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SEQU.NS - Sequent Scientific Limited - Special Call

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CORPORATE PARTICIPANTS

Abhishek Singhal *Sequent Scientific Limited - Head of IR*

Manish Gupta *Sequent Scientific Limited - CEO, MD & Executive Director*

Tushar P. Mistry *Sequent Scientific Limited - CFO*

CONFERENCE CALL PARTICIPANTS

Bharat Sheth *Quest Investment Advisors Pvt Ltd. - Head of Equities*

Mithun Soni

Ujwal Shah *Quest Investment Advisors Pvt Ltd. - Equity Analyst*

V.P. Rajesh *Banyan Capital Advisors LLP - Managing Partner & Portfolio Manager*

PRESENTATION

Operator

Ladies and gentlemen, good day, and welcome to Sequent Scientific Limited Corporate Update Conference Call. (Operator Instructions) Please note, this conference is being recorded.

I now hand the conference over to Mr. Abhishek Singhal. Thank you, and over to you, sir.

Abhishek Singhal - *Sequent Scientific Limited - Head of IR*

A very good morning, and thank you for joining us today for Sequent Scientific's Corporate Update Conference Call.

Today, we have with us Manish, Sequent's Managing Director; and Tushar, CFO, to discuss the corporate update around transition of promoter shareholding to Carlyle and the constitution of the new Board. I hope you've gone through our investor communication, which has been uploaded on the stock exchanges. We request you to restrict your questions around the corporate presentation shared with you.

Please note that today's discussion may be forward-looking in nature and must be viewed in relation to the risk pertaining to our business. After the end of this call, in case you have any further questions, please feel free to reach out to the Investor Relations team.

I now hand over the call to Manish to make the opening comments.

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

Thank you, Abhishek. And good morning, friends, and a very warm welcome to you all. Joining me on this call today, I have our CFO, Tushar Mistry.

I'm sure all of you are in receipt of postal ballot notice as also the corporate update deck, which is available at our website as well. This is not a business update call in that sense, and the limited purpose of this call was to update you on some of the initiatives undertaken by the new promoters, that is Carlyle, to align the interest of all the stakeholders in this journey of creating a valuable global animal health business.

Carlyle has now been on board since September, and these have been very exciting times for the whole organization as well as the management, along with the Board -- who along with the Board have been deliberately -- deliberating extensively to prepare a blueprint for providing the strategic direction and the execution tools to drive the company into the new orbit.

As already announced, Dr. Kamal Sharma and Mr. Milind Sarwate, both corporate luminaries have now joined us as independent directors. Further, Neeraj Bharadwaj, Rahul Mukim, Greg Andrews, and Dr. Fabian Kausche has also -- have also joined the Board as Carlyle nominees. While, of course, both Neeraj and Rahul bring in a lot of expertise in global scale up or financial expertise in that sense. Mr. Greg Andrews has been a business development head in one of the leading global animal health company and has both technical and commercial expertise in the developed markets. Dr. Fabian Kausche, on the other hand, has several decades of experience in biological and pharmaceutical research and development as R&D head in leading animal health companies around the globe. I'm sure that their insights and expertise would bring tremendous value to the shareholders of Sequent.

Investors who have been following the trajectory of the company since 2014, when the idea of a pure-play animal health business was conceived, will agree that the transformation of the company from a diversified pharmaceutical business to a formulation-led animal health company has been strategically calibrated one.

Today, Sequent prides itself on being amongst the top 20 global animal health companies. And the recent entry of Carlyle as the majority shareholder provides us the confidence to move to the next orbit, which may hopefully propel us to be counted amongst the global top 10 animal health companies in the world. Some of the actions are already in place to move towards this goal, including consolidating our minority interest in Turkey and Netherlands; engaging Stonehaven consulting, a specialized animal health consultant, will help us define the overall strategy of the company from a product portfolio and a market entry perspective as well as using PwC to further focus on operational excellence, which includes both supply chain as also the key operating plants in India and Spain.

Given the track record of performance, the Carlyle group as well as the Board has mandated the existing management team to continue to drive Sequent 2.0. Keeping in mind several key factors, including continuity of the current management team, attracting new talent as well as aligning employee interest with the long-term goals of the company, the Board has approved a new ESOP scheme to replace the existing one. The ESOPs are expected to be rolled out by February 2021 post shareholder approval. The accounting impact of the said ESOP issuance would range between -- somewhere between INR 160 crores to INR 185 crores, depending on the then prevailing stock price, the time value as well as the vesting period.

The Board of Directors have also approved a payment of commission to the nonexecutive directors, not exceeding 2% of the net profits of the company, again subject to shareholders' approval.

I now request the moderator to open the door for Q&A. However, before that, I would again request the participants to restrict the questions on the initiatives outlined in the presentation made available with you. And as such, we would not be in a position to comment on any of the financial or operational performance of the current quarter or year-to-date. Thank you.

QUESTIONS AND ANSWERS

Operator

Thank you very much, sir. Ladies and gentlemen, we will now begin the question-and-answer session. (Operator Instructions) We have our first question from the line of [Neelam Punjabi], an investor.

Unidentified Participant

I just wanted to know how much are we going to spend in total for the consulting by PwC and Stonehaven?

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

Yes. Thank you, Neelam. Basically, our total investment envisaged in these consulting assignments with -- between PwC and Stonehaven should be in the region of around INR 10-odd crores, spread over a period of 2 quarters because the assignments are spread over about -- between 4 and 6 months.

Operator

(Operator Instructions) We have next question from the line of Bharat Sheth from Quest Investment Advisors.

Bharat Sheth - *Quest Investment Advisors Pvt Ltd. - Head of Equities*

Manish, I mean, you said that total ESOP cost is roughly between INR 160 crores to INR 185 crores, depending on the sale price at the time of granting so -- and which will be spread over 7 years. Is that a correct understanding?

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

Largely speaking, yes. It will be -- see, there is a -- and Tushar -- I'll have Tushar to explain it more, but there is a fundamentally black shoes model that is adopted. So Tushar, if you can explain this?

Tushar P. Mistry - *Sequent Scientific Limited - CFO*

Yes. So this will be amortized over the vesting period of the options. And as you can see that there are 3 kinds of options. The first, Class A will be amortized over 5 years on a diminishing value basis. And Class B and Class C will be amortized over 7 years equally.

So what we expect is in the first year, roughly around 29% of the cost should come in the -- in year 1 itself for all those 3 classes put together.

Bharat Sheth - *Quest Investment Advisors Pvt Ltd. - Head of Equities*

That is FY '21, correct?

Tushar P. Mistry - *Sequent Scientific Limited - CFO*

FY '22. I mean, the grant will happen in -- by end of January, that is -- or in February. So for FY '21, it will be only for 2 months. A significant part of this should come in FY '22.

Bharat Sheth - *Quest Investment Advisors Pvt Ltd. - Head of Equities*

Okay. Okay. And on the second -- so it will be then the spread over, I mean, 5 years, evenly or it will be more in the, say, 29% when we are saying in -- and then we have stated that 7% in remaining years. So how just, I mean, spread will be over?

Tushar P. Mistry - *Sequent Scientific Limited - CFO*

It will taper down from 29% to...

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

So I think 29% will be the first 12 months hit.

Bharat Sheth - *Quest Investment Advisors Pvt Ltd. - Head of Equities*

Correct.

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

Yes. So which will be 2 months for -- potentially 2 months for FY '21. And -- so just from a mathematical perspective, suppose the hit is, say, INR 150 crores and 30% of that is to be taken over 12 months. So 4.5 -- INR 45 crores over 12 months. So that way, you can do the math.

Bharat Sheth - *Quest Investment Advisors Pvt Ltd. - Head of Equities*

Okay, okay. And then in addition to that also, whatever will be there for -- this is for the plan A. Plan B and C, again, will be some additional amounts may come in?

Tushar P. Mistry - *Sequent Scientific Limited - CFO*

No, this is all put together.

Bharat Sheth - *Quest Investment Advisors Pvt Ltd. - Head of Equities*

Okay. Okay. Okay. And Manish, if you just -- I mean, this PwC and Stonehaven, what will be the exactly the -- I mean, can you give some kind of a contour what were -- I mean, this consultancy, one is the growth and which are the other areas they are going to help us?

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

Yes. So I think the road map for both the consultant firms are totally separate. One is chasing growth, and one is chasing efficiency. So as far as Stonehaven is concerned, while we are having our own business plan, obviously, under the new shareholder, the objective is to be obviously a lot larger than that. So Stonehaven's mandate is to look at newer growth opportunities outside of the business plan that we already have. While PwC's mandate is more inward looking. It is to make the organization potentially more scalable to deliver those objectives because any scale up brings in complexity in execution. So their perspective would be making more efficiency or supply chain and operations-led efficiency and scale up to deliver those scaled up business plans.

Bharat Sheth - *Quest Investment Advisors Pvt Ltd. - Head of Equities*

Okay. Great. So is it fair to -- I mean, understanding that whatever new growth opportunity, but the cost escalation, I mean, apart from COGS, will not be significant. I mean, is that a fair -- I mean, where PwC will help us?

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

So PwC's efforts will be more towards making us cost-efficient as we deliver that. So certainly, at a conceptual level, your framework of question is right, that the idea is how do we scale up our margins even more than what we had originally envisaged as part of this initiative.

Operator

(Operator Instructions) We have next question from the line of Ujwal Shah from Quest Invest.

Ujwal Shah - *Quest Investment Advisors Pvt Ltd. - Equity Analyst*

Taking ahead the question from the last participant. So sir, can you point out some timelines given to that strategy that you have outlined in the presentation, by when do we plan to achieve the same? And even in terms of the services which have been taken from Stonehaven and PwC, you said it's ranging straight over 4 to 6 months. But looking at the chart, it seems these are long-term plans. So will the services be rendered again on a yearly basis to overlook the progress that we they outlined? Or how this will eventually pan out?

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

Yes. Thanks, Ujwal. Fundamentally, these are between 4 to 6 months assignments. Within it, a road map will be created. It will not be a Stonehaven road map or a PwC roadmap, it would be a jointly created road map. So it will be something that is agreed by the shareholders and also the management team from an execution perspective.

Also, simultaneously, an execution road map will also be agreed because while the strategies will be defined, execution can be a couple of years of execution. So there would be road maps agreed, a framework of monitoring those execution. So while going forward, none of these firms will be continuously engaged. However, the execution plan will be monitored by the shareholders or the Board in this case as also the management team. So it's onetime engagement. But in terms of lasting impact, I believe at least 3 to 4 years will be the road map for execution.

Operator

We have next question from the line of Mithun Soni from GeeCee Investments.

Mithun Soni

Yes. Just one question on this ESOP. How will you -- you're saying accounting, first 30% will come starting from, say, you're saying February of 2021. So like how does it go part? How much of it will flow through your P&L?

Tushar P. Mistry - *Sequent Scientific Limited - CFO*

Okay. So this cost entirely will flow through the P&L of whatever Manish explained, that the cost -- and this will all depend upon the fair value of the -- fair value as of the date of plan. Once that fair value is determined, that is the cost that needs to be captured in the P&L over the vesting period of stock options.

So we have estimated this cost to be in the range of about INR 180 -- INR 160 crores to INR 185 crores. And that will be amortized over 7 years. And the year 1, starting from February '21, should have a hit of 29%, tapering it down or going down to 7% in year 7. So it will gradually keep on coming down over a period of 7 years.

Mithun Soni

They are associated with the employee cost, right?

Tushar P. Mistry - *Sequent Scientific Limited - CFO*

Yes.

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

I think just for the benefit of the entire team, let me just reiterate some of the things about this ESOP because it's not something which is very common in Indian context.

So one is the vesting price of these ESOPs are aligned with the Carlyle entry price. So there is no discount to that. 86% is the price at which Carlyle invested in the company, and that would be the price for these ESOPs.

The ESOPs are split into 3 parts. The Class A -- all the entire ESOP scheme is performance linked. Class A ESOPs are linked to performance of retention or continuity of -- in the organization, which is spread over 5 years. Class B is linked to shareholder outcomes. So obviously, there is an expectation of certain outcomes by the majority shareholder, and linked to that only will this change -- I mean, this Class B shares will be granted or 7 years, whichever -- I mean, based on the -- whenever the change of control happens or at the end of 7 years. And the Class C is linked to individual performance, again, which will be Board determined or NRC will be conducting that.

So all are performance linked is first message. Second is the grant price is linked to Carlyle entry price and the spread is between 5 and 7 years. That will also give you the perspective of the time horizon of the new shareholders.

Mithun Soni

Perfect. Got it.

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

And one more thing which I wanted to obviously clarify while it is largely understood by all, that this is a noncash charge to P&L.

Operator

(Operator Instructions) We have next question from the line of [Rajeev Sadvidya] an investor.

Unidentified Participant

And congratulations for launching the Europe product as planned in November. Just one small question if you could just throw a light. In view of the fears of Europe situation, would there be any impact in terms of our launch, which we have done and the logistics and related?

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

Yes. Rajeev, as we had clarified that we are nearing the end of the quarter so it will not be possible for us to give a commentary or any update on the business aspect. I think that was fairly well covered in our previous conference, and we had guided to what we see for the rest of the year. So please bear with us. I will not be able to kind of clarify on this aspect.

Unidentified Participant

Okay. You can take the second, third question separately.

Operator

We have next question from the line of V.P. Rajesh from Banyan Capital.

V.P. Rajesh - *Banyan Capital Advisors LLP - Managing Partner & Portfolio Manager*

Yes. Manish, you mentioned that the goal is to get in the top 10 players. We currently are in top 20. So what is the share between the revenue of the 20th player and the 10th player?

Operator

Sir, I'm sorry to interrupt. We're not able to hear you. If you can please come in the net -- good network area or you may use the handset while asking the question, Mr. Rajesh. Could you please repeat the question again, sir?

V.P. Rajesh - *Banyan Capital Advisors LLP - Managing Partner & Portfolio Manager*

Am I audible now?

Operator

Yes, better sir. Please, go ahead.

V.P. Rajesh - *Banyan Capital Advisors LLP - Managing Partner & Portfolio Manager*

Okay. So my question is that, Manish, you mentioned in the opening remarks that the goal is to move from among the top 20 players to top 10 players. And I just wanted to know what is the revenue differentiation between being in top 20 versus being in top 10? So 20th player versus 10th player, what is the delta in that revenue?

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

Yes. So currently, our run rate -- revenue run rate is in the region of \$200 million. And I think upwards of \$500 million will get us in the top 10 as per current standing.

V.P. Rajesh - *Banyan Capital Advisors LLP - Managing Partner & Portfolio Manager*

Okay. And is the goal to accomplish that over this (technical difficulty)

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

Rajesh, we can't hear you at all. It would be better that you connect to us separately, and we can -- because these are, again, beyond the scope of the current conversation of this investor update. So we can take it offline with you. Is that okay?

V.P. Rajesh - *Banyan Capital Advisors LLP - Managing Partner & Portfolio Manager*

Yes, yes, sure. No problem.

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

Thank you, Rajesh.

Operator

Thank you very much, sir. Ladies and gentlemen, that was the last question. I would now like to hand the conference over to the management for closing comments.

Over to you, sir.

Manish Gupta - *Sequent Scientific Limited - CEO, MD & Executive Director*

Yes. Thank you all for taking time and hearing us in the -- so early in the morning. These are challenging times with the second wave or third wave now on its way. So please take care of yourself and stay safe and, of course, enjoy carefully the Christmas party as also the New Year.

Wishing you all a very Happy New Year in advance and look forward to staying in touch. Thank you all.

Operator

Thank you very much, sir. Ladies and gentlemen, on behalf of Sequent Scientific Limited, that concludes this conference call. Thank you for joining with us, and you may now disconnect your lines.

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