December 23, 2019

Acme Generics LLP: Ratings downgraded to [ICRA]BB+; outlook revised to Negative

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund Based –Term Loan	75.00	71.19	[ICRA]BB+ (Negative); Rating downgraded from [ICRA]BBB (Stable)
Fund Based – Working Capital Facilities	10.00	12.00	[ICRA]BB+ (Negative); Rating downgraded from [ICRA]BBB (Stable)
Unallocated Limits	0.00	1.81	[ICRA]BB+ (Negative); Rating downgraded from [ICRA]BBB (Stable)
Total	**85.00**	**85.00**	

**Instrument details are provided in Annexure-1*

Rationale

ICRA has taken a consolidated view on Acme Formulation Private Limited (AFPL) and Acme Generics LLP (AGL) (collectively referred to as Acme Group), while assigning the credit ratings, given the common management and significant operational and financial linkages between the entities. Acme Formulation holds an 81% stake in Acme Generics through direct and indirect holdings.

The ratings downgrade and the outlook revision factors in the heightened risk of crystallisation of the contingent liabilities of AFPL, which could lead to a weakening of the entity's credit and liquidity profile. AFPL has issued a total of Rs. 88.7[1] crore of corporate guarantees to its investee companies[2] (as on March 31, 2019). Out of the total amount, Rs. 49.7 crore of corporate guarantees have been extended to Immacule Lifesciences Private Limited, which continues to require significant funding support from Acme owing to cash losses and consequent delays in servicing its debt obligations (AFPL has further extended ~Rs. 6.8 crore of inter-corporate loans to the entity as on March 31, 2019). Even as the corporate guarantee extended to Immacule Lifesciences has not been invoked till date, an invocation of the same remains a concern and would lead to deterioration in its credit profile. As per management guidance, the entity is seeking revocation of the guarantees, given to the weaker group entities. ICRA would continue to monitor the developments in this regard and take appropriate rating action.

The ratings assigned continue to favourably factor the Acme Group's established position as a contract manufacturer for the leading pharmaceutical companies in India. Even as the Group primarily remains a supplier to the generic business of domestic pharmaceutical players, it benefits from its healthy customer relationships with large players in the industry such as Abbott India Limited and Dr. Reddy's Laboratories Limited among others. Despite the dilution of excise exemption benefits at its key manufacturing sites post GST implementation, the Group has been able to sustain its scale of operations, registering a high double-digit year-over-year revenue growth in FY2019. The increase in competitive headwinds post GST implementation, however, led to a moderation in the Group's operating profitability with consolidated OPBITDA margin declining by more than 400bps YoY in FY2019 (13.2% in FY2019from17.5% in FY2018). The

[1]Excluding Rs. 85.0 crore of corporate guarantees issued to AGL

[2]Investee companies include Immacule Lifesciences Private Limited and Globe CV Private Limited

Group's business risk profile remains constrained by its low geographical diversity, as exports continue to contribute only ~10-12% of the overall revenues.

Going forward, ICRA expects the company to continue to benefit from the healthy demand in the domestic pharmaceutical market, which coupled with its enhanced efforts to penetrate the regulated international markets is likely to help it record a moderate growth in revenues over the medium term. However, an increase in competitive headwinds post GST implementation is likely to constrain its operating profitability.

Key rating drivers and their description

Credit strengths

Well-established contract manufacturer in generic pharmaceutical industry with strong clientele – The Acme Group is involved in providing contract manufacturing services to the pharmaceutical industry. The Group benefits from its healthy customer relationships with leading pharmaceutical players such as Abbott India, Dr. Reddy's Laboratories and others as its clients.

Credit challenges

Significant support extended to investee companies weighs on Group's credit profile – AFPL has extended a total of Rs. 88.7 crore of corporate guarantees to its associate companies other than AGL. Enhanced risk of invocation of majority of such guarantees owing to the ongoing weakness in the operating performance and delays in the debt servicing of its significant investee company, Immacule Lifesciences Private Limited, adversely impacts the Group's credit profile. Moreover, as on March 31, 2019, AFPL extended ~Rs. 11.4 crore of inter-corporate loans to its associates that weighs on the Group's financial flexibility.

Exposure to stiff competition in generic pharmaceutical industry – The Group remains exposed to intense competition owing to presence in the fragmented generic pharmaceutical market, which limits its pricing power. Further, the increase in competitive headwinds, post the elimination of benefits available in excise/tax-free zones after GST implementation has led to pressure on the margins. However, the Group's track record of sustained market share with well-established customer relationships and continued advancements in technological capabilities provide comfort.

Low geographical diversity with exports contributing limited share of revenues – Acme's share of revenue from exports has remained primarily stable over the years at around 9-10%. At present, the company exports primarily to the semi-regulated markets of Vietnam, Malaysia, Venezuela and Philippines among others. However, the management is looking forward to increasing its share of exports in the near-to-medium term with penetration in the regulated international pharmaceutical market.

Liquidity position: Stretched

ICRA expects Acme's liquidity profile to remain stretched in the near-term, owing to the possibility of crystallisation of contingent liabilities on its books. Although, the Group's cash accruals are expected to adequately fund its annual debt obligation and capex requirements in FY2020, extension of incremental funding support to Group entities could weaken its liquidity profile.

Rating sensitivities

Positive triggers – The rating could be upgraded if there is a reduction in the financial support extended to Group companies on a sustained basis; in particular revocation of corporate guarantees extended to weaker Group entities could act as a trigger for a rating upgrade. Additionally, ICRA would positively view a significant improvement in the company's business risk profile. The same could be led by gain in business for exports as it remains a key business segment for Acme, following the dilution of excise exemption benefits post GST implementation.

Negative triggers – Acme's ratings could be downgraded if the corporate guarantees issued to the weaker Group entities are invoked. Further, deterioration in the company's financial performance with the increase in the competition in the domestic market would be viewed negatively.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Pharmaceutical Industry Consolidation and Rating Approach
Parent/Group Support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has consolidated the financials of two group entities (as mentioned in Annexure-2) given the close business, financial and managerial linkages among them.

About the company

Acme Generics LLP (AGL) was incorporated in 2014 as a partnership firm. It was primarily established as an extended arm to AFPL to continue to enjoy the excise exemption benefits, which expired in March 2015 for AFPL. However, with implementation of GST in FY2016, the excise exemption benefits are no longer applicable and thus both companies operate similarly with strong business linkages and the same management team. AFPL holds a majority stake in AGPL (81% through direct and indirect holdings).

AGL's development and manufacturing capabilities cover prescription products in solid and semi-solid dosage forms. Its manufacturing facility is situated in Baddi (Himachal Pradesh), spread across an area of 3.0 lakh sq. ft. The facility has an annual capacity of 13 billion tablets and two billion capsules. It is accredited by European Union – Good Manufacturing Practice Hungary(EU-GMP Hungary), Therapeutic Goods Administration(TGA) Australia and U.S. Food and Drug Administration (US-FDA) particularly for manufacturing OTC and dietary supplements.

Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	257.1	257.5
PAT (Rs. crore)	28.7	14.6
OPBDIT/OI (%)	17.7%	12.0%
RoCE (%)	27.2%	15.6%
Total Outside Liabilities/Tangible Net Worth (times)	2.1	1.9
Total Debt/OPBDIT (times)	1.8	2.7
Interest Coverage (times)	6.0	4.6
DSCR	3.9	2.0

Status of non-cooperation with previous CRA:

In its rationale published on Acme Generics, dated Oct 25, 2018, Crisil Ratings has stated the following:

"CRISIL has been consistently following up with ACME Generics LLP (ACME) for obtaining information through letters and emails dated March 31, 2018 and September 28, 2018 among others, apart from telephonic communication. However, the issuer has remained non-cooperative.

'The investors, lenders and all other market participants should exercise due caution while using the rating assigned/reviewed with the suffix 'ISSUER NOT COOPERATING'. These ratings lack a forward-looking component as it is arrived at without any management interaction and is based on best available or limited or dated information on the company.

Despite repeated attempts to engage with the management, CRISIL failed to receive any information on either the financial performance or strategic intent of ACME, which restricts CRISIL's ability to take a forward-looking view on the entity's credit quality. CRISIL believes information available on ACME is consistent with 'Scenario 1' outlined in the 'Framework for Assessing Consistency of Information with CRISIL BB' rating category or lower'.

*Based on the last available information, the rating on bank facilities of ACME continue to be '**CRISIL B+/Stable Issuer not cooperating'."***

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2020)				Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	Rating	FY2019*	FY2018	FY2017
					23-Dec-2019	27-Dec-2018	31-Aug-2017	16-Aug-2016
1	Fund-based - Term Loan	Long Term	71.19	71.19	[ICRA]BB+ (Negative)	[ICRA]BBB (Stable)	[ICRA]BBB (SO) (Stable)	[ICRA]BBB (SO) (Stable)
2	Fund-based Working Capital Facilities	Long Term	12.00	-	[ICRA]BB+ (Negative)	[ICRA]BBB (Stable)	[ICRA]BBB (SO) (Stable)	[ICRA]BBB (SO) (Stable)
3	Unallocated Limits	Long Term	1.81	-	[ICRA]BB+ (Negative)	-	-	-

*Amount in Rs. crore; *An update on reason for delay in periodic surveillance was published on November 28, 2018*

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	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan-1	February 2015	-	March 2025	61.46	[ICRA]BB+(Negative)
NA	Term Loan-2	November 2018	-	November 2023	9.73	[ICRA]BB+ (Negative)
NA	Fund-based - Working Capital Facilities	-	-	-	12.00	[ICRA]BB+ (Negative)
NA	Unallocated Limits	-	-	-	1.81	[ICRA]BB+ (Negative)

Source: Acme Generics LLP

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Acme Formulation Private Limited	100.00%	Full Consolidation
Acme Generics LLP	81.00%	Full Consolidation

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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.

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.

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