Strides Shasun Limited

May 28, 2018

Summary of rated instruments

Instrument*	Previously Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	1,094.6	1,094.6	[ICRA]A+/ Reaffirmed; Negative outlook assigned; Removed from watch with developing implications
Short-term fund based facilities	890.00	890.00	[ICRA]A1/Reaffirmed; Removed from watch with developing implications
Short-term non-fund based facilities	520.00	520.00	[ICRA]A1/Reaffirmed; Removed from watch with developing implications
Unallocated facilities	624.41	624.41	[ICRA]A1/Reaffirmed; Removed from watch with developing implications
Total	**3,129.01**	**3,129.01**	

*Instrument details in Annexure – I

Rating action

ICRA has reaffirmed the [ICRA]A+ (pronounced ICRA A plus) rating outstanding on the Rs.1,094.6 crore term loans of Strides Shasun Limited while assigning a Negative outlook to the same. ICRA has also reaffirmed the [ICRA]A1 (pronounced ICRA A One) rating outstanding on the Rs. 890.00 crore short-term fund-based facilities, the Rs.520.00 crore short-term non-fund-based facilities and the Rs.624.41 crore proposed limits of Strides Shasun Limited. The ratings have been removed from watch with developing implications.

Rationale

For arriving at the ratings, ICRA has taken a consolidated view of SSL along with its subsidiaries since all its subsidiaries operate in the same line of business and have operational linkages.

The revision in rating outlook follows its weak operating performance in the US market during Q4 FY2018. While the company's cumulative revenues from the US market during 9m FY2018 stood at 641.8 crore, the same during Q4 FY2018 stood at Rs.132.7 crore (q-o-q de-growth of 50.8%) in turn affecting the company's operating margins (down to 15.8% during Q4 FY2018 from 18.5% during Q3 FY2018). While the company's partnered products suffered heavy pricing pressure from the incumbent players and struggled to garner the anticipated market share, further delay in the approval of certain products also affected the company's performance adversely. While the company is expected to launch about 15 products in the US over the next one year, we expect the pricing pressure prevalent in the US market across the industry to affect SSL's business prospects going forward as well. The outlook also reflects the high debt levels of the company with total debt of Rs.2,528.4 crore as on March 31, 2018 even while large part of the cash-backed loans had been prepaid during FY2018. The company's TD/OPBDITA and Net Debt/OPBDITA stood at around 5.8x and 4.4xrespectively as on March 31, 2018 and continue to remain high as compared to medians for the company's rating category.

The ratings continue to be supported by SSL's diversified business profile, the company's long track record and its strong management team. Improving front-end presence across regulated markets coupled with strong manufacturing infrastructure approved by major regulatory authorities provide further support to the ratings. Further, healthy pace of product filings (and faster approvals of the same under the new GDUFA regimen for the US market) supported by its strong

R&D and regulatory capabilities are expected to support SSL's business prospects going forward. Going forward, backward integration of the Australian product portfolio to SSL's in-house facilities in India coupled with improving front end presence is expected to support the company's business prospects and margins. Further, the recently announced merger with Apotex in Australia is expected to strengthen the company's competitive position going forward.

The ratings also consider the sequential decline in SSL's institutional business due to lower offtake by global donor agencies and API supply chain disruption in the Anti-Retro Viral portfolio during FY2018. Further, challenges with respect to increasing regulatory compliance costs, and the vulnerability of margins to foreign exchange fluctuations with majority of revenues being derived through exports – though the same is mitigated to some extent by natural hedge from foreign currency denominated loans, also continue to affect the company's ratings.

While the company has been active in the in-organic space targeting growth and diversification through strategic acquisitions in the past, going forward, this remains an event risk and would be evaluated on a case-by-case basis. Going forward, the company's ability to revive its operating margins, reduce its debt levels especially in the face of increase in working capital intensity (on account of GST), and improve its credit metrics would remain key rating sensitivities.

Outlook: Negative

ICRA expects the pricing pressure prevalent in the US market across the industry to affect SSL's business prospects going forward as well. The outlook also reflects the high debt levels of the company with total debt of Rs.2,528.4 crore as on March 31, 2018 even while large part of the cash-backed loans had been prepaid during FY2018. The company's TD/OPBDITA and Adj. Net Debt/OPBDITA stood at around 5.8x and 4.0x respectively as on March 31, 2018 and continue to remain high as compared to medians for the company's rating category. The outlook may be revised to 'Stable' or 'Positive' if higher than expected revenue growth and profitability strengthens the financial risk profile.

Key rating drivers

Credit strengths

Diversified business and geographic mix lends revenue stability: SSL derives majority of its revenues from its regulated markets (Australia – 32.2%, US – 27.1% and other regulated markets – 11.8% of total revenues during FY2018). In addition to the same, the company also derives revenues from emerging markets like Africa where it is present in the branded and institutional businesses (28.9% of total revenues during FY2018).

Demerger of API business likely to support the margins of SSL over the longer term: While SSL's healthy market position in the formulations segment will be complemented by its preferred buyer status with Solara Active Pharma Sciences Limited (SAPL) ensuring a robust supply chain, its margins are expected to improve over the longer term supported by operating exclusively in the formulations segment which entails relatively higher margins.

Strong research and development (R&D) capabilities coupled with improving front end presence: Given it strong pipeline of limited competition products, we expect the company's revenue growth and margins to revive from FY2019 supported by healthy filing rate and product approval rates in the US market and enhanced product basket and expanding pharmacy coverage in Australia respectively. SSL's strong manufacturing infrastructure with key facilities having been approved by regulatory authorities of developed markets are expected to facilitate the same going forward.

Credit challenges

High debt levels: The company has high debt levels on account of the debt-funded nature of large acquisitions in the past coupled with recent stretch in working capital levels post GST implementation. TD/OPBDITA and Net Debt/OPBDITA stood at around 5.8x and 4.4x respectively as March 31, 2018 and continue to remain high as compared to rating medians for the company's rating category. Even while the company prepaid significant amount of loans (~Rs.900 crore) during FY2018, debt levels continue to remain high. However, recent debt refinancing taken up by the company with relatively longer tenure loans and lower repayments in the next 1-2 years is expected to support the company's cash flows over the near term.

High competitive intensity: Generic pharmaceutical business in regulated markets is characterised by low entry barriers and high pricing pressures. While the company's revenues under its own front-end in North America continue to maintain steady market share, some products under the company's partnered model witnessed significant headwinds in the form of intense competitive pressures resulting in decline in operating margins during FY2018.

Weak FY2018 performance: The company's revenue growth and margins during FY2018 was impacted on account of increased competitive intensity in some partnered molecules in the US. This, coupled with lower contribution from margin-accretive institutional segment sales on account of a weak demand scenario in conjunction with continued investments in R&D affected the company's OPMs adversely.

Risk arising from inorganic growth: Given the past history of inorganic growth, any large debt funded acquisition can impact SSL's credit profile.

Links to applicable criteria:

Corporate Credit Rating Methodology

Rating Methodology- Pharmaceutical Industry

About the company:

Incorporated in 1990, Strides Shasun Limited (previously known as Strides Arcolab Limited) is a medium sized pharmaceutical company engaged in the development, manufacture and export of a wide range of pharmaceutical products. The company has followed an inorganic growth strategy over the years that resulted in foray into new markets, and the addition of new business segments, therapy segments and manufacturing infrastructure. The company's product range covers most dosage forms including tablets, capsules and semi-solids. Following the divestment of its sterile/injectable business to Mylan Inc. in 2013, it concluded the merger with Shasun Pharmaceuticals Limited and acquired Aspen's Australian generic pharmaceuticals business (Arrow Pharmaceuticals) during FY2016. During November 2017, the company had sold its India generics business to Eris Lifesciences Limited to increase its focus on strengthening its market position in the regulated and African markets.

Currently, the company's business became broadly classified into: regulated markets formulations (comprising mainly the US, Europe and Australia), emerging markets (primarily Africa), institutional segment (tender-driven business mainly in developing markets) and APIs and services (the erstwhile business of Shasun Pharmaceuticals Limited). However, the API business will be demerged from the company (post receipt of NCLT approval) effective October 01, 2017.

Key financial indicators (audited)

Consolidated	FY2017	FY2018
Operating Income (Rs. crore)	2,830.8	2,879.7
PAT (Rs. crore)	279.7	70.2
OPBDIT/ OI (%)	21.3%	15.2%
RoCE (%)	12.9%	7.1%
Total Debt/ TNW (times)	1.3	1.0
Total Debt/ OPBDIT (times)	6.1	5.8
Interest coverage (times)	3.3	2.2

Source: Company, ICRA research; OPBDITA: Operating Profit before Depreciation, Interest and Taxes; PAT: Profit After Tax; RoCE: Return on Capital Employed; TNW: Tangible Net Worth; NWC: Net Working Capital

**The Adj.Net Debt/TNW ratio for FY2017 and FY2018 is 0.7x and the Adj.Net Debt/OPBDITA ratio for FY2017 and FY2018 is 3.4x and 4.0x respectively (Adjusted for receivable of Rs.131 crore receivable from SAPL towards sale of Strides Chemicals); the core ROCE for SSL is 18.4% and 9.3% during FY2017 and FY2018*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

					Current Rating (FY2019)	Chronology of Rating History for the past 3 years						
						Date & Rating in FY2018			Date & Rating in FY2017			Date & Rating in FY2016
	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding as on March 31, 2018 (Rs Crore)	Date & Rating May 2018	Mar 2018	Jan 2018	July 2017	Feb 2017	Sep 2016	Apr 2016	Jun 2015
1	Term Loans	LT	1,094.6	1,584.1	[ICRA] A+ (Negative)	[ICRA] A+ &	[ICRA] A+ &	[ICRA] A+ &	[ICRA] A+ &	[ICRA] A+ (Stable)	[ICRA] A+ (Stable)	[ICRA] A+ &
2	Fund based facilities	ST	890.0	944.4	[ICRA] A1	[ICRA] A1 &	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+ &
3	Non-fund based facilities	ST	520.0	-	[ICRA] A1	[ICRA] A1 &	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+ &
4	Unallocated facilities	ST	624.41	-	[ICRA] A1	[ICRA] A1 &	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+ &	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+ &

&: under rating watch with developing implications

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

Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
Term Loans	2016		FY2024	1,094.60	[ICRA]A+ (Negative)
Fund based facilities		-	NA	890.00	[ICRA]A1
Non-fund based facilities			NA	520.00	[ICRA]A1
Unallocated facilities	NA		NA	624.41	[ICRA]A1

Source: Strides Shasun Limited

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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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