Aurobindo Pharma Limited's
Business Update Conference Call

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	MR. ARVIND VASUDEVA – CEO
	MR. V MURALIDHARAN – SVP, BUSINESS DEVELOPMENT - EU OPERATIONS
	MR. SUDHIR SINGHI – CFO
MODERATOR	**MR. T. ROYCHOUDHURY – INVESTOR RELATIONS**

Moderator Ladies and gentlemen, good day and welcome to the Aurobindo Pharma Limited's Business Update Conference Call. As a reminder, all participant lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference, please signal an operator by pressing '*' then '0' on your touchtone 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. Roy Choudhury Thank you Inba. Hello and welcome everyone to the Aurobindo Pharma's Conference Call to discuss the announcement made on 18th January 2014 pertaining to the 'Acquisition of the Western European Operations of Actavis' in 7 countries. I am Roy handling the Investor Relations of Aurobindo Pharma and with me we have today, the senior management of the company represented by Mr. N. Govindarajan – Managing Director; Mr. Arvind Vasudeva – CEO; Mr. V Muralidharan – SVP Business Development, European operations, and Mr. Sudhir Singhi – CFO. We will begin the 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 assertions on our future business development and economic performance. While these forward-looking statements represent our judgment and future expectations concerning the development of our business, number of risks, uncertainties, and other important factors may cause actual developments and the results to differ materially from our expectations. Aurobindo Pharma undertakes no obligations to publicly revise any forward-looking statement to reflect future events of the concern. With that please let me turn the call over to Mr. Govindarajan for his opening remarks.

N. Govindarajan Thank you, Roy. Good evening everyone and thank you for joining us today. We are excited about the announcement of bid that we made for acquiring West European Operations of Actavis. As we maintained in every previous earnings call of ours that Aurobindo is constantly looking at combining both organic as well as inorganic growth, the inorganic being more focused on the twin principles of technology or market access. The current bid we made comes after several months of careful consideration of various other opportunities. The West European opportunity of Actavis turned out to be the most relevant in terms of market access and it soon became very clear to us that this is an opportunity which Aurobindo must pursue and achieve. The end result of four-month long efforts was the binding bid we made. With several strategic efforts taken in the last two years in strengthening of the leadership team at Aurobindo we were confident that we can now foray into enhancing our market access into markets where we are not dominantly present. This is possible today due to the fact that we created distinct SBUs with clear accountability and a leader heading it. Following the repayment of our FCCB in full our board set us the principle of having a prudential capital and debt structure to be followed as a golden principle coupled with controlled CAPEX allocations. Aurobindo today is a company with well-structured systems and standards and following discipline approaches to growth and adhering to set principles. The timing of this bid was also well planned coinciding with the cash flow operations coupled with optimum cash outflow for the bid. Further, it was also well planned not to be investing for acquiring manufacturing facilities in European destinations.

Let me now briefly touch upon the salient details of the transaction. We have bid to acquire West European Commercial Operations of Actavis which currently has estimated net sales of €320 million for the calendar year ended 2013, with 10% year-on-year growth. Actavis is a NYSE listed company having global operations. We will be acquiring relevant personnel, commercial infrastructure about 1200 existing products and another 200 pipeline products, relevant marketing authorizations and dossier licenses. This proposed acquisition will give us an entry into newer markets like France, Belgium, and Italy, and strengthen our presence in Germany, Netherlands, Spain and Portugal. In most of these markets the frontline work force is well focused on retail market as against our predominant focus of tender market thereby adding channel strength. We will be acquiring a strong well-established and longstanding brand known as Arrow Generiques. The proposed acquisition will perfectly complement in a timely manner, launch of our own injectable to the readily available hospital sales infrastructure that comes with this acquisition. With this proposed transaction we expect to be in the top 10 position in key Western European Generic markets. The bid also complements us in many respects like enhancing our European presence; the transaction not creating any additional debt profile to Aurobindo and acquiring businesses capable of self-funding on its working capital cycle; readymade frontline infrastructure which otherwise would have taken longer time to create organically; better geographical mix in our formulation sales between North America and European continent thereby providing required diversity in our revenue mix; leveraging our injectable, oncology, hormone, peptide and OTC portfolios; continuing strong partnership with Actavis in our European growth endeavor by way of long-term supply agreement with flexible changeover options for in-house manufacturing. We strongly believe with all of the above complementary synergies this acquisition will significantly enhance shareholder value in the near and medium term. We strongly feel that this is the right transaction for Aurobindo and the timing is also very perfect.

As you may be aware that we have uploaded a 'Presentation' about the bid details on our website this morning, which you all may have gone through in detail by this time.

Now, I open up the floor for Q&A. We will appreciate if participants can restrict their questions exclusively relating to the acquisition transaction. We are constrained not to answer any questions related to one of the closing conditions of employee consultations due to legal restrictions placed upon us. Further, we would also be constrained not to answer any questions relating to quarterly financial results which are due to be declared in a few weeks for which a separate call will follow after the announcement of results. We will greatly appreciate if you all respect our constraints and restrict your questions exclusively related to the bid transaction please. Thank you.

Moderator Thank you very much Sir. Ladies and Gentlemen, we will now begin the question-and-answer session. Our first question is from Ashish Rathi of Emkay Global. Please go ahead.

Ashish Rathi Sir, if our understanding was correct, we were seeing a very good operational run for the company and we were in the middle of a debt repayment cycle, suddenly we have done this acquisition where we have to pay $40-45 million. So do you think the same could have been avoided at this stage considering our debt and cash flow profile? Also if you could help us understand is there any change in the debt repayment plan of around $50-60 million each year going ahead?

Sudhir Singhi During the year whatever the debt obligations are there, as you are aware, we have repaid ahead to the plan; so up to Q2, we have repaid about $65 million of debt obligation and there is no fixed maturity date payable during the year '13-14, and ECB amount is payable over a period of '14-15 to '18-19. Hence, there is no immediate debt obligation for the company. As you are aware, from the half year results the company is in excellent growth mode in top line and EBITDA. And this acquisition as you said, around $40-45 million of outlay, the headline consideration declared is €30 million, which will be funded through internal accruals, no further additional debt would be there for this consideration amount.

Ashish Rathi I agree. In terms of debt repayment, you said that no repayment schedule is there from 2014-15 to 2018-19 it is there, but still we were targeting an aggressive debt repayment, is it correct?

Sudhir Singhi There are two components of debt. One is working capital, which is generally available to the company against stock and debtors, which we earn in dollars and we avail borrowing in dollars, and is available at a very low cost. Second thing, as you know RBI stipulation, the ECB cannot be repaid, and is to be payable on the fixed maturity date. Hence, the pre-payments will not work in the external commercial borrowings and is a fixed liability till its maturity.

Ashish Rathi Secondly, on this contract where we have done, we are looking to do some site transfers or maybe a manufacturing site backward integration towards India, please correct me if I am wrong, but some of the dossiers and licenses have a manufacturing site binding obligations when they are approved, is this going to be any kind of interest for us in terms of backward integration?

Arvind Vasudeva Site transfer can be done as long you follow the regulatory requirement. There is no restrain in moving a site. Whatever site is approved, we can have additional site through the process, which the regulator wants. So additional site can be added.

Ashish Rathi How much time does that take in terms of additional site?

Arvind Vasudeva It can take about 12-18 months.

Ashish Rathi Lastly on pricing concern, on the European markets in general, because these are very difficult markets to be, because of margins and tender business and whole pricing bids. So, will this lead to sort of an EBITDA margin pressure for the company, is that a fair assumption?

Arvind Vasudeva I think as we have talked about the revenue part, €30 million, we estimate, as of December '13, there could be a loss closer to about €20 million, but we know the whole cost structure, the internal COGS, we are confident with the action taken by Actavis in the last six months and product mix between generics and tenders, there will be margin improvement over the next 12 months time. At the same time, we also have a good number of products which are overlapping with Actavis and some of them have a lower CG profile, that also will add up in terms of improving margin expansion and then we look at site variation after 18 months time and that is the third phase of cost reduction and we are confident by second year end, we should be able to break even in this business standalone.

Ashish Rathi But 20% is what we were looking at somewhere for Aurobindo in terms of margins. Will that be taking a hit for FY15 and by how much, if you can have a sense?

N. Govindarajan I think we have certain other upsides if you really look at the next full year, so we are going to get benefit in terms of the increased sale in AuroMedics, and next year will also give us a benefit of full year of AuroSource providing enough profits, plus there are a couple of more opportunities which would give us enough benefits. So we would like to still go as close to the 20% maintaining that. So if at all if there is dip could be not more than say 2-3% on a short term basis, but we are still confident of recouping it in the next say, few quarters.

Moderator Thank you. Our next question is from Ranjit Kapadia of Centrum Broking. Please go ahead.

Ranjit Kapadia My first question relates to whether the business is positive at EBITDA level? And second thing we have said that this business is likely to grow at 10%. So I would like to know in which of the segments -- Generic, Prescription, OTC, Hospital Generic and Hospital? What are the growth rates in each segment?

Arvind Vasudeva As we have indicated that as of December '13, the EBITDA margin will be negative by about €20 million and in next two years time it will come to neutral that is break even. The larger part of the business is Generics Retail, followed by Hospital and followed by Tender. These are three large revenue generators in the portfolio. The smaller ones are branded generics which are innovator products, which are out of patent now and the smallest one is the OTC.

Ranjit Kapadia My second question relates to the Belgium market, which is just 1%, and 14 products are there. So what is plan for this market?

Arvind Vasudeva Belgium market currently is only branded generics of innovator products. We will look at developing other four parts of the business. As of now it is only one segment in Belgium.

Moderator Thank you. Our next question is from Sameer Baisiwala of Morgan Stanley. Please go ahead.

Sameer Baisiwala Is it possible to share any detail on this business on the balance sheet side, I understand this is part of a business from Actavis, but if there is a balance sheet of this business how would that look like in terms of fixed assets and in terms of debt if any?

Sudhir Singhi This business as we said in the opening remarks, we are acquiring the market authorizations, dossier licenses, people and the commercial infrastructure to run the business. So there is no fixed assets into that, and as such this business is virtually a debt-free, there is no short-term or long-term debt. The business is self-funded through the working capital cycle; the working capital cycle composition as you are aware constitutes the inventory, debtors and the creditors. Actavis on the closing, will leave a fairly good working capital including the cash equivalent to run the businesses smoothly going forward, and hence this business does not carry any liability and the fixed assets which are nominal in nature towards the commercial infrastructure to maintain the office outfit, there are no manufacturing facilities we are taking over with this business, hence there is no debt and there are no manufacturing facilities.

Sameer Baisiwala And second question, why is this business loss making as of now?

Arvind Vasudeva They have been in the expansion mode. Europe normally needs a minimum size of infrastructure and minimum revenue stream. So, as the scaling up of revenue happens it will turn into profitability as we said earlier. There is also high COGS base in certain areas, which I think our backward integration will help in bringing in high profitability. So these are a few reasons why it is currently loss making.

Sameer Baisiwala Do you see any immediate opportunity in terms of turning it profitable at EBITDA line either through price increase or taking out certain cost?

Arvind Vasudeva Price increases are not very easy in Europe. So COGS will be one important area to work on, and product mix between high profitable product and medium profitable product, and maybe easing out low profitable and loss-making products. So product mix and COGS will be major drivers here.

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

Prakash Agarwal On the financials, if you could share what kind of… we talked about that COGS is what we are looking to improve, what kind of gross margins currently this business would be at? And given the supply agreement with Actavis, what kind of improvement do we expect?

Arvind Vasudeva As of now the gross margin is in mid-30, but I think Actavis in last year has taken a lot of measures towards COGS reduction, product mix change, participating in profitable tenders, those work have been done, we can move towards through internal integration.

Prakash Agarwal But does the agreement also talk about that we would have to have supply agreement with Actavis? So by the time we shift our production base to India in the interim we would continue to take products from Actavis, right?

Arvind Vasudeva We have a supply agreement, which is comfortable and we have enough time to move to our places, and we have understanding with Actavis what we can do in terms of taking product in course.

Prakash Agarwal And in your view what is the potential of the business in terms of margin expansion? The first stage, as you said, improving product mix and using common products as a base, and the second would be the site transfers, so we are looking at four to five years from now. Would it actually go for double-digit kind of operating income or what is your sense on the business?

Arvind Vasudeva Like I said, we can move gross margin beyond 40 and I think we can reach operating income of double digits.

Prakash Agarwal With this do you think your CAPEX guidance with respect to investments of more formulations and API for Europe business would increase?

N. Govindarajan I think we had in the past also said, it would be in the range of like maximum Rs.400 crores. I think with the current cash scenario like we are comfortable with the Rs.400 crores number and we will review that as we progress in case if we have more cash available, we will decide upon that in terms of any additional further CAPEX which may be required.

Prakash Agarwal I understand COGS will definitely see improvement, but at the operating cost, do you see, like if there is a fixed part and the variable part. As we progress, in two to three years time, do you expect some improvement there as well, any specific focus area?

N. Govindarajan There will be improvement in that area.

Prakash Agarwal Just a couple of more, actually on 10% year-on-year growth what gives us visibility because largely it is a volume-based business. So do we see the market expanding or do we see more penetration from our side?

N. Govindarajan It is a combination of current molecule organic growth, launching of newer molecules, and also getting into higher value products which are hospital and specialty products. So it is a combination of volume, new products, and getting into high value products, which are injectables and specialty.

Prakash Agarwal Last question, as you said, injectables, what stage are we into the injectable phase for the Europe business, I understand we are currently ramping up the US piece; do we have the EU block ready for injectables, or how far we are?

N. Govindarajan I think the current facility can also serve the Europe, but depending on the need of the market in terms of the new products whatever we are going to expand, then we will also decide about the capacity expansion then.

Arvind Vasudeva The injectable will come from multiple steam, what Govind said is Unit IV, we also have Unit XII, Eugia which is our oncology and hormonal facility for injectables, and Auronext for Penems. So all four facilities will be able to give us products for this market.

Moderator Thank you. Our next question is from Arvind Bothra of Religare Capital Market. Please go ahead.

Arvind Bothra Just wanted to understand from the deal perspective, the supply agreement with Actavis, what does it entail actually -- is it only the supply relating the existing area of operations or you have a cross agreement to supply Actavis for other markets as well, just curious on that?

Arvind Vasudeva It is currently supply agreement of getting from Actavis the supply of products which they have been marketing that is the current arrangement that we have.

N. Govindarajan Apart from that we also supply something already like, we have an existing relationship as well.

Arvind Vasudeva We were supplying them a few products in the past and that continues anyway.

Arvind Bothra And since we talked about overlapping product portfolio along with the existing acquisitions which means site transfer for some of the products can happen much quicker than the rest. Do we have volume obligations to fulfill or we would be able to do the site transfer at the earliest for the existing overlapping products?

Arvind Vasudeva Because of the relationship with Actavis, we have flexibility to move as the market situation and business warrants.

N. Govindarajan Are you able to hear us?

Moderator Mr. Bothra, I am sorry, but we cannot hear you, clearly. I think we will move to our next question, maybe Mr. Bothra can back in the queue as there is no response coming in.

N. Govindarajan Please go ahead.

Moderator We will take the next question from Dhiresh Pathak of Goldman Sachs. Please go ahead.

Dhiresh Pathak What is the value of net current assets that will be transferred?

Arvind Vasudeva As you know the headline consideration is €30 million and depend upon the closing debt, the net current assets including the cash equivalents in the business would be more than €30 million.

Dhiresh Pathak You said gross margins of mid-30. Where Actavis is manufacturing these products?

Arvind Vasudeva Actavis is manufacturing on their own and also in-licensing from multiple manufacturers outside -- it is a combination of both.

Dhiresh Pathak Out of their own sites in Western Europe, Eastern Europe…?

Arvind Vasudeva In Europe, including Eastern Europe and Asia as well. They have multiple places, they have more than 30 sites, so I think a few of them are in Europe and a few of them are in Asia.

Arvind Vasudeva The main sites feeding are coming out of Iceland, Malta and also in Bulgaria and Jakarta, multiple sites.

N. Govindarajan Italy.

Dhiresh Pathak In terms of the manpower that you are taking on your books in your company, have you any pension obligations and other stuff involved?

N. Govindarajan There is, and that has been factored in the deal.

Dhiresh Pathak So, what is the unfunded or is it over-funded, that pension obligation that you are taking?

N. Govindarajan It is being adjusted to the consideration, which arrive, so adequately unfunded pension liability are being taken into the consideration, and the amount of the consideration what you declare is including that. On the closing date, in lieu of same, the net working capital assets including cash would be more than that.

Dhiresh Pathak What is the size of the pension asset pool?

Arvind Vasudeva It is difficult to comment, is being asserted, and it is a complex calculation. As you are aware about the matter, it is based on the actuarial valuation and the accounting policies being incorporated therein.

Moderator We will take our next question from Anil Shah of Birla Sun Life Mutual Fund. Please go ahead.

Mayank This is Mayank. Basically, I have two questions. First is that, how many people have come along with this deal, #1? An extension of that is that are we looking at any immediate cost rationalization from the employees cost front?

Arvind Vasudeva We indicated that 450 employees are currently part of the business, and we have talked about a disclaimer right in the beginning, so we will not be able to comment on that.

Anil Shah This is Anil here. So there could be some retrenchments that we are looking at possibly?

Arvind Vasudeva Please refer to the disclaimer, we will not refer to that please.

Anil Shah And second part was the Actavis, long term supply deal of the products. Under the terms of the deal will they be supplying at cost or cost plus basis?

Arvind Vasudeva It is agreed price that we have between us and Actavis.

Anil Shah At that cost or cost plus basis?

Arvind Vasudeva It is agreed price, so we cannot say anything beyond that please.

Moderator Thank you. Our next question is from Prashanth Nair of Citi. Please go ahead.

Prashanth Nair When is this likely to close?

N. Govindarajan We are expecting around 8-10 weeks approximately, Prashanth.

Prashanth Nair Apart from the consideration, would there be any incremental funding that you need to do in any form for this transaction?

Arvind Vasudeva Prima Facie we do not visualize it.

Prashanth Nair And any incremental CAPEX at the Aurobindo level that you will need to do to meet long term plans for this business?

N. Govindarajan Whatever numbers I have mentioned includes that, and any further expansion as I told you, we will review the cash flow and then decide in terms of further CAPEX. But as of now, like we are saying that approximately Rs.400 crores which will include whatever investment which is needed for this as well.

Moderator Thank you, our next question is from Rakesh Jhunjhunwala of Rare Enterprises. Please go ahead.

Rakesh Jhunjhunwala What I wanted to know is that, can there be some savings on the regulatory price? Can the regulatory work be shifted from Europe to India at the same way and what would be the approximate savings?

Arvind Vasudeva Regulatory costs are standard. What it will save will be primarily the regulatory work which can be done out of India.

Rakesh Jhunjhunwala Shifting out work from Europe to India, that should give a substantial savings, no?

N. Govindarajan Rakeshji, this is part of the particular restructuring aspects of it, so we may not be able to throw much light on that at this juncture please.

Moderator Our next question is from Saion Mukherjee of Nomura. Please go ahead.

Saion Mukherjee Sir, just wanted to have a clarification, you have acquired the entire Actavis front end operation in these 7 countries?

Arvind Vasudeva Yeah.

Saion Mukherjee You mentioned £20 million loss as your estimate of last year. How has been the trend like for this business -- has the loss been increasing? Coming down? Can you throw some light on how this has been panning out?

Arvind Vasudeva It has been decreasing over the years.

Saion Mukherjee The contract that you have with Actavis for material, is a large part of your raw material will come from Actavis or are there third-party suppliers?

Arvind Vasudeva Both -- there is Actavis supplies and there is third-party supplies as well.

Saion Mukherjee Can you just throw some light as to whether Actavis is a major part of the supplies or it will be the third-party?

Arvind Vasudeva Evenly distributed.

N. Govindarajan It gets evenly distributed.

Saion Mukherjee One last question, which is country specific, particularly to France and Germany, because these are the two big markets that you are acquiring. How has been the pricing trend, particularly in France, if you can highlight? I would assume that a large part of the losses would be from France. Will that be a right assessment to make?

N. Govindarajan I will request Murali to respond to that. Murali please?

V. Muralidharan France and Germany are, yes, as you rightly said, by far the most important critical high value markets for us. Germany has already turned much of it in their way, frequent tenders are being floated, but where Aurobindo has been successful, Actavis themselves have been successful. So we expect the combined might increase the portfolio, which is expected to give us substantial upside. In France, there has been some government initiated price cuts are being brought in, but that will not actually affect our operations, that will only to some extent be compensated through the market discounts that are going in. So we will strategize in such a manner but France still by far is the best high priced market. And Arrow Generiques is the brand which we are inheriting will provide us substantial upside there.

Saion Mukherjee So your operations in France is still not profitable?

V. Muralidharan Operations in France currently is still not profitable and that is Actavis. For Aurobindo France has been a target market wherein we have invested substantial amount of money towards building up our own basket of marketing authorizations. So already the Actavis range covers 90% of the top 100 in portfolio with Aurobindo's MAs coming in, we will be almost full in product mix, and also the substantial endorsing to hospital generics, so we expect to have the whole thing turned into our advantage.

Saion Mukherjee You mentioned about some price cuts in France which is being implemented. So can you just elaborate a bit as to what these changes are?

Arvind Vasudeva These are only just in the recent period it has started wherein obviously it is any government's initiative to bring down their overall healthcare spends where they depend on the pharma companies to part with some of their price top line. So this is in some market for turning tender way. Here they say they expect us to reduce on the top line.

Saion Mukherjee Can that be a major headwind for you to manage in case this escalates into something more significant?

Arvind Vasudeva The market dynamics and any successful player needs to rise up to the challenges. But as I said there are markets we would have observed in the last 6 years, how Germany turned in a different way and how generic companies have responded successful ones. So here is aggressive, ambitious organization, we are more than confident we will be able to live the challenge.

N. Govindarajan Like Murali said, most regulated markets will be under price pressure because of government burden of healthcare and I think most companies are prepared how to manage that.

Moderator Our next question is from Prakash Ramaseshan of Kotak Mahindra. Please go ahead.

Prakash Ramaseshan Govind, just trying to understand the transaction. You are paying more or less for £30 million of current assets and you are getting a whole lot of things along with that for free, but you get the burden of $450 million of turnover with a negative bottom line, you do not know how long that is going to take to repair that is a deal in crux?

Sudhir Singhi The EBITDA around is negative €20 million, the top line is €320 million, and working capital is being self-funded through the headline consideration and adequate cash left to run this business smoothly. Now, you have consolidated numbers with the current operations. Going forward this business if you want to expand from our current business of €100 million to €400 million, it takes a substantial time, it will take a substantial expenditure it is going to hit and it provides a ready platform to launch our product with correct backward integration of our API plus it offers a lot of marketleverage , for which there is no value. So the correct way of the comparison maybe the return on capital employed. There is no major capital outflow and the returns bound to increase, and from other perspective, the business is built in a very short span of time, which we took a longer time of 4-5 years. So I think I leave it to you.

N. Govindarajan More than that like Sindhi, Arvind had already mentioned, Prakash, that at the end of the second year it will turn EBITDA positive.

Prakash Ramaseshan We had right now have a turnover close to a billion dollar, we take in another close to half a billion dollars which presently have a negative EBITDA and goes to zero, but on our existing business we have an EBITDA of close to 22-23%. So for this to get 22-23% overall your turnover has to go up there as well. How does the math work?

Arvind Vasudeva You are correct. This year we will be closing with 60 around $1.2 billion. And as you know the company is in a good growth phase of top line and EPS and some of the key niche products on launch which will generate the profit. So I think the company will try to balance it out. And Mr. Govind rightly said that we bound to have a circumstance for EBITDA and we work towards that and we try to work for the improvement and the impact of EBITDA loss of 20 million is in books of Actavis and is bound to increase going forward as Mr. Arvind said. So if you work out mathematics right, we will deliver the threshold committed EBITDA to you.

N. Govindarajan Improved.

Moderator Our next question is from Anubhav Agarwal of Credit Suisse. Please go ahead.

Anubhav Agarwal Just one question on the rationale of the acquisition. Is this business acquired for getting market presence or was there core portfolio products which you wanted to enhance your position? For example, you are getting entry into the French business, is that the main reason, I have not understood -- is it product or market?

Arvind Vasudeva I think it is multiple reasons. One is getting market access like Govind said for France, Belgium and Italy. We are getting large product portfolio of 1200 products and 200 products to be launched over the next 2 years. That is second benefit. Third, we are getting access to hospital business where we are not present at all, which we will leverage our own assets of injectable to write on that to grow well. So there are multiple reasons behind it. We are also getting newer therapeutic area; we are getting oncology portfolio, we are getting hormone portfolio, and we are getting more specialized products in the areas of inhalers and some multiple new therapeutic area coming in with the product portfolio along with it. So these are 4-5 reasons why we went for this acquisition.

Anubhav Agarwal In the current state, how many companies are in the double-digit EBITDA margin in the French market today in the Generic portfolio? Among the top 5, would…

Arvind Vasudeva We can come back to you later on I will not have off hand answer for that.

Anubhav Agarwal But let us say your own expectation, once you are in steady state, what is the margin expectation you are expecting for the French market, because that is going to be almost half of the sales you have acquired?

Arvind Vasudeva I think like I said earlier, infrastructure needs a minimum investment and revenue has to be critical. So as we move beyond this number, it should get into profitability with the current portfolio, with around portfolio added, and with injectable portfolio plugging in along with the current infrastructure there. So it needs a revenue upside. We need to have a revenue critical mass to become EBITDA positive there.

Moderator Thank you. Our next question is from Nitin Agarwal of IDFC Securities. Please go ahead.

Nitin Agarwal Govind, I just wanted to check we are going to be on an EBITDA basis on the ongoing business about give or take few hundred million dollars of EBITDA in which we are going to grow, this business is going to breakeven the year after and we are adding a fair degree of complexity to our business in terms of the kind of the supply chain issues we are going to manage because almost 100% of the business is outsourced. Eventually what is the big game plan in terms of how this being plays out even say 5-6 years for adding so much complexity in the business?

N. Govindarajan Like we said earlier lot of this portfolio which are there will be over a period of time moved into our own site. But, we will still have some of the specialty product relationship with the supply which will come as in-sourcing from the supplier. So lot of this current supplies will be moved into in-house facility between 2-3 years' time.

Nitin Agarwal How much shift are we looking at, what proportion roughly?

N. Govindarajan It should be upward of 30-40%.

Nitin Agarwal Till 60% odd of this would be on an outsource model? My point is we are adding so much complexity to our business while the financial impact is readily muted, it is not 10% of our operating profits let us say 3 years from now. Take a 5-year view or 10-year view, how are we looking at this business?

N. Govindarajan Like I said upward of 40%, it can be toward (+50%) also. Complexity is something that we can manage if the supply arrangement management. So it is not a complexity that company cannot manage it.

Nitin Agarwal Singhi, on the working capital front, what is the typical receivable cycle and the inventory cycle which you have been maintaining in the market?

Sudhir Singhi These are fairly stable cycle as far as the receivables and the payable are concerned. Inventories peculiar to the products launch and order in hand show all those things have been very clearly factored into that while deciding the consideration.

Nitin Agarwal On an ongoing basis, what is the kind of inventory and debtor days are we looking at, typically on a steady state basis?

Sudhir Singhi Debtor days generally here in this market 60-90 days and it matches with the creditors' payment of 60-75 days.

Nitin Agarwal And the inventory?

Sudhir Singhi Inventory in around 3-4 months.

Moderator Thank you. Our next question is from Nimish Mehta of Research Delta Advisors. Please go ahead.

Nimish Mehta You mentioned that the gross margin is about 35% if I assume, then we are talking about top line of €320 million, about £112 million Euro of gross profit and at EBITDA level we are still negative by €20 million, so that translates below gross margin the cost is about €132 million. Can you throw some light on what are the major components of that cost? And if I am not wrong it is that cost that we will have to manage to get ourselves back to profitability, so how will you do that?

Arvind Vasudeva Like we said, since we acquired the front end, it is primarily the front end and commercial cost of sales and marketing, general administration and regulatory, and also some of this inventory-related costs.

Nimish Mehta What does that mean?

Arvind Vasudeva Sometime you have this because of expiry and other things and spoilages that is the minimal amount. So these are four levels of costs, but the major cost is the cost of goods which we think we referred earlier how we are going to address that issue.

Nimish Mehta And the 450 people that we are likely to take on board, what I am trying to understand is what are those related to and those are mostly administration and regulatory, people for that function or for sales function as well?

Arvind Vasudeva Like we said there are 450 people in 7 countries, majority is in front end.

Nimish Mehta What do you mean by front end because you want require people to market or detail the products right?

Arvind Vasudeva We talked about hospital sales, so you need to go to hospitals; you need to go to pharmacies, so you need a sales force for managing that.

Arvind Vasudeva And this involves pharmacy promotions and also Spanish retail sales those pharmacy promotions there is Aurobindo.

Nimish Mehta So if we were to break up the 450 people between sales, administration, and integration roughly how would you do it?

Arvind Vasudeva Sales will be more than half.

Moderator Thank you. Our next question is from Meeta Shetty of HDFC Securities. Please go ahead.

Meeta Shetty Just one clarification at the EBITDA level. Do we see the losses actually increasing in the immediate quarters and then attaining the break even, because now we will be sharing some manufacturing margins with Actavis?

Arvind Vasudeva Like we said it is improving over the last 3 years, and as we get indication, it also becomes better in the last two quarters.

Meeta Shetty No, why I am asking you is that 20 million included the manufacturing margins as well, but now we might be sharing some part of that with Actavis. So will the losses increase in the immediate quarters?

Arvind Vasudeva Let us say factoring the prices agreement that we have with Actavis, we are talking about the number.

Meeta Shetty So, we do not see it increasing.

Arvind Vasudeva No.

Moderator Our next question is from Chirag Dagli of HDFC Mutual Fund. Please go ahead.

Chirag Dagli On these how many products dossiers we currently have which will find a front end by virtue of this acquisition?

Arvind Vasudeva Like I said there are 1200 products that we have acquired in these 7 markets, and there are 200 more which will come as new product in the pipeline.

Chirag Dagli But those are Actavis approvals. I am talking about Aurobindo filings, which we might have done and they will find a way to the market now.

V. Muralidharan We have got nearly 20% of the products straight overlaps are available which we will be able to straightaway bring in at the most appropriate time in the coming months after exhausting the current inventories of Actavis. And then there are a few more filings will be there and then we will be able to draw leverage out of this.

Chirag Dagli So 20% of the 1200 you are saying are products that you already have own filing?

N. Govindarajan Yeah.

Chirag Dagli So about 240 products roughly is what you can start immediately manufacturing on your own?

Arvind Vasudeva Yes, marketing authorizations.

Chirag Dagli Anything specifically for the French market, do we have pending dossiers?

Arvind Vasudeva Definitely, yes.

Chirag Dagli How many will those be?

Arvind Vasudeva This exact overlap analysis if you want numbers I can come back to you. But as I said in France because that has been one of our target markets we have been waiting for one such opportune moment, because in France it is absolutely important to have a critical mass of products. So, we have been building our baskets, but now there are generics brand and Actavis combined might straightaway catapulting ourselves into the #1 amongst the Indian manufacturers or position in the top 10 rankings actually, we will be the 6th ranked player in France. To answer your question directly, some of the Aurobindo filings already granted marketing authorization will come in handy as well, which will provide us the cost advantage in terms of cost.

Chirag Dagli No sir, let me ask this differently. Of the 1200 products that Actavis currently sells, how many will be in France?

Arvind Vasudeva It is about 300 plus.

Chirag Dagli How many pending approval do we have from Aurobindo's table for the French market currently?

V. Muralidharan We have about 60 approvals and another 20 and odd due to be approved.

Chirag Dagli And any other large bucket like France where we have such large pending approvals?

V. Muralidharan We have been steadily applying across our key core identified markets which includes France, but not only limited to France, also Germany, Italy, Netherlands, Spain, Portugal, all these are part of the proposed acquisition. So this is going to have a complementary effect. In addition to that UK is one of our principal markets which is not part of this proposed acquisition, but again our filings pan across these countries.

Moderator Our next question is from Anmol Gangoo of JM Financials. Please go ahead.

Anmol Gangoo I have a specific question on the French market dynamics. Now Actavis commentary on the French market seems to suggest that till 2012 you have seen a double-digit price erosion, which until later part of 2012 has been offset by volume increases primarily led by injectables. My question is that in 2013, how has this dynamic played out and going ahead what do you think the French market dynamic will be like -- do you continue to see the pricing coming up for that is stabilized? And as far as volume uptick is concerned, where are we in the cycle?

V. Muralidharan As we touched upon, in France the recent phenomena of slight price dip has started happening, this is in line with France acting in line with some of the other European countries, some of them turned that in their way. But here the advantage with this proposed acquisition Arrow, Actavis with commitment of Aurobindo is one is the broad, very wide product portfolio and also the Arrow Generiques as the brand is highly reputed and acknowledged across the industry and very strong presence in the hospital market by volume and value in that of one and two positions. So that way we expect to spread the risks if at all and then strategize in such a manner to counter the pricing challenge that is coming up.

Anmol Gangoo I have a follow-up question, basically I am trying to understand especially the Hospital segment, how does the value-volume equation stack up today – in the last 3 to 6 months what are the trends that you witnessed when you looked at the asset?

Arvind Vasudeva You are talking about France market or overall?

Anmol Gangoo French Hospital market especially.

Arvind Vasudeva Like we said earlier current portfolio that we have has reached a size that is good, but it need to scale up more revenue for it to become profitable in French geography. As you bring higher value, low volume products in the market, they will give us higher revenue and hence we will be able to break even and become profitable there. So it leaves some more work in terms of revenue generation. So we have good coverage; the revenue generation needs to get enhanced.

Anmol Gangoo My second question is given that we now have enough on our plate in terms of revenue visibility; we are adding around $400 million in revenue, and there is a lot of work to be done around in terms of turning margins in this part of the business. So can we assume that as far as inorganic initiatives are concerned for Aurobindo we have done for a while or you will look at something if something as attractive as what you have got?

N. Govindarajan We would like to consolidate on what we have done at this juncture, like we will not be looking at such flat scale.

Moderator Thank you. Our next question is from Ranvir Singh from Sharekhan. Please go ahead.

Ranvir Singh Is there any stipulation in agreement which may restrain for a particular period to site transfer, or it is up to us to site transfer as soon as you are ready with regulatory things and we are ready with new site? That is one. Secondly, for a long term perspective in 4-5 years what do we expect whether 100% would be supplied from Indian side or part of it would be supplied from Indian side and that Actavis would also be supplying in there? So there are two questions, please clarify.

Arvind Vasudeva Either changing site or adding one more site has no restrictions as long as we follow the process of variation. So there is no restriction on the area. Two, we will get supplies from

Actavis, supplies from third-party and supply from India as well -- will be a mix of these three things. But going forward, this ratio will vary depending on how we bring the products into our own site.

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

Surya Patra Any intangible asset that you are adding to the books because of the acquisition?

Arvind Vasudeva Yes, we have intangible asset in terms of Arrow Generiques brand, and we also have another intangible asset in packaging technology which has exclusivity with Arrow Generiques. And we are also certain brand getting in-licensed which are branded generics in-licensed from a multinational.

Surya Patra Can you quantify that? Because of this what is likely addition to the asset?

Sudhir Singhi It has no financial impact as the assets value is more than the consideration. It will be assets intangible and a significant value, but will not be classified in the balance sheet as far as my knowledge goes.

Surya Patra So that means it is only the current asset that would be part of the…?

Sudhir Singhi Yes, only current assets and all the brands and all the market authorizations will be assigned to Aurobindo Pharma and it will be significant intangible assets. We presume that it has been written off in the books of account. It will not carry a value into that but it will be a part of the assets.

Surya Patra Any cumulative losses that is there and for which you might get some tax rebate or something like that?

Sudhir Singhi Yes, because these are legal entity, so legal entities continue to have their own filing of return, and those losses will benefit in future profitability and set off of losses will accrue to Aurobindo's Eu

Surya Patra So can you give some sense of what is the likely tax rate here on we should be seeing for next year?

Sudhir Singhi The next two years we are under MAT, so we will be with this MAT rate of 21% overall in India, and in Europe as we get profitability -- the tax clause I am not competent to comment upon right now, but is allowed to set off the past accumulated losses. So, there will be a bare minimum tax implication.

Surya Patra Are we expected to add some short term loans for working capital or the cash what you said is more than enough to handle the business?

Sudhir Singhi Presently, the working capital cycle is fairly stabilized. So as we progress, we will assess the situation, otherwise I do not think so unless the government policy changes significantly into the other matters.

Surya Patra On the Hospital segment side, can you give some sense what is your strategy because as of now this entire acquired business is offering something or currently generating something like $100 million revenue in the hospital segment, what is your strategy like, when do you think that you would be launching the injectable products there and what is the sourcing arrangement that you are planning or what is the nature of the products currently you are having in the injectable basket, some sense on that?

Arvind Vasudeva Major therapies are antibiotics, general injectables, oncological, hormones, this is our current portfolio that we have. And we will be bringing our own portfolio from Unit 4 Auronext which is Penem antibiotics and hormones as well as oncological, we will supplement the portfolio.

Surya Patra Can you give some idea regards to the value product and the volume product mix, because the Penems what you are talking about I think it will take some time to really launch from the year one ways and currently what is the value mix in that Hospital segment?

Arvind Vasudeva The volume products will come from Unit-4, the value products will come from Auronext facility of Penem as well as UGF facility of onco and hormone, and some of the antibiotics that we have.

Surya Patra That is few quarters away from here, right?

Arvind Vasudeva Yes, it will be some quarters away. Currently, we will only leverage what portfolio we have from Actavis coming.

Surya Patra Is that when currently we have just on the antibiotic to injectable portfolio in the Hospital segment?

Arvind Vasudeva I said we are going to launch about 200 products in the next 2 years which is coming from Actavis portfolio; some of them are injectable also. So there will be new launches happening in next 24 months before our things start plugging in from more sites.

Surya Patra Sorry for repeating once again, but the current level $400 million revenue what we are generating it is out of the Antibiotic portfolio or something else?

Sudhir Singhi Majorly, it is oncology and general injectables. Antibiotic is not a major product.

Arvind Vasudeva Oncology and anesthesiology injectables are also there in the Actavis portfolio, and we have the flexibility to fill the gaps where given product is granted only in two out of the seven countries, we will be able to stretch it to the other countries. So we will be also adapting this strategy in order to expand the Hospital business and parallelly bring in Aurobindo's own developed products plugging into this segment.

Moderator Our next question is from T Srihari of PCS Securities. Please go ahead.

T Srihari My question pertains primarily to the French operations. Could you please tell me what are the share of the French phase of the €320 million? Secondly, how much of that was tender-based business? And what is the kind of price erosion you saw in 2013?

N. Govindarajan The revenue of French market is about less than half of the total revenue of 320. It is primarily a retail market with Hospital business. It is not yet in tender.

T Srihari What is the institutional share?

Arvind Vasudeva Hospital is about 30% of the revenue.

T Srihari Price erosion during 2013?

Arvind Vasudeva Like Murali said earlier, price erosion is a combination of government regulated price erosion and the discount which pharmacy gets. So it sets off against each other. So at a company level you do not get impacted as much.

T Srihari So if it is government funded, erosion was how much?

Arvind Vasudeva Murali, is it about 12-15%?

V. Muralidharan Yes, and also it is product-specific. Initially, they are identifying some of the major products on which health reimbursement is happening. So that is being done, and yeah, it is in the percentage level as what you just said.

T. Srihari At the macro level, the government mandated price erosion was around 12-15%?

Arvind Vasudeva Like I said earlier, most regulated market, governments are on the health expenditure pressure. So it is a way of life in Generics market and including us are capable of handling those price erosions.

Moderator Thank you. Our next question is a followup from Sameer Baisiwala of Morgan Stanley. Please go ahead.

Sameer Baisiwala As you know there is 1200 approvals and €320 million is the total sales. So what would be the share of top 10 or top 15 products?

Arvind Vasudeva Top 10 product is about 20% revenue.

Sameer Baisiwala Is there a portion of 1200 which is not yet commercialized?

Arvind Vasudeva 1200s have been commercialized. The new one which is going to come is 200.

Sameer Baisiwala Because it looks a little low that per product you have commercialized the quarter of a million Euro, is the right way of looking at it or is there enough steam still left in these 1200 commercialized products?

Arvind Vasudeva All these are commercialized, sometimes we do not sell because some of the products in the market are not profitable, so sometimes they are sold and sometimes they are not sold. But all of them are commercialized, but there are pricing pressures where company sell maybe 90% plus of their commercialized products.

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

Surjit Pal How much time will it take if I take 200 plus and minus 20% will have to site transfer to your Indian terms?

Arvind Vasudeva I think we are working on a prioritization, so we will do over a period of 3 years time looking at what is high value, high profit early and going to moderate and low later on. So we have taken a serious plan to do that.

Surjit Pal Most of your peers including India and outside including Teva when they are finding it pretty tough because of more of institutional business is growing over there and the growing pressure of the government on healthcare expenditure, do you think there is still market left which could encourage you to be profitable more from here on?

Arvind Vasudeva Yes, there is definitely market left. Yes, there are pressures of prices not in Europe alone, it is in Japan, it is in other markets also -- it is a way of life. So I think all regulated markets are going to be under pressure, and even emerging markets will face that. So despite of that I think one has to work towards making your cost base in a way that you still remain profitable. We are seized of that regulatory risk in the marketplace or regulated market and emerging and we are consciously working on that to remain at a margin level that we want.

Surjit Pal Because why I am raising this issue is that because you are currently having very healthy EBITDA margin of around 20% for this year, and this will have a drag on your margin till the time you become profitable?

Arvind Vasudeva Just to share with you, we were on our own in European market and we broke even last year and now we are becoming profitable. So I think we understand this market quite well now, we know what it takes to do better in Europe and hence this acquisition has been done.

Surjit Pal What is your current revenue in Euro?

Arvind Vasudeva Gross sale of €100 million.

Surjit Pal In breakeven specifically?

Arvind Vasudeva Yes, in breakeven.

Moderator Our next question is from Mahesh Sarda of ING Life. Please go ahead.

Mahesh Sarda We have just turned our corners in the profitability over the last 6 quarters and suddenly we got some attractive opportunity and we have done this acquisition. As you said just about a minute back that Europe, you have just turned profitable. So is it not that we are taking too much risk and we were seeing very good repayment of our debt and suddenly we find that we will take some more time for the debt further to get down?

Arvind Vasudeva Like we said earlier, this acquisition is giving us entry into two large markets of France and Italy. It is giving us a platform of hospital sale and injectables, and it is also supplementing our current presence in Europe. Like Govind said earlier, we are also reducing this concentration risk only in US. So today we will have US and Europe being of comparable size. Then we have other three platform of ARB, emerging market and we do business which is evening out our revenue risk.

Mahesh Sarda Suppose, maybe about 6 months down the line, if you get some attractive opportunity again, would it not be more tempted to do these deals in future?

Arvind Vasudeva I think Govind has responded to that. We have taken this deal, we are not going to jump into anything as big as this, we will consolidate our acquisition for some time to come.

N. Govindarajan On the debt front, I just wanted you to be clear about that, as Singhi has consistently explained that our ECB is something which is only $16 million for next year, and also it gets spread over the subsequent 4 years or so, even considering that we still believe that we will have positive cash available to have optimization in terms of our working capital borrowing as well. Clearly I think we are better positioned to do it and we are not having any consensus on that front.

Mahesh Sarda On this acquisition, I have a couple of questions on this gross margins which we said that we are looking at increasing from 30% to 40%. Will it be more because we are sourcing products from our India facility, what would be the mix like suppose you are currently having 50% from Actavis and 50% from third-party, so will the third party sources reduce or the Actavis supplies reduce?

Arvind Vasudeva The margin expansion will happen for product mix, the tender participation management on the profitable side, there will be more site transfer from Actavis portfolio, less from the third-party.

Mahesh Sarda And what will be timeline, this 30%?

Arvind Vasudeva Like I said over the next 3 years.

Moderator We will take the last question from Sangam Iyer of Subhkam Ventures. Please go ahead.

Sangam Iyer Just wanted to understand, during the call you did mention to one of the participants that 20% of the products have a straight overlap, right? So how long will it take for us to launch the products or source it from Auro India itself?

Arvind Vasudeva Like we said we are going to look at site transferring to our site whatever we are acquiring from Actavis market.

Sangam Iyer Like, for example, say in France out of 390 products that we are acquiring from Actavis, Auro itself has around 60 products which are approved, which is an overlap, right? So these 60 products we can directly source it from India itself or is there an agreement that we need to have a site transfer for them, etc.?

V. Muralidharan The overlaps depending on whether it is Actavis overlaps or third-party overlaps, it will have a slightly differing way of bringing them into the stream, because if it is a third-party in-licensed product, which has been commercialized by Actavis then there are some underlying contract period needs to be honoured. But at the same time if it is an Actavis-manufactured product Aurobindo overlap, then we will be able to bring our product into the sales stream. We will take a very, very calculated call on timing of bringing in our products replacing the current overlapping of Actavis product.

Sangam Iyer Say for example, just to understand this deal bit more clearer in terms of the supply agreement that we have entered into Actavis and third party, is there any timeline till which we have to honor the third party agreements and beyond which we can look for a cheaper avenue for sourcing?

Arvind Vasudeva Yes, there are timelines and it will accrue over the next 3-4-5 years, and like Murali said strategically we will make a call of what we want to do then.

Arvind Vasudeva Because there are differing timelines, there are third-party products which are already expired, which are in the renewal phase. So our call on such products is entirely depending on us. But again we are very, very particular about having a supply continuity for the immediate period because for us to maintain the revenue. Then, as Arvind said we will be taking the prioritization exercise to bring in which product at what time point.

Sangam Iyer Till these agreements are actually completely honoured, the product rationalization that also we were talking about as a part of improving the product mix, will also take its own course because of this agreement that are there in the middle?

Arvind Vasudeva Yes, this will be done over the next 3-year-period and we are prioritizing which needs to be done earlier depending on various agreements that we had between various parties.

Sangam Iyer Coming back to the gross margin part of it because everything now hinges back to the same in a sourcing agreement from where we are looking to improve on the cost of goods sold. So this jump from 30 to 40 this timeline is again 2 to 3 years, wherein at least in the next one year or so it will not happen to the extent that we are factoring it, right?

Arvind Vasudeva We are not saying 30%, we are saying mid-30 to 40.

Sangam Iyer So that transition will actually take at least 18 months before which we actually see some kind of an improvement coming through?

Arvind Vasudeva Like we indicated that improvement has been done to an extent by Actavis, we saw some improvement in the second half, more will be accrued in the current year, and it will become more as we manage our product mix and participate in profitable tender, and as we bring products in-house, it will be gradual process over next 3 years.

Sangam Iyer So the expansion is primarily through new product launches, etc., that will actually help offset to or improve the product mix?

Arvind Vasudeva Yes, plus also launching in different countries as well. So all products are not in all countries.

Sangam Iyer On the existing business profile, as you mentioned price erosions, typically, when does these kind of the government revision of price rise, etc. come in -- is it like start of the calendar year itself in France like what happened in 2013?

Arvind Vasudeva They will keep doing a benchmarking work with their reference state countries, and they look at pricing in other countries and start benchmarking. Like Murali said, it is done product-to-product basis, it is not done across the board.

Sangam Iyer So when it is expected in this calendar year, can you throw some light on that?

V. Muralidharan Already one set of products which are due to be implemented from February-March and then the next may come possibly during end 2014 or early 2015.

Sangam Iyer But these would not be part of the supply agreements, right? Because the revision in product prices, is it because the pass-through when you actually enter into these agreements, or those kind of revisions are not actually factored in?

Arvind Vasudeva I think Murali has shared that earlier there is a balance between the rebates which the pharmacies get and the price reduction by the government. So there is a balance between these two. So as the prices come down rebates also come down. It is a balance that works between rebates that pharmacists get and the prices which government reduces -- so there is a play between these two areas.

Moderator Ladies and gentlemen that was the last question. I now hand the floor back to Mr. T. Roy Choudhury for closing comments.

T Roy Choudhury For any further information, request you to please visit our website www.aurobindo.com or feel free to get in touch with me. Thank you everyone for joining us in the call today.

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