July 15, 2017

Fortis Healthcare Limited

Summary of rated instruments

Instrument*	Rated Amount (in crore)	Rating Action
Non-convertible Debentures	250	[ICRA]A+; Rating placed on watch with developing implications
Commercial Paper/Short-term Debt	1000	[ICRA]A1+; Rating placed on watch with developing implications
Fund-based Limits	65	[ICRA]A+; Rating placed on watch with developing implications
Term Loans	104	[ICRA]A+; Rating placed on watch with developing implications
Non-fund-based Limits	10	[ICRA]A1+; Rating placed on watch with developing implications
Proposed Limits	21	[ICRA]A+; Rating placed on watch with developing implications

* Instrument details are provided in Annexure I

Rating action

ICRA has placed the short-term rating of [ICRA]A1+ (pronounced ICRA A one plus) [1] for Rs. 1000-crore[2] commercial paper (CP) programme and Rs. 10-crore non-fund based limits of Fortis Healthcare Limited (FHL) on watch with developing implications. ICRA has also placed the long-term rating of [ICRA]A+ (pronounced ICRA A plus) for Rs. 250-crore Non-convertible Debenture (NCD) programme, Rs. 65 fund-based limits, Rs. 104 crore term loans and Rs. 21 crore proposed limits of FHL on watch with developing implications.

Rationale

The rating action is on account of leverage and liquidity concerns of promoter's holding companies. The promoters, through Fortis Healthcare Holdings Private Limited (FHHPL), have reduced their stake in Fortis Healthcare Limited in Q4FY2017 and Q1FY2018 to bring down the debt of holding companies; however, in the absence of meaningful income from investments/ subsidiaries, the promoter group continues to be exposed to refinancing and stake/asset sales; further, majority of the investments of the group are already encumbered, leaving limited headroom to raise fresh debt. ICRA notes that promoter group is currently in discussion to further divest stake across various subsidiaries (including FHL) to reduce the debt of the holding companies and bring in a strategic partner for the operating companies. ICRA will continue to monitor the development closely and assess its impact on credit risk profile of the company once more clarity emerges.

The ratings take comfort from the improvement in performance of hospital business as reflected by 8% growth in revenues and 7% growth in OPBITDA {before Business Trust (BT) fees} in FY2017. Improvement in revenues and OPBITDA of hospital business before BT fees is on account of higher average revenue per occupied bed (ARPOB), increase in aggregate occupancy of the hospital network and multiple efficiency improvement initiatives undertaken by the company. After business trust expenses, the

1 For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications
2 100 lakh = 1 crore = 10 million

OPBITDA of hospital business grew by ~240% in FY2017 due to above factors as well as the acquisition of 51% economic interest in Fortis Hospotel Limited (FHTL), which led to lower net BT fees and consolidation of FHTL with FHL. The ratings also factor in low leverage (gearing of 0.30x as on March 31, 2017) and significant cash and equivalents (Rs. 938 crore as on March 31, 2017), which provide financial flexibility. The ratings continue to factor in long and established track record of the company in healthcare sector in India, its large and established network of healthcare facilities, its presence across various healthcare verticals, and positive outlook for healthcare services in the country.

The ratings continue to be constrained by the increase in FHL's overall debt levels on account of loans taken to acquire 51% economic interest in Fortis Hospotel Limited (FHTL) in Q3FY2017. Though the acquisition has resulted in improved OPBIDTA, it will adversely impact the cash flow position of the company in short term due to higher interest and debt repayment. Also, majority of the debt taken for acquisition is to be repaid within three years, exposing the company to refinancing risks. ICRA has noted that the company proposes to monetise certain non-core assets to repay this debt; however, the same is subject to market conditions and requisite approvals. Timely sale of these non-core assets will be crucial for making debt repayments and will be key rating sensitivity.

The ratings also factor in the significant outflows towards net BT fee payments (Rs. 371 crore in FY2017) made to Religare Healthcare Trust (RHT), which will continue to exert pressure on cash flows; after the acquisition of 51% economic interest in FHTL, the net BT fees has come down, but will still stay substantial. The ratings continue to be constrained by increasing competition in the healthcare sector, which may pose a challenge for the company in maintaining its margins. ICRA has also taken note of the on-going litigations against the company; however the financial impact of the same on FHL cannot be ascertained at this stage since the cases are sub-judice.

Going forward, movement in operating metrics (post business trust expenses), progress on asset divestment plans, movement in overall debt quantum and the extent of debt-funded investments/ capital expenditure will be key credit sensitivities. Further, movement in overall indebtedness of holding entities of the group and impact of the ongoing litigations of the group firms on FHL will be credit monitorables.

Key rating drivers

Credit Strength

- Established branded healthcare provider in India, with ~4600 beds spread across 45 healthcare facilities (including projects under development) and over 346 diagnostic centers
- Diversified presence across multiple healthcare verticals, such as secondary care, tertiary care, quaternary care, and diagnostics
- Positive demand outlook for healthcare services in the country, due to growing awareness of healthcare issues, under-served nature of the sector, better affordability through increasing per capita income, and widening medical insurance coverage
- Higher revenues from the hospital network, efficiency improvement initiatives taken by the company and closure of underperforming facilities led to improvement in revenues and OPBITDA in FY2017
- Diagnostic business has continuously registered healthy growth in revenues and has limited debt, leading to strong cash flows
- Low gearing and significant cash and equivalents provide financial flexibility, in case monetisation of non-core assets takes longer than expected

Credit weaknesses

- Stretched leverage and liquidity situation of promoter's holding companies, increasing the reliance of group on refinancing and stake sales. Further, promoters have already pledged ~83% of their stake in FHL to raise loans in holding companies
- Outstanding litigations and contingent liabilities; any adverse ruling may impact FHL's management and operations
- Acquisition of 51% economic interest in Fortis Hospotel Limited has led to increase in net debt and may result in adverse impact on cash flows in short term. Also, the acquisition will increase FHL's outflows towards capital expenditure
- Though the quantum of fee paid to Business Trust will reduce after acquisition of economic interest in Fortis Hospotel Limited, it will continue to have significant impact on the cash flows and consequently the debt coverage indicators of the company
- Mode of exit provided for remaining PE investors in SRL Limited (a subsidiary of FHL) may impact FHL's credit risk profile[3]

Description of key rating drivers

Fortis Healthcare Holdings Private Limited (FHHPL) holds ~44% stake in the flagship operating entity of the group for healthcare business- Fortis Healthcare Limited (FHL). FHHPL, in turn, is the subsidiary of RHC Holdings Private Limited (RHC). The promoters have sold stake in Fortis Healthcare Limited in Q4FY2017 and Q1FY2018 to bring down the debt of holding companies; however, in the absence of meaningful income from investments/ subsidiaries, the promoter group continues to be exposed to refinancing and stake/asset sales. Majority of the investments of the group are already encumbered, leaving limited headroom to raise fresh debt. Further, real estate industry is currently going through a slowdown, impacting the group's ability to sell assets to raise funds. ICRA also notes that all transactions that the group enters into may be exposed to legal challenge due to ongoing litigation with Daiichi Sankyo Limited.

The demand outlook for healthcare services in the country is positive, due to widening medical insurance coverage, growing awareness for healthcare issues, current under-penetration of healthcare services,

[3] Out of the Rs. 370 crore compulsorily convertible preference shares (CCPS) issued to PE investors in SRL, Rs. 250 crore CCPS have already been converted into equity shares, lowering FHL's buyback obligations to that extent

better affordability through increasing per capita income, technological improvements in early diagnosis & treatment, and higher incidence of lifestyle diseases.

FHL currently operates a network of 45 healthcare facilities with ~4600 beds, including owned & managed hospitals and heart command centres. The company has interests in two overseas hospitals, one each in Sri Lanka and Mauritius, with ~400 beds in aggregate. In addition, it has a wide spread diagnostic network, with over 346 diagnostic labs.

The company has reported improvement in occupancy, average revenue per bed (ARPOB) and average length of stay (ALOS) in FY2017, which resulted in increase in revenues from domestic hospital business from Rs. 3448 crore in FY2016 to Rs. 3712 crore in FY2017, registering a growth of 8%. On account of higher revenues from the network, consolidation of FHTL, efficiency improving initiatives taken by the company, focus on higher margin procedures and closure of underperforming facilities, the operating margin of hospital business after BT fees increased from ~1.5% in FY2016 to 4.7% in FY2017.

The company has raised ~S$510 million (Rs. ~2200 crore) through listing of a Business Trust (BT) on Singapore Stock Exchange (SGX) in October 2012. The company hived off various immovable assets of eleven of its clinical establishments into a BT and subsequently listed the BT on SGX; it has offloaded 72% stake in the BT through Singapore listing and continues to hold remaining 28% stake. The BT listing had enabled FHL in reducing its debt obligations by Rs. ~2100 crore in FY2013; however, the company has to make quarterly fee payments to the BT total fee paid in FY2017 was Rs. 371 crore). Further, the fees is projected to increase annually, as the fixed component of the service fees provides for contractual increase of 3% every year and the variable fees will increase in tandem with the revenues of the hospitals. Thus, the increasing outflow towards BT would continue to put pressure on cash flows. Although the acquisition of 51% economic interest in FHTL will lower the BT outflows, the fees will still stay substantial.

Company acquired 51% economic interest in Fortis Hospotel Limited in Q3FY2017. Fortis Hospotel Limited (FHTL) owns immovable assets and certain radiology equipment of two Fortis hospitals, located in Gurgaon (Haryana) and Shalimar Bagh (Delhi). Before this acquisition, FHL did not have any economic interest in FHTL because when the Business Trust (BT) was listed on Singapore Stock Exchange (SGX) in FY2013, 100% economic interest in FHTL was transferred to the BT, post which the BT collected quarterly fees from FHL to use its assets. Now, after this acquisition of economic interest from BT in Q3FY2017, 51% of this fee will flow back to FHL. Though the acquisition has resulted in improved OPBIDTA of the company through lower BT fee outflows, it will adversely impact the cash flow position of the company in short term due to higher interest and debt repayment. Majority of the debt taken for acquisition is to be repaid within three years, exposing the company to refinancing risks. ICRA has noted that the company proposes to monetise certain non-core assets to repay this debt; however, the same is subject to market conditions and requisite approvals. Sale of these non-core assets will be crucial for making debt repayments and will be a key credit rating sensitivity.

Total debt of the company stood at Rs. ~2220 crore and gearing stood at 0.35x as on March 31, 2017. Further, the company had cash and equivalents (Rs. 938 crore as on March 31, 2017), adjusting the same, the net debt stands at Rs. ~1282 crore and net gearing at 0.20x. Low debt and significant cash and equivalents provide financial flexibility, in case asset monetisation takes longer than expected. However, the debt coverage indicators remain weak due to pressure on accruals owing to large outflows towards fee payment to business trust- the adjusted total debt/OPBITDA stood at 13.5x and adjusted interest coverage ratio stood at 0.72x in FY2017.

Analytical approach
For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Link to the applicable criteria
[Corporate Credit Ratings: A Note on Methodology]
[Rating Methodology for Hospitals]
Impact of Parent or Group Support on an Issuer's Credit Rating

About the company
Fortis Healthcare Limited (FHL) was promoted by late Dr. Parvinder Singh. Currently, ~44% stake in FHL is held by promoters- Mr. Malvinder Mohan Singh, Mr. Shivinder Mohan Singh and their family members. The company commenced its operations with opening of its first hospital at Mohali in 2001. Since, then the Company has expanded its operations via expansions and acquisitions. It now has 45 healthcare facilities, operational bed capacity of ~4600 beds and the potential to reach around 10,000 beds. Further, through its subsidiary, SRL Limited, the company operates 346 diagnostic centres in the country.

Status of non-cooperation with previous CRA: Not applicable

Rating history for the last three years

Table

S. No	Instrument	Current Rating (FY2018)			Chronology of Rating History for the past 3 years							
		Type	Amount (Rs. Cr.)	Date(s) & Rating(s)	Date(s) & Rating(s) FY2017	Date(s) & Rating(s) FY2017	Date(s) & Rating(s) FY2017	Date(s) & Rating(s) FY2016	Date(s) & Rating(s) FY2016	Date(s) & Rating(s) FY2016	Date(s) & Rating(s) FY2014
				Jul-17	Mar-17	Sep-16	Jun-16	Mar-16	Sep-15	Apr-15	Mar-14
1	Non-convertible Debentures	Long Term	250	[ICRA]A+ (on watch with developing implications)	[ICRA]A+ (Stable)	[ICRA]A+ (stable)	[ICRA]A+ (on watch with developing implications)	[ICRA]A+ (Stable)	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)
2	Commercial Paper/ Short-term Debt	Short Term	1000	[ICRA]A1+ (on watch with developing implications)	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+ (on watch with developing implications)	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

3	Fund-based Limits	Long Term	65	[ICRA] A+ (on watch with developing implications)	[ICRA]A+ (stable)	[ICRA]A+ (stable)	[ICRA] A+ (on watch with developing implications)	[ICRA]A+ (stable)	[ICRA]A+ (Positive)	[ICRA]A+ (stable)	[ICRA]A+ (stable)
4	Term Loans	Long Term	104	[ICRA] A+ (on watch with developing implications)	[ICRA]A+ (Stable)						
5	Non-fund-based Limits	Short Term	10	[ICRA] A1+ (on watch with developing implications)	[ICRA]A1+						
6	Unallocated Limits	Long Term	21	[ICRA] A+ (on watch with developing implications)	[ICRA]A+ (Stable)						

Note on complexity levels of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1
Instrument Details

Instrument	**Date of Issue**	**Interest/ Discount Rate**	**Date of Maturity**	**Size of Issue* (Rs in Crs)**	**Current Rating & Outlook**
Term Loan	September 2015	10.10%	December 2019	54	[ICRA]A+ (on watch with developing implications)
Term Loan	January 2017	9.45%	January 2022	50	[ICRA]A+ (on watch with developing implications)
Non-convertible Debenture	--	--	--	250	[ICRA]A+ (on watch with developing
Commercial Paper	10.01.2017	8%	10.04.2017	100	[ICRA]A1+ (on watch with developing
Commercial Paper	20.02.2017	8%	19.05.2017	35	[ICRA]A1+ (on watch with developing
Commercial Paper	17.02.2017	9.50%	18.05.2017	25	[ICRA]A1+ (on watch with developing
Commercial Paper	20.02.2017	9.50%	19.05.2017	25	[ICRA]A1+ (on watch with developing
Commercial Paper	27.02.2017	9.50%	26.05.2017	50	[ICRA]A1+ (on watch with developing implications)
Commercial Paper	24.03.2017	10%	22.06.2017	100	[ICRA]A1+ (on watch with developing
Commercial Paper (yet to be placed)	--	--	--	665	[ICRA]A1+ (on watch with developing
Fund-based Limits	--	11.25%	--	40	[ICRA]A+ (on watch with developing implications)
Fund-based Limits	--	11.50%	--	25	[ICRA]A+ (on watch with developing implications)
Non-fund-based Limits	--	--	--	10	[ICRA]A1+ (on watch with developing implications)

Unallocated Limits	--	--	--	21	[ICRA]A+ (on watch with developing implications)

*Outstanding Amount in March 2017

Source: Fortis healthcare Limited

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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.

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