

December 23, 2019

## Acme Formulation Private Limited: Ratings downgraded to [ICRA]BB+/[ICRA]A4+; 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	22.70	20.40	[ICRA]BB+(Negative); Rating downgraded from [ICRA]BBB (Stable)
Fund Based – Working Capital Facilities	10.00	10.00	[ICRA]BB+ (Negative); Rating downgraded from [ICRA]BBB (Stable)
Non-fund Based – Working Capital Facilities	5.00	0.50	[ICRA]A4+; Rating downgraded from [ICRA]A3+
Unallocated Limits	8.30	15.10	[ICRA]BB+ (Negative); Rating downgraded from [ICRA]BBB (Stable)
<b>Total</b>	<b>46.00</b>	<b>46.00</b>	

\*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<sup>1</sup> crore of corporate guarantees to its investee companies<sup>2</sup> (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

<sup>1</sup>Excluding Rs. 85.0 crore of corporate guarantees issued to AGL

<sup>2</sup>Investee companies include Immacule Lifesciences Private Limited and Globe CV Private Limited

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 FY2019 from 17.5% in FY2018). The 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	<a href="#">Corporate Credit Rating Methodology</a> <a href="#">Rating Methodology for Entities in the Pharmaceutical Industry</a> <a href="#">Consolidation and Rating Approach</a>
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

Incorporated in 2004, Acme Formulation Private Limited (Acme Formulation) is involved in providing contract dosage for development and manufacturing services to the pharmaceutical industry. The company is a part of the JCBL Group, which has a diversified presence across automobiles, pharmaceuticals, information technology and international trading industries. JCBL India Private Limited (JCBL) owns 50.1% stake in the company, while 33.0% stake is held by Mr. Viral Shah.

Acme has a manufacturing facility in Nalagarh (Himachal Pradesh) spread across an area of 1.7 lakh sq. ft. The facility was set up in 2003 and has an annual capacity of 3.5 billion tablets and 0.5 billion capsules. Its development and manufacturing capabilities cover prescription products in both solid and semi-solid dosage forms. AFPL's facility is accredited by the World Health Organisation (WHO), Geneva and INVIMA Columbia.

### Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	63.9	119.5
PAT (Rs. crore)	5.7	10.8
OPBDIT/OI (%)	16.3%	15.7%
RoCE (%)	6.2%	11.3%
Total Outside Liabilities/Tangible Net Worth (times)	0.4	0.5
Total Debt/OPBDIT (times)	3.3	1.4
Interest Coverage (times)	3.6	6.9
DSCR	2.1	2.8

**Status of non-cooperation with previous CRA: Not applicable**

**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	20.40	20.40	[ICRA]BB+ (Negative)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)
2	Fund-based Working Capital Facilities	Long Term	10.00	-	[ICRA]BB+ (Negative)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)
3	Non-fund Based Working Capital Facilities	Short Term	0.50	-	[ICRA]A4+	[ICRA]A3+	[ICRA]A3+	[ICRA]A3+
4	Unallocated Limits	Long Term	15.10	-	[ICRA]BB+ (Negative)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)

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](http://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	July 2016	-	November 2022	3.72	[ICRA]BB+(Negative)
NA	Term Loan-2	July 2016	-	October 2026	16.68	[ICRA]BB+ (Negative)
NA	Fund-based - Working Capital Facilities	-	-	-	10.00	[ICRA]BB+ (Negative)
NA	Non-fundBased - Working Capital Facilities	-	-	-	0.50	[ICRA]A4+
NA	Unallocated Limits	-	-	-	15.10	[ICRA]BB+ (Negative)

Source: Acme Formulation Private Limited

### 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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