

February 10, 2017

Syngene International Limited

Instruments	Amounts (Rs. crore ¹)	Rating action
Fund based facilities	0.00 (Revised from 145.00)	
External Commercial Borrowings	445.50 (Revised from 0.00)	[ICRA]AA (Stable) / Assigned
Fund based facilities – Interchangeable	64.50 (Revised from 26.00)	[ICRA]AA (Stable) / [ICRA]A1+ / Reaffirmed
Fund based facilities	0.00 (Revised from 129.00)	

* Instrument details are provided in Annexure I

Rating Action

ICRA has reaffirmed the long-term rating outstanding on the Rs.64.50 crore (revised from Rs.26.0 crore) fund-based interchangeable facilities of Syngene International Limited (Syngene / the company) at [ICRA]AA (pronounced as ICRA double A)². ICRA has also assigned the long term rating of [ICRA]AA (pronounced as ICRA double A) to the Rs.445.50 crore external commercial borrowings (revised from Rs.0.00 crore) of the company. The outlook on the long term rating is Stable. ICRA has also reaffirmed the short-term rating outstanding on the Rs.64.5 crore (revised from Rs.26.0 crore) fund-based interchangeable facilities of Syngene at [ICRA]A1+ (pronounced as ICRA A one plus).

Rationale

The rating reaffirmation continues to factor Syngene's strong parentage (as a subsidiary of Biocon Limited (rated [ICRA]AA+ (Stable) / [ICRA]A1+)), strong market position supported by its integrated presence offering end-to-end discovery and development services for novel molecular entities and robust infrastructure lending considerable cost advantages and its healthy financial profile characterized by strong margins, conservative capital structure with low net debt levels and robust liquidity position. Syngene continues to be an integral part of Biocon's consolidated operations, with the research services contributing more than 30% of revenues during FY2016. Performance of the company remained strong during FY2016 and also first half of the current fiscal, characterized by strong revenue growth on the back of increased business with its existing clients and also new customer additions coupled with continuous widening of service offerings. The ratings also factor in the strong business potential in the contract research outsourcing (CRO) space given the burgeoning research and development (R&D) costs and increasing need for global pharma majors to successfully discover and develop novel molecules to support earnings growth over the medium term (especially given the impending expiry of patents) and its strong client relationship as illustrated by high rate of renewal of contracts and recurring source of revenues lending stability to operations.

The ratings also consider Syngene's strategy to forward integrate and diversify its revenue stream over the medium term by setting up a manufacturing unit for active pharmaceuticals ingredients (novel small molecules). While Syngene is the process of undertaking a large capital expenditure programme of ~USD 200 million (to be completed by FY2018 with about 30% completed by end of March 31, 2016), the same is expected to be funded through its healthy internal accruals and cash reserves held with moderate debt additions expected over the medium term. The ratings, continue to remain constrained by increasing competitive intensity in select service offerings, wage inflation, foreign currency risk given majority of the company's revenues are derived from the export markets, regulatory concerns governing the clinical trial operations for regulated markets and relatively high customer concentration. These concerns are largely mitigated by the benefits derived from its strong parentage, its healthy business profile with leading market position and integrated presence and its robust financial profile.

¹ 100 lakhs = 1 crore = 10 millions

² For complete rating scale and definitions, please refer ICRA's website (www.icra.in) or other ICRA Rating Publications

Key Rating Drivers

Credit Strengths

- Group support and financial flexibility arising from being a subsidiary of Biocon Limited (*rated [ICRA]AA+ (Stable) / [ICRA]A1+*)
- Strong business profile with integrated presence across discovery and development services for novel molecular entities; planned forward integration into manufacturing likely to support business growth and aid in diversification
- Robust infrastructure accredited by regulators and established client relationships likely to aid in sustaining growth momentum; long term contracts with global pharma majors provides revenue visibility and mitigates risk of moderately high customer concentration
- Healthy financial risk profile characterized by conservative capital structure with adequate coverage metrics, strong profitability indicators, stable cash flow generation and large cash and liquid investments balances

Credit Weakness

- Growing competitive pressures from other domestic and international CROs in select service offerings; diversified revenue base and strong client relationship lends comfort and stability to earnings
- Considerable capital expenditure outlined likely to moderate return indicators over the near term given the initial gestation period. Optimal utilization of facilities likely over the next 24 months with expected steady growth in scale of operations would remain key
- In line with the industry, the company faces regulatory concerns governing the clinical trial operations for regulated markets
- Challenges pertaining to wage inflation and foreign currency risk given large foreign currency exposure of the company

Description of key rating drivers highlighted above:

Syngene's operations can be broadly classified into three divisions – a) dedicated R&D centers for global majors like Bristol-Myers Squibb (BMS), b) discovery services and c) development & manufacturing services. Growth during FY2016 has been steady across segments, supported by its established position and its presence across the entire value chain. The growth in dedicated R&D segment was underpinned by the expansion of services towards its three large clients - BMS, Abbott Nutrition and Baxter (the company has also recently added a new center for Amgen (center for discovery & development projects across small and large molecules). While discovery services grew on the back of strong traction in the discovery biology area, growth in development and manufacturing services was largely driven by the expansion in chemical development business towards products reaching later stages of commercialization.

The company's financial profile remains comfortable as reflected by robust operating margins of 35.9% during FY2016 and sound coverage metrics with interest cover of 47.3x and Total Debt / OPBDITA of 2.2x. With strong cash and liquid investment balance as on March 31, 2016, the company's net gearing remained negative. While the company faces competition from other domestic and international players in select service offerings, the same is mitigated to a large extent by its integrated presence and wide product offering and inherent cost advantages when compared to other countries. On the other hand, given that it generates close to 95% of its revenues from exports, its margins remains vulnerable to adverse foreign currency fluctuations.

Analytical approach: For arriving at the ratings, ICRA has taken a consolidated view of the business and financial risk profiles of Syngene International Limited and its parent Biocon Limited given significant business linkages.

Links to applicable Criteria:

Corporate Credit Rating –A Note on Methodology

<http://www.icra.in/Files/Articles/2009-October-Rating-Corp-Rating-Methodology.pdf>

Rating Methodology for Pharmaceutical Industry

<http://www.icra.in/Files/Articles/Pharma-Methodology-Finalised.pdf>

About the Company

Syngene International Limited, a subsidiary of Biocon Limited, is engaged in the business of providing custom research services with strengths in synthetic chemistry and molecular biology. Syngene offers outsourced services to support discovery, development and manufacturing for organisations across industrial sectors like pharmaceuticals, biopharmaceuticals, nutraceuticals, animal health, agro-chemicals, etc. It currently caters to over 250 global customers including majors such as Bristol-Myers Squibb (BMS), Abbott and Baxter, among others.

Recent Results

For H1 FY2017, Syngene reported net profit of Rs.134.5 crore on operating income of Rs.577.5 crore crore as against net profit of Rs.95.1 crore on operating income of Rs.495.1 during the same period previous fiscal. For FY2016, the company reported net profit of Rs.221.2 crore on operating income of Rs.1,107.0 crore.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years:

Table: Rating History

S.No	Name of Instrument	Current Rating			Chronology of Rating History for the past 3 years		
		Type	Rated amount (Rs. Crores)	Month-year & Rating	Month- year & Rating in FY2016	Month- year & Rating in FY2015	Month- year & Rating in FY2013
				February 2017	September 2015	April 2014	January 2013
1	Fund based facilities – Interchangeable facilities	Long Term / Short Term	64.50	[ICRA]AA (Stable) / [ICRA]A1+	[ICRA]AA (Stable) / [ICRA]A1+	[ICRA]AA (Stable) / [ICRA]A1+	[ICRA]AA (Stable) / [ICRA]A1+
2	External Commercial Borrowings	Long Term	445.50	[ICRA]AA (Stable)	-	-	-
3	Fund based facilities- LT	Long Term	-	-	[ICRA]AA (Stable) /	[ICRA]AA (Stable) /	[ICRA]AA (Stable) /
4	Fund based facilities -ST	Short Term	-	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Complexity level of the rated instrument:

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1

Details of Instrument

Name of the instrument	Date of issuance	Coupon rate	Maturity Date	Size of the issue (Rs. Cr)	Current Rating and Outlook
Buyers' Credit	-	-	-	64.50	[ICRA]AA (Stable) / [ICRA]A1+
External Commercial Borrowings	March 30, 2016	-	March 2019 – March 2021	445.50	[ICRA]AA (Stable)

Source: Syngene International Limited

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About ICRA Limited:

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