



“Fortis Healthcare Limited  
Q1 FY23 Earnings Conference Call”

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**Moderator:** Ladies and gentlemen, good day and welcome to the Q1 FY23 Earnings Conference Call of Fortis Healthcare Limited. As a reminder, all participant lines will be in the listen only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing “8” then “0” on your touchtone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Anurag Kalra – Senior Vice President, Investor Relations at Fortis Healthcare Limited. Thank you, and over to you, sir.

**Anurag Kalra:** Thank you Steven. A very good morning and good afternoon, ladies and gentlemen, and welcome to Fortis Healthcare’s quarter 1 FY23 Earnings Call. I hope all of you have got a chance to go through the Presentation and our Press Release on the earnings that we had circulated on Friday evening.

The call today is being chaired by our Managing Director and CEO – Dr. Ashutosh Raghuvanshi. With him, we have our Chief Financial Officer – Mr. Vivek Goyal. On the SRL side, we have Mr. Anand – the CEO of SRL. And with him is Mangesh Shirodkar – our CFO of the SRL business.

We will start the presentation with some opening comments by Dr. Raghuvanshi, on the earnings gone by post which Anand will take you through certain key highlights of the diagnostics business. And then we shall open the floor for question and answers.

Thank you. Over to Dr. Raghuvanshi.

**Ashutosh Raghuvanshi:** Thank you, Anura. Very good day, everyone. And thank you for your time to join us on our Q1 financial year ‘23 Earnings Call. I hope all of you are safe and well. I shall come straight to the performance of the quarter. And then Anand will take you through the highlights of diagnostic business.

We've had a good start to the year. Our consolidated revenues have increased 5.5% versus Q1 of financial year ‘22 to Rs. 1,488 crore. Within this, our hospital business has done exceedingly well with a robust growth in revenue of 18.5% versus Q1 of financial year ‘22 and 14.6% versus quarter 4 of financial year ‘22. The consolidated revenues were impacted by the diagnostic business. And if you recall, we had clearly articulated this in our last earnings call, this business as expected, has seen a decline in gross revenue of about 25% versus the corresponding quarter and 11% versus the trailing quarter, led by a significant fall in COVID test volumes. There was a sizable revenue contribution from COVID, both in Q1 and Q4 of financial year ‘22, which was not there in Q1 of financial year ‘23. At the consolidated level, the company's revenue has grown by 5.5%.

On the profitability, our hospitals business EBITDA stands at Rs. 208 crore, an increase of 39% and reflecting margins of 17.4% versus 14.9% in Q1 of financial year ‘22 and 13.8% in Q4 of

financial year '22. Adjusting for the losses with respect to the Arcot Road facility in Chennai, EBITDA margins for the quarter stood at 18.3%. The improvement in margins has been led by a healthy performance on all the key hospital operating metrics, which I shall speak about a bit later.

On the diagnostic segment, commensurate with the decline in revenues due to the COVID impact, margins were lower with EBITDA for the quarter at Rs. 64 crore, this reflected margins basis gross revenue at 19.3% for the quarter versus 30.6% in Q1 of financial year '22 and 22.5% in Q4 of financial year '22. Combining both the hospitals and diagnostic business, our consolidated EBITDA for the quarter was Rs. 272 crore, marginally lower as compared to Rs. 283 crore in Q1 of financial year '22. Consolidated EBITDA margin was at 18.3% versus 20.1% in Q1 of financial year '22 and better than 16.5% in Q4 of financial year '22. It is pertinent to highlight that the contribution of hospital EBITDA increased to 76% in Q1 financial year '23 versus 53% in Q1 of financial year '22 and 63% in Q4 financial year '22, signifying the strength in hospital business earnings and largely balancing out the decline in earnings from the diagnostic business. At the PAT level, we reported a profit after tax prior to exceptional items of Rs. 134 crore compared to Rs. 124 crore in Q1 of financial year '22. This is an 8% growth versus the corresponding quarter and a robust 55% growth versus Q4 of financial year '22.

Coming to the qualitative aspects of hospital business:

We have made good progress on all fronts with higher footfalls and more demand for elective procedures for surgical revenue contributing to overall revenues reached 61%, which is an all-time high. This compares to 41% in Q1 of financial year '22 and 57% in Q4 of financial year '22. While the overall occupancy in the quarter was similar at 65% versus Q1 or financial year '22, the occupancy mix changes favorably due to the higher non-COVID IPB numbers and this was witnessed across almost all our key specialties. This resulted in a very healthy ARPOB at Rs. 1.96 crore, a 21% increase over the corresponding quarter and even better by 4% for quarter 4 of financial year '22. Our international patient revenue have also seen a good traction for the quarter. International Patient revenues were at Rs. 89 crore, a growth of 126% over the corresponding quarter and 36% over the trailing quarter. International Patient revenue at the end of quarter 1 of financial year '23 contributed 7.5% to the total hospital revenues.

It is also important to highlight that some of our key underperforming facilities such as Sirohi and Jaipur have witnessed higher revenues and better profitability versus both the trailing and corresponding quarter. We have also progressed well on our brownfield expansion plans and by small numbers. We have added a total of 55 beds primarily in Fortis Mulund where we have commissioned an additional floor and have also added some beds in FMRI Gurgaon. In line with our intent to expand our operational bed capacity by approximately 1,500 beds in the next few years, our existing facilities like FMRI, Mohali, Noida and Shalimar Bagh are slated to add in excess of 200 beds each. This I believe will be funded through internal accruals and I have already chalked out plans to move rapidly on this.

In addition, we have also commissioned the state of art 12-bedded oncology daycare center providing chemotherapy services in a prominent Delhi location to further expand our reach and presence and complementing our existing oncology service offerings in several of our hospitals in Delhi NCR. Depending on the success of this model, we would replicate this at a scale. Commensurate with our medical progress, we continue to attract high quality clinical talents. We have onboarded clinicians in specialty of urology, nephrology and transplant and rheumatology during this quarter.

Revenues from digital channels such as website, apps and online campaigns have grown 74% over Q1 of financial year '22 and contributed approximately 23% of the overall revenues. All in all, I am pleased with the way our hospital business is tracking and remain hopeful of continuing this momentum. On the diagnostic side, like I had mentioned at the start, business was impacted due to decline in COVID volumes, non-COVID revenues however have grown 29% versus Q1 of financial year '22 and 8% versus quarter 4 of financial year '22. This is on account of increase in the non-COVID test volumes as the pandemic recedes. I would like to highlight that competitive pressure in the diagnostic business remain and hence the operating environment would be challenging in short term. At the same time, our focus on channel expansion, which is our collection center network, our specialized test portfolio and our customer touch points to lab ratio all continue to be further strengthened. I will let Anand speak on that in detail after my comments.

On the balance sheet, we remain quite healthy with a net debt to EBITDA of 0.54x. This is similar to Q4 of financial year '22. Our net debt stands at Rs. 585 crore as on 30th of June 2022. A stronger balance sheet also allows us to evaluate inorganic growth opportunities in line with our cluster strategy approach. In tandem, such opportunities would also help us gain from potential network synergies in our key geographies of Delhi NCR, Maharashtra, Bangalore and Kolkata. As I conclude my comments, I want to reiterate to all of you that we remain committed to becoming a best patient focused organization, one that constantly strives to deliver excellent clinical care and best in class service offering to our patients. This is at the center of everything we do. And I believe this is what will eventually reflect in stronger organization and a progressive improvement in the performance of the company. Thank you. And with that, I would like to hand over to Anand for comments on the diagnostic business.

**Anand K.:**

Thank you, Dr. Raghuvanshi. A very good morning to everyone on the call. Thank you for joining us today. On behalf of SRL Diagnostics, I warmly welcome you all to Q1 FY 2023 results conference call. I hope all of you and your families are safe and in good health. I want to start off by thanking our employees, customers and partners for the trust and loyalty during the testing time. During the quarter, we reported a revenue of Rs. 332 crore with 96% of our revenue coming from non-COVID testing. Our non-COVID revenue numbers for Q1 FY23, that is excluding COVID and COVID alike tests, stands at Rs. 312 crore against Rs. 242 crore in Q1 FY22, registering a growth of 29%. COVID testing revenues contribution in Q1 FY23 is 4% compared to 26% in Q1 of FY22. Revenue contribution from specialized non-COVID tests have gone to 36% in Q1 of FY23 compared to 20% in Q1 of FY22. Our EBITDA stands at Rs. 64

crore with a margin of 19.3% for Q1 FY23, compared to a margin of 13.6% in Q1 of FY22. We are confident that non-COVID testing on our specialized categories will aid in growth over the rest of the year. As far as B2C, B2B mix is currently 55/45 in Q1 of FY23 compared to 57/43 in Q1 of FY22. During this quarter, SRL conducted approximately 9.96 million tests, a degrowth of 6% compared to Q1 FY22 and a decline of 7% versus the trailing quarter. This is primarily due to the drop in COVID testing volumes. We serviced 4.3 million patients during this period. Keeping in line with our network expansion strategy, especially in the priority cities, we added 243 new customer touch points in Q1 FY23. We have taken a number of initiatives to improve our customer experience including the launch of our new WhatsApp chatbot and live phlebotomist tracking feature. On the people front, we completed more than 1,400 mandates of training in Q1 of FY23. In the last few years, SRL has progressed to make many tailor-made competency enhancement programs. Training, learning and development continues to be one of our priority area. In this quarter, we have added 50 plus new tests and technologies to strengthen our testing portfolio. Our R&D team works on care development, technology evaluation and validation studies. Currently, we are undertaking a number of new initiatives, especially in the area of genomics, proteomics and pharmacogenomics that will enable us to be ready for the next big shift in diagnostics. In this year, we will particularly look at co-marketing initiatives, clinical trial studies and contract validation for kit manufacturers and technology providers, co-development of new biomarkers as one of our key areas of growth. We are progressing well on our project with Microsoft to develop an AI algorithm for the diagnosis of breast pathologies. This would be a breakthrough in digital pathology to usher in new AI driven tools in histopathology. Our focus on genomics, next generation diagnostics, along with our work in digital pathology and specialized testing category will help us differentiate ourselves and also enable us to be future ready. SRL has been at the forefront of embracing change and quickly adapting to changing customer expectations. Over the years, we will be focused on improving our customer experience, strengthening our test portfolio and go deeper in our priority markets. Thank you for your attention. I would like to now hand over the call to Mr. Anurag Kalra, our Head of Investor Relations.

**Anurag Kalra:** Thank you, Anan. Ladies and gentlemen, we will now open the floor for question answers. May I please the question the moderator.

**Moderator:** We will now begin the question-and-answer session. Ladies and gentlemen, we will wait for a moment while question queue assembles. The first question is from the line of Amit Goela from Rare Enterprises. Please go ahead.

**Amit Goela:** This is a very good performance, and congratulations to all of you. Sir, I've got a couple of questions on the hospital side. Sir, when do you think Arcot will breakeven?

**Ashutosh Raghuvanshi:** Amit ji, Arcot, the initial progress was a little slow. Normally, we would have expected in 18 months for it to mature. But the first year somehow was impacted greatly by the COVID wave. However, now that traction is happening, and we expect that it will take another 12 months before it becomes positive.

- Amit Goela:** 12 months, like so in the first quarter next year, it should be positive, sir?
- Ashutosh Raghuvanshi:** That is the hope.
- Amit Goela:** And sir, in that one particular slide where you've given the hospital margin metrics, almost 30% of your revenue is below 15% EBITDA. And 22% of your revenue is below 10% EBITDA. So, when do you see this part moving up because it can make a big difference to the margins then sir?
- Vivek Goyal:** Amit ji, if I can take this question, Vivek Goyal. Good morning. Your observation is absolutely correct. So, there is some hospitals where the EBITDA margins are on the lower category and that is dragging overall EBITDA margin below 20%, which is the immediate target for us. And we are working on those hospitals. As Dr. Raghuvanshi covered in the initial part of his address, 2 of those hospitals, FEHI as well as Jaipur have shown very good traction and we are quite hopeful that both these hospitals will very soon come out from this category, means will move up. And there are a couple of hospitals in Chennai including this Arcot Road, which is also impacting this and Malar also is performing below par. So, we are working on that. And hopefully, this list will narrow down and some of these hospitals will move towards the next category most probably in the next year.
- Amit Goela:** And sir, you're looking at 20% margin in the medium term, so you're looking at this year or next year.
- Vivek Goyal:** No, sir. This year it will be difficult, but we are keeping a target for ourselves for next 2 years, we should be reaching there.
- Amit Goela:** One last question. Did I hear it right, sir, you said you'll be doing a brownfield expansion of 1,500 hospital beds over the next couple of years?
- Vivek Goyal:** Not couple of years, sir. It will be over a period of for next 4 years because we have already identified the project, lands are available, we have applied for the approval for the building plan and all those stuff. So, this typically takes 2 to 2.5 years' time for construction post approval, and then some stabilization period, equipment ordering and all. So, we are hopeful that in 4 years' time, majority of this expansion will kick in.
- Moderator:** Thank you. The next question is from the line of Shyam Srinivasan from Goldman Sachs. Please go ahead.
- Shyam Srinivasan:** Just the first one on the hospital business. ARPOB dynamics again remain robust. I'm looking at not necessarily Y-o-Y, but if I do even 3 years 1Q '20, it's like 8% CAGR through the time. So, just Dr. Ashutosh, if you can help us understand, I think you talked about surgical, non-surgical mix. But what's driving this? Is there an element of price increase that is there? Or is it peer mix rationalization? And what's the prognosis or the outlook for this?

**Ashutosh Raghuvanshi:** Shyam, it's more of case mix rather than payer mix or any other pricing intervention. We have taken minimal price increase this year, so that there is not a significant component here or pricing that is very small. The main kick has come from the increase in the procedures and surgical revenue being higher. Now, our estimate is that the ratio will sort of become slightly tempered over some period of time, because some of this is driven by the pent-up demand is our feeling, but we will have to test that hypothesis over the next few quarters. But having said that, we have certain levers still available to us. As I said that we have not taken major pricing revisions. So, we are rationalizing our pricing. We're not necessarily increasing in all the cases, but we are rationalizing to see that it remains competitive, but at the same time is competitive with the rest of the market. And I think by using all those levers, we are fairly certain that the ARPOB trend will continue to improve or at least remain sustainable at the current levels.

**Shyam Srinivasan:** I'm just understanding, medical inflation, consumer inflation is high. So, what is the hesitancy to increase prices? Is it optically wrong? Maybe it'll also a philosophical question, why can't we raise prices?

**Ashutosh Raghuvanshi:** So, you're absolutely right. If one looks at it very clinically and compares the inflation and covers inflationary costs every year, I think that would be a natural response. Having said that, I think it is imperative on any business not only healthcare, to build in efficiency over a period of time and reduce the cost and hence keep the prices under control. So, if every industry would just be simply passing on, then I guess there is no end to inflation. So, having said that, we are very conscious of the way healthcare is looked at. And healthcare industry is always under the glare of media and everybody else and there is a certain degree of social responsibility on our industry. We are able to improve our performance by doing several other measures. So, there is no hesitancy. However, there is a sense of responsibility with which we are working. And that's the reason why we are little conservative as our approach. Having said that, we are very clear about one thing that our immediate target, as Vivek said just now is to go to at least 20% margin at consolidated level and in some of the clusters as you would see that we are already above that in almost 60% of our revenue. But that idea is to take at least 80% of the revenue within that range by the next year. So, profitability is extremely important for us, but at the same time we want to be balanced in our approach.

**Vivek Goyal:** Shyam, just to add what Dr. Raghuvanshi has said, as you know, some of our payees, it is difficult to increase the price, but on cash payers, we are taking measures to increase the price to the extent possible depending upon competition and other things. So, cash payment is not like we are not increasing price at all, but it is in line with competition.

**Shyam Srinivasan:** Any quantum there on cash, Vivek sir?

**Vivek Goyal:** Yes, we are at around 4%.

**Shyam Srinivasan:** 4% increase on cash. Last 2 questions from me, just on utilization and the pent-up demand point that Dr. Ashutosh had brought up. Dr. Ashutosh, when you did the call in May, I don't think we

got the sense that we were going to end the quarter with 65%. At least I didn't infer just looking at whatever I think trends you had talked about April and May, so what has changed? In I think June looks like much higher than 65%, right, must be 67%, 69%, I'm just guessing. And is that sustainable utilizations now possible for us to reach the 70% mark that we have talked about?

**Ashutosh Raghuvanshi:** Yes. We are seeing better occupancy levels, right. In the month of April and May, the occupancy levels were not that high, but June definitely was higher and that trend is continuing. And it think that going forward that will continue. And also, I would like to remind you that this is on a slightly higher base, though about 60 odd beds have been added which is not a very large number. But even with those 60 odd beds added, the occupancy remains at the level of about 68%, 69% at the moment.

**Shyam Srinivasan:** Dr. Ashutosh, just sorry to persist. When I add the number of beds in the hospital metrics, it's showing Q-o-Q decline. Am I missing beds there or that's just a subset of the beds.

**Ashutosh Raghuvanshi:** No, these beds you will see in the coming quarter.

**Shyam Srinivasan:** The 60 beds you have added, you're saying, okay.

**Ashutosh Raghuvanshi:** Yes.

**Shyam Srinivasan:** And my last question, sorry, I'll try and keep it very brief, is on diagnostic services. Anand, again just going to the forward path, how should we look at growth and margins? We've had an earlier margin guidance or a directional sense of 23% to 25%, we're well below that for the quarter. But what are the ways we can build it back? And what's the outlook for non-COVID growth for the remainder of the 9 month? Thank you.

**Anand K.:** So, as you know that we were having operating leverage because of COVID during last year and we found that during that time the revenues went up. We were able to deliver higher profitability margins. So, even though we have given guidance earlier on 22% to 23% kind of margins, this quarter has been lower and we expect that it will keep going up over the quarters because we also need to increase our revenues, which will give us the same operating leverage, as well as since we are moving from a COVID quarter of Q4, since the trailing quarter had some COVID and we are moving forward. So, there are also some costs related to COVID, which will be there in these quarters, so which will trail off over a period of time. So, I think all these factors will really help in growing the profitability. But the growth on the non-COVID looks quite promising for us.

**Moderator:** The next question is from the line of Sarvesh Gupta from Maximal Capital. Please go ahead.

**Sarvesh Gupta:** Sir, most of my questions have been answered. Just 2 versions. One is on the court case, if you can give us an update on what's happening. And secondly, are there any incremental thoughts



with respect to the structuring of SRL stake that we have in terms of either demerger or sale of stake or acquisition of the remaining stake?

**Ashutosh Raghuvanshi:** Yes, Sarvesh. As far as the legal case is concerned, there was a mention made at the Supreme Court and the judges made a comment that within a couple of weeks, we should hear something. So, this comment was made about 10 days back. So, we expect very soon a resolution of the case. So, that should be within the month of August is our expectation and that's what we're hearing from our lawyers as well. As far as SRL, I will request Vivek to address that.

**Vivek Goyal:** So, SRL stake, as I mentioned in the last call also, we will be exploring the different options, probably this may not be the right time because of the volatility in the market. But we are exploring different options and maybe come back with some plan by the end of this year.

**Sarvesh Gupta:** Are we also considering purchase of the remaining stake as one of the possible options for us?

**Vivek Goyal:** Right now, there is nothing in pipeline, but that option can also be explored actually.

**Moderator:** Thank you. The next question is from the line of Nitin Agarwal from DAM Capital. Please go ahead.

**Nitin Agarwal:** Dr. Raghuvanshi, just going back to the slide on the margin matrix, which is there in the presentation, two things; one is in the bottom layer, which is the five hospitals which are below 10% EBITDA margins, can you just help us understand which are these hospitals which are there below 10%?

**Vivek Goyal:** So, there are hospitals like Jaipur, Vashi – Mumbai, Malar, Sacred Heart and Arcot Road. These are the hospitals which are in that category.

**Nitin Agarwal:** In these hospitals, our occupancy is 50%, Arcot Road is understandable, because it's a new hospital, I presume the other hospitals are all reasonably mature hospitals. So, is there a structural problem in these other four hospitals that we have occupancy on an average for the group around 50%?

**Vivek Goyal:** Each hospital is having its unique problem, some are struggling for the occupancy, as you rightly mentioned, like Vashi hospital in Mumbai, that is struggling on occupancy, similar is the case with Malar, where the occupancy we are not able to build up either because of the infrastructure issue or because of the hospitals for example, in Vashi we could not ramp up post-COVID. In COVID, this hospital was doing quite well. On the other hand, occupancy has gone up to the normal level of 70%-plus level, however, the ARPOB there is quite low, and that may be attributed to a lot of government schemes are there and that is actually dragging the ARPOB lower. And we are working on adding some more stability, therefore, which will improve maybe the profitability margin there. The other hospital like Arcot Road is a new hospital. So, there the occupancy is less.

- Nitin Agarwal:** Vivek, if we look at the two clusters which are there, 20% to 25% and 10% to 15%, one observation there was occupancy in both the clusters are similar. The ARPOB is higher in the 10% to 15% cluster, but the margins are a lot lower. So, can you just help us again understand that a little better, what is the dynamic here?
- Vivek Goyal:** Hospital like Amritsar, Punjab hospital, where we have more of 18% or more there because of the geography and plus Noida also come in that category. Faridabad, we are going for expansion and renovation work is going on, and that is affecting actually the patient flow and things like that. Anandapur is another hospital in that category, which was supposed to be in the upper category, but this quarter was not very good for Anandapur. It has started recovering, I mean, June, July was a good month for them, and we are hopeful that this will also move up, and main reason was for the occupancy growth.
- Nitin Agarwal:** In which group, FEHI will be now?
- Vivek Goyal:** FEHI is in the third group.
- Dr. Ashutosh Raghuvanshi:** FEHI has come up from less than 10%, Nitin, it's gone one up. So, FEHI and CH Road, which were at the bottom rung, have now moved one level up
- Nitin Agarwal:** Is it sustainable given what we've seen so far?
- Vivek Goyal:** Yes, we can say that because it is consistently improving in last three quarters if you see, FEHI is consistently improving and last quarter it crossed 10%, and we are quite hopeful that it will continue to move upward only.
- Nitin Agarwal:** Vivek, you mentioned these costs are prior to the corporate costs. Can you give us a sense on what are annualized corporate cost in the hospital business?
- Vivek Goyal:** It is around 3% of the overall revenue. I'm talking hospital business only.
- Nitin Agarwal:** Is there a scope for optimization around here as we sort of scale up going forward?
- Vivek Goyal:** So, some measures we have taken post-tariff coming in and Dr. Raghuvanshi joining and the result of which has already come. But there is a big cost sitting in the form of legal costs, which is to deal with the various legacy issues the company's facing. And as these issues will start settling, I am quite hopeful that these corporate cost will also be under control. Plus, entity structure also we want to simplify it post Supreme Court order, because that should also reduce the corporate cost in my view. So, there is a scope, but we are restrained because of Supreme Court to some extent.
- Moderator:** The next question is from the line of Neha Manpuria from Bank of America. Please go ahead.

**Neha Manpuria:** Just extending on the hospital metrics, if I were to look at the hospitals below the 15% margin levels, is it fair to assume that some of this should see an improvement in margin, let's say in the next year or would it take longer for these hospitals to turn around and start contributing meaningfully to margin in a positive way I mean?

**Vivek Goyal:** I will not be able to give you exact timeline, but all the hospitals are showing very good improvement. And some of the plans which we are having is having a long-term plan, in the sense where we are trying to add some facility, for example, in Jaipur, suppose we want to add some biggest facility there just to get better margins as well as the patient flow. So, that may require some investment for equipment's ordering time, doctor having. So, those type of things sometimes take time. But all hospitals shown move according to my view.

**Neha Manpuria:** Sir, the reason I'm asking this question is, given our margin guidance of 20%, we're already at 17.5%, there is improvement that you've indicated in the existing hospitals. And if the existing hospitals below 15% move up, isn't the 20% conservative, particularly where mature hospitals for some of our peers are operating at? So, how should we build the bridge between what margins we should be operating at and where we are currently?

**Vivek Goyal:** No, you're absolutely right. So, there is always aspiration to move upward. But we will like to move a step-by-step, and our initial step when three years back was to cross 15%, which we have now done, and the next benchmark, we're keeping ourselves for 20%, and then we'll see how much more we can go. And I am 100% sure, looking at the potential in the company and the hospitals and the overall talent pool we are having, we are quite hopeful to move upward, 20%.

**Neha Manpuria:** My last question is on expansion. The 1,500 beds Brownfield expansion, I think we've mentioned that for some time now. But, given the assets available in the market, isn't entering new markets via, let's say, business development, or inorganic acquisition, part of the plan, we have a decent enough balance sheet to be able to do that, or our focus is on expanding and strengthening the existing hospitals that we have, just wanted to understand capital allocation a little bit more?

**Dr. Ashutosh Raghuvanshi:** You're absolutely right, with the strong balance sheet, we definitely aspire to look at beyond our existing clusters. However, the philosophy of having a focused cluster if we have to go to a new geography domains, so which means standalone hospitals are going to be evaluated in the given clusters, not in completely new geographies. But, if there was a cluster available, or there was even a couple of hospitals available in a close geographical area, we would certainly look at those. So, definitely, we have sort of activated our evaluation of the inorganic opportunities as well, and then we will be actively seeking those. But the priority to remain in a clustered approach as we grow. So, very remote geographies where we have no presence, even if there was a standalone asset, we would rather avoid that.

**Neha Manpuria:** Sir, from a cluster priority would it be East India over Mumbai, over NCR, just wanted to understand, what would be your priority when you're looking at acquisitions?

**Dr. Ashutosh Raghuvanshi:** Order of priority in our given clusters, NCR and Mumbai remain high priority and as well as Bangalore. So, these three are important and then followed by Calcutta and Punjab, so this is the order of priority. But we are open to new geographies if we are getting scale.

**Moderator:** The next question is from the line of Sabyasachi Mukerji from Centrum PMS. Please go ahead.

**Sabyasachi Mukerji:** First, I need one clarification. In your Q1 FY'22 presentation, the non-COVID revenue contribution in the diagnostics business was stated as 74%, in Q1 FY'23, it is stated as 55%. Where is the disconnect here?

**Anand K:** This is Anand here. So, the COVID revenue that we have talked about in the previous year same quarter was pure RT PCR tests alone. But this time, we have also included the COVID allied test, the CRP, D-dimer, because those steps were having a very significant contribution in Q1 of last year, because that was a second wave of COVID at that time. So, during that time, we have not looked at it that way. So, now, after the calculations, we have identified that it is about 19% of the revenue, so it is 26% plus 19%, so you have 45% is a total COVID contributions for Q1 of FY'22.

**Sabyasachi Mukerji:** Second thing on the margin improvement trajectory in the diagnostics business, I'm not so clear of how will you kind of go back to the earlier guidance of 22% to 23% given Q1 had 10% YoY growth on the non-COVID test volumes numbers, but still the margins are pretty low. What is the kind of actions you're going to take to kind of drive the margins from here?

**Anand K:** The margins, primarily because of operating leverage that we got last time, that we will continue to focus on revenue growth. So, I think on one side, we will keep a tight control on the costs, but at the same time, revenue growth is key since we have capacity utilization, so, we have capacities which can be utilized further. So, what we have seen is, we will be able to handle much more than what we are currently doing in our centers. Since the markets are also expanding, and there is some competitive intensity at this point of time, so, we are seeing these kind of changes, but overall I feel that over the next few quarters, we will see this improvement happening.

**Sabyasachi Mukerji:** What will drive the test volumes, I'm assuming you're going aggressive with the expansion, the test volumes are increasing, so, you will do some competitive pricing?

**Anand K:** No, actually, we are increasing our network also to see almost to the extent of close to 100 centers per month we are adding to our franchisee network. So, this kind of network expansion phase over a period of time centers start maturing, so, they start delivering more numbers, and since these centers are asset-light, and they deliver directly into an existing lab facility, so, they will contribute more towards margins over a period of time. So, if you see in the last one year, we have added close to about 800 centers. So, that will contribute over the next one or two years to improve the margins.

- Sabyasachi Mukerji:** My next question is on the hospital business. If I look at Q2 of last year and even Q3 of last year, we had a revenue run rate of nearly Rs.1,100 crores thereabout, we have clocked Rs.1,200 crores in Q1 of this fiscal, still the margins are lower. Have the losses increased over this period of time or what is that has changed?
- Vivek Goyal:** Q2 and Q3 is not exactly comparable because some part of COVID was there. But having said that, we are on the margin improvement trajectory as I have mentioned earlier to the questions also. So, no losses has increased, but, the margin improvement will be gradual, it will not be steep.
- Sabyasachi Mukerji:** But Q2 and Q3 of last year had COVID revenues, I understand that. The COVID I believe at a lower margin rather than a non-COVID surgeries or operations. Is that correct?
- Vivek Goyal:** You're right. So, non-surgical business was less, but at the same time, the volume was higher because the beds were occupied because of the COVID patients. And plus, in COVID-related patients the cost was not low, although the gross configuration one can say around 10% lower than the non-COVID business, but volume was compensated more than during that quarter, plus seasonality impact as well. So, first quarter generally remain very low for us, but later quarters generally pick up.
- Sabyasachi Mukerji:** So, you have been guiding that we'll reach hospital margins of 20% or more in the next couple of years. What is the kind of margins that you expect in this fiscal -- shall we touch 18% on hospital business?
- Vivek Goyal:** We may be getting 18% depending upon how the circumstances pan out. We are trending toward that level as you can see from our first quarter number.
- Sabyasachi Mukerji:** This is on reported basis, right, and not on adjusted for the losses of Arcot?
- Vivek Goyal:** No, it is after Arcot Road.
- Moderator:** The next question is from the line of Naushad Chaudhary from Aditya Birla AMC. Please go ahead.
- Naushad Chaudhary:** Some clarifications I have. Firstly, on the legal cost, if you can quantify it, it will be better, how much it is quarterly, if not is it at the similar run rate which it was in last two, three years or has it gone down?
- Vivek Goyal:** Legal costs had started coming down. It is difficult to quantify quarter-on-quarter because as you know legal costs generally depending upon when the hearing happen and when the things kick in. But as our cases are coming down, like FEHI is more or less settled, and Supreme Court hearing also settled more or less, so our legal costs start seeing a declining trend.

- Naushad Chaudhary:** Should we see a meaningful decline or how should we say it in this financial year?
- Vivek Goyal:** As I said, it's very difficult to comment because a lot of cases are going on and how each case will pan out, it is very difficult to predict, but rationally we are coming down in legal costs.
- Naushad Chaudhary:** Secondly, just a clarification. I couldn't hear this. You said there are some COVID-led cost, which should come in 2Q. I don't know if I've heard it correctly. What was this we were indicating sir?
- Dr. Ashutosh Raghuvanshi:** On the diagnostic side, some of the costs which have built up because COVID volumes will come down now. But that will happen gradually over the next two quarters.
- Naushad Chaudhary:** Lastly, on the hospital margin, sir, you have been sharing the steps which you are taking the mix improvement and turning around some low margin hospitals to good positive EBITDA. But can you give us the specific steps which we are taking to achieve our desired margin because mix is something one which is I am able to understand, otherwise, the low margin hospital and occupancy, these two things I am still unable to understand it, how will it make much dent because at any given point of time, we will have a low margin hospital if I'm correct in understanding your business, can explain this?
- Vivek Goyal:** As you know, the hospital business margins depend on one is the occupancy as you rightly said, and some of the hospitals in our hospitals network are operating below the average occupancy which other hospitals are achieving. So, one is the improvement in the occupancy by better empanelment, by attracting more patients, so, that is one thing which we are trying to achieve. And secondly, the surgical mix also we are planning to improve further where we are adding lot of clinical talent in our hospital network, adding more facility so that we can get the quality revenue, plus the payer mix also we are working and it has started showing results also where the TPA and Care including now the international business is going up which add to the better ARPOB and EBITDA Margin.
- Naushad Chaudhary:** What should be the hospital occupancy rate,
- Vivek Goyal:** So, any hospital which is operating below 70% occupancy level, there is scope for improvement, let me put this way.
- Naushad Chaudhary:** How much can we take, 70%?
- Vivek Goyal:** In peak, it may go up to 80%, 85% also. Some of the hospitals still operating at 80%, 75% -plus occupancy.
- Naushad Chaudhary:** This is on an individual level, right, but on a blended basis if we see the hospital businesses, how should we see it, Can the entire portfolio go beyond 70% or 70% is the limit?

- Vivek Goyal:** Yes, 75% is the level where the hospital start feeling the shortage of beds.
- Moderator:** The next question is from the line of Sanjay Shah from KSA Securities. Please go ahead.
- Sanjay Shah:** Sir, can you highlight upon the change in brand name, is there any update on that side?
- Dr. Ashutosh Raghuvanshi:** That is subject to the legal case getting settled and whatever direction we get from the hon'ble Supreme Court. So, we have to wait for that.
- Sanjay Shah:** Sir, can you highlight upon the development on medical tourism side, is there any growth seen on that side?
- Dr. Ashutosh Raghuvanshi:** So, those numbers are coming to almost normal, as we said that about 7.5% of the revenue came from international, and with an increase base, so that is almost near to the pre-pandemic levels. So, we would definitely look at it further.
- Moderator:** As there are no further questions, I now hand the conference over to the management for their closing comments.
- Anurag Kalra:** Thank you, Steven. Thank you very much, ladies and gentlemen. If there are any follow-up questions, Gaurav and myself are available to provide any further clarifications you might have. Thank you once again for joining us on the call and have a good day.
- Moderator:** Ladies and gentlemen, on behalf of Fortis Healthcare Limited, that concludes this conference. We thank you all for joining us and you may now disconnect your lines.