

June 30, 2020

Concord Biotech Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based Term Loan	100.00	100.00	[ICRA]AA- (Stable); reaffirmed
Fund-based Working Capital Facilities	20.00	15.00	[ICRA]AA- (Stable); reaffirmed
Non-fund based Letter of Credit	6.00	10.00	[ICRA]A1+; reaffirmed
Total	126.00	125.00	

*Instrument details are provided in Annexure-1

Rationale

The rating reaffirmation continues to reflect the extensive experience of the promoters and the established track record of the company in the fermentation and semi-synthetic biopharmaceutical (API) business, spanning around two decades. Further, the company's strong financial profile, characterised by healthy profitability levels, robust debt protection indicators and strong liquidity, has been factored in the rating assessment. The ratings also factor in the company's key market player 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 current operations, its high product concentration and high working capital intensity, owing to the elongated receivable cycle and high inventory holding period. Given the high working capital requirements, along with the capex and dividend outgo, the company has reported negative free cash flows in FY2020. Although the company remains one of the key players and faces limited competitive pressures in the API segment, the formulation segment entails high level of competitive pressures. ICRA also notes that the company is currently in the midst of a large debt-funded capex for increase in API capacity at a total cost ~Rs. 366 crore; and achieving healthy capacity utilisation and profitability levels would remain critical from a credit perspective.

ICRA also notes that the company has reported a de-growth of 33% in its April 2020 revenue (as compared to April 2019) owing to the lockdown imposed due to the outbreak of the Covid-19 pandemic, however the revenues have recovered from May 2020 onwards with the company expected to report moderate growth in the current fiscal. Nonetheless, ICRA will continue to monitor the impact of Covid-19 pandemic and other aligned regulatory restrictions on the company's operations in case of prolongation of existing conditions.

The Stable outlook on the [ICRA]AA- rating reflects ICRA's opinion that the company will continue to benefit from the extensive experience of its promoters in the biopharmaceutical industry and is likely to witness revenue growth, backed by new business garnered from the formulation segment and stable demand conditions for the API segment, supported by the ongoing capex for capacity enhancement.

Key rating drivers and their description

Credit strengths

Experienced management and established track record of company – 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.

Key market player in niche product segment - The company's key products – Tacrolimus and Mycophenolate (Mofetil and Sodium) are low volume but high value-added niche products catering to the immunosuppressants therapeutic segment. These complex molecules are exposed to limited competition and garner healthy margins. Although the molecules cumulatively contribute ~65%-72% to the company's revenues, the company is one of the key players in the industry for these products, commanding a healthy and increasing market share. The molecules have shown volume growth YoY, despite being off-patent, and have supported the revenues of the company. Going forward, healthy growth is projected for these APIs, given the company's ongoing production capacity expansion plans to cater to the growing demand from its customers.

Strong R&D capabilities and adequate regulatory approvals - The R&D centre of the company 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, such as - Intas Pharmaceuticals Limited, Mylan Inc., Alkem Laboratories Limited, Glenmark Pharmaceuticals, resulting in limited counterparty credit risk.

Strong financial risk profile - The profit margins of the company remained robust, with an operating margin in the range of 40-43% and a net margin in the range of 27-33% over the last few years. Net-worth base (Rs. 770.66 crore as on March 31, 2020) remained strong, supported by healthy annual cash accruals. This coupled with low dependence on external borrowings has resulted in comfortable capital structure, with a gearing of 0.06 times and TOL/ TNW of 0.21 times as on March 31, 2020 and an overall negative net debt position. Owing to low debt level and healthy profitability, debt protection metrics have remained robust—with the interest coverage of 278.12 times and Total Debt/ OPBDITA of 0.23 times in FY2020 as compared to 194.16 times and 0.05 times respectively for FY2019.

Credit challenges

Moderate scale of operations with high concentration risk - The company's scale of operations, though witnessed a healthy y-o-y growth of 29% from Rs. 337.99 crore in FY2018 to Rs. 436.01 crore in FY2019 and further by 17% to Rs. 511.41 crore in FY2020, remained relatively moderate. The company remains exposed to high concentration risk, with its top-three products contributing ~65%-72% 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. It also remains exposed to limited competition in the API segment and intense competition 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. 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 ~90-120 days to its key customers and maintains a high inventory of various cultures (raw material) to produce different APIs. 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 lowered from 77% in FY2018 to 52% in FY2019 and 47% in FY2020 because of faster collection of receivables and lower sales and purchase concentration in the last quarter; nonetheless, the same continues to remain high. Given the high working capital requirements, coupled with the high capex and dividend outgo, the company has reported negative free cash flows in FY2020.

Risks associated with large on-going capex - The company is exposed to the risks associated with timely completion and stabilisation of the expansion project, without any significant cost and time overruns. The company is in the process to set up a new unit for the manufacturing of API at a total cost of Rs. 366.00 crore (scope of work and cost increased from Rs. 224.75 crore estimated earlier). The new unit is expected to be operational by H2FY2021. The funding of the capex is through a mix of term loan and internal accruals, with debt-to-equity ratio of 0.38 times. The increase in debt exposure will result in some moderation in capital structure and debt coverage indicators in the near term, although both are expected to continue to remain healthy.

Liquidity position: Strong

The liquidity position of the company is strong, reflected in healthy profitability and accruals (Rs. 111.23 crore in FY2019 and Rs. 96.61 crore in FY2020), robust cash and liquid investments of Rs. 202.03 crore, and availability of cushion in the form of unutilised working capital limits of Rs. 15.00 crore as on March 31, 2020. 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 triggers –

- Significant growth in scale and diversification of revenues
- Sustained improvement in free cash flows

Negative triggers –

- Negative pressure on CBL's ratings could arise if there is any significant decline in revenues or material deterioration in margins.
- Higher-than-anticipated debt-funded capex or acquisitions, or regulatory measures that weakens the company's credit profile

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for 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

Concord Biotech Limited, 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. The company also 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 18 healthcare chains across the Asia-pacific region.

Concord Biotech Limited was initially set up with one manufacturing block for production of Amidase Enzyme. Capacities were subsequently added with the current facilities, comprising of 22 API manufacturing blocks. The company is involved in the manufacture of 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. It is currently under the process of setting up a new API unit, which is expected to commence commercial production from October 2020.

Key financial indicators (audited)

	FY2019	FY2020*
Operating Income (Rs. crore)	436.01	511.41
PAT (Rs. crore)	118.39	168.64
OPBDIT/OI (%)	41.45%	40.83%
RoCE (%)	27.77%	31.37%
Total Outside Liabilities/Tangible Net Worth (times)	0.12	0.21
Total Debt/OPBDIT (times)	0.05	0.23
Interest Coverage (times)	194.16	278.12

**provisional financials*

Status of non-cooperation with previous CRA: N/A

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)			Rating History for the Past 3 Years				
		Type	Amount Rated	Amount Outstanding*	Rating	FY2020	FY2019		FY2018
					30-Jun-2020	-	01-Mar-2019	25-Jan-2019	-
1	Term Loan	Long Term	100.00	48.03	[ICRA]AA-(Stable)	-	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	-
2	Cash Credit	Long Term	15.00	-	[ICRA]AA-(Stable)	-	[ICRA]AA-(Stable)	-	-
3	Letter of Credit	Short Term	10.00	-	[ICRA]A1+	-	[ICRA]A1+	-	-

Amount in Rs. crore *As on March 31, 2020

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	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan	FY2020	NA	FY2026	100.00	[ICRA]AA- (Stable)
NA	Cash Credit	NA	NA	NA	15.00	[ICRA]AA- (Stable)
NA	Letter of Credit	NA	NA	NA	10.00	[ICRA]A1+

Source: Concord Biotech Limited

Annexure-2: List of entities considered for consolidated analysis

N/A

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