Financial Analysis-Comparison & Perspective For The Companies In Healthcare Service Industry

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SUB THEME: FINANCIAL ANALYSIS

Abstract - Financial Analysis is the process of analyzing company's performance to determine its Profitability status and Liquidity position. It provides a deep understanding of viability of given venture. To understand role played by financial analysis in judging company's performance, the key financial ratios of 3 leading companies in healthcare space i.e. Apollo Hospitals Enterprises Limited (AHEL), Narayana health Limited (NH) and Healthcare Global Enterprises Limited (HCG) are calculated and studied. Since the 3 companies operate in the same industry segment i.e. healthcare service delivery, the differences in the financial ratios of the 3 companies would throw light on the specific differences in ways operation of the companies are conducted and how their balance sheets are structured. The idea is also to provide recommendations on which areas these companies could focus on from a financial perspective. But at the same time Financial analysis has limitations in that it analyses the financial statements of the companies on an as-is static basis and does not take into account the future strategy, industry scenario and qualitative strengths / weaknesses of the companies involved.

Keywords: ***Financial analysis, Current Ratio, Return on Capital Employed, Interest Coverage Ratio, Inventory Turnover, Debtors Turnover, Creditors Turnover, Debt to Equity***

I. INTRODUCTION

Financial analysis deals with analysis of financial statements of the Company from a financial perspective. Financial can be prima-facie indicators of the profitability, liquidity, efficiency and leverage of a Company. These ratios are categorized as a) Profitability ratios, b) Efficiency Ratios c) Working capital related Ratios d) Liquidity Ratio e) Leverage ratios. It is used by companies for monitoring performance and taking corrective measures, by investors for evaluating the attractiveness of the Company's securities and by lenders for ascertaining the financial health and ability of the Company to honour its financial obligations. However, financial analysis cannot be looked at in isolation and only at a given point in time for a company. It is important to look at their movement from one year to another. Likewise, it is difficult to interpret ratios by looking at them for one company only. At the same time, the companies chosen for analysis cannot be taken from different industry segments since different industry sectors would have their own specific industry characteristics, thereby making the comparison difficult. Therefore, one needs to look at 2-3 companies from the same sector over a period of minimum 2 years to carry out meaningful analysis, comparisons and recommendations, which has been done for the purposes of this research article.

II. OBJECTIVES OF THE STUDY

i) To understand how companies use the financial analysis for monitoring, financial control and communication to their stakeholders.

ii) To carry out critical inter-company comparison of financial ratios among these 3 companies.

iii) To draw inferences regarding financial strengths and weaknesses of the companies on a relative and absolute basis.

iv) To understand industry specific reasons for the differences in the ratios and comment on the same.

Main Body:

Key financial ratios of 3 leading companies in healthcare space i.e. Apollo Hospitals Enterprises Limited (AHEL), Narayana health Limited (NH) and Healthcare Global Enterprises Limited (HCG) are analyzed to understand the differences in the profit margin, liquidity, leverage and return profiles of the these companies. Since the 3 companies operate in the same industry segment, the differences in the ratios of these companies would throw light on the specific differences in ways operation of the companies are conducted and how their balance sheets are structured. Therefore, valuable insights could be derived from comparing such ratios side by side and the objective of this research project is to understand and highlight those learning's. The idea is also to provide recommendations on which areas these companies could focus on from a financial perspective.

III. A BRIEF OVERVIEW OF ABOVE HEALTHCARE COMPANIES:

1) Apollo Hospital Enterprises Limited (AHEL):

AHEL is the pioneer of corporate healthcare services delivery in India, was founded by Dr Prathap C Reddy in 1979. From that humble beginning over three decades back, AHEL has emerged as the pre-eminent private sector healthcare provider in India. AHEL is headquartered in Chennai and its diversified operations include multiple subsidiaries, joint ventures and associates. Today, AHEL's presence includes over 10,000 beds across 70 hospitals, over 2,500 pharmacies, over 172 primary care and diagnostic centres and over 148 telemedicine centres across 13 countries.

2) Narayana Health Limited (NH):

Narayana Health Limited (NH) is one of India's leading private healthcare service providers, operating a chain of multispecialty, tertiary healthcare facilities. Headquartered in Bengaluru, NH has a network of 24 hospitals (multispecialty and superspecialty healthcare facilities, which provide tertiary care), seven heart centres across India and one hospital in Cayman Islands.

3) Healthcare Global Enterprises Limited (HCG):

HealthCare Global Enterprises Ltd. (HCG), is headquartered in Bangalore, is the largest provider of cancer care in India. Through its network of 18 comprehensive cancer centres spread across India, HCG has brought advanced cancer care to the doorstep of millions of people. Its comprehensive cancer centres provide expertise and the latest technologies in diagnosis and treatment of cancer under one roof. HCG has pioneered the introduction and adoption of several technologies in the country including stereotactic radio-surgery, robotic radio-surgery and the use of genomics for personalized treatment of cancer.

Computation of key ratios for the companies in research:

Financial Ratios	AHEL		NH		HCG	
	31-3-17	31-3-16	31-3-17	31-3-16	31-3-17	31-3-16
EBITDA Margin	*10.0%*	*11.1%*	*11.9%*	*10.8%*	*15.0%*	*14.5%*
Cash conversion ratio	*79.0%*	*86.8%*	*98.6%*	*99.7%*	*92.7%*	*99.2%*
Current Ratio	*2.2*	*1.6*	*0.9*	*0.9*	*0.7*	*0.9*
Return on Capital Employed	*6.6%*	*7.6%*	*10.9%*	*8.0%*	*5.4%*	*5.2%*
Interest Coverage Ratio	*2.8*	*3.8*	*10.2*	*5.9*	*4.6*	*2.2*
Inventory Turnover	*7.7*	*7.5*	*8.3*	*7.8*	*9.1*	*11.2*
Debtors Turnover	*9.7*	*10.2*	*11.9*	*10.6*	*6.8*	*8.4*
Creditors Turnover	*7.2*	*5.6*	*2.3*	*2.4*	*1.2*	*1.4*
Debt to Equity	*0.9*	*0.9*	*0.3*	*0.3*	*1.3*	*1.1*

IV. FINANCIAL ANALYSIS OF ABOVE DATA:

EBITDA Margin: A review of the EBITDA margins of the 3 companies shows that while HCG enjoys higher EBITDA margin of 15%, NH and AHEL are much higher at 10-12%. This is primarily explained by the growth stage of the 3 companies. AHEL has a number of businesses in early stage such as its retail business which is loss making, which drags down the EBITDA on a consolidated basis. NH has made significant investments in setting up new hospitals and the hospitals take a long time to become profitable. In case of HCG, the drag of the new hospitals appears to be lower. Therefore, when analyzing EBITDA margins, the difference in the growth stage of the businesses should be taken into account.

Cash Flow conversion ratio: A review of the cash flow conversion of the 3 companies shows that Apollo has a lower cash flow conversion of 80-85% while NH and HCG have a higher ratio close to 100%. This is on account of better working capital management of the same by NH and HCG. This has resulted in lowering of cash outgo for working capital for NH and HCG and thus significantly higher ratio for both the companies. Therefore, working capital cycle is the key to understanding differences for this ratio between companies and over a period of time.

Current Ratio: A review of the current ratios of the 3 companies shows that Apollo has a higher current ratio close to 2 times while NH and HCG have a lower ratio close to 1. While this may denote better liquidity profile of AHEL compared to NH and HCG, this could also show that NH and HCG have been able to get better terms from their suppliers which has resulted in a longer payables position compared to debtors and inventory. Therefore, current ratio in this case may not be sufficient to draw a conclusion that NH and HCG have an inferior liquidity position while that's the prima-facie inference.

Return on Capital Employed: A review of the RoCE of the 3 companies shows that NH has a higher RoCE close to 8- 11% while AHEL is close to 7-8% and HCG has the lowest ratio close to 5%. NH has a capital light model wherein it does not own many of the hospital properties it operates on a lease model and hence capital employed is relatively lower. This combined with about 6% operating margins provides NH with a higher RoCE. HCG also rents the properties but the investment in equipment is higher and hence capital employed is relatively higher. Also several of HCG's new centres are ramping up and not yet operating at full capacity. AHEL has a mix of own and leased assets and therefore has a RoCE in the middle. For all the 3 chains, RoCE is expected to improve as their hospitals and clinics ramp-up and start generating higher profits.

Interest Coverage Ratio: A review of the Interest coverage ratios of the 3 companies shows that NH has the highest interest coverage at 10 times followed by HCG at 7 times and AHEL at 3times.

Inventory Turnover: A review of the inventory efficiency ratios of the 3 companies show that the inventory holding periods are close to 40-50 days for all 3 companies. The stock of these companies generally comprises medicines and consumables held for use at hospitals.

Debtors Turnover: A review of the Debtors' efficiency ratios of the 3 companies shows that the collection periods are close to 35 days for NH and AHEL, while they are a little higher for HCG at 45-50 days. While it is difficult to ascertain exact reason for the difference, this could be on account of higher mix of insurance patients in HCG where the payment cycle is longer.

Creditors Turnover: A review of the Creditor turnover ratios of the 3 companies shows that he credit periods enjoyed are close to 50 days for AHEL, they are a much higher for NH at around 150 days, while HCG is highest at close to 300 days. One possible explanation for this is that NH and HCG would have incurred significant capex during these 2 years and some of the credit enjoyed is capex credit. The other explanation is that they would have stretched the creditors cycle to manage working capital better. In case of AHEL, the credit period enjoyed is much lower on account of significant contribution of pharmacy business in the consolidated mix werein the credit period is close to 45-60 days.

Debt to Equity: A review of the Debt equity ratios of the 3 companies shows that HCG is highest levered at 1.3 times, followed by AHEL close to 1 times while the NH is lowest at 0.3 times. The reason for higher leverage for HCG is that they buy equipment from suppliers on credit which also gets added to debt on balance sheet.

V. CONCLUSIONS

One of the main learnings of this article through the detailed analysis of the 3 healthcare giants is that though financial analysis is very important tool for analyzing a company's performance, these numbers need to be put in context and not looked at in isolation. Unless one understands the business characteristics of the Company being analyzed, it would be very difficult to have a meaningful analysis. Companies surely monitor most of the ratios periodically, but they do not look for day to day or week to week fluctuations. Instead, they have short-term, medium-term and long-term targets for the ratios which they review and communicate periodically.

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