Apollo Hospitals
Q2 & H1 FY20 Earnings Conference Call Transcript
November 15, 2019

Moderator: Ladies and gentlemen, good day and welcome to Apollo Hospitals Ltd. Q2 FY20 earnings conference call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing “*” and then “0” on your touch tone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Mayank Vaswani from CDR India. Thank-you and over to you sir.

Mayank Vaswani: Thank-you Stanford. Good afternoon everyone and thank you for joining us on this call to discuss the financial results of Apollo Hospitals for Q2 and H1 of FY '20 which were announced yesterday. We have with us on the call, the senior management team comprising Ms. Suneeta Reddy – Managing Director, Mr. A. Krishnan – Chief Financial Officer and Mr. C. Chandra Sekhar – COO of AHLL and Mr. Obul Reddy – Chief Financial Officer of the Pharmacy business.

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 the investor presentation.

Documents relating to our financial performance have been shared with all of you earlier and these have also been posted on our corporate website. I would now like to turn the call over to Ms. Suneeta Reddy for her opening remarks.

Suneeta Reddy: Good afternoon everyone and thank you for taking time out for this call. I trust that you have received the earnings documents which we had shared earlier.

We are really glad to report that this quarter the fact that we have achieved several important milestones that we have guided you towards.

Firstly, our mature hospitals achieved a 70% plus occupancy. Alongside, there was double-digit IP volume growth across all our units, supported by 17% volume growth from our new units. This is a healthy growth rate, given the high volume base across which we operate. Mature hospitals have recorded an ROCE in excess of 25%, which validates our strategy of case mix calibration and our COE focus.
Secondly, the quarter saw a stellar performance from the SAP business. The business recorded 6% EBITDA margin, and has achieved an ROCE of 25%. A higher proportion of OTC and generic sales, along with Private label increasing to 7.9%, has contributed to the profitability.

Thirdly, AHLL has recorded revenues of Rs. 181 crore for the quarter, a 22% growth over prior year. The Company has turned EBITDA positive for the first time, with an EBITDA of Rs. 2.5 crore for the quarter. This is in line with our plan to make this business profitable, while delivering healthy top-line growth.

In summary, this has been a very satisfying quarter, a quarter of promises kept.

Against this backdrop, I am pleased to share the results for Q2FY20.

Q2 Revenues grew 18% to Rs. 2,464 crore; aided by Healthcare services growth of 15% to Rs. 1,291 crore and SAP growth of 22%. New hospitals reported revenues of Rs. 281 crore, representing a 17% year-on-year growth, while mature hospitals grew 12%.

Q2 total Inpatient volumes grew by 10% on a year-on-year basis, supported by 17% IP volume growth in new units. Overall Q2FY20 occupancy across the Group was at 5,305 beds or 71%, compared to 5,020 beds or 70% in Q2 FY19. The occupancy in mature hospitals was at 3,980 beds or 73% and New hospitals had an occupancy at 1,324 beds or 67%.

Q2 overall EBITDA Post Ind AS 116 was at Rs. 364 crore. The Pre Ind AS 116 Q2FY20 EBITDA stood at Rs. 308 crore as compared to Rs. 258 crore in Q2 FY19, a year-on-year growth of 19%. Within this, Healthcare services EBITDA grew by 15% to Rs. 237 crore. Healthcare services margins were stable on a y-o-y basis at 18.4% in Q2FY20. New Hospitals registered an EBITDA of Rs. 24 crore in Q2FY20 vs. an EBITDA of Rs. 15 crore in Q2 FY19. The Proton unit reported an EBITDA loss of Rs 6.9 crore for the quarter. EBITDA margins in mature hospitals increased from 21.7% to 22.2%. New hospitals EBITDA margins improved from 6.1% in Q2FY19 to 8.4% in Q2FY20.

In SAP, Revenues grew 22% y-o-y on the back of strong same store sales and increasing off-take of in-house products. We added 111 stores on a net basis during the quarter taking the total to 3,607 stores. SAP EBITDA pre Ind-AS 116 grew 40% to Rs. 71 crore. EBITDA margin was at 6.0% and with the high asset returns in the business, SAP ROCE is now at 25%.

In November 2018, we had announced our plan to segregate our front-end retail pharmacy business in the SAP segment into a separate Company, i.e Apollo Pharmacies Ltd. (APL), which will be a wholly owned subsidiary of Apollo Medicals Pvt. Ltd.

The structure is targeted at creating a platform for us to execute on an omni-channel strategy for our Pharmacy business. It allows the Standalone Pharmacies to be housed in a regulatory compliant structure.

Our strategic intent for this vertical is clear; we are focused on taking the stores count to 5,000 and achieving a Rs. 10,000 crore in revenues, and increasing sales
from private label products, improving EBITDA & ROI, while simultaneously building our digital play. We are on course with this strategy, which is evident from the healthy, industry-leading EBITDA margins delivered by this vertical in this quarter.

We have recently launched ProHealth, a three-year comprehensive preventive health program, designed to keep consumers healthy. We believe this is in keeping with our promise to combat the country’s rising burden of NCDs.

We have also built strong thrust on our Oncology vertical. We have received a very encouraging response for our Proton facility. We have over 100 patients, completed or on the couch, with over 30% of them coming from overseas. It is a matter of great pride for us that India, and Apollo Hospitals is being widely recognized internationally as a major Oncology player with the Proton.

Our path for the future is clear; clinical and technological differentiation, premium positioning in domestic and overseas markets, and a strong strategic thrust on keeping India healthy. I believe we have made strong strides towards achieving these strategic priorities. We are confident that our robust and highly diversified model, backed by our promise of the highest standards of service and clinical outcomes, will continue to deliver on investor and stakeholder expectations.

I now open the floor for questions. Mr. Krishnan, Chandra Sekhar and Obul Reddy are here with me to take your questions.

**Moderator:** Thank you very much. Ladies and Gentlemen, we will now begin the question and answer session.

**Neha Manpuria:** First on AHLL, now that we have achieved EBITDA breakeven, how should we look at profitability for this business from FY ‘21, FY ‘22 perspective, when do you see it getting to sustainable profitability levels and what will be the driver for that?

**Chandra Sekhar:** I think we are aiming to build on improvement in gross margins, we have seen a year-on-year increase of about 6% to 7%. We want to increase that further to about another 300 basis points we want to add to the gross margin expansion. Revenue growth across verticals continues to be upward of 25%; that is the broad thesis at AHLL level. I think the future growth will be driven by revenue and gross margin expansion and control on costs and I think most of our costs are covered for our margin expansions will start looking good. We are looking at a range of 12% to 15% at a Company level to be achieved in the next 24 months on EBITDA margins.

**Neha Manpuria:** In the next 24 months you mentioned?

**Chandra Sekhar:** Yes, but this will be progressively there, we could reach that a little earlier as well, but that is the progressive path on which we are embarking steady state kind of numbers.

**Neha Manpuria:** Second, if I were to look at a new hospital performance in this quarter adjusted for the Proton loss and Navi Mumbai, there seems to have been moderation from quarter-on-quarter level, you know could you give some color as to, is there some deterioration in other new hospitals excluding Navi Mumbai?

**Krishnan A:** No, if you look at the quarter, the quarter has been quite good for the new hospitals and one of the things we have been focusing on all these new hospitals have been
profitable growth. I think we have been pushing most of them to ensure that they get to a profitable line of business especially some of the Tier-2 hospitals like Nellore and Trichy and Vizag, etc. The first objective of especially some of these Tier-2 hospitals has been to take in cases, which has been to ensure that the occupancy has been optimal and people get used to the hospital. After that the focus, which we have always been saying has been on profitability and you will see that in our numbers, you will see that as we are at 8.4% now, we know that we have a target to get to double digits very soon on new hospitals and then accelerate that to mid-teens in the next year, so we have our focus on that. Navi Mumbai is focused on that, Navi Mumbai has already come to a Rs. 10 crore EBITDA for the quarter, in fact Rs. 9.3 crore to be precise. Other hospitals are also doing well and you will see Nellore is doing much better now than earlier. We are seeing very good performance from Malleshwaram, you will see some of that in our results going forward.

Neha Manpuria: Sir, on Navi Mumbai could you give us some color in terms of when we can see more bed addition there, what occupancies are like?

Suneeta Reddy: So current occupancy on 230 beds is 200 beds. We hope to add 50 beds next quarter. So by the end of the year, we will be operating with close to 300 beds.

Neha Manpuria: Will this be for any specific specialty or?

Suneeta Reddy: No, it will be for all the specialties.

Moderator: The next question is from the line of Sudarshan Padmanabhan from Sundaram Mutual Fund.

Sudarshan Padmanabhan: My question is on the standalone pharmacies, you had mentioned earlier that strong growth has been seen in the same store growth. Can you elaborate a bit about what is the kind of growth that we have seen in the same-store growth, what is the changes that we have done to the business and how sustainable is the growth?

Obul Reddy: We have focused on store level sales and fixed up targets and rationalize the product mix, you know, so that is why, if you see that (inaudible) sales have grown about a quarter during about 100 basis points during the quarter, so it is more focusing at the store level and improving the revenue. Private Label sales now is about 8% of the total sales.

Suneeta Reddy: So the total margin has also moved up to 8.3% on mature.

Sudarshan Padmanabhan: And what is the same store growth?

Obul Reddy: About 9%.

Sudarshan Padmanabhan: My second question is on the recent transactions that you have done which basically would entail cash coming into the business and therefore deleveraging something that we had expected and in addition to that the pledge. I mean, are we in line in terms of the timelines that we had earlier discussed or is there any kind of a delay; can you just throw some light on the regulatory platform where we are at this point of time?

Suneeta Reddy: No, there is no delay. I think that the two projects we were working on is Apollo Pharmacy, the creation at the front-end and that will be done by January. The disinvestment of the insurance Company should be completed by the end of this
quarter, I mean we should get regulatory approvals, I think it will be the last quarter of the year where we actually see the money coming to us.

Sudarshan Padmanabhan: Any update on anything that we plan to do with this Proton, I mean getting a partner, where are we on that side?

Krishnan A.: As of now, if you look at, the Proton facility is doing very well, even before answering the partner question I would want you to note that the first gantry is operational. We have capitalized almost around 60% of the project, bulk of the CAPEX in fact only Rs. 100 crore, I do not know whether you noted in this we have only Rs. 100 crore of CAPEX spending now for Proton between next quarter and the quarter after that, so bulk of the CAPEX is all behind us. We have already grossed a Rs. 15 crore revenue in this quarter. This is with only one gantry and this will start generating independent of the partner, which is obviously dependent on how we work through and how we get to that level. I would like you to note that even if we do almost around 300 - 400 cases next year, that is what the plan is to get to almost 400 cases for the next year, you would see that this business will go to almost around Rs. 100 - Rs. 125 crore next year itself and that is a profitable business and the EBITDA of that business is almost around 40% plus. So independent of the partner plan, I think you will see even now, if you have seen Q1 to Q2 that EBITDA of this has come down from Rs. 8 crore loss to Rs. 7 crore loss, Q2 to Q3 you will further see the losses coming down and once Q1, all the three gantries of the treatment room are expected to be operationalized by Q4 of this year, so beginning Q1 of next year, you will see a significant uplift in this and we will cross the 125 mark on top line also, we are now at Rs. 15 crore. If you annualize that, that is already at a Rs. 60 crore annualized revenue, this will more than double in the next year.

Moderator: The next question is from the line of Ashi Anand from Allegro Capital.

Ashi Anand: Just wanted to understand that, you know the business economics between the smaller hospitals we have in Tier-2, Tier-3 cities versus the larger hospitals in metros and Tier-1, just in terms of how quickly they ramp up or longer term should we look at similar margins across the two, just your overall thoughts on this?

Krishnan A.: Yes, overall the margins are even in our Tier-2, if you look at a place like Madurai or other hospitals like Bhubaneswar or Mysore, our EBITDA margins there are and all those are a part of a mature hospital margin. If you look at our mature hospital margin, they are at 22% and in that while Chennai is obviously a bit higher, we still know that all of these margins are at 18% to 22% in that range and over a period of time all of them will go over 20 and an ROI of 18% is what all of these will get to. Yes, our focus now as I said is first to get to mid-teens in the next year on the new hospital success and after that high teens in the year after that, EBITDA margins.

Ashi Anand: Just looking at the CAPEX over the next two to three years, I just wanted to know strategically actually your thoughts between how we look at capital deployment across say the different business units that we have of hospitals, Tier-1 versus smaller ones, the pharmacy, the Proton and AHLL, where are we kind of pre-disposed towards having a larger amount of CAPEX?

Krishnan A.: So as of now if we look at the CAPEX, we have said that we will first look at getting significant cash flows out of our existing investments itself, because there is still quite a bit of headroom in our investments, so if you look at it we are as of now not looking at allocating any capital for any Greenfield project as we speak in the next one or two years, there is no Greenfield project plan now. Yes, Bombay has been a plan which is still an asset-light model, we continue to speak with them which even if it comes it will be three years out by the time the South-Bombay project is ready.
but if you look at our current CAPEX, our routine CAPEX is at the Rs. 200 crore level. We will continue to look at the routine CAPEX of Rs. 200 crore levels every year and pharmacy is another Rs. 50 to Rs. 60 crore of the CAPEX which will happen because of fresh store additions that is continuing. Apart from that, there is no deployment plan as such and even if there is any bolt-on acquisition, we will come to you at a later stage, there is no specific plan now.

**Moderator:** The next question is from the line of Anubhav Aggarwal from Credit Suisse.

**Anubhav Aggarwal:** Just continuing with the previous question, so next year we expect CAPEX over Rs. 250 to Rs. 260 crore, so what will be your expectation of the debt reduction of the Company from that point?

**Suneeta Reddy:** Our plans currently were at Rs. 3,038 crore, so we believe that we will get another Rs. 600 crore from both the pharmacy, creation at the frontend of the pharmacy and by exiting the insurance business, so we should get about Rs. 600 crore, which will take us to a net debt of Rs. 2,400 to Rs. 2,500 crore.

**Krishnan A.:** From the next year if you look at the free cash flow, of course we could, depending on if there is any bolt-on acquisition, if there is not any bolt-on acquisition, basis the free cash flow of almost 500 plus crore is easily possible even after dividend and working capital increase.

**Anubhav Aggarwal:** Then second question was on AHLL, I just wanted to get the understanding on IFC stake. Now, your annual report says that they have a put option after eight years which is basically 2024, so is the value at which they exercise their put option already pre-determined or it will be determined at that time at certain multiple of EBITDA existing at that time?

**Krishnan A.:** Yes, it is, so there is two things, one is they have a fair market value based exit which is what is the exit which you should be looking at, if they do it. The put is just a principal protection, put, which is not very value accretive for them, it is just to protect their principal which means the principal at which they brought in plus I think 2% if I am not wrong is what they can get a put at, that is just a value, it is just a protection of principal.

**Chandra Sekhar:** Yes, 2% Krishnan.

**Anubhav Aggarwal:** Lastly, on the timing on the Proton deal that we were talking about from the last two calls, just trying to understand what has delayed it so far?

**Krishnan A.:** So there are two points, as I said we are working on the deal, the deal structuring is something that is taking some time and the partner has to obviously take a full commitment and we are looking at that at one level, because again there one of the things that we are discussing is the exit which has to be optimal and whoever comes in, we want them to be there for longer period of time, not like a private equity player and we do not want to commit to any specific IRRs etc. as you rightly are seeking also, and these are the two points, the exit and the IRR discussions are taking some time. Independently, the business is also doing well as I said and guided, so I think we will wait and see how it works.

**Moderator:** The next question is from the line of Prashant Nair from CITI Research.

**Prashant Nair:** Just one question on bed capacity, so without any incremental Greenfield project or big CAPEX, how much do you think you can add to your current operating beds by
just with the installed beds that are available, and for such additions how do we think about incremental costs on the P&L?

Suneeta Reddy: So currently, operational beds are 7,450, we have capacity close to 10,000 beds, so there is clearly at least another 1,500 beds that we can add within the system in the next 24 months, incremental costs we just to have buy beds.

Krishnan A.: Yeah, so it will not be significant because most of the MRI, CT scan, OTs everything would have been, the bigger ticket CAPEX would already be there.

Prashant Nair: So this is the potential as to how much you can add, do you have any specific plans on how much you take or to use this capacity?

Krishnan A.: We think it will be around 800 to 1,000 beds, it will still have capacity because the average length of stay, overall as Ms. Suneeta has been telling has been coming down in our system and especially with a lot of daycare work that is continuously happening across most of our Tier-1 hospitals, you know the average length of stay has been coming down and we think it will continue to be that way, even as we continue to increase the revenue intensity and ARPOBs because of the case-mix, we will see that, we will not require as much beds even in our current system. Over the next three or four years, we do not see this to be a limiting factor.

Prashant Nair: Just one more question, this 800 to 1,000 beds which you mentioned, would it be mainly in one or two of the clusters or would it be evenly spread across?

Krishnan A.: More than half of would be new, because in places like Navi Mumbai we will see 100 beds getting added, so half of that would be in the new.

Moderator: The next question is from the line of Kashyap Jhaveri from Emkay Global.

Kashyap Jhaveri: Just one question, our EBITDA has seen significant growth even adjusted for the Ind-AS number and despite that if I look at our net debt over H2 of last year on March ’19 has gone up from roughly about Rs. 3,200 crore to Rs. 3,400 crore, so what would have driven that?

Krishnan A.: So last year to this year, we continue to add on the Proton and as I said we have only Rs. 170 crore of Proton CAPEX at the end of Q1, if I remember that number Rs. 160 or Rs. 170 crore. We have spent another Rs. 60- Rs. 70 crore in this quarter itself, so if you go back to the last year, we will have added project CAPEX of almost Rs. 200 crore even in the last one year including the Proton, so if you go forward, if you look at it, the Proton project CAPEX is not going to be high, so you will see the results in the debt.

Kashyap Jhaveri: That also implies that H2 would see significantly accelerated debt repayment even considering the cash flows coming from the sale of one of the businesses, are you confident of that also happening?

Suneeta Reddy: So in the last quarter, yes…

Krishnan A.: Yes, in H2 anyway as I said there is Proton balance Rs.100 crore of CAPEX which is pending, so I do not see debt increase in any case and debt will reduce as Ms. Suneeta already said.

Kashyap Jhaveri: Besides the money that we get from the sale of the business, this would also imply that from operating cash flows also there will be a slightly higher debt repayment. Is that right?
Krishnan A.: Slightly, yes, you are right, it will not be significant in H2, it will be more after H2.

Kashyap Jhaveri: So in H1 of next year?

Krishnan A.: Correct.

Moderator: The next question is from the line of Nitin Agarwal from IDFC Securities.

Nitin Agarwal: Sir, on the standalone pharmacy business, we have been talking about the omni-channel strategy; A, can you just help us get a little more understanding of exactly what are we proposing to do and by when do we see some of these things falling in place?

Krishnan A.: I think we are working on a business plan, we are thinking through it, we are continuing to work on the private label expansion and on the same stores on our offline. Online, we are going slow; we are understanding the market, we are working on it, there is a consultant who is working with us on the same. The team is trying to see how do they focus on the omni-channel or the online without being value dilutive which is what is very important for us because we do not want to play the game akin to what some of the other peers are doing in the industry. We are cognizant of that, we know how they are driving sales and what are their chronic sales across each of the specialties, we are aware of that but we would take another six months looks like to kind of get to a more clearer answer to you around how do we propose to take this forward.

Nitin Agarwal: Sir, from an expansion perspective in the pharmacy business, are we looking to continue to grow in our stronger pockets, stronger areas of Southern India or are there any specific newer geographies that we are looking to target to grow going forward?

Obul Reddy: We are doing both, apart from Southern India, we are now focusing on Orissa and West Bengal where we have good number of stores added and good results is coming up.

Suneeta Reddy: If you look at the hospital’s presence, you can expect to see that there will be a strong pharmacy presence that will exist along with it, so at least 10 major states.

Krishnan A.: Because the brand leverage is significant, the moment we put in Apollo Hospitals brand for example in Guwahati, for Bhubaneswar, we are seeing that the brand patronization is very high and around that we continue to put add-on to the pharmacy.

Nitin Agarwal: Sir, lastly on that bit, we have seen a very sharp margin expansion over the last three to four quarters in the pharmacy business, now where we are and what is the optimal level of profitability that a mature pharmacy store can do in the current business model?

Krishnan A.: A good question, I think this is directly related to the private-label sales because the private-label sales is definitely a profitable and if you see, we had guided that we would get to a 12% of the topline in five years, we are already at 8%. If we accelerate and continue on the momentum; obviously the margin label from that is much higher compared to some of the branded label.

Obul Reddy: You could see that matured stores as suggested in the presentation is at (+8%), so we should grow further from there based on the PL contribution, we will work on that continuously.
Nitin Agarwal: Sir, on this pledge reduction, can you help us with the timelines, you were talking about pledge getting reduced 20 odd percent by the end of the year, any specific milestones that we can watch out in terms of events?

Suneeta Reddy: Yeah, we are hoping that the insurance remains that liquidity event happens by the end of the year at least by the end of the financial year.

Nitin Agarwal: And just to sort of revisit that, we are looking at a pledge getting reduced to 20% of the promoter shareholding?

Krishnan A.: 20% to 25% of the promoter shareholding.

Moderator: The next question is from the line of Sameer Baisiwala from Morgan Stanley.

Sameer Baisiwala: Question for your Proton projection for fiscal '21, what kind of utilization does that assume?

Krishnan A.: It will still assume only around 40% utilization, if you look at the number of patients, eventually this can treat 1,000 patients in a year in year five, eventually; 400 patients to be treated in year two for the numbers that I said.

Sameer Baisiwala: And these are all three gantries put together?

Krishnan A.: Yes.

Sameer Baisiwala: Roughly this is about Rs. 20 to 25 lakhs per patient sort of billing?

Krishnan A.: Rs. 28 lakhs is what the average.

Suneeta Reddy: For Foreign patients, it’s at $ 65,000 and 30% of our revenues are from foreign patients.

Krishnan A.: Yes, 30% of the revenues are from foreign patients and we think it will continue to be at that level or even higher.

Sameer Baisiwala: Okay. So is it a start-up pricing or this is sort of a mature pricing?

Suneeta Reddy: We think it is a start-up pricing.

Krishnan A.: We will look at it over time, as of now this is the prices at which we are.

Sameer Baisiwala: Second question is on your capital allocation thought process, over next three years when you start generating pretty meaningful free cash flow, how should we think about that?

Suneeta Reddy: I think we should think about it in terms of how we hope to grow Apollo Hospitals, so clearly we do want to have a presence in every Tier-1 cities, so we are looking at something in Bombay, which is an asset light model, however, we will invest in equipment and I think that while it is good to have free cash flows, we really need to capitalize on the opportunity that exist in this country and with the fundamental demand-supply gap being so large and the ability to pay, so there are 140 million people who are entering the new middle-class. We are targeting these people. Also, if you look at insurance, our insurance business has grown to about 30% of total revenues, so clearly, we have enabled access through health insurance...
program and with that we are seeing a large opportunity for growth in India especially in both Tier-1 and Tier-2 cities.

**Krishnan A.:** Especially in the new hospitals, as Ms. Suneeta said that we are seeing very good uplift in patients coming through insurance, you know that is definitely something that is working in our favor because people know the quality of work that they can afford using at Apollo and that is why they come here, so definitely there is a good traction that we are seeing. Again, to be aligned to your thoughts, we are cognizant about the debt EBITDA. We would not see any lumping up of debt coming on account of any of what we do, so we are in the 2.2 to 2.5 debt EBITDA is what we would be solving for even as we grow the EBITDA.

**Sameer Basiwala:** That is great, that means that our net debt target at Rs. 2,400 to Rs. 2,500 crore end of this year is sort of the bottom, after that we would be using this free cash flow as growth capital?

**Sangeeta Reddy:** Yes.

**Sameer Basiwala:** Just final one from my side and that is on the digital strategy, are there any key monitoryes that you can share with us, the active users, the apps, and how is this whole strategy playing out for us?

**Suneeta Reddy:** Right now we are just putting it in place, so we are working with Mckinsey to do so, so it is a little early for me to actually talk about it, however, we are in terms of marketing the existing Apollo facilities, we are seeing the digital channel is playing a very positive role in booking appointments, in referring patients into the system, so more on that in next quarter.

**Sameer Basiwala:** One more from my side, once we are hitting 60% to 70% occupancy across our network, how much headroom do you have to grow a volume specifically?

**Suneeta Reddy:** Lots of headroom, because we believe that ideal ALOS across the world has dropped to 3, we are already doing a lot of 40% of our surgeries at about 2, so clearly there is a lot of headroom available. We need to think of it as 60% capacity utilization, so there is across the group we really had 65-66 capacity utilization, so there is another 20 to 30 available there plus with the ALOS dropping to you know 2.5 to 3, I think you should think of us in terms of having 12,000 beds and I believe that we were at about 8 and we have come down to 3, so I think three years from now with our focus on surgical work and high intensive care work, we should be able to bring that down to 2, so definitely there is a huge headroom for growth.

**Moderator:** The next question is from the line of Damayanti Kerai from HSBC.

**Damayanti Kerai:** My question is regarding the annual tariff hike which we take for the hospitals, so have we taken for this year and if yes how much will be that?

**Krishnan A.:** So this quarter we did not take anything, we have taken in Q1 almost around 3% to 4%, but after that we will do it more in the Q4 or Q1 of next year.

**Damayanti Kerai:** Quantum will be similar around 3% to 4%?

**Krishnan A.:** Correct.

**Damayanti Kerai:** Ma’am just spoke about that we have enough headroom in terms of ALOS reduction but for key hospitals say in Hyderabad and Chennai, do you have sufficient headroom in terms of improving ARPOB consistently from here?
Suneeta Reddy: Yes, I think we do because we are focusing on quaternary care specialty that results in a higher ARPOB. We are not doing too much of the medical admissions, we are doing more of surgical admissions where at 50% of our work is surgical admissions, so definitely that will yield in a higher ARPOB and going forward we are focusing on these, because we also have a focus on centers of excellence, which lead to a higher ARPOB and higher margins.

Damayanti Kerai: That should sustain our 10% to 15% kind of annual increase in the ARPOB side, right?

Suneeta Reddy: Yes, it should.

Damayanti Kerai: Okay and ma’am one question regarding the SAP, standalone pharmacy business. So you mentioned your focus on improving digital strategy and all, but can you just elaborate a bit further like how we are preparing for competition against increasing presence from online pharmacies, how we are placing?

Krishnan A.: We are aware of how they are targeting the market and which are the Tier-1 markets on which they are focusing on and as Ms. Suneeta said targeting us in some way because obviously they are giving discounts, but if you look at the overall market size of the pharmacy business at over Rs. 100,000 crore and then look at where we are and then look at where the online pharmacies are. In terms of overall market size, it is still significantly lower. The way we intend to do it is very different from how they have handled it and I think as I said it will be nice if you can wait for six months for us to give you a proper rollout of the same because you should remember that we are healthcare players, we are not just a pharmacy operator, so what we give to the consumer will be significantly different from what a pharmacy player can offer, which means it would be something which will combine health and pharmacy.

Moderator: The next question is from the line of Pritesh Chheda from Lucky Investment Managers.

Pritesh Chheda: Just a question on the cash flow and the debt reduction side, so when I look at your half yearly cash flows and the construct of it versus the EBITDA that you generated and the type of CAPEX number that we shared, it looks less likely that your operational cash flows can be surplus enough to repay any kind of debt, is that the case and when we said that Rs. 600 crore of debt reduction is going to come from those two transactions, it also clearly means that the bulk of the debt reduction is not from operational cash flows, but largely from those two events that we have lined up, so if you could shed some light there in terms of cash flows and debt reduction?

Krishnan A.: So you are right, that is why if you look at it there was another question which asked us as to how much will it come down from the next half and I said it will be marginal reduction from these cash flows coming out of free cash flows in the next half and we also said that significantly it will come from H1 of next year, you are right that is why we said out of the Rs. 3,038 crore almost around Rs. 600 crore comes because of this. The incremental cash flows will have to be used towards Proton balance CAPEX of Rs. 100 crore as I said, so that is something that is being borne in mind. Even you should remember that this quarter, we paid Rs. 100 crore of dividend and that was part of Q2, which is where if you look at the cash flows, there will be some lumpiness in the overall cash flows in some quarters, especially in Q2 that was one of the reason that you saw that increase, and another thing since you are asking, I should tell you that today as we speak, we have still not migrated to the new tax regime of 25%, it has not yet come as any query so far from any of the analyst, but I am sure someone will ask later. We
intend to get into that 25% regime in the year after next. This year we continue to be on MAT, because we have MAT of past which is almost around Rs. 400 crore. The benefit of that will come in this year and next year. By end of next year, we will exhaust our MAT and move into the new tax regime in the year after next. What that does this year is we have a TDS (Tax Deducted at Source), because of our credit sales where they deduct almost around 10% and there is an excess tax which is getting deducted because our effective tax rate of MAT is only 18% whereas the TDS is much higher than that, overall that is getting held and we would get a tax refund by the end of the year of Rs. 40-45-50 crore that also gets factored into the cash flows because it comes only later. So you will see the cash flow getting unlocked significantly from H1 of next year.

Pritesh Chheda: I could not understand why are we referring to Rs. 3,050 crore debt when in the presentation it is written as Rs. 3,400, so is there any difference in the numbers?

Krishnan A.: One is the standalone and the other is the consolidated, So the Delta will be the same Rs. 600 crore, whichever way you look at it because the consolidated debt includes Ahmedabad and Apollo Health and Lifestyle and couple of other subsidiaries.

Pritesh Chheda: Lastly on the communication part where we said that we will again restart using the cash flow for growth, beginning FY ‘21, has the cash flow that you will have surplus available for growth, it would be fairly less, does it mean that you will again get into re-leveraging more or on capital need in the form of equity that is how one should look at?

Krishnan A.: No, we said no because we said that we would solve for a 2 to 2.5 debt EBITDA and if you do the cash flows and the EBITDA increase in the next two years, you would see that the cash flows would be able to support growth as well in two years.

Pritesh Chheda: Lastly, so we have looked at reducing the pledge which is a very good activity. There are two other areas, any thought on the related party transaction and what are the corporate guarantees that we have given out of Apollo?

Suneeta Reddy: So no corporate guarantee through Apollo, any cost on the related party transaction per se has to say that this was certified, PwC did an audit, they have certified everything is an arms lengths transaction and that is available in our annual report. So if you look at it I think you will be able to see the exact picture of all the related party transaction. If you want me to get into details, you please refer to annual report.

Krishnan A.: And the second thing the analysts who cover us know us, they know that for example even in Key Med, it is a different business altogether, it is a B2B business and it is distribution and logistics and B2B and even Mitsui is an investor there at almost some 20% and you should be rest assured that someone like Mitsui would not invest in a business like that when things are not at arm’s length.

Pritesh Chedda: I was just looking at requesting it can be resolved, I am not doubting the transaction, I am just saying is there any other way where we can rectify?

Sangeeta Reddy: At this point of time I think without the hospital is also suffering because I do not think so.

Moderator: The next question is from the line of Shyam Srinivasan from Goldman Sachs.
Shyam Srinivasan: First one is on Proton, can you just remind us what the guidance for the full year loss is, is it that Rs. 25 crore number that we highlighted earlier in the year, is that the number the same, EBITDA loss?

Krishnan A.: We are still working on the Rs. 25 crore as the number for the year, so which means Q4 should see a significant uplift from Proton.

Shyam Srinivasan: So 7 going to, I am just making up number 6 or 5, something like that to get to...

Krishnan A.: Yes.

Shyam Srinivasan: Second question, the utilization, you said Rs. 15 crore of revenue, what is the utilization rate that is commensurate to that?

Krishnan A.: Currently it is very little because there is only one gantry working now, so what happens is that, it is a stabilization period. It will take some time, as we said like Q4 of this year and Q1 of next year is when you will see all the three gantries working in full capacity and that will be 16 hours operation. So currently we are working with one gantry, eight hours then we will start two gantries with eight hours now in this quarter then the third gantry comes in and it goes to 12 hours and then 16 hours, so it is Q1 of next year when you will see all the gantries at 16 hours.

Shyam Srinivasan: I may have got the number wrong; you said 1,000 patients will ...

Krishnan A.: Eventually, that is, year five.

Shyam Srinivasan: Eventually, yes, year five so when you did the 40% number that you told, that does how many patients, I am just trying to know...?

Krishnan A.: Next year we are hoping that we should still get almost around 350 to 400 patients.

Shyam Srinivasan: And today, how much are we seeing?

Krishnan A.: It may not be relevant because it is also a capacity, because there are people in the waiting list and all as we speak.

Shyam Srinivasan: No problem, I just wanted to get a sense of the ramp, that is where I was coming from?

Krishnan A.: Ramp, it will be better to see by Q4 which is when we will get a much cleaner idea for all of us.

Shyam Srinivasan: My second question is a generic question, just on the pricing environment, you talked about talking 2% to 3% hike, ARPOB seems to be growing higher than that from first quarter, second quarter both, so are you able to take price plus this mix changes, do you think that is something that you can sustain in any of your conversations with Government, Ministry of Health, any of those entities, are you picking up any conversations which seems to suggest that they are looking at price action, so any of those from a general market color perspective would be helpful, across the value-chain?

Suneeta Reddy: I think the Government is looking at, they can rollout Ayushman Bharat, and look for the private sector, that is their focus. From all the meetings that we have had in Delhi, it has been mostly about that and you would have also read in papers that
even their conversation with the US has been on restricting this margin capping especially on imported devices.

Shyam Srinivasan: You do not think there is more things coming like what happened with stents and stuff, other than the trade margin caps..?

Suneeta Reddy: No I do not think what happened to stents and knees, is coming in again, let me be upfront about that. In terms of us getting reasonable margins, they know that we cannot operate without that and they also know that, they do want us to work with them on Ayushman Bharat, so that is their first priority.

Shyam Srinivasan: What is the plan for that, from an Ayushman Bharat..?

Suneeta Reddy: Our plan for that is if you look, what has happened is that they have revised the rates of 256 procedures out of which some are really to good work with, we are having a dialogue with them to allow the private sector to do the tertiary care work where I think the pricing is quite beneficial, on a marginal costing basis it should work and we are only doing it in our Tier-3 hospitals and some of our Tier-2, so let me say 5% bed allocation for these surgeries, but this has not impacted our P&L significantly but going forward we do hope to work with the Government on doing more of the tertiary care work.

Moderator: The next question is from the line of Sudhir R. from AV Capital.

Sudhir R.: My question has been responded, this was with respect to tax rate, why it is still at 35% and not gone down?

Krishnan A.: Which is what I said, I do not know whether you joined now, but we have not taken the benefit of the new regime because we have this past (inaudible) is that we had claimed deduction on, the 100%-150% depreciation. We have a MAT of almost around Rs. 400 crore in our balance sheet and that Rs. 400 crore which means that effectively, if you look at our effective tax rate that we will be paying this year it will be equal to MAT, this is from a cash flow perspective of 18% as compared to the 25% that the Government has come with up without any MAT. So for the next two years, we will be having a cash flow of 18% whereas the reported number because of deferred tax etc., will continue to show the same 33%-34%, but in the year after next which is FY’22, we will get into the 25%.

Moderator: Ladies and Gentlemen, that was the last question. I now hand the conference over to the management for closing comments.

Suneeta Reddy: Ladies and Gentlemen, thank you very much for joining this call. Thank you for your patience, I hope that we have answered all your queries, but more important I want to state that we are committed to this journey of providing world class healthcare and in the process of providing great clinical outcome, investing in technology, we believe that it will benefit all our stake holders and enhance shareholder value. Thank you very much.

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