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February 17, 2023

To  
**BSE Limited**  
Phiroze Jeejeebhoy Towers, 25<sup>th</sup> Floor,  
Dalal Street, Mumbai - 400 001

**The National Stock Exchange of India Ltd**  
Exchange Plaza,  
Bandra Kurla Complex  
Bandra (E), Mumbai - 400 001

**Scrip Code: 524558**

**Scrip Code: NEULANLAB; Series: EQ**

Dear Sir/Madam,

**Sub: Transcript of the Earnings call conducted on February 14, 2023**

Pursuant to Regulation 30 of Securities and Exchange Board of India (Listing Obligations and Disclosure Requirements) Regulations, 2015, please find enclosed the transcript of the Earnings call for the quarter and nine months ended December 31, 2022, conducted on February 14, 2023. Also please note that this transcript of the call has been uploaded on our website.

The weblink to access it:

<https://www.neulandlabs.com/investors/investor-updates/announcements/>

This is for your information and records.

Thanking you,

Yours faithfully,  
For **Neuland Laboratories Limited**

**Sarada Bhamidipati**  
Company Secretary

*Encl: As above*



“Neuland Laboratories Limited  
Q3 FY2023 Earnings Conference Call”

February 14, 2023



**ANALYST: MR. RAVI UDESHI – ERNST & YOUNG**

**MANAGEMENT: MR. SUCHETH DAVULURI – VICE CHAIRMAN & CEO -  
NEULAND LABORATORIES LIMITED  
MR. SAHARSH DAVULURI - VICE CHAIRMAN & MD -  
NEULAND LABORATORIES LIMITED  
MR. ABHIJIT MAJUMDAR – CFO - NEULAND  
LABORATORIES LIMITED  
MR. SAJEEV EMMANUEL MEDIKONDA – HEAD -  
CORPORATE PLANNING AND STRATEGY - NEULAND  
LABORATORIES LIMITED**



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**Moderator:** Ladies and gentlemen, good day and welcome to Neuland Laboratories Limited Q3 FY2023 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. Please note that this conference is being recorded. I now hand the conference over to Mr. Ravi Udeshi from Ernst and Young. Thank you and over to you.

**Ravi Udeshi:** Thank you Yashashree. Good evening friends we welcome you to the Q3 FY2023 Earnings Call of Neuland Laboratories Limited. To take us through the results and to answer your question, we have with us the top management from Neuland represented by Mr. Sucheth Davuluri – Vice Chairman and CEO; Mr. Saharsh Davuluri – Vice Chairman and Managing Director; Mr. Abhijit Majumdar – CFO; and Mr. Sajeev Emmanuel Medikonda – Head, Corporate Planning and Strategy.

We will start the call with a brief overview of the financials by Abhijit Majumdar and then Saharsh will give you a broad highlight of the business trends, and what he is observing in the market and post this we will open it up for the Q&A session. As usual, the standard safe harbor clause applies as we start the call. With that said, I now hand over the floor to Abhijit. Over to you Abhijit.

**Abhijit Majumdar:** Thank you very much Ravi and a very good evening to all friends and warm welcome to you all for joining our Q3 FY2023 earnings call. I think you must have seen the presentation, which Ravi mentioned and it is put up on our website and has been uploaded on the BSE and NSE websites. As always any comments on the content of this presentation, which we have sent will be highly appreciated, and we will do our best to give out additional data points, which will help you to understand our business better.

I will briefly talk about financials now. The total income for this quarter is Rs. 270.2 Crores against Rs. 238.4 Crores in Q3 at FY2022. This was largely driven by a growth in our GDS business. Our EBITDA for the quarter stands at Rs. 54.9 Crores with an EBITDA margin of 20.3% an increase of 6% or 600 basis points over the previous year. The increase in EBITDA margin has been led by a revenue mix shift towards high margin products. While we have continued to witness volatility in input prices; however in line with Q2 FY2023 we continue to experience some easing on a relative basis. Our focus on execution excellence and cost has enabled us to minimize the cost impact from raw material increases facing our industry. At the same time we have seen a sequential drop in revenue by 8% when compared to Q2



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FY2023 and an EBITDA margin drop of 330 bps due to a slight change in business mix as well as lower revenues impacting our operating leverage. I would request you to measure our performance over a one year time horizon as our EBITDA margins will fluctuate on a quarter-on-quarter basis.

Coming to specifics. Our gross margin was 55.2% in Q3FY2023 compared to 49.2% in Q3 FY2022 and 56.2% in Q2 FY2023. Profit after tax was at Rs. 30.4 Crores as compared to Rs. 12.7 Crores last year. This quarter's EPS is at Rs.23.7 per share.

On a nine month basis, the total income is Rs. 785.8 Crores, an increase of 12.3% over the prior period of last year. The EBITDA increased by 46.1% to Rs. 153.3 Crores as against Rs. 104.9 Crores in the 9M FY2022. The EBITDA margins has come in at 19.5% compared to 15% for 9M FY2022 on account of our stated shift to higher margin products. We generated a free cash flow of Rs. 161 Crores in the 9M FY2023 and net debt position stands reduced to Rs. 72 Crores versus Rs.212 Crores as at the end of March 2022. We continue to invest in upgrading our facilities and have invested Rs.50.9 Crores in Capex during this period. Our net gearing ratio stands at 0.1x as on December 2023.

With that I would like to hand over the call to Saharsh for his remarks and once again thank you very much.

**Saharsh Davuluri:**

Hi, good evening everyone. Thank you Abhijit. I think in terms of the quarter itself I will add a few comments on top of what Abhijit has already said and then we can open it up for Q&A.

The quarter in many ways is a fairly decent representation of the direction that we have been steering our business. While there is uncertainty surrounding raw material prices, we are starting to see some stability. In my opinion this quarter continues to indicate that our strategy of focusing on the GDS specialty and the CMS business is shaping up well. The growth driven by both the specialty and the commercial products in the CMS business has meant that we have healthy gross margins flowing through to the rest of the P&L. In the specialty segments products like Apixaban and Ezetimibe have contributed significantly and we are excited about these products. With regards to the CMS business, I would like to highlight the significant jump in revenues from commercial products. You may recall that over the past few years we had stressed that our molecules will gradually transition from development to commercial and this quarter marks such a transition. We expect further commercialization to happen over the medium to long-term. The contribution of the CMS business has been a significant driver of the improved EBITDA margins that we have witnessed in the last two quarters. We



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continue to see some early-stage projects get added to the business this quarter, and we are continuing to see an increased traction from new customers as our ability to execute complex late stage projects that distinguishes us and makes us a highly regarded CDMO.

In terms of the overall business, we are witnessing a shift towards high margin business which has been our stated goal. But we continue to remain slightly cautious about how the business or even product mix, raw material prices or Forex could negatively impact these margins in the future. I think that this is something that we would like investors, analysts, and all stakeholders to be mindful of.

I would further like to mention that our unit 3 operations continue to ramp up which has contributed to growth that you have recently witnessed. Some of our late-stage products are being scaled up here hence we foresee unit 3 utilization continuing to move up. As I had alluded earlier, we have a good visibility on the CMS business flow in terms of higher value projects over the short to medium-term and we expect these factors will contribute to our margin increase in the future as well. In order to keep up with the requirements of our customers, we will add new production blocks in unit 3 and invest in R&D infrastructure to facilitate their goals over time. As always, I would like to say that the very nature of Neuland's business in terms of working on high quality, complex molecules is such that revenues and margins could be lumpy on a quarter-to-quarter basis, but as Abhijit just now emphasized, on an annual basis they are steadily moving upwards and you could expect the same going forward. We think that the recent momentum is sustainable over long-term and therefore we continue to remain excited about the future of the business. So I think I will pause here and open it up for Q&A.

**Moderator:**

Thank you very much. We will now begin the question-and-answer session. We have a first question from the line of Sajal Kapoor an independent investor. Please go ahead.

**Sajal Kapoor:**

Hi! Thank you for taking my questions. I have a small acknowledgement to start with so I have been tracking Neuland Labs for almost two decades now and I must say that our balance sheet and cash flows has never been stronger than what we have today. So well done team and a warm welcome to our new CFO Mr. Abhijit Majumdar. I have two questions. So let us assume a hypothetical scenario where your competitor is a privately held and unlisted entity operating in the area of innovators and this is an NCE scale up as a service model and I guess they will have much more freedom to plan strategic objectives and execute them and as they will be a limited number of shareholders in a privately held business and these shareholders are also much more educated and much more aware of the business economics in terms of



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upfront capital deployment, long gestation window, and lumpiness in cash flows etc. Compared to being a listed entity like Neuland Labs where analyst and other shareholders are usually very impatient and short-term oriented and look one quarter at a time in a business that is fundamentally has very long cycle times like 7-8 or even ten years with upfront capital deployment in infrastructure, R&D, scientific talent etc. So which of these two companies is better placed in your view and the listed one or the unlisted one that is my first question.

**Saharsh Davuluri:** Yes. Thanks for sharing your observations. I think from the way we look at our business while there is challenges in the quarter-on-quarter smoothness of the business I think as CDMOs reach a certain size and think for Neuland our CMS business has been fairly small compared to our overall revenues. I think now it is closer to 35%-40% of our total revenues. But I think as we keep scaling up the business, we think that some of these volatilities can be managed and I think going forward also as the business keeps growing we should be able to provide a certain run rate of growth and performance, but it would be very difficult to demonstrate that on a quarter-to-quarter basis and I think ultimately investors will have to decide whether this is the kind of business that they would be interested in. But I think I do believe that as a listed company you can have lumpiness in your business model and as long as the business is profitable and has sustainable growth, I think being a listed company does not really create any kind of challenges being in the CDMO business.

**Sucheth Davuluri:** No, I would agree completely with what Saharsh has said it all depends on these specific organization rather than whether they are listed or unlisted and therefore as a company if you notice our investor calls over the last several quarters we have always said that please do not expect consistency on a quarter-to-quarter basis because that is not how our business operates that our business life cycle operates. However, we stated what our expectations from the business are in terms of product mix as well as margins over the long-term. So I think as long as the company is transparent, I think from shareholders and people like yourself you have always been understood and given that value.

**Sajal Kapoor:** That is helpful Sucheth and thank you Saharsh as well, and second question is on the private equity money that has been chasing API and generic CMO assets in India in recent years. Whether it is Carlyle Group or any other PE for that matter and they all are sitting on losses after almost three years and these guys typically invest for about five years right. So question really is on the economics of the generic pharma is throughout API businesses, I mean, is this not an investment worthy sector and private equity has got it wrong or you think they overestimated the growth runway and the cyclicity, which is inherent in any generic business with pricing pressure on one end and raw material and challenges on the supply side



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and both availability and the pricing of raw material and the pricing pressure of course on the product side. So how would you read it as an industry participant this obsession of private equity running after API assets and not being able to make any decent gains, I mean, all of them as far as sitting on losses and what do you think is it means for the industry and more importantly for Neuland Labs. Thank you.

**Saharsh Davuluri:**

Thanks for the question. I think we are quite well aware of the private equity activity in the API space and I think obviously while we are aware of what is going on it is hard for us to comment on what their specific strategy, financial goals, or exit plans are. I think what you understand about the business is that every API company is having a different strategy. Some companies are going after CRAMS of big pharma, some companies are going after Biotech companies, some companies are more focused on generic APIs, and every business has its own dynamics in terms of margin profile, growth, challenges, etc. So, I think the way we are looking at it from Neuland's perspective is the kind of businesses that we are focusing on which is the specialty API's as well as the CMS business. I think these require very high level of attention to the customer needs in terms of what needs to be done for their drug whether it is phased appropriate development, setting up the right kind of infrastructure, and providing them a partnership for a 5 to 10 year runway, and I think that is an area where we feel that we are very well calibrated as I think both culturally, organizationally to do that and in that space when we are going through that journey we do not necessarily see competitors around us I think because it is a very large space it is a \$50-\$60 billion space, the CDMO space that we operate in, we are too small a players or no one is big enough to really elbow the other out and therefore I think while we keenly observe what is happening we would find it very difficult to comment on what the rationale is but I think as far as our business is concerned we are not really seeing any direct threat or concerns coming out from these private equity backed organizations.

**Moderator:**

The next question is from the line of Mr. Rajat. Please go ahead.

**Rajat:**

Hi, Saharsh and congrats on the great side of numbers. I just have two questions. My first question is that if I were to compare your gross margins to any of the other API players right now even if I compare it to Divis. Right now, you are sitting at the highest gross margins within the API space in India at least on the listed space. I just want to understand like what you are doing so differently here like because I think you have large portion of your business coming from generic APIs also while if I see Divis they have roughly 50% of their revenues coming from custom synthesis, but still your gross margins are higher than them. Could you just give some color on that for my benefit? I also want to understand are there any particular



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products where you are really enjoying high realizations at the moment that you feel that going forward they might not be sustainable. That is my first question.

**Saharsh Davuluri:** I think what we have shared in terms of our remarks about the quarter I think it is a general representation of the trend going forward. I think yes, we also did see some challenges on raw materials, but as I had mentioned in my remarks it has softened a little bit it is not as severe as it was three or four quarters ago. I think some of these raw materials like these lithium metal based prices are still high, but solvents and all that has softened, but again I think the gross margins are also a direct factor of the business mix and the product mix that we have and maybe because of the mix that we have, we have this kind of margin, but again we are very clear that it is not a onetime exceptionally high gross margin. We think that this is a reasonable margin that we think is sustainable provided there is no major shift in terms of raw material supply situations or foreign exchange fluctuations and things like that. But I would not really know why the other players margins have maybe again because the businesses are so diverse within the API space it is just maybe the challenges that they are facing for their specific product. I think also another point to note is Prime has been relatively smaller compared to how big it used to be for us in the past and Prime is definitely a segment where we have some pricing challenges and maybe a few issues on raw materials, but I think we do not see any other challenges other than what we had mentioned.

**Rajat:** Could you also tell me like how much backward integrated are you at the moment like what percentage of your raw material is imported from China. Could you give some color there.

**Saharsh Davuluri:** So your question is about how backward integrated are we?

**Rajat:** Yes.

**Sucheth Davuluri:** It is a product specific strategy. So we do not have an overall umbrella of strategy that is where every product we have to be backward integrated because it does not make sense. So we do a product-by-product evaluation and for some products we are fully backward integrated, for some products given their supply situation they are not backward integrated, therefore we could not give you an overall percentage number. Today our procurement from China I would say is in the range of about 25% or so though our dependence on China is far less than that, but those are the rough numbers.

**Rajat:** Would it also be possible for you to break down this 24% growth which you have reported in the GDS segment in terms of price and volumes would that be possible.





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**Saharsh Davuluri:** We would prefer to keep the growth numbers to what we have shared. We would not be able to provide further.

**Rajat:** Okay, thanks. Thank you so much.

**Moderator:** Thank you. We have a next question from the line of Ankush Mahajan from Axis Securities. Please go ahead.

**Ankush Mahajan:** Thanks for the opportunity and congrats for good set of numbers. Sir, my question is that in the API segment at this time the whole industry is talking about the less export and prices are falling for the API's even the peers are also saying the same things on the con call. So would you throw some light how do you see our company in regarding to it that what about the price realizations for the API's that is the first part? Second, what about the capacity utilization of the new plant and how do you see the capacity utilization in the current quarter that is Q4.

**Sucheth Davuluri:** On the pricing side we had mentioned this in previous calls, but over the last decade or so we have consistently derisked our procurement positions from China to other suppliers. So we have made the supply chain much closer to home and therefore as far as our solvents our raw materials are concerned. We are seeing volatility, but it is not extreme volatility as we see reflected in our performance numbers as well. Coming to your second part I think our unit 1 and unit 2 the capacity utilization tends to range between 80% to 85% given that specific quarter and the product mix. Our unit 3 is about 65% based on the installed capacity today, but given that our unit 3 is growing and we continue to add capacity that number will keep evolving.

**Ankush Mahajan:** So, sir, unit 1, unit 2, 85% and unit 3, 65% currently.

**Sucheth Davuluri:** Correct, I said 80% plus, minus.

**Ankush Mahajan:** Sir would you throw some more light on the CMS business how the commercial and development stages they could do in upcoming quarters.

**Saharsh Davuluri:** I think as I had indicated earlier there has been good progress in terms of commercialization of certain CMS molecules. I think the increase in the commercial revenues this quarter is an indication of that. Going forward we expect over the several quarters in the next couple of years maybe that more molecules will get commercialized, and we are actually very excited about the potential of these molecules, and as these molecules get commercialized and the ones that just recently got commercialized also scale up, we think that will be a key driver for



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the CMS business. I think if you go back to our con calls two years ago we had indicated that we have pipeline of several molecules, which are either completing phase three early part of commercialization these molecules are all kind of still around and maybe 2 have become commercial since then. I think if you look at our tables that we disclose that number is evident and I think in the maybe next one to two years we expect maybe a couple more to get commercial. The number may be very small, but these are high potential molecules. So I think we are excited about that and the only caveat I would add is because these are new drugs there is always a risk that the drug may not get approved or there is also a risk that the drug may not be successful. So therefore we are still very cautious, but I think if you look at the last several quarters trend it should give you some indication that things are looking positive from a CMS commercialization. So I think that is what we can share at this point.

**Ankush Mahajan:** Even we see in the CMS business that from the last two quarters doing very well. So some kind of a growth, any growth number that we can put on the CMS side.

**Saharsh Davuluri:** We would not be able to give any sort of guidance, but I think all we have been confident to say is that whatever numbers we are seeing and whatever kind of trajectory we are seeing is a sustainable one. So there is nothing like an exceptional quarter that has happened and we will go back to how we were like say three, four quarters ago. But I think beyond that it is very difficult for us to give any guidance.

**Saharsh Davuluri:** Thank you. We have our next question from the line of Nikhil from SIMPL. Please go ahead.

**Nikhil:** Hi, congratulations on great set of numbers and I think I will add to previous participant's point that we have never seen the balance sheet of Neuland being so strong in terms of debt and cash flows. So great work and the efforts, which the management has been making I think now results are clearly visible. Just two questions, one is Saharsh if I look at our product mix break up between prime and specialty and compare it year-on-year so last year it was around 56 which is now 61 the prime and specialty both. While if we look at the industry across most API commentary people have been complaining about high inventory levels and as a result there is a major inventory destocking which is happening and the demand has been hit and also the pricing has been hit. But our numbers seem to be very different from what the industry across players what we are looking at. So if you can just help us understand what different is happening in our set of products because the prime and specialty mix has only improved where there should have been more inventory issues which the industry is talking about, but our numbers are good. So just help us understand on these two segments.



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**Sajeev E. Medikonda:** I think there are two elements here, when it comes to our specialty business I think the growth is being driven and the numbers are a reflection of some of the molecules which are in the pipeline where our customers are taking quantities for launch and as we have mentioned molecules like Apixaban and Paliperidone have driven some of the revenues and the growth there and also we have had other specialty molecules like Donepezil, Ezetimibe too which have contributed and I think even as you see that there is an industry trend. I think for these specific products a part of the cycle where I think there is a continuous growth and also customers are looking at launch, which is why you are seeing that reflection in the numbers. And when it comes to prime, I think again it is products like Mirtazapine and a few others which are contributing consistently to the revenues and it is in our case we have a lot of molecules which are say around 100 to 200 tons medium in terms of their molecule size when it comes to tons where there have not been fortunately so many inventory issues because the buildup is likely to be lower in the medium size kind of volume product. So that is the reason why we have seen a certain consistency in the last two quarters from these segments.

**Nikhil:** Thanks for the detailed explanation. Just one last question on the CMS side. Now if we go to slide #15 what we see is that the commercial launch has scaled up. So for last four quarters we were averaging around between Rs. 40 to 50 Crores and this quarter we move to almost Rs. 75 Crores. So which means there is a big commercial launch either which has happened or we have participated. So do you see because what we understand in the patented molecules the buyers pick up for large volumes and then it stays for some time and then it reduces to a normal level till the time the next quantum is required for a larger launch or based on the demand. So this Rs. 74 Crore, 75 Crore is sustainable or do you think we will come back to that Rs. 40 Crore, 50 Crore kind of a run rate. So is it supported by a launch of a molecule, which has driven this?

**Saharsh Davuluri:** The short answer is that it is sustainable because I think what you are alluding to is typically how a launch happens, but every case is very different sometimes you get, you are commercializing a drug that is already in the market as a second source in which case you will probably start supplying continuously from the beginning, in some cases there could be a situation where you will make maybe three, four months or three, four quarters of launch quantities and then you will go into maybe hibernation for a year or so. So I think it is possible, different scenarios are possible, but I think the question that I am guessing you want to know is like is this the onetime thing or is it sustainable I think the short answer to that is it is sustainable.

**Nikhil:** Thanks. I will come back to the queue.



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**Moderator:** Thank you. We have our next question from the line of Sanjaya Satapathy from Ampersand. Please go ahead.

**Sanjaya Satapathy:** Sir, thanks a lot. I just want to ask a couple of questions, that your specialty business contribution declined in this quarter, if you can just explain that and secondly though you have already warned that your numbers will be volatile because of the nature of business, but your commentary nowadays is far more confident than what you used to do in previous year. So what has really changed if you can just explain it.

**Sajeev E. Medikonda:** If we to look at the specialty segment I think we again because the molecules themselves are small volume in terms of their nature. So there is likelihood to be more lumpiness because even customers campaigns and all are not done on a regular basis, but are done more on make to order and the certain order is based on how the demand emphasis over a period of time. So therefore there is likely to be a certain lumpiness, but if you have to look at it over an annual period we can see that there has been a significant growth even in this specialty business and which is very clear both in the percentage from the specialty business and even it is reflected even in our margins too. So it is just there is likely to be a certain lumpiness because of the nature of the molecules, but overall we are seeing an upward trend.

**Sanjaya Satapathy:** Thanks and if you can just tell us about that will your numbers be less volatile and kind of a secular relatively secular compared to what the turbulence that you saw in the previous years or I mean have you kind of reached the stage where you can be a lot more sure about your prospects primarily because your new molecules are in a more better commercial state.

**Saharsh Davuluri:** Are you referring to the specialty business in particular or the overall business?

**Sanjaya Satapathy:** I am talking about the CMS business now.

**Saharsh Davuluri:** The CMS business. I think yes as we had indicated a couple of times in this call the CMS business the shift to commercialization is giving us more confidence that this business is sustainable and it is more sticky and I think you should see continued performance going forward. I think depending on the order mix there could be variation in terms of margins and numbers etc. But I think overall what we are emphasizing is if it is commercial revenue you can see that it will be sustainable maybe with a little bit of lumpiness, but it will be sustainable for sure.

**Sanjaya Satapathy:** And lastly on unit 3 can you just tell us like what kind of utilization now and what kind of utilization we are looking forward to next couple of years.



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**Abhijit Majumdar:** Yes. So, if you look at, I think so. Sucheth has mentioned that unit 3 utilization in FY2023 estimate is around 62% to 65%. As we move forward into FY2024 with the product mix change we would be closer to 68%-69% and so kind of tells you there is a window of growth that would come from next two years.

**Sanjaya Satapathy:** Understood. Thanks a lot, Sir.

**Moderator:** Thank you. We have our next question from the line of Gautam Bahal from Mauryan Capital. Please go ahead.

**Gautam Bahal:** Hi, thanks for taking my questions. Just a quick one on unit 3 has the US FDA approval come through there or if not what is the update there be.

**Sucheth Davuluri:** Yes. So we have a product that we are shipping into the US from unit 3 so we have had a virtual audits by the FDA we have not had a physical inspection yet, but, besides it is listed in the FDA database as an inspected site for the US market.

**Gautam Bahal:** Is there any sort of clarification of when that physical inspection will happen like it has been triggered already right.

**Sucheth Davuluri:** See, right now the FDA determines when the physical inspection happens. Right now as far as we are concerned, we have not seen any approvals from unit 3 being held up because of a lack of physical inspection. Therefore it is a complete prerogative of the agency to schedule an inspection.

**Gautam Bahal:** But, I mean, correct me if I am wrong at the moment you are not making any novel sort of, novel stuff from unit 3 right it is mostly the generic that is being manufactured there. You are waiting for the...

**Saharsh Davuluri:** We are making NCE's from unit 3 along with generics and I think what Sucheth said applies to both because the way the FDA has been functioning especially post COVID is if they are not seeing any broad based challenges with an organization they are approving specific filings with online inspections. They are not necessarily holding back approvals for a physical inspection. So therefore our product is getting consumed or will get consumed in the US markets without any physical inspections both for NCE's and genetics.

**Sucheth Davuluri:** Yes and that is the current status of this. But as you know things keep changing in the dynamic landscape.



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- Saharsh Davuluri:** Yes, they may come for a physical inspection which we are ready and welcome at any time.
- Gautam Baha:** But unit three at the moment is still running at a breakeven or loss or any update there.
- Saharsh Davuluri:** I think we have not disclosed unit wise numbers but I think we can indicate that I think by this upcoming quarter we would have turned the corner and it would be profitable. Yes.
- Gautam Baha:** Okay, wonderful thank you very much.
- Moderator:** Thank you. We have our next question from the line of Keshav Kumar from RakSan Investors. Please go ahead.
- Keshav Kumar:** Hi, good evening. Sir with the debt to equity of 0.13 looks like we have reduced a substantial amount of debt this quarter and one of our peers has seen challenges in receivables so I guess the inflation and cost of debt is leading to some pain over there due to clients deferring payments. So are we seeing or anticipating some impact in the near-term or as of now it is a business as usual for us.
- Abhijit Majumdar:** If you look at how we have reduced debt in this quarter kind of gives tells you the resilience of the underlying business. Working capital remains as it is as we gear up ourselves for Q4. So the short answer is we are not facing the challenges that others may be facing.
- Keshav Kumar:** And sir lastly on a medium to long-term. So there is quite a bit which has happened in bio pharma in the last 20 years and last five years we see AI impacting in a big way. So there is a lot of progress in proteomics databases are being populated at an ever increasing pace ability to figure protein structure, finding potential new targets, and so forth. So this should come as a beneficiary to both small molecules and peptides. But when we see the CDMO supply they have traditionally been in short supply and with the times of 18 to 24 months and the capacity cannot be scaled exponential to match the pace of drug discovery advances. So just pure empirically we should see a much larger share of inquiry because we are a decently established player and also have the capability to do both peptides and small molecules. So is it too soon to sort of have any feelers yet or are we seeing the intensity of early phase inquiries going up.
- Saharsh Davuluri:** I think generally speaking we have I think as we have been executing more projects successfully in the CMS space because it is a B2B space and a lot of recognition, brand recognition happens through professional networks etc. I think we are seeing increase, steady increase in terms of inquiries and I think beyond that I think it is hard to correlate with the



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comments you had made about the general drug discovery landscape and what is happening over there, but I think we have been kind of seeing a healthy increase in terms of inquiries and we become a little bit more selective in terms of the kind of projects we want to work on. Sajeev anything you want to add.

**Sajeev E. Medikonda:** Yes, so again the point that you make about the discovery the timelines and all of that is valid, but I think if you see over the past our focus has been more in terms of molecules in terms of our BD approach is bordered on molecules in phase two onwards and there even as we are seeing more traction I think it will take some more time for us the impact from flowing through from preclinical to phase two to happen for it to show up in our purview. So I think to answer your broader question that is where we are right now.

**Keshav Kumar:** Sure thank you Sir. That is all from me. Thank you.

**Moderator:** Thank you. We have our next question from the line of Sachin Jain an individual investor. Please go ahead.

**Sachin Jain:** Hi, Saharsh, hi, Sucheth, congratulations on good set of numbers. My question is as now business mix improving the desired level and probably the margin trajectory you are sounding more confident. What is the sustainable ROCE you guys building in.

**Abhijit Majumdar:** If you broadly look at our ROCE. So we are targeting an ROCE in the broad range of 17 to 20% and that I think so is what we would kind of want to sustain at in that broad range.

**Sachin Jain:** And my second question is basically if you have to see the CMS business for next three to five years can you give some color how you guys are seeing the scalability from here basically.

**Saharsh Davuluri:** I think it is definitely looking very exciting for us because the quality of the pipeline in the recent periods have been significantly better compared to what we used to have earlier and I think in terms of the annual revenue per molecule or the margin profile for the molecule or the likelihood of the drug success, the therapeutic area. I think on all the important parameters that you would assess and see I think the pipeline has been better and I think these molecules have also now started commercialization. So therefore I think in many ways there is a lot of scope for growth and obviously a lot of excitement about the CMS pipeline. The revenue growth that will come I think will be evident in the coming couple of years and it is hard to paint a picture around it because saying a percentage number I think could be misleading because it could be either way, but I think we have started to see commercialization and again



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as I mentioned two molecules have already commercialized in the last one year and we expect maybe another couple to commercialize and each of these by themselves are saying attractive and cumulatively it should be good and most important thing I would like to underscore is that our pursuit of new projects continues, our goal is to keep adding such opportunities to our pipeline and not every opportunity will be a successful commercial contract, but I think we are continuing to add these and we are creating capacities to support that. So I think overall it is very exciting I think next three to five years we should see a good healthy growth and profitability from the CMS business and I think it complements very nicely with our GDS business. So I think we have a good package or not, but I am not really able to quantify things unfortunately.

**Moderator:** Thank you. We have our next question from the line of Kunal from Carnelian Asset Management. Please go ahead.

**Kunal:** Thanks for the opportunity. I have just one question. What are our Capex plan for the next year. If at all any.

**Abhijit Majumdar:** Broadly if you look at trending we have been spending around Rs. 100 Crores to this capability in our plants and that could be taken as a trending that would continue. Having said that if large capital investments we have to do to grow our business as and when it happens and we get board approval, we will surely inform you in our quarterly earnings call.

**Kunal:** So basically Rs. 100 Crores would be maintenance kind of a Capex not capacity enhancing Capex I understand correct.

**Abhijit Majumdar:** Yes, so it is a combination of maintenance as well as upgrades, which kind of enables us to meet the capacities of a particular molecule, which suddenly grew so it is a combination of both, but you could take that as a broad indicator.

**Saharsh Davuluri:** And maybe what I will add to Abhijit's comment is I think a lot of the business growth may also require capital expenditure, which I think will happen in tandem with the business contract or some certainty of business. So in some ways I think beyond what Abhijit said if we do invest more it will be perhaps because we see more growth in terms of some other scale up opportunities, but I think what we have shared is currently what is on the radar.

**Kunal:** It will be safe to assume going to be more on the CMS business side. If at all anything lined up.





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**Saharsh Davuluri:** I think typically our strategy has been to add capital expenditure on the back of the CMS molecules and since the capacity is fungible between GDS and CMS we are also able to use the same capacities for the GDS business, but I think over the last few years I do not think we have created capacity exclusively for GDS business. I think in unit 3 to initiate unit 3 operations I think the initial capacity created was for GDS, but I think the capacity that we are creating now is we are creating new capacity it may be to accommodate the growth from these new CMS molecules, but irrespective the capacity is fungible between GDS and CMS and what we typically do is we look two years ahead and make sure that we have capacities in place.

**Kunal:** Just one question I do not know why its right. Just wanted to understand as our gross margin is pairing because of the product mix change and because of the branches that we have in the CMS specialty businesses. So how would one look at the margin basically for these three businesses, I mean, the ranking is known right, but still what would be the kind of difference and the gross margins between those three segments. So as an investor to gauge as to how much gross margin can vary between the three business verticals depending on the content.

**Saharsh Davuluri:** I think there can be see I think at a high level the gross margins of the specialty and the CMS may be similar to now. But I think what is very important for you to understand is that a product level there is a variation in gross margin product-to-product. In CMS or in specialty we have products which have 80% gross margins, we also have products which have maybe 30%-35% gross margins and how we do in a particular quarter is also a factor of how much of a particular product we have shipped. So I think it is hard to give you more granularity on how the gross margins will figure out, but I think what we are seeing is a good blend right now and unless there is a crazy surge in raw materials or maybe big fluctuation in forex. These margins are a reasonable baseline for now to take, but we do not really want to give you spell out margins of prime, specialty and CMS separately because that may also not be very accurate because then if we ship certain products in CMS then that margin will change and then you will wonder why is the margins of CMS different. So I think rather keep the margins at an aggregate level and just help you understand that these are broadly the reasonable margins to assume.

**Kunal:** Fair enough. The only reason for asking is if I look at the last year quarters the gross margin specifically has had wide variances. So just wanted to have color, but fair enough I understand what you are trying to say. Thank you wishing you all the best.



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**Moderator:** Thank you. We have our next question from the line of Sajal Kapoor an individual investor. Please go ahead.

**Sajal Kapoor:** Hi, thanks for the follow up. Quick question now our R&D infrastructure and so in terms of our R&D investment, is the current R&D setup in terms of campus size and capability as well as the scientific talent mix is it good enough for next two years or do you think we need a bigger R&D campus or we need to significantly scale up from our current base of around 300 scientists.

**Saharsh Davuluri:** I think today we are operating at about 360-370 scientists but as you indicate it is fairly tight because we do have, we do use a lot of scientists for troubleshooting in the plant, we use them for lifecycle management, we also have active GDS programs, and then we have the CMS business. So we are making some increases in R&D capacity in the upcoming financial year and we think tactically that should suffice for the upcoming financial year, but maybe from a two to three-year perspective it may not be enough. So we are also looking at slightly medium-term plans which might involve some expansion of R&D, but at the same time we are also looking at ways in which we can improve the effectiveness of R&D that could be in terms of maybe putting systems in place, trying to also be better in selecting the kind of projects we want to take up in the organization, maybe also trying to do more computer aided experimentation to reduce the load on the bench. So I think there are a lot of important initiatives that are being taken up right now. I think studying pilot actions carefully, using good modern techniques, using chemical engineering expertise is also a way to reduce your loan on R&D labs. So I think it is an important question I think we are in the midst of doing proper evaluation on what is good for doing process R&D. I think decisions to expand will be based on what we figure out in the next six months or so. But I think definitely as a growing company we will have to make sure that R&D resources do not limit our ability to scale up more and more projects.

**Sajal Kapoor:** That is very reassuring and thank you so much.

**Moderator:** Thank you. Ladies and gentlemen that was the last question for today. I now hand the conference over to management for closing comments. Over to you, sir.

**Sajeev E. Medikonda:** I would like to thank everyone for the engaging questions on the business. While we make every effort to answer your questions would be available clarity to us at this point of time, your questions also act as stimulants for our internal conversations. Even as we are excited about our business, it is important for us that our investors share that and your participation



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today reflects that and for that we would like to thank you. Wish you all a good evening and look forward to talking again.

**Moderator:** Thank you. On behalf of Neuland Laboratories that concludes this conference. Thank you for joining us and you may now disconnect your lines.