Neuland Laboratories Limited

April 11, 2017

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long-term Bank Facilities	240.08 (reduced from 255.27)	**CARE BBB+; Stable [Triple B Plus; Outlook: Stable]**	Revised from CARE BBB [Triple B]
Short-term Bank Facilities	114.00	**CARE A3+ [A Three Plus]**	Reaffirmed
Total Facilities	**354.48 (Rupees Three Hundred Fifty Four crore and Forty Eight lakh only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision in the long-term ratings assigned to the bank facilities of the Neuland Laboratories Limited (NLL) derive strengths from healthly growth in the financial performance during FY16 (refers to the period April 1 to March 31) and 9MFY17 , cognizance of strengths from experienced promoters having long-term presence in the pharma industry, diversified revenue and customer profile, improvement in capital structure and debt protection metrics and moderate product mix with rise in the share of high margin products. The ratings however are constrained by the absence of the long term contracts with clients, exposure to foreign exchange fluctuation risk, elongated operating cycle and highly competitive nature of industry. The ability of the company to complete the ongoing process of merger successfully with its parent and an associate companies, continue to expand the scale of operation, along with improvement in the profit margins and manage working capital requirement efficiently while maintaining healthy liquidity position are the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Improved operating income and profitability margins in FY16 and 9MFY17

Total operating income of the company has witnessed growth of 8.78% in FY16 over FY15. Growth in income is backed by increase in sales of APIs and Custom Manufacturing Solutions (CMS) business during the year. Furthermore, optimized product mix with higher contribution from CMS and niche molecule business has resulted in improved PBILDT margin by 150 bps in FY16 and PAT margin by 181 bps in FY16.

Furthermore, during 9MFY17, the company has achieved 15% growth (y-o-y) in total operating income with PAT margin of 5.53%.

Comfortable capital structure and debt risk metrics

NLL has comfortable capital structure as on March 31, 2016. Improved leverage position of NLL was on account of lower utilization of bank borrowings and accretion of higher profits to reserves. Furthermore, debt protection metrics (term debt/GCA and Total debt/GCA) have also remained comfortable in FY16. Furthermore, as on December 31, 2016, also the company had comfortable debt to equity and overall gearing below unity.

Diversified revenue and client profile

NLL has portfolio of 75 products (particularly APIs) with presence across 10 therapeutic segments. The revenue steam is well diversified with top 5 products contributing 50.86% and top 5 clients accounting 33.28% of the net sales in FY16. The company has diversified clientele and enjoys dependable relationships with major global and Indian Pharma majors.

Benefits expected from proposed merger of NLL with parent and an associate company

NLL is in process of merger with NHSPL and NPRPL resulting in merged entity as NLL. As per the new shareholding pattern, the promoters would have 41% stake followed by 38% stake of public and balance 20% would be held by others. Post merger, NLL would have enhanced financial strength marked by increased scale of operation, improved profit levels and profitability margins, improved liquidity profile and capital structure.

Key Rating Weakness

Elongated operating cycle period

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

NLL has stretched operating cycle of 111 days in FY16 from 107 days in FY15. Elongated operating cycle is primarily due to high inventory holding period of 107 days in FY16 as NLL is in phase of widening its product portfolio for which the company has to maintain adequate inventory stocks to support the operations.

Foreign Exchange fluctuation risk

NLL remains exposed to susceptibility of profitability margins with volatility in foreign exchange rate with around 76% of the revenue streamed from exports however the company ensures risk coverage of around 70% of the total exposure.

Exposure to regulatory risk and highly fragmented industry

The Indian pharmaceuticals market is third largest in terms of volume and thirteen largest in terms of value, as per a pharmaceuticals sector analysis report by equity master. The market is dominated majorly by branded generics which constitute nearly 70 to 80% of the market. Furthermore, the company is exposed to regulatory risk with its operations centered majorly into manufacturing pharmaceutical formulations along with APIs. In India, the government also controls the prices of pharmaceutical products however industry is highly regulated in many other countries and requires various approvals, licenses, registrations and permissions for business activities.

Analytical approach: Consolidated. The consolidated financial statements of NLL accompany financials of NHSPL and NPRPL.

Applicable Criteria

- Criteria on assigning Outlook to Credit Ratings
- CARE's Policy on Default Recognition
- Criteria for Short Term Instruments
- Rating Methodology-Manufacturing Companies
- Financial ratios – Non-Financial Sector
- Rating Methodology- Pharmaceutical Sector

About the Company

Incorporated in January 1984, NLL was set up as a private limited company by Dr D R Rao and Mr G V K Rama Rao and was reconstituted as a public limited company, with the current nomenclature, in 1994. NLL manufactures active pharmaceutical ingredients for global pharmaceutical companies and provides end-to-end solutions for the pharmaceutical industry for chemistry-related services. It supplies to pharmaceutical companies across India, Europe and North America amongst others with a presence in over 85 countries. NLL has two manufacturing facilities in Hyderabad, Telangana. The manufacturing facilities are compliant with health and regulatory agencies cGMP certifications, namely, Food and Drug Administration (USA), Health Canada (Canada), Pharmaceutical and Medical Devices Agency (Japan), Korea Food and Drug Administration (Korea), European Medicines Agency (European Union), European Directorate for the Quality of Medicines (Certificate of Suitability) and others (Rest of World). The company has a portfolio of around 75 Products with presence in 10 therapeutic segments viz. anti-asthmatic, anti-infective, anti-ulcerants, anti-fungals, cardiovascular, flouroquinolones, central nervous system (CNS) and anti-diabetic. NLL is listed on BSE Limited and National Stock Exchange (NSE).

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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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.

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
Term Loan-Long Term	-	-	January 2019	40.08	CARE BBB+; Stable
Fund-based - LT-Working Capital Limits	-	-	-	200.00	CARE BBB+; Stable
Non-fund-based - ST-BG/LC	-	-	-	108.00	CARE A3+
Non-fund-based - ST-Forward Contract	-	-	-	6.40	CARE A3+

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.	Term Loan-Long Term	LT	40.08	CARE BBB+; Stable	-	1)CARE BBB (26-Aug-16) 2)CARE BBB- (29-Apr-16)	1)CARE BBB- (16-Sep-15) 2)CARE BBB- (07-Aug-15)	1)CARE BBB- (04-Jul-14)
2.	Fund-based - LT-Working Capital Limits	LT	200.00	CARE BBB+; Stable	-	1)CARE BBB (26-Aug-16) 2)CARE BBB- (29-Apr-16)	1)CARE BBB- (16-Sep-15) 2)CARE BBB- (07-Aug-15)	1)CARE BBB- (04-Jul-14)
3.	Non-fund-based - ST-BG/LC	ST	108.00	CARE A3+	-	1)CARE A3+ (26-Aug-16) 2)CARE A3 (29-Apr-16)	1)CARE A3 (16-Sep-15) 2)CARE A3 (07-Aug-15)	1)CARE A3 (04-Jul-14)
4.	Non-fund-based - ST-Forward Contract	ST	6.40	CARE A3+	-	1)CARE A3+ (26-Aug-16) 2)CARE A3 (29-Apr-16)	1)CARE A3 (16-Sep-15) 2)CARE A3 (07-Aug-15)	1)CARE A3 (04-Jul-14)

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