Fleming Laboratories Limited

September 25, 2024

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	2.37 (Reduced from 4.68)	CARE BBB; Stable	Downgraded from CARE BBB+; Stable
Long-term / Short-term bank facilities	37.40 (Enhanced from 32.40)	CARE BBB; Stable / CARE A3+	Downgraded from CARE BBB+; Stable / CARE A2
Short-term bank facilities	4.10 (Reduced from 7.60)	CARE A3+	Downgraded from CARE A2

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

Revision in ratings assigned to bank facilities of Fleming Laboratories Limited (FLL) is considering significant decline in revenue from operations in FY24 (FY refers to April 01 to March 31), primarily caused by the loss of orders from a major client for the muscle relaxant segment. This and higher fixed overheads, resulted in a significant decline in operating profitability. However, ratings continue to derive strength from established track record of business, accredited manufacturing facilities, established customer base and diversified geographical reach, comfortable financial risk profile and established position in the niche product segment.

Ratings also factor in investment of ₹25 crore by InvAscent, a private equity firm through Compulsory Convertible Preference Shares (CCPS) through its fund, India Lifesciences Fund IV. Funds raised by FLL were invested as equity and unsecured loans to its subsidiary, Fleming Life Sciences Private Limited (FLSPL), for the establishment of a production unit in Kadechur, Karnataka, recently completed United States Food and Drug Administration (USFDA) inspection for its Unit II in Hyderabad.

Ratings strengths are partially offset by regulated business and project implementation risk related to ongoing debt-funded capital expenditure in Fermac Bio Private Limited (Fermac), a joint venture floated by FLL and Barsun Labs LLP (BLL), where FLL, and BLL extended a corporate guarantee for the debt availed by Fermac.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Improving total operating income (TOI) to over ₹200 crore while maintaining profit before interest, lease rentals, depreciation, and taxation (PBILDT) margins above 24% on a sustained basis.
- Reducing operating cycle below 150 days on a sustained basis.

Negative factors

- Un-envisaged incremental borrowings, deteriorating its overall gearing over 0.75x on a sustained basis.
- Declining TOI by over 30% and PBILDT margin falling below 15%.

Analytical approach: Standalone

Outlook: Stable

CARE Ratings Limited (CARE Ratings) believes that FLL will continue to benefit from the experience of promoters and established relationships with customers.

Detailed description of key rating drivers:

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

Key strengths

Established track record of operations

FLL has a track record spanning over two decades in the pharmaceutical industry. It is currently led by M Jeyamuruga Prakash, who holds a post-graduate degree in Chemistry and Chemical Engineering from BITS Pilani and MBA from Great Lakes Institute of Management. He possesses extensive experience in API industry and has a background in industrial and marketing roles, with a focus on pharmaceutical sector. Prior to joining FLL, he served as vice president for international business and marketing at Shasun Pharmaceuticals Limited. The company also benefits from the management's well-established relationships in the market with suppliers and customers.

Accredited manufacturing facilities

To compete with international and domestic contenders, the company invested in strengthening its business operations. This includes getting its facilities audited and approved by regulatory agencies like EUGMP, EDQM, WHO GMP, PMDA (Japan), COFEPRIS (Mexico), and Korea FDA. The company operates two active pharmaceutical ingredients (API) manufacturing facilities supported by a qualified team to ensure international standards. Furthermore, its R&D centre is recognised by Government of India under Department of Scientific and Industrial Research (DSIR). Further, USFDA Suo moto initiated an inspection from September 16, 2024, to September 20, 2024, for Unit II, Jeedimetla, Hyderabad. This is considering the increase in demand for D-Penicillamine (used for treatment of Wilson’s Disease) in the USA. Following USFDA clearance for products (produced at Unit II), export revenue is expected to rise given FLL will be able to export to the USA.

Established customer base and diversified geographical reach

The company has established relationships with its pharmaceutical clients, spanning over a decade and extending across the globe. FLL has expanded its geographical presence to encompass over 70 countries, including South American countries, Middle Eastern countries, Asia, Europe, and Russia, among others.

Comfortable financial risk profile

The company’s financial risk profile remains comfortable, although it deteriorated in FY24 compared to FY23 due to increased reliance on bank borrowings for working capital. As on March 31, 2024, working capital borrowings outstanding increased to ₹27.10 crore (PYE: ₹3.31 crore). Incremental working capital requirement was primarily to meet the fixed overhead expenses given cash generation being on a lower side resulting in a deterioration in overall gearing from 0.09x as on March 31, 2023, to 0.43x as on March 31, 2024.

Stable industry outlook

Indian Pharmaceutical Industry, including domestic and export segments, achieved 8% compound annual growth rate (CAGR) from FY18 to FY24. In FY24, the industry grew by 9% year-over-year (y-o-y), reaching US$ 54 billion, with exports rising by 10% and domestic market growing by 9% compared to FY23. Regulated markets, making up ~60% of exports, saw 11% y-o-y growth. Semi-regulated and unregulated markets grew by 7% y-o-y, rebounding from a 3% contraction in FY23. These markets are projected to grow at a CAGR of 8% (FY25-FY27), with regulated markets expected to grow at 9%. Exports demonstrated robust growth, particularly in the North American market, which accounts for ~40% of India’s total pharmaceutical exports. Indian pharmaceutical sector is on the brink of substantial growth, with forecasts predicting an ~9% increase for FY25-FY27. In the export domain, growth is expected to be fueled by diversification in specialty molecules, seizing opportunities in the off -patent market, and increased penetration in rest of the world (ROW) markets.

Key weaknesses

Significant decline in revenue and profitability

In FY24, revenue from operations witnessed a degrowth of ~24% y-o-y from ₹154.94 crore in FY23 to ₹118.48 crore in FY24. Brazilian pharma company, Brainfarma Indústria Química e Farmacêutica S.A. (Brainfarma) is a major client for FLL, procuring Carisoprodol. Following the COVID-19 pandemic, Brainfarma significantly increased its procurement of Carisoprodol due to heightened demand, leading to overstocking and a subsequent reduction in procurement in FY24. This led to a decrease in the Carisoprodol’s contribution to revenue from ~₹59 crore in FY23 to ₹15 crore in FY24. However, FLL expects to regain its orders from Brainfarma in the current fiscal. Decline in the scale of operations and presence of higher fixed costs has led to a decline in operating profitability marked by PBILDT margin deteriorating from 24.05% in FY23 to 16.01% in FY24. Further, the company incurred ~₹2.25 crore towards transaction cost for raising funds from PE firm and a loss of ₹1.50 crore towards writing off the investment in one of its associate entities. These exceptional items in addition to increased finance cost led to a decline in profit after taxation (PAT) margin from 16.29% in FY23 to 3.66% in FY24. In Q1-FY25, the company has recognised a revenue of ₹31.31 crore with PBILDT of ₹8.56 crore. Further, the company has a moderate order book of ~₹45 crore as on September 18, 2024, which is to be supplied in next 2-3 months.

Project implementation risk

FLL has established a joint venture named Fermac Bio Private Limited in collaboration with Brasun Labs LLP (BLL) to manufacture three antibiotic products: Daptomycin, Fusidic Acid, and Teicoplanin, which are currently not produced in India. The project cost is estimated at ₹66 crore which is funded through a term loan of ₹45 crore and the balance through equity infusion by joint venture (JV) partners. FLL and BLL extended a corporate guarantee for this debt. Expected commercial operations date (COD) for the project is October 2024. Further, FLL is also undertaking a project to establish a production facility (Unit III) in Kadechur, Karnataka, through its subsidiary Fleming Life Sciences Private Limited. The project's estimated cost is ₹30 crore, which is funded through equity, unsecured loans, and internal cash flows from FLL.

Elongated working capital cycle
In FY24, the company's operating cycle extended to 175 days from 103 days. This was due to a longer collections period caused by delays in receiving payments from some clients resulting in an increase in the collections period from 98 days in FY23 to 143 days in FY24. Accounts receivable as of March 31, 2024, stood at ₹49.75 crore, which was reduced to ₹26.53 crore by June 30, 2024. The company also maintained WIP inventory as of March 31, 2024, in anticipation of a recovery in business operations of Carisoprodol and increased demand for D-pencilimine, leading to a higher inventory period of 101 days compared to 72 days for the previous year.

Presence in regulatory industry
The company is exposed to regulatory risk given its involvement in manufacturing pharmaceutical APIs, a sector subject to strict regulations across countries. Compliance requires obtaining approvals, licenses, and registrations, which are often associated with lengthy and costly processes. Time required to secure these approvals can vary significantly by country, taking anywhere from six months to several years. Any delays or setbacks in obtaining necessary approvals for product launches could have a negative impact on the company's growth and overall business outlook.

Liquidity: Adequate
The company generates sufficient cash accruals to meet its short-term debt obligations. However, reliance on bank borrowings for working capital has increased, with average working capital utilisation at 73% for the 12 months ending July 2024. This increase is primarily due to fixed overheads, given lower cash generation. Liquidity is further supported by current ratio of 1.68x as on March 31, 2024.

Assumptions/Covenants - Not applicable

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

Applicable criteria

Definition of Default
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Rating Watch
Manufacturing Companies
Pharmaceuticals
Financial Ratios – Non financial Sector
Short Term Instruments

About the company and industry

Industry classification

Macroeconomic indicator	Sector	Industry	Basic industry
Healthcare	Healthcare	Pharmaceuticals and biotechnology	Pharmaceuticals

FLL was incorporated in 1992 and is engaged in manufacturing and exporting APIs. The company was initially promoted by B Ravishankar, with the primary objective of manufacturing APIs. Later, in November 2014, Jeyamuruga Prakash acquired a 55% stake and took over the company's operations from December 2014 onwards. The company operates two manufacturing units in Telangana, audited and approved by regulatory agencies, including EUGMP, EDQM, WHO GMP, PMDA (Japan), COFEPRIS (Mexico), and Korea FDA, among others.

Brief Financials (₹ crore)	March 31, 2023 (A)	March 31, 2024 (A)	Q1-FY25 (UA)
Total operating income	154.94	118.48	31.31
PBILDT	37.26	18.97	8.56
PAT	25.24	4.34	3.79
Overall gearing (times)	0.09	0.43	0.44
Interest coverage (times)	20.40	6.14	NA

A: Audited, UA: Unaudited, NA: Not available; Note: these are latest available financial results

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Annexure-2

Detailed explanation of covenants of rated instrument / facility: Annexure-3

Complexity level of 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 and Rating Outlook
Fund-based - LT-Term Loan		-	-	January 2026	2.37	CARE BBB; Stable
Fund-based - LT/ ST-CC/Packing Credit		-	-	-	37.40	CARE BBB; Stable / CARE A3+
Non-fund-based - ST-BG/LC		-	-	-	4.10	CARE A3+

Annexure-2: Rating history for 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 2024-2025	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
1	Fund-based - LT/ ST-CC/Packing Credit	LT/ST	37.40	CARE BBB; Stable / CARE A3+	-	1)CARE BBB+; Stable / CARE A2 (05-Oct-23)	1)CARE BBB+; Stable (08-Nov-22)	1)CARE BBB; Stable (05-Oct-21)
2	Fund-based - LT/ ST-Standby Line of Credit	LT/ST	-	-	-	-	-	1)Withdrawn (05-Oct-21)
3	Non-fund-based - ST-BG/LC	ST	4.10	CARE A3+	-	1)CARE A2 (05-Oct-23)	1)CARE A2 (08-Nov-22)	1)CARE A3+ (05-Oct-21)
4	Non-fund-based - ST-Forward Contract	ST	-	-	-	-	-	1)Withdrawn (05-Oct-21)
5	Fund-based - LT-Term Loan	LT	2.37	CARE BBB; Stable	-	1)CARE BBB+; Stable (05-Oct-23)	1)CARE BBB+; Stable (08-Nov-22)	1)CARE BBB; Stable (05-Oct-21)

LT: Long term; ST: Short term; LT/ST: Long term/Short term

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

Annexure-4: Complexity level of instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Fund-based - LT-Term Loan	Simple
2	Fund-based - LT/ ST-CC/Packing Credit	Simple
3	Non-fund-based - ST-BG/LC	Simple

Annexure-5: Lender details

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

Annexure-6: List of entities consolidated - Not applicable

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

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