

Fortis Healthcare

BSE SENSEX	S&P CNX
34,047	10,047
Bloomberg	FORH IN
Equity Shares (m)	463.1
M.Cap.(INRb)/(USDb)	65.0 / 1.0
52-Week Range (INR)	231 / 107
1, 6, 12 Rel. Per (%)	15/1/-35
Avg Val, INRm	1120.0
Free float (%)	65.6

Financials & Valuations (INR b)

Y/E Mar	2018E	2019E	2020E
Net Sales	47.0	52.6	60.5
EBITDA	3.5	5.6	8.8
PAT	-0.4	1.3	3.4
EPS (INR)	-0.8	2.8	7.3
Gr. (%)	-107.8	-440.1	164.5
BV/Sh INR	122.3	125.1	132.3
RoE (%)	-0.7	2.2	5.7
RoCE (%)	1.4	3.1	5.5
P/E (x)	N/A	58.3	22.1
P/BV (x)	1.3	1.3	1.2

Estimate change



TP change



Rating change


CMP: INR161 TP: INR185 (+15%)
Buy

2Q in-line, but a miss in 3Q; Entry of third-party key for re-rating

- Fortis Healthcare (FORH) reported 2QFY18/3QFY18 revenue of INR12b (flat YoY)/INR11.2b (-1.1% YoY), with EBITDA margin of 8.9%/4.6%. Hospital business revenue came in at INR9.7b (-0.6% YoY)/INR9b (-0.9% YoY) for 2QFY18/3QFY18, with EBITDA margin of 8.5%/5.5%. SRL reported revenue of INR2.2b (+5.2% YoY)/INR2.1b (+10% YoY), with EBITDA margin of 23.2%/18.4%. 2Q numbers were in line, but 3Q numbers missed our expectations. FORH reported a loss of INR236m/INR191m in 2Q/3QFY18.
- Promoter stake down to <1% due to invocation of pledged shares:** Promoter holding is now down to 0.8% from ~34% in Dec-17 due to invocation of pledged shares. Yes Bank now is the largest shareholder, with more than 17% stake in the company. Post invocation of pledge shares, banks and financial institutions (Yes bank, Axis bank, Indiabulls) have the right to sell their shares to a third party, which can eventually become the promoter of the company.
- Auditors have raised serious issues:** Auditors have raised red flags on related-party loans and inter-corporate deposits (details provided below). Consequently, they were unable to express conclusion regarding the financial statements. Notably, FORH needs to recover loan of ~INR4.7b from promoter entity. Management responded that it is confident about recovering this loan, but we see this as a concern, given the financial health of the promoter entity. SEBI investigation is ongoing related to this issue.
- Entry of third-party key for re-rating:** FORH's stock has remained volatile in the recent past on the back of news flow related to issues with the current promoter and possibility of equity infusion in the company. Given that current promoter holding is marginal, banks/financial institutes may look to find a new investor, which could lead to stock re-rating. We have valued the hospital and diagnostic business based on 20x and 18x 1HFY20E EV/EBITDA, respectively. We cut EBITDA by 26%/9% for FY19/20E as we build in slower margin ramp-up.

Consolidated – Quarterly Earning Model

Y/E March	FY17E				FY18E				FY17	FY18E	FY18E	Var
	1Q	2Q	3Q	4Q	1Q	2Q	3Q	4QE		3QE		%
Net Sales	11,212	11,957	11,334	11,234	11,566	11,972	11,207	12,242	45,737	46,986	13,034	-14
YoY Change (%)	8.4	10.9	8.9	3.2	3.2	0.1	-1.1	9.0	7.8	2.7	15.0	
Total Expenditure	10,585	10,968	10,211	10,444	10,705	10,907	10,691	11,157	42,208	43,460	11,587	
EBITDA	626	990	1,123	790	861	1,065	516	1,085	3,529	3,527	1,447	-64
Margins (%)	5.6	8.3	9.9	7.0	7.4	8.9	4.6	8.9	7.7	7.5	11.1	
Depreciation	476	517	599	630	590	607	590	563	2,222	2,350	780	
Interest	420	461	748	666	644	660	632	464	2,294	2,400	500	
Other Income	330	380	589	361	576	371	426	-1,073	1,660	300	75	
PBT before EO expense	61	393	365	-146	203	169	-280	-1,015	673	-923	242	
Extra-Ord expense	0	-9	-4,194	8	6	468	2	0	16	0	0	
PBT	61	402	4,559	-153	197	-299	-282	-1,015	657	-923	242	
Tax	29	242	190	263	123	170	26	-623	724	-305	80	
Rate (%)	47.3	60.2	4.2	-171.7	62.1	-56.8	-9.2	61.4	110.3	33.0	33.0	
MI & P/L of Asso. Cos.	-130	-154	-165	-41	-151	-233	-117	258	-4,861	-243	-61	
Reported PAT	162	314	4,533	-375	226	-236	-191	-650	4,793	-375	223	-186
Adj PAT	162	310	514	-354	228	497	-189	-650	4,792	-375	223	
YoY Change (%)	-82.6	-62.6	-193.1	-61.0	41.1	60.3	-136.7	83.4	460.3	-107.8	-56.7	
Margins (%)	1.4	2.6	4.5	-3.2	2.0	4.2	-1.7	-5.3	10.5	-0.8	1.7	

E: MOSL Estimates

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Investors are advised to refer through important disclosures made at the last page of the Research Report.

Motilal Oswal research is available on www.motilaloswal.com/Institutional-Equities, Bloomberg, Thomson Reuters, Factset and S&P Capital.

Exhibit 1: Key operating metrics

	3QFY16	4QFY16	1QFY17	2QFY17	3QFY17	4QFY17	1QFY18	2QFY18	3QFY18
Revenue Mix (%)									
Hospitals	81.6	80.7	81.2	81.3	80.9	81.3	81.2	80.7	81.1
Diagnostics	17.3	17.6	17.1	17.8	16.6	18.1	18.3	18.7	18.4
International	1.1	1.7	1.7	0.9	3.6	0.7	0.5	0.6	0.5
Revenue Growth (%)									
	1.6	2.3	8.4	10.9	8.9	3.2	3.2	0.1	(1.1)
Hospitals	7.3	5.6	9.1	11.0	7.9	4.0	3.2	(0.6)	(0.9)
Diagnostics	0.6	3.8	7.3	11.5	4.4	5.7	10.4	5.2	9.6
International	(79.2)	(61.4)	(9.9)	(6.9)	267.5	(59.4)	(70.7)	(33.2)	(86.2)
Cost of sales (%)									
	98.7	102.7	94.4	91.7	90.1	93.0	92.6	91.1	95.4
Raw material	22.4	22.5	22.7	21.9	20.8	21.9	22.5	21.6	22.4
Staff cost	19.2	20.3	20.0	18.7	20.0	20.8	20.5	19.1	20.9
Other expenses	57.0	59.9	51.8	51.1	49.2	50.3	49.6	50.4	52.2
Tax Rate	(17.9)	(13.0)	47.3	60.2	4.2	(171.7)	62.1	(56.8)	(9.2)
Margins (%)									
Gross Margins	77.6	77.5	77.3	78.1	79.2	78.1	77.5	78.4	77.6
EBITDAC Margins	16.9	16.9	16.9	16.9	16.9	16.9	16.9	15.5	12.9
EBITDA Margins	1.3	(2.7)	5.6	8.3	9.9	7.0	7.4	8.9	4.6
EBIT Margins	4.0	4.0	4.0	4.0	4.0	4.0	4.0	3.8	(0.7)

Source: Company, MOSL

Highlights from concall

- FORH expects recovery of loan given to the promoters by end of 1QFY19.
- Company expects RHT acquisition process to close in next 4-6 months. Post completion, it will have a positive impact of INR3b on EBITDA.
- FORH has reduced its debt by ~INR4b in the last few quarters.
- A few new players have entered the diagnostic business over the past few months. Competition has also intensified among the larger diagnostic players in large metros.
- The entire hospital industry was impacted last quarter by negative news, which hurt FORH's performance. Company believes that the business has stabilized now, and expects strong growth in 4QFY18 and FY19.
- Company has taken major initiatives in the digital platform and how to get patients online. Digital revenues have crossed INR1b.
- International business continues to be very big segment. Company is planning to enter into partnership agreements, which will increase the number of international patients. This partnership will also get patients from the untapped market of North America.

Red flags raised by auditors

Auditors of Fortis have raised certain concerns, due to which they are unable to express conclusion regarding the financial statement.

1. A wholly owned subsidiary of the company has given inter corporate deposits (ICDs); there have also been concerns about certain inter-group party transactions. Auditors have also raised red flag regarding implication of a legal notice received by the parent company. FORH is carrying out an independent investigation through an external legal firm for the same.

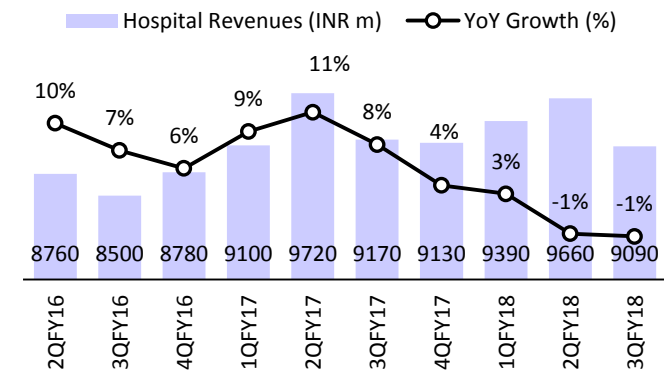
There has also been an issue with regard to secured short-term investments of INR4.7b made by a wholly owned subsidiary of the company, for which the SEBI will be conducting an investigation.

Due to these ongoing investigations, auditors are unable to conclude the effects of the outcome on company's operations, financial results and cash flow.

2. On 1st July 2017, Fortis Hospital Limited (FHsL), a wholly owned subsidiary of the group, had placed ICDs for a period of 90 days with three companies, which were not related to the group. Later on, these companies became part of the group and the transactions were termed as related-party transactions. Management is confident of recovering the outstanding amount.
3. Other current assets as on September 2017 include unsecured advances of INR567m due from certain vendor, where recoveries have been delayed. Management has assessed the recoverability of the same and concluded that the amount is recoverable.

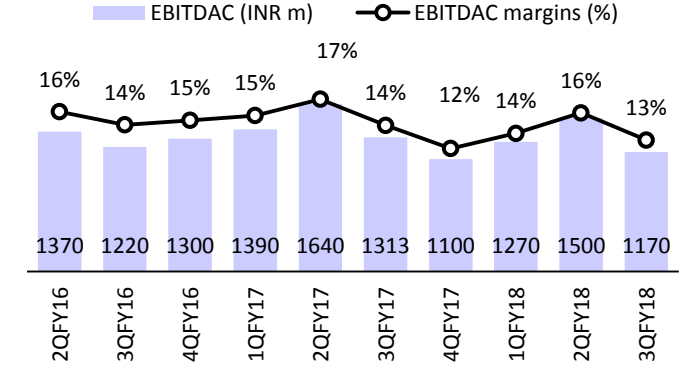
Story in charts- Hospital

Exhibit 2: Hospital revenues declined marginally by 1% YoY



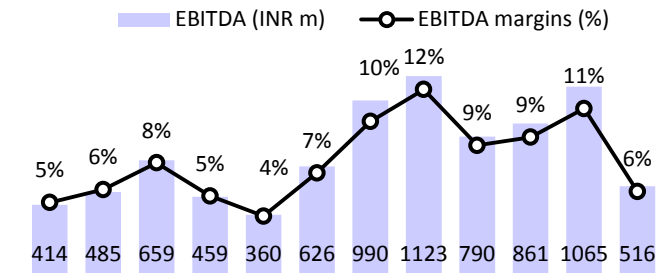
Source: MOSL, Company

Exhibit 3: Hospital EBITDAC margin shrunk 270bp QoQ



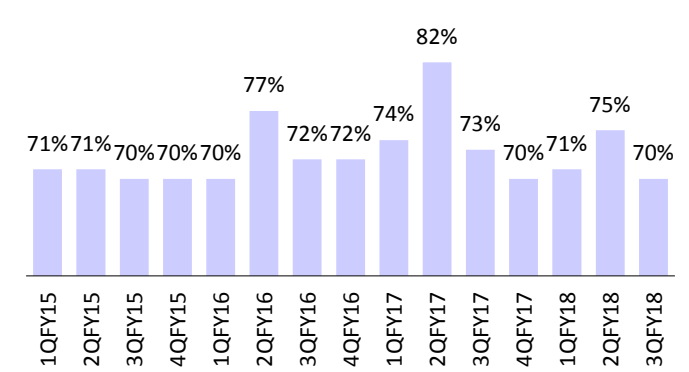
Source: MOSL, Company

Exhibit 4: Hospital EBITDA margins saw a sharp contraction of 700bp YoY



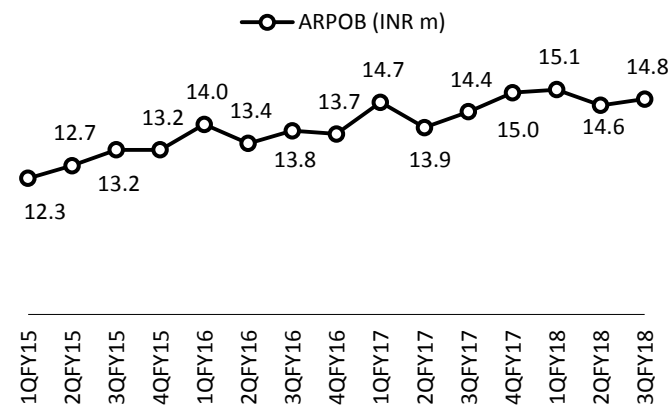
Source: MOSL, Company

Exhibit 5: Occupancy



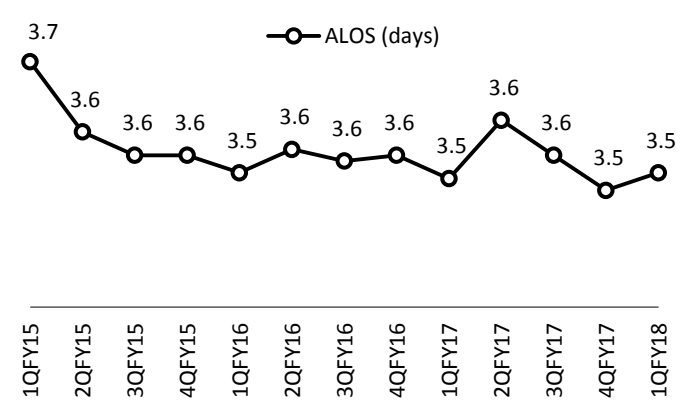
Source: MOSL, Company

Exhibit 6: ARPOB improved YoY



Source: MOSL, Company

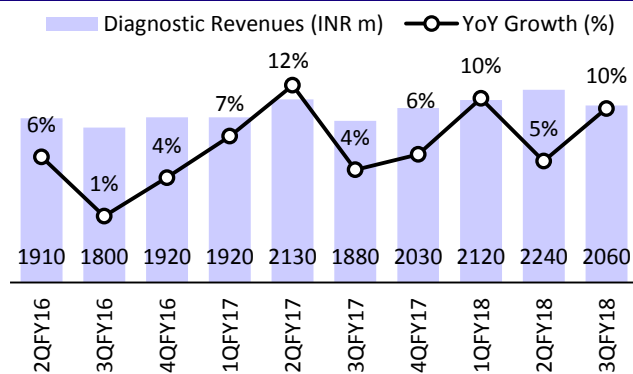
Exhibit 7: ALOS remained flat QoQ



Source: MOSL, Company

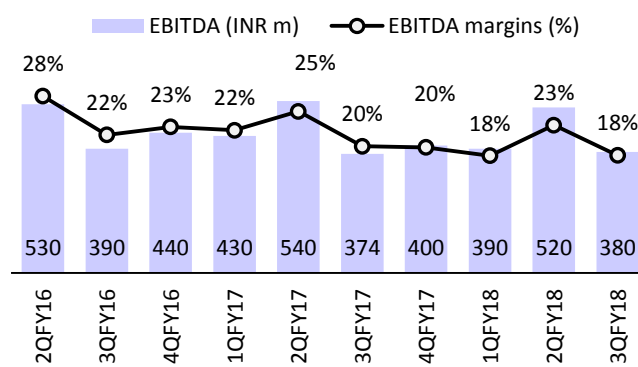
Story in charts- Diagnostics

Exhibit 8: Diagnostic revenues grew 10% YoY



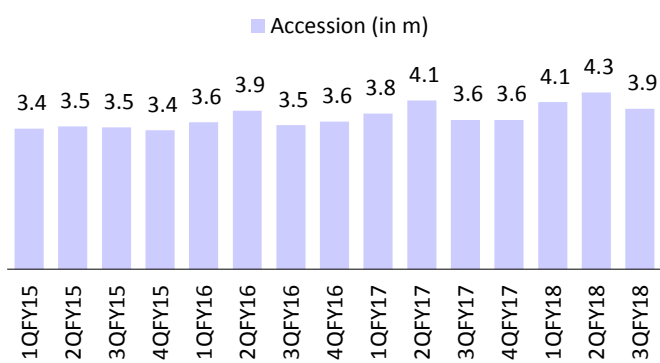
Source: MOSL, Company

Exhibit 9: Diagnostic EBITDA margin shrunk to 18%



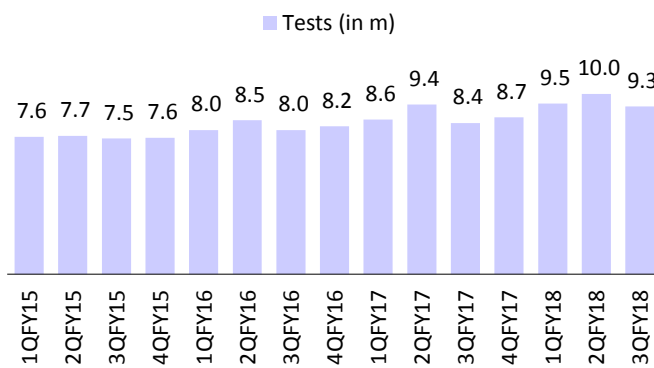
Source: MOSL, Company

Exhibit 10: Sample volumes



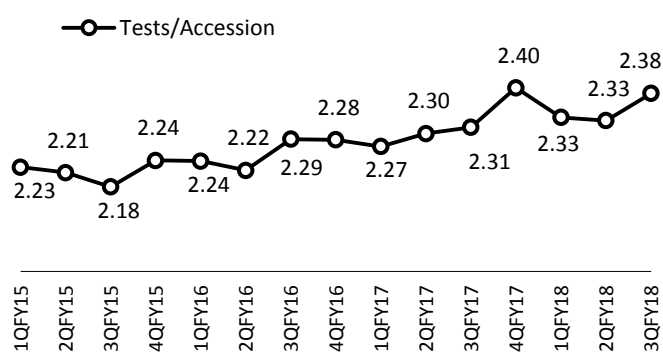
Source: MOSL, Company

Exhibit 11: No of tests conducted increased 11%YoY



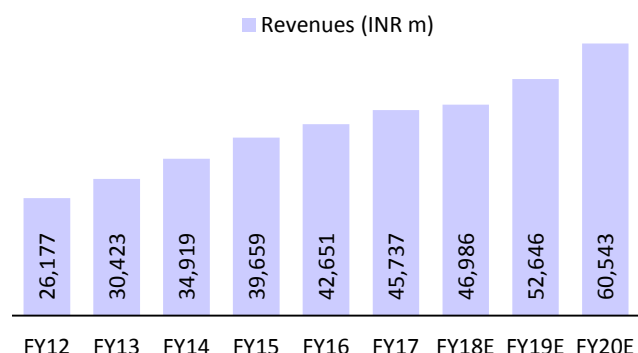
Source: MOSL, Company

Exhibit 12: No of tests/sample increased 3% YoY



Source: MOSL, Company

Exhibit 13: FORH revenues to exhibit 10% CAGR over FY17-20E



Source: MOSL, Company

Story in charts

Exhibit 14: FORH EBITDA to exhibit 35% CAGR over FY17-20E

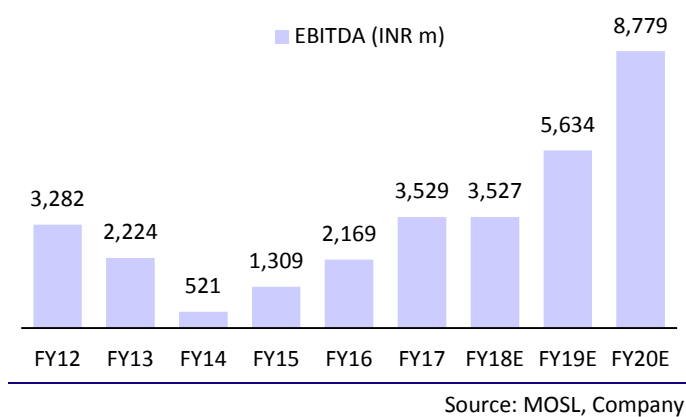


Exhibit 15: Hospital revenues to exhibit 10% CAGR over FY17-20E

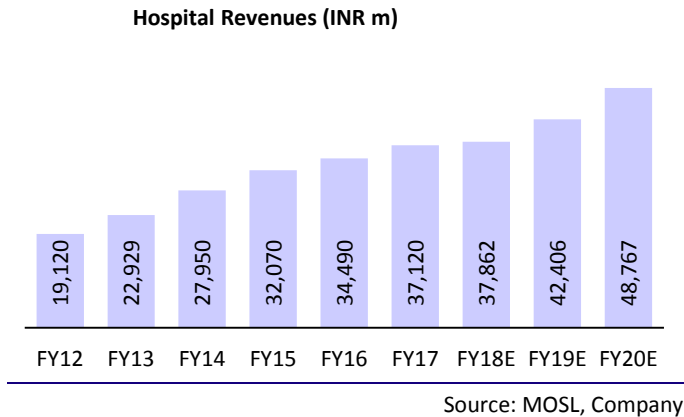


Exhibit 16: Hospital EBITDA margins to improve due to robust EBITDAC growth and lower BT costs

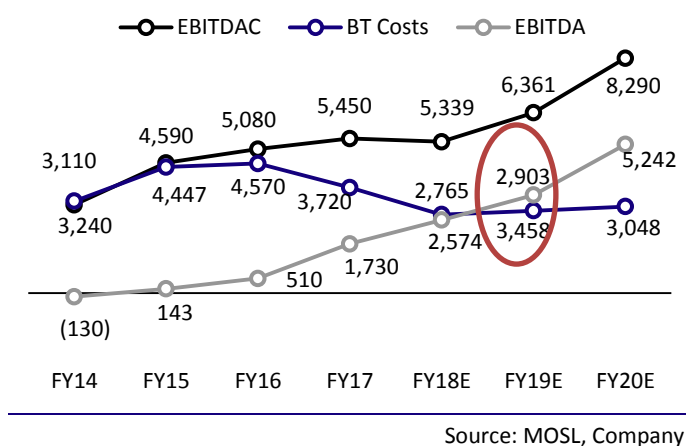
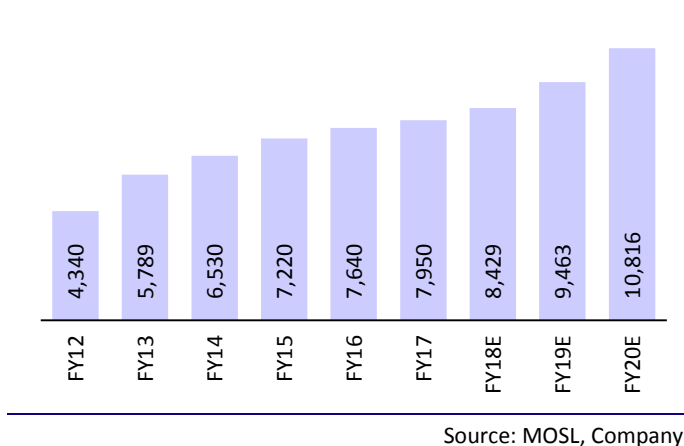


Exhibit 17: Diagnostic revenues to exhibit 11% CAGR over FY17-20E



Valuation

FORH stock has remained volatile in the recent past on the back of news flow related to issues with the current promoter and possibility of equity infusion in the company. Given that current promoter holding is marginal, banks/financial institutes may look to find a new investor which could lead to stock re-rating. We have valued the hospital and diagnostic business based on 20x and 18x 1H FY20E EV/EBITDA, respectively. We have cut our EBITDA by 26%/9% for FY19/20E as we build slower margin ramp-up.

Exhibit 18: SOTP based target price of INR185 provides ~15% upside to CMP

SOTP			Methodology	
(INR m)	1HFY20E	INR/ Share		
SRL (56% stake Diagnostic business)	27,331	20 x	52	EV/EBITDA x
Domestic hospital	79,170	18 x	151	EV/EBITDA x
Fortis stake in business trust (~30%)	9,600	CMP	18	CMP
Target EV (INR m)	116,101			
Net debt/cash	-13,000			
Monetization of non-core assets	5,000			Land Parcels in Delhi, Mohali & minority interest in Sri Lankan hospital
Minority interest in FHTL	-13,000			
Implied Equity Value	95,101			
Diluted Shares Outstanding	523			
Target Price (INR/share)	185			

Source: Company, MOSL

Key catalysts driving stock performance over medium term are:

- Buyback of RHT using proceeds from fresh equity issuance.
- Faster ramp-up of new hospitals, including FMRI, Bangalore, Ludhiana and Chennai.
- SRL business, in our view, trades at a significant discount to peers; demerger of the business should help unlock value for shareholders.

Financials and valuations

Consolidated - Income Statement

(INR Million)

Y/E March	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Total Income from Operations	34,919	39,659	42,651	45,737	46,986	52,646	60,543
Change (%)	14.8	13.6	7.5	7.2	2.7	12.0	15.0
Raw Materials	8,807	9,345	9,572	9,976	10,102	11,056	12,714
Employees Cost	6,952	7,646	8,260	9,054	8,223	9,213	10,292
Other Expenses	18,639	21,358	22,650	23,179	25,135	26,743	28,758
Total Expenditure	34,398	38,349	40,482	42,208	43,460	47,012	51,765
% of Sales	98.5	96.7	94.9	92.3	92.5	89.3	85.5
EBITDA	521	1,309	2,169	3,529	3,527	5,634	8,779
Margin (%)	1.5	3.3	5.1	7.7	7.5	10.7	14.5
Depreciation	1,828	2,346	2,295	2,222	2,350	2,800	3,400
EBIT	-1,307	-1,036	-125	1,307	1,177	2,834	5,379
Int. and Finance Charges	2,502	1,518	1,249	2,294	2,400	1,500	800
Other Income	1,674	887	926	1,660	300	300	300
PBT bef. EO Exp.	-2,135	-1,667	-448	673	-923	1,634	4,879
EO Items	-51	68	212	-16	0	0	0
PBT after EO Exp.	-2,186	-1,599	-236	656	-923	1,634	4,879
Total Tax	107	45	466	724	-305	539	1,610
Tax Rate (%)	-4.9	-2.8	-197.4	110.3	33.0	33.0	33.0
Minority Interest/ associate income	-105	-458	-443	-4,861	-243	-182	-108
Reported PAT - Continuing Opr.	-2,188	-1,186	-259	4,793	-375	1,277	3,377
Adjusted PAT - Continuing Opr.	-2,134	-1,256	-890	4,791	-375	1,277	3,377
Change (%)	-17.0	-41.1	-29.1	-638.2	-107.8	-440.1	164.5
Margin (%)	-6.1	-3.2	-2.1	10.5	-0.8	2.4	5.6

Consolidated - Balance Sheet

(INR Million)

Y/E March	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Equity Share Capital	4,628	4,628	4,631	5,177	5,777	5,777	5,777
Preference Capital/ FCCB	6,700	0	3,000	0	0	0	0
Total Reserves	38,196	35,848	36,980	46,258	50,886	52,150	55,491
Net Worth	49,524	40,476	44,612	51,435	56,663	57,927	61,268
Minority Interest	1,393	1,529	3,917	11,673	11,673	11,673	11,673
Total Loans	18,803	17,843	13,793	19,590	9,590	9,590	9,590
Deferred Tax Liabilities	350	-71	-2,250	-1,043	-1,043	-1,043	-1,043
Capital Employed	70,070	59,777	60,071	81,655	76,884	78,147	81,489
Gross Block	27,751	29,230	16,170	33,462	31,845	34,922	37,937
Less: Accum. Deprn.	10,056	11,726	1,915	3,722	6,072	8,872	12,272
Net Fixed Assets	17,695	17,504	14,255	29,740	25,773	26,050	25,665
Goodwill on Consolidation	23,773	24,673	22,391	24,778	24,778	24,778	24,778
Capital WIP	1,471	2,282	2,026	2,354	1,971	1,894	1,879
Total Investments	10,314	10,561	14,519	18,779	18,779	18,779	18,779
Curr. Assets, Loans&Adv.	25,255	20,826	16,877	19,188	14,568	16,555	21,565
Inventory	620	640	600	616	645	697	768
Account Receivables	4,407	4,094	4,637	4,839	6,436	7,212	8,294
Cash and cash equivalents	10,446	5,970	1,672	5,465	-3,493	-3,657	-1,644
Loans and Advances	9,782	10,122	9,967	8,269	10,980	12,303	14,148
Curr. Liability & Prov.	8,438	16,069	10,006	13,183	9,006	9,930	11,199
Account Payables	5,061	5,649	5,614	5,887	4,167	4,508	4,964
Other Current Liabilities	2,477	9,316	3,518	6,135	3,876	4,343	4,994
Provisions	899	1,103	874	1,161	963	1,079	1,241
Net Current Assets	16,817	4,757	6,870	6,005	5,562	6,625	10,367
Appl. of Funds	70,070	59,777	60,062	81,655	76,862	78,125	81,467

Financials and valuations

Ratios

Y/E March	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
Basic (INR)							
EPS	-4.6	-2.7	-1.9	10.3	-0.8	2.8	7.3
Cash EPS	-0.7	2.4	3.0	15.1	4.3	8.8	14.6
BV/Share	106.9	87.4	96.3	111.1	122.3	125.1	132.3
DPS	0.0	0.0	0.0	0.0	0.0	0.0	0.1
Payout (%)	-0.2	-0.9	-2.4	0.0	1.1	1.1	1.1
Valuation (x)							
P/E		-59.3	-83.7	15.5	-198.4	58.3	22.1
Cash P/E		68.3	53.0	10.6	37.7	18.3	11.0
P/BV		1.8	1.7	1.4	1.3	1.3	1.2
EV/Sales		2.2	2.0	1.9	1.9	1.7	1.4
EV/EBITDA		66.0	39.9	25.1	24.8	15.6	9.8
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0	0.0	0.0
FCF per share	-1.3	1.3	-0.8	15.4	-5.8	1.9	5.3
Return Ratios (%)							
RoE	-4.6	-2.8	-2.1	10.0	-0.7	2.2	5.7
RoCE	0.4	-0.2	1.0	3.4	1.4	3.1	5.5
RoIC	-2.0	-2.6	-0.2	2.1	1.4	3.1	5.8
Working Capital Ratios							
Fixed Asset Turnover (x)	1.3	1.4	2.6	1.4	1.5	1.5	1.6
Asset Turnover (x)	0.5	0.7	0.7	0.6	0.6	0.7	0.7
Inventory (Days)	6	6	5	5	5	5	5
Debtor (Days)	46	38	40	39	50	50	50
Creditor (Days)	53	52	48	47	32	31	30
Leverage Ratio (x)							
Current Ratio	3.0	1.3	1.7	1.5	1.6	1.7	1.9
Interest Cover Ratio	-0.5	-0.7	-0.1	0.6	0.5	1.9	6.7
Net Debt/Equity	0.2	0.3	0.3	0.3	0.2	0.2	-0.1

Consolidated - Cash Flow Statement

(INR Million)

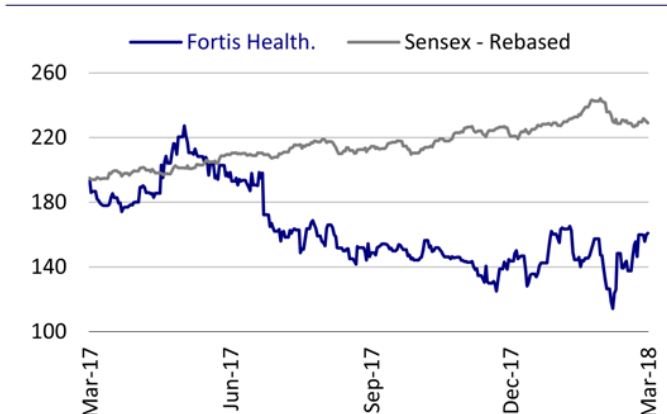
Y/E March	FY14	FY15	FY16	FY17	FY18E	FY19E	FY20E
OP/(Loss) before Tax	1,491	-1,374	338	5,517	-923	1,634	4,879
Depreciation	2,479	2,628	2,251	2,222	2,350	2,800	3,400
Interest & Finance Charges	1,839	1,048	733	1,197	2,100	1,200	500
Direct Taxes Paid	-1,049	-1,193	-1,324	-1,112	305	-539	-1,610
(Inc)/Dec in WC	-203	-280	440	2,097	-8,515	-1,227	-1,729
CF from Operations	4,556	829	2,438	9,921	-4,684	3,868	5,440
Others	235	-587	-492	-19	0	0	0
CF from Operating incl EO	4,791	242	1,947	9,902	-4,684	3,868	5,440
(Inc)/Dec in FA	-5,413	383	-2,299	-2,776	2,000	-3,000	-3,000
Free Cash Flow	-622	625	-353	7,126	-2,684	868	2,440
(Pur)/Sale of Investments	-5,858	4,097	1,918	-12,033	0	0	0
Others	42,162	-6,162	1,509	4,556	300	300	300
CF from Investments	30,891	-1,682	1,128	-10,254	2,300	-2,700	-2,700
Issue of Shares	10,196	1	32	79	5,600	0	0
Inc/(Dec) in Debt	-37,737	-1,539	-2,238	6,592	-10,000	0	0
Interest Paid	-3,777	-1,400	-1,337	-2,299	-2,400	-1,500	-800
Dividend Paid	0	0	0	0	4	-13	-36
Others	-854	-98	0	0	243	182	108
CF from Fin. Activity	-32,172	-3,035	-3,543	4,372	-6,553	-1,332	-727
Inc/Dec of Cash	3,510	-4,475	-468	4,020	-8,936	-164	2,013
Opening Balance	6,936	10,446	1,888	1,423	5,443	-3,493	-3,657
Closing Balance	10,446	5,970	1,419	5,443	-3,493	-3,657	-1,644

Corporate profile

Company description

Incorporated in 1991, the Hyderabad-based Granules India (GRAN) is a vertically integrated manufacturer of pharmaceutical products. It is among the largest manufacturers of Paracetamol and Ibuprofen in the world. It derives 63% of its business from Europe and the US. GRAN also has a formulations plant, with a capacity to produce 18b tablets per annum. It has its own Abbreviated New Drug Applications (ANDAs) and dossiers. GRAN services more than 300 customers across 60 nations (exports are ~87% of revenues).

Exhibit 1: Sensex rebased



Source: MOSL/Bloomberg

Exhibit 2: Shareholding pattern (%)

	Dec-17	Sep-17	Dec-16
Promoter	34.4	34.3	67.6
DII	9.9	9.0	1.1
FII	30.4	33.8	20.7
Others	25.3	22.9	10.6

Note: FII Includes depository receipts

Source: Capitaline

Exhibit 3: Top holders

Holder Name	% Holding
East Bridge Capital Master Fund Limited	4.1
Wf Asian Smaller Companies Fund Limited	3.5
Societe Generale	3.4
Morgan Stanley Mauritius Company Limited	2.8
Icici Prudential Top 100 Fund	2.0

Source: Capitaline

Exhibit 4: Top management

Name	Designation
Harpal Singh	Director
Malvinder Mohan Singh	Executive Chairman
Rahul Ranjan	Company Secretary
Shivinder Mohan Singh	Vice Chairman

Source: Capitaline

Exhibit 5: Directors

Name	Name
Brian W Tempest	P S Joshi
Joji Sekhon Gill	Pradeep Ratilal Raniga

*Independent

Exhibit 6: Auditors

Name	Type
Deloitte Haskins & Sells LLP	Statutory
Jitender, Navneet & Co	Cost Auditor

Source: Capitaline

Exhibit 7: MOSL forecast v/s consensus

EPS (INR)	MOSL forecast	Consensus forecast	Variation (%)
FY19	2.8	4.5	-39.4
FY20	7.3	7.1	3.3

Source: Bloomberg

NOTES

Explanation of Investment Rating	
Investment Rating	Expected return (over 12-month)
BUY	>=15%
SELL	< - 10%
NEUTRAL	> - 10 % to 15%
UNDER REVIEW	Rating may undergo a change
NOT RATED	We have forward looking estimates for the stock but we refrain from assigning recommendation

*In case the recommendation given by the Research Analyst becomes inconsistent with the investment rating legend, the Research Analyst shall within 28 days of the inconsistency, take appropriate measures to make the recommendation consistent with the investment rating legend.

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