



RESULT UPDATE

APOLLO HOSPITALS

Sets the stage for expansion

India Equity Research | Healthcare



Apollo Hospitals (APHS) is our top pick in the healthcare sector, and its Q1FY20 performance reaffirms our conviction that the company is on track to achieve healthy earnings growth. Key highlights: i) Overall EBITDA grew by 21% YoY and margin expanded by 45bps to 12.3% - 200bps margin expansion at new hospitals and 40bps at mature hospitals. ii) A 50% sequential reduction in AHLL losses to INR47mn, on track to break even in FY20. iii) Pharmacy revenue grew by 18% YoY and operating margin rose by 90bps YoY to 5.6%. Management has guided for INR6bn in debt reduction to INR25bn in FY20 on the back of: i) savings following the Pharmacy business spinoff; ii) liquidation of investments; and iii) internal accruals. As the capex cycle concludes and loss-making ventures break even, the stage is set for APHS to expand EBITDA margin and RoCE to mid-teens over the next three years. Maintain 'BUY' with a TP of INR1,700 (20x December 2020E EBITDA).

Strong show across geographies

Chennai cluster, largest geographical region, grew 14% YoY, led by 4% volume growth. Hyderabad region grew 12% with flat volume growth and Bangalore region grew 14% led by 10% volume growth. Proton EBITDA losses were INR81mn (from INR47mn in Q4FY19). Navi Mumbai contributed INR28mn to hospital EBITDA, and the company has guided for INR300mn in FY20. The promoter pledge reduced to 71.26% from 78.13% at end-FY19.

RoCE to get a boost; pledging to reduce post-Munich transaction

Two of APHS's businesses are yet to fuel RoCE growth as: 1) new hospitals with about INR21bn in capital employed are running at 63% occupancy; and 2) AHLL with about INR6bn in capital employed is clocking about 35% utilisation. Going forward: i) profitable growth at Navi Mumbai; ii) AHLL breakeven; and iii) disciplined cost control would drive margin expansion. As capex moderates to maintenance levels, we expect RoCE to rise from 9.7% to 13.3% over FY19-21E. Besides, management upheld its timeline to cut promoter pledge to 35% following stake sale in Munich.

Outlook and valuation: Attractive; maintain 'BUY'

Over FY19-21, we estimate EBITDA CAGR will be about 14%, margin will expand about 100bps and RoCE would rise about 350bps to 13.3%. The stock is trading at 14.4x FY21E EBITDA. We maintain 'BUY/SO' with our SoTP-based target price of INR1,700.

Financials (Consolidated)						(INR mn)		
Year to March	Q1FY20	Q1FY19	% chg	Q4FY19	% chg	FY19	FY20E	FY21E
Net revenue	25,719	22,046	16.7	25,214	2.0	96,174	1,05,978	1,14,508
EBITDA	2,945	2,323	26.8	2,827	4.2	10,637	12,727	13,732
EBITDA margin (%)	11.5	10.5		11.2		11.1	12.0	12.0
EV/EBITDA (x)						20.6	17.4	15.6
ROACE (%)						9.7	12.3	13.3

EDELWEISS 4D RATINGS

Absolute Rating	BUY
Rating Relative to Sector	Outperform
Risk Rating Relative to Sector	Low
Sector Relative to Market	None

MARKET DATA (R: APLH.BO, B: APHS IN)

CMP	: INR 1,360
Target Price	: INR 1,700
52-week range (INR)	: 1,445 / 997
Share in issue (mn)	: 139.1
M cap (INR bn/USD mn)	: 189 / 2,592
Avg. Daily Vol.BSE/NSE('000)	: 807.8

SHARE HOLDING PATTERN (%)

	Current	Q4FY19	Q3FY19
Promoters *	34.4	34.4	34.4
MF's, FI's & BK's	13.3	13.1	11.2
FII's	44.0	44.3	47.1
Others	8.3	8.2	7.3
* Promoters pledged shares (% of share in issue)			NIL

PRICE PERFORMANCE (%)

	Stock	Nifty	EW Pharma Index
1 month	0.8	(8.1)	(1.3)
3 months	13.1	(5.6)	(10.5)
12 months	36.1	(4.7)	(13.7)

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Q1FY20 conference call: Key highlights

Performance highlights:

- AHLL reported an EBITDA loss of INR47mn in Q1FY20 compared with an EBITDA loss of INR191mn in Q1FY19.
- With AHLL, the growth breakdown/outlook is: Cradle business: 30% YoY; Spectra: 17% YoY; Clinics: 20% YoY; diagnostic:-42% YoY—expected to sustain; sugar: 10% YoY; dental: growth expected in the coming quarters; dialysis: strong growth on a small base, estimates are muted for the year.
- Navi Mumbai (225 beds): 200 beds were occupied this month. It contributed INR28mn to EBITDA, and the company has INR300mn EBITDA target for FY20.
- No price increase was taken this quarter.
- Contribution of private labels in standalone pharmacies (SAP) has risen from 6.7% in FY19 to 7%. The plan is to move to 10% over the next two–three years.
- Capping of trade margins in oncology drugs did not impact margins.

Debt and cash flow

- Gross debt: standalone: INR31.29bn (decreased by INR700–800mn); consolidated: INR37bn
- Net debt stood at INR29.31bn and net debt/EBITDA at 2.79x.
- Going forward, the company is targeting gross debt of INR25bn as:
 - hiving-off of pharmacy should bring in savings worth INR3.5bn;
 - liquidation of one of the investments should bring in INR2.5bn; and
 - the balance will be funded from internal cash flows.
- INR1.7bn in capex to be incurred in Q2FY20 on the proton therapy centre (150 beds).

Update on promoter pledge

- APHS increased the pledge marginally to fund the Munich transaction.
- The company expects a liquidity event in September–October 2019, which will reduce pledge by 40–50%.
- The company is on track to bring the promoter pledge below 20% by the end of the year.

FY20 guidance

- 23% EBITDA margin for the mature health services.
- High-teen RoCE for Tier 2 and 22% for Tier 1.
- On the proton therapy centre, it is performing well and losses worth INR250mn are likely.

Table 1: Revenue and EBITDA breakdown by segment

	Q1FY18	Q2FY18	Q3FY18	Q4FY18	Q1FY19	Q2FY19	Q3FY19	Q4FY19	Q1FY20
Standalone hospitals (existing)									
Revenue	7,478	8,029	7,897	7,949	8,064	8,864	9,002	8,924	8,064
EBITDA	1,507	1,758	1,692	2,411	1,742	1,923	1,960	1,968	1,742
EBITDA margin(%)	20.2	21.9	21.4	30.3	21.6	21.7	21.8	22.1	21.6
Standalone hospitals (new)									
Revenue	1,724	1,956	2,058	2,050	2,120	2,399	2,570	2,558	2,120
EBITDA	(91)	94	151	77	108	147	170	179	108
EBITDA margin(%)	(5.3)	4.8	7.3	3.8	5.1	6.1	6.6	7.0	5.1
Standalone pharmacies									
Revenue	7,642	7,805	8,606	9,383	8,921	9,637	10,119	10,183	10,568
EBITDA	320	357	252	550	417	508	549	557	417
EBITDA margin(%)	4.2	4.6	2.9	5.9	4.7	5.3	5.4	5.5	3.9
AHLL									
Revenue	677	1,535	(198)	2,575	1,316	1,484	1,512	1,576	1,316
EBITDA	(283)	(231)	(263)	(369)	(197)	(138)	(167)	(97)	(197)
Total consolidated revenue									
Revenue	19,031	20,893	14,294	28,217	22,046	24,006	24,908	25,214	22,046
EBITDA	1,647	2,247	2,170	1,868	2,323	2,719	2,768	2,827	2,323
EBITDA margin(%)	8.7	10.8	15.2	6.6	10.5	11.3	11.1	11.2	10.5

Source: Company, Edelweiss research

Table 2: SOTP valuation on June 2020 financials

Valuation	Dec-20
Hospital business	
Multiple (EV/EBITDA)	20
EBITDA (June '20)	10,414
EV	208,281
Pharmacy business	
Multiple (EV/EBITDA)	15
EBITDA (June '20)	2,550
EV	38,257
AHLL (71% stake)	11,017
Apollo Munich Health Insurance (10% stake)	358
Other JVs	6,327
Total EV	264,240
Less: net debt	27,771
Market Cap	236,469
No. of shares	139
Value per share	1,700

Source: Company, Edelweiss research

Financial snapshot

(INR mn)

Year to March	Q1FY20	Q1FY19	% change	Q4FY19	% change	FY19	FY20E	FY21E
Net revenues	22,292	19,104	16.7	21,671	2.9	96,174	105,978	114,508
Cost of revenue	11,631	10,092	15.2	11,262	3.3	46,609	50,869	54,964
Gross profit	10,661	9,012	18.3	10,410	2.4	49,566	55,109	59,544
EBITDA	3,258	2,267	43.7	2,658	22.6	10,637	12,727	13,732
EBITDA margin	14.6	11.9		12.3		11.1	12.0	12.0
Depreciation	1,098	724	51.7	770	42.5	3,955	3,925	3,896
EBIT	2,160	1,543	40.0	1,888	14.4	6,681	8,803	9,836
Interest	999	621	61.0	709	40.9	3,270	2,295	2,295
Other income	47	21	131.2	22	120.5	314	340	465
Add: Exceptional items								
Profit before tax	1,208	942	28.2	1,200	0.7	3,726	6,848	8,006
Provision for taxes	415	341	21.8	433	(4.2)	1,734	3,187	3,725
Minority interest						(359)	(58)	(110)
Associate profit share	-	-		-		10	493	586
Reported net profit	793	602	31.8	767	3.4	2,361	4,212	4,977
Adjusted Profit	880	602	46.3	767	14.8	2,361	4,212	4,977
Diluted shares (mn)	139	139		139		139	139	139
Adjusted Diluted EPS	5.7	4.3	31.8	5.5	3.4	17.0	30.3	35.8
As % of net revenues								
Cost of revenue	52.2	52.8		52.0		48.5	48.0	48.0
Gross profit	47.8	47.2		48.0		51.5	52.0	52.0
Total expenses	101.3	105.8		106.0		88.9	88.0	88.0
Operating profit	9.7	8.1		8.7		6.9	8.3	8.6
Reported net profit	3.6	3.1		3.5		2.5	4.0	4.3
Tax rate	34.4	36.2		36.1		46.5	46.5	46.5

Company Description

Apollo is widely recognised as the pioneer of private healthcare in India, and was the country's first corporate hospital. The Apollo Hospitals Group, which started as a 150-bed hospital in Chennai in 1983 and today, operates 6,800 beds across 61 hospitals. The Group has emerged as the foremost integrated healthcare provider in Asia, with mature group companies that specialize in insurance, pharmacy, consultancy, clinics and many such key touch points of the ecosystem.

The group includes Hospitals, pharmacies, primary care and diagnostic clinics, telemedicine centres and Apollo Munich Insurance branches panning the length and breadth of India. As an integrated healthcare service provider with health insurance services, global projects consultancy capability, medical education centres and a research foundation with a focus on global clinical trials, epidemiological studies, stem cell & genetic research, Apollo has been at the forefront of new medical breakthroughs with the most recent investment being that of commissioning the first Proton Therapy Center across Asia, Africa and Australia in Chennai, India.

Investment Theme

Apollo is well positioned for RoCE improvement as its capex cycle comes to an end and they sweat assets. Apollo has spent ~INR25.9bn (~50% of gross block) over the last 3 years, majority being invested in its Navi Mumbai hospital and in Apollo Health and Lifestyle Limited (AHLL), which are currently incurring losses. Apollo's Navi Mumbai facility has been ramping up well with 80% utilisation of 150 operational beds. We expect the facility to breakeven in FY19 and believe it entails potential to generate INR1bn EBITDA by FY21. AHLL, Apollo's retail healthcare format, with INR5.5bn capital employed, is currently incurring losses. With the diagnostic and clinics already ramping up well, AHLL is on track to breakeven by FY20. Going forward, we believe capex will fall by 50%.

Key Risks

- Success of business depends on expansion of network
- Subsidiaries may be unable to sustain profitability in the future
- Specialist physicians could dis-associate
- Rising infrastructure costs could restrict investment

Financial Statements

Key Assumptions

Year to March	FY18	FY19	FY20E	FY21E
Macro				
GDP(Y-o-Y %)	6.5	7.1	7.6	7.2
Inflation (Avg)	3.6	4.5	5.0	5.9
Repo rate (exit rate)	6.0	6.3	6.5	7.5
USD/INR (Avg)	64.5	70.0	72.0	72.0

Income statement

(INR mn)

Year to March	FY18	FY19	FY20E	FY21E
Income from operations	82,435	96,174	105,978	114,508
Materials costs	40,327	46,609	50,869	54,964
Employee costs	14,044	15,982	17,900	20,048
EBITDA	7,932	10,637	12,727	13,732
Operating profit	7,932	10,637	12,727	13,732
EBIT	4,342	6,682	8,803	9,836
Less: Interest Expense	2,951	3,270	2,295	2,295
Add: Other income	321.5	314.39	340.29	465.00
Profit Before Tax	1,712	3,726	6,848	8,006
Less: Provision for Tax	1,119	1,734	3,187	3,725
Less: Minority Interest	(579)	(359)	(58)	(110)
Associate profit share	2	10	493	586
Reported Profit	1,174	2,361	4,212	4,977
Exceptional Items	-	-	-	-
Adjusted Profit	1,174	2,361	4,212	4,977
Shares o /s (mn)	139	139	139	139
Adjusted Basic EPS	8.4	17.0	30.3	35.8
Diluted shares o/s (mn)	139	139	139	139
Adjusted Diluted EPS	8.4	17.0	30.3	35.8
Adjusted Cash EPS	34.2	45.4	58.5	63.8
Dividend per share (DPS)	5.0	5.0	8.9	10.5
Dividend Payout Ratio(%)	59.2	29.5	29.5	29.5

Common size metrics

Year to March	FY18	FY19	FY20E	FY21E
Materials costs	48.9	48.5	48.0	48.0
Staff costs	17.0	16.6	16.9	17.5
Operating expenses	90.4	88.9	88.0	88.0
Depreciation	4.4	4.1	3.7	3.4
Interest Expense	3.6	3.4	2.2	2.0
EBITDA margins	9.6	11.1	12.0	12.0
Net Profit margins	0.7	2.1	3.9	4.3

Growth ratios (%)

Year to March	FY18	FY19	FY20E	FY21E
Revenues	13.6	16.7	10.2	8.0
EBITDA	8.9	34.1	19.7	7.9
PBT	(4.7)	117.6	83.8	16.9
Adjusted Profit	(46.9)	101.0	78.4	18.2
EPS	(46.9)	101.0	78.4	18.2

Balance sheet		(INR mn)			
As on 31st March	FY18	FY19	FY20E	FY21E	
Share capital	696	696	696	696	
Reserves & Surplus	31,819	32,639	35,361	38,564	
Shareholders' funds	32,515	33,334	36,057	39,259	
Minority Interest	1,324	1,355	1,297	1,186	
Long term borrowings	29,238	29,521	29,521	29,521	
Short term borrowings	3,792	4,982	4,982	4,982	
Total Borrowings	33,030	34,503	34,503	34,503	
Long Term Liabilities	4,813	4,918	4,918	4,918	
Def. Tax Liability (net)	2,393	2,975	2,975	2,975	
Sources of funds	74,076	77,084	79,749	82,841	
Depreciation	3,590	3,955	3,925	3,896	
Net Block	43,857	46,003	45,579	45,183	
Capital work in progress	7,122	8,218	8,218	8,218	
Intangible Assets	3,872	3,813	3,813	3,813	
Total Fixed Assets	54,851	58,034	57,609	57,213	
Non current investments	2,937	3,930	3,930	3,930	
Cash and Equivalents	4,751	4,156	6,279	8,724	
Inventories	5,658	5,848	6,279	6,784	
Sundry Debtors	8,846	10,232	10,511	11,358	
Loans & Advances	7,572	8,165	8,266	8,932	
Other Current Assets	1,341	1,293	1,451	1,568	
Current Assets (ex cash)	23,418	25,537	26,508	28,642	
Trade payable	5,888	7,132	7,247	7,830	
Other Current Liab	5,994	7,441	7,330	7,838	
Total Current Liab	11,882	14,573	14,578	15,669	
Net Curr Assets-ex cash	11,536	10,964	11,930	12,973	
Uses of funds	74,076	77,084	79,749	82,841	
BVPS (INR)	233.7	239.6	259.2	282.2	

Free cash flow		(INR mn)			
Year to March	FY18	FY19	FY20E	FY21E	
Reported Profit	1,174	2,361	4,212	4,977	
Add: Depreciation	3,590	3,955	3,925	3,896	
Interest (Net of Tax)	1,022	1,748	1,227	1,227	
Others	1,654	2,909	(1,441)	(616)	
Less: Changes in WC	2,071	1,481	(1,485)	(531)	
Operating cash flow	5,370	9,492	9,408	10,015	
Less: Capex	6,205	7,138	3,500	3,500	
Free Cash Flow	(4,014)	(917)	3,613	4,220	

Peer comparison valuation

Name	Market cap (USD mn)	Diluted P/E (X)		EV / EBITDA (X)		ROAE (%)	
		FY20E	FY21E	FY20E	FY21E	FY20E	FY21E
Apollo Hospitals Enterprise	2,592	44.9	38.0	17.2	15.7	11.5	12.5
FORTIS HEALTHCARE LTD	1,261	54.8	30.0	17.8	13.5	3.6	5.4
HealthCare Global Enterprises Limited	154	132.5	33.2	12.8	9.5	3.9	8.6
Max India Limited	231	(67.9)	(55.1)	10.2	10.1	(4.6)	(6.0)

Source: Edelweiss research

Cash flow metrics				
Year to March	FY18	FY19	FY20E	FY21E
Operating cash flow	5,370	9,492	9,408	10,015
Financing cash flow	(1,085)	(2,632)	(3,785)	(4,070)
Investing cash flow	(4,049)	(7,138)	(3,500)	(3,500)
Net cash Flow	236	(279)	2,123	2,445
Capex	(6,205)	(7,138)	(3,500)	(3,500)

Profitability and efficiency ratios

Year to March	FY18	FY19	FY20E	FY21E
ROAE (%)	1.7	5.8	11.5	12.5
ROACE (%)	7.1	9.7	12.3	13.3
Inventory Days	47	45	44	43
Debtors Days	36	36	36	35
Payable Days	50	51	52	50
Cash Conversion Cycle	33	30	28	28
Current Ratio	2.4	2.0	2.2	2.4
Gross Debt/EBITDA	4.2	3.2	2.7	2.5
Gross Debt/Equity	1.0	1.0	0.9	0.9
Adjusted Debt/Equity	1.0	1.0	0.9	0.9
Net Debt/Equity	0.8	0.9	0.8	0.6
Interest Coverage Ratio	1.5	2.0	3.8	4.3

Operating ratios

Year to March	FY18	FY19	FY20E	FY21E
Total Asset Turnover	1.1	1.3	1.4	1.4
Fixed Asset Turnover	1.7	2.0	2.1	2.3
Equity Turnover	2.4	2.8	2.9	2.9

Valuation parameters

Year to March	FY18	FY19	FY20E	FY21E
Adj. Diluted EPS (INR)	8.4	17.0	30.3	35.8
Y-o-Y growth (%)	(46.9)	101.0	78.4	18.2
Adjusted Cash EPS (INR)	34.2	45.4	58.5	63.8
Diluted P/E (x)	161.2	80.2	44.9	38.0
P/B (x)	5.8	5.7	5.2	4.8
EV / Sales (x)	2.6	2.3	2.1	1.9
EV / EBITDA (x)	27.6	20.8	17.2	15.7
Dividend Yield (%)	0.4	0.4	0.7	0.8

Additional Data

Directors Data

Prathap C Reddy	Founder, Chairman	Preetha Reddy	Executive Vice Chairperson
Suneeta Reddy	Managing Director	Sangita Reddy	Joint Managing Director
Sanjay Nayar	Non-executive Independent Director	T Rajgopal	Non-executive Independent Director
N Vaghul	Non-executive Independent Director	G Venkatraman	Non-executive Independent Director
Shobana Kamineni	Executive Vice Chairperson	Deepak Vaidya	Non-executive Independent Director
Murali Doraiswamy	Non-executive Independent Director	Vinayak Chatterjee	Non-executive Independent Director
Shirish Moreshwar Apte	Non Executive Director		

Auditors - S Viswanathan

**as per last annual report*

Holding – Top10

	Perc. Holding		Perc. Holding
Pcr investments ltd	19.57	Apollo hospitals ent	14.51
Life insurance corp	5.68	Reddy prathap c	3.91
Alliance bernstein	3.77	Schroders plc	3.57
Vanguard group	2.63	Reddy suneeta	2.43
Morgan stanley	1.99	Reddy sangita	1.75

**in last one year*

Bulk Deals

Data	Acquired / Seller	B/S	Qty Traded	Price
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No Data Available

**in last one year*

Insider Trades

Reporting Data	Acquired / Seller	B/S	Qty Traded
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No Data Available

**in last one year*

Company	Absolute reco	Relative reco	Relative risk	Company	Absolute reco	Relative reco	Relative Risk
Apollo Hospitals Enterprise	BUY	SO	L	Dr. Lal Pathlabs Ltd	BUY	SO	L
FORTIS HEALTHCARE LTD	BUY	SP	L	HealthCare Global Enterprises Limited	BUY	SP	M
Max India Limited	BUY	SP	M	Thyrocare Technologies Ltd	HOLD	SU	H

ABSOLUTE RATING

Ratings	Expected absolute returns over 12 months
Buy	More than 15%
Hold	Between 15% and - 5%
Reduce	Less than -5%

RELATIVE RETURNS RATING

Ratings	Criteria
Sector Outperformer (SO)	Stock return > 1.25 x Sector return
Sector Performer (SP)	Stock return > 0.75 x Sector return
	Stock return < 1.25 x Sector return
Sector Underperformer (SU)	Stock return < 0.75 x Sector return

Sector return is market cap weighted average return for the coverage universe within the sector

RELATIVE RISK RATING

Ratings	Criteria
Low (L)	Bottom 1/3rd percentile in the sector
Medium (M)	Middle 1/3rd percentile in the sector
High (H)	Top 1/3rd percentile in the sector

Risk ratings are based on Edelweiss risk model

SECTOR RATING

Ratings	Criteria
Overweight (OW)	Sector return > 1.25 x Nifty return
Equalweight (EW)	Sector return > 0.75 x Nifty return
	Sector return < 1.25 x Nifty return
Underweight (UW)	Sector return < 0.75 x Nifty return

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Coverage group(s) of stocks by primary analyst(s): Healthcare

Apollo Hospitals Enterprise, Dr. Lal Pathlabs Ltd, FORTIS HEALTHCARE LTD, HealthCare Global Enterprises Limited, Max India Limited, Thyrocare Technologies Ltd

Recent Research

Date	Company	Title	Price (INR)	Recos
14-Aug-19	Thyrocare Technologies	Revival in growth; <i>Result Update</i>	444	Hold
13-Aug-19	Dr Lal Pathlabs	Good show on all fronts; <i>Result Update</i>	1,075	Buy
09-Aug-19	Natco Pharma	Muted performance; outlook intact; <i>Result Update</i>	552	Buy

Distribution of Ratings / Market Cap

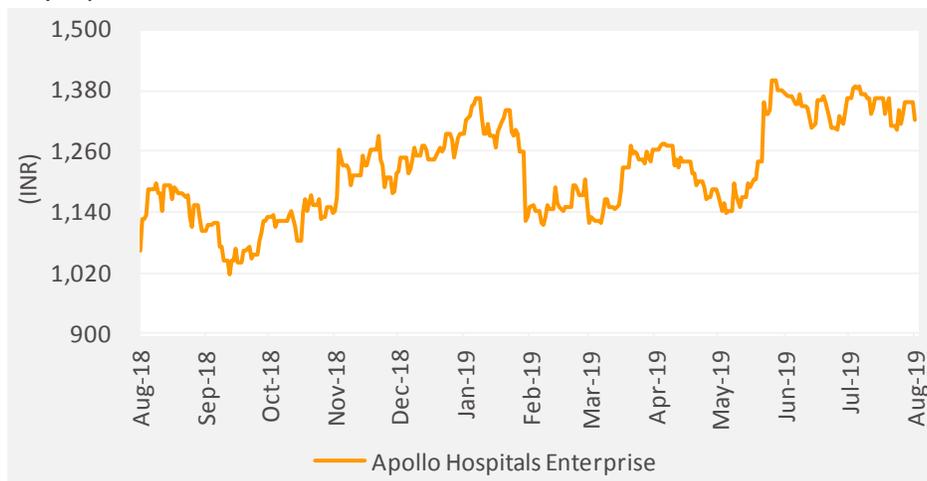
Edelweiss Research Coverage Universe

	Buy	Hold	Reduce	Total
Rating Distribution*	161	67	11	240
* 1stocks under review				
	> 50bn	Between 10bn and 50 bn	< 10bn	
Market Cap (INR)	156	62	11	

Rating Interpretation

Rating	Expected to
Buy	appreciate more than 15% over a 12-month period
Hold	appreciate up to 15% over a 12-month period
Reduce	depreciate more than 5% over a 12-month period

One year price chart



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