Syngene International's Q4 FY 2023 Conference Call

April 27, 2023

Key Participants from Syngene International

- Mr. Jonathan Hunt: Chief Executive Officer
- Mr. Sibaji Biswas: Chief Financial Officer
- Dr. Mahesh Bhalgat: Chief Operating Officer

Moderator: Ladies and gentlemen, good day, and welcome to fourth quarter ended March 2023 Financial Results Conference Call of Syngene International 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 star then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Ms. Avantika Mishra from EY. Thank you and

Avantika Mishra: Thank you, Yashashri. Good afternoon, everyone. Thank you for joining us on this call to discuss Syngene's Q4 FY '23 financial and business performance. From the management side, we have Mr. Jonathan Hunt, MD and Chief Executive Officer; Mr. Sibaji Biswas, Chief Financial Officer;

and Dr. Mahesh Bhalgat, Chief Operating Officer. Post opening remarks from the management, we will open the line for Q&A, and we'll be happy to answer any questions you may have.

Before we begin, I would like to caution that comments made during this conference call today will contain certain forward-looking statements and must be viewed in relation to the risk pertaining to the business. The safe harbor clause indicated in the investor presentation also applies to this conference call. The replay of this call will be available for the next few days, and the transcript will be subsequently made available.

With this, I now hand over the call to Mr. Jonathan Hunt. Thank you, and over to you, sir.

Jonathan Hunt: Thank you. Good afternoon, everybody. Thank you for joining us. Let me start with an overview of the fourth quarter before summarizing the full year. I'll then hand back to Sibaji to give you a more detailed insight and talk about guidance for the year ahead. Syngene's fourth quarter revenue from operations grew by 31% over last year, and was, in fact, our biggest quarter ever. As a result, we had a strong end to the year with positive performances across all four divisions. Profit performance was also strong with operating EBITDA for the quarter, up 26% to INR314 crores and profit after tax, PAT, was up 21% year-on-year to INR179 crores.

Turning to the business highlights for the quarter. Our research businesses, discovery Services and dedicated centers delivered sustained good performances. The growth in discovery services was led by the continued surge in demand we are seeing for chemistry which is delivered in part by our research facility in Hyderabad. That facility is expanded further in the fourth quarter and now accommodates almost 900 scientists.

In development services, the fourth quarter is often the largest of the year. This year was no exception and I'm pleased to report a sustained performance there. Growth in development services came mainly from orders from existing clients. This increased client stickiness, I think, really reflects our focus over recent years on operational excellence and on-time delivery. In manufacturing services, after successfully completing audits of our biologics facilities by the USFDA, EMA and the MHRA, we had a busy quarter supporting the long-term partnership that we have with Zoetis.

So let me spend now a few moments reflecting on the full year. I'm pleased with the progress throughout the year and in many ways, this fiscal year proved to be an important one in the delivery of our long-term strategy. The year saw a material progress in our manufacturing division, as I just mentioned. Alongside the continued good progress in

discovery services, the sustained improvement in service delivery and operational excellence in development services gave us a much broader base upon which to grow.

Our strong performance in the fourth quarter added to performance over the course of the year and ensured that we delivered full year results ahead of our upgraded guidance. On the financial side for the full year, we reported revenue from operations up 23% to INR3,193 crores and profit after tax was up 10%. From the start of the year, we saw many pharma clients were keen to make up for time that they felt they lost during the pandemic. This client base was supplemented with growth in the number of collaborations that we have with small and medium sized research-based companies.

We also celebrated the 25th anniversary of our partnership with BMS a few weeks ago. This collaboration, as you know, started out with a handful of scientists in a single lab. It is now BMS's largest R&D facility outside the US, accommodating several hundred scientists. The partnership with Zoetis is also a long-standing one. Although the 10-year manufacturing agreement is relatively recent our collaboration with Zoetis started back in 2011 and over the past 11 or so years we have undertaken research and development work on a number of monoclonal antibody projects for use in animal health.

Other highlights thinking about the year is the high operating standards which is the hallmark of the company and the year saw several notable successful regulatory inspections. In addition to the successful audits of our biologics facility, we completed almost eighty other regulatory and client audits during the year. The latest one of those was the successful completion of the GCP audit by NABL, the National Accreditation Board for Testing and Calibration Laboratories, which endorse Syngene scientific standards for clinical trials. While we take pride in our external audit track record, we know it really only comes from a meticulous and daily commitment to compliance, and we really don't take any of that for granted.

During the year, we continued to invest in building capacity. Let me give you some examples. Our campus in Hyderabad added around 400 scientists during the year. We commissioned a dedicated PROTAC facility that's part of Syngene's novel drug discovery strategy for clients involved in cancer and other treatments. In Bangalore, a state-of-the-art sterile clinical scale fill finish facility was commissioned and that adds to our end-to-end capabilities in development.

And finally, a kilo-scale lab for polymers and speciality materials was also commissioned during the year. Another important area of focus was our supply chain where we took steps throughout the year to increase

supply resilience. We increased the number of suppliers we have outside of China, added more suppliers here in India and we took steps to improve our overall supplier ecosystem.

Looking ahead, we see industry's trends for our sector that are positive. and although there are two macro trends that are yet to fully play out for our clients in biotech and pharma so let me comment a little bit more on those. Firstly, there are financial pressures coming from increased end product pricing, high inflation and higher interest costs, and we can see those pushing pharma companies to think more carefully about how to optimize their operating models and budgets. For some, this is making them much more cost conscious. And I would say that's not a bad thing for a business like Syngene given that we have a relative cost advantage.

For others, it's leading them to consider their total size of their operations and even bring into play thoughts on their own internal infrastructure. You have seen a number of these trends reported over the last year in the media. So overall, I think this is likely to increase the trend for outsourcing and that, I think, is a net positive for a company like Syngene.

Secondly, in the emerging biopharma segment, while we've seen a slowdown in funding in 2022 compared to the previous two years, I think

you'd note that the previous two years were some of the highest funding environments we've ever seen.

The share of industry -- share of the industry pipeline coming from those biotech companies continues to increase. And the current focus for many of these companies is how they extend their cash runway while keeping their promising scientific programs moving forward. And here, we think, of course, the breadth of capability and the relative cost advantage of Syngene offers can be attractive to them.

So, in conclusion, I think we had a good year on multiple levels. Syngene's revenue performance was positive. We beat the upgraded guidance. And I think we're starting to set a new trajectory as a positive one for the company. We saw good evolution in growth across all of the businesses. Discovery Services had a good year, and that was led by a sustained uplift in chemistry.

We made good progress through improved operating performance in Development Services. That was reflected in the number of repeat orders from existing clients and manufacturing had a strong year, led by the commercial-scale biologics manufacturing business. There, the long-term deal with Zoetis and the successful regulatory inspections sets the solid foundation for the future.

So, looking ahead, I think we're optimistic and that's despite the challenges of inflation, geopolitics and recessionary pressures that are visible in some regions of the world. I believe that our performance over the last year and the progress we've made on the strategic development of the company position us well for the year ahead.

So, with that, let me hand over to Sibaji to walk you through the financial performance and also to cover guidance for the year ahead.

Sibaji Biswas: Thank you, Jonathan, and a good afternoon to everyone. Fiscal year 2023 was a year after the pandemic, and I'm delighted to report that our company demonstrated remarkable resilience and emerged stronger than before. With a robust business model, a broad customer base, a strong balance sheet and with focus on execution, our company has delivered a very strong year-on-year increase in revenue and EBITDA.

The performance in the fiscal year 2023 has beaten the upgraded guidance and provided a strong foundation for our future. Before we delve into the detailed performance for the fourth quarter, I want to remind you that as in previous quarters, I'll be referring to the underlying performance. This is performance that excludes the impact of COVID-related remdesivir manufacturing, which provided a onetime revenue and profit stream in the previous fiscal year. As we have no remdesivir sales in the financial results that we are reporting today, it is useful to

exclude remdesivir from both periods to focus on the underlying performance of our ongoing business.

As Jonathan mentioned, the revenue from operations in the fourth quarter increased by 31% compared to the same quarter in the previous year, while the underlying revenue growth, excluding the remdesivir was marginally higher at 33%. We have seen continued good performance from the Discovery Services division, which grew steadily on back of healthy demand.

The Development and Manufacturing Services division as a whole grew by 42% year-on-year benefiting from repeat orders from existing clients in the small molecule development business and increasing collaborations with emerging biopharma companies. With the regulatory approvals in place, this quarter also saw the start of manufacturing of drug substance at commercial scale for Zoetis, which also added to the strong year-on-year growth. Reported EBITDA for the quarter saw a year-on-year increase of 27% amounting to INR337 crores, up from INR265 crores during the same period last year.

Reported EBITDA margins for the quarter was 33.1%, down a little compared to 34.3% in the previous year. EBITDA from operations, excluding other income came in at INR314 crores, up around 26% compared to the same quarter last year. The corresponding operating

EBITDA margin that is without other income stood at 31.6% for the quarter compared to 33% in the previous year. EBITDA margin was lower primarily due to hedge losses booked this year versus hedge gains in the previous year.

Now turning to the key elements of cost within our business. Material costs for the quarter increased by 37%, reflecting a shift in the business mix towards manufacturing services, and an increasing proportion of early-stage clinical manufacturing projects that carry higher raw material costs. The quarter saw a year-on-year increase in staff cost of 41%. I would like to remind you that the fourth quarter of the previous year had the benefit of lower costs relating to retirement benefits arising from higher level of attrition. Adjusted for this, the staff cost growth is in line with increase in headcount and annual pay rises. Other direct costs increased by 15%. The company's investment in renewable energy helped to reduce carbon emissions and mitigate rising energy costs. Despite the expansion of facilities and the surge in power tariffs, we successfully controlled the overall expenditure on energy in the company through green power. However, the inflationary pressure on the rest of the utilities, especially gas has partially offset the benefits we are getting from our investments in renewable energy.

Other operating expenses, which includes business travel, sales promotion and other overheads increased by 4% compared to the same quarter last year when the activities had already moved up to the near normal levels.

Revenue for the quarter was hedged at around INR79.5 per U.S. dollar and the revenue and margin guidance were given on the expectation of revenue realization around the hedge rate. The average spot rate, however, during the quarter was around INR82 per US dollar.

The EBITDA margin for the revenue listed at the hedge rate came in at 31.7% compared to 32.6% in the previous year. The company saw hedge losses of INR4.2 crores during the quarter compared to a hedge gain of INR9.1 crores in the fourth quarter of the previous year due to the difference between the average spot rate and the hedge rate.

Depreciation and amortization for the period increased by 19% year-on-year to INR95.5 crores, the increase is attributable to new investment in facilities, equipment, and infrastructure. Finance costs increased from INR5.6 crores to INR10.6 crores due to the rising interest rates and translation losses on foreign currency borrowings. Other income for the period increased by 55% to INR 22.8 crores, which was driven by the increase in cash balance and better yields on bank deposits and other instruments.

Profit before tax increased by 29%, profit after tax was INR179 crores compared to INR148 crores last year, registering year-on-year growth of around 21%. The difference in growth rate represents an increased effective tax rate of 21.8% in fiscal year 2023 as compared to the previous year's rate of 18.3%. This increase in tax rate is due to some profit generating units coming out of the SEZ tax benefit during the year.

In summary, the fourth quarter demonstrated sustained positive performance leading to strong full year results. Now I'll comment on the full year performance. Reported full year revenue from operations exceeded our guidance with a year-on-year increase of 23%. This reflects good performances from all divisions.

Our CRO businesses delivered growth over 20% and constitutes 65% of the revenue. The CDMO business grew by 28%, driven by the start of commercial manufacturing biologics and a healthy level of repeat orders from our clients in small molecule development services. EBITDA from operations grew at 17% year-on-year, the gap in growth rate between revenues and EBITDA is mainly due to the hedge losses booked during the year as against the hedge gain booked in the previous year.

Reported material costs showed a relatively lower year-on-year increase of 15%, mainly due to the base effect of remdesivir manufacturing in the previous year, which had high raw material costs. Adjusted for that, the

underlying material cost growth is a bit higher than the revenue growth due to the shift of business mix towards manufacturing. The overall material cost to revenue ratio now stands at around 27% of revenue, which is within the range guided by us in our previous calls.

Staff costs for the year increased by 20%, in line with the headcount growth and annual increments. Overall staff cost to revenue ratio stands around 28%, which is very similar to the previous year. Other direct costs increased by 27%, reflecting the inflationary pressures in utilities. Other expenses grew by 25%, driven by the resumption of activities post pandemic and other operating investments.

The EBITDA margin from operations for the 12 months period was at 29.3%, 130 basis points lower than the previous year's margin of 30.6%. However, if the revenue is restated at the hedge rate, which was incidentally the basis of our guidance, the EBITDA margin came in at around 30%. Depreciation and amortizing expenses for the year increased by 18%, reflecting capex additions.

The operating EBIT that is EBIT without other income increased by 17% in line with operating EBITDA. However, the interest expense for the year increased from INR24 crores to INR45 crores, driven by rising interest rates and translation losses on foreign currency loans. This is an

increase of 87%. The higher increase in interest cost and increase in effective tax rate, resulted in a PAT growth of 10% year-on-year.

Profit after tax was at INR464 crores which is above the guidance of single-digit PAT growth that we had given before. The capex guidance for fiscal year 2023 was for a spend of about USD 100 million. We recorded a capex spend of around USD 60 million and another USD 30 million has been committed. These projects relate to expansion of research, much of which will happen in Hyderabad and Biologics. The projects are currently under execution and has rolled over to the current year that is FY '24 for completion. To give you the breakup of capex for fiscal year 2023, about 60% of the capex in the reported period was deployed in research services expansion, another 35% was spend in CDMO business to scale up the existing biologics facility and add clinical scale injectable fill-finish facility amongst others. The rest of the capex was spent on common infrastructure, especially on digital technologies.

Now let me spend a few minutes on the guidance for FY '24. We expect the contract research, development and manufacturing market to continue to see growth with key fundamentals remaining strong. For the year ahead, we see healthy demand for our services on the back of global pharma and biopharma companies continuing to diversify their supply chains. With stable revenues in the dedicated center, good growth in

Discovery Services, healthy repeat and new business in development services and start of commercial manufacturing in biologics, we anticipate revenue growth on a constant currency basis to be in the high teens.

I want to emphasize that this guidance is being given at a constant currency. This is a change from what we have done in the past where our guidance was given in our reporting currency, that is Indian rupee. The average conversion rate realized in FY '23 was around INR81 per U.S. dollar and the growth rate in the reporting currency will depend on the spot rate prevailing during the year.For record, our average hedge rate for the year ahead is INR81 per US dollar which is similar to the average spot rate realized last year.

In the year ahead, we will continue to invest in building capabilities and expansion, which will lead to additional expenditures in our P&L. However, we expect our EBITDA margin to remain at around 30% for the overall business. This is, of course, assuming revenue realization at INR81 per U.S. dollar and it could change based on the actual spot rates seen during the year.

As mentioned earlier, in fiscal year 2024, we expect better operating leverage with EBIT growth actually tracking the revenue growth in the year. As explained earlier, the effective tax rate is expected to gradually

increase, and we expect the effective tax rate to be around 23.5% moving up from 21.8% in the fiscal year 2023.

The increase in effective tax rate will continue to provide headwinds for our profit after tax and hence, we anticipate that the growth in PAT or profit after tax will be in the mid-teens. New capex for the current year is expected to be around $70 million. With $30 million rolled over from the previous year, total capex spend will be around $100 million. Most of the investments will be focused on adding biologics manufacturing capacity, laboratory space for future expansion of research business and capability additions across our service lines.

Overall, we expect to continue the growth momentum of the last year with better margins leading to improved profitability. That concludes my remarks, and I'll now open the floor for questions. Thank you.

Moderator: We have a first question from the line of Prakash Agarwal from Axis Capital.

Prakash Agarwal: Thanks for the opportunity and congratulations on good numbers. Sir, first question on a little bit clarity on the guidance. So, I'm not sure if you talked about the revenue growth guidance, but margins, you said in the first statement that EBITDA margin likely to be around 30, 31 and then in the closing comment you said expected to see operating leverage and

margins to improve. So, two questions there. One is on the top line growth, if you could give some color for '24 and about the margins also? Thank you.

Sibaji Biswas: Yes, I'll take it. Thanks, Prakash, for that question. What we clearly said in the guidance, first of all, let me repeat my revenue guidance because it appears that you haven't heard it. We said constant currency growth will be high teens. And this is a change from the past. We are giving a constant currency growth guidance this time. But we also said the operating profit or EBIT will grow at least in line with growth of revenues. We have reported a 29.3% margin in EBITDA. And hence, when we were guiding around 30% EBITDA margin, we have been basically saying that the growth in margins or growth in EBITDA and operating margin and operating profit, which will go at least in line with the revenue. Hence, the margins will not be diluted, and the expenditures will not grow more than the revenues. That's what I said. Hope I'm clear, Prakash.

Prakash Agarwal: But I mean, with Zoetis business coming in, wouldn't the margins and the throughput that we've been investing into hard times also. So, in the good times, we should have seen some operating leverage. So, I think margins should likely improve; is the understanding not correct?

Jonathan Hunt: The guidance, we summed up our view on it giving you the guidance.

Prakash Agarwal: So, is there any more investments which are going on which requires some kind of gestation when we can see revenue flowing through later? Is that one part you want to cover?

Jonathan Hunt: Yes, I mean constantly. If you look at the evolution of the company, we've been putting in ever increasing amount of capex to work year-over-year because we see good prospective returns, and we see a good reason to put our shareholders' capital to work in that way. Our total capex investment last year came in at around $60 million. We expect that to increase in the year ahead to $100 million. And it's spread across the business, about half of it is going into the Research Services division and the remainder 20% into biologics, 10% or so into Development Services and the rest, which if I do the math quick, at least about 20% would be spread across the rest of the business. So, we're investing because we're optimistic about the outlook, and we see good prospective returns on those investments.

Prakash Agarwal: And one more clarification. So, the Zoetis business would have already started, right? I mean, in Q4, there would be some upside that we have already booked?

Jonathan Hunt: Correct. Prakash, hence, while we've delivered a 31% growth in the fourth quarter. Albeit I know -- and I'm just tweaking you slightly, you described that as a good quarter, I just thought 31% might have

deserved better than just good. But it was a very good end to the year, and I think a pretty good year overall.

Prakash Agarwal: Yes. So, extrapolating that also for fiscal '24 and since we said this $500 million business from Zoetis over the next 10 years, so this would have added or will have more visibility for fiscal '24, I assume. So that will add up to the overall revenue growth. So, you were talking about high teen growth. I'm just trying to understand the math. So mid-teen growth we normally do. And Zoetis just adds a couple of basis points or should have been higher in my view, is what I'm trying to understand?

Jonathan Hunt: I leave the modelling to you. I've given you most of the inputs you need. I'm sure like most of the sell-side analysts by now, you've divided $500 million over 10 years by 10 years and plugged in something around about $50 million.

Prakash Agarwal: Yes. So, is that the right way to do?

Jonathan Hunt: I don't know. I couldn't comment on your modelling. We don't guide on an individual level. But when we announced the deal, and I was asked the same question, I shared that in absence of any more detail, that is what I would probably do.

Prakash Agarwal: And lastly, on industry trends. So, we hear that a lot of innovative pharma, the RFPs, a lot of interest in terms of the earlier RFPs converting

into business. So are you seeing more traction, especially on the innovative pharma side, on the back of where we hear that small biotech companies are having funding crisis, etc. So just comments on the industry, what you are seeing from a client base from the innovative pharma side as well as smaller...

Jonathan Hunt: If you look at the comments I made, I tried to cover some of those. There are multiple moving parts at the moment and we're all going to make our own judgment on what we think the net position will be on all of these. And it will vary company by company and also client by client. But some of the sort of macro trends.

Firstly, I don't think the acceleration to catch up with lost time during the pandemic has played out fully. There are still companies that are pushing hard, recognizing their programs went a little bit slow in the 2, 2.5 years or so of the pandemic. And remember that many of these innovative assets are patent protected, and therefore this is the time that's incredibly valuable in the innovative biotech and pharma industry. So their only incentive is to try and recover time lost. So that there's one macro trend.

Secondly, I think it's the pandemic, but also geopolitics. In all the industries, people are thinking very carefully about the globalized nature of supply chains, where you get work from, where you get raw materials

from, how your supply chain gives your business a sense of resilience. And there, I think you can see people looking at dual sourcing and just rebalancing in various ways.

Now what that means for individual companies depends on their starting position. Some are heavily exposed to China. They may as well lessen that and rebalance to other regions of the world. If some are massively exposed to, say, their domestic market. I've seen examples of very US-centric clients actually looking to globalize because they're just looking for that dual sourcing and some resilience.

Now for some of you, that becomes a China plus 1 story. And I think in reality you can see growth coming from that. So, if you put those together, first thing is around economic pressures, most visible in the western markets, the U.S., North America, Europe, clearly, you're seeing unusually high inflation in those countries that's driving up labor rates for many companies. You're seeing higher interest rates. So, the cost of cash and cost of funding new business is going up for some.

And in the emerging biotech, you've seen a drop down from what was an all-time peak. So those that have funding are very keen to make it go as far as possible. I think I gave you three big building blocks of macroeconomic factors. And then you have integrate those and come to your own conclusion.

Mine is that I think at a firm level for Syngene, they offer some good opportunities. We have a relative operating cost advantage to our clients and some of our competitors in the west. But that means that we can make the R&D dollar go a little bit further to some of those clients.

We have scale and capability. So, in most cases, if a client comes with a particular request, we actually have the infrastructure, the people, the talent to be able to meet it. We don't often turn the work away because it's not the capability we have. So, the strategy being quite broad is working for us. And then we have a geographical advantage, which is in a China plus 1 world, we may well be the plus 1. So, did that help, Prakash?

Prakash Agarwal: Yes, very helpful. Thank you. I'll join back the queue.

Moderator: We have our next question from the line of Harith Ahamed from Avendus Spark. Please go ahead.

Harith Ahamed: Good afternoon. Thanks for the opportunity. My first question is on your parent, Biocon shareholding in Syngene. So, you have seen during the course of the year, that declined from roughly 70% to around 55% currently. So, my question is whether you have any indication from the parent company on their plans in terms of their shareholding in Syngene.

I'm asking this in the context of the parent company continuing to look at various avenues to raise capital to support their other businesses.

Jonathan Hunt: Yes. I think you know that I'm going to disappoint you by saying it would never be something that I would comment on, on any of our shareholders to be honest, it doesn't matter whether it's Biocon, whether it's any one of our myriads of investors. It's not management's job to comment on other people's investment horizons, holdings and plans. But that's a super question that I'm sure when you re-join the Biocon conference call, you'd be able to ask them.

Moderator: We have a next question from the line of Lavanya Tottala from UBS. Please go ahead.

Lavanya Tottala: Hi, thank you for the opportunity. Congratulations for very good set of numbers. And I just wanted to check on API plant FDA approval timelines that how you are seeing going ahead?

Jonathan Hunt: It wouldn't be a quarterly analyst call without such questions. So, thank you for throwing that one out. The expectations haven't changed. We're working with the FDA to come. It's down to their travel schedule and the logistics. But my expectation would be in the coming quarter. But very happy to have another go at answering that in a quarter's time.

Lavanya Tottala: Got it. So, I just wanted to understand one thing that the global player BMS have opened their one of the facilities in Hyderabad. So, do you see this as a risk? It might not be in the near term? Do you see anything about that in long term that it shifts from outsourcing to in-sourcing, any thoughts there?

Jonathan Hunt: No, not really. Firstly, I had very good visibility of that happening. And while you may have read it as a surprise in the media. It wasn't a surprise to us. We have a super, super working relationship with BMS, and they've definitely made sure that we were well aware of their plans.

I would make a really obvious statement, the capabilities of their planned center in Hyderabad has a range of things that Syngene don't offer and is not part of our strategy. So, I see no operational conflict with what we do with anything. I think it's a healthy indication of BMS' confidence in the relationship they've had with us, the experience they've had with us in India. And it also reflects more broadly the emergence of the Indian economy.

I think we all need to get used to it. You'll see people coming from all over the world to invest in India because there's an immense amount of talent, economic opportunity, scale. The domestic market is becoming bigger in many more industries. Flying from the airport of Bangalore, I am struck by the number of international executives that are coming in

and out. So, I think it's a healthy sign to the environment. If it builds more talent, that's a good thing for us. But on the specifics of the center that they announced in Hyderabad, it doesn't do anything that we could have done for them. So, it's off strategy for us. And I think we have a healthy relationship. Does that help?

Lavanya Tottala: Yes. If I may squeeze in one last question. So, I just have a doubt on the hedge rate. So, hedge rate for the current quarter was around INR79 and the spot was close to INR81, INR82, but this is a similar level that we have seen last quarter also but this time the hedge loss was relatively much lower. So, I just wanted to understand why is the difference between last quarter and this quarter?

Sibaji Biswas: Yes. So essentially, we carry a hedge book and the hedge rate that we had during the year quite anywhere between INR78 to INR80, what I was giving you a rough estimate of what the average looks like. And depending on what spot rate we got, this is the hedge loss that we have booked in the financials.

So, the numbers are very consistent in that sense. What we basically also said that the average rate is around INR81, the spot rate that we observed during the year. And next year also, we expect it to be around INR81 because our hedge book is around INR81. So, one of the reasons we gave a constant currency guidance is that we are not able to judge or

take a call on how the exchange rate will move. If it is around INR81, then the constant currency exchange rate will be almost will be similar to the reported exchange rate or reported growth. Otherwise, we'll have to make an adjustment based on where the spot moves.

Moderator: We have a next question from the line of Surya Patra from PhillipCapital. Please go head.

Surya Patra: Congratulations for the great set of numbers, sir. My first question is on the supply to the Zoetis. We are initially possibly talking about supplying to the U.S. but supplying to U.S. requires approval of the product, but that has not happened yet, so we have started supplying so possibly for European requirement. So, sir, my question is that when do you expect the approval of the products for the US market, and do you see a kind of a ramp-up in a stronger way post US approval, that is one. And second question is how lumpy or smoothened the supply would be for this Zoetis contract?

Jonathan Hunt: I think you know what I'm going to say, though, because certainly, the first one of those, that's a question that I think you have to direct to Zoetis. It would be really unfair of me or inappropriate to try and second guess what's a key business event for them and their shareholders, their views of the US regulatory approval. I don't have any special insight further .

It's actually not something I would comment on. If it's a Syngene related question, I'll try and help you a little bit to think about the modelling. But if it's a Zoetis question, I think you have to go and ask them rightly. It's really not for me to comment on somebody else's business, particularly when it's a flagship product for them. It's an important part of their strategy and real innovation in their industry. And I think you should be guided by them on that one.

But then to your second question, which I think is a bit more Syngene related, we did start some manufacturing during the fourth quarter. You can see that in strong fourth quarter we've had. I think the simplest thing, and it's the answer I reminded Prakash of in the first question on today's call, in absence of any more detail, divide 500 million by 10.

Surya Patra: But on a broader sense, sir, whether it would be a lumpy one within the year, it will not be a smoothened supply situation during the quarter, so?

Jonathan Hunt: Surya, again, if it was me modelling, I'd assume a fairly smooth flow through the year because the alternative would actually -- you could only really get to it if you were sitting on our operating floor, watching batches complete and whether or not they all finished on time or there were stop gaps and delays of an hour a day here. So, I think your best modelling assumption is divided fairly linearly through the year, looking for Sibaji to see if that makes sense.

Sibaji Biswas: Yes, that makes sense. And if you divide by 10 and then make some adjustments next year being the effectively full first year and we scale up to the maximum level. You will have the answer.

Jonathan Hunt: I mean, there's an infill error because we haven't just done a full year in in FY '23, so you have to adjust for that. Shave a bit off the first and add a bit on the end straight line it through a decade.

Surya Patra: Yes. Sure, sir. My second question is that, given the kind of supply challenges or people trying to de-risk from Chinese suppliers and the increased demand situation for the services. So, have you seen any kind of improvement in the billing rate for you or, let's say, that is what you are anticipating for FY '24 at least? Any sense on that?

Jonathan Hunt: No. But for us, I think it's a fairly stable pricing environment. I think we're more likely to benefit from volume, but we offer attractive prices that create value for us and for our customers. I'd much rather see that volume growth in a stable pricing.

Surya Patra: Okay. Sir, one clarification can I take from you. So, during the quarter that you have transferred your Hyderabad operation to Syngene Scientific Solutions wholly owned subsidiary. What is the motive behind that? And how are you differentiating the operation of Hyderabad versus the CRO operation in Bangalore?

Jonathan Hunt: Yes. I wouldn't over interpret. It's just tidying up a little bit of corporate structures and making sure that we've got all the assets that work well together in one place. So genuinely, it's more administration than it is strategy. I don't think there's anything that you can read into it. No change operationally by the way. If you're working in a lab in Bangalore, Mangalore, Hyderabad, the name on the bottom of your payslip might have changed, but other than that, nothing else changed.

Surya Patra: Okay. Sure. Sir, just last 1 clarification for the -- sorry for that. You mentioned about -- I mean, we have been associated with Zoetis in some time before we see a kind of a big positive surprise in terms of the supply contract. So similarly, we have been talking about the polymers and the fine chemicals since some time. And now we have seen some progress in terms of capability build up for polymers and fine chemicals. So, could you give some sense, some outlook there, is it right to think positively about some supply contract or something like that?

Jonathan Hunt: I wouldn't over interpret things like the polymers and the other elements. In part, when we talk to the capital markets, we're also talking to our customers. And therefore, we make sure we take every opportunity to remind them of the full range of capabilities and depth that we've got. So not everything has to be strategically significant that we're trying to direct you in the way we want you to model next.

If anything, I'd go back to the comment I made earlier. One of the reasons strategically that I think Syngene is doing well and we're progressing is that we did deliberately choose to be broad in our capability offering. We want to be one-stop full serve and therefore, we add in capabilities as much so that we have them, so we never turn the client away, but not all of them are going to always scale up to be big individual business lines, but they do play their part. So, we're very happy when a client comes that we can say we can go on the full journey with you from discovery to development to manufacturing. Does that help at least the context of the answer?

Surya Patra: Okay. Okay. Sure.

Moderator: We'll take our last question from the line of Cyndrella Thomas Carvalho from JM Financial. Please go ahead.

Cyndrella Carvalho: Thanks for the opportunity and congratulations on good set of numbers. The question to my mind is how much of success are we seeing from making available manufacturing facilities for our existing customers? How much of success do we see? What is the ratio that you have right now? And how much of it will be visible in the coming 2 years going ahead? And what is the thought process on that? And the second is, can you explain the gross margin change Q-on-Q that has happened?

And if any, is it driven largely by the product mix? If yes, can you please explain it?

Jonathan Hunt: Let's see those in reverse order now, I will give Sibaji a chance to talk about gross margins, they do bounce around a lot. So, which is why we tend to give commentary on where we see it strategically and on a full year basis. So, a week over week, month over month, quarter-over-quarter, you'll see quite some swings on a whole number of things. But full year picture usually makes most sense.

Sibaji Biswas: And I think, you are absolutely right. So, in quarter four, we had seen a big increase in material cost because the product mix changed. But on an average, as you can see, the material cost to revenue came to 27%, and we have been guiding 27% to 28%. So, what happened in quarter four, the mix definitely changed towards manufacturing. And that pushed up the material cost consumption in the business and hence the material cost as a percentage of revenue went up. But I also need to reflect on the accounting policy that we have on how we account for raw material cost.

Typically, when we kind of charge raw material to P&L, they are from the inventory, if they are inventorized raw material or they are consumables and consumables are not inventorized. So, consumables get charged on purchase. So, when we start commercial manufacturing, we do buy

consumables for a longer period of time and not for one quarter. So effectively, what you would see in quarter four is the beginning of the commercial manufacturing and hence, consumables being charged to the P&L and the raw material cost would go up.

And that would again be different in the next quarter. But broadly speaking, depending on when consumables are basically, what it will move from quarter to quarter, but there is a definite 200 to 300 basis points shipped in material cost that you would observe because our mix has changed and that we have seen. Over the last few years, you have seen that gradually going up and 27% to 28% is what we are clearly seeing is broadly stabilizing unless it changes once again, depending on the kind of projects we are taking. Is that clear?

Cyndrella Carvalho: Yes. Yes. That's very helpful Sibaji. Thank you for that. And thanks, Jonathan. But Jonathan, coming back to my first question. How are we seeing the manufacturing viability either on the small molecules on the large molecules, what's the conversion ratio from our existing partners to move towards the full supply or the entire forward execution, what is the ratio today? And how do you see it changing or any examples that you can share, which you would have seen over last 2 years and it would help us overcoming for the year?

Jonathan Hunt: I think I get it. But sadly, I don't think I've got the facts at my fingertips to sort of illustrate it. So, I'm going to talk about the strategy, and we're actually quite comfortable that the business is rebalancing. If you think about where Syngene was at the IPO, nearly all of the revenue would have been coming out of the Discovery Services as we talk about Discovery and Dedicated research.

And since then, we've not only grown there, that business is the research business now is bigger than the whole company was at IPO. So we've done well in progressing that. But at the same time, we forward integrated through the value chain. We're building a development business and the manufacturing one.

So, they work together. It's not an either all. And that really goes back to my comment about full serve being able to do the full journey with the client on the molecule at each stage. I'm optimistic about the outlook. I think we go into FY '24 with having seen a good year, one with good strategic progress in FY '23 and pretty good momentum. So better balanced with good momentum. On that, I'm not sure I've got the facts I'm prepared to break open on each individual part of the business.

Cyndrella Carvalho That's helpful. But just was trying to understand is like 10% of our consumers are moving ahead with us in terms of going ahead in the

manufacturing side? Or is it right now where -- anything that you can share on that?

Jonathan Hunt: Yes. The reason I'm struggling to give you a number is it's just not a number we would measure in that way. It's almost not how I conceptualize it. At any given point, we've got 400, 450 plus active clients. But within them, they may have a basket of 10, 20, 30 different projects. You're not tracking them to see which ones are definitely flowing through to which next stage.

Cyndrella Carvalho: I was trying to understand if any of our manufacturing projects, which are coming to us, are they coming to us from the -- like were they with us since discovery. That was the way of looking at it like I hope...

Jonathan Hunt: That was the last chance to defend the question. I think the best example we've got is that of Zoetis in the sense that we did work with them as an organization. I put that into my comments. We have had a relationship with them not for 11 months, but for 11 years, we started back in 2011, on the research, discovery, development side, and that relationship has grown from there. So, if you look at it less at the molecule level and think about it the firm-to-firm relationship, then I think you can get a much more comfortable picture of how those relationships grow over time.

Moderator: Ladies and gentlemen, that was the last question for today. I now hand the conference over to Ms. Avantika Mishra for closing comments. Over to you.

Avantika Mishra: Thank you, everyone, for joining today's call. I hope we have answered your questions. If you have any further queries, please do get in touch with our team, and we will be happy to get back to you. Have a good day and thank you once again.

Moderator: Thank you. On behalf of Syngene International Limited, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.