ViewCube

March, 2023

Reading the vitals

CRISIL Ratings view on the hospital sector

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An S&P Global Company

CRISIL ViewCube on the hospital sector

ViewCube is a compilation of sector views expressed during CRISIL's webinars. These include CRISIL's own views, those of stakeholders, and those emanating from a poll done during the webinar.

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Section 1

Our view

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Key messages

Steady 10-11% revenue growth seen in fiscals 2023 and 2024

- Bed additions, healthy occupancy and maintenance of average revenue per bed occupied (ARPOB) to support growth
- Recovering demand for medical tourism and increasing insurance penetration augur well for the sector
- Large hospital chains to grow at a faster pace owing to stepped-up expansion plans

Operating margin to moderate 200-250 basis points (bps) to ~16.5%; remain higher than the pre-pandemic level

- Doctor/medical staff expenses, pre-operative costs to go up due to augmented bed addition target
- Small hospitals to see steeper decline in profitability compared with large hospital chains

Capex, including brownfield investments, to hit an all-time high

- Annual addition of ~3,000 beds seen in fiscals 2023 and 2024 compared with ~8,000 beds added during fiscals 2018-2022
- Total capex estimated at Rs 12,000–13,000 crore over fiscal 2023 and 2024; ~Rs 20,000 crore was spent in the past five fiscals

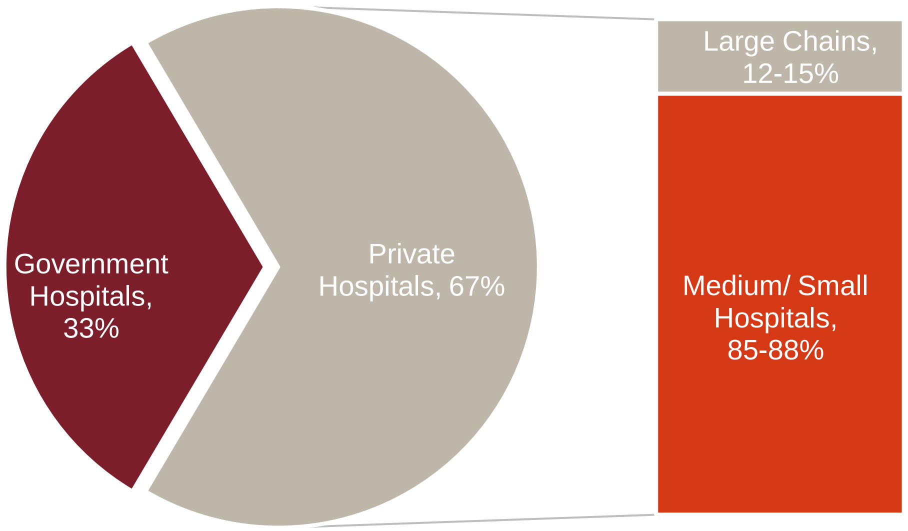
Credit outlook to remain ‘Stable’ despite high capex intensity

- Healthy cash accrual to limit material debt addition, keeping debt protection metrics comfortable
- Large hospital chains to see more bed additions, benefitting scale of operations
- Debt metrics of smaller hospitals to moderate, but remain adequate

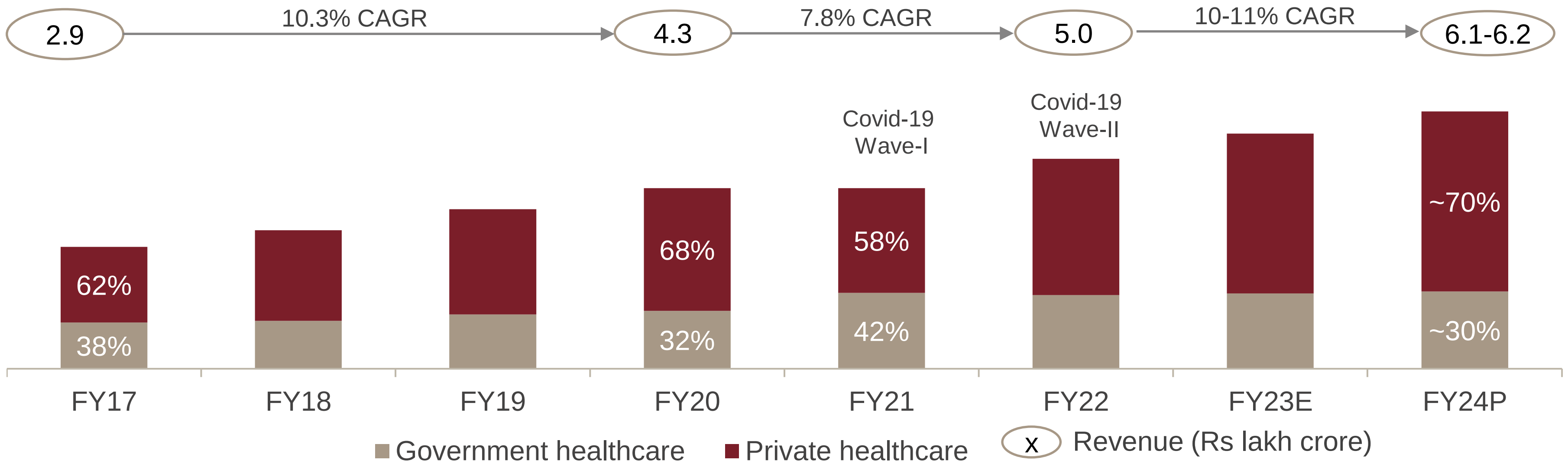
Outlook on revenue growth and profitability

Revenue to grow in double digits in fiscals 2023 and 2024…

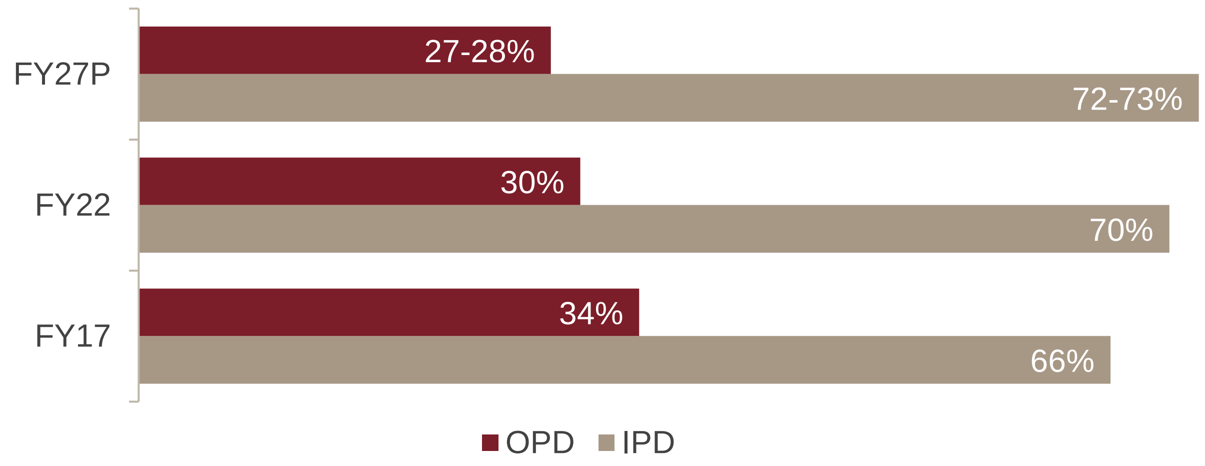
Industry dominated by private hospitals



Private hospitals bounce back, will continue to outpace government hospitals in growth



Share of IPD increasing steadily over the years

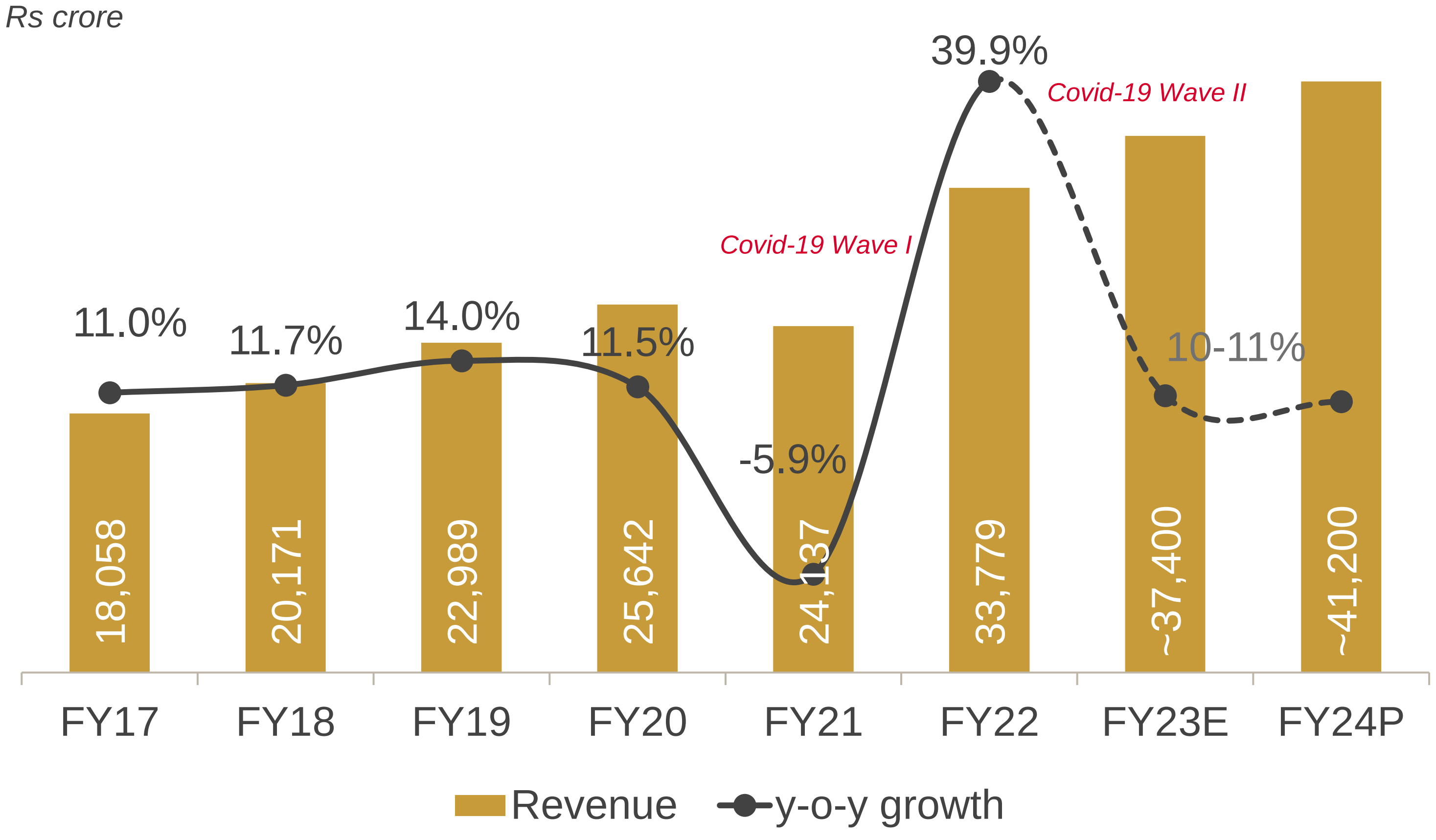


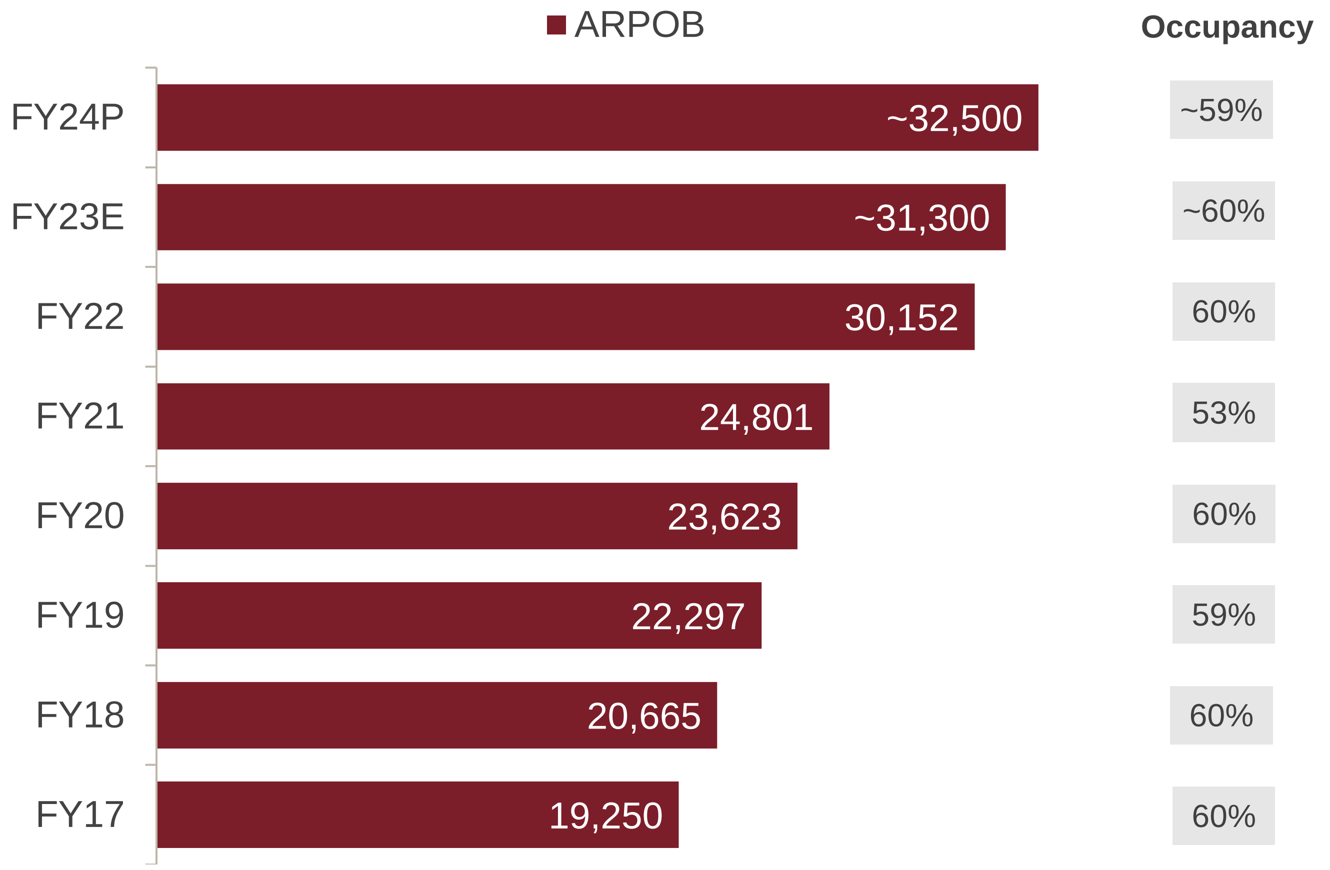
- Share of private hospitals to increase to nearly 70% by fiscal 2024 on the back of higher growth
  - In fiscal 2021, during the first wave of Covid-19, the share dropped to 58%, but recovered to 65% thereafter
- Private hospitals estimated to grow at a faster pace of 11-12% in fiscals 2023 and 2024, vis-à-vis 7-8% for government hospitals
- IPD (in-patient department) share to rise to 72-73% by fiscal 2027 from ~66% in fiscal 2017

Source: CRISIL MI&A Research, company annual reports

Growth to normalise to the pre-pandemic level

Increasing share of complex surgeries to support average revenue per bed occupied (ARPOBs) going forward





- After significant recovery in fiscal 2022, revenue growth to stabilise to the pre-pandemic level of 10-11% on healthy growth drivers
- Large hospital chains to post 100-200 basis points (bps) higher growth compared with medium/small hospitals, benefitting from scale of operations
- ARPOB expected to rise 3-4% hereon, compared with 6-8% before the pandemic, driven by continued organic and inorganic expansion, and occupancy to remain healthy at 59-60%

Source: CRISIL Ratings, company annual reports
Large hospitals: Revenue ≥ Rs 500 crore
Medium/ small hospitals: Revenue < Rs 500 crore

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Factors that will boost growth

Growth drivers

Structural growth drivers

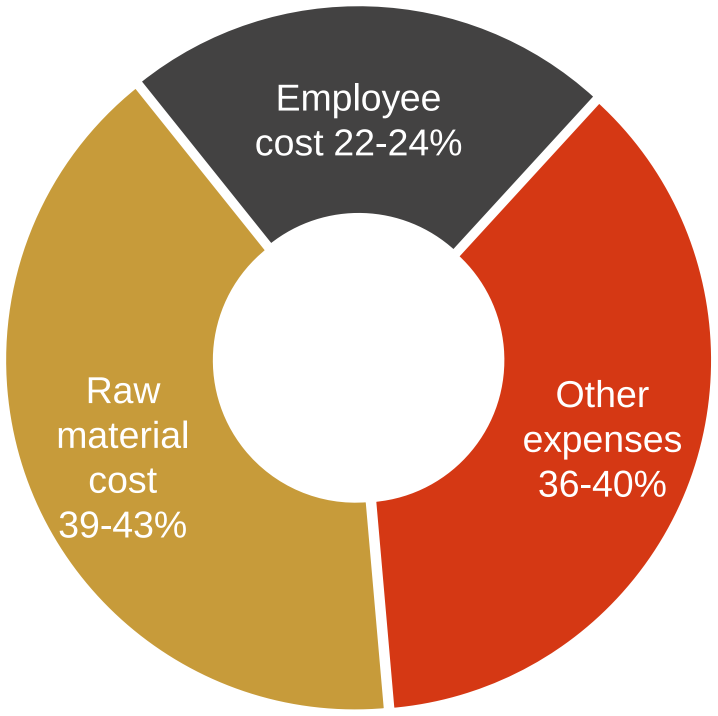
- Ageing population
- Income demographics
- Rising non-communicable diseases
- Public health expenditure

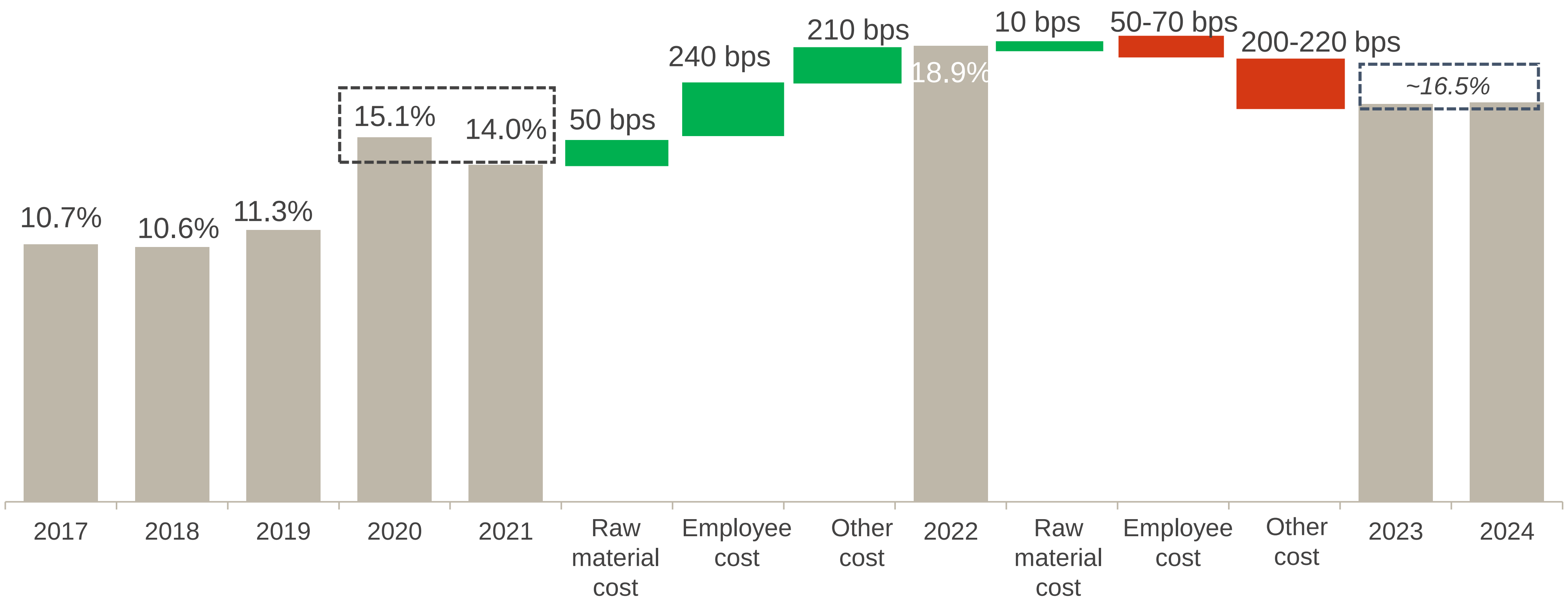
Immediate growth drivers

- Insurance penetration
- Medical tourism

Operating margin to moderate, but stay above the pre-pandemic level

Covid-19 and allied treatments during second wave, pent-up demand for elective surgeries led to all-time-high operating margin in fiscal 2022





- Operating profitability seen moderating 200-250 bps to ~16.5% in fiscals 2023 and 2024, but to remain above the pre-pandemic level, driven by:
  - Improvement in gross margin on account of higher share of complicated surgeries
  - Steady average revenue per bed
  - Sustenance of occupancy despite continued bed expansion
- Operating profitability was boosted by increase in Covid-19 and allied treatments and better operating leverage in fiscal 2022

Source: CRISIL Ratings, company annual reports

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Credit outlook remains 'stable'

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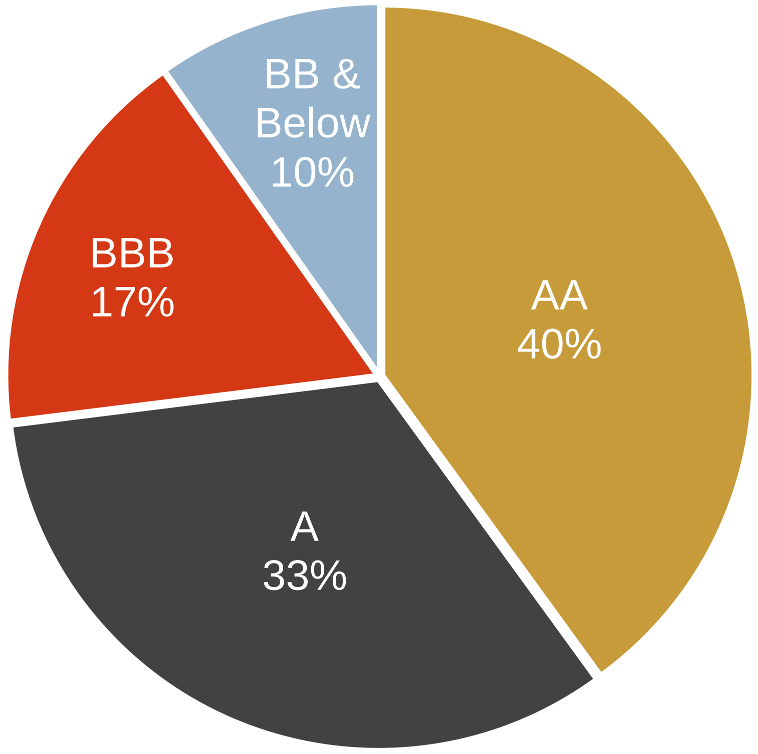
CRISIL Ratings has a wide coverage of the hospital sector

- Outstanding ratings on 87 companies with revenue of ~Rs 41,000 crore (~7.5% of sector revenue) and rated debt of ~Rs 11,300 crore
- Well-diversified portfolio covering large hospital chains and standalone hospitals across India
- About 60% of the companies in investment grade with median rating of ‘CRISIL BBB-’

Rating distribution



Large hospitals majorly comprise high-rated players

Company name	Long-term rating	Short-term rating	Outlook
Apollo Hospitals Enterprise Ltd	CRISIL AA+	CRISIL A1+	Stable
Fortis Healthcare Ltd	CRISIL AA-	CRISIL A1+	Positive
Krishna Institute of Medical Sciences Ltd	CRISIL AA-	CRISIL A1+	Positive
Yashoda Healthcare Services Pvt Ltd	CRISIL AA-	-	Stable
Global Health Ltd	CRISIL A+	CRISIL A1+	Positive
Quality Care Hospitals Ltd	CRISIL A+	CRISIL A1+	Positive
Kailash Healthcare Ltd	CRISIL A-	CRISIL A2+	Stable
Sahyadri Hospitals Pvt Ltd	CRISIL A-	CRISIL A2+	Stable

Source: CRISIL Ratings

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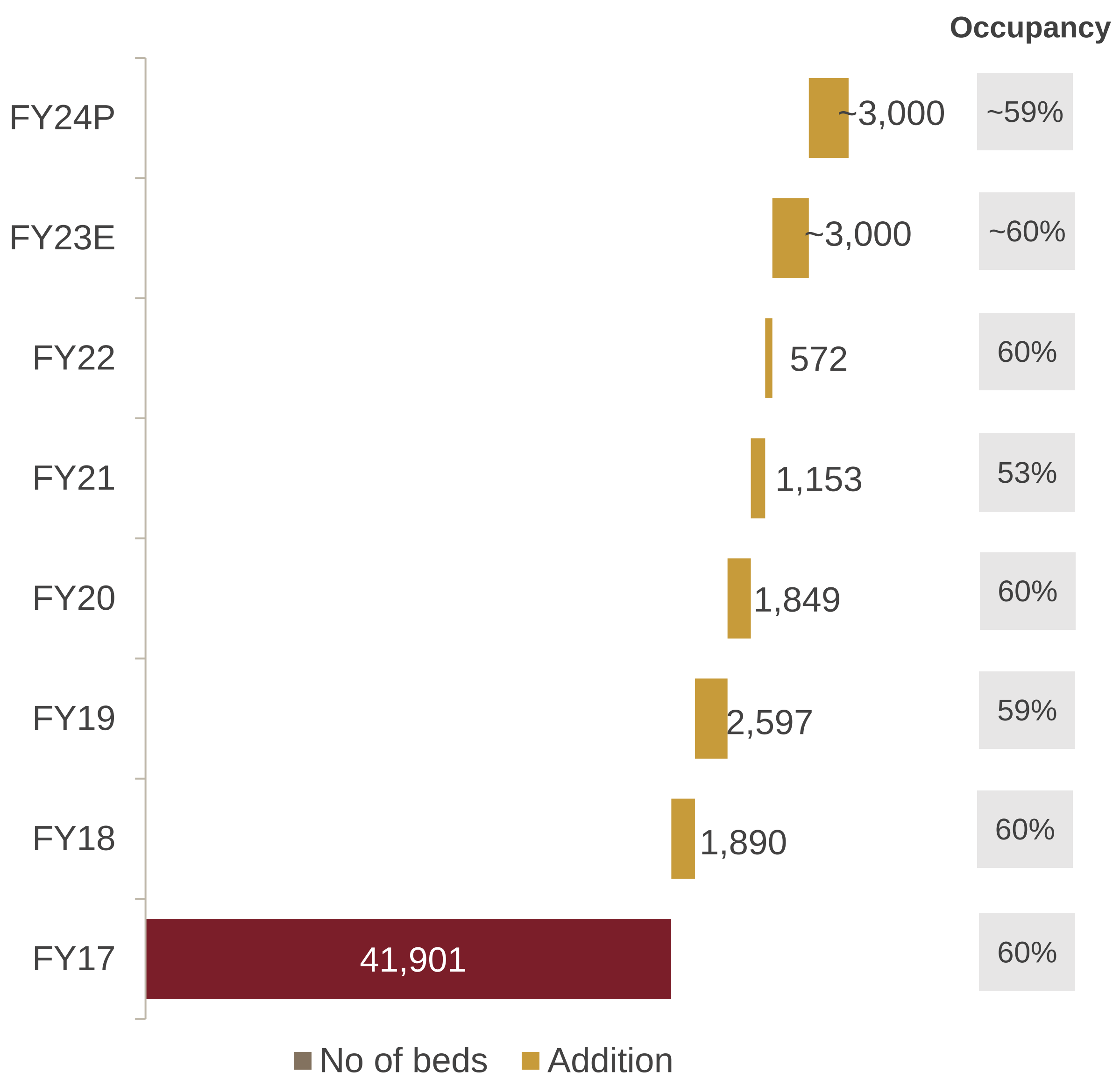
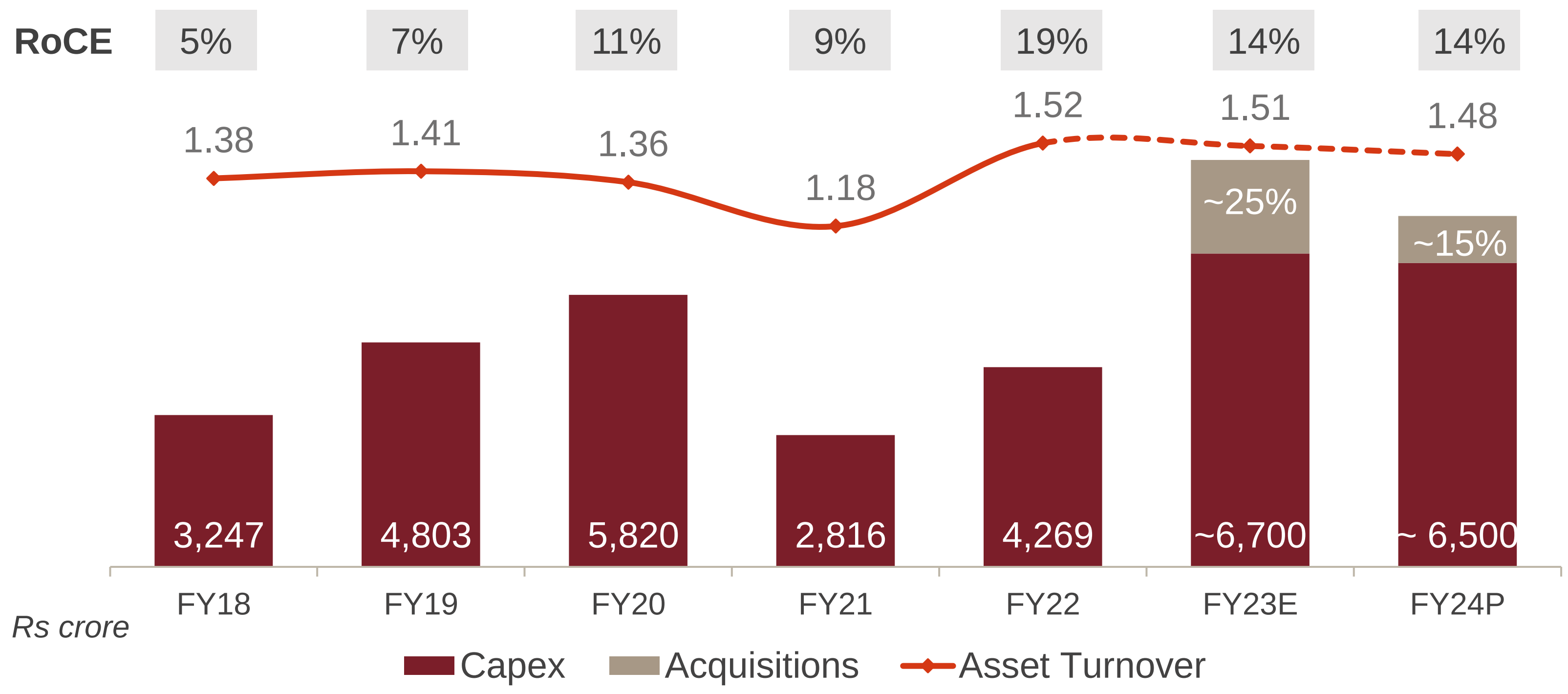
Significant pick-up in bed addition post pandemic-led slowdown





- Large hospital chains dominate the rated portfolio, accounting for about two-thirds of total beds
- Expansion slowed significantly in fiscal 2022, due to disruptions amid Covid-19
- Capex picked up in fiscal 2023 and will continue in fiscal 2024, comprising greenfield as well as brownfield investments
- Healthy occupancy to keep RoCE healthy at 14-15%, despite increased capex intensity

Source: CRISIL Ratings, company annual reports

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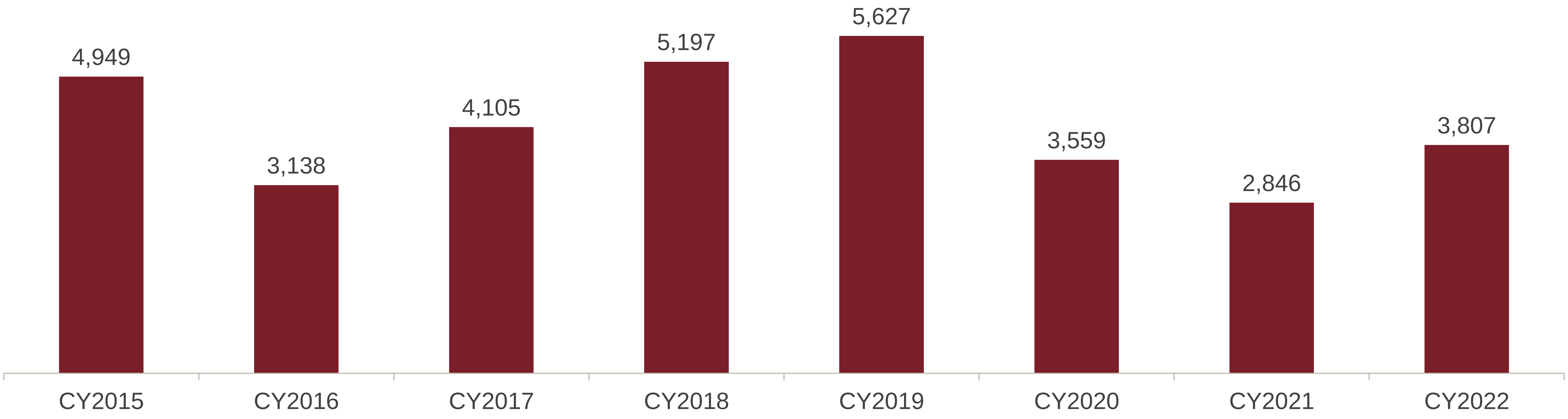
Strong prospects and high returns attract investments

Rs crore



Major deals in the past two years

- ASG Eye Hospital raised ~Rs 1,500 crore, led by General Atlantic and Kedaara Capital
- Dr Agarwal's Hospital raised ~Rs 1,050 crore from TPG and Temasek Holdings
- National Infrastructure Investment Fund invested ~Rs 2,100 crore in Manipal Hospitals for an undisclosed stake

Capital market activity in the past two years

- Global Health Ltd, Krishna Institute of Medical Sciences and Rainbow Children's Medicare Ltd together raised almost Rs 6,000 crore through an IPO in 2021 and 2022
- Cloudnine Hospitals and Park Group of Hospitals to raise more than Rs 3,500 crore through IPOs

Source: CRISIL MI&A Research, CRISIL Ratings

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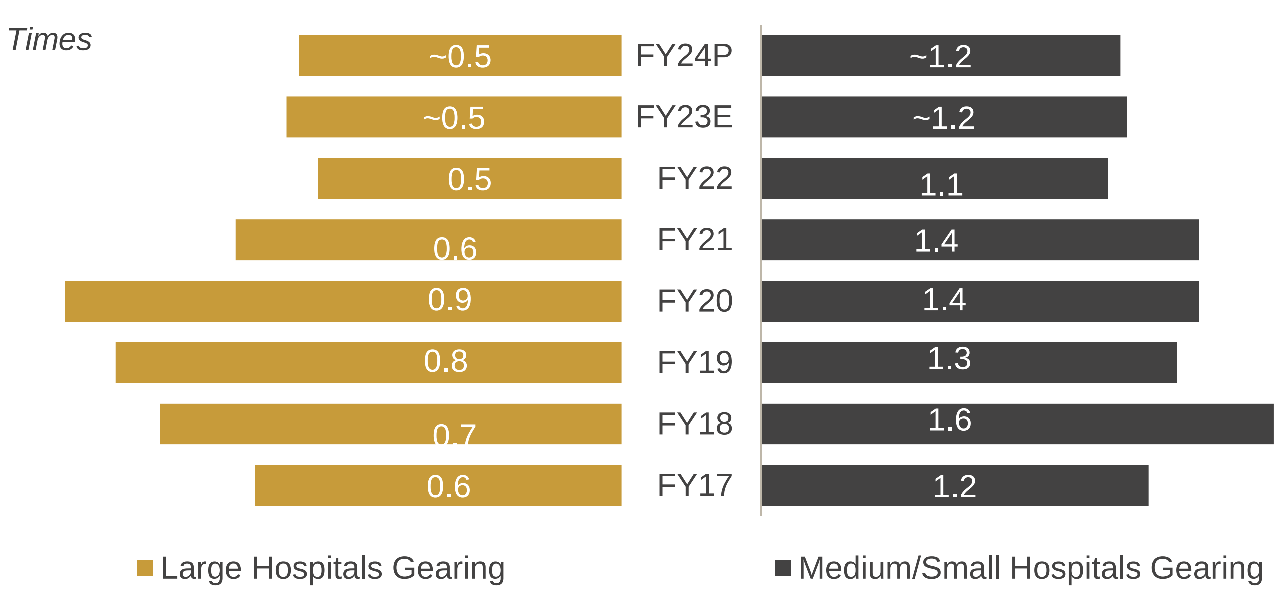
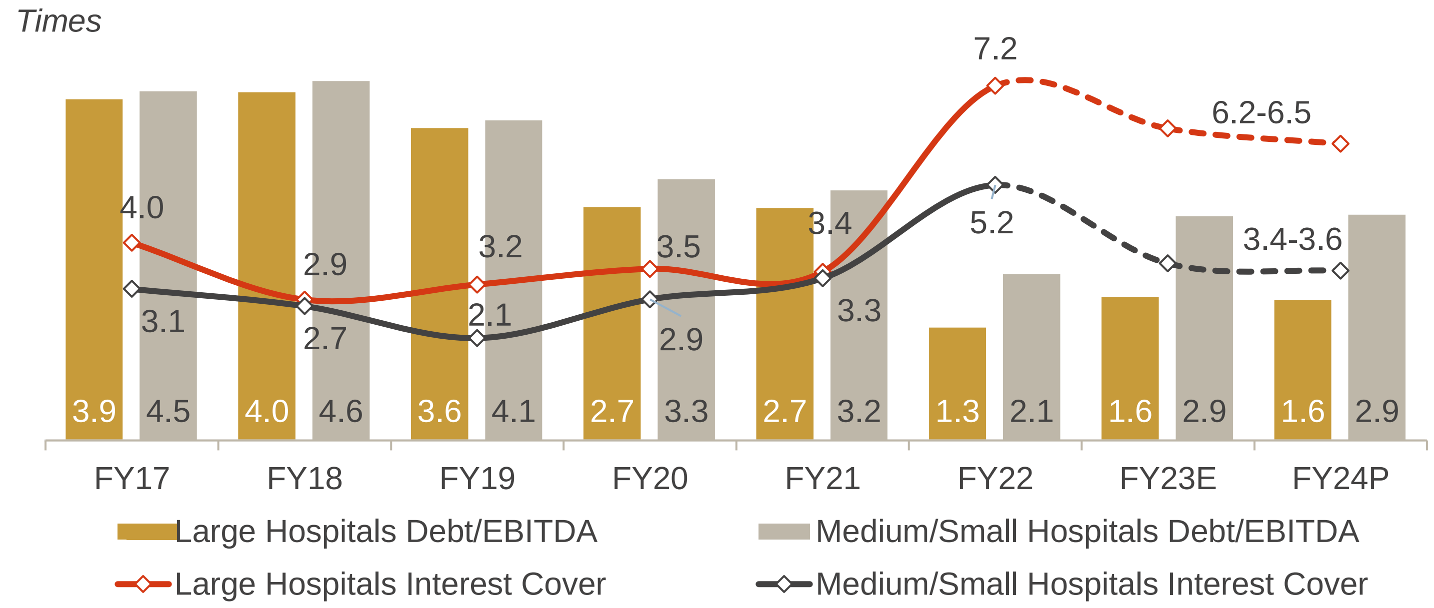
Credit profiles to remain stable on strong accrual, limited debt addition

Healthy gearing aided by strong accrual, fund raising

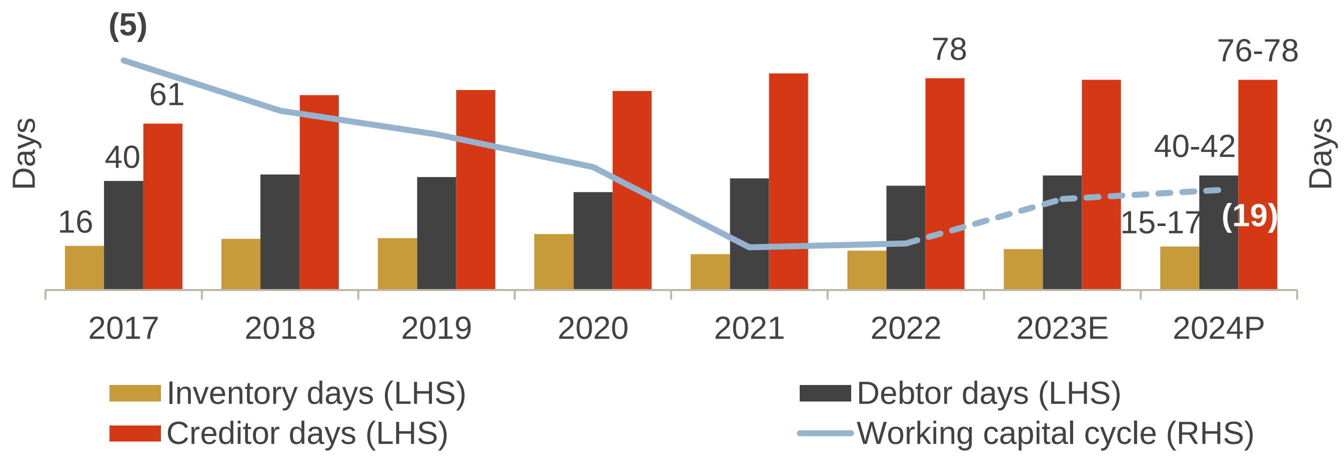


Improvement in key debt protection metrics to sustain

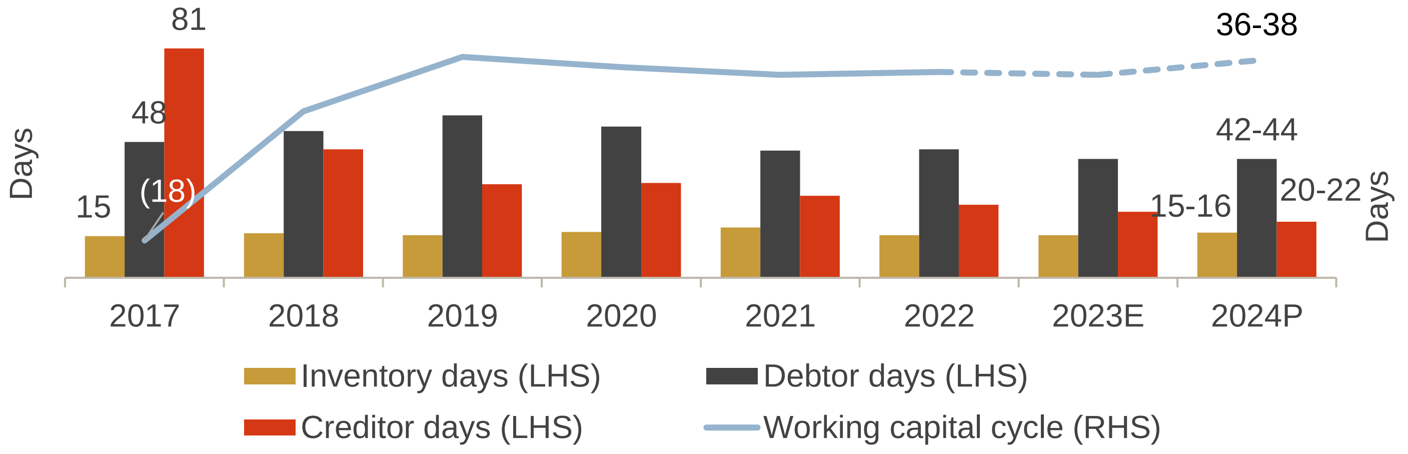


Working capital needs well managed; net working capital cycle for large hospitals is negative, unlike for medium-sized/ small hospitals

Large hospitals



Medium-sized/ small hospitals



Source: CRISIL Ratings; NWC: Net working capital cycle (in days)

Large hospitals: Revenue ≥ Rs 500 crore
Medium-sized/ small hospitals: Revenue < Rs 500 crore

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Emerging trends

To summarise

- Revenue growth seen at 10-11% in fiscals 2023 and 2024, with larger hospitals witnessing slightly higher growth than medium-sized and small hospitals
- Operating margin to moderate 200-250 bps to ~16.5% in fiscal 2023 and remain stable in fiscal 2024; to stay above the pre-pandemic level
- Capex intensity seen rising in fiscals 2023 and 2024 to cater to healthy growth prospects, given stronger balance sheets due to healthy cash generation in the past; some hospitals have also raised funds through IPOs
- Debt protection metrics to remain adequate despite higher capex intensity, lending stability to credit profiles
- Risk monitorables
  - Resurgence in Covid cases, resulting in lockdowns and travel restrictions, and the impact on elective procedures
  - Additional regulatory measures regarding cost of treatment

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Section 2

Their view

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Views excerpted from a panel discussion during the webinar (1/4)

Eminent panelists

Krishnan Akhileswaran
Group Chief Financial Officer
Apollo Hospitals Enterprise Ltd

Vivek Kumar Goyal
Chief Financial Officer
Fortis Healthcare Ltd

Sandhya J
Group Chief Financial Officer
Narayana Hrudayalaya Ltd

Revenue growth to remain in low double digits, driven by sustenance of higher occupancy and ARPOB

- Occupancy expected to remain stable despite significant bed additions, driven by:
  - Increase in lifestyle diseases resulting in higher hospitalisation amongst youth
  - Increased focus on preventive health check-ups, early detection, and lifestyle changes to prevent the onset of these diseases
  - Rising awareness of benefits of early hospitalisation
  - Investments in equipment to improve quality and attract more patients
- Recovery of medical tourism to the pre-pandemic level supported by the ‘Heal in India’ campaign to push up occupancy
- ARPOB, currently at a historical high, to sustain because of change in treatment mix, including increased demand for complex surgical work and preference for high-quality service
- Increased insurance penetration to also support ARPOB
- ARPOB to increase at a slower pace over the medium term owing to limited healthcare affordability for a large portion of the population

Views excerpted from a panel discussion during the webinar (2/4)

Increased role of medical tourism in the overall healthcare growth story

- Medical tourism is one of the critical drivers of revenue growth in the healthcare sector
- However, the pandemic led to a drastic reduction in medical tourism due to travel restrictions and fear of infection
- Effective measures by the industry and government amid the receding impact of the pandemic have restored faith amongst international tourists, translating into a significant recovery
- As a result, growth over the medium term is expected to surpass the pre-pandemic level

Operating margin to be impacted by inflationary pressure in the short term

- Higher overheads and material cost because of inflation will impact operating profitability over the short term
- However, with the increase in scale over the medium term, benefits accruing from better operating leverage will support profitability

Digital pharmacies to continue facing headwinds

- Digital pharmacies offering high discounts are not sustainable as funds dry up. As a result, the sector is facing headwinds. Profitable growth will take time and discounts may be scaled down in the near future
- That said, digital pharmacies are here to stay as the convenience factor remains a significant driver for customers
- Focus is shifting towards utilising available funds for profitable growth rather than scaling up

Views excerpted from a panel discussion during the webinar (3/4)

Increased capex intensity to sustain over the medium term

- India requires significantly more hospital beds than currently available, indicating growth potential for the sector. Consolidation is gaining traction among hospitals, particularly at the regional level
- Capex may be limited to large players with access to capital
- Excluding land cost, putting up a hospital costs the same across locations, but realisations are lower in non-metros, making them less viable. Also, many non-metro cities are covered by government hospitals and schemes, further reducing their viability for private players
- However, a change is imminent with a change in purchasing power parity and government initiatives for smart cities
- With Tier 2 and Tier 3 cities offering huge opportunities, it is imperative to increase the number of medical colleges to ensure adequate supply of doctors
- Limited availability of land in metros poses a challenge for setting up hospitals. Non-metro cities are emerging as strong growth areas with significant opportunity for expansion
- The government needs to provide more incentives to encourage private investment in healthcare infrastructure in underserved areas to improve healthcare accessibility

Views excerpted from a panel discussion during the webinar (4/4)

Regulatory aspects and healthcare affordability

- The government has stressed on expansion of affordable and accessible healthcare to more people
  - Universal Health Program launched to increase access to healthcare, but more efforts are needed on the supply side to achieve the desired results
- The government is considering price caps on multiple formulations to make healthcare more affordable for the masses. However, this may lead to de-empanelment of certain private hospitals from government schemes
- To improve access to healthcare, focus needs to be on universal insurance coverage. This will help people avail quality healthcare services without worrying about the cost
- Also, the quality of healthcare in government facilities needs to be improved for those who cannot afford private hospitals
- Higher real estate and raw material expenses have increased costs of operation for hospitals. At the same time, hospitals are expected to maintain affordability and accessibility for patients. As hospitals adopt newer and efficient technologies such as robotics, the cost of care is likely to increase further, requiring innovative regulatory solutions to maintain accessibility and affordability for patients
- To address these challenges, hospitals may require regulatory support in the form of incentives or subsidies to mitigate the impact of rising costs

Section 3

Poll questions

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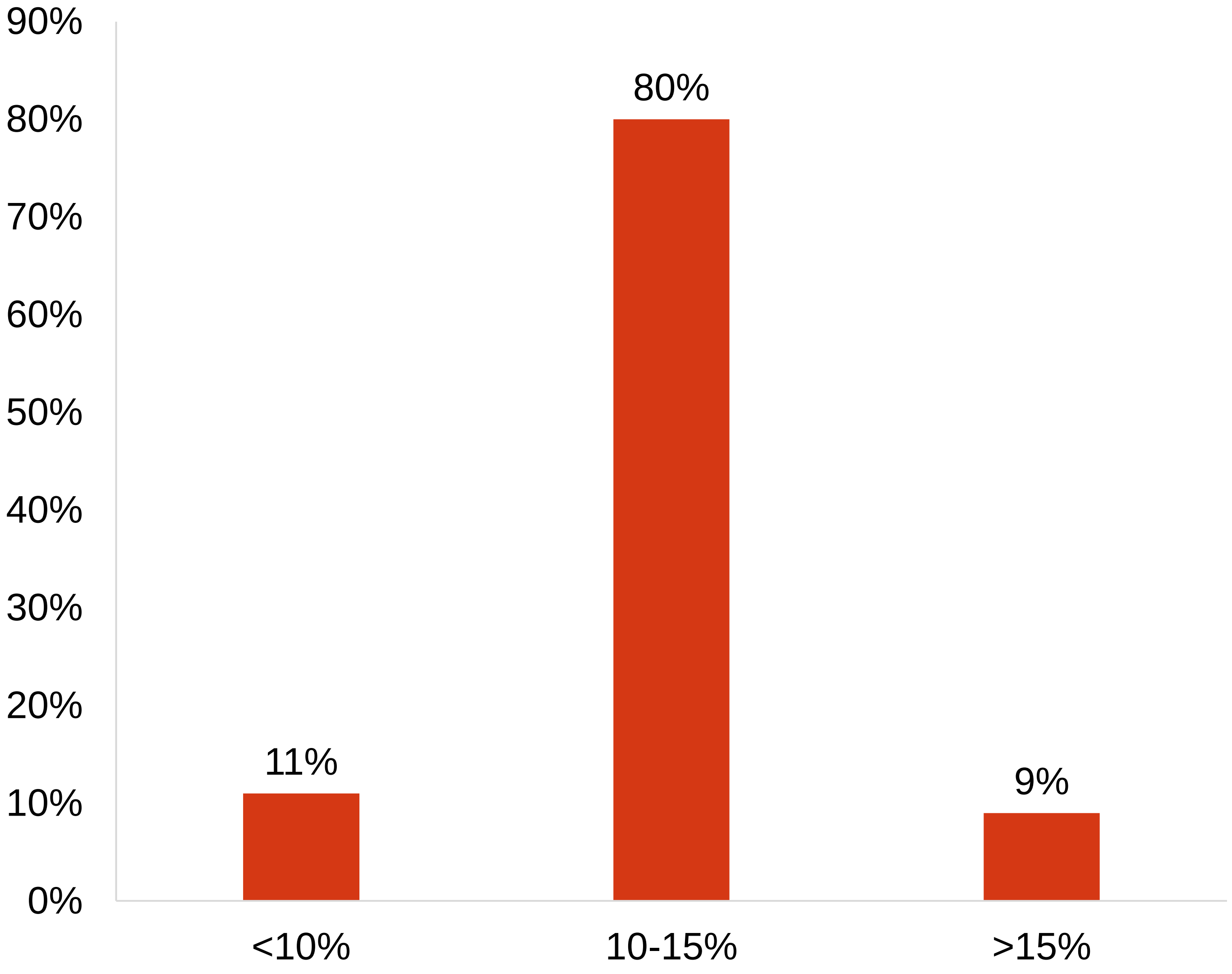
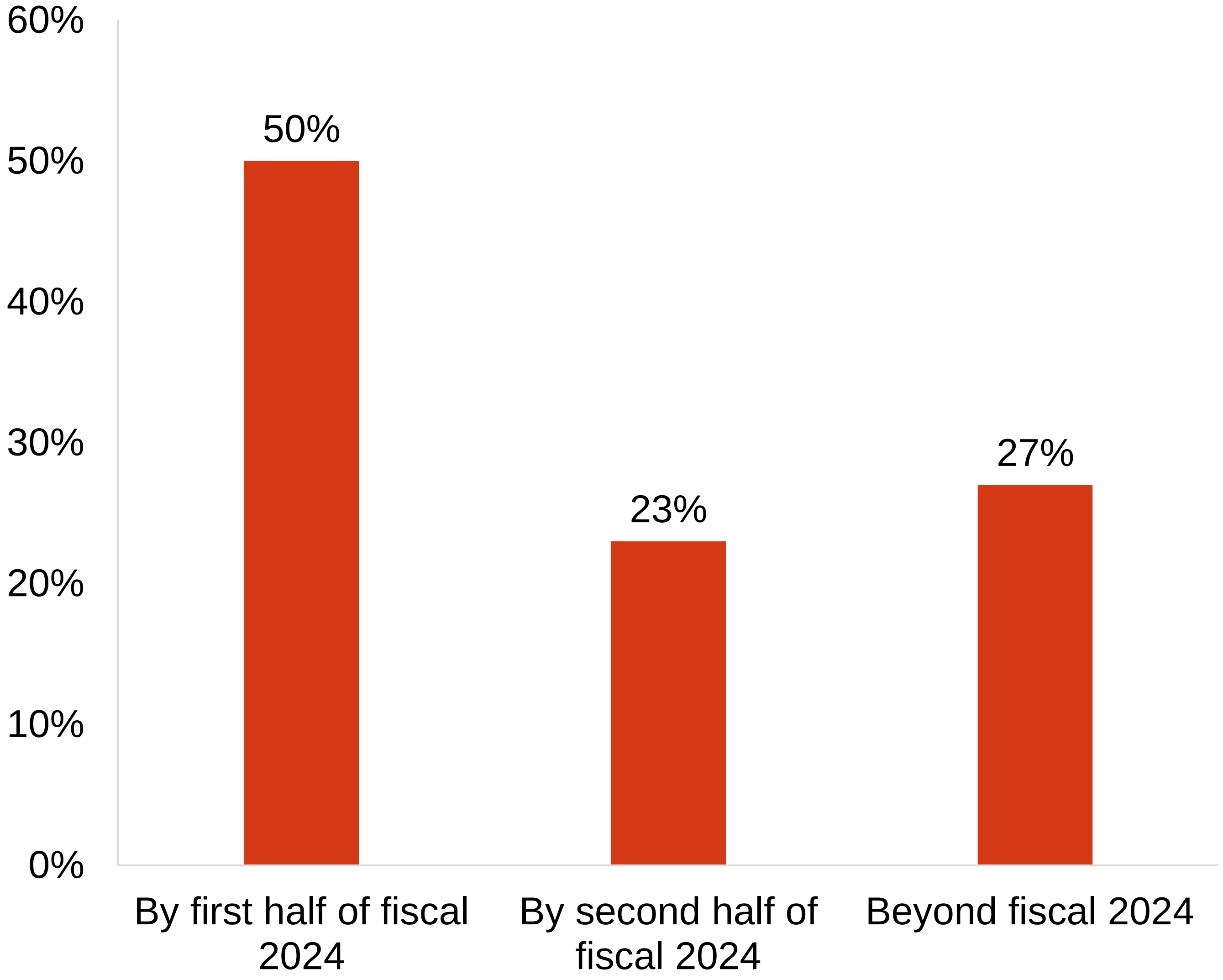
Results of a survey of more than 300 webinar participants (1/3)

Q1. What is your expectation of revenue growth in the hospital sector in fiscal 2024?



Q2. When do you expect medical tourism to recover completely?



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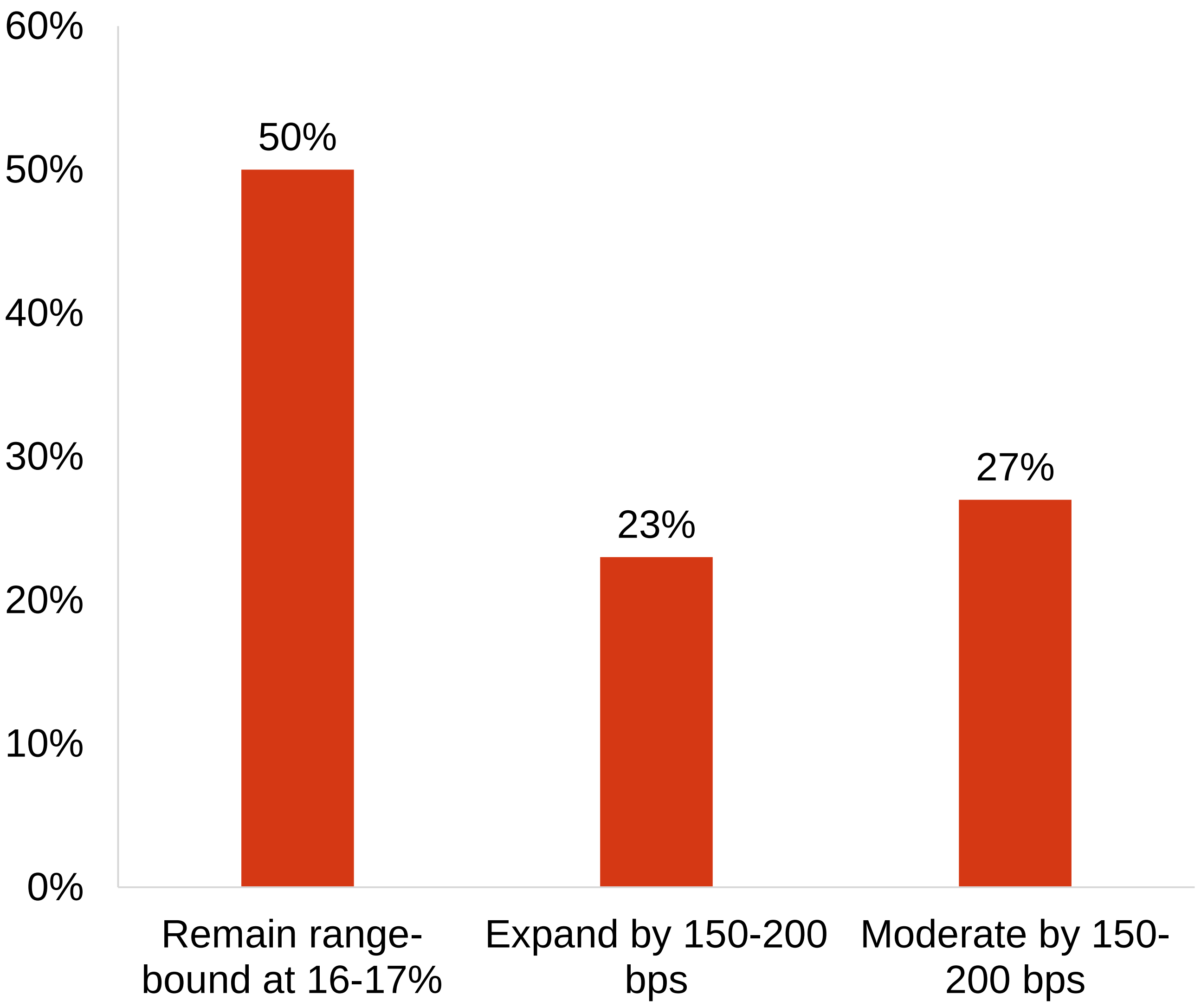
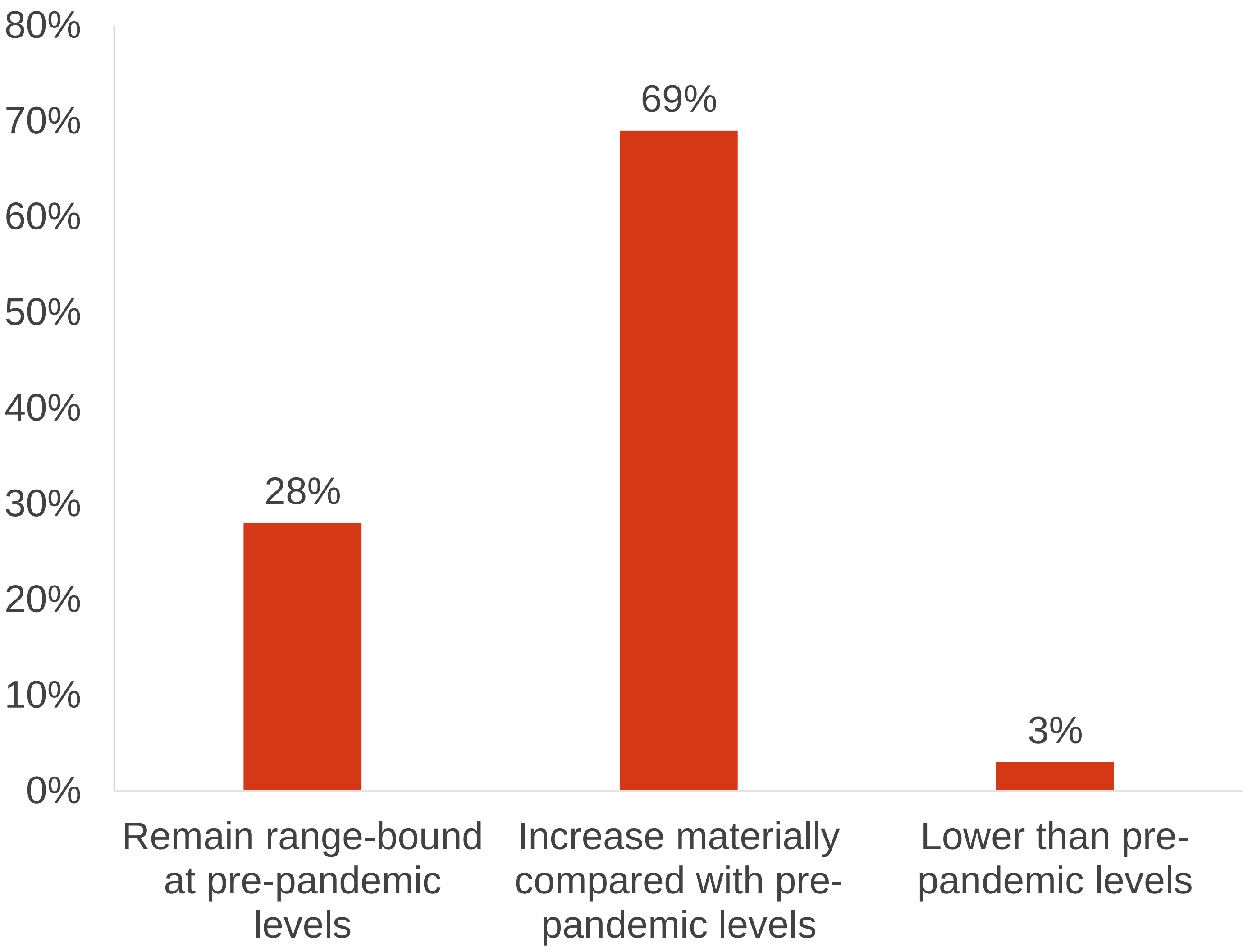
Results of a survey of more than 300 webinar participants (2/3)

Q3. What is your expectation of operating margin for the sector in fiscal 2024 vis-à-vis fiscal 2023?



Q4. Given the healthy structural growth drivers, what is your expectation of capex intensity in the next 2-3 years?



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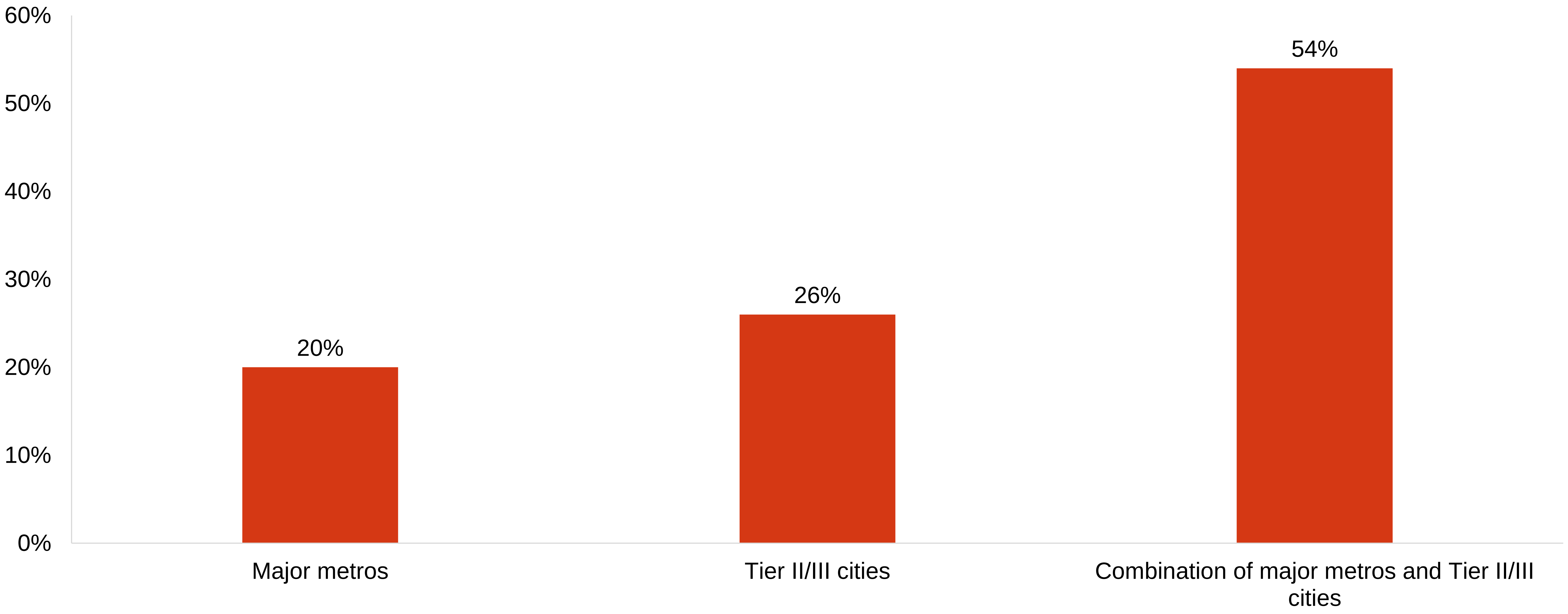
Results of a survey of more than 300 webinar participants (3/3)

Q5. Where do you expect major expansion by hospitals?



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Thank you

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