



“Cipla Q2 FY-11 Earnings Conference Call”

November 11, 2010



**MODERATORS: MR. S. RADHAKRISHNAN – WHOLETIME DIRECTOR, CIPLA
MR. AJAY LUHARUKA – CIPLA
MR. ANMOL GANJOO – SENIOR ANALYST,
PHARMACEUTICALS, KOTAK INSTITUTIONAL SECURITIES.**

Moderator: Ladies and gentlemen good day and welcome to the Cipla Q2FY11 earning conference call hosted by Kotak Securities Limited. As a reminder for the duration of this conference, all participants' lines are in the listen-only mode and there will be an opportunity for you to ask questions at the end of today's presentation. If you should need any assistance during this conference call please signal an operator by pressing * and then 0 on your touchtone telephone. Please note that this conference is being recorded. At this time, I would like to hand the conference over to Mr. Anmol Ganjoo, Senior Analyst – Pharmaceuticals, Kotak Institutional Equities. Thank you and over to you Sir.

Anmol Ganjoo: Good evening everyone and thank you Cipla Management for joining us, I am Anmol Ganjoo from Kotak Institutional Equities and Mr. Radhakrishnan and Ajay from Cipla are joining us to discuss second quarter results FY11 with this I will now hand over Mr. Ajay and Mr. Radhakrishnan. Over to you Ajay.

Ajay Luharuka: Thank you Anmol. Good evening and welcome to the Cipla call for the second quarter results. We have Mr. Radhakrishnan also on the call with us now. We hope you have received the second quarter financials and the performance highlights available on the website with that we would like to give you an overview of the financials which can be followed by a question and answer session.

During the second quarter, income from operations of about 1600 crores grew by nearly 12%. However, operating margins and profits were lower by about 4% and 5% respectively. This was primarily on account of increased factory overheads at Indore SEZ and an appreciation of the Indian rupee vis-à-vis the US dollar.

Domestic sales for the quarter grow by about 20% and export sales grew by about 11% and this was in spite of a rupee appreciation by 4-5%. Material cost for the quarter has increased by 1%, the increase in staff cost of Rs. 51 crores is mainly due to increase in man power particular at Indore SEZ, regrouping of contractual staff at Goa faculty, and annual increments. Interest cost has decreased due to repayment of short term working capital loans availed by the company. Depreciation for the quarter has increased by about 16 crores. This is mainly due to additions of fixed assets on account of commissioning of the Indore SEZ factory.

Other expenditure has increased due to increased in selling expenses and factory expenditure in particular Indore SEZ such as repairs and maintenance, power and fuel, stores and spares etc.

As of the quarter end, the outstanding amount of forward contracts is about \$230 million which substantially covers the outstanding debtors. We continue to follow the practice of hedging all loans and covering net export billing on a month-to-month basis.

With this overview, I would like to leave the floor open for questions. Mr. Radhakrishnan and myself are available to answer any questions that you may have. Thank you.

Moderator: Thank you. The first question is from the line of Nimish Mehta from MP Advisors. Please go ahead.

Nimish Mehta: Can you let know what is the growth in the branded business of Indian formulation?

S. Radhakrishnan: The growth in the formulation business for the quarter would be about 20%.

Nimish Mehta: Right.

S. Radhakrishnan: Yeah.

Nimish Mehta: Yeah, no but last quarter as in Q1 you mentioned about branded growth as well as generic growth in the same segment. So if you can provide that break-up that will be great?

S. Radhakrishnan: The break-up between generic-generic and branded you mean?

Nimish Mehta: Correct.

S. Radhakrishnan: I will get the break-up in the meanwhile any other question.

Nimish Mehta: Yeah sure, the other thing is do you expect the launch of Zyprexa under 180 day exclusivity through your partnership with Teva?

S. Radhakrishnan: These are very specific questions which are sensitive, I do not know and I am not able answer those questions you know because, they've got various implications.

Nimish Mehta: I see any broad guidance as to any such opportunities that you may look at in the next 12 months or two years.

S. Radhakrishnan: There are opportunities like this which have potential to really add on to our sale but as I told you, I am not able specifically disclose such opportunities.

Nimish Mehta: Ok fine, I am then with my question in case you have the branded and generic....

S. Radhakrishnan: Sorry, it is about 19%.

Nimish Mehta: Sorry.

S. Radhakrishnan: The branded generic, I think overall, branded formulation would be about 21% versus the generic-generic would be about 18%. So roughly all average is 20.

Nimish Mehta: I see, ok. Thank you very much.

Moderator: Thank you. The next question is from the line Chirag Dagli from ICICI Securities. Please go ahead.

- Chirag Dagli:** Can you indicate to the quantum of these overheads at the Indore SEZ which have impacted this quarter?
- S. Radhakrishnan:** Yeah the quantum of overhead is roughly in three months is about 25-30 crores is the impact for this quarter.
- Chirag Dagli:** And this is got spread across several heads.
- S. Radhakrishnan:** Yes, absolutely. Employee is separate. There are basically overheads including depreciation and running cost, etc.
- Chirag Dagli:** And what would the sales in the Indore SEZ?
- S. Radhakrishnan:** It is marginal loss because do not forget the SEZ deals purely in export unit and most of the markets are of a regulated nature today. So what we are doing currently is only where the regulations are giving you the opportunity to produce at any site which is very nominal as compared to whole export market that we actually are exporting. So at the moment, therefore the turnover is quite negligible. It must be very low, where as the factory is commissioned and therefore the overheads are being incurred but I think already WHO approval has happened in the last month. MCC South Africa has happened and in the coming months we are hoping that UK and Australia will get approved. So once these happen, then obviously the factory can start exporting from the sites, which will obviously help us to improve the productivity of this factory. But at the moment because of regulatory reasons we are not able to export from these factories.
- Chirag Dagli:** So you would say the Indore SEZ at the moment is EBITDA negative?
- S. Radhakrishnan:** Absolutely.
- Chirag Dagli:** If I can just ask one more question, the Seroflo market, Mr. Hamied mentioned on television today that you know you could potentially launch it in CIS markets as well. Any tab on how big the market size could be for Seroflo?
- S. Radhakrishnan:** Well I cannot give you the size. It is quite substantial. In the Seroflo combination is substantial both in Russia as well as South Africa which Dr. Hamied mentioned and it can substantially add to our top line in the next two quarters.
- Chirag Dagli:** So South Africa, I need tab of how you know you potentially do the full year or, has this quarter seen any sales from there?
- S. Radhakrishnan:** No this quarter has not seen but it will happen in the next two quarters.
- Chirag Dagli:** Ok second half will Seroflo launch both in CIS as well as South African market.
- S. Radhakrishnan:** That is right.

Chirag Dagli: And the quantum of the CIS market will be similar to that in South Africa?

S. Radhakrishnan: I think so, yes.

Chirag Dagli: Perfect. Thank you so much.

Moderator: Thank you. The next question is from the line of Ranjeet Kapadia from HDFC Securities. Please go ahead.

Ranjeet Kapadia: My question relates to API business. We have shown a 1% decline. Is there any specific one-off item or is this a normal course of business because the formulation has shown 14% growth?

S. Radhakrishnan: API exports on an annual basis contributes about 20% of the total exports. Now API exports as Dr. Hamied mentioned in the interview is not just export but also what is being used for captive. So when you are looking at API as only sales obviously you are getting a figure which seems to be negative but if you look at the overall basis lot the API which we manufacture for own consumption in formulation is substantially high. That is why you find that that is not getting reflected in the whole API profitability, but having said that, yes, regarding API this quarter a little tangential from the normal trend. I think overall we will still expect to grow the trend for the full year.

Ranjeet Kapadia: So that will be in double digit for the full year?

S. Radhakrishnan: I hope to do that yes.

Ranjeet Kapadia: Ok thank you very much and all the best.

Moderator: Thank you the next question is from the line Rajesh Pherwani from HDFC. Please go ahead.

Rajesh Pherwani: I just wanted to understand what is the net FOREX realization for this quarter for you or in the dollar realization or whatever, give me?

S. Radhakrishnan: You mean the export realization?

Rajesh Pherwani: Yeah export realization.

S. Radhakrishnan: Yeah we have to give it you Rajesh, I mean it is not readily available. The moment but roughly if you ask me, in terms of the impact, the top line is lower by about 2-3% because of you know the comparative positions, this year versus the same period last year.

Rajesh Pherwani: Ok that is fine.

S. Radhakrishnan: Yeah.

Rajesh Pherwani: Thanks.

- Moderator:** Thank you. The next question is from the line of Bino P. from IIFL. Please go ahead.
- Bino Pathiparampil:** Is there any this other expenditure, does it include any kind of FOREX losses in there?
- S. Radhakrishnan:** Not really there is no FOREX losses included.
- Bino Pathiparampil:** Ok, this quarter at least the top line has started showing some good traction with domestic market growing at 21% and for the next half we also have a lot of triggers waiting to happen like Seroflo launch and ramp up in the Indore SEZ. So if we simply add these factors to a historical 8-10% growth rate that could potentially take the growth rate above 15%. Is there anything wrong in looking at it like that way?
- S. Radhakrishnan:** Yeah, the potentially yes, what you are saying is right but I think the factors that needs to be really looked at in export is the rate of appreciation of rupee that can considerably impact all our computations.
- Bino Pathiparampil:** Ok. So you are maintaining still the 8-10% growth guidance as a conservative policy?
- S. Radhakrishnan:** Yeah, that is what we would like to do put potential is there, obviously upside potential is certainly there.
- Bino Pathiparampil:** Great, thank you very much.
- Moderator:** We have a follow-on question from the line Nimish Mehta from the MP advisors. Please go ahead.
- Nimish Mehta:** Sir you mentioned about the break-up of branded as well as generic as being 21 and 18 and overall growth at 20%. So if do a simple math, it tells me that the sales break-up is about 50-50 between branded and generic, I am I missing something here?
- S. Radhakrishnan:** You are talking about this quarter?
- Nimish Mehta:** Correct.
- S. Radhakrishnan:** Can I recheck the figure and tell you Nimish because this is not readily available at the moment, if you can send in your email, I will send it to you.
- Nimish Mehta:** Ok no issues and a quick why is the excise duty low this time, significantly low in comparison to in QoQ as well as YoY comparison?
- S. Radhakrishnan:** The excise duty is basically because in Baddi we get excise benefit number one, so that helps us also it depends on the contribution of exports where excise duty not available. These product mix calculations can get upset.
- Nimish Mehta:** Ok fine I understand. Ok thank you.

Moderator: The next question is from the line of Monica Joshi from Avendus Capital. Please go ahead.

Monica Joshi: Just wanted to check when you report domestic sales in your quarterly it is all formulation sales or there is component of domestic API also?

S. Radhakrishnan: Very marginal, we do not really sell domestic API in India.

Monica Joshi: Can you just give us the number what was it for a FY10 for example what was the number of domestic API sale?

S. Radhakrishnan: Really nothing, very marginal.

Monica Joshi: Very marginal, so these are all formulation related. And okay just to confirm you said there was no FOREX loss or gain, is it this quarter?

S. Radhakrishnan: There was a small gain not loss. There was a small gain this quarter.

Monica Joshi: And can you quantify it please?

S. Radhakrishnan: About 15-20 crores.

Monica Joshi: 15-20 crores and this is included in other income?

S. Radhakrishnan: Other expenditure, it would be in the expenditure. It would be net of the other expenditure.

Monica Joshi: Ok thank you Sir.

Moderator: Thank you. The next question is from the line of Alok Dalal from MF Global. Please go ahead.

Alok Dalal: Sir the 20% growth that you have done in domestic business would you say that this growth is sustainable over the next two quarters.

S. Radhakrishnan: Yeah I think so, because it looks okay on month-on-month and I think the trend looks okay.

Alok Dalal: Okay.

S. Radhakrishnan: Nimesh, let me just clarify your question, the generic this time was higher 27% and the branded was about 19%.

Nimish Mehta: Yeah. Got it. Continue please.

Alok Dalal: Sir could you throw any color on the licensing income for the rest of the year?

S. Radhakrishnan: That continues to be dependent upon you know the kind of milestones that we are achieving, but I think what is happening slowing is most of the project which are getting completed they

are now coming into commercialization phase. So I would imagine at the end of the year, it will end at around 75-100 crores maximum for this year and going forward I would imagine this would be, may be you know we maintain the same level or even a little bit lower.

- Alok Dalal:** Ok understood and the CAPEX for second half would be how much Sir.
- S. Radhakrishnan:** About 400 to 500 crores would be the total next year you know, if you take a year, you know its impact, for the one year we have budgeted 500-600 crores. For the second half, therefore would be about half of that.
- Alok Dalal:** So around 200-250 crores and FY12 I believe it should be around 500 crores.
- S. Radhakrishnan:** That is right.
- Alok Dalal:** Ok thank you so much.
- Moderator:** Thank you. The next question is from the line of Rishabh Sheth from Karma Captial. Please go ahead.
- Rishabh Sheth:** Sir, actually my question on the technical fees was answered but I just wanted to know in terms of the inhaler launches, I mean you talked about Seroflo, so if you can just give some more color in terms of what is happening on the inhaler business?
- S. Radhakrishnan:** Sorry in what business?
- Rishabh Sheth:** In your inhaler business.
- S. Radhakrishnan:** Inhaler business generally in the domestic front is substantially doing well. Major focus here and it contributes almost about 25% of our domestic branded sales so that is doing well. A lot of effort and initiatives are being taken to take this, you know even higher. As far as the international business this year, inhaler business must be doing about 20% for in export as well as and going forward, it is the major focus area for us and as you know that already we have got all the approval of these combinations in Russia and South Africa and we would imagine that going forward, if the European approval happens for some of these products, I think it will really contribute across to the top line in the next couple of years at least.
- Rishabh Sheth:** How is much must be, what do you think like inhaler as a part of your overall business or international business in 2-3 year's time, I mean considering what approvals you have currently and may be some of the European approval coming through which I think in the last call you indicated should happen sometime in the second half of this year?
- S. Radhakrishnan:** See currently it is about 15-17% of our total business and going forward I think that can jump to 20-25 depending on what potential happens.
- Rishabh Sheth:** Today, currently 15-17% of the global business is?

S. Radhakrishnan: Total turnover if you take inhaler today it will be about 17%.

Rishabh Sheth: Ok total turnover.

S. Radhakrishnan: That is right.

Rishabh Sheth: That can go to 25-30%.

S. Radhakrishnan: The potential aspects.

Rishabh Sheth: Ok. Alright, thanks a lot.

Moderator: Thank you. The next question is from the line of Saion Mukherjee from Nomura. Please go ahead.

Saion Mukherjee: Is it possible to give a break-up of your inhaler business in terms of domestic and exports?

S. Radhakrishnan: Domestic and exports inhaler business?

Saion Mukherjee: Yeah.

S. Radhakrishnan: At the moment I do not have it but it is possible if you can leave your email, we will send it to you.

Saion Mukherjee: Ok. Thank you.

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

Nitin Agarwal: I just wanted to check for the quarter have we seen a full impact of the Meditab consolidation?

S. Radhakrishnan: We have not taken that in account at all because these are standalone results and this consolidation will happen only in March. That is going to be other thing which we are not considering at the moment. So therefore the Meditab in India, the China facilities, the facilities in Uganda, these profitabilities is not considered in this results obviously because it is a standalone and this consolidation will happen in our annual account.

Nitin Agarwal: How much of an impact would you think it is going to have in the overall number? Is it going to be substantial or...

S. Radhakrishnan: It is going to be significant if not substantial.

Nitin Agarwal: And from a business prospective would these entities coming into now Cipla buying them back from other entities. Does it really have any impact on the business outlook for these entities also in terms of way things were apart from the margin impact that will have on the business?

- S. Radhakrishnan:** These businesses are independently run so that will continue to have the potential that it already enjoyed, for example China is a big market for formulation and that is a huge potential for us and we will get the benefit of that because we are a 50% partner there and these Chinese products are on various regulatory stages of approval and that is going to be an impact which we will enjoy as when Chinese formulations are launched through our partners. So similarly the rest of Africa, Uganda whatever potential we could have will accrue to Cipla. So I think from a potential prospective, these investments look very attractive equally the bio facility that we have invested in and there again, it is a major potential and our stakes will accrue the benefits that we think can happen. These investments that we made for the very purpose of the benefits or potentials we have seen in them.
- Nitin Agarwal:** And these formulations that you said after you filed in China has been filed from Cipla facilities in India or European.
- S. Radhakrishnan:** These are filed from these Chinese facilities already. These are already in the pipeline and we will get the benefit as soon as the commercial launch happens.
- Nitin Agarwal:** But incrementally going forward would you be filing products from India also for the Chinese markets?
- S. Radhakrishnan:** Because we got share holding obviously we should play a role to our partners and sort of support them on a technical and other basis because we have that advantage here and that will enable them to file this, these will not be filing from India obviously because these are belonging to China, it's a Chinese joint venture but we will support the whole exercise so that the benefit will accrue to us.
- Nitin Agarwal:** And in terms of when do you think, you will probably see a start in contribution from some of these new launches in all material contribution from these new product launches in China.
- S. Radhakrishnan:** Some of these products are already on the regulatory phases for the few years. Chinese regulatory norms are far tougher than any where else in the world. But I would imagine in the next one to two years these will start kicking in.
- Nitin Agarwal:** And on the biogenerics how many launches do you see happening by next year?
- S. Radhakrishnan:** Domestically, we would imagine the launch will happen sometime in the mid of 2011.
- Nitin Agarwal:** How many products will be launched next year in the biogenerics?
- S. Radhakrishnan:** Couple of products at least to start with will happen.
- Nitin Agarwal:** Ok thanks very much.
- Moderator:** Thank you. The next question is from the line of Vrishank Chandavarkar from ET Now. Please go ahead.

Vrishank C.: I just like to know your agreements with Dr. Reddy's, how significant is it, by when will it start showing in your top line?

S. Radhakrishnan: Dr. Reddy's we have tied up with them for supply of OTC products in some of these Russian countries and some the products have already been you know commercialized so therefore the benefits will start but majorly will start accruing in the next two quarters in terms of these markets.

Vrishank C.: How much you all see affecting your top line?

S. Radhakrishnan: I am sorry.

Vrishank C.: How much you all see it adding to your top line.

S. Radhakrishnan: It is going to be adding, I mean in terms of percentages those markets these are good numbers that is why we entered the agreement so but I cannot probably disclose because of our relationship issue. But I think there is a large potential here for both type of companies that is why the venture happened.

Vrishank C.: Sir are inhalers also going to be a part of this?

S. Radhakrishnan: No inhalers at the moment see inhalers will happen, one in Ukraine it may happen but at mostly the 20 OTC products and prescription products that have been included and that will help us in Ukraine we have got this inhalers arrangements.

Vrishank C.: Ok Sir I also wanted to know how much does Chinese operations really add as a percentage?

S. Radhakrishnan: Sorry come again.

Vrishank C.: Your Chinese operation how much do they really add as a percentage to top line?

S. Radhakrishnan: Right now we are not consolidating the top line because we are not majority shares holder there. So right now, it is the standalone results that we are giving. In March when we consolidate, we will be consolidating on the bottom line and that bottom line impact will come as I just mentioned to Nitin.

Vrishank C.: Alright, thank you so much Sir.

Moderator: Thank you. The next question is from the line of Nitin Agarwal from IDFC.

Nitin Agarwal: Sir just to check on the European inhaler market in terms of anymore updates or anymore colors that you have on the launch time lines for some of these combination inhalers in Europe?

- S. Radhakrishnan:** As far as Europe is concern we have focused on one or two products may get approved, you know in the next few months it may happen but these still will be the non-combination product but otherwise from other one as we still have a time lines for about 18 months to two years by the time they get approved and launched.
- Nitin Agarwal:** And Budesonide the launch in UK has it happen or how is that shaping up?
- S. Radhakrishnan:** See Budesonide launched in UK has happened but it was not significant in terms of the numbers.
- Nitin Agarwal:** Ok, thanks.
- Moderator:** Thank you. Ladies and gentlemen due to time constraints that was the last question. I would now like to hand the conference over to Mr. Anmol Ganjoo for closing comments.
- Anmol Ganjoo:** Yeah thank you once again for joining us this evening to discuss the results and thank you Ajay and Radha once again for joining us on the call.
- S. Radhakrishnan:** Thank you Anmol.
- Moderator:** Thank you. Ladies and gentleman on behalf on Kotak Securities Limited we thank you for joining us, this concludes the conference you may now disconnect your lines. Thank you.