

September 06, 2021

## Syngene International Limited: Ratings reaffirmed; rated amount enhanced

### Summary of rating action

| Instrument*                                 | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action                           |
|---|-----------------------------------|----------------------------------|---|
| Term loans (External Commercial Borrowings) | 375.00                            | 600.00                           | Rating reaffirmed at [ICRA]AA+ (Stable) |
| Long-term fund based                        | 136.00                            | 29.00                            |   |
| Short-term fund based                       | 379.50                            | 846.00                           | Rating reaffirmed at [ICRA]A1+          |
| Short-term non-fund based                   | 13.80                             | 00.00                            | -                                       |
| Short-term unallocated                      | 55.70                             | 25.00                            | Rating reaffirmed at [ICRA]A1+          |
| <b>Total</b>                                | <b>960.00</b>                     | <b>1500.00</b>                   |   |

\*Instrument details are provided in Annexure-1

### Rationale

The reaffirmation of ratings draws comfort from Syngene International Limited's (Syngene) strong business profile and well-entrenched position in the contract research space, its established client relationships and comfortable financial profile. The company also has strong parentage by virtue of it being a subsidiary of Biocon Limited (rated [ICRA]AA+ (Stable)/[ICRA]A1+). Syngene's operating income grew by 8.6% year-on-year (YoY) in FY2021 to Rs. 2,201.4 crore and by 46.1% YoY in Q1 FY2022 to Rs.609.1 crore, aided by healthy performance across segments. Further, Syngene has healthy growth prospects over the medium term, supported by the robust demand for services from contract research organisations (CROs), its new business additions, contract extensions and scope enhancements. Globally, CROs are expected to benefit from the trend of pharmaceutical companies increasingly outsourcing their research activities, and Indian CROs (including Syngene) are in an advantageous position, given their cost competitiveness, despite the growing competition. While the company already has an integrated presence across discovery, dedicated research and development (R&D), development and manufacturing services, the planned scaling up of operations in the newly commissioned Active Pharmaceutical Ingredient (API) manufacturing facility in Mangalore over the near to medium term, would diversify Syngene's operations further and strengthen its position in the drug-discovery-to-manufacture value chain. Syngene currently derives over half of its revenues from its top 10 customers and 74% of its FY2021 revenues from The United States of America (USA). However, the company has been engaging in focused efforts to diversify its client base and has added over 40 new clients in FY2021.

Syngene continued to maintain healthy margins and profitability, with operating margins of 30.8% (PY: 30.5%), net margins of 18.4% (PY: 20.3%) and core return on capital employed (core RoCE) of 21.9% (PY: 26.9%) in FY2021. Although the company has capex plans of ~Rs. 750.0 – 900.0 crore (\$100 - 120 million) in FY2022, ICRA draws comfort from the anticipated healthy accruals from the business and Syngene's strong liquidity position with cash and liquid investments of Rs. 1,125.5<sup>1</sup> crore as on June 30, 2021 and repayment obligations totalling to less than Rs.100 crore on existing loans in the next three years. The company remained net debt negative as on June 30, 2021 and is expected to remain so over the medium term.

<sup>1</sup> Only includes investments with maturity period less than a year

## Key rating drivers and their description

### Credit strengths

#### **Strong business profile with integrated presence across discovery, dedicated R&D, development and manufacturing services**

– Syngene operates through three major verticals, namely a) dedicated R&D centres for global majors like Bristol-Myers-Squibb (BMS), Baxter Inc., Amgen Inc., and Herbalife Ltd; b) discovery services; c) development and manufacturing services. The company's API facility in Mangalore was commissioned in March 2020. It has received the Good Manufacturing Practice (GMP) certification in FY2021 and has commenced production, albeit at a relatively small scale. Scaling up of manufacturing and production of high-end, novel molecules upon receipt of requisite regulatory approvals from The United States Food and Drug Administration (USFDA) department/European Medicines Agency (EMA) over the medium term is expected to diversify the company's revenue stream further and strengthen its position in the drug discovery-to-manufacture value chain.

#### **Established client relationships; healthy client additions year-on-year in the last several years aids revenue visibility**

– The company has long-term research contracts with reputed clients like BMS, Baxter Inc., Amgen Inc., and Herbalife Ltd. The company also collaborates with major players such as Hindustan Unilever Limited (HUL) in the consumer products industry, Glaxo Smith Kline (GSK) and Johnson & Johnson in the biopharma industry and Zoetis in the animal health industry, to name a few. About 25% of its customers have engaged with the company for over five years. In FY2021, Syngene has extended the strategic collaboration with BMS up to 2030, apart from signing a five-year R&D collaboration with Deerfield Discovery and Development Corporation for executing four integrated drug discovery (IDD) projects. Further, in Q1 FY2022, Syngene signed a five-year agreement with International Aids Vaccine Initiative, Inc. (IAVI), to develop and manufacture monoclonal antibodies (mAbs) for HIV. Syngene has increased its client base by over 40 customers to 400+ clients in FY2021. The deeper engagements and client additions provide revenue visibility for Syngene over the medium term.

#### **Strong financial profile characterized by revenue growth, healthy earnings and debt metrics**

– Syngene reported a healthy growth of 8.6% in OI to Rs. 2,201.4 crore in FY2021, aided by client additions in discovery services, scope expansions in dedicated R&D services and healthy demand in the development and manufacturing segment. Further, the revenue grew by 46.1% YoY in Q1 FY2022 to Rs. 609.1 crore, aided by healthy performance across segments in addition to the low base effect in Q1 FY2021 owing to the first covid wave. Syngene's margins and profitability remained strong in FY2021, with operating margins of 30.8% (PY: 30.5%), net margins of 18.4% (PY: 20.3%) and core RoCE of 21.9% (PY: 26.9%). For Q1 FY2022, the company reported operating margins of 27.0% (marginal reduction due to unfavourable product mix, with increased production of Remdesivir) and net margin 12.6% respectively. Syngene's interest coverage also remained robust at 24.5 times for FY2021 (17.9 times in FY2020). Further, as on March 31, 2021, the company was net debt negative at Rs. 173.0 crore<sup>2</sup>. The company's revenues are expected to witness a double-digit growth on a YoY basis in FY2022, supported by the anticipated healthy growth in the global contract research industry and Syngene's new business additions, scope enhancements and contract extensions. Further, Syngene's margins are likely to remain healthy and the company is likely to continue to be net debt negative over the medium term.

#### **Strong parentage by virtue of being a subsidiary of Biocon Limited**

– Syngene is a subsidiary of Biocon Limited (rated [ICRA]AA+ (Stable)/[ICRA]A1+) and contributed to 31% of the latter's consolidated revenues and 42% of its consolidated operating profit in FY2021. The company has robust infrastructure (with over 4,700 scientists and 2 million sq. ft of research space) and strong accruals. Thus, it does not require operational or financial support from the parent. However, Syngene enjoys implicit financial and operational flexibility by virtue of its parentage.

<sup>2</sup> Net Debt = Calculated as gross debt (including lease liabilities) minus cash and liquid investments

As on March 31, 2021, company had Total debt (including lease liabilities) of Rs. 892.9 crore and unencumbered cash and liquid investment of Rs 1065.9 crore

## Credit challenges

**Significant capex plans in FY2022** – The company has a capex plan of ~Rs. 750.0 – 900.0 crore (\$100 – 120 million) in FY2022 for its infrastructure development to support business expansion. However, ICRA draws comfort from the company's strong liquidity position and anticipated healthy accruals from the business, which will fund the capex.

**High customer and geographic concentration** – Syngene derives over half of its revenues from its top 10 customers, and 74% of its FY2021 revenues were from USA. This exposes the company to revenue risks arising from loss of customers to competitors and region-specific challenges. However, Syngene's periodic addition of customers (client base has grown at a CAGR of 10% in the last six years), stated intent to continue diversifying its customer base going forward and presence of customers globally across regions provides comfort to an extent.

**Growing competition in the contract research space** – With the industry poised for healthy growth over the next few years, several global and domestic players are expanding their presence in contract research. This is likely to increase competition and pricing pressure for Syngene going forward. However, Syngene's healthy scale of operations, robust infrastructure, employee skillset, focus on compliance and safety, and established client relationships are likely to mitigate competitive threats to a large extent.

**Regulatory risks and vulnerability to unfavourable forex movement** – Akin to other industry players, the company is bound by strict regulations for clinical trials for regulated markets. Although any deviation in the same could result in reputational risks and other penalties for the company, historical absence of regulatory issues in clinical trials provides comfort to a large extent. Also, with about 96% of its revenues from overseas markets, the company's revenues and margins are susceptible to risks arising from adverse forex movements including appreciation of rupee against dollar. However, the hedging mechanisms adopted by the company mitigate the risk to an extent.

## Liquidity position: Strong

Syngene's liquidity is strong with healthy retained cashflows over the last five years, consolidated cash and bank balances and liquid investments of Rs. 1,125.5 crore<sup>3</sup> (as on June 30, 2021). In relation to these sources of cash, Syngene has a total consolidated capex commitment of ~Rs. 750.0 – 900.0 crore in FY2022 (to be funded through internal accruals), and term loan repayments totalling to less than Rs. 100.0 crore on existing loans in the next three years. Syngene is expected to maintain its net debt negative position over the medium term. ICRA expects Syngene to be able to meet its commitments through internal sources of cash and yet be left with healthy cash/liquid investment surplus. Further, the company enjoys strong financial flexibility and lender/investor comfort, and this is expected to continue going forward as well.

## Rating sensitivities

**Positive factors** – ICRA could upgrade Syngene's ratings a) if the company achieves material improvement in its scale of operations and significant diversification of customer base, while maintaining its strong debt metrics and b) upon strengthening of the credit profile of the parent, Biocon.

**Negative factors** – Negative pressure on Syngene's ratings could arise if there is pressure on Syngene's revenues or weakening of profit margins or profitability on sustained basis; or weakening in the parent's (Biocon Limited, rated [ICRA]AA+ (Stable)/[ICRA]A1+) credit profile or Syngene's operational/financial linkages with the parent, Biocon.

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<sup>3</sup> Only includes investments with maturity period less than a year

## Analytical approach

| Analytical Approach             | Comments   |
|---------------------------------|--|
| Applicable Rating Methodologies | <a href="#">Corporate Credit Rating Methodology</a><br><a href="#">Rating Methodology for implicit or explicit support from parent or group on an entity's credit rating</a><br><a href="#">Rating Methodology for pharmaceutical industry</a> |
| Parent/Group Support            | Biocon Limited (rated [ICRA]AA+ (Stable)/[ICRA]A1+) holds 70.2% stake in Syngene. Syngene enjoys implicit financial and operational flexibility by virtue of its parentage.  |
| Consolidation/Standalone        | The ratings are based on the consolidated financial statements of Syngene International Limited  |

## About the company

Syngene International Limited (Syngene), a subsidiary of Biocon Limited, is a contract research organisation (CRO) providing integrated discovery and development services for novel molecules across multiple platforms, including small molecules, large molecules, antibody drug conjugates and oligonucleotides. The company's strengths include synthetic chemistry and molecular biology. Syngene offers outsourced services to over 400 global customers across biotechnology, nutrition, animal health, consumer goods and specialty chemicals including majors such as BMS, Amgen, Herbalife and Baxter, etc. Syngene has 2 million sq. ft. of R&D infrastructure and over 4,700 scientists currently. Syngene also incorporated a wholly-owned subsidiary, Syngene USA Inc., in the USA in FY2018 for providing marketing services to the company in the region.

## Key financial indicators (audited)

| Consolidated   | FY2020  | FY2021  |
|--|---------|---------|
| Operating Income (Rs. crore)                         | 2,026.3 | 2,201.4 |
| PAT (Rs. crore)                                      | 412.1   | 404.9   |
| OPBDIT/OI (%)  | 30.5%   | 30.8%   |
| PAT/OI (%)   | 20.3%   | 18.4%   |
| Total Outside Liabilities/Tangible Net Worth (times) | 0.9     | 0.7     |
| Total Debt/OPBDIT (times)                            | 1.3     | 1.3     |
| Interest Coverage (times)                            | 17.9    | 24.5    |

Source: Company and ICRA Research; 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 (FY2022) |                          |   |                    | Chronology of Rating History for the past 3 years |                                |                                |
|---|----------------------------------|-------------------------|--------------------------|---|--------------------|---|--------------------------------|--------------------------------|
|   |                                  | Type                    | Amount Rated (Rs. crore) | Amount Outstanding as of March 31, 2021 (Rs. crore) | Date & Rating in   | Date & Rating in FY2021                           | Date & Rating in FY2020        | Date & Rating in FY2019        |
|   |                                  |                         |                          |   | Sep 6, 2021        | Aug 10, 2020                                      | Sep 13, 2019                   | Jul 31, 2018                   |
| 1 | Term loans (ECB)                 | Long-term               | 600.00                   | 512.40  | [ICRA]AA+ (Stable) | [ICRA]AA+ (Stable)                                | [ICRA]AA (Positive)            | [ICRA]AA (Positive)            |
| 2 | Long-term unallocated            |                         | 0.00                     | -   | -                  | -   | -                              | [ICRA]AA (Positive)            |
| 3 | Long-term fund based             |                         | 29.00                    | NA  | [ICRA]AA+ (Stable) | [ICRA]AA+ (Stable)                                | -                              | -                              |
| 4 | Long-term/short term fund based  | Long/Short term         | 0.00                     | -   | -                  | -   | -                              | [ICRA]AA (Positive)/ [ICRA]A1+ |
| 5 | Long-term/short term unallocated |                         | 0.00                     | -   | -                  | -   | [ICRA]AA (Positive)/ [ICRA]A1+ | -                              |
| 6 | Short-term fund based            | Short term              | 846.00                   | 259.90  | [ICRA]A1+          | [ICRA]A1+   | -                              | -                              |
| 7 | Short-term non-fund based        |                         | 00.00                    | NA  | -                  | [ICRA]A1+   | -                              | -                              |
| 8 | Short-term unallocated           |                         | 25.00                    | NA  | [ICRA]A1+          | [ICRA]A1+   | -                              | -                              |

## Complexity level of the rated instruments

| Instrument                | Complexity Indicator |
|---------------------------|----------------------|
| Term loans (ECBs)         | Simple               |
| Long-term fund based      | Simple               |
| Short-term unallocated    | Not applicable       |
| Short-term fund based     | Simple               |
| Short-term non-fund based | 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, is available on ICRA's website: [www.icra.in](http://www.icra.in)

**Annexure-1: Instrument details**

| ISIN No/Banker Name | Instrument Name                   | Date of Issuance | Coupon Rate   | Maturity | Amount Rated (Rs. Crore) | Current Rating and Outlook |
|---------------------|-----------------------------------|------------------|---------------|----------|--------------------------|----------------------------|
| NA                  | Term Loan- ECB                    | FY2021           | Libor + 1.3%  | FY2026   | 375.00                   | [ICRA]AA+<br>(Stable)      |
|                     | Term Loan- ECB                    | FY2021           | Libor + 0.87% | FY2026   | 225.00                   |                            |
|                     | Long Term- Fund Based- OD         | NA               | NA            | NA       | 24.00                    |                            |
|                     | Long Term- Fund Based- CC         | NA               | NA            | NA       | 5.00                     |                            |
|                     | Short Term- Fund Based- PCFC/WCDL | NA               | NA            | NA       | 846.00                   | [ICRA]A1+                  |
|                     | Short Term- unallocated           | NA               | NA            | NA       | 25.00                    |                            |

Source: Company, ICRA Research

**Annexure-2: List of entities considered for consolidated analysis**

| Company Name                    | Syngene Ownership | Consolidation Approach |
|---------------------------------|-------------------|------------------------|
| Syngene USA Inc                 | 100%              | Full Consolidation     |
| Syngene Employees Welfare Trust | 100%              | Full Consolidation     |

Source: Company, ICRA Research

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