"Aurobindo Pharma Limited Q1 FY16-17 Earning Conference Call"

August 24, 2016

MANAGEMENT:

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Moderator: Good morning, Ladies and Gentlemen, and Welcome to the Aurobindo Pharma Q1 FY17 Earning 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 call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I would now like to hand the conference over to Ms. Deepika Gupta Padhi from Investor Relations. Thank you and over to you, ma'am.

Deepika Gupta Padhi: Thank you, Malika. Good Morning and Welcome, Everyone, to our First Quarter FY16-17 Earnings Call. With me, we have our Senior Management Team, represented by Mr. N. Govindarajan – Managing Director; Mr. Robert Cunard – CEO, Aurobindo Pharma USA; Mr. Ronald Quadrel – CEO, AuroMedics Pharma USA; Mr. Sanjeev Dani – COO & Head, Formulations and Mr. Santhanam Subramanian – CFO.

We will begin this call with the opening remarks from the Management, followed by an interactive Q&A session. The Company from 1st of April, 2016, has adopted Indian Accounting Standards, and hence the financials which we will discuss today are in accordance with the prescribed reporting structure. For comparison purpose, the Q1 FY15-16 numbers are also restated as per IndAS. Please note that some of the matters we will discuss today are forward-looking, including and without limitations statement relating to the implementation of strategic initiatives 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 developments 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 now hand over the call to Mr. N. Govindarajan for his opening remarks. Over to you, Govind.

N. Govindarajan: Thank you, Deepika. Good Morning, Everyone. We are here to discuss the first quarter financial year 2016 - 2017 results declared by the Company. We registered a double-digit growth in the revenues during the quarter on account of the broad-based growth across all the business verticals. Our revenues and EBITDA increased by 12.9% and 22.6% year-on-year during the quarter. EBITDA margin for the quarter stands at 23.9%. The profit after tax increased by 24% year-on-year during the quarter. Consolidated net operating income is at Rs.3,725.9 crores in Q1 FY16-17.

In terms of the Business Breakdown: Formulations business contributed 80.5% of the total gross sales; the gross Formulations sales for the quarter stands at Rs.3,032.1

crores, registering a 15.9% growth year-on-year. API business accounted for the balance Rs.734.5 crores for the quarter. In the Formulations business, the total sales from the US market stood at Rs.1,703.9 crores during the quarter. The business registered a growth of 20.5% year-on-year during the quarter. The growth is on account of new launches in the Oral and Injectable segment.

Aurobindo USA, the company marketing Oral products in USA has witnessed around 10% growth year-on-year during the quarter. We launched four new products during the quarter.

Aurolife, our US manufacturing arm continued to witness increase in sales during the quarter, mainly on account of increase in demand from VA. In order to meet further increase in demand, Aurolife has undertaken construction of additional manufacturing area which is expected to be completed in the calendar year 2017.

AuroMedics, the Injectable business continues its growth momentum with quarter last year sales at US$34.3 million, 95% growth year-on-year. We launched three new products during the quarter. Under the Injectables segment, including Ophthalmics, we have filed a total of 82 products as on 30th June, 2016, out of which 43 received approval including two tentative approvals and the balance are awaiting approvals. The year started with three approvals during the quarter and we expect a higher number of approvals during the financial year.

We have a large number of complex products under development, namely Hormones, Oncology, Liposome and Microsphere Depot Injectables which we plan to start filing over the next three to six quarters. AuroHealth, which manufactures and markets Pharma OTC products in the US continued to gain penetration in to several key national retailers as well as select regional accounts. AuroHealth is now shipping to five out of the top 10 OTC customers. Natrol, the acquired branded Neutraceutical entity is performing as expected. The company as on 30th June, 2016, has filed 403 ANDAs on a cumulative basis, out of which 228 are final approved and 41 are tentative approvals, including 21 ANDAs which are tentatively approved under PEPFAR and balance 134 ANDAs are under review.

The unit wise filing and approvals are as follows: From Unit-3, 124 filed, 93 approved; Unit-7, 151 filed, 61 approved; Aurolife, 26 filed, 13 approved; Unit-4, 68 filed, 31 approved; Unit-12 and Unit-6, 19 and 11 filed and approved respectively and Auronext- 4 products have been filed so far. Unit-3, Unit-7 and Aurolife manufactures Oral Non-Betalactam products; Unit-4 manufactures General Injectables and Ophthalmic products; Unit- 6 and Unit-12 manufactures Cephalosporin and Semi-Synthetic Penicillin respectively; and Auronext, which has its facility at Bhiwadi, in Rajasthan, manufactures Penem Injectable products.

Europe Formulations sales were at Rs.831.2 crores in Q1 FY16-17, registering 12.1% growth year-on-year. The acquired business continued to see profitability during the quarter, we have transferred manufacturing of four products from Europe to India during the quarter with a cumulative transfer of 36 products as on 30th June, 2016.

Emerging markets Formulations sales were at Rs.194 crores during the quarter with a growth of 17.6%. ARV Formulations sales were at Rs. 303 crores during the quarter.

In terms of Segmental Classification: US Formulations contributed 45% of the overall revenues in Q1 FY16-17 versus 42% in Q1 FY15-16. Share of EU Formulations is at 22% in Q1 FY16-17 while the share of the emerging markets remain the at 5%. ARV segment sales represent 8% of the total sales in Q1 FY16-17. API business contributed 19.5% of the total revenues in Q1 FY16-17.

Our EBITDA before FOREX for the quarter is at Rs.889 crores, representing the operating margin of 23.9% for the quarter, up from 22.6% from the corresponding period last year. R&D expenses is at Rs. 120 crores during the quarter which is 3.2% of the sales. The Company generated FOREX gain of Rs. 7.04 crores during the quarter. The closing rupee versus US dollar rate was Rs. 67.525 in June 2016 and Rs.66.255 in March 2016. CAPEX for the quarter is around US$56 million. The effective tax rate for the financial year is at 25.6% of PBT. The net debt stood at US$525 million on 30th June, 2016, after netting of the debt factoring of US$150 million. The majority of the Company's debt is denominated in foreign currency. The cash and bank balance is at US$172 million.

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

Moderator: Thank you very much, sir. Ladies and Gentlemen, we will now begin the question-and-answer session. Please go ahead.

Kumar Saurabh: Firstly, if you can help explain the net debts. So, including the debt factoring, debt should be around $675 million, how should we look at it? Because pre-IndAS era, FY16 we ended at around $584 million of net debt and now we can see that the restated number is $640 million, so should we assume that from $640 million net debt has gone up to $675 million? And if yes, then what would explain that? because US sales has not moved up to that extent.

Santhanam Subramanian: $640 million is as per the IndAS, IndAS provisions are very tight in terms of how you are accounting the debt, even if they are recourse or non-recourse, we account it as net debt actually. So, in terms of $640 million going to $675 million, I presume you are adding $525 million plus $150 million is the factoring, that is how you got $675 million, I presume?

Kumar Saurabh: Yes.

Santhanam Subramanian: The increase of net debt by $35 million is because of the higher charge backs which we paid during the quarter as charge backs is the function of net sales to the WAC which is the Wholesale Acquisition Cost and it depends upon the particular product and particular customer. So this quarter there is a higher charge backs and that is the reason why it has gone up. And we do not think it will continue like this because we have also launched new products during this quarter.

Kumar Saurabh: So sir, what should be the normalized rates of this debt factoring going forward, how should we look at debt?

N. Govindarajan: First of all, let me explain about the factoring before Subu talks about the rest of it. The US subsidiary has tied up with a leading bank for a continuous non-recourse sale of trade receivables in June 2016, initially raising around $150 million. Technically, it is a fee which you are paying for the program, it is much lower than the typical interest cost for the working capital limits and the strategy to monetize the available Account Receivables is a great potential to enhance liquidity. So, that is the background of the factoring.

Santhanam Subramanian: I have been talking about it in the last two, three calls that US invoicing mechanism is different than what we have been doing in India. If you really see the charge backs to the WAC is always around 70%, which means that debtors will be high. If you assume that debtors is 100 the net sale we are accounting will be around 30. So the difference is what we are paying for and that we will pay in advance or during the period of 15 to 30 days, whereas the receivable gross of the charge backs will be received between 70 to 100 days. If the sales are growing, and new products are launched there will be an immediate requirement of pumping additional working capital into the system to achieve the growth,

Kumar Saurabh: So sir, where should we look at our net debt ending at FY17 end?

Santhanam Subramanian: We will be working towards $500 million net debt.

Kumar Saurabh: And sir, in terms of US, if I may ask, we have seen our launch momentum has been pretty strong, how much of that do you think has already been factored into our current quarter number and how much is yet to come, what do you think from the existing launch pipeline?

Robert Cunard: In regards to the launches, the approvals have been very strong and we have talked about that in the past as far as the timing of those actually being a little sooner than expected. But being able to monetize those we have been lagging a little bit. So we expect that we will continue to gain strength through the balance of the fiscal year. As

we sit right now, we have 19 product families that are approved, that will be launched over the next three quarters and that is for approvals that we have on hand today. We have another 22 targeted action dates through the end of the fiscal year, obviously we do not anticipate all those will be final approvals but a significant number will be. And of that 19 product families today, the addressable market is about 6.8 billion per IMS June data. So, a large portion of that is Esomeprazole but still a lot of breadth remains in that pipeline and we think that accelerates through the balance of the fiscal year.

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

Anubhav Agrawal: Sir, one clarity on this net debt. I just wanted to understand that, I understood the logic you talked about but the quantum was very surprising. So, if you look at just the working capital increase for us, the numbers are just that the working capital for us has gone up by $80 million to $90 million in this quarter on a US sales of about almost $1 billion or $250 million in a quarter. So, the quantum I was not able to understand, just by charge back how much will increase, would you say that the charge back would have increased for you almost10% in this quarter?

Santhanam Subramanian: No, the quantum, if you really think the charge backs which has been increased in the US is around $35 million, apart from that we also discharged certain rebates pertaining to the European market European rebates we do not pay immediately, we will take around some time depending upon when the agencies like Insurance, Government are submitting the bills. So, this is a regular thing. If the bills or invoices for rebate are coming late, we have to discharge as and when it is coming.

Anubhav Agrawal: Sorry, can you explain this European thing, I did not follow, what has happened in Europe?

Santhanam Subramanian: It is a similar practice in Europe also, but there the rebates are asked at the later date not immediately like in US.

Anubhav Agrawal: But, has something changed there now?

Santhanam Subramanian: No change as this is a typical practice going on for years. Its only that both the things have happened in this quarter

Anubhav Agrawal: Sorry, that is the disconnect I am not able to understand. If it is a continuous practice why would working capital go up almost 10% up in this quarter only? Partly I can understand through US, because there the channel consolidation could have played a role that could have been the trickle point but what would have changed in the European market?

Santhanam Subramanian: If you see the annual accounts, in the other liabilities there is a line item called other liabilities, statutory liabilities and others amounting, Rs. 660 crores plus. So, out of the Other liability we have disbursed some amount in this quarter when the bills have been raised. You can see that, it is page number 160 of the annual accounts, on the last few lines.

Anubhav Agrawal: I will have a look at the details, thank you. Just one question, the CAPEX now, as Govind sir mentioned in the opening remarks that now for Aurolife you will put up extra CAPEX. Earlier we were guiding to almost $100 million CAPEX next year, what would be the expectation of FY18 CAPEX now?

N. Govindarajan: Same, we are maintaining that, Anubhav.

Anubhav Agrawal: But how would that happen, so is Aurolife CAPEX being extra but it is not very meaningful, is it?

N. Govindarajan: Yes, first of all in Aurolife, the entire CAPEX is not going to happen by next year. In the next three quarters itself for this year we will start investing in Aurolife, after that we will be able to still accommodate within the 100 million we have budged, Anubhav.

Anubhav Agrawal: Just one clarity I wanted to have on the OTC business for us in the US also, can you just give an idea that how many products we already have in the market? I know we have a lot approved but how many we have already in the market, roughly what is the size of this business for us as well as the prospect of this business over next two years?

N. Govindarajan: Okay. Right now, it is still less than $10 million in terms of the current sale Anubhav. As you would appreciate the fact that at the end of the day you need to have a critical mass in terms of the market before you really grow in this business, we expect towards the second half of next year you will suddenly see a growth is what we are expecting as far as OTC is concerned, Anubhav.

Anubhav Agrawal: You mentioned towards second half FY18 or FY17?

N. Govindarajan: FY18, that's right, FY18.

Anubhav Agrawal: And currently you will have less than five products in the market and roughly when it is $10 million?

N. Govindarajan: As far as products, we have 20 products in the market under OTC segment.

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

Rakesh Jhunjhunwala: My first question is, this $150 million is without recourse to you, whatever accounting standards say actually it is not a debt because you have received the money and the bank has no right to receive as a recourse to you.

N. Govindarajan: Which is true Rakeshji.

Rakesh Jhunjhunwala: Then why you consider it as debt, because the bank has no right against you. And therefore the quality of the customer has to be good then only they would give that kind of mortgage and the quality of the receipt should be very good then only they will take it without recourse.

N. Govindarajan: Obviously, sir.

Rakesh Jhunjhunwala: And what is the interest rates you are paying, are they competitive, are they good?

N. Govindarajan: It is less than, in fact, 1.5% annualized.

Rakesh Jhunjhunwala: And will you be able to do this on a continuous basis?

N. Govindarajan: We can do it sir, because this improves the liquidity and strategically it is good for us to keep doing it, sir.

Rakesh Jhunjhunwala: So then why don't you consider this a permanent reduction in working capital? You know, the accounting standards may say anything but in reality it is an actual reduction in your working capital cycle, because you are paying the cost for it and you are receiving the money in advance without recourse to you.

N. Govindarajan: That is true. But see, the reason why we have brought up this as a separate subject is this is the first time we are doing it, even though there are companies which have been doing it for long. We just wanted to give the clarity, but your point is well taken in terms of relooking at the entire working capital.

Rakesh Jhunjhunwala: Because it is not debt, it is without recourse, if it is recourse still we are talking about debt.

N. Govindarajan: There is no recourse sir, clearly.

Rakesh Jhunjhunwala: And if it is going to take place in a continuous basis, isn't it a permanent reduction in working capital?

N. Govindarajan: Yes sir, we can look at that way as well, sir.

Rakesh Jhunjhunwala: My second question is, there are some reports about, see there are a lot of initiatives that you are taking which are not giving any returns today, and it is going to take time, there is talk about you have been investing in vaccine. So, can you tell me which are the initiatives which may not give you revenue this year, next year but post 2018-2019 say vaccines or…

N. Govindarajan: I will give you, sir. So, obviously since you started with vaccine so I will talk about vaccine. So, vaccines would be like in the next two to two and a half years you cannot expect revenues, I will discuss what are the ones which you cannot expect revenues over the next two, three years. Vaccine is one, Microsphere is one, and Oncology in terms of larger quantity of products. So, while we start filing these please understand the fact that the approval will take at least, around one and a half to two years, even the majority of Oncology, Hormone and Steroids would be post the two, two and a half years time cycle. And Liposome and certain other films and patches would be after the two and a half, three years time cycle only, sir.

Rakesh Jhunjhunwala: Tell me one thing, the revenue potentiality that runs into, as in all these initiatives will have huge, because I am long-term investor I look at long-term things, so do these initiatives can they really turn to be very large revenue and profit measures?

N. Govindarajan: I will give you one example sir, which Ron has been consistently mentioning. There are four Peptide based Microsphere product which itself is around a 3 billion top-line, I mean, in terms of the opportunity. And even at the peak, it is our assumption, we do not see more than three or four players getting into that, so that is the level of opportunity which is existing which is one example I can give you.

Rakesh Jhunjhunwala: And what is the kind of, I mean, how sure do you feel that we will be able to launch this product?

N. Govindarajan: Sir, we have, obviously, fair level of confidence sir, You would appreciate the fact that we would otherwise not be investing our efforts on this.

Rakesh Jhunjhunwala: Like, there is a lot of talk in the market about some raising of equity and a lot of rumors and lot of talk, if we could get some clarity I think that will help.

N. Govindarajan: So, obviously sir last time also we had clarified, any fund raising as far as Aurobindo is concerned right now is more strategic than for CAPEX or for improving our debt and even the factoring which has happened now, obviously the liquidity has improved, so it will be more strategic. So let me tell you just two things, one is, we are not in any hurry towards just doing for the sake of it. Second thing is, obviously, I do agree with you, at some point of time will put closer to that and move on with that.

Rakesh Jhunjhunwala: And you do not think that other than acquisition, in your normal business today in next year you should not commit more than $100 million CAPEX.

N. Govindarajan: Yes, sir.

Rakesh Jhunjhunwala: And what is it this year?

N. Govindarajan: This year, we had projected around Rs. 1,200 crores, plus or minus Rs. 100 crores. As we had mentioned earlier, it would be around Rs. 1,200 crores to Rs. 1,300 crores.

Rakesh Jhunjhunwala: So, that means next year Rs. 500 crores - Rs. 600 crores of additional…?

N. Govindarajan: That is right, sir.

Rakesh Jhunjhunwala: This is because of reduction in capital expenditure?

N. Govindarajan: That is right, sir.

Moderator: Thank you. Our next question is from the line of Surya Patra from PhillipCapital. Please go ahead.

Surya Patra: Sir, on the US business front we have indicated that around four odd launches have happened in oral segment. And in the recent quarters also, muted number of launches only possibly we have seen. So, whether we have launched all the products because our last three quarters around 45 to 50 odd approvals that we have seen, so whether we have launched all those or we do not see that all are like commercially viable products at this moment or what is the scenario there, sir?

Robert Cunard: Yes, at this point the vast majority we do see is commercially viable. And as I indicated, we have 19 that we have final approval on that we will be launching and monetizing over the next three quarters in oral segment. We are trying to focus and make sure we maintain our service levels, introduce the products and get the most out of the launches. They do come a little bit faster than expected as far as the FDA turnaround time, so we had some catching up to do as far as validation and manufacturing, but I think we are in a good position with that now, the facilities have been able to step up and we are in a good position to launch those over the next three quarters.

Surya Patra: So, what is the kind of price erosion for the base business that we are observing there in the US? From the gross margin levels we do not see major kind of pricing impact to our portfolio, but I think possibly some sort of compensation that we should be getting from the improving margins there in European business. So, at least what is the kind of pricing scenario or impact to that we are facing in our US business?

Robert Cunard: In regard to our regular oral solid business, it is within the range that we had kind of anticipated earlier this year that 4% to 6% erosion on the base business and that is about what we have seen. We have been able to offset a lot of that with additional gains in volume and some improvement in product mix. I anticipate that is about where it is going to be as we continue through the year, we currently do not have any significant bid cycles but there are somethings that will be coming up with the joint venture between Mckesson and Wal-Mart that could have some pricing impact in the market place. But, overall we still see that as upside for us based on our current presence in Wal-Mart and we think that that has some upside for us.

Surya Patra: And on the Injectable business front, are we on track to achieve something like $200 million kind of revenue in FY17 itself, because this quarter is something in the kind of targeted number?

Ronald Quadrel: What I had said in previous calls is that I was expecting to have a growth rate very similar, or higher than we had last year on a year-on-year basis. Our first quarter was about the same as fourth quarter last year. One of the main reasons why it was like that was, as you recall, we launched Eptifibatide I believe it was the last five weeks of the quarter. And when we launched Eptifibatide market was completely dry, Merck was out of the market. So when we launched Eptifibatide, the market really pulled a lot of our product through. So we had an inordinate amount of sales over that short period of time, and it was a lot higher than we expected. As a result over the first quarter, as customers went through their inventory, our sales on the Eptifibatide were a little bit lower. But as we have gone into the second quarter now, our Eptifibatide demand has gone up, and is back to the run rate that we expected it to. We are also seeing Isosulfan Blue starting to pickup, Demand for Pantoprazole, which we launched in the first quarter has also started to increase. So, I am anticipating over the next two quarters a significant growth rate. We have seven to eight products that we will be launching within the 60 to 90 days' period. Of those products about two-thirds are approved already and we are already manufacturing launch quantities. We are expecting behind these launches, we are going to have several more products that we will launch. So, I do expect we are going to grow. However, I would not comment on the $200 million mark, but we are going to have a significant year-on-year growth over last year.

Surya Patra: And on the Penem front we are expecting meropenem approval and launch very soon, so what is the progress on that front?

Ronald Quadrel: Yes, we are expecting approval very soon. We have been back and forth with the FDA regarding our ANDA, and we are preparing to start manufacturing our launch quantities. That way once we get our approval there is not a significant lag between

the approval time and the launch time. So, I would say within the next several months we will have an approval on Meropenem.

N. Govindarajan: Yes, just to add to what Ron said, Sanjeev can also clarify that Meropenem got approved in Europe and they have already launched the product as well. Sanjeev?

Sanjeev Dani: Yes, that is right. Actually Meropenem has been launched in UK and Germany and we expect next quarter to be launched in Italy.

Surya Patra: And how big is that opportunity in the entire Europe, sir?

Sanjeev Dani: We are already having existing sales actually, so we are just moving from Europe based sourcing to India based and that is significant part of sales of hospital business, but overall hospital business is only 11% - 12% of European base. So to that extent it is generic product.

Surya Patra: Just one last question, on the R&D front the kind of a number that 3% kind of the total revenue that we are spending on the R&D side, whereas we have many more complex projects on, so whether we should be seeing kind of a meaningful jump from here or it would be kind of a normalized level that we would be maintaining?

Govind: We expect it to be around 4% to 4.5% by the end of the year because it also depends on the timing of the bio-study or the limited clinical trials as well as the filing. So, depending on that we still expect by the end of the year this to reach around 4% to 4.5%.

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

Neha Manpuria: Just a follow-up on the 19 products for which we have got approval. While I understand you mentioned that obviously some of that approvals are faster than we had expected, therefore we are not really prepared for launch. Are there any other big reasons for this lag in our ability to launch products? And going forward, how are we looking at it, should the lag reduce in terms of when we get approval and when we launch the product in the US?

Robert Cunard: Yes, in addition to the speed of the approvals, Neha, we had a couple of things. As you know Unit-7 is a very significant site for us and a lot of these products were heading there and we had some very specific areas, types of manufacturing areas that we had some overlap. There has been some expansion there, there has been some other blocks brought online, we have had some product that we will be moving to the new dedicated facility in Naidupet so we have a lot of benefits that are coming,

we think we are in a much stronger position now to deal with the future approvals and we will be turning those much quicker.

Neha Manpuria: And my second question is, in the past two accounts you have mentioned that two of our, Aurobindo USA and other, subsidiary we have moved it to a SPV. Any specific reason for this change?

Santhanam Subramanian: There are two companies, one is, if you really see the AR company in which we are doing the factoring and another we have created to do the restructuring of the entire holding company which will take place in the coming quarters.

Neha Manpuria: Sorry, I did not get it. The AR is just a manufacturing facility?

Santhanam Subramanian: The first one AR is for the factoring.

Neha Manpuria: And the Aurobindo Pharma USA?

Santhanam Subramanian: Aurobindo Pharma USA, we want to structure the entire, because we are having now five businesses there, we want to restructure it so we created that.

Neha Manpuria: So there is no tax benefit or etc that we are looking from this?

Santhanam Subramanian: No.

Neha Manpuria: My last question, if I may. On Europe, how are we tracking in terms of profitability, has it improved from the numbers that we saw in the FY16?

Sanjeev Dani: As you know, Neha, when we had taken over the business in FY14 it was double-digit negative PAT; in FY16 we had turned positive on the PAT. And we are continuing to be on the guidance, in fact, slightly ahead of the curve in terms of our guidance of 7% to 8% EBITDA by FY18. So, I think we are on course there.

Moderator: Thank you. Our next question is from the line of Surjit Pal from Prabhudas Liladhar. Please go ahead.

Surjit Pal: Govind, just to say is that we did not expect so many approvals. And if I am not mistaken, roughly around 30% of your approval are not launched, including I think Vancomycin which is in shortage list and there are many demands on that. So, do you think it was lacunae in terms of production plan for the Company as well as capacity constraint in Unit-4?

N. Govindarajan: No, not at all. I think I would like to first of all clarify that, I think majority of the approvals which have not been launched is more oral than Injectable, or it would be equal rather

than skewed more towards Unit-4. But first of all, I would like to clarify that as we had mentioned last time there are three large reasons why we would not be launching immediately, the first one is like typically when a targeted action date is given I think we also have an internal discussion in terms of how realistic it is. To just give an example, one of the injectable products we had a targeted action date in August and we all had a call with the regulatory head and we found that it may not be August, we expected it to be December or January. And obviously, if you anticipate August you make the material and keep it ready, but if it is going to be pushed later we do not want to make the material in anticipation because the moment like the approval gets delayed your product gets ageing, which is not the most preferred part, even though it has definitive timeline in terms of its retest or expiry, we do not want to do that. That is one aspect of it. And also, it is more prudent to ensure that we are utilizing the capacity for something which can get into the market soon that is one aspect of it. The second aspect of it is, sometimes I think we also work on process improvement or change of source at API level because of which we have decided that it is not prudent to launch immediately after the approval comes, rather, we would apply for a change of source or improvement for old products which we have filed in the past. The third is, prioritization. If there are some opportunity or end use which has come up which is right now running full and even if there is a new product approval has come, but the opportunity is not really meaningful compared to the product which is already running, we would defer the new product. What I claim is not the capacity constraint but I would use the word reprioritization and in fact, Bob had explained in terms of reprioritization also we are now bringing down the time to launch when the approval comes by allocating new oral product exhibit to different site to keep some headroom in Unit-7. And that would be the same case around in Unit-4 as well. So, I would not see capacity as a challenge.

Surjit Pal: Capacity is not a challenge as per you?

N. Govindarajan: No.

Surjit Pal: So if that be the case, in your number three point of prioritization had that been the case then why your market share is almost at the bottom among the competitors, like Tricor, like Valcyte, like Patanol these are all the very key products, limited competition. One product you got on day one and your growth is nowhere. I mean, if I see your guys performance in terms of volume, in terms of price, the way you play, I mean, it is no where seen in these three big products.

N. Govindarajan: See, first of all, I would allow Bob to answer that and I will come back with on more specific answer to this, Surjit. Bob?

Robert Cunard: Yes, we may be looking at different data, I mean, for example Valganciclovir is one that was existing generic market that we entered, I think we are already at 10% early in to that and likewise we will see that continue to grow. One thing you have to understand is that there is inventory in the market place when we enter these, and that has to move through. Same with Olopatadine we had actually a late entry in that, we were about a week behind some of the other competitors. So, I really do not see us underperforming on that market share and I think it will continue to grow.

N. Govindarajan: And also just to add to what Bob said, Surjit please remember the fact that if you need to take a call between the market side and the pricing, it would be more skewed towards pricing than the market share as far as our colleagues are concerned and that has been consistently maintained in most of the products as well.

Surjit Pal: I just need to reassure that the Injectable revenue is still confident that you guys will double than FY16 what you achieved?

N. Govindarajan: Don't know we will double or not, definitely there will be a significant growth is something which Ron had clearly assured in terms of his statement. Ron, over to you.

Ronald Quadrel: Yes. I do believe we will have significant growth year-on-year, I believe last year we had about 39% - 40% growth year-on-year, and we will have more than that this year. Similar to last year, we started off slowly and as we went through the year, quarter-by-quarter we grew tremendously and I would think the same thing will happen this year. As I said earlier in the call when I was answering someone else's question, we are expecting to launch nine of the products over this next 60 to 90 days and some of those are fairly big products like Linezolid Esomeprazole, Acetylcysteine,and Levofloxacin. So, we will gain ground very quickly.

Surjit Pal: Last question, if I may. Govind, I need your view on CRESTOR the price horizon and the competition, how it is?

N. Govindarajan: As far as CRESTOR is concerned, we have good market share from a generic perspective. As far as pricing is concerned, yes it had significant erosion. But having said that, we are still happy with what we got.

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

Girish Bakhru: First question was actually on the expansion, if you could update on Naidupet and Vizag expansion, when is that completing?

N. Govindarajan: Sanjeev will clarify on Vijag. Sanjeev?

Sanjeev Dani: We have received the European GMP approval last quarter, and we have started receiving product by product approvals. We expect to ship out on a regular basis from January next year.

N. Govindarajan: And as far as Naidupet is concerned, right now the validation batches are getting initiated, Girish. And obviously one other thing you have to remember is, the commercialization of Naudipet we have to be conscious to ensure that we do not lose benefit of SEZ.

Girish Bakhru: So the non-US market contribution would be meaningful?

N. Govindarajan: Obviously what will happen Girish, as Sanjeev was explaining the Vizag unit is going to kick in soon which will ensure that we will be able to transfer products from Unit-7 into the particular facility

Girish Bakhru: And on the US side, if you could give the number of launches you did this quarter.

N. Govindarajan: Four is what we had mentioned, Girish.

Girish Bakhru: So, when you say 19 products which are approved and which can come in next few months, you are including Nexium, has that settled or litigation is still to close?

N. Govindarajan: Bob will clarify that on Nexium.

Robert Cunard: Yes, that will be in our fiscal third quarter, the October quarter.

Girish Bakhru: So, I am just trying to understand, would you include the products where your litigation, say, maybe on like Angiomax, Prilosec OTC, are these products in the 19?

Robert Cunard: 19 is just our oral solid and that does not include any products where there is outstanding litigation.

Ronald Quadrel: There is a whole other set of numbers with injectables.

Girish Bakhru: How many are injectables, then?

Ronald Quadrel: We have launched three this year so far, as I said before we probably have another nine that we are going to be launching in the next 60 to 90 days. Above and beyond these, depending on FDA and how fast the approvals come for the rest of the year, we will have more launches coming. But to reiterate, there is significant number of launches in the next 60 to 90 days.

Moderator: Thank you. Our next question is from the line of Shyam Srinivasan from Goldman Sachs. Please go ahead.

Shyam Srinivasan: I just needed a clarification here, because your presentation talks about seven new products in the US market in the first quarter, so is it four orals and three injectables?

N. Govindarajan: That is right.

Shyam Srinivasan: And also I wanted to know the timing of these products, was it towards the far end of the quarter because we have not seen sequentially the US business actually improve from a revenue perspective.

Robert Cunard: Yes, I guess on my side the two significant ones were in June, so it was later in the quarter. And again, as we are entering existing generic markets there is a little bit of a time lag there as we move through the incumbent inventory and some things. So, yes we did not have the full quarter effect with all the four that we launched on the oral solid side.

Ronald Quadrel: On the injectable side, Pantoprazole was launched early in the quarter, Levetiracetam and Dexmedetomidine were later in the quarter. Levetiracetam is seen as a smaller product. Dexmedetomidine sales are just starting to take off now as we are getting into the second quarter.

Shyam Srinivasan: My second question, I know you may not comment on the press articles regarding the inorganic acquisitions that the talks have been about, but from a company perspective, what are the kind of leverage ratios that you look at and at which you could be comfortable to do in terms of the deals?

N. Govindarajan: I will put it this way, I think keeping the inorganic opportunities aside for a minute, if you remember what Subu has been maintaining is I think we are comfortable with a 0.5 to 0.6 level in terms of the net debt to equity ratio and towards the end of the year it would be even better than that. Also let's assume some large opportunity comes up and if we do not do any fund raising also we would not be going beyond, let's say, ratio of one. So we are not under any pressure on that front.

Shyam Srinivasan: So you think one time net debt to equity?

N. Govindarajan: If it goes also I am saying, short-term, but ultimately our comfort will be 0.5 to 0.6 which we have been always maintaining.

Shyam Srinivasan: And my last question is on the margins, we have seen margins improve both sequentially and YoY, so just your thoughts on what is the outlook for the margins for the remainder of the year?

N. Govindarajan: So, our outlook for the next two quarters would be better than the first quarter based on visibility.

Shyam Srinivasan: Would you want to quantify?

N. Govindarajan: We do not quantify Shyam, you know that.

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

Karthik Mehta: So, just trying to understand from the gross margins basis, our API, so non-US overall contribution is also lower while we do not have the Q4 FY16 IndAS numbers, it apparently is maybe down by about 50 bps assuming that there is an increase in the US business. So, Govind how would one look at this in terms of the gross margin on the sequential level?

N. Govindarajan: So, first of all, I would not say that it has been lower, that is as far as gross margin is concerned. Subu, can you correct me?

Santhanam Subramanian: You are right Govind, we are at 56%.

N. Govindarajan: That is number one. Number two is going forward, let me give you some clarity in terms of ARV and API. As far as ARV is concerned, the subsequent quarters we expect the growth to be better than the first quarter. There are one or two products where we are seeing better business because of which we have even debottlenecked some capacities in both API and finished dosage as far as ARV is concerned. As far as API is concerned, even though we did not see a huge growth in terms of the top-line, the bottom-line has been meaningfully expanding, but you have to remember that at the end of the day that meaningful expansion and overall company may not be making a huge impact but definitely the margins in API is also expanding.

Karthik Mehta: And on R&D we have seen most of your peers expanding the expense in a very large way. So, if I have to look at it from FY18-19 whatever R&D expense really spikes to up like 8% of top-line in terms of the initiatives that we have now?

N. Govindarajan: So, this year we have guided around 4% to 4.5%, Kartik. And next year I think it would be even more than that. But then, would it reach 8% level, we do not see at this juncture but we also have to remember the fact that if there are few clinical trials happens together, it can certainly for one year go up but would not be the normalized way, we do not see like that forever.

Karthik Mehta: And on the tax rate, so what should we assume that number for the 2017 and 2018?

Santhanam Subramanian: We had a tax rate of around 25.6% this quarter, last year we ended this around 27.3%. We believe as the current trend goes, because Europe has been doing well and we are able to do better sales from Unit-7 etc, probably we will be around 27% or slightly less than 27%.

Karthik Mehta: Would that be the number we should take in FY18 also?

Santhanam Subramanian: I do not believe any reason why it should be more at this stage.

Moderator: Thank you. Our next question is from the line of Manoj Garg from Bank of America Merrill Lynch. Please go ahead.

Manoj Garg: Sir, this question is for Bob and Rob, basically on the US. Given the current visibility on the pipeline and the investment which you are making for the future, just would like to understand that while it is just a direction and I am not holding you for the guidance, but just from a direction perspective how do you see US business panning out over the next two to four years kind of timeframe?

Robert Cunard: Well, I think from our side on the traditional generic side we are still very bullish on the US business as far as where we have kind of aligned ourselves strategically on the customer side and I think we have pretty good visibility as this pipeline continues to come to reality and we get approval so we get those into the market place. I think there will be some significant changes in the US market with the distribution network and some different things which I think we are well positioned to take advantage of that.

Ronald Quadrel: On the Injectable business, I would expect the growth rate that we have coming this year, as I said before, should be at least the same or more than the growth rate we had year-on-year last year. We should be able to maintain that for several years out. Dependent upon when our larger oncology drugs hit and when the microspheres hit maybe three, three and a half years out, that growth could be more. But it is all dependent on the FDA and the order of approvals and how long they take on the individual mixture of products. As Govind has said, right now the addressable market for the microspheres that we are chasing is about $3 billion. We do not expect more than four competitors in there and dependent upon how aggressive they are in terms of pricing and how successful we are in gaining share, we can do quite well. So, again if you look at it, just to repeat myself, we could look at the same type of growth, but a little bit greater than we have year-on-year last year, for this year, the year after and probably the year after and then after that, it depends upon how the FDA does in terms of our other product approvals. But we do have quite a robust portfolio and I am fairly confident that we will be growing at a fairly significant rate through at least 2020 - 2021.

Manoj Garg: So, will it be fair if somebody would like to put some numbers behind that, that we are confident to have a healthy mid-teens kind of growth in the US business despite a $1 billion kind of base?

Robert Cunard: I think that is fair to say on our side, as we have talked in the past the growth rate is definitely slowing as that base continues to go up. And if the trend continues on the customer side and obviously on the product side, we would expect that there will be further price erosion and margin compression there. But I think we are well equipped to deal with that. I think we still have a lot of efficiency that we can recognize through our supply chain and working closer with our customers in that regard. And with our level of vertical integration we are in a good position to compete.

Ronald Quadrel: I would think too, as I said, with adding all these new products and growing year-on-year I believe that the percentage contribution of the Injectable business to the total US will continue to grow year-on-year to 2021 at least.

Manoj Garg: And Govind, if I heard properly, you spoke about that the margins would be better in the ensuing quarters compared to Q1 despite higher R&D spend. So, what will lead to that margin expansion, is it improving portfolio mix or operating leverage or is it sum total of both of the things?

N. Govindarajan: It is a combination, Manoj. First of all, I think we have heard both Bob and Ron in terms of this quarter launches, they have already mentioned about what is coming for the next two quarters. Over and above that, I think Europe has been still having good traction in terms of better than the curve whatever we had earlier anticipated. And ARV also there are some expansion in terms of both top-line and bottom-line possible. And over and above that, I think we have certain other new product launches which can really maintain this momentum. In fact, second quarter and third quarter in our opinion should be better than the first quarter.

Manoj Garg: And last question from my side, basically on the debt number what we spoke, if I heard it properly you spoke about $500 million kind of net debt by this year end, which may further come down next year given that we are towards the end of CAPEX cycle without any inorganic move.

N. Govindarajan: That is right, Manoj.

Manoj Garg: So, we are aiming for $500 by this year end, right?

N. Govindarajan: Yes. Also whatever Subu had mentioned we will maintain that, but what is more important to note is that next year it will be still better because obviously the CAPEX cycle is coming down which will propel us to bring down the debt further.

Manoj Garg: And sir, last question if I may. Particularly on the regulatory side, last time we had a pending form 483 at Unit-7, can you just update the status on that facility?

N. Govindarajan: We had received that Manoj, we had received EIR's for both the Unit-7 as well as Unit-12.

Manoj Garg: So now there is no pending 483 or open 483 at any process?

N. Govindarajan: I would put it this way, when you say pending EIR, I cannot say that there are no pending EIRs at all because there is a silicon audit which has happened recently, there is an Auronext audit which has happened. So if we take example of silicon, there are no observations and there are few observations in Auronext, which is not critical I would believe. Having said that, these EIR will take some time, so I cannot say nothing is pending.

Manoj Garg: But nothing material, like in terms of observations or any other issues?

N. Govindarajan: No, nothing material is our opinion.

Moderator: Thank you. Our next question is from the line of Prakash Agarwal from Axis Capital. Please go ahead.

Prakash Agarwal: Just trying to understand this better, in terms of this increase in debt, so what I understood was $35 million because of charge back, just trying to understand the P&L and balance sheet impact. So, have we recognized this in revenue? And is it lying in debtors and would this reverse or given the price erosion it is unlikely to reverse?

Santhanam Subramanian: See, we always book the sales, after netting out the charge backs. So there is no P&L impact at all, it is a question of funding impact, we have to make the charge backs lets say 15 to 30 days while the gross revenues will be realized anytime between 70 to 100 days. So, there is a working capital impact between 30th day and 70th or 100th day that is the only thing. There is no P&L impact at all.

Prakash Agarwal: So what I am trying to understand, the example you gave of 100 revenue booked and 70 being under liability, so would that $35 million recoupable or how is it?

Santhanam Subramanian: No. $35 million is the charge back which has been accrued as liability and paid out of that.

Prakash Agarwal: So, given the launch momentum it is going to pick-up further as Ron and Bob talked about 19 plus 9 launches going forward. How would this charge backs look like going forward?

Santhanam Subramanian: Because the launches which has happened already this will get stabilized and that will fund the additional launches. And in any case Govind has explained the program we have entered into, we are not looking for any short-term, I mean, we will operate with the existing fund availability for the existing operation.

Prakash Agarwal: So, this is going to normalize and further reduce basically?

Santhanam Subramanian: Get normalized over a period because we have been launching product continuously in the last six months.

Prakash Agarwal: And secondly on the approval to launches, so we had about 49 final approvals last year with 28 launches, have we covered most of the critical launches for the last year approval?

Robert Cunard: We do have a couple of residual, if you remember last quarter we talked about seven, two of those were launched this quarter and the balance will be launched over the next two quarters.

Prakash Agarwal: So, any material products, if you could mention which are yet to be launched?

Ronald Quadrel: From my side, the vancomycin would be the more material launch, but as Govind mentioned earlier, we probably will launch vancomycin in the second half of the year once our capacity building is complete.

Prakash Agarwal: And the orals?

Robert Cunard: I do not see any significant material products that have not been launched at this point in comparison to some of the ones which are coming like Esomeprazole. And once again, they are entering existing space.

Prakash Agarwal: And just a thought on the Europe consolidation. We have all talked about US in the past, even we hear that Europe is consolidating and we being among the top 10 players. So, how do we see our position in the next three years, do we need to add more product portfolio going forward? So if you could just give broad level highlights there.

Sanjeev Dani: We are obviously focused right now on improving profitability. The next lever of growth will come from the new products which are being developed. Currently, we have almost 200 products under development for Europe alone and that will be launched over next three to four years and that will be the driver of growth.

Prakash Agarwal: So it is not fair to assume that there could be a sizable acquisition to get scale and size to be among the top three, among the consolidation and gain the consolidation phase?

Sanjeev Dani: See, this is a part of our assessment and evaluation process constantly, in fact, we neither rule out nor we rule in anything.

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

Nitin Agarwal: Subu, just to clarify the debt amount, the net debt number that you mentioned, so when you say $500 million of net debt by the end of the year, I mean, are we taking into account the factoring facilities or this is like a pre-factoring debt, I mean, how should we look at that?

Santhanam Subramanian: Same thing, whatever we have said like-to-like only we are talking, $525 million we are moving towards $500 million and as on date we are working on $500 million.

Nitin Agarwal: Which was $525 million as of June quarter end?

Santhanam Subramanian: Correct.

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

Sameer Baisiwala: Govind, just strategically speaking, how do you think about branded business, because that is sort of a missing piece in our overall business.

N. Govindarajan: Yes, so we are looking at it Sameer, but please understand the fact, unfortunately the opportunities that are available on brands are too high in terms of the expectation. So, we are evaluating that and we will continue to evaluate for the right opportunity and explore that that's my answer.

Sameer Baisiwala: And which markets are you referring?

N. Govindarajan: See, to give an example in Europe, I mean Sanjeev can clarify, thanks to the previous acquisitions there are some branded products available with us, not actually meaningful. So, obviously I mean when we explore it will be for both US and Europe.

Sameer Baisiwala: But I was also asking about the emerging market and critical market such as India, but this piece of business is something that can grow for 10, 20, 30 years.

N. Govindarajan: Unfortunately, you know pertaining to India like post one particular transaction in the past the expectations have moved out of bounds. So, obviously when that cools down I think that would also be an interesting market to look at. But having said that, I think we at this juncture have not looked at anything, but if any opportunity comes in we will evaluate based on our prioritization.

Sameer Baisiwala: And second question is for those 19 pending launches, you mentioned the addressable market is $6.8 billion, how much of this is you are counting for nexium?

Robert Cunard: Nexium is about $3.8bn of that.

Sameer Baisiwala: And just a final one, in general what is a typical conversion from target action date to approvals and what is the time gap between the two?

N. Govindarajan: I think Bob and Ron can answer that.

Ronald Quadrel: That is pretty hard to say, it varies from product to product and what we find with the FDA is each product has a different review team and each review team has its own characteristics. So, there are times when the action date comes, we are near approval; other times we receive additional questions. So there is really no correlation from product to product, at least not in the Injectable business.

Robert Cunard: Yes, I would agree with exactly what Ron said on our side, what we see as well. And those targeted action dates can be a complete response letter or it can go right to the final approval. We just do not know until we start to see the output from the agency.

Moderator: Thank you. Ladies and Gentlemen, due to paucity of time, we will be taking the last question from the line of Jigar Walia from OHM Group. Please go ahead.

Jigar Walia: Just a couple of questions. So, if you can give the Natrol numbers for this quarter and margins? And second question is, Unit-4 are we expecting any inspection this year?

N. Govindarajan: Subu, you want to give the Natrol numbers? I will put it this way, we have been maintaining the margins, and top-line you have Subu? We will get back on that, Jigar, later.

Jigar Walia: And on Unit-4?

Ronald Quadrel: We are expecting the FDA should be coming in at any time. We always have the FDA in one of our plants anytime during the year and we are due for another inspection with the FDA in Unit-4, last one was about two years ago.

Deepika Gupta Padhi: Just to add, Natrol number is $28.3 million for the quarter.

Moderator: Thank you. I would now like to hand over the conference to Deepika Gupta Padhi for her closing comments.

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

Moderator: Thank you very much, Members of the Management. Ladies and Gentlemen, on behalf of Aurobindo Pharma Limited, that concludes this conference call. Thank you for joining us and you may now disconnect your lines.