

Financing New Hospital Projects

Apollo's experience



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15th June 2009
Hospital Build Middle East Conference
Dubai

Structure of the Presentation

Apollo Hospitals Group overview

Investing in Hospital Projects

Capital structuring decisions

Metrics to watch

Case studies



Health should be seen as an integral part of the development agenda. There is, first of all, the basic recognition that deprivation of health is an aspect of underdevelopment. Just as for the individual, not having medical treatment for curable ailments constitutes poverty, similarly, for a country, not having adequate health arrangements is a part of underdevelopment. So you have to place the issue of health care right at the center of the development agenda

Noble Laurette Amartya Sen



Apollo Hospitals Group is a leading global healthcare player

- The largest hospital group in Asia with over 43 tertiary and secondary care hospitals, over 8,000 beds in India and abroad
- Listed on NSE, BSE and Luxembourg stock exchange
- Market capitalization of approximately US\$ 700 million
- Largest private sector employer of medical professionals
- Tertiary care services, high volumes and international standard outcomes
- International partnerships with John Hopkins Medicine, Cleveland Clinic, MD Anderson Cancer Centre, Kings College and others



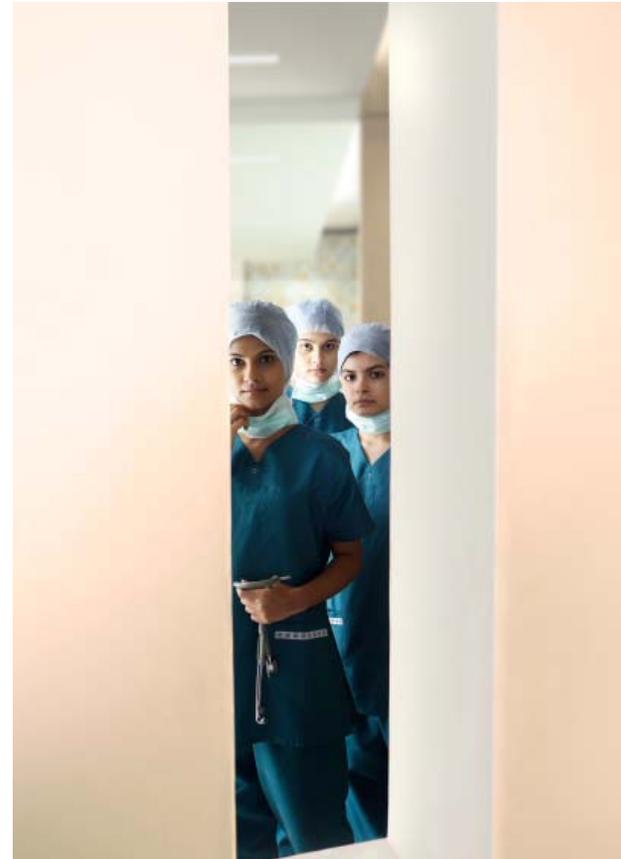
We have continuously expanded presence and strengthened the delivery model

Parameters	1983	2009	2014 (E)
No of Hospitals	1	43	>65
No of beds	150	8,000	>14,000
Shareholders	~10,000	~25,000 (foreign investors hold over 50% of the company)	
No of employees	350	~50,000	>75,000
No of doctors	200	~4,000	>6,000

Gained significant knowledge in financing, commissioning and managing hospitals globally. We are now extending our expertise to hospitals across the globe

Key prerequisites for investing in Hospitals

- Population support for the focus clinical services
 - Population within 30 minute commuting distance should be able to provide 80% utilization rate
 - Disease incidence and morbidity patterns
- Ability to source medical professionals
 - Doctors, nurses and other professionals at sustainable compensation levels. HR costs excluding doctor compensation should be <22%
- Need gap analysis
 - Competition analysis with a view to avoiding over capacity in any specialization
- Affordability
 - Willingness to pay should exist
 - Insurance penetration
- Credibility and brand of the hospital

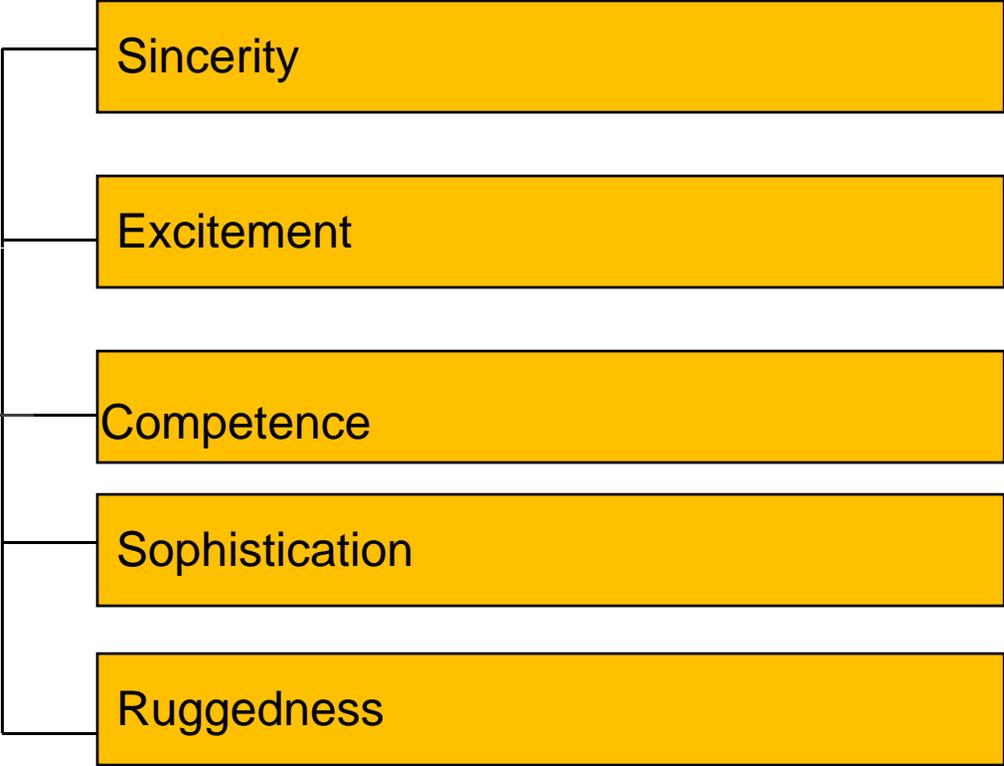


Dimensions of brand personality

Attracts good manpower, patients and better bargaining power



Apollo
Brand
personality



Brand has become a competitive advantage for Apollo and gives an edge to attract top notch talent, competitive prices from vendors and more importantly be the top of the mind recall for all healthcare needs

Tertiary care hospitals

Typical characteristics

Land area	4-6 acres
Bed strength	200-400 beds
Departments	Cardiothoracic surgery, Neurosurgery, Orthopedics, Oncology, Radiology and Imaging and others (3-4 focus clinical areas)
Major equipment	3 t MRI, 64 Slice CT, cathlab, 4D Ultrasound, Tread mill
No of Operation Theatres	8-12
Consultation rooms	~30
OP: IP revenues ratio	30:70
Cash breakeven	Year 2



Secondary care hospitals

Typical characteristics

Land area	2-4 acres
Bed strength	100-200 beds
Departments	Cardiology, Orthopedics, OBG, General surgery, Radiology and Imaging and others
Major equipment	6 Slice CT, Ultrasound, Tread mill,
No of Operation Theatres	3-5
Consultation rooms	~15
OP:IP ratio	30:70
Cash breakeven	Year 1



Project cost components

Component	% of the capital cost
Land	5-10%
Building	30-40%
Medical equipment	30-40%
Preoperative and preliminary expenses	10-15%
Margin money (start up expenses, cash losses, others)	10%
Contingency	5-10%

Important to optimize the area per bed and technology investment to keep the capital costs low and also to ensure optimal operational costs as wrong planning can lead to significant negative impact during hospital operations



Possible financial models to optimize the capital requirements

- Real Estate Investment Trusts (REIT)
 - Land and building are funded by a separate entity (Property co), leading to a reduction of ~50% in project cost
 - Hospital operator can focus on core competencies and invest capital in their area of competence i.e., operations
- Public private partnership
 - Land at concessional rate
 - Utilize existing public infrastructure (private wings in public hospitals)
- Equipment lease
 - Many technology companies offer equipment on lease
 - Given the high rate of obsolescence this options provides the flexibility to upgrade the equipment for newer technologies
 - Lease costs, agreements with supplier regarding consumables supply, maintenance contracts and other terms should be carefully evaluated before deciding on the lease option



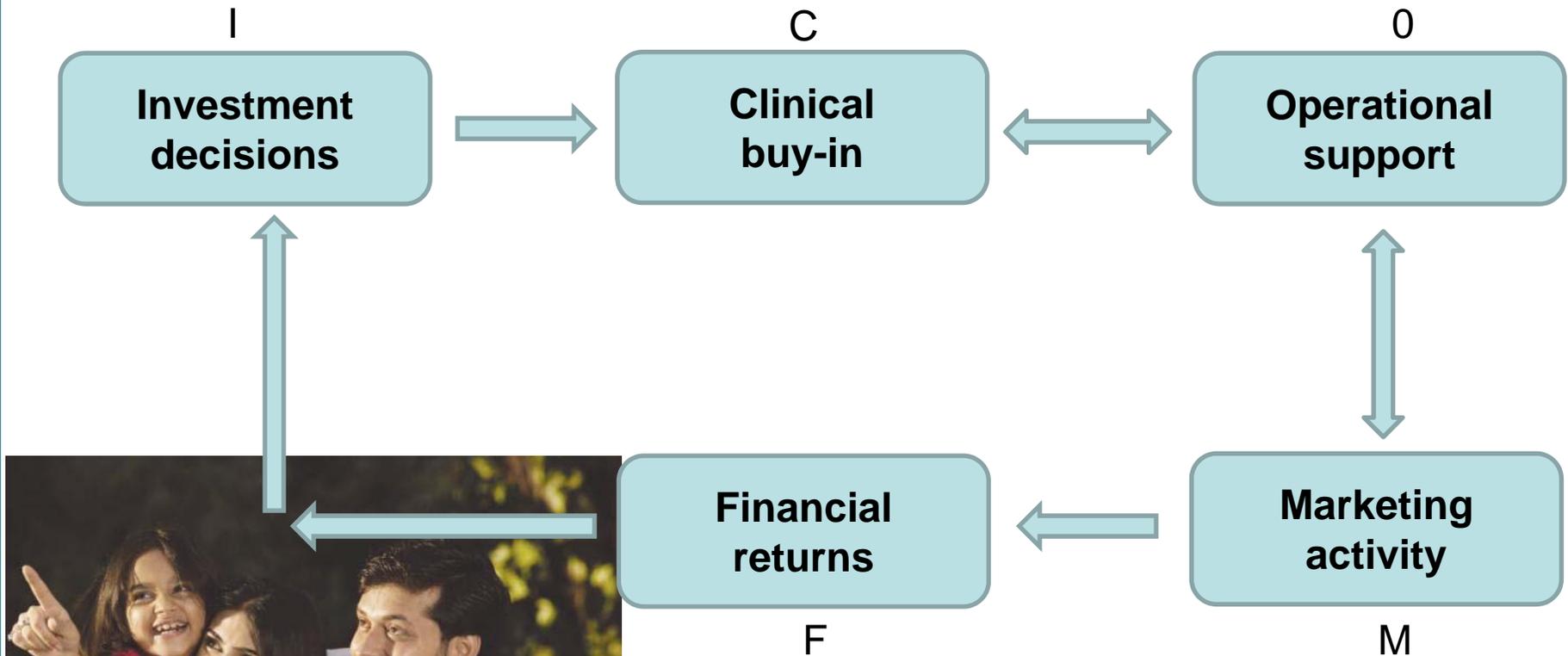
Capital cost per bed*

Facility type	Large cities	Medium cities	Small cities
Tertiary care (200-400 beds)	\$120k- \$200k	\$100k-\$140k	\$70k-\$100k
Secondary care (100-200 beds)	\$80k - \$100k	\$60k-\$80k	\$50k-\$80k
Primary care (Investment per center)	\$500,000	\$300,000	\$200,000



*Figures are based on experience in India and other emerging markets

“ICMOF” cycle / circuit



Profit and loss behavior (steady state)

Description	Value (%)
Income value	100
Materials & other variable costs	35
Gross margin	65
Salaries, wages & benefits (SWB)*	20
Administrative exp.	15
EBIDTA	30

*Salary costs exclude doctors compensation

Business and financial risk

- Higher business risk projects should follow low financial risk (more equity) and vice versa
- Business risk defined as operating leverage and assessed by the level of fixed costs in the business relative to contribution ($OL = \text{Contribution} / \text{EBIT}$)
- Financial risk defined as financial leverage and assessed by level of debt in the capital structure ($FL = \text{EBIT} / \text{EBT}$)
- Total risk defined as operating leverage x financial leverage (contribution/EBT)
- Expectation of the investor including currency fluctuations have a major bearing on the decision to invest and managing expectations is a key factor
- Credibility and reputation is earned by a track record of delivering on promises



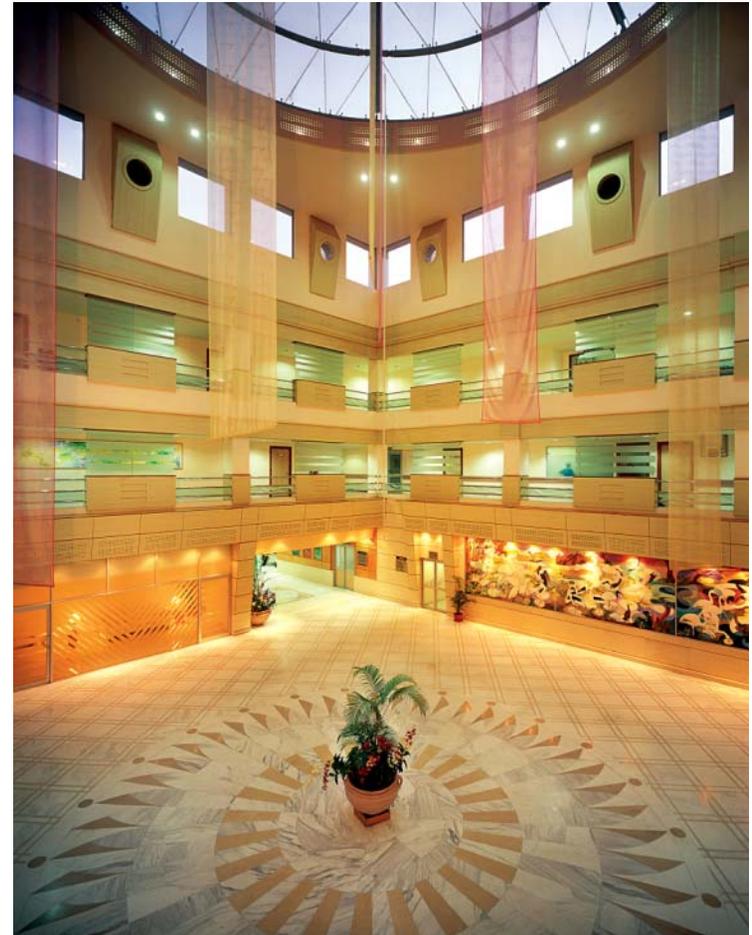
Capital structuring

- Capital structuring decisions are dependant on the assessment of business risk
- More equity is required for projects having higher risk reward ratios
- More debt is tolerated for projects having lower risk reward profiles
- Equity is the costliest form of financing with investors demanding CAGR of 25% and more for a 3-5 year horizon - the higher the perceived risk the higher the return demanded, so normally green field projects have a higher required return compared to brown field projects with positive EBIDTA
- Debt has maturities ranging from 5- 10 years and it is important to synchronize cash flows in the capital structuring with the cash flow signature of the project cash flows
- Debt has typical covenants on liquidity, security, and serviceability
- Working capital management is often ignored leading to considerable distress



Apollo Hospitals, Colombo

- Super specialty hospital, 350 beds
- Project cost – SLR 2.6 billion
- Conservative financing
 - Equity 1.6 billion
 - Debt – 1 billion
- Business risk – High
- New business model to Colombo
- Availability of qualified medical professionals, administrative personnel
- Medical and nursing council approvals were required for foreign professionals, work permits
- Achieving top-line and contribution – A major challenge
- High fixed costs, therefore a low financial risk model was pursued to achieve a balanced risk portfolio



Apollo Hospitals, Kolkata

- Super specialty hospital, 350 beds
- Project cost – INR 120 crores
- Aggressive financing
 - Equity INR 200 million
 - Debt – INR 1000 million
- Business risk – Low
- Established and proven business model and characterized by high brand recall in Kolkata
- Excellent population support
- Readily availability of qualified medical professionals, administrative personnel
- Achieving top-line and contribution – Relatively easy
- Relatively low fixed costs, therefore pursued a aggressive financial risk model



Apollo Reach Hospitals

- **The concept**
 - Offer world-class healthcare to the tier 2 and tier 3 locations in India.
 - Reduce migration to metro cities
 - Reaching out to the rural population in Tier II & III level cities and towns as well as at District level.
 - No frills- functional model . Cost per bed 20-30% lesser than benchmarks
- **Drivers**
 - Non-availability of quality care at local primary and secondary care levels
 - Lack of technology absorption in Tier 1 and Tier II cities



Over 20
hospitals under
implementation



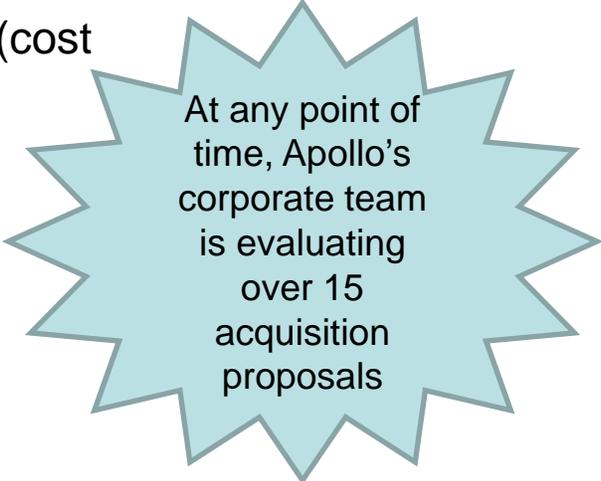
Acquisitions – What will make the mark

• Integration and Operational

- Location should complement our existing operations, political stability (country and regional)
- Bed :Manpower ratio- 1: 3.5, salary structure and skill sets
- Credibility of the hospital and the brand
- Case mix – do the services offered make a strategic fit for Apollo?
- Ability to modify the infrastructure to meet Apollo's standards and to add clinical service lines
- Cost per bed between US\$100,000 – US\$140,000 (cost of green field hospital as baseline benchmark)

• Financial

- EBIDTA % >25% if mature hospital
- Cost of debt
- Valuation of ~ 6 times EBIDTA
- RoCE > 22%



At any point of time, Apollo's corporate team is evaluating over 15 acquisition proposals



Clinical, Operating and Financial (COF) metrics

Sample metrics

Clinical

- ALOS
- Mortality rate
- ER to IP conversion
- Bed falls
- Ventilator acquired pneumonia

Operational

- Occupancy rates
- Manpower per occupied bed
- Material cost
- Procedure volumes
- Wait times for patients
- Throughput of key equipment

Financial

- Cost per bed
- Revenue per bed day
- EBIDTA%
- EBT%
- PAT%
- RoCE%
- RoE%
- Asset turnover ratio



"Most organizations, social movements, world records, new products or services, and remarkable achievements began as a figment of someone's imagination. Somebody had a thought that turned into a dream. That dream grew even as the dreamer was being ridiculed and told to "get real."

- from Jim Clemmer's article, "Yield of Dreams"





Discussion and questions..



Disclaimer

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