August 30, 2019

Indoco Remedies Limited: Ratings revised to [ICRA]A(Negative)/[ICRA]A2+

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Loans	250.00	250.00	[ICRA]A(Negative); revised from [ICRA]A+(Negative)
Long-term, Fund-based Limits	29.40	29.40	[ICRA]A(Negative); revised from [ICRA]A+(Negative)
Long-term, Non-fund Based Limits	24.37	24.37	[ICRA]A(Negative); revised from [ICRA]A+(Negative)
Short-term, Fund-based Limits	20.00	20.00	[ICRA]A2+; revised from [ICRA]A1
Short-term, Non-fund Based Limits	20.25	20.25	[ICRA]A2+; revised from [ICRA]A1
Long-term/Short-term, Fund-based Limits	25.00	25.00	[ICRA]A(Negative)/[ICRA]A2+ revised from [ICRA]A+(Negative)/[ICRA]A1
Long-term/Short-term, Unallocated Limits	60.00	60.00	[ICRA]A(Negative)/[ICRA]A2+ revised from [ICRA]A+(Negative)/[ICRA]A1
Commercial Paper Programme	25.00	-	[ICRA]A2+; revised from [ICRA]A1 and withdrawn
Total	**454.02**	**429.02**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings revision factors in the slower-than-expected improvement in Indoco Remedies Limited's (IRL's) international formulations business, owing to pending resolution of regulatory non-compliances. While some improvement in revenues was witnessed in Q1 FY2020 led by a pickup in sales in the European and emerging markets as well as improved performance in the domestic formulations business, a meaningful improvement in revenues and profitability remains highly contingent on the timely resolution of the regulatory non-compliances. This also exposes the company to refinancing risks, given its sizeable upcoming debt repayments, amounting to Rs. 54-57 crore per annum over the next two years. The company's credit profile, which weakened over the last two years, is thus expected to remain moderate. ICRA, however, derives some comfort from the company's adequate liquidity position, as evinced in moderate average working capital utilisation of 69% over the last 15 months. The ratings also derive strength from IRL's experienced management and established brands in the domestic formulations market.

IRL received regulatory observations from the Medicines and Healthcare Products Regulatory Agency of the United Kingdom (UK-MHRA) for its Goa-Plant I in March 2018, following which it received a restricted Good Manufacturing Practices (GMP) certificate to manufacture and supply 50 stock keeping units (SKUs) critical to public health in the UK. The ramp-up in the same, however, remained muted in FY2019 as IRL was testing certain critical parameters in the products to be supplied. One of IRL's key customers was also conducting its own audit of IRL's plant in FY2019 and resumed supplies only in Q1 FY2020. The revenue run rate for the Europe business is expected to improve in the coming quarters as the company starts supplying additional products from its recently UK-MHRA-approved Baddi-Plant III.

Nonetheless, large-scale improvement in the revenues will be driven only by re-instatement of the EU-GMP certificate for IRL's Goa-Plant I. IRL also received a warning letter from the United States Food and Drug Administration (USFDA) for its Goa-Plant I in July 2019. Furthermore, notwithstanding the successful resolution of the warning letters issued to Goa-Plant II and III in March 2019, revenue pickup in the US markets is expected to happen only from Q4 FY2020 (against earlier expectations of Q1 FY2020) as the company is now required to conduct new studies as per the revised USFDA container closure norms. IRL's key marketing partner in the US, TEVA Pharmaceuticals, is also reluctant to market some of the pending abbreviated new drug applications (ANDAs), which are now required to be filed in IRL's own name. All these factors are expected to result in lower-than-earlier-envisaged improvement in export formulations sales. IRL's domestic formulations business witnessed an 8% YoY revenue growth in Q1 FY2020 supported by healthy demand. The revenue run rate also improved for emerging markets in Q1 FY2020. The company's ability to sustain this momentum (of Q1 FY2020) in the coming quarters as well as improve sales to the Europe and US markets as envisaged is a critical rating monitorable. Besides, timely resolution of the observations by the UK-MHRA as well as the warning letter by the USFDA, and consequent scale-up of operations and improvement in IRL's profitability remain the key rating sensitivities.

Notwithstanding IRL's presence in mature molecules in the domestic market, it has a wide therapeutic coverage with a strong presence in anti-infectives, respiratory systems and dental therapies, with its major brands positioned among the top five in their respective categories. ICRA notes the regulatory risks associated with pricing controls in the domestic market. The company also remains exposed to foreign currency fluctuations, given its exports. However, the risk is partially mitigated as IRL enters into forward contracts for its export receivables.

ICRA has also revised the rating assigned to IRL's Rs. 25-crore commercial paper programme to [ICRA]A2+ (pronounced ICRA A two plus) from [ICRA]A1 (pronounced ICRA A one) and withdrawn the same, as there is no amount outstanding against the rated instrument.

Outlook: Negative

The Negative outlook reflects IRL's exposure to refinancing risks, due to moderate accruals and sizeable upcoming debt repayments. The ratings may be downgraded if the company is unable to improve sales to the Europe and US markets as envisaged and sustain the revenue momentum (exhibited in Q1 FY2020) in the domestic and emerging markets in the coming quarters. Timely resolution of the regulatory non-compliances is essential for ensuring a meaningful recovery in sales and profitability, and is a key rating sensitivity. The outlook may be revised to Stable, following a meaningful ramp-up in sales and improvement in profitability as well as resolution of the regulatory non-compliances in a timely manner.

Key rating drivers

Credit strengths

Established brands in respiratory, dental and anti-infective therapies of domestic formulations market - IRL's presence in the domestic market is primarily limited to mature molecules in acute therapies with intense competition. Notwithstanding this, it has a wide therapeutic coverage with a strong presence in anti-infectives, respiratory systems and dental therapies. The company enjoys a healthy reputation in the domestic market, with its major brands positioned among the top five in their respective therapy segments. However, given the matured molecules and the presence of many players, IRL's market share and pricing power remain low.

Experienced management - The company's operations are currently managed by Ms. Aditi Kare Panandikar and Mr. Sundeep Bambolkar, who have over 30 years of experience in the pharmaceutical industry.

Credit challenges

Pending resolution of regulatory non-compliances - IRL is yet to resolve the observations issued to its Goa-Plant I by the UK-MHRA, which remains under the restricted GMP list, and has additionally received a warning letter from the USFDA in July 2019. While some improvement in revenues was witnessed in Q1 FY2020, a meaningful improvement in its revenues and profitability remains highly contingent on the timely resolution of these regulatory non-compliances. Furthermore, notwithstanding the successful resolution of the warning letters issued to its Goa-Plant II and III, revenue pickup in the US is expected to happen only from Q4 FY2020 (against earlier expectations of Q1 FY2020) as the company is now required to conduct new studies as per the revised USFDA container closure norms.

Moderate credit profile; increased refinancing risks - The company's credit profile weakened over the last two years, amid a decline in accruals and elevated debt levels. This is evinced in TD/OPBDITA of 3.8x (1.8x as on March 31, 2017), DSCR of 1.2x (6.8x as on March 31, 2017) and NCA/TD of 17% (47% for FY2017) in FY2019. In the absence of any meaningful improvement in revenues and profitability, the company's credit profile is expected to remain moderate. The company is also exposed to high refinancing risks, given its significant upcoming debt repayments amounting to Rs. 54-57 crore per annum over the next two years. ICRA, however, derives some comfort from the company's adequate liquidity position, as evinced in its moderate average working capital utilisation of 69% over the last 15 months.

Domestic formulations industry vulnerable to changes in Government policies related to price control - Any adverse change in the Government policies related to price control can lead to pricing pressures and impact the profitability of IRL's domestic formulations business.

Liquidity position

IRL's liquidity position is adequate, as evinced in moderate average working capital utilisation of 69% over the last 15 months. As on July 31, 2019, the company had unutilised fund-based working capital limits of Rs. 41 crore. The free cash and bank balances as on March 31, 2019 stood at Rs. 20 crore.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Methodology for Pharmaceutical Industry
Parent/Group Support	Not applicable
Consolidation/Standalone	The ratings are based on the standalone financial profile of the company

About the company

IRL, established by Mr. Govind Ramnath Kare in 1945 as Indo Continental Trading Company, imported pharmaceutical formulations from Europe and sold them in India. In 1963, the current Chairman and Managing Director, Mr. Suresh G. Kare, took over.

At present, IRL manufactures and markets branded formulations and active pharmaceutical ingredients (APIs), and undertakes contract research and manufacturing services (CRAMS) with a strong presence in domestic formulations, which contributed ~64% to its total revenues in FY2019. In the domestic business, IRL has a prominent presence in anti-infective, respiratory, gastro-intestinal and dental segments, with its major brands positioned among the top five in their respective categories.

IRL's formulation plants are located at Goa (three plants), Mumbai, Waluj (Aurangabad) and Baddi (Himachal Pradesh), while its API plants are located at Patalganga (Maharashtra) and Rabale (Navi Mumbai). In FY2017, IRL acquired Micro

Labs Limited's solid oral dosage manufacturing facility located in Baddi, which is now being utilised to manufacture formulations for the European and UK markets, post receipt of the EUGMP certification and the UK-MHRA approval.

In FY2019, IRL reported a net loss of Rs. 2.8 crore on an operating income (OI) of Rs. 967.7 crore, against a profit after tax (PAT) of Rs. 41.2 crore on an OI of Rs. 1,038.2 crore in FY2018. In Q1 FY2020 (unaudited), IRL reported a PAT of Rs. 2.2 crore on an OI of Rs. 252.7 crore, against a net loss of Rs. 12.0 crore on an OI of Rs. 214.3 crore in Q1 FY2019.

Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	1,038.2	967.7
PAT (Rs. crore)	41.2	-2.8
OPBDIT/OI (%)	13.2%	8.0%
RoCE (%)	8.6%	1.4%
Total Debt/TNW (times)	0.4	0.4
Total Debt/OPBDIT (times)	2.1	3.8
Interest Coverage (times)	5.8	3.8

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Current Rating (FY2020) Date & Rating	Chronology of Rating History for the Past 3 Years: Date & Rating in FY2019				Date & rating in FY2018			Date & Rating in FY2017	
					August 2019	January 2019	November 2018	September 2018	August 2018	April 2018	November 2017	April 2017	July 2016	April 2016
1	Term Loans	Long-term	250.0	147.2*	[ICRA]A (Negative)	[ICRA]A+ (Negative)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]AA- (Negative)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
2	Fund-based Limits	Long-term	29.40	NA	[ICRA]A (Negative)	[ICRA]A+ (Negative)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]AA- (Negative)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
3	Non-fund Based Limits	Long-term	24.37	NA	[ICRA]A (Negative)	[ICRA]A+ (Negative)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	-	-	-	-	-
4	Fund-based Limits	Short-term	20.00	NA	[ICRA]A2+	[ICRA]A1	[ICRA]A1	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
5	Non-fund Based Limits	Short-term	20.25	NA	[ICRA]A2+	[ICRA]A1	[ICRA]A1	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
6	Fund-based Limits	Long-term/ Short-term	25.00	NA	[ICRA]A (Negative)/ [ICRA]A2+	[ICRA]A+ (Negative)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	-	-	-	-	-	-
7	Unallocated	Long-term/ Short-term	60.00	NA	[ICRA]A (Negative)/ [ICRA]A2+	[ICRA]A+ (Negative)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1+	[ICRA]A+ (Stable)/ [ICRA]A1+	-	-	-	-	-

8	Commercial Paper Programme	Short-term	25.00	NA	[ICRA]A2+; withdrawn	[ICRA]A1	[ICRA]A1	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

**As on June 30, 2019*

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 www.icra.in

Annexure-1: Instrument Details

ISIN No	Instrument	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
-	Term Loan 1	June2016	9.50%	July 2020	55.0	[ICRA]A(Negative)
-	Term Loan 2	September2016	6.70%	September2021	55.0	[ICRA]A(Negative)
-	Term Loan 3	September2016	5.60%	September2021	55.0	[ICRA]A(Negative)
-	Term Loan 4	December 2016	9,15%	December 2021	35.0	[ICRA]A(Negative)
-	Term Loan 5	FY2018	8.05%	FY2025	50.0	[ICRA]A(Negative)
-	Cash Credit 1	-	-	-	8.4	[ICRA]A(Negative)
-	Cash Credit 2	-	-	-	12.0	[ICRA]A(Negative)
-	Cash Credit 3	-	-	-	9.0	[ICRA]A(Negative)
-	Non-fund Based 1	-	-	-	12.66	[ICRA]A(Negative)
-	Non-fund Based 2	-	-	-	11.71	[ICRA]A(Negative)
-	Fund-based 1	-	-	-	10.0	[ICRA]A2+
-	Fund-based 2	-	-	-	10.0	[ICRA]A2+
-	Non-fund Based 1	-	-	-	5.25	[ICRA]A2+
-	Non-fund Based 2	-	-	-	3.0	[ICRA]A2+
-	Non-fund Based 3	-	-	-	5.0	[ICRA]A2+
-	Non-fund Based 4	-	-	-	7.0	[ICRA]A2+
-	Fund-based 1	-	-	-	10.0	[ICRA]A(Negative)/ [ICRA]A2+
-	Fund-based 2				15.0	[ICRA]A(Negative)/ [ICRA]A2+
-	Unallocated	-	-	-	60.0	[ICRA]A(Negative)/ [ICRA]A2+
-	Commercial Paper Programme	-	-	-	-	[ICRA]A2+; withdrawn

Source: Indoco Remedies Limited

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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.

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