

December 20, 2019

SRL Diagnostics Private Limited: Long-term rating upgraded to [ICRA]BBB+; short-term rating upgraded to [ICRA]A2

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based Limits	15.00	15.00	Rating upgraded to [ICRA]BBB+ (Stable) from [ICRA]BBB- (Stable)
Short-term interchangeable	(15.00)	(15.00)	Rating upgraded to [ICRA]A2 from [ICRA]A3
Non-fund Based Limits	2.00	2.00	Rating upgraded to [ICRA]BBB+ (Stable)/A2 from [ICRA]BBB- (Stable)/A3
Total	17.00	17.00	

*Instrument details are provided in Annexure-1

Rationale

ICRA has upgraded the ratings of SRL Diagnostics Limited (SRLD) to [ICRA]BBB+ (Stable) and [ICRA]A2 from [ICRA]BBB- (Stable) and [ICRA]A3 following an upgrade in the ratings of its parent company viz. SRL Limited (owns 100% equity stake in SRLD) to [ICRA]BBB+ (Stable)/[ICRA]A2 from [ICRA]BBB- (Stable)/[ICRA]A3. In September 2019, ICRA had upgraded ratings of the ultimate parent company viz. Fortis Healthcare Limited (Fortis; owns 57.7% stake in SRL Limited) to [ICRA]BBB+&/[ICRA]A2& from [ICRA]BBB-(&)/[ICRA]A3(&) aided by improvement in operational performance, which coupled with elimination of hospital service fees being paid earlier to RHT¹ led to improvement in company's earnings. In November 2018, IHH Healthcare Berhad Malaysia's (IHH) acquired a controlling stake of 31.1% in Fortis for a consideration of Rs. 4,000 crore.

SRLD is a leading provider of diagnostic services and its market position is supported by common branding with its parent company, SRL Limited. The company receives financial support from its parent company in the form of unsecured term loans.

SRLD's financial performance in FY2019 was in line with ICRA's estimates with revenue growth being flat and healthy profitability margins. The company's revenues remained flat over the years as increase in revenues from the pathology segment is mitigated by a decline in revenue from the imaging business due to closure of some unprofitable labs. Its margins improved in H1 FY2020 supported by lower rentals, legal fees and low administration expenses by centralising some of its processes.

SRLD's financial profile has improved over the years with negligible external debt as on September 30, 2019. The long-term debt on its balance sheet has been extended by its parent company SRL. The steady improvement in operating

¹ Fortis, in Q4 FY2019, acquired Indian assets of Singapore Stock Exchange listed RHT Health Trust (RHT); the same was primarily funded through ~Rs. 4000 crore equity infusion by IHH Healthcare Bhd (IHH) into Fortis.

performance, along with repayment of long-term borrowings from SRL and limited capital expenditure contributed to an improvement in coverage and capitalisation indicators over the past few years.

Despite strong business position and healthy credit metrics, SRLD's ratings are constrained by the ratings of its parent company, given its controlling stake and financial and business linkages. Besides providing an exit to P.E. players in SRL Limited, the Group at present is exposed to multiple investigations at SRL's parent company level and erstwhile promoters by the Securities and Exchange Board of India (SEBI) and Serious Fraud Investigations Office (SFIO) and significant outstanding litigations, especially the petition filed by Daiichi Sankyo Company Limited in Supreme Court of India and the High Court of Delhi. Any adverse outcome of these investigations or litigations may impair the parent company's ability to maintain its operational and financial risk profile. Thus, ICRA would continue to monitor the impact of these developments on the credit profile of SRLD of various ongoing corporate developments as well as litigations concerning the Group.

ICRA has taken a consolidated view of SRL Limited and its subsidiaries because of operational and functional linkages between them.

The outlook on SRL Diagnostics Limited's (SRLD) long-term rating remains at Stable. ICRA believes SRLD will continue to benefit from its extensive track record of operations, established brand, healthy financial risk profile and will maintain its strong credit indicators.

Key rating drivers and their description

Credit strengths

Leading diagnostics service provider backed by strong brand and widespread network of laboratories and collection centres – SRLD, along with its parent company, SRL, is positioned as the leading diagnostics services company in India backed by a well-known brand and a widespread network of 411 laboratories and wellness centres. The company is positioned as a leading diagnostics player within the organised segment in India. It has four regional labs covering the entire country. These are supported by an extensive network of 1,174 collection centres and 8,057 direct client pick-up points.

Comprehensive range of diagnostic tests including speciality test labs – The company boasts of one of the most comprehensive range of diagnostic tests in India and has four service verticals – pathology, radiology, wellness and clinical trials. The pathology segment accounts for almost 90% of its consolidated operating income.

Strong operational and financial support from parent – SRLD receives financial support in terms of unsecured long-term loans and benefits from the common management. It shares the common brand of SRL Diagnostics with its parent company, which results in higher bargaining power with suppliers and brand visibility through marketing campaigns.

Steady improvement in profitability indicators – The company's profitability has been improving since FY2017. It is having operating margins similar to those of Dr. Lal Path Labs and Metropolis healthcare. SRLD recorded an operating margin of 30% in H1 FY2020. The margins are improving due to high share of walk-in customers in partner doctor labs viz. Dr. Phadke Labs, Dr. Trivedi & Roy and others. As it does not cater to the Fortis Group, the debtor position is also satisfactory.

Credit challenges

Ongoing litigations and investigations by SEBI and SFIO – The Fortis Group and its erstwhile promoters are at present facing multiple investigations and litigations and any adverse ruling may impact the Group’s operations.

Increasing competition from new diagnostic chains (including online aggregators) and regional players offering significant price discounts – The competition in the diagnostics industry has increased substantially with significant investments from private equity players. In addition, entry of online aggregators that offer discounts to attract customers has put significant pressure on pricing. This is likely to put pressure on earnings of incumbent players going forward. Additionally, price caps set by regulators could lower the pricing power in the sector, which will have a negative impact on its profit margins.

Liquidity position: Strong

SRLD’s liquidity profile is strong supported by expectation of healthy cash flow generation, sizeable cash reserves of Rs. 29.7 crore (as on September 30, 2019) at the consolidated level and unutilised fund-based lines of credit of Rs. 15.00 crore (as on March 31, 2019). It has a negative cash cycle and a positive cash flow from operations indicating healthy liquidity profile.

Rating sensitivities

Positive triggers – Ratings may be upgraded if there is a positive event at the Group level leading to an improvement in credit profile of the parent company or improvement in scale of operations of the company, while maintaining operational profitability and sufficient liquidity.

Negative triggers – Ratings may be downgraded in case of any event, which might have an adverse impact on the Group’s business or financial profile or there is decline in profitability indicators due to pricing pressure in the industry.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Diagnostic Service Providers
Parent/Group Considerations	Parent/Group Company: SRL Limited ([ICRA]BBB+/A2); 100% stake in SRL Diagnostics Private Limited.
Consolidation / Standalone	The rating is based on the consolidated financial statements of the issuer.

About the company

SRLD, formerly known as Piramal Diagnostic Services Private Limited, is one of the larger chains of clinical diagnostic centres in India. It is a wholly-owned subsidiary of SRL Limited, which is owned by Fortis Healthcare Limited (57.7% stake). SRLD is one of the few diagnostic centre chains offering pathology and radiology services on a pan-India level. Most centres in addition, offer echocardiography, ECG, stress tests, pulmonary function tests, audiometry and body composition tests, besides pathology and radiology tests. SRLD operates 44 diagnostic centres and 54 collection centres (as on September 30, 2019). Additionally, through its joint venture, DDRC SRL Diagnostic Services, it operates 193 laboratories and five collection centres in Kerala.

In FY2019, the company reported a turnover of Rs. 282.3 crore with a profit after tax (PAT) of Rs. 27.0 crore. At the consolidated level, the SRL Group reported a consolidated turnover of Rs. 1003.7 crore with a PAT of Rs. 85.9 crore.

Key financial indicators (audited; consolidated)

	FY2018	FY2019
Operating Income (Rs. crore)	277.8	282.3
PAT (Rs. crore)	22.3	27.0
OPBDIT/OI (%)	24.1%	27.1%
RoCE (%)	34.8%	37.4%
Total outside liabilities / Tangible Net Worth (times)	33.1	5.0
Total Debt/OPBDIT (times)	2.3	1.7
Interest Coverage (times)	3.0	3.9
DSCR	2.0	2.2

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2020)			Rating History for the Past 3 Years												
		Type	Amount Rated	Amount Outstanding	Rating	FY2019			FY2018						FY2017		
						20 Dec 19	01 Feb 19	12 Apr 18	09 Mar 18	13 Feb 18	07 Feb 18	28 Dec 17	17 Jul 17	04 Jul 17	07 Feb 17	09 Sep 16	04 Jul 16
1	Fund based facilities	Long Term	15	NA	[ICRA] BBB+ (Stable)	[ICRA] BBB- (Stable)	[ICRA] BBB- (Negative)	[ICRA] BBB+@	[ICRA] A-@	[ICRA] A+@	[ICRA] A+&	[ICRA] A+&	[ICRA] A+ (Stable)	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	
2	Short term fund based interchangeable	Short Term	(15)	NA	[ICRA]A3	[ICRA]A3	[ICRA]A3	[ICRA] A2@	[ICRA] A2+@	[ICRA] A1+@	[ICRA] A1+&	[ICRA] A1+&	[ICRA] A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	
3	Non-fund based facilities	Long and Short Term	2.0	NA	[ICRA] BBB+ (Stable)/ A3	[ICRA] BBB- (Stable)/ A3	[ICRA] BBB- (Negative) / A3	[ICRA] BBB+@/ A2@	[ICRA] A-@/ A2+@	[ICRA] A+@/ A1+@	[ICRA] A+&/ A1+&	[ICRA] A+&/ A1+&	[ICRA]A+ (Stable)/ A1+	-	-	-	

Amount in Rs. crore

Complexity level 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

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund based facilities	NA	NA	NA	15.00	[ICRA] BBB+ (Stable)
NA	Short term fund based interchangeable	NA	NA	NA	(15.00)	[ICRA]A2
NA	Non-fund based facilities	NA	NA	NA	2.00	[ICRA] BBB+ (Stable)/ A2

Source: SRL

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
DDRC SRL Diagnostics Private Limited	50.00%	Equity Method

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