

# Vivimed Labs Ltd

## *Q2FY13 EARNINGS CONFERENCE CALL*

**MANAGEMENT:**

MR. SANTOSH VARALWAR – MD & CEO

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**MODERATOR:**

MR. SIDDHARTHA BHOTIKA – INDIA ECONOMIST, TATA SECURITIES

**Moderator**

Ladies and gentlemen, good day and welcome to the Vivimed Labs Q2FY13 Results Conference Call hosted by Tata Securities Limited. As a reminder, for the duration of the conference, all participants' lines will be in the listen-only mode, and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during the conference call, you may signal for an operator by pressing '\*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Siddhartha Bhotika of Tata Securities. Thank you. And over to you sir.

**Siddhartha Bhotika**

Thank you, Lavina. Good afternoon, everyone. On behalf of Tata Securities, I welcome you all to the conference call for Vivimed Labs second quarter earnings. From the management side we have with us Mr. Santosh Varalwar – M.D. and CEO; Mr. K. S. Sastry – Senior Vice President Finance. Now, I invite Mr. Varalwar for opening remarks, after which we will move on to the question-and-answer session. Thank you. And over to you sir.

**Santosh Varalwar**

Thank you, Siddhartha. Good afternoon, everybody. Nice to again come back and talk to you about the second quarter earnings, we will start with this. As you have seen, the presentation has already been shared with all of you Q2 Earnings. There has been a growth in income obviously 114% year-on-year. This definitely most of it has come from acquisition with UQUIFA consolidated numbers, last quarter also we have done it and this quarter, but last year this quarter there was no earnings from UQUIFA, so UQUIFA earnings are in line with the budget so far maybe again two major entities; UQUIFA Spain and UQUIFA Mexico, both of them on target growing. Similarly, the impact you can see it on EBITDA, which was 93% or 53.9 crores. EBITDA margin looking good; 19.5% in spite of standalone, UQUIFA, if you see I think we have been doing in the range of about 13% to 14% EBITDA, while the other results standalone business we had done better compared to last quarter last year. The EBITDA average is 19.5%. Profit after tax is 25.5 crores, again jump compared to year-on-year, but well in line with expected earnings for this year. If you look at H1 consolidation you have seen last year, the annual sales was about 670 crores as compared to H1 sales of 550 crores, which obviously see the jump again coming from the consolidation numbers for UQUIFA.....

Looking at the Specialty Chemicals and Pharmaceutical, look at the comparison Specialty Chemicals business continues to be a little stressed again in Europe and America with a bit of impact coming from one of our key products Triclosan which is antimicrobial, there has been some kind of batches going around on the products; however, we see mixed responses, I would say. Some companies trying to get back in Triclosan and some companies trying to walk out, but surely there is a change in the last quarter; substantial

scale down from one of our major users **Constantin 3:42** in Spain who was using quite a lot of materials on the **(Inaudible) 3:49**, but then good news in Triclosan is that Colgate which was eluding us **(Inaudible)** for last so many years, they look up better and they are in the final stage of completing the process approval and most likely will qualify in about 30 days for Colgate total approval which might give us additional volume.

So there is mix volumes in terms of Triclosan, but other segments particularly, the Hair Dye segment **not (Unclear) 4.19** very encouraging in Europe but compensated by a lot of interest in Asia and a lot of interest in China company has bagged that fortified. Sunscreens season just begun, so you wouldn't have seen the impact of those numbers coming in, which you would see probably in Q3 and Q4, the normal offtake for sunscreens begins this year, but good news is that, yes, we have bagged some good orders on sunscreens even if we go for the first time has definitely given us a much larger share of UV absorbent and we have also taken away some of the orders from Henkel Europe and L'Oreal continuing to repos faith have given us volumes back to us, so I think we will continue to do well on this front.

Some top stories, Photographic Chemicals, it really again nothing has been happening on the Photographic element, we are just seeing a flat growth, again same thing in Photochromic. We have tried to get the product out in some areas, particularly China where the growth story looks good, but we are yet to get some numbers again but more anytime we can see this happen.

Colgate, we have got Pharmaceutical definitely is far better, the acquisition that they have done last year Klar Sehen as per plan can expand its market proceeds in a retail branded formulation, initially it was the Northeast but after we took over, we have extended the expansion to Uttar Pradesh, Uttaranchal, Madhya Pradesh, Karnataka and Kerala and some of the areas have already come to and some of them may be positive, so I think the target of 50% growth that we have budgeted for this year is looking good; it is going as per target and yet to see some of the new ophthalmic products to be launched, which will probably come in the next two quarters, which should probably scale up our expectations from this particular segment of business next year.

There is API business, after post UQUIFA, as I mentioned last time, I think there were a couple of actions that were to be taken from the Vivimed India point of view; one obviously, was creating additional capacities for API in India, which is coming up. As I mentioned last time, I think because of delays coming from the Vizag Greenfield project, what we have done is we initiated a project in Bidar, Karnataka in our existing facility where we acquired additional area, and that project is coming up, substantial work is in progress and as the way it looks I think by June 2013, this plant should be fully ready to

go and then we expect to have validation of this to be completed. So as per target it should be ready by September 2013 and the progress is in good swing.

And second thing which we were supposed to add up was obviously the Intermediate business for UQUIFA which we are supposed to start production here. Original time span and time schedule was September 2012, but we just got some delays and other things, project implementation, it just got ready, I think November we have started the validation batches, but the commercial production will probably begin from December and scaling up will probably start in the last quarter, that is where you will see some chains of Specialty needs coming into Vivimed, which would also complement UQUIFA's bottom line and top line.

Another major important decision as far as UQUIFA and Vivimed API business is that we envisage investing on new R&D facility in Hyderabad and we have acquired premise in Alexandria in Genome Valley and **(Inaudible) 8:25** PPCs is over but I think end of this quarter, we will see it almost ready for operations, we will see some operations starting at R&D front, which will compliment the 40 people that are sitting in Spain, so that increase the whole thing. But in terms of sales, if you see, Pharmaceutical business **(Inaudible) 8.49** but still I would say that for one month during the month of August the plant was almost shut down for fixed approval, one of our plants in Hyderabad so fixed approval is over and we are expecting the approval to come anytime that will give us an edge over the Eastern European business when compared to many other US companies where it is critical for Vivimed's business as far as some related markets like Eastern Europe, otherwise the business is good, I think the other businesses **(Inaudible)** looks pretty good and the next two quarters orders are all in place and as such....

In terms of Finished Dosage Formulations, we have also started marketing FDF formulations in Europe. I think one of the first market evaluation that we got is for Omeprazole capsule and we just put up Omeprazole capsule, the finished form in the market, particularly in Portugal, so we have not seen the numbers yet, but we signed up with one of the major generics companies in Europe for Omeprazole capsules and we will start selling the materials to the market. So it will be the first market solution that we made **(Inaudible) 10.19** and will be getting to the regulatory market with one product and we have also got a couple of products in the pipeline which I will share with you over a period of time.

So in general, Specialty Chemicals business does witness some pressure, but nevertheless there are lots of like molecules in the pipeline and we are expecting some good approvals to come from Unilever recently for another skin lightener which I think has been audited by Unilever that they should come in and also should see some new molecules coming in.

In terms of Pharmaceutical in fact it is panning out to be pretty great for a sustained and continual growth, there are a lot of activities that Vivimed has to undertake in terms of strong R&D, strong pipeline and creating capacities and also **(Inaudible)** APIs, but as I say, we are still on course of a lot of activities and action and coming quarters, you will see a lot of these things happening. That is all for now and I leave it for the forum to ask me any questions if they have anything specifically I am going to reply to them, thank you very much.

**Moderator**

Thank you very much sir. Participants will begin the question and answer session. Our first question from the line of Mr. Rajendra Shah from Fidelity Management, please go ahead.

**Rajendra Shah**

Just two questions, one is on the Spanish acquisition after one year how do the prospects look and what are the challenges that are there? And the other question is the debt has gone up considerably from March 2012. What is the reason for it and how do we bring it under control?

**Santosh Varalwar**

I will split this answer into two. The first part I will answer and I will let Mr. Sastry answer the second part pertaining to the debt. As far as UQUIFA is concerned, I think I shared in the last call; strategy for Vivimed is pretty clear where UQUIFA has a strong API background and has got a strong pipeline going forward. I think most important post acquisition actions to be done from Vivimed is to consolidate the position in terms of that and also complement UQUIFA's business in terms of cost competitiveness, but it is very obvious that Spain has element of production and competition that is coming from various Indian and Chinese companies. Unless we have a good strategy in place in terms of going forward I think it is not going to really work out. So obviously three things that we decide to do post acquisition was #1 is to create a Pharma Intermediate plant within India and then complement UQUIFA by trying to supply in-house Intermediate which will bring down and we call that the most informant plant which is we have already captured it and obviously, the plant that we have invested here it will start growing the commercial production in December, so you will see some of the variety captured there. And the second obviously is like there are certain products under thrust in terms of cost because of Indian competition and these are the produts which we target to move them to India from Spain so that you need to have USFDA approved facility for API, and for that as per schedule we have started construction, and as I said until September 2013, really no time to build, improvement would happen in those directions, because there are regulatory approvals are required on the site. And the third thing obviously complement UQUIFA with the innovation pipeline and innovation things for which we have already invested on a pool of franchises in India hiring and that you will again see coming up because 40 R&D

centers are there in Spain right now and we are now taking about another 30 here which would really complement in terms of analytically regulatory filing in terms of new products. So what you really have seen so far in the last 11 months is some of the actions which we have taken in terms of including product but no tangible numbers here really reflecting in terms of it and it is yet to come and which is really expected nothing shocking for us because Pharmaceutical business, the regulated market business and **(Inaudible) 15.19** actions what we say is going to happen, after which even for the Intermediate, the key starting materials, we need to get approvals from prospective customers or existing customers including UQUIFA but they are all on course, all the activities are on course. And Sastry, I would request you to clarify as far as second part; the debt.

**K.S. Sastry**

The debt is in fact against the planned CAPEX. The IFC funds have been placed during the last 6 months from April to September, so that was again the CAPEX, so you see the increase in comparison to March, so that is the main reason for increase in debt; IFC funds coming in during last six months.

**Rajendra Shah**

But when do you think the debt will start coming down?

**K.S. Sastry**

The ones that have been borrowed for the purpose of acquisitions and all, they have already fallen into repayment mode. If you look at IFC it is a long term loan with three years of moratorium, but other loans they are of short-term moratorium of one year and one-and-a-half years, so probably you will see a striking difference from 2014 onwards where even IFC will start coming for repayments, so I am sure 2014 up you will see the debt coming down.

**Santosh Varalwar**

Adding to that, I also like to add, if you look at the business prospect, actuals obviously Pharmaceutical business is growing multifold obviously, we also need certain action to be cost competitive in certain segments **(Inaudible) 17.15**, so the actions were obviously to create subsidies, additional capacities for Pharmaceutical to strengthen your position and second was to create APIs, like API facilities in India, so that is going on and third one which probably we have not shared so far our investments in terms of creating **(Inaudible) 17.42** formulation. So as you have seen, the business of Pharma business I think going more towards forward integration. So Vivimed has already started investing money and also creating FDF facilities which would comply with USFDA requirement. So until all these three actions are fully completed, you would still see us spending some money, but once these are all there, there are long term plans, and when the CAPEX will scale down and you will always see the results of the investment that we have made.

**Moderator**

Our next question from the line of Charulata from Quest Investment, please go ahead.

- Charulata** I want to know what is the other long-term liabilities that is a part of the balance sheet in June?
- K.S. Sastry** Basically, there is a movement in this, in the sense basically this capital creditors for the capital goods. In fact, a lot of expansion activities are on, so the long-term creditors for running the capital goods.
- Charulata** I also wanted a breakup of the CAPEX that has been spent so far over the last six months?
- K.S. Sastry** The main CAPEX had gone into the API and Intermediate plants, then into Jeedimetla, which is a Pharmaceutical formulation unit; expansion of that. Then also we have a unit in Bonthapally Specialty Chemicals, some new products have been taken up; about 7 to 8 products and related expansion for those products, and Bidar also, we have expanded the capacity for Triclosan, so it is all spread across all the units and of course certain land acquisition also has gone into it.
- Charulata** Land acquisition to what extent?
- K.S. Sastry** We have around 250 acres of land in Vizag that is for the SEZ.
- Santosh Varalwar** Just probably to expand what Sastry said, we have of course what Vizag is the land which we acquired for special economic zone, but besides that there was some environmental clearance yet to come forth from Vizag, so just we are waiting for some time and using time on our plan of coming up with **(Inaudible) 20:34** and API facility. What we have done is interim, we have acquired additional facility; additional land and building in Vizag and the API, the first block is coming up again in Bidar and in Bonthapally, which is where our Specialty Chemicals plant is there, even in and around Bonthapally we acquired additional facilities having the plant because right now the original land is only about 9, 9.5 acres and the kind of growth we are anticipating and what we are creating, so we acquired almost 8 to 10 acres around it so we have additional..... So as you know very well we have a plant and we have option to avail something, acquire something in the vicinity or adjacent to it, it is there to be done because you will again not get chance and today like particularly in Hyderabad in these areas I think there is a lot of restrictions coming because of pollution control board in API....
- Charulata** In terms of the growth, can you classify the organic growth in the 100% growth that has been achieved?

- Santosh Varalwar** Organic growth if you see we gave a split last year. Do you have the number Sastry between Pharma and Specialty Chemicals?
- K.S. Sastry** For this quarter, we have about 87 crores from Specialty Chemicals and around 23 crores from Pharma. If you compare quarter-on-quarter, Spec Chem has done well for this quarter in comparison to last quarter; almost from 69 crores to about 87 crores, so that is a good growth there in the top line. On the Pharma side, it is more or less a little bit like 23 crores was done in the Q1 and a little increase there about 24 crores; a crore of increase in Pharma. Overall, you can say about 91 to 111; I am talking about standalone, around 20 crores of increase.
- Charulata** No, on a consolidated level, how much is the organic growth?
- K.S. Sastry** More or less it will be on the similar lines because inorganic growth of UQUIFA and all those additional businesses we added to our existing business, around 25 crores is the increase on quarter-on-quarter from organic side.
- Charulata** For Specialty?
- Santosh Varalwar** In the six months if you see it is all organic growth because there was no inorganic in the last 6 months you can see that, but if you look at compared to last year to this year, I think we have something around 20 to 22% organic growth other than whatever rest....because I think last acquisition was done in November last year, after that there is no acquisition.
- Charulata** This 20% how much is in Specialty and how much is in Pharma?
- K.S. Sastry** Specialty takes the major chunk which is 15 to 18% also and Pharma takes the earlier second bit.
- Moderator** Our next question from the line of Mr. Vimal Modi an Investor, please go ahead.
- Vimal Modi** The company has filed 47 Type-II DMFs with USFDA. Any three most promising ones out of these? I have a few more questions. Second one is if there is a demand for, let us say, 1 million shares to be placed to a PE at a hefty premium, I mean, reasonable good premium to CMP, are you open to it? This is to reduce the debt component, which is a little bit worrying. And the third one is you have acquired some local companies with focus on South and East India market. So what are you planning for Western part of India?
- Santosh Varalwar** So taking on your first question, three promising DMFs that we have it, obviously, one of them is the Pantoprazole, which is picking up in terms of marketing right now after



Omeprazole. In terms of today value and volume, I think Omeprazole is still a good product for Vivimed. It still contributes substantial and we still have leadership position there. But in terms of promising going forward, I would say I will bet on Pantoprazole, which is really doing well, which we have ground and then we have a unique position there and second, obviously is Esomeprazole which **sodium synonyms** in my opinion one or two companies in India only have it, like Cipla has and we have it and **(Unclear)** **26.06**. Till 2015, I think we will have this unenviable position in terms of this product is concerned. And the third one which is a lesser known and not much heard is a musculoskeletal disorder and anti-arthritic product called Etofenamate, which is picking up good volumes worldwide and we have seen some interesting numbers coming forth and I think we have almost kind of a monopoly situation over there without any competition coming from India and China. So I think I would say that I would really bet on these three products going forward in terms of revenue and profitability coming from this side. I think in terms of debt concerned product obviously is valid, because we have done some acquisitions in quick succession and partly we have borrowed, partly we have done, but one thing is certain is that I think we are trying to get confidence in terms of cash flow coming forward and business growth looking forward. I think strategy wise, it may not be appropriate for Vivimed to dilute now because this time we are ahead of us because so far I think only the outflow of funds we have seen and we have really not seen something coming out of it, so far we have seen only revenues that have added up to the inorganic revenue that has got added up, but have not seen coming out of it. So in my opinion I will really hold on rather than diluting at this point of time and definitely watch for next few quarters where I am very confident that Specialty Chemicals per se as well as Pharma, APIs and FDF, here we are again getting approvals are under way, so we would be on course. So I think I am not too worried about that part. And the third question, the acquired companies particularly the formulation company that we acquired has a very good track record and a good thing as well as East India is concerned and North East is concerned. Actually I am thinking exactly like what you are thinking. I think we have to increase our presence in western part of the thing, but we would like to do it in the phased way as you have seen during my initial talk, I said we have expanded to Uttar Pradesh, Uttaranchal and some parts of North India where we have manufacturing facilities over there and we have a little bit of edge over a lot of people, we are going to supply medicines from tax free zone, so I think our first focus will be like after Northeast India we go over to the Northern India where we have already started investing, like added people. The only **raise** we have seen that it is all consolidated and most of the investment that we have made are looking positive and profitable than we go to Western India. As you saw, Western India is a little more hard nut to crack particularly in Mumbai and other areas, so I don't think we would like to put our money right down there until we see positive cash flows coming from all the new areas where we have invested.

- Moderator** Our next question from the line of Rashmi Sancheti from MSFL, please go ahead.
- Rashmi Sancheti:** First question is can you give the breakup of other operating income, because this time it is quite high?
- K. S. Sastry:** Actually there was some grant that was received in Spanish company from the government grant, so that has been accounted there, that is why the other income is higher; that is the main reason.
- Rashmi Sancheti:** So this is like one-off?
- K. S. Sastry:** It is one-off.
- Rashmi Sancheti:** What about the tax rate? This has come down significantly. So like, what is your full year's guidance this year and next year?
- K. S. Sastry:** We expect that it will hover around anything between 18 to 20%, so even the future guidance we will look at that kind of range.
- Rashmi Sancheti:** Next question is, can you give update on OMC sales and Sun Care segment, whether they are picking up or they have declined this quarter?
- Santosh Varalwar:** OMC, as you said, we have kind of **(Inaudible) 31.12** ideally because one of our major customers ISP was acquired, if I recall, I have explained this last quarter, was acquired by Ashland, and after that there has been inconsistency in terms of their commitment to us, so OMC was primarily meant to supply to them, but with the change in situation, change of guard over there, we have kept away from it, but there are other products like **31.52(Inaudible)** and a few things which are going ahead and as you have seen, minus OMC, situation has not changed, it has been better than what we have done, but I again shared with you just now that the Sun Care season would typically begin now, and this year we have definitely got a much larger portion of the pie from Unilever, I think maybe more than 50% of their demand to Vivimed and we have also bagged a couple of large German orders from a company like Henkel and a few of that. And then there was a repetitive same thing coming back from L'Oreal; L'Oreal is our major customer, where we have seen almost like 3 to 4 Sunscreens we have supplied, so we have got again same repetition of orders where I think in one product we are almost like 90% of their market requirement and other products about 40%, so I think Sunscreen business, product say, like apple-to-apple if you compare, it is growing, OMC is only like something which we did not anticipate but that we have scaled down in terms of our projection also. There is a slight market picking up internally where we are selling. Instead of selling about 100

tonnes a month, we are selling about 20 to 25 tonnes a month, but that is purely not ISP, it is really being marketed by our own people in certain segments, mainly Asian segments, whereas if you see Sunscreen it is growing.

**Rashmi Sancheti:** You said that you have bagged German orders. That is in Sun Care segment or in Hair Dye segment?

**Santosh Varalwar:** It is only in Sun Care segment. Entire volume from Sun Care.

**Rashmi Sancheti:** And for L'Oreal, you are saying it is for Hair Dye segment?

**Santosh Varalwar:** No, it is all Sun Care. You asked about Sun Care, so I only talked about Sun Care.

**Rashmi Sancheti:** And this order you have bagged in this quarter?

**Santosh Varalwar:** Yes, last quarter.

**Rashmi Sancheti:** This quarter you have started ...?

**Santosh Varalwar:** We have supplies going for the whole year down. This quarter and the following quarter will be the peak, and then again it tapers down a bit. So normally like, that is how it looks. It is normally good in the Q3 and Q4, you will see a spike in sunscreens, and then it goes down a bit.

**Rashmi Sancheti:** What about Pharma business on a standalone basis? This first half has been declining on year-on-year basis and also the margins have dipped. So is it because of one-month shutdown in Jeedimetla plant or some other reasons?

**Santosh Varalwar:** It is clearly that order book very fine better than what was anticipated, but we had to literally shut down the plant for a complete **(Inaudible) 34:32** audit. What you see the impact is mainly because of that. And you will see that covering up during this quarter because again I think on order, there was a lot of valuation done in the plant, a lot of in-house capacity added up also, so you will see that coming back this quarter. It is only one-time; it is not a regular feature.

**Rashmi Sancheti:** Like when will it start improving?

**Santosh Varalwar:** It has already started now. You will hear good numbers coming in now.

**Rashmi Sancheti:** Can you give us the figure UQUIFA contribution and Klar Sehen and Octantis that is both retail branded formulation contribution to sales?

- Santosh Varalwar:** Retail branded formulations, last year we have done something like 19.8 crores, and this year we had budgeted something like 50 crores and we have done close to about 20 crores, and we have done close to our budget in the first half yearly now in terms of retail branded formulations. And in terms of UQUIFA I think we have two segments, as you know, in Spain and Mexico, and what we have targeted, we normally take current year, that is calendar year we take, we are almost there, we target about €42 million from Spain, there we have done something like €40 million. And in terms of Mexico, we have targeted about 350 Mexican Pesos, and where we have done about 325. So if you really look, add both of them in API I think by and large we are on target. And in terms of domestic formulations is concerned, I think barring this August, if you see half yearly, you might see a small dip, but otherwise I think next half year will make up. So all the three segments have been great consistency and that is the plan, as per budget.
- Moderator:** Our next question is from the line of Sapna Jhawar from Reliance Securities. Please go ahead.
- Sapna Jhawar:** If you could be kind enough to repeat the UQUIFA contribution? It was not very clear earlier.
- Santosh Varalwar:** UQUIFA, I said, we have the two accounts in two ways, and one is Spanish, where we have got two plants and Mexico, which is a separate plant. So, our budget for this year, that is for nine months now was about €42 million, and we have done about €40 million. And as far as Mexico is concerned, budget was about 318 million Mexican Pesos and we have done about 325. But if you really combine both of them I think by and large gets trail whatever we budgeted is there. And if you recall that during this year particularly compared to last year, we have not really kept any upside of the numbers, because a lot of actions to be confirmed we have made post acquisition, and the budget was overall for the whole year was about €78 million combined together and I think we are on target to achieve that.
- Sapna Jhawar:** We have received one in-principle approval earlier for an SEZ in Srikakulam. Have we started building any plant on that SEZ land or we are still waiting?
- Santosh Varalwar:** As I said earlier, like the plan was to get the API plant started in SEZ, Srikakulam, but somehow due to delays in getting environmental approvals, you would see a lot of stuff, (Inaudible) 38:32 approvals we got cleared in terms of public hearing last before quarter, which is the biggest landmark for getting a plant going. The second obviously like central approvals and state approvals. The central approval has just come in and we are waiting for state approvals. So we did not really wait for the plant to be started, because we missed the actions to be done from India. So what we have done is that we went and

acquired additional facility subsidiary from Spain, in Bidar Karnataka, and we started our API facility over there. In other words CAPEX which was meant to go in the first phase to Srikakulam has now gone to Bidar. In other terms probably like even after we get the EC approvals and all those things, we will not think about any CAPEX during the next half year and we look at plants next year. So, whatever our requirements are in terms of capacity requirements they are all being taken care in Bidar and Hyderabad right now. So, I think Srikakulam might have to wait a little longer because of the delay that already happened. So I think once we get this existing plant in operation and functional and capacity utilization is done, then we will put our next investment over there, until then it has to wait.

- Sapna Jhawar:** In a earlier con call you had mentioned that our total CAPEX for the year would be around 75 to 100 crores. Are we still maintaining that CAPEX budget, if you can just speak on that?
- K. S. Sastry:** The CAPEX budget, we had about 80 crores have been spent during this year and we intend to keep this slight, earlier it was thought that we will be doing about 100 crores, but probably we might be touching around 120 crores during this year based on the current updates on the project side.
- Sapna Jhawar:** My next question would be we have about some 18.5 lakh shares approved to Kitara at about Rs 327 per share. So when is the allotment due or have you already allotted those shares, have these shares been converted yet?
- K. S. Sastry:** Right from the beginning they have been issued the shares. They directly contributed to the equity. Direct issue.
- Santosh Varalwar:** There is no conversion in that. There is a conversion in other one, Jacob Ballas; I think which is going to happen in March next year or April it will be converted.
- Sapna Jhawar:** So both Jacob Ballas and Kitara, the preferential shares have been converted, is it?
- Santosh Varalwar:** No, the preferential was not given to Kitara, it was directly shares given to them, and so it was converted right from day one. And CCPS, Compulsorily Convertible and Preference Shares were given to Jacob Ballas, which will get converted in March or April 2013.
- Sapna Jhawar:** Another thing which we noted from your presentation was that in April 2012, institutional shareholding was around 21.8%, which has come down to 15.4% in November. So, with DSP BlackRock exiting completely and Emerging India Focus Fund have been continuously reducing stake, any particular reason that you would like to highlight?

- Santosh Varalwar:** DSP BlackRock to the best of my knowledge, when we had a meeting with them in a couple of conferences, they came back and said that they were not too happy with our Pharma expansion and they thought that putting more money in the Specialty Chemicals and we do not know their stance on it, but I think we are in line with our plan expansion plan And coming back to Emerging, of course, he was one of the early investors who probably come at very low price, if I recall he entered around 100 levels or something. So that is probably encashed. No other reason. So that is what I guess..
- Sapna Jhawar:** You mentioned earlier that you received some large orders in your Sun Care segment and Specialty Chemicals and I think we were maintaining that second half of FY13 would be much better for our Specialty Chemicals segment. So what kind of run rate do we see going ahead in the second half for Specialty segment because we have seen that the EBITDA margins or the PBIT margins rather have also come down in this quarter?
- Santosh Varalwar:** I think you are right. Specialty Chemicals business looks always better in the second half of the year and more so as I mentioned some capacities have been created and those have been going to operational by December. So even if you do not get Q3 numbers on, but Q4 numbers will be definitely be better when that capacity also is created. So I am sure there will be tremendous jump in terms of revenues and profit coming from the Specialty Chemicals in the second half, particularly in the last quarter.
- Sapna Jhawar:** In this particular quarter, we have seen a dip in your EBITDA margins sequentially in both Specialty as well as Pharma. So Pharma, we can largely assume that UQUIFA since it has low margins this could be a reason, but then in Specialty going ahead, what kind of margins do we see?
- Santosh Varalwar:** Specialty Chemicals business, as I said, primarily depends on customer approvals and a few things, that is one bit of **(Inaudible)** we always live with it, and as I explained in opening statement, Triclosan did impact the revenues and profits definitely during the last quarter, we expected this particular product, last year we had done about 410 tonnes and we expect it to go about 610 metric tonnes for the whole year, but on the contrary we should be happy if we can manage to maintain that level. Primarily of certain customers, taking negative report that came on like then seriously, but there is a lot of supporting data given by Vivimed to all those companies as well as American Ministry of Council which approved whatever concerns are there, they are really not true, and then we substantiate with data, but anyway I think we had to see the downward swing and the good news is that there are some companies like Colgate trying to come back and trying to use Triclosan back again, so we are expecting some orders coming from it. Just to give you probably a point blank I think that we would see that the next two quarters should see better positioning and particularly the next year again because of a lot of work having

done on new Hair Dye Intermediates particularly with P&G and few large customers, we are expecting some upside coming from that. So Specialty Chemicals typically depends upon major customers and products approvals and all, sometimes that is one, which is in certainty, the delays are there from that side, we cannot enforce that, but I am expecting like at least the (Inaudible) 46:21 should be bridged down very soon.

**Sapna Jhawar:** My last question would be for Mr. Sastry. Do we have a large impact of currency in this quarter because our gross margins have significantly reduced on a sequential basis, so any color on that?

**K. S. Sastry:** On the currency side, we have done a little better during this quarter; there has been a gain for this quarter. So, we expect like I said in the earlier earnings call, we are very conservative on this side, in fact, we would being an export oriented company, we have to a large extent natural hedge, and we play safe instead of like hooking up all our earnings. So in that side, I think we have been like no big gain, no big loss kind. So we had a gain this quarter against purchasing loss in the last quarter.

**Sapna Jhawar:** Can you just quantify the gain and loss in both the quarters; Q1 and Q2?

**K. S. Sastry:** The gain is around 2.4 crores, I am talking about standalone basis, on a consolidated basis it was 4.2 crores of gain and losses for the last quarter on a standalone basis, it was around 2 crores of exchange loss, and there was a gain of 1 crore on consolidated basis.

**Sapna Jhawar:** This is booked under which line item, other expenses?

**K. S. Sastry:** Other expenses, you are right.

**Moderator:** We will take our next question from the line of Vishal Jajoo from Nirmal Bang, please go ahead.

**Vishal Jajoo:** Just wanted one clarification of the reason for the fall in the margins, because you were not audible at that point in time. One is the closure of the facility at Jeedimetla for about a month and then the issues with regard to Triclosan. Apart from these two, were there any other reason for the dip in the margins both on year-on-year and quarter-on-quarter basis?

**Santosh Varalwar:** There is one more which we have probably not touched base is typically if you look at August, is a month where it is a vacation time, it is about three and half weeks of vacation over there, so typical run is about €4.5 to 5 million that comes from that particular factory, and obviously this one month, which always was less than half of that. So that is

also one of the reasons which had probably contributed. And that situation will come otherwise.

**Vishal Jajoo:** The lower tax rate in this quarter, was there any specific reason, or 18 to 20% which has been guided for that, that would be the rate going forward. Then if that was the case, any particular reason for the lower tax rate in this quarter

**K. S. Sastry:** In this quarter, there has been Spanish company that has been deferred tax gain is there, so that is the reason you will see lower tax gain, but going forward I think in March we will be looking forward for this 18 to 20% guidance.

**Moderator:** Our next question is from the line of Charulata from Quest, please go ahead.

**Charulata:** I want to know how much is the capacity utilization at Brazil and Spain?

**Santosh Varalwar:** Actually, Spain incidentally, the Spanish way, they are still working on a single shift basis or little extended shift basis, which means like they work five days in a week, and then they work about 8 to 10 hours per day, unlike many API plants across the world, so if you really like calculate the amount, capacity utilization, because all API plants are supposed to function on a 3-shift basis and continuous process, but in one certain case, which I think after post we made acquisition we are trying to do some changes, but they **(Unclear)** quietly, I think about 50% capacity utilization for **(Unclear)** in Spain, in both the plants, and Mexico, by and large is over 90% capacity utilization, and we have not touched upon, but we have also started capacity expansion in Mexico, we got the order position coming forward next year in certain products, and we are also creating different capacity expansions in Spain, because of one new product that we have signed contract with one customer, which would get into commercial mode by the end of December or early January, so it's a next year contract. So coming back to other plants in India, I think by and large, most of them are, unless it is a new plant, the capacity utilization is really because it was orientation and stabilization period, but **(Unclear) 51:45** is about more than 80% to 90% capacity utilization, and formulation plants, all run single shift, so the capacity utilization is only on single shift. We do not run round the clock, all the formulation plants.

**Charulata:** Second, could you highlight the change in the receivable cycle? Last quarter I believe the standalone receivables were lower compared to consolidated, but this quarter it is the other way round.

**K. S. Sastry:** Charulata, there has been increase in the sales during the quarter. So obviously the majority of sales has happened in the second leg of the quarter, so those receivables are



falling due in October and November, some of them even December, that is the reason we see the increase in the receivables.

**Charulata:** On consolidated basis.

**K. S. Sastry:** Yes, on both sides in fact, more or less.

**Moderator:** Our next question is from the line of Mr. Suryanarayan Naik from Network Stock. Please go ahead.

**Suryanarayan Naik:** Just want to understand what you see your turnover going forward let us say 2015, now that it is equally divided between the Pharma and Specialty of around Rs. 3 to 3.3 billion. Because going forward what I see, the traction from the Specialty Chemicals is going to recede and you are expecting more jump coming from the Pharma business, which is less remunerative or less profitable. Where do you see your margins going forward and how do you see the growth in the profit going forward?

**Santosh Varalwar:** If you look at it, Suryanarayan, one thing you should bear it in mind is that, in Pharma business, Vivimed, a substantial portion of Pharma business comes from regulated market, so I would not really agree with you that the Pharmaceutical business is not profitable business. Yes, if it is totally a domestic oriented and APIs are all sold in domestic, yes, definitely fight for the pennies, but where is a regulated market, where your plants are all US FDA approved and you are supplying to large customers it is not great, so that is what has affected even the gross margins that you can see. There is the second aspect as far as Pharma as concerned. Yes, retail branded formulations is again a very cream of the market, you are not selling products, like for pennies and then you have a branded identity and there again you will see that consumption of raw materials is comparatively much lower than this thing, that is again niche business, so you will not see profit dipping from that kind of business and what you really see is the companies are dependent on contract manufacturing and more of a job work kind of model, then yes, I think it is a very thin margin business but strategy wise, we are definitely looking at more of a regulated market business and as I told you in my discussion, the approval of our Jeedimetla plant for Pharma, once that comes in then you are addressing an interesting segment of semi regulated market where your margins are far better. You know where you are really going to sell and what kind of products you are going to sell. I think you will still remain bullish on that part of it. Specialty Chemicals business is a niche business, there is no doubt, the only thing that here we see is that the approvals and new products coming are a little slow in terms of the things, but if you see historically Vivimed has been consistently growing 30% to 35% in Specialty Chemicals and we do have a pipeline for it. And more so, I would like to make comments here that particularly the current year, we

have been adjudged as a "Strategic Partner" between the three large companies in the world that is P&G, Unilever, and L'Oreal. So this status would definitely give us more access to their innovation platform compared to other European companies, Vivimed is much proactive. So I think our engagement with these companies should step up more than what we have been doing in the past. I think Specialty Chemicals business will not really go away from the target of growth and the Specialty Intermediate which again is a part of Specialty Chemicals group and that is looking up because of new contracts and all. So I am still hopeful that barring a couple of quarters, because of changes approval, time taken for approval, but in 30-35% growth from Specialty Chemicals, I would still bet on it. And my Pharma business will not be a commodity business, definitely we are looking at something interesting coming forward, so we are talking about revenues going forward for the next two years, we have enough strategies and enough ideas and plans to see that revenues and profit growth for the company.

**Suryanarayan Naik:** Out of the Pharma business, total Rs. 3.3 billion how much are you generating from the regulated market and how much from the unregulated market as of now?

**Santosh Varalwar:** Yes, if you look at it, I think 75% of our business is a regulated market business, but it is not a low profit business.

**Suryanarayan Naik:** If you can segregate differently, like how much it is coming from the branded formulations and how much is it coming from the API?

**Santosh Varalwar:** 330, out of 330, I think...

**Suryanarayan Naik:** I am asking about the analysis of the 3.3. How much is it coming from the API segment, and how much is it from the branded formulation?

**Santosh Varalwar:** Do you have the break up, Sastry?.

**K. S. Sastry:** It is not in hand, I guess it must be ...

**Santosh Varalwar:** Roughly ballpark I can give it to you. The branded formulations we have got is only about 16 crores in the first half, that is this year, and non-branded, that is Eastern Europe and other contract manufacturing, that was about close to 70 crores, so that is about 86, so the 331 and 86, about 250 crores came from APIs; the balance came from APIs.

**Suryanarayan Naik:** Going forward, you see only the growth in the API segment, not in the branded formulations, which is tend to be a little bit profitable business. So how do you see the market panning out for you?

**Santosh Varalwar:** If you observe what I said, I think last year, the branded formulations was 19.8 crores and this year the budget was 32 crores, and we are probably clocking the same run rate, and going forward I think the retail branded formulations are, we expect to grow much faster because of the addition of new areas and new products that are coming on. But the only thing is that we are doing apple-to-apple comparison, what the revenues were there and compared to what the growth is there, then percentage wise is good. But on overall it might look smaller, and when it comes to the other than APIs, other formulation business is concerned, I think once we have this approval, I think that goes to the business shift to semi regulated market, so substantial revenues will come from there, which again is a profitable business and API business, if you look at it today, it is all regulated market business.

**Suryanarayan Naik:** Another point is which are the therapeutic segments you are targeting in the regulated and semi regulated markets, if you can throw light on them?

**Santosh Varalwar:** In semi regulated market our focus is definitely on anti-tuberculosis range and oncology range that is where our major new stations are lying there and once the approvals come in, that is where we will come into play. And in APIs, you have all those breakups. It is mainly an anti-(Inaudible)1.00 segment, which continues for substantial volumes.

**Suryanarayan Naik:** In the Tuberculosis segment are you targeting first line of drugs, or second line or third line of drugs, how is it actually?

**Santosh Varalwar:** It is all first line, different form, new drug more in a palletization form, more in a sustained release form. So some of the products are developed by Vivimed and we are like first line, sodium PAS granules and all are first line of treatment. But I think there is still (Unclear)1:01:23 market in the market side.

**Suryanarayan Naik:** Tuberculosis and Oncology, you might be targeting a sub-Saharan market and other poor countries, where the disease profile is quite prevalent. So how do you see the margins coming from that? I mean, you said the majority, you are targeting in semi regulated market for anti tuberculosis and oncology. So, it is not that profitable compared to other life cycle diseases. So what is your portfolio going to be in the other segments like CNS and other things?

**Santosh Varalwar:** If you really look at our existing manufacturing capabilities and our manufacturing capacities, we have only one plant right now, which is going to get the FDA approval, it is a fixed approval, which is like a European approval, which I mentioned that we have just got it. And RO plant, which I was saying in terms of forward integration, the new plant, which is coming up at Jeedimetla that would take time, another 12 to 15 months before

we have a manufacturing facility, which has got a US FDA approval, and where we can get into certain regulated market. So until such time, like one plant that I have in Jeedimetla, which is only capable of producing, so this is the only plant, which will cater to this market, and then oncology market which we are right now targeting particularly in Ukraine and Russia, and all, I think most of these government tendered business and margins are pretty interesting and pretty good. They are not as bad as what you are talking and they are pretty good. The **(Inaudible) 1:03:09**, and a few things, again are still supported by government in Russia and Ukraine, and because of the delivery form that we are giving and is accepted and approved by them, and we are getting a consistent order and that looks to be pretty good. And other third area where we have also seen **(Inaudible)** regular general products like bronchodilators and a few things, which are codeine based formulations, which are doing pretty good in those areas, which are again a good volume builders as well as bottom line builders. So I think until you have a new plant in place, our strategy will be still to hover around these areas what you mentioned and then relook at our strategy once we have a regulatory plant, which can cater to the much larger segment of the business.

**Suryanarayan Naik:** For these US FDA approvals, how long it will take to get the approval in place.

**Santosh Varalwar:** This plant will get probably be ready for inspection somewhere in September next year, so I think validation, batches and all, I will not see them coming till March 2014.

**Suryanarayan Naik;** Anything can be possible maybe FY14 end or FY15?.

**Management:** March 2014 it will be ready.

**Suryanarayan Naik;** It will be ready, but do you expect the inspections to be over?

**Santosh Varalwar:** I am talking about approval, because the plant will be ready in at least 8 to 9 months before that. And because it is our own product line and our own APIs and some things, so we will get the inspection done pretty quickly, we have a system in place to get the inspection done, so which means I think we should be ready to supply from that plant by March 2014.

**Suryanarayan Naik:** Another point is in your presentation it has been mentioned that some of the overseas facilities, you want to bring into Indian base. So which are the operations you want to bring it to India and how much of let us say, margin expansion you are looking at or you are expecting out of those activities?

**Santosh Varalwar:** I want to make it clear here, that I am not looking to stop any plant outside India right now. There are three facilities outside India. One is the Mexico plant, which is like going full swing and we are investing money back in Mexico for creating additional capacity for certain orders, guidelines we got from the customer. And coming back to Spain, I think we have two plants in Spain. Eventually what we are planning as a strategy, try to move some of the cost competitive or very competent APIs back to India for the business to be made, but otherwise we have no plans to shut down the plants. Both the plants in US FDA, EMEA and MHRA and TB approved plants, we like to leverage those advantages from those plants and look at the different product grouping, and as I mentioned probably last quarter, I said we are working with some of the innovator companies to pick up certain products, which are like the more suitable for that geographic region, but I think at this point of time, I am clear that we are not shutting down any plants and we are going to keep all the plants running and wherever we want to play the advantage of Vivimed and UQUIFA being **(Inaudible) 1:06:39** one is in India and the other is in Europe, and the other is in Latin America, and in going forward I think this is the most ideal situation that will emerge. I think that the customers from my perspective and my own experience would like to have a de-risk model, they would not like to buy everything from one country or one continent. So I think Vivimed and UQUIFA are the perfect situation today with three continents and three geographical locations, I think we should not do any kind of optimization anyway except that you have to move the products based on margins to different geographical regions.

**Suryanarayan Naik:** Going forward, let us say, fix a target year of 2015, from different two verticals; one is your Specialty Chemicals from Rs. 3.3 billion. At the moment it is, we are observing quite a bit of stagnation. So when do you see the revenue going to different places?

**Santosh Varalwar:** If you see again, I should split that answer into three parts. One is, API business, for API business you will see flat for another 6 months to nine months, because until we have plants ready in India, and until you have other things coming up, you will not see any spike coming out of it. So we are expecting FY14, that is next year, like revenue increase from API business, and the other two businesses are growing at FDF from retail plant growing at 40 to 50% and will continue to grow and Specialty Chemicals will continue to grow like 25% to 30%, it can be a little slow, but we will buck up on it, so overall you will still find it. And API I think will pick next financial year it will pick up. Once you see, then I think I will be in a better position to give right guidance in terms of number.

**Suryanarayan Naik:** Don't you think the global slowdown, especially in Europe area will have some cascading effect for your Specialty Chemicals or your lifestyle chemical business?

**Santosh Varalwar:** Yes, I think that observation we have seen it, particularly in Europe and USA. The growth has been almost like stagnant or even some de-growth in certain segments, but the good news is that I think Asia presence, and Asia manufacturing helps us. And if you have seen the guidance of lot of this for companies like L'Oreal and Unilever, I think the next 10 years, expect 80% of their growth coming from Asia and may be about 15 to 20% coming from Europe and America. So that will be a real scenario and we should accept it. But the only difference for Vivimed is that we may be still a small company in terms of Specialty Chemicals offerings and in the first two years we have taken advantage of our Asia positioning and Asia manufacturing and we have taken the businesses from other major companies, and that situation will not change for us. So our growth will predominantly come from taking away businesses from others rather than looking at other percentages that will happen in different geographical regions. And as far as Asia is concerned, I think India is particularly looking good and China is looking good, and Indonesia and Thailand are other exiting areas where you are seeing a lot of action happening in this Specialty Chemicals business.

**Moderator:** Thank you. Participants that was the last question. I would now like hand the conference over to Mr. Siddharth Bhotika for closing comments.

**Siddhartha Bhotika:** Hello, we will call this question and answer session to an end now. I take this opportunity to thank Mr. Varalwar and Mr. Sastry for joining us on this con call. A pleasure to have both of you here sirs. Thank you everybody for your participation.

**Santosh Varalwar:** Thank you, all. Thanks for being with us.

**Moderator:** Thank you. On behalf of Tata Securities Limited, that concludes this conference. Thank you for joining us. You may now disconnect your lines.