January 02, 2018

Strides Shasun Limited

Summary of Rated Instruments

Instrument*	Rated Amount (in crore)	Rating Action
Term Loans	1,094.6 (Revised from 969.60)	[ICRA]A+ & / Assigned to enhanced limits
Short-term fund based facilities	890.00	[ICRA]A1+ & / Outstanding
Short-term non-fund based facilities	520.00	[ICRA]A1+ & / Outstanding
Unallocated facilities	624.41	[ICRA]A1+ & / Outstanding
Total	**3,129.01**	

**Instrument details are provided in Annexure-1; & indicates ratings on watch with developing implications*

Rating Action

ICRA has assigned the long-term rating of [ICRA]A+ (pronounced ICRA A plus) to the Rs.1,094.60 crore (revised from Rs.969.60 crore) term loans of Strides Shasun Limited (SSL / the company)[1]. The ratings continue to be on watch with developing implications. ICRA also has the short-term rating of [ICRA]A1+ (pronounced ICRA A one plus) outstanding on the Rs.890.00 crore short-term fund based facilities, the Rs.520.00 crore short-term non-fund based facilities and the Rs.624.41 crore proposed limits of SSL.

Rationale

For arriving at the ratings, ICRA has taken a consolidated view of SSL along with its subsidiaries since all its subsidiaries operate in the same line of business and have operational linkages.

The ratings continue to be on rating watch with developing implications following SSL's announcement of hiving off its active pharmaceutical ingredients (API) vertical. While the eventual business mix is likely to be favorable, ICRA will continue to monitor the impact of the aforesaid corporate restructuring on the financial performance of the company. ICRA will take appropriate action as and when further details are finalized.

The ratings continue to be supported by SSL's diversified business profile with vertically integrated operations, the company's long track record and its strong management team. Improving front-end presence across emerging markets coupled with strong manufacturing infrastructure approved by major regulatory authorities further underpin the ratings. Further, healthy pace of product filings (and faster approvals of the same under the new GDUFA regimen) supported by its strong R&D and regulatory capabilities are expected to support SSL's business prospects going forward. However, the company's revenue growth and margins during H1 FY2018 (14.4% and 12.9% respectively as compare to 21.7% and 22.0% during FY2017) were restricted to a certain extent on account of increased competitive intensity in some molecules in the US while India sales was affected by GST implementation from July 1, 2017. With the company receiving approvals for about eight product approvals in the US market H1 FY2018, revenues from these products and other awaited approvals are expected to strengthen the company's market position in the US market going forward.

[1] *For complete rating scale and definition, refer ICRA's website (www.icra.in) or other ICRA rating publications*

While the company's debt levels continue to be high (~Rs.3,792.0 crore as on March 31, 2017) on account of debt-funded acquisitions in the past, the same has come down to a certain extent with the company's repaying debt of Rs.400 from net proceeds of its India generic business sale to Eris Lifesciences Limited (Eris) during November 2017. The ratings continue to draw comfort from the company's strong cash balance of ~Rs.1,451.0 crore as on September 30, 2017 (As on March 31, 2017, ~60% of the cash was lien marked for loan repayments). ICRA also notes that while the company's debt levels still continue to remain high, part of the debt is expected to be divested to the commoditized API division which is expected to be hived off from H2 FY2018.

The ratings also take into account relatively high competition in the generic pharmaceutical industry which would limit the pricing flexibility and growth to an extent; however, the company's focus on niche segments and products with limited competition are expected to provide comfort. The ratings also take into account challenges with respect to increasing regulatory compliance costs, and the vulnerability of the company's margins to foreign exchange fluctuations with majority of revenues being derived through exports – though the same is mitigated to some extent by natural hedge from foreign currency denominated loans.

While the company has been active in the in-organic space targeting growth and diversification through strategic acquisitions in the past, going forward, this remains an event risk and would be evaluated on a case-by-case basis. Going forward, the company's ability to revive its operating margins, reduce its debt levels especially in the face of increase in working capital intensity (on account of GST), and enhance its credit metrics would remain key rating sensitivities.

Outlook

ICRA believes SSL will continue to benefit from its strong market position; and healthy product filing and approval rate for the regulated markets. The outlook may be revised to 'Positive' if substantial growth in revenue and profitability strengthens the financial risk profile. The outlook may be revised to 'Negative' if margins continue to be lower than estimates, or if debt levels continue to remain high or stretch in the working capital cycle weakens liquidity.

Key rating drivers

Credit Strengths

- **Diversified business and geographic mix lends revenue stability**: During FY2017, SSL derived about 50% of its revenues from the regulated markets, followed by 18% from the emerging markets while the balance was accounted for by the institutional business and API segments.
- **Vertically integrated player with capabilities in API and formulations**: The company's operations remain supported by its healthy market position in the regulated markets supported by captive consumption from the API facilities which supports the benefits of backward integration for the company.
- **Strong research and development (R&D) capabilities**: Going forward, we expect revenue growth/margin to revive from H2 FY2018 supported by healthy filing rate and product approval rates in the US market; new products and expanding pharmacy coverage in Australia; and exit from lower-margin API business.
- **Financial profile characterised by healthy margins and cash balances**: The company witnessed margins of 22.2% during FY2017 with healthy cash balances of Rs.1,631.5 crore as on March 31, 2017. While the margins of the company during H1 FY2018 were relatively lower at 14.6%, the same is expected to improve from H2 FY2018 on the back of healthy pace of product filings and approvals. Cash balances continued to remain healthy at 1,451.0 crore as on September 30, 2018.

Credit Weaknesses

- **High debt levels**: The company has high debt levels on account of the debt-funded nature of large acquisitions in the past. The TD/OPBDITA for the company as on March 31, 2017 was 4.7x and continues to remain high as compared to rating medians for the company's rating category. While the company repaid Rs.400 crore of loans during Q3 FY2018, debt levels continue to remain high with relatively high repayments continuing into FY2019.
- **High competitive intensity**: Generic pharmaceutical business in regulated markets is characterised by low entry barriers and strong pricing pressures. While the company's revenues under its own front-end in North America continued to maintain steady market share, some products under the company's legacy partnered model witnessed significant reduction in profit share in wake of new market entrants during Q1 FY2018 leading to a decline in operating margins of the company.
- **Weak H1 FY2018 performance:** The company's revenue growth and margins during H1 FY2018 were restricted to a certain extent on account of increased competitive intensity in some molecules in the US while India sales was affected by GST implementation from July 1, 2017.
- **Risk arising from inorganic growth**: Given the past history of inorganic growth, any large debt funded acquisition can impact the SSL's credit profile.
- **Regulatory and compliance risks**: Increasing scrutiny and stricter controls by regulatory authorities of developed markets have resulted in higher compliance costs for players across the industry in the recent past.

Analytical approach: ICRA has applied its rating methodologies as indicated below.

Links to applicable Criteria

Corporate Credit Rating Methodology
Rating Methodology- Pharmaceutical Industry

About the company:

Incorporated in 1990, Strides Shasun Limited (previously known as Strides Arcolab Limited) is a medium sized pharmaceutical company engaged in the development, manufacture and export of a wide range of pharmaceutical products. The company has followed an inorganic growth strategy over the years that resulted in foray into new markets, and the addition of new business segments, therapy segments and manufacturing infrastructure. The company's product range covers most dosage forms including tablets, capsules and semi-solids. Following the divestment of its sterile/injectable business to Mylan Inc. in 2013, it concluded the merger with Shasun Pharmaceuticals Limited and acquired Aspen's Australian generic pharmaceuticals business (Arrow Pharmaceuticals) during FY2016. During November 2017, the company had sold its India generics business to Eris Lifesciences Limited to increase its focus on strengthening its market position in the regulated and African markets.

Currently, the company's business became broadly classified into: regulated markets formulations (comprising mainly the US, Europe and Australia), emerging markets (primarily Africa), institutional segment (tender-driven business mainly in developing markets) and APIs and services (the erstwhile business of Shasun Pharmaceuticals Limited).

Key Financial Indicators of SSL

	FY2016	FY2017
Operating income (Rs.Crore)	3,156.4	3,652.0
PAT (Rs.Crore)	208.9	446.0
OPBDITA/ OI (%)	16.6%	22.2%
RoCE (%)	12.4%	12.8%
Total Debt/ TNW (times)	1.3	1.3
Net Debt/ TNW (times)	0.7	0.8
Total Debt/ OPBDITA (times)	7.0	4.7
Net Debt/ OPBDITA (times)	4.1	2.7
Interest coverage (times)	2.9	3.6
NWC/ OI (%)	43.4%	28.6%

Source: company, ICRA; ***Source*** *– company annual reports*
OPBDITA: Operating Profit before Depreciation, Interest, Taxes and Amortization; PAT: Profit after Tax; NWC: Net Working Capital; TNW: Tangible Net Worth; RoCE; Return on Capital Employed; OI: Operating Income

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years:

S. No	Name of Instrument	Current Rating FY2018					Chronology of Rating History for the past 3 years				
		Type	Rated amount (Rs. Crore)	Outstanding amount as on March 31, 2017 (Rs. Crore)	Month-year & Rating	Month-year & Rating	Month- year & Rating in FY2017			Month-year & Rating in FY2016	Month-year & Rating in FY2015
					Jan 2018	June 2018	Feb 2017	Sep 2016	April 2016	June 2015	Sep 2014
1	Term Loans	Long Term	1,094.6	2,305.7	[ICRA] A+ &	[ICRA] A+ &	[ICRA] A+ &	[ICRA] A+ (Stable)	[ICRA] A+ (Stable)	[ICRA] A+ &	[ICRA] A+ &
2	Fund based facilities	Short Term	890.0	1,394.0	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+ &	[ICRA] A1+ &
3	Non-fund based facilities	Short Term	520.0	-	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+ &	[ICRA] A1+ &
4	Unallocated facilities	Short Term	624.41	-	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+	[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

Instrument Details

Name of the instrument	Date of Issuance / Sanction	Coupon rate	Maturity	Size of the issue (Rs. crore)	Current Rating and Outlook
Term Loans	2016	-	By FY2024	1,094.60	[ICRA]A+ &
Fund based facilities	-	-	-	890.00	[ICRA]A1+ &
Non-fund based facilities	-	-	-	520.00	[ICRA]A1+ &
Unallocated facilities	-	-	-	624.41	[ICRA]A1+ &

Source: Strides Shasun Limited

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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.
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