January 30, 2025

Aarti Drugs Limited: Ratings 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	209.09	302.80	[ICRA]AA- (stable); reaffirmed/ assigned
Long-term: Fund-based CC	65.00	65.00	[ICRA]AA- (stable); reaffirmed
Short-term: Fund-based/ Non-fund based facilities	1,085.00	1,085.00	[ICRA]A1+; reaffirmed
Total	**1,359.09**	**1,452.80**	

**Instrument details are provided in Annexure I*

Rationale

The ratings continue to consider Aarti Drugs Limited's (ADL/the company) experienced management and its long and established track record in the active pharmaceutical ingredients (APIs), intermediates, speciality chemicals and formulations space. Moreover, ADL's strong market position as one of the largest domestic and global manufacturers of most of its key products also provides comfort. ADL derives significant operational efficiencies from large installed capacities and backward integration of intermediates and related chemicals supporting its operations. The ratings also take comfort from ADL's diversified and reputed client base, including major pharmaceutical players. ICRA notes that ADL has recently received the Establishment Inspection Report (EIR) from the USFDA for its Tarapur facility, which had an import alert since 2015. ADL has also received the UK Medicines and Healthcare products Regulatory Agency's (MHRA) approval for its formulation facility in Baddi, Himachal Pradesh. These approvals are expected to support ADL's business prospects in the regulated markets going forward.

ADL's revenue declined 6.9% in FY2024 to Rs. 2,528.6 crore due to a 9.1% contraction in its API segment, mainly due to overstocking issues and relatively lower demand from export markets. The decline in consolidated revenues continued in H1 FY2025 with the company witnessing a 11.4% YoY decline in revenues. Despite volume growth, the company witnessed a decline in revenues led by a negative rate variance of 7-8% in H1 FY2025. The company's operating margin improved by 130 bps to 12.7% YoY in FY2024, supported by a correction in raw material prices for the API segment. However, the same moderated to 11.4% in H1 FY2025 due to subdued demand from export sales which typically entail relatively higher margins in addition to the impact of a high-cost inventory in a declining raw material price environment. While the API prices continued to correct in H1 FY2025, the performance of the API segment is expected to stabilise in H2 FY2025, driven by healthy volume growth and revival of export demand. Stabilisation of raw material prices, coupled with healthy operating leverage and increased cost efficiency with various backward integration initiatives, is expected to support margin expansion going forward. Additionally, the ramp-up of commercial operations for margin-accretive products from greenfield capacities is also expected to support the margins going forward.

The company is expected to incur a capex of ~Rs. 220-230 crore in FY2025, funded through a mix of debt and internal accruals and ~Rs. 150-160 crore in FY2026, funded through internal accruals. This is mainly towards setting up two greenfield facilities (salicylic acid and amine plants), various brownfield expansions, debottlenecking and maintenance capex. The ongoing debt-funded capex is expected to moderate the debt metrics to a certain extent. A timely ramp-up of operations for the newly added capacities and its impact on the company's credit metrics remain monitorable.

The ratings remain constrained by moderately high working capital intensity because of large receivables and inventory holding period, as ADL maintains safety stock for various raw materials and finished goods for uninterrupted flow of supplies. ADL's profitability is also exposed to regulatory risks, fluctuations in raw material prices and limited pricing flexibility due to a large share of the mature molecule portfolio. The risk is mitigated to an extent by its leading market position and backward integration in related intermediates that protect the profitability to an extent. ICRA also notes that the company has carried out ~Rs. 60.0 crore (Rs. 73.2 crore including the tax on the buyback) of share buyback in the current fiscal, which is in line with past trends. Going forward, any significant shareholder payout impacting the company's liquidity position and credit metrics remains a key monitorable.

ICRA notes the company's BSE disclosure dated January 28, 2025, pertaining to provisional attachment (debit freeze) by the Office of Joint Commissioner of State Tax, Investigation-B, Mumbai on operative bank accounts held by the company in Union Bank of India and State Bank of India. This order is issued pursuant to the intimation of tax ascertained amounting to Rs. 13.36 Crores along with applicable interest and penalty. ICRA understands from the management that these two accounts are largely non-operative and the company's debt servicing will not be impacted since the debt servicing obligations are not routed through these accounts. Further, the bankers have also confirmed that there is no freeze on any other bank accounts of the company. ICRA will continue to monitor any developments on the same and take appropriate rating action, if necessary.

The Stable outlook on the long-term rating reflects ICRA's opinion that, although realisations are expected to impact the revenue growth in FY2025 to a certain extent, the same will be offset by healthy volume growth driven by stable domestic demand, incremental capacities from ongoing brownfield and greenfield expansions, and an anticipated demand revival from export markets. Further, while the ongoing debt-funded capex is expected to moderate debt metrics to a certain extent, the same are expected to remain healthy.

Key rating drivers and their description

Credit strengths

Established bulk drug player with strong presence in therapeutic segments along with sizeable market share in key molecules – The company caters to 12 therapeutic groups, including antibiotic, antidiarrheal, antifungal, antidiabetic, anti-inflammatory, cardioprotective, vitamins and anti-arthritis, among others. The top three therapeutic segments—viz., antibiotic, antidiarrheal and antidiabetic contributed ~67% of the company's revenues in FY2024. The company remains one of the leaders in fluoroquinolones under antibiotic therapy on the back of strong backward integration and cost-efficient manufacturing supported by large capacities. ADL has a growing presence in antifungal and cardioprotective therapies as well. Its top five products, namely Ciprofloxacin, Ofloxacin, Metronidazole, Metformin and Ketoconazole, generated ~53% of its revenues in FY2024. ADL has a sizeable market share as the largest domestic and global manufacturer for most of its key products.

Diversified client mix; export customers across 100 countries – ADL's customer base is diversified, as the top 10 customers contributed 15.7% to its revenues in FY2024. Its client profile includes reputed domestic as well as export end-customers and distributors. Export sales comprised ~38% of ADL's consolidated revenues in FY2024. Its exports are diversified across 100 countries in Latin America, Asia Pacific, Europe and Africa.

Healthy financial risk profile – The company's debt primarily comprises working capital debt and term loans, with the latter contributing over 50% due to the ongoing large capex towards setting up incremental capacities. ADL's total debt increased to Rs. 590.1 crore as on September 30, 2024. This, combined with a decline in operating margins, led to the moderation of debt metrics to a certain extent. TD/OPBDITA as on September 30, 2024, increased to 2.2 times from 1.8 times as on March 31, 2024. The company's gearing remained unchanged at 0.5 times for the same period. While the ongoing and planned debt-funded capex is expected to impact the debt metrics to a certain extent going forward, the same is expected to remain healthy, driven by a revival in margins following the stabilisation in raw material prices and improvement in exports.

Favourable growth outlook in near-to-medium term, supported by greenfield and brownfield expansion projects – The company witnessed a YoY revenue decline of 6.9% and 11.4% in FY2024 and H1 FY2025, respectively, led by negative price variance due to correction in raw material and API prices and weak export demand. ADL is expected to witness stabilisation in realisations in H2 FY2025 for the API segment. This will also be supported by continued healthy demand from the domestic market, incremental capacities available from various brownfield expansions for key molecules and anticipated revival in export demand. Additionally, the benefits of ongoing greenfield projects for salicylic acid and amine plants will support the company's growth prospects in the medium term.

Credit challenges

Significant near-term debt-funded capex – The company is expected to incur a capex of ~Rs. 220-230 crore in FY2025 and ~Rs. 150 crore in FY2026, which will be funded through a mix of debt and internal accruals. This is mainly allocated towards setting up two greenfield facilities (salicylic acid and amine plants) with an average gestation period of 18-24 months, various brownfield expansions for key molecules, debottlenecking and maintenance capex. The debt-funded capex is expected to moderate the debt metrics to certain extent and the timely ramp-up of operations for the newly added capacities and its impact on the company's profitability along with its credit metrics remain a key monitorable. However, the company's proven track record of successfully implementing similar projects and its leading market position in addressable molecules provide comfort.

Moderately high working capital intensity – The company's working capital intensity remained moderately high at 33% in H1 FY2025 and 32.8% in FY2024. Its operations remain working capital intensive, which is essential for its growth, as the company generally maintains ~90 days of inventory that includes various raw materials and finished goods to maintain uninterrupted supplies to its customers. In addition, ADL's debtor days remain at 90-110 days due to its sizeable portion of export sales, making the company's operations working capital intensive. Going forward, the working capital intensity is expected to remain in line with past trends.

Profitability remains exposed to regulatory risks and fluctuations in raw material prices – The company is exposed to regulatory risks like manufacturing facility approvals and local manufacturing requirements by various Government authorities, as part of a regulated industry amid an evolving landscape. At present, regulators all over the globe are becoming more stringent with allowed levels of nitrosamines in pharmaceutical products, an industry-wide phenomenon, which might entail higher operating costs for pharmaceutical entities going forward. Further, the company's profitability remains vulnerable to packaging and freight costs in addition to volatility in raw material prices. However, backward integration for its key molecules, and operational efficiencies from large established capacities mitigate this risk to a certain extent.

Environmental and social risks

Environmental considerations – The company does not face any major physical climate risk. However, it remains exposed to tightening environmental regulations with regard to breach of waste and pollution norms, which can lead to an increase in operating costs or capital investments. The company is dedicated to minimising its environmental footprint and is consistently improving its operations, reducing its energy consumption and efficiently managing its waste and emissions. ADL also has plans for the installation of solar power plants at its key facilities. To meet the green energy needs and optimise energy costs, the company will acquire a 26.25% equity stake in a special purpose vehicle (SPV), Pro-Zeal Green Power Six Private Limited, as per electricity laws. The solar power generated by the SPV will be supplied to ADL for its captive consumption.

Social considerations – The industry faces social risks related to product safety and the associated litigation risks, access to qualified personnel for R&D and process engineering and maintenance of high manufacturing compliance standards. Further, Government intervention related to price caps/control also remains a social risk faced by entities in the pharmaceutical industry. The company is committed to promoting the health and safety of its employees by providing a safe work environment, supporting a culture of wellness and investing in training and development. The company also supports local initiatives, engage in philanthropic activities and partners with organisations that share its commitment to sustainability and social responsibility.

Liquidity position: Adequate

ADL's liquidity is adequate, with free cash and liquid investments of ~Rs. 20.4 crore and unutilised working capital limit of ~Rs. 213.4 crore against its drawing power of Rs. 421.4 crore (sanctioned limit of around Rs. 600 crore) as on September 30, 2024. The company's average working capital utilisation remained at ~58% against its average drawing power of Rs. 415 crore between September 2023 and October 2024. The company is expected to incur a capex of Rs. 220-230 crore in FY2025 and ~Rs. 150-160 crore in FY2026, which will be funded through a mix of term debt and internal accruals. ADL has annual repayment obligations of Rs. 77.6 crore, Rs. 56.4 crore and Rs. 63.8 crore in FY2025, FY2026 and FY2027, respectively, for its term loans. ICRA expects the company to meet its near-term commitments comfortably through its internal accruals.

Rating sensitivities

Positive factors – The ratings could be upgraded with a significant improvement in the company's revenue profile leading to increased profit margins and an improved financial profile.

Negative factors – The ratings could be downgraded in case of a significant and sustained deterioration in the company's profitability. Pressure on ADL's ratings could arise with a weakening of the company's DSCR below 2.5 on a sustained basis. The ratings could also be downgraded if its liquidity position worsens on account of higher-than-expected working capital intensity or capex funding requirements.

Analytical approach

Analytical approach	Comments
Applicable rating methodologies 9 Bold	Corporate Credit Rating Methodology Rating Methodology- Pharmaceuticals
Parent/Group support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of ADL.

About the company

ADL, incorporated in 1984, manufactures APIs, intermediates and speciality chemicals. The company was promoted by four chemical engineering graduates from UDCT Mumbai (now the Institute of Chemical Technology). ADL derived nearly 39% of its revenues from exports in FY2023. It has a strong presence in the antibiotic, antidiarrheal and anti-inflammatory segments with a growing product portfolio in antifungal, antidiabetic, cardioprotectant, vitamins and anti-arthritis therapeutic groups. ADL's key products include Ciprofloxacin, Metronidazole, Metformin HCL, Ketoconazole and Ofloxacin. It successfully developed more than 30 new molecules in the past seven years and is continuously developing new, value-added molecules through its innovative and cost-effective process. At present, the company has nine manufacturing plants in Tarapur (Maharashtra) and two plants in Sarigam (Gujarat). The manufacturing units have approvals from the USFDA, WHO-GMP, EDQM (Europe), accreditation from Japan, ANVISA, ISO 9001: 2000, TGA Australia, COFEPRIS, Canadian Authorities, China, Russia, Taiwan, Ukraine, Vietnam, and South Korea.

Pinnacle Life Science Private Limited is a wholly owned subsidiary of ADL, which manufactures formulations for the domestic (contract manufacturing) and export markets (own brand). The therapeutic segments it caters to include CNS, cardiovascular, dermatology ointments, gastrointestinal, oncology, pain management and respiratory. Its facility at Baddi (Himachal Pradesh) is ISO 9001: 2008 certified and WHO-GMP approved. PLS is also approved by various regulatory bodies like FMHACA (Ethiopia), NDA (Uganda), PPP (Kenya), and the Ministry of Health (Ivory Coast). Most of its API requirements are met by its parent.

Key financial indicators (audited)

ADL Consolidated	FY2023	FY2024	H1 FY2025
Operating income	2,716.1	2,528.6	1,153.7
PAT	166.4	171.6	68.2
OPBDIT/OI	11.4%	12.7%	11.4%
PAT/OI	6.1%	6.8%	5.9%
Total outside liabilities/Tangible net worth (times)	1.0	0.9	0.9
Total debt/OPBDIT (times)	2.0	1.8	2.2
Interest coverage (times)	8.3	8.5	7.5

*Source: Company, ICRA Research; * Provisional numbers; All ratios as per ICRA's calculations; Amount in Rs. crore PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2025)			Chronology of rating history for the past 3 years					
		Type	Amount rated (Rs. crore)	Date & rating in FY2025	Date & rating in FY2024	Date & rating in FY2023		Date & rating in FY2022		
				Jan 30, 2025	Feb 29, 2024	Dec 12, 2022	Jun 30, 2022	Jan 20, 2022	Apr 15, 2021
1	**Term loan USD million**	Long-term	-	-	-	-	[ICRA] AA- (Stable)	[ICRA] AA- (Stable)	[ICRA] AA- (Stable)
2	**Term loan (Rs. crore)**	Long-term	209.09	**[ICRA] AA- (Stable)**	[ICRA] AA- (Stable)	[ICRA] AA- (Stable)	[ICRA] AA- (Stable)	[ICRA] AA- (Stable)	[ICRA] AA- (Stable)
3	**Cash credit**	Long-term	65.00	**[ICRA] AA- (Stable)**	[ICRA] AA- (Stable)	[ICRA] AA- (Stable)	[ICRA] AA- (Stable)	[ICRA] AA- (Stable)	[ICRA] AA- (Stable)
4	**Fund based/ Non-fund based**	Short- term	1,085.00	**[ICRA]A1+**	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
5	**Commercial paper**	Short- term	-	-	-	-	-	[ICRA]A1+; withdrawn	[ICRA]A1+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Fund based - Working capital/cash credit	Simple
Term loan	Simple
Short-term fund based /non-fund based	Very 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	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Term loan**	FY2017-FY2025	NA	FY2026-FY2032	302.8	[ICRA]AA- (Stable)
NA	**Long term-Fund based CC**	NA	NA	NA	65.00	[ICRA]AA- (Stable)
NA	**Short term- Fund based/Non-fund based**	NA	NA	NA	1,085.00	[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	Ownership	Consolidation Approach
Pinnacle Life Science Private Limited	100.0%	Full Consolidation
Aarti Speciality Chemicals Limited	100.0%	Full Consolidation
Pinnacle Chile SPA	95.0%	Full Consolidation

Source: *ADL annual report*

ANALYST CONTACTS

Shamsher Dewan
+91 124 4545328
shamsherd@icraindia.com

Kinjal Shah
+91 22 6114 3442
kinjal.shah@icraindia.com

Mythri Macherla
+91 22 6114 3435
mythri.macherla@icraindia.com

Aman Mundhada
+91 22 6169 3341
aman.mundhada@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar
+91 22 6114 3406
shivakumar@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

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

HELPLINE FOR BUSINESS QUERIES

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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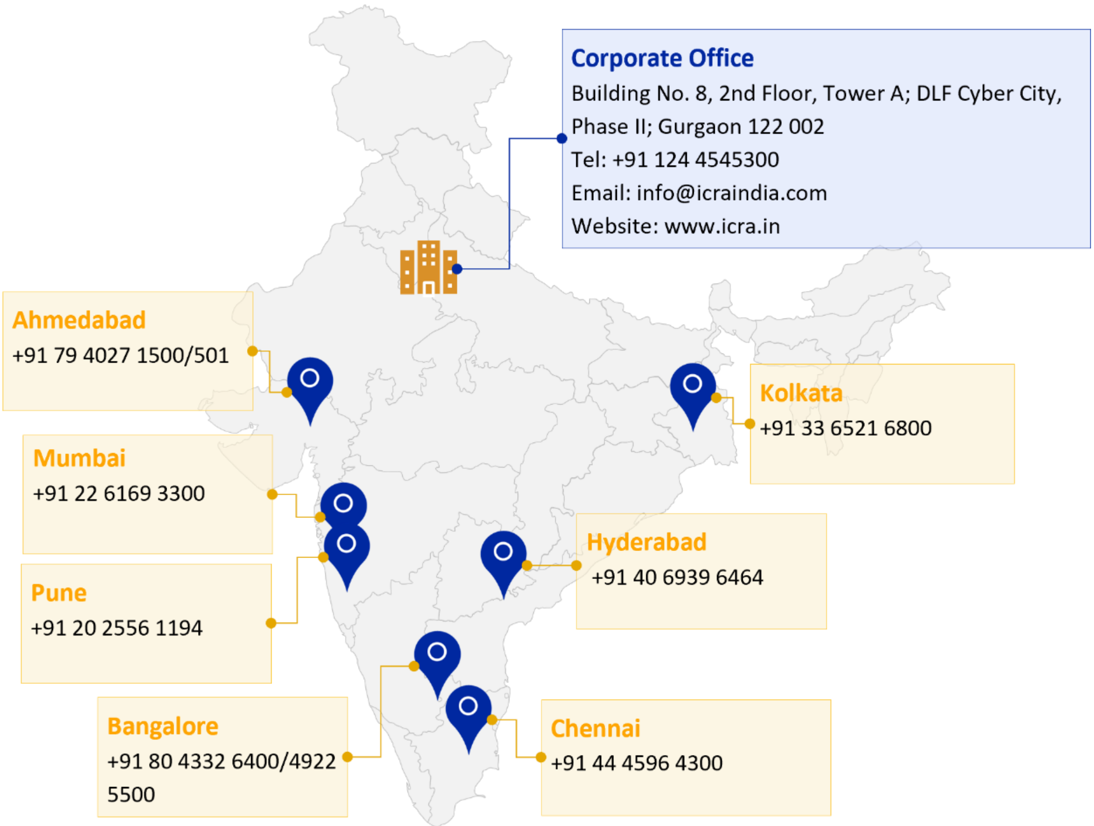
ICRA Limited

Registered Office

B-710, Statesman House, 148 Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

Branches



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