

## ICRA Lanka revises the ratings of Nawaloka Hospitals PLC to [SL]BBB+(Stable) from [SL]A-(Negative)

July 17, 2018

Instrument*	Current Rated Amount (LKR Mn)	Rating Action
Issuer Rating	N/A	Revised to [SL]BBB+(Stable) from [SL]A- (Negative)
Senior Unsecured Redeemable Debentures	1,500	Revised to [SL]BBB+(Stable) from [SL]A-(Negative)

### Rating action

ICRA Lanka Limited, Subsidiary of ICRA Limited, Group company of Moody's Investors Service has revised the Issuer rating assigned to Nawaloka Hospitals PLC ("NHL"/"the Company") to [SL]BBB+ (pronounced S L triple B plus<sup>1</sup>) with Stable outlook from [SL]A- (pronounced SL A minus) with Negative outlook. ICRA Lanka has also revised the issue rating outstanding on the company's LKR 1,500 Mn Senior Unsecured Redeemable Debenture Programme, currently listed on the Colombo Stock Exchange, to [SL]BBB+ (pronounced S L triple B plus) with Stable outlook from [SL]A- (pronounced SL A minus) with Negative outlook.

### Rationale

The rating revisions take into account the deterioration in capital structure and coverage indicators of the company on account of higher than expected debt funded capital expenditure, which has resulted in increase in gearing from 2.00(x) as on FYE March 2016 to ~2.71(x) and 3.41(x) as on FYE March 2017 and FYE March 2018 respectively. The total cost of the Multistory Car Park and Specialist Center project has increased from LKR 3.5 Bn to LKR 6.8 Bn due to certain changes in scope of the project. Apart from this project, the company had also incurred capex for other equipment and machineries during FYE March 2018, which was also partly funded by debt. With higher debt repayment obligations in the medium term compared to current cash accrual levels, the company may face some liquidity pressure and need refinancing if the growth in cash accruals are inadequate, although some comfort is drawn from the liquid investments of ~LKR 1.3 Bn.

The aforementioned capex is expected to help the company in debottlenecking its operations and addressing infrastructural issues, which had resulted in lower occupancy levels for the flagship hospital over the past several years. Further, the company has witnessed growth in laboratory operations under a new subsidiary, Nawaloka Green Cross Laboratories (Pvt) Ltd, which is currently carried out in collaboration with Green Cross Group, South Korea. The company's ability to realize targeted revenue growth and margin improvement from the infrastructure addition and new ventures in a timely manner will be critical for improvement in credit profile and therefore, this remains a sensitivity factor.

The ratings draw comfort from the strong brand name and operational track record of the Company, witnessed by the healthy market share enjoyed by NHL in Sri Lanka's private sector healthcare industry.

<sup>1</sup> For complete rating scale and definitions please refer to ICRA Lanka's Website [www.icralanka.com](http://www.icralanka.com) or other ICRA Rating Publications

Over the years, the company has been able to leverage its locational advantage to attract leading consultants which has aided in consistent expansion of service offerings, leading to healthy revenue growth (consolidated revenue excluding Nawaloka Green Cross Laboratories Pvt Ltd) of ~17.00% YOY growth during FYE March 2018.

NHL is also one of the few private sector groups to expand its services into the lab diagnostics business and also expand its bed capacities to locations outside of Colombo. These have enabled the Company to offset the increasing pricing pressures on account of rising competition in the market and the consolidated entity has witnessed improvement in operating margins during FYE March 2017 and FYE March 2018. Nonetheless, the margins remain susceptible to growing competition and inflationary pressure on employee cost. Further any regulatory restrictions on pricing of key healthcare services could also adversely impact the performance of the Company.

ICRA Lanka also takes note of the favourable demand outlook for the healthcare industry, which is expected to witness increase in demand driven by increasing medical insurance penetration and lifestyle related disorders; and given the physical limitations of the public healthcare system, incumbent private players (especially those who are expanding operations) are expected to benefit from the same.

### Outlook: Stable

The stable outlook reflects the company's established brand name and track record in private health care sector in Sri Lanka, which coupled with infrastructure additions undertaken should aid in revenue growth and performance. The outlook may be revised to 'Positive' if the company records healthy improvement in profitability and consequently its liquidity position. Conversely, the outlook may be revised to 'Negative' if there is any deterioration in coverage indicators and liquidity on the back of lower-than-expected earnings or on account of any debt funded-major capital expenditure programmes.

### Key rating drivers

#### Credit strengths

**Experience of the promoters, strong brand name and long operational track record in healthcare segment:** NHL is one of the oldest private sector health care providers in Sri Lanka and has been operational since 1985. The long operational track record and experience of promoters, have helped the company in establishing a strong brand name and healthy market share (among private sector players) in the private health care sector. The company has the single largest bed concentration per location, with ~400 beds in Colombo. The Company also has another hospital in Negambo with ~75 beds capacity, which has aided the company in increasing its reach. During FYE March 2018, the company has opened another unit in Gampaha.

**Steady growth witnessed in last few years; infrastructure improvement and laboratory operations to aid future growth;** The company has witnessed steady growth in revenue over the last few years on the back of its brand, favourable location and ability to attract consultants across several specialties, leading to growth in both outpatient and inpatient admissions. However, despite the growth in patients and improvement in revenue and margins, the occupancy levels have remained modest in the range of 45-50% in the last few years. This was on account of infrastructure constraints at the hospital which was limiting the ability of the hospital to optimally utilize the facilities. In order to address these issues, the company had undertaken the large capex to set up a Multistory Car Parking and Specialty Center, which was completed during FYE March 2018. The project had witnessed periodic increase in cost from initial estimate

of LKR 3.5 Bn to LKR 6.8 Bn due to changes in project scope and has been largely funded through debts. Further, the Company is also trying to expand the laboratory operations under a subsidiary – Nawaloka Green Cross Laboratories (Pvt) Ltd, with technical collaboration from Green Cross Group, South Korea. The infrastructural improvement and expansion of lab operations are expected to drive future growth. Therefore, the improvement in occupancy and translation into revenue growth and margins as a result of these new developments, remains to be reviewed going forward.

**Favourable demand outlook for private healthcare services:** The demand for private healthcare sector in Sri Lanka is expected to witness increase due to several factors. The fiscal constraints in the public sector, increasing per capita income levels, increased insurance penetration and health seeking behavior have aided the growth in the private healthcare sector. Moreover, Sri Lanka having the fastest-growing ageing population in the region and relatively higher deaths due to NCDs, amidst rapid urbanization and changes in life style patterns, will further increase the demand for private healthcare sector in Sri Lanka.

### Credit challenges

**Performance susceptible to competitive pressure and changes in Government policies:** The Company faces higher competition from both public and private sector-health care providers. While the demand for private sector health care has been growing, there is intense competition among the major private sector health care providers to attract consultants and medical staff, which is leading to inflationary pressure on wages. Further, the sector remains susceptible to regulatory or Government policy changes, such as higher taxation, imposition of price caps, etc.

**Capital structure characterized by high gearing and stretched coverage indicators:** The Company's capital structure is characterized by high gearing due to the debt funded capex undertaken. The gearing had increased from 2.06(x) in FYE March 2016 to 3.41(x) in FYE March 2018. The coverage indicators have also weakened during this period with interest coverage and TD/OPBDITA of 2.12(x) and 6.69(x) during FYE March 2018 compared to 2.5(x) and 7.57(x) during FYE March 2017. With high repayment obligations in the near to medium term, compared to current level of cash accruals, the company may require refinancing, if the growth in cash accruals is not commensurate.

**Ability to attract quality man power will be critical:** The Company's ability to attract medical staff (medical practitioners, consultants, technicians etc.) amidst increased competition from public and private sector, will be critical for continued improvement in financial performance. However, the Company continues to train new nurses through the Nawaloka College of Health (separately owned by the promoters of the group) and this has helped the company to infuse new talent while rationalizing staff costs.

**Analytical approach:** For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

**Links to applicable criteria:** [www.icralanka.com/images/pdf/Corporate%20Rating%20Methodology.pdf](http://www.icralanka.com/images/pdf/Corporate%20Rating%20Methodology.pdf)

### About the company:

Incorporated in the year 1982 by the late Mr. Deshamanya H K Dharmadasa, Nawaloka Hospitals PLC is a leading private sector hospital chain in Sri Lanka. The business commenced operations in September 1985 and currently has 475 operational beds, being operated under four separate entities. Nawaloka is listed on the Colombo stock Exchange with the promoters holding a majority share (~65%). All of the hospitals are operated by wholly owned subsidiaries of the Company. During FYE March 2018, Nawaloka has also

started a referral based laboratory operations with technical partnership with Green Cross Group-South Korea, under a subsidiary – Nawaloka Green Cross Laboratories Pvt Ltd.

### Key standalone financial indicators - consolidated (audited)

<i>Revenue and profitability indicators-Figs are in LKR Mn</i>	FY14	FY15	FY16	FY17	FY18
Operating Income	3,993.47	4,602.43	5,860.22	6,299.91	7,955.28
OPBDITA	724.97	684.92	1,022.45	1,123.96	1,618.61
PAT	208.95	84.28	206.04	240.88	179.96
ROCE (%)	9.8%	5.9%	8.3%	7.0%	9.8%
NWC / OI(%)	12.86%	14.72%	14.55%	21.81%	21.85%
Total Debt	2,604.80	3,881.21	6,194.84	8,508.49	10,823.74
Networth	2,912.08	2,896.81	3,004.03	3,143.14	3,175.05
Gearing (x)	0.89	1.34	2.06	2.71	3.41
OPBDITA/Interest & Finance Charges(x)	3.59	2.40	2.75	2.49	2.12
Total Debt/OPBDITA (x)	3.59	5.67	6.06	7.57	6.69

### Rating history for last three years:

Instrument	Current Rating (FY2018)			Chronology of Rating History for the past 3 years		
	Type	Amount Rated(LKR MN)	Date & Rating in May 2018	Date & Rating in May 2017	Date & Rating in Feb 2016	NA
Issuer rating	N/A	N/A	[SL]BBB+ (Stable)	[SL]A- (Negative)	[SL]A- (Stable)	NA
Issue rating	Unsecured listed debenture	1,500	[SL]BBB+ (Stable)	[SL]A- (Negative)	[SL]A- (Stable)	NA

### ANALYST CONTACTS

**Mr. Sai Krishna,**  
+91-4445964304  
[Sai.Krishna@icraindia.com](mailto:Sai.Krishna@icraindia.com)

**Mr. Danushka Perera,**  
+94-77-4781591  
[danushka@icralanka.com](mailto:danushka@icralanka.com)

### RELATIONSHIP CONTACT

**Mr. W. Don Barnabas**  
+94 11 4339907  
[wdbarnabas@icralanka.com](mailto:wdbarnabas@icralanka.com)



*Subsidiary of*

**ICRA Limited**

*A Group Company of Moody's Investors Service*

CORPORATE OFFICE

Level 10, East Tower, World Trade Center, Colombo 01, Sri Lanka

Tel: +94 11 4339907; Fax: +94 11 2333307

Email: [info@icralanka.com](mailto:info@icralanka.com); Website: [www.icralanka.com](http://www.icralanka.com)

© Copyright, 2018 ICRA Lanka Limited. All Rights Reserved.

Contents may be used freely with due acknowledgement to ICRA Lanka.

ICRA Lanka ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. ICRA Lanka ratings are subject to a process of surveillance, which may lead to revision in ratings. An ICRA Lanka rating is a symbolic indicator of ICRA Lanka's current opinion on the relative capability of the issuer concerned to timely service debts and obligations, with reference to the instrument rated. Please visit our website [www.icralanka.com](http://www.icralanka.com) or contact ICRA Lanka's office for the latest information on ICRA Lanka ratings outstanding. All information contained herein has been obtained by ICRA Lanka from sources believed by it to be accurate and reliable, including the rated issuer. ICRA Lanka however has not conducted any audit of the rated issuer or of the information provided by it. While reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA Lanka in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. Also, ICRA Lanka or any of its group companies may have provided services other than rating to the issuer rated. All information contained herein must be construed solely as statements of opinion, and ICRA Lanka shall not be liable for any losses incurred by users from any use of this publication or its contents