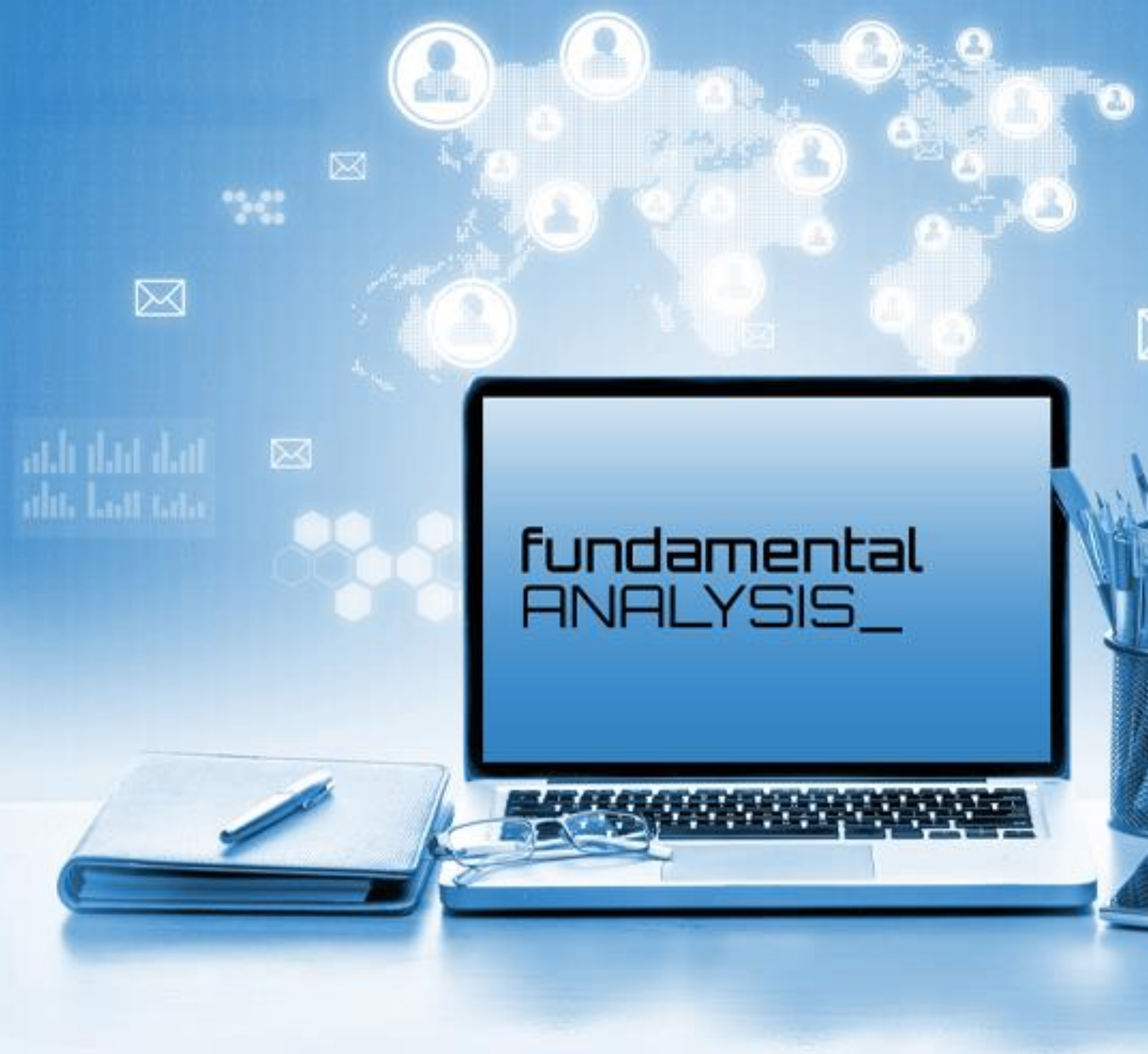
Stock Update

Fortis Healthcare Ltd.

Sep 21, 2022



RETAILRESEARCH

Fortis Healthcare Ltd.

Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Healthcare Facilities	Rs 314.9	Buy in the band of Rs 312-318 & add more on dips to Rs 277-282 band	Rs 345	Rs 372	2-3 quarters

HDFC Scrip Code	FORHEAEQNR
BSE Code	532843
NSE Code	FORTIS
Bloomberg	FORH IN
CMP Sep 20, 2022	314.9
Equity Capital (Rs cr)	754.9
Face Value (Rs)	10
Equity Share O/S (cr)	75.5
Market Cap (Rs cr)	23,777
Book Value (Rs)	81.8
Avg. 52 Wk Volumes	1631807
52 Week High	325.0
52 Week Low	219.7

Share holding Pattern % (Jun 2022)	
Promoters	31.2
Institutions	47.3
Non Institutions	21.5
Total	100.0

HDFCsec Retail research stock rating meter

for details about the ratings, refer at the end of the report

* Refer at the end for explanation on Risk Ratings

Fundamental Research Analyst
Hemanshu Parmar
hemanshu.parmar@hdfcsec.com

Our Take:

Fortis Healthcare Limited (FHL) – an IHH Healthcare Berhad Company – is a leading integrated healthcare services provider in India. It is one of the largest healthcare organizations in the country with 26 healthcare facilities and 4300 operational beds (including O&M model) as of March 31, 2022. Fortis offers a full spectrum of integrated healthcare services ranging from clinics to quaternary care facilities and a wide range of ancillary services to patients in Cardiac Care, Orthopedics, Neurosciences, Oncology, Renal Care, Metabolic diseases care and mother and childcare. SRL Ltd, a subsidiary of Fortis Healthcare, is among the leading diagnostic laboratory chains with an established strength of over 426+ laboratories, 20+ radiology / imaging centers; and a footprint spanning 3050+ customer touch points. With its corporate governance issues behind, Fortis Healthcare draws strength from its partnership with global major and parent company, IHH, to build upon its culture of world-class patient care and superlative clinical excellence.

We had issued initiating coverage & stock update report on the company. Although the diagnostic space would see moderation in profitability in the near term, we draw comfort from the strong growth in hospital business due to improved speciality mix, aggressive brownfield expansion, traction in international patients and cost rationalisation initiatives. Also any positive update in the legal proceedings would further strengthen its operational performance and financial position; and make a case for rerating of the stock.

Valuation & Recommendation:

Fortis Hospital's business is well positioned and has demonstrated healthy operational efficiency with industry leading ARPOB and decent capacity utilisation. The company undertook a comprehensive strategic review and prioritized key areas to drive revenues and operational performance. It has strategic plans to strengthen its clinical specialties, medical infrastructure, manpower training and onboarding of new talent. It aims cluster focused brownfield expansion along with turning around the lagging facilities, which are low-occupancy and earn low-EBITDA. The company plans to add 1500 beds over next 4 years mainly in their existing clusters. Deepening presence in existing locations would help leverage higher economies of scale in terms of both cost & revenue drivers and benefiting from cross-leveraging clinical and non-clinical resources.

SRL Ltd has been aggressively expanding its network in focused geographies. It has maintained strong position by adding advanced solutions in diagnostic testing, laboratory efficiency and clinical decision support with strong focus on Genomics. Expanding test menu with a focus on specialized tests would provide an edge to SRL in the recent challenging competitive times. Indian diagnostic sector is expected to grow in low to mid-teens over the next few years supported by industry tailwinds; however given the recent price competition, we will see moderation in margin for SRL. Any positive update on the final verdict on open offer of IHH would accelerate their plans for calibrated growth and evaluating future path for SRL. We expect revenue/EBITDA to grow at CAGR of 11.2%/11.3% over FY22-24E. **We think the base case fair value of the stock is Rs 345 (20.5x FY24E EV/EBITDA; 44.5x FY24E EPS) and the bull case fair value is Rs 372 (22x FY24E EV/EBITDA; 48x FY24E EPS) over the next two-three quarters. Investors can buy the stock in the band of Rs 312-318 and add more on dips to Rs 277-282 band (16.75x FY24E EV/EBITDA; 36x FY24E EPS).**

Financial Summary

Particulars (Rs cr)	Q1FY23	Q1FY22	YoY-%	Q4FY22	QoQ-%	FY20	FY21	FY22	FY23E	FY24E
Total Operating Income	1487.9	1410.3	5.5	1378.1	8.0	4,632.3	4,030.1	5,717.6	6,277.5	7,076.0
EBITDA	251.1	275.3	-8.8	221.2	13.5	609.5	404.4	1,069.0	1,130.0	1,323.2
Depreciation	74.3	72.9	1.9	77.3	-3.9	291.7	290.6	300.8	318.2	334.1
Other Income	20.7	7.8	164.0	6.0	245.6	52.6	46.6	27.3	50.2	56.6
Interest Cost	31.2	38.4	-18.8	30.0	3.9	205.1	165.9	146.9	124.7	107.2
Tax	42.0	55.8	-24.7	39.4	6.6	147.9	99.5	197.8	185.8	236.5
PAT	134.3	430.6	-68.8	87.0	54.3	17.5	-104.9	450.8	551.5	702.0
Adjusted PAT	122.3	263.6	-53.6	68.0	79.9	57.9	-109.8	555.1	464.4	586.2
Diluted EPS (Rs)	1.6	3.5	-53.6	0.9	79.9	0.8	-1.5	7.4	6.2	7.8
RoE-%						0.9	-1.7	9.0	7.2	8.5
P/E (x)						409.0	NA	42.9	51.2	40.6
EV/EBITDA (x)						41.1	61.5	23.0	21.6	17.9

(Source: Company, HDFC sec)

Q1FY23 Result Review:

Fortis Healthcare Ltd (FHL) reported revenue of Rs 1487.8cr (up 5.5%/ 8% YoY/QoQ) mainly led by healthy growth in hospital business. Better occupancy levels and higher ARPOB due to strong recovery in elective procedures resulted in sharp growth in hospital business revenue, while diagnostics business witnessed muted performance due to lower covid volumes. The company reported EBITDA of Rs 251.1cr (-8.8%/+13.5% YoY/QoQ). EBITDA margin improved by 82 bps QoQ to 16.9%, due to recovery in occupancy in hospital segment (19.5% in Q1FY22). It clocked PBT of Rs 166.3cr (-3.2%/+38.7% YoY/QoQ). FHL posted adjusted PAT of Rs 122.2cr (up 80% QoQ) as against Rs 266.5cr in Q1FY22. During Q1FY22, the company reported an exceptional gain of Rs 306.1cr related to remeasurement of the previously held equity interest of SRL in the SRL-DDRC JV at its fair value post-acquisition of the balance 50% stake in the said JV in April 2021.

Hospital business posted healthy topline growth of 18.5%/14.6% YoY/QoQ to Rs 1192.4cr, led by a strong recovery in elective procedures. Q1FY22 and Q4FY22 witnessed an impact on hospital revenues due to higher covid cases and a decline in elective procedures. Hospital business reported EBITDA of Rs 193.3cr, up 34.8%/36.7% YoY/QoQ. It saw improvement in margins from 14.6% in Q1FY22 to 16.2% in Q1FY23 (vs 13.6% in Q4FY22). Better occupancy levels, case mix and higher ARPOB lifted its operational performance. Overall occupancy for the quarter stood at 65% as compared to 66% in Q1FY22 and 59% in Q4FY22. Average revenue per occupied bed (ARPOB) for the quarter stood at Rs 1.96cr (+21% YoY), while it was Rs 1.88cr in Q4FY22. Revenues from key specialties such as Oncology, Gastroenterology, Renal Sciences and Orthopedics have seen strong growth versus the corresponding and the trailing quarters. Contribution from surgical revenue stood at 61% compared to 41% in Q1FY22 and 57% in Q4FY22. International Patient revenues grew 126% YoY to Rs 89cr in Q1FY23, contributing 7.5% to overall hospital business revenues vs 6.6% in Q4FY22. Covid revenues' contribution to overall hospital revenues stood at 28% in Q1FY22 and 6% in Q4FY22 versus a negligible 0.6% in Q1FY23. The company continued with its brownfield expansion strategy and commissioned around 55 additional beds in Fortis Mulund, Mumbai and FMRI, Gurugram. During the quarter, the Company onboarded eminent clinicians in the medical specialties of urology, transplants, rheumatology and nephrology.

Diagnostic Business (SRL ltd) reported revenue to the tune of Rs 332.6cr (down 24.6% YoY). Sharp decline in covid testing pricing and volumes resulted in such steep fall in revenue. It clocked EBITDA of Rs 57.8cr as against Rs 80cr in the previous quarter. EBITDA margin saw significant decline to 17.4% vs 21.5% in Q4FY22 (29.9% in Q1FY22). Non-covid revenues (excluding covid and covid allied tests) grew 28.2%/7.7% YoY/QoQ to Rs 312.3cr. Covid revenue contribution was at 6% in Q1FY23 compared to 45% in Q1FY22 (22% in Q4FY22). SRL conducted 9.96 mn test (-6%/ -7.4% YoY/QoQ). Average realization per test was at Rs 334 (-19.3%/-3% YoY/QoQ). On the positive side, revenue contribution from the specialized test portfolio (non-covid) increased to 37% from 34% in Q1FY22. Home collections and preventive care packages witnessed good traction during the quarter. SRL added 243 new collection centers to its network during the quarter, taking the total number of collection centers to 2,745. The customer touch points i.e. CTP / Lab ratio strengthened to 17.1 in Q1FY23 versus 11.4 in Q1 FY22, signifying the increase in network optimization. SRL's B2C: B2B revenue mix stood at 55:45 in the quarter compared to 57:43 in Q1FY22.

Concall Key Takeaways:

Hospital Business:

- The company intends to expand operational bed capacity to ~1500 beds in the next 4 years; it added 54 beds in Q1FY23. Most of the expansion would be brownfield.
- Expansion would be cluster focused; with NCR, Mumbai & Bangalore on high priority. This would be followed by Calcutta & Punjab.

- Existing facilities like FMRI, Mohali, Noida and Shalimar Bagh are slated to add in excess of 200 beds each, mainly funded by internal accruals.
- Few of its key underperforming facilities such as Sirohi and Jaipur have witnessed higher revenues and better profitability versus both the trailing and corresponding quarter.
- Arcot Hospital (Chennai) likely to breakeven by Q1FY24.
- The management expects better occupancy levels and trend may continue in Q2FY23
- Better case mix (higher surgical cases) would support sustenance of ARPOB

Diagnostic Business

- The management highlighted that competitive pressure in the diagnostic business remain and the operating environment would be challenging in short term.
- Focus would be on channel expansion, increasing collection center network, specialized test portfolio which would be further strengthened.
- The company has taken a number of initiatives to improve customer experience including the launch of new WhatsApp chatbot and live phlebotomist tracking feature. In this quarter, it added 50+ new tests and technologies to strengthen testing portfolio.
- Restructuring of SRL could be explored by the end of this year, given the volatility in diagnostic space.

Other Matters:

- Balance sheet remains healthy with net debt to EBITDA of 0.54x. Net debt stands at Rs. 585cr as on June 30, 2022. A stronger balance sheet would allow to evaluate inorganic growth opportunities in line with its cluster strategy approach.
- The final verdict for the pending legal case could come soon.

Key Triggers:

Hospital Business well positioned:

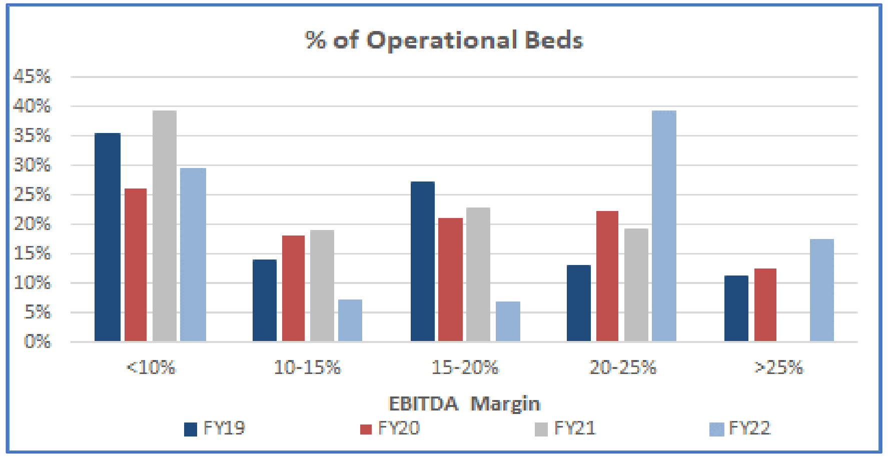
Fortis' Hospital business is well positioned and has demonstrated healthy operational efficiency with industry leading ARPOB and decent capacity utilisation. The company undertook a comprehensive strategic review and prioritized key areas to drive revenues and operational performance. The business witnessed sharp uptick in performance in FY22 with revenue growth of 38.6% YoY to Rs 4329.8cr on account of strong recovery in in-patient volumes and elective surgeries. Healthy occupancy levels 63% (vs 55%/68% in FY21/FY20) coupled with higher ARPOB at Rs 1.8cr (up 13.2% compared to FY20) supported robust EBITDA margin of 15.5% (vs 8.4%/12.2% in FY21/FY20). Revenue contribution from company's focus specialties comprising oncology, gastroenterology, Neuro Sciences, renal sciences, orthopaedics and cardiac sciences grew 43% YoY and contributed 55% to overall hospital revenues. It has strategic plans to strengthen its clinical specialties, medical infrastructure, manpower training and onboarding of new talents.

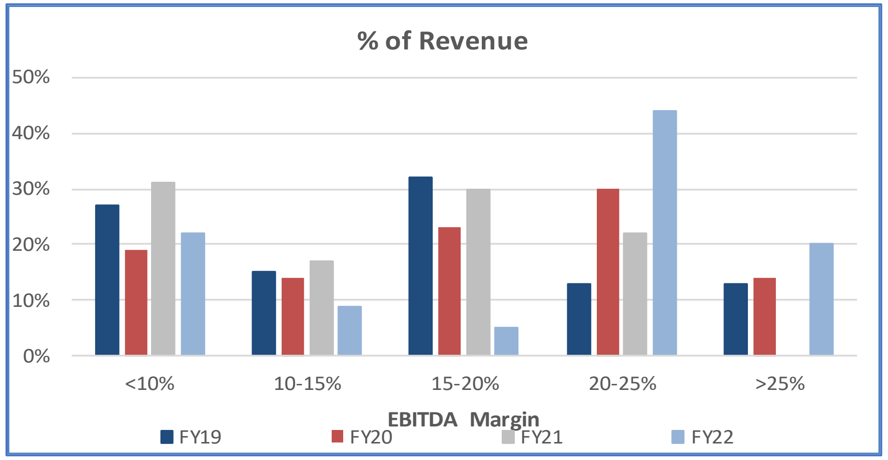
Focus on improving case mix by improving medical infrastructure and attracting clinical talents

It is strengthening its clinical programme especially its focus specialties - Cardiac Sciences, Oncology, Neuro Sciences, Gastroenterology and Orthopedics – by onboarding several eminent clinicians across some of its large units. It has heavily invested in high-end medical infrastructure and equipment including Cath Labs, Neuro-Surgical Microscopes, Neuro-Navigation Systems and Endoscopy Systems which would support higher in-patient volumes in higher margin case profiles. It has already started work on getting India's first MR Linac at its flagship facility in Gurugram which has equipped with advanced technology used in treating tumours with utmost precision. State-of-the-art bone marrow transplant unit was inaugurated at Fortis Hospital, Mulund in FY22. It also commissioned 12-bedded oncology daycare center providing chemotherapy services in a prominent Delhi location to further expand its reach and complementing existing oncology service offerings. The company would replicate the model depending on its success.

Cluster focused Brownfield expansion and improving performance of lagging units

Fortis aims cluster focused brownfield expansion along with turning around the lagging facilities, which are low-occupancy and low-EBITDA. Although there is decent recovery in few underperforming hospitals – Jaipur, Vashi, Malar, Sacred Heart – in terms of revenue; their occupancy and ARPOB has not witnessed recovery post covid. The management could evaluate strategic options if few hospitals don't see healthy turnaround.



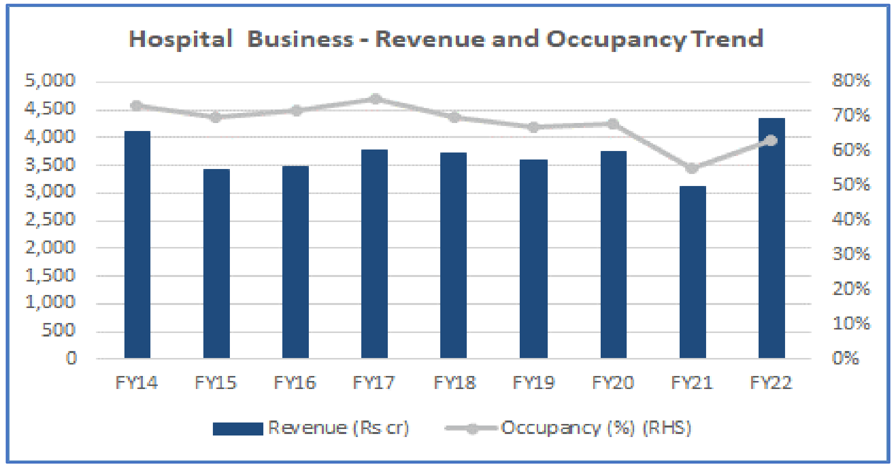


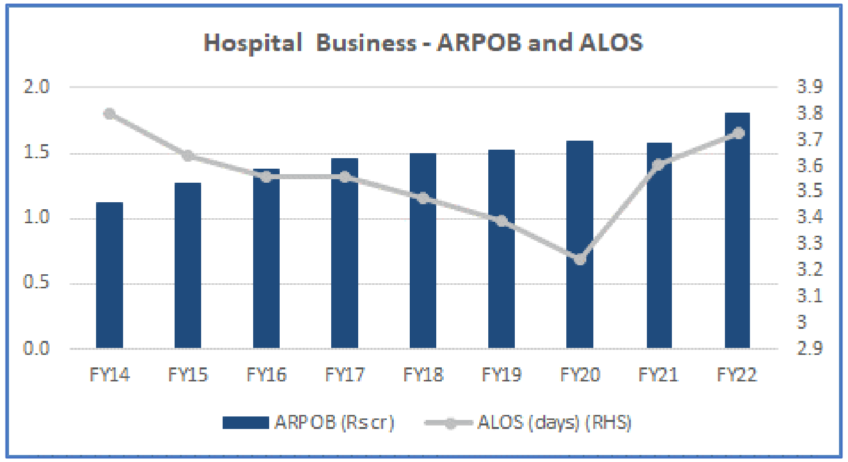
(Source: Company, HDFC sec)

Company's expansion plans in FY22 was impacted due to covid waves which resulted in delay in project execution. In FY22, it operationalized 127 new beds across units including Vadapalani, Shalimar Bagh, Jaipur, Ludhiana and Amritsar. The company plans to add 1500 beds over next 4 years mainly in their existing clusters. Delhi/ NCR, Mumbai, Bangalore remains its top priority for brownfield expansion; followed by Kolkata and Punjab. It has identified around 600 beds within the existing facilities that are ready to be operationalized depending on the market condition and occupancy levels. Existing facilities like FMRI, Mohali, Noida and Shalimar Bagh are slated to add in excess of 200 beds each; which would be mainly funded through internal accruals. Deepening presence in existing locations would help leverage higher economies of scale in terms of both cost & revenue drivers and benefiting from cross-leveraging clinical and non-clinical resources. Stronger balance sheet provides space to evaluate inorganic opportunities in line with its cluster strategy approach.

<u>Procurement excellence initiative and improving payor mix/ Other initiatives to fuel further growth</u>

The company is focused on implementing a comprehensive cost optimisation programme that aimed to rationalise drugs and consumables cost, bring in capex procurement efficiencies and optimize indirect spends. Efforts are undertaken to drive revenues via more focused sales and marketing efforts towards improving payer mix segments (cash payer & TPA) and increasing focus on medical tourism (from 4.8% in FY22 to low double digit in FY23). ARPOB is influenced essential larger mix of procedural and complex cases which would yield higher margins. Hiring of quality clinical talent to hospital network and improving medical infrastructure would support the company's ability to improve specialty mix going forward.





(Source: Company, HDFC sec)

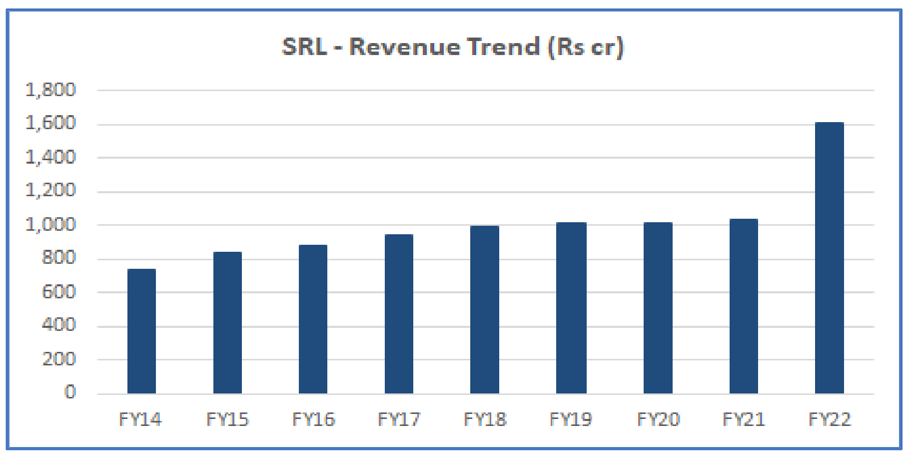
Quarterly Trend

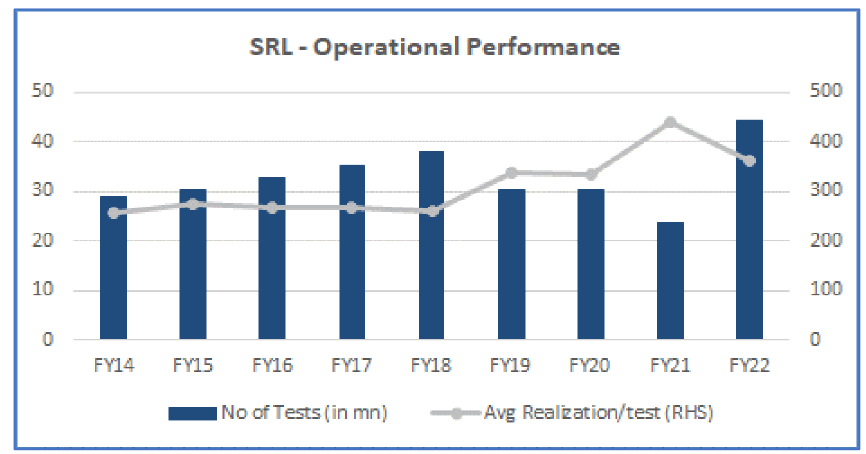
Hospital Business	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23
Revenue (Rs cr)	967	913	972	954	913	488	746	907	982	1006	1098	1118	1041	1192
EBITDA Margin (%)	5%	12%	13%	14%	11%	-17%	11%	15%	14%	15%	17%	17%	14%	17%
EBIT Margin (%)	1.6%	3.5%	6.6%	7.0%	3.9%	-29.8%	-0.7%	7.1%	7.9%	8.9%	11.7%	11.8%	8.2%	11.6%
Occupancy-%	68%	66%	72%	68%	65%	37%	57%	64%	64%	66%	64%	65%	59%	65%
ARPOB (Rs in cr per annum)	1.53	1.57	1.55	1.62	1.62	1.51	1.49	1.58	1.70	1.62	1.87	1.86	1.88	1.96

(Source: Company, HDFC sec)

Diagnostic Business – expect healthy growth but near term pressures in store:

The diagnostics business witnessed a healthy performance aided in part by the DDRC – SRL transaction and due to higher covid volumes. In FY22, SRL reported strong performance on all grounds in terms of overall revenue, profits by maintaining healthy margins. It reported robust topline of Rs 1278.9cr (up 55.1% YoY) supported by strong recovery in non-covid volumes (up 76.1% YoY). Covid tests also witnessed sharp jump in FY22, although average realization saw dramatic rationalization during the year. It conducted 5.6 million RT-PCR tests in FY 2021-22 which generated Rs 326 crores of revenue. Diagnostic business posted overall EBITDA margin of 26.5% in FY22 as against 19.3%/19.4% in FY21/FY20. Overall it conducted 44.2 mn tests in FY22 (up 87.8% YoY; 45.4% compared to FY20) and served over 21.4 mn patients compared to 11.1 mn in FY21. Apart from the organic growth initiatives, SRL also completed the 100% acquisition of DDRC SRL Diagnostics Private Limited in April 2021. In FY2022, SRL has significantly strengthened its channel mix with the B2C versus B2B component at 55 versus 45 (B2C:B2B in FY21 at 48:52).





(Source: Company, HDFC sec)

Retail Network Expansion to support volume growth

SRL Ltd has been aggressively expanding its network in focus geographies; adding 800+ customer touch points and embedded 1700+ direct clients in 570+ towns in FY22. It has established its presence across 600+ cities, 34 states and union territories It has ramped up its testing capacity and opened more centres and drive through sites to collect samples across the country. Its network currently consists of 426+ labs, 3050+ customer touch points (CTP) and 5,600+ direct clients. Aggressive expansion of customer touch points translates well in its B2C contribution of the business. The acquisition of balance 50% stake in the DDRC SRL, JV, Kerala during April 2021, also strengthened the business. Home collection service capabilities are available in 150+ cities across India. The business continued to have a well-diversified geographical mix with no over dependence on any particular region allowing it to capitalize on a pan-India network optimally. Revenue contributions from North/East/West/South/International was at 32%/12%/25%/28%/3% in FY22. Asset light franchisee led aggressive expansion in last couple of years will yield results as these centers start maturing delivering better numbers. CTP/lab has improved to 17.1 in Q1FY23 signifying the increase in network optimization thereby improving utilization and gaining higher operating leverage.

Expansion of test menu (specialized tests) and Digital Initiatives:

SRL has maintained strong position by adding advanced solutions in diagnostic testing, laboratory efficiency and clinical decision support with strong focus on Genomics. It added close to 100 tests with a special focus on genomics in the field of cancer, reproductive disorders, rare diseases and inherited disorders. Its newly introduced tests - Preimplantation Genetic Screening (PGS) on Next Generation Sequencing (NGS) platform, identifies genetic or chromosomal defects in embryos prior to using them in in-vitro fertilisation (IVF); Myeloid Panel on Next Generation Sequencing (NGS) provide predictive, prognostic, and diagnostic information for patients with a variety of myeloid malignancies; and TERT Mutation Analysis on Pyrosequencing which provides risk stratification and prognostic significance in multiple tumour types. In Q1FY23, it added 50+ new tests and technologies to strengthen its testing portfolio. It is in the process of introducing new tests under the category of the nutrigenomics, personal genomics, proteomics and pharmacogenomics that would prepare the company for next generation diagnostics testing. It has also procured Advanced Machines to improve TAT on some of these specialized tests. Expanding test menu with a focus on specialized tests (~41% of non-covid revenues in FY22) would provide an edge to SRL in the recent challenging competitive times.

Moreover, the company has taken a number of initiatives to improve its customer experience including the launch of new WhatsApp chatbot and live phlebotomist tracking feature. It launched the all new SRL website with features like easy sharing of lab location map link, booking multiple tests at one go; and also upgraded their app. In FY22, it started offering SMART report for select tests and packages. The Smart + health report, explains health reports in a language that is easily understood and intercepted by the consumers, is one of the many initiatives towards a customer centric approach.

International Business - although nascent could be a kicker

SRL's international division was operational in 2003. The international operations of the Company comprise state-of-the-art labs in Dubai, Kathmandu, and Biratnagar (Nepal). It started to send out business and expanded the SRL network in Ethiopia, Kenya, Uganda, Maldives, Oman, Mauritius and Uzbekistan. In FY22, it won transplant immunology tender from Ministry of Health Oman through its local partner in Oman. SRL's international network consists of more than 120 collection centres and 800 direct clients spread across the SAARC region, Sub-Saharan Africa, Southeast Asia, Gulf and the Middle East. Although currently its share is sub-5% to overall revenue; increased focus on international expansion would improve its operational performance. SRL could leverage its promoter IHH Healthcare Berhad's (IHH) wide international network, which would drive international test volumes. However, discussion on this would surface post supreme court judgement on open offer.

Plans for restructuring SRL could find its way by this fiscal-end

Minority shareholders of SRL hold a put option which was extended till Feb 5, 2024 and the liability towards this option is Rs 2074cr as at March'22 end. In the recent earning call, the management remarked that different options (demerger or acquisition of remaining stake or listing) are being explored. There could be delay in their plans given the heightened price competition and volatility in diagnostic space currently. Announcement in this regard could perhaps come by the end of this fiscal. Demerger of SRL business and possible of listing of the business would command better valuation and provide exit to the minority shareholders of SRL. Also more clarity on the competitive intensity in the diagnostic space and its impact on financials of well-established diagnostic chains in a years' time would help in deciding the optimal path for this business.

How is SRL placed in the current heightened competitive diagnostic industry?

Indian diagnostics industry is currently facing high competition intensity from online players. Its asset light (franchisee-led expansion) structure, high margin, high return ratios coupled with industry's sustainable growth over medium to long term and low entry barriers led to new entrants backed by large conglomerates. Tata acquired e-pharmacy 1MG and launched its own diagnostics wing, Reliance through Netmeds scaled up diagnostic business, Thyrocare (established player) was acquired by PharmEasy (e-pharmacy chain), Medplus (pharmacy retailer) have become aggressive in diagnostics. Large hospital chains have also announced their investment plans to expand beyond their hospitals cluster regions. Attractive predatory pricing is adopted by these players to garner higher volume share; which would impact volumes and profitability of established diagnostics chains.

New entrants have adopted discounted price strategy mainly for routine and wellness test segments. Moreover, their focus would be in metro cities atleast initially. Although routine tests form bulk of volumes and profits of existing players; this space is overcrowded in this fragmented industry. Focused digital marketing will happen more on the routine tests which are customer-driven; it would minimal impact in case of doctor-driven test (~50-55% in diagnostic industry). Large established players offer 4000+ test menu which includes semi-specialised and specialized tests which is likely to be continued by them due to high equipment cost, high value low volume and high maintenance cost of quality standards. Wide network of customer touchpoints of diagnostic chains especially in Tier 2 & 3 cities would witness less disruption from new age tech players; atleast in the near to medium term. Definitely, industry wide lower realization per patient and margins is underway as reflected in recent quarters results. But these are early days; meaningful impact on the industry is yet materialized.

Focus on channel expansion in the past couple of years, ramping up its test offering especially on specializes segment and healthy share of B2B has helped to strengthen SRL's position. It also has been working with digital aggregators in the preventive space. Indian diagnostic sector is expected to grow in low to mid-teens over the next few years supported by industry tailwinds; we will see moderation in margin for SRL as well.

Quarterly Trend

Diagnostic	Q4FY19	Q1FY20	Q2FY20	Q3FY20	Q4FY20	Q1FY21	Q2FY21	Q3FY21	Q4FY21	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23
Revenue (Rs cr)	251.1	258.5	276.6	249.4	231.9	140.4	282.4	306.2	305.7	441.4	402.7	388.5	372.3	332.6
EBITDA Margin (%)	19%	21%	25%	16%	15%	-8%	25%	24%	22%	31%	26%	27%	23%	19%
EBIT Margin (%)	15.9%	15.1%	17.9%	8.2%	4.5%	-20.8%	17.9%	17.3%	15.7%	25.6%	20.1%	20.4%	15.6%	11.7%
No of Test (in mn)	7.4	7.8	8.36	7.45	6.77	3.35	5.92	6.7	7.58	10.6	11.57	11.25	10.76	9.96
Average Realisation per test (Rs)	336	329	327	334	342	418	473	459	400	414	348	342	344	334

(Source: Company, HDFC sec)

Final verdict on open offer could come very soon:
The hearing in the open offer matter has been concluded and the company is awaiting judgement. As per a recent TV interview, the management pointed that the judgement on this matter would be completed by Sep'22 end. Once the legal matter on this case is behind, the new promoter group (IIH) would take measures for accelerated growth given their international experience and world class standards. It would also provide more flexibility in raising fresh capital for some significant acquisition and calibrated growth.

Concerns:

High competition: The healthcare sector is competitive, as increasing healthcare providers (newer and existing hospitals, low-cost nursing homes, etc) try to establish themselves among patients. Increasing subsidies from the government and improvement in services from the government hospitals may cause attrition in patients and disrupt business sustainability. With the advancing technology and newer medical interventions, several hospitals are evolving with their services as well. The diagnostic industry is witnessing heightened competition from new age tech players adopting aggressive pricing and new bundled offerings, which has resulted into lower margins and lower realization per patient for large established chains. This has also delayed the value unlocking of its investment in SRL.

Operational Risk: As significant capex incurred for new hospitals, or laboratory, delay in ramp-up will impact EBITDA and affect cashflow generation. Any delay in commissioning or expansion (reaching breakeven) of new facilities may impact overall growth, thus impacting overall financials. Hospital business, being a highly capital intensive business, can deliver high EBITDA margin/RoCE only through high utilization level. Lower occupancy level in hospitals could impact its profitability.

Ongoing Litigations and Investigations by SEBI & SFIO: Fortis Group, due to its erstwhile promoters is facing multiple investigations and litigations; any adverse ruling may impact the company's operations and its credit profile.

Recruitment and retaining of medical talent: This is one of the key hurdles faced by the industry that limits growth. Given the scarcity of quality resources, recruiting and retaining medical talent is a key challenge, especially with the competition also hunting for similar resources.

Price Regulation: Government regulating prices for critical medical treatment (including that of medical devices) which private hospital charges from patient remains a risk to revenues and margins.

About the company:

Fortis Healthcare Limited (FHL) – an IHH Healthcare Berhad Company – is a leading integrated healthcare services provider in India. It is one of the largest healthcare organizations in the country with 26 healthcare facilities and 4300 operational beds (including O&M model) as of March 31, 2022. Fortis offers a full spectrum of integrated healthcare services ranging from clinics to quaternary care facilities and a wide range of ancillary services to patients in Cardiac Care, Orthopedics, Neurosciences, Oncology, Renal Care, Metabolic diseases care and mother and childcare. Healthcare verticals of the company primarily comprise day care specialty, diagnostics and tertiary and quaternary care. SRL Ltd, a subsidiary of Fortis Healthcare, is among the leading diagnostic laboratory chains with an established strength of over 426+ laboratories, 20+ radiology / imaging centers; and a footprint spanning 3050+ customer touch points.

The erstwhile promoters, Malvinder Singh and Shivinder Singh, who were involved in diversion of funds and misrepresentation of financials statements, were forced to reduce their stake to less than 1% (Feb 2018) after the Supreme Court allowed lenders to invoke the pledge against shares of FHL held as security. Thereafter, the search for a new promoter began and bids were invited from investors. IHH was the winning bidder and became the new promoter, investing around Rs 4,000cr in the company against fresh issuance for around 31.1% stake. IHH also plans to bring open offer for acquiring up to 26% stake in FHL. Pursuant to order dated December 14, 2018 passed by the Court, the open offer has been put on hold. In order to reinforce complete dissociation with erstwhile promoters, the board has proposed to rename the Fortis brand as 'Parkway', which is a strong international brand belonging to IHH. Fortis Healthcare draws strength from its partnership with global major and parent company, IHH, to build upon its culture of world-class patient care and superlative clinical excellence.

Peer Comparison:

	Mcap (Rs cr)	Revenue			EBITDA Margin			APAT		
		FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Fortis Healthcare	**23,777**	**5,718**	**6,278**	**7,076**	**18.7**	**18.0**	**18.7**	**555**	**464**	**586**
Apollo Hospitals	65,556	14,663	16,747	19,598	14.9	13.9	15.2	1,056	1,033	1,443
Narayana Hrudayalaya	14,417	3701	4194	4672	17.7	19.3	19.9	342	422	488

	RoE (%)			P/E			EV/EBITDA		
	FY22	FY23E	FY24E	FY22	FY23E	FY24E	FY22	FY23E	FY24E
Fortis Healthcare	**9.0**	**7.2**	**8.5**	**42.9**	**51.2**	**40.6**	**23.0**	**21.6**	**17.9**
Apollo Hospitals	20.6	16.8	19.9	62.1	66.0	45.5	31.0	29.5	23.0
Narayana Hrudayalaya	26.2	24.9	23.1	42.2	33.8	29.2	23.7	18.3	16.0

(Source: Bloomberg estimates, Company, HDFC sec)

Financials

Income Statement

(Rs Cr)	FY20	FY21	FY22	FY23E	FY24E
Net Revenues	**4632.3**	**4030.1**	**5717.6**	**6277.5**	**7076.0**
Growth (%)	**3.6**	**-13.0**	**41.9**	**9.8**	**12.7**
Operating Expenses	4022.8	3625.7	4648.7	5147.6	5752.8
EBITDA	**609.5**	**404.4**	**1069.0**	**1130.0**	**1323.2**
Growth (%)	**170.6**	**-33.6**	**164.3**	**5.7**	**17.1**
EBITDA Margin (%)	**13.2**	**10.0**	**18.7**	**18.0**	**18.7**
Depreciation	291.7	290.6	300.8	318.2	334.1
EBIT	**317.8**	**113.8**	**768.1**	**811.8**	**989.1**
Other Income	52.6	46.6	27.3	50.2	56.6
Interest expenses	205.1	165.9	146.9	124.7	107.2
PBT	**165.4**	**-5.5**	**648.6**	**737.3**	**938.6**
Tax	147.9	99.5	197.8	185.8	236.5
RPAT	**17.5**	**-104.9**	**450.8**	**551.5**	**702.0**
APAT	**57.9**	**-109.8**	**555.1**	**464.4**	**586.2**
Growth (%)	**LP**	**-289.4**	**LP**	**-16.3**	**26.2**
EPS	0.8	-1.5	7.4	6.2	7.8

LP= Loss to Profit

Balance Sheet

As at March (Rs Cr)	FY20	FY21	FY22	FY23E	FY24E
SOURCE OF FUNDS					
Share Capital	755.0	755.0	755.0	755.0	755.0
Reserves	5906.1	5364.9	5423.3	5887.7	6473.9
Shareholders' Funds	**6661.1**	**6119.8**	**6178.2**	**6642.7**	**7228.9**
Minority's Interest	544.5	598.0	830.0	961.0	1126.4
Long Term Debt	1166.6	1199.3	1032.7	902.7	822.7
Net Deferred Taxes	-81.3	-81.5	12.1	12.1	12.1
Long Term Provisions & Others	85.1	1715.8	2193.1	2023.3	2280.7
Total Source of Funds	**8376.0**	**9551.4**	**10246.2**	**10541.9**	**11470.8**
APPLICATION OF FUNDS					
Net Block & Goodwill	8817.3	8800.9	9415.8	9497.6	9538.5
CWIP	188.8	163.1	193.4	193.4	193.4
Other Non-Current Assets	1008.4	783.7	773.2	932.2	1051.8
Total Non Current Assets	**10014.5**	**9747.7**	**10382.4**	**10623.2**	**10783.7**
Current Investments	0.0	0.0	0.0	0.0	0.0
Inventories	78.2	76.8	122.9	120.4	155.1
Trade Receivables	458.8	457.8	512.2	636.4	736.7
Cash & Equivalents	266.0	416.6	412.7	485.6	1185.9
Other Current Assets	137.6	85.7	85.5	104.9	157.0
Total Current Assets	**940.5**	**1036.8**	**1133.3**	**1347.3**	**2234.7**
Short-Term Borrowings	390.4	331.2	222.2	227.2	232.2
Trade Payables	597.6	548.2	660.9	739.5	814.2
Other Current Liab & Provisions	1591.0	353.6	386.3	461.9	501.2
Total Current Liabilities	**2578.9**	**1233.0**	**1269.4**	**1428.6**	**1547.7**
Net Current Assets	-1638.5	-196.2	-136.2	-81.4	687.1
Total Application of Funds	**8376.0**	**9551.4**	**10246.2**	**10541.9**	**11470.8**

Cash Flow Statement

(Rs Cr)	FY20	FY21	FY22	FY23E	FY24E
Reported PBT	239.4	43.3	987.8	737.3	938.6
Non-operating & EO items	-48.5	-7.0	-326.9	-310.2	169.5
Interest Expenses	174.8	123.9	125.3	124.7	107.2
Depreciation	291.7	290.6	300.8	318.2	334.1
Working Capital Change	-146.4	-12.7	-10.2	38.5	-55.3
Tax Paid	-339.5	47.5	-211.4	-185.8	-236.5
OPERATING CASH FLOW (a)	**171.5**	**485.5**	**865.4**	**722.6**	**1,257.5**
Capex	-136.6	-211.5	-115.3	-400.0	-375.0
Free Cash Flow	34.9	274.0	750.1	322.6	882.5
Investments	79.7	0.0	0.0	0.0	0.0
Non-operating income	120.4	81.0	-385.3	0.0	0.0
INVESTING CASH FLOW (b)	**63.5**	**-130.6**	**-500.6**	**-400.0**	**-375.0**
Debt Issuance / (Repaid)	-656.8	25.7	-370.3	-125.0	-75.0
Interest Expenses	-204.9	-168.6	-147.0	-124.7	-107.2
FCFE	-826.7	131.0	232.8	72.9	700.3
Share Capital Issuance	0.0	0.0	0.0	0.0	0.0
Dividend	0.0	0.0	0.0	0.0	0.0
Others	0.0	0.0	0.0	0.0	0.0
FINANCING CASH FLOW (c)	**-861.6**	**-142.9**	**-517.3**	**-249.7**	**-182.2**
NET CASH FLOW (a+b+c)	**-626.6**	**212.0**	**-152.5**	**72.9**	**700.3**

Key Ratios

	FY20	FY21	FY22	FY23E	FY24E
PROFITABILITY RATIOS (%)					
EBITDA Margin	13.2	10.0	18.7	18.0	18.7
EBIT Margin	8.0	4.0	13.9	13.7	14.8
APAT Margin	1.3	-2.7	9.7	7.4	8.3
RoE	0.9	-1.7	9.0	7.2	8.5
RoCE	4.4	2.0	10.5	11.3	13.0
Solvency Ratio (x)					
Debt/EBITDA	2.6	3.8	1.2	1.0	0.8
D/E	0.2	0.3	0.2	0.2	0.1
PER SHARE DATA (Rs)					
EPS	0.8	-1.5	7.4	6.2	7.8
CEPS	4.6	2.4	11.3	10.4	12.2
Dividend	0.0	0.0	0.0	0.0	0.0
BVPS	88.2	81.1	81.8	88.0	95.8
Turnover Ratios (days)					
Debtor days	39	42	31	33	35
Inventory days	5	7	6	7	7
Creditors days	53	52	39	41	40
VALUATION					
P/E (x)	409.0	NA	42.9	51.2	40.6
P/BV (x)	3.6	3.9	3.8	3.6	3.3
EV/EBITDA (x)	41.1	61.5	23.0	21.6	17.9
EV/Revenues (x)	5.4	6.2	4.3	3.9	3.3
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0
Dividend Payout (%)	0.0	0.0	0.0	0.0	0.0

(Source: Company, HDFC sec)

One Year Price Chart:

(Source: Company, HDFC sec)

HEMANSHU VIJAY PARMAR

Digitally signed by HEMANSHU VIJAY PARMAR
Date: 2022.09.21 08:48:32 +05'30'

HDFC Sec Retail Research Rating description

Green Rating stocks

This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. This stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the portfolio.

Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicality of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

HDFC securities Limited, I Think Techno Campus, Building - B, "Alpha", Office Floor 8, Near Kanjurmarg Station, Opp. Crompton Greaves, Kanjurmarg (East), Mumbai 400 042 Phone: (022) 3075 3400 Fax: (022) 2496 5066

Compliance Officer: Murli V Karkera Email: complianceofficer@hdfcsec.com Phone: (022) 3045 3600

HDFC Securities Limited, SEBI Reg. No.: NSE, BSE, MSEI, MCX: INZ000186937; AMFI Reg. No. ARN: 13549; PFRDA Reg. No. POP: 11092018; IRDA Corporate Agent License No.: CA0062; SEBI Research Analyst Reg. No.: INH000002475; SEBI Investment Adviser Reg. No.: INA000011538; CIN - U67120MH2000PLC152193