August 22, 2022

Everest Organics Limited: Long-term rating downgraded; short-term rating reaffirmed; outlook revised to Stable from Negative

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	Long term rating downgraded to [ICRA]B+ from [ICRA]BB; outlook revised to Stable from Negative
Long-term – Fund-based – Term Loans	18.00	18.00	Long term rating downgraded to [ICRA]B+ from [ICRA]BB; outlook revised to Stable from Negative
Short-term – Non-fund based	6.00	6.00	[ICRA]A4; reaffirmed
Long-term/Short-term – Fund-based	7.00	7.00	Long term rating downgraded to [ICRA]B+ from [ICRA]BB/[ICRA]A4 reaffirmed; outlook revised to Stable from Negative
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 as subdued demand from its customers impacts its revenues, earnings and debt protection metrics. The company recorded 16.2% YoY decline in revenues in Q1 FY2023, majorly due to decrease in demand for its products. Lower scale and higher input costs resulted in operating losses for the company during the quarter. While ICRA expects the company's performance to improve in H2 FY2023, the overall margins for the year are expected to remain weak, leading to stretched debt metrics. The company's liquidity also remains stretched with significant build-up of inventory and high receivables. Moreover, the company is expected to incur debt-funded capex of Rs. 18.0 crore in FY2023, which would impact its liquidity position and debt 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 and below par corporate governance practices. 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 established track record and customer relationships in the pharmaceutical industry, resulting in repeat orders and healthy capacity utilisation levels.

The Stable outlook on the rating reflects ICRA's opinion that EOL's revenues would improve with steady demand for existing products and launch of new products, and it will continue to benefit from its long association with the customers.

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 – The company's scale of operations is moderate despite a stable ramp-up in sales over the last two years. The total operating income has declined significantly in Q1 FY2023 due to decrease in APIs and intermediates owing to low demand for the products and the revenues are expected to remain low in the next quarter also. Although the scale of operations is expected to improve from Q3 FY2023, overall, the company is expected to witness a marginal decline in revenues in FY2023.

Significant moderation in margins impacting debt protection metrics – The company's profitability margins have decreased significantly in Q1 FY2023 owing to increase in raw material prices and input costs. Further, the company's margins are expected to remain low in Q2 FY2023 as well on account of muted demand and higher input costs. While ICRA expects the company's performance to improve in H2 FY2023, the overall margins for the year are expected to remain weak, leading to stretched debt metrics. ICRA expects debt indicators to be impacted further on account of and debt-funded capex.

Non-adherence to accounting policies and pollution control – In the quarterly results published for Q1 FY2023 and also the audited results published for FY2022, the company's auditor has provided qualified opinions which included production exceeding the 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 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 policies and /or 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 last four years. However, the proposed launch of products and ramp-up in the sales volumes of the recently launched products could reduce this risk to an extent.

Stretched liquidity position and high dependence on creditors for working capital requirements – The company's liquidity position stood stretched owing to high debtors and inventory and the company offers a credit period of 2-3 months to its customers and also maintains an average inventory of 60-90 days. Also, the creditors remained high in Q1 FY2023 and the working capital requirements are mainly funded by creditors, resulting in high TOL/TNW of 3.2 times as on June 30, 2022, which increased from 2.8 times as on March 31, 2022. 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 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. 8.0-12.0 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; a part of which needs to be funded from internal accruals.

Rating sensitivities

Positive factors – ICRA could upgrade the ratings if the company demonstrates recovery in the operating margins and improvement in liquidity position while recording healthy growth in the scale of operations, leading to improved debt metrics.

Negative factors – Negative pressure on EOL's rating could arise if there is a significant decline in revenues, or if there is no material improvement in earnings, or if the working capital cycle deteriorates, impacting the company's liquidity position further. Also, the company's inability to comply with the regulatory norms or accounting policies will be a key monitorable.

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 the 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)

EOL	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 O/s as on Mar 31, 2022 (Rs. crore)	Date & Rating on	Date & Rating on	FY2022	FY2021			FY2020
					Aug 22, 2022	Jun 08, 2022	Dec 15, 2021	Feb 19, 2021	Sep 09, 2020	Aug 31, 2020	-
1	Cash Credit	Long Term	16.00	-	[ICRA]B+(Stable)	[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]B+(Stable)	[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]A4+	[ICRA]A3	[ICRA]A3	[ICRA]A3	-
4	Fund-Based	Long/ Short Term	7.00	-	[ICRA]B+(Stable)/ [ICRA]A4	[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 are available on ICRA's website: www.icra.in

Annexure I: 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]B+(Stable)
NA	Term Loan	2021	-	2027	18.00	[ICRA]B+(Stable)
NA	Letter of Credit	-	-	-	5.50	[ICRA]A4
NA	Bank Guarantee	-	-	-	0.50	[ICRA]A4
NA	Bill Discounting/Export Packaging Credit				7.00	[ICRA]B+(Stable)/[ICRA]A4

Source: *Company*

Annexure II: 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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