August 29, 2022

Vijaya Diagnostic Centre Limited: Long term rating upgraded; short term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term/Short-term - Unallocated facilities	34.0	34.0	Upgraded to [ICRA]AA- (Stable) from [ICRA]A+ (Stable)/ [ICRA]A1+ reaffirmed
Total	**34.00**	**34.00**	

**Instrument details are provided in Annexure-I*

Rationale

The rating action considers Vijaya Diagnostic Centre Limited's (Vijaya) healthy scale of operations supported by addition of new centers. The company plans to add 15 new centers in FY2023 which is expected to result in a healthy revenue growth of 10-15%, notwithstanding the subdued revenues in Q1 FY2023 due to decline in revenues from Covid-19 segment. Vijaya's revenues witnessed strong growth of 23% in FY2022 on the back of healthy revenues from Covid-19 related testing as well as growth from non-Covid segments. Strong growth in scale of operations has resulted in healthy growth in earnings in FY2022 as the company continued to command strong operating margins of ~44%. While initial operating expenditure towards new centers are expected moderate the company's margins to an extent in FY2023, overall earnings are expected to remain healthy. The company has negligible external debt aside from lease obligations. This has resulted in strong coverage and leverage metrics with DSCR of 6.7 times in FY2022 and TD(incl lease liabilities)/TNW of 0.4 times in FY2022. ICRA expects the company's capital and coverage indicators to remain strong going forward as well.

The ratings also derive comfort from Vijaya's established brand name with 100 centres primarily in Telangana and Andhra Pradesh and its diversified diagnostic offerings including radiology and imaging, nuclear medicine, conventional and speciality laboratory services and diagnostic cardiology. Vijaya derives over 95% of its revenues from B2C customers which supports the company's margins. Further, the pathology-radiology mix of 65:35 is favourable as compared to other major players which derive higher share of revenues from pathology segment.

The ratings, however, are constrained by the high geographical concentration with Hyderabad accounting for 80-85% of total revenue during the past three years and low entry barriers in the absence of stringent government regulations, resulting in stiff competition in the medical diagnostic industry. Entry of new players and online aggregators offering deep discounts has accentuated the competition. ICRA notes that VDCL would require continued investments in medical equipment and infrastructure to remain competitive and provide quality service in the medical diagnostic industry. Further, VDCL has significant expansion plans in the medium term, primarily towards centre addition. The quantum and the funding mix of the capex plans, along with performance of the new centres, remains a key monitorable.

The Stable outlook on the long-term rating reflects ICRA's opinion that the company will witness a healthy growth and will continue to maintain a healthy financial and business risk profile on the back of its reputed brand presence in Telangana and Andhra Pradesh.

Key rating drivers and their description

Credit strengths

Consistent improvement in revenues and healthy operating margins – Vijaya's operating income has grown by 23% to Rs. 462.4 crore in FY2022 from Rs. 376.7 crore in FY2021. While Q1 FY2023 revenues declined by 14.5% YoY due to a decline in covid revenue by 90%, non-covid revenue increased by 11.6% YoY. Revenue is expected to grow sharply in the medium term aided by significant expansion planned by Vijaya through addition of new centres. Operating margins remain strong at 44.1% in FY2022. It declined to 38.2% in Q1 FY2023 due to lower revenues and incremental expenses associated with upcoming centers for which opex would have started being incurred before scaling up of revenues. However, margins are expected to stabilize over the long term. Margins are healthy vis-à-vis industry as over 95% of Vijaya's revenues are derived from B2C mix of customers which enables Vijaya to build brand loyalty and trust resulting in higher realizations. Further, the pathology-radiology mix of 65:35 is favourable as compared to other major players which have higher mix from pathology segment.

Strong financial profile with comfortable capital structure and coverage metrics – Consistent strong accruals along with low debt levels (excl lease liabilities) has resulted in strong coverage and leverage metrics for Vijaya with Adjusted Debt/TNW of 0.0 times in FY2022. (Total Debt (incl lease liabilities)/TNW of 0.4 times). DSCR remained healthy at 6.7 times in FY2022.

Established presence in medical diagnostics industry – The company has a track record of more than four decades in the medical diagnostics industry. Mr. Surendranath Reddy, the founder of VDCL, is a doctor by profession and started the first diagnostic centre in 1981. VDCL provides a comprehensive range of radiology and pathology diagnostic services and is an established regional player with a wide network comprising 100 centres, mainly in Telangana and Andhra Pradesh, with laboratories offering diagnostic services including radiology and imaging, nuclear medicine, conventional and speciality laboratory services and diagnostic cardiology. Strong clinical team led by more than 200 qualified radiologists, pathologists, microbiologists and other doctors, in addition to over 1,100 qualified technologists, support its operations.

Credit challenges

High geographical concentration – Hyderabad accounts for 80-85% Vijaya's revenue, indicating high geographical concentration risk. The company started its first centre in Himayathnagar, Hyderabad, which remains its flagship centre and reference laboratory, constituting over 15% of operating income in FY2022. However, ICRA notes that the company has built an established brand in Hyderabad diagnostics market on account of its strong network of centers in the city which enables it to have high B2C customer-mix of over 95% and command higher realizations.

Highly fragmented industry with intense competition - The medical diagnostics industry is highly fragmented with presence of many standalone diagnostic laboratories and laboratories within hospitals resulting in stiff competition for organised diagnostic chains in terms of patient volumes and aggressive pricing of diagnostic tests. The low entry barriers in absence of stringent government regulations result in intense competition in the medical diagnostic industry as illustrated by recent entry of players offering deep discounts to capture market share.

Sizeable expansion plans – VDCL has significant expansion plans in the near term, which may constrain the improvement in its operating margins due to the operational expenditure incurred towards set-up of new centres leading to losses during the initial months of operations before revenue from the centres scales up. Further, the company would require continuous investment in medical equipment and infrastructure to remain competitive and provide quality service in the medical diagnostic industry. However, reliance on debt is low due to healthy cash flows over the years.

Liquidity position: Strong

The liquidity position is strong with a robust cash and liquid investment balance of over Rs. 230 crore as of June 30, 2022 and expectations of strong retained cash flows in FY2023. Against this, Vijaya is expected to incur capex of Rs. 100-120 crore while repayment obligations are negligible.

Rating sensitivities

Positive factors – ICRA could upgrade VDCL's rating if geographical diversification of revenue profile leads to significant improvement in scale of operations and earnings, while maintaining healthy profitability and debt indicators.

Negative factors – The ratings may witness a downward pressure if larger-than-estimated capex adversely impacts its debt metrics and liquidity profile or decline in performance of existing centres or ramp up in new centres is slower than expected, significantly impacting operating margins. Specific credit metric that could lead to a rating downgrade includes Gross debt (incl lease liabilities)/ OPBITDA higher than 1.5 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Diagnostic service provider methodology
Parent/Group support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of Vijaya Diagnostic Centre Limited

About the company

Vijaya Diagnostic Centre Limited (VDCL) was founded by Dr. S. Surendranath Reddy in 1981 as a proprietorship concern and was subsequently incorporated as a private limited company in 2002 and listed in the stock market in September 2021. The Company is engaged in the business of providing comprehensive range of diagnostic services spanning across radiology & imaging, nuclear medicine, conventional & specialist lab services and diagnostic cardiology. VDCPL operates 100 centres (as of June 2022) primarily in Andhra Pradesh and Telangana.

Key financial indicators (audited)

Vijaya (Consolidated)	FY2021	FY2022
Operating income	376.7	462.4
PAT	85.1	110.7
OPBDIT/OI	44.0%	44.1%
PAT/OI	22.6%	23.9%
Total outside liabilities/Tangible net worth (times)	0.5	0.5
Total debt/OPBDIT (times)	0.8	0.9
Interest coverage (times)	10.9	12.4

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2023)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of August 29, 2022 (Rs. crore)	Date & Rating in	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020
					August 29, 2022	May 03, 2021	-	March 11, 2020
1	Unallocated	Long-term/ Short Term	34.00	-	[ICRA]AA-(Stable)/ [ICRA]A1+	[ICRA]A+ (Stable) / [ICRA]A1+	-	[ICRA]A+ (Stable) /[ICRA]A1+
2	Fund Based -Term Loans	Long-term	-	-	-	-	-	[ICRA]A+ (Stable)

Complexity level of the rated instruments

Instrument	Complexity Indicator
LT / ST - Unallocated	Not Applicable

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: www.icra.in

Annexure I: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Unallocated facilities	-	-	-	34.0	[ICRA]AA-(Stable)/[ICRA]A1+

Source: *Company*

Annexure II: List of entities considered for consolidated analysis

Direct Subsidiaries			
Sr no	Name of subsidiary	Ownership (%)	Consolidation Approach
1	Medinova Diagnostic Services Limited	62.14	Full Consolidation
2	VDC Diagnostic Karnataka (LLP)	100	Full Consolidation
3	Doctors Lab Diagnostic Centre Private Limited	100	Full Consolidation
Step-down Subsidiaries			
Sr no	Name of subsidiary	Ownership (%)	Consolidation Approach
1	Medinova Millennium MRI Services LLP	100	Full Consolidation
2	Namrata Diagnostic Centre Private Limited	100	Full Consolidation

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

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