April 07, 2021

Strides Pharma Science Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	-	200.00	[ICRA]A+ (Stable); reaffirmed
Long-term, Fund-based Facilities	850.00	940.00	[ICRA]A+ (Stable); reaffirmed
Short-term, Non-fund Based Facilities	420.00	480.00	[ICRA]A1; reaffirmed
Unallocated Facilities	530.00	180.00	[ICRA]A1; reaffirmed
Total	**1,800.00**	**1,800.00**	

**Instrument details are provided in Annexure-1*

Rationale

The rating reaffirmation continues to factor in Strides Pharma Science Limited's (Strides'/ the company) strong business profile with majority revenues being derived from regulated markets, its long track record of operations and strong management team. Strong manufacturing and research and development (R&D) capabilities, improving front-end presence in the US market and portfolio maximisation strategy employed in other regulated markets have supported improvement in the company's operating profit margins (OPM) over the last two years. Despite Ranitidine (which accounted for a sizeable part of the company's US business revenues and OPM in FY2020) being banned in the US market since March 2020, the company was able to achieve YoY growth of 8.6% in 9M FY2021 in its US business revenues and witnessed an improvement in its OPM to 19.8%, as against 18.9% (ex-Ranitidine) in FY2020. This was aided by relatively higher share of revenues from the US frontend business and the healthy growth under other regulated markets. ICRA also notes the debt prepayment of $206 million in FY2020 through proceeds from the sale of its Australia business to Apotex. Strides received an upfront payment of AU$ 300 million at the closure of the transaction, while the balance AU$ 94 million is expected to be received as deferred consideration in FY2023. This has resulted in an improvement in the company's debt coverage indicators in 9M FY2021 despite one-time sales reversal/write-offs of $45 million taken on account of the Ranitidine ban. Overall, the company's adjusted net debt /OPBDITA[1] (adjusted for deferred consideration of AU$ 94 million from Australia business sale) stood at 1.9x as on September 30, 2020, as against 2.3x as on March 31, 2020.

The ratings also take into account the company's high working capital intensity of operations given the elongated receivables and inventory holding period requirements for its US business. Furthermore, significant investments in Stelis Biopharma Private Limited (Stelis) to date (~$75 million) and going forward (incremental ~$14 million to be invested by Strides through partly paid shares in Stelis) and returns from the same is one of the key credit rating factors for the company. ICRA also notes that relatively high competition in the generic pharmaceutical industry which could limit the company's pricing flexibility and growth to an extent; however, the company's strong growth momentum in the regulated markets provides some comfort. The company has a warning letter issued by the USFDA[2] to its Puducherry plant in May 2019, which is pending resolution. While ICRA notes that the same has not had a significant impact on the company's revenue growth, timely resolution of the same is important. While the company's average fund-based working capital utilisation remained high at 95% for the 12-month period ended December 2020, the same is expected to reduce going forward due to the enhancement of $65 million in its working capital limits availed by the company in February 2021. As on December 31, 2020, the promoters held a 29.48% equity stake in the company, of which around 40.4% was pledged, a reduction from 51.3% as on September 30, 2019.

[1] *Operating profit before depreciation, interest, tax and amortisation*

[2] *United States Food & Drug Administration*

The company has a track record of growing and diversifying through strategic acquisitions. Any significant debt-funded acquisition, thereby impacting the company's credit metrics, remains an event risk and would be evaluated on a case by case basis.

Key rating drivers and their description

Credit strengths

Diversified business and geographic mix lend revenue stability: Strides derives majority of its revenues from the US market (48% of revenues in 9M FY2021). The company currently sells ~40 products out of its 100 approved ANDAs. Furthermore, with more than 85% of its revenues being derived from its front-end presence in the US markets, the company's OPM from the US business is expected to remain healthy going forward. The company also derives 33% of its revenues from other regulated markets (UK, Australia, Europe, Canada, South Africa, etc.). With increasing number of products and improving market share in these markets, the company has witnessed a robust YoY growth of 47% in FY2020 and 33% in 9M FY2021 from these markets. The company also has a portfolio of products for the emerging markets (both branded and institutional businesses accounting for 18.8% of revenues in 9M FY2021), which further supports the company's geographic and business diversity. While the performance of the emerging markets portfolio was subdued in FY2019 and FY2020, the same witnessed a YoY growth of 61.3% in 9M FY2021 on the back of strong revenue growth under its branded generics business in Africa. Going forward, the company's institutional business is expected to witness healthy ramp up in revenues given the recent approval for the company's TLD (Tenofovir, Lamivudine and Dolutegravir) combination, which has healthy revenue potential.

Strong manufacturing and R&D capabilities coupled with improving front-end presence: Given its strong pipeline of products and its manufacturing capabilities, ICRA expects the company's revenue growth and margins to improve going forward supported by its strong performance in the US market and its portfolio maximisation strategy in other regulated markets. Furthermore, improving front-end presence across markets is expected to support the company's revenues and margins going forward. The company also intends to invest in R&D for injectables selectively going forward, which could lead to further increase in revenues. Strides' R&D spend was ~Rs. 94 crore during FY2020, accounting for 6.3% of its US business revenues, wherein the company primarily focused on new formulations and portfolio maximisation, wherein it evaluated its existing product basket for extension to other geographies. R&D spend as a proportion of the company's topline is expected to reduce as scale increases.

Improvement in debt coverage indicators: Post repaying significant amount of debt (~$206 million) in FY2020 from proceeds of its Australia business sale, the company's debt coverage indicators have witnessed an improvement. Strides received an upfront payment of AU$ 300 million at the closure of transaction, while the balance AU$ 94 million is expected to be received during FY2023. ICRA understands that the deferred consideration carries an interest and receipt of the same is not dependent on any milestones being achieved. Adjusted for the deferred consideration, the company's adjusted net debt/OPBDITA stood at 2.3x as on March 31, 2020. Despite one-time provisioning/write-offs of $45 million taken in Q3 FY2021 on account of the Ranitidine ban, the company's adjusted net debt/OPBDITA further improved to 1.9x as on December 31, 2020 given the strong accruals.

Credit challenges

High competitive intensity: The generic pharmaceutical business in regulated markets is characterised by low entry barriers and high pricing pressures. While the company's revenues under its own front-end in North America continue to maintain steady market share, the generics industry is characterised by headwinds in the form of intense competitive pressures (leading to price erosions) which may affect margins. However, the company's strong market position and focus on filing for products with limited competition are expected to provide comfort to a certain extent.

Significant investments in Stelis: In addition to significant investments of ~$75 million, which have already been made in Stelis, Strides has indicated that it will invest an additional up to $14 million in Stelis. Given that Stelis has invested heavily in setting up a manufacturing facility, timeliness in achieving breakeven of operations and cash flows from the same would be key credit monitorables going forward, as those would determine the returns accruing to Strides. Stelis has recently raised equity of $155 million, further to which Strides will have a shareholding of 33% (post completion of the planned $14 million investment) in Stelis.

Exposure to regulatory risks; warning letter for the Puducherry facility yet to be resolved: Increasing regulatory scrutiny by the USFDA, compliance costs and risks associated with the same will be a key rating sensitivity going forward. The company has a warning letter issued by the USFDA to its Puducherry plant in May 2019, which is pending resolution. While ICRA notes that the same has not had a significant impact on the company's revenue growth, timely resolution of the same is important. Any other regulatory non-compliance issued to Strides for its products and/or manufacturing facilities, thereby impacting its product launches and thus revenues and profitability, would be key monitorables.

High working capital intensity of operations: The company's working capital intensity continues to be high at 31% as on September 30, 2020 (34% as on March 31, 2020) given the relatively high receivables (117 days as on September 30, 2020 and 128 days as on March 31, 2020) and inventory holding period (193 days as on September 30, 2020 and 161 days as on March 31, 2020) requirements of its US business.

Liquidity position: Adequate

Strides' liquidity is **adequate** with funds flow from operations remaining positive during FY2020 and H1 FY2021, in line with previous trends. The company also had cash and bank balances of ~Rs. 300 crore as on September 30, 2020 supporting its overall liquidity position. The company also availed enhancements of $65 million in its working capital facilities, providing further liquidity support to the company. The company has upcoming repayments of Rs. 198.5 crore in FY2022 and Rs. 181.6 crore in FY2023. In addition, the company has also committed to infuse up to $14 million in Stelis by FY2023 and will spend ~Rs. 150 crore on capital expenditure (capex) each fiscal, going forward. ICRA expects Strides to be able to meet its near-term commitments comfortably through internal accruals on the basis of its current and expected financial performance.

Rating sensitivities

Positive factors – Positive trigger for the company's ratings include improvement in cash flows and margins or monetisation of investments resulting in adjusted net debt /OPBDITA (adjusted for deferred consideration from Australia business sale) being lower than 1.5x on a sustainable basis.

Negative factors – Negative pressure on Strides' ratings could arise if any debt-funded capex/hive-off of profitable divisions lead to deterioration in the company's credit profile; further, drop in margins or increase in debt on account of inorganic transactions/regulatory changes could also impact ratings of the company. Any material financial support to group companies that results in weakening in credit metrics could also exert pressure on ratings.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for entities in pharmaceutical industry
Parent/Group Support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of Strides.

About the company

Incorporated in 1990, Strides Pharma Science Limited is a medium-sized pharmaceutical company engaged in the development, manufacture and export of a wide range of pharmaceutical products. The company has followed an inorganic growth strategy over the years that resulted in foray into new markets, and the addition of new business segments, therapy segments and manufacturing infrastructure. The company's product range covers most dosage forms including soft gel capsules, tablets, capsules and semi-solids. Currently, the company's business became broadly classified into regulated markets formulations (comprising mainly the US, UK, Europe, Australia,), emerging markets (primarily Africa) and institutional segments (tender-driven business mainly in developing markets). As on December 31, 2020, ~29.48% of the company's shareholding was held by the promoter group, while the balance was held by various institutions and public.

Key financial indicators – (audited)

Strides – Consolidated	FY2019	FY2020
Operating Income (Rs. crore)	3011.7	2,752.0
PAT (Rs. crore)*	107.3	137.8
OPBDIT/OI (%)	15.5%	18.9%
RoCE (%)	6.4%	6.1%
Total Outside Liabilities/Tangible Net Worth (times)	1.8	1.3
Adjusted Net Debt/OPBDIT (times)	5.2	2.3
Interest Coverage (times)	2.3	3.3

PAT: Profit after Tax including discontinued operations; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net Worth + Deferred Tax Liability - Capital Work in Progress); DSCR: (PBIT + Mat Credit Entitlements - Fair Value Gains through P&L - Non-cash Extraordinary Gain/Loss)/(Interest + Repayments made during the Year)

***Source**: Strides, ICRA research*

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 September 30, 2020 (Rs. crore)	Date & Rating	Date & Rating In FY2020	Date & Rating in FY2019			Date & Rating in FY2018		
					Apr-07-2021	Nov-29-2019	Feb-07-2019	May-28-2018	May-16-2018	Mar-12-2018	Jan-02-2018	Jul-12-2017
1	Term Loans	Long-term	200.0	50.0	[ICRA]A+ (Stable)	-	[ICRA]A+ &	[ICRA]A+ (Negative)	[ICRA]A+ &	[ICRA]A+ &	[ICRA]A+ &	[ICRA]A+ &
2	Fund-based Facilities	Long-term	940.0	894.0	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	-	-	-	-	-	-
3	Non-fund Based Facilities	Short-term	480.0	NA	[ICRA]A1	[ICRA]A1	[ICRA]A1 &	[ICRA]A1	[ICRA]A1 &	[ICRA]A1 &	[ICRA]A1+ &	[ICRA]A1+ &
4	Unallocated Facilities	Short-term	180.0	NA	[ICRA]A1	[ICRA]A1	[ICRA]A1 &	[ICRA]A1	[ICRA]A1 &	[ICRA]A1 &	[ICRA]A1+ &	[ICRA]A1+ &
5	Fund-based Facilities	Short-term	-	-	-	-	[ICRA]A1 &	[ICRA]A1	[ICRA]A1 &	[ICRA]A1 &	[ICRA]A1+ &	[ICRA]A1+ &

&: On rating watch with developing implications

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 click here

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loans	2020	NA	FY2024	200.0	[ICRA]A+ (Stable)
NA	Fund-based Facilities	2019/2020	NA	NA	940.0	[ICRA]A+ (Stable)
NA	Non-fund Based Facilities	2019/2020	NA	NA	480.0	[ICRA]A1
NA	Unallocated Facilities	NA	NA	NA	180.0	[ICRA]A1

Source: *Company*

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

Company Name	Ownership	Consolidation Approach
Altima Innovations Inc, USA	100.00%	Full Consolidation
Apollo Life Sciences Holdings Proprietary Limited, South Africa	51.76%	Full Consolidation
Arco Lab Private Limited, India	100.00%	Full Consolidation
Arrow Life Sciences (Malaysia Sdn. Bhd, Malaysia)	100.00%	Full Consolidation
Arrow Pharma (Private) Limited, Sri Lanka	100.00%	Full Consolidation
Arrow Pharma Life Inc, Philippines	100.00%	Full Consolidation
Arrow Pharma Pte Ltd, Singapore	100.00%	Full Consolidation
Arrow Remedies Private Limited, India	100.00%	Full Consolidation
Beltapharm, S.P.A, Italy	97.94%	Full Consolidation
Fagris Medica Private Limited, India	100.00%	Full Consolidation
Generic Partners (Canada) Inc, Canada	100.00%	Full Consolidation
Generic Partners (International) Pte Ltd, Singapore	100.00%	Full Consolidation
Generic Partners Ltd., UK	100.00%	Full Consolidation
Pharmapar Inc, Canada	80.00%	Full Consolidation
Shasun Pharma Solutions Inc, USA	100.00%	Full Consolidation
Stabilis Pharma Inc, USA	100.00%	Full Consolidation
Stelis Biopharma (Malaysia) Sdn Bhd, Malaysia	100.00%	Full Consolidation
Strides Arcolab International Ltd., UK	100.00%	Full Consolidation
Strides CIS Ltd, Cyprus	100.00%	Full Consolidation
Strides Emerging Markets Limited, India (formerly Strides Emerging Markets Private Limited, India)	100.00%	Full Consolidation
Strides Lifesciences Limited, Nigeria	100.00%	Full Consolidation
Strides Pharma (Cyprus) Ltd, Cyprus	100.00%	Full Consolidation
Strides Netherlands BV	100.00%	Full Consolidation
Strides Nordics Aps	100.00%	Full Consolidation
Strides Pharma (SA) Pty Ltd, South Africa	60.00%	Full Consolidation
Strides Pharma Asia Pte. Ltd, Singapore	100.00%	Full Consolidation
Strides Pharma Canada Inc, Canada	100.00%	Full Consolidation
Strides Pharma Global (UK) Ltd, UK (formerly, Strides Pharma (UK) Ltd)	100.00%	Full Consolidation
Strides Pharma Global Pte Limited, Singapore	100.00%	Full Consolidation
Strides Pharma Inc., USA	100.00%	Full Consolidation
Strides Pharma International Limited, Cyprus	100.00%	Full Consolidation
Strides Pharma UK Ltd, UK	100.00%	Full Consolidation
Strides Shasun Latina Sa De CV, Mexico	80.00%	Full Consolidation
SVADS Holdings SA, Switzerland	100.00%	Full Consolidation
Trinity Pharma Proprietary Limited, South Africa	51.76%	Full Consolidation

Company Name	Ownership	Consolidation Approach
Universal Corporation Ltd, Kenya	51.00%	Full Consolidation
Strides Vivimed Pte Ltd, Singapore (formerly, Vivimed Global Generics Pte Ltd)	100.00%	Full Consolidation
Vensun Pharmaceuticals Inc, USA	100.00%	Full Consolidation
Vivimed Life Sciences Private Limited, India	100.00%	Full Consolidation
Eris Pharma GmbH, Germany	70.00%	Equity Method
Oraderm Pharmaceuticals Pty Limited, Australia	50.00%	Equity Method
Fairmed Healthcare AG, Switzerland	70.00%	Equity Method
Fairmed Healthcare GmbH, Germany	70.00%	Equity Method
Juno OTC Inc	50.00%	Equity Method
Regional Bio Equivalence Centre SC	24.98%	Equity Method
Sihuan Strides (HK) Ltd	49.00%	Equity Method
Stelis Biopharma LLC	47.81%	Equity Method
Stelis Pte. Ltd.	47.81%	Equity Method
Strides Consumer LLC	53.64%	Equity Method
Strides Global Consumer Healthcare Limited, UK	53.64%	Equity Method
Aponia Laboratories Inc., USA	24.00%	Equity Method
Regional Bio Equivalence Centre S.C., Ethiopia	24.98%	Equity Method
Stelis Biopharma Private Limited, India	47.81%	Equity Method

Source: *Company annual report; *As on March 31, 2020*

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