Fermenta Biotech Limited

January 08, 2020

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long-term Bank Facilities (fund based limit)	109.00 (enhanced from 69.00)	**CARE A-; Stable (Single A Minus; Outlook: Stable)**	**Reaffirmed**
Long-term Bank Facilities (term loan)	74.56 (enhanced from 45.52)	**CARE A-; Stable (Single A Minus; Outlook: Stable)**	**Reaffirmed**
Short-term Bank Facilities (non-fund based limit)	6.25 (6.25)	**CARE A2 (A Two)**	**Reaffirmed**
Total	**189.81 (Rs. One Hundred Eighty Nine crore and Eighty One lakhs only)**		

Details of instruments/facilities in Annexure-2

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Fermenta Biotech Limited (FBL) continues to derive strength from established track record of FBL in pharmaceutical industry, leadership position in Vitamin D3 API product range, wide spread presence across various geographies with reputed clientele, as well as strong financial risk profile characterized by comfortable capital structure and debt coverage indicators. The core expertise for Vitamin D3 API is developed on the back of strong in-house research and development team.

The rating strengths are tempered by moderate scale of operations with high product concentration risk, working capital intensive nature of business, supplier concentration risk for major raw materials for Vitamin D3 API manufacturing (expected to reduce post completion of the ongoing backward integration project), profitability susceptible to volatile movement of commodity prices as well as competition from China in the feed grade segment. Furthermore, the company is exposed to stabilization risk related to the ongoing backward integration project.

The ability of the company to grow the operations and maintain profits in the wake of increasing competition, to maintain capital structure and to efficiently manage the working capital cycle are the key rating sensitivities. In addition, any major debt funded capital expenditure project will also be monitored.

Rating sensitivities:

Positive factors:

- Increase in scale of operations by more than 25% on a sustainable basis while maintaining profitability margins.
- Improvement in working capital cycle by improving debtor realization and efficient management of inventory on a sustainable basis.

Negative factors:

- Reduction in PBILDT margins resulting in deterioration in debt coverage indicators.
- Increase in overall gearing beyond 1x on a sustainable basis, due to capex or additional working capital requirements.

Detailed description of the key rating drivers

Key Rating Strengths

Established track record in the pharmaceutical industry along with strong research and development

FBL has an established track record of over three decades in the pharmaceutical business with key focus on Vitamin D3 API segment. Over the years, it has been able to prove its expertise in this segment and regularly added capacities to cater to this segment. In order to support and manage the overall operations, the senior management is supported by well qualified and experienced second tier management in a well-defined organizational structure. The company has also developed an in-house research and development (R&D) team to improve process and product technologies to have competitive edge in the industry.

Leadership position in Vitamin D3 API segment albeit high product concentration risk

The company's business can be classified majorly under four segments which are Vitamin D3 API, specialty APIs, biological enzymes and biotech based environmental solutions. The company is one of the few players globally to obtain a Certificate of Suitability from European Directorate for the Quality of Medicines (EDQM) for manufacturing of Vitamin D3 API. The demand for Vitamin D3 product range is growing and the company has developed expertise over the years and established its

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

presence in the global market (in 2009 it entered into export market). However, there is product concentration risk with around 85% of the total sales in FY19 contributed by Vitamin D3 API.

Reputed clientele with presence in domestic and export markets
Over the years, the company is increasing presence in export market (forayed in 2009) through sale of feed grade segment (commenced in FY15) and other Vitamin D3 API products. The company has established presence with around 78% of total sales derived from export markets in FY19. The company has presence across 50 countries including USA, UK, European Union, Brazil, Mexico, Russia, China, Turkey, Saudi Arabia, Israel, Australia and New Zealand.

Healthy operating profitability
PBILDT margins increased from 34.88% in FY18 to 40.18% in FY19 (FBL) mainly on account of increase in average feed grade price for Vitamin D3. The average price for animal feed grade increased from USD 35$ in FY18 to USD 44$ in FY19.
However, in H1FY20 the PBILDT margins declined to 28.35%, this is mainly on account of reduction in animal feed prices. The PBILDT margin are expected to remain healthy around 25% from FY20 onwards mainly as Vitamin D3 is a niche product manufactured by 4-5 players globally. However, company's profitability is vulnerable to competition from China and foreign currency fluctuations. The company imported around 60% of total raw material requirements whereas around 78% of sales are exports in FY19.

Comfortable capital structure and debt coverage indicators
The company's financial risk profile is comfortable, characterized by strong net worth. The overall gearing (including acceptances), although increased from 0.19x as on March 31, 2018 to 0.86 times as on March 31, 2019 and 0.71 times as on September 30, 2019, remains comfortable. The increase in debt is mainly due to addition of DIL Ltd's debt post its amalgamation with FBL. In FY20 and FY21, company plans to set up additional multi-synthesis plant in Dahej facility for manufacturing Vitamin D3 to increase the installed capacity by 20%. The total capital expenditure is expected to be Rs.30 Cr, funded through internal accruals of Rs.6 Cr and long term debt of Rs.24 Cr. Also, the company has projected additional working capital requirements to support the growing operations.
Despite additional term loan and working capital limits, the overall gearing is expected to remain comfortable. Furthermore, debt coverage indicators also stood comfortable for FY19 i.e. interest coverage ratio, total debt to gross cash accruals (GCA), and total debt/PBILDT at 7.29 times, 1.87 times, and 1.37 times in FY19 respectively.

Key Rating Weaknesses
Moderate scale of operations
The operating income reflected a growth of 34.01% in FY19 to Rs.400 crore from Rs.299 crore in FY18. Over the years (FY17-FY19), the company installed additional capacities to meet the growing demand under the same segment especially feed grade segment. However, the operations remain moderate.

Supplier concentration risk
The major raw material for manufacturing of Vitamin D3 API is cholesterol, the supply of which is an oligopolistic market with limited players. However, this risk will be mitigated to a large extent once the ongoing backward integration project at existing Dahej plant is completed in Q4FY20. Timely completion and stabilization of the same without disrupting the existing manufacturing process are crucial from credit perspective and a key rating monitorable.

Working capital intensive operations
The business is working capital intensive since it carries significant inventory for various products under manufacturing at different stages of production, maintained at two factories. Also, the credit period required to be offered to customers under feed grade segment is higher due to intense competition. These are being funded by creditors and working capital borrowing from banks with an average utilization of 72% for the past 12 months ending October 2019.

Susceptible to volatile movement of commodity prices and competition from China under feed grade segment
The Vitamin D3 API demand is derived from five segments which are from pharmaceutical, dietary nutritional and supplements (DNS), cold water dispenser (food industry), veterinary, and animal feed (feed grade and oil). Of the same, animal feed is a commoditized segment since no stringent pharmaceutical guidelines apply. The demand in animal feed is derived from export markets. China is the major supplier in animal feed grade segment and the industry is characterized with intense competition, low entry barriers and volatile commodity prices.
Liquidity position: Adequate
The improvement in profitability resulted in improved liquidity position of FBL. The total repayment commitment in H2FY20 and FY21 is Rs.4.55 crore and Rs.17.05 crore respectively. Moreover, company plans to avail additional fund based working capital limits amounting Rs.10.00 crore to support requirements of newly built multi synthesis plant in Dahej.

However, as on September 30, 2019, the cash and cash equivalents held by the company (consolidated level) is around Rs.50.30 crore. Therefore, the adequate liquidity cushion is available for repayments and working capital requirements.

Analytical approach: Consolidated; list of entities consolidated is mentioned below

- Aegean Properties Limited
- CC Squares Films Limited
- Fermenta Biotech UK Limited
- GI Biotech Private Limited

Applicable Criteria
CARE's Policy on Default Recognition
CARE's methodology for Short-term Instruments
Financial ratios – Non-Financial Sector
Rating Methodology – Pharmaceutical Sector
Criteria on assigning Outlook and credit watch to the credit ratings

About the Company
FBL, incorporated in 1986, was a subsidiary of DIL Limited (DIL) till September, 2019. As per NCLT order dated September 19, 2019, the amalgamation of DIL Limited (formerly holding company) with Fermenta Biotech Limited was approved. Post this amalgamation, DIL Limited was renamed as 'Fermenta Biotech Limited'. Post amalgamation, FBL has two business segments; i,e, lease rental business for commercial properties developed in Thane and manufacturing of active pharmaceutical ingredients (APIs).
FBL's pharmaceutical business can be classified majorly under four segments which are Vitamin D3 APIs, specialty APIs, biological enzymes and biotech based environmental solutions. The company's manufacturing facilities are located at Kullu (Himachal Pradesh) and in Dahej (Gujarat). The facilities are registered with Food Facility Registration Module (FFRM) which operates under the aegis of United States Food and Drug Administration (USFDA). FBL is also certified by World Health Organisation (WHO), Good Manufacturing Practise (GMP), USFDA Establishment Inspection Report (EIR) and received Certificate of Suitability (CEP) accreditation issued by European Directorate for the Quality of Medicines (EDQM) for manufacturing vitamin D3 API.
The company developed commercial property named "THANE ONE" (earlier part of DIL Limited) of a total area of 1.94 lakh square feet at Thane (leasable area is 1.86 lakh square feet). The commercial property is classified as information technology (IT)/IT enabled Services Park on its freehold land. Post amalgamation, the company has four wholly owned subsidiaries namely Aegean Properties Limited, CC Squares Films Limited, Fermenta Biotech UK Limited and GI Biotech Private Limited, of which latter two are dormant. Agean Propertes Limited and CC Squares Films Limited have lease rental business however, the scale is too small.

Brief Financials (Rs. crore)	FY18(A) FBL Standalone	FY19 (A) FBL Standalone	FY19 (A) FBL Consolidated
Total operating income	298.54	400.08	410.70
PBILDT	104.13	160.77	157.72
PAT	72.74	113.06	117.47
Overall gearing (times)	0.19	0.24	0.86
Interest coverage (times)	29.61	30.50	7.64

A: Audited

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating History for 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	-	-	-	77.00	CARE A-; Stable
Fund-based - LT-Cash Credit	-	-	-	32.00	CARE A-; Stable
Non-fund-based - ST-BG/LC	-	-	-	6.25	CARE A2
Fund-based - LT-Term Loan	-	-	March, 2025	74.56	CARE A-; 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	77.00	CARE A-; Stable	-	1)CARE A-; Stable (10-Jan-19) 2)CARE BBB+ (Under Credit watch with Developing Implications) (06-Apr-18)	1)CARE BBB+ (Under Credit watch with Developing Implications) (26-Dec-17) 2)CARE BBB+; Stable (19-Apr-17)	-
2.	Fund-based - LT-Cash Credit	LT	32.00	CARE A-; Stable	-	1)CARE A-; Stable (10-Jan-19) 2)CARE BBB+ (Under Credit watch with Developing Implications) (06-Apr-18)	1)CARE BBB+ (Under Credit watch with Developing Implications) (26-Dec-17) 2)CARE BBB+; Stable (19-Apr-17)	-
3.	Non-fund-based - ST-BG/LC	ST	6.25	CARE A2	-	1)CARE A2 (10-Jan-19) 2)CARE A3+ (Under Credit watch with Developing Implications) (06-Apr-18)	1)CARE A3+ (Under Credit watch with Developing Implications) (26-Dec-17) 2)CARE A3+ (19-Apr-17)	-
4.	Fund-based - LT-Term Loan	LT	74.56	CARE A-; Stable	-	1)CARE A-; Stable (10-Jan-19) 2)CARE BBB+ (Under Credit watch with Developing Implications)	1)CARE BBB+ (Under Credit watch with Developing Implications) (26-Dec-17) 2)CARE BBB+; Stable	-

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
						(06-Apr-18)	(19-Apr-17)	

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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