RATING REPORT

Shifa International Hospitals Limited (Shifa)

REPORT DATE:
December 29, 2022

RATING ANALYSTS:
Maham Qasim
maham.qasim@vis.com.pk

Qudsia Abbas
qudsia.abbas@vis.com.pk

RATING DETAILS				
Rating Category	**Latest Rating**		**Previous Rating**	
	Long-term	**Short-term**	**Long-term**	**Short-term**
Entity	AA-	A-1	AA-	A-1
Rating Date	*29th Dec '22*		*18 Nov '21*	
Rating Outlook	Stable		Stable	
Rating Action	Reaffirmed		Reaffirmed	

COMPANY INFORMATION	
Incorporated in 1987	**External auditors:** BDO Ebrahim & Co. Chartered Accountants for FY23
Public Listed Company	**Chairman:** Dr. Habib-Ur-Rehman **Chief Executive Officer:** Dr. Manzoor H. Qazi
Key Shareholders (with stake 5% or more):	
Tameer-e-Millat Foundation – 12.57%	
International Finance Corporation – 12.0%	
Mrs. Kalsoom Zaheer Ahmad – 8.40%	
Jubliee Life Insurance Company Limited – 9.68%	

APPLICABLE METHODOLOGY
VIS Entity Rating Criteria Methodology – Industrial Corporates (August 2021) **https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf**

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 1994. The hospital is Gold accredited by Joint Commission International (JCI) that certifies Shifa meeting international health care quality standards for patient care and organization management.

Profile of Chairman

Dr. Habib-Ur-Rahman graduated from King Edward Medical College. He received his internal medicine training at D. C. General Hospital, Howard University, Washington D.C. and Wayne State University, Detroit, Michigan and Wright State University, Dayton Ohio. He completed his fellowship of cardiovascular disease from Mount Sinai Hospital, University of Connecticut, Hartford, Connecticut.

Profile of CEO

Dr. Manzoor H. Qazi is a founding member of Shifa and has been a board member since its inception. He was appointed as CEO of the company on 10th October 2011. He received his medical degree from King Edward Medical College Lahore.

RATING RATIONALE

The ratings assigned to Shifa International Hospitals Limited (Shifa) 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 incorporate broad services array and scale of operations, as well as significant expansion plans over the next three years, involving establishment of large-scale hospital in Faisalabad. Business risk profile is considered to be medium to low given limited demand cyclicality in healthcare services sector and growing demographic trends of Pakistan. However, deficit of human capital in the industry is considered a business risk factor. Underpinned by growing demand for healthcare services, the company has generated sustainable revenue growth on a timeline basis. Growth momentum in operating revenue was experienced during the rating review period due to resumption in OPD services post pandemic closures. The ratings also factor in sound financial risk profile underpinned by comfortable FFO to total debt, adequate debt service coverage, and sizable cash position and scaled down leverage indicators. Going forward, the ratings remain dependent on timely completion of ongoing project without major cost escalation, projected uptick in revenues and maintenance of leverage indicators at around current levels.

Business Environment & Scale of Operations

Pakistan, being the world's 5th largest nation by population, faces various constraints and limitations to ensure equitable & convenient access of specialized quality healthcare services to the masses. Therefore, many developing countries have adopted Universal Health Coverage (UHC) to provide equitable health coverage to the people in the recent years. The Government of Pakistan has also announced a health card for the entire population of Punjab after piloting that in KPK province. For a corporate healthcare model like Shifa, provision of quality healthcare in compliance with international accreditation standards is cost intensive. However, keeping in view the prevailing trend, provision of healthcare in Pakistan will be impacted by an ongoing partnership between public and private sectors to address the challenges of affordability, and availability of healthcare.

Shifa currently has three hospitals in operation. 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. Shifa H-8 continues to account for more than 90% of total revenue. Services on offer include OPD, laboratory tests, x-ray, ultrasound, dentistry and onsite pharmacy. The hospital provides an extensive range of services with state-of-the-art equipment in 36 departments, which include 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. In addition to that, there are oncology services on offer as well, including medical & surgical management, radiation therapy, and chemotherapy. Not only that, Shifa is the only hospital in the country 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. During FY22, Sunday OPD clinics initiative was launched to not only facilitate patients by offering convenient time slots for OPD consultations but also to improve utilization of service provisions during low peak hours. Furthermore, by anticipating the increase in presence of Chinese nationals in Pakistan as part of CPEC projects, efforts are currently underway to facilitate these patients by establishing Chinese patients' coordination office on the same pattern through which Afghan citizens are facilitated.

Moreover in 2011, a 55 bed hospital was established in Faisalabad to provide IPD/OPD, diagnostic and critical care services. During the rating review period, Shifa has also adopted a market development strategy of expanding its footprint in major cities within its catchment area through digital means and on-ground presence to emerge as a local healthcare service provider for local communities. As part of the execution, throughout FY22 specialty OPD clinics were conducted in various cities as multi-specialty consultants visit cities and examine patients in person.

Profitability

SIHL's revenue base witnessed an increase of 14% to Rs. 16.2b (FY21: Rs. 14.2b) in FY22 mainly attributable to increase in capacity utilization due to returning of OPD/IPD services and elective surgeries back to pre-COVID level. The revenue stream for SIHL is classified in 3 segments namely Inpatient (IPD), Outpatient (OPD), and Other Services. Within IPD/OPD segments, the service portfolio comprises of clinical procedures, radiology, laboratory, surgical procedures, consultation and other services. The Other Services consist of revenue from external pharmacy outlets, internal pharmacy sales, cafeteria sales, operating leases to related parties/ other parties and corporate services to subsidiaries/associate respectively. During FY22, all segments have reverted back to pre-COVID levels and witnessed stable growth. The revenue concentration risk is considered manageable as the overall mix has largely remained stable over the years, with IDP contributing 59% (FY22: 60%; FY21: 60%), OPD contributing 34% (FY22: 34%; FY21: 34%) and Other Services contributing 7% (FY22: 6%; FY21: 6%) to gross revenue in 1QFY23. IPD segment revenue was recorded higher at Rs. 9.8b (FY21: Rs. 8.7b) as an outcome of increase in occupancy ratio of both Shifa H-8 and Shifa Faisalabad to 58.8% (FY21: 55.8%) and 26.4% (FY21: 23.1%) respectively during FY22. Revenue generated from OPD segment also witnessed an increase of 13% to Rs. 5.5b (FY21: Rs. 4.9b) as normal operations continued through the year without any frequent lockdowns. Other Services also reported growth of 23% to Rs. 1.0b (FY21: Rs. 843.0m) during FY22. Going forward the growth in revenue will be a function of increase in volume of business leading to increased capacity utilization coupled with increase in prices due to inflationary pressures. As per the management, the prices have been increased July'22 onwards on account of medical equipment, medicines and utilities becoming expensive in wake of increased fuel cost and currency devaluation.

Due to inflationary pressures the operating costs also increased in the same proportion as overall revenue. Operating cost was recorded at Rs. 14.8b (FY21: Rs. 12.9b); the increase was largely manifested in employee related expenses, cost of medicines & supplies and utilities. SIHL reported sizable other income amounting to Rs. 637.4m (FY21: Rs. 107.4m) owing to exchange gain reaped on foreign currency translation. As per the management, for long-term investments to be made the institution had kept a deposit in dollar denomination worth USD $11.0m. Given the gradual utilization of amount for investments in subsidiaries leading to conversion of foreign currency into local currency would mitigate the associated risk in short to medium term. Subsequently, in line with improved absorption of fixed costs in line with growth in operating scale coupled with higher exchange gain, Shifa reported improved EBITDA and profit before tax margins at 17.9% (FY21: 15.6%) and 9.8% (FY21: 15.6%) respectively during FY22. In addition, the upward trajectory of revenues was maintained during the ongoing year as well with net revenue recorded at Rs. 4.8b in 1QFY23 as opposed to Rs. 3.9b in the corresponding quarter last year. As a result, profit after tax margin remained at 7.75% in spite of huge increase in policy rate, taxes and utility costs etc. during 1QFY23. The management expects to close FY23 at a higher revenue than FY22; in line with growth momentum evidenced along with planned commencement of other long-term initiatives undertaken by Shifa, the aim is deemed realistic and achievable.

Liquidity profile in terms of cash flow generation slightly decreased during the period under review despite improvement in profitability metrics in line with increased adjustment of foreign currency translation; however, the same remains sound. Sizeable cash and bank balances on the balance sheet provides additional liquidity buffer. Liquidity profile is expected to strengthen further with higher projected profitability, going forward.

Despite higher profits, SIHL's funds from operations (FFO) were reported lower at Rs. 1.8b in FY22 (FY21: Rs. 1.9b) mainly due to adjustment of high gain on foreign currency translation. On the other hand, FFO exhibited an improvement during the ongoing in line with higher margins and profitability and was recorded higher at Rs. 518.0m during 1QFY23 as compared to Rs. 465.0m in the corresponding quarter last year. As a result of the combined impact of improvement in FFO during the ongoing year coupled with reduction in total debt levels, FFO-to-total debt ratio improved on a timeline to 0.64x (FY22: 0.50x; FY21: 0.43x; FY20: 0.22x) at the end-1QFY23. Debt servicing coverage ratio (DSCR) declined during the rating review period in line with higher long-term debt repayments falling due; however, the same is considered adequate at 1.10x (FY22: 1.04x; FY21: 2.43x) at end-1QFY23.In addition, sizeable cash and bank balances amounting to Rs. 2.3b were recorded at end-FY22 providing additional liquidity buffer; however, the same decreased slightly by end-1QFY23 in line with increased challenging of funds towards long-term investments. Going forward, the FFO to total debt is projected to improve owing to higher internal capital generation and reduction in quantum of debt from FY22's position in the medium term.

Current ratio was reported lower on a timeline at 1.03x (FY22: 1.09x, FY21: 1.23x) at end-1QFY23 in line with elevated levels of trade payables; the same however remains comfortable from the ratings perspective. A similar trend is projected to be evidenced with current ratio reported lower than 1.0x from FY23-FY25 owing to increase in trade payables pertaining to construction related expenses emanating from ongoing long-term investment project. Liquidity profile is expected to strengthen further with higher projected profitability, going forward.

Sound Capitalization indicators

Equity base, excluding revaluation surplus of Rs. 857m, increased to 9.2b (FY22: Rs.8.8b, FY21: Rs. 7.7b) on account of increase in internal capital generation by end-1QFY23. The Directors have recommended a final cash dividend of Rs. 1.50/ share which in addition to the interim cash dividend of Rs. 1.50/share already paid to the shareholders accumulated to total cash dividend outlay of Rs. 3/ share for FY22. Shifa's outstanding debt profile only consists of long-term borrowings which inclusive of current portion and lease liabilities, decreased to Rs. 3.2b (FY22: Rs. 3.6b, FY21: Rs. 4.5b) by end-1QFY23, on account of regular servicing of debt obligations. The company availed additional long-term borrowing to the tune of Rs. 212.0m during the outgoing year largely under SBP's concessionary Islamic Refinance Facility and TERF to combat the impacts of covid-19 pandemic. The funds obtained from aforementioned facilities were utilized for purchase of medical equipment/machinery. Given procurement of incremental borrowings was outweighed by long-term repayments made during the year coupled with augmentation in equity base, the gearing and debt leverage indicators improved on the timeline to 0.35x (FY22: 0.40x, FY21: 0.59x) and 0.84x (FY22: 0.86x; FY21: 1.07x), respectively, at end-1QFY23. Although SIHL plans to draw additional funding amounting to Rs. 1.3b in FY24 to partially finance new project the leverage indicators are expected to scale down further in the medium term in line with sound profit retention.

Investment base expected to consistently increase over the next three years

Asset base of the company augmented to Rs. 17.7b (FY22: 17.2b; FY21: Rs. 16.7b) by end-1QFY23 in line with continuous investments in Shifa Medical Center Islamabad (Private) Limited (SMCI) and Shifa National Hospital Faisalabad (Private) Limited (SNHF); the long-term investments were reported higher at Rs. 4.2b (FY22: 3.9b; FY21: Rs. 3.2b) at end-1QFY23. With sufficient cash and bank balances at hand SIHL has planned to continue investment in the ongoing long-term project along with expansion and capacity expansion of the existing projects. The expected cash outlay on SNHF is estimated around Rs. 3.0b which is planned to be executed through a mix of own sources, and debt and proceeds from sale of SMCI in the medium term. Apart from the aforementioned; there are no major investment plans for the coming years. However, on the flip side, SIHL plans on introducing Sunday Clinics, Evening Clinics and introduce strategies to attract overseas patients to add to its revenue stream. Following is an overview of the on-going projects:

- SMCI: The Company planned to establish SMCI as a full fledge hospital in F-11. SMCI will have separate departments for diagnostic services, day care surgeries, specialty OPD clinics, 24/7 emergency room and urgent care services. The construction work on the project was started in FY21 with management expecting to complete the project by end-Dec'23. During the period under review, the shareholding remained unchanged with Shifa holding 56% stake in SMCI, Interloop Holdings (Private) Limited holds 40% and the remaining 4% is held by consultants. However, as per the decision made in the recent Board meeting SMCI is planned to be sold and the proceeds emanating from the sale are expected to be utilized for the construction of SNHF.

- SNHF: Shifa plans to expand its footprint with this project in Faisalabad. Till date, the company has acquired land spread over an area of 49.5 kanals for this purpose, which has already been commercialized. Ground breaking ceremony was held during the outgoing year. Around 200 beds are planned to be added in Phase-I, which was expected to be completed by the end-FY22 but due to COVID-19 pandemic and current economic slowdown the project has been delayed; the same is now projected to become fully operational during FY25. Slight delays are expected in this due to weakening of external macro-economic factors. The shareholding pattern remained unchanged during the rating review period with Shifa owning 60% of the shares, Interloop Holdings (Private) Limited with 30% shares and 10% shares held by Interloop Welfare Trust.
- Shifa Care (Private) Limited (SCPL) (an associated concern): SCPL has been established in collaboration with a strategic investor with the aim to develop HIMS compliant healthcare management information solution for enterprise healthcare organizations. An equity investment of Rs. 45m was made in this associated concern till date. The software produced will be used in-house and will also be sold to national and international customers. Once new revenue stream initiates, the project will bring in flexibility to the revenue mix.
- Shifa Neuroscience Institute (SNI): During the period under review, SNI has earned rental income from its building leased out to the Shifa to operate it as Shifa Neuro Sciences Institute in the existing building. Moreover, Shifa has recently moved its Neurology department to SNI to facilitate the patients by giving them all neuro-care services under one-roof.
- Chemo Daycare, Oncology Inpatient and Endoscopy: With the space freed up after shifting of neuro department to SNI building Shifa expanded its chemo daycare and oncology inpatient services and is now able to cater to more patients. Shifa also plans to expand it endoscopy department going forward.

Shifa International Hospitals Limited (Shifa) Annexure I

FINANCIAL SUMMARY *(amounts in PKR millions)*				
BALANCE SHEET	**FY20**	**FY21**	**FY22**	**1QFY23**
Property, Plant & Equipment	6,992	6,792	7,134	7,385
Long-term Investment	2,934	3,179	3,919	4,180
Non-Current Assets Held for Sale	495	598	321	299
Stores, Spare, and Loose Tools	151	165	210	207
Stock-in-Trade	646	658	712	742
Trade Debts	512	859	965	1,380
Loans and Advances	390	338	236	220
Tax Refund Due from Government	478	471	448	420
Cash & Bank Balance	2,395	2,809	2,317	1,986
Other Assets	266	823	950	903
Total Assets	15,259	16,692	17,212	17,722
Trade and Other Payables	2,984	3,251	3,587	4,059
Short-Term Borrowings	0	0	0	0
Long-Term Borrowings *(Inc. current matur)*	3,997	4,551	3,555	3,224
Total Borrowings	3,997	4,551	3,555	3,224
Deferred Tax	439	350	343	344
Other Liabilities	71	51	76	78
Total Liabilities	7,492	8,204	7,562	7,705
Tier-1 Equity	7,007	7,696	8,783	9,161
Total Equity	7,768	8,489	9,650	10,017
Paid Up Capital	620	620	632	632
INCOME STATEMENT	**FY20**	**FY21**	**FY22**	**1QFY23**
Operating Revenue	12,152	14,220	16,198	4,742
Operating Costs	11,481	12,899	14,792	4,327
Finance Cost	479	360	382	116
Profit Before Tax	797	964	1,592	498
Profit After Tax	505	700	1,163	367
FFO	933	1,937	1,769	518
RATIO ANALYSIS	**FY20**	**FY21**	**FY22**	**1QFY23**
EBITDA Margin	17.2%	15.6%	17.9%	18.0%
Profit Before Tax Margin (%)	6.6%	6.8%	9.8%	10.5%
Net Working Capital	1,141	1,110	448	147
FFO to Long-Term Debt (%)	0.23	0.43	0.50	0.64
FFO to Total Debt (%)	0.23	0.43	0.50	0.64
Debt Servicing Coverage Ratio (x)	1.81	2.43	1.04	1.10
ROAA (%)	4%	4%	7%	8%
ROAE (%)	9%	10%	14%	16%
Gearing (x)	0.57	0.59	0.40	0.35
Debt Leverage (x)	1.07	1.07	0.86	0.84
Current Ratio (x)	1.32	1.23	1.09	1.03

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 Ratings

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
29-Dec-22	AA-	A-1	Stable	Reaffirmed
18-Nov-21	AA-	A-1	Stable	Reaffirmed
24-Nov-20	AA-	A-1	Stable	Reaffirmed
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.
Probability of Default	VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.
Disclaimer	Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile. Copyright 2022 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.

Due Diligence Meetings Conducted

Name	Designation	Date
Mr. Shams ur Rehman Abbasi	CFO	14-Dec-2022
Mr. Rizwan Hussain	Associate Manager Finance	14-Dec-2022