Farmson Pharmaceutical Gujarat Pvt. Ltd.

August 09, 2018

Summary of rated instruments

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Fund Based Facilities – CC/Others	10.00	[ICRA]A-(Stable); Assigned
Non-fund Based Facilities – BG/LC	15.00	[ICRA]A2+; Assigned
Total	**25.00**	

*Instrument details are provided in Annexure-1

Rating action

ICRA has assigned a long-term rating of [ICRA]A- (pronounced ICRA A minus) to the Rs. 10.00-crore[1] fund based facilities of Farmson Pharmaceutical Gujarat Pvt. Ltd. (FPGPL or the Company). The outlook on the long-term rating is 'Stable'. ICRA has also assigned a short-term rating of [ICRA]A2+ (pronounced ICRA A two plus) to the Rs. 15.00-crore non-fund based facilities of FPGPL[2].

Rationale

The assigned ratings favourably factor in the extensive experience of FPGPL's promoters spanning over four decades in the paracetamol industry, its leading position as one of the largest paracetamol producers globally and its geographically diversified sales with growing contribution of exports. The ratings also take into consideration the competitive advantage that the Company has in terms of backward integration of its operations for its key raw material viz. para aminophenol (PAP) through its group company JNP Products leading to cost advantage. The ratings are also supported by the reputed and diversified client portfolio consisting mainly of pharmaceutical majors like Sanofi, GlaxoSmithKline Pharmaceuticals, Proctor & Gamble, Ipca Laboratories, etc. ICRA notes that while FPGPL is in the midst of a large debt funded capex plan to enhance its capacities, the healthy improvement in internal accruals and availability of adequate working capital facilities continue to support the financial risk profile of the Company.

However, the ratings are constrained by the Company's heavy reliance on a single API product – paracetamol, which is partially mitigated by the historically widespread use of the product as a mainstay analgesic and antipyretic. The ratings are further constrained by the vulnerability of the Company's profitability to fluctuations in input prices of raw materials such as acetic anhydride and para-nitro chloro benzene (PNCB) as well as the possibility of non-renewal of the existing anti-dumping duty (valid till October 2018) on Chinese paracetamol which could lead to increased competition and affect the Company's profitability.

[1] *100 lakh = 1 crore = 10 million*

[2] *For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications*

Outlook: Stable

ICRA believes FPGPL will continue to benefit from its long standing customer relationships, its large production capacities coupled with favourable demand prospects and improving realisations for paracetamol in the export market. The outlook may be revised to 'Positive' if substantial growth in revenue and profitability strengthens the financial risk profile. The outlook may be revised to 'Negative' if earnings are lower than estimates on the back of weak volumes due to non-renewal of anti-dumping duties or if capital expenditure is more than estimated, impacting FPGPL's leverage indicators and liquidity position.

Key rating drivers

Credit strengths

Long experience of promoters in the paracetamol industry - The promoters' long track record of more than four decades, coupled with the presence of experienced professionals, has ensured FPGPL's strong brand position in the Paracetamol industry. Over the years, the Company has gradually increased its production capacity for Paracetamol. The total production capacity of all domestic players combined is about 70,000 MT per annum, of which FPGPL accounts for about 35% production capacity (considering the additional 4,800 MT capacity to be added in H1 FY2019).

Steady increase in geographical diversification with growing contribution of exports - FPGPL is primarily a domestic player with about 75% of its revenues being derived from the domestic market during FY2018. However, the Company has increased its focus on the export markets over the last few years. The company is European Directorate for the Quality of Medicines (EDQM) and European Union good manufacturing practice (EU GMP) certified and is therefore eligible to sell to any of the 28 EU countries. Also, it is World Health Organisation good manufacturing practice (WHO GMP) certified giving it access to the African market. Additionally, FPGPL also has relevant certifications for selling to Russia.

Established relationships with pharmaceutical majors - FPGPL has long standing relationships with several pharmaceutical majors such as Sanofi, GSK Pharmaceuticals, Ipca Laboratories, etc.; the Company has been supplying Paracetamol to Sanofi for over two decades. Additionally, FPGPL constantly strives to increase its customer base and has successfully tied-up with companies like Emzor Pharmaceuticals and May & Baker (Nigeria) over the past couple of years.

Backward integrated into production of PAP with JNP Products supplying the entire requirement - FPGPL has a significant competitive advantage as compared to the other paracetamol producers in India given that it has the capability to produce PAP in-house through its group firm JNP Products. Production of PAP is one of the barriers/bottlenecks for the paracetamol industry and most other Paracetamol producers source the PAP from China, resulting in increased raw material cost.

Significant revenue growth in FY2018; favourable growth prospects given capacity expansion plans - FPGPL's operating income stood at Rs. 481.2 crore in FY2018 which is a 34.1% increment over the previous year's operating income. The Company's revenue has clocked a healthy CAGR of 23% since FY2013 (despite the de-growth in FY2017) on the back of rising production given the increased demand as well as by improved efficiencies and achievement of economies of scale. FPGPL, in FY2018, has undertaken capital expenditure to increase its paracetamol production capacity which will aid its growth going forward.

Credit challenges

Heavy reliance on single product segment - FPGPL is essentially a single-product company focused on production and sales of Paracetamol in the domestic and export market. Though there are other APIs that have bioequivalence to

Paracetamol, Paracetamol has been the mainstay analgesic and antipyretic since its commercial availability due to its low cost and consistent safety profile, thus mitigating the API obsolescence risk.

Profitability vulnerable to volatility in raw material prices - Price of PNCB is linked to the crude oil prices and any variation in the crude oil prices will influence the raw material cost of JNP Products. Additionally, the price of acetic anhydride has become volatile due to global demand-supply mismatch. The company does not have any pricing contracts with the suppliers; however, any adverse price movement is transferred to the customers through a price variation clause in the annual contract.

Increased competition due to non-renewal of the anti-dumping duty on Chinese Paracetamol in Indian market - FPGPL currently holds a good market share in the domestic market which is facilitated by the anti-dumping duty of $0.79 per kg imposed on Chinese paracetamol. The validity of the existing anti-dumping duty is till October 2018 and non-renewal of the same could have an adverse effect on the company's revenues as well as profitability given the increased competition.

Moderate execution and market risk associated with the new debt funded capacity additions - FPGPL is in the midst of debt-funded expansion of its paracetamol production capacity at one of its manufacturing units; the new capacity is expected to be operational from H2 FY2019. While funding for the projects has been tied-up, the company will be exposed to moderate execution and market risks associated with the capacity expansion.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below**.**

Links to applicable criteria:

Corporate Credit Rating Methodology
Rating Methodology for Entities in the Pharmaceutical Industry

About the company:

FPGPL was founded more than four decades ago by late Mr. K. K. Vithani and is part of the Farmson group. The Company is in the business of manufacturing of bulk drug Paracetamol (also known as Acetaminophen or APAP) which is an API used as analgesic (pain reliever) and antipyretic (fever reducer). Besides the flagship company, Farmson Group owns and operates JNP Products, which manufactures the intermediate PAP which is the major raw material for the production of paracetamol and sells it entirely to FPGPL.

FPGPL has two manufacturing facilities for API Paracetamol at Nandesari, Gujarat having a total installed production capacity of 24,000 MT per year (including the 4,800 MT annual capacity to be added in H1 FY2019). Additionally, JNP Products has a unit at Jhagadia, Gujarat for production of PAP having a total installed capacity of 19,200 MT per year, which is sufficient to meet the PAP requirement of FPGPL. FPGPL supplies paracetamol to several leading pharmaceutical companies in India as well as 29 other countries in Europe, Africa and Asia.

In FY2018, on a provisional basis, the company reported a net profit of Rs. 23.9 crore on an operating income of Rs. 481.2 crore, as compared to a net profit of Rs. 16.1 crore on an operating income of Rs. 358.9 crore in the previous year.

Key financial indicators (provisional)

	FY2017	FY2018
Operating Income (Rs. crore)	358.9	481.2
PAT (Rs. crore)	16.1	23.9
OPBDIT/OI (%)	9.9%	10.6%
RoCE (%)	28.3%	34.1%
Total Debt/TNW (times)	0.2	0.6
Total Debt/OPBDIT (times)	0.5	1.2
Interest coverage (times)	12.6	11.3

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

		Current Rating (FY2019)				Chronology of Rating History for the Past 3 Years		
					Date & Rating	Date & Rating in FY2018	Date & Rating in FY2017	Date & Rating in FY2016
	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	August 2018	-	-	-
1	Fund Based Facilities – CC/Others	Long Term	10.00	-	[ICRA]A- (Stable)	-	-	-
2	Non Fund Based Facilities – BG/LC	Short Term	15.00	-	[ICRA]A2+	-	-	-

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 Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund Based Facilities – CC/Others	NA	NA	NA	10.00	[ICRA]A- (Stable)
NA	Non-Fund Based Facilities – BG/LC	NA	NA	NA	15.00	[ICRA]A2+

Source: Farmson Pharmaceutical Gujarat Pvt. Ltd.

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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.

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