Emcure Pharmaceuticals Limited

September 16, 2019

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long term bank facilities	1052.90	CARE A; Negative (Single A; Outlook: Negative)	Revised from CARE A+; Stable (Single A plus; Outlook: Stable)
Short term bank facilities (Non-Fund based)	98.00	CARE A2+ (A Two Plus)	Revised from CARE A1 (A one)
Long term / Short term bank facilities (Fund based)	586.00	CARE A; Negative/CARE A2+ (Single A; Outlook: Negative/A Two Plus)	Revised from CARE A+; Stable/ CARE A1 (Single A plus; Outlook: Stable/ A one)
Total Facilities	**Rs. 1,736.90 (Rupee Seventeen hundred and Thirty Six Crore and Ninety lakh only)**		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision in the ratings to the bank facilities of Emcure Pharmaceuiticals Limited (Consolidated, hereafter referred to as EPL/ Group) factors in the subdued performance of the company during FY19 (refers to April 1 to March 31) marked by de-growth in the total operating income, decline in the profitability, deterioration in the debt coverage indicators and moderation in liquidity parameters vis-à-vis the envisaged overall financial performance albeit the improvement in the operating performance from previous financial year, owing mainly to decline in sales to US markets with continued 'import alert' by United States Food and Drugs Administration (USFDA) on EPL's Hinjewadi facility coupled with dilution of significant market share for various products on account of stiff competition from new entrants. The decline in sales to US markets is also attributed to delay in launches of new products and dropping certain product launches due to changing market conditions. Further, the sales in domestic market in H2FY19 remained slow as a result of adverse domestic market conditions.

The revision also factors ongoing investigations relating to drug pricing matters along with the penalty paid towards settlement of various legal disputes. CARE believes, the uncertainty revolving around ongoing USFDA investigations and pending approvals for new launches is expected to keep the US sales volume and overall profitability under pressure in medium term.

Nevertheless, the rating continues to derive strength from long track record and promoters' vast experience of over three decades in the pharmaceutical industry, accredited manufacturing facilities along with diversified product portfolio across therapeutic segments; different geographies and long-term contracts with the pharmaceutical majors.

The rating strengths continue to remain constrained by delay in new product launches and cost incurred on revamp of processes at its plants in the wake of the 'import alert' by USFDA impacting profit margins, intense competition in the generic formulations industry along with regulatory risk inherent in the pharmaceutical industry. The ratings strengths are further constrained by EPL's exposure to regulated markets, especially the US, which is witnessing increased competition resulting into pricing pressure in the generics space and heightened regulatory scrutiny and exposure to foreign exchange fluctuations.

Going forward, EPL's ability to resolve pending regulatory issues and realize envisaged benefits out of expenditure incurred on Research and Development activities and capex across group companies remain the key rating sensitivities. The ability of the group to increase its scale of operations by expanding its footprint in regulated & domestic markets across therapeutic segments, stabilize the operations of the recently acquired companies, while improving its capital structure and debt coverage indicators, improvement in the profit margins and liquidity on the back of competition in domestic as well as overseas market are the key rating monitorable. Timely resolution of USFDA import alert is critical from credit perspective. Ability to successfully shift operations to newly established Sanand Unit and ramp up operations through new product launches from Sanand (USFDA approved) unit remains to be seen.

Outlook: Negative

The revision in outlook reflects CARE's belief that the consolidated operating performance of the company would remain subdued in medium term due to ongoing USFDA investigation & exposure of the company to competitive intensity. CARE also believes that the debt coverage indicators are expected to remain moderate on the back of subdued operating

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

performance coupled with high committed debt obligations in the medium term. The ability of the company to improve financial risk profile & clearance of USFDA would result in outlook being stable.

Detailed description of the key rating drivers
Key Rating Strength
Experienced management and successful track record of the group in pharmaceutical industry
The promoters have more than three decades of experience in the pharmaceutical industry. The CEO of the company, Mr. Satish Mehta is a first generation entrepreneur with an experience of over 3 decades in the field of pharmaceuticals. Ms. Namita Thapar (CFO), Chartered Accountant and MBA, is actively involved in the marketing and distribution division and finance division and overlooking human resources division of the company. Mr. William S Marth, President & CEO, North America & Europe region and board member for HPI, Marcan Pharmaceuticals Inc and Emcure Pharma UK Ltd has served as President & CEO for Albany Molecular Research Inc (AMRI) till January 2018 and was President & CEO for Teva Pharmaceuticals USA till 2012. The group has team of highly qualified and experienced professionals in the field of pharmaceuticals.

Diversified product portfolio with the new launches, operations in India, USA and various emerging markets and focus on chronic high-value segments
The group is vertically integrated, manufacturing APIs and formulations and is also involved in the bio-technology drugs. Under formulations, EPL has presence in the high value chronic therapy as well as in acute segments. Under chronic segment, the company's products are diversified across Cardiology, Oncology, Nephrology, Anti-HIV, etc. Acute products are diversified across Anti-infective, Pain Management, Anemia, Gynaecology, Anti Retrovirals, Pediatrics, etc. The group has launched various new products during FY18 and FY19 particularly within the Oncology/Antileukamics, Gynaec, hormones, Neuro/CNS, Anti-infectives and HIV segments.

Accredited manufacturing facilities with well-equipped R&D facility
In the group, EPL, Heritage Pharma Labs Inc (HPL), Gennova Biopharmaceutical Limited (GBL) and Zuventus Healthcare Limited (ZHL) have manufacturing facilities while other subsidiaries are engaged in warehousing and marketing of drugs manufactured by EPL in various geographies.
EPL has six manufacturing facilities (five in Pune and one located at Jammu), out of which three are approved by UK Medicines & Healthcare Products Regulatory Agency (MHRA, UK), Geneva WHO, South African Medicine Control Council (MCC) and ANVISA, Brazil while four of them are approved by USFDA. Furthermore, the group has six state of art R&D centres in India, all recognized by the Department of Scientific & Industrial Research (DSIR) and one in USA under HPL.
GBL's manufacturing facility is located at Pune while those of ZHL are located at Jammu, Sikkim and Bengaluru. HPL has a manufacturing facility along with R&D centre located at New Jersey, USA.

Strong marketing network coupled with strengthening presence in international markets along with long term contract with pharmaceutical majors
The group has a strong sales and marketing team both within India and outside the country. The group has an established marketing network through channel partners in the international markets and C&F agents within domestic market.

Geographical diversification and organic as well as inorganic growth
The group has a wide geographical presence with sales primarily to regulated markets like USA and UK, and has an overall healthy mix of exports, providing the group geographic diversification. The group is also expanding its presence in various emerging markets and Canada.
The geographically diversified nature of revenues significantly reduces the exposure of the company towards any adverse economic slowdown in any single geography. Over the years, the group has established its presence in domestic markets through EPL, GBL, and ZHL and in international markets through overseas acquisitions.

Liquidity
Although internal cash accruals are partially used for capex; Group's liquidity indicator derives comfort from cash and bank balance of Rs.105 crore as on March 31, 2019 and unutilized fund based working capital limits. However, the cash reserves of the company have declined from Rs 269.00 crore as on March 31, 2018. The Group's working capital utilization was seen high at around 80.84% as on June 30, 2019. Nevertheless, group's internal cash accruals, cash and bank balance and unutilized working capital limits provide adequate buffer to cover the scheduled debt obligations in medium term.

Key Rating Weaknesses

Growth in scale of operations, however, moderation in overall financial risk profile marked by lower profitability margin, deterioration in debt coverage indicators and liquidity parameters

During the year FY19, the company witnessed decline in the PBILDT margin to ~17.50% in FY19 as against 18.86% in FY18 majorly on account of higher employee cost. However, there was improvement in the revenue and the profitability of the company in FY19 vis-à-vis financial performance in FY18. The gross cash accrual marginally declined for FY19 at at Rs 385.29 crore as against Rs 395.34 crore in FY18 mainly on account of higher finance cost and depreciation charged during the year due to increase in debt and fixed assets. The debt service coverage ratio remained moderate with higher loan repayments due in the current year. Further, the company has witnessed decline in cash reserves from Rs.269 crore in FY18 to Rs.105 crore in FY19. The current ratio of the company also slightly declined from 1.02 in FY18 to 0.97 in FY19.

USFDA Import Alert at Hinjewadi Plant continues, impacting operations in USA and delaying new product launches, while additional costs burden profitability

In July 14, 2015, US-Food and Drug Administration (USFDA) has barred imports of drugs manufactured at the Hinjewadi, Pune plant of Emcure Pharmaceuticals Ltd. (EPL) due to violations of certain standard manufacturing process and documentation. The import alerts named 'Detention without physical examination of drugs from firms which have not met drug Good Manufacturing Practices (GMPs)' have been issued against the plant of the company. The said ban is also delaying EPL's new product launches in the USA markets and impacting the group's scale of operations and profitability.

Further, the Company is recently issued a warning letter by USFDA which cites the observations and significant violations of current good manufacturing practice (CGMP) regulations for finished pharmaceuticals which remains in continuation with the said ongoing USFDA investigation. However, EPL continues to manufacture and export 9 exempted products from the plant.

Intense competition and exposure to regulatory risk inherent in pharmaceutical industry

The company faces intense competition in the domestic as well as international markets. Pricing pressure, increasing regulation, increased sensitivity towards product performance are the key issues in the pharmaceutical industry. The pharmaceutical industry has been a highly regulated industry worldwide by virtue of its direct bearing on public health. In India too, government policies have played key role in performance of companies such as explicit control on drug prices in the form of drug price control order (DPCO). Further, the patent laws and related regulations might hamper company's plans to launch new products and cater to new markets.

Indian pharmaceutical companies are expected to continue to experience growth from US markets over medium term backed by sizeable generic opportunities over next two years, strong product pipeline of ANDAs with increasing proportion of complex generic. However, US markets are facing multiple challenges such as increased scrutiny by USFDA, consolidation of supply-chain and need for higher investments in R&D to tap complex segments. Companies with growing portfolio comprising niche or complex products and high levels of backward integration are likely to be better positioned considering above challenges.

Foreign exchange fluctuation risk

The group generates majority of its overall revenues in foreign currency mainly denominated in USD, Euro and GBP. Large portion of outflows in foreign currency is hedged naturally against the foreign currency receivables. As on March 31, 2019, foreign currency receivables stood at ~Rs.203 crore against which the group had debt in the form of ECB (External Commercial Borrowings) and other payables denominated in USD/EUR/GBP amounting to ~Rs. 281 crore as on March 31, 2019 thus offsetting the movement in foreign exchange rate to much extent.

Industry outlook: **Stable**

Outlook for The Indian pharmaceutical industry (IPI) remains stable in medium to long term backed by growth opportunity in terms of capitalization on major blockbuster drugs coming off-patent paving the way for entry of generics, especially in the USA market, geographical diversification into emerging markets, steady growth of governments' spending on healthcare, increasing awareness and accessibility of healthcare. However, the industry players are facing headwinds in terms of structural reforms by governments, stringent regulation both in regulated and semi regulated market, intensification of competition in generic and channel consolidation which has led to pricing pressure to the company together impacting the profitability of the industry players. Recent rupee depreciation against USD benefits the export oriented pharma sector however intense competition in USA markets offsets this benefit.

Analytical Approach – Consolidated*

CARE has considered consolidated financials of the Emcure Group including EPL and its 12 direct and 10 indirect subsidiaries on account of exposure of EPL to group companies in terms of corporate guarantee and similar line of business and management. Furthermore, the majority of the subsidiaries of EPL are engaged in the trading and marketing of products manufactured by EPL across various geographies. As a result of similar line of business and inter group transactions, consolidated view has been considered.

The 12 direct subsidiaries and 10 indirect subsidiaries are as given below:

Direct Subsidiaries	
1	Gennova Biopharmaecuticals Ltd
2	Zuventus Healthcare Ltd
3	Emcure Nigeria Ltd
4	Emcure Pharmaceuticals Mena FZ LLC
5	Emcure Pharmaceuticals South Africa Pty Ltd
6	Emcure Brasil Farmaceutical Ltd
7	Heritage Pharma Holdings Inc
8	EmcurePharma UK Ltd
9	EmcurePharma Peru SAC
10	EmcurePharma Mexico S.A DE C.V
11	Emcure Pharmaceuticals Pty Ltd
12	Marcan Pharmaceuticals Inc
Indirect Subsidiaries	
13	Heritage Pharma Labs Inc
14	Heritage Pharmaceuticals Inc
15	Tillomed Laboratories Ltd
16	Tillomed Holdings Ltd
17	TilomedPharma Gm
18	LaboratoriosTilomed Spain SLU
19	Tillomed Italia SRL
20	Emcure Newzealand PharmaCeuticals Limited
21	Tillomed France SAS
22	HACCO Pharma Inc

Applicable Criteria
Criteria on assigning Outlook to Credit Ratings
Criteria for Short Term Instruments
CARE's Policy on Default Recognition
CARE's methodology for manufacturing companies
CARE's methodology for Pharmaceutical sector
Rating Methodology: Factoring Linkages in Ratings
Financial ratios – Non-Financial Sector

About the Company
Emcure Pharmaceuticals Limited (EPL) was incorporated in April 1981 as a Private Limited Company and is engaged in manufacturing of pharmaceuticals products (mainly formulations) either on Loan License or Principal to Principal basis. Subsequently, in August 2001, the company was converted to public limited company (unlisted).EPL is managed by a ten member Board of Directors comprising four promoter/executive members and six non-executive and independent directors.

Brief Financials (Consolidated) (Rs. crore)#	FY18 (A)	FY19 (A)
Total operating income	4263.37	4812.31
PBILDT	804.27	843.90
PAT	174.19	209.19
Overall gearing (times)	1.25	1.24
Interest coverage (times)	4.64	3.79

A: Audited
 # Based on IND-AS

Status of non-cooperation with previous CRA – Not Applicable

Any other information- Not Applicable

Rating History (Last three years): Please refer Annexure II

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-Term Loan	-	-	March 2023	1002.90	CARE A; Negative
Non-fund-based - ST-BG/LC	-	-	-	98.00	CARE A2+
Fund-based - LT/ ST-Working Capital Demand loan	-	-	-	479.00	CARE A; Negative / CARE A2+
Fund-based/Non-fund-based-LT/ST	-	-	-	107.00	CARE A; Negative / CARE A2+
Fund-based - LT-Proposed fund based limits	-	-	-	50.00	CARE A; Negative

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-Term Loan	LT	1002.90	CARE A; Negative	-	1)CARE A+; Stable (05-Dec-18)	1)CARE A+; Stable (09-Oct-17)	1)CARE AA-; Stable (10-Feb-17)
2.	Non-fund-based - ST-BG/LC	ST	98.00	CARE A2+	-	1)CARE A1 (05-Dec-18)	1)CARE A1 (09-Oct-17)	1)CARE A1+ (10-Feb-17)
3.	Fund-based - LT/ ST-Working Capital Demand loan	LT/ST	479.00	CARE A; Negative / CARE A2+	-	1)CARE A+; Stable / CARE A1 (05-Dec-18)	1)CARE A+; Stable / CARE A1 (09-Oct-17)	1)CARE AA-; Stable / CARE A1+ (10-Feb-17)
4.	Fund-based/Non-fund-based-LT/ST	LT/ST	107.00	CARE A; Negative / CARE A2+	-	1)CARE A+; Stable / CARE A1 (05-Dec-18)	1)CARE A+; Stable / CARE A1 (09-Oct-17)	1)CARE AA-; Stable / CARE A1+ (10-Feb-17)
5.	Non-fund-based - LT-Letter of credit	LT	-	-	-	1)Withdrawn (05-Dec-18)	1)CARE A+; Stable (09-Oct-17)	1)CARE AA-; Stable (10-Feb-17)
6.	Fund-based - LT-Proposed fund based limits	LT	50.00	CARE A; Negative	-	1)CARE A+; Stable (05-Dec-18)	-	-

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.*

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