Jubilant Life Sciences Q4 & FY 2014 Earnings Conference Call Transcript

May 26, 2014

Ravi Agrawal: Thank you. A very good evening to you all. I am Ravi Agrawal – Head of Investor Relations at Jubilant Life Sciences. Thank you for joining us today on the Q4 & FY 2014 Earnings Conference Call. We have on the call today Mr. Shyam S. Bhartia – our Chairman and Managing Director; Mr. Hari S. Bhartia – our Co-Chairman and Managing Director; and Mr. Sankaraiah – our Executive Director, Finance.

We will commence with opening remarks from Mr. Shyam Bhartia on our businesses, operating environment and the outlook. Mr. Sankaraiah will follow with a discussion on financial highlights during the quarter and full-year period. Subsequently we shall then open the session for Q&A.

Before we proceed I would like to remind you that some of the statements made on the call today could be forward-looking in nature and a detailed disclaimer in this regard has been included in the 'Investor' presentation that has been shared on our website.

I now invite Mr. Bhartia to share his thoughts with you.

Shyam S. Bhartia: Thank you, Ravi and Good Evening to all of you. I am pleased to report key aspects of Jubilant's performance.

In Q4 FY 2014 income from operations was at Rs.1,562 crore, up 12% YoY. Reported EBITDA stood at Rs. 251 crore, giving a margin of 16.1%. Our margins during the quarter and full year were impacted by the effects of the warning letters in our CMO business. Our revenues from the international market grew 8% YoY at Rs.1,160 crore, contributing 74% to overall revenues. The share of regulated market stood at 58% with contribution from North America at 37%, and from Europe and Japan at 21%.

During the full year, our income from operations stood at Rs. 5,803 crore, up 12% since last year. Reported EBITDA stood at Rs.1,027 crore with margins at 17.7%. International market showed 13% growth YoY with 75% in overall revenues. The regulated market share in the revenues stood at

60% with North America contributing 38%, Europe and Japan contributing 21% to the mix.

Coming to our Business Segments. In Q4 FY 2014 our Pharmaceutical segment revenues were at Rs. 705 crore with a share of 45% of the overall revenues. In FY 2014, our Pharma revenues stood at Rs. 2,728 crore with a share of 47% to the overall revenues. Within Pharmaceutical segment, our Generic business grew 9% during the quarter, and 5% in year FY 2014 led by volume growth in key products in Solid Dosage Formulations. We have robust pipeline of 455 filings pending approval including 37 ANDAs in US in our Solid Dosage Formulations business. Our strategy includes undertaking multiple launches where we have received approvals for products. Newer geographies are being tapped simultaneously.

In Active Pharmaceutical Ingredients – continued cost reduction through processes and yield improvement led to lower cost of products, higher output and continued high margins. Various cost reduction and yield improvement endeavors will continue. We have systematically prioritized leadership in key products in API business and this philosophy is helping us to grow.

Our CMO of Sterile Injectable business faced challenges in FY 2014 from warning letters in our contract manufacturing operations. As you are aware, we saw successful resolution of the Montreal warning letter during the quarter. In Spokane, we have responded to all FDA observations. There is a new management team in place, and we have strengthened our quality management system and organizational reporting. The advisory team including industry experts are working to expedite the resolution of US FDA issues. We have also extended the plant shutdown of 3 weeks in Q1 FY 2015 to implement identified enhancements to existing system for better compliance.

Our Radiopharmaceuticals business saw a good growth during the quarter on the back of price increases from some of our key products. Our expected launch of Ruby-fill in FY 2015 will further augment growth in this business. In the last quarter, we sold our Hospital business to Narayana Health on a going concern basis as slump sale. This exit will enable Jubilant Life Sciences to focus on its core businesses in Pharmaceuticals and Life Sciences.

Life Science Ingredients segment contributed revenues of Rs.858 crore in Q4 FY 2014 thereby growing 24% YoY having 55% share in the overall revenues. In FY 2014, the revenues stood at 23% higher at Rs.3,076 crore, contributing 53% to the overall revenues.

During the quarter, our Advanced Intermediates and Specialty Ingredients business grew 19% on a YoY basis. With stable realization in Pyridine, our order booking has seen healthy increment. We are witnessing growth in our key markets including China. The demand for Symtet remains healthy and simultaneously the manufacturing capacity is seeing improvement in utilization levels. We are building good orders position backed by favorable feedback from our customers.

The Nutrition Products business continues to benefit from gains in pricing and we announced 18% increase in Niacin Feed-grade price during the quarter. We are now operating at full capacity.

Our Life Sciences Chemicals business is giving us good opportunities in Europe, which has been a focus of our geographical expansion. We remain focused on leveraging our cost advantages to maintain a leadership profile in the business. We are pursuing higher presence in the export markets of South East Asia and some other markets. We have seen volume growth and price hikes in key products.

In terms of outlook for FY 2015, we will continue to witness some of the good performance in our key businesses with growth accruing in both revenues and EBITDA. The recent stability in the exchange rate will have a positive impact on the profits of the company, and we hope that this stability continues.

Our Pharmaceutical segment should benefit from new launches in both existing and new geographies in our Generic business. As regards our CMO of Sterile Injectable business we expect our new quality management system and various advisory team engagements will expedite the resolution of Spokane warning letter. We are confident of bringing back our growth in this business on the back of strong order book and better compliance. The Radiopharmaceuticals business should benefit from the expected launch of Ruby-fill and robust pricing of various products in FY 2015.

Our Life Science Ingredients segment will show growth based on volumes enhancement and gains in pricing. Entry in newer geographies for our key products is another aspect that we are pursuing which is showing good results. Our investment in value-added products is yielding the expected performance with Symtet receiving praises from some large and prominent customers, and we expect to achieve better capacity utilization in Symtet. Our Vitamins business is poised to register further benefits from price improvements that have been implemented by us.

A healthier profile will result in a stronger cash generation, augmenting our balance sheet further. We continue to look at avenues to normalize our debt obligations.

We are in the process of consolidation of our Pharmaceutical business under Jubilant Pharma Limited, Singapore. I am happy to inform that the IFC financing of US$200 million will enable the company to achieve its objective. IFC financing is a combination of a 7-year term loan financing of US$87.5 million and US$60 million zero coupon optionally convertible loan having a tenure of 6-years and US$52 million loan for 5-years to be syndicated by IFC.

I am happy to report that Board of Directors has recommended a dividend of 300% or Rs.3 per equity share of Re.1. This will result in an outgo of Rs.55.9 crore including dividend distribution tax.

I would now invite Mr. Sankaraiah to continue the discussions with his thoughts on financial performance of the company. Thank you.

R. Sankaraiah: Thank you Mr. Bhartia, and I thank everyone for joining the call today. Let me walk you through the financial highlights for Q4 FY 2014.

During the quarter, income from operations was at Rs.1,562 crore, an increase of 12% YoY. This can be attributed to 2% price improvement and 10% exchange gain. The EBITDA for the quarter stood at Rs.251 crore giving us a margin of 16.1% which was adversely affected by the warning letter in CMO business in Montreal and Spokane. In Q4 FY 2014 the reported profit after tax stood at Rs.99 crore which includes an exceptional gain of Rs.36 crore. The normalized profit after tax was Rs.62 crore, normalized EPS for the quarter stood at Rs.3.92 paise per equity share of Rs.1 each.

During the quarter, the income from operations for the Pharmaceutical segment stood at Rs.705 crore contributing 45% to the overall revenues. The growth in this segment is driven by robust volume growth in Solid Dosage Formulations and price uptick in Radiopharmaceuticals. The EBITDA for the quarter was at Rs.132 crore, translating to an EBITDA margin of 18.8%. During the quarter, we saw the successful resolution of Montreal warning letter, divested our Hospital business to Narayana Healthcare to focus on our core competencies in the Pharmaceutical and Life Science Ingredients segment, and took strategic price adjustment for few Radiopharmaceuticals products.

In the Life Science Ingredients segment, income from operations increased by 24% YoY to Rs.858 crore contributing 55% to the revenue mix. During the quarter, we announced the price increase of 18% for Niacin Feed Grade. The EBITDA in the segment was Rs.131 crore giving an EBITDA margin of 15.3%.

Moving to FY 2014 performance. Income from operations stood at Rs.5,803 crore, an increase of 12% YoY. This includes 6% volume growth and 7% exchange gain. During the year, the EBITDA stood at Rs.1,027 crore giving us EBITDA margin at 17.7%. As mentioned our margins were impacted by the warning letters received in the CMO business, and expected price pressure in the Solid Dosage Formulations business. Reported profit for FY 2014 stood at Rs.109 crore and a normalized profit after tax was Rs.324 crore and a corresponding normalized EPS stood at Rs.20.31 per equity share of Re.1 each.

Let me now provide you with an update on the segment wise performance. In the Pharmaceutical segment income from operations stood at Rs.2,728 crore, contributing 47% to the overall revenue. The EBITDA for this segment was at Rs.610 crore with EBITDA margin of 22.4%. Growth in this segment is driven by Specialty Pharmaceuticals and Generic business.

Moving to the Life Science Ingredients segment, income from operations were at Rs.3,076 crore, growing 23% YoY. This segment now contributes 53% to the overall revenue. The EBITDA stood at Rs.483 crore translating to an EBITDA margin of 15.7%. All our businesses in these segments have demonstrated good volume growth and price improvements.

Let me now discuss some key balance sheet figures. As of 31st March 2014 our net debt stood at Rs.3,913 crore. Of this, the long term debt of Rs.2,301 crore and the working capital requirement stood at Rs.1,612 crore. Taking into account the foreign exchange differential, the net debt stood at Rs.3,653 crore as compared to Rs.3,838 crore as on December 31st 2013. We continue to focus on reduction of debt and we are committed to meeting all our repayments on time.

Our blended interest rates for FY 2014 is at 6.9%, the rate of rupee borrowing at 12%, and foreign currency borrowing at 4% approximately. In FY 2014 we have spent about Rs.150 crore on CAPEX as against the earlier estimate of Rs.250 crore, and also incurred Rs.126 crore on product development expenditure. This underlines our strict control on CAPEX and we will continue to do the same going forward to generate cash to reduce our borrowing levels.

Going forward we expect strong growth momentum in both the segments of our businesses. The Pharmaceutical business is expected to deliver on account of resolution of warning letter in Montreal, focused attention to resolve US FDA issue in Spokane, consolidation of global quality system for compliance, new product launches in Generic business and better price realization and expected launch of Ruby-fill in Radiopharmaceuticals business. Growth in Life Science Ingredients business will be led by higher capacity utilization, better pricing and entry into new geographies. With these comments, I would request the moderator to open the lines for Q&A please.

Moderator: Thank you very much sir. We will now begin the question-and-answer session. We will wait for a moment while the question queue assembles.

Saion Mukherjee: This Is Saion here from Nomura. Sir just on CAPEX what was the number for FY 2014 including the product development number?

R. Sankaraiah: It is Rs.276 crore including product development.

Saion Mukherjee: And product development would be around Rs.100 crore…?

R. Sankaraiah: Rs.126 crore because we have bought one molecule specifically under product development from outside.

Saion Mukherjee: And Sir how do you expect this to be for fiscal ’15?

R. Sankaraiah: Like about Rs.100 crore we have spent less during this year that is getting spilled over to next year, so totally this year we expect about Rs.200 crore of the new CAPEX and about Rs.100 crore of carryforward, totally about Rs.300 crore CAPEX and another Rs.100 crore of product development. But as we have committed, Saion, if you see for both the years put together we are very well within the commitment.

Saion Mukherjee: Sir for the next year in terms of growth and the pricing environment if you can just take us through like the price hikes that you have taken Niacinamide and Nutrition business, have you already seen the impact coming or it will come in a subsequent quarter? And also the opportunity on Ruby-fill if you can just throw some light on the market share competition and how should we think about that, and when do you expect that product to get approved exactly, and how do you expect the market share ramp up?

R. Sankaraiah: As far as Niacin is concerned the price increase, as you are aware. We have done the press release also, we have increased the price for Feed Grade about 18%.

Shyam S. Bhartia: And some price increase is already done in first quarter but the full impact will come from the second quarter.

R. Sankaraiah: As far as Ruby-fill is concerned, we expect to launch this in Q3 FY 2015, and we are very much encouraged with the response on that product, and like you know very much it is a 505 B2 product which is having a very good market potential, so we expect that to be launched in Q3.

Shyam S. Bhartia: Our plant inspection was done for the Rubidium Generator, and the plant inspection was approved, but of course the product approval we expect to come by third quarter.

Saion Mukherjee: Sir, what could be the revenue potential from this product?

Shyam S. Bhartia: Product wise we do not want to share those details, Saion. We expect a very good potential for this. If you have seen our press release earlier we have already mentioned it will be more than $70 million market size of the product. How much we can take share out of that and all those things depends upon the market and also the entry level.

Saion Mukherjee: And sir finally on Symtet, where do we stand in terms of ramp up, what exactly is the nature of the problem, I mean, there has been a lot of delay on ramping it up, so if you can throw some light?

R. Sankaraiah: As far as Symtet is concerned see last year we had a capacity of about like we mentioned about 2,000 tonnes, this year we expect to double the capacity. Whereas from the marketing side we have a very good pricing on this product because we are the single supplier for this product as of today, and there is a long-term contract which has been signed with big agrochemical companies, and the market prices are far better than the feasibility that we had taken. We have to get that product cracking properly then the potential is huge here again.

Saion Mukherjee: Basically you are saying that you expect the sales volume to double next year?

R. Sankaraiah: Yes, that is right.

Saion Mukherjee: So it is basically a process related issue which is a bottleneck, is it?

R. Sankaraiah: It is a process-related issue. Correct.

Saion Mukherjee: I mean you had a capacity from Symtet, right but what I understand was that we were not getting a stable product?

Shyam S. Bhartia: No, whatever we are getting we are supplying to large companies, there is no problem in the quality of the product.

Saion Mukherjee: What would it take to expand the capacity?

Shyam S. Bhartia: We have identified different areas where we have to strengthen the capacity and that is being done but it will take about 2 years to achieve that.

Saion Mukherjee: But because there is a market demand then can we not expedite that?

R. Sankaraiah: Saion, the management is taking all the required steps for doing that because we know the market is there very much and it is a very good profitable product and we are the single source supplier also, but only thing is the product output what we are supposed to get in the capacity of the plant against what we have put up so far as of today has not been achieved, so that is where we are trying to get the capacity utilization better.

Saion Mukherjee: You are not giving a guidance but you expect in terms of growth and margin FY 2015 will be better than FY 2014?

R. Sankaraiah: Very simple, Saion – clearly, we are not giving any guidance but like I mentioned in the speech also there are 5 or 6 points where we expect a better performance compared to the current year because in the Pharmaceutical business we expect to deliver a better result in CMO business on account of resolution of warning letter which has already been done in Montreal and the issues which has been raised by FDA we are focused to resolve that, in fact, what we have done is at the management level we have done a consolidation of the global quality system for better compliance so that is going to really create a good compliance compared to the previous year. Also in Generic products you know we have a very good pipeline, new product launches in the Generic business which is going to add to the contribution. In addition to that, on a select product in Radiopharmaceuticals business where we were able to increase the price, and also, as we just now mentioned that Ruby-fill is expected to get launched in Q3 FY 2015.

So with all this positive movement which is happening in the business we expect Pharmaceutical business to deliver better performance than last year. In case of Life Science Ingredients, the capacity utilization will be better, be it Symtet, in case of Niacinamide we are almost utilizing the capacity full, but otherwise the Advanced Intermediates and Fine Chemicals in those areas our capacity utilization will be better. Also in Life Science Ingredients business we have capacity, we are getting into new geographies which is going to expand the sales and also thereby the margins. So overall because of the various qualitative comments which I made just now we expect the performance of next year to be better than last year.

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

Chirag Dagli: Sir have the Radiopharma price hikes kicked in fully for the 4th quarter?

R. Sankaraiah: No.

Chirag Dagli: In terms of the full extent or in terms of more price hikes that will happen eventually?

R. Sankaraiah: No, it is not just mere price hikes. It is because of the products we have, we are in a very enviable position and we are single source suppliers for many products in Radiopharmaceuticals business, so that way we are very comfortable in the growth going forward in that business. So the impact of the price increases and all those things will happen full year going forward.

Chirag Dagli: But we have taken these in the fourth quarter, is it sir?

R. Sankaraiah: I do not want to further elaborate on all these things, we are in a very good position.

Chirag Dagli: And secondly Sir, did we say in the opening remarks that we are going to take a plant shut down at Spokane?

R. Sankaraiah: That was a normal plant shut down which is usually we used to take in the first quarter. So what we have taken in the opportunity is during the normal shut down we have extended the shut down for a few more weeks, thereby to put all the necessary FDA requirement systems in place for a better compliance.

Chirag Dagli: So this applies to just Spokane or to Montreal as well?

R. Sankaraiah: The warning letter has already been lifted for Montreal and the normal operations have started, this is only in Spokane.

Chirag Dagli: Sir just to understand the IFC funding, this is effectively just debt funding right?

R. Sankaraiah: Like Mr. Bhartia in his speech he has mentioned it is about $87.5 million of debt which is a 7-year debt and $60 million of convertible, which will be converted at the time of either private equity coming into the business or at the time of may be any listing which happens, they have the option to convert it. So as of today this $60 million is a 6-year loan with a zero coupon.

Chirag Dagli: This is in Jubilant Pharma?

R. Sankaraiah: Jubilant Pharma Singapore, and that money ultimately will come to Jubilant Life Science for moving the assets of API and Dosage Form business from Life Science to Jubilant Pharma Singapore. Just to remind you, Jubilant Pharma is 100% held by Jubilant Life Science.

Chirag Dagli: And over and above this, there is another US$52 million loan?

R. Sankaraiah US$52 million loan is something which IFC will syndicate over a period of time.

Chirag Dagli: And sir, what will be the interest rate on this US$52 million for five years and US$87.5 million for seven years?

R. Sankaraiah Seven years is at LIBOR+450.

Chirag Dagli: And the other one?

R. Sankaraiah At the time of syndication we will know.

Chirag Dagli: But this should not be very different from what our current 4%?

R. Sankaraiah Since the tenor is less it should be little less.

Chirag Dagli: So the equity raising can still happen eventually and of course, IFC will get an exit at that point in time?

R. Sankaraiah Correct.

Moderator: Thank you. The next question is from the line of Shubhankar Ojha from SKS Capital & Research. Please go ahead.

Shubhankar Ojha: In the outlook you have said that you are targeting a debt-to-EBITDA ratio of2.5x. So, how we are going to achieve this – can you just give a guideline on how the debt reduction is going to happen and basically the multiple is going to be achieved because right now we are almost 3.5x, and bringing it down to 2.5x is quite a task?

R. Sankaraiah In the medium term we wanted to reduce it but ultimately our objective is in the level of less than 2.5x that is what we wanted to achieve. So, the whole thing is that like just now I mentioned we have a commitment that we will bring in equity within 3-5 years, to IFC also when they are funding this facility. So, ultimately, out of operating cash flows like you already noticed, we have a strict control on capital expenditure and also the cash flows with ultimate objective to reduce the overall debt of the Company and that task will continue. Over and above that maybe at the right time in Jubilant Pharma, the Singapore company, we have to bring in some equity thereby our balance sheet will be strengthened very much.

Shubhankar Ojha: And the money that has come to your Singapore Jubilant Pharma basically, so that will ultimately come to India for the transfer of the Indian business?

R. Sankaraiah Correct.

Shubhankar Ojha: And ultimately you are going to list that?

R. Sankaraiah: Ultimately, we will use that money to repay the debt of Indian company.

Moderator: Thank you. The next question is from the line of Bhavin Shah from Gee Cee Investments. Please go ahead.

Bhavin Shah: Just to reiterate my question, the debt figure what is the quantum of reduction that you are looking for next year – should it be about Rs.200-300 crore?

R. Sankaraiah: I will not be in a position to put a number for all these things because since we have not given a guidance we cannot talk about that.

Bhavin Shah: Just in a ballpark range, what is it that you are looking at?

R. Sankaraiah: We have already given you a clear indication that in medium term our comfort level of retaining the debt is less than 2.5x of EBITDA.

Moderator: Thank you. Ladies and gentlemen, that was our last question. I now hand the floor over to Mr. Bhartia for closing comments.

R. Sankaraiah: Thank you.

Shyam S. Bhatia: Thank you so much. Mr. Modi must be swearing in now. So we hope for the good future. If you have any further questions, we will be happy to answer, Mr. Sankaraiah, Mr. Ravi Agrawal and I are happy to address any query of yours.

Moderator: Thank you. Ladies and gentlemen, on behalf of Jubilant Life Sciences Limited, that concludes this conference call. Thank you for joining us.