Zydus Hospitals and Healthcare Research Private Limited

November 30, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	219.13 (Reduced from 280.29)	CARE A+; Stable	Reaffirmed
Long-term/Short-term bank facilities	40.00	CARE A+; Stable/CARE A1+	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

The ratings assigned to the bank facilities of Zydus Hospitals and Healthcare Research Private Limited (Zydus Hospitals) continue to derive strength from the experienced and resourcefulness of its promoter group, i.e., the Zydus group. It also factors in the strong brand equity of Zydus Hospital in the Gujarat market and the healthy operating performance of its flagship multi-speciality and cancer-care hospitals in Ahmedabad.

The ratings further derive strength from the growing scale of operations, aided by geographical diversity, the healthy financial risk profile characterised by low reliance on external debt, apart from interest-free unsecured loans extended by promoters and the positive long-term outlook for the healthcare sector. The ratings also factor in the expected improvement in income and profitability of Zydus Hospitals over the medium term, driven by the scale-up in its multi-speciality hospital in Vadodara, apart from revenue from the existing multi-speciality hospital and cancer-care hospital in Ahmedabad.

The aforementioned strengths are partially off-set by the relatively modest scale of operations of Zydus Hospitals compared to other large-size multi-speciality hospital chains, the high geographical concentration of its operations, and the challenges pertaining to attracting and retaining quality doctors. Furthermore, the long-term rating is also constrained by the low return on capital employed (ROCE), which CARE Ratings Limited (CARE Ratings) expects a gradual improvement in over the next two to three years post the successful ramp-up of the overall occupancy level and the stabilisation of its Vadodara multi-specialty hospital.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Improvement in the occupancy rates across hospitals, leading to healthy growth in the scale of operations.
- Operating profitability (profit before interest, lease rentals, depreciation and taxation [PBILDT]) margin of more than 22% and ROCE of more than 15% on a sustained basis.

Negative factors

- Decline in the PBILDT margin below 12% on a sustained basis.
- Delay in turnaround of the Vadodara multi-speciality hospital, impacting the overall financial profile.
- Any large-sized debt-funded capex plan or acquisition and its funding pattern, adversely impacting the debt coverage indicators.

Analytical approach

Standalone, along with factoring in linkages with the strong prompter group, i.e., the Zydus group. The promoters of the Zydus group, i.e., Pankaj Patel, Chairman of Zydus Lifesciences Limited (ZLL), and his family members own a majority equity stake in Zydus Hospitals. Pankaj Patel is also the Chairman of Zydus Hospitals, and Dr. Sharvil Patel, Managing Director of ZLL and son of Pankaj Patel, is a Director at Zydus Hospitals.

Outlook: Stable

CARE Ratings believes that Zydus Hospitals will continue to benefit from its strong brand equity, high average revenue per occupied bed (ARPOB), and turnaround in operations in its Vadodara multi-speciality hospital, leading to better profitability. Furthermore, the strong financial flexibility being part of the Zydus Cadila group is also expected to support its credit profile in the event of exigencies.

Detailed description of the key rating drivers

Key strengths

Resourceful promoter group, i.e., the Zydus group

Zydus Hospitals is a part of the Ahmedabad-based Zydus group, promoted by Pankaj Patel and his family. Pankaj Patel, Chairman of ZLL, and Sharvil Patel, Managing Director of ZLL and Chairman of Zydus Wellness Limited (ZWL), are the promoter-directors of Zydus Hospitals, thereby demonstrating strong managerial linkages with the Zydus group. The promoter group has significant experience of more than six decades in the pharmaceuticals and healthcare industry. The flagship company of the group, ZLL, is

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

among the top five pharmaceutical companies in India. During FY23 (FY refers to the period from April 1 to March 31), on a consolidated level, ZLL reported a total operating income (TOI) of ₹17,522 crore with a profit-after-tax (PAT) of ₹2,092 crore. ZLL has a comfortable gearing and strong debt coverage indicators.

Strong brand equity in Gujarat; healthy operating performance of Ahmedabad hospital

The Zydus group forayed into the hospital business by incorporating Zydus Hospital in 2008. Zydus Hospital set up its first hospital in Anand, Gujarat, which commenced operations in 2012. It is the first tertiary care multi-specialty hospital in Anand. Later, in 2015, the company set up its second hospital in Ahmedabad, Gujarat, which is currently the flagship hospital of the company. It is one of the largest corporate hospitals in Ahmedabad, marked by an installed capacity of 550 beds, of which 382 beds are currently operational. In 2019, the company acquired Columbia Asia Hospital Private Limited in Ahmedabad and converted it into an exclusive cancer care centre, which has further solidified the company's brand image in the region. The company further expanded its reach by setting up its third multi-speciality hospital in Vadodara, Gujarat, which commenced operations in February 2022.

As on March 31, 2023, Zydus Hospitals has a total operational capacity of 756 beds along with Cath labs across all its hospitals, apart from being equipped with the latest technology. All the units are certified by the National Accreditation Board for Hospitals and Healthcare providers (NABH) while the in-house pathology laboratories are accredited by the National Accreditation Board for Testing and Calibration Laboratories (NABL). Moreover, all the properties of the hospitals are owned by the company itself.

The combined occupancy level of the Zydus hospitals remained at 44% during FY23 (58% in FY22) with the addition of new bed capacity in Vadodara. The overall occupancy level was impacted mainly due to the newly-commenced beds in Vadodara, while the occupancy level at the Ahmedabad hospital and cancer care remained healthy and stable at 56% and 66%, respectively, during FY23. With the ramp-up in the occupancy level at Vadodara, CARE Ratings expects the overall occupancy level to remain in the range of 55-65% in the medium term.

Diversified revenue profile with no major dependency on any single speciality

The Zydus Hospitals earns nearly 93-95% of its revenue from medical services and the remaining 5-7% from pharmacy. Of the total medical services income, the company earned 82% of its revenue from in-patients and 18% from out-patients in FY23.

Zydus Hospitals offers a range of medical and surgical care in a host of almost all major therapeutic segments, with specialists available round-the-clock. The hospitals are equipped with state-of-the-art and high-end medical equipment of the latest available technology. The company's facilities are integrated, with specialisation in various segments including cardiology, neurology, gastroenterology, orthopaedics, critical care, nephrology, and many other specialties, which offer a huge potential due to the shifting demographics of the Indian population. Zydus Hospitals has a revenue mix from diverse specialities. The top four specialities – oncology (18% of the total revenue), Gastrology (16%), general medicine and critical care (14%), and neurology (14%), accounts for 60-62% of the total revenue. CARE Ratings opines that the company's sizeable presence across multiple specialities helps it minimise the concentration risk and the presence across multiple segments expected to continue, thus further minimising the concentration risk.

Zydus Hospitals, on an average, earned 75% of its in-patients' revenue from private patients, 15% from third-party administrators (TPAs), 7-8% from corporates, and 1% from the government over the last three years ended FY23.

Growing scale of operations

The scale of operations of Zydus Hospitals, marked by the TOI, grew by a CAGR of 20% over the last five years ended FY23, including a growth of 13% in FY23 on a y-o-y basis, backed by growth in revenue from the existing hospitals, apart from the revenue from the new hospital in light of the strong brand image. During FY23, the company witnessed 5% improvement in its ARPOB and 19% growth in the number of patients treated during FY23 on a y-o-y basis.

With improvement in the scale of operations, the profitability margin of the company also improved gradually over the last five years ended FY22. However, its PBILDT margin declined by around 600 bps in FY23 and stood at 14.44%, primarily due to gestation losses pertaining to its recently commissioned Vadodara multi-speciality hospital. While its Vadodara hospital is incurring losses, its multi-speciality hospital and cancer care hospital in Ahmedabad continue to operate at a healthy operating profitability of over 20% in FY23 and H1FY24. As articulated by the management, the company expects to achieve monthly break-even at the operating level for its Vadodara multi-speciality hospital by March 2024. With a turnaround in the operations of the Vadodara hospital, CARE Ratings expects the PBILDT margin to be in the range of 16-17% for the period FY24-FY26.

Low reliance on external debt with significant headroom for long-term borrowings

The company has invested over ₹1,150 crore towards setting-up four hospitals, which was primarily funded through interest-free unsecured loans from the promoters. The unsecured loans from the promoters stood at ₹697 crore as on March 31, 2023. The company had availed a term loan of ₹280 crore for the Vadodara capex (including reimbursement of capex). As articulated by

the management, the company does not have any debt-funded capex or acquisition plans in the near to medium term. Furthermore, any future expansion is expected to be funded through unsecured loan from the promoters.
Moreover, with an asset base of over ₹1,150 crore, the external term debt of ₹220 crore as on September 30, 2023, provides significant headroom for long-term borrowings, as majority of the assets are unencumbered. The debt coverage indicators, marked by PBILDT/interest coverage remained comfortable at 5.18x and 6.00x, in FY23 and H1FY24, respectively, and the total debt (TD; excluding interest-free unsecured loans from promoters)/gross cash accruals (GCA) at 3.97x and 2.41x, in FY23 and H1FY24, respectively. Furthermore, CARE Ratings envisages the PBILDT/interest coverage of the company to improve to above 10x over FY24-FY26, with improvement in profitability and reduction in interest cost due to the scheduled repayment of the term debt and the absence of any debt-funded capex plan.

Positive long-term outlook for the healthcare sector in India, albeit increasing competition
The hospital and health services industry is the largest component of the Indian healthcare sector, comprising 70% of the sector. The net sale of the entire industry has grown at a healthy double-digit during the past couple of years. CARE Ratings expects healthcare services in India to grow at a healthy rate on account of the likely rise in per capita income and health insurance markets, and a transition in the disease profile of the country arising from growing lifestyle diseases. In addition to this, the healthcare industry is extending the services of e-consultations and other homecare services, which is also expected to support their revenues. Moreover, the Union Budget 2023-24 allocated ₹86,200 crore to the Ministry of Health and Family Welfare, which should augur well for the growth of the healthcare sector. As per CARE Ratings' estimates, the growth of the hospital and healthcare industry is expected at levels of 10% to 12% for FY24 and FY25, respectively.

Liquidity: Strong
The company is expected to earn a healthy GCA of ₹90-120 crore over FY24-FY25, as against its schedule external debt repayment obligation of ₹80 crore during the same period. Moreover, Zydus Hospitals, being part of the Zydus group, will benefit from the need-based financial support from its promoters. The promoters have been infusing interest-free unsecured loans to fund its capex and working capital requirements. Furthermore, the company operates with a lean working capital cycle; hence, the incremental requirement of working capital remains minimal. Moreover, the company does not have any capex plans in the near to medium term. As articulated by the management, the promoters are expected to infuse interest-free unsecured loans for its routine capex requirements.

Key weaknesses
Geographical concentration; high dependence on its flagship hospital
The company commenced its hospital operations in 2012 with its first unit at Anand, while its major investment happened at Ahmedabad in 2015; thereby, it has a limited track record of operations. Furthermore, Zydus Hospitals faces high geographical concentration risk, as it earned majority of its revenue from the Ahmedabad region. The Ahmedabad multi-specialty and cancer care hospital together contributed nearly 84% of the company's total revenue in FY23, while the entire operating profitability was contributed by these two hospitals. The operating profitability was constrained by losses incurred by the Vadodara hospital in FY23. Furthermore, despite the long operational track record of over 10 years, its Anand multi-speciality hospital continues to report net losses due to its small set-up, leading to relatively higher operating costs.

Gestation losses of Vadodara multi-speciality hospital
The company has set up a new multi-specialty hospital at Vadodara, which commenced operations from February 2022. The Vadodara hospital incurred operating losses in FY23, which remained marginally higher than envisaged due to the slower-than-envisaged ramp-up in occupancy level and delay in TPA tie-up of insurance. Furthermore, the Vadodara hospital continues to incur operating losses in H1FY24, which restricts the overall operating profitability and ROCE. CARE Ratings expected the ROCE to improve gradually over the next two to three years, post the successful ramp-up of the overall occupancy level and the turnaround of the Vadodara multi-specialty hospital.

Low net-worth base
The company has small paid capital of ₹0.01 crore and majority of the capex in the past has been funded through unsecured loans from promoters. The unsecured loans from promoters are repayable on demand. Furthermore, due to past losses, the net worth of the company remained constrained, despite the healthy profitability in FY22 and FY23. The net worth base of the company stood at ₹75 crore, including quasi-equity of ₹100 crore in the form of unsecured loans from promoters as on March 31, 2023. Accordingly, the leverage ratios of the company remained weak due to the high reliance on unsecured loans.

Retention of quality doctors and medical professionals in a competitive and fragmented industry
Undertaking a new project and expanding the existing facilities require trained doctors and medical personnels. Due to the scarcity of trained medical persons, including doctors, owing to the heavy competition in the state of Gujarat, it becomes relatively difficult to attract and retain a skilled pool of medical personnels. Furthermore, the loss of services of any senior medical personnel may seriously impair the company's ability to continue to manage and expand its operations due to the highly skill-driven nature of medical services. However, given the increasing competition and scarcity of quality medical specialists, the ability of the company to retain its current medical fraternity will be a key differentiator.
Zydus Hospitals has a dedicated team of full-time consultant doctors who practice in various therapeutic areas. Zydus Hospitals has a total of 461 doctors, who are full-time consultants. As articulated by the management, the doctors are associated with the hospital for a long tenure due to its well-known brand name.
The healthcare sector is highly fragmented with a few large players in the organised sector and numerous small players in the unorganised sector, leading to a high level of competition in the business. Zydus Hospitals faces competition from a few well-established hospitals, namely, Sterling Addlife India Private Limited, Shalby Limited, Healthcare Global Enterprise Limited, SAL Hospital and Medical Institutes, and K. D. Hospital, among others. Zydus Hospitals also faces competition from hospitals run by NGOs or trusts and the government. Thus, differentiating factors such as the range of services offered, quality of service, pedigree of doctors, success rate in treatment of critical or complex diseases, etc, will be crucial to attract patients and increase occupancy.

Applicable criteria

Policy on default recognition
Financial Ratios – Non financial Sector
Liquidity Analysis of Non-financial sector entities
Factoring Linkages Parent Sub JV Group
Rating Outlook and Credit Watch
Short Term Instruments
Rating methodology - Hospital
Service Sector Companies
Policy on Withdrawal of Ratings

About the company and industry

Incorporated in 2008, Zydus Hospitals is promoted by the promoters of the Zydus group. Zydus Hospitals currently operates a chain of multi-specialty hospitals in three cities of Gujarat, namely, Ahmedabad, Vadodara, and Anand, along with a cancer centre in Ahmedabad. As on March 31, 2023, Zydus hospitals has 756 operational beds with the potential to reach up to 1,000 beds in the next two to three years.

Industry classification

Macro-economic Indicator	Sector	Industry	Basic Industry
Healthcare	Healthcare	Healthcare services	Hospital

Brief Financials (₹ crore)	FY22 (A)	FY23 (A)	H1FY24 (UA)
Total operating income	511	579	319
PBILDT	104	84	55
PAT	69	20	21
Overall gearing (times)	16.21	11.49	NM
Interest coverage (times)	48.54	5.18	6.00

A: Audited; UA: Unaudited; NM: Not meaningful. Note: The above results are the latest financial results available.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for the last three years: Please refer Annexure-2

Covenants of the rated instruments/facilities: Detailed explanation of the covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of the various instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT-Term loan	-	-	-	30-06-2026	219.13	CARE A+; Stable
Non-fund-based - LT/ ST-Letter of credit	-	-	-	-	40.00	CARE A+; Stable/ CARE A1+

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/ Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021
1	Fund-based - LT-Term loan	LT	219.13	CARE A+; Stable	-	1)CARE A+; Stable (15-Nov-22)	-	-
2	Non-fund-based - LT/ ST-Letter of credit	LT/ST*	40.00	CARE A+; Stable / CARE A1+	-	1)CARE A+; Stable / CARE A1+ (15-Nov-22)	-	-

*Long term/Short term.

Annexure-3: Detailed explanation of the covenants of the rated instruments/facilities

Bank Facilities	Detail explanations
Financial and non-financial covenants	▪ DSCR>1.25x from FY23 onwards ▪ Promoter Loan to remain subordinate to bank facilities subject to company maintaining DSCR above 1.25 times. The company cannot repay the promoter loans during the currency of bank facilities except for those as reimbursement of capex as agreed by the bank. ▪ The bank considered event of defaults on occurrence of i) credit rating falls below 'BBB+' ii) change in ownership and management control of borrower below 51%. If an event of default occurred, lenders may accelerate the maturity of facilities or declare the outstanding amount of the facilities due and payable.

Annexure-4: Complexity level of the various instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Fund-based - LT-Term loan	Simple
2	Non-fund-based - LT/ ST-Letter of credit	Simple

Annexure-5: Lender details

To view the lender wise details of bank facilities please click here

Note on the complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About us:

Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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