



Infomerics Valuation and Rating Pvt Ltd

Press Release

Karuna Healthcare Pvt. Ltd.

May 09, 2017

Rating

Instrument	Amount	Rating	Rating Action
Non Convertible Debenture	Rs.160.00 crores	Provisional IVR A(SO)/Stable Outlook (Provisional IVR Single A [Structured Obligation] with Stable Outlook)	Assigned

Details of Instrument are in Annexure 1

Infomerics Valuation and Rating Pvt. Ltd. has assigned **Provisional IVR A(SO)/Stable outlook (Provisional IVR Single A Structured Obligation with Stable Outlook)** rating to the proposed Non-Convertible Debenture (NCD) issue of Rs.160.00 crores of Karuna Healthcare Pvt. Ltd. (KHPL). Instruments with this rating are considered to have adequate degree of safety regarding timely servicing of financial obligations. Such instruments carry low credit risk.

The final rating shall be assigned after compliance of various terms and conditions.

Detailed Rationale

The rating derives strength from the proposed unconditional & irrevocable guarantee of Mr. Arun Kumar Pillai, the main promoter, and the five entities belonging to promoter group having sizeable amount of unencumbered equity stake in two major listed group pharmaceutical companies (Strides Shasun Ltd. and Sequent Scientific Ltd.), backed by a defined structure, and current equity cover (as on March 31, 2017) of 4.29 times. In addition, the guarantors also have investments in shares of certain unlisted companies. The transaction documents provide for an implied stable cover of about 2.25 times in the form of unencumbered equity investments, even in case of adverse market volatility, subject to pledge trigger events and other terms and conditions in the definitive documents. Vistara ITCL India Ltd. (formerly IL&FS Trust Co.), a reputed company in the Indian trusteeship industry, monitoring the implementation of the proposed transaction in its capacity as the trustee also



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supports the rating. The rating also takes into account the recent incorporation of KHPL as a group investment company, equity market volatility and presence of significant keyman risk. Performance of the shares of Strides Shasun Ltd. (Strides) and Sequent Scientific Ltd. (Sequent) and effective implementation of the proposed structure shall be the key rating drivers in the medium term.

List of Key Rating Drivers

Rating Strengths

- Unconditional and Irrevocable guarantee of five corporate entities belonging to promoter group and the main promoter.
- The guarantors are having sizeable amount of unencumbered equity stake in two major listed group pharmaceutical companies, Strides and Sequent. Strides has been successful in developing niche and complex pharmaceutical products across wide dosage formats, and has significant growth potential in Australia, North America and Sub Saharan Africa, besides India.
- Defined debt servicing structure interalia providing adequate unencumbered asset cover.
- Presence of a reputed Trustee company to monitor the implementation of the debt servicing structure.

Rating Weaknesses

- Issuing company having been incorporated recently.
- Volatility in the equity market.
- Significant keyman risk.

Detailed Description of Key Rating Drivers

The servicing of the proposed NCDs shall be unconditionally and irrevocably guaranteed by Mr. Arun Kumar Pillai, the main promoter, and five group companies.



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The aforesaid guarantors collectively have unencumbered aggregate equity stake of 15.49% in Strides and 42.33% in Sequent, as on March 07, 2017. Given the market capitalisation of Strides of about Rs.9808 crores and of Sequent of about Rs.3141 crores as on March 31, 2017, the aggregate market value of the aforesaid unencumbered equity investment is arrived at Rs.2829.33 crores, as on that date. In addition, the guarantors also have investments in shares of certain unlisted companies across a diversified mix of sectors.

Based on the market value of aforesaid equity investment as on March 31, 2017, there is an implied cover to the extent of 4.29 times which, after sensitising the same for various stressed scenarios including 50% fall in price, comes to 1.86 times. The transaction documents provide for an implied stable cover of about 2.25 times in the form of unencumbered equity investments, even in case of adverse market volatility, subject to pledge trigger events and other terms and conditions in the definitive documents.

As per proposed debt servicing structure, the money required for debt servicing is to be deposited into a dedicated bank account five business days before the coupon payout date and a month before the principal redemption date. Each guarantor has undertaken to make all payments and discharge all obligations of the issuer owing to the NCD holders. All obligations of the guarantors are joint and several. In case of any insufficiency of fund, the trustee to the NCD issue, acting on the instructions and on behalf of the NCD holders, will have a set of rights to act upon (including invocation of guarantee). The debt servicing structure shall be backed by a Trust Deed and Guarantee Deeds, duly vetted by an independent legal counsel.

Strides is a vertically integrated global pharmaceutical company headquartered in Bengaluru. It has global manufacturing footprint with 14 facilities across India, Europe and Africa (including six US FDA approved facilities). The Company focuses on developing niche and complex pharmaceutical products across wide dosage formats for regulated and emerging markets. Given the above mentioned focus, it has often engaged in acquisition and divestments to achieve its strategy. As of now, it has businesses with significant growth potential in Sub Saharan Africa, Australia and North America, besides India.



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Vistra ITCL (India) Ltd. (Vistra ITCL), a SEBI approved debenture trustee, is proposed to be appointed as the Trustee for the transaction. Vistra ITCL, formerly known as IL&FS Trust Co. Ltd. established in 1995, is the largest independent corporate trustee in India.

KHPL was incorporated a couple of months back to act as a group investment company to arrange funds deployment majorly in various manufacturing entities of the group. It does not have any distinct revenue model of its own.

Mr. Arun Kumar Pillai is the main person in the Strides group providing the strategic direction to the companies. The markets also derive comfort from his presence in charting the growth path for these two companies, in particular. Thus, the continued presence of Arun Kumar is a key imperative for the sustainable growth of these companies, indicating a significant keyman risk.

Indian capital market, by its nature, is volatile arising out of many developments taking place in the social and economic front both at the national and international levels. Despite of particular equity scrip continues to remain fundamentally strong, the market price of such scrip may get adversely impacted due to the market behaviour. As the collateral cover for debt servicing, in the instant case, is in the form equity investment in two listed companies, the same is exposed to the risk of market volatility. However, such risk is proposed to be ring fenced by way of adequate additional cover as highlighted earlier.

Analytical Approach

While arriving at the aforesaid provisional rating by Infomerics, it has taken into consideration the credit enhancement by an unconditional and irrevocable guarantee by Mr. Arun Kumar Pillai, the promoter of the group, and five group business entities whose main assets are in the form of equity investments in Strides and Sequent, two major listed companies of the group.

Applicable Criteria

Rating Methodology for Manufacturing Companies

Financial Ratios & Interpretation



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About the company

KHPL is a part of the Bengaluru based Strides group with Strides and Sequent, being the two major companies which are listed in BSE and NSE. KHPL is essentially an investment company of the Strides group incorporated recently. Strides is a vertically integrated global pharmaceutical company headquartered in Bengaluru. The Company focuses on developing niche and complex pharmaceutical products across wide dosage formats for regulated and emerging markets. Sequent is an integrated pharmaceuticals company with presence in Human and Animal Active Pharmaceutical Ingredients (APIs) and veterinary formulations. Shri Arun Kumar Pillai, the promoter of the group, and Shri Abhaya Kumar, Executive Director in Strides, are the pivots for providing strategic guidance to the group.

During FY16 (refers to April 01 to March 31), the Strides reported a PAT of Rs.208.9 crores on Total Income of Rs.3156.4 crores. Sequent reported a Net Loss of Rs.22.2 crores on Total Income of Rs.634.5 crores during the aforesaid period.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Nil.

Rating History for last three years: Nil.

Note on complexity levels of the rated instrument: Infomerics has classified instruments rated by it on the basis of complexity and a note thereon is available at www.infomerics.com.

Name and Contact Details of the Rating Analyst:

Name: Shri Sarnambar Roy

Tel: (022) 40036966

Email: sroy@infomerics.com

About Infomerics:

Infomerics commenced rating & grading operations in April 2015 after having spent over 25 years in various segments of financial services. Infomerics is registered with the Securities and Exchange Board of India (SEBI) and is gradually gaining prominence in domestic rating and/or grading space. Infomerics is striving for positioning itself as the most trusted & credible rating agency in the country and is gradually widening its product portfolio.



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Company's long experience in varied spectrum of financial services is helping it to fine tune its product offerings to best suit the market.

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Annexure 1: Details of Instrument

Name of Instrument	Date of issuance	Coupon Rate	Maturity Date	Size of issue (Rs. Crores)	Rating Assigned/ Outlook
Non Convertible Debenture	Not yet placed	Coupon – 4.5% IRR – 10-15.5%, backed by a pricing formula (indicative)	January 31, 2020	160.00	Provisional IVR A(SO)/Stable Outlook (Provisional IVR Single A [Structured Obligation] with Stable Outlook)