally over the last 1.5 year period. So out of that, what -- how many of those units are underutilized or it's not been utilized so far or commercialized so far? What is the kind of spare capacity that is there and how long the spare capacity can ensure our growth momentum going ahead?

Because this quarter, there is no problem in the revenues. But is this the margin which you are saying that it would be improved subsequently? So just about the revenue growth visibility. So what is the spare capacity that we are having? Will that be sufficient enough to drive grow till the time the Kakinada facility reaches commercialization?

Dr. Murali K. Divi:

Currently, we are occupying about 75% to 77% of occupancy, at least 20%, 23%, 25% of free capacity. So going forward, as we -- the growth engines where we said that the future growth engine is 6 and the sartans engine and capacity increases where we have done... the qualifications being either completed or getting completed, regularly the agency clearances has been awaited. I think all this -- I think I mentioned in the last quarter and before quarter, earlier quarters also, it will take about 2 years to get into the full benefit out of them. So we have enough capacity for all that and we need not worry about that.



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- Moderator:** The next question is from the line of Shyam Srinivasan from Goldman Sachs.
- Shyam Srinivasan:** Just looking at 3Q and comparing 3Q '23 to 3Q '21, so December 2020, most of the numbers are absolutely the same, like look at generic API, custom synthesis, nutraceuticals. So my question was, historically, Dr. Divi, we had like a 10% growth coming through on and then.... removing all the 5, 6 quarters that you talked about, which have got, say, COVID drug Molnupiravir benefits. And just looking at like a 2-year, so that growth has not happened, right? There's been no 10% growth even on that base portfolio, excluding all that. So if you could disaggregate and say, is that underlying that business, has it seen volume growth and all the volume growth has been taken away by price? Would that be one way of looking at it?
- Dr. Murali K. Divi:** The volume growth has happened and is happening and we are foreseeing that it will continue. I think double-digit volume growth, we see -- foresee that it will continue. Now yes, the price pressures were there. That has impacted on the profitability, which we are hoping with the raw material prices being stabilized or going down, not going up. So we should be able to get back to the -- our profit margin on the gross level. On the taxation level, I cannot comment at this moment based on how the project which we planned in the SEZs, how soon they will come into commercial production in terms of clearances with regulatory authority. As and when they happen, of course, you will see the taxation coming down.
- Shyam Srinivasan:** That's helpful. Just following up here. So generic API or nutraceutical, I understand some pricing pressure. But custom synthesis, why should -- that number is also the same, INR 680 crores in 3Q '21 and INR 675 crores this quarter. So just any thoughts there on what's happening on custom synthesis or custom -- that particular line item specifically?
- Dr. Murali K. Divi:** On custom synthesis, it's different. It's not on the profit margin. There is no profit margin issue with that. Now after the -- during the COVID and towards the end of the COVID, end of the COVID just happened in the last 2 months, we all were able to remove the masks and were able to freely work around, whether it is in this country or abroad. But everybody, all the companies had preferences towards to see how good we can push the COVID drug, every big pharma, instead of looking at other therapy segments. Now everybody stepped on the pedal down for every other therapeutic segment products. So we are seeing now a number of projects coming to us from the various big pharmas, multiple opportunities in all therapeutic segments and we don't have any pricing pressures from the big pharma business.
- Shyam Srinivasan:** Got it, sir. So just last question. I don't know, maybe you'll answer this, but will we go back to this 10% to 15% historical growth rate that you have talked about in the past in some time in the future?
- Dr. Murali K. Divi:** Why not more?
- Moderator:** The next question is from the line of Sameer Baisiwala from Morgan Stanley.



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- Sameer Baisiwala:** Can you update us on the fast-track CS projects that you talked about?
- Dr. Murali K. Divi:** There were 2 big fast-track projects. We have completed the projects. We have validation completed for both. Both are in the commercial ramping up. You will see some values in the Q1 through Q4 of our financial year. And the Q1, they should be fully ramping up Q1 up '23, '24.
- Sameer Baisiwala:** Okay. That's great, sir. And this is pandemic-related, non-pandemic-related.
- Dr. Murali K. Divi:** Both are not non-pandemic-related.
- Sameer Baisiwala:** Okay. Got it. And sir, just on contrast media, now that you are getting very close to commercialization, any number that you can share? Is it like INR 100 crores to INR 200 crores opportunity to begin with or any color would be great, sir?
- Dr. Murali K. Divi:** I think it should be bigger. It should be larger because the business is much larger, we are aiming at bigger numbers.
- Sameer Baisiwala:** Okay. Okay. That's good to hear. And sir, just on margin weight, your normalized margins used to be 40%, give or take, and that's where you used to aim at EBITDA margin. You are probably closer to 29% now. So what's the road map for that? You have explained many things and it's going to improve and all of that. But do you think you can get to this number at all? And is it in the foreseeable future? That would be very helpful, sir.
- Dr. Murali K. Divi:** We are not talking about immediately in the next 3, 4 quarters to reach such level. But definitely, it is possible. We are making a lot of efforts with the new chemistry to how to minimize material consumption and how to increase the throughput. So I think we will see in the next 2 years, probably we should be back with such. And we have several opportunities we are getting from the big pharma. So we should be able to again see in the next few years, yes.
- Sameer Baisiwala:** Okay. Great, sir. And sir, can you split broadly qualitatively, custom synthesis business, what percentage is -- or what part is commercial molecules versus how much is contributed by development quantities? I mean, is it 50-50? Or is it skewed more on one side?
- Dr. Murali K. Divi:** We have never disclosed, or given any details on the developmental products for the big pharmas because we we have signed several confidentiality agreements, but it's very good, I would say. We have never seen so many opportunities coming and they'll be implemented in groups. So I think in the next 2 years, these small-volume products will go into the multiple tens of tons or higher.
- Moderator:** The next question is from the line of Cyndrella Carvalho from JM Financial.
- Cyndrella Carvalho:** You had mentioned on last call that regarding the pandemic supplies that we had, we had almost closed those orders for our partner. Our partner has given some more guidance also now. Just wanted to understand from the inventory that we are carrying with us today, do we have anything



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pertaining to this pandemic-related goods with us today out of the INR 2,981 crores that we highlighted?

Dr. Murali K. Divi: We do not have any stocks, whatever we made are already shipped and we don't have any stocks of any API for them. They are shipped as and when made.

Cyndrella Carvalho: That is very helpful, sir. Sir, coming back to the API pricing that we spoke about and the entire recovery that you're talking about, can you help us understand, can we see the reversal of, say, the top line around INR 1,800 crores, INR 1,900 crores in the coming 1 or 2 quarters' time? Or you think it will take 3, 4 more quarters to be at that run -- at the top line. And as soon as the top line comes back, should we expect the margins also to revive to the same extent?

Dr. Murali K. Divi: I don't want to say quarters, but definitely we are on the way, a double-digit growth and double-digit growth also reflects for both for the sales as well as profitability. And going forward, I think we talked about all the six growth engines and they should be able to see as to not only get back to the pre-COVID, but I think further way head.

Cyndrella Carvalho: Okay. But sir, in terms of... if we try and understand, you are seeing improvement in the volumes on the generic side as well as on the price side should follow. And you're saying that there will be a custom synthesis project also which could start shipping in Q4 and we will see maybe 1Q FY '24, we'll see a full quarter. So in the light of these two comments, how should we see? If you can help us understand qualitatively, we will also do not... on a number perspective entirely, but that's because the numbers have been fairly moving up and down because of pandemic supplies, so just want to understand some clarity there.

Dr. Murali K. Divi: Going forward with the two big custom synthesis projects, where their contribution will be seen a big potential from the Q1 of 2023 to '24. And I think with also our generic with a double-digit growth, I think we should see a good growth. We don't want to say anything about the custom synthesis or generic, separating them. But I think overall, the growth should be there and also increase in profitability.

Moderator: The next question is from the line of Chirag Dagli from DSP BlackRock.

Chirag Dagli: Sir, quarter-on-quarter, the mix is not very different. Custom synthesis business is 40% this quarter versus 43% in the second quarter. Despite that, our gross margins are down almost 7 percentage points. Two questions there. Why is that? You talked about product mix being different. So if you can just give a little more color around why this large 7 percentage point Q-o-Q dip in margins? And is this across both the pieces, generic as well as custom synthesis? Or is this more to do with generic business?

Dr. Murali K. Divi: I think we have made it in the past very clear that they were the onetime opportunity. With that -- we didn't -- though we should not wish that the COVID should be there and APIs should be consumed, the profit margin, our profitability as the anti-COVID drug was definitely a better



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one. And when it was there in those quarters and normal in the quarter just we went through minus COVID drug. I think this is where we are with the pricing pressures on the APIs and also on the increase in raw material costs, which I have explained that going forward in the coming quarters or year, we should be able to get back to the normal mode and growth model without the COVID drug.

Chirag Dagli:

Sir, is generic gross margin more impacted than custom synthesis gross margin?

Dr. Murali K. Divi:

Yes, the custom synthesis, the impact is less because there is no pricing pressure from the customer. It's only the raw material prices probably some of them went up, some got compensated, some did not by the customer, whereas in generics nobody will compensate you for the increase in raw material prices when the generic APIs more are available, if they aren't.

Moderator:

The next question is from the line of Sayantan Maji from Credit Suisse.

Sayantan Maji:

So I just wanted to understand what was the proportion of sales from US and Europe? And do we see the pricing pressure in these markets? Or is it mostly in the US market that you're witnessing this?

Nilima Divi:

Can you repeat the question again, please?

Sayantan Maji:

Yes. I just wanted to understand the proportion that you mentioned in the opening comments on the US proportion of sales coming from US and Europe and exports and the generic pricing pressure that you're observing, is it in the US or the Europe market?

Dr. Murali K. Divi:

The export to Europe and US is about 70% of our revenue for the quarter and 70% for the 9-month period. So between the Europe and US, we don't differentiate because the orders come from Europe and we ship to US, the orders come from US, we ship to Europe. So we don't differentiate much. And there are no price pressure differences between Europe US. I think the difference is not there, but overall, there can be little lower impact in the regulatory market and of course, in the non-regulated market is much like the pressures are more.

Sayantan Maji:

Okay. And what would be the proportion of export sales for this quarter?

Dr. Murali K. Divi:

Exports accounted to 87%.

Moderator:

The next question is from the line of Naushad Chaudhary from Aditya Birla Sun Life.

Naushad Chaudhary:

Two clarifications, sir. Firstly, on the CSM business side, can you explain us what is your pricing policy here? And typically, how often you revise your prices, annually, 6-monthly and in which all months it is noted as... Price revision policy in CSM business?



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- Dr. Murali K. Divi:** The pricing policy, it's not the revision of pricing policy. It is being discussed with the customers and see what is happening in the market on a quarter-on-quarter basis. Usually the contracts are over long period of time and some of them are discussed when the pricing pressures are more from the customers. But usually, on a quarter basis, we will discuss, but there's nothing like pricing policy on quarterly basis. It's driven by demand and supply from the customers.
- Naushad Chaudhary:** Okay. Secondly, on the operating deleveraging side, sir, is there any challenges we are facing on the operating leverage because of the infra we had created for the COVID-based product, is that creating us a -- giving a cost load to us on the balance sheet on the P&L or is it forcing us to do some low-margin product and that's why we are facing the challenge currently?
- Nilima Divi:** Well, at this point, what we see is... as the sales increase and the growth is driven more by the profit and the normalcy comes back into place, we would say that we've got the leverage would be more favorable.
- Moderator:** Ladies and gentlemen, this was the last question for today. I would now like to hand the conference over to Mr. Satish Choudhury for closing comments.
- M. Satish Choudhury:** Thank you, all, as for joining us today for the earnings call of Divi's Laboratories Limited. In case you need any clarification, please reach out to our Investor Relations. Thank you.
- Moderator:** Thank you. On behalf of Divi's Laboratories Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.