

Rating Action: Moody's upgrades DOC Generici's rating to B1; outlook change to stable

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Paris, March 03, 2022 -- Moody's Investors Service ("Moody's") has today upgraded the corporate family rating (CFR) to B1 from B2 and the probability of default rating (PDR) to B1-PD from B2-PD of Diocle S.p.A.'s ("DOC Generici" or "the company"). At the same time, Moody's has upgraded to B1 from B2 the company's EUR470 million guaranteed senior secured floating-rate notes due in 2026, of which EUR323 million remain outstanding, following the last partial redemption completed by the company on 21 February. The outlook has been changed to stable from positive.

RATINGS RATIONALE

The upgrade of DOC Generici's rating to B1 reflects Moody's expectations that key credit metrics will be well positioned in the rating category under the next 12 to 18 months. Moody's expects the company's Moody's-adjusted gross leverage to close at 3.6x at end-2021 (3.1x pro forma the latest debt redemption). Additionally, the agency expects the company will continue to generate Moody's-adjusted FCF of around EUR55 million over the same period, which represents a ratio of 17% to 18% of debt.

So far, the company's financial policy has been conservative with DOC Generici privileging debt redemptions with available excess cash. Under its ESG framework, Moody's considers the history and stability of the company's leverage and dividend policy as part of its assessment of financial strategy and risk management.

The company has redeemed around EUR150 million of its guaranteed senior secured notes over the past three years, significantly reducing its debt burden. The agency believes the risk of large debt-funded M&A remains low because the company does not intend to expand activities outside of Italy and it already has a leading position within its own core market of retail generics. Moody's forecasts do not incorporate any shareholder distributions over the next 12 to 18 months as the agency understands the company will continue prioritizing liquidity and deleveraging.

Over the next 12 to 18 months, Moody's expects DOC Generici will generate organic revenue growth in the mid-single digits in percentage terms thanks to its strong footprint in the Italian generics market, and in particular the Class A segment where the company has the second largest market share; the continued penetration of generics in the Italian market thanks to a supportive regulatory environment that is expected to endure in the foreseeable future; and the new generics launched over recent years.

RATING OUTLOOK

The stable outlook reflects Moody's expectation that DOC Generici will continue to generate a strong operating performance, including positive organic sales growth, and have a good liquidity profile. The outlook also reflects the agency's expectations of a continued prudent financial policy over the next 12 to 18 months that will support a leverage around 3.0x (Moody's adjusted gross leverage) on a sustained basis.

LIQUIDITY PROFILE

DOC Generici has good liquidity, with a cash balance of EUR40 million as of 31 September 2021 and access to a EUR50 million undrawn super senior revolving credit facility (SSRCF). The company has no immediate debt maturities. The SSRCF has a financial maintenance covenant, which will only be tested when the facility is drawn by 40% or more. Moody's expects the company to have significant headroom against this threshold, if tested.

Because of the company's asset-light model, limited amounts are required for capital spending, while working capital swings are generally low. Nevertheless, DOC Generici's exposure to wholesalers (around 60% of revenue) could, in more extreme scenarios, entail larger working capital swings if the wholesalers draw on their inventory levels rather than placing new orders.

STRUCTURAL CONSIDERATIONS

The PDR of B1-PD reflects Moody's assumption of a 50% recovery rate for covenant-lite debt structures. The B1 rating of the guaranteed senior secured floating-rate notes due in June 2026, of which EUR323 million are still outstanding, is in line with the B1 CFR, reflecting their positioning in the capital structure, with only the EUR50 million SSRCF ranking ahead of them.

The top entity of the restricted group is Diocle S.p.A., the issuer of the guaranteed senior secured floating-rate notes. All debt instruments share the same collateral package on first and second priority. In particular, the debt instruments benefit from guarantees by the parent company and significant subsidiaries, which must represent at least 80% of consolidated EBITDA.

FACTORS THAT COULD LEAD TO AN UPGRADE OR DOWNGRADE OF THE RATINGS

For upward pressure to materialize, DOC Generici would have to increase its scale and improve its diversification through, for example, a reduced reliance on the Italian market. Quantitatively, upward pressure could develop if DOC Generici's leverage ratio (defined as Moody's adjusted gross debt/EBITDA) trends well below 3.0x on a sustained basis supported by a prudent financial policy and if its Moody's-adjusted free cash flow to debt increases sustainably above 20%, while maintaining a good operating performance.

Conversely, downward pressure could develop if the company's Moody's-adjusted gross leverage ratio increases above 4.0x on a sustainable basis; or if its Moody's-adjusted free cash flow to debt decreases sustainably below 10%, or there are unfavorable developments in the Italian regulatory framework, significantly affecting the company's ability to sustain earnings and cash flow growth; or the company embarks on significant debt-funded acquisitions or significant shareholder distributions.

PRINCIPAL METHODOLOGY

The principal methodology used in these ratings was Pharmaceuticals published in November 2021 and available at https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_1285013. Alternatively, please see the Rating Methodologies page on www.moodys.com for a copy of this methodology.

COMPANY PROFILE

DOC Generici is a leading Italian independent generics company operating in the retail channel. The company operates only in the Italian market and has operations across a wide variety of therapeutic categories. Intermediate Capital Group (ICG) and Merieux Equity Partners acquired DOC Generici on 1 July 2019 and hold a majority shareholding of 95%. DOC Generici generated gross sales of EUR250 million in the 12 months that ended September 2021, with a reported EBITDA of EUR104 million during the same period.

REGULATORY DISCLOSURES

For further specification of Moody's key rating assumptions and sensitivity analysis, see the sections Methodology Assumptions and Sensitivity to Assumptions in the disclosure form. Moody's Rating Symbols and Definitions can be found at: https://www.moodys.com/researchdocumentcontentpage.aspx?docid=PBC_79004.

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At least one ESG consideration was material to the credit rating action(s) announced and described above.

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