



## **Apollo Hospitals Enterprise Ltd.**

### **Q4 and FY12 Earnings Conference Call**

### **May 31, 2012**

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**Moderator** Ladies and gentlemen good day and welcome to the FY12 Earnings conference call of Apollo Hospitals. As a reminder all participants' lines will be in the listen only mode. There will be an opportunity for you to ask questions at the end of today's presentation. If you should need assistance during this conference call please signal an operator by pressing "\*" and then "0" on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Mayank Vaswani from CDR India.

**Mayank Vaswani** Good afternoon everyone and thank you for joining us on this call to discuss Apollo Hospitals financial results for the year ended March 31<sup>st</sup> 2012. We have with us today the senior management team. Before we begin, I would like to mention that some of the statements made in today's discussions may be forward-looking in nature and may involve risks and uncertainties. For a more complete listing of such risks and uncertainties please refer to our investor presentation. We will start with Mrs. Suneeta Reddy who will discuss the operating highlights for quarter, Mr. Krishnan Akhileswaran will then discuss the financial highlights and progress of expansion plans and Mr. Padmanabhan will discuss highlights of the pharmacy operations, Apollo Munich Health Insurance and Apollo Health Street. Documents relating to our financial performance have been e-mailed to all of you earlier and have also been posted on our corporate website. I would now invite Mrs. Suneeta Reddy to provide key highlights of our performance.

**Suneeta Reddy** Good afternoon ladies and gentlemen and thank you for joining our call. Today I have with me Mr. Padmanabhan, our President, Mr. Premkumar, our new CEO, Mr. Krishnan, our CFO and Kartik Reddy. FY12 marks the completion of another landmark year for Apollo hospitals. It has been a year where we have forged ahead in the areas of technology adoption, clinical excellence and patient care excellence while continuing to demonstrate strong momentum and sustained leadership in both revenue growth and profitability. I'm happy to state that for the first time we have crossed the ₹ 30 billion milestone posting consolidated annual revenues of ₹ 3,148 crore.

Before we get into the financial highlights, I would like to discuss some clinical and operational achievements. The Apollo Transplant Institute has completed 929 transplants in a single year which makes it the busiest program of its kind in the world and makes us first medical institution to undertake as many transplants in a single year. It also sets a new annual benchmark for us as we planned to expand the program to include our hospitals in Bhubaneswar and Ludhiana.

The Apollo Institute of Robotic Surgery was launched six months ago and has already completed 55 robotic surgeries. In the short time of its existence it has helped to improve the quality of our healthcare delivery and elevate our clinical standards. Robotic surgery helps us to treat patients with minimally invasive surgery and has led to improvements in efficiency, precision, safety, lower blood loss, lesser tissue trauma and reduced pain and scars which are some of the aspects that distinguish the robotic surgery experience.

For us it means superior clinical outcomes, optimal pricing, translating to higher average revenue per per bed day and faster turnaround time, resulting in lower average length of stay. We further plan to scale up our offerings in the field of robotic surgery. We are currently offering robotic surgery in the areas of gynaecology, urology & oncology, general and bariatric surgery and plan to widen the scope to include cardiac surgeries and as well surgery on the head and neck. We also plan to roll out robotic capabilities at more facilities to help us touch and heal more lives.

I would also like to share with you some achievements on the clinical excellence front. In addition to our award-winning ACE@25, we have introduced the RACE program which was focused on the Centres of Excellence (COE) initiative and outlines 25 parameters which are incremental to those contained in ACE@25. It will help us monitor clinical standards with greater precision and ensure that we identify areas to increase the quality of clinical outcomes. The high standards of excellence have led to a re-accreditation by JCI's of our hospitals in Bangalore, Chennai, Delhi and Dhaka. We continue to have 7 JCI hospitals in our network. Our hospitals in Ahmedabad, Noida and Secunderabad were accredited by NABH during the year. Madurai was re-accredited by NABH and received the prestigious ISO 9001:2008 surveillance. We now have 5 NABH accredited hospitals and several other facilities are in the process of evaluation for accreditation.

We are also setting up many transformational initiatives to enable us to realize balanced growth across specialties, geographies and formats.

Getting on to the financial performance, we are pleased to report continued growth in both revenues and margins. Our consolidated revenues grew by 20.8% from ₹ 2,605 crore in FY11 to ₹ 3,148 crore in FY12. Consolidated EBITDA has increased by 22.5% from ₹ 419 crore to ₹ 513 crore in FY12. Profit after tax grew by 19.3% to ₹ 219 crore. The standalone pharmacy business has continued on its growth trajectory with over 30% year-on-year growth with increase in operating margins enabled by calibrated expansion with a focus on profitability. Revenue growth in standalone health care services was healthy. New capacity addition in the last fiscal in Hyderabad, Secunderabad and Bhubaneswar displayed good growth from increased patient flows and occupancy. Our subsidiary and joint ventures hospitals in Ahmedabad, Bangalore and Calcutta have reported an enhanced performance.

Lastly, our health insurance and BPO business has reported substantial improvement in contribution this year. In view of the sustained financial performance the Board of Directors has recommended a dividend of Rs. 4 per share. During this quarter we have entered into an agreement to buy 100% of the existing Bangalore facilities where we earlier had 51%. The Board has further approved 2 more hospitals in our earlier expansion plan. A 180 bed facility in Bangalore, Jayanagar and a 45 bed Heart Centre in Chennai. The two facilities that we are planning to add in Bangalore will complement our service offerings in that location and further enhance our geographical reach and patient connect in the city. As we have been stating as part of our overall strategy of having a dominant share in key markets.

Slide 16 has our expansion and CAPEX plans. The expansion plans are on course, including the two new hospitals that were approved this quarter. We will add 2,955 beds across 14 hospitals, thereby increasing the number of owned hospitals in our network to 51, from the present 37 and owned beds from 5,888 beds to over 8,800 beds in FY15. The total funds required for the project is in the range of ₹ 1,939 crore of which Apollo's share is approximately ₹ 1,748 crore. Of this, we have already invested ₹ 262 crore and have a cash balance of ₹ 250 crore. The balance requirement of ₹ 1,200 crore will be funded through a mix of internal accruals and debt. Our current leveraged levels and debt servicing abilities position us well our continued expansion plans.

Before I conclude I would like to share that FICCI has conferred Apollo hospitals the award for the "the Best Private Hospital in the country". They also presented our Chairman Dr. Prathap C Reddy with the "lifetime achievement award". With this, let me hand over to Krishnan, our CFO, to provide you with further details of our financial performance.

#### **A. Krishnan**

Good afternoon to all. I will quickly run through some of the highlights of the financial performance. I would like to start with the standalone numbers which are on Slide #9 of the presentation that has been circulated.

Revenue growth remains strong with over 20% year-on-year growth for FY12. EBITDA was up 23% from ₹ 377 crore in FY11 to ₹ 464 crore in the current year. The EBITDA margins have increased by 40 basis points to 16.6%, primarily on the back of richer case mix due to our COE initiative, increase in inpatient and outpatient volumes in our new hospitals added in Hyderabad, Secunderabad and Bhubaneswar as well as an increase in profitability from standalone pharmacies.

Depreciation and interest expense have increased due to the addition of operating beds at Hyderabad, Bhubaneswar and Karaikudi, among others. There was an improvement in other income in FY12 to ₹ 28 crore from ₹ 18 crore in FY11, aided by an increase in the cash and cash equivalents given the effects of our QIP in July 2011 and the conversion of warrants by the promoters. Standalone PAT for FY12 was higher by 27% at ₹ 231 crore.

If you now turn to Slide #10 on segment wise performance, you will see that the healthcare services segment grew by 15.1% over FY11. The revenue growth was driven by volume growth, improved pricing and richer case mix due to focus on centers of excellence like cardiology, oncology, neurosciences, orthopedics, emergency medicine and transplants. The EBITDA margin in our healthcare services segment in FY12 increased to 23.1% as compared to 22.4% in the previous year, while EBIT margins expanded from 18.6% to 18.8% in FY12, even after accounting for depreciation.

Standalone pharmacy revenues grew over 30% in FY12; The EBITDA margin in our standalone pharmacies in FY12 was 1.9%. FY12 EBIT from standalone pharmacies has improved from a negative EBIT from ₹ 4.3 crore in FY11 to a positive EBIT of ₹ 7.8 crore in FY12. The ROCE on healthcare services has dropped to 17.8% in FY12. This is because the facilities added in recent quarters are still in the ramp up stage and will deliver better returns as they mature. Similarly standalone pharmacies have witnessed improvement in ROCE in FY12.

I will now quickly take you through slide 12, which contains the key operating metrics in the hospitals business. The operating beds as of March 31<sup>st</sup>, 2012, were at 5,153. There was a net addition of 386 beds in FY12 at Hyderabad, Vizag and Bhubaneswar. We also added beds at our JV and subsidiary hospitals at Calcutta, Delhi and Bangalore. Occupancy has been largely stable at 71% in FY12, compared to 73% in FY11 despite bed additions in Hyderabad and other hospitals.

If you look at the Chennai cluster, Chennai has seen improved occupancy from 73% in FY11 to 75% in FY12 giving a marginal decrease in bed capacity due to facility modification to accommodate some high end programs like liver transplants and robotic surgery and we also had an overall facility up-gradation here. While there has been a healthy growth in outpatient volume, the inpatient volumes have remained flattish. While Q1 was impacted by state elections, we also have witnessed lower volumes midyear from PSU insurance companies pending their re-panels procedures which are now complete.

Volume growth has been strong at Hyderabad and 'other' hospitals led by Bhubaneswar. This has led to a robust increase in both IP and OP volumes at these facilities. This has resulted in a healthy 26% growth in revenues in Hyderabad cluster and 23% in the 'others' cluster. The average revenue per occupied bed in both these clusters have also grown by 14.5% and 15.1%, respectively due to the improvement in case mix and reduction in an overall ALOS. Among subsidiaries and JV's, Ahmedabad and Calcutta registered strong growth in both IP and OP volumes which translates to increased revenues. That is it from me. I will request Mr. Padmanabhan to talk about standalone pharmacies, Health Insurance and Apollo Health Street.

#### **K. Padmanabhan**

I will quickly walk you through the performance of the other businesses in our portfolio. Revenues in the standalone pharmacy segment have expanded over 30% from ₹ 661 crore in FY11 to ₹ 861 crore in FY12. Revenue growth continues to be driven by higher sales per store as well as an expansion of our network pharmacies. It is pertinent to note here that our own private label sales which constitute less than 1% of our total pharmacy turnover till a few quarters back have now risen to almost 4% of the total pharmacy turnover. These private labels as you are aware contribute significantly higher margins and profitability compared to the branded FMCG's and medicines.

If you examine Slide 14 which covers the operational performance of our standalone pharmacies, the stores have been categorized into three categories. Stores that were setup prior to FY2007, stores that were setup before FY2008 and others. The EBITDA performance continues to get better with the ageing of stores. Total EBITDA has improved from ₹ 3 crore in FY11 to ₹ 16 crore in FY12. While the overall EBITDA margins have improved from 0.5% in FY11 to 1.9% in FY12. The mature stores EBITDA margins have now risen to 5.7%. We are well ahead of our earlier target of 5% and this augurs well for the future EBITDA growth of the business. In Q4 we added 81 stores on a gross basis and closed 7 stores resulting in a net addition of 74 stores. As on March 31<sup>st</sup>, 2012 we have a network of 1,364 stores.

Apollo Munich Health Insurance our joint venture with Munich has recorded a gross written premium of ₹ 476 crore in FY12 which represents a growth of 68%, over the same period last year. Total income has more than doubled from ₹ 165 crore in FY11 to ₹ 331 crore in FY12. Losses at an EBITDA level declined to ₹38 crore from about ₹ 70 crore in FY11. The incurred claim ratio improved to 58% in FY12 compared to 52% in the previous year. This was largely driven by improved pricing and increased prudence in underwriting. We have now a network of 50 offices across the country and have assets under management of ₹ 419 crore as on 31<sup>st</sup> of March 2012. Munich Health Insurance was one of the fastest growing health insurance companies in the country this year.

Apollo Health Street reported an increase of 9.7% in the total income from ₹ 448 crore in FY11 to ₹ 491 crore in FY12. EBITDA expanded to 2% to ₹ 84 crore and the EBITDA margins expanded by 554 basis points from 11.6% to 17.2% in FY12. The improvement in operating efficiencies has been driven by a focused program undertaken during the year. However PAT was impacted by a one-time litigation

cost, as well as a higher interest cost. That is it from me, and now we're ready to take on your questions.

- Moderator** Ladies and gentlemen we will now begin with the question and answer session. The first question is from the line of Nitin Gosar from Religare AMC.
- Nitin Gosar** I just wanted to understand why is the inpatient volume for Chennai cluster not still growing?
- Suneeta Reddy** In fact, the inpatient volume of Chennai cluster has grown. If you look at Slide # 12.
- A. Krishnan** For the whole year when you look at the volume and it has been a 0.2% drop if you look at the outpatient volume, outpatient volumes have grown 16.1%, what Ms. Suneeta was saying, that it has begun picking up now and we have started seeing growth in the inpatient volumes in April of this year.
- Suneeta Reddy** We had to close 30 beds to include the transplant unit so that is one of the reasons why you are seeing less volume.
- Nitin Gosar** But if I was to just go back on the previous conference calls. We have been always quoting from this month's onwards we have been seeing some kind of an improvement in inpatient volume but they have never turned into the absolute figures, so I was just getting a little bit worried whether these numbers are really picking up or not?
- Suneeta Reddy** No, I think it is a combination of the fact that we were in dialogue with GIPSA and it is only in this quarter this that we have actually signed on with GIPSA so 2 to 3% is accounted by that and the fact is that we closed down around close to 30 beds.
- K. Padmanabhan** I think, as far as Chennai Main is concerned, the headroom for growth for inpatients in future is actually going to come from any significant reduction in ALOS., I think we need to be clear on that. We have about 600 beds we are operating pretty much closer about 75 to 80% occupancy. So I think a lot of headroom for growth in inpatient volume is going to come from a reduction in ALOS. Having said that we are now looking at how we can actually do that by increasing the number of daycare surgeries, etc. The point I said to that was coincidentally we had a reduction in number of beds because of our liver transplant program and also the fact that there was some delay in getting into an agreement with GIPSA.
- Suneeta Reddy** But just to conclude our outpatient volumes have increased, and we believe that we will be able to look at higher conversion so we are optimistic that inpatient volumes will grow next quarter.
- Nitin Gosar** According to you, the April numbers for inpatients are optimistic, they are positive YoY?
- K. Padmanabhan** Significantly better, yes.
- Moderator** The next question is from Perin Ali from Edelweiss.
- Perin Ali** Just one query which I had was that if you look at our standalone numbers the growth in earnings has been pretty robust around 26% and at an EBITDA level also the growth has been good, but if you look at our consolidated level, the quarter performance shows a 10% growth in our earnings. So having said that our subsidiaries and JV operations are also performing well, I'm just not just not able to

understand the disconnect between earnings growth of standalone and consolidated results, so if you could just help us out?

**A. Krishnan**

If you look at the consolidated numbers as you know consolidated finances are audited once in a year and we report the estimates every quarter for the analysts and these are the audited results which we publish. So to that extent the quarter is not something that is the exact representation because there are two one-off items, which has impacted the quarter. If you look at the EBITDA, the EBITDA growth is healthy, the operational EBITDA is healthy. On the PAT if you look at it, the Calcutta PAT was impacted a bit because there was this deferred tax liability which we had to reckon at the end of the year because Calcutta now is doing very well and the unabsorbed losses are also coming down - that is one of the reasons which is there and also there was a small increase in the depreciation also there. That's about it. Otherwise, if you look at it on an overall basis, directionally, the EBITDA margins for the full year, if you look at it the EBITDA margins are in line with the standalone.

**Perin Ali**

I agree, it is just that on the PAT's level I see only a 10% kind of growth so the one offs you said is higher tax or the deferred tax which was created. If you could just share of that number and if you adjust for that, what could be the growth in the consolidated level?

**A. Krishnan**

That is right because if you look at the overall year, the overall year is still showing a 19.3% increase in PAT's whereas the quarter is showing a 10.4% increase because the PAT was impacted by the tax provisions in Calcutta of almost around ₹ 15 crore in the quarter.

**Perin Ali**

And just to follow up if you could share with us how many bed additions you have done this year and how much of that has been operational or you have made operational this year if you could just share that number?

**A. Krishnan**

This year as I said the operational beds are there in the operational performance. If you look at the total operating beds at the end of FY11 these are at 4,767 and now we are at 5,153. So the additional operating beds are around 360 odd beds which we added in this year. But if you look at it, last year we had added Hyderabad, we had added Karaikudi in Q4 of last year as well so which was already reflected in the FY11 numbers. If you look at the last 18 months we would have added close to 800 beds across the system.

**Moderator**

The next question is Kashyap Pujara from Enam.

**Kashyap Pujara**

The presentation that you have sent across is pretty informative and covers most of the things but just wanted to run through some details on the operational performance. If one just looks at the page 12, the operational performance for FY12 and FY11 in terms of ARPOB it is close to 14,592 and 16,278. If I just see the last quarter, there is Q3 and if I see the YTD ARPOB it was close to 20,000 and even in the prior year it was close to YTD was 18,000 and even for that matter if one looks at the Q4 FY11, the ARPOB stood at 20,000. So if you can just explain where are the reclassification or regroupings done, which has resulted in to the ARPOB differences, especially more so from last quarter to full year?

**A. Krishnan**

No, I think, we will take a re-look at these numbers and we will get back to you with the corrected numbers because the total is not reflective of the correct numbers because we have not included the hospital based pharmacies here. If we include that the number would be a bit different so we will revert to you after re-looking at the total numbers.



**Kashyap Pujara**

Hospital based pharmacies are included, I'm sure the numbers would look substantially different?

**A. Krishnan**

That is correct because if you look at the Chennai cluster, Hyderabad and the others etc. each of those ARPOBs are the reflective ARPOBs.

**Kashyap Pujara**

Yes because that side I felt that there is a disconnect between Chennai, the way the clusters are reporting to what the total looks like.

**A. Krishnan**

That is right.

**Kashyap Pujara**

Second is, if you can just give us some light in terms of the expansion plan which we are planning to go to say, 8,500 beds and what is the status there? Are we on track, I mean, where are we seeing delays if you can just run us through? Is there any time overrun where we need to build in some of the capacities coming in at a later date if you can just run through a glimpse on that?

**K. Padmanabhan**

Yes, I think as far as overall implementation timelines are concerned we are broadly in line with our original plans plus or minus a quarter but in terms of overruns we will have certainly some overruns as a result of the change in the exchange rate. So we would expect that our capital cost, our overrun would be in excess of about 100 crore come back to what we have stated earlier from about ₹ 1,600 crore to about ₹ 1,700 crore.

**Kashyap Pujara**

Okay that is in terms of spend. I mean, if I am looking in terms of timelines like say for example in the Bombay we have three clusters where the expansion is coming through. So what is the status there, where has the construction begun, basically where are we on track and where are we seeing delays likewise if you can just give a glimpse as to in terms of timelines would we be maintaining? How confident are we to operationalize these beds by the timelines that we have laid out?

**K. Padmanabhan**

I think, originally we have talked about Navi Mumbai being in the last quarter of 2014. I think we may actually move over to the 1<sup>st</sup> Quarter or thereabouts of 2015. Otherwise I think it will be broadly in line with all our other expansions.

**Kashyap Pujara**

So by and large we can say that by the 2015 if I just drop a line, by FY15, we will definitely be exiting the year with more than 7,000 beds operational on the ground for sure.

**K. Padmanabhan**

That is right.

**Moderator**

The next question is from Bino Pathiparambil from IIFL.

**Bino Pathiparambil**

Just a couple of questions, in the Hyderabad cluster, given the level of occupancy and lot of new bed additions; I would have expected the occupancy levels to grow a little bit faster. Are we seeing some slowdown or is it in line with your expectations?

**Suneeta Reddy**

Yes, I think it is in line with our expectations. Hyderabad is on a new bed base, it registered an occupancy of 62% but looking at the competition profile in Hyderabad I think it will take a little bit more time for people to recognize the Apollo brand name, having said that they have added 20 new doctors in specialty so I believe that volumes will increase in the next year.

**Bino Pathiparambil**

Actually following up on an earlier question my derivation from the numbers you have given suggests that there was a drop in the EBITDA margins in associate /

joint venture hospitals. Were there any new addition of beds large scale there which led to that or I am getting something wrong in my calculation?

- A. Krishnan** No, there was nothing significant. Actually we started this, there was a management fee which was there in Calcutta which has begun this year which has to be shared between us and the other joint venture partner, that is something which gets accounted in the standalone financials and to that effect the Calcutta numbers in the consolidated numbers don't reflect the same increase, whereas operationally the increase in EBITDA has been over 20% there. So it is just an accounting entry, if you come off-line I can help you understand that better.
- Bino Pathiparambil** Sure, that is likely to continue the way it is now, right?
- A. Krishnan** Yes.
- Bino Pathiparambil** In the opening remarks you mentioned about buying out a few beds in Bangalore and Chennai, I just could not get it clearly, could you explain that once and is it over and above the expansion plans described in the presentation?
- Suneeta Reddy** What we are doing in Bangalore, we have bought out our partner in Bangalore. We had 51% of the hospital there, and we are now 100% owners of the hospital in Bangalore. In addition to that we are adding 180 beds in Jayanagar and we are also, on the other side of the town, in Malleswaram we are, adding 160 beds. So it is a combination of buying out our existing owner and adding new beds.
- Suneeta Reddy** Yes, in Chennai in OMR we are adding 40 beds for a Heart Centre.
- Bino Pathiparambil** This is all within the presentation, what is given in the presentation.
- K. Padmanabhan** Yes, these are all three of them are in the presentation
- Bino Pathiparambil** Okay, nothing over and above what is in the presentation?
- K. Padmanabhan** No
- Bino Pathiparambil** Okay and the Insurance joint venture seems to have been profitable at the EBITDA level in this 4<sup>th</sup> Quarter, was that true and what is the outlook going forward?
- A. Krishnan** It was breakeven in 4<sup>th</sup> Quarter, the outlook as Mr. Padmanabhan said for the next year is also good, it's grown very well this year and we would continue to see a momentum in that business going forward as well as it moves into profitability levels over the next 15 to 18 months.
- Bino Pathiparambil** So we are looking at positive EBITDA in FY13 from there?
- A. Krishnan** That's it but what we consolidated here is only because our share in that joint venture is only around 10% so what we look at here is happening around 10% of the revenues and EBITDA.
- Moderator** The next question is from Amit Hiremath from Enam AMC.
- Amit Hiremath** My question is regarding the COEs. What is the contribution of COEs to the overall sales and the EBITDA?
- A. Krishnan** Approximately 65% of our revenue comes from the COE focus and the EBITDA from the COEs are in line with the overall company EBITDA.



**Suneeta Reddy**

I will ask Mr. Premkumar to talk about the potential of this theme.

**S. Premkumar**

I think in the context of the COEs they are six of them and in the context of what they are contributing today is 65% and we believe that as an overall contribution the growth of this would come to almost about 80% as we go forward and we would also be looking at some of the newer specializations which will come in and look at new centers of excellence that we keep creating.

**Amit Hiremath**

That will invariably mean that the EBITDA margin should be improving every year?

**S. Premkumar**

Well as Krishnan suggested, I think, the EBITDA margins are in line with the rest of the business so there is no material skew which would impact margins either on the positive side or the negative side.

**Amit Hiremath**

Okay and regarding the clusters, if you could share the guidance for the inpatient volume for this particular year for all the clusters?

**A. Krishnan**

Are you saying guidance for the next year?

**Amit Hiremath**

Yes.

**A. Krishnan**

No, we don't guide on forward numbers.

**Amit Hiremath**

I just missed the contribution of the private label to the overall pharmacy sales?

**K. Padmanabhan**

Private-label contribution is 4% for standalone pharmacy revenue and our program is taking it significantly higher in the years to come. Last year was 1%.

**Moderator**

The next question is from Kaustav Kakati from PUG Securities.

**Kaustav Kakati**

My question is again basically on the private labels, you mentioned its around 4% of the revenues of the pharmacies. What I would like to understand is what is margin difference that you see between your private labels and normal FMCG goods that you would be selling?

**K. Padmanabhan**

The normal branded products that we sell has a gross margin of about 18%. The private labels although the price is somewhat lower than the branded labels offers margins in excess of 60%.

**Kaustav Kakati**

And secondly would it also be possible for you to share the working capital division between your healthcare division and pharmacy specifically in terms of inventory?

**A. Krishnan**

Okay, we will share that with you.

**K. Padmanabhan**

As far as pharmacy business is concerned it is nearly neutral as far as net working capital is concerned.

**Moderator**

The next question is from Ravi Dodhia from Crisil.

**Ravi Dodhia**

I have two queries, one is, I was looking at hospital business EBIT margins on QoQ basis, it has declined around 60 basis points so just want to know reasons for the same because new bed additions in the last quarter was also around 21 beds?

**A. Krishnan**

In Q4 of this year we had few costs on the administrative side, we had some JCI accreditation process in certain of our hospitals which required us to incur some cost on the repairs and maintenance. We had some bad debts write-off also which

were there which were bit of a one-off and apart from that as you would be aware that the nursing cost also has increased from Q4 of this year. Of course, we have started realizing efficiencies by looking at productivity, etc., subsequent to that but there was an impact in Q4 because of increase in nursing cost as well.

- Ravi Dodhia** Right so do we see this kind of margin going forward?
- A. Krishnan** No we should be able to come back to the overall margins that we had reported in the year in Q1 itself.
- Ravi Dodhia** Right and also want to know the status of the company was earlier looking for strategic partner in the pharmacy business and also it had plans to divest BPO business so what is the update on the same?
- K. Padmanabhan** As far as pharmacy business is concerned we continue to add value in that business both EBITDA positive and bottom-line positive now and we will continue to expand that business profitably. However, having said that, we believe that this is not core to Apollo therefore we need a partner who can actually take it forward and grow this in a more aggressive manner and we would be looking at strategic partners who could come and join us. However, because at this point of time FDI in retail is not very clear, we will actually wait for some time till we have clarity on that and apart from that I think, the timing of divestment will depend on what is the valuation that the business can actually command. As far as medical BPO business is concerned again, you would have seen that we have a healthy growth in EBITDA margins during the year but the business require a lot of money to make it grow and therefore we are also looking for strategic business partners and we are in talks with several of them.
- Ravi Dodhia** In terms of pharmacy business whether company has any plans to retain either 49% stake or it wants to totally divest it?
- K. Padmanabhan** Since you are attempting to capture value obviously we will be keeping a fair stake with us.
- Ravi Dodhia** I also had another query on ARPOB but that will be clarified after you include HBP. So if I have any further questions I will get back in the queue.
- Moderator** The next question is from Nitin Agarwal from IDFC Securities.
- Nitin Agarwal** For the year what would be sort of free cash that you would have generated on the hospital business?
- A. Krishnan** From operations we would have generated approximately ₹ 200 plus crore and after interest and dividend if you look at it we would still have around ₹ 100 crore.
- Nitin Agarwal** So when we say our internal accruals would account for a fair proportion of our CAPEX plan, how much do you see it really sort of contribute over next three years for you?
- A. Krishnan** Around ₹ 400 crore.
- Nitin Agarwal** So the balance about ₹ 800 odd crore would be an incremental debt that will take on?
- A. Krishnan** That is correct.

**Nitin Agarwal**

And what sort of a debt equity number that you are typically comfortable with?

**A. Krishnan**

We have said that over period of time, we are comfortable taking it 1:1 but that is over a period of time. If you look at our projections and where we stand even after including the ₹ 800 crore we are probably at around 0.4 to 0.5.

**Nitin Agarwal**

Because of the additional net worth and the way it is going to shape up?

**A. Krishnan**

That is correct.

**Nitin Agarwal**

And what would essentially take it to when you say you are comfortable taking it 1:1, what sort of event can really take it there? You are looking at inorganic growth or which will potentially take it there if it has to?

**Suneeta Reddy**

Yes, we are looking at inorganic growth if we need to take it to 1:1 otherwise it is 0.6 is the level that gives us comfort.

**Nitin Agarwal**

And what sort of acquisition would be looking at?

**Suneeta Reddy**

Probably in a place where we don't have a presence, that would be key and second I think it has to be at a price which makes it value accretive to us.

**Nitin Agarwal**

Do you see enough assets around there in the landscape to buy into because I guess a lot of assets that are around are essentially standalone hospitals, typically those are the nature of most of the assets around there. Is that a value for you in terms of buying individual hospitals and then trying to sort of get them into the fold?

**K. Padmanabhan**

I think given that currently health care valuations are fairly rich, we will have to look at the price at which you can acquire some of these facilities. If it makes financial sense we will certainly look at these acquisitions but I don't think we will do acquisitions for the sake of acquisitions.

**Nitin Agarwal**

Right and on the hospital business, for the year ROCEs seem to have come off despite of having added too many beds in the current year?

**A. Krishnan**

Between last year and this year we have added lot of beds. If you look at from FY11 and FY12 we had capitalized hospitals in the last quarter of FY11. Karaikudi was capitalized in the last quarter of FY11. There was one more hospital which was capitalized in FY11 end so between that if you look at this that is why it has come down but if you look at the EBIT margins which takes care of depreciation as well it has still expanded from 18.2 to 18.8 which is good and again as you have seen that Bhubaneswar is now doing well, Hyderabad is still at 62% occupancy given that we have now taken it to 930 beds so some of those as the occupancies increase we will see the overall margins go back to the 20% level.

**Nitin Agarwal**

Given the fact that we will have a lot of capacity sort of coming on stream over FY13, 14, and 15. Is it sort of fair assumption to make that from a return capital perspective we have pretty much peaked out at least in the near term, we will probably see some pressure on ROCEs at least till the time the next phase of expansion stabilizes for us?

**A. Krishnan**

If you look at our expansion plan pretty much it is calibrated, it is not that we are going to be adding significant numbers in one year so to that extent our rollout plans do take care of ROCE and if you look at it even this year we are going to be adding two new hospitals which is Ayanambakkam and as well as Trichy. So to that extent the ROCEs will not be impacted substantially. While the inherent ROCEs, etc., are still continuing to be at the range is that we have been looking at

earlier. This is something that will continue. The other important thing that you should look at is from a PAT perspective given that we have new 35 AD benefit is going to be available for us. The new hospitals roll out are going to be giving us that 150% depreciation and our effective tax rate going forward effective this year given the rollout plans can come to 24 to 25% from the 32% level that we were at. So the PAT increase is going to be higher.

- Suneeta Reddy** And just to add our growth has been very calibrated growth where new hospitals that we added this year will start maturing and contribute to the cash flows when the new hospitals come up. So I believe that because of this the ROCE won't get impacted too much.
- Nitin Agarwal** On the expansion how many beds do you see actually getting operationalized this year? We're talking about the commissioning schedule.
- A. Krishnan** Around 500 to 555 beds.
- Nitin Agarwal** And 500 odd each year for the next two years or is that a fair way to look at it?
- A. Krishnan** That is approximately yes, around the same 500 should be a bit higher in the next year.
- Suneeta Reddy** Yes, next year should be 800.
- Nitin Agarwal** That is commissioning or operationalization?
- S. Premkumar** Our data is based on operational.
- Nitin Agarwal** You talk about the bed addition so the 181, the new hospitals in North Bangalore, 180 beds that is one hospital. Which are the others in the table?
- Suneeta Reddy** 160 which is being added in Jayanagar.
- A. Krishnan** So if you should look at Jayanagar it is 125 beds that are operational, Bangalore is 180 beds which will get operational.
- Nitin Agarwal** Jai Nagar listed in the project schedule can you give us?
- A. Krishnan** Jai Nagar is there, if you look at the Bangalore Ortho and Spine which is going to start in FY13 which is part of the 555 beds this year. FY13 the third last in the project list.
- Nitin Agarwal** This project was not there earlier?
- A. Krishnan** That is correct. So with the new project that came in this quarter was the second last one which is 180 which is North Bangalore, Malleswaram. Jayanagar 125 beds is South Bangalore.
- Nitin Agarwal** But the fact that it is going to be commissioned in FY13, so how are you getting such a quick commission for this one?
- A. Krishnan** The building is already ready and it is an operating lease that we are entering into and the building was already ready and is just being repurposed for a hospital and we will be getting in there.

**Nitin Agarwal**

So the overall on a strategic level, has there been some sort of rethink over how you look at leasing and sort of building your own hospitals and buildings going forward, is there any sort of rethink on that?

**K. Padmanabhan**

We have said several times that we believe that we would like to own our own hospitals within India and if we were to, there could be Greenfield or acquisition but we would like to own them. But having said that we would like to see the lease model available for taking the building on lease then that would be a preferred option if the yield on the lease are significantly lower than our cost of capital. So whatever are the projects that we have of late taken on lease are at a significant discount to our cost of capital and that is our preferred mode as we go forward.

**Nitin Agarwal**

Typically what is the structure of these lease models? Do you give them a percentage of revenues?

**K. Padmanabhan**

There are a few, but these are invariably straightforward lease where we take them for about 30 years lease which are rental lease between interest 6 to 7% with an escalation of about 12% every three years but there are one or two where we give a percentage of EBITDA but never a percentage of turnover.

**Nitin Agarwal**

What is 6 to 7%?

**K. Padmanabhan**

It is a running yield for the property owner.

**Nitin Agarwal**

And lastly, last time we talked about the Board sort of formulating the strategy for the daycare centers as well as the single speciality clinics. So have we arrived at some sort of roadmaps as far as that single speciality clinics and rollouts and all is concerned?

**K. Padmanabhan**

We have in fact mentioned in the last quarter that is in 3<sup>rd</sup> Quarter that we have commissioned our daycare centers which is a pilot and all signs show that it would be a successful pilot and after evaluation of that pilot we will look at rolling it out throughout the country. As far as the clinics are concerned it is part of our clinics business and we are rolling out outpatient clinics quite aggressively. Currently we have about 100 clinics in the country of which 50 are owned.

**Nitin Agarwal**

But this would be the primary clinics or these are the speciality clinics like probably dialysis clinics or the diabetology clinics?

**Suneeta Reddy**

That we are actually testing the model, we do have a few dialysis centers but it is part of our hospital business right now.

**Nitin Agarwal**

You don't see that per se becoming a different vertical or a significant vertical for you in terms of?

**Suneeta Reddy**

We are looking at taking whatever we can which is retail and daycare into a separate vertical which includes dialysis, dental, cosmetic and the clinics that we do now and the sugar clinics and wellness clinics.

**Nitin Agarwal**

How do you see this piece of business growing for you going forward? Is that a big investment piece for you?

**A. Krishnan**

Form an investment perspective these are not as large because pretty much if you look at the clinics it is around 1-1.5 crore per clinic, etc., and even in dental it is less than a crore so investments should be not as large as compared to a hospital. So as Ms. Suneeta said we are evaluating the model, we are testing the model on a

- pilot basis already and based on the responses we would decide on the full-fledged rollout across.
- Suneeta Reddy** I think the way that we are progressing is that in cities where we have a presence we are very comfortable opening the clinics we are just looking at the other markets little bit more carefully before we start.
- Moderator** The next question is from Priti Arora from Kotak.
- Priti Arora** My question is on your pharmacies, you open 155-165 pharmacies every year and the non-performing ones are then shut down three of five years later. So my question is on the strategy of why not take it slow from day one on opening stores in sort of more profitable areas than reduce the gestation time, and not spend those 3-5 years?
- K. Padmanabhan** What we do now is an annual review, yes, you are right in the sense that we did a review after 3 to 4 years, last year we closed some unprofitable units. This happened at the time frame when we are opening one pharmacy a day and therefore growth took precedence over profitability at point of the life cycle of that business but today we are calibrating the growth with a focus also on the EBITDA and so we are opening pharmacies far less aggressively than we used to let us say 3-4 years back and we are also having to close down few of the pharmacies as a result of that.
- A. Krishnan** And this is visible in the Q4 closure, Q4 if you look at it we added 81 stores and closed down seven so for the year as Padmanabhan said it is a skewed because in Q1 and Q2 there were some higher closures.
- Priti Arora** But overall where do you want to stop at, you are at 1,300-1,400 pharmacies?
- K. Padmanabhan** Yes, I think the critical mark would be around 5,000 odd or even 10,000 pharmacies but right now we are in the next couple of years we are looking at taking it to about 2,000+ pharmacies next 3 to 4 years but given that the total numbers of pharmacies outlets in this country is about 600,000 and aiming for 5,000 or 10,000 is not a very ambitious target at all.
- Suneeta Reddy** Just to add to that is not just pharmacies but there are certain synergies that they bring within the system. So every profitable pharmacy that we have actually adds value to the system itself.
- Priti Arora** Okay and this 5.7% EBITDA margin for mature pharmacies, how quickly can you ramp it up to say 8% odd with your private sales label going up?
- K. Padmanabhan** I think what we have looked at is that in this business we can actually take the EBITDA margins of mature pharmacies anywhere between 7 to 8% in about 4 to 5 years' time. To have a steady state 7% to 8% EBITDA margins we need private labels to contribute at least 12% to 15% to our total revenues.
- Priti Arora** On Chennai to drive home the point that inpatient volume you mentioned has picked up. So can you give us the 4<sup>th</sup> Quarter numbers, how much has the growth been?
- A. Krishnan** Not in the 4<sup>th</sup> Quarter, as we said April numbers have been looking good compared to April of last years, what I said, 4<sup>th</sup> Quarter numbers were higher only by 1%.
- K. Padmanabhan** Yes but I mentioned earlier in Chennai Main we are building out facilities in Chennai. In Chennai Main itself is a limited by the number of beds. Unless we have



some significant reduction in ALOS I don't think we can see significant growth in inpatients numbers because the hospital itself is only about 600 beds and it has got about 80% occupancy. So the head room for growth can only come from reduction in ALOS but what we are attempting to do is some reduction in ALOS but a significant improvement in case mix, as Prem was referring to the inpatient COE which will increase revenue for beds and an absolute EBITDA and this is what our aim is.

**Priti Arora** But do you think you have scope to reduce ALOS that much because ALOS in Chennai is already the lowest among all the other major hospitals and given Chennai as a super speciality?

**Premkumar** As Padmanabhan has said, it is one of those measures but apart from it we are also looking at increasing our average realization in terms of case mix and so on.

**Priti Arora** And one last question, please can you comment on the EBITDA margin trend across your standalone hospitals and JV subsidiaries and hospital based pharmacies, how has that panned out?

**K. Padmanabhan** The EBITDA margins range from something like 20% to about 32%, 33% or 34% as some of our facilities like Chennai and Calcutta enjoy a EBITDA margin in the hospital business in the order of about 30% plus. Some of our newer facilities have EBITDA margins in the range of 18 to 20%. The only exception is Hyderabad where we have an EBITDA margins of 20% that is only because a lot of the new facilities are coming there so we have a lower EBITDA margin and of course Bhubaneswar which is a new facility.

**Suneeta Reddy** Which is at 13% currently.

**K. Padmanabhan** The hospital business can very well deliver on an average of about 25% EBITDA margins, it includes the hospital based pharmacies.

**Priti Arora** But how have the JVs and subsidiaries on the whole behaved – have the margins have gone up YoY?

**K. Padmanabhan** The JVs, if we look at in Calcutta I think Krishnan was explaining about someone one-time issues there therefore the EBITDA margins did come down. Bangalore has actually gone up and so has Ahmedabad and Delhi has remained about the same.

**Moderator** The next question is from Aditya Khemka from Nomura.

**Aditya Khemka** Firstly, how many of the current 37 hospitals premises are leased and how many are owned by Apollo?

**A. Krishnan** We have to come back to you on this if you come off-line we could probably give you that number.

**Aditya Khemka** That is absolutely fine and in the pipeline the 13 facilities that you have so how many of those would be leased, can I just get a rough number there?

**A. Krishnan** So if you look at the list that we have, Navi Mumbai is owned, Byculla is an operating lease, Thane is owned and if you look at going forward Woman & Child is owned, the Chennai one in OMR is leased, the South Chennai one is again leased, Nasik is owned, Nellore is owned, Trichy is owned, Patna is owned, Vizag is owned, Bangalore Ortho & Spine is leased, Bangalore North is leased.

**Suneeta Reddy**

And Bilaspur is also leased.

**Aditya Khemka**

Okay that is great. About the acquisition plan that we just spoke about, just to get some more insight into that. So what kind of expansion, what kind of inorganic opportunities are we looking at? Are we looking at consolidating our current presence into tertiary and super speciality care or are we looking at diagnostic and are we looking at acquisitions only in the domestic arena or are we also open to opportunities outside India?

**K. Padmanabhan**

As far as acquisitions are concerned it is going only within India and our focus predominantly will be only hospitals of 100 beds and above, therefore the intention is to specialize. As I mentioned earlier they must come at a discount to the valuation which the company currently enjoys.

**Aditya Khemka**

But in that case if I look at the pipeline and obviously you guys are stressing more on increasing the concentration in the urban areas. So when you are looking at the acquisition targets are you really looking at more rural set-ups or are you looking at urban setups?

**K. Padmanabhan**

It would be urban where there is good potential in rural but it will be urban centers.

**Suneeta Reddy**

We don't want to duplicate our presence unless it's consolidates our presence there so it is highly unlikely that we will move to a city where we are already there.

**Aditya Khemka**

Any ROCE hurdle rates that we have in mind before we go ahead and do such a transaction any ROCE that we have in mind?

**K. Padmanabhan**

Long-term return on capital employed that we should get is about 20% plus.

**Aditya Khemka**

The other question that I have was on the Navi Mumbai hospitals. So if I remember correctly in our previous presentation we were expecting the hospitals to be commissioned by June 2013 that is 1<sup>st</sup> Quarter 2014 and now we are saying that it could get further delayed about first-quarter of FY15. Did I hear that correctly?

**K. Padmanabhan**

Yes, that is right.

**Aditya Khemka**

Any issues you are facing there?

**Suneeta Reddy**

I think all the issues have been settled and the construction is on full swing. Approvals and contractors which got delayed but now everything is on full swing but now everything is on full swing and we should have it by the end of 2015.

**Aditya Khemka**

So that is early FY15 or is it calendar year 2015?

**Suneeta Reddy**

FY15.

**Aditya Khemka**

Last question, if I look at the CAPEX that you still need to do some of 1,750 odd crore and we just spoke about how we need about ₹ 800 crore of debt. So if I look at the next three years, how would the CAPEX these ₹ 1,750 crore be spent over the three years, my guess would be most of this needs to be front-ended for the building?

**A. Krishnan**

It is almost given that, if you look at there are fair number of hospitals which are getting commissioned now and a couple of hospitals in FY13 itself and then FY14 and FY15. It is not really as front ended there is some stress that will come now because of the medical equipment requirements for the new hospitals after that in

FY14 and 15 it would equalize so maybe you can look at it around 400 crore each of the year and 400-500 or maybe 500.

**Aditya Khemka**

Sorry I didn't get that.

**A. Krishnan**

The requirement that we have for the CAPEX is approximately 400 crore this year, 500 and then 500.

**Aditya Khemka**

So that is still 1,400 out of the 1,750 that you need?

**A. Krishnan**

That is correct so between the last two years it would be a bit more higher because if you look at it, it could be then 650 and 650 because two new hospitals that got added now in this quarter.

**Aditya Khemka**

Right but we have quite a good visibility on the 400 crore CAPEX in FY13?

**A. Krishnan**

Yes, it is almost tied up.

**Moderator**

Ladies and gentlemen due to time constraint that was the last question. I now hand over the conference back to the management for closing comments.

**Suneeta Reddy**

Ladies and gentlemen thank you for attending this call. On behalf of team at Apollo hospitals, we would look forward to communicating and interacting with you. Please reach out to Krishnan or Krishnakumar if you have any further questions. Thank you for now.

**Moderator**

Thank you very much. On behalf of Apollo Hospitals that concludes this conference call.