April 07, 2022

Concord Biotech Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Term Loan	100.00	100.00	[ICRA]AA- (Stable); reaffirmed
Long-term– Fund-based Working Capital	15.00	15.00	[ICRA]AA- (Stable); reaffirmed
Short -term – Non-fund Based Limit	10.00	10.00	[ICRA]A1+; reaffirmed
Total	**125.00**	**125.00**	

**Instrument details are provided in Annexure-1*

Rationale

While arriving at the ratings, ICRA has taken a consolidated view of Concord Biotech Limited (CBL) and its Joint Venture (JV) concern Concord Biotech Japan K.K, due to strong operational linkages.

The rating reaffirmation continues to reflect the extensive experience of the promoters and the company's established track record in the fermentation and semi-synthetic biopharmaceutical (API) business, spanning around two decades. Further, the ratings takes into account the strong financial profile, characterised by healthy profitability levels, robust debt protection indicators and strong liquidity. The ratings also factor in the company's key market position in the global immunosuppressant therapeutic API segment, its strong R&D capabilities with adequate regulatory approvals and its reputed clientele with strong inflow of repeat business.

The ratings are, however, constrained by the company's relatively moderate scale of operations, its high therapeutic segment concentration and high working capital intensity, owing to the elongated receivable cycle and high inventory holding period. Given the high working capital requirements and capex undertaken the company's free cash flows moderated in FY2021. The company had positive cash flow from operations which was primarily used for capex in expanding the API capacity in Limbasi, Gujarat and the new injectables project at Valthera, Gujarat. Although it remains one of the key players and faces limited competition in the API segment, the formulation segment entails stiff competition from peers.

ICRA also notes that the company has begun commercial operations for its Unit-3 which has enhanced its API capacity. The total project cost of ~Rs. 380 crore was funded through a mix of internal accruals and term loans. The unit was commercialized in March'2021, however the unit is still to get the requisite regulatory approvals from its key markets, hence revenue from the same is expected to be marginal in FY2022 and in FY2023, given that the management expects the same to be received by Q1 of FY2024. Also, the company is in the midst of establishing an injectables plant in Valthera at a total cost of Rs. 135.0 crore to be funded entirely through internal accruals. The company is expected to begin commercial operation of its injectables plant by December'2022. Satisfactory receipt of approvals for both the units, followed by sustained ramp up of operations would be a key rating monitorable, for next level of growth for the company

The Stable outlook reflects ICRA's opinion that the company will continue to benefit from the extensive experience of its promoters in the biopharmaceutical industry, likelihood of sustained revenue growth, backed by ramp up of operations from the enhanced formulation as well as the APIs capacities, and limit the debt levels. ICRA also takes note of the stable demand conditions for the niche product profile of the API segment.

Key rating drivers and their description

Credit strengths

Experienced management and established track record - The promoters and management are well experienced, having run the business for two decades and are well-established in the fermentation and semi-synthetic biopharmaceutical (API) business. The current promoter Mr. Sudhir Vaid is a technocrat turned entrepreneur who has close to four decades of experience in the field of biotechnology space, having been associated with reputed pharma companies in the past.

Key market player in niche product segment - The company's key products are catering to the immunosuppressants therapeutic segment. These complex molecules are exposed to limited competition and garner healthy margins. Although the molecules cumulatively contribute significantly to the revenues, it is one of the key players in the industry for these products, commanding a healthy and increasing market share. The key product in the immunosuppressants segment has shown volume growth on a YoY basis FY2021, despite being off-patent which supported its revenues. Going forward, healthy growth is projected for these APIs, given the company's strong market position of its product profile coupled with favourable demand dynamics in its key export market US.

Strong R&D capabilities and adequate regulatory approvals - The company's R&D centre is recognised by the Department of Scientific and Industrial Research (DSIR), India and backed by a strong team of technocrats. Its API facility is approved by U.S. Food and Drug Administration (USFDA), European Union's Good Manufacturing Practices (EUGMP), Japanese Foreign Manufacturer Registration (FMR), Korea Ministry of Food and Drug Safety, Indian Good Manufacturing Practices (GMP), whereas the formulation facility is GMP and USFDA approved.

Reputed customer base - The customer base of the company comprises reputed formulation players resulting in limited counterparty credit risk. The company also has a marketing arrangement through a Joint-Venture concern (50% stake) Concord Biotech Japan K.K to cater the Japanese market. The offtake to Japanese market has shown healthy growth in FY2021 and in the 7M FY2022 period, however remains not material in comparison to overall sales of the entity.

Strong financial profile - The company reported robust profit margins, with operating margin in the range of 40-43% and a net margin in the range of 27-34% over the last four fiscal years. The operating margins improved to 53.13% in FY2021 owing to improved realisations, better product mix as well as Covid related cost rationalizations. Its net-worth base (Rs. 999.37) crore as on March 31, 2021)) remained strong, supported by healthy annual cash accruals. This coupled with low dependence on external borrowings resulted in comfortable capital structure, with a gearing of 0.09 times and TOL/ TNW of 0.27 times as on March 31, 2021 and an overall negative net debt position. The gearing had moderated from the FY2020 levels owing to the increase in long-term debt following the debt funded capex of its new API plant (Unit-3). With low debt level and healthy profitability, debt protection metrics have remained robust—the interest coverage of 362.03 times in FY2021 was higher as the interest costs were capitalised as a part of the project cost. Therefore, post commercialisation of unit-3 the interest coverage has moderated to 49.16x for the 7M FY2022 period albeit remaining comfortable. Total Debt/OPBDITA has robust between 0.24-0.27 times between FY2020 and 7M FY2022 period.

Credit challenges

Moderate scale of operations with high concentration risk - The company's scale of operations remains relatively moderate in the pharmaceutical industry with operating income (OI) of Rs. 436.01 crore in FY2019, Rs. 512.33 crore in FY2020 and Rs. 616.41 crore in FY2021. It remains exposed to high concentration risk, with its immunotherapy category contributing significantly to the total revenue. The scale and diversification are expected to improve in the medium term, with the increase in sales from the formulation segment and stabilisation of the new API unit. Though its benefits from limited competition in the API segment, the competition remained intense in the formulation segment, the latter being characterised by the presence of numerous large organised as well as cost-competitive-players in India and outside India. Moreover, the competitive intensity remains high in the regulated markets with aggressive defence tactics by innovator companies. However, the company's dominant position in the immunosuppressant API business and repeat orders from its customers reflect a preferred supplier status, thereby limiting the risk to an extent.

High working capital intensity - The company normally provides a credit period of ~115-120 days to its key customers and maintains a high inventory of various cultures (raw material) to produce different APIs. The higher inventory is due to the lengthy fermentation process, whereby it takes about anywhere between 30-50 days for the cultures to undergo fermentation and purification. The company would require various chemical and organic compounds for nutrient supply during the fermentation process. Also, the WIP inventory remains high as it does not complete last stage (~1-5% of production process), until it receives the order, since the shelf life of the product starts after the completion of entire process. Hence, elongated receivables cycle and high inventory holding requirements have resulted in high working capital intensity of operations in the past. The working capital intensity ranged between 45%-55% in the last three financial years ending FY2021. Nonetheless, the same continues to remain high. Given the high working capital requirements, coupled with the high capex the free cashflows remained moderate in FY2020 and in FY2021.

Risks associated with successful scale up of the large on-going as well as recently completed capex- The company is in the process to set up a new unit for the manufacturing of injectables at a total cost of Rs. 135.0 crore. The funding of the capex is through internal accruals. The company has expended about ~Rs.25 crore as on October 31, 2021. The company had capitalised the unit-3, API plant in March 31, 2021 which is expected to report marginal revenue in FY2022 and is likely to report operating loss given under absorption of costs on a low top-line. The revenue for FY2023 is also likely to be subdued, given the company is looking to get requisite approvals for its unit-3 by Q1 of FY2024. Obtaining all the requisite approvals for both the plants, achieving healthy capacity utilisation levels with commensurate returns, through desired scaling up at reasonable size would remain critical from a credit perspective.

Liquidity position: Strong

The company's liquidity position is strong, reflected in healthy profitability and accruals, robust cash and liquid investments, and availability of cushion in the form of unutilised working capital limits. The estimated cash accruals will remain strong against debt repayments and adequate to fund the ongoing capex and incremental working capital requirements.

Rating sensitivities

Positive factors – Significant growth in scale and diversification of revenues along with improvement in working capital cycle, supporting free cash flows. Successful scale up of new capacities in a profitable manner so as to support overall financial profile will also be a positive rating trigger.

Negative factors – Negative pressure on the ratings could arise if there is any significant decline in revenues or material deterioration in margins. Moreover, higher-than-anticipated debt-funded capex or acquisitions, or any adverse regulatory measures that weakens the company's credit profile may trigger a rating downgrade. Inability to scale up new capacities in a profitable manner leading to deterioration in credit metrics, will also be a negative rating trigger.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Consolidation and rating approach Rating Methodology for entities in the Pharmaceutical Industry
Parent/Group Support	Not Applicable
Consolidation/Standalone	The rating is based on the consolidated financial profile of the company- details of which are given in Annexure-2

About the company

Concord Biotech Limited (CBL), incorporated in November 1984, was taken over by the current promoter, Mr. Sudhir Vaid, in 2000. Mr. Sudhir Vaid is a technocrat, having over four decades of experience in the field of biotechnology, which includes eight years as a director-of Fermentation at Ranbaxy Laboratories Limited and thereafter as a consultant to various leading pharmaceutical companies. It has a robust investor profile with Mr. Rakesh Jhunjhunwala and group holding ~24% and Helix Investment Holdings Pte Limited holding 20% stake in the company. Helix Investment Holdings Pte Limited is an SPV floated by Quadria Capital, which has invested in diverse healthcare chains across the Asia-pacific region.

CBL was initially set up with one manufacturing block for production of Amidase Enzyme. Capacities were subsequently added and at present it has 22 API manufacturing blocks. The company is involved in manufacturing fermentation and semi-synthetic biopharmaceutical active pharmaceutical ingredients with immunosuppressants as its key therapeutic segment. As a means of forward integration, it set up a formulation unit, which commenced commercial production from March 2017. The company enhanced its API capacities through commercialisation of Unit-3 plant in Limbasi, Gujarat in FY2021 and is in the process of setting up an injectables plant in Valthera Gujarat, expected to be commercialised by December'2022.

Key financial indicators (audited)

CBL- Consolidated	FY2020	FY2021
Operating Income (Rs. crore)	512.33	616.41
PAT (Rs.crore)^	168.96	235.33
OPBDIT/OI (%)	42.07%	53.13%
PAT/OI (%)	32.98%	38.18%
Total Outside Liabilities/Tangible Net Worth (times)	0.22	0.18
Total Debt*/OPBDIT (times)	0.24	0.27
Interest Coverage (times)	184.67	362.03

*All ratios as per ICRA calculations; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ^excludes share of profits/loss from JV; *Includes lease liability.*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)				Chronology of Rating History for the past 3 years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Oct 31, 2021 (Rs. crore)	Date & Rating in	Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019	
					April 07, 2022	Feb 04, 2021	Jun 30, 2020	Mar 01, 2019	Jan 25, 2019
1	Term Loans	Long-term	100.0	68.75	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)
2	Fund based Working Capital Limit	Long-term	15.0	--	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	-
3	Non-fund based Limit	Short-term	10.0		[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-

Complexity level of the rated instrument

Instrument	Complexity Indicator
Cash Credit	Simple
Term Loan	Simple
Letter of Credit	Very 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 analyzing 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	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. Crore)	Current Rating and Outlook
NA	Term Loans	FY2020	NA	FY2026	100.00	[ICRA]AA-(Stable)
NA	Fund based Working Capital Limit	NA	NA	NA	15.00	[ICRA]AA-(Stable)
NA	Non-fund based Limit	NA	NA	NA	10.00	[ICRA]A1+

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis

Company Name	CBL Ownership	Consolidation Approach
Concord Biotech Japan K.K	50%	Equity Method

Source: *Company data;* ***Note:*** *ICRA has taken a consolidated view of the CBL and JV concern while assigning the ratings.*

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