

Aanjaneya Lifecare Limited

CRISIL IPO Grade 1 / 5 (Poor)

March 28, 2011

Grading summary

CRISIL Equities has assigned a CRISIL IPO grade of '1/5' (pronounced "one on five") to the proposed IPO of Aanjaneya Lifecare Limited (Aanjaneya). This grade indicates that the fundamentals of the IPO are **poor** relative to the other listed equity securities in India. However, this grade is not an opinion on whether the issue price is appropriate in relation to the issue fundamentals. The offer price for the issue may be higher or lower than the level justified by its fundamentals. The grade is not a recommendation to buy, sell or hold the graded instrument, its future market price or suitability for a particular investor. To arrive at the overall grade, amongst various other parameters, CRISIL has considered the company's business prospects, its financial performance, management capabilities and corporate governance practices.

The assigned grade reflects the company's limited corporate governance practices. In Aug 2009, Aanjaneya was acquired by Finaventure Capital (FCL), a shell company listed on the Bombay Stock Exchange (BSE), through a share swap, whereby Aanjaneya's promoters parted 33.75% holding to FCL's shareholders. For the transaction, Aanjaneya was valued at Rs 280 mn and the implied valuation of FCL was Rs 143 mn. CRISIL Equities believes that the amount paid does not commensurate with the business prospects of FCL. In addition, the independent directors' engagement and board practices need to be significantly strengthened.

Aanjaneya's focus areas – formulations for cough and cold, anti-malarial, anti-cancer and herbal medicine segments – are expected to see steady demand growth. The company, an anti-malarial API manufacturer, entered into codeine-based formulation by acquiring Prophyla Biologicals Private Ltd in March 2010. Prophyla was into formulation job-work for large Indian pharmaceutical companies and had one of the largest codeine quotas in the country. Aanjaneya's key strength is its ability to source quinine and codeine, which are the two key raw materials for anti-malarial and cough and cold formulations. As formulations for anti-malaria and cough syrup are in constant demand, Aanjaneya's unique position aids in revenue stability. All the clients are dependent on Aanjaneya for the APIs and formulations. The company has strong relationships with clients like Cipla, Wockhardt, Tablets India Zydus Cadilla and others.

Aanjaneya has entered the branded segment with its own codeine-based formulations and lozenges for cough and cold. Post IPO, the company plans to focus on anti-cancer and own brands. The codeine business is highly regulated by the Bureau of Narcotics (BoN). BoN controls the quota of codeine and constantly monitors for misuse of codeine. As codeine can only be purchased from BoN, any production shortfall or non-import by BoN can limit the company's growth potential.

Incorporated in 2006, Aanjaneya has scaled up revenues to Rs 1,617 mn in FY10 with EBITDA and PAT margins of 18.1% and 9.3%, respectively, and RoE of 48.5%. In March 2010, Aanjaneya bought the assets of Prophyla Biologicals Pvt Ltd for Rs 280 mn. These assets were transferred with effect from 1 April 2010 and, thus, Aanjaneya's financials for H1FY11 cannot be compared to its historical financials. For H1FY11, the company posted a top line of Rs 1,401 mn which included Rs 801 mn of API-related revenue and Rs 599 mn of formulation revenue. EBITDA and PAT margins were 19.3% and 10.1% respectively. RoE was 13% on the back of capital infusion.

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About the company

Originally incorporated as Aanjaneya Biotech Private Ltd on January 3, 2006, it changed its name to Aanjaneya Biotech Private Ltd on March 8, 2007. Converted into a public limited company on April 12, 2010, it subsequently changed its name to Aanjaneya Biotech Ltd. It was rechristened Aanjaneya Lifecare Ltd (Aanjaneya) on June 19, 2010. The current promoters are Finaventure Capital Ltd (name changed to Aasda Life Care Ltd, yet to be approved by the BSE) and Dr. Kannan K. Vishwanath. Finaventure Capital Ltd is a BSE-listed company with a market capitalisation of Rs 950 mn (as of December 21, 2010).

Dr. Kannan K. Vishwanath and his father Mr Kashi Vishwanathan were the erstwhile promoters of Benzo Chemicals, which focused on anti-malarial and anti-cancer segments.

Though the company was incorporated in 2006, it commenced commercial production of APIs (active pharmaceuticals ingredients) of quinine salts (a second generation anti malarial), in 2007. In 2010, the company ventured into manufacturing of finished dosage forms by acquiring the assets of Prophylla Biologicals Pvt. Ltd through an asset purchase agreement dated March 30, 2010 and deed of assignment for trademarks dated April 1, 2010.

A. Issue details

No. of shares being offered	5 mn; fresh issue
Targeted issue size (Rs Mn)	Not available at the time of grading
Face value per share	Rs 10
Proposed price per share	Not available at the time of grading
Lead managers	Aanand Rathi Advisors Ltd, IDBI Capital Market Services Ltd
Legal advisors to the Issue	M/s Crawford Bayley & Co.
Registrar to the issue	Link Intime India Private Ltd

Detailed Grading Rationale

B. Corporate Governance

- *Acquisition by Finaventure Capital*

- Aanjaneya was formed in 2006 by Mr Kannan K Vishwanathan (60%) and Finaventure Advisors Ltd (40%). Finaventure Advisors exited the company in 2008.
- Finaventure Advisors acquired Indusvista Ventures Ltd, a shell company listed on the BSE at Rs25 per share. The name of the company was changed to Finaventure Capital Limited (FCL) in May 2009 and then to Aasda Lifecare Ltd in March 2010 (name change yet to be approved by the BSE).
- In March 2010, Aanjaneya became a 100% subsidiary of FCL at a conversion price Rs 40 per FCL share. Through this transaction, Aanjaneya's shareholders gave away 33.75% stake to FCL's shareholders although FCL did not have a business of its own. Also, FCL was originally acquired by Finaventure Advisors Ltd for Rs 25 per share, and within one year, with no value addition to the business, Aanjaneya's shareholders agreed for a share swap at Rs 40 per FCL share.
- For the transaction, Aanjaneya was valued at Rs 280 mn and implied valuation of FCL was Rs 143 mn.
- As per the management, the above transaction was done so that Aanjaneya could raise funds through FCL for growth opportunities. Any such transaction in the future may have an implication on the minority shareholders of Aanjaneya.
- Aanjaneya and FCL entered into a non-compete agreement in March 2011, as both the companies have similar business objects.

- *Corporate governance practices needs further strengthening*

- From our conversation with the independent directors, we believe that their engagement and awareness levels and board practices can be significantly improved. Also, the company has had frequent capital structure and name changes.

C. Business Prospects

- *Indian pharmaceutical industry is poised for ~16 % CAGR*

- CRISIL Research expects the Indian pharmaceutical industry to grow at 16% over FY10-15, with the domestic formulation market growing 13% and exports up by 17%. The domestic market is expected to improve on increased demand due to chronic and lifestyle diseases and rising disposable incomes. Aanjaneya's focus areas – formulations for cough and cold, anti-malarial, anti-cancer and herbal medicine segments – are expected to see steady growth in demand. Exports are expected to benefit with products going off patent in the developed markets, which is an opportunity for Indian players to enter, given the low cost base.
- **Anti-malarial market:** The anti-malarial market is expected to grow on the back of an increasing population, lack of infrastructure and repeated attacks on people with a low immunity system. Some of the largest markets for anti-malaria drugs are China, India, Indonesia, Latin America and sub-Saharan Africa. In India, the anti-malarial drugs market has grown at a CAGR of 22% over FY06-10. The anti-malaria API market is dominated by artemotil, artesunate, chloroquine and quinine, which do not come under pricing regulations. Hence, Aanjaneya stands to benefit from the demand growth in the anti-malaria segment.
- **Anti-cancer market:** Oncology is one of the fastest growing therapeutic segments in both global and domestic markets. The Indian oncology market, with a CAGR of 30% in the past three years, is valued at ~Rs 800 crore. As per industry sources, this segment is expected to grow at 21% over the next three years. Globally, the oncology market was valued at US\$ 45 bn in FY09 and is expected to grow at a CAGR of 11.6% over the next five years. Aanjaneya, with the IPO proceeds, plans to set up an anti-cancer unit to cater to the generic oncology market. Aanjaneya's promoters have experience in anti-cancer APIs through their association with Benzo Chemicals.
- **Herbal medicine market:** The domestic herbal medicine market is worth ~Rs 70 bn and is expected to grow at a CAGR of 20% over the next two years. India's total herbal export is worth Rs 36 bn and is expected to grow at a CAGR 25% over the next two years. Over the years, herbal medication is being increasingly used in combination with allopathic treatments. This rising trend is on the back of the availability of quality ingredients, price competitiveness, and virtually no side effects. Exports of herbal products from India are on the rise as they meet the required WHO standards. In the herbal space, Aanjaneya is focussing on cough and cold, liver protection, throat congestion and osteoporosis therapy areas.

- *Aanjaneya Lifecare Limited has carved out a few niche segments for itself*

The pharmaceutical market - though diverse - sees severe competition among both organised and unorganised players. Hence, Aanjaneya has decided to focus on a few niche therapeutic segments - anti-malarial, erectile dysfunction, pain management, herbals, codeine-based syrups, hormone replacement, anti-obesity and is also setting up a dedicated anti-cancer drugs facility. The company is selling these products in the domestic market and has applied for registrations in semi-regulated markets; currently, it exports APIs to semi-regulated markets. It has received registrations for its Prosil lozenges range in Haiti,

South Africa, Hong Kong and the Dominique Republic. Registrations of its various products are in progress in Africa, the Gulf Cooperation Council (GCC) and East Asia, which will augment revenues going forward.

Aanjaneya also under takes P2P (price to price¹) contracts for formulations with the large local pharma companies like Cipla, Wockhardt, Glenmark. In the own branded generic segment, the company has products like Anjtil, Rankorex, Doktor Qure, Prosils, LivChek, Herbal Drops and Eshhil, catering to cough, cold and liver segments.

The company has an Indian patent for gel-based formulation for hormone delivery and is yet to launch the drug. Also, it is one of the five lozenge manufacturers in India.

- *Aanjaneya is in a transition phase, thanks to the Prophyla acquisition*

- Aanjaneya started as an API manufacturer, primarily engaged in quinine salts – a key second generation API - for curing malaria. It entered the formulation business by acquiring Prophyla Biological Pvt Ltd in March 2010. Prophyla's list of clients included the top 100 domestic pharmaceutical companies for whom it used to undertake job-work. Post acquisition, Aanjaneya restructured Prophyla's operations from a job-work based player to a P2P manufacturer of formulation. The company has also launched its own cough syrup – Rankorex, after acquiring Prophyla.

- *Access to raw materials*

- The company's inherent strength lies in its access to two key raw materials – codeine and quinine.

- *Codeine*

- Cough syrups are predominantly manufactured using dextromethorphan or codeine. Top codeine-based cough syrups in India include Corex (Pfizer), Phensedyl (Nicholas Piramal) and Ricodex (Wockhardt).
- Codeine is a narcotics-based formulation, manufactured from poppy seeds (opium), which is highly regulated globally through the Vienna Convention. In India, it is controlled by the Bureau of Narcotics (BoN), which licenses codeine quotas and allocates supplies to licence-holders in India.
- BoN has not given fresh licence to any player in the past 5-10 years.
- Allocations are made based on the output of poppy seeds and in case of short supply, only BoN can import codeine.
- In India, Pfizer has the highest licensed quota with 8,000 kgs per annum, followed by Piramal (acquired by Abbot) 7,200 kgs and Aanjaneya with 6,000 kgs. There are 10-12 other predominant but unlisted players and information about their quota is not available. As per management, India has given out about 50,000 - 80,000 kgs of codeine licence.
- Due to the regulatory entry barrier, Aanjaneya has higher supplier power compared to its clients. Hence, it has been able to turn around Prophyla from a job-work player to a P2P manufacturer.

¹ Price to price is where the supplier (Aanjaneya) undertakes entire responsibility for the product, right from sourcing raw material to the finished product. In job-work, all materials are provided by the client.

- *Quinine*

- In use for more than 400 years, quinine salt is a second-generation anti-malarial product derived from cinchona bark, which is abundantly available in Africa (world's largest grower). But the difficult socio-economic nature of the African nations makes sourcing the bark difficult too. Globally, there are only nine companies manufacturing quinine salts while most companies prefer to buy APIs and formulate the product. But Aanjaneya's management's expertise in sourcing the bark (gained from Benzo Chemicals) is a significant advantage for the company. Aanjaneya is the second largest quinine manufacturer in India. Aanjaneya is the only other company apart from IPCA to receive WHO pre-qualification for APIs and formulations of anti-malarial drugs.

- *Raw materials sourcing capability provides stability to revenues*

- As formulations for anti-malaria and cough syrup are in constant demand with a 12-15% y-o-y growth, Aanjaneya's unique position aids in revenue stability. All the clients are dependent on Aanjaneya for the APIs and formulations. The company has strong relationships with clients like Cipla, Wockhardt, Tablets India, Zydus Cadilla and others.

- *Entering the branded formulations market*

- Post IPO, the company plans to significantly scale up its marginal presence (in two and three tier cities in north India) in the OTC herbal segment and branded generics formulations business. The key products include Aanjatone (similar to Liv-52), Rankorex (similar to Corex), Prosils (lozenges) amongst others. The company is currently building relationship with the distributors through promotional route.
- For future growth, the company has entered into an agreement (in June 2010) with Rx Pharma India, a marketing company, for availing their services for sales management, logistics and marketing its products through their distributor network. The company has earmarked Rs 150 mn towards marketing its products on a pan-India basis.

- *Anti-cancer – focus on institutional sales:*

- Aanjaneya is planning to set up an anti-cancer facility through the IPO proceeds to cater to the oncology market. Anti-cancer drugs are primarily sold to institutions like Tata Memorial, Cancer Institute and other institutions specialising in cancer through tenders, and not through the normal distribution network. The promoters of Aanjaneya have expertise in anti-cancer segment by virtue of managing Benzo Chem.

D. Financial Performance

Aanjaneya started in 2006 as an API manufacturer of quinine salts and later diversified to artemisinin during FY10 – both anti-malarial APIs. Commercial production commenced in 2007. The company's revenues increased to Rs 1,617 mn in FY10 from Rs 219 mn in FY08. It posted EBIDTA and PAT margins of 18.1% and 9.3%, respectively, in FY10 with RoE of 48.5%. In March 2010, Aanjaneya bought the assets of Prophyla Biologicals Pvt Ltd (which undertook formulation job-work for pharma companies) for Rs 280 mn. With this acquisition, the company got an entry into the pharmaceutical formulation space. These assets were transferred with effect from April 1, 2010 and thus, Aanjaneya's financials for H1FY11 cannot be compared to its historical financials.

In H1FY11, the company posted a top line of Rs 1,401 mn which included Rs 801 mn from API-related revenue and Rs 599 mn from formulation revenue. EBIDTA and PAT margins were at 19.3% and 10.1%, respectively. RoE was at 13% on the back of capital infusion.

Financial performance snapshot

Rs mn	FY10	FY09	FY08
	Actual 12 months	Actual 12 months	Actual 12 months
Net Sales	1617	901	219
PAT	151	51	23
Net block	469	132	107
Capital WIP	42	-	-
Equity capital	58	50	20
Net worth	497	123	43
Debt	597	376	124
Cash and bank balances	8	7	0.8
Net debt-to-equity	1.2	3.0	2.9

Source: DRHP

E. Proposed use of Issue Proceeds

Sr. No.	Proposed use of issue proceeds	Total estimated costs (Rs mn)	Amount estimated to be utilized from net proceeds (Rs mn)
1	Setting up of Anti Cancer API Facility at Mahad, Maharashtra	265	265
2	Setting up of cGMP Block for APIs at Mahad, Maharashtra	137	137
3	Setting up of Intermediate API Block at Mahad, Maharashtra	87	87
4	Expansion of existing Research & Development centre at Mahad and Pune, Maharashtra	191	191
5	Setting up of a Quality Control and Quality Assurance Block at Mahad, Maharashtra	142	142
6	Setting up of Product Development Laboratory at Mahad, Maharashtra	16	16
7	Setting up of Stores Building at Mahad, Maharashtra	71	71
8	Meeting the Expenses for Branding and Registration of our Products in the International Markets	100	100
9	General Corporate Purposes	--	--
10	Issue Expenses	--	--
	Total	--	--

Source: DRHP

F. Management Capabilities

- *Experienced top management*

- The company is run by Dr. Kannan Kashi Vishwanath, who is the promoter, vice-chairman and managing director of the company and has around 10 years of experience in the pharmaceutical industry, and his father, Mr Kashi Vishwanathan, who was the promoter of Benzo Chemicals. Prabhat K. Goyal, whole-time director in charge of the plant in Mahad, has over 30 years of experience in the pharma space. Management's expertise is mainly in anti-malaria (quinine and artemisinin APIs) and anti-cancer drugs owing to their earlier association with Benzo Chemicals.

- *Second line is adequate for current operations*

- Based on our interactions, we believe that the second line is adequate to run the current operations, but will have to be scaled up to handle the demands of future expansions. Most of the second line has been recruited recently, with few business heads coming through the Prophyla acquisition. Also, the management is heavily dependent on the company's distribution partner, Rx Pharma, for distribution of its formulations as it lacks in-house distribution expertise.

Annexure I Business Profile

- *Business overview*

- Aanjaneya Lifecare Ltd is a vertically integrated pharmaceutical company manufacturing and marketing anti-malarial APIs (active pharmaceutical ingredients) and finished dosage forms (FDFs) catering to various therapeutic segments.

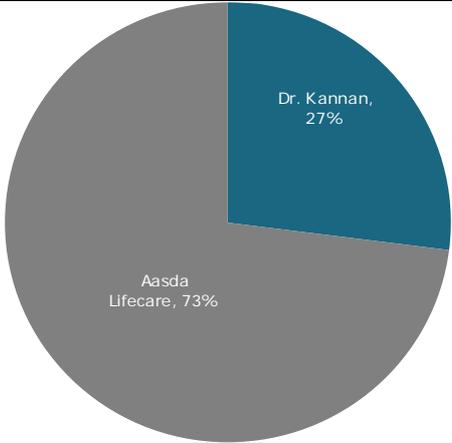
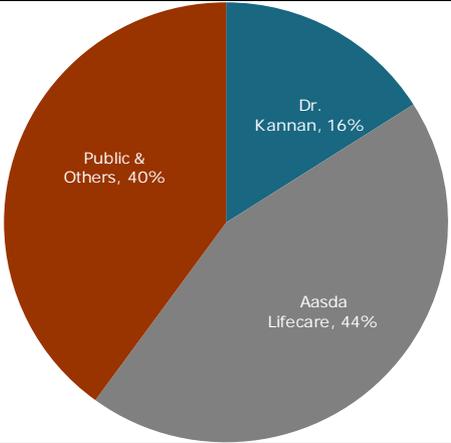
- *Mahad: API manufacturing*

- The company began its manufacturing in 2007 with an installed capacity of 200 MT per annum for processing quinine, a pharmaceutical API derived from natural extracts, for supplying to other pharmaceutical companies for their FDFs. Located in Additional MIDC, Mahad (Maharashtra), the GMP-certified API facility has also been awarded ISO 4001:200 (Environment Management System), ISO 9001:2008 & ISO 22000:2005 certifications by BSI Systems. The company's installed capacity for processing quinine has grown from 200 MT per annum in 2007 to 450 MT per annum in 2010. It has already commenced production of third generation anti-malarial APIs i.e. artemisinin and its derivatives.

- *Pune: Formulation manufacturing*

- Through an asset purchase agreement dated March 30, 2010, the company acquired assets of Prophyla Biologicals, which is spread over 6,430 sq. mts in Mulshi, Pune. Prophyla was engaged in the business of formulations/ FDFs. With this acquisition, Aanjaneya is able to manufacture lozenges, syrups and ointment/gels/creams. Prophyla had codeine quota of six tonne per annum and it is one of the largest quota holder in this space. This acquisition has not only given the company an access to codeine-based formulation but also helped it to be an integrated player with its presence in the entire value chain in the pharmaceutical industry.

- *Shareholding pattern*

Pre-issue shareholding pattern	Post-issue shareholding pattern
	
Source: DRHP	Source: DRHP

Annexure II: Profile of the Directors

Board of Directors

Name	Designation	Age	Qualification	Experience (years)	Previous Employment	Directorships / partnership in other entities
Mr. Kashi Vishwanathan	Executive & Non-Independent Chairman	65	Science Graduate, Mumbai University	45+		Aasda Life Care Ltd
Dr. Kannan K Vishwanath	Vice-Chairman & Managing Director	34	Bachelor's degree in Chemical Engineering, MBA from Hamilton College, USA	10+		Aasda Life Care Ltd
Mr. Prabhat K Goyal	Executive & Non-Independent Director	55	Post-Graduate in Organic Chemistry From Vikram University	33+	Elder Pharmaceuticals Limited, IPCA Laboratories Ltd, Ranbaxy Laboratories Ltd & Jayant Vitamins Ltd	
Mr. Shashikant B Shinde	Executive & Non-Independent Director	58	Bachelor's in Science and Master's in Management from Marathwada University,	32+	Aristo Pharmaceuticals Private Ltd, Geno Pharmaceuticals Ltd, Rathi Brothers Ltd & Lyka Labs Private Ltd	Prophyla Biologicals Ltd
Dr. Ullopee S. Badade	Non-executive & Independent Director	40	MBBS from Amravati University & Master's in Business Administration(Hospital Administration) from University of Pune	16+	Manipal Cure & Care Private Limited, Lokmanya Hospital, Supertech Neurosurgical Centre and Nirmay Hospital	Aasda Life Care Limited
Mr. Giridhar G. Pulleti	Non-executive & Independent Director	42	Masters degree in Science with specialisation in Organic Chemistry	20+		Sanova Pharma Chem Private Limited Nutra Specialities Private Limited
Mr. Balkrishna R Parab	Non-executive & Independent Director	39	Bachelor's degree in Commerce from University of Mumbai	10+		
Mr. Kalidas S Patel	Non-executive & Independent Director	57	Bachelor's degree in Commerce from University of Mumbai & a qualified graduate Cost & Works Accountant, Practicing CA	29+		

Please note that all the companies wherein above Board members have directorships have not been listed in the above table. Hence, the list is just indicative.

Source: Company, DRHP

Disclaimer

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