January 31, 2022

Sakar Healthcare Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based- Cash Credit	8.00	8.00	[ICRA]BBB(Stable); Reaffirmed
Fund-based- Term Loan	73.50	73.50	[ICRA]BBB(Stable); Reaffirmed
Unallocated Limit	0.50	0.50	[ICRA]BBB (Stable)/A3+; Reaffirmed
Total	**82.00**	**82.00**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings take into account the proven track record of Sakar Healthcare Limited (SHL) of over 17 years in the pharmaceutical formulations industry and its healthy financial risk profile characterised by satisfactory return indicators, comfortable capital structure and debt coverage indicators. Moreover, prudent working capital management and buffer in working capital limits have also supported the liquidity profile. Furthermore, the ratings derive comfort from the company's diversified product profile and geographical presence, along with the diversification in the oncology segment where the commercial operations of oncology formulation unit started from October 2021. In addition, it is expected to further add to SHL's diversification profile once it achieves an optimum scale and magnitude.

The ratings, however, remain constrained by the moderate scale of operations amid intense competition in the generic formulations industry and vulnerability of profitability to fluctuations in raw material as well as forex changes. ICRA notes that the company is in the midst of a large debt-funded capex related to a new oncology project for formulations as well as active pharmaceutical ingredients (APIs). The oncology unit achieved commercial operations from October 2021, and the API unit is also expected to start in the next six months. SHL's ability to successfully scale-up the new oncology unit along with stabilisation of the project to achieve commensurate return in the near to medium term remains critical from a credit perspective. The rating also remains constrained by the exposure to regulatory restrictions in terms of product launches/ facility approvals/ socio-political risks in export destinations.

The Stable outlook on the [ICRA]BBB rating reflects ICRA's opinion that SHL will continue to benefit from the extensive experience of its key promoter in the pharmaceutical formulations industry and its diversified product and customer profiles.

Key rating drivers and their description

Credit strengths

Established track record of over 17 years in the pharmaceuticals formulation industry - The company has had established operations of more than 17 years in manufacturing pharmaceutical formulations. SHL manufactures generic formulations in 23 therapeutic categories, such as antibiotics, antihistamine, antifungal, cough preparation, and vitamins, among others.

Vast experience of promoters and established relationships with customers and suppliers - The promoters have an extensive experience in the pharmaceutical industry. Mr. Sanjay S. Shah, SHL's chairman and managing director, has an extensive experience of more than 31 years in the pharmaceutical, mineral water and plastic industries. Over the years, the company has developed strong relationships with its customers in domestic and export markets, ensuring repeat business.

Diversified product portfolio and geographic presence - The company's product profile is diversified, comprising liquid injectables, tablets/ capsules, oral liquid syrups, dry powder injections and syrups. SHL's product portfolio includes approximately 300 product registrations for various therapeutic segments, such as antibiotics, anti-cold drugs, anti-malarial, and multi-vitamins, among others. Moreover, it has a diversified geographical presence in the domestic market with sales to established industry players such as Cadila Healthcare Ltd., Torrent Pharmaceuticals Ltd., Baxter India Pvt. Ltd., Ferring Pharmaceuticals etc. and exports primarily to semi-regulated markets of various African countries and South-East Asian countries including Philippines. The company is increasing its focus on export markets, owing to the intense competition in the domestic generic formulations industry. Export sales increased to ~Rs. 69 crore in FY2021 from ~Rs. 57.00 crore in FY2020. Further, the company has received European Union Good Manufacturing Practice (EU-GMP) certification for its existing liquid and lyophilised injectables units in accordance with the European Medicines Agency (EMA) standards and started exports to European countries in FY2021.

The company has also undertaken a capex to set up a plant for manufacturing oncology drugs including formulations, APIs, R&D and injectables which is expected to further strengthen the company's product portfolio once it successfully scales up this business and it reaches an optimum scale and magnitude.

Healthy financial risk profile characterised by satisfactory return indicators, comfortable capital structure and debt coverage indicators - The company's low dependence on external borrowings and the improvement in net worth base over the years have resulted in a comfortable capital structure, albeit moderating marginally in FY2021, marked by gearing of 0.43 time as on March 31, 2021 against 0.21x as on March 31, 2020. The total debt increased to Rs. 42.60 crore as on March 31, 2021 from Rs. 16.70 crore as on March 31, 2020 on account of addition of new term loans during the year. The net worth of the company stood at Rs. 98.46 crore as on March 31, 2021 (PY: Rs.81.32 crore). The company raised an equity of Rs. 48.05 crore over FY2017-FY2021 through an IPO and preferential allotment to promoter/ non-promoter group, mainly for funding its capex requirements. The RoCE remains satisfactory and improved over the years driven by healthy profitability levels, standing at 20.79% in FY2021. ICRA notes that due to recent debt-funded capex for the oncology unit, the coverage as well as the return indicators may moderate in the near term; however, with returns flowing fully from FY2024 onwards, the indicators are expected to improve and will remain a key rating monitorable.

Credit challenges

Risks associated with stabilisation and successful scale-up of operations for recently completed and ongoing debt-funded project for manufacturing oncology drugs - SHL has undertaken a debt-funded capital expenditure (capex) for setting up a new plant to manufacture oncology drugs. The formulation unit achieved commercial operations in October 2021 whereas the operations of API unit is expected to commence in next six months and the injectable unit is expected to commence from December 2022. The risk associated with the successful implementation of ongoing projects without any time and cost overruns and ramp-up in sales following the commercialisation of operations remains critical from a credit perspective and will remain a key rating monitorable.

Moderate scale of operations - The company's revenue grew at a healthy CAGR of ~20% over FY2017-FY2021; however, it remains a moderate-sized player in the intensely competitive generic formulations industry, with a revenue base of Rs. 95.30 crore as of FY2021. The company reported ~13% YoY growth in its revenue in FY2021 and a revenue of ~Rs. 62 crore in H1 FY2022 against ~Rs. 46 crore in H1 FY2021. The domestic generic formulations industry faces stiff competition from numerous contract manufacturers, MNCs as well as established domestic brands, with some players also having a pan India presence. The intense competition also restricts the company's revenue growth and pricing flexibility; however, its presence in the export market mitigates these constraints to some extent.

Profitability remains susceptible to fluctuations in raw material prices and risk associated with forex fluctuations – The company's major raw materials include APIs, such as Paracetamol, Artemether and Diclofenac; and procures it from domestic suppliers all over the country. SHL's profitability, hence, remains susceptible to such raw material price fluctuations. The operating margin during H1 FY2022 moderated by 238bps over full year FY2021 on account of the inflationary raw material regime, wherein the ability to fully pass on such costs remain critical to protect margins. Further, the company is exposed to foreign exchange rate fluctuations as the receivables are in foreign currency while most of SHL's expenses are in INR. The company does not have any formal hedging policy in place; however, as most of the exports are against advance payment/ sight LC, the foreign currency fluctuation risk is mitigated to a large extent.

Inherent regulatory risk associated with pharmaceutical industry like Government controlled pricing policies and presence in competitive generic formulation industry - The company's operations remain exposed to regulatory restrictions in terms of product/ facility approvals/ socio-political environment of export destinations. With increasing focus on exports, ICRA notes that timely product and facility approval/ renewal in various semi-regulated markets, along with a stable socio-political environment, remains critical for its revenue growth.

Liquidity position: Adequate

SHL's liquidity position remains adequate, as evident from the adequate cash accruals against the scheduled term loan repayments. The liquidity is further supported by an undrawn line of credit of Rs. 6.31 crore as on March 31, 2021 and limited average working capital limit utilisation of ~32% during the last 12 months ended November 2021. The company's debt repayments and working capital requirements are expected to increase, going forward, post commercialisation of the oncology unit and subsequent scale up of operations. Nevertheless, the proposed enhancement of working capital limits and the annual cash accruals are expected to easily cover the annual debt repayments of ~Rs. 4-9 crore over FY2022-FY2024, and any incremental requirement of working capital.

Rating sensitivities

Positive factors - ICRA could upgrade SHL's ratings if there is a significant improvement in the operating income of the company on the back of scale-up of the new plant, while maintaining healthy profitability and debt coverage indicators.

Negative factors - Downward pressure on SHL's rating could arise if there is any decline in operating income or material decline in operating margin, with any significant delay in the commissioning of the new plant or lower than expected ramp up of scale or operating profitability, which in turn impacts the coverage indicators or liquidity profile adversely. Specific credit metrics, which can lead to negative rating trigger will be DSCR below 1.5 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Entities in the Pharmaceutical Industry
Parent/Group Support	Not applicable
Consolidation/Standalone	The rating is based on the standalone financial profile of the company.

About the company

Incorporated in 2004, Sakar Healthcare Limited manufactures pharmaceutical formulations in the form of liquid injectables, tablets/ capsules, oral liquid syrups, dry powder injections and syrups. The company manufactures generic formulations in 23 therapeutic categories, such as antibiotics, cough preparations, vitamins and mineral supplements, among others. The company is listed on the National Stock Exchange (NSE), India. SHL is involved in contract manufacturing for leading brands in the domestic market as well direct sales on principal-to-principal basis in the domestic and export markets. SHL's manufacturing facility is at Changodar, near Ahmedabad, Gujarat. The unit is ISO 9001:2008 and WHO-GMP certified. The company has also received EU-GMP certification in accordance with EMA standards, as well as INVIMA-Colombia and Health Canada approvals. In addition, SHL also has certifications from the national drug authorities of the countries it exports to, like the Philippines, Uganda, Ivory Coast, Kenya, Zimbabwe, Cambodia and Peru, among others. The company currently holds over 300 marketing authorisations (registrations) in these countries. The key promoter, Mr. Sanjay S. Shah, who is actively involved in SHL's daily operations, has extensive experience of over 17 years in the pharmaceutical industry.

Key financial indicators (Audited)

	FY2020	FY2021	H1FY22
Operating Income (Rs. crore)	84.11	95.30	61.90
PAT (Rs. crore)	9.62	10.68	6.12
OPBDIT/OI (%)	24.58%	24.31%	21.93%
PAT/OI (%)	11.44%	11.21%	9.88%
Total Outside Liabilities/Tangible Net Worth (times)	0.42	0.81	0.90
Total Debt/OPBDIT (times)	0.81	1.84	2.43
Interest Coverage (times)	9.18	9.33	10.64

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation, All ratios as per ICRA calculations,

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 on March 31, 2021 (Rs. crore)	Date & Rating in	Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019
					Jan-31, 2022	Nov-02, 2020	Feb-05, 2020	-
1	Fund based- Cash Credit	Long term	8.00	1.69^	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	-
2	Fund based- Term Loan	Long term	73.50	29.24^	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	-
3	Unallocated Limit	Long Term/ Short term	0.50	-	[ICRA]BBB (Stable)/A3+	[ICRA]BBB (Stable)/A3+	[ICRA]BBB (Stable)/A3+	-

^source: company

Complexity level of the rated instruments

Instrument	Complexity Indicator
Fund based- Cash Credit	Simple
Fund based- Term Loan	Simple
Unallocated Limit	NA

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

Annexure-1: Instrument details

ISIN No/ Bank name	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. Crore)	Current Rating and Outlook
NA	Cash Credit	NA	NA	NA	8.00	[ICRA]BBB (Stable)
NA	Term Loan	FY2020-FY2021	NA	August 2028	73.50	[ICRA]BBB (Stable)
NA	Unallocated Limits	NA	NA	NA	0.50	[ICRA]BBB (Stable)/A3+

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis – Not applicable

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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.

For more information, visit www.icra.in

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