



“Advanced Enzyme Technologies Limited Q1 FY-19 Earnings Conference Call”

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Moderator: Good day, ladies and gentlemen and a very warm welcome to the Advanced Enzyme Technologies Limited Q1 FY19 Earnings Conference Call. We have with us today on the call, Mr. Piyush Rathi - Chief Business Officer, Mr. C. L. Rathi - Managing Director, Mr. Varun Khunteta – Senior Manager Finance and Accounts, Mr. V. L. Rathi – Chairman. As a reminder, all participant lines will be in the listen-only mode. 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 ‘*’ and then ‘0’ on your touchtone phone. I am now glad to hand the conference over to Mr. Piyush Rathi. Thank you and over to you sir.

Piyush Rathi: Thank you, very good afternoon to all of you. We will like to take you through the financial highlights for this quarter. The consolidated sales are up by 38% year-on-year to 1043 million as against 756 million in last quarter Q1 FY18. The EBITDA for Q1 FY19 stands at 487 million as against 297 million in Q1 FY18, up 64%. The EBITDA margin stands at 47% this quarter as against 39% in Q1 FY18 and the net profit has risen by 91% to 312 million as against 163 million in Q1 FY18. Overall, the financials are in line with the expectations of the company and the company is on track to achieve its annual guidance. We would now like to open the call for questions.

Moderator: Thank you very much. Ladies and gentlemen, we will now begin the question and answer session. The first question is from the line of Amar Maurya from Emkay Global. Please go ahead.

Amar Maurya: I have two questions sir. Number one is what was the revenue from the Evoxx during this quarter and what was the EBITDA?

Piyush Rathi: The revenue from Evoxx was about 30 million.

Amar Maurya: Okay, so 30 million and I believe it was same quarter last year this revenue was not there, right?

Piyush Rathi: Yes, it was not consolidated last year.

Amar Maurya: Yes, okay and what was the EBITDA sir during this quarter?

Piyush Rathi: From Evoxx you mean?

Amar Maurya: Yes, Evoxx.

Piyush Rathi: Negative 25 million.

Amar Maurya: Okay, 25 million negative and sir in Q4 it was how much negative?

Piyush Rathi: Also similar.

- Amar Maurya:** Okay, so 25 million and which we are assuming that by the Q3 this will be a breakeven right at the EBITDA level also?
- Piyush Rathi:** Yes, it shall be breakeven at the EBITDA level on a standalone basis.
- Amar Maurya:** On a standalone basis because that the centers which we are consolidating and all those things that is why restructuring at the Evoxx level will lead to this, correct?
- C.L. Rathi:** We had already done the same calculation before buying the company. That until December or so we would be continue to lose money on a standalone level.
- Amar Maurya:** Correct sir.
- C.L. Rathi:** One and a half years or maybe even two, are required to bring them in line with our business.
- Amar Maurya:** And sir secondly what was the contribution for JC Bio if you can share, JC Bio's revenue and EBITDA?
- Piyush Rathi:** Revenue was 125 million.
- Amar Maurya:** Okay and what would be the EBITDA?
- Piyush Rathi:** The EBITDA was 48 million.
- Amar Maurya:** 48 million and I believe this business had also grown right because if I see the same quarter last year this was 90 million, correct?
- Piyush Rathi:** Correct.
- Amar Maurya:** And at that time what was the EBITDA sir if you have handy?
- Piyush Rathi:** 33 million in Q4 FY18.
- Amar Maurya:** Okay sir, Q1 would be what?
- Piyush Rathi:** Q1 FY18 was 19.4 million.
- Amar Maurya:** 19.4 million, so basically in this JC Bio the margin has also come up?
- Piyush Rathi:** Margin has expanded significantly in JC Bio, correct.
- Amar Maurya:** Okay so any specific reason for this sir?

- C.L. Rathi:** We put our technology now to great use in JC Bio as well. Advanced Enzymes has been a technology leader in this particular space and we have been working for last over like 30 years in this space. JC Bio was a small company and they did not have this kind of expertise, so we gave our technical expertise to improve all their numbers.
- Amar Maurya:** This question is largely to understand the US outlook because this quarter the top account has also shown a growth as well as the good part here is that the human nutraceutical non top account also started growing in a very high double digit number, so just wanted to know what is changing at our hand for this human nutraceutical segment overall as well as the US outlook of the human nutraceutical?
- V. L. Rathi:** There you have a two-part question, so let me go over the first part. If you are comparing numbers from the last year, last year the quarter was very abnormal or very abnormally low. So, having said that, that is not a very good comparison to compare. Second part is quarter-to-quarter results are never our what you call it way of business, we cannot take one quarter and make it into the similar things for the next quarters or something like that. Having said that, our nutraceutical business is very stable and growing and we see reasonable growth as usual in this market and your second question was?
- Amar Maurya:** So, basically sir knocking of the top accounts like say top two accounts or top four accounts, are we seeing now growth in the non top accounts also per se for the nutraceutical?
- V. L. Rathi:** We see the top accounts probably maturing and stabilizing or little bit less but other accounts have grown.
- Amar Maurya:** Okay, but then you don't see a large growth over here, you are saying that mid two digit number is the number which we should look, correct?
- V. L. Rathi:** Yes, that is the correct.
- Amar Maurya:** Okay sir, anything specific sir to know from the US outlook or from the overall business point of view which you are seeing is changing dramatically?
- V. L. Rathi:** Only this year we are going to expand our R&D research and development in US quite a lot and we see putting the laws of foundations for the future growth in probiotics etc.
- Amar Maurya:** Okay, so is that going to be a large expenditure of R&D over there or the guided number which is of around 25-27 crores which we are talking about. This is the part of that initiative or it is over and above that?
- V. L. Rathi:** It is going to be a substantial number, but until the plans are finalized I cannot give you some kind of ideas on it, but we are working on those things right now.

Amar Maurya: And how fast we will be able to see some fructification of the revenue from those R&D's, is it going to be immediate phenomena or how much timeframe which is required towards the R&D execution happens?

V. L. Rathi: Reasonably quick because there are several different types of R&D and there are R&Ds which are customer related R&Ds and there are R&Ds which are fundamentals like culture area things which we do here. So, each R&D is little different and this R&D will give you more often customer oriented R&D's gives you little bit faster results than the basic R&D.

Moderator: Thank you. The next question is from the line of Ashi Anand from Allegro Capital. Please go ahead.

Ashi Anand: The question is a little basic. If you are looking at general trends in the industry around human nutrition, diet, preventive, wellness, nutrition, all of these are relatively higher growth areas. However, on a human nutrition business, we kind of speak a relatively more muted growth, just trying to understand is this dynamic way we have a large top account which is growing slower which is pulling down overall growth rate so how really do we see this?

Piyush Rathi: I think the assessment that the human nutrition is not growing would be incorrect, maybe I can request Mr. V. L. Rathi to share his thoughts on how well the human nutrition business is growing especially with the US business in focus.

V. L. Rathi: You wanted to know how the human nutrition is growing? We are always adding new customers and we can see that the growth is started, taking old things to various different human nutrition areas from various different customers, some of them are small, some of them are large, but this is consistent and this will be I see a normal growth year like any other thing you have seen in the previous years.

Ashi Anand: So, we should be looking at kind of mid-teens growth right on the human nutrition side?

V. L. Rathi: We to be more conservative side, things like low teens.

Ashi Anand: And just kind of understand how exactly should we try to understand the growth, do we first need to invest in the R&D to developed products that we take to consumers or so is there an existing kind of product basket or adequate capacity to drive stronger growth when you have some acquisition business, just trying to understand how would we look at the growth?

V. L. Rathi: Our business model is not like a particular product per se, we customize the product for the day to day business. So, our customers are business-oriented people, we are trying to reach to their customer belts and it takes little time to develop with them but once they develop how they market it to the consumers depends on that their growth happens and that really translate into our growth for the larger part of it. Does it make sense?

- Ashi Anand:** Yes, absolutely. Sir the second question was around we have got different segments and in the past we have alluded to the fact that there is a margin differential with certain segments in higher margin. Just wanted to kind of understand how significant is the difference in margins across the human animal nutrition and food and nonfood processing segments?
- Piyush Rathi:** Sure, so not very different because if you look at the overall gross margin profile of the company at a consolidated level we are between 75 and 80%, very close to 80% rather, so even though we may have a notion that industrial enzyme business might be lower margin, it depends on the competitive strength of the company in each of the spaces it operates in. We generally operate in areas where we have higher competitive strength and therefore reasonable profitability in comparison also with our nutritional business. So does that answer your question?
- Ashi Anand:** Sir, you think there is a differential, but it is not very significant because you are also earning higher relatively decent margins on the industrial side, is that correct?
- Piyush Rathi:** In the industrial segments, we operate in niches again where we have relative competitive strength and therefore higher profitability.
- Ashi Anand:** Okay, excellent and just lastly can you quantify what is the revenue we getting currently from our top account?
- Piyush Rathi:** The top account this quarter contributed Rs. 164.5 million to the revenue.
- Moderator:** Thank you. The next question is from the line of Rohit Sinha from Emkay Global. Please go ahead.
- Rohit Sinha:** Just one question on the tax rate. This quarter we have tax rate of around 26%, so post that US benefit by the end of this financial year, what kind of tax rate it would be?
- Piyush Rathi:** Yes, it would be similar 26%-28% range.
- Rohit Sinha:** Okay and going forward for FY20 also in the same range, right?
- Piyush Rathi:** We should expect the same, unless there is substantial change in Indian tax rates.
- Moderator:** Thank you. Next question is from the line of Rahul Marate from Akash Ganga Investments. Please go ahead.
- Rahul Marate:** Sir I just wanted to get guidance from you like that we are seeing very good attraction in terms of the numbers in growth, so could you guide us for the next three years like the topline growth which we can see on a sustainable basis for the next three years?

- Piyush Rathi:** Rahul, it is a bit difficult to give you a three-year guidance, but we have in the recent past given a guidance of about 440 to 450 crores for FY19, with an EBITDA of 190 to 200 crores and PAT of about 110-115 crores. So we are very much on target to achieve those set of numbers.
- Rahul Marate:** Okay sir and just would want to know on the client acquisition like did we have any new clients acquired in this quarter or are we like seeing by the end of the year that we would be acquiring new clients?
- Piyush Rathi:** So, client acquisition is a normal process, although we have some churn always but this quarter the interesting thing is the top client has come down to 16%, yet our top 10 client revenue is in the same range of 44-45%. This shows that the growth in non-top account has been significant. So the overall revenue mix has become more diversified.
- Moderator:** Thank you. The next question is from the line of Ashi Anand from Allegro Capital. Please go ahead.
- Ashi Anand:** On the palm oil extraction opportunity, I just wanted to understand how large is this opportunity given the fact that we have also got a patent?
- Piyush Rathi:** We estimate the market potential to be close to a half of billion dollars, roughly \$450 to \$500 million. We expect some commercial revenues to begin in FY20, which is next financial year.
- Ashi Anand:** And how large, if competitive, would you be in this particular market, given that the market size is obviously quite large, and what kind of market share could we look at by say FY23-24?
- Piyush Rathi:** Difficult to predict, it is early days, but so far, we are only seeing one competitor and maybe there would be an oligopoly consisting say 3 or 4 players at max. The technology would definitely progress, and the innovation too would keep on happening. So we have to stay abreast and keep on being at the forefront, and that is why the R&D is very critical. And that is why some of the pieces of our R&D, especially the acquisition of Evoxx, have an important role to play, as we keep on innovating and stay at the forefront of technology. So, difficult to give market share numbers currently, but you can imagine that we would emerge with a decent market share in a duopoly or in a tri-poly situation.
- Ashi Anand:** So, would it be safe to say that 3 to 5 years from now this would be one of the larger kind of segments in terms of contribution?
- Piyush Rathi:** Yes, so this would get classified under the industrial bioprocessing segment, and yes 3 to 5 years from now, we should definitely see \$10-15 million in revenues or more. You never know, there could be exponential growth as well.
- C.L. Rathi:** It's too early right now to really start counting such numbers. We are a research driven company and always early days of new technology adoption are always challenging. Gestation is always

long. If you look at palm oil we have been investing for the last 10 odd years. Yet, the opportunity is quite large, and so we're very excited about the way this whole technology can take shape. There are huge advantages of such technologies slowly maturing over a period of time.

Ashi Anand: Sir, just to understand what our technology does, so the use of enzymes in palm oil extraction, what is it competing against? And what would the benefits be?

C. L. Rathi: Oh, very nice question. Some years back, if you tried to produce apple juice, you would get roughly about 74-75% recovery. And as they have started using enzymes today all over the world, globally the juice recovery is anywhere between 90-94%. Today, no company in the world can afford to produce apple juice without the use of enzymes and still continue to be in the market. And with this technology we are also able to offer lot of other advantages like producing apple fiber for consumption as a human food. So, these are the kinds of novelties that come out from enzymatic processing, which are very useful for human nutrition. Enzymes offer limitless potential to help the whole humanity get the best value out of the all agri-produce or all kinds of crops or all kind of extraction processes. So, this is the upcoming trend, green technology. And currently there is no such available technology to compete with enzyme technology.

Piyush Rathi: To give you a more specific answer to your question, currently the industry is using only a thermo-mechanical process.

Ashi Anand: Excellent. So, would it be fair as in what would be the use of enzymes for other oil extractions, you will obviously customize it, but is that the way to look at the potential of enzyme technology in food processing?

Piyush Rathi: Yes, several raw materials are already processed using enzymes; and the technology can be extended to many more.

Ashi Anand: Excellent. Sir, second question on Evoxx, so just wanted to understand if I am looking at it from the strategic rationale part, is there primarily access to technology or is the whole geographic kind of, the potential to target Europe, is Evoxx an important part of that?

Piyush Rathi: So, there are 4 main reasons why we acquired Evoxx and technology acquisition had a major role to play, almost to the extent of 80-90%. The first was the directed evolution platform that we have got in Evoxx. The second was the access to proprietary strains and technologies on the bacterial engineering side where we needed to improve our competencies. So, Evoxx has a reasonable competitive strength there. And the third has been the vast library of enzymes for pharma bio-catalysis industry and some business around that. And the fourth has been of course the access to the German and the European markets.

Moderator: Thank you. The next question is from the line of Ankit Kanodia from Smart Sync Services. Please go ahead.

Ankit Kanodia: Most of my questions have been answered, just one simple question. Sir, if we take a 2-3-year view what would be the 1 or 2 major risk factors which you would be right now tracking? That's it.

Piyush Rathi: I think the risk that we would be tracking is for example competition coming in some of our larger products. So, one of the key products that we have is serratiopeptidase from which we derive close to 25% of our revenues today. And any competition in that area could definitely have a major impact on the company. That's one risk area - product concentration. Client concentration risk has come down this quarter, as is already seen. The topmost client contributed only 16% vis-à-vis almost close to 25% about 2 to 3 years back. I think this is a good trend to see that overall we are not relying on a single customer or a few large customers, and rather our customer base is widening. These are the two large risk areas that we see, and we have been addressing them appropriately.

Moderator: Thank you. The next question is from the line of Dharmik Patel from ActiveAlpha Advisors. Please go ahead.

Dharmik Patel: I just have one question. Recently there was a discovery of new enzyme which consumes plastics. So, do we plan to move into this field or are you exploring presently?

Piyush Rathi: Dharmik, not at present.

Moderator: Thank you. The next question is from the line of Anshul Sehgal from Kotak Portfolio Management. Please go ahead.

Anshul Sehgal: I have 2 questions. One is that you mentioned Serratiopeptidase is about 25% of revenues. And obviously someone entering into this space can cause some amount of risk to business. How do you intend to mitigate this risk? One is that and second is that in all the products that we are present in and in those product categories, what would be the market opportunity for the company?

Piyush Rathi: Yes, let me take each question one by one. So, the first question about regarding serratiopeptidase, our strategy has been to keep a tight focus and reign on the cost structure. And we can say that we are most competitive in producing this enzyme today. And there is constant innovation, although there is hardly any competition we still continue to innovate and continue improving the margin and the productivity profile. So, that's our way of approaching and of course constantly monitoring the market for any new competition that comes in. If I come back to your second question I think that's regarding the different products and the market sizes, right?

Anshul Sehgal: That's right. What is the market opportunity for us? And in a sense what would be our market share?

- Piyush Rathi:** It's a very large product portfolio that we have starting from 68 base enzymes and probiotics and then these when we convert into products are more than 400, so it becomes very difficult to give you a product by product overview. But that's why if you look at the overall industry or segments that we focus on, the human nutrition has a market potential of around 300 million globally. And the animal nutrition is close to 900 million. And the industrial bio-processing is close to 4.5 billion.
- Anshul Sehgal:** Now of these 3 segments our presence or our key products would be a few of the entire segment. So, if you were to just break it down into our product say Serratiopeptidase is about 25% of sales and it is a significant product for us. Say for something like that how much would be the market share that we would be at?
- C.L. Rathi:** See, there are lots of things which are under development. We are present only in certain geography where currently our market penetration is not as high as compared to global levels. Also different markets are in different phases of development. For example, the nutraceutical industry is very well developed in the US, however it is in a relatively nascent stage here in India
- Anshul Sehgal:** Okay. If you permit me I will ask one more question, please. On this aspect of growth, given that many of our products, as Mr. Rathi earlier mentioned that these are customized for specific requirements. How is it that we track growth? How is it that, we know that so much will be our revenues for a particular year and thereafter? So, what mechanism do we use for that?
- Piyush Rathi:** We are always in close contact with our customers and we understand their annual demands. So, that's how we are able to project at least a year out.
- Moderator:** Thank you. The next question is from the line of Ratna Rajmohan, Individual Investor. Please go ahead.
- Ratna Rajmohan:** The recent dollar appreciation, will it have a material positive impact in your revenue and profit?
- Piyush Rathi:** Yes, certainly because if you see India revenues is 45% and global revenue which are mostly dollar denominated is about 55% for the company. So, naturally, since our revenues are reported in rupees, a rupee depreciation vis-à-vis the dollar will definitely have a positive impact for us.
- Ratna Rajmohan:** Can you quantify it in a percentage terms like you are sticking on to the same guidance of 110 to 115 crore PAT. So, with this appreciation also, you still want to stick on to that number?
- Piyush Rathi:** Yes, we would like to be conservative. That's our approach. But we may very well see a PAT in excess of 120 crores.
- Moderator:** Thank you. The next question is from the line of Rajat Goyal, Individual Investor. Please go ahead.

- Rajat Goyal:** Actually, I want to know about the debt presently on the company.
- Piyush Rathi:** Yes, as of the June quarter, June 30th the gross debt in system was 654 million and the cash on the balance sheet was 931 million.
- Rajat Goyal:** Okay, so any plan to reduce it further?
- Piyush Rathi:** Yes, the company is looking at different avenues of reducing the debt.
- Rajat Goyal:** And what about the pledged shares? Any plan to reduce that also?
- Piyush Rathi:** So, I think that question should be addressed specifically to the promoters.
- Moderator:** Thank you. As there are no further questions, I now hand the conference to Mr. Piyush Rathi for closing comments.
- Piyush Rathi:** Thank you very much for joining us today and good day to you all.
- Moderator:** Thank you. Ladies and gentlemen, on behalf of Advanced Enzyme Technologies Limited that concludes this conference call for today. Thank you for joining us. And you may now disconnect your lines.