

# New Capex Cycle to Boost Corporate Hospital Bed Capacity by 35-40% Over 3-5 Years

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## Synopsis

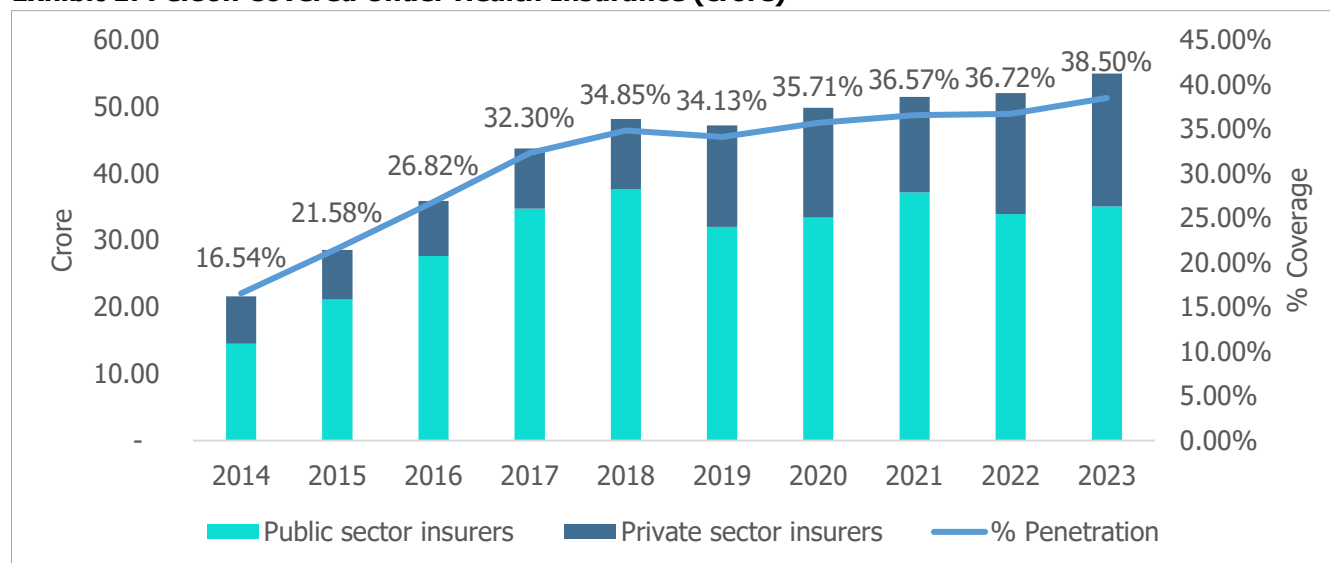
- The healthcare sector has experienced significant structural changes after COVID-19, such as increased health awareness, expanded insurance coverage, greater acceptance of elective surgeries, and rising costs. These factors have led to improved operating profitability, Return On Capital Employed (ROCE), and cash flows. The improved cash flows are being reinvested to expand capacity and sustain ongoing growth momentum.
- In response to the growing consumer focus on healthcare post-pandemic, the corporate hospital sector has initiated an expansion plan aimed at increasing bed capacity by approximately 35-40% over the next 3-5 years, based on FY24 levels, for the top-9 multi-specialty listed hospital chains.
- Following a consolidation phase from FY17 to FY24, during which hospitals focused on maximizing occupancy in their existing beds, current investment strategies aim to promote ongoing growth. This approach is bolstered by an increased emphasis on brownfield projects and operation and maintenance expansions, which mitigate execution and liquidity risks while improving overall performance profitability.
- Given the significant mismatch between demand and supply for quality beds, along with the improved financial health of corporate hospitals following the pandemic, players appear well-positioned to achieve profitable growth as they strengthen their presence in core markets and venture into Tier 2+ areas geographies.
- CareEdge Ratings forecasts that the corporate hospital chains in its coverage will achieve approximately 10-12% year-on-year sales growth in fiscal 2025 & 2026, driven by a 5-6% increase in Average Revenue Per Occupied Bed (ARPOB), a 100-200 basis point improvement in occupancy, and rise in new bed additions.
- Despite accruing additional debt to finance expansion and significant capital expenditures, CareEdge Ratings anticipates that net leverage (net debt to EBITDA) will remain approximately 1x in the near to medium term, bolstered by increased ARPOB and enhanced occupancy rates.

## Demand Outlook for Quality Healthcare is on the Rise

India's healthcare spending is significantly below the global average and that of other developing nations, such as Mexico, Brazil, Russia, and Argentina. Over the last decade, capital investment in healthcare in India has typically ranged between 2% and 4%. With significant untapped market opportunities and a shortage of healthcare infrastructure in India, leading Indian companies have immense potential for expansion. There have been significant structural changes in the healthcare sector post-COVID, including heightened health awareness, greater insurance coverage, growing acceptance of elective surgeries, and price increases. Supported by long-term structural growth factors, renewed momentum from PMJAY, and increased government focus on the healthcare sector, the Indian hospital sector is projected to grow at a compound annual growth rate (CAGR) of 10-11% over the next 3-5 years. Key demand drivers include the rise in lifestyle-related diseases, growing medical tourism, increasing incomes, and demographic changes. With limited government capital expenditure and a lack of infrastructure, the private sector is expected to experience accelerated growth in the years to come.

## Increasing Insurance Penetration to Support Demand

### Exhibit 1: Person Covered Under Health Insurance (crore)



Source: IRDA, CareEdge Ratings

The slow adoption of health insurance presents a significant obstacle to the advancement of India's healthcare services, particularly for low-income communities who are concerned about the affordability of healthcare. As of FY23, around 55 crore individuals in India had health insurance, a significant increase from 20 crore in FY14; however, the insurance penetration rate stood at only 39% in FY23. This shows considerable room for growth in the sector.

With initiatives like the PMJAY scheme and essential growth factors such as heightened health awareness, an ageing demographic, increased disease incidence, and easier online insurance application processes, health insurance coverage in India is projected to reach 47-50% by FY27. As coverage expands, hospitalisation rates are expected to rise, and the incorporation of mandatory health check-ups within insurance policies will further drive demand for a robust healthcare delivery system.

The rise in insurance penetration has also resulted in increased premiums. Insurers that have raised premiums post-COVID-19 are experiencing faster growth in premiums compared to the overall insurance penetration rate. This trend positively benefits the healthcare sector by enhancing patient access to affordable care.

As awareness of the importance of health insurance continues to increase, premiums are anticipated to sustain strong growth over the next 2-3 years, further propelling the healthcare sector.

## Medical Tourism Marching Onwards After Covid Fall

India has emerged as a leading destination for medical tourism, driven by efforts to make healthcare accessible and affordable for all. Its strategic location provides excellent connectivity to Southeast Asia, the Middle East, Africa, and West Asia. Additionally, the number of medical tourists arriving from the United Kingdom and Canada is increasing as the cost of treatment is lower in India.

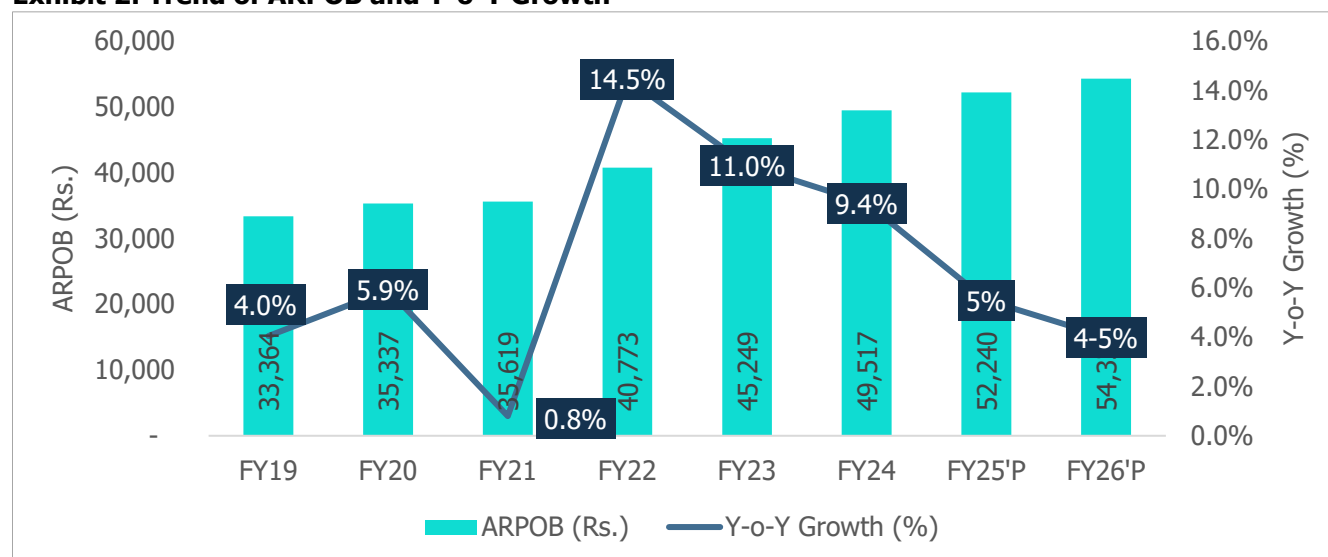
The availability of skilled professionals, advanced medical technology, and JCI-accredited facilities positions India for continued growth in medical tourism. Medical tourism is highly profitable for corporate hospitals, which benefit

from a higher share of JCI-accredited facilities, skilled staff, and strong brand recognition. International patients contribute higher ARPOBs compared to domestic cash patients, driving better profitability. Furthermore, corporate hospitals are shifting toward direct sourcing of international patients, moving away from the agent model, which is expected to boost margins in the coming years.

### Momentum in ARPOB Continues; Expected to Drive New Capex Cycle

ARPOB has grown at a CAGR of 8-9% over the past five years, exhibiting consistent annual growth, except during the Covid-19 period. Several factors influence ARPOB, including case mix, payor mix, the rise in surgeries, and annual price increases by healthcare providers. Post-COVID-19, increased awareness of the benefits of insurance has led to more people purchasing health insurance, while the growth of medical tourism has improved the payer mix. Additionally, hospitals have increasingly focused on high-end speciality treatments such as oncology, transplants, and neurology—high-revenue surgeries—that have contributed to the overall rise in ARPOB.

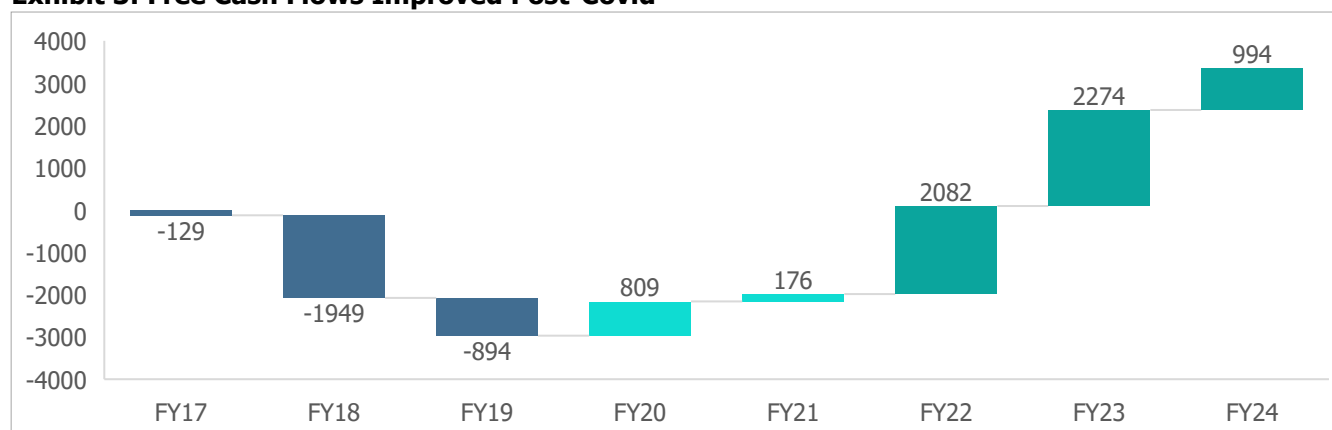
### Exhibit 2: Trend of ARPOB and Y-o-Y Growth



Source: Sample set of listed 9 Players, CareEdge Ratings

In fiscal year 2024, the sector experienced remarkable ARPOB growth of 9.5-10%, building on the solid foundation established in FY23. CareEdge Ratings anticipates that this upward trend will persist, with ARPOB projected to grow by 4-5% in the next two years. The significant increase in ARPOB in recent years has enhanced cash flows within the industry, initiating a new cycle of capital expenditures. Considering strong demand drivers and the necessity for quality healthcare, alongside increasing occupancy rates, companies have unveiled plans for both greenfield and brownfield development expansions.

### Exhibit 3: Free Cash Flows Improved Post-Covid

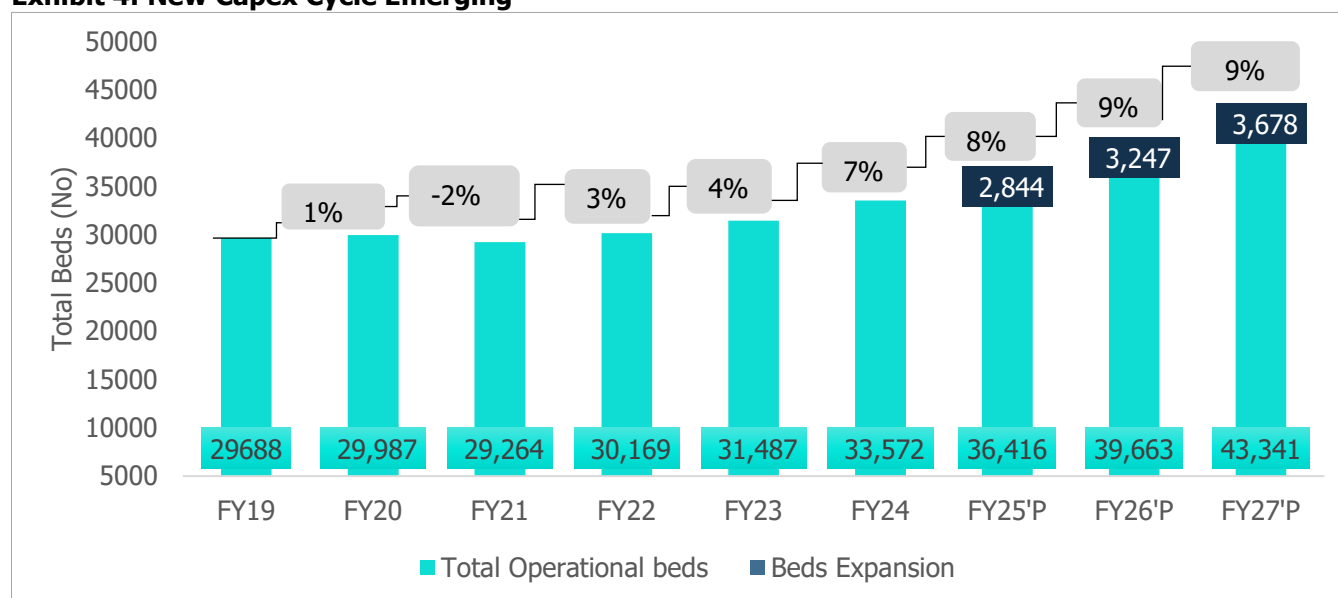


Source: Sample set of listed 9 Players, CareEdge Ratings

The low capital expenditure observed during FY19-24 played a key role in driving improved EBITDA margins, as it allowed hospitals to focus on enhancing business efficiency and optimising their service mix without the pressure of adding new beds to support volume-driven growth. After a consolidation period, most hospitals are now prioritising capacity expansion to take advantage of clear growth opportunities in their key markets. Major listed hospitals in India are expected to add around 10,000-12,000 beds over the next 3-5 years, representing an 8-9% year-on-year growth, compared to approximately 4,000 beds added during FY19-24.

Revenue growth for these listed corporate hospitals during this period was primarily driven by ARPOB, which increased at an 8-9% CAGR, supported by the structural changes that improved pricing and case mix. In contrast, bed growth for listed companies was relatively modest, at just 2-3% CAGR. Moving forward, growth will be fuelled by capacity expansion, with improved free cash flow generation and reduced leverage. Hospitals are entering a substantial capital expenditure cycle, aiming to expand bed capacity by approximately 35-40% on average over the next three to five years. CareEdge Ratings believes that future growth will be driven mainly by volume expansion and bed additions rather than significant ARPOB growth, as seen in the past.

### Exhibit 4: New Capex Cycle Emerging



Source: Sample set of listed 9 Players, CareEdge Ratings

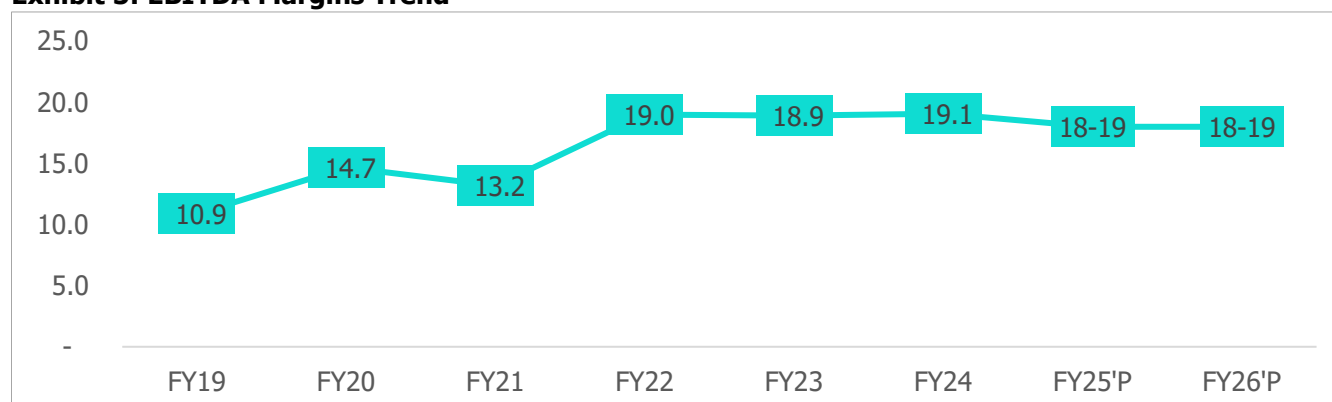
Given the strong demand outlook, fuelled by demographic changes (including an ageing population and the growing prevalence of lifestyle-related diseases), expanded insurance coverage, rising incomes, and better connectivity (improving access to healthcare), we anticipate that new beds will be easily absorbed without adversely impacting EBITDA margins due to these favourable conditions. An expanding and strengthening EBITDA base will help offset any potential pressure on profitability from the addition of new beds.

### Margins and Credit Matrix To Remain Stable

Corporate hospital-listed players' revenues have been growing steadily, except in FY21, when the COVID-19 pandemic led to a slight decline due to reduced occupancy and ARPOB. Post-COVID, a combination of favourable factors has driven growth in ARPOB and occupancy, resulting in healthy revenue growth at a CAGR of 15-16% over the past five years. CareEdge Ratings anticipates this growth momentum to persist, with a projected CAGR of 10-12% over the next 2-3 years, despite the expansion of its bed base.

Before the pandemic, industry margins typically ranged from 12% to 15%. However, in the past 2-3 years, margins have improved and stabilised at around 18-19%, driven by cost optimisation efforts, higher ARPOB, and operating leverage. CareEdge Ratings forecasts that operating margins will remain in the 18-19% range even after the new supply enters the market. Factors such as increased insurance coverage, international patients, and a diverse clinical mix are expected to help sustain these margins despite additional overhead costs associated with the addition of beds in new facilities.

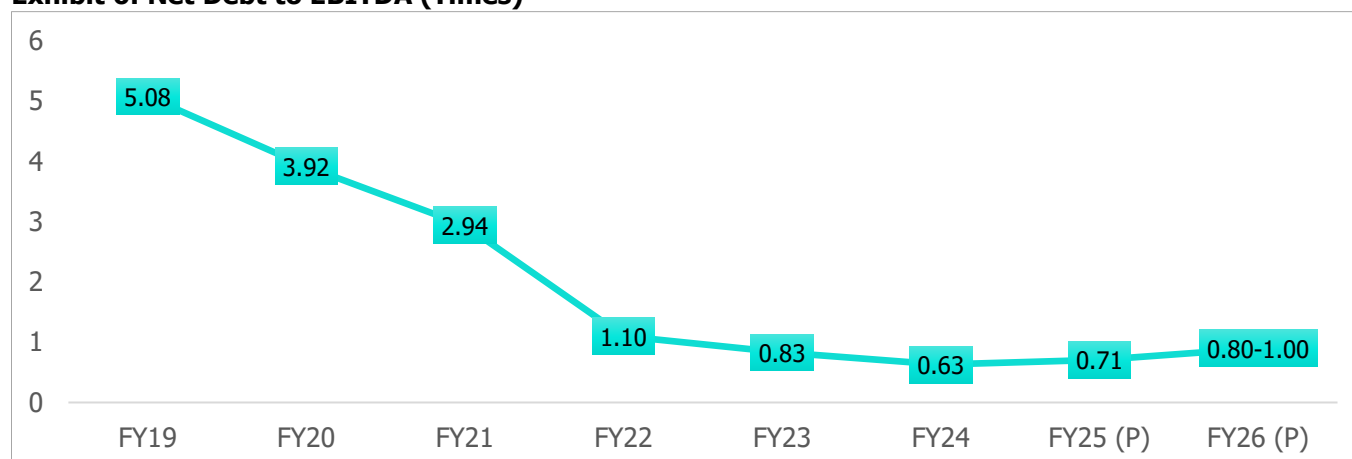
### Exhibit 5: EBITDA Margins Trend



Source: Sample set of listed 9 Players, CareEdge Ratings

With the improvement in operating profitability, cash accruals have risen, enabling industry players to significantly reduce their leverage over the past three to four years. The net leverage, calculated as net debt to EBITDA, was approximately five times in FY19 but has notably improved to 0.63 in fiscal 2024, as the players primarily focused on ARPOB expansion and debt reduction, rather than engaging in any capital expenditure. CareEdge Ratings anticipates a slight moderation in the leverage ratio from fiscal 2024 levels as companies enter an expansion phase, partially financed by debt. Nevertheless, it is expected to remain strong and healthy over the next two years.

### Exhibit 6: Net Debt to EBITDA (Times)



Source: Sample set of listed 9 Players, CareEdge Ratings

### CareEdge Ratings' View

During FY19-24, revenue growth for listed corporate hospitals was primarily driven by ARPOB, which grew at an 8-9% CAGR, supported by structural changes that improved pricing and case mix. In contrast, bed growth for these companies was relatively modest, with a CAGR of just 2-3%. Looking ahead, growth will be fuelled by capacity expansion. With more substantial free cash flow generation and reduced leverage, hospitals are entering a significant capital expenditure phase, aiming to increase bed capacity by around 35-40% on average over the next 3-5 years.

"CareEdge Ratings believes that future growth will be driven mainly by volume expansion and bed additions. Given the considerable demand-supply gap for quality beds and the improved financial health of corporate hospitals post-pandemic, these players are well-positioned to achieve profitable growth as they deepen their presence in core markets and expand into Tier 2+ regions. Operating margins are expected to remain in the 18-19% range, even with the influx of new supply, as factors like increased insurance coverage, international patients, and a diversified clinical mix will help sustain margins despite the added overhead from new facilities. Although additional debt will be taken on to fund expansion and capital expenditures, CareEdge Ratings expects net leverage (net debt to EBITDA) to remain around 1x in the near to medium term," said Ravleen Sethi, Director, CareEdge Ratings.

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