

Q1 FY06 Earnings/Investors Conference call (July 26, 2005)

Moderator

Good evening ladies and gentlemen. I am Ganesh, the moderator for this conference. Welcome to the Cadila Healthcare Limited conference call. For the duration of the presentation, all participants' lines will be in the listen-only mode. I will be standing by for the question and answer session. I would now like to hand over the floor to Mr. Pankaj Patel of Cadila.

Thank you and over to you sir.

Pankaj Patel :

Thank you Ganesh. Good afternoon and welcome to the post result teleconference for the first quarter of FY06. The numbers are with you and I will highlight the key numbers.

Coming to the details of performance of 1Q 2005-6 on a standalone basis,

- the net sales revenue increase by 13.4% y-y to Rs 3275 million.
- Revenue growth driven mainly by formulation exports - up 76% and overall domestic business up 13%.
- Domestic formulation growth of 13% was partially due to restocking benefit of VAT.
- The PBIDT was up by 14% to Rs. 774 million - this is after a 44% year-on-year increase on R&D expenses.
- The PAT is up 46% to Rs. 479 million.

Coming to the consolidated number for Q1

- The consolidated net sales is up 11% to Rs. 3653 million.
- The PBIDT is 8% lower year on year at Rs. 674 million.
- In line with the net profit is also lower by 2% at Rs. 342 million.

The consolidated profit suffered due to lower contribution from Altana JV due to several reasons.

- The expansion related closure of plants for two months
- lower sales
- the Euro depreciation leading to lower realization in rupee terms, and also the ERF (loss) on the Euro deposits on hand.

The capacity is now expanded to 56 tons each for the 2 intermediates from 48 tons. Simultaneously, there will be also a slight price adjustment, but the overall profit will be protected other than (for) the Euro depreciation versus rupees.

As far as French operation is concerned, the planned losses of the French subsidiary was Rs. 57 million, although higher y-y, was lower sequentially.

Before we start the Q&A session, as promised during the last conference call, I have an update on progress made in respect of contract manufacturing activity.

During the quarter we signed four new contracts with (aggregate) peak revenue potential of US\$ 13 million s or approximately Rs. 550 million. The cumulative number of contract signed up to the end of the quarter is five , excluding the joint venture we signed with Mayne Pharma.

Thank you very much, and we will now start the Q&A session. You may address the question on domestic market and non-regulated market to Mr. Nayak. On results and finance to Mr. M. K. Patel. On regulatory market to me.

Over to coordinator for Q&A. Thank you.

Moderator.

Thank you very much sir. We will now begin the Q&A interactive session. Participants who wish to ask question may please press *1 on you touchtone-enabled telephone keypad. On pressing *1 participants will get a chance to present their questions on a first-in-line basis. Participants are requested to use handsets while asking a question. To ask a question please

press *1 now. We have our first question from Ms. Monica from Quantum Securities.

Monica

Good evening Sir. Could you just repeat the sales and profit figures of your French subsidiary please.

Leena

The sales for the quarter which is April-June 2005 quarter, is Rs 13.4 crores, and there was a net loss of Rs 5.7 crores.

Monica

Okay. If you could also give us some update on your ANDA filings, how many you have done till date?

Pankaj Patel

During the quarter, we have filed two ANDAs additionally, so now the number stands at, total filling at 26.

Monica

Filing totally is 26, out of which you have received 5?

Pankaj Patel

5 approvals.

Monica

You can give a timeline on how do you expect this to pan out, approvals coming in?

Pankaj Patel

We expect another 4-6 approvals during the year, minimum, and we expect to launch between 5-7 products during this year in the US market.

Monica

Okay, and these are all generics or they are going to be future generics going further?

Pankaj Patel

They are all generics.

Monica

Okay, thank you.

Moderator.

Thank you very much madam. Participants who wish to ask question may please press *1 now. We have our next question from Mr. Ravi Agarwal from JP Morgan.

Jaisal

Good evening. This is Jesal on behalf of Ravi. I just have a couple of questions. Firstly on the French subsidiary you mentioned current quarter number at Rs 13.4 crores sales and losses of Rs 5.7 crores, I wonder if you gave the previous year's comparable number and also the preceding quarters comparable number?

Leena

Okay, Jaisal, actually you have to bear in mind that for the Q1 2004-2005, the quarter was January-March quarter. The number was Rs 5.6 crores of sales and net loss was Rs 2.1 crores. For the previous quarter, which means the January-March 2005 quarter, the sales was Rs. 10.4 cr and there was a net loss of Rs 10.8 cr. Basically the loss has come down q-q or sequentially and the sales have gone up.

Jaisal

Right. The second question is, could you give us some idea about the market share in simvastatin in France?

Pankaj Patel

Currently, on launch, it is couple of months now and we have achieved about 4.7% market share in France.

Jesal

Can you give us some idea about the pricing prevailing now?

Pankaj Patel

I do not have the exact number Jesal just now in front of me about the exact prices of simvastatin, when it was launched the prices were significantly lower and the discount were ranging in between 70-80%, but currently I do not have the latest update on price.

Jesal

Can you give us some sense on how many more products you plan to launch in France out of your own pipeline or how many you have filed in the current quarter?

Pankaj Patel

During the year we plan to launch few more products to bring the total number of presentations to 80-90, and these will be coming out of our own filings as well as the products for which we already have approvals, plus some of the products we are getting from the third party.

Jesal

Right, and how many products have you already filed in Europe?

Pankaj Patel

At this moment, we have filed up 4 products in Europe, and we have target to file 12 this year.

Jaisal

The last question is on your Altana JV, actually I missed the explanation which you gave in terms of why the sales is lower than in the preceding quarter. I just got one aspect which is the Euro depreciation, and I missed the other part...

Pankaj Patel

Okay. During the quarter the plant was shut down for about two months for increasing the capacity, so the capacity which was around 48 tons has been expanded to 56 tons as a result, and the plant has already been re-commissioned. We had a lower sale during the quarter because of lower lifting by Altana during the quarter of the intermediate, compared to last year. Also there is a lower rupee realization because the Euro depreciated between 7-8%. We also had a substantial amount in foreign currency, Euro currency in our deposits, and because significant loss of Euro we (JV) have lost around Rs. 4.5 crores because of foreign exchange loss. And of course because now we are expanding the capacity, going forward there will be slight adjustment in price in order to maintain the same profitability in terms of absolute amount. However, if the

Euro shows the same kind of trend, we expect some kind of profit erosion happening in terms of that, because up till now we were gaining because of Euro appreciating all the while, and this time, the first time we see the Euro has depreciated by about 7-8%, which has impacted the profit. If this trend continues, then this could impact the number by the similar percentages. So if I give you Jaisal very clear indication, we expect the profit this year, our contribution to about Rs. 60 crore. However, if the Euro depreciates then we expect that the profit to come down by 7-8% as which is today. If the Euro appreciates back then the impact could be negligible.

Jesal

How much was the profit in the first quarter?

Pankaj Patel

Total profit for the first six months is about 45 crores, our share.. no sorry. There is no 6-monthly number available, but if we take the first, because this is the first quarter and we are merging quarter to quarter, if you are going to take the number.... The numbers Leena can you give

Leena

The profit contribution against our 50% share from Altana for this quarter is Rs. 6.6 crores, and the sales was Rs. 14.2 crores.

Jesal

So, the erosion in margin is partly because of the Euro depreciation, are there any other reasons why the margins have dipped?

Pankaj Patel

As I told you we have the substantial currency in the bank in Euro and that also depreciated, so we (JV) had a foreign exchange loss of Rs. 4.5 crores. Plus, during the two months when the plant was shut down, the overheads were still there but we did not produce anything.

Jesal

Okay, just a last question on how many ANDAs you have filed in the current quarter?

Pankaj Patel

We have filed 2 ANDAs during the quarter.

Jaisal

Thanks so much.

Pankaj Patel

Just to give you update on what has been said and I did not highlight it, but during the quarter we initiated our first shipment to US, so end of the quarter in the month June, on 24 June actually, the first shipment of the finished dosage forms which was Ateolol was shipped to US, and we expect the revenue from US to start coming from this quarter onwards.

Moderator

Mr. Patel we can take the next question.

Pankaj Patel

Yes.

Moderator

We have our next question is from Mr. Rahul from Karvy Stock.

Rahul

Sir, just a query on Altana, wanted to know how the sales will pan out in the remaining three quarters, you have done 14 crores, will it be commensurate to the quarter 15 crores or....?

Pankaj Patel

No, it will be on higher side. This quarter, as I mentioned before, has a lower sale, which we do not expect in the next quarter. As per the plan we expect the sale to be on the similar line as has been in the past.

Rahul

Sir, how much of sales have you recovered from due to VAT in this quarter?

Pankaj Patel

This is to the extent of about Rs. 23 crores.

Rahul

What is your view on the remaining nine months, what type of growth you are looking at for the domestic formulation?

Pankaj Patel

Mr. Nayak would you like to take this question?

Mr. Nayak

Yeah, see for the second quarter, let me first go to the first quarter. Actually our growth could have been slightly better but for two reasons,

- one is on the generic front as compared to the sales we had in the corresponding quarter, we had a decline unlike in the formulations where we had a good growth, that was because, you know, because of this excise on MRP, most of the manufacturing is being shifted to Baddi, and that transition time for the generic business to, for us to get the generic products manufactured from these excise benefit zones took some time. So that is why, we are now gaining that up in the second quarter. So we lost out during the first quarter on that and our generic business is not very small.
- The other is on vaccine front we are increasing our capacity, so that is why we lost around Rs. 2 crores sales though we had the orders. Also, one of our product Rivaldo, which is COX-2 inhibitor, because of the withdrawal of that we lost around Rs. 1.8 to 2 crores sales. So that is the justification for the last quarter.

Coming to the second quarter looking at the numbers of the second quarter last year, we expect a growth of around 9-10%.

Rahul

Sir, you are planning to year you will be ending with 10 odd percent growth in domestic formulations business?

Mr. Nayak

The growth should be slightly above 10% for the year.

Rahul

Sir, US sales will be reflected in coming quarters? The entire basket will be launched or is it only Atenolol which is going to be launched?

Pankaj Patel

We are launching two products for the quarter, so we have already shipped, as I mentioned the first shipment happened and the another shipment are being done now, so in this quarter we will see the first US revenues coming in, and that will be two products for this quarter and then by the next quarter we should add couple of more.

Rahul

What is the outlook on your API front, on export front we have seen a de-growth, are we planning to recover? Is it mainly due to the Altana JV or apart from that something else has also contributed to the decline?

Pankaj Patel

See, API on standalone business itself has shown a decline as far as export front is concerned, and that is the industry wide phenomenon where the price erosion has basically significantly contributed to this decline. Our understanding and the trend as we see, we think that we are now getting into the bottom and we expect that now the sales to be stabilized, and third quarter onwards we are looking at growth on API business.

Rahul

Okay. But you all will be able to do what you all had done last year or you will see some decline?

Pankaj Patel

We would be able to match the sales number as we did last year.

Rahul

Okay sir. Thank you sir.

Moderator.

Thank you very much sir. We have our next question from Mr. Ajay Sharma from CLSA.

Ajay Sharma

Good evening Pankaj Bhai, I am actually calling from a mobile phone, so there may be some problems because we cannot get through landline in Bombay.

Pankaj Patel

I hope you are not locked up in water.

Ajay Sharma

One thing is this deal that has happened between Teva and Ivax, how do you see that from being a leading company share of changing the structure, and what steps we as Indian management need to take on that?

Pankaj Patel

A very interesting question Ajay. As I see this major leading, what is happening is, larger and larger generic players are being created globally, so more and more as we go forward size is going to matter for success of generic business in all markets. As a result of this merger, which is a significant initiative by Teva, and that would basically generate into lot of disruptive practices in the market place, which could be a significant opportunity for newcomers like us, and Indian companies in particular, and there could be opportunities here to really do things because this integration is going to be a major initiative for Teva and it is going to be a much more challenging. Another merger which happened few months back, we are already seeing some results of the problems linked with the merger usually gets into, and considering that we are seeing a opportunity in short term for companies. Also there to be some competition issues of the common product between

the two and the market share issues from the competition law point of view in both Europe and US, and there could be some divestment opportunities here where Indian companies could be looking at opportunities to grab something out of it. However, long-term message is clear, scale is going to matter, and larger the size better it is for everybody.

Ajay Sharma

Okay, just then on the scale front since you are saying that size would matter as Cadila you would want to grow bigger and acquire companies globally. Do you think yourselves or Indian companies in general have the management bandwidth to acquire any integrate big companies?

Pankaj Patel

I believe we have the capabilities to do this. We have created enough reputation in terms of quality of management internally and also externally, and given the opportunities we could also attract enough talent to take on this challenge, that is what we believe.

Ajay Sharma

Finally, just one thing on your plan B in terms of US generic market, because one question that we have raised, especially say Cipla had an alliance with Ivax, and now that Teva acquires Ivax given the overlap that Cipla would have, we do not know how that alliance will phase out. Suppose hypothetically Mallinckrodt gets divested by Tyco and some big company acquires it, how will be your game plan if that contingency were to occur?

Pankaj Patel

First, I think it is a speculation, we don't know, but just assuming that what you are saying is going to happen, we are already building our own sales. We are already supplying products at this moment directly to few customers, and we expect that sales between us and Mallinckrodt is going to be in the vicinity of about 50:50. So, I am seeing clearly that we would be prepared eventually if something is going to happen of what you described.

The second point is that, we don't know who is the new partner and what kind of opportunities could be there as well. So, there could be even opportunities there itself.

Ajay Sharma

Anyway your product with Mallinckrodt has your branding, it is co-branded right?

Pankaj Patel

Number one, it is co-branded so it is already branded as us. And we also are selling ourselves in US. So, the consignment which we have shipped is also for Mallinckrodt and also for our own sales, and which is also going to be on the market and we have signed contracts to supply to major customers directly.

Ajay Sharma

Okay. So, you don't see that as much of a risk because....

Pankaj Patel

We do not see as much of a risk this kind of eventuality.

Ajay Sharma

Wonderful. And just last question Pankaj Bhai is on the four contracts that you signed, the contract manufacturing, what is the outlook for the full year, and in three years say what is the kind of revenues you can generate from these?

Pankaj Patel

I did tell you that peak revenue we expect is \$13 million per year, and that should happen definitely in three years' time. I do not have exact number of outlook of what kind of numbers which happened in this year, so I cannot say that. As I told you during the last conference call that we would be signing at least 8 deals this year, and you could see that we have already signed four deals in this quarter itself, and we are hopeful of overshooting our target.

Ajay Sharma

Okay. Wonderful, thanks a lot.

Moderator

Thank you very much sir. We have a followup question from Ms. Monica from Quantum Securities.

Monica

Sir, I just wanted to know if you could throw some light on what is the total capex plan that you for this year?

M K Patel

We have capex plan of 110 crores.

Monica

Okay. And does this include the Mayne JVs?

M K Patel

No. Mayne JV is going to be investment and not capex.

Monica

So you really don't have to..., what is your investment going to be like then?

Pankaj Patel

Well, we expect anything between Rs 10-20 crores, but we don't have the final number available as of today.

Monica

Okay. So, this plan is yet to be finalized.

Pankaj Patel

The plan has been finalized, the final numbers are being worked out. We would be able to give you exact numbers next month.

Monica

Okay. My second question is on your Baddi plant, what sort of production did you realize sales from this plant in this quarter?

M K Patel

Baddi, we are now averaging sale of about Rs 22 crores (per month), so total sales out of Baddi was Rs 61 crores in the first quarter. And if you have seen our results, our excise has come down by about 1.6% in the first quarter, so that is the clear result of Baddi coming in.

Monica

We should actually have lot more benefits coming in the next 9 months with more production being transferred there?

Pankaj Patel

No, we are not going to transfer anymore products, I mean, we are working at full capacity now.

Monica

Okay. You could also repeat the figures for Altana, I think the profit contribution was Rs 6.6 crores.

Pankaj Patel

Leena just give you the number again.

Leena

The sale, that is, at 50% contribution, this is our part of the JV, was Rs 14.2 crores , and PAT was Rs 6.6 at our 50% contribution.

Monica

The Rs 6.6 is opposed to your 50% contribution.

Leena

6.6 is our 50%.

Monica

Okay. Thank you mam.

Moderator

Thank you very much mam. Participants who wish to ask question may please press *1 now. We have our next question from Ms. Shahida from IDBI.

Shahina

Hi, I just wanted to know what is the difference between the consolidated and standalone numbers for consumers and others in that heading under domestic consumer and other sales? And maybe what does this group comprise of?

Pankaj Patel

That is (difference is) Sarabhai Zydus sale.

Shahina

Okay. So Sarabhai Zydus sales is the difference between the two?

Pankaj Patel

Yeah.

Shahina

Okay. And what do you see the, could you give us some sort of feel of how you see this business going forward?

Leena

Which one, consumer or Sarabhai Zydus?

Shahina

Consumer.

M K Patel

Consumer is growing at around 24%, and it will continue to grow around the 20% during the whole year.

Shahina

Okay, thanks.

Moderator

Thank you very much mam. We have our next question from Mr. Surya from Capital Market.

Surya

Good evening sir. In fact, I have a question that still some states in India they have not implemented VAT because of that you are getting some sort of a threat currently?

Pankaj Patel

We do not see any threat because of that and I believe that it is matter of time when all the states would have VAT, but we do not see much of the threat at all because some states have not implemented VAT.

Surya

So, in the last quarter did you get some less sales or something happened because of that?

Pankaj Patel

No, not really.

Surya

Okay. That means you really got some Rs 24 crores sales recovery during the quarter?

Pankaj Patel

Yeah, we have actually, our sales have been higher to the extent of Rs 21 crores higher than the budget which we had

Surya

How much is that, 21 crores?

Pankaj Patel

21 crores.

Surya

Okay sir. Thank you.

Moderator

Thank you very much sir. Participants who wish to ask question may 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. Patel for final remarks.

Mr. Patel

Thank you very much for joining the investor conference call. I know that Mumbai is pouring heavily and I wish you all a safe journey back home.
