“Aurobindo Pharma Ltd. Q4 FY17 Earnings Conference Call”

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Moderator: Good Day, Ladies and Gentlemen, and Welcome to Q4 FY'17 Earnings Conference Call of Aurobindo Pharma Limited. As a reminder, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*', then "0" on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Krishna Kiran -- Investor Relations, Aurobindo Pharma Limited. Thank you and over to you sir.

Krishna Kiran; Good Morning and a warm welcome to our Fourth Quarter and Full Year FY'17 Earnings Call. I am Krishna Kiran from Aurobindo Pharma Investor Relations Team. We hope you have received 'Q4 Financials' and the 'Press Release' that was sent out yesterday. These are also available on our website. With me, we have our senior management team, represented by Mr. P.V. Ramprasad Reddy – Executive Chairman, Aurobindo Pharma USA; Mr. N. Govindarajan – Managing Director; Mr. Sanjeev Dani – COO & Head, Formulations and Mr. Santhanam Subramanian – CFO.

We will begin the call with "Summary Highlights from the Management" followed by "Interactive Q&A Session."

The company from 1st April 2016 has adopted Indian accounting standards (IND AS), and hence financials which we will discuss today are in accordance with that. For comparison purpose, the Q4 and full year FY'16 numbers are also restated as per IND AS.

Please note that, some of the matters we will discuss today are forward-looking, including and without limitation statements relating to the implementation of strategic actions and other affirmations on our future business, 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 statements to reflect future events or circumstances.

With that, I will hand over the call to Mr. N. Govindarajan for the highlights. Over to you sir.

N. Govindarajan: Thank you Krishna. Good Morning Everyone. We are here to discuss the fourth quarter and FY'16-17 results declared by the company. For the year, the company registered a revenue growth of 8% YoY to Rs.15,090 crores. The EBITDA before FOREX and other income increased by 8% to Rs.3,434 crores and profit after tax increased by 13% to Rs.2,296 crores. In Q4 FY'16-17, overall revenues declined by 3% YoY to Rs.3,642 crores, mainly due to competitive environment. The EBITDA before FOREX and other income declined by 16.7% to Rs.721 crores, impacted by one-time inventory write-off and other exceptional items. PAT declined by 4% to Rs.533 crores.

In terms of the Business Breakdown: Formulations business contributed 80% of the total gross sales in FY'17. The Formulations sale for the year stands at Rs.12,045 crores, registering a 9% growth YoY. The Formulations sale for the quarter stands at Rs.2,879 crores. API sales for the year were at Rs.3,042 crores, an increase of 5% YoY, for the quarter API sales were at Rs.763 crores. In the Formulations business, the total sales from the US markets stood at Rs.6,827 crores for the year, an increase of 12% YoY. For the quarter, the US sales witnessed a growth of 1% YoY. The company achieved the growth despite pricing pressure in the oral products base business. Injectable business continued its growth momentum.

Aurobindo USA, the company marketing oral products in USA has witnessed a decline of 1% YoY for the year and 13% YoY for the quarter due to higher price erosion in few selected products as explained in the earlier call.

We launched five new products in the quarter taking the total launches in FY'17 to 24 products. We received 12 approvals including 2 tentative approvals during the quarter. We have filed 5 ANDAs during the quarter. AuroLife, our US manufacturing arm, continue to witness increase in demand.

AuroMedics, the Injectable business maintains its strong growth momentum; for the year the business witnessed a growth of 67% YoY to US$157 million. For the quarter, sales grew by 18% YoY to US$42 million. We launched one new product during the quarter, taking total launches in FY'17 to 11. We have filed three ANDAs during the quarter taking total ANDA filings for the year to 12 ANDAs. Under the Injectable segment, including Ophthalmics, we have filed a total of 92 products as on 31st March 2017, out of which 54 have received approval including 2 tentative approvals and the balance 38 are awaiting approval. We received 4 approvals during the quarter. We have started filing Oncology ANDAs with USFDA from Q4 FY'17.

Aurohealth, which manufactures and markets pharma OTC products in the US continue to gain penetration into several key national retailers as well as select regional accounts. Currently, Aurohealth is now shipping to a total of 24 customers and having a product basket of 85 products.

The company as on 31st March 2017 has filed 429 ANDAs on a cumulative basis, out of which 276 have final approval and 38 having tentative approvals, including 10 ANDAs which are tentatively approved under PEPFAR and the balance 115 ANDAs are under review.

The unit wise filing and approval are as follows: From Unit-III, 126 filed, 100 approved; Unit VII, 158 filed, 88 approved; AuroLife, 26 filed, 16 approved; Unit IV, 78 filed, 41 approved; Unit XII, 20 filed 19 approved; Unit VI, 11 filed and approved; Auronext, 4 filed and 1 approved; Unit X, 4 filed and Eugia 2 products have been filed so far; Unit III, VII, and AuroLife manufactures Oral Non-Beta lactam products; Unit IV manufactures General Injectables and Ophthalmic products; Unit VI and Unit XII manufactures Cephalosporin and Semi-Synthetic

Penicillin, respectively; Eugia manufactures Oncology and Hormonal products and Auronext which has its facility in Bhiwadi, Rajasthan manufactures penem injectable products.

Europe Formulations sales for FY'17 were at Rs.3,277 crores, an increase of 5% year-on-year. For the fourth quarter the business registered a decline of 8% year-on-year to Rs.777 crores, largely due to base currency depreciation and it is flat at base currency.

The acquired Actavis business continue to see profitability during the year. During the quarter, Unit XV, the dedicated manufacturing facility for European markets has been commissioned. Emerging markets formulations sales for the year were at Rs.756 crores, up 17% year-on-year. For the quarter, the revenue was at Rs.197 crores, up by 21% year-on-year. ARV Formulations sales was at Rs.1,185 crores for the year and Rs.262 crores during the quarter, representing a decline of 2% year-on-year for the year and 20% year-on-year for the quarter.

In terms of Segmental Classification, US Formulations contributed 45% of the overall revenues in Q4 FY16-17 Vs 44% in Q4 FY15-16. Share of EU Formulations declined to 21% in Q4 FY16-17 Vs 22% in Q4 FY'15-16. ROW market share increased to 5% in Q4 FY'16-17 Vs 4% in Q4 FY'15-16. ARV segment sales represent 7% of the total sales in Q4 FY'16-17. API business contributed 21% of the total revenues in Q4 FY'16-17.

R&D expenses is at Rs.146 crores during the quarter, which is 4% of the revenues. The closing rupee versus US dollar rate was at Rs.64.85 in March 2017 and Rs.67.925 in December 2016. CAPEX for the quarter is around US$109 million, including inorganic CAPEX of US$35 million. The effective tax rate for the quarter is at 18.1% of PBT. The net debt stood at US$439 million as on 31st March 2017 against US$640 million of March 2016 and US$410 million in December 2016. The majority of the company's debt is denominated to foreign currency. The cash and bank balance is at US$80 million.

This is all from our end and we are happy to take your questions now.

Moderator: Thank you very much. We will now begin with the Question-and-Answer Session. The first question is from the line of Kumar Saurabh from Motilal Oswal. Please go ahead.

Kumar Saurabh: Sir, how should we look at your US sales growth in FY'18 especially in the current context and how much was the base price erosion during the quarter which we saw?

N. Govindarajan: As far as base price erosion is concerned, it is around 7-8% in FY17. We do not guide in terms of specific number but overall, we are confident about growth for the next year on a year-on-year basis. Even though there can be pricing pressure in terms of the oral business, you have to remember the fact that there are other four engines which will continue to fire like Auromedics, Aurolife, Natrol and Aurohealth. So we would still grow. Overall as an institution, we still believe that we would be able to grow when compared on an year-to-year basis

Kumar Saurabh: So, if I look at your other businesses which is Europe and ARV, those businesses have delivered muted growth during the quarter. Is this one-off thing or this is the new base which we should look at?

Sanjeev Dani: Actually in Europe, we had a base currency-wise flat growth but going forward there will be 5% to 8% as we have always maintained.

N. Govindarajan: As far as ARV business, we have been continuously maintaining that it is a tender based business and we would be more focused on the bottom line rather than just focusing on the top line. During the last quarter, actually due to certain prioritization, our ARV bulk was not completely supplied to the finished dosages, that was one of the drivers but we expect with the new product approval, we still expect that ARV business to maintain its growth, but again as we have maintained in the past it is all subject to the tender pricing.

Kumar Saurabh: In US, we have been continuously seeing that, launches are lacking with the pace of approvals. So how should we look at FY'18 from that perspective? How many launches do we expect in FY'18 and in terms of approval also what is the outlook for FY'18?

P.V. Ramaprasad Reddy: Our Unit-III and Unit-VII are running almost at 85-90% capacity. The unit XV for Europe has commissioned and lot of product transfers are happening to it. Another new unit for US in Naidupet has been approved by FDA without any 483 in the last month. We are launching both newly approved products and some of the old approved products, still around 25-products we have to launch it, which are going to launch in coming quarter steadily. But we are not hurry to launch until and unless easing of capacity issues.

Kumar Saurabh*:* So is it fair to assume that given the fact that these couple of plants are getting commissioned…?

P.V. Ramaprasad Reddy*:* Already approved and commissioned

Kumar Saurabh: Shift to Vizag will continue. So then more capacity from Unit-III and Unit-VII would also come. Then the launch momentum should pick up in FY'18 vis-à-vis FY'17?

P.V. Ramaprasad Reddy: Yes.

Kumar Saurabh: How should we look at your EBITDA margins going forward in FY'18? I think adjusted EBITDA margins would be roughly around 21% or little above that for the quarter. Going forward in FY'18, given the fact that your R&D expense should also go up from the current levels, how should we look at the margins?

N. Govindarajan: Let me first answer the R&D part. Please remember the fact that as a percentage we do not expect it to drastically change for a simple reason because our top line is still growing. So whatever incremental expenses which comes up, because of the top line growth, it would not tectonically shift in terms of a percentage. Having said that, we continue to see growth in terms of the business

and we expect the EBITDA margin to at least maintain and grow from here and we do not see the EBITDA margin further coming down, it will only improve from here on year-on-year. One underlying statement I would like to make is that it cannot be compared on a sequential quarter or a quarter-to-quarter basis, on a year-on-year we are fairly confident about growth even in EBITDA.

Moderator: Thank you. The next question is from the line of Neha Manpuria from JP Morgan. Please go ahead.

Neha Manpuria: Could you give us a little color on what the one-offs were in this quarter, you mentioned in your opening comments of inventory write-off and other exceptional items in EBITDA?

Santhanam Subramanian: The one-offs are related to various inventory adjustments which we have done at the end of the year and we have also booked certain pre-acquisition expenses related to Actavis business.

Neha Manpuria: How much would this be? I am assuming the inventory write-off would be reflected in our cost of sales.

Santhanam Subramanian: No. It is reflected in the other expenses. So, all put together will be around Rs.50 crores plus

P.V. Ramaprasad Reddy: This inventory write-off majorly related to the stock which we received from Actavis at the time of acquisition. Those stocks are getting expired and a majority of that were written-offs.

Neha Manpuria: So they are actually related to Europe and not to the US?

P.V. Ramaprasad Reddy: Major is Europe and that to the stocks we got from Actavis

Neha Manpuria: For the US business, I understand launches should increase going into FY'18. Could we break up as to what we are seeing in new approvals and new launches in Oral Solids and Injectable please?

N. Govindarajan: Injectable would still grow much faster than the rest of the portfolio. Rest of the breakup probably we can take it offline as we progress.

Moderator: Thank you. The next question is from the line of Anubhav Agarwal from Credit Suisse. Please go ahead.

Anubhav Agarwal: One question is on this McKesson-Walmart consortium. Have you seen the impact of this in this quarter or will that largely reflect in the June quarter?

P.V. Ramaprasad Reddy: Our share with the Walmart is very limited. McKesson-Walmart deal will come as a net benefit in long run. So we are not foreseeing any big difference as far as Aurobindo is concerned about

this merger. We are hoping some benefit because recently Walmart-McKesson tender was completed and we can add some more products for the McKesson

Anubhav Agarwal: On the Injectable business, is there any impact of channel consolidation or this is largely on the oral business only?

P.V. Ramaprasad Reddy: As of today, there is no consolidation issues in Injectable business and in the oral side, now we feel majority of the consolidation is over.

Anubhav Agarwal: Just one question on the OTC franchise for us. We will be launching this Mucinex DM pretty soon. What about the other two forms the Mucinex – have we filed for the other two forms as well or the only file to Mucinex DM?

P.V. Ramaprasad Reddy: We filed only Mucinex DM.

Anubhav Agarwal: Why would that be the case because the other two strengths are also having good market size?

P.V. Ramaprasad Reddy: We are working on that; one going to be filed and another is under development.

Moderator: Thank you. The next question is from the line of Ranjit Kapadia from Centrum Broking. Please go ahead.

Ranjit Kapadia: My question relates to Oncology segment. How many products are there currently and how many products we pushed over the next two, three years, and whether this will become 10% of the Formulations business in future?

P.V. Ramaprasad Reddy: Our Oncology business has come through the joint venture where we have around 68% share and our filings we already filed around 2 products and we are hoping before March 2018 we will file at least 15-17 products and we have FDA audit for the facility in next month.

Ranjit Kapadia: Any update on Controlled Substances business, because that has not been in the part of the Formulations business?

P.V. Ramaprasad Reddy: Controlled Substance is part of Aurobindo USA sales.

Ranjit Kapadia: Natrol products, are we planning to launch in other markets or we are restricting to US only?

N. Govindarajan: We will be spreading to international markets as well, in fact, we are right now looking at even hiring somebody based out of Europe and cover the rest of the US markets. This is the process where it will take some time, because country-by-country the registration has to go through. In certain countries which we are working through and you would start seeing the improvement of international sales towards the second half of next financial year. By that time, we would have launched in few markets.

Moderator: Thank you. The next question is from the line of Karthik Mehta from Deutsche Bank. Please go ahead.

Karthik Mehta: When you say that on the top line in the US, you will be able to grow in FY'18. What is the YoY erosion that you run with when you make that…?

N. Govindarajan: I would like to clarify on erosion, we do not expect this erosion to be forever. We are considering that to be there for the next four quarters at the current level and on that basis we are saying. Our focus on growth is more on bottom line rather than purely focusing on top line.

Karthik Mehta: When we hear what your Indian peers talk about, we do not hear them talking about the end of erosion. So what makes you believe that we are almost at the end, and if that is the case, then we have a fair amount of launches in injectables lined up which are there for FY'18?

N. Govindarajan: We are not saying that it is ending in the next four quarters. I am only saying that it would not continue forever. It might take another six, seven quarters and then after that it has to taper down, our dependence on any single product is very minimal, and so it is not easy to compare us with any other institution.

Moderator: Thank you. The next question is from the line of Nishit Shah from Ambika Fincap. Please go ahead.

Nishit Shah: If you can give some color on the progress on the Microsphere side, and then on Dermatology and Inhaler side?

P.V. Ramaprasad Reddy: We do not want to tell about the specific products. But we are sure we will file at least three products. Our plan is to file before end '17-18 or early '18-19. As far as the inhalers are concerned, we are not in DPI, we are in MDI. We may not file in FY17-18. In FY18-19, we are going to file at least two-three products in Derma and MDI.

Nishit Shah: On the Inhaler side sir… on the Dermatology?

P.V. Ramaprasad Reddy: Both Derma and MDI product will be manufactured at US North Carolina manufacturing facility. We are going to take the exhibit batches at least to ten Derma products and one MDI Inhaler in this year. Only thing is we are not working on DPI.

Nishit Shah: On your Vaccine side, would you like to add some color? I believe you started construction of the plant on that is what in the last con call you had mentioned on.

N. Govindarajan: Yes, we are likely to start is what we had said. The development is nearing the completion cycle and we have to make the batches for Phase-1 and then subsequently go to the next phase. In fact, we should start the construction in the next few months.

Nishit Shah: Govind, would you like to give some color on the Biosimilars, when those in-licensed products you are going to start the clinical trial process?

N. Govindarajan: Originally, we had licensed four molecules and then subsequently now we have licensed the fifth molecule as well. As far as the clinical trials are concerned, our Phase-1 would start by next year and typically it should take around 2-years in terms of completing both the phases. So we are talking about 2018 & 2019 and the filing should happen by beginning of '2020.

Moderator: Thank you. The next question is from the line of Chirag Jain, he is an individual investor. Please go ahead.

Chirag Jain: My question is regarding your tentative approval. When your tentative approvals would start coming in, in the actual sales?

P.V. Ramaprasad Reddy: We have 28 tentative approvals in US products. These 28 products can be launched based on their patent expiry and court cases with innovator companies. So it may be from this year onwards to next five years.

Chirag Jain: There was a news regarding Hyderabad FDA facility which was recently inspected. So what is the status on that if you could highlight?

N. Govindarajan: Any given quarter, there would always be one of the facilities getting inspected. So there are few facilities which have been inspected. So the recent inspection which had happened was in Unit-X in Naidupet and the inspection has gone without any 483 and the previously Unit-IV was inspected. There are a few inspections where we are awaiting the EIR

P.V. Ramaprasad Reddy: Last three months, four units were inspected.

Moderator: Thank you. The next question is from the line of Girish Bakhru from HSBC. Please go ahead.

Girish Bakhru: What is the CAPEX guidance for FY'18?

N. Govindarajan: Barring Vaccine and Biosimilar, it would be around US$120 million

Girish Bakhru: So this is US$120 million, it is a significant fall, you are maintaining that deduction in…?

N. Govindarajan: You have to also consider that US$120 million along with Biosimilar and Vaccine. That would get added. If we remember, we had committed in the past we would like to bring capex down at least for a year or two in terms of looking at cash flow. That is what we are looking at. But having said that, CAPEX would be there adding the Biosimilar and Vaccine.

Girish Bakhru: Is there any TAD issued on Triumeq filing, on the DTG combination drug?

N. Govindarajan: DTG combination we have the TAD. What I remember is around August timeline

Girish Bakhru: Any change in assessment given that I think there are increasing number of trials involving DTG, would you think this market will significantly take off or what is your broad assessment now?

N. Govindarajan: As far as the combination is concerned, we have to wait and watch. But, I can only tell you that from a technical viewpoint, there is a high level of optimism because as you would have observed that we have already received the approval for the plain and in fact plain has taken off well better than what our folks had anticipated.

Girish Bakhru: So from the pending, if I see you have launched 30 products in Injectables, pending 10 are still not launched and there are 35 under review. Will this significant number of pickup in FY'18-19?

N. Govindarajan: It is our belief.

Girish Bakhru: You do not see that 483 particularly slowing down the approvals, right?

N. Govindarajan: That is not something which we would be able to comment in terms of the regulatory inspections outcome. We have responded and we have to await till the outcome is concluded by the regulator.

Moderator: Thank you. The next question is from the line of Surjeet Pal from Prabhudas Lilladhar. Please go ahead.

Surjeet Pal: Could you please tell me this inventory adjustment which belongs to Actavis three years back when you acquired, what could be the reason for carrying that in the inventory for so many years?

P.V. Ramaprasad Reddy: Actavis stocks have three-four-years expiry time. So those stocks are expiring now. Whatever we can sell maximum, we have sold. Some maybe go to expiry. Now we have a better control on what exactly we are going to sell and what we are going to supply. So it will be there to some extent but not this much extent.

Surjeet Pal: So you have not actually provisioned the whole amount whatever has been left over?

P.V. Ramaprasad Reddy: Yes, whatever is expiring, we started provisioning once in six months.

Surjeet Pal: Actually I did not follow that guidance about Onco and Respiratory. When did you say that you could see the light of your pipeline of Oncology in US market?

P.V. Ramaprasad Reddy: This year FY17-18 we will be filing 15-17 products and we can get some 4-5-products in hormonal and oncology injections. We have an audit in July end or August beginning and we hope definitely we will sell from that unit this year end.

Surjeet Pal: So this year-end you will get at least three-four approvals, that is your expectation?

P.V. Ramaprasad Reddy: Yes, filings would be around 17

Surjeet Pal: I think you guys have already filed Fondaparinux and we know that Fonda has an issue of yield. Even if I assume that you get approval in say August, do you think it will take much longer time in terms of introduction of that product in US market? Because we know Dr. Reddy to be specific when he got approval, he took around two, three months to introduce that product in US because production process is pretty slow.

N. Govindarajan: For us the regulatory approval itself should take some more time and we had to wait and watch it even though we have TAD. Sometimes on TAD we can receive further queries as well. We have a couple of more queries which we need to closed out. We do not expect the approval in the next couple of months, it would take some more time.

Moderator: Thank you. The next question is from the line of Bino Pathiparampil from SBI CAP Securities. Please go ahead.

Bino Pathiparampil: Is there any update on the Department of Justice case regarding price fixing in Generics?

N. Govindarajan: It is a status quo, there are no further updates at this juncture.

Bino Pathiparampil: Have you received any new subpoena or have any official visited your office or anything?

N. Govindarajan: Whatever has happened was happened in the past, that subpoena was issued and we had responded and we had met them. Subsequently, there is no fresh movement on that.

Bino Pathiparampil: I see that your receivables have come down sharply this year over last couple of years. What would have left to that?

Santhanam Subramanian: You should add the receivables which we have put it on for non-recourse factoring and we have not drawn. So you need to take another Rs.739 crores also to the receivables. It is appearing as part of the current assets schedule.

Bino Pathiparampil: So that should be taken in receivables that you are saying?

Santhanam Subramanian: Yes, that should be taken as receivables.

N. Govindarajan: But it is a non-recourse factoring. I would like to clarify just for the benefit of everyone.

Bino Pathiparampil: A general update on how the margin expansion story in Europe is playing out. Is it as per your plans, better than that or slightly below your targets?

Sanjeev Dani: When we took over, it was -10% EBITDA. We moved into the PAT positive last year and this year it is as per the expectation. India switches are also helping and going forward we think that it will further improve.

Moderator: Thank you. The next question is from the line of Sumit Singhania from IDFC Securities. Please go ahead.

Nitin: Nitin here from IDFC for Sumit. On the US business, with the way the market has really shaped up over the last few quarters and our strong focus on the US, are there any tweaks in the strategy that we are evaluating?

N. Govindarajan: As of now, we don't see the need for a mid-course correction. As I had explained earlier also that our model is a bit unique and our dependence on any specific product is minimal. If you really look at the portfolio and if you look at the top-20 or top-30 in terms of the percentage, the dependence would be much-much different when you compare with other institutions. Having said that our strategy still we believe is intact in terms of delivering the growth.

Nitin: In that context, just sort of taking that point forward, can you help us understand a little bit in terms of what exactly happen in Q4 the fact that we did have some launches. Was there any specific products where there is a heightened price erosion due to account for or it was a like a broad-based portfolio erosion?

N. Govindarajan: No, it was again a few products were more specific. Having said that, you also have to remember the important launches have happened towards the end of the quarter. So that also did not help us.

Nitin: In terms of some of the larger pending injectables that you had, Vancomycin and Meropenem and the others, what are the launch sort of timeline, some of the approved injectable products which are there for us?

N. Govindarajan: Meropenem has been already launched and as far as Vancomycin is concerned, it would take another few more months before we could go for that product. As far as injectable portfolio is concerned, year as a whole, we still have some decent launches which would really maintain the growth momentum.

Moderator: Thank you. The next question is from the line of Chetan Shah from Jeet Capital. Please go ahead.

Chetan Shah: I just wanted to understand a little about the price erosion in the US market especially in the third and the fourth quarter? If you can just throw some light that is it something which is kind of a trend going forward or you think that we have seen the worst of the price erosion happen and do you think it will be normalized in years to come?

N. Govindarajan: My suggestion is since we had talked about it two-three occasions, we will take it offline. What we have said is yes, there is erosion but as year as a whole we still projected that we would be able to grow the bottom line.

Moderator: Thank you. The next question is from the line of Rakesh Jhunjhunwala from Rare Enterprises. Please go ahead.

Rakesh Jhunjhunwala: My question is Generis acquisition. When it is going to be consolidated?

Santhanam Subramanian: Generis will be consolidated in the June quarter. The acquisition has been closed in April.

Rakesh Jhunjhunwala: What is the EBITDA of the company last year?

Sanjeev Dani: It is about 20%, around €12.5-to-€13 million p.a. basis.

Rakesh Jhunjhunwala: What vaccine you are developing as vaccine is a vast area?

N. Govindarajan: We are developing pneumococcal vaccine.

Rakesh Jhunjhunwala: Then you will intend to increase the portfolio?

N. Govindarajan: This is a very high end of this particular product portfolio. We can always add the rest of it as we progress.

Rakesh Jhunjhunwala: What is the market size?

N. Govindarajan: That is running into a few billion dollars.

Rakesh Jhunjhunwala: Lot of competitors or not many?

N. Govindarajan: At this juncture, it is limited, but to the best of our knowledge, at least two-three more people are also working.

Rakesh Jhunjhunwala: You think you can file in a year or so?

N. Govindarajan: It would take two years to file, because we need to run the batches at the manufacturing facility which has to be created, so you take it as 18-24 months before we can file.

Rakesh Jhunjhunwala: Do you not think this price erosion is now reaching a climax because everywhere I hear only price erosion?

P.V. Ramaprasad Reddy: Price erosion is going to stay as more and more approvals are coming. Only fittest will survive. The companies having the broad ANDA portfolio will survive. Price erosion can be between 2% and 12% it all depends. There is no authenticated number, what is the base business erosion and

the new product erosion. But as everyone indicated, it is around 9-10%. There is no much room in future for erosion. It will slowly taper down.

Rakesh Jhunjhunwala: You are also saying what I am saying that everybody talking so much and that is getting consolidated, but some point even players will go out, no? What happened to the derma field? The two bit was $5 became $1 and then people withdrew and they become $15. So do you not think price erosion will lead to withdrawal of competition also or the market will adjust it?

N. Govindarajan: As Mr. Reddy was explaining, in the base business if you take the same set of products, the margins are not so much for people to keep reducing the price forever. So it can happen for next few more quarters. As you rightly said, the competition would start shrinking. But whether that would lead to price improvement? We cannot generalize it. We need to wait and watch.

Moderator: Thank you. The next question is from the line of Nimesh Mehta from Research Delta Advisors.

Nimesh Mehta: I just missed the R&D increase part. So what is the R&D increase?

N. Govindarajan: When the Biosimilar and the Depot Injection clinical trial happens, which can happen together for a couple of years, R&D expenses can reach around 6-7%. If you keep the top line constant it could be even more. But you have to remember the fact that the top line is also growing. It would take another two years before it reaches that level and it will increase progressively, it will not be a sudden jump in terms of only one year. Today, we are at 4%, next year it could be 5%, then it could be reaching 6%, but then 6% is not forever, it again can come down because when the top line keeps increasing, it will not be staying at that level forever.

Nimesh Mehta: We expect margin to improve despite the increase in R&D, right?

N. Govindarajan: Yes

Moderator: Thank you. The next question is from the line of Ranveer Singh from Systematix Shares. Please go ahead.

Ranveer Singh: Just had a few clarification; in CAPEX you said US$120 million apart from Vaccine and Biosimilar. So Vaccine and Biosimilar taking together how much it could be?

N. Govindarajan: We are working on it. We have better clarity on Biosimilar, that can add to another say Rs.150-200 crores. As far as Vaccine is concerned, we need to conclude that budget. After that we will have complete clarity on that. Barring those two, US$120 million.

Ranveer Singh: But CAPEX related to that Vaccine and Biosimilar would be in this year only?

N. Govindarajan: Majority would start this year, some would flow into the next year as well.

Ranveer Singh: If I heard correctly, you said that one-off which is there in this quarter, you have more inventory to be written-off for next six months. That is what you said?

N. Govindarajan: No, the explanation was given for what had happened in the last quarter. So what was also told is that for the future is it will not be at the same tone.

Ranveer Singh: Yes, my concern is whether next quarter will see any part of inventory to be written off or it has already been cleaned now?

N. Govindarajan: It has already been cleaned. Some part can come but it will not be significant to the extent of last quarter was what was explained.

Ranveer Singh: If you could give the number about the ANDA approved, not launched yet?

P.V. Ramaprasad Reddy: Approved, but not launched would be around 26 products and tentative approvals are 28 and under review is 115.

Ranveer Singh: On Oncology, you said three-four approvals you are expecting in this year?

P.V. Ramaprasad Reddy: We expect to file around 16 or 17 including hormonal injection, 3-4 approvals before end of March.

Ranveer Singh: A question has been discussed repeatedly about price erosion. But just one query that price erosion going to stay. Question is that for base business how much erosion will sustain because after a limit, nobody would afford to sell at a particular price. So that way we believe there should be some limit, some cap somewhere, what is your thought on this?

N. Govindarajan: It could be more generalized is what I would say, as it was explained, we do not expect this to be sustaining forever in terms of the erosion. In a normal generic business, you will always see like some erosion, that will continue. Instead of assigning a number, right now whatever we are seeing the increased erosion would taper off over the next 6-7-quarters.

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

Vishal Manchanda: Do you think US drug prices can go as low as prices in Europe?

N. Govindarajan: We cannot be generalizing so much, because the markets are completely different.

P.V. Ramaprasad Reddy: In Europe also, products with 15-20% EBITDA are there, in US previously there were 28-30% EBITDA. More or less at some level it would match. Sometimes in European some countries prices are better than US. That is my personal feeling. Always US will have 2-3% more EBITDA margins than Europe.

Vishal Manchanda: If we look at some of the most products, there is a lot of competition greater than ten players and have been generic since a long time. So, prices in these products would be similar to the European sizes or they would still be higher?

P.V. Ramaprasad Reddy: Very difficult. In Europe, multiple models are there. Definitely it is better than German tenders. But definitely it is slightly less than like Spain or France. It all depends. We cannot generalize.

Moderator: Thank you. The next question is from the line of Chandra Mouli from Goldman Sachs. Please go ahead.

Chandra Mouli: I have a clarification on the rate of erosion that you had mentioned over the next 3, 4-quarters that you're modeling. So 7-8% that was mentioned is it and annual erosion that you are mentioning or is it a quarterly 7% to 8%?

N. Govindarajan: Annual erosion we have mentioned.

P. V. Ramaprasad Reddy: We told whatever happened in '16-17 not indicated about '17-18. We are not sure how much is going to be in '17-18.

Chandra Mouli: My question was when you had given a projection, what do you have in mind in terms of your model. So we are saying that I think around that number in spite of that we expect it should be better off is the assumption. You are right in terms of we cannot have a specific number for next year.

P.V. Ramaprasad Reddy: But the erosion of 3-4% is there since 5-years on the base product.

N. Govindarajan: That is true. Unfortunately now it is seen as increased erosion is where the concern comes up.

Moderator: Thank you. The next question is from the line of Jatin Kotian from Emkay Global. Please go ahead.

Jatin Kotian: Just wanted to clarify, you mentioned that the jump in other expenditure sequentially or quarter-on-quarter, of that about Rs.50 crores was the exceptional towards inventory and other things. Is that right?

N. Govindarajan: That is right, Rs.50 crores plus.

Moderator: Thank you. The next question is from the line of Harith Ahmed from Spark Capital. Please go ahead.

Harith Ahmed: Can you help us understand the observations at Unit-IV and nature of these observations and if you have received any approvals from this facility after the inspection?

N. Govindarajan: As far as observations are concerned, we have mentioned earlier also it is not related to any data integrity, these are more procedural is what we had commented. Having said that, we have not received any new product approval from that site after that. As we progress, we will be able to assess that.

P.V. Ramaprasad Reddy: We have given reply a week back, due date 15-days after audit. We have to see one or two months.

Harith Ahmed: So you do not expect an escalation of this?

P.V. Ramaprasad Reddy: Yes, that is what we believe.

Harith Ahmed: Second question is on your net debt reduction. I see roughly $200 million of net debt reduction in FY'17 and some of this is on the back of the receivables factoring you did. So can you help us understand the net debt reduction on account of receivables factoring and a breakup between the net debt reduction on account of receivables factoring and the net reduction that may have happened from your own free cash generation?

Santhanam Subramanian: The factoring is a non-recourse, which is predominantly to take care of the exceptional outflow on account of higher chargebacks and hence should not be taken into cognizance. US$ 200 million is the net debt reduction during the year. This has been explained in detail in the August concall also.

Harith Ahmed: The debtor days that we see now will be relevance that we should project?

Santhanam Subramanian: Yes, it will be like this level.

Moderator: Thank you. The next question is from the line of Purvi Shah from Sharekhan. Please go ahead.

Purvi Shah: You said that we can maintain the EBITDA margins despite the pricing pressure you are seeing. But have you also factored in the appreciating rupee scenario into this as R&D expenses would also be increasing?

N. Govindarajan: On a constant currency, I would consider this. On an annualized basis it is even with the increased R&D. If there are some surprises, then accordingly we need to leave it at that number. So just I am saying on a constant currency.

Purvi Shah: Sir, the other thing is that on the tax side front for the year has been around 25-26%. So do we see the same range going forward as well?

Santhanam Subramanian: We believe so.

Moderator: Thank you. The next question is from the line of Kumar Saurabh from Motilal Oswal Securities. Please go ahead.

Kumar Saurabh: Three new plants are getting commissioned in late FY'17 and FY'18. So are we getting any kind of tax benefit because of that tax rates can actually come down in FY'18?

Santhanam Subramanian: Two facilities are located in the SEZs. But first year we may not be seeing a great tax benefit but going forward we will be able to see.

N. Govindarajan: You need to give some time in terms of the transfer of products and approval.

Kumar Saurabh: But is it not a fair sense that FY'17 is like a pretax rate and actually from going forward tax rate actually will come down only?

Santhanam Subramanian: In FY'17, we had a lot of commissioning happened and availed the tax benefit. Going forward it will always be around 27-28% level.

Moderator: Thank you. The next question is from the line of Surya Patra from Phillip Capital. Please go ahead.

Surya Patra: Just a clarification; this Aurolife for the year that you have indicated in the opening remarks, was that because of the capacity expansion or it is because of the new tender addition or what has related to that kind of approvals and what is the outlook that we are giving sir?

N. Govindarajan: It is a combination of both.

Surya Patra: Going ahead, it is a capacity driven business I believe. So is that capacity more that is there or what would be the outlook for that stream?

N. Govindarajan: We have already expanded that capacity and that is going to help us as we progress as well.

Surya Patra: On the Injectable front, how many active products are there in the market and what is per product revenue that we are currently generating sir, and when can we see meaningful improvement there?

P.V. Ramaprasad Reddy: Injections as on today approved is 48 products and filed to be approved is 28 products, tentative approval are 2.

Surya Patra: All 48 are there in the market sir and we must be doing revenue around …?

P.V. Ramaprasad Reddy: At least 10 products is not there in the market. Few for the capacity reasons and few for the market pricing reasons. Majority will be launched except few market reasons products.

Surya Patra: So that means we are currently US$3 million kind of revenue per product that we are generating. So do you see kind of meaningful upgrade there in the coming year?

P.V. Ramaprasad Reddy: We have a good budget this year.

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

P Srihari: Firstly, on the other expenditure part, it has gone up by more than Rs.100 crores sequentially. When I adjust Rs.50 crores, still the incremental is quite significant. Can you please explain that? Secondly, your gross margins have expanded significantly vis-à-vis any other quarter for the year. So can you please explain that as well?

Santhanam Subramanian: The other expenses we have explained in detail earlier. It has gone up by about Rs.100 crores. Out of that, around Rs.50 crores will be one-off. But the balance Rs.50 crores is on account of increase in certain sales related expenses. Some part maybe recurring and some part may not be recurring.

P Srihari: So what should one consider is the regular run rate because it has gone up by nearly 500 basis points sequentially?

Santhanam Subramanian: We are not giving any guidance but our view is based on that is something like 50 crore is one-off item, so you can remove it and balance itself a projection we are doing.

P Srihari: The gross margin you talked about, has improved this quarter because of the geographic mix and the business segment mix which came very favorably and that has helped to improve the gross margin percentage this quarter. Which geography in particular?

Santhanam Subramanian: The US business percentage has moved up by 1%, the Europe also has done well in terms of shifting the products to India and ARV business slightly dropped in the percentage. So these are various factors which have really helped to improve the gross margin this quarter.

P Srihari: Can I get the share of Oral Solids in your US business?

N. Govindarajan: It would be around 70-75%.

Moderator: Thank you. The next question is from the line of Charulata Gaidhani from Dalal & Broacha. Please go ahead.

Charulata Gaidhani: I wanted to ask regarding the emerging markets growth of 20%. In which geography does this growth pertain to?

Sanjeev Dani: The growth has come from almost all geographies, including Africa, Middle East, Canada and LATAM.

Charulata Gaidhani: How many EIRs are pending from US FDA?

N. Govindarajan: If you really look at the EIR including for no 483s issued, it could be around five to six.

P.V. Ramaprasad Reddy: Yes, last three months four audits and before that one.

N. Govindarajan: Unit 11 also has not been received till now.

Moderator: Thank you. Ladies and gentlemen, due to time constraints, that was the last question. I now hand the conference over to Mr. Krishna Kiran for closing comments.

Krishna Kiran: Thank you, all for joining us on the call. If you have any questions unanswered, please feel free to keep touch in with investor relations. The transcript of this call will be uploaded our on our website, www.aurobindo.com in due course.

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