INDOCO REMEDIES LTD

indoco remedies limited

April 4, 2018

To The Listing Department **National Stock Exchange of India Limited** Exchange Plaza, Bandra - Kurla Complex Bandra (East) Mumbai - 400 051 ***Stock Code : INDOCO-EQ***	To The Listing Department **Bombay Stock Exchange Limited** Floor 25, P. J. Towers, Dalal Street, Mumbai - 400 001 ***Stock Code : 532612***

Dear Sirs,

Sub : Disclosure Under Regulation 30 of LODR Regulations 2015

Credit Rating by ICRA .

This is to inform you that the Rating Committee of ICRA has revised the rating from [ICRA]AA- (pronounced ICRA double A minus) to [ICRA]A+ (pronounced ICRA A plus) for the long term borrowing programme of the company. The Outlook on the long-term rating has been revised to 'Stable' from 'Negative'.

The short term rating has been reaffirmed at [ICRA]A1+ (pronounced ICRA A one plus)

Please find enclosed rating research update issued by ICRA for your reference.
Thanking you,

Yours faithfully,
For Indoco Remedies Limited

Jayshankar

Jayshankar Menon
Company Secretary

Indoco Remedies Limited

April 4, 2018

Indoco Remedies Limited: Update on Material Event

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term, Loans	165.00	165.00	[ICRA]A+ (Stable); Revised from [ICRA]AA- (Negative)
Long-term, Fund-based Limits	97.40	97.40	[ICRA]A+ (Stable); Revised from [ICRA]AA- (Negative)
Short-term, Fund-based Limits	20.00	20.00	[ICRA]A1+; Re-affirmed
Short-term, Non-fund Based Limits	13.25	13.25	[ICRA]A1+; Re-affirmed
Commercial Paper Programme	25.00	25.00	[ICRA]A1+; Re-affirmed
Total	**320.65**	**320.65**	

*Instrument details are provided in Annexure-1

Material Event

Indoco Remedies Limited (IRL) has announced on March 27, 2018 that The Medicines and Healthcare Products Regulatory Agency of the United Kingdom (UK-MHRA) inspected its drug manufacturing facility (Plant at Goa) from March 14, 2018 to March 16, 2018. Subsequent to the inspection, the UK-MHRA has issued observations, comprising three critical and four major ones.

Impact of the material event

ICRA has revised the long-term rating assigned to the Rs. 165.00-crore[1] term loans and the Rs. 97.40-crore long-term, fund-based facilities of IRL to [ICRA]A+ (pronounced ICRA A plus)[2] from [ICRA]AA-(pronounced ICRA double A minus). The outlook on the long-term rating has been revised to Stable from Negative. ICRA has re-affirmed the short-term rating of [ICRA]A1+ (pronounced ICRA A one plus) assigned to the Rs. 20.00-crore short-term, fund-based facilities, the Rs. 13.25-crore short-term, non-fund based facilities and the Rs. 25.00-crore commercial paper programme of the company.

Rationale

The revision in the long-term rating factors in the greater-than-expected weakening in IRL's operating performance in FY2018 and FY2019, following regulatory observations issued by the United States Food and Drug Administration (USFDA) and the UK-MHRA to the company's manufacturing plants and pricing pressures in other regulated markets. IRL witnessed a YoY de-growth of 11.0% in export formulations sales in 9M FY2018 led by~62% YoY decline in the US formulations sales following the receipt of the warning letter from the USFDA for two of its plants at Goa during March 2017. The company had voluntarily stopped supplies of its ophthalmic products to the US from this facility. While it had

[1] *100 lakh = 1 crore = 10 million*

[2] *For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications*

earlier indicated re-commencement of supplies of ophthalmic products to TEVA from its units in Goa from November 2017 onwards, the same has not yet materialised. The company now expects to commence the same from Q2 FY2019 onwards, post TEVA's due diligence of IRL's manufacturing facilities and post USFDA audit of Goa Plant II and III. Besides continued muted sales from the US in the near term, this is also expected to result in delays in approval of the pending abbreviated new drug applications (ANDAs).

While IRL has witnessed a healthy 29% YoY growth in sales to Europe in 9M FY2018, its revenues are expected to moderate going forward following the receipt of observations from the UK-MHRA, coupled with the pricing pressures being faced by the company in this region. ICRA also notes the de-growth in sales in the emerging markets and other regulated markets (barring Europe) during 9M FY2018 due to continued weak order inflows. The domestic formulations sales have also witnessed a YoY decline of 2% in 9M FY2018 owing to ~30% decline during Q1 FY2018 due to the GST impact with effect from July 01, 2017. Sales de-growth has also led to a decline in operating profit margin to 11.1% in 9M FY2018 vis-à-vis 15.2% in 9M FY2017.

Timely resolution of the observations by the UK-MHRA and the warning letters by the USFDA for scaling up of operations and an improvement in the profitability of IRL remain the key rating sensitivities.

The ratings continue to derive comfort from IRL's diversified geographic presence, with ~36% of 9M FY2018 sales derived from the exports markets, including 83% of export sales from regulated markets. While IRL's presence in the domestic market is primarily limited to mature molecules in acute therapies with intense competition, it is characterised by wide therapeutic coverage with a strong presence in anti-infectives, respiratory systems and dental therapies, with its major brands positioned amongst the top five brands in their respective categories. Furthermore, notwithstanding the moderation in the operating profitability, the financial profile of the company has remained comfortable as characterised by low gearing and healthy debt protection indicators. ICRA also takes note of the regulatory risks associated with pricing controls in the domestic market. The company also remains exposed to foreign currency fluctuations, given the sizeable exports. However, the risk is partially mitigated as the company enters into forward covers.

Outlook: Stable

ICRA expects IRL's operating profit margins to benefit in the long-term from the increasing share of higher margin export sales from the US with expected ANDA approvals and out-licensing deals and improved operating efficiencies in the domestic market as well as favourable product mix. However, this is contingent on the resolution of the regulatory non-compliances at its Goa facility. Prompt resolution of the same is a key rating sensitivity and ICRA would continue to monitor the developments in this regard. IRL's management has indicated commencement of the supplies of ophthalmic products to Teva from Q2 FY2019 onwards. Furthermore, it does not expect any adverse impact of the recent observations by UK-MHRA on the future sales from the European region.

The outlook may be revised to Negative following non-resolution of the observations in a timely manner, resulting in a further de-growth in sales as well as weakening of profitability. The outlook may be revised to 'Positive' in case of significant improvement in revenues and profitability aided by high margin export sales, led by ANDA approvals/out-licensing deals.

Key rating drivers

Credit strengths

- **Established brands in respiratory, dental and anti-infective therapies of the domestic formulations market –** IRL has a diversified geographic presence, with ~36% of its 9M FY2018 derived from exports markets, including 83% of export sales from regulated markets. While IRL's presence in the domestic market is primarily limited to mature molecules in acute therapies with intense competition, it is characterised by wide therapeutic coverage with a strong presence in anti-infectives, respiratory systems and dental therapies. The company enjoys good reputation in the domestic market, with its major brands positioned amongst the top-five positions in their respective therapy segments. However, given the matured molecules and presence of large number of players, market share and pricing power of IRL remain low.

- **Comfortable financial risk profile, characterised by low gearing and healthy debt protection indicators –** Notwithstanding the moderation in the operating profit margin during 9M FY2018, the financial profile of the company has remained comfortable, as characterised by low gearing (less than 0.5 times estimated as on March 31, 2018) and healthy debt protection indicators, with interest cover of 5.6x as on December 31, 2017.

Credit challenges

- **Regulatory non-compliances for all of IRL's plants at Goa –** At present, regulatory non-compliances have been issued to all of IRL's plants at Goa, which account for a majority of the company's formulation exports. While Goa plant II and III have been issued warning letters by USFDA, Goa plant I has received 483's from USFDA and inspection observations from UK-MHRA. These plants together accounted for ~26% of IRL's sales in FY2017. Prompt resolution of these non-compliances is a key rating sensitivity.

- **Increasing pressure on profitability –** Profitability pressures in FY2017 were contributed by increased employee expenses and continued high research and development investments. Furthermore, the company has witnessed a decline in operating profit margin to 11.1% in 9M FY2018 from 15.2% in 9M FY2017 due to the sales de-growth.

- **Exposed to foreign currency fluctuation risks –** With ~36% of its revenues coming from exports, the company remains exposed to foreign currency fluctuations. However, the risk is partially mitigated as it enters into forward covers.

- **Domestic formulations industry remains vulnerable to changes in Government policies related to price control**

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria:
Corporate Credit Rating Methodology
Methodology for Pharmaceutical Industry

About the company:

Indoco Remedies Limited was established by Mr. Govind Ramnath Kare in 1945 under the name Indo Continental Trading Company, and was involved in imports of pharmaceutical formulations from Europe and their sales in India. In 1963, the current Chairman and Managing Director–Mr. Suresh G. Kare–took over.

IRL currently manufactures and markets branded formulations, active pharmaceutical ingredients (APIs) and contract research and manufacturing services (CRAMS), with a strong presence in the domestic market, which contributed to ~59% of its total revenues in 9M FY2018. In the domestic business, IRL has a prominent presence in the anti-infective, respiratory, gastro-intestinal and dental segments, with its major brands positioned amongst the top-five in their respective categories.

IRL's formulation plants are located at Goa (three plants), Mumbai, Waluj (Aurangabad) and Baddi (Himachal Pradesh), while API plants are located at Patalganga and Rabale. IRL has manufacturing facilities with regulatory approvals from UK-MHRA, USFDA, TGA Australia, MCC South Africa and German regulatory authorities. In FY2017, IRL acquired Micro Labs Limited's solid oral dosage manufacturing facility located at Baddi, which would be utilised to manufacture formulations for the European and UK markets, post receipt of the EUGMP certification and the UKMHRA approval.

For the 12 months ended March 31, 2017, IRL reported a profit after tax (PAT) of Rs. 77.5 crore on an operating income (OI) of Rs. 1,094.1 crore, as against a PAT of Rs. 82.3 crore on an OI of Rs. 1,004.8 crore for the 12 months ended March 31, 2016.For the nine months ended December 31, 2017 (unaudited), IRL reported a PAT of Rs. 20.7 crore on OI of Rs. 771.9 crore.

Key Financial Indicators (audited)

	FY2016	FY2017
Operating Income (Rs. crore)	1004.76	1094.06
PAT (Rs. crore)	82.29	77.46
OPBDIT/ OI (%)	17.46%	14.35%
RoCE (%)	17.92%	12.91%
Total Debt/ TNW (times)	0.24	0.43
Total Debt/ OPBDIT (times)	0.79	1.78
Interest Coverage (times)	14.44	25.48
NWC/ OI (%)	27%	30%

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2019)				Chronology of Rating History for the past 3 years				
		Type	Amount Rated (Rs crore)	Amount Outstanding (Rs Crore)	Date &Rating	Date & rating in FY2018		Date & Rating in FY2017		Date & Rating in FY2016
					April 2018	November 2017	April 2017	July 2016	April 2016	-
1	Term Loans	Long-term	165.00	141.90	[ICRA]A+ (Stable)	[ICRA]AA- (Negative)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	-
2	Fund-based Limits	Long-term	97.40	NA	[ICRA]A+ (Stable)	[ICRA]AA- (Negative)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	-
3	Fund-based Limits	Short-term	20.00	NA	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-
4	Non-fund Based Limits	Short-term	13.25	NA	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-
5	Commercial Paper Programme	Short-term	25.00	NA	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	

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 No.	Instrument	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
-	Term Loan 1	June-2016	9.50%	July 2020	55.00	[ICRA]A+ (Stable)
-	Term Loan 2	September-2016	6.70%	September-2021	55.00	[ICRA]A+ (Stable)
-	Term Loan 3	September-2016	5.60%	September-2021	55.00	[ICRA]A+ (Stable)
-	Cash Credit 1	-	-	-	8.40	[ICRA]A+ (Stable)
-	Cash Credit 2	-	-	-	10.00	[ICRA]A+ (Stable)
-	Cash Credit 3	-	-	-	12.00	[ICRA]A+ (Stable)
-	Cash Credit 4	-	-	-	9.00	[ICRA]A+ (Stable)
-	Proposed Cash Credit	-	-	-	58.00	[ICRA]A+ (Stable)
-	Fund-based 1	-	-	-	10.00	[ICRA]A1+
-	Fund-based 2	-	-	-	10.00	[ICRA]A1+
-	Non-fund Based 1	-	-	-	5.25	[ICRA]A1+
-	Non-fund Based 2	-	-	-	3.00	[ICRA]A1+
-	Non-fund Based 3	-	-	-	5.00	[ICRA]A1+
-	Commercial Paper Programme	Not placed yet			25.00	[ICRA]A1+

Source: Indoco Remedies 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.

For more information, visit www.icra.in

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