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Look beyond drug producers

Investors can consider stocks of healthcare providers

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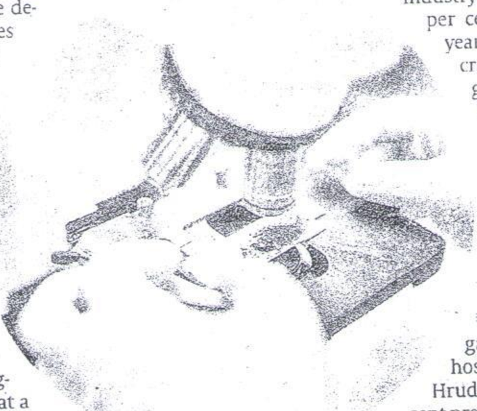
Expanding the scope of the pharmaceutical market to include healthcare opens a host of opportunities to investors. Factors such as favourable demographic profile, increasing focus on preventive healthcare and rising share of chronic diseases indicate strong domestic growth prospects for healthcare companies.

While such companies did not actively pursue the equity market earlier, a slew of healthcare IPOs in the recent past opens up an exciting new segment to investors. Offers from mid-cap companies that derive revenues by providing either healthcare delivery or diagnostic services have the potential to add zing to investor returns. Post-listing exposures, too, can be considered.



Diagnostic chains

According to a World Bank report, the healthcare spend in India is only 4 per cent of GDP and trails developing countries such as Brazil and China.

A CRISIL report estimates that the Indian diagnostic industry will grow at a CAGR of approximately 16-18 per cent to reach ₹58,500-61,600 crore in FY18. The report also expects the share of organised diagnostic chains to grow faster at a CAGR of 21-23 per cent to reach 16 per cent share by FY18.

Some companies in this segment have tapped the capital markets this fiscal year. The ₹638-crore offer for sale in December 2015 from New Delhi-based Dr Lal Path Labs witnessed strong investor interest. The issue was oversubscribed around 33 times. Propped up by strong financial performance, the debt free company trades at a trailing 12-month price earning ratio of around 60 times. This is almost three times the valuation of the broad-based indices and twice the earnings multiple of the S&P BSE Healthcare Index. Likewise, the offer for sale of Thyrocare Technologies was oversubscribed around 73 times and raised close to ₹480 crore. The company, which listed on May 9, closed with gains of 40 per cent.

The offer from pure-play pharmaceutical company Alkem Labs was also in demand. With oversubscription of around 44 times, it witnessed strong listing gains. The company, though, trades at a discount to the listed diagnostic players. Biocon's contract research arm Syngene International also had a good run. It was oversubscribed around 31 times, and now trades 55 per cent above its offer price.

Potential triggers

According to a WHO strategy report, the private sector dominates the personal healthcare market in India, providing 80 per cent out-patient care and 60 per cent of in-patient care. CRISIL estimates that the healthcare delivery industry will grow around 12 per cent over the next five years to reach ₹6,80,000 crore by 2019-20. Lower government investments in healthcare, low penetration of health insurance and high scope for medical tourism can act as potential triggers for organised players.

It is, therefore, not surprising that the ₹613-crore issue of Bengaluru headquartered hospital chain Narayana Hrudayalaya trades at a 23 per cent premium to its offer price. A low debt to equity ratio and asset-light operating model, coupled with plans to expand into anti-cancer, neurology and gastroenterology from cardiac care, is expected to drive revenues.

The common thread running through companies that have provided listing gains is a potent combination of sensible offer price, established business, strong management, good financials and viable growth prospects.

In the medium term, retail pharmaceuticals may well be the next emerging trend. According to *Pharmaleaders*, the unorganised channel commands 97 per cent of market share, providing ample scope for organised players to grow.

The evolution of e-commerce can also act as a fillip to such players.

Industry