January 06, 2022

Healthcaps India Limited: Ratings reaffirmed; Rated amount enhanced; Outlook revised to Positive

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term - Fund Based/ Cash Credit	27.87	32.00	[ICRA]BBB+ reaffirmed; Outlook revised to Positive from Stable
Long Term - Fund Based/ Term Loan	25.18	62.71	[ICRA]BBB+ reaffirmed; Outlook revised to Positive from Stable
Long Term - Fund Based/ Working Capital Term Loan	-	8.34	[ICRA]BBB+ (Positive) assigned
Short Term – Non Fund Based/ Letter of Credit	7.50	7.50	[ICRA]A2 reaffirmed
Total	**60.55**	**110.55**	

**Instrument details are provided in Annexure-1*

Rationale

The revision in outlook factors in improvement in Healthcaps India Limited's (HIL) product mix led by encouraging export demand in the hydroxy propyl methylcellulose capsules (HPMC) segment, emanating particularly from the nutraceutical space in the ongoing Covid-19 pandemic. Consequently, the company's margins have displayed substantial improvement in the H1FY2022. The ability of the company to sustain the revenue and margin growth are critical rating factors. The ratings continue to be supported by the company's established position as an empty hard gelatin capsule (EHGC) manufacturer, supported by the ability to steadily grow capacities and its established relationships with its customer base.

The ratings, however, are constrained by the high working capital intensity of operations owing to the long collection period offered to customers, coupled with high inventory holding levels. ICRA also notes the medium forex exposure and the raw material price fluctuation risks associated with the business. While the company has been witnessing steady growth, its scale remains moderate given the low value nature of product.

Key rating drivers and their description

Credit strengths

Established player in empty capsules industry; promoters have strong industry experience – HIL is a leading manufacturer of empty capsules in India with installed annual production capacity of around 17.4 billion capsules. The promoters have more than three decades of experience in the empty capsules segment. The company started with manufacture of EHGC capsules and later diversified into HPMC capsules in FY2017. HPMC capsules are vegetarian capsules which have started gaining healthy demand in overseas and domestic market. Further, HIL is one of the early entrants in HPMC capsules segment and has been able to scale up its capacity due to access to in-house capsule manufacturing technology in its group entity.

Broad customer base with clients spread out in exports as well as domestic market– The company has a wide customer base in the domestic as well as export markets. HIL shares good relationships with its clientele resulting in high repeat orders. In the past few years, the company has been able to penetrate Europe, the Middle East and the South American markets as well as scale up the revenues from these markets. Furthermore, the Group companies (AlfaCaps LLC in the US and HealthCaps Europe Ltd in Europe) directly cater to the demands of small players based in the US and Europe, thereby increasing its exports.

Healthy ramp-up of HPMC sales resulting in revenue diversification and better margin profile– The HPMC capsules are gaining popularity in the US and Europe markets as these are starch-free, gluten-free and preservative-free, and meet the strict dietary needs of customers that choose a vegetarian lifestyle. Further, due to the ongoing pandemic Covid-19, the demand for HPMC capsules have increased significantly especially from the nutraceutical industry in the overseas markets. As a result, HPMC sales grew significantly in FY2021 and H1 FY2022 respectively gaining the majority revenue share in the product mix of the company. Due to increase in HPMC capsule share, which command higher realisations and better margins, HIL's return metrics have improved over FY2021 and H1FY2022.

Healthy financial risk profile characterised by low gearing and healthy coverage indicators– The capital structure of the company remains healthy, given the continuous reserve accretion. However, the debt levels have increased over the last three years in the backdrop of continuous capex. Nevertheless, HIL's gearing (TD/TNW) is moderate at 0.9 times as of Mar 31, 2021, albeit slightly higher than FY2020. Due to improvement in OPBITDA and decline in the interest rates owing to conversion of term loans to FCNR, the debt coverage indicators such as interest cover and DSCR improved to 7.7 times and 2.4 times in FY2021 compared to 4.3 times and 1.7 times earlier. While company has contracted additional loans for its capex in the current financial year, ICRA expects the debt indicators to remain healthy due to expected scale up in OPBITDA in FY2022.

Credit challenges

Moderate scale of operations given the low value nature of product, though established position in the domestic market– Despite the continuous growth in OI over the past five years, the scale of HIL's operations and net cash accruals have remained moderate mainly owing to empty capsules being a low value high volume product. However, with continued capex, the company has become one of the key players in the domestic market. Nonetheless, the demand is steady given the consumable nature of the product in the end segment. Also, the buoyant demand for HPMC led by Covid-19 and the planned capacity addition should help revenues grow substantially in the medium term.

High working capital intensity owing to high debtor days and inventory days–HIL's business has remained working capital intensive. Moreover, due to increasing focus on exports, the working capital cycle has elongated with the company offering more credit period to new clients in export markets and high transit time. This apart, the net working capital intensity stood high at 40% in FY2021 and 30% in H1FY2022. ICRA also notes that a large part of the export business is being done through group entities. However, the company's working capital limits have been recently enhanced resulting in adequate buffer to meet incremental working capital needs.

Moderate foreign exchange risk – Being a net exporter, the company is exposed to forex risks. However, with increased demand due to Covid-19 and HIL's increasing exports, the company has taken forward contracts for Pound sterling hedging. However, HIL has not taken any hedging for US dollars for which the company has natural hedge as it purchases imported raw material in US dollars. There were no significant forex losses in FY2020 and FY2021.

RM price fluctuation risk due to moderately high dependence on imports – The company is able to pass on input price rise to its clients to a partial extent. Given the lead times for imported raw material, the company remains exposed to price fluctuation risks to some extent.

Liquidity position: Adequate

HIL's liquidity is adequate supported by the buffer in working capital limits and modest cash levels. In addition to working capital requirements, the company has sizeable growth capex requirements which are funded by long term loans of 5–6-year tenor resulting in debt repayments of Rs. 10-12 crore which can be covered by the growing company's cash accruals.

Rating sensitivities

Positive factors – ICRA could upgrade HIL's rating if there is a significant scale up in HIL's revenue with the HPMC segment and improvement in its profitability and liquidity position. Specific thresholds would be net cash accruals of more than Rs. 50 crore and the net working cycle lesser than 75 days along with adequate buffer in the working capital limits.

Negative factors – Negative pressure on HIL's rating could arise in case of lower than the anticipated levels of revenues and profitability, or worsened liquidity position. Specific credit metrics that could lead to downgrade of HIL's rating include DSCR below 2x on a sustained basis, deterioration in NWC/OI beyond 50%.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology
Parent/Group Support	Not Applicable
Consolidation/Standalone	Not Applicable

About the company

Incorporated in 1983, HIL is a closely held public limited company engaged in manufacturing of EHGC capsules. HIL diversified into manufacturing of HPMC capsules from FY2017 to cater to the growing demand from pharmaceutical and Nutraceutical industry due to changing consumer preferences. The manufacturing facility of the company is in Fatehpur Village, Nawan Punjab. The company has sales offices in Delhi, Mumbai and Mohali. The company also exports the capsules to various international clients spread across Americas, Europe and Africa. It manufactures capsules in sizes of 00, 0, 1, 2, 3 and 4. HIL has a customer base of over 400+ clients in more than 60 countries across the world.

Key financial indicators (audited)

APSPL Consolidated	FY2020	FY2021	H1 FY2022
Operating Income (Rs. crore)	108.1	149.8	115.2
PAT (Rs. crore)	8.3	15.0	23.7
OPBDIT/OI (%)	17.3%	18.1%	31.2%
PAT/OI (%)	7.6%	10.0%	20.6%
Total Outside Liabilities/Tangible Net Worth (times)	1.2	1.5	1.3
Total Debt/OPBDIT (times)	2.4	2.7	1.0
Interest Coverage (times)	4.3	7.7	16.3

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2022)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as on Sep 30, 2021 (Rs. crore)	Date & Rating in	Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019
					Jan 06, 2022	Dec 02, 2020	Oct 09, 2019	Jul 17, 2018
1	Cash Credit	Long term	32.00	-	**[ICRA]BBB+ (Positive)**	**[ICRA]BBB+ (Stable)**	**[ICRA]BBB+ (Stable)**	**[ICRA]BBB+ (Stable)**
2	Term Loan	Long term	62.71	39.13	**[ICRA]BBB+ (Positive)**	**[ICRA]BBB+ (Stable)**	**[ICRA]BBB+ (Stable)**	**[ICRA]BBB+ (Stable)**
3	Working Capital Term Loan	Long term	8.34	8.42	**[ICRA]BBB+ (Positive)**	-	-	-
4	Letter of Credit	Short term	7.50	-	**[ICRA] A2**	**[ICRA] A2**	**[ICRA] A2**	**[ICRA] A2**

&= Under watch with developing implications

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long Term - Fund Based/ Cash Credit	Simple
Long Term - Fund Based/ Term Loan	Simple
Long Term - Fund Based/ Working Capital Term Loan	Simple
Short Term – Non Fund Based/ Letter of Credit	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, is available on ICRA’s website: www.icra.in

Annexure-1: Instrument details

ISIN No/Banker Name	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Cash Credit	NA	8 - 9.5%	NA	32.00	[ICRA]BBB+ (Positive)
NA	Term loans	FY2014	8-9.7%	FY2027	62.71	[ICRA]BBB+ (Positive)
NA	Working Capital Term loans	FY2021	7-8%	FY2026	8.34	[ICRA]BBB+ (Positive)
NA	Bank Guarantee	NA	NA	NA	7.50	[ICRA] A2

Source: *Company*

[Please click here to view details of lender-wise facilities rated by ICRA]

Annexure-2: List of entities considered for consolidated analysis-Not Applicable

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

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