Nobel Medical College Teaching Hospital Private Limited: [ICRANP] LBBB-/A3 assigned

March 29, 2019

Summary of rated instruments

Instrument	Rated Amount (NPR Million)	Rating Action
Long-term loans; Fund based (term loans)*	1,180	[ICRANP] LBBB- (Assigned)
Short-term loans; Fund based (working capital loans)	230	[ICRANP] A3 (Assigned)
Short-term loans; Non-fund based (letter of credit)	70	[ICRANP] A3 (Assigned)
Total	**1,480**	

** Including proposed term loans of NPR 500 million*

Rating action

ICRA Nepal has assigned a long-term rating of [ICRANP] LBBB- (pronounced ICRA NP L triple B minus) to the existing and proposed long-term loans of Nobel Medical College Teaching Hospital Private Limited (NMCTH). ICRA Nepal has also assigned a short-term rating of [ICRANP] A3 (pronounced ICRA NP A three) to the company's short-term loans (including the non-fund-based limits).

Rationale

The ratings assigned factor in the company's experienced promoter/management team along with its established operational track record of over a decade. The ratings also take into consideration the healthy growth trend in NMCTH's hospital income (~37% growth in the last three years), which has compensated for the low growth in income from the medical college (~7%), thereby supporting the overall revenue growth (~19%). Growth in the company's hospital segment has been supported by its improving market position, which has resulted in a consistent increase in patient flow as well as revenue metrics (per bed day inpatient revenues) over the past three years. The rating action is also supported by the healthy intake level across all major courses in NMCTH's medical college, supported by the favourable demand-supply scenario for medical education in Nepal.

The ratings are, however, constrained by the uncertain operating environment for medical colleges in Nepal with reduced fees as well as lowered seat allocation for the MBBS course, which has been historically the major contributor to medical college revenues (~80%). ICRA Nepal also takes note of NMCTH's sizeable capex plans for facilities upgradation in the hospital, in order to position it as a super specialty hospital. While the said capex augurs well for the hospital's revenue growth prospects over the medium term, reliance on debt for part funding of the capex is expected to result in increased leveraging and moderation in company's coverage indicators from the current levels (gearing of 2.1x as of mid-July 2018 with interest cover of ~6x and DSCR of 2.9x in FY2018). Further, NMCTH has financed some of the capex from short-term sources in the past, which has led to the piling up of payables at times, leading to a weak current ratio (0.21x as of mid-July 2018). Overall regulatory risks are also significant, as inherent in the medical education sector, including stringent compliance requirements and limited flexibility in fee determination. This would remain a key monitorable. Going forward, NMCTH's ability to attain healthy revenue growth from the hospital while maintaining healthy margins and lower the working capital mismatch will remain a key rating sensitivity.

Key rating drivers

Credit strengths

Experienced promoters/management team and established operational track record – Incorporated in 2003, NMCTH started enrolling students in the MBBS course from August 2007. With increasing track record and an experienced promoters/management team, NMCTH has improved its market position over the years. The key promoters are from medical backgrounds themselves and have been managing the company's operations over the years, which is a source of comfort.

Healthy income growth from hospital operations supported by increasing patient flow and fee revisions – NMCTH was able to post healthy sales growth during FY2016 to FY2018 (CAGR of 19%). This was primarily supported by growth in hospital income (~37%) while the medical college reported low income growth (~7%) amid regulatory reduction in fees and seat allocation for the MBBS course. With higher growth, hospital income comprised of ~50% of overall revenues in FY2018 against ~30% in FY2016. The growth in hospital income was backed by increasing patient flow with CAGR ~12% and ~18% growth in OPD and IPD (outpatient and inpatient department) patients, respectively during the last three years. The occupancy of the hospital has also remained healthy at ~70%. At the same time, the revenue per patient has increased at a healthy pace (CAGR ~38% for OPD and ~57% for IPD during FY2016-FY2018) with regular fee revisions, in line with market trends. Within the hospital income, NMCTH garners stable rental income by leasing out the hospital premises to pharmacies and diagnostic centres. This provides additional comfort. The company has further reported significant hospital revenue growth in H1 FY2019 (~36% annualised growth). The sustainability of the same would remain a key monitorable.

Full enrolment across all major courses – Given the healthy demand outlook for medical education in Nepal, NMCTH has been able to report full enrolment for all major courses, excluding BDS which generally witnesses lower enrolment. The MBBS course is the key revenue driver, accounting for ~80% of medical college income. This has consistently reported 100% enrolment. Further, NMCTH's brand positioning has been improving, given the increasing patient flow which implies better practical exposure for its students. This remains a positive for the enrolment outlook over the medium term.

Positive demand outlook for medical education and healthcare services in Nepal – Demand for healthcare services is likely to improve in Nepal on the back of rising healthcare awareness, growing population and increasing penetration of medical insurance. This, in turn, will boost demand for medical education as well as health-care services.

Credit challenges

Uncertain regulatory/operating environment for medical education in Nepal – Regulatory risks are significant for medical education in Nepal with limited flexibility in determining the fees as well as uncertainty in YoY seat allocation for the MBBS course. While 10% of the seats in the MBBS course are allocated to scholarships, fees for the national seat quota (50%), which are determined by Kathmandu University, have witnessed a reduction in recent years. The company has flexibility in determining the fees for the foreign seat quota (40%), which has witnessed a healthy growth rate (~11% in AY 2018-19), thereby providing some respite. However, the seat allocation for private medical colleges has gradually reduced over the years (to 100 seats for AY 2017-18 for NMCTH from 150 for AY 2014-15). Any further reduction in seat allocation would impact the company's revenue stream and financial profile.

Sizeable capex plans likely to pressurise debt coverage and profitability indicators – NMCTH has plans for high investment in capex, over the medium term, to maintain and expand its infrastructure facilities, which would increase its debt levels. Though the current healthy operating margins (~30% in FY2018) and low debt mix result in comfortable coverage indicators (gearing of 2.1x as of mid-July 2018 and interest cover of ~6x in FY2018), any moderation in margins would pressurise these indicators, given the rising debt levels to fund a part of the proposed capex. Moreover, considering the sizeable employee and administrative expenses (~39% and ~27%, respectively, of operating income in FY2018), regular increments on these fronts could impact profitability significantly. Incremental depreciation and interest charges related to the capex are also expected to impact the company's net margins (7.2% in FY2018). Further, rising interest rates will have a bearing on net profitability.

Weak current ratio – In the past, the company has funded a part of the incremental capex from short-term funds including advance fees from students. While the yearly net cash accruals were inadequate to support the incremental capex, fresh term loans were not raised for the same. This led to the piling up of short-term liabilities, including sizeable salary dues at times. As a result, the company's current ratio was weak at 0.21x as of mid-July 2018. NMCTH's ability to implement judicious working capital practices and reduce the funding mismatch would remain a key monitorable, going forward.

Risk of cash flow mismatch – The fees for various courses are collected in advance and as the collected funds have been utilised towards capex in the past, this may lead to short-term liquidity mismatches. The lumpiness in cash flows against the periodic repayment obligations necessitates prudent cash-flow management to ensure regular debt servicing. However, sizeable working capital limits have been sanctioned for the company, which provides some comfort.

Analytical approach: For arriving at the ratings, ICRA Nepal has applied its rating methodology as indicated below**.**

Links to applicable criteria:
[Corporate Credit Rating Methodology]

About the company

Nobel Medical College Teaching Hospital Private Limited (NMCTH) was established in 2003 with the objective of running a private medical college and teaching hospital. The Kanchanbari, Biratnagar-based company is affiliated to Kathmandu University for medical and allied health sciences, and the Council for Technical Education and Vocational Training (CTEVT) for the paramedical courses. NMCTH offers courses such as MBBS, PG, BDS, B.Sc. Nursing, BNS and paramedical courses like staff nurse, dental hygiene, lab technician, radiography and pharmacy. In the last academic year, 351 students had enrolled for various courses.

Key financial indicators

	FY2016 (Audited)	FY2017 (Audited)	FY2018 (Audited)	H1 FY2019 (Provisional)
Operating income (OI; NPR million)	1,070	1,341	1,690	797
OPBDITA/OI (%)	22%	27%	30%	42%
Total debt/Tangible net-worth (TNW; times)	3.4	2.1	2.1	1.5
Total outside liabilities/ TNW (times)	9.8	6.4	5.7	4.2
Total debt/OPBDITA (times)	2.5	1.7	1.7	1.3
Interest coverage (times)	4.7	6.8	6.2	7.3
DSCR (times)	1.9	3.3	2.9	2.9

Source: Company data

Analyst Contacts:

Mr. Kishor Prasad Bimali (Tel No. +977-1-4419910/20)
kishor@icranepal.com

Mr. Rajib Maharjan (Tel No. +977-1-4419910/20)
rajib@icranepal.com

Relationship Contacts:

Ms. Barsha Shrestha (Tel No. +977-1-4419910/20)
barsha@icranepal.com

About ICRA Nepal Limited:

ICRA Nepal Limited, the first credit rating agency of Nepal, is a subsidiary of ICRA Limited (ICRA) of India. It was licensed by the Securities Board of Nepal (SEBON) on October 3, 2012. ICRA Nepal is supported by ICRA Limited through a technical support services agreement, which envisages ICRA helping ICRA Nepal in areas such as rating process and methodologies, analytical software, research, training, and technical and analytical skill augmentation.

Our parent company, ICRA Limited, was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment information and credit rating agency. Today, ICRA and its subsidiaries together form the ICRA Group of Companies. The international credit rating agency, Moody's Investors Service, is ICRA's largest shareholder.

For more information, visit www.icranepal.com

ICRA Nepal Limited,
Sunrise Bizz Park, 6th Floor, Dillibazar, Kathmandu-33, Nepal
Phone:+977 1 4419910/20
Email: info@icranepal.com
Web: www.icranepal.com