

## Profitability of hospitals touch a multi-year low: ICRA

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The health of the hospital sector has been deteriorating since early CY2017 due to several factors that have adversely affected its profitability.

These include the implementation of the Goods and Services Tax (GST), cap on prices of stents and knee implants by the National Pharmaceutical Pricing Authority (NPPA) and; stiff regulatory actions by certain states, including putting restrictions on procedure rates, levying penalties and placing operational limitations on erring hospitals.

Though the aggregate revenues of ICRA's sample set have grown by 9%, from Rs. 132.6 billion in FY2017 to Rs. 144.9 billion in FY2018, the operating profit before interest, tax, depreciation and amortisation (OPBITDA) has dropped by ~4%, from Rs. 17.3 billion to Rs. 16.6 billion, this being the first fall in aggregate OPBITDA in the last six years.

Further, the operating profitability margin has declined from 13% in FY2017 to 11.4% in FY2018, the lowest in more than six years; the highest was 15.7% during this period. Hospital chains with a large presence in the National Capital Region (NCR) have seen the sharpest dip in the OPBITDA (up to 21%) due to additional Government restrictions placed on certain players, following media reports on alleged cases of medical negligence and overcharging.

ICRA note mentions that on the operational front, all players faced pricing pressure in FY2018, primarily due to restrictions placed by the NPPA in February 2017 and August 2017. Consequently, ARPOB of the sample set has grown by a muted 3% in FY2018, the lowest growth rate in last five years and much below the five-year compounded annual growth rate (CGAR) of ~7.2%.

The aggregate number of operational beds has gone up by 6%, from 19621 beds in FY2017 to 20825 beds in FY2018. The growth in occupied bed nights has been muted, at 4%, and the aggregate occupancy level has dropped during this period, from 61.5% to 60.4%, due to the sharp fall in occupancy for one of the largest hospital chains which, in addition to other

regulatory measures, has also been impacted due to alleged cases of medical negligence/overcharging and internal challenges. Excluding this, the occupied bed nights of the sample set have grown at a healthy 7% and despite the increase in bed capacity the occupancy level has been stable, at ~58.5%, indicating satisfactory volume growth.

The regulatory environment continues to be the overarching challenge for the hospital sector. The NPPA has already published two office memorandums in CY2018 which indicates additional pricing restrictions. Further, the Governments of West Bengal and Karnataka have implemented the Clinical Establishment Acts in 2017 to overhaul the regulatory mechanism for the sector, setting up of a grievance redressal mechanism, fixing the procedure rates and laying down the criterion for levying penalties on hospitals.

“The proposed regulatory action from the Government of National Capital Territory of Delhi (GNCTD) and the Niti Aayog may further impact the margins going forward. ICRA expects that within the industry, hospitals based in the NCR are likely to face maximum pressure due to the sweeping changes proposed by the GNCTD,” said Mr. Banga.

On account of the increase in debt and pressure on OPBITDA, the interest coverage ratio of the sample set has dropped from 2.73 times in FY2017 to 2.44 times in FY2018. Consequently, the net debt/OPBITDA has deteriorated from 3.08 times as on March 31, 2017 to 3.33 times as on March 31, 2018. The aggregate debt coverage indicators of the sample set include the impact of non-hospital businesses as well, such as standalone pharmacies and diagnostics services, which have fared much better.