Apollo Hospitals Enterprise Limited

Q1 FY16 Earnings Conference Call Transcript
August 12, 2015

Mayank Vaswani: Good afternoon and thank you for joining us on this call to discuss the financial results of Apollo Hospitals for Q1 FY16 which were announced yesterday. We have with us the Senior Management Team comprising Ms. Suneeta Reddy – Joint Managing Director, Mr. S. K. Venkataraman – Chief Strategy Officer and Mr A. Krishnan - Chief Financial Officer.

Before we begin, I would like to mention that some of the statements made in today's discussions may be forward looking in nature and may involve risks and uncertainties. For a complete listing of such risks and uncertainties, please refer to our investor presentation.

We will start with Ms. Suneeta Reddy who will discuss the operating highlights for the quarter following which Mr. Krishnan will discuss the operating metrics, expansion plans and other highlights. Documents relating to our financial performance have been shared with all of you earlier and have also been posted on our corporate website. I now invite Ms. Suneeta Reddy to touch upon the key highlights of our performance.

Ms. Suneeta Reddy: Good afternoon everyone and thank you for taking out time to join our call.

We have started this fiscal on an exciting & eventful note with a strong financial performance. We extended our presence into the north eastern region of the country by entering into an agreement with 220 bedded Assam Hospitals to acquire 51%, we have also relaunched Nova Specialty Centers as Apollo Spectra Hospitals, integrated operations of Hetero Pharmacy apart from making progress on our organic expansion plan.

I am delighted to inform you that our revenues during Q1 grew by 20% on a year on year basis. This was accompanied by an EBITDA growth of 16%. This performance was driven by a growth of 12% in hospital services revenues. The Existing Hospital EBITDA margin grew to 24% from 22.5%. This is also supported by a strong 35% growth in our Standalone Pharmacy business. With the improved economic outlook we expect to sustain the momentum in revenues.

New hospitals have reported a 91% growth in revenues on a y-on-y basis aided by outstanding performances by Jayanagar and Vanagaram. Trichy and Nashik have not performed up to expectations but with the recent additions of new consultants we anticipate an improved performance from these 2 hospitals in the quarters ahead. New Hospitals at Nellore and OMR are in the initial stage of operations have reported encouraging volumes. The Indore Hospital in which we acquired a majority stake in the last fiscal has seamlessly transitioned to the Apollo way of functioning and we are already witnessing an improved EBITDA profile at this facility.

EBITDA margins for existing health care services have improved both on a yearly basis as well as on a sequential quarter basis. However we have reported higher EBITDA losses in new hospitals primarily due to the addition of OMR, W&C – SMR in Chennai & Nellore all of which were commissioned in Q4FY15. As stated last quarter, we have started disclosing EBITDAR numbers for the hospitals business as well as Standalone Pharmacies. The focus over the next 3 Quarters will be to increase volumes which should help us report better margins. However you should expect some costs on Advertisement & Marketing beginning Q2FY16.

For the coming year the expansion plans are on track and you will see us adding another 800 beds across Navi Mumbai, Malleswaram & Vizag. With over 30% of new capacity of beds added by end of this fiscal our strategy over the next 2 years is to strengthen our dominance in the existing clusters while ramping up volumes and operations in the new hospitals. Across all our mature hospitals we are looking at greater operational efficiencies with the twin objective of both reducing costs as well as augmenting our clinical capabilities and service quality. In the new hospitals the focus is on having a strong diverse set of clinical offerings in line with the demand assessment and the specialty gaps that we have identified in that region.

The Standalone Pharmacy business sustained its momentum with revenues growing by 35% and EBITDA increasing by 58%. Excluding the revenues from the Hetero network – revenue growth was 31%. The EBITDA margins on the existing chain improved from 3.1% to 3.9% on a like for like basis. It is pleasing to note that the Combined Stand Alone pharmacy margins are still higher at 3.6% after integrating the Hetero network into our fold.

I would like to share with all of you another interesting development that the pharmacy team has been working on for some time. Currently, we have an online presence for wellness products and supplements and have equipped ourselves and are operationally prepared for medicines and OTC drugs. We will scale up this offering once the appropriate Government regulations and guidelines are in place. We are confident that the combination of our wide network of brick and mortar stores with an online presence will go a long way towards reinforcing our dominance in pharmacy.

In addition to the growth in the Standalone operations, growth in key subsidiary hospitals like Ahmedabad, Bangalore, Kolkata which have performed well have contributed to the improved performance of the consolidated financials. Hospitals in Ahmedabad, Bangalore, & Kolkata reported y-on-y revenue growth of 12%, 14% & 7% respectively. Apollo Munich our joint venture company clocked 31% growth in Gross written premium at Rs. 181 crore in Q1 FY16.

Total Income for Clinics & Specialty hospitals housed under AHLL grew by 14% to Rs. 20.3 Crores in Q1 FY16 compared to Rs. 17.7 Crores in Q1FY15. We have been nurturing the clinics business and driving scale in Cradles and Day Surgery & Short stay centers to build them as strong growth engines for the future. During the quarter, the Nova Specialty Hospitals acquisition was completed with the centers being rebranded as Apollo Spectra Hospitals. Of the 11 centers that we acquired 2 have been remodeled as Cradles – one each in Delhi & Hyderabad while the other 9 centers have been relaunched as Day & short stay multi-specialty hospitals.

Given the expansion plans that AHLL has, the Board has approved the AHLL management team to raise money independently including from private equity to fund their next phase of growth. AHLL now has 2 distinct segments:

1) Primary care which includes Clinics, Diagnostics and Sugar clinics and

2) Secondary Care Specialty Hospitals which includes Cradle & Apollo Spectra Hospitals.

The secondary care segment has been separated out as an SBU into a Downstream Company below AHLL with AHLL holding 49%, AHEL Promoters 15% and the balance 36% being held by another financial investor, who will allow AHLL to reach an impactful scale which will continue to add value to the company.

During the quarter, the Government completed a year in office and I would like to highlight a couple of initiatives specific to healthcare which have been of immense benefit. The introduction of the medical visa has gone a long way in eliminating a significant hurdle in the growth of the medical tourism industry.

The tourism ministry plans to further support the potential by establishing a medical tourism board to boost the medical tourism industry. Given the sizeable opportunity available in this space, AHEL has demonstrated a 25% increase in foreign patients. Additionally, the ministry of communication and information technology is embarking on an ambitious project to connect 60,000 villages of the country through tele medicine under the aegis of the 'Digital India' mission and we are happy to state that Apollo has been chosen as a partner for the same. As all of you would be aware, we have always championed the use of technology to enhance access to healthcare as well as improve outcomes and wholeheartedly support this initiative. Now over to Krishnan, our CFO, for further details of our financial performance.

Mr. A. Krishnan: Thank you Ms. Suneeta. Good afternoon everyone. We are pleased to report standalone revenue growth of 20% on a year on year basis in the first quarter. While Healthcare Services grew by 12% Standalone Pharmacies displayed a strong growth of 35%. Standalone EBITDA grew around 15.8% from Rs. 156 crore in Q1FY15 to Rs. 181 crore in Q1FY16. The EBITDA margin was 14.3% as compared to 14.8% a reduction of 52 basis points compared to the same period last year. This is primarily due to the increasing share of revenues from the Standalone Pharmacy business and EBITDA losses from new hospitals. Finance costs increased 42% from Rs 18.9 crore to Rs 26.9 crore on a yoy basis due to newer facilities having got commissioned in Q4FY15, while other income declined from Rs 6.5 crore to Rs 4.2 crore in Q1FY16. The Effective Tax rate 19.9% in Q1FY16 as compared to 20.4% in Q1FY15 is due to the applicability of 150% depreciation u/s 35AD of Income Tax on new Projects. PAT grew by 9.8% to Rs 90.8 crore as compared to Rs 82.7 crore in Q1 last year.

If you go slide 8, Existing Hospitals revenues grew by 7% aided by 4% increase in volumes. This is on back of rebalancing that we have undertaken in the Chennai cluster by shifting some of the corporate cases as well as a couple of specialties to our new hospitals. We have also reduced subsidized businesses at the Hyderabad cluster. Initiatives to augment the case mix and strengthen medical teams have yielded dividends. EBITDA margins in the existing health care services expanded by 144 bps from 23.1% in Q1FY15 to 24.5% in Q1FY16.

New hospitals have reported revenue growth of over 90% on a y on y basis. Vanagaram & Jayanagar reported 37% growth in revenues. The total EBITDA loss from the new hospitals has been Rs 4.1 Crore in Q1FY16. However the New Hospitals EBITDAR grew by 41.5% on a y-on-y basis. While hospitals at Vanagaram and Jayanagar have reported a positive EBITDA of Rs 3.5 crores, this was offset by the combined EBITDA loss of Rs 7.6 crores from our hospitals at Trichy, Nashik, Nellore, Karapakkam, Perungudi and W&C SMR. The high initial fixed costs would be absorbed and recovered as the new units mature. Our focus is to get Trichy, Nashik & Karapakkam to breakeven by the end of this fiscal with strengthened medical teams & a better local market connect including GP referrals.

I would now like to draw your attention to Slide 9 where the capital employed in Healthcare services now is Rs 3,655 crore. The new hospitals added in Fy13, Fy14 & Fy15, Vanagaram, Jayanagar, Trichy, Nashik, W&C Karapakkam, Nellore, Perungudi, W&C – SMR with a total capital deployment of Rs. 832 crore are yet to begin contributing to ROCE. As a result, the annualized Total healthcare services ROCE has decreased from 14.8% in Q1FY15 to 13.3% in the Q1FY16. However the ROCE from our existing hospitals was at 19.3% in Q1FY16 as compared to 18.5% in Q1FY15.

Slide11 and Slide 12 provide details of our consolidated financial performance. Consolidated revenues grew 18.1% to Rs. 1,420 crore in Q1FY16. In Healthcare services, revenues from existing facilities including hospitals in Ahmedabad, Kolkata and Bengaluru grew 6.3% on a y-o-y basis to Rs 793 crore. Apollo Munich and Apollo Health and Lifestyle reported a revenue growth of 12% and 14.5%, respectively. Consolidated EBITDA grew 14.1% to Rs. 197 crore with an EBITDA margin of 13.9%. AHLL reported an EBITDA loss of Rs 8 crore whereas Apollo Munich reported an EBITDA loss of Rs 1 million. However, the existing Healthcare

Services reported an EBITDA of Rs 191 crores as compared to Rs 167 crores in Q1FY15.The existing Hospital EBITDA margins were at 24% as compared to 22.5% in the same period last year.

Moving to Slide 14, which covers the operational performance by clusters, you will notice that there has been a growth in both inpatient and outpatient volumes on an overall basis. The overall occupancy was at 65% on an expanded bed base of 6,334 beds. ARPOB grew by 12% to Rs 27,939.

In Chennai, inpatient volumes grew by 10.7% while OP volumes have increased by 11.9%. This has come about through healthy volumes at our new facilities and encouraging numbers at existing facilities. The occupancy was at 63% on an expanded bed base of 1,490 beds. ARPOB grew by 12.9% to Rs 39,340. At Hyderabad, the rationalization of subsidy scheme cases and focus on high value cases as well as international patients has resulted in decreased IP & OP volumes. However this has resulted in Revenue growth of 6.3% and ARPOB growth of 17%.

The hospitals which form part of the “Others” cluster and account for 1,818 beds witnessed double digit volume growth in both Inpatients and outpatients volumes. The occupancy of 62% was on an expanded bed base. This cluster now includes 4 new hospitals added in FY13 and later, while Jayanagar has done well the hospitals in Trichy, Nashik & Nellore are still in the initial stage of operations. Revenues here grew by 13.6% with ARPOB growing 7.3% to Rs. 16,412.

The Joint Venture & Subsidiary hospitals in Ahmedabad, Bangalore & Kolkata have performed well with good revenue & volumes. Outpatient revenues grew 11% on the back of increase in OP volumes by 5.5%. IP revenues increased by 8% signifying a richer case mix with reduction in IP volumes, this reduction is mainly due to the rationalization of low paying & subsidised cases in Kolkata and Ahmedabad. Total revenues increased 8.2% and ARPOB grew by 14% to Rs 29,733.

Slide 16 contains details about the performance of the Standalone Pharmacies segment. EBITDA margins increased from 3.1% to 3.6% excluding Hetero which is at 3.9%. Growth momentum remains strong as revenues grew by 35% on a year on year basis to Rs. 520 crore in Q1FY16.

Excluding Hetero, y-on-y growth was 31%. The combined business posted a robust growth in EBITDA of 57.7% and a 53 bps in in margins. Excluding Hetero the EBITDA margins was at 3.9%. We have seen healthy gains in EBITDA margins across all batches of stores. The private labels share of the turnover was at 6.2% in Q1FY16 compared to 5.8% in Q1 last year.

The batch wise margin indicators were favorable with FY08, FY09 as well as the FY10 batch reporting improved EBITDA margins 6.5%, 4.5% and 5.3% respectively. FY08 batch are now closer to 6.5% which translates to an ROCE of almost 22%. In Q1FY16 56 stores were added and there were 11 store closures for a net addition was 45 stores. The Hetero network of 304 stores has now been integrated taking the total number of stores in our network to 2,171.

Slide 18 includes details of our expansion plans – Of the 875 beds that we plan to add this year 780 will be at 3 new hospitals in Navi Mumbai, Malleswaram in North Bangalore and Vizag. Given the 1,300 beds we have added in the last 24 months and the 875 beds planned this year, we will have commissioned nearly 2,200 beds in 3 years. In FY17 & FY18, we will focus on consolidating new hospitals and fast tracking them towards maturity.

Coming to Health Insurance, Apollo Munich Health Insurance reported an increase of 31% in Gross Written Premium at Rs. 181 crore in Q1FY16. The incurred claims ratio stood at 64% in Q1FY16. During the quarter, Apollo Munich launched a unique and first-of-its-kind plan to cover a contagious disease with the launch of the Dengue Coverage plan.

The business remains EBITDA neutral as the improved operating profile is being offset by investments for growth and expansion of the network. At the PAT level, we reported a loss of Rs 2.7 crore compared to a loss of Rs 1.4 crore registered during the same period last year. The Asset under management in this business stood at Rs 723 crore as on June 30, 2015.

That's it from me. We will now take your questions.

Moderator: Ladies and gentlemen, we will now begin the question and answer session. We have the first question from the line of Ruchi Vora from CLSA. Please go ahead.

Ruchi Vora: My question one is relating to your new hospitals. Just wanted some update on Trichy, Nashik, Women & Child – OMR, Nellore and some of the other hospitals which started in FY14 and FY15 in terms of what is the current occupancy, what is the status of doctors and how are the hospitals scaling up and also if you could touch upon what is going to be the new hospital costs in FY16?

A Krishnan: If you look at this quarter, as we stated, some of the hospitals like Vanagaram and Jayanagar, these were two hospitals that we had opened in FY13 and FY14. They have done significantly well, and the occupancies are now over 50% at both of these facilities. If you look at some of the other hospitals, Trichy, Nasik and Nellore, all the three new hospitals that we have, we now have the medical teams in place in all these three hospitals. The teams are now looking at seeing how they can increase the GP referrals and the local community connect etcetera, to be able to get to the 40% to 50% occupancy over the next three, four quarters. So these are three hospitals that we are now currently focused on seeing how we can increase the growth. The two other new hospitals in Chennai, are the ones now in the suburbs which is OMR, even here we already have all the specialties in place and currently we are looking at seeing how we can increase the volumes, Today, the rate of occupancy here is close to 30%, in both OMR as well as the new one which is the Women and Child one, because these were added in Q4 FY15. But if you look at Chennai division, the Chennai cluster as a whole now has witnessed a good inpatient volume increase of around 11% Q1 over the same quarter last year, which includes the OMR as well as the Women and Child and Vanagaram. So Chennai as a cluster is doing well.

Ruchi Vora: Yes and my related question on what should be the expected new hospital cost for FY16 if you could touch upon that, given the fact that we are going to add the highest number of beds in this year?

A. Krishnan: So that is a bit if you look at it today New Bombay would probably come more around the Q3, Q4 and Malleswaram is one which would come more around the Q3 of this Fiscal. So we think we should be able to continue with the current run rate EBITDA losses for what we have reported in Q1 for the rest of this year.

Ruchi Vora: That is very helpful. And my last question is on the AHLL business. Just wanted some colour from the management in terms of what is going to be the strategy for this part of the business going forward and also could you elaborate on the further investment?

Suneeta Reddy: Going forward, clearly we believe that this segment is all about retail health. It includes preventive healthcare through the clinics and it also includes short stay surgery, for which there is a growing demand. The third part of it is Cradle, which is a birthing initiative. So these are the three consumer segments that we are looking at, and we believe that the potential is definitely there. AHLL is a vehicle that we used, to actually capture this potential. The first three, four years of any company I think is challenging, and we have had to face those challenges, but having said that I think there is now a good management team in place and more importantly, we have got a good strategy in place.

With regard to the capital that they will require, I think that clearly they will require another Rs.200 crores over the next five years, and this is based on the fact that they have identified locations for the setting up of new Cradles and also short stay centers. The clinics as you know are less Capex intensive because they are on rental premises. Based on this, I think the trajectory going forward in the next three to four years, we will start to see better performance in terms of EBITDA, but I do hope to see a revenue ramp up happening in the next 18 months from this subsidiary.

Ruchi Vora: And ma'am, in terms of the strategy for AHLL, how does this fit in the overall scheme for Apollo, how does this benefit as in, is there a synergy with our specialty business? Does it help us to generate more footfalls etcetera?

Suneeta Reddy: Certainly, I think that is one of the reasons why we started this, because if you look at internationally how healthcare is delivered, people tend to not want to go into tertiary care hospitals, they prefer to go into a clinic with a minor ailment. So the clinics look after the primary care aspect, and then there is a strong referral system established into the hospital.

With regard to Cradles, it is now an accepted fact that birthing is not an element of sickness, rather it is for joy, so I think that the response to cradles will be very good and India having you know, the world's largest youngest population, I think we can really capture that space, and grow it in which I think the team is very focused on.

The third required special skill sets, short stay surgery is something that when we acquired Nova, the old team could not succeed, but I think with the Apollo expertise, and the fact that they have a high dependency on a tertiary care hospital, there is a lot of trust that the hospital plays in the Nova specialty and they come to it because it is an Apollo specialty plus it takes out, it actually clears up some space for our operating theatres which minor surgeries would have blocked a lot of operating time and taken it away from quaternary care. So that is the rationale behind supporting the expansion of AHLL.

Moderator: Thank you. We have the next question from the line of Balaji Prasad from Barclays. Please go ahead.

Balaji Prasad: So while I don't have many questions on the pharmacy segment, I am still not clear about the hospital segment performance this quarter. Can you help me understand the contribution of Nova hospitals in this quarter's revenue number?

A Krishnan: So Nova as Ms. Suneeta said is a subsidiary of AHLL and it is actually a 49% holding, so the revenues and EBITDA does not get consolidated into the numbers that we have provided as Apollo Health and Lifestyle.

Balaji Prasad: But how much so what has been the state of this since the acquisition seven, eight months ago?

A. Krishnan: This is just the first quarter, so we have just in the process of integrating those into the SBU that we have created. It will take a couple of quarters before we get some hint on numbers etcetera.

Suneeta Reddy: We have just finished the acquisition, we have also re-configurated 2 Nova centres into cradles and we have to change some aspects of design, make sure that doctors who are there, the clinical teams who are in there, clinical protocols were in place, so all that is now just done. I think it is more of a take off stage at this time. So in the next two quarters, we should be able to give you a better picture of what the revenues are looking like.

Balaji Prasad: And so Suneeta so it is right now still getting rebranded and it is not functioning, is that what I should infer?

Suneeta Reddy: No, I mean some of them are functioning, but I would not say that they are not functioning at optimum capacity. I think from here on, from this quarter onwards, as Nova specialty with our doctors and with our clinical protocols it will start functioning.

Balaji Prasad: On the subject of acquisitions, can you also speak a bit more about the hospital in the North Eastern side that you have taken. How old is this hospital, how many beds are operational, current revenues?

A. Krishnan: This in the heart of Guwahati and this is the hospital which has been functioning for many years now. Their top line is approximately around, they have revenues of around Rs. 80 crores to Rs. 100 crores, and they are a profitable hospital. The more important thing is there is the land behind that for us to be able to grow it, and we think over the next three four years we have plans to take it from the current 200 beds to over 300 beds. It is an interesting play for us and we think we should be completing the transaction any time in Q2.

Balaji Prasad: What you said, the operating margin was?

A. Krishnan: Operating margin is approximately around 10%.

Balaji Prasad: And so if I understand your M&A strategy or your expansion strategy, it seems to be going from South, South East, and Kolkata and from North East, you are as a conscious decision completely avoiding the NCR region, is that fair?

Suneeta Reddy: Our acquisition strategy is based on our ROCE strategy. So wherever we get the yields we will make an acquisition. Guwahati, we have a strong brand presence there is a strong demand, so we would rather get into places where there is demand, rather than those where the competition is high and creation is also high.

Balaji Prasad: Lastly on operating margins, the last two quarters have been some of the weakest in the last few years, but that is understandable, considering the number of beds that you have added. Should this be the run rate that we should be working towards for FY16, is that right?

Suneeta Reddy: That is right.

Balaji Prasad: So you will be working at an EBIT margin of around 11%, EBITDA of around 14% to 14.2%?

Suneeta Reddy: No, I think with healthcare services, we will work towards 25% and pharmacy we will continue to grow. I mean we have seen 3.9% in the old pharmacies, but our ambition is to get it to 6% and since Pharmacy contributes 41% as total revenues, you probably seen the impact of that.

S. K. Venkataraman: You would have probably noticed that our standalone pharmacy has gone up from 36% to 41%.

Balaji Prasad: Of course.

S. K. Venkataraman: Optically it looks as if compressed, but in reality actually all our existing units are doing pretty well.

Balaji Prasad: And so we should expect these pharmacies to improve at least for another two to three years before it reaches maturity?

Suneeta Reddy: Certainly, yes.

S. K. Venkataraman: Yes, at the same time our new facilities will also start ramping up. So one could probably guess that the ratios would stabilize sometime around that.

Moderator: Thank you. The next question is from the line of Manoj Garg from DSP Merrill Lynch. Please go ahead.

Manoj Garg: Just like to understand particularly on the existing healthcare services business where we have seen steady improvement in the margins over the past few quarters. What could be the optimum level of margin which we can achieve on the healthcare services side of the business?

A. Krishnan: So I think what we are seeing now is around 23% to 24% is what we have said even earlier what we are looking at. This includes the hospitals in Hyderabad, Mysore etc. which are doing well now. So clearly as Hyderabad occupancy goes up from the current 60% levels to around 65% to 70% over the next few quarters which we have plans to take it to, then you will see the EBITDA margins can go up by another 100, 150 bps. But it is now going to be dependent on some of the other hospitals outside of Chennai to be able to increase the EBITDA margins from the current levels of 24%.

Manoj Garg: And while you have given the guidelines for this year kind of EBITDA margins which is in the range of from 14% to 14.5%, with most of the CAPEX done for by this year end, can we start expecting the margin improvements from the next year onwards, or you feel that probably it will be more of a function in FY18 than FY17?

Suneeta Reddy: The existing hospitals will contribute to improved margins, so I think with so much new facilities kicking in it would be quite challenging to see a margin improvement.

Manoj Garg: Even in the next year also?

Suneeta Reddy: I think the next year is when all the new facilities are actually going to be commissioned, so around 885 beds if I am not wrong.

A. Krishnan: That is right, including New Bombay and Bangalore also.

Manoj Garg: And the last question from my side, like when we look at in terms of the cluster wise performance, in the other cluster while we have seen the in patient volume growth of around 16% there was an inpatient revenue growth was around 12%. So was there any price corrections or like pardon me for ignorance, if you can explain on this?

A. Krishnan: Some of these are new hospitals and some of the new hospitals within the case mix of the patients that we have taken are still not high-end ones. As the hospital keep maturing you will see that we will start getting the high-end cases as well.

S. K. Venkataraman: It is only the statistical impact of weighted average.

Moderator: Thank you. The next question is from the line of Neha Manpuria from JP Morgan. Please go ahead.

Neha Manpuria: First a couple of them on AHLL. Have I understood correctly that Cradles, Short stay Surgical Center and Day Care surgery centers are all under the SBU or is it only the acquired Nova business which is under the SBU?

Suneeta Reddy: Yes, all that you mentioned.

Neha Manpuria: So, has this process been completed or should we see this over the next few quarters?

Suneeta Reddy: The process is completed and the launch will be seen over the next few quarters.

Neha Manpuria: What was the need for the structure ma'am, while I understand that you require capital to grow this business? But is it just that to get that financial investor in because if this is such a big growth driver would not AHLL like to have a larger share in this business?

Suneeta Reddy: I think AHLL will always have the option to have a larger share in this business. So that we structured transaction, and if we look at the shareholders, the shareholders are people who understand healthcare to they will create value in the initial years of ramp up which is challenging. And post that, I think AHLL always has a right to actually consolidate, and keep as much as the equity as they would like and can handle.

Neha Manpuria: Second question, just to put things in perspective, so the quarter-on-quarter decline that we saw in the AHLL revenue and losses is because of some of these hospitals moving out from AHLL to the subsidiary, I mean to this associate sorry?

Suneeta Reddy: Yes.

Neha Manpuria: Ma'am, in your opening remarks you mentioned that Trichy and Nasik have not been in line with our expectation in terms of ramp up and we are hiring a new consultant team. Do you think this sort of highlights one of the concerns about doctor availability in these non-metro cities or smaller cities? How confident are we performance improving in these hospitals?

Suneeta Reddy: No, I think we are very confident. Sometimes you go through this learning curve, and this for us is a learning curve. But we do have a good CEO and we do have good consultants in place. For Apollo especially challenging because the quality of consultants we look for is exceptionally high. So sometimes we do not find them in the local markets and we have to relocate consultants from other markets, and which is why what happened was the slow ramp up.

Neha Manpuria: So should we expect these hospitals then to breakeven let us say in the next year if not in the next few quarters, at least in 12 months' time, would that be a fair expectation?

Suneeta Reddy: Yes, I think that we proved that with many of the Reach hospitals as we were able to do it. These are the only two that was outliers and I think that now that they are on track, we should expect to see that.

Neha Manpuria: And my last question is on Pharmacies. The margin improvement there has been good despite the Hetero drag in the quarter, while I understand private label like you mentioned in your press releases one of the factors, is there anything else that is driving such a strong improvement in margin excluding Hetero on a quarter-on-quarter basis?

Obul Reddy: It is basically revenue growth and improving the generic and the PL ratio. And keeping the cost under control.

Neha Manpuria: And Hetero would be profitable breakeven this year or should we expect that in the next year?

Obul Reddy: We expect by end of this year, because as we reported earlier, that as the advantage of lower backend costs which are where we have a strong integrated infrastructure. So even at that low revenues it is about 2.6% negative EBITDA. We expect by year-end to close on a positive note.

Moderator: Thank you. Next question is from the line of Girish Bakhru from HSBC. Please go ahead.

Girish Bakhru: Just one, first one on Hyderabad. I mean, I understand the rationalization that we are doing by focusing on high margin, but 7% decline is not that too sharp and where do you see this settling down?

Suneeta Reddy: No, I think if you were to look at the analyzed volume of this whole hospital last year, would have been close to 15% to 16% CGHS patients. So they have actually got back some of the volumes which they have lost when they discontinued with the CGHS patients. So, I believe we should look at it from that side. The other way to look at it is that now they are aggressively focused on new patient who can pay what is worth which is a higher realization, which is going to come from the insurance market and more of the retail private space. And then there are foreign patients, which I think will create a huge uptick in this field.

Girish Bakhru: Right, you had said in that last call as well that 15% to 18% of international patients are within the Hyderabad cluster?

A. Krishnan: That is correct.

Girish Bakhru: What would be the percentage for Chennai and others?

Suneeta Reddy: Chennai is at 12%.

Girish Bakhru: Okay. So, I mean other question was related to this that, the kind of ARPOB growth which is there in the Hyderabad cluster which is very healthy, why cannot that be say translated to I mean we are seeing better than Chennai, but is there a potential in other clusters like in Bangalore or other hospitals to increase ARPOB?

Suneeta Reddy: Yes, I think, if we look at Bangalore, we have lots of new facilities or new beds opened out. So as a percentage our first thing was to drive occupancy and if you look at our occupancy in Bangalore it is actually at 76%. So now we will really focus on ARPOB and we also have Malleswaram opening out in the next few months, but we would definitely focus on our ARPOB but primary focus is always occupancy when we start up the new hospital.

Girish Bakhru: Right, but overall, if you have to see in terms of the mix, I am just trying to get with all the rationalization activities what is the target, how much of business say in the subsidized business will the hospital services have on the consolidated level?

A. Krishnan: If you look at subsidized businesses it would be probably less than 10%.

Girish Bakhru: This is come down from what percentage say which used to be like say two, three years ago.

A. Krishnan: Yes, maybe around 13% to 14%.

Girish Bakhru: So from 14% to 10% you are saying basically, right?

A. Krishnan: Yes.

Girish Bakhru: The next question was on the Cradles. The Cradle does not offer any fertility services, right?

Suneeta Reddy: They are starting to, yes.

Girish Bakhru: So there they will be like having equipment and setup in place to do IVF and stuff like that?

Suneeta Reddy: Yes.

Girish Bakhru: So would not that increase the cost in setting up Cradles?

Suneeta Reddy: I think they have factored in that cost into the Rs. 22 crores for Cradles.

Girish Bakhru: Can you give color on what is the market there; because it seem like that is a very interesting market for even private investors to get in. What is the sense of overall market and how much fast it is growing?

Suneeta Reddy: We will send you details of that offline then I think you can. We will get connected with management team in terms of wanting to understand the market size of that.

Moderator: Thank you. We have next question from the line of Saion Mukherjee from Nomura. Please go ahead.

Saion Mukherjee: Just one question on this AHLL you mentioned I think the new SBU, Cradle, Primary Clinic and Day Care such as including Nova, what about dental clinic and sugar clinics?

A. Krishnan: Sugar is part of this as well. Dental is currently separately held by AHEL and it will also be transferred into AHLL over a period of time.

Saion Mukherjee: And I think in your remarks, you mentioned about the shareholding, so can you just take us through what it is, I just missed that?

A. Krishnan: 49% is held by AHLL, 15% is held by the promoters and 36% is held by investors.

Saion Mukherjee: So how much is the total fund infusion that would happen as part of this?

A. Krishnan: So that is currently being done, there is a separate private equity consideration which is happening at the AHLL level, you will have to wait for that, the team is working around that. And it will take couple of quarters before we get the understanding on how much we are going to be investing based on their requirements of how much they are still putting together the plan and on how many hospitals they need to open up the Cradles and everything else.

Saion Mukherjee: One of the understanding I had except for Day Care Surges like all of the other setup is fairly low on CAPEX right, so I am just wondering if Rs. 200 crores over 5-year period, is not it that AHLL could have or Apollo could have managed on its own?

A. Krishnan: So it is more because, this is the strategy. The retail health and the primary care and secondary care is what we wanted to have as a separate business segment and the Board of Apollo suggested that they should have their own charter and they should kind of figure out how they should raise their own money and not really depend only on AHEL for the same and which is the reason that they are now going forward with that.

Saion Mukherjee: So I mean, going forward you think like 49% stake is something which is the minimum, right I mean you do not expect it to fall below that?

Suneeta Reddy: No.

A. Krishnan: And as Ms. Suneeta said, we also will have an opportunity and an option to kind of increase it over a period of time.

Moderator: Thank you. We have next question from the line of Praveen Sahay from B&K Securities. Please go ahead.

Praveen Sahay: My question is related to the ARPOB, the overall ARPOB if I had to look at that is improved by somewhere around 12%.So can you give the breakup like how much is from the tariff or from the operational efficiencies?

A. Krishnan: So approximately around 7% of this is from volume. The ARPOB of 12% increase is 7% is because of volume. Only in ARPOB you are saying is it?

Praveen Sahay: Yes, right.

A. Krishnan: Okay the ARPOB is almost around 4% is because of tariff and the balance is because of case-mix and operational efficiencies and also because of the ALOS drop. You would have seen that the ALOS is also dropped from 4.41% to 4.17% because of the efficiency.

Praveen Sahay: The next question regarding expansion plan for our hospital. If I see this compared with the last year quarter the fourth quarter of '15 so this quarter the expansion over one location in Patna for 240 beds is not seen now. So what is the plan over there?

Suneeta Reddy: In Patna, we actually bid for the land and we were very much engaged in studying Patna. But unfortunately after studying the peer mix, competitive dynamics, etc. our bid was lower someone paid much higher premium and got that piece of land. But we will be on the lookout for sites in Patna, but we definitely cannot buy something at market price because we believe that it is a market where you have to, it is not a high margin market at this time.

Praveen Sahay: And also the MLCP CAPEX of Rs. 83 million that happened already or?

A. Krishnan: Yes, that is already done and the MLCP is now operational.

Praveen Sahay: And related to the Proton Therapy now we had pushed from 17% to 19%, so what's the development over there?

A. Krishnan: We had delays in getting the AERC approval, we only received the AERC approval last quarter. Having received the AERC approval now we have gone ahead and already started developing the site, because the site also needed an AERC approval before we started construction. We could not have started the construction before that approval. So we have now got their approval for the whole site and design and everything. So the construction will take at least another 18 months and after the construction of that, the installation typically takes another one year. So this is of the Proton, after it comes here the installation of the Proton and testing and everything else itself takes a year which is why it has gone into FY19.

Praveen Sahay: And what would be the capacity for this?

A. Krishnan: So this will have 150 to 200 beds over and above the Proton.

Praveen Sahay: And just a last one on the hospital side for the Ahmedabad, Kolkata and Bangalore hospitals. Can you give some numbers on the EBITDA front for these hospitals, because these hospitals are growing very rapidly lately?

A. Krishnan: Can you take that offline; we would not have that number readily available with us.

Praveen Sahay: Okay.

Moderator: Thank you. Next question is from the line of Shyamal Lahon from Asia Growth Capital. Please go ahead.

Shyamal Lahon: We have seen that the share of revenue has changed this quarter versus quarter one year before in terms of share of pharmacy retail versus healthcare. So, these businesses having different ROC profiles, what should be our expectation maybe in the mid-term let us say two years down the line what is going to be the revenue share from each and what are the ROCE profiles of each of these components which will contribute to the whole entity?

Suneeta Reddy: That pharmacies are growing at 30% and I think that 30% growth is somehow part of the quarter something to expect. The healthcare services are growing at 14% to 15%. With the addition of new beds we hope to take that to close to 20%.

S. K. Venkataraman: Inherently the standalone pharmacy as Krishnan mentioned earlier could go as high as 25%. And inherently the healthcare business if all things go well as for ideal test conditions could be 20% to 25%. So that is the potential of the business.

Suneeta Reddy: And the ROCE for hospitals could definitely reach… I think Venkat answered that question.

Moderator: The next question is from the line of Abhishek Sharma from IIFL. Please go ahead.

Abhishek Sharma: I basically had some broader industry question. So the first one is around three of your FY16 openings which is around Vizag, Indore, and Navi Mumbai. How do you see these micro markets in terms of market dynamics pricing as well as competitive intensity?

S. K. Venkataraman: I think this is beyond the scope of this call and we will be happy to actually take this question offline so that we can take you through the intricacies.

Abhishek Sharma: The other one is, in one of the earlier questions you said that you bid for land in Patna and somebody else came in and outbid you. Are you seeing more of that given the fact that there has been a lot of investment in the healthcare services market; are you seeing more of that in other territories as well?

Suneeta Reddy: Yes I mean, I think if someone wants a foothold in a certain city and they have relationships within that city, yes they will bid. But we will I think Apollo's strategy is only to bid when we know at prices which we know we make a decent ROC. So, we will continue to look for land, we will continue to look for facilities that maybe you know we can make an organic acquisition. But yes, there is a lot more cash in the healthcare sector right now. But I think for us it is important how we use that cash and what returns we get on that cash. That is what drives us.

Abhishek Sharma: So you still see a lot of lucrative opportunities outside your core market of South India to basically replicate the model?

Suneeta Reddy: Certainly.

Moderator: Thank you. Next question is from the line of Prashant Nair from Citigroup. Please go ahead.

Prashant Nair: Just one question on the expansion plans, now that some of the Fiscal 18 projects have been pushed out to Fiscal 19 how do we see CAPEX on these rolling out would it still be similar to what was expected earlier or would it change now?

A. Krishnan: So, we have provided that Prashant in the slide, which is saying that we now have approximately if you look at our CAPEX we have Rs.1,470 crores now of which Rs. 640 crores has already been made. So the balance Rs.750 crores is what will be required now and most of that will comes out of our proposed rights issue. So you will see that we will be using that to pay down our debt initially and then it should show in lower interest costs, etc., and then going back and picking up more debt as we require it.

Prashant Nair: And this balance CAPEX that is required for these projects, would it be evenly spread across the three years or would it be?

A. Krishnan: There would be some it will be a bit higher than this year and then the next two years would be lower. So we will give you the split of that separately, we do not have it on hand.

Moderator: Thank you. Next question is from the line of Ruchi Vora from CLSA. Please go ahead.

Ruchi Vora: I just wanted a quick clarification on Slide #14, which highlights the operational performance of hospitals. I am seeing ARPOB growth is in mid-teens I mean double-digits largely for each cluster, and I see the volume growth also at 8% to 10%, but the revenue growth is still lower. So what is that we are missing? Just to give you an example Chennai in-patient and out-patient volume growth is 11% and 12% and we are seeing an overall ARPOB increase of 13%, so should not your revenue growth be higher it is just 16%?

A. Krishnan: ALOS also come down, right. If you look at the average length of say the number of days that people are saying has come down. So that gets reflected in ARPOB. So you will have to look at in-patient volume into realization equal to revenues and ARPOB is also dependent on the ALOS. So this is why it will not reflect directly in your revenue.

Ruchi Vora: Understood. Maybe I can take this offline.

A. Krishnan: Yes.

Moderator: Thank you. Ladies and gentlemen, that was the last question. I would like to now handover the floor back to the management for their closing comments. Over to you, sir.

Suneeta Reddy: Ladies and gentlemen, thank you for joining us on this call. As we go forward I think the management and the entire teams at Apollo are prepared to really look forward to consolidating the performance and to improving EBITDA in the existing in the hospitals the new hospitals that we have created. With regard to Apollo Health & Lifestyle Ltd. (AHLL) we look forward to a very successful launch in that space. Thank you for joining our call today.

Moderator: Thank you very much, ma'am. Ladies and gentlemen, on behalf of Apollo Hospitals that concludes this conference call. Thank you for joining us and you may now disconnect your lines.