

WOCKHARDT HOSPITALS LTD

IPO REVIEW

31st January 2008

AVOID

Issue Details

Issue Price: Rs.225-260
Issue Size: Rs.564-652 cr

Issue Opens: Jan31, 2008
Issue Closes: Feb05, 2008

Basis of Allotment

QIBs 60%
(5% for Mutual Funds)

Non-Institutional Bidders 10%

Retail Bidders 30%

Listing

Bombay Stock Exchange
National Stock Exchange

Lead Managers

Citigroup Global Markets
Kotak Mahindra Capital

Public issue of 2.5 crore equity shares of Rs.10 each for cash at a price of [Rs.225/Rs.260] per share. The issue will constitute 24.06% of the fully diluted post-issue paid up capital of the company.

Wockhardt Hospitals Ltd (WHL) is a private healthcare service company. WHL has a super specialty focus on areas such as cardiology & cardiac surgery, orthopedics, neurology & neurosurgery, urology & nephrology & critical care.

- WHL currently has a network of 15 hospitals and bed strength of 1,374 beds. After the proposed expansion the company will have 3500 beds by March-09. The company plans to have total 31 hospitals and 4,780 beds in two years.
- The debt equity ratio presently stands at 5:1 which is significantly high. But if WHL is able to mobilize the funds at upper price band it will come down to 0.59:1. Given the sector dynamics, the Debt equity ratio will become quite favorable and WHL can even raise further debt for expansion.
- Out of the total 15 hospitals, six are owned and constructed by the company whereas other 9 hospitals are located on the premises of others and only operated by WHL pursuant to revenue sharing or lease arrangements. The margins at these hospitals are lower than others.
- The private healthcare services sector is likely to witness healthy growth with the rising income levels, increase in awareness of health issues, lifestyle diseases and health insurances. However the players in secondary market are available at much cheaper valuations, making the company highly unattractive. *(Kindly refer to the peer comparison done later)*

Objects of the issue

Proposed Expenditure Program	Financed from issue(Rs Cr)
Construction, expansion and development of greenfield & brownfield hospitals	569
Prepayment of short term loans	285
General corporate purposes	[.]

The issue is priced at 278x and 241x its annualized earnings for 9 months of FY08 at upper and lower price band respectively. This is stiffly priced as compared to Apollo Hospitals which is trading at 30x FY07 earnings. EV per bed for WHL, Apollo and Fortis comes out to Rs 2.25 crore, Rs44 Lacs and Rs1.59 crore respectively, making WHL unattractive compared to its peers. We expect that the sector as a whole is likely to witness healthy growth in the coming years. However, considering the WHL's stiff valuations and better opportunities like Apollo available in the secondary market at much cheaper valuations, we advise investors to **AVOID** this issue.

INDUSTRY OVERVIEW

With increase in awareness of health issues, lifestyle diseases and health insurances, hospitals sector is likely to witness a high growth in coming years.

CRISINFAC expects the total healthcare delivery market in India to grow from Rs. 1,253 billion in 2006 to Rs.3,642 billion by 2016.

Private healthcare is expected by CII-McKinsey to increase to Rs.1,560 bn by 2012 if health insurance coverage becomes more widely available to the upper and middle classes. Government spending is also expected to increase. CII-McKinsey expects public spending to double by 2012. Rising income levels in India and health awareness in the society are the major positives for the hospital sector.

Thanks to a significantly lower cost of medical treatment in India, medical tourism market in India estimated at US\$ 333 million in 2004 is predicted to become a US\$ 2 billion-a-year business opportunity by 2012 as per E&Y report.

Apollo, Fortis, Max, CARE are the major Indian players in the corporate hospitality sector. But some international players like Pacific Healthcare Holding (Singapore), Columbia Asia (Malaysia) are also eyeing the pie of hospital sector and in the process of establishing in India. With this the sector will become more competitive but considering the industry structure and opportunity laying ahead it should not matter. But the players will have to ensure the better services and expansion. Here the players with established brands and having specialized services like Apollo, Wockhardt will be a better positioned to take on the competition.

ABOUT THE COMPANY

Wockhardt has a pan-India presence with a network of 10 super-specialty hospitals and 5 regional specialty ICU hospitals having superspecialty focus on core areas such as cardiology and cardiac surgery, orthopedics, neurology and neurosurgery, urology and nephrology.

WHL currently has a network of 15 hospitals and bed strength of 1,374 beds. After the proposed expansion the company will have 3500 beds by March-09. The company plans to have total 31 hospitals and 4,780 beds in two years.

WHL derives its revenue from Inpatient hospital services (76%), Outpatient services (13%) and pharmacy sales (11%).

WHL is the only hospital company in India having a strategic collaboration with Harvard Medical International (not-for-profit subsidiary of Harvard Medical School). This relationship helps it to design hospitals adhering to global standards, improve quality of services, train and educate hospital staff, reducing attrition rate.

Key concerns

- Two hospitals in Bangalore and one in Mumbai collectively contributed 68.3% of the total income of the company for 9 months ended Dec-07. These 3 hospitals collectively have only 35.2% of total beds. Such concentration may have adverse effect if the macro conditions in these cities changes. But on the other side, this poses a great opportunity of capturing business in the Tier-II and Tier III cities where the income levels are increasing and in future can generate significant revenue.
- Out of the total 15 hospitals, six are owned and constructed by the company whereas other 9 hospitals are located on the premises of others and only operated by WHL pursuant to revenue sharing or lease arrangements. Company own and operate ten pharmacies.
- The trademark, brand name and logo of "Wockhardt" is owned by Wockhardt Ltd and taken on license by WHL in consideration of annual license fees.

PEER COMPARISON

*(Figures in Rs Crore except for numbers)

	Apollo	Fortis	Wockhardt**
No of hospitals	40	13	15
No of beds	7076	1400	1374
For FY07			
Revenue	950	512	236
Operating profit	152	48	39
OPM	16%	9%	17%
Net profit	95	-98	16
Market cap	2859	1813	2711
EV	3147	2225	3085
PE(on FY07 earnings)	30	NA	174
Revenue per bed	0.13	0.37	0.17
Operating profit per bed	0.02	0.03	0.03
EV per bed	0.44	1.59	2.25
EV per hospital	79	171	206
BY 2010			
No of beds	10,000	7,000	4,780
No of hospitals	NA	40	31

**Market cap and EV taken at upper price band

- WHL is a smaller player compared to Apollo. The expansion plans of Apollo will take it way above WHL in 2010 and will have more than double the capacity of WHL in terms of number of beds.
- On the upper band, EV per bed of WHL is significantly higher than that of Apollo and Fortis.
- Both Apollo and Wockhardt enjoy similar type of brand loyalty. There appears no supporting for such higher valuations of WHL.

VALUATION AND RECOMMENDATION

The issue is priced at 278x and 241x its annualized earnings for 9 months of FY08 at upper and lower price band respectively. This is stiffly priced as compared to Apollo Hospitals which is trading at 30x FY07 earnings. EV per bed for WHL, Apollo and Fortis comes out to Rs 2.25 crore, Rs44 Lacs and Rs1.59 crore respectively, making WHL unattractive compared to its peers. We expect that the sector as a whole is likely to witness healthy growth in the coming years. However, considering the WHL's stiff valuations and better opportunities like Apollo available in the secondary market at much cheaper valuations, we advise investors to **AVOID** this issue.

FINANCIAL STATEMENTS

Profit & Loss account					Rs. crore
Particulars	Dec-07	Mar 07	Mar 06	Mar 05	Mar 04
No of months	9	12	12	12	12
Net sales	259.48	236.48	158.68	129.10	82.25
<i>% increase</i>		49	23	57	
Consumption of inventories	71.47	73.82	50.57	47.18	26.15
<i>% increase</i>		46	7	80	
<i>% of net sales</i>	28	31	32	37	32
Personnel Expenses	31.04	29.57	19.30	14.82	11.22
<i>% increase</i>		53	30	32	
<i>% of net sales</i>	12	13	12	11	14
Operating expenses	88.83	78.93	51.72	35.06	25.70
<i>% increase</i>		53	48	36	
<i>% of net sales</i>	34	33	33	27	31
General Admin Expenses	8.20	7.97	5.08	4.81	3.52
<i>% increase</i>		57	6	37	
<i>% of net sales</i>	3	3	3	4	4
Selling Expenses	5.98	6.91	3.76	5.60	4.00
<i>% increase</i>		84	-33	40	
<i>% of net sales</i>	2	3	2	4	5
Total expenditure	205.52	197.20	130.43	107.46	70.58
<i>% increase</i>		51	21	52	
<i>% of net sales</i>	79	83	82	83	86
PBIDT	53.96	39.28	28.25	21.64	11.67
<i>% increase</i>		39	31	85	
<i>% of margin</i>	21	17	18	17	14
Interest	23.56	11.31	5.70	9.35	8.28
<i>% increase</i>		98	-39	13	
<i>% of margin</i>	9	5	4	7	10
PBDT	30.41	27.98	22.55	12.29	3.40
<i>% increase</i>		24	84	262	
<i>% of margin</i>	12	12	14	10	4
Depreciation	14.59	12.01	8.85	9.07	8.22
<i>% increase</i>		36	-3	10	
<i>% of margin</i>	6	5	6	7	10
PBT before other income	15.82	15.96	13.71	3.22	-4.82
<i>% increase</i>		16	326	-167	
<i>% of margin</i>	6	7	9	2	-6
Other income	0.50	0.22	0.49	0.13	0.08
PBT after other income	16.32	16.18	14.19	3.35	-4.75
<i>% increase</i>		14	324	-171	
<i>% of net sales</i>	6	7	9	3	-6
Tax	9.01	0.59	-0.18	2.04	3.92
<i>% increase</i>		-428	-109	-48	
<i>% of PBT</i>	55	4	-1	61	-82
Rep. PAT	7.30	15.59	14.37	1.31	-8.66
<i>% increase</i>		8	999	-115	
<i>% of net sales</i>	3	7	9	1	-11

Balance Sheet		Rs. crore			
Particulars	Dec-07	Mar 07	Mar 06	Mar 05	Mar 04
No of months	9	12	12	12	12
<u>Sources of funds</u>					
Equity share capital	74.28	50.00	50.00	25.00	6.00
Reserves & surplus	9.69	21.34	5.75	0.46	0.46
Equity shareholders funds	83.97	71.34	55.75	25.46	6.46
Preference share capital	0.00	0.00	0.00	25.00	0.00
Secured loans	201.40	150.57	113.26	79.45	71.41
Unsecured loans	235.00	135.68	24.92	20.00	52.80
<i>Loan funds</i>	<i>436.40</i>	<i>286.25</i>	<i>138.18</i>	<i>99.45</i>	<i>124.21</i>
Deferred tax liability	13.27	6.72	8.37	10.06	8.26
Total	533.64	364.31	202.31	159.97	138.93
<u>Application of funds</u>					
Gross block	374.32	284.14	131.59	120.42	112.57
Depreciation	71.84	57.33	45.35	36.66	27.60
Net block	302.48	226.81	86.24	83.76	84.97
Capital WIP	139.13	80.64	99.36	37.70	13.35
<i>Fixed assets</i>	<i>441.61</i>	<i>307.45</i>	<i>185.59</i>	<i>121.47</i>	<i>98.32</i>
<i>Goodwill on consolidation</i>	<i>13.84</i>	<i>13.84</i>	<i>13.84</i>	<i>13.84</i>	<i>13.84</i>
Investments	0.00	0.00	0.07	2.50	0.00
Inventories	20.94	8.22	3.84	2.83	2.02
Sundry debtors	34.22	21.79	10.71	6.54	4.06
Cash & bank	62.69	40.92	8.45	12.57	2.42
Other current assets	2.53	0.21	0.00	0.00	0.00
Loans & advances	42.62	26.77	13.73	10.09	25.30
Total Current assets	162.99	97.91	36.72	32.03	33.80
Less: current liab	76.12	49.04	31.24	17.86	16.75
Provisions	8.68	5.84	2.68	1.09	0.66
Net current assets	78.19	43.03	2.81	13.09	16.39
P&L Debit balance	0.00	0.00	0.00	9.08	10.39
Total	533.64	364.31	202.31	159.97	138.93

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