"IPCA Laboratories Limited
Q2 FY2022 Earnings Conference Call"

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ANALYST: MR. NITIN AGARWAL – DAM CAPITAL ADVISORS LIMITED

MANAGEMENT: MR. A.K. JAIN - JOINT MANAGING DIRECTOR – IPCA LABORATORIES LIMITED

Moderator: Ladies and gentlemen, good day and welcome to Q2 FY2022 Earnings Conference Call of IPCA Laboratories Limited hosted by DAM Capital Advisors. 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. Nitin Agarwal from DAM Capital. Thank you and over to you Sir!

Nitin Agarwal: Good morning everyone and very warm welcome to IPCA Labs Q2 FY2022 post results earnings call hosted by Dam Capital Advisors. On the call today we have representing IPCA management, Mr. A.K. Jain, Joint Managing Director and Mr. Harish Kamath Senior VP Legal and Company Secretary. I hand over the call to Mr. Jain to make some opening comments and then we will leave the floor open for questions. Mr. Jain please go ahead Sir!

A.K. Jain: Thanks Nitin and DAM Capital Advisors for organizing this call. Good afternoon to all participants and thanks for taking our time and joining us for Q2 FY2022 earning call. Today's earning calls and discussions and answer given may include some forward looking statement based on our current business expectations that may be viewed in conjunction with risk that pharmaceutical business faces. Our actual or future financial performance may differ from what is being projected or perceived. You may use your own judgment on the information given during this call.

Our business recorded a strong performance for the quarter. Domestic formulation business delivered 30% growth for the quarter and on improved base of Q2 last year from Rs.535 Crores to almost around Rs.698 Crores. Domestic API business delivered around 25% growth for the quarter from Rs.67 Crores to almost around Rs.82 Crores. Export business of formulations and API declined during the quarter, but excluding the exceptional business of last year Q2, the branded generic business has grown by almost around 17%, generic formulation business has grown by around 15% and institutional business declined by around 23% and API business at around Rs.287 Crores has declined by around 7%. Some of these businesses also impacted due to the delayed availability of containers and shipments.

Some of the key highlights of our domestic formulation business, domestic market our ranking has improved to 16th in the month of September, our MAT ranking has also improved to our 19th in September and currently it is around 18 as per IQVIA. We have improved our market share to almost around 1.75% in mid-September 2021. Most of our therapeutic areas have delivered a strong performance. Our internal sales growth in key therapeutic areas if you look at the pain segment excluding Hydroxychloroquine, it is almost around 32% growth including Hydroxychloroquine where we had the significant business from institutions last year has delivered around 24% growth overall. Cardiovascular has delivered almost around 13% growth, antibacterials around 37% growth, cough and cold preparation almost doubled practically 95% growth, dermatology almost around 52% growth, CNS 30% growth, neuro almost around 46% growth and anti-malarials has also delivered almost around 75%. The therapeutic contributions of key therapies in domestic market, pain is now almost around 48% of our business, cardiovascular accounts for almost around 17% of business, antibacterials has now jumped to around 8% of the business, anti-malarial is around 7% and derma has significant growth by almost around 2% point and now it is increased to almost around 5% of the business and cough and cold has also become around 4% of our business.

Standalone EBITDA for Q2 FY2022 stood at around 23.63% for the quarter as against 27.28% for Q2 FY2021. We have witnessed a very significant cost rise during Q2 due to increase in commodity prices, energy costs, shipments and logistic costs, raw material prices also moved up in some cases to almost around two to three fold and more due to the energy issue faced by China and also impacted by the China's dual control policy since the key provinces where the chemicals and intermediate units are located were functional only for few days a week and that created the shortages. Lower energy allocation by China into the mining sector also impacted the prices of some of the raw materials very adversely, higher prices trend is still continuing and we have not seen much of the sign of decline yet. Domestic prices of the key materials like solvents, acid, alkali, specialty chemical, pharma in many cases has moved by almost 100%. Higher inbound and outbound freight cost increase as well as domestic logistic cost increase has also impacted overall overhead cost, as a result of input cost increase material cost to sales ratio went up by 2.12% in Q2 in standard accounts and overall EBITDA went down by almost around 2.65% compared to Q2 last year, but as against our earlier guidelines of around 25% EBITDA for the financial year FY2022, EBITDA is lower at around 24.63% for the Q2 FY2022.

Having given some broad numbers, now I will request participants to ask questions.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from the line of Tushar Manudhane from Motilal Oswal Financial services. Please go ahead.

Tushar Manudhane: Sir firstly on the overall guidance for FY2022 given the first half FY2022 performance, would you like to revise the full year guidance?

A.K. Jain: It is our domestic business is doing very well and it has recorded almost around 30% growth in this quarter and last quarter also it was almost around 28% growth and our overall projection for domestic market was almost around 16% to 18% as against that we are performing much, much better so overall domestic business would be far better and we hope that even some of the seasonalities where the antibacterial sales was much higher due to the infections in the first half of the current year, even if they are at lower side we still feel that in second half also we will be doing better than what we have projected in the overall for the full of the year and overall growth for the whole of the financial year is going to be much better compared to last financial year overall. As far as our branded generic businesses are concerned more or less our guidance remains same. Institutional business also our guidelines would remain same what we had given earlier, but our API business will see some kind of decline because of some disturbances, more particularly on sartan sales due to the Azido impurities we have already filed with regulators or revised processes and taken all the establishment bases and done everything, but there could be sometime maybe the regulator test may take around two months trying to give approval, we expect that approval might come at December end or maybe early part of January and therefore in the next quarter, there could be some impact on business relating to API so overall projection for the API business in third quarter particularly will go down and there will be significant recovery coming back in the fourth quarter of the year. Overall as far as the EBITDA numbers are concerned right now we are not in position to give the guidelines because the input cost rises are significant and we are yet to see the kind of the retracement in those kind of prices, no signals are yet visible. Industry is hoping that maybe by fourth quarter things would be normalized but we are yet to see the sign of that.

Tushar Manudhane: Understood Sir. Just on the domestic formulation front the pain segment has been giving significant growth any factors you would like to call out and of course the sustainability for those factors?

A.K. Jain: Let us say most of our businesses have given good growth in the first half of the year I would say that every segment we are in except cardio, diabetes where we are given almost first half around 14%, pain has given significant growth to us almost around excluding the Hydroxychloroquine business exceptional business we did. We have grown by almost around 34% in first quarter in pain segments. Antibacterials has recorded in first half almost around 81% percent growth, cough and cold almost 90%, derma almost around 65% and some of these higher numbers are also because in the first quarter last year the base was lower but overall the trend appears to be good and we should be doing very well and the factors for that is as far as first and current year overall infection levels and all were very high and therefore overall acute business has improved significantly in the whole of the industry we are not seeing such kind of antibacterials and other sales but as far as pain is concerned we continue to even in normalized period we will continue to grow around 18%

to 20% kind of business because we are significantly taking the market share from various other molecules in the market and that trend would continue, we are long way to go.

Tushar Manudhane: And just lastly Sir on the gross margin, gross margin is trending down despite higher share of domestic formulation business so is that to do with the raw metal price increase being already factored in 2Q or it will be more intense and visible in the upcoming quarters?

A.K. Jain: Let us say in the Q2 as against around 10% growth in the topline our material costs gone up by almost around 17% and that trend will continue maybe even in the third quarter also. Fourth quarter I cannot say what kind of visibility will come because if there is some kind of signal start coming at the end of December or early part then some kind of reduction may happen in material course, but we are yet to see those kind of signals.

Tushar Manudhane: All right Sir. Thanks that is it from my side.

Moderator: Thank you. The next question from the line of Kunal Dhamesha from Emkay Global. Please go ahead.

Kunal Dhamesha: The first question again on the input cost given we are highly backward integrated should not that be kind of blunting the impact of the material cost or input cost increases for us?

Kunal Dhamesha: Yes that gives us some kind of advantage but lot of domestic products also the cost has significantly gone up some example like even caustic soda flax has gone up by almost around 150% in this period, even your product like phosphoric acid has gone up by around 235%, a simple product like sulfuric acid has gone up by almost around 88% even some kind of solvent, the prices has been significant MDC has gone up almost around 107% because petroleum product prices have gone up it almost rises around 27% to 30%, ethylene dichloride almost around 44%-45% so a lot of solvent prices, methanol almost 46% rise so significant prices and also the specialty chemicals which are supplied by the Indian manufacturer that has moved up so all the your input costs whether it is for solvents whether it is acid alkaline whether it is a specialty chemicals and all that they are moving up for example even like say commodity prices are impacting like all packaging are in PVC, PVDC that has moved almost around 28% to 30% all plastic bottle cap, pet bottles has moved up almost around 35%, all paper products has moved by almost around 15%-18% kind of those moments has happened so all those prices are moving up so and in case of like say all anti-bacterial phenzy prices have moved up significantly practically double. Common product like paracetamol which used to be a year about Rs.350 now we are buying almost around Rs.900 the pricing now and every pill you sell you are making losses today because it does not cover the prices today the kind of prices which has gone up in the market so there are a lot of those kind of challenges which are there currently because of all the disturbance which are happening in the supply chain and if it is stabilized then yes then your material cost to sales ratio can again come down but currently it is all disturbed.

Kunal Dhamesha: Okay and between let us say September to October also you are seeing increase or they are more or less stable now?

A.K. Jain: Increase trend is not there but currently the stabilized level of increased level but we are not seeing any kind of retracement yet.

Kunal Dhamesha: Sure and second question on the other expense sequentially other expenses including R&D has gone up I believe some part would be due to power fuel as well as logistic cost but in terms of these branding or sales and marketing effort except for component is everything back in the domestic market or the branded market?

A.K. Jain: Overall if you look at I will just give you some kind of breakup on what kind of cost impact we had on the major items in Q2. Let us say the fuel cost is almost moved by almost 24% and export freight and insurance that is another area where it has almost moved by almost 51% in this quarter. Overall if you look at factorization overall against let us say 10% increase in the topline my expenditure on factory level has gone up by almost around 12%. Marketing cost has moved up by around 7%, R&D cost has moved by almost around 18% and other overhead which are reduced by almost around 9% so overall there is a increase of 7% in other expenditures as against as 10% increase in the overall topline. It is all because of let us say exceptional increases which has happened in the energy cost and also the freight cost. Marketing cost increase was significant in first quarter because last year the sales force was all sitting at home and there was hardly any kind of promotional cost from second quarter onwards the marketing cost started returning back so from that level we have not seen much kind of growth so marketing cost has only gone up by 7% in the second quarter of current financial year.

Moderator: Thank you. The next question from the line of Viraj Kacharia from Securities Investment. Please go ahead.

Viraj Kacharia: Thanks for the opportunity. I just had one question was on the subsidiary, there seem to be some dip in the performance?

A.K. Jain: Subsidiary side let us say we have major subsidiary one is Onyx in UK that is doing very well its income has almost gone up by around 50% and they have a significant profitability, they have contributed. As far as Ramdev is concerned that we are talked that we are changing the product mix there and it was almost a drug intermediate company we are in process of validating a lot of APIs and also filing to Educam and other regulators so that process is going on so we have a lot of those kind of intermediate business this company was doing they have stopped those kind of businesses and more focusing on the API side and therefore business got disturbed and there are losses for some more time it is only matter of time I think maybe in one or two quarters this company will be coming back to the profitability overall so we do not foresee any kind of difficulties there on that account. So only problem we have is that the subsidiary company where we in U.S. that company there are some kind of losses we wanted to have the point of crams business which my our UK subsidiary doing similar kind of business there. Because of pandemic and all it became difficult to approach the customers and also talk on and also increase the manpower there and all that so that business was disturbed there we have started getting now the contracts on the crams business and all and hopefully next year that business will also start seeing a lot of revival. Another company we have is Bayshore pharmaceutical that is the front end what we have created for once our US FDA get cleared that company will be front end currently they are doing some kind of some product tie-up from companies and they are doing marketing and there are some kind of nominal losses and that those losses are also on account of whatever their intellectual property is right which we have capitalized that we are writing off so those losses are only because of that so other than that by and large Onyx profit by and large getting set of against losses what we have in these two-three subsidies kind of thing which we in time to come will definitely improve.

Viraj Kacharia: I was just trying to understand what kind of losses these would have made the US and the other one?

A.K. Jain: Losses I will give you the number let us say that your Bayshore losses will be around 4.62 Crores, Onyx profit is around this is half year numbers is around 18.79 Crores. Ramdev has incurred around 6.5 Crores losses and Pisgah around 7.67 Crores losses.

Viraj Kacharia: So these should by and large get reversed?

A.K. Jain: Pisgah may take a little longer time but Ramdev maybe I think in two quarters once we have validated around 5-7 APIs and all things would be well and things will start improving from third and fourth quarter.

Viraj Kacharia: Okay Sir thank you.

Moderator: Thank you. The next question is from the line of Abdul Kadir from Elara Capital. Please go ahead.

Abdul Kadir: Thank you for the opportunity. Sir can you please provide some update on capacity addition at Dewas and Ratlam on UPS side?

A.K. Jain: I think Dewas project got little delayed and I think it should be operational in the first quarter of the next financial year and as far as Ratlam is concerned that capacity will be available from the next month onwards the validation exercises are all going on and it should be commercially available from December.

Abdul Kadir: Okay and by and large what would be the blended increase in capacity once Ratlam comes in place?

A.K. Jain: I think overall increase will be at Ratlam will be around 10% and once Dewas come it will be almost around another 25% capacity it will add.

Abdul Kadir: Sure Sir just one more question on this API price hike so I understand your commentary on the raw material increase, but how are the customers and I mean how are we approaching our customers with renewed pricing or are we still waiting for to move out and see what is scenario?

A.K. Jain: Normally what happens that we have almost around three to four months order in pipeline always so those order prices cannot be revised and when your price moved up like solvent prices acetalically and chemical prices but we generally know that what kind of trends are there some kind of coverages are there for intermediate but these are spot buying so when these prices move up or energy prices move up you cannot help it and you cannot pass them to the customers immediately and as far as intermediate prices when overall trend which are the major building blocks you revise the prices but after your service all those kind of pending orders so it takes some time with the gap of almost four to five months in the overall the prices revision takes place so to the extent you are covered maybe around two-three months that helps you but some of the prices moves immediately some prices you already covered so you still get some kind of lower prices material, but it takes almost around four to five months to get the higher price range then customer also knows that yes what kind of intermediate prices trends are taking place so you get a price increase it is not that these all price increase whole industry is passing on but there is a time lag.

Abdul Kadir: Okay understood.

Moderator: Thank you. The next question is on the line of Ankit Jain from Spoon Advisors. Please go ahead.

Ankit Jain: Thank you for this opportunity. Sir my question is regarding the associate company Krebs Biochemicals and industries now they have been incurring losses from the last four to five years and which I can recall last concall it was said that we could break even this quarter that is third or fourth quarter but if I look at the numbers apart from equity we have put in around 30 plus 80 Crores of presence capital further 100 as expected there could be some discrepancy in the number but the present capital has been put at 9% rate so when do you think that Krebs can service this debt with its own operating profit as you see sales last like half year sales is roughly around 16 Crores so our rough figure says that maybe around 120-130 Crores of sales could help them just service this debt with their own operating profit? So for how long does the parent company IPCA see that we will keep putting in capital in this associated so overall if you could just see like if you could like describe the issue is it more from the production side or is it like there is no demand for this for what we are like for what Krebs is doing so just to understand how the numbers will move in case of Krebs?

A.K. Jain: As far as Krebs is concerned they have two plants, one is at Nellore which is producing some kind of the APIs which are not fermentation based API. Another plant is that Vizag which is a fermentation plant. As far as Nellore plant is concerned that has already come in the profits now and as far as Vizag plant is concerned we were producing some kind of fermentation product like Serratiopeptidase that demand which used to be almost 3-4 metric tonnes practically we were selling every month that has come down significantly during this kind of pandemic period it is also producing Simvastatin and Lovastatin so those all demands also got disturbed and therefore the overall whatever journey we were planning that did not happen that way. The demands are now coming back we have already started selling Lova good quantities have started selling now. Simva also now is picking up and Serratiopeptidase we have our own captive demands and also demand from other customers so that is also picking up so hopefully it is only a matter of time maybe around two more quarters you should be able to get Vizag plant also in the overall in the break even.

Ankit Jain: Okay so is it like two quarters are you saying that within two quarters Krebs will turn profitable?

A.K. Jain: Yes it should be.

Ankit Jain: Okay so it looks like very ambitious that is like we are expecting almost like 3 to 5x jump in the revenue within next two quarters so is that kind of dependency we have on this Vizag plant itself or because….

A.K. Jain: Overall guidelines it is a listed company so I cannot talk much about that but broadly I can say that yes we are on the course.

Ankit Jain: Okay so maybe within next two quarters we could see something very good?

A.K. Jain: Better results.

Ankit Jain: Okay thank you Sir.

Moderator: Thank you Sir. The next question from the line of Dipali Patadiya from Sameeksha Capital. Please go ahead.

Dipali Patadiya: I think most of my questions are answered, but I wanted to ask that in exports we are maintaining our guidance for generic and branded right for FY2022 so that means?

A.K. Jain: And institution yes.

Dipali Patadiya: And in the institution so there were approval for anti-malarial vaccine so in the long-run how are we looking at it how would it impact our revenue in institutional business?

A.K. Jain: As far as this vaccine is also to be given with some kind of your anti-malarial tablets so it is not that vaccine is administered alone so your traditional products will continue to have good sales.

Dipali Patadiya: Okay thank you. I will join back in this queue.

Moderator: Thank you. The next question from the line of Charulata Gaidhani from Dalal & Brocha. Please go ahead.

Charulata Gaidhani: I wanted to know if you could quantify the delayed shipments or the exports because of container unavailability?

A.K. Jain: That number we have not worked out but let us say institutional business we have seen around 23% decline in this quarter that is purely because of your non-availability of container even in our branded generics business we have seen a lower growth is also because of almost around $2 million worth of shipment got delayed so those are the things but exactly I do not have quantifications right now. As far as institutional business is concerned we maintain our guidelines for whole of the year that whatever guidelines of around 400 Crores we have given in the beginning of the year that will happen and the overall branded generic markets is also doing well so we should be able to deliver on our guidelines. There will be disturbances as far as the generics are concerned and there will be also because of lot of the API prices are higher a lot of our export goes to the Europe and Europe is still disturbed and there are excess inventory in the market and demand is sluggish so Europe we will see some kind of challenges. Other markets like South Africa, Canada, Australia and New Zealand they are doing well, but on Europe side there could be some kind of challenges. In API there will be some kind of disturbances because of Losartan part overall and that is for one quarter, the next quarter there could be a disturbances and thereafter it should be it should be back so by the time our Azado impurity free process will get an approval from Emma and we should be able to be back in the businesses as well whatever normal business what we were doing. Even in first half our Losartan shipments by and large much higher compared to what we had done in the first half of last financial year, but because of intermediate prices coming down of Losartan. Overall there is some kind of decline in there but once Azado free impurity process comes up prices are again moving up and therefore the overall business could be better but the time being for a quarter there could be some more disturbance.

Charulata Gaidhani: Okay and in terms of the degrowth in exports how much of this degrowth can you attribute to price erosion?

A.K. Jain: There are no price erosion as such so basically your input cost increase and we do a lot of European business on generics practically and there we are facing problem because market is sitting with higher inventory because there are still lockdowns and so many other things and Europe was operating with much higher inventory levels and that is most of the your distributors are sitting with higher inventory and therefore your overall order flows are slow and therefore they are some kind of declines in European markets.

Charulata Gaidhani: Okay and in terms of the China increase in cost from China by when do you expect this to settle down.

A.K. Jain: It is a very difficult question to answer. We have not yet seen any kind of prices coming down so I cannot really make out when it will happen. Industry is hoping that by fourth quarter that is what we hear from industry player that hopefully it should settle around fourth quarter but we are not yet seen those kind of signals.

Charulata Gaidhani: Okay right. Thank you all the best.

Moderator: Thank you. The next question for the line of Prakash Agarwal from Axis Capital. Please go ahead.

Prakash Agarwal: Sir my question is on the clarity on the cost aspect you talked about China disruption etc., so the current quarter would have seen only impact in September because we would be sitting on existing inventory would that be correct understanding and we are yet to see a full quarter impact in terms of rising costs etc?

A.K. Jain: I think it started from let us say part of August and September so those issues were there so around one-and-a-half months there was little excess prices paid and some of these costs like your alkali your solvents and all they started moving from the beginning of the quarter.

Prakash Agarwal: So knowing that and seeing significant cost increases on something which we can control on our expenses, are there any efforts so that we can maintain or improve the margin or at least not let it go down what are those measures Sir?

A.K. Jain: Let us say those measures are on a regular basis those kind of let us say cost cutting exercises and all are regularly done so more particularly on overhead side and all to reduce the overall operating cost and all so those exercises are regular but some kind of price increase play will also come up so therefore even if there is a higher increase in the cost that will start getting offset by our increases in the prices also and most of let us say our domestic market related price hikes has happened in the late first quarter and in second quarter per se so those all effects will also come in third and fourth quarter because there we work with almost maybe around 60 days inventory overall in the cycle so I think those extra realizations will also start coming in as a result whatever the cost increases we have compensated so somewhere the overall trend I would say that yes the cost increases are higher and compared to whatever topline increases are there but some cost reimbursement will start coming in and full impact will come in the third quarter definitely of the overall cost increase I agree with you.

Prakash Agarwal: Okay so I mean the Q2 EBITDA margins we could see some further pressure or with the cost to saving measures we will be?

A.K. Jain: We could see some further pressure on that.

Prakash Agarwal: Okay fair enough got it and the second question is the clarity on this API impurity this is largely pertaining to the European markets is what you said?

A.K. Jain: But once say it is out in Europe every country wants those kind of impurity free kind of products so there are disturbances in business.

Prakash Agarwal: And we seem to be certain about resolving by Q4?

A.K. Jain: We have already resolved and filed, the process and updates are already filed with and regulators have given us almost around 60 days to get approval so hopefully by December end we should get approval but it is because of Christmas holidays and all it gets delayed then maybe in early part of January we should get an approval and we already started sampling to all customers so practically all our customers sampled so that they can do the testings and everything is our and except European manufacturer all others need not to wait.

Prakash Agarwal: Is that specific or it is industry wide phenomena that you have see?

A.K. Jain: It is industry wide phenomena.

Prakash Agarwal: Okay and lastly Sir on the inventory side I do not know if you covered there is a spike if you could explain that as well receivables more so?

A.K. Jain: In fact inventory has gone down I will give you the overall number.

Prakash Agarwal: Sir it is there BSE sheet just wanted number on the receivable?

A.K. Jain: Inventory turnover ratio in 2020 it was almost 109 days,. In September 2021 it is a 109 days so in fact the inventory to sales ratio is currently we are as again 107 days inventory in FY2020 and 109 days inventory in 2021. We are currently at 92 days inventory so we have in fact all reduce the inventory level as far as receivable cycles are concerned. In 2020 it was almost around 71 days which in 2021 it has come down to around 56 days is largely because a lot of those incremental businesses and all of the Hydroxychloroquine and Chloroquine that has happened on advanced payments and all so it has come down but currently we are around 63 days overall inventory level so from receivable levels so practically we have improved from 71 days to 63 days so it is not on higher side.

Prakash Agarwal: Okay fair enough. Thank you Sir and all the best.

Moderator: Thank you. The next question from the line of Kunal Randeria from Edelweiss Securities. Please go ahead.

Kunal Randeria: Thanks for taking my question. Sir can you share how much is statin contribution in your API business and how much is the price corrected se?

Harish Kamath: Roughly both statin contributes about 30% of my API business.

Kunal Randeria: How much price corrected?

Harish Kamath: Mr. Jain already said now whatever price correction that has happened is because of the reduction in the intermediate prices and whatever reduction was there it was passed on.

A.K. Jain: Almost 20% reduction was there.

Kunal Randeria: Got it Sir…

Harish Kamath: Even our sales quantity tonnage is more than what it was in the first half of last financial year but realization is lesser because of this price correction.

Kunal Randeria: Understood Sir and therefore you earlier mentioned that you typically see a three to four month lag on price realization so I mean just hypothetically would it be fair to assume that in case this input price remains elevated you can pass on the entire increase to customers and still protect your margin?

A.K. Jain: What is happening today because of this phenomenal increase in the prices even customers are also not very sure whether to increase their inventory or reduce them so they are also into a tight corner what to do that is also the reason why even the order inflow has reduced because of this issue.

Kunal Randeria: This is more like a hypothetical question but I am just assuming three or four months down the line the prices do not correct so I mean what is the typical practice do you sort of…

Harish Kamath: There is no option the manufacturer will increase the price and customers will buy see today paracetamol prices are so high so inventory in the market is also reduced because people are not willing to buy they are not willing to give order at this price so because of that also generic business has impacted it is not only paracetamol several of APIs prices have increased like.

Kunal Randeria: Sure Sir and do you maintain the tax rate guidance around 18% to 19% for this year?

Harish Kamath: We are MAT company so actual tax also there would not be any difference percentage wise as far as deferred tax is concerned if there is more capitalization of the asset there will be more default tax but it is a non-cash outgo item.

Kunal Randeria: Right and that will increase only in FY2024?

Harish Kamath: It will increase maybe even next financial year once you capitalize your Dewas new API facility it will increase so it is the difference between the IT depreciation and the company's depreciation right so on that tax whatever amount is there.

Kunal Randeria: Understood okay so thank you very much and all the rest.

Moderator: Thank you. The next question is from the line of Sonal Gupta from L&T Mutual Fund. Please go ahead.

Sonal Gupta: Hi good afternoon and thanks for taking the question so just on impurities I mean this is an older issue for rest of the industry so why is it coming for you now I am just trying to understand?

A K Jain: No initially it was not Azido impurities it was something else this is a new phenomena.

Sonal Gupta: There was some nitro?

A K Jain: Nitrosamine that was the issue this is something different.

Sonal Gupta: Okay and this is again because of some input KSM or is this that is what is the driving reason for this?

A K Jain: Let us say there are Azide reactions happens in statins and as a result of this in part for billions there are some kind of impurities generated which was earlier not regulators overall requirement was your impurity levels was little higher which regulators have now reduced that level so we have to qualify the process now at a reduced level of those kind of impurity and therefore the whole process correction has happened. There is one more stage has increased in the manufacturing of another purification stage and therefore all our cost of productions are also going on, it is increasing and the market prices are correspondingly is also increasing of the those products so Azido impurity products are 20% higher the pricing compared to the normal material so that all process corrections and everything is done it is already filed with regulators we are just awaiting the approvals. I would say that other markets may not wait to that an extent to get the Emma approvals but whatever Emma markets like say European markets are there supplies will have only happen after your revised safety approval is received and therefore to that extent that there will be some kind of disturbances going to be there then some kind of additional your existing inventory also need to be reprocessed so instead of producing new, your capacities will go in purification side and therefore some kind of disturbances would happen as far as the business of Losartan is concerned in the current quarter that is why I say that the business would decline in the third quarter for Losartan and statins and it will come back in the fourth quarter of the next year.

Sonal Gupta: Got it so you do not really see this fundamentally impacting your market share and this is…

A K Jain: It is only time being temporary impact.

Sonal Gupta: And just again another broader question on the API side like you mentioned that the inventory levels with distributors etc., are high and the manufacturers are high as well and at the same time prices are going up because there is a lot of input cost pressure so I mean do we see that like this is not just for you in specific but I am like do we see that the API manufacturers therefore have to bear more of the brunt in terms of margin because last year of course there was a very strong margin because the demand was very strong but now we are seeing a normalization or worse than that because demand is weak and the price inputs are going up.

A K Jain: My comment was with reference to generics more particularly with reference to generics in Europe that European generic manufacturers are having higher finish goods inventory of all the finished formulations not with reference to it the API. The APIs is bought by your producers they do not keep higher inventories of API so they are what Mr. Harish has given the comment that when there is a price increase the order size goes low because they do not want to buy higher at those prices because they also see that what kind of trends are going to be there so at a higher prices they give a lower order so on the floor get reduced that is what he commented on that.

Sonal Gupta: Got it thanks for that clarification but just on the API side do we see the potential to pass on the cost pressure fully or do you think there will be some margin?

A K Jain: I think everybody has to pass on, there is no option. Whole industry is passing on. Absolutely everybody is passing on so only time being maybe three-four months time you suffer because whatever your orders are there in with you, you cannot revise those prices.

Sonal Gupta: Got it great Sir. Thank you so much.

Moderator: Thank you. The next question from the line of Samir Baisiwala from Morgan Stanley. Please go ahead.

Samir Baisiwala: Thank you so much and good evening everyone. Sir just taking from the previous participants so you are passing on prices for API domestic formulation and for export formulation as well so all lines of your businesses you are able to pass it on?

Harish Kamath: Yes European business since business itself is slow there it is a little difficult, there because market is having higher inventory so they are passing on will take a little longer time, rest all business that is happening maybe at the gap of around three-four months time.

Samir Baisiwala: Okay and Sir if you say in January 2022 looking back what sort of a portfolio-wide company-wise price increase, would you have taken or something that you need to take?

Harish Kamath: Each product wise impacts are different so each product-wise price increases are there I can say about domestic market or normal price increases used to be around 4.5% or so now this year it is almost around 6.5% to 7% price increases are there beyond which we cannot go because there are the portfolio which is in price control where this year there was no price increase was there so it almost around full price increase of 10% whatever is there for non-schedule formulation we have taken 100% full 10% price increase on almost all products of the company so that and a lot of those price increases happen in the end of first quarter and in the second quarter because you can take price increase on a 12 month rolling basis suppose price increase is due in September then you take in only in September so some of the prices increase are taken late so they will become effective after say two months' time when the overall company inventory get exhausted.

Samir Baisiwala: What would be similar number for export formulation in APIs?

Harish Kamath: Export formulation each product by it differs because in fact in each product is different some products there are no impact, some product there is a significant impact like say Metformin and all we choose to sell this currently the prices are practically doubled so 100% it is passed down to the customer some product maybe 5% some product maybe 10%, somewhere that may be 20% each product wise it is different because it is not that everything is coming from that 810 provinces which are there some are coming from other provinces where disturbances are not much that is different on each product so I cannot give an API side those number I can give one formulation and I would say that European price increases was not much even though their input cost because there is the only resistance from customers because he is already higher inventory so the buying are at a reduced level so their price increase has not been much.

Samir Baisiwala: Got it and Sir any update on the FDA's reinspection for the three warning letter side?

Harish Kamath: No Samir nothing it is just a status quo.

Samir Baisiwala: Even though the agency has started to come down for international?

Harish Kamath: But we have not received any notification so far.

Samir Baisiwala: Your best guess Sir?

Harish Kamath: It is anybody guess.

Samir Baisiwala: Okay that is fine and Sir I have heard all your commentary pluses and minuses but your full year guidance for sales was 8% to 10% and the EBITDA margin was 25% for FY2022 so does it stand or keeping all the pluses or minuses?

Harish Kamath: If you see as far as guidance is concerned of domestic Mr. Jain has already explained we will do better than the guidance given and the same is whatever guidance given for institutional business also we will do but today issue is about API export business and the generic business especially Europe so we are into such a situation very difficult so may be end of third quarter. Third quarter along with the third quarter result we will give the guidance so this quarter is very crucial Mr. Jain has already explained API there are issues, generic business especially Europe which is a very big market there is a problem today so very difficult to say at this juncture and also the all price increases and other things even though we are trying to pass on the benefit will come after a quarter or four months so next quarter will be crucial.

Samir Baisiwala: Okay it is very clear Sir and that is it from my side. Thank you.

Moderator: Thank you. The next question from the line of Rahul Jeewani from IIFL Securities. Please go ahead.

Rahul Jeewani: Thanks for taking my question now with respect to the Pithampur and Silvassa formulation facilities because these facilities are underutilized because we are not exporting to the U.S. market right now, what is the effect operating expenses on account of these two facility?

Harish Kamath: As far as these two facilities are concerned there is no any improvement in their capacity utilization unfortunately as we explained today Europe generic business is also not in that kind of a good shape so overall whatever margin pressures were there on these two units are continuing today also.

Rahul Jeewani: Okay but in part you have indicated that the quantum of fixed operating expenses which you were incurring from these two plants way through the tune of Rs.50 Crores to Rs.60 Crores so is that number correct or that number higher than one?

Harish Kamath: That number has not increased that is what I said so accept whatever inflation related and increments to people other than that there is no change in these numbers and capacity utilization of both these plants are almost similar last a year or so until today also.

Rahul Jeewani: Sure Sir and answer my second question is on Sartan market you indicated that the intermediate prices for Losartan have come down but they have again started in China but how do you see the overall pricing in the Sartan API market to shape up over the next 12 to 18 months period given that the formulation products in the U.S market have been seeing price pressure whereas some of the other Chinese players who had vacated the Sartan market they could also incrementally make a comeback in the market so how do you think the overall price environment will play out in the certain API portfolio for you?

Harish Kamath: Let us say the prices has mainline intermediate used to be almost around $28 from that it came down to around $12 it again started moving to around $18 and since this new issue of Azido impurity has come up so everybody was busy with revising their processes and maintained that demand dried out for the suppliers for the Chinese suppliers so the prices again come down to around $12 or so there has been too much of zigzag on prices of all these kind of intermediates are there and the Azido impurity issues is only as is a very Nitrosamine impurity for industry took a lot of time because a lot of process correction was required. Azido impurity is not going to take a long time for industry we have already filed our process and many other manufacturers will also file the process revised processes maybe in a month or two so it is not only a time being difficulties for industry but it will evolve very quickly.

Rahul Jeewani: Okay but you expect the overall starting pricing to hold up over the next let us say a 12-month period despite the incremental competition which might come in from China?

Harish Kamath: Prices still increase by 20% now because your additional purification will be required by everyone when there is an additional purification one more step your overhead goes up and also there are some kind of process loss are there so you have since your cost goes up that price is so currently also Azido impurity free prices are almost around 20% higher than normal pricing so those prices would again increase. It is already increased here.

Rahul Jeewani: Okay Sir but that is related to the cost of production for us also going up because of this additional purification step which we have in the process so that 20% price hike I think would actually not load to margin as such for us?

Harish Kamath: Or that it will also cover the margins here.

Rahul Jeewani: Sure Sir okay that is it for myself. Thank you.

Moderator: Thank you. The last question from the line of Dipali Patadiya from Sameeksha Capital. Please go ahead.

Dipali Patadiya: I have been broader question can you help me understand that we have almost we decided top selling products are vertically integrated so in such environment where prices are going up is there any area where I know shipping and all the costs are going up but if there are any area where we are benefiting because we are vertically indicated or in the longer run if such crises continue in China would be able to benefit because we are vertically integrated and we are so strong in API which is again vertical integrated?

Harish Kamath: Vis a vis a company which is not vertically integrated definitely to that extent we will benefit other than that it is a normal industry phenomenon. There is nothing called more benefit and all every company which is vertically integrated will have a better margin in their formulation business.

Dipali Patadiya: Okay Sir got it and the second question in the long run again that the answer goes for that as well right?

Harish Kamath: Yes correct right.

Moderator: Thank you as there are no further questions. I would now like to hand the conference over to the management for closing comments.

A.K. Jain: No further comments since there are no questions we will close this session. Thank you.

Moderator: Thank you. On behalf of Dam Capital Advisors Limited that concludes this conference. Thank you for joining us and you may now disconnect your lines.