26 May 2024

India | Equity Research | Q4FY24 results review

Fortis Healthcare

Pharma

Hospital margins ascending

Fortis Healthcare's (Fortis) hospital division margin of 22.4% in Q4FY24 was the best under the new management. It has recently divested two underperforming hospitals in Chennai to curtail cost. Focus on adding brownfield beds (2,200 beds in next 4 years) is likely to improve scale without denting profitability. Occupancy in FY24 rose 200bps YoY to 67% and is likely to touch 70% on the existing beds in Q1FY25E. Rebranding of diagnostics arm to Agilus has taken a toll on diagnostic revenue growth and margins. The branding cost of INR 310mn may reoccur in FY25E, a 5-7% price increase in B2C business (53% of sales) in Feb'24 can help it safeguard profitability. We resume coverage on the company with **ADD** rating and target price of INR 500, valuing hospitals/diagnostics at 21x/23x FY26E EV/EBITDA.

Q4FY24 traction driven by hospital division

Revenue rose 8.7% YoY (+6.3% QoQ) to INR 17.9bn driven by rise in elective surgeries and a 10% improvement in ARPOB. Gross margin rose 10bps YoY (30bps QoQ) to 76.8%. EBITDA margin rose 480bps YoY (440bps QoQ) to 21.3% driven by better margins in hospitals. Adjusted PAT rose 44.6% YoY (36.7% QoQ) to INR 1.8bn.

Rise in ARPOB, better case mix scale up hospital margins in Q4

Hospital revenue grew 7.2% QoQ (+10.3% YoY) at INR 14.9bn driven by better traction in Mohali, BG Road and Shalimar Baug hospitals. Occupancy stood to 67% vs 64%/67% QoQ/ YoY. ARPOB rose 3.8% QoQ to INR 63,442. ALOS stood at 4.41 days vs 4.32/3.83 QoQ/YoY. Revenue from international patients' grew 9.9% YoY (9.8% QoQ) to INR 1.24bn. Hospital EBITDA margin stood at 22.4%, up 430bps QoQ and 600bps YoY due to APROB and case mix improvement. It will add 2,200 beds in existing clusters in 4 years by incurring capex of INR 12-13bn and may also acquire hospitals in existing clusters.

Rebranding cost impacts Agilus' performance

Diagnostics revenue rose 1.5% YoY (+2% QoQ) to INR 3bn. Number of tests was flat YoY (+1.8% QoQ) to 9.95mn. Patient count declined by 3.7% YoY at 4.1mn. Average revenue per test was up 3% YoY at INR 344. Margin contracted 70bps YoY (+480bps QoQ) to 16.2%. Parent entity Fortis may raise capital (equity or debt) to honour put option liability and give an exit to PE investors in Agilus by Oct'24.

Financial Summary

Y/E March (INR mn)	FY23A	FY24A	FY25E	FY26E
Net Revenue	62,976	68,929	78,358	88,962
EBITDA	11,013	12,676	15,223	18,118
EBITDA Margin (%)	17.5	18.4	19.4	20.4
Net Profit	5,315	5,868	7,273	9,332
EPS (INR)	7.0	7.8	9.6	12.4
EPS % Chg YoY	75.3	10.4	23.9	28.3
P/E (x)	59.2	58.2	48.0	37.4
EV/EBITDA (x)	32.2	28.0	22.7	18.5
RoCE (%)	5.8	6.4	7.9	9.1
RoE (%)	7.9	7.9	9.1	10.5

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Market Data

Market Cap (INR)	349bn
Market Cap (USD)	4,197mn
Bloomberg Code	FORH IN
Reuters Code	FOHE.BO
52-week Range (INR)	480 /271
Free Float (%)	69.0
ADTV-3M (mn) (USD)	7.5

Price Performance (%)	3m	6m	12m
Absolute	5.3	26.1	60.6
Relative to Sensex	2.2	11.7	38.6

Valuation and risks

Hospital division margin in Q4FY24 was marginally (100bps) driven by seasonality while bulk of the improvement was aided by divestment of two hospitals in Chennai, price increases, cost optimisation and better case mix. The company plans to add significant bed capacity in each of the existing hospitals. In FY25, it will operationalise 300 beds of which 50 beds will be in Faridabad, 50 in Shalimar Bagh, 100 beds in new Manesar facility, 100 beds in Kolkata and a few OT beds in Bengaluru. Beyond FY25, it will focus on brownfield expansion, aiming to add another 1,500 beds by FY28. These new beds are unlikely to create a sizeable dent in margins. Management expects hospital margin to be between 20-21% in FY25 and ~25% in the next 2-3 years. Efforts to boost growth in diagnostic division are underway with the company taking a price hike on B2C portfolio, coupled with a revival in industry volumes, we remain hopeful of a better show in FY25E.

We expect EBITDA to register a CAGR of 19.6% over FY24-26E driven by revenue CAGR of 13.6%. EBITDA margin is likely to rise to 19-20% over the next couple of years backed by improvement in ARPOB, surge in occupancy, divestment of loss-making hospitals and healthy growth in Agilus diagnostics.

The stock currently trades at EV/EBITDA of 22.7x FY25E and 18.5x FY26E. We remain optimistic on the outlook considering strong growth in hospitals with increasing occupancy (targeting 70% levels) and ARPOB, imminent recovery of non-covid volumes, and cost-control initiatives employed by the current management. We resume coverage on Fortis with **ADD** rating and target price of INR 500/share based on FY26E SoTP-based valuation, valuing the hospital/diagnostic business at 21x/23x FY26E EV/EBITDA.

Exhibit 1: Sum of the parts (SoTP) valuation

	FY26E EBITDA	(x)	Values (Rs mn)
Hospitals	15,720	21	3,32480
Agilus (56.9% stake)	2,398	23	31,380
EV			**3,63,860**
Less: Net debt			(13,944)
Implied Mkt Cap			**3,77,804**
Value per share			**500**

Source: Company data, I-Sec research

Q4FY24 concall highlights

Hospitals

- Top 6 specialties (62% of hospital revenue) viz. oncology, gastroenterology, neurosciences, renal sciences, orthopaedics and cardiac sciences grew 13.8% YoY in Q4FY24 and 13% in FY24.
- ARPOB increased 10.3% YoY in Q4FY24 to INR 23.2mn. Growth was led by improvement in surgical revenue and case mix.
- Occupancy in Q4FY24 stood at 67%, flat QoQ vs 64% in Q3FY24.
- Revenue from international patients grew 12.2% YoY to INR 4.8bn in FY24.
- In FY24, it added 246 beds across key facilities such as in Anandpur (Kolkata), Mohali (Punjab), BG Road (Bengaluru) and Mulund (Mumbai). It also commissioned a new 70-bed facility in Ludhiana (Punjab).
- In FY24, the company exited Chennai market by divesting its underperforming facilities at Arcot Road and Malar.

- Volumes in key procedures such as transplants grew 11%, and 50% and 8% YoY for robotic surgeries and radiation therapy.
- In FY24, revenues from key facilities such as Mohali, Noida, Shalimar Bagh, Anandpur and Amritsar grew 19%, 16%, 16%, 15% and 21%, respectively.
- It will operationalise 100 beds (450 bed capacity) at the acquired Manesar facility in Q2FY25.
- Next hearing for the pending litigation with Daiichi is scheduled on Jun 15, '24 in the Delhi High court.
- Divestment of two hospitals in Chennai aided 26bps benefit in margin in FY24, further 100bps came from manpower and procurement cost optimisation and the rest from better case and payor mix.

Diagnostics

- Management expects diagnostic industry to grow 8-9% for the next couple of years.
- In B2C business, it took 5-7% price increase in Feb'24.
- Adjusting for the one-off pertaining to rebranding expenses (INR 310mn) and the provisioning related to certain government business (INR 270mn), operating EBITDA margin improved 100bps to 15.9% in Q4FY24 and 180bps in FY24 at 19.5%.
- Agilus added 200+ customer touchpoints to its network in Q4FY24.
- B2C:B2B revenue mix stood at 53:47 in Q4FY24.
- In Q4FY24, Agilus conducted ~9.6mn tests vs 9.8mn last year. The decline in the tests was primarily because of lower covid volumes.
- Covid accounted for 0.3% revenue in FY24 as against 4.45% last year.
- Non-covid revenue grew 5% YoY in Q4FY24 and 6% in FY24.
- Revenue from preventive care test grew 14% and genomics grew 27% in FY24.

Q4 financials

- Net debt at the end of FY24 stood at INR 2.64bn, net debt to EBITDA stood at 0.17x.
- Due to seasonality, Q4 hospital business was higher by 100bps, balance improvement in hospital margin was aided by better case and payor mix.

Guidance

- Management expects an upward revision in CGHS (4% of hospital revenue) rate in the near term.
- Revenue contribution from government schemes had increased to 20% (of which 4% is CGHS), in FY24 and will be optimised in FY25.
- ARPOB in FY25 is likely to improve by 5-6%, aided by 3% from price increase and 2-3% from case and payor mix.
- Hospital business revenue will grow between 13-16% in FY25.
- Mulund and BG Road have seen good pick up in occupancy in Q1.
- Currently, blended occupancy stands at 70%.
- It plans to add ~2,200 beds by FY28 and will incur capex of INR 12-13bn.

- In FY25, it will operationalise 300 beds of which 50 beds will be in Faridabad, 50 in Shalimar Bagh, 100 beds in new Manesar facility, 100 beds in Kolkata and a few OT beds in Bengaluru.
- Hospital margin is likely to increase 200bps to 20-21% in FY25. Guidance factors negative margin for new Manesar facility. In next 2-3 years, management aspires to achieve ~25% margin.
- Management may pursue inorganic opportunities in existing five clusters of hospital business.
- Management is working with private equity for revival of Agilus IPO and other options pertaining to put option liability (to be exercised by Oct'24). The company may have to honour the liability and will fund it by raising equity or debt in the parent entity. Further clarity to emerge by Aug'24.
- Agilus will continue to incur branding expense of INR 310mn in FY25.

Exhibit 2: Quarterly review

Particulars (INR mn)	Q4FY24	Q4FY23	YoY % Chg	Q3FY24	QoQ % Chg	FY24	FY23	YoY % Chg
Net Sales	**17,859**	**16,427**	**8.7**	**16,797**	**6.3**	**68,929**	**62,976**	**9.5**
Gross profit	13,722	12,603	8.9	12,859	6.7	**52,742**	**48,429**	8.9
Gross margins (%)	**76.8**	**76.7**	**10bps**	**76.6**	**30bps**	**76.5**	**76.9**	**-40bps**
EBITDA	3,810	2,709	40.7	2,840	34.2	12,676	11,013	15.1
EBITDA margins (%)	**21.3**	**16.5**	**480bps**	**16.9**	**440bps**	**18.4**	**17.5**	**90bps**
Other income	141	155	(8.9)	113	24.5	478	836	(42.8)
PBIDT	**3,952**	**2,864**	**38.0**	**2,953**	**33.8**	**13,154**	**11,849**	**11.0**
Depreciation	922	818	12.8	869	6.1	3,425	3,157	8.5
Interest	347	317	9.4	330	5.2	1,310	1,291	1.4
Extra ordinary income/ (exp.)	31	105		77		160	736	
PBT	**2,714**	**1,834**	**48.0**	**1,832**	**48.2**	**8,580**	**8,137**	**5.4**
Tax	682	451	51.3	489	39.5	2,128	1,807	17.7
Minority Interest	244	58	324.5	(4)	(5,647.7)	463	443	4.7
Reported PAT	**1,787**	**1,326**	**34.8**	**1,347**	**32.7**	**5,989**	**5,887**	**1.7**
Adjusted PAT	**1,764**	**1,220**	**44.6**	**1,290**	**36.7**	**5,868**	**5,315**	**10.4**

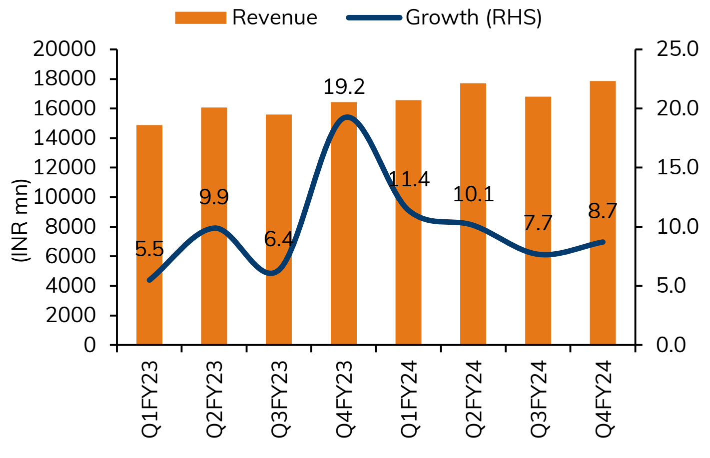
Source: Company data, I-Sec research

Exhibit 3: Business mix

	Q4FY24	Q4FY23	YoY % Chg	Q3FY24	QoQ % Chg	FY24	FY23	YoY % Chg
Hospitals	14,898	13,510	10.3	13,894	7.2	56,859	51,076	11.3
EBITDA margins(%)	22.4	16.4	600bps	18.1	430bps	18.6	17.1	150bps
Agilus	2,961	2,917	1.5	2,903	2.0	12,070	11,899	1.4
EBITDA margins(%)	16.2	17.0	-70bps	11.4	480bps	17.4	21.1	-370bps
Total	**17,859**	**16,427**	**8.7**	**16,797**	**6.3**	**68,929**	**62,976**	**9.5**

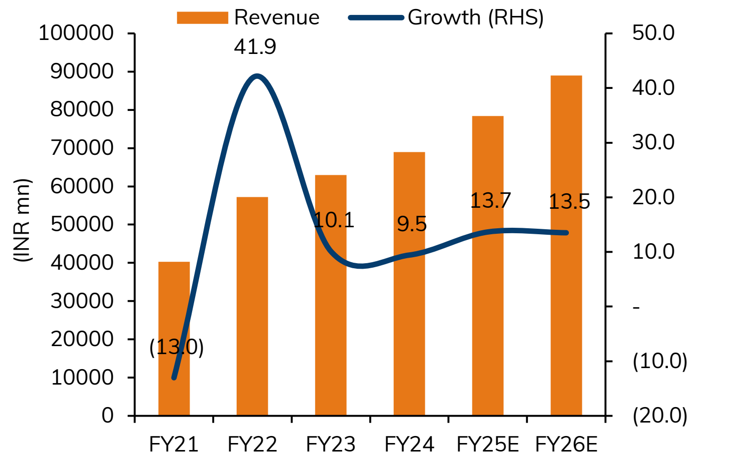
Source: Company data, I-Sec research

Exhibit 4: Traction across key hospitals is driving growth



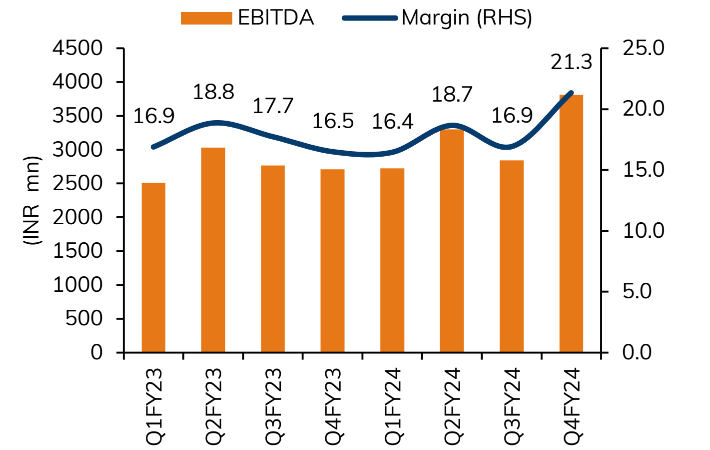
Source: I-Sec research, Company data

Exhibit 5: Hospital revenue to deliver healthy growth with improved occupancies and capacity



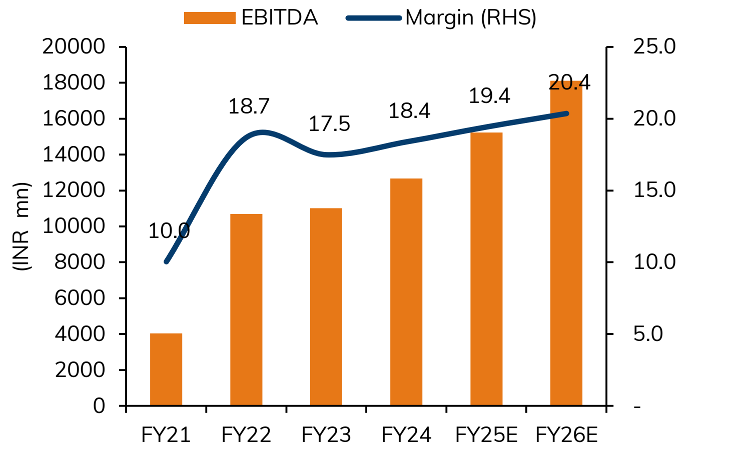
Source: I-Sec research, Company data

Exhibit 6: Hospital business is driving overall improvement in margins



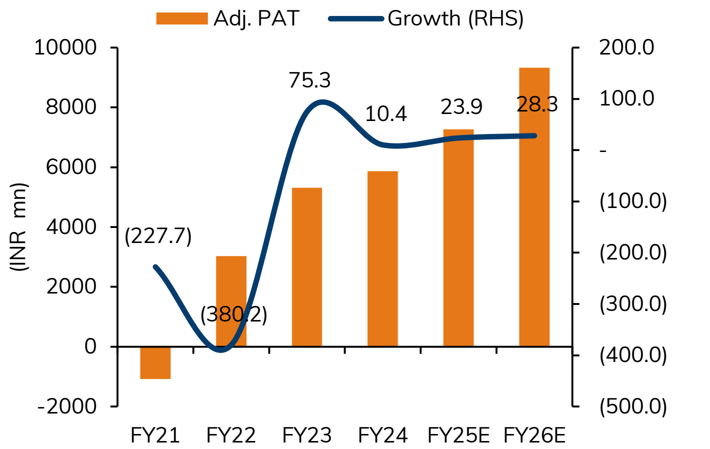
Source: I-Sec research, Company data

Exhibit 7: Expect 198bps improvement in margins over FY24-26E



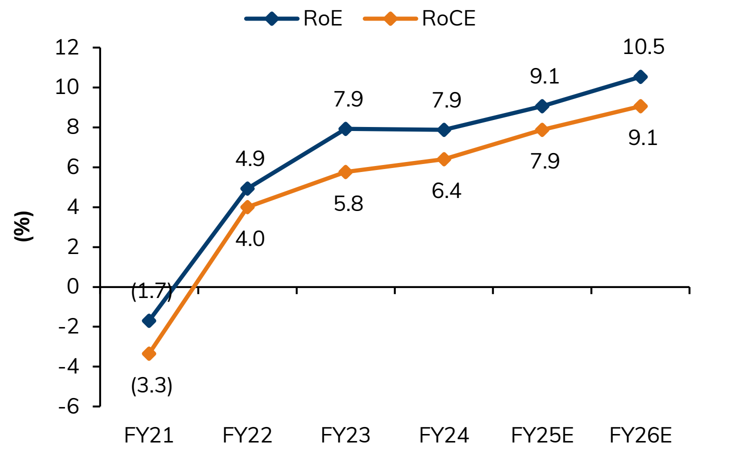
Source: I-Sec research, Company data

Exhibit 8: Sustained improvement in profitability



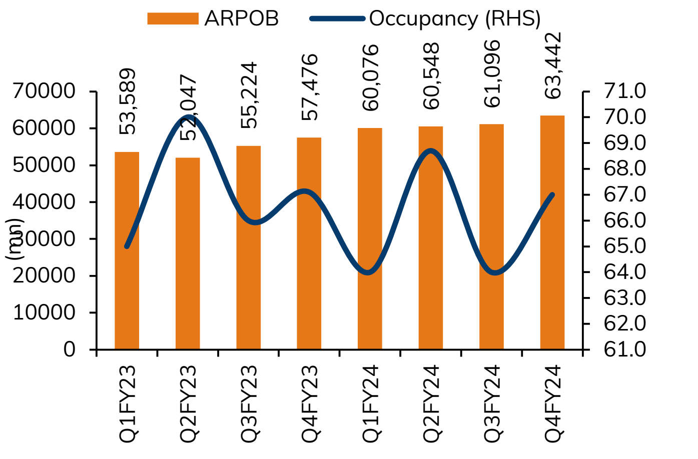
Source: I-Sec research, Company data

Exhibit 9: Return ratios may improve from current of 6-8% levels



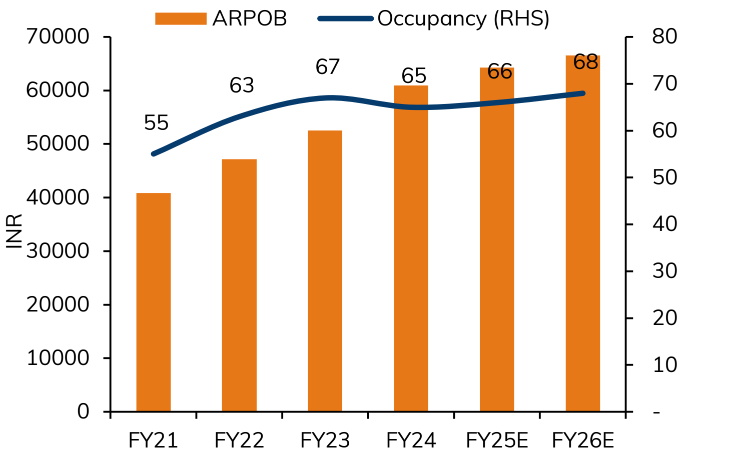
Source: I-Sec research, Company data

Exhibit 10: ARPOB rose ~10% YoY



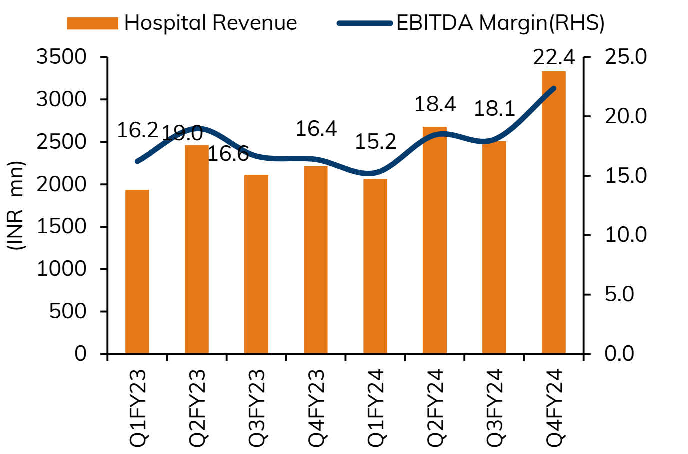
Source: I-Sec research, Company data

Exhibit 11: ARPOB to increase ~5-6% every year



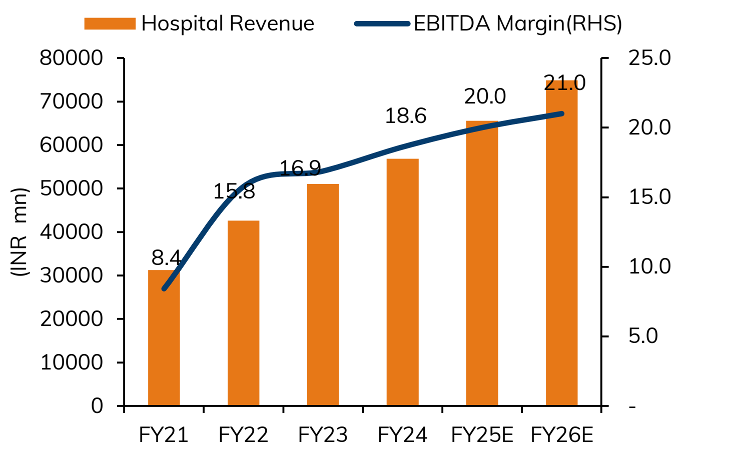
Source: I-Sec research, Company data

Exhibit 12: Better ARPOB and case mix are driving growth and margins



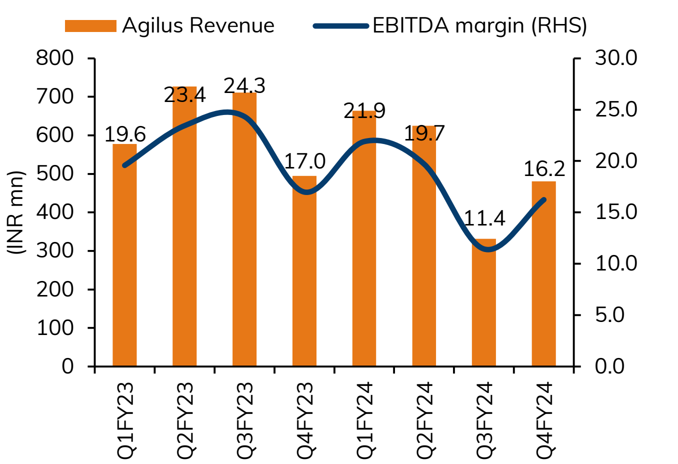
Source: I-Sec research, Company data

Exhibit 13: Hospital business is at an inflection



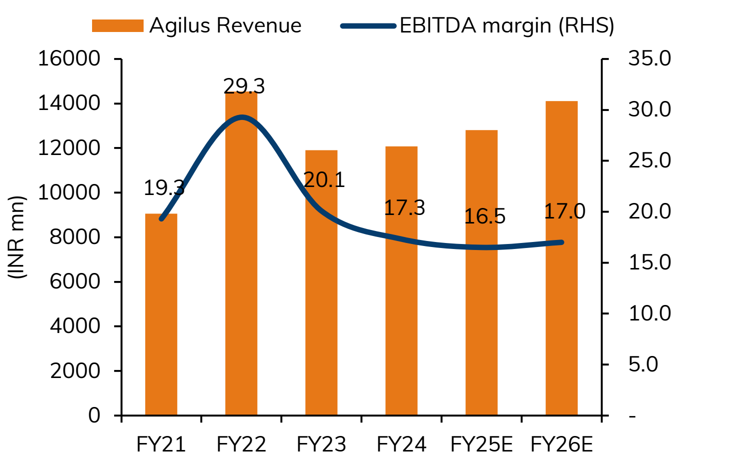
Source: I-Sec research, Company data

Exhibit 14: Rebranding cost has dented margins



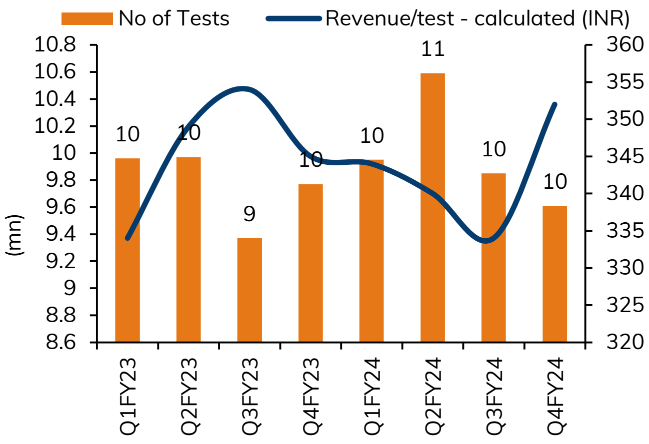
Source: I-Sec research, Company data

Exhibit 15: Price hikes to revive diagnostic margins



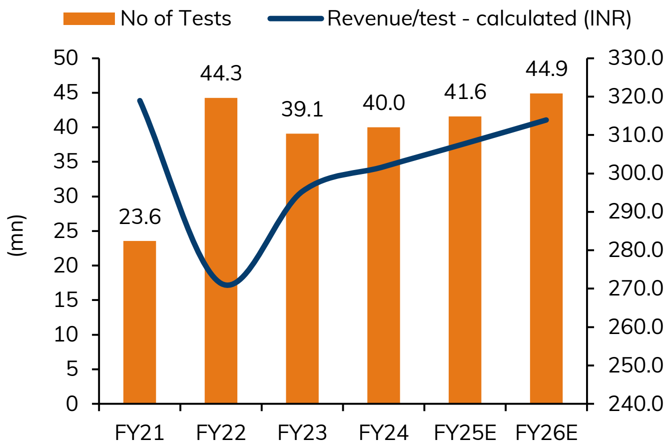
Source: I-Sec research, Company data

Exhibit 16: Number of tests was flat YoY



Source: I-Sec research, Company data

Exhibit 17: Efforts to improve test volumes underway



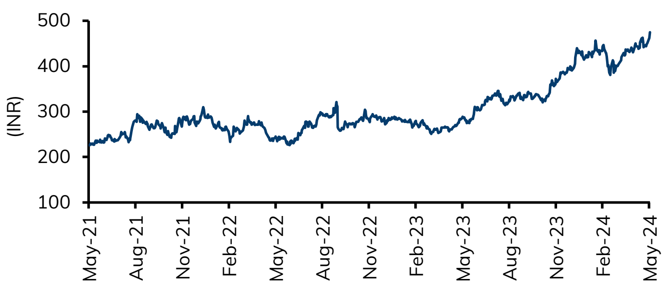
Source: I-Sec research, Company data

Exhibit 18: Shareholding pattern

%	Sep'23	Dec'23	Mar'24
Promoters	31.2	31.2	31.2
Institutional investors	52.9	53.1	54.4
MFs and others	22.5	25.0	26.5
FIs/Banks	1.2	1.2	1.2
Insurance	2.8	3.1	3.3
FIIs	26.4	23.8	23.4
Others	15.9	15.7	14.4

Source: Bloomberg

Exhibit 19: Price chart



Source: Bloomberg

Financial Summary

Exhibit 20: Profit & Loss

(INR mn, year ending March)

	FY23A	FY24A	FY25E	FY26E
Net Sales	**62,976**	**68,929**	**78,358**	**88,962**
Operating Expenses	51,963	56,253	63,135	70,844
EBITDA	**11,013**	**12,676**	**15,223**	**18,118**
EBITDA Margin (%)	17.5	18.4	19.4	20.4
Depreciation & Amortization	3,157	3,425	3,998	4,198
EBIT	7,856	9,251	11,226	13,920
Interest expenditure	1,291	1,310	1,454	1,454
Other Non-operating Income	736	160	-	-
Recurring PBT	**8,137**	**8,580**	**10,288**	**13,025**
Profit / (Loss) from Associates	-	-	-	-
Less: Taxes	1,807	2,128	2,551	3,230
PAT	6,330	6,452	7,737	9,795
Less: Minority Interest	(443)	(463)	(463)	(463)
Extraordinaries (Net)	-	-	-	-
Net Income (Reported)	**5,887**	**5,989**	**7,273**	**9,332**
Net Income (Adjusted)	**5,315**	**5,868**	**7,273**	**9,332**

Source Company data, I-Sec research

Exhibit 21: Balance sheet

(INR mn, year ending March)

	FY23A	FY24A	FY25E	FY26E
Total Current Assets	14,064	14,206	24,676	36,104
of which cash & cash eqv.	3,627	5,984	15,330	25,494
Total Current Liabilities & Provisions	12,550	30,010	31,208	32,644
Net Current Assets	**1,513**	**(15,804)**	**(6,532)**	**3,461**
Investments	2,103	2,297	759	759
Net Fixed Assets	37,918	40,968	40,970	40,773
ROU Assets	10,577	11,708	11,708	11,708
Capital Work-in-Progress	2,278	5,420	5,420	5,420
Total Intangible Assets	45,768	46,061	46,061	46,061
Other assets	8,175	9,039	9,039	9,039
Deferred Tax Assets	3,443	3,174	3,174	3,174
Total Assets	**1,11,786**	**1,02,878**	**1,10,615**	**1,20,410**
Liabilities				
Borrowings	**7,032**	**8,583**	**8,583**	**8,583**
Deferred Tax Liability	**4,107**	**4,293**	**4,293**	**4,293**
provisions	1,302	1,466	1,466	1,466
other Liabilities	16,115	8	8	8
Equity Share Capital	7,550	7,550	7,550	7,550
Reserves & Surplus	64,873	69,079	76,353	85,685
Total Net Worth	**72,423**	**76,629**	**83,902**	**93,234**
Minority Interest	8,581	8,932	9,396	9,859
Total Liabilities	**1,11,786**	**1,02,878**	**1,10,615**	**1,20,410**

Source Company data, I-Sec research

Exhibit 22: Cashflow statement

(INR mn, year ending March)

	FY23A	FY24A	FY25E	FY26E
Operating Cashflow	**8,222**	**11,001**	**13,262**	**15,618**
Working Capital Changes	(211)	(221)	(155)	(86)
Capital Commitments	3	15	20	19
Free Cashflow	**8,225**	**11,016**	**13,282**	**15,637**
Other investing cashflow	**776**	**(2,227)**	**1,537**	**-**
Cashflow from Investing Activities	6	30	40	38
Issue of Share Capital	-	-	-	-
Interest Cost	-	-	-	-
Inc (Dec) in Borrowings	(3,256)	1,296	-	-
Dividend paid	(1,598)	(860)	-	-
Others	(132)	(1,300)	(1,454)	(1,454)
Cash flow from Financing Activities	(4,985)	(865)	(1,454)	(1,454)
Chg. in Cash & Bank balance	**3,243**	**10,166**	**11,849**	**14,202**
Closing cash & balance	7,370	13,794	17,833	29,532

Source Company data, I-Sec research

Exhibit 23: Key ratios

(Year ending March)

	FY23A	FY24A	FY25E	FY26E
Per Share Data (INR)				
Reported EPS	7.8	7.9	9.6	12.4
Adjusted EPS (Diluted)	7.0	7.8	9.6	12.4
Cash EPS	11.2	12.3	14.9	17.9
Dividend per share (DPS)	2.1	1.1	-	-
Book Value per share (BV)	95.9	101.5	111.1	123.5
Dividend Payout (%)	27.1	14.4	-	-
Growth (%)				
Net Sales	10.1	9.5	13.7	13.5
EBITDA	3.0	15.1	20.1	19.0
EPS (INR)	75.3	10.4	23.9	28.3
Valuation Ratios (x)				
P/E	59.2	58.2	48.0	37.4
P/CEPS	41.2	37.5	30.9	25.8
P/BV	4.8	4.6	4.2	3.7
EV / EBITDA	32.2	28.0	22.7	18.5
P / Sales	5.5	5.1	4.5	3.9
Dividend Yield (%)	0.0	0.0	-	-
Operating Ratios				
Gross Profit Margins (%)	76.9	76.5	76.9	77.1
EBITDA Margins (%)	17.5	18.4	19.4	20.4
Effective Tax Rate (%)	22.2	24.8	24.8	24.8
Net Profit Margins (%)	8.4	8.5	9.3	10.5
NWC / Total Assets (%)	-	-	-	-
Net Debt / Equity (x)	0.0	0.0	(0.1)	(0.2)
Net Debt / EBITDA (x)	0.1	0.0	(0.5)	(1.0)
Profitability Ratios				
RoCE (%)	5.8	6.4	7.9	9.1
RoE (%)	7.9	7.9	9.1	10.5
RoIC (%)	5.7	6.4	8.2	10.4
Fixed Asset Turnover (x)	1.7	1.7	1.9	2.2
Inventory Turnover Days	7	6	6	6
Receivables Days	35	35	35	35
Payables Days	43	40	40	40

Source Company data, I-Sec research

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