

Healthcare Global Enterprises Limited

April 04, 2019

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term loans	245.70	532.20	[ICRA]A-; reaffirmed, outlook revised from Stable to Negative
Long-term Fund Based – CC	85.00	85.00	[ICRA]A-; reaffirmed, outlook revised from Stable to Negative
Long-term Non-fund based (sub-limits)	(163.70)	(356.11)	[ICRA]A-; reaffirmed, outlook revised from Stable to Negative
Short-term - Fund based	0.00	20.00	[ICRA]A2+; Assigned
Short-term - Non fund based	0.00	28.50	[ICRA]A2+; Assigned
Short-term Non-fund based (sub-limits)	0.00	(48.50)	[ICRA]A2+; Assigned
Long-term Unallocated limits	250.00	0.00	- ¹
Total	580.70	665.70	

*Instrument details are provided in Annexure-1

Rationale

The revision in outlook takes into account Healthcare Global Enterprises Limited's (HCG) weaker-than-expected performance during 9M FY2019 wherein the company's operating margin declined by 130 bps on a y-o-y basis to 12.9%. This was largely on account of increase in losses from the new centres (Rajkot, Jaipur, Borivali (Mumbai) and Nagpur) and decline in existing centre EBITDA due to losses from phase-2 expansion at Nashik during Q3 FY2019. Decline in OPM coupled with high interest expenses, including forex loss (notional) of Rs. 11.9 crore resulted in the company incurring net losses of Rs. 14.3 crore during 9M FY2019. Going forward, the losses from the new centres opened in the past two years and new centres launched at South Mumbai and Kolkata in Q4 FY2019 are expected to continue exerting a downward pressure on the company's OPM in the medium term. Additionally, with reduction in MRP of cancer drugs sold by hospitals post the capping of trade margin by National Pharmaceutical Pricing Authority (NPPA), ICRA expects the company's operating margin to be affected during FY2020. The ratings are also constrained by the company's stretched debt protection metrics with gearing and TD/OPBDITA of 1.2x and 5.0x respectively as on September 30, 2018. With the company expected to incur a sizeable debt-funded capex during FY2020 and FY2021 and decline in operating profits expected going forward, ICRA expects the capitalization and coverage indicators to remain stretched in the medium term.

¹ ICRA had [ICRA]A- (Stable) rating outstanding on the Rs. 250.00 crore long-term unallocated limits earlier. This has currently been revised to nil.

With ~32% of its total debt as on March 31, 2018 denominated in USD, the company's margins also remain exposed to unfavourable movements in exchange rate fluctuations in INR against USD. However, with hedging through forward contracts put in place by the company from Q3 FY2019 onwards, ICRA expects the forex risk to be mitigated to a certain extent. The ratings also take note of HCG's high reliance on its Bangalore facility, which contributed 35.2% to revenues in H1 FY2019 (although reduced from 48.6% in FY2016) and the company's high geographical concentration in Karnataka and Gujarat (contributing to ~68.7% of its revenues during H1 FY2019).

The ratings continue to factor in HCG's longstanding presence, niche focus on cancer therapy and established brand equity of the hospital chain and the promoters in the field of oncology. The ratings are supported by the company's healthy revenue growth of 18.5% during 9M FY2019, aided by healthy ramp-up in new centres, strong growth in certain existing centres and improving average revenue per occupied bed (ARPOB) trend. ICRA also expects the near-term revenue visibility of the company to remain strong supported by healthy ramp up of new centres opened at South Mumbai and Kolkata, ongoing plans to set up new centers in Gurgaon and Kochi, in addition to increase in occupancies at the new centres which commenced operations in the last 24 months. Over the longer term, increasing incidence of cancer in India coupled with a positive demand outlook for healthcare services in the country due to factors such as better affordability, widening medical insurance coverage, growing awareness and under-penetration of healthcare services is expected to benefit the company given its scalable model. With high quality of infrastructure and ability of the company to attract and retain reputed consultants, ICRA expects healthy patient inflow supporting business prospects of the company going forward. ICRA notes that the company is currently in talks with various investors to raise funds during FY2020 and FY2021 by means of either equity infusion, sale and leaseback of certain assets or sale of stake in subsidiaries to external investors; part of the proceeds from the same are expected to be used towards prepayment of debt. ICRA will continue to monitor for any such developments and evaluate the same for its impact on the ratings.

Outlook: Negative

The revision in outlook takes into account weaker-than-expected performance of the company during 9M FY2019. The outlook may be revised to 'Stable' if there is improvement in the financial risk profile of the company characterized by higher-than-expected revenue growth and profitability and improvement in debt protection metrics going forward.

Key rating drivers

Credit strengths

- **Strong market position:** HCG's long standing presence, niche focus on cancer therapy and established brand equity of the hospital chain and the promoters in the field of oncology continue to support its business prospects.
- **Expansions in partnership with other medical professionals:** HCG's business strategy includes partnerships with eminent oncologists / fertility specialists as it sets up new cancer care centres (CCCs) / fertility clinics, especially in non-metro towns. While a doctor's reputation in the field plays a significant role in attracting patients, the company's strong brand recognition in the field of oncology mitigates the risk of revenue volatility in the event of termination of contract with certain doctors.
- **Healthy growth in revenues during 9M FY2019:** Ramp up in revenues from new centres, healthy growth in revenues from certain existing centres namely Nashik, Maharashtra (post the phase-2 expansion), Hubli, Karnataka and Vijaywada, Andhra Pradesh (post the consolidation of partners' business named 'City Cancer Centre', purchased in March 2018), apart from improving ARPOB resulted in healthy revenue growth of 18.5%

on a y-o-y basis during 9M FY2019. Increasing realization on the back of advanced medical equipments and treatments such as Tomo Therapy and Robotic surgery, improving patient mix (with continued reduction in revenues from government schemes), further ramp up in revenues expected from new centres apart from additional revenues from new centres in Kolkata and South Mumbai are expected to support the revenue growth going forward.

- **Positive demand outlook:** ICRA notes that the increasing incidence of cancer in India coupled with a positive demand outlook for healthcare services in the country due to factors such as better affordability, widening medical insurance coverage, growing awareness and under-penetration of healthcare services, is expected to benefit the company given its scalable model.

Credit challenges

- **Increase in losses from new centres and reduction in existing center EBITDA results in decline in OPM during 9M FY2019; commissioning of new hospitals to constrain near-term profitability:** Despite continued reduction in losses from the centres at Borivali (Mumbai) and Nagpur during 9M FY2019, the losses from new centres increased to Rs. 11.9 crore during 9M FY2019 from Rs. 6.9 crore during 9M FY2018 on account of losses from the new centres opened at Rajkot and Jaipur. This, coupled with reduction in existing center OPM during Q3 FY2019 to 17.5% (18.5% during Q3 FY2018) owing to losses from phase-2 expansion at Nashik had resulted in the company's overall operating margins declining by 130 bps to 12.9% during 9M FY2019. Going forward, the losses from new centres opened in the past two years, new centres launched at South Mumbai and Kolkata in Q4 FY2019 and Gurgaon centre (which is expected to commence operations in Q3 FY2020) are expected to constrain the operating margins of the company.
- **NPPA's capping of trade margins on cancer drugs expected to affect the company's operating margin going forward:** With NPPA capping trade margins on 42 non-scheduled anti-cancer medicines at 30.0% as per the regulation released on February 28, 2019, the MRP of the drugs sold by stockists and hospitals have come down, with reduction of up to 87% in certain cases. With HCG deriving around ~29-30% of its revenues from the pharmacy vertical, ICRA expects the company's operating margin to be affected by the same during FY2020. However, decline in cost of treatment is expected to draw more patients to reputed players like HCG. This would remain a key credit monitorable going forward.
- **Stretched capitalization and coverage metrics; expected to remain stretched owing to sizeable expansion plans during FY2020-FY2021:** Owing to sizeable debt-funded capital expenditure of ~Rs. 361 crore during FY2018 and H1 FY2019, purchase of the partner's stake of 49.99% in the Borivali (Mumbai) centre (for a consideration of ~Rs. 22.0 crore) and acquisition of City Cancer Centre at Vijaywada (for a total consideration of Rs. 51.7 crore including cash consideration of ~Rs. 22 crore), the company's debt increased to Rs. 635.8 crore as on September 30, 2018. Increasing debt levels, coupled with declining operating profits strained the company's debt protection metrics with gearing and TD/OPBITDA at 1.2x and 5.0x respectively as on September 30, 2018 (0.9 times and 4.0 times respectively as on March 31, 2017). These are higher than the rating medians for the company's rating category. With sizeable debt-funded capex plans (cumulatively) in the range of Rs. 200-Rs. 250 crore primarily towards expansion at Gurgaon and Kochi apart the regular maintenance capex during FY2020 and FY2021 coupled with declining profits, ICRA expects the capitalization and coverage indicators to remain stretched in the medium term. However, the company is currently in talks with various investors to raise funds during FY2020 and FY2021 by means of either equity infusion, sale and leaseback of certain assets or sale of stake in subsidiaries to external investors; part of the proceeds from the

same are expected to be used towards prepayment of debt. This would remain a key credit monitorable going forward considering the impact on capitalization and coverage indicators of the company.

- High geographic concentration; significant dependence of revenues on Bangalore:** The company has high geographic concentration with Karnataka and Gujarat contributing to ~68.7% of its revenues during H1FY2019. Furthermore, the company has high dependence on Bangalore with revenue contribution of ~35.2% during H1FY2019. However, with the company's continued expansion into other cities during FY2017-FY2019, the revenue contribution has reduced from 48.6% in FY2016. With continued ramp-up expected in new centres opened during FY2018 and FY2019 coupled with expansion at Gurgaon and Kochi during FY2020 and FY2021 respectively, the geographic concentration is expected to reduce going forward.
- Vulnerability to fluctuations in foreign exchange rates; however, hedging through forward contracts is expected to mitigate the risk going forward:** With ~32% of the overall debt denominated in foreign currency (USD) as on March 31, 2018 (Rs. 148.8 crore of equipment loans) , the company's margins remain vulnerable to fluctuations in foreign exchange rates. However, the company has commenced hedging through forward contracts in Q3FY2019 which is expected to mitigate the risk to a certain extent.

Liquidity Position:

HCG's liquidity remained adequate during FY2018 with positive cash flow from operations. However, the cash flow from operations was stretched as on September 30, 2018 on account of increase in interest expenses (comprising forex loss of Rs. 15.9 crore) and working capital requirements during the same period. The company currently has fund-based (FB) working capital limits of Rs. 85.0 crore from Yes Bank. The average fund-based working capital utilization of the company was moderate at 57.6% over the 12-month period ending February 28, 2019. The company has cushion available in the form of cash and liquid investments of Rs. 34.8 crore as on September 30, 2018 in addition to accruals supported by healthy operating margins.

The total debt outstanding as on September 30, 2018 is Rs. 635.8 crore, primarily comprising term loans of Rs. 357.8 crore and letter of credit (LC) of Rs. 169.9 crore used to purchase medical equipments: these are converted to term loans post the moratorium period of 3 years supporting its liquidity position. The company has capex plans of Rs. 345.6 crore during FY2019 and FY2020, which is expected to be funded through a mix of term loans and internal accruals. Including the additional term loans to be availed, the company has repayment obligations of Rs. 29.5 crore, Rs. 39.6 crore and Rs. 41.3 crore during FY2019, FY2020 and FY2021 respectively. The company's projected accruals appear to be comfortable in comparison to the repayments indicating a comfortable liquidity position. Furthermore, the company is expected to raise funds over the next two years (FY2020-FY2021) and part of the proceeds from the same are expected to be used towards prepayment of debt. However, this would remain be a key credit monitorable.

Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology ICRA's Rating methodology for Hospitals
Parent/Group Support	NA
Consolidation / Standalone	The ratings are based on the consolidated financial profile of the company

About the company:

Established in 1989, Healthcare Global Enterprises Limited, is present primarily in the oncology field with the largest cancer care network (with 22 cancer care centres as on February 28, 2019) in South Asia. HCG was promoted by Dr. B.S. Ajai Kumar, a practicing radiation and medical oncologist with over 30 years of experience. Originally established with a single cancer care centre, the Bangalore Institute of Oncology (BIO), at Bangalore by Dr. B.S. Ajai Kumar and four other oncologists, the company has rapidly expanded its presence to Ahmedabad, Chennai, Nasik, Ranchi, Rajkot, Cuttack, Hubli, Mumbai, Nagpur, Vizag and Vijayawada, among others. The company is currently present across the oncology value chain, offering services from prevention, screening, diagnosis and treatment to rehabilitation, supportive care and palliative care. The company also offers India's largest network of cancer care facilities with over 40,000 patients visiting the company's hospitals every year.

The company had acquired 50.1% equity interest in BACC Healthcare Private Limited (BACC) in 2013, which operates fertility centres under the Milann brand. Pursuant to this acquisition, it now operates eight Milann fertility centres in Bengaluru, Delhi, Mumbai and Chandigarh. In accordance with the terms of the shareholders' agreement dated March 22, 2013 between the company, Dr. Kamini A. Rao ("Dr. Rao") and BACC, the company has announced that it shall acquire the remaining 46,695 equity shares, constituting 49.9% of the share capital of BACC ("Shares") from Dr. Rao at a consideration of Rs. 65.0 crore. The same is expected to happen during Q2/Q3FY2020.

Key financial indicators (Consolidated)

	FY2017	FY2018
Operating Income (Rs. crore)	700.1	830.7
PAT (Rs. crore)	23.0	18.3
OPBDIT/OI (%)	15.0%	14.3%
RoCE (%)	8.3%	9.0%
Total Debt/TNW (times)	0.9	0.8
Total Debt/OPBDIT (times)	4.0	3.9
Interest coverage (times)	4.6	2.8

Source: company

Status of non-cooperation with previous CRA: India Ratings and Research (Ind-Ra) had revised Healthcare Global Enterprises Limited's Outlook to Positive from Stable while affirming the Long-term Issuer Rating at 'IND BBB' and simultaneously migrating it to the non-cooperating category during March 2017. Subsequently, Ind-Ra had withdrawn ratings outstanding on the company during April 2017.

Any other information: None

Rating history for last three years:

		Current Rating (FY2020)		Chronology of Rating History for the Past 3 Years						
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore) as on March 31, 2018	Date & Rating April 2019	Date & Rating in FY2018 January 2018	Date & Rating in FY2017			Date & Rating in FY2016	
						April, 2017	December, 2016	October, 2016	March, 2016	September, 2015
1	Term Loans	532.20	251.90	[ICRA]A-(Negative)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]BBB+(Positive)	[ICRA]BBB+(Positive)	[ICRA]BBB+(Stable)	[ICRA]BBB+(Stable)
2	Fund Based – Cash Credit	85.00	1.70	[ICRA]A-(Negative)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]BBB+(Positive)	[ICRA]BBB+(Positive)	[ICRA]BBB+(Stable)	[ICRA]BBB+(Stable)
3	Non-fund based Limits	(356.11)	NA	[ICRA]A-(Negative)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]BBB+(Positive)	[ICRA]BBB+(Positive)	[ICRA]BBB+(Stable)	[ICRA]BBB+(Stable)
4	Fund based – Short Term loan	20.00	NA	[ICRA]A2+	-	-	-	-	-	-
5	Non-Fund based – LC/BG	28.50	NA	[ICRA]A2+	-	-	-	-	-	-
6	Non-fund based limits	(48.50)	NA	[ICRA]A2+	-	-	-	-	-	-
7	Unallocated	0.00	NA	-	[ICRA]A-(Stable)	-	-	[ICRA]BBB+(Positive)	[ICRA]BBB+(Stable)	[ICRA]BBB+(Stable)

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	Term loans	FY2017	10.4%	FY2027	532.20	[ICRA]A- (Negative)
NA	Long-term fund based limits	FY2017	10.6%	-	85.00	[ICRA]A- (Negative)
NA	Non-fund based limits (sub-limits)	FY2017	-	-	(356.11)	[ICRA]A- (Negative)
NA	Short-term fund based limits	FY2017	-	-	20.00	[ICRA]A2+
NA	Short-term non-fund based limits	FY2017	-	-	28.50	[ICRA]A2+
NA	Non-fund based limits (sub-limits)	FY2017	-	-	(48.50)	[ICRA]A2+
NA	Unallocated limits	-	-	-	0.00	-

Source: company

Annexure-2: List of entities considered for consolidated analysis²

Company Name	Ownership	Consolidation Approach
HCG Medi-Surge Hospitals Private Limited	74.00%	Full Consolidation
Malnad Hospital & Institute of Oncology Private Limited	70.25%	Full Consolidation
Healthcare Global Senthil Multi Specialty Hospital Private Limited	100.00%	Full Consolidation
Niruja Product Development and Research Private Limited	100.00%	Full Consolidation
BACC Healthcare Private Limited	50.10%	Full Consolidation
Healthcare Diwan Chand Imaging LLP	75.00%	Full Consolidation
Apex HCG Oncology Hospitals LLP ³	50.01%	Full Consolidation
HCG Oncology LLP	74.00%	Full Consolidation
HCG NCHRI Oncology LLP	76.00%	Full Consolidation
HCG Manavata Oncology LLP	51.00%	Full Consolidation
HCG EKO Oncology LLP	50.50%	Full Consolidation
HCG (Mauritius) Private Limited	100.00%	Full Consolidation
HCG Sun Hospitals LLP	74.00%	Full Consolidation
Healthcare Global (Africa) Private Limited	76.73%	Limited Consolidation
Strand Life Sciences Private Limited	38.20%	Limited Consolidation

Source: company; Note: all figures are as on March 31, 2018

³ As on December 31, 2018, the company has acquired the balance stake of 49.99% in Apex HCG Oncology Hospitals LLP

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