RATING REPORT

P.D.H Laboratories (Private) Limited

REPORT DATE:
December 31, 2019

RATING ANALYSTS:
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RATING DETAILS		
	Initial Rating	
Rating Category	Long-term	Short-term
Entity	BB+	B
Rating Outlook	Stable	
Rating Date	December 30, 2019	

COMPANY INFORMATION	
Incorporated in 1970	**External auditors:** Baker Tilly Mehmood Idrees Qamar, Chartered Accountants
Private Limited Company	**Chairman & CEO:** Mr. Sheikh M. Ilyas
Key Shareholders (with stake 5% or more):	**Managing Director:** Mr. Mohsin Ilyas Sheikh
- Mr. Faizan Ghani ~ 66.0%	
- Ms. Yasmin Ilyas ~ 24.3%	

APPLICABLE METHODOLOGY(IES)
Applicable Rating Criteria: Industrial Corporates (May, 2016) ***http://www.vis.com.pk/kc-meth.aspx***

P.D.H Laboratories (Private) Limited

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

In 1970, P.D.H Laboratories (PDH) was incorporated as a Private Limited Company. PDH is engaged in the production and sale of pharmaceutical products.

Financial Statements of the company for FY19 were audited by Baker Tilly Mehmood Idrees Qamar, Chartered Accountants.

Financial Snapshot

Net Equity: June 2019: Rs. 224.1m, June 2018: Rs. 113.8m

Net Revenue: FY19: Rs. 457.6m, FY18: Rs. 229.0m

RATING RATIONALE

P.D.H Laboratories (Private) Limited (PDH) is a small but growing player in the pharmaceutical sector. The Company has been engaged in the manufacturing and sale of pharmaceutical products for around five decades. Broadly, the business portfolio includes human and animal healthcare products. PDH's major (~90%) shareholding is vested between Mr. Faizan Ghani and Ms. Yasmin Ilyas while remaining stake is held by four other family members. Lately, in line with long-term business growth plan and revised business strategy, the company has revamped its management team structure which primarily includes the appointment of experienced professionals at senior level management.

Registered head office and production facility is located in Sheikhupura Road, Lahore. The plant is well equipped for producing medicines in Liquid Injections (Ampoules/Vial), Dry Powder Injection (Cephalosporin and Penicillin), Ointment/Creams (Steroidal) and Drenches (Veterinary). However, PDH is currently manufacturing Ampoules and Vials only. Total annual capacity of manufacturing Ampolues and Vials stand at ~85m units while combined capacity utilization of both segments was reported at 63% during FY19. Sales team comprises a formal sales structure with a national sales manager, distribution managers and a field force of around 20 representatives catering mainly to retailers. Over the medium term, management plans to enter in semi-promotional activities alongside expanding sales force.

Key Rating Drivers

Business risk profile is supported by non-cyclical nature of the industry and steady projected demand growth.

Given the non-cyclical nature of the pharmaceutical sector with relatively stable (inelastic) demand, revenues of pharmaceutical industry are likely to remain unaffected by the economic downturns. Sales of the sector are supported by growing population and increasing life expectancy (implying increase in elderly population) and continuous emergence of diseases. Thus the business risk of the sector is considered to be low. However, impact on margins due to rupee devaluation and significant dependence on Drug Regulatory Authority of Pakistan (DRAP) for hardship cases and new product launches continue to remain the key rating sensitivities.

Growing product portfolio & therapeutic coverage

Of total 8 therapeutics areas, top four leading revenue generating are Vitamins (29%), Penicillin (28%), Cephalosporin (16%) and (15%) Analgesics/Anti-inflammatory agents which represented more than four-fifth of revenue base in FY19. Product-wise concentration in sales is high with two-fifth of revenues emanating from top five injectable brands (Apoclox, Dolnot, Vibion, Sonnet and Ferrodin). Going forward, in line with management's strategy to expand product portfolio, 14 new product launches are planned. Over the rating horizon, addition of new product is expected to facilitate in reducing product concentration risk and achieving planned growth in sales.

Sales depicted healthy growth in the outgoing year mainly on the back of increased capacity utilization. Going forward, growth in revenues will primarily be a function of new products launches. VIS expects significant increase in sales over the rating horizon.

Topline of the company depicted significant growth in FY19, amounting to Rs. 457.6m (FY18: Rs. 229.0m). Increase in sales was due to improved capacity utilization, efficient human resource management and focused sales efforts. These measures facilitated in reduced fixed cost per unit which resulted in higher gross margins of 46.3% (FY18: 23.9%) in FY19. On the administrative cost front, overheads have increased but have remained at a similar proportion to sales. Finance cost also increased considerably on the back of higher debt utilization and increase in benchmark rates. Nevertheless, bottom line profitability witnessed considerable improvement on account of higher operating margins. Profit after tax was reported at Rs. 110.3m (FY18: Rs.1.4m) in FY19. Going forward, profitability growth will primarily be a function of higher sales. Net sales (Jul'19 to Oct'19) were reported at Rs. 234.0m.

Debt servicing cushion is expected to remain modest due to sizeable debt repayments. Cash flow coverage of outstanding debt is low.

Given significant improvement in bottom line, Funds from Operations (FFO) has increased to Rs. 139.4 (FY18: Rs. 6.5m) in FY19. Resultantly, FFO in relation to long term and total debt were reported higher at 8.3% (FY18: 0.9%) and 7.7% (FY18: 0.8%), respectively. However, cash flow coverages continue to be on the lower side. Debt service coverage ratio (DSCR) was reported at 1.0x (FY18: 1.0x). Assessment of liquidity profile is supported by expected improvement cash flow generation ability and adequate coverage of short term borrowings by way of inventory & receivables. Trade debts in relation to sales have increased on a timeline basis and stood at 38.6% (FY18: 25.1%) at end-FY19. Ageing profile of trade debts is considered manageable with a very limited proportion of receivables being overdue for over three months.

Leverage indicators are expected to remain elevated

Total interest bearing debt of the company amounted to Rs. 1.8b (FY18: Rs. 816m; FY17: Rs. 84.5m) as at end-FY19; out of which 93% constitutes long term debt. Annual principal repayments stand at Rs. 335m for the next three years.

Loan Type	Term Finance I	Term Finance II	Term Finance III
Amount	Rs. 700m	Rs. 850m	Rs. 125m
Term rate	3M KIBOR + 4.0%	3M KIBOR + 4.0%	3M KIBOR + 4.0%
Disbursement Date	April 2018	April 2019	May 2019
Payments	Annual payments	Annual payments	Annual payments
Tenure	Five years	Five years	Five years

Leverage indicators remain significantly higher levels on account of low equity base and increased debt levels. Gearing and leverage ratios were reported at 8.12x (FY18: 7.18x) and 8.92x (2018: 8.01x) respectively at end-FY19.

Financial Summary (amounts in PKR millions)			Appendix I
	FY17	**FY18**	**FY19**
BALANCE SHEET			
Paid Up Capital	48.0	48.0	48.0
Total Equity (without surplus revaluation)	112.4	113.8	224.1
INCOME STATEMENT			
Net Sales	220.3	229.0	457.6
Profit Before Tax	5.0	6.0	116.0
Profit After Tax	2.0	1.4	110.3
RATIO ANALYSIS			
FFO	8.1	6.5	139.4
Current Ratio (x)	1.5	2.9	4.6
Gearing (x)	0.7	7.2	8.1

RATING SCALE & DEFINITION — Appendix II

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES	Appendix III
Name of Rated Entity	P.D.H Laboratories (Private) Limited
Sector	Pharmaceutical
Type of Relationship	Solicited
Purpose of Rating	Entity
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
12/30/2019	BB+	B	Stable	Initial

Instrument Structure	NA
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.
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