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Axis Capital Limited, Research Division - Head of Research & Executive Director of Strategy

Nomura Securities Co. Ltd., Research Division - Head of India Industrials Research

Ladies and gentlemen, good day, and welcome to the Apollo Hospitals Limited Q2 FY '19 Earnings Conference Call. (Operator Instructions) Please note that this conference is being recorded.

I now hand the conference over to Mr. Mayank Vaswani from CDR India. Thank you, and over to you, sir.

Thank you. Good evening, everyone, and thank you for joining us on this call to discuss the financial results of Apollo Hospitals for Q2 and H1 of FY '19, which were announced earlier today. We have with us on the call, the senior management team comprising Mrs. Suneeta Reddy, Managing Director; Mrs. Sangita Reddy, Joint Managing Director; Dr. Hariprasad, President of the Hospitals Division; Mr. A. Krishnan, Group CFO; and Mr. Obul Reddy, CEO of Apollo Pharmacy.

Before we begin, I would like to mention that some of the statements made in today's discussions may be forward-looking in nature and may involve risks and uncertainties. For a complete listing of such risks and uncertainties, please refer to the investor presentation. Mrs. Suneeta Reddy will briefly cover the operational progress and financial performance for the quarter and half year, following which, we shall open the floor for Q&A.

Before I hand over, I would like to remind everyone that documents relating to our financial performance have been shared earlier. This includes a deck on the reorganization of the stand-alone pharmacy business.

I now invite Mrs. Suneeta Reddy to cover the highlights of our performance for the quarter. Over to you, ma'am.

Thank you, Mayank. Good evening, everyone, and thank you for taking time out to join our call. I trust all of you have been able to refer to our earnings documents. Our growth momentum continues in this quarter. The company reported a robust performance, both in hospitals and stand-alone pharmacy. Quarter 2 revenues year-on-year grew 15% to INR 2,090 crores, aided by Healthcare Services growth of 11% and sharp growth of 20%. Existing hospital revenues grew by 9%, and new hospitals INR 240 crores, representing a 23% growth.

Overall, quarter 2 FY '19 occupancy across the group was at 5,020 beds or 70% compared to 69% in quarter 2 FY '18. The occupancy in mature hospitals was at 3,884 beds or 72% and new hospitals 1,136 beds or 64%. Quarter 2 overall EBITDA was at INR 258 crores as compared to INR 221 crores in quarter 2 FY '18, a year-on-year growth of 17%.

Healthcare Services margin were at 18.4% against 18.3% in quarter 2 FY '18, aided by new hospitals, which reported a 6.1% EBITDA margin compared to 4.6% in the last year. Existing Healthcare Services margins were at 21.7% versus 21.1% in H1 FY '18. On SAP, the actual revenues in SAP grew 20% on the back of 82 new stores added. SAP EBITDA grew to 41% -- by 41% -- 42% to INR 51 crores. EBITDA margin was at 5.3%.

PAT grew by 11% to INR 79 crores. Interest costs were higher by 12% year-on-year at INR 66 crores, and depreciation was higher by 11% year-on-year at INR 74 crores on account of additional CapEx in new facilities. Effective tax rate for quarter 2 FY '19 was 33%. Mature hospitals' ROCE has crossed 20% threshold and has reached 21% in H1 FY '19. SAP ROCE is at 18%. 11 new hospitals with capital employed of over INR 1,900 crores will begin contributing to the ROCE.

Present debt as of 30th September, '18, is INR 3,222 crores. Cash and cash equivalents of INR 258 crores. Net debt or -- is at INR 2,964 crores, debt-to-equity ratio of 0.84, net debt to EBITDA of 3.06x. Consolidated performance, too, grew in line with standalone, reporting a 15% revenue growth and EBITDA growth of 21%.

AHLL reported revenues of INR 148 crores in quarter 2 FY '19 with an EBITDA loss of INR 14 crores as compared to revenues of INR 150 crores and an EBITDA loss of INR 22 crores in quarter 2 FY '18. We believe the quarter's performance has demonstrated the resilience of our business module, which is well diversified across specialties, geographies and maturities. Of the 7,000-plus operating beds across the network, excluding AHLL and our managed beds, 13 hospitals with 1,717 plus

the operating beds are new, and the progressive increase in volumes and utilization in the quarters ahead will aid EBITDA growth and sustain margin expansion through the rest of the fiscal and beyond.

Our strategy around both services pricing as well as cost optimization has delivered results in our existing units. We have also began to witness an increased uptick of our assured pricing plans across units. While providing certainty to patients on cost, the assured pricing plans also recognize the intrinsic value of this delivered service itself rather than the individual input.

Looking ahead, we have a clear and calibrated strategy for each of our business verticals. From a Healthcare Services point of view, our short-term focuses are very clear. We will focus to drive asset utilization. Our centers of excellence are well established now. And through higher-acuity cases in our mix, we are able to deliver a superior margin profile.

We have already stated that we will improve our mature hospital EBITDA margin to 23% over the next few quarters. Sole focus on these fundamentals will ensure that our mature hospitals will continue growing at 10% to 12%. Our new hospitals, which are currently growing at 20-plus percent and contributing close to INR 1,000 crores in annualized top line will continue to grow at the high teens. As these new units begin delivering higher EBITDA, we expect overall ROCE to be well in the mid-teens over next 3 years.

From a medium- to long-term perspective, it is important to note that health care is changing dramatically and at Apollo Hospitals, we have to harness that emerging opportunity. We have made investments in what we believe to be the format of the future. Apollo Health & Lifestyle, our retail format of clinics, day care centers, cradles, sugar, dental and diagnostics is one such investment catering to the community on primary care space and leveraging patient preference for short-term and premium virtual experiences. Here, revenues are growing at a healthy pace. We expect that the entity will achieve EBITDA breakeven by mid-FY 2020, and thereafter, deliver healthy returns.

Health care delivery is also becoming habitus. In an effort to take care to our patient's home, we have strengthened our home health vertical, and we believe it will gain critical mass over time. The democratization of health care is another important trend. Our digital strategy recognizes the consumer's interest in taking charge of his own health and will seek to engage each consumer across all the care lifecycles and across all formats: hospitals, clinics, pharmacies, home health. And this opens up a rich source of data and opportunities for us to maximize wallet share. More importantly, we believe our digital and AI work will enrich our focus on preventive health and wellness.

And that brings us to pharmacy. Our board today approved the reorganization of the stand-alone pharmacy business. AHEL SAP business stands at an inflection point, requiring greater focus and attention, independent of the hospital business, to fully leverage its potential and growth opportunity and enable a foray into digital commerce and execute an omni-channel strategy. Most importantly, we believe this reorganization will help us maximize shareholder value and set the platform for value discovery of the pharmacy business at a later stage through a regulatory compliance structure.

Overall, the SAP business will be grown to achieve a revenue of INR 10,000 crores and 5,000 stores over the next 5 years. Contribution from private labels will double from 6% to 12%, and we will deliver a combined ROCE of 30%. Under the reorganization, we will segregate the front-end SAP business into a separate company, Apollo Pharmacy Limited, which would carry out the front-end operations of direct sales to retail customers. This would be supported by back-end supply chain, which will continue to be housed in AHEL. AHEL will be the exclusive supplier for APL under the long-term supplier agreement. AHEL will enter into a brand-licensing agreement with APL for the use of the Apollo Pharmacy brand. As far the impact on AHEL is concerned, we will still be able to retake 85% of the business economics in the books of AHEL and will continue to strengthen our back-end capability to fulfill orders of front-end business.

15% of the SAP revenues, or approximately 5% to 6% of overall AHEL revenue, will be shifted to the front-end. This amounts to INR 600 crores at top line level. However, given the record of the SAP business, which is grown at 20% consistently, we are confident that there will be no significant impact on AHEL top line going forward. Similarly, while 1% to 1.3% EBITDA will reside in APL, we do believe that overall margin will expand significantly. We have circulated a separate press release and presentation on the reorganization.

I now open the floor for questions. Dr. Hariprasad, Krishnan and Sangita Reddy and Obul Reddy are here with me to take your questions.

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Questions and Answers

Operator [1]

(Operator Instructions) We have the first question from the line of Kashyap Pujara from Axis Capital.

Kashyap Pujara, Axis Capital Limited, Research Division - Head of Research & Executive Director of Strategy [2]

My question was mainly related to the recent transaction that's been announced in terms of segregation of the front-end. So just to basically seek a clarification on that. You mentioned about regulatory requirement, so would this basically be that this has been driven because of the need of the restriction on FDI and retail that we have? And would that mean -- would be -- that be the key reason for the segregation?

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [3]

I think it's -- you should not look at it from a regulatory alone point of view, because there's also a value discovery opportunity, and we were waiting for SAP to get to these mature margins. So one is that we do want an omni-channel presence. We do believe that value discovery is important. And we need to do it in a regulatory framework. So compliance and regulatory is also one of the factors.

Kashyap Pujara, Axis Capital Limited, Research Division - Head of Research & Executive Director of Strategy [4]

Sure. And if -- so when you say 15% economics would go to APL, so INR 600 crores of top line. And typically, say -- and 5% margins thereof. So essentially, it will be around INR 30 crores or INR 40 crores sort of EBITDA kind of a impact as far as SAP is concerned. So essentially, the EBITDA margin impact because of this and us continuing to retain 85% would be 1% at the stand-alone pharmacy level, would that be a fair understanding?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [5]

That's correct, at the EBITDA level, you are right, and approximately INR 40 crores in current term should be shifted to the front end. But it's also important then for you to understand that the cash flows would be even lesser in the front end, because the front-end pharmacy will also take care of the expansions of the stores at that level through the cash flows generated in the front-end pharmacy. So if you look at the cash flows which is going to be captured in AHEL, it will be even higher than the 85%.

Kashyap Pujara, Axis Capital Limited, Research Division - Head of Research & Executive Director of Strategy [6]

Okay. So my question was if you look at -- if I look at the operational performance on -- of SAP, it's been pretty encouraging. We are -- we have reached 20% ROCE in this quarter. Now we are doing this at this point when we are already at -- our threshold ROCE is here. Now how do I basically judge the impact on return on capital employed for the residual 85%, which remains with Apollo Hospitals in terms of economic interest? So could you elaborate in terms of what is the capital employed which will go there? What will be the cost reduction that we can see? If you can just give us a glimpse of the ROCE for the 85% which remains with us versus the 20% which was there with us before this transaction is segregated, essentially.

Obul Reddy, [7]

Yes. As explained, the ROCE is expected to improve further because about -- of that INR 800 crores of capital employed currently in the business, about INR 500 crores capital employed will move into the new company. You will see that the capital employed in the back end will be about INR 300 crores with 80% of the economic benefit attributed to that ROCE should improve further. And given that our growth in the past few years, we are growing at 20%, that will further compensate for what we are transferring the -- in terms of the business to the Apollo Pharmacy Limited, the new entity.

Kashyap Pujara, Axis Capital Limited, Research Division - Head of Research & Executive Director of Strategy [8]

Okay. So just to get this right, when you say 85% is retained with us, would I -- would that also include the brand licensing revenues that we are looking at? Or that would be add-on to that?

Obul Reddy, [9]

Including that. Okay, so it won't be brand license to the front-end entity, the front-end entity get an EBITDA on percent. So today, at current terms, if you look at 1% out of 5% will move away and the 4% remains, given that we have been growing this business at 20%-plus at the revenue level and almost 30%-plus at the EBITDA level in the last few quarters. So it should further improve from the current absolute levels. And given that capital employed is sensibly down, ROCE should improve.

Kashyap Pujara, Axis Capital Limited, Research Division - Head of Research & Executive Director of Strategy [10]

Okay. So basically what you're saying is that if I take the 85% of the economic profits which accrue to us, all in including brand licensing and back-end selling that involves, the INR 500 crores which comes in, so basically we are looking at a capital employed of INR 500 crores and to that extent, we are looking at INR 160 crores. Is that how you are doing the math?

Obul Reddy, [11]

That's right. At the current terms, it is.

Operator [12]

The next question is from the line of Anubhav Aggarwal from Crédit Suisse.

Anubhav Aggarwal, Crédit Suisse AG, Research Division - Associate [13]

Just continuing on the previous question...

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [14]

Could you talk louder, please?

Anubhav Aggarwal, Crédit Suisse AG, Research Division - Associate [15]

Yes, can you hear me now well?

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [16]

Barely. Louder.

Anubhav Aggarwal, Crédit Suisse AG, Research Division - Associate [17]

Okay. Yes, so just asking -- continuing the question on the pharmacy business. In the new kind of structure, would it mean that the margins for AHEL will now largely become capped? Basically, all the operating leverage benefit will go to the front end?

Obul Reddy, [18]

No. We'll -- as explained that the operating expenses will also move away. So to the extent any margin expansion will stay with us, given that the EBITDA maintained at front-end company is maintained.

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [19]

So it's clearly through the combination of supply agreement that we have and also the brand license agreement. Remember that the -- it's like a -- in some way like a franchisor/franchisee, right? If you look at it, there is the -- the front end is exists only because of the brand of Apollo Pharmacy. So clearly, through the combination of supply and the brand licensing agreement, as we said, almost around 8 -- it will be an 85% of the overall EBITDA margins will always be with us. And we don't expect over 1% to 1.2% of the EBITDA margins to be in the front-end pharmacy. So the operating leverage will continue to be captured at AHEL.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [20]

And we truly believe that the EBITDA, the absolute EBITDA will increase and the margins over a period of time because plan for the private label business is to actually double it. And when that happens, you will see an increase in both absolute EBITDA and in margin.

Anubhav Aggarwal, Crédit Suisse AG, Research Division - Associate [21]

Sure. That's helpful. And ma'am, you talked about value discovery here. So the numbers suggest you sold this business or effectively transferred this business at 18x trailing EV by EBITDA. Is the calculation correct?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [22]

So you could be right.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [23]

Yes.

Obul Reddy, [24]

That's right.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [25]

Yes.

Anubhav Aggarwal, Crédit Suisse AG, Research Division - Associate [26]

So is that the fair multiple, effectively, you're looking now? Is that the value discovery that you were talking about?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [27]

So that has to get discovered over time. What we have said, obviously -- yes, obviously, potentially, if you look at the current value at which transactions can be done, that would be the right value. But eventually, this will become even valuable.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [28]

And we have -- when we did part of this process was, we had Deloitte, KPMG, Luthra, all of them together watching on it. So in terms of valuation of 18x, I think that you have to recognize that it was done in a fair manner.

Anubhav Aggarwal, Crédit Suisse AG, Research Division - Associate [29]

Right. Sure, ma'am.

Obul Reddy, [30]

Given that it is more transparently constructed.

Anubhav Aggarwal, Crédit Suisse AG, Research Division - Associate [31]

Sure. Now just one question on the hospital business also. In the Karnataka cluster, we've seen a very sharp decline in utilization this quarter. Any particular reason over there?

Obul Reddy, [32]

In the cluster, actually there, we have added a hospital, a new hospital got added in KR Puram. So actually, the volume have been distributed in the Karnataka cluster. And second thing is, we've been strategically focusing on the payer and the specialty mix with insisting on the margins. So we have consciously actually stopped some of the low-paying corporates and low-paying patients coming into the hospital. So wherein you would see a lower volume in terms of the Karnataka region, but the revenues have grown, and the EBITDA margins have increased significantly.

Anubhav Aggarwal, Crédit Suisse AG, Research Division - Associate [33]

Okay, okay. And just, sorry, one more clarity, if I can. This Proton time lines have shifted, is it? Because we -- earlier mentioned about fiscal '19, and we're yet to spend INR 300 crores balance amount. If the time lines have shifted, that's one question. And what's the reason for delay over there?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [34]

So that is some vendor financing which is there, which is for the Proton equipment itself. It should be -- we -- it will be -- the Proton project itself will actually be phased out over the next 1 year. It's not going to be operational all of a sudden in a quarter. Because obviously, there are 3 gantries in that, and each gantry has to be calibrated, and that goes live, I think, 6 months after the first gantry. So we are expecting the go-live date around the 1st -- between the Jan to March quarter. That's what we are expecting the go-live for the Proton itself and followed by the hospital thereafter. That's the broad plan as it stands. But between FY '19, so there will be some of the monies which will definitely move into FY '20.

Operator [35]

The next question is from the line of Saion Mukherjee from Nomura Securities.

Saion Mukherjee, Nomura Securities Co. Ltd., Research Division - Head of India Industrials Research [36]

Just on following up from the last question on the pharmacy business. You mentioned INR 40 crores, right, of EBITDA that will go into the new company, and your EBITDA run rate is currently INR 200 crores. So it is 20%, right? You were mentioning it is 15%. Just wanted to clarify that first.

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [37]

It also -- when that really happens in the next financial year, we have to factor in the growth that will happen. So we can say we are growing at 20%. So effectively, it goes to 15%.

Saion Mukherjee, Nomura Securities Co. Ltd., Research Division - Head of India Industrials Research [38]

Okay. And the thing is that, let's say, your EBITDA margin is around, say, slightly less than 5%. And I understand, over time, it was supposed to expand. Now that entire expansion, where will it happen? In the front end or it -- the expansion will happen at the back end?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [39]

The expansion will happen in the front end.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [40]

But the numbers will also be -- growth will be reflected in the back end.

Saion Mukherjee, Nomura Securities Co. Ltd., Research Division - Head of India Industrials Research [41]

Okay. So actually just one very basic question, I mean, when you say front end and back end, I mean, what exactly is the activity at the back end? What value Apollo brings to the table besides the brand thing which you mentioned?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [42]

Apart from the brand, Apollo over a period of last decades of our expansion has established a robust supply chain where we have -- we enjoy special pricing and better terms. So all those things will get us an advantage to the overall system. And then we retain those margin in the manner we structured upon the transaction.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [43]

Also, it's the ability to leverage the strong distribution and supply chain and increase operational leverage.

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [44]

In fact, we have operations in over 20 states. So creating the largest fleets, the delivery mechanic, all that advantage today lies with the Apollo. So apart from the brand, entire logistic support will move to the front-end company as a -- and whatever the coverage they will develop, that is under the ownership of existing listed AHIL.

Saion Mukherjee, Nomura Securities Co. Ltd., Research Division - Head of India Industrials Research [45]

And this exclusive supply agreement that is there, so that is, I mean, for a period or it will continue, I mean, for a long time? What is the time line to that?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [46]

The brand supply arrangements are fundamental to the structure, and they will continue very well.

Operator [47]

The next question is from the line of Sudarshan Padmanabhan from Sundaram Mutual Fund.

Sudarshan Padmanabhan, [48]

Sir, my question is around the valuation. I think you mentioned INR 40 crores of EBITDA is moving out. And if I'm reading it, I think you are getting INR 527 crores or INR 528 crores. I mean, would that basically mean it is on a EBITDA -- EV by EBITDA of about 13.2x? I mean, if that is the case, it's really not value accretive, right?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [49]

So 2 things I think that's why it's very important for you to understand that EV by EBITDA is not the only metric at which it has to be seen. The discounted cash flows is the basis of the INR 527 crores. As I said, we are incurring almost around INR 30 crores to INR 40 crores of CapEx every year on the front-end growth. All of that growth will also be spent, growth CapEx will also be incurred from the front-end company. So if you look at the cash flow discounting, obviously, EV EBITDA is one metric in this or one valuation metric that we use as a -- from our perspective. But if you look at what goes at the -- what is being valued at INR 527 crores, as I said, is probably 10% of the cash flows of the pharmacy business and not 15% of the EBITDA. So -- which is why it is getting reflected as INR 527 crores. So which is the last thing which you should use to look at the overall combined pharmacy business. Point 2, as Obul already overarticulated, the ROCE of this business will be significantly uplifted in the back end itself from next year because out of the INR 500 crores -- INR 850 crores capital employed that is there, almost around INR 500 crores of capital employed is moving to the front end. And at the back-end level, you will have significant uplift in the ROCE. So the back end is significantly more valuable than as is visible in the some of the parts based on EV EBITDA, because the front is based on the DCF valuation.

Sudarshan Padmanabhan, [50]

Yes, sure. Sir, I mean, with respect to the other, the private equity holders and others coming into this entity, is that a hurdle rate which you have, kind of, promised? Or is there any performance related -- a thing that has been giving to the people who are coming in? And second is you also mentioned that you have the rights to buy the stakes back from the holder. So what would be the contours of it? I mean, would we be buying at certain IRR? What could be the range of that?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [51]

See, the valuation is always going to be based on fair market value, the current fair market value estimated was INR 527 crores. But if you ask us based on the EBITDA that is being estimated by us, between 1% and 1.2% in the front end, we think the range of IRR that they may get would be between 14% to 16%. It's not committed IRR.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [52]

But we do have a call option.

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [53]

And it's also important that you realize that out of the INR 527 crores, the equity portion which is being brought in by the outside investors is INR 106 crores, because there is also a debt which is coming there which will be a bank borrowing, which will get liquidated through the front-end profits.

Sudarshan Padmanabhan, [54]

I didn't understand that. I mean, can you repeat that?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [55]

So the INR 527 crores is not all equity rates which is happening there. Out of the INR 527 crores...

Obul Reddy, [56]

INR 143 crores is handled through the equity, and the domestic investors will be putting about INR 106 crores. So that will now exit after a 5 -- after some period at the market -- fair market value.

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [57]

The balance is coming through bank borrowings and debt which will be raised at the front-end company, which will get liquidated through its own profits.

Operator [58]

The next question is from the line of Neha Manpuria from JPMorgan.

Neha Manpuria, JP Morgan Chase & Co, Research Division - Analyst [59]

On the -- this one, I'm still not able to understand as to how AHEL will be able to expand EBITDA margins, because we already have an entity which is -- which supplies to the pharmacy business. So AHEL will just continue to provide those supplies to APL?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [60]

So AHEL currently purchases from a set of manufacturers directly, or through distributors, as you are aware. That function continues to be in AHEL. AHEL will continue to do its purchases from distributors, as applicable, and it will in turn supply those -- supply to the front-end company. And -- but through that activity, 85% of the top line of the combined pharmacy business still continues to be in AHEL. And the 80 -- almost around 85% of the EBITDA also continues to be in AHEL. The incremental of -- the brand licensing is made in such a way, it's a percentage of the top line because of which, obviously, some of the operating leverages, which would otherwise be available as a combined entity, will move into AHEL, which is the reason that the EBITDA margins of AHEL will continue on the front -- back-end pharmacy will continue to expand as the overall pharmacy business continues to grow.

Neha Manpuria, JP Morgan Chase & Co, Research Division - Analyst [61]

So you're trying to say that the brand licensing that is based on the percentage of top line of APL?

Obul Reddy, [62]

Of total, that's correct, of APL.

Neha Manpuria, JP Morgan Chase & Co, Research Division - Analyst [63]

Okay, understood. My second question is on the new hospital performance, if I exclude Navi Mumbai. Navi Mumbai has been turning around well, but if I look at the new hospital EBITDA excluding Navi Mumbai, that has been, sort of, been tepid over the last 2 or 3 quarters after peaking in December last year. Any specific reason? And are we -- how should we see the recovery of the new hospitals, ex Navi Mumbai?

Obul Reddy, [64]

See, if you actually look at all the new hospitals, there were at least 5 or 6 hospitals which were losing on the EBITDA level in the last year at the same time. And this year, we have none of our new hospitals losing at all at the EBITDA level. And Navi Mumbai has definitely added on to the EBITDA margins and the EBITDA of the current year. And it has been a high-focus area for us, because investments are large and the hospital has got a lot of operating expenditure on it. So the Navi Mumbai has definitely contributed significantly to the EBITDA of the new hospitals.

Neha Manpuria, JP Morgan Chase & Co, Research Division - Analyst [65]

But excluding Navi Mumbai, you're saying that all hospitals are performing better than they did last year?

Unidentified Company Representative, [66]

Yes.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [67]

No, I think the way to look at it is this way. Last year, they were EBITDA negative. For the past 2 quarters, they've been EBITDA positive. Our focus in the other new -- Navi Mumbai, as you know, quarterly care. It's a quarterly care hospital where you can expect to see quite a dramatic turnaround. With these hospitals, we are focusing on occupancy. So I think the occupancy, which has moved from 52% to 60%. So clearly, there's an 8% uplift in this and overall 23% growth in new hospitals.

Operator [68]

The next question is from the line of [Ishud Sid] from Anvil Wealth Management.

Unidentified Analyst, [69]

I had a couple of questions on the pharmacy business. In the press release, you have mentioned that you'll have a plan to take the revenues to almost INR 10,000 crores versus the current run rate of close to INR 4,500 crores that we have in the pharmacy business. In that, you all have mentioned that the additional stores would be closer to something like 5,000 pharmacy stores versus 3,200 that we already have. So what are we looking at? Are we looking at significant same-store sales growth also happening in our existing chain because of which the revenue growth...

Unidentified Company Representative, [70]

It's a combination of both expansion and same-store sales growth. As you said, we currently have about 3,200 stores. So to reach 5,000, we need about 1,800, which at the current run rate, we should be able to add in the next 5 years. Revenues, if you look at it, the current growth rate, even if you factor about 2%, 3% volume-related lesser growth, we should be able to reach that number.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [71]

And it is also going to be an omni-channel, which is, we are activating the digital presence of the pharmacy network.

Unidentified Analyst, [72]

Okay, okay. Sure. And sir, when you're -- when the target of 30% ROCE that we talk about, right now, we are closer to almost 20%. So when we grow to almost this INR 10,000 crores kind of a number, we're talking about margins being at least 2%, 3% higher from the current level?

Unidentified Company Representative, [73]

So 30% ROCE is what we said, the combined ROCE of the business including the Apollo Pharmacy Limited asset. Overall, combined ROCE would be 30% is what we have said. Clearly, if you look at even the ROCE now for the quarter at 5% EBITDA margins that we have provided, it's already a 20% ROCE on an annualized basis. And getting to a 30% ROCE is also considering a few costs which could be incurred even on the expansion. So that is not something that we have a worry about. And you are right. If you look at the most mature stores now, we have crossed 7% EBITDA margin. It's at 7.4% for the quarter. And clearly, we are seeing that even private label growth is something that will further foster the EBITDA margins to go to over 7%. So our overall target for the pharmacy is 7% over time.

Unidentified Analyst, [74]

Okay, sure. And another way to look at this valuation that we've done is, basically, this INR 527 crores that we have received in terms of the slump sale that we did, and we still have 25.5% stake in that, does that value, the entire pharmacy business at close to INR 5,000 crores? Is that correct?

Unidentified Company Representative, [75]

Yes, you may be right.

Unidentified Analyst, [76]

It's about right, right?

Unidentified Company Representative, [77]

Yes.

Unidentified Analyst, [78]

Okay, okay. Sure. And sir, one question I had was on the hospital business. Overall, I mean, last year last couple of years, we've seen a lot of one-off issues that we had with some celebrity patients and then the capping of stent pricing and all of that. Now with all that behind us now, how do you see the overall trajectory for our hospital business in terms of actually growing on top line as well as EBITDA being much better than top line growth in the next 2, 3 years?

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [79]

I think we'll be able to deliver in excess of 15% top line. We've already proved by 2 quarters of 15% growth. And on a stand-alone basis, we actually grew by 17%. EBITDA is grown by 20%. So clearly, as -- now that we've built up the capacity, we believe by higher asset utilization, cost optimization, we should also be able to increase EBITDA, improve margins, and therefore, deliver on our ROCE. We've also -- the new hospitals' occupancy is ramping up. We've covered -- we've been able to cover all the fixed costs. So I think, looking forward, you can see that mature hospitals, 23% margin. And in new -- and the new ones should move to 20%.

Unidentified Analyst, [80]

Okay. That's great, ma'am. And just one last question I had on AHLL. If I look at AHLL, like, we've done better over the last year in terms of the operational metrics. When do you expect this business to breakeven for us?

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [81]

So as committed, because of the various improvement, strengthening of team, enhancing of the entire formats and close monitoring as well as some aggressive cost rationalization, we have committed to mid-'20, and that target will definitely be met. We also are looking for -- to make sure that this continued growth happens while we keep our focus on cost.

Unidentified Analyst, [82]

Okay. So this mid-'20 is for EBITDA breakeven. Is that correct?

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [83]

That's correct.

Unidentified Company Representative, [84]

Yes, mid-'20.

Unidentified Analyst, [85]

Mid-'20 is for EBITDA breakeven. Okay, okay.

Operator [86]

The next question is from the line of Nitin Agarwal from IDFC securities.

Nitin Agarwal, IDFC Securities Limited, Research Division - Analyst [87]

Just coming back to the pharmacy restructuring, 2 clarifications. One is, a, on the -- as the question has been asked a few times. So assuming hypothetically, we get like a 3% margin improvement from current levels over the next 5 years, so is the understanding right that 85% of the 3% will be retained in the AHSL, and only 15% of the 3%, which is, say, about 50 bps would be retained by the front end? Is that the right understanding?

Unidentified Company Representative, [88]

That is the plan. That is the right understanding.

Nitin Agarwal, IDFC Securities Limited, Research Division - Analyst [89]

Okay. So only -- so basically, even of incremental EBITDA margin gains, 50% -- 85% of it will be retained by AHEL, and the balance will stay in APL?

Unidentified Company Representative, [90]

That's correct. So 1% to 1.2% EBITDA margins will go to the front-end Apollo Pharmacies Limited. The balance will be here. So as we start, assuming that we did this quarter at 5%, and we exit, hopefully, at the higher number, 5% minus 1%, 4% will remain in AHEL. 1% will go to Apollo Pharmacies Limited as we start next year. Over a period of time, that 1% will increase to 1.2% to Apollo Pharmacies Limited, and the balance will be in AHEL.

Nitin Agarwal, IDFC Securities Limited, Research Division - Analyst [91]

So 1.2% is a cap for the front-end on the margin?

Unidentified Company Representative, [92]

Kind of because of the range (inaudible).

Unidentified Company Representative, [93]

Range, it's a range.

Unidentified Company Representative, [94]

Because of the cap, the expected range is that because the licensing agreement will significantly help us extract value into AHEL.

Nitin Agarwal, IDFC Securities Limited, Research Division - Analyst [95]

Sure. And secondly, you mentioned that the equity that the investors are bringing in is only about INR 140-odd crores, right?

Unidentified Company Representative, [96]

That's right. The total, including Apollo.

Nitin Agarwal, IDFC Securities Limited, Research Division - Analyst [97]

Okay. So in terms of, when you are looking to buy out these investors, we'll have to give returns only this component of it?

Unidentified Company Representative, [98]

We are only (inaudible) correct, of the INR 106 crores.

Unidentified Company Representative, [99]

INR 106 crores because the balance is from AHIL's investment for the 25%.

Nitin Agarwal, IDFC Securities Limited, Research Division - Analyst [100]

Right. And the balance -- as you mentioned, the bulk of the other amount which is being raised is through debt, which, obviously, gets liquidated by the cash flows of business?

Unidentified Company Representative, [101]

Correct. That's right.

Nitin Agarwal, IDFC Securities Limited, Research Division - Analyst [102]

Perfect. And secondly, that we are raising, I mean, to what end are we looking to use this money? Is this money being utilized for the pharmacy growth or for the growth of the overall group, per se?

Unidentified Company Representative, [103]

Majorly for -- it will be from the front-end company to Apollo, which will be reduced -- for reducing the debt at Apollo level.

Nitin Agarwal, IDFC Securities Limited, Research Division - Analyst [104]

Sorry, come again, sir?

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [105]

So the money will come from APL. It will go into AHEL to reduce debt.

Nitin Agarwal, IDFC Securities Limited, Research Division - Analyst [106]

So at the group entry level? At the group level?

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [107]

Yes.

Operator [108]

The next question is from the line of Sameer Baisiwala from Morgan Stanley.

Sameer Baisiwala, Morgan Stanley, Research Division - Executive Director [109]

On APL, a question. Your DCF-based valuation, which has generated, I think, the value of roughly INR 4,500 crores for SAP business, and that's a value discovery. So -- and AHEL's enterprise value right now is about INR 20,000 crores. So roughly, what percentage, you think, has been the value discovery in this?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [110]

So as you said, it should be around INR 5,000 crores is the pharmacy value discovery itself has bases this number that has happened because the cash flows, the front-end cash flows are roughly 10%, and 90% still is in the back end. So INR 527 crores of enterprise value of the front end represents approximately 10% of the combined cash flows of the pharmacy business. So given that if you use that, it will -- we will obviously -- there's no valuation done of back end of the combined pharmacy. It is only the front end which was done. So if you use that as a proxy, the over INR 5,000 crores valuation is the right number that you should look at for the enterprise value, which is embedded in AHEL, which doesn't have any debt.

Sameer Baisiwala, Morgan Stanley, Research Division - Executive Director [111]

No, fair point, Krishnan. But I'm saying that, was the market more or less valuing SAP business at the same level?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [112]

I don't know. I guess, I wouldn't really know that answer exactly because it is people like you who decide the value of the -- which is embedded in the overall price. I would think it is still not fully captured.

Sameer Baisiwala, Morgan Stanley, Research Division - Executive Director [113]

Okay. What is the end game for APL?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [114]

So APL, so we will have to -- we have said that at a future date, we have said that we will unlock value in the overall business. So one is, over time, we can figure out how to unlock that value and how the value discovery can happen for the combined business because the -- now this can, at a potential future date, the AHEL business along with the front end, which is APL, which is in a regulatory-compliant structure can now be monetized in whatever fashion you think it can be monetized. So it can be monetized. It can be demerged. Those are all things that we will have to, over a period of time, come to an answer. But this will -- obviously, this first step helps us for a potential value discovery over time.

Sameer Baisiwala, Morgan Stanley, Research Division - Executive Director [115]

Why is -- why are you moving 15% or 10% of economic value to the front end but a much larger, I would say, 60%, 65% of the capital employed in the entity? Are you not artificially boosting ROCE for AHEL?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [116]

No, that is how the capital employed of the front end is actually. If you look at it, the assets, which is 3,167 stores which is there in the inventory, which is being carried in those, is, apart from the back-end inventory, will still rest with Apollo Hospitals, which is the inventory which is there at the back end. But significant portion of the front end, the lease, the deposits and everything else will have to move to the front end. So it is not a artificially done number. It is a very scientifically done number.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [117]

I think it's good to remember that with this team, we're creating an optionality for Apollo. So there is an opportunity to create a multichannel, omni-channel play. There is the opportunity to actually grow the private label and not be constrained by any other regulatory framework.

Sameer Baisiwala, Morgan Stanley, Research Division - Executive Director [118]

SAP is currently buying the back-end supply chain from certain distributors and manufacturers. These distributors are related parties, promoter entities? And will this arrangement continue?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [119]

So part of the -- so if you look at the overall -- around 60%, 65% of the revenues of the supplies happen from the related parties, you're right. But the point is, even in that company, if you look at that company supplies to Apollo Hospitals, it's only 45%. Because both companies, which is [Key Med] and the other related parties which supply, they have an independent business of their own outside of Apollo Hospitals on the distribution side, which is growing significantly. B, as you know, [Mitsoi] is the critical center holder in that distribution business. And that business is independently growing, which is quite independent of Apollo Hospital's business. And we still continue to get a significant value accretion on the economic front getting the supplies from them because we get a preferred pricing over most of the other supplies that they make to other non-Apollo entities because we have a preferred supply agreement with them that -- which allows us to procure at over 1% to 1.5% lower than others.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [120]

And [Key Med] now has distributorships in 20 states. So it allows us to purchase at a significant discount to other distributors in those...

Unidentified Company Representative, [121]

And uniform pricing across the states, and they will deliver to our network directly. So we'll have significant logistics cost savings in account of that.

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [122]

And just since you're also asking, Sameer, it's also important that because it's the largest set of investors, I would also like to let you know that one of the big 4s, even last year, Deloitte had done an arm's length transaction for the purchases from all the related parties. As we speak, one of the other big 4s, because Deloitte is now conflicted because they are auditors as well, one of the other big 4s is working on ensuring and establishing to the audit committee and the board that it is at an arm's length.

Sameer Baisiwala, Morgan Stanley, Research Division - Executive Director [123]

That's fair enough. Just shifting the focus to the hospital side of the business, Suneeta. So a couple of strategic questions. How are you thinking of expanding the bed capacities going forward next 2, 3 years?

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [124]

So first, we've operationalized 7,250 beds, whereas, we have another 2,500 beds that we can operationalize with hardly any costs over the next -- with no fixed costs over the next few years. Just some variable cost. So we are thinking of growing -- we're looking at growing at least by 17%. And that's what we've factored into our plan. And I think we should be able to deliver on that while growing EBITDA significantly because the fixed costs have all been met.

Unidentified Company Representative, [125]

I think it's also important to look at our changing (inaudible) runoff. Because of our high degree of robotics surgery, quicker turnaround times with our new anesthesia techniques, we're able to get better utilization out of the beds that we have as well.

Sameer Baisiwala, Morgan Stanley, Research Division - Executive Director [126]

Sure. So you would first like to consume these 2,000 beds before you move on to expand capacity?

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [127]

Pardon?

Sameer Baisiwala, Morgan Stanley, Research Division - Executive Director [128]

So first, you would want to use this 2,000 bed excess capacity, which was not operationalized.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [129]

Yes.

Sameer Baisiwala, Morgan Stanley, Research Division - Executive Director [130]

Before you look to expand the platform?

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [131]

No. Yes, yes..

Sameer Baisiwala, Morgan Stanley, Research Division - Executive Director [132]

Okay. One final question, Suneeta, is, your update on 2 things. One, outpatient-to-inpatient strategy. I see that the inpatient volumes this time has been probably one of the highest. So how far do you think this has worked well? And second is on the digital strategy.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [133]

So I think both, in a way, are connected. The one thing that we can say is that with OP to IP conversion, we are looking at our data analytics to see how we can improve that. We've actually looked at about significant -- in Hyderabad, we've actually done a live case. Will you to talk about it?

Unidentified Company Representative, [134]

So I'll move first to the digital strategy and come back to the impact on our numbers. So we are going through an overall digital transformation. Right now, in some of our mature hospitals, so where we aggressively implement it, we have almost 85% data capture. So when in an outpatient environment, we're able to do a high degree of data capture, this translates into a higher realization per patient in diagnostic revenue, pharmacy revenue and the conversion rate. And all these metrics are being measured. We actually saw a 12% enhancement in conversion rate in Hyderabad where the pilot project was done, and this is something that we're focusing on even further. We're also looking at moving into day care surgery. And those numbers have increased as well. Also, I think it's a fairly significant thing, based on the CRM system that we've put into place. We're working on reenrollment or reutilization rates. So our loyalty plan across referral, across from clinics to hospital and reference from pharmacy and the CRM are now making us realize further loyalty in our mature customers. So these are all evolving strategies where we're doing specific pilots. Once we've perfected this system, we're scaling them across the enterprise.

Operator [135]

The next question is from the line of [Manish Purda] from [Reliance AI].

Unidentified Analyst, [136]

Just wanted to dwell on this margins thing which you alluded. So if I understand, there are 2 areas where you're making money, or this business would make money for AHIL. One is the branding part, which you said, is linked to sales. And the second is, the supplier invent. Are these the only 2 areas which are -- which profits will be booked for AHIL?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [137]

Yes. The supplier invent has a set of activities and -- which is -- both these -- the agreement are 2, as you rightly said. But the agreements captures -- both these agreement sets which captures the list of activities that is -- AHEL will perform on behalf of the overall combined pharmacy business.

Unidentified Analyst, [138]

No, so what I'm trying to understand then is, let's say, you said the incremental margin, also 85%, flows through you. So let's say, when the sales go higher, and we are just going to be a supplier to the entire mechanics for the pharmacy business, only the COGS part gets taken care of. The COGS part will be, as a percentage of sales, would be taken care of? But the all the additional margins, which are on the basis of operating leverage, wouldn't that flow to the original entity or the acquirer?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [139]

No, it comes here because of the brand licensing agreement, as we said. The brand licensing agreement is, over a period of time, keeps increasing in the overall percentage of revenues. As you've been extract at [0.5], it goes higher over time as well, overall revenues increases for the business. And that is something which even AHEL, as an activity, does perform actively on the customer data leveraging loyalty. It administers the loyalty program for the overall customers. So all those are activities that under the brand licensing agreement is done and performed by AHEL, which is the reason that there is a lot of growth which comes there. And which is the -- in the overall front end. And that gets captured in the back end because of AHEL doing this brand -- performing this brand licensing, which is why the brand licensing is where -- is an important agreement through which that additional of EBITDA margins comes back to the back end. So that is the reason that the front end would be in the range of 1% to 1.2%.

Unidentified Analyst, [140]

Got it. So it's something that is a loyalty agreement, wherein would you evaluate it annually that this percentage would step up by X percentage every year?

Unidentified Company Representative, [141]

Yes.

Unidentified Analyst, [142]

And does evaluation -- so are there set terms of contract initially, or this will be evaluated every year?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [143]

It will be evaluated every year.

Unidentified Company Representative, [144]

Yes. Annual basis.

Unidentified Analyst, [145]

On an annual basis. And just wanted to understand, for this pharmacy business, let's say, when we go on the online channel, and let's say, initially, if there is some sort of investment which is required, would AHEL also participate in that round to the proportion of 26%?

Unidentified Company Representative, [146]

It will be in the front-end company. We expect that to be funded by the (inaudible) of cash flow. But if necessary, we will do the funding at that time.

Unidentified Analyst, [147]

And the management of the business of the front-end part completely goes to the acquiring entity? That is how it is? So the management bandwidth for the -- for this part of the business would be relatively lesser for the AHEL. That is right understanding, right?

Unidentified Company Representative, [148]

That's right. It will have its own independent board and ANP and senior team will manage that activity.

Operator [149]

The next question is from the line of Nitin Gosar from Invesco Mutual Funds.

Nitin Gosar, Invesco Asset Management (India) Private Limited - Analyst [150]

I'm just trying to understand the way now this pharmacy business is positioned. So typically, there are multiple layers, company get followed by C&F (inaudible) then get followed by distributor, then the subdistributors or (inaudible) and then the retailer. I fail to figure out, where this company newly formed, will reside in. I mean, the AHEL, where it will stay?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [151]

So as we said, as we articulated, this is being done to be in a regulatory compliant manner as well. This is a significant first step that is being taken for value discovery over time. You -- we will not be -- we are not in a position to currently -- in the current form that and the structure that the pharmacy businesses is, it -- we cannot discover value in this business or independent of this structure, which is the reason that there is a significant -- this is one of the important reasons why we had to go ahead with this structure, which is the regulatory compliant, blessed by Rudra & Rudra, blessed by Deloitte, blessed by all the people who matter. So clearly, from that perspective, you should remember, so you should look at this as a combined business. You should just -- because at some -- at all points in time, we should remember that there is a call option that we have to be able to call the buyback, the investors' interest in that front-end company, which when the regulatory framework allows us to do, we have the ability to do so. So AHES still continues to be an overall -- you should look at it as a potential stand-alone pharmacy operator over a period of time.

Nitin Gosar, Invesco Asset Management (India) Private Limited - Analyst [152]

Okay. And you mentioned about the back end part. So back end, around 65% of back end is still coming in from distributor/related party?

Unidentified Company Representative, [153]

Yes.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [154]

I mean, at this time, what you can factor always is, as revenues increase, I mean, as...

Unidentified Company Representative, [155]

Mix changes.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [156]

As the mix changes, that could change as well.

Nitin Gosar, Invesco Asset Management (India) Private Limited - Analyst [157]

Mix regarding purchased directly from the companies versus purchased from the distributor?

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [158]

Purchase -- I mean, no...

Unidentified Company Representative, [159]

We have significant plans to improve private label. We may get referred -- other preferred network partners to buy directly. So that might change over period of time based on the economics.

Nitin Gosar, Invesco Asset Management (India) Private Limited - Analyst [160]

And does the current region, does it allow us to source more directly from the company? Why do we need to go from -- via distributors?

Unidentified Company Representative, [161]

Current distributors, we are not allowed to do that.

Nitin Gosar, Invesco Asset Management (India) Private Limited - Analyst [162]

The current system is not sure.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [163]

No, I mean, APL will buy from AHEL.

Nitin Gosar, Invesco Asset Management (India) Private Limited - Analyst [164]

No. I got it. I'm saying, AHEL, which is currently buying from the related party.

Unidentified Company Representative, [165]

Current distribution system doesn't allow direct procurement.

Nitin Gosar, Invesco Asset Management (India) Private Limited - Analyst [166]

No, 34% is still getting distributed.

Unidentified Company Representative, [167]

We are also a distribution channel. And we have a preferred network partner who brings the economy, we prefer that because it's more important to have the logistics and uniform pricing across 20 states where we are present.

Nitin Gosar, Invesco Asset Management (India) Private Limited - Analyst [168]

Okay. So you mean to say the AHEL is not..

Unidentified Company Representative, [169]

It won't have (inaudible) today.

Nitin Gosar, Invesco Asset Management (India) Private Limited - Analyst [170]

So correct me on this. So AHEL is not allowed to buy any distributor license?

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [171]

No. It's not allowed.

Unidentified Company Representative, [172]

Initially, it's not allowed.

Nitin Gosar, Invesco Asset Management (India) Private Limited - Analyst [173]

Okay, okay. And on the CapEx part, so around 1,500 stores are yet to come up as per the plan to reach 5,000 stores. Per store, I think capital employed is roughly around INR 30 lakh as of now. So INR 450 crores is the additional investment which

will happen over period of time in this new entity?

Unidentified Company Representative, [174]

No. The 1,500 stores we have to add over a period of 5 years, and then the 300 stores which we are currently doing. The real CapEx will be only about INR 10 lakh to INR 12 lakh, what we are talking about including the stocking [is about] INR 20 lakh average. So I'd say, yearly, about INR 10 crores or INR 50 crores to INR 60 crores of CapEx, which we are confident that the new company will generate (inaudible) from the business operation.

Nitin Gosar, Invesco Asset Management (India) Private Limited - Analyst [175]

Okay. So overall, this transaction is more structured to make it more compliant rather than cash flow generation because cash flow that you're going to generate out of this transaction is INR 400 crores, INR 500 crores is not going to materially move the needle?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [176]

So this is more for the -- as we said, this is regulatory-compliant structure. That is exactly the point we said.

Unidentified Company Representative, [177]

Took optionality open for...

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [178]

And it helps us to keep the option to buy it back once the regulator is -- once there is easing up of the regulation and if it allows it because obviously we have our investors in AHEL, which doesn't allow us to keep the pharmacy business in the current structure.

Nitin Gosar, Invesco Asset Management (India) Private Limited - Analyst [179]

And one final bit on this. So when the optionality is available, have you defined what valuation we can -- or what IRR we can settle out this transaction?

Unidentified Company Representative, [180]

As we said, it's a -- the business it will be at -- the buyback will be -- the buying will be at an SMB at the appropriate time. And we don't think, based on the current estimates of the front-end company, we think that the IRR would be between the 14% to 16% range.

Nitin Gosar, Invesco Asset Management (India) Private Limited - Analyst [181]

Okay. So that's the what the existing investors or the new investors will end up getting?

Unidentified Company Representative, [182]

Yes.

Operator [183]

The next question is from the line of Shyam Srinivasan from Goldman Sachs.

Shyam Srinivasan, Goldman Sachs Group Inc., Research Division - Equity Analyst [184]

Just on the hospital business. I was just looking at some of the inpatient volume numbers and I think sequentially, we have seen a slowdown in say, Tamil Nadu or in Karnataka. So can you just walk us through what's happening. I may have missed because I joined a little late. But I just wanted to know what's happening to the volumes?

Unidentified Company Representative, [185]

Yes. As we actually look at the numbers, there is -- you need to look at like-for-like in -- as I said earlier, in Karnataka, we have the new hospital which is functional. And in Tamil Nadu, we have mother or mothers in the Cradle, which is functional. So all the women care is moved from the main hospital into the mother and mother's hospital. So that way it is being done by our volume distribution. And second thing is that, as we've just explained, a lot of procedures which needed IP admission are now being done as day care procedures. In the third and last thing is, we've taken a conscious decision to shut out some of the low-paying corporates and low-margin corporates where we were not earning much. So all this put together, you will see a decrease in the volume in the Tamil Nadu and Karnataka regions in terms of inpatient. But the revenues have gone up significantly in double digits in both the areas.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [186]

And I think we should also recognize that the ARPOB has gone up because of the strategy by 8%.

Shyam Srinivasan, Goldman Sachs Group Inc., Research Division - Equity Analyst [187]

No. I was going to come to that. But before that, if you can help us understand, what are like-for-like growth if I were to kind of normalize for this because we are not able to see it. Can you just help us understand what could be, like a like-for-like volume growth in some of these regions, if we were to do this historically as well?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [188]

I think you should take this off-line and Krishnakumar can help you with that. But one perspective that you should also remember is that there is a lot of -- for example, even if you look at Chennai, we have been focusing on the CoEs. And clearly, the focus on CoEs has helped us grow our volumes in cardiac, oncology and places like that, which is accretive to the overall revenues. And also, simultaneously, some of the day care work has also moved into places like Apollo Health & Lifestyle. Because there is this day surgery center (inaudible) and Chennai for example, where there is some movement of volumes of day care which has happened from Apollo into Apollo Health & Lifestyle. So these are certain calibrations which are happening at a volume level because we follow a cluster approach for our strategy. Hence, that is why if you look at the overall revenue, the revenue growth is healthy 6% on inpatient. And outpatient is a 13% growth. And clearly, there is a lot of outpatient growth that we've seen in most of these specialties. And some of them are also being referred to day care centers.

Shyam Srinivasan, Goldman Sachs Group Inc., Research Division - Equity Analyst [189]

Okay. And my second question was just on the ARPOB. I think, Suneeta also alluded to it, the kind of growth, so you think this ARPOB growth, which is say somewhere in like 10%, do you think that is sustainable? And how much of it is because of this whole -- you did an exercise 2, 3 quarters back when you looked at...

Unidentified Company Representative, [190]

Can you finish your last sentence?

Shyam Srinivasan, Goldman Sachs Group Inc., Research Division - Equity Analyst [191]

I'm just saying, we did an exercise looking at procedure pricing and trying to improve transparency on some of our procedures. How much of this has translated into the kind of ARPOB growth that we have seen?

Krishnan Akhileswaran, Apollo Hospitals Enterprise Limited - CFO [192]

So almost around -- there has been an uplift which we have got because of that also. And broadly, around, I would think, almost around 30%, 40% of this would've been a combination of service pricing and CoE and case mix at a broad level.

Shyam Srinivasan, Goldman Sachs Group Inc., Research Division - Equity Analyst [193]

Got it. And you think this is sustainable on a go-forward basis? I think that's the key question.

Unidentified Company Representative, [194]

Yes.

Operator [195]

We'll take that as the last question. I would now like to hand the conference back to the management team for closing comments.

Suneeta Reddy, Apollo Hospitals Enterprise Limited - MD & Executive Director [196]

Thank you for joining us on this earnings call. As always, we believe that the fundamental demand and supply gap will continue to increase the demand for quality health care. At Apollo especially, we believe that creating the entire ecosystem of customer health care delivery will not only result in revenues and profits, but better outcomes for patients. As an institution, we remain committed to patient care and value creation for all our shareholders and stakeholders. Once again, thank you, and good evening.

Operator [197]

Thank you very much. On behalf of Apollo Hospitals Limited, that concludes this conference. Thank you for joining us. Ladies and gentlemen, you may now disconnect your lines.