Conference Call transcript

23 August 2023

YEAR END RESULTS PRESENTATION

Operator
Good day, ladies and gentlemen, and welcome to Adcock Ingram's year-end results presentation. All attendees will be in listen-only mode. There will be an opportunity to ask questions when prompted. If you should need assistance during the call, please signal an operator by pressing * and then 0. Please note that this event is being recorded. I would now like to hand the conference over to the CEO, Mr Andy Hall. Please go ahead, sir.

Andy Hall
Thank you, Judith. Good morning, ladies and gentlemen. Welcome to our results webcast for the year ended 30 June 2023. We appreciate you taking time to show interest in the company. Although we're reporting a good set of results, yesterday was a very sad day for Adcock Ingram. When we established the OTC Sponsors of Brave during COVID, which effectively was a campaign established to recognise healthcare workers who were doing exceptional things during COVID and post the pandemic to recognise healthcare workers who do good work in their communities, Derek Watts came on as the ambassador of the Sponsors of Brave. And he's been with us since that campaign was started.

Unfortunately, you would have heard yesterday of the sad passing of Derek. He was an extremely good ambassador for our company and someone who epitomised bravery in all aspects of his life. At the company we extend our condolences to his wife Belinda, his children Kirsty and Ty, and all his family and loved ones. A great giant has fallen in the broadcasting industry and I think in South Africa in general, and we wish that Derek's brave soul will rest in peace.

I'm going to take you through an overview of what we consider to be a solid financial and operational performance. Once again, I think at Adcock Ingram we've been fortunate on the resilience and defensive nature of our healthcare portfolio and our team's ability to adapt to what's happening in the market at the moment, particularly with the depressed consumer and a weak Rand. According to IQVIA, the company that measures pharmaceutical market shares, Adcock Ingram has retained its top-ranked position in the private pharmaceutical market in South Africa. And they also report again at the end of June that Adcock Ingram is the biggest provider to the state in South Africa.

For the year under review, turnover improved by 5% to R9.1 billion. This was aided particularly by strong trading performances from our OTC and prescription divisions. Mix contributed 4% to the increase and included the onboarding of the E45 skincare range, which we got from a Scandinavian company called Karo Pharma. And we also had a number of new product launches in the prescription division. Organic volumes did decline by 3%, and this was mainly due to reduced demand for products used in the treatment of COVID-19. And as you will recall, we also had a much lower ARV tender award in the last adjudication. So, those volumes also went down significantly.

The organic volumes declines, though, were mostly compensated for by improved demand in the OTC business, which really recovered nicely, and the prescription private sector portfolio. We got overall price realisation out of our portfolio of 3%. The gross margin declined marginally from 35.1% to 34.9%. We think that's a pretty exceptional outcome if you take into account the weaker exchange rate – Dorette will give you the exact figures later on – the additional operating costs due to electricity and water disruptions, significant cost push from suppliers over the last year as well as wage increases. So, effectively holding that margin at 35% we thought was a very good outcome from our teams.

Operating expenses were well controlled. They increased by just 3% and that then resulted in a 6% improvement in trading profit to R1.18 billion. With the benefit of a lower tax rate, some good joint venture income and the effect of a share repurchase that we did during the year, that all translated into double digit growth in headline earnings per share and we pushed the total dividend for the year up by 17%. The HEPS was up 12%.

Just moving on to some regulatory issues, as you know, the quantum of the annual single exit price adjustment that's awarded by the Department of Health determines to a large extent the pressure on our margins in our regulated portfolio. We did receive a sub-inflation single exit price adjustment in January 2023. That was 3.28%. But since then, we've had a significant amount of interaction between the industry and the Department of Health. That eventually resulted in a top-up adjustment being granted by the minister, that top-up being 1.73%.

And we're busy with the administrative work around getting that into the portfolio. Probably it will become effective at the end of September. We welcome, of course, that top-up adjustment, but if we look at the combined annual adjustment and the top-up, it is still below our current input inflation and also below the consumer price index for the last 12 months. So, we can still expect quite a bit of margin pressure on the price regulated basket of products going forward.

Looking at the highlights of the divisions, our consumer division which competes in healthcare, personal care and home care segments of the market, mainly in analgesia, energy and dermatology, smaller portfolios in sun care, vitamins, minerals and supplements, shoe care and home care. The business is now home to four brands with revenue in excess of R200 million per annum and reported an increase in turnover of 6% during the year. The standout performance was from one of our flagship brands called BioPlus, which has shown growth in excess of 20%, and the widely used Epi-Max brand grew in double digits very close to 20%.

The division did experience significant cost push from its suppliers. A large proportion of its portfolio is imported in Dollar terms. And with the adverse impact of the weak Rand, the 6% increase in turnover yielded trading profit of just 2%. As previously reported, this division also commenced with the selling, marketing and distribution of the well-known E45 skin treatment range in January 2023, and in the six months we got revenue of just under R50 million out of that brand. There were also line extensions within the existing portfolio that added another R50 million in revenue, mainly in Epi-Max where we put some body washes, some soap, baby wipes, and lip balm into the market. We've broadened the GynaGuard and Cepacol offerings. And then Plush, our home care business, also launched some range extensions during the year. So, we've seen nice innovation from that business over the last year just to counter those volume declines.

Our OTC division, which as you will know is the market leader in pain, cough, cold and flu, digestive and allergy therapeutic categories through the pharmacy channel in South Africa. It has a market share of about 19% in Schedule 1 and Schedule 2 medicines in pharmacy. We now have three brands in that business producing revenue in excess of R200 million per annum. And we've grown another two brands this year to revenue in excess of R100 million for the year. So, a nice core portfolio in this division. We saw turnover improve there by 11%. Products like Allergex, which is the biggest brand in that division, Alcophyllex, Adco-Mayogel, and Scopex, all post a double digit ex-factory growth. The gross margin was softer than the prior year, again, mainly due to the weak currency and increases in production costs, but trading profit, not far off the revenue growth, increased by an impressive 10% to R349 million.

Our prescription division, which is the division that markets our branded and generic medicines that require scripts from doctors, also does some specialised skin care products and is the biggest ophthalmology company in the country, also promotes brands on behalf of multinational partners. They grew turnover by 2%, which I know will not look particularly impressive, but there was a solid performance from all the segments there except ARVs, where we had a big decline in the tender volumes. The performance of this business has been supported by normalisation in elective surgeries and also full healthcare practitioner room visits post-COVID-19. And they had a good year in terms of product launches.

In their branded prescription portfolio, eight of the 10 top products are in growth. And in their generic medicine portfolio, seven of the top 10 products are growing. And they've retained their fourth place ranking in the prescription market, according to our QVIA. They launched five new products during the year, including a product for breakthrough cancer pain on behalf of Teva, one of our partners, and Vimovo, a combination of a non-steroidal anti-inflammatory and proton-pumping inhibitor from Grunenthal, also one of our multinational partners. That Vimovo brand, in fact, did more than R40 million since launch. So, a good product for us. On the back of the revenue increases, some nice gross margin expansion because of less ARVs in the mix. This division grew trading profit by an exceptional 16% during the year.

Our hospital division is the leading manufacturer and supplier of critical care and hospital products in South Africa. Turnover year increased by just 2% as there was lower demand for products used in the treatment of COVID-19. The business and a number of its key suppliers also experienced production and supply chain challenges during the year and with increased production costs this led to trading profit decline of 7% in this part of the business. The South African Large Volume Parenterals Tender, where we currently have a share of about 60% expires at the end of September 2023, and we expect adjudication of that tender imminently, so we'll know what things look like there going forward.

Looking at our manufacturing and distribution facilities, at Clayville, this is our plant that does high volume oral liquids, effervescence and powders, and also eye drops, it had some operational issues during the year, including power supply challenges, some civil action in the broader Tembisa area where it's located. Nonetheless, the oral liquids facility operated in excess of 50% of capacity during the year, and the effervescence facility above 70%. And utilisation of that ophthalmic facility is steadily increasing.

We have at Wadeville a liquids facility which has shown very good improvement in throughput during the year. We've pulled in some third party manufacturing into that business. Contract manufacturing that was done on our products we're now doing internally. So, manufacturing unit output in that part of the facility doubled year on year. The oral solid dosage part of that facility has now been reconfigured for shorter runs following the low allocation in the ARV tender and capacity utilisation in that part of the factory was equivalent to the previous financial year despite the significantly reduced ARV tender volumes.

At Aeroton, where we do our intravenous drips and renal fluids, again, some production problems there, mainly around complications with electricity supply interruptions, which also have a knock-on effect onto water supply, resulted in some fairly hefty in-process product write-offs and a lot of diesel usage at that factory, but still ran at capacities in excess of 90% during the year.

Our distribution business operates in partnership with RTT, who do all our outbound logistics for us. We have a contract with them that expires at the end of February 2024. We have executed a new contract with RTT just subsequent to the year end, and that'll start running from the 1st of March 2024 for a period of 40 months. Our focus in distribution remains service levels, which were good during the year – we had a 98.5% on-time delivery – regulatory compliance, and of course, cost containment. The biggest issue there in terms of cost being what happens with the diesel price. The three major risks in our warehousing and logistics operations are that diesel price, reliable power supply and any civil unrest or industrial action which may affect the transport industry which you have seen quite commonly over the last year.

Moving on to our ESG journey, in our efforts to manage the effects of unreliable electricity supply and move towards renewable energy, we now have solar installed at five of our sites, including our Clayville manufacturing site and four of our distribution centres. Our Clayville installation that we did this year can supply up to 30% of our daytime energy usage at that factory. So, solar energy is starting to grow in our business. It made up 5% of our electricity supply over the last year. And if we include the electricity supply by our generators, we generated about 11% of our electricity during the year. We put real-time water and electricity meters in at all of our sites.

Our other environmental initiatives are focused on water harvesting. We've installed water harvesting at most of our sites now, and we are particularly focused on our waste management and reducing the waste that we send to landfill. That's improved significantly over the last year. We've also got a pilot project running. We've got a couple of electric trucks that go and collect our pallets from our customers and we're extending that pilot project as we speak.

Our transformation remains a key focus in the group. We are still a level two BEE rating as of the end of November 2022. We will have a new accreditation done at the end of November 2023, effectively based on where we ended at June. But we don't expect any significant deterioration in our rating. We've also expanded our enterprise and supplier development programme during the year and continue to invest in corporate social responsibility projects.

These CSR projects included a new fully equipped computer laboratory at a Feed My Lamb school here in Eldorado Park near Soweto. We did that with the same foundation. And we are still continuing to financially support the Smile Foundation, which does magnificent work and operations on children born with facial abnormalities. That concludes my overview of the company. Dorette will give you a detailed commentary on the financials and then we'll be happy to take questions after that.

Dorette Neethling

Thank you, Andy, and good morning ladies and gentlemen. Before I get into the details of the financial results, I would just like to mention that the annual financial statements are available on our website as well as on the SENS platform. We have also provided summary financials on our website and this investor presentation will be made available a bit later today. I will now move to the financial results which we regard as a healthy financial performance for the year, and I'll start with the income statement and just give a bit more colour to certain figures Andy already mentioned.

Revenue for the year under review increased by 4.9% to R9.1 billion. Mix contributed 4.2% and includes the onboarding of E45 from Karo Pharma, as well as the number of the new product launches in the prescription division and some line extensions in the consumer division. Overall price realisation of 3.4% was achieved. The organic volumes declined by 2.7% due to the lower demand for products used in the treatment of COVID-19, as well as the lower ARV tender sales. Much of this decline was compensated for by the strong demand in the OTC and other prescription portfolios.

Gross profit of almost R3.2 billion ended 4.2% ahead of the prior year, some slight de-leveraging from the sales increase that we've seen. The gross margin declined marginally as Andy alluded, impacted by an average increase of 9.2% in forward exchange rates for products acquired in foreign currency, a significant cost push from both local and foreign suppliers, increased production costs due to the interruptions in water and electricity supply, and wage increases of 7%. Every attempt was made to mitigate the margin compression through selling price increases in the non-regulated portfolios, increased throughput and efficiencies in the factories, and concentrating the sales mix on products with higher margins. So, in the prevailing circumstances we are very satisfied with the margins that we achieved in the business.

In a closer look at the impact of the exchange rate, we bought the following material foreign currencies during the year. $72 million at an average rate of R17.19, which represents a 12.9% weakening compared to the previous year, which was at R16.22. And €46 million at an average rate of R18.19, which represents a 3.9% weakening compared to the previous year, which was at R17.51. With approximately 60% of FECs in US Dollars and 40% in Euro, the weighted cost of our basket of all currencies weighted on actual settlements in the period was then 9.2% higher than last year. At 30 June, the group was carrying the following open FECs. $16.2 million at R18.64, which is a further weakening of 8.4% over the R17.19 we achieved in the 2023 financial year. We also carried €25.8 million at R20.30, which is an 11.6% weakening over the R18.19 achieved in the 2023 financial year.

Looking at operating expenses of just over R2 billion have been well controlled and increased only by 3.1%, below inflationary levels, and the primary drivers was increased distribution, regulatory and IT expenses. Trading profit of just short of R1.2 billion ended 6.1% higher than last year. The non-trading expenses of R45 million consist of share-based expenses of R44 million and a fair value adjustment on a long-term receivable of R1 million, leaving operating income of R1.14 billion, 7.9% above the prior year.

Net finance costs were R52 million during the year, including IFRS 16 finance costs of R30 million. This was R11 million higher than the prior year, following the increase in the average borrowing cost of 7.4% last year to 10.2% in the current year. Equity accounted earnings from joint ventures for the year improved an impressive 36.9% to just short of R120 million. National Renal Care, our JV with Netcare, showed growth of 27% and our joint venture in India with Medreich Meiji showed growth of 42.3%. Just as a note, India comprised about two-thirds of those earnings.

The effective tax rate adjusted for equity-accounted earnings is 28.3%, with non-deductible expenditure causing the increase over the statutory rate. We no longer have any minority interests as both of the companies with minorities, which were Novartis Ophthalmics and Menarini, have been dissolved. Headline earnings for the year amounted to almost R900 million, compared to the prior of R812 million, an improvement of 10.7%. The group increased its treasury shares, helped by a subsidiary, by an additional 9.2 million shares during the year at an average cost of R51.16, and this supported the increase in headline earnings per share to 561.3 cents, 11.8% above the previous year.

If we turn to the balance sheet, and starting with non-current assets, within the non-current assets, depreciation charges amounted to R189 million, which were R5 million ahead of the prior year, and include depreciation charges of R44 million on the separately disclosed right of use assets. Intangible assets, including goodwill, have a carrying value of R1.2 million and comprised of consumer, OTC, and generic trademarks and license agreements. Amortisation in the year was similar to 2022 and was R9.4 million.

In looking at the current assets, we had inventory of R2.4 billion, which is stated at the lower of cost and net realisable value. Our days in inventory increased from last year's 133 days in June to 141 days at the end of this past June. The increase from last year includes the prior price increases and the exchange rate impact. We had extended lead times on certain raw materials, so bought up some safety stock. We had new product launches as well as the onboarding of E45, and then there was items that were previously out of stock back into stock.

Our trade accounts receivables of R1.8 billion are shown net of provisions of R38 million. And despite being R270 million higher than last year, which is purely a factor of the highest sales in the towards the last quarter of the year, days and receivables are now 55 days, an improvement from the 58 days we reported last year.

Government debt makes up 12% of this trade receivable figure, and of this, 64% of the amount is due within 60 days or less. The net cash and cash equivalents amounted to R82 million, as we do disclose a cash balance of about R92 million and an overdraft balance of R10 million.

Looking at the bottom part of the balance sheet, the group had shareholders' funds of R5.4 billion in June 2023. The R87 million movement in the non-distributable reserve since June last year relates to changes in the foreign currency translation reserve of R45 million relating to the Indian JV conversion, the share based payment reserve increase by R35 million and the cash flow hedge accounting reserve by R5 million. And then there was some smallish year end pre-value revaluations on the post-retirement medical aid and investments.

Turning to the segmental information and starting with the consumer division, consumer turnover of R1.66 billion ended 5.9% above the prior year. The increase in their turnover was supported by an average selling price increase of 6.9% and a mix benefit of 5% due to product extensions in Epi-Max, Cepacol, GynaGuard, and Plush, and the onboarding of the E45 skincare product range. Organic volumes declined by 6% due to the lower demand for Panado, which benefited from COVID-19 vaccination campaign in the prior year. The lower volumes are also an indication of pressure on consumers' wallets.

The gross margin ended well below that of the prior year as the full impact of the significant cost pushes from suppliers, as well as the weaker exchange rate – this division was mainly impacted by the move in the US Dollar – could not be fully compensated for by the selling price increases. Operating expenses were very well controlled and ended below the prior year due to savings in discretionary expenses and curtailed marketing expenditure marketing expenditure in an attempt to compensate for the pressure on the gross margin. As a result, trading profit ended on R357 million, 1.6% ahead of the prior year, a performance which we regard as commendable.

Moving to the OTC business, the turnover of just under R2.3 billion, ended a very healthy 10.8% above the prior year due to strong sales performances from the pain, cough and cold and allergy portfolios in the first half and the last quarter of the financial year. Volumes improved by 5.1% with major brands like Allergex, Alcophyllex, Adco-Mayogel and Scopex, continuing to show good growth. Average price realisation in this business was excellent at 5.7%.

The gross margin ended below that of the prior year and was adversely impacted by the weakening of the Rand as well as increased API costs and increased production costs during water and electricity disruptions. Operating expenditure is pretty much flat compared to last year, and they also curtailed some marketing expenditure following the pressure on their gross margin. As a result, trading profit of almost R350 million ended 9.6% higher than the prior year, and we think that's a very good achievement under the circumstances.

In looking at prescription, where sales of just under R3.3 billion ended 2.1% ahead of the prior year, mix contributed 8.6% with several new product launches, as Andy mentioned earlier. Organic volumes declined by 7.8% attributed to the loss of the ARV tenders and the average price increase that this division realised was only 1.2%. The gross margin improved since last year and it was impacted by this beneficial sales mix with a lower proportion of low margin ARV tender sales. As a result, trading profit of R320 million ended at a very impressive 15.8% ahead of the prior year.

Lastly, our hospital division. Sales of R1.9 billion ended 2.4% above the prior year as this division was impacted by local and international supply and production challenges and the reduced demand for COVID-19 related products. A price increase of 1.9% was realised with volumes and mix contributing to the balance of the increase.

The gross margin ended below the prior year with the adverse impact from the exchange rate. So, this division is mainly impacted by the Euro rate, which was a little bit better than the depreciation of the Dollar rate. And they also have seen higher production costs, but those were partly compensated for by the beneficial sales mix of higher private market sales. As a result, trading profit declined by 7.4% to R152 million. Thank you ladies and gentlemen. That concludes my part of the presentation and I will hand back to Judith, the operator and we welcome any questions.

Operator
Thank you very much ma'am. Ladies and gentlemen, for the benefit of the participants who have joined via the telephone lines, if you would like to ask a question, please press * and then 1 on your telephone keypad or the keypad on your screen. If you decide to withdraw the question, please press * then 2 to exit the question queue. For the benefit of the participants who have connected via the webcast, you are welcome to pose your questions in the question box provided on your screen. At this stage we have no questions on the telephone lines. I will now hand over to Dorette Neethling for questions on the webcast.

Dorette Neethling
Thank you Judith. I'll start with a question from Grant Morris from ClucasGray. Grant, if you don't mind, I'm going to maybe combine it with a question from James Corkin from Steyn Capital Management. So, there are actually two questions. Andy, the first one with regards to the top up single exit price adjustment of 1.73%. So, Grant is asking what brought this about? What is the industry lobbying about? And what is the approach going forward given that the SEP calculation still seems to be far off from the actual formula calculation? So, maybe if you deal with that, I'll give you the share buyback question after that.

Andy Hall
Thanks, Dorette. Hi Grant, James. Look, there's no question that that 3.28% increase we got at the beginning of the calendar year was significantly below the input cost inflation for the industry. And if you recall at the time, effectively that's when the Rand had fallen out of bed. And there was going to be and was significant pressure on margins not only at Adcock Ingram but you can assume in any part of the pharmaceutical industry that imports product, which is everybody.

Through our pharmaceutical task group, which is an industry association which represents four of the smaller industry associations in the country, we are part of an association called PHARMISA, which represents local manufacturers. We've had extensive interactions with the pricing committee at the Department of Health, the

Director General at the Department of Health, as well as the Minister, and eventually managed to persuade those forums that some sort of adjustment on top of the 3.28% was necessary.

And this is not only a margin thing from year to year. This is about making sure that we protect the local pharmaceutical manufacturing industry and have a sustainable industry in South Africa. So, I think the Minister was gracious. He heard the arguments and I think acted in the best interest of the local pharmaceutical manufacturing sector in terms of sustainability. So, we felt he did the right thing.

Going forward, in fact, PTG will be making a submission to the pricing committee before the end of this month, because we are allowed to make reference to the formula that's in the regulations. That formula says 70% CPI, 15% Rand-Dollar, and 15% Rand-Euro. So, we will make reference to that formula. We will also make reference to CPI, which is running at about 7% if you look at the average time period for the last year. And then effectively it's in the hands of the pricing committee relative to whatever recommendation they might give to the Minister. But at the end of the day, the full discretion on the SEP price increase lies with the Minister.

Dorette Neethling

Thank you Andy. Then the questions with regards to the share buyback is firstly, confirm that the status of the current approval is complete, which I can confirm. Will a further programme be considered? And then linking on to that, James asks if it's our intention to cancel the almost 17 million treasury shares we have bought and continue buying shares, and would we use debt to do that?

Andy Hall

Look, on the share buyback we have completed the mandate that we got from shareholders in November 2022, so there's nothing that we can do in the market at the moment. We will be going at the AGM again and asking for a buyback authority from shareholders. And I can tell you that our controlling shareholder is supportive of buybacks and our significant minority shareholders in general are supportive of buybacks, although some of them do raise liquidity concerns, which obviously we try and take into account in terms of the size of the mandate that we ask for.

So, we will be back in the market after November, depending obviously on the price at which the share is trading. At the moment, as you see, we have no debt on the balance sheet, but we have about R1.5 billion worth of approved facilities at the moment. So, if the share price relative to the borrowing costs makes sense, then there's no reason why you wouldn't see debt on the balance sheet. But we're not specifically raising funds to buy back shares.

Dorette Neethling

Thank you, Andy. There is a question from Zintle Twala from Steyn Capital, saying, could you please explain why the receivables grew by 13% where there's a 5% growth in sales. Then I'll deal with that. So, our receivables are actually a factor of the sales in the last two months. As I mentioned, our debtors days did decrease, which is an indication that we had very robust sales towards the start of the winter season. I think we all knew in the market that we had seen a bit of an earlier winter. In the prior year, the winter was a bit lighter and I think we only saw more robust sales on the winter products starting in July. So, in June and then July, whilst this year it was more starting April, May and June. So, it's really just a seasonal impact. Then Nellie Brand-Jonker. Nellie asked, are the volumes of Panado sold less than before the pandemic?

Andy Hall

Hi, Nellie. So, Panado volumes are effectively at the level that they were pre-pandemic. So, we had a big spike on Panado sales in the previous fiscal year when a lot of health care practitioners were recommending Panado when people got their vaccinations to help them with the side effects. So, effectively, we're back to where we were. We haven't gone backwards.

Dorette Neethling

Then there's a question from 361 Asset Management. Operating expenses have been controlled exceptionally well. Maybe talk a little about how you managed to achieve this in the context of so many inflationary pressures.

Andy Hall

Yeah, look, 3% opex control we think is good. So, the major push in opex this year came on the distribution costs because of the diesel price increase, regulatory costs which continue to increase in the industry, so that's something that we all have to learn to live with. And then we've done quite a bit of IT work this last year, including on cyber security and the like. Where we've held back spend is on what we call the discretionary spend of in-store promotions, those types of things that lie in selling expenses, and then our above-the-line marketing spend we've also managed to hold back. But going forward, I think we need to be investing again in our above-the-line marketing campaigns. So, I think it would be difficult to show you a sub-inflation increase in opex in the year going forward.

Dorette Neethling

Thank you Andy. So, Luyanda from Nedbank, I assume that also answers your question on what the sustainable marketing expenditure levels are given that we have cut this cost. So, I assume that is answered there as well. Then Patsy from All Weather Capital. Hi Andy. Can you please unpack the increase in replacement capex? So, I can maybe get two that, Patsy. In certain of our plants, we are obliged to do some regulatory upgrades that are necessary for SAHPRA accreditation. So, some of those products, especially at the critical care plant, have started in the current year and we've already committed to that spend going forward. We've also seen in our distribution facilities that we have to do some regulatory improvements with regards to our HVAC system across our bigger facilities. So, both of those actually contributed to the increase in the replacement capex.

Let me just see, Nick De Vos from Centaur. Nick asks if we can discuss the India JV in a bit more detail, as it's becoming a more meaningful number on the bottom line.

Andy Hall

Yeah, Nick, we've had a joint venture in India. It's effectively just a contract manufacturing company. We've had that joint venture for around about 15 years now. So that business does most of our tablet and capsule manufacture, aside from tablets and capsules that we receive from our multinational partners. And then it also does contract manufacturing on behalf of some companies in Europe, some other companies here, and other companies in Australia. The main reason for producing in India is the cost of capital there is lower, capital equipment is lower, and the cost of skilled labour is lower. So, there tends to be a financial reason for manufacturing over there. We've recently put up another factory there within that JV. So, outside of the tablets and capsules, this facility will be doing effervescence and some additional other oral solid dosage forms. It's just received Indian regulatory approval. It's just had its SAHPRA inspection, so we are waiting for the SAHPRA report to see if that facility gets issued with a license or not. So, that's effectively how that operation runs. We have a 49.9% share. We don't have any managerial control in the business. That's all done by our Indian partner.

Dorette Neethling
Thanks Andy. Then Warren from Bateleur. If we can comment on any significant changes in the shareholding register, particularly if any changes in the offshore shareholding. So, Warren, what I can tell you, and Andy can maybe add to that, is that in the previous financial year, 6% of our shares were held outside of South Africa, and in the past year it's 5.8%. So, I don't know if there's a movement within the shareholders, but there isn't a big uptick from the country itself or outside of South Africa.

Then we have a question from Eswee Bothma from Oyster Catcher Investments asking what percentage of our portfolio now consists of SEP regulated products?

Andy Hall
Eswee, hi. So, in this current set of financial results, it's 57% SEP based and obviously 43% non-SEP.

Dorette Neethling
Thanks Andy. And then we have Geena Kopping from Allan Gray that wants to split off their SEP products by segment. I can maybe help with that as well. So, Geena, if we look at our starters consumer, they are predominantly non-SEP. They have a very small portfolio of SEP, only the stronger Panado or bigger formulations of Panado, stronger formulations. Then in OTC, about two thirds are SEP and a third non-SEP. In the prescription division, it’s about 80% SEP and 20% non-SEP. Just a reminder that that division has all the instruments and the ophthalmology as well as dermatology products in it. And the hospital business is very much 50/50. It seems like there are no further questions. Let me just make sure. Yeah, that is all from my side. There seems to be, Judith, one that came back on the Choruscall from Charles Bowles from Titanium Capital. We are happy to take that now.

Operator
Thank you very much, ma'am. Charles Bowles of Titanium Capital. Please go ahead.

Charles Bowles
Thanks. Thanks Andy, Dorette. A good set of results. I had a couple of questions if I could just shoot through them quickly. You say that ARVs is about 8% of prescription turnover. If you were to lose that, how big a factor would that be in terms of factory under recoveries and sustainability. How big an impact would that be?

Andy Hall

Yeah, Charles, good morning. It's not a big impact anymore, because we've reconfigured that Wadeville facility to do other oral solid dosage forms. We do some Allergex there, some Panado, and we're bringing back some Myprodol, some Gen-Payne, some Adco-Dol production into that factory. So, on the tablets and capsules not a big problem for us. And the triple combination that we sell into the private sector we actually get from an Indian partner, so we import that in any event. We do some liquids on the tender but we've brought in a large amount of other liquids into the factory now from a contract manufacturer. So again, I don't think this will have a significant impact on the factory, but we'll still keep servicing the private sector. It's really the government sector where we lost a huge chunk of business.

Charles Bowles

Got you. On BioPlus, it's a curveball question. I would have thought with the proliferation of energy drinks, which would seem to be a substitute or an alternative to BioPlus, that might have pressured BioPlus and yet it's still growing quite strongly. Maybe just some understanding of that.

Andy Hall

Yeah, you should come and get a job here in marketing. My people keep telling me how BioPlus drinks are going to do so well in the market. So, look, the drinks are a very small component of the BioPlus brand. So, we don't go up against the real big guys like Red Bull and Monster and those guys. So, it's very much just a convenience factor of where BioPlus drinks can be available. They are a very small part of the almost R300 million of BioPlus. The part of BioPlus that's really growing are these, what we would call convenient formulations. If you go into a forecourt store or a point of sale, you often see these Bioplus sachets, which people can take on the run. And that's effectively just the Bioplus syrup you used to find in bottles, now in a much more convenient form. So, those are the ones that are the formulation that's causing the growth in that brand.

Charles Bowles

I'm so little surprised that somebody goes into a forecourt, where they might have bought a BioPlus before, they now could buy an energy drink and it gives the same caffeine or kind of energy kick. I'm interested that it's continued to grow.

Andy Hall

Yeah, look, you know, BioPlus has huge brand equity as you know, particularly amongst youngsters when they study, varsity students when they study. So, the brand equity kind of remains. And don't forget, if you're selling a sachet of BioPlus, there's a huge price differential between buying a can of expensive drink and buying a BioPlus sachet. So, that also, I think, helps. And then, during COVID-19, we didn't sell a lot of BioPlus because effectively people weren't out and about. Whereas now people are out and about, they come home from a party, whatever it might be, and Bioplus is one of the go-tos.

Charles Bowles

That's useful, thank you. Codeine, is there any regulatory still on the radar or has that gone quieter? Any issues there to think about?

Andy Hall
Yeah, there are still issues to think about there. As you know, SAHRPA has been looking at the scheduling status of codeine for a few years now. The focus turned in the last year towards the use of codeine in patients under the age of 12. So, the industry had to submit information to SARPA to support the use of codeine in children under the age of 12. There is not a lot of good clinical data to support the use of codeine in children. So, SARPRA has now asked the industry to provide periodic safety updates in case anything goes wrong with administering codeine to children. And the industry is now doing that. But that's been the only part of the codeine focus over the last year.

Charles Bowles
Am I reading it correctly that it's still leaning towards ensuring responsible dispensing rather than banning. Is that a fair assessment?

Andy Hall
Look, one never knows what a regulator is going to do, because they have to act independently. But certainly, from an industry perspective, we believe that if there is responsible sale of codeine, responsible recording of who purchases the codeine, then it can be properly controlled and be given to people who need it for the right conditions. So, we will continue to support that. At Adcock Ingram we restrict our sales now to only certain big corporate customers because we know they've got the right controls in place to sell the products. I'm talking particularly of the cough syrup. And we are also still working on what's called the Codeine Care Initiative where we effectively are educating and trying to help pharmacists into making sure that there's responsible sale of these products.

Charles Bowles
Got you. Sorry, just two other questions if I may. The first one is your Indian joint venture, you answered that that's useful. I see it has got a carrying value of R471 million, so it is quite meaningful. Is that locked in in future? In other words, they are a contract manufacturer. It’s a good partnership. You would never have a reason to exit or realise that. Or does that lock you into that manufacturer? Could you ever exit that investment if you had to? Or is that not a consideration?

Andy Hall
Charles, we can exit it, although I think it would be unlikely. So, they do a good job on quality, they do a good job on price, and they do a good job on service. So, I think we'd be unlikely to ever liquidate that investment, but certainly we could. The benefit of being a shareholder of course is as a customer of that factory, we get treated well. So, I think it would be unlikely we consider exiting that unless supply chain issues go completely awry in India. In other words, that getting our hands on certain products with certain active ingredients in India becomes a problem. But we try and mitigate that by making sure that we can at least manufacture the products here that we manufacture in India, albeit on much lower scale.

Charles Bowles

Got you. And just linked to that, you had an unusual shareholder that popped up on your register, Natco, which seems to be controlled by a business out of India. Is there any link to your joint venture partner there, or is it a completely separate party?

Andy Hall
Natco is an Indian pharmaceutical company. I think they have operations outside of India as well. But they have no relationship with our contract manufacturer, and we have no commercial relationship with them.

Charles Bowles
Got you and my last question if I may. You alluded to products that are growing. And one of the questions or concerns I suppose has been with the Adcock portfolio is you've got older molecule type formulations that might be dated or become more competitive. How do you monitor what portion of your portfolio is in growth and what is at risk of becoming more commoditised, if that makes sense?

Andy Hall
Yeah, no, it does make sense. So, the data that we get from IQVIA, which is the company that measures the pharmaceutical industry, and another company called Circana [?], which does the FMCG sector, that goes all the way down to product level and in fact down to regional level. So, you can see in every part of the country how well you're doing. What one tends to find is that in the generic space, particularly prescription generics, there these brands do get commoditised over time. And in fact, we discontinued three generic products in the last year because we simply can't make money out of them given the proliferation of people in the market selling those products.

But if you stick to big brands, and I don't mean big, I just mean in terms of equity, not necessarily in terms of size in South Africa, those products are difficult to commoditise. So, if you think of a brand like Panado, there are dozens of Panado generics out on the market, including good brands that other companies sell. But yet the brand equity is there because there's a trust in the brand. So, the real issue is to get the brand reinforced in the minds of the healthcare practitioner and the consumer. And then you can still get your price and get your brand equity.

Charles Bowles
This is going to sound like a completely non-pharmaceutical comment, but when you look at a product like Panado and you think paracetamol is paracetamol, kind of more or less. I'm being a bit simplistic, but it's interesting that a fairly standard product has that much brand equity, but it seems to.

Andy Hall
Yeah, it is interesting. But it's not only a factor of the brand. Panado is effectively Panadol in the UK, so it's effectively the same formulation. But if you go and buy half a dozen paracetamol products off the shelf in any pharmacy or Shoprite or wherever you might go and open them, you'll see that these things are pressed differently, so in other words in the tableting machine. Some of them start giving off a powder, so they don't stay together as well as they should. Some of them are more difficult to swallow because our product is

polished. So, there is a reason why people would go to a brand like Panado. It looks better, it swallows better, and it's trusted. It works.

Charles Bowles

I got you. Thanks so much for all the help, and again, well done on the results. Good set of results.

Andy Hall

Thanks, Charles. Appreciate it.

Operator

Thank you. We have no further questions on the telephone lines.

Andy Hall

Judith, thank you. I think we may be done. Dorette.

Dorette Neethling

There is one more question. Sorry, Andy, just before lunchtime. Actually, to Richard from Protea Capital Management. So, your question was answered on the Natco investment that you also raised. And then we had the last question from Geena from Allan Gray. So, two questions, are there any acquisitions planned for the next year? And do we have any further thoughts on the development of NHI and the impact on the company? And with that we will conclude. Thanks, Judith.

Andy Hall

Okay, thanks Gina. Yeah, look, in terms of acquisitions we are still looking where we can to bolster our non-price regulated portfolio, so effectively trying to put products into our consumer division. Mainly we are looking at personal care and home care at the moment. There's nothing on the table at the moment, but certainly we will continue to search in the private company sector of the market over the next year. And then on NHI, we are obviously involved with discussion of the best of the private sector in terms of making representation to government on how NHI can be rolled out.

As a company, Adcock Ingram remains in favour of universal health care coverage. We believe that everyone has a right to healthcare. We don't believe the impact on pharmaceuticals is as material as it may be on the other sectors of the private market. So we are, I don't want to say going with the flow, but we are giving input and watching where we might end up. But we do believe that there are significant questions to be asked around how NHI will be funded, whether the public sector infrastructure can cope with NHI, and also on the ability of people to access insurance outside of NHI. And those are the sorts of issues we are making representation to government on in collaboration with all private sector players. Judith, thank you. We appreciate everyone dialling in. We wish everyone a good day and thanks also for your very able assistance.

Operator

Thank you very much, sir. Ladies and gentlemen that concludes today's event. Thank you for joining us and you may now disconnect your lines.

END OF TRANSCRIPT