SMS Pharmaceuticals Limited

October 4, 2018

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long term Bank Facilities	174.25	**CARE A-; Stable (Single A Minus; Outlook: Stable)**	Reaffirmed
Short term Bank Facilities	50.83	**CARE A2 (A Two)**	Reaffirmed
Total	**225.08 Rs. Two hundred and twenty five crore and eight lakh only)**		

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of SMS Pharmaceuticals Limited (SMS) continue to derive strength from experienced promoters with established track record of the company in pharmaceutical industry, presence of regulatory approvals with well-equipped manufacturing facilities with the United States Food & Drug Administration (USFDA) and current Good Manufacturing practices (cGMP) certified production units, stable order book position with reputed customers, satisfactory working capital cycle with improved collection period and favorable industry outlook. The ratings also takes into account increase in revenue with improved profitability margins during FY18 (refers to the period April 01 to March 31) and Q1FY19 (Q1 refers to April 1 to June 30), improved capital structure as on March 31, 2018 and debt coverage indicators. The ratings are, however, tempered by continued sales concentration risk in terms of client as well as therapeutic segment and product, risk on account of exposure towards associate company, foreign exchange fluctuation risk and regulatory risk with respect to the pharmaceutical industry.

The ability of the company to enhance the scale of operation by diversifying the product base along with increased presence in therapeutic segments and manage forex exchange fluctuation risk are the key rating sensitivities. Further, getting approval for the products patents filed will be critical from the credit perspective.

Detailed description of the key rating drivers

Key Rating Strengths

Increase in revenue with improved profitability margins during FY18: The Total Operating Income (TOI) of SMS increased by 6% to Rs. 463.78 crore in FY18 vis-à-vis FY17. PBILDT level and margin improved by 25% and 316 bps to Rs.94.48 crore (Rs.75.53 crore in FY17) and 20.37% (17.21% in FY17) during FY18 respectively post demerger. By dint of demerger SMS is able to focus on regulated markets where margins are higher which has resulted in improved margins.

Improved capital structure: The overall gearing level of SMS further improved to 0.50x as on March 31, 2018 as against 0.57x as on March 31, 2017 on account of improved networth coupled with decrease in debt levels during FY18 at the back of repayment of term debt along. Total debt/GCA further improved to 2.22x during FY18 (2.89x for FY17) on account of improved GCA coupled with decrease in debt level at the back of repayment of debt.

Experienced promoters with established track record of operations: The promoters have over 29 years of experience in the pharmaceutical industry. Under the present management, SMS has remaining two regulated facilities (Unit I-Bachupally, Telangana (Erstwhile Unit II) and Unit II- Vizianagaram, Andhra Pradesh (erstwhile unit VII)) and the one R&D facility post demerger.

Presence of regulatory approvals: All the units meet World Health Organization (WHO) cGMP standards and also have various certifications. Unit I and Unit II has US FDA approval along with other approvals.

Stable order book position with reputed customers: SMS had total order book of around Rs.338.79 crore to be executed for clients which are associated with the company for more than a decade.

Satisfactory working capital cycle with improved collection period: The operating cycle of SMS was satisfactory at 63 days during FY18 (60 days during FY17). The collection period of the company improved to 16 days (33 days in FY17) on account of timely collections.

Favorable industry outlook: The outlook of the pharma industry is favorable in light of healthy prospects for the domestic as well as the export markets. Exports to regulated markets along with emerging markets would drive the growth for Indian Pharmaceutical Industry (IPI) on the back of patent expiries and increasing government emphasis on generics in these markets.

2Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.

Key Rating Weaknesses

Continued sales concentration: The revenue of the company remains concentrated wherein the top 6 clients contributing around 87% to the revenue in FY18 with 75% revenue contribution from Contract Manufacturing(CRAM). Further, major revenue share is constitutes from Anti-retroviral therapeutic segment which accounts for 75% of total gross sales.
Risk on account of exposure to associate company: SMS has demonstrated support to wards VKT in the form of regular equity infusion in order to support the operation in the past. Going forward, any further exposure to its associate company will be critical from credit perspective.
Foreign exchange fluctuation risk and regulatory risk: SMS is exposed to forex risk as major revenue of the company comes from exports. The forex risk is partly mitigated by natural hedge through the imports. During the year FY18, SMS has earned net gain on foreign currency transaction and translations.

Analytical approach: Standalone

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
Rating Methodology: Factoring Linkages in Ratings

About the Company
SMS Pharmaceuticals Limited (SMS), a listed company, was originally started by Mr. K G Suggula in the year 1987 as a private limited company and soon turned sick due to the lack of demand for the products being manufactured. The current promoters' Mr. P Ramesh Babu (Chairman and Managing Director) and Mr. TVVSN Murthy (Director) acquired the company in the year 1990. SMS is engaged in manufacturing of Active Pharmaceutical Ingredients (APIs) and its intermediates and also undertakes contract manufacturing for API/ bulk drugs. SMS has over the years set up manufacturing facilities to suit its operations and to meet various regulatory requirements. SMS demerged its semi-regulated units under Food and Drug Administration (FDA) (i.e. Unit I-Kazipally unit (erstwhile unit I of SMS) Unit II-Jeedimetla unit (erstwhile unit IV of SMS) and Unit III- Bollaram unit (erstwhile unit V of SMS) and one R&D facility along with other assets, liabilities and investments and transferred to SMS Lifesciences India Limited effective from May 17, 2017. Currently, SMS has remaining two regulated facilities (Unit I and Unit II) with both the units having U S Food and Drug Administration (USFDA) approval and 1 R&D facilities. Apart from USFDA approval, Unit I also has European regulatory approvals while Unit II has Korean Food and Drug Administration (KFDA) and Japan Pharmaceuticals and Medical Devices Agency (PMDA) approval and all units also meet World Health Organization (WHO) cGMP standards.
The company has presence in more than 9 therapeutic segments including Antiretroviral (ARV), Anti Migraine, Anti-Hypertensive Anti-Ulcerants, Anti Diabetic etc. SMS had an order book valued Rs.338.79 crore as on September 12, 2018. The company supplies to pharmaceutical companies across North America, Europe amongst others and has presence in over 70 countries across the globe.

Brief Financials (Rs. Crore)	FY17 (A)	FY18(A)
Total operating income	438.86	463.78
PBILDT	75.53	94.48
PAT	35.61	40.45
Overall gearing (times)	0.57	0.50
Interest coverage (times)	4.88	6.10

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

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
Fund-based - LT-Cash Credit	-	-	-	75.00	CARE A-; Stable
Fund-based - LT-Term Loan	-	-	September 2022	84.25	CARE A-; Stable
Fund-based - LT-Packing Credit in Foreign Currency	-	-	-	15.00	CARE A-; Stable
Non-fund-based - ST-Bank Guarantees	-	-	-	2.00	CARE A2
Non-fund-based - ST-Letter of credit	-	-	-	30.00	CARE A2
Fund-based - ST-Line of Credit	-	-	-	16.00	CARE A2
Non-fund-based - ST-Forward Contract	-	-	-	2.83	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-Cash Credit	LT	75.00	CARE A-; Stable	-	1)CARE A-; Stable (12-Sep-17)	1)CARE A- (Under Credit Watch) (12-Oct-16)	1)CARE A- (18-Sep-15)
2.	Non-fund-based - ST-Letter of credit	ST	30.00	CARE A2	-	1)CARE A2 (12-Sep-17)	1)CARE A2 (Under Credit Watch) (12-Oct-16)	1)CARE A2 (18-Sep-15)
3.	Fund-based - LT-Term Loan	LT	84.25	CARE A-; Stable	-	1)CARE A-; Stable (12-Sep-17)	1)CARE A- (Under Credit Watch) (12-Oct-16)	1)CARE A- (18-Sep-15)
4.	Fund-based - ST-Line of Credit	ST	16.00	CARE A2	-	1)CARE A2 (12-Sep-17)	1)CARE A2 (Under Credit Watch) (12-Oct-16)	1)CARE A2 (18-Sep-15)
5.	Fund-based - LT-Packing Credit in Foreign Currency	LT	15.00	CARE A-; Stable	-	1)CARE A-; Stable (12-Sep-17)	1)CARE A- (Under Credit Watch) (12-Oct-16)	1)CARE A- (18-Sep-15)
6.	Non-fund-based - ST-Bank Guarantees	ST	2.00	CARE A2	-	1)CARE A2 (12-Sep-17)	1)CARE A2 (Under Credit Watch) (12-Oct-16)	1)CARE A2 (18-Sep-15)
7.	Non-fund-based - ST-Forward Contract	ST	2.83	CARE A2	-	1)CARE A2 (12-Sep-17)	1)CARE A2 (Under Credit Watch) (12-Oct-16)	1)CARE A2 (18-Sep-15)

CARE Ratings
Professional Risk Opinion

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