

CADILA HEALTHCARE Q2 2004-05 POST RESULTS CONFERENCE CALL (OCTOBER 25, 2004)

Moderator: Good afternoon ladies and gentlemen. I am Ajay, the moderator for this conference. Welcome to the Cadila Healthcare conference call. For the duration of the presentation, all participants' line will be in the listen-only mode. I will be standing by for the question and answer session. I would like to hand over the floor to Mr. Pankaj R. Patel of Cadila Healthcare. Thank you and over to Mr. Pankaj R. Patel.

Pankaj Patel: Good afternoon and welcome to the post result teleconference.

Overall, we have managed a double-digit growth both on top line and bottom line in spite of being in investment phase in several markets. The margins are somewhat under pressure, especially in the API business. **The highlight of the Q2 2004-05 results is that we have, on consolidated basis, crossed the half billion mark in profit for the first time in the company's history.**

Coming to the details of consolidated results:

The consolidated net sales increased by 14.4% to Rs. 3492 million in the Q2 from Rs. 3052 million in the corresponding quarter in the previous year. The growth was driven by exports which went up by 31% year on year, and the international formulation sales doubled y-y. Domestic formulation net sales grew by over 10%.

The PBIDTA increased only marginally by 3% due to higher expenses. However, the operating profit i.e. PBIT grew by 13% y-y. The profit after tax increased by 28.7% to Rs. 511 million- crossing the half billion mark for the first time.

During the quarter company filed 2 DMFs, one ANDA with the US FDA, taking the total number of DMF filings to 16 and ANDA pending for approval to 13. Additionally, the company also filed 2 COS (Certificate of Suitability) and one Canadian DMF.

Coming to the details of the standalone performance during the Q2, the highlights are as follows:

The net sales revenue increased 10.3% to Rs. 3034 million from Rs. 2751 million in Q2 last year. Total domestic sales has increased 8% y-y (to give you the breakup- the formulation sales grew by 12%, the API domestic degrew by 15%) while the total exports grew by 17% y-y (31.3% growth of formulations and 11.8% total API). The domestic sales constituted 85% of total sales, whereas exports for the quarter constituted 15%.

The PBITDA (profit before interest, depreciation, tax, and amortization) increased by 3% year on year to Rs. 726 million from Rs. 702 million last year, and PBITDA margins were slightly off (by 80 basis points) due to higher expenses during the quarter. The net profit for the quarter was Rs. 432 million, up 10% from last year number of Rs. 394 million. This was helped by the lower interest and taxes.

Thank you very much and now we can start the Q&A. With me is Mr. Ganesh Nayak, Mr. M. K. Patel, and Leena Sagar, and you may ask questions with respect to domestic markets and non-regulated markets to Mr. Nayak, for the results and finance to Mr. M. K. Patel and Leena, and for the regulated market to me.

Over to the coordinator for the Q&A session.

Moderator: Thank you very much sir. We will now begin the Q&A interactive session. Participants who wish to ask questions, please press *1 on your telephone keypad. On pressing *1, participants will get a chance to present their questions on a first-in-line basis. To ask a question, please press *1 now. First we have Ms. Shahina from HDFC Securities.

Shahina: Hi good afternoon, good set of numbers, congratulations. I had a couple of questions on the breakup of the consolidated- what was the contribution from the subsidiary, Altana, and how is this accounted for the dividend.

Pankaj Patel: On the dividend for the quarter we have received a Rs. 10 crores dividend from the Altana JV.

Shahina: And where is this accounted for?

Pankaj Patel: But in the consolidated account it gets removed.

Shahina: So is the gross revenue includes the dividend?

Pankaj Patel: No. No, if you look at the consolidated number, there it is removed, but if you look at the standalone numbers, then it is included in other income.

Shahina: In consolidated it is in?

Pankaj Patel: In consolidated it gets removed because dividend has to be cancelled. In the standalone company numbers, if you look at the other income of Rs. 15 crores- it includes Rs. 10 crores of dividend.

Shahina: Okay, may be I will clarify this later, I still haven't got it, but let me just go on to the next one. Basically, there has been a reduction in excise duty also. Is there any specific reason for that, as a percentage to sales?

Pankaj Patel: Mainly the excise duty has gone down because substantial quantity of the production was carried out on third party basis.

Shahina: So this would be something that we can expect to continue going forward?

Pankaj Patel: Yes.

Shahina: Okay, thank you sir.

Moderator: Thank you very much madam. Next in line we Mr. Balaji from Sundaram Mutual Fund.

Balaji: Hello, good afternoon everybody. I just want to know the status of your Altana JV, I mean the negotiations that is happening- will you be supplying more ingredients other than KSM6 and 14 , and also what about the other products of Altana ?

Pankaj Patel: Currently we are only supplying KSM6 and KSM14, and we are still discussing, so, currently I cannot give you any further guidance on this.

Balaji: And can you give me any guidance on how many tons will be produced FY '06?

Pankaj Patel: Sorry, you are asking numbers for FY 06?

Balaji: Yeah.

Pankaj Patel: FY '06 numbers would be 43 tons of each intermediate.

Balaji: Okay thank you.

Moderator: Thank you very much sir. Participants who wish to ask questions, please press *1 now. Next in line we have Mr. Kirit from ASK Raymond James.

Kirit: Hello. Good afternoon sir and congratulations on good set of numbers. I just would like to know about what is the current status of your distribution network in US, which you have been planning with some generic companies in the US market . Where is it right now and when do we expect some announcement on that front?

Pankaj Patel: It is very much under control, I can only say that to you at this moment, announcement - I cannot give you a specific date.

Kirit: Okay, and I believe that we had launched couple of products in the French market, so how those products are doing and how do you see the future launches in this market?

Pankaj Patel: We have just began launching- as you are aware - somewhere end of the last month generics in the French market, and we expect that the product should grow rapidly in terms of sales. We would be launching in the current month

omeprazole for the first time in the French market, which would help us increase the sale. We see the numbers growing fast now.

Kirit: Okay, and what is strategy for other European markets, because right now we are focusing just on French market, so do we have a strategy for other European markets, large markets like Germany and UK, and when do we plan to enter these markets?

Pankaj Patel: Again Kirit, you know I have been saying this, we have been looking at both Germany and UK as an opportunistic markets, we do not want to basically aggressively push getting something unless we get a niche opportunity in this market; however, we are actively pursuing our opportunities in French and Italy market, and a lot of work has been done around that now, and we intend to complete the entry into these markets as I have mentioned by the end of financial year '06.

Kirit: Okay. Thanks a lot.

Moderator: Thank you very much sir. Next in line we have Mr. Ranjit Kapadia of Tower Capital.

Ranjit Kapadia: Good afternoon sir and congratulations for good set of numbers. Sir I would like to know the strategy for the domestic market, you have said that you will be putting a facility in Baddi, and converting the Moraiya facility for the regulated markets. So can give a brief outline of what is the investment in Baddi and what sort of products are likely to be manufactured?

Pankaj Patel: Okay. For Baddi our total investment is Rs. 27 crores. The facility is mainly to produce tablets and capsule formulations. The production has already commenced as of last month, and it will go into the full stream of production by end of this year. So all the tablet and capsule productions are being shifted to Baddi facility, which would basically offer us both sales tax and excise tax benefits. We expect when the Baddi facility goes on the full stream, we expect our production load on our existing facility for the regulated market increasing, and that facility will then be used for regulated markets.

Ranjit Kapadia: Sir, what sort of manufacturing be generated in the current year from this facility in terms of the numbers, in terms of tax saving?

Pankaj Patel: I can give you specific number offline, I do not have numbers in front of me now.

Ranjit Kapadia: Okay. And sir any future plan to upgrade or increase this facility at Baddi- any further investment is expected in the coming two years.

Pankaj Patel: Currently we are not planning to expand that, we would like to basically successfully run that and prove that we can make money out of it.

Ranjit Kapadia: And any suspension or liquid orals going, because we have said that only tablets and capsules, so all other formulations will be manufactured at Moraiya?

Pankaj Patel: Yes, currently we do not have substantial volumes in liquid orals, so we do not require this at all.

Ranjit Kapadia: Okay. Thank you sir.

Moderator: Thank you very much sir. Next in line we have Mr. Rahul Sharma from Karvy.

Rahul Sharma: Hello, congratulations sir on a good set of numbers. Sir I just wanted to find out why there has been a substantial difference in our formulations exports compared to standalone, which are the markets which are reflected in the consolidated numbers sir?

Patel: Because of the French business, this gets merged for the first time, the numbers look higher.

Rahul Sharma: Okay sir. So similar will be the case with API, the Altana reflected in the consolidated numbers?

Mr Patel: Yes.

Rahul Sharma: Okay so the entire sale will be due to Altana?

Mr Patel: No, there is sale from the Cadila Healthcare also. So if you look at our API exports on a standalone basis, from Cadila Healthcare, it showed a growth of 11.8%.

Rahul Sharma: Okay, thank you.

Mr Patel: Then Altana is of course

Rahul Sharma: Thank you sir.

Moderator: Thank you very much sir. Next in line we have Mr. Rajesh Vora of ICICI Securities.

Rajesh Vora: Good afternoon and congrats for good set of numbers. Just two questions; first on the status of product filing for the US market, which you can update us; and secondly, on the investment phase that the company is in today and two years down the line where does company see itself in terms of revenues from the regulated market and overall revenue going forward?

Pankaj Patel: Good afternoon Rajesh. Two good questions. First the question regarding the filing, I think we are very much on track with respect to our filing targets, things are moving as we have anticipated, during the last quarter as I mentioned we filed one ANDA and two DMFs and we will file required number by the end of March. With respect to the business going forward in next two years, particularly from the regulated markets, US and Europe, we expect they would be contributing significantly over a three year's period rather than a two year period . I would say, and by FY '07, we expect that this market should be contributing about 25% of our sales.

Rajesh Vora: Okay. And in terms of any filings in this quarter on the ANDA side?

Pankaj Patel: Last quarter we filed one, and this quarter we intent to file several.

Rajesh Vora: Okay. So you are on track to file

Pankaj Patel: Yeah our original target of 16 to 18.

Rajesh Vora: Okay. And in terms of the phase of investment as of now, you are going through investing in the US and Europe, particularly in France, versus revenues which are going to come through over the next two to three years, and one of the driver that has been helping you maintain margins has been the huge success of PRISM program. So how is that program going on?

Pankaj Patel: PRISM - this year we are in cycle 2, and cycle 2 has a target of improving the margin further by about 2%. As of now, we are very much on target on that number.

Rajesh Vora: Okay thanks a lot and good luck gentlemen.

Pankaj Patel: Thank you.

Moderator: Thank you very much sir. Next in line we have Mr. Surjit from KJMC.

Surjeet: Hi! Congratulations. Actually what is your total R&D expense during this quarter?

Pankaj Patel: During the quarter our R&D expenditure is Rs. 12.8 crores.

Surjeet: Rs. 12.8 crores, vis-à-vis?

Pankaj Patel: Vis-à-vis the same number last year.

Surjeet: Okay. Another thing is what is the total sales of Altana that has been shown in your consolidated number?

Pankaj Patel: 50% of our share basically.

Leena: I think he is asking for the number.

Pankaj Patel: Oh! Okay numbers, number is Rs. 20.64 crores (Q2 sales - Zydus share) .

Surjit: Rs. 20.64 crores. Yeah, and would you give us some strategic input in terms of company's thinking to replicate Altana model which sharing?

Ganesh Naik: First of all we cannot say that; we definitely havr plans to replicate this model; however, I would like to draw your attention that this models takes time, this is the kind of a model that has gestation period between three to four years before they start earning like this. We are currently negotiating and discussing with several of our partners and other companies for similar initiatives. However, nothing has been finalized as of yet.

Surjeet: Are you also trying with Altana for their new drug, Roflumilast/Daxas or for any other drugs?

Pankaj Patel: We are discussing everything possible with Altana, but currently we do not have any specific plan to tell to you.

Surjeet: Thank you sir.

Moderator: Thank you very much sir. Next in line we have Mr. Chetan from Mehta Partners.

Chetan: Couple of questions, one on capex, what are your plans for next couple of years, and second one on your contract manufacturing initiative, if you can give us a broad update on where you are and what kind of revenue streams you look from this business?

M K Patel: First question with respect to capital expenditure, the current year, we expect the capital expenditure to be about Rs. 120 crores. We would expect a capital expenditure of about Rs. 100 crores next year.

Pankaj Patel: With respect to our contract manufacturing initiative, we have initiated this about 8 months back now, we have several negotiations going on for this contract manufacturing deal. We are closed to finalizing few of the deals, and we expect to give the news to the market by last quarter of this financial year or say between January and March '05.

Chetan: And any broad guidance on the kind of profitability you see from this kind of business?

Pankaj Patel: It is difficult to say at this moment because the moment I tell you the numbers, then you would say what is the total volume, so generally as a policy we are not giving any guidance . In general I can say that this kind of business (contract manufacturing) could have a bottom line between 30 – 40%.

Chetan: Okay, thank you.

Moderator: Thank you very much sir. Next in line we have Ms. Rohita from Prabhudas Leeladhar.

Rohita: Could you give us an update on your initiative for the Brazilian market?

Pankaj Patel: Sorry, could you please repeat the question.

Rohita: Could you give us an update on your initiative for the Brazilian market?

Pankaj Patel: Mr. Nayak would you like to take this question?

Ganesh Naik: Yeah this is Ganesh Nayak here. We have been working on the Brazilian market for the last two and a half years, and now we have something concrete in terms of, not only a model but also in terms of revenue generating model. And we have applied for 9 products, out of which 5 products we are expecting in this month. One of them we have already got, in fact it is our first registration in the Brazilian market.

The Brazilian market is growing quite well at around 20%, and the generics as well as the branded generics both offer a good opportunity. We have a plan of submitting 36 dossiers in the next one year. We already have a country head based in Sao Paulo who is a local manager from a multinational, and our plans for Brazil seems to be in place. In fact, our revenues

would start from April next year.

Rohita: Okay, fine, thanks.

Moderator: Thank you very much mam. Next in line we have Mr. Pawan from Kotak Securities.

Pawan: Hi, my question is for Mr. M. K. Patel as it relates to finance. Sir, can you tell me in the consolidated numbers, your depreciation and amortization, it has dropped from around 22 crores to about 17 crores, anything that you would like to say on this?

M K Patel: In the same quarter last year, we have huge depreciation on brands coming in from Sarabhai Zydus, and this time it is not there and that is why a drop has been reported.

Pawan: So it was a one-time charge that you had in the last year quarter? Hello.

M K . Patel: Yes.

Pawan: Okay. Second is, can you please be little more specific in terms of Altana sales and profits, I am sorry if you have mentioned it, sales and profits for this quarter and the last year quarter?

Pankaj Patel: Sales for the quarter is 2064 lacs, and the profit is 1834 lacs.

Pawan: And what was it last year this quarter, could we have that?

Ganesh Nayak: Last year the same quarter?

Pawan: Yeah.

Ganesh Nayk: I will give you the number, one minute. Last year the sale was 1698 lacs and the profit was 1190 lacs.

Pawan: Okay, one last question for Mr. Pankaj Patel. Sir, how would you like to position Cadila in the mind of investors, would generics be the big story, generics and the stable domestic business be a big story going forward, or would it be a mix of generics, manufacturing, and a stable domestic business?

Pankaj Patel: I think, going forward our revenues, and I am looking at now 3 to 5 years revenues, would be strongly driven by 3 areas- domestic, generics and contract manufacturing.

Pavan: Okay, and you think, the....

Pankaj Patel: Already we have in our existing business portfolio, domestic business- you know very well about it. Generics- we are already in France and we are getting into US- you know very well- and contract manufacturing- Altana is example. So basically we have these three and I think, we believe these three will go forward further.

Pavan: Okay, would you have any targets in mind, say, you think say, Altana kind of deal, I mean, obviously that is like a blue sky scenario but otherwise what is the kind of say, 3 years down the line, what is the kind of contract manufacturing business you are looking at?

Pankaj Patel: We want to double the revenues, which we are getting today.

Pavan: In 3 years?

Pankaj Patel: Yeah.

Pavan: Okay. Fine thank you, and best wishes.

Moderator: Thank you very much sir. Participants who wish to ask questions, please press *1 now. Next in line, we have Mr. Purushotam of ICICI Securities.

Purushotam: Hi, just a clarification, did I hear right that you said the profits from the Altana JV were 18.34 cr for this

quarter on sales of 20.64 crores.

Pankaj Patel: Yes

Purushotam: Then, last year you said that you did profit of 11.90 crores on sales of 17 crores, so what is the reason for this sharp spike in profitability.

Pankaj Patel: There are several reasons, one is some cost efficiency we have achieved at the plant level. The second is we have been getting a little better realization because of exchange rate. And generally an overall cost consciousness at the plant in spite of making huge profits. We have been very cost conscious, so we are looking at reducing cost y-y, every year, to improve the profitability further.

Moderator: Thank you very much sir. Next in line we have Mr. Ravi Agarwal of JP Morgan.

Ravi Agarwal: Hi, just wanted to check with you, when do you expect to receive product approvals in the US market, and how do you propose to market these products?

Pankaj Patel: We expect product approvals coming in maybe, in next couple of months. With regard to marketing- we have a strategy in place now. We would be basically marketing products under Zydus label. We would initially use a partner to market our products for a limited period, and we intend to launch the product in the next quarter in the US market.

Ravi Agarwal: Will this partner be a pharma partner or will it be more of a distributor?

Pankaj Patel: No, no, a pharma partner- existing generic company.

Ravi Agarwal: Okay. Thank you.

Moderator: Thank you very much sir. Next in line we have Mr. Anshu Govil of CLSA.

Anshu Govil: Hello, my question is regarding the tax rate, why has it fallen drastically by this year?

Pankaj Patel: That is basically because of the tax incentives, particularly the R&D investments and ..

Anshu Govil: Your R&D investments were flat year on year.

Pankaj Patel: No no, only for the quarter, not for the half...

Anshu Govil: Yeah, but you said that your R&D investments for the quarter were flat at 12.8 crores, if I remember right.

Pankaj Patel: Only for the quarter, but you know, the R&D investment is not divided into 4 equal parts, it is always divided into several parts, in different months, so it is not that you could see the R&D expenses divided by 4 every quarter. But if you see the 1st half, then, in first half there is substantial increase in R&D expenses.

Anshu Goel: Okay, thanks.

Moderator: Thank you very much sir. Next in line we have Mr. Pawan of Kotak Securities.

Pavan: Yeah, I sorry, just one repeat question, despite the modest top line growth that you had, I see your EBITDA is actually kind of flat, and also your R&D expense is flat, so any particular reason or was this, in this quarter it is probably not reflecting the gains that you probably got from your Prism project.

Pankaj Patel: Okay, good question. I think if you see our material cost actually has shown a significant improvement by 4%. The EBITDA is flat mainly because of higher expenses on some market development related strategic expenses during the quarter.

Pavan: So probably margin expansion would be higher, you know, better in the subsequent quarters.

Pankaj Patel: Yes.

Pavan: Okay. Thanks.

Moderator: Thank you very much sir. Participants who wish to ask questions, please press *1 now. Next we have a followup question from Mr. Balaji of Sundaram.

Balaji: Sir if you could let us know the sales figures and the reported loss of the Zydus France for the first half?

Moderator: Sorry to interrupt you sir. Hello Mr. Balaji?

Balaji: Yeah.

Moderator: Are you on a speaker phone?

Balaji: No.

Moderator: Please go ahead with your question sir?

Pankaj Patel: Balaji, the first half, the sales of Zydus France is 1318 lakh, and the losses of 1st half is 415 lakhs.

Balaji: How much?:

Pankaj Patel: 415 .

Balaji: Okay. Thank you.

Moderator: Thank you very much sir. Next in line, we have Mr. Surjit of KJMC.

Surjit: Actually I just wanted to know what the latest update is on Ankleswar plant, when are you expecting US FDA approval on this?

Pankaj Patel: We expect FDA to be in our plant, maybe in next couple of months because that is the time they come to India usually. We have filed several DMFs and in fact some of our ANDAs have been inspected, so we expect this inspection happening in next 2 months.

Surjit: Wasn't it expected last month September?

Pankaj Patel: No.

Surjit: Thank you.

Moderator: Thank you very much sir. Participants who wish to ask questions, please press *1 now. At this moment, there are no further questions from participants. I would like to hand over the floor back to Mr. Pankaj R. Patel.

Pankaj Patel: Thank you very much for participating in our teleconference, and looking forward to talk to you again at the declaration of result of the quarter three.

Thank you and good evening. Bye.

Moderator: Ladies and gentlemen, thank you for choosing CyberBazaar's conferencing service. That concludes this conference call. Thank you for participation. You may now disconnect your lines. Thank you and have a nice day.
