Vivimed Labs Limited

(NSE: 532660; BSE: VIVIMEDLAB)

Earnings Conference Call

Q2 FY2017

November 23, 2016

Mr. Santosh Varalwar, Managing Director

Mr. Ramesh Challa, Chief Financial Officer

Mr. Saurabh SG, Director – Corporate Strategy

Moderator: Ladies and gentlemen, good day and welcome to the Vivimed Labs Q2 FY2017 Earnings Conference Call. We have with us today on the call; Mr. Santosh Varalwar - Managing Director, Mr. Ramesh Challa - CFO and Mr. Saurabh S.G. - Director (Corporate Strategy). As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded.

Before we begin, we would like to mention that some of the statements made in today's call may be forward looking in nature and may involve risks and uncertainties. For more details on such considerations, kindly refer to the earnings presentation. I would now like to hand the conference over to Mr. Santosh. Thank you and over to you sir.

Santosh Varalwar: Thank you very much. Good afternoon everyone for joining us on this call today. Though late from the day we have concluded our Board meeting, due to some inconvenience but I think we are back here again. Hope you had a chance to go through the earnings presentation and financial results which are also available on the company website.

Moving to the discussion of the performance for the quarter and half year ended FY2017, I will start by providing the overview of our financial performance and strategic initiatives. Then I will pass on the call to my colleague, Saurabh to provide you detailed operational overview.

Our performance in H1 FY2017 has been in line with our expectations. In the first half of the fiscal year, we registered revenue of Rs. 6,679 million, a decline of marginal 1% year-on-year. This softness in revenue was primarily on account of decline in revenue from Specialty Chemical division due to the divestment of certain product lines effected earlier in the previous fiscal year.

EBITDA for H1 FY2017 stood at Rs. 1,281 million representing a decline of 1.8% compared to the same period last year. However, EBITDA margin remained relatively flat at 19.2% compared to H1 FY2016. Despite decline in revenue, the Company was able to sustain EBITDA margins due to improved utilization level as well as higher contribution of custom manufacturing within the API business. Continued focus on higher value products in Specialty Chemicals segment also benefited consolidated margins.

Our finance cost for H1 FY2017 was Rs. 302 million, a decline of 20.3% compared to the same period last year. This decline was due to repayment of long-term debt coupled with better working capital management. Net debt as of 30th September, 2016 was Rs. 8,074 million compared with Rs. 8,618 million as of 31st March, 2016.

Net profit for H1 FY2017 was Rs. 547 million, up 13.9% as compared to H1 FY2016. Net profit margin improved by 107 basis points compared to H1 FY2016 to 8.2%.

I would also like to inform that in the month of October, we completed the transaction with Clariant and the final tranche of funds were received and adjusted towards debt reduction.

We believe that going ahead the business prospects of the Company are promising as the various initiative undertaken by our teams look to be securing long-term growth and market position across the Pharmaceuticals and Specialty Chemical verticals.

With this, I now hand over the call to Saurabh. Thank you.

Saurabh S.G.: Thank you, Mr. Santosh. Good afternoon everyone and thank you for joining us on this call today. I will start with providing you the overview of the Pharma business which is today a largest segment of the group. The segment constituted nearly 76% of the total sales on a consolidated basis for the first half of this financial year. The segment grew nearly 5.4% on year-on-year basis for the first half for which a sales level of Rs. 504 crores. This growth was primarily driven by performance of our active Pharma Ingredients segment and within the API segment in particular the custom manufacturing line of activity where we have seen the strong interest and traction as far as the order book is concerned.

We believe that our strong market positioning in the API segment has enabled us to gain significant traction from both new as well as existing customers for the custom manufacturing business as well as the generic pipeline which we have. Furthermore, higher market share in our generic products coupled with the new product pipeline which we have been investing on, we believe will be instrumental in supporting our endeavour to secure faster than industry growth rates and profitability. As far as the Formulations business is concerned, focused on the US market, we continued to remain in investment mode and look forward to building a competitive product basket and we are tracking our new product filing targets for the near term on both the FDF as well as API business lines.

For our Specialty Chemical business, as Mr. Santosh alluded to, clearly we are in a period of transition after the Clariant transaction and the reported numbers for the first half have been around Rs. 161 crores which is a decline of 15% compared to the same period last year and this has primarily been to the divestiture of certain product lines which was done earlier in the last fiscal year. Despite the decline in revenues, the profitability in the Specialty Chemicals vertical improved by over 200 basis points which we believe is largely attributed to product mix and certain customer specific trends which we have been seen.

To sum it up, we believe that the efforts which our management team has undertaken over the past fiscal year have now started to yield some initial results and these measures coupled with our focus on new products, new customers and markets, we believe will continue to drive growth for Vivimed in the near to medium term. Also, we continue to remain committed towards further strengthening of our balance sheet which we believe will give us more flexibility to grow our chosen lines of activity going forward.

With this, I would now like to open up the floor for the interactive Q&A. Thank you.

Moderator: Thank you very much. We will now begin the question and answer session. We have the first question from the line of Suhani Doshi from Edelweiss. Please go ahead.

Suhani Doshi: Sir, can you give us details of the money received in the final tranche and how much of it has been used to repay and balance?

Santosh Varalwar: So, basically the whole deal was about Rs. 380 crores, of which some part had to go in doing some CAPEX and so the net result that we got it is something in the range of about Rs. 325 crores which we got Rs. 258 crores in the first tranche and the second tranche about Rs. 70 crores we got, it was that and this money has all gone to repay the debt and it went to the banks, so that is why you would have seen a substantial reduction in the debt from where it was in March till today also.

Suhani Doshi: This Rs. 70 crores is what we received in October, right?

Santosh Varalwar: Yes, you are right.

Suhani Doshi: So this Rs. 70 you also used for paying the debt?

Santosh Varalwar: Yes, you are right.

Suhani Doshi: Going ahead, March 2017 also we will see a further reduction in debt?

Santosh Varalwar: Yes, of course there are some repayment terms which probably will follow the suits so there will be some kind of debt reduction that will continuously go on in.

Suhani Doshi: And this Rs. 325 is after paying the taxes?

Santosh Varalwar: No, this tax settlement still to be paid, it is only the net amount realized from that.

Suhani Doshi: Another thing is if it is possible to give me the breakup of Pharma in terms of the API and the Formulation revenue?

Saurabh S.G.: See, we are reporting the numbers on a segment basis. So you have the first half numbers with you but I think just to give you an idea, the API business would be significant part of this, so at least 75% to 80% of the sales which you are seeing would be coming from API.

Suhani Doshi: Of the Pharma sale?

Saurabh S.G.: Yes, that is right.

Suhani Doshi: And another thing is the Specialty segment revenue of quarter two, would that be the base revenue or does it still include any other contracts which you have and I think last quarter you were doing some part of the revenue still for the sold off business?

Santosh Varalwar: Yes, I think the second quarter revenue Specialty Chemical still included a part of sales to Clariant. Now post closure in October, we have handed over the manufacturing facility to them, but we will still see some products being contract manufacture in other facility in Karnataka. So the revenues definitely compared to Q2 will come down, but whatever revenues will remain after that will probably remain for few years because it is a long term contract to continue support them in certain product segments.

Suhani Doshi: But any otherwise guidance on the growth of Specialty Chemical revenues now after this closure has been done?

Santosh Varalwar: Yes, the Specialty Chemical if you really see now, what we are having is a hair dye business which is definitely growing about 10% to 15% year-on-year at a global level and photochromic segment which probably if you look at last 3-4 years had almost like a flat growth but we definitely seeing because of the launch of certain products like Humber & Pennine and few of them which are patented by Vivimed. So we see, these are fast fading dyes, so we see a lot of traction coming from these products. There is a lot of demand coming from it. So if not further next few quarters at least for the beginning of next year, we should see a ramp up in demand for these new fast fading photochromic chemicals which we find it has significant interest across the globe from major players from Japan and US and Europe and so I think we would see that coming up and there is also some active discussions going on with certain customers in trying to add more product lines in the photochromic segment. In antimicrobial segment, Triclosan is continuing to de-growth in terms of our revenue. Triclosan as you are aware had taken a setback in terms of FDA's restriction in certain areas, but the demand from the toothpaste manufacturers particularly Colgate and Hindustan Unilever's Pepsodent, they seem to be still going on. There is no decision taken by them to taper down or remove the Triclosan from it but definitely Triclosan impact has come into the industrial segment, so you might see some numbers going down from that segment but there are of course some new antimicrobials which Vivimed has developed and we are testing those products in the market and we have seen significant interest coming from customers and I am sure like in next about 12 months to come. I think those are the lines which we will some growth coming from it and there is absolute clarity in terms of companies that we are only focusing on high-end specialty chemicals and not taking any road towards commodity kind of things. So we would be more selective in terms of using our assets going forward in Specialty Chemicals.

Suhani Doshi: So it will be you will be looking at 20 plus EBIT margin business only?

Santosh Varalwar: This business probably can see you in better EBIT margin because photochromic segment is something very niche, I think not much of competition across the world. I think there are one or two players in the Europe, but there is some small competition from unregulated markets but does not really go to market because we are growing in a different base altogether.

Suhani Doshi: And lastly can you give us some directional view on your Formulations business as in except for API, it has been quite a flattish growth?

Santosh Varalwar: In the Formulations business, I would split that into two segments. One is the domestic contract manufacturing segment which probably remained pretty stable and in terms of capacity utilization has been pretty high. So, the Company is of course ramping up certain capacities in certain areas to accommodate the future growth as well as the contract manufacturing is concerned. Coming back to the major bet which I think company has put is on US FDA generics but as you aware I think that is a slow process, we have been seeding at least actively working on 10 to 12 new products which will go off patent anyway from 2018 onwards and we are in different stages of filing and so far as I updated earlier, we have five approved ANDAs and we have at least three new products that have been filed and another three products will go filing before March this year. So, at the end of the year will have about 4 or 5 new filings this year and probably will meet in the same rate of filing next year also. So, the revenue ramp up will still need some time, maybe I would guess another 12 months when we start getting approvals for all the new filings. Revenues from Eastern Europe which was muted last couple of years start seeing some traction. We started getting some revenues last quarter and there is a repeat order even this quarter, but it is not very significant to talk about numbers but definitely from where it was about a year back, it is definitely very positive.

And the branded formulations as you are aware, we divested part of branded formulation, so to that extent revenue impact has already occurred in the books so you see that the revenues are no more there but the pain segment and the other management area where still a balance formulation, there it seems to be drawing pretty well. This year will probably see about 20%-25% growth there and next year, we are expecting maybe 30% growth in that area because of launch of new products. So, overall if you really asked me, I think US generics FDA business, we have invested and waiting for approvals to come in, so my guess is another waiting of 12 months is definitely there before you see some substantial revenues coming from it. But rest of the areas, we are definitely seeing lot of growth coming from all the areas.

Suhani Doshi: And just one last thing. You see the second half getting better than the first half in terms of everything taken into account?

Santosh Varalwar: If I have to make a very conservative comment, I think we will be able to maintain what we have done in the first half or may be slightly better than the first half. But of course, most of things probably will happen in the first half of next year where we would see some new activities in CMO getting into fruition and then some products where I think we had some capacities ramping up that is happening, so will see some growth coming from that.

Moderator: Thank you. We have the next question from the line of Subhankar Ojha of SKS capital. Please go ahead.

Subhankar Ojha: So few questions. You said at the end of quarter two, your net debt is Rs. 807 crores, right?

Santosh Varalwar: September 2016 was 807 crores.

Subhankar Ojha: So you received the money in the month of October so there will be another reduction of debt after the reduction?

Santosh Varalwar: Yes, you are right. There will be another reduction of debt after that.

Subhankar Ojha: So as on today, your debt will be how much, net debt?

Santosh Varalwar: Net debt I guess will be in the range of about Rs. 740-730, I guess.

Subhankar Ojha: That is one. Secondly sir for H1 what was the CAPEX number and what is your FY2017 guidance?

Saurabh S.G: See if you see capital expenditure, apart from what Mr. Santosh mentioned it which had to be done for conclusion of transaction, apart from that we have not really been spending much on CAPEX. I think most of the CAPEX which will come up is probably earmarked for the second half and typically they have been spending between 3% to 4% of sales on CAPEX, I think that number is something which will continue. So, if you ask me the second half, probably the number will be higher than the first half and for the next year, I think we will continue with in terms of fixed asset including maintenance etc., the same Rs. 50 to 60 crores.

Subhankar Ojha: And the line was bad so in terms of the Specialty Chemical business, so basically Rs. 80 crores kind of run rate per quarter if I see last two quarters, now Rs. 80-81 crores quarter one and quarter two revenue from this business, so is this the stable run rate that we can assume?

Santosh Varalwar: No, I think as I said till September ending or till October first week or second week when we did the second closing, the Bonthapally plant also was done by us and revenues were coming into our books because we are doing a transfer pricing arrangement to them. But now effective October, the asset has been transferred to Clariant so the revenues from that side would not come up, so which means I think the revenues predominantly will be the leftover business of Vivimed Specialties which is hair dye, photochromic and antimicrobial, but as I said beside that we have a long-term contract with Clariant for supply certain in products. So the revenues from that will come in. So my guess is that at least from the Rs. 80 crores that you saw should come down by Rs. 20 crores per quarter since we have divested the whole personal care business to Clariant and we are only doing a part of contract manufacturing at our Bidar site.

Subhankar Ojha: And finally sir, if you can give some idea about the performance of the foreign subsidiaries that we have?

Santosh Varalwar: If you see, we have about 4 subsidiaries overseas, one is Vivimed Labs UK, which is predominantly a specialty chemical subsidiary with a R&D centre in Huddersfield which exclusively develops products for hair dyes and photochromic. Now that particular subsidiary accounts a revenue of about Rs. 110-120 crores revenue per annum and does close to about 20% EBITDA year-on-year and it has been consistent in the last few years and as I just mentioned my previous answer, the photochromic probably will see a spike in the demand after we developed certain products in that segment which have been patented by us, they are called fast fading photochromic. So I think that probably will hit the market somewhere next year. With that hitting the market, the revenue ramp up will probably happen in the photochromic segment which is really high margin business for Vivimed, it is a very profitable margin for Vivimed.

Now the second subsidiary which is Spanish subsidiary, which is a part of Uquifa, so that is of course continuing to ramp up. In the last 3 years some €40-50 million business 3-4 years back, this year it is going to be close to €80 plus million and our budget is about 85-87 million Euros with 16%-17% EBITDA margin. So far we are definitely tracking the budget. And Mexico is another subsidiary that we have, which is again an API business. That is doing significantly better, even much better than the budget. Just to give a little bit of a flavor of that, I think probably it outperformed the budget by more than 20%-25% in the first half. I think the trend seems to be in same way going forward and with the more drug master files being filed from that side, I think in the coming years also will keep the trend of that growth equally good.

The last subsidiary which is in US is mainly a trading subsidiary which is based out of New Jersey and this is mainly buy and sell. It buys the products from subsidiaries and sells it in the US market. Our distributors are generally from the US market. So it is more of a transfer pricing arrangement rather than talk about anything numbers about it. So that is the brief about the four major subsidiaries outside India.

Moderator: Thank you. The next question is from the line of Ashok Shah from LFC Securities. Please go ahead.

Ashok Shah: First of all, while going through the Clariant sale, it was done it around Rs. 380 crores but actually it came around Rs. 325 crores, so what is the adjustment done? What was the tax paid out of it approximately Rs. 25 crores and what was the debt reduction done and again there was a second sale of Klar Sehen, the branded products, the ophthalmic section. So does that amount has been also realized and how it is going to be utilized?

Santosh Varalwar: Thank you, Mr. Ashok for being there again. So as I said Rs. 380 crores, so the deal with we are like creating a waste water treatment plant for them and some research R&D centre from them inside the plant. So we may decide not to do them and then we agreed for some kind of a deductible there. So the Rs. 325 crores is after we paid about Rs. 15 crores tax from that, so the net amount that we received after adjustments and after some hold back. There is a little bit of hold back again in terms of certain deliverables. So with all that, right now the net amount is about Rs. 325 crores and most of this money has gone to the bank besides certain things, has gone to reduce the debt at parent level as well as subsidiary level within India.

And as far as the branded formulation is concerned, the sale of branded formulation concluded in somewhere in September I guess or just prior to September and whatever September 2016 numbers are there, I think monetization is already over and then to that extent, like money has been received and adjusted towards the debt reduction.

Ashok Shah: So that Rs. 73 crores from the branded products sold, so it is shown in the other income or in which section it is shown?

Santosh Varalwar: So it is actually sold in the subsidiary. The subsidiary has received the money, so Klar is a 100% subsidiary of Vivimed. So whatever debts were there like working capital and other things after they paying it and paying certain taxes, so that money was like transfer to Vivimed as a dividend and then that will get adjusted, that were adjusted in the banks again.

Ashok Shah: So that will be in the current quarter?

Santosh Varalwar: Yes, it is already effected by September 2016.

Ashok Shah: So it is shown in the other income in the quarterly results?

Saurabh S.G.: No, it would be basically what Mr. Santosh is saying is that if you map it from FY2015 onwards, we have had 2 transactions, so there is one of course with the Clariant transaction which is there and in the first half numbers you have only the first milestone payment which is received and that was around Rs. 258 odd crores and then you have to transfer in transaction which was around Rs. 70 crores. So that was the total number which was realized on monetization and that was basically used to retire the debts. So if you see the number was close to Rs. 1,000 crores in March 2015 and today we are down to nearly 807 odd crores. So that is the difference and we would probably see lesser number also on the net debt because we have received the second tranches after the closure of the first half. So, as he mentioned probably, it will go down to another Rs. 730 crores sort of level in March 2017 balance sheet presented.

Ashok Shah: And secondly from the sale of the Klar Sehen, Rs. 73 crores were to be received. So, debt how it is going to be deployed?

Saurabh S.G: It has already been received and it has been used for the reduction of debt because the Clariant proceeds are also used for reduction of debt plus some CAPEX which required to be done for handover the plant plus the US FDF filings etc. which are undergoing, so it is a cumulative of all the three.

Ashok Shah: So CAPEX done during the first half is around Rs. 50 crores or approximately?

Saurabh S.G.: Yes as I mentioned, it is roughly around that number.

Ashok Shah: How is the liquidity position?

Saurabh S.G.: The balance sheet?

Ashok Shah: Yes, balance sheet because large amount is received by the divestment of some division specialty and this ophthalmic division brands, any plan to give dividends to shareholders?

Saurabh S.G.: No, I think if you would recollect, one of the main reasons for which the dividend policy has been changed in this earlier part of the fiscal was that we wanted to see some debt reduction happening and then to do it. So clearly since that has happened and we are also seeing a better outlook for both our businesses in the next half, I think you would expect that to return at the end of the financial year.

Ashok Shah: And the first half net profit is around Rs. 54 crores, so that could be around similar line in the next quarter, next half year?

Saurabh S.G.: No, as Mr. Santosh mentioned we would like to believe that we would at least keep to the same number, though it is difficult for me to give you any specific guidance or anything from what we are seeing in the different business lines. Second half should not be very different from first half.

Ashok Shah: So over the last 2 years, we had done some divestment in Specialty Chemical to improve the Pharma section. So when company could be in inflection point after doing some introducing some molecules in US and other markets. So it could be first half of next year or second half of next year?

Santosh Varalwar: Mr. Ashok, the Company has invested on 2 things very clearly. One, we definitely see the opportunity of CMO business in Europe and US for which lot of business has been done at R&D level as well as creating some capacities in different places and all those sites and whatever revenues today you capture, what are revenues you are seeing is only outcome of about 2 or 3 products which have been commercialized. So, there is a still a good pipeline coming out of it and we believe that one of the molecules will get approval in the next quarter by FDA. If that happens, then there will be definitely an inflection point for the company where you will see revenues ramping up and profitability also coming in. But besides this, you should appreciate that I think in the last 3 years we have been patient in terms of deploying capital for the FDF generic business in India and first of course was to buy this facility and then later on like expand the facility to meet higher standards of FDA and also ramp up capacities a bit and third one obviously is the filing of ANDAs and all. So I think it is a work in process and we firmly believe that it needs at least another 12 months before we start seeing the speed of approvals coming in and there the ramp up of revenues will happen. So the company has been investing on this 3 areas very diligently and hoping that, things will change far better than where we are.

Ashok Shah: And what was the capacity utilization at Alathur plant?

Santosh Varalwar: Alathur still continues to be in the range of about 30%-35%.

Ashok Shah: And recently the Company has expanded or changed the website, so there is a major change in many data has been removed, so does the company which going to put all the data like conference call and transcription everything?

Santosh Varalwar: We are trying to be more transparent as you can see, I think pretty transparent website, giving you an insight into every segment of our business, trying to capture as much information for investor.

Saurabh S.G.: Yes, Mr. Shah, we will make sure that it is uploaded again, should be the same as what it was earlier.

Moderator: Thank you. We have the next question from the line of Tushar Manudhane from Anand Rathi. Please go ahead.

Tushar: The Pharma segment revenue, there has been a decline on year-on-year basis for the quarter as such, though for the first half there has been a growth but for the quarter there has been a decline.

Saurabh S.G.: The Pharma businesses we have been saying, so there is element of seasonality also which is there because part of Q2 the manufacturing units which are outside India, in Spain and Mexico, they have some sort of annual shutdown which is a maintenance thing. But I think apart from that, the other reason has been that we are clearly awaiting from our USFDA plant which is key part of the capital employed in the Pharma business, for that also to pick up some utilization. So I think that has been pretty much the reason and I think if you see in terms of the local reporting currency, there has been a growth in the foreign subsidiaries but clearly the Rupee equation also becomes the factor.

Tushar: And in terms of ANDAs, so this three filed and may be another three to be filed, these would be for own or again for the contract manufacturing?

Saurabh S.G.: So these we are talking about to be our own ANDAs which were mentioning.

Tushar: So, I mean filed as well as the one which would be filed before March 17?

Saurabh S.G.: That is right, these would all be own projects because if it is something for a customer, clearly that is their property, will be doing more manufacturing sort of jobs. When we speak about ANDAs having our own approvals, we talk about the Company's IP.

Tushar: And just lastly, may be it is a repetition but the amount which is received from the sale of branded formulation, consolidated P&L just would like to understand where it is accounted or how it is accounted?

Saurabh S.G.: If I understand correctly, what you are trying to say is that I mean to clarify again is that these proceeds have been received and they have been used towards the retirement of debt and little bit of capital expenditure which was done. So they are in the balance sheet already with respect to the first half.

Moderator: Thank you. The next question is from the line of Varun Ghia from Equitree Capital. Please go ahead.

Varun Ghia: So my first question is with regards to the pledge of the shares, so we have seen increase in pledge of shares this year, so the reason for that and would you see that coming down?

Santosh Varalwar: The reason for pledge is that like we have a chunk of shares still lying with the bank, so we are trying to like repay that I think next month it will all come out. So basically the debt has reduced substantially from a peak of about Rs. 12.5 crores has come down to something like Rs. 3 crores. So I think once we pay the balance Rs. 3 crores, I think that 35,00,000-

40,00,000 shares which is there with the banking institution will come out so that you will see a substantial reduction at that point of time.

Varun Ghia: And with regards to the Mexican unit of the API, so how was the currency impacted out there, the Mexican depreciation of Peso?

Saurabh S.G.: So clearly Mexico unit in terms of sales, it caters to the US market, Europe and certain parts of Africa as well. So, it is blended sort of currency invoicing but clearly there is a good amount of Dollar sales also. So to that extent, we would have benefited from the movement in the currency but I think what is more critical to understand and appreciate is also as Mr. Santosh has told earlier is that if you see Mexico, I think couple of things are happening which is sort of likely to drive the outperformance going forward also. One is of course the fact that most of our new products filings are due to come out from there which are coming up for expiry in the next 36 months or so. So that is one factor and these are all sort of high value DMFs which we have, there we see significant amount of commercial interest. The second is also on the custom manufacturing business where we work with certain innovator companies, their couple of projects which are close to getting into scale up mode and I think once that begins to happen towards the end of this year, I think you would see probably better numbers emerging from that particular business.

Varun Ghia: So there is not much impact on that, right?

Saurabh S.G.: No, there is impact since there is certain amount of revenues which is invoiced in the US Dollar terms. So clearly if the Mexican Peso depreciates that does make a difference but then you would have to reconcile to the fact that all of it is also converted to Rupees sort of that way.

Varun Ghia: The impact would be in percentage term if you could say?

Saurabh S.G.: It would be difficult to give you a number but I think it is safe to assume that at least half of our sales from Mexico would be in Dollar terms.

Varun Ghia: And how do you see the business visibility of Uquifa?

Saurabh S.G.: So just the explanation which I gave you about Mexico business that is part of Uquifa which is the API franchise of the group. So clearly I think there are two triggers which we see for this part of the business. One is the ramp up of the CMO which we have seen successfully, when I said CMO, I mean, custom manufacturing which we work with innovative companies, so that has clearly happened in the last three years wherein we have grown that particular revenue line from nearly $2 million level to nearly $30 million which is what it is contributing today, so that has happened on the back of certain high value engagements which we had and going forward, we see more visibility in that business from couple of other customers. So that is something which should be giving significant numbers in the next 24 months and the second is the new products as and when they start to come on stream after the patent expires, those will also start to add to the business. So in short, I think the visibility is quite high in terms of the next six months and I think going forward also given our focus on the custom manufacturing business and new generics scale up, I think we would be growing faster than the industry.

Varun Ghia: And sir with regards to the PE investor evolving, so basically PE stays for around 3 to 5 years, so are there any plans for them to exit?

Santosh Varalwar: Yes, I think as we mentioned**,** they are going to finish this 5th year of investment this year so it is a necessary for us to like give them an exit and we are negotiating with them the exit terms. So my guess is that by end of this quarter, we should be able to like finalize on that and give a more visibility to shareholders.

Varun Ghia: And with regards to the contract manufacturing at the Chennai, you are going to set the Chennai assets, so has then been started off sir?

Santosh Varalwar: The contract manufacturing, of course work is going on but I think the first CB30, we will probably expect in the last quarter of this year. So I would safely assume that revenues will probably as it comes in the last quarter are more so to begin with the first quarter from this contract manufacturing opportunity.

Varun Ghia: And that would be with the clients you could name?

Santosh Varalwar: A little bit of secrecy on that like confidentiality but they are top ten companies in the world.

Varun Ghia: And just last question on the Chennai facility ANDAs, two have launched, right out of the total five?

Santosh Varalwar: Yes, now even the third one has gone. So Metronidazole is the third product which has also gone into the market and we are expecting one more product Donepezil to also go to the market by end of this quarter and then we will have one more product called Zolpidem which waiting for change of source because the present source is not good enough, so looking for change of source. So once we get that approval, I think probably in the first of same quarter of next year even this fifth product will launch.

Moderator: Thank you. The next question is from the line of Cindrella Carvallo from Dolat Capital. Please go ahead.

Cindrella Carvallo: Sir just wanted to know about your Speciality Chemical segment that on a like-on-like comparison what was the growth and the improvement in the EBITDA margin, what is driving that and can this base would be a stable base going ahead or we can see some more improvement in this? That is all from my side.

Santosh Varalwar: Specialty Chemical side, if you really see maybe 8% to 10% growth comparatively in the rest of the portion and the margins that you have seen are like the residual business which is hair dye and photochromic definitely has better gross margins compared to the divested products. So you would have seen that improved numbers in terms of EBITDA margins of Spec Chem significantly in that but my guess is that going forward we should be slightly better than this because with the launch of those 2-3 new products which I mentioned in photochromic segment which are of newly patented products, I am sure I think the margins will be significantly better, but I will wait for the orders to come and before I make an estimate about the numbers.

Moderator: Thank you. We have the next question from the line of Piyush Chadda whose is an individual Investor. Please go ahead.

Piyush Chadda: Basically, I have two questions. One is just some housekeeping stuff. We typically have an inventory of round about Rs. 500 crores or so. Is this likely to continue in the future or this is something we are looking to bring down?

Santosh Varalwar: I think most of this inventory have arose owing to the chemical business that was being divested**.** I think post October, most of that will come down because along with that some receivables, some inventories will go away to the acquiree company and in general also, I think we are of course trying to see that how we can overall improve the receivable period and also downsize on inventories. So our focus will be that in the next 3 to 6 months, you will see significant changes happening in that front.

Piyush Chadda: Second question is this is a strange item on your balance sheet which is loans and advances. This is a large item loans and advances, short term loans and advances under current assets which as of September 30th was nearly Rs. 350 crores?

Santosh Varalwar: Yes, this is because when we received the first tranche of funds, since the closing did not happen, it was a slump sale. Whatever we received it, it was not apportioned against like liability but it was kept as loans and advances. So that is why that inflated number looks, but post October after the closing, I think probably when we come out of the balance sheet, that number would downsize substantially.

Piyush Chadda: Third is against the balance sheet again, you spoke about further strengthening the balance sheet. Now your free cash flow after whatever working capital, etc. you pay would be somewhere around about Rs. 100 crores a year.

Santosh Varalwar: On a consolidated basis?

Piyush Chadda: Yes on a consolidated basis.

Santosh Varalwar: Right.

Piyush Chadda: Most of that is going back into CAPEX.

Santosh Varalwar: Substantial of it is going back, may be Rs. 50-60 crores going back to CAPEX.

Piyush Chadda: Some dividend, etc., there really is not much left to deleverage. How do you plan to deleverage this company?

Santosh Varalwar: See as I said, we have still invested in some, believing that revenue will come up in FDF generics and some CMO projects. So obviously I think next 12 to 24 months is critical for the company to see that kind of a revenue ramp up coming up and margins being created to go and deleverage it. So I think it is a little bit of wait and watch for us, but I guess we are making the right investments.

Piyush Chadda: So it is basically from some kind of a future cash pay.

Santosh Varalwar: Absolutely, because FDF generics I think if you really look at it, I think we have almost invested over Rs. 200 crores and yet waiting for like revenues and EBITDAs to come from that business. So obviously that is something which I look forward in the next 12 to 24 months. I think once those contributions come in, then we will be talking different numbers.

Moderator: Thank you. As there are no further questions, I would like to hand the conference back to the management for any closing comments.

Santosh Varalwar: Thank you, ladies and gentlemen. Thanks for bearing with us and my apologies that we had to do this earnings presentation, analyst call a little later because of the pre-occupation of the company. But as I again reiterate our stance, I think the strategy of moving more into pharmaceutical and investing into Pharma business with FDF generics or CMO, yes, I think we believe it is a right move for us and we are definitely investing all the Dollars into that and hope to see some ramp up of revenues coming from that. And Speciality Chemical business which we have retained, it is a very interesting business which we have retained and I think the company will work towards optimize the margins and work with more companies and add more verticals into that in the next near future. But as said again, I think very critical for us to improvise on capacity utilization Chennai plant, US FDA plant and also like accelerate our ANDA filings and await for the confirmations or registrations as soon as possible and we are also working towards product registrations in other geographies like North Africa, South East Asia but it is too early to predict numbers on that, but I think company is investing in intellectual capital and trying to build up global base for the company. So I am sure all these efforts will yield dividends in the near future and thank you very much for bearing with us and thank you very much for being invested in the company.

Moderator: Thank you very much. With that, we conclude this conference. Thank you for joining us ladies and gentlemen, you may now disconnect your lines.

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Note: This transcript has been edited to improve readability