



“Neuland Laboratories Limited Q1 FY23 Earnings Conference Call”

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Moderator: Ladies and gentlemen, good day and welcome to the Neuland Laboratories Limited Q1 FY23 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing ‘*’ and then ‘0’ on your touchtone phone. Please note, that this conference is being recorded. I now hand the conference over to Mr. Diwakar Pingle, from Ernst & Young. Thank you and over to you, sir.

Diwakar Pingle: Thank you, Tanvi. Good evening friends. We welcome you to the Q1 FY23 Earnings Call of Neuland Laboratories Limited. To take us to the results and to answer your questions, we have with us the top management from Neuland, represented by Mr. Sucheth Davuluri - Vice Chairman and CEO; Mr. Saharsh Davuluri – Vice Chairman and Managing Director; Mr. Deepak Gupta – CFO and Mr. Sajeiv Emmanuel Medikonda – Head, Corporate Planning and Strategy.

We will start the call with brief overview of the financials by Deepak and then Saharsh will give you a broad highlight of the business trends and what he is observing in the markets and post this, we will open it to the Q&A session. As usual, the standard safe harbor clause applies as we start the call. With that said, I now hand over the floor to Deepak. Over to you, Deepak.

Deepak Gupta: Thank you very much, Diwakar and a very good evening all friends and very warm welcome to all of you for our Q1 FY23 earnings call. I think that you must have seen the presentation, which Diwakar was just mentioning about and it is put up on our website and also we have uploaded both on BSE as well as on NSE websites. As always, any comments on the content of this presentation, which we have sent will be highly appreciated and we will do our best to give out additional data points which will help you to analyze the data points much better.

I will briefly talk about the financials. The total income for this quarter is Rs. 221.7 crores as against Rs. 202.9 crores in Q1 of FY22. While our performance has improved compared to the last year, we had expected far better. Our EBITDA for the quarter was Rs. 29 crores with EBITDA margins of 13.1% which was almost flat as we compare to the previous year, which was 13.6% and it has decreased by 220 basis points based on a sequential basis. I would like to give some context on the flat EBITDA margins on yearly basis. We continue to experience increased cost structures across the whole value chain, for example, raw material cost, logistics, power and fuel cost, etc. Our focus is more on execution excellence and to optimize cost to ensure integration from the external events that we are facing.

We have also witnessed high manpower costs and other costs arising mostly from unit III commercialization that we did earlier. We continued to maintain high levels of inventory to avoid any future possible disruption due to disruption which are happening globally as of now. I would like to share that our focus on improving the business mix has also led to increase in the

gross margins. Gross margin was 46.1% in Q1 of FY23 as compared to 41.5% in the last quarter and also 42.4% on Q1 of FY22. Also, we expect this shift portfolio to continue to drive higher gross margins. Profit after tax was at Rs. 9.8 crores as compared to Rs. 8.6 crores last year. This quarter EPS is at Rs. 7.7.

In terms of cash and cash equivalents as on the date of the balance sheet which is June end, it is at Rs. 18.1 crores. We continue to make investments in the future and also for the CAPEX we have spent around Rs. 15 cores in Q1 of FY23 and also if we talk about the CAPEX plan, it is on track and with greater commercialization of products which is happening and also for the future commercial prospects. We expect that CMS segment will perform well and it will also help us to do our future innovation as well. I would like to mention that even though we have done substantial CAPEX till date, our net gearing ratio continues to be low. So, as of now, it is at 0.2x. With that, I would like to hand over the call to Mr. Saharsh for his remarks and thank you very much.

Saharsh Davuluri:

Thanks, Deepak. Good evening everyone. Just like to add a few comments on top of what Deepak has already said and then maybe we can open it up for Q&A. In terms of the prime business, we did have a very muted quarter. We have done well in products like Levofloxacin, Ciprofloxacin and Labetalol, but I think the product which has been our largest in the prime segment Levetiracetam, which has been doing well for us historically, we have had challenges in this quarter. We believe that this is also because of limited customer offtake, possibly because of high inventory. We expect that the volumes should recover in the coming quarters based on what we have seen historically with a product like this. On the specialty side, we have recorded good growth, which is very encouraging. Products like Donepezil, Salmeterol, Apixaban and Paliperidone have done well for us and that is something we are excited about. These have also helped us in maintain healthy gross margins.

With regards to CMS, we have clocked around Rs. 69 crores, which is a growth of over 50% year-on-year basis. Here, I would like to point out that our CMS pipeline is growing strongly with a number of molecules moving to commercial stage. We have seen traction across the clinical lifecycle. We have also added 3 new projects in the early stages of the quarter. We have also seen an exclusive development product for our customer go commercial this quarter. The cumulative impact of these developments lead us to believe that they are a harbinger for a higher and more stable CMS revenues in the future.

In terms of the business, as we have already mentioned, we are working with a lot of biotech companies, many of them are US based and our ability to complete challenging last-stage projects is what sets us apart and establishes us as a highly regarded CMO. As a result, we have been putting a lot of effort into accelerating the completion of our projects and, although we have been making steady progress over the past several months, we do continue to face delays in execution, for a variety of reasons. Our customers do understand and comprehend the

complexity of these projects and they continue to be very supportive of us as we work towards scaling up these New Chemical Entities. I would like to also say that unit III is scaling up successfully. Some of our important late-stage CMS projects are also being ramped up over there as we can see. As these products scale up, unit III's usage has also been driving up gradually and consequently as Deepak has also remarked, unit III has also contributed to rising operational expenses. We also continue to see good traction with both GDS and CMS customers that would help us drive growth in the medium to long term. The potential for the CMS projects, especially in phase 3 for both development and commercial which have been evident in the revenue in this quarter as well as for specialty GDS business gives us the confidence that the long-term business profits remains intact and while the results of the quarter have not been encouraging, we expect to be back on track for growth this year. These are some of the comments that I wanted to share. Maybe, we can now open it up for Q&A, Diwakar and then we will be happy to answer more questions. Thanks.

Moderator: Thank you. We will now begin the question-and-answer session. The first question is from the line of Mr. Keshav from RakSan Investors. Please go ahead.

Keshav: Good evening sir. Sir, in our presentation, we have mentioned about delays arising in CMS due to technical complexities, can you share some light on the same, what challenges we are facing over there and has that led that to any delays in delivery from our end?

Saharsh Davuluri: I think the complexities are quite varied. I think as the molecules we are scaling up our APIs are in phase 3 going into the commercialization and typically, when we are scaling up these molecules, there are a lot of restrictions in terms of our ability to treat the process. There are a lot of restrictions on what kind of analytical methods can be used, there are lot of restrictions on specifications, there are also restrictions on what kind of documentation is needed. What kind of data needs to be generated. So, when we are scaling up these molecules, there are several restrictions that apply towards the scaleup and obviously the scaleup is also successful when you are able to achieve the yields and the costs that are targeted in the project. So, sometimes when we are scaling up these kinds of molecules, we are also referring to the original process that may be the innovator may have developed and sometimes there are minor variations that might come out between the process that we are scaling up versus what the innovator may have originally designed. So, these result in certain challenges either on the chemistry side or on the analytical side or on the engineering side and those are the things that sometimes require us to pause the project, go back to the lab, do some studies and then come back and implement it and sometimes they could add to delays and in a project that is like a phase 3 API or any API that is going to validation, a difficult project from the start to finish takes a year and these kind of challenges could potentially add several weeks to the delay. So, these are broadly some of the challenges we face in the API scaleup phase, particularly from a CMS prospective.

Keshav: We haven't faced any delays in delivery of the product, right, it is just at the lab end, we are facing some complexities because for phase 3, I reckon there will be time critical, they require it at a particular time?

Saharsh Davuluri: No, this will eventually lead to delay in delivery of the material also because when you are having to go back to the drawing board or you are having to go back to the lab, you are actually pausing the campaign in the plant and once you fix it, then you go back to the plant, so typically it will result in a delay in the campaign.

Sucheth Davuluri: Absolutely, there will be a delay in the campaign, but at the same time we probably know our customer's priorities, their programs, their projects were also undergoing change based on their priorities. So, what you are ensuring that, the delays from our end are really not impacting the timelines of our customers that we are able to make sure that we are just ourselves to still keep the customer programs on schedule and that is where we have been successful.

Moderator: Thank you. The next question is from the line of Mr. Subramanian. K from Alpha Invesco. Please go ahead.

Subramanian. K: Sir, I wanted to understand about the CMS segment, overall, we had a more than 50% growth year over year for this particular quarter and in the commercial segment, we had almost doubled and in the development, we had almost 30% increase in revenue, sir can you break down how the growth will be in each segment and what is the margin in each segment?

Saharsh Davuluri: I think broadly your analysis as it reflects, the growth has come in the overall CMS business, it has come both from the baseline business as well as from the development business. I think, the baseline business is driven by one of our key CMS molecules that has been doing well over the last year or two and I think the volumes are continuing to increase. There are multiple products in the baseline, but the growth has been driven by one particular molecule. On the development side, there have been multiple molecules. As we have been mentioning in our comments for the past several quarters, there are several molecules that Neuland is actually going through phase 3 into commercialization. Some of these molecules are going through various phases and whatever revenues we are recognizing in those projects, which are not yet commercial, but are getting scaled up, those are categorized as development revenues. So, it is not necessarily triggered by one molecule, but it is triggered by multiple molecules that are not yet commercial and so that is a kind of how we would analyze the numbers.

Subramanian. K: So, regarding the margin, whether the margin differs in the commercial and development?

Saharsh Davuluri: No, I think every molecule has a different margin profile with various dynamics, but broadly speaking, development projects seem to have higher margins than commercial molecules, but they are always different cases.



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- Moderator:** Thank you. The next question is from the line of Amey from Haitong. Please go ahead.
- Amey:** I just have one question to the management, in the commercial side, we have added three new products at least what they showed on the PPT, is it possible for you to give further color on these three new projects from the commercial side?
- Sajeev:** Amey, I think over the last one year as you rightly pointed out that we have had 3 projects moved then from development to commercial. Of them, I think two are NCEs where we are part of the NDA, we are part of the filings, one of which is for antibacterial and antifungal segment and the other is for a broader therapy area and the third molecule is something that we did custom development for a customer who has now commercialized the products with their set of customers. So, these are the 3 molecules, which I can talk about without giving away more information in line with our agreement.
- Amey:** Just one follow-up, what are the probably timeline for the monetization from the commercial side?
- Saharsh Davuluri:** I think the way we measure the business Amey, is when we start calling it commercial it means that the molecule, we are ready, the validation is over and we are ready to start commercial supplies, but as you know, in many of these molecules, they have life cycle, right, when in the early stages of commercialization, the volumes are typically low. After 1-2 years maybe they start picking up, years 3 to 5 is when they typically peak. That is the only information we can give because each of these molecules has a different profile and we really don't have specific molecule level clarity which we can share in terms of how we will go, but once they become commercial, the idea is that the volumes will start picking up.
- Amey:** So, these are recently approved molecules or these are molecules which were already approved, but we got the contract now?
- Saharsh Davuluri:** So, Sajeev told you about 3, two of them are New Chemical Entities which have been recently approved. One is the older molecule for which Neuland has actually adapted technology and has scaled up. So, two are new and one is old.
- Amey:** So, at least that the older molecule we should be able to get them phased up quickly, right because it is an old molecule already?
- Saharsh Davuluri:** No, all three of them we have an indication of how the volumes are likely to pan out, it is just that we would not go into product level explanation of how we expect the volumes to fair up.
- Moderator:** Thank you. The next question is from the line of Pramesh, Individual Investor. Please go ahead.

Pramesh:

I have couple of questions, number one is you have seen that your CMS segment is growing, but if you see over the last 3 quarters, the CMS segment has not been growing at all, it has been coming down continuously. If we see that the growth as compared to last year last quarter same time, then it is probably mostly because of the base effect we had supply chain issues at that point of time, so how do I read as an investor in terms of how it is growing in the sense because the GDS is not growing, the CMS as I see is not growing, so as an investor, where do I look for actually in terms of the growth? I understand CMS should be a growing segment, but it is not so actually? That is number one. The debt movement, I would also, I would not use the word erratic, but net debt movement also is completely like, one quarter it goes up, other quarter it goes down, so I am not able to figure it out in terms of a net debt movements, it is Rs 214 crores from March 20 and it has come down and then again it has gone to Rs 212 crores and then again come back to Rs 160 crores now, I think I had asked you this question last quarter also that why the debt has gone up? Now the debt has come down also, that is the net debt obviously, I am not talking about the debt per se so again that is another question and the last part is, how much depreciation of your third unit plant is still pending to be incorporated as expense? So, these are my 3 questions?

Saharsh Davuluri:

I will answer the first one and ask Deepak to answer the second and the third. I think with regards to your observation about the CMS business, I think it is absolutely valid. I think the business has been volatile in many ways. Yes with regards to Q1 of FY22, it is showing 50% growth, but if you sequentially look at the last 4 or 5 quarters, it actually doesn't indicate a growth not so consistently at least. I think the way I would look at it or rather explain it is our CMS business comprises of both a baseline business as well as a development business. Today, Neuland is a kind of in a phase where are we are moving from development projects and we are moving our development projects into commercial projects. So, as Sajeew had answered to the gentleman earlier also, we had talked about molecules which have been commercialized in the last one year. They are molecules which are likely to be commercialized in the next 12 months as well. These molecules are not yet consistently on a quarter-on-quarter contributing to the baseline revenue of Neuland. With regards to the development revenues, the development revenues are fairly volatile because depending on which quarter we execute our project, the revenues of that particular quarter go up or they don't go up. So, we have been experiencing over the last 4-5 quarters, a situation where we are converting development projects into commercial projects, commercialization has happened. More importantly, we are also executing and continuing to execute more development projects. So, from a progression point of view, we are seeing a healthy progress in development projects, we are also seeing a good conversion of development projects into baseline projects and we are also seeing revenues from that. If you look at it from a quarter to quarter basis, it does show inconsistency, but the way I would look at our CMS business is look at it from a fairly long perspective, look at it over a 15 quarter period and if you look at it over a 15-20 quarter period, you would actually see that there is progression and as I had also mentioned in the opening remarks, we are still in the early stages of our CMS business where commercialization has still not happened yet and as then when more molecules get

commercialized, that is when we will actually start seeing more consistent performance in terms of the revenue. So, I think that is the kind of how we would look at it. If you look at it from a slightly broader horizon like 3 to 4 years, you will be able to see growth, you will also be able to see from the disclosures we have made that the number of projects have been consistently increasing, you will also see that molecules have been consistently moving from development to commercialization and we have been very consistent in what we have been sharing. I think at this point of time that is the only information I think we can share and I think our expectation is that this path will take us towards higher growth in CMS. So, that is how I would look at it and maybe I will ask Deepak to answer the answer the second question.

Deepak Gupta:

With respect to the net debt, so yes it has substantially come down from Rs. 212 crore to Rs. 160 crores, so it is because of a better cash flow that we have generated in this quarter mainly coming from higher realizations from the debtors as well as we have received the advances from the customer for certain CMS projects. So, overall we have repaid more than Rs. 45 crores to Rs. 50 crores debt back to the lenders, so this has helped us to improve the leverage that we have taken, right, so that is with respect to the debt and with respect to the second question, about how much is the remaining unit III assets that needs to be depreciated, so as of June end roughly around Rs. 225 crores of block needs to be depreciated over the period of time. Definitely, it is like a spread across several years from now. So, still unit III is pretty new in our portfolio and we will see that investments happening in last couple of years to build unit III, so still Rs. 225 odd crores needs to be depreciated over a period of time.

Moderator:

Thank you. The next question is from the line of Keval Ashar from DSP Investment Managers. Please go ahead.

Keval Ashar:

So, just a few questions, so first as you have mentioned that in FY22 annual report that you will be also focusing on GDS segment for the growth this year, but this quarter we had underperformance in GDS, so sir, just wanted to understand have you lost any customer or there were delays in the orders for us?

Sajeev:

Keval, to answer your question, when it comes to the GDS business overall it is more in terms of certain customers for products, we see that they have issues in terms of their inventory, but we have not lost any customers, we see their interest in the products like even as Saharsh had mentioned during his opening comments, even though Levetiracetam didn't do well in this quarter, but over a period of time, we see that there are orders and our customers leave the product, I think with respect to this quarter, a product where we didn't do well, but we see that coming back and over the period of time, we will see that in GDS, specialty products, we will also do well and we are quite excited about with products which Saharsh had mentioned with you is Apixaban and Paliperidone Palmitate as well as Donepezil which are doing very well there. We have seen customers do launches for a novel forms, so I think overall the GDS business

is expected to grow, but I think this quarter was a little decline around 7%, but that was basically because of reasons which are more with respect to timing.

Keval Ashar: The next question is that if I heard it right, you mentioned that we did Rs 50 crores of expenditure in quarter 1, so what was this expenditure for? Second is, the total expenditure we have done in unit III till now? And the third is how much CAPEX are we doing this year? And in coming years how much CAPEX year-on-year do we plan to do?

Deepak Gupta: In this quarter, we have done CAPEX investment of Rs. 15 crores and unit III out of this Rs. 15 crores is roughly around Rs. 2 crores that is your first question and with respect to how much CAPEX we will do, so we will stick to what we have said earlier, like this year we will be spending close to Rs. 70 crores to Rs. 80 crores in the CAPEX investment for the full year, so out of that, Rs. 15 crores is already a kind of taken care of in this quarter.

Keval Ashar: Another question is, you mentioned, Saharsh specifically mentioned that now we are in a growth trajectory and we plan to grow this year as well, so sir, last year we had a base of Rs. 951 crores of topline in FY22, so this year if you can give any guidance for the growth in topline in FY23?

Saharsh Davuluri: Keval, I think what we have said in the past and in over a period of time, I think in Neuland we have targeted around may be 15% to 20% of average growth over the period of time. I think we have also observed that over FY21 and FY22, we had actually stagnated, we have not grown at all. I think the comment I was making I think is really to indicate that the way things are shaping up and the way this year is and how the future is, I think it is based on these metrics from CMS and GDS side. We expect to get back on track with regards to that growth past that we have been talking about, but I think having said that as you know we don't give guidance. So, we are not really be in a position to give guidance either for FY23 or for the near term, but I think at least we feel that the period of stagnation that we went through, we will break away from that and we should get back on track for growth. I think that is a kind of how we would clarify that.

Keval Ashar: And the last question from my side is that since you mentioned that 15% growth we targeted in the medium term, so CMS given the lower base compared to our other 2 segments as a percentage of revenue, so if we grow our overall revenue at 15%, at what rate, do we expect CMS to grow in midterm?

Saharsh Davuluri: No, I think CMS being the smaller business, I think it contributes only over 30% of our overall revenue. I think its growth is expected to be at a higher rate, but we really would not be able to give you any kind of a breakdown. I think, mathematically, you know it will grow at a higher rate than what the average growth rate of the organization is going to be, but we don't want to give more color to it than that.

Moderator: Thank you, the next question is from the line of Aditya Khemka from InCred PMS. Please go ahead.

Aditya Khemka: Saharsh, I understand the gross margins this year or this quarter, obviously you had a favorable mix, you had more contribution from CMS relatively versus GDS, but can you talk a little bit about your input cost, how they have behaved quarterly, let us say 4Q 22 versus 1Q 23, are you seeing some cool off in the spot prices, how much inventory of high-priced raw material do you have and when does the lower spot price raw material procurement translate to lower cost for you?

Sucheth Davuluri: Just saying that it is not secret that because of this whole Russia-Ukraine conflict, there has been a lot of volatility especially in the pricing, not so much on the supply of raw materials. On a net basis, we estimated that the impact for this year alone was almost of the amount of about Rs. 45 crores, taking the spot prices into consideration. Notwithstanding that, we have taken a lot of corrective and preventive measures, so that we can mitigate a lot of this impact by working with our customers, getting price increases wherever we can and also taking aggressive steps inside to reduce our cost. So, our goal is and that is what we have said today in the release to our results as well that even though Q1 saw a significant impact from that pricing in spite of the favorable product mix, for the entire year we do expect our performance to be as per expectations, but those are roughly the contours that was going on.

Aditya Khemka: The only thing I wanted to understand was that, are you seeing any decline in the raw material prices at the spot market or are the raw material prices still as elevated as they were let us say in 4Q?

Sucheth Davuluri: As if now, it has been even split Aditya, we are seeing softening of prices for certain solvents and certain raw materials, whereas for some of the other raw materials, it has actually gone up. However, for the whole year, as compared to where we were, at the beginning of the year, we still expect may be 20% to 25% softening of the prices.

Aditya Khemka: And that is for all your raw material as a basket that 20% to 25% decline in prices?

Sucheth: That is correct.

Aditya Khemka: And how much inventory of raw material do you normally maintain in your business across the 3 segments with a specialty, prime and CMS?

Sucheth: About 30 days, I think that is how much will we will update.

Aditya Khemka: 30 days?

Sucheth: 30 days or 40 days we maintain.

Aditya Khemka: Now coming to the prime API segment right, so in the prime products, you obviously mentioned a few products which did very well for you, but at a basket level, the prime did not do well for

us, so can you name a couple of products which did not do well because they must have done really bad for the overall segment to decline, despite some of your larger products doing well for you in the basket?

Sucheth:

I think Saharsh mentioned this in his opening Aditya, but our biggest impact on the prime segment was Levetiracetam. Levetiracetam is also our largest product in the prime segment and that is what impacted our performance. If we believe it is the combination of reduction in demand as well as some inventory buildup at our customers end, however, when we examine the market for future requirements, we don't see any significant alarms, but as far as Q1 is concerned, the biggest impact was Levetiracetam followed by another product of ours called Mirtazapine, but we do see the demand coming up.

Saharsh Davuluri:

I think Levetiracetam has been our largest product over the last 3-4 years and I think even our 15% decline in volumes on Levetiracetam actually had an impact. So, I think, frankly speaking from GDS point of view, other than the hit in Levetiracetam which we believe and hope is temporary, there is nothing else that causes concern for us at this at this point of time.

Aditya Khemka:

Sorry to hop on this, but I have a follow up on this. So, Levetiracetam, the hit will be temporary only if it is driven by an inventory buildup at your customer level where he is sort of rationalizing his inventory, but if it is driven by competitors getting more aggressive or lower pricing and competitors gaining market share from you, then it may not reverse. My concern on Levetiracetam is the Divi's in their remarks historically have said that in this particular molecule, they have backward integrated a lot, they have increased their volume production, so you see my concerns there right, so which is why I am a sort of trying to get more sense from you as to whether Levetiracetam volumes will ever bounce back or what are we perceiving as inventory correction is actually a shift in market share from us to our competitors?

Sucheth Davuluri:

Aditya, we think that your concern is very similar to our concern as well. So, our response is stemming from two factors and it doesn't take away from your observation. One is, when we saw a decline in volumes of Levetiracetam, we got in touch with all our customers, we pulled the data from the market, we analyzed the market share of all the companies out there, we marked to the customers that are buying from us and customers that are buying from our competition, we looked at the export data and we also got feedback from our customers whether they have any accumulated inventory or have they lost market share. So, our response is also stemming from a fairly detailed analysis from our end as to what is going on from the product and that is where the primary response coming from? Notwithstanding that, your observation is absolutely right, Levetiracetam is an extremely competitive API which is just the sheer size of this API. Levetiracetam approximately is 3,000 tons API globally and the bad part is that it is highly competitive, the good part is also that, there is enough market out there for strong players such as Neuland, Divi's and couple of others to gain market share as well. So, coming back in your point, there may be a decline in market shares due to either buildup of inventory, loss of market

share, but our strategy over the medium and long term is to continue growing with product where we have done for all of our products. So, whether you look at Sotolol, you will get Mirtazapine, you will get Ciprofloxacin, Levofloxacin, pretty much other APIs, if all consistently grown in volumes, then near that that we took a building in terms of market share and volumes, but we have taken up all, reassessed and done whatever it is up to gain back the market share. We will do the same for Levetiracetam, therefore I think your observation is absolutely right. We could see a temporary setback in this molecule, but we will continue to gain market share on the long run.

Saharsh Davuluri:

And to just add to what Sucheth said, I think it is a very dynamic market, right. It is not like we are waiting for the Levetiracetam business to unfold; we are getting qualified by new customers as well. So, some of these large formulation players, who are very strong traditionally in Levetiracetam finished dosage, they have also been adding Neuland as an API source over the last 3 months, 6 months, 12 months. So, it is a very dynamic market. So, it is not like, we have made our best and now we are waiting for the cards to open. I think we keep getting qualified with new customers and we keep working on the process as well and it is a very large market. No one I believe has more than 10% market share in the Levetiracetam business because it is 3000 tons API and even the largest players don't make more than 400-500 tons. So, I think it is a big market. It is just important to be connected to the customers, be constantly looking at your profits and be competitive and I think we do believe that we will bounce back, but we have to wait and see.

Aditya Khemka:

Coming to the CMS business right, so I see an expansion in the pipeline at least in the development projects and your commercialized molecules, can you divide your development projects into big pharma and small pharma in terms of your clients, what would be the split be? I know you can't give me an exact number, but some sense is it like 70% big or 70% small pharma, biotech etc.?

Saharsh Davuluri:

So, I think, we probably mentioned this in different contexts in our commentary earlier, but almost all of our business in CMS comes from small pharma companies or what we call as biotech companies so biopharmaceutical companies, so I think if we have to categorize our top 3 segments within CMS, it would be US based biotech companies, it would be European midsize innovator companies and then it would be Japanese innovator companies, which includes Japanese big pharma. So, there are very few projects in our portfolio which belong to big pharma. So, I think that should give you enough color on what our pipeline is, so most of the molecules we are referring to belong to biotech companies, these are NASDAQ listed, one billion, two billion dollar market cap companies with one or two products. That is the kind of portfolio of customers we work with.

Aditya Khemka:

And while your number of projects has gone up, has the number of clients also gone up over the past one year in the development and commercial side?

- Saharsh Davuluri:** Yes, we saw lull for the first half of the pandemic where we were not really able to add a lot of projects, but I think over the last 6 months, we have added some interesting products phase 2, phase 3 molecules from innovator companies. It has also been facilitated by their visits to our facilities and things like that. So, I think things are coming back into normal and in fact we are also spending more or at least investing more in business development now. So, we are adding more resources in business development, spending more on B2B marketing and things like that. So, I think we expect the pipeline to strengthen now. It has already started in the last 6 months, but I think it will continue.
- Aditya Khemka:** And last question on your unit III, so I heard pre-operating expenses were Rs. 225 crores, yet to be depreciated, is that what I heard?
- Deepak Gupta:** Yes, Aditya, that is right.
- Aditya Khemka:** So, Rs. 225 crores of pre-operating expenses, not fixed as it is to be depreciated?
- Deepak Gupta:** Not preoperative, this is the CAPEX spend, which we have done which is yet to be depreciated so WDV of the asset which are there in the unit III.
- Aditya Khemka:** And in terms of operating expenses, what would unit III be incurring annually right now?
- Deepak Gupta:** As of last year if I see, roughly around Rs. 60 crores of operating expenses from unit III.
- Aditya Khemka:** Rs. 60 crores, yes, so roughly 30% and then is unit III at its current utilization breaking even for you, standalone as a facility?
- Sucheth:** It will break even in the current year, not yet.
- Aditya Khemka:** So, you expect it to break even in FY23, is that what I heard?
- Saharsh Davuluri:** Yes, because everything that is being scaled up is getting scaled up in unit III.
- Aditya Khemka:** So, all your incremental volumes are essentially coming to the unit III? That is how it will break even.
- Moderator:** Thank you, the next question is from the line of B. Suresh from Burrans Financials. Please go ahead.
- B. Suresh:** Sir, CMS business this financial year, how much standalone, how much revenue is expected?
- Saharsh Davuluri:** So, Suresh we typically don't give any guidance on what we expect to do for the year.

- B. Suresh:** Standalone only CMS business?
- Saharsh Davuluri:** Yes, even for standalone CMS or for the overall business, we do not provide guidance on how much we expect to do.
- B. Suresh:** You can give your comment in quarterly results presentation. The line of the full year is when to reach targets. Last year sales is as expected, same sales will continue? It will give the good impression this financial?
- Saharsh Davuluri:** Yes, so what we said, Suresh is FY21 and FY22 we did not have growth, but in FY23 we expect to have growth, so we should expect growth in FY23.
- B. Suresh:** Full year 23 can be expected?
- Saharsh Davuluri:** Yes.
- B. Suresh:** Sir, profit margin any increased profit margin this year increased percentage of around 20%?
- Saharsh Davuluri:** Yes, again we will not give guidance on that, but I think the one comment we will make is that as you can see because of the improvement of the business mix, the gross margins are improving, despite raw material challenges our gross margins are improving. However, the EBITDA margins or the PBT has not improved in Q1 because the overall revenues have still not been at a critical threshold and what we believe is that if we are able to bring back the growth, which we do believe will happen in FY23, then the operating leverage should ensure that we will have much better profit margins than what we are currently seeing, both at an EBITDA level and as a PBT level because what operating expenses we have incurred in Q1, they are likely to be more or less similar for Q2, Q3, Q4, but if the revenues are going to grow, then the margins are likely to improve, so that is how I would explain it, but we will not be able to guide on what is the margin going to be.
- B. Suresh:** Sir, any future fundraising plans or acquisitions and this facility is enough for your future plans fundraising or any acquisitions or mergers, any plan of that?
- Sucheth:** No plan as of now, Suresh.
- B. Suresh:** This facility is enough for your growing business? This facility? Present facility?
- Saharsh Davuluri:** It will be adequate for the next couple of years. It also depends on what kind of growth we are going to achieve. If we are going to achieve growth that is going to be more faster than anticipated, then we may have to create more capacity, but unit III has a lot of capacity headroom for additional capacity creation, so we don't expect any challenges for the next 2 years at least.

- Moderator:** Thank you. The next question is from the line of Aditya Khemka from InCred PMS. Please go ahead.
- Aditya Khemka:** I had just one more question, the employee expense growth that I noticed sequentially, fourth quarter versus the first, an incremental Rs. 3 odd crores in expenses, so just wanted to understand, is this additional manpower or is it incremental bonus payout this quarter?
- Deepak Gupta:** So, actually it is a mix of both, so mostly coming from the performance that we have given to the employees and also we have added a few headcounts in this quarter, but those are very small in number actually, mainly coming from direct increase and little bit of headcount increase.
- Aditya Khemka:** Were they bonus payouts also this quarter?
- Deepak Gupta:** No, bonus payout we apportion over a 12 months period so irrespective of the payments we make our charge to the P&L on a monthly and a quarterly basis, so that won't impact the performance.
- Aditya Khemka:** So, this is going to be like the normalize run rate. There is no lumpiness in this expense therefore?
- Deepak Gupta:** Yes, correct.
- Moderator:** Thank you. We will take the next question as the last question from the line of Keval Ashar from DSP Investment Managers. Please go ahead.
- Keval Ashar:** So, just one question sir, how big is the size of opportunity for us in Bilastine?
- Saharsh Davuluri:** So, I think, we typically for the CMS molecules, Keval we don't, due to the contracts we have with our customers, we are not allowed to disclose the names or discuss the specifics of the molecule. So, we will not be able to comment on any molecule, its growth prospects or anything about it, specifically in the CMS side because of the confidentiality agreements we have with the customers.
- Moderator:** Thank you, I now hand the conference over to management for closing comments.
- Sajeev:** We would like to thank everyone for joining us on this call and for your interest in Neuland for the questions that you asked regarding our performance and also regarding the potential of our business. We thank you once again for your participation in today's call. Thank you.
- Moderator:** Thank you very much. On behalf of Neuland Laboratories, that concludes this conference. Thank you for joining us and you may now disconnect your lines.