"Hikal Limited
H1 FY2020 Earnings Conference Call"

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Moderator: Ladies and gentlemen, Good day and welcome to H1 FY2020 Earnings conference call of Hikal Limited. This conference call may contain forward-looking statements about the company, which are based on the beliefs, opinions, and expectations of the company as on the date of this call. These statements are not a guarantee of future performance and involve risks and uncertainties that are difficult to predict.

As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Sameer Hiremath - Joint Managing Director & CEO of Hikal Limited. Thank you and over to you, Sir!

Sameer Hiremath: Thank you. Good afternoon and very warm welcome to everyone present on our earnings call. I am Sameer Hiremath, Joint Managing Director & CEO and along with me I have Mr. Anish Swadi, President Business Development and Strategy and Mr. Kuldeep Jain, Finance Controller as well as Strategic Growth Advisors – our investor relations advisors. I am pleased to interact with all of you on our semi-annual earnings call for H1 FY2020. I hope you have received our investor press release and results by now. For all of those who have not, you can view these from the stock exchange and our website.

Revenue for H1 FY2020 was at Rs. 724 Crores and Profit Before Tax before exceptional items was up by 5% to Rs. 62 Crores. We had an exceptional item of approximately 15 Crores pertaining to payment of customs duty on past import of raw material at an export-oriented unit of the company. There were some unforeseen events in the last quarter as well. We will explain the same in detail in the call today.

The crop protection division performance was impacted by heavy flooding at our Mahad facility in the month of August, which led to temporary shutdown of manufacturing unit and lower production. At the Taloja facility, due to the order by the National Green Tribunal to curtail water supply by 50% to all industries in the MIDC area as well as de-stocking by innovator clients lead to postponement and reschedule of offtake volumes of some of our products.

We expect the de-stocking exercise at customers end to normalize by next quarter and volume offtakes to pick up from Q4 FY2020. With regards to flooding at the Mahad facility, the operations were temporary disrupted for a short period, but were resumed and production has normalized. The NGT order impact for the whole of MIDC industrial area at

Taloja wherein water supply to all manufacturing plant in the area was curtailed by 50%, the issue is being amicably resolved and water supply is in the process of being restored.

Based on the new products identified and growth opportunities, we are investing approximately Rs 150 Crores over the next 18 to 24 months to add manufacturing capacity for this division. Currently, on the contract manufacturing side, the project pipeline is looking good and healthy. On our own products, we have identified few niche molecules, which are used by multiple industries and are currently imported into India. These have global demand. We have developed in-house technology and have a fully backward integrated manufacturing process to eliminate our risk on Chinese imports for these products and we have already started supplying test quantities and validation quantities to potential customers. We expect to ramp up the manufacturing of this products in the next few quarters to a full production on stream by the next financial year.

For the pharmaceutical division, the performance of our pharmaceutical division was impacted due to lower volume-off take of a few products by our customers due to increased finished good inventory as well as lower production at our manufacturing site due to a planned annual shutdown taken at a multipurpose plant in Bangalore to increase manufacturing capacity.

The de-stocking exercise is expected to normalize in the next couple of quarters and the volume pickup will happen from end of the current financial year. The new capacity at Bangalore which will come on stream from this quarter onwards will help us to cater to higher demand for some of our products and will contribute towards growth for the next few years.

Currently, we are also working on adding capacity at our Panoli site. Total Capex for the pharmaceutical division would also be approximately Rs. 150 Crores which we are adding in the next 18 months. We are also adding capacities to our existing generic APIs as well as new products, which we will be introducing this year and the next year. The capacity addition would also be towards adding our finishing product facility at our Panoli site so that we can supply APIs from two facilities, Bangalore and Panoli, both of which have been recently recertified by the US FDA. On the contract manufacturing side, we are seeing a healthy pipeline of new projects. Based on our exemplary regulatory track record, we are confident of converting these opportunities into business. We are looking at two to three new products in contract manufacturing to be commercialized this year with intermediate and an advance intermediate and APIs.

The US FDA inspected our Bangalore and our Panoli facilities in August and September 2019. I am happy to inform you that the Panoli site received Zero 483s while the Bangalore site had only one minor 483 observation which has already been closed out. This is a strong testament to our continuous focus on regulatory compliance, quality and integrity of operations.

The gross debt on our balance sheet as of September 30, 2019 is Rs. 607 Crores and our net worth is Rs.779 Crores translating to a debt to equity of 0.8x. The working capital days as of September 30, 2019 is around 120 days, which is similar to March 31, 2019.

Recently ICRA has reaffirmed our credit rating for long-term facilities as ICRA A with stable outlook and short-term bank facility at ICRA A1. Considering the tough economic environment, the reaffirmation of credit rating reiterates our balance sheet strength.

Last year we embarked on a Capex of Rs. 300 Crores to be completed in 18 to 24 months. As of September 30, 2019, we have already invested approximately Rs. 100 Crores and the balance Rs. 200 Crores will be invested in the next 18 months. The Capex plan is equally split between both the division in pharmaceutical and crop protection with a majority of which being included in our Panoli site. This will be funded through debt and internal accruals in the ratio of 50:50. As part of the Capex plan, we will also be investing in some associated infrastructure and facilities like zero liquid discharge plant to ensure environmental compliance. The asset turnover on the total capex is expected to be about 1.5x and the full ramp up would happen within two years of commissioning.

Despite the challenging period, we had a strong net cash flow from operating activities of Rs. 136 Crores for this first half of the year compared to Rs. 86 Crores in the H1 FY2019. The net cash outflow for investing activities for H1 FY2020 has been Rs. 106 Crores, which largely reflect the money invested till September 30, 2019 in the current Capex plan. During the first six months of the year, we have repaid 28 Crores of debt and borrowed additional Rs. 40 Crores for the Capex, which is reflected in net cash flow for financing activities of Rs. 20 Crores for H1 FY2020 as compared to Rs. 22 Crores for H1 FY2019.

Based on the first half performance of this year, and visibility for the remaining part of the year, we expect to grow in single digit for the full year. However, based on our new investment and product launches, we expect to resume double digit growth from next financial year onwards with an improvement in margins.

With this we can now open the floor for questions. Thank you.

Moderator: Thank you very much. We will now begin the question and answer session. The first question is from the line of Niteen Dharmavat from Aurum Capital Services LLP. Please go ahead.

Niteen Dharmavat: Yes. Thank you for the opportunity. Great to know that we continue to do well with regulators and compliant with US FDA one more time. Regarding this NGT order and heavy flooding, so did we inform the exchanges in the same spirit of working with regulators when this has happened?

Anish Swadi: No, we did not inform the regulators in terms of the NGT hearing because it is something that has affected the entire industry. We did not have an idea how long this was going to last. We had approached…

Niteen Dharmavat: But the general practice is that whenever such material information is there, it has to be informed is it not?

Anish Swadi: That is the general principle, we did not have any idea on how long this would last and we did not know how much would be the impact and this was towards September, more in a month of September, so that is why we did not inform.

Niteen Dharmavat: That is okay, whenever it is, it has to be informed, let the decision be taken by the investors and if it is getting cleared, you could have filed another information with the exchanges.

Anish Swadi: Yes, but this is also in our case, a force majeure kind of situation which is not in our hands, so flooding is something that is not in our hand, so every time a flood happens or something extraneous happens that is not in our control, we cannot inform, because it is part of our business so we have to take it with the ups and downs so that is why we took a call not to inform the exchange and just to clarify this is not something that has only happen to us, but the entire industry.

Niteen Dharmavat: That is very strange actually. The second question is you mentioned about the single digit growth, so I wanted to understand what is the guidance for the year now, does it remain same for revenue and bottom line and if it remains same, what is the run rate required to achieve the number for the remaining second half? I am sure that it is going to be in the double digit rate for the remaining half of the year considering the first half is not so good and we are talking about the double digit will come from the next year onwards, so can you give some light on that.

Sameer Hiremath: I think the growth in the second half of the year will be better than the first half of the year and that is definitely going to be the case, so we expect single digit growth for the full year, so for the first half we have had flat growth of 1%, so for the second half of the year, the growth will be in the high single digit or low double digits.

Niteen Dharmavat: But that will not be leaving 7% or 8% growth as they talked about earlier, will it be lower for the full year in that case or we are going to meet that the full year target what we talked about earlier.

Sameer Hiremath: No, I think that we are seeing it will be in the 5% to 10% range for the full year versus over 10% we said earlier based on the first half performance.

Niteen Dharmavat: Okay got it. Thank you so much.

Moderator: Thank you. The next question is from the line of Rajesh Khotari from AlfAccurate Advisors Limited. Please go ahead.

Rajesh Khotari: Good Afternoon Sir. This is Rajesh Khotari from AlfAccurate Advisors India, shareholders of the company. Few questions, first is it possible for you to give the impact of each and every factor which you have mentioned, which were abnormal in nature, say for example in crop protection you have mentioned postponement of volume off take due to de-stocking, what is the impact of that, likewise if you can explain for each point what is the impact and for each point what is the outlook?

Sameer Hiremath: Well I think for this quarter the impact approximately from the crop protection business was about Rs. 40 to Rs. 50 Crores for this quarter in that range. I could not give you the exacts of the outlook or how much were due to the Mahad flooding or the Taloja matter or de-stocking, but the overall impact was close to Rs. 50 Crores for this quarter.

Rajesh Khotari: Understood, and for pharmaceutical?

Sameer Hiremath: Pharmaceutical was about Rs. 40 Crores to Rs. 50 Crores also the similar range, but some of it was de-stocking and some of due to the planned annual shutdown.

Rajesh Khotari: I understand so you know coming to crop protection, when you say Rs. 40 to Rs. 50 Crores is the impact so, should one take it as a kind of a one off effect for example the customer de-stocking whether that is near to over how much you think you will be able to recoup the normalcy, will it happen in third quarter?

Sameer Hiremath: Yes, I think the customer de-stocking will come back on between Q3 and Q4, we will recoup both of the customer destocking completely, but the production loss because of the flooding and the water cut is large part of that Rs. 50 Crores, it is more of that rather than the customer de-stocking.

Rajesh Khotari: Oh, I see, so now 3Q and 4Q basically would be more like a normalcy coming back, I am talking about crop protection I am going division by division.

Sameer Hiremath: Yes, yes we do not see unless another act of God which we hope not…

Rajesh Khotari: No, no of course I am talking about normal circumstances

Sameer Hiremath: Yes, we expect normal operations.

Rajesh Khotari: Good and on pharmaceutical side you mention in your opening remarks that finished goods inventory at customer end you expect by fourth quarter it will turn into normalcy, am I right that is what you mentioned in the opening remark?

Sameer Hiremath: Yes, improvement in Q3 but back to normal by Q4.

Rajesh Khotari: Improvement in Q3 on Y-o-Y basis on quarter-on-quarter basis?

Sameer Hiremath: Quarter-on-quarter basis.

Rajesh Khotari: Okay and the multipurpose plant shutdown what you have mentioned which is now you are saying, whether that was a bulk of the effect of the Rs. 40 Crores or was it inventory de-stocking was major factor?

Sameer Hiremath: It was about 50-50 inventory and the shutdown that was about 50%.

Rajesh Khotari: As far as your multipurpose plant shutdown is that is now on, the plant has now become operational or it is still under problem?

Sameer Hiremath: Already started.

Rajesh Khotari: Already started, okay so for full year you are looking at about high single digit, I would say between whatever 5%-10% kind of a growth and is it possible for you to give the exports and domestic breakup for both the segments, pharmaceutical and agro (crop protection).

Sameer Hiremath: It is 80% export of our business and about 20% is domestic and that will be the more or less little bit here and there between the two divisions, but that is about the same for these two businesses.

Rajesh Khotari: So that means what growth or degrowth for pharma exports, I am just going segment wise so that makes life a little bit more easy because otherwise it is a very shocking result and I am not able to figure out where you would have lost in a big way, so is it possible for you to give exports and domestic breakup from the growth perspective for 2Q?

Sameer Hiremath: It is 80:20, I think we overall as a company 80% is export and 20% is domestic.

Rajesh Khotari: Thank you.

Moderator: The next question is from the line of Pratik Sinha from Alfa Wealth Management. Please go ahead.

Pratik Sinha: Thanks for the opportunity. So I have got two, my first question is regarding this NGT and other regulatory bodies in general, they have been very stringent with pollution and control especially in the states of Maharashtra and also Gujarat, so for example Gujarat they do not allow any chemical, new specialty chemical or commodity chemical set up anywhere other than the Dahej and I believe that even in Maharashtra they are getting stringent, so it is looking like another China type situation for the whole industry, the future looks very uncertain so what gives you the confidence to give a double digit guidance for next year please?

Sameer Hiremath: First of all, all are plants are in designated chemical zones, so none of them are outside. The problem with China if you compare, in China the reason why many of these factories in China shut down because they were outside the designated chemical zone or chemical parks, so that risk of zones shutting down in India does not exist, but these are designated zones with infrastructure, common effluent treatment plant facilities outside the towns and cities plus we have five manufacturing sites spread between Karnataka, Maharashtra and Gujarat. So, we are able to kind of de-risk this to a large extent.

Pratik Sinha: The second question is I know the credit rating agency ICRA has given an A1 or even an increased level of debt, but looking at your absolute debt, I am including the working capital into it, it is high compared to your operating cash flows that you have been reporting over the recent few years, you have reported somewhere in the region of Rs. 150 Crores to Rs. 180 Crores in operating cash flows. Relative to that the debt of close to I think Rs. 800 Crores, it looks like a high debt in an uncertain world?

Sameer Hiremath: The debt is Rs. 683 Crores to be exact, not Rs. 800 Crores. Out of that long-term debt is about Rs. 380 Crores which was required for our Capex funding and our debt levels have more or less remained same in spite of growth in our top line. So, we have been able to maintain a very healthy debt equity ratio over the last few years and we have always honored our debt.

Pratik Sinha: I agree from a debt equity perceptive, but from operating cash flow to debt ratio, is there any internal target to bring debt to say within two times operating cash flows, so if your operating cash flow is Rs. 200 Crores, your overall debt should be within Rs. 400 Crores, is that sort of a number or any other number the organization is working with?

Sameer Hiremath: Yes, that will happen as our business grows and the ramp up takes place. Our long-term debt will come down and our overall debt will start coming down on a year-on-year basis as new products and new Capex comes on stream. We are investing in Capex ahead of one or two years ahead of schedule in our business, it takes two to three years to ramp up, so the nature of our business, it takes two to three years to get the cash flows going from the Capex that you put in. The debt will start coming down over the next few years and we are keeping a very strict control and eye on this overall debt level to ensure it does not go out of control.

Moderator: Thank you. The next question is from the line of Sudarshan Padhmanathan from Sundaram Mutual Fund. Please go ahead.

Sudarshan P: Sir, can you tell a bit more about your Capex, you talked about this Rs. 300 Crores of Capex of which Rs. 100 Crores odd is being spent, what I would like to understand here is if you can give a bit more color about, on both the divisions what is the capacity utilization at this point of time. The Rs. 100 Crores of money that is being spent and the Bangalore facility coming back, what kind of capacity it releases and which divisions, you can actually see some headroom coming in as far as capacities are concerned and the third is this Rs. 200 Crores, how is it going to be spread across and what are the timelines that you see in terms of also getting regulatory clearances, EC etc., and basically getting this cleared and completely executing the Capex?

Sameer Hiremath: So, I will answer those questions. First one is the total Capex is Rs. 300 Crores, Rs. 100 Crores has already been spent till September of this year, but as a work in progress Capex, it will start generating revenues by first quarter or second quarter of next year, that Rs. 100 Crores Capex. The balance Rs. 200 Crores Capex will be spent by middle of next year, so by about September 2020 and that will start generating full revenues about two years after that. It will immediately start but it will get ramped up to about two years. It is split approximately 50:50 between the two businesses. We are expecting an asset turnover of about 1.5x, so about Rs. 450 Crores to Rs. 475 Crores revenue to be generated from this Capex after full ramp up. Apart from this, we are looking at re-tooling and our product mix. If you look at our EBITDA margins, despite having lower sales, we have been able to maintain our EBITDA margins because we have been able to look at higher margin products. We are taking out some of the older low margin products and replacing them with high margin products, so our growth strategy is based on two fundamentals. One is to replace with higher margin products in our current capacity which does not call for much Capex and second put in Brownfield Capex of about Rs. 300 Crores in 18 to 24 months of which 6 months are over and use that to grow our business going forward. So the combination of the two will ensure that the business is back on track from next year, we start doing the double digit growth which we have had in the past few years and we improve our return on capital employed as well as our EBITDA margins going forward.

The third question regarding environmental compliances and regulatory compliances, well the good news is that we have got the environmental compliances for all the sites for expansion and we have compliances even from a regulatory FDA perceptive, both the Panoli and Jigani sites were just inspected two months ago so that also, the risk does not remain currently in our business. So, once we build in the Capex very quickly, we can start selling and we have the approvals already in place to start manufacturing them once the plants are ready.

Sudarshan P: Just on the question on current capacities and what capacities that Bangalore recent addition can bring in?

Sameer Hiremath: Current capacity addition is about 15% and the new Capex will add another 15% to 20% more.

Sudarshan P: The Bangalore will add another 15%, right?

Sameer Hiremath: That is what we are doing currently, de-bottlenecking and all that, it is small, but the big Capex of Rs. 150 Crores will add another 15% to 20% overall for the company.

Sudarshan P: Bangalore will be for both the agri and the pharma or is it ….

Sameer Hiremath: Bangalore is only pharma, Panoli is agri and pharma.

Sudarshan P: Okay, thanks a lot, I will join back the queue.

Moderator: Thank you. The next question is from the line of Rohit Nagraj from Sunidhi Securities & Finance Ltd. Please go ahead.

Rohit Nagraj: Sir, my question is about the guidance that you have provided, so 5% to 10% of revenue growth, now if I just make a rough calculation, we have done about Rs. 700 Crores of revenue for the first half and for achieving say 5%, we will need to do close to about Rs. 900 Crores to Rs. 950 Crores so are we equipped to make a run rate of Rs. 450 Crores odd for the next couple of quarters both in terms of capacity and the order book that is having clear visibility?

Sameer Hiremath: Well I think in terms of visibility and order book, that is intact, and our target are to do over Rs. 450 Crores per quarter, that is the target we have set for ourselves.

Rohit Nagraj: Earlier I think we have also mentioned about EBITDA margin expansion of 50 to 100 basis points per year, so where do we stand on that front?

Sameer Hiremath: Well that will happen post capacity expansion from next year onwards.

Rohit Nagraj: Just last clarification on the customs duty, so this particular litigation has been there since the implementation of the GST or is it recent, unfortunately again from the regulatory perspective, we did not inform about this issue to the investors?

Anish Swadi: Basically, the issue was known to us just recently in the month of late August and September. It actually stems back to the implementation of GST, so post the implementation of GST, to explain to you the current issue is, we are an EOU unit. We import materials duty free and then we sell them to our customers. A lot of our customers also having DTA units, which are local units. So, our customers claim duty drawback benefits when we did not pay the customs duty. So the customs came to us and claimed the duty payable on this, now we in turn have approached our customers to see how best we can be compensated for that, but this only happened in late August early September and this is an ongoing process which we just settled.

Rohit Nagraj: Okay, will there be any impact coming in future quarters as well or is it a one-time impact which has been completely been taken care of?

Anish Swadi: This is a one-time impact and it has been closed out.

Rohit Nagraj: Alright, thank you, I will come back to the queue.

Moderator: Thank you very much. The next question is from the line of Nikunj Doshi from Bay Capital Partners. Please go ahead.

Nikunj Doshi: I just wanted to express my displeasure regarding, I would say disclosure standards. The answer to the first question was totally not acceptable even the current answer to the last question also was not acceptable. In case of tomorrow if you plant falls down because of earthquake, it will be a force majeure and again you will not be informing the exchange for that.. So, this answer was really not acceptable, so I just wanted to express my displeasure.

Moderator: The next question is from the line of Sidhant Khandekar from ICICI Direct. Please go ahead.

Sidhant Khandekar: Most of my questions have been answered. Could you just elaborate on the capacity part, I missed the capacity part? What will be the current capacity utilization in Bangalore, Panoli and what will be the new capacity addition in Bangalore. I have missed that piece, if you could just elaborate it, it will be great?

Sameer Hiremath: The capacity utilization is currently about 80% to 85% and we are adding about Rs. 300 Crores of Capex between the crop business in Panoli and pharm business in Bangalore and Panoli over the next 18 months.

Sidhant Khandekar: Just one last question, what will be the new tax rate after the tax reduction by the government?

Kuldeep Jain: We will continue to use the earlier method, so our current tax rate from the P&L point of view is 32.5%, but as we had the MAT credit available, our cash tax rate is only 18% for the current year and we will continue this year and the next year under the old tax regime.

Sidhant Khandekar: Okay, thanks.

Moderator: Thank you very much. The next question is from the line of Manan Patel from Equirus PMS. Please go ahead.

Manan Patel: Just wanted to understand two things, one your credit rating report talks about a very different number on Capex than what you are talking, so can you just clarify that? Second, if we talk about 7% growth for the remaining of the year, full year, 7% to 8% growth, that would mean a high double-digit growth for the remaining six months. Is there enough visibility and which segment is going to drive that?

Sameer Hiremath: I will answer your first question about the ICRA report, about the Capex. Yes, the Capex number is higher than what I'm saying, but I am talking about the immediate Capex that is underway. ICRA is talking of long term Capex which we are going to be doing after this Capex, that is the planned Capex in phase 2, so we have undertaken phase 1 Capex which will be completed in the next 18 months and this phase 2 Capex is also in part of the ICRA rating, hence the difference in the numbers.

Manan Patel: The second question was for what you have actually delivered in the first half, to achieve the guidance of 7% to 8%, you will need high double digit growth in the second half, so, is there enough visibility there because you again mentioned in the call that the plant will just start now, so again even in October we have lost like almost full month and these are continuos plants I am assuming, so they would take some time to ramp up so how do we propose this 7% to 8% growth?

Sameer Hiremath: First of all, I did not say 7% to 8%, I said 5% to 10%, I am giving a range

Manan Patel: I took the mid point.

Sameer Hiremath: Okay, see some of our business was due to inventory correction by our customers, that business is there and we have some material already lying in inventory as finished goods that is already with us, that we will sell. So, we are quite confident that we will be able to achieve this growth in the next two quarters. This was a one off. We had a shutdown on two of our sites and the third site was a planned shutdown, we do not expect any of these to happen in the next two quarters.

Manan Patel: Sir, just last question. In the AGM, Sir mentioned that we will do 15% to 20% growth for the next year in the general meeting for the shareholders; do we still stand by that guidance?

Sameer Hiremath: Once the Capex comes on, we will have double digit growth, we are still working towards that target, yes.

Manan Patel: Thank you.

Moderator: Thank you very much. The next question is from the line of Pranay Dedhia from Panchatantra Advisors LLP. Please go ahead.

Pranay Dedhia: We have been used to very good set of numbers from Hikal, so this was definitely a disappointment. Two concerns, one is that your depreciation is lower this time around than the previous quarter as well quarter compared year-on-year, if it is an increase asset base, I do not understand how your depreciation could be lower?

Kuldeep Jain: Certain assets have been fully depreciated, so therefore the charge for the quarter and the half year have been lower.

Pranay Dedhia: Okay and more importantly, what is our average cost of funds with your debt ratio, what is the average cost of funds that you have, because what we see is that you are paying dividends to the shareholders is appreciable and paying dividend distribution tax on it as well, whereas you are having higher borrowing and you need to increase your borrowing, this does not help the investors in the long run? As an investor I prefer a debt free company.

Kuldeep Jain: That is fine, our average interest rate is 8.28%.

Pranay Dedhia: I believe if your ROE is higher than this, I do not see why you are paying dividend and not repaying the debt?

Kuldeep Jain: That is a policy by the company.

Pranay Dedhia: But that is hurting the investors in the long run is it not?

Anish Swadi: Yeah, but it is a different school of thought, right investors want we generate positive cash flows and that is why we are paying dividend again like Kuldeep mentioned, it is a policy of the company. Ours is a very Capex intensive business, so you have to borrow in order to get the Capex on the ground and then generate revenues from there and that is what we have a track record of doing. So, we will continue to do that and that is our firm policy.

Pranay Dedhia: I appreciate your concern Sir, but the point is if you have a higher Capex and you need more cash flows all the more reason for you to rather sustain with the cash flows than distribute it, it helps the investors in the long run. Well, that is my point of view, but again the management would have their own point of view, so that is the way you can go about it.

Moderator: Thank you. The next question is from the line of Devang Patel from Crest Wealth Management Pvt. Ltd. Please go ahead.

Devang Patel: Sir, the other operating income is higher for this quarter, can you please clarify on that.

Kuldeep Jain: Basically, this was because we have developed some of the products and we have charged to the customers which will be classified just only as a non-operating income.

Devang Patel: Is this one-time income that you have?

Kuldeep Jain: Not really, this keeps coming basically. We are into development of the products for the other customer as well, so that keeps coming. If you look at, averagely we have always grossed Rs. 5 Crores to 6 Crores each year.

Devang Patel: Sorry, I am still not understanding. The amount is quarter equal to the amount of full of last year?

Anish Swadi: Yes, let me just explain more clearly. Basically, we get some advance in terms of projects that we do, so we do a lot of early stage development projects for innovator customers and hence we have taken this as other operating income and when the products do commercialize then they go up into revenues or sales.

Devang Patel: Thank you.

Moderator: Thank you very much. The next question is from the line of Nisarg Vakharia from Lucky Investment Managers Pvt. Ltd. Please go ahead.

Nisarg Vakharia: While it has been very unfortunate events altogether in one single quarter, I would like to say that as investors we should also support you at your most difficult times. Every company goes through somethings which they might have not foreseen, but I do agree with some of the participants on the call that we may have been a little more sensitive in terms of disclosing these one off events, but of course you have also faced them for the first time so we understand that you may or may not know how to react. I wanted to ask you a question if I heard it correct, you said that steady state basis, we should have a Rs. 400 Crores to Rs. 450 Crores top line per quarter from the next quarter onwards, is that correct?

Sameer Hiremath: That is correct.

Nisarg Vakharia: And that is the top line which you have achieved over the last many quarters, if I see your company, that is the top line that you have achieved at your peak in March 2019, which is Rs. 457 Crores odd. So that top line you are saying can or is possible to do from the next quarter onwards itself?

Sameer Hiremath: Yes, in that range, close to that. Next quarter and Q4.

Nisarg Vakharia: That is all I wanted to know, thank you.

Moderator: Thank you very much. The next question is from the line of Bajrang Bafna from Sunidhi Securities & Finance Limited. Please go ahead.

Bajrang Bafna: I think a lot of people have talked about, just a humble request that in this unfortunate circumstances, if you could have reported to the exchanges, the damage risk of price would have been much lower you know the way the stock has reacted, if not today in the absence of precisely the information why this sort of thing has happened. So just a humble request in this plant closures and all, we see from most reputed companies they always disclose the exchanges because of certain reasons the plant has closed down during a particular period. So henceforth if you could report us, it would really be helpful. Just one question on the October month like you said most of the issues have already been resolved, so what is the current run rate in the month of October in terms of visibility from the customers as well as since the de-stocking is under progress, either there is any pricing impact which we are seeing from the customers so as to protect our margins?

Sameer Hiremath: Well the first point is taken, and we will bear it in mind. Regarding the second point, as I mentioned earlier, things are normalizing back in this quarter because this is a one-time impact last quarter. I think the question was asked earlier and answered earlier, we expect to return back to a run rate of between Rs. 400 Crores to Rs. 450 Crores in this quarter and the next quarter.

Bajrang Bafna: So, October is going normal, last 20 to 25 days?

Sameer Hiremath: Yes.

Bajrang Bafna: Just one more question, on the insurance side, any loss of business or loss of profit, are we not insured from a company perceptive so that we can claim from the insurance for this unforeseen event because I think this is something which all reputed companies also do?

Kuldeep Jain: As far as the flood is concerned, we are fully insured and we are working on it and we have already discussed with the insurance company, we will finalize it very soon.

Bajrang Bafna: Okay, thank you very much Sir.

Moderator: Thank you. The next question is from the line of Kiran Kartik from Table Tree Capital. Please go ahead.

Kiran Kartik: Sir, a couple of questions. One is slightly broader question, not specific to this quarter. So, we spent about Rs. 55 Crores R&D per year, Sir, some of our peers both of agrochemical and pharma peers spend a similar amount, but kind of generate multi million dollars molecules, can the management comment on the effectiveness of our R&D that we have been doing for the past three to four years and are there any chances of improvement, because the new molecule like Pregabalin and other gliptins have come probably this year and gliptins will come through in the future, but Rs. 55 Crores R&D and we are not generating multi million-dollar molecules like some of our Indian peers, so just wanted to know if management has any thoughts on the effectiveness of our R&D strength?

Anish Swadi: Firstly R&D does not only work on new molecules; R&D also works on improving the processes and the efficiencies of the current process or molecules that we have in both our portfolios. If you have noticed that the last two years, we have had 25% plus growth and that has come through the launch of new molecules and the improvement of existing molecules, so R&D does have effectiveness, we measure it in terms of what return we get from the investments. To address your point, we spend around Rs. 40 Crores to Rs. 44 Crores of R&D, not Rs. 55 Crores in terms of expenses, more or less between 3% and 4% of sales. Yes, going forward the new molecules that we have talked about, the Capex that we are doing, these are all innovative processes that have been developed at our R&D, they are not copycat processes. This is our own technology that we have developed in-house, and we will be launching these molecules from which we will be getting significant revenues. So yes, R&D has a measure, we measure it, we measure the performance and we do expect it to pay off. I do not know whether there is a billion-dollar molecule coming upfront, but we definitely hope so that we do have significant leverage going forward from the R&D resources or the spend that we have.

Kiran Kartik: Second question essentially is, if I look at the PBIT margins, because it is segment wise rather than the overall annual result, we are looking at 13% PBIT margins in pharm, 15% crop protection, this looks ultralow given Hikal's history, so I am just assuming that this is the bottom of margins that we are going to see this year, so just wanted to kind of see what was again reiterated in the AGM, are we looking at Rs. 2,500 Crores revenue by FY2022, are the margins going to go up quite significant given that we are adding new molecules, just wanted to get that overall outlook from Sameer.

Sameer Hiremath: Yeah, this the bottom of the barrel I think on the margin side with the new products have a significantly better margin profile and that is why the reason we are launching them. As I have mentioned earlier in my call, we are replacing some of the older products in the current plants with newer molecules, so the margin profile will improve and get back to the older historical level which were much higher than what they are today and the target for Rs. 2,500 Crores is still remain. We are still on track despite this year being a subdued and muted year and we still believe that we will be able to achieve this FY2022 target that we have set for ourselves.

Kiran Kartik: Got it, thank you so much.

Moderator: Thank you very much. The next question is from the line of Roshan Raghavan from ithought Advisory. Please go ahead.

Roshan Raghavan: My question as regarding your cash position, it is almost down to half, may I know why that is? From the last quarter, if you see the cash and cash equivalence, it is Rs. 596 million now versus Rs. 1,141 million and that is almost a 48% decrease.

Kuldeep Jain: Yes, the cash position has certainly gone down, because we do not want to keep cash with us. So, if you look at cash flow totally as Sameer has mentioned earlier, the cash flow was much better than the last half year. We generated almost Rs. 150 Crores against Rs. 98 Crores last year. We have listed many out of internal accrual into the Capex.

Roshan Raghavan: So, this was for Capex, am I right?

Kuldeep Jain: Yes.

Roshan Raghavan: Okay that was my question. Thank you.

Moderator: Thank you very much. The next question is from the line of Amit Kadam from Canara Robeco Mutual Fund. Please go ahead.

Amit Kadam: When you said that whatever the losses of H1, we should able to recoup by H2 where we should be able to come to that target run rate like 400 Crores to 450 Crores odd, and also giving a revised guidance of EBITDA for full year between 5% to 10%, so if I just go back and look at Q3 FY2019 and Q4 FY2019 number, we were already at Rs. 400 Crores to Rs. 450 Crores run rate know, so in that particular case we should be maximum it will be like a flattish growth for H2?

Sameer Hiremath: Yes, that is what. Slightly more this year.

Amit Kadam: H1 is 1%, then H2 will be in that run rate of Rs. 400 Crores to Rs. 450 Crores, we will be like a flat growth, then how would we be able to meet 7% to 8% kind of a growth for the full year?

Sameer Hiremath: We are expecting Rs. 400 Crores to Rs. 450 Crores, so the numbers are in that range and we will meet that number. The target is to grow at about 5% to 7% for the full year.

Amit Kadam: Okay, we can discuss later Sir. Second thing is that how the things are happening for shift in pharma from Gabapentin to Pregabalin? How we are going to be get impacted and how the market is also shaping up?

Sameer Hiremath: Pregabalin just got launched in the month of August in US, it was launched in Europe last year, but both the products in Europe have continued to grow. So, there are different set of patients, there were different indications. Because of the cost difference is very large between Pregabalin and Gabapentin, so they cater to different segment of patients, so we expect both of them to continue growing. We do not expect any impact on the Gabapentin overall with this.

Amit Kadam: Till date even though Pregabalin is like gradually picking up, but Gabapentin is retaining its share, that kind of impact has not come to us in terms of sales impact right Sir?

Sameer Hiremath: There has only been some de-stocking of some inventory of some products including Gabapentin, people were waiting for the Pregabalin launch. That will only be a one quarter impact, so it is not a significant impact. Overall, volumes have been intact.

Amit Kadam: Okay, any particular strategy or plans if Pregabalin is the new generation thing which down the line will try to displace this thing, how is your strategy placed to take similar market share in future in Pregabalin?

Sameer Hiremath: We are already supplying Pregabalin to customers in Europe, CIS and in Japan, we have got approvals. We have already started sales. US approvals are coming through in the next few months, so it will increase our customer base and we will have a wide range of customers and we expect that if a shift does takes place, which we do not believe it will, we have Pregabalin as a backup product which can take over from Gabapentin because many of our customers are launching both, Gabapentin and Pregabalin. Our customers and our understanding of our market is that both will remain, and both will grow.

Amit Kadam: Just to finish this particular topic, right now the numbers are like Gabapentin is 30% to 35% of our pharma revenue, is that a right number?

Sameer Hiremath: For the company it is lower than that, significantly lower than that.

Amit Kadam: Where does Pregabalin stand as of this date?

Sameer Hiremath: Pregabalin is more; it has just been launched in Europe and in Japan which have been launched last year. It will pick up in the next few years. One of the reasons for a shutdown that we did last quarter was also to increase Pregabalin capacity.

Amit Kadam: So, in pharma, likewise Gabapentin, there are also some high value product that comprises like significant part of our pharma revenues?

Sameer Hiremath: Yes, we have Bupropion which is another molecule. We have Venlafaxine, we have Quetiapine and we also have some custom manufacturing projects for innovator clients which are higher margin products.

Amit Kadam: So top five products will be like 75% to 80% of our pharma business?

Sameer Hiremath: It was 70% of our pharma business, but it will come down in the next few years.

Amit Kadam: Okay, that is all from my side. Thank you.

Moderator: Thank you very much. The next question is from the line of Anubhav Sahu from M3 Global Research. Please go ahead.

Anubhav Sahu: I have just one specific question, wanted to know more details on the de-stocking part of the pharma space, is it because of just one customer or set of clients and which category of drug or molecule this has happened?

Sameer Hiremath: It is not one customer, it is a basket of products, multiple customers are just pushing back purchases, but the demand is coming back, I mean whatever we have spoken to them, it is one or two quarter impact, not beyond that.

Anubhav Sahu: Is there any only geography, is it more pronounced say in Europe or US?

Sameer Hiremath: It is more products in the US, currently and partially in Europe, but more in US.

Anubhav Sahu: Okay got it thank you.

Moderator: Thank you very much. Ladies and gentlemen, due to time constraint that was the last question. I will now hand the conference over to Mr. Sameer Hiremath for his closing comments.

Sameer Hiremath: I would like to take this opportunity to thank everybody for joining the call. I hope we have been able to address all your queries. For any further information, kindly get in touch with the strategic growth advisors, our investor relations advisors. Thank you once again, have a great day and wish you a very happy Diwali and a prosperous New Year.

Anish Swadi: In addition we would just like to add as a company, we have noted the feedback of several investors with regards to informing the stock exchange on some material impact, so we will keep that in mind and next time we will address the situation accordingly. Thank you for all your feedback.

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