

Om Megashree Pharmaceuticals Limited

Rating

Facilities/ Instrument	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	444.00	CARE-NP BB- [Double B Minus]	Assigned
Short Term Bank Facilities	112.00	CARE-NP A4 [A Four]	Assigned
Total Facilities	556.00 (Five Hundred Fifty Six Million only)		
Issuer Rating*	NA	CARE-NP BB- (Is) [Double B Minus (Issuer)]	Assigned

* The issuer rating is subject to the company maintaining overall gearing not exceeding 3.0x at the end of FY23 (FY refers to the financial year ending mid-July).

Details of Facilities in Annexure-1

CARE Ratings Nepal Limited (CRNL) has assigned the rating of 'CARE-NP BB- (Is)' to Om Megashree Pharmaceuticals Limited (OMPL). Issuers with this rating are considered to offer moderate risk of default regarding timely servicing of financial obligations, in Nepal.

CRNL has also assigned the rating of 'CARE-NP BB-' to the long term bank facilities and 'CARE-NP A4' to the short term bank facilities of OMPL.

Detailed Rationale & Key Rating Drivers

The ratings assigned to OMPL and its bank facilities are primarily constrained by the project implementation risk and stabilization risk thereafter associated with its under-construction partly debt funded project, which albeit is at a later stage of construction. The ratings also factor in working capital intensive nature of pharmaceutical business particularly due to high inventory holding requirements, stiff competition from existing players in the Nepalese market and exposure to regulatory risk and volatile interest rates.

The ratings, however, derive strengths from OMPL's experienced promoters and management team and steady demand outlook of pharmaceuticals products in Nepal over the medium term.

Going forward, the ability of the company to complete the project within the envisaged cost and stabilization of the operations while achieving the envisaged scale of business thereafter will be key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Weaknesses

Implementation risk associated with the partly debt funded greenfield project

The company is setting up a manufacturing facility at an estimated cost of Rs. 745 Mn, which is being financed with debt of Rs. 444 Mn and equity of Rs. 301 Mn (debt to equity ratio of 60:40). The debt component for the project has already been tied up. The project is currently at final stages of implementation. As per progress report dated January 11, 2023, the company has incurred capital expenditure of around Rs. 702 Mn (financial progress of around 94% of the estimated cost) which was funded in the debt equity mix of 60% and 40% respectively. The commercial operations are expected to

¹Complete definitions of the ratings assigned are available at www.careratingsnepal.com and in other CRNL publications.

commence from March 2023. Although at final stages of construction, the company still remains exposed to the residual risks associated with the ongoing project implementation and swift stabilization as envisaged thereafter.

OMPL has already received manufacturing license for 40 different drugs and has applied for additional license to manufacture 9 drugs from Department of Drug Administration (DDA). It is critical for the company to receive the necessary approvals to achieve the envisaged scale of operations.

Working capital intensive nature of business

Manufacturing of pharmaceuticals business is working capital intensive in nature with the company sourcing raw materials from different foreign countries and selling products in the local market. Furthermore, pharmaceuticals manufacturers, generally, hold inventory for about 2-3 months due high lead time from suppliers, minimum order quantity fulfilment and transportation constraints there by increasing inventory holding period. Furthermore, being a highly competitive business, the manufacturer has to offer reasonable credit period to its dealers / distributors which leads to high collection period. Entailing all leads to high to reliance on bank loans to meet the working capital needs.

Competition from existing players and exposure to regulatory risk

Pharmaceuticals industry is competitive with presence of few domestic players and importers of pharmaceuticals products from large pharmaceutical manufacturers in foreign countries. Further, with low product differentiation and controlled pricing for some of the essential drugs, pricing ability remains a key hurdle in this industry.

Pharmaceuticals sector being a matter of public interest is highly regulated industry. DDA under Ministry of Health and Population is the major government institution responsible for regulating pharmaceuticals sector in Nepal. Policies like fixing of maximum retail price on selected products could have impact on profitability of pharma sector. Hence, sector is prone to regulatory risk and changes in other policies of Government of Nepal.

Exposure to volatile interest rate

Nepalese banking sector has a floating interest rate regime, where a certain premium is added to the quarterly base rate and interest rate is changed accordingly on quarterly basis. The base rates of the banks and financial institutions (BFIs) in Nepal remain quite volatile as they are impacted by available liquidity in the system which leads to change in interest rates. The volatility in interest rate is more evident currently on account of the ongoing liquidity stress in the economy, with substantial upward pressure on interest rates in the last few quarters. A contractionary monetary policy for FY23 coupled with increasing inflation has only added to the upward pressure on interest rates, resulting in increased base rates of BFIs in the first half of FY23. Any further significant rate hikes could put increased interest burden on the company, squeezing its profitability and impacting its liquidity position. Therefore, funding taken by the company from BFIs is subject to volatile interest rate.

Key Rating Strengths

Experienced promoters in related field

OMPL is managed under the overall guidance of the company's board of directors (BOD) who possess wide experience in diversified sectors. Mr. Arjun Kumar Shrestha, Chairman, has experience of over two decades in various industries including operation of oxygen plants and trading of medical equipment. Similarly, other directors have considerable experience in different industries. BOD is further supported by an experienced team across various functions/ departments.

Steady demand outlook for pharmaceuticals products

Consumption of pharmaceutical products has been on a growing trend in Nepal supported by increasing access of the general public supported by growing income levels and increasing awareness, particularly in the rural geography. As per the report of Department of Industry on Pharmaceutical and medicine, pharmaceutical industry grew by compounded annual growth rate of ~3% to 430 Mn USD in the country in FY21 from 386 Mn USD in FY18. Almost half of the pharmaceutical products in Nepal is still being imported, thus providing ample opportunities for growth for domestic manufacturing companies. With increasing access of health facilities along with increase in new health facilities across the country, demand for pharmaceutical products is expected sustain over the medium-term. Furthermore, demand of pharmaceuticals products generally remains unaffected by macroeconomics parameters unlike other industries, hence domestic players like OMPL stand to benefit from the increasing demand scenario, if they are competitive in price and quality vis-à-vis imported products.

About the Company

OMPL is a public limited company, incorporated on June 12, 2016, promoted by group of institutional and individual promoters of Nepal for manufacturing pharmaceuticals products at a plant located in Chitwan, Nepal.

Annexure 1: Details of the Facilities Rated

Name of the Bank Facilities	Type of the Facility	Amount (Rs. In Million)	Ratings
Long Term Bank Facilities	Term Loan	444.00	CARE-NP BB- [Double B Minus]
Short Term Bank Facilities	Fund Based Limits	82.00	CARE-NP A4 [A Four]
Short Term Bank Facilities	Non-Fund Based Limits	30.00	CARE-NP A4 [A Four]
Total		556.00	

Contact Us

Analyst Contact

Mr. Girish Bhatta
+977-01-4012630
girish.bhatta@careratingsnepal.com

Mr. Santosh Pudasaini
+977-01-4012628
pudasaini.santosh@careratingsnepal.com

Relationship Contact

Mr. Achin Nirwani
+977-9818832909
achin.nirwani@careratingsnepal.com

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