Sun Pharma Innovative R&D Demerger
Conference Call Transcript
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Corporate Participants

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Moderator:
Good morning ladies and gentlemen. I am Monali, the moderator for this conference. Welcome to the Sun Pharma conference call. For the duration of the presentation, all participants' lines will be in the listen-only mode. I will be standing by for the question and answer session. I would now like to hand over to Ms. Mira Desai of Sun Pharma. Thank you and over to you mam.

Mira Desai:

Thank you Monali. Good morning and a warm welcome to our conference call to discuss the demerger of the company that will do R&D innovation. I am Mira from the Sun Pharma investor relations team. Today our hosts are Mr. Dilip Shanghvi, Chairman and Managing Director and Mr. Sudhir Valia, Whole-time Director. We sent out a note on the demerger and a press release last evening and we hope that you have received it. These will also be shortly available on our website. The call transcript will be put up on the web site as soon as possible and a replay would be made available. It would be appropriate to mention that the discussions today may include certain forward-looking statement and these must be viewed in conjunction with the risks that our business faces. Any questions that remain unanswered during today's call can be sent to corpcom@sunpharma.com. I now hand over the call to Mr. Dilip Shanghvi.

Dilip Shanghvi:

Good morning and thank you for joining us today for the conference call after announcement of the proposed demerger of the innovative R&D business. As you know, the board of directors of Sun Pharma met last evening to deliberate on the proposed demerger of innovative R&D. A note detailing what we intend to do and the reason we are taking this approach was also sent out last evening. Before we go into question and answer, I would like to highlight the salient features of the scheme that has been proposed. Currently at Sun Pharma, we spend around 10 to 11% of our turnover on R&D. About 35 to 40% of this is spent on longer-term projects in new chemical entity and novel drug delivery systems, while the rest is spent on reverse engineering based products and process development, which fuels our current business. In doing close to 12 years of process and product development, we have learnt that this kind of work typically has a definite approach, a more or less well defined timeframe, predictable outcome and costs. Hence the risk of sudden surprises or downsides is to that extent limited. On the other hand, new chemical entity and novel drug delivery system projects not only tend to be unpredictable, fund requirements are uneven, and much larger than the simpler reverse engineering products. As a project goes through later stages of development, fund requirements escalate. Also as we know, despite the best minds and large resources committed, a project may or may not reach market. Recognizing this fundamental difference, we have proposed to divide the company into two parts, one is the reverse engineering based process and product development research and development that stays with Sun Pharma and drives the current business. The other is the innovative R&D part that is hived off in a separate company with resources, equipment, and people along with current new chemical entity and novel drug delivery system projects and all intellectual property rights related to these products. It would have enough funds to take projects ahead for next few years and its own management team. Keeping shareholder interest in mind, one share of the demerged company would be offered to shareholders who have one share of Sun Pharma on the record date. We are quite convinced that this move will create shareholder wealth and simplify the business structure of Sun Pharma and the innovative research company.

We are now open for questions.

Moderator:

Thank you very much sir. We will now begin the Q&A interactive session. Participants who wish to ask questions may please press *1 on your telephone keypad. Participants are requested to use only handsets while asking questions. To ask a question, please press *1 now. First in line is Mr. Rajesh Vora from ICICI Securities.

Rajesh Vora:

Good morning to the Sun Pharma team. Congratulations to Mr. Shanghvi and his team for making another unconventional long-term move. I think it is extremely smart strategic and positive. I just wanted to hear from Mr. Shanghvi, you know, what are his views, thought process if you can elaborate in terms of why this decision at this stage, and if you could also give us numbers of value of the tangible assets being transferred to this new R&D company?

Dilip Shanghvi:

As I think we have explained in the note that we sent yesterday, the purpose of the splitting of both the companies is the nature of business is very different. The investment, the risk profile, and the skill sets required to succeed are also very different. We believe that the current investors in Sun Pharma who have invested in a growth company, we would like to maintain for them an opportunity to stay invested in a growth company which continues to grow its profits and turnover on a consistent basis. At the same time, if they wish to be participating in the risks and the upside involved with research and development, which as we explained is relatively high risk, high return business, they can stay invested in both the businesses, otherwise over a period of time we expect that the research and development and innovative product company would attract sector investors who are familiar with investing in speciality pharmaceutical companies and who are familiar with both the risks as well as the reward associated with this. The approximate capital allocation at the time of split to the demerged company, in terms of physical infrastructure and equipment for the R&D company would be around 50 to 55 crore rupees.

Rajesh Vora:

Okay, okay. Thanks a lot and all the best.

Dilip Shanghvi:

Thank you.

Moderator:

Thank you very much sir. Next is Mr. Amrit Mathur from Business Standard.

Amrit Mathur:

Mr. Shanghvi you mentioned that the new company, the innovative R&D will have a equity capital of 50 to 55 crores, so what I am trying to understand is, I mean, obviously I know it will be a forward looking statement, but what kind of improvement in margins are we looking at in your main core Sun Pharma business? And also equity structure- this 50 to 55 crores will again have a Rs. 10 paid up capital or what will it be, if you just indicate, I know it will be forward looking, I am trying to understand your margin position going forward because your margins had been under pressure in the December quarter because of your R&D cost, so I am just trying to understand, I mean, going forward what does all this mean for your margins and operating profit side?

Dilip Shanghvi:

I think it is better to clarify. Mr. Valia can explain the capital….

Sudhir Valia:

As regards to capital structure, when we are issuing one share of the demerged company to shareholders who have one shares of Sun Pharma, we would like to keep value of the share as rupee 1. So it will have about 18 crores equity number and may be similar kind of options available for the bondholders which will then increase if it gets converted to the extent of 21 to 22 crores. So that kind of capital structure would be available.

Amrit Mathur:

Okay, so what does this now mean for the parent Sun Pharma. What kind of margin, I know it is looking forward, but what kind of margins, are we going to see margins improve obviously with so much cost going aside to the new company now, I mean, getting transferred to the new company?

Dilip Shanghvi:

Our current investment in innovative R&D is around 4% of the turnover. At the same point of time, we are likely to continue to increase our investment in process research. So the purpose is not to protect margin, purpose is to what you call focus on different set of business with different outcome probabilities in different companies.

Amrit Mathur:

Okay, I got the rationale the risky part is in a separate company. Fair enough.

Sudhir Valia:

Thank you.

Amrit Mathur:

Thank you so much.

Moderator

Thank you very much sir. Next is Mr. Madhusudhan from Citigroup.

Madhusudhan:

Good morning sir. I have a simple question, could you detail how the FCCB holders will get all these rights to the two companies and what would be the strike prices for the two ventures because I think there are some issues, and how much of the debt will get split between the two companies?

Sudhir Valia:

We appreciate your question, so far as the debt splitting is concerned we have designed it so that it will remain in the first company only, and the liability will continue to be with Sun Pharma. Only in the eventuality of the refund the money will be made available on maturity. As far as option for the conversion is concerned, as per the terms of offer bondholders are treated on par with Sun Pharma shareholders, and if a Sun Pharma shareholder is getting share of a new company without any cost, they will have a right to have the same kind of a shares in eventuality of their conversion.

Madhusudhan:

No, what you are saying is, let say I am an FCCB holder today and my strike price I think it is around 730 or something, at that price if I convert my shares, when I do the conversion then I will get a new share of both the companies?

Dilip Shanghvi:

Yes.

Madhusudhan:

So therefore, okay, so the strike price remains the same despite this stripping out of this asset from the company.

Sudhir Valia:

Correct, because there is no correction in this part.

Madhusudhan:

Sorry.

Dilip Shanghvi:

There are no corrections here.

Madhusudhan:

No, no, I am just trying to understand sir, so basically what you are saying is that even after the hiving off this R&D unit you are not bringing down the conversion price?

Sudhir Valia:

See we are not refunding or anything to existing shareholders of Sun Pharma, and similarly we are giving, similar rights to the bond holder in eventuality of the conversion. So there won't be any change in conversion price, but since we are in discussion with bond holders and the eventuality is that they would like to give up their options, in that eventuality we have to find out what should be the correct value which we should reward, and if anything is rewarded then it will effect a correction in conversion price.

Dilip Shanghvi:

But Madhusudhan I think this is a function of the negotiated settlement with the trustee of the bond holder. So as the scheme proposes, the bondholder has the same right as that of the shareholders.

Madhusudhan:

Okay, thanks. What I am just trying to figure out over here is that lets say from 1st April you go in with the demerger process, _and the entity which will be there on the stock market for sometime will be the unit which is only having the Sun Pharma core business.

Sudhir Valia:

Other company also will get listed.

Madhusudhan:

Okay so it will also get listed, now there is interim value which will be there between the two entities, so one should probably expect a correction on the Sun Pharma core business from whatever the value to the R&D unit will be ascribed, right?

Dilip Shanghvi:

What we plan to do is at least 30 days before the potential listing and splitting of the business, we will give much more details of the innovative product pipeline that we have, which generally we have not been giving till now. The idea would be to allow people to find a method by which they can value that part of the business, so that when it gets listed there is a fair relationship between its market value and the intrinsic value.

Madhusudhan:

Okay, sir just one more question, have you given any thought as to how much cash you are going to transfer? You said this R&D unit will be able to sustain itself for the next few years, have you given any thought to how much that would imply in terms of cash that you would be putting into this company?

Dilip Shanghvi:

The way it is currently structured it would be able to operate for 2 years for all its funding requirements, and we expect that within 2 years there should be a much more clearer value, so either they can raise money or would be able to raise thelicensing fees for their products in some of the markets. Approximately 200 crore rupees will be given to the research company.

Madhusudhan:

Okay, thanks so much sir, and all the best for the future.

Dilip Shanghvi:

Thank you.

Moderator:

Thank you very much sir. Next is Mr. Abhay from HSBC.

Abhay:

Congratulations on a totally different strategy. Just a couple of questions, #1 is, you talked about 200 crores being transferred to the new R&D company, now this 200 crores will be entirely cash or, you know, you are talking about the asset block of that company being a part of this 200 crores?

Dilip Shanghvi:

200 crore would be cash.

Abhay:

Okay, and you are estimating that this company would be, you know, would be able to spend this money in about 2 to 3 years, is that what you are looking at?

Dilip Shanghvi:

That is correct.

Abhay:

So it would be spending about you know 50 to 75, 80 crores a year, this would be roughly the sort of number we could look at in terms of the R&D spend for that company.

Dilip Shanghvi:

Approximately that is what we estimate.

Abhay:

Yeah, just a followup question now. Typically you know when companies do R&D that is more for the long term growth prospects, and though we all agree that it is a high risk activity, but it is required for the growth requirement, future long term growth requirements for the parent. Now in such a scenario that you have hived off the business and that will remain a totally independent company going forward, would we see, I mean, would we be concerned that it would impact the long term growth prospects for the generic company?

Dilip Shanghvi:

Our view is that the generic business on its own can continue to grow more or less or maybe even more aggressively in future. We have hardly any share of business in US which will happen and can continue to grow. We are currently not present in Europe or in Japan. There are many, many products that are very interesting, very profitable, and can be genericized. So we believe that there are medium and long term opportunities in generic business, and with our ability to develop and manage products based on complex technology, the existing Sun Pharma business has significant future growth prospect. Our view is that it is important for our generic business to be international sized business going forward, and this focus only on generic would help us achieving that.

Abhay:

Okay so that does it mean that Sun Pharma, I mean, in future you would not get into the branded space even for generic products for the US market?

Dilip Shanghvi:

Branded products will not be marketed by Sun Pharma, yes, that is…

Abhay:

So your focus would remain a very clear and substantial generic across any market globally, that is what the focus of Sun Pharma would be?

Dilip Shanghvi:

Absolutely.

Abhay:

Okay fine. Sir the other thing is you know, there was also talk about margin pressure or whatever, sir are we seeing so much of pressure on margins that this thing had to be done at this point of time?

Dilip Shanghvi:

Abhay just me clarify. When I say that this company will focus on generics, what I meant is it will focus on generics in the regulated market. In markets like Russia, Brazil, Mexico, it will continue to market branded generics through field force like we are doing.

Abhay:

Yeah, yeah that is right. Yes, sir on to the next question of you know this pressure on margins, you did talk about that the R&D investment will increase at a much faster rate than the growth of profitability of the generic business, so is there some issue of pressure on margins also which is being felt at this point of time?

Dilip Shanghvi:

I think the kind of research investment as a generic company we would have ended up doing would have been in excess of 15 to 18% if both the businesses would have stayed together. At the same point of time our view is that managing innovative products and businesses requires a very different skill set than generic , and also focus of management, priority for management, so it is better to split both of them. So, I mean, if I am giving an impression that the decision for splitting the company is for the purpose of protecting margin then I think I am only giving partial, what you call, reflection of our thinking. The key purpose of decision is to be able to manage business more effectively.

Abhay:

So that means you would have a entirely, other than the chairman, which is being yourself, I mean you would have a full set of a management team out there, who will be different from the ones who are leading the generic business?

Dilip Shanghvi:

Absolutely. I think over a period of next 12 to 18 months that is what we wish to achieve.

Abhay:

Sir going on to a lateral question, you know, with this sort of a hive off do we see that R&D company getting into services, I mean, say contract research or whatever, could that also be a sort of a driver now that it is out of, you know, it is not into generics per se?

Dilip Shanghvi:

No, I think the strategic focus for us does not change, which is creating value for shareholders. We are not in services business.

Abhay:

Okay fine, thank you sir. Thank you.

Moderator:

Thank you very much sir. Next is Mr. M. G. Arun from Financial Express.

M. G. Arun:

Good morning Mr. Shanghvi. My question is regarding the new innovative R&D division. Can you give me some more specific details of this division? What are the NCE areas that you will be working on and what are the out licensing opportunities that you see in this, and what is the kind of manpower that you are going to have in this new division?

Dilip Shanghvi:

As I explained I think 30 days before the division, I mean, the new company is to be listed, for the purpose of allowing people to estimate the value we will give much more detailed presentation and information related to pipeline. So I am not able to share specific information with you right now. We expect that the innovative research company would have around 120 to 140 people initially and that would continue to expand. Those would be scientists in medicinal chemistry, biology, clinical development, and various other aspects of delivery system research.

M. G. Arun:

So the unit is going to be basically based in Bombay?

Dilip Shanghvi:

Both in Bombay as well as in Baroda, both research centers would have part of the research center doing innovative research with specific set of people and separate laboratories.

M. G. Arun:

Okay, thank you very much.

Dilip Shanghvi:

Thank you.

Moderator:

Thank you very much sir. Next is Mr. Gautam Trivedi from Goldman Sachs.

Gautam Trivedi:

Yes hello Dilipbhai, how are you? I had a quick question with respect to something similar which Dr. Reddy's did last year, and they got in a strategic partner which is ICICI Ventures, do you have plans to do something similar?

Dilip Shanghvi:

I think it is slightly different, what they have done is they have only licensed out four products to a company which is going to do clinical development, and they have given rights of these products for some of the international market to the joint venture company. I think they continue to do innovative research in Dr. Reddy's within the company. What we have done is we have separated both the companies and we have not got in any external funding, we will continue to fund this from the existing cash flow and for the benefit of the existing shareholders.

Gautam Trivedi:

Okay, thank you.

Moderator:

Thank you very much sir. Next is Mr. Kaustubh from Crisil.

Kaustubh:
Hello.

Dilip Shanghvi:

Yes, hello.

Kaustubh:
Good morning sir. Sir I had a couple of questions, you mentioned cash moving out of around 200 crores, I wanted to get a feel on the total capital employed that would move out in terms of assets, and you know a part of debt will also move?

Sudhir Valia:

No debt will not move. Just as Mr. Shanghvi expressed assets is around 50 to 55 crores.

Kaustubh:
50 to 55 crores of assets and 200 crores of cash, is that understanding correct?

Sudhir Valia:

Yes.

Kaustubh:
Okay, another question sir would this new entity be consolidated with Sun Pharma?

Sudhir Valia:

No, it will be a mirror image, but there is no relationship in terms of a subsidiary holding.

Kaustubh:
Okay

Sudhir Valia:

They are two independent companies.

Kaustubh:
Okay, so they will not, in consolidated accounts of Sun Pharma this new entity will not be in involved.

Sudhir Valia:

Sure.

Kaustubh:
Okay, another question sir this new entity you mentioned that this 200 crores would be enough for the research expenditure for the next 2 odd years, so beyond that if this new entity were to raise debt would Sun Pharma act as a guarantor?

Dilip Shanghvi:

I don't think that Sun Pharma would do anything for this company without getting anything in return.

Kaustubh:
Okay sir.

Dilip Shanghvi:

If it stands for a guarantee, it would expect any form of return which will justify guarantying the debt.

Sudhir Valia:

If you appreciate, today the shareholders are the same. Any distribution that is there is within the shareholders. After 2 years the set may be different.

Kaustubh:
Right.

Sudhir Valia:

And it will be unfair if something is done at a cost of one part of the shareholders.

Kaustubh:
Okay, true sir. Another thing sir, you mentioned that at present around 4% of your turnover is for R&D towards innovative research, so when this innovative research moves to this new company in terms of quantum will the R&D expenditure go up for this new entity? Would there be more focused energies on innovative research and would the R&D expenditure go up?

Sudhir Valia:

As Mr. Shanghvi expressed as time passes there is an escalation in the commitment of funds for the same project, at the same time newer project also will be coming up because once it is a company with focus, the whole objective of segregating is to give recognition and focus to the innovative research which otherwise seems to have been diluted -a loss to some extent.

Kaustubh:
Okay. Another thing sir, will this new entity also look at contract research for other companies, innovative pharma or any other companies?

Dilip Shanghvi:

No.

Kaustubh:
Okay. Thank you so much sir.

Dilip Shanghvi:

Thank you.

Moderator:

Thank you very much sir. Next is Mr. Rahul Sharma from Karvy Stocks.

Rahul Sharma:

Hello sir. Good set of parameters for the R&D sir. I just had a query on, we have around 10 to 11% of our revenues allocated to R&D of which around 7 to 8% is for revenue R&D, I just wanted to get clarity how much of innovative R&D is done through revenue R&D?

Dilip Shanghvi:

We did not understand the question?

Rahul Sharma:

Total we spend around 10 to 11% of our revenues on research.

Dilip Shanghvi:

That is correct.

Rahul Sharma:

Out of which around 7 to 8% is on revenue R&D which is charged to the profit and loss account.

Sudhir Valia:

All 11% as on today is cash.

Rahul Sharma:

Sir, part of it is capital R&D, and is it capitalised, or the entire thing of 10 to 11% is charged because what I gather was 10 to 11%, 3 to 4% is for NCE research and long term, what extent of capital expenditure on the equipment and other things and that is capitalized and not charged, can you give me some clarity sir?

Sudhir Valia:

To the extent of the capital expenditure that is not charged what you say is correct, and charges are there only to the extent of revenue expenditure. Within the revenue expenditure this portion of R&D, innovative, is also charged. Now between the capital expenditure and the revenue expenditure if we are understanding then today for the last 4 years we have been doing the innovative research and the assets which we are talking is having a worth only 50 crores. So generally the initial stage set up cost is higher, but the running cost of them is not so in the terms of fixed assets.

Dilip Shanghvi:

I think the question is how much of the 8% revenue R&D is for the innovative R&D. I think the overall R&D spend including capital investment is around 4%.

Rahul Sharma:

Sir, the thing is I just wanted out of the 11% R&D, 8% is revenue R&D, and that is charged 2 P&L, am I getting it right sir?

Sudhir Valia:

That is correct.

Rahul Sharma:

And out of that how much is for out of revenue R&D, how much is allocated for innovative R&D?

Dilip Shanghvi:

We don't have currently the split in terms of the revenue as well as the capital allocation, but I think when we give more detailed information at that time we will give more information.

Sudhir Valia:

But ideally it should be 1% and 3%, if we say 4%. So the 25% of the research R&D is on the capital and the 75% on the revenue.

Rahul Sharma:

You are saying that 25% of 8% is capital R&D.

Sudhir Valia:

See, we say that suppose we say 4% is innovative R&D, then 25% of that is for the capital so that is 1%.

Rahul Sharma:

Okay, So the rest is innovative R&D which is also part of our long term research. Okay sir, thank you.

Moderator:

Thank you very much sir. Next is Mr. Pawan from Kotak.

Pawan:

Yeah hi. Congratulations on this innovative move. My question is that lets say the new company develops a product and in that case does Sun Pharma, the existing company, does it have the first right of refusal for marketing or is there, I mean, is there any such relationship to the assets developed by the R&D company?

Dilip Shanghvi:

This relationship between Sun Pharma as well as the new innovative research company logically it would be more appropriate to introduce products using with Sun infrastructure, but any rights that the new company will give to Sun Pharma will be a arms length transaction

Pawan:

Hello.

Sudhir Valia:

Yes.

Pawan

I am sorry I missed the last portion.

Dilip Shanghvi:

Both the companies will have business relationships on arms length basis.

Pawan:

Okay, okay. Thanks. Thank you so much.

Moderator:

Thank you very much sir. Next is Mr. Harshad from ABN Amro.

Giri:

Hello, this is Giri here. Just couple of things Dilipbhai, You know, on the innovative R&D side you said you will give more details -at this point in time can you please let us know in terms of how many NCE molecules you are developing and how many NDDS molecules that are there? If we can know what stage they are at, any indication on that right now will be helpful.

Dilip Shanghvi :

Giri, what we have shared with investors till now is that, one, new chemical entities going into phase 2 shortly, we should be filing a IND with the US FDA about that very shortly. And two delivery system products will go into US and European clinical trial within next few months and for that also we should be giving more detailed information about the nature of innovation and all of that in next may be 1 or 2 months.

Giri:

Okay fine, thanks.

Dilip Shanghvi:

Thank you.

Moderator:

Thank you very much sir. Next is Ms. Jyothi from Business Line.

Jyothi:

Good morning Mr. Shanghvi. I just wanted to find out how many researchers will continue to remain with the generic company, you said 140 in the new unit; and the second point is, at a later stage since there is a high risk profile will we look at cushioning that risk either with a strategic investor or venture cap or some such thing?

Dilip Shanghvi:

We have approximately 400 people in R&D, so the rest of the people, research scientists will be in the process research. We have currently no intention of having any strategic investor in the research company.

Jyothi:

Thank you.

Dilip Shanghvi:

Thank you.

Moderator:

Thank you very much mam. Next is Mr. Ravi Shenoy from HDFC Bank.

Ravi Shenoy:

Good morning sir. Sir I needed some clarity on the balance sheet side. You were talking about roughly 250 crores of capital employed in the new company and about 18 crores of equity as of now, what would the rest on the liability side be, would that be net worth that one is talking about since one is not talking about transfer of any debt?

Sudhir Valia:

Yes, what you say is right.

Ravi Shenoy:

Secondly sir, if that is true, then would that mean that the book value of Sun Pharma would come down to that extent?

Sudhir Valia:

Naturally.

Ravi Shenoy:

Okay. Thirdly sir we have some arrangement with Caraco for transfer of technology, would that be impacted in anyway by transfer of projects, by the de-merger?

Sudhir Valia:

No.

Ravi Shenoy:

Okay, and my last question sir we are transferring certain R&D personnel into the new company, would their cost be included in the R&D expense as of now?

Sudhir Valia:

It is correct. As on today it is part of the consolidated companies R&D expenses which will get split once the new company is formed.

Ravi Shenoy:

Okay, these personnel expense would not be in the form of staff expense sir? Hello…

Sudhir Valia:

Yeah, we are telling you, just a moment. The R&D personnel cost are charged to the personnel account…

Dilip Shanghvi :

They are under the head of personnel expenses, but at the end of the P&L account we give a separate overall R&D spend, in that also personnel related to R&D is shown. This does not reflect in books, but that is consolidated expenses related to R&D in various heads.

Ravi Shenoy:

Okay, thank you sir.

Moderator:

Thank you very much sir. Participants who wish to ask questions may please press *1. Next is Mr. Jesal Shah from JP Morgan.

Jesal Shah:

Yes hi, good morning. I just had one or two questions, firstly, if you can just throw some light on what would be the tax implications for the de-merger, both for Sun Pharma as a standalone entity and the transaction itself?

Sudhir Valia:

Transaction will have no tax implications. So far the de-merged entity is concerned, it has its own standing and based on the income and the expenditure, which they incur, they will have taxability. They continue to have the same benefit which otherwise is there of 150% of the revenue to be given as a weighted deduction. So the new entity will not have major implications as we foresee in near future. As regards the main entity Sun Pharma, currently we have hardly marginal tax liability, and going future for next 3 to 4 years we do not expect that our tax rate will change.

Jesal Shah:

So even after transferring this much R&D expenditure and not having those kind of weighted average deductions available for Sun, you are anticipating that the tax rate for Sun Pharma will not change. So are you anticipating some more tax benefits, why is the tax rate not likely to go up for Sun Pharma?

Dilip Shanghvi:

It will go up marginally, but not huge. There is no significant impact.

Jesal Shah:

Okay. Secondly, while just trying to make some model for Sun, if you could, you know, last year your R&D expenditure which you had shown was about close to about Rs. 1 billion, and looking at the run rate for the current year, lets say it works out to about, lets say assuming about Rs. 1.5 billion as the R&D expenditure, so if you could just tell us how much of this in absolute amount will be the innovative R&D cost?

Dilip Shanghvi:

Around 35% should be the innovative, 35 to 40% should be the innovative R&D cost.

Jesal Shah:

So close to about 60 crores will be the innovative R&D cost.

Dilip Shanghvi:

Slightly less, yes.

Jesal Shah:

Okay, and incrementally what kind of expenditure are you looking at in the next year on the innovation side?

Dilip Shanghvi:

Around 70 plus crore in the first year.

Jesal Shah:

Is that incremental or is that the total you are indicating?

Dilip Shanghvi:

That will be the total expense, 70 to 80 crore rupees in the first year.

Jesal Shah:

So incrementally it is only about 10 to 20 crores is that right?

Dilip Shanghvi:

It would be around 30 to 35 crores.

Jesal Shah:

Incrementally 30 to 35 crores, right. Okay, and the last question was from my side, are you envisaging any revenue generation in the new company or is the new company only going to be engaged in R&D activities or will it also be engaged in marketing products and so on?

Dilip Shanghvi:

No, it will not be engaged in the marketing of products right now. At some point when their own innovative product comes to market they need to decide whether they want to market it themselves or license out or leave it to Sun Pharma or do any other thing, and since they have no other revenue source initially it will only have R&D….

Jesal Shah:

Okay, thank you so much.

Dilip Shanghvi:

Thank you.

Moderator:

Thank you very much sir. Next is Mr. Sameer Baisiwala from JM Morgan Stanley.

Sameer Baisiwala:

Given the fact that the two entities would belong to the same family of the company and would have the same promoter, how would you assure the minority shareholders, lets say for example, the value in the research entity would remain vested in there in, because in the next 2 to 3 years, there can always be a manufacturing deal, will the value get shifted from one entity to the other?

Dilip Shanghvi:

What I think Sameer you need to keep in mind is that there is no purpose that we achieve as owners by shifting value from one company to another company because the equity that owners have in both the company is not different.

Sameer Baisiwala

But it can be different in the future.

Dilip Shanghvi

Hypothetically, how much different?

Sameer Baisiwala

Okay.

Dilip Shanghvi

I mean we own 70 plus % of this company. We may own 75% of another company.

Sameer Baisiwala

Okay.

Dilip Shanghvi

Is that enough?

Sameer Baisiwala

No, I mean that is pretty close actually.

Dilip Shanghvi

So it hardly matters.

Sameer Baisiwala

Okay.

Dilip Shanghvi

And I think it is good that you asked this question that the purpose of splitting the company is in no way, with no intention to benefit any group of shareholders. It is a strategic business decision which is very different from what people have taken in the past. Because it is different I understand that there is a significant level of curiosity as well as uncertainty related to the decision, but I am reasonably confident that as time progresses people will see the logic and the benefit of the new structure. Almost everything that we have done in Sun Pharma is typically very different from what others have done, and in a way that has helped the company grow fast. I hope that this strategy will also achieve similar kind of benefit for the shareholders.

Sameer Baisiwala

Okay that is comforting. The second question is when do you think that the research entity would start generating revenues.

Dilip Shanghvi

There are two types of revenue that the research company can generate, One, when it licenses out the product, and the second is when the products come to market. For some of the markets, I think at least after 3 years we should be able to license some products out, and 4 years down the line we should also see the revenue coming from some of the major markets in terms of either royalty or in terms of marketing of products.

Sameer Baisiwala:

Okay, and the last question is, of the total amount that has been spent on the innovative research, how would you break up for NCE and the NDDS?

Dilip Shanghvi

We don't have that separate breakup but I think as time progresses we will, in the innovative company, start giving more detailed information about the various activities and spend.

Sameer Baisiwala

Okay, thank you very much.

Dilip Shanghvi

Thank you.

Moderator

Thank you very much sir. Participants who wish to ask questions may please press *1. At this moment there are no further questions from participants. I would like to hand over the floor back to Ms. Mira Desai for final remarks.

Mira Desai
Thank you very much everyone for all your questions and for joining us on this call. Thank you and have a good day.

Disclaimer: it may be appropriate to mention that this communication may contain certain forward looking statements and these must be viewed in conjunction with the risks that our business faces.