June 08, 2022

Everest Organics Limited: Ratings downgraded to [ICRA]BB/[ICRA]A4 from [ICRA]BB+/[ICRA]A4+; outlook revised to Negative from Stable

Summary of rating action

Instrument	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – Fund-based – Cash Credit	16.00	16.00	[ICRA]BB; downgraded from [ICRA]BB+; Outlook revised to Negative from Stable
Long-term – Fund-based – Term Loans	18.00	18.00	[ICRA]BB; downgraded from [ICRA]BB+; Outlook revised to Negative from Stable
Short-term – Non-fund based	6.00	6.00	[ICRA]A4; downgraded from [ICRA]A4+
Long-term/Short-term – Fund-based	7.00	7.00	[ICRA]BB/[ICRA]A4; downgraded from [ICRA]BB+/[ICRA]A4+; Outlook revised to Negative from Stable
Total	**47.00**	**47.00**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings downgrade factors in the expected moderation in Everest Organics Limited's (EOL) debt metrics and overall financial profile in FY2023 on account of low margins as raw material prices remain high while its ability to pass on the increased costs to end customers remain limited. Its operating margins significantly declined to 4.3% in FY2022 from 12.9% in FY2021 because of increased input costs; margins are expected to remain low in the next two quarters as well. Moreover, the company is expected to incur debt-funded capex of Rs. 20.0 crore in FY2023, which along with decline in profitability would impact its debt protection metrics. ICRA also takes note of the statutory auditor's qualifications in the recently published quarterly results concerning EOL's non-compliance with accounting standards below par corporate governance practices, EOL's production beyond approved limits etc. ICRA will continue to monitor the same.

The ratings consider EOL's moderate scale of operations and high revenue dependence on the mature anti-ulcerative therapeutic segment. The ratings are also constrained by the vulnerability of its profits to fluctuating raw material and finished goods prices owing to stiff competition in the active pharmaceutical ingredient (API) industry. The company's working capital intensity is moderate and is primarily funded by creditors.

The ratings, however, draw comfort from the company's stable revenue growth over the past three years, driven by an increase in commercial orders for the anti-ulcerative products, which is expected to continue over the medium term on the back of addition of new products. Moreover, EOL's established track record and customer relationships in the pharmaceutical industry resulted in repeat orders and healthy capacity utilisation levels.

The Negative outlook on the rating reflects ICRA's opinion that low profitability and debt-funded capex plans are expected to impact the company's debt metrics in the near term.

Key rating drivers and their description

Credit strengths

Extensive experience in pharmaceutical industry – The promoters have an established track record in the pharmaceutical industry, which enabled the company to have established relationships with various reputed formulation companies resulting in repeat orders over the years.

Healthy capacity utilisation levels – The plant capacity utilisation remains high at more than 90%, especially for the top two products—Omeprazole and Esomeprazole. Given the high utilisation levels, the company plans to expand the capacity of Esomeprazole, Pantoprazole and Benzimidazole, and newly added products in FY2023.

Credit challenges

Moderate scale of operations – Despite stable ramp-up in sales over the last two years, the scale remains moderate with revenues of Rs. 202.3 crore in FY2022. However, this is expected to improve over the medium term with proposed expansion of capacity, commercialisation of new products and exports to regulated markets.

Significant moderation in margins impacting debt protection metrics – The profitability margins of the company have decreased significantly in FY2022 owing to increase in the raw material prices and the company's inability to pass on the same to the customers. Further, the company's margins are expected to remain low in H1 FY2023 as well as high competition would limit the company's ability to pass on increased costs to its customers. While the company is expected to record 10-15% revenue growth in FY2023, its margins are expected to remain low at less than 5%. The debt indicators moderated in FY2022 due to decrease in profits and increased debt levels. ICRA expects debt indicators to moderate further in FY2023 on account of lower profitability and debt-funded capex.

Non-adherence to accounting standards and pollution control – In audited results published for FY2022, the company's auditor has provided qualified opinions which included production exceeding approved thresholds which could impact the going concern, overstatement of accruals and profit because of the revenue recognition policy which is not in line with IND-AS 115, absence of confirmation for a significant part (received only for Rs. 14.81 crore) of Rs. 68.04 crore debtors, adopting cash basis of accounting to recognize sales commission payable to the sales agents, absence of disclosures regarding the assets kept aside for sale, and absence of actuarial assessment to assess the gratuity liability. ICRA also takes note of the comments on below par corporate governance practices; continued non-adherence to accounting standards wherein production beyond approved limits could impact the company's business operations.

High exposure to mature anti-ulcerative segment – The company is focussed on the matured anti-ulcerative segment with the entire revenue over the years being generated from APIs and intermediates in this segment. Majority of the sales are derived from Omeprazole, Esomeprazole and Pantoprazole as they accounted for ~60% of EOL's revenues in the past four years. However, proposed launch of new products and ramp-up in sales volumes of recently launched products could reduce this risk to an extent.

High dependence on creditors for working capital requirements – The working capital requirements are mainly funded by creditors resulting in high TOL/TNW of 2.8 times as on March 31, 2022, which increased from 1.9 times as on March 31, 2021. The company receives high credit period from domestic suppliers, who account for ~70-80% of its raw material procurement, on the back of established relationships of the company.

Exposed to intense competition in the API industry – The pharmaceutical industry is intensely competitive due to the presence of various established bulk drug manufacturers resulting in limited pricing power and profitability.

Liquidity position: Stretched

The company's liquidity position is stretched with low cash balances and absence of any buffer in working capital limits. The company's retained cash flows are also expected to remain low at ~Rs. 6.0-10.0 crore in FY2023 with high term loan debt repayment obligations of Rs. 5.2 crore during the year. Moreover, the company has sizeable debt-funded capex plans; it also needs to rely on promoters' infusion to fund the capex.

Rating sensitivities

Positive factors – Ratings are unlikely to be upgraded in the near term, given the Negative outlook on the long-term rating. ICRA could upgrade the ratings if the company demonstrates recovery in the operating margins and improvement in liquidity position, while recording healthy growth in scale of operations leading to improved debt metrics. Adherence to all the requisite accounting standards and regulatory norms also remains critical monitorable.

Negative factors – Negative pressure on EOL's rating could arise if there is significant decline in revenues, while profitability continues to remain low on a sustained basis, or deterioration in working capital cycle impacts the company's liquidity position further. Also, the company's inability to comply with regulatory norms or accounting standards on a continual basis could lead to a rating downgrade.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology - Pharmaceuticals
Parent/Group Support	Not applicable
Consolidation/Standalone	The ratings are based on the company's standalone financial profile.

About the Company

Everest Organics Limited was established in 1993 by Dr. Srihari Raju. It is currently managed by his daughter, Dr. Sirisha Kakarlapudi who is the new CEO of EOL. Initially incorporated as a private limited company, it went public and was listed on the BSE in 1995. The company manufactures APIs and intermediates such as Omeprazole, Esomeprazole, Pantoprazole, Chloro compound and Benzimadizole. Its manufacturing facility is at Aroor Village, in Medak district of Telangana with an installed production capacity of 820 MTPA. The company is ISO 9001-2008 certified, while the plant is WHO-GMP certified. The manufacturing facility also received US FDA approval in June 2017.

Key financial Indicators (Audited)

	FY2021	FY2022
Operating Income (Rs. crore)	182.1	202.3
PAT (Rs. crore)	13.7	1.1
OPBDIT/OI (%)	12.9	4.3
PAT/OI (%)	7.5	0.6
Total Outside Liabilities/Tangible Net Worth (times)	1.9	2.8
Total Debt/OPBDIT (times)	1.0	4.5
Interest Coverage (times)	7.2	2.8

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation;

Source: Company & BSE

Status of non-cooperation with previous CRA: NA

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2023)				Chronology of Rating History for the past 3 years				
		Type	Amount Rated (Rs. crore)	Amount Outstanding as on March 31, 2022 (Rs. crore)	Date & Rating on	FY2022	FY2021			FY2020
					June 08, 2022	December 15, 2021	February 19, 2021	September 09, 2020	August 31, 2020	-
1	Cash Credit	Long Term	16.00	-	[ICRA]BB (Negative)	[ICRA]BB+ (Stable)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	-
2	Term Loans	Long Term	18.00	15.40	[ICRA]BB (Negative)	[ICRA]BB+ (Stable)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	-
3	Non-fund Based	Short Term	6.00		[ICRA]A4	[ICRA]A4+	[ICRA]A3	[ICRA]A3	[ICRA]A3	-
4	Fund-Based	Long/Short Term	7.00	-	[ICRA]BB (Negative)/ [ICRA]A4	[ICRA]BB+ (Stable)/ [ICRA]A4+	[ICRA]BBB- (Stable)/ [ICRA]A3	[ICRA]BBB- (Stable)/ [ICRA]A3	[ICRA]BBB- (Stable)/ [ICRA]A3	-
5	Unallocated	Long/Short Term	0.00	-	-	-	[ICRA]BBB- (Stable)/ [ICRA]A3	[ICRA]BBB- (Stable)/ [ICRA]A3	[ICRA]BBB- (Stable)/ [ICRA]A3	-

Complexity level of the rated instrument

Instrument	Complexity Indicator
Long Term – Fund based – Term Loan	Simple
Long Term – Fund based - Cash Credit	Simple
Short Term – Non Fund based – Letter of Credit/ Bank Guarantee	Very Simple
Long Term/Short Term – Fund based - Bill Discounting/ Export Packaging Credit	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

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	Cash Credit	-	-	-	16.00	[ICRA]BB (Negative)
NA	Term Loan	2021	-	2027	18.00	[ICRA]BB (Negative)
NA	Letter of Credit	-	-	-	5.50	[ICRA]A4
NA	Bank Guarantee	-	-	-	0.50	[ICRA]A4
NA	Bill Discounting/Export Packaging Credit				7.00	[ICRA]BB(Negative)/ [ICRA]A4

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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