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passion for patients
(A member of Boustead Group)

Our Ref. : PHARMA/SD/PB/MSWG/2023/241/MY
Date : 9 June 2023

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

(Attn: Mr. Devanesan Evanson, Chief Executive Officer)

25th ANNUAL GENERAL MEETING (AGM) OF PHARMANIAGA BERHAD (Pharmaniaga) TO BE HELD ON 12 JUNE 2023

We thank you for your letter which was received via email on 30 May 2023. Our response to your enquiries are set out below:

Operational and Financial Matters

1. Pharmaniaga's total equity for FY2022 came in at negative RM227 million, primarily as a result of the full impairment of slow-moving COVID-19 vaccine inventories of RM552 million (page 39 of the Integrated Report 2022 (IR 2022)).

a) Please provide a comprehensive explanation of the decision-making process behind the exceptionally high volume of vaccines that were procured. How did Pharmaniaga evaluate the financial impact of this procurement decision, and what steps were taken to ensure transparency, accountability, and adherence to good governance practices? What methods, approaches, and considerations were taken into account when assessing the potential risks associated with procuring such a large volume of vaccines?

Our response:

Pharmaniaga underwent a stringent and thorough decision-making process for the procurement of the COVID-19 vaccines. During the pandemic, Pharmaniaga had worked closely with the authorities (such as The Special Committee for Ensuring Access to COVID-19 Vaccine Supply, (JKJAV) and the Ministry of Health (MOH) on the supply and distribution of the Sinovac COVID-19 vaccines.

Prior to entering into any sales and purchase agreement with the supplier (Sinovac), and any agreement with the Ministry of Health, Pharmaniaga is required to obtain Board of Directors' approval.

The initial agreement between Pharmaniaga and MOH was to supply 12 million doses of Sinovac Covid-19 vaccines, with deliveries scheduled from April to October 2021. It is pertinent to note that the deliveries to MOH are for "Fill and Finish" (FF) Sinovac vaccines.

However, as the deliveries of Pfizer and AstraZeneca vaccines were delayed, the Government requested Pharmaniaga to secure additional doses of Sinovac vaccines to expedite the vaccination process. Pharmaniaga fulfilled this request by purchasing an additional 10 million doses of Finished Goods (FG) from Sinovac.

During the peak of vaccination, Pharmaniaga delivered the highest number of doses to support the slow delivery of vaccines from other manufacturers.

The Group managed to supply a total of 12.4 million doses, which was 4.5 months ahead of the initial contract schedule. This was achieved by delivering 4 million doses of FF and 8.4 million doses of FG Sinovac vaccines.

The request from MOH to expedite the deliveries of Sinovac Covid-19 vaccines through both FG and FF disrupted the whole process since the initial agreement was for FF delivery to MOH. However, as per the agreement with Sinovac, Pharmaniaga continued to produce the FF doses until the completion of the total 14 million doses purchased earlier.

Upon completion of the delivery of 12.4 million doses, MOH had requested an additional 8 million doses, bringing the total delivery to MOH to 20.4 million doses, consisting of 7.3 million doses of Fill and Finish (FF) and 13.1 million doses of Finished Goods (FG) Sinovac vaccines.

Concurrently, the total projected volume for the private market was estimated at 13.3 million doses, based on submissions of Letter of Intents (LOIs) from various state governments, private healthcare, and corporations. However, Pharmaniaga was not allowed to sell to the private market until the Group had fulfilled its commitment to the Government. As a result, only 2.3 million doses were sold to the private sector, as Malaysia had achieved herd immunity earlier.

Subsequently, with 11.2 million people had received the Sinovac primary vaccination, Pharmaniaga prepared for the administration of 11.2 million doses as the first booster. Additionally, 6 million doses were allocated for the vaccination of adolescents aged between 12-17 years old, and 3 million doses for children aged 5-11 years old.

Unfortunately, the announcement of a mixed vaccines policy for booster vaccination by the Government on 4th October 2021, and the earlier approval of Pfizer-BioNtech Cominarty vaccines for adolescents and children, had affected the demand for Sinovac vaccines.

Pharmaniaga had taken all the necessary prudent considerations in procuring the vaccines while concurrently balancing its obligation to the Government. As the purchases occurred during an emergency period and supplies were tight, ensuring sufficient supply was the primary consideration.

b) Why was there a need for a significant stockpile of vaccines, particularly given the government's announcement of the nation achieving herd immunity in September 2021?

Our response:

The procurement of the vaccines was carried out much earlier, during the emergency period when supplies were scarce, and ensuring an adequate supply was the primary consideration.

With 11.2 million people had received the Sinovac primary vaccination, Pharmaniaga was also preparing for the administration of 11.2 million doses as the first booster, 6 million doses for vaccinating adolescents aged between 12-17 years old, and 3 million doses for children aged 5-11 years old.

Unfortunately, the announcement of a mixed vaccines policy for booster vaccination by the Government on the 4th of October 2021, along with the earlier approval of Pfizer-BioNtech Cominarty vaccines for adolescents and children, had affected the demand for Sinovac vaccines.

c) Please provide an update on the progress made in clearing the vaccine stocks and potential agreements with buyers. What strategies and timeline are in place to facilitate the sale and the vaccine stocks? What is the expiry date of the vaccine stocks, and how confident is Pharmaniaga in clearing them before expiry?

Our response:

Pharmaniaga is currently collaborating with several strategic partners to facilitate the sale of the vaccine stocks to countries with low vaccination rates, with a particular focus on the African Region.

The current expiry date ranges from June 2023 to September 2023, and new stability data submission is planned in July 2023 to extend the shelf life until June 2024 to September 2024. The final extension of the shelf life will provide Pharmaniaga with approximately one year to clear the stocks before they expire.

d) At what prices is Pharmaniaga looking to sell the vaccines, and how does this compare to the procurement price?

Our response:

We have already impaired the entire cost and recognised the losses. However, for the remaining stocks, the Group is willing to engage in negotiations with interested parties to determine suitable pricing. Any sale for the stock at any pricing will be positive to the cashflows and profitability of the Company.

2. Pharmaniaga has initiated remedial efforts via its regularisation plan, aimed at improving shareholders equity with a view towards exiting its current PN17 status (page 39 of IR2022).

Please provide an update on the progress of Pharmaniaga's regularisation plan. What specific measures and strategies have been implemented as part of the plan, and what results have been achieved thus far?

Our response:

We have appointed MIDF Amanah Investment Bank Berhad as the principal adviser for our proposed regularisation plan.

The regularisation plan is currently being drafted, and a requisite announcement will be made in due course, detailing the regularisation plan.

The Group aims to complete the execution of the regularisation by the end of the first quarter of 2024.

3. In order to ensure Pharmaniaga is a going concern, operations and capital expenditures were funded via short-term borrowings. Pharmaniaga is working to improve its cash flow position, with a particular emphasis on ensuring that suppliers are paid on time (page 39 of IR2022).

a) The Group's operating cash flow for FY2022 and 1QFY2023 was negative RM62.2 million and negative RM65.6 million, respectively. As of 31 Dec 2022, the Group's borrowings that were due within three months totalled RM715.6 million, with RM331.4 million subject to potential immediate repayment based on contractual rights due to breaches in financial covenants granted by certain banks (page 312 of IR2022).

Will Pharmaniaga be able to meet its repayment obligations and avoid defaulting on its borrowings?

Our response:

We are confident that we can fulfil our repayment obligations due to the implementation of several ongoing initiatives. These include, among others, implementing cost-reduction measures, improving working capital management, and seeking additional funding.

b) On page 216 of IR2022, it is stated that the Directors are confident that implementation of the new concession agreement with the Ministry of Health would improve the Group's financial position and help to address its PN17 status by providing a steady source of revenue, supporting financial performance, and contributing to profitability.

How significant of an impact is the new concession expected to have on improving the Group's financial position?

Our response:

The new concession is expected to continue contributing at least 50% to the Group's overall revenue.

c) In Pharmaniaga's 1Q2023 notes, it is mentioned that higher payables were primarily due to a delay in payment to suppliers, resulting from cash flow constraints.

What is the latest outstanding amount owed to suppliers? Has there been any instances where suppliers have ceased supplying medicines or taken other actions due to payment delays or non-payments?

Our response:

The outstanding amount to suppliers stands at approximately between one to two months. In cases where potential supply disruption was identified, we managed to re-establish the supply by negotiating with the suppliers for staggered payment basis.

d) What alternative options is Pharmaniaga considering to address cash flow constraints, meet payment obligations to suppliers, and repay borrowings? Given the current circumstances, how likely is it that capital raising initiatives, such as a rights issue, will be implemented in the near future?

Our response:

The Group is actively exploring alternative options to address its cashflow constraints, meet payment obligations to suppliers, and repay borrowings. These options include, among others, implementing cost reduction measures, improving working capital management, and seeking additional funding.

At this juncture, we are unable to provide any details regarding capital raising initiatives pending the requisite announcement.

Corporate Governance Matters

1. On page 126 of IR2022 and in last year's IR2021, it was highlighted that Pharmaniaga's Board Risk Management Committee (BRMC), which has been renamed to Board Risk and Investment Committee (BRIC), consists exclusively of Independent Non-Executive Directors and is chaired by an Independent Non-Executive Director. The BRIC's primary role is to oversee the adequacy of risk management within the Group and ensure that risk exposures and outcomes affecting Pharmaniaga are effectively addressed by the Board. This includes formulating policies and frameworks to identify, monitor, manage, and control material risks impacting the Group.

Considering the significant impairment for the vaccines and other related concerns, what specific actions did the BRIC take in formulating policies and frameworks to identify, monitor, manage, and control material risks impacting Pharmaniaga? How did the committee contribute to ensuring the effectiveness of risk management and addressing the identified risks?

Our response:

The BRIC plays a vital role in overseeing the governance of risks and investments and ensuring the implementation of appropriate infrastructure (policies, frameworks, processes, resources, and systems).

Any newly established or revised policies/frameworks are reviewed and deliberated at BRIC before obtaining the Board's approval, ensuring alignment with the organisation's risk appetite and strategic objectives.

In 2022, three risk management-related documents, namely the newly established Risk Appetite Statement and Business Continuity Management Policy, and the revised Enterprise Risk Management Framework, were reviewed and recommended for the Board's approval.

Risk management activities are discussed and deliberated at BRIC on a quarterly basis, focusing on the adequacy and effectiveness of the risk management processes.

Additionally, BRIC reviews the controls and actions in place to manage and mitigate the Group's overall risk exposure, including emerging risks. It also addresses raised concerns and recommends mitigating actions.

The Board, through BRIC, maintains risk oversight for the Group by receiving quarterly reports on critical matters related to controlling processes, risk management activities, and systems for managing risks.

Should there be any further inquiries or clarification, please do not hesitate to contact our Puan Wan Intan Idura Wan Ismail (idura@pharmaniaga.com) at 03-3342 9999 ext. 206 or Syaruzaimi Yusof (syaruzaimi@pharmaniaga.com) ext. 258.

Thank you.

Yours faithfully,
For and on behalf of,

PHARMANIAGA BERHAD

ZULKIFLI JAFAR
Deputy Chief Executive Officer