March 20, 2023

Sri Krishna Pharmaceuticals Ltd.: Ratings reaffirmed, rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Term loan	8.67	41.50	[ICRA]BBB+ (Stable); reaffirmed/assigned
Long-term – Fund-based working capital facilities	113.00	203.00	[ICRA]BBB+ (Stable); reaffirmed/assigned
Short-term – Non-fund based working capital facilities	34.00	15.00	[ICRA]A2; reaffirmed
Long-term/short-term - Non-fund based working capital facilities#	-	(94.00)	[ICRA]BBB+ (Stable)/ [ICRA]A2; assigned
Total	**155.67**	**259.50**	

**Instrument details are provided in Annexure-I; #Sub-limit of long-term – Fund-based working capital facilities*

Rationale

The ratings favourably factor in Sri Krishna Pharmaceuticals Ltd.'s (SKPL) long track record of operations as an established supplier of Paracetamol Active Pharmaceutical Ingredient (API) and Directly Compressible (DC) granules. The company has a wide presence in the domestic market and various export markets like the US, the EU, Latin America and West Asia, among others. SKPL has approvals from the regulatory authorities of key developed markets, including the US, Europe and Australia, among others, which support its operations. The ratings also factor in SKPL's diversified customer base, which it continues to expand. The company has a long track record of relationships with its key Chinese suppliers, though it remains dependent on them.

The ratings, however, factor in the pressure on SKPL's credit metrics over FY2022 and 9M FY2023, led by margin erosion on account of adverse movements in the price of the key raw material, para-amino phenol (PAP). While the volatility in the input prices was due to supply constraints in China, from where SKPL procures majority of PAP, the increase in the realisation of the end-product paracetamol has not been commensurate. Input prices have been volatile in the past, although there has been some stabilisation in H2 FY2023 supported by ease in supply side pressures, thereby expected to result in a sequential improvement in margins. SKPL's working capital intensity remains high owing to the need to maintain stock levels. Dependence on working capital debt and new debt for the ongoing capex in nutraceuticals are expected to increase leverage. With improvement in margins and returns from the new unit, SKPL's leverage and coverage metrics are expected to improve in the medium term. The ratings continue to factor in the current limited product diversification with high dependence on a few molecules (paracetamol and folic acid), which face intense competition in the market.

The Stable outlook on the rating reflects ICRA's opinion that SKPL will continue to benefit from its long and established market position in key product segments and stable demand outlook. Planned foray into nutraceutical also augurs well for long-term diversification.

Key rating drivers and their description

Credit strengths

Established presence in key product segments – SKPL has a demonstrated track record of four decades in the domestic paracetamol business and enjoys a strong market position. It is one of the largest producers of paracetamol in India, with an installed capacity of 12,000 MTPA. It is also one of the largest producers of food and pharma-grade folic acid in Asia. Further, SKPL's key facilities (except for the Nacharam unit in Hyderabad, which is yet to be approved by the USFDA) are approved by the regulatory authorities of key developed markets including the US, Europe and Australia, among others; lending comfort to the company's processes and systems. The company is setting up a nutraceutical unit, which is expected to be commissioned by the end of Q1 FY2024, which will aid revenue diversity, going forward.

Geographical and customer diversification – SKPL derived around 66% of its revenues from exports in 9M FY2023 across markets (up from 53% in FY2022). The company's sales are also diversified across customers, with the top-10 customers accounting for ~43% of sales in 9M FY2023. Over the years, it has developed relationships with leading domestic pharma majors, resulting in recurring orders from its customers. Although in 9M FY2023 around 31% of its total revenues came from Europe, which has been facing a slowdown, SKPL's presence across customers and geographies reduces the risks arising from region/customer specific demand concerns.

Credit challenges

Exposure to raw material price fluctuations – The company procures PAP, the primary raw material for paracetamol API, from three established players in China, which reflects an import dependence. However, ICRA notes that SKPL has made efforts to diversify its supplier base and started procuring PAP from Cambodia. PAP prices started increasing sharply from Q4 FY2021 and remained elevated till early FY2023 due to the supply constraints emanating from China. While paracetamol witnessed healthy demand in FY2021 and early FY2022 owing to the pandemic, the demand normalised subsequently, and paracetamol realisations did not increase in line with PAP prices. Significantly high PAP prices, thus, adversely impacted SKPL's contribution margins in FY2022 and H1 FY2023. While input prices are moderating in H2 FY2023 with reduction in supply-side concerns, SKPL's margins in FY2023 are expected to be weaker than anticipated. The company also remains exposed to foreign currency fluctuations to an extent.

Limited product diversification – SKPL's revenues remain dependent on its top two products, paracetamol and folic acid, which accounted for over 70% of its sales over the last five years. SKPL is working on reducing its concentration risk on paracetamol by focusing on folic acid, ibuprofen, furosemide and domperidone, going forward, along with foray into nutraceuticals.

Weakening of credit metrics in 9M FY2023, in line with expectations – SKPL's operating margins declined to 6.7% in FY2022 from 12.9% in FY2021 and further to 3.0% in 9M FY2023 (provisional). In FY2021, SKPL benefitted from high demand owing to Covid as well as favourable input prices. The cost structure started worsening from early FY2022 and continued till early FY2023. While the company witnessed a high revenue growth of 47% in FY2022 led by higher realisations, its dependence on working capital debt increased. In the current fiscal, even as the spread between PAP and paracetamol prices has been improving since September 2022, the impact on SKPL's margins will come with a lag and its leverage as reflected by Total Debt/OPBDITA will continue to be elevated. SKPL has availed term loans apart from internal accruals for its nutraceutical capex. The company's ability to improve and sustain its margins, given the volatile nature of input prices, is thus crucial to maintain comfortable coverage metrics.

High working capital intensity – SKPL's working capital intensity has remained high in the past fiscals at around 37% as the major raw material (PAP) is procured from Chinese suppliers through advance payments and higher inventory levels being maintained, given the increased lead times for supply post the pandemic-induced supply chain disruptions. However, the Chinese suppliers have started providing credit period in H2 FY2023, which augurs well for SKPL. In addition, SKPL has received limit enhancements to address its growing working capital requirements.

Liquidity position: Adequate

SKPL's liquidity is adequate. The company received enhancements in its fund-based limits and has been utilising them to an average of 81.5% over the 12-month period ended December 2022. The company has modest repayment obligations of Rs. 5.09 crore in FY2023, which would rise to Rs. 10.72 crore in FY2024. SKPL had modest free cash balances and available undrawn fund-based working capital limits of ~Rs. 32 crore as of December 2022.

Rating sensitivities

Positive factors – The ratings can be upgraded on the company's ability to improve its profitability, thereby leading to improvement in credit metrics on a sustained basis. A specific credit metric for an upgrade will be if TD/OPBITDA is less than 2.3 times, on a sustained basis.

Negative factors – Pressure on the ratings could arise, if there is a higher-than-expected weakening of the company's credit profile led by erosion of margins or sizeable debt-funded capex. A weakening in liquidity position of the company could also be a negative rating trigger.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology for Pharmaceutical Companies
Parent/Group support	Not Applicable
Consolidation/Standalone	Standalone

About the company

Sri Krishna Pharmaceuticals Ltd., promoted in 1974 by Dr. V. V. Subba Reddy and family, manufactures bulk drugs and directly compressible (DC) granules. At present, the company has five manufacturing units, including four based in and around Hyderabad (Uppal, Nacharam, Bollaram and Shamshabad) and one in Solapur, Maharashtra. SKPL's key products include Paracetamol API as well as formulations, folic acid and domperidone, accounting for more than 70% of its revenues in 9M FY2023.

Key financial indicators (audited)

SKPL Standalone	FY2021	FY2022	9M FY2023^
Operating income	595.7	875.7	671.3
PAT	44.2	35.2	6.9
OPBDITA/OI	12.9%	6.7%	3.0%
PAT/OI	7.4%	4.0%	1.2%
Total outside liabilities/Tangible net worth (times)	0.7	1.1	-
Total debt/OPBDITA (times)	1.3	3.4	-
Interest coverage (times)	20.6	9.7	3.3

PAT: Profit after tax; OPBDITA: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore; ^Provisional figures

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2023)					Chronology of rating history for the past 3 years			
		Type	Amount rated (Rs. crore)	Amount outstanding as of Dec 31, 2022 (Rs. crore)	Date & rating in FY2023		Date & rating in FY2022	Date & rating in FY2021		Date & rating in FY2020
					Mar 20, 2023	Oct 31, 2022	Jul 14, 2021	Dec 11, 2020	Oct 05, 2020	Nov 22. 2019
1	Term loans	Long-term	41.50	40.00	[ICRA]BBB + (Stable)	[ICRA]BBB + (Stable)	[ICRA]A- (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB + (Stable)	[ICRA]BBB (Stable)
2	Fund-based working capital facilities	Long-term	203.00	-	[ICRA]BBB + (Stable)	[ICRA]BBB + (Stable)	[ICRA]A- (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB + (Stable)	[ICRA]BBB (Stable)
3	Non-fund-based working capital facilities	Short-term	15.00	-	[ICRA]A2	[ICRA]A2	[ICRA]A2+	[ICRA]A2	[ICRA]A2	[ICRA]A3+
4	Non-fund-based working capital facilities	Long-term/ Short-term	(94.00)	-	[ICRA]BBB + (Stable)/ [ICRA]A2	-	-	-	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund-based – Term Loan	Simple
Long-term – Fund-based working capital	Simple
Short-term – Non-fund-based working capital	Very simple
Long-term/Short-term – Non-fund-based working capital	Very simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan	FY2022	NA	FY2027	41.50	[ICRA]BBB+(Stable)
NA	Fund-based working capital limits	NA	NA	NA	203.00	[ICRA]BBB+(Stable)
NA	Non-fund-based working capital limits	NA	NA	NA	15.00	[ICRA]A2
NA	Non-fund-based working capital limits	NA	NA	NA	(94.00)	[ICRA]BBB+(Stable) /[ICRA]A2

Source: Company

Please click here to view details of lender-wise facilities rated by ICRA

Annexure II: List of entities considered for consolidated analysis – Not Applicable

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