

Hester Biosciences Limited

December 25, 2018

Ratings

Facilities	Amount (Rs. crore)	Rating ¹	Rating Action
Long-term Bank Facilities	20.82 (Enhanced from Rs.19.82 crore)	CARE A-; Stable (Single A Minus; Outlook: Stable)	Reaffirmed
Long / Short-term Bank Facilities	30.00 (Reduced from Rs.35.00 crore)	CARE A-; Stable/ CARE A2 (Single A Minus; Outlook: Stable/ A Two)	Reaffirmed
Short-term Bank Facilities	28.97	CARE A2 (A Two)	Assigned
Total Facilities	79.79 (Rupees Seventy Nine Crore and Seventy Nine Lakh only)		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Hester Biosciences Limited (HBL) continue to derive strength from its experienced promoters, established position in the poultry vaccine industry, strong marketing and distribution network and diversified revenue stream with increasing focus on large animal division and healthcare products. The ratings also factor in the consistent growth in its total operating income, healthy profitability margins, comfortable capital structure and debt coverage indicators, and adequate liquidity.

The rating strengths are tempered by HBL's working capital intensive nature of operation with high inventory holding requirement, presence in regulated vaccine industry, lower than envisaged production and sales volumes from Nepal operations largely due to tender driven nature of business and implementation and salability risk associated with ongoing large size capital expenditure plan in Africa.

Ability of the company to maintain its healthy profitability margins and comfortable capital structure along with effective management of working capital are the key rating sensitivities. Moreover, ramp up in production and sales volumes at Nepal in order to achieve the envisaged returns and timely progress of Africa project also remain key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Wide experience of promoters: HBL was founded by Mr. Rajiv Gandhi, CEO and Managing Director, who has an experience of around three decades in vaccine industry and looks after the overall operations of the company. The promoters are supported by qualified second tier management.

Long and established track record of operations: HBL has track record of more than two decades in manufacturing of poultry vaccine. HBL primarily operates into two segments, i.e. vaccine and animal healthcare products each for poultry as well as large animals. HBL manufactures vaccine and health products mainly for poultry apart from sheep, goats, cattle and buffalo. Moreover, HBL is certified by DSIR (Department of Science and Industrial Research), WHO-GMP (World Health Organization-Good Manufacturing Practice), GLP (Good laboratory Practice), ISO 9001:2015, ISO 14001:2015 and OHSAS 18001:2007.

Diversified revenue stream with increasing focus on large animal division and healthcare products: As on March 31, 2018, the product portfolio of HBL comprises of 49 vaccines (including both poultry and large animal vaccines) and 50 animal health products (medicines, feed supplements and disinfectants). Over the year, the company has regularly launched new products as well as expanded its geographical presence in Nepal through its subsidiary Hester Biosciences Nepal Private Limited (HBNPL) which is engaged in the manufacturing of animal vaccines mainly PPR (Peste Des Petits Ruminants) and Goat pox vaccines of Nigerian strain, the production of which is banned in India. Moreover, HBL is strategically shifting its focus on large animal division and healthcare products rather than depending solely on poultry vaccines segment in order to leverage the business benefits of a diversified product portfolio and strengthening value addition. During FY18, HBL has acquired 54.80% stake in Texas laboratories, engaged in manufacturing of pharma formulations, tablets, capsules, powder and oral liquid and subsequently converted into private limited company namely, Texas Lifesciences Private Limited (TLPL).

Established marketing and distribution network: The marketing function of HBL is supported by six own warehouses, three C&F agents and strong network of distributors which has pan India presence. With the government's initiative to

¹Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.

control the diseases of animals & poultry, it decided to increase the level of scientific diagnosis. In this direction, HBL has developed a diagnostic laboratory division for animals to diagnose the diseases at an early stage thereby representing a backward integration of its business model of vaccines development. Moreover, The Company is also in process of creating distribution network in Africa and has established Hester Biosciences Kenya Limited and Hester Biosciences Tanzania Limited as distribution companies in Kenya and in Tanzania respectively.

Consistent growth in total operating income with healthy profitability: The total operating income of HBL at a consolidated level reported a Y-o-Y growth rate of 10% during FY18 on the back of increase in the sales volumes supported by increased penetration of products in the domestic markets. However, export revenue has declined due to delay in regulatory approval and slow flow of tenders. During FY18, the PBILDT margin also improved by 138 bps over FY17 backed by cost optimisation and change in product mix. However, the PAT margin declined due to higher interest and depreciation cost on the back of commencement of capacity expansion capex.

Comfortable capital structure and debt coverage indicators: The capital structure marked by overall gearing ratio at a consolidated level has witnessed improving trend for the past three years ended FY18 backed by continuous accretion of profit to the reserves. It remained at 0.48 times as on March 31, 2018 backed by strong capital base of Rs.144 crore. The debt coverage indicators i.e. total debt to GCA and Interest coverage remained comfortable at 2.02 years and 11.77 times respectively during FY18.

Liquidity analysis: Despite elongated operating cycle of 216 days, the liquidity profile of the company remains adequate with current ratio of 1.80 times as on March 31, 2018 and average fund based working capital utilizations at 43% for past trailing 12 months ended October 2018. Moreover, liquidity is supported by healthy cash accruals from operating activities during FY18. Further, HBL had unencumbered cash and bank balance of Rs.13.08 crore as on March 31, 2018.

Large opportunity in the animal healthcare market: Food and Agriculture Organization (FAO) of the United Nation (UN), and OIE (World Organization for Animal Health) have embarked on a worldwide PPR disease eradication program over a period of 15 years, starting in 2015. This PPR eradication project will induce a high demand for the PPR vaccine thereby growing the PPR vaccine market by leaps and bounds. HBL through its manufacturing set-up in Nepal is engaged in manufacturing of PPR and Goat pox vaccines of Nigerian strain, thereby provides opportunity to grow.

Key Rating weakness

Lower than envisaged production and sales volumes from Nepal operations: During November 2016, HBNPL commenced its operations in Kathmandu, Nepal to manufacture PPR and goat pox vaccines of Nigerian strain with an installed capacity of 1.2 billion doses per annum. For the year ended March 31, 2018, HBNPL reported total operating income of Rs.1.48 crore with net loss of Rs.7.36 crore owing to higher depreciation charges on the back of recently completed capital expenditure. Lower revenue from operation is due to delay in regulatory approval and slow flow of tenders. Though, there is a sign of improvement during H1FY19 where the Nepal operation has earned a total operating income of Rs.1.48 crore and net loss of Rs.4.45 crore. Therefore, stabilization of the Nepal operations in order to achieve the envisaged scale of operations would remain crucial from the credit perspective.

Modest and working capital intensive nature of operation: Despite consistent growth in total operating income, the scale of operation of the company remained modest marked by total operating income of Rs.136 crore during FY18 and tangible net-worth of Rs.144 crore as on March 31, 2018 on a consolidated basis. Further, the operations of HBL remained working capital intensive with high inventory requirements considering the nature of its products. High Inventory days is largely due to the manufacturing process of the product being manufactured by HBL which requires average two-three months of work in progress for various stage of product development for the formulation, processing, stimulations and quality check, etc.

Implementation and salability risk associated with large size capital expenditure in Africa: During FY18, HBL has incorporated wholly owned subsidiary, Hester Biosciences Africa Limited (HBAL). HBAL is setting up a green filed project for animal vaccine manufacturing in Tanzania with capacity to produce 1.5 billion doses of vaccines. Total cost of project is \$18 million (approximately Rs.125 crore) which is being funded by HBL in form of equity capital of \$4 million and through capital grant of \$4 million and soft loan of \$10 million from Bill & Melinda Gates foundation. Manufacturing facility of HBAL is being constructed on lease land acquired from Government of Tanzania. The project is expected to commission from December 2020 (i.e. FY21). The size of the capex is relatively large compared to the present operation of the company and the timely implementation without any major time and cost overrun and subsequent early stabilization remains critical from the credit perspective.

Presence in regulated industry and risk related to poultry industry: The vaccine industry has very high entry barriers and is a highly regulated market in terms of intellectual property rights (IPR) and other regulatory requirements. Further, the

poultry industry is exposed to the risks of outbreaks of diseases, which in turn, could affect the poultry vaccine industry. Such instances cause a severe reduction in the consumption of poultry products besides causing a cascading effect on the profitability of poultry companies.

Analytical Approach: Consolidated; CARE has considered the consolidated financials of Hester Biosciences Limited (HBL) along with its subsidiaries namely Hester Biosciences Nepal Private Limited (HBNPL; 65% equity Stake by HBL), Hester Biosciences Africa Limited (HBAL; wholly owned subsidiary of HBL) and Texas Lifesciences Private Limited (TLPL; 54.80% equity Stake by HBL) as per the audited financial result for the year ended March 31, 2018. These companies are engaged in similar line of business and are the extension of HBL in different geographies. They also have cash flow fungibility and operate under common management platform.

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 Companies](#)

[Financial ratios – Non-Financial Sector](#)

About the Company

Incorporated in the year 1987, HBL was promoted by Mr. Rajiv Gandhi as a private limited company and subsequently converted into a public limited company in 1993. HBL is one of India's leading animal healthcare companies engaged into manufacturing of vaccine and healthcare products mainly for poultry apart from sheep, goats, cattle and buffalo. The manufacturing facility is located at Kadi in Mehsana district of Gujarat with installed capacity of 4.8 billion doses per annum as on March 31, 2018.

(Rs. Crore)

Brief Financials of HBL (Consolidated)	FY17 (Audited)	FY18 (Audited)
Total operating income	123.28	136.19
PBILDT	41.31	47.52
PAT	22.79	23.07
Overall gearing (times)	0.53	0.48
PBILDT Interest coverage (times)	11.81	11.77

- On a standalone basis, during H1FY19 (Un-audited), HBL has reported a net profit of Rs.19.62 crore on total operating income of Rs.81.86 crore as against Rs.15.04 crore and Rs.68.70 crore during H1FY18 respectively.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

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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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/ ST-Cash Credit	-	-	-	30.00	CARE A-; Stable / CARE A2
Fund-based - LT-Term Loan	-	-	September 2023	20.82	CARE A-; Stable
Fund-based - ST-Working Capital Demand loan	-	-	-	28.75	CARE A2
Non-fund-based - ST-Credit Exposure Limit	-	-	-	0.22	CARE A2

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 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Fund-based - LT-Term Loan	LT	-	-	-	1)Withdrawn (03-Jan-18)	1)CARE A-; Stable (24-Jan-17)	1)CARE BBB+ (21-Mar-16)
2.	Fund-based - LT/ ST-Cash Credit	LT/ST	30.00	CARE A-; Stable / CARE A2	-	1)CARE A-; Stable / CARE A2 (03-Jan-18)	1)CARE A-; Stable / CARE A2 (24-Jan-17)	1)CARE BBB+ / CARE A3+ (21-Mar-16)
3.	Fund-based - LT-Term Loan	LT	20.82	CARE A-; Stable	-	1)CARE A-; Stable (03-Jan-18)	1)CARE A-; Stable (24-Jan-17)	1)CARE BBB+ (21-Mar-16)
4.	Fund-based - ST-Working Capital Demand loan	ST	28.75	CARE A2	-	-	-	-
5.	Non-fund-based - ST-Credit Exposure Limit	ST	0.22	CARE A2	-	-	-	-

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