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LAURUS Labs
Knowledge . Innovation . Excellence

January 30, 2024

To	To
The Corporate Relations Department BSE Limited Phiroz Jeejeebhoy Towers, 25th Floor, Dalal Street Mumbai – 400001 **Code: 540222**	The Listing Department National Stock Exchange of India Limited Exchange Plaza, Bandra Kurla Complex, Bandra (East) Mumbai – 400 051 **Code: LAURUSLABS**

Dear Sirs,

Sub: Transcript of the Q3 FY24 Results conference call hosted on January 24, 2024

Pursuant to Regulation 30 & 46 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015 and with reference to our Results conference call intimation dated January 17, 2024, please be informed that the Results conference call for Q3 FY24 was hosted on January 24, 2024 and the Transcript of the conference call is **enclosed** for information and record.

Thanking you,

Yours sincerely,
For Laurus Labs Limited

VENKATESWAR REDDY GOGIREDDY
Digitally signed by VENKATESWAR REDDY GOGIREDDY
Date: 2024.01.30 18:22:28 +05'30'

G. Venkateswar Reddy
Company Secretary &
Compliance Officer

Encl: As above

“Laurus Labs Limited

Q3 FY ‘24 Earnings Conference Call”

January 24, 2024

MANAGEMENT: **DR. SATYANARAYANA CHAVA – FOUNDER AND CHIEF EXECUTIVE OFFICER – LAURUS LABS**
MR. V. V. RAVI KUMAR – EXECUTIVE DIRECTOR AND CHIEF FINANCIAL OFFICER – LAURUS LABS
MR. VIVEK KUMAR –INVESTOR RELATIONS – LAURUS LABS

MODERATOR: **MR. MONISH SHAH – ANTIQUE STOCK BROKING**

Moderator: Ladies and gentlemen, good day, and welcome to Laurus Lab Limited Q3 FY '24 Earnings Conference Call hosted by Antique Stock Broking. 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 star then zero on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Monish Shah from Antique Stock Broking. Thank you, and over to you, sir.

Monish Shah: Thank you, Yusuf. Good evening, everyone, and welcome to Laurus Labs 3Q and 9 Months FY '24 Results Conference Call. On behalf of Antique Stockbroking, I thank the management for giving us the opportunity to host this call. Today, we have with us Dr. Satyanarayana Chava, Founder and CEO; Mr. V.V. Ravi Kumar, Executive Director and CFO; and Vivek from the IR team.

I will hand the call over to Dr. Satya for his opening remarks. Thank you, and over to you, sir.

Satyanarayana Chava: Thank you for joining us for our Quarter 3 and 9 months FY '24 results conference call. We are pleased to have this opportunity to update you on our progress and answer your questions.

We continue to make good progress in advancing our strategic priorities with focus on long-term success. We are progressing on building promising pipeline, augmented by our widening technology platform offerings and leveraging our commercial excellence. Our enabling capability is gaining lot of customer confidence, and this is quite well complemented by our continued growth investment which is expected to accelerate future business potential driven by several volume and value late-stage projects with key CDMO partners.

We also remain quite excited on transformative cell and gene therapy space that were added through strategic business development, such as India's first indigenously developed cell therapy product, NexCAR19, which was approved in December 2023 and is moving rapidly with commercial collaboration to enhance access, which will benefit cancer patients in India.

In addition, the Phase II interim results of NexCAR19 were presented during November '23 ASH conference, which was well appreciated. Secondly, our collaboration on gene therapy is progressing well and started GLP lab construction for the manufacture of viral vectors and cGMP gene therapy products. We expect to operate Phase 1 of this facility at IIT Kanpur campus from June 2024.

Moving on to our financial results. While our quarter 3 headline results were subdued, the underlying financial strength of our business have remained quite strong, which was reflected in our resilient gross margins of over 52% for several quarters. EBITDA margin were negatively impacted due to higher upfront expenses on growth projects and new initiatives to access

innovative technologies. It is important to keep in mind as well as our year-on-year growth was impacted due to a particularly strong quarter we had in 2023, which included large PO delivery in the CDMO space.

Our revenues for the quarter increased by 6% ex-large CDMO PO, but overall declined by 23% to INR1,195 crores. And our EBITDA came at INR183 crores with a margin of 15.3%. The positive momentum in FDF and Onco APIs as well as Bio division was more than offset by softer sales in CDMO and our APIs.

This volatility was more driven by timing of several customer contracts. Having said that, the overall volume tr end across our business have remained upbeat. Our cost improvement programs are also progressing quite well. We anticipate that a slower Q3 performance should rebound resulting from both healthy order book and strong commercial execution from Q4 FY '24 onwards.

Overall, our confidence in the business remains high, and we are moving ahead with a clear focus on technology breadth, coupled with scale differentiation to address commercial needs of our customers and create a value for our stakeholders over long term.

To begin, I would like to share key updates on our Formulation business. Our formulation division reported overall revenues of INR367 crores for the quarter 3, increasing by 47% over last year. On a sequential basis, revenues improved by 11%. Moreover, if you look at our 9 months, the revenues increased by 32%. This is primarily driven by consistent recovery in the ARV business, along with growth in developed market sales.

Coming to our LMIC business, overall market volumes have largely remained stable, partly supported from stable prices. We remain on course to fully stabilize our ARV franchise business through FY '24 and beyond. We are actively pursuing optimization programs to counter any pricing impact in the future. Supplies to recent NACO tender has started that will ensure our volume continuity.

Coming to the developed market, demand for our broader portfolio have remained healthy. In US, we continue to get good market share on the products that we are selling and also with very good increase in volumes. We have additional products under launch preparation for Q4, which will support asset utilization of our expanded greenfield capacity.

During 9 months, we filed 2 ANDAs. Cumulatively, we have a total 39 ANDAs filed to date. Of this, we have a total 16 final approvals and 14 tentative approvals so far. In Canada, we have 21 filings, 14 product approvals, of which we have launched 9 products, and we intend to launch 2 more products in the current quarter.

For EU markets, we have 18 filings with 14 product approvals with 6 commercial launches. We have continued to strengthen our existing CMO relationships and discussing additional opportunity with new customers. Accordingly, we anticipate further volume increases in the coming quarters.

Our FDF division has a total commission capacity of 10 billion units right now, and we anticipate that some of the brownfield capacities that we have added in the last year should start to get optimally utilized from the next quarter onwards. This is primarily driven by sales in partner portfolio, full scale benefit of our new launches scheduled in Q4 and certain key product approvals besides stabilizing ARV volumes.

On R&D front, overall R&D spending to sales for the 9 months FY '24 was at 4.8%. Higher R&D spend in this quarter is in line to enhance our pipeline, which also includes our spend toward additional initiatives in gene therapy assets. We continue to make good progress and invest in portfolio with product-specific approach based on complexity and scale. We have a total of 61 products in the R&D pipeline, either under review or under development.

I'd like to share the status of our filings as of now. We have filed so far 13 ANDAs in US, 18 dossiers in Europe, 21 in Canada, 9 with WHO, 8 dossiers in South Africa and 1 in Australia, while 20 dossiers were filed in India. And 23 products were filed in various Rest of the World markets. Of the 13 ANDAs filed in US, we have 16 Para IV filings, including 11 fast-to-file opportunities. Overall, R&D to sales for the full year is expected to be around 4.5%.

In the generic API space, the revenue from generic API during the Q3 declined by 9% year-on-year to INR574 crores. For the 9 months, overall revenue was down by 5% only. ARV APIs retained its volume-led steady momentum and reported revenues of INR347 crores, a decline of 8% year-on-year and quarter-on-quarter. The current order book for these APIs looks encouraging. We continue to maintain a leading market share in the first-line HIV treatment.

Onco API business for the quarter delivered a strong revenue increase of 18% year-on-year to INR87 crores. When compared to 9 months, the revenue increased by 38%. We remain upbeat on this portfolio, which was supported by positive market dynamics. Accordingly, new capacity addition work is also under progress. More importantly Laurus Labs have one of the largest high-potent API capacity in the country. Our aim is to strengthen global leadership in some of the existing products by focusing on high-potent molecules.

In the other API segment, which includes cardiovascular, diabetes and asthma, these API sales largely remain muted and reported sales of INR140 crores, a decline of 23% year-on-year, whereas it was very flat quarter-on-quarter. The moderation was mainly due to transitionary shipment impact and subdued pricing. We anticipate a better Q4 following the scheduled delivery of some of our CMO contracts.

We are confident that the underlying demand for our products in the CMO space, which have remained very strong and order book continue to look healthy. During the 9 months period, we filed 4 DMFs, 3 in non-ARV category that shows the diversification efforts of the company moving away from filing more DMFs in non-ARV space. As of today, the company has filed 83 DMFs.

Coming to the Synthesis business. During the Q3, the company's CDMO business recorded revenues of INR212 crores. Baseline business is tracking healthy and project pipeline continue

to scale up well with our existing and new customers. On 9 months basis, ex-large CDMO PO, the division recorded a 30% growth.

We are seeing good RFPs flow from several big pharma and leading biotechs, and our advanced and integrated scientific platform is helping us in working towards addressing commercial needs of our customers, which is expected to accelerate CDMO growth potential in the coming years. We are working on over 60 active projects with ongoing commercial supplies for about 10 products, including APIs as well as advanced intermediates.

Key CDMO capex projects across R&D and commercial manufacturing facility are on track. Our Crop Sciences chemical unit is under construction. And the Animal Health unit has started commercial validation supplies and scaling up well. As we mentioned, the Animal Health capacities are almost fully contracted to one big pharma partner.

The new animal site will have the capabilities to handle steroids, hormones, high-potent molecules apart from other large volume products. Our dedicated R&D center likely to get commissioned by end of this financial year, which will support our new business opportunities. Our focus remains to build diversified CDMO engine besides riding on the momentum in our NCE clinical projects.

Our Bio division witnessed a continued strong momentum with INR42 crores sales in Q3 and INR131 crores sales in the 9 months of FY '24, reporting a significant growth. The strong growth was led by diversifying application of our CDMO services across expanding customer base. We have continued to grow our enzyme engineering and production capabilities into small molecule clinical as well as commercial API projects, which will augment our pipeline in the green chemistry for sustainable journey.

Downstream processing at R2 is now operational, increasing capacity by about 20%, and this unit will achieve its peak revenues during FY '25. We broke the ground for greenfield R3 facility after receiving environment clearance. The construction is likely to begin this quarter with a target to install up to 2 million liters fermentation capacity in a phased manner.

We see overall demand for products delivered from fermentation to remain upbeat, and the new large-scale capacity expansion should further transform Laurus capabilities into API offerings and CDMO activity.

Let me share brief on our quality and ESG side as well. While we execute on our R&D-led commercial strategy and planned growth investments, we remain equally committed to advance our quality systems and ESG agenda. We signed GHG commitment with SBTi during the quarter, and there are several ESG projects under implementation, including carbon neutral sourcing of power for few of our manufacturing units.

Further, during 9 months FY '24, a total of 97 quality audits were performed, including several customer audits. To date, since inception, we have successfully passed 96 regulatory audits,

including 45 audits from major global regulatory agencies like USFDA, WHO, PMDA, TGA, EMA and MHRA.

With that, I would like to hand it over to Ravi to share financial highlights.

V. V. Ravi Kumar: Thank you, Dr. Satya. A warm welcome to quarter 3 and 9 months of FY '24 conference call. Excluding large CDMO PO, the underlying business delivered 11% growth in the 9 months' time. Total income from operations, INR3,601 crores in 9 months as against INR4,660 crores, with a declining of 23%. During the quarter, we reported INR1,195 crores sales against INR1,545 crores with a 23% decline. But barring large CDMO PO, we have registered a growth of 6%. The underlying demand across our growth portfolio has largely remained healthy. Gross margin for quarter 3 have improved at 54.3%. This is in line with our guidance on the improvement in various areas, especially in the ARVs. However, EBITDA for the quarter was lower to INR183 crores with 15.3% EBITDA margins.

Our EBITDA for 9 months was at INR539 crores, with a margin of 15%. The impact is primarily due to operational deleverage, lower CDMO business. And these are the two reasons. Our diluted EPS of INR0.4. And for 9 months, it is INR1.60. Our ROCE and return on net worth was lower due to the lower profitability and higher investments.

On the capex front, we have invested INR191 crores during the quarter. And for the 9 months, it is INR576 crores. As you are aware that FY '24, the majority of the capex is for the Synthesis and Bio divisions. Most of the expansion projects are on track to support our future growth. You may refer for further details in IR presentation.

And with this, I would request the moderator to open the lines for the Q&A. Thank you.

Moderator: Thank you. We will now begin the question-and-answer session. First question is from the line of Sajal Kapoor an investor.

Sajal Kapoor: So firstly, Laurus operates in highly regulated markets, including the U.S. and Japan. They have multiple lines of business in Bio CDMO, NCE CDMO, generic APIs and generic formulations. We have a diverse development and manufacturing footprint across several units and locations, and we are growing. So in future, we will be a much bigger organization. With all that context, my question is, how do you verify that good culture is uniform.

And that there is no cross contamination between compliance plus mindset and the practice of cutting corners and not maintaining the high standards of compliance that regulators and stakeholders expect from Laurus. That's my first question, and I've got another one.

Satyanarayana Chava: Interesting question. Our philosophy always remain operate all units to one standard, quality standard. When we go through audits, either customer or regulatory audits, any comments which will improve our quality systems are implemented across the units, even one unit comments from the audits, we don't implement for that unit only. We take those improvements across all of our units. That's the corporate culture, and we don't want to deviate from that. So going back

to your question, the quality culture will remain similar across all units. There are no cost-cutting or corners taken unit-wise.

Sajal Kapoor: That's helpful and reassuring, Dr. Satya. And my second question is, one of our Indian competitors which is a pure-play CDMO has close to 100 projects with 400 scientists. So 4 scientists per project is the average. We have 60 projects and 750 scientists excluding generic formulations and generic API scientific talent that we have.

So I'm adjusting the number that we have published, which is 1,088, and I'm reducing that to a number closer to 750, spread across 60 projects. Now this is way above the industry average of 4 to 5 scientists per project. So 60 projects should require anywhere between 200 to 400 scientists as a rough estimate, depending upon where that project is in the life cycle. Early-stage projects will require more scientists, Phase III projects will require less scientists and so on.

So how come our scientific talent pool purely on the CDMO side is double that of the industry average? That is the question I'm trying to get your view on because clearly, scientific talent is a fixed cost for us. And part of the operational deleverage that we are seeing in the operating margins is because of this high fixed cost that is not translating into revenues and scientific talent is definitely 1 element in that fixed cost. So why are we having such a high ratio of only 60 projects with 750 scientists?

Satyanarayana Chava: Thanks for asking this question. It all depends on the stage and complexity of the projects being handled. If it is RSM, which may involve 1 or 2 steps. If it is intermediate, maybe 6, 7 steps, if it is API, it could involve additional steps. I'll give you an example. We executed on project last quarter, including backward integration, we did 15 chemical steps. So you can't compare projects and number across the 60 projects.

We also hope to work on some projects which are even more complex than what we handled so far, 30, 40 chemical steps for each project. Then the demand for the scientific talent, I would say depending on number of steps, your initial comment of 4 scientists. It may be valid for 1 step. If we are handling 30, 40 steps, you may need 100 people for project also, depending on the complexity.

So the advantage what the company is having is the ability to handle complex projects at scale. Maybe we are in a sweet spot to attract such kind of projects, high volume, high complex, large synthetic schemes. That is taking away a lot of our scientific talent. One good thing is there are not many companies who can offer such complex chemistry and scale. That is the reason we have some interesting projects coming to scale up. I hope I answered your question.

Sajal Kapoor: Definitely, Dr. Satya. Thank you so much. I've got more questions. I will rejoin the queue.

Moderator: Next question is from the line of Jeevan Vijay from Sahasrar Capital.

Jeevan Vijay: So just wanted to understand, so I would request you to actually give us some sense on how we are going to move in next quarter and next year? So since start of the year, we are saying this is

a consolidating year for us. And we are seeing that in terms of technology, in terms of projects, everything we are basically moving toward diversifying from ARV based and we are doing it pretty successfully. I just want to understand in terms of numbers.

So qualitatively, I understand we are on right track. But quantitatively, just want to understand where are we? So -- because last 3 quarters, I think, honestly, it's below our expectations. So in terms of numbers, in term of quantitative give us some sense, where do we stand? And how do you see FY '24 year closing and the next year?

Satyanarayana Chava: We believe we are putting the bad quarters behind. And we hope Q4 onwards, we definitely see improvements. That confidence is coming because of the order book and the deliveries what we are going and planning to do in Q3. That's the confidence what we have.

Jeevan Vijay: Any quantitative numbers -- I just request you to -- if you can just share some numbers because we are already close to FY '24 and we are 1 month already into Q4. And we'll be closing the year after 2 months. So last year, it was like we will be somewhere closer to what we did in FY '23. And now we are almost 23% lower than there. So is it like we are going to close actually minus 10%, minus 15%, where do you see this year getting closed

Satyanarayana Chava: I will give it to Ravi to give some light on this?

V. V. Ravi Kumar: I think we can't give any quantity guidance. We never gave except once. But if you look at it in our investor presentation, we have given a slide where we said that based on the capex investment, what could be the asset turn we can do it, what we have done in the peak. So we are in a growth phase. We also indicated in the last 2-3 quarters back that 3 year or back, actually, we have seen the same situation. We are hoping that history should repeat, and there is a progress but we can't give any quantitative guidance

Jeevan Vijay: I also have similar view, Ravi, that history will repeat, the FY '20, FY '21 numbers should start again coming in FY '25, '26. So just wanted to check what is happening as after Q1 everyone and I also thought that the bad is behind, and now we should move ahead. But Q2 was, again, the number didn't come and now Q3 again, the number didn't come. So I'm just trying to understand, are we closer now to the end of the tunnel

V. V. Ravi Kumar: That's what Dr. Satya indicated. And if you look at our last quarter call, we have guided that second half will be better than the first half. We still commit to that. We have not indicated quarter 3 will be better than quarter 2, but second half will be definitely better than the first half. That's what we indicated in the last call, and we are still committing to that.

Jeevan Vijay: Okay. Perfect. Around the BIO side, we say that we have started the work on the new facility, the 2 million-liter facility and we see that Phase 1 should start in June '26, which is almost 30 months from now. So why there is so much of time? Is it like once we start the Phase I the next phases will come quickly after that?

Satyanarayana Chava: As I mentioned, the 2 million liters fermentation capacity will be added in a phased manner. The first phase, we are expecting to add 700,000 to 800,000 liters fermentation capacity and which will come up in qualified trials done in '24 months. That's the estimation of what we have right now. It's not a brownfield, it is a greenfield expansion, yes.

Jeevan Vijay: Okay. Okay. And then the next expansion, the next phase will come pretty fast.

Satyanarayana Chava: 12 months. We expect it will be 12 months, yes.

Jeevan Vijay: Okay. And the third question, the last question, we have commercialized the ImmunoACT, the CAR-T cell therapy in India. So any sense on how is the response or what is our strategy to reach to the patients in India? How do you basically plan to reach to the masses of India.

Satyanarayana Chava: So last month, they started enrolling patients. And we're happy to share. Hopefully, they will turn from red to green in this quarter.

Moderator: Next question is from the line of Harith Ahamed from Avendus Spark.

Harith Ahamed: So Ravi sir, when I look at the operating cash flows that you have shared in your presentation, I see that for 9 months FY '24 is around INR370 crores, which is less than what you have shared in the last quarter. So we are seeing a negative OCF in 3Q? How would you explain this?

V. V. Ravi Kumar: Harith, your voice is not very clear. Are you using hands-free?

Harith Ahamed: No. Yes. Is it better now? Can I try again?

V. V. Ravi Kumar: Yes, it's better.

Harith Ahamed: Yes. So for the operating cash flows that you've disclosed for 9 months FY '24, it's less than what you had disclosed in 1H. So it appears that there is a negative operating cash flow in the third quarter. So I'm just trying to understand what exactly has happened. So the INR370 crores number that you shared in the 3Q presentation for 6 months, it was INR475 crores.

Harith Ahamed: So 9 months OCF is less than 6 months OCF. That's my question.

V. V. Ravi Kumar: It cannot be probably we will discuss offline on this, yes.

Harith Ahamed: Yes. And the last couple of years, we had a capex of around INR900 crores and as compared with where we are looking at a similar level for FY '24 as well. So from FY '25 there will be a moderation from this INR900 crores numbers that we've seen in the last few years?

V. V. Ravi Kumar: Right now, the capex for the FY '25, the ongoing projects of Animal Health, may be one block from Animal Health and Agri unit also will be there and then Bio. These 3 are the ongoing projects, apart from that, the LSPL R&D. These 4 are the ongoing projects. We are not taking up any new projects as of now. So probably on the specific number, what we are planning for

FY '25, we will come back in the April conference call. But we are also thinking like if possible, actually, we want to downsize without cutting the future

Harith Ahamed: Okay. And then you mentioned that we have operationalized LSPL 2 during the quarter. So I'm just wondering if there is a contribution from the Animal Health contract in the CDMO revenues for the quarter?

V. V. Ravi Kumar: Very small and meager. They are very meager in the quarter 3. And maybe quarter 4 onwards, it will slowly pick up. But as we envisaged it before, it has got 1, 2 quarters delay, yes.

Harith Ahamed: Okay. And sir, just to rephrase my previous question on the operating cash flow. When I look at net debt number currently, based on your disclosure of around 3x EBITDA, it's around -- it's working out to around INR2,500 crores. The same number at the end of September quarter was around INR2,000 crores. So there's a INR500 crores increase in net debt, that cash flow deficit is what I am trying to understand.

I will connect with you offline on this. So the question from my side is on the R&D center, CDMO R&D center, which you've guided for commissioning in June this year. So how should we think about revenues from the center? Is this R&D center for our captive R&D work? Or Should we look at this as R&D center commissioning will lead to revenue generation from this center? So just trying to understand the nature of work that we are planning at the center.

Satyanarayana Chava: R&D center will augment our capacity to offer more clinical early stage projects. We don't anticipate significant revenue coming out of that R&D center.

Moderator: Next question is from the line of Rohit Jain from Tara Capital Partners. Please proceed.

Rohit Jain: One question from my side. Can you help us understand what is the target margin, let's say, levels for FY '25, the EBITDA margin levels?

Satyanarayana Chava: As the volume of sales picks up, we do anticipate significant improvement from the EBITDA margins from current little over 15% to definitely behind 20%. We can't give you a number, but it will improve significantly, yes.

Rohit Jain: Just one -- I think one of the earlier callers has also mentioned this. Over the last 3 quarters, what we have seen on the call, which is just qualitative comments that it will get better without any tangible numbers. So for us, to be honest, it's a very difficult situation because, let's say, if you have 15% going to 18%, that can also be classified a significant improvement, 20% can also be significant, 22% can also be significant. So how should we think about the actual numbers because a lot of improvement is obviously already baked in?

Satyanarayana Chava: I think, see, one confidence what we wanted to give the investors is, one is quality of business. Second is quantum of the business. As we mentioned in this call, the quality of business is very good. We are doing gross margin well above 52% even in the current quarter Q3 FY '24, we did over 54%. And we expect that will continue.

As we increase our sales in CDMO space, which we expect next year will increase. The ability to remain at that level for gross margins is very high. And what we are saying as the order book increases and the revenue goes up, and most of the gross margin will flow into EBITDA, not all of that, most of the gross margin.

So that is the reason we expect significant improvement. And it's not that we have done that performance earlier. Which we had. Without segment contribution from CDMO, we were at close to 30% of EBITDA. And we came down, but we never went down at a gross margin level. So that's the confidence the management has. And I'm sure we will regain your confidence for sure in as shortest possible time as we can, yes.

Rohit Jain: And just one last question on margin again. Your slide said that your asset turn is right now 0.9 and the average is 1.1. So assuming we reach 1.1 next year, let's say, 20% increase from the current level. And if we assume gross margin at 50% and we assume that the entire incremental sales flows to EBITDA then we get to a margin of 20% from the current 15%. Would that be the right way of looking at it, that is pretty much the ceiling as far as our utilization remains at 1.1?

Satyanarayana Chava: I'm not going to give arithmetic of that statement, but we are on the right direction, you and we, both of us, yes.

Rohit Jain: Okay. Fair enough. And can you help us understand, you mentioned that Animal Health has been delayed by a couple of quarters. So is this just a time delay or the initial amount that we thought we will get from this, has there been some tampering in that also?

Satyanarayana Chava: No, no. So we have a long-term contract in place. The delay was due to 2 reasons. One was there was delay in qualifying the facility. There was some delay in validations because of the strong chemical synthesis needs of that. And as I mentioned in my opening remarks, whatever capacity we have created in that unit is already contracted to 1 big pharma. And we don't have any reservations that the quantum of the business will go down than what we anticipated.

Like the CDMO revenue coming from our Unit 5 steroids and hormones went into a pretty stable mode. We expect Animal Health revenues will also go into a stable mode in the next 3 years. So we will have a very detailed plan in place, how many products are going to validation, how many products are going to filing, how many products are going to be commercialized. This is a well-structured program, and we don't see any challenges out of that.

Rohit Jain: Okay. And I think you mentioned to the other participant that you will clarify the cash flow and the debt, even we can't understand whether this quarter had a negative operating cash flow because that is what the slide deck suggests. So in case there is any clarification, it would be really helpful if you can file it with BSE so that the wider group can understand what happened with the cash flow in this quarter. That would be one suggestion.

Satyanarayana Chava: We'll submit revised statement, if there are any changes, yes.

V. V. Ravi Kumar: As far as the debt is concerned, as answered to the previous question, it is indicated around that level.

Rohit Jain: I'm talking about cash flow. So in case there is any change in numbers there. That is what I was mentioning.

Satyanarayana Chava: Thanks for raising that question. If there are any changes, we'll resubmit to the stock exchanges.

Moderator: Next question is from the line of Foram Parekh from Sharekhan.

Foram Parekh: Thank you for the opportunity. I only have one question. So in the last concall, the management has alluded that H2 would be better than H1. And 9 months down the line, our EBITDA margin is just 15-odd percent. And now in the commentary also, the management did mention that H2 will be significantly better than H1, despite 3 quarters being passed. So are we confident that we will close FY '24 at 20% EBITDA margin as guided in the previous quarter con call?

Satyanarayana Chava: Our CFO mentioned, we are committed to our statement made in the last con call that H2 will be better than H1, and we are very confident that we will deliver better H2 than H1 even now.

Foram Parekh: Okay. So then we see that in the larger pie of [inaudible 0:43:43] segment and commodity prices are softening and also CDMO, which is just 25% of the total sales. So if there's a pickup in CDMO sales too, so you'll be still saying that when the larger pie is not growing, we can still increase our EBITDA margin?

Satyanarayana Chava: You are right, we'll definitely increase our EBITDA margins. See, currently, all our costs are absorbed and any improvement in sales the gross margins, most of that will flow into EBITDA. So we're very confident the EBITDA percentage will also move upwards in Q4.

Foram Parekh: Okay. So while gross margin remains the same and EBITDA is expected to increase, so where are we seeing the cut. Are we expecting R&D sales to come down or employee costs to come down? If you can just specifically highlight which cost is expected to come down?

Satyanarayana Chava: Costs are not going to come down. Only sales is going up.

Moderator: Next question is from the line of Harshal Patil from Mirae Asset Capital Markets. Please go ahead.

Harshal Patil: Thank you sir for the opportunity to ask the question. Most of my questions are answered. Just need 2 clarifications from you. One is for the other APIs where we've clearly mentioned of shipments getting impacted or delayed. So is it that, sir, we will see the shipments coming back in Q4?

Satyanarayana Chava: Actually, see, it's not shipment delays. So that is a scheduled delivery. Our partner asked us to deliver in Q4 than in Q3, yes.

Harshal Patil: So it will be there in Q4. And sir, if you could just also mentioned like, you also said that there's some impact of pricing. So any flavor of what can be the impact in terms of maybe percentage or something for the pricing thing?

Satyanarayana Chava: Actually, the pricing impact was offset by increased volumes in some of the products. So that's the one reason where our gross margins also went up. If you look at it from quarter-to-quarter, we have improved our gross margin of 180 basis points, yes.

Harshal Patil: Okay. Got that. And sir, just one more thing on the Animal Health project, where we are envisaging some delay of 1 to 2 quarters, I'm sure that would definitely be starting. But sir, any flavor on the potential size of revenues that can be expected from the Animal Health, I guess it will be mostly in FY '25 now.

Satyanarayana Chava: The peak revenues for that unit will be in FY '26, not in FY '25 also. So we have to validate 20 APIs from the site. But currently, third product validation is going on right now. You can imagine 17 more products to go validation. And we have to do at least 1 product per quarter or more than 1 product per quarter to complete our validation. We scheduled to complete our validation by 2026 April. That's the current schedule.

Harshal Patil: Okay. So post that only, we would see some material revenue coming in from the Animal Health.

Satyanarayana Chava: The earlier products, which are validated, will be filed and we expect 12 months' time required to get approvals from the agencies. So we expect commercial sales will come from first product, 2 products are already done. I think we have orders for 1 product for next year. Second product orders will come end of FY '25. So it is a very well-defined program we have in place.

Harshal Patil: Okay. And the potential definitely would be a sizable one?

Satyanarayana Chava: It will be very good, yes.

Moderator: Next question is from the line of Tushar Bohra from Emkay Ventures. Please go ahead.

Tushar Bohra: Thanks for the opportunity. Sir, first, just to quickly check what is the expected gross block going to be end of this year as per the guided capex line, ballpark number?

Satyanarayana Chava: I'll ask Ravi to take this question.

V. V. Ravi Kumar: Around INR6,000 crores, Tushar.

Tushar Bohra: And next year, we are doing another, sir, INR1,000 crores capex. I don't know the exact ballpark, what is your guidance for next year?

V. V. Ravi Kumar: Nothing at this juncture, but probably, we have a visibility of adding at least INR500-600 crores-. We will get back on the exact number in the April quarter.

Tushar Bohra: So my question is just looking back, the first time we hit, Sales more than INR1,100 crores about INR1,140 crores was second quarter of FY '21, which was quite a few quarters back. I am just looking at the gross margin and the cost structure and the profit structure for the company at that point versus for the current quarter, which is INR1,195 crores or thereabout revenue. So the revenue profile is in the similar ballpark Q2 FY '21 versus Q3 FY '24. And on the cost side, below gross profit, I see a difference of INR300 crores on a quarterly basis.

And for the corresponding revenue, the costs are higher by INR300 crores, employee, other operating costs, depreciation and interest. So my assumption would be a large part of this would be for incremental initiatives, which are not yet yielding results because the revenue profile is very much similar. And now that the CDMO business has also seen an increase in revenues but some segments have degrowth elsewhere. But the overall revenue profile is similar.

So I'm assuming and that is where I would like a commentary from you that this INR300 crores difference in cost, a large part of this, can we attribute this to new initiatives where obviously, the depreciation and interest toward the capacity? That's first. Second, from INR2,700 crores or thereabouts gross block end of FY '21, which was good enough to support close to INR5,000 crores revenues that year.

We are now going to be at INR6,500 crores gross block by end of next year, INR6,000 crores by end of this year. So Ideally, if we assume that the asset utilization would be similar to earlier levels, we are talking potentially more than INR10,000 crores revenue being supported by the current gross block alone, and we're adding to it.

So just to get a sense, when do we start to see the revenue profile not exactly in the same ballpark, but the revenues have been stagnating for some time now. When do we start to see material traction on revenues, which obviously will then cover for your operating deleverage for the operating cost as well?

Satyanarayana Chava: I think, Tushar, very interesting thought provoking question you put. The revenue profile in Q3 FY '21 to Q3 FY '24 has changed significantly. From ARV-driven revenues to non-ARV driven revenues, that is one. And second, as we mentioned, gross block improved significantly. Our team size has also improved significantly.

Not just capex, in the last 3 years, we also invested non-capex close to INR450 crores, almost INR300 crores equity infusion done in Laurus Bio. And about INR100 crores, a little over INR100 crores was done in ImmunoACT. And the gene therapy assets were licensed from IIT Kanpur. So over INR450 crores, non-capex-related investments were also done.

That is another significant diversification by the company. And second, 2021, no new R&D center for Synthesis, no new unit for Animal Health, no new unit construction for Crop Science chemicals. So we have taken a lot of initiatives to diversify revenues from nongrowing therapies like HIV to potentially high-growth segments like CDMO, Animal Health, Crop Science with great opportunity, disruptive therapies like cell and gene therapy and also going into new age precision fermentation by investments in Bio.

So all these have added to our cost structure significantly, while we are not seeing the real benefit right now. But all these at some point of time, will start delivering the right results what we anticipated. If you look at Bio, which is older investment, when compared to other investments. When we invested the company was having INR50 crores revenue. Today, this year, I'm sure that will deliver INR50 crores EBITDA. So that is definitely giving benefit what we thought. ImmunoACT will also give benefit.

As I mentioned, hopefully, this quarter, they'll become green from red. That is very remarkable for a start-up. Whereas our Animal Health, we invested significant money. We had a full-fledged team on the ground, but we are only doing validation right now. So it will take another 12 months for that unit to turn green.

Crop Sciences will take 18 months to turn green. So all these are very conscious and judicious investment the company is doing to diversify and also bring sustainability to the organization.

Tushar Bohra: Sir, noted, and we appreciate the purpose of the management, which is not looking at a short-term view. But so the point to really understand is that the gross block investment has already been done, and it's a sizable investment. And we've done it over a 4-year period from FY '21-- at least 3-year period until end of this year.

Now -- so one question that we need to understand is that whether some of the revenue profile that has changed, does this point to a permanent loss of competitiveness or revenue opportunities from the existing business. So what happens to that gross block, which was part of the original INR2,700 crores whether that gross block can be or has been repurposed and is yet to deliver results because we don't have a breakdown of the gross block for each segment or at least not immediately in front of me to qualify that.

But if you're saying that some of these gross block change has gone toward a revenue replacement for the earlier ARV business. Then what has happened to the original gross block, the original capacity dedicated to ARV. Have they been repurposed in any way? Or how do we ensure that, that capacity can be repurposed if the ARV business is going to permanently be at a different scale than originally envisaged?

Second, if the new initiatives like you highlighted. Can we have some more milestones for the other segments? Like let's say, from here over the next 3 years, how do we look at Laurus Bio. What kind of numbers can we look at from Animal Health business? Some more clarity that allows us to say, if not segment-wise at an overall gross block level, this INR6,500 crores gross book that we're talking FY '25.

How do we look at this over the next 3 years? How should we look at the overall utilization? And how do we get a comfort that by the time we reach the utilization for this gross block, the management would have not already added another INR2,000 crores, INR3,000 crores gross block in anticipation of the business, which are thereafter. We don't want to be in a perennial investment situation where the investors don't see a profit outcome.

V. V. Ravi Kumar: I think, Tushar, your points are valid, good observation. So the overhead numbers and coming to the ARVs more or less in this last 3-year time, the more or less the ARV revenue is close to the number of what quarter to FY '21 you have talked about. But if you look at the price fall in the last 3 years on the ARV side and then the volume increase there in the ARV. For example, efavirenz is the 1 product of ARV, which was fallen, which was replaced with the dolutegravir, we have changed that.

But if you recollect and refer to Slide 8, what we have given here, how the capex is right now, the 0.9 is the asset turn and the peak is 1.4, but if you look at last 5-year average is 1.1. This is how the revenue can be scaled. It's only a matter of time. The kind of an investment, what we have made in the last 3 years or last 4 years when we added a INR3,000 crores capex. Some of it has not generated any revenue. So that has a potential to generate more revenue. If you look at on the positive side, once everything has been done, actually, we have a capacity to run, people to run. We are incurring the expenditure.

So probably the incremental revenue generate with a not significant upside on the expenditure side. That's how you have to look at. And, then coming to the numbers, what we are saying, we don't want to give any quantitative guidance, Tushar. And then I think once we start generating revenues, then everything will be fine.

Moderator: The next question is from the line of Nitin Agarwal from DAM Capital.

Nitin Agarwal: Sir, we've discussed a bit on the CDMO part during the call. But the other relevant component of the business, which is the Fixed Dosed Formulations business and the other API business segment, I mean, they've also had their share of challenges over the last 1 year, 1.5 years.

Now when you look forward or the next few quarters, I mean, the 2 things is what has really led to relatively modest growth in some of these segments. I think we've been reasonably positive on the contract manufacturing opportunities in both these businesses. And from here on, sir, how should we look at growth in these businesses?

Satyanarayana Chava: Nitin, you're breaking, but we got the essence of your question. Some segments did very well in the Q3 as well. The oncology did report significant growth. Other APIs did okay. The FDF we did well. FDF in developed market did very well. We hope oncology growth will continue to be there. That will also be reflected in our Q4 numbers you will see in April. Overall, the growth has to come from oncology, other APIs, generics CMO, CDMO and Bio. And as we mentioned, we expect the plateau for ARV APIs and formulation sale together. It will be vary INR50 crores-INR100 crores here and there, but it will stabilize around INR2,500 crores.

We don't expect that will go significantly up or significantly down. The growth is anticipated in other areas, and that is primarily, we believe, because of the projects we are working, customers who are talking to us on the volumes in various fields.

Nitin Agarwal: Sir, on the FDF last capacity expansion that you undertook, most of the capacity was utilized by the ARV supplies. Now since the ARV supply is not an incremental growth driver for the

business, and we've put up significant FDF capacity since then. How do you see the FDF capacity getting utilized? I mean, what will be the utilization drivers for the FDF capacity going forward? Because CDMO largely, I presume, is all API and specialty chemical driven.

Satyanarayana Chava: The capacity required for ARV formulations is very less. So less than 20% of our capacity, 2 billion. I wouldn't expect we'll use even 2 billion tablets. It is probably 1.5 billion tablets will be used for ARVs because these are a 3-drug combination. So increase or decrease in ARV capacity utilization formulations will not consume bigger capacity for our molecules. I hope Nitin, I answered your question.

Nitin Agarwal: What sort of therapies, what segment do you think, which geographies will use up the 8 billion other capacity, which is there outside of the ARVs? And how much utilization are we on that right now of the 8 billion?

Satyanarayana Chava: We're between 6 billion and 7 billion right now. And we expect to use maybe 1 more billion during this quarter because of the anticipated launches in U.S. and also increased demand coming from our CMO partner from Europe. So in next 6 months, we hope to utilize that capacity optimum. And at the time, I think once we reach that stage, where we will equip our remaining MB3. But right now, we definitely have some capacity to offer to our launches or to our CDMO partner.

Moderator: We will take our last question from the line of Shivam Agarwal from Mirae Asset Capital Markets. Please go ahead

Shivam Agarwal: So just one question for you, sir. On the CDMO side, so can we assume that the quarter 3 revenues for CDMO will be the base going forward? And even that on an ex-PO basis, we have grown at 30% on the 9-month period. So can this growth trajectory be sustained going forward?

Satyanarayana Chava: We have enough projects on hand to take our revenue beyond our peak last year. But we are not committing when we will cross that. But we can tell you we have enough projects to surpass that number. See, we have no control on the advancement of clinical programs, but we have enough projects in advanced stages. That is the reason despite of the current challenges, management is very upbeat and continue to invest in resources to take us to the next level in our CDMO plays.

Moderator: Thank you. Ladies and gentlemen, that was the last question for the day. I now hand the conference over to the management for the closing comments.

V. V. Ravi Kumar: The question asked by 2 people on the operating cash flow, the numbers are right. Numbers have been reflecting because of this change in working capital. So this, we thought we will clarify. We are clarifying in the call itself. Thank you.

Satyanarayana Chava: Thanks, everyone, for you insightful questions and also patience in waiting for our performance and which, as we mentioned, we hope to keep up to your confidence from Q4 onwards. Thanks for your time to join this call. Thank you.

Moderator: Thank you very much, sir. On behalf of Antique Stock Broking that concludes this conference. Thank you all for joining us, and you may now disconnect your lines.