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Media Release

RAM Ratings Lanka assigns A+/P1 to Lanka Hospitals Corporation PLC

RAM Ratings Lanka has assigned respective long- and short-term corporate credit ratings of A+ and P1 to Lanka Hospitals Corporation PLC ("LHC" or "the Hospital"). The long-term rating has a stable outlook. The ratings are upheld by the Hospital's strong financial profile, liquidity, ongoing state support and the positive outlook for the private healthcare industry. On the other hand, the ratings are tempered by LHC's moderate profitability; coupled with the fragmented nature of the private healthcare industry and the shortage of skilled personnel in the industry.

Incorporated in 2002, LHC was previously known as Apollo Hospitals Colombo, a subsidiary of Apollo Hospitals Group India. In 2003, Sri Lanka Insurance Corporation PLC ("SLIC") acquired 54.61% of the Hospital while 28.66% was acquired by Distilleries Company of Sri Lanka Limited ("DCSL"). Following the renationalisation of SLIC in 2009, majority stake of LHC is now indirectly owned by the state. Meanwhile, Fortis Global Healthcare Holdings Pte Limited ("Fortis"), an Indian-based private healthcare provider acquired 28.66% of LHC which was held by DCSL. We opine that state support will be forthcoming through its major shareholders as LHC is expected to play a key role in the Government of Sri Lanka's ("GOSL") agenda of making private healthcare more affordable. Furthermore, LHC's board mainly consists of representatives of GOSL.

The ratings are supported by LHC's strong financial profile; its gearing ratio clocked in at a relatively low 0.06 times as at the end of FYE 31 December 2010 ("FY Dec 2010") while the cash-protection metrics were also strong. At the same time, LHC's funds from operations ("FFO") debt coverage had improved to 3.10 times as at end-FY Dec 2010 (9M FY Dec 2009: 2.19 times), supported by the overall improvement in its performance. RAM Ratings Lanka notes that the Hospital's gearing levels and debt coverage are better than those of its corporate and industry peers, reflecting the management's conservative funding policy. Going forward, we expect these numbers to ease on LHC's increased debt burden to fund its planned expansion. Nonetheless, they are still envisaged to be better than its peers'.

The ratings are further supported by the Hospital's strong liquidity. LHC's cash and cash equivalents ("CCE") provide a strong buffer against its short-term borrowings; its ratio on CCE to short-term debts improved from 2.98 times as at end-FY Dec 2010 to 5.71 times as at end-September 2011, stronger than most of its corporate peers'. We note that LHC's current and quick ratios are also stronger than those of its industry counterparts.

Meanwhile, growth prospects for the local private healthcare industry remain encouraging, underscored by increased health awareness, higher disposable incomes, an expanding ageing population and better healthcare-insurance coverage among the working population. Moreover, better service quality and shorter waiting times compared to state hospitals also attract patients to private hospitals. In light of these factors, we envisage demand for private healthcare to continue to improve.

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Despite the above strengths, LHC's overall profitability is hampered by high overheads arising from its high-cost business model and personnel expenses. Amid faster revenue growth along with increased occupancy, however, LHC's margin on operating profit before depreciation, interest and tax ("OPBDIT") broadened from 5.71% in fiscal 2009 to 12.04% in FY Dec 2010. Nonetheless, this is still weaker than those of its industry peers.

On a separate note, the private healthcare industry is fragmented in nature. Nevertheless, the competition within Colombo is keen as most of the established players are concentrated in Colombo where the demand for private healthcare is high owing to higher disposable income. In this regard, our concerns hinge upon LHC's lack of branch network as there are other private hospitals with multiple branches and the capacity to cater to the rising demand for healthcare. At the same time, a significant challenge to the sector's growth is the shortage of skilled personnel and resultant rising costs.

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