Apollo Hospitals Enterprise Limited

Q3 FY23 Earnings Conference Call Transcript

February 15, 2023

Moderator: Ladies and gentlemen, good day and welcome to Apollo Hospitals Limited Q3 FY23 earnings conference call. As a reminder, all the participants' lines will be in the listen-only mode, and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" then "0" on your touch-tone phone. Please note that this conference is being recorded.

I now hand the conference over to Mr. Mayank Vaswani from CDR India. Thank you and over to you, sir.

Mayank Vaswani: Good afternoon everyone and thank you for joining us on this call to discuss the financial results of Apollo Hospitals for Q3 and the 9M of FY23, which were announced yesterday. We have with us today the senior management team comprising Ms. Suneeta Reddy – Managing Director; Dr. Hariprasad – President of the Hospitals Division; Mr. A. Krishnan – Group CFO; Mr. C. Chandra Sekhar – CEO of AHLL; Mr. Obul Reddy – CFO of the Pharmacy Division; and Mr. Sanjiv Gupta – CFO of Apollo 24/7.

Before we begin, I would like to mention that some of the statements made in today's discussion may be forward-looking in nature and may involve risks and uncertainties. Please note the disclaimer mentioning these risks and uncertainties on Slide #2 of the investor presentation shared with all of you earlier. Documents relating to our financial performance have been circulated and these have also been uploaded on the corporate website and the websites of the respective stock exchanges.

I would now like to turn the call over to Ms. Suneeta Reddy for her opening remarks. Thank you and over to you, ma'am.

Suneeta Reddy: Good afternoon everyone and thank you for taking time out for this earnings call. I hope that you have received the earnings documents which we had shared yesterday.

We have delivered a steady performance in Q3 FY23 with the Healthcare Services business growing at 10% year-on-year excluding vaccines. Growth was driven by an increase in IP volumes which were 7% higher year-on-year and supported by pricing and case mix gains. ARPOB has increased 12% year-on-year and it is currently at Rs. 51,482 in Q3. It is important to note that we had reported 41% revenue growth last year Q3 FY22 which was aided by COVID revenues and vaccination revenues, which was ahead of the industry growth. In the light of the high base, the 10% year-on-year growth in Healthcare revenues is meaningful and adjusted for nonrecurring COVID revenues and vaccine revenues on a like-to-like growth in the Healthcare Services business is at 17% year-on-year.

Q3 FY23 occupancy across the group was 65%. The Q3 FY23 occupancy in mature hospitals is 66% and new hospitals is 62%. We witnessed an improvement in the payer mix too as cash and insurance segments registered a year-on-year improvement of 28% in revenues.

Against this backdrop, let me take you through the consolidated financials for the quarter:

Consolidated revenues grew 19% on a year-on-year basis to Rs. 4,264 crore after normalizing for vaccine revenues in quarter 3 last year. Healthcare Services revenue grew 10% to Rs. 2,194 crore. HealthCo revenue grew by 34% on a year-on-year basis to Rs. 1,758 crore. Offline pharmacy distribution revenue grew 21% year-on-year to Rs. 1,581 crore. Online pharmacy distribution and 24/7 revenue was at Rs. 178 crore.

Combined pharmacy revenue grew by a healthy 31% on a year-on-year basis. AHLL revenue stood at Rs. 311 crore. Excluding COVID vaccination and testing, it grew by 30% on a year-on-year basis. Diagnostics core revenue grew by 62% on a year-on-year basis to Rs. 92 crore in Q3 FY23.

Healthcare Services EBITDA was at Rs. 543 crore, a year-on-year growth of 9%. This was supported by volume, price, and case mix improvement. Healthcare Services EBITDA margin was at 24.7%, a 15 basis points improvement over last year. Margins in mature hospitals were at 27.5% as against 25.6% in Q3 FY22. Margins in new hospitals stood at 18.2% for the quarter.

EBITDA for the offline pharmacy distribution business was at Rs. 124 crore for the quarter, representing a growth of 28%. The online pharmacy distribution and 24/7 business reported an EBITDA loss of Rs. 186 crore, resulting in a net loss of Rs. 63 crore for Apollo HealthCo. AHLL recorded an EBITDA of Rs. 25 crore for the quarter. Overall consolidated EBITDA was at Rs. 505 crore, reflecting the investments that we have made in the online business.

At the PAT level, Healthcare Services PAT was at Rs. 261 crore, a year-on-year growth of 30%. Consolidated PAT, however, was at Rs. 153 crore.

I will now summarize the performance for the 9 months ending December 2022:

We closed the 9 months of FY23 with a consolidated revenue of Rs. 12,310 crore, a growth of 16% over the 9 months of FY22, excluding revenue from vaccination. This includes a revenue growth of 12% year-on-year in the Healthcare Services business and in AHLL and 23% growth in Apollo HealthCo. EBITDA stood at Rs. 1,561 crore. Within this, Healthcare Services EBITDA was Rs. 1,598 crore. EBITDA from mature hospitals increased by 25% year-on-year, with an increase in the EBITDA margin to 27.4% from 24.3% in the 9 months of FY22. PAT for the 9 months of FY23 stood at Rs. 675 crore.

In operating terms, the offline pharmacy business added 194 net new stores for the quarter, taking the network to 5,196 stores, with private label sales at 11.03%. The online pharmacy distribution in 24/7 platform recorded a strong GMV growth of 85% quarter-on-quarter to Rs. 543 crore. The platform added 3 million users this quarter, and its total users as of date is 23 million users. The platform witnessed around 42,000 transactions per day compared to the 25,000 transactions in March 2022.

This has been a good quarter for our Healthcare Services business. Our occupancy and volume levels are robust and our margins have expanded. There is still room for growth in both the mature and new hospitals as surgical cases increased and international patients returned. We continue to focus on the centers of excellence, case mix, and payer mix as levers for revenue and EBITDA growth.

AHLL has demonstrated resilience in a quarter that was muted for the sector. Our penetration and growth plans for primary care and diagnostics will continue, and we will see improvements in EBITDA and margin profile.

Apollo HealthCo has done really well on the pharmacy distribution revenue and GMV growth and operating metrics. It is on track to exceed Rs. 1,500 crore of GMV this fiscal and well ahead of the information memorandum to deliver 2x growth in FY24. We believe we are at the peak burn rate this quarter and expect losses to moderate from here on. Margins in Apollo HealthCo will improve with the offline pharmacy distribution margins improving as well as discount rationalization, digital health services revenue improvement, and expansion of private label sales. We expect HealthCo to directionally be PAT neutral by the end of FY24 and become the fastest digital player to achieve segment profitability by FY25.

In the larger context, while individual business verticals are all delivering to pan, the largest opportunity for us is the network effect. It's really leveraging the synergies across all the formats in both the physical and digital touch points that we have created. We are the only 360-degree integrated healthcare ecosystem and our clinical proposition remains strong. I believe that we have put a lot of work into our strategy not just for this year but for the coming 24 months and we look forward to our next call to see it play out over the next 24 months.

Meanwhile, I have Dr. Hariprasad; our CFO – Krishnan; Obul Reddy; Chandra Sekhar from AHLL; and Sanjiv from 24/7 to take questions from all of you.

Moderator: We will now begin the question & answer session. The first question is from the line of Anuj Suneja from ICICI Prudential. Please go ahead.

Anuj Suneja: I have a couple of questions mostly related to 24/7 expenses. One, I would like to understand what is the breakup of the expense at Rs. 134 crore that we are doing. Is it just going to discounts or is there any other strategic initiative that is also being driven by this number? And going forward, you have given a guidance of Rs. 200 crore for H1. If you are giving the breakup right now, what would be the breakup six months down the line? That's the first question.

Sanjiv Gupta: Let me just talk about the breakup of expenses that was your first question. As we spoke in the last earnings call, we talked about that the Company is investing in the resources and tech and products side for the new line of businesses which it intends to start. As you recall, pharmacy, diagnostic, and consultation are something which are the firing engines as of now. And during Q3, we invested into product and tech essentially and some bit on people resourcing for the new line of businesses. Essentially, that is where most of the incremental expenditure has happened. If I look at broadly about 30% of the expenditure is into product and tech side. We have about nearly 20% to 22% on the operations side. We do have marketing for acquisition of new customers to the tune of about 15% of expenditure, and something to do with the call centers and sustenance of communication and SMS and all that stuff another 15% to 20%, and the remaining expenditure happens towards the support side. So that's a broad breakup of the expenditure. And some bit of additional expenditure in Q3 is accounting for only related to the new line of businesses wherein we are putting money.

Anuj Suneja: And the second question is, we are reporting somewhere around Rs. 1,500 crore of GMV. What is the GMV to revenue bridge? And going forward, how would the EBITDA look like for this Rs. 1,500 crore of GMV? If we can have some thoughts on that.

Sanjiv Gupta: If you look at it, for the last quarter, we did a GMV of about Rs. 543 crore. And the revenue that comes to the books which is including of the online pharmacy and the take rate for the other services is about Rs. 177 crore. That is the ratio that we are looking at it. And yes, Rs. 1,500 crore, I think we should be doing more than Rs. 1,500 crore. Idea or rather the estimate at this stage is to hit around Rs. 1,600 crore, with another 2x growth for the next year. As far as the overall investment into the project is concerned, I think ma'am suggested this during her opening remarks also that we're looking at somewhere peak of the expenses as far as digital side is concerned. And next year in the Apollo HealthCo, somewhere in 3rd or 4th quarter, we are looking at coming to near breakeven.

Anuj Suneja: Any guidance on the EBITDA front? Say Rs. 1,500 crore to Rs. 177 crore of revenue. And beyond that, on EBITDA any guidance?

Sanjiv Gupta: As we get into the annual operating exercise for the next year and during this month and first half of the next month, there will be a detailed exercise done on this. And I think in the next earnings call, probably we can guide you on the digital side of the EBITDA also for the next year.

Moderator: The next question is from the line of Shyam Srinivasan from Goldman Sachs. Please go ahead.

Shyam Srinivasan: Thank you for taking my questions; the first one on the Hospital business. Occupancies on a blended basis have come off 300 basis points. I just want to understand how should we look at the quarter 4? And I think we had an earlier guidance of reaching higher occupancies. If you could just reiterate or at least observe what those occupancies are and what are our targets for the next, say, 12 to 18 months?

Suneeta Reddy: October to December are generally holiday months and I think the seasonality of the business is something that we have to consider and which is why our occupancies were around 64%. But having said that, they have picked up in February and March, and we expect to see a higher occupancy rate. Our target was 70% for the year. We will be close to 70%, especially for the last quarter.

Shyam Srinivasan: Ms. Suneeta, I think we had a longer-term goal also, right? I recollect because….

Suneeta Reddy: Yes, what we said was that our intention is to take it up to 75%. We do have a target for the next 18 months where we will do that. In fact, it is baked into next year's AOP. And hopefully, we will be able to commit to absolute numbers after the first quarter of next year is over.

Shyam Srinivasan: The second question is to the previous participant's question on revenue to GMV. While it is 33% conversion on the 24/7 this quarter, last quarter was 55% and the quarter before was 56%. Is there any change in how we now get our revenue or the conversion from GMV? Is there any marketplace that makes the take rate lower relative to previous quarters? Is it like are we now starting to recognize revenue from, say, the Amazon platform that is making this take rate lower?

Sanjiv Gupta: That's a good call out. This quarter, we started the entire IP/OP business for 24/7 users, and typically, it's a question of mix. What I would broadly say is that between 30% to 35% should be the revenue to GMV ratio which we see in this quarter should be the percentage that we can see in the next 1 or 2 quarters. And as we get into more of the digital therapeutics and insurance distribution side of it, probably this percentage will further go up. But for the current quarter Q4 as well as for Q1, let's assume in the range of about 35%.

Shyam Srinivasan: And Sanjiv, what is the mix of the revenue? If you could help us refresh that as well? How much from pharmacy, what is from consult? Because, the commentary seems to suggest that the growth has largely come from IP/OP, at least in the commentary on the presentation. If you could just give us a qualitative color, please.

Sanjiv Gupta: Yes, that's true. Most of the growth has come from the IP/OP business, this is the new vertical that we started in Q3. If you read through the Q2 transcript, we said that we would be investing into the customer journeys for the users who can come from Apollo 24/7 and then get the physical bookings as well as get the IP and the other things done. For Q3, a little distortion because a new vertical whenever it comes and starts firing, the percentage mix changes. But for Q3 if I talk about, pharma is about 50% and consultation together with IP/OP is about 45% and the rest is Diagnostic and VC, virtual consultations.

Shyam Srinivasan: And this mix for 1H was what?

Sanjiv Gupta: Mix of H1 was, about 80% is pharma and then we had about 10% of consultation and about similar 10% for diagnostic and the subscription and pay model.

Shyam Srinivasan: My last question is on the pharmacy business. Both in terms of network addition, just a simple observation; we used to add 350 stores annually in the past years, we have now added 757 in 9 months, but now the number of closures is also equal to like one-third of how much we were adding earlier. Is there any change in the philosophy? Why are we closing more stores? Maybe it's a percentage of new stores added, but I just wanted to get the philosophy there. And also a data point on what is the combined pharmacy EBITDA margins? I think you were disclosing it until last quarter, I can't see it in the presentation for this quarter.

Obul Reddy: This year, we embarked on additional stores and expect to open for the full year about 950 stores, and we closed around 100 stores which is more on the basis of identifying them as nonperforming, not that it is as a percentage to the store additions. And on the EBITDA, it is about 7.38% on the pharmacy business, slightly about, say, 50 to 60 basis points lesser than last quarter and largely because of the establishment costs on the addition of stores. And the growth coming from these new stores in the next 2 quarters, that will considerably change.

Moderator: The next question is from the line of Damayanti Kerai from HSBC. Please go ahead.

Damayanti Kerai: My first question is on your Hospital business. How much is International patient contribution during the quarter? And how do you see this piece moving, say, next few quarters?

Suneeta Reddy: We have moved from 5% last quarter to 7%, and our focus is that it will be 10% in the last quarter.

Damayanti Kerai: 10% by the end of this fiscal?

Suneeta Reddy: End of this fiscal, yes.

Damayanti Kerai: Ma'am, my second question is on hospitals again. We have seen improvement in the AP & Telangana cluster which has seen a good pickup in the third quarter. Among your all cluster hospitals, which are the segments where you see enough headroom to improve on the payer mix, etc.? I think last quarter you talked about AP & Telangana. Apart from this, which are the segments where you see you are not yet targeted payer mix payable?

Suneeta Reddy: So we are looking at some of the new hospitals which are now ready to ramp up. I think we had moved the whole strategy from being primary and secondary care to tertiary care. And with this offering of tertiary care, we should be clinically differentiated in these markets. So, you will see improvement in Vizag, you will see improvement in Madurai and Trichy, and Navi Mumbai coming through in the last quarter.

Damayanti Kerai: Ma'am, my next question is on your cost improvement plan for your business. You earlier mentioned some 100 to 150 basis point improvement over the next 18 months. If you can provide an update on that. And which are the key drivers for this cost improvement?

Suneeta Reddy: I think we are pretty consistent with what we hope to achieve. You will most probably see it at the end of 2023-24. What are the drivers for this; - clearly, we are looking at creating surgical packages, kitting it out. We are also looking at admin costs. We are looking at HR costs as well. But more importantly, I think the whole initiative is about improving the overall efficiencies within the system, so conversions happen at a better rate. It's also about growing revenues as well as cutting costs. So, I think it's a very crucial program for Apollo, and we will deliver on both revenues, volumes, and EBITDA margins.

Damayanti Kerai: My last question is, can you specify at your network level, what is the contribution from cash, TPA as of third quarter in terms of your payer mix? If you can call out a number?

Krishnan A: Almost around 80% is from cash and insurance.

Damayanti Kerai: And within that, I assume around 50% is cash and another 50% TPA. There is equal contribution or how is the status?

Management: Yes, equal contribution.

Moderator: The next question is from the line of Shaleen Kumar from UBS Securities. Please go ahead.

Shaleen Kumar: Since, on 24/7, the nature of GMV has changed a bit, is it possible to get a like-to-like comparison of GMV? If I have to see my previous Q2 GMV versus Q3 GMV, how the growth has been?

Sanjiv Gupta: Q2 GMV was Rs. 295 crore and like-to-like comparison would be about Rs. 340 crore; that would be up by about 15%. That is like-to-like. Like-to-like here means pharmacy, consultation, and diagnostics.

Shaleen Kumar: But then, basically the new GMV contribution to revenue is quite less because if I look at the revenue growth, it's also somewhere around that, right? 12% to 15% kind of a revenue growth is there sequentially.

Sanjiv Gupta: Yes, the observation is right. And this was one of the questions asked previously also. Whenever a new engine fires, the entire mix undergoes change and that leads to change in the mix. I think it is all temp from that sense. But as we see another one or two quarters, we are coming out with new lines of the businesses, this will continue to be slightly different before it starts maturing on 1%.

Shaleen Kumar: So, we intend to increase our contribution margin from that or there is a scope for that?

Sanjiv Gupta: Absolutely. That's the constant endeavor to reduce expenses and increase your top line as well as the margin.

Shaleen Kumar: Just one bookkeeping question. There is a cost related to JV and associate. Just trying to understand what is it pertaining to? Is it one-off or it will be sustained or something like that, around Rs. 21 crore?

Krishnan A: That is the consolidation of the front-end pharmacy business. There is this establishment cost also, which as Obul said, as part of those costs which is getting consolidated.

Shaleen Kumar: Will it be at this level?

Krishnan A: No, it will come down as some of that starts maturing.

Moderator: The next question is from the line of Harith Ahamed from Avendus Spark. Please go ahead.

Harith Ahamed: I was looking at AHLL and within AHLL the diagnostics segment. We have seen a sequential decline in margins this quarter at around 5% which is a sharp decline versus the second quarter. Are there any one-offs? And what's the number that we should expect for this segment going forward?

Obul Reddy: On an even basis, I think this YTD number stacks to the range of 8% to 8.5%. These are turnover discounts and such other one-offs that have spiked the Q2, but they pertain to both the Q1 and Q2 overall. So, we sequentially record them as and when such credits come our way. The overall outlook this quarter has been muted in line with the overall industry trend. There is a Rs. 10 crore approximate drop between quarters, and that contributes to about Rs. 6 crore to Rs. 6.5 crore of EBITDA for us considering that the fixed costs are covered. So, on an even basis on a steady state, we are hoping to be in the 8.5% to 10% mark this year. We are continuously growing. So, our move from 10% onwards is something that we are planning to achieve next year as we start realizing the front-loaded costs and thereof the revenues from areas such as specialized testing and such. That's the broad growth path.

Harith Ahamed: And to a previous participant's question, you mentioned that the like-to-like GMV for the quarter is around Rs. 350 crore while what you disclosed is around Rs. 540 crore. What exactly accounts for the difference between these two numbers?

Sanjiv Gupta: I think this is pertaining to 227 wherein they want to check on the increase in the new admissions. So, during Q3, we started opening up the customer journeys for booking of physical appointments for hospitals across the full ecosystem as well as helping the customers to get the radiology, pathology, and the other IP-related items. And I am happy to share some broad numbers. Monthly, we have on an average 2 lakh leads that we get for the OP/IP business and about 22% is the current conversion leading to the OP side of it and about 6% to 7% conversion from there towards the IP side of it. That is the line of business that we started. Q2, we spent some money into it building up the tech and products side of it, and Q3 essentially came realizing the entire GMV. Put together, about Rs. 200 crore worth of GMV what we got for the Q3. That's the incremental versus Q2.

Harith Ahamed: For the combined pharmacy revenue that you have disclosed for the quarter, around Rs. 2,175 crore, is there an offline and online breakup for this number that you can share, like we have for the pharmacy distribution?

Obul Reddy: It's about 9% of the revenues coming from online, rest is offline. As a number, it is Rs. 1,963 crore from offline, Rs. 204 crore from online. Together, it is Rs. 2,167 crore.

Harith Ahamed: And last one with your permission. Can you help us with the timelines around some of our bed additions expected over the next 2 or 3 years? How should we think about the number of beds from the current 7,855, let's say for FY25 and FY26?

Suneeta Reddy: In terms of bed addition, I think that our short-term challenges on the current bed addition, let's move to 70% occupancy. Over a 24-month period, we are looking at adding beds. There will be 2 brownfields in Bengaluru, which will give us another 400 beds. Adding on to this, which is more of from FY25 onwards, you will see beds added in both Chennai OMR, a large hospital, as well as Gurgaon which will come in the year 2025. With that, we will have an additional 1,000 beds in that year. Our plan is really to go to 2,000 beds in the next 3 to 4 years with a capital outlay of Rs. 3,000 crore.

Moderator: The next question is from the line of Tushar Manudhane from Motilal Oswal Financial Services. Please go ahead.

Tushar Manudhane: Again, on the GMV, while the rate has been quite exponential over the past year or so and you have given the guidance for FY23 as well, but if you can take this forward for the next 12 to 15 months in FY24, how do you see this GMV moving?

Sanjiv Gupta: Rs. 1,600 crore roughly that we are going to hit this year, truly 2x growth in any case we will have in the next year. That would be anything over and about Rs. 3,200 crore to Rs. 3,300 crore. However, as I said previously that our annual operating plan exercise just initiated and from now to till 15th of March, we have detailed workings around it. Probably a bit more color we will have in the next earnings call. But for now, you can think as 2x growth for the next year.

Tushar Manudhane: And on the offline pharmacy side, while the store addition has been quite aggressive over 9 months, but particularly in 3Q, the offline pharmacy sales growth has been much higher at 22%. It was just 8% for the first half of FY23. Anything in particular in this quarter to highlight?

Obul Reddy: We have also added a similar number of stores in the Q1 and Q2, which have started contributing to the sales and the growth is there.

Tushar Manudhane: On the current base, even to grow by 15% to 18%, almost 1,000 stores at least to be added every year. Is that the number to go by in the coming years?

Obul Reddy: No, with the 1,000 stores, we are growing at 24%. At 21% to 22%, we will have normal 500 stores addition. And the growth coming from this will be sufficient for us for the next 2 years.

Tushar Manudhane: Lastly, the private label as a portion still remains relatively low. Any efforts out there to improve that?

Obul Reddy: Number 1, the stores are increasing and the new stores, it will be slightly less for some period. Number 2, if you go back to the earlier period, there was a lot of COVID portfolio which is not there currently. So, we are seeing like-to-like on these SKUs volume growth. So, maybe it will take another two quarters for us to show the growth on this from hereon.

Moderator: The next question is from the line of Kunal Randeria from Nuvama. Please go ahead.

Kunal Randeria: Sir, my first question is on the 24/7 business. If I were to look at your revenues, it has grown from around Rs. 120-odd crore in Q1 to around Rs. 175 crore in Q3. But at the same time, the OpEx that you are doing has grown in almost exactly the same proportion, which is at 100% of your revenues. I am just wondering, going forward, assuming that the revenues will be more than double in 1 to 1.5 years' time, which cost items can be controlled so that as ma'am mentioned, you can also turn profitable?

Sanjiv Gupta: I think what we need to actually look at is that now we are in the fourth year; on 5th of February, we stepped into fourth year. It is something like one of the fitness centers have this traditional line that Today's Pain, Tomorrow's Gain. I think more or less, we are off the mark of putting up more investment into the tech and the products side. I think our app, websites, our individual customer journeys within, and the entire integration with the service providers, all that is more or less done. 1) That means going forward, as we scale up and as we get more GMV and more revenue, my cost with respect to product and tech will not be in that proportion. 2) On the resources side also, we are adequately staffed, so does the office infrastructure and the other things. I think what we can clearly save further on the existing costs is the discretionary expenditure on the marketing side of it, which is to do with the branding. And I would just recall this point a couple of earnings calls back I had talked about this is that the users were also to be talked about various benefits that they can get from the Apollo 24/7 app. To that extent, we had to do a lot of campaigns and marketing to make them aware about the fact that you can now easily put your medicines on the app, you can get the diagnostics done through the app, you can get the consultations, physical bookings, so on and so forth. All that is something which is now passed and all that expenditure is kind of a discretionary expenditure today. So cut short, moving forward, we would get more scale on a very low incremental cost, and we would have higher margins. So, we should be able to do a better job as far as the EBITDA side is concerned. So, the possibility is very high to do a pretty good job in the next fiscal year for the EBITDA line for the digital side.

Kunal Randeria: Sir, I need to understand this, maybe, a bit more. Would it be fair to assume that you are now at a tipping point where, let's say, for the next Rs. 100 crore in quarterly revenue, you need not spend Rs. 100 crore and spend maybe Rs. 40 crore or Rs. 50 crore to achieve the Rs. 100 crore revenue?

Sanjiv Gupta: Absolutely. I don't know about 40 or 50, but absolutely. Now the scale that we have it, we don't spend a lot of dollars to fulfill the upside on the revenue. The system itself, the engine itself will take care of the additional revenues without any additional cost.

Kunal Randeria: And this we should see from the coming quarter or it will be in the next fiscal?

Sanjiv Gupta: No, I think some benefit we will start seeing it from Q1 itself and those benefits will start coming down as we move forward beyond Q1.

Kunal Randeria: Just one quick question on the Hospitals side. Your ARPOBs are close to Rs. 60,000 in metros. Just wondering what the headroom over here is, especially considering that you already have 80% of patients from cash/TPA, which is almost at an optimum level. So, what kind of ARPOB growth we should assume in the coming years?

Krishnan A: We will continue to go with what we have been doing in the past. I think a combination of case mix and price increase is what you should factor in. You are right, we have not been guiding you for towards anything specific around change in payer mix. We will continue to work on the payer mix, but as Ms. Suneeta said, the payer mix opportunity still exists in non-metros, which is what we are focusing on. In the metro cities, we would not have much of payer mix opportunities. So, you should look at the ARPOB growth of around 8% CAGR. This is a combination of 4% to 5% on pricing and the balance on case mix.

Moderator: The next question is from the line of Rishabh Tiwari from Allegro Capital. Please go ahead.

Rishabh Tiwari: What was the combined pharmacy EBITDA number for this quarter? I think it was not mentioned in the presentation this time.

Krishnan A: Yes, that was missed in the presentation. We will put up the presentation with the number; 7.4% is the number.

Rishabh Tiwari: Also, I am not sure if this is a miss. The number of new hospitals has been brought down to 14 from earlier 15.

Krishnan A: There was one hospital which got transferred. There was a Karapakkam Center in Chennai, which got transferred to Apollo Health & Lifestyle. This is the hospital which was within the AHEL books, which got transferred to Apollo Health & Lifestyle. That's a Cradle business that we had within Apollo, which got transferred to Apollo Health & Lifestyle. That's why it has gone lower by one.

Rishabh Tiwari: And since you mentioned AHEL, does the management see any specific guidelines regarding the margins going down in AHEL?

C. Chandra Sekhar: The quarter 3 margins at a consol level, we are at about 10% at this point of time on a YTD basis. On Quarter 3, I think we are lower essentially because of the aberration on account of in October, which actually dragged us into a negative EBITDA zone. And November was a muted recovery. So, it is not very representative of where we stand in terms of how the businesses are performing. Having said that, despite these seasonal fluctuations, I think the revenue buildups have been, especially in the 4 businesses minus the vaccines and the COVID testings which were one-offs, continues to be a robust growth. So, we are hoping to have a sequential improvement quarter-on-quarter on our margin profile going forward because we are also controlling some of our costs as we are on a growth path both in primary care and diagnostics. These are likely to remain a little muted for some more quarters in comparison to the industry.

Moderator: The next question is from the line of Nitin Agarwal from DAM Capital. Please go ahead.

Nitin Agarwal: Sir, two questions. One is on the pharmacy business. On the offline pharmacy piece, what kind of growth rate can we assume for the next, say, 2 to 3 years? And do we see incremental operating leverage on the margins on this revenue growth?

Obul Reddy: Very difficult to guide you for the next 2 to 3 years. At least next 12 months, we expect to be in the range of 22% to 24% given that we have invested in the growth during the current year.

Nitin Agarwal: And sir, on the margins, we have been kind of flattish to a little muted on the margins for the business versus our trend that we have been consistently increasing these margins in the past.

Obul Reddy: The margins as we have last guided you, we expected that customer discounts will be in the range of about 13.5%. But we could see a big round. It is moving to 14.5%. So, we are largely muted on the margin. Whatever increase in the customer discounts, we were able to manage through the additional procurement margin, but still there is about 30 to 40 basis points impact on the EBITDA. We will be managing that at this level because now we are at about 14.5% on the customer discounts, which we consider very decent for the off market to sustain the growth.

Nitin Agarwal: And secondly, Sanjiv, on the online business, we have talked about the HealthCo being PAT positive or EBITDA neutral by the second half next year. When does the online piece on its own start to become EBITDA neutral in your assessment?

Sanjiv Gupta: That would take a little bit of time. I don't see that to happen in the calendar year of 2025 but somewhere in the fiscal year of FY25, maybe in the last quarter. That should be the time when we should see this segment as becoming profitable. There are a couple of engines that we need to fire. We are working on them. Potential is huge. And if you are able to execute well, which we believe that the current set of team members would be able to do well. Once we do that, I think we should be able to give you a better guidance on the timeline, but FY25 should be the year where we should think that digital would also be, as a segment, EBITDA neutral.

Nitin Agarwal: This is towards the end of FY25?

Sanjiv Gupta: That's right.

Nitin Agarwal: And we talked about the doubling of revenues on this business next year. And I think earlier we talked about $1 billion in revenues in this business in the next, I think, 2 years or 3 years. So if you can refresh on the revenue targets for the online business, by when do you get to the $1 billion number or thereabout?

Sanjiv Gupta: I think FY25 should be the year when we should look at numbers closer to $800 million to $1 billion. And that is the scale which is required to ensure that you have a high repeat rate, you have a high net margins and you are able to leverage on your fixed expenses and so you are able to do justice to the entire economics. So, I guess, as I said that next year the numbers are still to be worked upon, but if you are looking at roughly 2x growth and another similar growth for a year thereafter, I think FY25 should be the year to get near the $1 billion mark.

Nitin Agarwal: What kind of margin this business you should be ideally making at the size?

Sanjiv Gupta: I think anything around 20% should be the margin that you should get it as a blended margin. It all depends upon the mix that comes. A little difficult for me to give you one number, but yes, anything between 20% to 25% should be the mark.

Nitin Agarwal: Our operating cost, you said, is probably getting to a point where it will start to plateau out beyond a point after some time versus the current base that we have built in.

Sanjiv Gupta: Yes, absolutely. Pretty much it's a fixed expenditure. Once you have a tech product done, then it is just a maintenance cost. And digital platforms help you to get to the scale faster. But yes, in the initial years, there is a pain with respect to putting up expenses and putting up lot of infrastructure there. But at that scale, from next year onwards, I don't see that expenses going up substantially. They will start getting plateaued and we would also do a certain bit of rationalization given the fact that we understand the external environment and what are the right decisions to be taken for the business. And I think those business decisions would also be implemented and executed. So, I think a mix of everything, but yes, expenses are plateauing there.

Nitin Agarwal: On the Diagnostics business, I think we have had, from an industry participant perspective, a lot of mixed commentary around the outlook for the organized business in the near to medium term. Mr. Chandra Sekhar, how are you looking at the dynamics of the business? Are there some challenges on the organized sector volume growth or that's sort of come up over the last few quarters?

C. Chandra Sekhar: I think there has been more than normal competitive intensity for the digital aggregators. But the way I see it is this is on the top 20 to 25, if not 30, frequently used tests which form the bucket of routine. I guess the competition is intense there and so I believe that it's going to remain that way for a while. But I think the focus of the more organized larger players and rightly so will shift to more specialized and more high-end testing and also towards packages with an emphasis on quality because at the end of the day, I think 95% of all clinical decisions are taken on the basis of these diagnostic tests. So, it's important to also bring up the topic of quality. There is a cost to it. So, I think pricing for organized players in terms of responding to such competitive pricing from digital aggregators is not likely. There could be some short-term dips in volumes in the routine basket, but the endeavor for the organized sector will be to make up for that through other semi-specialized, specialized, and super-specialized buckets. That's I think the outlook that I think we will see. But this will settle down.

Nitin Agarwal: There has been a lot of emphasis on selling bundled packages versus specific illness tests. Is this a strategy that we are also following in terms of trying to increase our share of bundled tests?

C. Chandra Sekhar: We are following that. In another business which is not reported in the Diagnostics actually is the Clinics business which is in the Primary Care. I think we will do a lot of health checks. I think 60% of the business there comes out of health checks, which essentially also has a radiology component but essentially a lot of pathology. But within the Diagnostic business like-to-like in comparison to other larger organized players, our wellness packages are now around 7% to 8% of our mix. We are hoping to make this go to 20%, and that will offset this very stark comparison in terms of a-la-carte testing.

Moderator: The next question is from the line of Sayantan Maji from Credit Suisse. Please go ahead.

Sayantan Maji: My first question is on discounting levels. You mentioned that discounting level has increased from 13% to 13.5% to 14.5%. Can you give us a split of your discounting level in offline and online pharmacy? And if this increase is happening in online pharmacies, do you see an increasing discounting pressure again in this segment, which is causing the higher discounting level? And also, can you update on the Amazon partnership?

Obul Reddy: The online discounts are at about 18% to 18.5% like last quarter. It is only offline which moved slightly. And on the Amazon, Mr. Sanjiv will comment.

Sanjiv Gupta: Before Amazon, I think we guided on the online discounts that we would retain our 18% mark. YTD December has been 17.6% although the last quarter was 17.8%. We will continue to maintain discounts near 18% and we will also time our discounts in such a way that wherever opportunities are there to reduce it, we will continue to do that or sustain at this level. On Amazon, we are now live with 15 stores and current rate is around 3,000 orders per day. We couldn't increase the run rate in the middle of the year due to tech integration issues which we had between us and Amazon, but now those have been resolved. And there has been a little bit of network expansion also to take care of Amazon operations. And in the next 4 weeks, we would see that Amazon customers would be able to see breadth and depth of inventory across the top 6 cities to start with. And there is a little bit of marketing activity also in Amazon app that has started over the last 3 to 4 weeks. And what we believe that we should be able to hit a $10,000 per day somewhere in July or August of the current year.

Sayantan Maji: Are we doing a revenue-sharing arrangement here? Or is it on a profit-sharing basis?

Sanjiv Gupta: It's a revenue share.

Sayantan Maji: My second question is on a little clarification on the new GMV. This hospital IP/OP segment, is it the same customers who are coming, they are basically being converted online or is this a new set of customers that you are targeting here? Can you explain a bit about this IP/OP segment?

Sanjiv Gupta: Yes. This is a new set of customers. Obviously, there is no point in having the same customers both sides; it is a new set of customers. The way the entire operational side of it works is that; one is that we have integrated our 24/7 app with the entire

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Apollo ecosystem where we have about 55 participating hospitals which in the current quarter will go to 70; and second, there is an engine that works behind all this. People who search out surgeries, say suppose say knee surgeries or some kind of surgeries online, googling and all that stuff. Those are the data points that we collect. And then those are the curative leads that we use to further engage with them. As I said, the monthly average for Q3 was about 2 lakhs leads that we got from various, I would say, websites or the places where digital customers were trying to find out about those surgeries. And those 2 lakh leads were then kind of, we engaged with them through tele calling and through various nudges that we do it from Apollo 24/7 and finally we converted about 22%, 22.54% to be very precise, for the last quarter and about 45,000 customers went on during the month of December to the hospitals and they got the OP consultations done, and from there, about 2,500 people got the surgeries done. This is all is well managed and a curated engine and then you have got many apps out there in the market who does this kind of work wherein they identify people who are digitally looking out solutions around surgery and those are the leads that we get, those are the leads we further cure and then we further kind of engage with them to get into this side of the business. It's all very different. I can discuss a lot more, but in the interest of time cannot discuss much about it, but happy to engage with you one-on-one whenever you want a bit more information about this.

Sayantan Maji: No, that's very clear; that explains. And finally, just wanted to check what will be the loss run rate for Apollo 24/7 going ahead now that we have peaked?

Sanjiv Gupta: First of all, we are cognizant to the fact that somewhere we need to convert the entire thing to EBITDA positive. And we are also looking at how we build our plan for the next year, which are the segments that need to fire more, and where exactly we need to do incremental investment. And all this will result into a detailed exercise of building our budget for the next financial year. And accordingly, we will get to know about the expenses that we feel appropriate for the business. And accordingly, we will have a little more color on this. Maybe next earnings call will be the right time to discuss about this by quarter; in fact, for the entire year, we can talk a lot more in the next earnings call. So, I would just request you to wait for some more time before we dialogue on this.

Moderator: The next question is from the line of Bhagwan Chodhary from Sunidhi Securities. Please go ahead.

Bhagwan Chodhary: Sir, one question on the Healthcare side. Can you comment something on the future capex side how we are going to do this, as we are going to generate a lot of cash, Rs. 1,500 crore to Rs. 2,000 crore kind of or so? Can you comment something on that?

Krishnan A: Clearly, the plan, as Ms. Suneeta has already articulated, is to get to an additional 2,000 beds over the next 3 years. And we have a clear plan on our road map and where we are adding that. And the free cash flow, as you already know, is around Rs. 800-plus crore that we have in this segment across, and we will deploy this into some of them. We don't think we are going to be requiring significant incremental debt. Whatever is required, we will take some debt. Debt/EBITDA is also very comfortable, as you have seen.

Bhagwan Chodhary: And this will be organic or inorganic? How it is going to be?

Krishnan A: There will be some inorganic, some bolt-on acquisitions that we are looking at and also greenfield.

Bhagwan Chodhary: And secondly, can you talk about this performance of Proton, how that is doing?

Krishnan A: Proton is doing much better now. We are on track to get to Rs. 50 crore of EBITDA in this year. And we would like it to double in the next year. That's our plan.

Bhagwan Chodhary: Finally, an observation on the Slide #19 where you have detailed these pharmacies across India in all the States. But there is no pharmacy in Madhya Pradesh. Any particular reason for that?

Obul Reddy: We don't have logistic support. We are planning in the next year. We need to set up a back-end support system before we open the retail pharmacies. Just working on that. You could see next year some pharmacies there.

Moderator: The next question is from the line of Neha Manpuria from Bank of America. Please go ahead.

Neha Manpuria: Sir, on the GMV increase that we have seen; I understand that obviously a lot of this gets monetized in other parts of the Apollo value chain. But for Apollo Digital itself, is it fair to assume that these would just be leads which help the Hospital business and Diagnostic business and not so much the Apollo 24/7 and therefore the take rate would remain in the mid-30 level?

Sanjiv Gupta: No, there's no free lunch. There is a highest board governance and the things at various entities of Apollo and we got Deloitte as auditors and we got PwC who is helping us on the arms' length pricing. As I said, there are no free lunches. As we start ramping up our business, soon the take rate will also go up. And classic example is, Diagnostic; we started our journey with about less than 10% discount. Today, we are near 17% to 18% discount, and as we grow business, more commission will come to us. Everything is dependent upon how much business and what are the commercials around it. It's not like that our take rates are not going to go up. Our take rates would be dependent upon the kind of efforts that we are putting on the cost that we are incurring and the net EBITDA that the other participant group companies are getting out of it.

Krishnan A: Neha, just to be on the same page, these are only for new customers. It's not for the existing customers, point #1. Point #2, these are only for customers which are coming to us through the Apollo 24/7 platform. Digital leads which come directly through our marketing efforts into the Apollo website and us come directly to us and also the call centers come directly to us. It's only the Apollo 24/7 whereas as Mr. Sanjiv said, there are significant efforts which are happening into the customers of Apollo 24/7. And which is where if you remember, a couple of years back, we did say that even if you look at the pharmacy customers of Apollo and if we look at the number of customers that they have and look at the number of those customers who come into Apollo, it is less than 1%. That is one of the big opportunities which are there because he is already an Apollo customer in some sense and to really work on getting them into Apollo is what Apollo 24/7 is working on. We should see benefit of that with time.

Neha Manpuria: I get that from an Apollo consolidated perspective, but I was just trying to understand how will Apollo 24/7 monetize this incremental GMV that we are getting over time?

Krishnan A: Yes, as we said, he will get a percentage of the revenue for the incremental numbers that he has done.

Neha Manpuria: Suneeta ma'am or Krishnan, any update on the Apollo 24/7 stake sale, strategic sale that we have?

Suneeta Reddy: I think we have seen peak losses that 24/7 has incurred, but we have also seen an 84% growth over last year. And we believe that in this current environment where we as a Company are looking for growth, but we are also looking at profitability. We understand that this is a very difficult environment to get the valuation that we deserve, because 24/7 is differentiated in many ways. It's just not pharmacy online. It connects all of Apollo's physical offerings and creates the digital offerings. So, keeping in mind the value proposition of 24/7, we believe that there is investor interest which will take a little bit more time to convert. I wouldn't really like to put a time horizons here. But I would like to say that at Apollo, we believe that this is the future; it is necessary to invest in the business. Fortunately, we have capital to enable it to grow in the next 6 months. And by which time, we are quite sure that we will have an investor there.

Moderator: Due to time constraint, we will take one last question from the line of Shaleen Kumar from UBS Securities. Please go ahead.

Shaleen Kumar: Sir, just one thing. If I heard correctly, you said the discount in offline pharmacy has increased a bit?

Obul Reddy: That's right. Keeping the market in the view and what is happening and consistency between the two offerings, we have definitely introduced some schemes which increased the loyalty cost to the customers. And as I said, largely, we are able to get that compensated through the procurement improvement margin. And net-net we are about 30 to 40 basis points impacted; and with the growth coming in, we will be able to take that in the cost.

Shaleen Kumar: So, it's more of an initiative from our side? Is it to kind of parallel the scheme and not driven by the….

Obul Reddy: It is an initiative from our side to see that we don't want to lose our offline customers. So, we have introduced some schemes, something called Circle plan where they get some extra benefits, thereby there is a cost increase.

Shaleen Kumar: Sir, just last one observation. In Diagnostics when I was looking at, while the revenue has understandably grown only by 2%, but our profitability has come down significantly. Any specific reason over there?

C. Chandra Sekhar: You are comparing Q3 FY22, and that had a very significant component of COVID and COVID-allied testing's, which we have mentioned. The non-COVID revenues are to be seen and the margin profile there is definitely lower, and not the ones that we got in the COVID testing margins; that's the reason. You are comparing Q3 FY22 to Q3 FY23.

Moderator: I now hand the conference over to the management for closing comments.

Suneeta Reddy: Thank you, ladies and gentlemen for taking time out today. As you can see, at Apollo, we firmly believe that we have established 3 strong engines of growth. Of course, the core Hospital business continues to grow, and we believe that the fourth quarter will be a fairly good quarter for us. The pharmacy business, again, the offline pharmacy business continues to grow, and we are seeing about over 20% growth in revenues, and we will see an improvement in margins in the future. Our primary healthcare business which is Diagnostics and Clinics is an area that we are focusing on. And again, we are seeing strong growth in these three verticals, while keeping our core clinical proposition as our core differentiator. More importantly, I think the network effect of having these verticals and bringing them together through 24/7 is something that has not been attempted so far in this part of the world. And we believe that investing in the future and making us digital is very important for us to retain our position as the #1 healthcare provider in this part of the world.

Thank you, ladies and gentlemen, for supporting us on this journey, and we hope to hear more from you in the fourth quarter. Thank you once again.

Moderator: On behalf of Apollo Hospitals Limited, that concludes this conference. Thank you for joining us, and you may now disconnect your lines.
