



## Apollo Hospitals

### Q3 FY14 Earnings Conference Call Transcript February 11, 2014

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- Moderator** Ladies and Gentlemen, Good Day and Welcome to the Apollo Hospitals Q3 FY-'14 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode. There will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference, please signal an operator by pressing '\*' then '0' on your touchtone telephone. Please note that this conference is being recorded. I now hand the conference over to Mr. Mayank Vaswani of CDR India.
- Mayank Vaswani** Good afternoon and thank you for joining us on this call to discuss the financial results of Apollo Hospitals for the quarter and 9-months-ended December 31<sup>st</sup> 2013. We have with us the senior management team comprising of Ms. Suneeta Reddy – Joint Managing Director, Mr. S.K. Venkataraman – Chief Strategy Officer; and Mr. Krishnan Akhileswaran – Chief Financial Officer.
- 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 our "Investor Presentation." As always we shall start with Ms. Suneeta Reddy who will discuss the operating highlights for the quarter, Mr. Krishnan will then discuss the financial highlights and expansion plans, and Mr. Venkataraman will cover the Retail Pharmacy and Health Insurance businesses. Documents relating to our financial performance have been e-mailed to all of you earlier and have also been posted on our corporate website. I now invite Ms. Suneeta Reddy to touch upon the key highlights of our performance.
- Suneeta Reddy** Good afternoon everyone and thank you for taking time out for our call. We are pleased to share with you the results of Q3 FY-'14. Despite a complex economic environment and a slowdown in corporate healthcare spend I am most happy that against this background our performance has been quite satisfactory. We have analyzed how competition is performing and Apollo continues to maintain market share. This in spite of some of the consumers choosing to delay elective surgeries. However, I would like to add that from a profit perspective, we do not expect that these will impact our profitability.
- You would have noticed that we have commissioned our 200-Bed hospital in Trichy this quarter which is part of our planned expansion with nearly 2,500 beds in FY-'17. This will continue to be followed by a launch of hospitals in Nellore and Nasik, both of which we hope should become operational by Q1 FY15.
- In addition to these three Reach Hospitals, our expansion plan and augmenting our presence in existing urban clusters at Chennai and Bengaluru over the next couple of quarters is well on track with 200-bedded Malleswaram facility in Bengaluru as well as 170-Bed OMR facility in Chennai should be ready by Q1 FY15 as well. As we build these new Hospitals, our focus is currently on aggressively strengthening our medical team in our new start-up while adding new specialties too. We are also implementing programs to build and enhance our capabilities both clinical and otherwise. Initiatives such as the focus on centers of excellence continue to contribute to improvement in our case mix and revenue realization.

Hospitals across the networks have witnessed a rise in the incidence of high acuity cases across key specialties such as Cardiology, Oncology, Neurology and Transplantation. If you look at the ARPOB of our Chennai main hospital which is currently at around Rs.40,000 it is proof that our case mix has become richer. We have also aggressively leveraged technology which has enabled us to sustain excellence in clinical outcomes, while also delivering positive results towards . our efforts to reduce length of stays across network hospitals. We are heartened by the balance growth across the business which has been driven by incremental contribution from hospitals located in major urban clusters as well as Tier-2 locations, apart, of course, from South which continues to witness expansion in margins. Our Retail Health presence through clinics and cradles have also made further progress this quarter.

Now, coming to some of the specifics of our financial performance: Standalone revenues have grown by 16% from Rs.856 crore in Q3 last year to Rs.993 crore in Q3 this year. This includes 10% year-on-year growth in revenues from existing hospitals and a strong 20% year-on-year growth in revenues from Standalone Pharmacies. If you were to deconstruct those revenues, 37% of our revenues is from Pharmacies. Standalone EBITDA has grown by 8% from Rs.146 crore in Q3 last year to Rs.158 crore in Q3 this year. On a reported basis the EBITDA margin has dipped to 15.9%. However, EBITDA margins in the existing Healthcare Services have remained resilient at 24.3% in Q3 while EBITDA in the Standalone Pharmacy has expanded by over 70 basis points to 3.4% in Q3. If we adjust for the impact of operating losses from new hospital facilities, EBITDA has remained healthy at Rs.163 crore at a margin of 16.7%. Standalone PAT was higher by 3% at Rs.83 crore.

New facilities which are in the initial stage of operations, including the recently commissioned Trichy Hospital, had operating losses at Rs.5.4 crore this quarter. As we have shared earlier, we stay committed to try and achieve breakeven profitability levels at all these facilities over the next few months. The hospital in Jayanagar at Bengaluru has already achieved EBITDA breakeven, and we are now expecting the hospital in Vanagaram, Chennai to break even during Q4. Trichy was launched in October 2013 while it will take some more time to reach EBITDA break even.

Growth in Healthcare Services has been driven by a balanced contribution from all facilities. Revenue growth from mature hospital clusters in Chennai and Hyderabad was once again healthy at 12% and 11% for 9-months. The quarterly growth in these mature facilities was good especially viewed against the backdrop of festival holidays in the quarter as also a planned shutdown of operating theatres for maintenance. Hyderabad specifically has seen good traction in our "Physician Connect Program" which has led to increased volumes as well as enrichment in case mix. As Krishnan takes you through the operating metrics, you will see that the Hyderabad facility has reported increased occupancy levels leading to an improved EBITDA. Hospitals outside the major clusters in Tier-2 in Bhubaneswar, Mysore and Madurai have also reported healthy growth rates. Bhubaneswar, in particular, with an 84% occupancy, has performed ahead of our plan averaged with over 20% EBITDA for the 9-month period. We are currently working on a plan to further increase the beds in this center, and I believe this is testimony to our calibrated and well thought out location strategy which differentiates from the others. Hospitals in Mysore and Madurai also reported double-digit revenue growth leading to improved EBITDA margins while the hospitals in locations like Karur and Karaikudi have reported positive EBITDA in the first 9-months of this year.

The standalone pharmacy business continues to grow with the momentum of 23% in revenues and 57% growth in EBITDA in Q3 FY14. As guided last quarter, the DPCO pricing policy did impact top line by about 180 basis points and about 30 basis points at the profit level. However, despite this EBITDA margins improve to 3.4% of Q3 driven largely by the impact of an increasing proportion of sales from private labels as well as double digit same-store growth in most of our mature stores. We had mentioned last quarter that store rationalization is largely complete and with discontinuation of unviable stores in the network has also contributed to improving the trajectory of our EBITDA margins. Our store expansion plan to have another 150 stores every year is on track, and we should continue to witness improvement in EBITDA margin as well as some

operating leverage as well as further increase in the private label sales across the network, which has currently moved from 5% to 6%.

On a consolidated basis, revenues grew 16% to a Rs.1,129 crore in Q3. In addition to strong revenue growth contributed by Retail Pharmacies and Healthcare Services in the standalone entity as well as in subsidiary JV hospitals in Bengaluru, Calcutta, Ahmedabad and Delhi also reported year-on-year growth rate. All these facilities contributed to EBITDA with Ahmedabad and Bengaluru registering the sharpest improvement in EBITDA performance. While the standalone EBITDA margin was impacted by newly added hospitals, the consolidated operations, the operating loss of Rs.4 crore from Apollo Health and Lifestyle – our Retail Healthcare subsidiary primarily from the addition of new clinics and cradles which was in line with our forecast has also been absorbed. Consolidated EBITDA grew 9.2% in Q3 to Rs.172 crore. Going forward I believe that we will focus on a new rollout policy to ensure higher utilization as we start. For this to happen all 74 licenses that we need to operate for a hospital has to be in place. We will also see that a vigorous cost control initiative will be implemented across the group.

Before I close, I would like to share that three facilities in the group were included in the list of Top 15 Multi-specialty Hospitals in India in the 'Best Hospital in India Survey 2013' conducted by The Week-Nielsen. Hospitals in Chennai, Delhi have featured in the list of top 10 hospitals for several years, and have also found a mention in the best hospitals with the specialty of Cardiology and Oncology.

Our Chairman Dr. Prathap C. Reddy was awarded the Lifetime Achievement Award by the Asian Business Leadership Forum in 2013 in Dubai. He was also conferred the Lifetime Achievement Award by CNBC TV18.

I am also happy to inform that Penguin has released his biography titled 'Healer' by historian Pranay Gupte. Of course, while we are happy with all these awards we equally understand with each award comes the additional responsibility to serve the patient even better than the past, and this is the one thing that keeps us engaged 24X7, 365 days of the year. Now, let me hand over to Krishnan – our CFO for details of our financial performance.

#### **A. Krishnan**

Thank you Ms. Suneeta. Good afternoon and thank you for joining our call. I trust all of you have received our 'Earnings Presentation' which has been circulated earlier, and is also available on our website. On a Standalone Basis revenues were higher by 16% at Rs.993 crore compared to Rs.856 crore in Q3 last year. Given the challenging economic environment, we are pleased to report healthy double-digit revenue growth while the growth of the newer facilities could have been sharper had it not been for some delays in permissions and empanelment by insurance companies. We believe that our efforts to enhance medical team and augment the specialty mix are already starting to pay dividends. These facilities will catch up over the next few quarters, and on an overall basis our plans are looking fairly intact. EBITDA increased by 8% from Rs.146 crore in Q3 FY13 to Rs.158 crore in Q3 this year. The EBITDA margin has declined to 15.9% in Q3.

For a deeper insight into the margin performance by segments and to assess the impact of new facilities please refer to Slide #8 of the Investor Presentation. On a year-on-year basis EBITDA margins in the existing Healthcare Services segment was broadly steady at 24.3% despite cost pressures from wage increases, rupee depreciation as well as increased marketing costs. EBITDA margin of the Retail Pharmacy business has improved by 70 basis points to 3.4%. The main impact on standalone EBITDA has come from operating losses of Rs.5.4 crore in the new hospitals. This includes our facilities in Vanagaram in Chennai, Jayanagar in Bengaluru which were launched in Q4 last year and Trichy which was launched in October 2013 this quarter.

As shared by Ms. Suneeta, the hospital in Jayanagar, Bengaluru has already reported EBITDA breakeven in December, and we expect the Vanagaram facility in Chennai to report breakeven some time in Q4. This means that we are on track to achieve EBITDA

breakeven for these hospitals within 12-months of their launch. The real highlight this quarter has been higher volumes and improved profitability of several standalone and subsidiary / JV hospitals within the network, thereby validating our strategy of focusing on centers of excellence, which has resulted in enrichment of the case mix as well as leveraging medical technologies to reduce average length of stay.

Coming to Slide #9, Healthcare Services ROCE is at 15.3% for the first half on an enhanced capital employed which includes Jayanagar, Vanagaram and Trichy capital employed of over Rs.330 crore. These facilities are yet to contribute at the EBIT level, and hence are currently subduing our overall ROCE. Excluding the new hospitals the return on capital employed of existing Healthcare Services is at 18.5% in 9-months FY14 as compared to 18.2% in 9-months FY13. Consolidated revenue growth has been equally healthy growing 16% from Rs.973 crore in Q3 to Rs.1,129 crore in Q3 this year. EBITDA has grown 9% from Rs.158 crore to Rs.172 crore while the EBITDA margin has softened to 15.3% by around 95 basis points, this is due to the initial operating losses of Rs.5.4 crore in the Clinic subsidiary as said by Ms. Suneeta. Consolidated PAT has grown 4% and not kept in pace with growth in revenues and EBITDA due to several factors; firstly, the contribution from other income has reduced, as surplus funds which were earlier parked in mutual funds have now been deployed into new projects. Further, finance cost as expected have been driven up by funds borrowed for expansion CAPEX and depreciation is higher on account of beds and equipment added to existing hospitals as well as new facilities over the last 1-year. On a consolidated basis we have also invested in new Lifestyle Birthing Centers and Primary Clinics, all of which are yet to contribute to organizational profitability. The only tailwind to PAT came from reduced effective tax rate of 21% due to the benefits of 150% depreciation on new hospitals under Section 35AD of Income Tax Act.

I will now walk you through Slide #14 which contains details of key operating metrics in the Hospitals' business. Operational beds as of December 31<sup>st</sup> 2013 were at 5,732. The net increase of 400 beds over the same period last year has largely come about through the launch of new hospitals in Chennai, Bengaluru and Trichy. There have also been additions at our standalone hospitals in Madurai, Mysore, Karimnagar and Karur as well as Delhi and Ahmedabad. Overall Inpatient revenues grew by 6% and Outpatient volumes by 7%. Total occupancy was 72% in 9M FY14 at 4,142 beds compared to 75% in 9MFY13 at 3,989 beds. The reduced occupancy can be attributed to the increase in capacity by 400 beds.

What needs to be highlighted here is that despite growth in Inpatient volumes and revenues there has been a dip in average length of stay indicating that the group is successful leveraging use of medical technologies and embracing newer medical techniques and procedures to reduce number of days stay per patient. The sharp rise in Outpatient volume growth with an accelerated increase in Outpatient revenues is a result of the focus on Daycare Surgeries and improved Outpatient facilities. Volume growth has picked up in the key clusters – Hyderabad specifically has reported increased occupancy rate for the second consecutive quarter. Growth in Inpatient revenues has been more than twice the growth in Inpatient volumes, and this has been positively influenced by an improved case mix.

Slide #18 has our expansion plans for the next four financial years and related CAPEX. Of the total planned expansion of 2,310 beds up to FY17 about 370 beds are scheduled to be rolled out before the end of this fiscal. Apart from the 200 beds Reach Hospital in Trichy launched in Q3, 325 beds will be added at Reach Hospitals in Nasik and Nellore while 45 beds will be added at the OMR facility in Chennai by end of this fiscal. However, these will be operational more around Q1 next year. The remaining 1,940 beds will be rolled out in phases till FY17. As mentioned earlier, our funding for these expansion plans will be through a combination of debt and internal accruals in a phased manner. That is it from me. I will now hand over to Mr. Venkataraman who will walk you through developments on Retail Pharmacies and Apollo Munich Health Insurance.

**S. Venkataraman**

Good afternoon, everyone. Traction in the Standalone Pharmacy business remains strong as revenues grew 23% from Rs.291 crore in Q3 last year to Rs.357 crore in Q3 this year. Growth in same-store sales was healthy while the expanded network of course

although helped drive incremental revenue. As mentioned earlier by Ms. Suneeta the DPCO pricing policy impacted top line growth by about 180 basis points.

The EBITDA margins improved by around 70 basis points from 2.7% in Q3 last year to 3.4% in Q3 of the current fiscal. While the DPCO policy affected EBITDA margins by around 30 basis points this was mitigated by the higher proportion of sales from private label products in the revenue mix. Compared to 5% in the same quarter last year private label represented 6% of total revenue this quarter. The closure of unviable Stores over the last few quarters has also had a positive impact on the EBITDA margins. Last quarter, we mentioned that the review of our loss-making units was largely complete and that there will be a reduction in the number of shut downs going forward. We added 35 stores and shut 9 stores resulting in a net addition of 26 stores in Q3 FY14. After this our pan India network of Pharmacies is 1,586 stores as of December 31<sup>st</sup> 2013. We expect to expand operating margins further through operating leverage as well as turning newer stores into profitable ones. Our focus is to drive up the share of private label sale while profitably expanding the store network.

Coming to Health Insurance, Apollo Munich Health Insurance reported an increase of 4% in gross written premiums at Rs. 373 crore for 9M FY14. Earned premium increased by 24% during the 9M to Rs.396 crore and increased in the claims incurred ratio and investments towards network expansion and the reason for an EBITDA loss of Rs.19 crore in the 9M FY14 compared to a marginally positive EBITDA in the same period last year. Apollo Munich is now enhancing its focus on retail customers by introducing unique and innovative plans as well as gradually expanding its network of distributors and agents. We are confident that this business will begin contributing more to profitability as we attain greater skills. That is it from me. We can now take your questions.

- Moderator** Ladies and Gentlemen, we will now begin the question-and-answer session. Our first question is from Ruchi Vora of UBS.
- Ruchi Vora** My first question is on your expansion plans especially focusing on FY15. If you could just touch upon the expansions and what particular quarters do we expect them to be commissioned that will be very helpful? And secondly how do we see new hospital startup cost spanning out for the next year? We do appreciate that it will take some time for the EBITDA to breakeven but just wanted some sense on that.
- A. Krishnan** So the expansion plans as you will notice there have been a couple of hospitals especially in the Chennai, we plan to open the hospital in OMR which is South Chennai by this quarter, but that has got pushed out a bit because of licenses and approval delays which is outside our control. So as things stand by Q1 we should be having Nellore, Nasik fully operational. By end of Q1 we should be having the OMR facility which is the Lifeline facility of 170 beds begin operations by end of Q1 as well. And after that you will also see the OMR Karapakkam which is the woman and child also coming up by Q1 again. So all of these are going to be facilities which will start by Q1. As things stand the Trichy Hospital as well as Vanagaram and Bengaluru we are expecting should become EBITDA positive by end of Q1; Vanagaram by Q1 it should get EBITDA-positive, it should get followed by Trichy, so those EBITDA will be positive. We will not have a drain because of those EBITDAs. So if you look at the full year and look at the EBITDA losses on account of new hospitals its almost around Rs.20 crore this fiscal. If you go to the next fiscal we would see similar numbers coming from some of our new hospitals which will get pulled out but these will then start generating to EBITDA.
- Ruchi Vora** Did I hear this correctly that the EBITDA impact for FY14 should be about Rs.20 crore and we should expect an equivalent impact as new capacities scale up through FY15?
- S.Venkataraman** Around that number of Rs.20-25 crore for the next fiscal.
- Ruchi Vora** And my second question is on your cluster of subsidiary and JV as the way I see it contributing to your revenue, it is a meaningful portion of your top line. Just wanted some more color and outlook on that particular segment in terms of what is the expectation on

ARPOB growth and volumes, and how do we expect that particular part scaling up in terms of occupancy also?

**A. Krishnan**

The JVs have done pretty well. The significant JVs that we consolidate on our top line is Kolkata, Ahmedabad and Bengaluru; Bengaluru, of course, though it is a joint venture, 85% of that is owned by us, so Bengaluru as we said has done very well, of course, the new hospitals in Bengaluru are coming into standalone which is the AHEL which is not going to this JVs and subsidiaries, like Jayanagar is into the standalone as well as Malleswaram in Bengaluru is going to be coming into the standalone financials but the existing JVs are doing well and we expect them to do even better as we get into next quarter especially Kolkata we are seeing good traction in the Oncology side of business, we are also seeing good traction in volumes in Gastro, we are again trying to focus on the CoE in places like Ahmedabad. So we would expect that the JVs and subsidiaries should help us on the Hospitals side. On the other side you have Apollo Lifestyle where we are now still investing in newer clinics, etc., as well as cradles, we would see traction in those EBITDAs and revenues in the next fiscal.

**Moderator**

Our next question is from Balaji Prasad of Barclays.

**Balaji Prasad**

Firstly, on the Hospital's business, if I can take a step back and look at the last 15-20 quarters, last 3-4 quarters seems to be inching around the mid-teens revenue growth unlike the 20% growth you have experienced and that was for a consistent time now long time. Despite new beds being launched so what is affecting the business – is this a structural shift, a lower trajectory or may be just 3 comparatively weaker quarters lining up?

**Suneeta Reddy**

So I think one part of it is definitely the fact that on a larger base if you take 15% it is still healthy, in some we had reached 80% occupancy levels which led to the creation of new facilities which we have not been able to open up all the facilities. So the ramp up is taking time before we get, I think post 2015 when we have added 3,000 beds to the base you will see again a growth that you saw earlier, till then I believe there was certain capacity utilization in the hospitals that were really generating higher ARPOB.

**Balaji Prasad**

So you would be saying that we could probably see a +20% trajectory beyond fiscal '16 onwards?

**Suneeta Reddy**

Yes.

**Balaji Prasad**

Just on that question, are we currently satisfied with the kind of ramp up that you have seen in your hospitals in the 400 beds that have been launched?

**Suneeta Reddy**

Am I satisfied? No, we are never satisfied in this business but there are lessons that we have learned that we can really shorten the ramp up period from our experience in the past, and the thing is that we continue to remain extremely cautious on not opening up facilities till all the licenses are in place so that we have no issues or problems once the facilities are open which is why it has been a little slow.

**A. Krishnan**

The other conscious strategy of that was to ensure that we operationalize some of these beds slowly so that the cost that we incur are not very high on those, and that is why if you look at the EBITDA and the operating losses on the new facilities those are contained which is helping us on our overall cash flow.

**Balaji Prasad**

Just on the EBITDA part coming to it, particularly happy to see that you have achieved break even in Jayanagar in just 12 months. I remember in my earlier discussions with you a few years ago when the timeframe was ranging from 30-36 months. So how are you achieving a faster EBITDA break even? I think you just now answered one part of the question saying that you are releasing the beds slowly.

**Suneeta Reddy**

I think we were able to do it because we did have surgical teams that we had cultivated. Because we were already in Bangalore in Bannerghatta we were able to move out and that place was getting a bit crowded. So in a new location where we had access to new markets we were able to move good surgical team there and therefore ramp it up much faster.

**Balaji Prasad**

On the Pharmacies part, following the completion of the store rationalization, would it be fair to say that EBITDA expansion trajectory could be lower?

**Obul Reddy**

We are adding the stores, still continuing to add the EBITDA and we will continue to do so.

**Suneeta Reddy**

I think you have seen this quarter's performance, as we continue to grow the private label, where our margins are higher 'B Positive' and 'Doctor Choice' being the brands, I think that they will continue to contribute to a positive EBITDA margin.

**Obul Reddy**

And we will be driving the margins further through the private label expansion.

**Balaji Prasad**

So currently it is around 10-12% of your private labels Pharmacy revenues?

**Suneeta Reddy**

Private label is 6% of the revenue, but easily we can push it to a higher number.

**Balaji Prasad:**

Update on the Byculla project, there was some discussions on the charitable status of the existing hospital, where are we on that?

**Suneeta Reddy**

We have clearances, but I do not think all the licenses are in place which is why we have not clearly started working on that project. But we have an agreement with the trustees, the trustees I think for their own sake are seeing that we get started on this project, but we will have a much clearer picture next quarter which we will report to you on Byculla.

**Moderator**

Next question is from Neha Manpuria of JP Morgan.

**Neha Manpuria**

Just to go back on the expansion, I notice that there was a cost escalation in the Navi Mumbai project. In one of our hospitals in the Chennai cluster which was moved out of the expansion, was there any change in your expansion plan in the Chennai cluster, and the reason for the cost escalation please?

**A. Krishnan**

In New Bombay one of the things that we had not planned for earlier which we have added now is Oncology which is not part of the initial project but now we have added that and that is one of the reasons that the cost has gone up in New Bombay. Now, when you come to the facility in Chennai, yes, we had a plan to take a facility on lease in Chennai for the outpatient block, and the lease terms unfortunately were not favorable and we had to walk out of the same. And that outpatient facility was related to the expansion plan which is why the 100 beds could not happen.

**Neha Manpuria**

In your opening comments you talked quite a bit about the competitive intensity increasing, corporate spending going down, etc., and plus we have seen our growth rates are not really slow, but from 20% to more in the teens. Overall, how would you see the hospitals' market generally – Is there just a slowdown in expenditure itself which is like a structural change or do you think this is more just probably a two or three year phase which will ramp up over time?

**Suneeta Reddy**

I think you said it yourselves which is the two or three year phase, and we clearly believe it is, which is why we are continuing with our expansion, because we believe that once this phase is over, the demand will rise again. Having said that I have to say that in these cities we are present, our market share remains intact. And the way that we see Apollo story growing is that there is a very strong clinical differentiator between Apollo's value proposition and what the other hospitals offer,

which is why currently our pubs are among the highest in all the cities that we are present.

**Neha Manpuria** On Hyderabad again, very good performance there given the occupancy seems to be going up. Part of it you have been mentioning over the last two quarters has been our doctor initiative. How much more upside do we see there as this initiative gets rolled out, what I am trying to understand is how much longer would it take for the full benefit of this to come through in Hyderabad?

**Suneeta Reddy** I think in the next one year that they will focus clearly on occupancies and on improving the case mix. So you will see occupancy going up and hopefully ARPOB also in line with that. There is a lot of competition in Hyderabad because the number of hospital beds are probably 5 per 1,000. So in terms of ARPOB let us not have very high expectations, but you will see occupancy going up because of the new facilities that they have created, and with the fixed costs already having been absorbed it should flow down to the bottom line.

**Moderator** We will take the next question from Bino Pathiparampil of IIFL.

**Bino Pathiparampil** Just following upon the earlier question I see couple of more changes in the latest hospital expansions plan list, if I see the South Chennai has come down from 200 beds to 125 beds and Vizag has come down from 300 to 250, so what has led to this? Also despite that the CAPEX plans for these hospitals remain the same, so are we also seeing a cost escalation in these projects?

**A. Krishnan** One is the South Chennai project which is a 175-bedded because we are putting it along with the 'Proton Therapy Center' there as you are aware of – that is going to be first in this part of the world. There were some changes in the number of beds because of trying to fit in the proton and that was because of some of those changes there. As we operationalize the project we have plans to see whether we can further increase it by another 10 to 15 beds but today it is at around 175 beds. So there is no cost increase per se in this, it is only because of some changes that had to be done to fit in the proton. On the Vizag project, yes, there was a 300-bed plan that we had, but we are making the project fully ready, but we are not going to go ahead with the full 300-bed plan because we believe that we do not want to do 300-bed, we would start off with 250 beds, and then add Oncology, and then take it forward to the 300 beds. So that is again a plan to ensure that we can quickly make it EBITDA positive and that is in line with that.

**Bino Pathiparampil** Just a clarification, this Vanagaram that you talked about, is it the same as Ayanambakkam?

**A. Krishnan** That is correct, it is called Vanagaram and that is how the local people know it, and that is why we are calling it Vanagaram.

**Bino Pathiparampil** Finally, if I look at overall the pricing trend in this quarter compared to last two-three quarters pricing trend, (pricing I am talking about the Average Revenue Per Occupied Bed), I saw a healthy increase Y-o-Y, whereas this quarter it has been much more muted in select clusters tending down or so, is there a pricing pressure which of late you have seen?

**A. Krishnan** No, there is no pricing pressure that we have seen. Each cluster there is a different reason. For example, in the Chennai cluster that is because of the Vanagaram facility. As Ms. Suneeta said in the main hospital the ARPOB is almost from 40,000 which compared to around 36,000 last fiscal. So clearly we have seen over 10% increase in ARPOB in the Chennai main hospital. Vanagaram has been at ARPOB of around 23,000 which pulls down the overall ARPOB for Chennai cluster, and as Vanagaram occupancy increases you would see that the overall reported cluster ARPOB will not see so much growth and it will be a bit timid. So that is something that you will see in Chennai. Again, in Hyderabad it has been healthy at around 10% whereas in others as well it has been healthy. There has been a one-off impact

because of the DPCO pricing order in hospital-based pharmacies also, which impacted pharmacy pricing by around 2% across which has got absorbed in the ARPOB that you are seeing now. So we do not think it is reflective of times ahead.

- Bino Pathiparampil** In Pharmacies the expansion plan in terms of number of stores, does it continue to be similar with the historic trend?
- Obul Reddy** It will continue to be so, we are adding a similar number to what we have been doing for the last two years.
- Suneeta Reddy** 150 stores for the next year.
- Moderator** Next question is from Chunky Shah of Credit Suisse.
- Chunky Shah** Relating to the Hospitals business, what would be the current utilizations for Jayanagar and Ayanambakkam?
- A. Krishnan** Jayanagar occupancy is around 40% that is where it has become EBITDA breakeven, and in Ayanambakkam it is around 35% now.
- Chunky Shah** When do you expect the next set of beds over there to be launched or to be operationalized?
- A. Krishnan** Jayanagar we have already operationalized the balance beds as well, so we now have 125 beds in Jayanagar, we are hoping that it should improve in occupancy over the next few quarters. Vanagaram will take another quarter before we operationalize another 40-odd beds.
- Chunky Shah** This 40% and 35% is on the existing numbers, right?
- A. Krishnan** This is correct.
- Chunky Shah** On the Pharmacy we are going to add around 150 stores in the next year, we are currently at around 1,586 stores. What I was looking for a bit of a long term guidance, for the next five years can we assume it to be doubled around 3,000 stores or can it be a little lower number than that?
- Suneeta Reddy** I think projecting so far out into the future is not wise for us to give a prediction, that far out is difficult. What we will say is that as long as we continue to find attractive location which is key in businesses we will continue to add Pharmacies. As you know we use only leased premises and we should not get to a point when our own Pharmacies are competing with each other. To tell you that it will double, we cannot confirm this at this point, but to say that we will increase the scope of what the Pharmacy is going to do by introducing new products, I think this is something that we are looking at.
- Chunky Shah** In terms of metro v/s non-metro incrementally, will we see a higher proportion of non-metro pharmacies coming into this or?
- A. Krishnan** We are expanding across the cities equally.
- Suneeta Reddy** I think you will see clusters especially in places where the hospital has a presence. So those 56 locations there will be clusters.
- Chunky Shah** My final question is on the private label. We say that it is currently at 6%. I just wanted to get a sense on the EBITDA margin for this because we are driving our EBITDA margins from private label. So what kind of margins....?
- Obul Reddy** It is about 50-55%.

Next question is from Nitin Agarwal of IDFC Securities.

**Nitin Agarwal**

How should we look at the growth for those mature hospitals – if you take a 2-3 year view, is it reasonable to assume a 10-15% growth or is it to a wider band essentially for growth to come on the mature hospitals as far as revenues are concerned?

**Suneeta Reddy**

It is not unreasonable to expect that, and the way that it will happen is that certain hospitals which are equipped like Chennai, the main one in Grems Road, hospital in Bangalore in Bannerghatta, and Hyderabad, for example, all these because of the case mix, they will show a richer case mix. We can only do 80% without compromising quality of care, but you will see that there will be a richer case mix. ALOS has been going down steadily over a period of time. So, we should benefit from that. One of the main drivers of this is the fact that we are moving a lot of surgeries into robotics into shorter stay procedures which is why ARPOB has moved to 41,000 even though people have become very price sensitive, they are willing to pay. With the increase in technology and case mix I think definitely you will be able to see that up to 15% we can grow the revenue from these facilities.

**Nitin Agarwal**

If I were to look at your revenues, what proportion of our revenues, typically if you were to classify them into buckets, it is pretty much classified in this mature hospital revenues of the hospital revenues that we generate currently?

**A. Krishnan**

I think you will have to get off line on this and talk to Krishnakumar, we can provide you the details.

**Nitin Agarwal**

So we have got plans lined up for FY15 and FY16 and we have got a fairly aggressive expansion coming through there in terms of the commissioning. Two things; one is, is there scope to add or are we looking at possibilities to add some more hospital projects during this time period, how does one look at the period beyond this – are we looking at a period of consolidation after these two years of aggressive commissioning?

**Suneeta Reddy**

Two things will happen; one is we are already looking at consolidating what we have an improving performance metrics. So that is happening simultaneously. Beyond the three years, I think in locations where we think the Apollo brand is common, people have the capacity to pay and where there is not too much competition, we are already looking at some acquisitions.

**A. Krishnan**

As things stand, if things go well, Indore should be an acquisition that we should be doing, which is why if you have seen the commencement date is FY15, which is something that we hope we should be able to fructify over the next three months. We are also looking at a hospital in Northeast which is our stronghold, and we are looking at seeing whether we can do something there.

**Nitin Agarwal**

The Northeast hospital is something that we are running right now?

**A. Krishnan**

That is not something that we are running right now.

**Moderator**

Our question is from Krishna Prasad of Kotak Securities.

**Krishna Prasad**

My first question is relating to... I think in your opening comment Suneeta had alluded to slowdown in consumer spending and sort of delay in elective surgeries and so on. Could you give us an example of how things have changed over the last 6-9 months and what you expect over the next 12 months?

**Suneeta Reddy**

I think if you look at Outpatient growth you would have seen that Outpatient is higher than Inpatient and we track conversions very carefully, and we also have patient counseling. Because 55% of our revenues are cash, they are not insurance, etc. Some of these patients take a decision to postpone the surgeries as it is not absolutely required. These are the elective surgeries.

**Krishna Prasad**

What I am trying to understand is when did you last see this trend happen or does it happen at regular intervals or are you starting to see that happen?

**Suneeta Reddy**

We last saw it in 2008. It moves with the economy.

**Krishna Prasad**

Where do you see that in the next 12 months?

**Suneeta Reddy**

In the next 6-8 months we believe that things will get better, and these people may be did not expect to do the surgery and have not saved money, will probably put it together and come back because it is an elective, but it does not get postponed forever. I strongly believe that people if they have to make a choice and they have a health care expenditure they will make the decision to put their money into healthcare rather than anything else.

**Krishna Prasad:**

My second question is relating to your comments on acquiring some of these facilities. I think you mentioned Indore and one in Northeast. Have you had a rethink on buy v/s build at this point and has the market changed – are you seeing more opportunities to buy, is that what is driving your change in approach, just want to get your thought around that?

**Suneeta Reddy**

I think buy at the right price and buy in a location that we can handle and where people know the brand.

**Krishna Prasad**

Would you think that is may be a more derisking strategy as we get into newer areas, would you look to do that more often now?

**Suneeta Reddy**

We are actively looking at that because one team will definitely look at the 3,000 new beds making them profitable, but there is a group looking at markets where we would like to be and may be get there quickly and it is at the right price.

**Moderator**

Our next question is from Praveen Sahay of B&K Securities.

**Praveen Sahay**

My question is first related to the Pharmacy business. In the stores of FY10 that we had seen an improvement in the margin of 139 basis points, in third quarter '13-14 as compared to '08 of 36 basis points. So I just wanted to know in these two batches what exactly we are doing more in the 10 batches seeing more improvement as compared to matured ones?

**Obul Reddy**

You can see the matured ones at a lesser pace at the expansion level, because they are already at 6% EBITDA level, and since this 2010 batch is currently at 2% the expansion is more there because any revenue addition will result in the EBITDA addition. We are already at 6% kind of EBITDA level for matured pharmacies.

**Praveen Sahay**

So we can say the matured pharmacy can go maximum till 6% of margin or so?

**Obul Reddy**

6+ or over 6 will result out of the private label or margin expansion we have to work on strategies for that.

**Praveen Sahay**

On the Hospitals front I had noticed in the managed hospital number of beds had decreased from 150. I suppose that is Bhillai facility. Would you please give some information like what happened in that JV?

**A. Krishnan**

We have said that certain markets where the licensing conditions are not favorable and it is not something that we would want to renew the license. We have said that we would look at withdrawing these out of our managed hospitals. So this is part of that strategy.

Unless you have a strong partner and you are not able to put in place the controls that you need to do whether it is clinical or has to do with management. It is best to step back.

Would you please give a contribution from across the insurance companies to our hospital revenue?

Insurance contributes to around 15% of our overall business.

Our next question is from Nitin Gosar of Religare Invesco.

Just wanted to understand on this Reach Hospital-related strategy, are we going to see no more Reach related kind of expansion beyond FY14, or is there something which is still left in this part of the strategy?

There is a Reach strategy which is there, but the way we are looking at some of these markets there are opportunities to do Oncology, there are opportunities to do higher beds, etc., which is there, you would see that Reach in certain locations would be higher than Reach per se, but we have a Reach strategy which is in line with what we had earlier planned. So you are looking at Nasik which is going to come in soon, Nellore is coming now in the next quarter. These are part of our strategies to get to the market from where we have patient flow.

Can I take a conclusion that Reach is seeing a backburner because of the other Oncology or Specialty kind of related CAPEX that you want to incur right now?

No, it is not really back burner, it is just that every quarter we go through investment opportunities and are constantly analyzing those that will give us the best in terms of returns. Its just prioritized in that fashion. It is not to say that we are not going to look at Reach, but sometimes by adding facilities to hospital is doing well where the market appreciates us it makes more sense and Reach is a Tier-2 strategy, so we have identified some cities and like we said earlier some we are doing via acquisition.

My second question is pertaining to Retail Pharmacy. Just seeing FY09 batch is right now doing relatively low margins as compared to FY10 batches, is it more to do with...?

Primarily that batch is concentrating some of the metros where we have high rental cost and we are addressing that issue.

Ladies and gentlemen, due to time constraints, we will take a last question from Ravi Dodhia of CRISIL.

I have two questions. One is on the Q-o-Q performance if you look at for the Chennai and JVs business, revenues have kind of declined Q-on-Q in both the segments. So any particular reason for this?

Q-on-Q is not a metric that we want you to look at because this is a business there are cyclical, for example, in this quarter that ended in Q3 we have festival holidays because of Diwali, then there is Christmas, and then we have theatre closures as well which is in line with what we have seen in the past as well. Last year, in Chennai we closed the theatres in Q4, we did not close it in Q3 but this time the theatre closures were also in Q3. So we are not overly concerned about this and it is something that is in line with our expectation.

Earlier discussing about plans for this REIT listing, so any progress or update on that?

**A. Krishnan**

There is no update at this point in time; we are waiting for the SEBI rules to also firm in for us to be able to see how the Indian REIT structure looks over a period of time and we are not in a hurry to do this, so we will keep evaluating and revisiting this to see whether there is an appropriate time when we can look at this actively.

**Ravi Dodhia**

How many beds are operationalized at Trichy facility currently?

**A. Krishnan**

Around 80 beds are operationalized in the Trichy facility.

**Moderator**

Ladies and gentlemen, I would now like to hand the floor back to the management for closing comments.

**Suneeta Reddy**

Ladies and gentlemen thank you for joining us on this call. I have to say at this time that I continue to be optimistic about our performance, because the one thing that leads to this optimism is our belief in the fact that Apollo will be able to deliver strong clinical performance, backed by the fact that the demand for healthcare has not diminished, and I believe that on the basis of these strong fundamentals the company will continue to grow and deliver a much better performance in the coming quarters. Thank you.

**Moderator**

On behalf of Apollo Hospitals that concludes this conference. Thank you for joining us and you may now disconnect your lines.