IOL CHEMICALS AND PHARMACEUTICALS LIMITED

19th November 2022
IOLCP/CGC/2022

National Stock Exchange of India Ltd.
Exchange Plaza, Plot no. C/1, G Block,
Bandra-Kurla Complex, Bandra (E)
Mumbai - 400 051
Security Symbol: IOLCP

BSE Limited
Phiroze Jeejeebhoy Towers,
Dalal Street
Mumbai – 400 001
Security Code: 524164

Subject: Transcript of Earnings Conference Call, post declaration of audited financial results for the quarter and half year ended 30th September 2022

Dear Sir,

In continuation to our letter dated 14th November 2022 regarding intimation of Schedule of analyst/ investors conference call – Q2 & H1 FY23, please find attached herewith the transcript of Earnings Conference Call organized by the Company on 15th November 2022 post declaration of audited financial results for the quarter and half year ended 30th September 2022.

This is for your information and records.

Thanking You,

Yours faithfully,
For IOL Chemicals and Pharmaceuticals Limited

ABHAY RAJ SINGH Digitally signed by ABHAY RAJ SINGH Date: 2022.11.19 11:21:42 +05'30'

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IOL Chemicals and Pharmaceuticals Limited
Q2 & H1 FY23 Earnings Conference Call
November 15, 2022

Moderator: Ladies and gentlemen, good day and welcome to Q2 FY23 earnings conference call of IOL Chemicals and Pharmaceuticals Limited. From the management, we have with us Dr. Sanjay Chaturvedi, Executive Director and CEO; Mr. Pardeep Khanna, Chief Financial Officer; and Mr. Abhay Raj Singh, VP and Company Secretary.

As a reminder, all the participants' 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 this conference call, please signal an operator by pressing "*" and then "0" on your touch-tone phone. Please note that this conference is being recorded.

Before we begin, I would like to mention that some of the statements made in today's discussion may be forward-looking in nature and may involve risks and uncertainties. I will now hand the conference over to Dr. Sanjay Chaturvedi for his opening remarks.

Dr. Sanjay Chaturvedi: Good afternoon everyone. We welcome you to our Q2 and H1 financial year '23 earnings call. I trust you have all gone through our financials and the investor presentation that is available on exchanges as well as on our website. I would like to share some insights on the global economic growth and the Indian market before we dwell into your company's performance for the second quarter. Then, my colleague, Mr. Pardeep Khanna, our CFO, will take you through our financials, post which we will open up the forum for a Q&A session.

The global economy is going through a rollercoaster ride as the Central Banks battle inflation through rate hikes. Though the commodity prices have softened in the last few months, the developed markets are still facing very high inflation and thereby prompting Central Banks to take very stringent steps. In the United States, the Central Bank, the Federal Reserve last week approved a fourth straight rate hike to 4%, the highest Fed rate since the 2008 crisis. Hong Kong and Norway have followed the suit raising the benchmark rates to 4.25% and 2.5%, respectively. This was followed by the Bank of England raising interest rate to 3%, the biggest rate rise in 3 decades. With Central Bank still chasing inflation, the global growth outlook has weakened with the International Monetary Fund forecasting global growth at 3.2% in 2022 and 2.7% in 2023, down from 6% in 2021 in its latest global economic outlook.

Apart from inflation, the global trade and investor sentiments are also impacted by uncertainty over Russia's invasion of Ukraine and the resulting trade imbalances. Frequent lockdowns in China following a zero COVID policy with further destabilizing the global supply chains. These global challenges have led to broader and sharper-than-expected slowdown alleviating the cost of living crisis as the IMF puts it.

Back home, the Indian economy, despite global uncertainties is recovering as is evidenced from numerous factors like factory growth, manufacturing purchasing managers index, optimism around fresh hiring and overall demand scenario. The Indian economy has shown resilience towards persistent high inflation and has clearly emerged as an outlier with private capital expenditure expected to surge in the next half of the current financial year as companies gear up to increase production and to add inventories to fulfill the growing demand.

The optimism for the Indian economy is high in the global investor community as well which is shown by continuous FII inflows into the equities market. For the Indian market, there are factors that are a blessing in disguise. API is one such opportunity. While the world has looked at China so far for APIs, the supply disruptions amidst the COVID-related lockdowns is opening up a grand opportunity for the Indian API players who are finding robust export inquiries. We believe that this situation is likely to persist over the next few quarters, as Indian players vie for the Chinese share. For the pharmaceutical segment, we continue to de-risk and reduce the Ibuprofen business and increase the share of the non-ibuprofen API business and other intermediates. Currently, the company is focusing on growing metformin, clopidogrel, fenofibrate, and doing capacity additions to grow our market share in some of these molecules.

In the specialty chemicals segment, the Indian players are trying to stabilize with commodity import price cooling off to a certain extent. We believe that the rise in energy and commodity prices is temporary. And hence, we have tried to absorb some portion of it and some of it has been passed along to the customers.

As mentioned in our last call, we are in the process of setting up new capacities for both specialty chemicals as well as pharma products. By the time the capacities are up and running, we expect the headwinds to subside and therefore give us an edge in terms of operational efficiency and higher margins with increased production.

During the quarter, we registered the REACH Certificate for ethyl acetate and with a tonnage band of more than 1,000 tonnes per annum in accordance with EU REACH regulations on the chemicals and the safe use. This certification allows the company to export ethyl acetate across all countries in the European Union. Last week, we also received EDQM certification to supply pantoprazole sodium as well as API in the European markets.

With this, I would like to hand over to my colleague, Mr. Pardeep Khanna, our CFO, who will be sharing financials in detail. Over to you, Mr. Pardeep.

Pardeep Khanna: Good afternoon everyone and thank you for joining us today to discuss our performance for the second quarter ended 30th September 2022. I will take you through the financial highlights for the second quarter and first half of the financial year 2023.

The total income of the company in the second quarter of financial year '23 stood at Rs. 546 crore as against Rs. 540 crore in the corresponding quarter of financial year '22 and Rs. 570 crore in the previous quarter ended June 2022. EBITDA for the quarter was Rs. 37 crore as against Rs. 54 crore in the corresponding quarter of financial year '22 and Rs. 61 crore in quarter 1 of financial year '23. EBITDA margin for the quarter was 6.7% as against 10.7% in the previous quarter.

Net profit in the second quarter was Rs. 15.70 crore as against Rs. 31 crore in the corresponding quarter of the last year and Rs. 35 crore in the quarter 1 of financial year '23.

With this, we open the forum for a question-answer session.

Moderator: We will now begin the question & answer session. We will wait for a moment while the question queue assembles. The first question is from the line of Venkat from 3Sigma Financials. Please go ahead.

Venkat: Sir, for the last several quarters, our margins have been coming down. What is the challenge? Are we not able to pass on the price or what kind of challenges are we facing? Now that the raw material prices also have come down and freight prices have come down substantially, is there some problem in product mix? Or what kind of challenges are we facing if you can throw some light? And also, if you look at the sales numbers also, they are somewhere around Rs. 550 crore. It looks like there is some scalability issue also we are facing.

Dr. Sanjay Chaturvedi: There are 2 questions you have asked. One is on the profitability as it relates to raw materials and the second has got to do with scalability. Let me talk about the second point first. On scalability, there is no issue. If you look at our business, we have 2 divisions - on the chemical side and the pharmaceuticals side. The chemicals business is capped in terms of volume because the capacity expansion that we are doing hasn't come on stream yet. So, the revenue that we get on the chemicals side depends entirely on the price of our key product that, i.e., ethyl acetate. If you look at the price of ethyl acetate in Q1 versus Q2, the price corrected by about 14%. And that's the reason you see the dip in sales for the chemicals segment. If you look at our pharmaceutical segment, it has actually grown. And that growth is related directly to the volume and the asset utilization on the pharmaceuticals side. We are addressing the scalability issue by actually adding capacity on the chemicals side, and there is no scalability issue on the pharmaceuticals side.

Now let me come to the profitability part. You are right in saying that now the raw material prices seem to have stabilized, but a lot of the raw materials that we buy along with our peers are actually imported, and therefore, these orders are placed months in advance. If you look at the chemicals side, our key raw material is acetic acid. Between Q1 and Q2, the acetic acid price has corrected by as much as 40%. And what that meant was that during quarter 2, we were left with a lot of inventory of acetic acid that we had actually purchased towards the end of Q1 at a much higher price. And in these kind of commodity products, it is not easily possible to pass on the entire cost increase. If you look at, say, the corresponding quarter for Q1 in the previous financial year, you will see that the chemicals business has shown huge profitability. And that was because the prices of raw materials have actually gone up. So, we benefited in that quarter because we had a lot of inventory at a lower price. So, when you look at chemicals, in some quarters, you will come out ahead, and in some quarters, you will come out behind. But on an average, it is reasonable to expect that your EBITDA margins will be maybe in the 6% to 8% range.

On the pharmaceuticals side, the raw material prices, we have been able to pass along. And actually, that is a business that is also running at about almost double-digit EBITDA margins. Yes, with our asset utilization going up, we expect these margins to go up as well. And the API industry if you look at overall Q2, all our peers and competitors have highly muted numbers. And I think with the exception of maybe one large API player, almost 8 or 10 API players that I have benchmarked have all de-grown their profits quarter on quarter. But I think it is good to understand what the baseline is, and I would say that running an API business at about 15% EBITDA margin is a reasonably good quality business and we will get there by the end of this year.

Venkat: And how would the growth numbers look sir, from next quarter, next year? Earlier, we used to give a 15% growth projection actually. Are we on the track or we are not going to be there?

Dr. Sanjay Chaturvedi: This year, we are going to show some muted growth in the single digits, but next year going forward, in the next financial year, we are very confident of double-digit growth in terms of value, not just volume.

Venkat: Sir, my second question is on the specialty chemicals and chemicals where we are talking about EBITDA margin of 6% to 8%. While the cost of funds itself is getting closer to a double digit, do you actually see value in expanding the capacity or do you find justification like returning that money to shareholders? And the management itself is a big shareholder and they might be benefited with that. So, 6% to 8% isn't even covering the cost of capital actually or close to cost of capital?

Dr. Sanjay Chaturvedi: It is an excellent question. And if I were borrowing capital at 6% to 8% to run this business, then you are absolutely right. But I am currently a zero debt company and meeting all my costs through internal accruals. So, I am not really…. This is a notional cost or the cost of borrowing as far as this business is concerned. One is, of course, running the business. The other is customers. There are a lot of customers who buy from me, not only the specialty chemicals but APIs as well. We cannot take long-term business decisions based on quarter-by-quarter performance. Imagine for a moment that I have a very large pharmaceutical customer who is buying ethyl acetate along with APIs and I walk up to this customer and tell him that, "Look, I understand you've been buying with me for the last 10 years, but today, this quarter, I am not making money. So, I'll stop the production." My point is, I am trying to sensitize you that there are larger issues at play when you are dealing with large pharmaceutical customers who buy a range of products that include specialty chemicals and intermediates and APIs.

Venkat: There are 2 aspects that I wanted to mention, sir. Quarter on quarter, we have been discussing about the chemicals and specialty chemicals EBITDA less than or probably in single digit. This is not a specifically quarter-related problem. And the second point is we are adding CapEx on top of the existing capacities, actually, on something which has such a low EBITDA. That is where my thought process comes actually.

Dr. Sanjay Chaturvedi: I am not actually adding a new plant for this right now. But I am augmenting my existing capacity at a very modest Capex that I am funding through internal accruals without taking debt.

Venkat: So, you find justification in giving value to the customers. That is the value add that you are providing by adding the capacities in the functioning of the chemicals and specialty chemicals?

Dr. Sanjay Chaturvedi: Yes.

Moderator: The next question is from the line of Avinash Kumar from Hridaya Kumar. Please go ahead.

Hridaya Kumar: Sir, my question is regarding the expansion that we have planned. By when the capacity would be upstream and how much revenue are we going to generate from that capacity expansion?

Dr. Sanjay Chaturvedi: The current capacity expansion that we are doing in our existing site is roughly around 20,000 tonnes a year. And depending on what the price of ethyl acetate would be, if the price of ethyl acetate is Rs. 100 a kilo, that would add Rs. 200 crore, and if it is Rs. 80 a kilo, it would add about Rs. 160 crore.

Avinash Kumar: Actually, my question was regarding the expansion which you had planned in the West side of India.

Dr. Sanjay Chaturvedi: That exercise is still ongoing. We have contracted some credible partners to identify the site for us. And I think it would take maybe Q4 before we are able to conclude what we are going to do and at what scale we are going to do.

Moderator: The next question is from the line of Shaikh Mohammad Ayaz, an individual investor. Please go ahead.

Shaikh Mohammad Ayaz: Sir, what margins we can expect from the next 2 quarters? EBITDA margins?

Dr. Sanjay Chaturvedi: I think it is reasonable to say that in the next 2 quarters, we will be back into the double-digit margins as far as EBITDA numbers are concerned.

Shaikh Mohammad Ayaz: Sir, you told that most of the companies' EBITDA margins have been reduced. But if you see Neuland Laboratories, Granules, Gujarat Themis, and even Solara has reduced their loss. Last quarter, they have made a sequential loss, but now they have reduced their loss. But while comparing to that, we have shown a de-growth in terms of EBITDA margins. I understand it is because of the chemical division only, but due to the reduced cost of raw material and shipping costs, there should be some improvement. I was expecting some improvement in margins. And from the last 2 quarters, you are telling that we will be back to double-digit margins. But since then, I haven't seen those kind of margins.

Dr. Sanjay Chaturvedi: I think that recovery has been delayed a little bit. And you talked about some of the other players where their business model is somewhat different. You talked about companies that are actually not pure-play API companies. They are a combination of formulations and APIs and some of them have a very strong CRAMS business. And as you know, CRAMS and formulation businesses run at significantly higher margins compared to API businesses, but they also carry very different types of risks associated with those. If you really compare us apple-to-apple within the pure-play API segment, I think we are pretty much in line with the industry. Actually, if you look at our performance this quarter also, at least the API business has already delivered double-digit EBITDA margin, and that is going to improve significantly in Q3 and Q4. And what we also expect is an improvement in the performance on the chemicals side as well.

Shaikh Mohammad Ayaz: The next question is, if you see investor-friendly companies, there will be bonuses, there will be splits, there will be buybacks. But when I see your company, nothing has been done since listing of the company. I think rights issue has been done once. But among others, nothing has been done. And if I see companies which are really confident in their business, they are increasing their stake as a promoter, but I can't see anything in your company, sir?

Dr. Sanjay Chaturvedi: We have not initiated any buyback, but I think there are many ways to look at confidence in the business. The buyback is certainly one, but I would argue that the ability to put Capex and the ability to invest money into R&D, the ability to invest money into human capital, there are a lot of ways to look at management's confidence in the company. And this is actually a year I would argue that we spent more on Capex than any other year. And in fact, a lot of the Capex spend that we have done has gone into things like EHS to take care of the environment, and into warehousing. These are investments into Capex that don't necessarily translate directly into revenue. But to me, they are as strong of an indicator as a buyback program.

Moderator: The next question is from the line of Bezad Deboo from Systematix Group. Please go ahead.

Bezad Deboo: For this quarter, what is your capacity utilization in Ibuprofen and Isobutylbenzene?

Dr. Sanjay Chaturvedi: I can tell you about the ibuprofen. My current asset utilization is about 75% or so - between 75% and 80%. And in the next few quarters, I will take that to about 85%.

Bezad Deboo: And you are adding additional capacities on the chemicals front. When can we expect that to come online?

Dr. Sanjay Chaturvedi: That should come online by the end of this financial year. We will see accruals from that business in the Q1 of next financial year.

Moderator: The next question is from the line of Govindlal, an individual investor. Please go ahead.

Govindlal: I got only one question, sir. In the last call's closing comments, you had told that IOL has come out with a strong set of numbers and these will only improve here on. This is almost in the middle of the last quarter after 40 days. Now the results have come; EBITDA is 40% down, margins are down 4%, and PAT is down 55%. How should we believe, sir, going forward, what you are guiding, it will be done when? Middle of the quarter, you know your business better. After 40 days have gone in a quarter, you don't have visibility of another 40 days also, how should we believe the management? That's what I am asking, sir? You know yourself better. When you told that it will be improved from here on, but it has de-grown; that is also 40%, 50%, not 10%, 20%.

Dr. Sanjay Chaturvedi: I understand. It's a valid concern. And I would say, "Look at our business as a deconvolution of 2 different segments. One is on the chemicals side and the other is on the pharmaceuticals side." Most of the dip in performance has been on accord of actually the chemicals front. That's a business where not only did I lose profitability, I actually went into a loss for the quarter because on account of a huge inventory of the raw material at a much higher price. That has since been corrected. And also the energy costs have gone up since the last quarter. My pharmaceutical business is still delivering double-digit margins. And now my focus in Q3 and Q4 is to, a) completely turn around the chemicals business for which I already have the visibility. b) If I look at the pharmaceutical business, through better control on costs and better utilization of the assets, with now as you have seen through our presentation, we have gotten regulatory approvals for more and more products. The India business for most APIs is actually a very spot business, whereas the real money for APIs is when you export into regulated markets. As we grow that side of the business and the lead indicator for that are more and more approvals that you have on the CEP side and approvals from other European markets. Those are lead indicators. And today, we are very confident that as an average, we will come back into double-digit EBITDA margins from next quarter onwards.

Govindlal: Only my request is that as investors, we depend upon your guidance all the time and we take investment decisions, sir. So, better to be a little conservative in guiding. That will be very helpful, sir. So, build in some all this contingency in your guidance always. Don't build in rosy scenarios, build some contingencies also.

Moderator: The next question is from the line of Mahesh Vyas from UTI Mutual Fund. Please go ahead.

Mahesh Vyas: Just a couple of questions I have on our imports. What percentage of total consumption is from imports? And what percentage of imports is there from China and the percentage of imports excluding DCDA because any which way we are dependent on DCDA on China?

Dr. Sanjay Chaturvedi: If I look at the chemicals side, roughly 70% is imports. If I look at the pharmaceuticals side and if I take out DCDA, then I would say, maybe between 15% to 20% would be total imports, not including the DCDA.

Mahesh Vyas: Any dependence on particular suppliers?

Dr. Sanjay Chaturvedi: No. For every product that we import, we have multiple suppliers.

Mahesh Vyas: Total import percentage of business, including pharma and chemicals, both?

Dr. Sanjay Chaturvedi: Maybe around 40% or so.

Mahesh Vyas: So, we are 40% dependent on imports?

Dr. Sanjay Chaturvedi: Yes.

Moderator: The next question is from the line of Niharika from Aequitas Investments. Please go ahead.

Niharika: My question is regarding ethyl acetate. The prices which were there in quarter 2 and how are they moving now? And also for the acetic acid, how are they in quarter 2 and how are you seeing it in the current scenario?

Dr. Sanjay Chaturvedi: The prices of ethyl acetate in Q2 versus Q3 have been fairly flat. And the prices of acetic acid have shown a marginal dip, but the real change happened between Q1 and Q2 and not between Q2 and Q3.

Niharika: How are you seeing the demand scenario? Because there was some con-call, they said that China is dumping a lot of ethyl acetate in Europe, and that's why the demand is going down. How are you seeing the demand in India currently?

Dr. Sanjay Chaturvedi: I'll break down the demand into 2 geographies. One is domestic and the other is outside India. In the domestic demand, there is not much disruption. We don't have too much ethyl acetate being imported from China. But clearly, in the overseas markets, the Chinese have been gaining market share, but that does not again impact us too much because traditionally, historically, IOL has not exported a lot of ethyl acetate to Europe.

Niharika: Currently, how much of ethyl acetate are we exporting or it is negligible?

Dr. Sanjay Chaturvedi: Our current exports of ethyl acetate are roughly around 20%.

Niharika: Once the capacity expansion is live, how are we seeing it to get absorbed in the domestic market?

Dr. Sanjay Chaturvedi: We are very confident that roughly 70% to 80% of that will get absorbed into the domestic market, and the balance will go to the exports of our regular export customers.

Niharika: Are there any new players coming in for ethyl acetate? And do you think the supply would get absorbed in the domestic market?

Dr. Sanjay Chaturvedi: No, we are not aware of any new players coming into ethyl acetate with scale.

Moderator: The next question is from the line of Anupam Agarwal from Lucky Investment Managers. Please go ahead.

Anupam Agarwal: Sir, you mentioned in the first participant's question about high-cost inventory in our chemicals business. Is it possible for you to quantify what percentage of margin we would have lost in that business because of the high-cost inventory?

Dr. Sanjay Chaturvedi: No, that would be unfair for me to give you an exact number of how much margin I would have gained if I did not have that inventory because that is a hypothetical question.

Anupam Agarwal: Or if maybe on an average basis, if our inventory would have remained at the same level as last year, then how much inventory or how much margin would we have made?

Dr. Sanjay Chaturvedi: It's not just the inventory issue, it is the pricing of that inventory, really, and what is the relationship of the raw material inventory versus the finished product pricing in the market. The challenge for me is not inventory management. The challenge for me is managing the price at which I sell the end product and the price at which I buy the raw material because that is done a few months in advance. It’s a timing issue more than inventory management issue. Believe me, if acetic acid was available domestically through manufacturers in India, none of the ethyl acetate manufacturers would be facing this issue.

Anupam Agarwal: Sir, you mentioned acetic acid prices were 40% down sequentially. How much is it on a Y-o-Y basis?

Dr. Sanjay Chaturvedi: On the year-to-year basis, roughly around the same, maybe 40% or so. But the thing is, these prices came down not over a period of 1 year. These prices came down over a period of weeks.

Anupam Agarwal: Sir, just a question on metformin. What is our capacity utilization? And have we seen some change in pricing on metformin?

Dr. Sanjay Chaturvedi: Metformin is one of those dynamic products where you will see change in pricing if not month on month, at least quarter on quarter, depending entirely on what is the DCDA import price. If I look at historically, these prices used to be in the domestic market below Rs. 300 a kg. And then they went up to Rs. 400 a kg, even beyond Rs. 400 a kg. Then they came down to about Rs. 330 a kg, Rs. 340 a kg levels, and they still continue to be in the Rs. 320 a kg, Rs. 330 a kg levels even now. Our asset utilization is above 90%.

Anupam Agarwal: Any plans of expanding capacity in metformin?

Dr. Sanjay Chaturvedi: No, not yet.

Anupam Agarwal: What percentage of metformin is sold in the domestic market versus exports?

Dr. Sanjay Chaturvedi: Currently, most of it is domestic for us. I would say, about maybe 10% is into the export market right now.

Anupam Agarwal: Any price differential between export and domestic market?

Dr. Sanjay Chaturvedi: Most certainly. There is a significant price differential and that's the whole reason why we filed for regulatory approvals both in the US as well as Europe. And our focus is to improve the share of our business. You asked about, am I planning to add capacity? No, I am not planning to add capacity. I am actually planning to shift the quality of customers and go more towards the regulated markets.

Anupam Agarwal: The price difference would be anywhere about 20% to 25% or higher than that?

Dr. Sanjay Chaturvedi: I would say, at least 20% depending on the customer and volume.

Anupam Agarwal: Sir, lastly, on the Capex. Are we still sticking to the Rs. 100 crore to Rs. 150 crore Capex guidance per annum?

Dr. Sanjay Chaturvedi: Yes.

Anupam Agarwal: Sir, lastly, any update on the PAP project (para-aminophenol)?

Dr. Sanjay Chaturvedi: We are making our own para-aminophenol, and the paracetamol that we make is through our captive PAPs. We have ironed through all the quality issues and there is no issue in terms of making our own PAP and making our own paracetamol from PAP.

Anupam Agarwal: Sir, what is your guidance you would be giving on the non-ibu side? What is the kind of top line you want to achieve, let's say, 2 years down the line? We are at about Rs. 500 crore in FY23. What is your sense, given the new pipeline is largely non-ibu and higher-margin products, what is your sense there?

Dr. Sanjay Chaturvedi: I would say in the next 2 years, one should expect that the non-ibuprofen portfolio will exceed the revenues from the ibuprofen portfolio.

Anupam Agarwal: Any price change in ibuprofen we have seen? Or is it still about $11 or something?

Dr. Sanjay Chaturvedi: The price is still between $11 and $12 for the export market, and it is slightly lower for the Indian market and that pricing continues to be stable.

Moderator: The next question is from the line of Gautam Gosar from Perpetuity Ventures LLP. Please go ahead.

Gautam Gosar: I have a few questions on ibuprofen. I wanted to know your market share in terms of capacity and in value terms for ibuprofen.

Dr. Sanjay Chaturvedi: I can give you the market share in capacity terms. We have roughly one-third of world market share. That gives us roughly about 33% or so of capacity and market share. Because we are also backward integrated, we are supplying some of these intermediates to some other ibuprofen manufacturers. If I add that in, I think it would be fair to say that through a combination of API and intermediates, we command maybe upwards of 50% market share.

Gautam Gosar: Sir, what would be your monthly run rate for ibuprofen currently?

Dr. Sanjay Chaturvedi: Our monthly run rate is, we are running at about 80% of capacity. So, roughly around 800 tonnes a month.

Gautam Gosar: Do we look to increase it at a monthly rate?

Dr. Sanjay Chaturvedi: We are looking to improve the run rate, but I am not looking to add capacity into ibuprofen right now.

Moderator: The next question is from the line of Chaitanya Chinmayi, an individual investor. Please go ahead.

Chaitanya Chinmayi: My first question is, the acetic acid raw material inventory which is corrected right now, for the current month or for the current quarter, our inventory which is on the higher side of what price or is it already the corrected value we have got now?

Dr. Sanjay Chaturvedi: On the high-value inventory that we had for our chemicals business is exhausted, and we are in line to have the right volume of inventory and be profitable in the chemicals business, not only for Q3 but also for Q4.

Chaitanya Chinmayi: And another one is, as you said the Capex of the 20,000 tonnes a year for ethyl acetate, may I know when it will be completed? Excuse me please if you have already answered it.

Dr. Sanjay Chaturvedi: The Capex for ethyl acetate, the plant should be up and running by the end of this financial year.

Chaitanya Chinmayi: And finally, the last one, sir. What is the overall revenue growth you are expecting for this financial year?

Dr. Sanjay Chaturvedi: For this financial year, it should be muted in the single digits. But for the next financial year, we are very confident of double-digit top line growth.

Moderator: The next follow-up is from the line of Venkat from 3Sigma Financials. Please go ahead.

Venkat: Sir, there is some energy issue in Europe, and our biggest competitor has closed 1 plant which is in Germany while he is running it in Texas. Are we seeing any dynamics in paracetamol where it has reached like $15 or something or the media information is wrong?

Dr. Sanjay Chaturvedi: Your information is right. The difference is that the competition that you are talking about, they do not make ibuprofen in Europe. The ibuprofen is actually made in the US. A plant closure in Europe does not impact that.

Venkat: None of the APIs that we are actually manufacturing has any influence on power issues in Europe. Is my understanding right?

Dr. Sanjay Chaturvedi: Not directly but indirectly they do because the power cost has gone up in India as well. If you look at Q1 versus Q2 margins for all pure-play API players and all API manufacturers require a significant amount of power, what you will see is that margins have muted or have gone down for almost all the pure-play API players. And power has a huge role to play in it.

Venkat: Sir, my second question is, when I look at our portfolio, the portfolio looks very good actually when we look at the APIs. And those are like repetitive kind of medication that we take.

When I look at the growth in our pharma business plus the inflation, it is not such a substantial increment even in our pharma business. Are we losing out some customers who are traditionally our buyers or what is happening? Because these are repetitive medicines. Most of the medicines that are in our portfolio are kind of repetitive. Are they having a kind of overstock? Can you throw some light on that, please?

Dr. Sanjay Chaturvedi: Let me take the simplest portfolio that I have, which is really ibuprofen, metformin, paracetamol and clopidogrel. In all of these molecules, my current capacity is capped. With the exception of adding some capacity in paracetamol, I really haven't added any capacity in the last 1 year. So, my way to improve the business is to actually improve the quality of the business rather than sell more volume.

Venkat: Unless you increase the capacity, you cannot basically increase the revenue in the top line. Is that what you are saying, sir?

Dr. Sanjay Chaturvedi: No. What I am saying is that without increasing capacity, I can improve the quality of the business by selling more and more into regulated markets where I have a higher price realization. So, my revenue actually goes up without addition of capacity. And my profits also go up because all the extra pricing that I get, it gets directly into my bottom line.

Venkat: Coming to capacities. One is the regulatory approvals that you are going to get. Probably you are work-in-progress and I am not going to ask you details on that. But what is the thought process on increasing the capacity of some of these medicines? In the last call, you mentioned there are some medicines which are almost like $100 as well. Do you see challenges in demand or to increase the capacity? Or do you see other challenges?

Dr. Sanjay Chaturvedi: Our bottleneck is not capacity right now. Our bottleneck is higher volumes into the regulated markets. So, our focus entirely is on improving the asset utilization and selling the higher quantity that we manufacture into regulated markets. That will improve both the top line as well as bottom line.

Venkat: But when I look at the medication, I cannot vouch about ibuprofen and metformin and paracetamol. But if you look at other medicines, these medications are expensive even in India. So, you mean to say that the formulations are having a better margin on this one compared to the API players?

Dr. Sanjay Chaturvedi: Yes, absolutely. What I was saying was that I don't want to comment on the profitability of formulators, but what I can tell you is if you look at clopidogrel or pantoprazole, the API manufacturers in these products make more money when they export to regulated markets versus selling to IP grade material in the domestic segment.

Venkat: Even gabapentin and all these also, these are like nice products actually. Firsts one is interesting actually, but at the end of the day, we need to start seeing those numbers translating and that would happen once we get the approvals. Are we looking at the US FDA also in the road map? Or how are we actually looking at it?

Dr. Sanjay Chaturvedi: Absolutely. Our plants are already USFDA approved. And we have DMF for a couple of products. We continue to file more and more DMF. And as those approvals come in along with the CEP approvals, you will see the share of our business grow both in the US as well as Europe. And that will improve both top line as well as bottom line.

Venkat: Any new molecules? You mentioned that there are some molecules in pipeline. You want to share which molecules? Are those in R&D or you want to just wait till those are actually announced?

Dr. Sanjay Chaturvedi: We will wait for this announcement, but some of the ones that we have already announced is certainly paracetamol where not only have we introduced the molecule last year, but we are also expanding capacity on that molecule as well as we filed regulatory paperwork for approvals in both the US as well as Europe.

Venkat: Again, when we look at the portfolio and look at paracetamol. Sorry for extending the conversation and I apologize to others who are waiting for the call for their turn. Sir, when you look at the portfolios, the other portfolio looks like they are like high-value and high-volume business, but paracetamol is high-volume and low-margin business. So, why are we focusing on paracetamol? I am just trying to figure out what is the strategy behind that.

Dr. Sanjay Chaturvedi: You are right, it's a low-margin business if you don't have backward integration. But if you are completely backward integrated into PAP like us, we make our own para-aminophenol. And so we don't believe this is a low-margin business.

Moderator: The next follow-up is from the line of Bezad Deboo from Systematix Group. Please go ahead.

Bezad Deboo: You said the ibuprofen capacity utilization is around 75% to 80%. What is the peak capacity utilization you can reach?

Dr. Sanjay Chaturvedi: In principle, we can reach a peak of about 95% or so.

Bezad Deboo: Can you give your shares in regulated markets and emerging markets?

Dr. Sanjay Chaturvedi: No. At this point, I can't give you my shares, but what I would like you to understand is the nature of this business is evolving and changing very rapidly. A lot of customers in India are buying regulatory grade products that they are converting into formulations and then exporting into regulated markets. In other words, what I am trying to tell you is even what is called as a domestic sale for me, not all of it is going into the Indian market as formulations. Some of it is getting exported to the US and Europe and other countries, of course.

Bezad Deboo: My last question is on ethyl acetate. What is the reason for the volatility in the ethyl acetate prices?

Dr. Sanjay Chaturvedi: The volatility is related directly to the volatility in raw material prices, where the key one is actually acetic acid. Ethanol has also seen volatility, but perhaps not to the same extent as acetic acid.

Moderator: The next follow-up is from the line of Niharika from Aequitas Investments. Please go ahead.

Niharika: My question is on the patent which has been granted for the sitagliptin process from the Indian patent office. I just wanted some more detail on it? And will we be able to get some share from other domestic players from this patent? How is it going to benefit us?

Dr. Sanjay Chaturvedi: It will benefit us because it's a novel process and a greener process. It will translate into a cost advantage. The cost advantage should translate into higher market share when we launch the product.

Niharika: When are we planning to launch the product?

Dr. Sanjay Chaturvedi: This is still under development and validation. So, I think it would be a few quarters out.

Niharika: You said that our current bottleneck is selling and percolating in regulated markets. How are we planning to do that? Are we very aggressive in filing or how is management pursuing that?

Dr. Sanjay Chaturvedi: It's a slow and steady aggression rather than going all out. And what I mean by that is if you look at historically, we filed maybe one product a year. Since last year, we have increased our filings to at least 4 products every year. And we think that at a steady state, we can do 5 to 6 product filings every year.

Niharika: And on this EBITDA for chemicals, you said that 6% to 8% is a sustainable range for chemical business. I just want to understand, considering our ROE and ROCs upwards of, say, 12% and 13%, don't you think buyback or something else makes more sense than for me to be okay with a 6% to 8% of EBITDA margin? I am just talking from the point of capital allocation perspective. I understand that there are some internal accruals, but it would have an opportunity cost.

Dr. Sanjay Chaturvedi: Sure, it will have an opportunity cost. And as I was telling earlier that buyback is one of the ways to show confidence that the management has in the business. There are multiple ways to show that confidence. One is through Capex. The other is through investment into R&D. Third could be investment into human capital. Our R&D, we have more than doubled the expenditure in the last 1 year. If you look at our Capex, this financial year will be the highest ever Capex spend that we have had. In terms of human capital also, we have spent a lot of money training and developing and making sure that our leadership - first line and the second line - is ready as well. What you are talking is a pure finance perspective. The challenge with the other things that I am talking about is it's very hard to put a dollar matrix and see what the ROI on Capex will be or what the ROI on R&D will be. But those are more long-term initiatives, and we believe that in order to build a sustainable business and a sustainability not just in terms of the environment, but sustainability in terms of business growth, in terms of business stability, in terms of the profits in the business. We believe it is important to invest in people, in technology, in R&D, and also in Capex.

Moderator: The next follow-up question is from the line of Anupam Agarwal from Lucky Investment Managers. Please go ahead.

Anupam Agarwal: Sir, my question is on the intersegment line item. We were about Rs. 25 crores to Rs. 30 crores in FY21, which is now about Rs. 115 crores in H1. What exactly is this line item? And if you could explain how we should look at the trajectory going ahead?

Dr. Sanjay Chaturvedi: The internal line item is related to isobutylbenzene, monochloroacetic acid, and acetyl chloride. This is the business where we make on the chemicals side and then do a transfer pricing to our pharma business.

Anupam Agarwal: This should be around Rs. 200 crores every year or does it also depend on the pricing?

Dr. Sanjay Chaturvedi: Yes, I think it depends on the pricing. It depends on the volume, but it will be in the Rs. 150 crores plus/minus every year.

Anupam Agarwal: Sir, just on the REACH certificate. Congratulations to you for getting the certificate. What kind of spends are we making per annum on this REACH certificates for getting approvals and product registrations in Europe and other regulated markets?

Dr. Sanjay Chaturvedi: The recertification spend is pretty modest. It is not something that is a very large number. But what it does is it opens up opportunities and doors for you to export into Europe. And if I look at today, the timing does not seem right because the Chinese have crashed the ethyl acetate prices. So, I think in the next 1 quarter or so, I would not be looking at generating any large-volume business in Europe. But I think more than the spend, what it demonstrates to customers is the intrinsic capability and the strength of the manufacturing team that is supporting the front end.

Anupam Agarwal: Sir, lastly, just trying to understand. I was going through numbers over the last 3-4 years, in fact, 15-20 quarters. Our pharma business top line has ranged between Rs. 250 crores to Rs. 300 crores. But on the other hand, our EBIT margins have drastically fallen to single digits.

You mentioned that incrementally, our pipeline is the higher-margin business which is translated to non-ibu other API business which is now accounting for about 22% but it is not really translating on the margins front. Does this signify that ibu business margins have fallen drastically to sub 15%?

Dr. Sanjay Chaturvedi: I would have 2 points you should focus on. One is, certainly, in ibuprofen because of the price decrease, there has been some fall in the profitability of the ibuprofen business. But the other point is that as we grow the non-ibuprofen business, I need to reach that asset utilization beyond a critical point for that to turn profitable. And the second part there is I also need to turn a significant portion of that business away from just the plain domestic market to get higher profitability. So, the challenge for not only for us but anyone building API business from the ground up is, first you build the manufacturing plant and your first objective is to run that plant to as high asset utilization as possible. And that typically comes from the domestic business first, where your margins are actually very low. As you parlay that volume more and more into regulated markets, that's when the profitability of that plant starts to grow.

Anupam Agarwal: Sir, 2 questions related to this. At Rs. 240 crores in H1, what is the kind of asset utilization in non-ibu business? And what is the kind of EBITDA breaking even at Rs. 240 crores?

Dr. Sanjay Chaturvedi: Asset utilization is currently in the range of 50% plus/minus. Some plants are running at 70%, some are running at slightly below 50%. And I think going forward, once that number goes above 60% overall, 65%, that is when the profit churn really starts to happen.

Anupam Agarwal: Does this mean that we are still at EBITDA negative in the non-ibu business?

Dr. Sanjay Chaturvedi: We are almost neutral now.

Moderator: The next follow-up is from the line of Mahesh Vyas from UTI Mutual Fund. Please go ahead.

Mahesh Vyas: Sir, can you take me through your chemicals business? How you have been through to the business till now and what you expect from a long-term horizon point of view, let's say, 3 to 4 years?

Dr. Sanjay Chaturvedi: In the last 3 to 4 years, I would say that my capacity - I am again focused on the primary product which is ethyl acetate that dominates my chemicals business - I do about 100,000 tonnes. If the price of ethyl acetate is Rs. 100, I'll have a Rs. 1,000 crores business. If it is Rs. 80, I'II have Rs. 800 crores top line. That is the range in which the chemicals business will operate. And what I am doing now is I just expanded that capacity by about 20%. So, next financial year, you should expect a 20% higher number in the top line from that business.

Mahesh Vyas: And what EBITDA margins you expect from here?

Dr. Sanjay Chaturvedi: That business should consistently give me around 6% to 8% EBITDA.

Moderator: Ladies and gentlemen, that was the last question for today. I now hand the conference over to Dr. Sanjay Chaturvedi from IOL Chemicals for closing comments.

Dr. Sanjay Chaturvedi: Thank you all very much for joining us today and listening to us on the second day of our quarter results season. As we discuss, the Indian economy is emerging as a green shoot amidst slowdown globally. However, the domestic pharma and specialty chemicals have their own challenges. And the companies in both these segments have their own armor to fight these battles. Here at IOLCP, we are dependent on de-risking our business. We are adding more and more APIs to our portfolio and backward integration to really increase market share and build a robust and sustainable growth trajectory.

With this, I would like to conclude the call. Thank you all, and have a nice day.

Moderator: On behalf of IOL Chemicals and Pharmaceuticals Limited, that concludes this conference. Thank you for joining us and you may now disconnect your lines.