PRESS RELEASE
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Headwinds in remission; revenues of ICRA's sample set of Indian API companies to grow by 7-8% and operating profit margin to improve to 12-14% in FY2025: ICRA

- ***Credit profile of ICRA's sample set companies to remain comfortable with Total Debt/OPBDITA of 1.2 times in FY2025***
- ***Capital expenditure expected to moderate to Rs. 5.6 billion in FY2025 from an estimated Rs. 7.6 billion in FY2024***

In its recently released research note, rating agency ICRA highlighted the encouraging growth prospects of the Indian active pharmaceutical ingredients (API) industry. ICRA expects the revenues of its sample set of companies to expand at a CAGR of 7-8% between CY2023 and CY2029 from an estimated size of USD 13-14 billion in CY2023. This will be driven by a steady ramp-up in the pharmaceutical formulations industry, which in turn, will be aided by an increasing geriatric population, higher prevalence of chronic diseases, and rising demand for contract manufacturing with global customers looking to diversify their supply chain along with greater focus on domestic sourcing. ICRA forecasts the operating profit margin (OPM) of its sample set of companies to improve mildly in FY2025.

Indian API industry players faced considerable volatility in earnings over FY2021-FY2023 on account of multiple headwinds such as rising raw material costs due to elevated crude oil prices and pandemic-induced lockdowns in China, resulting in a shortage of key starting materials (KSMs) and APIs globally, inflationary pressures and increased energy costs in Europe, as well as heightened volatility in foreign exchange rates. Nonetheless, raw material prices have softened post FY2023. The container availability issues during the lockdowns were further accentuated by the Russia-Ukraine war, which led to a considerable increase in global freight rates.

Commenting on the industry performance, **Deepak Jotwani, Vice President & Sector Head – Corporate Ratings, ICRA** said: "*Given the subsequent remission in many of these headwinds, ICRA expects revenues of its sample set of companies*[1] *to grow by 7-8% in FY2025, post an estimated increase of 3-5% in FY2024. Given the lower input costs, along with growth in revenues, ICRA expects the earnings improvement recorded in FY2024 to sustain in FY2025 and the OPM to enhance to 12-14% from 11-13% in the previous fiscal. However, the impact of subdued demand from some key export markets such as Europe and tensions in the Red Sea impacting supply chain and freight costs will continue to be monitored*."

India imported APIs and bulk drugs worth ~Rs. 377 billion in FY2024, accounting for ~35% of its total API requirement, of which China accounted for ~70%. Moreover, dependence on Chinese imports of APIs for certain essential medicines is as high as 80-100%. Almost the entire requirement of certain fermentation-based APIs like ciprofloxacin and norfloxacin is sourced from China. The cost advantages with the Chinese API industry and the volatility in the prices of APIs have made domestic production of certain APIs unviable for Indian manufacturers, resulting in continued dependence on China. Even where APIs are manufactured locally, KSMs are primarily sourced from China. The Chinese API industry, which accounts for ~40% of the global requirement, is supported by higher economies of scale, subsidies, and fiscal incentives offered by the Chinese Government, along with lower power, fuel, and borrowing costs.

India has witnessed favourable traction in the production linked incentive (PLI) scheme launched by the Central Government for the bulk drugs industry. The scheme particularly focuses on select molecules such as Penicillin G

[1] ICRA's sample set of companies includes Aarti Drugs Limited, Anuh Pharma Limited, Covalent Laboratories Private Limited, Everest Organics Limited, Hikal Limited, NGL Fine Chem Limited, Satya Deeptha Laboratories Private Limited, Sri Krishna Pharmaceutical Limited, Supriya Lifescience Limited, Virchow Petrochemicals Private Limited

and 7-ACA, which require sizeable investments and involve high energy consumption during the manufacturing process.

Commenting on the updates on the PLI scheme, **Mr. Jotwani** said, "*As of now, ~62% of the originally envisaged investment of ~Rs. 6,500 crore has been made in 32 commissioned projects out of a total of 48 envisaged projects. One of the key products approved under the scheme is penicillin-G, for which India remains highly dependent on China. A leading Indian API manufacturer is likely to commission its penicillin-G manufacturing facility under the PLI scheme in FY2025, helping reduce India's dependence on China for this bulk drug. Domestic manufacturing will also help formulations manufacturers reduce their inventory carrying cost through efficient supply chain management. However, the overall lowering of dependence on China for APIs will ultimately depend on the ramp-up in production of various approved products and price competitiveness of the Indian manufacturers*".

With the completion of capacity expansion by most companies in ICRA's sample set, the capex is expected to moderate to Rs. 5.6 billion in FY2025 from an estimated Rs. 7.6 billion in FY2024. Credit metrics for ICRA's sample set of companies are thus expected to remain comfortable, with Total Debt/ OPBDITA at 1.2 times and interest coverage of 10.0 times in FY2025, supported by a marginal improvement in OPM and modest capex plans. This is after the weakening of debt coverage metrics in FY2023 due to pressure on earnings and range-bound movement noted in FY2024.

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