ICRA

March 12, 2018

Strides Shasun Limited

Summary of Rated Instruments

Instrument*	Previous Rated Amount (in crore)	Current Rated Amount (in crore)	Rating Action
Term Loans	1,094.6	1,094.6	[ICRA]A+ & / reaffirmed
Short-term fund based facilities	890.00	890.00	[ICRA]A1 & / revised from [ICRA]A1+ &
Short-term non-fund based facilities	520.00	520.00	[ICRA]A1 & / revised from [ICRA]A1+ &
Unallocated facilities	624.41	624.41	[ICRA]A1 & / revised from [ICRA]A1+ &
Total	**3,129.01**	**3,129.01**	

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

Rating Action

ICRA has revised the short-term rating 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 Strides Shasun Limited (SSL / the company)[1] to [ICRA]A1 (pronounced ICRA A one) from [ICRA]A1+ (pronounced ICRA A one plus). ICRA has reaffirmed the long-term rating outstanding on the Rs.1,094.60 crore term loans of SSL at [ICRA]A+ (pronounced ICRA A plus). The ratings continue to be on watch with developing implications.

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 revision in short-term rating of the company follows the weak operating performance of the company during 9M FY2018 wherein SSL had witnessed OPM contraction to 14.2% as against 21.7% during 9M FY2018. While the company's margins were affected by pricing pressures in the North American market during Q1 FY2018, the same was marred by weak demand scenario in its margin-accretive institutional business during Q2 & Q3 FY2018. ICRA also notes that the company's debt levels continue to remain high with total debt of Rs.2,835 crore (excluding debt of Rs.456 crore pertaining to its API vertical which is expected to be demerged in the immediate future) as on December 31, 2017 even while large part of the cash-backed loans have been prepaid. The company's TD/OPBDITA and Net Debt/OPBDITA stood at around 6.0x and 4.0x respectively as on December 31, 2017 and continue to remain high as compared to rating medians for the company's rating category.

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

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 regulated markets coupled with strong manufacturing infrastructure approved by major regulatory authorities provide further support to the ratings. Further, healthy pace of product filings (and faster approvals of the same under the new GDUFA regimen for the US market) supported by its strong R&D and regulatory capabilities are expected to support SSL's business prospects going forward. With the company receiving approvals for twelve new products in the US market during 9M FY2018, revenues from the same and other awaited approvals are expected to strengthen the company's market position in the US market going forward. In the Australian market, SSL's ddistribution footprint continues to expand with pharmacy coverage of 1,200+ stores. Overall, the company has launched 23 new products in Australia during 9M FY2018. Going forward, backward integration of the Australian product portfolio to SSL's in-house facilities in India coupled with improving front end presence is expected to support the company's business prospects and margins.

The ratings also consider the relatively high competition in the generic pharmaceutical industry which would limit the company's pricing flexibility and growth to an extent; however, SSL'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.

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.

Key rating drivers

Credit Strengths

- **Diversified business and geographic mix lends revenue stability**: SSL derives majority of its revenues from its regulated markets business in North America and Australia. In addition to the same, the company also derives revenues from emerging markets like India and Africa where it is present in the branded and institutional businesses. During 9M FY2018, the company derived 78% of its revenues from the regulated markets and the balance from emerging markets.
- **Vertically integrated player with capabilities in API and formulations**: The company's enjoys healthy market position in the regulated markets on the back of its cost-competitiveness supported by captive consumption from the API facilities providing benefits of backward integration for the company.

- **Strong research and development (R&D) capabilities coupled with improving front end presence**: Given it strong pipeline of limited competition products, we expect the company's revenue growth and margins to revive from FY2019 supported by healthy filing rate and product approval rates in the US market and enhanced product basket and expanding pharmacy coverage in Australia respectively. SSL's strong manufacturing infrastructure with key facilities having been approved by regulatory authorities of developed markets are expected to facilitate the same going forward.

Credit Weaknesses

- **High debt levels**: The company has high debt levels (Total debt of Rs.2,835 crore and net debt of Rs.1,775 crore as on December 31, 2018) on account of the debt-funded nature of large acquisitions in the past coupled with recent stretch in working capital levels post GST implementation. TD/OPBDITA and Net Debt/OPBDITA stood at around 6.0x and 4.0x respectively as on December 31, 2017 and continue to remain high as compared to rating medians for the company's rating category. Even while the company prepaid significant amount of loans (~Rs.900 crore) 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 high 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 9M FY2018 performance:** The company's revenue growth and margins during 9M FY2018 were restricted to a certain extent on account of increased competitive intensity in some molecules in the US. This, coupled with lower contribution from margin-accretive institutional segment sales on account of a weak demand scenario in conjunction with continued investments in R&D affected the company's OPMs adversely.
- **Risk arising from inorganic growth**: Given the past history of inorganic growth, any large debt funded acquisition can impact 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 Ratings: A Note on 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). However, the API business will be demerged from the company (post receipt of NCLT approval) effective October 01, 2017.

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				Chronology of Rating History for the past 3 years						
		Type	Rated amount (Rs. Crore)	O/s amount as on March 31, 2017 (Rs. Crore)	Month-year & Rating	Month-year & Rating in FY2018		Month- year & Rating in FY2017			Month-year & Rating in FY2016	Month-year & Rating in FY2015
					March 2018	Dec 2017	June 2017	Feb 2017	Sept 2016	April 2016	June 2015	Sept 2014
1	Term Loans	LT	1,094.6	2,305.7	[ICRA] A+ &	[ICRA] A+ &	[ICRA] A+ &	[ICRA] A+ &	[ICRA] A+ (Stable)	[ICRA] A+ (Stable)	[ICRA] A+ &	[ICRA] A+ &
2	Fund based facilities	ST	890.0	1,394.0	[ICRA] A1 &	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+ &	[ICRA] A1+ &
3	Non-fund based facilities	ST	520.0	-	[ICRA] A1 &	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+ &	[ICRA] A1+ &
4	Unallocated facilities	ST	624.41	-	[ICRA] A1 &	[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	2016	-	-	890.00	[ICRA]A1 &
Non-fund based facilities	2016	-	-	520.00	[ICRA]A1 &
Unallocated facilities	-	-	-	624.41	[ICRA]A1 &

Source: Strides Shasun Limited

Name and Contact Details of the Rating Analyst(s):

Analyst Contacts

Subrata Ray
+91 22 2433 1086
subrata@icraindia.com

Pavethra Ponniah
+91 44 4596 4314
pavethrap@icraindia.com

Mythri Macherla
+91 80 4332 6407
mythri.macherla@icraindia.com

Name and Contact Details of Relationship Contacts:

Jayanta Chatterjee
+91 80 4332 6401
jayantac@icraindia.com

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**

Registered Office
ICRA Limited
1105, Kailash Building, 11th Floor, 26, Kasturba Gandhi Marg, New Delhi 110001
Tel: +91-11-23357940-50, Fax: +91-11-23357014

Corporate Office
Mr. Vivek Mathur
Mobile: +**91 9871221122**
Email: vivek@icraindia.com

Building No. 8, 2nd Floor, Tower A, DLF Cyber City, Phase II, Gurgaon 122002
Ph: +91-124-4545310 (D), 4545300 / 4545800 (B) Fax; +91- 124-4050424

Mumbai **Mr. L. Shivakumar** Mobile: +**91 9821086490** Email: shivakumar@icraindia.com 3rd Floor, Electric Mansion Appasaheb Marathe Marg, Prabhadevi Mumbai—400025, Board : +91-22-61796300; Fax: +91-22-24331390	**Kolkata** **Mr. Jayanta Roy** Mobile: **+91 9903394664** Email: jayanta@icraindia.com A-10 & 11, 3rd Floor, FMC Fortuna 234/3A, A.J.C. Bose Road Kolkata—700020 Tel +91-33-22876617/8839 22800008/22831411, Fax +91-33-22870728
Chennai **Mr. Jayanta Chatterjee** Mobile: +**91 9845022459** Email: jayantac@icraindia.com 5th Floor, Karumuttu Centre 634 Anna Salai, Nandanam Chennai—600035 Tel: +91-44-45964300; Fax: +91-44 24343663	**Bangalore** **Mr. Jayanta Chatterjee** Mobile: +**91 9845022459** Email: jayantac@icraindia.com 'The Millenia' Tower B, Unit No. 1004,10th Floor, Level 2 12-14, 1 & 2, Murphy Road, Bangalore 560 008 Tel: +91-80-43326400; Fax: +91-80-43326409
Ahmedabad **Mr. L. Shivakumar** Mobile: +**91 9821086490** Email: shivakumar@icraindia.com 907 & 908 Sakar -II, Ellisbridge, Ahmedabad- 380006 Tel: +91-79-26585049, 26585494, 26584924; Fax: +91-79-25569231	**Pune** **Mr. L. Shivakumar** Mobile: +**91 9821086490** Email: shivakumar@icraindia.com 5A, 5th Floor, Symphony, S.No. 210, CTS 3202, Range Hills Road, Shivajinagar,Pune-411 020 Tel: + 91-20- 6606 9999; Fax: +91-20-25561231
Hyderabad **Mr. Jayanta Chatterjee** Mobile: +**91 9845022459** Email: jayantac@icraindia.com 4th Floor, Shobhan, 6-3-927/A&B. Somajiguda, Raj Bhavan Road, Hyderabad—500083 Tel:- +91-40-40676500	