"SeQuent Scientific Limited Q1 FY-21 Earnings Conference Call"

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Moderator: Good morning ladies and gentlemen. Welcome to SeQuent Scientific Limited Q1 FY21 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 Lizann. A very good afternoon and thank you for joining us today for SeQuent Scientific's Earnings Conference Call for the First Quarter ended Financial Year 2021. Today we have with us Manish – SeQuent's Managing Director, Sharat – Joint 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 website. 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 will now hand over the call to Manish to make the opening comments. Over to you Manish.

Manish Gupta: Thank you, Abhishek. Good morning friends. A warm welcome to all of you who have joined this call.

Joining today with me on the call, we have Sharat Narasapur, the Joint MD and Tushar Mistry, CFO.

It has been almost 4 ½ months since the world went into various lockdown modes and if the indications are to go by, this is likely to continue in the foreseeable future. I do hope that you and your families are keeping well and adopting all safety measures as we get into potentially the more difficult period as the lockdown eases and economy opens leading to spurt in cases.

At our end as well, recently some of our employees at Mahad tested positive in RT-PCR testing as part of mass-testing undertaken in the area at the behest of the District Collector, under which all employees across all plants in the area got tested. Even though most cases were asymptomatic, we temporarily stopped production while continuing other operations and undertook deep disinfection of all the areas in the factory premises. These actions were in addition to everyday disinfection, screening of employees for body temperature & oxygen levels and social distancing in common areas which have been in practice since the onset of pandemic in March-2020. The production will restart shortly, and we do not expect any material impact on our performance for the quarter or year.

These are indeed challenging times and we function in an essential industry where demand is consistent. This has allowed us to operate our plants albeit with significant operational challenges. I would like to use this opportunity to place on record my sincere appreciation of the efforts of our employees as well as our leadership team across the globe for a near flawless execution in a difficult operating environment.

I will briefly touch upon the performance of the quarter and then we can throw open the floor to the Q & A session.

For the quarter ended June 30, we clocked revenues of Rs.310 crore, a 11.6% increase over the corresponding period last year. The growth was primarily led by another consistent quarter from APIs which grew at 13.4% while formulations came at about 8.5% on constant currency basis. This comes under the backdrop of a very nervous business environment as well as operational challenges and the team showed great courage and flexibility to adapt to the new-normal and deliver a near normal performance.

If I had to analyze formulations, you would observe that we have had good growth across LATAM, Europe and Turkey. However, as I alluded in the earlier call, we stay cautious in emerging markets leading to a decline of 43% during the quarter, partly tempering the growth of formulations. Adjusting for this, our growth in the rest of formulation business is upwards of 20%. However, as I have always mentioned, the strength of our business model is in its diversified portfolio mix which ensures resilience to such challenges.

Going forward, we expect the growth in the emerging markets to return and we expect to finish the year on a strong note. This will also be facilitated by our recent commercialization from 1st July of a multi-year agreement with Zoetis India to market and distribute their ruminant portfolio in India. This portfolio of 13 brands (19 SKUs) covering the therapeutic areas of Antibiotics, Parasiticides, Vaccines & Hormones covers both their vintage brands of over 25 years as well as the global brands. This addition effectively shall double our presence in the India ruminant business.

APIs, as discussed earlier turned in another strong performance with growth of 21.5% on reported basis and 13.4% on constant currency basis. Our focus on API business continues to be on regulated markets and the recent global developments in the space augers well for us in the medium to long term.

In keeping with the increasing demand, we have initiated expansion at our Vizag site which should facilitate our growth in FY22 and beyond. We envisage a total investment of around Rs. 50 crores over next 18 months. As mentioned in the last call, we have deferred the expansion plan at the Bremer facility in Germany due to execution challenges brought about by Covid.

Coming to financials, our EBITDA margins have improved 290 bps for the quarter at 16.8%. Our highest ever EBITDA at Rs. 52.1 crores in a generally weaker quarter gives us a sound start in the new financial year of unpredictable environment. Net profit for the quarter was higher by over 80% at Rs. 21 crores.

We place probably equal or even higher emphasis on our balance sheet ratios with both ROCE and Net Debt to EBITDA moving in right direction over 13 quarters consistently. We draw great comfort in generating over Rs. 40 crores cash flows from operations for the quarter, leading to significant reduction in our net debt since last quarter.

I am sure that you would have also seen our update on the progress on Carlyle transaction. The transaction is expected to conclude within the current quarter.

To conclude, our focus during the pandemic has been to keep the business functioning while at the same time empathizing with all our stake holders. While placing employee safety as the top priority, we have also ensured that our bankers and more importantly our vendors and other partners are paid in time. We now look at the rest of the year with far more confidence compared to where we started the year.

With those words, I will now throw open the floor to Q & A.

Moderator: Thank you. Ladies and gentleman, we will now begin with the question and answer session. The first question is from the line of Cyndrella Carvalho from Centrum.

Cyndrella Carvalho: Just wanted to understand from you how are we looking at the formulation emerging market business, you indicated that from June onwards have we seen some recoveries there or what is the current status?

Manish Gupta: Cyndrella, I will break the emerging markets business into two buckets, one is India and second is of course other emerging markets that we operate in. Both these markets were down in the last few quarters and our concern largely has been around collections rather than revenues. So that's why we have been going slow. Having said that with oil prices moving up and the dollar being stable now the other emerging markets have stabilized and we already see a traction in business. Even in India there has been an improvement in the business environment starting from June and that has really picked up in July. Further, facilitated by our recent Zoetis commercialization of portfolio in India, we are confident of this part of business being back on growth track for the rest of the year.

Cyndrella Carvalho: Any color on Zoetis how it will help us and what is the strategy over there?

Manish Gupta: Zoetis portfolio comprises of both their vintage brands - .old Pfizer brands which have been in existence in India for over 25 years as also some of their recent global or innovator brands, including vaccines. Clearly, there is a strong element of pull in these products and what we are likely to achieve out of this is not only kind of enhances our presence with the doctor base, But more importantly, it will also help facilitate some of our own business practices. So, what we foresee out of this is our own debtors across India business will come down because of the very high pull that the Zoetis portfolio commands in the marketplace.

Cyndrella Carvalho: Any color on the API side, how is the pricing environment? Are we seeing some price inflation there and any view in terms of sustainability of that?

Manish Gupta: Sorry, I didn't hear the last part clearly. Can you come again?

Cyndrella Carvalho: Sustainability of the pricing, pricing environment on the API side?

Manish Gupta: Yes. So, you have to bear in mind that our strategy is in and around regulated market and regulated customer and being in animal health, the end product pricing does not really change. We are not in human pharma, wherein shortages lead to spike in prices. Animal Health is a commercial industry with stable prices. So for us, we are not seeing any short-term benefit of the price changes that are happening in the human pharma industry, nor are we wanting to go that route, because ours is a long-term sustainable business model with regulated customers who do not like price changes on an order-to-order basis. Having said that, the recent global dynamics or geopolitics that are emerging clearly reflects to a long-term good time for API business, maybe between 3 to 5 years. So I see a definitive improvement in the way API businesses are looked going forward for a sustainable period of time.

Moderator: The next question is from the line of Varun Goenka from Nippon Mutual Fund.

Varun Goenka: My question is regarding the Zoetis agreement. If you can just help us understand what's in it for us, how does this agreement really come to be? Exactly what is the strength that we are bringing to the table and what is the demand opportunity in India for these products that you are going to market? Maybe the whole, if you can help us understand the end-to-end market opportunity, it will be giving us a good sense.

Manish Gupta: Obviously, I cannot disclose too much details about it given the confidentiality reason. Some of the color around the arrangement, I've already shared in the previous question by Cyndrella. So anything more specific will be difficult but having said that as I said this kind of doubles our presence in the ruminant business in India. While Zoetis also benefits from it because they are not having their own field force to market these products., we are also going to benefit not only from incremental profitability out of this portfolio, but more importantly, improving our own hygiene of business as well, leveraging the long-standing relations due to vintage nature of these brands.

Varun Goenka: And what would be the probable India demand opportunity or addressable opportunity for us as such?

Manish Gupta: We expect between 25 crores to 30 crores of incremental sales out of these products in the current year, which is about 9 months of operations.

Varun Goenka: And that would be what market share...

Manish Gupta: I think you must bear in mind that animal health does not have this kind of data.

Varun Goenka: No, but in your estimate, sir, what could be the size of the market and we would be getting our trading margins or how is that?

Manish Gupta: Let me say it slightly differently. This has a meaningful impact on our India business in terms of both sales and profitability. But in an overall perspective, it is obviously not that significant. On a global P&L basis, it is not material. But certainly, for our India operations, it is significant.

Varun Goenka: So, would that also maybe in future entail that we can get into some kind of a manufacturing arrangement for them or something or this is purely distribution?

Manish Gupta: This is purely a sales and distribution arrangement for India. Having said that, we are already engaged with them on the API side of business and that will always continue to kind of expand the association as part of our regular business strategy.

Moderator: The next question is from the line of Samir Palod from AUM Fund Advisors.

Samir Palod: My question pertains to the US geography there if I look at your R&D slide, you've talked about a lot of filings that you are likely to do in the US market over the next few years as well as on the API side. So since you're already present in Europe and LATAM in a big way, US is I guess is baby step, so if can you just explain the US strategy and the size of the market and when you expect to crack into that market?

Manish Gupta: So Samir, of course, this requires a much larger conversation, which we can do off-line at some point of time. But broadly speaking, I'll split this into two, the API side of business, wherein we are already in US and selling, as we speak. Between 3 to 4 molecules of ours are already commercialized and this will only expand as we go forward. However, coming to the formulation side of business, we are at least 18 months away from our first commercialization in US, having filed the first product in the last quarter that was in March 2020. We do not foresee US to really appear in terms of our formulation business till end of FY22 and the meaningful contribution will only start from FY23.

If you need more clarity on this, we can get into a separate conversation off-line because it requires a much detailed conversation.

Samir Palod: So it's not an immediate FY22 or '23 sort of initiative, it's just building up the pipeline at the moment.

Manish Gupta: Yes, because there is a regulatory approval time line. So anything that we have filed today will take minimum 18 months for approval. And that's how we are building up the pipeline. But the journey has been started and in the meantime, obviously, the commercialization of those in-house developed products in other geographies, including in Europe, will keep driving our formulation business. So we are still confident of a double-digit formulation growth in the medium term.

Samir Palod: And my second question is with respect to margins. How do you see, you've got almost a 300 basis point increase in margin on a YOY basis. Given your mix, how do you see and you also mentioned that emerging markets are going to bounce back, so how do you see the margin profile for the rest of the year and maybe for FY22 as well in your business?

Manish Gupta: So again, I'll take a step back here and as we have been alluding in our previous con calls, we have been targeting a mid-teens growth in revenue and about a 200 bps margin improvement year-on-year in the medium term. Largely speaking, we stay in line on delivering those objectives. Having said that, the current year is a bit unique and it is very challenging to predict what will happen and as I have been always mentioning, we will take one quarter at a time in the current year because we do not know how really the lockdowns and the localized spurts will play out across the globe. So after first quarter, certainly we are far more confident for the rest of the year. Having said that I would really kind of reserve my comments for the current year and will take quarter-by-quarter as we go along but the long-term directional goals continue to be intact.

Samir Palod: Just as a follow on to that, Manish, so like we are seeing a lot of others on the pharma side, in animal health, are you seeing a very robust pricing environment given what's going on with China and with this pandemic both on the formulation and the API side? Are you seeing price increases or the margins are increasing as a result of some mix or efficiencies that you've brought to the table or it's a combination of all of this?

Manish Gupta: So, our margins are headed in the right direction, largely coming out of scale as we scale up in every geography or each of our initiatives. Animal health business is a commercial industry unlike human pharma. So we do not see any price changes happening in animal health because the price of protein is not changing for the end consumer. So, to that extent, the dynamic of animal health business is different from human pharma. Again, we can take this up in a slightly one-over-one conversation because this requires a lot of understanding of the business, and we are happy to invest that time with you. So, Samir, we'll take it off-line if you are ok.

Moderator: The next question is from the line of Dushyant Mishra from SageOne Investment Advisors.

Dushyant Mishra: Just quick question on the US acquisitions. Do we have anything in the pipeline? Are we looking for any opportunities to emerge right now?

Manish Gupta: So, a difficult question at this point of time especially where we are awaiting a conclusion of change of control. So, in a way we have to partly reset our thinking in terms of way ahead with once the new ownership is in place. So all I can say is, there's nothing the pipeline in the short term. But once the change of promoters takes place or change of shareholding takes place, that's when we will probably get into an engagement with the new promoters and look at the world probably a little differently.

Dushyant Mishra: And I know that you have also mentioned something about maybe entering the China market and you wanted to focus on that as well. So, is that something that would also happen once the change of ownership has fully transpired?

Manish Gupta: That is correct. Thanks.

Moderator: We'll move on to the next question that is from the line of Vishal Manchanda from Nirmal Bang.

Vishal Manchanda: On the US, can you guide us how the distribution is? Is it like we see in human pharma or is it more complex in case of animal health products?

Manish Gupta: Vishal, what I'll do is because this, again, is a slightly detailed question beyond the quarter performance, we can again take it off-line and I'm happy to even organize the call of yours with our US Head of Business, who will be able to give you a better color around it.

Vishal Manchanda: Okay, sir. Another one is on this Zoetis transaction. So one, how was this distribution happening prior to you taking over the distribution rights?

Manish Gupta: So, there was another animal health company, Boehringer Ingelheim that was distributing these products in India till recently and that's what is getting transitioned to us now.

Vishal Manchanda: Are these kinds of unique products which kind of would have lower competition than other animal health products, we would have many suppliers is what I would understand. So what would create that pull for these products basically?

Manish Gupta: So as I alluded to, this includes portfolio of certain vintage brands, which are very important and relevant in animal health as also some of their innovative products, which means there is no competition for those products. So both the range of products is part of this portfolio and that kind of creates a strong pull for these products.

Vishal Manchanda: Would you need to incrementally invest in terms of the field force to promote these or this you would be leveraging your existing field force?

Manish Gupta: So more or less, we are leveraging our existing field force. The only thing we have done is, we historically had not started operations in Karnataka and Kerala which is what we have started as part of this arrangement because with the complete portfolio between what Zoetis brings in and also our own portfolio, the operations in Karnataka and Kerala now becomes viable for us.

Vishal Manchanda: Is the injectable approval in Europe on track? So basically, are there any additional queries or that can potentially delay the approval?

Manish Gupta: There are no surprises thus far. It seems to be on track and is following the regular time lines as mandated by the DCP application process.

Moderator: The next question is from the line of Sachin Kasera from Swan Investment.

Sachin Kasera: My first question was on the gross margin; so despite the share of developed market being higher this quarter, when I compare the gross margin vis-à-vis the March quarter, there is a small decline. So would you just like to comment on that?

Manish Gupta: The tougher questions I'll pass on to Tushar. So Tushar, if you can?

Tushar Mistry: So, the gross margin actually is lower compared to Q4FY20 but in line with Q1FY20. In this current quarter we have had higher contribution from our European and Brazilian subsidiaries, where the gross margins are generally on a lower side. And that's the reason why you see this mix change.

Sachin Kasera: If you could update us on our strategy of buying out the minority stakes in some of the JVs or subsidiaries? So any thoughts or any progress on that how are we looking to go because we are very confident in terms of the cash flows? So are we looking at any of those opportunities?

Manish Gupta: I think this is something we will align with the new shareholders and probably based on their thought process, we can see some clarity on this in the later part of the year.

Sachin Kasera: On the US, you have been mentioning about building up front-end there and maybe taking whether organically, inorganically, so any progress on that front? How are we thinking? Are we now more or less decided that we are going inorganic or are we still evaluating the options?

Manish Gupta: So I'll again split this into two parts. On our own, we were thinking of setting up our own organization and to that extent, we had already hired a US Head of Business last year. Having said that, this is one area wherein we do foresee Carlyle making a contribution and their thinking will certainly impact our strategy, especially on the acquisition front. So give us couple of weeks or couple of months before we can clearly give an answer on this. But surely, I expect our US strategy bid to be a little more aggressive than what we had envisaged earlier.

Sachin Kasera: And then just last question regarding the other expenses. So we have seen a lot of operating leverage coming this quarter. So I would believe part of that would be the cost reduction initiative done by the company and operating leverage. But is it that some part of the expense could not be incurred because of the lockdown and that will normalize from Q2 or this is like a new run rate that we are looking for?

Manish Gupta: Again, difficult one, so I'll pass it to Tushar.

Tushar Mistry: So on the OPEX front; you see some reduction that is happened. 50% of this is related to field and travel expenses because our field people and all have not been traveling and that is the reason why you see a reduction there. And 50% is towards certain reduction in our outsourced cost that is conversion cost which we outsource, since we got that in-house. So that is what is an impact on OPEX. But also important to note is that you see some increase in the employee cost side which we spend almost about a crore on additional expenses on employee cost related to incentives that were given for employees during this pandemic time and also certain additional welfare expenses that we incurred on them. So both these things are contributing to the movement in that OPEX.

Manish Gupta: I think at a broad level, roughly 50% of these OPEX reduction will scale back once the field operations start and the balance 50% which is on account of transitioning outsourcing internally will stay for good. And also there would be a kind of normalization of employee costs going forward. So, all in all, I don't think we have tackled the cost side drastically. In fact, we want the eco-system to survive. And that's why you'll see in my commentary also I've been mentioning that we have operated our business very responsibly. Only if our vendors survive, can we survive in the long run. So, we have been making their payments on time and we have not been harsh with them. And we have been in a way proven right at the end because we see similar behavior from our own customers.

Moderator: The next question is from the line of Rahul Veera from Abakkus Asset Manager.

Rahul Veera: Just wanted to understand like in terms of our manufacturing facilities, what would be the top three manufacturing facilities for us contributing maximum?

Manish Gupta: On API side, we have two major facilities. The real major one is the Vizag facility and then we have Mahad, which together will constitute almost, 90% of our API revenues. Tarapur is more of an intermediate facility.

And coming on the formulation side, our three major facilities would be Spain is for Europe, Turkey facility for Turkey and Brazilian facility for Brazil. So it's fairly evenly spread out. In that sense, we are not dependent on single facility.

Rahul Veera: Due to a few COVID cases on the Mahad facility, do you see some revenue loss on that end of the business? 15 days or 20 days of quarantine is required for the same in COVID.

Manish Gupta: So I will have Sharat respond to it from how we are dealing with it and what all actions we have taken. But from a revenue perspective, we do not see any impact because we have that kind of headroom available per se in terms of production capacities. But Sharat, if you can explain?

Sharat Narasapur: So, at Mahad, we have over 400 employees and about 80 of them tested positive, largely asymptomatic cases, so out of that already as we speak today, about 45 have already been released from the quarantine center. So they are all doing well. But rest of them who are negative as a part of abundant precaution, we have discontinued production temporarily. But within next couple of days all of those who are negative will turn back for the work and in the meantime, we have all processed everything which is in WIP and the show continues.

Moderator: The next question is from the line of Anmol Ganjoo from JM Financial.

Anmol Ganjoo: I have an easy question for you Manish, you alluded to the absence of data which characterises our business. This typically also throws up arbitrages or short term opportunities in the market. Given where our filings are how would you characterise that landscape and market opportunity in the current times and are there possibilities of it, positive surprise emanating from that in the quarters to come?

Manish Gupta: See ours is a kind of dull and drab industry, unfortunately with very few big opportunities and everything in our business is branded generics which mean there are no short term surprises that can typically happen in this industry. That goes both ways because there are no short term positive surprises and also any short term negative surprises as well because it’s slow and steady and consistent business. So personally I do not see any of those surprises emerging in our business as well as also for the industry as I see it at this point of time, both from a positive angle or a negative angle.

Moderator: We will move on to the next question that is from the line of Vipul Shah from RW Equity.

Vipul Shah: Just one question which I believe was partly answered but also in the letter of offer we mentioned that we are actually looking at buying out our Turkish partners which is also visible in the minority interest contribution to the total PAT doubling from the March quarter. So any thoughts on that and how soon can we expect to have our desired outcome of having total control over the Turkish subsidies?

Manish Gupta: This is also part of our agreement in Turkey; there was a put option at the end of 5 years so it is all in line with that. We are making good progress on that conversation and again probably within the current calendar year itself, we should be in a position to finalise that arrangement.

Vipul Shah: So in general very difficult to model, I understand the volatility also of the currency but on a steady state basis what is the total contribution of minority interest to our total PAT which we can factor in?

Manish Gupta: I think you should look at the annualized number rather than any quarter-on-quarter number because of the seasonality or different aspects of business coming out in each quarter. So if you look at the annualised number of last year that will give you a very good perspective. Tushar you want to add?

Tushar Mistry: Yes, it is approx. 15% when we look at the annualized numbers for FY20 as the minority interest contribution.

Moderator: The next question is from the line of Ashish Thavkar from Motilal Oswal.

Ashish Thavkar: Manish this entire concept of the government where they are trying to promote manufacturing, would we be a party to it and any plans on that if you can share?

Manish Gupta: So first let me respond at an industry level and then we'll respond at a SeQuent level but this is first time I'm seeing government moving decisively and proactively in terms of the initiatives that they are taking and this feels to be a real serious exercise I must admit at this point of time unlike in the past wherein you could do some tinkering, this time we see some clear incentives and some clear direction in the medium to long term perspective. Having said that the focus of these new initiatives is towards antibiotics and towards import dependence of the human pharma drugs. So we clearly are not participating in that area at this point of time and right now we do not see any impact of this on our business strategy.

Ashish Thavkar: And for our injectable Europe business, so how are we placed in terms of sourcing of our raw materials, in terms of establishing that linkage with the supply chain? So just broadly, one or two minutes if you could highlight help us understand this.

Manish Gupta: We are fairly well placed on this as far as our supply chain is concerned and material supplies were a bit uncertain for some point of time but everything is now more than back to normal across the world.

Ashish Thavkar: And Manish would the plans also be to monetise similar products in US?

Manish Gupta: That's correct. You are talking of formulation development right?

Ashish Thavkar: Yes.

Manish Gupta: Formulation development is global with most of those products also going to be eventually commercialized in US.

Ashish Thavkar: So you said in the veterinary side of the business the pricing typically remains constant. So in terms of margin expansion as you said in your opening commentary, we do anticipate some margin expansion going ahead, so if you could help us understand how those margin expansion would come up?

Manish Gupta: So our margin expansion is obviously coming out of scale benefits, both on the API side as well as formulation side. On the API front obviously all our investments have been made at the sight and operating costs for the sites remain same even as we expand the business especially in US and Europe which are better priced markets. And similarly on the formulation side of business, once you establish your field force your fixed costs are already there. So as your revenues grow, the impact on margins is far superior in this industry compared to other industries.

Ashish Thavkar: And in terms of our capacities how are we placed? Are we done with the CAPEX that we need for the next 3-4 years or we're about to expand?

Manish Gupta: Again, this is something I alluded to in my opening comment that we have started expansion at Vizag which we entail an investment of about INR 50 crores over 18 months and this will facilitate our growth. We are obviously fully invested for the current year. But it will start helping our growth from FY22 and beyond. Similarly on the formulation side, our major investment which is about €3 million is envisaged for facilitating in Germany to have a 4X expansion there but that is a project that we have deferred to sometime early next year, simply because of the uncertain environment and getting a project team in this environment is not so easy specially in Europe.

Moderator: The next question is from the line of Sajal Kapoor from Unseen Risk Advisers.

Sajal Kapoor: Just a couple of questions. First one is on our new line of business which we have initiated recently the CDMO I'm talking about and what sort of capability is attracting our potential partners and customers for that line of business and secondly do we intend to serve the innovators only or we don't care who the customer is as long as we have the capability and the economics are favourable for us?

Manish Gupta: So Sajal as we talk of we are focusing on CDMO only on API side of business and that too only for veterinary customers. So ours is a very narrow focus simply because the expertise we have and we really want to be one stop solution to the big veterinary companies which are not too many. There are only four or so as we speak and we want to be their one stop solution for all their API needs including CDMO arrangements. This is the new skill set we are developing, so technically we are capable but it's all about project management and how do we interact with these customers. You do not see too many bio-techs or new startups in the animal health space. So our focus would be largely towards these three or four customers and in catering to their API development needs.

Sajal Kapoor: Just to follow up Manish, where do we expect competition if any to come from because clearly ours is a pure play animal pharma and not any other player has got the US FDA approved facility, so do we expect no competition at this point in time especially from any other Indian players?

Manish Gupta: No, I don't think anything in the world can be with no competition for a long time but we are certainly fairly well placed because obviously the attention which we give to these customers is very different from the typical human pharma companies. Also you have to bear in mind that increasingly regulators are seeking segregation of animal heath production from human health which again kind of puts us in a good shape because eventually CDMO also has a MO part, the manufacturing part. So given that we have dedicated veterinary API facility, so I would say we are very well placed but it's not a huge area that we are getting into.

Sajal Kapoor: Second question is on our VMF filing. So on six of those we are the sole filers, so an example could be the Robenacoxib which we filed last year. Any feedback from the regulator or the timeline for approval and whether it's come and Robenacoxib is injectable as well as a tablet. What sort of launch and timeline are we guiding?

Manish Gupta: So the API launch is dependent on the formulation. And the API file in US is never reviewed till the formulation is filed and formulation is up for nearing commercialisation or review in that sense. So all these filings which we have referred to are at various stages of customer approvals and will be commercialized as and when either the patent expires and/or the customer gets an approval.

Moderator: The next question is from the line of Mitul Soni from GeeCee Investments.

Mitul Soni: Did we have any loss of business because of COVID during the quarter, the early months?

Manish Gupta: Depends on how you want to see, call it loss of business obviously the performance was lower in certain aspects of business especially India formulation because nobody could travel even supplies could not be made. So there are obviously difficulties in conducting business. There have been some losses in that context but very difficult to quantify and that's why for us its part of life.

Mitul Soni: Are we seeing increase in enquiries for our API products, are we seeing more enquiries from the customers across who have joined hands for the API, are we seeing any sort of that?

Manish Gupta: So I'll again respond it in two buckets. Certainly, in Q1 there was, and this is first time referring from an immediate business perspective as we were nervous, even customers were nervous, and we could see some kind of element of deferring of purchase decisions at their end. So it was not a normal quarter in that sense even for us. Even on the API side though we did display or ended up with a 21% growth. Having said that from a long-term perspective I think there is a clear move towards sourcing from other than China and we clearly see a long-term move. This is not going to happen in a hurry simply because of the regulatory process that we have to follow but I see a strong positive momentum for next 3 to 5 years.

Mitul Soni: And one more last question, on our Europe and Turkey subsidiaries, we are seeing the strong constant currency growth. How much of that growth would be value driven and in the sense price increase or it is all primarily volume driven and how much we can take as a future like can we still continue to see about mid-teen growth there?

Manish Gupta: Turkey certainly will grow mid-teens in the medium term. Europe touching double-digit is always a good thing to achieve and the way I look at is roughly one-third of the growth comes out of value or price increases and the rest two-third comes out of the volume.

Moderator: The next question is from the line of Vishal Mora from MK Ventures.

Vishal Mora: My questions on CDMO were answered though I have some questions on the Zoetis transaction. I will just bunch them into a single question. Just want to understand what was the reason for this business being transferred to us from Boehringer and what was this price of this business for Zoetis in India. I am assuming the profitability would be good because these are exclusive products but what is the size in my words is transferred and whether this opens up a possibility for you to do in other geographies as well with Zoetis or even some of the other innovators?

Manish Gupta: The first part of the question is slightly difficult for me to answer and partly may be better for Zoetis to respond on why they are transferred. But having said that I have been eyeing this business I would say for last 5 years. So in some sense it has happened for us at the right time in that context. Zoetis has been using another partner for distribution in the past and they have transitioned it to us. It is also kind of reflection of now we are 5 and 6 years old in the business, so there is an enormous acceptability around Alivira even in India. The size of the business, again I covered broadly in the first year or first nine-months of the current year, we extract between 25 to 30 crores of revenues coming out of this business and of course profitability is something I would stay away, that’s too confidential and internal but clearly it is meaningful business or meaningful arrangement for both the parties. And finally can it be expanded to other regions, time will tell. Obviously the intend would be to do is something beyond India as well.

Vishal Mora: On CDMO just one thing are we looking at say over the next 2-3 years CDMO being relevant enough and big enough that they may have dedicated capacities for it or do we need seal that CAPEX may be accelerated because of the CDMO initiatives.

Manish Gupta: Difficult to answer this because we are very-very new. We are still understanding this business specially and opportunity within the animal health space. We are very clear that we don’t want to venture on the human side of business. So at this point of time I would stay away from commenting on this. It is not built-in our business plan, let me be candid but maybe in next 6 to 12 months we will be able to give you a better color around it.

Moderator: The next question is from the line of Akash Jain from MoneyCurves Investment.

Akash Jain: Just one question for my broad level understanding. There are lot of parts to our business, there is an API business and even in formulation there is a LATAM business, Europe business and India business. If you want to get our arms around the margin profiles and how the margin of the company is going to improve. Can we get some qualitative understanding of how the interplay of the margins are between these businesses? API and within formulation our emerging markets/India, Turkey, Europe and LATAM. Just to get a sense of where we are, where is most of the operating leverage going to come from and how does it interplay work on an overall basis for the company?

Manish Gupta: Broadly speaking the strength of our business model is having multiple growth engines and that has what has worked well for us because always you will see that certain things are firing for a quarter and you may be faced with some challenging environments in certain parts of business. At a broad level certainly the gross margins are higher in Turkey which we have been alluding to in the past. Fundamentally all injectable businesses have higher margins compared to the oral businesses. So, our European as also Brazil business is more orals while our Turkish and emerging market business is more injectables. So that would probably give you an indication of margins. The moment there is a faster growth in markets like Europe and/or in Brazil there would be slight change in our gross margins though it is not very-very significant. Similarly on our API side of business our API margins are not very different from the collective margins of the formulation business. So again all in all you will see very narrow shift in our margins across quarters and across years. The benefit we are deriving is really the scale of benefit as we drive our business going forward. So our investments are already there in place and as the business ramps up while revenues may ramp up by 15% odd the impact of that on the margin side is obviously slightly more disproportionate given that most of our costs are fixed.

Akash Jain: And just a follow-up question Manish if may I ask. On API obviously scale leads to lot of operating leverage and on formulations business given that it is all branded generics. Typically the productivity or whatever we call the revenue per sales person is a big driver for improvement in margins. Am I reading it right in terms of how you expect scale-up of margins to happen?

Manish Gupta: Absolutely bang on.

Moderator: The next question is from the line of Saket Bansal from Opulent Investments.

Saket Bansal: My question is regarding the API business. So last quarter we mentioned there was a deferred sales of Rs. 8 crores, so this quarter we would have got that sales. Is it correct to understand like that?

Manish Gupta: Yes, we did get back. That sale has been booked in this quarter but there is also an element of deferred sales even for this quarter obviously because of logistics.

Saket Bansal: What would be that quantum?

Manish Gupta: About 4 crores.

Saket Bansal: You spoke about the margins just now like different countries have different set of margins. I wanted to understand what is the utilization level in all the plants like is it at 80-90% or what is it?

Manish Gupta: In pharma you can never go 80%-90%. Typically once you hit or once you envisage you are hitting about 80% you have to start planning expansion.

Saket Bansal: What would be the current state?

Manish Gupta: Our current capacity is certainly adequate for this year and also part of next year and as I alluded or spoke earlier, we are already working on expansion at Vizag and at Germany.

Saket Bansal: Can you throw some color on injectable business like what is the size and what is the target size of the market? How big this opportunity is?

Manish Gupta: Very difficult question Saket. I don't have ready-made answer but having said that we are happy to engage on a more one-on-one basis and give you a better color because the answer is going to be very long.

Saket Bansal: Just one more question. Out of this we are 75% of our API businesses in regulated market 65% of formulation is in regulated market now. And in earlier calls because you have mentioned as we move more into the regulated market more the margins can be improved, right?

Manish Gupta: That's correct, especially on the API side.

Saket Bansal: So how much room is still available?

Manish Gupta: Again I will respond at a broader level. The fact that we are alluding to a 200 bps margin improvement year-on-year over a medium term and not for the year alone is all coming out of those quality of business parameters that we have been talking about.

Saket Bansal: In Turkey business, how is it like what is the growth rate we are expecting?

Manish Gupta: Turkey we are expecting mid-teens growth rate in the foreseeable future. It cannot be every quarter and all, there will be some volatility across quarters but on a directional level we are talking of mid-teens growth.

Saket Bansal: Because this quarter was a growth of only 4% that is why I am asking?

Manish Gupta: No but on a constant currency it is 11%. That's why we are very upfront in giving growth in every geography on a constant currency basis because there is an element of volatility of currency.

Moderator: The next question is from the line of G. Vivek from G. S. Investments.

G. Vivek: Congratulations on yet another consistent quarter and I am surprised at times on how come you are so consistent and if you can elaborate on that part also plus what is the value add been done by our partner Carlyle which is expected and what experience do they have in the animal healthcare sector? And second question is about our domestic dogs and other things that they are almost becoming like a part of family world over with the cycle going on in for a Western lifestyle and no kids and the pets are having the important place. So how positive is it for us and opportunity size if you can tell for us.

Manish Gupta: As I understand your first question was around Carlyle and their experience in this industry. So from whatever we know while Carlyle has great experience in the global health care space and it is one of their preferred areas of investments. They have no direct exposure or this will be their first investment in animal health space. They have in the past, been associated with animal feed businesses but not something directly in animal health space and the idea is how do we create a far more global organization in the animal health space is the fundamental thesis of their investment. At a broad level they have given us three or four areas of value creation that they will be focused on, one is US, second is China and third vaccines. Having said that given that they are not as yet part of the promoters, we have not yet interacted and created a new or we have not interacted to the extent that is will happen over the next couple of months once they are part of the promoter group. The second part of the question was pertaining to the Indian companion animal business. That clearly is a growing segment in India as dogs and not so much cats in India but dogs are becoming part of families. As we speak we are not there in that business in a meaningful way though we have one or two products. That is again an area which we will look at as we move forward. One thing you have to bear in mind is animal health is very-very complex in that context because there are too many species you need to deal with. So we'll really pick and choose what we want to play and in that context, while companion animal in India is growing and important but it so far we didn't see an opportunity for us to make a dent in this industry but that can change going forward.

G. Vivek: That is a true for world over, not only for India companion analysis and specially in the West?

Manish Gupta: That is correct but if you follow our strategy we have stayed away from companion animal business across the globe and that is simply because that's an area of big focus of the big daddies and there is a lot of dollars and money that flows in that part of business. So, we are very conscious of the way we leverage our capital and therefore we have chosen to opt for or chosen to focus on the ruminant or the production side of business.

G. Vivek: Can you just highlight the differentiator for us which has been able to give the consistent performance over the last so many quarters and I believe your leadership has played a key role and if you can keep up the good work but off the record's sake and for the new investors like us differentiators will be really helpful.

Manish Gupta: On a lighter note, I would probably say that we are lucky to be in the right industry at the right time. First is the industry is that way very dull and drab industry. It's a slow and steady industry wherein being in branded generic you can't gain something very quickly and also you can't lose something very quickly so that's a positive of this industry. Having said that I think at our end we are a very strong execution team and that's what has made the difference. So it's not about me, it's about the entire management team who have come together. We are a very professionally run organization in that context with promoter not being part of the team in a way, not even at the board level. So, it has been great responsibility on the management team and so far, we have been extremely execution focused. This has largely enabled us to t deliver consistently, partly coming as I said from the industry nature and partly on account of execution focused management team.

Moderator: The next question is from the line of Manoj Shah from Lax Glow Investments.

Manoj Shah: Part of my question has been answered but just wanted, if you can clarify on the growth part of it how would the Carlyle coming in; where do you see the company over next 2-3 years in terms of the revenues whether newer market penetrations, margins as you have just said that will grow by 200 bps YOY for next 2 years and on the new product launches.

Manish Gupta: How Carlyle impacts our business strategy; you please give us about 2 quarters before we can respond to it because the transaction is yet to close. So we still haven't really got a chance to interact with them and redesign the strategy. Give us time till end of the year before we can come out with how the things will look; if at all any different from what we have been alluding to. But on our own we stay confident on the medium-term direction of the company which we have been always communicating.

Manoj Shah: As of now your plans are your top line to grow in what range?

Manish Gupta: We have been alluding towards a mid-teens growth rate in revenues and 150 to 200 bps margin improvement year-on-year in the medium term. This year is an exception, of course not that we know anything about this year. Everyone is nervous about the current year. The things are only evolving, so for the current year we are looking at one quarter at a time, that's the way we have been speaking about.

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

Manish Gupta: Thanks for joining us on the call. The key points that we would like you to take back today are:

- It has been a strong quarter under the challenging circumstances; both our segments API & formulations have performed well

- Emerging markets growth was tepid this quarter, but we expect the numbers to stack up in the second half of the year.
- We have signed a multi-year deal with Zoetis to market and distribute their ruminant portfolio in India
- We are expanding the Vizag facility while the expansion at Bremer has been deferred
- The Carlyle transaction is on track and will close in this quarter
- Finally, In the call last quarter, I had mentioned that we shall take one quarter at a time this year given the environment. While I still maintain the same, I do believe that our performance in Q1 does provide us the impetus to look at both Q2 and rest of the year with greater confidence.

Moderator: Thank you. Ladies and gentlemen on behalf of SeQuent Scientific Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines. Thank you.