COVID 19 - Impact assessment for private healthcare sector and key recommendations on financial measures required for the sector

April 13, 2020

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Contents

Context

- With the stipulation of stringent lockdown measures to contain the outbreak of COVID 19 in India, private healthcare sector is witnessing a dual challenge of significant drop in patient footfalls, elective surgeries and international patients as well as facing the need to continue operations and invest in additional materials, equipment and manpower to ensure preparedness for eventual treatment of COVID patients if required

- Given that the private healthcare sector is expected to face a severe financial crisis due to the ongoing COVID 19 outbreak, FICCI collaborated with EY for the following-

  - Estimate and project the operating losses and return on capital employed for the sector over a 1-3 month timeframe

  - Determine the likely cash position and time period over which businesses can sustain with such cash levels

  - Co-develop recommendations on financial measures required in context of the operating losses and weak cash position likely to be faced by the private healthcare sector

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Executive summary (1/7)

1 Despite >60% share of bed capacity, the private healthcare sector's financial performance was severely constrained even in the pre-COVID state

- **Private healthcare sector** is the bedrock of capacity and capability in India particularly in higher secondary and tertiary care, **constituting >60% of beds at ~8.5-9 lac, > 60% of inpatients, 80% of doctors** and is also among the country's **Top 5 employers**

- **Revenue** for the private healthcare sector is **estimated at ~Rs 2.4L crore, EBITDA is estimated at ~Rs 31K crore (13%)** and **PAT is estimated at ~ Rs 7K crore (3%)**. The sector's **median return on capital employed is ~7%** which is lower than **cost of capital of 14%** and the **median interest coverage ratio is ~2** vis-à-vis **best in class reference of 5-6**

- The sector is also constrained severely in terms of liquidity with **cash balances available to cover up to 19 days of operating costs** and **government receivables to the tune of 7-8% of revenue**

2 Stipulation of lockdown measures has further constrained the financial performance by March-end causing providers to make operational losses

- With **strict lockdown measures** being imposed to contain the outbreak of COVID 19, hospitals are witnessing a **drop in both domestic and international patient footfalls and elective surgeries**, resulting in **occupancy levels** to fall to a **mere 40% by late-March** vis-à-vis **pre-COVID occupancy levels of ~65-70% and is expected to reduce further.** Impact on **diagnostic labs → 80% fall in patient visits and revenue**

- Limited options for containing fixed costs due to need for continuing operations coupled with focus on preparedness for eventual treatment of COVID patients, has resulted in **EBITDA margins witnessing a sharp fall to a level lower than -40%** by **end-March/early-April** with the sharp decline in revenues

Executive summary (2/7)

3 **If the situation persists, providers will face severe liquidity crisis with cash balance likely to cover operating losses only for 1-2 months**

- **Operating losses** are estimated to the tune of **Rs 4,500 crore for a month** and **Rs 13,400 crore for a quarter if revenues are at 50% (occupancy of 35%).**
- **Losses** are estimated to the tune of **Rs 7,300 crore for a month** and **Rs 21,900 crore for a quarter** if **revenues are at 30% (occupancy of 20%).**
- For the sector which is already constrained in terms of liquidity, the **onset of operating losses will cause** cash balances to be completely depleted if the situation persists for a quarter.
- While bed utilization is low, private hospitals are expected to be **"super ready"** to manage any eventuality emerging from this epidemic situation. Hence **opportunity to rationalize fixed costs is very limited** unlike other industry sectors. Increase in costs owing to infection control and PPE have not been factored in the above estimates.

Assessment for a quarter

	Pre-COVID	Post-COVID Occupancy 35%	Post-COVID Occupancy 20%
Revenue Rs Crore	59K	29K	18K
EBITDA %	13%	(42%)	(119%)
EBITDA loss and top up required Rs Crore		(13K)	(22K)
Cash position in days	19	(32)	(42)

Executive summary (3/7)

3 **If the situation persists, providers will face severe liquidity crisis with cash balance likely to cover operating losses only for 1-2 months (contd.)**

- The sector is also expected to be lower by **20-35% in terms of revenue (compared to FY 20)** and have **early single digit or negative EBITDA in FY 21**
- **FY 21 ROCE for the sector is estimated at -5 to -15%**

Hospital segment-wise projection of financial performance is as follows-

Bed category	No. of hospitals	No. of beds	ARPOB (Rs)	EBITDA loss per occupied bed day (Rs)	Monthly EBITDA loss (Rs Cr.)	Quarterly EBITDA loss (Rs Cr.)
Tertiary	1,500	2.8 L	21 – 22K	5 – 8K	2,900 – 4,700	8,600 – 14,000
Secondary	42 – 43K	5.8 L	5 – 6K	1.5 – 2.5K	1,600 – 2,600	4,800 – 8,000
Total	**44 – 45K**	**8.6 L**	**10 – 11K**	**2.5 – 4K**	**4,500 – 7,300**	**13,400 – 22,000**

- Short term operating losses for the **diagnostic sector** will be to the tune of **Rs 200-800 crore for a month and Rs 600- 2,200 crore for a quarter** (assuming 50-80% decline in revenue)

Executive summary (4/7)

Private sector providers are acutely aware of the critical role they have to play in effectively combating the menace of rapidly spreading COVID threat across the country. Further, the sector acknowledges that this solemn responsibility is considered as national duty. While the private healthcare sector stands fully committed to partner with the government with all its resources, to best serve the nation in this hour of crisis, it finds itself in a compelling situation to beseech the government for certain financial forbearance measures to best utilise its capacities and capabilities to serve the nation during this period of medical emergency.

4 Liquidity infusion, indirect and direct tax benefits and fixed cost subsidies are among the key recommendations for financial relief to the sector

Key themes	Key recommendations
Liquidity infusion	1. **Short term interest free/ concessional interest loans** to the tune of Rs 14,000-24,000 Cr. to address liquidity gaps for 3 months ▸ Relaxation for a period of at least 2 years of various debt covenants inserted in the loan documents including but not limited to the following- ▸ Debt to EBITDA threshold ▸ Debt to Equity threshold ▸ Obligation with respect to interest coverage ratio
✓✓	2. **Immediate 100% release** of dues locked with Central and State government authorities. Estimated dues of Rs 1,700 Cr. outstanding from CGHS and ECHS based on industry sources. While government has issued notification on payment of dues under CGHS and ECHS schemes to private hospitals, immediate release of such dues should be made

✓✓ Recommendations for which government action has already been taken

Executive summary (5/7)

4 Liquidity infusion, indirect and direct tax benefits and fixed cost subsidies are among the key recommendations for financial relief to the sector (contd.)

Key themes	Key recommendations
Indirect tax reliefs/ exemptions/ waivers	3. **Relief to hospital sector - recoup amount equivalent to ineligible GST credits paid on procurements** for a specified period which is estimated to the tune of Rs 2,000 Cr. for 3 months
	✓✓ 4. **Provide Customs duty / GST exemption** on essential medicines, consumables and devices for treatment of COVID patients
	5. **Waiver of Health Cess** for identified medical devices introduced in Budget 2020 – If complete waiver not feasible, need for reduced levy of Health Cess @ 2% instead of @5% for a period of one year
	6. **Extension of time for a period of three years needs to be provided under the EPCG scheme** for fulfilment of existing export obligations for the healthcare sector given that international patient traffic flow has completely stopped and it would take a considerable period of time for the same to return to the pre COVID-19 incidence levels

✓✓ Recommendations for which government action has already been taken

Executive summary (6/7)

4 Liquidity infusion, indirect and direct tax benefits and fixed cost subsidies are among the key recommendations for financial relief to the sector (contd.)

Key themes	Key recommendations
Income tax benefits	7. **NIL TDS for FY21 and TDS at 5% for FY22:** In order to provide relief on cash flow, and by way of acknowledgement of the fact that profits of healthcare companies are going to be under stress for the next two years, Tax Deducted at Source may be declared as NIL (on payments from government authorities and insurance companies) for healthcare organisations for FY21 and may be set at 5% for FY22 8. **Recoup income tax refunds by adjusting taxes payable and tax dues**: Government to enable a mechanism for adjusting the TDS and advance tax dues against pending refunds of corporates, wherever applicable
Statutory liability payments	9. **Deferment of statutory liabilities** such as TDS, PF, ESI, GST for a period of 3-6 months without interest, late fee and penalty

Executive summary (7/7)

4 Liquidity infusion, indirect and direct tax benefits and fixed cost subsidies are among the key recommendations for financial relief to the sector (contd.)

Key themes	Key recommendations
Fixed cost rebate	**10. Rebate on commercial rate of power for a stipulated period.** Estimated power cost for the sector is Rs 7,000 Cr.
Waiver of fees on license renewal	**11. Waiver of renewal fees for licenses** along with option for renewal on self certification basis to speeden up the process of bed capacity addition

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Assessed COVID impact on the hospital sector basis the study of immediate impact in the last week of March 2020, post the nation-wide lockdown

1. **Baseline P&L and key performance metrics from representative sample**
2. **March (FY20) P&L study and immediate COVID impact assessment**
3. **COVID impact basis estimates for likely scenarios for Q1 FY21**
4. **Potential full year impact for the private healthcare and diagnostic sector**

Step 2:

- ***Studied March week-wise revenue and occupancy levels for 10 hospitals and 5 diagnostic chains***
- ***Discussions with 10 healthcare and diagnostic labs to understand post-COVID impact***

Step 1:

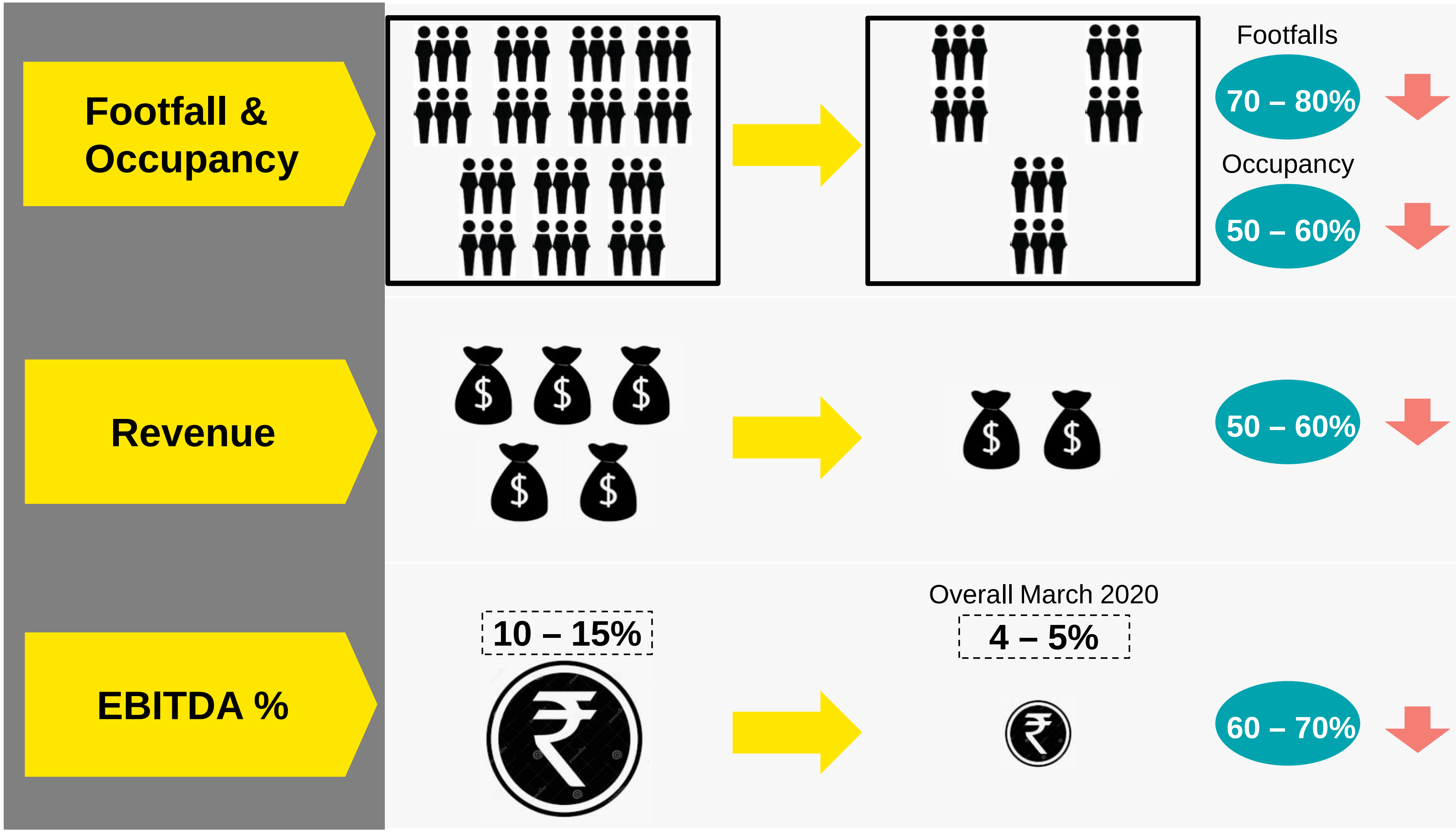
- ***Studied median performance across 74 hospital groups and 17 diagnostic chains****

Category	No. of entities
Tertiary care	51
Secondary care	23
Diagnostic chains	17
Total	**91**

*74 hospital groups contribute to 20% of Sector revenue and 17 diagnostic chains contribute of 15% of Diagnostic sector revenue

Hospitals: 5 chains with presence across geographies have highlighted significant drop in footfalls, revenue and EBITDA in the last week of March 2020 vis-à-vis pre-COVID levels

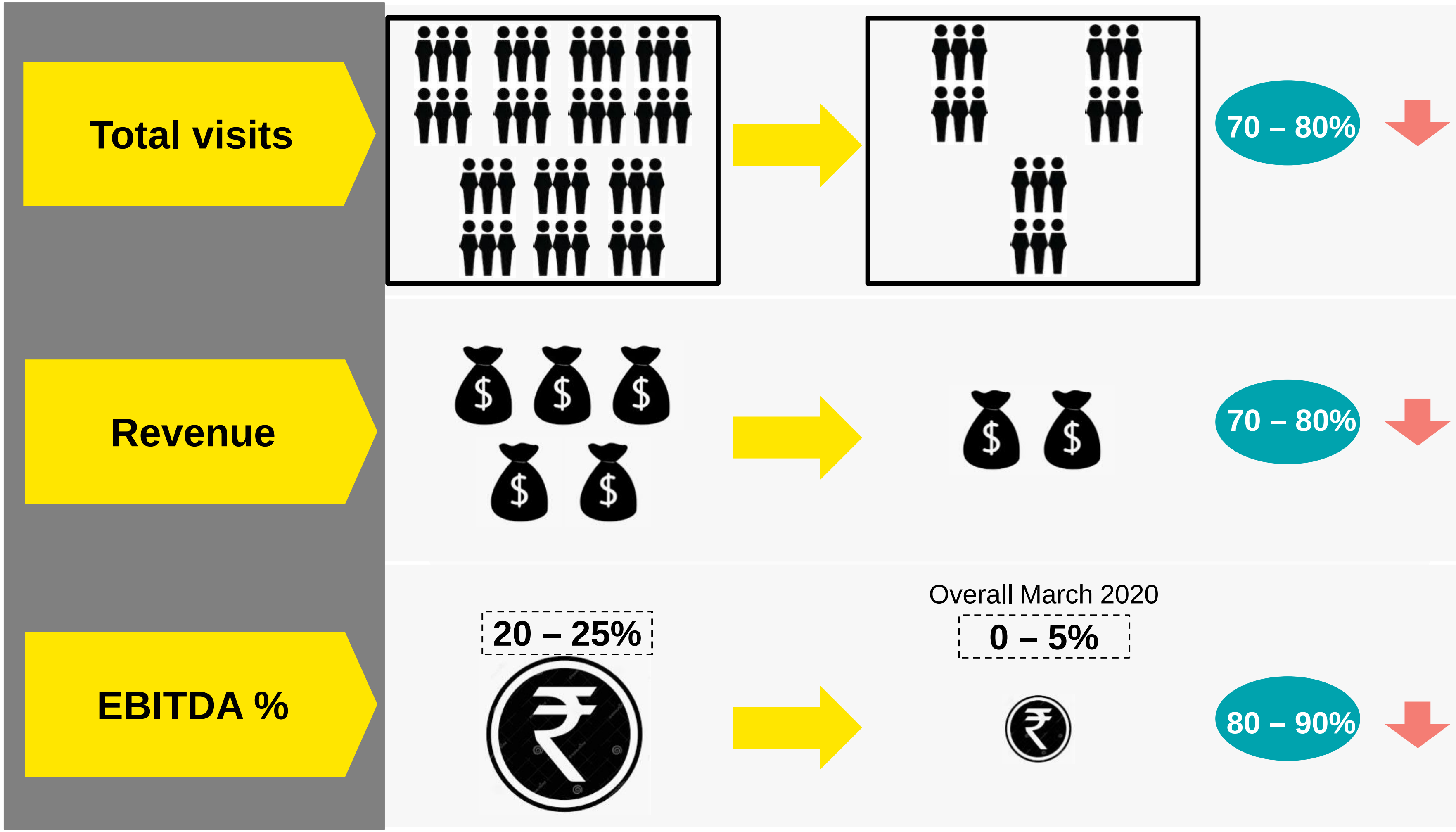
Hospitals | Diagnostic



Source: FICCI

Diagnostic: 5 chains with presence across geographies have highlighted significant drop in footfalls, revenue and EBITDA in the last week of March 2020 vis-à-vis pre-COVID levels

Hospitals | **Diagnostic**



Source: FICCI

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The total revenue of private hospital sector in India is around Rs. 2.4L Cr. with an EBITDA of approximately 13%

Rs. 2.4 L Cr.
Revenue

31K Cr.
EBITDA

~9L | *Tertiary: ~3*
Secondary: ~6
Bed Strength

	% of Total cost		*% of Revenue*
Category	**Fixed Cost**	**Variable Cost**	**EBITDA**
Tertiary (n=51)	65 - 70%	30 - 35%	13%
Secondary (n=23)	75 - 80%	20 - 25%	14%
Overall (n=74)	65 - 75%	25 - 35%	13%

Note: 'n' refers to the sample size of data under consideration (source: VCCEdge database)

Source: VCCEdge, EY Analysis

Liquidity and return on capital employed for the sector has been constrained even in the pre-COVID context

● = 75th percentile figure
All other values based on Median

	75th percentile	Overall	Tertiary	Secondary
Interest Coverage Ratio	5	2	2	6
Receivables Days	18	45	48	39
Cash position in days	46	19	20	17
Annualized ROCE %	15%	7.3%	7.4%	7.2%

Source: VCCEdge, EY Analysis

Note: Cash position in days represent number of days of cash to cover operating cash expenses

Hospitals observed a drop in revenue to ~40% of their pre-COVID figures post the nation-wide lockdown and this drop to 30-50% is likely to continue in following month/s

March →

Lockdown starts: 25th March

Area		Feb-20		Mar-20	1st – 7th	8th – 14th	15th – 21st	22nd – 28th	29th – 31st	Apr-20 1 (a)	Apr-20 1 (b)
Revenue		**100**		**88**	**23**	**23**	**23**	**14**	**4**	**50**	**30**
Expenditure		**87**		**84**	**20**	**20**	**20**	**17**	**7**	**72**	**66**
- Material	***VC***	25	***25%***	22	6	6	6	3	1	12	7
- Doctor cost	***VC***	6	***6%***	5	1	1	1	1	0	3	2
- Manpower	***FC***	18	***18%***	18	4	4	4	4	2	18	18
- Doctor Cost	***FC***	18	***18%***	18	4	4	4	4	2	18	18
- Indirect	***FC***	21	***21%***	21	5	5	5	5	2	21	21
EBITDA		**13**		**4**	**3**	**3**	**3**	**-3**	**-3**	**-22**	**-36**
Key metrics											
Revenue/ day		3.3		2.8	3.3	3.3	3.3	2.0	1.3	1.7	1.0
Variable cost %		31%		31%	31%	31%	31%	31%	31%	31%	31%
Fixed cost %		57%		65%	55%	55%	55%	92%	137%	114%	189%
EBITDA %		**13%**		**5%**	**14%**	**14%**	**14%**	**-22%**	**-68%**	**-44%**	**-120%**
Revenue drop								**60%**	**40%**	**50%**	**30%**

Revenue drop to x% of pre-COVID daily revenue

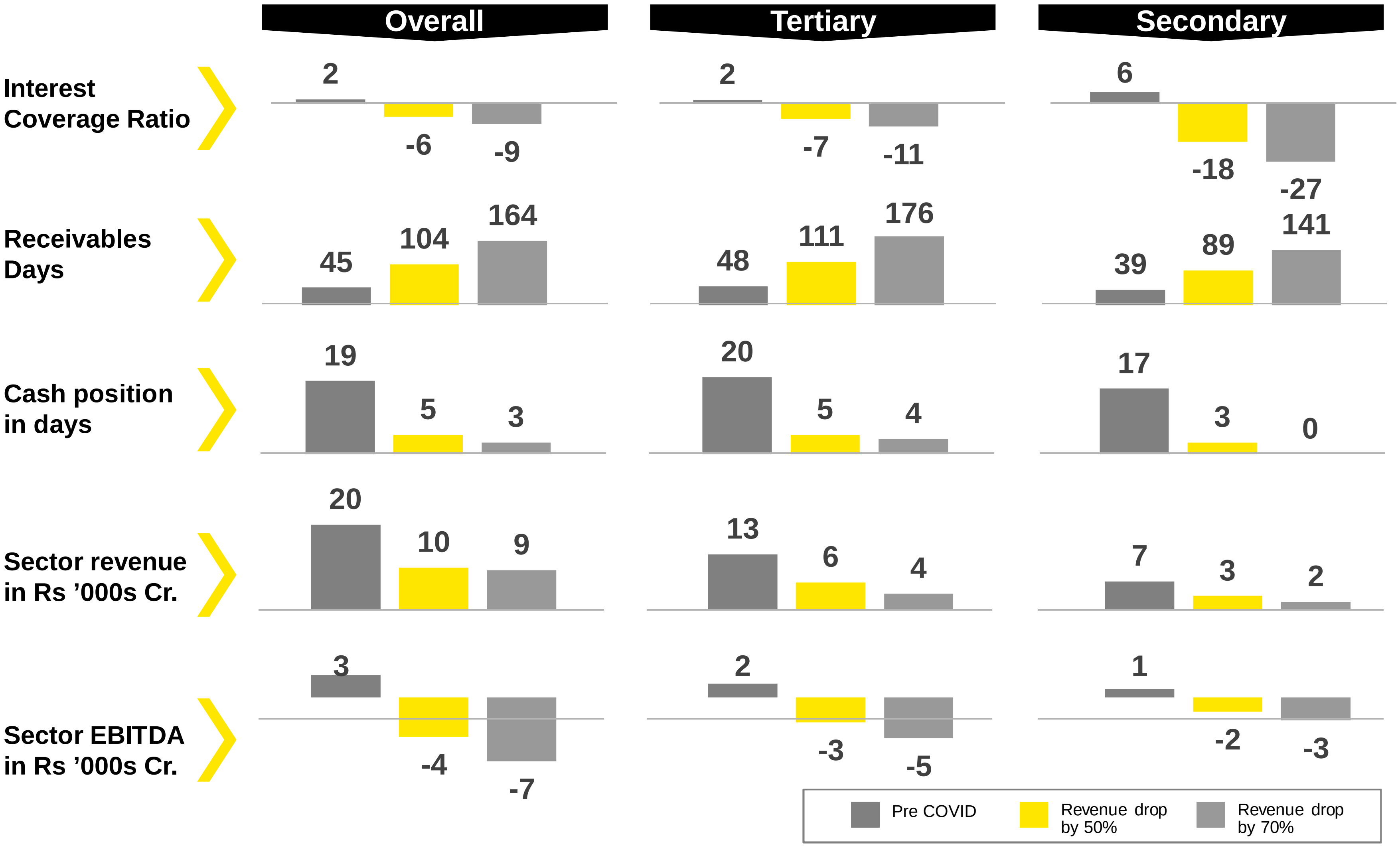
The lockdown is likely to result in significant operating losses to the tune of Rs 13,400 – 22,000 Cr. for the quarter and liquidity crunch as evidenced by the impact assessment

	Scenario 1 (Lock Down =1 Month)			Scenario 2 (Lock Down = 1 Quarter)		
	At Pre-COVID Revenues	50% Fall in Revenue	70% Fall in Revenue	At Pre-COVID Revenues	50% Fall in Revenue	70% Fall in Revenue
EBITDA (Rs '000s Cr.)	2.6	-4.5	-7.3	7.7	-13.4	-21.9
Interest coverage ratio	2	-6	-9	2	-6	-9
Receivable days	45	104	164	45	135	194
Cash position in days	19	5	3	19	-32	-42

Note: Based on discussions with industry sources which highlighted that collections have been very limited since end-March due to lockdown situation, no collection of receivables as on year end FY 20 has been considered for the above 1 month and 1 quarter projections

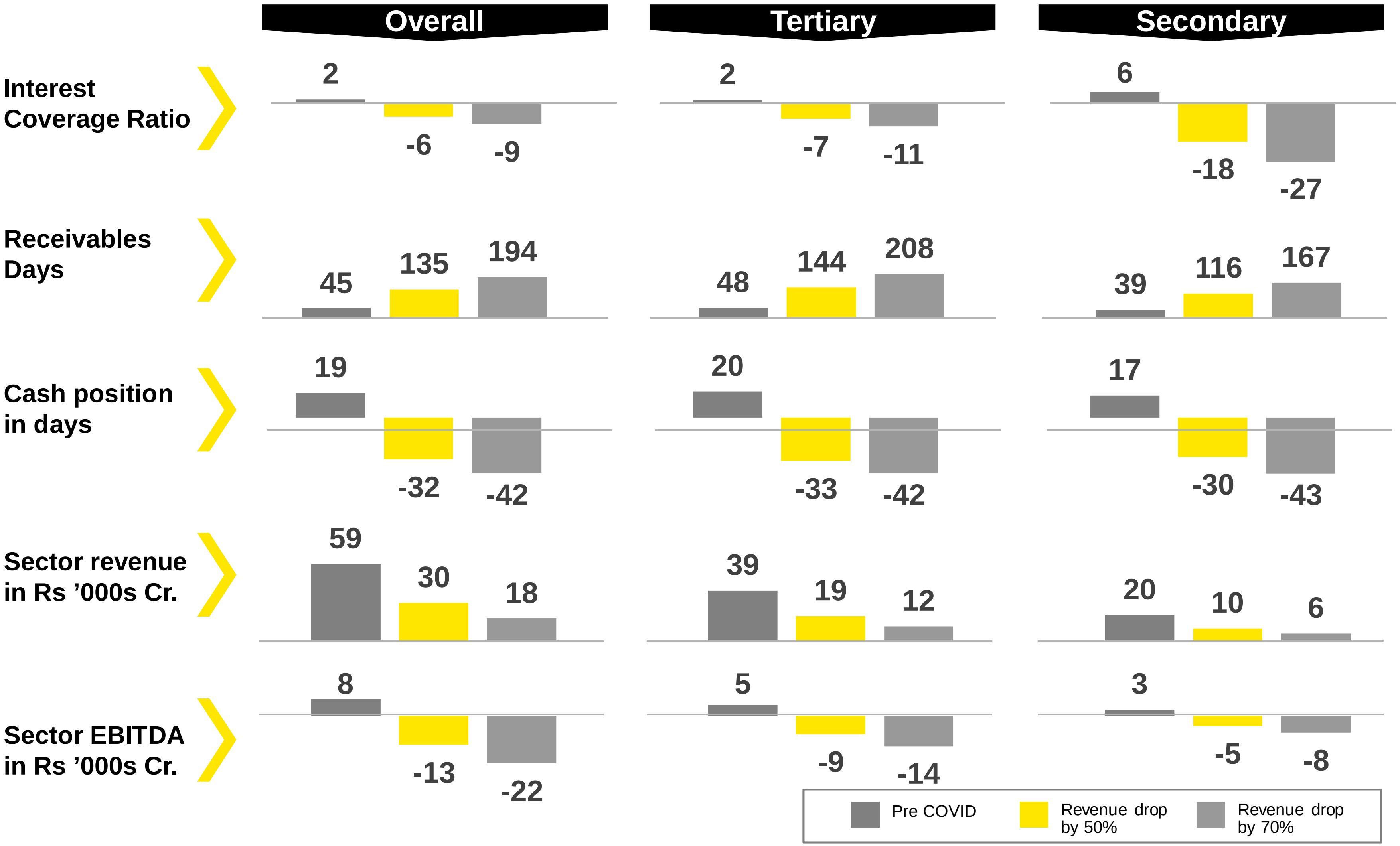
Detailed impact assessment for tertiary & secondary care players

Scenario 1: Revenue drops by 50% - 70% of the pre-COVID monthly revenue for one month



Detailed impact assessment for tertiary & secondary care players

Scenario 2: Revenue drops by 50% - 70% of the pre-COVID monthly revenue for one quarter



It is estimated that FY21 performance for the sector will be muted with revenue lower by 20-35% and negative EBITDA

		Scenario 1	Scenario 2
Metric	**FY20**	**FY21E**	**FY21E**
Revenue	**100**	**75 – 80**	**60 – 65**
Occupancy %	**70%**	**55 – 60%**	**45 – 50%**
EBITDA %	**13%**	**(5) – 5%**	**(15) – (10)%**
ROCE %	**7%**	**(10) – (5)%**	**(15) – (10)%**

Scenario 1: Occupancy to gradually ramp-up from 40 – 45% in Q1 to 65 – 70% in Q4 FY21

Scenario 2: Occupancy to gradually ramp-up from 30 – 35% in Q1 to 60 – 65% in Q4 FY21

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The lockdown is likely to result in operating losses to the tune of Rs 600- 2,200 Cr. for the quarter as evidenced by the impact assessment

Pre-COVID

Rs. 35.4K Cr.

Revenue

EBITDA	25%
Fixed Cost	35 - 40%
Variable Cost*	35 - 40%
ROCE	18%

Post-COVID impact on the diagnostic sector

		Pre and Post COVID Scenarios (Fall in Revenue)		
		Pre-COVID	50%	80%
EBITDA (Rs '000s Cr.)	1 Month	0.7	-0.2	-0.8
	1 Quarter	2.2	-0.6	-2.2
Interest Coverage Ratio	Overall	18	-10	-27

Pre-COVID Interest coverage ratio for key radiology players is 5

*Variable cost includes materials consumed, fees to collection centres and channel partners, logistics cost and few indirect expenses

Source: VCCEdge, EY Analysis

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Improving liquidity position, indirect and direct tax benefits and fixed cost subsidies are key recommended measures to provide financial relief to the sector (1/4)

1

Key themes	Proposed actions
Improve liquidity position of private healthcare providers ► Estimates highlight that onset of operating losses will result in **cash balances to be completely depleted if the situation persists for a quarter**	► **Financing of the operating losses through short term interest free/ concessional interest rate** loans to address the liquidity gap to the tune of Rs 14,000 - 24,000 Cr. (Rs 13,400 – 21,900 Cr. for hospitals and Rs 600- 2,200 Cr. for diagnostic chains) for 3 months ► Relaxation for a period of at least 2 years of various debt covenants inserted in the loan documents including but not limited to the following- ► Debt to EBITDA threshold ► Debt to Equity threshold ► Obligation with respect to interest coverage ratio ✓✓ ► **Portion of the above liquidity gap** can be addressed through the immediate release of 100% dues to the hospitals locked with central and state government authorities. ► It is estimated that for top 7 hospital dues from both central and state government authorities is in the range of 7% of revenue. Based on industry sources, the outstanding dues from CGHS and ECHS is ~ Rs 1,700 Cr. While government has issued notification on payment of dues under CGHS and ECHS schemes to private hospitals, immediate release of such dues should be made

✓✓ Recommendations for which government action has already been taken

Improving liquidity position, indirect and direct tax benefits and fixed cost subsidies are key recommended measures to provide financial relief to the sector (2/4)

2

Key themes	Proposed actions
Indirect tax relief and exemption, waiver of health cess ► It is estimated that the ineligible GST credits is in the range of ~**Rs 2,000 crore for 3 months** for the private healthcare sector (**Impact of 6-7% on post-COVID revenues for the sector assuming 10% average GST on materials and 18% GST on services)**	► **Recoup amount equivalent to ineligible GST credits paid on procurements** for hospitals for a specified period: ► Government to provide a methodology / approach to identify the fiscal benefit, as above, in a manner which is easy to operate / monitor – may be have a common platform to upload details of the GST paid on procurements during the specific period ► Enable provisional refund (~50-75% of the amount involved) to facilitate swift release of funds to hospitals pending verification of documentation / details uploaded, as above ► Care to be taken to delink the above benefit from "anti-profiteering clause under the GST Act" to avoid additional interpretational / operational challenges for the Sector ✓✓ ► **Provide customs duty / GST exemption** on essential medicines, consumables and devices which are required to treat COVID patients ► **Waiver of Health Cess for identified medical devices introduced in Budget 2020** – If complete waiver not feasible, need for reduced levy of Health Cess @ 2% instead of @5% for a period of one year

✓✓ Recommendations for which government action has already been taken

Improving liquidity position, indirect and direct tax benefits and fixed cost subsidies are key recommended measures to provide financial relief to the sector (3/4)

	Key themes	Proposed actions
2	**Indirect tax relief and exemption, waiver of health cess (contd.)**	► **Extension of time for a period of three years needs to be provided under the EPCG scheme** for fulfilment of existing export obligations for the healthcare sector given that international patient traffic flow has completely stopped and it would take a considerable period of time for the same to return to the pre COVID-19 incidence levels
3	**Income tax benefits**	► **NIL TDS for FY21 and TDS at 5% for FY22:** In order to provide relief on cash flow, and by way of acknowledgement of the fact that profits of healthcare companies are going to be under stress for the next two years, Tax Deducted at Source may be declared as NIL (on payments from government authorities and insurance companies) for healthcare organisations for FY21 and may be set at 5% for FY22 ► **Recoup income tax refunds by adjusting taxes payable and tax dues**: Government to enable a mechanism for adjusting the TDS and advance tax dues against pending refunds of corporates, wherever applicable
4	**Statutory liability payments**	► **Deferment of statutory liabilities** such as TDS, PF, ESI, GST for a period of 3-6 months without interest, late fee and penalty

Improving liquidity position, indirect and direct tax benefits and fixed cost subsidies are key recommended measures to provide financial relief to the sector (4/4)

	Key themes	Proposed actions
5	**Fixed cost rebate**	► **Rebate on commercial rate of power for a stipulated period:** The estimated power cost for the sector is Rs. 7000 Cr.
6	**Waiver of fees on license renewal**	► **Waiver of renewal fees for licenses** alongwith with option for renewal on self certification basis to speeden up the process of bed capacity addition

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Government has exempted BCD and Health Cess on import of equipment and consumables associated with COVID treatment and approved expeditious clearance of outstanding dues

	Key financial measures	Actions already taken by the Government
1	**Basic customs duty and Health Cess exemption**	► In light of immediate requirement of ventilators and other items, the **Central government has granted exemption on basic customs duty and Health Cess**, on the import of following goods with immediate effect ► Ventilators ► Face Mask, Surgical Mask ► Personal Protection Equipment (PPE) ► Covid-19 Test Kits ► Inputs for manufacture of above items ► Basic custom duty exemption shall be **available up to 30th Sept.**
2	**Clearance of outstanding dues of CGHS, ECHS**	► Ministry of Finance (PFC-II) has approved **clearance of outstanding dues with Government** to be taken up immediately, especially outstanding of **CGHS and ECHS**

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