Suven Life Sciences Limited

Q2 FY16 Earnings Conference Call Transcript
November 16, 2015

Moderator Ladies and gentlemen, good day and welcome to Suven Life Sciences Limited Q2 FY16 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 touch tone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Gavin Desa of CDR India. Thank you and over to you sir.

Gavin Desa: Thank you. Good afternoon and thank you all for joining us on this call to discuss the financial results of Suven Life Sciences Ltd. for the quarter and half year ended September 30th 2015. We have with us, Mr. Venkat Jasti, the Chairman and CEO and Mr. Venkatraman Sunder-VP Corporate Affairs. Before we begin, I would like to state that some of the statements made in today's discussion maybe forward looking in nature and may involve risks and uncertainties. Documents relating to the company's financial performance have already been mailed to you. I now invite Mr. Jasti to share some perspective on the performance over the quarter and the half year and his outlook for the year ahead. Over to you sir.

Venkat Jasti: Thank you Gavin and good afternoon everyone. Regarding the 2nd quarter earnings' call, as we have given you the guidance for the whole year last time, there are no real positive surprises to give you as you could see from the results. Even though the quarter on quarter, the growth in revenue is up by 15.5%, growth in PAT is up by 22%, growth in EBITDA is up by 21.27%. While for the same half year ended last year versus this year, the growth in revenue is down by 19%, PAT is down by 24%, EBITDA is down by 29%. So, as I said earlier, this year will be status quo year and the 3rd quarter also looks similar. Hope to achieve the same as 2nd quarter and hopefully the 4th quarter; there are some indications that new business will come in and therewith we should see some growth happening from that time onwards. And with respect to the pipeline, Suven 502 is progressing well and we are in the process of recruiting patients after the meeting with the investigators; investigators meeting was done recently and it will take time as you know, we have about 537 patients to be enrolled, all in USA, roughly it will continue, for 18-24 months. So, middle of 2017, there will be the possible readout of the data.

With respect to G-3031, we have finished Phase-1and we are getting the final document from the CRO and also this 3031 will have now to undergo the GLP long term toxicological studies, in order for us to prepare thisPhase-2 which will be some time in 2017. And as far as D-4010 is concerned, the Phase-1 is undergoing now and single ascending dose is already completed and we will be starting the multiple ascending dose in the 1st quarter and it will run until July or so. With SUVN-911, we are finishing the GLP toxs and we will be preparing the documents for IND for the

Phase-1submission, sometime in the second half of 2016.These are the various activities that are going on in the innovational side. So, I think it is better for me stop at this time and ask you to throw some questions, so I can answer you. Thank you.

Moderator: Thank you very much. We will now begin the question and answer session. Our first question is from the line Ashish Thakkar from Amsec. Please go ahead.

Ashish Thakkar: Sir first question would be on the Phase-2 trials, last time you had indicated that the trials would commence in October but we are yet to recruit the patients, so just wanted to understand, we are looking to recruit around 500+ patients, so approximately what time it would take for the trials to start?

Venkat Jasti: Anyday, see the way towards is, from the first time patients comes and sees the doctor after screening and testing, it will take about 45 days before they can start the first dosage. So, it is not that it is not happening because dosing is not happening but recruitment is going on, screening is going on, tests are going on, the inclusion-exclusion is being taken care of, IRB permissions are coming and everything is going on. I think it can be any day because some of these things which we have started way back in October, they will be maturing any day for the patients to be enrolled as a patient with our medications, everything is ready and all the doctors are trained and ready; it is only a matter of time because this is a procedural thing, that needs to be taken into consideration.

Ashish Thakkar: Do you by any chance anticipate a delay in the enrollment of the patients and do you see it going beyond December?

Venkat Jasti: No, I think, we may be miscalculating it. It will not happen in one month, the total enrollment will be happening over a period of 12 months; 1 year, after that it will be about 7 months, minimum to have the closure after the last patient came, which will be 7 months later than the close of these data log will happen. So, it is not going to be happening in one month, this is a long and difficult study in the sense because people are already under medications and you need to have taken care of the inclusion, exclusion criteria's, always it is a minimum 1 year before and being a special protocol we have, we may expect that to be little bit better, maybe in 10 month but only time will tell.

Ashish Thakkar: Sir second question would be on, since we would also be doing our 3031 and 4010 trials, along with the Phase-2 trials for this molecule, could you help us understand how the R&D would change going forward because first half we had done around Rs. 60 crore in R&D, so could you help us over the next two years how the R&D would shape up?

Venkat Jasti: I think now maybe whether you have noticed or not, the R&D will remain same as in the same range but the developmental costs, it is a different thing, it is not an R&D, it is a clinical development, so that it is going to be done in the subsidiary which we have created already in USA which we have intimated to you through a press release and it will be onto that account and it will not be on the standalone account, it will be year on year basis and then there will be consolidation in the annual report but it will not be on the main standalone.

Venkatraman Sunder: Ashish to answer your question also; it is not Rs. 60 crore in the first 6 months, first 6 months it is only Rs. 31 crore that is what we have spent that is one small correction I am trying to make it.

Ashish Thakkar: Sir you are saying in the quarterly results it will not be reflected, but it will be reflected on a full year basis when you consol the numbers?

Venkatraman Sunder: Yes.

Ashish Thakkar: Sir my second question would be on the repeat orders that we were supposed to get from our clients. You said that 4th quarter FY16 there are possibilities of these orders flowing in, I just wanted to understand what could be the frequency of these orders flowing in on a half yearly basis or every quarter, if that is possible?

Venkat Jasti: See they have given an indication but I think they will know by the end of year that is why I was saying December before the holidays, they will have the procurement planning done, then only we will come to know. Most likely it will be thrice in a year they will be taking, depending on the quantity would differ anyway but it will be usually twice in a year.

Moderator: Thank you. Next question is from the line of Sai Prabhakar from Karvy Stock Broking. Please go ahead.

Sai Prabhakar: In continuation of the R&D expense, since 502 has entered the cost intensive phase and we have couple of other programs in the R&D stages, so are you confident of the research expenses, even standalone or consol; we will have to do the expenses, so do you have scheduled the expenses and the financing ? I was just asking about if our operations will be able to sustain the R&D expenses?

Venkatraman Sunder: Yes.

Sai Prabhakar: Since we have one advanced program and couple of others in the IND stages?

Venkatraman Sunder: That is correct, the regular INDs will be spent as explained by Mr. Jasti, up to Phase-1 studies, the current R&D guidance we have given this year of up to Rs. 55-60 crore will be spent, that is adequate enough. The clinical development will be a separate one which will be incurred through Suven Inc., which is a company created outside India which is in US and all the expenses will be through that company.

Sai Prabhakar: But we will be routing it through Suven Incorporation that will be only the mandate…..

Venkat Jasti: It is the only one subsidiary as of now and as you know we have taken permission from the Board to invest up to $25 million and after that it is likely that partners can come in if not today, 6 months from now. That is the whole purpose of creating this outside the country. And also we need to develop a management team which can take up not only clinical development but also in business development activities for future requirements. So, yes as of now, we have enough money for these 2 compounds. As you know we have taken QIP and the revenues generated and accrued in the next 2 years will be used for the 2nd compound in case needed but we are hoping that some monetization may happen after the 502 finishes, 2017. So, I do not see any problem either from the regular R&D side or even on the developmental side.

Sai Prabhakar: So, like we had a bulk, strong sale in Q1 this year, similarly Q4 probably you see the repeat order coming in?

Venkat Jasti: Yes.

Sai Prabhakar: And similarly, are we looking at something we did similar to A&D, Malathion, any other coming up in that?

Venkat Jasti: As of now not really, because it takes time because only when we get into the market I think we expect that sometime in the fag end of 2016, if not 2017 for sure, couple of compounds, couple of products.

Moderator: Thank you. Our next question is from the line of Veena Patel from I-Wealth Management. Please go ahead.

Veena Patel: Sir I wanted to know the revenue from the Specialty Chemicals segment in the first half?

Venkatraman Sunder: Yes, the first half revenue from the Specialty Chemicals for 1st quarter is about Rs. 37 crore, 2nd quarter is, Rs. 49 crore.

Veena Patel: So, that will be total around Rs. 86 crore, so which was what in the first half of FY15?

Venkatraman Sunder: The first half FY15 was it was close to little above Rs. 104 crore.

Veena Patel: Sir, can you just give us a breakup of the projects under the different phases, Phase-1, Phase-2 and phase 3 for the first half?

Venkatraman Sunder: There are about 58 projects in Phase-1, 54 projects in Phase-2, 1 in phase 3, apart from the 3 commercial launch, which is the separate prelaunch, so that will come in commercial.

Veena Patel: And sir in the press release you have mentioned that you have commenced the operations in the Vizag facility, so like currently what are we manufacturing over there?

Venkat Jasti: As you know, one of the Specialty Chemicals we are making in 3 different plants and the purpose of creating this facility is mainly to take care all in one place, so in Vizag the Specialty Chemicals has started operations and first commercial shipment has happened last quarter.

Veena Patel: So, as of now you have been manufacturing only 1 Specialty Chemical, which you have been manufacturing..

Venkat Jasti: See as of today, it is one Specialty Chemical but it will be more into other multipurpose products in a year and half time.

Veena Patel: Sir are we seeking some kind of an customer approval to manufacture any products that we have in the pipeline in the Specialty Chemical division to get them manufactured from Vizag?

Venkat Jasti: There is no customer approval, it will be a validation, whenever you change a plant or even in the same plant you change a reactor, you need to get it. You need to get some 4 batches validated, get it authorized and then it is okay.

Veena Patel: Sir you just mentioned about a subsidiary being created and it is getting operational from October 2015, so what will be the nature of this subsidiary?

Venkat Jasti: The nature of this subsidiary is for the clinical development of our in-house molecules initially and to develop a management team separate from the Suven main team, to take care of the developmental activities and business developmental activities of its clinical compounds because it needs a different mindset and different skill sets and at the same time to invite the partners there in the process and also to enlighten some compounds eventually and which we can develop it further for the co-development, mainly a developmental company.

Veena Patel: Sir you just mentioned to the earlier participant that whatever would be the expenses because you are again bifurcating the research expenses from the developmental cost that would get reflected in the subsidiary, so I was not able to get what was the meaning of that?

Venkatraman Sunder: There are two aspects, one is that the regular cost what we have been incurring in Suven up to Phase-1will continue, which we have given guidance about this year of about Rs. 55-60 crore, of which we have already spent Rs. 31 crore. What we are talking about is the SUVN-502 kind of compounds where you know Phase-2, which is the clinical development; that expenditure will go into that subsidiary because it will be routed through Suven, Inc; there is an investment from Suven Life Sciences, about $25 million into that company which is Suven Inc. And all the expenditure over a period of next 1.5-2 years for SUVN-502 will be incurred from that company.

Veena Patel: Okay, so that will get reflected in the subsidiary and towards the year end it will be reflected in the consolidated basis?

Venkatraman Sunder: That is correct that is what Mr. Jasti was explaining.

Veena Patel: Okay and we are still maintaining the guidance of Rs. 60 odd crore on an annual basis for our regular expenses?

Venkatraman Sunder: That is right.

Moderator: Thank you. Our next question is from the line of Charulata Gidani from Dalal and Broacha. Please go ahead.

Charulata Gidani: My question pertains to Other Income, what is the Other Income in Q2?

Venkatraman Sunder: Other Income in Q2 which is about Rs. 578 lacs.

Charulata Gidani: Right, it is higher substantially than the other quarters, is there any additional income that has come in?

Venkatraman Sunder: No, the majority of this income is like income from the deposits, like we have raised a QIP last year, the earning of the investment from that has been classified as Other Income.

Charulata Gidani: And my second question is relating to the developmental expenses, what will be the amount that you estimate towards developmental expenses by the subsidiary?

Venkat Jasti: First 502 will be to the tune of 22-25 millions in a two year period. As of now that is the only program in clinical development.

Charulata Gidani: And why is the depreciation higher in the quarter?

Venkatraman Sunder: That is because of the capitalization of the facility at Vizag, the commercialization has happened only recently in the last quarter and as the capitalization has happened in Vizag now, the depreciation effect of the same has been taken into consideration.

Charulata Gidani: Okay, so going forward, you estimate depreciation at this level?

Venkatraman Sunder: Yes, on similar lines.

Moderator: Thank you. We have a question from the line of Dheeresh Pathak from Goldman Sachs. Please go ahead.

Dheeresh Pathak: The manufacturing CRAMS revenues; ex of specialty chemicals, ex of pre-launch supplies, that has de-grown in the first half, so can you just explain that de-growth?

Venkatraman Sunder: The manufacturing expenses did not de-grow, I think you are trying to compare with the last year, right?

Dheeresh Pathak: Yes.

Venkatraman Sunder: From Rs. 130 crore to now Rs. 104 crore; because of the product mix changes, sometimes the material cost will be higher or lower based on changes in product mix. particularly in this quarter not only we may not have the high cost material consumedin the process actually. That is the reason, there is a reduction.

Dheeresh Pathak: Second half FY15 was very strong for manufacturing CRAMS, ex of Specialty chemicals and ex prelaunch; is it on a full year basis ?

Venkatraman Sunder: There is a reduction of almost about Rs. 69 crore when you really look at that for 6 months because if you really see the overall volume also was lesser, compared to what it was, it is always in relation to the sales. The sale of last year 6 months was Rs. 281 crore as against the current one is about Rs. 217 crore for 6 months actually. So it is in prorata more or less aligned with that.

Dheeresh Pathak: I just want to clarify that FY15 as per the numbers we have; the manufacturing CRAMS business was about $50 million for the full year, now second half of FY15 was very strong, first half of FY16 has seen a de-growth in dollar terms; can you just help us get some understanding for the full year numbers for this revenue stream for FY16?

Venkat Jasti: Yes, we have given a guidance last year, we would like to achieve the same as last year's target because as I said, it is a status-quo year and to achieve that it is a task for us but as of now, it looks like around Rs. 500 crore for sure but we are trying to achieve those Rs. 520 crore which we have done last year.

Dheeresh Pathak: In which you also include specialty chemicals, right?

Venkat Jasti: Yes, all inclusive.

Dheeresh Pathak: But we look at it differently; we strip out the specialty chemicals separately, so can you just guide in terms of the 2 separate revenue streams; specialty chemicals and manufacturing?

Venkatraman Sunder: You know, we are likely to achieve around close to $85 million for the whole year as expected and of which this specialty chemicals is likely to be around $30 million.

Venkat Jasti: Actually Specialty chemicals this year will be little bit more than last year and the CRAMS side because of one-offs are not there, it will be less than what was last year.

Dheeresh Pathak: And in this subsidiary, the whole year on subsidiary you would move, right now you just have 502 Phase-II clinical trials in that subsidiary ..

Venkatraman Sunder: Whenever a compound comes into the Phase II level, then only it will go into this developmental aspect, until that time the expense are taken in the main company only, up to Phase I.

Dheeresh Pathak: Would you create separate subsidiaries for each molecule, I mean I am just trying to get the intent?

Venkatraman Sunder: No, it can be. As of now, it is only one molecule, tomorrow somebody wants to come and become a partner into this molecule; maybe, 50-50 also is possible. So, when second molecule comes, then we will think about it, by that time we have enough time because second molecule will go into the clinics sometime in2017, at that time 502 will be out. So these are various possibilities; it can be a single thing or it can be a combination. As time goes, we may have partners coming in and depending on their requirements, we will consider what is feasible.

Dheeresh Pathak: Can you just refresh cumulatively, how much have we spent in 502 so far and how much have we spent in Phase II, how much have we spent in the initial Phase II round that we are working on?

Venkatraman Sunder: We are in the very early stages, the amounts will be strengthened in the next 2 months for yearly money also. And right now, it is $1 million which we have transferred, out of the $25 million investment we have proposed to do it.

Venkat Jasti: The trial has just begun.

Venkatraman Sunder: As it moves, then we get expenses to think around.

Dheeresh Pathak: And cumulatively, so far how much have we spent in this molecule?

Venkat Jasti: On this molecule, it is about $20 million to $25 million depending upon what the rate is.

Moderator: Thank you. Our next question is from the line of Ashish Thakkar from Amsec. Please go ahead.

Ashish Thakkar: Sir, on the recent Vizag facility that we have commercialized, 2 years down the line where do you see this facility, you know at what level do you see this facility working at, at what capacity levels this facility working at?

Venkatraman Sunder: Let me tell you, the first one; the capacity is being utilized fully, whatever the block we have done but because of the total infrastructure we have developed, the cost is more but when we do the second block onwards, it will be not this much cost but anyway by the time 2017 comes, we should have 4 or 5 products, we will be working on that product from Vizag; not only the specialty chemicals because that will be multipurpose plant.

Ashish Thakkar: So these 4 to 5 molecules would be additional molecules or they would be existing ones?

Venkatraman Sunder: Now, it will be existing ones, when we go into the next level. Now if we are doing in the R&D scale say 100 kilos, when it comes to ton levels, then it will go there, scale up.

Ashish Thakkar: So in that case, since we would be freeing up some capacities that are older facilities, is there any particular reason?

VenkatJasti: It is not like that, it is never like that because always we are using as a multipurpose, capacity is freed up when we completely take over this specialty chemicals into this unit. Right now, still we are doing it another unit also because we do not want to just change everything in one go but being multipurpose there will not be any additional capacities created because we are always creating additional capacities because number of projects are also going up and hopefully the number of successes also will go up, so that we can build new capacity there but the cost will not be that much.

Ashish Thakkar: Okay, and the repeat orders; this would be executed from the Vizag facility?

VenkatJasti: Not the repeat orders, when the R&D thing goes into the piloting or into the commercial, then only it will go there.

Venkat Jasti: The repeat order could be from the existing facility itself.

Ashish Thakkar: I am talking about the ones that we are supposed to receive by fourth quarter.

VenkatJasti: It will be from the existing only but anyway the new plant, the new block will take at least one year minimum to come into operations.

Ashish Thakkar: So to that extent, could you give us guidance on the CAPEX, how much we are planning to do?

VenkatJasti: Next CAPEX will be about Rs. 50 crore for one block.

Ashish Thakkar: Total Rs. 50 crore you are saying?

VenkatJasti: Yes, for one block, not total. Every year we will be doing something, not one go.

Ashish Thakkar: And tax guidance, if you would like to give because first half we have done lower than what we were guiding earlier?

Venkat Jasti: The thing is that; the first half tax has come down basically because of the capitalization effect, what has happened at Vizag. Last year, if you really see actually the total tax is close to about 29%, now it has come down to 21% because of the depreciation affect, the capitalization that has happened.

Ashish Thakkar: So for this FY16, we should assume 20%, 24% kind of a range?

Venkatraman Sunder: Yes.

Ashish Thakkar: And going ahead, anything you would like to guide?

Venkatraman Sunder: It will be more or less in the same range.

Moderator: Thank you. Next question is from the line of Veena Patel from I-Wealth Management. Please go ahead.

Veena Patel: Sir to earlier participant you just mentioned that the CAPEX has been capitalized, so whatever the CAPEX that we had done for Vizag, is entirely capitalized or it is from the one box related CAPEX?

Venkatraman Sunder: That is whatever incurred up till now, is totally capitalized.

Veena Patel: How much was budgeted and how much has been incurred?

Venkatraman Sunder: Budgeted was Rs. 120 crore and what was incurred was Rs. 132 crore.

Veena Patel: So how much has been spent?

Venkatraman Sunder: Rs. 132 crore; entire thing has been spent, it is capitalized, it is commissioned.

Veena Patel: Apart from this, what would be our routine CAPEX for the existing facilities?

Venkatraman Sunder: Existing facility, not much, it will be mainly maintenance CAPEX.

Venkat Jasti: Our yearly, roughly it will be Rs. 40 crores to Rs. 45 crores on an average you see, recurring CAPEX for the replacement of the balancing equipment or that is what we do.

Veena Patel: Okay, this is the maintenance CAPEX.

Venkat Jasti: Yes, that is right.

Veena Patel: And Sir, coming on to the Vizag facility, what kind of peak revenues can it achieve?

Venkat Jasti: Peak revenues it can achieve in 4 years' time around Rs. 500 crore; that is what we are targeting.

Moderator: Thank you. Our next question is from the line of Dheeresh Pathak from Goldman Sachs. Please go ahead.

Dheeresh Pathak: Just in continuation of the last question; how much has been spent on Vizag facility, what is the CAPEX?

Venkat Jasti: Rs. 132 crore.

Dheeresh Pathak: And this is commercial in part or this is yet to be commercial?

Venkat Jasti: See, let me explain to everybody. When you start a brand new facility with 21 acres, you have to create the total infrastructure. Even though we created only one building for the one block for one product but the infrastructure has to be total; like the administrative facilities, integrities, roads and the hazards material, the environmental facilities and all other things. The cost of that is roughly 55% to 60% as total cost goes to the common infrastructure which is useful for the future as a matter of fact Rs. 55 crore to Rs. 60 crore only for the slot that is right. When I build a new block, next year it will be in the same range, it will not be more than that. Then there is not much infrastructure cost for the common facility, only the building for the manufacturing only will be built.

Dheeresh Pathak: Okay, this one block that is commercial, this is for specialty chemicals, right?

Venkat Jasti: That is right, as of today.

Dheeresh Pathak: But I think sometime back you had said that this block can do $15 million, so you know specialty chemicals can on a steady state do $20 million plus v$15 million;

$35 million, so this $35 million we should do next year because this year run rate is lower?

Venkat Jasti: I mean, yes we can create up to $25 million easily in these blocks.

Dheeresh Pathak: And when you say Rs. 500 crore of revenue potential, this would be assuming that you will add more blocks, right?

Venkat Jasti: That is right, in 4 years' time, yes.

Dheeresh Pathak: And the FY14 had these pre-launch supplies and then '15 had just for one quarter, then I think it was expected that '16 would have pre-launch supplies atabout $10 million to $11 million run rate annually, but that has not come yet, can you just explain what is happening; with the end product in terms of market share, is it seeing some issues or what is the reason?

Venkat Jasti: No actually, there are no issues. It is progressing well but their calculation of the quantum that is required I think there was some mistake and they bought more quantities than required, that is why this delay is happening on the main product. The other products have been small in nature and they have enough stocks until the first quarter.

Dheeresh Pathak: What is the annualized run rate of the product which was supposed to be main out of these 3 products?

Venkat Jasti: About $15 million.

Dheeresh Pathak: Not for you, I am saying, for your client; the final product has it reached an annual run rate close to $500 million.

Venkat Jasti: In the peak, when it goes to the peak, is you are talking is about $800 million to $1 billion.

Dheeresh Pathak: No not peak, I am asking as of now, the last month's..

Venkat Jasti: That is not in our purview, because they will not tell us and as their results comes out then only people will know about it and the only guidance they gave in the stock market, so that is all we know they are saying at the peak it will come to $800 million to $1 billion but as you know nowadays, the cost of the API is miniscule compared to the selling cost unlike good olden days where you can estimate to 5% to 10% of the total sale will be our API cost but now, it is not like that. It is 1% to 2% only.

Dheeresh Pathak: You would know the product, so in the IMS numbers that come out monthly, is it not possible to know in that therapeutical segment its performance

Venkat Jasti: Yes, I know what it is but I cannot tell you because I am not allowed to tell.

Dheeresh Pathak: But in the estimate that they mentioned v/s what you are seeing right now, is it on track? Is it better, is it worse?

Venkat Jasti: No, it is in the same range.

Dheeresh Pathak: And when can it hit that peak revenues of $1 billion?

Venkat Jasti: Peak; that is third or fourth year.

Dheeresh Pathak: From now.

Venkat Jasti: No, from the date of last year, sometimes 2017, 2018.

Moderator: Thank you. As there are no further questions, I would now like to hand the floor over to the management for closing comments, over to you Sir.

Venkat Jasti: Thank you everyone for tuning in and sorry I could not give you a real positive surprise but at least this year I am trying to maintain the same and the things are looking nice and hopefully it will come sooner than later. And in terms of our clinical development also, is going on very well, happened 3 molecules in the clinical development, fourth one also; 911 also will be going sometime in 2016. So our company will have 4 clinical development molecules in the 5 plants which is value accretion and that gives us a much more partnering opportunities hopefully sooner than later. Thank you again for listening to us and catch up with you next time.

Moderator: Thank you very much. On behalf of Suven Life Sciences; that concludes this conference call. Thank you for joining us and you may now disconnect your lines.