“Fortis Healthcare Limited Q3 FY16 Post-Results Conference Call”

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Moderator: Ladies and Gentlemen, Good day and welcome to the Q3 FY16 Post-Results Conference Call of Fortis Healthcare Limited. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference, please signal an operator by pressing '*' and then '0' on your touchtone telephone. I would now like to hand the conference over to Mr. Anurag Kalra – Vice President, Investor Relations at Fortis Healthcare Limited. Thank you and over to you, sir.

Anurag Kalra: Thank you, Inba. A very good evening and good afternoon ladies and gentlemen and welcome to Fortis Healthcare's Q3 FY16 Results Call. The call today is being led by Mr. Bhavdeep Singh – our Chief Executive Officer, joining him we have Mr. Sanjeev Vashishta – the Chief Executive Officer of our Diagnostics business and Mr. Gagandeep Bedi – our Chief Financial Officer. The format of the call will be as follows. I would request Mr. Singh to make some opening comments of the quarter gone by, post which Sanjeev will make some remarks on the Diagnostics business and then I will join you for the financial presentation. Over to Mr. Singh please.

Bhavdeep Singh: Thank you very much Anurag. Good afternoon and Good evening to all of you. Thank you for joining the call. As Anurag just mentioned we would like to walk you through Q3 performance. Just at a high level, we have seen some of the numbers already, Fortis Healthcare continues on its journey towards building a better healthcare proposition for India. Our focus continues to be in a very significant way focusing on the patient, focus on clinical outcomes, working with our doctors, our nurses to ensure that every patient and every time they come into our hospital has an experience that they can feel good about and they leave the hospital and feeling better.

With that said, when you look at some of the numbers, quarter three as you know encompasses Diwali and Festival season and there was a little bit of an impact there, but with that said, our revenue has come in at still high single-digit over last year, 7% over last year, a combination of Fortis numbers and SRL numbers and we are going to each one of them as Anurag talks through them.

Our EBITDA continues to grow. On a percentage basis we are slightly above last year and certainly feel that on a trajectory basis, encompassing the holiday season, the festival season our numbers that we feel good about as well.

We continue to invest in our hospitals, we continue to invest in our diagnostic business, you will hear more from Sanjeev on that in a couple of minutes but from a CAPEX perspective they were very aggressive plans with respect to upgrading the equipment, the technology and ensuring that we will continue to support our doctors with what they need to take care of our patients.

We also, as Anurag will share some details with you in a few minutes, the Board of Directors approved the acquisition of 51% economic interest in FHTL which encompasses two hospitals i.e. Shalimar Bagh Hospital and Gurgaon Hospital and we will go through the numbers with you, but the bottom-line is that once the transaction is completed this is going to add 200 crores to our EBITDA number and 50 crores to our PAT number. So we certainly think it is a good transaction and a good outcome for the organization.

So net-net, at a very high level revenue continues to grow, we will talk more about that in detail but we certainly feel that as we look forward to Q4 and next year beyond that, the revenue work should continue in a solid fashion, our EBITDA numbers continue to deliver, we did have an exceptional loss that we declared this quarter and we will hear more details about that around the bonus and some one-time activity. They are one-time incidents and while they impact the quarter, I think operation we look at the business as going forward we certainly do not anticipate that happening on a regular basis so I think you have to reflect that as we look at the numbers to see where the business has landed this quarter.

So with that, I am going to ask my colleague Mr. Sanjeev Vashishta to make some comments and then we will give it to Anurag for financial overview.

Sanjeev Vashishta: Thanks Bhavdeep. Good afternoon everybody. So as I had shared with you during the last call in very brief, third quarter is the most sluggish quarter in our case and it has really lived up to its expectation. While the quarter was sluggish, we have taken a lot of steps to ensure that the business grows in a similar fashion and a robust fashion and it has been doing over the last 20-odd quarters. In fact, if you look at our top-line growth, top-line growth if I make apple-to-apple comparison, we have closed certain centers last year and the first half of this year, you will see that the growth is close to around 11%, 12%, not too great but we are hoping to kind of turn the corner in the coming quarter on the growth side. However, we have been able to really protect our margins. If you look at the margins in the Q3, they are close to about 22% as opposed to around 18% in the corresponding quarter over last year. The YTD number is impressive, it is still holding fort around 25% on the marginal side.

Now while we understand that we need to work on this quarter thing which is pretty much reflective of what is happening in the industry, we have taken a lot of steps to ensure that going forward even in the third quarter we are able to make good business or show good results to our investors. We have worked extensively in setting the processes right, initiated various programs to increase our footprint. Just to share with you, we have opened 24 new labs in this quarter, in Q3. And you would recall, I had briefly shared with you about our balance presence across the length and breadth of the country.

Just to reiterate, 35% business comes from north, 27% from west, 22% from east and about 16% odd from south. And this time when we had opened, we did extensive mapping of the geography we have opened a few labs in the service sector and in the days to come you will see that this is becoming more and more balanced growth for us. So that is pretty much what we have done, we have got some initial couple of very-very prestigious products, we grabbed very prestigious project from UNICF which is around 37 crores, we have to execute this in less than 18 months' time. We have successfully completed the pilot and on the Valentine's Day which is on 14th of February we are starting with the main project and we are hoping to close this within 12 months' time so that will give us a significant presence, bump. We have tried to kind of put our foot in the door and we are hoping to get such businesses from the multilateral agencies.

Another big win for us in this quarter has been we are winning the PPP tender with the UP Government and by virtue of this we have been given the lab management, actually through opening the, it is really asset like model, we will be opening our own company operated collection centers in 22 government hospitals and this is highly lucrative. Even today we have seen, though it is early days for us, yet we see on an annualized basis we are doing a business worth about 7 crores to 8 crores. Going forward, it should expand to both 15 crores - 20 crores per annum. So all in all, I think we have got the right kind of building blocks and we will ensure that we will go on with a strong growth in the coming quarters, coming years which will be to be seen by everybody.

And with this, I think I will be very happy to take up the question-and-answers, but before that I am just giving the call to Anurag who will take you through the financial performance.

Anurag Kalra: Thank you Sanjeev. Ladies and Gentlemen, I shall first take you through the financial presentation for quarter three FY16 in terms of the P&L followed by the YTD nine month numbers, then talk a little bit about the balance sheet and end with a synopses of the FHTL transaction that we have just announced.

For quarter three FY16, our India hospital business recorded revenues of Rs.850 crores, this compares to Rs.792 crores in the corresponding previous quarter. Our operating EBITDAC which is EBITDA before the net BT cost recorded a margin of 14.3% as compared to 15% in the previous corresponding quarter. The diagnostic business continues to do well, it recorded revenues of 180 crores which were more or less similar to the corresponding quarter but EBITDA continued a good growth trajectory, it grew a strong 21% to Rs.39 crores and this figure represents a margin of 21.9% and compares to 18.2% in the corresponding previous quarter.

At a consolidated level, for the India business, revenues were at 1,029 crores compared to 971 crores. Our consolidated EBITDAC was at Rs.161 crores and this presents a margin of 15.7% versus a margin of 15.6% in the corresponding previous quarter.

After accounting for the net business trust cost of Rs.113 crores for the quarter, our operating EBITDA which is without assuming any other income grew 25% to Rs.48 crores and like-to-like figure was Rs.38 crores in the corresponding previous quarter.

Our finance cost stood at Rs.29 crores and this was lower by Rs.6 crores, it was about 35 crores in Q3FY15, the results being primarily due to the FCCB redemption we did which was about US$100 million in Q1 of FY16. Our depreciation and amortization was at Rs.53 crores versus Rs.65 crores in the corresponding previous quarter. Our PBT before any exceptional items stood at a (-)18 crores versus (-)42 crores in Q3 FY15. Our PAT after exceptional items, minority interest and share and associates, the share and associates being our 28% share in RHT profits was a negative 50 crores compared to a negative 26 crores, but this PAT is also impacted by the one-time exceptional expense of Rs.32 crores primarily due to the revision in the Bonus Act which took place from retrospective effect and the exit of select laboratories on the diagnostic business side.

At the Group level, we have recorded revenues of Rs.1,041 crores versus Rs.1,025 crores. Just to remind all of you, this is not comparable to the corresponding quarter because the corresponding quarter has the business of both RadLink and the Fortis Surgical Hospital, if you recall these were the businesses that we have divested in Q1FY16.

Our EBITDAC at the Group level was Rs.159 crores versus Rs.147 crores, representing a margin of 15.3% and this is better than the 14.3% in the corresponding previous quarter. Our PAT after minority interest and share and associates was a (-)55 crores, this compares to a loss of 22 crores in the corresponding previous quarter, but as I had mentioned before, the 55 crores loss includes an exceptional expense of about 32 crores.

On a nine months basis, YTD FY16 financials, our hospital business recorded revenues of Rs.2,571 crores, a growth of 8%. Our operating EBITDAC grew 14% to reach Rs.377 crores, this represents a margin of 14.7%, 70 basis points higher than the previous corresponding period. The diagnostic business grew 9% to reach revenues of Rs.572 crores, its EBITDA stood at Rs.141 crores, a robust growth of 31% and this represents a margin of 24.6% versus margin of 19.9% in the previous period.

At a consolidated level for the India business, revenue stood at Rs.3,144 crores, a growth of 8%. Consolidated EBITDAC both hospitals and diagnostics grew 18% and reached Rs.518 crores, this 518 crores number represents a margin of 16.5% compared to a margin of 15.1% in the corresponding previous period, so again a very good growth on a YTD nine months number basis. Our BT cost for nine months were at 345 crores, representing an increase of about 3.5% and our operating EBITDA after BT cost was 174 crores, a very-very strong growth of 63%. The finance cost for nine months stood at 88 crores versus 107 crores in the corresponding previous period, while the depreciation and amortization was at 153 crores versus a number 171 crores. Our PBT before exceptional items was actually at a breakeven for the first nine months of the year versus a (-120) crores as compared to the nine months of FY15. Our PAT after exceptional minority interest, and share and associates was (-67) crores compared to (-89) crores in the corresponding previous period.

At the Group level, we have recorded revenues of Rs.3,188 crores versus Rs.3,076 crores, but like I had mentioned to you at the Group level the numbers are no exactly comparable. Our EBITDAC at the Group level recorded a 21% growth to reach Rs.512 crores, representing a margin of 16.1% versus a margin of 13.8%, so very good growth over there as well. Our profit after tax after minority interest and share and associates was a positive 66 crores as compared to a loss of 126 quarter in the corresponding previous period.

That was the P&L on the quarter and YTD basis, I shall now run you through the balance sheet as of 31st December, 2015. We have a shareholders' equity of including minority interest of Rs.4,875 crores, we have outstanding FCCBs of Rs.563 crores, you would know that these FCCBs are substantial in the money now but there is still debt on the books so we take them as debt. Our debt, excluding the FCCBs was Rs.714 crores, which gives us a total capital employed of Rs.6,151 crores. This is employed as follows: about Rs.1,791 crores in net fixed assets, about Rs.2,156 crores in goodwill, our investments as of 31st December 2015 stood at Rs.1,007 crores while we had cash and cash equivalents of Rs.569 crores, our net current assets stood at Rs.628 crores, giving us total assets of about Rs.6,151 crores, this we continue to maintain a strong balance sheet with a balance sheet that I just disclosed to you we are sitting on a net debt to equity about 0.15 times and this is actually better than the corresponding previous quarter where it was 0.27 times. That is on the balance sheet side.

I shall now briefly take you through a synopsis of FHTL transaction that the Board has just approved. The FHTL is basically an RHT subsidiary that comprises of Fortis Memorial Research Institute, our key facility in Gurgaon and the Fortis Hospital Shamilar Bagh, our facility in New Delhi. We have acquired 51% economic interest in this subsidiary for approximately Rs.970 crores. I do not know if some of you got a chance to read the RHT announcement, but they have stated their intent to distribute the net proceeds from this divestment as dividend to their shareholders. You know that Fortis has a 28% stake in the trust and we would receive our share of commensurate dividend. If you were to assume some numbers around that, our net investment for this 51% economic interest would be about Rs.740 crores. What this does to our P&L, as Bhavdeep had also mentioned in his initial opening comments, is add an EBITDA of about Rs.200 crores because that is the service fee that was paid to them and it adds about Rs.50 crores to our PAT.

That is a very brief synopsis of FHTI and that is the end of my presentation. We would be glad to take questions from the audience please. Thank you very much.

Moderator: Thank you. Ladies and Gentlemen, we will now begin the question-and-answer session. Our first question is from the line of Girish Bakhru of HSBC Securities. Please go ahead.

Girish Bakhru: Just first on the acquisition bit, if you could just give us some color on how this basically changes the role of Fortis in investments in FMRI and CAPEX plans going ahead?

Anurag Kalra: So now with Fortis acquiring I think the role for the entity that we take control over, we will take on the CAPEX basically.

Girish Bakhru: So whenever the next phase of FMRI happens, basically that entirely comes to you, right?

Anurag Kalra: Yes, to the extent yes, we have control so it comes to us and from a consolidation perspective of course 51%, so based on 51% we get consolidated in our books.

Bhavdeep Singh: The answer to your question is exactly, the answer is a strong affirmative, where there is the CAPEX perspective only the governance thing that takes places, it is done strictly through Fortis Healthcare.

Girish Bakhru: And when do you envisage that, I mean I do not know what is the occupancy currently in FMRI so when do you think that expansion phase will happen?

Bhavdeep Singh: This is a hospital that we certainly think has a tremendous future, but there is nothing planned at this time, we continue to move forward with investing in the hospital, but I think that the growth that we have will come from the existing four walls. But at the appropriate time we will consider it and when we do it will be financially and otherwise logical to do so.

Girish Bakhru: Right, my question is more on that similar line, that given that this is a key asset in the network and it has performed very well compared to the standard set in the country and what level do you think where this deal can benefit you? I know you have given some numbers for this year but say three, four years down the line where do you think this transaction will materially add in the P&L and if you could throw some color on what kind of contribution do you see from FMRI particularly?

Bhavdeep Singh: See, when the deal was set up because it was 51%, if we go forward, if the hospital continues to grow, everything the earnings growth stays here, the EBITDA stays here. And I think that you rightly mentioned that hospital is doing well, very soon this will become our first 500 crores facility and there is no reason that as we go forward in the next two, three four years it would not become 600 crores, 700 crores, 800 crores hospital. So either the return on this investment would continue for the foreseeable future as we go forward because every year that profit is all going to sit right here versus going back to RHT which was there before.

Girish Bakhru: And can you comment on what is the level of margins that FMRI is doing at this moment?

Bhavdeep Singh: We are at the high end of 17% and the good news there is that as the hospital continues to fill up that number continues to grow quarter-on-quarter.

Girish Bakhru: And just second one on the overall investment in the robotics, I just wanted to know, I mean this being the first investment I think in that area, what are your long-term plans with that and how do you account for this investment?

Bhavdeep Singh: So robotic is a medical equipment, it is a normal CAPEX.

Girish Bakhru: It is not expense, it is basically normal CAPEX, okay.

Bhavdeep Singh: It is like an MRI or a CT scan, it is a medical CAPEX.

Girish Bakhru: And is it something that you think will be materially, I mean I think overall view is that yes robotics will grow significantly but is there something that you think it will be beneficial in the near-term or will take a long time say to be accretive on the margin side?

Bhavdeep Singh: No, I think the benefits come in fairly quickly, I think there are two or three things, one is, from a positioning perspective as a premier flagship hospital for Fortis Healthcare I think it takes our positioning up. As you are probably aware, because you sound like a bit about healthcare, the primary, the initial focus here with any robotic program is gynecology and neurology and we have actually done our first transplant here. Gynec procedures are continuing to go up, so I think that the return on it is going to start coming fairly quickly. We are ahead of schedule with respect to the number of procedures we are doing, and we are so encouraged by what we are doing, in quarter one we are actually going to order our second robotics program, so we did not have any till six months ago, we have ordered our first and by Q2 we will have at least two within Fortis and potentially we are planning for two or three more. So initial results are very strong and we think this will be a big boost for our value proposition as we going forward.

Moderator: Thank you. Our next question is from the line of Ayan Deb of Nomura. Please go ahead.

Saion Mukherjee: Hi, this is Saion Mukherjee. I just have a question on the FHTL transaction, in terms of cash flows can you take us what is the kind of maintenance CAPEX that you need to do? And is there any other cash outflow on account of this transaction that we need to service?

Anurag Kalra: So Saion, in terms of pure cash flow from the transaction, clearly what is going to happen is, like I had mentioned earlier about 200 crores of EBITDA comes into our fold because FHTL we becomes our subsidiary. However, at the same time the 49% that is still lying owned by the RHT still needs to be serviced and that servicing will be done by interest cost on our P&L to the tune of about 75 crores. Other than that, FHTL as a standalone entity will also have to pay some tax broadly in the range of about 20 crores to 25 crores. So purely from a cash flow perspective, this will probably add 100 crores to our kitty.

Saion Mukherjee: And what about CAPEX, the one which FHTL was doing?

Anurag Kalra: So FHTL was really not doing any CAPEX on the FMRI or the Shalimar Bagh side, nothing extensive or substantial.

Saion Mukherjee: And in terms of regulatory clearances for this from the RHT side, what are the norms there, I mean what percentage of the shareholders need to accept this?

Anurag Kalra: I think we will have to check that, we are not sure of that, but I think the way this will function and I think RHT is best position to answer this, but to the best of our knowledge I think this goes to the regulator there for his approval, post which unit holders over there will have to give it in approval. Now I am sorry I am not sure whether the Fortis there can vote for that or not, but I do not think it can.

Moderator: Thank you. Our next question is from the line of Praveen Sahai of B&K Securities. Please go ahead.

Praveen Sahai: My question also related to this transaction, the Religare Health Trust used to own the subsidiary health Fortis Hospital and where we had taken a 51% stake, right? And another, the company Fortis Health Management has also stake in the Shalimar Bagh and the FMRI, am I correct in that?

Anurag Kalra: Praveen, FHML, Fortis Health Management is a subsidiary of RHT.

Praveen Sahai: So I just wanted to clarify, both the subsidiaries like Fortis Hospital is subsidiary of RHT and the Fortis Health Management also is a subsidiary of RHT and both hold stake in this two entities?

Anurag Kalra: No, the stake in FHTL is held by FHML, Fortis Health Management Limited, there is a cross holding basically.

Praveen Sahai: And now the Fortis Healthcare is going to hold the 51% stake and the rest is going to be owned indirectly by the RHT?

Anurag Kalra: That is right, 49% by RHT and 51% by Fortis Healthcare.

Praveen Sahai: And next thing on this transaction is, two clinical establishments belong to this transaction, the rest 10 are still directly with the Religare Health Trust?

Anurag Kalra: Yes, that is correct, no change there.

Praveen Sahai: And others for Greenfield and two operating hospitals are also directly with the RHT?

Anurag Kalra: Yes, absolutely.

Bhavdeep Singh: There is no change in any other holding, it is just a very specific piece.

Praveen Sahai: So next question is related to the diagnostic business, just wanted to understand what highest margin we can go and achieve on this particular business because right now we have somewhere around 22% of EBITDA margin for this quarter, so what is our goal going ahead to achieve?

Sanjeev Vashishta: So Praveen, I think the goal is rather encouraging and promising, I think the goal has to be always aspiration. I think going forward, we expect that the margins should be touching around 30 and that is something which is sustainable in the business given the opportunity, given the scale and size at which we are operating because if you look at the building blocks which we have been able to build over the last few years, these are quite enabling. I think we need to now fill the capacities, get as much business as possible into these assets and I see it is not really difficult for us to reach there really and if you look at the last quarter I think every year we have grown the margins by 2.5% - 3%. So I think this trend should continue for few more years.

Praveen Sahai: So I just compared with the peers, so the peers' numbers are also available, so they are fetching a higher margin as compared to our diagnostics business. So any specific comment on that?

Sanjeev Vashishta: So Praveen, I will not be doing justice if I try to get into the shoes of my competitors, I mean they have to fend for themselves. But all I can tell you is that while our margins are actually increasing, if you look at the so called competitors I think their margins are either shrinking or they are kind of stabilizing at some level. And this gap which used to be considerable over the last few years has actually shrunk almost to an inch. So in my mind I think we are on the right trajectory and going forward I think the numbers are going to show an upward trend only.

Praveen Sahai: Any guidance on the growth side sir, like our expectation for the going forward two to three years, what growth we are expecting?

Sanjeev Vashishta: I can just tell you about the fundamentals, and if you look at the fundamentals in our country they are very good about this business, that is the reason why this industry has become darling of everybody, and rightly so. See, if you look at the sample to test ratio, in our country is abysmally low and I am just giving you one of the parameters, it is less than two times which means that from one sample normally less than two tests are being done, in the European countries it is close to six times, in US it is 12 times and in certain hospital systems it is as high as 20 - 25 times. Now this is the opportunity, without actually having to do any significant investment if we are just able to educate the doctors, reach out to the masses and do all right things which we are doing, I think this number can be really grown exponentially. That is one. Secondly, I was talking to somebody and I can reflect this thought with you, somebody told me in one of the forums that in our country there are only about 27% - 28% of people who have never given the blood for testing, so that is a scope which is available to us, I think the market has to be explored and really penetrated which we are doing.

Moderator: Thank you. Our next question is from the line of Rakesh Naidu of Haitong Securities. Please go ahead.

Rakesh Naidu: I have a follow-up question on the transaction, you said that maybe about 51% stake in FHTL, what is actually preventing us from taking the entire 100% stake? And second question is, if I have heard it correctly, you said that remaining portion of 49% which still remains with RHT will be serviced in the form or interest payouts. So does that mean that the transaction has been renegotiated, and if it is, can you please share the details?

Bhavdeep Singh: On the first part of the question, at this time this is the only transaction that we are conducting, you have heard already that the buying back 51% makes eminent sense for the business, the investments that we are making on a cash outlet perspective is while there has been an appreciation on what the value that we sold for versus what we are paying for is 11% CAGR on that, we think that is a fair number. And I think bringing it back in makes all the sense in the world from an economic perspective, it is delivering the numbers you have heard already, a solid return on the bottom-line, EBITDA and PAT number as well and this time this is the only thing which we are doing. I do not think there is anything more to comment beyond that at this time.

Anurag Kalra: Rakesh, on your second question in terms of the interest cost, very clearly, the structure that was put in place at the time of the RHT IPO still stays in place, so there is really no change in terms of the financial service fee that we will have to pay them. Like I had mentioned earlier, there are still 49% holders of FHTL and hence they are entitled to 49% of the service fee that we would pay them. So that is basically going not as a service, it will go in the form of interest.

Rakesh Naidu: Can you elaborate, I mean what would be the nature of the OPEX line item, it would still be sensitive to the operational performance of both these hospitals or it would be fixed?

Bhavdeep Singh: Sorry, just repeat, did not get your question.

Rakesh Naidu: Wanted to understand the nature of this interest payouts, would it be fixed peg or it would still be a function of how these two entities continue to perform?

Bhavdeep Singh: There is no connection with the performance of the units.

Rakesh Naidu: These would be fixed peg, is it?

Bhavdeep Singh: Again, the operational unit, there is no contribution, there is no component of which that is FHTL does well we pay more or less whatever it might be, no connection with that whatsoever.

Rakesh Naidu: And one more question if I may ask, Sanjeev suggested that he would see 30% EBITDA margin as a sustainable rate for the diagnostic business, is it correct?

Sanjeev Vashishta: Yes, that is right, over a long-term we are looking at this kind of, as I told you given the opportunity that we have at hand I think that is possible.

Rakesh Naidu: So sir, I want to know what portion of your COGS is export depended and given how the currency has shaped up how do you see that impacting the margins going forward?

Bhavdeep Singh: See, the good thing is that we have been able to, if you are talking about the COGS you are talking about the consumption essentially, we have been able to tie-up with all our vendors in the INR. So all our agreements as of now are in INR so which is a very good thing and going forward we intend to kind of carry forward these agreements with them, so it really does not impact us adversely should the INR goes down further. So to that extent we are hedged.

Moderator: Thank you. Our next question is from the line of Prashant Nair of Citigroup. Please go ahead.

Prashant Nair: I had a question on the diagnostics business, now there is a sequential dip in the margins, second quarter was around 28.5% or thereabouts, now should we take or what level should we take your steady state margin for the near to medium-term?

Sanjeev Vashishta: Prashant, so if you are aware I think third quarter every year is a sluggish quarter, and this is the point which I made last time also, while second quarter invariably is the best quarter in our case of maybe quite similar to the fourth quarter, but third quarter is very rather slow for couple of reasons, one is the festival seasons and in the healthcare industry this is considered to be a healthy season which was good, I mean if you want people to stay healthy. But again, if you look at our numbers and every year the history repeats, so there is a slight dip in the third quarter and again it takes off. If you look at consol numbers, I am not talking about the standalone because numbers which you get from the Fortis system or from the group systems are the ones where the net off the Fortis transactions between Fortis and FHTL. Now if you look at our margins, they are consistently growing over the last four years from 9.7 to 12.9 to 16.5 to 19 last year and this year we are hoping to take up the overall number to about 21% - 22%. So this is the guidance I can give to you. Now going forward I think the hope that this improvement in the margins by 2.5% year-on-year for the near foreseeable future should be replicated.

Prashant Nair: So this 22% margin is as the numbers are reported or the way you track it without netting of the Fortis?

Sanjeev Vashishta: I am talking about EBITDA numbers, these are essentially the reported numbers only. See, the gap would be only in the revenue numbers.

Moderator: Thank you. Our next question is from the line of Dhiresh Pathak of Goldman Sachs. Please go ahead.

Dhiresh Pathak: The 970 crores or call it 1000 crores, this is for 51% stake right or for 100%?

Anurag Kalra: This is for 51%.

Dhiresh Pathak: So then about or call it 1900-odd crores for the full two hospitals, and you are saying it was about 1480 when you sold?

Anurag Kalra: 1400.

Dhiresh Pathak: Now that has become 1900, 11% CAGR is what you refer to, right?

Anurag Kalra: Yes.

Dhiresh Pathak: Now just to understand better, why are you showing it as an interest cost and not taking that in minority interest?

Anurag Kalra: No, no Dhiresh there is a minority interest outgo also, so basically from a cash flow perspective as we were explaining earlier on, from a cash flow perspective there is an EBITDA addition to our P&L and because we still have to give them 49% of the service fee in the form of interest there is a cash outgo of about 75 crores that you will see in our P&L. Post that, yes there would be a minority interest for their 49% stake as well.

Dhiresh Pathak: No, so this is not clear. So for example, let us say 200 crores of service fee that represents for the 100% of the asset, right?

Anurag Kalra: yes.

Dhiresh Pathak: Now you own 51%, just to keep it simple let us say 50:50, you own 50% they own 50%, you are entitled to 100 of this and they are entitled to let us say 100. Now this 100 you are going to show part of it in interest cost and part in minority interest, is that what you are saying?

Anurag Kalra: So Dhiresh what we have done, and this is a little complex, we have actually taken over the assets and liabilities in the ratio of 51:49 and we have actually affected the transaction through the purchase of CCDs to the extent of 51%. So those CCDs would be consolidated in our P&L and the interest cost that I was referring to was on those CCDs. They have certain CCDs that we purchased and certain with them in the ratio 51:49/

Dhiresh Pathak: So their economic interest is through the instrument of CCD not through an equity or anything?

Anurag Kalra: Yes, that is right, correct.

Dhiresh Pathak: So that will then reflect as interest cost and not as minority interest, then why would you put in minority interest, there would be no minority interest on this, right because they do not own an equity, they own a debt instrument on which they are getting interest?

Anurag Kalra: No, you have to look at the minority interest from the perspective of the FHTL P&L, so FHTL has a certain revenue, it has a certain income, it has a certain expense and the net of that is an FHTL profit or profit after tax. Now if FHTL has a profit after tax, 49% of that PAT will have to be treated as minority interest.

Dhiresh Pathak: No, but if you look at FHTL as an SPV then what we are saying is that the 49% economic interest is through a debt instrument and not through an equity instrument and that you are remunerating the debt holder through an interest cost, then there should not be minority interest, right?

Gagandeep Bedi: So let me explain to you, we are picking up 51 stake of FHTL which is a company, now with that we are able to consolidate FHTL's P&L and balance sheet into our books, so by consolidating the P&L we get the total let's say 200 crores of EBITDA into solidated P&L of Fortis. FHTL per say needs to pay out what Anurag was referring to as an interest for the instrument which is the payout of the interest, and FHTL to another related party which is another entity of RHT. And going down, still out of the P&L the minority interest will need to be adjusted and thereby getting you the net PAT after minority interest at 50.

Anurag Kalra: So Dhiresh, let me just add to what Gagan is saying and that will really clear up things, what was happening was that while 51% legal ownership is with Fortis Healthcare, 49% legal ownership is with RHT or FHTL. 100% economic interest was with RHT, so what we have done by 51% economic interest we have got 51% legal and economic interest which is equity and economics and RHT has 49% equity and economic interest. That is what we have done. So once they have equity and economic interest, that economic interest was transferred to them at the time of the IPO in the form of management control which was now getting extinguished so we have 51% economic and equity interest. And since they are now owners of 49% both economically and equity wise, there is a minority interest there as well and I think we can explain this to you once this call is over because it flows through the entire structure and take you through that.

Dhiresh Pathak: And then it adds 50 crores to the PAT, you mean after minority interest it adds 50 crores?

Anurag Kalra: Yes That's PATMI.

Dhiresh Pathak: And these CCDs, they are like perpetuity or they convert into equity at some point, although it will not change the economics, but what is the nature of these CCDs?

Gagandeep Bedi: So it is 18-year maturity.

Dhiresh Pathak: And the coupon is what?

Gagandeep Bedi: So there is coupon is basically, just to remind you the coupon is basically a structuring angle because it is a way of servicing the fees there, the coupon is about 17.5%, but that is purely from structuring perspective, one should not interpret it otherwise.

Dhiresh Pathak: So we will have to maybe explain this better.

Gagandeep Bedi: Yes, of course.

Dhiresh Pathak: And then again because why this, I think you alluded to some approvals not coming through or something right, that is why you needed to do this, that was the reason?

Gagandeep Bedi: As Anurag has mentioned, I think that we can have an appropriately detailed conversation around this because there are complexities behind it. But having said that, at a simplest level there are two hospitals that sit in FHTL that were being held by the trust, we have brought back 51% economic interest in them. The purchase price net of the dividend that is coming our way because we have 28% holding in RHT is about 750 crores. The 750 crores is going to be funded by cash in our book and liquidation of some assets that we have, so we believe that we can manage it, we may have some temporary debt for a very brief period of time but we believe we can self fund it. With these two facilities, with these two hospitals there are a couple of debt instruments that are there which is at 300 crores - 400 crores which Anurag referenced earlier, but the cost of that debt is factored in the 200 EBITDA number and the 50 crores PAT number. So net of everything after self funding, after servicing the debt, the business is looking at a 200 crores improvement on EBITDA and 50 crores improvement on PAT, and again a lot of the details are behind it.

Dhiresh Pathak: No, that is helpful, I was just asking on a more underlying philosophy basis that as you keep generating cash, one way would be to keep buying these properties back and they will always look better on the PAT accretion, but that will end up leading to an old Fortis wherein you owned the asset and balance sheet was heavy and all those things and later you talked about making the balance sheet clean and having asset light. So I am just asking that was this is a one-off transaction or as you generate more cash and you keep talking about PAT accretive, you keep on going buying back the assets from RHT?

Bhavdeep Singh: Yes, listen, right now this is all we are doing right now, because based on everything that you have heard we said just now that it makes good sense, there is nothing beyond that that we are considering at this time. The only thing we are thinking about is how to take care of our patients and our hospitals every day.

Dhiresh Pathak: But why then you know, again this is coming back to the square one, we wanted to be an asset light company, again we will be an asset heavy company.

Bhavdeep Singh: No, we are not, our strategy remains intact, when you articulate a position, any company articulates a position that we are going to be asset light, that is exactly the focus that we have. This is a opportunity that came up, we have taken advantage of it, we move on but we are asset light is exactly the road we want to move and we are moving towards, we have held to that for the recent quarters and we plan on holding to that as we going forward. What I would suggest is, please reach out for Anurag and have a detailed conversation, we are happy to do that, but I will tell you that the fact, while there is a lots of details and lots of numbers and things that we can share with you, at a high level it is everything that I have articulated in the last 60 seconds, this is a good outcome for us.

Moderator: Thank you. Our next question is from the line of Nitin Agarwal of IDFC. Please go ahead.

Nitin Agarwal: My question is on the business, when we look at the hospital business for the nine months this year and as a way it has been tracking, the revenue seems to have slowed down quite a bit and we have not seen any material improvement in the EBITDA also. How do we look at the trends in the underlying business?

Bhavdeep Singh: I think that the trends in the underlying business are solid and they continue to show progress. But what we feel is we have seen what happens in quarter three every year in the healthcare industry which is the elective surgeries, planned procedures, if you have a trauma situation it does not matter whether January 1st or October 15th you go to the hospital, you go to the doctor, if you do not fell well you do that. But when it comes to plan, a good chunk of our business is planned, it is elective and by virtue of that those things do not happen around all the time because everybody wants to be. So the nine months I think the comparison to look at is year-on-year where we are looking at high single-digit approaching 10% growth when it comes to revenue, EBITDA and margins have gotten slightly better than last year, we have done some rationalization, we are making some structure changes to eventually run a better organization, we are looking at the come which we have to get out of the system but I think that the business is on solid footing. I think the more appropriate look would be where are we quarter-on-quarter against last year, if you look at quarter two numbers it was a very good solid quarter and we are anticipating certainly good quarter four as well. I think three is just you had Sanjeev Vashishta allude to it in the pathology business it is the same thing and in our business as well, it is a little bit of dip there but I think that the underlying trends and when we visit our hospitals doctors adopt it, when we see the patients inside our OPDs might certainly think that the trends are solid and will continue to do well.

Nitin Agarwal: So on the existing network, what do you think is a sustainable growth on the revenue line over the next two to three years?

Bhavdeep Singh: We believe that we are looking at low double-digit growth, high single-digit low double-digit, so anywhere between 9% to 11% I think is absolutely sustainable, I think we can do better but I think ongoing for the next sustainable three, four, five years that is our plan and we certainly think that our program will run themselves to that as well.

Nitin Agarwal: So early double-digit growth on the base business as it is and what pace do you see addition happening as far as the new capacities are concerned where we have got 4500-odd beds right now operationally, how do you see those number of beds changing over the next three years?

Bhavdeep Singh: We think that our bed count as you rightly said we are sitting at 4500 beds, within the four walls of Fortis without adding a single hospital we can go to 9000 beds, we are planning based on the requirements of a very specific hospital. So for example, in Shalimar Bagh we are building a oncology block right now, in two or three of our hospital we are building mother child centers, we are looking at expanding and building better capacity in our Jaipur hospital. So I would tell you that ongoing we forecast and project that we should see 10% to 15% better growth, again for the next four, five years and again we may very well add as we go forward but right now because it is strictly Brownfiled and strictly adding to the existing, we can get to 9000, the plan is to do that over the next four five years with a growth of 10%, 15% incremental every year driven by medical programs.

Nitin Agarwal: And lastly, Anurag you mentioned about 750 crores the addition debt which is going to happen with transaction, plus I guess with the transaction we will be buying out the minority stakes in the Escorts units, so that is another 360-odd crores of debt, means how do we see debt really ending up by the end of FY16 and FY17?

Bhavdeep Singh: We are not adding 750 crores debt, what we said was that the 51% economic interest that you have heard reference a couple of times, the cost is that the total cost is 970 crores, there is a 28% holding that we have in RHT, RHT has announced that they are going to be declaring a dividend with the proceeds from this transaction. Our share of that will bring our cost for this 51% economic interest in that 750 range, that is not debt we have, 500-odd crores cash available and our plan is to liquidate some assets and for the most part self fund this, so we may see a temporary increase in debt but in the range of 150 crores to 200 crores but very temporary, ongoing we see this being a self funded transaction.

Nitin Agarwal: Can you throw some more light on how do you propose, in terms of the asset liquidation that you referred to?

Bhavdeep Singh: Any organization when you look at your portfolio where there is a location that land we may have purchased at some point or some investments that we have made in other organizations, so we are looking at to recognize appropriate, nothing specific that we can share at this time, but we are comfortable that this is something that we can do and we are investigating this too as we speak.

Nitin Agarwal: And lastly, what would be the CAPEX that we would have done by this year on Fortis' books?

Bhavdeep Singh: In a range of about 150 crores and that is a combination of medical CAPEX, civil CAPEX, some general upgrade IT, we continue to upgrade our IT systems, so in the range of 150 crores.

Nitin Agarwal: For the nine months?

Bhavdeep Singh: Yes.

Moderator: Thank you. Our next question is from the line of Pritesh Chedda of Lucky Investment Managers. Please go ahead.

Pritesh Chedda: Sir, can you give some color on the EBITDAC margins on the hospitals business over the next three to five years considering that the incremental bed addition can be Brownfield in nature, so the way you gave an aspirational number in the diagnostic side of the business, what possibility of EBITDAC margin is possible in the hospital side?

Gagandeep Bedi: From the hospital side, looking towards the long-term moving towards the 20%.

Pritesh Chedda: And what will be the drivers of that 20%?

Gagandeep Bedi: So a couple of drivers, basically of course the operational drivers being specialty mix, the way we do more of surgical work versus there is a bed mix, more of ICU beds versus ward beds, a pair mix, you go towards a higher price realization payers depending on individual hospitals when they reach a peak occupancy they make those choices and of course cost management coming. Those four primarily would be the key levers driving and of course the revenue growth that needs to come with it.

Pritesh Chedda: Sir I have a little bit confusion here, whatever industry reports that we would have read across or data that we would have collected generally a matured hospital has an ability to reach about 20% - 21% margin and when I am comparing your numbers with the peer number, the peer number let us say the peer number also report a 20% - 21% margin but there is some reporting differences is the doctors fee part and if you tend to adjust that then your number and his number is similar at about 21%. So is there anything that I am missing in terms of analyzing it and second, when you said 20, so I hope you guys are catching on where I am coming from, I could not understand…

Gagandeep Bedi: So you are right, I think you refer to basically the doctor fee being shown as net revenue thereby as a percentage margin so it shows higher margin.

Pritesh Chedda: Yes, it looks 21.

Gagandeep Bedi: So you have to add back to compare apple-to-apple.

Pritesh Chedda: Yes, so when I am doing that in your case also it is 21% today at 72% utilization number and you have never gone above 74% for a fairly long time, so considering that if you could share some light on that margin number.

Gagandeep Bedi: No, I did not get you, so what are you saying, you are saying that if you compare us or you put the doctor…

Pritesh Chedda: So if you do apple-to-apple comparison, your margin today is 21%.

Gagandeep Bedi: No, our margin today is 14.7%.

Pritesh Chedda: That is because the gross number includes the doctor fee?

Gagandeep Bedi: Yes.

Pritesh Chedda: If you net it out it becomes 21?

Gagandeep Bedi: Approaching, yes.

Pritesh Chedda: Now matured hospital, whatever literature we have read, the matured hospital has 21% margin, so is that that today if I look at net of you are already 21% and the margin cannot expand.

Bhavdeep Singh: Let me comment on that, what you have read and the data points that you are referencing are absolutely right but this really talks about an average, this talks about where most hospitals land, the reality is that when you start looking at hospitals like a Gurgaon hospital or a Mohali hospital or similar, some of these hospitals you are going to be driving home a high return with respect to bottom-line, that is number one. Number two is, that as we look forward, one of the reasons that Gagandeep has mentioned what he has in terms of margin and the growth opportunity is that as we continue to sweat our system because the most mature healthcare system in the country is 10 - 15 years old and we believe there is an opportunity to build additional efficiency to drive cost out of this system while continuing to support our doctors and nurses. So I think that while the numbers you have mentioned are directionally correct, we are going to have and we have had, we have had hospitals that are in fact as high as 27% - 28% and so I think the numbers are exactly right, I mean the net will be that it will be a bit higher but that is gist of it, so I hope that answers your question and again we continue to look forward with those anticipations.

Pritesh Chedda: So basically I should take home the message that the EBITDAC margin which you are reporting today at about 14% - 14.5% has the probability to go up to 20% over the next four, five years?

Bhavdeep Singh: Yes, that is exactly right.

Pritesh Chedda: Right, that is the message that I should take home.

Bhavdeep Singh: Absolutely.

Moderator: Thank you. Ladies and Gentlemen, that was our last question, I now hand the floor back to the management for closing comments. Over to you, sir.

Bhavdeep Singh: Thank you all very much, we appreciate you joining the call. Clearly there is a lot of interest in the FHTL transaction and again we are happy to make ourselves available as appropriate to share additional details. Having said that, the high level point that we have shared with you as a couple of you have asked about it, really come down to the fact that for the amount we mentioned 750 crores that we are improving our bottom-line in a significant way. So we feel good about it, I think as far as the business is concerned third quarter blues which a lot of the industries have in India as well and we certainly believe that as we roll into quarter four the numbers will ramp back up. So Thank you very much for your time, thank you for your support and we look forward to staying in touch with all of you. Good Night.

Moderator: Thank you members of the management. Ladies and Gentlemen, on behalf of Fortis Healthcare that concludes this conference. Thank you for joining us and you may now disconnect your lines.