

Ipca Laboratories Limited

April 26, 2017

Ratings

Facilities	Amount (Rs. crore)	Rating ¹	Rating Action
Long-term/Short-term Bank Facilities (Fund-based/ Non-fund-based)	1190.00	CARE AA; Stable/ CARE A1+ [Double A; Outlook: Stable/ A One Plus]	Assigned
Total Facilities	1190.00 (Rupees One Thousand One Hundred and Ninety crore only)		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Ipca Laboratories Limited (Ipca) derive strength from the proven track record of more than six decades and experienced promoters, global presence and dominant market position in anti-malarial and pain management drugs in the domestic pharmaceutical industry, strong and diversified product portfolio with backward integrated and diversified operations.

The ratings also positively factor the continuous product development in terms of Research and Development and improvement in operational performance during 9MFY17 [refers to period from April 1 to December 31]. Ipca has also consistently exhibited a strong financial risk profile with comfortable capital structure and liquidity profile.

However, the ratings strengths are partially tempered by the import alert levied by United States Food and Drug Administration (USFDA) on three of the manufacturing facilities and suspension of direct funding of anti-malarials by the Global Fund impacting the overall scale of operations and operating profitability of the company adversely. Additionally, the ratings also factor the long inventory holding period and Ipca's exposure to regulatory and foreign exchange fluctuation risk.

Ability of the company to improve the operating profitability margins and working capital cycle amidst the regulatory changes and foreign currency fluctuations would be the key rating sensitivities. Also any significant delay in withdrawal of the import alert by USFDA would be a key rating monitorable.

Detailed description of the key rating drivers

Key Rating Strengths

Well-established brand with global presence and growing market position

During FY16, Ipca had a growing market share for branded generic products in India with market leadership in Anti-malarial, pain and rheumatoid arthritis drugs. During FY16, the domestic formulations business recorded a growth of 7% at Rs.1206.70 crore as against Rs.1128.73 crore in the previous year. During FY16, the active pharmaceutical ingredients (APIs) and Intermediates business recorded sales of Rs.647.33 crore as against Rs.691.97 crore in FY15. Nearly 78% of the APIs and Intermediates business is from exports. The company exports its APIs across the globe. Most of the international customers of the company are end user formulations manufacturers including several multinational companies.

Geographical as well as product diversification

The products of Ipca are exported to over 100 countries across the globe. During FY16 the international business amounted to Rs.1428.72 crore as against Rs.1752.86 crore in the previous year (FY15). Formulation exports of Ipca decreased by 26% to Rs.922.05 crore and exports of APIs and Drug Intermediates decreased by 1% to Rs.506.67 crore on account of idle capacities at the three facilities under USFDA import alert and the suspension of export of antimalarial drugs directly funded by the Global Fund. During FY16, Ipca's sales in Europe and Africa reduced by 15% and 37% respectively, while the sales grew by 7% in Australia and Asia.

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

Improvement in operational performance during 9MFY17

Although the total operating income of the company declined to Rs.2927.78 crore in FY16 as compared to Rs.3176.92 crore in FY15, it continued to remain at a moderate level. During FY16, Profit Before Interest Lease Depreciation and Tax (PBDILT) amounted to Rs.311.45 crore as against Rs.556.07 crore in FY15. PAT margin declined from 8.00% in FY15 to 3.19% in FY16. Nevertheless, the material cost to sales ratios improved from 36% in FY15 to 33% in FY16. Further, the operational performance improved during 9MFY17 on a standalone basis and total income increased from Rs.2188.78 crore during 9MFY16 to Rs.2453.95 crore during 9MFY17 (12% increase) due to stabilization of currencies and higher sales in pain and dermatology segments in domestic as well as export markets and is expected to improve further from FY18 onwards on account of consolidation of branded generic exports and increase in demand from Russia, Asia and Africa.

Strong financial risk profile with a comfortable liquidity position albeit working capital intensive nature of operations

During FY16, the internal accruals of the company majorly funded increase in fixed assets and working capital operations. The overall gearing ratio of the company decreased to 0.40 times as on March 31, 2016, as compared to 0.59 times as on March 31, 2015 due to a decrease in total debt on account of redemption of NCDs and lower utilization of working capital bank borrowings. There is a reduction in interest coverage ratio to 9.06 times in FY16 (17.45 in FY15) on account of low profitability while total debt/GCA increased to 3.41 times as on March 31, 2016 (2.72 times as on March 31, 2015) on account of lower profits and depreciation.

The collection period continued to remain at a moderate level during FY16 at 68 days as compared to 76 days during FY15. The inventory period continued to remain stretched at 130 days in FY16 as compared to 136 days during FY15. Though the company had significant repayment obligations in the near term, the net debt of the company was approximately Rs.700 crore and Ipca maintains cash reserves of Rs.100 crore and above as a cushion for debt repayment at all times.

Key Rating Weaknesses

Import Alert by USFDA

In January 2016 Ipca received warning letters from the USFDA for three facilities which were already under an import alert for not adhering to good manufacturing norms. The USFDA had imposed import alert on three of Ipca's facilities on account of procedural lapses while no deviation notices were issued in terms of quality of products and no products were required to be recalled. The company had voluntarily suspended shipments of its APIs and formulations for the US market. The company has since taken remedial measures and has proposed to invite the USFDA for inspections in FY18. While the three facilities are under import alert by the USFDA, its Ratlam API plant has undergone inspection by the WHO (twice), formulation plant at Silvassa is inspected by Health Canada and EU Authorities and formulation plant at Pitampur, Indore has successfully been inspected by UK MHRA.

Suspension of Global Fund, Geneva direct funded anti-malarial Programme

In April 2016, the Global Fund, Geneva which is responsible for providing financial aid to various diseases suspended its direct funding to source anti-malarial drugs from Ipca on account of warning letters being issued by USFDA to the company. The Global Fund used to source Artemisinin based Combination Therapy (ACTs) drugs from the company. Ipca has since taken remedial measures to correct procedural lapses. Although the USFDA has issued import alert to three facilities of the company, sales from the US contributed approximately Rs.200 crore (less than 10% of turnover) to the total sales of the company in FY14-FY15 before the import alert was issued. Lifting of USFDA Alert and the reinstatement of the anti-malarial business direct funding by Global Fund are the key rating monitorables.

Heightening of regulatory risks

The Indian pharmaceutical industry, being one of the exporters to the UK has seen the aftermath of Brexit, albeit very limited, due to modified supply chain requirements, uncertain regulatory scenario, revised intellectual property laws, and depreciating currency. However, Pharmaceutical R&D and clinical trials set up have got a boost as the UK is looking for more economical collaborators in the absence of huge funding which the UK was receiving from the EU. The Brexit impact on pharma industry is expected to cause companies to face issues in regulatory and approval process going forward. The company has seen a reduction of 14-15% in overall realizations from UK post Brexit due to currency fluctuation. Profit margins in UK business being high may cause some changes in contracts and may impact company's profit margins but the impact is not expected to be significant. Ipca's profit margins were impacted by the drug price averaging under the regulations by the NPPA from FY14-FY16. As such, the company would continue to be exposed to regulatory risk.

Analytical approach:

CARE has analysed Ipca's credit profile by considering the consolidated financial statements of the company owing to financial and operational linkages between the parent and subsidiaries.

Applicable Criteria

[Criteria on assigning Outlook to Credit Ratings](#)

[CARE's Policy on Default Recognition](#)

[CARE's Methodology for Short Term Ratings](#)

[Rating Methodology: Factoring Linkages in Ratings](#)

[Rating Methodology-Manufacturing Companies](#)

[Rating Methodology-Pharmaceutical Sector](#)

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

About the Company

Ipca Laboratories Limited (Ipca) (CIN: L24239MH1949PLC007837) was founded by a group of businessmen and medical professionals in 1949. In 1975, Mr. P. C. Godha became a part of the management of the company. It is a fully integrated Indian pharmaceutical company manufacturing over 350 formulations and 80 active pharmaceutical ingredients (APIs) for various therapeutic segments. It manufactures formulations, APIs and drug intermediates. It produces formulations that include oral liquids, tablets, dry powders, and capsules. Its product range includes antimalarial, pain management, antiemetic, antibiotic, analgesic, antidiabetic and cardiovascular medicines and formulations for cough and cold therapy, skin problems, and problems with the central nervous system. The company is one of India's largest suppliers of bulk drugs, such as atenolol (antihypertensive), chloroquine and artemisinin derivatives (antimalarial), furosemide (diuretic), and pyrantel salts (anthelmintic).

The company's manufacturing facilities have approvals from all the major regulators including India's Central Drugs Standard Control Organisation, USA's Food and Drug Administration (FDA), UK's Medicines and Healthcare Products Regulatory Agency (MHRA), World Health Organisation (WHO), European Directorate for the Quality of Medicines (EDQM), South Africa's Medicines Control Council (MCC) and Brazil's National Health Vigilance Agency (ANVISA) and Australia's Therapeutic Goods Administration (TGA). Ipca's top 10 brands are Zerodol (Aceclofenac + combinations), Lariago (Chloroquine), HCQS (Hydroxychloroquine), Perinorm (Metoclopramide), Rapither (Artemotil), Tenoric (Atenolol + Chlorthalidone), Lumerax (Artemether + Lumefantrine), Etova (Etodolac), Malirid (Primaquine) and Folitrax (Methotrexate). Ipca's international client roster includes global pharmaceutical giants.

At a consolidated level, the profit after tax (PAT) of Ipca stood Rs.93 crore on total operating income of Rs.2,928 crore in FY16 vis-à-vis PAT of Rs.254 crore on total operating income of Rs.3,177 crore in FY15. Also, in 9MFY17 (Standalone - Unaudited), Ipca's PAT stood at Rs.144 crore on a total operating income of Rs.2,454 crore vis-à-vis PAT of Rs.60 crore on a total operating income of Rs.2,189 crore in 9MFY16 (unaudited).

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

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In case of partnership/proprietary concerns, the rating /outlook assigned by CARE is based on the capital deployed by the partners/proprietor and the financial strength of the firm at present. The rating/outlook may undergo change in case of withdrawal of capital or the unsecured loans brought in by the partners/proprietor in addition to the financial performance and other relevant factors.

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/Non-fund-based-LT/ST	-	-	-	1190.00	CARE AA; Stable / CARE A1+

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 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016	Date(s) & Rating(s) assigned in 2014-2015
1.	Fund-based/Non-fund-based-LT/ST	LT/ST	1190.00	CARE AA; Stable / CARE A1+	-	-	-	-

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