September 28, 2023

Granules India Limited: Long-term rating assigned and short-term rating reaffirmed; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund-based – term loan	-	199.80	[ICRA]AA- (Stable); assigned
Long-term short-term fund-based/ non-fund based limits	-	1,324.00	[ICRA]AA- (Stable)/[ICRA]A1+; assigned
Unallocated limits	-	226.20	[ICRA]AA- (Stable)/[ICRA]A1+; assigned/reaffirmed
Unallocated limits	50.00	-	-
Total	**50.00**	**1,750.00**	

**Instrument details are provided in Annexure-I*

Rationale

The long-term rating assigned to Granules India Limited (GIL) factors in its established operational track record and business position in the pharmaceutical industry, its integrated manufacturing operations and sizeable manufacturing capacities. These factors have supported the company to achieve leading market share across its key products like paracetamol, metformin, ibuprofen, guaifenesin and methocarbamol. GIL's revenue has expanded at a CAGR of ~21% over the last six years and the momentum is likely to sustain, supported by its increasing footprint in Europe and new product launches. Moreover, GIL's profit margins are supported by its low-cost manufacturing due to economies of scale, steady transition of revenues from a relatively lower margin segment (active pharmaceutical ingredients, or APIs) to a more margin-accretive segment (finished dosages, or FDs), and significant backward integration with APIs of four of the five key molecules being manufactured in-house. For its key products, GIL has a dominant market share in the US and is making significant inroads into other regions like Europe, which is expected to support its growth and margins, going forward.

The ratings also factor in GIL's comfortable capital structure and coverage metrics, supported by steady accrual generation and no major increase in debt levels in the past two fiscals. ICRA notes GIL's capex commitment of around Rs. 2,000 crore over the next five years, towards setting up facilities in Kakinada (Andhra Pradesh), as part of its green chemicals manufacturing initiative in partnership with Greenko ZeroC Private Limited (Greenko). In addition to the positive impact on the environment from the use of green power and green chemicals, the project is expected to be margin accretive for GIL as it expects to manufacture key starting materials (KSMs) for its key APIs as well as intermediates in this facility. Despite partial debt funding of this planned capex, GIL's debt protection metrics are expected to remain healthy with net debt/OPBDIT of ~1.0 times over the next few years.

The ratings are, however, constrained by the high product concentration risk in mature generic molecules with its top-five products generating 80-85% of its total sales in recent years. However, GIL's established market position and a healthy market share in most of these key molecules mitigate the risk to a certain extent. GIL's profitability is vulnerable to high competitive intensity of the industry and volatility in raw material prices. However, strong market share in key molecules, increasing economies of scale and continued initiatives to enhance backward integration have supported the company's operating margins in recent years. With North America and Europe driving 70-80% of its revenues in recent years, GIL is also exposed to regulatory risks and litigations as well as scrutiny by various agencies like the US FDA and the EU GMP. However, ICRA notes the company's clean track record with minimal observations in prior as well as recently concluded inspections.

The Stable outlook on the long-term rating indicates ICRA's opinion that GIL shall continue to maintain its healthy credit profile supported by its leadership position across its key molecules, backward integration of operations and economies of scale translating into healthy internal accrual generation.

Key rating drivers and their description

Credit strengths

Established operational track record and business position in the pharmaceutical industry, supported by global leadership in paracetamol and other key molecules – GIL is an established player in the pharmaceutical industry, with a leadership position in some first line of defence, mature generic molecules like paracetamol, metformin and ibuprofen. For these molecules, GIL has an established market position in the US with established relationships with several reputable players in the market.

Healthy revenue growth supported by growth across key molecules; momentum expected to sustain – GIL has witnessed a healthy revenue expansion at a CAGR of ~21% over the past six years, supported by steady growth for some of its key molecules including paracetamol and metformin in key markets like North America, Europe and Latin America. Moreover, the growth momentum is expected to sustain over the near to medium term, supported by increasing sales of its existing key molecules, increased penetration in key markets and rising revenue contribution from new launches. The recently commissioned multi-unit pellet system (MUPS) facility in Gagillapur (Telangana) and the upcoming FD facility in Hyderabad are also expected to support GIL's growth momentum. ICRA also notes the information security incident in May 2023, which impacted GIL's operations to some extent in Q1 FY2024; however, the measures taken by the company resulted in restoration of production activities to a large extent by first half of July 2023. While this disruption is likely to have a short-term impact on GIL's revenue, the overall growth is expected to remain healthy.

Margins supported by backward integration and economies of scale – Over the years, GIL has been able to largely maintain its operating margins (18-20% range), supported by significant backward integration with in-house manufacturing of four out of five key APIs and economies of scale from its sizeable manufacturing capacities at the Gagillapur and Bonthapally (Telangana) facilities. Although GIL started out as an API manufacturer, over the years it integrated its operations to manufacture FDs, which have generated ~50% of its revenues in recent years. Moreover, the commissioning of the MUPS facility and the upcoming FD facility in Hyderabad, is expected to further support its FD sales, which provide better margins. Despite some volatility due to unpredictable raw material prices and forex risks, the margins are expected to remain healthy (notwithstanding some moderation in the near term due to the information security incident), supported by its increasing backward integration (in the Kakinada project) and cost-optimisation initiatives.

Comfortable capital structure and coverage metrics – Steady internal accrual generation and no major increase in debt levels in recent years have resulted in a comfortable capital structure and coverage metrics, marked by low gearing of 0.4 times as on March 31, 2023, and total debt/OPBDIT of 1.2 times (net debt/OPBDIT of 0.9 time) and interest cover of 16.5 times for FY2023. GIL is likely to incur capex of ~Rs. 2,000 crore over the next few years, which is expected to be funded through a mix of internal accruals and debt. However, despite the same, its debt protection metrics are expected to remain healthy, with net debt/OPBDIT of around 1.0 times over the next few years.

Credit challenges

High product concentration risk in mature molecules, although mitigated to some extent by healthy market share in these molecules – GIL's top-five molecules are first line of defence mature generic molecules. The company is exposed to product concentration risk as these molecules have continued to account for 80-85% of its revenues in recent years. Moreover, a significant share of GIL's revenue is generated by North America (~52-57%) and Europe (18-23%), which have witnessed continued pricing pressure over the recent past, which is likely to sustain. However, the risk is mitigated to a certain extent by GIL's market leadership for some of these key molecules in its key markets. Moreover, the company has focussed on enhancing its footprint in Europe and Latin America. With increased focus on R&D, new launches are expected to improve, going forward. However, a few key molecules will continue to contribute meaningfully to the revenues.

Vulnerability of profitability to volatility in raw material prices – GIL's profitability continues to be vulnerable to volatility in raw material prices, though its backward-integrated operations provide some comfort. ICRA also notes GIL's capex plan in Kakinada (Andhra Pradesh) for manufacturing KSMs of its key products like paracetamol and metformin, which is expected to further support its profitability against volatility in raw material prices over the medium to long term.

Exposure to regulatory risks and litigations; however, GIL has had a successful track record of inspections – Not unlike its peers, GIL remains exposed to regulatory risks and litigations including scrutiny by agencies like the US FDA and the EU GMP. Considering the US contributed ~50% to its revenue in FY2023, scrutiny by the US FDA continues to be key for its overall operations. However, comfort can be drawn from GIL's successful track record with regulatory agencies including the US FDA. GIL's Gagilapur (Telangana) facility, which had received a Form 483 with three observations by the US FDA post inspection in January 2023, has subsequently received an establishment inspection report. Moreover, its two other facilities at Jeedimetla (Telangana) and Visakhapatnam (Andhra Pradesh) also completed the US FDA inspections in June 2023 with zero Form 483 observations.

Environmental and Social Risks

Environmental considerations – GIL does not face any major physical climate risk. However, it remains exposed to tightening environmental regulations regarding the breach of waste and pollution norms, which can lead to an increase in operating costs and new capacity instalment costs. This can also require capital investments to upgrade its effluent treatment infrastructure to reduce its carbon footprint and waste generation. GIL is developing processes that reduce resources, minimise wastage and eliminate the use of hazardous substances. It is also increasing its share of renewable energy every year by installing solar panels at plant locations. Further, GIL is focusing on exploring green chemistry initiatives such as enzymatic biotransformation, non-halogenated solvent and solvent recovery, among others, and reducing dependence on groundwater through water conservation techniques like rainwater harvesting, recycling, and effluent water treatment. GIL is also working with its top-10 carbon intensive suppliers to reduce its scope-3 carbon emissions. It recently signed an MoU with Greenko for a partnership for supply power, hydrogen, ammonia, nitric acid and a few other chemicals, which will all be carbon free.

Social concerns – GIL faces high industry-wide social risks related to product safety and its associated litigation risks, access to qualified personnel for R&D and process engineering, as well as for maintenance of high manufacturing compliance standards. Further, Government interventions related to price caps/controls also remain a social risk for entities in the pharmaceutical industry.

Liquidity position: Adequate

GIL's liquidity position is **adequate**, supported by healthy cash accruals and unencumbered cash balances and liquid investments of Rs. 291.6 crore (as on March 31, 2023). Moreover, the liquidity is supported by undrawn working capital limits of around Rs. 480 crore (as on March 31, 2023). GIL has planned capex of ~Rs. 700 crore in FY2024 and term loan repayments of around Rs. 90-100 crore each in FY2024 and FY2025. The obligations are expected to be fulfilled by a mix of internal accruals and debt.

Rating sensitivities

Positive factors – The long-term rating could be upgraded, if the company demonstrates healthy growth in its revenues and accrual generation and strengthening of its liquidity position and coverage metrics. In addition, improved product diversity shall also be considered favourably for a rating upgrade. A specific credit metric for an upgrade is if Total debt/OPBDITA is less than 1.0 times, on a sustained basis.

Negative factors – The rating of the company is likely to be downgraded if there is any significant weakening of its profit margins or an increase in its working capital intensity, leading to deterioration in its liquidity profile, on a sustained basis. Any regulatory non-compliance issued to GIL for its products and/or manufacturing facilities, impacting its product launches and, thus, its revenues and profitability, would also be a negative trigger.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	[Corporate Credit Rating Methodology] [Rating Methodology for entities in the Pharmaceutical Sector]
Parent/Group support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of GIL. As on March 31, 2023, GIL had six subsidiaries, which are enlisted in Annexure-II.

About the company

GIL was incorporated as a private limited company in 1991 and was later converted into a public limited company in 1993. It started out as a merchant exporter of bulk drugs like paracetamol, guaifenesin and chloro pheniramine maleate. At present, GIL manufactures APIs, pharmaceutical formulation intermediates (PFIs) and FDs, which are marketed to more than 300 customers across more than 80 countries, primarily in North America, Europe, Asia and Latin America.

GIL has seven manufacturing plants across Hyderabad, Visakhapatnam and Virginia (USA), and two R&D centres in Hyderabad and Virginia, with an installed manufacturing capacity of 39,360 TPA of API, 24,640 TPA of PFI and 23.3 billion dosages of FDs.

Key financial indicators (audited)

GIL – Consolidated	FY2022	FY2023
Operating income	3,764.9	4,511.9
PAT	412.8	516.6
OPBDIT/OI	19.5%	20.4%
PAT/OI	11.0%	11.4%
Total outside liabilities/Tangible net worth (times)	0.7	0.7
Total debt/OPBDIT (times)	1.5	1.2
Interest coverage (times)	31.6	16.5

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2024)					Chronology of rating history for the past 3 years	
		Type	Amount rated (Rs. crore)	Amount outstanding as of Aug 31, 2023 (Rs. crore)	Date & rating in FY2024		Date & rating in FY2022	Date & rating in FY2021
					September 28, 2023	August 07, 2023	-	-
1	**Term loan**	Long-term	199.80	199.80	**[ICRA]AA- (Stable)**		-	-
2	**Fund-based/ non-fund based limits**	Long term/ short term	1,324.00	-	**[ICRA]AA-(Stable)/ [ICRA]A1+**		-	-
3	**Unallocated limits**	Long term/ short term	226.20	-	**[ICRA]AA-(Stable)/ [ICRA]A1+**		-	-
4	**Unallocated limits**	Short term	-	-	**-**	[ICRA]A1+	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund based – term loan	Simple
Long-term short-term fund-based/ non-fund based limits	Simple
Unallocated limits	NA

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	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Term loan 1**	January 2020	6M Euribor + 1.0%	January 2026	135.00	[ICRA]AA- (Stable)
NA	**Term loan 2**	July 2021	6M Euribor + 0.8%	January 2026	64.80	[ICRA]AA- (Stable)
NA	**Working capital facilities**	NA	NA	NA	890.00	[ICRA]AA-(Stable)/ [ICRA]A1+
NA	**Proposed working capital facilities**	NA	NA	NA	434.00	[ICRA]AA- (Stable)/ [ICRA]A1+
NA	**Unallocated**	NA	NA	NA	226.20	[ICRA]AA- (Stable)/ [ICRA]A1+

Source: Company

Please click here to view details of lender-wise facilities rated by ICRA

Annexure II: List of entities considered for consolidated analysis

Company Name	Lupin Ownership	Consolidation Approach
Granules USA Inc	100.00%	Full Consolidation
Granules Consumer Health, Inc.	100.00%	Full Consolidation
Granules Pharmaceuticals Inc	100.00%	Full Consolidation
Granules Europe Limited	100.00%	Full Consolidation
Granules Lifesciences Private Limited	100.00%	Full Consolidation
Granules CZRO Private Limited	100.00%	Full Consolidation

Source: FY2023 annual report

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About ICRA Limited:

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