Cohance Lifesciences Limited

November 1, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long Term Bank Facilities	112.37	CARE AA-; Stable	Assigned
Long Term / Short Term Bank Facilities	296.80	CARE AA-; Stable / CARE A1+	Assigned

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

The ratings assigned to the bank facilities of Cohance lifesciences limited ("CLL") at the combined level (i.e. CLL, ZCL Chemical Limited (ZCL) and Avra Laboratories private limited (Avra), derives strength from the diversified business operations with presence across major pharmaceutical markets in India and abroad, accredited manufacturing facility, diversified product profile and reputed clientele base. The stable scale of operations with healthy margins, comfortable liquidity position and strong credit risk profile also strengthens the rating.

In addition to the above, the existence of strong parent Advent International Corporation (AIC), a global private equity investor and experienced management also augurs well for the company. Advent international acquired 100% stake in RA Chem pharma limited (RACPL), ZCL in August 2022 and ~100% stake in Avra September 2022. Further, in November 2022, Advent has merged RACPL with its holding company Al Pharmed Consultancy India private limited (APC) and subsequently renamed the company as Cohance lifesciences limited. The holding company, APC has issued compulsorily convertible debentures amounting to ~₹1000 crores for the acquisition, given that they are compulsorily convertible within 8 years, CARE Ratings has considered the same as part of equity. AIC's global network is expected to benefit the three companies and enable them to deepen its market penetration in regulated markets going forward.

Advent has acquired a controlling stake in all three companies and plan to combine them into CLL by March 2024.

CLL has established track record of more than two decade and has presence in the major regulated pharmaceutical markets with majority of revenues derived from exports (79% during FY23 against 75% during FY22). CLL has a presence across 42 therapeutic segments and majorly caters to niche therapeutic segments viz. Anti-spasmodic, Anti-Depressant; besides Muscle relaxants, Anti-epileptic and Anti-Parkinson. The top 5 therapeutic segments contribute to 57% of the revenue during FY23 as against 60% during FY22. The manufacturing facilities of CLL have approvals from USFDA, Korean Food and Drug Administration (FDA), World Health Organization Good Manufacturing Practices (WHO CGMP), European Directorate Quality of Medicines (EDQM) and Japan Pharmaceutical and Medical Devices Agency (PMDA).

Advent has also acquired 50.1% stake in Suven Pharmaceuticals Limited and has plans to acquire further 26% stake through an open offer. CARE Ratings will continue to monitor any major updates regarding the acquisition.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Improvement in the total operating income (TOI) by 15% on continuous basis.
- Improvement in the profit before interest, lease rentals, depreciation and taxation (PBILDT) margins on a sustained basis over 30%

Negative factors

- Elongation of working capital cycle beyond 200 days
- Overall gearing going beyond 1.00x on sustained basis
- Dividend or any other form of outflow of cash to the holding companies exceeding 1x of the net profits for the year.
- Any major debt funded capex, increasing the Total debt/PBILDT more than 1.5x, leading to weakening of credit risk profile of company at combined level.

Analytical approach: Combined

CARE Ratings has done a combined assessment of CLL, factoring the other two entities i.e. ZCL and Avra due to the following reasons:

- Advent International, through its wholly owned subsidiaries, hold entire stake in these companies
- There exists common promoters-cum-management across these three companies, have centralised treasury functions to manage its investments, debt finance, and forex requirements.
- These three entities are expected to get merged into one single entity going forward
- All of them are into manufacturing APIs and majorly into exports.
- Synergies have been created across functions including sales & business development, operations, supply chain and support functions.

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

Hence considering above factors Care Ratings has carried out the credit risk assessment by combining the said three entities i.e. CLL, ZCL and Avra.

Outlook: Stable

The stable outlook reflects CARE Ratings' expectation that the combined entity will continue to derive strength from its diversified business operations with presence across major pharmaceutical markets, strong parentage and comfortable credit risk profile in the near future.

Detailed description of the key rating drivers:

Key strengths

Diversified business operations with presence across major pharmaceutical markets

On a combined basis, the domestic sales of the three companies are only around 19% in FY23. Majority of the sales i.e. 81% is derived from exports. These companies on a combined level derived over 50% of its TOI from regulated market with Europe contributing about 30% and US contributing about 27%. Furthermore, in terms of the therapeutic segment wise the company derives about 47% of its total operating income from therapies such as gastrointestinal (21%), anti-spasmodic (13%), anti-depressant (9%), muscle relaxant (7%), and anti-parkinson's (6%). The diversification in business operations expected to continue going forward.

Accredited manufacturing facilities:

CLL has two formulation units, 2 API units, one clinical research unit and two R&D facilities. The manufacturing facilities of CLL have approvals from USFDA, Korean Food and Drug Administration (FDA), World Health Organization Good Manufacturing Practices (WHO CGMP), European Directorate Quality of Medicines (EDQM) and Japan Pharmaceutical and Medical Devices Agency (PMDA). ZCL has an API and R&D facility at Ankleshwar, Gujarat and these facilities are successfully inspected and audited by regulatory authorities such as US FDA, EDQM, KFDA, WHO-GMP & COFEPRIS and Japanese MOH. Avra has two API and two R&D facilities and its manufacturing facilities are located in Hyderabad (USFDA and WHO-GMP approved) and Vizag. These facilities are duly approved by various regulatory authorities.

Diversified product profile and reputed clientele base:

The company at combined level has over 100 products and revenue derived from top 10 products contribute about 47% of TOI. Further, there are 28 DMFs (Drug master files) and 17 ANDAs (Abbreviated New Drug Application) pending for approval. CARE Ratings expects that this would benefit these companies to expand further into regulated markets.

Stable Total Operating Income (TOI) with healthy profitability margins:

The total operating income witnessed a growth of about 5.4% during FY23 from ₹1,289 crore during FY22 to ₹1,359 crore during FY23. The growth is driven by increase in sales volumes of existing products in new markets.

The growth in total operating income was majorly driven by growth in Finished Dosage Forms (FDF) segment. The API segment saw slight moderation, while the FDF segment grew by 29% during FY23.

Strong credit risk profile, despite recent moderation:

During FY23, the company (at combined level) was able to reduce the long-term debt from ₹77.34 crores to ₹59.36 crores by way of scheduled repayments. Contrastingly, the short-term debt has increased from ₹118 crores as on March 31, 2022 to ₹229 crores as on March 31, 2023 to fund working capital requirements. The two companies – ZCL and Avra had paid dividend of around ₹373 crores and ₹81 crores respectively in FY23. This has resulted in a fall in cash and liquid assets balance at combined level from ₹389 to ₹97 crores as on March 31, 2023 and moderation in net worth. Owing to increase in total debt and slight moderation in networth, the overall gearing of the company has increased from 0.15x as on March 31, 2022 to 0.26x as on March 31, 2023. Total debt/GCA deteriorated to 1.12 times during FY23 vis-à vis 0.73 times during FY22 due to the same reason. The debt-to-equity ratio has however improved slightly from 0.06x to 0.05x on lower long-term debt. The interest coverage ratio has deteriorated from 25.24x in FY22 to 5.97x in FY23 due to increase in interest costs by ₹50 crores on account of payment of interest on CCDs (~₹1000 crores) issued by the erstwhile holding company of RA Chem (now merged and renamed as Cohance). CARE Ratings understands that the cash outflow towards CCD interest payout will be made only after meeting all the operational requirements and financial debt obligations for the fiscal, which lend comfort. The company continues to maintain higher inventory levels (₹364 crores in FY23 vs ₹327 crores in FY22) mainly towards orders which materialized in H1FY24.

Strong parentage and experienced management:
The company is owned and managed by Advent International which is one of the globally reputed and leading PE firms. Dr. V. Prasada Raju is the Managing Director and Chief Executive Officer of the company. In addition to having a PhD in chemistry and PG Dip in patents law, he is also an alumina of the IIMc under Sr Management programme and IIT, Chicago, USA, where he was trained in material sciences. He has 28+ years of techno-commercial experience in the pharmaceutical space across the value chain. Dr Prasada Raju served in various leadership roles at Granules India Limited and Dr. Reddy's Laboratories. Additionally, AIC is represented on the board of CLL and ZCL by Pankaj Patwari and Shweta Jalan.

Key weaknesses
Working capital intensive nature of operations:
The working capital cycle still remains elongated and stood at 166 days during FY23 (FY22: 148 days) on account of increased inventory days. The average Inventory days increased from 114 days during FY22 to 131 days during FY23. The high closing inventory is on account of orders which materialized in H1FY2024. Furthermore, the company has to maintain semi-finished goods and finished goods inventory to meet expected demand as part of its growing business, resulting in stretched working capital cycle for the company.

Forex risk on account of exports:
CLL at combined level is exposed to forex risk as major revenue (81% of the revenue) of the company is derived from exports. The company imports around 10-15% of its raw material consumption which provides natural hedge to some extent of the total foreign exchange earnings. The company manages currency fluctuations by having a better geographic balance in revenue mix and ensures a foreign currency match between liabilities and earnings. According to the company's management, it continually assesses the currency volatility impact on the cost structure and engages with customers to address such risks. Also, the company enters into hedging transactions as and when it is required. During FY23, the company booked a net forex gain of ₹14.7 crore.

Exposure to regulatory risk:
The company is exposed to regulatory risk with its operations centered mainly into manufacturing pharmaceutical formulations and APIs. Besides, the pharmaceutical industry is highly regulated in many other countries and requires various approvals, licenses, registrations and permissions for business activities. The approval process for a new product registration is complex, lengthy and expensive. The time taken to obtain approval varies by country but generally takes from six months to several years from the date of application. Any delay or failure in getting approval for new product launch could adversely affect the business prospect of the company. Given, India's significant share in the USA's generic market, the USFDA has increased its scrutiny of manufacturing facilities and other regulatory compliance of the Indian pharma companies supplying generics drugs to the USA. Non-compliance may result in regulatory ban on products/facilities (as in the recent cases of import alerts issued by the USFDA to top pharma companies) and may impact a company's future approvals from USFDA. Hence, the ongoing regulatory compliance has become critical for Indian pharma companies including CLL, ZCL and Avra as they seek to strengthen its position in the regulated markets like USA, UK etc.
Given that the manufacturing facilities are approved by USFDA and other regulatory authorities and as of September 2023 these companies have successfully cleared all the audits carried out by various regulatory authorities without any observations, this risk is mitigated to an extent.

Liquidity: Strong
The liquidity profile of the company at combined level is strong. It has been generating healthy cash accruals vis-à-vis repayment obligations. The average utilisation of working capital limits remained moderate at about 65% for the last 12 months ended June 30, 2023. The two companies – ZCL and Avra had paid dividend of around ₹373 crores and ₹81 crores respectively in FY23. This has resulted in a fall in aggregate cash and liquid assets balance from ₹389 to ₹97 crores as on March 31, 2023 sand moderation in net worth. Further the company plans to pay dividend together with CCD interest of ₹130 and ₹65 crores in the next 1 or 2 years. The net cash flow from operations with improved scale of operations is expected to remain about ₹300 crore going forward which is more than adequate to meet its incremental working capital needs in the immediate future. The interest coverage ratio has deteriorated from 25.24x in FY22 to 5.97x in FY23 due to increase in interest costs by ₹50 crores on account of payment of interest on CCDs (~₹1030 crores) issued by the erstwhile holding company of RA Chem (now merged and renamed as Cohance). CARE understands that the cash outflow towards CCD interest payout will be made only after meeting all the operational requirements and financial debt obligations, which lend comfort. Considering the trend of GCA levels generated along with presence of unutilised credit lines, the company is in a comfortable liquidity position to meet its debt obligations which is about ₹20 crores during FY24 and FY25. For FY24 & FY25, on a combined level, there are numerous capex (such as new capacity creation at its API-2 facility, FDF l facilities etc) aggregating to ₹300 crores. Out of the total Capex, the management plans to fund around ₹100-150 crores through external debt and the remaining through internal accruals

Assumptions/Covenants – Not applicable

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

Applicable criteria

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

About the company and industry
Industry classification

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

Cohance lifesciences limited (CLL) was incorporated on 6 July 2020. Advent international, one of the world's established PE firm, through its step-down subsidiary AI pharmed consultancy India private limited (APC) acquired ~100% stake in RA Chem Pharma limited (RACPL) in Aug 2022. Post this, in November 2022, RACPL amalgamated with APC and the merged entity's name was changed to "Cohance lifesciences limited".

RACPL, was initially incorporated in January 1996. It is engaged in the manufacturing of active pharmaceutical ingredients (APIs), formulations, and clinical research activity at its four manufacturing facilities located at Jaggaiahpeta, Mukuteswarapuram, Krishna District (Andhra Pradesh), Achyutapuram Industrial Area, Andhra Pradesh, and Nacharam, Jadcherla, Hyderabad, Telangana, and clinical research activity at Balanagar, Hyderabad, Telangana.

About ZCL:
ZCL Chemicals Limited (formerly Zandu Chemicals Ltd) is an Indian pharmaceutical company established in 1991. The facilities are successfully inspected and audited USFDA, EDQM, KFDA, WHO GMP, and COFEPRIS, Japanese MOH with a capacity of 227,000 litres (60,000 gallons) along with strong R&D capabilities. In August 2022, Advent International (Advent), a global private equity investor, acquired a 100% stake in ZCL (through its wholly-owned step-down subsidiary – Jusmiral Holdings Limited).

About Avra:
Established in the year 1995, Avra is among the first in India to focus on providing high-end contract research and manufacturing of advanced intermediates and APIs covering oncology and other therapeutic areas. Avra was founded by AV Rama Rao, who is a highly experienced scientist by profession. It has several active process patents and is the only company in the world to develop and successfully commercialise a synthetic process for irinotecan (currently being used in antibody drug conjugates for targeted therapies in treating cancer). In September 2022, Advent International (Advent), a global PE investor, acquired 99.98% stake in Avra (through wholly owned step-down subsidiary – Jusmiral Holdings Limited.

The following table depicts the financial parameters at the combined level:

Brief Financials (₹ crore)	March 31, 2021 (C#)	March 31, 2022 (C#)	March 31, 2023 (C#)
Total operating income	1059.49	1309.33	1358.78
PBILDT	287.82	356.42	380.61
PAT	175.72	219.38	198.84
Overall gearing (times)	0.14	0.15	0.26
Interest coverage (times)	25.20	25.24	5.97

#The combined audited financials of the three companies for the years FY21 and FY22 are presented considering that these 3 entities (RA Chem, ZCL and Avra). From FY23, figures includes the financials of APC, RA Chem, ZCL and Avra. In FY23 RA Chem merged with its holding company

Al Pharmed (APC) and FY23 includes the combined financials of 4 companies - AI Pharmed, ZCL, RA Chem and Avra. APC did not have any business on its own and was merely an investment holding company
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 last three years: Please refer Annexure-2

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

Complexity level of various instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT/ ST-Working Capital Limits		-	-	-	296.80	CARE AA-; Stable / CARE A1+
Term Loan-Long Term		-	-	30-05-2028	112.37	CARE AA-; Stable

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 2023-2024	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
1	Fund-based - LT/ ST-Working Capital Limits	LT/ST*	296.80	CARE AA-; Stable / CARE A1+				
2	Term Loan-Long Term	LT	112.37	CARE AA-; Stable				

*Long term/Short term.

Annexure-3: Detailed explanation of covenants of the rated instruments/facilities: not applicable

Annexure-4: Complexity level of the various instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Fund-based - LT/ ST-Working Capital Limits	Simple
2	Term Loan-Long Term	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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About us:

Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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