"Ajanta Pharma Ltd Q2 FY '23 Earnings Conference Call"

November 03, 2022

MANAGEMENT: **MR. YOGESH AGRAWAL – MANAGING DIRECTOR – AJANTA PHARMA LIMITED**
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Moderator: Ladies and gentlemen, good day, and welcome to Ajanta Pharma Q2 FY '23 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 this conference call, please signal an operator by pressing star then zero on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Yogesh Agrawal, Managing Director of Ajanta Pharma Limited. Thank you and over to you, sir.

Yogesh Agrawal: Good evening, and welcome to all of you. With me, I have; Mr. Rajesh Agrawal, Joint Managing Director; Mr. Arvind Agrawal, our CFO; Mr. Rajeev Agarwal, Head of Finance and Investor Relations.

I'm really glad to inform you that the Board of Directors have approved an interim dividend of Rs. 7 per equity share, that is 350% of the face value of Rs. 2 each. I'm also truly delighted to share with you that Ajanta Pharma has been awarded the best managed companies for the year 2022 by Deloitte. This validates Ajanta's journey towards the excellence in product, people and various other things.

Coming to the results. They are already with you. And I'm happy to share with you that we have been able to achieve the continued growth in revenues. I will take you through the business-wise performance for the Q2 and H1 FY 2023, along with the comparison of the previous year same period.

Let's begin with the emerging market branded generic business. I'll first start with Asia. During the Q2, sale was Rs. 251 crores against Rs. 191 crores, posting a very healthy growth of 31%. In H1, sales was Rs. 492 crores against Rs. 357 crores, again posting a very healthy growth of 38%. The growth appears a bit elevated due to the low base of Q2 and H1 FY 2022.

Let's move to Africa. During the Q2, sales was Rs. 146 crores against Rs. 159 crores, posting a de-growth of 8%. And in H1, sales was Rs. 314 crores against Rs. 284 crores, posting 10% growth. The growth in this market was impacted due to the Rupee appreciation against Euro from the previous year, which has adversely impacted about 7%.

Branded Generic business of Asia and Africa contributed 43% to the total revenue during the H1. Our exports to these markets were Rs. 397 crores against Rs. 350 crores, posting a double-digit growth of 13% in Q2, and Rs. 805 crores against Rs. 641 crores, a growth of 26% in H1. We continue to post superior growth as compared to the market on the back of identifying opportunities and executing it clinically. We launched 16 new products during H1 in both the territories.

Let me now move to US generics business. US generic business contributed 19% to the total revenue. In – Q2, sale was Rs. 185 crores against Rs. 194 crores, posting de-growth of 5%. In H1, sales was Rs. 364 crores against Rs. 362 crores, posting 1% growth. Despite continued price erosion and absence of new product launches, we maintain the same level of the business as previous years. We continue to have 39 products on the shelf. In the first half of the year, we filed 3 ANDAs and also received one final and one tentative approval. At the end of September 2022, we had 21 ANDAs awaiting approval with US FDA. We are looking to file 10 to 12 ANDAs during the year.

Let me now move to Africa Institution Business. This contributed 3% to the total of revenue. In Q2, sale was Rs. 33 crores against Rs. 66 crores, posting 50% de-growth. In H1, sale was Rs. 110 crores against Rs. 120 crores, posting 8% de-growth. As we have been mentioning in our earlier call also, the institution business remains unpredictable and depending on the procurement agencies, funds and the requirement by the various donor countries.

With this, now I hand over to Mr. Rajesh Agrawal, Joint Managing Director, who will take you through India business. Thank you and over to you, Rajesh.

Rajesh Agrawal: Thank you. Good evening to all of you. Let me discuss some of the key highlights of India business with you now. India business contributed 32% in total revenue in first half FY 2023. In Q2 FY 2023, sales stood at Rs. 314 crores against Rs. 248 crores, posting a healthy growth of 27%. And in H1 FY 2023, sales stood at Rs. 593 crores against Rs. 477 crores, posting a healthy growth of 24%. This includes sales from the trade generics of Rs. 38 crores against Rs. 30 crores in Q2 and Rs. 71 crores against Rs. 57 crores in H1 of FY 2023. We have launched 15 new products in H1 FY '23 and three of them have been first to market.

Our performance has been satisfactory, which was on the back of new product launches, market share gain and price increase. As per IQVIA MAT September 2022, we have posted healthy growth in all the therapeutic segments and exceeded industry growth across countries. We have three of our brands appearing in top 500 in the IPM. As per IQVIA, we have improved 2 ranks and now ranked 27th in September 2022 from being 29th rank in March '22.

With this, I will now hand over to Arvind Agrawal, CFO, to take you through the financial performance. Thank you, and over to you, Arvindji.

Arvind Agrawal: Thank you very much. Good evening to all of you, and a warm welcome to this earnings call. For the ease of discussion, we'll look at the consolidated financials and provide year-on-year comparison. Let me take you through key financial highlights for H1 FY 2023. In Q2 FY 2023, total revenue stood at Rs. 938 crores against Rs. 885 crores, posting 6% growth. In H1, total revenue stood at Rs. 1,889 crores against Rs. 1,633 crores posting growth of 16%. The breakup of revenue has already been discussed by MD and JMD.

Q2 FY '23 saw material costs at 28% and H1 was at 29%. This is little higher compared to our estimates on account of continued higher level of raw and packing material costs, continued US price erosion, rupee appreciation against euro. And going forward, we estimate COGS to remain at around 27%.

In other expenses, we saw significant rise in the export freight cost. Pre-COVID, our freight costs have been around 6% to the sales, which got escalated to 9%, translating to Rs. 38 crores adverse impact for the H1 FY 2023. This external factor beyond our control and adversely impacted the profitability to that extent. Even in this particular quarter, there were some expenses which got preponed from the next quarter as well. R&D expenses were Rs. 59 crores against Rs. 49 crores for the quarter. And for the half year, it was Rs. 113 against Rs. 94 crores. R&D expenses stood at 6% of revenue, which will continue at this level.

EBITDA in Q2 was at Rs. 196 crores to Rs. 263 crores last year. For the H1, it was at Rs. 418 crores against Rs. 483 crores, 22% of the revenue. EBITDA was lower, mainly due to higher material and logistic costs as informed above. Going forward, we expect around 26% plus/minus 1% -. Other income stood at Rs. 73 crores in H1, mainly contributed by forex gain of Rs. 61 crores. Income tax stood at 23% for Q2 and 22% for H1. We expect it to be in the same level during FY 2023. PAT in Q2 was at Rs. 157 crores against Rs. 196 crores, 17% of revenue. And for H1, it was Rs. 331 crores against Rs. 370 crores, 18% of revenue.

We incurred capex of Rs. 63 crores in H1. Capex, including maintenance capex for the FY 2023 is estimated at Rs. 150 crores. We have improved in inventory holding period to 73 days from 88 days in March 2022, while receivables remained at same level of 115 days and payable at 76 days against 70 days in March 2022. With these highlights, I open the floor for the discussion and question and answer. Thank you.

Moderator: Thank you, very much. We will now begin the question-and-answer-session. Ladies and gentlemen, we will wait for a moment while the question queue assembles. The first question is from the line of Tushar Manudhane from Motilal Oswal Financial Services. Please go ahead.

Tushar Manudhane: Sir, just a clarification on the freight cost, particularly for 2Q, how much was the impact?

Arvind Agrawal: Almost about Rs. 24 crores.

Tushar Manudhane: So that is what quarter-on-quarter largely, explains the increase in other expenses?

Arvind Agrawal: Exactly. Plus also, as I mentioned earlier, there is also some preponement of expenses, which has happened in the quarter. So afterwards, in the next quarter it'll be little less.

Tushar Manudhane: If you could also share the mix of air shipments and air transport and other transport in terms of raw materials as well as MSD?

Arvind Agrawal: I don't have that number readily with me. But one thing which I can definitely say is that air transport is very less. And there the freight cost has softened to some extent. But sea-freight has not really softened. So that's where the impact is.

Tushar Manudhane: And just lastly on the ANDA filing, given that you have filed three, so that'd be kind of bunched up considering the target of 10 to 12 filing or this can get pushed to FY '24?

Arvind Agrawal: That is something which is very difficult to say now, but we are trying our level best to complete that 10 to 12 filings in this year itself.

Yogesh Agrawal: There will be some filing which will get skewed towards the end of the year. So our aim is to achieve that target.

Tushar Manudhane: And just lastly, any further development on generic Chantix?

Yogesh Agrawal: No, Chantix, I don't have any significant update to tell you. It is still work in progress.

Moderator: Thank you. The next question is from the line of Rashmi Sancheti from Dolat Capital. Please go ahead.

Rashmi Sancheti: So one question on Africa branded, as you mentioned that the growth was impacted due to the INR appreciation against euro, correct?

Yogesh Agrawal: That's right.

Rashmi Sancheti: What kind of growth have you seen in the business in the constant currency?

Yogesh Agrawal: For the current quarter in constant currency, it was flattish. So pretty much that 7% to 8% de-growth, which we have seen, that was purely on account of rupee appreciation against the euro.

Rashmi Sancheti: So how should we see this Africa branded business for the entire year and why there is a flattish growth in the market?

Yogesh Agrawal: Africa for the whole year, I think I would say that we should grow in the high single digit for the whole year. I think, as already shared with you if you add in the constant currency it could be higher because this 4% is also considering the rupee appreciation against the euro. So this the rupee appreciation is purely external factors beyond our control, which adversely impacted. Had that was not there, the growth could have been even higher.

Rashmi Sancheti: So high single digit growth you're talking in the INR terms, right?

Yogesh Agrawal: Yes, INR terms for the whole year.

Rashmi Sancheti: And in terms of Asia, we are continuously seeing the extraordinary growth from last quarter. So how should we see in the second half this kind of growth would continue and therefore for FY '23 the growth would be much higher, that is the guidance of mid-teens growth and even for India if you can guide?

Yogesh Agrawal: So I think really Asia has been very well for us this year. And as we have seen last quarter also, we did pretty nice. This quarter also the performance was quite good, very encouraging. So for the whole year, we are looking to post a growth of 20% and above for Asia.

Rashmi Sancheti: And India sir?

Rajesh Agrawal: For India, given that we have had two very strong quarters. We are now confident of posting high-teens, as against the mid-teens what earlier guidance we had given, so we are quite confident of going for high-teens growth.

Rashmi Sancheti: And finally, on the expenses, if you could give like what is the price erosion currently in the US market, any particular guidance which you can give that this year US would be majorly in the declining phase or it would remain flattish or probably we will have some good launches in the second half? If you can guide on that? And on the expenses side, we are seeing that the raw material cost has come up sequentially, so quarter-on-quarter any softening of the KSM prices or anything which you have noticed? And even on the freight cost after September, how are you seeing the trend, whether it is coming down, or is it still high and it is going to keep on impacting even in the H2? And your overall EBITDA margin guidance for the year?

Yogesh Agrawal: So first you said about the US business. US business, we are looking at one or maximum two launches during the year, whatever approval we've got. Based on that, we are looking at a full-year to be high single-digit growth, which we'll be able to post in the US. Despite, I think the CFO will take on the COGS and PAT. But even though we are going to post high single-digit growth for the US, because of the price erosion, the margins have shrunk, that has already impacted, in fact already you have seen in the Q1, Q2 in the COGS as well as in the EBITDA.

Second, on the freight front, some freight, so they have softened, but that was purely for the regular containers for some markets and when you add other costs of those freights which are there. So overall, when you add some of the products which we said they're in the reefer container. So they have not softened so significantly. So we've seen some softening of the freight of around 5% to 7%. Let's hope that this continues and it further soften. So that's on the freight. I think on the expenses and the EBITDA, CFO will tell you.

Arvind Agrawal: Yes. So in terms of the COG which you were talking about, it has softened from Q1 to Q2. In Q1, you know that there was an impact of some inventory write-off which was there. So practically, we are almost at the same level currently, but going forward, we are expecting some benefit certainly in the material cost in COG, because of softening as also the business mix. The product mix will change to some extent positively because of which we should get some benefit there.

In terms of other expenses, as I mentioned earlier also that some expenses got preponed. So certainly, some expenses will be a little lower as compared to what we have incurred in this year. Overall, as I mentioned in that the EBITDA guidance which we are talking about is about 26%, plus/minus 1%. So that is the estimate which we had for the EBITDA guidance for the whole year.

Moderator: Thank you. The next question is from the line of Kunal Randeria from Nuvama Institutional Equity. Please go ahead.

Kunal Randeria: Yogeshji, if I look at the data on the FDA, around 65 to 70 ANDAs are being approved on a monthly basis. But since you haven't got any approval and this monthly approval rate from the FDA is almost at pre-COVID level. So just wondering what exactly the reason for not getting those approvals?

Yogesh Agrawal: Yes, good question. A lot of ANDAs we had filed from our Dahej facility. And for a number of ANDAs, I think 4 to 5 ANDAs, FDA told us that the review processes is at advanced stage, but they had put that on hold as the facility inspection was a requirement for approving these ANDAs. Dahej has undergone the USFDA inspection last few months back. We had two 483-observations which were of routine nature, which we have responded. We believe the EIR should follow in the normal course of a few months. So that clearly paves a way for the approval from all the ANDAs which we have filed from Dahej. And after the EIR is received, we are expecting flurry of approvals that should come through. So that was -- to answer your question, the holdup was primarily FDA's requirement for the inspection of our Dahej facility. Now since that is behind us, we are expecting approvals to come through.

Kunal Randeria: Second question is on the India business. In the last three quarters or four quarters, you have demonstrated industry leading growth. So I understand your guidance and all. I just want to understand what's the reason that you have been so consistent in India?

Rajesh Agrawal: Primarily, if you look at the segment-wise growth, Dermatology has been doing exceptionally well for us. That is contributing to the growth percentages. We are growing multifold compared to the industry growth rate. Pain Management also we are growing robustly, so that also is adding to the growth. And so it is in cardiovascular.

Kunal Randeria: Sorry to cut you off, sir, but actually I s aw the data in the press release. I just want to understand the reason. Have you taken higher than average price increase or there is substantially new products are contributing a lot more? What exactly is driving this growth?

Rajesh Agrawal: Price increases are as expected or maybe as guided by NLEM, and also as per the NPPA guidelines, correct. So our price increases maybe slightly more than the industry. And the volume growth is what is driving our growth. So industry has de-grown in volume by minus 1%, whereas we have grown by 4% in volume, so which is the best thing to happen, which shows the inherent strength of the brands that we have built. Does that answer your question?

Kunal Randeria: Yes. I mean just for sure, you have grown -- volume was 4% and lets assume price growth would be 6%, 7%. Then the remaining 6%, 7% would be coming from new products?

Rajesh Agrawal: Yes. New products also, yes. New products is at par with the industry, which is contributing around 2% to 3% for us.

Kunal Randeria: Yes. Arvindji, if I heard you correctly, you mentioned that the freight cost is around 9% of revenues. Is that correct?

Arvind Agrawal: Yes, you are right. For the export.

Kunal Randeria: I mean 9% of the export revenues.

Arvind Agrawal: Yes.

Kunal Randeria: Okay. So what will it be for the total revenue?

Arvind Agrawal: This is for the export revenue and the export revenue earlier it used to be 6%. Now it is 9%, so almost about 3% increase on the export revenue.

Kunal Randeria: But sir, the reason I'm asking this is because on a year-on-year basis, while I understand that exports would have gone up, some trade elements would have come down, right, like container cost or something. So why such a sharp increase? I'm not being able to completely understand. Or is it because your air shipments are substantially higher up, so not able to completely understand.

Yogesh Agrawal: No, Kunal, it is primarily because of the global factor, which is affecting not only Ajanta, everyone. The container costs have gone 3-x to 4-x, the sea cost, sea shipment costs. So we've seen for the US as I have 4-x of what used to be at the pre-COVID level. So now that has started to soften a little. So that's why from everything, Arvindji has said, from 6% pretty much 50% price has happened from 6% to 9% it went up. So primarily external factors which hopefully it pass-through, softens and comes down. There is no element of the air going up or anything like that. Those kind of components are I think in line with what were in the past as well.

Moderator: Thank you. The next question is from the line of Priya Harwani from Perpetuity Ventures. Please go ahead.

Priya Harwani: I just wanted the clarification on the capex number you mentioned for this quarter as well as the guidance for full year?

Arvind Agrawal: Yes. For the first half, it is Rs. 63 crores. And for the whole year, we are talking around Rs. 150 crores.

Moderator: Thank you. The next question is from the line of up to Abdulkader Puranwala from Elara Capital. Please go ahead.

Abdulkader Puranwala: Sir, just one clarification on the EBITDA guidance. So this guidance of plus/minus 1%, 26% is for the second half or for the full year of FY '23?

Arvind Agrawal: Second half.

Abdulkader Puranwala: And sir, on a sequential basis, if I see your other expenses, so there has been a rise of almost like Rs. 25 crores, out of which Rs. 10 crores as explained would be the freight cost. So would it be fair to assume that the balance Rs. 15 crores, a large part of it would be the preponement of expenses?

Arvind Agrawal: To some extent, you can say about Rs. 10 crores, you can say. Almost 1%.

Abdulkader Puranwala: And sir, just one final one on this INR appreciation against the euro, which impacted your Africa sales. Would there be some amount of forex loss as well which will be sitting in your P&L for Q2?

Arvind Agrawal: Yes, about Rs. 6 crores is there in the P&L, which is there in other expenses also.

Moderator: Thank you. The next question is from the line of Bino Pathiparampil from InCred Capital. Please go ahead.

Bino Pathiparampil: One follow-up on Chantix. So if I remember correctly earlier, you had said that there were some FDA queries which you were in the process of responding. So have you responded? And if not when do you plan to respond?

Yogesh Agrawal: We have responded. So it is a work in process from FDA. So based on that, they have also some additional data. So we are in the process of furnishing that with the FDA.

Moderator: Thank you. The next question is from the line of Nikhil Mathur from HDFC Mutual Fund. Please go ahead.

Nikhil Mathur: Sir, my questions are more on the margin side. If I look at the next quarter, your India-plus branded Asia sales is almost 60% of total revenues. And then we have clocked in a gross margin of around 72%. If I look at pre-COVID, let's take FY '20. When the mix of these two markets combined, was more 54%, 55%, the company was doing almost 75% gross margin. So can it be safe to assume that this entire 3 percentage points hit or the RM hit is more than 3 percentage points because the mix has improved, but your gross margin has come down to 3 percentage points. So the RM hit could be around 4%, 4.5 percentage points? Can that be the right way of looking at the RM hit?

Arvind Agrawal: I think what we need to understand is multiple factors. See, one is the cost has gone up. Now that is something which is across. So even for the Global inflation for the raw materials. So everywhere it has increased, and this is something which is normal. Apart from that, certainly, the product mix also has got some impact on that. As the product mix will improve, I think that should give us…

Yogesh Agrawal: So I think as CFO said, there are three components. One is the raw material price is going up on account of global inflation. Second is the euro adversely impacting that has further increased. And third is the price erosion. So all three impacted our COGS, which is what is reflecting here. So all these things -- what is important to see is that the health of the business is that are our brands growing, are we increasing our market share? These are the factors which are going to be there. Now they soften up and they will improve. So I think the overall approach is that we are able to gain the market share, we're able to grow the brands. That's, I think, the key health indicator of the organization.

Nikhil Mathur: I'm not fully clear, but if I may just try to understand it better. Are you also trying to imply that while the raw material costs across business segments, perhaps the margin setback in India were also in branded Asia, they are also under pressure and because you are in pursuit of growth both in India and branded Asia, we might not go back to historical high gross margins, whatever they were. Obviously, we don't have exact numbers there, but qualitatively, we are at a margin level, which is much lower than what it was pre-COVID and as you say more growth in the next two years, three years, the margin reversion in those markets might not happen to that extent?

Arvind Agrawal: I think to some extent, like what we said, the inflation, the global inflation, which is there in the RM/PM cost, that is going to be there. So that is something definitely will be there. But we are talking about 26% as the right COG which should be there for the going forward. That is what we are expecting, H2.

Nikhil Mathur: And sir, in India, in terms of growth in '23, '24, '25, what are your expectations from new product launches? I mean I believe Ajanta in the last few years has been higher than industry average of 2%, 2.5 percentage points, I think more in the range of 3.5% to 4%. Is that budget for next two years, three years as well from new products in terms of growth?

Rajesh Agrawal: Our expectation would be in line with the industry growth from the new products. So our contribution also, even if you look at the first half is at par with the industry, which is 2% growth. And I expect that to be the same going forward.

Nikhil Mathur: Another question on the logistics side, again, sorry to harp on that. I'm having multiple questions on that. I'm just trying to understand, when we look at various data points, including the Baltic Index and whatever we hear from some certain other industries experts and companies as well. There seems to be a pretty sharp softening of logistics cost. Actually, the spot prices have gone down. So is it that your contracts on the logistics side are more -- you would have entered in the more near term, that's why your pricing on the logistics front is higher than the spot, and that's why a bit more benign the margin commentary from your end for second half? Or would that be right way of why there's a bit of disconnect between your guidance and what the prices are looking like?

Yogesh Agrawal: To summarize your question, you are saying that freight cost, what is there in the press or otherwise has gone down, we have not gone down correspondingly. Is that your question?

Nikhil Mathur: Yes,

Yogesh Agrawal: Yes. So there are two things. One is that the freight cost, let's say, for example, for the US, it has gone down for the regular containers which are not cold-chain. But we export our products into the cold-chain containers. So for that, the prices have not gone down to that extent. We are seeing 7% to 8% price reduction in the reefer container. Whereas for the regular containers, the price drop has been quite significant. So this is common to all, any company who wants to export the product in the reefer container, they are seeing this kind of price reduction. And non-reefer containers, the price reduction has been slightly better.

Other markets, the price has reduced, but not to the level, pre-COVID level. So there are some fluctuations which is happening. We'll see how it stabilizes in the coming next half of the year. Does that answer your questions.

Nikhil Mathur: Yes, sir. And then one final question on the US market. The commentary from various industry experts has been pretty guarded for some quarters now, including yours as well, I think last couple of quarters, if I remember correctly, you have also been sounded a bit cautious in the US market. Any evidence that changes that outlook for the market or it continues to be as same as it was last quarter or few quarters back as well?

Yogesh Agrawal: Yes. So nothing changes. It remains same what we've been talking for the last few quarters. We continue to be cautious and trade very carefully and navigate the challenges as they come. So there is nothing further to have than what others have guided in the industry as well.

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

Kushal Chovatia: Yes, so the domestic business has been doing quite nicely in the past few quarter. So I have just one question with regards to that. So what has been the contribution of the institutional business of the whole domestic segment?

Rajesh Agrawal: For the first half, it is about Rs. 70-odd crores, yes, Rs. 73 crores. Rs. 71 crores to be precise.

Kushal Chovatia: INR 71 crores. What's the contribution in FY '22?

Rajesh Agrawal: FY '22 was Rs. 100 crores, Rs. 99 crores to be precise.

Moderator: Thank you. The next question is from the line of Harsh Beria, Professional Investor. Please go ahead.

Harsh Beria: Congrats on the great set of execution and the branded business in India and Asia. My question is about one of the recent product approvals, which is Vivomo. I think Ajanta got it a month back or something. When you plan to launch this product? And how is the market currently in this product in the US?

Yogesh Agrawal: We are gearing up for the launch. Maybe it will get pushed out to the Q4. The product has declined significantly from what it used to be when we had filed the ANDA. So let us see. We will try to do our best to garner whatever market share we can. So it will be launched in Q4.

Harsh Beria: One question I have about your trade generic business in India. What was the sales in this quarter?

Rajesh Agrawal: This quarter Rs. 38 crores.

Harsh Beria: And what was this number in the last quarter or in Q2 FY '22?

Rajesh Agrawal: Q2 FY '22, Rs. 30 crores.

Arvind Agrawal: So from Rs. 30 crores, it has gone to Rs. 38 crores. And for first half, from Rs. 57 crores, it has gone up to Rs. 71 crores.

Harsh Beria: So one thing which is very clear in the trade generic number is Ajanta is doing quite well now. I think this year you will end up with close to Rs. 140 crores, Rs. 150 crores. Can you throw some more light on this business?

Rajesh Agrawal: So we are operating just the way as industry operates. Yes, we are doing exceptionally well. And it is primarily a pharmacy or a chemist push business. It's all branded generics. And so that's how we've been operating and our team has been very-very active in identifying new product opportunities and also exploring markets which are untapped by some of the other competitors, which is giving us the growth.

Harsh Beria: And once we have some kind of a pull for a given product, do we also plan to migrate it towards branded generics, so migrating products which already are showing traction in the trade generics to branded generics?

Rajesh Agrawal: So usually, I have not seen that from trade generic brand would come into prescription generic, branded generic as such. So we don't intend to do that. But you are right, if there is some kind of pull that gets created in some kind of market that created especially for any chronic nature of product, then there is an auto demand that happens. So it's better for the organization as such, because the influence or the control of the chemist reduces to that extent for that brand.

Harsh Beria: One last question is on the US price erosion. What was the price erosion in our base portfolio for this quarter?

Yogesh Agrawal: We have seen double-digit price erosion.

Harsh Beria: This would be early double digits or mid-double-digit?

Yogesh Agrawal: Mid-double-digit.

Moderator: Thank you. The next question is from the line of Alisha Mahawla from Envision Capital. Please go ahead.

Alisha Mahawla: A couple of clarifications. One, the EBITDA margin guidance has been given for H2 of 26%. Is this including other income?

Arvind Agrawal: No. The EBITDA margin doesn't contain other income. It is excluding other income.

Alisha Mahawla: And in the US market earlier, we were talking about 4 to 5 launches in the current year. And now we're talking about one or two launches. The reason for relatively lower launches in all the anticipated?

Yogesh Agrawal: So as I had explained earlier, that is purely related to the approval of the ANDAs and the ANDA approval got linked to the facility inspection. Now since the Dahej facility inspection has occurred with very routine type of two 483-observations, we are expecting the EIR to come in next few months. And after that, this will pave the way for the approval of the ANDA products. And as we get approved, then we will bring into the market. It was purely approval regulatory process. So we are just awaiting that to be completed.

Alisha Mahawla: And you mentioned that margins in this quarter were impacted because of higher freight cost and expenses preponement. What is cost preponement? What could this be pertaining to?

Arvind Agrawal: Some of the product registration, R&D and also some of the promotional expenses.

Moderator: Thank you. The next question is from the line of Nitin Gosar from BOI Mutual Fund. Please go ahead.

Nitin Gosar: Two questions. I wanted to understand the stand on US generics business, keeping in mind that we're constantly seeing price erosion, especially for the portfolio that you carry, the price erosion has been pretty harsh. The incremental investment that we are doing for R&D, how are we trying to secure the future growth prospect and the profitability pool in US generics?

Yogesh Agrawal: So we are very careful in the product selection, and we are putting a lot of filter to identify and see the products which we try to do the modeling and forecast and see that what kind of competition it will have and what kind of margins we will be able to get. So earlier, the aspiration was to find a much higher products, but then we have curtailed the ambition, and we've brought a number of products to make sure that we do our best in product selection. And I think we are trying our best to see how we can maintain and increase our market share in the market ahead in the frontend.

Nitin Gosar: And should you keep in mind that until we don't see new launches, this trajectory of price erosion or the profit pool of US generics will continue to remain muted?

Yogesh Agrawal: So I think without the new launches, the current Q2 numbers which we have seen, we expect that to remain. Maybe there will be minor variations here and there depending on the quarter performance. But this is the base which we believe is there. And based on that, and new product approvals that we should be able to add on this base going forward.

Nitin Gosar: And could you comment on the US share, profit pool, how are we in terms of breakeven post R&D?

Yogesh Agrawal: We do not give the numbers territory wise. So I think I have some limitation in sharing that kind of information.

Nitin Gosar: Yes. I understand, but if you could acknowledge whether we are breaking even post R&D?

Yogesh Agrawal: I'm sorry, I'll not be able to comment much.

Nitin Gosar: No issues. One last bit on Africa business. I've been trying to understand here, in the past we have tried not to aggressively hedge ourselves on currency part. But this time, it has not worked in our favor. Going forward, how are we approaching the currency hedging part? And the kind of currency volatility that we have seen, does it push us to look for price increases in both territory to compensate for the margin erosion that we see?

Yogesh Agrawal: So we are not looking at the price erosion, price increases there. There are some limitations. They are regulated and controlled, the price approval. And it's difficult to get a price increase there. So more or less, the best we can do is hedge the currency, which we are doing. And rest, I think we have to just see once this Russia-Ukraine war settles and hopefully then that kind of the euro bounces back probably. I think that is a factor which is beyond our control.

Moderator: Thank you. The next question is from the line of Tushar Manudhane from Motilal Oswal Financial Services. Please go ahead.

Tushar Manudhane: Just on Asia business, first half has been phenomenal. And compared to that, we are still guiding for a lower number for a full year of FY '23. And given that second half FY '22, any which case was soft. So any particular comment on this?

Arvind Agrawal: I think if you remember, Asia business, last year, mainly Q4 was the highest. So because of that, I think that will not be sustainable. So to that extent, I think we are expecting that to get corrected, and because of which the overall guidance is about 20% plus.

Tushar Manudhane: And any forex gain in other income, other profit?

Arvind Agrawal: Pardon me?

Tushar Manudhane: Other income has been higher at about Rs. 40 crores. So any forex gain?

Arvind Agrawal: Yes. I think maximum is forex gain only. As I mentioned in my talk, I think it was Rs. 63 crores for the whole half year is forex gain. And that is what is basically the hedging which we have done, that has benefited. So it has not gone in the topline, but it has come into the other income.

Tushar Manudhane: How much was it in Q2 in particular?

Arvind Agrawal: INR 39 crores is Q2, out of Rs. 63 crores.

Moderator: Thank you. The next question is from the line of Naushad C from Aditya Birla Sunlife AMC. Please go ahead.

Naushad C: A couple of clarifications, firstly on the free cash flow. Sir, if I look at the next couple of years, two-three years, we are generating very strong free cash flow, like we have a decent cash on the balance sheet as well. So how are we planning to utilize this? Any thought on the acquisition please?

Arvind Agrawal: As far as acquisition is concerned, I think we are continuously looking for it. But unfortunately, we have still not got a suitable candidate for the acquisition. But we keep on looking for it. We are open for acquisition every time and we are looking at every opportunity which is coming to the market, certainly. Only thing is that unless it happens, you really don't know. So as far as free cash flows are concerned, you have seen in the past two years, so the Board has to decide how they want to deal with it, but we have been repaying to the shareholders consistently. Like last year, we have given almost about Rs. 450 crores back to the shareholders.

Naushad C: Secondly, in terms of percentage of billing in dollar terms, would you be able to share what percentage of revenue billing we do in terms of dollars?

Arvind Agrawal: Majority is dollar. Only one small portion is in euro. Africa is euro, and else everything is in dollars.

Naushad C: And lastly, just again, I'm touching on the margin side. Just a clarification, sir, based on your guidance, if I see your revenue mix towards India and emerging markets has improved and it will improve going forward as well, but your margin guidance has been flat. So the reason of this could be to either your US business is eating a lot of cash or the profitability of the India and emerging market has gone down versus past. So what could be the specific reason, sir?

Yogesh Agrawal: As we have mentioned, it's a combination of all the three things. We have mentioned that the US aggressive price erosion has adversely impacted our costs and correspondingly EBITDA. The second was the appreciation of rupee against euro. So that has also impacted our Africa part, and that also got baked in into the COGS. So, and the third was the price increase, which we have seen across all the raw materials, COVID situation, so that was third. And the fourth is the expense of freight going up. So these are the four big buckets, which is not unique to Ajanta. That is, I think, impacting any and every pharma companies that is there. So this is a combination of cost as we were getting a little bit the reduction in the COGS and impacted the EBITDA as well.

Naushad C: So if we leave the US business aside, once thing improve in terms of your logistics and raw material side, should we assume that the profitability of the India and emerging market should come back to the normalized level, or there is no structural changes in terms of the margin or profile of those businesses?

Arvind Agrawal: Honestly, there is no structural changes. Absolutely no structural changes. We are still talking about 26% purely for the H2, which is quite good according to me. If you remove the US, definitely it will be at the same level what it used to be earlier.

Moderator: Thank you. The next question is from the line of Bezad Deboo from Systamatix. Please go ahead.

Bezad Deboo: I just want to clarify on the EBITDA margin. So earlier you had guided somewhere around 25% to 27% for the full year, and now we are expecting around that for second half?

Arvind Agrawal: Yes.

Bezad Deboo: So for FY '23, you would be lowering our FY '23 guidance, right, a few basis points?

Arvind Agrawal: You are right.

Moderator: Thank you. The next question is from the line of Suresh Agrawal, Individual Investor. Please go ahead.

Suresh Agrawal: What is our plant utilization, like capacity utilization at present?

Arvind Agrawal: We should be around 60-65%.

Suresh Agrawal: And if you are planning to go to other geographies for utilization of this plant to 100%?

Yogesh Agrawal: We have sufficient capacities to take care of our growth requirement

Suresh Agrawal: If you are planning to go to other geographies, like which you have not already entered actually.

Yogesh Agrawal: There are a few countries which are work in progress, but there's nothing significant which will happen. I think our focus is to remain in the existing market and grow them, expand them more. So I think that is where the focus is.

Moderator: Thank you. The next question is from the line of Mitesh Shah from Nirmal Bang. Please go ahead.

Mitesh Shah: I just have a question on your branded market, emerging markets. So are you adding the MRs over there, so that is already added? Or you are still adding over there?

Arvind Agrawal: We have already added quite a bit, and there will be small additions, which may happen in the second half also.

Mitesh Shah: So the advantage of the improvement in the MR productivity will be coming from the next year only, right?

Arvind Agrawal: Oh, yes, positively.

Mitesh Shah: So I think from next year onwards, what would be the drivers for the margin improvement? Because this year definitely it's a blip because of the trade charges, raw material cost and everything. What could be the drivers? And how much you can expect the margins from next year onwards? If like historical 30% plus margin can we achieve in next two years?

Yogesh Agrawal: I think it's very uncertain. What we are looking at is that the H2, the COGS should be around 26%, and the EBITDA margin we have guided as 26%, plus/minus 1%. Any improvement from here onwards on various parameters which we have said will further improvise only. If the freight comes down, it will get added into the margin. Raw material prices, soften that will get added into our margins. So these are the factors which are beyond the control and I think we have to negotiate those challenges as they come. But again, yes, that's the answer I think to your question.

Mitesh Shah: So whatever in your control, like operational leverage and the kind of other mix change would be expected to be 100-150 basis margins would it be possible?

Yogesh Agrawal: Possibility is always there. As you said, it is the productivity we are trying to expand from the existing people. So to that extent, correspondingly the sales will go up, but the expenses will not go up to that extent because people are not getting added. So of course, all those possibilities are there where the margins can be expanded for various efficiencies.

Mitesh Shah: In the emerging branded market, also you have increased marketing spend as well, right, this year, or you will be in -- so that also will be coming down in next year, right? That will be the possibility for the improvement in margin?

Yogesh Agrawal: Yes, that is there. And as you said, the effect of this expansion and the people, addition of the field, will start to -- we'll be seeing from the next year onwards. So a combination of both, hopefully, we should be able to be in a better situation.

Mitesh Shah: And the R&D cost would be at around 6%, right?

Yogesh Agrawal: Yes, exactly. That's right.

Moderator: Thank you. The next question is from the line of Madhav Varda from Fidelity International. Please go ahead.

Madhav Varda: I just wanted to understand, on the US business, are we seeing like, Ajanta or competitors beginning to withdraw products in the market because of profitability being so weak?

Yogesh Agrawal: Yes, we've seen some players talking about exiting some products which are very hyper competitive. So, but that has been the case in the past also. If there are eight players, if two players get dropped off, it really doesn't shake up the market so much either ways, positively or negatively.

Madhav Varda: So US business, is competition going to remain this high, structurally how do we see the profit profile of this part of the market improving, like next two years, three years, if competition is here to stay and many people have their capacity to supply. Is there any thought process that we have in terms of how profits improve here, not just for us but for the industry as whole?

Yogesh Agrawal: No, we have to negotiate the challenges as we get there. The thing is that it got -- the whole thing, I think, precipitated because of the two factors. One is the price erosion was significantly higher than historical levels. And second, there was no new approvals. Otherwise, what happens is that 8% to 10% price erosion is there and you're launching the new products. And from there, you are able to drive 20%, 30% growth. So net-net, you come out positive of 20%, 15%, 20%. So combination, as you can say, it's a perfect storm which happened last year. Both happened, and that is why we see a very-very significant adversely impacted business for the US market for all the companies.

Now as the base gets reset to the margins for the new prices which we have seen, and as the new product approval comes through, that should be able to, I think, tackle the current situation and we should be able to grow on that business and expand the margin there.

Moderator: Thank you. Participants, if you have any further questions, we would request you to please e-mail your questions. Due to time constraint, I would now like to hand the conference over to Mr. Yogesh Agrawal for closing comments.

Yogesh Agrawal: Thank you, everyone, for joining today. And if there are any other questions which got less answered, please feel free to e-mail to investor relations. Thank you.

Moderator: Thank you. On behalf of Ajanta Pharma, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.