



Vivimed



Vivimed Labs Limited

Conference Call to Discuss the Sale of Certain
Products in SpecChem Division

Management:

Mr. Santosh Varalwar, Managing Director and CEO

Mr. Saurabh SG, Director, Corporate Strategy

Moderator: Ladies and Gentlemen, Good Day and Welcome to the Vivimed Labs Conference Call to discuss the Sale of Certain Products in its Specialty Chemicals Division. We have with us today, Mr. Santosh Varalwar — Managing Director and CEO; and Mr. Saurabh SG — 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. I would now like to hand the conference over to Mr. Santosh Varalwar — Managing Director and CEO. Thank you and over to you sir.

Santosh Varalwar: Good Afternoon, everybody, and thanks for being on this call at such a short notice. The idea of hosting this call is to apprise you based on the news that you would have seen last evening or this morning that Vivimed has divested a part of its SpecChem business to a strategic player — Clariant India Limited, which is part of a global group Clariant AG of Switzerland. This is a very strategic decision taken by the board of Vivimed and this will also enable the Company in terms of optimizing its capital and also focusing on core segments in which it is doing business - the Specialty Chemicals and Pharmaceuticals.

So I will just give you a little background about the deal, as you are aware Vivimed supplies ingredients to different segments like Home and Personal Care segment, Photochromic, Imaging Chemicals, Anti-Microbials for Industrial segment and also Pharma segment. So this deal primarily focuses on divesting part of its business which is in the Home and Personal Care segments and we will continue to retain other segments like Photochromics, Anti-Microbials for Industrial Application and Hair Colors, etc. The deal size is about Rs. 380 crores. This tantamount to revenue of about Rs.140 plus crores and has EBITDA margin of 20%. Post this deal the Specialty Chemicals business residual 70% of it will be left which comprises other segments which will continue to enjoy the same margin, and going forward, company will focus more on niche products in their existing



segments, mainly the Photochromatics which is high end where the Company's position is definitely at a global level and we want to penetrate more into the markets like Europe, America and Japanese markets and try to bring more value add going forward.

As you are all aware that in the last 2-years Vivimed has invested substantial capital in Pharmaceuticals business. We have expanded capacities in API business in the two plants in Barcelona as well as in Mexico. We have also expanded our business beyond Generic Pharmaceuticals to CMO business with the innovator companies and we have engaged in a lot of new projects with world leaders in pharmaceutical. We have also invested in August 2013 in acquiring a US FDA formulation facility, and last 2-years we have done a good job in terms of increasing the capacity of production over there and also started filing new ANDAs and from 0 in 2013 August, today we have five product approvals, and out of them two of them have gone commercial and we expect three more products to go commercial. So the strategic direction for the company is very clear that our focus will continue to be in the regulated markets in Pharma space, whether it is API, whether it is Formulation.

I am also glad that we have started selling the formulations in Eastern European and European countries. So our plan is to penetrate as much in terms of filing more DMFs for Generic Pharmaceutical and also more ANDAs for Formulations.

In Specialty Chemicals, our focus area after divesting a part of the Personal Care business will be more towards niche chemicals focused on the same segments where we are already operating. They are more of a high value in nature and will definitely will continue to add top line and bottom line to the company.

So we are quite excited in terms of handing over this business to Clariant who are leaders in this business. I think they will take this business forward serving all our customers and they have the capability and strategy and are well penetrated across the globe and I

am sure that business will grow in their able hands. We will continue to support Clariant in terms of supply chain during the transition period and we will continue to support the company in any which way to see that the customers are taken care of and all the global customers are glued to us as we will continue to have relations with these customers beyond this because we are still engaged with them in various segments like Anti-Microbials and Hair Colors and other things. So this is the brief update.

So if you have any questions I will be glad to answer them. Thank you very much.

Moderator: Thank you very much, sir. Ladies and Gentlemen, we will now begin the question-and-answer session. We have first question from the line of Sriram Rathi from Anand Rathi. Please go ahead.

Sriram Rathi: My question is basically pertaining to the business which has been sold now to Clariant like Rs. 140 crores of revenue. So, what would be the EBITDA margin of that business?

Santosh Varalwar: The EBITDA for this business is in the range of about Rs. 32 crores, but as I said I think we will continue to have manufacturing and supply arrangement, so the impact for us will be during the current year not more than Rs. 22 crores because we will be getting Rs.10 crores as a conversion charge in the meanwhile for FY2016.

Sriram Rathi: Second question was that basically out of this Rs.380 crores that you will be getting, in the press release you mention that most of that will be used for repaying the debt. So any idea how much of the debt will be repaid and by when?

Santosh Varalwar: What we are looking at 70% of the receipts we will use for retiring the debt post-tax. So probably something in the range of about Rs. 275-280 crores debt will be reduced.

Sriram Rathi: What will be the tax that we will have to pay on this deal out of Rs. 380 crores?



Santosh Varalwar: We are expecting about something in the range of Rs. 60 to 70 crores.

Sriram Rathi: As you mention that the five products have been approved from the Alathur plant, can you name the product?

Santosh Varalwar: In the past I shared that Losartan was approved about a year back, we are already selling it and Donepezil is other product which we got approval which we are already selling it. Now Metronidazole is a recent approval which we will start selling it in a month or so, we also got approval for Amlodipine that probably will commercialize before the end of this year and then we have of course some 3rd party supply that is more on the conversion basis, so that has already started supplying.

Moderator: Thank you. The next question is from the line of Avinash Agarwal from Sundaram Mutual Fund. Please go ahead.

Sudarshan: This is Sudarshan here. What I wanted to understand this business that you had divested, if you can give a broad idea of how this business has grown in the last 2-3-years? Broadly, this business is moving to Clariant. What would be the EBITDA margins for your Chemicals business excluding the ones that you have divested?

Santosh Varalwar: As I mentioned we had a revenue of over Rs. 440 crores in Specialty Chemicals, out of that about Rs. 140-odd-crores revenue is being divested which had EBITDA of close to about Rs. 30-plus-crores, so I think we had about more than Rs. 90 crores EBITDA in the whole Spec Chem business, so 70% of the EBITDA is still retained. So this is what it is. If you really see historically this business is growing @15-20% year-on-year and we also have a pipeline of products for its future growth. I am sure that Clariant will benefit from the pipeline that we have developed. There are certain products which are going off patent in the next few years. I think that will be really very positive sight for them. So in principle, I guess, the EBITDA levels of the divested business as well as the retained business are over 20% and that will be maintained over there.

Sudarshan: With respect to the supply agreement that you have, can you just throw a bit more light on that how long would it be and what is the kind of incremental numbers that we can look at from here?

Santosh Varalwar: As I said the revenues may not have a major impact because there is a supply agreement backed by it and obviously, the money is being used for reducing the debts, so your cost of interest will come down, probably mitigate the loss of EBITDA. Presently I think this arrangement will go on for certain time, we are not sure how long it is, there is nothing inked on it, as the time goes I think we will have more clarity on that.

Sudarshan: Sir, now that we have divested a portion of this Specialty Chemicals. Do we look at further divestment of any businesses going forward or I think are we comfortable with the kind of money that we have raised through the divestment and probably the debt repayment?

Santosh Varalwar: I think there was a bit of concern last 1-year or so in terms of debt levels. So primarily we have to address that concern. So this decision was taken by board. But having now done this I guess there is no need for any further divestiture. We should focus on investing back in areas where we are strong and where we intend to grow. So my guess is that we will need no further inflows of capital in the next couple of years.

Moderator: Thank you. The next question is from the line of Kavita Thomas from First Global. Please go ahead.

Kavita Thomas: My first question is regarding the debt level. By the end of FY2015 we had a debt of around Rs. 10 billion. Now, we are talking of reducing the debt by around Rs. 270-275 crores. So, with that also, we would be left over with a debt of still around Rs. 700 crores or so and plus you say that as of now you are not looking out for any further divestments. So, how do we plan to repay off the debt going forward?

Santosh Varalwar: If you really see the split of that we have about Rs. 600-odd-crores of long term debt and the remaining is working capital debt. So obviously

this addresses the reduction of a substantial long term debt which will obviously come down almost 50%. I think we will be left with about Rs. 300 crores and odd of long term debt which has next 3-years repayment plan. And with the kind of EBITDA that we are generating I am sure our company is in a position to generate that much of surplus to repay the debt in the next 3-years. Then the rest all is all working capital which is backed by current assets which has got a good working capital cycle, I think that will continue to be there. So I think in my opinion there is no concern in terms of repayment. And then business is now growing, whatever investment the company has made in the last 3-4-years they all come to a cycle to start giving cash flows. So with that improving in the next 2-3-years I think Rs. 300 crores odd is not a challenge in terms of repayment of our long term debt. And I guess working capital that will continue to be there as long as business keeps growing.

Kavita Thomas: Secondly, considering that this deal has happened with Clariant, so Clariant is basically a company which is into dyes and those kinds of specialty chemicals. So is it fair to assume that much of the Specialty Chemicals that we have divested is primarily catering to our Home Care segment or is it a combination of Home Care and Personal Care?

Santosh Varalwar: I think you are right. What we looked at is that we wanted to retain other segments. So the deal is primarily on the Home and Personal Care though all the Specialty Chemicals catering to that segment.

Kavita Thomas: Actually, if you see in FY2015, growth was 2% where much of the growth primarily came in from the home care segment which was up 35%, even much of the margin also was from this segment. Now, with this business getting divested, what are the kinds of top line growth guidance that you would like to give us and margins going forward?

Santosh Varalwar: As I just mentioned, the EBITDA margins that we had or we have on the spin off part of business as well retain business is almost similar. Now going forward our focus will be to do more on the niche and

specialty high-end chemicals. So the focus will not be really on the top line, I think we will focus more on the bottom line.

Kavita Thomas: Actually if you see much of your Healthcare business there the EBIT margins have been around 7%. So much of your margins have been actually generated from the specialty chemicals business where the EBIT margins have been around (+20%). So with this business getting divested, will the mix remain the same or is there going to be a near-term where the EBIT margins will be a bit lower and then it probably would pick up gradually as our focus is on Niche Chemicals?

Saurabh SG: What we are saying is that the business which is going out of the Specialty Chemicals and what will remain they have same sort of margin profile and also in terms of growth what we are expecting growth will be retained with us in terms of the residual portfolio we expect growth of 15-20% year-on-year.

Kavita Thomas: This 15-20% as such will be primarily again from the healthcare space or it will be a mix because I am more concerned where last year FY2015 if I see Personal Care was down 15%, so the Home Care was primarily one of the clear growth drivers?

Saurabh SG: Whatever we are referring to is regarding the Specialty Chemicals. Healthcare business, as we spoke also, has seen better margin in the first quarter which is basically a mixture of better revenue mix, the higher productivity, and input prices went down. We believe that is sustainable. So overall we expect that the margins will be on an uptrend.

Kavita Thomas: We have now around 16% EBITDA margins at least that is likely to witness an uptrend?

Saurabh SG: Yes, there will be some phasing effect definitely because of commodity prices going up but we are confident we will keep the margin in that band which we just mentioned.

- Kavita Thomas:** More details on the supply agreement? I understand that is not going to impact because we have this continued supply agreement with Clariant for the near-term at least. So the top line impact would not be much. Is that a right assumption?
- Saurabh SG:** It is right to an extent but supply agreement is for some period of time. So eventually you should look at this revenue not being part of the recurring business.
- Moderator:** Thank you. The next question is from the line of Jindal Seth from SKS Capital & Research. Please go ahead.
- Jindal Seth:** You mentioned the tax implication from this deal will be around Rs. 60-70 crores payable that is net realization from the deal will be around Rs. 310-320 crores?
- Santosh Varalwar:** You are right.
- Jindal Seth:** What will be the gain from this transaction?
- Saurabh SG:** There is no gain from this transaction if you refer to the P&L, this is basically slump sale of certain products and that proceeds will be used to retire debts. So there is no gain which is going to come. Whatever the proceeds are net of tax and working capital adjustments, those will be primarily used to retire debts.
- Jindal Seth:** Coming back to your Pharma business, we have seen in Q1, decent improvement in margins at 8.7% on EBIT level with 5 products coming on stream, 2 already commercialized, and 3 in the pipeline. What kind of revenue profile from these products will be and how is the margin panning out in the Pharma business?
- Saurabh SG:** On the Pharma business as we are saying we have the API business and then we have contract manufacturing and the finished Formulations business in the US. We have two products which are already commercialized and we will have another two products which will be commercial by end of this calendar year and we expect that

business will start to pick up once we get our new filings and this year we are looking at around \$13-\$14 million of sales from our contract sales.

Jindal Seth: What kind of margins are coming from that business?

Saurabh SG: Let us not get into sub-segment margins but overall for the business we have been expecting that margins will be at the level which we are and that is where we should track performance in the coming quarters, and as our product mix gets better in terms of Formulations, we are becoming larger, then the margins will start to pickup in the next 6 to 9-months.

Jindal Seth: What are the kind of pipeline in investments you are looking forward in the next 2-3-years for ANDAs and Applications?

Saurabh SG: Our R&D investments roughly has been around 4% of sales and that is the number which will begin to go up and we have a new product filing plan, so obviously we are looking to file a good number of ANDAs and DMFs.

Moderator: Thank you. The next question is from the line of Kunal Sabnis from VEC Investments. Please go ahead.

Kunal Sabnis: I wanted to know by when will this deal be closed and when do you expect the money to come in? And also will this be a one-shot payment or it will come in parts?

Santosh Varalwar: This is of course as we said we are waiting for the regulatory approvals primarily it is shareholder approvals which we are awaiting and couple of more regulatory clearances and in our opinion it should all come in next 4 to 6-weeks. So once we have it then we have the first tranche, that is 70% of the amount of the deal will be paid in the first tranche and then of course we will be doing the technology transfers and all those things. So once everything is done the second tranche will come may be 3-months later that.

Kunal Sabnis: Is it safe to assume that this initial 70% when it comes in, the debt will be repaid at that time or it will happen in parts as well?

Santosh Varalwar: The primary focus will be even from the first tranche substantial amount will go for debt reduction.

Kunal Sabnis: Are any facilities being transferred as well?

Santosh Varalwar: Because the whole transaction is a thing where they will get all the products as well as one facility along with it, we have two facilities for Specialty Chemicals — one in Hyderabad and one in Bidar, Karnataka, so the deal is along with the facility in Hyderabad. It is a part of the deal. So when the second closing happens, even that will go away. Hyderabad will go.

Kunal Sabnis: So you will transfer technology from Hyderabad to Karnataka facility and then you will sell?

Santosh Varalwar: Yes because right now what happens the products that are there in both the places, so the way it is structured is that in the first phase once the first tranche comes in then we will continue to transfer those products which are part of our retention plan to go back to Karnataka and whatever are their from there it will come back to Hyderabad then we will hand over the facility.

Kunal Sabnis: Is it possible to accommodate these products as well as grow just based on Karnataka facility or you will have to invest in other facility for Spec Chem?

Santosh Varalwar: Yes, that is a good question. Actually we have done investments in Karnataka facility last year. So by this rejig what is happening is that a lot of products that are there in Karnataka will come to Hyderabad and vice versa. So in the near term I do not think there is a need for any capital expenditure over there... when I say near-term at least next 1-year, 18-months we do not need because we have just created enough capacities over there in the last 12-to-18-months. And just to give you a flavor of the facility that is there in Karnataka, it is a pretty

big facility, it is bigger than the one in Hyderabad and has got a capacity of over 600 KL capacity and it is one of the oldest facilities of Vivimed.

Kunal Sabnis: So the remaining amount of the deal after when debt gets paid, primarily be used for I think Pharma growth in terms of filings as well as maybe capital expenditure, is that a fair assumption?

Santosh Varalwar: If you really see the capital expenditure also has been done post our acquisition whether it is in Spain or in Chennai, so now the focus will be more on IP building and filing ANDAs and DMFs. As you are aware today, I think each ANDA filing there is a cost for that, each DMS filing there is a cost for that. So after retiring the debt as we said, most of the money will go only for investing on IP rather than on any hard assets.

Kunal Sabnis: So savings about Rs. 270-280 crores of debt should be about Rs. 35-37 crores?

Santosh Varalwar: There are two portions of loan here — one is a dollar debt and also a INR debt. So we target to reduce the INR debt which will bring savings of almost 14%, 15%. So we should see about Rs. 40 crores reduction in the debt.

Kunal Sabnis: So that should be EPS-accretive even if the entire revenue goes out but just one clarity that I need on the supply agreement, what is this pertaining to and if you are selling the facility as well as the products you will still have to manufacture the same products for Clariant?

Santosh Varalwar: It is like this; now that there is a transition period for technologies to move from here to there and all these things. During this period the customers will continue get the support and we will continue to manufacture in the same facility and supply them. So once the whole thing is done when you hand over the asset to them, then you do not have manufacturing and things like that. Then there could be some residual part of it. We think we have an understanding that there are a few products even after that which will continue to come from Bidar.

So that is the only residual portion left. Otherwise most of the business will get transferred along with everything.

Moderator: Thank you. The next question is from the line of Jindal Seth from SKS Capital & Research. Please go ahead.

Jindal Seth: You mention Rs. 40 crores interest cost saving just a bit before. Is it correct?

Santosh Varalwar: Yes, you are right.

Jindal Seth: So that will be substantial saving you are paying annual interest cost of around Rs. 78-79 crores, out of it Rs. 40 crores saving will come?

Santosh Varalwar: You are right.

Jindal Seth: Your blended interest cost of debt is around 8-9% including your foreign debt as well as domestic debt. So, please throw some light how the saving of Rs. 40 crores will come.

Santosh Varalwar: The blended debt today if you really look at it you are right about 8-9%, in the new scenario the blended debt will turn down to something like 6% I guess because obviously we are targeting to repay high cost INR debt in the initial phase.

Moderator: Thank you. The next question is from the line of Jessica Mehta from HDFC Securities. Please go ahead.

Jessica Mehta: As of June 2015 shareholding pattern, the promoters still have pledge shares of about 83.4%. So, is there any update on the same like revoking of the number of shares because the price has increased so the promoters can revoke the shares?

Santosh Varalwar: As I said in the past most of the shares have been pledged to the banks because there was a multiple banking arrangement and there was no consortium arrangement done, but in the last few months we have undertaken the consortium with the bank. So once that is in place, 65 to 70% of that are with the banks they will all come out

because there are no loans of the promoters, promoters have not got anything against that the charges were not distributed to them or charges were not there, so we try to give them comfort level bank, but once the consortium is over which we expect to be over by October ending or so, then all those shares will probably get released.

Moderator: Thank you. We have a follow up question from the line of Kunal Sabnis from VEC Investments. Please go ahead.

Kunal Sabnis: Say Rs. 40-50 crores are kept aside for the future growth, right, but based on the investments required in Pharma, within a year that should be used up, is that assumption correct or that can work for longer?

Santosh Varalwar: Kunal, your assumption is right because now it is all about work of how many ANDAs we are filing, as you very well know that today one ANDA costs you anything from 300K to a million dollar depending upon the product and we will primarily use this for this kind of investment. In terms of capital expenditure I said after post acquisition of Chennai facility we have almost doubled the capacity, and even in Spain and Mexico we have added up substantial capacity in the last 2-years and more than 50% of accruals I think we have put back in the capacity creation. So I think the Rs. 40-50 crores what will have surplus will go primarily into filing ANDAs and DMFs. Since we have been doing this for the last 2-years we expect revenues to catch up next year FY2017- 18, where I think our investments will start repaying and that will be good enough to support the future business.

Kunal Sabnis: So you basically expect the cash flows to fund it next year onwards?

Santosh Varalwar: Absolutely right.

Moderator: Thank you. As there are no further questions from the participants, I would now like to hand over the floor back to Mr. Santosh Varalwar for his closing comments. Over to you, sir.

Santosh Varalwar: Thank you, Ladies and Gentlemen. So kind of you to be patiently hearing my story and thanks for everyone who have asked questions and taken interest in understanding Vivimed. As we said strategically it is a fantastic move for Vivimed. We continue to retain both the businesses and grow both the businesses at a different level. The financial flexibility that will come with this arrangement will definitely add more value to our shareholders and stakeholders. Thank you very much and stay tuned.

Moderator: Thank you very much, sir. Ladies and Gentlemen, with this we conclude today's conference call. Thank you for joining us and you may now disconnect your lines.

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Note: *This transcript has been edited to improve readability*

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