



“Narayana Hrudayalaya Limited Q2 FY17 Earnings Conference Call”

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RELATIONS AND MERGERS & ACQUISITIONS**

Moderator: Ladies and gentlemen, good day and welcome to the Narayana Hrudayalaya Limited Q2 FY17 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 call, please signal an operator by pressing ‘*’ then ‘0’ on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Debangshu Sarkar from Narayana Hrudayalaya. Thank you and over to you sir.

Debangshu Sarkar: Thank you, Janice. Good afternoon, ladies and gentlemen, I am Debangshu Sarkar and I run the Investor Relations and Mergers & Acquisitions function at NH and I welcome you all to the Q2 FY2017 earnings conference call. To discuss our financial and business performance, future outlook and to address your queries today, we have with us Dr. Raghuvanshi - our Group CEO and Mr. Kesavan - our Group CFO, alongside myself. I hope you have gone through the copy of the press release along with the quarterly earnings update which were uploaded on the stock exchange. Before we proceed with this call, I would like to remind everyone that this call is being recorded and the transcript of the same shall be made available on our website in due course of time. I would like to remind you that everything that being said on this call that reflects any outlook for the future or which can be construed as a forward looking statement must be viewed in conjunction with uncertainties and the risk that they face. These uncertainties and risks are included, but not limited to what we have mentioned in our prospectus filed with SEBI last year and the subsequent annual report on our website. After the end of this call, in case you have any further question, please feel free to get in touch with us. Now, I would like to hand over the call to Dr. Ashutosh Raghuvanshi.

Ashutosh Raghuvanshi: Thank you, Debangshu. Very good afternoon to all of you. On behalf of Narayana Hrudayalaya, I welcome you all to our earnings conference call. I am happy to share that we have maintained our growth momentum this quarter along with noteworthy improvement in the quality of earnings. From quarterly perspective, our total operational income grew approximately 20% year-on-year to INR 4,874 million in Q2 fiscal 2017 as compared to INR 4,078 million in Q2 of fiscal 2016, which was split across the healthy 13% growth across our matured hospitals in greater than 5 years’ bucket with the newer hospitals along with the acquired facilities contributing an impressive 44% growth. Further as we scaled up our operations in these younger hospitals, the operational efficiencies led to a robust 31% absolute EBITDA growth for Q2 financial year 2017 year-on-year. We registered an EBITDA of INR 681 million in Q2 financial year 2017 as compared to INR 519 million in Q2 of financial year 2016, which translates to a margin of 14.0% and 12.7% respectively. Overall, the baseline numbers from the first 2 quarters of this fiscal give us confidence and reinforcement to our group’s belief that affordable healthcare can go hand in hand with a profitable business model and create value for all our stakeholders.

Further in line with our recent disclosure to stock exchange, NH has decided to call off its proposed facility in Lucknow and exit from its operations at the Berhampore unit. These decisions were necessitated through continuous evaluation of our portfolio. At NH, we regularly

monitor our strategy at unit level and would continue to be flexible and take decisions to sustain the long-term interests of our business. Besides, we also see the current overall environment being conducive for us to explore new possibilities that could potentially align with our long term vision.

Coming to the International Operations, you would be very pleased to know that our facility at Cayman Islands has broken even at quarterly EBITDA level. This is a significant development for us as we took just 30 months to achieve this milestone. We also successfully achieved the milestone of conducting 130 cardiac surgeries on children from 13 neighbouring islands till date at our Cayman Islands facility at a very affordable cost in partnership with several charitable organizations. The largest number of kids in this group were from Haiti Island. This geography bodes well with our group strategy and we expect the business to demonstrate growth going forward

Let's now move to the key operating highlights of this quarter, some of the key clinical developments during this quarter were:

- Our doctors at Mazumdar Shaw Medical Center performed a unique functional surgery to correct anatomical abnormality of oral-pharyngeal and palatal area of a high profile patient
- Our team of doctors at Jaipur unit successfully treated a double outlet tricuspid valve repair operation which is an extremely rare occurrence and only five such cases have been reported
- Our flagship unit at Bengaluru performed TactiCath procedure which is the first of its kind in Southern India
- Our super-specialty unit at Howrah conducted an EP study on an eight-year-old child, again being the first such study in the Eastern India

I am also pleased to announce that during the last quarter, our organization was recognized at various platforms, the key ones being as follows:

- Narayana Institute of Cardiac Sciences, Bengaluru was awarded the best single specialty hospital in cardiology at the 6th edition of ICICI Lombard and CNBC TV18 Health Care Awards in August this year. This is the second time this institution won this award in 6 years
- NH also won the innovative marketing practices award at Express Healthcare Excellence Award for our unique initiative called NH Dialogues where we interact with patients and specialists through webinar
- NH Jaipur received the CSR award at the second annual ELETS Healthcare summit in Rajasthan in September 2016

The list goes on, while these achievements recognize our work in healthcare space, we continue to evolve our business across the geographies with focused approach on affordability, high quality tertiary care and fostering clinical excellence.

With this, now we could open the floor for questions and answers.

Moderator:

Thank you. Ladies and gentlemen, we will now begin with the question and answer session. We take the first question from the line of Neha Manpuriya from JP Morgan. Please go ahead.

- Neha Manpuriya:** My first question is that given the seasonality has a big impact on this quarter, just wanted to understand what is the contribution from Dengue, Chikungunya etc. in this particular quarter if you could classify the revenue?
- Ashutosh Raghuvanshi:** Typically as we have stated earlier, most of our revenue comes from procedure based care and medical specialties do not play a very major role in our facilities. However, we do see some impact on the number of medical patients. There is a minimal impact on realization i.e. if you see the ARPOB which was 72 Lacs in the previous quarter has come down to 70 Lacs during this quarter. The reason for the same is two-fold. One is as you said correctly, a slight increase in the number of medical patients than what we usually see in our network and second is the slight increase in the number of patients coming through the government schemes which typically have a slightly lower realization. However, we do not see a huge impact of seasonality in our network because most of our core service lines are non-medical and procedure oriented.
- Neha Manpuriya:** So is it fair to say that ARPOB in this case should be sustainable to a very large extent or it should only improve from here?
- Ashutosh Raghuvanshi:** No, you were right when you said that there is an impact of seasonality on our business. Our seasonality is slightly different, the change in ARPOB is not because of infective diseases which impact us but the elective work of major procedures usually comes down during the festival period and that typically is seen during the third quarter starting from Durga Puja lasting up to Christmas. So we expect that some impact of the same could be there. But we do not think that it would be very significant
- Neha Manpuriya:** Sir, my second question is that margins have seen a very sharp improvement quarter-on-quarter and this is despite our ARPOB coming down quarter-on-quarter. Could you probably point out two-three areas, I understand based on your margin that you have given maturity wise, all your segments have seen improvement but the sharpest, I guess is in the acquired facilities. So what changed essentially to drive this strong margin, is there any one-off in this number that we should be considering?
- Ashutosh Raghuvanshi:** There is no one-off item. One of the things which you pointed out that there is an improvement in margins in the acquired facilities, this uptick is primarily because when you acquire a facility, the integration and upgradation of that unit takes some time. So that is one of the main reasons that you are seeing the impact now. These were existing hospitals which would not typically follow the cycle of 5 years of maturity because these hospitals already existed when we took over. However, we upgraded the infrastructure and we also integrated the operations with our larger functions so that efficiencies could be brought in terms of supply chain, etc. So these are the main reasons why these hospitals have started yielding results.
- Neha Manpuriya:** And how much of this improvement is backed into the numbers that 11% margin that I can see in the acquired facilities, is there more in terms of just purely on upgradation and integration, I

understand obviously case mix improves etc. but just purely on making changes which are required, is there more to flow in?

Debangshu Sarkar: Yeah, Neha this is Debangshu here. While Dr. Raghuvanshi highlighted the fact that obviously these were acquired facilities with operational track record in the manner that it required us integrating them within the broader network. Having said that, you would also recognize that we had made specific interventions across the clinical domain as well as quite a bit across the medical equipment in these particular acquired facilities that has already started showing up some result in the form of the current margins that you see, but the story is still going to pan out that we feel out there in terms of further improving margins on an annual basis from these numbers as well going forward.

Moderator: Thank you. We take the next question from the line of Nitin Agarwal from IDFC Securities. Please go ahead.

Nitin Agarwal: Dr. Raghuvanshi as far as growth is concerned, how are we looking after the cancellation of lease for the Lucknow setup, we do not have much on our plate in terms of projects that will go live over the next year and half. So, how are we looking at growth for the next 2 to 3 years, is it largely going to be just scaling up the existing assets and how proactively are we looking at adding new assets to the network?

Ashutosh Raghuvanshi: We had mentioned earlier that the Mumbai Hospital was supposed to be commissioned at the beginning of 2017 is absolutely on track. The hospital fitments are complete and we are in the process of getting all the necessary clearances and the hospital is expected to be operational by January 2017. This will add 297 beds to our existing bed count. Other than that, we are in continuous process of evaluating some other projects in geographies of our interest which would help us to leverage our scale and size and also the operational efficiencies. We would be happy to share that information with all of you at the right time. We believe that we have a robust pipeline available to us.

Nitin Agarwal: In terms of the opportunities that you see in the landscape, do you see any opportunities which are in line with the existing capital structure or that kind of cost structure is not easy to replicate as we go forward as we look at some newer opportunities?

Ashutosh Raghuvanshi: Yes, there are opportunities which are available in our kind of model. We have certain opportunities coming which would fit in the same model what we have been following. Now it is important for us to understand that there will always be a mix of projects where certain projects would come to us at virtually no cost whereas certain projects may cost us as much as a traditional hospital in a metro area, but when we will balance these two out, we believe we will keep our structure similar to what it has been in the past. So the projects which we are evaluating are in line with the business model we follow so as to ensure that the total amount of capital we deploy is manageable and is well within the limits of what we can afford.

- Moderator:** Thank you. We take the next question from the line of Charu Latha from Dalal & Broacha. Please go ahead.
- Charu Latha:** I wanted to know that there is an addition of 289 operational beds in this quarter. From which areas do they pertain to and my second question is that you just mentioned regarding expansion in geographies of interest, so can you expand further on that?
- Debangshu Sarkar:** Sure, Charu Latha, this is Debangshu here. On the first part, yes, you are right in your observation that we have added 289 beds in our operational beds' portfolio in our existing network. This ramp-up has come up across the length and breadth of the network, predominately across our Health City, Bengaluru facility itself and some beds in Mysore and Shimoga as well but like I said it is spread out across all our hospitals. This is mostly in line with the ramp-up of occupancies in all these units that you have seen. On to your second question of the geographical clusters that we guys are looking for in terms of our expansion going forward, as Dr. Raghuvanshi had mentioned in his previous call as well while we today have two predominant clusters regionally speaking across the Southern region and the Eastern region centred around Bangalore and Kolkata respectively, the intention is to further strengthen them and capitalize on the advantages that we have created out here by the virtue of being there for a long period of time but at the same time we would want to create meaningful clusters around the balance part of the country where today we probably do not have that strong network. Let us say around Mumbai itself in the Western part and subsequently in the Northern part centred around NCR.
- Moderator:** Thank you. We take the next question from the line of Ravi Nareddi, an Individual Investor. Please go ahead.
- Ravi Nareddi:** Sir, can you tell me what will be your CAPEX plan in further 6 months or in a period of two years?
- Debangshu Sarkar:** So generally what we have seen over the last two years and probably going forward that should play out as well, is around INR 100 crores of annual maintenance / upkeep / upgradation CAPEX and you need to add on to it any new projects on top of that which we are commissioning for the period that you are mentioning. So let's say for Mumbai, we are talking about, around INR 50 crores kind of a number towards the medical equipment that we are setting up out there in the asset-light format. Should we be opening up more hospitals, obviously that number needs to be topped up against that.
- Ravi Nareddi:** And in future, your business model will be asset-light model or you will commission new hospitals also?
- Debangshu Sarkar:** We would always prefer to keep our model asset right, so we would always like to look at opportunities which are asset light. Having said that, if in order to create a very sustainable cluster, we need to do some Greenfield or a complete acquisition, we would look for that as well. However, the choice or preference would always be towards asset-light model.

- Moderator:** Thank you. We take the next question from the line of Ashish Kumar from Infinity Alternate. Please go ahead.
- Ashish Kumar:** I have two questions, one was in terms of understanding on the oncology side, how many centers are operational and what is your plan over the next 12 months on the oncology side and second one was more a housekeeping question on Cayman in terms of what is the current investment in capital per day?
- Ashutosh Raghuvanshi:** Answer to your first question is that we have four fully functional cancer centers. We have a center at Mazumdar Shaw Medical Center, we have a center in the Westbank in Calcutta. We have a center working in Mysore and one in Jammu in Katra. Our revenue from oncology has come up to 4.5% of our revenues and we expect the oncology services to be one of our focus areas. Infrastructure in Westbank is currently being upgraded to add the second LINAC which will be functional by January and we have also added the bone marrow transplant unit in that setup so that is going to be a comprehensive cancer center in Eastern India. Other than that, we have plans to add cancer facilities at our units at Jaipur and Raipur as well. That is work in progress at the moment. As far as Cayman unit is concerned, as I said earlier, we are very happy to say that in the last quarter, it turned EBITDA positive though at a small level, but it is the beginning of a great story. As far as the capital structure is concerned, I will request my colleague Mr. Kesavan to address that.
- Kesavan Venugopalan:** Hi, Ashish, Kesavan here. So, we have invested around US\$ 23 million in Cayman till date
- Ashish Kumar:** So if I were about to remove the Cayman investment, the capital employed is roughly around INR 1,000 crores.
- Debangshu Sarkar:** It will be around INR 1,000 odd crores. Yeah.
- Ashish Kumar:** And we have a run rate EBIT already of around 195 crores, so we are at 18%-19%, is that correct, ROCE?
- Debangshu Sarkar:** No, run rate EBIT will be a little lower than that. Our EBIT for the first half is around 85 odd crores.
- Ashish Kumar:** I was looking at the second quarter numbers as well.
- Debangshu Sarkar:** If you look at half year number, it is around 85 which annualized will come to 170 and adjusted for the Cayman investment, ROCE will come to around 16%
- Ashish Kumar:** And if I can take the liberty, let's say 12 to 18 months down the line, do you expect this to be in the 20% plus range or is that too much to ask for?
- Debangshu Sarkar:** Ashish, I think we better not guide the performance in terms of any number. I mean we would not hazard a guess on this, but at the same time you will also recognize that it is a function of the

continuous mix that we strive to balance out, I mean obviously you will possibly see us expanding in terms of newer projects. To that extent, the capital deployed gets bloated up and the capital return ratios thus get muted in the short term.

Moderator: Thank you. We take the next question from the line of Bhagwan Chaudhary from Sunidhi Securities. Please go ahead.

Bhagwan Chaudhary: One question on Cayman Islands, can you please comment that earlier we were having plan to raise our equity into that, one is that and secondly, on the same Islands side, this quarter it was EBITDA breakeven, so how do you look forward, we say it is a one-time phenomenon or it is sustainable there?

Ashutosh Raghuvanshi: No, in Cayman Islands we have not planned to increase our stake. We had an option to raise our stake to 50% in 2016 which we did not exercise. The reason is we wanted little more stability and we have complete operational control with minority stake here. So, we would like to continue that and see how the hospital settles down. This is not a one-time phenomenon, there has been a steady growth which has been consistent now for last six months so we expect it only to become better and if I can hazard a guess, there may be certain improvement because of the changes in the US Healthcare Regulation. We do not know at the moment whether the Accountable Care Act will be repealed or whether it will continue but in case the situation in the US remains the way it is today, we expect medical tourism to increase in this facility. So this is a sustainable growth story. Other than that, this hospital has received Joint Commission accreditation also and that has made it very attractive for the entire Caribbean region. So this is likely to be a very sustainable operation.

Bhagwan Chaudhary: And second, can you please give some comment on Vaishno Devi operations, I think we commenced 5-6 months back, so how it is there and what kind of revenue and losses were there in this quarter?

Ashutosh Raghuvanshi: As we said earlier, this is the EBITDA neutral or viability gap funded PPP project. The result of this project is very encouraging. Currently, the hospital has been seeing close to 300-400 odd patients with an occupancy of over 50 beds. So we expect this hospital to do reasonably well in short term as well as long term. There is a provision where the Shrine Board provides support for any gap in the viability. There are no losses associated with this project for NH.

Bhagwan Chaudhary: So, can you please quantify sir, how much that quantum was?

Kesavan Venugopalan: I do not think we will do that, may be possibly when the results are published for each of the subsidiaries at the year end, maybe I think we would have a look at it.

Moderator: Thank you. We take the next question from the line of Nitin Agarwal from IDFC Securities. Please go ahead.

- Nitin Agarwal:** When we look at the different clusters, age profile clusters that we have, how do we see the profitability progress across these clusters over the next 2-3 years' timeframe, do we still see possibility for margin expansion in the matured cluster and how do you see the profitability in the other clusters?
- Ashutosh Raghuvanshi:** Absolutely. The matured hospitals have been showing a healthy growth of about 13% in this quarter. We expect to improve this by adding additional services, changing the case mix and also adding new technology, etc. For example in the cancer hospital, we added robotic surgery program couple of months back which has taken off very well and similarly, we also added a 30-bedded platinum service ward which provides high-end service offerings and these kind of initiatives will continue the momentum of growth in the matured hospitals. Now as far as the overall clusters are concerned, the Eastern cluster contributes around 38% of the revenue. We expect all the clusters to become almost of an equal size, though currently the Karnataka cluster is slightly bigger and the Eastern cluster is at the second position and the rest of the units come at the third place. But as we go forward, all these clusters are likely to grow and come to a similar level. Within the existing cluster of Bangalore of South, also we see that there are certain areas and opportunities which may come as the growth of healthcare providers in the city has been slightly towards one side of the city. So we expect that there may be opportunities within our given clusters as well where we not only have a very strong brand recall, but we also have an infrastructure which we can leverage upon and create a quicker turnaround even for a newer facility or possible acquisitions.
- Moderator:** Thank you. We have the next question from the line of Dheeresh Pathak from Goldman Sachs. Please go ahead.
- Dheeresh Pathak:** You mentioned two hospitals from which you have withdrawn, decided to exit Lucknow and one more you mentioned, can you just talk about the reasons in more detail, why you decided to exit?
- Ashutosh Raghuvanshi:** We decided to exit from Lucknow because of non-conformance by the counterparty with regards to our requirements in terms of the building which they were supposed to provide us. So that was the main reason why we terminated the agreement for this prospective hospital. However, the facility in Berhampore was a part of the acquisition we did in 2014. This was a small hospital with secondary care facilities. As a part of our strategy, we continuously evaluate such projects and in line with the same, post our assessment of the entire business mix of the Eastern cluster, decided that this facility should be discontinued as it is not very useful in the long-term interest of the business and it was not a very significant part of the business anyways.
- Dheeresh Pathak:** So Lucknow was yet to be operational.
- Ashutosh Raghuvanshi:** Yes, it was yet to be operational. It was a future project.

- Dheeresh Pathak:** Where the land and the building would have been owned by the builder and you would have leased the premises.
- Ashutosh Raghuvanshi:** That is correct.
- Dheeresh Pathak:** And can you just briefly talk about the economics of the managed beds because in the PPT in the revenue split, it does not show up, although you have around 700 managed beds, but in the business mix which is on slide #5 on the top right hand side chart, it does not have any share in the revenue mix. Is it capital or something else?
- Debangshu Sarkar:** It has been captured as a part of the other ancillary businesses within the business mix pie which denotes a figure of 2%, but other ancillary businesses does include other items like let us say teleradiology, learning and development, clinics, so on and so forth. Standalone, only the managed hospitals business contributes 0.1% of our total operational revenue.
- Dheeresh Pathak:** Can you just explain that what capital do you bring to such beds and then what do you do and why does not it have a large share in the revenue?
- Ashutosh Raghuvanshi:** There is a background to these particular projects. These are essentially CSR projects for some other groups and since they do not have the expertise in managing hospitals, they have requested us to help them manage these facilities. So how they add value to us is that they usually fall in an area where we can expect referrals of patients into our base of hospitals in that region. All these hospitals are essentially secondary care hospitals run by other larger corporates as their CSR initiative. So as a model, we do not like to do managed hospitals where we do not own the P&L. These projects add to the overall strength of the network in terms of patient referral channels.
- Moderator:** Thank you. We take the next question from the line of Jackson Yeow from Eden. Please go ahead.
- Jackson Yeow:** I would like to just check with you, in your presentation slide on the profitability snapshot as you said in cost structure, the cost actually decreased from 89.5% to 87.7%. In this case, I realized that the other expenses actually decreased from 25.2% to 24.1%, could you share with me what constitute other expenses?
- Debangshu Sarkar:** These other expenses are primarily the administrative overheads in the form of power and fuel expenses, the rent and revenue share expenses, the repair and maintenance expenses as well as the business promotion expenses. These four broad heads constitute the bulk of those other expenses that you see over there.
- Jackson Yeow:** Because we have been following Narayana for quite a while now and we are very impressed with the value that the management has shown, so I was just considering would you consider to acquire any eye specialty hospitals, values are congruent and aligned to your mission of providing low cost healthcare, something like that, eye facility for example.

- Ashutosh Raghuvanshi:** We do run an eye facility in Eastern India; however, we have not scaled that up. We believe that eye business is primarily a retail kind of business which is very different from our core strength. At the moment, we would not really look at that, but as a part of larger ecosystem of healthcare, we could look at it in future, but at the moment we have no plans to consider eye care.
- Jackson Yeow:** How about renal care?
- Ashutosh Raghuvanshi:** Renal care is a very important part of our portfolio, currently about 8.4% of our revenue comes from renal care. There is a large number of dialysis units we have and we also do a significantly large number of transplants across five of our centers. We expect that service to grow further as you know that the incidences of diabetes as well as hypertension are very high in India and these two diseases make people prone to renal diseases. We see that as a growth segment for us.
- Moderator:** Thank you. That was the last question. I now hand the conference over to the management for their closing comments. Over to you.
- Debangshu Sarkar:** We thank all of you for being there for our investor call. Thanks for the participation and thanks for the insightful questions that you guys asked. Should you have any further queries or clarifications, feel free to touch base with us directly at any point of time. Thanks a lot and look forward to interacting with you guys going forward as well.
- Moderator:** Thank you. On behalf of Narayana Hrudayalaya Limited that concludes this conference. Thank you for joining us. You may now disconnect your lines.