"Laurus Labs 4QFY21 Earnings Conference Call Hosted by Ambit Capital Private Limited"

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MODERATORS: **MR. NIKHIL MATHUR – AMBIT CAPITAL PRIVATE LIMITED**
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Moderator: Ladies and gentlemen, good day and welcome to the Laurus Labs Limited 4QFY21 Earnings Call hosted by Ambit Capital Private 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 phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Nikhil. Thank you and over to you sir.

Nikhil Mathur: Yes, hi, thanks a lot. Good morning, everyone. On behalf of Ambit Capital, I thank the Laurus management for giving us an opportunity to host the 4QFY21 Earnings Call. Today, on the call, we have Dr. Satyanarayana Chava -- Founder and CEO and Mr. V. V. Ravi Kumar -- ED and CFO.

I now handover the call to Dr. Satya for his opening remarks. Over to you, sir.

Dr. Satyanarayana Chava: Thank you, everyone, for joining us for 4Q and Annual Results of FY21 Conference Call. We are pleased to have this opportunity to update our progress and answer your questions. We hope everyone and their family members, colleagues and friends are safe during this severe second wave of COVID pandemic.

To begin with, we will share the "Status of our Locations." Our manufacturing units, R&D center, corporate office all functioned normally during the FY21. At Laurus, we are committed to protecting the health and wellbeing of our employees and their families. We continue to implement rigorous safety and hygiene measures across all locations without any compromise. I am extremely proud of the agility and resilience of our teams have shown in the phase of this challenge since last year. I am very thankful to all our colleagues for rising to this challenge and ensuring business continuity. Our performance focus is on growth, driven by excellent execution and creating a platform for our future growth with manufacturing capacity expansions, a combination of Brownfield as well as Greenfield in API, formulations as well as Custom Synthesis divisions.

In FY21, we have established a wholly-owned subsidiary, Laurus Synthesis Private Limited to take care of contract manufacturing for big pharma and also incorporated another step-down subsidiary named Laurus Ingredients Private Limited. These initiatives will bring focus to our contract manufacturing division to allocate, create, offer increased capacity to service customer needs. We believe by the end of FY23 this division, Laurus Synthesis, will be self-reliant in all respects.

We have forayed into biotechnology space by acquiring a majority stake in Richcore Life Sciences Private Limited, which was renamed as Laurus Bio. The current promoters will continue to run the operations. And this equation gives us entry into fermentation capabilities as well as foray into recombinant proteins. In the medium-term, what we expect this division to be vertically integrated into offering a contract development and manufacturing services in biotech space.

We're happy to share that in FY21 Laurus Labs has done exceptionally well; our 4Q revenue stood at Rs.1,412 crores, showcasing a robust growth of 68% year-on-year and for the whole year, we have achieved Rs.4,813 crores revenue with a growth of 70%.

To begin with, we would like to share the "Key Updates on our Various Segments." In the Formulations division, we achieved Rs.1,664 crores for the year and in the current quarter, we have done Rs.430 crores revenue. The revenue contribution from the formulations division for the whole year is about 35%. Recently, we also got an approval for a triple combination anti-retroviral drug containing Tenofovir, Alafenamide. We are in the process of obtaining in-country registrations. We already got orders for this triple drug combination and we expect to service those orders in the first half of FY22. Apart from LMIC business, we are also seeing growth in developed markets in North America as well as in the Europe.

To leverage our front-end US business, we have commenced the marketing of in-license products. Out of five in-license products, two products were launched, and we are in the process of launching the rest of the products in the next six months. We have a total of nine final approvals and eight tentative approvals out of the 26 ANDAs filed so far. In Canada, we have eight approvals and four launched and two more products will be launched soon.

For EU, we have validated additional products as part of the contract manufacturing with our partner and we expect significant upside from these products in FY23. We also obtained approvals and marketing operations for five products; two of those launched and we are in the process of launching others shortly.

As we informed, we continue to invest in strengthening and enhancing our formulations infrastructure. Capacity expansion through debottlenecking was operational and already commercially used right now. Our Brownfield expansion on the same site with similar capacities will become operational in a phase manner from October 2021 and will be fully operational by end of FY22. On the R&D front, we continue to invest about 4% of our revenue.

In the Generic API division, this year was very good for our anti-retroviral APIs; we have achieved Rs.1850 crores API sale in anti-retroviral, this was the highest ARV API sale so far. And second line ARV APIs also continue to see healthy sales in 4Q. Due to the increase in the demand for third-party API sales, we are still expanding the API capacity to serve the existing demand from the customers. We expect to maintain good sales for ARV APIs in FY22 as well.

In oncology segment, we recorded a 5% growth in the current quarter over corresponding quarter. As you are aware, Laurus Labs has one of the largest high potent API capacity in the country. And we are expanding high potent API manufacturing capabilities in one of our units, unit-4 at Atchutapuram. We expect oncology business to grow fairly well in the coming quarters as well.

The most important days is our contract manufacturing of generic APIs and non-ARV, non-oncology. We have seen a healthy growth in 4Q, and we have initiated validation of several APIs, non-ARV, non-oncology and we are adding additional manufacturing capacities for these products. So, our diversification efforts in generic APIs will be very visible in FY23 as these capacities are commercially utilized.

In the Synthesis division, we recorded a growth of almost 20% from 4QFY21 for corresponding period. We have achieved a sales growth of over 35% in FY21 when compared to FY20. We are pursuing several active projects in the late-stage clinical programs as well as the commercial supplies of four products which are ongoing.

Construction activity is in progress at the dedicated CRAMS R&D at Genome Valley, Hyderabad.

We have also acquired land for new manufacturing Greenfield site at Vizag which will cater to the manufacturing needs of this division for the next four to five years.

We are also in the process of acquiring an additional land for the division to manufacture steroids and hormones, high potent molecules. That land will be at Harwada, very close to our existing manufacturing facility.

When it comes to Laurus Bio, we have closed the transaction to acquire majority stake in Richcore in the month of January. And Laurus Bio is on the course of commissioning a large scale fermentation capability, 180,000 liters in the next two weeks. We are also planning to acquire additional land for further expansion of our Laurus Bio by creating close to million litres fermentation capacity.

With that I would like to hand it over to “Ravi to share Financial Highlights.”

V. V. Ravi Kumar: Thank you, Dr. Satya, and very warm welcome to everyone. I wish and pray god that everyone is safe at your home and your offices.

Let me quickly take through some of the highlights. Income from operations for the quarter is at Rs.1,413 crores with the 68% growth. For the full year, we did about Rs.4,814 crores, growth of 70%. With a better product mix, gross margin improved significantly; now, it is a 55% gross margin. Our EBITDA is one of the best achieved so far is 34% for the Q4. Our diluted EPS for the quarter without annualization is Rs.5.5, whereas our annual EPS for the full year is Rs.18.30. Our ROCE is 40% on annualized basis due to operational leverage and higher asset utilization. On the CAPEX front, we have incurred around Rs.700 crores, which includes the capital workin progress. Out of this CAPEX, we have invested 50% into the APIs, around 30% in FDF and 20% for Synthesis and Bio and way forward in the coming periods we will be spending the similar ratios. And what we are expecting is CAPEX in the next two years will be Rs.1,500 crores to Rs.1,700 crores. So, why we are giving a two-year guidance is there will be spillovers from one year to the other.

We have incorporated in step-down subsidiary for our Laurus Synthesis. Probably in the next two years' time we are targeting to have an independent Synthesis company, where it has its own production, R&D and business development… of course, business development is separate already, so, it will be very independent business unit.

We want to have an integrated player as we were and that is the reason we are investing into the backward integration; we are investing in intermediates and APIs. That is the reason 50% of the CAPEX is getting into the API side.

We acquired a second site for our formulations in Hyderabad already. We have not yet started the activities, but we will start in the coming year.

So, based on the performance of the company we have declared a third interim dividend of 80 paise per share. So, with this in all three interim dividends together, it is coming to Rs.2, it is like a 100% dividend first time your company is being offered.

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

Moderator: Thank you very much. We will now begin the question-and-answer session. First question is from the line of Dhaval Shah from Girik Capital. Please go ahead.

Dhaval Shah: A couple of questions from my side. So, firstly, on the CAPEX, just want to clarify, you mentioned Rs.1,500 crores to Rs.1,700 crores over FY'22 and FY'23?

Dr. Satyanarayana Chava: You're right, that is the plan as of now to invest an additional Rs.1,500 crores in FY'22 and FY'23 put together.

Dhaval Shah: From the last two concalls what we have mentioned, is there an increase in the amount?

Dr. Satyanarayana Chava: We have increased the CAPEX based on visibility what we have in the API division as well as Formulations division based on the estimated approvals. And also, we are also investing significantly into Custom Synthesis, based on certain projects we need to execute at a new manufacturing site depending on the volumes. So, we have increased CAPEX by around Rs.500 crores than what we have indicated earlier. That increase is based on the visibility what we have right now from the customers and projects what we are handling.

Dhaval Shah: Yes, it was Rs.1,100 crores before?

Dr. Satyanarayana Chava: Yes, yes.

V. V. Ravi Kumar: Partly added from the Bio also.

Dhaval Shah: Bio, how much you will be allocating?

V. V. Ravi Kumar: Bio this year around Rs.60 crores.

Dhaval Shah: FY'22 will be Rs.60 crores Okay. But majority is coming from APIs, the new…

Dr. Satyanarayana Chava: I would say if we wanted to put order of investment, the majority will go to API and then next to our CRAMS division and then Formulations.

Dhaval Shah: Sir, the question on the segmental numbers. Now in Formulations, we did around Rs.430 crores. I believe there was some debottlenecking done. So, is the impact yet to be seen in the number because we are flat quarter-on-quarter?

Dr. Satyanarayana Chava: Debottlenecking operation was completed in the month of March and qualifications were done. That came into commercial use only in the current month April. So, that will be used in the first two quarters and from Q3 onwards we do expect significant increase in our formulations capacity because we will be using the very large-scale new building by October.

Dhaval Shah: Under the API and the others category, you have seen a big traction like Rs.166 crores quarterly run rate now. So, any one-off in this or how should we look at this number?

Dr. Satyanarayana Chava: When it comes to the other API, it consists of contract manufacturing of generic APIs to other generic customers. So, this segment you have to see as a whole year rather than quarter-to-quarter. This year FY'22 and FY'23 most of our CAPEX in API division is for non-ARV, non-oncology. So, non-ARV APIs will see significant sales increase partly in FY'22 but big jump will come in FY'23.

Dhaval Shah: So, you mean like we did around Rs.500 crores in the other category for FY'21. Now, this number should significantly increase in 2022 and more than 2023?

Dr. Satyanarayana Chava: Yes.

Dhaval Shah: In today's article and newspaper that China has reduced or stopped the cargo planes to India. Now, how is the impact you read for the pharmaceutical company in the current time when you have to meet demand, a lot of like pandemic-led demand, also plus our exports demand, so, is there a big impact on us, still we depend a lot on China for KSM, couple of intermediaries, APIs?

Dr. Satyanarayana Chava: We do depend on China for our starting materials, which generally we get through sea shipments. Intermediary people do get by air, but most of our shipments come by sea. We have not seen any impact of the logistics challenges. The one thing is logistics costs have gone up in the recent past. Other than that, we have not seen any disruption which is going to affect our manufacturing in the near future.

Moderator: Thank you. The next question is from the line of Sudarshan Padmanabhan from Sundaram Mutual Fund. Please go ahead.

Sudarshan Padmanabhan: My question is to understand this investment that you are doing in non-ARV both with the FDF and the non-FDF coming together. You have given fair amount of threadbare description on the CDMO, CRAMS business. And I understand that we are looking at almost 50 active projects and four projects almost at commercial level. We are also developing fair amount of strength in hypo as well as chiral chemistry. So, from the current level of say, Rs.500 crores, Rs.600 crores, say in the next two to three years, where do we see this business? And also, from a longer-term perspective, how do we see this business panning out for us as well as the industry?

Dr. Satyanarayana Chava: This Custom Synthesis unless the project goes into commercial phase, it is very difficult to project. That is the reason we have to do as many number of projects as possible to see success here. But we are doing good number of projects in the late-stage clinical phase right now, for which especially in high potent we are building large scale capacity for NDA batches. And we are also in the process of building large capacity for steroids and hormones as well. We cannot give a guidance on where this division will be in next two years, but we are very, very bullish on this division. That is the reason we have initiated construction of a dedicated CRAMS, R&D with an investment of close to Rs.150 crores with 2 lakh sft R&D. And we acquired land for this division, and we are in the process of acquiring another piece of land for this division. That shows our confidence and conviction that this division will grow significantly in the near future.

Sudarshan Padmanabhan: With respect to the FDF given that the debottlenecking is going to come this quarter and also the large capacity is coming in the second half, how do we see the traction to happen, last time we were continuously surprised with the numbers that came in on the formulations side, so should we assume a quick, say, for the next two years, we should be able to completely utilize the capacity?

Dr. Satyanarayana Chava: As and when the capacity is qualified and ready to go commercial, we have products to maybe made there. So, the increased capacity we have visibility that we will use pretty well significantly.

Sudarshan Padmanabhan: This triple combination, where do we see sir, I mean, this market, from the FDF side?

Dr. Satyanarayana Chava: This triple combination we do expect this year could be a $10 million opportunity for us in formulations but next year could be big. Out of 10 million, we have order for almost half of that.

So, we will service before September and we do anticipate some additional orders for that. Whereas the big revenues coming from the most popular triple combination drug DLT, which we are servicing, and our supply commitment is very, very good and our on-time and full score is also close to 100.

Sudarshan Padmanabhan: With the Rs.1,700 crores of CAPEX that we are seeing, I think in various forums we have talked about somewhat aspiration of a billion-dollar sale in the next couple of years. I mean, would this CAPEX more or less suffice for us to take us through that billion-dollar sales in the next couple of years, so we will do additional CAPEX for this?

Dr. Satyanarayana Chava: Actually, part of the CAPEX which we will do in FY'23 will not be used in FY'23. So, I think, to achieve that aspiration number, we do not need more CAPEX, I want to make it clear.

Moderator: Thank you. The next question is from the line of Tushar Manudhane from Motilal Oswal Financial Services. Please go ahead.

Tushar Manudhane: Just on the Richcore side, now that acquisition is done, and we have a clarity in terms of the new facility ramping up. So, any color you would like to give like how revenue shape up from this facility?

Dr. Satyanarayana Chava: Laurus Bio's new facility will go commercial by 15th of May and by September, entire facility will go commercial; we are putting four fermenters of 45,000 liters each; two fermenters will go commercial in May and two more fermenters will go commercial in the month of August, September. And we have order book for all those capacity. And we are also in discussion with current partners. And we are in the process of acquiring additional land. And we will create probably a million liters fermentation capacity in the next growth.

Tushar Manudhane: So, for the existing four reactors, now that order book is in place, so the revenue visibility would also be there, so any number you would want to give?

Dr. Satyanarayana Chava: We're not giving a number, but we will probably double the revenue in the division at least in FY'22 itself.

Tushar Manudhane: To create this 1 million litre capacity, investment will be Rs.60 crores or more than?

Dr. Satyanarayana Chava: Rs.60 crores is for the current 180,000 litre fermentation capacity. For 1 million litre, we are in the just drawing board stage, what could be the size of the fermenters and all. So, maybe we will be able to provide you with a number in the next six months.

Tushar Manudhane: Rs.1500 crores CAPEX for two years kind of anything investment for this 1 million litre?

Dr. Satyanarayana Chava: Partly considering. That is the reason we are giving a range between Rs.1,500 crores to Rs.1,700 crores.

Tushar Manudhane: Lastly, on formulations side, for the past three quarters just would like to understand how has been the volume growth and the price growth in the FDF segment?

Dr. Satyanarayana Chava: We haven't increased any price for any of our APIs or formulations in FY'21. Revenue is only coming from volume growth and product expansion.

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

Krish Mehta: I have two questions; the first one is what is the percentage of non-ARV revenues for Q4 FY'21 and for the entire year '21?

Dr. Satyanarayana Chava: Out of Rs.1,413 crores of total company's revenue, Rs.570 crores came from ARV, about 60% is non-ARV API revenue in Q4.

Krish Mehta: What is the expectation for non-ARV revenues going forward for FY'22?

Dr. Satyanarayana Chava: FY'22 we are not expecting major diversification of revenues. FY'22 revenue base will be very similar to FY'21. But we do believe FY'23 good diversification will happen and we are working towards complete diversification of revenues by FY'25. So, that will be visible from FY'23 onwards.

Moderator: Thank you. The next question is from the line of Bharath Kumar from Quest for Value. Please go ahead.

Bharath Kumar: My question is regarding Custom Synthesis. The current share of Custom Synthesis is around 10%. In an interview with media a couple of months back, you said that four to five years down the line, the share of Custom Synthesis, which is very, very high margin business would be around 20%. So, it is almost double the share. It means the growth in Custom Synthesis would outpace the growth in API and formulations. And already API and formulations for Laurus is growing at very, very high rate. So, what I am not clear is like what makes you to be so bullish in Custom Synthesis segment to grow faster than API and Formulations? I understand that you already answered this question saying like you have some late-stage molecules and all, but how many molecules and all, can you give some visibility on that?

Dr. Satyanarayana Chava: Can't give you these details, what molecules, what phase and all, but we are very hopeful FY'23 onwards, our Custom Synthesis growth will definitely outpace rest of the divisions.

Bharath Kumar: So, this would be from the Vizag manufacturing plant is it?

Dr. Satyanarayana Chava: That is the reason we are investing in capacities in this division. Once the capacities come commercial, I am sure the growth in this division will be very good.

Bharath Kumar: So, once Vizag plant is commercial, then you have more growth in this Custom Synthesis, right?

Dr. Satyanarayana Chava: You're right.

Bharath Kumar: Also, you have a new R&D discussions in Hyderabad. So, that is mainly for the CRO services?

Dr. Satyanarayana Chava: We are not doing any FTE service. This is to do CDMO. This is a dedicated site for CRAMS business.

Bharath Kumar: Where do you see Laurus Bio in three to four years from now, like how much Laurus Bio would be contributing in terms of percentage to the top line?

Dr. Satyanarayana Chava: It is a difficult question. Right now, Laurus Bio by FY'21 is about Rs.50 crores revenue, that is about 1.2% of revenue. Will it be 10% of revenue in two years? I doubt. But well 50 crores become 200 crores or 300 crores probably yes. But that division growth we need to attract big customers. And we need another four or four years to make that division also very sizable. So, if you look at our CRAMS division, is moderate right now. But it took seven, eight years for us to nurture the division. So, we will start putting our resources, our thoughts, our strategy, execution into the division, will become a sizable in next five to six years.

Moderator: Thank you. The next question is from the line of Foram Parekh from Choice Broking. Please go ahead.

Foram Parekh: I just wanted to know like we have achieved the highest EBITDA margins ever. So, just wanted to know like can we sustain these kind of margins or should we assume that we have peaked out or going forward the margins would continue to come back from the product mix or from the cost rationalization, how should we assume, if you can throw some color on that?

Dr. Satyanarayana Chava: As we were mentioning in the previous calls also, we are confident to maintain 30% from FY'23 onwards the same profit ratios.

Foram Parekh: We have not taken any price hike in FY'21. So, do we want to take any price hike in FY'22?

Dr. Satyanarayana Chava: Our growth is not driven by price hikes. I do not know why people think growing business by hiking prices. We want to grow business, make more money by increasing our product basket, increasing our market share, our growth will be primarily driven by market share gain and portfolio enhancement, not by price hikes, we have not done that in FY'21, I do believe we will never do that in FY'22 also.

Moderator: Thank you. The next question is from the line of Ranveer Singh from Sunidhi Securities. Please go ahead.

Ranveer Singh: My question is around ARV API. What has been the growth in volume and price if you could give some ballpark numbers?

Dr. Satyanarayana Chava: This year, the significant revenue increase in ARV APIs came only because of volume gain. Earlier we used to supply one or two APIs of the fixed dose combination, three drug combination. In the most recent year, for the triple drug combination, we got approvals for all the three APIs in the triple drug combination. That is the reason our volume in ARV APIs went up significantly which led to growth. And we do continue to have the same momentum in FY'22 also. So, we do not see that there is one-off in our ARV APIs.

Ranveer Singh: In ARV API, why this volume growth has suddenly been so high in this year? Is there any supplier from China or anybody has stopped supplying in API segment, because I think the ARV market itself has not grown especially during this COVID related impact. So, in this scenario, what actually has led this volume growth and whether this will sustain?

Dr. Satyanarayana Chava: Earlier, the most preferred treatment was Efavirenz-based where we do not have many approvals for Lamivudine or Tenofovir from many customers. When the therapy moved from Efavirenz-based to Dolutegravir-based, we got approval for Lamivudine and Tenofovir with most of the customers. So, people started buying three APIs -- Dolutegravir, Lamivudine, Tenofovir -- from us, where earlier people used to buy majority Efavirenz and some Tenofovir. So, that is the primary reason for our volume growth last year.

Ranveer Singh: It is a preference of product for consumers, that is…?

Dr. Satyanarayana Chava: Yes.

Ranveer Singh: You said that in '23, diversification in API we'll see. So, despite this diversification, our EBITDA margin would be the same or we see some negative or positive impact due to this diversification?

Dr. Satyanarayana Chava: We do not see any dilution of margins because of diversification. There is a limited growth in ARV APIs right now. So, we are already having a lion share of market. So, it is not easy to grow beyond. So, we are adding diabetic segment, cardiovascular segment, which will be commercialized in the beginning last quarter of FY'22 onwards. So, that is the reason we are investing more into non-ARV API infrastructure. Even our formulation also most of the Brownfield expansion what we are doing right now will be used for non-ARV.

Ranveer Singh: Can you give us a broad breakup of CAPEX, Rs.1,500 crores to Rs.1,700 crores you mentioned, so how much would be on API intermediates?

Dr. Satyanarayana Chava: 50% is going into API intermediates and then maybe 25% in FDF and 25% in Custom Synthesis, that is the broad breakup.

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

Nimish Mehta: Just to continue from the previous participant, you mentioned that the growth in formulations has been driven in the product side from Efavirenz-based, Dolutegravir-based. What is the scope of further growth in terms of the shift happening? What is the competition outlook there? Are we likely to continue higher market share in that expanded market, that would be great for me to understand?

Dr. Satyanarayana Chava: Nimish, we will see some growth both in ARV APIs as well as formulations in FY'22. But FY'23 onwards, the growth will be driven by non-ARVs both in APIs as well as in formulations. From FY'20 to FY'21, the majority growth came from therapy shift from Efavirenz-based to Dolutegravir-based. Once that is done… and we do have the product basket, even there is a shift from one therapy to another therapy in ARVs, we are fully prepared to take that opportunity to our favor.

Nimish Mehta: Correct. What I am trying to understand is the shift towards Dolutegravir-based therapy as a kind of feet in the sense like there is no more increase in DTG-based therapy over Efavirenz-based, have we reached that point or you see that some far away and there is further growth in that DTG category, not just for Laurus but in general, is the DTG category likely to grow?

Dr. Satyanarayana Chava: Based on the reports, the DTG penetration will continue to increase in this year as well as next year.

Nimish Mehta: The other thing I just wanted to know in the API segment, I think we are a leader or like an expert in antiviral medication drug. So, are we not seeing any opportunity related to COVID drug where the API was right from Remdesivir to many of the protein inhibitors are now being touted as a potential drug for COVID like new drug and all of those things. Do we not see an opportunity there in maybe older drugs or new drugs due to COVID-related? And finally, if you can also let us know what is related to regulate the API?

Dr. Satyanarayana Chava: At the beginning of the COVID crisis, we produced hydroxychloroquine sulfate, but it never became popular. So, we never had any significant sales coming out of that. Other than that, we have not made any COVID-related APIs or formulations and we are not planning to do that also.

Nimish Mehta: Sir, any particular reason because that looks like to be one of the fastest, you can correct me if my understanding is wrong? And I see Laurus is an expert in antiviral medication for drug. So, like, why not?

Dr. Satyanarayana Chava: So, we are operating our capacities fully and for us to divert these capacities for any opportunities, we have to meet our commitments to existing suppliers on ARV. ARV is equally important for 20 million patients. So, our commitment to supply ARVs on time we are honored in the COVID crisis. So, we looked at but I would say we did not get an opportunity to serve.

Nimish Mehta: Finally, a word on the API opportunity, Lenalidomide now that is likely to be US-centric market next year?

Dr. Satyanarayana Chava: We do not have any DMF in US. So, we cannot comment on that right now.

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

Nitin Agarwal: My question is on the formulations business in FY'21, what will be the typical composition of this business, how much would be LMIC business segment?

Dr. Satyanarayana Chava: Nitin, broad split is three-fourths in LMIC and one-fourth in Europe and North America. We do anticipate similar actually 70:30 in FY'22 and FY'23 onwards, we do expect it will go to two-third, one-third. As we mentioned, the formulation diversification benefits will start showing in FY'23 onwards. So, FY'23 we expect from 75:25 which will be 70:30 and FY'23 that will be even bigger, so we'll have maybe 60:40 in FY'23.

Nitin Agarwal: On the LMIC business, do we see opportunities for further growth from where we are?

Dr. Satyanarayana Chava: Nitin, when we are saying the percentage is coming down, that does not mean the number is going down. So, we are increasing our revenue significantly, that it the reason coming down. We do anticipate growth in LMIC market in FY'22 when compared to FY'21. We do some growth in FY'23 also, but the other non-ARV, non-LMIC business will grow significantly in FY'23 based on the product what we are going to file.

Nitin Agarwal: On non-LMIC business, what proportion of this, largely will be developed market business, US, Canada, European business as we drive it or what will drive the non-LMIC business for us from '23 onwards?

Dr. Satyanarayana Chava: Non-LMIC business is only from Europe and North America, nothing else for us.

Nitin Agarwal: That is based on the visibility of the ANDA. All products that we are doing are under own ANDAs or our own site?

Dr. Satyanarayana Chava: Yeah, fully integrated offerings, Nitin.

Nitin Agarwal: When we capture the contract manufacturing for formulations or is there a business like that?

Dr. Satyanarayana Chava: There are three types of contract manufacturing we are doing. Generic APIs will come in generic APIs itself. We do contract manufacturing of formulations of generic formulations that comes in formulations division. The contract manufacturing clinical programs comes in synthesis division.

Nitin Agarwal: So, how big is this contract manufacturing in the formulations business?

Dr. Satyanarayana Chava: Most of our European sale as of now is contract manufacturing.

Moderator: Thank you. The next question is from the line of the Tushar Bohra from Emkay Ventures. Please go ahead.

Tushar Bohra: When we discuss Custom Synthesis, are we including the specific opportunities in cosmeceuticals and nutraceuticals within that, if you can just help understand if there are any significant triggers in this part of the business? That is one. And second, I wanted to understand, are there any vaccine-related opportunities like as an adjuvant or any such opportunity for Laurus going forward that we are exploring?

Dr. Satyanarayana Chava: I will answer the first question. Whatever the nutraceuticals, dietary supplement we sell to multiple customers is not part of the Synthesis business. Any product we make exclusive to one customer will be part of the Synthesis business. One customer exclusive products will be in Synthesis business. When we sell to multiple customers, that is not part of that. The second question, are we making anything for vaccine business. Our Bio division makes cell culture ingredients which are used in the vaccine manufacturing. We are not making adjuvants right now.

Tushar Bohra: But is there a COVID-related vaccine play also then for our Bio division, if not now, in future, are we exploring?

Dr. Satyanarayana Chava: I do not think we will be catching the COVID vaccine wave by supplying ingredients from Bio division, I do not think that will be an opportunity for us.

Tushar Bohra: Second, we mentioned the sterile facility in a way setting up a plant specifically for the rise in hormone. In previous call, we had mentioned possibility of an M&A in this space. So, does this investment preclude in that M&A activity, or is that something we are also looking at in parallel?

Dr. Satyanarayana Chava: I did not remember we mentioned M&A activity. Our investments into steroids and hormones is based on discussions with the potential customer and the volumes what we are talking. So, we need a specific exclusive capacity for steroids and hormones. So, we are investing based on our discussions what we are doing with a potential customer.

Tushar Bohra: The overall capacity constraints that we have been facing, and the continuous upward revision in CAPEX, why haven't we looked at acquiring USFDA designated plant, I am sure that there will be a few available, have you explored that to augment capacity faster?

Dr. Satyanarayana Chava: We looked at earlier, but we believe building our own capacity is much more cost effective. See, no capacity will come at 1x of sales whereas our asset turnover ratio is 1.5 right now. So, we believe putting CAPEX in Greenfield or Brownfield to enhance capacity is much more cost effective than acquisition.

Tushar Bohra: A clarification on one of the points you have mentioned in the call. So, this Rs.1,500 crores to Rs.1,700 crores of CAPEX over FY'22, '23 is not likely to be contributing or at least FY'23 portion is not going to contribute to a 1 billion revenue target. That is the point you mentioned, right?

Dr. Satyanarayana Chava: Part of it will not be required to go to the target. What we do in FY'23 will not be fully utilized in FY'23 itself.

Moderator: Thank you. The next question is from the line of Ankush Agarwal, an individual investor. Please go ahead.

Ankush Agarwal: We have a stance that ARV as a business will not grow much for us given that we are already a big player in the market. So, for Laurus to grow at a high rate, our other business of non-ARV business are at very fast paced, because non-ARV business still relatively small for around 25% to 30%. So, what are the initiatives and objectives that we are targeting over the next couple of years for this business to grow that fast if you can highlight this?

Dr. Satyanarayana Chava: Two things. Non-ARV, API and formulations growth we already developed the products, we have filed DMFs, we have filed dossiers for marketing authorizations. That is already I would say midway in that diversification. When it comes to the Custom Synthesis investments what we are doing, half our feet based on some kind of commitments what we are having from our customers with respect to capacity and rest is to increase the product portfolio in Custom Synthesis. Not every product will go to commercial when we do phase-I. So, we wanted to increase our phase-1 pipeline. Right now, we are constrained to take more phase-I project. That is the reason we are creating a dedicated capacity. Right now, when there is a project, allocation of resources is becoming a challenge both in R&D or in manufacturing. We wanted to take away that constraint and bring some abundancy, we are creating two lakh sft R&D for CRAMS and we are creating two new sites for CRAMS division. So, by FY'23, CRAMS division will have three manufacturing sites, hopefully, four and an R&D center. So, that will be a fairly big organization itself.

Ankush Agarwal: Secondly on the MDL business, the entire growth we are targeting for next couple of years is on the contract manufacturing, of course, with the European customers. We will be adding more products, right?

Dr. Satyanarayana Chava: No, majority growth will come from non-contract manufacturing.

Ankush Agarwal: So, apart from the opportunity we will have based on the European customer, the added capacity that we are adding?

Dr. Satyanarayana Chava: We grow contract manufacturing, but the non-contract manufacturing revenues in formulations also will be significant.

Moderator: Thank you. The next question is from the line of Onkar Ghugardare from Shree Consultancy. Please go ahead.

Onkar Ghugardare: Based on the CAPEX number you talked about for the next few years, what kind of asset turnover expecting on that?

Dr. Satyanarayana Chava: We can give you a broad number; it is 1.5 what we have achieved right now, you can expect that.

Onkar Ghugardare: What would be the maximum revenue potential in that expecting 100% capacity utilization?

Dr. Satyanarayana Chava: If you do a math 1,500 into 1.4 that would be the opportunity. But we continue to invest. If we stop investing, how we will grow? For these investments, we are not raising debt, probably everything will be done through internal accruals. And we also need to be careful in whenever ROCE and return on equity numbers are so high and our cost of debt is so low. So, the question and our challenge for us is to go for CAPEX which is giving very high returns versus retiring our debt. See, our debt-to-EBITDA is 0.8. We are doing that constant debate internally whether to retire debt or to put more CAPEX.

Onkar Ghugardare: Okay, so the second question is you have been selling stake in the open market to reduce the hedge which you have done. So, what would be the plan on that front?

Dr. Satyanarayana Chava: There is no pledge of shares from my side, everything was removed.

Moderator: Thank you. The next question is from the line of Gagan Thareja from Kotak. Please go ahead.

Gagan Thareja: Just wanted to clarify that there will not be any additional debt for the CAPEX that you are undertaking for next two years?

V. V. Ravi Kumar: There may not be any significant debt increase.

Gagan Thareja: My question is that with the additional CAPEX, there will be additional OPEX and depreciation also coming in. So, what could be the magnitude of OPEX and depreciation related to the additional capacities?

V. V. Ravi Kumar: Most of it is Brownfield, it is in a proportionate to the CAPEX and the operations utilization.

Dr. Satyanarayana Chava: In FY'18, '19, we have created so many Greenfield facilities, had an impact on our OPEX and depreciation in our PAT numbers, but this time most of the expansion is happening in the Brownfield and we do not see the investment impacting our numbers from now onwards.

Gagan Thareja: On your LMIC formulations, I think this year all the sales would have been from the TLD combination, we also have the approval for TLE 400 where you would probably be from a competitive standpoint, it is probably a better market although probably on the lower side. If you could give some idea of what could be the size for the TLE 400 market next year?

Dr. Satyanarayana Chava: We can give you the TLE 400 uses in general, we will not give you what market share we have. It is between $120 million to $150 million TLE 400 opportunity.

Gagan Thareja: TLE 600?

Dr. Satyanarayana Chava: TLE 600 the opportunity is very small.

Gagan Thareja: But TLE 400 the number of approved companies would be only two to three at most?

Dr. Satyanarayana Chava: Yeah, three as of now.

Gagan Thareja: You also indicated you have the approval for TAF-based formulation if I understood it correctly, or is it for the API you are talking about?

Dr. Satyanarayana Chava: We got approval for Dolutegravir, Emtricitabine TAF NDA and we also got orders for these formulations, and we will service that in the next six months, and we would expect more orders for that.

Gagan Thareja: On TAF, just wanted your expert opinion. What I am able to understand is that because of the weight gain, especially in the female cohort of the African population is very high, lot of thinking, that is a concern for comorbidity. Do you concur with that and therefore, do you see that being a limited sort of market right now or do you see this as a product that will substitute TDF in a very big way going ahead?

Dr. Satyanarayana Chava: See, the difference between switch from Efavirenz to Dolutegravir is a class. Efavirenz is NNRTI and Dolutegravir is integrase inhibitor. When it comes to Tenofovir and TAF, these are same class. So, we do not see the disruption like Efavirenz to Dolutegravir similar to TDF and TAF.

Moderator: Thank you. The next question is from the line of Tarang from Old Bridge Capital. Please go ahead.

Tarang: I was reconciling some numbers. So, Laurus today would have a gross block of about 2,600 crores and about CWIP of 400 crores, so that is 3,000 crores and about 1,500 crores of CAPEX going in the next two years, part of which will not help in revenue in FY'23. So, if I add all of this, about 4,000 crores of gross block, so 1.5x would translate about 6,000, 6,200 crores of revenue whereas you have been indicating that maybe this asset base could help us reach about a billion dollars of revenue. So, where is the disconnect sir?

Dr. Satyanarayana Chava: You're talking about net block probably. Our gross block would be bigger than 4,000 crores if you take 1,500 crores ensuing CAPEX, maybe close to 5,000 crores gross block.

Moderator: Thank you. Last question is from the line of Prashant Rane from Exclusive Advisors. Please go ahead.

Prashant Rane: My question is about we are expanding our businesses in so many new areas and there are a lot of challenges which will be going ahead, so how it works out in terms of management bandwidth and attracting talent as far as the ESOP plan, I would like to know the management views about it, and do you think this ESOP is one of the dilution or it is going to be a feature for attracting talent?

Dr. Satyanarayana Chava: Thanks for asking a very interesting question, Prashant. We continuously allocate stock options to retain talent. And we are setting a benchmark in the pharma industry with the number of stock options and the value of the stock options what we have given to our colleagues. Right now, we are not seeing any challenge in attracting talent in any of these divisions, and we constantly in lookout for adding mid to senior management talent in all the divisions, and we continue to add that. One good thing is we are not in the process of adding hundreds of ANDAs, we are not having the strategy of filing hundreds of DMF. So, our approach is develop few products, maximize those products into many geographies and get leadership position and gain market share. So, with that, our commitment to scale, commitment to quality is very well appreciated across the industry and that is helping us to retain talent very well.

Prashant Rane: Revenue per employee is that the matrix which you track internally? And if you can also answer about the management bandwidth going ahead, is it sufficient or you expect some changes?

Dr. Satyanarayana Chava: We do monitor revenue per employee, EBITDA per employee since inception. And currently our revenue per employee is a little over crore per employee. If you look at our Richcore acquisition, we did not acquire a company, we acquired the talent. In fact, the current leadership team and the founders will continue to run. So, there we do not see any management bandwidth challenge. When it comes to the other business, we are running the same business adding more blocks, more products. So, we are adding talent and currently, we do not see any challenge in senior management bandwidth.

Moderator: I would now like to hand the conference over to the management for closing comments.

Dr. Satyanarayana Chava: Thank you, Nikhil for organizing this call and thanks all of you for participating and giving us your perspective how we should perform and how we should invest and stay safe during this pandemic.

V. V. Ravi Kumar: Thank you.

Moderator: Thank you. On behalf of Ambit Capital Private Limited, this concludes this conference. Thank you for joining us and you may now disconnect your lines.