

"Fortis Healthcare Limited Q3 FY19 Earnings Conference Call"

February 13, 2019





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FORTIS HEALTHCARE LIMITED

MR. GIRISH GUPTA – CHIEF FINANCIAL OFFICER,

FORTIS HEALTHCARE LIMITED

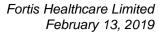
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MR. SAURABH CHADDHA - CHIEF FINANCIAL

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Moderator:

Ladies and gentlemen, good day and welcome to the Fortis Healthcare Limited Q3 FY19 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode. And there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference, please signal an operator by pressing '* and then '0' on your touchtone telephone. I now hand the conference over to Mr. Anurag Kalra - Head, Investor Relations. Thank you and over to you, sir.

Anurag Kalra:

Thank you, Raymond. A very good evening, ladies and gentlemen. Welcome to Fortis Healthcare's Q3 FY19 Earnings Call. The call today is being chaired by Mr. Bhavdeep Singh – CEO, we have with him Girish Gupta – Chief Financial Officer. From the SRL Team we have Mr. Arindam Haldar – CEO of SRL, and with him is Saurabh Chaddha – CFO of SRL.

We will begin this call with some opening comments by Mr. Bhavdeep Singh on the quarter gone by. I will then request Arindam to make a few comments on the diagnostics business. Post which I shall take you through a summarized presentation of our financials. We can hen open the floor for question-and-answers. Over to Bhavdeep.

Bhavdeep Singh:

Thank you very much, Anurag. Good evening, everybody. Want to just apologize for the delay, just had a little bit of a glitch getting our results uploaded. But nonetheless, here we are, and again thank you for being here as well.

So, as you all know, it has certainly been an event full two, three quarters for us and this past quarter was no different. Actually, I suppose it was different with respect to the fact that I believe that the team is stabilizing the organization, the business is back on steady footing, the numbers continue to get better, and we will talk about that in a couple of minutes. And I can tell you that generally speaking with 25,000 employees I think there is certainly an uptake in terms of how we look at the business, how we look at the organization. I think, in general, that would excite me by the organization. I think all that bodes well.

Two, three very significant things, obviously, took place. Obviously, you are aware of the transaction being completed by IHH and new board members coming onboard, which we all see as a positive. The other big news that took place in December, at the end of the month, was the completion of the RC transaction. That is something that has been in the works for quite some time now, and really glad on multiple levels to see it come to fruition.

And while Anurag will go through the financials in a few minutes, at an overall level this brings in savings from a cost perspective and a cash perspective, somewhere between Rs. 270 crores to Rs. 280 crores, and that is a significant shift from the business. And that is a positive thing.

If you look at what is happening out, I will talk more about the Fortis business. Arindam will give you an overview of the thorough diagnostics business. Our EBITDA margins crossed 11% which was an improvement over 9.5% over quarter before. Our occupancy was sitting at about 68%, the prior quarter was slightly better, and that is a function, we discussed this last quarter,



a function of a little bit of fever and H1N1 and dengue which we know happens every year. The other thing that impacts our occupancy is the fact that November, with Diwali being a seasonal month, and you are all aware of the fact that there is an impact on business. And what really happens around Diwali time is while the critical issues continue, all the elective work basically comes to a stop. So joint replacement, knee replacements, any elective surgery, any elective procedures, most of things come to a grinding halt for a bit of time.

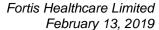
I think if you look at some other key indicators inside the business, RPOB, revenue per occupied bed is at Rs. 1.5 crores, Rs. 1.52 crores actually which places us at very-very top. And it is a very strong number, even I think by quality clinical programs in our hospitals and just some outstanding doctors, and I think the work we are doing clinically is par excellent and among the very best in the country.

If you look at our length of stay, we are at about 3.4 days. Most of our competition is above that and I think obviously the lower the number they are the better. So, if you look at RPOB, if you look at occupancy and if you look at the length of stay, I think we are seeing positive movement in all three, and that certainly bodes well with respect to where we are headed. I think if we start looking at the future, again, the EBITDA number that came in, EBITDAC number that came in for the quarter, we sit at Rs. 100 crores. Q1, you will recall was Rs. 42 crores, Q2 was Rs. 88 crores and now we are at approximately Rs. 100 crores, so the growth story that we committed to and talked about when we launched our Build Back Plan back in May, June, is very much on track and continues. And we believe that the growth story should continue going forward as well.

I can tell you that inside the organization when we look at our clinical program, well, ultimately it comes down to good clinical activity, good clinical excellence in our hospitals. We are moving forward and the number, the volume that we are doing in terms of organ transplant is very significant, the number of joint replacements we are doing, the number of angioplasty. So, across by clinical specialty up and down, up and down the entire spectrum the organization continues to do well.

Now, looking forward, we continue to see some good performance in some of our larger hospitals. The FMRI hospital had a very good quarter, the business continues to rebound FY12. Escort is showing some improvement as well. So, I think generally speaking, all the indicators and all the hospitals, I think are at least moving in the right direction and that is an important step for us to be taking at this time.

So, that is where we are. Good progress, stabilization that we talked about continues, the organization continues to be on better footing. And look, one of the things that I wanted, which was very important to me and all of us was that make sure that the organization stabilizes and starts to grow, and that is exactly what we are doing. So the run-rate is good. And I believe it will lead to further growth and further improved results as we go forward.





So, on that note, I will ask my colleague Arindam to give overview of SRL, and then Anurag will walk you through some financials.

Arindam Haldar:

Thank you, Bhavdeep. At SRL, I will just make a few quick comments. At SRL we are completely focused on building back the business from the past challenges. And essentially we are focused on the basics. We remain the most doctor-preferred lab in the country. And that we have done in the last quarter is dialed up, our engagement with the prescribing doctor via the Doctor Connect program that we have. We have conducted more than 130 medical conclaves in quarter three, touching almost 2,000 doctors. And this is a number that we do almost over eight to nine months, so we have dialed it up more than double in quarter three. And those are activities which we are going to give us benefit in coming months.

We have also improved efficiencies and process control across the value chain, which has helped us maintain our EBITDA margin despite lower than expected revenue growth. The like-to-like revenue growth for the quarter is about 3%, while the reported growth is 1.6%, taking care of some of the large businesses like UP PPP, which we shutdown beginning of the financial year. We are also deeply engaged in finding higher synergies with both our hospital business and rest of the IHH network. And we believe that that can give a significant gain.

In the quarter we have also expanded our franchise network of sample pickup points and these are coming up and these will again give us higher accessibility to patients, leading to better growth in future.

Anurag Kalra:

Thank you, Arindam. Ladies & gentlemen, I shall now take you through brief financial presentation. I will just mention the numbers of our group consolidated P&L for the quarter FY2019 and then for the nine months FY19.

At the operating revenue level, our total revenues for Q3 FY19 stood at Rs. 1,103 crores, this comprised of the hospital business revenues at about Rs. 889 crores and the diagnostic business revenues at about Rs. 209 crores. Both the hospital and diagnostics business were marginally lower versus the corresponding previous quarter.

At the operating EBITDAC level, our operating EBITDAC margins for Q3 FY19 stood at 12.4%, a number of Rs. 136.6 crores. This compares to a number of Rs. 152.6 crores in the corresponding previous quarter, a margin of 13.6%, but versus the trailing quarter the margins are broadly in line. In Q2 FY19 we were at 12.5%, in Q3 we are at about 12.4%.

Our net BT cost stood at Rs. 68 crores versus a similar number of Rs. 67 crores in the corresponding previous quarter. As you would know that in mid-January we completed the acquisition of RHT Assets, and hence this number going forward will be significantly lower. This piece will only come for the first 15 days of January and then going forward this number will be significantly lower, so no net BT fees going forward.



At the operating EBITDA level, we registered an operating EBITDA, post the net BT cost, of about Rs. 68 crores compared to a number of Rs. 85 crores in the corresponding previous quarter and a number of Rs. 75 crores in the trailing quarter. Our other income was significantly up, our other income stood at Rs. 45.3 crores in Q3 FY19 versus about Rs. 33 crores in the corresponding previous quarter and Rs. 13 crores in the trailing quarter. This is largely due to the utilization of the funds that IHH had infused till the time we were able to consummate the RHT transaction.

At the EBITDA level, after accounting for other income, for Q3 FY19 the numbers was at Rs. 113.6 crores versus a number of Rs. 118.2 crores in Q3 FY18. Our finance cost showed an increase, our finance cost for Q3 FY19 stood at Rs. 111 crores versus a number of Rs. 63 crores in Q3 FY18, and a number of Rs. 84.6 crores in Q2 FY19. I would like to point out that this was largely due to certain one off costs related to pre-closure and other charges for certain high-cost debt that we had taken over the last few months, those were paid off, there were certain charges related to that, and hence the finance cost, there are certain one offs in this finance cost and that is why you are seeing a higher number. This, obviously, will not be there going forward.

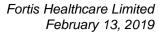
On the depreciation and amortization front, it is a Rs. 60 crores number versus a similar number in the corresponding previous quarter. PBT before FOREX stood at a negative Rs. 57.5 crores versus a negative Rs. 4 crores in Q3 of FY18 and a negative Rs. 53 crores in trailing quarter.

After accounting for exceptional loss, tax expense, our PAT before minority interest and share and associates was a negative Rs. 197 crores, I think this was largely because of an exceptional loss of Rs. 158 crores, which is related to impairments of goodwill and of certain assets. These also include certain off-offs, financial and legal expenses related to advisory fees for the corporate transactions that we have done over the past few months. So there is a one-off in this number of about Rs. 158 crores, which is leading to a loss of about Rs. 197 crores for Q3 FY19. This compared to a loss of Rs. 31 crores in the corresponding previous quarter.

After accounting for our share and associates, share and associates is our share of profits in Associates Investments in Mauritius, Lanka and RHT. Our PAT after minority interest in share and associates was a similar amount, amount of Rs. 37 crores in Q3 of FY18.

Coming to the group consolidated P&L for the nine months of FY19. Operating revenue, comprising both the hospital and diagnostics business was lower by 5%-odd. Operating revenue stood at Rs. 3,285 crores versus Rs. 3,474 crores. Our operating EBITDAC margins for the nine months were at 10.9% versus a number of about Rs. 14.8%. Our operating EBITDA, after accounting for other income our EBITDA stood at Rs. 228 crores versus a number of Rs. 420.8 crores compared to the corresponding previous period.

Our PBT before FOREX, after accounting for depreciation and amortization and the higher finance costs, for the reasons I explained a while back, stood at a negative Rs. 216 crores versus a number of Rs. 48.5 crores for the period nine months ended FY18. Our PBT before exceptional





Moderator:

items was again a negative Rs. 204 crores versus a positive of Rs. 13.3 crores for nine months FY18.

PAT after minority interest and after share and associates after accounting for exceptional loss that I had explained a while back, stood at negative Rs. 434.5 crores versus a negative Rs. 77.2 crores. having said that, I think despite this being a seasonally low quarter, both the hospital business and the diagnostic business has shown steady improvement.

The hospital business margins have been flattish versus the trialing quarter. On a nine months basis the diagnostic business is still at 19.9% margin. We believe that with the acquisition of RHT, the financial performance is set to improve. The business has reached levels of normalization and stabilization. And we do expect that in the ensuing quarters we will see a progressively improving performance.

With that, I come to the end of the financial presentation. And open the floor for question-and-answers. Thank you.

Sure. Thank you very much. We will now begin the question-and-answer session. We have the

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

Neha Manpuria: My first question is on the occupancy. While I understand that the December quarter has seasonality, it seems like we are trending below our guidance of at least 70% occupancy for even

the fourth quarter. Have we not seen the pickup of these sort of planned surgeries, etc, into this

quarter?

Bhavdeep Singh: No, I think Neha, as I mentioned, the Diwali seasonality component, as I mentioned, there is a

significant drop. I can tell you in one of our hospitals where we do a fairly healthy number of joint replacements to the tune of two, four a day, for seven, eight days leading up to Diwali we did not even do one. Because I think at that point nobody wants to be sitting and hobbling around or be in bed during holiday time. So there is a significant drop that takes place then. I think if you look at the numbers outside of that, we are, broadly speaking, on track with what we had

said and we are approaching the 70% number. We are not at 70%, we are approaching it, but I

do not see it as a major miss or anything that we said before. I think the key piece here is that

somewhere we were where we have come, and how we see it moving forward.

Neha Manpuria: So my question was on the current quarter, in the Jan-Feb of this one, it seems like occupancy

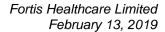
remains flat versus the last quarter. So I was just wondering if you have seen the pickup in occupancy post drop-off in the festive season, because the number does not seem to indicate

that?

Bhavdeep Singh: Yes. So, I would tell you that we have shared the January number, January was at about 56%,

February right now it is early, but I do not want to comment occupancy 10 days or 15 days into

the month. But I can tell you, we are very much hovering around 70% number as far as where





we stand right now. So, again, I think that plus or minus 100 basis points, 120 basis points, I think we are broadly there. I do not think there is a slippage here at all, I think it may be, quite honestly, we may be stabilizing at 68%, 69%, 70% range, but I do not see us going backwards at all. I think we are going at the spot that we said we would be.

Neha Manpuria:

Understood. And also on the one-offs in the quarter, again, what was the goodwill impairment again in this quarter for? And could you also quantify the other one-offs, in the interest cost and the legal charges, how much were they in the quarter?

Anurag Kalra:

As far as interest cost was concerned, we basically retired some high-cost debt which was taken in the earlier part of 2018. So, we retired that debt and there were some charges for prepayment of those items. So, effectively, one off charge was there from a finance cost perspective. And in terms of impairments which we have taken for goodwill, because of IHH coming on board, we thought it prudent to sort of do a testing for certain businesses and where ever applicable we took a goodwill impairment for those businesses.

Neha Manpuria:

Sir, I was wondering if you could quantify the higher interest cost and the legal charge, how much were they in the quarter?

Bhavdeep Singh:

So, Neha, broadly the interest charges, the higher finance cost was close to about Rs. 30-odd crores. And the financial and legal expenses was of similar nature.

Neha Manpuria:

Okay, understood. And SRL, in this quarter, while I understand there is a seasonality component, etc, but given our growth rate is so low, it is surprising to see that realization has come off, average realization for SRL has come off. Are we, I mean, is there something in terms of competition cutting prices which is impacting us, therefore, hurting growth and reflected in our margins? I mean, there is no reason for realization to have come off in the quarter, right?

Arindam Haldar:

Neha, so our realization for the quarter is marginally ahead of the realization that we had in quarter three. And typically what also happens is, the realization also goes a little bit higher and lower based on the mix that happens. There hasn't been any significant change of pricing of any of our test. So primarily, it is a function of the mix of test that is there.

Moderator:

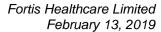
Line for Ms. Manpuria seems to have dropped off. We wil lmove to the next question. The next question is from the line of Aimee Truesdale from Jupiter. Please go ahead.

Aimee Truesdale:

Just one, would you be able to clarify where we are with this open offer and the Supreme Court order? And what the next steps there are, please?

Bhavdeep Singh:

Aimee, the Supreme Court hearing is scheduled for the 15th of February. We will provide you an update only post that. We are trying to do it in an expedited manner, this has been for quite some time. As you would have seen in the presentation that we have shared with you, the funds required are put in an escrow. We want to do it quickly. And the funds required are there in the





escrow from November onwards, but we will have to wait for what the Supreme Court says. And the next hearing is scheduled for 15th.

Moderator: Thank you. Our next question is from the line of Sarvesh Gupta from Maximal Capital. Please

go ahead.

Sarvesh Gupta: Just one thing, I could not understand the one off part, so can you just quantify the one off part

in this P&L above the net profit line, which is Rs. 90 crores of loss. So, above that what is the

one off?

Anurag Kalra: Sarvesh, where are you taking this Rs. 90 crores number from, please?

Sarvesh Gupta: From the consolidated unaudited financial results for Q3 FY19.

Anurag Kalra: Sarvesh, so what we have done is in the consolidated results you would have seen an exceptional

loss of Rs. 127 crores, which primarily relates to, as Girish was mentioning, primarily relates to impairments of goodwill and of certain assets. In addition to that, like I mentioned before, we also have one off financial and legal expenses which were related to the corporate transactions. So when you look at the investor presentation, the total of that is about 157 above that you should

go well.

Sarvesh Gupta: So, when we see a Rs. 90 crores loss from continuing operations, this Rs. 150 crores is already

considered in this Rs. 90 crores loss? So point number #5 if you see, net profit from continuing

operation before share in profit of associate is Rs. 90 crores of loss, correct?

Anurag Kalra: Yes.

Moderator: Thank you. Our next question is from the line of Shyam Srinivasan from Goldman Sachs. Please

go ahead.

Shyam Srinivasan: Just on the operational performance of the hospitals, I think the press release also talks about

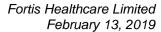
improvement in some of the hospitals like FMRI, Mulund, I think some of the other hospitals. So, what are we doing in terms of profitability improvement on a sequential basis for some of

these hospitals? Can you just outline this please.

Bhavdeep Singh: Sure. So, couple of things. As you rightly said, we have seen improvement in the FMRIs of the

world, the Mulunds of the world, the BG Roads of the world, even Escorts has shown an improvement as well. I think there are three or four things, number one is driving a well balanced patient flow. And we rely on our doctors, we take a great deal of pride. You have heard me say many times, Shyam, but the capability of our clinicians and the medical programs that we have in our hospitals. So, first and foremost is around medical program and the doctors that we have, that is number one. I think the second piece is, we are looking in our system around when we

talk about profitability, we are looking at all of our cost very thoroughly. The reality is that we





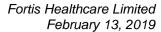
have an opportunity, we have talked about the fact that we need to get 200, 300 basis points in cost in our system. And so we have made some strides and progress in terms of managing our cost and having an improved outcome there. The third thing is that, just the general mix of business. One of the things that has impacted, as I mentioned, is the whole Diwali period, so I think there has been a bit of a challenge there. But I think that maximizing the mix and building some of the more complex medical programs has been helpful as well. And then you look at the various payer platforms that we have, so our international business has done exceptionally well. In fact, I would tell you, the last two, three months have been some of the strongest the company has had in business. And some of the work that we are doing with our corporate business as well is supporting some of these good initiatives. So, I think Shyam, I do not think it is any one thing, I can tell you that broadly speaking that is a good clinical platform, good clinical program, good doctors, good outreach program reaching out. But I think overall the whole efficiency component and cost management component is playing a key role in terms of what we are doing.

Shyam Srinivasan:

Bhavdeep, just on this cost efficiency. So, you talked about 300 bps, I think you have given this number in the past as well. How much has been achieved? What needs to be further done? Is it going to be more back ended in FY20? If you can give us some thoughts there.

Bhavdeep Singh:

I think we have done some good work on cost management. The challenge is that by virtue the experience that the organization had this last year, our top-line has taken a bit of a hit. I can tell you that from an efficiency perspective I think we are more efficient than we have been. We use the Fortis Operating System software where we track over 200 patient relating activities in terms of efficiency, in terms of patient care, in terms of customer service. So I would tell you that probably 30%, 40% in terms of what we need to do. Having said that, we are in an industry and we are in a business environment where the things on ground are changing very-very quickly. So, quite honestly, while I think, wherever we started, we might have achieved 50%, 60% of our goal, but the dynamics being what they are I think there is still a long way to go in terms of how we get more efficient and have a more profitable environment. So we start looking at operating cost with respect to looking at more centralized facilities, whether it is food and beverage in our NCR market place, we centralize, we are using a central kitchen to support four, five of out hospitals, we are doing the same thing with laundry as well. I think we have an opportunity to do that in other markets where we have a multi-hospital presence. I think when we start looking at equipment utilization, we are closely tracking what percent of the time, so whether it is a cath lab, whether it is OT or whatever else it might be, what kind of utilization we have. I think we are starting to look at our medical programs in terms of medical strategy and what kind of work do we do in one hospital versus another. So while I think, Shyam, that I think from where we started I think we have made some good headway. The reality is that the size of the pie continues to get bigger and bigger and I think there is a big opportunity that is out there. And I think we have to get much more updation. So, the number hasn't changed quite honestly. I think if we hadn't done anything the 200, 300 points would have been 500 points today. But I think there is still another 200, 300 points and I think we have to get that much more efficient.





Shyam Srinivasan:

Got it. And my last question is on SRL, all the companies that have reported so far, Dr. Lal or Thyrocare, we have seen kind of a slowdown in all their growth. You have been slow for maybe a few more quarters than them. So, just wanted to understand from an industry perspective, are we moving to a lower gear here in terms of industry growth or is it something that you think will kind of reverse and come back in FY20?

Arindam Haldar:

What you are saying is right. At a very broad level if you look at listed here and track the growth rate over the last seven or eight quarters, there is a slight decline. However, it is too early to say that diagnostic business at overall level will settle at a far lower growth. Yes, there is a slight decline and that is true for all the competitors. However, fair to say that I do not see there will be any recession in this, if one was talking about the industry growing at a higher teens, I guess it is more towards the lower side of the teens, that probably is the difference. But I do not think that so called relative slowdown is a permanent thing.

Shyam Srinivasan:

Arindam, just to follow-up, is the pricing the main challenge here or is it too many players, what is the key challenge that the industry is facing today?

Arindam Haldar:

In terms of industry pricing and you may have heard from others as well, the primary growth that as players that we are getting in the industry is primarily because of volume. We have not been able to take any price action in the last couple of years, and that is to do with competitive nature of the industry. And that is true for SRL and many of our listed peers.

Moderator:

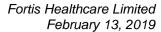
Thank you. Our next question is from the line of Neha Manpuria from JP Morgan. Please go ahead.

Neha Manpuria:

Sorry, I got dropped off the call. One other follow-up, IHH has been now on board for a couple of months. How has the entire process gone? I mean, what is the feedback that you have got, are you sensing some sort of disruption per se or concerns on the ground in the Fortis operational level? Any color there would be appreciated.

Bhavdeep Singh:

You probably heard earlier what was referenced was a 100 day plan. And I think that we are on course we are just about at the tail end of that 100 day plan. And part of the 100 day plan, by the way, was the RHT acquisition, obviously, which is completed. And so healthy amount of funds have been injected in the company. So, let me step back for a second, one of the things that we did was that we actually formed a group of people who we actually worked on, because we are a subsidiary of IHH in terms of what that looks like, in terms of 100 day plan, and what the various initiatives that came out of there. I can tell you that look we recognize, I think we take a great deal of pride at Fortis in terms of who we are, what we do, how we take care of our patients, how we take care of our employees and what the brand represents. Now, while the brand has got beat up, over the recent past we still think we have a pretty cool thing inside Fortis Healthcare, and we are very proud of that. Having said that, we are also very respectful of the fact that IHH brings with them tremendous credibility, very strong credentials and a very outstanding track record of success. So, I would say to you that I think that it is too early for me to say that we are





all sitting in nirvana. But what I can tell you is that there is a huge level of optimism, I think that we are seeing is some good solid positive indicators, I think the fact that the IHH organization has made, the kind of investment they have made; and look, there is no secret, we had some challenging times, they are standing strong and standing with them side by side. I think there is a high level of optimism, I think that early indicators are that things are going to be a huge winwin. And whether we look at things like medical programs or we look at equipment utilization or we look at something as simple as patient service model, I think there is a lot for us to learn, a lot of things that we can benefit. And I think quite honestly I think we have things to offer IHH as well. So, I would tell you Neha that 100 days in, things are on track and I think there is generally a very positive attitude and people are feeling quite optimistic about where we go from here. So, looking good. I would imagine that three months from now I will give you a better update, but I imagine it will be very much along those lines as well.

Moderator:

Thank you very much. As there are no further questions, I would like to hand the conference back to the management team for closing comments.

Bhavdeep Singh:

Thank you very much, operator, we appreciate that. Thank you all very much for joining. First of all, again, apologies for a late call, but we appreciate you joining us. Look, I think there is a lot of good stuff happening at Fortis Healthcare. We have been through one hell of a ride and we are standing, we are standing firmly with our feet on the ground. And I think the indicators are that the business is back on track and we have lot of good things to look forward to. So thank you very much for your support. We welcome catching up with any of you at any time in the future as and when you'd like. So, look forward to continue with the discussion. Thank you very much and have a good night.

Moderator:

Sure. Thank you very much. On behalf of Fortis Healthcare, that concludes the conference. Thank you for joining us. You may now disconnect your lines.