AGM INVESTOR Q&A

1. Product Revenue Split

In FY 2020 – 21, our diabetic, cardiovascular and anti – infective therapies are contributing equally i.e. 1/3rd to revenues. In the previous year, diabetes contributed 43%, whereas cardiovascular and anti-infectives contributed about 28% each. As you may have noted, Metformin being the main diabetic molecule, our dependence on Metformin has reduced in the last year.

2. Revenue & Margin Growth

The last two years were mostly focused on improving profitability even at the expense of revenue growth. Last year, particularly due to Covid, the company was very careful in doing business, so as to not expose itself to unnecessary risk of bad debts. Now that we have established a profitable customer base and the uncertainties around Covid have significantly reduced, we are focusing on volume growth through new customer acquisition and geographic expansion going forward. With regards to geographic expansion, our exports last year increased to Rs. 58 Cr viz. 46% of revenue. Going forward, particularly after EU approvals, we expect exports to surpass 50% of our sales in the next 2 – 3 years.

In the current year, we should see double digit growth in volume of both diabetic and cardiovascular therapies while growth in anti infectives will be muted. Majority of this growth will come from the existing molecules as commercial volume offtake in newer molecules will take some more time. In FY 22 – 23, we should see the newer molecules driving high double digit volume growth in the diabetic category, while cardiovascular category will see similar growth rate. Majority of the growth is expected to come from molecules other than metformin, hence we foresee the company's dependence on Metformin will reduce from the current level.

3. Cost Saving & Sustainability

The process improvements has resulted in cost reduction varying from 5 – 15% for different products at constant RM price level. It is due to improvement in yields, lower raw material inputs as well as backward integration. Backward integration is an ongoing process. Every year we take up and execute multiple projects for different products with a goal of reducing dependence on external vendors, reducing cost and becoming a reliable supplier. These types of cost reduction exercises are sustainable over long periods of time.

However, there have been fluctuations in RM prices, generally with an increasing trend since last year, which can offset any savings from process improvements. For instance, year on year, we have seen a 20% increase in the RM cost of our top 20 raw materials, which constitute more than 90% of our total raw material purchase. This has put strain on margins, which was reflected in our recent quarter results. In constant RM price terms, our profitability would have been much better. Hence, it is very difficult to predict the impact of the increasing trend in commodities and other materials on our raw material costs, especially in the near term.

However, we believe that over a period of time, the firmness in RM prices will soften. In addition, we will also be better able to pass on these cost increases to our customers. In time, the margins will improve.

On other cost parameters, some initiatives taken last year in semi variable expenses like power and fuel are sustainable over long term. However, as volumes increase, power and fuel consumption will also increase proportionally. As would be expected, labour cost will continue to increase every year due to increments and team expansion.

4. R&D

As mentioned in the annual report, we are targeting 5 – 6 API on the lab scale and 4 – 5 molecules on the commercial scale. This would mean at least one API launch at a commercial scale every quarter. The molecules in the R&D pipeline for this year are from the diabetic and anti – platelet therapeutic segment. Next year we shall be adding more therapeutic segments to our portfolio.

In addition, the R&D will be developing various intermediates and key starting materials as part of our backward integration strategy in the current year. Some of these intermediates shall also be commercialized in the current year itself.

5. Regulated Markets

The Company has addressed all the issues raised by the EU & US regulatory authorities. The Central Drug Standards Control Organization, Govt of India, has issued WHO GMP Certificate in 2016 after thorough inspection. With this certification, we can export to several countries across the world. However, we want to expand to regulated markets of EU and hence, shall be filing dossiers called drug master files (DMF) in the current year.

Post filing and review of DMF, we expect EU authorities to inspect our facility before they can give a GMP certification. However, due to the nature of the pandemic, it is extremely difficult to predict when an inspection would happen. However, we are ready to get inspected anytime.

Our target is to file 2 DMF by Q4 FY 22 for the EU market. We shall also be filing other DMF in various other markets in FY 22 as well. In FY 23, our target is to file 4 DMF in EU and many more in other markets. Although the cost of filing DMF various across countries, based on our identified markets and molecules, we estimate the cost of DMF filing over the next two years will be in the range of Rs. 50 lakh.

6. Formulations or FDF

The Company started building its formulation marketing team in FY 21. After a lot of groundwork, the Company launched its Formulation Marketing Division with the name SMRUTHI HEALTHCARE in April 2021. We have started operations in 4 southern states of Telangana, Andhra Pradesh, Karnataka and Tamil Nadu with a team of over 50 professionals. We have launched 7 brands and 15 stock keeping units in the diabetic and cardiovascular therapeutic category with an addressable market of our products at Rs. 5700 Cr growing at the rate of 11.6% CAGR.

Business Expansion of FDF

The Company plans to first stabilize its operations in the existing markets over the next 2 quarters before expanding its geographic coverage and product portfolio. The company is expecting to break even in FY 23.

Geographic Expansion

The Division faced some operational setbacks due to Covid related lockdowns in Q1 FY 22, which has resulted in a quarter's delay for initiation of geographic expansion to other states in western and northern India. Nevertheless, the Company is working to cover up lost time. The plan is to expand coverage throughout India except North East India except North East by Q2 FY 23.

Product Portfolio

The Company plans to extend its product lines by adding combinations to its existing brands and multivitamins in FY 22. New therapeutic segments will be added in FY 23 after existing operations stabilize.

7. Financial Plans

The company has accrued Rs. 16 Cr cash on its balance sheet last year due to higher profitability and lower capex. We are glad to announce a dividend of Rs. 3 per share post the bonus issue of last year. The company maintains a policy of giving consistent and growing dividends based on profitability to its shareholders as it has in done in the past.

To address the questions regarding cash utilization, we have earmarked it for various initiatives as mentioned in the annual report. I will go through some of them here.

CAPEX

Although we are not investing major capital this year for capacity expansion, we do have other initiatives for which a larger capex budget than FY 21 has been planned for FY 22. The areas of investment have been mentioned in the annual report.

OPEX

We are increasing our opex budget for R&D and Formulation marketing division in FY 22.

A significant portion of the accrued cash will be utilized for these purposes. Any leftover cash will be utilized for future capacity expansion without increasing much debt. Currently the company is not looking at any inorganic opportunities for growth and focusing on executing its organic growth strategy.

OTHER POINTS

1. We are booking MEIS benefits.
2. Due to the facilities being multi product, it is difficult to estimate exact capacity as it changes for different products. However, as a general estimate the company is operating at 65%.
3. NSE Listing: The Company's Networth is below NSE listing requirements of Rs. 75 Cr. As soon as the Company will meet all of NSE's listing norms, the company has get itself listed on NSE.