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“Vivimed Lab Q3-FY13 Earnings Conference Call”

February 20, 2013



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MANAGEMENT: MR. SANTOSH VARALWAR – MD & CEO
MODERATOR: MR. ANMOL GANJOO – ANALYST, ANTIQUE STOCK BROKING



Moderator

Ladies and gentlemen good day and welcome to the Vivimed Labs Management Q3 FY13 Earnings Conference Call hosted by Antique Stock Broking Limited. As a reminder all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. Should you need assistance during this conference call please signal an operator by pressing * followed by 0 on your touch-tone phone. Please note that this conference is being recorded. I would now like to hand over the conference to Mr. Anmol Ganjoo from Antique Stock Broking, thank you and over to you sir.

Anmol Ganjoo

Hi good morning everyone thanks to the Vivimed Labs Management team for joining on their 3QFY13 conference call. The format of the call will be as follows. We will start with opening comments from the Vivimed Lab Management, Mr. Santosh Varalwar, will give his opening remarks and explain how the quarter went by and then it will be followed by Q&A session. So, in the end if the participants have anymore questions they can feel free to contact either the Vivimed Lab management or us here at Antique Stock Broking. With this I hand over the call now to Mr. Santosh for his opening comments. Thank you.

Santosh Varalwar

Good morning everybody this is Santosh, so welcome to this call again. The year to date performance remains pretty robust. We have recorded an increased income of 97% compared to last year even EBITDA has grown up and PAT has grown up. Compared to Q3Y year-on-year consolidated income has gone up by 62% and EBITDA has gone by 12% and PAT has gone up and sequential quarter there has been slight impact because of some of the subsequence events. However projects that are underway creation of pharma intermediate block is completed and last quarter we have started the trial batches and product approvals are in the process for the main **KSM's (Key Starting materials)** And also the other projects mainly building of API facility in India is underway and various other projects in specialty chemicals are by and large completed. In regards to pharma formulation we had inspection by Ukraine authorities that went through but I think we are going to have one more inspection in this month and after that you will have one plant fully approved by European FDA so yes I think compared to last quarter there have been one off events mainly Vivimed Labs Spain, Uquifa has signed a contract of CMO business from an innovator company and last quarter we were doing validation batches and engineering batches, obviously the initial phase you will have obvious reasons for like lesser performance because of involvement in doing engineering batches and also the optimization of yields and other things but come off January I think it's in good shape and going forward and we have for a modern place and Spec-Chem, Spec-Chem yes I think there has been an impact because of Triclosan continuing to impact the top line and bottom line sales for bad press on Triclosan. However there has been alternate reports from American Cleaning Institute confirming it's still safe but there

has been like blow hot blow cold situation in Triclosan continuous to be there and the other major impact which we had in this whole year because of the OMC plant. Good news is that I think we recaptured the plant and we reallocated the resources and the different reactors to other products and we had almost had about two new products launch into that one is anti-dandruff compound another sunscreen I think they have come to a commercial level, I think you would be seeing in the coming quarters now revenues coming from there and good news is that I think one of the products we also bagged an order from L'Oreal so we should see at least next financial year we will see some numbers coming up from there, otherwise yes I think we still maintained on a consolidated basis the revenue outlook has not changed it is still going to be around INR 10 to 11 billion and PAT of 900 to 950 million. The business in general looks good, pharma looks pretty robust in terms of order book for this quarter particularly in Spain. Mexico has been fairly steady this thing except for December we had one off holidays where almost three weeks plant was closed in Spain Mexico that impact otherwise I think Mexico plant is going fine. So, I think nothing specific, things are going on and I will be open for any questions if you have any. Thank you.

Moderator

Thank you very much sir. Participants we will now begin with the question and answer session.

Anmol Ganjoo

This is Anmol Ganjoo. The only question for Mr. Santosh on the quarter when you talk about the one off events during the quarter, which of these events do you think have the potential to repeat themselves and which were transitional, so when we look at the next quarter or the full year FY14 and look in terms of margins what are the drivers which you think were just this quarter phenomena and won't repeat themselves and in that case what is the EBITDA margin level that we should be looking here on a full year FY14 as well as the next quarter basis.

Santosh Varalwar

Yes, I think the one off events, the sad is major account was the CMO business which was bad last quarter and then particularly last full quarter where the engineering batch is going on, initial batch is going on, so until the product gets stabilized you would really won't get the required yields so normally it's stabilization phase and as we have seen in January it's almost stabilized so I guess we will not have the reputation because it's a normal course nothing I am specific about it. And the second major one obviously was some civilian castes which we had in Europe some optimization after post Uquifa, we are trying to relook at the Europe as such because we have two bases in Europe one is the UK and other Huddersfield other is now in Barcelona so we are trying to optimize the manpower so in the process of that we optimize few people in UK, so there was one of severance cost which were also involved in that and there is also an impact of some products that we have used intermediates, which one off intermediates which we have used in this CMO business which obviously was not up to the mark so we had to create a provision and write



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them off because December still remains year end for Uquifa Spain. And going forward I guess these are not repeatable things and we should still maintain a reasonable EBITDA margins as we have forecasted.

Anmol Ganjoo which will be around what levels?

Santosh Varalwar It should be around 17% - 18% level on a consolidated basis.

Anmol Ganjoo Okay I will join back the queue.

Moderator Thank you. We will take the next question from the line of Mr. Deepak Agarwal from Anand Rathi, please go ahead.

Deepak Agarwal Sir, wanted to know how much of Uquifa contributed in this quarter and can you let us know the Uquifa margin currently likely to be whether it has improved from 14% to 15% level.

Santosh Varalwar Uquifa's contribution is 114 crores in this quarter and the margins on the contrary declined during this quarter EBITDA margins as I again said it's mainly because of this specific events which have bring it down but in general going forward I think it will stand corrected during the current quarter and we would see the EBITDA margins to go up to 13% - 14%. We won't see any major shift in EBITDA margins until the end of this financial year but definitely going forward with some of the business improvement plans that are already set in and pharma intermediate production happening in India, and we can definitely hope to see some improvement in EBITDA margins next year specifically for Uquifa.

Deepak Agarwal And sir one more, just can we have the debt numbers as of now and what is the cash balance?

K.S.Sastry Well debt on consolidated level including the short-term borrowings is about 630 crores and what else you said, you wanted to know?

Deepak Agarwal The cash balance.

K.S.Sastry On consolidated level it is showing about 17 crores of cash balance.

Deepak Agarwal alright sir, sir that's it from my side thank you.

Moderator Thank you. We have the next question from the line of Sapna Jhawar from Reliance Equities please go ahead.



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Sapna Jhawar

When I see your press release I see that from FY12 levels our borrowings have increased significantly in nine months of FY13. So, any specific process where we have outlaid this debt or where it has been used and second what will be the total contribution of Triclosan to our sales?

Santosh Varalwar

I will take you this question. See the debt is gone up primarily on account of various projects that we initiated. There has been a capital expenditure that we incurred outside India mainly in Mexico as well as in Spain for the new projects that are coming on way and In India again these nine months we have seen pharma intermediate block being built and we also revamped the pharmaceutical FDF (Finished Dosage Formulation) at jeedimetla facility to upgrade the European standard and we also are underway constructing an API facility in Karnataka Bidar and there has been expansion also in Hyderabad, specialty chemical factory and we also acquired one more manufacturing facility in Hyderabad for contract manufacturing for formulations mainly to address the needs of the company while we have existing approved facility for European markets. So these are the reasons for this and coming back to your second question on Triclosan. Triclosan today stands at revenue of less than 5% on a consolidated basis to be précised it's about 3.5% and if you look at standalone I guess it should be about 6% to 7% so it's not a major product but yes, I think for US it's important product for us because for Triclosan we are the only company in the world having EPA registration and raw material production agency registration. so there are lot of customers who use Triclosan in the non-personal key products like industrial care, so from that prospect it is significantly important to be made in terms of owing the responsibility of the molecule. so we are trying to support our argument in terms of why Triclosan is still safe being of course backed by American Chemical Industry and other things. so we will have to see how things will shape up but we have been seeing the up and down on Triclosan for almost two decades now I think. But this time, I think things are blowing against us. So let's see how things will really take shape. But just to answer your fair thing is about on a consolidation it is not more than 3.5% to 4% of Triclosan.

Sapna Jhawar

Right, but then when we see the rational of the muted performance in the specialty chemicals business it's due to lower off take of Triclosan so I mean are the other products contributing even lesser than that so that it has a huge impact on our specialty chemicals business.

Santosh Varalwar

See as I said there are two things which impacted obviously on like specialty chemical basis if you see the impact is about 7% of revenue Triclosan did not take off the way it should take and the second one is that we factored a huge off take of Octyl Methoxycinnamate (OMC) which is a sunscreen which did not happened during this year and Vivimed had to go for a revamping the whole production block to suit the capacities for other products. So if you see, that we have launched two new products

in the same block which means non-utilization of capacities for some time mainly on anti-dandruff product and one new sunscreen which has just come in but the volumes have really not picked up we just picked up a good order from L'Oreal and which will be seen more in the FY14 rather than FY13 so I think it's an impact of various factors which have determined that.

Sapna Jhawar Right and also the business details the order book details that is mentioned in the press release more of it is likely to come in FY14 but any guidance on what contribution could come in, in Q4.

Santosh Varalwar Contribution from specialty chemicals?

Sapna Jhawar From a specialty chemicals yes.

Santosh Varalwar I think specialty chemical in Q4 will remain at the same level as last Q3. We typically see the sunscreens off take being better and now it has slightly started tapering down during the first quarter of the calendar year which is Q4 for us then but you would see the other products taking off so I wouldn't see any major shift in terms of revenue outlook in the Q4, but yes I think going forward FY14 because of some new products in pipeline I am sure we will see a spike in that.

Sapna Jhawar So, normalized 20% growth outlook would be fair enough to assume at this level.

Santosh Varalwar Yes, I can even look better than 20% because of some pipeline products which are almost seen at approval stage it is the last quarter and even in this quarter we have some new customers which have come in and as we have also mentioned that we are entering into two new segments mainly the fragrance segment and the silicon segment. So the traction has already started with customers and we would see some orders slowing in the first quarter of next year onwards, so I think revenue steam will start looking better from there. So, I think the mix of organic growth from the existing product range and the new products to the pipeline and the new approvals that are coming through should see over 20% growth next year.

Sapna Jhawar Right that is helpful. Sir, another one on Finoso acquisition, when do we see it I mean completing would it be completed in this fiscal year or and how would the payments being made the deferred payments, is there scheduled planned for this.

Santosh Varalwar Yes, I think if you have seen Finoso the acquisition had part cash and part stock so I think we intent to complete this acquisition, we will close this acquisition before 31st March that's why we have called for EGM on 12th March when the EGM is over then I think we will go ahead and complete this transaction. I think the deferred payment other one is more on milestone basis so we are obviously expecting Finoso to

perform in terms of developing & filing new dossiers for the company. So obviously we will link the existing technical team and existing promoter in terms of milestone payments. So based on that I think we will have five year milestone payments linked to a five year performance. So idea is also to retain over the next five years because that's where the value add will come for the company overall.

Sapna Jhavar

So, does Finoso come with a package of dossiers along with it ready to file or would we start from scratch before filing the dossiers.

Santosh Varalwar

Yes, Finoso is an existing research lab for formulations and they have been in the service for almost five years filing dossiers and right now they have got as many as 31 with them, now we will have to see as to how many of them Vivimed can use it because our idea is to like leverage our own API to see that we file dossiers so we can be cost efficient in terms of marketing our products. I guess out of 30 – 31 that we have existing, I think one-third of them could be used for our own usage and going forward as the indication I had received from people is that they can file at least one dossier every alternate month so which is good enough, which means we can expect about six dossiers to go from our side every year besides whatever we have.

Sapna Jhavar

Right, sir any color or I mean what therapies would these dossiers be based on and the market that they would adhere?

Santosh Varalwar

See I think the first target would be to see how we can leverage the API positioning of Vivimed/Uquifa, so obviously like our focus should be on that and the second quadrant when we move to the next level we would look at some interesting compounds and combination therapies and different things, but they will not be focusing on any specific. I think primarily the initial phase is utilized by our domination on anti-ulcer segment and that is where we are focus initially. But going forward, I think we will look into more value added things.

Sapna Jhavar

Right and sir last question from my side. Any tax guidance for FY13 and FY14 going ahead.

K.S.Sastry

Santosh let me take this question, On the tax side in fact we had set of reversals from the previous quarters, so on a consolidated level we are looking at 10% on PBT, whereas on standalone it could end up somewhere between 22% to 24% as a guidance for the year end.

Sapna Jhavar

Right so, did we book any FOREX loss this quarter?



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- K.S.Sastry** No, in fact we had a very small, very thin gain of about a crore of rupees on consolidated that's what split into about 75 lakhs on a standalone and about 25 lakhs on consolidated basis.
- Sapna Jhavar** In which line item have we included this FOREX gain or?
- K.S.Sastry** Ma'am that is included in the admin expenses and grouped under other expenditure.
- Moderator** Thank you. We have the next question from the line of Rashmi Sancheti from Sunidhi Securities, please go ahead.
- Rashmi Sancheti** How much has retail branded formulation has contributed in this quarter as well as for the nine months?
- Santosh Varalwar** Yes, I think this quarter it's about 6 crores roughly.
- Rashmi Sancheti** 6 crores okay and for nine months.
- Santosh Varalwar** Nine months it's about 22 crores.
- Rashmi Sancheti** 22 crores okay and you have received \$2 million order from Ranbaxy it is for which drug?
- Santosh Varalwar** I think it's for acyclovir, we have contacted, acyclovir is already there in our file so we started supplying acyclovir earlier also and they are taking this time also. I think they went ahead and gave reasonably good volume for the whole year.
- Rashmi Sancheti** Okay pardon which drug?
- Santosh Varalwar** Acyclovir.
- Rashmi Sancheti** Okay and these \$2 million is just for fourth quarter or for the entire.
- Santosh Varalwar** No, it's for the whole year.
- Participant** CY13.
- Santosh Varalwar** Yes, calendar year almost, yes you are right.
- Rashmi Sancheti** Okay and next thing is that how much capacity is being created in Bollaram facility.
- Santosh Varalwar** I think we have almost about half a billion capacity for solid dosage formulations and almost roughly about six million liquid orals that should take care of our institutional



and domestic market requirements, as I said the whole idea of acquiring this facility was to meet domestic requirements, whereas the existing facility is now being upgraded to the European standards. obviously when we use those capacities for outside, we need something to fill up the domestic requirements so this year we will be taken care and will add up some more lines based on need and demand which will change from time to time.

Rashmi Sancheti Okay and my last question is related to annual report of FY12, can you just give us the break up of intangible assets. It is around 54 crores if you can just give the breakup it will help us a lot?

K.S.Sastry Santosh let me answer this, 54 crores you are saying on consolidated level right?

Rashmi Sancheti Yes, on consolidated.

K.S.Sastry In the past year FY12, we have acquired the business of **Malladi Specialty Chemicals** and their products, technology and also their customers and their markets that was the major thing that was capitalised and also of the products that we have been working for years together so the cost of developing those products have been accounted in that account.

Moderator Thank you. We have the next question from the line Amit Shukla from Omega Capital, please go ahead.

Amit Shukla Sir my question is about another acquisition, are we looking to acquire any other company apart from Finoso in upcoming future?

Santosh Varalwar See right now there is nothing on anvil. We just completed Finoso, it's mainly to support the filing of dossiers which right now we don't have internally so having geared up is to consolidate now.

Moderator Thank you. We will take a next question from the line of Mr. Anmol Ganjoo sir you may go ahead.

Anmol Ganjoo Yes, one last question from my side. On the pharmaceutical side \$20 million order when you have what is the margin profile you are looking at because my understanding is that this anti-HIV, antiretroviral business is fairly margin diluted so what is the kind of margins that we are working with and my second question is that on the spec-chem business, given the challenges that we are facing in Triclosan market in a two-year timeframe what is the breakup that we are looking at in terms of composition say how much would say fragrances contribute or silicon contribute and then Triclosan contribute, that's it from my side.



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Santosh Varalwar

Yes, answering your first question since we are doing this custom manufacturing for innovative company so margin dilutions would not really impact because we are not selling in the open market, we are not competing on margin pressures or something, it's a purely contractual with innovative company, so fairly they remain pretty stable in terms of margins and this kind of businesses relatively margins are pretty good, pretty robust and longstanding and these are also not one year or two years but literally a long-term deals, so I guess the margins will stay exactly the same level where the performance is going. And coming back to your second question on spec-chem it's too early to predict how the silicones and fragrances span out but as I mentioned earlier with these two things will obviously add to future like growths in terms of Asia but still we have got about 20% - 25% in spec-chem segment owing to other products which are there and we are also factoring negative impact on Triclosan so if Triclosan gets truly impacted still I guess 20% - 25% growth will be easily achieved year-on-year because of the products which have been launched last year and which have retained volumes particularly I mentioned about antidandruff product, I mentioned about new sunscreen, skin lightener so they are the ones which will really add more volumes in the coming years to drive the numbers. Fragrances and silicones are just beginning I really would not like to give any big indication on it but at the end of the year one I am sure we will see some traction and we can predict more correct the following year.

Moderator

Thank you. As there are no further questions from the participants I would now like to hand the floor back to Mr. Anmol Ganjoo for closing comments, over to you sir.

Anmol Ganjoo

Thank you Vivimed Management for joining us on this conference call to discuss your 3QFY13 results. We really look forward to your insights on the business and hope to continue this interaction that's it from my side, with this back to Mr. Santosh.

Santosh Varalwar

Yes, thank you ladies and gentlemen for being with us, I am sure you have got a deeper insight into our operations. As you could see clearly two drivers specialty chemical and pharmaceutical and as you have also seen there is a lot bit of activity going on in terms of pharmaceutical of course signaling the acquisition of Finoso and then ramping up capacities for APIs in Spain, Mexico and India and creating pharma space..... I guess, I think we have really steady growth plan and steady strategy going forward and I am sure like we will be able to deliver much better numbers going forward and thanks for being with us and please send us the mails if you have any further questions after this call and we would be glad to address them. Thank you, thanks so much.

Moderator

Thank you sir. Ladies and gentlemen on behalf of Antique Stock Broking that concludes this conference call. Thank you for joining us and you may now disconnect your lines. Thank you.