Apollo Hospitals

Transcript of Q2FY17 Earnings Conference Call
November 12, 2016

Moderator Good Day, Ladies and Gentlemen and Welcome to Q2 FY17 Earnings Conference Call of Apollo Hospitals. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing '*' then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mayank Vaswani from CDR. Thank you and over to you sir.

Mayank Vaswani: Good Afternoon and thank you for joining us on this call to discuss the Financial Results of Apollo Hospitals for Q2 FY17 which were announced yesterday. We have with us the senior management team comprising, Mrs. Suneeta Reddy -- Managing Director, Mr. S.K. Venkataraman – Chief Strategy Officer & Mr. A. Krishnan – CFO.

Before we begin, I would like to mention that some of the statements made in today's discussion maybe forward-looking in nature and may involve risks and uncertainties. For a complete listing of such risks and uncertainties, please refer to our 'Investor Presentation'. Mrs Suneeta Reddy will discuss the performance for the quarter along with the Operating Metrics, Expansion Plans and Other Highlights, following which we will open the floor for Q&A. Documents relating to our financial performance, have been shared with all of you and have also been posted on the corporate website. I would now like to hand over to Ms. Suneeta Reddy to provide Highlights of our Performance. Over to you, ma'am.

Suneeta Reddy: Good afternoon everyone and thank you for taking out time to join our call on a Saturday. Before we begin, on behalf of Apollo Hospitals I would like to convey our greetings for the festive season and wish all of you a prosperous new year.

I am pleased to share with you that the positive momentum that has been building up in the business over the last few quarters is now really showing up in volumes. While, there have been some benefits from the seasonality that is generally witnessed in the second quarter, overall there have been encouraging trends across both existing and new hospitals, strong growth in focused specialties in the healthcare services business and continued improvement in profitability benchmarks in the Standalone pharmacy business.

Let me take you through some of the key developments.

We are launching our 480 bedded hospital in Mumbai on Monday, Nov 14. It is one of the most advanced Multi-Specialty Tertiary Care Hospitals in the region and effectively represents the final leg of our current expansion plan which has resulted in an increase in capacity by 30% with the addition of ~2,500 beds over the last 3 years. Our focus is to have a dominant market presence in all these locations over the next 2 years by delivering superior clinical outcomes and service standards.

We are confident that the Mumbai Hospital will also contribute to our strategic imperatives of growth in the 'Center Of Excellence' volumes, increasing footfalls of both domestic and international patients and deliver superior healthcare delivery and clinical outcomes.

We have also moved forward on these strategic imperatives by enhancing our focus on specialty forays and clinical differentiation through advanced medical treatment. The increased prevalence of advanced medical equipment at our centers across the country has been serving us well as we ramp up volumes of robotics, transplants and high acuity surgeries. We have taken the initiative to ramp up these offerings at clusters as well as hospitals located outside of the metro cities.

The focus on elevating our offerings in each specialty has seen us converting our cancer management infrastructure into an independent functional division; viz. Apollo Cancer Institutes which we believe can provide industry leading oncology treatment through cutting edge equipment, a team of high quality specialists and a strong track record of clinical outcomes.

We are also making steady progress towards increasing the digital footprint in the delivery of healthcare services. The next wave in healthcare is all about ensuring shorter stays at hospitals, deploying high-tech equipment to improve outcomes while enabling patients to recover faster. Through such initiatives we plan to exponentially increase the reach of our network.

Now let me take you through the achievements in this quarter.

Our hospital in Ahmedabad became the first multispecialty care hospital in Gujarat to receive JCI accreditation. The Ahmedabad hospital also won the Smartest Hospital Building 2016 award at the Network 18 and Honeywell Smart Building Awards 2016.

Apollo Hospitals has ventured into the medical rehabilitation space in a 50:50 joint venture with Italy-based post-acute care service provider Kos Group ApoKos. The JV commissioned its first 64-bedded medical rehabilitation facility in Hyderabad which is another first in the industry in India.

We continue to elevate the quality of care and high acuity cases. Starting from the first successful pediatric liver transplant in India in 1998, the Apollo Group has till date performed 2,514 liver transplants of which 209 have been in children, the highest for any healthcare group not only in India but in the entire Asia-Pacific Region. Apart from the sheer numbers we continue to drive path breaking initiatives in the transplant specialty in this country. Doctors at our Vishakhapatnam hospital performed the first ever liver transplant without a blood transfusion on a 54 year old patient while Doctors at Apollo Gleneagles, Kolkata conducted the first ever successful Cadaver Liver Transplant in East India.

Against this backdrop, I will now take you through the key highlights of our performance for the first half: On a standalone basis, our revenues grew by 14% in H1 on a year-on-year basis to Rs.3,100 crore, while our revenues in Q2 grew by

16%. Consolidated revenues for the half year grew by 16% to Rs.3,510 crore. Within Standalone Revenues, 'Healthcare Services' grew 9% in the first half enabled by growth in overall patient volumes in Q2 of 10% y-o-y. The Pharmacy business reported revenue growth of 22%.

Standalone EBITDA grew by 9% to Rs.410 crore led by strong 50% growth in EBITDA from the Pharmacy business and supported by 4% growth in EBITDA from Healthcare Services. EBITDAR growth however has been higher at 11% as some of our newer hospitals are on leased facilities.

Reported EBITDA margins were at 13.2% for H1 FY17 as compared to 13.9% in the same period last year primarily due to the combined effect of a change in accounting norms and continued shift in the revenue contribution mix. As shared with all of you during the Q1 results, the Ind-AS norms recommend slightly different treatment of certain items and the major impact has come from guarantee fees paid to doctors being treated as costs against the earlier practice of netting these off from revenues. Further, changes to norms for bad debts and unredeemed points in loyalty programs in pharmacies have impacted the EBITDA margin.

Secondly, the shift in the revenue mix has also impacted the margin performance as Standalone Pharmacies which has lower EBITDA margin represents 43% of total revenues as compared to a little over 40% last year. Additionally, new hospital revenues which now account for 15% in Healthcare Services revenues or Rs.270 crore in H1 have a lower EBITDA margin of 5.6% compared to mature facilities which are at 22.7% due to unabsorbed initial fixed cost. Standalone PAT de-grew by 7% due to higher depreciation and interest on account of new hospital CAPEX.

The other aspect that I would like to point out is that the margin should also be viewed in the context of the nearly 2,000 beds we have added in the last 3 years. With such a large volume of beds and the addition of daycare there is a rebalancing of cases resulting in occupancy levels in the mid-sixties. If we look across the landscape we are delivering margins at par with other healthcare providers who have substantially higher occupancy levels. As we ramp up occupancy levels we are confident of improving our EBITDA margins.

The growth in Healthcare Services has been led by strong momentum at several facilities. While mature centers witnessed a rebound in volumes on the back of augmented medical teams and strengthening of specialty mix resulting in a pickup in inpatient admissions, the new hospitals have clearly stood out with 57% growth in revenues driven by strong growth in volumes. Growth in overall volumes was robust at 10% on a y-on-y basis and this was largely driven by a very strong performance in the second quarter.

Slide 9 of our presentation shows EBITDAR growth and the EBITDA turnaround in the new hospitals. Within our new hospitals, Vanagaram and Jayanagar continue to report a strong performance as they have seen very good patient footfalls and have a positive EBITDA of Rs 17 crs. New hospitals at OMR - Chennai, Trichy, Woman & Child Karapakkam and Woman & Child - SMR have too seen good momentum build up and have achieved EBITDA break even in Q2FY17. Malleswaram and Vizag which was added in Q4 have shown very rapid progress and should breakeven by Q4. Nashik & Nellore are progressing a bit slower than expected, though we are confident of doing well in these locations too over the next 2-3 quarters and now have a clear plan focused on local market needs.

Mature hospitals saw a good rebound in overall patient volumes as compared to Q1 aided by strong inpatient admissions in Chennai in particular. Revenues in the Chennai Cluster grew by 5% aided by 8% growth in Q2. ARPOB grew 9%. This was despite a reduction in outpatient volumes on a y-o-y basis. Inpatient volumes grew 3.3% and the richer case mix meant that IP revenue grew 7% which is more than twice the growth in volumes. Occupancy at Chennai was at 60% given new hospitals beds added in recent quarters. Volume growth bounced back in the second quarter as Q1 volumes were partly impacted by the state elections. Having said that, we believe a large part of the volume increase is sustainable due to efforts to reinforce the specialty mix and strengthen the doctor teams in the entire cluster. The resulting impact has showed up in the main hospital as well as in new hospitals within the cluster.

Hyderabad has continued with the momentum that you have seen in recent quarters and the strategy implemented over the last 6-8 quarters is reflected in good results. Many of you would have noticed a reduction in beds in Hyderabad and this is due to an overhaul of the infrastructure at the Jubilee Hills facility as we enhanced the specialty mix. If you look at the operating metrics, the shift in case mix and quality of medical programs is apparent. While both IP and OP volumes have improved there has been strong double digit growth in both OP and IP revenues supported by a decline in ALOS. This has enabled 17% growth in the ARPOB.

The Karnataka region which includes hospitals in Bangalore & Mysore has also performed well and witnessed good growth this year in the local client base. The Karnataka region revenues grew by 21%.

We have witnessed double digit volume growth outside our clusters. The high growth in outpatients is fueling the pipeline for IP volumes for the next few quarters. We are very pleased with the reduction in ALOS and continued growth in ARPOB. Having added beds at multiple locations, we now have enough headroom for growth and as occupancy levels rise we will see improved profitability. So from a growth and profitability perspective we are poised for a strong run over the next 3 years.

Standalone pharmacies while continuing to grow at an overall 22% Y-o-Y reported EBITDA margins in excess of 4.0% in H1 - which is in line with our strategy for sustainable profitable growth that we have been pursuing for the past over 16 quarters now. I am happy to report that the Standalone pharmacy segment is at 13% ROCE in H1 and 17% based on annualised Q2. We are confident of sustaining this momentum going forward.

We have seen healthy gains in EBITDA margins across all batches of stores due to the increased proportion of sales from private labels which improved to 6.6% in Q2FY17. The batch wise margin indicators were favorable and the EBITDA margin of the pre-2008 batch of stores continues to inch upwards hitting a new high of 7.3% in Q2. For the quarter, net addition was 47 stores taking the total number of stores in our network to 2,430 stores on a pan India basis.

Apollo Munich reported a 24% increase in revenues in H1 and a PAT of Rs 25 Crores compared to a PAT of Rs 2 crores in H1FY16. That's it from me; we will open the floor for questions.

Moderator The first question is from the line of Neha Manpuria from JP Morgan. Please go ahead

Neha Manpuria On the existing hospital growth which seemed at 2%, given there was a benefit of seasonality in the quarter, if I strip out the seasonality, did we see an improvement quarter-on-quarter in our base business, just wanted to understand how our existing businesses are doing?

A. Krishnan Yes, the existing hospitals for the quarter did do well. Even if you look at it versus last quarter, we have done quite well, there was some rebound of volumes, because if you look at Q1, in Chennai in particular, there was this election and we did see some rebound because of that in Q2 as well. So this is a bit of seasonality in Q2. Q3, as you know, this is typically a seasonally low quarter for us because of Diwali and Navratri and even in Durga Puja in Kolkata etc. So that's something that you should remember, but broadly we are happy with the volumes that have come in Q2 and we think, we should be able to build on this momentum going forward.

Neha Manpuria For the new hospitals, as we now ramp up, commission our Bombay hospital how should we look at the incremental cost that would be required in the initial period for this ramp up both direct hospital cost and any overheads that would be required for the Bombay hospital, i.e., marketing promotion etc.?

A. Krishnan We would request you to wait for the quarter, the hospital is getting inaugurated day after tomorrow and we would request you to wait for the quarter for us to be able to provide you this guidance because we are ramping up on the cost, the doctors, there are going to be guarantee moneys, etc., but we will get back to you by the next call.

Neha Manpuria And my third question was on the standalone pharmacies, a very sharp rebound in margins, what changed on a quarter-on-quarter basis because it is 3.5% in the first quarter and the margin has increased to 4.9% in Q2, so on a run rate basis, what is the number we are looking at. I know we want to improve margins, to what our mature stores are doing, but the quarter-on-quarter jump seems quite large?

A. Krishnan I will ask Mr. Obul to answer, he heads the pharmacy finance as you know.

Obul Reddy: There are 2 – 3 indicatives we internally worked on, in the last 6 months we have been working on volumes based discounts for the product. Then working on the fixed cost so that they don't take the character of variable costs and then overall volume growth in sales, all together contributed to the expansion in the margins.

Neha Manpuria Is there anything specific to the quarter in this number or should we assume margins to improve from this 4.9%, going forward?

Obul Reddy We should work towards improving that and we will definitely sustain those levels in the near future and then work on improving them.

Neha Manpuria Last question if I may, the entire demonetization, do you see that impacting both the hospital business, I understand hospital would probably be short term but more on the pharmacy business, given you could see some issues in the trade channel?

A. Krishnan Short term, we are seeing some inconveniences such as patients not being able to mobilize the currencies in the denomination, etc., for care. But we have seen that people have shifted to credit cards, there is a general pay out of even banking channels. We are also accepting cheques selectively from people to facilitate payouts. We are taking KYC documents. There would be some short-term pains, but we don't think it is going to impact any of the businesses over the medium term in a meaningful manner.

SK. Venkataraman: And I think we should congratulate the whole move because it has certainly helped the business. And I think it will actually facilitate more trade. So I don't think we will get affected at all.

Suneeta Reddy In the pharmacy says there has been no impact at all.

Neha Manpuria We are not expecting anything also in the pharmacy side?

Suneeta Reddy No.

Moderator The next question is from the line of Girish Bakhru from HSBC. Please go ahead.

Girish Bakhru Just a broad level observation, if you look at the existing facilities, that margin has been slightly coming down since Q4, any particular reason why would that be?

A. Krishnan Structurally there is no margin compression in the existing. It is because of the "IndAS" requirement of the guaranteed money fees being restated, etc. That is the reason and pretty much you would be in the 22.5 – 23% range in the existing health care services, even as we move forward.

Girish Bakhru And on the Mumbai, I know you are not giving any guidance but broadly if you could comment on, where do you see occupancy in the first year and what kind of ARPOB levels you can reach?

A. Krishnan We have said our target in 6 months is to get to the 50-bed occupancy and 12 months getting to 100 and thereafter 150 by 18 months. That's what is our internal target that we have such that between the 12th to 18th month from launch, we get to breakeven EBITDA.

Girish Bakhru And in terms of the ARPOB, would there be an element where Mumbai can reach Chennai level?

Suneeta Reddy We think over a period of time, it is possible.

Girish Bakhru You said that you have opened all the specialties at one go, including say high end transplant and?

Suneeta Reddy No, it would be very difficult to open all the specialties. What we are starting off with is only 60 beds with the usual facilities which include cardiac care, orthopedic. The Oncology will be added later and the transplant next year. Not next financial year but in the last quarter.

Girish Bakhru Just broadly, if one has to look at, at any point in time, how much percentage of surgeries in the Apollo network would be discretionary, I am just asking in the sense that, is there an element that those surgeries can be shifted given the impact from the cash change?

A. Krishnan So it between 10 – 20%, could be discretionary because many of the minor surgeries, because of insurance and everything, we have seen a good uplift in the overall surgeries coming on general surgeries, from general surgeries, gynaec and others. Some of them are elective. We would think it would be between 10 – 20% range.

Girish Bakhru But you are not seeing any impact whatsoever at this point in time?

A. Krishnan As I said the short term because of… are you asking for demonetization?

Girish Bakhru Yes.

A. Krishnan We are seeing some impact may be, we don't think it should last because the government has reassured that the currency should be available in the next week. So week wouldn't really matter us much.

SK Venkataraman: Already government has made excellent arrangements, there are banking norms new currencies are introduced, I don't think it's a long term thing at all.

Suneeta Reddy And even if there is dull in one week, there will be a catch up in the following week.

Girish Bakhru I mean I am just asking from a quarterly impact yes, so just lastly on the Hyderabad side, this has been very consistently strong growth in ARPOB where do you think this will peak out essentially?

Suneeta Reddy Very difficult to say because for one thing Hyderabad has lots of competition but also if you look at the city limits of Hyderabad, they have grown exponentially. So there is let me say the capacity to pay and I think at the right time, they will keep increasing ARPOB. We are introducing something called smart pricing for critical surgeries etc., we are managing to increase prices and this will be reflected in the ARPOB.

Moderator Thank you. The next question is from the line of Anubhav Agarwal from Credit Suisse. Please go ahead.

Anubhav Aggarwal Can you explain me again, I didn't understand the pharmacy margins sequentially, can you be quantitative in your answer that 3.5% going to 4.9%, a level we have never achieved, ever, across the stores. In a certain bucket of mature stores we may have done it but this quarter when we look at the pharma companies, there was further impact of pricing on some of the drugs. In that part we have done this, is there a change in the way you account for point now between quarter 1 and quarter 2, the schemes the customers have, something has changed otherwise such a sharp kind of thing cannot happen?

A. Krishnan As Obul said the most important thing has been cost control which we have been working on the ground. There have been 2 levers of cost control that they worked on, one is been the administrative expenses and the operating expenses itself has actually been kept under control even as the same store growth has ramped up, they have kept that well within control. Secondly employee cost also has been looked at and they have looked at manpower counts across pharmacies and they have optimized on that. It is the impact of efficiencies which is visible and that's why we feel it's sustainable.

Obul Reddy Specific on the numbers the way in which you are looking at quarter-on-quarter between Q1 and Q2, there is about 12.5% revenue growth. So that has directly contributed to the EBITDA level after adjusting for the modest fixed cost increase.

Anubhav Aggarwal Just to understand when you say about cost control, is it like now number of people working in same stores earlier in quarter 1 and quarter 2, are number of people lesser.

Obul Reddy We worked on some ratios and we are continuously reducing that ratio. Earlier it was 6 per store, now it got down to 5.7 employees per stores on an average. These are some initiatives we have taken and keep the fixed cost under control while the volume growth contributes to the bottom line.

Anubhav Aggarwal Sequentially how is the number more 5.7 - 5.8, what was it in quarter 1 and quarter 2, has it changed sequentially, that is what I am asking? One is only the operating leverage paying out with higher revenue.

Obul Reddy On an average in the last 3 quarters, we brought down per employee ratio by about 0.3%, it is 30 basis point which has kept our employee cost under constant control.

SK Venkataraman: You can always call back Obul offline, so we can give you the complete breakdown. We will be happy to share that with you.

Anubhav Aggarwal I will surely do that. Now you think let's say for next 12 months on an average I am not talking about 1 - 2 quarters there, next 4 quarters, you think our margins will be between 4.5 to 5% on here on pharmacy?

Obul Reddy We are working towards that.

Suneeta Reddy Also per prescription I think they are realizing higher.

Obul Reddy We are working on various initiatives like on average bill value, per employee, per store. There are host of metrics we will be very happy to share it to offline so I can't make reconciliation of all those and put it to numbers but I can explain to you offline if you are interested. We can have a detailed call later.

Anubhav Aggarwal Some questions on the hospital side, one on Hyderabad, we saw a very sharp jump in volumes sequentially and they came at lower prices, can you help what happened in Hyderabad in this quarter? Of course there is a component of seasonality, but the utilization moved very-very sharply.

A. Krishnan There were medical cases, there were a lot of dengue and malaria etc. which was there in this quarter. This is the seasonal spike which we see in Hyderabad and medical cases are typically low acuity and hence low ARPOB which is what is visible in this quarter in Hyderabad.

Anubhav Aggarwal Can you also explain about Chennai, there volumes were largely, let's say there was marginal up moves in volumes, but ARPOB is up 3.6%, so is there a big change in case mix sequentially, or is it like some price increase helped us?

A. Krishnan Chennai was more surgical cases which came in this quarter, because of the elective surgeries as we said in Q1 was postponed etc. because of elections, people could not come, so we saw a good spike in surgical volumes which is why ARPOB of Chennai has been higher.

Anubhav Aggarwal Last clarity from me is, on the new hospitals sequentially outside Vanagaram And Jayanagar, the other hospitals have done quite well. You mentioned across the board it's been pretty good but any 1 – 2 hospitals you want to highlight which has done significantly better.

A. Krishnan We saw a good uptake of business in Malleswaram having started just in Q4 of last year. We are very confident we have almost have 40 beds occupied now in just 2 quarters, we are quite confident of getting that to break even by Q4. Even the new hospital in Vizag has done very well. In fact Vizag, the hospital again has got closer to breakeven almost and we are quite confident of getting that also to break even. So these 2 hospitals are panning out very well.

Moderator Thank you. The next question is from the line of Manoj Garg from Bank of America. Please go ahead.

Manoj Garg Just one question, most of the expansion is through, and last of our new hospital is coming from Monday, from a broad level perspective, just want to understand that how do we see now the margins in the hospital segment, may be over the next 2 – 3 years directionally?

Suneeta Reddy If you look at the mature hospitals they are at 22.7 and if you look at Apollo Hospitals on the whole, it is at 12 – 13%, but this is also because of pharmacy bringing down the EBITDA margin but over a period of time, I think as we fill up beds and cover our fixed costs, definitely you will see a significant improvement in EBITDA margins. Bombay is probably the last frontier for us to conquer and once we have done that, it reaches a breakeven level, I think for the next 5 – 10 years, I don't think you will see any other healthcare company with such a strong potential, to see a 20% growth in topline, especially in healthcare space.

Manoj Garg If I can ask, in the sense over the next 2 – 3 years, where do you see the margins for the hospital segment likely to settle down?

A. Krishnan For the mature hospitals, as you see the occupancy today is around 62% or around that number 64. We have visibility and we would like to take it to 70 – 75%, as that moves up the overall EBITDA margins, for the mature hospitals can also move up by at least 200 bps over the period of time and the overall new hospitals as well can move to the number of 20 – 24% over a period of time. So clearly if you look at 2 years - 3 years hence, 24% is something you can look at.

Suneeta Reddy You have to understand the strategy a bit, here the difference was 5 years ago, we too were at 80% and we were showing EBITDA margins of close to 27 – 28%. But there was no headroom for growth. Now we have created headroom for growth. We did not want to follow the strategy of one hospital in each city because we know once it reaches 80% occupancy, its time to create more capacity and the cities are large enough, Indian cities especially the Tier-1 have grown exponentially and there was room to do the cluster strategy and I am sure that over the next 3 years, you will see the pay offs that come from the cluster strategy plus our investment in Tier-2.

Manoj Garg Carving out Apollo Cancer hospital as separate entity, just I would like to understand your thoughts behind that, are we seeing more expansion in that particular segment, any possibility of bringing out some investors out there in the cancer entity?

SK Venkataraman It is not actually a separate entity. What we will now and in yesterday's press release, we have clearly said that it will be a Cancer Infrastructure structure as a functional division, so there is not going to be any carve out. What we are going to do is refocus because we are going to also get the proton in the next year and year and a half. So it is one of the kind of cancer facility, that we are offering across the country. It is going to continue as a division, it is not an entity.

Manoj Garg Between hospital and pharmacy business mix, do you think the mix that we are running currently, you will see long growth coming in the new hospitals. I think this mix will sustain or you could see further, the mix is moving towards the pharmacy side?

Suneeta Reddy The new hospitals have grown by 50%, but again you can't add hospitals as fast as you can add pharmacies. So I am sure you can deduce the answer to that. It's easier to add pharmacies than hospitals and therefore we can show revenue growth and we can also show that their ROCE is currently at 13% but eventually over a period of time, mature hospitals ROCE will reach 17 – 18%. So, I think that's really what's important.

SK Venkataraman And the fundamental thing to understand is that they are totally 2 businesses, independent businesses, each having their own growth trajectory. So, it would be fairly impossible to predict, what will be the share of revenues, one could you know easily extrapolate given the rate of growth in both businesses. That will settle down around somewhere around what it is now? But truly speaking, both are independent businesses having their own trajectory. And we will take a call on expansion on each based on the merits of each business.

Moderator Thank you. The next question is from Dheeresh Pathak from Goldman Sachs. Please go ahead.

Dheeresh Pathak I am referring to slide 13 of the presentation, I would like to know the health care services group numbers? What is the capital deployed and in this refers close to 1200 beds that you added in the last 3 years?

A. Krishnan The capacity that we have added is 12 hospitals. If you look at the consolidated numbers, there are 2 hospitals which are part of the consolidated numbers, Indore and Guwahati, which we have acquired 51% stake as part of the consol. numbers. So what we added is actually from our perspective, 12 hospitals, what is getting reported in the standalone is 10 hospitals. That is around 1,945 beds and operational as you said is around 1,200 and around Rs 1,200 crore of capital employed.

Dheeresh Pathak In the 12 hospitals, that show up on slide 13 as new and others, that could have a capacity of 2,000 beds and capital deployed would be Rs. 1,200 crore?

A. Krishnan Yes, Rs. 1,200 crore, that's correct.

Dheeresh Pathak And their blended occupancy right now is how much?

A. Krishnan Blended occupancy would be around 40%.

Dheeresh Pathak On AHLL in the same slide second last column, what is the capital deployed in AHLL?

A. Krishnan AHLL capital deployed is around Rs. 550 crores.

Dheeresh Pathak Like a 200, 250 crore revenue level, what is the cost structure different that we are not able to break even EBITDA level at more than 200 crore?

A. Krishnan For AHLL, what we propose to do is, to have a separate call in the next 1 month, so I have to take you through the dynamics of AHLL, the potential of AHLL etc. What you have to appreciate here is it's a day surgery model, it has operating theatres of almost 3 and 4 operating theatres per day surgery center, the cradle and if you look at the utilization levels of most of these, they are probably more around 30%. There is a very high potential for growth over the next 4 – 5 years in AHLL. As the market matures as well as AHLL starts, getting the right mix of specialties and doctors, there is a high potential to take this significantly higher in the next 5 years which is why as you rightly say the current capital employed is not reflecting the full potential of what AHLL can achieve. So, there is a fixed cost because there are lease, many of these centers are on lease currently which is why there is a lot of fixed cost in these centers. As the top line grows, you will see most of that falling down into the EBITDA and the team has EBITDA break even target. In FY19 which is 12 – 18 months from now they will break even. That is the target that they have.

Dheeresh Pathak	At a portfolio level you are saying, the occupancy of these assets is less than 30%?
A. Krishnan	That is correct, utilization is more important that occupancy because there are lot of operating theatres and it is more of a day surgery. So, we look at utilization there than occupancy.
Dheeresh Pathak	And on an average what is the maturity of these assets like how many years old are they?
A. Krishnan	Most of them are new, if you look at the acquisition that we did of Nova was little over 18 months now and we have just integrated most of them in 6 months, its only around 6 months that we integrated them. So pretty much the Nova acquisition which is a day surgery is fairly new and then we have cradle and cradle we have added half of the cradle that we have out of 10, are less than 1 year old. So, you will have to wait for a year, year and a half, before we start seeing good traction there which is why the call that we proposed to have once things go well, we should be having the private equity investment into AHLL in less than a month or month and a half. At which time, you could ask for a separate call wherein you can have a proper understanding of the business.
Suneeta Reddy	We would also have a different management team and they will also be there to answer your questions.
Dheeresh Pathak	And also just one last question on the existing health care services, first column for the first half, the EBITDA growth is flat, that is mainly because of Chennai elections in the first quarter and all those things right?
A. Krishnan	Yes.
Dheeresh Pathak	On a steady state basis for the full year, for existing mature assets, what sort of topline growth and EBITDA growth do you have in mind, is it mid single digit, high single digit?
A. Krishnan	We don't want to guide around that currently we don't provide any forward looking guidance. We would like to continue to grow well. We have grown well in Q2 and we are pushing the units to report good numbers even going forward.
Moderator	Thank you. The next question is a follow up from the line of Neha Manpuria from JP Morgan. Please go ahead.
Neha Manpuria	Since you mentioned you are going to have separate call for AHLL, just one thing, from an Apollo management perspective, I understand that you have a PE investor coming in, what is the amount that we are looking to invest in AHLL, over the next 5 years for it to get critical mass, is there a limit that we have set that this is the amount we are okay investing in the business?
A. Krishnan	Currently if we look at it, we would be looking at private equity coming between Rs 400 - 450 crore, that's the number that should be invested by the private equity. Once that's done, we would be 70% holding from our side and 30% from their side, that's where we are trending towards and post that we don't see over the next couple of years, we don't envisage much investments from our side and we would take the call after getting to sustainable numbers here.
Neha Manpuria	It's fair to assume that this is what our investment will be limited to, in AHLL?
Neha Manpuria	As of now yes.

Moderator Thank you. The next question is a follow up from the line of Anubhav Agarwal from Credit Suisse. Please go ahead.

Anubhav Aggarwal Just one more question on AHLL, just a clarity on the business model, the breakeven for Cradle business or dental clinics, how is it different from starting a new hospital? This will be like faster breakeven, I am just trying to understand that we are trying to get private equity in business, is that because we are into multiple clinics such as sugar clinics, dental clinics, diagnostic centers versus hospitals, because this will be faster break even right?

A. Krishnan It's a good question. We would defer this question to the call that we are planning and you can also take this offline. The breakeven can be faster but because of the asset light model and because of the fixed cost and leasing cost in particular, it gets extended a bit but it is better you take it offline, we will help you with this question and before the all you can send across your questions to Krishnakumar, so that the management is well prepared for your call.

Anubhav Aggarwal Some more questions, not on AHLL, but on hospital business, just one question on are the expansion that we have done in last let's say 4 years, majority of our expansions with the exception of Guwahati but majority of expansion have been either in couple of assets in Mumbai that we are working on, or in Indore or mostly in South. What about North region and the east region because now the expansion plan that you laid out in FY19 you are working on one more hospital in Mumbai and the proton what about this 2 region, North and East, are you thinking about inorganic there or no expansion for next 3 years?

Suneeta Reddy East we are looking at inorganic acquisition, but when it happens, it will be good to talk about it. Right now all we are doing is to see how we can strengthen our presence. You are right we do want to strengthen our presence in East, while as the north is concerned, we have already acquired land in Amritsar. And Punjab is one state that we would like to be present in, we do have a presence in Delhi and I think Delhi is- let me say that there are a lot of big providers in Delhi, so we don't want to be a marginal provider in a big city.

Anubhav Aggarwal What does the comment mean, do you want to expand in Delhi or not?

Suneeta Reddy No, I think there is enough, I think the beds right now in Delhi is quite sufficient. They have already reached an average of 3.3 beds per 1,000. So, I think it's an indication to us that unless we make an acquisition which is probably the best thing to do, rather than create new facilities and inorganic growth in Delhi which would be quite challenging, and the price of entry into Delhi has become very high. So leaving Delhi, we are looking at something in Punjab. We are looking at an acquisition in East. In Bombay, we are going to be 2 hospitals. So, I think we will also be strong in the West with Nasik, with our day care presence in Pune, plus 2 hospitals in Bombay and a day care center in Bombay.

Anubhav Aggarwal So, effectively when we look at our expansion plans, largely organic layout, we could see from 17 – let's say FY20, some acquisitions in North and East if that's possible.

Suneeta Reddy If a good opportunity comes, certainly.

Anubhav Aggarwal Sir can you help me with CAPEX FY17 what do you expect, not much of expansion FY18, what will be our CAPEX number?

A. Krishnan If you look at the balance CAPEX that we have for our new hospitals is approximately around Rs 750 crore, over the next 3 years and that's what is the number that we would have. So roughly about 400 a year for the next two years third year will be a bit lesser.

Anubhav Agarwal So, including maintenance CAPEX can you roughly?

A. Krishnan Maintenance CAPEX every year is around Rs 120 crore, you can take that separately.

Anubhav Aggarwal Effectively, for 18, you are guiding to a 400-crore kind of CAPEX annually?

A. Krishnan That should be fine.

Anubhav Aggarwal And for 17, what would that number be, 600 - 700 crore,?

A. Krishnan That should be fine.

Anubhav Aggarwal Couple of more clarities, about Hetero pharmacies, when do we expect this acquisition to become EPS accretive?

Obul Reddy This quarter we did well with about 1.2% to positive EBITDA previous quarter, 3% negative EBITDA. We should grow that further to our network EBITDA levels in the next 6 to 8 quarters.

Anubhav Aggarwal And, that may be at 5% that will be just about, it still will not be breakeven because our interest cost itself is 14 – 15 crore?

Obul Reddy We have to see the overall advantage network as far as competition, in terms of expense control, for the existing system, so we will reach that level, after that we will further grow on that.

Anubhav Aggarwal And just one last question from my side, on the hospital side we have commissioned almost 2,000 beds since FY13, most of the hospitals are about 40 – 50% utilization right now. When we consolidated on this hospital for next 2 years, 3 years may be, not expanding much, what are you doing now differently, whats your last 2 years where we already reached a break even and doing well in most of the hospitals to increase the utilization, let's say the environment picking up overall macro environment picking up. Second is, from your own side what efforts you are doing to increase utilization in each of the places?

Suneeta Reddy I think the first thing we did is to recruit doctors in each of these specialties and the way we worked is, we have full time doctors who are there, let me say based on 12 hour basis who initially worked on guarantee money which is why our margins were low in the first few years, later they moved to Fee for service. Doctor engagement policy is very important. Second is we look at asset utilization, and to do so we are in terms of pricing, we have different prices for new hospitals, which are at a discount to existing hospitals because the intention is to fill the beds, use the operating theatres, so that we can cover the fixed costs as quickly as possible and which is why hospitals like Vizag and Malleswaram became EBITDA positive in the first year itself. The third things we are now doing is to use digital very effectively to handle both our marketing and to see that our reach into patients is extended. Patients can communicate and book appointments with us extremely fast. In fact, Apollo main has 2000 E-doc bookings. So that's really risen from what it was earlier. We are also looking at referrals from that local market area, where we see a drainage area and we focus on that drainage area, by looking at the local doctors there, referrals, we work with local doctors to see that these referrals happen and of course Apollo has built a name a brand in high acuity cases, so I think, we will continue to do that. People with more tertiary work, are definitely coming to us but we have looked at creating even in the higher secondary space, we have engaged with Doctors, we have engaged with Surgeons, so that we take all the cases and enable us in the strategy to use all the beds to fill all the beds as quickly as possible and cover our fixed cost.

Anubhav Aggarwal Do you think pricing is one of the factor that you have lower utilization today in your market feedback survey, Apollo pricing versus existing competition in the market, that is not the reason why we have lower utilization?

A. Krishnan We don't think pricing is the reason because we have priced it appropriately for those markets, and over a period of time, we think pricing can actually help.

Moderator Thank you. Ladies and gentlemen, that was the last question. I now hand the conference over to the management for closing comments.

Suneeta Reddy Ladies and gentlemen, thank you for joining this conference call. As part of the strategy, to grow our network, we are opening our hospital in Bombay, a 480 bed hospital in Mumbai on Monday, November 14th. We would like you all to attend. Krishnakumar would have reached out to all of you with invitation. So please we would be very happy to receive you at the opening of our hospital and at the ceremony that follows. Thank you ladies and gentlemen once again for joining this call.

Moderator Thank you. On behalf of Apollo Hospitals, that concludes this conference. Thank you for joining us and you may now disconnect your lines.