

RATING REPORT

OBS Pharma (Private) Limited

REPORT DATE:

February 28, 2024

RATING ANALYST:

Shaheryar Khan Mangan

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Preliminary Rating	
Rating Category	Short-term
Instrument Rating	A-1
Rating Date	February 28, 2024
Rating Outlook	Stable
Rating Action	Preliminary

COMPANY INFORMATION

Incorporated in 2022

Board Chairman: Mr. Tariq Moinuddin Khan

Private Limited Company

CEO: Mr. Shahzad Khan

Key Shareholder:

Aitkenstuart Pakistan (Pvt.) Limited – 80%

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria Methodology – Industrial Corporates (May 2023)

<https://docs.vis.com.pk/docs/CorporateMethodology.pdf>

Applicable Rating Criteria: 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 Pharma (Private) Limited

OVERVIEW OF THE INSTITUTION

RATING RATIONALE

OBS Pharma (Pvt.) Limited” was incorporated on November 18, 2022, as a Special Purpose Company (“SPC”) to acquire pharmaceutical brands and a manufacturing facility from Bayer. The Company is a subsidiary of Aitkenstuart Pakistan (Pvt.) Limited. Ultimate parent company is West End 16 Pte Limited, Singapore.

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.

OBS Pharma (Pvt.) Limited (“the Company”) forms part of the OBS group which ranks amongst the top ten local pharmaceutical groups in Pakistan with a group turnover of ~PKR 19bn (in CY22) with four manufacturing facilities located in Karachi and one in Lahore.

The Company is a Special Purpose Company (“SPC”), created to acquire pharmaceutical brands and a manufacturing facility from Bayer AG and its associates. The Company is a subsidiary of Aitkenstuart Pakistan (Pvt.) Limited with 80% shareholding while remaining is held by employees. Ultimate parent company is West End 16 Pte Limited, Singapore. On November 21, 2022, the Company entered into an agreement with Bayer AG and its affiliates for the above-mentioned acquisition, at a cost of Rs 7,000m, which was concluded in July 2023. The acquisition was funded through equity of Rs. 1.75b and a syndicated facility of Rs. 5.125b.

The Target Products acquired had a cumulative revenue of PKR 5,177mn in CY22 (PKR 4,277mn in CY21). The portfolio primarily comprises of women’s healthcare and dermatology products. Some of the well-known brands in the portfolio are Ciproxin, Gravibinan, Travocort, Primolut N amongst others.

Out of the 12 brands acquired, 10 are market leaders in their respective molecular categories. Moreover, in addition to the Target Products, the Seller has also passed on the rights to manufacture two brands of Greenstar Social Marketing (Femi-Ject and Nova-Ject) that are manufactured by Bayer PK.

Mr. Shahzad Khan as the new Chief Executive Officer spearheads the Company. He has about 26 years of experience in the healthcare industry, with the last assignment with CCL Pharmaceuticals as their Managing Director and Chief Executive Officer. The manufacturing facility acquired is spread over 3 acres and is located at Plot 108, Quad-e-Azam Industrial Estate, Lahore. All Target Products are manufactured at Bayer PK’s facility except for Ciproxin and Resochin that are manufactured by Novartis Pharma Pakistan Limited.

S.No.	Rank	Indication	Market Rank	Net Sales (PKR Million)			
				2020	2021	2022	6M 2023
1	Gravibinan	Miscarriage Prevention	1	1,127	1,275	1,571	875
2	Ciproxin	Anti-Infective	2	1,078	1,080	1,298	803
3	Primolut N	Ovulation Suppression	1	847	847	1,100	540
4	Travocort	Dermatology Anti-Fungal	1	546	630	656	391
5	Proviron	Low Testosterone Treatment	1	135	16	174	65
6	Testoviron	Low Testosterone Treatment	2	107	95	121	95
7	Advantan	Eczema and Psoriasis	1	113	118	102	61
8	Resochin	Anti-Malaria	1	56	78	55	-
9	Skinoren	Acne Treatment	1	46	39	49	38
10	Noctamid	Sleep Disorder	1	0	65	28	25
11	Travogen	Dermatology Anti-Fungal	1	15	20	23	17
12	Nerisone	Skin Allergy	1	26	14	2	-

13	Femi-Ject	Contraceptive	N/A	11	0	0	-
14	Nova-Ject	Contraceptive	N/A	33	0	0	-
Total				4,136	4,277	5,177	2,912

Proposed Short Term Sukuk:

As part of the business takeover, the Company had to acquire upfront inventory worth Rs. 3,539m, payment of which is to be made in installments. To fund the upfront inventory payment, the Company is proposing to issue a Short term Sukuk for an amount of Rs 1,500m for a 6 month tenor which will be repaid on maturity through internal cash flows and working capital lines currently under approvals. The profit rate on the instrument is 6 month KIBOR + 1.40% pa. The Sukuk will be secured against first pari passu hypothecation charge over present and future current assets of the Company inclusive of 20% margin.

As of Feb 22, 2024, about Rs. 2.9bn has been paid from internal cash and cash available from the syndicated facility (acquisition funds). The proceeds from the proposed instrument will be used to pay off the remaining installment of Rs. 569m due in Feb 2024 and to replenish the syndicated facility cash flows to pay off the remaining acquisition payments.

The Company is currently in the process of negotiating working capital lines with Banks. As represented by management, sufficient lines are in pipeline with Rs. 1bn expected to be available by end March 2024.

For the purposes of assigned rating, OBS Pharma(Pvt) Limited to provide an undertaking to the Issue / Investment Agent authorizing buildup of 25% of monthly sales in each of the last three months leading up to the maturity of the proposed Short Term Sukuk.

Key Rating Drivers

Strong group profile

Aitkenstuart functions as the holding entity of OBS Group, which possesses ownership of five pharmaceutical enterprises: AGP Limited, Aspin Pharma (Pvt.) Limited, OBS AGP (Pvt.) Limited, OBS Pakistan (Pvt.) Limited, and OBS Pharma (Pvt.) Limited. OBS Group stands as a prominent player in Pakistan's healthcare sector. Established in 2006 through the acquisition of Organon Pakistan via a management buyout, OBS has since forged strategic partnerships with various renowned international pharmaceutical companies, including Merck, Sharp & Dohme (USA), Schering Plough (USA), Eli Lilly (USA), Johnson & Johnson (USA), Mylan (USA), Vifor (Switzerland), Santen Pharma (Japan), Aspen Pharma (South Africa), Alcon (USA), Bio Growing (China), Alliance (UK), Sandoz (Germany), Viatrix (USA), and Bayer (Germany), among others.

Currently, OBS stands among the top ten local pharmaceutical groups in Pakistan, boasting a group turnover of approximately PKR 19 billion (in CY22), with four manufacturing facilities in Karachi and one in Lahore. OBS Group's primary therapeutic focus areas include Oncology, Anti-Infectives, Cardiology, Diabetes Metabolic Disorders, Gastroenterology, Ophthalmology, Respiratory, Women's Health, Hormones, Contraceptives, and Hepatology.

With over 150 pharmaceutical brands in Pakistan and numerous others undergoing registration, OBS exports significant volumes to neighboring countries and is actively expanding its export endeavors.

Sponsor's Indicators (PKR Million)	2020 Audited	2021 Audited	2022 Audited
Net Sales	10,307.23	13,389.85	18,996.96
Gross Profit	7,228.0	5,792.0	9,876.3
Gross Margin	70%	43%	52%
PAT	1,963.7	2,153.5	1,718.1
Net Profit Margin	19%	16%	9%
FFO	2,704.5	3,351.7	2,880.4
Long Term Debt	3,406.8	4,800.3	3,744.9
Short Term Debt	1,419.0	4.0	1,352.6
Total Debt	4,825.9	4,804.3	5,097.5
FFO/ Long Term Debt	0.8	0.7	0.8
FFO/Total Debt	0.6	0.7	0.6
Leverage	0.3	0.3	0.4
Gearing	0.2	0.2	0.2
DSCR	1.7	1.9	1.8
Total Equity	19,956.6	22,009.6	22,893.0
Current Ratio	2.7	3.1	2.1

Ratings incorporate low business risk of the sector

Owing to the non-cyclical characteristics of the sector, which features relatively stable (inelastic) demand, it is anticipated that revenues and profitability within the pharmaceutical industry will remain impervious to economic downturns, although currency fluctuations will persistently influence margins. The sector's sales are supported by an expanding population, and the continuous development of new products for disease treatment. Consequently, sector business risk is deemed to be relatively low. However, regulatory risks, including potential alterations in pricing policies and pronounced devaluation of the rupee (given that a significant portion of raw material is imported) remain a key challenge for the sector.

Rating incorporates strong market presence of product portfolio.

Products acquired are well-established in their respective categories. They have a strong market presence and are regularly prescribed by practitioners. The acquired portfolio consists of 12 products, primarily focused on women's healthcare segment. Out of the 12 products acquired, 10 are market leaders in their respective molecular categories.

Among the product portfolio, Gravibinan (miscarriage prevention), Ciproxin (anti-infective), and Primolut N (ovulation suppression) are the flagship products, each holding a significant market share and enjoying a strong competitive position. Total revenue generated by the acquired portfolio is approximately Rs 5,177 million, with these three products contributing 74% of the total revenue. Hence, signifying high level of concentration risk in the target portfolio, due to its heavy reliance on just three products for overall performance. Nevertheless, these products are well-established brands that command substantial market shares. Gravibinan holds a 99% market share (Market Rank 1), Ciproxin accounts for 12% (Market Rank 2), and Primolut N possesses 98% (Market Rank 1) in their respective markets. Strong brand equity of these products contribute a measure of confidence to sales stability going-forward.

Proven track record of successful acquisitions supports projected growth

Revenues of the target products have exhibited growth at a 5-year Compound Annual Growth Rate (CAGR) of 13%, including the COVID years. In CY22, net sales amounting to PKR 5,177mn and a Gross Profit of PKR 2,434mn were recorded by the acquired brands, while the first six month sales of the Company have been recorded at Rs.2.9bn, Given OBS Group's expansive distribution network in over 60 cities, management aims to substantially increase the coverage of the acquired portfolio, thereby seizing a larger market share. In addition, OBS plans to significantly augment the team size in line with the requirements of the brands, with the aim of achieving an extended reach in marketing and sales efforts. Based on this, management forecasts a net sales growth of ~21% for the acquired portfolio going forward. Moreover, management expects the women healthcare segment to be a major growth opportunity in the pharmaceutical sector, and plans on expanding its reach in this segment by introducing more products in this market.

Over time, Gross Margins are expected to improve mainly due to the reduction in raw material costs on account of change in Active Pharmaceutical Ingredients (API) source. The previous owner of the brands was mandated to source materials from global group companies, which often limited the cost efficiencies. Management represents that subsequent to the transfer of Marketing Authorizations to OBS, the sourcing of API and other raw materials would be re-evaluated to ensure better pricing resulting in improved margins. Margin improvement over the rating horizon will remain important.

Improvement in capitalization indicators over time

Current capitalization indicators are expected to streamline as business projected revenues are achieved and margins realized. We expect that current elevated gearing levels will reduce over time as projected by management. Streamlining of capitalization profile as presented by management will remain important for assigned rating.

Finalization of committed short-term lines will remain a key rating sensitivity.

As per the management, they are in the process of securing working capital lines from banks to the tune of Rs. 2bn. As per the negotiations, they expect Rs 1bn of lines to be formalized by March end and remaining to follow.

For purposes of rating, comfort is drawn from an undertaking from the Company to the Issue / Investment Agent outlining a buildup of sales proceeds up to 25% of monthly sales with the trustee for the last three months before the maturity of the Short Term Sukuk. As per management projections, this buildup will be approximately around Rs 500m till the maturity date. The remaining will be funded through internal cash and available working capital lines. Finalization of working capital lines remain critical.

REGULATORY DISCLOSURES		Appendix I			
Name of Rated Entity	OBS Pharma (Private) Limited				
Sector	Pharmaceutical				
Type of Relationship	Solicited				
Purpose of Rating	Short Term Sukuk				
Rating History	Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
	Rating Type: Short Term Sukuk				
	28-Feb-2024		A-1	Stable	Preliminary
Instrument Structure	<p>Type: Unlisted, Rated, Secured, Privately Placed, Short Term Sukuk Issue to be issued as instrument of redeemable capital under Section 66 of the Companies Act, 2017 and as conferred in Sukuk (Privately Placed) Regulations, 2017.</p> <p>Purpose: To fund the purchase of Inventory/API and support the working capital needs of the company.</p> <p>Amount: Rs. 1,500,000</p> <p>Tenor: 6 months from the date of Drawdown.</p> <p>Profit Rate: Base Rate + up to 1.40% per annum Base Rate is defined as the 6-Month Karachi Interbank Offer Rate (“KIBOR”). The Base Rate will be set 1 (one) business day prior to the Disbursement date.</p> <p>Security: The Sukuk Issue will be secured against First / Joint pari passu hypothecation charge over present and future Current Assets of the Issuer inclusive of 20% Margin.</p> <p>Undertaking: Undertaking from the Company to Issue / Investment Agent outlining a buildup of sales proceeds up to 25% of monthly sales with the trustee for the last three months before the maturity of the Short Term Sukuk.</p>				
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Due Diligence Meetings Conducted	S.No.	Name	Designation	Date	
	1.	Muhammad Kamran Mirza	Director	February 23, 2024	
	2.	Bosco Firmin	Dep. General Manager Investments & New Ventures (OBS Group)	February 21, 2024	