

February 02, 2023

Micro Life Sciences Private Limited: Ratings assigned

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Long Term / Short Term-Fund Based- Working capital - Others	50.00	[ICRA]AA (Stable)/[ICRA]A1+; Assigned
Total	50.00	

*Instrument details are provided in Annexure I

Rationale

For assigning the ratings, ICRA has considered the consolidated financials of Micro Life Sciences Private Limited (Micro or the company), which includes its subsidiaries and associate companies, given the common management and significant operational and financial linkages among them. The ratings consider Micro's established market position in the medical devices industry (mainly in cardiovascular and orthopedic implants segments), and its diversified product portfolio. The company's brand presence is also aided by the product approvals from the USFDA (US Food and Drug Administration) and the European regulatory authority. The ratings also consider the extensive experience of the promoters (Bilakhia Group) in the industry. The promoter group has supported the company in the past, and is expected to continue its support, in case of any further requirements. Micro witnessed strong revenue growth during FY2018 – FY2022 (compounded annual growth rate (CAGR) of 25% during FY2018-FY2022), supported by increasing penetration in the domestic and export markets. Micro's OPM expanded to 20.5% in FY2022 from 4.0% in FY2018 backed by increased scale of operations. Further, in H1 FY2023, the company's OPM expanded by 480 bps to 25.3%, on revenues of Rs 1,088 crore, backed by continued operating leverage benefits. During H1 FY2023, the company received significant equity infusion of Rs. 1,427.5 crore and investment of Rs 472.5 crore in the form of compulsory convertible preference shares or CCPS, from a group of private equity (PE) investors (Warburg Pincus LLC, Anchorage Capital Partners, and Volrado Venture Partners). The company's debt metrics have substantially improved backed by the debt reduction from the PE fund infusion, and the net debt had turned negative as of September 30, 2022 and is expected to continue over the near term. The company had cash and liquid investments of Rs. 975.7 crore as on September 30, 2022. Further, over the longer term, higher lifestyle diseases, increased health awareness and improving affordability will benefit the company.

The ratings, however, consider the high working capital-intensive nature of operations (39.1% in FY2022 and 38.7% in H1 FY2023) due to high inventory and debtor cycles. Further, exposure of the company to regulatory risks attached to the healthcare industry, coupled with the ongoing patent infringement litigation against Meril Life Sciences Private Limited (MLSPL), a wholly-owned subsidiary of Micro (which handles the cardiovascular segment) constrains the ratings. Significant legal expenses on the litigation have already been incurred till December 2022 by Micro (~Rs. 260 crore). Any adverse outcome of the litigation which could impact the company's future business prospects and credit profile, remains a key monitorable. Further, to support business expansion, the company has sizeable capital expenditure (capex) plans of Rs.700-720 crore during FY2023-FY2025, which is expected to be funded through a mix of debt and accruals. The ratings also consider the moderate scale of operations and low profitability of the diagnostic and endo-surgery business, and the stiff competition from other established players in the industry.

The company derives ~50% of its consolidated revenues from the export markets. As the company is expected to focus more on the export markets over the near term, any adverse fluctuations in foreign currency will have an impact on the profitability of the company. Any significant debt-funded expansion plans, impacting the Group's credit metrics or liquidity position, shall remain an event risk and would be evaluated on a case-by-case basis.

The Stable outlook on the long-term rating reflects ICRA's expectation that the company will continue to benefit from its established presence in the medical devices industry, coupled with its strong financial profile characterised by healthy revenue growth and operating margins and strong liquidity position.

Key rating drivers and their description

Credit strengths

Established presence in the medical products and devices industry with diversified product portfolio – Micro operates in four major business segments in the medical device industry through its wholly-owned subsidiaries. At a consolidated level, the vascular intervention segment (which includes stents, heart valves and balloon catheter) contributes ~45-50% of the company's revenues, the orthopaedic segment (includes knee and hip implants) contributes ~35-40% and the balance ~10-15% is contributed by the diagnostics (includes medical instruments, test kits and reagents) and endo-surgery (includes sutures and closures) segments. Apart from this, Micro has also commenced trading of surgical robots from FY2021. ICRA notes that the company has designed and manufactured India's first indigenous heart valve - Myval. The product is Drug Controller General of India (DCGI) approved and CE-certified, and Micro presently sells this in various European countries apart from catering to the domestic market, where it commands a strong brand position. Further, many of its knee implants are also CE-certified and USFDA approved, which have supported the market penetration in the recent past. Meril Diagnostics Private Limited (MDPL), subsidiary of Micro, is a registered vendor with World Health Organization (WHO) for providing various diagnostic kits. Further, it launched the Covid-19 test kits in India post the pandemic, which supported the company's performance in FY2021 and FY2022. The established brand position of the company's products in the market, is expected to support healthy revenue growth and margins, over the medium term. The company's products (mainly cardio and orthopaedic) are sold in over 100 countries (exports contribute ~46% of the company's revenues in FY2022). Going forward, the company expects the contribution from export sales to increase with increasing focus on capturing potential opportunities in such markets.

Experienced and strong promoter group – Bilakhia Holdings Private Limited (BHPL) is the holding company of the Bilakhia Group. The Group entered the healthcare sector in 2006. The promoter group had infused funds into Micro in the past, by way of non-convertible preference shares and unsecured loans for supporting its operational/debt servicing requirements, which was primarily repaid in H1 FY2023, following receipt of private equity investment. At present, BHPL owns an 89.06% stake in Micro (on a fully-diluted basis, post-CCPS conversion of PE investors, promoter group stake will be 85.95%). Going forward, the extensive experience of the promoters and the management team will continue to support Micro's operations.

Financial profile characterised by robust improvement in revenues and healthy margins; sizeable equity infusion in H1 FY2023, led to sharp improvement in debt metrics – Micro witnessed strong revenue growth (CAGR of 25%) during FY2018-FY2022 on the back of improved penetration in the domestic as well as export markets. While the revenues were impacted in FY2021 (de-growth of 11.5%) due to the pandemic, pent-up demand for deferred procedures (knee/hip replacements and other elective surgeries) and increase in the diagnostic segment revenues from Covid-19 test kits, aided 61.7% revenue growth in FY2022. The OPM expanded to 20.5% in FY2022 from 4.0% in FY2018, supported by increased scale of operations. Further, in H1 FY2023, the company's OPM expanded by 480 bps to 25.3%, backed by continued operating leverage benefits. The company also received substantial investment from private equity investors of Rs 1,900 crore in H1 FY2023, which led to a sharp improvement in its debt metrics. Of the total investment, ~Rs 950 crore was utilised to repay promoter-level debt (preference shares and unsecured loans) and the balance is being held in the form of bank fixed deposits. The same is expected to be utilised as growth capital for expansion requirements (including clinical trials for product development and launch). As of September 30, 2022, the company had turned net-debt negative, backed by its strong liquidity position. Further, the debt metrics improved sharply in H1 FY2023. Going forward, healthy revenue growth is expected to continue aided by improving market share and increasing demand for medical products and devices. Further, the company is expected to maintain healthy operating margins, which would also be supported by backward integration benefits. Also, the company is expected to remain net-debt negative, backed by healthy accruals, strong liquidity and no major debt-funded expansion plans over the near term.

Healthy long-term industry outlook – The company operates in an industry that is generally considered to be resistant to inflation and primarily consists of non-discretionary products. The demand for healthcare products and devices is expected to remain high due to increasing lifestyle diseases. Further, increased health awareness and improving affordability of treatments are expected to drive the industry growth. In the domestic market, the increasing penetration of health insurance will support the industry. Further, the healthcare industry in developing countries which are under-penetrated at present, poses growth opportunity for the company and the broader industry.

Credit challenges

High working capital intensity of operations – Micro's net working capital (NWC) intensity (NWC/operating income) remained high at 39.1% in FY2022 and 38.7% in H1 FY2023, primarily owing to high inventory stocking requirements and moderately high receivable days. As the company operates in multiple segments of medical devices, and has a wide range of product portfolio, Micro needs to maintain multiple SKUs (stock keeping unit) to meet customer requirements. This leads to high inventory holding i.e., 204 days and 186 days as of March 31, 2022, and September 30, 2022, respectively. Further, the company's debtor days remained at 107 and 91 as of March 31, 2022, and September 30, 2022, respectively, thereby increasing the WC cycle. Going forward, the working capital intensity is expected to remain high, in view of the higher inventory requirements and moderately high debtor cycle.

Exposure to regulatory risks – Akin to other industry players, Micro is exposed to regulatory risks pertaining to pricing restrictions, medical liabilities due to faulty products, approval timelines for new product developments and various compliance norms. The pricing for stents and knee implants is capped by the National Pharmaceutical Pricing Authority (NPPA) in the domestic market. Last notification from the NPPA for orthopaedic knee implants was issued on September 10, 2021, which was applicable till September 15, 2022. The same was further extended for one year by the NPPA. The inclusion of products on the NPPA list reduces the company's pricing flexibility and any future inclusion of key products on the list will likely affect the company's profitability. Further, any medical liabilities from patients/hospitals, due to faulty implants could impact Micro's accruals. However, Micro has a product liability insurance cover in place, which mitigates such liability to certain extent.

Ongoing patent infringement litigation – MLSPL, a wholly-owned subsidiary of Micro, is involved in a patent infringement lawsuit filed by one of its competitors in the US and certain European countries for heart valve (MyVal). The dispute began in April 2019 when the competitor accused MLSPL of infringing on trademark and multiple patents, however, the company has claimed that it is not in violation of any patents and is contesting the lawsuit. The company had incurred significant legal expenses of ~Rs. 260 crore till December 2022, for this litigation and expects to incur legal cost of ~Rs 50-60 crore per annum over the near term. The outcome of this litigation remains a key monitorable, as any adverse outcome could lead to revenue loss of MyVal, thereby impacting the company's profitability. Further, any significant settlement claims could impact the liquidity position of the company.

Sizeable capex plans of the Group; some businesses are still in early stages of operations – The company plans to incur sizeable capex of ~Rs. 700-720 crore during FY2023 to FY2025. This investment will primarily focus on expanding its manufacturing capacities. The capex is expected to be funded predominantly through debt. Further, in terms of revenues and profitability, the diagnostic (MDPL) and endo-surgery (Meril Endo-Surgery Private Limited or MEPL) businesses are in their early stages of operations, incurring operating/net loss (endo surgery is incurring PAT losses and diagnostic business is yet to breakeven at OPM level). While the diagnostic business had improved substantially in FY2021 and FY2022 backed by Covid-tests, operating losses were incurred in H1 FY2023. The company has deployed its salesforce to build its brand position, which is expected to support the increase in revenues from these businesses; however, the turnaround of operations in these segments remains monitorable. ICRA draws comfort from the anticipated healthy accruals from Micro's business over the medium term and strong liquidity position of the company, despite its high capex plans and moderate operations of the diagnostic/endo-surgery business.

Stiff competition in the industry – The company is exposed to stiff competition from other domestic as well as established international players in the medical devices industry. Further pricing pressures, if any, could impact the profitability. However, ICRA notes that the company has been able to establish its market position, demonstrated by its strong growth and expansion in operating profit margins over the years.

Liquidity position: Strong

The company's consolidated liquidity position was characterised by free cash and liquid investments of Rs 975.7 crore as of September 30, 2022. Further, the company had undrawn available working capital limits of ~Rs. 340 crore as on July 31, 2022. Average working capital utilisation remained moderate at 40% for the 12-month period ending July 2022. The company's long-term repayment obligations are moderately low at Rs. 54 crore, Rs. 30 crore and Rs. 21 crore during FY2023, FY2024 and FY2025, respectively, on the existing term debt. Micro's capex plans are high at ~Rs. 700-720 crore during FY2023-FY2025, which is expected to be funded predominantly through term loans. Going forward, ICRA expects the liquidity position to remain strong, backed by anticipated healthy accruals from its business operations.

Rating sensitivities

Positive factors – The ratings can be upgraded, if there is any significant improvement in the company's scale of operations, aided by strengthening of market position in addressable segments along with greater business diversity. In addition, the company's ability to generate healthy profitability indicators, while improving working capital intensity and maintaining strong credit metrics will also be critical.

Negative factors – Pressure on the ratings could arise with contraction in profit margins and/or deterioration in working capital intensity, which could impact the company's credit profile, liquidity position or debt metrics. Any material adverse impact of the alleged patent infringement litigation will also trigger a downgrade. A specific metric for a downgrade is if Net Debt/OPBDITA is greater than 1 time, on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Approach - Consolidation
Parent/Group Support	NA
Consolidation/Standalone	For arriving at the ratings, ICRA has taken consolidated financial statement of Micro, which includes its subsidiaries and associate companies, while assigning the credit ratings, given the common management and significant operational and financial linkages among them, as mentioned in Annexure II.

About the company

Micro is the holding company for the healthcare segment of the Bilakhia Group. It is a subsidiary of BHPL, which is the ultimate holding company of the Group. At present, BHPL owns an 89.06% stake in Micro. The company received PE investment of Rs. 1,900 crore in H1 FY2023, of which Rs. 1,427.5 crore was equity infusion and Rs 472.5 crore was in the form of CCPS. The CCPS is expected to be converted into equity at a predetermined conversion ratio, depending on a mutually agreed milestone achievement. On a fully-diluted basis (considering CCPS conversion, post-milestone achievement), private equity investors will hold a 14.05% equity stake in the company. There are no terms attached to the PE investment, viz. repayment, exit terms, buyback, or guaranteed returns. On a fully-diluted basis, post CCPS conversion of PE investors, promoter group stake will be 85.95%.

Micro, through its wholly-owned domestic subsidiaries is involved in design and development of medical products and devices. The company caters to segments like cardiovascular, orthopaedic, diagnostic and endo-surgery. The company has marketing

offices in various countries like Germany, Turkey, the US, Russia, South Africa, Brazil, Bangladesh, Australia, China, and the UK, which is handled by its foreign subsidiaries.

Key financial indicators

Micro Consolidated	FY2021	FY2022	H1 FY2023
Operating income (Rs. crore)	1,032.3	1,669.6	1,088.0
PAT (Rs. crore)	(107.9)	151.7	152.1
OPBDITA/OI (%)	13.1%	20.5%	25.3%
PAT/OI (%)	-10.5%	9.1%	14.0%
Total outside liabilities/Tangible net worth (times)	(3.4)	(5.2)	0.7
Total debt/OPBDITA (times)	11.6	4.5	1.2
Net debt/OPBDITA (times)	11.3	4.3	(1.2)
Interest coverage (times)	1.6	4.5	8.0

PAT: Profit after Tax; OPBDITA: Operating Profit before Depreciation, Interest, Taxes and Amortisation; All amounts as per ICRA calculations

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Type	Current rating (FY2023)		Chronology of rating history for the past 3 years			
		Amount Rated (Rs. crore)	Amount outstanding as of Sep 30, 2022 (Rs. crore)	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020
				Feb 2, 2023	-	-	-
1 Fund based – Working capital others	Long-term/Short-term	50.00	--	[ICRA]AA (Stable)/[ICRA]A1+	-	-	-

Amount in Rs. Crore

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long term/Short term – Fund based – Working capital others	Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: [Click Here](#)

Annexure I: Instrument details

ISIN No	Instrument Name	Date of Issuance	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Long/short term – Fund based – Working capital others	FY2022	NA	NA	50.00	[ICRA]AA (Stable)/[ICRA]A1+

Source: Company; Note: Amounts in Rs. crore

[Please click here to view details of lender-wise facilities rated by ICRA](#)

Annexure II: List of entities considered for consolidated analysis

Company Name	Micro Ownership	Consolidation Approach
Meril Life Sciences Private Limited	100%	Full Consolidation
Meril Life Sciences India Private Limited	100%	Full Consolidation
Meril Diagnostics Private Limited	100%	Full Consolidation
Meril Healthcare Private Limited	100%	Full Consolidation
Meril Endo Surgery Private Limited	100%	Full Consolidation
Meril GmbH, Germany	100%	Full Consolidation
Doc Med Comercio Importacao Exportacao LTDA, Brazil	99.99%	Full Consolidation
Meril Tibbi Cihazlar Imalat Ve Ticaret Anonim Sirketi, Turkey	100%	Full Consolidation
Meril INC, USA	100%	Full Consolidation
Meril Medical LLC, Russia	100%	Full Consolidation
Meril Bangladesh Pvt Ltd	99.99%	Full Consolidation
Meril SA Pty Ltd, South Africa	100%	Full Consolidation
Meril Australia Pty Ltd., Australia	100%	Full Consolidation
Meril Cardiology Pty Ltd., South Africa	100%	Full Consolidation
Meril (China) Co. Limited, China	100%	Full Consolidation
Meril UK Limited	100%	Full Consolidation
Maxx Medical Pte Ltd, Singapore	45%	Equity method

Source: company [annual report FY2022](#)

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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.

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