Stock Update

Narayana Hrudayalaya Ltd.

Feb 05, 2024

RETAILRESEARCH

HDFC securities
Click. Invest. Grow.
20 YEARS

Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Healthcare Facilities	Rs 1342	Buy in the band of Rs 1342-1358 & add more on dips to Rs 1211	Rs 1467	Rs 1557	2-3 quarters

HDFC Scrip Code	NARHRUEQNR
BSE Code	539551
NSE Code	NH
Bloomberg	NARH IN
CMP Feb 2, 2024	1342
Equity Capital (Rs cr)	204.4
Face Value (Rs)	10
Equity Share O/S (cr)	20.4
Market Cap (Rs cr)	27,428
Book Value (Rs)	122
Avg. 52 Wk Volumes	397518
52 Week High	1399
52 Week Low	708

Share holding Pattern % (Dec, 2023)	
Promoters	63.9
Institutions	21.7
Non Institutions	14.4
Total	100.0

* Refer at the end for explanation on Risk Ratings

Fundamental Research Analyst
Kushal Rughani
kushal.rughani@hdfcsec.com

Our Take:

Narayana Hrudayalaya Ltd (NHL) has a network of 45 healthcare facilities in India, including 18 owned/operated hospitals, 1 managed hospital, 4 heart centres and 21 primary care facilities with 6,164 bed capacity. Company has an established presence and strong brand recognition in India especially in two geographies (Bangalore and Karnataka). Strong performance of flagship units is complemented by steady improvement in new hospitals. Improving occupancy and footfalls coupled with increasing ARPOB resulted in narrowing losses in new hospitals. To cement its position in India, the company is prioritizing debottlenecking and brownfield expansion at its existing facilities. There would not be meaningful bed additions in the next 2 years in India. Its key priority is to add brownfield capacities at existing hospital units. Steady revenue from newer hospitals, change in payor mix, increase proportion of higher-end surgeries coupled with high bed turnover (lower ALOS) are key drivers in the medium term. NHL is open to pursue strategic growth through greenfield facilities at core regions as well as inorganic opportunities.

Narayana owns and operates Health City Cayman Islands (HCCI), which is a 110-bed facility located in the Cayman Islands, Caribbean. The new hospital at Camana Bay is likely to improve its reach to patients both – international and local, due to close proximity to the airport and several major residential complexes. This would enable NHL to cater to local residents, who usually travel abroad for high-end medical treatment. The new facility would complement the existing setup by focusing more on day care, short stay but niche categories of oncology care while the existing facility would continue to cater to tertiary and quaternary care. Capex guidance of Rs. 1140 crore in FY24E of which Rs 400 crore incurred in H1FY24. Newly commissioned radiation oncology block at Cayman island saw a meaningful traction. A new multi-specialty hospital at Cayman is on track to be commercialized by Q1FY25.

We had issued a report on Narayana on Sep 15, 2023 at a CMP of Rs 1092 with base case target of Rs 1195 and bull case target of Rs 1265 in the 2-3 quarters (link). The stock had achieved both the targets in just 2 months. We issue stock update note on the stock given strong numbers in the first half and healthy outlook on the sector.

Valuation & Recommendation:

'Narayana Health' brand is strongly associated with its ability to deliver high-quality, affordable healthcare services by leveraging economies of scale, skilled doctors, and an efficient business model. NHL operates at lower ARPOB compared to its peers, and over the years it has implemented and followed unique cost control measures right from construction of hospital buildings to sourcing equipment and consumables. India business ARPOB growth will not come from pricing, but from increased throughput and increased quaternary care in the overall mix. NHL is working on reducing ALOS by working on efficiencies and changing the clinical pathways to improve throughput. NHL has a steady expansion plan and is committed to refurbishing its flagship facilities in Bangalore and Kolkata, which will help to improve the quality of healthcare services offered to patients. It has unveiled its new logo and announced a rebranding exercise across all its healthcare facilities.

NHL has taken significant strides towards diversifying its portfolio by submitting an application to the Insurance Regulatory and Development Authority of India (IRDAI) for its bundled insurance plans. Few weeks back, the company has received license from IRDAI to launch health insurance business in India. This strategic move aims to bridge the gap between healthcare services and insurance, bringing more comprehensive and integrated solutions to patients and healthcare customers. The integration of healthcare services and insurance can contribute to better health outcomes. Patients may have access to a wider range of preventive and diagnostic services, resulting in early detection and treatment of health issues.

Higher maturity mix in hospitals, steady performance of flagship hospitals in India and improving profitability of new hospitals (SRCC, Gurugram, Dharamshila) solidifies its position in India. Prioritizing debottlenecking and brownfield expansion at its existing centres and expansion in Cayman support growth going forward. Commissioning of new hospitals would account for a large part of the growth however could pose a risk on the margin front. We expect revenue/EBITDA/PAT to grow at CAGR of 14%/15.2%/14.3% over FY23-26E. We recommend buy on the stock in the band of Rs 1342-1358 and add more on dips to Rs 1211 for base case fair value of Rs 1467 (20.3x FY26E EV/EBITDA; 33x FY26E EPS) and bull case fair value of Rs 1557 (21.5x FY26E EV/EBITDA; 35x FY26E EPS) over the next two-three quarters.

Financial Summary

Particulars (Rs cr)	Q2FY24	Q2FY23	YoY (%)	Q1FY24	QoQ (%)	FY21	FY22	FY23	FY24E	FY25E	FY26E
Total Operating Income	1305	1142	14.3	1233	5.8	2,583	3,701	4,525	5,164	5,759	6,685
EBITDA	308	244	26.4	271	13.8	183	654	966	1,136	1,256	1,477
PAT	226.7	168.9	34.2	184	23.1	-7	351	607	760	773	910
EPS (Rs)	11.1	8.3	34.2	9.0	23.2	-0.7	16.9	29.9	37.1	37.7	44.3
RoE (%)						-1.3	26.2	33.5	30.6	24.1	22.9
P/E (x)						-	80.2	45.2	36.0	35.6	30.2
EV/EBITDA (x)						153.7	42.8	28.9	24.7	22.3	18.6

(Source: Company, HDFC sec)

Q2FY24 Result Update

- Revenue for the quarter grew 14.3% YoY at Rs 1305 crore. EBITDA margin improved 230bps YoY and 170bps QoQ at 23.6%. Net profit was up 34.2% YoY at Rs 226.7 crore. PBT for the quarter increased 17.8% YoY at Rs 248.4 crore. Other Income declined 41% YoY while increased 22% QoQ at Rs 18.4 crore. Finance cost increased 51.5% YoY at Rs 22.9 crore.
- EPS for the quarter stood at Rs 11.1 and it stood at Rs 20.2 for H1FY24.
- In Q2FY24, India business reported revenue growth of 14.7% YoY and 6.7% QoQ at Rs. 1053 crore. It was mainly due to 7.6% growth in inpatient volume which were at 64,000, while OP footfalls were at 685,000, growth of 11.7%.
- ARPOB for India business witnessed growth of 10.7% YoY to Rs 36712 with occupancy level of 60%.
- Cayman business recorded revenue of 12.7% YoY and 5.7% QoQ to Rs 261 crore. This was mainly due to improvement in ARPOB by 9.5% YoY and incremental revenues from addition of oncology unit.
- NHL witnessed healthy growth in Bangalore and Southern Peripheral clusters and saw strong momentum in high-end Cardiac Sciences, Oncology, Gastro Sciences, Orthopedics, Image Guided Therapies. Steady performance of flagship hospitals and improvement in ARPOB & margin in new hospital improved its overall profitability.

Q2 FY24 Concall Highlights

- Growth drivers: Next phase of growth would come from changing payor profile of patients, increasing proportion of higher-end surgeries and efficiency in systems with high bed turnover/discharges; as there is no new capacity addition for 3.5 years. The company's focus is increased quaternary care and increased throughput. The company is investing to improve throughput such as changing old MRIs, renovation work and this delivers highest RoCE.
- New hospitals performance: New hospitals continue to perform in-line with company's expectations. Management targets Mumbai hospital to be EBITDA positive by end of FY24. Ahmedabad facility continues to generate positive EBITDA (mid-single digit), albeit lower than the average domestic margins. NHL is prioritizing investments in flagship Bangalore, Kolkata and Cayman; new hospitals would not be a major drag on margins as their contribution is low.
- Narayana Health Integrated Care: The newly launched retail health venture, Narayana Health Integrated Care (NHIC), is gaining good traction. The company has expanded its presence across six touchpoints in Bangalore. It achieved revenue of ~Rs 5.2cr in the quarter, with patient transaction numbers 45,000+. It is still in early phase and the focus is on building an integrated care program.
- Cayman expansion: The radiation oncology block (Block A) commissioned in May'23 and has seen good traction. The block required huge capex but has low operational costs as compared to other specialties. This facility has not been margin dilutive.
  The commercialization of new multi-specialty hospital at Cayman (Block B) is likely to be operationalised by H1FY25 and will be margin dilutive due to high fixed costs.
- NHL continues to pursue M&A opportunities in India and abroad.

- Capex guidance of Rs. 1140 crore in FY24E of which Rs 400 crore incurred in H1FY24. This is a mix of greenfield, brownfield and inorganic. For Cayman, it has guided for a capex of Rs. 590 crore in FY24. In India, it plans to spent Rs. 540 crore across various projects which includes Rs. 120 crore to be spent on purchasing land parcel in Kolkata and Rs. 390 crore to be spent on brownfield and replacement capex.
- Cayman - Newly commissioned radiation oncology block at Cayman island saw a meaningful traction. A new multi-specialty hospital at Cayman is on track to be commercialized by Q1FY25. Cayman revenue growth was also aided by consolidation of ENT specialty acquired in March 2023. New hospitals contributed to Rs 120 crore of revenue with EBITDA at Rs. 8.7 crore.
- Brownfield expansion in flagship unit - NH initiated the process to build hospital at already owned land in Health City. Overall plans to build 700 beds in 3-4 years in Bangalore. Added additional two floors in Howrah unit in Kolkata where 110 beds will be operationalized by end of Q4FY24. Margin levers would be technology improvements such as faster online discharges, robotic surgeries, adding more ICUs, OTs, Labs and developing communication between doctors, nurses and patients which would help improve ALOS days.
- Occupancies are above 65% in the India segment. As the company continues to work on improving throughput, there is scope for increasing footfalls at existing hospitals.
- NH continues to explore brownfield opportunities in Bengaluru and Kolkata. It has initiated the process of construction at the excess land at Bengaluru. In Kolkata, NH is scouting for land (at an advanced stage) and will start construction in H1FY25.
- EBITDA margin in Cayman have improved sequentially due to healthy offtake in the radiology oncology block.
- Net debt, as of September 2023, stood at Rs 86 crore, which includes US$ 52mn foreign currency denominated debt, implying a net debt-equity ratio of 0.03x.
- In Q2FY24, India business reported revenue growth of 14.7% YoY and 6.7% QoQ at Rs. 1053 crore. It was mainly due to 7.6% growth in inpatient volume which were at 64,000, while OP footfalls were at 685,000, growth of 11.7%.
- ARPOB for India business witnessed growth of 10.7% YoY to Rs 36712 with occupancy level of 60%.
- Cayman business recorded revenue of 12.7% YoY and 5.7% QoQ to Rs 261 crore. This was mainly due to improvement in ARPOB by 9.5% YoY and incremental revenues from addition of oncology unit.
- Average revenue per patient (ARPP) in Cayman was at US$ 34,100 in Q2FY24 which has witnessed a decrease of 13.2% YoY.
- Brownfield expansion: The company is looking for brownfield expansion plans in Bangalore and Kolkata, there has been some progress in acquiring land within the Health City campus. The advantageous stages of closure in obtaining land in Kolkata are noteworthy.
- Company foresees a reduced YoY tax rate for FY24 to the tune of 10-12%. Looking ahead to FY25, the tax rate applicable to the India business is likely to settle in the range of 23-25%.

Key Triggers:

India Business remain on strong footing

NHL has a network of 40 healthcare facilities in India, including 18 owned/operated hospitals, 1 managed hospital, 3 heart centres and 17 primary care facilities and one facility at Cayman having 6,096 bed capacity and 30+ specialities. Company derived 35% of revenue from Cardiac segment, 13% from Gastro, 14% from Oncology, 9% from Renal and the balance from others in FY23. Company has an established presence and strong brand recognition in India especially in two geographies (Bangalore and Karnataka). India business reported healthy revenue growth of 22.8% YoY to Rs 3642cr in FY23 on account strong inpatient volumes & OPD footfall and robust traction demonstrated by new units. In H1FY24, India hospitals revenue grew 15.8% YoY at Rs 2043cr along with better margin. Company's flagship hospitals in Bangalore and Kolkata saw robust recovery after pandemic; cardiac sciences-led high-end elective work and footfalls in out-station and international patients. EBITDA margin improved ~500bps YoY in FY23 to 18.3% on the back of gradual pick-up in high-end procedures/surgeries. The company rationalized its portfolio by exiting operations at ophthalmology-focused centre in Kolkata and Cardiac Care operations in Bangladesh. To cement its position in India, the company is prioritizing debottlenecking and brownfield expansion at its existing centres. It is open to pursue strategic growth through greenfield facilities at core regions as well as inorganic opportunities.

The "Narayana Health" brand is widely recognized for providing high-quality healthcare at affordable prices. Company operates at lower ARPOB compared to its peers, the company has over the years implemented and followed unique cost control measures right from construction of hospital buildings to sourcing equipment and consumables. India business ARPOB growth would not come much from pricing, but from increased throughput and increased quaternary care in the overall mix. Payor mix and room configuration are focused to target middle class, resulting in lower ARPOB compared to peers. Adding new service lines, improving case mix and investment in new capacity at Bangalore and Kolkata to address and upgrade the infrastructure and faster patient discharges would lift ARPOB.

There would not be meaningful bed additions in the next 3 years in India. Its key priority is to add brownfield capacities at existing hospital units. The company is focused on improving the throughputs in the ICUs – investing in technology to facilitate better communication tools between doctors and nurses, ensure faster discharges, lab results, seamless appointments. Infrastructure enhancement and internal refurbishment would address patient bottlenecks (adding OTs, ICUs, lab billing). Room upgrades, equipment upgradation new service lines like adding new diagnostic therapies and plans for adding oncology units Jaipur, Ahmedabad and Mysore is also in works. Bed additions to address few specialties at existing units which already sees high occupancies would be key lever in the near term. NHL would be building specialties and capabilities across different units based on the demand and traction in specific specialities. In Bangalore, it will be adding infrastructure to the Health City and would look for expansion to the heart hospital; via partnership with land owners. For Kolkata, the company is looking to acquire land parcel and add new infrastructure close to its existing hospital. These projects would take a duration of 3-4 years; and will be operationalized in phases. Further expansion in Raipur would require securing land nearby in conjunction with the trustees. Other small hospitals in Mysore, Shimoga have enough brownfield capacity for adding departments. 'Narayana Health' brand is strongly associated with its ability to deliver high-quality, affordable healthcare services by leveraging economies of scale, skilled doctors, and an efficient business model. Steady revenue from newer hospitals, change in payor mix, increase proportion of higher-end surgeries coupled with high bed turnover (lower ALOS) are key drivers in the near term.

India - Operational Performance

	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24
Revenue (Rs cr)	682	764	772	757	852	910	897	977	990	1053
EBITDA (Rs cr)	56	100	108	94	138	182	172	187	180	213
EBITDA Margin (%)	8.2%	13.1%	14.0%	12.4%	16.2%	19.9%	19.1%	19.1%	18.2%	20.3
ARPOB per day (Rs)	30,685	33,425	32,055	33,425	33,425	33,699	35,068	36,986	37,260	36712
ALOS (days)	5.4	4.6	4.6	4.6	4.6	4.5	4.5	4.4	4.4	4.4
Discharges (#)	3,32,900	5,26,300	5,20,200	49,000	5,72,000	6,13,400	5,81,700	5,95,000	6,14,000	6,85,000
ICU Occupied Beds	97,000	86,400	86,600	85,000	86,000	87,500	87,600	87,000	90,000	1,04,000

(Source: Company, HDFC sec)

Strong performance at its flagship Hospitals

Narayana reported impressive performance at its flagship hospitals. Healthy revenue growth coupled with increasing ARPOB and EBITDA lifted its overall performance. The company's flagship units in Health city are running at optimum utilization. Scope for occupancy & volume expansion is limited until a full scale capacity expansion is not undertaken which would happen in the next 2-3 years. Margin expansion in these facilities may come from improving its efficiency – reducing ALOS, change in payor profile mix, case mix. But, the next level of growth would come from capacity expansion (brownfield, greenfield). Also, reversion of international patient mix (8-9%) which saw greater traction in its flagship hospitals would be an important growth lever. Currently, its flagship hospitals mainly Bangalore and Kolkata do not have enough capacity to cater to higher patient volumes; they have peaked out in ICU beds, OPD rooms. There is no scope for expansion in existing campus in Kolkata; so it has announced plans to build greenfield hospital. Expansion in other hospitals like Bangalore and Raipur would be brownfield. These hospitals will be massive health cities that have the best and latest equipment, conduct large number of training programs, and will be the sites for cutting edge clinical research. The management in their latest earning call reiterated their focus on core and high performing regions such as Bangalore, Kolkata and Cayman which enhances growth visibility. NHL has a steady expansion plan and is committed to refurbishing its flagship facilities in Bangalore and Kolkata, which would help to improve the quality of healthcare services offered to patients.

Received license to launch health insurance business from IRDAI

Some time back, the company has received license from IRDAI to launch health insurance business in India. This strategic move aims to bridge the gap between healthcare services and insurance, bringing more comprehensive and integrated solutions to patients and healthcare customers. Narayana Health Insurance Limited would carry health insurance business in India. It would cover both Inpatient and

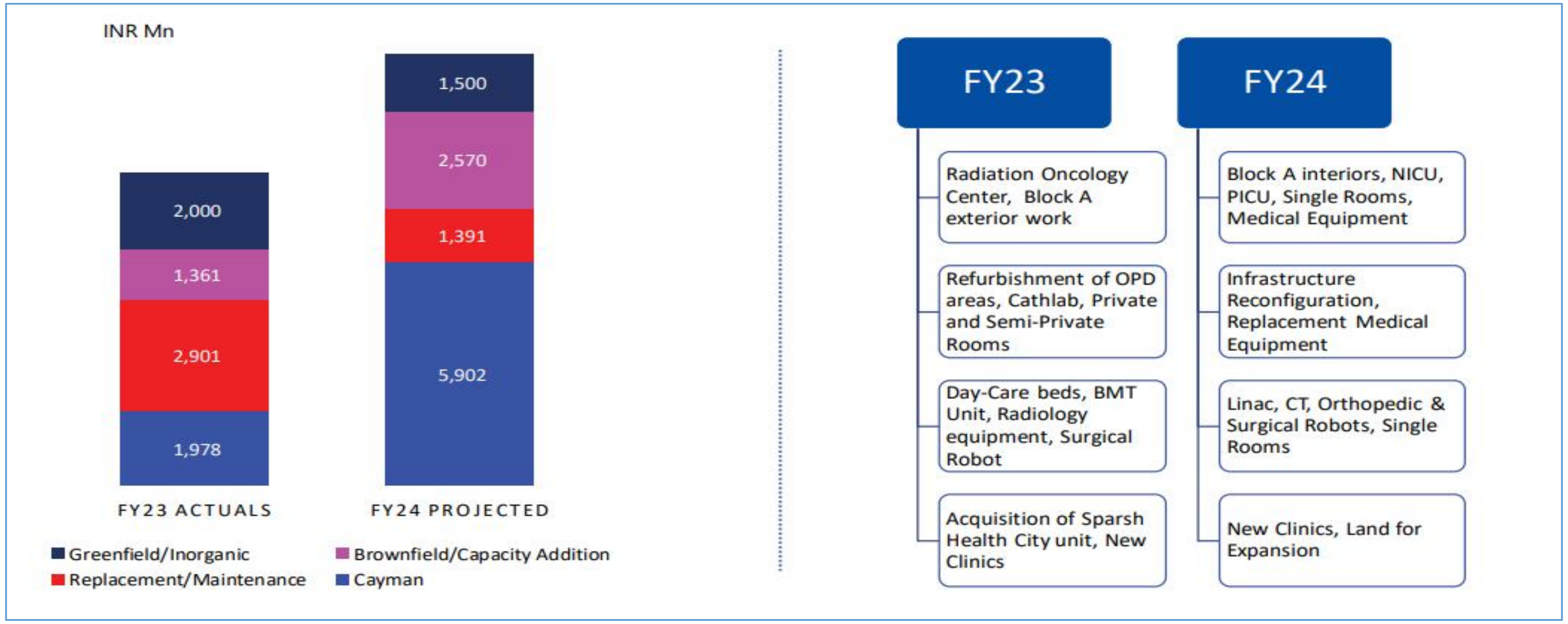
Outpatient programme. Company got the license in just about 5 months, which is one of the fastest health insurance license. It would initially launch at Bengaluru cluster and then at Kolkata and then gradually cover its other facilities.

Improving maturity mix; new hospitals to see improvement in near term

Strong performance of flagship units is complemented by steady improvement in new hospitals (Dharamshila, Gurugram & SRCC (Mumbai)). Improving occupancy and footfalls coupled with increasing ARPOB resulted in narrowing losses. EBITDAR margin improved from -15.8% in FY21 to -3.5% in FY22. These new hospitals saw improvement in performance and generated 7% EBITDA margin in H1FY24. Gurugram Hospital generated a revenue of ~Rs 133cr, EBITDA margin of 3%. While Dharmshila hospital clocked revenue of Rs 209cr, EBITDA margin of 14%. NHL has taken correction measures as it marked its presence in newer regions. Dharamshila which was heavily focused on oncology, saw gradual improvement in case mix as the company added new specialties. Known for its oncology treatment for two and half decades, growth in other specialities has been relatively slow. Gurugram has 223 bed capacity is relatively smaller facility compared to peers in the city. It has been underperforming as not being strategically located and didn't attract high clinical talents and consultants across various specialities. The company plans to recalibrate its approach in the market and play by its strengths; it would offer only those specialties that would best fit the market. In the western cluster, Ahmedabad has similar dynamics as Mumbai, where consultants don't get themselves empaneled to a single hospital. Even though it managed to get full time consultants and doctors from outside Ahmedabad, it did not work. Also, the payor mix was not favorable as it heavily dependent on low income patients who are under a government scheme. NHL is adding oncology unit and high-end private, semi-private rooms to improve its operational performance. The management targets Mumbai hospital to be EBITDA positive by the end of FY24. Ahmedabad facility continues to generate positive EBITDA (mid-single digit).

NH's hospital usually takes 3-4 years to breakeven, and post that another 3-4 years to reach maturity. The company would be expanding the facility depending on the occupancy and demand. In Gurugram, it wants to add two more floors and in Dharamshila, it is in talks with hospital trustees to expand another wing. Bombay Children Hospital had taken relatively longer time to reach the desired profitability. The utilization level of Mumbai pediatric hospital is 65%. This hospital had been struggling for quite few years to break even due to low patient's admission. Being highly specialized in children's care and it has very different earnings profile and would take longer time to break even. Both Gurugram and Dharamshila are expected to reach sustainable margin level in next couple of quarters, while SRCC would take around a year. Measures to improve the performance in new hospitals would bear fruit in the near term and would be a key lever lifting the profitability.

Capex Programs



Cayman operations is on strong trajectory with improved operations and profitability

Narayana owns and operates Health City Cayman Islands (HCCI), which is a 110-bed facility located in the Cayman Islands, Caribbean. HCCI has continued to deliver strong and consistent performance over the last few quarters. It posted strong revenue of US$ 109.2 million (up 18.8% YoY) with EBITDA margin of 40%+ in FY23. In H1FY24, revenue grew 19% YoY at US$ 61.4 million and a strong 40% increase in EBITDA. Strong pickup in patient footfalls was on account of gaining traction from neighbouring islands. During covid related restrictions, high-net-worth Caymanian population chose treatment at HCCI for some high-end procedures, instead of travelling abroad (US). Although some percentage, especially insured would definitely go back to US as they are more comfortable of getting treated there; but the covid crisis has enhanced NHL's credibility and would retain some percentage of such HNI patients which augurs well for medium-term growth. Moreover, higher outpatient/daycare work which has higher margin improves the overall profitability.

NHL is making investments in primary care and oncology block. During FY22, it opened state-of-the-art clinic which will be integrated into the larger new campus. The group recently acquired ENT in Cayman Ltd. (EICL), a Cayman Islands resident company providing complete diagnosis and treatment of ear, nose, and throat conditions for cash consideration of US$ 5 million. It is opening up pharmacies, clinics and plans to setup a diagnostic centre in the future as a part of its overall strategic to engage more patients hooked into the whole HCCI ecosystem.

Cayman Business	Q1FY22	Q2FY22	Q3FY22	Q4FY22	Q1FY23	Q2FY23	Q3FY23	Q4FY23	Q1FY24	Q2FY24
Revenue (in US$ mn)	23.2	19.7	24.9	24.4	22.7	29.1	28.2	29.3	29.9	31.5
ARPOB (US$/day)	5,205	5,205	5,479	5,205	5,205	5,753	6,027	6,027	6,301	6,317
Discharges	694	594	591	578	533	545	492	627	629	558
Out Patients	8198	7451	6781	8239	7950	7609	7647	7116	8214	9615

(Source: Company, HDFC sec)

The company incurred capex of Rs 198cr in FY23 and plans to spend Rs 590cr in FY24 for expansion of its Cayman operations with a new hospital in the city centre. The new hospital at Camana Bay is likely to improve HCCI's reach to patients both – international and local, due to close proximity to the airport (10-min drive) and several major residential complexes. This will enable NHL to cater to local residents, who usually travel abroad for high-end medical treatment. The new facility will include an advanced Cancer Center which will offer comprehensive oncology treatment including bone marrow transplant, CAR-T cell therapy, medical oncology, haemato oncology, surgical oncology and radiation oncology. The new facility would complement the existing set up by focusing more on day care, short stay but niche categories of oncology care while the existing facility would continue to cater to tertiary and quaternary care. The hospital will be commissioned in two phases; first phase - radiotherapy facility (Block A) commenced operations in May'23 which is likely to fuel revenue growth going forward. The rest of the IP rooms and ancillary businesses will be commissioned in H1FY25. On commercializing of new facility (Block B); there would be some margin dilution due to upfront fixed costs and shifting of business from existing facility to the new facility. Given the city centric-location of the facility and focus on high-end oncology & critical care, NHL expects to break-even at a rapid pace. Management's long term EBITDA target is 40-45%.

Although management target of getting traction of the medical tourists from overseas (US, Canada) fell short of expectation. Covid restriction enhanced NHL's credibility and quality services by serving affluent local population. Medical tourists from overseas would play out over the years as it built its foundation and improves its brand name. The management is engaging with other islands and government to move their patient to their facility. Commencement of operations of new facility which has radiotherapy and Oncology would address the gaps and perhaps gain more patient footfalls. The company plans to enter into consultancy contract (asset-light projects/ arrangements) in nearby countries to understand the market better and improve its positioning. Improving credibility, capacity expansion, focus on primary and daycare coupled with likely traction from overseas medical patients makes a case for strong trajectory going ahead.

~40% EBITDA contribution in H1 FY24, Cayman's relevance continues to grow

Post commencing operations in the year 2014, the Cayman facility underperformed for the initial 4-5 years. Contrary to its original plan of attracting medical tourists, a huge majority of the current patient volumes are locals from Cayman. Pre-Covid, NH's Cayman operations were contributing ~20% to its overall EBITDA. With greater acceptance from locals post Covid coupled with a better case mix, Cayman contributed ~40% to consolidated EBITDA in H1FY24.

At the time of its inception, the company intended the Cayman unit to primarily focus on attracting patients from the US, Canada and Latin America. However, it proved to be a challenge for NH. Currently, a huge majority of the patient volumes are locals from Cayman, with some from other Caribbean islands and very few patients from the US and LatAm.

Acquisition in Bangalore to complement other specialties

NHL signed an agreement with Shiva and Shiva Orthopaedic Hospital to acquire its 100 beds Orthopedic and Trauma Hospital in Bengaluru (Sparsh Hosur Road unit) on slump sale basis for consideration Rs 280cr (subscribed optionally convertible debentures of Rs 80cr to be redeemed after 4 years). This unit has strong operational track record of offering orthopaedic services and generated revenue of Rs 49cr in FY22. The acquisition was a little expensive given its margin profile ~20-25% (17-18x EV/EBITDA). It added orthopaedic specialty and supplement other specialties of its Health City operations by supporting Trauma patients for cardiac, renal, pulmonary, neuro and other multi-organ treatments thereby increasing the breadth of the multispecialty program at its flagship campus. It is only used for orthopedics and will free up a capacity of 140 beds at Bangalore Health City. There is scope of adding 100 beds (which will be taken up gradually). Ramp-up of this facility would be a key driver in the medium term.

Incorporation of Narayana Health Insurance to explore integrated care segment

NHL has established Narayana Health Integrated Care, a new entity aimed at exploring the managed/integrated care segment. The newly formed entity's main objective is to carry on health insurance business. The company would provide primary care services in these clinics and offer remote services such as home care, online care, and long-term care plans. Eventually, it will combine this primary care with a comprehensive health insurance plan that would cover not just hospitalization expenses but also outpatient expenses. Revenue model would be subscription based as well as direct sales (medicines, lab tests, consulting fees, diagnostics). This would be capex light and would achieve breakeven relatively faster. Although EBITDA margin would be lower compared to hospitals; the management does not expect much impact on consolidated RoCE given the small scale of operations. The company has expanded its presence across six touchpoints in Bangalore. It achieved revenue of Rs 4.5cr in Q1FY24, with patient transaction numbers 29,000+. It achieved revenue of Rs 5.2cr in Q2FY24, with patient transaction numbers at 45,000. It is still in its early phase and the focus is on building an integrated care program. Scale up of this segment would be key to monitor.

Key Concerns:

Delay in project execution and challenges in expansion in adjacent territories: The company has set timelines for increasing its bed capacity and its entry into new markets. As the company believed in procurement of land and construction of building; approvals regarding the same could take time. Delay in commissioning of these projects would impact its topline growth. Also, upfront capex for additional capacity is high due to land acquisition; debt funding would be required.

Competitive Intensity: 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. Entry of other players in Cayman Island could impact revenue and operating performance over medium over for the facilities located there.

Operational Risk: Any delay in commissioning or expansion (reaching breakeven) of new facilities may impact overall growth, thus impacting overall financials. Lower occupancy level in hospitals could impact its profitability. With respect to its Cayman operations, inability to sustain patient footfalls at existing units and extended payback period for the new unit remains a key risk.

Exposed to regulatory risks inherent in the sector: Regulatory risks pertaining to restrictive pricing regulations levied by the Central and State governments could constrain profit margins of the company. Any adverse government policy intervention, viz. price caps would impact its margins.

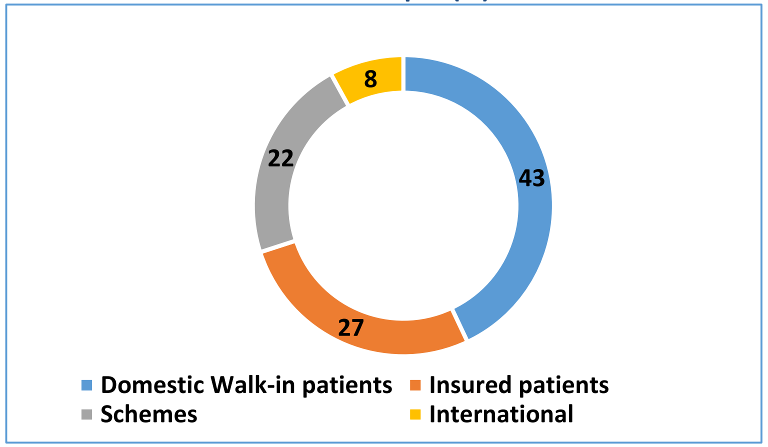
Discontinuation of leases: The company's operations are carried out in leased hospital buildings. In the event of these leased properties are not renewed or are not renewed on favourable terms to the company, its business operations would be disrupted.

Company Background

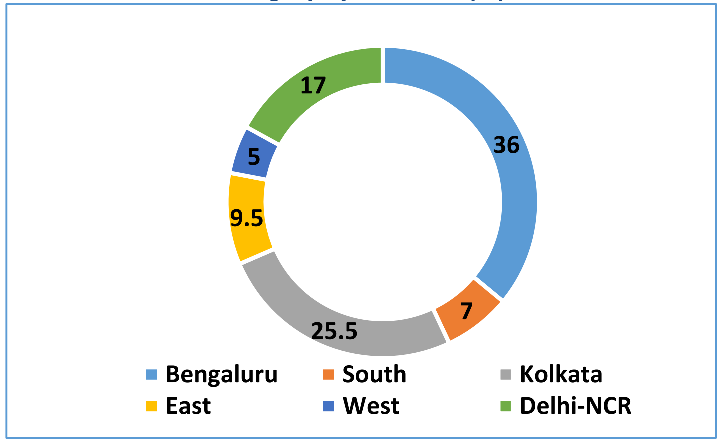
Narayana Hrudayalaya Ltd (NHL) is a healthcare service provider that operates a chain of multi-specialty hospitals in India and in the Cayman Islands. NHL has a network of 40 healthcare facilities, including 18 owned/operated hospitals (multi-speciality and super-speciality healthcare facilities which provide tertiary care), 1 managed hospital, 3 heart centres and 17 primary care facilities (including clinics and information centres) having 6,096 bed capacity. The company has a strong track record of providing quality healthcare services at an affordable cost. NHL was founded by Dr. Devi Shetty in 2000 and is headquartered in Bengaluru. NHL has a strong presence in the southern state of Karnataka and eastern India, with an emerging presence in western, northern and central India. Narayana Hrudayalaya owns and operates Health City Cayman Islands (HCCI), which is a 110-bed facility located in the Cayman Islands, Caribbean (contributes ~20% to revenue).

NHL's centres provide advanced levels of care in over 30 specialties, including Cardiology and Cardiac Surgery, Cancer Care, Gastroenterology, Neurology and Neurosurgery, Orthopaedics, Nephrology and Urology. The business is attractively placed to create an affordable, globally-benchmarked quality-driven healthcare services model. "Narayana Health" brand is strongly associated with its ability to deliver high-quality, affordable healthcare services by leveraging economies of scale, skilled doctors, and an efficient business model. Despite lower ARPOBs (~30-35% lower than peers), its profitability and return ratios are largely in line with peers given it has followed an asset-light expansion model with a strong focus on achieving operational efficiencies through cost optimisation measures and economies of scale.

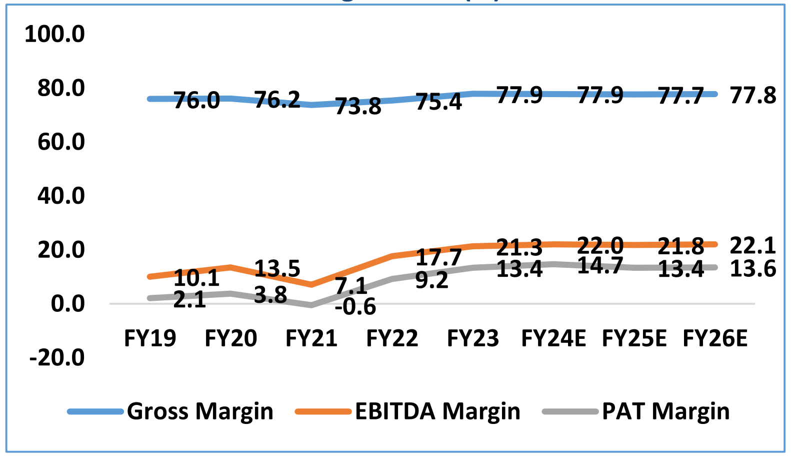
Revenue Split (%)



Geographywise Mix (%)



Margin Trend (%)



(Source: Company, HDFC sec)

Financials (Consolidated)

Income Statement

(Rs cr)	FY21	FY22	FY23	FY24E	FY25E	FY26E
Total Revenue	**2583**	**3701**	**4525**	**5164**	**5759**	**6685**
Growth (%)	-17.4	43.3	22.2	14.1	11.5	16.1
Operating Expenses	2400	3048	3559	4028	4504	5208
EBITDA	**183**	**654**	**966**	**1136**	**1256**	**1477**
Growth (%)	-56.8	257.5	47.8	17.6	10.5	17.6
EBITDA Margin (%)	**7.1**	**17.7**	**21.3**	**22**	**21.8**	**22.1**
Depreciation	184	183	210	236	271	322
EBIT	**-1**	**470**	**756**	**900**	**985**	**1155**
Other Income	27	35	65	72	79	87
Interest expenses	76	66	69	88	89	75
PBT	-49	438	752	885	976	1167
Tax	-42	88	145	124	203	257
RPAT	**-7**	**351**	**607**	**760**	**773**	**910**
Growth (%)	-	-	77.3	25.2	1.5	17.6
EPS	**-0.7**	**16.9**	**29.9**	**37.1**	**37.7**	**44.3**

Balance Sheet

As at March (Rs cr)	FY21	FY22	FY23	FY24E	FY25E	FY26E
SOURCE OF FUNDS						
Share Capital	204.4	204.4	204.4	204.4	204.4	204.4
Reserves	916	1284	1927	2637	3346	4193
Shareholders' Funds	**1120**	**1489**	**2131**	**2841**	**3551**	**4397**
Minority's Interest	1	1	1	2	2	4
Long Term Debt	673	567	715	1045	945	745
Net Deferred Taxes	11	50	81	81	81	81
Long Term Provisions & Others	259	243	240	280	313	363
Total Source of Funds	**2065**	**2349**	**3169**	**4250**	**4892**	**5590**
APPLICATION OF FUNDS						
Net Block & Goodwill	1963	1984	2336	3200	3780	3958
CWIP	18	63	259	259	259	259
Other Non-Current Assets	122	173	267	305	369	426
Total Non Current Assets	**2103**	**2219**	**2863**	**3765**	**4408**	**4643**
Current Investments	110	131	251	251	251	251
Inventories	48	59	72	89	110	128
Trade Receivables	279	437	432	499	568	654
Cash & Equivalents	132	172	380	561	490	899
Other Current Assets	97	109	160	184	208	262
Total Current Assets	**665**	**909**	**1294**	**1589**	**1634**	**2202**
Short-Term Borrowings	152	156	169	229	201	163
Trade Payables	410	449	615	640	702	806
Other Current Liab & Provisions	141	174	203	235	246	286
Total Current Liabilities	**703**	**779**	**987**	**1104**	**1150**	**1255**
Net Current Assets	-38	130	307	485	484	947
Total Application of Funds	**2065**	**2349**	**3169**	**4250**	**4892**	**5590**

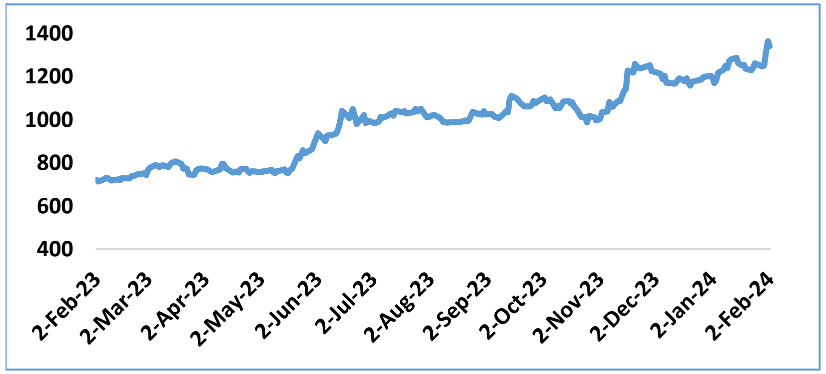
(Source: Company, HDFC sec)

Narayana Hrudayalaya Ltd.

Cash Flow Statement

(Rs Cr)	FY21	FY22	FY23	FY24E	FY25E	FY26E
Reported PBT	-14	342	607	885	976	1,167
Non-operating & EO items	-38	120	194	-12	-38	-17
Interest Expenses	63	58	54	88	91	73
Depreciation	184	183	210	234	269	322
Working Capital Change	56	-152	105	-41	-35	-5
Tax Paid	54	-67	-86	-124	-203	-257
OPERATING CASH FLOW (a)	**304**	**485**	**1,085**	**1,030**	**1,059**	**1,282**
Capex	-70	-250	-521	-1,100	-850	-500
Free Cash Flow	235	235	563	-70	209	782
Investments	-42	-27	-401	0	0	0
Non-operating income	-1	11	-254	0	0	0
INVESTING CASH FLOW (b)	**-113**	**-267**	**-1,176**	**-1,100**	**-850**	**-500**
Debt Issuance / (Repaid)	-150	-123	151	390	-128	-238
Interest Expenses	-43	-36	-43	-88	-91	-73
FCFE	41	76	671	232	-10	471
Share Capital Issuance	0	0	0	0	0	0
Dividend	0	0	-20	-51	-61	-61
Others	0	0	0	0	0	0
FINANCING CASH FLOW (c)	**-194**	**-159**	**88**	**251**	**-280**	**-372**
NET CASH FLOW (a+b+c)	**-2**	**59**	**-4**	**181**	**-71**	**409**

One Year Price Chart



Key Ratios

Particulars	FY21	FY22	FY23	FY24E	FY25E	FY26E
Profitability (%)						
EBITDA Margin	7.1	17.7	21.3	22	21.8	22.1
EBIT Margin	1	13.6	18.1	18.9	18.5	18.6
APAT Margin	-0.6	9.2	13.4	14.7	13.4	13.6
RoE	-1.3	26.2	33.5	30.6	24.1	22.9
RoCE	1.4	24.3	31.4	27.3	24.2	24.8
Solvency Ratio (x)						
Debt/EBITDA	4.5	1.1	0.9	1.1	0.9	0.6
D/E	0.7	0.5	0.4	0.4	0.3	0.2
PER SHARE DATA (Rs)						
EPS	-0.7	16.7	29.7	37.2	37.7	44.4
CEPS	8.3	25.7	39.9	48.7	50.9	60.2
Dividend	0	0	0	2.5	3	3
BVPS	54.8	72.8	104.3	139	173.7	215.2
Turnover Ratios (days)						
Debtor days	38	35	35	33	34	33
Inventory days	8	5	5	6	6	7
Creditors days	55	42	43	44	43	41
VALUATION (x)						
P/E	-	80.2	45.2	36	35.6	30.2
P/BV	24.5	18.4	12.9	9.7	7.7	6.2
EV/EBITDA	153.7	42.8	28.9	24.7	22.3	18.6
EV/Revenues	10.9	7.6	6.2	5.4	4.9	4.1
Dividend Yield (%)	0	0	0	0.2	0.2	0.2
Dividend Payout (%)	0	0	0	6.7	8	6.8

KUSHAL MAHENDRA RUGHANI

Digitally signed by KUSHAL MAHENDRA RUGHANI
Date: 2024.02.05 09:39:05 +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
For grievance redressal contact Customer Care Team Email: customercare@hdfcsec.com Phone: (022) 3901 9400