

UPDATE

MID CAP

Share Data

Reuters code	FOHE.BO
Bloomberg code	FORH IN
Market cap. (US\$ mn)	1266
6M avg. daily turnover (US\$ mn)	4
Issued shares (mn)	317.3
Target price (Rs)	162

Performance (%)	1M	3M	12M
Absolute	19	53	178
Relative	12	53	35

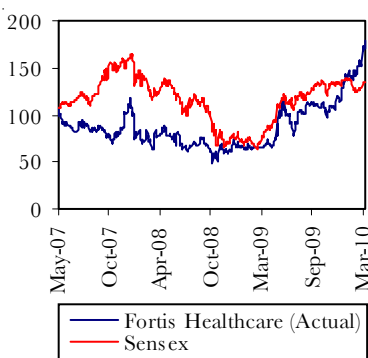
Valuation ratios

Yr to 31 Mar	FY10E	FY11E
EPS (Rs)	2.2	4.2
+/- (%)	245.1	88.4
PER (x)	77.0	40.9
PBV (x)	3.0	2.8
EV/Sales (x)	6.3	3.9
EV/EBITDA (x)	37.0	19.4

Major shareholders (%)

Promoters	69
FII's	4
MF's	1
BFSI's	1
Public & Others	25

Relative performance



Fortis Healthcare

Maintain Outperformer

Price: Rs 181

BSE Index: 17,167

12 March 2010

Acquires 24% in Parkway...becomes Asia's largest hospital chain

Fortis announced its third and the largest acquisition (first was Escorts for Rs 5.9 bn and second was Wockhardt hospitals for Rs 9 bn) as it acquires 23.9% stake in Singapore-based Parkway Holdings from TPG capital for US\$ 685 mn (valuing Parkway at US\$2.8 bn). Parkway Holdings Limited, listed on the Singapore Stock Exchange, is one of the region's leading providers of healthcare services, with a network of 16 hospitals with ~3,600 beds across Singapore (1,022 beds), Malaysia (1,900 beds), Brunei (20 beds), India (425 beds), UAE (260 beds) and China (14 beds). With this acquisition, Fortis becomes the largest hospital company in Asia with ~62 hospitals and 10,000+ beds (much ahead of Apollo which has ~8,000 beds). The funding for the acquisition will be through a mix of internal accruals, equity and debt.

The deal values Parkway at US\$ 2.8 bn (~20% premium to its market cap of US\$ 2.4 bn) and at a valuation of ~21x CY09 EV/EBITDA (deal is expensive as compared to 14x FY09 EV/EBITDA for Wockhardt - which was a distressed asset). However, given the premium positioning of Parkway hospitals and benefits that would be accruing to Fortis, we expect the deal to be positive for Fortis in the long run. At the current market price of Rs 181, Fortis trades at 41x FY11E and 29x FY12E earnings, respectively. In its quest to become a regional leader, P/E valuations based on medium-term perspective has gone overboard and now with Parkway Holdings acquisition, valuations appear stretched based on Fortis' current market cap of Rs 57 bn (US\$ 1.25 bn). On EV/sales and EV/EBITDA also, Fortis trades at a significant premium to Apollo (130% and 69% premium, respectively). Key risk includes managing global chain along with domestic chain and smooth integration of acquired businesses.

About the deal: Fortis announced its third and the largest acquisition (first was Escorts for Rs 5.9 bn and second was Wockhardt hospitals for Rs 9 bn) as it acquires 23.9% stake in Singapore-based Parkway Holdings from TPG capital for US\$ 685 mn (valuing Parkway at US\$ 2.8 bn). Fortis intends to seek four seats on the board of directors of Parkway and intends to nominate Mr Malvinder Mohan Singh as the Chairman of board of directors of Parkway. Of these, two members (including Mr Malvinder Mohan Singh) will be relocating to Singapore. However, the Fortis management indicated the current management of Parkway will continue to manage the chain.

About Parkway: Parkway Holdings Limited, listed on the Singapore Stock Exchange since 1975, is one of the region's leading providers of healthcare services, with a network of 16 hospitals with ~3,600 beds across 6 countries. Further, the company is also a provider of radiology services, laboratory services, management services (to Parkway Life REIT which has ~2 mn sq ft of space), healthcare education and operates 39 Parkway Health Patient Assistance Centres (PPAC) across the globe. In India, Parkway has a JV with Apollo hospitals which operates a 325 bed Apollo Gleneagles hospital in Kolkata. Parkway through a JV with Koncentric

investments ltd is working on a Greenfield project in Mumbai which will have ~500 beds.

Strategy of going global: With this acquisition, Fortis enters into various Asian markets and becomes the largest hospital company in Asia with ~62 hospitals and 10,000+ beds. According to the management, the two entities will leverage the skill set of the combined entity and will penetrate into Asia. Further, the management indicated the next phase of growth for Fortis would be to go beyond Asia and tap Global healthcare market.

Funding: According to the management, the funding for the acquisition will be through a mix of internal accruals, equity and debt. The company has around Rs 2 bn from the rights issue, plans to raise capital through FCCBs/ECBs apart from infusing capital by way of conversion of warrants. Since the capital raising from FCCBs/ECBs and warrant conversion is expected to take time, the company will raise short term loan (bridge finance) to finance the deal. The company guided from 1:1 debt-to-equity structure for the deal.

Valuation and rationale: The deal values Parkway at US\$ 2.8 bn (~20% premium to its market cap of US\$ 2.4 bn) and a valuation of ~21x CY09 EV/EBITDA. The deal appears to be on the expensive side compared to 14x FY09 EV/EBITDA valuation for Wockhardt deal. However, given the premium positioning of Parkway hospitals along with various synergy benefits (sharing of medical technology, multi-specialty capabilities, exchange of human talent, quality standards and cost optimisation) that would be accruing to Fortis, we expect the deal to be quite positive for Fortis in the long run.

We continue to maintain our positive outlook on Fortis mainly due to its aggressive strategy of expanding its network and focus on profitable growth. The key drivers for growth in the domestic market are improving operational efficiency across its existing facilities, scope of growth from the existing facilities and ongoing expansion which will add ~1,800 beds over the next 2-3 years. Key risk includes managing global chain along with domestic chain and smooth integration of acquired businesses. At Rs 181, the stock trades at an expensive valuation of 19x FY11E EV/EBITDA and 4x FY11E EV/Sales. We maintain Outperformer.

Valuation comparison

FY11E/CY10E (US\$ mn)	Fortis	Apollo	Parkway	Raffles medical	Bangkok Dusit	Bangkok Chain
Mkt cap	1,262	955	2,511	550	909	265
Revenue	335	528	799	176	710	144
EBITDA	67	79	180	42	170	43
PAT	29	33	124	31	60	21
EPS (Rs)*	4.2	24.2	0.1	0.1	1.6	0.4
P/E (x)	43.1	29.0	22.1	18.0	15.4	12.4
Mkt cap/Sales (x)	3.8	1.8	3.1	3.1	1.3	1.8
EV/Sales (x)	3.9	1.7	–	–	–	–
EV/EBITDA (x)	19.4	11.5	17.3	12.2	7.1	6.5
RoE (%)	5.9	8.9	11.5	16.2	13.3	21.9
RoCE (%)	7.7	12.7	–	–	–	–

*EPS in local currency. Fortis and Apollo in Rs, Parkway and Raffles in Singapore dollar, Bangkok Dusit and Bangkok Chain in Thai Baht

Source: B&K Research, Bloomberg estimates

Fortis network of hospitals

S.No.	Hospital	Ownership	% Holding	Category	Care	Region	Capacity	Operational
1	Mohali	100%	100%	Greenfield	Quaternary	North	300	215
2	NOIDA	100%	100%	Greenfield	Quaternary	North	350	177
3	Vasant Kunj	0%	O&M	O&M	Quaternary	North	200	107
4	La Femme	31%	O&M	Associate	Quaternary	North	45	38
5	EHIRC - Delhi	90%	90%	Brownfield	Quaternary	North	331	264
6	Raipur	0%	PPP	Brownfield	Secondary	Central and West	50	45
7	Faridabad	100%	100%	Brownfield	Secondary	North	250	210
8	Amritsar	100%	100%	Brownfield	Secondary / Tertiary	North	166	133
9	Jaipur	100%	100%	Greenfield	Tertiary	North	320	108
10	Malar	50%	50%	Brownfield	Secondary / Tertiary	South	250	178
11	Vashi	40%	40%	Associate	Secondary / Tertiary	Central and West	148	148
12	Jessa Ram	0%	O&M	O&M	Secondary	North	150	75
13	Fortis Hospital, Bangalore	67%	O&M	Brownfield	Secondary / Tertiary	South	100	54
14	Mauritius	29%	O&M	Associate	Tertiary	International	120	110
15	Kota	0%	O&M	O&M	Secondary	Central and West	200	44
16	S L Raheja	0%	O&M	O&M	Tertiary	Central and West	280	140
17	Anandpur	100%	100%	Greenfield	Tertiary	East	414	-
18	BG Road	100%	100%	Brownfield	Quaternary	South	451	255
19	CH Road	100%	100%	Brownfield	Tertiary	South	40	40
20	Chord Road	100%	100%	Brownfield	Tertiary	South	128	128
21	Kalyan	100%	100%	Brownfield	Tertiary	Central and West	60	60
22	Mulund	100%	100%	Brownfield	Quaternary	Central and West	567	251
23	Nagarbhavi	100%	100%	Brownfield	Tertiary	South	55	55
24	Rashbehari Road	100%	100%	Brownfield	Tertiary	East	67	67
25	Sarat Bose Road	100%	100%	Brownfield	Tertiary	East	-	-
26	Yeshwantpur	100%	100%	Greenfield	Tertiary	South	120	-
27	Bhiwani	0%	O&M	O&M	Tertiary	North	175	-
	13 heart command centers (HCC)	0%	O&M	O&M	Secondary	Across India	-	-
	Total						5,337	2,902

Source: Company

Projects under construction

Project location	No. of beds	Expected date of commencement
Shalimar Bagh	350	1QFY11
Kolkata	414	3QFY11
Gurgaon	450	4QFY11
Bengaluru	120	4QFY11
Ludhiana 2	100	4QFY12
Ludhiana 1	200	1QFY13
Ahmedabad	200	2QFY13
Total addition	1,834	

Source: Company

Income Statement

Yr end 31 Mar (Rs mn)	FY09	FY10E	FY11E	FY12E
Net Sales	6,305	9,400	15,254	20,046
<i>Growth (%)</i>	24.3	49.1	62.3	31.4
Operating Expenses	(5,447)	(7,802)	(12,203)	(15,837)
Operating Profit	859	1,598	3,051	4,210
EBITDA	859	1,598	3,051	4,210
<i>Growth (%)</i>	315.9	86.1	90.9	38.0
Depreciation	(487)	(651)	(977)	(1,207)
Other Income	284	286	295	174
EBIT	655	1,233	2,369	3,177
Interest Paid	(437)	(433)	(801)	(847)
Pre-tax profit	219	800	1,568	2,331
(before non-recurring items)				
Non-recurring items	63	–	–	–
Pre-tax profit	282	800	1,568	2,331
(after non recurring items)				
Tax (current + deferred)	(41)	(104)	(314)	(583)
Net Profit	241	696	1,254	1,748
Minority interests	(32)	5	65	102
Reported Pat	208	701	1,320	1,850
Adjusted net profit	145	701	1,320	1,850
<i>Growth (%)</i>	NA	383.2	88.4	40.2

Balance Sheet

Yr end 31 Mar (Rs mn)	FY09	FY10E	FY11E	FY12E
Current assets	3,635	6,358	8,026	8,123
Cash & marketable sec.	579	2,873	3,187	2,179
Other current assets	3,056	3,485	4,839	5,944
Investments	541	541	541	541
Net fixed assets	14,005	24,655	25,528	26,908
Total assets	18,182	31,555	34,095	35,573
Current liabilities	2,462	1,825	2,513	2,952
Total debt	4,790	8,083	8,537	7,609
Other non-currnet liabilities	12	52	131	247
Total liabilities	7,265	9,960	11,180	10,809
Share capital	2,387	3,294	3,294	3,294
Reserves & Surplus	8,319	18,090	19,410	21,259
Less : Misc. expenditure	(5)	(5)	(5)	(5)
Shareholder's funds	10,701	21,379	22,699	24,548
Minorities interests	216	216	216	216
Total equity & liab.	18,182	31,555	34,095	35,573
Capital employed	15,719	29,729	31,581	32,621

Cash Flow Statement

Yr end 31 Mar (Rs mn)	FY09	FY10E	FY11E	FY12E
Pre-tax profit	282	800	1,568	2,331
Depreciation	426	651	977	1,207
Chg in working capital	617	(1,105)	(708)	(713)
Total tax paid	21	(26)	(193)	(420)
Cash flow from oper. (a)	1,346	320	1,645	2,405
Capital expenditure	(971)	(11,301)	(1,850)	(2,588)
Chg in investments	(211)	(2,373)	(114)	1,508
Cash flow from inv. (b)	(1,181)	(13,674)	(1,964)	(1,079)
Free cash flow (a+b)	165	(13,354)	(319)	1,325
Equity raised / (repaid)	724	9,977	–	–
Debt raised / (repaid)	1,035	3,293	454	(927)
Cash flow from fin. (c)	254	13,275	519	(825)
Net chg in cash (a+b+c)	419	(79)	200	500

Key Ratios

Yr end 31 Mar (%)	FY09	FY10E	FY11E	FY12E
Adjusted EPS (Rs.)	0.6	2.2	4.2	5.8
Growth	NA	245.1	88.4	40.2
Book NAV/Share (Rs)	31.6	56.2	60.4	66.2
Tax	14.6	13.0	20.0	25.0
EBITDA margin	13.6	17.0	20.0	21.0
EBIT margin	10.4	13.1	15.5	15.8
RoCE	4.2	5.4	7.7	9.9
Net debt/Equity	38.6	24.1	23.3	21.9

Valuations

Yr end 31 Mar (x)	FY09	FY10E	FY11E	FY12E
PER	283.4	77.0	40.9	29.2
PCE	65.0	39.9	23.5	17.7
Price/Book	5.4	3.0	2.8	2.6
EV/Net sales	9.2	6.3	3.9	3.0
EV/EBITDA	67.7	37.0	19.4	14.1

Du Pont Analysis – ROE

Yr end 31 Mar (x)	FY09	FY10E	FY11E	FY12E
Net margin (%)	2.3	7.5	8.7	9.2
Asset turnover	0.4	0.4	0.5	0.6
Leverage factor	1.6	1.5	1.5	1.5
Return on equity (%)	1.3	4.3	5.9	7.8

Gaurav Chugh
gaurav.chugh@bksec.com
+91-120-460 5630

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 2. **OUTPERFORMER:** 0 to +25%
 3. **UNDERPERFORMER:** 0 to -25%
 4. **SELL:** Potential downside of < -25% (absolute returns)
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Equity Research Division: City Ice Bldg, 298, Ground/1st Floor, Perin Nariman Street, Behind RBI, Fort, Mumbai – 400 001, India. Tel.: 91-22-4031 7000, Fax: 91-22-2263 5020/30.
Registered Office: Room No. 3/4, 7 Lyons Range, Kolkata – 700 001. Tel.: 91-33-2243 7902.

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