“Piramal Pharma Limited

Q2 FY '25 Earnings Conference Call”

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Moderator: Ladies and gentlemen, good day and welcome to Piramal Pharma Limited Q2 FY '25 Earnings 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 the star then zero on your touch-down phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Gagan Borana from Piramal Pharma Limited. Thank you, and over to you, sir.

Gagan Borana: Thank you, Steve. Good evening, everyone. I welcome you all to our post results earnings conference call to discuss our Q2 and H1 FY '25 results. Our results material have been uploaded on our website, and you may like to download and refer them during our discussion. The discussion today may include some forward-looking statements, and these must be viewed in conjunction with the risks that our business faces. On the call today, we have with us Ms. Nandini Piramal, Chairperson, Piramal Pharma; Mr. Peter DeYoung, CEO of Global Pharma; and Mr. Vivek Valsaraj:, CFO of our company. With that, I would like to hand it over to Ms. Nandini Piramal to share her thoughts.

Nandini Piramal: Good day, everyone, and thank you for joining us on our post results earnings call. Before I begin, I'd like to thank all of you who attended our Investor Day on the 24th of September. For those of you who could not attend, please note a copy of the detailed presentation and the recording is available on our website.

I'm pleased to share we've delivered yet another quarter of healthy revenue growth accompanied by margin expansion thereby carrying forward the momentum which we have built over the last few quarters. Our revenues during the quarter grew by 17% year-on-year, with an EBITDA margin of 18%, indicating an expansion of about 150 basis points year-on-year. This has been primarily driven by consistent growth in our CDMO business, which has witnessed an uptick in revenues from innovation-related work, especially from on-patent commercial manufacturing.

In the CHG business, we continue to witness good volume growth in our inhalation anaesthesia portfolio in the U.S. and emerging markets. In the ICH business, our power brands continued to grow at a strong double-digit rate backed via trade and media efforts.

Thus, we have seen a good overall performance across all our business verticals. During the quarter, we released our FY 2024 Sustainability Report, giving an overview of our progress in the area of sustainable operations. The report follows GRI standards and is aligned with SASSP and UNGC frameworks. It also highlights our commitment to reduce our greenhouse gas emissions in line with the science-based targets initiative, 1.5-degree decarbonization pathway.

Moving on to business-specific highlights. Starting with our CDMO business. This was another robust quarter for our CDMO business with year-on-year growth -- revenue growth of 24%, accompanied by EBITDA margin expansion. This is the 6th consecutive quarter of

strong growth and margin expansion for our CDMO business, both the challenging times that we faced in FY '22 and FY '23 in account of the COVID 19 pandemic, geopolitical disturbances, high inflation environment and suppressed by tech funding environment.

The growth has been mainly led by strong traction in innovation-related work, particularly the on-patent commercial manufacturing projects, leveraging our strong execution capabilities and the global network of facilities, we continue to emerge as a trusted partner for our customers and are seeing a steady inflow of new orders.

In terms of the market outlook for the CDMO industry, the overall biotech funding has improved over the previous years but remains uneven across months. Regulatory changes such as the Bioseure Act, and consideration for supply chain diversification are driving customer inquiries and visits. However, we continue to see a wider request for proposal processes and the delayed decision-making by the customer.

We expect these tailwinds of improved biotech funding and supply chain diversification to gradually play out over the medium term, and are, therefore, making adequate investments in our capacities and capabilities, especially in the areas of differentiated service offerings such as ADC, HP API, sterile fill finish and peptides.

We have recently announced a strategic investment of $80 million to expand of sterile fill-finish facility in Lexington. This will more than double our current capacity of the plant and is expected to commercialize by the end of FY 2027. The site specialized and sterile compounding, liquid filling, and lyophilization of sterile injectable products, playing a vital role in Piramal's integrated antibody drug conjugate development and manufacturing programs, ADCelerate.

The injectables market has shown a steady expansion in recent years, and there's a current demand and supply gap. This expansion will enable the Lexington site to capitalize on this opportunity and establish itself as a key player in the segment. Multiple customers plan to commercialize their products post expansion of this facility. Our generic API business has seen a good pickup in demand during the first half of the financial year, complementing our growth in innovation-related work, driven by robust revenue growth, coupled with our continuous efforts towards cost optimization, operational excellence initiatives, we are seeing a steady improvement in our CDMO business EBITDA margins.

Going ahead, we will continue to focus on customer delight with superior execution, which will help us drive cross-selling opportunities in repeat business. Our global network of facilities, along with strong product management skills aims to increase the share of integrated projects. With timely capex investments, we look forward to capitalizing on growth opportunities, which, however, as they pan out in the CDMO industry.

Moving to our complex hospital generics. During the first half of the year, we continue to see a steady volume growth in inhalation anaesthesia products in the U.S. and emerging markets. The volume growth backed by vertical integration and cost optimization initiatives has helped us to support healthy EBITDA margins in our CHG business.

To further grow our Sevoflurane franchise in the rest of world markets, we have embarked upon our capacity expansion plans at our facilities in Digwal and Dahej. We're putting up new manufacturing lines of Sevoflurane in Digwal facility, which will complement our current Sevoflurane manufacturing capacities at Bethlehem in the U.S. also to ensuring vertical integration of this expanded capacities, we're also increasing the KSM manufacturing capacity at the Dahej site in Gujarat.

In the injectable pain management system segment, our growth remained slow due to supply constraints. However, we are taking multiple initiatives to strengthen the supply chain and these initiatives are gradually yielding results. In the intrathecal segment, we continue to defend our leadership position in the Baclofen market in the U.S. with over 70% market share.

Going forward, we are investing in portfolio expansion to build a portfolio of differentiated and specialty products, which can leverage our existing customer relationships and sales force to drive long-term profitable growth. We have witnessed good success in differentiated products such as Gablofen, Mitigo, Neatricon and would like to build on our experience.

Moving on to our India Consumer Healthcare business. In our ICH business, our power brands delivered a strong growth of 18% during the quarter and half year, taking its contribution to 48% of sales. Brands such as CIR, Little's and Tetmosol delivered a strong double-digit growth rate, while the growth in i-range was impacted due to is being bought under price control. We continue to invest in media and trade promotions to support the growth in our power brands. Our new product launches have also played an important role in driving growth in recent times.

Over the last 4 years, we have launched close to 200 new products in SKU, which we pilot on the e-commerce channel before rolling them out in the general trade. Our sales in the e-commerce platform has seen the significant contributors to our growth with online sales growing by over 30% year-on-year during the first half of the financial year contributing to about 20% of ICH soon.

We are also present on over 22-plus leading e-commerce platform, which allows us to accelerate our new product launches. Our focus is on improving the profitability of e-commerce led by pricing mix and investment optimization. Going forward, we're looking to widen our distribution network transitioning from a pharmacy dominant to an omnichannel consumer healthcare company. We're looking to expand our presence in smaller towns and also maximize our distribution across hyper super standalone modern trade outlet.

Summarizing the quarter. Our businesses have delivered a good all round performance during the quarter in first half of the financial year. Our CDMO business is growing well with an increasing share of innovation-related work, differentiated services and integrated orders. Our CHG business continues to see a good volume-led growth in inhalation anaesthesia products, while our power brands and consumer business are growing at a healthy rate.

The EBITDA continues to outgrow the revenue growth, driven by operating leverage and

cost optimization initiatives. We reiterate our guidance for the year to deliver early teens growth in revenue and EBITDA and meaningful improvement in PAT. We hope to continue this momentum as we strive to achieve our long-term target of becoming a US$2 billion revenue global pharma health and wellness company by FY30 with a 25% EBITDA margin and a 1x net debt-to-EBITDA ratio. With this, I'd like to open the floor for the Q&A. Thank you.

Moderator: Thank you very much. We will now begin the question-and-answer session. The first question is from the line of Vinod Jain from WF Advisors. Please go ahead.

Vinod Jain: Yes. My question is only related to the taxation. Why is the tax incident so high in the quarter?

Vivek Valsaraj: So Vinod, incidentally, the quantum of revenue and profitability from taxpaying jurisdictions in the first half has been high. And this is -- compared to our overseas, this has been high because of which the absolute value of tax outflow is high which is reflected in the quarter's financials.

Vinod Jain: Okay.

Moderator: Does that answer your question, Mr. Vinod.

Vinod Jain: Yes. That answers the question.

Moderator: Okay. Thank you. The next question is from the line of Yasser. Please go ahead. Mr. Yasser your line has been unmated. Please go ahead with your question.

Yasser: Yes. I mean, could you help us sort of understand the opportunity for Neoatricon in terms of the market size and in terms of the opportunity that Piramal has and the marketing agreement that we have with BrePco Biopharma?

Peter DeYoung: So we don't describe a lot of detail beyond what would already be in the public domain, but what we would like to highlight is that this particular product filled the gap for dosing of a certain age of infants and neonatals which the alternatives require some manual effort by the healthcare practitioner to do the dosing which could result in dosing errors or adverse events related to the dosing errors.

So this is going to have exclusivity with the regulator because we invested along with the partner into developing the data to allow this presentation and we're in the process of developing the market access and launch strategies as we speak. And so we would anticipate this to benefit us in the coming quarters and we would show it up in aggregate numbers, but we don't typically describe individual product market sizes or specific arrangements we have with individual partners such as Brepco that we mentioned.

But we remain excited about the product because we think it is an example of the differentiated or specialty product offering because of the nature of the presentation what we are offering, can't be offered by other people and it solves the problem that was previously present.

Yasser: Are we expecting to launch a few more parts of the differentiated products?

Peter DeYoung: So I think Jeff would have described in the Investor Day that this is our plan to start to add more products of this category to our offerings. If you look at some of our already present offerings, you could argue that Gablofen and Mitigo would also be in the same category. And so this would be the third one of this streak or this category and we would expect to have our pipeline provide more of those in the future. These do take a bit longer to implement and they do take a little bit more on the investment side.

And this is a renewed focus in line with our new strategy that came along as Jeff joined our organization. And so we would anticipate this to play out more in the medium to long term, and we would expect a string of these to happen, but they won't all be in successive quarters.

Moderator: Thank you. The next question is from the line of Gopinath from PNR Investments. Please go ahead.

Gopinath: Ma'am I want to know what is the amount that the company has paid to the Piramal family as royalty in this quarter?

Vivek Valsaraj: So, Gopinath, as per the agreement that we had the royalty paid is 0.75% of the turnover of the company and this is benchmarked and validated as arms length and approved by the Audit Committee as per the positions required.

Gopinath: Can I know the amount, please?

Vivek Valsaraj: Just hold on around INR15 crores.

Gopinath: INR15 crores. Thank you. That's it from my side.

Moderator: Thank you. The next question is from the line of Yash Darak with RSPN Ventures. Please go ahead.

Yash Darak: So the employee expenses is around INR580 crores and it is now INR560 crores. Is it the run rate for the FY'25 year or are you expecting it to increase?

Vivek Valsaraj: Yash, could you please repeat, your voice is cracking up a bit.

Yash Darak: Hello. Can you hear me?

Gagan Borana: Yes. Was your question related to employee costs?

Yash Darak: Yes. Is the run rate is going to continue?

Vivek Valsaraj: No. So are you referring to the run rate?

Yash Darak: Yes, of the employee costs.

Vivek Valsaraj: Broadly it will be in this range. There may be some ups and downs depending upon any provision for incentives for the quarter, but broadly it will be in this range.

Yash Darak: Okay. Thank you. And with regards to effective tax rate, can you guide on to the whole year effective tax rate?

Vivek Valsaraj: So, Yash, firstly, the tax that we pay is standard in line with the tax applicable in the respective jurisdictions. So 25% for India and likewise for U.S. Currently, the tax looks high because the outflow of profitability and hence tax in those jurisdictions where we operate has been higher. Overall, the effective tax rate will be higher as we have guided during the beginning of the year to be in the range of 50-plus percentage. It may be slightly higher than that, but it will still be higher.

Yash Darak: Okay. Thank you so much.

Moderator: Thank you. The next question is from the line of Abdul Khader from ICICI Securities. Please go ahead.

Abdulkader Puranwala: So if you could just provide some color on how the innovative CDMO order book is shaping up. And I know vis-à-vis where we were a couple of quarters ago and in terms of new inquiries, what are the kind of inquiries are we talking about -- receiving from the customers? And when we talk about the sterile fill-finish, is the GLP-1 fill-finish also something what we may target in the near future as well?

Peter DeYoung: So first of all, we've had a reasonably good order flows over the last few quarters, as we indicated on prior calls and in particular for our on-patent commercial products which has been enabling our current performance. That being said, we have also mentioned and I think the trend is continuing that the biotech funding is impacting some of the earlier stage or development projects for some of our potential and current clients.

And so I think that overall trend that we described in the beginning of the year has continued without any major change because the funding environment hasn't materially changed from, let's say, at the beginning of the calendar year to now. That being said, we have a lot of customer inquiries, a lot of customer visits and the number of open RFPs would be materially higher than last year. And we think that's in part due to both the macro trends of the higher funding this year versus last year and the geopolitical de-risking that clients are or potential clients are evaluating.

And as such, we see they're running wider processes for potential alternative CDMO partners and they're also taking longer to decide. We expect this to culminate in decisions in the coming quarter and quarters and we anticipate an improvement in the order flow translating to order booking, but we can't exactly predict when because of the factors I just mentioned. Specifically in the area of sterile, we see strong demand, both with customers that have already placed their product at our Lexington site and anticipate increased volumes as they progress through the clinic registration and launch.

And in addition we have a - it's one of our sites with the highest number of open RFPs across our network because of a little bit of a supply demand inbound at the moment, in part driven by as you mentioned, the GLP scenario. That being said, that side does lie out and liquid for sterile, but it does not vials, but it does not have the particular dosage formats most used for

GLP-1. So we would have an indirect benefit, not a direct benefit from that opportunity at that site.

Abdulkader Puranwala: Got it, sir. And the next question is on the guidance. When you're talking about -- I mean, I think we are being a little conservative when we talk about reiterating our earlier guidance of early teen growth in revenue and EBITDA, considering we have done well -- or we have done quite better as compared to that already in the first half. So any reason for being a little conservative? Or we may look forward to upgrade our guidance in quarters ahead?

Vivek Valsaraj: Firstly, as Nandini mentioned, we are reiterating our annual guidance of what we gave at the beginning of the year. In the first half, we benefited from some favourable phasing of orders and some forex gain, some of which could change -- the forex gain could change depending upon how the currency moves in the subsequent part of the year. In the absolute value, the H2 EBITDA will continue to be higher than what it was in H1 and the way it has been in the prior years. A large portion of the one-off spends that we have flagged in our consumer complex hospital generics business, which we had guided at the beginning of the year will actually get spent some time in quarter 3.

And quarter 3 will also see some variation in the mix, which may have an impact on the margins within quarter 3, but quarter 4 will continue to be the largest quarter that we have. So as of now, we believe that we will be able to meet the guidance is, of course, going to be an endeavour to try and exceed, but we are not changing the guidance at this point in time.

Abdulkader Puranwala Got it. And a final one on the bookkeeping side. So we talk about the mix improving towards innovative CDMO business. But if I look at the gross margins for the quarter, there has been, I say, nearly 220 bps dip in your gross margins on a Y-o-Y basis. So could you help me understand the reason for the shift in gross margins for the quarter?

Vivek Valsaraj: Abdul, the previous year quarter 2 gross margin is not very representative. So I don't know if you were on the call last year in quarter 2, we had called out to say that the gross margin in the previous year was an aberration due to a high quantum of inventory overhead leading to a credit in the P&L, which subsequently got reversed in the subsequent quarters. If you look at our half year gross margin, you will see that it was 65%, which is in line with the previous year and more representative of what the normalized gross margins will be.

Moderator: The next question is from the line of Harsh Bhatia from Bandhan Mutual Funds.

Harsh Bhatia: Just in terms of the comment for Q3, the variation in terms of the mix -- so when you look at the Q2 numbers, this is a very normalized level of business that we are seeing across all the segments? Or has there been any change or variation in the numbers. I understand that your H2, as you mentioned, will be heavier than H1, but has there been any certain specific movement in Q2? Or is this in line with your anticipation?

Vivek Valsaraj: Harsh, the business and especially the CDMO part of the business does tend to get a little lumpier across the quarter. So typically, in the prior year, you would have seen that Q3 and Q4 tend to be bigger quarters that come back to Q1 and Q2. This time within quarter 2, we've had a more mix of innovative products leading to a different margin profile, which could

possibly change within quarter 3.

So, over the quarters, there may be some variations. As always, urge you to look at the YTD figures. So when we look at our quarter 3 as well, we should actually look at the 9-month figure to get a more normalized view of our performance.

Harsh Bhatia: Okay. And just to clarify 1 or 2 quarters back, we had this price cut or rather driving pressure on the hospital generics space from the competitor. So is there some impact on this quarter as well? Because I believe in the last 1-2 quarters, we had certain impact from that particular product price?

Peter DeYoung: I think as we may have discussed on our prior earnings call, I don't know if you were on that, I think you were, the pricing event happened with a particular product in the U.S. with 1 GPO and that event happened and became effective more in the Q3 of last fiscal year over that period of that quarter.

And so then when you do year-on-year comparisons that will show up 4 quarters afterwards. And so we would anticipate that most of that would have been the year would have passed at the end of this quarter.

Harsh Bhatia: So there is some element of that incremental costing in pricing pressure in this quarter as well? Or that has already been conserved.

Peter DeYoung: For that particular pricing event that we discussed, this would be the quarter that just ended, it would be the last quarter with a full quarter would have been impacted. There may be some partial effect next quarter.

Harsh Bhatia: Could you quantify the amount that you would have taken, if it's possible?

Peter DeYoung: We don't typically do that level of granularity on individual price contracts. So, I would advise against that other than, that was a factor that will show up in our commentary for 4 quarters. And I think now we're probably going to move beyond that.

Harsh Bhatia: And lastly, on this Lexington capacity expansion, you have made a comment on the press release, customer led $80 million expansion, just paraphrasing, is there some amount of capex that is going to be supported by the customer or other customers? Or is it going to be entirely done through our balance sheet?

Peter DeYoung: It's done through accruals and loans. The mention behind that is that this is not speculative capex, which is built in anticipation of future orders. This is capex that -- we already have customers who have trusted us with their most important programs at the site. And in order for us to meet the volume forecast they anticipate as they progress, we would need the expansion to accommodate that. And so in partnership with them, we have pursued the extension, but they are not providing us with the capex funding for it. That's through accruals and bank loans.

Harsh Bhatia: Yes. That's very helpful. To clarify what you made as a statement to the earlier question with

the other participant, I mentioned as an indirect benefit from that particular opportunity in terms of the GLP-1 and the supply-demand situation, the indirect part of it is because you are only catering to the part of the value chain? Or is there some other reason? I'm not able to...

Peter DeYoung: This generally been a lot of capacity soaked up from the innovators wanting to get fill-finish capability for their GLP-1 from CDMOs internal capacity and even certain corporate M&A actions that have changed the availability of CDMO alternatives, and that has created a little bit of a capacity gap in the market.

And some lines have been retooled or repurposed for those requirements. And some of those actions may have made certain alternative CDMOs less attractive to potential clients. And so we're seeing that demand in parts spill over to what we're doing at our facility for vials. But to be clear, we can't make prefilled surges or cartridges at that facility, and so we wouldn't directly participate. Does that help explain it?

Harsh Bhatia: Okay. Okay. Okay. So this is purely a fill-finish expansion we are targeting.

Peter DeYoung: Yes.

Moderator: The next question is from the line of Bharat Sheth from Quest Investment.

Bharat Sheth: Congratulations on the excellent performance. My question -- first question is related to CDMO. Can you share the mix of our discovery business and commercial and...

Vivek Valsaraj: Bharat, can you just repeat the question once again?

Bharat Sheth: In our CDMO business, the contribution of the mix of discovery and commercial business?

Vivek Valsaraj: So discovery typically is about 5% of the total. Another 25% is development. So discovery development together is 30% and the balance 70% is commericial.

Peter DeYoung: We get those numbers once a year. We don't have -- because there can be lumpiness between quarters. So we find it more effective to give an annual update on that. So the numbers Vivek shared were for the fiscal year ending March.

Bharat Sheth: And based on our pipeline, how do we see by the next couple of years, how this will -- change will mix -- will move?

Vivek Valsaraj: So Bharat given the fact that commercial business typically tends to be much higher in value, the mix will not significantly alter over the period. It's the sheer size of commercial business that will still remain a dominant part of the business.

Bharat Sheth: Okay. And one bookkeeping question. If you try to derive, I mean, from console and standalone, we see that our rest of the all subsidiaries, despite there is a Y-o-Y sales growth, but EBITDA margin has declined. So can you throw more light on that? What has really happened in other subsidiaries or that EBITDA margin has declined Y-o-Y?

Vivek Valsaraj: So, Bharat, it's more a question of skewness in sales between H1 and H2. The stand-alone

components had a higher quantum of sales happening in H1. The consolidated overseas components will have higher quantum of sales and EBITDA happening in H2. And typically, that's been case in prior years as well. They do have a higher Q3 and Q4 component. So as much progress in the rest of the year, you will see that improving.

Bharat Sheth: So my question was, I mean, if I compare it to this current year or current quarter Y-o-Y, then there is a decline also what I've observed.

Vivek Valsaraj: It is because of the skewness being more skewed towards the later part of the year. There will be some correction that you will see in the subsequent quarter.

Bharat Sheth: Sorry. My question is related to last year's Q2 EBITDA margin -- was the rest of the subsidiary was higher than the reported in the current quarter?

Vivek Valsaraj: Yes, Bharat, I'm explaining the same thing that this time the skew is more towards H2 than it was in the prior year because of which the skew is more accurate.

Bharat Sheth: Sir, I'll take it separately.

Vivek Valsaraj: Thank you.

Moderator: Thank you. The next question is from the line of Shahzad Shroff from Demeter Advisors. Please go ahead.

Shahzad Shroff: I just had one. I was looking at your annual report, and I wanted to understand a couple of line items within your other income. One is your write-back of liability is no longer payable and the other is miscellaneous income. So I just wanted to understand what these items are? And how should we think about it going forward? Are they referring -- Yes, that's it.

Vivek Valsaraj: So basically, as we analyze and review provisions over a period of time, there will be certain provisions which are no longer required, which typically gets reversed in the other income. And that happens periodically depending upon what provisions get exhausted and periodic review of the same.

With respect to miscellaneous income, there is a host of other things which could come in. It could be interest income on the investment that you make to pass your cash or it could be related to some other state of scrap or other items. So this could vary at most of other items that are included there.

Moderator: The next question is from the line of Ashish Kabra an Individual Investor.

Ashish Kabra: Congratulations on a great set of numbers. I just want to -- just build on that, that you said that Q3 and Q4 are on a historical level, they are better than Q1 and Q2. But since this year's Q2, you said that the mix was different. Do you still think that Q3 and Q4 of this financial will be greater than Q1 and Q2?

Vivek Valsaraj: Yes, Ashish, the absolute value of EBITDA generated in Q3 and Q4 this year will be higher than the absolute values EBITDA generated in Q1 and Q2.

Ashish Kabra: Okay, sir. And sir, 1 thing the way Piramal Pharma is growing, the guidance that you gave for FY '30, can you -- do you feel that in subsequent years, we have to actually -- you have to relook at the guidance and that can be met before FY '30?

Nandini Piramal: Let's get closer to that, then we'll see. And if we have to revise upward, then we will do that. But right now, we will keep it as it is.

Ashish Kabra: Congratulations on a great set of numbers.

Moderator: As there are no further questions from the participants, I now hand the conference over to Mr. Gagan Borana for the closing comments.

Gagan Borana Thank you very much. We appreciate you taking time to join us for today's call. In case you have any further queries, please get in touch with us. Thank you. Have a good day.

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