

Plans another round of fundraising; see downside risk

Board approves fundraising; risk of dilution looms

Fortis's board has approved plans to raise INR27.5bn (~USD610mn) equity and has also increased the borrowing limit to INR60bn (~USD1.3bn). We believe such fundraising, likely for raising its stake in Parkway, could lead to dilution and stretch the balance sheet ahead. We see ~INR30 downside risk to our target price in case of a successful bid based on Parkway's current market price.

Fundraising likely to fund counter bid on Parkway...

Currently Fortis controls Parkway with over a 25% stake. Khazanah- a Malaysian govt owned fund offered to increase its 23% stake in Parkway to 51.5% by way of an open offer. With the new fund raising intentions announced by Fortis we see possibility of a bidding war for control of Parkway that could result in Parkway shareholders benefiting at the cost of Fortis shareholders.

... and could lead to balance sheet stretch

On May-10 Fortis bought a 24% stake in Parkway for USD685mn by way of debt. This raised its leverage to 2.2x at the end of FY10. Post a consequent ~US\$85mn equity issuance to GIC and ~US\$311mn equity infusion by way of warrants conversion, the leverage will likely come down to 0.8x by June-10 end. However, we believe another round of fund raising will dilute earnings and stretch the balance sheet limiting Fortis's medium term ability to expand in India.

Retain Buy but see downside to estimates and PO

While we retain our Buy on the stock with a target of INR210 that incorporates negative INR20 value for its erstwhile investment in Parkway, we see potential downside risks. In case the company bids to increase its stake to over 50% it will need USD790mn at Parkway's current market price. This investment would earn ~3% ROI and could likely lead to downside of INR30 to our target price.

Estimates (Mar)

(Rs)	2008A	2009A	2010E	2011E	2012E
Net Income (Adjusted - mn)	(556)	209	504	852	1,780
EPS	-2.4	0.7	1.8	3.3	5.6
EPS Change (YoY)	42.3%	NM	180.2%	79.4%	68.7%
Dividend / Share	0	0	0	0	0
Free Cash Flow / Share	-4.9	-2.9	-25.9	5.1	8.5

Valuation (Mar)

	2008A	2009A	2010E	2011E	2012E
P/E	NM	213.3x	76.1x	42.4x	25.1x
Dividend Yield	0%	0%	0%	0%	0%
EV / EBITDA*	318.6x	77.4x	49.3x	27.8x	19.6x
Free Cash Flow Yield*	-1.9%	-1.6%	-14.3%	2.8%	4.7%

* For full definitions of *iQmethod*SM measures, see page 6.

Equity | India | Hospital Management
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**Bank of America
Merrill Lynch**

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Stock Data

Price	Rs140.45
Price Objective	Rs210.00
Date Established	22-Apr-2010
Investment Opinion	C-1-7
Volatility Risk	HIGH
52-Week Range	Rs76.00-Rs187.50
Mrkt Val / Shares Out (mn)	US\$1,221 / 408.1
Average Daily Volume	3,221,060
BofAML Ticker / Exchange	XFFTF / BSE
Bloomberg / Reuters	FORH IN / FOHE.BO
ROE (2010E)	3.4%
Net Dbt to Eqty (Mar-2009A)	31.4%
Est. 5-Yr EPS / DPS Growth	55.0% / 0%
Free Float	24.0%

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Refer to important disclosures on page 7 to 9. Analyst Certification on Page 4. Price Objective Basis/Risk on page 4. Link to Definitions on page 4. 10945647

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iQprofileSM Fortis Healthcare Limited

Key Income Statement Data (Mar)

(Rs Millions)	2008A	2009A	2010E	2011E	2012E
Sales	5,071	6,305	10,067	17,196	25,355
Gross Profit	3,456	4,410	7,124	12,255	18,196
Sell General & Admin Expense	(3,248)	(3,551)	(5,775)	(9,865)	(14,799)
Operating Profit	(260)	371	829	1,448	2,395
Net Interest & Other Income	(146)	(153)	(228)	(403)	(96)
Associates	(5)	(5)	(8)	(14)	(20)
Pretax Income	(411)	213	593	1,031	2,279
Tax (expense) / Benefit	(195)	(41)	(45)	(104)	(345)
Net Income (Adjusted)	(556)	209	504	852	1,780
Average Fully Diluted Shares Outstanding	228	317	408	408	408

Key Cash Flow Statement Data

Net Income	(556)	145	504	852	1,780
Depreciation & Amortization	468	487	520	942	1,002
Change in Working Capital	(85)	(476)	735	321	362
Deferred Taxation Charge	NA	NA	NA	NA	NA
Other Adjustments, Net	288	323	526	1,012	1,046
Cash Flow from Operations	116	480	2,284	3,127	4,191
Capital Expenditure	(1,229)	(1,412)	(10,500)	(1,500)	(1,500)
(Acquisition) / Disposal of Investments	(378)	(243)	0	0	0
Other Cash Inflow / (Outflow)	(401)	689	0	0	0
Cash Flow from Investing	(2,008)	(966)	(10,500)	(1,500)	(1,500)
Shares Issue / (Repurchase)	6,140	0	3,000	0	0
Cost of Dividends Paid	(4)	(3)	(2)	(1)	0
Cash Flow from Financing	3,331	920	8,516	(1,439)	(1,392)
Free Cash Flow	(1,113)	(932)	(8,216)	1,627	2,691
Net Debt	3,594	4,211	9,908	9,219	7,420
Change in Net Debt	(3,667)	(45)	5,700	(688)	(1,799)

Key Balance Sheet Data

Property, Plant & Equipment	9,533	10,044	20,024	20,582	21,080
Other Non-Current Assets	6,961	6,986	6,986	6,986	6,986
Trade Receivables	959	1,335	2,363	3,821	5,635
Cash & Equivalents	161	579	882	1,071	2,370
Other Current Assets	2,097	1,721	1,386	2,362	3,474
Total Assets	19,711	20,666	31,641	34,823	39,544
Long-Term Debt	3,755	4,790	10,790	10,290	9,790
Other Non-Current Liabilities	25	12	12	12	12
Short-Term Debt	NA	NA	NA	NA	NA
Other Current Liabilities	1,779	2,462	3,890	6,645	9,932
Total Liabilities	5,558	7,265	14,692	16,948	19,734
Total Equity	14,153	13,401	16,949	17,875	19,810
Total Equity & Liabilities	19,711	20,666	31,641	34,823	39,544

iQmethodSM - Bus Performance*

Return On Capital Employed	-1.6%	1.7%	3.2%	4.7%	7.0%
Return On Equity	-5.6%	1.5%	3.4%	5.0%	9.7%
Operating Margin	-5.1%	5.9%	8.2%	8.4%	9.4%
EBITDA Margin	4.1%	13.6%	13.4%	13.9%	13.4%

iQmethodSM - Quality of Earnings*

Cash Realization Ratio	NM	2.3x	4.5x	3.7x	2.4x
Asset Replacement Ratio	2.6x	2.9x	20.2x	1.6x	1.5x
Tax Rate (Reported)	NM	19.2%	7.6%	10.1%	15.1%
Net Debt-to-Equity Ratio	25.4%	31.4%	58.5%	51.6%	37.5%
Interest Cover	-0.5x	0.9x	1.7x	1.5x	2.7x

Key Metrics

* For full definitions of iQmethodSM measures, see page 6.

Company Description

Fortis is the second largest hospital chain in India with a pan India presence and about 6,700 beds under management. While Fortis has entered hospital business in late nineties, it has grown aggressively through organic as well as inorganic route. Post acquisition of stake in Parkway holdings it has the largest number of beds under management in Asia.

Investment Thesis

We like Fortis for its i) aggressive management, ii) strong execution capabilities and iii) high earnings growth ahead. We believe, given majority beds for the company are about to reach profitable age, earnings will surge led by strong revenue growth. EPS growth will be driven by higher occupancy rates and higher Average Revenue per Occupied Bed (ARPOB)

Stock Data

Price to Book Value 3.4x

Table 1: Funding details of the first 23.9% stake in Parkway

Funding through...	Amount	Details
FCCB	\$100mn	5% coupon, 3yr to 5yr conversion, @INR167/share, no reset
Preferential equity	US\$85mn (INR3.8bn)	Preferential issue to GIC
Warrants	US\$311mn (INR14bn)	Money likely to come in the first half of June
debt	US\$180mn (INR8bn)	@6.5-7% pre tax cost of debt

Source: Company

Price objective basis & risk

Fortis Healthcare Limited (XFFTF)

Our PO of INR210 is based SOTP for i) target of INR230 for Fortis's domestic operations valued at 20% cut to DCF given execution risks and ii) negative INR20 value for Parkway deal which we view as expensive. We believe, given majority beds will turn profitable going ahead, the company will report 74% CAGR in earnings. Expensive PE valuations are justified given strong growth. Risks arise from i) manpower shortages, ii) new acquisitions, iii) pending litigations post Escorts acquisition and iv) capital intensive growth impacting return ratios in the initial years.

Link to Definitions

Healthcare

Click [here](#) for definitions of commonly used terms.

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India - General Coverage Cluster

Investment rating	Company	BofAML ticker	Bloomberg symbol	Analyst
BUY				
	Aditya Birla Nu	ADYAF	ABNL IN	Reena Verma Bhasin, CFA
	Anant Raj Industries Ltd	XNRJF	ARCP IN	Unmesh Sharma, CFA
	Brigade Enterprises	XBDGF	BRGD IN	Gagan Agarwal
	Chambal Fertilisers & Chemicals	CHBZF	CHMB IN	Prasad Deshmukh
	Container Corp	CIDFF	CCRI IN	Sanjaya Satapathy
	Cummins India	CUIDF	KKC IN	Sanjaya Satapathy
	DLF Limited	XVDUF	DLFU IN	Unmesh Sharma, CFA
	Exide Indus Ltd	XEDRF	EXID IN	Sanjaya Satapathy
	Fortis Healthcare Limited	XFFTF	FORH IN	Prasad Deshmukh
	Housing Development and Infrastructure	XGHSF	HDIL IN	Unmesh Sharma, CFA
	Indiabulls Real Estate Ltd	IBELF	IBREL IN	Unmesh Sharma, CFA
	Jain Irrigation Systems Ltd	JNIDF	JI IN	Prasad Deshmukh
	Jet Airways	JTAIF	JETIN IN	Anand Kumar
	Motherson Sumi	XMSUF	MSS IN	Sanjaya Satapathy
	Puravankara Projects Ltd	XPJVF	PVKP IN	Unmesh Sharma, CFA
	Renuka Sugars	SRNKF	SHRS IN	Sanjaya Satapathy
	Sobha Developers	SBD RF	SOBHA IN	Unmesh Sharma, CFA
	SpiceJet Ltd	MDLFF	SJET IN	Anand Kumar
	Voltas	VTSJF	VOLT IN	Sanjaya Satapathy
NEUTRAL				
	Shree Cements	SREEF	SRCM IN	Reena Verma Bhasin, CFA
	Unitech Ltd	UTKIF	UT IN	Unmesh Sharma, CFA
UNDERPERFORM				
	Ambuja Cements	AMBUF	ACEM IN	Reena Verma Bhasin, CFA
	APIL	ANSFF	APIL IN	Gagan Agarwal
	Assoc. Cement	ADCLF	ACC IN	Reena Verma Bhasin, CFA
	Bajaj Hindusthan	BJJHF	BJH IN	Sanjaya Satapathy
	Balrampur Chini	BMPRF	BRCM IN	Sanjaya Satapathy
	India Cements	INIAF	ICEM IN	Reena Verma Bhasin, CFA
	India Cements -G	IAMUY	ICEM LX	Reena Verma Bhasin, CFA
	Jindal Saw	SWPFF	JS AW IN	Sanjaya Satapathy
	Nagarjuna Fertilizers & Chemicals Ltd	NFACF	NFCL IN	Prasad Deshmukh
	Omaxe Limited	XOMXF	OAXE IN	Gagan Agarwal
	Tata Chemicals Ltd	TTCXF	TTCH IN	Prasad Deshmukh
	Triveni Engg	TVIEF	TRE IN	Sanjaya Satapathy
	Welspun Corp Ltd	XUQRF	WLCO IN	Sanjaya Satapathy
RSTR				
	Grasim	GRSJF	GRASIM IN	Reena Verma Bhasin, CFA
	Grasim -G	GRSJY	GRAS LX	Reena Verma Bhasin, CFA
	UltraTech Cemen	XDJNF	UTCEN IN	Reena Verma Bhasin, CFA

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*iQmethod*SM Measures Definitions

Business Performance

Return On Capital Employed	NOPAT = (EBIT + Interest Income) * (1 - Tax Rate) + Goodwill Amortization
Return On Equity	Net Income
Operating Margin	Operating Profit
Earnings Growth	Expected 5-Year CAGR From Latest Actual
Free Cash Flow	Cash Flow From Operations – Total Capex

Quality of Earnings

Cash Realization Ratio	Cash Flow From Operations
Asset Replacement Ratio	Capex
Tax Rate	Tax Charge
Net Debt-To-Equity Ratio	Net Debt = Total Debt, Less Cash & Equivalents
Interest Cover	EBIT

Valuation Toolkit

Price / Earnings Ratio	Current Share Price	Diluted Earnings Per Share (Basis As Specified)
Price / Book Value	Current Share Price	Shareholders' Equity / Current Basic Shares
Dividend Yield	Annualised Declared Cash Dividend	Current Share Price
Free Cash Flow Yield	Cash Flow From Operations – Total Capex	Market Cap. = Current Share Price * Current Basic Shares
Enterprise Value / Sales	EV = Current Share Price * Current Shares + Minority Equity + Net Debt + Sales Other LT Liabilities	
EV / EBITDA	Enterprise Value	Basic EBIT + Depreciation + Amortization

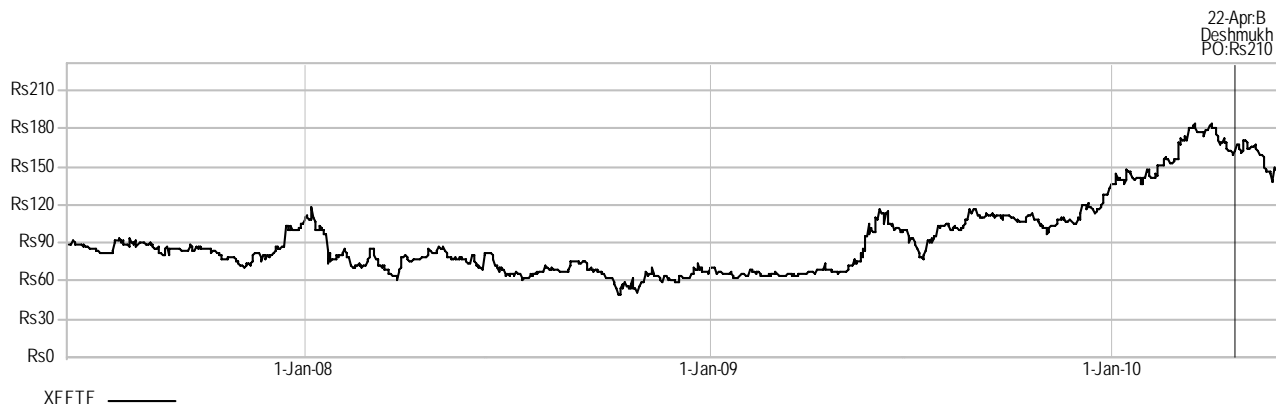
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XFFTF Price Chart



22-Apr:B
Deshmukh
PO:RS210

B : Buy, N : Neutral, S : Sell, U : Underperform, PO : Price objective, NA : No longer valid

"Prior to May 31, 2008, the investment opinion system included Buy, Neutral and Sell. As of May 31, 2008, the investment opinion system includes Buy, Neutral and Underperform. Dark Grey shading indicates that a security is restricted with the opinion suspended. Light grey shading indicates that a security is under review with the opinion withdrawn. The current investment opinion key is contained at the end of the report. Chart is current as of May 31, 2010 or such later date as indicated. BofAML price charts do not reflect analysts' coverage of the stock at prior firms. Historical price charts relating to companies covered as of December 31, 2008 by former Banc of America Securities LLC (BAS) analysts are available to BAS clients on the BAS website."

Investment Rating Distribution: Health Care Group (as of 01 Apr 2010)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	104	50.98%	Buy	60	60.61%
Neutral	55	26.96%	Neutral	33	66.00%
Sell	45	22.06%	Sell	27	62.79%

Investment Rating Distribution: Global Group (as of 01 Apr 2010)

Coverage Universe	Count	Percent	Inv. Banking Relationships*	Count	Percent
Buy	1818	52.41%	Buy	952	58.01%
Neutral	873	25.17%	Neutral	490	61.95%
Sell	778	22.43%	Sell	355	49.72%

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