

Equities

6 December 2010 | 6 pages

Fortis Healthcare (FOHE.BO)

Alert: Takeaways from India Pharma Conf., Dec. 6-7

Takeaways from Mumbai — Fortis Healthcare presented at our India Pharma Mini-Conference in Mumbai. Below are key takeaways.

Aiming for leadership in India — Currently Fortis has only a c0.5% share of the total cUS\$46bn Indian healthcare market - management believes there is significant opportunity for growth. The market is highly fragmented, with 85% of the hospitals having less than 30 beds and <1% of hospitals having more than 200 beds. Fortis aspires to garner 4-5% market share in the next 8-10 years through a combination of greenfield, expansion & inorganic opportunities.

Expansion Plans — Fortis currently has c3,500 operational beds, 2,000 of which are owned and 1,500 are managed. Currently 2,000 beds are under project stage and another 2,500 beds will be added in the next 2-3 years. Fortis Healthcare will drive expansion plans in India, while the group entity (Fortis Global Healthcare) will look at global expansion. Synergies between the two entities would be explored at a later stage.

Medical tourism, a large opportunity — as costs are much lower in India and waiting times are manageable. Lower infrastructure and manpower costs, more efficient doctors (more surgeries) and affordability have resulted in lower surgery costs. Fortis has started seeing traction from medical tourism patients and expects three times revenues (6-7% of sales) in FY11 as compared to FY10.

Other key takeaways — 1) Although ROCE on an overall basis is only 8% (target 26%), the older hospitals have started delivering ROCEs of 20%+; 2) Integration of acquired Wockhardt hospitals is complete and the company should start deriving benefits in the coming quarters; 3) The average cost of setting up additional bed capacity ranges from Rs 60m/bed in a tier-II/tier-III city to Rs 100m/bed in a tier-I city; 4) The company is looking at asset-light strategies, including leasing of land, equipment, etc; 5) Acquiring and retaining talent is a big challenge due to a scarcity of skilled manpower.

Maintain Buy — as we believe healthcare delivery is a structural growth story in India and Fortis is one of the well positioned companies to benefit.

Fortis Healthcare (FOHE.BO; Rs153.30; 1L)

■ Company Update

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See Appendix A-1 for Analyst Certification, Important Disclosures and non-US research analyst disclosures.

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Fortis Healthcare

Valuation

Our target price for Fortis is Rs190. We prefer to use EV/EBIDTA versus EBIDTA CAGR as the primary method to value the company. We believe that hospital companies in India would have a predictable and steady revenue stream, given high unmet demand and low but growing penetration of organized healthcare. However, given that these companies are still in an investment phase, we believe EBIDTA provides a much better reflection of the operating profitability of the business at this point. Fortis has only one directly comparable company listed on the Indian market - Apollo Hospitals. We value Fortis at a slight premium to Apollo, at 16x EBITDA (vs 15x for Apollo) as we believe Fortis' greater scale & geographical diversification post the WHL hospitals acquisition merit a higher multiple. Our current EV/EBIDTA multiple of 16x is also in the range that Fortis has traded over the last several years. At 16x Mar'12E EBITDA we arrive at a target price of Rs190.

Risks

Our risk rating for Fortis is Low Risk as suggested by our quants-based rating system, which tracks 260-day historical share price volatility. Key upside risks that could prevent the stock from achieving our rating and target price include: (1) Faster than expected ramp up in occupancy rates, especially in Escorts, could lead to the company beating our earnings estimates; (2) Better than expected performance of the WHL acquisition, could change the outlook for the stock; (3) Any progress on Fortis' plan to unlock value in its land holding could also trigger an upward move in the stock price.

Appendix A-1

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Fortis Healthcare (FOHE.BO) Ratings and Target Price History Fundamental Research

Analyst: Prashant Nair, CFA

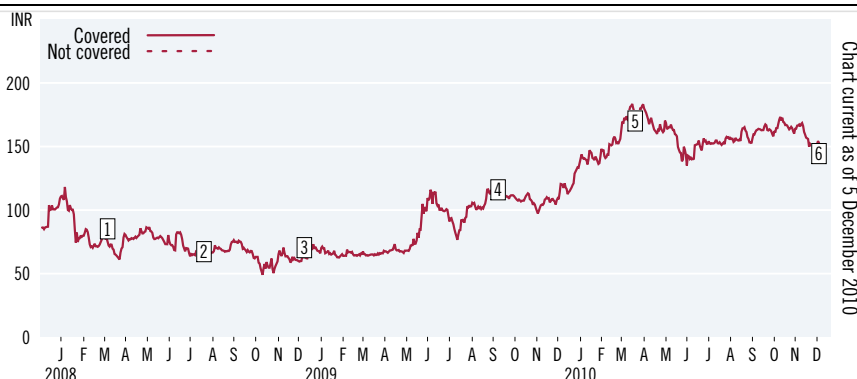


Chart current as of 5 December 2010

| | Date | Rating | Target Price | Closing Price | | Date | Rating | Target Price | Closing Price | | Date | Rating | Target Price | Closing Price | | |
|---|-----------|--------|--------------|---------------|--|------|----------|--------------|---------------|--------|------|--------|--------------|---------------|---------|--------|
| 1 | 6-Mar-08 | *3M | *75.00 | 77.95 | | 3 | 9-Dec-08 | 3H | *59.00 | 62.95 | | 5 | 19-Mar-10 | 3M | *145.00 | 177.55 |
| 2 | 21-Jul-08 | *3H | *60.00 | 62.15 | | 4 | 8-Sep-09 | *3M | *110.00 | 110.95 | | 6 | 3-Dec-10 | *1L | *190.00 | 152.90 |

* Indicates change

Rating/target price changes above reflect Eastern Standard Time

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|--|-----|------|------|
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