Unichem Laboratories Limited
Investor/ Analyst Conference Call
January 20, 2014

Moderator: Ladies and gentlemen, welcome to the Unichem Laboratories Limited's Q3 & Nine Months FY14 Earnings Conference Call hosted by Sunidhi Securities and Finance Limited. We will start the call with all participant lines in a listen-only mode. There will be an opportunity to ask questions at the end of today's call. I would now like to hand the conference over to Ms. Rashmi Sancheti. Thank you. And over to you, ma'am.

Rashmi Sancheti: Good afternoon to all. I Rashmi Sancheti, on behalf of Sunidhi Securities and Finance Limited welcome all the participants to discuss Q3 and Nine Months FY14 results of Unichem Laboratories Limited. Today, we have with us Mr. Bhagwat Dhingra – Chief Executive, Domestic Pharmaceutical Business; Mr. Rakesh Parikh – VP, Finance and CFO; Mr. Gundu Rao – EVP, Corporate Affairs; and Mr. Monish Shah – Manager, Investor Relations. I would like to hand over the floor to Mr. Rakesh Parikh and other team members for the discussion. Over to you sir.

Rakesh Parikh: Thank you. I welcome everyone on behalf of Unichem and Sunidhi. We concluded our board meeting on Saturday to consider the results for the third quarter of financial year and the nine months. Updates were circulated and I am sure most of you all would have gone through the details.

Just to recap, the company's standalone revenue was at Rs.265 crores compared to the corresponding quarter last year of Rs.232 crores showing a double-digit growth of around 14%. And growth within India and outside India was well balanced out; within India growth at 12% and the outside India growth at 17.5%. As far as the Domestic Formulations is concerned, we have inched very close to the double-digit mark showing a primary sales growth of over 9% with the secondary's being even better which I leave to Mr. Dhingra to comment a little later.

In terms of the margins in spite of the NELM and the increase in inflationary pressures and also a slightly higher cost in terms of R&D and marketing we have still been able to keep the margin above 18% and as far as the bottom line is concerned we also had an exceptional item this quarter; If we exclude that for the quarter PAT comes to about Rs.32 crores and about

Rs.104 crores for the nine months. This is higher than the corresponding period of previous year. As you all know the company had decided to sell its SEZ unit in Indore, the closure of that happened during the quarter and the money was received. The impact of that exceptional item which is reported before tax in the SEBI results is around Rs.49 crores includes amortization of intangible assets based on estimated useful lives. The net profit including the exceptional items for the quarter comes to around Rs.74 crores. On, the company's expansion plans – one is to have similar capacity to which we have sold in the SEZ which will be ready in less than 2 years time by way of expanding our Goa capacity for which the work has already begun. We have received the basic approval from the GIDC land authority for the same. In addition the expansion of our API plants is in full swing, being implemented at the Pithampur and the Roha API plant. And on the Biosciences which is for the long-term, the capital expenditure is going on. So these plans are all under implementation. Company is also having its accruals which can fund these expansion plans. We are also looking at an opportunity to further enhance the API capacity discussions for which are at an advanced stage. In order to reward the shareholders the Board has decided to give interim dividend which is declared at 200%, coming to Rs.4 on a share face value of Rs.2. I think this would summarize the results and the numbers. I would like to hand it over to Mr. Dhingra to give overview on the India market before we go to the Q&A session.

Bhagwat S. Dhingra: Good afternoon everybody and first of all thank you Mr. Parikh for giving me this opportunity to have an interface with all the investors. To begin with I would like to wish each one of you and your families a very happy and prosperous 2014. I am sure as investors you are equally concerned as we are in Unichem to see not only your prosperity but also to see the prosperity of your customers, isn't it? Coming to the IPM, most of you have read and you must have seen that how the IPM movement is. Because most of you must be expecting that in quarter 3 IPM may bounce back to double-digit, but it has not happened because after NLEM impact in Q2, we were thinking that Q3 will bounce back at least to the double-digit but for our surprise as well as surprise of the industry, Q3 has also shown a very modest growth of single digit and looking forward to Q4 I feel that the trend will not be quite different because Q4 will also see the modest growth only.

When it comes to Unichem, I look into secondary numbers reported by AWACS, they are very buoyant and we are happy to see those numbers and these numbers are also matching to our internal secondary growth. When I am saying there is a part called as 'Primary Sale' which is a reported number where Mr. Parikh has rightly mentioned that it is into a single-digit around 9.3% but when it comes to the secondary numbers the sales which happens from stockist to retailer, they are into a positive double-digit growth. AWACS also show a similar number. So more or less our secondary number internally and AWACS have started matching now. That shows a very-very positive trend. And Q3 has really shown that the initiative which we have taken in the beginning of the financial year has started paying dividends to us. You can raise the questions which can be addressed by all of us here. Thank you very much.

Moderator: We have a question from Mr. Ravi Shenoy from Motilal Oswal Securities. Please go ahead.

Ravi Shenoy: Wanted to understand on your sales front, your API exports have moved up. And if you could give some information on any CRAMS sales during the quarter?

Rakesh Parikh: Regarding the API part of it?

Ravi Shenoy: Yes.

Rakesh Parikh: API, we do not have CRAMS per se, it is insignificant. If you see the first two quarters, API exports have shown higher growth mainly because of the lower base on YoY basis. But we are happy to say that the backlog of orders was there and in spite of the capacity constraints and our own captive requirements, we could manage to service those customers. As a result of which, we are seeing a big jump as far as this particular quarter is concerned; If you see on a nine monthly basis still the growth is robust at around 18% or so. And this is in spite of the capacity constraint which we have been talking; we have to ramp up our capacity, the expansion for which going on. So on the order front and on the marketing side there is a good potential plus we have not opened up the other regulated markets like US and may be Japan etc where we have started a small business development activity. We are confident enough of meeting the existing customers' requirements, after fulfilling our captive requirements which are there for the Formulations.

Ravi Shenoy: And on the export Formulation side any CRAMS number this quarter?

Rakesh Parikh: Yeah, the CRAMS is part of it, but as we have said for the last two quarters, the offtake especially from our CRAMS market of US has not been picking up, and it is basically flattish to negative and Europe is also flattish. No new parties or products would have come which would drive it. But it has slightly improved compared to the last couple of quarters and at this level we feel it will continue as far as the existing CRAMS is concerned in the current year. We are talking with a few more parties and for new products from the existing party but it will take at least 2-3 quarters till the commercial dispatches start. Then, we can see a jump. And having sold the SEZ capacity now, we are not having that much of excess capacity. So from that angle, we would not like to push too much. The preference would obviously be given to our filings if more approvals come in from US and even from Brazil. To that extent, CRAMS is second preference.

Ravi Shenoy: And on the US FDA front, how many products filed, approved and in the market?

Rakesh Parikh: We have 28 ANDAs filed, of which 16 have been approved, including 2 tentative approvals and 10 products have been launched. The balance products are now ready to be launched. So maybe by the end of this quarter or early next quarter we will be launching those two products. They will enable the growth to continue. Excluding that if you see the subsidiary numbers, the growth has been coming without any new additional products in the last couple of quarters or so. The subsidiary has shown about 30-35% growth in dollar terms and we expect that to continue, and to maintain it we are looking forward to some more approvals, because one filing has now crossed 30 months. Post all this it looks a promising market and there is very good buoyancy as far as sales from our own filings are concerned.

Ravi Shenoy: In terms of filing momentum, what is the likely filing rate per quarter?

Rakesh Parikh: R&D which was earlier at Jogeshwari, we started shifting the same almost about 3 odd quarters back and the new R&D centre which has come up at Goa, has been completed. That is now fully functional and they have started work on filings now. There have been some constraints on the API side, because even after the R&D completes their work, the development batches which are required, have to be done under cGMP conditions at the plant even as far as API is concerned. So that does remain a constraint for which the expansion is going on; at the end of this quarter the expansion at Pithampur should be over. So maybe from next year onwards we are looking at starting our resumption of filing which maybe one or two per quarter. We have more than 10-12 molecules which are at a very advanced stage of filing, subject to API validation batches being completed.

Ravi Shenoy: You talked about acquisition of a company?

Rakesh Parikh: Not a company, we are basically looking at a facility, because Roha and Pithampur both have API plants that are approved by various agencies including the US FDA, With Roha working at three shifts in heart of MIDC which we can't expand further. So at the most we can just do little modification and debottlenecking which we are now going to implement. As far as Pithampur is concerned, it has also reached 75% on 3-shift basis and in the next 2-3 months expansion will also be over.

So what we are looking at is how to supplement our Formulations growth, the Formulation expansion will happen at Goa, which will be much more beneficial because it is at our existing location. We have got the land which is why we sold the SEZ, once GIDC land was made available to us. For API, since there is no possibility of getting any of our neighbors land or expanding at our existing land, we are looking at acquiring a facility for which discussions are going on and two or three parties have been shortlisted, having come to a reasonably advanced stage. Maybe in the next few months we should be able to take a call on any of these facilities which will enhance our API capacities. After we take it, we will have to go for modification and if approvals are required we will have to go in for it that as well. So the capacity may not be available at least for a year plus after we complete the acquisition. But, it will be in time when the Formulations plant comes on stream.

Ravi Shenoy: On the Domestic side, in our Cardiac segment we have seen quite lot sales come under NLEM. So what are we doing to counter that?

Bhagwat S. Dhingra: As you rightly said that Losar is a product in Cardiac segment which contributes around 23% of our sale within that division. But looking into the intrinsic value of Losartan and a lot of study supporting our belief, the latest being SMSRC, I am sure that the prescription audit suggest that cardiologists and then nephrologists and diabetologists have increased their uses for Losartan by 32% over corresponding period last year. That shows that when we are going to specialist and talking to them about Losartan they are feeling more attracted to it. Similarly, after the price reduction, we are looking into how we can expand our prescriber base. So, we started this initiative around one year back, and then we started moving to consulting physicians and also to the family physicians, telling them how Losartan is better than other molecules in the segment.

In hypertension today, there is a very large market of Atenenol of around Rs.250 crores, there is a large market of Amlodipine of around Rs.300 crores, and there is a large market of Atenolol Amlodipine which is almost of Rs.350 crores. And we own only around 35% market share into Losartan market which is almost Rs.500 crores. So it means that there is a huge potential available to expand Losar into Losartan market as well as into the other anti-hypertensive market which are available with the family physicians, consulting physicians and also with the specialists. We are encouraged by these numbers. I am really happy to share with you that internally we have started showing positive buoyancy in terms of a unitage growth, and the prescription audit is also suggesting that we are gaining our prescription with top end specialties, along with the family physicians. Just the consulting physician is yet to take off. I am sure in this quarter we will find very good buoyancy in consulting physicians also.

Ravi Shenoy: Two more queries. One was that you introduced a new segment by the name of 'Life Care.' What does that cater to?

Bhagwat S. Dhingra: Life Care is into critcare segment, for the patient who is critically ill maybe because of septicemia and pneumonia or any other infection, where patient has not been treated by a doctor into OPD practice, such patient move to Intensive Care Unit (ICU). And these patients either in nursing home or in a hospital set up are being treated by the top end antibiotics. So, Life Care division is into top end antibiotics which reach to the corporate hospitals, government hospitals and also the lower end hospitals which have 10 or 15 bedded hospitals like nursing homes etc.

Ravi Shenoy: How large would that market be?

Bhagwat S. Dhingra: That market size is around Rs.2,800 crores. And we have started in month of April in this business. We envisage our team size to be around 125 people. Today, we have 115 people in place. And last month our all India sales were around Rs. 85 lakhs and primary around Rs. 90 lakhs. And from last 2-3 months the business is showing a very good color, that gives us hope that this year we can close around Rs.7.5 crores, but next year we are definitely looking to develop this business with the existing field force.

Ravi Shenoy: Lastly, the Anti-infectives market has been growing at a pretty low pace. Is there any chance of improvement there which you may be looking at?

Bhagwat S. Dhingra: In a country where economic conditions will continue to be the same, the poverty lines and hygienic conditions to work and infrastructure issues in our rural area, Anti-infective market continue to be the biggest market and will continue to grow at least in a positive single-digit to double-digit growth. Because within Anti-infective there are some segments which are more related to seasonality, like maybe malaria, maybe typhoid, they are more related to seasonality, but day-to-day fever and day-to-day infections are one that will continue to be integral part of our country. So I do not think so that Anti-infective will degrow in coming future.

But when we talk from Unichem's perspective we were not a very well known company when it comes to Anti-infective. We have taken some initiatives, in the month of April, we realigned our Anti-infective business and today the Anti-Infective we launched in the market are paying us very good dividend, they have started doing very well.

Moderator: Thank you. The next question is from Mr. Alok Dalal from Motilal Oswal. Please go ahead.

Alok Dalal: What is the growth outlook for the India business for FY15?

Bhagwat S. Dhingra: In FY15, there are two things which I look into– one is that the first quarter was without NLEM, the second quarter was with NLEM in FY 14. I look into the FY14-15 should be at least 200-300 basis points better than the FY13-14.

Alok Dalal: And apart from the NLEM impact, which are the other things that need to work for you, for you to achieve this 200-300 basis points improvement over FY14 numbers?

Bhagwat S. Dhingra: As you know that we have taken many initiatives in our Chronic Care as well as into our Acute Care business. Despite NLEM, these initiatives have started paying dividend to us. Because within our Chronic, we have three divisions which deals with Cardio and Diabeto segment and we also have one division which deals with Neuro-psychiatry. We have revamped the Neuro-psychiatry business last year which has started showing big buoyancy in last 2-3 months, we are growing @ around 15-20% internally as well as in AWACS when it comes to our Neuro-psychiatry business. When it comes to Acute business you can see in Acute business also we are showing a very good buoyancy, rather today Acute business though the base is less, is showing around 400-500 basis points higher growth than our Chronic business. In the past Unichem was running on one wheel. At least we are trying to change into two wheels i.e Acute as well as Chronic. I am sure that the alignments which we have done with the right divisionalization, with the right manpower placed into every division is going to create better momentum for Unichem.

We are also evaluating that before entering into Q1 of next financial year, what all should we do internally so that there is growth in Losar, or the products like Anti-infective like Ampoxin or the old products like Unienzime. We are brainstorming within ourselves in order to see what all can be done. So that, these products start contributing to growth in the next financial year. I am pretty confident because the numbers on quarter-on-quarter basis internally and externally are showing that there is a very good alignment when it comes to products, there is a very good alignment when it comes to promotion, there is a very good alignment when it comes to our customers across therapy. When I joined, the attrition levels were huge. Today, the attritions have come down drastically. That means the people in the field, our medical representative and the managerial hierarchy is beginning to settle down. So that helps us to increase per call productivity. I am pretty confident that next year will be a very good year for Unichem.

Alok Dalal: Have our trade-related margin issues are sorted out?

Bhagwat S. Dhingra: Already over 51 companies have declared that they are going to give an extra margin budgets being demanded by trade that is 4% to retailer and 2% to the stockist. When there was tremendous pressure we went to give that kind of margins but we have played the margins trade differently with the trade association. We told them that we will not be able to give 4% for retailer, instead of that we will give you 19 plus 1 as free goods. When I talk of free goods it means that instead of that 5.3% it becomes 1.5% at cost for me, and for stockist we have given 2%, so net-net impact will be on our current average sale is around Rs.68-70 lakh a month.

Alok Dalal: Our transition from the distribution model to the CNF model, is that nearing an end?

Bhagwat S. Dhingra: As per our internal schedule we have planned to complete it in Q2 next financial year. So nine months from now we hope to complete that. But as of now almost 50% sale is happening through C&FA and 50% is happening through our distributor network.

Moderator: Thank you. The next question is from Mr. Anandha Padmanabhan from Canara Robeco. Please go ahead.

Anandha Padmanabhan: This query is regarding the recent Supreme Court judgment regard to penalty on charging over and above the NLEM prescribed price. So, do you think there is a risk of increased penalty coming in the coming year?

Bhagwat S. Dhingra: The Supreme Court verdict is a right verdict. Because when government had announced the NLEM they have specified the dates to roll out NLEM. But unfortunately, many companies have made an appeal either through the land of the law or directly to the NPPA, but as you know Unichem is a very clean and ethical Company which followed the law as required. So the day when NLEM was announced we started to plough back our stocks, and to be honest one of the reasons of our depressed growth in Q2 FY14 is because we were the first to roll out our NLEM stocks at the price points suggested by NPPA. And we have also taken back the stocks during June-July and August period, and we have completed the cycle in the stipulated period. As far as Unichem is concerned, there is no question of any penalty in this regard.

Anandha Padmanabhan: The other question is with regard to approval of new product on your combinations to domestic market which has slowed down considerably. Do you see this as a temporary trend or do you see the company getting new product introduction will become incrementally difficult, the company will hence have to concentrate more on growing the existing brands rather than drive sales through new product introductions?

Bhagwat S. Dhingra: It is a very-very good question. If I look into the governments' own statement and the report which we keep getting, government today is burdened with many truck loads of data being pushed by various companies supporting the combinations which are already in the market or which company intends to launch. But if I understand correctly the government's intention, they do not have the manpower to map that all data, number one, therefore the combinations which are already existing in the market for quite some time are likely to get cleared by FDA. So it is my own presumption, I do not think that it is going to be like some guidelines tomorrow for IPA. Second is that when it comes to Unichem, our most of the products belong to the category which has been introduced way back, at least that they will be cleared and the other products like the tri series which we have introduced recently, they have local approval but the composition of the molecule within the Tri series are such which are available nationally and internationally. So I do not find any issue related to Unichem products that are going to be hurdle for our growth and we will continue to sell those products with a similar aggression as we are doing now.

Anandha Padmanabhan: What would be your total consolidated profit or loss or your subsidiaries put together?

Rakesh Parikh: In the last financial year the difference between the standalone and consolidated was about Rs.16 crores and Niche had turned profitable for the whole year for the first time; Niche is continuing to be profitable as far as the current year is concerned; the loss in the US has lowered down. We have started a new subsidiary in Ireland; some initial costs are there. In Brazil, no approvals have come apart from the two products which we have test launched. So it is practically at the same level as what it was last year. Since already 10 months have gone, what it appears is that this year the loss will be definitely lower compared to last year, it will be much lower than the Rs.16 crores which we had last year.

Anandha Padmanabhan: Basically, the loss would be primarily from your US and Brazil subsidiary?

Rakesh Parikh: Yes, that is right; and in Ireland, where some small expenditure has started for developing products for the tender market, and profits from Niche may not be sufficient enough to offset losses from there. The way it is going, next year looks to be much more promising because US can easily break even, and if the approvals come faster even the US subsidiary can show a profit. Niche is showing around 17% growth in GBP growth, US is already showing top line growth of around 35% plus, i.e dollar growth on the top line. In EU tender business has started. We have already started participating in the tender business and there are signs that we will start some initial business there. And this should be able to offset the losses.

Internally we are targeting to see that in the next year there is nothing which comes as a baggage from these subsidiaries on to our standalone performance. But having said that our model is such, that most of the manufacturing, around 100% for the US as well as some for Niche is being done by Unichem India, and the results of which are reflected in the standalone numbers. And as we see it on a consolidated business basis, we are seeing a profit that is recovering all the costs for these subsidiaries at a manufacturing level as well as the selling, distribution, but except the R&D which we are writing off as a conservative account practice, which is about 4-5% and significantly skewed towards the regulated markets of US and Europe, though being for the future. We have come to a stage where we are recovering only a part of it. So for next year what we are trying to say is that, not only will we recover the entire R&D expenditure but also we will try to see whether the legal entity wise also they can break even.

Anandha Padmanabhan: What would be the threshold level of sales which you need to achieve in each of these markets, basically US and Brazil in order to break even?

Rakesh Parikh: In Brazil we have about 18 filings, two products which have been test launched. The current filling which are on the hold, have about four or five products. So what we feel is that if we get these 4-5 approvals then with about 5-7 products launched in the full year, the company can break even at a legal entity level. But at a consolidated level even with 3-5 products we should be able to break even.

Anandha Padmanabhan: And in Brazil, you are into unbranded generics, right?

Rakesh Parikh: That is right, generic- generic.

Moderator: We have a question from Mr. Krishna Kiran from ICICI Direct, please go ahead.

Krishna Kiran: Continuing the previous question, if I am right, in this quarter we have not made profit on Niche generics, and we have seen sales growth of under 20%, can you just explain on that?

Rakesh Parikh: It is basically very marginal as far as the bottom-line net is concerned. In December compared to the first two quarters, the sales have been lower, because practically Europe was closed from about the second week December onwards, and they have not started till almost the first week of January. But at an operating level, and as well at a cash level, they have made a profit. The product mix did affect it. If you see the sales also, we are slightly lower compared to that the past, but the loss is small, hardly a few thousand pounds at the bottom line, so that is not an issue. In the Fourth quarter there will be a profit as per our indications suggest, accordingly for the full year also, we will end up with a profit.

Krishna Kiran: In the same way in US, if we need to break even, how many products are need to be launched, or how much time as per your internal targets?

Rakesh Parikh: It is difficult to say in terms of how many products because the product mix is also very important; some of the products are much more profitable, and some of the products are less, plus there are a lot of opportunistic orders which one is able to get. For example, though December was a bad month for Niche, for our US business it was an excellent month, and it also made some profit for the month was not emphasized per se. And if you see in terms of the penetration and the relation which we have with our distributors even with the existing products without any new approvals or launches in the last 2-3 quarters, still the dollar growth, we have been able to show around 30-35%.

We have another two products where we have got the ANDA approval these are in the process of being launched and the API supplies are in place. So maybe in this quarter or in the next we will be able to launch those products. That will enable the momentum to go through. What we feel is that if we are able to get another two more products, so basically four products from today; from 10 if we go around 14 products, then next year, even at the legal entity level, we should be able to see the break even.

Krishna Kiran: Just to understand your CRAMS business more, I think we have not got any new contract, but in the last few quarters, we were saying that maybe in Q3 or Q4 we will get some clarity on how CRAMS business going ahead. So can you just give us outlook on this CRAMS business?

Rakesh Parikh: As we said, the CRAMS business is more like a filler business to use our capacities and to make our assets sweat since we have the approved plants until our own orders and approvals come through. What we had indicated is that we were not expecting any new business in the current year. Unfortunately, the offtake also reduced especially from North America, because they themselves were feeling certain constraints and competition for the products, which we had taken on CRAMS from them. However, the discussions are going on with the other parties, the details of which I can't disclose right now because of confidentiality agreements. I would not say very advanced, but at a reasonably advanced stage for at least a couple of them. But even if it materializes the actual commercial dispatches obviously happen next year only and then maybe we will have better clarity by the end of the current quarter.

Krishna Kiran: How much we have spent during these nine months, and FY15 guidance on CAPEX?

Rakesh Parikh: In the Nine months, we would have spent roughly around Rs.55-60 crores. And as we said, though we were talking of commitments being there for more than Rs.100-125 crores for the current year, let us see how the things progress, because we do not look at it from quarter-to-quarter point of view, but those are the committed CAPEX which are there. In all, today the CAPEX of almost about Rs.200 crores have been committed, and most of this implementation has started.

In Formulations, having received the approvals from Goa Industrial Development, the plans are approved, and the work on that has started i.e the land development and the site development.

In API plant expansion are at an advanced stage as far as the Pithampur API is concerned, the Roha CAPEX is also going to start , and then we are actively looking to acquiring a new facility. And as far as the long term is concerned, we are also scaling up our biosciences pilot plant, where the equipments have come; their installation is going at a reasonable pace. So, we are looking at something in the range of Rs.150-200 crores from now and a year and a half or so, in addition to the maintenance CAPEX.

Krishna Kiran: Maybe in next one year and a half timeframe how many re-inspections will happen?

Rakesh Parikh: Two of them have got re-inspected in the last financial year; otherwise they are welcome to come any time. There is no fixed schedule as far as the next year is concerned. Both the inspections have gone through. In the last financial year we already had two re-certifications.

Moderator: We have a question from Mr. Karan Doshi from Subhkam Ventures, please go ahead.

Karan Doshi: I would like to know your segmental breakup for Formulation and API business.

Rakesh Parikh: For the quarter?

Karan Doshi: Yes, for the quarter.

Rakesh Parikh: Out of Rs. 265 crores which we have done API sales are around Rs.35 crores for the quarter. Balance will be Formulation at around Rs.227 crores. This does not include the captive API which we make for our own Formulation, especially for the US and Europe, and the regulated markets.

Karan Doshi: Out of this Rs.227 crores, how much was from Domestic and Exports?

Rakesh Parikh: Rs. 166 crore was from domestic market and about Rs. 61-62 crore was from international.

Moderator: We will take the question from Rashmi Sancheti, please go ahead.

Rashmi Sancheti: How much was the R&D during the quarter?

Rakesh Parikh: R&D during the quarter was slightly more than 5% of our turnover, so that comes to between Rs.13 and Rs.14 crores.

Rashmi Sancheti: What is the outlook for FY15?

Rakesh Parikh: We have been saying that normally we would like to spend around 4-5% of our turnover on R&D. Even if you see on a 9-month basis, it is slightly around 4.5%. This is only revenue R&D excluding the capital expenditure.

Rashmi Sancheti: What is the CAPEX guidance you are giving for FY15?

Rakesh Parikh: We have plans for roughly between Rs.150-200 crores, which would last over the next 4- 6 quarters.

Rashmi Sancheti: In the last quarter you said that there will be around Rs.20 crores impact due to pricing policy, out of which Rs.13 crores was reflected in the last quarter, and excluding the trade margin issues, it was around Rs.5 crores. This time there are no trade margin losses as such I believe. So how much would be the pricing policy impact only in this quarter, what would be the revenue loss?

Bhagwat S. Dhingra: If you see in the last quarter the pricing policy impact was around Rs.5 crores. This quarter the impact will be around Rs.4 crores because our internal volumes are not going to dip compared to Q3, and that tradeoff will be with the trade margins which will be impacting us on an average of around Rs.68-70 lakh on per month basis.

Rashmi Sancheti: So you still give the guidance of Rs.20 crores from July to March 2014, the entire year impact.

M. Gundu Rao: I do not think that is a correct measurement. In the second quarter the impact was around Rs.5.7 crores including the stock which we called back from the market. This quarter it is approximately around Rs.5 crores. I think that may continue on a quarterly basis. What we said about Rs.20 crores is an annualized impact, not the impact for the current year.

Bhagwat S. Dhingra: Overall impact may come between Rs.14-15 crores, not Rs.20 crores. For the financial year it come that much, yes.

Rashmi Sancheti: This quarter there has been very strong pickup in API sales. So once Pithampur facility comes on stream, which will be coming on stream in FY15, what kind of growth we can see in the API segment – will it continue to show such kind of growth that is double-digit growth or again next two quarters it will get normalized?

Rakesh Parikh: Even if you go back to last two quarters, it is not right to see on quarter-on-quarter basis, but now let us look at 3 quarters which have passed, and for which growth of almost about 17-18%. We feel that this is the kind of internal growth we can achieve, which also includes growth coming from the domestic demand, where we have come out of the NLEM, because earlier the APIs were under price control, and one of our major products being API is now out of price control. Also, what has happened is, some help came from the exchange rate because of which the Chinese imports have become much more expensive. So that gives a good benefit to us as far as the other parts of the world as well as the domestic market is concerned. But the capacity constraint is not only because of the orders that we are having, but the captive consumption which are showing a very buoyant growth.

If you see our Formulation growth of US and Niche, they are showing a higher double-digit growth for which the API requirements are met by our own plants. Our first objective would be to see to what extent it API would add value for requirement of our formulations. As a result of which we are holding back certain development activities in terms in the API business as far as sales of external parties in regulated markets are concerned. Depending on what is the state of our captive requirements based on quantum of approvals the growth may continue at mid teens levels; otherwise we will try and see a higher growth for external sales.

Moderator: We have next question from Ashish Rathi from Emkay Global.

Ashish Rathi: Wanted to check on the API facility which we are planning to acquire, what is the kind of amount that we are likely to spend here?

Rakesh Parikh: We are having few options available. These options are more or less on as is where is basis. We can use basic infrastructure, but to make it to our requirements in terms of the products which we require and then to go in for approvals. As a result of which we are not talking of some very high cost, but it is difficult to put any number, but pure acquisition or facility, the typical land and basic building and other paraphernalia costs which are there, can be anywhere between like Rs.15-25 crores or so, in addition to it, that much amount or more we will have to put in to bring it up to a certain stage, so that we can go in for approvals and meet our requirements.

Ashish Rathi: This will be above Rs.200 crores which we are talking about as committed?

Rakesh Parikh: This 200 crores I have included this part also.

Ashish Rathi: Secondly on tax rate, any guidance for next year?

Rakesh Parikh: Basically, we remain a MAT paying Company, I presume there will not be any budget this year, that is what they have said, so vote on account, I do not think they will change anything. And if MAT of 21% remains and also the deferred tax since will continue our capital expenditure, so anywhere between 22-23% is the guidance which we can give.

Ashish Rathi: On the Ireland facility you said you have put in a subsidiary. So just wanted to understand what is the thought process here, because if I am not wrong it is a de-growing market?

Rakesh Parikh: The subsidiary per se is registered there; we are not planning to sell immediately in Ireland. Niche generics, our UK subsidiary already have a plant in Ireland. What we are doing is that we want to use this benefit to participate in certain markets of Europe which have gone through the tender route. The tender business there has become very lucrative, and it is a very fast growing business. Because of certain agreements which we have our UK subsidiary may not be able to participate.

Ashish Rathi: Will we do the manufacturing from India only for those tenders?

Rakesh Parikh: Depending on the type of the products, it may be done in India or in Ireland, or both, except APIs, because we do not have an API plant there.

Ashish Rathi: So mostly Ireland would be used for exports from Ireland?

Rakesh Parikh: Yes, the products would be exported if they are manufactured from Ireland. It will be basically a Niche kind of a model with a third-party manufacturer as far as Ireland subsidiary is concerned, since it does not have any plant of its own.

Ashish Rathi: In European markets, I agree may be the growth rate is high, but how about the pricing scenario there, and tender participation again being a low margin business, if you could throw any color on what is the understanding on this business, and how the growth potential remains for the company in terms of both margins and profitability on the whole?

Rakesh Parikh: What you said is very true, in Europe the overall growth has been subdued though it is slightly coming up, but as far as the tender market is concerned, in the regulated markets on the Western European side, predominantly in the countries, like Germany, Netherlands, there are good prospects and since they want to promote the generic business there are reasonable margins. From our side what we are planning to do is that wherever we are cost-competitive, only in those products we are going. Any products which are more like commodity type or which can fetch very low margins or there are too many players, we may not go. These tenders are not new, and most of these tenders are for two years, and last year the prices have been known, based on that we are identifying and selecting. Where the market is huge we are talking of a small market share where we are having the product development and manufacturing advantage what we feel in terms of cost plus quality or so.

Ashish Rathi: When you say manufacturing or cost advantage, will we be eyeing margins at current company level or even despite that cost advantage what we are looking at, the margins would be lower than the company has?

Rakesh Parikh: If you are looking at the current standalone Indian company, it would be the same. Even the contractual business which we are doing for US market it maybe 15-20% at EBITDA level which we are looking for.

Moderator: We have a question from Mr. Saravanan Viswanathan from Unify Capital. Please go ahead Sir.

S Viswanathan: Most of my questions have been answered, just a clarification, you had mentioned that two of your facilities were inspected by US FDA during the year. I would like to know are there any pending observations that you have to close, or are there nil observations?

Rakesh Parikh: There were not nil observations, there were observations, but just happy to say that USFDA closed their inspection at one place one day earlier, at other place two days earlier compared to what they had scheduled. And whatever observations were there, they weren’t major. But these have already been replied to and we understand if they do not come back it is closed.

Moderator: We have a question from Mr. Suranjoy from Escorts Securities, please go ahead.

Suranjoy: Most of my questions have been answered, but there is a query on the CAPEX, you have mentioned that you will be spending something around Rs.200 crores till FY15. What I want to know is that how much contribution are we expecting in the revenue side from this CAPEX, and also what is the kind of margin improvement which can happen from this CAPEX?

Rakesh Parikh: The major driving force on the CAPEX is going to be the requirement in terms of our top line growth which we are expecting and because of which we will need the capacities, especially in API. How much revenue growth? Maybe a bit difficult to answer, but if you see overall in the industry, you can safely take the in terms of Formulations, you should get anywhere between 1.5 to 3X the cost which you are incurring, and if it is not a Greenfield site, it can be even more than that. But ultimately what happens is that we have to see how much of capacity we are able to translate into revenue.

Suranjoy: The subsidiary in US and Brazil, they have been making losses. When can we see them coming to break even and start making profits and starting to be one of your star performers?

Rakesh Parikh: As we said, US has been showing a very good traction. Even as a standalone legal entity if we see, in the next full year we are internally aiming at seeing that it comes to breakeven although depending on the approvals. Even if the approvals do not come, or even if one or two products which we have already approved which we are going to launch, we should be able to break even in the next year as far as legal entity is concerned. And on a consolidated basis also, it should show profit, because the manufacturing is done here.

As far as Brazil is concerned, what I would say is that we are looking at least for another 3-5 approvals. Now, let us say, we get couple of approvals then definitely the losses will be lower, and if we get about five approvals or so, then maybe in FY16 Brazil also can break even. Niche as we know is already making profit, and this year also they should end at a profit.

Moderator: I would now like to hand over the conference to Ms. Rashmi Sancheti. Please go ahead.

Rashmi Sancheti: On behalf of Sunidhi Securities and Finance, I would like to thank the management of Unichem Laboratories and everybody for participating in the call. Now I would like to hand over to the management for the closing comments.

Monish Shah: Thank you everyone for joining on the call. We apologize for the technical glitch experienced by our audio service provider - iJuncution. If there any questions which are not answered, please get in touch with us, we will be happy to answer them. Thank you and have a nice day.

Rakesh Parikh: Thank you.

Moderator: Ladies and gentlemen, this does conclude your conference for today. We thank you for your participation and for using iJunction Conference Service. Thank you. You may please discontinue your lines now.