"Eris Lifesciences Q4 FY19 Results Conference Call"

May 21, 2019

MANAGEMENT: **MR. AMIT BAKSHI – CHAIRMAN & MANAGING DIRECTOR, ERIS LIFESCIENCES LIMITED**
MR. HIMANSHU SHAH – EXECUTIVE DIRECTOR, ERIS LIFESCIENCES LIMITED
MR. SACHIN SHAH – CFO, ERIS LIFESCIENCES LIMITED

MODERATOR: **REPRESENTATIVE OF FACILITY PROVIDOR**

Moderator: Ladies and gentlemen, good day and welcome to the Eris Lifesciences Q4 FY19 Results Conference Call hosted by Axis Capital Limited. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' and then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Prakash Agarwal of Axis Capital Limited. Thank you and over to you Mr. Agarwal.

Prakash Agarwal: Thanks. I welcome you all on behalf of Axis Capital to the Q4 fiscal 19 Eris Lifesciences concall represented by the senior management. Over to you sir.

Amit Bakshi: Thank you, Prakash. Good evening everybody. Since this is the year ending call, I would request some time for me to take you over through couple of slides. These are the same slides which we have put in the presentation as the presentation for quarter 4 and FY19. So, I am just following the slides giving you a broad indication of what is to be told and then we will move into question and answer session.

So, FY19, from a business highlight point of view, we had a substantial high growth in H2 which is 16.7% versus 9.9% for IPM after a slow growth in H119 which was 2.4% versus 9.3% for the IPM, this I am quoting the AIOCD numbers. For quarter 4, our growth has been 22.3% vis-à-vis 9.9% for IPM, so slow growth in H1 and the last quarter in the preceding year has been fairly compensated in the last 2 quarters and if I only talk about H2 19, we are now as per AIOCD growing at 16.7%.

Second important thing is business has become more chronic in nature than ever. In FY16, I think we were 18% of acute which has now come to only 15%, so 85% of the business is now either chronic or subchronic. Other important things were couple of new collaborations, so you know past year with Medtronic for diabetes monitoring device called Guardian. I have also told that we will be launching blood pressure meter which has happened. We have just launched the blood pressure meter. This is in collaboration with Microlife with the brand name of CIRCA 120/80 Exclusio and Premier in India.

In this year, we would be launching the 3 products which have been inlicenced, two of them should be commercialized byQ2 20 a month here and there and one of them would be the first time in India which will go through the regulatory approval depending upon the classification, it might take between 6 months to two years. We had a substantial inventory reduction in the last quarter. Internally, we figure out that we would have high reduction of at least 25 crores in the last quarter. This reduction was majorly done to streamline the inventory. Since the secondary growth had picked up, we wanted the inventories to come in line. You know that there has been pressure post GST on inventory management, so we took this step in the last quarter.

Last year, we also had discontinuation of one of our brand which was Triglimisave LS which was the leader in its own in the brand category and approximately in the last year, we would have lost 20 crores on account of Triglimisave LS discontinuation which happened approximately in the month of June. The Kinedex acquisition has been completed, we bought over the remaining ~17.81% and now it is a completely owned company. Also, in April 2019 we prepaid the entire term loan once again achieving a debt-free status, so that was more from a highlight point of view. Now, I will go to quarter 4.

Before that, I must inform you that Financial Express CFO of the Year Award was conferred to Sachin Shah and we are all very happy about it. Not only that, we also got the National Best Employer Brand of the year. It was a big exercise and we made it in between 100 brands.

Now coming straight to Q4 19, as I have alluded that we had cut inventory in our mind that number should be close to 25 crores and because of that the Q 4 FY19 growth is at 1.5%. EBITDA went down 624 crores from 717 crores, so PAT margins were at 25% , so this is more or less how we figured out in quarter 4. Numbers are there in the presentation. These are broad numbers.

We have actually broken down the sales into each and every bucket for a deep understanding of everybody and since it is year end, we just wanted to give feel across everything, so in the standalone, we have grown by 2.4%. In the base business of Eris excluding Strides we have grown by 4% and Strides has degrown by 5.1%. In the subsidiary, Aprica has grown by 44%, Aprica actually took this exercise last quarter where they reduced the inventory, so it is a base effect probably but we are seeing a good handsome growth there also. Kinedex has degrown by 40% in the fourth quarter. So, this is about quarter 4. As I told you, it was 86% chronic, the chronic therapies grew by 5% and acute therapies degrew by 15%year on year in the last quarter.

Now coming to FY19, FY19 on the whole we grew by 17% on the topline. The gross margins were at 84.4% which are exactly what they were in the last year which signifies that after taking all the other businesses including the businesses which we had bought, we have been able to bring them to the same gross margin level. This has largely happened because of the pruning of the portfolio which is high margin and high growth category. The Operating EBIDTA for the year stands at around 345 crores with a growth of around 7%. Margins are at around 31.4% vis-à-vis 34%. As you know that the last piece of the sale actually contributes more than 70% to the bottomline, so that is where you see this disturbance.

On the expenses side, there has been an increase in the HR, it has been basically because the people which we took in Strides was the reflection of only 5 months in the last year which has now been to 12 months. That is the major component of that increase which you see. The net profit margin had been around 30% which have come down from 34% last year. Now, very importantly, let me break down the sales in different entities. So, base sales for the last year had been at 724 crores which has been a growth of around 7%. Strides has been at 158 crores this year, Aprica 46 crores, Kinedex 40 crores and UTH which is within UTH has been 1 crore.

That is how the numbers are, so the base business growth has been subdued largely because of two components, one is the inventory correction which we took in quarter 4 and the other is the discontinuation of Triglimisave LS. If I try and put these two things together, then the way IPM is reflecting around 9% consolidated growth, our base business growth, which is more chronic, is around 12 to 12.5%, if I try and normalize these 2 caveats**.**

As I told you, we have become more chronic, so 85% of the sales in the last year has been chronic. The chronic has grown by 20% while acute therapies have grown by 4% and once again, I reiterate that acute therapy has now become only 15% of the total portfolio. The growth, as far as the AIOCD, the secondary growth as I mentioned in the start that we are happy to inform you that we have not only come back in the growth trajectory, but are once again delivering secondary growth which are industry-beating, so we are more often than not, we are in the top three fastest growing companies among the top 30 companies in the last one quarters. Besides that, the chronic business, the base business has been growing better between all other businesses and Strides as a business is also showing a growth which is a tad better than the base business.

Our prescription ranking remained unchanged or have got a little better. We continued to hold fourth rank in cardiology, 3 in diabetology, 3 in gastro, 6 in CP physician practice and fourth in Neurology. This is as per the SMSRC February 19 data, MAT February 19 data. Of course, it is on our own portfolio on our own markets.

Other very important and good aspect of the sales of the last year is that the top 10 brands of us which has contributed 63% to the total sales, 6 out of those 10 brands has grown more than the industry. The two brands which have not done best, one is Rabonik which is the PPI, which has grown by 3.2% vis-à-vis 7.6% of the market and one is Tayo which is our brand of vitamin D which has degrown by 1% when the market has grown 11%. We have taken remedial steps for Tayo immediately because this is our flagship brand. Other than the number one brand, mother brand of us which is Glimisave which contributes to Rs. 220 crores annually have grown by 13% vis-a-vis 11.5%. Telmisartan, our brand Eritel has grown by 18% vis-a-vis 17%, Olmin has grown by 10% vis-a-vis 8.7%. Tendia, Teneligliptan is now at 60 crore brands has grown by 36% which is at par with the market. So, even at a larger base, the market share has been intact. Renerve is 60 crores and 3.6% growth. there is a caveat, this is only AIOCD based data, internally Renerve has done far better, Remylin at 55 crores, 14% vis-a-vis 8%. Rabonik, I told you, Tayo I told you, Ln Bloc at par with the market more or less and Cyblex which is our anti-diabetic 40 crores, it is 51% vis-a-vis 12%. So, if you look at the share of the top 10 brands, they have done relatively better than the market, but if you cut out again two half, H1 and H2, H2 would have been very significant over H1, so the point which I am trying to say is it is the H2 actually wherein the team actually came up and the business got back to track.

We are now 2000 people, so number doesn't really change. We were in the same vicinity last year. The YTM is 4.1 lakh per person. In the presentation, we have some charts which basically talk about how the revenue had grown over the last 4 to 5 financial years and it is there for everybody to see. This more or less is what I want you to tell and we are able to take question from your side.

Moderator: Thank you very much sir. Ladies and gentlemen, we will now begin the question and answer session. We have our first question from the line of Anubhav Agrawal from Credit Suisse. Please go ahead.

Anubhav Agrawal: Sir, just one clarity, this 25 crores number that you mentioned on inventory rationalization, can you just roughly help how was this distributed between Strides and your base portfolio?

Amit Bakshi: Look I haven’t done that maths, but look at the proportion of the sales between the two and I think that would be a fair calculation both sides.

Anubhav Agrawal: Because I was asking that Strides sales are down from 42 crores in third quarter to 29 crores now. That is like 30% sales down. Normally fourth quarter is weak, but not more than 10% typically, so that is why I was asking that such a sharp decline in Strides sales that is the reason I was asking out of 25, if I do proportionally still the decline in sales is very high in Strides portfolio. Would you say third quarter was abnormally high number for you?

Amit Bakshi: If you look at the total number which you are putting up is around 158, so if I do 158 divided by 12, the average is 13.16, so 14 from 13.16 is not very high, so we haven’t done the number between both of this, but we were close to landing at around 164, 168. That was the number which was in our mind if we wouldn't have done the inventory correction.

Anubhav Agrawal: And can you just take us, GST related inventory correction doing now, what is the reason if so long after this, you suddenly decided to take this inventory right of now? What happened? What triggered this?

Amit Bakshi: Anubhav, honestly, we didn’t have the headroom to do this earlier because the secondary growth were not progressing the way we would have liked to. So, if you could have done it at that point of time, the fall would have been steeper, so we just waited for the time when the growth actually comes back, so we thought that this is the right time for us, so that this year from next year, we move up in a symmetrical manner.

Anubhav Agrawal: What were your channel inventory days earlier versus what is now?

Amit Bakshi: Internally, it is very difficult to, we don’t get the stock and sale statement from everybody, so the numbers which I am going to tell you is based on 60 to 65% of what we collect and then there is an extrapolation. So, I think we were this transit, we were at 44 to 45 days roughly, these are all numbers roughly but they make sense and if 25 crores goes down, then I think 4 days is something which we would have corrected.

Anubhav Agrawal: Amit Bhai, I have not understood, what was so pressing need of this correcting 4 days, you are saying that the liberty was at your side when to correct it, so the channel was really not pressing for it, so what is the need?

Amit Bakshi: We would have applied extra force to put this up and that we didn't want to do. 44 is not a good number anymore, it was something which was right a couple of quarters back or years back. Now the good number is 35, 36.

Anubhav Agrawal: So, that means you will take further 4 days correction at some point of time?

Amit Bakshi: It depends. What happens is it is a two-way metrix. If the growth is better, then what happens, lot of accommodation happens because of the growth, so if we grow by that 18 to 20% which is showing in the market, then the correction would be automatic. It works both ways.

Anubhav Agrawal: And just one clarity on Triglimisave LS, I was assuming that you would have shifted prescription from this combination drug to your other, let us say, similar molecules, so when you show a loss of 20 crores, that is not net loss to you. That is just loss from that brand but this would not be total impact on sales for you, right?

Amit Bakshi: We wish it would have happened, but finally this is about prescription. It takes a long time for these kinds of market to come together, it takes 3 to 4 years and also remember what has happened is when Triglimisave was building up, these shipped gliptins were not in the market, so lot has changed, Triglimisave LS adds for the market and we were the brand leader in the lower strength, so technically how much have I gained in Triglimisave I don't know; but has it shifted? It has not even shifted 25%.

Anubhav Agrawal: So, you would say that this quarter would have at least 3 crore kind of loss just because of the Triglimisave kind of impact?

Amit Bakshi: 4-4.5 crores.

Anubhav Agrawal: No, but 25%, you would have shifted, 5 crore is total gross.

Amit Bakshi: Yes. Total is this. But 25% is the best case scenario, which I'm telling you.

Moderator: We have a next question from the line of Mr. Prakash Agarwal from Axis Capital. Please go ahead.

Prakash Agarwal: Sir, if you could just highlight on the outlook, how do we see the fiscal '20 as the growth in fiscal '19 has been a tad lower because of external reasons? If you could just throw some light on the outlook, a. And b, how big are these in-licensing opportunities?

Amit Bakshi: Okay. So,2 of 3 in-licensing opportunities are not a game changer. The game changer what we assume is something, which will take 6 months to 2 years depending upon the regulatory classifications. The two, which we are getting, are only incremental in nature. So, I don't expect any opportunity from these 2 categories. That's on the other side. The first side is, largely, Prakash, we would like to reiterate that we will beat the market by a decent 30% to 50%. And there is a tailwind in the brand, and there is a tailwind in the overall portfolio also. And if the market remains, it becomes a little more buoyant because last month, there was a stark difference. One data showed around 9.5%. The other data showed 13%. So, we don't know which one is more closer to the reality. But if the market comes back to 13%, as was indicated by IMS, then the growth would be much higher. If it remains at 9%, 10%, then we will try and aim for that 30% to 50% ahead of the market.

Prakash Agarwal: Okay. Understood. And secondly, since you achieved debt-free status, what are your plans for fiscal '20 in terms of any spots that you want to fill up? Or what are your thoughts in terms of utilization of cash flow?

Amit Bakshi: So, from a capital point of view, you know there is something which is just coming up in Guwahati, which is incremental in nature, so there is some allocation which has happened on that site. As far as acquisition is concerned, we have nothing in sight as of now. So, acquisition doesn't seem to be happening because we have not even started at this point of time. But we will be building up laterally, so there is a plan of having more portfolios. So, there will be brand launches, and then there will be some addition in people and new therapy lines. So, it will be more of organic till the time we find an opportunity for acquisition.

Prakash Agarwal: And lastly, on the CAPEX, you mentioned there's something in Guwahati. So, what was the CAPEX last year and this year?

Amit Bakshi: Sachin will answer this.

Sachin Shah: The CAPEX last year was around 35 crores. Not Guwahati. Guwahati was around 1 crore only last year. And this year, we are planning around 35 crores in Guwahati.

Prakash Agarwal: So, 35 crores was not last year, 1 crore was fiscal '19. You are expecting it to go to 35 crores for fiscal '20.

Amit Bakshi: Yes. We are getting a plant for soft gels and we are also getting a smaller unit for nutraceuticals also. That should get us around 8% to 10% of manufacturing inhouse for us.

Prakash Agarwal: Okay. And this will be construction for '20 and revenue generating for '21. Would that be fair to understand?

Amit Bakshi: , the sales should come from the quarter 4, but being a little pessimistic let's assume for next year, quarter 1.FY 21

Moderator: We have next question from the line of Duby Rex from Ithought Financial. Please go ahead.

Duby Rex: Sir, do we have any export breakup in the sales this year? And do we have any plans to export in the future?

Amit Bakshi: No, not as yet. Neither we have any revenue from export, neither there is any plan to export.

Moderator: We have our next question from the line of Ashish Thapkar from Motilal Oswal. Please go ahead.

Ashish Thapkar: Yes. So, sir, for Guwahati, look, whatever site plans for that we were about to do for Strides in-house, has that happened? And if not, when? And if that happened, is there a scope for gross margin expansion?

Amit Bakshi: Yes. So, Ashish, that is what exactly what Sachin answered, that pessimistically we will start producing from Guwahati in the fourth quarter. And before that, we have a brand, which is a 60 crores product, which we will shift to Guwahati. So, then all these things happened. So, 60 crore advantage will come, I think, very soon. And Strides' advantage will actually kick in from the fourth quarter. If 60 crores come in, then there will be a gain, both the sides. And once the whole thing is actioned, then we will be at the stage where we started, when 85% was inside manufacturing . So, we hope to reach the same stage when the Guwahati is functioning completely.

Ashish Thapkar: Okay. Got it. And in terms of the employee costs and the other expenses in terms of absolute numbers for FY '19, as far as the Strides integration is concerned, everything is in the cost. And what's your outlook there for the next 1 or 2 years? Say, for example, other expenses like almost like 290 crores and even employee cost is 190 crore. So, like all the integration has been done and what would you like to guide on?

Amit Bakshi: So, we will maintain that we would look at an additional up to roughly around 200 people across the year. That's what has been the guidance. And that is what we are keeping in mind at this point of time. So, for all practical purpose, assume that we will add 200, 250 people during the current fiscal. And over and above, we don't expect anything significant at this point of time.

Ashish Thapkar: Another thing, softgel and in nutrition side of the businesses, like we have an inorganic portfolio? Or how will I look at that?

Amit Bakshi: So, softgel, Ashish, one large brand, Renerve Plus, is in a softgel formulation. So, when it comes inhouse, we are roughly doing 6.5 crores monthly on that, 6.5 crores, 7 crores monthly on that. And that's going well. So, once that comes inside, that is the leverage we were talking about.

Moderator: We have next question from the line of Tushar Manudhane from Motilal Oswal Financial Services. Please go ahead.

Tushar Manudhane: Sir, just coming back to gross margin. We are already at 84.4%. And with this inhouse transfer, if you can just quantify what can be the further improvement in gross margin for FY '21 full year basis?

Amit Bakshi: I won't really expect, any major increment from there. If we are there, that's what we are planning.

Tushar Manudhane: Okay. And you also referred to some new therapy to add, so if you can further elaborate on that.

Amit Bakshi: Okay. So, we have launched the blood pressure meter, as I alluded in my presentation. And we are just 1 month in the market. So, that's one business which we have already started. The other business, which we have started is the cosmetology business, but that is on a very small scale. We only have 15, 18 people because the portfolio which we want will only come in, in the third quarter, so we scale up in the third quarter.

Tushar Manudhane: Sir, which therapy you referred to? I'm so sorry, I missed it.

Amit Bakshi: Cosmetology. Yes. And incrementally, we are adding some people in the neurosciences business. That business is showing good traction. So, incrementally, we are adding some people in the neurosciences. And as of now, this is the plan.

Tushar Manudhane: And sir, any impact of this trade generics on the growth or on the brand success?

Amit Bakshi: Nothing, which I could have figured out actually.

Moderator: Thank you. We have the next question from the line of Duby Rex from Ithought Financial. Please go ahead.

Duby Rex: Sir, on a steady state, what would be the expected tax rate going forward, the tax bucket you will be having?

Sachin Shah: Yes, the expected tax rate is around the same, 8.5%, 9%, should be the same.

Amit Bakshi: For this year, yes.

Moderator: Thank you. We have our next question from the line of Mr. Prakash Agarwal from Axis Capital.

Prakash Agarwal: Yes. I had one more, sir. Just if you split the 2,000 MRs, in the past, you have given the split, which is how much is above 4.5 lakh productivity versus the Strides, which came later and had a lower productivity. What is the split today?

Amit Bakshi: Okay. Let me just try and give you an approximate number. Almost 700 people would be below 4, and rest will be above 4. And if you include the subsidiary, this will go to 800 actually.

Prakash Agarwal: On a net basis also, what would...

Amit Bakshi: 700 to 800 should be the number.

Prakash Agarwal: And this 800 would be primarily Strides and the subsidiaries and some of the tailwinds.

Amit Bakshi: Yes. So, out of the 700, 250 would be the neuro team, which is kind of coming up. Another 200 would be in the gynecology business, which now you see gynecology business, from the market data it is growing at around 20%-25%. And some other people placed in different divisions. But largely these are 3 businesses where we will have the major chunk and, of course, in the Kinedex. So, these are the 3 major chunks and then some here and there.

Moderator: Thank you sir. We have the next question from the line of Ashish Thapkar from Motilal Oswal Financial Services. Please go ahead.

Ashish Thapkar: Sir, any update on our tie-up with Medtronic?

Amit Bakshi: So, Medtronic, we got a product called Guardian. Right now, that product is being used as a service product. And how do we commercialize this, we are still not figured out. So, I don't think any commercialization would happen in this financial year. It will remain more of a service product. You know we have a very large patient engagement group, and that's where we are using it.

Ashish Thapkar: Okay. So, currently, you are offering it to the doctors.

Amit Bakshi: Yes, we are offering it to the patient directly through doctors.

Ashish Thapkar: Okay. Fair enough. And last question on any update on the IVF segment because we were looking for something...

Amit Bakshi: So, IVF segment started working. We have deployed around 50 people in the IVF segment. They have started touching 1 crore on a run rate basis. Every year Ashish, there will be couple of businesses which will be hypergrowth business, so IVF this year will be a hypergrowth business.

Ashish Thapkar: Okay. You said 1 crore per month run rate?

Amit Bakshi: Yes, a month.

Moderator: Thank you sir. We have next question from the line of Kunal Mehta from Vallum Capital. Please go ahead.

Kunal Mehta: I'm Kunal. Sir, I just wanted to understand, I do appreciate the hiccups which we have been facing because of a slowdown in the chronic market. So, just 2 questions from my side. So, firstly, can you just attribute the reasons why, I do understand the economy as a whole is slowing down. But can you just attribute the reasons for slowdown in a lot of these extremely chronic brands, which have given fairly robust growth for many years in the past? And secondly, from a long-term perspective, from a 3-year perspective, can you just give us a road map of how you wish to, I would say, steer your organization in terms of both the growth in the existing brands and introduction of new brands and plus entering in new therapy areas for the next 3 years?

Amit Bakshi: Yes. So, chronic has actually not slowed down significantly. Nothing really for us to worry. It is the acute, which had seen a sudden slowdown during the last year, and that is what has pull down the industry's overall growth. So, right now, I don't have an answer. I haven't even discovered whether the chronic has really slowed down significantly for anybody to look out for the reasons. I think these are more transient stuff, 100, 200 basis points here and there is more transient, and that I think would settle down. And I feel that the movement would have been much more in the inventory side than actually on the organic side.

Kunal Mehta: Sure. And to the second question?

Amit Bakshi: Yes. From a prospective point of view, prospect?

Kunal Mehta: Yes. So, I just want to understand that so now we are reaching a stage whereby in terms of the key therapeutic areas, key brands we have, we are #3, 4, 5 in all of those brands. And I do appreciate the fact that going from #3 to #2 would be a lot more tougher process than going from #5 to #3. So, I just want to understand in terms of the new brand introductions, new therapeutic areas, which we plan to enter, what is the strategy there from a longer-term perspective, for the next 3 years?

Amit Bakshi: Okay. So, a small improvisation here. The rank, which we have shown you is from the prescription chart side. From the sales side, the ranks are not as inspiring as we would like. So, we are, more or less our brands are between 1 to 7, 1 to 8 that is where most of the brands would sit. So, all these brands and the market themselves have still a long way to go. And these are not the markets which would shy away from growth, so the opportunity there is large. And overall, diabetes and hypertension, which is now 25%, 26% of our business, there, our market share is one is 5.5%, 6% and the other is 4%. So, for us, headroom is not a problem.

Moderator: As there are no further questions, I now hand the conference over to the management for closing comments. Sir, over to you.

Amit Bakshi: Yes. Thanks for taking your time, and this is what we have to say to you next time. Thank you, Prakash. Thank you for hosting the conference.

Prakash Agarwal: Thank you very much, sir. Ladies and gentlemen, on behalf of Axis Capital Limited, that concludes this conference call. Thank you for joining with us. You may now disconnect your lines.