



“Cipla Limited Q3 FY15-16 Earnings Conference Call”

February 10, 2016



MANAGEMENT: **MR. UMANG VOHRA – GLOBAL CHIEF OPERATING OFFICER - CIPLA**
MR. ANANT ATAL – HEAD - INVESTOR & MEDIA RELATIONS, HEAD - PARTNERSHIP BUSINESS FOR EMERGING MARKETS - CIPLA

MODERATOR: **MR. CHIRAG TALATI – INSTITUTIONAL EQUITIES, KOTAK SECURITIES LTD**

Moderator: Ladies and Gentlemen, Good Day and Welcome to Cipla Q3 FY 15-16 Earnings Conference Call hosted by Kotak Securities Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Chirag Talati from Kotak Securities. Thank you and over to you sir.

Chirag Talati: Good Evening, Everyone. This is Chirag here from Kotak Institutional Equities. I thank the Cipla management team for giving us the opportunity to host this call. From Cipla we have with us today Mr. Anant Atal – Head, Investor and Media Relations, Head Partnership Business for Emerging Markets and Mr. Umang Vohra – Global Chief Operating Officer.

I will now hand over the call to the Cipla management team for their remarks. Over to you sir.

Anant Atal: Thanks, Chirag. Good evening to all of you and welcome to our third quarter FY15-16 earnings call. I hope you have received the investor presentation that we have posted on our website. As requested by several of you, we have disclosed a lot more on our key markets such as India and South Africa as well as on the R&D spend this quarter. Over the following quarters we will continue to provide more updates on our performance in key markets as well as on our pipeline.

This quarter had an impact to revenue due to change of distribution policies largely in our India business. Our overall income from operations stands at Rs.3,107 crores this quarter registering a year-on-year growth of 12.3%. Excluding the impact of the distribution policy change, our growth would have been approximately 16.5%. Domestic sales for Q3 stands at Rs.1,194 crores and have stayed flat due to the impact of the distribution policy changes mentioned above. Our sales outside of India continue to show robust growth driven by a strong performance in South Africa and emerging markets. This quarter we have registered export sales growth of 28.5% with absolute sales closing at Rs.1,833 crores

The quarter also includes base level of Eesomeprazole that is expected to continue quarter-on-quarter at roughly the same level going forward and this is significantly lower than that captured in quarter one and quarter two of this financial year. For year-to-date 2015-16, our revenues stand at Rs.10,412 crores, a growth of 26.2% over last year. Employee costs for this quarter is Rs.586 crores, an increase of 16% year-on-year. This increase in absolute terms is largely attributable to normal increments, consolidation impact of acquisitions and new front ends. The other expenses for this quarter which included R&D expense, regulatory, quality, manufacturing and sales promotion have increased by 16% year-on-year to Rs.832 crores. Our EBITDA for this quarter stands at Rs.454 crores. While reported EBITDA is at 14.6% this quarter, there are several moving parts that have impacted EBITDA as compared to Q3 2014-15 that we would like to highlight. Firstly, excluding the impact of change in distribution policies, our EBITDA would have been approximately 17%. Secondly, Eesomeprazole is down to a sustainable level and this creates an impact to our EBITDA. Our core R&D project related

spend for this quarter has increased by 85% year-on-year and R&D expense now stands at approximately 8% of revenue as compared to approximately 6% last year.

Further, as you are aware, emerging market currencies have had a bad quarter, specifically the South African Rand which has had an impact of approximately 0.7% to EBITDA margin. We have also ramped up consumer healthcare and biologics expenses which are impacting EBITDA margins to the extent of approximately 1%. Consumer healthcare will in due course transition to the newly announced consumer healthcare company and will be de-risked for cash but will continue to have an accounting impact at the time of consolidation. We see base business EBITDA margins levels at about 17% to 18% which will continue over the following quarters.

Our guidance of closing the financial year with an EBITDA margin improvement of approximately 100 basis points over the 2014-15 margin remains unchanged. This quarter we have initiated a program to reduce internal complexity and enhance the base business profitability through initiatives such as portfolio rationalizing, pricing improvements and cost optimization. Our PAT is Rs.343 crores and is up 4.7 versus last year. The PAT percentage has remained nearly stable at approximately 11%, our year-to-date PAT has grown by 54.7% and now stands at Rs.1,425 crores. The results for the current period includes a gain on sale of investment in an associate company (Biomab Holdings Limited) of Rs.74.2 crores on a consolidated basis.

Tax expense for the current period is net of minimum alternate tax credit of Rs.55.16 crores. Our CAPEX is approximately 6.6% of sale. Total debt to equity ratio is 0.13. Outstanding forward contracts as hedge for receivables as of 31st December 2015 are ZAR735 million at around 4.85. We have working capital loans of about US\$ 200 million which acts as a natural hedge towards our receivables.

I will now hand over to Umang to take you through some of the business details.

Umang Vohra:

Thank you, Anant. Good Evening and welcome to all of you.

I will now take you through the business performance starting with our India Rx business. The overall numbers have already been mentioned by Anant. Specific to India, excluding the impact of our distribution policy changes, our Rx business has grown at 13% on a year-to-date basis. 18 out of our 22 brands of Cipla in the top 300 have outperformed the respective markets and we continue our strong performance in the respiratory therapy with gains in the MDI segment.

For the quarter ended December, our ORG growth rate is at 18% for the October to December quarter versus 16% for the market, and we have also shown a market share gain of about 0.25% from 5.24% to 5.46%. Emerging therapies such as GI, Urology, Derma and Pediatrics are growing strongly with increase in year-on-year market share.

In line with our approach to invest for the future we have entered into new areas through partnerships - Cutisera in cosmetology, Nasovac S in Vaccines, Reteplase in Anti-Thrombolytic. The contribution of new introductions continues to increase quarter-on-quarter from 3% of sales in quarter one to 3.6% in quarter three. Significant efforts are underway to build on our launch excellence and robust pipeline in our Hepatitis C portfolio with the Hepcvir combinations. This will enable Cipla's lead in Hepatitis B to extend to Hepatitis C as a franchise as well. Excluding the impact of our distribution policy changes, our generics business grew 8% for this quarter. We expect continuing challenges in our generic business segment.

Our South Africa business has shown a strong growth across both private market and tender businesses with year-to-date sales growing by 43% compared to last year in local currency terms. Our partnership with Teva is gaining further traction while our agreement with the Serum Institute of India has enabled us to introduce low cost vaccines in South Africa. We continue to expand the market share in respiratory with products showing strong high-teens growth in the MDI segment. We have recently invested in a state of the art distribution center facility doubling our existing capacity. In-house distribution is a competitive advantage which is helping us improve customer service levels, enhance compliance as well as reducing the cost of distribution.

Our North America business has registered an overall YTD growth of 138% compared to last year in local currency terms. As previously disclosed, we have entered into a definitive agreement to acquire 100% stake in the US companies of InvaGen and Exelan for which the transaction closure is imminent. Our supply of Esomeprazole and Budesonide Respules continues but at a much lower scale. Q3 includes base level of Esomeprazole that is expected to continue which is significantly lower than what is captured in the first half of the year.

In Europe, our YTD 2015-16 sales have grown by 32% year-on-year in local currency terms, driven by strong top-line growth across the B2B markets. We have enhanced the depth of our respiratory offering with new product launches of Mometasone in Belgium, Fluticasone in Italy and Spain, and Ipratropium Salbutamol Respules in Romania.

In our international business, we have registered an overall sales growth of 20% in local currency terms with strong performance in our front end market and stable growth in our partner markets. Our Cipla Global Access business is facing a slower than expected take off.

Our API business B2B business has declined 5.3% this quarter, though it is still 33% higher than last year for the YTD period.

As Anant has mentioned earlier, we have increased our allocation to R&D and in this quarter our R&D expenses on a consolidated basis are almost 2% higher than what we spent in the previous year. On the portfolio front, we have over 200 formulations development projects under way of which top 50 projects address a market size of \$30 billion based on innovator sales. Of these projects, the US accounts for 26 projects. The inhalation and injectable delivery forms account for 25 of the 50 top projects. Our year-to-date formulations filing stand at 4 for

North America, 24 for Europe and 1,087 for international markets. We now expect to file almost three to four products per quarter in the US going forward and have good line of sight to file between 15 to 20 products in the US next year with some potential first to file opportunities. Also in the next year, we expect to launch some of our own new launches in the US in less crowded and less competitive product categories.

As you are aware, on the organizational front, Cipla has instituted a six-member management council in order to simplify decision making and improve operational excellence. On the regulatory side, we have sent our remediation action plan back to the FDA on 483s that had been issued over the last year and are waiting feedback for the Indore facility. We have recently received new product approvals as well from our Goa facility from the US FDA.

To summarize, while growth remains on track, we are choosing to invest in R&D. This will impact our reported numbers as the company invests for the future. Our priority for the next year is going to be on the simplification and focus on a set of core markets. We also will substantially simplify the way we do business which will entail making choices on our geographic focus, our portfolio business model and overall resource allocation.

I would like to thank you very much for your interest in Cipla. Over to you, Chirag.

Moderator: Thank you very much sir. Ladies and Gentlemen, we will now begin with the question-and-answer session. Our first question is from the line of Aditya Khemka from DSP Blackrock. Please proceed.

Aditya Khemka: Could you clarify as to how many ANDAs are pending approval with the US FDA including our own and partner filings? And how many of those ANDAs are filed from Indore?

Anant Atal: We have about between 65 to 70 ANDAs pending, and of those pending ANDAs a majority of them are partner owned. Almost two-thirds are partner owned, and the remaining third will be our own ANDAs.

Aditya Khemka: And how many of our own or partner ANDAs are filed from Indore?

Anant Atal: I do not have that information available right now Aditya. We can dig into it and at the right time put it up on our website.

Umang Vohra They are not significant in number though.

Aditya Khemka: Could you just also clarify if we had any approvals from Indore since the Form 483 was issued?

Umang Vohra: I do not think so. But at the same time, I do not think any products are coming up for approval in the near future from that site.

- Aditya Khemka:** And secondly on the business side, obviously the distribution policy change would have had an impact this quarter, but if my understanding is correct, then the generic-generic market is also sort of not doing well industry wide. So how much is the contribution of the generic-generic portfolio to our sales in this quarter?
- Umang Vohra:** We provided that in the investor presentation. The generic generics portfolio is roughly 18% of the total India portfolio.
- Aditya Khemka:** And when you say that Rx business grew 13%, that excludes the generic-generic business?
- Umang Vohra:** That is right and the Rx business has grown 13% excluding the onetime change that we have. I want to repeat that our underlying growth as reported by ORG IMS on secondary sales still continues to be 18% and higher than the market for the October to December quarter.
- Aditya Khemka:** And lastly on the South African business, I understand that the Rand is weighing on our profitability and revenue, but do we have an action plan there? Because the way the currency has moved, I think the primary driver is oil so that does not seem to change in the near future. I mean, at least that is not the expectation. So are we planning something as to how we can hedge ourselves against that, how we can improve profitability or are we renegotiating prices?
- Umang Vohra:** So on the pricing I can tell you that there are price increases which are being allowed in South Africa due to the Rand devaluation and that action is under way. We pretty much hedge what we have on the balance sheet but the translation impact of Rand to rupee we cannot hedge. But whatever is on our balance sheet we hedge completely and I do not think on that account we have lost too much because of the Rand. What we are losing out on is the translation impact of the Rand to the rupee. So if price increases, then hedges on the balance sheet is the action that we are taking and that should help us offset some of the devaluation on the Rand.
- Aditya Khemka:** And sir last question if I may, on the UK approval for generic Seretide, any updates there? Have we filed out the critical and regulatory data with the regulatory authority or are we yet to submit some data to them which is basically stalling up the whole approval?
- Umang Vohra:** So we have heard lately from them. There is still some correspondence with the regulatory agency and therefore we still believe that Cipla is close to an approval. But, as of now, we do not have an approval for the UK.
- Aditya Khemka:** What sort of correspondence.
- Umang Vohra:** Our file is under active review and we have heard from them. They have asked for more data to which we have already responded
- Moderator:** Thank you. Our next question is from the line of Chirag Dagli from HDFC Mutual Fund. Please proceed.

Chirag Dagli: Sir what is this “distribution change” that we have done in India and does this have any impact on the top-line as well as on the bottom-line?

Umang Vohra: Yes. The distribution change in India will impact both top-line and bottom-line because essentially what has happened is that quantum of sales has effectively got deferred. So what we have done is that as a result of the fact that the last two weeks of the month typically have much higher sales than the first two weeks of the month, there has been a decision made to stagger what we dispatch up-country and what we dispatch to metros by a certain date. So as a result of this, there is a onetime impact of sale being withheld from being reported this quarter. This will not continue going forward but as a result of the fact that some of the sales has been withheld, the profit of that sales is also not booked in the current quarter.

Chirag Dagli: So when you say in the presentation 18% margin, this is on the sales after adding back this particular number to the sales?

Umang Vohra: You are right. So after we add back this, the EBITDA margin goes to 18%. The only thing I would like to draw your attention to is that the 18% is after a 2% increase in R&D.

Chirag Dagli: No, I understand sir, what I am trying to conclude is that this 18% is on 3,100 crores sale or should we add back that number on the topline as well?

Umang Vohra: EBITDA margin is roughly the same and it would be in the range of 17.5% to 18% even if you add it back on topline

Chirag Dagli: And the other thing is on the base business margin ex of Nexium. So Nexium sort of impacts a lot in the first half but when you look at the margins over the last four quarters would you say that they have broadly been in this range?

Umang Vohra: When you say margins in the first half are you saying with Nexium?

Chirag Dagli: Base business margins ex of Eesomeprazole supplies.

Umang Vohra: So margins ex of Eesomeprazole supply would be slightly higher in the first one or two quarters because R&D has really peaked most in this quarter.

Chirag Dagli: Higher than the 18% is what you are saying?

Umang Vohra: Higher than 18% because R&D is beginning to peak now as we invest more for US related files.

Chirag Dagli: Has the full impact of Pulmicort supplies coming in third quarter?

Umang Vohra: No, it has not. There is a very minor impact but basically you could say there there is nothing from Pulmicort in this quarter.

- Chirag Dagli:** Why is that sir because we have been supplying now for two quarters?
- Anant Atal:** Because there is a one quarter lag and the sales that have happened in the first quarter were almost miniscule. So that is why the impact in this quarter is virtually negligible.
- Umang Vohra:** So Pulmicort launched, if you are aware, somewhere in the middle of the second quarter and towards the end. Therefore even whatever we have as an impact will largely come in the next quarter. So there is hardly anything in this quarter.
- Chirag Dagli:** But there is a profit share on this with the partners?
- Umang Vohra:** That is right. There is a profit share and it generally gets recorded with a quarter lag.
- Chirag Dagli:** And just one more point on this - is the Pulmicort agreement any materially different than that other partnership agreements that we might have?
- Umang Vohra:** When you say other?
- Chirag Dagli:** Generally on this partnership model that we have pursued in the United States from a percentage of profit share standpoint - is Pulmicort materially different given the product specific dynamics that it might have?
- Umang Vohra:** Unfortunately, I cannot divulge details about this. But probably what we can say is that most profit share agreements follow a certain percentage in the US and I think we are in line with that. But each agreement is different.
- Moderator:** Thank you. Our next question is from the line of Saion from Nomura. Please proceed.
- Saion:** Umang, can you just tell what is the total R&D spend for the nine months' period, you said it is 8% for this quarter.
- Umang Vohra:** It is 6.6% for the nine month period
- Saion:** So you think this 8% level would continue as we go into next year?
- Umang Vohra:** Yes, I think what we are indicating Saion is that as the US filings pick up we are likely to head closer to 8% on a sustainable basis.
- Saion:** And Umang just on the generic-generics part of the business which is 18% of revenues, there are challenges as you see, I mean how do we see this business from a slightly longer term perspective?
- Umang Vohra:** So Saion there are two ways to answer this question. The first, and again you have to keep in mind that there is a fair amount of uncertainty on basic margins in this business, is in terms of

the price margin for this business that has been going on as a policy by the government. So that is leading to some uncertainty in the business. But effectively, this business has been growing for Cipla at a rate of about 15% to 16% annually. In this year we have almost rationalized close to 10% the business's top-line on account of some product categories and therefore this base has been set lower. I think this quarter is the first quarter in the year that you are seeing an 8% growth. Every other quarter, we have some either flattish or de-growth and therefore we are hoping that this business will probably at least begin to start growing back in the 8% to 10% range. But I have to caveat with the uncertainty around the whole margin issue and I am not sure whether I can give you a view on a longer period for this business.

Saion: And one last question on the currency impact, I mean you have through partnership selling in many other markets including Russia and maybe Latin America, so how does currency impact us, do we need to take some hit on account of the depreciation?

Umang Vohra: I think our currency impact largely is the ZAR because as a result of our imports versus export, the US dollar is not so much of an impact for us but the ZAR currency is a fair amount of impact for us and we have called that out in the presentation. I think this quarter has been pretty brutal on the rand and therefore we have seen an impact of almost 0.7% to the EBITDA.

Moderator: Thank you. Our next question is from the line of Neha Manpuria from JP Morgan. Please proceed.

Neha Manpuria: First on the distribution change, is it done and over with in this quarter or could we see lingering impact of this in the near-term in the next few quarters too?

Umang Vohra: No, I think this is the one-time impact Neha is this quarter. I do not think we are going to see this lingering on.

Neha Manpuria: And the second question on South Africa, the growth is pretty strong, you mentioned expansion of Teva portfolio. So have we rolled out the full Teva portfolio that we have in- licensed and are we doing more such in-licensing deals now that we have seen the success with the Teva portfolio?

Umang Vohra: The answer to both is yes. The whole portfolio has been rolled out and it has done a lot better than our partnering deal case for the portfolio. And as we speak, the whole effort is to in-license more and more products both for India and for South Africa.

Neha Manpuria: And third on the respiratory, particularly on the US front actually, now that we have done InvaGen, if you look at next year do you think your focus will be probably on scaling up your presence in the US particularly given we have a consolidated customer base or would you be open to doing a more strategic M&A to sort of improve your presence in some of the niche areas?

- Umang Vohra:** I think our business today in the US, between the partnering business and our direct to market business, is somewhere closer to about \$150-odd million. If the transaction closes with InvaGen, this business would be closer to \$400 million. Though that is not small, it is still sub-scale compared to some of the other Indian players. So I am not sure in the immediate future we would do another transaction in the US but at least the focus in the next one to two years is going to be to try and get our own pipeline in. Our current R&D expenditure also includes what we are scaling up for the respiratory product families in the US.
- Moderator:** Thank you. Our next question is from the line of Nimish Mehta from Research Delta Advisors. Please proceed.
- Nimish Mehta:** Just wanted to know whether we have been booking any revenue or royalty from Rifaximin or is that an opportunity?
- Anant Atal:** Nothing for this quarter Nimish.
- Nimish Mehta:** Is that an opportunity or it is not an opportunity, how should we look at it?
- Anant Atal:** So it is an opportunity but it is unclear on when that opportunity will actually materialize.
- Nimish Mehta:** It does not materialize upon the launch of Rifaximin for the irritable bowel syndrome?
- Anant Atal:** It is beyond that Nimish. The product is already commercialized but the agreement we had two quarters back was of slightly different nature. So it is about when they will launch a slightly differentiated version of that product.
- Nimish Mehta:** But for the irritable bowel syndrome, right?
- Anant Atal:** Yes.
- Nimish Mehta:** The second thing I just wanted to know, you alluded to having heard from the UK authorities on the generic Seretide, so whatever queries they have kind of raised or whatever questions they would have raised, do we need to undertake any new clinical trial for that or it will be regular data that we will have to submit?
- Umang Vohra:** I cannot comment on the specifics. I think this type of regular data exchange is expected with the agency. We are still hopeful of an approval which does not take too long.
- Nimish Mehta:** And what have been the impact of the competitor's launch, let us say by Mylan and Sandoz in UK with their own generic Advair? Have you been able to free any kind of market ramp up for those two companies?
- Anant Atal:** Firstly, the Sandoz product is a DPI and hence that is in a different segment. On Mylan, we are closely monitoring and I guess you should ask them that question and see how their

performance is going. But if your question is whether we are seeing an uptake in the Mylan product, then I think that we are seeing an uptake and they are gaining market share.

- Nimish Mehta:** Is it significant or if you can share that number?
- Umang Vohra:** We can take it off-call. Since it is about Mylan, we would rather not talk about it on our analyst call.
- Moderator:** Thank you. Our next question is from the line of Girish Bakhru from HSBC Asset Management. Please proceed.
- Girish Bakhru:** First one was on Pulmicort, just wanted to check when is the launch of the other remaining strengths by Sandoz?
- Umang Vohra:** When you say other remaining strengths, there is one strength where they have exclusivity Girish, from what I understand, and then there are two strengths for which they have shared exclusivity along with Teva and I think other companies. From the information I have I think they have launched all three strengths.
- Girish Bakhru:** Okay, all are in the market. So in a way when you say that there is hardly any contribution this quarter, so next quarter will be contribution from all the three strengths combined, right?
- Umang Vohra:** That is right.
- Girish Bakhru:** And second one was again in the Exelan business, this is largely government business as I understand, right, and if you could comment on what are the API sources for this company, where does it buy API from?
- Umang Vohra:** It is a mix. There is API from what we understand and to the amount we can comment, I think API is brought from inside the US, outside of the US and substantial transformation is probably proved by them. There is no change effectively in the US law from what we understand and the US law still says that substantial transformation has to happen in the US.
- Girish Bakhru:** And just last one on the UK approval, when you are talking to the agency, if you could throw some light on whether UK per se is too stuck up on Q1, Q2 data or how does it work? Is it too lenient to approve any differentiated product, I mean why would they ask a differentiated data, I am just trying to understand that.
- Umang Vohra:** I cannot comment on that Girish for two reasons. One, I am not exactly sure on whether their approach is for differentiated data or not. All I can say is that we are in active discussions with them. Our file is being reviewed. Each file has different questions that the regulators make and I think we have an obligation to answer it.

- Girish Bakhr:** But is there stability still in the question that you are asking for that why this data maybe more critical for you than for others?
- Umang Vohra:** Cannot answer that Girish.
- Moderator:** Thank you. Our next question is from the line of Nitin Gosar from Religare Invesco. Please proceed.
- Nitin Gosar:** The six-member management council to simplify the decision making process, so what are the avenues or what are the scope of this treaty, is it more to do with the product rationalization or production metrics or anything else if you can explain here and what will be the savings or simplicity which we can seek from this particular exercise?
- Umang Vohra:** No, so the management council is not doing the exercise. The management council is the new leadership structure of Cipla. So I think that is just something that we have released in public domain. I will take the second part of your question. Yes, Cipla will try and simplify and what we will be looking at is which markets do we focus on as against all markets. We will be looking at which products we would invest in more time and disproportionately in. I think that is what we are trying to do at Cipla.
- Nitin Gosar:** And sir on this WPI index which is going negative off late, how do we see the impact of pricing of the same on our India NLEM portfolio?
- Umang Vohra:** It is a very good question. All I would say is that all of us will have to honor whatever has been agreed with the government. So cannot really give you any specifics but at the same time, this is a topic that almost every company is grappling with.
- Nitin Gosar:** And the final question was with regards to InvaGen, could you update what is the status of those 483s?
- Umang Vohra:** I think we will be happier to comment on this once the deal is done. At this stage I do not think we can comment. The only thing I would say is we have reviewed this and it was part of our diligence.
- Moderator:** Thank you. Our next question is from the line of Sameer Baisiwala from Morgan Stanley. Please proceed.
- Sameer Baisiwala:** Just a couple of questions, one is on the US business, you made a comment that you will launch your own product in fiscal 2017 which has less competition, do you want to expand on that and does this include any from Exelan that you had in mind?
- Umang Vohra:** Sameer, this was all our existing Cipla products for now, so we have not given commentary on Exelan. There are a couple of products which we have already filed as part of our 65-70 odd pending which today's market has four to five players but they are reasonably good products

to launch even today. So we are not going to be in the first wave for these, but those are the ones that are coming up in two or three quarters that we will be launching.

Sameer Baisiwala: And just as we understand the size of it, so it could be like 20 million plus minus sort of a sales opportunity for Cipla?

Umang Vohra: Yes, a couple of them could be 15 million, 20 million on a full year basis.

Sameer Baisiwala: And second, I saw that InvaGen has also filed for Renagel and Renvela. At this point would you want to make a comment on that?

Umang Vohra: Sameer, I cannot but we would be happy to address this once the deal is closed and at that time we will speak about their pipeline as well.

Sameer Baisiwala: And you mentioned that you have taken price hikes in South Africa, anyway to say that what could this mean? Would it be good enough to neutralize the entire impact of currency depreciation or any color on this?

Umang Vohra: So Sameer I do not think it will neutralize the entire impact, so just to give you a flavor - our growth in local currency is 43% year-on-year, growth in rupee for the same period is 20% odd. So the price will not go up and the price increases we are taking what the government is allowing because of the depreciation in the Rand. So the price increases typically are in the 5% to 10% range and not higher than that.

Sameer Baisiwala: And for the entire portfolio or part of the portfolio?

Umang Vohra: I would say most of the portfolio that is what is allowed.

Sameer Baisiwala: And one final question from my side - any thoughts on US Advair? How is your effort progressing and when do you see the product get into clinical?

Umang Vohra: We would choose not to comment Sameer because of the competitive nature of the category. But if your question is are we close to clinical trials as yet, then the answer is not in the immediate future.

Moderator: Thank you. Our next question is from the line of Deep Master from Enam Holdings. Please proceed.

Deep Master: Just on the domestic sales, you mentioned it is a onetime impact so can we expect some of the sales to come back Q4 and beyond?

Umang Vohra: Yes. Some of the sales would come into Q4 as well. I think what will also happen is that as we have implemented this, this is a onetime, but every quarter there will be some kind of

staggering, but the onetime has been taken this quarter. So therefore, yes, there will be some sales that will come into the quarter of this year.

Deep Master: And on your biosimilar piece for the emerging markets, is there any update that you can share with us?

Umang Vohra: Well, we have reached an exciting point. I think we have proof of concept on one and as we speak, we are thinking of investing further for the emerging market for and extending this to two or three other biosimilars. So, at this point, this is all we can say. We have established proof of concept, we feel good about what we have and we are going to take this further for the other emerging markets.

Deep Master: But could this be an FY17 or FY18 story for us?

Umang Vohra: Probably FY18 and not before that.

Deep Master: And just lastly, if I may ask, in South Africa what percentage of your cost would be in rupee denominated? Because although the currency was not in dollars.

Umang Vohra: Yes, most of it is. The only thing is that there is a lot of import that South Africa does which the main Cipla India standalone business sends to them basically, and the ZAR currency. So we try and hedge whatever we sell to them here in ZAR itself.

Deep Master: So further depreciations from here, so it would not have a linear impact, right?

Umang Vohra: It will not have a linear impact. But we also feel that a large part of the depreciation has possibly happened for this market already. We can't predict but the Rand has moved quite significantly already.

Moderator: Thank you. Our next question is from the line of Anmol Ganju from JM Financial. Please proceed.

Anmol Ganju: I just wanted to drill down on couple of factors. One, if you look at the change in the distribution policy, what exactly are we trying to optimize here and what was the rationale for doing it now in particular?

Umang Vohra: So I do not think we chose a time to do it in our worse quarter. I do not think that was in our thinking. I think what was in our thinking is that we have got to continue optimizing supply to the market in a manner that is sustainable. As I explained earlier, there is a fair amount of dispatch that happens in the last couple of days, last two weeks, last 10 days of the month. So we have just made a distinction in terms of what goes out when and how we recognize the revenue for what is going out when. That is what has happened and that is the impact that has come as a result of the policy change.

- Anmol Ganju:** And the second question is, if you look at both the factors which at least have impact with the quarter, one is obviously the change in distribution policy and second obviously Pulmicort not reflecting in the quarter, both these should revert next quarter. So in that context do you not think there is a material upside to our guidance on both the top-line and the margin front?
- Umang Vohra:** So we have actually said that we will beat margin on a full year basis and we have also said that we are okay on the top-line growth as well. So from a full year guidance perspective we are okay. All that we are trying to signal is that base level EBITDA, with this level of spending and R&D for the next immediate one or two quarters, is definitely going to be around the 18% range.
- Anmol Ganju:** And this is obviously a multi-year process where you think there will be a structural uplift of margins to converge with some of the other peers, is that understanding correct?
- Umang Vohra:** Yes. So I think some of the other peers have a much larger share over US business than we do. I think we are getting there but there is obviously a lag.
- Anmol Ganju:** Lastly before I get into the queue again, if you look at what is happening with the timelines of the Advair launch. I understand that each file is different, but broadly from an understanding standpoint given that now there has been some back and forth of the file, do you see as far as Cipla's capability in addressing this whole inhaler franchise is concerned, any competence gap which will have to be plugged in or you think we are just fine and this is a process we are learning more about as we go along?
- Umang Vohra:** I would say both. The only thing I would say is that this has been approved in other markets within Europe itself. It is not as if it has not had a European approval. It is a learning process for Cipla and I would imagine that it is a learning process for every other company that is going to go down the respiratory route as well. But just on this specific thing we are in dialogue with the agency but the same product has been approved in the other EU regions as well and we sell there.
- Moderator:** Thank you. Our next question is from the line of Prakash Agarwal from Axis Capital. Please proceed.
- Prakash Agarwal:** Sir, we joined the call a little late because of the earlier call. Could you help us again understanding the distribution policy, what we just heard what there has been some change due to the last two weeks of the month adjustment, can you please elaborate.
- Anant Atal:** So Prakash, we have simply just streamlined the distribution policy. There used to be some bunching which would happen towards the end of the month as we would distribute either up country or to metros. So this is a one-off and we have changed the policy. You will not see it in the future quarters.

- Prakash Agarwal:** But what do have changed, because if you are changing in just the timing why should it impact during the quarter if it is just a monthly event, I am just trying to understand that.
- Umang Vohra:** We have changed the dispatch. So if you change the dispatch you would not book the revenue. So basically if you are changing the dispatch between what goes to up-country and what goes to metros, it will finally reach the customer much later. So that is what we have changed. This is a one time change and it has been done because there is a fair amount of bunching in the last 10 days of supply. So, as Anant explained, it is a onetime event that will happen this quarter.
- Prakash Agarwal:** And there is no change in terms of the bonus issues or stuff like that?
- Umang Vohra:** No, nothing. No change in bonus, no change in incentives, Cipla does not operate with a field incentive policy either.
- Prakash Agarwal:** And adjusted for this change one time change you said the quarter performance is 18% growth on a total portfolio?
- Umang Vohra:** On a total portfolio I think growth is 16.5% is the total growth for the company in this quarter if you exclude the change.
- Prakash Agarwal:** No, sir only the domestic business growth adjusted.
- Umang Vohra:** Domestic is lower. Domestic growth, if we exclude this for the quarter, will be between 12% and 13%.
- Prakash Agarwal:** And if we adjust this back, we would be on track with our gross margin average of 61%, 62%?
- Umang Vohra:** Yes, that is right.
- Prakash Agarwal:** And sir secondly on the other expenses, clearly a lot of improvement, any specific reason or it could be because of the ZAR cost reduction or if you were to highlight because last two quarters specifically a lot of QoQ improvement in the cost.
- Umang Vohra:** We are looking at our cost more seriously and I think the first one or two quarters had significantly higher cost uptick. This is now being looked at and managed. We are optimizing spend as much as we can.
- Prakash Agarwal:** But any specific thing you have done?
- Umang Vohra:** There have been certain decisions made on hiring which is how many people do we hire, when and how. There has been also some sort of a hiring freeze for a while and we are trying to look at discretionary spending. So it is more in the nature of cost control.

- Prakash Agarwal:** And in terms of filing, clearly momentum picking up three to four filings per quarter is what you are planning, but with specific areas you mentioned in the past ophtho, derma, injectables, so would these four filing would be in these buckets?
- Umang Vohra:** Yes, typically these. There will also be oncolytics and stuff like that and I think that is the trend you will start seeing that over time three to four filings per quarter will come up for the US.
- Prakash Agarwal:** And lastly, if Celecoxib approval, you said Indore has not received approval as of now post 483. So if you can highlight where is this Celecoxib approval coming from?
- Umang Vohra:** Celecoxib was from a Goa facility and not from Indore.
- Moderator:** Thank you. We will take the last question now from the line of Surjit Pal from Prabhudas Liladhar. Please proceed.
- Surjit Pal:** Could you please explain that why tax rate is so low this quarter?
- Umang Vohra:** Yes. There is a MAT credit which the company has taken on account of reasonable certainty of using the MAT that we paid earlier in the future.
- Surjit Pal:** So your MAT rate is 55 crores and your typical tax rate is around 26% - 28%. So if I deduct it than your tax rate should be 13%?
- Umang Vohra:** No. The effective tax rate for the quarter is about 23%. For the full year the annual effective tax rate is roughly about 22% to 23%.
- Surjit Pal:** I was going by your 26% to 28%.
- Umang Vohra:** We have signaled even in the last quarter, we are in the range of 22% to 24% and MAT credit does not get recognized on account of a phasing. It gets recognized at the quarter in which it is deemed reasonably certain that you can use it.
- Surjit Pal:** And any latest readers on your 483 on your Indore plant, any particular if you can?
- Umang Vohra:** No. I think we are corresponding with the agency and we are submitting the data as they have requested. We do not have any fresh update on this.
- Surjit Pal:** One last question about management council, I mean the latest structure that you have met, generally what we see is that there are single point leadership or authority happens in a company globally or domestically, what has prompted your company to get into this kind of unique structure of management council because generally what you say it simplifies rather with the experience previous of the organizations of other examples is that it complicates and delays the decision, that is one question. Second question is that, there are many people what we have seen in the last two, three years in our company who have come with a very high cost,

left the company, their reserves remain and generally those reserves given with a long-term commitment. And what we have seen is that those reserves generally have not been cancelled in your company but which is actually not the practice globally without any long-term commitment to the company which is taxing to the shareholders too. So could you throw some light on this prospect?

Umang Vohra:

So I might be the wrong person to answer because I have also just recently joined. But let me say two things. The management council is a council of people who lead individual functions. Every company has a management council today. It is not as if this is a unique structure to Cipla. It is just that Cipla had a larger team earlier and largely on account of the operating, we have structured the operating committee in such a way that the markets get consolidated with the manufacturing and that is why the council has become a smaller council than it was before. The council does not run the company, the council is the leadership of the company. It is the HR head, it is the finance head, it is me, it is Subhanu, it is Samina who is our Strategic Ventures Head, the R&D and the quality head. So the council is Subhanu's direct reports, but each one of us run our own functions. So, for example, if there is an issue in operations, I would not go to the CFO to solve it. The CFO solves his own problems in finance and the HR person deals with his own stuff in HR. So it is just a committee of people who report to Subhanu. There is nothing unique and every company operates like this. It is just that we have made this committee smaller.

Coming to your second question on ESOPs, I am not aware and maybe I probably need more data and certainly Anant can send this data to you, but it would be my understanding that most ESOPs lapse after people leave and I do not know if you are hinting at the fact that ESOPs do not lapse, but I am under the impression that ESOPs lapse and definitely we could give you date and could clarify this later. And as I said I am the wrong person to comment because I myself have just joined.

Moderator:

Thank you. Ladies and Gentlemen, that was our last question. I now hand over the conference over to the management of Cipla for closing comments. Over to you.

Anant Atal:

Thank you all for your interest in Cipla and if there are any specific questions do reach out to the Investor Relations team and we shall respond. Thank you.

Moderator:

Thank you very much members of the management. Ladies and Gentlemen, on behalf of Kotak Securities that concludes today's conference call. Thank you for joining us and you may now disconnect your lines.