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passion for patients

(A member of Boustead Group)

Our Ref : PHARMA/SD/PB/MSWG/2024/039/FWM
Date : 4 June 2024

Minority Shareholders Watch Group
Level 23, Unit 23-2, Menara AIA Sentral
No. 30, Jalan Sultan Ismail
50250 Kuala Lumpur.

(Attn : Dr. Ismet Yusoff, Chief Executive Officer)

26th ANNUAL GENERAL MEETING (AGM) OF PHARMANIAGA BERHAD (Pharmaniaga) TO BE HELD ON WEDNESDAY, 5 JUNE 2024

We thank you for your letter which was received via email on 28 May 2024. Our response to your enquiries are set out below:

Operational and Financial Matters

1. MIDF Amanah Investment Bank Berhad (MIDF Investment) was appointed as the principal advisor for the proposed Regularisation Plan, favouring a proactive approach focused on (i) capital reduction of approximately RM180 million issued share capital to reduce Pharmaniaga's accumulated losses, (ii) fundraising of RM354.6 million via rights issuance for shareholders to strengthen their investments, and (iii) RM300 million in private placement for potential investors to participate in the company's growth plans moving forward. Pharmaniaga also has support from its substantial shareholders, Lembaga Tabung Angkatan Tentera (LTAT) and Boustead Holdings Berhad (BHB), to ensure that their combined entitlements to the rights issue, totalling RM190 million, will be fully taken up. Pharmaniaga has submitted the Regularisation Plan to Bursa Malaysia on 23 February 2024 and anticipate approval of the plan by the following quarter. With the plan well in place for execution, the Group anticipates exiting PN17 status by the third quarter of 2025. (Page 22 of IR2023).

   As at 31 December 2023, the Group reported accumulated losses and negative shareholders' equity of RM603.4 million and RM274.1 million respectively. Exiting PN17 status is dependent on successfully raising sufficient capital through the proposed rights issue and private placement which will ultimately improve the shareholders' equity.

   (a) How confident is the Company in securing the RM300 million private placement for potential investors?

   Our response:

   We are optimistic and confident in securing the RM300 million private placement from potential investors, both locally and internationally. The level of interest shown by potential investors during discussions is positive and is indeed a crucial indicator of the Company's confidence in securing the investment. The Company's proactive approach to regularising its financial health, combined with strong demand in the pharmaceutical sector, underscores its attractiveness to investors.

(b) What is the Company's plan if it fails to raise the necessary capital as outlined in the proposed Regularisation Plan?

Our response:

We remain optimistic and confident. Should the plan requires adjustments, we are prepared to conduct a comprehensive review to pinpoint necessary changes or develop alternative strategies.

2. The loss before interest, taxation, depreciation, and amortisation (LBITDA) of RM22.3 million for FY2023 was primarily attributed to a one-off provision of RM63.9 million for stock obsolescence from the slow demand of pandemic-related consumables inventory such as personal protective equipment and a write-down of RM4.1 million of plant and equipment. (Page 25 of IR2023)

The Group has recorded consecutive provisions for stock obsolescence on pandemic-related inventories, following a substantial provision of RM552.3 million for slow-moving COVID-19 vaccine inventories in FY2022.

(a) When were these pandemic-related consumables inventory purchased by the Group?

Our response:

These pandemic-related consumables inventory, which include disposable particularly respirators, disposable boot covers, shoe covers, hood covers, and surgical latex rubber gloves, were mostly purchased in 2021. This period coincided with the spike during the pandemic, prompting the Group to acquire these items in response to the heightened demand for personal protective equipment.

(b) Are these pandemic-related consumables inventory related to back-to-back orders? If so, why were these items not sold to customers and does the Group have the right to claim for the loss? If not, does this indicate inefficiency in inventory management and what corrective actions have been taken?

Our response:

These pandemic-related consumable inventories are not related to back-to-back orders, but reflects our strategic role as the Government's logistic and supply partner during the pandemic. This approach underscores the importance of maintaining the national stockpile for public health emergencies, showing a proactive stance rather than inefficiency in inventory management.

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(c) What is the carrying amount of pandemic-related consumables inventory aged more than 3 years as at 31 December 2023?

Our response:

The majority of these pandemic-related consumables were purchased in 2021, hence, the age of the inventories is less than 3 years. For those inventories aged over 3 years, the cost is approximately RM1.8 million and we have fully impaired them.

(d) At the previous AGM, the Company mentioned collaborating with strategic partners to facilitate the sale of vaccine stocks to other countries. Please provide an update on this collaboration and the amount recovered by the Group.

Our response:

Ever since the World Health Organization (WHO) announced that the world has entered the endemic phase of the COVID-19 pandemic, the demand for COVID-19 vaccines has dropped significantly. Despite our efforts to collaborate with strategic partners to facilitate the sale of vaccine stocks to other countries, the reduced demand has impacted our ability to sell these stocks.

3. The external auditor has determined that recoverability of property, plant and equipment carrying value of the Group's small volume injectable (SVI) plant as one of the key audit matters. The carrying values of property, plant and equipment other than land and buildings occupied by the Group's SVI production plant as at 31 December 2023 is RM87.5 million. An impairment assessment was performed by management for the Group's SVI plant as it has not been utilised to its optimum production capacity as most of the products are still in the development stage. (Page 187 of IR2023)

While no impairment was required as the recoverable amount of the SVI plant was in excess of the carrying amount of the assets, please share more insight of the products under the development stage (i.e., type of products, number of products, expected launching date, etc).

Our response:

In view of confidentiality, we are unable to disclose the specific types of products under development. However, there are a total of 11 products in the pipeline. We plan to commercialise 5 products in 2024, 2 products in 2025, 3 products in 2026, and 1 product in 2027.

Additionally, we have successfully secured tender contracts with the Ministry of Health (MOH) for 16 products with contract value of approximately RM78 million for 3 years' contract, which further supports the viability and future utilisation of our SVI plant.

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4. The Group had several discussions with Ministry of Health, Malaysia (MOH) from 4 March 2024 to 6 March 2024 to agree on the basis and parameters of an eligible waiver of penalties claimed. As a result of those discussions, the Group expects the total penalties claimed of RM124.9 million to be waived as these waivers have met the parameters agreed by both parties and will be tabled to Concession Management Committee within MOH for consideration. (Page 303 of IR2023)

When does the Group expect to table the waiver and obtain approval from MOH?

Our response:

The waiver of penalty was tabled to the Concession Management Committee within the Ministry of Health (MOH) on 24 April 2024. We expect to receive the waiver letter by latest in the third quarter of 2024. We are optimistic about the favorable consideration of our waiver request.

Sustainability Matters

1. The total energy intensity of the Group has gradually increased from 48.67 GJ/RM mil in 2021 to 70.92 GJ/RM mil in 2023. (Page 112 of IR2023)

(a) What are the reasons for the increasing energy intensity?

Our response:

The increase in energy intensity from 48.67 GJ/RM mil in 2021 to 70.92 GJ/RM mil in 2023 can be attributed to several factors:

I. Energy Intensity and Its Relationship to Company Revenue

Energy intensity is calculated by dividing the total energy consumption by an organization-specific metric. At Pharmaniaga, we use company revenue as the denominator in this calculation.

In 2021, the energy intensity recorded its lowest value at 48.67 GJ/RM million due to the significant increase in sales of COVID-19 vaccines. The high revenue from both Fill-and-Finish as well as Finished Goods vaccine which further lowered the intensity, as less energy consumption was required for supply through importation. Additionally, the focus on vaccines resulted in decreased demand for non-COVID-19 medicines, which in turn slowed down manufacturing and reduced overall energy consumption.

In 2021, Pharmaniaga's energy consumption was 234,355.48 GJ. By 2023, this figure had increased to 239,488.99 GJ, representing only a 2.19% increase in energy consumption. However, in terms of energy intensity, which is calculated as energy consumption per RM million of revenue, 2023 recorded 70.92 GJ/RM mil, an increase of approximately 45.7% compared to 2021.

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Based on our data, energy intensity over the past five years has fluctuated, reflecting the impact of revenue changes on our energy efficiency. Although the energy intensity in 2023 is higher compared to 2021, it remains approximately 20.1% lower than the 2019 baseline. This indicates a significant improvement in our energy efficiency over the longer term.

II. **Operational Expansion**
Operational expansion can lead to an increase in energy consumption which resulted to higher intensity. The Group has expanded its operational activities, including the following.

a. Logistic and Distribution of Sek 23
b. New manufacturing lines in PLS; Pre-filled Syringe (PFS) and Cartridge (insulin).

(b) Has the Group established energy consumption target in terms of energy intensity?

Our response:

Yes, the Group has established energy consumption targets in terms of energy intensity. Our goal is to continuously improve our energy efficiency and reduce our environmental impact. Here are the key points regarding our energy intensity targets:

1. Baseline and Monitoring: We are using 2019 data as our baseline year for energy intensity targets and we monitor our energy consumption and revenue regularly to track our progress against this baseline. Our energy intensity metrics are reviewed quarterly, and results are reported to Board Sustainability Committee to ensure we are on track to meet our targets. Any deviations are analyzed, and corrective actions are implemented promptly.

2. Strategies for Reduction
   - **Efficiency Improvements:** We will continue to explore energy-efficient technologies and processes across our operations to reduce energy consumption. We have initiated retrofitting and upgrades our facilities with energy-efficient lighting, HVAC systems, and machinery to reduce energy consumption.
   - **Operational Optimisations:** We are optimizing our operational processes to ensure more efficient use of energy through automation in operation, digitalization, paperless initiatives, and Internet of Things (IoT)
   - **Renewable Energy**: We are exploring the integration of renewable energy sources to lower our dependence on traditional energy through installation of solar panels. 6 sites have been identified, to power our logistic and manufacturing operations. Currently we are at tender evaluation assessment with expectant installation by Q3/Q4 2024.

2. Pharmaniaga undertook a climate-related risk assessment to evaluate and identify the risks and opportunities that will most likely impact its business in the long term. The climate-related risk assessment and disclosures are in accordance with the recommendations of the TCFD.

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Pharmaniaga has identified 7 risks namely policy & legal, technology, market, reputation, acute and chronic. (Page 113 of IR2023).

What approaches has Pharmaniaga adopted to manage or mitigate these identified risks?

Our response:

The Company undertook among others, the following initiatives to mitigate and manage the identified climate-related risks and opportunities in relation to the recommendations by the TCFD.

To ensure proper governance, the company has the Board Sustainability Committee (BSC) which assists the Board in performing its oversight responsibility over Pharmaniaga's sustainability objectives, policies, and practices.

Complying to ISO 14001:2015 Environmental Management System has also helped us to manage and mitigate the identified risk while continuous education and awareness play an important role to enhance our employees and other stakeholders on the importance of environmental stewardship.

Corporate Governance Matters

1. The Company has not adopted Practice 5.9 of the Malaysian Code on Corporate Governance 2021 (MCCG), which advocates that the Board comprises at least 30% women directors. The Board currently has 2 female directors among its 9 members, which represents about 22% of the Board composition.

   The Company mentioned that it continues The Board acknowledges the call for gender diversity of at least 30% of women directors in companies and has been actively searching for the right candidate to fill in the directorship positions.

   Of the 5 new directors appointed in the past year, there is only 1 female director. Does the Company face any challenges in searching for female directors?

   Our response:

   The Company has made various efforts to improve gender diversity on its board but there are several challenges faced by the Company in achieving the desired level of diversity, due among others, limited candidate pool and our PN17 status.

   To address these challenges, the Company has adopted several strategies:

   1. **Broadening Recruitment Networks:** Expanding search efforts to include diverse networks and organisations dedicated to female leadership in identifying more potential candidates.

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2. **Fostering an Inclusive Culture**: Promoting a company culture that values and supports diversity at all levels to make the Company more attractive to top female talent.

3. **Diversity Goals and Accountability**: Set clear diversity goals for board composition and hold leadership accountable for achieving them.

4. **Inclusive Recruitment Practices**: Use executive search firms with a focus on diversity, and actively seek female candidates from both within and outside the industry.

Should there be any further enquiries or clarification, please do not hesitate to contact our Puan Wan Intan Idura Wan Ismail (idura@pharmaniaga.com) or Encik Syaruzaimi Yusof (syaruzaimi@pharmaniaga.com) at 03-3342 9999 ext. 262.

Thank you.

Yours faithfully,
For and on behalf of,

PHARMANIAGA BERHAD

ZULKIFLI JAFAR
Executive Director

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