Windlas Biotech Private Limited

August 23, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	33.04	18.91	[ICRA]A(Stable); upgraded from [ICRA]A-(Positive)
Cash credit	27.00	27.00	[ICRA]A(Stable); upgraded from [ICRA]A-(Positive)
Long-term/short-term Fund Based Limits	23.30	23.30	[ICRA]A(Stable)/A1; upgraded from [ICRA]A-(Positive)/A2+
Short-term Fund-Based	0.00	25.00	[ICRA]A1; upgraded from [ICRA]A2+
Short-term non-Fund Based	2.00	2.00	[ICRA]A1; upgraded from [ICRA]A2+
Unallocated Limits	23.46	12.59	[ICRA]A(Stable)/A1; upgraded from [ICRA]A-(Positive)/A2+
Total	**108.80**	**108.80**	

*Instrument details are provided in Annexure-1

Rating action

ICRA has upgraded the long-term rating of [ICRA]A- (pronounced ICRA A minus) outstanding on the Rs. 108.80-crore bank limits of Windlas Biotech Private Limited (WBL or the company) to [ICRA]A (pronounced ICRA A)[1]. ICRA has also upgraded the short-term rating of [ICRA]A2+ (pronounced ICRA A two plus) to [ICRA]A1 (pronounced ICRA A one). The outlook on the long-term rating has been revised from Positive to Stable.

Rationale

The ratings upgrade favourably factors in the improvement in the company's financial metrics supported by improved profitability and expectation of no further equity support to its subsidiary company viz. Windlas Healthcare Private Limited (WHL), following an announcement of strategic investment from Cadila Healthcare Limited (Cadila).

In FY2018, WBL's sales growth was flat because of weak performance of the Indian pharmaceutical market (IPM) due to Goods and Services Tax (GST) related de-stocking in H1 FY2018 and rationalisation of low-margin products in its contract manufacturing business. The company identified the low-margin products in its contract manufacturing business and it re-negotiated prices with its customers or phased out these products. This helped to improve its operating profit margin (OPM) by over 250 basis points to 10.8%, which strengthened its coverage indicators.

The improvement in profitability was also supported by an expansion of its export business and own brand sales (collectively 10% of turnover), which have higher margins as compared to its contract manufacturing business. WBL expanded its export sales in the rest of the world (ROW) markets like Africa and Southeast Asia. It has filed several dossiers in close to 20 countries and exports are expected to ramp up significantly in the next two to three years.

[1]*For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications*

WBL also increased the scale of its own-brand operations by scaling up its generics portfolio. The sales from generics increased to approximately Rs. 10 crore in FY2018 from Rs. 1 crore in FY2017 supported by setting up a robust distribution channel, which increased its penetration in the small towns and rural areas. It has over 800 stockists on its platform and it will focus on marketing established salts in the anti-biotic, cough syrup and pain killer segments. The improvement in scale of its generics business has been margin accretive for the company because margins in the generics segment are higher than the contract manufacturing business.

ICRA favourably factors in the strategic investment into WHL, which will nullify any further infusion from WBL. On August 13, 2018 Cadila announced that it plans to acquire 51% ownership in WHL for a consideration of Rs. 155 crore, valuing the company at Rs. 304 crore. This investment will help Cadila to ramp up its operations and increase its product offerings. WHL has a USFDA-approved plant in Dehradun and it has filed four abbreviated new drug applications (ANDAs) in the US, of which it will commence sale of one. The investment from Cadila will help WHL scale-up its ANDA filings in the US in the coming years.

The ratings are, however, constrained by WBL’s moderate scale of operations, limited scale of own-branded products and relatively low profit margins as compared to its peers. The company’s scale of operations remained flat in FY2018 because of rationalisation of low margin business and weak performance of the IPM because of GST-related de-stocking of inventory in H1 FY2018. The scale of WBL’s contract manufacturing business declined by 3.3% in FY2018 and the same was mitigated by an increase in its export and generics business. Although there was growth in its generics business, the company’s branded generics business remained flat at Rs. 7 crore in FY2018. The growth in its generics and branded generics segment is also constrained by high concentration of sales in North India. The company’s profit margins continue to lag peers but WBL has been successful in reducing the difference by rationalising low-margin products, besides witnessing an increase in exports and own brand sales.

ICRA notes that the implementation of the GST has led to a change in the overall tax and duty structure in the pharmaceutical industry, with previously available benefits in excise/tax-free zones for contract manufacturers being eliminated. This has led to increased competition for WBL and is likely to moderate its growth prospects. However, ICRA continues to take comfort from the established relationships of the company, product development strengths and the management’s effort to expand its export business, which are likely to mitigate the adverse impact of the elimination of excise exemption benefits.

Outlook: Stable

ICRA believes WBL will continue to maintain strong financial indicators supported by growth in all segments. The outlook may be revised to Positive if it is able to increase its scale of operations by obtaining business from a new customer in its contract manufacturing business and increase the export and own-brand sales. The outlook may be revised to Negative if there is a substantial decline in its scale of business due to the loss of a key customer.

Key rating drivers

Credit strengths

Established relationships with several domestic pharmaceutical majors - The company has a well-reputed client base with supplies to several big formulators including Mankind Pharma, Glenmark Pharma, Orchid Pharma, Torrent Pharma, etc, which has supported the growth of its contract manufacturing business.

Ramp up of export sales in Africa and Southeast Asia to benefit profit margins - WBL’s export sales grew by 67% in FY2018 to Rs. 13.9 crore from Rs. 8.3 crore in FY2017, which has supported the improvement in the company’s profit margins in FY2018.

Focus on value-added generics, combination drugs and change in delivery systems gives a competitive edge - The company has, over the years, been able to improve its margins through its focus on developing new formulations (new combination drugs and new drug delivery systems) through its own product development capabilities.

High focus on quality procedures limits legal and regulatory risks - The company has a very high focus on maintaining its quality standards and its units are compliant with stipulations issued by international and national organisations like the World Health Organisation (WHO) and the International Organisation for Standards (ISO).

Credit challenges

The scale of operations remains much lower than other major contract manufacturers - WBL's scale of operations continue to remain lower than other contract manufacturers because of which it is not able to achieve economies of scale.

Operating margins lag other contract manufacturing companies - WBL's profitability lags its peers in the contract manufacturing industry. However, the company is taking measures to reduce the difference by rationalising low margin business and increasing its export and generics sales.

Limited scale of own-branded products restricts diversification of revenues - The limited scale of WBL's own-branded products limits the diversification of revenues and the contract manufacturing business accounted for 90% of its sales in FY2018.

GST implementation negates excise exemption benefits, thereby increasing competition - WBL's unit two had excise duty exemption till FY2020, but the implementation of GST led to a change in the overall tax and duty structure in the pharmaceutical industry and has eliminated the benefits available in excise/tax-free zones. This has negated the competitive advantage for players operating from such zones and increased competition in the sector.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below**.**

Links to applicable criteria:

Corporate Credit Rating Methodology

Rating Methodology for Pharmaceutical Industry

About the company:

The Windlas Group primarily has two companies – Windlas Biotech Private Limited (WBL) and Windlas Healthcare Limited (WHL) with the latter being a 49% associate of WBL at present. WBL derives its business from two segments - contract manufacturing of formulations for domestic pharmaceutical companies and manufacturing and marketing of branded generic formulations. The contract manufacturing business accounts for a major part (90%) of the company's total sales, while the branded formulations business accounts for the balance. In the contract manufacturing business, WBL undertakes manufacturing of formulations on principal-to-principal (P2P) basis. The company's key customers includes – Mankind, Glenmark, etc. with the top five contributing 56% to its overall turnover. In addition, WBL has also entered into domestic formulation market through its own-branded business. However, after initial investments, it has adopted the pure generics model to scale-up business citing stiff competition.

The promoters – Windlass family owns 88% stake in WBL, while the balance (12%) is held by Tano Capital. Tano had invested Rs. 82 crore as a mix of equity shares and preference shares in FY2016, valuing the company at Rs. 460 crore.

WHL runs a USFDA-approved plant and provides an array of services including site transfers, contract research for formulations development, small scale to commercial production and regulatory support. Over the years, the Group has initiated investments in developing products for US generics markets and has filed six ANDAs so far. These investments are routed through WBL's wholly-owned subsidiary – WHL. Given the limited experience in international markets, especially regulated ones, the Group has partnered with other generics companies to de-risk itself from litigation and marketing-related risk that are common to US generics business. WHL has so far commercialised Prasugrel through tie-up with Granules. The cumulative investments in the subsidiary till March 2018 stood at Rs. 105 crore. Cadila Healthcare Limited acquired a 51% stake in WHL in August 2018 by infusing Rs. 155 crore at a valuation of Rs. 304 crore.

Key financial indicators (audited)

	FY2017	FY2018 (Provisional)
Operating Income (Rs. crore)	316.1	320.8
PAT (Rs. crore)	9.2	13.6
OPBDIT/OI (%)	8.2%	10.8%
RoCE (%)	10.2%	14.4%
Total Debt/TNW (times)	0.4	0.2
Total Debt/OPBDIT (times)	2.4	0.8
Interest Coverage (times)	5.2	7.3

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2019)				Chronology of Rating History for the Past 3 Years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating Aug 2018	Date & Rating in FY2017 Mar 2017	Date & Rating in FY2016 Jan 2016	Date & Rating in FY2015 Nov 2014
1	Term Loan	Long Term	18.91	18.91	**[ICRA]A (Stable)**	**[ICRA]A- (Positive)**	**[ICRA]A (Stable)**	**[ICRA]BBB+ (Stable)**
2	Cash Credit	Long Term	27.00		**[ICRA]A (Stable)**	**[ICRA]A- (Positive)**	**[ICRA]A (Stable)**	**[ICRA]BBB+ (Stable)**
3	Short-term Fund Based Limits	Short Term	25.00		**[ICRA]A1**	**NA**	**NA**	**NA**
4	Short-term Non-Fund Based	Short Term	2.00		**[ICRA]A1**	**[ICRA]A2+**	**[ICRA]A 2+**	**[ICRA]A2**
5	Shot-term Interchangeable	Short Term	(19.00)		**[ICRA]A1**	**[ICRA]A2+**	**[ICRA]A 2+**	**[ICRA]A2**
6	Long-term/ short-term fund interchangeable	Long Term/ Short Term	(1.50)		**[ICRA]A (Stable)/ A1**	**[ICRA]A- (Positive)/ A2+**	**[ICRA]A- (Stable)/ A2+**	**[ICRA]BBB+ (Stable)/ A2**
7	Long-term/ short-term fund based	Long & Short Term	23.30		**[ICRA]A (Stable)/ A1**	**[ICRA]A- (Positive)/ A2+**	**[ICRA]A- (Stable)/ A2+**	**[ICRA]BBB+ (Stable)/ A2**
8	Unallocated	Long & Short Term	12.59		**[ICRA]A (Stable)/ A1**	**[ICRA]A- (Positive)/ A2+**	**[ICRA]A- (Stable)/ A2+**	**[ICRA]BBB+ (Stable)/ A2**

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

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan 1	FY2015		FY2021	3.35	[ICRA]A (Stable)
NA	Term Loan 2	FY2015		FY2021	10.98	[ICRA]A (Stable)
	Term Loan 3	FY2015		FY2021	4.58	[ICRA]A1
NA	Cash Credit				27.00	[ICRA]A1
NA	Short-term Fund Based Limits				25.00	[ICRA]A1
NA	Short-term Non-Fund Based				2.00	[ICRA]A (Stable)/ A1
NA	Shot-term Interchangeable				(19.00)	[ICRA]A(Stable)/ A1
NA	Long-term/ short-term fund interchangeable				(1.50)	[ICRA]A (Stable)/ A1
NA	Long-term/ short-term fund based				23.30	[ICRA]A(Stable)
NA	Unallocated				12.59	[ICRA]A(Stable)

Source: WBL

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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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