“Sequent Scientific Limited
Q1 FY2022 Earnings Conference Call”

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Moderator: Ladies and gentlemen, good day and welcome to the Q1 FY2022 Earnings Conference Call of Sequent Scientific Limited. As a reminder, all participant lines will be in the listen only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on your touchtone phone. 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: A very good morning and thank you for joining us today for Sequent Scientific's Earnings Conference Call, for the Q1 FY2022. Today we have with us Manish Gupta – Sequent Managing Director, Sharat– Joint Managing Director and Tushar– CFO to share the highlights of the business and financials for 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 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 maybe 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 now hand over the call to Manish to make the opening comments.

Manish Gupta: Thank you Abhishek. Good morning friends. A very warm welcome to all of you who have joined us for this Q1 call; joining me on this call are Sharat Narasapur, our Joint Managing Director as well as Tushar Mistry, our CFO.

We are meeting in quick succession this time as we had met just about 40 days back. So, my address will be short and focus on some key highlights for the quarter and also the strategy for the way ahead.

Q1 has been one of the most challenging operating quarters as we saw multiple challenges right from muted demand, inflated cost structures across businesses as well as significant execution challenges. Overall, in that context, the performance in this quarter was a bit of a mixed bag for us. While formulation business grew about 15% on a constant currency basis, there was a decline in API business after many quarters of consistent growth. We closed the quarter with revenues of Rs. 3200 million or Rs. 320 Crores, which broadly translated in a growth of 9% in constant currency terms. This is slightly lower than where we would have liked to be at this stage.

The overhang of costs all-around also impacted our profitability with EBITDA pre-ESOP charges being about 20% lower at Rs. 358 million or about Rs.36 Crores. Tushar will cover the financials in greater detail in his remarks.

Coming to the respective business segments, the growth of 15% in formulations was primarily led by continuing outperformance in India and Latin American markets primarily Brazil. Our India business continues to do well on the back of strong outperformance in the cattle business as well as recovery in the poultry side of the business. Brazil also recorded strong growth driven by recent launches. While Turkey performed ahead of the markets, the depreciation in the Turkish Lira took away all of that growth. Our performance in Spain dragged our European performance even as Sweden and Benelux did well. We expect a recovery in Spain starting this quarter i.e. Q2 which should put our largest region back on the growth track.

API as I mentioned was muted this quarter. This was primarily due to the lower offtake by some customers along with operational challenges at both our end as well as our supply chain partners.

As I had mentioned in the last call, we had more COVID cases this time in April and May as compared to the entire 12-month period before that. An equal number of employees had to be quarantined due to COVID in their families. We also suffered two unfortunate casualties; however, the situation has been in control since June, and we also draw comfort from the fact that more or less our entire eligible workforce is now vaccinated with at least one dose.

Notwithstanding the numbers, we continue to move in the right strategic direction in terms of quality of business with an ever-increasing contribution of our regulated markets business, which now stands at 76% for APIs. We commissioned the R&D pilot plant as well as an additional cleanroom at Vizag, leading to a ~20% increase in capacity during the quarter. We expect a strong recovery in our API business in the second half of the current year.

There have been some significant strategic developments on the formulations front in line with our blueprint for Sequent 2.0. I am pleased to announce that we have now launched the Pet division in India with 8 Headquarters. I am also pleased to welcome Alexis Goux into the organization as Vice-President, Commercial to spearhead our formulations business. Alexis brings in over 20 years of experience with leading companies like Virbac and Ceva, having lead businesses in multiple geographies including Europe, Latin America as well as Southeast Asia. His last role or his most recent role was with Virbac where he was responsible for the global marketing department on food-producing animals. Based in Barcelona, Alexis will drive our business in key markets of Europe, Turkey, and Latin America, including global marketing, especially for our value-added R&D portfolio under development, as well as entry into key new markets of the UK, Germany, and South-East Asia.

Overall, while we had a slower start to the year than our expectations, we stay confident and on track of achieving our financial and strategic objectives for the year. I would now like to close here and hand it over to Tushar for his comments.

Tushar Mistry: Thank you, Manish, and good morning all. While Manish has given insights on the operational performance, let me discuss the financial performance for the quarter.

Our revenues for the quarter have grown by 8.9% year-on-year on a constant currency basis to Rs. 3.2 billion. Formulation business continues to drive the growth, with strong 15% growth year-on-year, supported by stellar growth momentum in India, LATAM, and Brazil. European business continues to remain muted due to subdued performance in Spain whereas Turkey's business was affected due to adverse currency movement.

Overall, we also saw input cost price pressures for both API and Formulation, as also for some specific operating costs like furnace oil as well as logistics costs. EBITDA excluding ESOP costs stood at Rs. 358 million, while the reported EBITDA came in at Rs. 202 million after considering the ESOP cost of Rs.156 million. This ESOP cost as has been explained earlier is a non-cash cost to account for the recent grant of ESOPs to key employees with almost 50% of the impact coming in the first 12 months.

Further, the EBITDA is also after considering the additional cost of Rs. 58 million incurred during the quarter as spelled out in slide 13 of the investor deck. What we also missed this quarter was other operating income which was almost Rs. 29 million last year as RoDTEP rates are yet to be announced by the authorities.

On the balance sheet side, we witnessed a slight increase in the working capital as we built strategic stocks of some of our key products in line with our business plans. We have also consolidated our minority interest partners in Turkey, Belgium, and the Netherlands during the last fiscal year, and should be completing minority stake buyout in Brazil in the current quarter.

I would like to conclude my remarks by stating that this quarter has been challenging, but we stay extremely focused in terms of execution on both business and cost fronts, even as we continue to invest in and pursue our strategic objectives around Sequent 2.0. Thank you and we can now open the floor for Q&A.

Abhishek Singhal: So, Rutuja can we take the Q&A, please?

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Satwik Jain from RH Perennial Fund. Please go ahead.

Satwik Jain: Thank you for the opportunity. So, there was a note in the audited financial statement, there was some revenue recognition which was overstated in the last quarter. So, could you through some light on it because it was of a decent size of around Rs.50 Crores of profitability?

Manish Gupta: Rs.50 Crores of profitability, I do not know where you are getting these numbers but if you recollect in the last call, I had mentioned that we detected certain instances wherein revenues for certain sales transactions were recognized earlier than those allowed by the group revenue recognition policy. It is in light of those that the revenues and the P&L have been restated. So, these are timing issues pertaining to the API shipments in terms of where the revenue should be recognized. There were certain gaps in the documentation, and on account of that, after a complete review, we have undertaken a correction of the entire process of recognition as also the impact of the same on P&L. Tushar if you want to add anything?

Tushar Mistry: No. That is right.

Satwik Jain: Most of it would have been done, so there would be no such things like in the further quarters that is what I am assuming?

Manish Gupta: If you look at the notes of last financial year again, we had spelled out the complete implication for each of the quarters of the previous year. There is no continuing implication because all of it was corrected within the year, and they were within the year corrections between the quarters. So, Q1 sales went into Q2 in a way, therefore if you look at the disclosure or the notes of the last financials, all adjustments have been detailed out. There is no continuing impact, everything has been resolved within the last financial year.

Satwik Jain: Perfect. Thank you so much.

Moderator: Thank you. The next question is from the line of Jolyon Loo from Sixteenth Street Capital. Please go ahead.

Jolyon Loo: Thanks for the call. I have two questions I think first is a small observation and wanted your commentary - certain major selling of the APIs, and you declare very aggressive restructuring targets, I think it might be the cause of our supply chain rationalization maybe you can give us more color around this, and what gives us the confidence that demand should return in second half of the year for API? Thanks, that is the first question.

Manish Gupta: I am not sure whether we could understand the question properly, but I am assuming you are referring to the impact of COVID on operations, or is it something else?

Jolyon Loo: I am talking more of the supply chain rationalization that was related to API so we may get more details or color around that?

Manish Gupta: Last year during the first wave of COVID around March and April there was enormous uncertainty in the marketplace. We believe at that time many companies secured a certain level of inventories to ensure steady plant operations. Once things stabilized, the purchases came down, which is what we believe has affected our API side of the business. So, there must have been some inventory built up undertaken by our customers in Q1 and Q2 of last year given the uncertainty. That rationalization is occurring at this point leading to a slowdown in procurement. I believe the demand will be back to normal levels probably in the second half, if not earlier. Does that answer?

Jolyon Loo: Sure, Okay, and just in terms of the ESOP what is the nature of this, is this treated as a one off maybe if you can give more details around that please?

Manish Gupta: Yes, so this is as a part of the change of control that occurred in the company last year. The new promoters had rolled out a new ESOP scheme. It underwent a process of approval through the shareholders. Consequently, from the time they rolled out to the time of approval, there was a significant change in the stock, and therefore while the vesting price of these ESOPs was in line with the entry price of Carlyle, but by the time the final approval was received, there was a price difference in that period. The fair market value of these ESOPs is calculated by using the Black-Scholes model and difference of fair market value versus vesting price, those charges are to be booked in the P&L. These are non-cash charges and the way the model works is, given that these ESOPs vest over five years, almost 50% of the cost get booked in the first year or the first 12 months. So, that is the implication of the ESOP cost that we have booked during the current quarter. It started from March 2021, so one month cost was booked in the previous quarter, the current quarter reflects the peak cost which is three months of cost, and it will continue till February of next year and thereafter it will start coming down unless new ESOPs are also granted to new employees.

Jolyon Loo: Okay, that is very clear. Thank you so much.

Moderator: Thank you. The next question is from the line of Vishal Manchanda from Nirmal Bang Institution Equities. Please go ahead.

Vishal Manchanda: Good morning and thanks for the opportunity. This is related to the API business can we expect on a full year basis would you grow over your FY2021 base or could that be difficult to achieve?

Manish Gupta: Certainly, there will be growth over FY2021, but right now guiding to what kind of growth is slightly difficult, but we are hoping that it should not be very different from the past.

Vishal Manchanda: Okay, so we have been growing around 20% - 25%, so can we look at that kind of growth number?

Manish Gupta: No, I think even if you look at last year it was a mid-teens growth on the API side of business, and we certainly are working towards achieving that. I am not committing that we should achieve that, but we certainly have clear plans on how to go back to those levels of growth. I do believe that the quarter is more of an anomaly and not a trend.

Vishal Manchanda: Got it Sir. On the Turkey business, it has sharply corrected as you pointed out there are supply challenges and challenges on the customer front, but are there spread of level disruptions, demand disruptions. So, can we see kind of higher demand in subsequent quarter to make up for what we have lost in first quarter?

Manish Gupta: This is pertaining to formulations, is that right?

Vishal Manchanda: Yes, formulations business.

Manish Gupta: Now, formulations I do not think we have lost too much except in Turkey, wherein we had operating challenges. Our order book is full and the order book is already in line with the business plan for the year. So, we have no issues in terms of achieving what we have envisaged for Turkey. It is all about what we missed out in the previous quarter will be covered up within the rest of the year, because the order books are already in place.

Vishal Manchanda: Great Sir. And the new tablets facility that has come up in Turkey, would that also contribute during the year?

Manish Gupta: For within Turkey? Yes, it is going to contribute but what we have highlighted is now we have EUGMP approval for the tablet facility. So, we will be initiating filings for the EU which is going to be more valuable, but it will still take some time to fructify in terms of commercial numbers.

Vishal Manchanda: Right, but in Turkey this can start contributing to the current year?

Manish Gupta: Absolutely.

Vishal Manchanda: Any colour on what kind of peak revenues we can look to generate maybe four years or five years down the line from this facility?

Manish Gupta: No, it is not a new facility, it is an additional line per se. We have been growing at 20% plus in Turkey and we continue to maintain the same growth rate in terms of our expectations. What we are adding in Turkey is export business which is over and above the Turkish growth rates and that is something that will get facilitated by the approvals we received. Difficult to put a number but it is a part of our strategy to develop Turkey as a manufacturing hub for all markets other than US. Vishal, you would also kind of appreciate that we have multi-capability in Turkey in terms of manufacturing and almost eight or nine manufacturing lines, most of which are sterile manufacturing. So that makes it a very strong manufacturing hub for us.

Vishal Manchanda: Thank you, Sir. That's all from my side.

Moderator: Thank you. The next question is from the line of Bharat Sheth from Quest Investments. Please go ahead.

Bharat Sheth: Good morning. Manish ji, can you add some more color on your opening remark where you said that some formulations strategy has been already in place. So, how will that drive, that is one. Second, our injectable business, if you can give some details on what stage we are at for German plant and when do we start supplying to US, and third on the Vizag facility supplying to regulated markets, particularly USA and the FDA inspection stage?

Manish Gupta: Let me first start with the formulation strategy of Sequent 2.0. As we have spelt out last time, fundamentally it is a focused strategy – sterile would be our core focus area of domain in terms of product development and manufacturing and to that extent, we are looking to expand both our Germany facility primarily for the US and also the Turkish facility for rest of the world, including EU. You would also recollect that we had spelt out the markets we have chosen to expand, which includes US, UK, and Germany for front-ending in Europe along with select Southeast Asian markets, Indonesia and Vietnam to be specific, for footprint expansion. We had also decided to dive deeper into the three key strategic markets of Brazil, Turkey, and India including a foray into the pet animal segment in these markets. So, that was a very clearly articulated strategy for Sequent 2.0. To that extent, what we have already kind of initiated in this quarter is that we have launched the Pet division in India. We have started work in Germany for the project expansion for US FDA standards. This is not only for US FDA standards but also about capacity built up because volumes in the US are very, very different and the pack sizes in the US are very, very different from the rest of the world. Everything in the US is much bigger as we are all aware. So, the work in the German facility has been already started. We have also initiated or expanded our entire R&D framework for formulations including value-added generics. I would not be able to give more details on that for strategic reasons. In that context, we are also fast-tracking new GMP approvals for Turkey, including the recent renewals because clearly, we are building Turkey as a global manufacturing hub for all the other markets other than the US. And finally, I think your last question was about the API side of the business and the Vizag plant. Vizag has already been US FDA approved since 2016 and it has been also re-inspected and re-approved in 2018. So, our entire API strategy has been built around that. We continue to stay approved and stay the only US FDA-approved veterinary API facility from India. What has slightly slowed down is validations at the customer end because of COVID. As an API supplier, finally, the customer has to validate our APIs in their formulations before they can start using them. Last 12 months, as you would understand, every company has suffered on execution, so have our customers. To some extent, both on account of rationalization of their supply chain, and some validations delays at the customer end, you could see a muted API demand in the current quarter, however, we are very confident that the API business will bounce back fairly strongly in the second half of the year.

Bharat Sheth: Okay, so when do we expect from German supply of the injectable or sterile business to start delivering in terms of timeframe?

Manish Gupta: I believe it will be FY2024 before the first commercialization occurs in the US because while we have already made our first filing for the US, in the current scenario you would expect that FDA may not visit for the next 12 months to 18 months.

Bharat Sheth: Because this US FDA is not visiting or this 2024 also because of the validation and getting approval for whatever project we have filed?

Manish Gupta: No, this is predominantly for the US FDA not visiting. Right now, FDA is not traveling, and animal health will obviously not have that high a priority vis-à-vis the other plant that they have to audit once they start visiting. So, on account of that, we believe that we will be slightly later in the queue in terms of their priority.

Bharat Sheth: Is that a fair assumption that with API bouncing back strongly and formulations we are already growing, 15% of course you said it is in constant currency, despite there was a growth in Turkey in constant currency there is a decline. So, how in rupee value overall company growth we can look forward?

Manish Gupta: Bharat Bhai, you will not see much difference between a constant currency growth and the reported growth as well. So, while formulations grew 15.3% on constant currency, even the reported currency growth is 14.7%, so it is not very different. Collective growth is about 9% for the organization that is because of the slight decline on the API side of the business, but as API business recovers, we believe that the overall growth will not be very different from the growth that we delivered in the last few years for the overall business.

Bharat Sheth: Great.

Moderator: Thank you. The next question is from the line of V. P. Rajesh from Banyan Capital. Please go ahead.

V P Rajesh: Good morning, Tushar and Manish. Manish, just trying to understand with API a little bit better, was it a supply chain issue or was it the demand issue or was it a logistics issue in this quarter, if you can just give more colour on that?

Tushar Mistry: It is a bit of both and I will have my colleague, Sharat to explain the supply side challenges that we had, but there was a subdued demand as I mentioned. It is coming from the inventory rationalization at the customer level and there were also execution issues because whatever demand we had also we could not service the demand due to our execution challenges and Sharat can explain a little more about the execution challenges given the quarter that we had.

Sharat Narasapur: Basically, on the supply side the situation which we faced was an industry-wide phenomenon, predominantly driven by uncertainties during COVID lockdowns. So, we also depend on several of our CMOs for the supply of inputs, late-stage intermediates for making APIs. They also did undergo the same challenges, therefore there was a muted supply, plus there was pressure on as Tushar mentioned on the cost side. So, availability, as well as cost, hindered the ability to execute properly.

V P Rajesh: I see, a few questions on the options side, is it typical that we would be able to write off 50% of these ESOP costs in the first 12 months itself, I would think they would have gone over the period of vesting schedule?

Tushar Mistry: Yes, Rajesh it goes as per the vesting period for each year, so the way it works - the first year you have the expenses sitting for the first vesting, that is happening plus all the other four vesting periods that is happening. Second-year it will only hit for the four vestings, so earlier it is only for three vestings that are happening. That way the maximum impact is in the first year and then it keeps on going down over a period of time over the vesting period.

Manish Gupta: Rajesh, if I explain it a little more since it vests over five years, 20% is in the first year or at the end of the first year. So, the entire cost of the first vesting will hit in the first year itself. The second-year vesting 50% of the cost will hit in the first year and 50% in the second year. In the third year of vesting, a third of the cost will hit in the first year itself. So, effectively it becomes 100% of year one vesting plus 50% of year two vesting plus 33% of year three vesting plus 25%, and so on. So, that way if you add up, the first-year impact is the maximum.

V P Rajesh: Understood, then the dilution is the same as what you had indicated previously right at the shareholding base there is no change beyond that like in terms of number of issues in terms of share.

Manish Gupta: Absolutely.

V P Rajesh: Thank you and all the best.

Moderator: Thank you. The next question is from the line of Raghav Soni from Deloitte. Please go ahead.

Raghav Soni: Sir, first of all good morning. Sir, just want to get clarity on note number 7, although you discussed that but was it a one-time event or it is going to take hit in subsequent events also, subsequent quarters? That is the first question. Sir can you give the guidance on margin even before the ESOP hit it was very low, it was close to 11.8, can your guidance on the margins? That is it from my end, Sir.

Manish Gupta: I think I clearly spelt this out whatever was the impact was limited to last year and within the quarters of last year, there was no impact even in Q4 of last year but within the quarters there was a kind of re-adjustment of P&L, all of which was disclosed in the annual filing. So, does that answer your first part of the question?

Raghav Soni: Yes, Sir it answers the first part and second part on the guidance, Sir?

Manish Gupta: Second part on the guidance. I will split this into two parts of business one is the operating part and second is the built up of Sequent 2.0. On the first part of business, we stay very confident of delivering if not better but at least similar margins as last year. From the operations front there may be some mismatch within the quarters simply because there is a lag between cost and by that time you can start recovering or pass on to the customers, there is always some lag. There is a second part of that which is the cost built up for the future Sequent 2.0. Now that is something which is still work-in-progress. There may be incremental costs coming on R&D front, on employees front and as we build up the organization, that is something difficult for me to guide you at this point of time and therefore, what you would have seen is we have brought in these on slide 13 in our investor deck, which we will keep disclosing. We will not adjust the margins or we are not calling them exceptionals or whatever, they are part of our strategy. But we will certainly spell it out for you to take a view on those additional costs that we would have built up during the quarter or the year.

Raghav Soni: Thanks. Just want to clarify these questions are asked in my personal capacity as a retail investor. Thank you very much, Sir. My questions have been addressed.

Moderator: Thank you. The next question is from the line of Hardik Vora from Union Mutual Fund. Please go ahead.

Hardik Vora: Good morning everyone and thank you for this opportunity. Actually, my question is in line with what the earlier participant asked. So the margin guidance that you gave that we would come back to at least the last year's level, this guidance is by when will we touch that level?

Manish Gupta: What I am suggesting, while it is very difficult to guide on a quarter-to-quarter basis I think at an operational level, our EBITDA margins will not be any inferior to what we showed last year by the end of the year. Certainly, a lot of this growth or improvement will be back ended because you would understand or appreciate that the incremental contribution of API business in margins is much superior, given that there are no sales and marketing costs related to a B2B business. So, certainly the catch up will be more back ended, not front ended but at the end of the year, I do believe, and I have fair confidence to say that our EBITDA margins from operations will not be very different from where we ended last year.

Hardik Vora: Okay, so now if I remove the one-off cost that you have highlighted in the slide 13 and given the ESOP cost it seems total cost seems to be growing at the pace of between 12% and 15% and our revenue historically have grown at that level, the consistent growth rate that we have just seen in this one blip now coming. Also, the question is before this ESOP plan was announced and before we had a conversation you had guided it as a 2x revenue growth potential in five years from FY2020 as the base. So, I am just trying guess that that still holds right that in a 20% EBITDA margin potential within five years. This is just some short-term pressures that we are seeing in the profitability otherwise going forward that strategy is not changing.

Manish Gupta: You are absolutely right. In fact, obviously, as I said in Sequent 2.0 our aim would be to better that and not be satisfied with that.

Hardik Vora: Manish Sir I am sorry; I actually missed the beginning part of the call. So, these costs that have highlighted in slide number 13 while one of them is clearly indicated I do not understand the nature of the rest of them, what are the new initiative and one-off expenses. So, if you could just highlight what they are?

Manish Gupta: There are multiple new initiatives currently happening in the organization, both on strategic front, product selection front, R&D front as also on the processes and the systems of the organization because we are obviously scaling up and preparing for a much larger organization. So, all the new initiative costs are pertaining to that. There are obviously also inorganic initiatives that company keeps looking at, and there are costs that come on account of that. The one offs and exceptionals are on the other side, which are sometimes there as past expenses and all that, so that is coming as one offs the costs. Tushar, you have better colour on the one off and exceptional?

Tushar Mistry: Yes, so some of these costs pertain to last year, which have come in the current year, like in the case where one of the service providers has charged us in last year for the entire period for the past costs. Also, in some of the geographies, we have taken certain provisions for certain inventories and all which are coming here as one offs, so all that is built up into this one off and exceptional.

Hardik Vora: Understood Sir, of these the non-recurring ones are the 7 million and the 23 million right, 28.5 million as such may recur for some time before they start getting absorbed in the incremental basis?

Manish Gupta: Yes, but we do believe those will start dipping as you would have seen that they are already lower than Q4.

Hardik Vora: Okay, even an absolute dip going forward?

Manish Gupta: That is correct.

Hardik Vora: One final if I can squeeze in, the capex plan has that been over the last two quarter any sense on that front?

Manish Gupta: On what front?

Hardik Vora: Capex, the capital expenditure?

Manish Gupta: I think we stay in line with what we have guided.

Hardik Vora: Thank you for that. If I have more questions, I will join back. Thank you so much and all the best for the future.

Moderator: Thank you. The next question is from the line of Vikas Jain from Financial Quotient. Please go ahead.

Vikas Jain: Good morning Mr. Gupta and Mr. Tushar. Though my questions had already been taken up by the earlier participants, I do not have my question now to be answered. But I wish you all the best for the upcoming quarter and hope the guidance works and we perhaps see a better margins and better profitability in times to come. Thank you. You all have a good day.

Manish Gupta: Thank you.

Moderator: Thank you. The next question is from the line of Rishabh Kochar from Edelweiss. Please go ahead.

Rishabh Kochar: Good morning everyone. So, I have two questions, firstly on the European side - they have launched three products last year. So, there is dip in the overall performance, so can you throw more colors on that?

Manish Gupta: Sorry, come again?

Rishabh Kochar: On the European business we have launched three products last year and we saw dip, so can you throw some light on that?

Manish Gupta: We are not able to hear you properly. Can you repeat or can you take the mike closer to you?

Rishabh Kochar: Sir, European side of the business we have launched three products last year despite that there is a dip in the overall performance. So, can you throw more light on the overall performance what is impacting the European business?

Manish Gupta: In Europe basically we are present in three geographies or three prominent areas, one is Spain which is our largest business followed by Benelux and finally Sweden. As I eluded in my opening remarks, both Benelux and Sweden have done well for us and grown ahead of the market during this quarter. Where we have suffered is in Spain, which saw reasonable, about 7% decline in business. Now, while we had new launches, we also suffered from two other areas in Spain, one is there was hyper competition in select range of products, the oral powder products and second is we also had certain supply chain issues from our other third-party suppliers in Spain. So, collective impact of that was that we had a decline of about 7% in Spain which led to the overall decline in Europe in spite of the new launches. Having said that a lot of those situations have been corrected, we have now started receiving supplies from our third-party suppliers as also our own powder sales has started picking up so we do believe Q2 you will see a reasonable recovery as far as our European operations are concerned.

Rishabh Kochar: Sir, should we expect that the European segment would grow higher than the industry level going forward?

Manish Gupta: As of now, we do believe we should grow faster than the industry for rest of the year in Europe. You have to be aware that European growth rates are always muted, compared to the Rest of the World. So, it will still be a single digit number.

Rishabh Kochar: Thank you Sir, the second question is on the API side. Sir, long-term outlook for the API was 20% CAGR. Given that there is some demand rationalization, will that impact the overall thesis for the long-term, or is it intact?

Manish Gupta: In the long-term, I do not think there is need to make any changes. What has happened in this quarter and probably will continue for the first half is more transitory. The long-term strategy stays intact. We do expect the API business to start recovering from second half and accelerate going forward because we have not lost any business, there has been only deferment, both caused by inventory built either at customer end or delays in validation at their end. There has been no loss of business, so therefore our guidance remains intact for the medium-term to long-term.

Rishabh Kochar: Okay, Sir if I may ask one more question. So, given that there is rise in COVID cases in China and if supply disruptions happen once again what would be your guidance going forward on that?

Manish Gupta: It is very difficult to give guidance around COVID honestly. So, I would stay away from that. I do not think anyone of us was ready for wave-2, or rather the intensity of wave-2. First time I must admit as a leader there was a sense of helplessness at some point of time, because otherwise our firm belief was that as a corporate, we will be able to help all our employees and find solutions, but this was the first time wherein even as a corporate and with all the connects we had as corporate, there was little we could do given the intensity that happened. Having said that, I do believe that the world is better prepared including ourselves. You would have also seen that there is an inventory built up that we have undertaken at our own end. So, we have taken a lot of care in terms of how to secure our business. Having said that, there are no fool proof mechanisms, certain business risk and uncertainty we have to live with, but whatever have been the learnings of the past have been incorporated in our business model, including some short-term practical decisions around inventory.

Rishabh Kochar: Thank you so much. All the best for the future.

Moderator: Thank you. The next question is from line of Rushabh Sharedalal from Pravin Ratilal Share and Stockbrokers Limited. Please go ahead.

Rushabh Sharedalal: Thanks for the opportunity. Just a small question on the operating expense part, just pardon me if my question is repeated. So, operating expense has increased by roughly Rs.14 Crores odd in this quarter. So, if you can just guide me as to what is the reason for this increase?

Tushar Mistry: If you refer to slide 13, part of the explanation is given in slide 13 for that wherein there are costs which are incurred towards these initiatives. There is COVID death compensation and there is a certain one offs and exceptional cost which are sitting in the operating expenses, others are in line with our business expansion.

Manish Gupta: One thing also you have to bear in mind is to some extent costs in Q1 last year were slightly understated because that was the peak of first wave of COVID and there was a complete lockdown, so many operating costs would not have been incurred, especially on sales and marketing front. So, to some extent there was a bit of an understatement of Q1 cost from a normal running operations basis.

Rushabh Sharedalal: Correct me if my understanding is wrong but if in the coming quarters, we will not be having such kind of one offs at these exceptional costs and some of the new initiatives and also the fact that the new ESOP scheme that you have given to the Carlyle due to this transfer. So, in the coming quarters, we would be seeing higher earnings, is my understanding correct or are some of the costs going to be incurred in the coming quarters also?

Manish Gupta: Certainly your understanding is correct. It has certainly improved earning going forward. This quarter has been exception, both on the cost front and also on the revenue front. So, if you look at our overall revenue, this is much lower than what we have been normally delivering, which is closer to Rs.3.5 billion per quarter. This has been lower. So, as the revenues recover, and also some of the one offs go away, you will certainly see a reasonable increase on the operating performance side.

Rushabh Sharedalal: Right, and just a small question if I may squeeze in, we as a group had even partnered with Zoetis to sell some of the drugs as we are in the distribution of those drugs. So, presently I do understand that it does not contribute significantly but in the coming quarters let us say four, five quarters down the line what kind of an impact do you see in the revenue from operations from this particular area of business or is it not much?

Manish Gupta: No, see our current arrangement with Zoetis is limited to India and is limited to selected range of products. So, unless the arrangement expands to either additional products or to addition geographies the impact will continue to be minimal. It is material from an India perspective but at an overall context of the organization it is not significant.

Moderator: Thank you. The next question is from the line of Vishal Manchanda from Nirmal Bang Institutional Equities. Please go ahead.

Vishal Manchanda: Thanks for the opportunity. Sir, with respect to the Pet division initiatives could you give some colour on whether it has to do with nutritional aspect or it has to do with therapeutics. So, are you venturing into prescription drugs or you would look at kind of nutritional products for pets?

Manish Gupta: We are fundamentally a pharmaceutical company, and our focus would always be the therapeutics or the pharmaceutical or prescription drugs, doctor led business. We are not getting into pure nutritional side of business.

Vishal Manchanda: You have a bouquet of drugs that you would start selling immediately?

Manish Gupta: That is correct. So we have launched the division with eight headquarters and four products. Obviously, we launched at the peak of COVID in a way, so the customer connects are initially difficult. But as we gain more and more confidence, we will be adding more territories as also adding more products in that business.

Vishal Manchanda: Sir, could this require a larger field force effort versus what we typically do for veterinary animals?

Manish Gupta: No, not at all. In fact, it requires much smaller field force because it is still a very urban business. So, typically you start with category A cities and gradually you may go to comparatively smaller towns, but you will never go to, where the rest of the veterinary business is, in extremely rural areas. It is a different skill set, and different kind of people we need to hire in pet vis-à-vis the other veterinary parts of business.

Vishal Manchanda: Okay, and sir if we look at the competition would we see this larger names Zoetis, Elanco in this category or there are also smaller Indian domestic names that you would compete with?

Manish Gupta: No, I think more or less, it will not be very different from what we are competing within the rest of the business. So, there are obviously all the MNC's and there are a couple of Indian companies as well.

Vishal Manchanda: Okay, so it would be difficult to launch niche products in this category so you would have identified high growth therapy areas and probably looking at those?

Manish Gupta: Yes, and we are also looking to leverage our own R&D pipeline here, so we have a multiple strength here not only we have our own R&D pipeline we also have lot of products outside India which we are looking to bring in, many of which are not available in India at this point of time. I think we are very well placed as far as Pet business in India is concerned, of course it will take time to build up.

Vishal Manchanda: Got it, Sir. Thanks very much.

Moderator: Thank you. The next question is from the line of Karthi Keyan from Suyash Advisors. Please go ahead.

Karthi Keyan: Good morning, thanks. Couple of things initially if you could deliberate the topic of APIs just wanted to understand what kind of schedules would you have in terms of advance notice meaning is there a predefined schedule or will it be, how exactly would it work so as things stand today how far ahead are you able to look in terms of scheduling of shipments?

Manish Gupta: I did not understand your question can you repeat?

Karthi Keyan: I was asking you on the API side would there be a predefined schedule for shipments and if yes, how far ahead are the schedules defined?

Manish Gupta: I think this happens in most businesses, and I do not think our API business is any exception. There are always two buckets to API business. One is part of businesses which are driven by long-term contracts. These are multiyear contracts which come with the forecast, and the forecast that is there will be annual forecast with a firm forecast or firm commitment for one quarter or two quarters. So, that would be roughly about more than 50% of our business of that kind, and then there are other regulated business, especially with the generic companies, they do not give long-term commitments, but they are committed to buy from you given that you are part of their regulatory filing. So, another 25% of our business will be on that account and finally 25% odd of our entire business would be what I would call as more spot or unregulated market customers wherein these customers have not much regulatory requirement and they will buy on a need basis. So, all in all I think where I am coming from is there is a fair degree of certainty about 75% to 80% of the business and what you always are on a lookout for to fill up is the last 20%-25% of the business which comes from more of spot kind of customers.

Karthi Keyan: Right and you would say that the shortfall has been on category one or category one and category two or all three categories?

Manish Gupta: No, it will be more on category one and category two which is more coming from timing as I mentioned.

Kirthi Keyan: Right, the second part that I wanted to understand is you talked about profitability coming back obviously I am including one off, when you said that did you mean on a quarterly basis or on an annualized basis?

Manish Gupta: Quarterly is a very difficult game to play. I would always request to insist on evaluating on an annual basis.

Karthi Keyan: No, so when you said your profitability will come back to at least last year's levels did you say that on a full year revenue base your profitability will be restored, or did you mean that for the quarter the profitability will come back to last year levels?

Manish Gupta: No, I am talking for the full year numbers when they are displayed or disclosed, it will not be very different from where we had been last year.

Karthi Keyan: That was a steep decline actually so that is impressive.

Manish Gupta: There was a steep decline also this quarter, so you have to understand that businesses like us are highly fixed cost intensive business, so moment if the sales is not in line with what you envisage, then the margins get impacted, and same is on the other side, the moment sales recover, the margins expand fairly rapidly.

Karthi Keyan: Fair, one last quick question I am sorry. On the Pet business side, this does not lead to any kind of conflict with your partnership, like of Zoetis, in fact that you are launching some Pet product even if it can be say relatively non-core market?

Manish Gupta: No, not at all. In the pharmaceutical industry I think this is a general trend we all compete and also cooperate.

Karthi Keyan: Correct, but I was just trying to understand that you are partnering with them in India for example I was asking in this question.

Manish Gupta: Not at all.

Karthi Keyan: Thank you so much. Thank you and best wishes.

Moderator: Thank you. Ladies and gentlemen this will be the last question for today, which is from the line of Rajamohan Vaikuntaraman a Professional Investor. Please go ahead.

Rajamohan V: Thank you for the opportunity. Manish previously to a question in one of the previous calls on reaching the top ten animal health manufacturers roughly about $500 million in revenues you had indicated to the consulting firms coming back by the middle of this year to give you a broad objective guidance. Could you give some objective outlook and also based on Carlyle's initiative is this $500 million target as say four-five-year kind of purview that you reach that scale say by 2025–2026?

Manish Gupta: So, Rajamohan I think this will entail a slightly prolonged conversation, so can we take it offline, and I will be happy to talk to you at your convenience, because it entails a fairly lengthy answer.

Rajamohan V: Sure, the second part was you have indicated to the upfront investments like Carlyle that will happen in the next one or two years, broadly would it be largely on the formulation side or on the API side and does this have the possibility of pushing our revenue growth by upskilling and up scaling to beyond the mid-teens growth that you have indicated to?

Manish Gupta: You are absolutely right. First, most of the additional investments will occur on the formulations side of business, whether it is inorganic acquisitions or opportunities, whether it is capability built up both in terms of market footprints, as also skill sets, as also on the R&D side of business. So, we will be moving from pure generics to speciality generic kind of products, with of course balancing the risk and reward ratios in that profile. So, that is one part of it, certainly it should boost up the business in the later part of the strategic plan. It will have no impact because nothing in pharmaceutical other than acquisitions can reflect in your numbers in the first two years. But I am very, very confident that whatever initiatives we are working on will translate into faster growth for the business from what we had envisaged in the past in the last two years of our business plans.

Rajamohan V: So, this essentially would be playing out from say FY2024?

Manish Gupta: That is correct.

Rajamohan V: One final question was Carlyle's current comfort with that has taken the company are they comfortable or are they still inclined to increase their stake further higher up obviously I think it is a sensitive question for you to answer but still some subjective opinion on this?

Manish Gupta: My personal opinion is Carlyle would love to own 100% but clearly that is not feasible, but I would rather encourage you to ask this question to Carlyle.

Rajamohan V: Okay, Manish thank you very much and best wishes for the future.

Moderator: Thank you. Ladies and gentlemen, as this was the last question for today. I would now like to hand the conference over to the management for closing comments.

Manish Gupta: Thank you very much for your questions and we do hope we have been able to answer most of your queries. While the performance in the recent quarter was challenging, our continued belief in our unique and well-diversified business model as well as our execution capabilities give us confidence to deliver consistent growth and business outcomes even as we invest in new business segments, geographies, people, and assets to realize our vision for Sequent 2.0. I would also like to thank all our stakeholders for their continued support throughout the difficult times of COVID and otherwise. Thank you once again and we can now close the call. Thank you.

Moderator: Thank you. On behalf of Sequent Scientific Limited that concludes this conference. Thank you all for joining us. You may now disconnect your lines.