November 29, 2019

Strides Pharma Science Limited: Ratings reaffirmed and removed from watch with developing implications

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	1,094.6	-	-[1]
Long-term fund-based facilities	-	850.00	[ICRA]A+ (Stable); reaffirmed and removed from watch with developing implications
Short-term fund-based facilities	890.00	-	-[2]
Short-term non-fund-based facilities	520.00	420.00	[ICRA]A1; reaffirmed and removed from watch with developing implications
Unallocated facilities	624.41	530.00	
Total	**3,129.01**	**1,800.00**	

**Instrument details are provided in Annexure-1*

Rationale

For arriving at the ratings, ICRA has taken a consolidated view of Strides Pharma Science Limited (Strides/the company) along with its subsidiaries since all its subsidiaries operate in the same line of business and have operational linkages.

The removal of the rating watch factors in the company's divestment of its Australia business which concluded during H1 FY2020. The company's debt metrics strengthened following the same. Strides received an upfront payment of AU$ 300 mn at the closure of transaction while the balance AU$ 94 mn is expected to be received during FY2022. The company also received US$ 42 mn from full and final release of the General Claims Escrow relating to the Agila transaction. Using these proceeds, the company repaid debt of ~US$ 206 mn during H1 FY2020 resulting in improved debt indicators as on September 30, 2019. The company's Net Debt (excl.leases)/OPBDITA stood at 2.7x as on September 30, 2019 as against Net Debt/OPBDITA of 5.2x as on March 31, 2019.

The ratings continue to factor Strides' diversified business profile, the company's long track record and its strong management team. Strong manufacturing and research and development (R&D) capabilities coupled with improving front end presence further underpin the company's ratings. The company has witnessed improved operating margins supported by healthy ramp up in both the US and the company's portfolio maximization strategy in the other regulated markets division during H1 FY2020. While the company had operating margins of 15.5% during FY2019, the same had improved to 19.5% during H1 FY2020. Also, the company's ROCE improved to 11.5% in H1 FY2020 from 6.4% in FY2019. Further, in addition to improvement in its debt indicators, the company also expects to retain some part of the Australian operations' OPBDITA under the preferred supply agreement with Arrotex. This is expected to further support

[1] *ICRA had rating outstanding of [ICRA]A & on Rs.1,094.6 crore term loans of Strides earlier. This has currently been revised to nil.*

[2] *ICRA had rating outstanding of [ICRA]A1 & on Rs.890.0 crore short-term fund-based facilities of Strides earlier. This has currently been revised to nil.*

the company's revenues and margins as supplies to Arrotex reach full potential (likely to happen from Q4 FY2020/Q1 FY2021).

The ratings also take into account the weak performance of the company's emerging markets division during FY2019 and H1 FY2020. Further, significant investments in Stelis to date (~Rs.251 crore as on March 31, 2019) and going forward (incremental ~Rs.280 crore to be invested by Strides in Stelis by H1 FY2022) and returns from the same will be one of the key credit rating factors for the company. ICRA also notes that 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 company has a pending warning letter issued by the US FDA to the its Puducherry plant during May 2019. Timely resolution of the same consequent revival of operations at the Puducherry facility will be a key rating monitorable going forward.

While the company has been active in the in-organic space targeting growth and diversification through strategic acquisitions in the past, going forward also this remains an event risk and would be evaluated on a case by case basis.

Key rating drivers and their description

Credit strengths

Diversified business and geographic mix lend revenue stability: While Strides derives majority of its revenues from the US market (56% of revenues during H1 FY2020), it has been witnessing healthy ramp up in its other regulated markets portfolio (from markets like the UK, Australia, Europe etc; 27.9% of revenues in H1 FY2020) over the last few quarters. Going forward, healthy ramp up in supplies to Arrotex and continued growth in its regulated markets business is expected to support the company's business prospects. The company also has an emerging markets portfolio (both branded and institutional businesses; 16.1% of revenues in H1 FY2020) which further supports the company's geographic and business diversity. Performance of the emerging market portfolio has however been subdued during FY2019 and H1 FY2020.

Strong manufacturing and research and development (R&D) capabilities coupled with improving front end presence: Given it strong pipeline of limited competition products and its manufacturing capabilities, ICRA expects the company's revenue growth and margins to improve going forward supported by its strong performance in the US market and its portfolio maximization strategy in the other regulated markets. Further, improving front end presence across markets is expected to support the company's revenues and margins going forward.

Improvement in debt indicators during H1 FY2020: Post repaying significant amount of debt (~$206 mn) during H1 FY2020 from proceeds of its Australia exit, the company's debt indicators have significantly improved. The company's Net Debt/OPBDITA stood at 2.7x as on September 30, 2019 as against Net Debt/OPBDITA of 5.2x as on March 31, 2019. With this correction, the company's debt metrics are falling in line with medians for the rating category. However, with elevated working capital intensity (above 35% during FY2019 and H1 FY2020) given healthy growth of its US business, the company's working capital intensity and utilization of its working capital facilities continues to be relatively high. Over the 12-month period ending September 30, 2019, the company's average utilization of its fund-based working capital limits was high at 86%.

Credit challenges

Weak performance of the company's emerging markets business: Strides' emerging market business reported subdued performance during H1 FY2020 and FY2019. While some part of the revenue de-growth has been on account of the company moving away from low-margin business, Strides has also witnessed reduction in its branded generics and ARV segments on account of weak demand conditions. However, the company continued to retain its market share in the anti-malarial business wherein donor funding has witnessed a decline. While the company has taken corrective measures to improve its emerging markets business, the same is one of the key rating monitorable going forward.

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 continue to maintain steady market share, the generics industry is characterized by headwinds in the form of intense competitive pressures which may affect margins. However, the company's focus on niche segments and products with limited competition are expected to provide comfort to a certain extent.

Significant investments in Stelis: In addition to significant investments of ~Rs.251 crore which have already been made, the company has indicated that it will invest up to ~Rs.280 crore (~$ 40 mn) by H1 FY2022 in Stelis. Given that Stelis has invested heavily in developing its products, timeliness in commencement of operations and profitability of Stelis would be key credit monitarables going forward.

Warning letter for the Puducherry facility: Timely resolution of the warning letter by the USFDA and consequent revival of operations at the Puducherry facility will be one of the key rating monitorables for the company going forward.

Risk arising from inorganic growth: 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.

Liquidity position: Adequate

Strides' liquidity is **adequate** with funds flow from operations remaining positive during FY2019 in line with previous trends. However, with elevated working capital intensity given healthy growth of its US business, the company's working capital utilization continues to be relatively high. Over the 12-month period ending September 30, 2019, the company's average utilization of its fund-based working capital limits was high at 86%. That said, despite significant repayment of debt during H1 FY2020, the company continued to retain ~Rs.397 crore of free cash balances as on September 30, 2019 supporting its overall liquidity position. In terms of repayments, the company has upcoming repayments of Rs.111.4 crore in FY2021 and Rs.141.6 crore in FY2022. In addition to the same, the company has also committed to infuse up to Rs.280 crore (~$ 40 mn) in Stelis by H1 FY2022. ICRA expects Strides to be able to meet its near-term commitments comfortably through internal accruals on the basis of its current and expected financial performance.

Rating sensitivities

Positive triggers – The company's ratings could be upgraded if the company's accruals and margins improve resulting in ROCE in excess of 20% and the TD/OPBDITA is lower than 1.5x on a sustainable basis.

Negative triggers – Negative pressure on Strides' ratings could arise if any debt-funded capex/acquisitions/hive-off of profitable divisions lead to deterioration in the company's credit profile; further, drop in margins or increase in debt on account of regulatory changes or inorganic transactions respectively could also impact ratings of the company.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating methodology for pharmaceutical industry
Parent/Group Support	NA
Consolidation/Standalone	The ratings are based on the consolidated financial statements of the issuer

About the company

Incorporated in 1990, Strides Pharma Science Limited (previously known as Strides Shasun 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 soft gel capsules, tablets, capsules and semi-solids. Currently, the company's business became broadly classified into regulated markets formulations (comprising mainly the US, UK Europe and Australia etc. markets), emerging markets (primarily Africa) and institutional segments (tender-driven business mainly in developing markets). As on September 30, 2019, ~31.28% of the company's shareholding was held by the promoter group while the balance is held by various institutions and public.

Key financial indicators (Consolidated)

	FY2018	FY2019
Operating Income (Rs. crore)	2,845.1	3,011.7
Adjusted PAT (Rs. crore)	91.1	107.3
OPBDIT/OI (%)	14.1%	15.5%
RoCE (%)	5.6%	6.4%
Core RoCE (%)	6.4%	7.3%
Total Outside Liabilities/Tangible Net Worth (times)	1.5	1.8
Total Debt/OPBDIT (times)	6.3	6.9
Net Debt/OPBDIT (times)	4.7	5.2
Interest Coverage (times)	2.0	2.3

Source: Strides Pharma Science Limited

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

S.No	Name of Instrument	Current Rating (FY2020)				Chronology of Rating History for the past 3 years							
		Type	Rated amount	O/s amount as on March 31, 2019	Month-year & Rating	Month-year & Rating in FY2019		Month-year & Rating in FY2018			Month- year & Rating in FY2017		
					29-Nov 2019	Feb 07, 2019	May 28, 2018	Mar 12, 2018	Jan 02, 2018	Jul 12, 2017	Feb 28, 2017	Sep 28, 2016	Apr 05, 2016
1	Fund based facilities	LT	850.0	808.8	[ICRA] A+ (Stable)	-	-	-	-	-	-	-	-
2	Non-fund-based facilities	ST	520.0	-	[ICRA] A1	[ICRA] A1 &	[ICRA]A1	[ICRA] A1 &	[ICRA]A1+ &	[ICRA]A1+ &	[ICRA]A1+ &	[ICRA]A1+	[ICRA]A1+
3	Unallocated facilities	ST	624.41	-	[ICRA] A1	[ICRA] A1 &	[ICRA]A1	[ICRA] A1 &	[ICRA]A1+ &	[ICRA]A1+ &	[ICRA]A1+ &	[ICRA]A1+	[ICRA]A1+
4	Term Loans	LT	1,094.6	1,882.5	-	[ICRA] A+ &	[ICRA]A+ (Negative)	[ICRA] A+ &	[ICRA]A+ &	[ICRA]A+ &	[ICRA]A+ &	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)
5	Fund based facilities	ST	890.0	-	-	[ICRA] A1 &	[ICRA]A1	[ICRA] A1 &	[ICRA]A1+ &	[ICRA]A1+ &	[ICRA]A1+ &	[ICRA]A1+	[ICRA]A1+

Amount in Rs. crore

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	Fund based facilities	2018/2019	NA	NA	850.0	[ICRA]A+ (Stable)
NA	Non-fund-based facilities	2018/2019	NA	NA	420.0	[ICRA]A+ (Stable)
NA	Unallocated limits	NA	NA	NA	530.0	[ICRA]A1+

Source: the company

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Alliance Pharmacy Pty Ltd, Australia	50.99%	Full Consolidation
Altima Innovations Inc, USA	100.00%	Full Consolidation
Amneal Pharma Australia Pty Ltd, Australia	99.99%	Full Consolidation
Amneal Pharmaceuticals Pty Ltd, Australia	99.99%	Full Consolidation
Apollo Life Sciences Holdings Proprietary Limited, South Africa	51.76%	Full Consolidation
Arco Lab Private Limited, India	100.00%	Full Consolidation
Arrow Life Sciences (Malaysia Sdn. Bhd, Malaysia)	100.00%	Full Consolidation
Arrow Pharma (Private) Limited, Sri Lanka	100.00%	Full Consolidation
Arrow Pharma Life Inc, Philippines	100.00%	Full Consolidation
Arrow Pharma Pte Ltd, Singapore	100.00%	Full Consolidation
Arrow Pharma Pty Ltd, Australia	99.99%	Full Consolidation
Arrow Pharmaceuticals Pty Ltd, Australia	99.99%	Full Consolidation
Arrow Remedies Private Limited, India	100.00%	Full Consolidation
Beltapharm, S.P.A, Italy	97.94%	Full Consolidation
Fagris Medica Private Limited, India	100.00%	Full Consolidation
Generic Partners (Canada) Inc, Canada	50.99%	Full Consolidation
Generic Partners (International) Pte Ltd, Singapore	50.99%	Full Consolidation
Generic Partners (M) Sdn Bhd, Malaysia	50.99%	Full Consolidation
Generic Partners (NZ) Ltd, New Zealand	50.99%	Full Consolidation
Generic Partners (South Africa) (Pty) Ltd, South Africa	100.00%	Full Consolidation
Generic Partners Holding Co Pty Ltd, Australia	50.99%	Full Consolidation
Generic Partners Pty Ltd, Australia	50.99%	Full Consolidation
Generic Partners Ltd., UK	100.00%	Full Consolidation
Pharmacy Alliance Group Holdings Pty Ltd, Australia	50.99%	Full Consolidation
Pharmacy Alliance Investments Pty Ltd, Australia	99.99%	Full Consolidation
Pharmacy Alliance Pty Ltd, Australia	50.99%	Full Consolidation
Pharmapar Inc, Canada	80.00%	Full Consolidation
Shasun Pharma Solutions Inc, USA	100.00%	Full Consolidation
Smarterpharm Pty Ltd, Australia	50.99%	Full Consolidation
Stabilis Pharma Inc, USA	100.00%	Full Consolidation
Stelis Biopharma (Malaysia) Sdn Bhd, Malaysia	100.00%	Full Consolidation
Strides Arcolab (Australia) Pty Ltd, Australia	99.99%	Full Consolidation
Strides Arcolab International Ltd., UK	100.00%	Full Consolidation

Company Name	Ownership	Consolidation Approach
Strides CIS Ltd, Cyprus	100.00%	Full Consolidation
Strides Emerging Markets Limited, India (formerly Strides Emerging Markets Private Limited, India)	100.00%	Full Consolidation
Strides Lifesciences Limited, Nigeria	100.00%	Full Consolidation
Strides Pharma (Cyprus) Ltd, Cyprus	100.00%	Full Consolidation
Strides Pharma (SA) Pty Ltd, South Africa	60.00%	Full Consolidation
Strides Pharma Asia Pte. Ltd, Singapore	100.00%	Full Consolidation
Strides Pharma Canada Inc, Canada	100.00%	Full Consolidation
Strides Pharma Global (UK) Ltd, UK (formerly, Strides Pharma (UK) Ltd)	100.00%	Full Consolidation
Strides Pharma Global Pte Limited, Singapore	100.00%	Full Consolidation
Strides Pharma Inc., USA	100.00%	Full Consolidation
Strides Pharma International Limited, Cyprus	100.00%	Full Consolidation
Strides Pharma Therapeutics Singapore Pte Ltd, Singapore	100.00%	Full Consolidation
Strides Pharma UK Ltd, UK (formerly, Strides Shasun (UK) Ltd)	100.00%	Full Consolidation
Strides Shasun Latina Sa De CV, Mexico	80.00%	Full Consolidation
SVADS Holdings SA, Switzerland	100.00%	Full Consolidation
Trinity Pharma Proprietary Limited, South Africa	51.76%	Full Consolidation
Universal Corporation Ltd, Kenya	51.00%	Full Consolidation
Strides Vivimed Pte Ltd, Singapore (formerly, Vivimed Global Generics Pte Ltd)	100.00%	Full Consolidation
Vensun Pharmaceuticals Inc, USA	100.00%	Full Consolidation
Vivimed Life Sciences Private Limited, India	100.00%	Full Consolidation
MyPak Solutions Australia Pty Ltd, Australia (formerly, MyPak Solutions Pty Ltd)	50.495%	Equity Method
Oraderm Pharmaceuticals Pty Limited, Australia	50.00%	Equity Method
Strides Consumer Private Limited, India	53.65%	Equity Method
Strides Global Consumer Healthcare Limited, UK	53.64%	Equity Method
Aponia Laboratories Inc., USA	24.00%	Equity Method
Generic Partners (R&D) Pte Ltd, Singapore	19.35%	Equity Method
Regional Bio Equivalence Centre S.C., Ethiopia	24.98%	Equity Method
Stelis Biopharma Private Limited, India	38.56%	Equity Method

Source: the company's FY2019 annual report

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