Interview with Maurizio Silvestri, President & CEO, Euticals Group

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After a long experience at BMS, you are since 2002 at the head of Euticals- a well established group consisting of four entities (Euticals, Ambrosia, Prochisa and Pro.Bio.Sint), each of them developing and producing Active Pharmaceutical Ingredients (APIs) by different processes. To begin, could you give us an overview of the role of each entity together with its contribution to resources and growth?

To be precise, Prochisa and Pro Bio Sint have merged on October, 31st, 2008- transforming Euticals Group into one single legal entity with four manufacturing Units. Euticals S.p.a's site in Lodi is mainly focused on manufacturing generics in the gastrointestinal, CNS and oncology areas. Approval from the FDA allows the 20+ different types of chemical entities produced in the plant to be sold worldwide, therefore accounting for 50% of the group's 50 million Euros turnover (2008 data).In the smaller Rozzano Manufacturing Unit are located the R&D centre and the production of an important antibacterial agent- which generates 10% of the total turnover.The Pro.Bio.Sint, now called Varese Manufacturing Unit, traditionally involved in RNA derivatives, is slightly moving its focus towards oncologic injectables, and exploring the biotech field. In addition, following the recent FDA approval of the plant, a custom fermentation project was launched with a major US group. These activities contribute to 20% of the turnover.Prochisa, now Casaletto Lodigiano Manufacturing Unit, developed throughout the years a deep knowledge in difficult chemistry, enabling it to carry the most challenging reactions of Eutical's fully integrated manufacturing cycle.

20% of the group’s turnover is generated by this site.

What would you highlight as the main milestones and achievements since you took the reins of the company?

The centralization of all services has been a major achievement, which enabled the company to improve its effectiveness and reduce its operating costs with one single unit managing all the activities ranging from purchasing to sales, including administration, human resources and engineering. The Lodi manufacturing site now centralizes Euticals’ corporate activities like sales, marketing, purchasing, administration, Human Resources, Engineering, EHS, IT and General Management. However, it is worth mentioning that self-standing Quality Assurance Units have been maintained in each plant, in order to ensure the best level of quality. Getting the recent FDA approval for Rozzano and Varese– while Lodi used to be the only FDA authorized facility- was another main milestone. The three plants recently received and passed positively FDA inspections, showing that Euticals is increasingly focusing on quality as the most strategic way to make the difference.In addition, a lot of efforts have been recently dedicated to customer service. A new “supply chain manager” function has been created, which is responsible of selling and managing the existing product portfolio and overviews all the activities from purchasing to sales. A business development manager has also been appointed, coming from the chemistry discovery department of another group. This highly skilled talent therefore changed his working stile and business area- as in the API business, technical knowledge is as important as selling skills, and there is a need to balance both. As a last strategic evolution, Euticals strengthened in the past years its focus on the most promising foreign markets. The group started looking at Eastern Europe three years ago, and this region now represents 5 to 7% of the total turnover.As a result of these successful changes, Euticals’ turnover jumped from Euros 34 to 53 million between 2004 and 2008- in an environment which is growing at lower rate. And surely the most recent milestone has been in December 2008, when the Italo-Chinese private equity fund Mandarin Capital Partners bought the vast majority of Euticals’ shares from the Carinelli family. In a context when leverage buy-out processes are made even more difficult than usual due to restrictive credit conditions, which strategy enabled

Mandarin Capital Partners and Euticals to attract enough financings to successfully lead such a significant operation?

In the recent years, Euticals has built a solid platform of products and clients starting from a significant initial portfolio coming from decades of presence in the API market. The growth has been sustained by recent FDA approvals including one Paragraph IV, and a promising pipeline of new generic APIs is creating the condition for boosting further revenues and profitability. In

addition an accurate cost control and a prudent management of investments targeting principally quality, environment and safety, have made Euticals attractive for Institutional Investors. An additional common characteristic of Euticals and Mandarin is the proactive analysis of the opportunities for synergies worldwide with a special attention to China in term of end market, source of technologies and low cost manufacturing capabilities.

What does this operation says about Euticals ambitions in the Chinese market, and what will be the guidelines of the future international strategy?

Euticals is present with its products in China since many years, has a good reputation as reliable and consistent supplier, and buys raw materials from China. Cooperation and technologies exchange are already in place with few companies. Building on this solid base, further strategic decisions will be orientated towards re-enforcement in the Chinese market. In addition, appropriate combinations will certainly contribute to develop Euticals as a more important global player in the chemical pharmaceutical context. Beyond the presence in the US, Europe, and India through commercial agents, Euticals is constantly looking at new international opportunities, such as in Eastern Europe and Russia where several products have been registered thanks to short approval processes. The group’s four entities, collaborating to cover all the steps of API production, managed to fuel the company’s growth even in more challenging times.

As Italy has been facing for the past six years increasing competition coming from emerging markets- namely India and China- how would you describe the Italian environment for API production, and the current state of the competition with these markets?

The few last years were very dark for the Italian API industry. The first reason for that was the specific patent law that used to be applied in the country. This issue has been resolved thanks to Aschimfarma’s hard work towards the implementation of a new regulation in 2005, enabling Italy to be at the same level than other European countries in terms of patent protection. The second restrictive factor is related to Good Manufacturing Practices (GMP). Whereas companies operating in regulated markets have to get a GMP certificate delivered by local authorities before being able to start their activities, it is still not the case for other countries. Aschimfarma presented this issue to the European Community through the “Written Declaration on Active Pharmaceutical Ingredients” in 2006- the final goal being the implementation of a regulatory directive at the European level, stating that any company intending to sell APIs in Europe shall be inspected by a European authority who would certify its compliance to GMP. Only then, barriers will be at the same level for everyone and competition will be fair. As you said, the main competitive advantages of Italy are the quality and reliability of its products – surely Italy still exporting 85% of its production

means that the country is still competitive price-wise in terms of quality.

What is your strategy to ensure that you can provide quality products that meet your customer’s requirements?

The first important step is to get the Italian authorities’ approval, which can be a long process- but hopefully time frames will be reduced with the introduction of more resources in AIFA, as expectation is that business and regulatory processes should go at the same speed.FDA approval is also crucial in a context when the US remains Euticals’ main international market, accounting for 30-40% of the turnover- even if future growth will come from a strengthened commercial presence in Eastern Europe, India and China. By selling products in India and China on a regular basis, we can perceive changes in the balance between price and quality. Firstly, cost structures evolve in two different directions- while prices are decreasing or not increasing significantly in Italy, they are going up in emerging markets. And in addition, whereas significant price differences used to be appealing for the industry, most laboratories are now realizing that buying at lower prices often means compromising quality, which could involve damages generating higher costs than the initial savings. As a result, companies are increasingly trying to incorporate the value of quality, consistency and business stability in their evaluation of APIs prices.

Aside from quality, which other competitive advantages of Italian APIs could you highlight?

Italy knows the business. The country has a long tradition of knowledge in the API field, which enabled producers to know exactly how and when things should be done, and to anticipate market trends in order to offer the customers the possibility to be the first entrants in the market- which is critical to succeed in the generics business. On the other hand, Italian producers are conscious that price remains an important topic. It has been particularly true in 2007 and part of 2008, when the exchange rates were very unfavourable to the industry, while there was no room for price increase. But Euticals has been able to face this challenge by balancing the prices, focusing on the launch of niche products as well as the revitalization of old molecules, still maintaining a steady focus on technology expertise in some specific areas such as Pyridin production. This strategy enabled the group not only to survive, but to grow and prosper even in the midst of a difficult context. As a result, 2007 has been a good year and 2008 the best year ever. Maintaining a focus on technology expertise surely requires long term investments for Euticals in terms of research, development and production processes.

Could you describe the rationale behind your investment policy?

In times when European regulations are getting stricter, investment is compulsory to constantly adapt to the new framework. Such investments might not seem productive at first glance- but I am personally convinced that the future of the chemical industry will have to follow certain universal rules, which will eventually be applied even in India and China. It is a matter of years, but overall nobody can escape from respecting the environment and workers safety. The other line of Euticals' investment policy is targeting special technologies, looking at "de-bottlenecking" specific issues in our production plants as well as developing expertise new focus areas such as oncology.Of course, the group is also seeking to develop new co-operations, especially in the R&D field where, in addition to the in-house resources, processes are developed together with Indian and Chinese companies. At a later stage, manufacturing agreements will also be considered, but on a smaller scale in order not to spread Euticals' know how too quickly. Overall, the first target to develop partnerships will be China. Even though India will always remain a main player in the API field, I personally see China as a more stable country, which is also able to improve its business structures and general infra-structures at an amazing speed.

What will make Euticals a partner of choice for future third-part manufacturing agreements?

Firstly, Euticals' manufacturing plants are able to offer quality products at a lower cost.In addition, the group is looking to expand its product portfolio in areas in which it is not present yet and sees some room to grow. And finally, new works on final dosage forms are currently in the way to be implemented . A clinical trial has been launched with a Chinese partner, to work on a formulation aimed at future patent protection. The whole industry is now aware that APIs have to be protected by being integrated into dosage forms. The challenge is to select the best partnerships and the most promising category of products. In this regard, Euticals sees injectables as an adequate high technology formulation and oncology as the most strategic therapeutic area where we could value our expertise.

To which extent will R&D activities contribute to the development of these new niche products as well as the improvement of the existing portfolio?

R&D investments are, of course, critical, but have to be carried out in a careful way. As a European chemist is five times as expensive as an Indian one, costs are high and projects have to be selected cautiously. Euticals dedicates 5% of its turnover to R&D, which resulted in 2008 in the development of 10 new products. Such a great performance might not be sustainable each year- but it says a lot about the company's expertise, which is a main asset for developing partnerships. Maintaining its focus on R&D will surely serve the group's strategy to bet on optimizing the resources more than expanding the capacity, and on external growth more than organic

development. Overall, the main driver of growth for any company is its human capital.

What is your strategy to attract and retain the best talents?

Euticals' management stile has changed a lot over the last four years, increasing the focus on teams' motivation- even though reaching excellence in this field requires a lot of work.A main initiative is to increasingly involve the personnel in the company's results, in order to avoid having managers who are only focused on their specific area without having a global picture of the strategy. For this reason, the exact results are communicated monthly to all the key employees so that they can assess their work and correct eventual mistakes at a very early stage. And as each manager has a clear budget and a deep knowledge of the challenges, each of them developed an aggressive approach- working hard and in the respect of the others, but trying to be always under pressure in order to raise the bar and overcome their limits everyday.Involvement in the results also relies on Euticals' remuneration policy. We are planning to strictly relate salaries and incentives plans to economic and financial targets before the end of 2009, in order to reinforce the entrepreneurial spirit within the company. Internal communication is another essential point to create a good working atmosphere. And in this regard, the group works as open box, closed outside but very opened inside.

As a result, many employees feel that working here is like studying for a master: they can learn a lot about management, which is a great opportunity for them to reach higher levels at a later stage. Relying on this strong management stile, where do you personally want to take the company in the next 10 years, and where will the growth mainly come from?

As shown by the recent acquisition of Mnadrin capital Partners, a plan has been put in place to boost the group's internationalization and I strongly believe that even though each country should remain linked to its own traditions, working together on a worldwide scale is the best way to learn and catch opportunities. You worked 20 years in BMS, starting from a research position then going upscale to top-management.

What made you move to a local company and how challenging was it to move to an entrepreneurial environment?

Nobody would like to move from a multinational, and I did not volunteer for that. But reaching a certain level also implies being ready for changes, which has never been a problem for me. Of course, it has not been easy to leave a company which gave me so much, after 20 years of experience. But I was very well prepared and it did not disrupt my life nor affected my ambitions. I refused to work again in a multinational afterwards because at this stage of my career I wanted to

be in a position in which I could see the direct consequences of my actions, taking the leadership of difficult situations and involving other people in my strategies. While multinationals sometimes consider their employees as numbers –which is extremely frustrating- in structures such as Euticals the whole workforce has got all the tools in hands to achieve a great team work and lead the company towards success.

Could you describe how moving from a family-owned to a public structure will radically affect Euticals strategy in the future?

There will be differences in managing decisions and resources allocation. All the current results should be attributed to the ability and determination of the previous owner, the Carinelli's, to believe in the future of Euticals and put in place all resources for the achievement of the continuous growth of the company. Future steps require additional resources and the new controlling shareholder is committed in implementing the management strategy.

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