

Inorganic foray into non-core markets; scalability key monitorable

Healthcare ▶ Company Update ▶ December 10, 2024

TARGET PRICE (Rs): 2,400

MHL announced its acquisition of Core Diagnostics—an oncology focused diagnostics chain with majority of its revenue derived from North/East India—for Rs2.47bn, thus valuing the company at ~2.24x EV/Sales on FY24 revenue. While the acquisition ticks most boxes wrt MHL's inorganic strategy outlined in the past (high-end testing, complementary geographical mix, reasonable valuations), its scalability via cross-selling MHL's offerings to oncology-focused B2C customers of Core Diagnostics and the resultant profitability could be challenging, in our view. We derive comfort from management's track record of successful acquisitions (Exhibit 2), and its expectation of the transaction being EPS accretive from FY26 (on the back of cost synergies, cross selling); albeit the 6-8Y payback period is likely to be a drag on ROCE. We retain BUY on MHL.

Metropolis Healthcare: Financial Snapshot (Consolidated)

Y/E Mar (Rs mn)	FY23	FY24	FY25E	FY26E	FY27E
Revenue	11,482	12,077	13,393	15,331	17,539
EBITDA	2,883	2,826	3,395	4,011	4,729
Adj. PAT	1,434	1,278	1,737	2,190	2,737
Adj. EPS (Rs)	28.0	25.0	33.9	42.7	53.4
EBITDA margin (%)	25.1	23.4	25.3	26.2	27.0
EBITDA growth (%)	(15.9)	(2.0)	20.1	18.1	17.9
Adj. EPS growth (%)	(33.0)	(11.0)	35.9	26.1	25.0
RoE (%)	15.3	12.3	15.0	16.7	18.1
RoIC (%)	17.1	15.6	18.9	24.8	32.2
P/E (x)	78.1	87.8	64.6	51.2	41.0
EV/EBITDA (x)	38.8	39.5	32.4	26.9	22.3
P/B (x)	11.3	10.2	9.2	8.0	6.9
FCFF yield (%)	1.8	1.9	2.1	2.8	3.3

Source: Company, Emkay Research

Acquisition of Core Diagnostics, a leading oncology diagnostics chain

MHL has approved the 100% acquisition of Core Diagnostics for a purchase consideration of ~Rs2.47bn, partially funded by cash (Rs1.36bn) and partly via equity issuance of ~0.5mn shares, amounting to 1% dilution post-allotment. The transaction values the company at 2.2x EV/Sales on FY24 revenue and per the management's internal calculations at 13.5-14x EV/EBITDA on FY26 basis. As per the management, the acquisition would enhance MHL's specialty portfolio (therapy monitoring tests as well as cancer confirmatory tests), thereby allowing it to provide an end-to-end test menu and to tap into the high-growth oncology diagnostics vertical, which is a ~Rs40-50bn market slated to see 17.5% CAGR over the next 5 years. With this acquisition, MHL's revenue contribution from oncology would grow to 10% from 4%, while specialty contribution would inch up to 41% from 37%. Cost synergies like rationalization of overhead costs, and optimization of network and logistics along with procurement efficiency of reagents should aid profitability, as MHL endeavors to scale up this asset by cross-selling its non-oncology test menu to the Core Diagnostics customer network.

Inexpensive valuation; M&A track record provides comfort on turnaround

Owing to its sub-scale and focus on single specialty testing, Core's profitability has been sub-par (EBITDA losses in FY23; low single-digit margin in FY24). MHL has bagged this asset at relatively inexpensive valuations (2.2x EV/Sales and 14x EV/EBITDA on FY26, as per management), with a complementary geographical mix (North/East focus, which only contributes 8%/4% of MHL's current revenue, respectively) and specialized testing capabilities (only 30% overlap in oncology). The management's successful track record of scaling up and turning around assets provides comfort on cost synergies and network integration, though we note that cross selling the non-oncology test menu to Core's B2C network could be challenging. We will incorporate the Core Diagnostics acquisition in our estimates once the transaction closes (within 60 days). We retain BUY on MHL, with unchanged TP of Rs2,400 (based on DCF methodology).

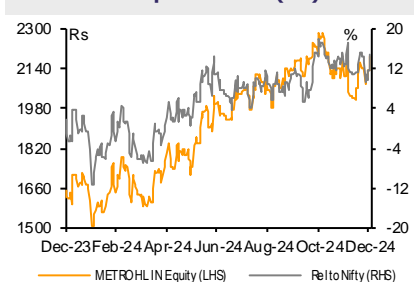
Target Price – 12M	Sep-25
Change in TP (%)	-
Current Reco.	BUY
Previous Reco.	BUY
Upside/(Downside) (%)	9.5
CMP (09-Dec-24) (Rs)	2,190.5

Stock Data	Ticker
52-week High (Rs)	2,318
52-week Low (Rs)	1,450
Shares outstanding (mn)	51.3
Market-cap (Rs bn)	112
Market-cap (USD mn)	1,325
Net-debt, FY25E (Rs mn)	-2,141
ADTV-3M (mn shares)	-
ADTV-3M (Rs mn)	317.3
ADTV-3M (USD mn)	3.7
Free float (%)	-
Nifty-50	24,619
INR/USD	84.7
Shareholding, Sep-24	
Promoters (%)	49.4
FPIs/MFs (%)	18.6/28.0

Price Performance

(%)	1M	3M	12M
Absolute	3.5	1.7	32.5
Rel. to Nifty	1.6	3.0	12.8

1-Year share price trend (Rs)



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Exhibit 1: Overview of Core Diagnostics network – North and East focus to complement MHL

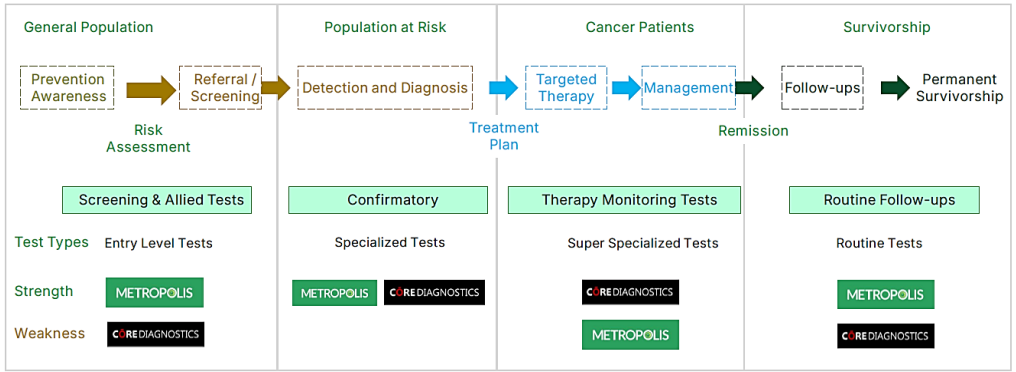
Source: Emkay Research

Exhibit 2: Acquisitions made by MHL over the years

Acquired company	Year of acquisition	Location	Revenue at the time of acquisition (Rs mn)
Sudharma Metropolis Health Services	2003	Kerala	18
Lister Lab	2006	Chennai	NA
Desai Metropolis Health Services	2006	Mumbai	NA
Golwilkar Metropolis Health Services	2006	Pune	39
Desai Metropolis Health Services	2008	Surat	34
RV Metropolis Diagnostics & Healthcare Centre	2008	Bengaluru	36
Micron	2011	Chennai	NA
Lab One	2012	Bengaluru	NA
Amin's Pathology	2012	Ahmedabad	NA
Raj Diagnostics	2012	Mumbai	NA
Dr Patel Metropolis Healthcare	2012	Nasik	18
Ekopath	2013	Kolkata	NA
Sanjeevani Rajkot	2017	Rajkot	120
Hitech Diagnostics	2022	Chennai	1,240

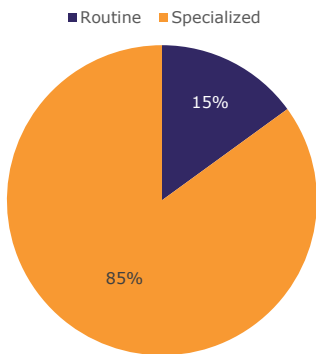
Source: Company, Emkay Research

Exhibit 3: MHL will get a strong footing in the fast-growing oncology diagnostics market, leveraging Core’s super specialty test menu



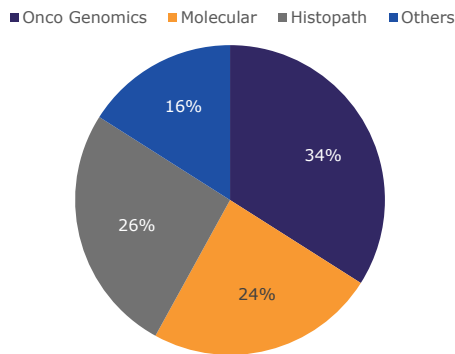
Source: Company, Emkay Research

Exhibit 4: Specialized testing contributes to 85% of revenues...



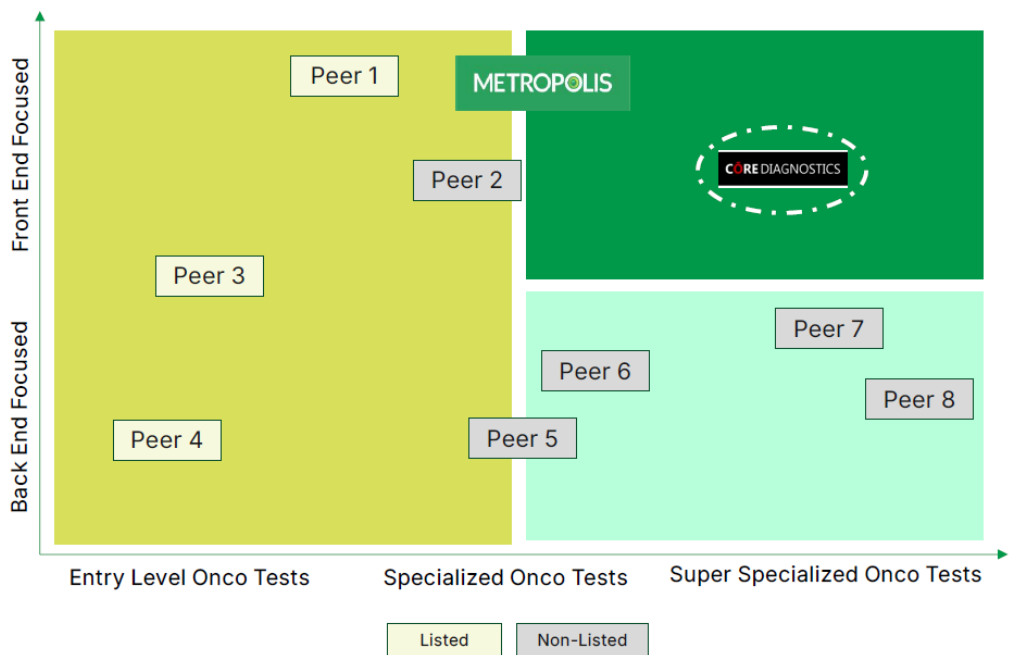
Source: Company, Emkay Research

Exhibit 5: ...with high-end onco-genomics testing amounting to 1/3rd revenues



Source: Company, Emkay Research

Exhibit 6: MHL and Core Diagnostics have 30% overlap in their oncology test menus



Source: Company, Emkay Research

Exhibit 7: Acquisition would lead to a 9-10% increase in revenues; however, ROCE is likely to be dragged down by 200bps

Pro forma financials (FY26)			
Particulars (Rs mn)	Metropolis (Emkay estimates)	Core Diagnostics*	Combined entity
Sales	15,331	1,357	16,688
EBITDA	4,011	183	4,194
- margin	26.2%	13.5%	25.1%
EBIT	2,917	159	3,076
Capital employed	15,607		18,075
ROCE	19%		17%

Source: Company, Emkay Research. *Note: Assumptions: i) H1FY25 revenue is annualized and expected to grow 15% in FY26E; ii) EBITDA margin is assumed basis management guidance on the acquisition multiple of 13.5-14x EV/EBITDA; iii) D&A as a % of gross block to be the same as that of MHL

Exhibit 8: Operational strengths of the combined entity

FY24 (mn)	Metropolis	Core Diagnostics	Combined entity
Total Revenue	11,890	1,100	12,990
Specialty Revenue	4,400	930	5,330
Specialty as a % of Contribution	37%	85%	41%
North and East			
Oncology Sales Team	10	36	46
Oncologist Connect	300	900	1,200
Oncology Reach			
Oncology Sales Team	30	100	130
Oncologist Connect	600	1,600	2,200

Source: Company, Emkay Research

Call Highlights

- Core's recent gross margin was a low ~60%, as affordability becomes a concern given that there is no insurance available for such high-end tests. The brand has been built on the back of specialty testing.
- The management expects FY26 profitability to inch up owing to optimization of the lab infrastructure and procurement costs. FY25 margins were low single-digit as per management.
- Firms like Core Diagnostics require a national player to be able to sustain and undertake scalability. Core has a menu with 1,300 high-end tests and >150 genome tests, but only focusses on one single specialty thus finding it difficult to scale up.
- MHL will now have the oncology portfolio under one roof, with 1.4mn cancer patients anticipated every year from targeting therapy and repeat customers, given the nature of the disease cycle. The management alluded to an organic expansion into the North and East would have taken ~6 years to scale up and build test capabilities
- The management commented on the payback period from the EBITDA perspective to be 6-8 years, and on PAT basis an additional 2-3 years.
- Based on internal calculations, the management suggested the transaction value at 14x FY26 EV/EBITDA multiple. It also indicated that it would take almost 3-4 years for the asset to match MHL's margin.
- The transaction would enable MHL to leverage cross-selling along with addition of super specialty oncology diagnostics to its test menu. Pharma-aligned operations of both the entities would centralize to one.
- On Core's price and volume dynamics, the management explained that new tests are launched, prices are higher as volume does not increase. Going ahead, with more volumes, prices are likely to come down. Volume CAGR would be 10% for the last 4-5 years.
- The value chain/cycle of Oncology diagnostics is not limited to radiology or screening. It starts with blood tests, followed by tissue testing and then screening.
- On the cost synergies front, the management pointed out that efficiency would come through optimization of procurement, lab processes, corporate overheads costs, salaries, and IT infrastructure.
- On the macro front, the management suggested oncology diagnostics market size of 40-50bn and expected to grow at 17.5% CAGR over next five years.

Metropolis Healthcare: Consolidated Financials and Valuations

Profit & Loss					
Y/E Mar (Rs mn)	FY23	FY24	FY25E	FY26E	FY27E
Revenue	11,482	12,077	13,393	15,331	17,539
Revenue growth (%)	(6.5)	5.2	10.9	14.5	14.4
EBITDA	2,883	2,826	3,395	4,011	4,729
EBITDA growth (%)	(15.9)	(2.0)	20.1	18.1	17.9
Depreciation & Amortization	892	945	1,072	1,094	1,120
EBIT	1,991	1,881	2,323	2,917	3,609
EBIT growth (%)	(28.8)	(5.5)	23.5	25.5	23.7
Other operating income	0	0	0	0	0
Other income	152	91	114	171	239
Financial expense	268	225	134	161	177
PBT	1,875	1,747	2,303	2,927	3,671
Extraordinary items	0	0	0	0	0
Taxes	441	462	560	732	929
Minority interest	0	(6)	(6)	(5)	(5)
Income from JV/Associates	0	0	0	0	0
Reported PAT	1,434	1,278	1,737	2,190	2,737
PAT growth (%)	(33.0)	(10.9)	35.9	26.1	25.0
Adjusted PAT	1,434	1,278	1,737	2,190	2,737
Diluted EPS (Rs)	28.0	25.0	33.9	42.7	53.4
Diluted EPS growth (%)	(33.0)	(11.0)	35.9	26.1	25.0
DPS (Rs)	12.0	12.0	9.0	9.0	9.0
Dividend payout (%)	(42.8)	(48.1)	(26.5)	(21.1)	(16.8)
EBITDA margin (%)	25.1	23.4	25.3	26.2	27.0
EBIT margin (%)	17.3	15.6	17.3	19.0	20.6
Effective tax rate (%)	23.5	26.5	24.3	25.0	25.3
NOPLAT (pre-IndAS)	1,522	1,383	1,758	2,188	2,696
Shares outstanding (mn)	51.1	51.2	51.2	51.2	51.2

Source: Company, Emkay Research

Cash flows					
Y/E Mar (Rs mn)	FY23	FY24	FY25E	FY26E	FY27E
PBT	1,875	1,747	2,303	2,927	3,671
Others (non-cash items)	0	0	0	0	0
Taxes paid	(441)	(462)	(560)	(732)	(929)
Change in NWC	780	254	(321)	(145)	(284)
Operating cash flow	2,471	2,641	2,764	3,384	3,767
Capital expenditure	(526)	(638)	(503)	(498)	(465)
Acquisition of business	7	(400)	0	0	0
Interest & dividend income	57	33	0	0	0
Investing cash flow	468	(894)	(489)	(427)	(326)
Equity raised/(repaid)	0	0	0	0	0
Debt raised/(repaid)	(1,795)	(791)	0	0	0
Payment of lease liabilities	0	592	250	250	250
Interest paid	(268)	(225)	(134)	(161)	(177)
Dividend paid (incl tax)	(614)	(615)	(461)	(461)	(461)
Others	(1,000)	(500)	(250)	(250)	(250)
Financing cash flow	(3,676)	(2,131)	(845)	(872)	(889)
Net chg in Cash	(737)	(384)	1,429	2,085	2,553
OCF	2,471	2,641	2,764	3,384	3,767
Adj. OCF (w/o NWC chg.)	3,251	2,895	2,442	3,239	3,483
FCFF	1,945	2,003	2,261	2,886	3,302
FCFE	1,734	1,810	2,126	2,725	3,124
OCF/EBITDA (%)	85.7	93.5	81.4	84.4	79.7
FCFE/PAT (%)	120.9	141.6	122.4	124.4	114.2
FCFF/NOPLAT (%)	127.7	144.8	128.6	131.9	122.5

Source: Company, Emkay Research

Balance Sheet					
Y/E Mar (Rs mn)	FY23	FY24	FY25E	FY26E	FY27E
Share capital	102	102	102	102	102
Reserves & Surplus	9,780	10,859	12,141	13,875	16,156
Net worth	9,882	10,962	12,243	13,977	16,258
Minority interests	25	31	31	31	31
Deferred tax liability (net)	713	674	674	674	674
Total debt	791	0	0	0	0
Total liabilities & equity	11,411	11,667	12,949	14,683	16,963
Net tangible fixed assets	1,372	1,559	1,673	1,779	1,800
Net intangible assets	3,553	3,863	3,685	3,506	3,328
Net ROU assets	1,734	1,801	1,397	974	575
Capital WIP	0	0	0	0	0
Goodwill	4,547	4,547	4,547	4,547	4,547
Investments [JV/Associates]	148	548	548	548	548
Cash & equivalents	932	712	2,141	4,226	6,779
Current assets (ex-cash)	2,465	2,443	2,623	2,678	2,893
Current Liab. & Prov.	3,536	3,807	3,666	3,575	3,507
NWC (ex-cash)	(1,071)	(1,364)	(1,043)	(898)	(614)
Total assets	11,411	11,667	12,948	14,682	16,963
Net debt	(141)	(712)	(2,141)	(4,226)	(6,779)
Capital employed	11,411	11,667	12,949	14,683	16,963
Invested capital	10,331	10,406	10,259	9,908	9,636
BVPS (Rs)	193.3	214.0	239.0	272.8	317.4
Net Debt/Equity (x)	0.0	(0.1)	(0.2)	(0.3)	(0.4)
Net Debt/EBITDA (x)	0.0	(0.3)	(0.6)	(1.1)	(1.4)
Interest coverage (x)	0.1	0.1	0.1	0.1	0.0
RoCE (%)	16.2	14.8	17.1	19.6	21.7

Source: Company, Emkay Research

Valuations and key Ratios					
Y/E Mar	FY23	FY24	FY25E	FY26E	FY27E
P/E (x)	78.1	87.8	64.6	51.2	41.0
P/CE(x)	46.5	48.8	38.6	33.0	28.1
P/B (x)	11.3	10.2	9.2	8.0	6.9
EV/Sales (x)	9.7	9.2	8.2	7.0	6.0
EV/EBITDA (x)	38.8	39.5	32.4	26.9	22.3
EV/EBIT(x)	54.3	57.2	45.7	35.7	28.2
EV/IC (x)	10.5	10.3	10.4	10.5	10.5
FCFF yield (%)	1.8	1.9	2.1	2.8	3.3
FCFE yield (%)	1.6	1.7	2.0	2.5	2.9
Dividend yield (%)	0.5	0.5	0.4	0.4	0.4
DuPont-RoE split					
Net profit margin (%)	12.5	10.6	13.0	14.3	15.6
Total asset turnover (x)	2.1	1.8	1.9	2.0	2.1
Assets/Equity (x)	1.3	1.1	1.1	1.1	1.0
RoE (%)	15.3	12.2	14.9	16.7	18.1
DuPont-RoIC					
NOPLAT margin (%)	13.3	11.5	13.1	14.3	15.4
IC turnover (x)	1.0	1.0	1.1	1.3	1.6
RoIC (%)	17.1	15.6	18.9	24.8	32.2
Operating metrics					
Core NWC days	23.0	19.8	19.8	14.8	13.6
Total NWC days	23.0	19.8	19.8	14.8	13.6
Fixed asset turnover	2.1	1.8	1.9	2.0	2.1
Opex-to-revenue (%)	52.3	55.4	53.2	52.9	52.1

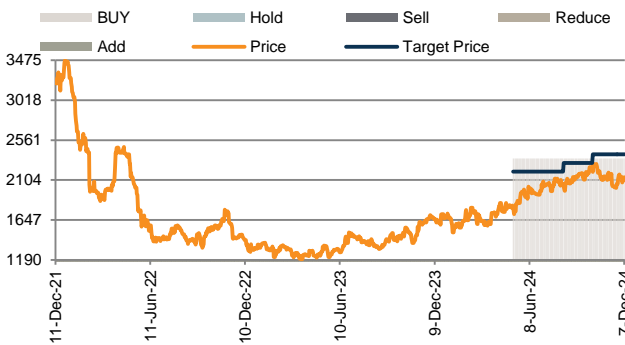
Source: Company, Emkay Research

RECOMMENDATION HISTORY - DETAILS

Date	Closing Price (INR)	TP (INR)	Rating	Analyst
11-Nov-24	2,155	2,400	Buy	Anshul Agrawal
07-Oct-24	2,198	2,400	Buy	Anshul Agrawal
12-Aug-24	2,039	2,300	Buy	Anshul Agrawal
22-May-24	1,956	2,200	Buy	Anshul Agrawal
07-May-24	1,779	2,200	Buy	Anshul Agrawal

Source: Company, Emkay Research

RECOMMENDATION HISTORY - TREND



Source: Company, Bloomberg, Emkay Research

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