



“Neuland Laboratories Limited Q1 FY-21 Earnings
Conference Call”

August 4, 2020



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Moderator: Ladies and gentlemen, good day and welcome to the Neuland Laboratories Limited Q1 FY21 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, 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. Diwakar Pingle from Christensen IR. Thank you and over to you, sir.

Diwakar Pingle: Thank you everyone. Good afternoon friends. Welcome to the Q1 FY21 Earnings Call of Neuland Laboratories. To take us through the results and answer your questions today, we have with us the management team from Neuland, represented by Sucheth Davuluri – Vice Chairman & CEO; Saharsh Davuluri – Joint Managing Director and G. V. Bharadwaj – DGM (Finance).

We have sent out the press release as well as the detailed presentation and the same have been uploaded on the website as well as the exchanges. You could take a look at that or in case anyone of you wants it we could mail it to you if you write to us.

Before we start I would like to say that everything that is said on this call which reflects any outlook for the future, or which can be constitute as a forward-looking statement must be viewed in conjunction of the risks and the uncertainties that we face. These uncertainties and risks are included but not limited to what we have mentioned in the prospectus and subsequently in the annual reports which you can find on the website.

With that said, I will hand over the floor to Saharsh who will basically give you highlights of the quarter gone past and then we will open the floor for Q&A. Saharsh?

Saharsh Davuluri: Thank you. Good evening friends. First of all I would like to inform all of you that we are taking the call remotely, so Sucheth and I are in different locations than our team. So my apologies in advance if there is some mis-coordination or a delay in response but we do have good lines that are connecting us. So I do not expect us to have any issues. But I just wanted to give that disclaimer upfront.

But again good evening. Warm welcome to all of you joining this call. Like always I will first touch upon the business highlights of the quarters that has gone past and some of the key highlights of the financials. After which we will open the call for the Q&A session.

I am not going to call out the individual numbers for the quarter. Please note that a detailed presentation also has been sent to you and posted on our website and the exchanges, which would give you a lot of color on the operating metrics and other data.

Going forward we plan to continue updating you with bit more data if required. But please do give us your feedback so that it will help us in being more transparent and make life simpler for you to analyze our business.

Before I begin, we think that all of us have become more familiar with the pandemic situation. There is a continued surge in numbers from across the country. So we do hope all of you are keeping safe and are observing all the practices to fight this pandemic. So coming to the numbers, I did give you a brief outlook in the last quarter call itself in response to questions and we are glad that the quarter has panned out as expected.

Despite challenging conditions, we turned out in revenue of about Rs. 206 crores which is the highest ever by Neuland in a quarter in our history. This translated to a revenue growth of about 13.5% over the past last fiscal quarter and sequentially also it is a 6.4% growth. And I am pleased that the growth has been driven by all round performance both in GDS as well as the CMS segments of our business.

EBITDA at about Rs. 34.4 crores has shown an improvement of over 80.4% compared to the first quarter of last financial year and margin terms it was about 16.7% which is also in line with our expectations. The efforts from our perspective is to move the portfolio mix towards value added segments in the years to come and CMS will continue to play an important role.

I would like to highlight that the work being done by our teams on cost optimization which is also contributing towards the improvement in margins across the business. Quick word on what is driving the business in each of the product segments. Prime growth has been largely driven by Mirtazapine and Labetalol, while varied number of products have contributed well in the specialty segment.

We believe that the focused attention that is being given to each product in our portfolio in GDS will help us continue to grow this business. On the CMS front, the key highlight was the real growth from both existing products as well as products which are in the development stage. So now you would have seen that in slide number 9 of the presentation where we have started to show a split of commercially revenue versus project revenue and we think it is a very simplistic way of giving you a color of our CMS business.

The very nature of this business is evident when you look at those charts especially when you look at it over the past eight quarters. So you can see that there is a quarter-on-quarter volatility but when you look at it on an annualized basis you are able to see a clear picture and you are also able to see profits which we have been alluding to in all our past conversations.

I do urge you to go through the presentation where all other metrics including the number of CMS projects, the split across different segments are mentioned along with the balance sheet numbers and the ratios.

So with this I would like to throw the floor open to Q&A. Thank you.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Sudhir Bheda from Right Time Consultancy. Please go ahead.

Sudhir Bheda: My first question is sir, how much of your growth is led by increase in the price due to China import restriction? That is the first question.

Sucheth Davuluri: Okay. Can you ask the other questions as well?

Sudhir Bheda: Sir, is that margin what you have reported in the Q1 is sustainable and can you throw some long term outlook in your CMS business?

Sucheth Davuluri: Thank you for your questions. Our overall sales, revenues as well as our margins, have been largely unaffected by the China situation. So for us the primary situation that we have faced from China is managing the logistical issues and maintaining continuity of supply of raw materials, but we have not had any issue in terms of any significant price changes either on the consumption side or on the sale side.

As far as the margins for Q1, they do reflect our business as usual and not withstanding any significant unexpected changes. We do expect the margins to be sustainable.

Moderator: Thank you. We move to the next question. The next question is from the line of Sajal Kapoor from Unseen Risk Advisors. Please go ahead.

Sajal Kapoor: I have a few questions. So regarding this recent addition and qualification of a third party CMO for our sterile APIs, which is indeed a very strategic move for sure, so is this supporting our CMS pipeline or specialty GDS and when we do expect to go commercial using this third party CMO?

Sucheth Davuluri: Actually, when we qualified the third party CMO it was not done specifically with an intent only for GDS or the CMS business, it was done with the intention of making sterile APIs. However, currently the APIs that we are making at the third party CMO are for the generic space and one API we are already seeing commercial orders come through.

Sucheth Davuluri: It is for the specialty segment.

Sajal Kapoor: Basically, we have qualified this CMO for our specialty APIs on the GDS front, but the same facility can be used when required for our innovative synthesis pipeline, right?

Sucheth Davuluri: That is correct.

Sajal Kapoor: And second question is over the years, Neuland had a very immaculate regulatory compliance track record, starting 1997, but now that we are developing and manufacturing more and some

very complex chemistry like the sterile APIs and other complex APIs and the peptides as well. What are we doing to ensure that we sort of stay ahead of the curve as far as the USFDA, PMDA or any other regulatory orders are concerned because in recent days what we have seen is some of the API manufacturing units have been under USFDA scanner.

So now that the complexity of our business has increased many fold, what incremental steps are we taking to just stay ahead of the curve and not be sort of challenged by any of these stringent regulatory audits?

Sucheth Davuluri:

I think it is a valid question. Alluding to what you just said I think one of the reasons why we have a good track record would be FDAs because we have always put the culture of quality and compliance as a number one priority. I think as we added products and as the facilities became more multiproduct in nature, we ensured that these procedures, the overall culture of compliance, the training and development, updating those regulations and incorporating them into our quality management system were always done in a way which was very provocative so that we could continue the track record.

So we continued to do the same thing and we have been regularly inspected by the FDA almost since about 1997 and then in 1999, 2002 and since then we have pretty much had an inspection every year and sometimes it has been more frequent. So we believe that we need to keep that high level of awareness, keeping ourselves updated and ensuring that our culture of compliance does not get compromised at any time. So it is an ongoing effort. I do not think we can ever sit back and say that everything is hunky dory and we are in a strong position. I think we will continue to have that healthy level of paranoia at the system.

Sajal Kapoor:

That is reassuring, Sucheth. And lastly our margins have been steadily recovering over the quarters and given our strong focus on complex APIs and custom synthesis for innovatory molecules, which are higher entry barriers, higher margin play, what could be an aspirational operating margin over medium term, let us say three to five years? Any broad-brush guideline because now that we are into more complex APIs and custom synthesis for innovative, the margin should increase from here on. So we have been recovering, but what is the sort of aspirational target over the three to five years?

Saharsh Davuluri:

This is Saharsh. I think as you rightly indicated as the business mix improves, we have more CMS coming in, specialty APIs improve and even on the prime segment as well we continue to make cost improvements, we will see improvements happening first at a gross margin level and then later at EBITDA level. That is something that has already started to happen and as we have seen over years, we have also had ups and downs in our quarterly performance, largely determined by the kind of mix we have had in that specific quarter.

Two things we could say over here. One is we expect the business mix to continue to improve largely driven by CMS as well as specialty. But also very strategic growth coming from prime products where we are going to not add products which are not going to be profitable, but

products, which really utilize the capacities well. So as a result of that the operating leverage is going to go up. We are going to be getting more contribution out of our existing plants that should help EBITDA margin improve.

Second of all, we should also see through other measures like backward integration as well as strengthening our control on the manufacturing. We should see overall improvements in margins as well. The last thing I can quickly say is we have maintained in the past that our aspirational number has been 20% of EBITDA, but that has been a number that is largely going to be determined by how the business pans out.

So we are steadily seeing a progress in that extent and I think as growth comes through different businesses, we could see a certain level of variation on that, but beyond that we think it is difficult for us to give more specific guidance.

Moderator: Thank you very much. We take the next question from the line of Raj Rishi, who is an individual investor. Please go ahead.

Raj Rishi: What is the capacity utilization presently?

Sucheth Davuluri: On an average for whole organization it would be around 70% to 75%, but this varies from site to site as well as production block to production block. So right now unit-3 is the lowest in terms of capacity utilization. Unit-1 is probably on top and unit-2 is in the middle.

Raj Rishi: Any comments on USFDA status regards unit-3?

Sucheth Davuluri: Well it is a continuous process, so we are continuing to file unit-3 as an additional manufacturing site across our DMFs and we do not anticipate any issue in terms of unit-3 being able to supply to US or Europe or any of the other markets that we already supply to.

Moderator: Thank you. The next question is from the line of Sunil Kothari from Unique Asset Management. Please go ahead.

Sunil Kothari: Sir, my question is currently API producers are getting some extra advantage of demand locally and internationally so we being a pure API player mainly other than just CMS. So are we getting any advantage of those additional opportunities or not? And if not, then what is our strategy? This is my first question. And second is we have very low ROCE, so what has been our Historic ROCE and our aspirational ROCE? That is my two questions.

Saharsh Davuluri: So I will just try to give a brief response and then ask Sucheth also to share his perspective. I think with regards to the Chinese business, you are absolutely right because of the trade situation with China I have been getting feedback from customers and also we have been hearing from various fronts that both on CMS and GDS, there has been a greater focus on India and consequently there has also been a lot of interest in Neuland because we tend to be one of the few established players with a very strong track record.

However, that has not yet resulted in material improvements in our business. We continue to see a steady growth in our business. But we believe that over the long term this should help us. It will help us obviously in the specific products or the technologies we are strong in, but as we keep making investments and we keep adding the right kind of products, it should help us grow faster as well, but it is not very clear at this time. I will just pause here, let Sucheth also respond and then we will also answer your second question.

Sucheth Davuluri:

I think the only thing I would add to it is that there is definitely a trust deficit for companies that we were buying out of China and it is very clear to them that companies out of India as long as they can supply and meet their demand on time with a more long term reliable partner, so we are definitely seeing the evidence of that in our business.

It is also one of the reasons where in spite of being hit with the pandemic and the uncertainty because of the COVID situation, we never slowed down on our capital deployments to increase our capacity so that we are prepared to take on the opportunities. So we are definitely seeing that in the numbers and the consistent growth demonstrated by the organization and we will continue to do so.

Saharsh Davuluri:

On the ROC, I think we are mindful of the fact that the last two years, the ROCE numbers have been low. But I think back in 2015-16 it was around 18.5%, 2016-17 if I recall it was around 16%. Going forward, we expect to see good improvement in our ROCE because of the reasons that we have been talking about, better performance, better operating leverage and as a result we are being able to deliver more from our plants, being able to better utilize our access. So historically it has been a challenge in the last two years perspective, but we believe going forward our business will yield attractive ROCE.

Moderator:

Thank you. The next question is from the line of Viraj Mahadevia, who is an individual investor. Please go ahead.

Viraj Mahadevia:

Saharsh, I had a question. On page 21 of your presentation you referred to the commentary saying adding capacities for backward integration and new business. Can you elaborate a little bit on this backward integration? How much of your overall product suite is already fully backward integrated, now we going to 100% where we are completely backward integrated in all products and cut off dependence on China? Secondly can we expect gross margin expansion as a consequence?

Saharsh Davuluri:

On this question I think backward integration is something that we are looking at very carefully especially since the China situation erupted a few years ago and we had one financial year specifically where we got stocked out on Levetiracetam and we had huge financial impact. I think since then the organization has made strategic move on de-risking ourselves and as part of the de-risking strategy backward integration has been a key part of that strategy.

So, even I can share the broad numbers and may be Sucheth can throw more color on this, but compared to three, four years ago where we were buying may be 45% to 50% of our raw materials from China, today we are buying 20% to 25% of raw materials from China.

Not all of that has happened because of backward integration, but some of it has happened because of our ability to find local sources to be able to do technology transfers, to be able to integrate them well into our supply chain. But yes, in certain cases especially where the products are very important and the sartan materials are complex.

For example, SABAM for Levetiracetam or some of the other starting materials for our CMS project, we have intentionally used our unit-3 for backward integration and we will continue to use that strategy where it makes sense. What we do not want to do is blindly backward integrate on all our products because that is something necessarily may not generate more value or more margin going forward especially when you have seen a surge in good reliable Indian intermediate and sartan material suppliers.

Viraj Mahadevia: So I think it is important make versus buy decision and if you can buy it at a reasonable price then no need to invest and integrate. But would you say your raw material that you referred to 25% sourcing from China will come down to somewhere in single digits over the next year or two as you backward integrating more and more products and consequently expand gross margins?

Sucheth Davuluri: Yes, that is our target actually. So as you are saying earlier our strategy is not to completely backward integrate, but actually integrate good reliable partners and as long as we are able to ensure that, we feel like we have achieved the objective. So our goal over the next 12 to 18 months is to go down to less than 15% in terms of the materials that we procure from China, not that we do not want to have sources out of China, but to also have an equally robust source outside of China.

Viraj Mahadevia: Can I ask another question regarding peptides or should I get back in the queue?

Saharsh Davuluri: It is better get back in the queue because they are saying that we have a long queue, we will come back to you again.

Moderator: Thank you. The next question is from the line of H. R. Gala from Finvest Advisors. Please go ahead.

H. R. Gala: I got two questions. One question is as far as your CRAMs is concerned, each opportunity is probably of approximately what size in terms of the value that you can fetch over a period of the lifetime of the project? That is first question. And second question is, if we look at our last five years' performance, our revenue and profit have grown at CAGR of just 10%.

So next five years can you give us approximate indication that what kind of growth do we expect as you have always said that your 13% to 14% type of EBITDA margin will grow to

roughly say 20% in next couple of years because of change in the product mix? So how do you see this equation working for the next five years?

Saharsh Davuluri:

On the CMS business, we have provided the information in our slides, we have wide number of projects and as they become commercial they give us annual revenues. Today we are seeing projects, which give us as little as stable commercial revenue of Rs. 5 crores per year to molecules which would give us may be Rs. 50 crores, Rs. 60 crores, Rs. 70 crores a year. We do expect some molecules to be bigger blockbuster, so maybe they could potentially give us maybe Rs. 100 crores or maybe more. But they will continue to be a wide variety of products in this portfolio.

To answer your second question, we have said in past is that we expect this business over time to grow at about 20%. It could be give or take, they could be quarter-on-quarter, they could be year-on-year volatility as well, but that is the expectation we have going forward. We feel a lot more confident about the business today than say four or five years ago because we are at a bigger base.

Today, we are at Rs. 200 crores a quarter, we are at a Rs. 800 crores base versus may be three years ago, we were a Rs. 500 crores company. So I think we do have a stronger base, we do feel that overtime as I also answered the gentleman earlier maybe aspirational trying to get to 20% EBITDA and having a growth rate of 20% is something that we could share. But this is not really guidance and these numbers are just more to give you a broad sense of our outlook and I would probably just leave it at that.

Moderator:

Thank you. The next question is from the line of Vikrant Kashyap from Kedia Securities. Please go ahead.

Vikrant Kashyap:

Sir, I have just one question. Can we consider this performance as a base performance and do we expect to improve upon from here and if yes then what will drive the future growth?

Saharsh Davuluri:

I think Vikrant, it is definitely the performance was in line with our expectations and I think as it stands today despite the challenges of COVID, we think that we are in a good fortunate situation. So we think it is a reasonable base only because there are no exceptional items that have contributed to the business of this quarter. But I do expect quarter-on-quarter volatility so there could be some ups and downs as well. What was our second question?

Vikrant Kashyap:

If you improve upon from here, what will drive future growth? Which segment? Where do you see potential?

Saharsh Davuluri:

Yes, I think a lot of the growth will come across the three segments and not just saying this to be politically right, but we do have products and growth coming from the prime segment. Products like Levetiracetam, Labetalol, Mirtazapine will continue to do well, so on the prime segment they will do well.

On the specialty side, there are exciting parts like the sterile products that Sucheth was talking about and other new products that we are adding. We have talked a lot about CMS because we are also expecting a lot of projects to get commercialized in the next two years in the CMS front and some of these projects could be really big. However, we are also stay guarded because until the drugs do become commercially successful, it may not necessarily translate into API business for us.

But I think that is what going to drive the business and whatever business we are pursuing right now, these are all likely to improve our margins. We have been focusing on improving our margins even for prime through cost reductions. So therefore I think going forward the base that you have seen in this quarter and last quarter will be a decent base to benchmark and I think growth will come on top of this.

Moderator: Thank you. The next question is from line of Pritesh Vora from Mission Holdings. Please go ahead.

Pritesh Vora: Can you tell me how the growth will materialize? You highlighted GDS as well as the CMS, where do you think in next three to five years the growth will materialize from?

Sucheth Davuluri: I think Saharsh was elaborating on this earlier. But as we have mentioned in previous calls, that it is not one segment versus the other that we are emphasizing. We believe that our prime API segment continues to grow. Our strategy of course is different across the segments. For the prime API business segment our strategy is to add new customers for the market penetration, increase Neuland's market shares across the global market.

For the specialty API segment, the focus has been on technology patterns, supplying sterile API, complex APIs where we do not expect too much competition and obviously contract manufacturing side is where we also see the huge opportunity. And we have spent the last several years building capabilities to be able to consolidate our position in this market as well. So as we see it, we expect to continue to maintain focus on all of these segments and we expect all of them to grow and contribute to the top as well as bottom line.

Pritesh Vora: Our aspiration for 20% EBITDA margin because currently our margin is somewhere around 13% to 14%, so how do you bridge that 20% EBITDA margin aspiration? Which are the products which will give you that kind of a margin?

Saharsh Davuluri: See our margins recently have been at about 16.5% so what we have done in Q1 that is what we did in Q4 of last year. So I think going from 16.5% to 20% will happen as the CMS business as well as the specialty business continues to grow because those are two business segments, which have higher profit margin. And cost reduction has been a big focus for us especially in the last 12 to 18 months, so that should also help us sustain and grow on these margins going forward.

Moderator: Thank you. The next question is from the line of Sandeep Shah, who is an individual investor. Please go ahead.

Sandeep Shah: I have two questions. First is how many work days did you lose in the quarter gone by? So were they substantial or were they insignificant? And my second question is taking a queue from the slide, which shows the business growth strategy looking forward and you mentioned here that you want to augment capacity and also leverage your longstanding relationships with leading generic and innovative companies. So could you throw some light on this?

Sucheth Davuluri: Yes, I think in terms of working days we would have lost total 15 days in Q1. Obviously because of the dip in manpower and a staggered increase in manpower were spread over a much longer time. However, it would not be fair to connect that to the performance in this quarter because in several places we are able to recover from the loss in those working days and some places we will probably recover it over Q2 as well as Q3.

In terms of the overall strategy I think our strategy has always been clear there are a few pure play API companies who have had an implacable record with the USFDA. I was just mentioning earlier that will continue to be a focus area and we do that by being always paranoid that anything could go wrong and therefore we keep a very high kind of awareness.

So our goal going forward is to continue to grow the prime API segment by getting more customers, increasing our market share, continue to add capabilities on the specialty API side as well as a huge focus on the contract manufacturing side. That is our strategy going forward.

Moderator: Thank you very much. Before we take the next question, we would like Mr. Pingle to make an announcement.

Diwakar Pingle: Good evening friends. I think there are still about 25 people in the queue. We just like everyone to ask a question, so we are just restricting it to one per participant. So please ask your most important question then come back in queue again please.

Please do cooperate because there are 325 people in the conference and 25 people are still waiting in the queue and we do not want anyone to go without asking a question. So just restrict to one question. Do not ask three questions in one, just one question and then come back in the queue again.

Moderator: Thank you very much. We take the next question from the line of Mr. Mukesh Prajapati, who is an individual investor. Please go ahead.

Mukesh Prajapati: First thing is I just want to understand about the peptide commercialization, which we are expecting I think by August and September. Can you throw some light on that, sir?

Saharsh Davuluri: As as part of the 76 peptides projects that we have shown in our table, right now, we do not have any commercialized peptides, but in the future we may have peptide. But at this point we

do not have enough clarity as we would not be in a position to give any specific guidance on what will get commercialized when.

I do also want to mention that we have three peptides which are under development for the generic business, on the GDS side. For those peptides, we anticipate to file DMS in the next two years. So as we do that, those products would be commercially available. So that is kind of what I would share on the peptides front.

Moderator: Thank you. The next question is from the line of Keval Ashar from Investment Options. Please go ahead.

Keval Ashar: I would like to ask the question that what are the CAPEX plans over the next few years, every year?

G V Bharadwaj: So, as we mentioned in the earlier calls, the CAPEX for the year would be generally around, Rs. 45 crores towards maintenance CAPEX and for the year as a whole we expect it to be around Rs. 70 crores to Rs. 80 crores.

Moderator: Thank you. The next question is from the line of Rakesh Kumar, who is an individual investor. Please go ahead.

Rakesh Kumar: I have one very simple question. Is this EBITDA margin sustainable for the remaining quarters of this financial year?

Sucheth Davuluri: Thanks for your question, Rakesh. As we were mentioning earlier, this quarter has been business as usual for us, except for there was about 15 working days that were disrupted because of the pandemic and the disruption of operations. However, Neuland's team, our employees have been great through this whole period. They have been very committed and continue to be committed, and therefore notwithstanding any significant disruption, we do expect that these margins are sustainable.

Moderator: Thank you. The next question is from the line of Jay Shah from Navrang Enterprise. Please go ahead.

Jay Shah: I wanted to ask, actually going ahead with the API chain, for the peptide molecules, since lot of it is based on amines, has the company or the management thought of, try or procure it locally?

Because the amines industry is a very critical industry and based on how we are focusing the entire product chain on the peptide molecules going ahead, have we thought of doing backward integration in that similar field or how to procure the products domestically rather than importing them?

Saharsh Davuluri: Yes, so I think what you are alluding to is amino acids, which form the base ingredient of peptides. I think today amino acids are naturally occurring as well as synthetic. And there are very established companies in China, in Japan, some in India as well, which specialize in making amino acids. And today we source many of these amino acids from these companies.

Sometimes if there is a complex amino acid, we make it in house. But it is not really our strategy to backward integrate and make those because that is a very different infrastructure and knowledge base needed for that business.

Moderator: Thank you. The next question is from the line of Nikhil Upadhyay from Securities Investment Management. Please go ahead.

Nikhil Upadhyay: Saharsh, I just wanted to understand this. The PLI scheme which the Government has launched, how do you guys read it and, because we are a pure API player and because of the production-linked incentives, do you see any merit in this scheme for any of the products we could be looking at?

And secondly, post the PLI, so players who are opting for PLI, do they actually become competitive versus Chinese or the pricing-wise the competitiveness is still un-competitive to China?

Sucheth Davuluri: Yes, thanks for your question. I think there are about 53 APIs listed under this PLI scheme. And out of those APIs, we have about four APIs that we manufacture. However, where we found the possibility of applying this scheme is if you are undertaking any new capital expenditure to make these APIs for the domestic market consumption, then the Government would give back rebates to the tune of 10% to 20% off the money spent by the organization.

So, we have done a thorough evaluation. And right now it is possible that one, at the most may be two APIs could possibly benefit. Where we are not clear is how much volume we could actually sell in the domestic market versus how much would be exported. So, the benefits on the PLI scheme is not very clear at this point. We are still waiting for further clarifications from the Government.

Moderator: Thank you. The next question is from the line of Rahul who is an individual investor. Please go ahead.

There seems to be no response from the line of Rahul. We will move to the next question. The next question is from Palak Agarwal from The Tycoon Mindset. Please go ahead.

Palak Agarwal: I really wanted to ask like looking at our annual net cash numbers, which was around less than Rs. 20 crores, and coupling with promoters' stake, how we are planning to fund our further CAPEX? And how would it impact our debt to equity?

G. V. Bharadwaj: Palak, for our regular maintenance CAPEX, we have maintained it with our own internal accruals. But if there is any CAPEX for putting on a capacity expansion, we have our own criteria of payback period of about 36 months to 48 months. So in all these scenarios, wherever possible, we use a debt-equity mix to make sure that our ratios are intact and in line with the overall requirements. And we do not see much degradation in terms of debt to equity ratios.

Moderator: Thank you. The next question is from the line of Deepak Mehta who an individual investor is. Please go ahead.

Deepak Mehta: So my question is that as more and more biotechnology companies are focusing on Corona, so there is possibility their budget is, might get cut down and it indirectly might hamper our company because we have some of the biotechnology mid-sized company as a client. Any insights you can give on this, sir?

Sucheth Davuluri: So far we have not really seen any significant change in the demand from our customers. You are right, there are a lot of companies that are focusing on research related to the COVID pandemic, but these are new companies, and companies that already had capabilities in these areas.

We are really not seeing any biotech or drug discovery and development companies change their focus, let us say, from a CNS area to the COVID situation, because that is the need of the hour. And our demand and interest from those kinds of companies continues to be stable.

Moderator: Thank you. The next question is from the line of Srihari C. from P.C.S. Securities. Please go ahead.

Srihari C: If I have to restrict myself to one question, then it would be pertaining to your workforce. Except your scientists, I think it is around 700. So, can you please give a breakdown in terms of how many are permanent employees? What is the temp force? And has there been any impact across the temp force is concerned because of the pandemic? And is there any possibility for a re-structuring there?

Sucheth Davuluri: Yes, so our full-time work force is actually closer to 1,260. And then we have contract workmen on top of that. So, as a result of the disruption or the COVID situation or the pandemic, we have not had any layoffs. In fact we, given that this has brought out a lot of uncertainty even for employees. This is the time where we felt the need to step up and take care of their needs and make sure that we are not causing them anymore uncertainty or anxiety than what is already being experienced.

So, on top of that, as I was mentioning earlier, there has been tremendous commitments from all of the employees of Neuland during this extremely difficult situation. They have shown up to work even when the company was not able to provide transportation. They have used other

modes of transportation just so that they could be here and help continue the operations to the organization.

Moderator: Thank you. The next question is from Gagandeep Singh who an individual investor is. Please go ahead.

Gagandeep Singh: Hi, I was wondering if you could throw some light on the pipeline of peptide? And, also wondering if you are counting on any particular peptide for the DMF submission?

Saharsh Davuluri: Yes so, as I was answering to a gentleman earlier, we do have several peptide projects in our CMS portfolio. Many of them are still under development. Right now there is no peptide which is under the commercialized category for CMS. However, on the GDS side, we do have three peptides which are under development for which we expect to file DMF in the next two years. I can share those names.

They are public information. It is Linaclotide, Liraglutide and Semaglutide. And they are very exciting, and we do expect to see a good part of our growth in the future coming from peptide. But at this point, we are not being very specific about it because we do not see anything very near-term.

Moderator: Thank you. The next question is from the line of Pratik Kothari from Unique Asset Management. Please go ahead.

Pratik Kothari: Hi, sir. If you compare our other expenses, manufacturing expenses quarter-on-quarter, even in absolute terms or also as a percentage of revenue it has come down substantially. So, anything you would like to call out on that? Is this sustainable mainly of the manufacturing and other expenses?

Sucheth Davuluri: Sorry, if I understood your question, what you are asking us is that you have seen that the expenses have come down, or remained stable? And if we believe that sort of a thing is sustainable? Is that your question?

Pratik Kothari: Yes, because if you compare quarter-on-quarter, from Quarter 4 of FY20 to Quarter 1 of FY21, our revenues have gone up, but our other expenses and our manufacturing expenses come down substantially. In absolute terms, about 15%, and as a percentage of revenue, significantly. So is there any one-off, anything you would like to call out on that?

Sucheth Davuluri: Not really. I think we do expect and as you know that Unit 3 is also ramping up as well. And that is, that will start to add to the revenue stream. On top of that, we are also tracking our expenses very, very closely. Expenses which are related to the pandemic as well.

And as a result of this whole COVID situation, there were expenses that we would otherwise incur, which we have not incurred, such as conferences, travels, sales & marketing expenses, without really eroding any revenues.

On top of that, we have also seen a better product mix. Therefore, our expenses did not increase proportional to the revenues as well. So, all of this has contributed to a better margin. And that is why we expect that it would be sustainable.

Moderator: Thank you. The next question is from the line of Raj Rishi who an individual investor is. Please go ahead.

Raj Rishi: What is the sort of asset turnover ratio which you look at, for incremental CAPEX?

Saharsh Davuluri: Yes, so your question was, what is your asset turnover ratio? Current asset turnover ratio?

Raj Rishi: Of the incremental CAPEX. Yes, that is right.

Saharsh Davuluri: Bharadwaj, do you want to answer that question?

G. V. Bharadwaj: Yes. The current asset turnover ratio is about 2.48. And going forward it could be more in line with the same expectation, the ratio would be intact.

Raj Rishi: Okay, and any fund-raising plans? QIP, etc. because the market is giving its evaluation better than earlier. So, any comments on that?

Saharsh Davuluri: No plans as of now.

Moderator: Thank you. The next question is from the line of Sajal Kapoor from Unseen Risk Advisors. Please go ahead.

Sajal Kapoor: Thanks for the follow up first of all. So how do you see the industry structure unfolding for the Indian players as the world is aiming to sort of de-risk their sourcing requirements away from a single supplier? And the potential revival of API manufacturing in the western world?

So, what we hear today is that there are many API companies, good quality API companies in Europe and US as well. And they are going for capacity expansion using a much superior technology relative to some of the Chinese as well as the Indian players. So, how will that change the dynamics of the API manufacturing over the medium to long term?

Saharsh Davuluri: It is a very deep question. So may be, I think both Sucheth and I will try to give our perspectives on it. I think the way we look at API business especially from Neuland's perspective, the way we see it is we produce 75 APIs commercially today both for CMS and GDS. Today if you go to Europe, and you try to identify how many European CMOs produce 75 APIs on an on-going basis, you will probably not even get a handful of them.

So, I think when it comes to the depth of experience in producing APIs, I think companies like Neuland, we have really gone through a lot. And I believe that that knowledge is invaluable going forward.

You are absolutely right that supply chain de-risking is going to be the way forward. People, pharmaceutical companies do not want to be single source, especially if that source is in China. And I think that will help in many ways for Indian companies, pure play API players like Neuland, to consolidate our position and grow.

Modernization and usage of technology can play an active role in making our efficiency go up. And I think that is something as a company we are looking as well. So, for example, instead of using traditional vacuum tray dryers, we are moving towards to modern drying equipment. We are doing this in a phased manner across all our facilities. That kind of modernization is something that any leading company will have to do, whether you are in India or in Europe. And I think that is something we will do.

Obviously, I think as you probably know, Europe will still continue to be a strong player for APIs they have traditionally been very strong. And if they invest in capacities then definitely that could be an alternative to China. And I do believe that the market is large enough that even if there is a threat from the European resurgence, it will not necessarily be detrimental to Neuland or the Indian API industry.

Sucheth, you want to share any thoughts on that?

Sucheth Davuluri:

No, I also think similar really. I think, even historically, we have always said this to our customers is that, we never position ourselves as an Indian API company with a lower cost base, trying to penetrate the market share. We have always competed based on our chemistry as well as our technology. And that has nothing to do with being based out of India or having lower labor cost or the cost of capital.

So, our focus continues to be the same whether it is in contract manufacturing specialty APIs as well as our prime APIs. Just that we continue to focus on adding capabilities, focus on technologies so that we can do better APIs, in the products that we manufacture, better than others.

Moderator:

Thank you. We will be able to take one last question. We take the last question from the line H. R. Gala from Finvest Advisors. Please go ahead.

H. R. Gala:

Yes, you know I was cut short. My question is, you have guided for about say, Rs. 70 crores to Rs. 80 crores type of CAPEX. But, say in case some opportunities come up in CMS space, will you have to spend something more on that?

Saharsh Davuluri:

I think the number that Bharadwaj had given you is the kind of CAPEX we need for the business that we are seeing in front of us in terms of the order book or contracts or confirmations from the customer. But as the aspiring company that is focusing in new projects, there could be certain projects that would need CAPEX. So for example, there might be a peptide project that might come tomorrow that would require a project-specific CAPEX. The

CAPEX that my colleague had referred to was the CAPEX for the business that is already visible for us, in terms of contracts, purchase orders, confirmations etc. Other than that, if there are new projects that are coming up, say like a peptide project or something that is very specific than there would be a project-specific CAPEX that would be incurred. And we would make sure that we make those investments in line with the guidance that we have for our finance department, in terms of the kind of returns, etcetera that we would like to have.

And also, when it comes to project-specific CAPEX, we would also probably negotiate for advances from our customer to make sure that we are not having to fund the entire CAPEX by ourselves.

H. R. Gala: Okay. What could be the approximate size of those CAPEX plans, project CAPEX? Approximate.

Saharsh Davuluri: Could be Rs. 5 crores, could be Rs. 20 crores, could be even like Rs. 50 crores. So, it could be a wide range of CAPEX. Small CAPEX we would not typically ask customers for advances. But if it is a specialized project, then we would ask for an advance.

Moderator: Thank you very much. We will have to take that as the last question. I would now like to hand the conference back to management team for closing comments.

Sucheth Davuluri: Again good evening everyone. Thanks a lot for all your questions and interest in Neuland. Thanks for being here on this call and for all the questions. It definitely helps us look at our business from your point of view as well and that is very helpful. I would also take this opportunity to thank the entire Neuland team that has really worked relentlessly with an amazing level of commitment through this disruption, through this uncertainty of the pandemic and what you see today in terms of our results and ongoing performance is a direct outcome of the commitment of all our employees.

So thank you again for the continued interest. Hope we have answered all your questions and if you have any further questions, you can reach out to us at any point of time and we will be more than happy to take and clarify whatever questions you might have. Thanks again and have a good evening.

Moderator: Thank you very much. On behalf of Neuland Laboratories, that concludes this conference. Thank you for joining us. Ladies and gentlemen, you may now disconnect your lines.