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Hospitals grow bigger for better health

A deal frenzy is underway in health care even as big hospital chains are battling falling margins and rising costs



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A spate of hospital deals is set to remake India's fragmented health care landscape, with many old players exiting the market and new ones taking their place.

Just last week, private equity firm KKR announced plans to buy a 49.7 per cent stake in Max Healthcare from South Africa's Life Healthcare for \$293 million. The deal, struck at a premium of 33 per cent, would give KKR joint control of the 2500-bed Delhi-based hospital chain along with its founder-Chairman Aniljit Singh.

With this, KKR has overtaken Bengaluru-based Manipal Hospitals in terms of number of beds. The PE fund, which uses Radiant Life Care as a vehicle for its health care forays, will have 3,500 beds under its belt, compared to Manipal Hospital's 2,200 operational beds.

This is not the only health care deal by KKR in recent months. It also invested in two other multi-specialty hospitals, Delhi's BLK Hospital and Mumbai's Nanavati Hospital, giving itself a sizable foothold in the sector.

Curiously, a deal frenzy is underway in health care even as big hospital chains are battling the

fallout of price cap on medical devices, which has put their bottom line under pressure. But that's not dampening the enthusiasm of suitors. The sector is attracting investors in droves—from global hospital chains, corporates, PE funds, either on their own or along with strategic partners, to local hospital chains looking to consolidate their position and grow faster through a combination of acquisition and greenfield projects (a greenfield project typically takes six years to build and then break-even).

TPG, for instance, is backing Manipal Hospitals and is looking at acquisition opportunities. Bain Capital has identified health care as a core area. Quadria Capital, a health care-focused fund, is planning to raise \$250-300 million via a new fund with India as its priority area.

Global chains like Malaysian hospital major IHH, which grabbed Fortis recently beating KKR and Manipal, also has Hyderabad-based Global and Continental Hospitals under its fold. It has picked up pace in the last few years to become the second largest player closing in on Apollo with over 7,350 beds only through acquisitions.

Apollo is not keeping quiet either. This July, it bought 50 per cent stake in a Lucknow-based 330-bed facility floated by Medica International

Lifesciences, which will be commissioned this year.

West Asian hospital chains run by Indian entrepreneurs are jumping on to the health care bandwagon too. UAE-based VPS Healthcare, which runs 22 hospitals in that country, has put together a corpus of ₹10 billion for acquisition in India. Dubai-based Moopen family, who run Aster DM Healthcare that has presence in the Philippines and West East, bought Ramesh Hospital in Vijayawada and Prime Hospital in Hyderabad, amongst others, to add to their portfolio of 19 hospitals. The Moopens, too, are looking at both acquisitions and greenfield projects to grow. New players are eyeing the sector as well. ITC has announced it will enter health care and others may follow suit.

So what is fuelling this shake-out in health care? One of the reasons could boil down to timing. Manipal Education and Medical Group Promoter Ranjan Pai says: "There is consolidation as the market has matured and people are seeing the benefits of scale. In the next three to four years you will see a lot of consolidation and there will be four or five big players who will remain in the market".

For many of the early investors, including doctor entrepreneurs, who put in money in the network for the last 15-20 years, the cycle of exit has now come, explains Pai. In some cases, the next generation wants to move out of hospitals and in other cases, such as Fortis, external factors have forced them to sell.

This process has been hastened, however, by the changing health care regime—the stiffening regulatory mechanism (price caps on medical devices) and the roll-out of the nationwide national insurance policy, Ayushman Bharat, which will give health protection to 100 million poor families. Hospitals fear the policy will force

them to accept irrational pricing and squeeze margins even further.

The impact of all this is likely to be felt more strongly by smaller chains, which dominate India's health care. The top six listed hospital chains have just over 23,000 beds, or a little over 3 per cent of the total 0.7 million beds in the private sector, with smaller hospitals and branded chains making up the rest. For the smaller hospitals, merging with a bigger chain or new players who are aggregating hospitals could be the only way to survive.

Indeed, the pressure on margins is for all to see. "The wide range of regulatory restrictions from multiple authorities will continue to suppress the average revenue per occupied bed in the short to medium term," says brokerage house ICRA in a recent report.

Even bigger chains are struggling to stem the slide in profitability. Max Healthcare saw its EBITDA (earnings before interest, taxation, depreciation and amortisation) margins at 4.6 per cent in the June quarter of FY 2019 compared to 9.6 per cent in the previous year. Apollo Hospital Enterprises' EBITDA margins fell to 11.5 per cent in FY 2018, from 12.2 per cent in FY 2017.

Yet there are long-term gains to be had for bigger players and that explains the interest from new investors. Poor reach of health care, increase in life expectancy, growth in lifestyle disease as well as expansion of medical tourism, all these

factors make hospital assets attractive in the long term.

The dismal bed-to-patient ratio at one bed per 1,050 people, instead of the World Health Organization recommended five beds, speaks to the potential for upside here.

"Investing in health care is a no brainer in India where government investment is so low and the number of beds added by them much lower than demand," says a leading PE fund executive who does not want to be named.

Pai enumerates three reasons why smaller hospital chains would eventually exit the space. One, the bigger boys have the advantage of economies of scale not available to smaller ones, which means they can buy larger volumes of consumables at a lower price. Two, it is easier to

attract good doctors to a big brand than a stand-alone chain. And three, the same set of doctors at a big chain can move across centres to handle complex cases, which saves money. "You might not have a liver transplant expert in each hospital, but you might want to have a doctor to run around different hospitals," says Pai. The bigger the hospitals, the better they will be.

