"Advanced Enzyme Technologies Limited Q2 FY-18 Results Conference Call"

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MANAGEMENT: MR. CHANDRAKANT RATHI – MANAGING DIRECTOR, ADVANCED ENZYME TECHNOLOGIES LIMITED
MR. PIYUSH RATHI – CHIEF BUSINESS OFFICER, ADVANCED ENZYME TECHNOLOGIES LIMITED
MR. BENI PRASAD RAUKA – GROUP FINANCIAL OFFICER, ADVANCED ENZYME TECHNOLOGIES LIMITED
MR. SUPREET SINGH – INVESTOR RELATIONS, ADVANCED ENZYME TECHNOLOGIES LIMITED

Moderator: Ladies and gentlemen, good day and welcome to the Advanced Enzyme Technologies Limited Q2 FY18 Results conference call. 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 this conference call, please signal an operator by pressing '*' and then '0' on your touchtone telephone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Supreet Singh – Investor Relations Executive of Advanced Enzymes. Thank you and over to you, Supreet.

Supreet Singh: Thank you. Good afternoon to all. On behalf of Advanced Enzyme Technologies Limited, I welcome all participants on the con-call of Advanced Enzyme Technologies Limited. From the management team today, we have with us Mr. Chandrakant Rathi – Managing Director; Mr. Piyush Rathi – Chief Business Officer; and Mr. Beni Prasad Rauka – Group Financial Officer.

I would now like to hand over the call to Mr. Piyush Rathi to give the opening remarks, post which we can open the floor for Q&A. Over to you, sir.

Piyush Rathi: Thank you. Good afternoon to all. For this quarter, we have had an uptick in the consolidated sales, up 9% to 986 million versus 904 million in Q2 of FY '17. The consolidated EBITDA for Q2 FY '18 stands at 414 million as against 487 million in Q2 FY '17, down 15%. Consolidated EBITDA margin for Q2 FY '18 stands at 42% as against 52% in Q2 FY '17. And the net profit is down 23% to 224 million as against 291 million in Q2 FY '17. As far as the first half is concerned, H1 FY '18 is down about 6% to 1,742 million compared to 1,847 million in H1 FY '17. The consolidated EBITDA is down 29% to 712 million as against 997 million in H1 FY '17. The EBITDA margin is about 40% in H1 FY '18 as against 52% in H1 FY '17. And the net profit is down to 387 million in the first half as against 569 million in the first half of FY '17. Overall, this company has reasonably consolidated the operations of JC Biotech, and as you can see, the revenues of that business line have been consolidated in first half. In this first half, we also had the acquisition of Evoxx Technologies, Germany and these results also include about half a quarter, that's 6 weeks of Evoxx results and other businesses are also fully incorporated. Now, we would like to open up the floor for question-and-answers.

Moderator: Thank you, everyone. We will now begin the question-and-answer session. We have first question from the line of Aditya Khemka from DSP Blackrock. Please go ahead, sir.

Aditya Khemka: Yes, just a couple of questions from my side. Firstly, this OTC product sales. So, this quarter, we did about 27.5 crores, if I'm not mistaken. And the presentation says 10% to 15% growth in dollar terms. That 10% to 15% growth in dollar terms and that is the guidance for the full year or for the remaining 2 quarters?

Piyush Rathi: That's the guidance for the full year.

Aditya Khemka: That's the guidance for the full year, okay. That's comforting. And secondly, on the margin front, so 2Q FY '18 versus 1Q FY '18, I know you guys are discouraged looking at the business on a quarterly basis, but just to gauge some sort of trends that is appearing in our financials, in 2Q, our gross margins were actually only 75% compared to 1Q FY '18 gross margins of 80%. And that is despite us having incremental OTC sales in 2Q versus 1Q. So, can you explain why we are sort of getting pressurized from the gross margin front?

Chandrakant Rathi: You need to again understand that in this last quarter, we also added Evoxx Technology which is like a new acquisition, which was the loss making company which we acquired.

Aditya Khemka: Correct. But there will be some raw material cost in Evoxx and no topline, is that the case?

Chandrakant Rathi: And then, it has hit our EBITDA and the margins in the process, because there are R&D companies, R&D acquisitions. So that part also gets evaluated plus you need to understand that JC Biotech is also integrated with the company and the expenses there are getting integrated into the company. So, these 2 acquisitions overall will take certain time to get adjusted to our way of working.

Aditya Khemka: Right. No, sir, the only worry I have is this that, for instance, if I look at your other cost items basically, the gross margin alone for the time being, your employee cost even in 1Q was up 65% YoY, year-over-year, it was up and your other expenses were up 65% in 1Q and employee cost was up 24% in 1Q. And then the same number for 2Q is 24%, 24% for both the cost items and our topline isn't really growing in conjunction with the cost growth. So, I'm just wondering as to why the costs are going so much higher versus the topline not really growing as much? So, any directional help there could be great, sir?

Piyush Rathi: So what happens, Khemkaji is that last year, we did not have JC Biotech. So, of course we have now 3 plants and the overheads pertaining to those. So, there are certain fixed costs, which are now associated with our business. Of course, the revenues have also increased. So, these fixed cost, so we say, 65% has basically increased in the fixed cost from the acquisitions. So, it's not a direct comparison as for the time being.

Aditya Khemka: So, in other words, let's say, last year our average EBITDA margin was above 47%-48% across the 4 quarters. And this year, the average seems to be more like 40%. So, if I were to sort of forecast your FY '18 margins, I should take 40% as the running run rate of EBITDA margin?

Piyush Rathi: No, if you see earlier the quarter 1 was smaller, in quarter 2, it improved to 42%, quarter 3, quarter 4 further improvement will happen. So, overall, we end up on much higher number.

Aditya Khemka: You mean higher than FY '17 or 47% EBITDA?

Piyush Rathi: No, it won't be higher than 47%. But so far in the top customers, we had about 5 million in revenues this year. And when you look at the 10%-15% annual guidance, in the next 2 quarters, the sales will cover up and you will see also an improvement in the margin because of that, by virtue of that mix also product mix and various issues.

Aditya Khemka: Just last one from my side and then I will get back in the queue. If you can just help me with your full-year guidance now on the topline in FY '18 over FY '17, so first half, as you said, there has been minus 6% growth. So full year are we looking to do like single-digit growth or how much growth do you see in FY '18 topline?

Piyush Rathi: I think last quarter, Khemka, we had given approximate guidance of 380 to 400, topline guidance, we still maintain that. We believe this is achievable going by whatever visibility we have currently.

Aditya Khemka: Right. And on the margin front, Piyush, given that we have done 40% in first half, second half should be, so what should be your full year margin picture wise?

Piyush Rathi: I think it would be in between 40% and 45%.

Moderator: Thank you very much. We have the next question from the line of Amar Mourya from Emkay. Please go ahead.

Amar Mourya: Most of my questions are answered. One last probably, what could be the contribution of JC Bio in current quarter?

Piyush Rathi: You mean in terms of topline or...?

Amar Mourya: Yes, in terms of the topline as well as in terms of the EBITDA, I believe they are in the losses, right? I'm sorry, Evoxx, I'm talking about the Evoxx contribution.

Piyush Rathi: Evoxx is a negative contribution to EBITDA to the tune of 2 crores.

Amar Mourya: And what would be the topline?

Piyush Rathi: Topline is about 3 crores?

Moderator: Thank you very much. We have the next question from the line of Anurag Tiwari who is a retail investor. Please go ahead.

Anurag Tiwari: Actually that's what because I was not clear about Evoxx earlier. And I saw the revenue, current revenue for Q1 and Q2 from geographical perspective, both are 3%. So I mean I was just trying to understand that when we say 3% from Europe, is it coming from Evoxx or how should we read it, that Q1 FY ' 17 is also 3%, Q1 FY '18 is also 3%. So does this number include from Evoxx too?

Piyush Rathi: No. The current number won't include Evoxx, but you must understand that we already have some existing business there. So both the numbers are correct. 3% both for last year Q2 as well and as well as Q2 this financial year. So, both the 3% numbers are correct.

Anurag Tiwari: So, what would be the guideline from Evoxx perspective in coming second half of FY '18?

Piyush Rathi: The guidance for the full year, do you mean for Evoxx or for...?

Anurag Tiwari: Evoxx.

Piyush Rathi: I don't think we discuss individual company number, but overall our Europe numbers would start to tend towards 8% to 10%. So, in the full financial year, we expect 8% to 10% of our revenue is coming from Europe.

Anurag Tiwari: Okay, one last question. That's good to hear. From the revenue again coming from geographical, if I compare the last Q2 FY '17 and '18, the revenue coming from India has grown, I'm saying from percentage wise, and from U.S., it has been become less. So, I mean, I'm just trying to understand this percentage and the relationship with the EBITDA percentage. Is there any relation between this percentage revenue and the EBITDA margin, or we should not read in that way?

Piyush Rathi: There is no direct correlation, but you can see that our revenues because of by virtue of JC acquisition and consolidated revenues thereof. So, India business has grown. And as far as the U.S. business is concerned, it's primarily also driven by the top-end customer. So, once we see again in the next 2 quarters, when you see the consolidated sales, you'll see that it'll probably normalize equally between India and U.S.

Anurag Tiwari: So, just to point out, because I was looking at earlier financial year, so are we going in the direction of FY '16, because when I follow the FY '16 and FY '17, quarter wise, there has been a lot of variation. But if you can perform the same way as FY '16, FY '18, we can achieve what we are targeting from revenue perspective.

Piyush Rathi: I'm not sure we understand. You mean the same variation?

Anurag Tiwari: Yes.

Chandrakant Rathi: Very difficult to predict that way honestly, but as a whole we already communicated that we expect the year to finish our above 380 crores and between 380 crores to 400 crores. And now I think since we have done some around 172 crores in the first half, so balance 210 crores will come in next 2 quarters.

Moderator: Thank you very much. We have the next question from the line of Chirag Dagli from HDFC Mutual Fund. Please go ahead.

Chirag Dagli: Sir, on a YoY basis our top client contribution remains very similar, 27 odd crores. Despite that, the gross profit, the absolute gross profit, which is simply net sales minus raw material cost, is showing a YoY decline. What am I missing here, of course, we don't know the margins in this top client versus the rest of the business, but if you can just sort of throw some light on what's happening with the rest of the business, is this something that you are worrying, just broadly if you can give some sense?

Piyush Rathi: The decline in the gross margin is not related to the top customer, so it's a product mix effect.

Chirag Dagli: And this is not something that you were worried about or...?

Piyush Rathi: No, at this point in time, we are not concerned about it.

Chirag Dagli: Is this to do with currency, sir?

Piyush Rathi: Possibly, yes.

Chandrakant Rathi: Currency is 4.1% loss right now to some extent, very small but overall, Chirag, the guidance we will be able to come with very nice numbers in the next half.

Chirag Dagli: And sir, secondly, I can see in the notes to the accounts, you've done some acquisition in Malaysia, it's a small one, but just if you can sort of throw some light on what that is? And is this related to the palm product that we have?

Piyush Rathi: Yes, it is related to palm, but also in a larger vision to establish ourselves as a pan global player. This is basically setting up of our Malaysian office and so it's basically cater to Southeast Asian market.

Chirag Dagli: So, what is it that you've sort of built, sir? I mean what is it that if you can give us some sense of what is the real asset there, are the salespeople that you've hired or is there an office, just some color would be helpful?

Piyush Rathi: So it's really not an acquisition, of course it's term technically as an acquisition, but basically setting up of more or less fresh subsidiary in Malaysia.

Chandrakant Rathi: And the people are technical support team to start because our business is totally technology, innovation driven. So we always first look at the technical people to go forward and meet the client, establish our technological issues with them. So, there's a very hard core technological people who are being hired to take our vision forward.

Chirag Dagli: Can you quantify the number of people, sir?

Piyush Rathi: Between 5 and 10.

Chirag Dagli: Between 5 and 10. And is this adequate to sort of reach out to most of the customers that you intend to tap for this new product?

Piyush Rathi: At this point in time, yes.

Chirag Dagli: So, you're done with the scale up?

Piyush Rathi: Yes.

Chirag Dagli: And that incremental OpEx is also part of the consolidated financials in the second quarter?

Piyush Rathi: That's, yes, of course.

Moderator: Thank you very much. There are no further questions at this moment in time. I can hand the floor over now to Mr. Supreet Singh.

Supreet Singh: Thank you. On behalf of Advanced Enzyme Technologies Limited, I thank Mr. Chandrakant Rathi; Mr. Piyush Rathi and Mr. Beni Prasad Rauka and all participants for joining us on the call today. Thank you, and good day.

Moderator: Thank you very much. On behalf of Advanced Enzyme Technologies Limited, that concludes this conference. Thank you for joining us, you may now disconnect your lines.