RATING REPORT

OBS Pakistan (Private) Limited

REPORT DATE:
August 23, 2023
RATING ANALYST:
Saeb Muhammad Jafri
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RATING DETAILS		
	Current Rating	**Previous Rating**
Rating Category	**Long-term**	**Long-term**
Sukuk	A+	A+
Rating Date	*August 23, 2023*	*April 18, 2023*
Rating Outlook	Stable	Stable
Rating Action	Final	Preliminary

COMPANY INFORMATION	
Incorporated in 2021	**Group Chairman:** Mr. Tariq Moinuddin Khan
Private Limited Company	**CEO:** Mr. Muhammad Kamran Mirza
Key Shareholder:	**External Auditors: Grant Thornton**
AGP Limited- 85% as of August 18, 2023	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria Methodology – Industrial Corporates (May 2023)
https://docs.vis.com.pk/docs/CorporateMethodology.pdf

APPLICABLE RATING SCALE(S)
VIS Issue/Issuer Rating Scale:
https://docs.vis.com.pk/docs/VISRatingScales.pdf

OBS Pakistan (Private) Limited

OVERVIEW OF THE INSTITUTION

OBS Pakistan (Private) Limited (OBS-Pak), was incorporated in December'2021. The Company is a subsidiary of AGP Limited. Ultimate parent company is West End 16 Pte Limited, Singapore.

The Company commenced operations in April 2023 following the acquisition of 17 pharmaceutical brands from Viatris Inc. and Pfizer Pakistan.

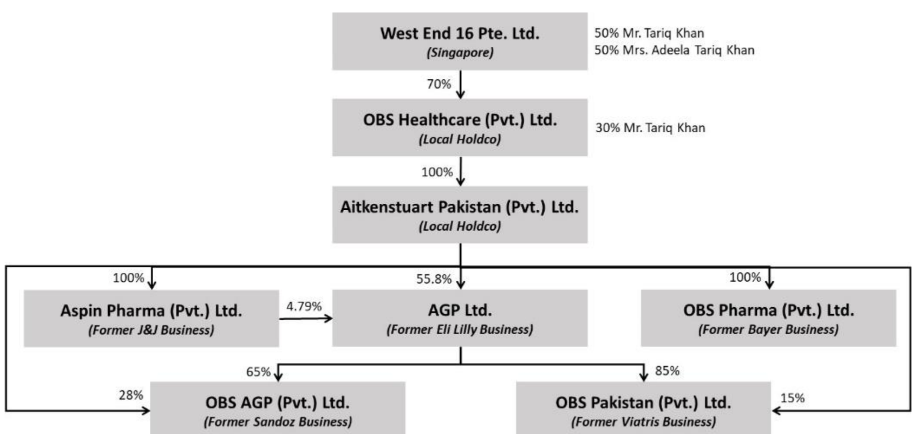
Profile of Board Chairman:

Mr. Tariq Moinuddin Khan is the founder and CEO of OBS Group. He carries over four decades of domestic and international professional experience. Mr. Khan is a graduate of Concordia University Canada and acquired Post Graduate Diploma from McGill University and Certified Public Accountant designation from USA.

RATING RATIONALE

Sponsor Profile

AGP Limited (AGP) is a public listed local pharmaceutical company engaged in manufacturing and marketing of medicines (of its own brands and under licensing arrangements with other companies) for over three decades. Few recognized brands include Rigix, Ceclor, Osnate-D, Anafortan, Keflex etc. Major shareholding of the company (55.8%) is held by Aitkenstuart Pakistan (Private) Limited (APPL) which is a wholly owned subsidiary of OBS Healthcare (Private) Limited. OBS group, as explained in the illustration below, has strong presence in the pharmaceutical industry and currently operates in the country via five companies i.e., AGP Limited, Aspin Pharma (Private) Limited, OBS AGP (Private) Limited, OBS Pakistan (Private) Limited and OBS Pharma (Private) Limited. AGP Limited has 3 manufacturing facilities while Aspin Pharma (Private) Limited and OBS Pharma (Private) Limited have one each. Four of OBS Group's manufacturing facilities are located in Karachi while one is in Lahore. The shareholding structure of the group is as follows:



Purpose of the SPC and Financing Structure

Revised Financing Cost Rs. 9.3b	Sukuk of Rs. 3.6b	Sukuk of Rs. 3.3b	Equity investment of Rs. 2.4b
Pattern of Shareholding of OBS Pakistan (Pvt.) Limited			
Existing		**Ultimate**	
Aitkenstuart Pakistan (Pvt.) Limited	15%	AGP Limited	Up to 92.5%
AGP Limited	85%	Other Shareholders	7.5%

OBS Pakistan (Private) Limited (OBS-Pak) was incorporated in December'2021 and entered into an asset purchase agreement in June'22 with Viatris Inc. and Pfizer Inc.

to acquire a portfolio of pharmaceutical products. The total funding requirement for the acquisition is estimated at PKR 9,300 mn with payments being remitted to Viatris Inc. on weekly basis with the approval of the State Bank of Pakistan. The acquisition is being 75% financed of debt resources (Rs. 6.9b) and the remaining through equity injection (Rs. 2.4b). OBS-Pak is currently 85% owned by AGP; however, AGP's shareholding will ultimately increase to up to 92.5%.

OBS-Pak commenced operations in April 2023. The company is now going through a 2-year transition period during which the transfer of Marketing Authorizations (MA) will take place. During the transition period, OBS-Pak will source all locally manufactured/imported products from Pfizer Pakistan Limited. Upon the transfer of MAs, it has been planned to commence local manufacturing of majority products at AGP's manufacturing facilities for which sufficient capacity is available and AGP will incur minimum capex to commence the operations.

The debt portion will be arranged through the issuance of two Sukuk instruments of Rs. 3.6 bn and Rs. 3.3 bn. The tenor of both facilities is 7 years with a grace period of 18 months. Specific terms of the 1st Sukuk include:

- Interest rate applicable on the Sukuk shall be the 3M KIBOR plus 1.60% (previously 1.75%) spread with principal payment to be redeemed over 22 quarters (previously 18 quarters). Profit payment will also be made quarterly in arrears with the first profit payment being due 3 months from the disbursement date.
- Security Structure entails exclusive hypothecation charge on future fixed assets of OBS-Pak.
- Pledge of AGP's shares by Aitkenstuart Pakistan (Pvt.) Limited, the major shareholder, of AGP inclusive of 40% security margin.
- Corporate Guarantee from AGP for the Outstanding Issue Amount plus Profit.
- Collection Account to be maintained under lien in which all revenue of OBS-Pak will flow.
- Financing Payment Account (FPA) to be filled in with upcoming installment amount (Principal + Profit) 2 working days prior to installment due date. The FPA shall be reset to zero after settlement of each installment and shall be replenished in the same manner subsequently.

OBS-Pak is distributing its products through Muller & Phipps Pakistan (Pvt) Limited which is the largest pharmaceutical distributor in Pakistan. They have presence in 950+ towns with 67 depots and over 900 owned vans. This has significantly enhanced the availability of the acquired brands across the country.

Key Rating Drivers

Strong sponsor strength along with financial support

Assigned ratings take comfort from the Parent Company's (AGP) established market position, long track record in the pharmaceutical industry and the resulting operational, managerial and financial support available to OBS Pakistan. AGP had an annual consolidated turnover of Rs. 14.5b (2021: Rs. 9.3b) in 2022 with continuous growth recorded in sales and sufficient liquidity profile. Ratings incorporate AGP's healthy cash flows and low leveraged capital structure on a consolidated and stand-alone basis. AGP's consolidated equity base amounted to Rs. 11.1b (2021: Rs. 10.2b) at end-2022.

AGP Standalone (Rs. In m)	**CY21**	**CY22**
DSCR	2.8	3.1
FFO	1,985	1,671
Debt Servicing (consolidated)	(607)	(605)
Capex (consolidated)	(479)	(914)
Amount left	898	152
AGP Consolidated (Rs. In m)	**CY21**	**CY22**
DSCR	3.1	2.3
FFO	2,337	2,049
Debt Servicing	(607)	(605)
Capex	(479)	(914)
Amount left	1,251	530

AGP Limited Consolidated (Rs. In m)	**CY21**	**CY22**
Net Sales	9,316.8	14,458.8
Gross Margin (%)	54.3%	50.7%
Net Margin (%)	19.8%	11.8%
PAT	1,846.0	1,704.8
FFO to Total Debt (%)	75.3%	62.3%
Gearing (x)	0.31	0.30
Leverage (x)	0.46	0.49
DSCR	3.12	2.30
Consolidated FFO	2,337.4	2,049.0
Debt Servicing	(606.8)	(604.8)
Capex	(479.4)	(914.2)
Total Debt	3,103.2	3,288.6
Total Equity	10,161.3	11,131.1

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

Given the non-cyclical nature of the sector with relatively stable (inelastic) demand, revenues and profitability of pharmaceutical industry are likely to remain unaffected by economic downturns, however, currency volatility will continue to impact margins. Sales of the sector are supported by geographical diversification, growing population and continuous development of new products to treat diseases. Thus, the business risk of the sector is considered to be on the lower side. Regulatory risk including changes in pricing policies and sharp rupee devaluation (a major portion of raw material is imported) remain key challenges for the sector.

Despite concentrated product portfolio and therapeutic coverage, strong market presence provides comfort to the ratings.

Product portfolio being acquired caters primarily to 6 broad therapeutic segments, Cardiology, Anti- Hypertensive, Anti- Epileptics, Ocular Hypertension and Urinary Incontinence. For the current year, around 79% of the current year's revenue contribution is expected to originate from locally manufactured products, while imported products will contribute to the remaining 21% of the revenue base.

In line with actual sales mix during the last two years (2021 and 2022), projected product-wise concentration in sales will continue to be on the higher end with around 60% of revenues emanating from one brand- Norvasc followed by Zoloft (~10%) and Cardura (~10%). Comfort is drawn from Norvasc and Cardura possessing sizeable market share of 41% and ~88%, respectively in FY23. As per the management, future business strategy will focus on volumetric sales growth of existing brands) as well as introduction of new products, SKUs and combinations. Revenue growth projected for the transition period also draws comfort from the supply prices being locked under the agreement with Viatris and Pfizer during the transition period.

The Company is focusing on enhancing sales by appointing M&P as the primary distributor, enhancing the team strength, increasing the number of cities under coverage, enhancing marketing and promotional activities and new product launches.

Gradual growth in profitability indicators is expected on the back of expected increase in prices and uptick in volumetric sales planned through line extensions and new product launches over the rating horizon.

Projected growth in revenue is expected to emanate from increase in selling prices along with volumetric growth (conservative approach to projected unit growth has been assumed) planned through organic growth and line extensions in the current product portfolio over the rating horizon. Actual and projected gross margins of the product portfolio compare favorably to other pharmaceutical players as all products command high margins with Norvasc having the highest sales contribution as well as highest margin. As per the company's financial projections, GMs are projected at around 68%. While risk of variation in product pricing is mitigated through pre-agreed product costs locked in for the 2-year transition period, currency volatility risk will continue to prevail. The Company has projected higher selling and administrative expenses along with elevated finance costs due to borrowings. However, the management projects gradual improvement in the same through timely reduction of debt. Achieving projected profitability levels post the locked margin transition period is considered important from a ratings perspective.

Adequate projected debt servicing over the rating horizon, further supported by Corporate Guarantee. Liquidity indicators also depict improvement over the long-term. Projected profit retention and annual debt repayments are expected to result in improvement in leverage indicators.

With overall debt quantum reducing, cash flow coverages depict improvement. Debt servicing also remains adequate with DSCR ranging between 1.2-1.5x over the rating horizon, however, the same shall remain exposed to interest rate and exchange rate volatility impact. However, debt repayment capacity is enhanced through corporate guarantee of AGP for the entire principal and profit amount of the Sukuk and remains a key rating driver. Improvement in the liquidity profile is considered important from a ratings perspective.

Equity base of the company is projected to stand at Rs. 2.7b at end-Dec'23 after equity injection for the acquisition. With elevated debt levels to finance the acquisition, leverage and gearing levels are expected to be reported on the higher side. However, the same are expected to gradually decrease through timely debt repayments and augmentation in equity base by profit retention. Ratings remain dependent on maintaining sound debt servicing cushion and reducing leverage indicators in line with projections over the rating horizon.

REGULATORY DISCLOSURES	Appendix I
Name of Rated Entity	OBS Pakistan (Private) Limited
Sector	Pharmaceutical
Type of Relationship	Solicited
Purpose of Rating	Sukuk Rating
Rating History	see table below

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
Rating Type: Sukuk				
23-08-2023	A+	-	Stable	Final
18-04-2023	A+	-	Stable	Preliminary
23-09-2022	A+	-	Stable	Preliminary

Instrument Structure	OBS Pakistan is in process of issuing a Rated, Secured and Privately Placed Sukuk Issue of up to Rs. 3.6b. Disbursement of the Sukuk has commenced and the funds are being used to finance the acquisition of 17 pharmaceutical brands from Viatris Inc. which were being marketed by Pfizer Pakistan. The tenor of the Sukuk is 7 years with a grace period of 18 months. The issue offers quarterly profit payments with a base rate of 3-Month KIBOR plus a spread of 1.60% per annum. The Sukuk is secured with exclusive hypothecation charge on future fixed assets of OBS-Pak, pledge of AGP's shares inclusive of 40% security margin, corporate guarantee of AGP on the principal and profit payments, lien on collection account through which all revenue would flow and formation of a Financing Payment Account (FPA) in which upcoming installment (profit+ principal) will fall 2 working days prior to the due date.
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.
Probability of Default	VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.
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Due Diligence Meetings Conducted

S.No.	Name	Designation	Date
1.	Bosco Firmin	Dep. General Manager Investments & New Ventures (OBS Group)	March 27, 2023