"HealthCare Global Enterprises Limited Q3 FY22 Earnings Conference Call"

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MANAGEMENT: DR. B. S. AJAIKUMAR – EXECUTIVE CHAIRMAN
MR. RAJ GORE – CEO
MR. SRINIVAS RAGHAVAN – CHIEF FINANCIAL OFFICER

Moderator: Ladies and gentlemen, good day and welcome to the Q3 FY22 earnings conference call of HealthCare Global Enterprises Limited. As a reminder, all participants' 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 for an operator by pressing '*' and then '0' on your touch-tone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Diwakar Pingle from Christensen Advisory. Thank you and over to you, sir.

Diwakar Pingle: Good evening and good morning to all the participants of the HealthCare Global Enterprises Q3 FY22 earnings conference call. Today, we have with us Dr. B. S. Ajaikumar – Executive Chairman, Mr. Raj Gore – CEO, and Mr. Srinivas Raghavan – Chief Financial Officer of HCG Enterprises along with the top management members to share the highlights of the business and financials. Please note that we have uploaded the earnings presentation to the stock exchanges and also shared the same through our mailers. In case anyone has not received it, please reach out to us and we are happy to send the presentation over to you. As usual, the standard safe harbor clauses applies, and without delay, I now hand over the floor to Dr. Ajaikumar for his opening remarks.

Dr. B. S. Ajaikumar: Thank you very much Diwakar and welcome to this investors' call, and good evening to everyone. I am pleased to report that hopefully the COVID threat has passed and now we can forge ahead with a strong sense of optimism. We are happy to report a robust Q3 FY22 with secular growth across regions and segments. The last 6 years as a publicly listed Company have seen a sustained growth in footfalls and revenue. Our new patient registration has almost doubled since 2018 and we currently have above 100,000 new patients per annum and which also in turn has doubled the revenue in the said period. The fact that 85% of this revenue is oncology centric is a clear testament of our model in addition to the deep social impact that we make to the lives of thousands of patients and their families. Looking at the future, we believe that this growth will enhance not only at the back of increasing longevity of patients, but also a realization that cancer is now being viewed and treated as a curable and chronic disease with a good lifestyle.

With addition of labs and the clinical trial business, we are now uniquely positioned to not only enhance our diagnostic capabilities and offerings, but potentially redefine precision medicines with end-to-end expertise spanning bioinformatics, genomics, and research. With 25 hospitals, 21 of which are oncology focused, we have built a niche platform in the Indian healthcare space. Managing CAPEX effectively, I believe the future years will see the Company benefiting from these investments. Overall, HCG is well positioned to generate superior growth and profitability under the resourceful stewardship of Mr. Raj Gore, our CEO. All this comes along with a clear focus on productive outcome for all our stakeholders, the most important of whom are our patients for whom the best consequence is a positive medical outcome. Before I hand over to Mr. Raj Gore, I also want to touch upon the issue of our Gurugram project where we had undertaken building a cancer center. Because of the inordinate delay, various factors including the most important being the COVID for the last couple of years. Internally, that matter has been discussed, and at a board level, we have taken a decision to not pursue this project at present. We have made necessary adjustments in the financials to that effect. I am sure some of you will have questions about what will be the future of Gurugram project. At this point, we are not pursuing it. Obviously, in the future, we may revisit this project. I now hand over to Mr. Raj Gore.

Raj Gore: Thank you Dr. Ajai for being a role model and mentor to everyone at HCG. I extend a hearty welcome to all of the attendees and it is great to have this dialogue with you again. We are happy to share that we have delivered another quarter of sustained performance. This was our 4th consecutive quarter with all-time record revenue and 2nd consecutive quarter with all-time record EBITDA. Our new centers also recorded their 2nd consecutive quarter of positive EBITDA with margin expansion. Implementation of go-to-market plan across our network locations during the last 3 quarters has started showing results through this profitable growth. Overall, these results were made possible through execution focus and hard work of the entire HCG team, and we remain committed to driving growth and optimizing operations in the coming quarters.

As we look to the future, we want to build a long-term relationship with our patients to be their trusted advisor over a lifetime. With that objective in mind, we have begun our digital transformation journey to create an omnichannel end-to-end patient engagement platform with the help of digital technology. Our immediate priority will be on driving volume growth by focusing on 3 sets of patient funnels. One, creating awareness and lead generation. Second, purchase and conversion. Third, patient retention and lifetime value capture. We believe that this initiative combined with our differentiated clinical services will accelerate our growth in future and help HCG to solidify its leadership position in oncology. I would now like our CFO, Srini, to go over the important financial highlights for the quarter and year to date.

Srinivas Raghavan: Good evening to all of you. The highlights for the quarter ended 31st December 2021. Consolidated revenue was INR 3,581 million, up 30.7% from INR 2740 million in the previous year's equivalent quarter. During the quarter, vaccination revenue was INR 43 million compared to INR 250 million in Q2 FY22. I would like to highlight that the quarter's highest ever revenue was largely domestic led. International business revenue is steadily growing quarter on quarter but is yet to return to BAU level. Hence, it has substantial potential going forward. Consolidated EBITDA was INR 648 million, up from INR 437 million in the same quarter of the previous year, a Y-o-Y increase of 48.4%. Consolidated operational EBITDA was INR 690 million, up from 378 million in the same quarter last year, a Y-o-Y increase of 63.5%. The existing centers' operating EBITDA was INR 566 million, up from INR 399 million in Q3 FY21 that is 41% increase Y-o-Y resulting in a 20.6% operating EBITDA margin. This has been achieved by vigilant control in operating expenses resulting in consolidated operating margins being at 17.3%, an expansion of 350 basis points from 13.8% the year earlier. Vaccination contribution was INR 12 million compared to INR 58.3 million in Q2 FY22. The operating profit for new centers was INR 52 million compared to a loss of INR 21 million in the corresponding quarter of the previous year. Reported PAT was a loss of INR 458 million compared to a loss of INR 293 million in Q3 FY21. Proforma PAT was INR 21 million as compared to a loss of INR 205 million in the corresponding quarter of the previous year.

I would like to give a context to the said proforma PAT. We are continuously assessing the carrying amount of our assets. Hence, as a measure of prudence, there was an impact of impairment of the NCR project of INR 472 million. We also had a one-time project fee cost of INR 20 million for support on value creation plans. These were partly offset by an exceptional gain of INR 19 million on account of the Suchirayu acquisition.

I now request your attention to slide 32. YTD FY22 revenue grew by 44.4% Y-o-Y. HCG centers grew by 44% and Milann centers by 53.1%. YTD operating EBITDA of existing centers was INR 1,698 million, 21.3% margin versus 17.6% margin in YTD FY21. New centers witnessed an EBITDA of INR 51 million versus a loss of INR 111 million in YTD FY21.

I request your attention to slide 33 for normalized EBITDA as well as give us trends on proforma EBITDA arising out of the Suchirayu acquisition. We have had one-time consultancy fee for support on value creation activities of the organization. We have also covered proforma EBITDA assuming consolidation of Suchirayu, the EBITDA for Q3 FY22 and 9 months FY22.

I would like to draw your attention to slide 34 please. The revenue split for our business is 95% contribution by HCG centers and 5% by Milann centers. Within HCG centers, Karnataka's contribution to the revenue is 37% followed by Western India comprising of Gujarat at 25% and Maharashtra at 16%.

I would now like to draw your attention to slide 35 of the presentation. Strong growth in revenue continues across centers in the 3rd quarter of FY22. Jaipur delivered 146.7% Y-o-Y growth, South Mumbai delivered 116.5% Y-o-Y growth, Nagpur delivered 95.4% Y-o-Y growth, Bengaluru Center of Excellence delivered 42.8% Y-o-Y growth, and Borivali delivered 28.1% Y-o-Y growth. Revenue from new centers was INR 784 million in quarter 3 of year 22 versus INR 509 million in quarter 3 in FY21, which is a growth of 54.2% Y-o-Y. The existing centers recorded a healthy revenue growth of 25.1% in quarter 3 of FY22 on a Y-o-Y basis.

I would now like to draw your attention to slide 36. Increase in average occupancy rate in quarter 3 FY22 Y-o-Y basis of 56.9% versus 51.6% at a consolidated level. For existing centers, occupancy rate was 56.7% versus 50.3% corresponding quarter of last year. Increase in existing center ARPOB in quarter 3 FY22 was INR 37,248 versus INR 33,074 which is a 12.6% Y-o-Y growth.

Looking at key geographies in slide 37, in Karnataka region, our Center of Excellence performance in Q3 with revenue growth of 42.8% Y-o-Y. Center of Excellence ARPOB was INR 58,000 versus 49,000 in the corresponding quarter last year and 26.7% operating EBITDA margin. With respect to Gujarat region, we had a strong revenue growth in Q3 FY22 on a Y-o-Y basis with oncology revenue growing by 29.1% and the multispecialty revenue decreased by 17.5%. This was due to high COVID treatments in Q3 FY21 and we expect multispecialty to resume its growth of trajectory in the next few quarters. With respect to Maharashtra region, new centers grew by 62.5% Y-o-Y, South Mumbai BAU revenue continues to grow. For East India, existing centers' revenue grew by 32.5% Y-o-Y and expansion of revenue at new centers by 43.6% year on year. Cuttack is leading the regional revenue growth driven by Radiation and PET cases. In Andhra Pradesh, we have witnessed a strong revenue growth across the region. Vizag and Vijayawada delivered a growth of 36% and 21% Y-o-Y respectively.

Coming to slide No. 38, covering key highlights of Milann fertility business. Milann demonstrated good recovery in Q3 FY22 across all metrics. New centers' revenue grew by 23.9% Y-o-Y. There was a big improvement in digital traction as a result of continued efforts on our digital campaigns and with focus on strengthening clinical talent across Milann. Milann is looking to consolidate and focus on market leadership in Bengaluru and scaling up North Indian centers in near term for Milann going forward.

I would now like to draw your attention to slide 39. With respect to the CAPEX table, we have implemented judicious control measures with respect to both routine and growth CAPEX with most of our expansion completed. Total CAPEX for Q3 FY22 was INR 198 million which was largely with respect to the HCG existing centers. With respect to the net debt as on December 31st, total debt was INR 2,025 million which is a reduction compared to the previous quarter of INR 2,268 million.

I would now like to hand over the call back to Diwakar please.

Moderator: We will now begin the question & answer session. Ladies and gentlemen, we will wait for a moment while the question queue assembles. The first question is from the line of Rishabh Parekh from Sunidhi Securities. Please go ahead.

Rishabh Parekh: Congratulations on a very robust set of numbers. I had a couple of questions. One is, all our existing centers, we have already reached a revenue run rate of about 25%. Going forward, what could be the growth that can come from our existing centers? Also, on the margins, we have already reached about 20% to 21% operating EBITDA in existing centers. How can these expand further?

Raj Gore: Rishabh, in our existing centers, we are expecting higher than oncology market growth. The oncology market is growing about 11%. We are expecting about 12% to 14% growth going forward in our existing centers.

Rishabh Parekh: And the question on EBITDA; we are already about 20% to 21% operating EBITDA on our existing centers. With this kind of 15 odd percent of growth that you guided for, can this go up to 23% to 24% over the next couple of years?

Raj Gore: Yes, absolutely. Our Center of Excellence is already clocking 26% EBITDA margin. Even if you look at our investor deck, on regional highlights, our Karnataka region is delivering 26%. As all other centers start ramping up, I think that's the current gap and I am sure it will lift as new centers start ramping up and increasing their EBITDA margins which is positive now and every quarter it is increasing. As that picks up, the scale of new center picks up, automatically the overall EBITDA margin of the organization will keep going up.

Rishabh Parekh: My second question is on the regional split of revenue and operating EBITDA. Maharashtra and East India are the 2 regions where our operating EBITDA is lower than the Company average. Just wanted to understand by what time frame can this be expected to be at about 20 odd percent and why is East India in particular at about 12% to 13%?

Raj Gore: Both these regions, if you consider Maharashtra, you have 3 new centers. If you take East India, you have Kolkata which is our newest center. Because new centers being a significant chunk of this portfolio, I think that's where it's pulling down the EBITDA margin. I think, as more revenue growth starts happening in these centers, their revenue share of the total HCG revenue will start going up. Also, another interesting factor is these two are big cities, these are metro markets. So, we are expecting our quality of revenue or realization better in these 2 cities than many of other non-Tier-1 cities. There is also an opportunity for us to get international business in Mumbai as well as Kolkata. As a combination of all these potential opportunities, we are confident that not only revenue growth but ARPOB realization as well as EBITDA margin realization will be higher in both these markets in the coming years.

Rishabh Parekh: My last question is on the international business actually. If you could quantify how much lower it is as a percentage of our pre-COVID level? Secondly, steady state FY23 once international business hits pre-COVID level, what could be our ARPOB going forward?

Raj Gore: With every subsequent quarter this year, the international business was picking up but again the COVID wave 3 has put an arrest to it. We are expecting to close this year's international business at about 65% to 70% pre-COVID level and we are hoping that this will be the last wave and we are geared with our marketing and sales activities and plans for these markets to drive international growth at a much faster rate going forward.

Rishabh Parekh: Our ARPOB is about Rs. 38,000. What could this be if we hit pre-COVID level international revenue?

Raj Gore: Usually, the ARPOB will be about 5% more on international patients compared to domestic cash.

Moderator: The next question is from the line of Ravi Lodhka, an individual investor. Please go ahead.

Ravi Lodhka: Sir, any update from Gurugram? What is the progress in Gurugram plan?

Dr. B. S. Ajaikumar: As I described in the beginning, as you know, Gurugram plan has been in the works for several years, but unfortunately due to the COVID situation and the local issues, we have not been able to complete it. Because of the long delay, we have decided to take a break and wait and not pursue the project at this time, but that does not mean we will not relook at this project in the future. At this time, we have decided not to pursue this project as of now. That is the decision the board has taken. As our CFO explained, we have made the necessary adjustment financials to that effect.

Ravi Lodhka: Sir, one more question. What is your update from the Strand? Whether you have completely exited from the business of the Strand or some stake is now also there?

Srinivas Raghavan: On Strand, as I explained last time, we were a 34% investor and when the offer was made, we decided to exit completely; take that 34% which was about Rs 160 crores and in turn we also took back our labs for which we paid Rs 75 crores. As has been indicated by Srini that we got Rs 80 crores and we also got our labs back. With this lab coming back, we are now further expanding particularly being with genomics and oncology, we are expanding in the genomics field – molecular diagnostic field – on our own and we do work with Strand's bioinformatics and together with biorepository and some R&D work. So, we see a significant potential in this area as we move forward.

Ravi Lodhka: Sir, I heard from your side that except Gurugram plan, our greenfield expansion or any other expansion is nearly closed for a few years. I want to know up to what time we are able to just focus on increased profitability and free cash flows?

Raj Gore: The thing is we are not focusing on any new projects now. We are focusing on consolidating all our existing business and that's the way we would like to go. Our strength is oncology, we will continue to focus on oncology. The business has been generating free cash flow in the last few quarters and that trajectory will continue in the future years as well.

Dr. B. S. Ajaikumar: As Srini said and as Raj also said, our focus now is to really look at our Mumbai centers. We have 2 centers in the prominent locations and we have Kolkata region, we have Jaipur, we have so many projects which can grow up significantly and reach an optimal steady growth. So, we feel as a board and our message is to really consolidate, use capacity utilization, make the assets sweat, and once that happens this year, then we will look at the projects.

Moderator: The next question is from the line of Shyam Srinivasan from Goldman Sachs. Please go ahead.

Shyam Srinivasan: When you talk about the long-term growth, you talk about the cancer market growing at 11%, we can grow faster. Looking at some of the quarterly numbers, we are doing much faster than that, right? Top of mind I don't know what the 2-year CAGR is, but is this something that is happening? Is it like pent-up demand in the last few quarters that is leading to much faster growth even at the existing centers?

Dr. B. S. Ajaikumar: I think what is happening, Shyam, is, as you know, one of the theories is because of the COVID period, the footfall from cancer patients may have decreased elsewhere all over, but HCG being in the leadership position, we saw very minimal decrease in the footfall, but certainly, now it is increasing. Maybe patients waited, maybe now with more awareness about healthcare, they are seeking now centers of excellence, dedicated oncology centers, and also some reorganization is happening where HCG is very significant in Tier-2 and Tier-3 cities unlike a lot of other centers. And being dedicated, people instead of traveling to big cities going for oncology care, now they are beginning to come to the Tier-2 and Tier-3 cities. This is what is also maybe propelling the growth. We are collecting a lot of data on this, and once we complete the data and have a more clear visibility, we will certainly talk about it. The other issue is, also the mix is changing with high technology with a technology like CyberKnife and few other things like digital technology, we are seeing also increased growth because of the average recovery is also increasing. All of this is adding to this kind of growth.

Shyam Srinivasan: Dr. Ajai, if that is the case, then why can't we be a little bit more optimistic? Is it the worry that say fiscal 23 or 24 things normalize or you are worried from a more competitive standpoint that all the other multispecialty hospitals are talking about it? Is that where the conservativeness is in terms of trying to guide?

Dr. B. S. Ajaikumar: Shyam, I think honestly we are optimistic. And as you know, in the past, COVID came, other things, a little bit of these issues were there, but we are very optimistic in terms of future in cancer care. As you know, cancer care has evolved to such a high level and people are living longer. When people get recurrence, they keep coming back and because of the longevity, there is no question and the cancer cases itself are increasing across the nation and we are nearly serving by one account accessible for nearly Rs 53 crores. And as we move forward, I think we are very optimistic. We hope the cancer if it becomes less. Obviously, as a human being, we want that. Unfortunately, cancer will increase. With the quality of care and with the leadership role, we are very optimistic about the future.

Shyam Srinivasan: Last question from me, capital allocation. As you are generating the cash and EBITDA margin is now 20% to 21%, what are the priorities for us? You said you are not doing projects but just if I could understand the usage of the cash, what is the CAPEX requirement that we have maintenance such as this, how are you going to deploy this cash?

Srinivas Raghavan: The idea is to generate cash, use that cash to invest in revenue-generating assets. As I mentioned it here, our focus is on consolidation and revenue-driven growth. So, we will use this cash to focus on revenue-generating assets and that's the way we will work for the next foreseeable future.

Shyam Srinivasan: Srini, how is this cash being used? Is there any forward thing that you want to share? Or is it just only organic growth and there is no bed growth at all?

Raj Gore: There are 2 or 3 verticals. One is, of course, replacement CAPEX which is always there. The second like what Srini said is about revenue generating. We look at the mix. For example, in radiation oncology, as you know, there are higher and higher technology equipment's coming. If you look at the CyberKnife, average recovery is much higher compared to 3D-CRT and IMRT. And more and more treatment is moving towards IMRT, IGRT, and radiosurgery. In future, hypofractionated radiosurgery will come. So, we will use to CAPEX to obviously acquire these revenue-generating units. Also, in terms of medical oncology, obviously talent is very important. We have tumor boards. Talent acquisition is also important because what makes a good center is not only technology but medical talent. So, we will be using that also for the future growth. And that has shown in the past clearly where you acquire medical talent, the revenue definitely increases.

Dr. B. S. Ajaikumar: And we have a big training program. With that, internally we will have a lot of talent generated, be it doctors or nurses. Of course, in future, we will look at inorganic M&A at appropriate time, but we are in the process of consolidation. As Srini said, as our cash reserve increases, we will look at appropriate M&A also. At this point, we are not looking at any greenfield projects.

Moderator: The next question is from the line of Kaustubh Pawaskar from Sharekhan. Please go ahead.

Kaustubh Pawaskar: Congrats for a great set of numbers. Sir, I have a couple of questions. First, in your initial comments, you mentioned about a digital platform for patient acquisition. Now, you are almost acquiring around 1 lakh patients per annum. How will this digital platform help you to increase patient addition in the coming years?

Raj Gore: At least my personal experience is that any cancer patient that I have come across in the last few years, they have done 2 things. One, they have gone online and tried to learn more about their condition. And second, they have gone online and searched for if there is a better treatment option available and gone for a second opinion. Now, for our Center of Excellence, the kind of clinical services that we have, we feel that geography is not a boundary for us. And you know from personal experiences that when someone gets diagnosed with cancer, this is one condition where patients are willing to travel across cities, across states, across countries. So, we feel that there is an opportunity for us to create brand awareness, create awareness about HCG's specialized cancer care, our research academic's achievements through online, and create a funnel of leads. And with this digital platform what we aim to achieve is create awareness, create leads, convert those leads to make them a purchase decision, and then make sure that you stay in touch with them because once a cancer patient, you always have a concern of recurrence throughout their lifetime. So, you have to make the patient come back, do follow up checkups, make sure that they are cancer-free or you diagnose the recurrence as soon as possible if it is there. What this capability offers us is that we can stay in touch with our patients, follow up with them, and capture the lifetime value of the patient as a healthcare provider. I think, for us, we believe that will give us a clear edge especially because we are in cancer care going forward to drive volumes.

This is the capability that once we develop, the advantage of it is something that the Bengaluru unit can use or Ahmedabad unit can use; we can use it within Karnataka, within our existing markets, anywhere. We can target the patients who are interested in knowing more and getting better treatment anywhere in India or worldwide because the capability is same, the platform is same, and the approach to create awareness and create lead is same across anywhere in the world.

Dr. B. S. Ajaikumar: Also, Kaustubh, one point I want to add. Obviously, like what Raj said, the international funnel as well will happen, but you raised a question if you have 100,000 patients already, with the digital, what will be the impact. I think, as Raj explained, I just want to add, when you look at India and you look at people who access technology and all could be around 300-350 million people which is about 28% to 30% which is a large population as big as the United States. And we are covering 100,000. If you look at what should be the population we should still reach is about one-third of approximately 1.2 billion which comes to over 500 to 600 million. Obviously, we have a lot of ways to go. I think this digital platform hopefully will reach us, like Shyam said, be optimistic, reach us to 500,000. Why not? That could be our goal. We hope we can do this through…. one of the areas could be digital.

Kaustubh Pawaskar: Sir, my related question is, in Tier-2 and Tier-3 towns, there is a lot of hesitancy about consulting with doctors about the cancer or any particular disease they have. In that context, how are you trying to increase your awareness into Tier-2 and Tier-3 towns? Because as per your vision, you want to spread well into India and that is the biggest opportunity for you. And Tier-2 and Tier-3 towns are obviously a very big opportunity because still the penetration over there is very small. Considering that, how are you looking to improve your awareness over there?

Raj Gore: Kaustubh, as you know, one of the things that we take pride in at HCG is that 60% of our centers are in Tier-2 and Tier-3 cities. 1) While everyone else is focusing on big cities, we are actually addressing the need in real Bharat where the disparity and the demand/supply gap is even larger. 2) I think the digital play doesn't change, instead, if you look at the the consumption of digital services in Tier-2 and Tier-3 cities is actually growing at a faster rate whether it is data consumption, whether it is video consumption, or vernacular content. Therefore, I don't think there is any opportunity difference between Tier-1 cities and Tier-2 cities. In fact, our presence in Tier-2 cities gives us a combination of digital plus physical to actually deliver that service. However, I think, through our platform, what we aim to do is have the capability to do virtual consults and have the capability to deliver second opinions through patient apps. In fact, one of the things you will be…. I don't know if you were on the call last time. We have today capability to help a surgeon in Tier-2 and Tier-3 cities through a virtual reality Microsoft technology where our experts in our Center of Excellence can actually be present in the OT in Tier-2 and Tier-3 cities as a digital avatar and actually specifically guide on specific surgical technique in a complicated case and we have actually done it in reality. The possibilities are immense. The applicability and need in Tier-2 and Tier-3 cities is even larger and we have a large presence there and therefore we feel we are well poised to actually capitalize on that opportunity.

Moderator: The next question is from the line of Anurag Jain from Green Lantern Capital. Please go ahead.

Anurag Jain: Two very simple questions. I essentially wanted to understand on a steady state basis, when new centers also reach an optimum level of occupancy and utilization, what can be the margins for the Company? Also, I wanted to understand what is the optimum level of occupancy? I see that the cancer-focused hospital can achieve? And is it very different from a multispecialty kind of setup?

Raj Gore: I think the best way to answer your margin query is what we have been able to demonstrate in big cities in our Center of Excellence. 1) Whether it is Bengaluru or whether it is Ahmedabad, we have consistently delivered margins higher than 25% at a steady state. This is our track record and it speaks for itself. 2) The oncology hospitals are different in many ways from multispecialty hospitals. If you look at broad verticals in oncology, one is the outpatient and diagnostic vertical and then there is medical oncology which is chemotherapy, radiation oncology, and surgical oncology. Outpatient and diagnostic is purely indifferent to beds because it's purely outpatient. Chemotherapy (medical oncology) and radiation is daycare. The only specialty which we probably regularly use overnight beds is surgical oncology, and therefore, our dependence on bed occupancy or our focus on bed occupancy is not as much as multispecialty hospitals. However, you would be happy to know that quarter 3 which is considered usually a lower quarter in terms of seasonality in healthcare, we have been able to deliver our highest occupancy for the quarter without COVID. So, we focus more on utilization parameters across radiation and medical oncology. However, we are still driving occupancy ramp-up in our hospitals.

Anurag Jain: So, the question I want to come down to is, by when do we start seeing the true potential of your franchise? New centers for example, by when do you think they reach the steady state margins that the COEs are delivering today?

Raj Gore: If you look at our new center bucket, we were in a negative territory last quarter of last financial year. We reduced that in the 1st quarter. Second quarter we reached about 2.5% to 2.7% positive EBITDA. Last quarter, we were at 6 plus percent of EBITDA. So, we are on the right track. Most of our centers in the new bucket are EBITDA positive. It's only Kolkata that is still in the phase of ramping up. We are confident that in the coming year, we will get that to a positive territory.

Anurag Jain: Progressively, quarter after quarter, you should keep on seeing this improvement on this.

Raj Gore: Quarter 2 was 2.5% new centers, quarter 3 was 6.3%. So, you can do the calculation.

Moderator: The next question is from the line of Ankit Agrawal from Yellowstone Equity. Please go ahead.

Ankit Agrawal: My first question is what is the annual run rate of CAPEX we can expect given the replacement and upgradation requirements you talked about?

Srinivas Raghavan: While our intention is to consolidate and invest in revenue-generating assets and strengthening our existing centers, typically we do not give any forward guidance on this matter.

Ankit Agrawal: But is it fair to say that on a ballpark basis it will be around the same number that we did for this quarter?

Srinivas Raghavan: I would prefer not to comment on this particular point, but to reiterate, it is going to be on assets that will earn revenue for the business.

Raj Gore: As you know, there is replacement as we said as well as revenue generating and the reason also we cannot comment is obviously in the last 2 years, COVID and other issues the CAPEX and now could be different. So, as Srini said, it will be mostly replacement and also revenue-generating CAPEX.

Srinivas Raghavan: Our ideology is to kind of earn the money and spend the money and we don't intend to borrow the money.

Ankit Agrawal: The second question is on the impairment related to the Gurugram project. The 47 crore number sounds a big high. Could you give a rough breakup of what it comprises of? Is it mostly lease termination cost or something else?

Raj Gore: We have already incurred about Rs 40 crores of it in terms of civil construction under TUF. The balance is on account of the future rentals and some committed costs. That's how it is coming to Rs 47 crores. We incurred everything – current and what we would incur for the next 2 years.

Ankit Agrawal: So, it's mostly construction cost, I think, that the construction had already been done towards that.

Srinivas Raghavan: Yes.

Moderator: The next question is from the line of Bhagwan Chodhary from Sunidhi Securities. Please go ahead.

Bhagwan Chodhary: Sir, can you explain this decline in revenue in the Maharashtra region given the fact that the higher occupancy on sequential basis?

Raj Gore: As a business as usual, Maharashtra revenue is growing. I think the decline that you see is the difference in vaccination revenue that happened between Q2 and Q3. You know that vaccination had slowed down because most of the population in bigger cities are doubly vaccinated. That's the difference that you can show. Business as usual continues to grow in Maharashtra quarter on quarter.

Bhagwan Chodhary: The reason for decline in ARPOB on the sequential basis because last time I think you mentioned that ARPOB is not included in any vaccination business.

Raj Gore: The same thing. The vaccination revenue is an add-on on ARPOB, right? As that declines, the ARPOB comes down. There is no patient admission on that.

Bhagwan Chodhary: Secondly, can you just put a comment on your cash flow in the quarter? I think there was some cash flow received from the warrants and some in the acquisition of Suchirayu. Was there any other…. I think there was Rs 19 to 20 crores CAPEX as well.

Srinivas Raghavan: Yes, we did receive money from warrants to the tune of Rs 130 crores. As I explained earlier, we did acquire Suchirayu, increased our stake in Suchirayu by close to 80%. When we acquired it, it came with Rs 100 crores of loan as well. So, kind of net-net, 130 and 100. Net cash inflow is about Rs 30 crores basically which is shown in the corporate action. I think that's broad math.

Bhagwan Chodhary: And all the operating cash flow went into the CAPEX side and reduction in that?

Srinivas Raghavan: Exactly. What has happened is, I have generated free cash flow which has kind of helped to pay out my principal and interest and as well as my CAPEX. Post that, I have generated a free cash flow.

Moderator: The next question is from the line of Rajat Srivastava from Incred AMC. Please go ahead.

Rajat Srivastava: Sir, just one bookkeeping question. Your employee expenses seem to have grown by around Rs 6 crores on a sequential basis. Just want to understand, is this the ESOP charge or is this because of the consolidation of the Suchirayu Hospital.

Srinivas Raghavan: Yes, it is largely on account of the ESOP cost basically plus we have added some key staff in the key positions that has contributed to that. And the third point is, we divested our stake in Strand and took back all the labs. Those costs are also getting added to the employee cost numbers.

Rajat Srivastava: Sir, on your long-term vision on the Milann business. You have already divested the Strand business, but what would be your strategy on the Milann business going forward? If you can talk a bit about that?

Dr. B. S. Ajaikumar: We are definitely looking at the growth of Milann which has turned around. And as I indicated last time, we have reorganized the people who are also going to manage with Shailesh Guntu there and we are looking at adding more medical talent. Also, obviously, COVID had disrupted. So, post COVID, I think, there is a huge growth opportunity for Milann. We have also included some mother and child within the system. With all this, I think there is a significant growth which is going to happen in the next 2 years. That is our plan for the next 2 years.

Rajat Srivastava: Sir, in the numbers reported, there is 1-1/2 months of the Suchirayu Hospital sale. Am I right?

Srinivas Raghavan: Yes, you are right. We acquired that nearly 78% now.

Rajat Srivastava: If I exclude that sales from the hospital revenue, on a quarter-on-quarter basis, we have actually seen a decline in sales. Is that right? And that is due to the seasonality effect as you have mentioned earlier.

Srinivas Raghavan: The thing is it doesn't demonstrate any decline in the revenue if you exclude Suchirayu. In fact, steady and that is the way it will go.

Moderator: The next question is from the line of Vicky Patel, an individual investor. Please go ahead.

Vicky Patel: Sir, my question is on debt. When will we become debt-free?

Srinivas Raghavan: I think we go back to history. We have come down from Rs 650 crores of debt to about close to Rs 200 crores of debt today. As we keep generating free cash flow, we will balance between debt reduction and investment and assets. That's the way we will go about. Keeping that in mind, we will have a very small debt, but we will do what is right for the business on a total basis. However, if you see on a debt-to-EBITDA basis at a pre Ind-AS level, at an Ind-AS level also, we are at about 2-1/2 times to debt to EBITDA at an Ind-AS level. This is a very good number as far as the market is concerned.

Moderator: The next question is from the line of Arpit Singh, an individual investor. Please go ahead.

Arpit Singh: I had a couple of questions. When I was looking at the quarter-on-quarter growth, I could see that Gujarat as a market has not grown for HCG when I look at the growth both for quarter on quarter and year on year. Is there anything particular happening there? Because other markets have grown very well.

Raj Gore: In the Gujarat region, we have 3 multispecialty hospitals. Last year same quarter, COVID wave 1 was strong. We had COVID patient admissions, and therefore, occupancy was higher. This year, we do not have that and that's the difference.

Dr. B.S. Ajaikumar: In fact, our oncology has grown significantly as we see there.

Arpit Singh: The Ahmedabad oncology has grown significantly?

Raj Gore: Yes. Our core business or business as usual is growing strongly.

Arpit Singh: But the multispecialty revenues have gone down. You were saying that is because this is excluding COVID?

Raj Gore: Yes.

Arpit Singh: So, going forward, is it fair to assume that this will be the run rate because going forward you would not see any COVID revenues?

Raj Gore: Yes, in this COVID wave 3, there have hardly been any admissions. So, we don't expect any. At least you shouldn't predict or forecast on this pandemic, but knowing the experience of wave 3 where the admissions have been really less, we don't anticipate it to change in the future. Let us hope that it doesn't change.

Arpit Singh: And for Andhra Pradesh market also, your occupancy has gone down similar to Gujarat. Is that also because of COVID you saw higher occupancy?

Raj Gore: Earlier, in Andhra, we had a significant government scheme business. With the government scheme business, you need to provide dormitory facilities to these patients. We used to earlier count that. Now we do not count that as our occupancy because they are not really patients. It's more of a stay facility. So, we started excluding dormitory stay from our occupancy count. It's a government requirement. We were mandated to fulfill it. But it is not really patient bed occupancy. So, we have started excluding it.

Arpit Singh: My third question is on the ARPOB number. Again, ARPOB for Gujarat and Andhra Pradesh have risen very highly and for Karnataka also, it is high. Are you expecting that going forward also, these numbers will continue or is this because of the pent-up demand?

Raj Gore: Both in Gujarat as well as Andhra Pradesh, I just explained the reason for higher occupancy in the last year's quarter. As the occupancy goes down, automatically ARPOB goes up. That's the reason there is a significant rise. But we expect it because this is a normalized ARPOB in the current quarter. We expect it to sustain. In fact, we will keep working on improving it through the better pair mix and a higher revenue realization by delivering high-end treatments.

Moderator: The next question is from the line of Mayur Parkeria from Wealth Managers. Please go ahead.

Mayur Parkeria: Sir, firstly, my sincere apologies because in case I ask a very simple and basic question, I do not have a very great insight. I have started just looking recently. So, if there is a very basic question, my apologies. The question is, sir, when I look at the Tier-2 and Tier-3 focus which you have been mentioning along the call in the opening remarks as well as in the presentation which is

60%, a question comes on mind is, organized oncology treatment and care anyways is on the rise now over the last couple of years, and even Tier-1, there is a lack of so much understanding and I will say not less but there is less…. I am saying purely from the point of view of penetration and understanding and visibility. On what basis have we chosen to be in Tier-2 and Tier-3 cities rather than some of the large cities? I see in Nashik, you have so many beds, and in Cuttack, the presence of beds is so high. Why not in Tier-1 or larger cities? Is it because of the presence of the organized Apollos and the Maxis of the world here or is it for some other reasons?

Dr. B. S. Ajaikumar: I would like to answer this because when we started HCG, the entire model of hub and spoke model was using the hubs in the main cities and spokes in the Tier-2 and Tier-3 cities. As you know, Mayur, as an oncologist, oncology is a very complicated treatment. For a lot of people, affordability or accessibility was the problem all the time. So, the model was created on that – how do you make it when people don't have to travel to big cities? Even in Cuttack or Nashik, we have PET scan, we have high-end linear accelerator and use the technology too and talent pool is there, why would anybody like to go? That is the reason we chose because Indian population, as you know, is widely distributed and majority is not in the Tier-1 cities. This is the concept. But we did have major cities like Bengaluru or Kolkata now or Ahmedabad or Mumbai, we are in these and we are the leaders in these centers. Bengaluru for example and Ahmedabad, we are the leaders. We are not afraid of any Apollos and all. In fact, they are afraid of us, honestly. That is the reason. Because we control so many patients and our market share in Bengaluru and Ahmedabad is very high. Among all the centers, we have the majority. We have No. 1 market share. But our model is that hub and spoke model. Look at in COVID period, what happened? Majority of the people could not travel. Where would they get cancer treatment? They came to HCG centers in Tier-2 and Tier-3 cities. So, we reorganized and came. That is how our flow into Tier-2 and Tier-3 increased. That served our purpose of serving the people who needed it at their home locations. My philosophy has always been, as a founder, to make sure patients take treatment, go home, and sleep in their own beds. And that is what I think potentially we have achieved with this kind of model and this has been a very successful model, as you can see from the numbers.

Raj Gore: Mayur, out of 18 cities, in 13 cities, we have No. 1 market share in oncology. I think the way to look at it is HCG has a business model that does very well in big cities as well as in smaller cities and that's the uniqueness of our model and that's what differentiates us. And our margins – Bengaluru is about 25% to 26% but even in Tier-2 and Tier-3 cities like Cuttack, we are 25% plus. So, irrespective of the location, our model we have ability to deliver higher margins and better returns.

Mayur Parkeria: In these Tier-2 and Tier-2 cities, is it mainly focused on diagnostics alone or all the services are being offered there?

Dr. B. S. Ajaikumar: Mayur, all of our Tier-2 and Tier-2 cities are all complete comprehensive cancer centers. That is why, during my talks, I always say our model is not replicable by others. In fact, globally also, nobody is like HCG network where it is actually comprehensive cancer centers across India in Tier-2 and Tier-2 cities. They have linear accelerators, most of them have PET scan, but Center of Excellence may have like CyberKnife and bone marrow transplant. We are even trying to do all these there and 2 virtual Tumor Boards. We are connecting all these centers where even the expertise can be brought there like what Raj Gore reported like mixed reality. All of this is helping us to be the D-dominant oncology provider in this country. We do major surgeries in cities like Visakhapatnam, Vijayawada, or Cuttack – major surgeries, reconstruction surgeries, all the things are done across India because they are highly trained people and we work with them through this hub and spoke model.

Moderator: Ladies and gentlemen, due to time constraints, that was the last question for today. I now hand the conference over to the management for closing comments.

Raj Gore: Thank you to all the participants for joining in this call. In case you have any follow-on questions, you could write to us or Ashutosh@HCGEL.com and we would be happy to answer your questions. Hope that most of your questions were answered. We look forward to coming back to you with the full-year numbers and with more updates on as to how HCG is on the growth path. Thank you and have a good evening.

Moderator: On behalf of HealthCare Global Enterprises Limited, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.