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Acquisition Update
Metropolis Healthcare Ltd

Acquisition of Hitech Diagnostic to boost growth

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CMP: INR 2,183
Rating: BUY
Target Price INR: 2,426
Upside: 11%

Bloomberg:	METROHL:IN
52-week range (INR):	2,323 / 998
Share in issue (cr):	5.1
M cap (INR cr):	11,055
Promoter Holding (%)	50.39

Date: January 18, 2021

Metropolis Healthcare (METROHL) has acquired Dr. Ganesan's Hitech Diagnostic Centre (100% stake) for a consideration of INR618cr (combination of cash and stock deal). The acquisition should aid METROHL's aggressive expansion plans to achieve its targeted B2C revenue contribution of 65% in focus cities. Hitech Diagnostic Centre (Hitech) is well established in Tamil Nadu, Karnataka, Kerala, Andhra Pradesh and Pondicherry, and is the second largest player in Chennai, next only to METROHL. We maintain 'BUY' rating on METROHL.

Acquisition details

The acquisition is a combination of cash and stock deal. Cash portion of the deal is INR511cr, which will be funded through internal accruals as well as debt of up to INR300cr. METROHL is expected to issue around 1% stake (at CMP, it is valued at ~INR107cr). Completion of the acquisition will make Hitech a wholly-owned subsidiary of METROHL. The transaction is expected to get completed within the next three months.

Hitech consolidation is EPS accretive

Hitech Diagnostic Centre is a 35-year old company and is well established in Tamil Nadu, Karnataka, Kerala, Andhra Pradesh and Pondicherry. Hitech reported revenue of INR83.3cr in FY20 (up 21% YoY). Its EBITDA margin was same as METROHL. Also, Hitech enjoys strong brand equity like METROHL. According to management, Hitech should report revenue growth of ~50% and higher EBITDA margins over 9MFY21, partly aided by the current pandemic situation. The company has 31 laboratories, including 3 NABL and ICMR accredited laboratories, 68 collection centres and a menu of 1,100+ tests. Routine tests/ B2C business contributes 60%/65% to Hitech's revenue.

Outlook and valuation: Robust growth; maintain 'BUY'

We believe the Hitech acquisition will accelerate METROHL's B2C revenue growth without compromising on margins. While the deal will increase METROHL's borrowings and dilute equity, it will still be EPS accretive. We believe the company is a compounding story and have revised our earnings estimate upwards for FY22/FY23E by 3.5%/3.4%. The stock is currently trading at 52x/46x FY22E/FY23E earnings. Maintain 'BUY' with revised target price of INR2,426.

Year to March (INR Cr)	FY19	FY20	FY21E	FY22E	FY23E
Revenue	761	856	937	1289	1463
YoY growth (%)	17.6	12.5	9.4	37.6	13.5
EBITDA	200	233	242	350	400
EBITDA margin (%)	26.3	27.2	25.8	27.1	27.3
Profit after tax	125	128	150	215	246
YoY growth (%)	11.8	22.0	-1.7	43.2	14.5
EPS	25	25	29	42	48
ROAE (%)	29.7	32.3	25.9	32.0	32.4
RoACE (%)	42	38	31	34	31
P/E	89.0	86.7	74.0	52.1	45.5
EV/EBITDA	54.4	46.9	45.0	32.6	28.4

METROHL - M&A to be a core part of growth strategy

In our earlier reports, we have highlighted METROH's intention to acquire a meaningful player to accelerate growth and gain market share. This acquisition is on similar lines as Hitech is among the top-15 diagnostics chain in India. Also, this acquisition should help METROHL's aggressive expansion plan to achieve its targeted B2C revenue contribution of 65% in focus cities. B2C contribution in H1FY21 was 58%.

The acquisition will also strengthen METROHL's presence in South India, particularly in Chennai (the combined entity will have 30% market share in Chennai). METROHL will get access to 68 collection centres and 31 laboratories (25% addition for METROHL), adding to its existing 125 labs and 2447 service centres. It will allow METROHL to gain cost synergy and access to more customer segments in several key markets in South India e.g. Bengaluru and other key markets in Tamil Nadu, apart from Chennai.

We believe METROHL will follow its track record of turning its acquisitions into strong and sustainable businesses. The company has earlier reported sales CAGR of 20%+ in its acquired entities and improvement in margins.

Exhibit 1: Successful track record of its inorganic strategy: 22 acquisitions in 15 years

Few of the acquired companies	Year of acquisition	Location	Revenue at the time of acquisition	Revenue for FY20	CAGR (%)
Sudharma Metropolis Health Services Pvt	2003	Kerala	INR 1.8 crore	INR 49.6 crore	**22%**
Golwilkar Metropolis Health Services (India) Pvt	2006	Pune	INR 3.9 crore	INR 41.3 crore	**18%**
Desai Metropolis Health Services Pvt	2008	Surat	INR 3.4 crore	INR 39.2 crore	**23%**
RV Metropolis Diagnostic & Healthcare Centre Pvt	2008	Bengaluru	INR 3.6 crore	INR 43.5 crore	**23%**
Dr Patel Metropolis Healthcare Pvt	2012	Nashik	INR 1.8 crore	INR 14.6 crore	**30%**
Sanjeevani Pathology Labs	2017	Rajkot	INR 12 crore	INR 18.1 crore	**15%**

Source: Edelweiss Wealth Research

Exhibit 2: Change in Estimates

	FY22E			FY23E		
INR cr	Old	Revised	Change (%)	Estimate	Reported	Change (%)
Net sales	1,151	1,289	12.0%	1,305	1,463	12.1%
Gross Profit	859	955		974	1,087	
Gross margin (%)	74.6	74.1		74.6	74.3	
EBITDA	318	350	9.9%	361	400	10.9%
EBITDA margin (%)	*27.6*	*27.1*		*27.6*	*27.3*	
PBT	275	287	4.5%	315	329	4.4%
PBT margin	*23.9*	*22.3*		*24.1*	*22.5*	
Net profit	205	215	4.5%	236	246	4.4%
EPS (Rs)	40.4	41.9	3.5%	46.4	48.0	3.4%

Source: Edelweiss Wealth Research

Income statement (INR Cr)

Year to March	FY19	FY20	FY21E	FY22E	FY23E
Income from operations	761	856	937	1,289	1,463
Direct costs	185	217	243	334	376
Employee costs	176	190	215	284	322
Other expenses	376	407	452	605	687
Total operating expenses	561	624	695	939	1,063
EBITDA	200	233	242	350	400
Depreciation and amortisation	20	39	46	54	62
EBIT	180	194	196	296	338
Interest expenses	1	8	8	22	24
Other income	8	9	12	13	15
Profit before tax	188	194	200	287	329
Provision for tax	63	41	50	72	83
Core profit	125	153	150	215	246
Extraordinary items	-	-25	-	-	-
Profit after tax	125	128	150	215	246
Minority Interest	-1	-1	-1	-1	-1
Share from associates	0	0	0	0	0
Adjusted net profit	124	128	149	214	245
Equity shares outstanding (cr)	5.0	5.1	5.1	5.1	5.1
EPS (INR) basic	24.6	25.2	29.5	41.9	48.0
Diluted shares (Cr)	5.02	5.06	5.06	5.11	5.11
EPS (INR) fully diluted	24.6	25.2	29.5	41.9	48.0
Dividend per share	13	8	7	22	24
Dividend payout (%)	52.8	26.6	23.7	52.5	50.0

Common size metrics- as % of net revenues

Year to March	FY19	FY20	FY21E	FY22E	FY23E
Operating expenses	73.7	72.8	74.2	72.9	72.7
Depreciation	2.6	4.6	4.9	4.2	4.2
Interest expenditure	0.1	1.0	0.8	1.7	1.6
EBITDA margins	26.3	27.2	25.8	27.1	27.3
Net profit margins	16.2	14.9	15.9	16.6	16.8

Growth metrics (%)

Year to March	FY19	FY20	FY21E	FY22E	FY23E
Revenues	17.6	12.5	9.4	37.6	13.5
EBITDA	12.3	16.2	3.9	44.5	14.4
PBT	14.9	3.1	3.4	43.2	14.5
Net profit	11.8	22.0	(1.7)	43.2	14.5
EPS	13.6	2.3	17.0	42.0	14.6

Balance sheet					(INR Cr)
As on 31st March	**FY19**	**FY20**	**FY21E**	**FY22E**	**FY23E**
Equity share capital	10	10	10	10	10
Preference Share Capital	-	-	-	-	-
Reserves & surplus	409	513	620	698	795
Shareholders funds	419	523	630	708	805
Secured loans	17	67	67	367	317
Unsecured loans	0	-	-	-	-
Borrowings	18	67	67	367	317
Minority interest	1	2	2	2	2
Sources of funds	**438**	**592**	**698**	**1,076**	**1,123**
Gross block	271	394	429	539	569
Depreciation	58	98	144	198	259
Net block	213	296	286	342	310
Capital work in progress	6	3	-	-	-
Total fixed assets	219	299	286	342	310
Goodwill	-	-	-	361	361
Investments	33	14	76	130	170
Inventories	26	24	27	37	42
Sundry debtors	137	128	140	193	219
Cash and equivalents	80	210	244	117	138
Loans and advances	31	17	18	25	28
Other current assets	-	-	-	-	-
Total current assets	274	380	430	372	427
Sundry creditors and others	93	85	93	128	145
Provisions	14	12	12	12	12
Total CL & provisions	107	97	105	140	157
Net current assets	167	283	325	232	270
Net Deferred tax	1	12	12	12	12
Misc expenditure	18	-17	-	-	-
Uses of funds	**438**	**592**	**698**	**1,076**	**1,123**
Book value per share (INR)	83	103	124	138	157

Cash flow statement

Year to March	**FY19**	**FY20**	**FY21E**	**FY22E**	**FY23E**
Net profit	125	177	150	215	246
Add: Depreciation	20	39	46	54	62
Add: Misc expenses written off	-9	35	-17	0	0
Add: Deferred tax	0	-11	0	0	0
Add: Others	-1	-1	-1	-1	-1
Gross cash flow	135	239	178	268	307
Less: Changes in W. C.	37	-14	8	35	17
Operating cash flow	98	254	170	233	290
Less: Capex	31	120	32	471	30
Free cash flow	**67**	**134**	**138**	**-238**	**260**

Ratios

Year to March	FY19	FY20	FY21E	FY22E	FY23E
ROAE (%)	29.7	32.3	25.9	32.0	32.4
ROACE (%)	41.6	38.1	31.0	33.8	31.1
Debtors (days)	66	55	55	55	55
Current ratio	2.6	3.9	4.1	2.7	2.7
Debt/Equity	0.0	0.1	0.1	0.5	0.4
Inventory (days)	13	10	10	10	10
Payable (days)	44	36	36	36	36
Cash conversion cycle (days)	34	29	29	29	29
Debt/EBITDA	0.1	0.3	0.3	1.0	0.8
Adjusted debt/Equity	-0.1	-0.3	-0.3	0.4	0.2

Valuation parameters

Year to March	FY19	FY20	FY21E	FY22E	FY23E
Diluted EPS (INR)	24.6	25.2	29.5	41.9	48.0
Y-o-Y growth (%)	*13.6*	*2.3*	*17.0*	*42.0*	*14.6*
CEPS (INR)	28.6	37.8	38.5	52.4	60.1
Diluted P/E (x)	*89*	*86.7*	***74.0***	***52.1***	***45.5***
Price/BV(x)	26.2	21.1	17.5	15.8	13.9
EV/Sales (x)	*14.3*	*12.7*	*11.6*	*8.9*	*7.7*
EV/EBITDA (x)	54.4	46.9	45.0	32.6	28.4
Diluted shares O/S	*5.0*	*5.1*	*5.1*	*5.1*	*5.1*
Basic EPS	24.6	25.2	29.5	41.9	48.0
Basic PE (x)	*88.7*	*86.7*	*74.0*	*52.1*	*45.5*
Dividend yield (%)	0.6	0.4	0.3	1.0	1.1

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Rating	Expected to
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HOLD	appreciate between 5% and 15% over a 12-month period
REDUCE	return below 5% over a 12-month period

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