RATING REPORT

OBS Pakistan (Private) Limited

REPORT DATE:
November 05, 2024

RATING ANALYSTS:
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RATING DETAILS

Rating Category	Current Rating Long-term	Current Rating Short-Term	Previous Rating Long-term	Previous Rating Short-Term
Entity Long-term	A	A2	A	A2
Rating Date	*November 05, 2024*		*September 25, 2023*	
Outlook/Rating Watch	Stable		Stable	
Rating Action	Reaffirmed		Reaffirmed	
Sukuk 1	A+	-	A+	-
Rating Date	*November 05, 2024*		*August 23, 2023*	
Outlook/Rating Watch	Stable		Stable	
Rating Action	Reaffirmed		Final	
Sukuk 2	A+	-	A+	-
Rating Date	*November 05, 2024*		*February 28, 2024*	
Outlook/Rating Watch	Stable		Stable	
Rating Action	Reaffirmed		Final	

COMPANY INFORMATION

Incorporated in 2021	**Group Chairman:** Mr. Tariq Moinuddin Khan
Private Limited Company	**CEO:** Mr. Muhammad Kamran Mirza
Key Shareholder/s (with stake 5% or more):	**External Auditors:** Grant Thornton Anjum Rahman
AGP Limited- 91.82%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria Methodology – Industrial Corporates
https://docs.vis.com.pk/docs/CorporateMethodology.pdf
Rating the Issue
https://docs.vis.com.pk/docs/Rating-the-Issue-Aug-2023.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	RATING RATIONALE

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.

Profile of Group Chairman:

Mr. Tariq Khan is the founder and sponsor shareholder of OBS Group. Under his leadership, in a span of 18 years, OBS has grown to become Pakistan's 8th largest pharmaceutical company.

Profile of CEO:

Mr. Muhammad Kamran Mirza holds an undergraduate degree in commerce and an MBA from the Institute of Business Management (IoBM). He has over 14 years of experience in financial markets, focusing on sell-side and buy-side investment advisory. Before joining OBS Group in 2018, he served as EVP and Head of Investment Banking at JS Bank and currently holds board positions at

Company Profile

OBS Pakistan (Private) Limited ("OBS Pakistan" or "the Company") was incorporated on December 07, 2021, as a private limited company. The Company's primary business activities include the import, marketing, export, dealership, distribution, and wholesale of various pharmaceutical products. OBS Pakistan is a subsidiary of AGP Limited (AGP), the parent company, which holds a 91.82% ownership stake in the Company.

Operations commenced in April 2023 following the acquisition of 17 pharmaceutical brands from Viatris Inc. and Pfizer Pakistan, with 10 brands actively marketed. Of these, 3 are locally manufactured and 7 are imported. The acquisition was financed through 73% debt and 27% equity, with the debt portion raised through two sukuks of Rs. 3,600 mn and Rs. 2,900 mn, respectively.

Post-acquisition, the Company has been in a two-year transition period during which the transfer of brand marketing authorizations is ongoing. OBS Pakistan continues to source all locally manufactured and imported products from Pfizer Pakistan, except for Norvasc. After the transfer, the Company plans to gradually begin local manufacturing of most products at AGP's facilities. As of August 2024, Norvasc is already being produced at these facilities, with plans to begin manufacturing other products in the near term.

Auditors' Report

The CY23 financial statements were audited by Grant Thornton Anjum Rahman, categorized as 'Category A' on the SBP's Panel of Auditors. The auditor issued an unmodified and unqualified opinion on the financial statements.

Industry Update

The Pakistani pharmaceutical market comprises around 650 companies, with less than 26.0% being multinational. The industry contributes approximately 1.0% to the country's GDP and grew by 15.0% over the past year, reaching an estimated $3.0 bn. Local companies dominate the market with a 74.0% share, while multinationals hold the remaining 26.0%. The top 25 companies account for 74.0% of the market, and the top 50 make up 90.0%. Approximately 11,000 drugs are actively marketed in Pakistan, and sold through licensed pharmacies based on prescriptions. The Drug Regulatory Authority of Pakistan (DRAP) regulates the *several OBS Group companies.*

sector, overseeing medicine registration, manufacturing site approvals, and the setting of Maximum Retail Prices (MRP).

The industry heavily relies on imports, with over 90.0% of raw materials sourced from abroad and only 10.0% of Active Pharmaceutical Ingredients (API) produced locally. This reliance exposes the sector to risks from currency devaluation, inflation, and rising utility costs. Price controls further compress profit margins, leading to the exit of some multinational companies. However, recently in February 2024, the government deregulated drug prices for medicines not listed on the National Essential Medicines List (NEML). Previously, price increases were capped based on the Consumer Price Index (CPI). Now, non-essential medicines can be priced without regulatory caps, potentially benefiting companies with a significant proportion of non-essential drugs.

According to data from IQVIA, a healthcare analytics firm, Pakistan's pharmaceutical industry recorded sales of Rs. 916.0 bn in FY24, reflecting a 24.0% year-on-year (YoY) increase in rupee terms. The fourth quarter of FY24 saw the highest-ever quarterly sales of Rs. 237.0 bn, representing a 25% increase compared to the same period last year (SPLY). Of this growth, approximately 20.0% was driven by price increases, while the remaining 5% resulted from volumetric gains. The price increase was influenced by the one-time price adjustment allowed by DRAP in May 2023 to absorb the significant rupee devaluation.

Sponsor Profile

AGP Limited (AGP) is a publicly listed pharmaceutical company in Pakistan that has consistently grown by manufacturing and marketing products under licensing arrangements with several reputable multinational pharmaceutical companies, as well as developing and marketing its own brands. Some of its well-recognized brands include Rigix, Ceclor, Osnate-D, Anafortan, and Keflex. The majority shareholding of the company (~55.8%) is held by Aitkenstuart Pakistan (Private) Limited (APPL), a wholly owned subsidiary of OBS Healthcare (Private) Limited.

Following its acquisition, AGP focused on growth, process efficiency, and productivity, leading to significant improvements in the business. The company's revenue stands at Rs. 13.9 bn in CY23 (CY22: Rs. 10.3 bn), representing a YoY growth of 35.0%. Moreover, total equity was reported to be Rs. 10.9 bn (Dec'22: Rs. 10.2 bn), while total debt amounted to Rs. 3.5 bn (Dec'22: Rs. 785.7 mn) by end-Dec'23. Subsequently, AGP's gearing and leverage ratios stood strong at 0.32x (CY22: 0.08x) and 0.57x (CY22: 0.25x) respectively in CY23.

The OBS Group, comprising five companies, holds a strong position in Pakistan's pharmaceutical industry: AGP Ltd, Aspin Pharma, OBS AGP, OBS Pakistan, and OBS Pharma. The Group's operations are supported by five manufacturing facilities, four located in Karachi and one in Lahore. Of these facilities, four are focused on the production of pharmaceuticals, while one is dedicated exclusively to the production of nutraceuticals.

Product Portfolio of the Company

The acquired brands include a range of therapeutic classes, such as anti-depressants and anti-hypertensive medications. OBS Pakistan has 11 actively promoted brands. Among these, Norvasc-V was launched in the ongoing year for the treatment of hypertension and coronary artery disease.

The following table provides details of the 11 brands currently being marketed by the Company.

Sr. No	Brand	Indication
1	Norvasc	Blood Pressure & Coronary disease
2	Zoloft	Anti-Depressant
3	Xalatan	Ocular Hypertension
4	Cardura	Anti-Hypertensive
5	Lyrica	Anti-Epileptics
6	Detrusitol	Urinary Incontinence
7	Efexor	Anti-Depressant
8	Lipitor	Cholesterol
9	Xalacom	Ocular Hypertension
10	Zeldox	Antipsychotics
11	Norvasc-V	Blood Pressure & Coronary disease

Key Rating Drivers

Ratings incorporate low business risk of the pharmaceutical sector

Ratings account for stable demand and low economic sensitivity of the pharmaceutical industry, which ensures steady revenue and profitability. Factors such as population growth, a high incidence of diseases, the emergence of new illnesses, and inadequate hygiene practices are expected to sustain the demand for pharmaceutical products in the country.

However, the pharmaceutical industry in Pakistan faces profitability pressures due to a stringent regulatory framework, including the reliance on the Drug Regulatory Authority of Pakistan (DRAP) for the approval of new products and pricing increases. The Company also encounters challenges in accessing raw materials, with 70.0-80.0% of ingredients sourced from overseas. This results in a significant portion of product costs being denominated in foreign currency, exposing the Company to exchange rate risks.

The recent deregulation of drug prices for Non-Essential Medicines provides companies with the autonomy to independently raise prices, which further supports the business risk profile of the sector.

Strong sponsor profile supported by corporate guarantee

The ratings draw comfort from the strong sponsor profile of AGP Limited, with the Company's debt secured via corporate guarantee from the parent company, further supporting the overall credit assessment.

Strong volumetric gains realized in the current year

During the first six months of CY24, sales volumes recorded a significant uptick compared to CY23, contributing to higher revenues in 6MCY24.

Relatively stable gross margins

In the ongoing transition period following the acquisition, product supply has been committed by Pfizer Pakistan under the terms of the Asset Purchase Agreement (APA). The APA also addresses the risk of cost variability during this period through pre-negotiated product costs. As a result, OBS Pakistan achieved a gross margin of 66.0% in CY23, which also remained fairly stable during 6MCY24. However, despite strong gross margins, profitability was constrained by high financial charges amidst the elevated interest rate environment.

Debt servicing costs related to acquisition financing have taken full effect in the ongoing year and are expected to continue to drag the Company's net profitability in the medium term. However, going forward, management anticipates that supply chain efficiencies will improve, supported by plans to manufacture 5 out of the 7 imported active brands at AGP's facilities. This is expected to contribute positively to the Company's profitability profile over time.

High product concentration

The top five products accounted for ~91.3% of total sales, indicating significant product concentration, while the top product, Norvasc, contributed ~66.2%. The management plans to introduce 4-5 new products in the Cardiometabolic and Hypertension therapeutic areas. Reducing product concentration over time will remain important.

Strong distribution network

During the review period, the Company shifted its distribution to Muller and Phipps (M&P), which has a wider reach across more towns and cities and connects with a larger number of pharmacies, including retail chemists, institutional sales, and e-commerce channels. M&P's network is expected to support the Company's market coverage and operational efficiency.

Debt servicing pressure

The Company's profitability remains constrained due to acquisition-related debt servicing pressures, which have impacted cash flows and strained debt servicing in the first half of CY24. However, margins are expected to improve in the second half of CY24 and beyond, driven by the in-house manufacturing of the Company's flagship product, Norvasc. This shift is projected to enhance the Company's profitability and generate sufficient operational cash flows to meet debt obligations over the next six months and beyond, with the DSCR anticipated to remain within the 1.0x to 1.1x range.

Looking ahead, the Company's liquidity profile is likely to remain constrained, with the current ratio projected to stay below 1.0x due to increased current liabilities arising from the debt-financed acquisition. In addition, since OBS Pakistan is in an expansionary phase, liquidity is to be channeled towards heavy marketing in the medium term. Nonetheless, comfort is derived from the working capital support committed by the parent company. Going forward, maintaining effective liquidity management and enhancing the Company's debt servicing capacity will remain important.

Capitalization profile impacted by acquisition financing

As of Dec'23, OBS Pakistan reported long-term debt (inc. of current maturity) of Rs. 6,339.8 mn. The debt portion of the acquisition financing was raised through two Sukuks, amounting Rs. 3,600 mn and Rs. 2,850 mn respectively. Moreover, by end-Dec'23, OBS Pakistan's total equity amounted to Rs. 2,589.8 mn. Due to the significant debt incurred for the acquisition, the Company's gearing and leverage ratios stood at 2.45x and 2.73x, respectively.

In Feb'24, OBS Pakistan raised another Rs. 50.0 mn through its second Sukuk. As of Jun'24, the Company's total equity increased to Rs. 2,643.7 mn owing to profit retention. With a decrease in total liabilities following a reduction in trade and other payables, the Company's leverage ratio improved to 2.63x, while the gearing ratio stood at 2.48x.

Going forward, the Company's ratings remain sensitive to gradual strengthening of equity base and a reduction in debt levels.

OBS Pakistan (Private) Limited — Appendix I

Financial Summary		
Balance Sheet (PKR Millions)	**CY23A**	**6MCY24M**
Property, plant and equipment	14.85	129.93
Stock-in-trade	262.01	491.90
Trade debts	190.17	211.89
Cash & Bank Balances	40.18	24.73
Other Assets	9,162.37	8,728.15
Total Assets	9,669.58	9,586.60
Creditors	285.84	180.63
Long-term Debt (incl. current portion)	6,339.78	6,545.93
Short-Term Borrowings	0.00	0.00
Total Debt	6,339.78	6,545.93
Other Liabilities	454.17	216.34
Total Liabilities	7,079.79	6,942.90
Paid up Capital	440.00	440.00
Equity (excl. Revaluation Surplus)	2,589.78	2,643.69
Income Statement (PKR Millions)	**CY23A**	**6MCY24M**
Net Sales	1,673.26	1,636.53
Gross Profit	1,103.47	1,122.18
Operating Profit	746.18	837.90
Finance Costs	498.07	762.50
Profit Before Tax	248.11	75.40
Profit After Tax	229.73	53.90
Ratio Analysis	**CY23A**	**6MCY24M**
Gross Margin (%)	65.95%	68.57%
Operating Margin (%)	44.59%	51.20%
Net Margin (%)	13.73%	3.29%
Funds from Operation (FFO) (PKR Millions)	328.99	54.37
FFO to Total Debt* (%)	5.19%	1.66%
FFO to Long Term Debt* (%)	5.19%	1.66%
Gearing (x)	2.45	2.48
Leverage (x)	2.73	2.63
Debt Servicing Coverage Ratio* (x)	1.90	0.86
Current Ratio (x)	1.41	1.17
(Stock in trade + trade debts) / STD (x)	-	-
Return on Average Assets* (%)	2.38%	1.12%
Return on Average Equity* (%)	8.87%	4.12%
Cash Conversion Cycle (days)	26.22	73.41

**Annualized, if required*

A - Actual Accounts

M - Management Accounts

REGULATORY DISCLOSURES — Appendix II

Name of Rated Entity	OBS Pakistan (Private) Limited
Sector	Pharmaceutical
Type of Relationship	Solicited
Purpose of Rating	Entity & Sukuk Rating

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
		Rating Type: Sukuk		
05-11-2024	A	A2	Stable	Reaffirmed
25-09-2023	A	A2	Stable	Reaffirmed
23-09-2022	A	A2	Stable	Initial
		Rating Type: Sukuk 1		
05-11-2024	A+	-	Stable	Reaffirmed
23-08-2023	A+	-	Stable	Final
18-04-2023	A+	-	Stable	Preliminary
23-09-2022	A+	-	Stable	Preliminary
		Rating Type: Sukuk 2		
05-11-2024	A+	-	Stable	Reaffirmed
25-09-2023	A+	-	Stable	Preliminary

Instrument Structure(s)

Sukuk 2:
The second Sukuk, amounting to Rs. 2.9 billion, features a 7-year tenor with an 18-month grace period. It has a profit rate of 3M KIBOR plus a 1.60% spread, with principal payments scheduled over 22 quarters. Profit payments will be made quarterly, commencing three months after the disbursement. The security structure includes the following: mortgage/hypothecation charge on AGP's fixed assets, a corporate guarantee from AGP, and a designated collection account for revenue receipts. Similar to the first Sukuk, the Financing Payment Account (FPA) will be replenished two working days prior to each installment 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.

Disclaimer

Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile.

Due Diligence Meetings Conducted

S.No.	Name	Designation	Date
1.	Mr. Shahzaib Tariq	CFO	Sept 27, 2024
2.	Mr. Bosco Firmin	Dep. GM Investments	
3.	Mr. Aaqib Siddiqui	Sr. Manager Finance	