ALKEM LABORATORIES LTD.
Regd. Office : ALKEM HOUSE, Senapati Bapat Marg,
Lower Parel (West), Mumbai - 400 013, Maharashtra, India.
• Phone: +91-22-3982 9999 • Fax: 022-2495 2955
• Email: contact@alkem.com • Website: www.alkemlabs.com
• CIN: L00305MH1973PLC174201

10th August, 2022

To,

The Corporate Relationship Department **BSE Limited** Phiroze Jeejeebhoy Towers, Dalal Street, Mumbai 400 001. ***Scrip Code: 539523***	**National Stock Exchange of India Limited** Exchange Plaza, Bandra Kurla Complex, Bandra East , Mumbai 400 051. ***Scrip Symbol: ALKEM***

Dear Sirs,

Sub: Q1 FY2023 - Earnings Conference Call Transcript

We enclose herewith the transcript of the "Q1 FY2023 Earnings Conference Call" which was hosted by the Company on Friday, 05th August, 2022

The said transcript shall also be made available on the website of the Company.

Kindly take the same on record.

Sincerely,
For **Alkem Laboratories Limited**

Manish Narang
President – Legal, Company Secretary & Compliance Officer

Encl: a/a

"Alkem Laboratories Q1 FY23 Earnings Conference Call"

August 5, 2022

MANAGEMENT:	**MR. SANDEEP SINGH – MANAGING DIRECTOR, ALKEM LABORATORIES** **MR. RAJESH DUBEY - CHIEF FINANCIAL OFFICER, ALKEM LABORATORIES** **MR. AMIT GHARE - PRESIDENT, INTERNATIONAL BUSINESS, ALKEM LABORATORIES** **MR. YOGESH KAUSHAL - PRESIDENT, CHRONIC DIVISION, ALKEM LABORATORIES** **MR. AMIT KHANDELIA- AVP FINANCE, ALKEM LABORATORIES**
MODERATORS:	**MR. TUSHAR MANUDHANE – MOTILAL OSWAL FINANCIAL SERVICES LIMITED**

Moderator: Good day, ladies and gentlemen, and a very warm welcome to the Alkem Laboratories Q1 FY23 Earnings Conference Call hosted by Motilal Oswal Financial Services 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 after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone.

I now hand the conference over to Mr. Tushar Manudhane from Motilal Oswal Financial Services. Thank you and over to you, Tushar.

Tushar Manudhane: Welcome to 1Q FY23 Earnings Call of Alkem Laboratories. From the management side, we have Mr. Sandeep Singh - Managing Director; Mr. Rajesh Dubey - Chief Financial Officer; Mr. Amit Ghare - President, International Business; Mr. Yogesh Kaushal - President, Chronic Division and Amit Khandelia – AVP Finance. Over to you, Amit, for opening remarks.

Amit Khandelia: Thank you, Tushar. Good evening everyone and thank you for joining today for Alkem Laboratories Q1 FY23 Earnings Call. Earlier during the day, we have released our financial result and investor presentation and the same are also posted on our website. Hope you have had a chance to look at it. To discuss the business performance and outlook going forward, we have on this call the senior management team of Alkem.

Before I proceed with this call, I would like to remind everyone that this call is being recorded and the call transcript will be made available on our website as well. I would also like to add that today's discussion may include forward-looking statements and the same must be viewed in conjunction with the risks that our business faces. After the end of this call, if any of your queries remain unanswered, please feel free to get in touch with me. With this, I would like to hand over the call to Mr. Sandeep Singh to present the key highlights of the quarter gone by and strategy going forward. Over to you, Sandeep.

Sandeep Singh: Thank you, Amit. Good evening to all of you and thank you for joining us today for our Quarter 1 FY23 Earnings Call. I would briefly take you through the key operational and financial highlights of the quarter. Total operating revenues for the quarter declined by 5.7% year-on-year. EBITDA margin coming in at 7.9% and net profit after tax at 128 crores. We continue to maintain strong net cash position of 950 crores.

Talking about our India business, which declined 6.7% year-on-year during the quarter, this was due to huge base effect of last year. Adjusted for COVID base impact, the company has delivered reasonably good performance in domestic sales led by contribution from new product introductions and price improvements.

Our CAGR over the last three years is 13.4% for domestic business. We continued to outperform in the domestic market and as per secondary sales data by IQVIA, the Company sales remained flat year-on-year compared to a decline of 1.8% for the Indian pharma market. This outperformance is driven by a leadership position in acute therapy areas like anti-infective and gastrointestinal.

Our chronic business continues to significantly outperform the market and as we are gaining market share and rankings. Our growth rate in derma and antidiabetic during the quarter is significantly higher than the market. We have gained four ranks in antidiabetic and one rank in derma therapy.

Now coming to international business

U.S. Business reported a sequential growth of 2.7% with year-on-year decline of 7.9%. The performance in U.S. market continues to be impacted by a higher price erosion. During the quarter, we filed three ANDAs with the USFDA and received four approvals including one tentative approval. Apart from U. S., other international markets delivered a year-on-year growth of 9.6% with good all-round performance from the Australian market.

Coming to our progress in the Biosimilar segment

We have launched three products in domestic market last year, and we are seeing very interesting response on these products. We expect to add a few more products to our basket in the financial year which makes our Biosimilar franchisee very promising in the domestic market. We have also signed deals in the CDMO space with couple of international companies and few Indian players. In coming years, our Biosimilar franchises will be one of the future growth engine for Alkem.

Coming to regulatory inspection conducted by USFDA during the quarter

St. Louis facility was inspected in June 2022, and post the inspection, we received few observations. We have already replied to the USFDA with corrective and preventive plan to resolve these observations. Apart from St. Louis, our Indore facility was also inspected by FDA. This was a pre-approval inspection and we received one observation after the inspection which we have also replied.

Our Taloja Bioequivalence Center was inspected by USFDA in April and the inspection was successfully closed without any observations. All other manufacturing facilities supplying to the U. S. market have an EIR as on date.

To conclude, we have started the year with market beating performance in domestic market and we continue to outperform the market in our domestic franchisee. Our margin for the quarter was impacted by headwind from spike in material cost, higher marketing expense, and distribution expense and the price erosion in U. S. We would continue to drive operation efficiency through productivity improvements and various streams of cost optimization that we are running in the company.

Thank you very much. With this, I would like to open the floor for question-and-answer. Thank you.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question-and-answer session. The first question is from the line of Kunal Dhamesha from Macquarie Capital. Please go ahead.

Kunal Dhamesha: First one on the U.S. How many products are we planning to launch in the U.S. for FY23? And any meaningful product we would be aware of for FY23-24?

Sandeep Singh: We are expecting to launch about between eight to ten products, probably ten during the fiscal year and meaningful, you know, we don't want to take a shot right now in terms of answering that question. But there are some shared exclusivities that we have already launched and we are looking forward to a few others as well. Time will tell how successful we are in those.

Kunal Dhamesha: And second question is on the other expenses. What is driving the other expenses on sequential basis? I think it is by about 100 crore.

Sandeep Singh: See, you are asking from sequential quarter?

Kunal Dhamesha: Yes, sequential perspective.

Sandeep Singh: So, generally, our other expense is around 23 to 24% and this time it is higher and in fact, it is somewhere close to 29%. And mainly it is on account of some additional marketing expenditure. Some additional travelling expenditure because of normalization. Sales and distribution expense also it was on higher side, particularly for our export fit and then we have some FOREX loss, which also had gone in there.

Kunal Dhamesha: Can you quantify the, you know, maybe the kind of one-offs like FOREX loss and maybe higher freight expenses which might not recur for the coming quarter?

Sandeep Singh: Around 50 crore this FOREX loss all put together, conversion and all, I think that we can termed as one-off and then on expense front, somewhere around 20, 25 crores, it's a kind of additional in this quarter.

Kunal Dhamesha: And if I may just squeeze in one more, this is, you know, for the India business. In terms of return on capital, how does trade generics fare against the branded generic piece?

Sandeep Singh: So, we have decent ROC on trade generic.

Company Representative: Branded is better. Anything specific we will not answer. I mean, we can't give a number, but branded generic our scale is better in ROC versus generic.

Kunal Dhamesha: And what proportion of trade generic revenue would be like in source versus outsource, if you can share that?

Sandeep Singh: A lot of them is outsourced what we do, yes.

Kunal Dhamesha: So, majority is outsourced.

Sandeep Singh: Yes, that's true.

Moderator: Thank you. The next question is from Kunal Randeria from Edelweiss. Please go ahead.

Kunal Randeria: Sandeep, you did mention that you are investing in biosimilars and that's going to be one of the growth engines going forward. So, maybe just a couple of questions around that, you know. So, if you can share the kind of product that you're targeting, has the investments started and hitting that P&L already? And when do you expect to have, let's say, you know, portfolio of six to eight products starting to contribute meaningfully?

Sandeep Singh: So, your question is, is that expense hitting the P&L?

Kunal Randeria: Yes, Sandeep. Actually, there are two or three questions around that. So, yes, one of it was this.

Sandeep Singh: So, I think Mr. Dubey is in a better position, but yes, we have already completely expensed our R&D from the very beginning. So, it's hitting our P&L, obviously, and it's hitting it for the last many years, not for the first time. So, yes, revenues have just started as I mentioned, you know, very recently and as I mentioned in my opening commentary, we have launched three products. Now when you say meaningful, I think, meaningful is very subjective. But if your question is like when will we have six products? I think by end of the year, we will have six products in India. But you know, for it to really contribute, it's gonna take three to four years.

Kunal Randeria: So, in three to four years maybe you can expect four, five, six, five, seven percent of your top line or something coming from biosimilars?

Sandeep Singh: But let me do my math. 5, 10% would be how much?

Company Representative: 500 crores.

Sandeep Singh: Yes, maybe one or two years in there. We can't really be, till we don't launch something, regulated markets we're not sure whether it can go that high. 2026 is something I think we'll see an inflection if we manage to do things well. It's possible.

Kunal Randeria: And in this quarter, so I'll obviously, you know, your impact for the high base of last year. But you know, considering that 7% year-on-your decline in the revenues, would it be fair to assume that all your verticals decline and your branded acute, branded chronic or even the trade generics decline or did one or two really, you know, actually grow over last year?

Sandeep Singh: But chronic business clearly had a very healthy double-digit growth.

Yogesh Kaushal: No. So, it's not all verticals. Yes, our acute business was flat, but I would say that with high base, even a flat was a reasonably good performance. Generic here because of demand, there is little, you know, muted growth in generic or negative growth, but chronic sustain a growth of 20% plus. So, you know, all three verticals have different growth levels. Overall we could just manage slightly negative as we started our opening remarks.

Kunal Randeria: And if I can just squeeze in one more around trade generic, Sandeep, you know, a lot of your peers have now started to enter into this space. So, I'm just wondering, you know, if you can sort of maintain the tempo of your business going ahead, and what will give you the confidence that you can do it with, you know, with so much, with so many different entry?

Sandeep Singh: That is a good question. See, we are one of the leaders not just in terms of sales, but we are one of the pioneers. We started very early. The relationship we enjoy with the stockist fraternity is kind of unparalleled. So, you know, it's I think trade generics is also kind of a misnomer because they are brands actually. It's not sold to the doctor's prescription, but they do have a very good brand recall with a lot of customers and stockists and retailers. So, we enjoy that. So, a lot of big companies are welcome, but this is a business which is very different from what prescription business is. So, I think they'll take, they'll have their own learning curve. We have a very strong equity and I think will outperform. We are very confident about it.

Moderator: Thank you. The next question is from the line of Saion Mukherjee from Nomura. Please go ahead.

Saion Mukherjee: Sir, can you take us through the, you know, how the gross margin is shaping up? We have a low gross margin this quarter. If you can give some more color, any specific, you know, raw material that you're facing pressure? And how are the, you know, the raw material prices trending? And therefore, how should we think about gross margins going forward?

Rajesh Dubey: We can see our gross margin from 60% coming down to 57.5%. Basically, yes, you rightly mentioned also, material cost it has impacted. So, impact of material cost is around 2.5%. Obviously, expensive raw material will be purchased and is consumed in this period. So, that is one of the reason. Second, you ask how raw material prices now it is behaving. So, yes, it has started softening, but still I think it has not come back to its original position. So, it is in between kind of, but definitely, going forward, we'll start getting benefit of this raw material cost. Of course, it is going to soften going forward.

Second, as we discussed in U.S. price deflation that that is another reason and that also impacted us somewhere close to 2%. But that is off-setted by favorable mix. So, we got better business risk. So, that has become clear and that's the reason 2.5% difference we have.

Sandeep Singh: And just to add to that, he wanted some on specifics like cephalosporins have been most impacted at price rise and we are the number one company they sign as you know. So, therefore, we were kind of impacted by that. So, it continues to be one of the most impacted raw materials.

Saion Mukherjee: So, this is due to the P&G prices and how are they trending?

Sandeep Singh: They're trading very high. Historically, I think lifetime high, I think in my memory.

Saion Mukherjee: And is it possible to quantify like, you know, how much of, you know, the impact is? I'm just wondering this raw material, which is used to make these cephalosporins. How much in terms of rupees crore if you can give, you know, where we are versus where we were?

Sandeep Singh: No, we don't have it right now. But Amit will get back. He can share it with anybody who wants it.

Saion Mukherjee: Is there any guidance you can give on grass margin going forward?

Rajesh Dubey: I think we have already guided our gross margin 59% and we remain with that for a year.

Saion Mukherjee: 59% for the full year. And what about EBITDA margins that you had talked about 18% in the previous call. This quarter it has been very low and also if you can give some color on other expenses, again, if it's on a very high side, how should we think about that as well?

Sandeep Singh: So, Saion, I think we last time we spoke about yes, you're right about 18% EBITDA, but the kind of two things which are a little bit, you know, new this quarter, which we have to see how it goes. One is we have our close to 50, 48 crore to be precise of currency impact, which we were not very sure last time. So, this is out of the blue slightly and then U.S. price erosion is also slightly more than what we're anticipating. So, it looks like it we could be 100 to 150 basis point lesser than 18% what we thought we'd be doing.

Rajesh Dubey: Yes. So, other expenses, I think, I have already covered that, and in other experiences, particularly in this quarter, there are few expenditure where frequent it has happened, mainly in marketing expense. Then as I said, traveling expense is on higher side, as selling and distribution, mainly freight expenses is on higher side and FOREX loss is one-off, which Managing Director just now mentioned now somewhere close to 48 crores. So, of course, 28.9% other expenses is abnormally on higher side. Traditionally, we have other expenses in the range of 23 to 24% and by year end, we will be somewhere closer to that.

Saion Mukherjee: So, 23, 24 by the end of the year you're saying.

Rajesh Dubey: Yes.

Moderator: Thank you. The next question is from the line of Yash Tanna from iThought Portfolio Management. Please go ahead.

Yash Tanna: So, sir, I went through your annual report and I was just looking at this one-line item called sale of services in the revenue. So, that has increased from about 7 crores in FY20 to 17 crores in FY21 and it's around 58 crores in FY22. So, what is this exactly pertaining to? So, I was saying that this line-item sale of services in revenue that has gone up from 7 crores in FY20 to 58 crores in FY22.

Sandeep Singh: That is CDMO. That is contract services maybe.

Yash Tanna: So, that has scaled up pretty well and so I was just curious to know could this be like a 100, 200 crore kind of a line item going forward? Since it has scaled up pretty, it's still a very smart portion of our revenue, but scaled up pretty well.

Sandeep Singh: So, I mean, yes, we want to ramp it up, but we really don't know, I mean, whether it can be done in the next one or two years. We're kind of seeing how the business rounds up.

Moderator: Thank you. The next question is from the line of Nithya Balasubramanian from Bernstein. Please go ahead.

Nithya Balasubramanian: I just had the one question on trade generics. Is there any update at all or any more visibility you have on the trades margin cap that the government keeps talking about time and again? So, is there any update? Have you heard anything new from the government on trade margin cap? Any plans of implementing it? Any timeline? Anything you might have picked up in recent times?

Sandeep Singh: No, we have picked up everything which everyone picks up from the media. We don't know.

Nithya Balasubramanian: Does that concern you? Is that a real threat? How do you think about it?

Sandeep Singh: So, I think, see, it does not concern us too much. Of course, it would be a disruption because those rules would apply to everyone. So, nobody's going get any advantage or disadvantage and we being leaders in it will continue to grow and we will continue to grow market share. I think the new players would be specifically more impacted and so it doesn't worry too much. And anyway, we don't worry about things not in our hands. We have a large portion of prescription business. Maybe we have a rub off there as well. So, I think we are fine.

Moderator: Thank you. The next question is from the line of Neha Manpuria from Bank of America. Please go ahead.

Neha Manpuria: Sandeep, if I were to look at your cost numbers in the quarter, there's been an increase in employee cost and in your SG&A even adjusting for all the one-offs. I think, what you mentioned is because of sales and promotion. Now, you know, if I were to look at the last data that is available for Alkem, our margins have been in the 15 to 17% range, and we've been trying to sort of, you know, improve it to 18 plus for some time now. But do you think given the competitive scenario in India and the investment that the business requires, incrementally, it's getting difficult for us to improve margins? What gives you confidence, you know, in the margin guidance that we are giving for 18 plus percent next year?

Sandeep Singh: I think, this year is a anomaly. So, you know, this year, of course, will not hit that. But going forward, we will, because we understand the cost structures what we need to take care of and we are looking at the expenses very carefully. On international business side, we also have, you know, very clear understanding of where we need to cut costs, and that's going to take some time. So, next year we think we could implement it. Also please, you know, understand that chronic business continues to grow very well. Operating leverage would really kick in. We have seen the growth we have in anti-diabetes and things like that. So, ultimately, you know, the compounding, the operating leverage of chronic will help domestic business get far more profitable, because productivity is very less in chronic and now you are seeing growth in the last few months very well. So, we think we can address this in the long term for sure.

Neha Manpuria: Sandeep, just to follow up on that. You know, based on the investment that we have on our sales force currently, do you think that's enough, you know, to meet the growth that we have forecasted for the next, let's say, one or two years? Or do you see the need for additional investment, you know, in our field force? And similarly, in the sales and promotion cost, I know some amount of it is linked to the sales momentum, but do you see a need for incremental investment in the India business as we go ahead?

Sandeep Singh: No, I think this quarter still we have added 300 people compared to last year. So, I think I will not reach say the yearly saturation, but we have added 3,000 people in the last three years if I am correct. So, I think we have already kind of maxed out. We don't really want to add too many people because you also realize that if you can go grow only by just adding people, that's kind of something not to be proud of. So, I don't see to answer you very like clearly, I don't see that we need to add too many people in the next two to three years to outperform the market. We have been ahead of the curve. We have been aggressive and I think now is the time to make them productive and kind of scale the business without adding too many people. Similarly, in SG&A, I think, it will not grow in line with the sales. It will grow much lesser than sales. So, we are very confident that profit will go up.

Neha Manpuria: So, from a two-year prospective, we should see margins improve to the 20% level that we've spoken of in the past?

Sandeep Singh: See whether 20 or 19 is I think something I'll refrain from, but certainly, let's say, you with see it's like above what we guided last time of 18%. It should be more than that for sure. This year is a anomaly kind of lot of reasons.

Moderator: Thank you. The next question is from the line of Subramanian K from Alpha Invesco. Please go ahead.

Subramanian K: Sir, you have mentioned about two deals of CDMO. So, can you make us understand what which therapy segment and what are the products you are focusing?

Sandeep Singh: So, these are lot of things confidential. So, I will not disclose any geographies or the company name. So, these are for clinical trials. So, they are in early stage, you know, for clinical trial supply. They could be in the chronic space and what therapy areas and all that stuff is for it could be onco. It could be osteo.

Subramanian K: So, what kind of competition is there in that like the India space for this CDMO? So, like you might have spent a lot for this for marketing. So, how long can we expect to--?

Sandeep Singh: No, we have spent nothing on marketing. So, this is not a marketing game. It's a service industry. You don't require lot of marketing in CDMO.

Subramanian K: My other question is on this dermatology. So, sir, this quarter we had a solid double-digit growth. So, moving forward, what is the strategy to scale up the revenue in dermatology? Because I could see the ranking is kind of not as same as in the other segment. So, do you have any particular strategy in dermatology?

Sandeep Singh: Yes, we do. One is that we are consolidating our current brands. There are like anti-fungals, antihistamines. These are something which we are at a very nascent stage. So, a lot need to be done there. Plus we are also looking at, you know, strengthening our cosmetic portfolio there, particularly these creams and all, your sunscreen lotions. So, these are some very high volume and high used product. So, are too very small there. So, one is, currently, there are multiple, some of the therapies where we are reasonably, we have a good presence, and some, particularly in cosmetology, you know, we were not so big and there we are exploring. So, I think these two put together, we see a reasonably good growth in next two to three years' time. And beyond that, you know, we will look at some of the maps which are being used in dermatology which is just shortlisted. So, we will see how do we progress there. But currently, for next two to three years, we are very clear and there are lot of innovations which can be done in dermatology. We should be working on those directions as well.

Moderator: Thank you. The next question is from the line of Sumit Gupta from Motilal Oswal. Please go ahead.

Sumit Gupta: Sir, my question is on the US business. So, first question is the US sales has been stable despite price erosion. So, any specific reason to highlight on this effect? And second question is US sales growth, what is the growth in the constant currency basis?

Amit Ghare: For the first question is no, we have degrown compared to last year year-on-year. We have not grown and we are not steady. Sequentially, yes, we have grown. The price erosion has been one of the factors which negatively affected. Volume has been steady and of course, new products contributed positively, but they could not offset the loss in price essentially.

Sumit Gupta: Sir, sales growth in the constant currency basis?

Amit Ghare: So, what I reported was in dollar terms. So, in rupee terms, obviously, you have seen what results are now start.

Sumit Gupta: And sir, it's the stable part I was like looking on to the sequential number. So, that's why.

Amit Ghare: You were looking at sequential. Okay. So, sequential, constant currency basis, we are probably flat.

Sumit Gupta: And overall investment in biosimilar which is expected in FY23-24?

Sandeep Singh: 23-24, next year, it's within the 6%, right, overall.

Rajesh Dubey: Yes, overall R&D including biosimilars and small molecules is 6%.

Sumit Gupta: Sir, regarding like the overall investment in the biosimilar business. So, what kind of investment can you see that in the numbers also in the value terms?

Sandeep Singh: Specifically, we can't, I mean, I am not sure we can answer. But I can tell you, yes, biosimilar expense will be going up compared to this year. But overall, we manage in the guidance we have given of 6% R&D of revenue. We will not be spending more than that.

Moderator:. Thank you. The next question is from the line of Saion Mukherjee from Nomura. Please go ahead.

Saion Mukherjee: On the US, you, I think, have talked about possibly growth this year over last year, but with the situation now, do you still think you can deliver growth in the US this year?

Amit Ghare: Yes, Saion, we have just done one quarter. We have three more quarters. So, right now the overall guidance for the year that we had given, at least for now we are sticking to it and obviously, we are looking forward to delivering that as well.

Saion Mukherjee: Is it more dependent on, of course, on new product, right? So, will we see that momentum of growth from next quarter onwards or it will be more sort of second half?

Amit Ghare: No, it will have to be a combination of everything, Saion, to be honest. So, we are not going to deliver growth if there is a 20% price deflation as you very well will understand. So, to that extent, if we have to achieve our overall growth, it will have to come from all the three pieces, a normal sort of a price deflation, unit growth and of course, from new products.

Saion Mukherjee: And what was the level of price erosion this quarter? And how does that compare to last quarter?

Amit Ghare: This quarter was 20% in dollar terms. Last quarter I think it was around, you know, 14% if I remember. I am not very sure of the last quarter number, but this quarter it was 20%.

Saion Mukherjee: Amit, 20% is a very high number. You are talking about year-on-year 20% decline in sales?

Amit Ghare: Yes, I'm talking year-on-year 20% price decline for our portfolio.

Sandeep Singh: No, not rest of new products. We have price decline on legacy business, on existing business. Yes, we did suffer, Saion, huge price deflation this quarter.

Saion Mukherjee: And is that very product specific or is it spread about your portfolio? Because this number looks very high.

Amit Ghare: This is across portfolio obviously. This is not product specific.

Saion Mukherjee: And how do you think sequentially the pricing momentum should be in your view based on what you are seeing at this point in the market?

Amit Ghare: Right. Like I said, we were expecting that the price deflation will reduce, but sequentially, from 14 we have gone to 20, you know, over those two quarters. So, it's gone the other way round than what we had expected. Now, obviously, we will hope and expect that, you know, it doesn't go beyond this number and in fact, it starts coming to normal number.

Saion Mukherjee: And you know, a general question on margin. You were about margins sort of moving higher in due course. So, the question is that what is that dependent on in the sense that do you have leverage in your India business? Or is this going to depend more on, let's say, the U.S. business stabilizing and you know, growth coming there? And you know, if you compare the margins for the India business, let's say, pre-COVID till now, how is that comparison?

Sandeep Singh: So, Saion, increase in margin dependent on both. One is domestic leverage obviously, as we mentioned during the previous question. And you know, on international business, we have identified some cost rationalization, which could be pretty meaningful, but we are still evaluating that. So, we can't really kind of give you really guidance on that, but we understand that, you know, everybody is restructuring their portfolio. We also know what kind of, you know, portfolio we could restructure in international business and that could lead to some cost optimization in terms of some, you know, a lot go to this manufacturing plant cost optimization as well linked with that. So, we have got some levers there. Now they will take like a year to implement because, you know, to do those stuff, it's not that easy. So, we have those levers and we are fully committed to increasing margins, not just as a lip service. So, we feel very confident that if we go this year, and you take like a three-year horizon, we would be increasing our margins.

And on the second question is with the pre-COVID margin compared to now on the domestic side, I think you asked.

Sandeep Singh: So, as far as pre-COVID margin is concerned, so more or less normalization is coming. So, this quarter was exception because some of the expenditure, it is pre-COVID. So, I think, going forward, it will get normalized. That's the reason why I said our other expense, it is going to remain between 23.5 to 24%, because of major expenditure that is on marketing, it lies over there, as well as we will start getting some kind of softness in material cost also.

Saion Mukherjee: And just, Sandeep, if I can, you know, based on the comment you made about cost initiatives on the international business, so even if you are looking at 18% margin, let's say, when things stabilize, typically, the India business margins would be in mid to high 20s, right? So, which implies that the international business margins, you know, would still be very low or is obviously now very low. So, how can we think about the, you know, steady state margin for the international business?

Sandeep Singh: I think see, international with if the price erosion which you have seen is obviously like very high this quarter. So, I think it also a lot depends on how the US market kind of responds in the future. If this kind of erosion remains, then obviously the, you know, even whether it has margins will be under question. So, I will refrain from really saying that. Let's see how the US market functions. Otherwise, you know, any kind of guess on what profit margin we will have might be just a guess. This quarter was really tough. Let's see how it sustains.

Moderator: Thank you. The next question is from the line of Aditya Khemka from InCred Portfolio Managers. Please go ahead.

Aditya Khemka: Sandeep, sir, from a marketing and sales driven organization to manufacturing and now CDMO and biosimilars, the journey in the last four, five years for Alkem has been quite revolutionary in that sense. Can you talk us through, so these two businesses, which is your India business, which is more branding, selling, marketing and then the second part of your business, which is manufacturing, contract research, contract development, capital intensity being high? Which direction is Alkem tilting to? And why are we diversifying away from our core competency of marketing, branding and selling?

Sandeep Singh: So, first of all, let me start with the latter part. We are not tilting or diversifying. I mean, we are diversifying, but we are not letting go off core. I would put the question to you. Do you think we are letting go off core? Do you see us domestic sales lack? I would say, no.

Aditya Khemka: No, that's not what I meant.

Sandeep Singh: No, what I meant is we have not let go off core. Point number one. See, understand that is our kind of core and it's critical. So, that remains and progression cannot at all think of letting go off, you know, from the ball on domestic market. Now see CDMO is something which we discussed, but that's still very small, and we have not put any large CAPEX or any marketing or anything of that sort. So, that is kind of something which is getting built up, but I will not say the whole company is geared towards that. Now, Aditya, you understand obviously that the world including India is changing. Biotech and Biosimilars will be an important part. So, you will have to ultimately kind of take part in that. So, biosimilars again is very, is going to get core of what we are doing the next few years. And similarly, so, you know, you can't win those markets like biosimilar play without manufacturing of biotech. And we have not been like too aggressive on that, like we have not put hundreds, like we have just put 200 crores on the plant of biotech, and we are like measuring it. We are not going all hog and not like if I can say, we are, you know, measuring the depth of water with one leg at a time, not with both legs. So, just to reiterate, we are not letting go off our core at all, Aditya.

Aditya Khemka: No, that's not what I meant. I just wanted to understand the diversification perspective, which is well answered by you.

Sandeep Singh: Specifically, this has also growth opportunities. I mean, justification for diversification, I'm not a believer of that, but it's also a matter of growth because you see that US market is challenging with small molecules. You need to find other things like biosimilars and we are very simple company compared to a lot of other companies. Lot of other companies are doing injectables, inhalation, everything else, but we are not. We are using oral solids and now we are saying we are doing, you know, biosimilar. So, I would say one of the most focused companies, sir.

Aditya Khemka: And Sandeep, I joined the call little late. Did you talk about what kind of price increases on a weighted average basis have you taken so far? And how much of the older price inventory was sold in 1Q? And how much of the newer price inventory has been sold in 1Q?

Rajesh Dubey: As you know for scheduled product, we had opportunity to go with 10.73%. That's wholesale price index released this time. I think, in most of the cases, we have gone for it, and you rightly mentioned. Actually, impact of that, it has not come fully in this quarter, because we had some extra inventory of earlier manufactured or earlier batches. So, once it is consumed and then we are going to have, and obviously, in Quarter 2, we are going to have entire benefit of price increase. As far as non-scheduled is concerned, so wherever depending on our competitor's price and all this, it is subject to that, but wherever opportunity is there, we have taken increase there as well.

Aditya Khemka: On the raw materials side as we understand from what we are noticing in some of the commodity prices, it seems that there is a bit of cool off. You know, Brent has come down and other commodity prices also seem to be cooling off. So, how much of high price to inventory run? Do you agree with the assessment that spot raw material prices from China etc., are lower than what they were, let's say, three months back? And if that assessment is correct, how much of the older higher price inventory do we have of raw material? And when do we start seeing the reflection of the newer, relatively lower priced inventory getting consumed in the P&L?

Rajesh Dubey: You are very right. Actually, prices of API stock is started softening and as far as high-priced raw material consumption is concerned, I think more or less substantial part we have consumed and will start getting a little bit softer raw material price consumption going forward. So, if I have to quantify to certain extent, I think somewhere close to 80, 85% of expensive API is already consumed so far.

Aditya Khemka: One question for Amit. Amit, one of your largest competitors in the U.S. market spoke about product nationalization, letting go of loss-making products, and reducing the product offering to the customers because those products were just not generating profits, and you said 20% price solution on a portfolio level, whereas in the India business, we have been able to take price increases. I'm sure raw material costs for both businesses have gone up alike. So, in that context, how is the Alkem portfolio going to survive given that the companies that I'm talking about are in multiples of the size of your business in the US and yet they are facing the problem of cash flow in that geography and rationalizing portfolio? So, how do you look at the outlook of your portfolio in the U.S.? And how do you sort of differentiate yourself versus those larger players?

Amit Ghare: Differentiation, I won't be able to answer, Aditya. The generic business commodity market, of course, we have our USPs and our strategies, but at the end of the day, you know, if a competition has the same product, there's very little differentiation per se. Going back to the original question, yes, we do this exercise always. If there are products within our portfolio, which we think are not generating return or investment or margin for that matter, we certainly discontinue or look at reducing them. And in many cases, when, you know, like we just discussed, if there is a 20% price deflation, there will be some products which will start getting into the negative area, and we will let go of those businesses. So, really sometimes we get forced out of the market also. Of course, we can keep that business by making losses, but that's not our philosophy. We don't do that. We simply get out of those products. So, we do it actively and sometimes we are forced out as well.

Aditya Khemka: So, that's a fair point, I mean, if these are not making money, why do the business? So, in that context then in terms of capacity, would you need additional capacity for your small molecule business in the U.S. for the coming three years?

Amit Ghare: No. I think, some time back we had very clearly guided that we have built the capacity for the next five to seven years, and now it's very little growth happening on the volume terms. We think that five to seven year still remains the same despite two-year stance.

Aditya Khemka: One last question and I think maybe Sandeep can answer. Sir, we are seeing a lot of merger and acquisition activity. I know you get this question every Con Call. So, in terms of deploying capital, you know, you have options. You have an option of putting up a plant or capacity for Biosimilar, CDMO, US generics, and you have the other option of buying some brands. I know the pricing may not be as per what one would ideally want, but at least there is a positive ROI on that business at a certain stage. So, have you reassessed your threshold of considering a acquisition in the Indian market or would you stick with your original parameters of what you consider as value of buying Indian brands and investing in India?

Sandeep Singh: Yes, Aditya, I think we'll stick to it. So, you know, but let me kind of build on that little bit, because I know from where you're coming from. So, you mentioned domestic business, you know, international, you know, CDMO etc. But we don't have any CAPEX planned for any of them which is like significant in the next two to three years. So, there's no question of choice among the three of it. Obviously, so, you know, first thing is that. And second, see, we continue to grow our domestic business organically, which is, I think, is a good thing. We continue to outperform. So, I don't think we have changed the standard of acquiring something, but that doesn't mean that we never evaluate opportunities. We do look at them, but we kind of when we hear those valuations from bankers, we kind of stay out. So, we are still looking at few things. If it makes sense, we'll buy, but if it does not make sense, we'll never do it for vanity. We don't want to look good. We want to be good in the long term.

Aditya Khemka: I really like discipline in the organization. That has been one of your highlights and I really appreciate you sticking with it.

Moderator: Thank you. The next question is from the line of Nikhil Mathur from HDFC Mutual Fund. Please go ahead.

Nikhil Mathur: My question is on the profitability of the domestic business from a slightly longer-term horizon. I'm not looking for answers, numbers here. I very well understand that there could be some gross margin reversal in the near term because of raw material price cooling. But if I look at the OPEX below gross profit, Alkem works with enhanced field force of more than 10,000. Or if I remember correctly from previous Con Calls, 20, 25% return that the company used to indicate. With that kind of return, is it possible to increase the PCPM structurally from where the company is today? I am also aware that chronic is something that that can add to the PCPM, but at the same time, there would be some concern that's happening on the acute side. So, I'm not too confident or too sure whether the PCPM can improve from where the levels it currently are and add on top of this, the bias in this build up that needs to be done for the next three, four years, aren't we looking at some sort of a peak OPEX and sales ratio or similar OPEX and sales ratio going forward in the coming three, four years?

Yogesh Kaushal: I'll answer your first, because you have two questions actually. You ask about increasing productivity, and then you ask about the OPEX on current 10,000 field force, and then how do we address that, correct? So, number one is PCPM obviously, when we intend to grow at around 10, 11% on a productivity of around 6 lakhs, which usually we are improving our productivity on acute front. Yes, our chronic productivity is at a mid-level, so around 3.5 to 3.7 where there we take little aggressive growth around 23 to 24%. So, our acute therapy continue to outperform the market and thereby increasing the productivity, and we intend to grow chronic by at least 2 to 2.5x of market and therefore, you know, outperforming not only the market, but increasing the productivity more than what market increases. So, that is what is our objective. So, over a period of time, productivity is bound to increase if we sustain our growth levels. Because we are not increasing manpower much now. We have done almost thousand every year for last five years, as our MD also spoke just now that, you know, we don't intend to do much on expansion front except for a few this year. But it is more consolidation and building productivity. I believe, last time we answered the same that our one of the growth level would be increasing the productivity.

Nikhil Mathur: Sir, but with our field course of 10,000 and more, your top performing MRs was the price assets for many other companies. So, a) wouldn't they need to retain them which would involve that you have to raise salaries of MRs, and if you don't retain the top performing ones, the PCPM hit that you take because the new ones will take some time to ramp up. Why I'm asking this question is why is this person more relevant for Alkem in my view it's because of the MR base that you operate and versus unlike other companies that are at half or 70% of the MR base that the company is at.

Yogesh Kaushal: See, that remains challenge across industry. It is not specific to Alkem. So, retaining team will always be issue and we have our inherent, you know, that bonding with team and we have various HR initiatives. We are, you know, team bonding and retaining the team and we are certified as best place to work for last three years. So, we keep on continuing to see that, you know, our attrition level remains lower than the industry and thereby retaining people, and we are known in the industry to be one of the best paymaster in terms of incentives and we are very highly incentive driven company, and that helps us retaining people. So, one is providing the right culture and environment, and second is how do we reward them to the best of the incentive structure in the industry that to help us to retain people. But yes, nevertheless this still remains a challenge of retaining people, and we are aware about this.

Sandeep Singh: But very clearly PCPM will increase. I don't know why you doubt that. It has to. You asked someone R&D biosimilars.

Moderator: Thank you. the next question is from the line of Shrikant from Asian Market Securities. Please go ahead.

Shrikant: My question is on domestic trade generic industry. So, if you can talk about how big trade generic industry is? What has been your market share movement for the last four, five years? Because last couple of years we have been done very good business. So, if you can comment on the market share and a little bit on the futuristic how we should look at trade generic industry growth rate in India?

Sandeep Singh: So, a lot of questions there. I'll try to answer them. Question on trade generics, we cannot really say that because, you know, there is no data like you have for prescription business. But I can tell you that we are either number one or number two in trade generics. That's point number one. So, we are very close number one or maybe a number one. And you know, trade generics is really growing now. It's outperforming the market to a large extent. It's also mentioned in some of the questions we had earlier that a lot of other companies are now entering this. So, I think you have got tailwind, this industry will outperform the, you know, normal pharma industry.

Shrikant: And anything on the market share movement?

Sandeep Singh: No, market share movement I think has only increased because as I said we are close number one, if not a number one. And there is no secondary data, no validated like third party data. So, I think whatever market share tell you might be not very accurate.

Shrikant: And one small bookkeeping question is on if you can provide the actual chronic and trade generic contribution during the quarter?

Yogesh Kaushal: So, acute is 84% and chronic is 16% to the domestic business.

Sandeep Singh: The prescription business.

Yogesh Kaushal: The prescription business, yes.

Shrikant: And trade generic, any number? Trade generic?

Yogesh Kaushal: It is close to 20.

Moderator: Thank you. The next question is from the line of Vijay Karpe form Shriram Life. Please go ahead.

Vijay Karpe: I have three questions and the first one is what has to happen for the price erosion in the US to reduce? That is one. Two, what kind of ROC do you enjoy in the U.S. business versus the trade generics and branded generics?

Sandeep Singh: There's a lot of echo over there.

Vijay Karpe: So, the first question is what is to happen for the price erosion in the US to reduce? One, and the second question is, what kind of ROC do we enjoy in the U.S. business versus the trade generics and branded generals? And the final question is can you throw some light on the working capital cycle for this quarter and the inventory days as well?

Amit Ghare: Price erosion I said it was 20% for this quarter. It was actually 19% and 1% was volume reduction. Total 20%.

Vijay Karpe: No, my question was what has to happen for this price erosion to reduce?

Amit Ghare: I can't really tell you. One of the key issues that, you know, of course, customer consolidation, but that's not going to change in this quarter, and the only thing I can say is that, you know, at some point of time, there will not be so many offers or people giving so many offers coming through and therefore, that automatically will come down. Some players getting out, manufacturers, that is on our side, that is. Those kind of things will impact.

Rajesh Dubey: As far as ROC on international business is concerned, we have in single digit, but definitely, it is positive single digit, and we are in the process of improving ROC. I think third question, I don't recollect. What was your third question?

Vijay Karpe: The working capital cycle, inventory days?

Rajesh Dubey: So, working capital cycle for this quarter, it is 110 days. I'm not talking US. I'm talking on company level. So, 110 days.

Moderator: Thank you. The next question is from the line of Prashant Nair from Ambit Capital. Please go ahead.

Prashant Nair: Just a couple of clarifications because I got disconnected in between. So, on your margin guidance you know, if you just clarify both on the gross and the EBITDA margin line. Did you mention that on EBITDA margin, you expect to be north of 18% from next fiscal, but this fiscal it could be a bit short of that number? Is that what you indicated?

Sandeep Singh: Yes, absolutely.

Prashant Nair: And on the gross margin line as well, you know, if you could just give us a general sense of, you know, how margins could progress over the next two to three years, that would be useful.

Rajesh Dubey: We have given guidance of 59% on gross margin front and yes, obviously, first quarter it is not there. Going forward, we will try to improve, but I think in the immediate future, we are going to remain somewhere in 59, 60% kind of gross margin.

Prashant Nair: And just one last question. Can you quantify the expenses you are incurring on the biosimilar biologic side currently? R&D, any other expenses all put together, what would it be on the P&L?

Sandeep Singh: So, in biosimilars, you know, we don't have a huge pipeline for regulated markets and in the regulated markets we have huge city costs. We just have one product which we are doing currently for global markets. So, the costs are not very high. So, you know, R&D and OPEX would be close to 150 crores. 150 for OPEX, that is plant and everything, all other administrative cost and pure R&D would be close to 100 crores. So, it's not significant.

Prashant Nair: Cumulatively about 250 is what?

Sandeep Singh: 250, yes.

Moderator: Thank you. We have the last question in queue from the line of Kunal Dhamesha from Macquarie Capital. Please go ahead.

Kunal Dhamesha: Just couple of basic questions. One, what would be your working capital cycle for the branded India business? Just a ballpark number.

Rajesh Dubey: So, for ethical business, our working capital days is, it will be somewhere close to 55, 58 days.

Kunal Dhamesha: And would it be fair to say that the trade generic would be slightly higher than this?

Rajesh Dubey: Yes.

Kunal Dhamesha: And secondly, out of our 3400 crores gross block, can you just give me a ballpark number of what would be the, you know, gross block which is targeting the US market or you know?

Rajesh Dubey: Actually, I think readily I'm not having this figure, but generally, we never share our fixed asset utilization on respective businesses, but Amit, he will be talking to you separately and try to provide some kind of.

Kunal Dhamesha: Amit Khandelia.

Sandeep Singh: Yes, Amit Khandelia.

Moderator: Thank you. That was the last question. I now hand the conference over to the management for their closing comments.

Amit Khandelia: Thank you everyone for joining the call. If any of your questions are unanswered, you can get in touch with me. Thank you and have a great weekend.

Moderator: Thank you. Ladies and gentlemen, on behalf of Motilal Oswal Financial Services Limited, that concludes this conference call for today. Thank you for joining us and you may now disconnect your lines.