“Laurus Labs Limited Q4 FY2019 Earnings Conference Call”
May 3rd 2019

Moderator: Ladies and gentlemen, good day and welcome to Laurus Labs Q4 FY2019 Earnings Conference Call hosted by Kotak Securities 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. Chirag Talati from Kotak Securities. Thank you and over to you Sir!

Chirag Talati: Good afternoon everyone. On behalf of Kotak Securities, I thank the Laurus Management team for giving us the opportunity to host this call. From Laurus, we have with us today Dr. Dr. Satyanarayana Chava- CEO, Mr. Ravi Kumar - CFO and Monish Shah from the Investor Relations Team. I hand over the call to the management for their opening remarks. Over to you Sir!

Dr. Satyanarayana Chava: Thank you Chirag. Thanks everyone and a warm welcome to our results conference call and our business highlights for Q4 FY2019 and the full year FY2019.

Our revenues for Q4 at INR 635 Crores and INR 2,292 Crores for the full year FY2019 showing a growth of 13% on year-on-year basis for the quarter and 11% for the full year. All our major business segments have reported robust revenue growth during this period. I would like to share our formulation business updates. As you are all aware that we have entered into a strategic partnership with Global Fund under this partnership we supplied TLD for LMIC countries and through this partnership we can also continue to participate in the various In-Country tenders.

With this we have demonstrated our ability to develop, file and get approval for triple drug fixed dose combinations that is a biggest milestone for our formulation business. We continue to remain highly bullish on the business as it offers opportunities for us to forward integrate into LMIC ARV finished dosage form business ensuring high volume and stable revenues in the coming quarters. We have also filed several triple drug combinations, notable ones are TLE600, TLE400, with this we have a major fixed dose combinations, which are in the first line ARV therapy with market size well over a billion dollar.

We are expecting approvals for Dolutegravir Singles as well as Emtricitabine & Tenofovir combination in the next six months. We will be filing TEE, Tenofovir, Efavirenz, Emtricitabine, in the next few months. We are also on the verge of completing several key products for the second line ARV therapy and we expect most of the ARV filings will be done by the end of FY2020.

Moving to the US market we have commercialized Metformin during this quarter where we currently have single digit market share. As of today we have received three final approvals and two tentative approvals. Going forward we expect three more approvals and expect to launch those products during FY2020.

As you are aware we also entered into contract manufacturing agreement with a European partner for certain non-ARV finished dosage forms for which we have started commercial supplies and we have a healthy order book for FY2020. We continue to make R&D related investments in to our FDA business. We aim to file about 10 ANDAs every year. I would like to share the status of our filings as of now across the geographies, we have filed 19 ANDAs in US, 6 dossiers in Europe, 4 products in Canada, and 8 dossiers with WHO, 2 dossiers in South Africa, 2 in India as well apart from almost 90 dossiers in the rest of the world.

Of the 19 ANDAs filed in US we believe that 2 products have Para IV opportunities while 7 of them have first to file opportunities with addressable market size of well over $10 billion. Our approach remains product specific rather than market specific, so we are only talking about the filing of 19 products wherever there is a possibility we extended the market into various other geographies.

Moving into the growth pattern, despite of some decrease in ARV sales we have been able to grow our revenues significantly in Q4 FY19, this demonstrates the Company's ability to transform from one product Company to ARV Company, and from ARV Company to a multiproduct Company to a full-fledged pharmaceutical Company.

Oncology grew very significantly and synthesis did extremely well, notable thing is our finished dosage form generated significant revenues in Q4. With all the growth coming from these divisions, in Q4FY19 we did more than INR 75 Crores than our Q4 FY2018.

Going to our divisional wise commentary, in the generic API year-on-year if you look at the FY2018 versus FY2019 we grew by 4%; however, the volumes were lower in Q4 FY19 that is primarily because of inventory holding of Efavirenz in South African market was lower mainly because of hope that the market will shift towards Dolutegravir, which in fact did not happen and we expect to gain good traction in ARV sales in coming quarters.

In fact if there is a shift in DTG that will also result in higher formulation sales for us. We have prepared in either of the scenarios. So the shift happens we will get more opportunity in formulations, shift does not happen we will sell more of APIs in the African market.

Moving on to our backward integration efforts, we successfully backward integrated two ARV intermediates and the benefit of that was clearly visible in Q4FY19. However the situation in China for some case still remains challenging and prices will definitely not go down for some starting materials and intermediates we have seen some opportunities.

We also started supplying large quantities to Aspen South Africa for TLD combinations for private markets and as and when they get orders for the tenders we will start supplying to them as well. During last quarter we also got approvals for Dolutegravir, Lamivudine, DMFs where we supplied validation quantities to our partners. Lamivudine capacity is fully operational right now and we expect the FY2020 will see significant growth in Lamivudine API sales.

We are also about to finish our offering in second line ARV APIs and we expect during FY2020 we will have a full range of first line and second line ARV APIs. Unit 6 underwent FDA inspection with one procedure observation and we received EIR a long back. We are very optimistic about maintaining the ARV franchise at the current level in the coming year as well.

Going to Hep-C, Hep-C did show some growth in Q4FY19 that is mainly because of the third party API sales; however, we expect API to see franchise will remain stagnant in the coming quarters as well. The significant movement in our API businesses came from oncology sales which have showed almost 35% growth in FY2019 versus FY2018, we cannot compare one quarter growth, but was significantly higher than the year growth. Increase in sales was mainly due to expanded capacities and also increased volume from existing products. We also expect to sell two new oncology APIs during FY2020. We remain very optimistic on the order book for oncology APIs in FY2020 and beyond.

In other API segment we did very well in Q4, INR 65 Crores and which was almost 40% growth compared to Q4 FY2018 this was mainly because of offtake from our existing CMO partner. The business prospects for CMO generic APIs looks very bright given the supplier related issues from China resulting in customer interest to source from sustainable companies like us. We have seen good traction in products like Metformin, Pantoprazole, Atorvastatin, Valsartan, Rosuvastatin etc other than our key segment of ARV, oncology, Hep-C, we see significant growth coming from Other API products.

Going to our Synthesis business, which was the business where we saw continued growth and we grew 65% when compared to FY2018 versus FY2019 that was the biggest growth we saw in the last four years. The growth was led by performance from our CDMO business rather than the business coming from Aspen. Although we started supplying commercial quantities of steroidal and hormone intermediates to ASPEN from Unit 5 that became commercially operational. We are very optimistic about our CDMO business because of the traction of audits by our customers and also increased RFQs from existing as well as new customers.

Going to our ingredients division, this division remained very muted, we have the similar revenues like FY2018, but the growth in this division looks very good in FY2020 because we started manufacturing some new ingredients for the existing clients. So the division sales look very interesting in FY2020. In Unit 4 we also expanded our capacities through the natural extracts that will give some additional flexibility to offer new products to our existing customers.

With that I will hand it over to Ravi to share some financial highlights.

V.V. Ravikumar: Thank you Dr. Satya and very warm welcome to everyone on the call. Our Total income has grown by 13% for the quarter and 11% for the full year. Our EBITDA margin has improved by more than 1% on a sequential basis. Our margin improved mainly because of the product mix, because of the higher Synthesis and Oncology businesses and then utilization of capacities that is in the Q4 and the completion of the backward integration of the key ARV intermediates. However, the raw material prices are still high, as Dr. Satya said from China it has remained high

but it is not alarming, but it is not in a decreasing trend either. Our diluted EPS for the quarter was at INR 4.1 and for the year INR 8.8. The board has recommended a final dividend of INR1.5 per share and also the payout ratio of around 20%.

On the capex front we have invested around INR 250 Crores in FY2019, going forward we have an normalized capex plan of around INR 150 to 200 Crores including the maintenance capex and here one more point we need to keep in mind is that we are not planning to do any greenfield expansion, but only on the brownfield expansion. We also have improved contribution from our high margin businesses that is Synthesis and FDF in the quarter and as Dr. Satya explained the FDF business is looking very bright and we are expecting to receive in bigger orders.. So we are very optimistic on our improvement of our return ratios in FY2020 and looking forward to a positive free cash flow in FY2021 and beyond. With this I would request the moderator to open the lines for Q&A. Thank you.

Moderator: Thank you very much Sir. Ladies and gentlemen, we will now begin the question and answer session. The first question is from the line of Amey Chalke from HDFC Securities. Please go ahead.

Amey Chalke: Thank you for taking my question and congratulations for good set of numbers. I have two questions, first is regarding the ARV API segment. So sir can you give us more colour on how this segment will behave in FY2020 with a TLD switch becoming reality and also the Lamivudine and the Dolutegravir API supply to what extent they would be able to compensate if there is any fall in Efavirenz.

Dr. Satyanarayana Chava: In the ARV API segment the TLD is picking up that is very evident, but our customer base where we are supplying Efavirenz is mainly to South African segment, the switch from Efavirenz to Dolutegravir is not as expected in South Africa so we expect Efavirenz sales will not be as low as we expected six months back that is one and second is assuming there is some shift from Efavirenz to Dolutegravir as I mentioned we will have a opportunity to grab the finished dosage form market for that and second we have expanded our capacities in PMPA that is intermediate for Tenofovir and also we have Lamivudine new block constructed, which we had very small sales in FY2019 and the capacity will become handy. So with increased sales of Lamivudine, Tenofovir intermediates and the API sales of Dolutegravir, any shortfall in Efavirenz will be definitely be offset by these API sales.

Amey Chalke: And any colour on how many clients we have been able to get for this Lamivudine supply because the validation that is you have already supplied?

Dr. Satyanarayana Chava: We have given it to 4 customers including Aspen.

Amey Chalke: And second question is related to the formulation business, that with the WHO, TLD approval and also TLE400 and TLE600 approvals, what all tenders we expect to participate in FY2020?

Dr. Satyanarayana Chava: Just a minor clarification we got approval for TLD from FDA not from WHO and second we filed TLE600, TLE400 for approval we expect in this calendar year and with those approvals we will be in a position to participate tenders floated by Global Fund, PEPFAR and any In-Country tenders as well.

Amey Chalke: No, because I believe with the FDA you have been able to participate with Global Fund, so with the WHO what all incremental tenders you get an opportunity to participate that was my question?

Dr. Satyanarayana Chava: The difference between the ability to participate in tenders based on FDA and WHO is very, very small. So WHO tenders will give flexibility not to get approved from many African countries, but with FDA approval itself we can capture maybe 95% of the LMIC market.

Amey Chalke: Okay, thank you for taking my questions Sir.

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

Sudarshan P: Thank you for taking my question. Sir my question is on the gross margins. In your initial remarks you embarked on the backward integration program, given that the prices in China still remain sticky and also the fact that we have done higher amount of formulation this quarter compared to the other components one would have assumed that the gross margin should have actually improved on a quarter-on-quarter basis or at least shown some kind of improvement, that seems to be not visible in this quarter, sir, any comments which you can?

Dr. Satyanarayana Chava: Yes, see our backward integration efforts have gone into fructification only in Q4 and also we have sold some intermediates of ARVs during the Q4 that was the one reason for our lower gross margin, but on a going basis from Q1 FY2020 onwards we expect to have very good gross margins. Ravi you want to add any comments here?

V.V. Ravikumar: And in Q3FY19 if you look at, we had a one time income from CASI Pharma which you need to consider. So the entire income from CASI pharma goes is 100% gross margin, so if you remove that actually there is an improvement in Q4FY19 when compared to Q3FY19.

Sudarshan P: Yes, sir and how much would that be, if you can quantify Sir?

V.V. Ravikumar: It is a $2 million about around INR 14 Crores.

Sudarshan P: Sure sir. And Sir my second question is on your utilization. With your finished dosage sales increasing and also earlier we were looking at a scenario where our gross block utilization was lesser primarily on account of your finished dosage being operating at a lower utilization and second as we were also spending in excess of INR 100 Crores on the finished dosage without commensurate sales and given that this quarter we are running at around INR 30 Crores run rate should we believe that number one is in terms of the finished dosage division with all the

approvals in place we should be able to at least with the INR 30 Crores run rate and additional growth coming in we should be able to at least finish this year with quarterly run rate of INR 45 to 50 Crores and second is in terms of again margins and the operating leverage picking in, we should at least be able to see 100, 150 bps margin expansion from the fourth quarter as the sales pickup. So what is your trajectory sir with this growth?

Dr. Satyanarayana Chava: We are not giving an absolute number, but as we mentioned rightly any gross margin we generate in finished dosage form we will definitely add to the EBITDA because we were already expensing every other expenses. So your guess on current approvals and expected approvals, we definitely will do much better than our Q4FY19 run rate in our finished dosage form division in FY2020.

Sudarshan P: Sir just one final thing from my side, what would be the utilization right now sir compared to what it was the previous year?

Dr. Satyanarayana Chava: You are talking about FDF or APIs?

Sudarshan P: Yes, sir in FDF.

Dr. Satyanarayana Chava: In FDF we have installed capacity of 5 billion units, currently we are at 25% of capacity utilization.

Sudarshan P: And what was this last year it would have been significantly lesser?

Dr. Satyanarayana Chava: Yes.

Sudarshan P: Thanks a lot Sir.

Moderator: Thank you. The next question is from the line of Jeevan Patwa from CandyFloss. Please go ahead.

Jeevan Patwa: Yes, my first question is as I always keep on asking every quarter. So how much is the gross block now which is idle by the end of this quarter?

Dr. Satyanarayana Chava: We could confidently say as of now every unit is running and there are some capacity utilization percentages vary, but otherwise if you say unit 1, unit 3 started generating positive cash a long back unit 5 is generating, unit 4 is yet to generate positive cash flow. We hope this year we will do that. For Unit 2 Q1FY20 onwards we will generate positive cash flow, unit 6 is already generating positive cash flow. So with Q1 FY2020 most of our units will generate positive cash and starting from Q3 FY2020 including unit 4 all units will generate positive cash.

Jeevan Patwa: And when we were just plain API player, so I am just talking sometime in the historical times, that time what was our gorses margins when we were just plain API player?

V.V. Ravikumar: Being an API player we are around 19% EBITDA Margins.

Jeevan Patwa: No, I am asking gross margin level I am saying, not EBITDA level.

Dr. Satyanarayana Chava: Gross margin also has been around 45%.

Jeevan Patwa: Around 45% right?

Dr. Satyanarayana Chava: Yes.

Jeevan Patwa: Okay because this quarter we are I think somewhere around 46.5% gross margins. So do you think with more FDF and everything coming in the next few years maybe one year or two years, our gross margin can move up to say 53%, 54%?

Dr. Satyanarayana Chava: We are not quantifying, but definitely will improve.

Jeevan Patwa: And I just missed on the initial part of the call. So what is the size of the order from the Global Fund that we have, multiyear contract that you are talking?

Dr. Satyanarayana Chava: Actually we signed a contract then we will get allocations once or twice in a year, we cannot tell you right now how many orders we have, but as we confirmed in previous call when you are not there, we have a good order book right now.

Jeevan Patwa: When we are saying the tender market size is basically $1.5 billion, so are we now qualifying for that particular size or we are qualifying for lesser than that?

Dr. Satyanarayana Chava: By end of this calendar year we will be in a position to participate well over the billion dollar worth of tenders.

Jeevan Patwa: And how many players are there right now?

Dr. Satyanarayana Chava: There are five active players and then some not so active players.

Jeevan Patwa: And some of those players we have to supply APIs to those players who are active?

Dr. Satyanarayana Chava: Yes, we supply APIs to integrated, semi-integrated, nonintegrated players as well. So we supply intermediates to integrate players and also some APIs to them. We supply API to most of the nonintegrated players.

Jeevan Patwa: Okay, thanks a lot Sir.

Moderator: Thank you. The next question is from the line of C Srihari from PCS Securities. Please go ahead.

C Srihari: Thanks for the opportunity and congratulations on the good set of results except ARV. My first question is once again on the gross margin front, levers of Q3 even if you consider let us say the

previous quarters despite a significant shift on ARV sales the gross margin is continuing to hold it is not improved. So any particular reason there and secondly at present we said we have three TADs on the FDF side, so any meaningful approvals out there and finally your payables have shot up significantly can you please throw some light there? Thank you.

Dr. Satyanarayana Chava: Well the first two I will answer and the last one I will ask Ravi to take. Going back to your first question on gross margins in ARV front we had some stress on gross margins during Q1, Q2, Q3 because of price increase of key starting intermediates that was taken care in Q4 that was the reason gross margin improved and we expect to maintain that for ARVs if not increased the gross margin. And going back to your second question on what are the significant approvals we are expecting? We got approvals for Hydroxychloroquine, we got approvals for Metformin, we got approval Tenofovir, we got tentative approvals for Pregabalin and Abacavir, Dolutegravir, Lamivudine, we expect two more tentative approvals and maybe three final approvals. We are in a good shape, as we mentioned our approach is product specific rather than market specific, some of these ARV combination products where we got tentative approvals, maybe we can start selling in the emerging markets as part of this LMIC tender processing.

C Srihari: Okay.

V.V. Ravikumar: I think the payable increase is because of the additional purchases we have done in the Q4 that is the reason the payables are higher.

C Srihari: So this is likely to translate into sales in the near future?

V.V. Ravikumar: Yes, correct you are right.

C Srihari: Coming back to the gross margin figure, actually considering that the base was very low, the increment should have been significantly higher that has not happened. So is there any pressure in some segments other than ARV?

V.V. Ravikumar: Other than ARV if you look at the Hep-C though there is an additional sale in Hep-C most of the Hep-C sale is to the third party API. Which is lower gross margin business, as compared to profit sharing business with Natco.

C Srihari: So it would be, I think it would be correct to say that Hep-C is one of the reasons why the blended margin has not improved?

V.V. Ravikumar: Yes you are right.

C Srihari: Coming back to formulations then should we say that Pregabalin should be one key approval for you that is in the near-term?

Dr. Satyanarayana Chava: Yes we already got tentative approval and we are expecting final approval and we will be there amongst the Companies who will launch on the day one of after the loss of exclusivity.

C Srihari: What is the competitive scenario?

Dr. Satyanarayana Chava: It is difficult to predict there are more than a dozen approvals. How many will launch? How many of them are integrated? This is still difficult to guess, but we are geared up for launch. We cannot give you the exact number, but we made formulation launch quantities and we are in the process of shipping some more quantities to US.

C Srihari: Is it a complex product in the sense that it could be a problem for some of the players to crack?

Dr. Satyanarayana Chava: It is not that way, the problem is, it more into how much of FDF capacity allocation will people do to take the market share, is more into FDF capacity rather than API complexity.

C Srihari: Okay fine, that is right. Thank you.

Moderator: Thank you. The next question is from the line of Gagan Thareja from Kotak Investments. Please go ahead.

Gagan Thareja: Sir first question basically pertains to the funding for the LMIC ARV tenders and the pricing related to the tender. Year-on-year on an average we are seeing pricing come down and at the same time I think over the last couple of years the funding for the ARV LMIC tenders has not grown if I understand it correctly. So for the coming year or the coming two, three years I think it is generally budgeted on the three year rolling if I understand it. Do you see a funding related pressure and how do you see the pricing for these combinations, formulations evolving?

Dr. Satyanarayana Chava: Going back to your first question, funding availability for the LMIC countries? We do not expect funding will be a challenge, the reason is out of $20 billion all multilateral organizers spending on these problem, roughly $2 billion is spent on purchasing of drugs and if you look at countries like India, China, Thailand, South Africa, they do not depend too much on funding from multilateral agencies. The only LMIC countries in Sub Saharan Africa they depend very heavily on these funding and that also countries like Kenya and all they are moving more to the internal funded procurement coordinated by these agencies rather than funding coming from these agencies.

Even when we look at the funding available for Global Fund and they have raised more than what they thought, so we do not expect funding will be a problem. And second question on will these markets will remain at the same level or it will continue to decline? We expect there will be a slight decline in the formulation market price, but not the API price. If you look at the API prices for the key ARVs hasn't not gone down significantly in the last 12 months. The reason is none of the new APIs launched into the market except Dolutegravir, so market for API is very much stabile and for the formulations still there is a scope to decline. With price decline integrated players will have the more ammunition to stay on the market rather than the nonintegrated players.

Gagan Thareja: Sir remaining on the same topic, if you could give us a proportion of the total LMIC ARV market, which is dependent upon funding you point out to the market size being around $1.5 billion what part of it is dependent upon PEPFAR, Global Fund and so on. If you could give us a ballpark number we are not looking for any accurate?

Dr. Satyanarayana Chava: Half of it probably, maybe it will be between 50% and 60%.

Gagan Thareja: Okay and the rest is funded through the country's sovereign?

Dr. Satyanarayana Chava: India there is little over million patients on treatment, Russia also around a million, China and the Brazil three quarters of a million, Thailand half a million patients, so these are well funded.

Gagan Thareja: Right and what is the order of the price erosion that you see on the formulations ARV LMIC formulations is it 8%, 9% or is it more than that?

Dr. Satyanarayana Chava: No I would say any price drop will be very, very gradual and we do not expect below 5% price drop.

Gagan Thareja: And is the TLD combination also priced at $75 per patient per year or is it different and is the TLE also at the same benchmark?

Dr. Satyanarayana Chava: No, the TLE there is no benchmark pricing set, the $75 was set by UN Global Fund in those days, which they gave some volume commitments, price commitments to Aurobindo and Mylan at that price. If they do not get orders beyond what they have committed they will compensate, but that number has gone, so people started supplying less than that.

Gagan Thareja: So right now the Efavirenz combination is below $75 is it.

Dr. Satyanarayana Chava: No actually Efavirenz combination is not below $75, Dolutegravir combination is below $75. Efavirenz combination is on par or better than that.

Gagan Thareja: And so coming onto the ARV API sales, so you have two things happening, one is the movement towards the Dolutegravir combination the other which you have yourself filed for is the TLE400 the shift from TLE600 to TLE400. You would have probably understood and in detail worked out on the one hand what could be the potential loss of ARV API sales for you given these two transitions and at the same time there will also be a gain because you will be supplying the Dolutegravir API you also got a new additional capacity for Lamivudine and you will also enter into the ARV formulations. So I am just trying to understand on the ARV side what is the magnitude of sales loss you incur because of these two transitions from 600 to 400 in TLE and the other transition is from TLE to TLE. That is the first part and the second part is I said is the gain that you could get from Lamivudine and the gain that you could get from going into the formulations.

Dr. Satyanarayana Chava: Going back to your question the switch from Efavirenz to Dolutegravir will not be 100%, we expect it will be evenly divided between Efavirenz and Dolutegravir and it is more likely Efavirenz 400 then Efavirenz 600 over a period of time. It will have an impact on our Efavirenz sales, but we also need to keep in mind the fittest will survive in the sense we are not considering right now that some people will be exiting the Efavirenz API business, which we foresee to happen so we will be the last one standing in the queue because of our scale, our technology better than the rest of the manufacturers, some people will exit, some people will start buying intermediate from us so the loss of Efavirenz is not going to be back significant that is one.

And second going back to our formulations we are not considering ARV formulations as a part of our API franchise. So API franchise we do not expect there will be a shortfall because in the next six months we are going to have a full basket of first and second line APIs and as we mentioned Lamivudine, where we did not have significant sales in the last financial year, we think we have good sales coming from FY2020 onwards, and we have increased our capacity on Tenofovir and its intermediates. So as an ARV franchise I think we will still very confident to maintain at the same level.

Gagan Thareja: I am just sort of trying to get a little more handle around this, so 600 transiting to 400 itself means 200 grams gets knocked off, so let us on a base of 600 third of your volume getting knocked off and you also mentioned that the current market will transition at least halfway to Dolutegravir, so would I be correct in assuming that in the first place it would translate into a 50% to 60% drop in Efavirenz related formulations or API sales directly, obviously I understand that since you are the best and the most cost competitive API supplier you might actually gain market share in a shrinking market and mitigate this loss, but to start with would it be a fair assumption that 50% to 60% theoretically speaking if you add the math there would be a dip in tonnages of Efavirenz API.

Dr. Satyanarayana Chava: You are right, definitely there is a dip in Efavirenz, but that does not mean a 50% drop in Efavirenz volumes globally means we will lose 50% of our Efavirenz sales.

Gagan Thareja: And on the formulation side, you have one approval in TLD you filed for TLE600 and TLE400. So I understand these two might get approved by the third or the fourth quarter of this year, but once you have all these three approvals in the bag, what timeframe do you sort of get to an optimal market share and what is that optimal market share that you are looking for in these formulations or what is the number you are aspiring to let us put in that way?

Dr. Satyanarayana Chava: We do not have a specific number to give you, but let us wait for 12 months for us to get the approval, to understand our ability to penetrate into the market. There are 2 million new patients are added in to the treatment last year, this year and hopefully next year I think the numbers will be same and we are not trying to dislodge anyone, we are trying to take the growth in the market as of now. Once we get approval for TLE600, TLE400 we will be in better position to get market share, we will leave it at that stage, we do not want to speculate how much market share we get right now.

Gagan Thareja: Again let me try to sort of build around it, your early API sales if I understand correctly is now at a run rate of around 300 to 325 Crores per quarter am I right there, you ended last year at around 1300 Crores?

Dr. Satyanarayana Chava: Yes, see if you look at the quarter four numbers, our ARV API sales constitutes only 50% of our sales despite we have grown. So I think ARV is significant portion of our sales, but it that is not the only one we are banking up.

Gagan Thareja: All I am trying to say is that even if Efavirenz is half of your ARV API sales that would be an annual sales of around 600 to 700 Crores theoretically, which could drop down by 50% to 60% or you could have a knock of 300 to 400 Crores there and you have an addressable market in the formulation side of $1 billion and if you mange to do a 10% market share there we are talking of $100 million, which translates to around 700 Crores. So net gain on sales could be as I see it in the magnitude of 250 to 300 Crores obviously the gross margins are higher and you have Lamivudine. So I am just trying to sort of build numbers based picture around here, if you could just validate it somewhat for me I would be very grateful?

Dr. Satyanarayana Chava: See as I mentioned we are not considering our formulation sales into our API ARV franchise. So our target is to maintain our ARV API franchise at the current level by selling more of Efavirenz, by selling more of Lamivudine, selling Dolutegravir, selling more of intermediates now for Efavirenz and Tenofovir. We do not want to compensate our ARV, API sales by selling more formulations. We are treating this as two independent business divisions.

Gagan Thareja: Got it Sir. Thanks a lot. That is helpful.

Moderator: Thank you. The next question is from the line of Jeevan Patwa from CandyFloss Advisors. Please go ahead.

Jeevan Patwa: Just one more question sir, sir this quarter the quarterly revenue has been pretty good. So is there any kind of one off this thing in this quarter or we can think of this as going to continue in the year ahead as well, so can we take a run rate of 600 plus for the next few quarters?

Dr. Satyanarayana Chava: There is no one off in the fourth quarter.

Jeevan Patwa: So there is no shipment so one time shipment or anything or you have not started anything on the Global Fund side?

Dr. Satyanarayana Chava: We did one shipment in the March, but as we mentioned earlier we have a good order book. So we do not expect to do less than our Q4FY19.

Jeevan Patwa: And secondly on the CRAMS side we have shown a very good growth of almost 60% plus so what kind of growth you expect in the next two to three years, we are right now at 225 Crores?

Dr. Satyanarayana Chava: We did INR 255 Crores in FY2019.

Jeevan Patwa: Yes, so 250 Crores so what kind of revenue you see in the next three years?

Dr. Satyanarayana Chava: We cannot predict and project four, five years down the line, but we can tell you FY2020 we expect between 30%- 40% growth in this division.

Jeevan Patwa: Thanks a lot Sir.

Moderator: Thank you. The next question is from the line of Purvi Shah from Sharekhan Limited. Please go ahead.

Purvi Shah: Yes, congratulations on the numbers. Sir my question with respect to the debt side, for the year we have seen an increase of around 55 Crores; however, the interest cost for the quarter has declined to around 17.5 Crores which usually is the run rate of around 23, 24 Crores. So if you could just explain some more on that?

V.V. Ravikumar: You are talking on the full year number or the quarter number?

Purvi Shah: Sir one part of the question is full year the number has gone up, so what is the average cost for it and the second part is just for the quarter the run rate has gone down, so what is the run rate that we should assume going forward and what was the reason for the decline?

V.V. Ravikumar: Actually if you look at on an yearly basis we have availed an additional term loan of $25 million ECB in the month of May 2018, that is the reason there is a slight increase, but if you look at decline in March versus the previous quarter its mainly because of the forex. There is no forex loss in the fourth quarter so that is the reason there is a dip from December.

Purvi Shah: Right, so if we see even in the last four quarters say from Q3 I guess Q4 of FY2018 and till Q3 of FY2019 all the quarters had around 22 to 24 Crores of interest cost, so those quarters include some forex element?

V.V. Ravikumar: Yes there is some forex element because the first three quarters there is a rupee depreciation.

Purvi Shah: So sir generally 17 to 18 Crores is the normal run rate that we can assume going forward?

V.V. Ravikumar: Yes, we look on yearly basis of around INR 85-88 Crores, but we do not have any plans to increase loans significantly.

Purvi Shah: Sir do we have any repayment schedule for the next two three years wherein we may see the debt coming down from FY2020 or FY2021?

V.V. Ravikumar: Yes in the FY2020 we have repayment of around INR 85 Crores and similar number next year onwards. So I think we have long-term debt of around INR 350 Crores in the next four years time this is going to be zero.

Purvi Shah: And Sir if you could just help us on the tax rate front what is the tax rate that we should be assuming for FY2020 and 2021?

V.V. Ravikumar: We cannot take FY2019 tax rate because of the lower profitability and weighted deduction of R&D and the other incentives made effective tax rate is a very low. And as you are aware that from FY2021 onwards there is no weighted deduction for DSR so taking that factor into consideration maybe 25% is the right number to take, it is all subject to the profit exemption from our two SEZ units.

Purvi Shah: So 25% for FY2020 is what you have?

V.V. Ravikumar: 25% - 27% should be the reasonable number you can take.

Purvi Shah: For the next two years?

V.V. Ravikumar: Yes.

Purvi Shah: Okay thank you Sir and all the best.

Moderator: Thank you. The next question is from the line of Nitin Agarwal from IDFC. Please go ahead.

Nitin Agarwal: Thank you sir. Sir we have had a pretty strong growth in the oncology business so if you can just help us understand what is happening in the oncology API business and two because of this I presume will require dedicated capacities so what kind of growth can we do with the current sort of capacities in this business?

Dr. Satyanarayana Chava: We increased our capacity to handle high potent molecules in the last 12 months that is the reason we had growth in this segment and also we started commercial supplies in the last year for two new launches in Europe and we expect two more new launches will happen this year. We expect the segment will continue to grow as we mentioned this needs a dedicated capacity and we have the largest oncology API manufacturers in the country as of now.

Nitin Agarwal: So that per se is not going to be constraint for us in terms of growing at this kind of 25%, 30% sort of growth rate that you have said, capacities will not be constraint for us?

Dr. Satyanarayana Chava: No, we have enough capacities.

Nitin Agarwal: And Sir in terms of the opportunities you have mentioned about the two new molecules that you would be commercializing but these are what, these are innovation molecules or these are older generics?

Dr. Satyanarayana Chava: These are generics.

Nitin Agarwal: And Sir secondly on this custom synthesis business, which is there, how do you see this business in terms of what kind of opportunities are you seeing in this business incrementally?

Dr. Satyanarayana Chava: In this business we are offering a wide spectrum of services in chemistry starting from intermediates to APIs to some generic APIs for combination products, so from this division we have a wide variety of offerings to start from virtual companies to mid size companies to big pharma. Out of top ten big pharma we are working with four. So that demonstrates that we are in the very good books of these companies.

Nitin Agarwal: And lastly in this business the Aspen part of the business is it now at this peak of levels or still it is not pretty scaled up yet?

Dr. Satyanarayana Chava: The Aspen business will peak out in FY20, but majority of our growth will come from non-Aspen CDMO.

Nitin Agarwal: In the current quarter that the Aspen would be closer to its peak I presume?

Dr. Satyanarayana Chava: It is equal I would say.

Nitin Agarwal: Thank you.

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

Tushar Manudhane: Sir just on this DTG API are we in a position to be like cost efficient to supply DTG API as well the way we need for Efavirenz?

Dr. Satyanarayana Chava: Since the volumes are much smaller we can very confidently say we are on par with anyone else on the Dolutegravir API.

Tushar Manudhane: But as of now we do not have any contract as such in any of the formulator?

Dr. Satyanarayana Chava: We have approval from few customers we are expanding our API offerings to many customers, the volumes are picking up.

Tushar Manudhane: Okay, and just from the asset utilization point of view as Efavirenz volume reduces the asset would be utilized for what purpose if the DTG as such volume is low, Lamivudine we have already have the asset in place separately so that asset would be utilized for what purpose?

Dr. Satyanarayana Chava: Part of that asset we have already converted into Dolutegravir and the rest of the assets we expect to utilize it for Efavirenz itself, we do not expect the sharp drop as we thought six months back.

Tushar Manudhane: Okay Sir that helps. Thanks.

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

Amey Chalke: Thanks for taking my question again. I just have followup question on Lamivudine with commercialization in FY2020 how much utilization we expect of our 500 metric tonne capacity in this year?

Dr. Satyanarayana Chava: Both the external and internal we expect it will be 50% of utilization.

Amey Chalke: And second thing on depreciation since most of our unit will get commercialized maybe in mid of FY2020 so should we consider this depreciation quarterly depreciation rate as a base for going ahead or there would be any incremental changes will happen?

Dr. Satyanarayana Chava: It is mostly yes, but there will be some two more new production blocks will be capitalized during next six months time.

Amey Chalke: And what is the asset size of those two blocks?

Dr. Satyanarayana Chava: Maybe it could be INR 125- 150 Crores. We are into a steady state right now we expect our capex will be similar to our depreciation.

Amey Chalke: So should we expect around 150 Crores kind of annual capex?

Dr. Satyanarayana Chava: Our depreciation is more than that, INR 150 to 200 Crores.

Amey Chalke: Okay. Thank you Sir. Thank you for taking my questions.

Moderator: Thank you. Ladies and gentlemen we take the last question from the line of C Srihari from PCS Securities. Please go ahead.

C Srihari: Yes, thanks for the opportunity again, three set of questions again. On the ARV front we see GSK getting approvals for two drug combinations how is that likely to impact the overall business and on the FDF side you said your capacity inflation was around 25% so if you could give some kind of an indication on that asset for FY2020 and finally you have said that you expect free cash flow to be positive only in FY2021, now with our capex being far more calibrated in FY2020 why do not you expect it to be positive in FY2020 itself? Thank you.

Dr. Satyanarayana Chava: The lag between product approval and launch in LMIC market is between two to three years and the two drug combination is not getting traction in advance markets it is only for treatment naive patients it s not for the patients who underwent treatment with some other drugs. So there is no scope of existing patients who are on treatment will move to the two drug regimen that is ruled away and we do not expect that will be a threat to the market in LMIC.

C Srihari: So it is only limited?

Dr. Satyanarayana Chava: Very limited.

C Srihari: The capacity utilization for FDF?

Dr. Satyanarayana Chava: We are not adding any new production lines for APIs we have good capacities to serve API markets ARV API market as well as supporting our finished dosage form for ARV APIs, ARV tenders in LMIC market.

C Srihari: No, I was talking about the FDF business I mean it was around 25% in FY2019 so what can be the corresponding figure for FY2020?

Dr. Satyanarayana Chava: Maybe it will probably go to 40%- 50%.

C Srihari: And finally on the free cash flow question?

V.V. Ravikumar: Yes the free cash flow we are expecting only in FY2021. There will be an additional NWC requirements in FY2020, so that is the reason we are expecting a free cash flow from FY2021 onwards.

C Srihari: I missed, free capex.

V.V. Ravikumar: The capex also there to that extent of around 200 Crores and the additional NWC also will be there net working capital.

C Srihari: Okay fine, thank you.

Moderator: Thank you. Ladies and gentlemen that was the last question. I now hand the conference over to the management for closing comments.

Dr. Satyanarayana Chava: We thank everyone for participating in this call and we are very happy that you guys are putting very interesting questions for us to write down. Thank you for your active participation.

V.V. Ravikumar: Thank you.

Moderator: Thank you very much Sir. Ladies and gentlemen, on behalf of Kotak Securities that concludes this conference. Thank you for joining us. You may now disconnect your lines.