ICRA

September 28, 2020

Laborate Pharmaceuticals India Limited: Long-term rating upgraded to [ICRA]A+ (Stable); short-term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund-based	80.00	80.00	[ICRA]A+(Stable); Upgraded from [ICRA]A (Stable)
Short-term fund-based	40.00	40.00	[ICRA]A1; Reaffirmed
Short-term non-fund based	5.00	5.00	[ICRA]A1; Reaffirmed
Total	**125.00**	**125.00**	

**Instrument details are provided in Annexure-1*

Rationale

The rating upgrade factors in the improvement in the financial profile of Laborate Pharmaceuticals India Limited (LPIL) characterised by healthy revenue growth over the last couple of years across business segments, improving profitability indicators, driven by cost cutting initiatives and process improvements, and improving credit profile due to healthy cash flow generation and subsequently reduction in debt levels. The ratings favourably factor in LPIL's diversified product portfolio and wide therapeutic segment coverage, which includes non-steroidal anti-inflammatory drugs (NSAIDs), anti-biotics, eye/ear/nasal drops and anti-allergic among others.

LPIL registered a revenue growth of 7.5% YoY to Rs. 903.7 crore in FY2020, primarily supported by growth in the domestic formulations business (~12% growth over the prior year). Further, despite certain challenges because of the pandemic-induced lockdowns, it witnessed a healthy revenue growth of 18.9% Y.o.Y during Q1 FY2021, supported by healthy growth across all the segments. With several pharmaceutical products achieving significant scale up in the recent past, LPIL has an established brand in the trade generics segment. The company's personal care division (launched in FY2015), which manufactures and markets a range of products - such as talcum powder, cosmetics, face wash, body lotions and other personal care products, under the brands 'Labolia' and 'Shree Ayu-veda' - recorded strong revenue growth of 13.3% and 18.0% in FY2020 and Q1 FY2021, respectively, with some of its products gaining market traction in tier-II and III cities and towns in India.

In FY2021, ICRA expects the company's domestic sales to maintain healthy revenue growth, aided by traction towards trade generics vis-à-vis prescription generics because of disruption caused by the Covid-19 pandemic and continued focus on new product launches. The export sales are likely to grow at a healthy pace because of favourable demand from the key markets and its established associations with local distributors in those markets.

The company's operating profit margins have been consistently improving over the last three years. In FY2020, LPIL's operating profit margin improved considerably to 14.5%[1] from 11.1% in FY2019 and 10.1% in FY2018, supported by reduction in selling expenses due to change in incentives structure, rising scale of operations and process improvements. The NPM improved to 9.6% in FY2020 from 6.4% in FY2019, supported by higher OPBITDA and lower interest expenses.

[1] *Figures for FY2020 and Q1 FY2021 are provisional*

Going forward, ICRA expects the company's OPM to remain stable over the medium term, aided by the company's continuing efforts at process improvements and increasing scale of operations. Nevertheless, any regulatory changes either in the domestic or the exports markets with respect to any price cuts or rationalisation of trade margins could impact its financial profile and would remain a key monitorable.

The ratings also take comfort from the strong credit indicators and comfortable capital structure of the company. With better working capital management, limited capital expenditure and healthy cash accruals, its working capital borrowings remained nil since January 2020 and it has accumulated surplus cash and liquid balances of ~Rs. 90 crore as on August 31, 2020. The decline in debt levels, combined with improvement in profitability led to an improvement in TD/OPBDIT to 0.1 times in FY2020 from 0.7 times in FY2019 and improvement in interest cover to 24.3 times in FY2020 from 9.6 times in FY2019. ICRA expects the company to maintain its comfortable credit indicators in the near-term, supported by healthy cash accruals and moderate capital expenditure plans.

The ratings are constrained by company's presence being limited to the trade generics segment. Its domestic formulations business is characterised by its limited presence in the chronic therapy segments such as anti-diabetics, cardiovascular (CVS), central nervous systems (CNS), etc, and low research and development (R&D) spend, which limits its scope to develop novel drug delivery-based formulations (in domestic market) as well as foray into regulated markets that offer superior profitability besides diversification. Furthermore, LPIL's exports its products mostly to semi-regulated and unregulated markets with significant share of revenues coming from countries in Africa and Middle East. This exposes the company to credit risk during periods of macro-economic headwinds and geopolitical uncertainties. This risk is, however, partially mitigated by a portion of its sales being backed by letter of credit (LC) or advance payments in some cases. With respect to foreign exchange exposure, the company's export sales are denominated primarily in US Dollar and to some extent in Euros. This limits the foreign exchange fluctuation risk related to local currencies.

The Stable outlook on the long-term rating reflects ICRA's belief that LPIL will maintain its market presence supported by launch of new products across therapy segments, scale-up in export business and ramp-up in the personal care division. It is also expected to maintain its healthy profitability indicators, comfortable credit metrics and strong liquidity profile.

Key rating drivers and their description

Credit strengths

Among the leading companies in Indian trade generics segment – LPIL has positioned itself amongst the leading companies in the trade generics segment in India with significant presence in tier-II and III markets and an increasing presence in the tier-I markets. The company is primarily present in the branded generics segment and drives its business by promoting products directly through the trade channels rather than promoting through doctor's prescriptions. Its domestic formulations business has ~700 products and is supported by a network of ~450 marketing representatives.

Well-diversified domestic sales with wide therapeutic segment coverage – LPIL has a well-diversified domestic formulations business with top 10 products typically contributing to only 25-30% of its total revenues and the top five therapeutic segments accounting for ~70% of its revenues.

Established distribution network in international markets supports growth prospects – The company's export sales have grown at a CAGR of ~15% between FY2016 and FY2020, aided by its established association with distributors and improvement in the economic conditions of its target markets. The export sales contribute to 27-30% of its total revenues.

Healthy scale-up of personal care division aids diversification – The personal care division, launched in FY2015, has scaled up significantly during the last two to three years because of successful brand launches and has gained market traction in the tier-II and tier-III markets in India. Revenues from this division has scaled up to Rs. 50.4 crore in FY2020 from Rs. 19.5 crore in FY2015 (20.9% CAGR), driven by increasing brand recognition in its target markets. This division has a separate team of marketing representatives and promotes some of its products via television advertisements.

Favourable financial risk profile reflected by comfortable capital structure and strong debt protection metrics – The company's financial risk profile is characterised by negligible external long-term borrowings, improving cash accruals and healthy cash balances. Its credit metrics are comfortable with TD/TNW at 0.02 times as on March 31, 2020 (PY: 0.3 times), TOL/TNW at 0.7 times in FY2020 (PY: 1.1 times) and interest cover at 24.3 times in FY2020 (PY: 9.6 times). ICRA expects the company to maintain its comfortable credit indicators in the near-term supported by expectations of healthy cash accruals and moderate capital expenditure plans.

Credit challenges

Presence limited to low-value added branded generics segments – LPIL's sales are primarily concentrated low-value added branded generics, which is characterised by stiff competition compared to fast-growing chronic therapy segments. The company's R&D spend is only 3-4% of the net sales, which is lower compared to the leading pharmaceutical companies in India (averaging 6-10%), thus limiting its capability to develop complex pharmaceutical products.

Limited presence in fast-growing lifestyle-related chronic therapeutic segment – The company has limited presence in lifestyle-related chronic therapeutic segments such as anti-diabetics, CVS, CNS, etc. Chronic drugs are consumed by patients over a long time, which creates a strong brand recall. LPIL is present only in acute segments such as anti-biotics, NSAIDs, etc, where it faces strong competition from several companies. As a result, it has limited presence in tier-I cities in India.

Exports limited to semi-regulated countries – The company's exports are mostly limited to semi or un-regulated markets, which include countries in Africa and Asia including Nigeria, Zambia and Burundi. However, this risk is mitigated by LC-backed or advance payments, majority of the exports being denominated in USD and LPIL's established association with local distributors in those markets.

Potential regulatory developments in relation to rationalisation of trade margins –The National Pharmaceutical Pricing Authority (NPPA) and the Department of Pharmaceuticals (DoP) have been finalising a proposal to limit the trade margins of non-scheduled medicines (drugs not under direct price control) and medical devices. This is aimed at reducing the prices and thereby improve the affordability of high-value medicines and medical devices. While it remains uncertain how many medicines would see a price reduction, LPIL's financial performance would remain sensitive to regulatory risks associated with the rationalisation of trade margins or any price cuts.

Liquidity position: Strong

LPIL has a **strong** liquidity profile, which is supported by healthy cash flows from operations, surplus cash balances (~Rs. 90 crore as of August 31, 2020) and unutilised working capital limits of Rs. 120.0 crore. ICRA expects the company to maintain its strong liquidity profile, going forward, because of expectation of healthy cash flow from operations, minimal capex plans (~Rs. 10 crore in FY2021) and modest debt repayments (Rs. 1.3 crore in FY2021).

Rating sensitivities

Positive triggers – The company's ability to strengthen its business profile by increasing its presence especially in fast-growing lifestyle-related therapy segments, improving product mix or geographical presence with foray into regulated markets would be considered favourably for a rating upgrade. In addition, significant scaling up of operations, while maintaining healthy profitability indicators, along with sustenance of comfortable credit metrics could lead to an upgrade in the ratings.

Negative triggers – The ratings could be downgraded if the company's operational and financial performance weakens significantly due to reasons such as increase in competition in the domestic market or any large debt-fund capex/acquisitions. Any regulatory changes either in the domestic or the export markets with respect to uncertainty governing rationalisation of trade margins and drug pricing remain a monitorable.

Analytical approach

Analytical Approach	**Comments**
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Pharmaceutical Industry
Parent/Group Support	Not applicable.
Consolidation/Standalone	The ratings are based on standalone financial statements of the issuer.

About the company

Established in 1985, LPIL is a medium-sized pharmaceutical company, which manufactures and markets branded generic formulations, both in the domestic and export markets. The company was founded by the Panipat-based Bhatia family, whose various members head different functions of the company at present. It manufactures pharmaceuticals and cosmetics from its plants in Panipat (Haryana) and Paonta Sahib (Himachal Pradesh). After exporting its products for a decade, LPIL commenced selling its products in the domestic market under its own brand name.

The company's domestic business can be divided into three verticals—the elite division, the GPP division and the personal care division, which contributed to 56%, 11% and 6%, respectively, of its turnover in FY2020. A major portion of the domestic sales are generated by the elite division, which sells branded generic formulation products under the Laborate brand and drives its business by promoting products directly through the trade channels rather than promoting through doctor's prescriptions. Antibiotics, ear/nose/eye drops, and NSAIDs are its key therapeutic segments with the top 10 brands contributing to 27.5% of its turnover. The division is supported by a network of 450 marketing representatives. In terms of the geographical split, North India accounted for 44% of the domestic revenues in FY2020, followed by East India (21%), South India (19%) and West India (16%).

The company's GPP vertical was set up in FY2012 to combat competition in the branded generics sold directly to super stockists. It sells the same products as that in the elite division, but under the GPP brand and through a different supply chain. LPIL launched its personal care division in FY2015 to leverage its distribution reach and diversify its operations. The elite division has ~500 products, the personal care division has 60 cosmetic and Ayurvedic preparations, while the GPP division has ~200 products. LPIL enjoys a healthy mix of both domestic (73%) and international (27%) branded generic sales. The company primarily markets its branded formulations in semi-regulated markets with the major ones being Nigeria, Yemen, and Iraq.

Key financial indicators

	FY2019 (Audited)	FY2020 (Provisional)
Operating Income (Rs. crore)	840.9	903.7
PAT (Rs. crore)	53.8	87.0
OPBDIT/OI (%)	11.1%	14.5%
PAT/OI (%)	6.4%	9.6%
Total Outside Liabilities/Tangible Net Worth (times)	1.1	0.8
Total Debt/OPBDIT (times)	0.7	0.1
Interest Coverage (times)	9.6	24.3

Status of non-cooperation with previous CRA:

CRISIL had suspended its ratings for LPIL in July 2016 due to lack of information.

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)				Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	Rating	FY2020	FY2019	FY2018
					28-Sep-2020	12-Jun-2019	-	31-Jan-2018
1	Cash Credit	Long Term	80.00	NA	[ICRA]A+ (Stable)	[ICRA]A (Stable)	-	[ICRA]A (Stable)
2	Packing Credit	Short Term	40.00	NA	[ICRA]A1	[ICRA]A1	-	[ICRA]A1
3	Buyer's Credit Facility/ Letter of Credit	Short Term	5.00	NA	[ICRA]A1	[ICRA]A1	-	[ICRA]A1

Amount in Rs. crore

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Cash Credit	NA	NA	NA	80.00	[ICRA]A+ (Stable)
NA	Packing Credit	NA	NA	NA	40.00	[ICRA]A1
NA	Buyer's Credit Facility/ Letter of Credit	NA	NA	NA	5.00	[ICRA]A1

Source: Laborate Pharmaceuticals India Limited

Annexure-2: List of entities considered for consolidated analysis- Not Applicable

Analyst Contacts

Subrata Ray
+91 22 6114 3408
subrata@icraindia.com

Shamsher Dewan
+91 124 4545 328
shamsherd@icraindia.com

Rohan Kanwar Gupta
+91 124 4545 808
rohan.kanwar@icraindia.com

Arushi
+91 124 4545 396
arushi@icraindia.com

Relationship Contact

Jayanta Chatterjee
+91 80 4332 6401
jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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.

For more information, visit www.icra.in

ICRA Limited

Corporate Office
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300
Email: info@icraindia.com
Website: www.icra.in

Registered Office
1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50

Branches

Mumbai	+ (91 22) 24331046/53/62/74/86/87
Chennai	+ (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,
Kolkata	+ (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,
Bangalore	+ (91 80) 2559 7401/4049
Ahmedabad	+ (91 79) 2658 4924/5049/2008
Hyderabad	+ (91 40) 2373 5061/7251
Pune	+ (91 20) 2556 0194/ 6606 9999