

METROPOLIS HEALTHCARE LIMITED

IPO Note

(SUBSCRIBE)

Analyst:

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IPO details

| Key Data | |
|--------------------------------|-------------------------|
| Issue Opens | 3-Apr-19 |
| Issue Closes | 5-Apr-19 |
| Equity Shares Offered (in mn.) | 13.70 |
| QIB | Up to 75% |
| NIB | Min 15% |
| Retail | Min 10% |
| Face Value (Rs.) | 2 |
| Price Band (Rs.) | 877-880 |
| Max. Issue Size (Rs. mn) | 12,056 |
| Lot Size (Eq. Shares) | 17 and multiple thereof |

| Valuation | @ Rs.877 per share | @ Rs.880 per share |
|-------------------------|--------------------|--------------------|
| Market Cap (₹ mn) | 44,007 | 44,157 |
| Net Debt (₹ mn) | -60 | -60 |
| Enterprise Value (₹ mn) | 43,947 | 44,098 |
| EV/ Sales | 68.3 | 68.5 |
| EV/ EBITDA | 251.3 | 4.8 |
| P/B | 2.0 | 2.0 |
| P/E | 42.6 | 42.7 |

Source: Red Herring Prospectus, Dealmoney Research

| | Pre Issue | | Post Issue^ | |
|----------------|-------------|----------------|-------------|---------------|
| | # mn Shares | % Holding | # mn Shares | % Holding |
| Promoters | 34.0 | 67.8% | 27.7 | 55.3% |
| Public | 16.2 | 32.2% | 8.7 | 17.4% |
| Offer for sale | | | 13.7 | 27.3% |
| Fresh Issue | | | 0.0 | 0.0% |
| Total | 50.2 | 100.00% | 50.2 | 100.0% |

Object of the issue

- To achieve the benefits of listing
- Enhance its visibility and brand image and provide liquidity to the Shareholders.
- MHL will not receive any proceeds from the Offer

Recommendation

The country's second largest diagnostics player by profits. The company is seeking to expand its presence in a large under-penetrated market which is dominated by smaller, unorganised players. The company has been utilising both organic and inorganic opportunities (15 acquisitions over 10 years) to grow its business. The company has also followed a strategy of concentrating on a few large cities with higher growth.

On valuation front, upper issue price at 42.7x FY18 earnings is fairly at par with its peers and can be looked for further growth on back of its robust growth for long term. Therefore we recommend **SUBSCRIBE** over the issue.

Leaders in west and south India..

- ❑ Metropolis Healthcare Limited (MHL) is one of the leading diagnostics companies in India, by revenue, as of March 31, 2018 (Source: Frost & Sullivan). It has widespread presence across 19 states in India, as of December 31, 2018, with leadership position in west and south India (Source: Frost & Sullivan).
- ❑ Through its widespread operational network, the company offers a comprehensive range of clinical laboratory tests and profiles, which are used for prediction, early detection, diagnostic screening, confirmation and/or monitoring of the disease.
- ❑ According to Frost & Sullivan, the Indian diagnostics market was valued at approximately ₹ 596 billion in the financial year 2018, and is projected to grow to approximately ₹ 802 billion by financial year 2020, driven by favorable changes in demographics, improvements in health awareness, increased spend on preventive care and wellness, increase in medical tourists, increase in lifestyle-related ailments and rising penetration of insurance in India.
- ❑ It has a broad range of approximately 3,487 clinical laboratory tests and 530 profiles, as of December 31, 2018. The profile comprises of a variety of test combinations which are specific to a disease or disorder as well as wellness profiles that are used for health and fitness screening.
- ❑ MHL classifies tests into:
 - I. 'routine' tests such as blood chemistry analyses, blood cell counts and urine examination;
 - II. 'semi-specialized' tests such as thyroid function tests, viral and bacterial cultures, histology, cytology and infectious disease tests
 - III. 'specialized' tests such as tests for coagulation studies, autoimmunity tests, cytogenetics and molecular diagnostics.
- ❑ The company conducts its operations through laboratory and service network. It has implemented a 'hub and spoke' model for quick and efficient delivery of services through the widespread laboratory and service network, which covers 197 cities in India, as of December 31, 2018.
- ❑ As of December 31, 2018, the laboratory network consists of 115 clinical laboratories, comprising (i) a global reference laboratory ("GRL") located in Mumbai, which is the main 'hub' and equipped to conduct majority of the tests offered by the company; (ii) 14 regional reference laboratories 57 ("RRLs") (out of which four are located outside India), which are equipped to conduct routine, semi-specialized and few specialized tests; (iii) 56 satellite laboratories (out of which one is located outside India), which are equipped to conduct routine and semi-specialized tests; and (iv) 44 express laboratories (out of which five are located outside India), which are equipped to conduct routine tests.

Source: Red Herring Prospectus, Dealmoney research

Strengths

- ❑ **One of the leading diagnostics companies in India which is well positioned to leverage the expected growth in the Indian diagnostics industry :** MHL is one of the leading diagnostics companies in India, by revenue, as of March 31, 2018 as per Frost & Sullivan. It has widespread presence across 19 states in India, as of December 31, 2018, with leadership position in west and south India according to the Frost & Sullivan. As of December 31, 2018, it has an operational network of 83 clinical laboratories, 1,473 patient touch points and 396 ARCs in west and south India. The company has a growing presence in north and east India, and clinical laboratories, patient touch points and ARCs have increased from 15, 25 and 59 as of March 31, 2016 to 22, 132 and 149, as of December 31, 2018, respectively. As of December 31, 2018, the operational network is spread across 197 cities in India. The widespread presence provides a hedge against the risks associated with any particular geography while benefitting from the competitive advantages of each location.
- ❑ **Widespread operational network, young patient touch point network and asset light growth of service network:** Its operations are supported by a laboratory network comprising of 115 clinical laboratories, including GRL and a service network comprising of (i) 1,631 patient touch points, including 256 Owned PSCs and 1,375 Third Party PSCs, which service the individual patients; and (ii) approximately 9,000 pick-up points and 552 ARCs, which service the institutional customers, as of December 31, 2018. the 'hub and spoke' model, whereby specimens are collected across multiple locations within a region for delivery to its clinical laboratories for diagnostic testing, provides greater economies of scale and enhances consistency of the testing procedures . In addition, it is able to leverage the widespread network of clinical laboratories to compete effectively with local diagnostic providers in each of the markets in which we operate.
- ❑ **Comprehensive test menu with wide range of clinical laboratory tests and profiles:** The company offers comprehensive range of approximately 3,487 clinical laboratory tests and 530 profiles to patients, as of December 31, 2018. The test menu includes pathology tests ranging from basic biochemistry and surgical pathology to cytogenetics and high-end molecular diagnostic tests. Besides pathology tests, some of the centers also offer non-pathology tests such as ECG, X-ray, ultrasound and stress tests. According to Frost & Sullivan, there has been a significant growth in demand of preventive health checkup in India, and to cater to this demand.
- ❑ **Strong and established brand with a focus on quality and customer service:** It has established a well-recognized brand by delivering quality and reliable diagnostic services since 1980. Over the years, it has received several awards that recognize the strength of its brand and the focus on offering superior diagnostic tests and services. The was rewarded for "excellence in customer service and delivery" by Biotrains in 2018, and also received special jury mention for "service excellence (diagnostic center)" by FICCI at the Healthcare Excellence Awards 2018.

Strengths

- ❑ **Robust Information Technology Infrastructure with Focus on Improving Efficiency :** The laboratory operations are supported by a cloud-based information technology platform, while rest of the operations are managed using a centralized SAP platform. The information technology system allows them to fully integrate and automate processes ranging from registration, bar-coding and billing of specimens to analysis and reporting of test results. The information technology system enables them to (i) achieve standardization across its operations; (ii) reduce incidence of errors due to human intervention; (iii) monitor technical operations; (iv) closely track the key performance metrics; and (v) provide convenience to the patients and customers, by allowing them to book appointments, complete registration and access test reports online. The information technology infrastructure is scalable and has been designed to support the growth of the business and help ensure reliability of the operations as well as the security of customer information.
- ❑ **Established track record of successful acquisition and integration in India and overseas :** it has a track record of acquiring and successfully integrating companies to grow its portfolio of laboratory and service network. It has acquired several companies since 2002, which includes established local chains such as Sudharma Metropolis Health Services Private Limited in Kerala and Golwilkar Metropolis Health Services (India) Private Limited in Pune as well as companies outside India.

Future road ahead

- ❑ **Continue to Focus on Organic Growth Initiatives to Expand the Reach:** The has developed a highly differentiated and focused growth strategy of dividing the key target cities in which it operate, i.e, focus cities, seeding cities and other key cities, on the basis of market share, the strength of brand, operational history, experience and the quality of the team. The channel resources in growing the market share within these geographies in order of their importance in growth strategy
- ❑ **Continues Focus on Providing Quality Tests and Services :** The quality and reliability of its tests and services are critical to its success. Its vision is to help doctors treat their patients better and its strategy is to take the following steps in this regard:
 - upgrading technology for better quality, efficiency and reliability;
 - consistent value addition to tests being offered; and
 - promoting disease and disorder specific profiles, to allow doctors to receive comprehensive view of the patient's disease status.

Further, the value added services, such as house calls, e-services, longer operating hours for patient touch points and call centers, and home delivery of test reports, make the services easier to use. It intends to continue to improve the value added services to make them more attractive for the existing as well as prospective patients. Also, the company also actively involved in campaigns focused on creating awareness of particular conditions such as cancer, lifestyle diseases, monsoon diseases, and the importance of periodic testing.

- ❑ **Focus on the Expansion of the Service Network:** the company is particularly focused on using the Third Party PSC model for expanding the geographical reach of the service network, due to its high scalability and limited capital expenditure involved. The Third Party PSCs include associate patient service centers ("APSCs") and standalone independent laboratories converted into Metropolis-branded patient service centers ("D-APSCs"). In recent years, MHL has successfully used the Third Party PSC model to grow the business and the total number of the APSCs and D-APSCs have grown from 41 as of March 31, 2016 to 408 as of December 31, 2018. These models enable the company to grow its revenue by providing management and branding to Third Party PSCs, while benefitting from the extension of its network and brand presence in key geographies .
- ❑ **Focus on Increasing its Business from Individual Patients:** Across the Focus Cities, it derived 47.8% of the revenue from operations from individual patients in the financial year 2018 as compared to 41.9% of the revenue from operations in the financial year 2016, representing a CAGR of 20.72%. During the nine months period ended December 31, 2018, the company derived 51.34% of its revenue from operations from individual patients.
- ❑ **Pursue New Avenues of Growth:** It intend to pursue several new avenues of growth, including growing in offering of test packages , pursuing scientific upselling of tests, participating in select Public-Private Partnership tenders and increase focus on contract research.

Source: Red Herring Prospectus, Dealmoney research

Peer Comparison

| Company Name | Net Sales | Profit After Tax | PBIDTM (%) | PATM (%) | ROE (%) | ROCE (%) | P/B(x) | PE (x) |
|-----------------------------|-----------|------------------|------------|----------|---------|----------|--------|--------|
| Metropolis Healthcare Ltd. | 643.6 | 109.7 | 28.4 | 17.1 | 29.8 | 44.3 | 2.0 | 42.7 |
| Dr. Lal Pathlabs Ltd. | 1,056.9 | 171.8 | 27.9 | 16.3 | 25.3 | 37.8 | 9.4 | 46.3 |
| Thyrocare Technologies Ltd. | 356.3 | 93.4 | 47.2 | 26.2 | 22.2 | 33.6 | 7.3 | 29.9 |

| Company Name | Domestic Presence | International Presence | No. of Centers | No. of Reference Laboratories |
|--------------------------------|-------------------|--|--|---|
| Dr. Lal PathLabs Limited | Pan-India | Bhutan, Sri Lanka, Myanmar, Malaysia, Tanzania, Nigeria, Saudi Arabia, Maldives, Ethiopia, Kenya, Ghana, Uganda, Qatar, Kuwait and UAE | Clinical Labs- 193 Patient service centers – 2,153 Pickup points - 5,624 | National: 1 at Delhi Regional: 1 at Kolkata |
| SRL Diagnostics | Pan-India | Dubai, Sri Lanka, Nepal, Congo, Africa, Middle-East, Hong-Kong, Maldives and SAARC countries | Clinical Labs- 364 Patient service centers – 1,078 Pickup points – 6,271 | Regional: 4 laboratories, each at Mumbai, Gurugram, Kolkata and Bengaluru. |
| Metropolis | Pan-India | Nepal, Nigeria, UAE, Oman, Ghana, Kenya, Zambia, Mauritius and Sri Lanka | Clinical Labs- 106 Patient service centers – 1,130 Pickup points – 8,500 | National: 1 at Mumbai Regional: 12 laboratories, each at Rajkot, Guwahati, Raipur, New Delhi, Surat, Bengaluru, Kochi, Pune, Chennai, Kolkata, Kenya and Sri Lanka. |
| Thyrocare Technologies Limited | Pan-India | Nepal, Bangladesh, Gulf | Authorized Service providers – 3,379 Collection points - over 30,000 | National: 1 at Navi Mumbai Regional: 8 laboratories, each at New Delhi, Mumbai, Patna, Kolkata, Bhopal, Hyderabad, Coimbatore and Bengaluru. |

Source: Red Herring Prospectus, Dealmoney Research

Consolidated Summary Financials

Income Statement

| ₹ mn | Mar-15 | Mar-16 | Mar-17 | Mar-18 |
|-------------------------|------------|------------|------------|------------|
| Total Income | 455 | 524 | 545 | 644 |
| Operating Expense | 337 | 388 | 391 | 469 |
| EBIDTA | 118 | 136 | 153 | 175 |
| Depreciation | 21 | 21 | 17 | 19 |
| Other Income | 6 | 22 | 26 | 8 |
| Finance Costs | 2 | 2 | 2 | 4 |
| PBT & (EI) | 101 | 136 | 160 | 160 |
| Exp Income | - | - | - | - |
| PBT | 101 | 136 | 160 | 160 |
| Tax | 33 | 46 | 53 | 51 |
| PAT | 68 | 90 | 107 | 110 |
| Less : Minority Intrest | (7) | (8) | - | - |
| Share of Associate | - | - | (6) | (7) |
| Net Profit | 61 | 81 | 107 | 110 |

| ₹ mn | Mar-15 | Mar-16 | Mar-17 | Mar-18 |
|---------------|--------|--------|--------|--------|
| EBIDTA Margin | 25.8% | 26.0% | 28.2% | 27.2% |
| Net Margin | 13.4% | 15.5% | 19.7% | 17.1% |
| ROE | 18.8% | 26.2% | 36.5% | 29.8% |
| ROCE | 27.5% | 40.1% | 54.3% | 44.3% |

Balance Sheet

| ₹ mn | Mar-15 | Mar-16 | Mar-17 | Mar-18 |
|-----------------------------------|------------|------------|------------|------------|
| Liabilities | | | | |
| Share capital | 10 | 10 | 10 | 11 |
| Reserves and surplus | 351 | 255 | 314 | 404 |
| Minority Interest | 23 | 20 | 21 | 14 |
| Long-Term Borrowings | 4 | 0 | 0 | 0 |
| Unsecured Loans | 4 | 3 | - | - |
| Deferred Tax Assets / Liabilities | (2) | (5) | 4 | (1) |
| Other Long Term Liabilities | 1 | - | 9 | 2 |
| Long Term Provisions | 3 | 3 | 3 | 4 |
| Trade Payables | 34 | 38 | 36 | 35 |
| Other Current Liabilities | 35 | 38 | 102 | 42 |
| Short Term Borrowings | 0 | 0 | 0 | 0 |
| Short Term Provisions | 6 | 28 | 13 | 12 |
| Total Liabilities | 468 | 391 | 512 | 525 |
| Assets | | | | |
| Net Block | 153 | 148 | 202 | 207 |
| Capital Work in Progress | 0 | 1 | 1 | - |
| Non Current Investments | 3 | 2 | 8 | 2 |
| Long Term Loans & Advances | 10 | 16 | 13 | 7 |
| Other Non Current Assets | 0 | 0 | 2 | 9 |
| Currents Investments | 167 | 79 | 134 | 100 |
| Inventories | 18 | 18 | 14 | 21 |
| Sundry Debtors | 76 | 77 | 80 | 101 |
| Cash and Bank | 29 | 43 | 41 | 60 |
| Other Current Assets | 2 | 3 | 4 | 5 |
| Short Term Loans and Advances | 9 | 6 | 12 | 13 |
| Total Assets | 468 | 391 | 512 | 525 |

Source: Red Herring Prospectus, Dealmoney research

Key Risks

- ❑ Disagreements with ETA Star Healthcare LLC due to which it has not been able to account for the results of its associate, Star Metropolis Health Services Middle East LLC, in its consolidated financial statements since Fiscal 2012 and there is an auditor qualification in its financial statements in this regard.
- ❑ Result of operations and financial condition could be affected by adverse results of legal proceedings.
- ❑ Has certain contingent liabilities that have not been provided for in financial statements, which, if materialize, may adversely affect results of operations, financial condition and cash flows.

Source: Red Herring Prospectus, Dealmoney research

Dealmoney Securities Private Limited

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