Sunil Healthcare Limited

November 23, 2018

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long-term Bank Facilities (Fund Based)	28.00	CARE BBB-; Stable (Triple B Minus; Outlook: Stable)	Reaffirmed
Long-term Bank Facilities (Term Loan)	-	-	Withdrawn*
Short-term Bank Facilities	18.90	CARE A3 (A Three)	Reaffirmed
Total Facilities	**46.90 (Rupees Forty Six crore and Ninety lakh only)**		

Details of instruments/facilities in Annexure-1

**CARE has withdrawn the rating assigned to the term loan facility of Sunil Healthcare Limited, with immediate effect since there is no amount outstanding under the facility*

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Sunil Healthcare Limited (SHL) continue to derive strength from the long track record of operations with a highly experienced management team and comfortable PBILDT margins. The ratings further derive strength from its satisfactory overall solvency position, wide product profile & revenue stream with established brand name.

The ratings are, however, constrained by the weakening of the financial risk profile and customer concentration risk in FY18 (Audited; refers to April 01 to March 31) along with decline in scale of operations and lower profitability at net level in H1FY19 (Unaudited), small scale, inherent commodity price risk associated with the trading operation along with susceptibility of profitability margins to raw material price & foreign currency fluctuations and regulatory policy risk in a competitive pharmaceutical industry with increasing pricing pressure.

Going forward, the ability of the company to profitably scale-up its operations, manage its working capital requirements efficiently and improve its overall solvency position will remain the key rating sensitivities. Furthermore, any new capex and funding mix for the same will also remain a key rating sensitivity.

Detailed description of the key rating drivers

Key Rating Strengths

Experienced promoters with long track record of operations: SHL is promoted by Mr. Anil Khaitan (Chairman and Managing Director) who has nearly four decades of industry experience and is involved in the overall business operations of the company. The directors of the company are assisted by a team of professionals who are highly experienced in their respective domains.

Comfortable PBILDT margins: The PBILDT margins of the company have remained comfortable in the past and improved in FY18 on a y-o-y basis to 17.16% from 15.74% in FY17 on account of better cost controls and improved efficiencies in the system on account of regular cap-ex undertaken by the company and decline in income realized from the trading segment which is associated with lower margins.

Established brand name: SHL is the second largest EHGC (Empty Hard Gelatin Capsules) shell manufacturer in the domestic market with installed capacity of 13 billion shells per annum, as on March 31, 2018. The company sells its products under the brand name, 'Sunloc'.

Wide product profile & revenue stream: The company's product profile is well diversified with production of double lock, triple lock, multiple groove capsules, HPMC (Hydroxy Propyl Methyl Cellulose) capsules along with liner, circular, two colour printing & 360 degree printing being offered. The company has further diversified its revenue stream by starting trading of food products including raw cashew nuts, dehydrated vegetables, Almonds, pistachio, cardamom, etc., under brand 'Sunloc foods'.

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

Key Rating Weaknesses

Deterioration in the financial risk profile along with customer concentration risk: The scale of operations of the company continued to remain at a small level and declined by ~12% in FY18 on account of lower income achieved from both; the trading segment [which declined by ~60% on a year-on-year (y-o-y) basis] and the Empty Hard Gelatin Capsule (EHGC) shell segment [declined by ~1% on a y-o-y basis]. The decline in income in the EHGC segment was on account of stricter norms imposed by the FDA (Food and Drug Administration) coupled with price controls in domestic market, which led to lower overall industry demand in an already competitive industry. During FY18, the proportion of income derived from top-5 clients also increased to ~46% of the total operating income from ~28% in FY17, thereby exposing the company to customer concentration risk. Top 2 clients contributed ~23% of the total operating income. Any change in the procurement policy of these customers may adversely impact the business of the company.

The capital structure of the company also weakened on a y-o-y basis with long-term debt to equity and overall gearing ratios of 0.45x and 1.34x, respectively, as on March 31, 2018 (PY: 0.39x and 1.19x, respectively). The deterioration was on account of new term loans availed by the company for capex to increase its manufacturing capacities in FY18 and higher reliance on the working capital borrowings. Further, the debt coverage indicators of the company also deteriorated on a y-o-y basis with total debt to GCA of 6.15x, as on March 31, 2018 (PY: 4.86x) and interest coverage ratio of 3.08x in FY18 (PY: 3.88x). The overall solvency position, however, continued to remain at a satisfactory level, in FY18.

In H1FY19 (UA), the scale of operations of the company declined by ~9% on a year-on-year (y-o-y) basis compared to corresponding period last year due to absence of any income from the trading segment. Though the PBILDT margins during the period remained at almost the similar level (16.74% compared to 16.7% in the same period last year), the PAT margins declined significantly (from 4.5% in H1FY18 to 1.77% in H1FY19) on account of decline in PBILDT in absolute value terms and increase in the interest and depreciation expenses during the period. The overall gearing ratio stood at 1.4x, as on September 30, 2018, while the interest coverage ratio stood at 2.25x in H1FY19.

Weakening of the liquidity profile: The operating cycle of the company elongated to 136 days, as on March 31, 2018 from 95 days, as on March 31, 2017 on account of elongation of the average collection days. Higher credit period was offered to the customers to sustain the sales. The average working capital limit utilization also stood at a high level of ~95% in the last 12 months ended September, 2018. The company has a total debt repayment obligation of Rs. 5.87 cr. in FY19, proposed to be met through the internal accruals. As on March 31, 2018, SHL had free cash & liquid investments of Rs. 0.65 Cr. The current and quick ratios continued to remain weak at 0.97x and 0.82x, respectively (Previous Year: 0.97x and 0.79x, respectively).

Exposure to raw material price volatility and foreign currency fluctuations risk: The raw materials, primarily gelatin, colour & chemical compounds, are obtained from both domestic and foreign suppliers. Due to competitive nature of industry, the company is not always able to pass on any increase in costs to its customers, thus, the profitability margins are exposed to any adverse fluctuation in raw material prices.

The foreign currency exposure of SHL is hedged to an extent as the company is engaged in both import of raw material and exports of its products. The company also enters into derivative contacts to hedge some part of its unhedged portion. The remaining portion, however, remains unhedged thereby exposing the profitability margins to adverse fluctuations in foreign exchange rates. Additionally, the company supplies to several countries located in the African continent. Thus, the company is also exposed to unfavorable changes in the government policy of respective African nations.

Highly fragmented and competitive nature of industry: SHL is engaged in the manufacturing of capsule shells which is raw material (excipient) for pharmaceutical and food supplement industry. The industry is characterized by a high level of competition having presence of a large number of small and big players.

Regulatory risk: Pharmaceutical industry is a closely monitored and regulated industry and as such there are inherent risks and liabilities associated with the products and their manufacturing. Issues like price control of essential medicines by the Government of India through the Drug (Prices Control) Order, 2013, pose regulatory risk for the Pharmaceutical industry.

Inherent commodity price risk associated with its trading operation: SHL is engaged in the trading of agro commodities and their prices are linked to the demand supply scenario in the domestic and international market. The company is exposed to the vagaries of nature and fluctuations in the prices of major raw materials in case of demand supply mismatch. However, the company's sales are largely order backed which mitigates the risk of carrying commodity at a price.

Analytical Approach: Standalone

Applicable Criteria

[Criteria on assigning Outlook to Credit Ratings]

[Financial ratios – Non-Financial Sector]

CARE's policy on default recognition
CARE's methodology for manufacturing companies
CARE's methodology for Pharmaceutical sector
Criteria for Short Term Instruments

Company Background
SHL was incorporated in 1973 by Late Mr. S.N Khaitan, the father of Mr. Anil Khaitan, who is the present Chairman and Managing Director of the company. SHL was originally constituted as a closely held public limited company by the name of Sunil Synchem Limited, however, the same was changed in June-2005 to its current name.
SHL is mainly engaged in the manufacturing of Empty Hard Gelatin Capsule (EHGC) shells (~92% of income in FY18) with an installed capacity of manufacturing approximately 13 billion shells per annum, as on March 31, 2018 at its sole unit at Alwar, Rajasthan.
The company is also engaged in the trading (including merchant trading) of agro based commodities including raw cashew nuts, dehydrated vegetables, Almonds, pistachio, cardamom, etc. since 2013, under brand 'Sunloc foods'.

Brief Financials (Rs. crore)	FY17 (A)	FY18 (A)
Total operating income	103.08	90.30
PBILDT	16.23	15.49
PAT	5.62	5.32
Overall gearing (times)	1.19	1.34
Interest coverage (times)	3.88	3.08

A: Audited
Status of non-cooperation with previous CRA: NA

Any other information: NA

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-Cash Credit	-	-	-	25.00	CARE BBB-; Stable
Fund-based - LT-Stand by Limits	-	-	-	3.00	CARE BBB-; Stable
Non-fund-based - ST-BG/LC	-	-	-	14.65	CARE A3
Non-fund-based - ST-Forward Contract	-	-	-	0.60	CARE A3
Fund-based - LT-Term Loan	-	-	-	-	Withdrawn
Fund-based - ST-Standby Line of Credit	-	-	-	3.65	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 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	25.00	CARE BBB-; Stable	1)CARE BBB-; Stable (14-Nov-18)	1)CARE BBB; Stable (26-Dec-17) 2)CARE BBB; Stable (05-Oct-17)	-	-
2.	Fund-based - LT-Stand by Limits	LT	3.00	CARE BBB-; Stable	1)CARE BBB-; Stable (14-Nov-18)	1)CARE BBB; Stable (26-Dec-17) 2)CARE BBB; Stable (05-Oct-17)	-	-
3.	Non-fund-based - ST-BG/LC	ST	14.65	CARE A3	1)CARE A3 (14-Nov-18)	1)CARE A3+ (26-Dec-17) 2)CARE A3+ (05-Oct-17)	-	-
4.	Non-fund-based - ST-Forward Contract	ST	0.60	CARE A3	1)CARE A3 (14-Nov-18)	1)CARE A3+ (26-Dec-17) 2)CARE A3+ (05-Oct-17)	-	-
5.	Fund-based - LT-Term Loan	LT	-	-	1)CARE BBB-; Stable (14-Nov-18)	1)CARE BBB; Stable (26-Dec-17) 2)CARE BBB; Stable (05-Oct-17)	-	-
6.	Fund-based - ST-Standby Line of Credit	ST	3.65	CARE A3	1)CARE A3 (14-Nov-18)	1)CARE A3+ (26-Dec-17)	-	-

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