Aurobindo Pharma Limited

Q2 FY15 Earnings Conference Call

November 7, 2014

MANAGEMENT

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MR. ROBERT CUNARD – CEO, AUROBINDO USA
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Moderator: Ladies and Gentlemen, Good Day, and Welcome to the Aurobindo Pharma Earnings Conference Call to Discuss Unaudited Numbers for the Second Quarter-ended September 30th 2014. 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, please signal an operator by pressing '*' then '0' on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. T Roy Choudhury. Thank you. And over to you Sir.

T. Roychoudhury: Hello and Welcome everyone to Aurobindo Pharma's Earnings Call to discuss the unaudited results for the Second Quarter ended 30th September 2014. We released our Q2FY15 Results yesterday, 6th November, and the same is available on our website for your reference.

I am Roy, handling the Investor Relations of Aurobindo Pharma. With me we have today the senior management of the company represented by Mr. N. Govindarajan – Managing Director; Mr. Arvind Vasudeva – CEO; Mr. Robert Cunard – CEO, Aurobindo USA; Mr. Ronald Quadrel – President AuroMedics Pharma, USA; and Mr. Santhanam Subramanian – CFO.

We will begin this call with the opening remarks from the company's management followed by an interactive Q&A session. Please note that some of the matters we will discuss today are forward-looking including and without limitations, statements relating to the implementation of strategic initiatives and other affirmations on our future business development and commercial performance. While these forward-looking statements exemplify our judgment and future expectations concerning the development of our business, a number of risks, uncertainties, and other important factors may cause actual developments and results to differ materially from our expectations. Aurobindo Pharma undertakes no obligation to publicly revise any forward-looking statement to reflect future events or circumstances. We expect the call to last about an hour. And with that let me please turn the call over to Mr. Govindarajan for his opening remarks.

N. Govindarajan: Thank you, Roy. We are here to discuss the unaudited numbers for second quarter of fiscal 2014-15 along with the corresponding periods of previous year. As far as our revenues are concerned, our consolidated net operating income in Q2FY15 grew by 50% to Rs. 2881 Crores over Q2FY14.

Gross sales from Formulations has been Rs 2236 Crores, recording a growth of 82% over Q2FY14. The US Formulations sales continued on a strong momentum growing by 61% against corresponding quarter last year, which was at Rs 1174 Crores. Cephalosporin represented $12mm of Net Sales for the quarter in line with our expectation.

In Aurolife, the manufacturing arm of Aurobindo USA the growth is more skewed towards Controlled substance and Non Institutional business.

AuroMedics, the company marketing injectable products in USA continued to outperform and generated $17million revenues in Q2FY15 growing by 119% of corresponding quarter last fiscal and 15% sequentially over previous quarter.

In terms of our US filings, we have 378 ANDAs filed as at September 2014 of which 2 ANDAs were filed during the quarter. We have received 171 final approvals, 26 tentative approvals and the balance 181 ANDAs are under review. The unit wise filing and approvals are as follows… From Unit-3 – 119 filed, 114 approved; Unit-7—134 filed, 36 approved; Auro-life- 26 filed, 9 approved; Unit-4 – 66 filed, 8 approved; Unit-12 – 20 filed, all of which are approved; Unit-6—11 filed and 10 approved and AuroNext – 2 product has been filed so far. Units 3, 7 and Aurolife manufactures oral non-betalactum products, Unit 4 manufactures general injectables and ophthalmic products, Unit 6 and 12 manufactures cephalosporin and SSP products respectively and AuroNext which has its facility at Bhiwadi in Rajasthan manufactures penem injectable products.

Europe recorded sales of Rs. 766 crores in Q2FY15 thereby growing more than four-fold over corresponding period of last year's sales of Rs 171 crores. This has been more on account of our recent acquisition of the western European commercial operations of Actavis to help enhance our European presence. The revenue and profit numbers of our integrated European operations has been in line with our expectations for the year.

The RoW formulations sales grew by 70% to Rs. 156 crores in Q2FY15 over Rs 94 crores in Q2FY14, the focus markets being South Africa, Canada and Brazil contributing to the revenues. There has been a decline in ARV formulations sales by 40% to Rs 139 crores during the quarter but we have recently started executing some notable tenders, which will help grow this segment for the year as well.

In terms of segmental classification, US formulations contributed 52% to the overall formulations revenue in Q2FY15 against 60% last year, the share of Europe increased to 34% from 14% in the corresponding period last year amplifying our focus on that market. Share of RoW remained the same at 7% while ARV declined to 7% against 19% in the first quarters of FY15 against FY14.

Gross sales from API have been Rs.685 crores in Q2FY15, which is lower by 5% over Q2FY14. The additional sales which had happened in API were more towards internal consumption in line with the exponential growth in the formulations business. We are expanding the capacity across various units. While certain capacity would kick in by the beginning of next financial year, the major capacity at Vizag would be commissioned by Second quarter of next financial year.

Our EBITDA for the quarter is Rs. 637 crores which is 22.1% of net operating income and has gone up by 45% over Q2FY14. The EBITDA as a percentage of Net Operating income is appearing marginally lower on account of European acquisition. Also mainly due to this acquisition staff cost to net operating income increased by 1.5% and other expenses by 3.4%.However, improved business mix translated into decrease in materials consumptions to net operating income by 4.1%, which helped offset such cost escalations and sustain the profitability in the business.

As far as ForEx is concerned, the closing Rupee Vs. US Dollar rate was 61.75 in September 2014 and 60.175 in June 2014. The Rupee depreciated by 2% and accordingly resulted in a net consolidated ForEx loss of Rs 42 Crores during the quarter as against a loss of Rs 68 Crores in Q2 last year and included loss on account of exchange difference arising from restatement of foreign currency borrowing to the tune of Rs 67 crores

The company's capex including maintenance CapEx is expected to be a range of Rs 600 Crores for FY 2014-15, which will be spread out across APIs and Formulations. The company's operations have resulted in substantial improvement to support the capex through internal cash generation.

The majority of the company's debt is denominated in foreign currency. The net debt is USD 447 million as on September 2014 as compared to net debt of USD 532 million on March 2014. The cash and bank balance is about USD 83 million. The company has reduced USD 85 Million of debt during the first half of FY15 and it we may bring down the debt down further by USD 25 - 40million in the second half of the year. Growing Export revenue offers hedge against repayment of Foreign Currency Term Loans, which is payable over 4 to 5 years.

So this is all from our end and we will be happy to take your questions now.

Moderator: Thank you very much, sir. Ladies and Gentlemen, we will now begin the question-and-answer session. Anyone who wishes to ask a question, may press '*' and '1' on their touchtone telephone. If you wish to remove yourself from the question queue, you may press '*' and '2'. Participants are also requested to use only handsets while asking a question. Our first question is from Prakash Agarwal of CIMB. Please go ahead.

Prakash Agarwal: The first question is on the US business, clearly on the QoQ front, a very good set of numbers, given that Cymbalta will be a small component, so base business has really improved. So any thoughts there, that despite some channel consolidation issues which we have been hearing from the peer group and lower product launches for us, we have done well, so has the volume growth happened, or what really has happened and led to that growth?

Robert G. Cunard: Prakash, this is Bob. As you indicated and as we talked about in the past, we have experienced channel consolidation on the customer side here in the US and we are certainly aware of what the world may look like after Duloxetine and it has been very good for us. We have seen a slowing in approvals from the FDA and we really did not have any significant new approvals within the quarter, but our base business is growing as well as some of the full quarter effect of some of the products that were launched during the first fiscal quarter. So the consolidation has not been a large detriment to us, at this point we still consider there are opportunities with the key customers and we continue to grow and we are also taking advantage of some inflationary opportunities on the products side.

Prakash Agarwal: So two follow-ups on this; one is base business you said has grown. So from both pricing and volume, can you just give some indications – is it high single digit or double digit growth that we have seen in our base business?

Robert G. Cunard: As I indicated, it is volume, pricing as well as product mix. So a key driver that we have been talking about for years now for our US business is Controlled Substances out of Aurolife, which were strong contributors for the quarter as well as some of the new product introductions that we saw late last fiscal year and first quarter this fiscal year. So the volumes overall were up slightly, the mix was better in terms of our inline products and then some of the price inflation was a nice driver for us.

Prakash Agarwal: This Aurolife number, I think I missed, what was the number Mr. Govind sir?

N. Govindarajan: Aurolife I did not give any specific number per se Prakash, because it gets merged with Aurobindo USA number.

Prakash Agarwal: Yes, last quarter we shared, it was around $25 million.

N. Govindarajan: You can say it has grown by around 25% to 30% on a quarter-on-quarter basis also.

Prakash Agarwal: And this would be largely Controlled Substances?

N. Govindarajan: Controlled Substances and Non-Institutional business is what I had said.

Prakash Agarwal: Okay, it is not VA, VA is yet to come in?

N. Govindarajan: No, I think Bob would explain you, VA is also there, but it is more skewed towards Controlled Substances and Non-Institutional business is what I said. Bob over to you.

Robert G. Cunard: Yes, that is correct, VA was pretty stable for the quarter and our improvement came on the Controlled side and from that more retail-based business.

Prakash Agarwal: Secondly, on the Europe side, could we have a number for Actavis, which we shared last quarter?

Arvind Vasudeva: Specifically, we will not be able to share but like I said we will be in line with the previous year revenue plus single digit growth up to 10%.

Prakash Agarwal: And if I look at sequentially, would we have done better or marginally or similar kind of performance?

Arvind Vasudeva: First two quarters are more integration quarters, so we will not be able to see a trend during this quarter, maybe next two quarters will give a direction.

Prakash Agarwal: In terms of good gross margin improvement because of the improvement in revenue mix, so ARV has gone down, API has gone down, so which has led to better revenue mix, so you said ARV is supposed to

come back. So how do we see your revenue mix going forward and qualitatively if you could give how the margins moving from first half versus second half?

N. Govindarajan: Qualitatively the ARV margins have improved compared to the past. Prakash, because of the improved margins it would not disturb the overall margins what we are achieving right now. So in simple terms, "Would it bring down the overall margins?" The answer is 'no', even with the improved business of ARV. As far as API is concerned, growth would happen more from non-Betalactam products rather than the Betalactam because as you would appreciate the capacities are getting increased in non-Betalactam, and we are not increasing the Betalactam capacity.

Prakash Agarwal: So our margins of 22% are sustainable given the existing product basket?

N. Govindarajan: That is our belief.

Moderator: Our next question is from Neha Manpuria of JP Morgan. Please go ahead.

Neha Manpuria: First on the Europe business. I understand that you are not giving us a breakup between Actavis and your existing business, but if I look at the numbers sequentially there has been a decline quarter-on-quarter. So has there been a certain market that has probably underperformed versus another, if you could give us region wise, some trend, and how we should look at Europe?

Arvind Vasudeva: Like I said these have been the first two quarters after acquisition have gone dominantly in integrating the businesses Since the larger revenue comes from tender markets of Germany, tender supply changes will give a little change in quarter-to-quarter revenue, but in market demands are quite consistent.

Neha Manpuria: In terms of second half, how should we look at EBITDA margins? We have done 22%, we had mentioned that ex-Cymbalta, ex-Actavis acquisition, we should have 22% margins. So should we see upside from the number that we talked about last quarter because we have already done 22% in the current quarter?

N. Govindarajan: I think I would like to just clarify that we said that it is ex-Duloxetine including Actavis. Yes it is our belief. I think first of all we would like to sustain the 22% before we start talking about improving that, even though there is scope for improvement as we progress. Please remember the fact that the more profitable business are still growing like while the US business is growing, while AuroMedics is growing, and also as I was mentioning, ARV is going to grow and the margins are better than what we used to achieve in the past. So there are enough steam left but at this juncture we would like to sustain the 22% margin for say a couple of quarters before we start talking about what further improvements can happen.

Neha Manpuria: What is the update on the US FDA inspection on Unit-4?

Ronald Quadrel: We had our inspection a month and half ago, the inspection went well, we had no critical observations, the observations that we had were process-related. We have put in our responses to FDA and we are hopeful that everything will go well.

Moderator: The next question is from Prashant Nair of Citi Group. Please go ahead.

Prashant Nair: Just a couple of questions. Firstly, is Cymbalta now at a normalized level or was there some upside in second quarter which can still normalize a bit further?

N. Govindarajan: I would put it this way, like the numbers from Cymbalta have been minimal at this quarter like it can further come down but it would not have significant impact in terms of our overall numbers, we will still maintain, that is what we are mentioning, Prashant.

Prashant Nair: Secondly from an R&D perspective, as you start filing some of the slightly more complex products going forward, where do you see your R&D spend moving say over a 2- to 3-year timeframe?

N. Govindarajan: I think you have to remember that with the huge addition of top line, thanks to Actavis, that acquisition, we were doing around 4.5%, so significantly the sales is growing and I had mentioned earlier also we will still be able to do more complex R&D within 4.5% of the increased sales. Commensuratively we are getting more money for the R&D spent.

Prashant Nair: From an overall revenue perspective, if we assume 4.5% to 5%, which should be reasonable, right?

N. Govindarajan: Absolutely.

Moderator: Our next question is from Manoj Garg of DSP Merrill Lynch. Please go ahead.

Manoj Garg: I would like to understand from an inventory perspective, we have seen a significant jump in the inventory, which is almost up by 48% in the first half. Does it indicate a very strong second half in the US?

Robert G. Cunard: Definitely, we continue to make investments in inventory. I would not say it is indicative of growth in the second half like we have seen once again product mix, some of the higher value items that we have seen, that has been a corresponding increase on our inventory as well, and again we are taking more proactive measures to make sure we have safety stock and everything to meet the rising customer demand. We have talked about it and some other points, and those about the customer consolidation. The market share that any given customer drives can be pretty significant, so we want to make sure we are in a position to prepare for those things and meet their service levels.

Manoj Garg: Bob, is it fair to say that whatever the impact of customer consolidation which was expected to come, which is already there in the base quarter, and from here we do not see much impact going forward in terms of price corrections or price erosions or something like that?

Robert G. Cunard: Yes, it is hard to say, as we stand right now, we have been through most of the consolidation, I do not see any more really significant consolidation on the customer, just on where they exist right now. So we will see as we go through bid cycles and everything else, but I think the majority we have been through and once again hopefully any reductions we see there or anything as far as price leverage gain through

the consolidation would be able to offset with some of the inflationary elements we have seen with some specific products.

Manoj Garg: This is a question for Robert. Like when do you start seeing the ramp up in the Injectable portfolio? Is it from the second half or Q1 of FY16 onwards?

Ronald Quadrel: One of the things that has happened is, you probably read in the papers, the FDA is taking longer on their approval times. As a matter of fact we just ran a study to show that if all the approvals that have been out there over the last year or so, the FDA is averaging somewhere in the neighborhood of 44 months with a standard deviation of about 16 months plus or minus. What we think is going to impact us is probably what we had expected for approvals this quarter will probably be delayed three to four months, not a big impact business wise for us because most of those original products that we were going to get approved were smaller products with a large product coming towards the second half of fiscal year 2016. So to answer your question, probably the first approvals we will see towards the end of this fiscal year and beginning of next fiscal year.

Moderator: Our next question is from Surya Patra of PhillipCapital. Please go ahead.

Surya Patra: In fact again on the Injectable business in US, recently we have again seen that three of your important Injectable products like Lidocaine, Tazo-Pip and Bupivacaine all three have become part of the shortage list. So does that mean we will be seeing kind of much better ramp up in the Injectable revenues in the subsequent quarter?

Ronald Quadrel: As I said, some of our approvals have been delayed which we had originally planned to have more revenues, which has been probably delayed a bit, but we are seeing some up side on Piperacillin, Tazobactam, Nafcillin, Oxacillin and a bit more on Lidocaine. So those have given us more sales, probably you will see more in the second half, but the shortages are intermittent shortages. So some of our larger competitors that have been in and out depending on where their supplies are, so it is not like we have a clear field to be able to take the whole market. So we are taking advantage wherever we can, we are seeing some upside but the upside is not to a magnitude that will show significant upside in the second half more than we are doing right now.

Surya Patra: Is my understanding that the Tazo-Pip is the leading product contributing more than 50% of the Injectable portfolio currently, is correct?

Ronald Quadrel: It is our largest product, but it is not contributing as much you think. It is probably more in the range of the high-30s.

Surya Patra: Secondly, just wanted to know, what is the pricing scenario in European regions that you are currently seeing, is it possible for you to give some idea, region basis, what is the kind of price that you are witnessing for the Generic products?

Arvind Vasudeva: Pricing pressures will remain in the country where you are on tenders. Because everybody competes on the tender prices, but specifically in the markets of France and maybe Italy there could be pricing pressures. All of us know that European Countries governments are working towards reducing the Healthcare costs. These price drops needs to be compensated by higher volumes internal cost reductions and also launching new products.

Surya Patra: So in fact what we understand is you are continuing with your product rationalization initiative that you have already taken for European markets after the acquisition and also seeing the pricing pressures. So what is the kind of volume and value growth that you are anticipating, and when that would really come, can you give us some sense on it?

Arvind Vasudeva: We indicated that value growth will be in single digits and it can be on the higher side between 9 and 10. The focus will be product mix and reduction in cost from Aurobindo point of view, the focus will remain dominantly on profitability, revenue growth will be in line of single-digit and at best towards 10%.

Surya Patra: On ARV Formulations, can you give some outlook, because both in the first quarter as well as first half we have seen kind of 14% to 15% kind of a decline YoY respectively, so what is the kind of outlook one should have for the ARV business?

Arvind Vasudeva: Like I think Govind indicated, tenders have cyclicity. So this year the tenders are more in the second half in terms of supply. But like we indicated we will grow at about 10% on a year-on-year basis on ARVs on top line, profitability will be better because the product mix is moving towards triple combination, which have a better margin due to lower competition.

Surya Patra: So that means we are anticipating a robust second half so far as ARV Formulations are concerned?

Arvind Vasudeva: Yes, the tenders are more skewed towards the second half of this year.

Surya Patra: Immediately after the tender, we can start booking revenues?

Arvind Vasudeva: Yes. Within 60, 90 or 120 days depending on type of the tender.

Moderator: Our next question is from Nimesh Mehta of Research Delta Advisors. Please go ahead.

Nimesh Mehta: I just want some more color on the explanation of steep increase in gross margins vis-à-vis our last quarter on a sequential basis. So I understand the base business has improved, but given that last quarter we had Cymbalta sales also, what could explain the sharp improvement in gross margins?

N. Govindarajan: Obviously, due to the increased US sales and also in other business like the rest of the world sales. You have to appreciate the fact that like when we have committed very clearly that non-Cymbalta also, we will target this particular bottom-line of Rs.400 crores plus or minus 10% maintaining 22% EBITDA. So that is because of the fact that leaving Cymbalta the rest of the business we clearly see the visibility of growth

which is particularly if you see the US growth has been an exponential growth and also like I think the margins in terms of the various other businesses is also better than what we used to achieve.

Nimesh Mehta: On the Europe business, in terms of the operational integration, what would be the next plan, meaning, we will be changing the source of some of the products or we will be changing the raw materials, supply, what would be the next step to ensure that the integration is smooth?

Arvind Vasudeva: First, what we have done is, we have done a front end operational integration, most of which has been done. Second part is we will be switching the Actavis product with Aurobindo product wherever we have a better cost of goods that is being done currently where ever regulations allow us. The third Phase which will take another I think 18 to 24 months more, we will be moving some of the products to our own site so as to reduce the cost of goods. So these will be three Phases. One is completed almost, second is ongoing in terms of replacing Actavis products with our products.

Nimesh Mehta: How many of those products are replaced?

Arvind Vasudeva: Currently, it is not a large number, but ongoing basis half of them will be replaced with Aurobindo products over the next 24 months for sizable number of products and some more can take longer depending on our R&D and Manufacturing capacity.

Nimesh Mehta: Out of the 1200 products that we have, roughly about 600 we will be able to source it from Aurobindo directly?

Arvind Vasudeva: No, molecules are only 450, so 200 may be replaced; 1200 is product forms, so half of them could be replaced over the next 24 months or so depending on R&D and Manufacturing capacity creation.

Nimesh Mehta: Those products where you already have an overlap, meaning Aurobindo is already manufacturing the product and you will be changing it?

Arvind Vasudeva: Yes there is some overlap but majority are non-overlap products.

Moderator: The next question is from Surjit Pal of Prabhudas Lilladher. Please go ahead.

Surjit Pal: I just have one question, in the sense that I was just focusing on this loss or gain on foreign currency. So is it mainly because of your reinstatement of debt, comparing the 2% of volatility and if I compare your Q1 number, is it not too high?

Santhanam Subramanian: We closed the rupee at the end of June at 60.17 and the rupee is now closed on 30th September at 61.75. The Rs.42 crores exchange fluctuation, the includes Rs.66 crores coming by way of reinstatement of borrowings . Because we have a long-term loan ECB to the tune of around 180 million and also having the short term loan PCFCs, etc. So that is the main reason.

Surjit Pal: Govind, can you throw some light on the Penem prospect, how many products you are still planning to file and when do you see those products, possibility of launches in the US market?

N. Govindarajan: Two have been filed and one is under validation, and for one more product the project completion would happen by let us say somewhere in the month of April-May, so the total filing would be four. We expect the inspection somewhere towards the end of next year, so then once the approval is in place, then we will start pushing into the US market, so that is the plan. As of now, the two products which we have already filed, one of them we have started exporting to Mexico, we are expecting Brazil approval in the next few weeks to a couple of months, The European business also should start somewhere in the middle of next financial year, with that I think this facility would start breaking even and start making money.

Surjit Pal: Europe, already you have filed?

N. Govindarajan: Inspection has been done already, yes.

Surjit Pal: How about Peptide business?

N. Govindarajan: The Peptide business, we are planning to file our first set of DMF by the end of the financial year, we will be filing at least two products, and two more products will be filed six months from then. So clearly we have created a facility where we have two modules, now we are expanding it to a third module because there is pressure in terms of filing more number of products. So I think clearly once we file the DMF by the end of this financial year, we expect inspection to happen within 15-18 months, while parallely the DMF is also reviewed so from there like the business would kick in. But, there is good amount of excitement because there is enough requirements from the customer and from a technology perspective today we are within the top 3 or 4 in the global arena in terms of our capability, that has been established – thanks to supplying samples and being qualified through the sample evaluation.

Surjit Pal: Basically what we are seeing is that FY17 or FY18 will be the main time when these two products will start performing for you?

N. Govindarajan: From a commercial perspective the answer is yes, but please understand the fact that even during the filing Phase of DMF, we will be supplying enough quantity of validation batches as well. So from a revenue perspective we do not need to necessarily wait till the product gets commercialized.

Surjit Pal: What will be the target market in both these kind of products?

N. Govindarajan: We are right now focusing on US and Europe, but interestingly, even now like there is some sale which is happening even in domestic market and some non-regulated country as well.

Surjit Pal: No, I was looking for quantification of numbers, what kind of target market are you looking at?

N. Govindarajan: You are talking about from a revenue perspective?

Surjit Pal: Yes.

N. Govindarajan: I think at peak, let us say, out of the 30 products if they reach around let us say 15 to 20 products this has a capability of reaching at least $70 million to $80 million of top line or even reaching $100 million dollar topline. Please remember the fact that Peptide is one of the most profitable businesses in the entire spectrum.

Moderator: Thank you. Our next question is from Prakash Agarwal of CIMB. Please go ahead.

Prakash Agarwal: Sir just trying to understand next year where we had earlier commented that fiscal '16-17 is the year where we would see more Injectable approvals? So that is a). And b) Controlled Substance would start contributing in a bigger manner. So what I am trying to understand is given the fact that we have already had $200 million exit rate per quarter, so annualized $800 million, so what is the outlook there for FY16 and FY17 on the US?

N. Govindarajan: I think from a revenue perspective we are not giving any outline at this juncture, Prakash, obviously, yes we are confident about the growth but we are not putting any numbers at this juncture on the table.

Prakash Agarwal: In the past we had talked about (+20%) growth….?

N. Govindarajan: That is something which is minimum guaranteed, it can be better than that, that is what we are saying, but we are not giving specific numbers. Having said that, definitely, we still feel that we will be able to maintain the momentum what we have achieved as of now.

Prakash Agarwal: But in FY16, do you think the Injectables would drive the bigger portion of growth or it would be like other pieces as well, if you could just highlight?

N. Govindarajan: Let me explain to you one part, while already Ron is reaching 65 to 70 million revenue level on an annualized basis, please remember the fact that we will still keep growing, when the major shift will also happen when the products from the Oncology will also kick in, so that would be at least let us say three years from now, but having said that I would let Ron handle in terms of how the outlook for the next three years. Ron?

Ronald Quadrel: What I would say from the approval perspective, over the next six quarters, we are expecting approximately 25 to 28 FDA approvals, wholly dependent on their approval time, but we feel pretty comfortable with the times that we put in place that we can hit that. Behind that we have another 20 some products that are currently under FDA review and then behind that we had another 50 products that are in development and we have not yet filed. So Prakash, as you correctly assume, as we move forward here, fiscal year 2016, fiscal year 2017 will be heavy growth for us as we get these approvals, but then also as Govind mentioned in the fiscal year '18 timeframe we will start seeing heavy approvals from the Oncology side as well as the Hormonal side. So all in all you are going to see upward growth in '16, '17, '18, '19 in the Injectable business.

Prakash Agarwal: If you could throw some light on the outlook on Controlled Substances, I think this quarter it has been a phenomenal growth, what is the current share in terms of revenue and what are the pending approvals we are targeting and what is the addressable market size there please?

N. Govindarajan: In the Controlled Substance side, we have not broken out specifically what that is driving, but it is a significant contributor to our Aurolife revenue and overall US revenue. We currently have 7 products coming with the agency on the Controlled Substance side, markets about 500 million with those products. As Ron indicated on his comments on FDA and approval timeline we are experiencing the same thing on the Oral Solid side. So a little bit of that is uncertain as far as the exact timing of the approval, but we think that continues to be a driver in the next year and the following as well.

Prakash Agarwal: I missed it, you said 7 products in the market with 500 million addressable market size is it?

Robert G. Cunard: That is actually the pipeline, they are not in the market today, that is what is pending with the agency.

Prakash Agarwal: How many do we have today and what is the likely revenue share?

Robert G. Cunard: Again, we have six controlled substances in the market today, and we have not broken out detail on what they generate.

Moderator: Our next question is from Prashant Nair of Citi Group. Please go ahead.

Prashant Nair: I just had a question on the European business. If you could just repeat the strategy you have, I could not catch all of it, so what you are doing in Phase-1, 2, and 3 to improve profitability?

Arvind Vasudeva: Phase-1, what we have done is we have integrated both Aurobindo and Actavis business together. So there is benefit coming out of that in all the countries that we had operations, both for Actavis and Aurobindo. Phase-2 is wherever possible that Aurobindo products have lower cost of goods and higher margins, they will replace- Actavis portfolio but this will happen country to country and depending on regulatory possibility. These two are ongoing. And third will be when we bring up to 200 of the 500 molecules that we have, which is equivalent to 600 and odd product forms, will be brought in-house into India manufacturing sites and thereby reducing the cost and enhancing the margins.

Prashant Nair: The different between Phase-2 and 3 is that currently you already have approvals for these dossiers and you are just replacing them with the Actavis products and Phase-3 is when you actually have to get fresh approvals from your side, is that correct?

Arvind Vasudeva: Yes, true.

Moderator: The next question is from Jigar Valia of Ohm Group. Please go ahead.

Jigar Valia; Mine is a follow-up on the EU operations. Just to understand on the strategy, when your Phase-1 you say integrated business in all countries, does it also mean that you would have integrated distribution,

particularly, in the form of common markets there, you are also there, is there any realignment on the distribution side of it, I mean?

Arvind Vasudeva: Initially like I said customers are uncommon, the products are uncommon, wherever we have a tendering business, that is where the replacement can happen early on, or wherever we have the pharmacy direct supply, there the replacement can happen early on. So, there could be addition of distributors, because Actavis have their own distributor, we have our own distributor.

Jigar Valia; Now you are going with all the products with both the distributors probably, is it?

Arvind Vasudeva: No, depending on the products and customers. So distributors are only via media to reach there.

Jigar Valia; Secondly to understand in terms of, we have seen tremendous traction in terms of the margin expansion over the past many quarters and I would compliment you for that, but incrementally going ahead, is it fair to assume that the scope for further improvement from operating leverage would be less, it would be more out of product mix and our increasing share of US business, so if you can indicate in terms of do we have capacities at certain plants right now, we are on the current product mix also, you would have be like more than 25% spare capacity?

N. Govindarajan: No, I think we are expanding both in terms of API and the Finished Products, and frankly right now we have more opportunities than what we are digesting right now because if you ask me, if the capacity had been a bit more available than what we have right now, it would have been great, but having said that, in API already, we have started investing across all the plants, in fact, certain capacities would kick in starting from the end of the year to the beginning of next year, but the major capacity which is a pretty large volume, Vizag would kick in towards the end of the first quarter of next year or beginning of second quarter, parallely in finished dosage we have invested in Unit-7 in terms of certain capacity plus we are also investing in terms of the European facility which is for the Actavis requirement in Vizag, plus we have also started working on the facility which is needed for the next level of US growth in Naidupet. So that CAPEX is already going on.

Jigar Valia; Any indicator apart from the Rs.600 crores of maintenance CAPEX, what would be the overall CAPEX be?

N. Govindarajan: We are expecting this year like it would be around Rs.600 crores, once we start measuring the cash flow and looking at the various aspects of it we will review it at the end of the next quarter, but next year would be equivalent or slightly more than this, in terms of let us say Rs.600 to 700 crores of CAPEX would also be there for next year is what our estimation as far as this year and next year is concerned.

Jigar Valia; When you have given this guidance of Rs.400 crores a quarter and approximately Rs.1500-1600 crores for this year, would you be able to help us on a broader basis over the years, is it possible to grow on the bottom line CAGR (+20%) with steady margins or around similar margins?

N. Govindarajan: I think it is absolutely possible, but as I have been mentioning that we do not want to have blue ocean numbers, like I think we would like to just move one point at a time, as of now like we are very clear for the next few quarters this is what we have in terms of achieving this 400 plus or minus 10% and ensuring that from a top line perspective to the EBITDA percentage at least maintaining the 22% EBITDA. So this is our aim in the short term. But to answer you more specifically, in the medium to long term, can it improve? Absolutely! As I was mentioning earlier that the base business is growing as Bob had explained his business growing from the regular products apart from the new approvals which he is waiting for including Aurolife/Controlled Substance, apart from that Ron was explaining about the various aspects which are going to happen in terms of the next three to five years, apart from that we are also seeing traction in terms of the ARV business, like the margins are going to be better than what it used to be in the past. The European business like as Arvind was explaining that we are clearly seeing that next year we would break even at the PAT level and subsequent year we will improve to the extent of at least 8% EBITDA and then subsequently further improving. Even in the API, the growth is clearly happening in terms of the non-Betalactam which is predominantly high value products and even Japan kicking in, and there are enough steam left out for us to further improve without any doubt.

Moderator: Thank you. The next question is from Chirag Dagli of HDFC Mutual Fund. Please go ahead.

Chirag Dagli: I was looking at the kind of mix that you always sort of disclose for the US business. If I see the Injectables business, it is growing reasonably well and with all the scale up, the second half should be better than the first half, this has been the trend in the last few quarters and as you are scaling up, similarly for Cephalosporin as well the second half should be better than the first half and Controlled Substances which are now scaling up well, that also if I assume this exit rate, then the second half will be better than the first half. Is there anything within the balance business which will sort of lead to an inferior performance in the second half of this year which we should be aware of.

N. Govindarajan: No, as I was explaining, there are only two areas where you had seen degrowth. One of the gentlemen had asked earlier, by growing ARV or by growing API, would it have an impact on the bottom line, so you are also having a similar concern in terms of like any other business can bring down the margin, the answer is 'no', for a simple reason as I was explaining earlier, like the ARV business, the margins are better than what it used to be in the past, #1, #2, please remember the fact that within the ARV, the growth is more towards the triple combination where in fact I think definitely it is a sustainable business for the next couple of years which has been explained in the past as well and also in the API the growth has been from more of non-Betalactam products, which definitely will have better margins than the typical API margins what we used to have. So clearly we do not see any spoiler from this particular bunch of business which is happening.

Chirag Dagli: My question was more to do with the US sales run rate, which was $185 million roughly in the first quarter, it is now $194 million in the second quarter, and if I look at individual components, each of these seem to be scaling up and probably second half should be better than the first half, which is what I was trying to understand. Do you think that there can be any spoilers in the base business for the US sales?

Ronald Quadrel: I do not think there are any spoilers from the Injectable side at all.

Robert G. Cunard: I think as you indicated, some upsides on the Controlled Substances, if nothing else, just from the kind of a full quarter effect as we go forward as we continue to ramp up some of those products. Cephs I believe will be pretty consistent, they come in near 35 to 40 for the year, we will see when we get in the season right now and see how that continues to proceed. The one thing I will caution just a little bit is, we have seen some inflation on items, we think that can continue on some specific products, when things start to break through with the FDA as far as approvals, that creates upside for us with new products that also can bring other people into the market as well. So we need to be sensitive with that and when that happens, and what that may do the competitive environment. But right now I think we are very bullish on US business, it is growing, and we have good drivers.

Chirag Dagli: Then a follow-up on that, if the US business will continue its momentum and probably be better in the second half than in the first half, then my own sense is that I think this Rs.400 crores totally PAT run rate should actually improve, is it not, sir?

N. Govindarajan: I think frankly we would like to first of all maintain them and reach that for the next couple of consecutive quarters before we start talking about it, like even better numbers than that.

Moderator: Thank you. Our next question is from Rakesh Jhunjhunwala of Rare Enterprises, please go ahead.

Rakesh Jhunjhunwala: Nexium today the approval of Ranbaxy has been withdrawn, and the other product that Valcyte, the exclusivity also has been withdrawn. So there is likelihood I am told there is a lot of pressure on the FDA to withdraw the exclusivity of Ranbaxy on Nexium also. Because you know people are saying they want cheaper generics of Nexium. So if that happens, it can be very significant for us?

N. Govindarajan: It will not be significant for us because the reason is, there are a few players who already have got tentative approval and we are still in the queue, we have not received the tentative approval, and we are not sure about the timing of the tentative approval and when that particular market would be opened for others. At this juncture we are not sure about the particular opportunity which is existing for us. We feel that it might not be existing, but we have to wait and see in terms of how fast our filing is moving. So at this juncture we have not received tentative approval compared to a couple of people who have already got tentative approvals. Bob, you have any comments on this?

Robert G. Cunard: That is correct; it is all a question of the timing of it and where we will be on the approval timeline.

N. Govindarajan: Just to clarify, we already filed it and it is under review.

Rakesh Jhunjhunwala: If FDA gives approval to a lot of people, we may also get it?

N. Govindarajan: We wish sir that is something which we are not able to predict, but as I said, like we are not ahead in the queue, so we are obviously behind the queue.

Moderator: Next question is from Ranjit Kapadia of Centrum Broking. Please go ahead.

Ranjit Kapadia: My question relates to API business. Both SSP and ARV is referred in the API segment. So is there any chance of revival, is the market conditions or the prices were slashed?

N. Govindarajan: First of all let me clarify, the ARV what all we are segmenting it is not API, it is Finished Product. As far as API is concerned, our capacities are running at full level and in terms of our supplies internally I think compared to the year-on-year, like compared to last year, Q2 to this year Q2, I think it has increased by almost around 27% in terms of the products getting into the Formulations business, #1. #2, I think there has been some pressure in terms of certain penicillin-based products. So we have held the material to sell it at a better price rather than rushing towards just achieving the sale. As we were consistently maintaining Ranjit bhai that in the API business also we are clear that we are not chasing the top line, we wanted to ensure that we have a healthy bottom line. So obviously the major concerns right now or the constraint is the capacity, and as I was explaining that we have invested already across various units, out of which certain capacities are going to kick in towards the end of the year, but the major capacity would kick in by the end of the first quarter of next financial year, after that you will still start the propulsion and the API growth will also happen. Frankly, there is enough opportunity for us, in fact, we clearly see the customer interest on the API business is also growing because they clearly see that they would like to go to the large players rather than the smaller players compared to the regulatory environment as well. So clearly we see that there is a great opportunity for the API as well.

Ranjit Kapadia: My second question relates to Vizag. Is there any impact of cyclone on this manufacturing facility or?

N. Govindarajan: There has been an impact to the extent of, there was no power and we were not able to run full like the first few days, and we right now are getting back on track in terms of ensuring at least we are able to run the key products, there has been some minor issue in terms of the labor as well, but we are still ensuring that the key products whatever we need to internally supply, we are focusing on ensuring that there is no disturbance, the majority of the products will come on track, so we do not see much of an issue in terms of the main products.

Ranjit Kapadia: Any damage to the property?

N. Govindarajan: There were, but not something which is really halting, across the plant there were some damages, and we had brought it on track in terms of whatever damages happened.

Moderator: The next question is from C. Sri Hari of PCS Securities. Please go ahead.

C. Sri Hari: Two questions basically. #1, if you could please quantify the share of price hikes in the growth in the US business? And secondly if I look at the other expenditure, it has grown significantly even sequentially considering that the sales in the two major markets have remained more or less flat. So could you please elaborate on that as well?

Santhanam Subramanian: On year on year basis, the other expenditure has increased by about Rs.282 crores, mainly because of the acquisition of the Actavis business, which is not comparable and apart from that there is an increased volume growth taking place in US, which is also contributing to some additional expenditure; however this is well within the overall control of the numbers.

C. Sri Hari: I am talking sequentially, there is close to 300 basis points growth in other expenditure as a percentage of sales?

Santhanam Subramanian: On quarter on quarter basis, increased carriage outward expenses and some selling expenses, etc, that is the main reason.

C. Sri Hari: Are there any one-off items there?

Santhanam Subramanian: Only the carriage outward selling expenses.

C. Sri Hari: I wanted to know the share of price hikes in the US Generic sales?

Robert G. Cunard: Obviously, we do not break anything out on the specific product base, we have seen a few products, it is certainly not large in terms of number of product families or SKUs that we have seen, but the increases that we have seen have been attractive, hopefully that opportunity continues and we see some inflation on some other items as well, but we have not broken out anything specifically what they are.

C. Sri Hari: In micro numbers, would it be let us say 2% to 3% the contribution?

Robert G. Cunard: It is in the mid single-digit.

Moderator: Thank you. The next question is from Chetan Vora of Value Quest Research. Please go ahead.

Chetan Vora: Just wanted to understand the employee cost; have increased sequentially from Rs.308 crores to Rs.337 crores. What that would be primarily?

Santhanam Subramanian: There is expansion in capacity in some of the formulations units and increase in US operations staff welfare expense.

Chetan Vora: So the employee cost as a percentage to sales sequentially has gone up from 10.7% to 11.8%?

N. Govindarajan: We will get back on that more specifically offline.

Chetan Vora: You said the CAPEX would be what, Rs.600 to 700 crores?

N. Govindarajan: Next year you are talking about Rs.600 to 700 crores, this year I said 600 crores, Chetan.

Moderator: Thank you. Our next question is from Prakash Agarwal of CIMB. Please go ahead.

Prakash Agarwal: Just a follow-up on the two questions asked on employee cost and other expenses. Obviously business is expanding and we accordingly need to expand. But is it fair to assume this will continue to increase given the revenue growth because of added facilities as well as integration in the Europe business?

N. Govindarajan: As a percentage we do not expect it to further increase is what we would say, Prakash.

Prakash Agarwal: Both from employee side and other expenses?

N. Govindarajan: Yes, because the reason is, it should be commensurate to the growth which is happening in the sales is what we would say.

Prakash Agarwal: So first half we can take an average basically?

N. Govindarajan: Yes.

Prakash Agarwal: Second question was on the CAPEX so far in H1. What would be the number like?

N. Govindarajan: Approximately around Rs.275 crores or so.

Prakash Agarwal: Little higher is expected for the second half? So we ideally could have seen higher debt reduction versus your guidance of $25 million to $40 million?

Santhanam Subramanian: Certainly, because we will be getting the cash flow generation from the business also, that will take care of CAPEX, plus we will be reducing as it stands today to the tune of around $25 million to $40 million. We have indicated this number at the beginning of the year itself, around $100 million to $125 million. So we will be trying to stick on to that.

Prakash Agarwal: Second question was to Arvind sir, on the France business. We understand from industry participant that France has seen a significant erosion in terms of billing from around 15%, 20% to 40%. So since France is a big market for us, what has been the impact for this quarter, and what is the outlook for us?

Arvind Vasudeva: This is I think the pharmacy discount change, it is not to do with the price reduction, price reduction is in line with normally happens, year-on-year as government defines the prices, but there was regulation change in terms of what margin can be given to the pharmacies, that has been changed from 17% to 40%, but that is within the system, it does not have any impact on the margins.

Prakash Agarwal: But in France market, what is our outlook – is it better than your Europe outlook of high single-digit to 10% growth or we expect this to be little inferior in terms of quality of growth?

Arvind Vasudeva: We have three businesses across the Actavis portfolio – one is Hospital Injectable, second is Branded Generics, and third is Generics. So Hospital has minimal impact, it is doing well, Branded Generics, minimal impact, it is doing well, Generics is the only area where there is a pricing impact, because every

year the prices will keep coming down, and like I said earlier we need to look at product mix management, new product launches, and internal cost reduction which has to undo those value losses.

Moderator: Thank you. Our next question is from Manoj Garg of DSP Merrill Lynch. Please go ahead.

Manoj Garg: Just a couple of questions. First of all on the R&D side. At a percentage to sale, maybe it may remain between 4% to 5%, but there is going to be significant increase in the absolute dollar spend on the R&D side. So just want to understand like which are the areas where we are putting up this incremental money and have we started any other therapeutic area apart from Injectables in the US?

N. Govindarajan: In the US, we have also started microspheric, that is another additional area. Bob and Ron, you want to comment in terms of what are the other things we are doing on the R&D additional thing which you are doing in US.

Ronald Quadrel: From the Injectable side as you just said, we have microspheric as well as Liposomol Injectables and what we feel is that those products are much more difficult to develop and to manufacture, there will be less competition on those and higher addressable market.

Robert Cunard: As far as US obviously we have a very specific development base again around the Controlled Substances and specifically some of the extended release Formulations and some of the abuse deterrent Formulations we are looking at.

Manoj Garg: Ron, when do we expect this microspheric, in terms of filing, is it like some time away, or we may see the filing over the next 12 to 18 months?

Ronald Quadrel: I would say probably more in that 18-month timeframe because of the requirements of Formulations as well as doing Bioequivalence. And once we have that, then we will file as soon as we can, but I think it will be probably more than 18- month timeframe.

Manoj Garg: Arvind like if you look at in terms of ROW market, we have seen a steady increase in the ROW market in the last couple of quarters, and now we have come to around $23 million to $24 million kind of quarterly base run rate. Just want to understand which of the markets contributing to this and how do we see the growth going forward?

Arvind Vasudeva: The major markets are Brazil, South Africa, and then we will look at markets of Canada, and then cluster of Africa, Asia-Far East, Russia-CIS and LatAm. These are the areas that we are looking at. What we have done is, we have been putting people on the ground now because gross margins in these countries are good, and we are working towards increasing revenues from these markets where it is a Branded Generics market. Dominant, like I said is Brazil, South Africa, the two large markets, then the clusters of Africa, Asia-Far East, Russia-CIS and LatAm.

Manoj Garg: And overall now as a consol these markets are offering us very good margins because as you said the realizations are pretty high in these markets?

Arvind Vasudeva: As the revenue go up, the cost of promotion and people will come down, so initially there will be investment, which happened last year, but as we go forward, EBITDA margins will be better because fixed cost will remain similar.

Manoj Garg: Since you have outlined that the growth drivers are in place for the next two or three years. Particularly one has to understand the challenges or the key risk which you envisage in the business to achieve those milestones. What could be the key challenges?

N. Govindarajan: Obviously, the top most is to ensure that we are always on the right regulatory environment, that is the top most thing. Apart from that, we have always the typical Generic business risk in terms of the pricing and in terms of certain other competing introductions and what not. But one of the reasons, Manoj if you have seen, if there are enough questions in terms of whether we can even improve or we can do better, so one of the reasons we are still maintaining, we would like to achieve consistently or consequently the number what we had committed is because while there can be some upside, there can be some downside in terms of the business and we would like to ensure that it gets balanced and at least we are able to maintain this.

Moderator: As there are no further questions from the participants, I now hand the floor back to Mr. T. Roychoudhury for closing comments**.**

T. Roychoudhury: For further information, please visit our website www.aurobindo.com or feel free to get in touch with me for any additional queries that you may have. Thank you everyone for joining us in the call today and wish you a very good evening.

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