Sun Pharma Q1 FY21
Earnings Call Transcript
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Corporate Participants

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Moderator: Ladies and gentlemen, good day, and welcome to the Sun Pharmaceutical Industries Limited Q1FY21 Earnings Conference Call. 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.

I now hand the conference over to Mr. Nimish Desai. Thank you, and over to you, sir.

Nimish Desai: Thank you. Good evening and a warm welcome to our first quarter FY21 earnings call. I am Nimish from the Sun Pharma Investor Relations team. We hope you have received the Q1 financials and the press release that was sent out earlier in the day. These are also available on our website.

We have with us Mr. Dilip Shanghvi – Managing Director, Mr. Abhay Gandhi – CEO (North America), Mr. C. S. Muralidharan (CFO) and Mr. Kirti Ganorkar (Head – India Business). Today the team will discuss performance highlights, update on strategies and respond to any questions that you may have. As is usual, for ease of discussion we will look at the consolidated financials. Just as a reminder, this call is being recorded and a replay will be available for the next few days. The call transcript will also be put on our website shortly.

The discussion today might include certain forward-looking statements and these must be viewed in conjunction with the risks that our business faces. You are requested to ask two questions in the initial round. If you have more questions you are requested to rejoin the queue. I also request all of you to kindly send in your questions that may remain unanswered today.

I will now hand over the call to Mr. Shanghvi.

Dilip Shanghvi: Thank you, Nimish. Welcome, and thank you for joining us for this earnings call after the announcement of financial results for the quarter of FY21. I hope you and your family are safe and healthy.

Let me discuss some of the key highlights. Consolidated sales for the quarter were at Rs. 7,467 crores. This is in line with the comments in our Q4 call wherein we had indicated some softness going forward. The Q1 performance shows we have done well and have not lost market share in any of the key products or key specialty products in the US or in any other market. Our timely risk mitigation initiatives ensured smooth operations of our manufacturing network, thereby maintaining continuous supplies of APIs and formulations for our customers and patients.

Also, for the Q1 last year, we had the onetime contribution from special business in the U.S., and hence the numbers are not comparable to that extent.

Let me now update you for our global specialty business. We witnessed the impact of the lockdown on our US specialty business, which we view as temporary. For Q1, our global specialty revenues were approximately US$78 million across all markets, while specialty R&D accounted for about 39% of total R&D spend for the quarter.

We have recently received regulatory approval in Japan for Ilumya and launch preparations have been initiated. This launch in Japan will be a step forward for Sun Pharma in expanding the global franchise for Ilumya. We have also recently entered into an exclusive licensing and distribution agreement with Hikma Pharmaceuticals for commercialization of Ilumya in the Middle East and North Africa region.

Abhay will give you more details on the specialty business later.

We've commenced clinical trials in India for two products, which we are repurposing for COVID-19. These trials are progressing quite well. As a matter of fact, because of the current large number of patients across the country, the enrollment is much faster than originally planned, and hopefully we should be able to announce the result of these two studies possibly after two quarters.

We continue to focus on employee protection, keeping workplace COVID-free, while at the same time engaging with doctors in a safe and consistent way, and ensuring supply continuity of our products across markets.

I will now hand over the call to Mr. Murali for a discussion of Q1 financial performance.

C. S. Muralidharan: Thank you, Mr. Shanghvi. Good evening, everyone, and welcome to all of you. Our Q1 financials are already with you. As usual, we will look at key consolidated financials.

Q1 sales are at 7,467 crores down by 9.6% over Q1 last year. Material cost as a percentage of sales was 26.4%, lower than Q1 last year due to product mix. Staff cost was at 23.6% of sales, higher than Q1 last year mainly due to a lower sales base and increase in field staff in India and the US. There was no rationalization of manpower across the organization due to the COVID-19 pandemic. Other expenditure was at 28% of sales, lower than Q1 last year mainly due to reduced marketing, selling and traveling expenses across markets.

EBITDA for Q1 was at Rs. 1,725 crores with EBITDA margin at 23.1%.

For this quarter, Taro had a provision of about US$419 million related to the settlement with the Department of Justice in the U.S., plus an additional provision of about US$60 million for the related ongoing multi-jurisdiction civil antitrust matters, totaling to US$479 million or about Rs. 3,633 crores. Adjusted for this one-time exceptional charge, as well as the minority interest on it of Rs. 832 crores, the adjusted net profit for Q1FY21 was Rs. 1,146 crores with adjusted EPS of Rs. 4.78. Including the above exceptional charge, the company reported a net loss of Rs. 1,656 crores.

Let me now discuss the key movements versus Q4 of last year. Our consolidated sales were down by 8% Q-on-Q, mainly due to sequential decline in Taro sales as well as in US specialty sales. Material costs at 26.4% of sales are lower than Q4 on account of efficiencies and management of inventories, including the provisions for the slow and non-moving. Staff costs at 23.6% of sales are higher than Q4 mainly due to lower sales base, merit increase and increase in field staff in India. Other expenses at 28% of sales are lower than Q4 due to decreased marketing, selling and traveling expenses across markets. We had a forex gain of Rs.79 crores for Q1 against forex loss of Rs. 143 crores in Q4.

Reported EBITDA for Q1 was at Rs. 1,725 crores, higher by 37% compared to Q4 last year. Adjusted net profit for Q1 was at Rs. 1,146 crores, higher than Q4 adjusted net profit by about 73%. During the quarter, the company has reduced its debt position by approximately US$200 million as compared to the quarter ended March 2020.

Let me now briefly discuss Taro's performance.

Taro posted Q1FY21 sales of US$ 117.6 million, down 27% over Q1 last year. Excluding the one-time charge of US$ 478.9 million, net profit was US$ 29 million compared to US$ 66.2 million in Q1FY20. Taro's reported net loss for Q1 was US$ 434.9 million.

Taro reported settlements and loss contingencies of US$ 478.9 million, which reflect the one-time settlement charge of US$ 418.9 million related to the global resolution of the Department of Justice investigations into the U.S. generic pharmaceutical industry. An additional provision of US$ 60 million has been taken for the related ongoing multi-jurisdiction civil antitrust matters. The ultimate outcome of the antitrust matters cannot be predicted with certainty.

I will now hand over to Mr. Kirti Ganorkar, who will share the performance of our India business.

Kirti Ganorkar: Good evening, everyone. Thank you, Murali. Let me take you through the performance of our India business. For Q1, sales of branded formulations in India were Rs. 2,388 crores, a growth of 3.2% over Q1 last year and accounting for approximately 32% of total sales.

Given the challenges of the lockdown across India, we have done well for Q1 and have retained our overall market share. Our chronic business has shown good performance. We faced some challenges in the acute segment due to closure of doctor clinics in the quarter. Also, as expected, there were savings in branding & promotion and travelling due to the lockdown.

While many doctors have started their clinics recently, the patient flow still remains low. For non-Covid hospitals, OPDs are gradually starting.

We continue to engage with doctors digitally for brand promotion and new launches. Our medical representatives have started field work, barring in those areas that have been designated as containment zones by the respective governmental authorities.

Our expansion of the field force in India is nearing completion which will help us in the long-term to enhance our geographical and doctor reach.

For Q1, we launched 10 new products in the Indian market.

Sun Pharma is the largest pharmaceutical company in India and holds approximately 8.2% market share in the over Rs. 142,000 crore pharmaceutical market as per June 2020 AIOCD-AWACS MAT report.

We also continue to remain the partner of choice for in-licensing, given our strong no. 1 position in many therapy areas.

I will now hand over the call to Abhay.

Abhay Gandhi: Thank you, Kirti. I will briefly discuss the performance highlights of our US businesses.

For Q1, our overall sales in the US were at US$ 282 million, accounting for approximately 29% of overall sales. Although we recorded a 33% decline YoY, the numbers are not strictly comparable as sales for Q1 last year included a one-time contribution from the special business in US.

Let me now update you on developments in our specialty business.

Our specialty revenues in US have declined over Q4. This quarter reflects the full impact of the lockdown due to Covid-19. Two of our specialty products – Ilumya and Levulan – are clinic administered products. Hence, the temporary closure of clinics has impacted these products. The decline is mainly driven by lower sales of Levulan as the entire treatment is undertaken in the clinic setting. Cequa also witnessed some decline in sales compared to Q4.

For most part of the quarter, dermatology and ophthalmology clinics were closed. However, the important thing to note is that we have not lost market share in any of our key specialty products. Prescription share is now near to pre-COVID levels, and we also see a month-on-month sales improvement.

We continue to rely on digital engagement with doctors and healthcare workers for promoting our products. Patients in US have also significantly expanded their digital connect with doctors.

Let me now update you on our US generics business.

As you all have seen, Taro has recorded a decline in sales for Q1 leading to a de-growth in our overall generics sales for the quarter. The US generics business continues to be competitive.

I will now hand over the call to Mr. Shanghvi.

Dilip Shanghvi: Thank you, Abhay. I will briefly discuss the performance highlights of our other businesses as well as give you an update on our R&D initiatives.

Our sales in emerging markets were at US$ 173 million for Q1, down by about 10% year-on-year and accounting for 18% of total sales. The decline is driven by reduction in tender revenues in our South Africa business. Excluding this tender business, sales are flat compared to Q1 last year.

Formulation sales in Rest of World markets excluding, US and Emerging Markets, were US$ 136 million in Q1FY21, down by about 18% over same period last year. This decrease was mainly driven by lower sales in Japan coupled with some decline in Taro's RoW sales. RoW markets accounted for approximately 14% of Q1 revenues.

We have done well in our API business, with Q1 sales at Rs. 554 crores, up by 20% over Q1 last year.

We continue to invest in R&D for enhancing our specialty and differentiated generic pipeline. Consolidated R&D investments for Q1 is Rs.421 crores, accounting for 5.6% of sales. Our current generic pipeline for the US market includes 95 ANDAs and 6 NDAs awaiting approval with the US FDA.

Over the past few months, we have learned how to operate well in the Covid-19 environment. This experience has imparted more resilience to our business. We continue to focus on supply chain and on ensuring business continuity without compromising the safety of our employees. With this, I would like to leave the floor open for questions. Thank you.

Moderator: Thank you very much. We will now begin with the question and answer session. The first question is from the line of Prakash Agarwal from Axis Capital. Please go ahead.

Prakash Agarwal: My first question is regarding the other expenses. So, I'm just trying to understand there's been a significant drop both Q-on-Q and Y-o-Y. So, you mentioned a large part of it is India, or you mentioned marketing, selling and traveling expenses have been lower. So, I'm trying to understand, is it largely India-led or is it a function of the US branded marketing initiative also, which has come down and it has an ability to come back again once it is normalizes?

C. S. Muralidharan: So, I did mention that the marketing sales and traveling has been lower across regions.

Prakash Agarwal: If I see the stand-alone, I see that India reduction is less. So, I'm just trying to understand is the US a bigger piece or India is a bigger piece?

C. S. Muralidharan: No but, at the end of the day you are seeing a delta which is material enough, which is driven by the factor what was explained. And both India and US and other markets also contributed to this.

Prakash Agarwal: Okay. It is across the market, is what you said?

C. S. Muralidharan: Yes.

Prakash Agarwal: Okay, thank you. Fair enough and my second question.

Nimish Desai: Prakash. This is Nimish here. Just to add to what Mr. Murali is saying, you also must keep in mind that the entire India business is not reflected in our stand-alone numbers. You know that a part of the India business is also in one of the subsidiaries. So, looking at consolidated number is much better rather than stand-alone.

Prakash Agarwal: Fair enough. I understood that. And my second question is on the specialty business. Given the lockdown, sales have come down. R&D as a percentage has moved up. Just top management thought process is there a plan moving ahead to monetize part of it to reduce the burden. We could clearly see the margin that has come up with reduction in costs. Is there a plan to monetize a part of our specialty asset going ahead maybe two, three years out?

Dilip Shanghvi: No, there's no such plan to monetize the specialty business. The focus is on growing that business and potentially looking at future synergistic addition. That is something that we've clarified multiple times.

Prakash Agarwal: No, I have not asked it properly. I meant to create an SPV and sell up stake out of it so that.

Dilip Shanghvi: We have no need. We are generating enough cash so that we don't need to create SPV to generate cash.

Moderator: Thank you. The next question is from the line of Tushar from Motilal Oswal. Please go ahead.

Tushar Manudhane: Just on the India business side, just if you could share your experience in terms of launching products during the COVID phase, where I presume there would be a lot of digital connect with the doctors on one hand, and at the same time there has been relatively reduced patient, doctor connect. So how do you map the way the product launches that would have happened has converted to revenue. Though two, three months is quite a short period to map, but just if you could throw some light on it?

Kirti Ganorkar: Sure. This is Kirti. As I said, we have launched 10 new products, and almost close to 27 SKUs during the first quarter. And this has been a very different experience of launching product digitally to the doctors. Making it available into supply chain was also challenging. So, what has happened is some of these new products which are having less competition and some unique features, they are doing well, and they are also available across the supply chains. So, our experience is launching a new product digitally is challenging and since the patient flow at the doctor is also limited, there is less opportunity for the doctors to write a prescription for a new therapy or for a new molecule. But this is in the short term. Going forward in next quarter or following two to three quarters, it should pick up. But only the advantage of digital launching is now doctors know our brand very well because they have been exposed digitally during the launch of the product. So, whenever they get opportunity, the sales will pick up for new products.

Tushar Manudhane: So, does it mean that structurally, the operating cost for launching product will be lower compared to the campaigns, which pre-COVID we used to have?

Kirti Ganorkar: For the first quarter, where we have launched new products, most of them were launched digital. So, the cost of launching the product digitally is lower than what we do in a normal case when we launch product physically to the doctors.

Tushar Manudhane: Understood, that helps. And just secondly on this specialty side prescription trends. So, is it to do with the pent-up demand or that is in addition to pent-up demand, the overall recovery is very much visible?

Tushar Manudhane: On the specialty portfolio for the US or the development? So, you highlighted in the opening remarks about the prescription trend coming back to pre-COVID levels. So out of that, how much would be let's say, because if there is any pent-up demand, or this is more the new prescription is being done?

Abhay Gandhi: It's patients who were not reaching out to doctors coming back to the clinics gradually, and we're regaining share to where our pre-COVID levels of prescription there. So that's what I was talking about. I hope that answers your question.

Moderator: Thank you. The next question is from the line of Neha Manpuria from JPMorgan. Please go ahead.

Neha Manpuria: My first question is on specialty business. Now Levulan you said obviously was probably the most impacted along with Ilumya. Are you seeing, by when do you expect near normalization of trends in terms of patient portfolio? In your view, will this take a couple of quarters. And second is in on Ilumya itself. In your interaction with the doctors, what is the biggest selling point for Ilumya versus the other IL-23. We understand that IL-23 will gain share, but I don't know. What is the biggest selling point for the doctor prescribing Ilumya versus the other IL-23 drug?

Abhay Gandhi: Neha, you have asked two questions, let me respond to them sequentially. For me to be able to forecast when things will normalize is really something, I will not be able to do because if I see it in the US context, just a couple of days ago the death toll in the country has crossed 150,000. And even today we are seeing close to anywhere from 90,000 to 100,000 new detections every single day. In the past week or so, four important states have sort of once again reinforced their lockdowns. Florida, Texas, a little bit of Arizona, California, so these are major markets. So, these were some of the few markets were first to open but after seeing the spike in cases, they are going back to lockdown kind of a situation. So, while in some states, the situation is improving, in some states it has regressed. So, when things will normalize is very difficult to say.

Month-on-month, whether it is Ilumya or Levulan, I'm seeing an increase. But when it will reach pre-COVID levels is a tough question to ask, and I really wouldn't have an answer to that. On your second question, we have said this on different calls as well. The three major points we are talking to doctors, one is of course on the efficacy of Ilumya, the second is on the safety. And the third is on the durability of results and these three messages do resonate with doctors. And they are also able to see the product leading up to their expectation on these three fronts, therefore, in the face of COVID as well, many doctors even ask their patients to continue, not come back for Ilumya and to stay where you are because they knew that the results and the patient's clearance of skin would sustain. And when the patient is then able to come back to the doctor, the prescriptions of Ilumya has resumed.

Nimish Desai: So, is the durability of results, will that allow us to probably regain share faster than our peers?

Abhay Gandhi: We hope to. But also, do remember that ours is a medical benefit product and others are pharmacy benefit product. So just working on one aspect of a product attribute, alone will not help us to regain share. We must work on multiple fronts and make it a cohesive working unit to ensure that we improve our market share and gain faster than others and that's always the objective.

Neha Manpuria: Understood. Just to follow up on the R&D spend on specialty, that has stepped up quite a bit quarter-on-quarter, even though our total R&D has come off. As we look at our R&D pipeline for specialty, how should we look at the specialty R&D spend through the rest of the year. Is this level enough for us to take our programs through or should it increase further?

Dilip Shanghvi: So, first in today's situation, one of the biggest casualties has been the clinical trials. Because since the clinics were not operating, doctors were not putting patients on trial medication. So, we really don't know when the normal operations of the clinical studies will start. My sense is that with our continued investment on Ilumya as well as additional indication plus the recently licensed product from SPARC, for which also the Phase II studies will start shortly, the overall spend, if the clinical studies get into the normal rhythm, that spend will go up a little bit.

Moderator: Thank you. The next question is from the line of Sameer Baisiwala from Morgan Stanley. Please go ahead.

Sameer Baisiwala: Sir, what's the update on Halol remediation?

Dilip Shanghvi: So, we continue to update the agency about the remediation that we've done. And in my understanding, almost all the remediation would have been done or are likely to be done shortly. But the agency hasn't yet come out with any clearly defined guideline on how to audit a facility, which is currently on an OAI status. So, they are working on it is what I understand. But till the time there is clarity, we really don't know how the agency will look at it. Hopefully, they will come out with a way by which like what they are saying for regular product and for pre-approval inspections and regular audits, it can be based on the desk audit. They will find a way to complete this also based on the desk audit, but difficult to respond at this point.

Sameer Baisiwala: Okay, great thanks. And Abhay, this is for the derma portfolio, both for the specialty as well as for generic in the US Now whatever sales has been lost right now, the prescriptions so how do you see this going forward. Is it gone, or do you think this then comes back in some measure?

Abhay Gandhi: So, the situation is gradually evolving, So, we have had around 35-40% of the derma clinics opening till about last month, doesn't necessarily mean that all of them were willing to meet your reps and have normal kind of visit. But electives were also pushed into the background, so we were doing what was sort of important. And electives were still being put into the background and you're right. That did impact both the specialty as well as the generic part of the derma portfolio. There is improvement seen literally on a week-to-week basis, but it's not so rapid, that I can say that things will normalize in the next couple of weeks or in the quarter. So, it's a gradual process and as I was mentioning to Neha earlier on the call, some states are going back on their reopening plans and going back into a shutdown mode. So, it's an evolving situation here in the U.S.

Sameer Baisiwala: Okay. And just one final one from my side on Taro settlement on DOJ. Sir, given that the underlying sales was about $500 million that was cited, was it a bit of a pervasive practice in the company during that time period. And second is how do you think about the ongoing 44 state attorney general case on the same price fixing?

Dilip Shanghvi: Taro being a public company, beyond whatever that Taro has shared, I don't think we can share any further information. But at the same point of time, there is a structured process for all this DOJ settlement. So, we must remain in compliance with those settlements.

Moderator: Thank you. The next question is from the line of Nithya B.S. from Bernstein Research. Please go ahead.

Nithya Balasubramanian: My first question was on the India market. Are any of the savings related to efficient marketing or more efficient selling now that the doctors using digital tools, et cetera. Are any of these savings likely to outlast COVID, as you see normalcy come back, do you see any of the savings being sustained?

Kirti Ganorkar: I think is some of the savings would continue in second quarter. And then quarter three and four if things are normalized, then some of these savings will reduce substantially, when things will start coming back to normalization maybe in the third or fourth quarter.

Nithya Balasubramanian: Okay. So, you do not see anything, any fundamental changes in the way you do business in India. So, all the expenses that used to happen before are likely to come back once the market opens?

C. S. Muralidharan: Yes. So, what we believe is once things are normalized then all these expenses will come back. There will be some savings here and there, but that will not be very substantial.

Nithya Balasubramanian: Got it. My second question was again a related question on the DOJ probe on price fixing. So, beyond Taro, Sun has also been named in some of these things. So again, a question around what is the progress currently and what can we expect going forward?

Dilip Shanghvi: As we explained, the settlement is only for Taro and it does not include Sun. The products for Sun as well as Taro are also different. So as on today, there is no progress, that we can report beyond whatever that we have shared.

Moderator: Thank you. The next question is from the line of Anubhav Aggarwal from Credit Suisse. Please go ahead.

Anubhav Aggarwal: One question I had for Kirti for the India business. I just wanted to understand that if you look at the mix product marketing in terms of digital channels versus physical interaction, if you just provide us rough indication May versus July. What percentage will be digital, I'm just looking for a trend. I'm not looking for the exact number. Just looking at as things started opening, patients started visiting office, et cetera how digital marketing has started phasing out. So, May versus July as the trend?

Kirti Ganorkar: Yes. I will just start from April, since the lockdown started in March end. So, you can say like April almost there were no calls to the doctor. There was no physical call to the doctors in the month of April. In the month of May at least the first quarter also, there were no physical call to the doctors. But from the second half of the May, at least in a green zone area as they were defined at that point of time, we started working in the field. And in the June, most of our field force now are working in the field, except in a containment zone or wherever there are restrictions. So, if you see the transition, April was almost like I would say 100% digital where the medical reps or managers are calling the doctors. May is like 20% to 30% of the calls, which are like physical calls and when you come to June, then things have improved a lot. So, in June, you will see like almost close to 50% of the calls which we can go and meet with the doctors for a short period of time. So, this is how the progression is happening and in July there still we see some improvement, but not to the extent what I was expecting. We have a lot of challenges in terms of local lockdowns.

Anubhav Aggarwal: So physical interaction right now in July is 80%?

Kirti Ganorkar: It's slightly better than June but, and as the number of patients visiting to the doctors are very limited. Still, there is a big challenge and fear psychosis in the mind of patients.

Anubhav Aggarwal: Okay, that's helpful. My second question is just wanted clarity that personnel cost for us on a consolidated basis has gone up by 100 crores sequentially. So, is it, have we recruited more guys, that would have benefit us? So, is it just, what could explain this?

C. S. Muralidharan: This is Murali. The increase is attributable to several factors, increase in the field force in India and US, some component of exchange rate impact and actuarial valuation impact. So, these are certain components and drivers for this change.

Anubhav Aggarwal: So, this India sales force increase was already planned, it's just that people, the new decisions are not taken, because the same 10% increase that you talked about, it just started going in?

C. S. Muralidharan: Correct.

Moderator: Thank you. The next question is from the line of Damayanti Kerai from HSBC. Please go ahead.

Damayanti Kerai: My question is regarding the US generic business. So, if we see some further delay in Halol resolution, how do you see your US generic part evolving in next two to three years. And what is the pricing environment right now for your portfolio?

Abhay Gandhi: So, when I look at the opportunity that is available with current products and some of the products, which we have launched or are launching in the next few months, I'm pretty confident that there is still scope for us to do better in the overall Sun generic part of the business and that's what the team is working towards. The pricing situation, I have consistently maintained, is not improving from an industry perspective and we continue to face a challenging environment.

Damayanti Kerai: Okay. So challenging means most of your peers have mentioned about mid to high single digit kind of pricing erosion to continue. So, are you witnessing the same level of erosion?

Abhay Gandhi: It is very product specific. So, in an aggregate sense, maybe I would probably like to go along with the same kind of a number. But when I see some products, sometimes the drop can be so severe, it just moves the earth under you. But at an aggregate level, yes maybe you can take that kind of a number.

Damayanti Kerai: Sure. My second question is regarding Absorica. So, you had plans to move your patients from Absorica to Absorica LD formulation. So how has been the progress there?

Abhay Gandhi: It's very gradual, and the COVID situation is the primary contributing reason to that. So, the shift is very gradual. So, in the absence of proper promotion to the doctors, the loyal customers of the products stay with what they know, and that's the Absorica brand. So, some shift is happening, but not as fast as we would like, clearly.

Damayanti Kerai: Okay. So, any year-end target, like what percentage of patients you would like to move after seeing a disruption of COVID?

Abhay Gandhi: That would be a difficult question for me to answer now.

Moderator: Thank you. The next question is from the line of Vishal Manchanda from Nirmal Bang. Please go ahead.

Vishal Manchanda: Could you share a tax rate guidance for the year?

C. S. Muralidharan: We have always maintained our tax rates are to seen at annualized level. For last year FY20, our effective tax rate was about 16.4%. And we have guided already last year, that gradually it will inch up, so we'll maintain that position.

Vishal Manchanda: So, will this merger have any implications Sun Pharma Global FZE with you?

C. S. Muralidharan: No.

Vishal Manchanda: Okay, and just one more. One of the executive orders that Donald Trump has passed, talks about passing on the rebates to customers. The pharmacy benefit managers should basically pass on the rebates. So, does this have any favorable or unfavorable implication on your specialty revenue, especially Ilumya?

Abhay Gandhi: So, the fine print of the order and how exactly it will get implemented is still unknown. The whole industry and the associations are trying to work through it and trying to understand more. So as of now, it's very difficult to respond to that.

Moderator: Thank you. The next question is from the line of Krish Mehta from Enam Holdings. Please go ahead.

Krish Mehta: I had two questions. The first one is about, if you could share the net debt position for the consolidated and stand-alone statements and I'm guessing this will be ex-Taro?

C. S. Muralidharan: The net debt position at ex-Taro is about $850 million as of 30th June.

Krish Mehta: Okay. And the other question I had was if you could share.

C. S. Muralidharan: No, I stand corrected. The net debt position as of 30th June for ex-Taro is $451 million.

Krish Mehta: Okay, 451. And, I had another question about the working capital if you could share the accounts receivable, payable and inventory numbers for this quarter consolidated?

C. S. Muralidharan: Accounts receivable, payables in this quarter, we will let you know separately

Moderator: Thank you. The next question is from the line of Shyam Srinivasan from Goldman Sachs. Please go ahead.

Shyam Srinivasan: Just the first one is on the gross margins, it seems to have come up quite well and when we look at Taro, clearly Taro has declined. So, I'm just trying to see what has happened in the rest of the business from a gross margin perspective?

C. S. Muralidharan: Overall, we have also said in the readout that there have been efficiencies in management of operations, coupled with we have also managed our overall inventory management more efficiently. That includes the slow and non-moving related management of inventories. So, these are some of the factors that help us to improve overall margins.

Shyam Srinivasan: Got it. So Murali sir, is this sustainable do you think or when the mix kind of comes back to a normalized mix, this will be sustainable or not, that's the follow up?

C. S. Muralidharan: It's very difficult to answer. We need to wait for the mix of what's going to happen.

Shyam Srinivasan: My next question is on the API business. It has grown 20% Y-o-Y and the press release talks about using it more for captive purposes. But I'm just trying to understand from a trend to third party sales, is there something that you are observing in terms of qualitative color?

C. S. Muralidharan: We have been maintaining a robust position on the API business consistently. The philosophy is of course to leverage the vertical integration capability the company has, which helps us to speak to market. That's why we are saying that we will try and enhance more and more captive. At the same time, we are also focusing on whatever available on the third-party sales and we have consistently performed on the API in the third-party sales also.

Shyam Srinivasan: And last one is on the API localization efforts by the government. Is there any update, or are you looking at any specific drugs in that list for you to kind of localize?

Dilip Shanghvi: Yes. there are quite a few products in that list other than antibiotics that we are considering because we already are in that business. So, we are evaluating all options, but the idea would be to use this to become fully integrated in India.

Moderator: Thank you. We have Mr. Shanghvi reconnected. We take the next question from the line of Surya Patra from Philip Capital. Please go ahead.

Surya Patra: Two questions, one on the two products for COVID that you had mentioned. So how are you thinking whether just thinking for the domestic market or you're thinking as a kind of a global initiative through this. Any thought process on that and in terms of opportunity, how big and what that you are thinking about it, so if you say something on that front?

Dilip Shanghvi: We are currently doing the study in India, and these studies are being done with a view to meet the Indian regulatory requirement. All different countries have different regulatory requirements. Plus, we also must keep in perspective that we only have IP for AQCH and not for Nafamostat. So, depending on what is the opportunity and what kind of clinical outcome benefit we will get, we must then decide about launching the product outside of the country.

Surya Patra: Okay. My second question is sir about the specialty business. See, I believe in the previous quarter commentary, you had mentioned that most probably this year, FY21 is likely to see a kind of decline in terms of specialty spend. Last year, I believe on the promotional side that you are mentioning, so whether any progress that we have seen on that front that is one. And secondly, relating to the specialty only, see we have seen a sequential quarter-on-quarter run rate has come down by almost like 30, $40 million because of the COVID factor. And there is also a sequential decline in the branded business of our ROW emerging market as well as India. So, despite that, there is a kind of sequential improvement in the gross margin thing that is visible. So, whether it is coming from the sequential correction in the raw materials, and hence that would be sustainable?

Dilip Shanghvi: So, if we look at the reduction in the marketing spend some of this is planned and some of this is as response to the COVID because we couldn't spend the money. People couldn't travel we couldn't visit doctors. So, all those things. And as Kirti says and as even Abhay says, once post-COVID when things become normal we will evaluate which kind of expenses don't produce any meaningful additional benefit and we may relook at those expenses. Otherwise, most of the other expenses will continue to be normal.

Surya Patra: So, in fact I was trying to understand the specialty spend. So, I was believing that you had indicated this in this year possibly we'll see a slightly low kind of specialty spend compared to FY20. So, on that front, whether is there any difference that would change in the thought process?

Dilip Shanghvi: No, there's no change in thought process.

Abhay Gandhi: It was mentioned on the last call also, that one of the reasons why the spend may be a little lower than last year is because we have optimized the DTC spend on Ilumya. I should keep that apart and the rest of the spend is what we have planned for. I'm sure both for Kirti in India and for me in the U.S., going ahead the total money that we spend may not change. But having said that, within that the marketing mix of the promotional mix may change depending on what works with customers and what is required to be done in a COVID and a post-COVID environment.

Surya Patra: Okay. And on the gross margin front, if you can give me, if you can. Despite the branded business coming down and that there is a sequential decline in the specialty revenue, still there is a gross margin improvement. It is purely because of the saving or declining raw material prices or something else?

C. S. Muralidharan: So, this is Murali. The same question I responded, what I did share is that efficiency in manufacturing operations, coupled with management of inventories more efficiently which includes the management of slow and non-moving inventory related matters. So, these are the contributors for the improvement in material cost consumption.

Kirti Ganorkar: What I can add is also the product mix for India business has improved.

Moderator: The next question is from the line of Gaurav Hinduja from GEPL Capital. Please go ahead.

Gaurav Hinduja: So firstly, I wanted to know that in the US business, we are seeing some sort of pricing erosion as mentioned on the generic. So, from a long-term perspective, do you see any changes to our product mix sort of increasing on the branded portfolio to augur well for the margins. So that's my first question.

Abhay Gandhi: The key in the generic business is to have a wide product basket and if you see the number of new product filings that we have and we have been giving this on our earlier calls as well, we have a robust pipeline of products to be able to cater. And then of course the other thing which you do as part of running the business is there are products which we feel that the pricing is so low, that it actually is not worthwhile doing it. And we continually look at products and try and see whether we need to continue or prune them from the basket and keep them dormant.

Gaurav Hinduja: Okay. So, are we likely to see the current product mix sort of normalizing for the next couple of quarters going to the gross margin and the EBITDA margins targets come up? So how

Abhay Gandhi: I did not understand what you mean by product mix normalizing, I didn't understand what you mean by that?

Gaurav Hinduja: You mentioned that the gross margins have come up a little bit because of the product mix, in the earlier question. So, are we likely to see this on a recurring basis for the next couple of quarters or is this only due to the COVID led disruptions?

Abhay Gandhi: So, in generics pricing is something that you can be sure of today. And if there is a new RFP or a ROFER, things can change. So, to look at what the pricing for a product with a particular customer is today and to then give a forecast of how to look a year down the line becomes a very challenging task because it can change quickly.

Moderator: Thank you. The next question is from the line of Nimish Mehta from Research Delta Advisors. Please go ahead.

Nimish Mehta: Yes. The question is for you Abhay. It's basically, I'm trying to understand the profitability of specialty business. Directionally, whether it is higher or lower sequentially, given that there has been reduction in other marketing expenses, even for that business.

Abhay Gandhi: We are in the investment phase, so there is no profitability as such. Having said that, at the beginning of the last quarter itself when we were entering into the COVID phase and we mentioned this on the call also last time. We took very conscious decisions to cut down on what we thought were non-business critical expenses, the non-business critical hiring. So that has led to a conscious reduction of cost for the current quarter and depending how the situation evolves, we will either continue to maintain a tight control over the expenses that we have. Or we might sort of loosen the strings and start investing if the situation comes back to normal. So, it's a watch and respond situation rather than take a decision now and regret later.

Nimish Desai: Yes, understood. I'm sorry, I made use of the word profitable, but I just wanted to know whether the loss would have increased or decreased. If you can let me know, that will be great, vis-à-vis the last Q4 FY '20?

Abhay Gandhi: I haven't looked at that really. But the drop in this turnover, we have said, but I have not done that analysis personally and business-by-business anyway on the call we would not share the details anyway.

Nimish Mehta: Okay. The other thing I just wanted to know the API cost. It has, we have seen we have been seeing that it is increasing from a lot of products and there is a sense that it will the higher cost will continue. So, in view of that how do you see our input material cost changing and any view on the API cost also would be very helpful?

Dilip Shanghvi: I don't think we can look at the API cost as a whole. In some of the products, there is a clear increase. In some products, we also see reduction. So maybe a slight overall increase, difficult to take a longer-term view because of multiple dimensions.

Nimish Mehta: Understood. So as of now from whatever API pricing we are at today and if again it remains the same. We won't see much impact on our margin, is that a fair understanding?

Dilip Shanghvi: What you are not factoring is that we have different countries and different businesses. So, what is relevant for India business, maybe India business because its price controlled and so many other variables. There is a direct correlation with cost and that may go up because of the multiple products, which have gone up in terms of cost in China. Now at the same point of time, in some other businesses, the impact of cost is not so high. So difficult to give a very defined answer.

Moderator: Thank you. The next question is from the line of Anubhav Sahu from MC Research. Please go ahead.

Anubhav Sahu: A couple of questions. One, sir for the India business, could you please segregate what was the growth of chronic portfolio versus acute portfolio and how much of India sales is from chronic sales now, did we gain market share in the last quarter?

Kirti Ganorkar: Yes. Broadly, if you look at the IMS data or even for that matter AIOCD-AWACS data, 50% of our portfolio is our chronic portfolio and rest will be like a semi-chronic and acute. And, I just missed your second question. What was it?

Anubhav Sahu: Sir, did we have sir my first question was on the segregation of growth. In this quarter, what was the growth of chronic portfolio in India versus semi-chronic portfolio?

Kirti Ganorkar: Sure. So, like chronic portfolio has grown by 10%. And semi-chronic has grown negatively and some of the others like acute has even de-grown by 20-22%. So, the chronic business looks like a normal business, it continues to grow what it was pre-COVID period.

Anubhav Sahu: Okay. And sir particularly on the chronic portfolio, did we gain market share, or did we maintain market share, what was the situation?

Kirti Ganorkar: So, I can give you overall picture for India business and we can look at this from two perspectives, the way we can look at the data. So, if you can look at the IMS data for this quarter, April-June, then you will see that Sun Pharma as a whole business we have gained 0.5% market share. But at the same time if you look at AWACS-AIOCD data, then our market share is up by 0.1%. But more importantly is the market is not growing. Our market is showing negative growth in the first quarter both in AWACS as well as IMS. Against that, we have shown a 3% growth. So, we are going in the right direction to gain market share.

Anubhav Sahu: Got it, sir. And sir, I had a question for Shanghvi sir. So, wanted your thoughts on recent executive orders by US President on the pharma sector. I know its earlier days and fine prints is awaited, but the way debate has shifted to the overhaul of price negotiation process. Any early comments on that, how should we position for things, the way things are changing, will it lead to a potentially increasing pricing pressure for the specialty portfolio or do you think there is a case for a better market access?

Dilip Shanghvi: I hope we have clarity because it is necessary for us to get it for making investment decisions. But I don't think there is clarity. Now my own sense is that if I simply look at stock prices of all the large pharma companies, there is no major impact post that executive order. So, I don't think that people are expecting any significant impact. But, it's good to have clarity as Abhay says we are looking at details and understanding the fine print. And we are not even sure whether this will be challenged or with all the changes we've made whether they are within the presidential authority. So, all those things, people will analyze and come back with greater clarity.

Anubhav Sahu: Got it, sir. Sir final one, is on specialty business side do we see a situation of breakeven like fiscal at the EBITDA level. Or do we have any target in mind for the breakeven segment?

Dilip Shanghvi: We should not look at specialty business alone. We should look at product-by-product. And we will start breaking even on some of the products from next year.

Moderator: Thank you. We'll be able to take one last question. We take the last question from the line of Anubhav Aggarwal from Credit Suisse. Please go ahead.

Anubhav Aggarwal: I just have one question. I just wanted to understand, get a general understanding of this price litigation case in the US just in terms of, if I look at the parties who are involved, one is department of justice, second is state and third is the commercial insurance. And my question was more from the commercial insurance perspective. Most of the cases investigation we have seen so far are from the state attorney generals and department of justice separately investigating, in your experience, how does commercial insurance do in this case. Generally, do they go with the judgment or whatever decide in the state attorney general cases, or they have separate cases. What's the process in general?

Dilip Shanghvi: The biggest challenge in all of this is that very few of this go into litigation and final judgment. Most of them get settled out of court. So, ultimately it will be a function of how that negotiation will go and what gets settled. And I'm not responding to your specific query. I'm giving you a general comment. In very few cases like let's say, Esomeprazole litigation that we had for reverse payment. It went all the way to litigation, and we got a favorable judgment. But like that, very few companies go up to the end. So generally, it gets settled. And how that gets settled is all over. So difficult to predict.

Anubhav Aggarwal: Sir one query on that. When we look some ex Taro, like some of the drugs where we had case against state attorney generals. So, when we look at the commercial insurance cases there for Sun ex-Taro, and apparently, I have not looked at that in detail. But have you've been litigated by multiple commercial insurance companies over there?

Dilip Shanghvi: There is a litigation ongoing by many companies. But ultimately it will depend on the strength of the litigation, the size of the business and all these issues. And the evidence they have or the burden they, ultimately there is a certain amount of burden of proof. It's difficult to respond, because all plaintiffs and litigants would have different arguments and all companies also will have a different strength of their case.

Moderator: Thank you very much. We'll take that as the last question. I would now like to hand the conference back to Mr. Nimish Desai for closing comments.

Nimish Desai: So, thank you everybody for joining this call. If you have any questions that have remained unanswered, do send them across and we'll get them answered. Thank you and have a good day.

Moderator: Thank you very much. On behalf of Sun Pharmaceuticals Industries Limited, that concludes this conference. Thank you for joining us. Ladies and gentlemen, you may now disconnect your lines.