RATING REPORT

Shifa International Hospitals Limited (Shifa)

REPORT DATE:
November 11, 2019

RATING ANALYSTS:
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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	Long-term	Short-term	Long-term	Short-term
Entity	AA-	A-1	AA-	A-1
Rating Date	*06 Nov '19*		*01 Mar'18*	
Rating Outlook	Stable		Stable	
Rating Action	Reaffirmed		Initial	

COMPANY INFORMATION	
Incorporated in 1987	**External auditors:** Grant Thornton Anjum Rahman & Co. Chartered Accountants
Public Listed Company	**Chairman:** Dr. Habib-Ur-Rehman **Chief Executive Officer:** Dr. Manzoor H. Qazi
Key Shareholders (with stake 5% or more):	
Mrs. Kalsoom Zaheer Ahmad	
Tameer-e-Millat Foundation	
Matthews Emerging Asia Fund	
International Finance Corporation	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: Corporates (May 2019) *http://www.vis.com.pk/kc-meth.aspx*

Shifa International Hospitals Limited (Shifa)

OVERVIEW OF THE INSTITUTION

Shifa International Hospitals Limited (Shifa) was incorporated in 1987 as a private limited company. Later, it was converted into a public limited company in October 1989. Shifa was listed on the Pakistan Stock Exchange Limited (PSX) in 1995.

Financial Snapshot

Tier-1 Equity: end-FY19: Rs. 4.9b; end-FY18: Rs. 4.4b; end-FY17: Rs. 4.1b.

Assets: end-FY19: Rs. 11.9b; end-FY18: Rs. 10.1b; end-FY17: Rs. 7.7b.

Profit After Tax: FY19: Rs. 777m; FY18: Rs. 557m; FY17: Rs. 606m.

RATING RATIONALE

The assigned ratings take into consideration the clinical reputation of Shifa as a large private healthcare organization within northern region of the country and ample experience of senior management team. The ratings draw comfort from Shifa's unique positioning, vis-à-vis other large hospitals, as an integrated health system providing primary, secondary, tertiary and quaternary healthcare services with the hospital specializing in high acuity cases. The ratings also factor in broad services array and scale of operations as well as significant expansion plans, including establishment of large-scale hospital and medical center in Faisalabad and Islamabad, respectively.

The ratings also draw comfort from the limited demand cyclicality in healthcare services sector and growing demographic trends of Pakistan. Underpinned by growing demand for healthcare services, the company has generated sustainable revenue growth on a timeline basis. Deficit of human capital in the industry is considered a business risk factor. The ratings also factor in sustained profitability, healthy generation of funds from operations, adequate debt coverage and manageable leverage. The ratings also positively view the equity issuance to International Finance Corporation (IFC) with the aim to support the expansion plans.

Scale of Operations

Shifa currently has four hospitals in operations. Established in 1993, Shifa H-8 Hospital Islamabad (Shifa H-8) is the flagship hospital of the company with ~550 beds and IPD/OPD facility. During FY18, all the four floors of Block 'C' were remodeled and renovated with the inclusion of OPD Clinics, Medical ICU, Medical Step-down beds, Isolation and IPD rooms. The renovation of Block F-O was also carried out to house different radiology facilities.

Shifa G-10 Hospital Islamabad (Shifa G-10) was setup in 2014 to reduce workload at H-8. The hospital was providing IPD/OPD services including neurology, nephrology and urology & rehabilitation centre. The facility had ~30 IPD beds and a dialysis unit. During financial year 2018-19, this facility has been converted into complete dialysis unit due to ever growing demand for such services. Shifa Medical Center F-11 Islamabad (Shifa F-11) was established to facilitate residents of sectors F-10, F-11 and E-9, and their surrounding areas by delivering services at lower time/traveling cost. Services include OPD specialties, laboratory tests, x-ray, ultrasound, dentistry and onsite pharmacy. Shifa Hospital Faisalabad (Shifa Faisalabad) was established in 2011 and is engaged in provision of IPD/OPD, diagnostic and critical care services with ~55 beds.

Shifa H-8 is the flagship hospital of the company, accounting for nearly 90% of total revenue. At hospital located in H-8 sector, Shifa is providing broad service array with state of the art equipment in departments including allergy, cardiology, dermatology, dental, emergency medicine, endocrinology, gastroenterology, general and vascular surgery, minimally invasive neurosurgery, plastic and reconstructive surgery, infectious diseases, nephrology, ophthalmology, pediatrics, pulmonology, rheumatology, urology, ear nose & throat, orthopedic, obstetrics & gynecology and psychiatry. Shifa also provides oncology services including medical & surgical management, radiation therapy and chemotherapy. Shifa is one of the few hospitals in the world, where four transplants i.e. liver, bone marrow, renal and corneal are being performed under one roof. Laparoscopic surgery, interventional radiology, comprehensive critical care and GI & Endoscopy suite are also few of the notable services provided by Shifa.

Revenue and Profitability

Revenue stream of Shifa comprises four segments, namely Inpatient (IPD), Outpatient (OPD), Pharmacy, and Cafeteria. Revenue concentration risk is considered manageable as the overall mix has remained largely stable over the past three years, with IPD accounting for 41% of gross revenue during FY19 (FY18: 39%; FY17: 39%), followed by OPD 22% (FY18: 22%; FY17: 22%), Pharmacy 34% (FY18: 36%; FY17: 36%) and Cafeteria 3% (FY18: 3%; FY17: 3%). Nearly 60% of patients come from Islamabad/Rawalpindi and the remaining patients from northern areas. Moreover, while the company is looking to expand into Islamabad, Faisalabad and Tanzania, the geographic concentration is expected to remain around similar levels in the short to medium term, albeit new projects would reduce dependence on Shifa H-8 to some extent.

Within IPD/OPD segments, the service portfolio comprises clinical procedures, radiology, laboratory, surgical procedures, consultation and other services. Net revenue of Shifa increased 14% to Rs. 11.7b during FY19 (FY18: Rs. 10.3b; FY17: Rs. 9.3b), as barring Cafeteria, all other segments registered growth during the period. IPD segment revenue grew by 20% to Rs. 4.8b during FY19 (FY18: Rs. 4b; FY17: Rs. 3.7b) mainly on the back of higher IPD admissions. Available bed days at Shifa H-8 were recorded higher at 175,734 days during FY19 (FY18: 167,781 days; FY17: 162,356 days). Meanwhile, occupied bed days increased steadily to 118,808 (FY18: 117,671; FY17: 113,927)

Available bed days at Shifa Faisalabad were recorded lower at 13,505 (FY18: 14,322; FY17: 16,514) owing to optimization of operations and ongoing extension, however, occupied bed days steadily increased to 5,724 (FY18: 5,455; FY17: 5,095), which resulted in improved occupancy ratio of 42.4% (FY18: 38.1%; FY17: 30.9%). No IPD operations were conducted at Shifa G-10 during FY19 as it was converted into dialysis only center.

OPD segment revenue increased by 15% to Rs. 2.6b during FY19 (FY18: Rs. 2.3b; FY17: Rs. 2.1b) mainly on account of sustained growth in OPD visits. Revenue growth also emanated from increased number of doctors, commencement of evening clinics, 24/7 radiology, and volumetric increase in CT Scan and MRI and other lab tests. Pharmacy segment witnessed 10% growth in revenue which amounted to Rs. 4b during FY19 (FY18: Rs. 3.7b; FY17: Rs. 3.2b) due to volumetric increase.

In line with the business growth, operating costs increased to Rs. 10.6b (FY18: Rs. 9.5b; FY17: Rs. 8.5b), driven largely by inflationary adjustment in salaries, wages & other benefits, utilities, supplies and medicines consumed as well as higher depreciation charge during FY19. Finance cost amounted to Rs. 96m (FY18: Rs. 57m; FY17: Rs. 66m) owing to increase in debt financing and increase in Policy rates by SBP. Resultantly, the company reported earnings before interest, taxation, depreciation & amortization (EBITDA) of Rs. 1.7b during FY19 (FY18: Rs. 1.3b; FY17: Rs. 1.4b) with an improved EBITDA margin of 14.8% (FY18: 12.9%; FY17: 15.0%). Accounting for income tax, Shifa's net profit increased to Rs. 777m (FY18: Rs. 557m; FY17: Rs. 606m) on the back of improved net margin of 6.6% (FY18: 5.4%; FY17: 6.6%).

Asset Mix

Asset base of the company augmented to Rs. 11.9b by end-FY19 (FY18: Rs. 10.1b; FY17: Rs. 7.7b) with an increase in both fixed and current assets. Property, plant and equipment increased to Rs. 6.8b (FY18: Rs. 6b; FY17: Rs. 5.5b) due to higher capex of Rs. 1.6b (FY18: Rs. 1.1b; FY17: Rs. 1.3b), of which work-in-progress was Rs. 929m (FY18: Rs. 421m; FY17: Rs. 247m) and mainly pertained to installation of CT, angio & MRI machines, neuro navigation system, server virtualization, brachytherapy machine, flow cytometer machine, ventilator high frequency, immobilization devices, and Shifa guest house. Investment property amounted to Rs. 1.6b (FY18: Rs. 1.4b; FY17: nil) comprising leasehold land with a multistory building, which the company intends to sublet to its subsidiary Shifa Neuro Sciences Institute Islamabad (Private) Limited. Intangible assets increased to Rs. 84m (FY18: Rs. 33m; FY17: Rs. 11m) as the company made further capex in Oracle Financials along with other software platforms to strengthen its MIS. Long-term deposits amounted to Rs. 87m (FY18: Rs. 61m; FY17: Rs. 45m), which mainly pertained to Ijarah key money deposit and security deposits given to various institutions.

The expansion/renovation projects that were completed during FY19 included D4 Lab renovation/alternation under Total Lab Automation (TLA) project, Afghan patient facilitation office, employee health clinic, blood bank relocation, GCC area renovation, rehabilitation (orthotic lab relocation), and commencement of operations at F-O block.

Shifa long-term investments increased to Rs. 80m by end-FY19 (FY18: Rs. 18m; FY17: Rs. 18m). Long-term investments comprised following projects;

- 100% shareholding in Shifa Medical Center Islamabad (Private) Limited (SMC) worth Rs. 39.8m (FY18: nil). SMC has been incorporated with the aim to focus on diagnostic services, day care surgeries, specialty OPD clinics, 24/7 emergency room and urgent care services. The land has been transferred to the SMC. The construction work will commence after the regulatory approval and project will be completed in two years. The company is projecting to achieve breakeven in the first year of operations.

- 100% shareholding in Shifa National Hospital Faisalabad (Private) Limited (SNH) worth Rs. 8.2m (FY18: nil). Shifa plans to expand its footprint in Faisalabad by establishing SNH. Land for the hospital has been acquired while other activities like architectural plans and related legal requirements are underway at different stages of completion. The project will be completed in two phases over four years. Around 150 beds will be added in Phase 1. Moreover, the company is projecting to achieve breakeven in the third year of operations.

- 100% shareholding in Shifa Neuro Sciences Institute Islamabad (Private) Limited (SNCS) worth Rs. 7.5m (FY18: nil). Shifa is planning to offer neurology, neurosurgical, neurophysiology, neuroimaging/neuroradiology, and neuro-rehab services by developing a neurosciences center in Islamabad under the umbrella of SNCS. Land and multistory building has been acquired for that purpose.

- Reduced investment in Shifa Development Services (Private) Limited (SDS) to Rs. 10m (FY18: Rs. 18.1m) by selling 45% shareholding to M/S October Holding (Private) Limited. SDS is a healthcare-focused development and management services provider, which is currently managing different projects of Shifa including Shifa Pan Africa Hospitals, Dar-es-Salaam Tanzania, Shifa Faisalabad, F-11 Islamabad, SNCS Islamabad, City Hospital Sialkot and expansion projects of H-8 and Faisalabad facilities.

- 50% shareholding in Shifa Care (Private) Limited (SCPL) worth Rs. 14.4m (FY18: nil). SCPL has been established in collaboration with a strategic investor with the aim to develop HIMSS compliant healthcare management information solution for enterprise healthcare organizations.

Stores, spares and loose tools increased to Rs. 132m by end-FY19 (FY18: Rs. 120m; FY17: Rs. 81m) owing to installation of new machinery and construction work. In line with the growing revenue base, stock in trade (medicine) increased to Rs. 497m (FY18: Rs. 469m; FY17: Rs. 380m). Meanwhile, trade debts decreased to Rs. 581m (FY18: Rs. 714m; FY17: Rs. 448m) due to vigilant collection strategy. Credit sales pertain to corporate clients and insurance companies and on average account for 30% - 35% of total revenue. Loans and advances remained largely stable at Rs. 413m (FY18: Rs. 419m; FY17: Rs. 340m) as the impact of slight increase in advances to suppliers and contractors was offset by decline in loans to employees. Trade deposits and prepayments amounted to Rs. 61m (FY18: Rs. 53m; FY17: Rs. 38m).

Tax refund due from government was recorded at Rs. 413m (FY18: Rs. 348m; FY17: Rs. 97m) on account of lower payment/deduction at source and higher provision for the year. Cash and bank balance accumulated to Rs. 792m (FY18: Rs. 479m; FY17: Rs. 642m), of which Rs. 641m (FY18: Rs. 398m; FY17: Rs. 566m) were parked in saving accounts, carrying effective profit rate between 2.25% and 6.88%. Shifa recorded Rs. 307m in non-current assets held for sale, at end-FY19 (FY18: nil) against carrying amount of a plot located at sector F-11 Islamabad, which has been sold to Shifa Medical Center Islamabad (Private) Limited subsequent to the year end.

Liquidity and Cash Flows
Shifa has witnessed notable improvement in cash flows generation as funds from operations (FFO) increased to Rs. 1.4b during FY19 (FY18: Rs. 858m; FY17: Rs. 995m) due to better profits and steady income tax payments. Resultantly, FFO-to-total debt ratio improved to 0.54x (FY18: 0.51x; FY17: 1.97x) despite considerable increase in debt burden. Debt coverage ratio (DSCR) improved considerably to 5.28x during FY19 (FY18: 2.37x; FY17: 2.64x) on account of higher FFO amid lower debt repayment. Going forward, the DSCR may decrease to some extent owing to likely increase in debt repayments, albeit Shifa's capacity to timely meet its financial obligations is expected to remain adequate. Current ratio decreased marginally to 0.81x by end-FY19 (FY18: 0.83x; FY17: 0.97x).

Capitalization and Funding
Equity base, excluding Rs. 772m in revaluation surplus, augmented to Rs. 4.9b by end-FY19 (FY18: Rs. 4.4b; FY17: Rs. 4.1b) with the retention of profits. Distribution to shareholder in the form of dividend amounted to Rs. 245m for FY19 (FY18: Rs. 273m; FY17: Rs. 164m), with lower payout ratio of 32% (FY18: 49%; FY17: 27%). Total liabilities increased to Rs. 6.3b by end-FY19 (FY18: Rs. 5b; FY17: Rs. 2.9b) on account of trade & other payables of Rs. 3.3b (FY18: Rs. 3b; FY17: Rs. 1.9b) and new borrowings. Trade creditors were recorded at Rs. 1.5b at end-FY19 (FY18: Rs. 1.4b; FY17: Rs. 708m) due to higher operating revenue.

The debt profit of Shifa comprises long-term borrowings only. Total long-term borrowings, inclusive of current portion, were recorded higher at Rs. 2.5b by end-FY19 (FY18: Rs. 1.7b; FY17: Rs. 504m) as Shifa mobilized new financing to fund the capex. The syndicated Islamic finance facility – 2 carries markup rate of 3-month KIBOR plus 0.85% and is repayable in 14 equal quarterly installments, while diminishing musharakah facility carries markup rate of 3-month KIBOR plus 0.80% and is repayable in 36 equal monthly installments. The gearing and debt leverage indicators increased to 0.51x (FY18: 0.38x; FY17: 0.12x) and 1.29x (FY18: 1.14x; FY17: 0.69x), respectively, by end-FY19, the said indicators are still considered manageable.

On July 12, 2019, Shifa issued 7.44m ordinary shares of the company to IFC at a price of Rs. 239.21 per share, resulting in total proceeds of Rs. 1.78b which will be utilized as equity injection in SMC Islamabad and SNH Faisalabad. IFC will have one member on the board of Shifa, and the lock-in period is 5 years.

Habib Bank Limited (HBL) has agreed to provide long-term loan of Rs. 2.34b for the debt portion. The tenure of loan is 10 years with grace period of 3 years and repayable in semi-annual instalments having markup rate of 6 months KIBOR plus 0.85%. As the amount of long-term loan will appear on the balance sheet of respective subsidiaries, the leverage indicators of Shifa due to these borrowings will remain unaffected on a standalone basis.

Shifa International Hospitals Limited (Shifa) — Annexure I

FINANCIAL SUMMARY *(amounts in PKR millions)*			
BALANCE SHEET	**FY17**	**FY18**	**FY19**
Property, Plant & Equipment	5,458	6,029	6,846
Investment Property	-	1,402	1,642
Non-Current Assets Held for Sale	-	-	307
Stores, Spare, and Loose Tools	81	120	132
Stock-in-Trade	380	469	497
Trade Debts	448	714	581
Loans and Advances	340	419	413
Tax Refund Due from Government	97	348	413
Cash & Bank Balance	642	479	792
Other Assets	303	165	315
Total Assets	**7,748**	**10,146**	**11,938**
Trade and Other Payables	1,932	2,917	3,328
Short-Term Borrowings	-	6	-
Long-Term Borrowings *(Inc. current matur)*	504	1,675	2,499
Deferred Tax	414	375	384
Other Liabilities	27	46	79
Total Liabilities	2,877	5,020	6,291
Tier-1 Equity	**4,145**	**4,403**	**4,875**
Paid Up Capital	545	545	545
INCOME STATEMENT	**FY17**	**FY18**	**FY19**
Operating Revenue	9,257	10,271	11,744
Operating Costs	8,465	9,508	10,630
Profit Before Tax	863	768	1,073
Profit After Tax	606	557	777
FFO	966	826	1,318
RATIO ANALYSIS	**FY17**	**FY18**	**FY19**
EBITDA Margin (%)	15.0	12.9	14.8
Net Working Capital	(78)	(535)	(682)
FFO to Long-Term Debt	1.97	0.51	0.54
FFO to Total Debt	1.97	0.51	0.54
Debt Servicing Coverage Ratio (x)	2.64	2.37	5.28
ROAA (%)	-	6.2	7.0
ROAE (%)	-	13.0	16.8
Gearing (x)	0.12	0.38	0.51
Debt Leverage (x)	0.69	1.14	1.29
Current Ratio	0.97	0.83	0.81

ISSUE/ISSUER RATING SCALE & DEFINITIONS Annexure II

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES	Annexure III
Name of Rated Entity	Shifa International Hospitals Limited
Sector	Healthcare
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
6-Nov-19	AA-	A-1	Stable	Reaffirmed
1-Mar-18	AA-	A-1	Stable	Initial

Instrument Structure	N/A
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.
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