November 28, 2024

HealthCaps India Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – Fund based – Cash credit	55.00	50.00	[ICRA]A- (Stable); reaffirmed
Long-term – Fund based – Term loan	44.27	55.49	[ICRA]A- (Stable); reaffirmed
Long-term – Fund based – Working capital term loan	13.78	9.56	[ICRA]A- (Stable); reaffirmed
Short-term – Non-fund based – Letter of credit	9.50	7.50	[ICRA]A2+; reaffirmed
Total	**122.55**	**122.55**	

**Instrument details are provided in Annexure-I*

Rationale

The reaffirmation of the ratings factors in HealthCaps India Limited's (HIL's) established position as an empty capsule manufacturer in India, having long relationship with its customers across the gelatin capsule (empty hard gelatin capsules [EHGC]) and the relatively higher-margin hydroxypropyl methylcellulose (HPMC) capsule segments and the long experience of the promoters in this industry. The ratings also factor in the company's diversified presence across domestic as well as regulated export markets, including the US and Europe. The ratings also factor in the favourable financial risk profile of the entity, as reflected in its healthy operating margin, despite some moderation in FY2024 on a YoY basis, a conservative capital structure and comfortable coverage indicators, which are expected to continue, going forward, despite a planned capex, which would be partly funded through debt. ICRA notes the breach in the negative trigger earlier specified, however, it expects material improvement in HIL's DSCR in the next fiscal.

The ratings are, however, constrained by the high working capital intensity of operations on account of a stretched receivable cycle, coupled with moderately high inventory holding levels and a relatively moderate scale of operations. The company's profitability remains vulnerable to fluctuations in input prices and competitive pressure. Weaker-than-expected demand and high input prices, particularly of gelatin, resulted in moderation in the company's operating margin in FY2024. However, the company's operational profile is expected to improve with encouraging recent demand trends. ICRA also notes the medium forex exposure risks associated with the business. Besides, capsules as a product segment are at the risk of substitution from alternative/new drug delivery mechanisms, especially in the pharmaceutical industry.

The Stable outlook on the long-term rating factors in the company's significant presence in the high-margin HPMC capsule segment, favourable long-term demand outlook for the segment as well as the established relationships with its customers.

Key rating drivers and their description

Credit strengths

Established player in empty capsules industry with second largest domestic capacity; strong industry experience of the promoters – HIL is one of the leading manufacturers of empty capsules in India with an installed annual production capacity of ~19 billion capsules. The promoters have more than three decades of experience in the empty capsules segment. The company started with manufacturing EHGC, and later diversified into HPMC capsules in FY2017. HIL scaled up its HPMC capacity in the past few years owing to better realisations and margins compared to gelatin capsules. In FY2024, HPMC capsules contributed around 69% to the revenues while the rest came from gelatin capsules.

Geographically diversified customer base – The company has established relationships with a large customer base in the domestic and export markets, including the US and Europe. HIL caters to the US and European markets largely through its associate companies (AlfaCaps LLC in the US and HealthCaps Europe Ltd. in Europe). HIL earns around 64% of its revenue from the export markets and the domestic market accounts for the rest. The US and the European markets together contributed almost 60% to FY2024 revenues.

Low gearing and healthy coverage indicators – HIL's capital structure, as reflected by a gearing (TD/TNW) of 0.5 times as on March 31, 2024, continues to remain conservative (despite an elevated debt level owing to an elongated working capital cycle) because of healthy net worth at an absolute level. Owing to the decline in OPBITDA in FY2024, coverage indicators such as Total Debt/OPBITDA and DSCR weakened to 2.1 times (PY: 2.0 times) and 1.6 times (PY: 2.2 times), respectively. ICRA expects the coverage indicators to improve from the next fiscal with an overall recovery in the company's performance, despite a planned debt-funded capex.

Credit challenges

Moderate scale of current operations, though established position in domestic market – The company's scale of operations continues to remain at a moderate level. In FY2024, HIL's operating income fell by 2% to Rs. 242.3 crore from Rs. 247.6 crore in FY2023 due to lower volume of sales of gelatin capsules. In H1 FY2025, the company generated a total revenue of Rs. 115.4 crore compared to Rs. 110 crore in H1 FY2024, registering a nominal YoY growth of 5% and the OPM also improved to around ~23% from ~18% in FY2024. Nevertheless, the full year OPM in FY2025 is likely to remain at a level similar to that of FY2024. The company is expected to witness a demand recovery both in the domestic and the export markets in the medium term, supported by an expected ramp-up of gelatin capacities.

High working capital intensity with a long receivable period – HIL's business has remained working capital intensive, and the working capital intensity has increased to 55% in FY2024 from 49% in FY2023 due to a further increase in the receivable cycle. However, the company continues to be one of the leading players in the domestic market. Owing to increased exports, the working capital cycle has elongated on account of high transit time and relatively higher credit offered to export clients. ICRA notes that a large part of the export business is carried out through associate entities. The company is currently focusing on reducing its receivable cycle by increasing its focus on the domestic market, where the receivable cycle is relatively shorter. The company's ability to improve its working capital position would remain a key rating sensitivity.

Margins vulnerable to fluctuations in raw material prices and forex rates – The company's margins continue to remain dependent on the movement of raw material prices and realisations. In FY2024, the dip in overall realisations was higher than the decline in the raw material costs, resulting in a drop in the OPM to ~17.4% from 18.9% in FY2023. In FY2025, the OPM is expected to marginally improve, supported by demand recovery and uptick in realisations. Being a net exporter, the company is also exposed to forex risks, however, the risk is hedged through both natural and derivative hedging.

Threat of substitutes due to technological advances in other drug delivery mechanisms, although favourable demand outlook in nutraceutical space for capsules – The company's key product, empty capsules, is facing substitution risk from alternative drug delivery mechanisms such as tablets, injectables, etc., which can impact its global market share and growth rate. Generally, capsules have better bioavailability and masking properties over their closest oral substitutes, especially tablets. Capsules are preferred by consumers as it masks the medicinal taste and odour, although the shelf life is smaller. Thus, capsule manufacturers need to keep improving the quality of the capsules to meet the changing requirements of the pharmaceutical and nutraceutical industry.

Liquidity position: Adequate

HIL's liquidity remains adequate, with positive cash flow from operations over the past years and the same is expected to continue going forward. The moderate buffer available in its working capital limits also provides some comfort to its liquidity. The company has annual debt repayments of ~Rs. 14 crore and ~Rs. 10 crore in FY2025 and FY2026, respectively, and moderate capex requirements in the near term, which would partly be covered by its cash flow from operations and partly by a term loan, which is yet to be tied up.

Rating sensitivities

Positive factors – ICRA could upgrade HIL's ratings if there is a sustained and significant scale-up in its revenues, while maintaining its profitability and coverage metrics along with a significant reduction in the working capital cycle.

Negative factors – Pressure on HIL's ratings could arise in case of a sharp deterioration in its revenue and earnings, or a material elongation in the working capital cycle, affecting its liquidity. A specific credit metric for ratings downgrade would be DSCR below 2.0 times, on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology - Pharmaceuticals
Parent/Group support	Not applicable
Consolidation/Standalone	Standalone

About the company

Incorporated in 1982, HealthCaps India Limited (HIL) is a promoter held company involved in manufacturing of empty capsules. The company started with manufacturing EHGC and later diversified into the manufacturing of HPMC capsules from FY2017 to cater to the growing demand from the pharmaceutical and nutraceutical industries due to changing consumer preferences. The company sells capsules in both domestic and international markets such as the US, Europe, Africa and the Middle East.

The manufacturing facility of the company is in Nawanshahar district, Punjab. HIL has sales offices in Delhi, Mumbai and Mohali. As of March 31, 2024, the company has total operational capacity of ~18 billion capsules per annum (BCPA). It manufactures capsules in sizes of 00, 0, 1, 2, 3 and 4. HIL has a diversified customer base of over 400 clients in more than 60 countries across the world.

Key financial indicators (audited)

HealthCaps India Limited	FY2023	FY2024	H1 FY2025*
Operating income	247.6	242.3	115.4
PAT	29.8	21.5	14.8
OPBDITA/OI	18.9%	17.4%	22.7%
PAT/OI	12.0%	8.9%	12.9%
Total outside liabilities/Tangible net worth (times)	1.0	0.9	-
Total debt/OPBDITA (times)	2.0	2.1	-
Interest coverage (times)	6.4	5.5	-

*Source: Company, ICRA Research; * Provisional numbers; All ratios as per ICRA's calculations; Amount in Rs. crore PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2025)			Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Date & rating in FY2025	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022
				Nov 28, 2024	Sept 29, 2023	Aug 17, 2022	Jan 06, 2022
1	**Cash credit**	Long term	50.00	**[ICRA]A- (Stable)**	**[ICRA]A- (Stable)**	**[ICRA]A- (Stable)**	**[ICRA]BBB+ (Positive)**
2	**Term loan**	Long term	55.49	**[ICRA]A- (Stable)**	**[ICRA]A- (Stable)**	**[ICRA]A- (Stable)**	**[ICRA]BBB+ (Positive)**
3	**Working capital term loan**	Long term	9.56	**[ICRA]A- (Stable)**	**[ICRA]A- (Stable)**	**[ICRA]A- (Stable)**	**[ICRA]BBB+ (Positive)**
4	**Letter of credit**	Short term	7.50	**[ICRA] A2+**	**[ICRA] A2+**	**[ICRA] A2+**	**[ICRA] A2**

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term – Fund based – Cash credit	Simple
Long-term – Fund based – Term loan	Simple
Long-term – Fund based – Working capital term loan	Simple
Short-term – Non-fund based – Letter of credit	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	**Cash credit**	NA	8.5 – 9.0%	NA	50.00	[ICRA]A- (Stable)
NA	**Term loan**	FY2019	8.5 – 9.0%	FY2027	55.49	[ICRA]A- (Stable)
NA	**Working capital term loan**	FY2021	9.25%	FY2027	9.56	[ICRA]A- (Stable)
NA	**Letter of credit**	NA	NA	NA	7.50	[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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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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