"SeQuent Scientific Limited Q2 FY20 Earnings Conference Call"

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Moderator: Ladies and gentlemen, good day. And a welcome to SeQuent Scientific Limited Q2 FY20 Earnings 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 the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Abhishek Singhal. Thank you. And over to you, sir.

Abhishek Singhal: Thanks, Bikram. A very good afternoon and thank you for joining us today for SeQuent Scientific's Earnings Conference Call for the Second Quarter and Half Year ended Financial Year 2020.

Today we have with us Manish – SeQuent's Managing Director; and Tushar – CFO; to share the highlights of the business and financials of the quarter. I hope you have gone through our results release and the quarterly investor presentation which have been uploaded on our website, as well as the stock exchange. The transcript for this call will be available in a week's time on the company's website. Please note that today's discussion may be forward-looking in nature and must be viewed in relation to the risks pertaining to our business. After the end of this call, in case you have any further questions, please feel free to reach out to the investor relations team. I hand over the call to Manish to make the opening comments.

Manish Gupta: Thank you, Abhishek. A very good afternoon to all of you and a warm welcome as well. Thanks for joining us for the earnings call for the second quarter and half year ended 30th September. Joining me on this call is my colleague and our CFO, Tushar Mistry. I will start with a brief overview of the operating and the financial performance for the period, post which we shall open the call for any question and answer session that you may have.

We continued our steady performance in this quarter from where we had left in Q1 FY20. Revenues for the first half were Rs. 562 crores as compared to Rs. 487 crores in the first half of the previous year, exhibiting a growth of 15.5%. EBITDA in the period at Rs. 76 crores reflected a growth of 34% with a margin improvement of 190 bps for the corresponding period. On a constant currency basis, the business grew by 18% over first half, with the API continuing to outpace formulations business growth, registering a growth of 37%.

And as guided, this was on the back of increasing penetration with top 10 players in the animal health industry. Formulation, on the other hand, grew at 11% on constant currency basis in the first half, this was slightly below our expectations. This growth has been impacted on account of slowdown that we saw in Europe, and decline in India Business, even as we did well in the other geographies. Our overall growth, I believe, is reflective of the strength of our business model of having multiple growth drivers, making us less dependent or vulnerable to any short-term issues in any specific geography.

On the API side, we continue to expand margins through focus on regulated markets and high value products. Growth in the API segment continues to be driven by top 10 customers, who now constitute 58% of our API revenues. We had an additional one-time OPEX of almost Rs. 18 million during the quarter, part of which is attributable to the intense monsoon that we had, especially in Mahad.

We filed for Robenacoxib VMF, which is a NSAID with the US FDA, making us the only VMF filer for the product as of now. In the last three years, Alivira has now filed for 17 VMFs, with five sole filings for any molecule other than the innovator. Our API facilitate at Vizag also received WHO Geneva approval during the quarter, opening up new additional business opportunities for us.

Coming to Formulations, we had a robust growth across LATAM, emerging markets and Turkey. Turkey in fact grew at 63.5% in first half on constant currency basis. Interestingly, Turkey is now increasingly supporting local manufacturing in pharmaceutical industry, which will further benefit us given our strong manufacturing footprint locally.

EU performed below expectations with the decline of 2.5% in first half. This has been on account of a mix of issues ranging from continuing Brexit uncertainty, supply disruptions from a particular supplier that we have from UK, as also slowdown in Spain. However, we expect the market to be back on growth track in second half in Europe.

In Europe, we initiated our commercial operations in Italy with the launch of four oral products in September, and we expect to launch three injectable products in the current quarter. Having said that, we did incur operating losses in Italy in the current quarter and expect to breakeven by Q4.

LATAM grew mid-teens, with both Brazil and Mexico witnessing steady growth. Emerging markets grew by 9.7% in the first half on constant currency basis, with India dragging the performance in emerging markets. All of us know what is happening in India, which is really unprecedented. However, the impact is limited, given that our India Business is less than 7% of our Formulations business.

During the quarter, we also filed the world's largest animal health injectable product in EU from our facility in Germany. Globally, this molecule has an addressable market size of $300 million plus, it's amongst the top three global animal health products.

We have now expanded our R&D team to address a huge opportunity in front of us and we prepare ourselves for our first US filing soon, and subsequent commercialization in the next year. Our new state of the art facility for R&D is now functional at Ambernath in Mumbai, as we invest significant resources in developing the regulated market pipeline.

During the quarter, we also strengthened the global leadership teams with the induction of a US business head who will drive the commercialization strategy in the region, with a focus on front end, while the German injectable operations teams has a new manufacturing and project head capable of executing and operating the planned 4x increase in capacity.

Our balance sheet ratios continue to improve with a net debt to equity ratio now down to 1.79, as compared to 1.84 at the end of last year.

To conclude, we had a steady growth in the first two quarters of the current year and are confident of building on this momentum in the second half, which historically has been stronger than the first.

With those few words, I now throw open the floor for any questions and answers.

Moderator: Thank you very much, sir. Ladies and gentlemen, we will now begin the question and answer session. We have our first question from the line of Sachin Kasera from Swan Investments. Please go ahead.

Sachin Kasera: Just one question on gross margins. From June to September quarter, there is a decline of around 1.5% in the gross margins. Can you just throw some light on why it is, the reason? Because last six, eight quarter we have been seeing continuous improvement in terms of gross margin, it is mainly because of prices going up or anything else behind that?

Manish Gupta: So, largely, I think it's a business mix issue during the quarter. There is no specific kind of change that has occurred otherwise, strategically. It's more a business mix between various countries and with products in various countries. However, if you look at a H1 level, there has been a small decline of 60 basis points, and we expect the margins to kind of be in the right directions in the second half.

Sachin Kasera: So for the full year should we look at, at least for last year your gross margins were 47.8%, should we build in a 50 to 70 basis points improvement for the full year or that will be a little optimistic sitting today?

Manish Gupta: No, I think we will be able to deliver what you are specifying.

Sachin Kasera: Secondly, sir on Europe, you have been facing some challenges, but you are now managing that supply chain is more or less in place. So how should we look at Europe for the second half?

Manish Gupta: So there have been, as I said, two or three different issues in Europe. A lot had to do with one particular supplier who had some regulatory challenges. He's a big injectable manufacturer in Europe, and they had some stability issues, which has been resolved. And therefore we expect distribution of supplies from Q3 onwards from that particular supplier of our own. So that has been a significant impact as far as our European operations are concerned. There's always been a Brexit overhang as you would realize in pharma, anything that goes between UK and EU currently do not require any QP release. But post Brexit will require another level of QP release, which complicates a lot of supply chain challenge or brings in a lot of supply chain challenges of movement between the regions. So companies have been building additional inventories to tackle the same and what not.

The third one, of course, we have certain specific issues in Spain. There has been for the first time in 3.5 years since we have been running that operations, there has been a slowdown. Spain historically has been delivering double digit-growth, but there was a decline of 2.5% in the first half of the current year. We expect that to be back in growth in the second half on the back of new launches, and commercialization of the new nutritional facility that we have commissioned in Spain.

Sachin Kasera: So far constant currency basis we have seen a 2.5% decline in the European numbers. Can we look at a small growth for the full year since second half is relatively better? Or we still be looking more at a flattish number?

Manish Gupta: We are confident to deliver industry level growth rates on a full year basis.

Sachin Kasera: Industry growth is around 2% - 2.5%, if I get it right?

Manish Gupta: That's correct.

Sachin Kasera: And just one last question on Turkey, this 63% growth in the first half on a constant currency basis, very heartening. But this is like something that can be sustained and how do we see the growth momentum further building up in Turkey?

Manish Gupta: So, Turkey always has been a very interesting market for us. Previous year, FY18 was slightly subdued because of regulatory challenges. So some of this growth is reflective of normalization of situation in Turkey. Going forward, we do believe Turkey will continue to grow at 20% to 25% year-on-year business in the medium-term.

Moderator: Thank you. We have next question from line of Vishal Manchanda from Nirmal Bang. Please go ahead.

Vishal Manchanda: Sir, basically this quarter had a sharp increase in other income. Could you guide how has that increased so much?

Manish Gupta: That is because of the special dividend that was declared. So as you are aware, we do own 3.3 million shares of Strides and that other income is only attributable to the dividend income from Strides and Solara, especially the special dividend.

Vishal Manchanda: And there is a CAPEX of Rs. 20 crores in the first quarter, could you guide what this pertains to?

Manish Gupta: So this CAPEX is all inclusive across all the sites that we have, eight manufacturing sites. A significant part of this relates to the nutrition facility that we have established in Spain, and rest is the normal incremental CAPEX we keep incurring across various sites. Some of it, of course, relates to the Bremer upgradation in Germany.

Vishal Manchanda: Sir, this new facility is ready for commercialization, it has got approvals in place and it can start delivering revenue?

Manish Gupta: That's correct.

Vishal Manchanda: How big is it in terms of revenue potential?

Manish Gupta: I don't have an answer handy for you right now. Can I come back to you on this?

Vishal Manchanda: Sure. And sir on this API that you have talked about, being the first VMF filer, is this a patent expired product and you would look for partners and basically commercialize it going forward?

Manish Gupta: So see, on the API side we always have a two pronged strategy. Fundamentally, our API model is independent of our own Formulation strategy. So API development is driven by where we believe there is a market opportunity. Having said that, on such unique products which are (A) under patent; and (B) do not have easy API availability, we do look for developing our own formulation as well. So on this particular molecule, we expect to have both API revenues from a customer base and our own formulation revenues in the long-term.

Vishal Manchanda: So basically, you can look to file it as a formulation also going forward?

Manish Gupta: Yes.

Vishal Manchanda: But it will be more of an API revenue?

Manish Gupta: That's correct. I mean, both revenue streams will be independent of each other.

Vishal Manchanda: Okay. So you would wait for a partner to -- someone who would have a filing on this product can use your API source?

Manish Gupta: No, nobody would have a filing as a formulation on this, because this molecule largely is under patent. We do not foresee anybody, being the first filer is very clear that nobody else has filed it. And I don't foresee that any formulation guy would source it from a supplier who still haven't filed it. I believe we should be able to capture all new developments of this API.

Vishal Manchanda: And this injectable product that you have filed for, so can that get approved in the next 12 months?

Manish Gupta: Between 12 and 15 months is the approval timeline that we have for Europe. It's a TCP filing, so it's fairly clockwork approach that they have. So unless there are deficiencies in a filing, which we hope not, we do foresee between 12 to 15 months approval time.

Vishal Manchanda: And out of the $300 million sales, is that all in Europe or what part of that would be in Europe?

Manish Gupta: Typically, see, obviously nobody has precise information, given the lack of IMS in this industry. But typically, one-third of the global market is in Europe.

Vishal Manchanda: And you would imminently commercialize it in Europe and will file it for U.S. later?

Manish Gupta: We will certainly commercialize in Europe, filing in U.S. should occur within next three or four months. The patent expiry for U.S. is also about four to six months behind EU for the product. So we should be on time for Day 1 launch even in U.S.

Vishal Manchanda: And any sense on how many other players would have filed for this product?

Manish Gupta: Very difficult question to answer. Certainly there will be a handful of players, but I don't see many.

Moderator: Thank you. We have next question from the line of Ankit Gupta from India Nivesh. Please go ahead.

Ankit Gupta: Sir, our CAPEX has been Rs. 20 crores, as you explained, our property plant and equipment have increased by Rs. 110 crores. Is there any subsidiary which has been consolidated?

Tushar Mistry: So, it is because of the new IndAS 116 on lease assets…

Ankit Gupta: Okay. So these are Right to use assets, can you quantify how much is that?

Tushar Mistry: Lease assets were about Rs. 115 crores that have got added.

Manish Gupta: So, this includes the Vizag land and other leases.

Tushar Mistry: Major chunk is the Vizag land which is being a long leased was classified or was part of expense.

Manish Gupta: It was part of prepaid expenses earlier.

Ankit Gupta: So sir, because of this our interest and depreciation must have also gone up, right?

Tushar Mistry: So, typically what happens is, earlier it was all getting accounted as rent, it was prepaid rent which was hitting us. Now that rent goes away, in place of that it is replaced by finance cost and depreciation.

Ankit Gupta: So there is no material impact on P&L?

Tushar Mistry: No.

Moderator: Thank you. We have next question from line of Manoj Agarwal from Tulip Wealth. Please go ahead.

Manoj Agarwal: So my first question is on your cash flow. So net cash generated from operations is down. Y-o-Y, like-for-like last year September was Rs. 70 crores and this year is less than half of that. And I can see that the receivables have jumped significantly, and they are probably the biggest contributors. So can you just add some color to that, please?

Tushar Mistry: So, the previous year numbers and the current year numbers are not exactly comparable. In the previous numbers you see there is a decrease in trade receivables and other assets for almost Rs. 47 crores. This was in light of the demerger that happened. We had realized certain balances within the group, because of which these balances went down, so it was not clearly operational in nature. Coming to the current year, in the current year it is reflective of the business, in some geographies there have been better businesses which has resulted in the increase in receivables. And so is the case where, Manish explained, in some of the geographies like in EU and all, we built up the inventories, but we have also paid off the creditors to that extent, and that has impacted. So it's totally a temporary impact that you see, it's not permanent in nature.

Manoj Agarwal: Okay. So on a full year basis, last year March 2019 your cash generated from operations was way over Rs. 100 crores, I think it was close to like Rs. 120 crores. Do you expect to be somewhere in that region this year or below or above that, any ballpark?

Manish Gupta: I see no reason why we should not be in that range once the working capital cycle normalizes post this Brexit issue.

Manoj Agarwal: And the other question I had was on the US filings and getting commercial, so you haven't filed there, if I heard you correctly. So dreaming, again, it's a 12 to 15 month regulatory approval timeline and everything goes well, the earliest maybe we could reach US market, is it Q4 next fiscal or you think that there is a risk of looking into FY22?

Manish Gupta: Yes. So, see, as far as formulations are concerned, we expect our first filing in Q4 of the current year. And with the 15 month approval cycle, really the revenues will be in FY22 and at best, from March of 2021, because that's the patent expiry.

Manoj Agarwal: FY22 is more realistic?

Manish Gupta: Absolutely.

Manoj Agarwal: Okay. And finally, sir, this revenue generating CAPEX that you plan on an annual basis, I think the typical run rate is anywhere between Rs. 50 crores and Rs. 100 crores on a per year basis. What is the length of time a plant would stay operational? I mean, is it fair to assume a 15 to 20 year or because of technological disruptions it may be lower than that. Any thoughts around that please?

Manish Gupta: The pharmaceutical industry does not have much of technological obsolescence. Okay? Fundamentally, it continues to operate, you may get into more automation and whatnot, higher speed machines, but the basic technology of either on the API side or on the formulation side continues to be the same what was being done many, many years back. So I don't see any risk of obsolescence as far as assets are concerned. Just to clarify, we do not incur Rs. 100 crores CAPEX each year, in fact, it will be less than Rs. 50 crores of CAPEX. Some of the numbers that you see are the potential acquisitions and other things which get added in the cash flow side, that impacts the numbers. CAPEX otherwise is very much in control, we are fully invested already, the real CAPEX that we will incur is, (A) to scale up the Bremer facility which we expect about EUR3 million over the next 18 months, and (B) to potentially balance our increasing demand at Vizag, which can be again about US$10 million over two years.

Manoj Agarwal: Right. So a normal growth. So, when you say less than Rs. 50 crores, you include the maintenance CAPEX as well, right?

Manish Gupta: That's correct.

Manoj Agarwal: So including maintenance and growth, it will be on an annualized basis less than Rs. 50 crores, unless some special opportunity comes up which we cannot plan in advance, right?

Manish Gupta: That’s correct.

Moderator: Thank you. We have a next question from the line of Cyndrella Carvalho from Centrum Brooklyn. Please go ahead.

Cyndrella Carvalho: Manish, just wanted to understand, if you look at the formulation growth, just looking on the first half basis this is looking subdued, you have explained the reasons. But if these scenarios were not there, what it could be, like any color on that if you could provide? And going ahead, what is our outlook over there?

Manish Gupta: See, we have been guiding towards a 15% odd formulations growth, if you have been tracking us. On an overall basis we have been saying we will be growing high teens with the API business growing faster than the formulation side in fact, in medium-term. So generally we have been guiding or expecting about a 15% growth on the formulation side of business. So to that extent, that has been impacted to 11% in the first half.

Cyndrella Carvalho: Okay. And if we look at the API side also, we have reached almost 33% in the first half in terms of share. And where do you see this by FY21 or FY22, what's the outlook over there?

Manish Gupta: Small gradual shift, but I foresee, typically it will stay within 35% of our overall portfolio.

Cyndrella Carvalho: So 35:65 would be an ideal combination to go ahead with?

Manish Gupta: That's correct.

Cyndrella Carvalho: And if I look at the U.S. opportunity that you are talking about from the formulation perspective, how significant from a market perspective this could be? And where should we see in the scheme of game, what kind of share it could mean to SeQuent going ahead?

Manish Gupta: I can't give you a simple answer here, Cyndrella, you will have to come and see us on this. All I can say is, you can't ignore U.S. to build a global business. It accounts for almost 40% of the global animal health space. Everything that is in U.S., even in the animal health front is priced at least 50% premium to the rest of the world, even EU markets. So it's a very important market to target. We have carefully chosen a product portfolio for that market. We foresee about 10 filings for U.S. in the next three years. If you do a little homework on various generic companies, there are two of them who have done well in U.S., a look at what kind of revenues they generate in U.S, you will probably get the number which we have in mind, organically to achieve in U.S. over the next four years.

Cyndrella Carvalho: That's pretty exciting, I guess. We will definitely catch up on that. And just one last question from my side, in terms of inorganic how are we placed in terms of Europe region? Have we reached all the designated markets that we wanted to be or is there something on the card that we should look forward to?

Manish Gupta: Again, I will answer it in two parts. Strategically, our inorganic strategy will be focused on U.S. and potentially Australia going forward. As far as Europe is concerned, I think the only significant gap that we have in Europe is UK, given the Brexit scenario. That's one area we will look at, everything else will be opportunistic.

Moderator: Thank you. We have next question from line of Himesh Satra from Joindre Capital. Please go ahead.

Himesh Satra: What will be our tax rate for FY20 and FY21?

Manish Gupta: Tax rate you should assume in the range of about 15% for overall. I think tax rate we should assume at around 15% for FY20 and FY21.

Moderator: Thank you. We have next question from the line of Sachin Kasera from Swan Investment. Please go ahead.

Sachin Kasera: Sir, just one question on this tax, you mentioned this 15% is for FY21 or FY20 as well, for the first half the tax rate is quite low.

Manish Gupta: Yes. So, for the first half it is low, one of the facilities in India would be going in for the new tax regime and that's why it is reduced. But on an overall basis, you should assume that we will remain within that 15% range.

Sachin Kasera: So this year we should be at 15%, that's the way to look at it?

Manish Gupta: Yes. Maybe for the current year it will be lesser simply because, so second half you can again take 15% and for the next year at 15%, current year net impact will be slightly lesser than 15%.

Sachin Kasera: Secondly, what is the impact on EBITDA because of this IndAS, how much of that is in interest and depreciation?

Manish Gupta: It's fairly insignificant. It's about 15-18mn**.**

Sachin Kasera: Okay. Secondly, if we remove this other income, then we compare the number of vis-à-vis the June quarter, the PBT number is coming a little lower despite Rs. 6 crores higher sales. So, can you just highlight something on that?

Manish Gupta: Coming from EBITDA right, our gross margins were lower this quarter, if you see. I mean, everything is mathematical that way in that sense. So clearly it originated from lower gross margins So, you will see that our quantum of gross margin during the FY20 second quarter is Rs. 133 crores vis-à-vis Rs. 135 crores. And that is what is reflecting down more of a business mix issue for the quarter rather than anything else. There is no structural change and we expect the gross margins for the current year on an overall basis to be ahead of the previous year. And also, one more thing, you would also recollect, I mentioned that we had additional one-time OPEX of 18 million during the quarter, part of which was caused because of intense monsoon in Mahad and also some operational issues at Vizag.

Sachin Kasera: Sir, just one question on depreciation in that case, we have not seen too much of capitalization, despite that the depreciation is higher by around Rs. 4 crores, Rs. 4.5 crores. Is there some write-off or anything there, what exactly, this asset stabilization is not up too much.

Manish Gupta: There is nothing specific there. The Rs. 4 crores, Rs. 4.5 crores vis-à-vis what period?

Sachin Kasera: Q1. I am saying, if I look for the first half the depreciation we had almost of Rs. 4.7 crores, is like 25%...

Manish Gupta: No, Mahad was not there last year. Yes, Mahad came in only from August of last year.

Sachin Kasera: And sir coming back to this U.S., you have mentioned in the presentation that there are five API's where you are probably the only seller as of now. Can you give us some sense of what is the opportunity as we are looking in these five products?

Manish Gupta: Very tough question, Sachin. Because again, the lack of IMS deprived us of any further details

Sachin Kasera: Some ballpark would help, some broad sense, if it is a range also that will be helpful.

Manish Gupta: See, broadly what I can tell you is, okay none of these individually will be game changers or contributing few hundred crores of revenues. But every opportunity and where I am coming from is, all of these API's are very high priced API's, ranging from few hundred U.S. dollars to few thousand U.S. dollars per kg. So collectively they will be very meaningful, could add 20% to 25% additional revenues for us.

Sachin Kasera: On an overall company basis you are saying?

Manish Gupta: I am talking of API basis.

Sachin Kasera: And sir, any color on this Robenacoxib, what is the size, is it meaningful?

Manish Gupta: Yes, it is meaningful certainly, because that's why I told you we also have a formulation strategy around the product.

Sachin Kasera: And sir on this injectables, what is the trend that you have seen across U.S. and Europe once the product goes generic? Is it very unpredictable across products or there is a broad sense that you only see a 15%, 20%, 30% type of correction, any sense on that, how does the market behave in injectables as to go generic?

Manish Gupta: Yes, so I think what I am speaking is more for Animal Health rather than only injectables. Given the nature of this industry, the genericization leads to a 20% to 30% price correction and nothing beyond that. And this holds good for either oral generics or injectable generics in the animal health industry.

Sachin Kasera: And what is the type of market share the generic guys are able to garner? They're able to like get 30%, 40% market share within a period of 18, 24 months once the product goes generic or very difficult for the generic guys to get healthy market share?

Manish Gupta: So, in the production animal side, which is our focus area, the generic companies are far more successful vis-à-vis the companion animal products which some other companies operate in. Certainly nothing happens, I mean, there is no 90% and 80% genericization, but yes, between 30% and 40% over two to three years is achievable.

Sachin Kasera: So, coming back to this product that you mentioned that you filed injectable in Europe. So going by that we can at least conservatively assume that this $100 million market very ballpark which is in Europe, even after the recession should be at least $50 million, $60 million type of a market addressable to us, given the price correction?

Manish Gupta: Yes, maybe more.

Sachin Kasera: And then it will depend on how type of market share we can gain?

Manish Gupta: Yes. And that's where we have a strength, given that we have front-end organizations in eight of top 25 European markets.

Sachin Kasera: And you mentioned this first U.S. indictable, that is the same filing that you have done for Europe also or this is a different injectable that you are investing for Q4?

Manish Gupta: It will be the same. We need to do some additional work for U.S., which is what we are doing and then we will file.

Moderator: Thank you. We have next question from the line of Prashant Hazariwala, individual investor. Please go ahead.

Prashant Hazariwala: Sir, I would like to know what kind of benefit will get from Ambernath Mumbai facility. And how much costs we have incurred? Because so far we are not showing any R&D expense separate line, so will come into the picture, right?

Manish Gupta: The CAPEX incurred are you referring to or…?

Prashant Hazariwala: No, benefits of Ambernath facility Mumbai, that we have just started. How much cost it will incur?

Manish Gupta: We were already having our R&D in Ambernath, but it was not in a dedicated area, we were coexisting with manufacturing historically. What we have done is, now that we have doubled our R&D team and also brought in lot of specialized R&D equipment that is required. We have now created a separate and dedicated R&D area by adding a floor in the facility that we have at Ambernath. So, it is not very significant additional CAPEX that we have done. What we have done is, of course, made a fit to design R&D center at Ambernath. Clearly, when we are referring to 30-odd products that we are working on, about two-thirds of these products will be developed or are being developed at Ambernath, especially all our injectable pipeline. So, it is already a significant part of our growth strategy. In terms of how much we spend or how much we spend on R&D, of course, we do not disclose those numbers separately at this point of time. Having said that, other than the U.S. filing fee, we do not foresee significant increase in our R&D spend. As all of us are aware, U.S. filing is a very big cost element of any product development in animal health. Each filing in U.S. costs $0.5 million.

Prashant Hazariwala: Sir, actually how much annual cost it will incur? Because we have now reached almost double the R&D team, right? And all these other costs like overall…

Manish Gupta: See, this doubling of R&D team was done almost six months back. So these costs have been already hitting in our current P&L. Nothing has changed.

Prashant Hazariwala: So, it's not significant, right?

Manish Gupta: That's correct.

Moderator: Thank you. We have next question from the line of Vishal Manchanda from Nirmal Bang. Please go ahead.

Vishal Manchanda: Sir, just a repeat question on the 12 APIs that you have less than three competitors. Sir, could you share how many of these are commercialized?

Manish Gupta: See, all are commercialized in one way. When I say commercialized means these molecules or products have been made available to customers. Has the customer commercialized?

Vishal Manchanda: Yes, that's the question.

Manish Gupta: Okay. If that is the question, I will have to get back to you.

Vishal Manchanda: Okay. So basically, you are currently yielding revenues from any of these API's or none of these APIs?

Manish Gupta: We certainly will be getting revenues from some of these API's. But since your question is how many of those API's are yielding revenues, I will have to check and get back to you.

Vishal Manchanda: Sir, what I actually want to understand is the potential that we are yet to realize from these APIs filings basically.

Manish Gupta: So that is a slightly easier answer, because we have already built up our API business plan. And we have been guiding or have been confident of delivering a 30% year-on-year growth in the API side of business for at least next two years.

Vishal Manchanda: So even in FY21 we can look at a 30% growth in API?

Manish Gupta: That's right.

Vishal Manchanda: That's great. Okay. And one more on the injectable filing, it will need to be marketed as a branded product, right?

Manish Gupta: That's correct.

Vishal Manchanda: And so once you get an approval, will Turkey also be a part of the approval or it will need to be filed separately there?

Manish Gupta: So Turkey is, of course, separate regulatory filing and approval. It does not follow either EU or U.S. So we need to file and get approval in Turkey separately. And, yes, eventually we will certainly commercialize in Turkey as well.

Vishal Manchanda: And just one more on Turkey. So, all what do you sell in Turkey, is it your in-house manufacturing or you also procure from a third parties?

Manish Gupta: So, whatever we sell in Turkey is in-house manufacturing in Turkey for us. A very small part is outsourced, but more than 90% will be in-house manufacturing.

Vishal Manchanda: And you have enough capacity to continue to grow on whatever you are doing now?

Manish Gupta: Yes, we certainly have adequate capacities. Having said that, there will be a need for some minor balancing in some of the line equipment's.

Moderator: Thank you. We have next question from the line of Anubhav Sahu from MP Research. Please go ahead.

Anubhav Sahu: Sir, a couple of questions. One, if I got it right, in your opening remarks you mentioned about higher OPEX in Mahad facility. Was it due to some flood-like situation? And how much was the impact? I think you mentioned some numbers, but I couldn't get it.

Manish Gupta: Yes. So we incurred about 18 million as one time OPEX across the two major sites in India, Mahad and Vizag, most of it related to Mahad. I think all of us would have read this time that Mahabaleshwar received more rainfall than Cherrapunji, and Mahad is, of course, the foothills of Mahabaleshwar. So it has been very bad monsoon this time in that part of the region. So I will give you a simple example. We have a briquette fire boiler there. Now, clearly, for last three months, getting briquettes was a big challenge. So we had to get it from long distances. So these are the kind of simple things which impacted the operations. It wasn't that the plant was under water. It was just that the cost of operating the plant required certain unique actions to keep the production going.

Anubhav Sahu: And how is the situation now? Are we back to track as we were in Q1?

Manish Gupta: Absolutely.

Anubhav Sahu: And sir wanted an update on Promoters' pledge holding. I mean, for this quarter we have seen a sharp jump in pledge holding. So what is the rationale behind this, if you can provide an update on this?

Manish Gupta: Yes. So this is one question I will have to direct you to Bangalore. Because it's a promoter related question, nothing to do with the operations of the company.

Abhishek Singhal: There was a separate press release put out to this context by the Promoters. I think that's on the exchanges, and you can possibly access that.

Moderator: Thank you. We have next question from the line of Tushar Bohra from MK Ventures. Please go ahead.

Tushar Bohra: Sir, couple of points. You mentioned there are specific supplier issues in Europe, which has affected our H1 results, and which should not be the case going forward. So what could be a normalized run-rate for Europe? Let's say, adjusting for the backlog them that might have been in all, what should be the normalized run rate for Europe that we should build?

Manish Gupta: So, historically if you see, we have been growing close to double-digits in Europe, that has certainly dipped in the first half, we are down to minus 2.5% on constant currency basis. I foresee on a long-term sustainable basis before our new pipeline comes in, we should grow between 6% to 7% in Europe, again, on a constant currency basis, because currency is something we cannot really comment on.

Tushar Bohra: And H2 numbers should be slightly higher than that, should be better?

Manish Gupta: Yes, probably. Yes, we should be hoping for better than that.

Tushar Bohra: Second, sir you mentioned that we don't have a very large R&D expense. In fact, whatever it is, its mainly the filing cost. At the same time, we mentioned this product where we are the only VMF filer. So just to understand, of course, I do appreciate that this is different from pharma, animal health is a very different space from pharma. But what would have stopped other people from filing the VMF for this product? Or in general, why are there not enough filers and in VMF? And is it not very research intensive from a cost perspective?

Manish Gupta: So, I think you would have heard me saying this multiple times because people kept asking questions on the size of the market for particular APIs or molecules. The fundamental challenge of this industry is lack of information and not chemistry. So, the cost of developing a veterinary product is not very different from human side. So the cost of developing either a API or a formulation is not very different between human and veterinary side. What is lacking in animal health is information. Clearly, nobody can figure out volumes and also the pricing. Also, individual molecule size is very small compared to a human molecule that makes it unattractive for the typical human pharma companies to look at veterinary side of business. So that is the only reason I foresee.

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

Manish Gupta: Thank you, all. Thank you for taking time and having this extensive Q&A. As a company, we have chosen a path less treaded. We stay confident of what we have been achieving and confident of delivering what we have been guiding towards for the current year. It has been a little challenging environment globally and more so in India. But all in all, we stay confident of delivering the financial outcomes that we have been guiding towards. Thank you, everyone. Thanks again.

Moderator: Thank you very much, sir. Ladies and gentlemen, on behalf of SeQuent Scientific Limited, that concludes this conference call. Thank you for joining with us.