

Vijaya Diagnostic Centre Ltd

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IPO Price: Rs522-531

Issue Opens: 01-Sept-21

Issue Closes: 03-Sept-21

Largest integrated diagnostic chain in South India

Vijaya Diagnostic Centre (VDCL) is one of the largest integrated diagnostic chain in South India, having a dominant market share and brand recall in the Telangana and Andhra Pradesh. After starting in 1981, the company has 81 diagnostic centres in 13 cities/towns. It has 7% share in Telangana and Andhra non-hospital diagnostic market. Promoted by S. Surendranath Reddy, promoters own 60% stake while rest is owned by PE firm Kedaara Capital. After OFS, Kedaara would own 10%.

One of the highest B2C contribution amongst organized chains

Vijaya Diagnostics has the highest B2C revenue with 93% of its revenue coming from B2C segment in FY20. The company has ensured that the focus will remain on building a strong B2C presence in and around the geographies it is present in along with new geographies it is looking to grow. VDCL's network includes 1 flagship centre, 20 hub centres and 60 diagnostic centres. The company also has 11 reference laboratories (including a national reference laboratory). The 'hub and spoke' model implemented by the company, collects specimens across multiple locations within a catchment area for shipment to their reference laboratories. Since company also offers radiology services across the network, it has higher realisation and tests per patient compared to DLPL and METROHL.

Focus on growing in existing adjacencies and East India

VDCL has a market share of 7% in the organized out of hospitals diagnostic space in Telangana and AP. The management estimates the size of this market to be ~Rs.51bn and Vijaya is well placed to capture a larger piece of this market. The company is focusing on expanding in Tier 1 and 2 cities/towns which is underpenetrated and will help them cater to nearby villages also. VDCL is also looking to expand its footprint in the East India and has acquired Medinova in 2015 which has a good presence in Kolkata. Management reckons East India is largely underpenetrated and has better scope of growth. Company has guided for Rs650mn-750mn capex which will be funded through internal accruals.

Early teens growth in past 2 years with best in class margin

VDCL has delivered 13% CAGR Revenue growth from FY19 to FY21 and is expecting to grow considerably faster than the industry average of 10-12%. EBITDA Margins of ~40% in FY20 are impressive largely a result of the company catering to the B2C segment which is less impacted by pricing erosion compared to B2B sourcing of samples. A new centre breaks even in the quarter of its inception. Strong return ratios coupled with negative working capital due to higher B2C revenues is another positive we like. Promoter owns land housing some of the diagnostic centres and receives rent from company.

Subscribe to a retail-footfalls driven franchise

At a post-issue market cap of Rs54.1bn, OFS is priced at ~64x FY21 P/E. On a forward basis, a steady growth and margin profile would translate in to valuation which would be at a marginal discount or in line with the 55-60x FY23 multiples commanded by DLPL and METROHL. Vijaya owns a retail footfall-driven business which would take time to scale up in newer geographies but then precludes pricing pressure due to lack of a sizable B2B business. We note that other listed peers like DLPL and METROHL have a significant B2B presence. Also, there appears to be a lot of scope to grow market share in existing markets given the large potential. Recommend Subscribe on a medium term basis though cognizant that near term triggers or surprises on growth after a COVID-fueled Q1 FY22 appear unlikely.

Issue details

Face value (Re)	1
Issue Size*	Rs18.95bn
Offer for sale*	Rs18.95bn
Fresh Issue	NIL
Post-issue M-cap*	Rs54.1bn
Issue type	100% Book building *At upper price band

Share reservation (of net offer)

QIB	Not less than 50%
Non-institutional	Not more than 15%
Retail	Not more than 35%

Issue Manager

BRLM	ICICI Securities, Edelweiss Financial Kotak Mahindra Capital
Registrar	KFin Technologies Pvt. Ltd.
Listing	BSE, NSE

Company management

Dr. S Surendranath Reddy	Executive Chairman
Sunil Chandra Kondapally	Executive Director
S Geeta Reddy	Non-Executive Director
Narasimha Raju K.A.	CFO

Financial Summary – Y/E March (Rs mn)

	FY19	FY20	FY21
Revenue	2,926	3,388	3,767
Gross margin	86.2%	87%	84.8%
EBITDA margin	37%	39.1%	44.1%
PAT	463	625	849
EPS (Rs)	4.5	6.1	8.3
RoE (%)	22.3%	25.9%	26.8%

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MANAGEMENT TEAM

Dr. S. Surendranath Reddy, Executive Chairman

Dr. Reddy has been associated with Vijaya Diagnostics for the last 19 years. He holds a bachelor's degree in medicine from Shri Venkatesvara University and a provisional degree of Doctor of Medicine in Radiology from Osmania College, Hyderabad. Dr. Reddy is also a life member of Indian Radiological and Imaging Association. He has received several awards for his work and leadership qualities in the field of Healthcare.

Mr. Sunil Chandra Kondapally, Executive Director

Mr. Sunil Chandra Kondapally is the son of Mr. S Surendranath and Mrs. S Geeta Reddy. He possesses more than 17 years of the field of pharmaceutical industry and has been associated with the company since its inception. He holds a bachelor's degree in science in electrical engineering from Florida State University and has founded a pharmaceutical company, Trikona Pharmaceuticals Private Ltd. In 2016 and another company QPS Bioserve India Private Ltd. In 2004.

Mrs. S Geeta Reddy, Non-Executive Director

Mr. S Geeta Reddy is the wife of Dr. S Surendranath Reddy. She holds a bachelor's degree in law from Osmania University and is enrolled as an Advocate with Andhra Pradesh High Court in 1986. Apart from Vijaya Diagnostics, she is also on the board of various other companies. She has on an ongoing pending litigation case where she was a Non-Executive Director of Park Health Systems in 2006, relating to a fire accident. The matter is subjudice as of now.

Mr. Narasimha Raju K.A., CFO

Mr. Narasimha Raju K.A. was associated with the company from June 2017 to November 2020 and was a part of the finance, MIS and strategy department. He later re-joined the company on March 15, 2021, and was appointed as the CFO with effect from May 1, 2021. He holds a bachelor's degree of commerce from Osmania University and is a member of the Institute of Chartered Accountants of India. He has previously worked with S.R. Batliboi & Co., NSL Renewable Power Private Limited and PBEL Property Development (India) Private Limited and possesses over 14 years of professional experience

Exhibit 1: Shareholding pattern

Entity	No of shares	Holding (%)
Karakoram Limited	39,316,387	38.56
Dr. S Surendranath Reddy	38,521,195	37.78
Sura Suprita Reddy	9,176,933	9.00
Sunil Chanra Kondapally	9,106,933	8.93
S. Geeta Reddy	4,058,638	3.98
Kedaara Capital AIF 1	1,469,970	1.44
B. Vishnu Priya	27,922	0.03

Source: RHP

PRE-IPO MEET TAKEAWAYS

Initial Remarks:

- ✓ Started in 1981, currently having 81 clinical labs and 11 reference labs across India. Most dominant in South India. VDCL services to more than 10000 customers per day.
- ✓ Highest B2C revenues among listed peers.
- ✓ Backed by Kedaara Capital
- ✓ 1610 pathology tests offered by VDCL.
- ✓ Each Small Format Centers has 12-13 staff.
- ✓ Revenues have increased from 50crs a decade back to 377crs in FY21.

Expansion Strategy:

- ✓ Out-of-hospital diagnostic market in AP and Telangana is 5100crs and Vijaya's market share are 7%. Company is looking at growing in Tier 2 and 3 cities and consolidating market share.
- ✓ The company has visibility in locations (adjacencies to Tier 1 and larger cities) where we they believe market is underpenetrated and they could grow.
- ✓ Vijaya acquired Medinova in 2015, which was not doing well due to mismanagement issues. Started doing well and making a turn for the better.
- ✓ Open to acquisitions and inorganic opportunities. Strong liquidity on books. Will look at companies having more B2C model.
- ✓ The plan is to grow in East through Vijaya Brand. Competitive intensity in Kolkata is very low in comparison to other bigger cities in India and so the company has decided to grow its integrated offerings in Kolkata before going in to other markets.
- ✓ Capex required per center is higher than peers as the company provides more services. Strong brand recall helps it to achieve breakeven within 1 quarter itself. Spoke center costs 90-100 lacs (18 months is the payback period). Hub centers has more facilities and requires larger capex (payback period 3-3.5 years).
- ✓ Cash will be majorly used either for organic or inorganic opportunities.

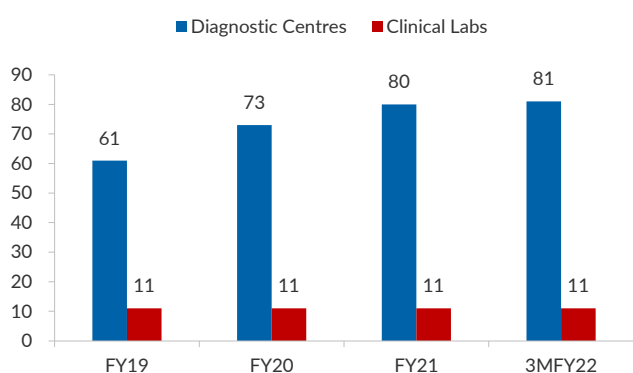
Revenue and Cost Structure:

- ✓ Integrated model along with higher B2C model will keep the per footfall revenues to be higher.
- ✓ Testing of COVID started in Q2 FY21 as state was not permitting private players to conduct COVID tests earlier. FY21 covid contribution was 14% to revenues and Q1 FY22, 15% contribution from covid tests.
- ✓ 8% of shares on fully diluted basis are held by ESOP holders. Absenteeism in Q1 FY21 was the reason for lower employee expenses in FY21.
- ✓ AMC contracts and certain indirect expenses were lower in FY21 leading to lower other expenses in FY21.
- ✓ Cost structure is lower in Tier 2 cities, so despite revenues being lower, the margins are sustainable as the company expands into these cities.
- ✓ Revenue mix: 65% pathology & 35% radiology. This revenue mix has almost remained same over the last 3 years. Focus is on both the segments growing well. Due to various common costs involved giving margin breakup in pathology and radiology is difficult. Gross Margins in radiology: ~90%.
- ✓ Negative working capital is due to the business model which is B2C focused. This should continue going ahead.

Miscellaneous:

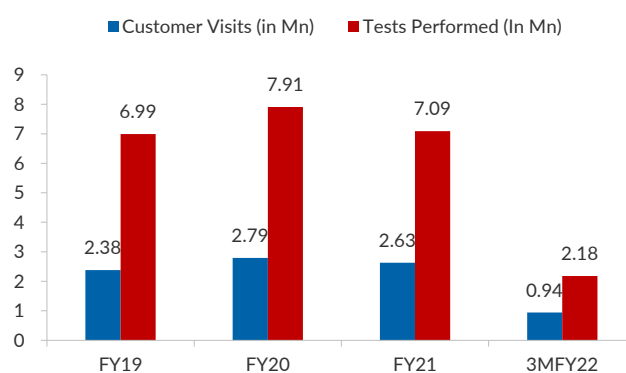
- ✓ 78 centers are leased and 2 are owned by the company.
- ✓ All the centers have radiology integrated in them. Expansion to Tier 2 region supports lots of villages in and around that area.
- ✓ Post IPO also, Kedaara will continue to own 10% in the company. Promoter and promoter group will hold 55% after IPO.
- ✓ No plan to merge Medinova (listed) with Vijaya as of now. Maybe some time in future.

Exhibit 2: Increasing Footprint in its core market



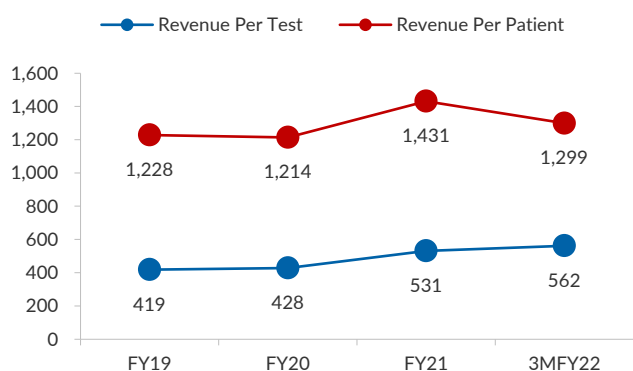
Source: Company, YES Sec

Exhibit 3: Strong Brand Recall Leading to Higher Customer Push



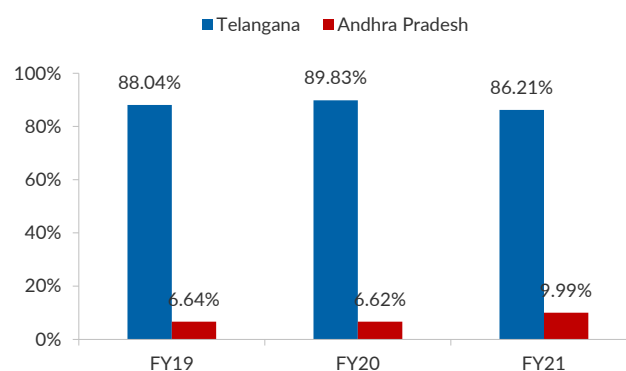
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Exhibit 4: Integrated Model helps to deliver strong user metrics



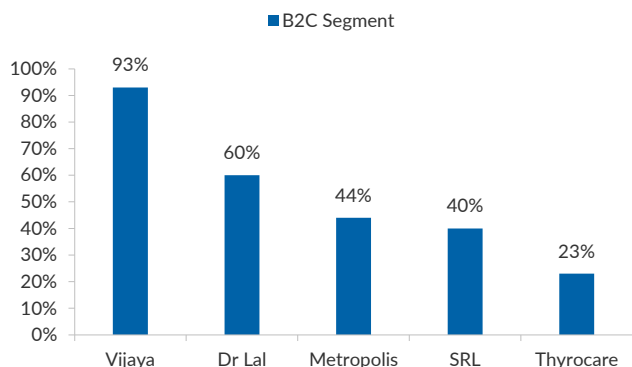
Source: Company, YES Sec

Exhibit 5: Concentration Risk as diversification outside Telangana and AP remains slow



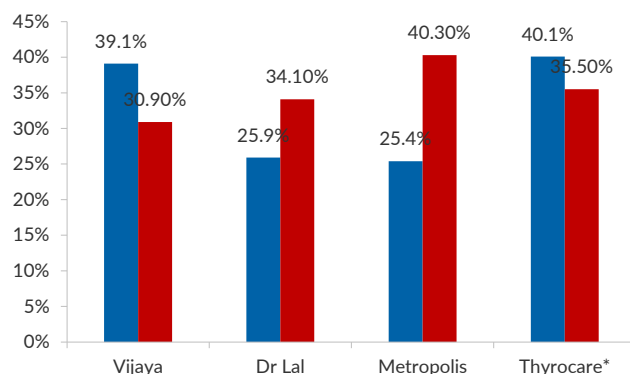
Source: Company, YES Sec

Exhibit 6: Overall contribution of B2C Segment highest amongst peers (FY20)



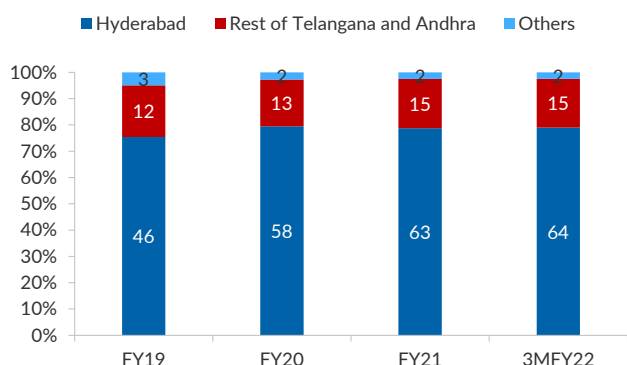
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Exhibit 7: Strong Operating Metrics compared to listed peers (FY20)



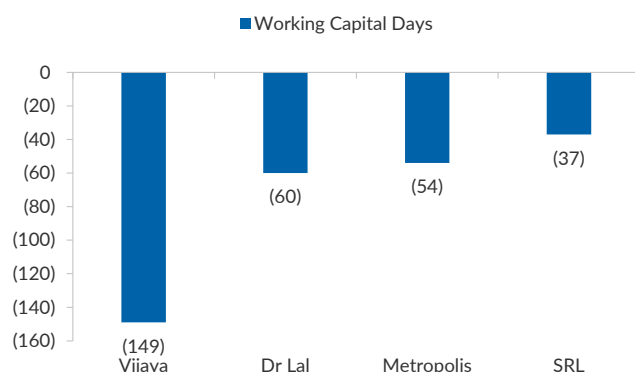
Source: Company, YES Sec

Exhibit 8: Geographical Presence



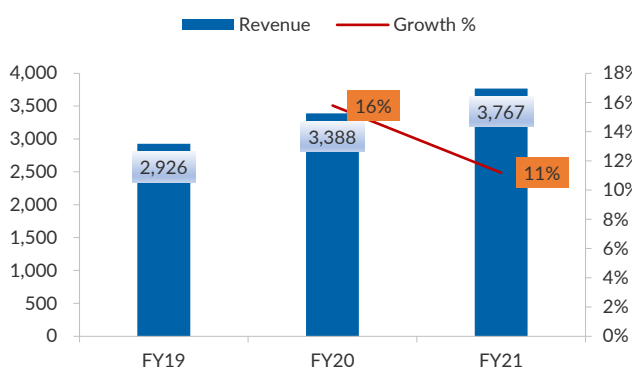
Source: Company, YES Sec

Exhibit 9: Lower Working Capital due to higher B2C



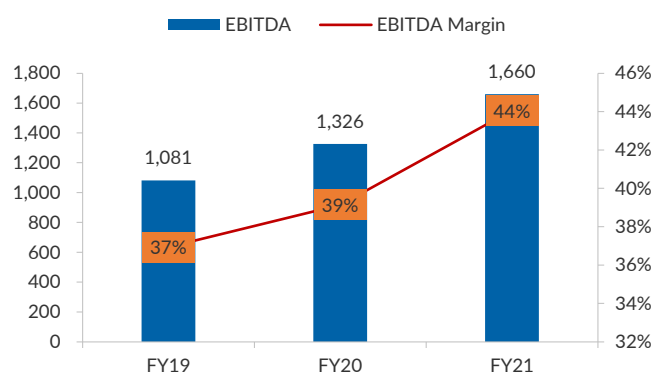
Source: Company, YES Sec

Exhibit 10: Revenue and Revenue growth



Source: Company, YES Sec

Exhibit 11: EBITDA and EBITDA margins



Source: Company, YES Sec

FINANCIALS

Exhibit 12: Balance sheet

Y/E March 31 (Rs mn)	FY19	FY20	FY21
Equity and Liabilities			
Equity share capital	45	45	45
Other equity	2028	2700	3545
Non-controlling interest	(4)	(4)	2
Total equity	2070	2741	3592
Borrowings	315	221	33
Lease liability	1034	1196	1265
Other financial liabilities	19	9	2
Provisions	53	67	77
Other non-current liabilities	1	1	1
Total Non-current liabilities	1423	1495	1377
Borrowings	109	107	12
Lease liability	73	88	101
Trade payables	218	217	221
Other financial liabilities	115	127	61
Other current liabilities	31	20	20
Provisions	11	10	7
Current tax liabilities (Net)	16	14	16
Total current liabilities	571	586	440
Total equity and liabilities	4064	4823	5409
Assets			
Property, plant and equipment	1437	1398	1358
Right-of-use assets	1079	1254	1260
Capital work-in-progress	27	97	94
Goodwill	69	53	53
Other intangible assets	7	10	6
Financial Assets	44	55	123
Deferred tax assets (net)	12	16	61
Other non-current assets	15	76	67
Total Non-current assets	2689	2959	3022
Inventories	22	28	26
Investments	688	547	276
Trade receivables	91	80	64
Cash and cash equivalents	526	1182	1943
Other financial assets	30	5	52
Other current assets	17	22	27
Total current assets	1375	1864	2387
Total assets	4064	4823	5409

Source: Company, YES Sec

Exhibit 13: Income statement

Y/e 31 Mar (Rs m)	FY19	FY20	FY21
Revenue	2926	3388	3767
Operating profit	1081	1326	1660
Depreciation	396	492	505
Interest expense	135	154	152
Profit before tax	653	834	1121
Taxes	190	209	272
Net profit	463	625	849

Source: Company, YES Sec

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