ICRA

Concord Biotech Limited

January 25, 2019

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund-based (Proposed)	75.00	[ICRA]AA-(Stable); assigned
Total	**75.00**	

Instrument details are provided in Annexure-1

Rationale

The assigned rating takes into account the extensive experience of Concord Biotech Limited's promoters and the company's established track record in the fermentation and semi-synthetic biopharmaceutical (active pharmaceutical ingredient or API) business, spanning around two decades. The rating considers the company's strong financial profile, characterised by healthy profitability levels, strong debt protection indicators and robust liquidity. The ratings also factor in the company's key market player position in the global immunosuppressant therapeutic API segment, its strong research and development (R&D) capabilities with adequate regulatory approvals and its reputed clientele with strong inflow of repeat businesses.

The rating is, however, constrained by the company's moderate scale of current operations, high product and client concentration, and high working capital intensity, owing to the elongated receivable cycle and the high inventory holding period. Although the company remains one of the key players in the API segment, its entry into the formulation segment entails intense competitive pressures. Further, the successful scale up of the formulation business remains to be seen. ICRA notes that the company is in the midst of a sizeable debt-funded capex for an increase in the API capacity at a total cost ~Rs. 224.75 crore spread over the next two fiscals. Also, achieving healthy capacity utilisation levels would remain critical from a credit perspective.

Outlook: Stable

ICRA expects Concord Biotech Limited to continue to benefit from the extensive experience of its promoters in the biopharmaceutical industry and witness revenue growth in the near term, backed by stable demand conditions, healthy order flow for the API segment and new businesses from the formulation segment. The outlook may be revised to Positive if healthy scaling up of operations, whilst maintaining/improving the profitability, and better working capital management strengthen the financial risk profile. The outlook may be revised to a Negative if cash accrual is lower than expected, if there is any material deterioration in the profit margins or if any major debt-funded capital expenditure, or a stretch in the working capital cycle, weakens liquidity.Key rating drivers

Credit strengths

Experienced management; established track record - The promoters and management are well-experienced, having run the business for two decades. They are well-established in the fermentation and semi-synthetic biopharmaceutical (API) business.

Key market player in niche product segment - The company's key products - Tacrolimus and Mycophenolate (Mofetil and Sodium) are low-volume but high value-added niche products, catering to the immunosuppressant therapeutic segment. These complex molecules are exposed to limited competition and garner healthy margins. Although the molecules cumulatively contribute to ~60% of the revenues, the company is a key player in the industry for these products, commanding a healthy market share. The molecules have shown volume growth YoY, despite being off-patent and have supported the revenues of the company. Going forward, further growth is projected for the APIs given the ongoing production capacity expansion plans (because of the growing demand from its customers).

Strong R&D capabilities; adequate regulatory approvals - The company's R&D centre is recognised by the Department of Scientific and Industrial Research (DSIR), India and backed by a strong team of technocrats. Its API facility is approved by the US Food and Drug Administration (USFDA), the European Union Good Manufacturing Practices (EUGMP), the Japanese Foreign Manufacturer Registration (FMR), the Korea Ministry of Food and Drug Safety and the Indian Good Manufacturing Practices (GMP), whereas the formulation facility is GMP and USFDA approved.

Reputed customer base - The company's customer base comprises reputed formulation players, such as Intas Pharmaceuticals Limited, Mylan Inc, Alkem Laboratories Limited and Glenmark Pharmaceuticals, which result in limited counterparty credit risk.

Strong financial risk profile - The company's profit margins remained robust with the operating margin at 42-52% and the net margin at 26-34% over the last few years. The net worth base (Rs. 594.36 crore as on March 31, 2018) remained strong supported by healthy cash accruals and equity infusion of Rs. 76.30 crore in FY2017. This, coupled with a low dependence on external borrowings, resulted in a comfortable capital structure (with gearing of 0.04 times and TOL/TNW of 0.16 times as on March 31, 2018) and an overall negative net debt position. Owing to the low debt level and the healthy profitability, the debt protection metrics remained robust with interest coverage of 125.85 times and Total Debt/OPBDIT of 0.15 times in FY2018. The DSCR also stood comfortable at 12.05 times in FY2018. The liquidity position remains robust as evidenced by low working capital limit utilisation and healthy cash and liquid investments (Rs. 153.44 crore as on March 31, 2018).

Credit challenges

Moderate scale of operations; high product concentration risk - The company's scale of operations remained moderate with the operating income (OI) of Rs. 337.99 crore in FY2018. Also, the company is exposed to high product concentration risk with the top three products contributing to ~60% of the total revenues. However, the scale and product diversification are expected to improve FY2019 onwards (with the gradual increase in sales from the formulation segment and the stabilisation of a new API unit). Its top two customers - Intas Pharmaceuticals Limited and Mylan Inc - contribute to ~40% of the revenues, reflecting customer concentration risk. However, the company's dominant position in the immunosuppressant API business and the repeat orders from customers reflect its preferred supplier status, limiting the risk to an extent.

High working capital intensity - The company normally provides a credit period of ~90-120 days to its key customers and maintains a high inventory of various cultures (raw material) to produce different APIs. Also, the WIP inventory remains high as the last stage is completed (~1-5% of the production process) after the order receipt. This is because the shelf life of the products starts after the entire process completion. Hence, elongated receivable cycle and high inventory holding requirements resulted in high working capital intensity of operations in the past. The fiscal-end intensity stood at 72% and 77% in FY2017 and FY2018 respectively, due to high sales and purchase concentration in the last quarter. However, the average working capital intensity during the last two fiscals stood at ~50-55%.

Risks associated with sizeable ongoing capex - The company is setting up an API manufacturing unit at a total cost of Rs. 224.75 crore. It is, therefore, exposed to the risks associated with timely completion and stabilisation of the expansion project without any significant cost and time overruns. The new unit is expected to be operational by FY2021. The proposed capex funding is through a mix of term loan and internal accruals, with a debt-to-equity ratio of 0.50 times. Moreover, the increase in debt exposure will result in some moderation in the capital structure and the debt coverage indicators in the near term, although the same are expected to remain healthy.

Successful scale up of formulation segment to achieve desired level of profitability - The company's formulation unit started commercial operations from March 2017 and is yet to stabilise with the operating loss of Rs. 23.47 crore and the net loss of Rs. 29.54 crore in FY2018. Although the company remains one of the key players in the API segment, it faces intense competition in the formulation business with the presence of multiple large organised players. Thus, the company's ability to garner market share in the intensely competitive environment, scale up its operations and achieve breakeven remains to be seen. The formulation operations remain exposed to regulatory restrictions in terms of pricing caps in the domestic markets and product/facility approvals in the export destinations. ICRA notes that timely product and facility approval/renewal, in various regulated and semi-regulated markets, remains critical for the formulation unit growth.

Liquidity position

The company's cash flows remained healthy over the past years, supported by healthy profitability and low cash outlays towards interest expenses and debt repayments (due to low dependence on external borrowings). The company's liquidity position remains robust as evidenced by the low working capital limit utilisation, with average utilisation of ~2% (undrawn line of credit of Rs. 20.00 crore as on November 30, 2018) from December 2017 to November 2018, and strong free cash and liquid investments (Rs. 153.44 crore as on March 31, 2018 and Rs. 203.49 crore as on November 30, 2018).

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating methodology for entities in the pharmaceutical industry
Parent/Group Support	Not Applicable
Consolidation/Standalone	The rating is based on the standalone financial profile of the company.

About the company

Concord Biotech Limited, incorporated in November 1984, was taken over by the current promoter, Mr. Sudhir Vaid, in 2000. Mr. Vaid is a technocrat having over four decades of experience in biotechnology. He served eight years as Director-Fermentation at Ranbaxy Laboratories Limited and thereafter, as a consultant to various leading pharmaceutical companies. The company also has a robust investor profile with Mr. Rakesh Jhunjhunwala and Group holding ~24% and Helix Investment Holdings Pte Limited holding a 20% stake in the company. Helix Investment Holdings Pte Limited is a special purpose vehicle (SPV) floated by Quadria Capital, which has invested in 18 healthcare chains across the Asia-pacific region.

Concord Biotech Limited was initially set up with one manufacturing block for the production of amidase enzyme. Capacities were subsequently added and the current facilities comprise 22 API-manufacturing blocks. The company manufactures fermentation and semi-synthetic biopharmaceutical APIs with immunosuppressants as the key therapeutic segment. As a means of forward integration, it set up a formulation unit which commenced commercial production from March 2017. It is currently setting up a new API unit, which is expected to commence commercial production from June 2020.

In FY2018, the company reported a net profit of Rs. 100.49 crore on an OI of Rs. 337.99 crore, compared to a net profit of Rs. 108.82 crore on an OI of Rs. 321.71 crore in the previous year.

Key financial indicators (audited)

	FY2017	FY2018
Operating Income (Rs. crore)	321.71	337.99
PAT (Rs. crore)	108.82	100.49
OPBDIT/ OI (%)	51.46%	42.97%
RoCE (%)	36.41%	25.02%
Total Debt/ TNW (times)	0.05	0.04
Total Debt/ OPBDIT (times)	0.17	0.15
Interest Coverage (times)	156.71	125.85

Source: Company financials and ICRA research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

		Current Rating (FY2019)				Chronology of Rating History for the past 3 years		
	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating January 2019	Date & Rating in FY2018	Date & Rating in FY2017	Date & Rating in FY2016
						-	-	-
1	Term Loan (Proposed)	Long Term	75.00	**NA**	**[ICRA]AA- (Stable)**	-	-	-

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 (Proposed)	NA	NA	NA	75.00	[ICRA]AA-(Stable)

Source: Concord Biotech Limited

ANALYST CONTACTS

K. Ravichandran
+91 44 4596 4301
ravichandran@icraindia.com

Suprio Banerjee
+91 22 6114 3443
supriob@icraindia.com

Sanket Thakkar
+91 79 4027 1528
sanket.thakkar@icraindia.com

Anuja Shah
+91 79 4027 1530
anuja.shah@icraindia.com

Pratika Bhandari
+91 79 4027 1518
pratika.bhandari@icraindia.com

RELATIONSHIP CONTACT

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

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries:

+91-124-2866928 (open Monday to Friday, from 9:30 am to 6 pm)

info@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

ICRA Limited

Corporate Office
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300
Email: info@icraindia.com
Website: www.icra.in

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

Branches

Mumbai	+ (91 22) 24331046/53/62/74/86/87
Chennai	+ (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,
Kolkata	+ (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,
Bangalore	+ (91 80) 2559 7401/4049
Ahmedabad	+ (91 79) 2658 4924/5049/2008
Hyderabad	+ (91 40) 2373 5061/7251
Pune	+ (91 20) 2556 0194/ 6606 9999