August 10, 2020

Syngene International Limited: Long-term rating upgraded to [ICRA]AA+ (Stable) from [ICRA]AA (Positive); short-term rating of [ICRA]A1+ reaffirmed

Summary of rated instruments

Instrument*	Previously Rated Amount(Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term loans (External Commercial Borrowings)	606.60	375.00	Rating upgraded to [ICRA]AA+ from [ICRA]AA; outlook on the long-term rating revised to stable from positive
Long-term fund based	-	136.00	Rating upgraded to [ICRA]AA+ from [ICRA]AA; outlook on the long-term rating revised to stable from positive
Long-term/short-term unallocated	353.40	-	-
Short-term fund based	-	379.50	
Short-term non-fund based	-	13.80	[ICRA]A1+ reaffirmed
Short-term unallocated	-	55.70	
Total	**960.00**	**960.00**	

**Instrument details in Annexure – I*

Rationale

The revision in the long-term rating considers Syngene International Limited's (Syngene) healthy business prospects over the medium term supported by the robust demand for services from contract research organisations (CROs) and Syngene's new business additions/scope enhancements. Globally, CROs are expected to benefit from the trend of pharmaceutical companies increasingly outsourcing their research activities, and Indian CROs are in an advantageous position, given their cost competitiveness. Syngene's operating income (OI) grew by 11.1% year on year (YoY) in FY2020 to Rs. 2,026.3 crore aided by healthy performance across segments and improved traction in discovery services. For FY2021, Syngene is expected to witness double-digit growth, despite the flattish revenues in Q1 FY2021. While the company already has an integrated presence across discovery, development and manufacturing services, the scaling up of operations in Syngene's recently commenced Mangalore facility, would diversify Syngene's operations further and strengthen its position in the drug-discovery-to-manufacture value chain.

Syngene continued to maintain its healthy profit margins, with an operating profit margin (OPM) of 30.5% (previous year (PY): 29.4%) and net margin of 20.3% in FY2019 (PY: 18.2%). The company's core return on capital employed (core RoCE) stood at a healthy 26.9% in FY2020 (PY: 29.4%) despite the ongoing capex. Syngene's liquidity position also remained strong with cash and liquid investments of Rs. 1,019.9 crore as on March 31, 2020[1] and it remained net debt negative as

[1] Only includes investments with maturity period less than a year

on the said date. Although the company has a total capex plan of ~Rs. 700 crore ($100 million) and repayment obligations of about Rs. 376.7 crore for FY2021, ICRA draws comfort from the anticipated healthy accruals from the business. Syngene is expected to remain net debt negative over the medium term.

ICRA notes that the significant growth opportunities in the contract research space could increase competition going forward, resulting in pricing pressure and margin compression. However, the company's robust infrastructure/employee skillset, constant focus on compliance and safety, and its established client relationships are likely to mitigate competitive threats to a large extent. Akin to other industry players, the company is bound by strict regulations for clinical trials for regulated markets. Nevertheless, Syngene's legacy of zero regulatory issues in clinical trials provides comfort.

Given that about 96% of its revenues are from overseas markets, Syngene's revenues and margins are susceptible to unfavourable forex movements. However, the hedging mechanism adopted by the company (hedging majority of its net exposure over the next 24 months through forwards and put-option contracts) mitigates the forex risk to an extent. Syngene also has high customer and geographic concentration currently, with 62% of its revenues in FY2019 from its top 10 customers and 76% of its revenues in FY2020 from USA.

Syngene is a subsidiary of Biocon Limited (Biocon; rated [ICRA]AA+ (Stable)/[ICRA]A1+) and contributed to 32% of the consolidated revenue and 46% of the consolidated net profit of the latter in FY2020. Although the company does not require operational or financial support from the parent, Syngene enjoys implicit financial and operational flexibility by virtue of being Biocon's subsidiary.

Key rating drivers and their description

Credit strengths

- **Strong business profile with integrated presence across discovery, development and manufacturing services** – Syngene has presence across discovery, development and contract manufacturing services for small and large molecules. The company operates through four verticals, namely a) dedicated R&D centres for global majors like BMS, Baxter, Amgen and Herbalife; b) discovery services; c) development; and d) manufacturing services. The company's Mangalore plant (for commercial scale manufacturing of APIs/novel drugs/small molecules) commenced operations in March 2020 and is currently undergoing qualification testing. Scaling up of manufacturing over the medium term is expected to diversify the company's revenue stream and strengthen its position in the drug-discovery-to-manufacture value chain.

- **Established client relationships; healthy client addition in the last one year** – The company has long-term research contracts with reputed clients like BMS, Baxter, Amgen and Herbalife. About 25% of its customers have engaged with the company for over five years. Syngene has also increased its client base by ~30 customers to over 360 clients in FY2020. The deeper engagements and client additions provide revenue visibility for Syngene over the medium term.

- **Healthy revenue growth in FY2020; expected to continue going forward** – Aided by healthy performance across segments and improved traction in discovery services, Syngene reported a healthy growth of 11.1% in OI to Rs. 2,026.3 crore in FY2020 from Rs. 1,823.7 crore in FY2019. The company had a one-time pass-through billing of Rs. 40.0 crore in FY2019; excluding that, the operating income grew by 13.6% on YoY basis in FY2020. The growth in the discovery services segment was driven by contract renewals, expansion of business collaborations with existing clients and addition of new clients. The company's revenues are expected to witness double-digit growth on YoY basis in FY2021, despite the flattish revenues in Q1 FY2021, supported by the anticipated healthy growth in the global contract research industry and higher growth in Asia, and Syngene's new business additions.

- **Strong financial profile** – Syngene continued to maintain its profit margins and profitability at healthy levels, with an operating profit margin (OPM) of 30.5% (against 29.4% in FY2019), net margin of 20.3% (against 18.2% in FY2019) and core RoCE of 26.9% in FY2020. Further, the company was net debt negative at Rs. 247.0 crore[2] as on March 31, 2020, while its interest coverage remained strong at 17.9 times for FY2020. For Q1 FY2021, the company reported operating and net margin of 29.8% and 13.9% respectively, while its interest coverage stood at 16.8 times. Syngene's margins are likely to remain healthy and the company is likely to continue to be net debt negative over the medium term.

- **Strong parentage** – Syngene is a subsidiary of Biocon Limited (rated [ICRA]AA+ (Stable)/[ICRA]A1+). The company has robust infrastructure (with over 4,200 scientists and 1.9 million sq ft of research space) and strong accruals. Thus, it does not require operational or financial support from the parent. However, Syngene enjoys implicit financial and operational flexibility by virtue of its parentage.

Credit challenges

- **Significant capex plans and repayment obligations in FY2021** – The company has a capex plan of ~Rs. 700 crore ($100 million) in FY2021 years for its infrastructure development to support business expansion. Also, Syngene has aggregate repayment obligations of about Rs. 376.7 crore for FY2021. However, ICRA draws comfort from the anticipated healthy accruals from the business, which will fund the capex and repayments.

- **High customer and geographic concentration** – Syngene derived about 62% of its revenues in FY2019 from its top 10 customers and 76% of its revenues in FY2020 from USA. This exposes the company to revenue risks arising from loss of customers to competitors and region-specific challenges. However, Syngene's periodic addition of customers, stated intent to gradually diversify its customer base going forward and presence of customers globally across regions provides comfort to an extent.

- **Growing competition in the contract research space** – With the industry poised for healthy growth over the next few years, several global and domestic players are increasing presence in contract research. This is likely to increase competition and pricing pressure for Syngene going forward. However, the company's robust infrastructure/employee skillset, constant focus on compliance and safety, and Syngene's established client relationships are likely to mitigate competitive threats to a large extent.

- **Regulatory risks and vulnerability to unfavourable forex movement** – Akin to other industry players, the company is bound by strict regulations for clinical trials for regulated markets. Although any deviation in the same could result in reputational risks and other penalties for the company, historical absence of regulatory issues in clinical trials provides comfort to a large extent. Also, with about 96% of its revenues from overseas markets, the company's revenues and margins are susceptible to risks arising from adverse forex movements including appreciation of rupee against dollar. However, the hedging mechanisms adopted by the company mitigate the risk to an extent.

---

[2] Calculated as gross debt (including lease liabilities) minus cash and liquid investments

Liquidity position: Strong

Syngene's liquidity is strong with positive retained cashflows over the last five years, consolidated cash and bank balances and liquid investments of Rs. 1,019.9 crore (as on March 31, 2020) [3] and substantial working capital buffer. In relation to these sources of cash, Syngene has a total consolidated capex commitment of ~Rs. 700.0 crore (to be funded through internal accruals), and term loan repayments of Rs. 376.7 crore in FY2021. ICRA expects Syngene to be able to meet its commitments through internal sources of cash and yet be left with healthy cash/liquid investment surplus. Syngene is expected to maintain its net debt negative position over the medium term. Further, the company enjoys strong financial flexibility and lender/investor comfort, and this is expected to continue going forward as well.

Rating sensitivities

Positive triggers – ICRA could upgrade Syngene's ratings if the company achieves material improvement in its scale of operations and significant diversification of customer base, while maintaining its strong credit profile.

Negative triggers – Negative pressure on Syngene's ratings could arise if there is pressure on Syngene's revenues or weakening of profit margins or profitability on sustained basis; or weakening in the parent's (Biocon Limited) credit profile or Syngene's operational/financial linkages with the parent, Biocon.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Pharmaceutical Industry Impact of Parent or Group Support on an Issuer's Credit Rating
Parent/Group Support	Biocon Limited (rated [ICRA]AA+ (Stable)/[ICRA]A1+) holds 70.2% stake in Syngene. Syngene enjoys implicit financial and operational flexibility by virtue of its parentage
Consolidation / Standalone	Consolidation

About the company

Syngene International Limited (Syngene), a subsidiary of Biocon Limited, is a CRO providing integrated discovery and development services for novel molecules across multiple platforms, including small molecules, large molecules, antibody drug conjugates and oligonucleotides. The company's strengths include synthetic chemistry and molecular biology. Syngene offers outsourced services to over 360 global customers across biotechnology, nutrition, animal health, consumer goods and specialty chemicals including majors such as BMS, Amgen, Herbalife and Baxter, etc. Syngene has 1.9 million sq. ft. of R&D infrastructure and over 4,200 scientists currently. Syngene also incorporated a wholly-owned subsidiary, Syngene USA Inc., in the USA in FY2018 for providing marketing services to the company in the region.

[3] Only includes investments with maturity period less than a year

Key Financial Indicators (audited)

Consolidated	FY2019	FY2020
Operating Income (Rs. crore)	1,823.7	2,026.3
PAT (Rs. crore)	331.6	412.1
OPBDIT/ OI (%)	29.4%	30.5%
RoCE (%)	18.6%	21.3%
Total Outside Liabilities/ TNW (times)	0.8	0.9
Total Debt/ OPBDIT (times)	1.5	1.3
Interest coverage (times)	16.6	17.9
Debt Service Coverage Ratio (times)	3.4	2.3

Source: Company, ICRA research; OPBDITA: Operating Profit before Depreciation, Interest and Taxes; PAT: Profit After Tax; RoCE: Return on Capital Employed; TNW: Tangible Net Worth

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

<table>
<tr><th rowspan="2"></th><th rowspan="2">Instrument</th><th colspan="4">Current Rating (FY2021)</th><th colspan="3">Chronology of Rating History for the past 3 years</th></tr>
<tr><th>Type</th><th>Amount Rated (Rs. crore)</th><th>Amount Outstanding (Rs Crore)</th><th>Date & Rating
Aug 10, 2020</th><th>Date & Rating in FY2020
Sep 13, 2019</th><th>Date & Rating in FY2019
Jul 31, 2018</th><th>Date & Rating in FY2018
Apr 13, 2017</th></tr>
<tr><td>1</td><td>Term loans (ECB)</td><td rowspan="3">Long Term</td><td>375.00</td><td>375.00</td><td>[ICRA]AA+ (Stable)</td><td>[ICRA]AA (Positive)</td><td rowspan="2">[ICRA]AA (Positive)</td><td rowspan="2">[ICRA]AA (Stable)</td></tr>
<tr><td>2</td><td>Long-term unallocated</td><td>-</td><td></td><td>-</td><td>-</td></tr>
<tr><td>3</td><td>Long-term fund based</td><td>136.00</td><td></td><td>[ICRA]AA+ (Stable)</td><td>-</td><td>-</td><td>-</td></tr>
<tr><td>3</td><td>Long-term/short-term fund based</td><td rowspan="2">Long Term/ Short Term</td><td>-</td><td></td><td>-</td><td>-</td><td>[ICRA]AA (Positive)/ [ICRA]A1+</td><td>[ICRA]AA (Stable)/
[ICRA]A1+</td></tr>
<tr><td>4</td><td>Long-term/short-term unallocated</td><td>-</td><td></td><td>-</td><td>[ICRA]AA (Positive)/ [ICRA]A1+</td><td>-</td><td>-</td></tr>
<tr><td>5</td><td>Short-term fund based</td><td rowspan="3">Short Term</td><td>379.50</td><td></td><td rowspan="3">[ICRA]A1+</td><td rowspan="3">-</td><td rowspan="3">-</td><td rowspan="3">-</td></tr>
<tr><td>6</td><td>Short-term non-fund based</td><td>13.80</td><td></td></tr>
<tr><td>7</td><td>Short-term unallocated</td><td>55.70</td><td></td></tr>
</table>

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 loans (ECB)	FY2016	Libor + 1.3%	FY2021	375.00	[ICRA]AA+ (Stable)
NA	Long-term fund based - Overdraft	NA			56.00	
NA	Long-term fund based – Buyer's credit				80.00	
NA	Short-term fund based - PCFC				379.50	[ICRA]A1+
NA	Short-term non-fund based – LC/BG				13.80	
NA	Short-term unallocated				55.70	

Source: Syngene International Limited

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Syngene USA Inc	100%	Full consolidation
Syngene Employees Welfare Trust	100%	

Source: Syngene International Limited

ANALYST CONTACTS

Subrata Ray
+91 22 6114 3408
subrata@icraindia.com

Pavethra Ponniah
+91 44 4596 4314
pavethrap@icraindia.com

Vinutaa S
+91 44 4596 4305
vinutaa.s@icraindia.com

RELATIONSHIP CONTACT

Jayanta Chatterjee
+91 80 4332 6401
jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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

ICRA Limited

Corporate Office
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300
Email: info@icraindia.com
Website: www.icra.in

Registered Office
1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50

Branches

Mumbai	+ (91 22) 24331046/53/62/74/86/87
Chennai	+ (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,
Kolkata	+ (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,
Bangalore	+ (91 80) 2559 7401/4049
Ahmedabad	+ (91 79) 2658 4924/5049/2008
Hyderabad	+ (91 40) 2373 5061/7251
Pune	+ (91 20) 2556 0194/ 6606 9999