"Granules India Limited Q2 FY '20 Earnings Conference Call"

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MANAGEMENT: **MR. KRISHNA PRASAD CHIGURUPATI – CHAIRMAN AND MANAGING DIRECTOR**
MS. PRIYANKA CHIGURUPATI – EXECUTIVE DIRECTOR, GRANULES PHARMACEUTICALS, INC.
MR. SUMANTA BAJPAYEE – HEAD, CORPORATE FINANCE, TREASURY AND INVESTOR RELATIONS

Moderator: Ladies and Gentlemen, Good Day and Welcome to the Granules India Limited Q2 FY '20 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Sumanta Bajpayee. Thank you and over to you.

Sumanta Bajpayee: Thank you, Janice. Good Afternoon everyone and I welcome you all on our earnings call for second quarter of Financial Year 2020. I have Mr. Krishna Prasad Chigurupati, Chairman and Managing Director of Granules India Limited, and Ms. Priyanka Chigurupati, Executive Director of Granules Pharmaceutical Inc., with me to explain any business parameters and outlook. Before I start with the call, I would like to request everyone that we have shared the business breakup as well as other details through our investor presentation which is currently available on our website as well as it is available in the stock exchange. Please refer to the breakups so that we can continue to focus both on business-oriented and strategy-oriented questions during the Q&A session. I also would like to highlight here that some of the statements made in today's call will be forward-looking in nature. The safe-harbor statement contained in our press release is also applicable for this call. I now hand over the call to Mr. Krishna Prasad Chigurupati for his opening remarks. Thank you all. Sir, over to you.

Krishna Prasad C.: Thank you, Sumanta. Ladies and Gentlemen, thank you very much for attending our earnings call for the second quarter of this FY '20. During this quarter, we continued and built on the performance of Q1 achieving a stronger performance. This again validates our confidence in exceeding our target of INR 300 crores PAT for the current financial year and 25% CAGR in PAT over the next three years. In this quarter, we have achieved a revenue of INR 700 crores, which is 20% growth on a year-on-year basis. The revenue growth for H1 FY '20 was 25% on a year-on-year basis. The growth on a yearly basis was driven by higher sale of FDs and PFIs which stood at 34% and 37%, respectively. The FD growth was due to new launches in North America. FDs constituted 50% of the total revenue, PFIs 19%, and APIs 31%. North America was the key driver constituting 53% of the revenue followed by Europe and LATAM. The growth in North America was 39% on a year-on-year basis. Gross profit in this quarter has improved both on yearly and sequential basis. Gross margins have increased year-on-year by 3.3%. The increase is the outcome of increased revenues especially in the FD and PFI verticals. We are confident that our gross margins at this level are sustainable. We have achieved an EBITDA of INR144 crores compared to INR 101 crores, which is an increase of 43% compared to the same period last financial year. This shift in EBITDA is on account of a positive contribution across margin level with minimal increase in fixed operational expenses.

I am very happy to state that during this quarter, our EBITDA margin has grown to 20.5% as compared to 17.3%, which is very close to our historic high of 21%. We have targeted to achieve 19% EBITDA for this year whereas we believe we can maintain more than 20% for the year. Regarding net profit, this quarter does not have any share of profits from JVs, but our net profit for this quarter was still at INR 96 crores, which is a 59% increase from INR 60 crores during Q2 of FY ‘19. If we do not consider the INR 13 crore profit from JVs during Q2 of FY ‘19, the net profit growth would have been 103%. Current tax and deferred tax liability reversal put together has contributed INR17 crores for this quarter to net profit. Free cash flow during this quarter was INR 35 crores. Operating profit was INR158 crores out of which INR 15 crores was spent on working capital requirement, advance tax was INR 32 crores, dividend was INR 15 crores, CAPEX was INR 49 crores, and capitalized R&D was INR 11 crores. As compared to Q1 FY ‘20, working capital had increased by INR 21 crores due to increased sales, advanced taxes increased by INR 18 crores, dividend outflow increased by INR 15 crores as no dividend was paid in Q1. R&D capitalized decreased by INR 7 crores and regular CAPEX went up by INR 13 crores, so in the first half of the current fiscal we generated a free cash flow of INR 96 crores and we will definitely keep up the momentum for the balance of the year.

Gross debt by end of Q2 FY ‘20 was INR 928 crores as compared to INR 1120 crores at the end of Q2 FY ‘19. Net debt by Q2 FY ‘20 was INR 827 crores as compared to INR 1,008 crores at the end of Q2 FY ‘19. Net debt to EBITDA by end of the current quarter was 1.6 times as compared to 2.9 times by end of Q2 FY ‘19. We are already close to our year-end target of 1.5 times and are confident that we will keep on improving on this metrics. ROCE at the end of quarter after current quarter was 21.7% while considering the JVs as compared to 17.6% by end of Q2 FY ‘19. Cash-to-cash cycle was 106 days during the current quarter as compared to 112 days by the end of Q1 of the current fiscal year. The total R&D expenses for this quarter were INR 30 crores compared to INR 25 crores during the same period of the previous fiscal year. It stands at 4.28% of sales for the quarter. Out of the total R&D expense, we have expensed out INR 19 crores and the balance INR11 crores was capitalized. I am happy to inform you that we have delivered an improved EBITDA margin despite increased R&D expenses. We have received approval for one ANDA in this quarter and filed for two. As it stands today, there are a total of 22 filed ANDAs awaiting approval. We expect to receive four to five approvals by the end of the current fiscal year. We had launched one product from GPI during this quarter.

On the JV front, in order to strengthen our current strategy and focus on our core capabilities and generate free cash, we decided to exit both our joint ventures. Regarding Granules Omnichem, we felt CRAMS is not our core strength and getting out of this will help us in focusing on our current strategy which had evolved differently from the time of the beginning of the JV. We entered into an agreement for this divestment for a consideration of INR109.85 crores and filed for permission to the Government for the divestment and expect to close the transaction during Q4. Regarding Granules Biocause, we entered into this JV in the year 2007 to ensure a consistent supply of ibuprofen API. The JV had worked well all these years and in times of shortages, we got benefited by these supplies. However, the ever-increasing environmental compliance standards in China had led to the JV investing heavily in CAPEX in the past and also currently as we speak. We expect the CAPEX to continue in future too. The current focus on reduced CAPEX and increased free cash flow led us to this decision.

Our Board has recently approved exit from the JV and we will be starting discussions with our partners on the valuation shortly. We have a supply agreement with the JV and do not see any supply issues even after divestment. Moreover, ibuprofen supply had softened and manufacturers in India have increased capacities. We also have other sources approved for most of our products. Our decision to exit the JV will not impact our commitment to achieving our profitability targets, but will help us in generating free cash and a reduction in the Net debt. At GPI, our US subsidiary, we achieved a revenue of INR 63 crores, an increase of INR 36 crores on the corresponding quarter of the last fiscal. EBITDA stood at INR 7.8 crores and PAT at INR 4.8 crores. On the pledged shares, since our last call, the pledged shares as a percentage of the total shares I own, had come down from 43% to 37%. As a percentage of pledged shares to the total outstanding shares of the company, it currently stands at 16%. Currently, I am in the process of repaying some more amounts and we will see a dip shortly. With this, Ladies and Gentlemen, I would like to open the call for questions.

Moderator: Thank you very much. Ladies and Gentlemen, we will now begin the question and answer session. We take the first question from the line of Ashwini Agarwal from Ashmore. Please go ahead.

Ashwini Agarwal: Sir, my heartiest congratulations on a wonderful set of numbers, it is truly heartening that everything that the company has been working towards over the last few years is now starting to become visible such as improvement in return ratios, improvement in asset turn ratios and return in equity ratio, so many, many congratulations for that and for generating the FCF and paying down debt. So I had couple of questions, one is that we have obviously seen a significant reduction in your working capital days or cash conversion cycle down to 106 days and if I look at the trend over the last several years, this is the lowest number that I have seen. Is there something one off that is driving it. What should be the sustainable number of days that we should use as the cash conversion days?

Krishna Prasad C.: Definitely, there is no one-off Ashwini, it has been a constant effort that we have been putting on and this is showing results. We are working on reducing our receivables days and also concentrating on inventory control and if you actually see the inventory days are 54 days as compared to 59 days, receivable days reduced from 115 days to 102 days and payable days stood stationary at 50 days, so the cash cycle has come down due to all these efforts and we are striving our best to make sure we will be able to reduce this a little better as we go by.

Ashwini Agarwal: The other thing is that I was just trying to figure out thanks to your opening remarks on the exit from the JV, regarding your Biocause JV. You said that you will be commencing the discussions shortly. Do you think that it will be possible to exit in the current financial year or do you think it might stretch a little bit longer?

Krishna Prasad C.: No, we are fairly confident we will be able to close this by Q4. Both JVs will be able to close by Q4.

Ashwini Agarwal: If I am not mistaken, this should actually significantly improve your return ratios further because roughly these two assets which are showing up as assets held for sale as of September 30th will take away about INR 200 crores worth of assets from your balance sheet and the return ratios that we are seeing at least in the September quarter are without any contribution from the JVs, so this should further help to bolster the return ratios. Would that understanding be right?

Krishna Prasad C.: Ashwini, it will definitely help us to do that.

Ashwini Agarwal: What is your plan. You will get roughly say 110 odd crores from your first JV which you already concluded, I do not know the amount for the second JV, what is the plan for the cash utilization, payment of debt, or do you have any other application of these funds in mind?

Krishna Prasad C.: We just would like to hold the assets and fixed deposits and generation of Treasury income rather than paying down debt. Debt as I have always mentioned is cheaper than the income we will be making on these amounts and then going forward, this will effectively reduce our net debt, but going forward we will see where, what we should do with this amount. But currently we do not have any plans for CAPEX.

Ashwini Agarwal: Sir, my next question is if I look at your gross margin profile, your gross margin profile on a quarter-to-quarter basis is reasonably volatile, I mean we have seen a number which is as low as 43% in Quarter-3 last year and then we saw 50% in Quarter-1. I mean is it just a revenue mix or is there an interplay of raw materials also here because what we are hearing from many other people is that raw material tightness that was prevailing in China is causing a lot of disturbance seems to have abated significantly. So how should we view this number. You are in the vicinity of 50% or so for the first half this year, how will this number look on a sustainable basis?

Krishna Prasad C.: Ashwini, the 45%, 43% gross margin we were making in the past was mainly due to the ever increasing prices at that period of time of raw material. However, the raw material prices are stable now and in a few cases that is coming down, but that does not necessarily improve our margins because the sale from our side also will slightly go down. Last quarter, we had a gross margin of 50% and this quarter it went down slightly to 48.6%, which is mainly due to the product mix. We had more sales of APIs in India and then we sell in the domestic market, the margins are low and if we have more sales to export markets the margins would get better, but however I am sure we will definitely manage and sustain our margins of around 48% going forward. I do not see any risk of that going down.

Ashwini Agarwal: Sir, last question from my side before I fall back in the queue, the other income number of INR 8.7 crores, could you give me the breakup of that?

Krishna Prasad C.: It is about INR 2.6 crores on account of Forex and we had the settlement where on a litigation with the company in the US for one of our products and as part of the settlement where we agreed on a launch date, they had given us INR 4.2 crores as compensation and rest of the money is from Treasury.

Moderator: Thank you. We take the next question from the line of Tushar Bohra from MK Ventures. Please go ahead.

Tushar Bohra: Just couple of points. First, if you see even quarter on quarter, there has been a very sharp buildup on the core business. I believe your PAT on the core business was about INR 60 crores in Q1, which is now INR 96 crores. If you could just help us qualitatively understand where this difference has come in the business and how sustainable is it or is there an element of seasonality or a one off or a spillover between quarters. How sustainable is this delta that has come up and from a guidance perspective qualitatively?

Krishna Prasad C.: Definitely, it is sustainable, and the growth has been mainly due to growth in markets of US and Europe and also Finished Dosages and PFIs. As you are all aware Finished Dosages and PFIs have better margins and that is what has contributed to the increase in profit and also increased revenues with the same or a little more overhead have contributed to this extra margin. From here on, every increase in revenue would contribute at least 40% or 35% of the bottom line, so the key is to keep growing a little bit or at least maintaining the levels here and that will definitely sustain the margins.

Tushar Bohra: As in the increase in formulation revenue, is it been driven by your existing core molecules say metformin or paracetamol or is it being driven by the new launches. If you could just help us understand where the Delta has come from in formulations also?

Krishna Prasad C.: It is mostly from existing molecules and where we have added it is just not five, we have been adding a few more products into this core strategy where we are integrated from API to FD. So that is the main thing, but we have also got good gross margins from new launches in the US, however, we have been getting ready to scale up operations. We have been hiring people, so the overheads there have gone up, so net margin from GPI has not increased, so mainly it comes from the core molecules. Also there is another thing, the margin has also improved due to partly the reduced taxes and the effective tax rate where there was also a little deferred tax income.

Tushar Bohra: Sir, has the metformin new capacity for which we got EIR last quarter, is that operational now and is that reflecting also in the overall margins or should we expect the benefit from that to take going forward?

Krishna Prasad C.: It is operational and maybe it would have been about 15 days of benefit we would have got from that in the past quarter. But this quarter, we will get the full benefit of the new capacity.

Tushar Bohra: Sir, let us say we did about INR 60 crores in Q1 about INR 96 in Q2 so about INR 155-INR160 crores vicinity in H1. Your guidance for the full year was 300. I think that was including the JVs at the start of the year. Right now, if we analyze the H1 number we touched 300 without the JVs. If we analyze Q2 number, we are significantly higher than that 300 guidance, so what would be the revised guidance from the management. What should we look at when we are trying to project for '20 and '21?

Krishna Prasad C.: The Q1 had the JV income, Q2 does not have JV income.

Tushar Bohra: The INR 60 is without JV is what I am considering.

Krishna Prasad C.: Yes, you are right. We will sustain this profit even without the JV and we are very confident that we can easily cross the target PAT of INR 300 crores.

Tushar Bohra: Sir, when we say sustaining are we looking at Q2 number as baseline number now or are we looking at Q1. What should be the baseline number for core business when you are say sustaining?

Krishna Prasad C.: Core business, I would say it is somewhere in between. We will grow but would we grow at the same rate quarter on quarter. I am not sure, but definitely getting that 25% growth in PAT, I do not see at all as a problem. Hopefully we can do better than that.

Tushar Bohra: Sir, can you also throw some light on the Oncology block. What is the status now?

Krishna Prasad C.: Oncology again it is a long-haul process. We have been filing DMF for APIs and we are also working on formulations and also we are discussing with certain companies for doing contract manufacturing. So all these things will fall in place only into the next fiscal and we can expect some revenue in the next fiscal. But I think the fiscal '22 would be a proper year for generating profits from the Onco facility.

Moderator: Thank you. The next question is from the line of Nitin Ranjit from Capstocks. Please go ahead.

Nitin Ranjit: My question was with respect to the Biocause exit which we have recently concluded. So how much of our PAT last year was it contributing to?

Krishna Prasad C.: When we work on the actual numbers, vaguely I would say our share has been INR 44 crores for the whole year.

Nitin Ranjit: Sir, again this question arises. Have we decided to exit these JVs because the ibuprofen prices have kind of softened over the last four to five months and you yourself have said that. So is it because our JV has decided to further expand our ibuprofen API capacity over in China. Is that the reading one must get from that?

Krishna Prasad C.: The main reason Nitin is there is a lot of investment going. When we started the JV, we started with a very low amount, so whatever that was being generated as profits over all these years had gone towards building up working capital. Initially, the working capital was given as a loan by our partner, so as we had some profits. We were building up working capital and then in the last few years, the environmental standards, compliance standards in China have become very tough and continuously they are becoming tougher and tougher. We took a shutdown last year. We spent a lot of money on building a new effluent treatment plant and it met the compliance standards, but within six months the Government comes back with tougher standards. Again, we took a shutdown recently and we again spent a lot of money. So there is a lot of uncertainty going on in China. So they may still tighten the standards and in some places they may even want to shut down some facilities even though you are clean. They say this entire area has to be free of industries, so they have something called the blue sky. A lot of uncertainty happening there, so under these circumstances we felt it is not a good idea and the idea of getting into JV was to get a security of supply for our API. So the JV has served its purpose. Many times during the long period, during periods of shortage, the JV was able to support us and we benefited drastically by having ibuprofen. We were able to get good market share in the US just because we had access to the API. Today that does not stand as important as it was before because lot of expansion is going on in India and outside India and India there is almost like more than doubling of capacity that has happened and we have also improved other sources for our formulations and we do not see supplies as a major issue. Moreover, biocause, the JV we have a supply agreement and supplies would continue to come from the JV, so we do not see any risk. That is the reason we felt that when there is no cash being generated and coming to us as profit. we felt we should exit it and whatever proceeds come from the sale would help us in reducing our net debt and building up cash in the company.

Nitin Ranjit: But Sir since we have exited the JV, do we have any plans for building up additional capacity domestically for ibuprofen API because we have already exited the JV right. So are we planning to increase the capacity of ibuprofen domestically on our own. Do we have any plans for that?

Krishna Prasad C.: Right now, we have no plans to start manufacturing ibuprofen because there is already a surplus capacity that has come up. However, we would be entering into some sort of understanding with a few suppliers on pricing and supply, that is what we would do. But definitely we do not have any plans right now.

Nitin Ranjit: Just one last question Sir. We had launched our generic ibuprofen formulations in the US in the year 2015, so how much sales does that product actually bring us?

Krishna Prasad C.: Nitin, I cannot share the revenue number, but all I can tell you is we have about 35% of the US market.

Nitin Ranjit: Fair enough and since now that we are a customer how do you see the ibuprofen prices moving from here? Because we are no longer in the manufacturing game, so what is your outlook on that because BASF kind of restart their facility in Texas? So how do you view the overall market situation in ibuprofen?

Krishna Prasad C.: Ibuprofen prices have already started softening and they can only soften as we go by and definitely we will see improvement in the next few quarters.

Moderator: Thank you. We take the next question from the line of Chirag Dagli from HDFC Mutual Fund. Please go ahead.

Chirag Dagli: Sir, what is the tax outflow for the divestments that we will do in both these JVs? Is there a tax angle to it?

Krishna Prasad C.: There would be a tax angle because if you see the Biocause JV, we invested only INR18 crores in 2007 which is like 12 years ago. There will be long-term capital gains and it also depends on what we agree as the valuation between our partner and us and the same thing with Omnichem JV. There also we invested about INR 43 crores and since we are getting about INR109 crores now, on the balance there will be a long-term capital gain and I think it will be around 15%-20% long-term capital gains.

Chirag Dagli: Sir, is there a guidance for depreciation that you have for the next year because next year you will have to sort of take amortization on some of the capitalized R&D as well as the new CWIP as well. So some thoughts there?

Krishna Prasad C.: Definitely Chirag, yes, we know what is coming ahead. We would just stick to our guidance of 25% CAGR over the next three years that we are very confident and we can achieve and maybe they can do better.

Chirag Dagli: Sir, what is the capitalized R&D for first half of FY '20?

Krishna Prasad C.: First half of FY '20, out of INR 64 crores it is INR 29 crores.

Chirag Dagli: Should we extrapolate this for the full year, Sir?

Krishna Prasad C.: It will be more or less the same. We go by a formula, but I do not think it will change.

Moderator: Thank you. The next question is from the line of Tushar Manudane from Motilal Oswal Securities. Please go ahead.

Tushar Manudane: Sir, just to the formulation segment where you referred the growth has been coming from the core molecules. The good part being that it has been now three quarters where the volume growth itself has been at a number of 25% on year-on-year basis plus driven by the double-digit price growth. So this core molecules being the matured molecules in the respective markets, just would like to understand the sustainability of such kind of growth?

Krishna Prasad C.: If you have seen the last few years, there has been a steady growth in the core molecules and again the definition of core molecules is in the past we had just five molecules. Today we have eight which we call core, so these are also increasing. It is in addition to the core molecules and also growth on the initial molecules that is driving this and we are very confident it is sustainable. We are a very efficient manufacturer and we are able to compete in the market and this will be sustained.

Tushar Manudane: So this is coming from more of a market share gain or it is like the inherent growth in those markets?

Krishna Prasad C.: It is partly market share and partly addition of new molecules. I said we have added three products. It is a mix of both, and also partly geography addition. In other geographies also we have started selling a little bit more, it is a combination of all these.

Moderator: Thank you. The next question is from the line of Prateeksha Malpani from Equirus Securities. Please go ahead.

Prateeksha Malpani: I had a question regarding core molecule, can you please throw some light on which is the key contributor to the core molecule business growth this quarter?

Krishna Prasad C.: Are you talking of products or are you talking of any other factor?

Prateeksha Malpani: No, I am talking about the products. Which of the molecule, can you throw some light on that? Which molecule is the key contributor to this growth?

Krishna Prasad C.: I am sorry, this is sensitive information and in the last few calls we mentioned that we would not be able to share this.

Prateeksha Malpani: Apart from that as you mentioned previously in the call that ibuprofen prices have started softening. So what is your outlook on the pricing going ahead? Will it stabilize around the current level or will we be seeing more softening going ahead?

Krishna Prasad C.: There will be more softening going ahead. We see prices coming down.

Prateeksha Malpani: Apart from that, one more question. What is the update on the ramp up in the new facility?

Krishna Prasad C.: The new facility if you are talking about GPI, yes, it is getting commercialized and we have increased GPI in the US. They are increasing capacities and preparing for new launches. We expect four to five more product approvals in this fiscal year and we are getting ready for that. However, if we talk of the Unit-5 in Vizag, which has gotten Onco and a multipurpose facility, the ramp up is going slow. It is a long haul and like I have answered the gentleman before, we will expect to see some revenues in next fiscal, but proper revenues and profitability in fiscal '22 and we have taken all that into account for our target of INR 300 crores plus.

Moderator: Thank you. We take the next question from the line of C. Srihari from PCS Securities. Please go ahead.

C. Srihari: Firstly, if I look at the sales mix, the share of FPIs and FDs is that 69% and even the capacity utilization is close to 70% for both the verticals. So don't you see this as a challenge and what could be the optimal levels in terms of capacity utilization? Secondly, regarding Biocause, is there any number here in mind, the first one was done at 2.2x book, so do we have any kind of a target for that and how would it impact the pricing? I have presumed the pricing policies may change once we exit the JV, so what is the implication of that? And thirdly, you mentioned litigation settlement is 4.2 crores. So if you could please throw some light on that?

Krishna Prasad C.: Let me address the Biocause first. The price we have an agreement where we will be the lowest the JV supplies to and whatever has been happening now, the same policy will continue and we do not see any increase in prices. And regarding the sale value, it all depends on many factors, so there are many issues there, the uncertainty is an issue and so the partner also may not be very excited about giving us a great valuation, but definitely I can say it will be a decent valuation and we will see once the negotiations are over. Maybe in the next quarter, I will be able to share the number with you.

C. Srihari: Will it be on par with Omnichem or better?

Krishna Prasad C.: Let us not make some guesses. The settlement is a little confidential between both of us. I do not think I will openly share this, but Priyanka I think can throw some more light on this. You want to explain where they can get information if they want to?

Priyanka Chigurupati: It is just available in the public domain if you do a little bit of digging, but because of the CDA we have in place with the company that we settled with, we cannot give you more information at this point.

C. Srihari: At least what is the addressable market size? What is the launch timeline? How many settlers are there?

Priyanka Chigurupati: Again, the launch timeline and such are details that are confidential between us and settler. The addressable size of the market is about INR 60 million in brand and generic put together.

C. Srihari: And you are the only settler?

Priyanka Chigurupati: Again, I do not want to give you more information Mr. Srihari. We have been bound by CDA.

Moderator: Thank you. The next question is from the line of Nimesh Mehta from Research Delta Advisor. Please go ahead.

Nimesh Mehta: Just a question for my understanding. Why have we not booked the JV profit this quarter because we already have it still in the balance sheet? What are the reasons of that not beginning effective this time?

Krishna Prasad C.: Nimesh, by accounting standards, I understand that anything where you have decided to sell is treated as an asset for sale and as an asset for sale and accounting standards do not permit us to take the income into our accounts. Again let me explain. We have not been getting any dividends or income from the JV, whatever profits that are coming in are being shown as it is mainly a book profit, so we thought it is better that we go ahead and divest.

Nimesh Mehta: That I understand, just trying to understand the accounting part of it?

Krishna Prasad C.: Accounting, our auditors have advised us not to take it into account and moreover we do not want to add on to more paper money. It is not real cash.

Nimesh Mehta: Till the time which is held as assets for sale, the book profit which is not a cash profit will be booked in those assets or something like that. How will you treat the book profits? You said there was a book profit, I mean the last quarter we had shown some INR 13 crores of book profit from the JV that used to generally come to us on a regular basis, so now that the assets are held as assets for sale, that book profit whatever is generated in your name will be treated how or it will just be shown as nil from now on?

Krishna Prasad C.: That is what our auditors have advised us. It will be treated as nil. It will not appear in any form.

Nimesh Mehta: Secondly, just wanted to know the sales of US geography from the finished dosage if that is possible. I understand the US sales that you mentioned in the presentation includes API as well, so just wanted to know what is the sales from US from finished dosage and the growth in that if you can share?

Krishna Prasad C.: Sales of FDs in the US as a percentage of FDs. I do not have these numbers straight away but maybe Sumanta can. If you can get in touch with him he would be able to furnish that number, However, I am sure you are aware that the US has contributed a major percent i.e. 53% of our gross revenue.

Nimesh Mehta: How has the US growth been? If you can just highlight that. I mean a lot of the growth that we see in FDs is because of US. Is that fair understanding?

Krishna Prasad C.: It is from the US. Yes, you are right. US about altogether was about 36% and mainly from FDs.

Moderator: Thank you. The next question is from the line of Charulata Gaydhani from Dalal & Broacha. Please go ahead.

Charulata Gaydhani: My question was pertaining to fexofenadine. How much would be the market size and how would you compete with so many players in the market?

Priyanka Chigurupati: First of all, the market size at this point I do not have the exact details, but in terms of how to compete with competition is purely due to the fact that we are an integrated player. We do have a certain market share already in the US market because of the integration and we also have several other sources qualified. Now, we also have our own internal approval for our ANDA, so going forward we are going to strength our acquisition as a finished dosage supplier in the US.

Charulata Gaydhani: You have got approvals right recently?

Priyanka Chigurupati: Yes, our own ANDA we got recently and earlier we had licensed this product from another partner and we were manufacturing the product and selling to the market.

Charulata Gaydhani: So are you manufacturing in India or in the US?

Priyanka Chigurupati: It will be manufactured in India.

Charulata Gaydhani: How many ANDAs do you have pending approvals?

Priyanka Chigurupati: We have 22 ANDAs pending approval.

Charulata Gaydhani: Are there any limited competition products in those?

Priyanka Chigurupati: Limited competition, yes, of course most of our GPI products, about 80% of our GPI products have less than three to four players at this point.

Moderator: Thank you. The next question is from the line of Dipan Mehta from Elixir Equities. Please go ahead.

Dipan Mehta: Just wanted to confirm that the pledged shares was on account of the warrant issue which you made to the promoters. Is that the correct understanding?

Krishna Prasad C.: That is right. When we were doing expansion of our facilities, we were doing lot of CAPEX. I had to take some warrants and pay for that and to pay for that I had to pledge my shares. Again, I would like to reiterate all the money raised by pledging the shares has gone into the company.

Dipan Mehta: Sir, are you disclosing the top three or four drugs and much they are contributing to the turnover either segment wise or otherwise because product concentration is definitely a concern as far as the company is concerned?

Krishna Prasad C.: Product concentration, definitely the top five-six products contribute a majority of our revenue. But what has happened if you see the history over the last five to six years, we have been steadily growing in these molecules, even though there is a concentration, these are products of first-line defense where margins have been totally rundown and where people are not really excited about continuing in these products. Whereas with our efficiencies and backward integration, we are able to generate margins and the history shows that the risk of concentration is minimal. However, we continue to add more products like I said the five core products have now become eight, so in the same range of high volume products we will keep adding continuously. We have filed some more products and we will be filing for some more products and also our low volume products from the US also will start contributing to the entire gross revenue.

Priyanka Chigurupati: Just to add to that in terms of contribution from our core molecules, we are also expanding into different R&D, basically for example paracetamol, we had paracetamol 500, but now we have paracetamol 650. So within the core molecules itself there is multiple products that we are filing and expanding the number of products that we have been marketing. In metformin, we had metformin IR earlier, now we have metformin XR and we have some more products going forward. In addition to all this, we are also expanding the presence of our core molecules across geographies, so we are also mitigating our concentration in the US for the core molecule. But to answer your question, in addition to these products of first line of defense, I think we are pretty well protected.

Dipan Mehta: One last question about the CAPEX for this year that is fiscal '20 and if you can talk about your plans for the next two to three years as well?

Krishna Prasad C.: Two to three years is a little difficult, but as a policy we have decided to not to have any CAPEX in the short-term. But going forward without any CAPEX, it is just not possible to have growth at which point of time we will do more CAPEX is what we will decide as we go forward. However, total CAPEX so far for H1 has been INR 84 cr as against our guidance of INR 150 cr and we expect to be within the INR 150 cr or a little slightly above or around that number.

Moderator: Thank you. The next question is from the line of Ashwini from Ashmore. Please go ahead.

Ashwini Agarwal: Just looking at your revenue guidance and the limited CAPEX that is coming through, the ratio of revenues divided by capital employed or capital turns, which is currently at about 1 should go up to 1.2 or 1.3. Given the business that you have built over the years, we have seen this ratio at a peak of 1.4 back in 2014-15 which progressively came down to 0.8 or 0.9 because you had a lot of capital work in progress. So alluding to the earlier question that you answered, at what point are you comfortable that your capital turn should not go up beyond such a number because then you start compromising on future growth prospects, so are you comfortable with 1.2-1.3 and then CAPEX starts to kick in. How do you think about these numbers?

Krishna Prasad C.: More than asset turns, asset turns is the right way of looking at it. But the way I look at it is I look at capacity left over for the next one year or one-and-a-half years and I plan at least if I think I am running out of capacity one-and-a-half years from today, maybe in the next six months I will start construction or investing into CAPEX and mostly these CAPEX will be on line balancing. We may not make a new building, we may just get some equipment. In the same footprint, we may remove inefficient equipment and put some high capacity equipment in there, so that will reduce your CAPEX and yet generate more revenue and more output, so maybe sometime during next year, we may look at some CAPEX, we will see how it goes. You are perfectly right. We cannot risk future growth by restricting our CAPEX. It all depends on our cash flows and other things, and there is a reason to be comfortable and yet comfortable as we go by. On this again, Ashwini, I would like to say we still have enough capacity left, but we expect to ramp up our sales also, so depending on how the ramp up is happening, we will decide on CAPEX.

Ashwini Agarwal: Sir, continuing with that thought if I look at your first half number, your revenue to capital employed is roughly 1x. I mean if it goes to 1.2 or 1.3 x which is what your guidance of 20% revenue growth over the next couple of years suggests and if you take into account that your profit growth guidance is 25% per year that means your capital utilization continues to become more efficient, and therefore, we should expect expansion in ROCEs and ROEs from here. But how comfortable are you with that? At what point do you think that we are running ahead of ourselves in making these assumptions? Let me ask you very simply Sir at what ROE do you think we should say that look 23%, 24%, 25% that is a very, very good reasonable number and then CAPEX starts to kick in after that?

Krishna Prasad C.: I do not have a straight answer on this Ashwini, but let me work on this and maybe we can send you this data.

Ashwini Agarwal: But 20% revenue growth based on existing capacity or existing plant and machinery and whatever have you with the CAPEX plans that you have including Onco for the next couple of years and 25% profit growth is pretty much in the bag?

Krishna Prasad C.: It is possible Ashwini, I think we can definitely stretch up to Financial Year 2022 without any CAPEX.

Ashwini Agarwal: Your future growth prospects whatever you pursue, you aim to keep net debt to EBITDA at or below 1.5 which is pretty much where you will get to in the next quarter or maybe two quarters?

Krishna Prasad C.: 1.5 is the peak. We will never allow this to cross 1.5, but we aim to get to 1 and at 1 we would feel comfortable in putting some cash into whatever expansion we have.

Moderator: Thank you. The next question is from the line of Sachin Kasera from Swan Investment. Please go ahead.

Sachin Kasera: Sir, just one clarification on this discussion that you are having on peak revenues and capacity, so broadly from what I could understand you are saying that may be up to INR 3800 to INR 4000 crore type of revenue we can achieve with minor CAPEX? Is that a proper understanding may be till FY '22?

Krishna Prasad C.: That would also depend on how quickly the Onco business takes off, but I think somewhere around that number, yes we could.

Sachin Kasera: As we keep ramping Sir today we are at roughly 25 run rate if I realize the first-half numbers, do we see efficiency measures other than gross margins starting to flow in terms of operating leverage and from more upside possible from there?

Krishna Prasad C.: We always aim for upside and we have a continuous program on operational efficiencies, so however, I would not commit to that, but these numbers of 20% plus EBITDA we can definitely sustain. There is no issue on that and like I said the 25% over the next three years is given on the PAT and going forward also I do not see any reason if you plan well why we will not be able to maintain that.

Sachin Kasera: Sir, second question was regarding the product concentration again. It was asked by one of the earlier participant and there was a mention by the management, so if you can just tell us what is the revenue from the top five products as of now?

Krishna Prasad C.: I would say not just top five, the core products which I said are eight products, the percentage is 83% from the core products.

Sachin Kasera: What was these numbers Sir, four to five years back? The core products it was that time also 83?

Krishna Prasad C.: It was almost 100.

Sachin Kasera: The second question is regarding the segment mix, as you have been seeing in the last few years the issue of APIs continues to come down, how do we see this ratio in the next three years? Sir, the mix between API and FDs and PFIs?

Krishna Prasad C.: APIs since we have added new capacities, the API sales have gone up, however slowly if the conversion happens from APIs customers are going to PFIs and PFIs to FDs, so as we go by we will see reduced API sales and possible a steady PFI sale and then increasing FD sale.

Sachin Kasera: Fair assumption that API as a percentage of revenue should come down by 5% to 10% in the next three years from the current?

Krishna Prasad C.: It should, definitely.

Sachin Kasera: Sir, next question is regarding ANDAs. What is the type of ANDAs you plan to file this year and approvals we are expecting and are we looking at any attractive or meaningful approvals in the second half?

Priyanka Chigurupati: We are going to have between four and five approvals within the next two quarters. Most of them are going to be limited competition, some extended releases and some controlled substances. We have already filed three plus two ANDAs this year and we are going to be filing another between four and six ANDAs by the end of this year.

Sachin Kasera: So total of around 10 to 12 ANDAs we are looking at?

Priyanka Chigurupati: Yes.

Sachin Kasera: This R&D budget which is roughly around INR 30 crores in the first half, does it move up in the second half and how is it going to go in the next? Is it going to improve significantly from here, we may end up 4% of sales?

Priyanka Chigurupati: The guidance given for R&D was about INR 150 crores for the whole year and we should be within that limit.

Sachin Kasera: One last question on the working capital, we have seen some improvement Sir, is there still scope for improvement in the working capital or we are more or less done with that program?

Krishna Prasad C.: We are always striving to do that, but actually we have started off front end in the United States and we are selling directly to distributors whereas in the past we used to go through partners. If it was a partner, we used to receive the cash less than 60 days or so, but today we need to keep lot of inventory in the US and also the credit terms to distributors are little longer, so there is a need for extra working capital; however, in spite of our sales in the US being about INR 60 crores per quarter we are trying to maintain this as low as possible and we will see where we go. There could be a slight increase, but we will strive our best to maintain it or maybe bring it down.

Sachin Kasera: So basically it should remain somewhere closer to the levels we are seeing today, maybe slight increase or slight dip that is it?

Krishna Prasad C.: We will have to see, if there is a very profitable business in the US I do not see any reason just look at inventories, so we will have to see as we go by, but definitely they will keep these things within reasonable limits, we will definitely maintain good ratios.

Sachin Kasera: Sir, just last question on this cash flow from the divestment of the JVs, you mentioned that you intend to not repay debt as it is a very low rate of interest and you also mentioned that we are not looking in more than INR150 crores of CAPEX this year, so then it only means that are we looking at rewarding shareholder in terms of various options via higher dividend or buyback, or the third option could probably also be acquisition, so if you just tell us more on that?

Krishna Prasad C.: Right now the thought is just to keep the cash in the company, but anything is possible, we will take a decision as we go forward, we will sit with the Board and see what to do next.

Sachin Kasera: When can we expect Sir clarity on this maybe by next quarter or it will take some time for the Board?

Krishna Prasad C.: After the money comes in, we can start talking about it, we do not want to talk about it ahead of time.

Moderator: Thank you. Ladies and Gentlemen, that seems to be the last question for today. I would now like to hand the conference back to Mr. Prasad for his closing comments. Over to you, Sir.

Sumanta Bajpayee: Thank you everyone for attending today our Earnings Call. Thank you again. Just want to highlight one point, we have taken the help of EY to further strengthen our IR practice and in this regard, I would request everyone if any question we have not been able to answer fully or any future contact, please get in touch with Jill Deviprasad and Richa Singh. They can definitely help you to reach out to management and Richa's email ID is shared in our investor presentation, so thank you all.

Moderator: Thank you very much. Ladies and Gentlemen, on behalf of Granules India Limited, we conclude today's conference. Thank you all for joining us and you may disconnect your lines now.

Contact Details: Email: investorrelations@granulesindia.com

Registered Office: My Home Hub
Second Floor, Third Block
Madhapur, Hyderabad – 500 081
Ph. No: +91 40 3066 0000/6676 0000
Fax: +91 40 23115145
Website: www.granulesindia.com
CIN: L24110TG1991PLC012471