“Laurus Labs Limited's 2QFY22 Earnings Conference Call”

October 29, 2021

MANAGEMENT: **DR. SATYANARAYANA CHAVA – FOUNDER & CHIEF EXECUTIVE OFFICER, LAURUS LABS LIMITED**
MR. V V RAVIKUMAR – EXECUTIVE DIRECTOR & CHIEF FINANCIAL OFFICER, LAURUS LABS LIMITED
MR. VIVEK KUMAR – SENIOR GENERAL MANAGER, INVESTOR RELATIONS, LAURUS LABS LIMITED
MODERATOR: **MR. PRASHANT NAIR – AMBIT CAPITAL**

Moderator: Ladies and gentlemen, good day and welcome to the 2QFY22 Earnings Conference Call of Laurus Labs Limited hosted by Ambit Capital. As a reminder, all participant lines will be in 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 Prashant Nair from Ambit Capital. Thank you and over to you sir.

Prashant Nair: Thank you. Hello, everyone. On behalf of Ambit Capital, I thank the Laurus management for giving us the opportunity to host their 2QFY22 Earnings Call. On this call, we have Dr. Satyanarayana Chava -- Founder and CEO; Mr. V.V. Ravi Kumar -- Executive Director and CFO and Mr. Vivek Kumar, Senior General Manager, Investor Relations. I now hand over the call to Dr. Satya for his opening remarks. Over to you, sir.

Dr. S. Chava: Good morning, Prashant and good morning, everyone. Thank you for joining us for our 2Q & 1HFY22 Results Conference Call. We're pleased to have this opportunity to update you on your progress and answer your queries. I hope everyone and your family members, colleagues, friends are safe during this COVID times.

We continue to witness a normal operations across our manufacturing units, R&D center and at our corporate office.

At the company, we are committed to protecting health and well-being of our colleagues and their families. We continue to implement rigorous safety and hygiene measure across all locations without any compromise. We continue to conduct regular testing for all the employees and provide work shift flexibility wherever possible.

We are very thankful to all our colleagues for rising to this challenge and ensuring business continuity.

We're excited to announce Laurus Synthesis Private Limited which is our CDMO subsidiary, has signed a multi-year supply contract with a global life science company during the quarter. The deal entails complete drug development and manufacturing for a portfolio of niche APIs. Under this agreement, LSPL will use part of the existing capacity to manufacture and supply APIs and also set up a dedicated manufacturing site to cater to the demand. Part of these CAPEX will be funded through long-term commercial advance apart from sponsoring development costs. We believe this development and manufacturing agreement demonstrates our capability and mark a significant step towards our evolution as a valuable partner for global life science companies.

We're also seeing additional opportunities in the CDMO space from a few existing as well as new partners who are looking to diversify and build their supply chain base.

I would also like to briefly touch upon the recent manufacturing challenges in China which we believe can have internal challenges to pharma industry including fluctuation in the cost of API, availability of raw materials and supply chain disruptions, along with higher logistics costs. We are closely monitoring situation relating to this while taking relevant course correction to fortify our business continuity and customer need.

Coming to our results, 2Q numbers have been slightly weak due to transient impact of channel destocking of various business; however, for 1HFY22 the operational performance were resilient overall as we continue to demonstrate, healthy revenue mix and profitability. Our sustained traction in FDF and CDMO business was key drivers for the growth so far and we expect the same diligence to continue as a growth in the future as well.

We are well on course in our journey to expand and intensify our diversification plan as we double our growth in the coming years. We remain affirmative on our aspirational revenue target of billion by FY23 and this will be supported by several approvals anticipated and we made big progress in creating capacities across our four business segments to reach these aspirational goal.

Moving on to our 2QFY22 revenues, we achieved Rs.1,203 crores, showcasing a growth of 6% year-on-year when compared to H1 we achieved 75% growth year-on-year.

To begin, I would like to share key updates on our Formulations business. The Formulations division reported a revenue of Rs.495 crores, a healthy growth of 10% year-on-year for Q2. The contribution from the formulations segment has improved during the first half to 41% when compared to 35% in the financial year FY'21.

Coming to the LMIC business, we have seen some traction across the region. During the quarter, we launched a triple combination of using Tenofovir, Alafenamide after obtaining in-country approvals and we expect gradual ramp up for this product.

Apart from the ARV LMIC business, we have seen big growth in developed markets in North America and EU. We are seeing healthy market share increase in some of our existing portfolios in this market.

We continue to leverage our front-end presence in US for new product launches. During the quarter, we filed two ANDAs and four in the first half of FY'22. Cumulatively, we have filed a total of 30 ANDAs. Out of this, we have nine final approvals and nine tentative approvals. In Canada we have eleven product approvals, of which we launched five and we intend to launch two in the next two quarters.

In EU, we have validated the two products as part of the contract manufacturing agreement with the partner. We expect a significant upside in FY'23 from these products and we are also creating capacities to cater to this demand in the new formulations building.

Medicines Patent Pool and Merck entered into a licensing agreement for Molnupiravir for low- and mid-income countries. As you are aware, Laurus and MPP have a very long and successful partnership in various HIV and FC drugs and we will approach MPP for Molnupiravir license as well.

With a very good visibility in FDF segment, we will continue to invest in our capacity expansion. As part of the debottlenecking, we added 1 billion capacity during the first quarter and additional Brownfield expansion at the same side is going to add significant capacity in a phased manner starting from 4QFY22. With this, we will achieve a 10 billion unit capacity in our formulations side.

We continue to allocate critical resources to our research initiatives and investing in portfolio based on complexity and scale. So, far we have immediate release forms. We graduated into developing sustainable forms and some complex generics as well. With overall spend to the sales for the quarter and H1 was at 4% of our revenue. We have a total of 66 products in the R&D pipeline either on review or in the development in a very significant addressable market side.

We have filed 30 ANDAs in the US, 11 dossier in Europe, 15 dossiers in Canada, 8 with WHO, 4 in South Africa, 4 in India, and we are filing several in the other African markets. Out of the 30 ANDAs filed in US, we have 14 Para IV filings with 10 first-to-file opportunities. Our approach remains product-specific and not market-specific, but that is very visible in our filings across the regions of Europe and Canada.

When it comes to generic API, our anti-retroviral business during the quarter was weaker than expected and declined 11% year-on-year to Rs.339 crores. Sequential drop is always due to continued demand stabilization in the channel as indicated in the last quarter itself. This is expected to stabilize in Q4.

We continue to maintain leading market share in the products what we sell. So, there is no concern with respect to market share or cost of the product or the capacity for the product.

When it comes to oncology APIs, we see good traction in the sales, although there is a decline in the Q2, that's not because of business challenges, it is only because of deliveries access to the customer, we see by the end of the year oncology will see a growth when compared to the FY'21.

As you are aware, the company has one of the largest high potent API capacities in India. We also added a new capacity during the first half of this year and we are further expanding the capabilities in high potent manufacturing in Unit-IV located at Visakhapatnam.

Our aim is to strengthen global leadership in some of the existing products by focusing on capacity and backward integration.

In the generic API segment, other APIs predominantly constitutes of cardiovascular, diabetes and some asthma products, recording a 8% growth year-on-year and there is a decline of 20% in the first half of the FY'22. This decline has nothing to do with the business opportunities, it's only the scheduling of the delivery by CMO partners. And we do believe this segment by the end of the year will see significant growth.

When it comes to the CDMO Synthesis business, we maintained a very strong growth and delivered 34% year-on-year during the quarter to achieving Rs.154 crores sales. For 1HFY22, CDMO business grew over 60% year-on-year.

As I mentioned, our contract with the global life science company will take these into much higher heights in the coming years.

Strong growth year-on-year was led by first time new client addition and increased businesses from existing customers also.

We are pursuing several active projects in the late-stage clinical programs. And as we indicated there are four products we supply on a commercial scale. We are also doing capacity expansion for this division and we commercialized LSPL Unit-I at Vizag during the Q1. This will cater to exclusively CDMO activities for the division. Our Greenfield investment to set up the dedicated R&D at Genome Valley, Hyderabad will be completed by end of FY'23. And we're also putting up two new manufacturing units at Vizag under the subsidiary. These units are expected to be operational by FY'23 and the commercialization will be done during FY'24. These sites will have capabilities to handle steroids, hormones, high potent molecules apart from very large volume molecules.

When it comes to Laurus Bio, this division achieved Rs.26 crores for the quarter and Rs.40 crohres for the H1 FY'22. On a quarter-on-quarter basis, the business is scaling very well as per our expectations and have grown over 80% that is mainly due to the availability of the new fermentation capacity.

During the quarter, we have commercialized using the second fermentation, taking the total fermentation capacity to 90 KL. The remaining capacity two fermenters are in the qualification and are expected to get commercialized before December. The capacity is used for large scale CDMO for Food proteins.

We are also going for expansion at R1, adding a new very large R&D block and also already started installing some balancing equipments which will be done by September 2023.

We are also in the process of acquiring additional land to meet our customer demand in the recombinant food protein business.

At Laurus,, our focus on ESG quality and regulatory compliance to drive sustainable growth and further adds to our pipeline which will lead our journey towards our division apart from strengthening core values. Manufacturing capacity is expected to achieve our aspirational revenue of a billion in sales by FY'23 are already yielding results. And some manufacturing facilities will be qualified by March 2022. If we receive ANDA's approval as we anticipated, we don't see any challenges in achieving our aspirational target of 1 billion revenue by FY'23.

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

V V Ravi Kumar: Thank you, Dr. Satya and a very warm welcome to everyone for our Q2 and H1 FY'22 earning call. The total income from operation for the quarter is at Rs.1,203 crores as against Rs.1,138 crores, registering a growth of 6% whereas for the half year it is 17% growth. Gross margin for the quarter is around 56% which is equal to the corresponding quarter. Our EBITDA is at Rs.348 crores for the quarter with a margin of 29%. Our EBITDA for H1 is Rs.748 crores with a margin of 30%. So, we remain confident of achieving close to 30% EBITDA for the full year. Our diluted EPS for the quarter is Rs.3.80 on annualized basis, whereas for H1, it was Rs.8.4. Our ROCE at 29% on an annualized basis on the back of sustained operating leverage across all our manufacturing units.

On the CAPEX front, we invested close to 242 crores during the quarter and Rs.518 crores during H1. We remain on course to strengthen our position as a cost effective integrated pharma player. We're investing in backward integration efforts in making intermediates creating further APIs and FDF capacities.

As you are aware that we have embarked upon a significant growth CAPEX of Rs.1,500-1,700 crores for FY'22 and '23 in two years' time. We want to update you that most of the investments across the key projects on track and we expect to be in the similar range for the two years and we will give you an update by the end of the financial year so where we will be for the next year.

Given that we are at the start of the festive season, we would like to wish you all very happy and safe and Prosperous Diwali for all of you.

And with this I would request the moderator to open the lines for Q&A.

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

S Padmanabhan: My question is to understand the situation more as far as the raw material availability is concerned. I think across the industry people are talking about it. And from what I understand is

that there have been a substantial increase in the base materials in the second quarter and further increase say in the month of October. So, in this backdrop and given that we have also been backward integrating quite aggressively, how much do you think that incrementally in the third quarter you see issues both in terms of price escalation and availability for us?

Dr. S. Chava: The raw material price increase is especially visible in the solvents and utility costs also gone up significantly. The increase in these prices will be visible only three, four months from the day we start buying the solvents because of the inventory in the pipeline. As you are also aware, the grass margins for the quarter were very healthy when compared to previous quarters. That was primarily because of higher revenue contribution coming from Synthesis and FDF. And in the case of ARV, most of the ARVs are under a long-term contract to other formulators as well as in the FDF space. We will maintain similar prices to our partners… I am not saying same prices, we will maintain similar prices, and we have built significant inventory, you might have seen our inventory also gone up by close to Rs.300 crores, that is primarily because we are having a lot of ARV inventory, actually big for us, because the ARV business will continue to boom because of moving from 30s to 90s, we do believe a lot of destocking is happening in the country. Once that issue is over, the ARV business will continue to be back on track and our inventory will certainly help us to service the demand with our customers.

S Padmanabhan: On China, how much will be the dependence? And with other business, apart from ARV, is it possible for us to pass it on?

Dr. S. Chava: Right now, close to 50% of raw materials we buy from China and we don't buy any intermediates. All intermediates are made in-house. So, that way we are insulated from the fluctuations to a great extent. That's why our challenge is only to monitor the prices of solvent, which is a global phenomenon, not limited to the country, other than that because of our initiatives and also capacity creation for the backward integration, we are in a better question than people who import from intermediates and buy APIs from other countries.

S Padmanabhan: My second question is basically two parts; one is we were previously adding a lot of capacities and we have signed a long-term contract on the CDMO space which lends a very good comfort as far as future growth is concerned. The second is if I break the cost, below the gross margin, because of lower-than-expected ARV sales, we have seen some kind of a negative operating effect and also I would assume that the transportation cost as you said would be higher. So, as we move to the second half, number one, do we see say an FDF or you CRAMS business picking up and offsetting some kind of ARV loss? Second is cost control. Is there a possibility of absolutely controlling certain costs given that we are facing some of these issues?

Dr. S. Chava: Your voice was not very good but if I grasp what you are asking, see, the second half the ARVs will pick up especially the Q4 we don't see any challenges to go back to the Q4 of FY'21. So, we are also confident because of enough capacity we have created enough inventory in the

pipeline for us, we are very confident to service the ARV growth in Q4. Coming back to your question of gross margins, our gross margins are very healthy, 30 basis points reduction when compared to the QoQ, 100 basis points variance to the YoY. So, we are not having any concern to maintain that gross margin despite of these challenges because of shift in regular contribution coming from FDF as well as Synthesis business.

S Padmanabhan: I am talking about margin below the gross margins, that is the operating leverage. So, again should the volumes more than offset the kind of drop in ARV in the second half? Specifically talking about the other expenses. So, is there a way where we can control that cost?

Dr. S. Chava: In the Q2, we had a negative leverage actually. We have less ARV sales, we produced more APIs. So, despite of having higher same gross margin we had a lower EBITDA that is because of deleverage in operations because without selling we produced more.

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

Tushar Manudhane: Sir, on the FDF front, while we had capacity expansion and even new launches happened during the quarter but quarter-on-quarter in fact FDF sales have declined a bit. Can you explain that?

Dr. S. Chava: The decline in FDF sales is not significant, Q1 we did 521 and Q2 495, if you look at year-on-year we did from 450 to 495 and we don't see any challenge to utilize our external capacity in the next financial year. As we mentioned, we are creating capacity to service our demand in FY'23.

Tushar Manudhane: So, you mean to say that FY'22 would be more or less at the similar run rate as the capacity or rather commercialization will start having fruits in FY'23?

Dr. S. Chava: New revenue coming from the Brownfield expansion in the site will come from FY'23. The debottlenecking capacity will come handy partly came in H1 and fully in H2. Actually, coming from Q3, Q4, our formulations lines are running at very-very optimum capacity.

Tushar Manudhane: And just extending to that like so with this your lines operationally fully, so other expenses and the employee cost will also then increase in line in the upcoming quarters?

V V Ravi Kumar: Slightly maybe higher side, Tushar.

Dr. S. Chava: We started recruiting people for the Brownfield expansion at all levels. H2 will be better than H1. We believe in formulations, we have more people, we are going to start reducing in Q3 as well as Q4.

Tushar Manudhane: Secondly, while you have alluded that 50% of raw materials are procured from China but how has been the price changes for these raw materials which you have procured from China, let's say over the past six to nine months, what percentage approx.. increase would have happened.

Dr. S. Chava: As I mentioned, we are more concerned on the volatility in the solvent prices rather than on the intermediate starting materials prices from China right now.

Tushar Manudhane: And this solvent should be contributing to what percentage of your total raw material cost?

Dr. S. Chava: About single digit.

Tushar Manudhane: Lastly on CAPEX while we have almost about Rs.580 crores in first half and given that it's 1,500 to 1,600 over FY'22, '23, so just trying to understand how much CAPEX would you be doing in the second half FY'22?

V V Ravi Kumar: Actually, what we are saying is whatever guidance we gave 1,700 crores, majority will be there in the current year itself. In the first half whatever 518 is there, that includes the large portion of land what we have acquired for both subsidiaries as well as for the parent.

Moderator: Thank you. The next question is from the line of Ankush Agarwal from Search Capital [ph]. Please go ahead.

Ankush Agarwal: Firstly, in Q2 of last year and also in Q3 of last year you had stated that the rise in our ARV business is not because of channel stocking at our customers end, but now you're seeing channel destocking at a customers end, which you expect going forward as well. So, what explains this contrast?

Dr. S. Chava: Two reasons. One is most regulators in the country health authorities moved from multi-month dispensing from 30s to they moved to 90s. So, suddenly there was an uptick in the number of units they procure to give multi-month dispensing, number one. And partly shift from Efavirenz-based regimen as we also left some inventory of Efavirenz-based regimen, it took some time for that regimen, inventory to be dispensed. So, these two happened in the last six months.

Ankush Agarwal: So, do you think our business can scale back to those kind of numbers going ahead?

Dr. S. Chava: From Q4 onwards we do believe we will go back to the Q4 of FY'21, we're very confident on that.

Ankush Agarwal: Secondly, just a clarification. You mentioned that on the ARV business side you are not expecting to pass on the prices like the cost, right and you will be maintaining similar prices to our customers. Was that…?

Dr. S. Chava: We do have the ability to pass on part of the cost increases to the customer, we are already talking to them but for the new orders what customers will place, for the existing orders what they have placed, we are honoring at the same prices, that is the kind of distribution we built in the industry. We never went back to customers for a new initiative but the new orders we are already negotiating and we will certainly pass on the price increases partly if not fully.

Ankush Agarwal: And this is for both ARV, API and FDF, right?

Dr. S. Chava: Yeah, that will be in ARV API, not FDF.

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

Krish Mehta: I had two questions. The first is could you share the number for the share of non-ARV revenue for the quarter?

Dr. S. Chava: Out of Rs.527 crores, 36% of API revenue came from non-ARVs.

Krish Mehta: For the entire business including FDF?

Dr. S. Chava: I don't have the number right now.

Krish Mehta: I just wanted to clarify on the CAPEX for Q2. Could you please just restate that number?

V V Ravi Kumar: What we are saying is the majority of Rs.1,700 crores what we have guided for the for two years will be spent in this year, maybe in full year we may spend around Rs.1,000 crores.

Moderator: The next question is from the line of Harit Ahamed from Spark Capital. Please go ahead.

Harit Ahamed: On the formulations side we are expecting to complete the Brownfield expansion of 4 billion tablets by the end of this year. So, can we expect revenues from these expanded capacities from early FY'23 or should we wait for a period of filings or site transfers and inspections before we start commercial supplies from this expanded capacity?

Dr. S. Chava: It will start giving revenues from FY'23 itself. We don't need any new site approval. We are planning to have inspections required in Q4 FY'22 itself. Already scheduled by the authority. So, we don't see any challenges of product approval or regulatory approval to utilize our Brownfield expansion in the formulations.

Harit Ahamed: Again, on the formulations side, can you talk a bit about our filing strategy in terms of what are our priority areas, will we go beyond oral solids or will we stick to products where we have strong API capabilities and then how should we think of R&D spends in this context, so currently

we are filing almost entirely in oral solids. So, will we think of going beyond oral solids into let's say injectables and other dosage forms?

Dr. S. Chava: As of now, most of our commercial products are immediate release. Only one is modified release. We are going into the modified release dosage form-V and we are also developing more complex generics which we will file one by end of FY'23 and other one in FY'24. Apart from the oral solids, we also clear on going into sterile manufacturing and our R&D will be ready by end of Q4. For that, we started recruiting talent and we are building a portfolio and some partnerships too. We decided to go into other delivery forms into injectables.

Harit Ahamed: On Molnupiravir, we mentioned we will look at getting a license from MPP like you've done in the past for other products. So, what are the next steps and what's the kind of timelines that we should think of in terms of licensing?

Dr. S. Chava: It's only expectations. FDA has to approve in their 30th November meeting and then the local regulatory DCGI has to approve. Our files are pending with DGCI. We do hope they will take a decision after FDA approvals by end of November. If approval comes, we are ready to take the opportunity.

Harit Ahamed: Will be supplied in India as well along with the MPP designated regions?

Dr. S. Chava: Many people will approach MPP for licenses. As I mentioned we have a very long successful partnership with MPP. Probably very challenging to say whether launch will happen in this quarter but definitely we do hope the products will be launched across the low, middle income countries by January for sure.

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

Nitin Agarwal: Dr. Chava, you mentioned in your opening comments about the billion-dollar aspirational target for FY'23. You're saying that you don't see any issues in achieving that subject to the timely ANDA approvals. So, is this a target for us contingent on some few specific approvals, largely contingent on that which makes it sub-sensitive to these?

Dr. S. Chava: Majority of the capacity what we are getting in the formulations will be utilized to our partner in Europe where actually they have done site transfers already, include our site in the dossier. Sites are under review. Regulators have already scheduled a visit to our site in the first quarter of the calendar year next year. We don't see that will be an obstacle in commercializing our products.

Nitin Agarwal: On the USFDA that you mentioned, are there any large approvals which are pending approval from the FDA that may impact our target?

Dr. S. Chava: There were three, four approvals pending but not because of facility inspection. There were queries on the DMF and ANDA but in a normal course only. So, we do expect significant approvals coming in next eight to nine months.

Nitin Agarwal: On the Synthesis business, two questions; one is on the contract that you signed up, so by when does the full impact of this contract start to get visible and how meaningful can it get, what's the current size?

Dr. S. Chava: We can't give you specific but we are investing already with existing investments; we are investing close to Rs.450 crores to service the contract and we do hope full productivity will be realized in FY'25.

Nitin Agarwal: Apart from this particular contract that we've signed up, how is the traction on the other potential partnerships or pipeline of products?

Dr. S. Chava: Now, we are very bullish on our CDMO division than we were bullish previously. That is the reason we are investing more into this division. We have a very interesting project from the bag line and we are adding more resources and R&D also for the division. So, this division will do very well this year as well as in the years to come.

Nitin Agarwal: These would be again as you mentioned in the category of steroids and the high potency molecules largely, these business that we're getting?

Dr. S. Chava: It's a combination. See, we have largest capacity to handle high potent. That became our unique offering and large volume. So, it is a combination of potent molecules as well as large volume molecules, it is a combination of those.

Moderator: The next question is from the line of Cyndrella Carvalho from Centrum Broking. Please go ahead.

Cyndrella Carvalho: Just a take on the site, earlier you had mentioned that we have two molecules in Phase-3. Could you help us with some more details and any update on those and the outlook ahead?

Dr. S. Chava: From last quarter to this quarter there is no further update from those two molecules, they are still in the Phase-3, no further update available.

Cyndrella Carvalho: Sir, if we understand the raw material inflation which is ongoing, what is our sense as of now and do we have any mitigation strategy or these being the basic solvent kind of variety we have to wait until this storm settle down, so how should we look at these raw material inflation scenario as of now and what is your sense on it if you could help us with that?

Dr. S. Chava: The mitigation strategy is to backward integrate to that we already achieved and other mitigation strategy is we have very good inventory so that we will not be vulnerable to the disruptions in operations, that also we have done. The other one is we can't make solvents and reagents. So, that's where a lot of volatility we have seen. We are closely monitoring and if there is a significant volatility, partly we will pass it on to a customer for the future orders as well.

Cyndrella Carvalho: But sir on the backward integration side, would we need any additional CAPEX or is it something that you are planning or is it already done?

Dr. S. Chava: Already done. We are not investing additional CAPEX to do this because this is part of our strategy which we have executed or executing.

Cyndrella Carvalho: To carry forward this, if we look at any ARV tenders which would be upcoming with these inflationary costs also would be part of the standard pricing, any thoughts on that?

Dr. S. Chava: These standards are multi-year standards, so you have to wait and watch on how the pricing will move.

Cyndrella Carvalho: If we have to take the ARV business, how is the volume traction, any demand scenario change that you are seeing given the slight weakness that we have observed?

Dr. S. Chava: Demand has been less during the Q1, Q2 and we do expect by end of Q3 the demand will pick up and Q4 we do believe it will be quite normal.

Cyndrella Carvalho: Sir, one clarification on Molnupiravir with MPP. This would be for the LMIC market, right, and on the formulations side if I understand it correct?

Dr. S. Chava: Yes, it's for the LMIC market for the formulations.

Cyndrella Carvalho: And the API for Molnupiravir would be sourced from Merck's entity or you will be also working on the API side for the formulations?

Dr. S. Chava: As part of the agreement, API manufacturing can also be done in-house and it will be in-house.

Moderator: The next question is from the line of Aditya from Carlisle. Please go ahead.

Aditya: I just wanted to clarify on a couple of things. What percent of the raw material costs would the solvents be?

Dr. S. Chava: Purchase of solvents overall is between 5% and 10% depending on the products.

Aditya: Over the last six to nine months what is the kind of inflation that you have seen in those prices?

Dr. S. Chava: The significant increase in price happened in the last week only. Some solvents went up by 10%, some solvents went up by 50%, some solvents went up by 200%, this varies, some solvents prices are normal, for example, ethanol prices were quite stable rather a little lower than what we anticipated, some solvents went up significantly

Aditya: GM impact of this price increase according to you will be visible with a lag in a month or two given that will get built into the inventory, right?

Dr. S. Chava: As we are saying, some solvents constitute 6%, 7% and I think this will not disrupt the overall gross margin level. This may influence but this will not disrupt.

Aditya: On the formulations side are you seeing any cost pressures as well?

Dr. S. Chava: Majority of our revenue coming from LMIC, ARV and contract manufacturing to European partner and sales in Canada and yes, we fortunately haven't seen much pressure on the pricing as yet.

Moderator: The next question is from the line of Gagan Thareja from ASK Investment Managers. Please go ahead.

Gagan Thareja: My first question is around the API contracts that you have talked off in your presentation. Are these off patent or are they on patent and you're going to supply for them?

Dr. S. Chava: It's a combination.

Gagan Thareja: Seems a lot of your foreseeable future opportunity for growth comes from one, this contract and the other is the EU supply contract which I presume will be an off-patent formulation contract. Are the margin profile for these supplies comparable to what you have currently or are they different or markedly different from that?

Dr. S. Chava: We don't see any margin contraction by entering into the CMO partnership whether in formulations, API, we don't have that challenge.

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

Nimish Mehta: Just wanted one clarification on the formulations sales. You mentioned that our sales will come back to Q4 FY'21 level which is actually much lower than what we have reported today, so Q4 FY'21 was Rs.495 crores you reported.

Dr. S. Chava: I said we will come back to Q4 FY'21 number, but that's on API, not for the formulations.

Nimish Mehta: Any broad guidance on the formulations sales on the same front?

Dr. S. Chava: Formulations sales, we have done much more than our Q4 FY'21 of Rs.430 crores, in Q2, we have done Rs.490 crores. We are not comparing our formulations number with the Q4. As I mentioned the Q3, Q4 we do hope to do one in the formulations side.

Nimish Mehta: The second question is again some clarification on the raw material pricing. You mentioned that we are not really exposed to pricing related to intermediates, but we are exposed to solvent pricing. So, does this mean that we are kind of fully backward integrated on the intermediate manufacturing?

Dr. S. Chava: Yes, you can be clear, we don't buy any intermediates, everything is made in-house.

Moderator: The next question is from the line of Harit Ahamed from Spark Capital Advisors. Please go ahead.

Harit Ahamed: So, on Laurus Bio, we've seen a good ramp up on a quarter-on-quarter basis. So, can you comment a bit on the margin profile of the business versus FY'21, have we seen an improvement now that the revenue run rate has picked up? And if you could also give some sense of the revenue potential once we have all the four new reactors up and running?

Dr. S. Chava: If you look at the first half of current financial year, we have partly closed and in the second half we will do more than the first half, that is clear, and margin is good. We can't give you specific numbers because we are not publishing margins for the division-wise, this is a very good margin business for us.

Harit Ahamed: LSPL unit-I facility which we commercialized last quarter, how has the ramp up been so far and then should we expect FDA and other regulators to audit the facility in the near term and then is the ramp up really linked to these inspections?

Dr. S. Chava: We had one virtual audit by FDA for pilot plant which was concluded two months back and they have sent a satisfactory letter because they have visited, so they don't give an EIR. So, there are no approvals pending from the pipe and we don't have any pending inspections from FDA, last inspections we had in 2019, we don't have any pending instructions, none of our approvals are our partners approvals were held because sites were not inspected by regulators.

Harit Ahamed: So, the subsidiary, LSPL that we have, we've talked about this subsidiary getting into a stage of independent existence on its own. So, will we be consolidating our CDMO-related manufacturing facilities under this subsidiary in the near to medium term, is that something that they're looking at?

Dr. S. Chava: We are not consolidating. Whatever the new manufacturing infrastructure required for the CDMO business, we are creating a dedicated site. CDMO already utilizes capacities which are already available with the parent, they will continue. So, it is not easy to move manufacturing from one site to another site for these molecules. So, existing business they will continue to use these parent capacity, the new capacities are created exclusively from the division. I hope this answers.

Moderator: The next question is from the line of Charulata Gaidhani from Dalal & Broacha. Please go ahead.

Charulata Gaidhani: In terms of CDMO what is the contribution to revenue that you expect going forward?

Dr. S. Chava: In the past six months we have done 350 crores revenue in the CDMO business. For FY'23, we expect it will be 15% and it is going up, so we used to have 10% till 2019, we do hope this business will contribute more from FY'24 onwards, when we commercialize the new sites, this division will start contributing more.

Charulata Gaidhani: How many customers do you have as of now?

Dr. S. Chava: We have good number of customers from virtual to small biotech to big pharma and we are adding a few new clients as well.

Charulata Gaidhani: My second question pertains to FDF. How many launches are you planning in FY'22 and '23?

Dr. S. Chava: FY'22 we will launch only one more in US, two in Canada but FY'23 we expect to launch five in US and two in Europe.

Charulata Gaidhani: Are you witnessing any price erosion especially in the diabetes segment and cardiovascular?

Dr. S. Chava: Formulations in cardiovascular is contract manufacturing. So, we are insulated from the pricing. We also make API there. So, in the diabetes for Europe also, it's mostly contract manufacturing. So, we know at what price we produce API and we know what price we produce formulations. So, that's where we have greatly insulated from the price drops during the launch.

Moderator: Ladies and gentlemen, due to time constraint, we take one last question from the line of J Modi from Emkay Global. Please go ahead.

Jay Modi: Sir, I had a question pertaining to debt. So, from current level of 1,800 crores will we be looking to pay down debt or maintain at current levels?

V V Ravi Kumar: It may increase slightly more by end of this year but from next year onwards it will come down.

Jay Modi: What would be our current cost of debt?

V V Ravi Kumar: Around 5%.

Moderator: I now hand the conference over to the management for their closing comments. Over to you sir.

Dr. S. Chava: Thank you, everyone for your insightful questions and we wish all of you a very healthy and safe festive season and happy Diwali.

Moderator: Ladies and gentlemen, on behalf of Ambit Capital that concludes this conference. Thank you all for joining us and you may now disconnect your lines.