Smruthi Organics Limited

March 13, 2023

Facilities	Amount (₹ crore)	Ratings[1]	Rating Action
Long Term Bank Facilities	15.00	CARE BBB; Stable	Reaffirmed
Short Term Bank Facilities	13.00	CARE A3+	Reaffirmed

Details of facilities in Annexure-1.

Rationale and key rating drivers

The reaffirmation of the ratings assigned to the bank facilities of Smruthi Organics Limited (SOL) continue to derive comfort from extensive experience of promoters in the pharmaceutical industry, accredited manufacturing facilities, and comfortable financial risk profile. These rating strengths, however, remain tempered by, modest scale of operations, product and customer concentration risk, competitive nature of business, and exposure to regulatory and foreign exchange fluctuation risk. This apart, SOL also remains exposed to volatile raw material prices and thus, it has witnessed significant moderation in the operating margins in the current fiscal (refers to period from April-22 to March-23). Furthermore, the company has planned to undertake capex to upgrade and expand existing facilities which coupled with weakening of margins, is likely to deteriorate the debt protection metrics (Total debt/Gross Cash Accruals and Total debt/PBILDT) in near term. Nevertheless, the metrics are expected to remain at comfortable level, given low leverage profile of the company and shall revive to existing levels in medium term.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Increase in TOI to more than Rs.300 crore along with operation margin of 18% and above on sustained basis
- Ability of the company to reduce the therapeutic concentration risk with no segment contributing more than 30% along with diversifying its customer base.
- Ability of the company to diversify geographically with significant level of revenues from regulated markets.

Negative factors

- Deterioration in the overall gearing beyond 1x on sustained basis.
- TOI falling below Rs. 100 crore and PBILDT margin falling below 10% on a sustained basis.

Analytical approach: Standalone

Outlook: Stable.
Stable outlook reflects the company's ability to maintain its comfortable financial risk profile while sustaining its existing operational performance over medium term.

Key strengths

Comfortable Financial risk Profile: As on March 31, 2022, the overall gearing of the company stood comfortable at 0.05 times. Owing to healthy profitability in past two years ended FY22 (refers to the period from April 01 to March 31), the company was able to pare down its working capital limits and pay off term debt resulting in improvement in overall gearing from the level of 0.50x as on March 31, 2020. Going ahead, the company has planned to avail term debt owing to its expansion plans and accordingly, gearing is expected to deteriorate, however will continue to remain at comfortable level below 0.60 times. Healthy profitability coupled with reduction is overall debt has also resulted in improved debt coverage indicators. Total debt/ PBILDT and total debt/ GCA stood comfortable at 0.15x and 0.20x for FY22 as against 0.36x and 0.41x for FY21 respectively. However, due to moderate profitability and additional debt drawdown, the debt coverage indicators are likely to weaken in near term.

Experienced promoters in the bulk drug manufacturing Industry: SOL is managed/promoted by Mr. Purushotham Ega and Mr. Ega Swapnil, having more than 30 years and 15 years respectively in pharmaceutical industry. SOL's operating track record is of more than three decades in the pharmaceutical business with presence in the area of manufacturing of bulk drugs and APIs.

Accredited manufacturing units: The company has two manufacturing units located at Solapur in Maharashtra. The facilities are spread over an area of 22 acres with total annual capacity of around 5,800 MT, thus capable of handling large volumes. The plant is Good Manufacturing Practice (GMP) certified. The company's research and development department is recognized by the Directorate of Scientific and Industrial Research (DSIR), Government of India.

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

Key weaknesses

Susceptibility of operating margins to volatile raw material prices and foreign exchange rate: The major raw materials required for the company are Dicyandiamide (DCDA) and Dimethylacetamide, prices of which are volatile in nature. Since, raw material (contributed around 69% of cost of sales in FY22) is the major cost driver for the company, any upward movement in raw material prices, with limited increase in prices of finished products in an intensely competitive industry may result in adverse performance of the company. Further, SOL imports majority of raw material from China and exports its products to several countries like Pakistan, Thailand, Argentina etc. In the absence of a hedging mechanism, although being a net exporter, the company is exposed to foreign currency fluctuation risk owing to timing differences.

Moderation in profitability margins: The operating margin of the company declined from 23% in FY21 to 14% in FY22, owing to significant increase in raw material prices mainly led by global supply chain disruption. Such increase in cost could not be passed on fully and thus, company had to absorb some of the costs. This apart, due to set up of formulation division and hiring of employees at senior level in operations and R&D division, the employee cost of the company also increased, which has also led to dip in profitability margins. The PAT margin of the company witnessed similar decline of 900 bps. In 9MFY23 as well, owing to continuous increase in raw material cost and high employee cost, the operating margin moderated to 9%. The profitability of the company is likely to remain under pressure in near term and shall remain key rating monitorable.

Product and customer concentration Risk: SOL is primarily an API manufacturer, with APIs representing more than 80% of revenue contribution and remaining is accounted by intermediates. The product portfolio of the company is skewed as top 5 products derived close to 95% of the revenue in 9MFY23 as against 92% in FY22. While, the share of top two products stood at over 55% of the revenue in FY21 and 9MFY22 each, reflecting high dependence on sales from top two products i.e. Metformin and Telmisartan.
This apart, the customer concentration of the company continues to remain high with top 10 customer contributed close to 69% and 50% of total sales in FY22 and 9MFY23.

Exposure to regulatory risk: The pharmaceutical industry is highly regulated and requires various approvals, licenses, registrations and permissions for business activities. Each authority has its own requirement and they could delay or refuse to grant approval, even when a product has already been approved in another country. The approval process for a new product registration is complex, lengthy and expensive. Any delay or failure in getting approval for new product launch could adversely affect the business prospect of the company. This apart, the ability of the company to continue to observe the regulatory and CGMP standards without receiving any adverse observations from regulatory authorities remains critical from business and credit risk perspective. Furthermore, the company has substantial level of imports from China and exports to Pakistan, any geopolitical issues with such countries could materially impact the operations of the company.

Liquidity: Adequate
The company has a comfortable liquidity position characterized by expected cash accruals of around Rs.10 crore against negligible repayment obligations. With a gearing of 0.04 times as of March 31, 2022 and close to 0.10 times as on December 31, 2022, the issuer has sufficient gearing headroom, to raise additional debt. The liquidity of the company is further supported by unutilized bank lines as the average working capital limit utilization remained low at 29% in the last 12 months ended September 2022. Further, the current & quick ratio stood comfortable at 3.42 times and 2.12 times respectively as on March 31, 2022.

Environment, social and governance (ESG) risks: Not applicable

Applicable criteria

Short Term Instruments
Rating Outlook and Credit Watch
Policy on Withdrawal of Ratings
Policy on default recognition
Pharmaceutical
Manufacturing Companies
Liquidity Analysis of Non-financial sector entities
Financial Ratios – Non-financial Sector

About the company and industry

Industry Classification

Macro Economic Indicator	Sector	Industry	Basic Industry
Healthcare	Healthcare	Pharmaceuticals & Biotechnology	Pharmaceuticals

SOL established in 1989 by Mr. Ega Purushotham (Managing Director) and is headquartered at Solapur, Maharashtra. Mr Eaga Purushotham along with Mr Eaga Swapnil (son of Mr. Eaga Purushotham) manages the overall operations of the company. The company is engaged in the business of manufacturing and marketing active pharmaceutical ingredients (APIs) and intermediates. The product portfolio of the company consists of various APIs and intermediates including Metformin, Diloxanide Furoate, Norfloxacin, Telmisartan, Amlodipine, Potassium Losartan amongst others.

Brief Financials (₹ crore)	March 31, 2021 (A)	March 31, 2022 (A)	9MFY23 (UA)
Total operating income	126.57	133.37	104.31
PBILDT	28.60	18.43	.48
PAT	18.03	10.10	3.36
Overall gearing (times)	0.22	0.05	0.10
Interest coverage (times)	26.16	18.74	13.12

A: Audited; UA: Unaudited; Note: 'the above results are latest financial results available'

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for the last three years: Please refer Annexure-2

Covenants of the rated instruments/facilities: Detailed explanation of the covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of the various instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT-Cash Credit		-	-	-	15.00	CARE BBB; Stable
Non-fund-based - ST-BG/LC		-	-	-	13.00	CARE A3+

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1	Fund-based - LT-Term Loan	LT	-	-	-	-	-	1)Withdrawn (28-Jun-19)
2	Fund-based - LT-Cash Credit	LT	15.00	CARE BBB; Stable	-	1)CARE BBB; Stable (05-Jan-22) 2)CARE BB+; Stable; ISSUER NOT	1)CARE BB+; Stable; ISSUER NOT COOPERATING* (14-Sep-20)	1)CARE BB+; Positive (28-Jun-19)

						COOPERATING * (13-Aug-21)		
3	Non-fund-based - ST-BG/LC	ST	13.00	CARE A3+	-	1)CARE A3+ (05-Jan-22) 2)CARE A4+; ISSUER NOT COOPERATING * (13-Aug-21)	1)CARE A4+; ISSUER NOT COOPERATING * (14-Sep-20)	1)CARE A4+ (28-Jun-19)

Annexure-3: Detailed explanation of the covenants of the rated facilities: Not applicable

Annexure-4: Complexity level of the various instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Fund-based - LT-Cash Credit	Simple
2	Non-fund-based - ST-BG/LC	Simple

Annexure-5: Lender details

To view the lender wise details of bank facilities please click here

Note on the complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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