East West Pharma

May 30, 2019

Ratings

Facilities	**Amount (Rs. crore)**	**Rating[1]**	**Rating Action**
Long -term Bank Facilities	10.00	CARE BB+; Stable (Double B Plus; Outlook: Stable)	**Assigned**
Total Facilities	**10.00 (Rupees Ten Crore Only)**		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of East West Pharma is tempered by modest scale of operations with fluctuating total operating income during the review period, working capital intensive nature of operations, inherent regulatory risk associated with pharmaceutical Industry albeit steady growth prospects and partnership nature of business constitution with inherent risk of withdrawal of capital. However, the rating derives comfort from experienced partners along with established track record of the business, satisfactory profitability margins albeit fluctuations during the review period, comfortable capital structure and debt coverage indicators, diversified product portfolio and wide range of distribution network.

Going forward, the firm’s ability of the firm to increase scale of operations amidst tough competition and intense regulations while managing its working capital requirements efficiently are the key rating sensitivities.

Detailed description of the key rating drivers

<u>Key Rating Weaknesses</u>

Moderate scale of operations with fluctuating total operating income during the review period

The scale of operations stood moderate marked by total operating income of Rs.113.95 crore during FY18 and networth of Rs.80.44 crore as on March 31, 2018. During the last three years ended March 31, 2018, the total operating income has been moderately fluctuating from Rs. 82.59 crore in FY16 to Rs. 113.96 crore in FY18. Nearly 88% of the total operating income is driven by sale of medicines and pharmaceutical products while the remaining from hospital receipts.

Working capital intensive nature of operations

The operating cycle stood at 126 days in FY18 as against 77 days in FY17 owing to deterioration in the average payable period. The creditors are usually settled within a span of 40 days, the decline in average creditor period was on account of early settlement to creditors owing to increased reliance on cash credit facility in FY18. Besides, the firm maintains multiple stock keeping units as a result of which its inventory levels tend to be relatively high which increased from 41 days in FY17 to 66 days in FY18. The firm allows credit period that ranges between 90-120 days to its customers. Further, the working capital limit utilization also stood high at 95% in during 12 months ended March 31, 2019.

Inherent regulatory risk associated with pharmaceutical Industry albeit steady growth prospects

Competitive pressure in domestic formulation market has been rising steadily prompted by significant increase in investments by domestic players in marketing efforts through expansion in field force. Further, Government regulations, including those implemented by the National Pharmaceutical Pricing Authority (NPPA), have also impacted the industry’s growth and profitability. Nevertheless, domestic formulations segment is expected to grow led by rise in chronic diseases, increasing per capita income and improvement in access to healthcare facilities along with growing penetration of health insurance.

Partnership nature of business constitution with inherent risk of withdrawal of capital

The group is constituted as a proprietorship/partnership firm wherein it is exposed to frequent withdrawal of capital and resultant erosion of the net worth resulting in lower capital base despite the firm being able to generate sufficient profits in the past.

<u>Key Rating Strengths</u>

Experienced partners along with established track record of the business

Mr. B.B. Mohan Kumar, the Managing Partner, is having vast experience in manufacturing pharmaceutical products. The firm, established in the year 2010, is a closely held concern with the entire capital held by the same family members. The partners are well experienced in health care segment and actively participate in the management of day-to-day affairs of the firm. Mr. Ganesan, Vice president, qualified in M.Sc. (Chemistry), has about a three decade of experience in pharmaceutical industry

[1]*Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

and takes care of the overall activities of the group. The vast track record of operation and the vast experience of the management team is expected to benefit the firm in the future also.

Satisfactory profitability margins albeit fluctuations
In absolute terms, the combined operating profits of the group grew by 60% over FY17-18. While, on a standalone basis, Sikkim unit reported net loss of Rs. 8.20 crore and 1.84 crore for FY17 and FY18 respectively. The net loss was primarily on account of low income generated by the hospital division in the initial years of its operation leading to under-absorption of fixed salary cost and professional consultancy charges spent towards doctors and professionals. Apart, investment in hospital division of the Sikkim unit has resulted in increased depreciation provision from FY17 onwards. In addition to high employee cost towards medical staff and depreciation provision, the group spends significant portion of expenses towards marketing of pharmaceuticals. As a result of decline in quantum of losses as well as the decline in overall sales promotional expenses, the PBILDT margin of the group improved and stood at 20.29% in FY18 as against 12.61% in FY17. The PAT margin stood at 16.33% in FY18 increasing by 750 bps from 8.80% in FY17. The improvement in PAT margin was mainly on account of improved operating profits resulting in absorption of financial expenses and depreciation provisions.

Comfortable capital structure and debt-coverage indicators
The debt profile of the group comprises predominantly of working capital facility only. The capital structure of the group as represented by overall gearing has remained comfortable at 0.13x as on March 31, 2018 as against 0.11x as on March 31, 2017 on account of strong net worth base. In line with debt level of the group, the interest cost also stood low leading to comfortable PBILDT interest coverage of 29.42x and 34.07x, in FY17 and FY18 respectively. TD/GCA stood comfortable at 0.48x in FY18 as against 0.54x in FY17 at the back of improved cash accruals reported by the group in FY18 which stood at Rs. 22.16 crore (PY: Rs. 13.93 crore).

Diversified product portfolio and wide range of distribution network
The group has a portfolio of around 900 products spread across eight therapeutic segments, however, the diabetic, dermatology and cardiology segments are the major revenue contributor to the company. EWP Associates, a stock keeping and distribution unit of the group has seven branches at various locations namely Salem, Bangalore, Palakkad, Vijayawada, Chennai, Roorkee and Guwahati with nearly 448 distributors in FY18 as against 226 distributors in FY16. Besides stock keeping and distribution, EWP associates also acts as a marketing arm for its products on behalf of all the three units. The firm sells its products in domestic market to distributors as well as participates in government tenders and supplies to central/state government health departments as well as private hospitals.

Liquidity analysis
The group had total cash and cash equivalents amounting to Rs. 7.45 crore as on March 31, 2018. As on March 31, 2018, the current ratio and quick ratio stood at 3.10x and 2.34x respectively. As a result of high utilization of the working capital facility the average unutilized portion was around 5% which amounted to Rs. 0.50 crore (approx.) during 12 months ended March 2019.

Analytical Approach: For the purpose of analysis, CARE has combined financials of three entities of the East West Pharma (Sikkim) and its group, East West Pharma- Unit II, Roorkee, and East West Pharma (Guwahati) since these entities are engaged similar industry, and have common management along with having significant operational and financial linkages.

Applicable criteria
Criteria on assigning Outlook to Credit ratings
CARE's policy on Default Recognition
Financial ratios: Non-Financial sector
Rating Methodology- Manufacturing Companies
Rating Methodology- Pharmaceutical Sector
Rating Methodology- Factoring Linkages in Ratings

Background
East West Pharma is a Tamilnadu based closely held firm, established in 2010 is engaged in manufacturing of drug formulations and pharmaceuticals products from its three manufacturing facilities located in the states of Sikkim, Assam and Uttarakhand respectively. All the units are ISO 9001:2015 accredited and WHO-GMP certified facility. EWP Associates, a marketing and distribution division and Chennai National Hospital (CHN), a multispecialty hospital which are the units of East West Pharma (Sikkim) and its group and was established in 2015 and 2016 respectively.

Brief Financials (Rs. crore)	FY17 (UA)	FY18 (UA)
Total operating income	114.45	113.95
PBILDT	14.42	23.12
PAT	10.07	18.61
Overall gearing (times)	0.11	0.13
Interest coverage (times)	29.42	34.07

UA: Unaudited

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History (Last three years): Please refer Annexure-2

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Cash Credit	-	-	-	10.00	CARE BB+; Stable

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Fund-based - LT-Cash Credit	LT	10.00	CARE BB+; Stable	-	-	-	-

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

Contact us

Media Contact
Mradul Mishra
Contact no. – +91-22-6837 4424
Email ID – mradul.mishra@careratings.com

Analyst Contact
Group Head Name - Manish Kumar
Group Head Contact no. - 9949547551
Group Head Email ID - manish.kumar@careratings.com

Business Development Contact
Name: Uma. S
Contact no. : 9894321525
Email ID: uma.s@careratings.com

About CARE Ratings:

CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

****For detailed Rationale Report and subscription information, please contact us at www.careratings.com**