Max Healthcare Institute Limited

October 05, 2018

Ratings

Facilities	**Amount (Rs. crore)**	**Rating[1]**	**Rating Action**
Long term Bank Facilities	344.82	**CARE A (Single A) Credit watch with developing implications**	**Revised from CARE A+ (Single A Plus) (Credit watch with developing implications)**
Short term Bank Facilities	0.76	**CARE A1 (A One) Credit watch with developing implications**	**Revised from CARE A1+ (A One Plus) (Credit watch with developing implications)**
Total	**345.58 (Rs. Three hundred and forty five crore and fifty eight lacs only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

CARE has taken a view on the combined financials of MHC network of hospitals which includes MHIL consolidated financials and the trusts' (Devki Devi Foundation, Baljai Medical & Diagnostic Research Centre, Gujarmal Modi Hospital & Research Centre & Four Season Foundation) financials. MHC network of hospitals are either owned by MHIL and its subsidiaries or are providing medical services through medical service agreements entered between MHIL and its subsidiaries.

The revision in the ratings assigned to the bank facilities of Max Healthcare Institute Limited (MHIL) factors in moderation in PBILDT margin during FY18 on account of increased regulatory supervision in the healthcare sector and the temporary closure of Max Shalimar Bagh hospital over an alleged case of medical negligence. The pressure on the margins led to net loss during FY18 as well as substantial decline in the cash accruals. The increased regulatory supervision is expected to have a sustained negative impact on the margins of the MHC network hospitals going forward. Furthermore, there is an expected increase in debt in the medium term for certain committed debt funded plans which coupled with lower profitability are likely to have an adverse impact on the leverage levels of MHIL in the medium term.

The ratings continue to be on credit watch with developing implications on account of impending stake sale of Life Healthcare to a new JV partner and likely infusion of equity into MHIL in this transaction which may lead to improvement in leverage levels of MHIL. CARE is in the process of evaluating the impact of the event and the quantum of equity infusion on the credit profile of the company and would take a view on the rating once the exact implication of the said event can be ascertained.

The credit watch earlier was on account of cancellation of license of Max Hospital, Shalimar Bagh (one of the 14 hospitals in the Max network) by the Directorate General of Health Services (DGHS) of the Delhi government's heath department for alleged medical negligence. However, the financial impact of the Shalimar Bagh event has been captured in FY18 results and consequently in the credit profile of MHC network. The Delhi Medical Council through its order dated May, 2018 has concluded that, "no medical negligence can be attributed on the part of doctors of Max Super Specialty Hospital," though the final decision in the Court of Financial Commissioner will come in its due course. The ratings however continue to be on watch on account of reasons stated earlier in this communication.

The ratings continue to derive strength from resourceful promoter group and experienced management team, established and leading market position, diversification across various specialties, experienced team of doctors, modern infrastructure and the strong brand equity of Max network. Furthermore, the operational parameters of MHC network have consistently improved during past couple of years and have also demonstrated resilience during the current stringent regulatory environment.

The strengths are offset by decline in profitability, debt funded acquisitions and capex in medium term leading to moderation in the capital structure and intense competition from other established players in Delhi and NCR region. MHC network has no plans for greenfield projects in the medium term, however, planned acquisition and bed additions in the existing hospitals which would be majorly debt funded is expected to result in increased leverage levels in FY 19 – FY 22.

[1]*Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.*

Going forward, decrease in leverage levels on account of higher profitability or infusion of equity would be a key rating sensitivity. The ability to profitably scale up the operations, ramping up of the recently acquired facilities and any debt funded large capex / acquisition beyond planned levels shall also be key rating sensitivities. The final judgment with respect to Shalimar Bagh hospital which has a stay on its license from the Court of Financial Commissioner will be crucial going forward.

Detailed description of the key rating drivers

Key Rating Strengths

Resourceful promoter group and experienced management team

Max Healthcare Institute Limited (MHIL) is a JV between Max India Limited (MIL) and Life Healthcare International (Proprietary) Limited wherein each partner holds equal share of 49.70% as on March 31, 2018.

Max India Limited provides healthcare & allied services and operates the Healthcare Business (through MHIL), Health Insurance (through Max Bupa Health Insurance Company Limited) and Senior Living (through Antara Senior Living Limited). On a consolidated basis, MIL reported a total income of Rs.1,616 crore (PY: Rs.1,440 cr) during FY18 and net worth of Rs.1,280 crore as March 31, 2018 (PY:Rs.1267 crore).

Life Healthcare is one of the leading private hospital operators in South Africa which owns and operates 50 hospitals with 8152 beds and a support base of over 2900 doctors and specialists. There is an impending stake sale by Life Healthcare to a new JV partner. The transaction may also lead to fresh equity infusion into MHIL. However, the exact contours of the deal and the quantum of the equity infusion are not yet finalized.

Established and leading market position driven by strong brand equity

MHIL started its operations in 2001 and since then has established itself as a leading market player in the Northern India region. All the hospitals operate under the 'Max' name which has become an established brand and enjoys strong brand equity in North India. MHIL operates 14 facilities in North India, offering services in over 32 medical disciplines. Of these, eleven facilities are located in Delhi & NCR and the others in Mohali, Bathinda and Dehradun. The 14 facilities together had 2,378 operational beds as on March 31, 2018 (PY: 2,330) which have an average occupancy of 73%.

Experienced team of doctors and modern infrastructure

The operations of the company are well supported by a team of experienced doctors, nurses and paramedic staffs. The company had around 1850+ doctors, 4750+ nurses and 1000+ consultant physicians on board to service its patients.

Diversification across various specialties and improving channel mix

MHIL derives its revenues from a number of specialties including cardiology, oncology, neurology, orthopedic etc, thus not depending upon any single specialty. Among the various specialties, Oncology, Cardiac, Neuro, Renal have demonstrated healthy growth in last five years. MHIL derived 22.03% (PY:20.90%) of its total FY18 revenue from Institutional/PSU segment which is a low margin business. The company plans to reduce the contribution from this segment and focus more on international business.

Healthy operational parameters with consistent improvement during past couple of years

Operational parameters of the hospital as indicated by occupancy rate, inpatient-outpatient registrations, average revenue per occupied bed, etc have all consistently improved over the five year period FY14-FY18. The number of operational beds on combined basis for MHIL increased from 1,472 in FY14 to 2,378 in FY18. The Average Revenue Per Occupied Bed (ARPOB) increased from ~Rs.33,950 to ~Rs.44,000 for the same period.

The average occupancy rate has remained above 70% during the last five years even though the company has been constantly adding beds each year. This indicates the brand equity of "Max Hospitals" and acceptability of the same among patients.

Moderate financial risk profile

MHIL reported growth of 7% in its total income during FY18 on account of better occupancy rate and ARPOB. MHIL has been continuously increasing its bed capacity/occupancy enabling the consistent growth in revenue. Though, the growth in revenue was not as compared to the one envisaged earlier.

Although MHIL witnessed improvement in its operational parameters such as ARPOB and occupancy levels during FY18, however, the PBILDT margin declined by 300 bps while at net level, MHIL reported loss during FY18 as against PAT margin of 0.97% during FY17.

The profitability margin was impacted due to combination of sustained factors such increased regulatory intervention (such as capping of stent prices and knee implant) and stricter compliance norms along with reversible factors such as closure of Shalimar Bagh facility for 12 days, intermediate shift to institutional business and closure of referral business. Though the impact of reversible factors is expected to reduce, the profitability is expected to remain under pressure going forward in medium term.

MHIL's overall gearing stood at 1.18x (PY: 1.02x) as on March 31, 2018, whereas the interest coverage ratio remained at 1.71x (FY17: 2.11) during FY18.

Key Rating Weakness

Exposed to regulatory risk
MHIL operates in a regulated industry which has witnessed continuous regulatory intervention during past couple of years. Regulations such as capping of stent prices and knee implant and stricter compliance norms have adversely impacted the margin of the company.

Recently acquired hospitals are still in ramp up stage leading to lower profitability
MHIL has acquired few hospitals in past five years. Some of them have ramped up and have already turned profitable. However, a few hospitals such as the ones located in Bhatinda and Dehradun have not yet turned profitable leading to pressure on the MHIL (combined) profitability. Going forward, improvement in profitability of the recently acquired hospitals will be crucial and remains to be seen.

Large planned bed additions in the existing hospitals with debt funding
MHIL plans to add around 700 beds over the period of FY19-FY22 in an organic way. Other than the bed additions, MHIL also plans to acquire remaining stakes in two of the hospital acquired in past couple of years. No further greenfield projects / acquisitions are in the pipeline and the company plans to grow organically going forward. MHIL plans to partly fund the bed expansion and stake purchase through debt which would have an impact on the leverage structure of the company. Going forward, the amount of debt for capex and stake purchase would remain crucial for MHIL's credit profile.
Intense competition from other established players in Delhi and NCR region
The growth in population, increase in lifestyle-related diseases, rising purchasing power of the middle class and higher awareness of chronic illnesses will be the key growth drivers for the sector. Although there is increasing competition in the sector; however, comfort is drawn from the sizeable presence and established position of Max Hospitals. Going forward, MHIL's prospects would depend upon its ability to improve its profitability, continued scale-up of operations and to manage the competitive pressures in the sector.

Analytical approach: Combined financials of MHC network of hospitals which includes MHIL consolidated financials and the trusts (Devki Devi Foundation, Baljai Medical & Diagnostic Research Centre, Gujarmal Modi Hospital & Research Centre & Four Season Foundation) financials. MHC network of hospitals are either owned by MHIL and its subsidiaries or are provided medical services through medical service agreements entered into by MHIL and its subsidiaries.

Applicable Criteria
Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
CARE's methodology for Services Companies
Rating Methodology: Factoring Linkages in Ratings
CARE's methodology for financial ratios (Non-Financial Sector)

About the Company
Max Healthcare Institute Limited (MHIL) was incorporated in 2001 and operates 14 hospitals in North India as on March 31, 2018. Of this, 11 facilities are located in Delhi & NCR and the others in Mohali, Bathinda and Dehradun. MHIL holds 6 hospitals directly under it, 4 hospitals are under various subsidiaries and 4 others are under a trust structure.

Brief Financials (Rs. crore) - Standalone	FY17 (A)	FY18 (A)
Total income	1047.75	1102.78
PBILDT	80.16	54.68
PAT	6.34	-27.58
Overall gearing (times)	0.23	0.29
Interest coverage (times)	2.28	1.34

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating History for last three years: Please refer Annexure-2

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Term Loan	-	-	November 2031	269.82	CARE A (Under Credit watch with Developing Implications)
Non-fund-based - ST-BG/LC	-	-	-	0.76	CARE A1 (Under Credit watch with Developing Implications)
Fund-based - LT-Working Capital Limits	-	-	-	75.00	CARE A (Under Credit watch with Developing Implications)

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Fund-based - LT-Term Loan	LT	269.82	CARE A (Under Credit watch with Developing Implications)	-	1)CARE A+ (Under Credit watch with Developing Implications) (14-Dec-17) 2)CARE A+; Stable (28-Nov-17) 3)CARE A+; Stable (06-Oct-17)	-	-
2.	Fund-based - LT-Working Capital Limits	LT	75.00	CARE A (Under Credit watch with Developing Implications)	-	1)CARE A+ (Under Credit watch with Developing Implications) (14-Dec-17) 2)CARE A+; Stable (28-Nov-17) 3)CARE A+; Stable (06-Oct-17)	-	-
3.	Non-fund-based - ST-BG/LC	ST	0.76	CARE A1 (Under Credit watch with Developing Implications)	-	1)CARE A1+ (Under Credit watch with Developing Implications) (14-Dec-17) 2)CARE A1+ (28-Nov-17) 3)CARE A1+ (06-Oct-17)	-	-

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