



Dr. Lal PathLabs Limited (LPL)
Q3 & 9M FY19 Earnings Conference Call Transcript
February 08, 2019

Call Duration	▪ 1 hour 4 minutes
Management Speakers	<ul style="list-style-type: none">▪ (Hony) Brig. Dr. Arvind Lal – Chairman & Managing Director▪ Dr. Om Prakash Manchanda - Whole-time Director and CEO▪ Mr. Ved Prakash Goel – CFO▪ Mr. Bharath Uppiliappan - Chief Executive Officer (India Business)▪ Mr. Rajat Kalra - Company Secretary & Head of Investor Relations
Participants who asked questions	<ul style="list-style-type: none">▪ Anirudha Bhandari from Sixteenth Street Capital▪ Chandramouli Muthiah from Goldman Sachs▪ Dheeresh Pathak from Goldman Sachs Asset Management▪ Dr. Harith Ahamed from Spark Capital▪ Manoj Garg of White Oak Capital▪ Nitin Agarwal of IDFC Securities▪ Prakash Kapadia from Anived Portfolio Management▪ Pritesh Chheda of Lucky Investment Managers▪ Raghuvveer Singh - Individual Investor▪ Sameer Baisiwala from Morgan Stanley▪ Shivam Gupta of CWC Advisors

Moderator: Ladies and Gentlemen, Good Day and Welcome to the Dr. Lal PathLabs Q3 & Nine Months FY19 Earnings Conference Call. As a reminder, all participant lines will be in the listen-only mode and there will be an opportunity for you to ask questions after the presentation concludes. Should you need assistance during the conference call, please signal an operator by pressing "*" and then '0' on your touchtone phone. Please note that this conference is being recorded. I now hand the conference over to Mr. Nishid Solanki from CDR India. Thank you and over to you Sir.

Nishid Solanki: Thank you. Good evening, everyone and very warm welcome to Dr. Lal PathLabs Q3 FY19 Earnings Conference Call. Joining us today are (Hony) Brig. (Hony) Brig. Dr. Arvind Lal -- Chairman and Managing Director of the Company; Dr. Om Prakash Manchanda -- Wholetime Director and CEO; Mr. Ved Prakash Goel -- CFO; We also have with us Mr. Bharath Uppiliappan -- CEO (India Business) and Mr. Rajat Kalra --Company Secretary & Head of Investor Relations.

I would like to highlight that some of the statements made on the conference call today could be forward-looking in nature. Results may vary significantly from these statements. A detailed disclosure in this regard is available in the 'Results Presentation' which was circulated to you earlier. I would now like to request Dr. Lal to share his perspectives with you. Thank you and over to you, Sir.

(Hony) Brig. Dr. Arvind Lal: Good evening, everyone. I am delighted to address you all on our Q3 FY19 results. In my address today, I would like to share with you my thoughts on the journey ahead, as we prepare to scale new horizons and capitalize on the upcoming opportunities in the diagnostics sector.

Our business growth momentum continues to be driven by robust patients and sample volume growth. Our hub-and-spoke model continues to strengthen our network with non-linear increase in Capex. Given the state of the available opportunity we are yet to reach out to many more patients in times to come.

During the quarter, we have introduced high end tests for two more disease conditions under the brand name 'Neuropro' which is mitochondrial mutation detection Panel and MELAS mutation detection and 'Oncopro', that is BRCA1 and BRCA2 mutation drug profiling and the Alpha Thalassemia, MPN extended profile and others. We have also received good response to our marketing campaign around Diabetes which was run during this quarter.

The Kolkata reference laboratory has become central to our operations in the East region now. It now supports a wide variety of tests. Our focus has been on building volumes across regions to grow business.

As I have frequently mentioned, the cornerstone of our service philosophy is high quality affordable services to patients with improved accessibility and time-bound diagnostic services. We thank our customers, patients, investors and other stakeholders for their continued support and faith in our services.

With that, I would like to hand over to Om to share his thoughts and update on the operational performance.

Dr. Om P Manchanda:

Thank you, Dr. Lal. I would like to give a backdrop before I share the highlights for this quarter.

- Usually, festivals are spread between September and October months; however, this year festivals were in the month of October and November. Therefore, last year corresponding Q3 had higher base.
- Secondly, relatively December experienced much lower temperatures than usual in Northern part of India.

With this backdrop, I am pleased to inform you that our revenue for Q3 improved by 11.3% to Rs.292.5 crore. We continue to experience higher volume-led growth both in terms of patients and samples. The volume growth for Q3 FY19 is at 12.1% and sample growth for Q3 FY19 is at 17.3%.

The seasonal sluggishness in the business which is usually seen on account of festivals was experienced largely in Q3 FY19 as against being spread over both Q2 and Q3 in FY18. This has contributed to slightly lower than expected growth in this quarter.

Our revenue growth for nine months ended 31st December 2018 stands at 14.2% driven by patient growth of 16.3% and sample growth of 21.2%. We are not only strengthening our network footprint by adding new collection centers, but we are also helping the existing centers to grow in size and scale. This is contributing towards healthy volume run rate.

We continue to see good progress on our Preventive healthcare bundled test packages under the brand name 'Swasth Fit'. This is gaining further momentum and hence has helped us to increase our samples per patient from 2.28 in Q3 FY18 to 2.38 in Q3 FY19. The contribution from Swasth Fit brand has gone up from 10% in Q3 last year to 12% of revenue in Q3 this year. YTD contribution of Swasth Fit is now at 13% of the total revenue.

With the menu covering the entire range from basic tests to more high end tests, the Kolkata Reference Lab is geared to meet the need of the Eastern region.

We are able to maintain our EBITDA margins despite no price increase for the last two and a half years. This has been possible due to renewed focus on cost optimization and productivity enhancements. Ved will share more details on this aspect later.

In the coming quarters, we plan to intensify our focus on the individual segments of our business based on patients, channels and disease conditions. This coupled with further deepening of our network footprint through additional franchisee collection centers would help us to drive the growth momentum as we move ahead. The Kolkata Reference lab will also build scale with time. As we look to drive natural growth in diagnostics healthcare services, the intent is also to tighten operational efficiencies and productivities in order to deliver consistent returns.

With that I come to the conclusion of my opening remarks and would request Ved to give an update on the "Financial Performance."

Ved P Goel:

Thank you, Om. Good evening once again and thank you for your participation on this call. I will now run you through the important financial highlights.

The underlying patient volume for Q3 FY19 stood at 4.28 million as compared to 3.82 million in the same period last year, representing a growth of 12.1%. Samples per patient have also increased to 2.38 in Q3 FY19 from 2.28 in the same period last year. Revenue realization per patient for Q3 FY19 is at Rs.683 which is marginally lower as against Rs.688 for Q3 FY18.

Normalized EBITDA after eliminating the impact of stock-based compensation and CSR expenses in Q3 FY19 stood at Rs.706 million as compared to Rs.607 million reported in Q3 FY18, representing a growth of 16.3%. Normalized EBITDA margin for Q3 FY19 stood at 24.1% versus 23.1% in Q3FY18. YTD normalized EBITDA margin stood at 26.6% versus 26.5% last year same period. Other income comprises of interest and dividend on investments for Q3 FY19 is at Rs.122 million versus Rs.71 million in Q3 FY18.

PBT came in at Rs.679 million in Q3 FY19 versus Rs.555 million in the same period of previous year, a growth of 22.3%. This is higher than EBITDA growth due to higher contribution from other income. PAT grew by 27% to Rs.461 million in Q3 FY19 as compared to Rs.363 million in Q3 of last year. EPS for Q3 FY19 is Rs.5.56 Vs Rs.4.39 in the same quarter last year. Cash and liquid funds at the end of Q3 FY19 stood at Rs.6,537 million.

As explained by Om, we have maintained our margins by doing effective cost management where we have renegotiated some rental cost and enhanced productivity for better utilization of our existing infra. We are continuously looking at opportunities to optimize our cost further.

I would like to update that the merger of our wholly-owned subsidiary, Delta Ria and Pathology Private Limited has been approved by NCLT during Q3 FY19 with an appointed date of 1st April 2017. Accordingly, the results for the respective quarter and year-to-date have been restated to give effect of this merger. This re-statement does not have a significant impact on the results for Q3 FY19 and YTD Q3 FY19.

That brings me to the conclusion of my opening remarks and I would now invite the moderator to open the forum for Question-and-Answer. Thank you.

Moderator:

Thank you very much, sir. Ladies and Gentlemen, we will now begin the question-and-answer session. The first question is from the line of Prakash Kapadia of Anived PMS.

Prakash Kapadia:

Recently, we have stepped up the noise on Diabetes with some check-ups, weight loss programs. So how does it work and is this value-added service to create differentiation and stickiness for clients, are you targeting existing customers, can you throw some light on that?

Bharath Uppiliappan:

Like in the opening notes, Om had mentioned that we are looking at various segments and the NCD portfolio which is non-communicable disease is a very big component of our growth strategy and the program which we had launched is called "Sugar and Me". It was trialed two quarters back and we are now scaling this program up. This program offers our patients opportunity to get not only some test but also some consultation services along. So it is definitely a value added service and we see the scaling up in the near future as well.

- Prakash Kapadia:** We have tied up with enough of support in terms of doctors, experts, dieticians, what is the process there?
- Bharath Uppiliappan:** We do have a panel of doctors and dieticians who have empanelled with us. So this will be scaled up in a manner which can support the traffic growth as well. So we are very mindful of the service quality and the experience of the patients.
- Prakash Kapadia:** This is currently North India or ...?
- Bharath Uppiliappan:** It is predominantly in NCR which is where this campaign is running, given our strong base in NCR.
- Prakash Kapadia:** On Kolkata and the Eastern region, what would be the hospital reach, what is the potential, how much of inroads have we made and can you give us some insight in our go-to-strategy for that region, because initially we were targeting getting into the hospitals, building awareness and then focusing on the B2C parts, so where are we and what is happening in Kolkata and Eastern region?
- Bharath Uppiliappan:** Eastern region is a very important geography for our growth. Like Om talked about the Kolkata reference lab maturing, so we started operating this lab from January, February onwards, but started to commercially move in around April-May, we went into the market around August. Since August, we have been doing lot of one-to-one meetings, small group meetings with key influencers in this business and we have made good inroads across Kolkata city as well as the up-country geographies of West Bengal. We are seeing momentum build-up but it will be in a gradual fashion, it will not be instantaneous overnight but we are seeing very-very positive traction, led by the fact that the Kolkata reference lab has facilities which are first time introduced in India; accessible at very shorter timeframes and going to other large medical hub. So we have almost doubled the test menu at our reference lab in KRL and that is yielding good results. So yes, the journey into the eastern region continues. I will not quantify number how many hospitals we will reach at this stage, but yes, it is gaining traction every day.
- Dr. Om P Manchanda:** Just to add to what Bharath said, our promotion strategy in East will always be to reach out to lot of these institutional clients and more B2B business because that is where our strength would lie, where our test menu is very wide and we can provide quality service to these people. So we have done lot of activities where one-on-one contract has been established with these clients.
- Prakash Kapadia:** I was in Sitargunj recently and the feedback there was very-very positive from our center. I think last call Bharath and you did mention about potential in smaller towns of North. So the same feedback is from Varanasi. So what I was trying to understand here is can some of the smaller centers and places de risk from our NCR dominance and where are we in that journey because if the network kicks off into some of the smaller places, then North volumes can also grow substantially.
- Dr. Om P Manchanda:** I think you are making a very good point. In fact, since I have been here for some many years, I have seen journey from NCR dependence from 90% to 43% now. So gradually we are reducing our dependence and I think the observation that you made is also very appropriate, that deepening our presence in strong markets is always better than trying to widen in weaker markets. That is what we have always articulated in our strategy of cluster approach while sometimes it sounds that our dependence is very high in North, but North is a very large geography, it is something like 6, 7 states and now

North and East put together is virtually half of the country. So, we believe that deepening our presence in these markets will always help and that is where the Tier-2, Tier-3 towns and that is also precisely the reason why we went to East with the Central lab because then we can deepen in that geography with times to come. So as Bharath mentioned, it is a very gradual process, you do not see needle very sharply moving QoQ but I think over a longer period one will see definitely a difference.

Moderator: Thank you. The next question is from the line of Anirudha Bhandari from Sixteenth Street Capital.

Anirudha Bhandari: Congratulations on good Q3 numbers. I wanted to know a general perspective on how the competition is shaping up because recently there were many private equity funded players with regional labs. So can you throw some light on that?

Dr. Om P Manchanda: We have discussed this particular question many times on investors call. As I mentioned, relatively what we used to see kind of competition in 2016 has definitely tapered off. But overall pressure on top line growth I think everybody is facing this, I see that even smaller labs are also facing it. That primarily is coming because of value driven growth rather than volume driven growth. I actually would say it is a status quo and generally it is a highly fragmented space, the market leader only enjoys about 4-5% market share. So you can understand the hyper intensity in terms of competition. There are small, small labs, everybody is trying to jostle for the same space. So to that extent competition remains but I think from PE-funded, I really would not say that it is much because I have not seen too many PE transactions in the last couple of years. So it has been a bit of status quo as it used to be about a year back.

Anirudha Bhandari: Also wanted to know going ahead, how is the industry shaping up in terms of volumes and in terms of revenue growth?

Dr. Om P Manchanda: Industry, I think overall if you look at diagnostics it is going to gain further importance in medicine because without diagnostics there is no treatment; 70% of medical diseases depend on that. Secondly, diagnostics industry is not only just going to cater to diagnostics need but also in a progression of disease and deciding line of treatment. So firstly, I believe that diagnostics will continue to grow even probably faster than overall healthcare growth. The only challenge that remains is that as the frequency of testing goes up, price elasticity will also go up. So to that extent I would say pricing pressure will be there but volumes will significantly grow.

Moderator: Thank you. The next question is from the line of Pritesh Chheda of Lucky Investment Managers.

Pritesh Chheda: Sir, in your observation, of fragmented market in your key market areas, what is the extent of unorganized market and what would be your market share? In the nine months of FY19, what would in your opinion, have been the market growth rate and what would be your growth rate?

Dr. Om P Manchanda: Unfortunately, there is no published data that is available which I can quote. It is more an internal estimate I would say. These market shares also vary city-to-city because our base is very high in Delhi-NCR. We did a rough back-of-the-envelope calculation in what our market share could be in this area. I think it is between 20 - 25%. Rest of North, would be close to between 10% to 15% but all India will again drop down to about 4-5%. So, I do not think there is enough data available for me to put a number. But directionally, market share is not

that large for us to say that we are sitting on a saturated sort of situation. So the market opportunity remains for all of us. To your second question, surrogate measure is that there are four, five companies at the top where the numbers are public and we just add it together. I think it is still hovering at around 15 - 16%. I do not have data for smaller players but as I visit the market, I think many of these guys are growing below 10% is the number that I see because they are getting impacted by large players. So, my sense is close to 15%- 16% number would be the market growth.

Pritesh Chheda: Smaller players are growing less than 10%?

Bharath Uppiliappan: Relatively their growth rates are lower than larger players. I think that will be a fair statement to make.

Pritesh Chheda: This rest of North and NCR, at what pace you would have taken market share in the last five, seven years? What is the pace of addition of market share – is it 50 basis points, 25 basis points, is it 100 basis points? I will put it other way, the 10% rest of North market share that you are putting today what this number would have been five years back?

Dr. Om P Manchanda: I do not know what probably you are trying to get at. Let me give you a one data point. For Delhi NCR business about 13 - 14-years back was about Rs.35-40 crore range. Today it is about Rs.400-450 crore. So technically 10x we have seen a number growth in the last 12-13 years. That gives you a trajectory for the region. For the rest of North, that number would look very high, maybe not a representative figure. But Delhi NCR because it is a large market, we were also market leader at that time, that give you some sense of how the trajectory has been.

Pritesh Chheda: This expansion pace continues, the market share gaining continues in Delhi or we have kind of stagnated at one-fourth of the market for a few years now?

Dr. Om P Manchanda: So that would continue, our expansion strategy is basically, we grow our business either B2C or B2B. B2C growth comes through in the early part of our growth phase. It came by opening lot of labs. With time our focus has shifted to franchisee collection centers, so that would continue. So more and more as the areas grow, new areas keep coming up. So we will keep opening our collection centers. It is not that there is no room for further growth. So collection center expansion will keep happening, and good news about CC network is that it does not have any fixed cost, it is all variable cost. At the same time we will continue to look for new markets like Eastern Region, Central India, M.P., Rajasthan or Chhattisgarh, some of these markets will keep seeding. So these are future markets for us. So the expansion program in terms of reaching out to institutional clients as well as collection centers is ongoing process, it will continue.

Pritesh Chheda: In rest of North, what would you call as your 'strength markets' and what you call as your 'white space', what would it be in terms of states?

Bharath Uppiliappan: Within the North, there are very small districts where we would not be present with our own infrastructure but predominantly in all of North India I can say with reasonable confidence that we would have a presence.

Pritesh Chheda: Last question is on technology disruption side. So anything which is brewing in the industry which could disrupt the way diagnostics has been delivered or being done?

Dr. Om P Manchanda: There are two areas where I can see a disruption on the technology side. The disruption which can have significant impact the way this industry would look like in future: #1 is moving away from biochemistry-based tests to genetic based test or DNA based test, this is genomics. But that is according to me and technical experts; it is a slow process. But it is good for medicine because ultimate objective in diagnostics is you want to diagnose it early and accurately. If you diagnose that through genetic route, probably you can diagnose it much earlier than through biochemistry route. But if you try to chase to diagnose something early, you are also moving into grey zone because you need to be also very specific that whether you have a problem or not. So that is one area on technology.

The other area on technology is that today some of the centralized models exist because sample moves from point of collection to point of testing. There can be a point of care testing where the testing actually happens near to patients which is the term used in our industry is called "Point of Care Testing." That would be another disruption. But what one has seen there is that the cost and again a little bit of quality aspect becomes a compromise. I think with time, quality has started improving in POCT, cost in Indian context is still prohibited factor. So let us see how it goes. So these are the only two areas.

Pritesh Chheda: In that second area, which is 'point of collection' to 'point of testing', there is an emerging technology where at the point of collection itself, you can test based on the (AI) Artificial Intelligence mapping of past sample. So you need not send it to a testing center and no reagents are used. This is one model where I think the Indian regulator has approved that form of testing. So any thoughts there?

(Hony) Brig. Dr. Arvind Lal: We think it is too hypothetical right now. We have not seen even what is practiced in western countries what we normally call as point of care testing for a simple reason that it is very-very expensive. So we are waiting for some kind of technological breakthrough, you remember we heard about 'lab on a chip' and so many other things, etc., and artificial intelligence is a part of it. But the real technology of testing has not been cracked yet as far as POC is concerned.

Pritesh Chheda: So here some equipment has come which is really cheap and it tends to just collect the sample, scans it, sends it to the Central wherever lab via wifi or internet and it is reviewed and compared with the history of samples or whatever?

(Hony) Brig. Dr. Arvind Lal: Why don't you share your contact details with us? We will reach out to you and study this.

Pritesh Chheda: I will send it across. But you have not heard anything of?

Dr. Om P Manchanda: No-no, let me also tell you, we keep hearing about lot of these start-ups are coming in this kind of field. Many of these instruments I have seen, first of all there is no scope of testing, they only test one or two, they will test maybe haemoglobin or they will test maybe sugar, but the patient is looking for let us say 8-10 tests in one-go. So what tends to happen is that you are doing only one or two tests but other tests you still have to go to lab. Like this example of glucometer where you can test glucose, is nothing but a point of care test. But even there also the medical professional will tell the patient saying that once in a while you also must get it tested from a lab as well just to be sure that your results are right. Similarly, all of us have blood pressure monitor at home, but then again once in a week, once in two weeks I will still go to hospital and check whether my BP what I am checking at home is correct or not. So some

of these things are there. So let us see how it goes. But it will be useful if you connect with us with the gentleman.

Moderator: Thank you. The next question is from the line of Manoj Garg of White Oak Capital.

Manoj Garg: Om, you have indicated that the intensity of PE fund has come down than what it used to be maybe a couple of years ago, but at the same time the growth of the standalone mom & pop labs has also come down, they are growing slower than the industry growth or maybe the larger peers. How do you see the consolidation in the industry going forward given that obviously the complexity of the testing is going to increase as we move forward?

Dr. Om P Manchanda: I have studied western models quite a bit. If I were to maybe share my learning from that model I will try and give you some perspective that may help you as to how I feel the industry would grow in future. Industry in any case in western world is also highly fragmented. In relative terms, they are more organized than us but let us say 25-years back they were also what we are. Then a phase came and the market became very insurance-led there and that started putting pressure on the pricing and indirectly started putting pressure on the profitability, and most people used to say that it is going to become very-very difficult for many companies to survive. But then came a very important phase for the industry which was the consolidation phase.

It goes back to the point that which I made earlier to a question that deepening your presence in strong market is a better idea than widening your presence in weaker market. So many companies started chasing growth in weaker markets by widening their presence. But they soon realize it is a good idea to consolidate and come together rather than do it yourself. So, many of the large companies that we see today in the world they are product of consolidation move. I think as the growth rate slows down, industry goes through a phase of protecting their margins. I am very sure that time will come when the consolidation has to happen. So to my mind, next two to three years, every company will fight it out to make sure that they stay efficient, protect the margins, stay competitive which is a good sign for the industry, good sign for the patients, for everybody else, I do believe that time will come for consolidation, I do not know whether it is three years, four years but I do see that should happen. And consolidation is not bad because if you look at over last 10-years, we have actually seen average test per price has gone down if you correct it for inflation. Our average price increase has not been more than say 1.5% at a portfolio level while the inflation is much higher. It is a very good example where competitive forces are ensuring that all stakeholders are benefiting out of this; patient is getting benefit because it is becoming affordable with better quality. We have seen a huge shift in the last 15-years where we have brought in lot of new tests, accessibility has gone up because collection center model, hub-and-spoke model has actually made now test available every nook and corner of this country. I believe that the consolidation phase should come. It is anybody's guess whether it is immediate or two, three years from now.

(Hony) Brig. Dr. Arvind Lal: I would like to add that in view of the large number of unorganized labs in India, more than 100,000, I am speaking from a quality point of view, only 1,000 labs are accredited by NABL. So the rest of the labs, etc., they have to fall in line for which some kind of a government regulation or something has to come in like the clinical establishment act. So this is the gray area and once this kind of a regulation comes in, after a few years the quality accreditation kind of things will kick in. So it is a very long procedure here. So we have to wait because right now the Supreme Court says that the report has to be

signed by a pathologist, somebody says that you put a pathologist even in a collection centre, as collection center have to be accredited. So there is a gray area right now but all of this will fall into place gradually.

Manoj Garg: Second, again, you said that it is a good idea to strengthen the position obviously when one is very strong and as you indicated that you are pretty strong in North and East, I think probably two, three years ago we also had a plan to spread our wings on the central part of the country, the Central India so-called Hindi belt of UP, MP and particular Bihar areas. So what is your plan out there and do we have any plan in terms of strengthening our franchise in that pocket because I do not see any large player out there who claims a very strong position in the Central area?

Bharath Uppiliappan: In fact, UP, Bihar, Jharkhand, Odisha, MP, Chhattisgarh is a very important market for us. We are making significant investment in improving our presence over there by putting up infrastructure. We are trying to cover up most of the geographies through a hub-and-spoke model once again. So there is a lot of focus on these markets which you mentioned and our growth rates here are very robust as well.

Dr. Om P Manchanda: Actually when we say North, we mean these states also, actually the right word would be all the Hindi belt area, so we are there in all these parts.

(Hony) Brig. Dr. Arvind Lal: The right word would be North, Central and East, the full arc going from North of India right across to the East, covering significant areas of Madhya Pradesh above Vindhya's.

Dr. Om P Manchanda: Madhya Pradesh, Chhattisgarh, even these markets are important markets for us.

Manoj Garg: Recently the ICMR has come with the draft guidelines on essential diagnostics list. Just would like to pick your mind is it a precursor to some kind of price control by the government?

(Hony) Brig. Dr. Arvind Lal: That is what they are not saying. They are saying it is just to ensure that these kind of basic tests are available at a basic level. They have pointedly said that this has got nothing to do with price control; however, in the same breath they say that, they stand for affordable pricing of all the tests. So I think what remains to be seen is some clarity on this. The NEDL is coming and we have already given our remarks to the various bodies, but let us see as it is too much at the inception right now.

Moderator: Thank you. The next question is from the line of Nitin Agarwal of IDFC Securities.

Nitin Agarwal: Om, on the business, given the fact that our realization per patients have been reasonably flattish over the last several quarters, two questions – One is a) if that is the trend that is going to follow and probably would be good to know your sense on do you see a situation where you probably see an inflationary situation as far as realizations per patient is concerned? Then our growth would largely be a function of our patient volumes and we have not seen a situation where the patient volumes have been growing at more than 15% for example over the last several quarters on a consistent way. So how should one look at when we take three year view on organic growth basis on a top line?

Dr. Om P Manchanda: First of all, the way you look at model for us, volume growth fluctuates very high depending on how the dengue season goes. I think that becomes little challenging for us to communicate because in dengue season one patient ends up giving multiple tests in a week's time and this volume is not a unique patient, actually if the patient visits 10x in a week, then it becomes 10 patients.

So in particular year when the volume growth is very high one can safely assume that there is some sort of seasonal fever that has come in especially if it is dengue, then the volume growth will be high. Second thing is for last 2.5-years, we have not taken a price increase, consciously wanting to drive volume growth and with the launch of bundled test, I think this whole revenue per patient has been a mix of many variables. So we have tried to decompose this entire revenue per patient idea because bundled packages like Swasth has taken this up but in some places we have rationalized our prices, that has brought it down, contribution of business from outside Delhi NCR has been moving up, that also is bringing it down because our realization per patient in rest of India versus Delhi NCR is quite different, mix of test also has affected this, there is one test which used to sell close to Rs.8,000 - 9,000, HCV which is now down to Rs.2,000, that also has impacted revenue per patient. I think during this last 1.5-2-years we have gone through lot of churn on this. My sense is we have tried to make sure that our EBITDA margins remain intact. Second thing is also B2C versus B2B mix itself is also going through a change. So I know it is a little bit of dynamic figure. When we sit down one-on-one and maybe offline I can tell you as to how to look at this entire revenue per patient because it is too detailed conversations to have this on the phone call.

Nitin Agarwal: My point is, if this is the broad construct of organic growth, at what stage does the inorganic growth become imperative for you to drive up the business, in your strategy where is inorganic growth, how much of imperative it is...?

Dr. Om P Manchanda: Understood, I think inorganic growth basically fits in for me to grow into new markets. I feel we have to perfect the model of growing the business organically because after I acquire, I still have to grow the business, right. To my mind, there are white spaces where it may be very expensive for us to go right from day zero, it may be a good idea for us to go and see inorganic in those markets. That is where the imperative for inorganic growth lies.

Nitin Agarwal: But when you look at the landscape, do you see opportunities for reasonably sized chains in some of the white spaces that you probably have in mind?

Dr. Om P Manchanda: We do see at city level, may not be at regional level because there are not too many large players because scaling is not that easy in this business because most companies have struggled to scale beyond the city. So there are city based players, even some of these PE funded players we talk, they actually have found it very difficult to grow beyond a large city. We do see those players but also as we have always stated that quality is very-very important for us, we do not want to do any inorganic growth just for the sake of doing it, we want to make sure that governance issues, quality issues, all are in place and efforts are on always to do something on that side.

Nitin Agarwal: Just to push the thing a little further, what has your experience been on transaction multiples that probably are in offer in some of these transactions over the last six months—have they gone up, have they rationalized a bit?

Dr. Om P Manchanda: Actually to be very honest, the last three years there were not too many transactions that have taken place, actually most transactions took place during the period when two companies in this space went public. I have not

seen any PE transaction since 2017. So I do not have any benchmark to say that these are the multiples which are going. Surprisingly, not too many M&A deals also have happened, lot of discussions are going on, but nothing much has happened on that aspect. I guess the challenge is everybody is expecting the listed players' multiple which is difficult for either PE guys to give or anybody else to give. So to that extent, there are no transactions as of now.

Moderator: Thank you. The next question is from the line of Dr. Harith Ahamed of Spark Capital.

Dr. Harith Ahamed : Since we are almost close to end of the year, can you give a sense of the metro expansion that you have done during the year, number of collection centers, at least a rough figure if it is in line with what you have done last year?

Bharath Uppiliappan: At very broad level, network expansion plans are on target. We continue to grow our collection center network across our strong markets of North and East. So last year in Q4 '17 we had about 1,759 collection centers which has now gone up to about 2,400 plus. So it sees a 15% growth on year-on-year basis. That is what we keep driving to reach new customers and newer cities and towns and geographies.

Dr. Harith Ahamed : My second question is on the revenue per patient which we reported roughly at Rs.680 for the quarter, can you give some directional sense of what this number would be across different channel, the labs, collection centers and pickup points versus the average level of Rs. 680 where it would be above or below for each of these channels?

Bharath Uppiliappan: From a channel perspective, the walk-ins, labs, etc., would be higher, pickup points depending on the type of pickup points because there are some who will give us routine business and then some who will give really high end business specialized test. So it has to be looked at from a segment of the pickup business as well rather than have a broad brush on the pickup points. So very largely you said our walk-in business will be higher ...

Dr. Om P Manchanda: Let us say if the realization per patient in walk-in business is 100, through a collection center it would be about 80 because we give 20% revenue share to our franchisee. For the institutional business, depending on scale, there is a little higher discount, so this can actually go down to about say 70 or 75. But the thing is that I do not want to be misconstrued as if it is like institutional business is less profitable because you also should know that to service the patient through a walk-in in our lab, our costs are also equally high because cost of institutional business is only to the extent of logistics.

Dr. Harith Ahamed : Is it fair to assume that the margin profile of volumes that are coming through each of these channels are broadly not materially different?

Dr. Om P Manchanda: I think one can safely assume that.

Dr. Harith Ahamed : Lastly, currently, you talked about B2B mix being at roughly 60:40, given a lot of growth is coming from the East where there is a lot of focus on the B2B part of the business. Do you see the mix changing materially in the next couple of years?

Dr. Om P Manchanda: I think the mix is changing, what we do it through our lab network is moving towards collection center network, but collection center are technically catering to B2C as well. Since our tracking mechanism of collection center whether it is

B2C for them or B2B for them is not that robust. So to that extent it might be changing plus it does not change overnight so sharply. But directionally our franchisee network is moving up and that is where probably in the P&L you must have seen that fee to collection center has gone up slightly compared to earlier quarters.

Moderator: Thank you. The next question is from the line of Chandramouli Muthiah of Goldman Sachs.

C Muthiah: At the start of the call you had mentioned that there was adverse seasonality effects from the festive season and temperatures in December in the North were low. So just related to that if you could give us what the North India growth was YoY versus what it usually is and what the East India growth was as well?

Dr. Om P Manchanda: So festival affected our November month particularly. So that was a bit of dampener. On East, actually we have not shared the number in the past but just to give you overall YTD growth it is around 20%-odd. That is what I would say on East side. North has two components – one is the Delhi NCR and other one is rest of North, so our rest of North was significantly higher, we just had a bit of dampener in Delhi NCR.

C Muthiah: If I just look at your revenue per sample numbers, the last couple of quarters, you had called out there were some free testing promotion scheme in the east related to Kolkata reference labs, there was about 5-6% decline YoY, this quarter I see it only 2% decline. Is this because some of these promotions are tapering off and coming towards the end of the cycle, could you give us some commentary there please?

Dr. Om P Manchanda: This quarter we had less promotional activity. So that is why the delta is only 1%.

C Muthiah: Can you give us some clarity on what volume split is in same centers volume growth and the new center volume growth, I think your sample growth is about 17% which is some split on same center versus new center, that will be very helpful?

Dr. Om P Manchanda: I think this question does come in every call and we always struggle to answer in that fashion. So I think surrogate measure for us on the same store growth is the same market growth I would say rather than same store because for us it is ecosystem of institutional business, collection center and stores. I think that is the best way to understand this particular figure. If I were to fragment this number of 14.2% is the number for YTD growth as a company, how much would have come from the same market if there was no expansion, that number would be around 9-10% and the balance 4% would have come from through expansion. So I think that is the way we look at it. Otherwise, the way you look at retail business we have always struggled to answer in that fashion. I think I would say that we look at same market growth which is mature or slightly in advanced lifecycle, I would say that growth would be about 9-10%.

C Muthiah: Just last one again on the East. Is it fair to think that you are still targeting reaching 25% and 30% East India growth overtime as KRL gains more momentum?

Dr. Om P Manchanda: I think that is our ambition. I know this current growth rate of 20% that I mentioned is slightly below our expectation. In this industry there are not too many large players. We are the only ones who are creating teams and people

who can manage large scale businesses. So I think gestation period is much longer for us to have the teams in place and train them, mobility is another big issue, we cannot really move talent from one geography to another geography. So it has taken little bit of time for us to stabilize our operations but I am fully confident that the market is very large as the brand grows. In healthcare actually you cannot buy the franchise overnight, it has to go through time and this is what it is. I am pretty hopeful that it will deliver results for us.

Moderator: Thank you. The next question is from the line of Shivam Gupta of CWC Advisors.

Shivam Gupta: Just the two questions. Could you help me understand how do you see the home service trend picking up in diagnostics like what percentage of your revenue will be coming from that and how do you see that going forward over the next few years?

Dr. Om P Manchanda: In our business, there are two components – one is that most labs have this whole B2C idea as a full-service model idea where you actually manage the patient right from the time the patient walks into a lab. Now that has gone to home collection. I believe that full service model is an idea which probably may not be fully scalable idea. So I continue to believe that we will have to partner with franchisee who do lot of collection. So the first mile has to be handled by franchisee. Our real core strength is on quality of testing and accuracy of reports and that is where we will have to really build our model where we work with franchisee collection centers. They manage both the services, whether patients walk into their centers or they do home collection. Role that we have to play is make sure that the collection is done properly, phlebotomists are trained and we continue to have a monitoring mechanism on the entire network. So I think that is the way I would see model evolving for us.

Shivam Gupta: Just to get this clarity right, so effectively you are saying the onus of this thing becoming significant for Dr. Lal operations lies more on the franchisee? You are not like kind of promoting it anyway?

Dr. Om P Manchanda: That is a service aspect of the business but scalability in our model has been building this hub-and-spoke where spokes are collection centers, they are all franchised out. So close to 2,400 centers that Bharath mentioned, most of them are franchisee collection centers. And we have to actually set a mechanism so that we are able to monitor the entire network.

Shivam Gupta: The other question I had was in fact, I did pick up on one of the comments you made that this is the business which is easy to establish but not very easy to scale for the inherent volume-led benefit you do enjoy. Against that how do I read the B2B wins there, some of the aggregators businesses like 1 MG, MedLife who are initially just the aggregator of samples have put up their own labs?

Dr. Om P Manchanda: I think to my mind I do not know how it pans out. Brand experience in this business is not about booking online. Brand experience in this business is all about accuracy of the report. And that to me is dependent on right from how you collect the sample, how you transport the sample, how you test the sample. All these three activities I am not sure if these aggregators are currently doing. The moment we decide to get into this activity they will get into the same trap of how do I scale up. I know online part is easy to scale but to service the customer from a collection till testing is definitely lot of hard work.

- Bharath Uppiliappan:** Just to add on to the point, even at this point of putting up labs, there are two types of labs – lab with the restricted test menu, labs with the full suite test menu. For a patient they would always like to go to a full suite menu lab because then the whole journey of their whole life can be mapped into the lab. That is also very important angle and that would require significant investments to scale up the full suite laboratory menu.
- Shivam Gupta:** In this result, the other expense has just kind of shown almost no growth if I compare YoY. Even on a nine months basis, just 10% growth against very healthy volume growth we are showing. So is there some one-off in this quarter and how to look at this line item going forward?
- Ved Goel:** Yes, you are right, overheads we are maintaining, so lot of cost optimization we have done. Especially the savings are coming on account of 2-3 heads where we have some of the rental agreements we have renegotiated, some savings is coming on account of that plus as Bharath mentioned we are opening more and more collection center and franchisee network where the fees to collection center is going up but other overheads which is fixed overheads in terms of infra cost is coming down. So that is where we are optimizing our cost and that is where we are seeing a saving on account on the total overheads.
- Moderator:** Thank you. The next question is from the line of Raghuveer Singh, an Individual Investor.
- Raghuveer Singh:** I would like to understand what is your strategy for moving into West and South? Currently you are just in North and East.
- Dr. Om P Manchanda:** I think that is a good question. Earlier also we had mentioned there are two ways we are trying to gain entry into West and South -- #1 is focus city approach, we have identified two cities, Pune and Bangalore, primarily because these cities have lot of North Indian population and our attempt is to build critical mass to a scale to something like Rs.40-50 crore. If we can build that and from there then we will grow into the regions. We are some distance away from that number but our focus is on these cities. Second is B2B institutional network which is directly going to the hospital and picking up samples, that exists, it is on a consumer facing business, that we are doing in any case in all these markets. Continuing further as we mentioned, inorganic efforts will only continue in these markets so that we get entry into new geography. So, that is how we will approach South and West.
- Raghuveer Singh:** For South and West zones, how much of revenue come from these two zones approximately?
- Dr. Om P Manchanda:** About 15%.
- Moderator:** Thank you. The next question is from the line of Sameer Baisiwala of Morgan Stanley.
- Sameer Baisiwala:** Just thinking about your industry growth rate, you mentioned that in the matured markets and that is the way we should look at, your growth is about 9-10%. So is it then not the industry growth?
- Dr. Om P Manchanda:** I think the question is same store. I am just picking a very-very small geography where if I were to look at a surrogate measure to put that number, but that is not the representative of the entire country, it is just a small pocket where that number is there. But if you look at our rest of India, where our

growth rates are much higher because our average growth rate is 14%, so obviously rest of India we have grown much faster. If I were to do an average, it would be close to 18, 19%, so that is the number I would have. I think the point which was made earlier is that how quickly you can reduce your dependence on DNCR which will help us going forward.

The challenge which is happening is that we do not have any published data on an ongoing basis like in FMCG there is ORG data or in Pharma you get IMS data, unfortunately in Diagnostics, there is no such data which you track. So we all have to make our internal estimates. So there are two, three ways I can figure that out – one is of course ask my sales team and that you know how it will happen. Second is, I just add up every company's growth rate and see what that number is. So I eagerly wait for everybody's quarterly results and then figure it out as to how it is. If I add that number, somewhere the average is falling between 14, 15%, that is the number I end up quoting here. Third is when I travel the market, I ask lot of these individual players, you get all kinds of figures. So my sense is overall smaller players are not growing that fast as the larger players are. And larger players growth rate is falling in this mid-teens and that is the number which I end up sharing with all of you.

Moderator: Thank you. The next question is from the line of Dheeresh Pathak from Goldman Sachs Asset Management.

Dheeresh Pathak: Is there any test in any region/state which is under price control as of today?

Dr. Om P Manchanda: Not through some regulatory mechanism, but some of these tests like dengue or sometime swine flu at a local level, people, CMOs, etc., these people end up reaching out to private labs. So I do not know whether I can use the term, price control but there is definitely during this epidemic, there is a local government authority's intervention that happens and we tend to oblige because this is also a requirement and as a responsible lab we should come up in the need of this hour. So this is what probably we end up doing.

Dheeresh Pathak: Is it verbal goodwill sort of thing or do they come out with some order?

Dr. Om P Manchanda: There is a written sort of communication that takes place.

Bharath Uppiliappan: But many a times, just to add, Chief Medical Officers request that, the government machinery does not have enough testing capacity or capability at this point of time, so they would request for the patient's interest to say whether can you just do it at the government rates or acceptable rate which they can ...

Dr. Om P Manchanda: But communication also happens between Government medical departments and us.

Dheeresh Pathak: There is a regulatory mechanism through which State governments can regulate prices?

Dr. Om P Manchanda: Yes.

Dheeresh Pathak: But they only do it in these epidemics and if they do it for longer then you will contest it?

Dr. Om P Manchanda: Right now there have been two, three instances. I think it has happened on dengue, it has happened on swine flu, also on chikungunya to a small extent, at least during my time it has happened that way.

- Dheeresh Pathak:** These online aggregators, when they are giving you business, do you give them the B2B price or B2C price?
- Bharath Uppiliappan:** It is not a very big component of our business. So it is negotiated on terms of trade which includes volumes, payment terms and so on. So, with these lead generators or the servicing agents, etc., it is slightly more detailed way of building up the terms of trade with them.
- Dr. Om P Manchanda:** We look at them like any other collection centers or institutional clients. That is the way to look at. If that guy is going to collect the sample, then we will look at as institutional client. If he is expecting us to collect the sample, then we look at him as lead generator only plus as Bharath mentioned the contribution in this business is nothing to write home about, it is very small.
- Moderator:** Thank you. As there are no further questions from the participants, I would now like to hand the floor back to the management for closing comments.
- Dr. Om P Manchanda:** Thank you for joining this call and we will come back to you in the month of May probably for the Annual Meet.
- Moderator:** Thank you. On behalf of Dr. Lal PathLabs, that concludes the conference. Thank you for joining us and you may now disconnect your lines.

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