Gandaki Medical College Teaching Hospital and Research Centre Private Limited: [ICRANP] LBB-/A4 assigned

April 5, 2021

Summary of rated instruments

Instrument	Amount (NPR Million)	Rating Action
Long-term loans: fund based (Term loans)	886	[ICRANP] LBB-; assigned
Short-term loans: fund based (Working capital loan)	135	[ICRANP] A4; assigned
Total	**1,021**	

Rating action

ICRA Nepal has assigned a long-term rating of [ICRANP] LBB- (pronounced ICRA NP L double B minus) to the long-term loans of Gandaki Medical College Teaching Hospital and Research Centre Private Limited (GMC). ICRA Nepal has also assigned a short-term rating of [ICRANP] A4 (pronounced ICRA NP A four) to the company's short-term loans.

Rationale

The rating action factors in the company's established operational track record (since 2010), its adequate scale of operations (~550-bed capacity) and its experienced promoter/management team. The rating also takes note of GMC's steady revenue growth in the recent years (CAGR of 5% in the last three years ending in FY2020), strongly supported by the growth in hospital revenues (CAGR 21% over the same period), despite relatively stagnant growth in medical college revenues. Moreover, ICRA Nepal takes note of the strong student enrolment in MBBS course, which provides comfort on the sustainability of the medical college revenues over the medium term. The company's increased focus and infrastructural upgradation in the hospital segment, have resulted in better per-patient revenue metrices and is likely to support the incremental revenue and profitability outlook. The rating also factors in the company's adequate operating margins and revenues, which translates into adequate debt coverage indicators (interest coverage of 2.9 times and DSCR of 1.3 times in FY2020). Additionally, positive demand outlook for the healthcare industry along with increasing medical insurance coverage and rising awareness for better healthcare, remain positives for GMC.

Nonetheless, the ratings remain constrained by the company's weak capitalisation profile (negative net worth of ~NPR 385 million as of mid-July 2020, excluding the revaluation reserves). GMC has also reported a drop in hospital occupancy in FY2020 and H1 FY2021, primarily due to the impact of Covid-19. This concern is, however, partly mitigated by the increase in average per patient revenue because of improved outpatient and inpatient revenues, leading to overall top-line growth. The company is also exposed to the risks of asset liability and cash flow mismatch as the course fees are collected at the start of the academic year, while the expenses are relatively evenly distributed across the year. The sizeable operational payables have also resulted in a negative net working capital and weak current ratio, which remains a key rating concern. Further, ICRA Nepal notes the intense competition in the fragmented healthcare industry in Nepal. The medical education sector is also exposed to regulatory risks in areas such as fee determination and seat allocation. Going forward, GMC's ability to attain adequate revenue growth while generating healthy margins, improving the capitalisation and lowering the working capital mismatch will remain the key rating sensitivities.

Key rating drivers

Credit strengths

Adequate track record and steady revenue growth – Established in 2007, GMC started its operations from 2010. The company has been running a medical college along with a ~550-bed hospital in the Kaski district and has been able to report annualised revenue growth of 5% from FY2017 to FY2020. GMC's revenues grew by 9% in FY2020 despite operational disturbances caused by Covid-19. While income from the medical college segment was largely stagnant in the last few years, the overall revenue growth was supported by the income from the hospital and the pharmacy segments that contributed ~54% of the total FY2020 revenue (39% in FY2017). The revenues in this segment have grown despite the pandemic-induced decline in hospital occupancy to ~58% in FY2020 from ~66% in FY2019. This can be attributed to addition of advanced/new medical services and facilities, leading to improvement in average revenue per patient.

Improved operating margins and comfortable coverage indicators – With sharp improvements in average revenue per patient, the company's operating margins expanded to ~25% in FY2020 from ~20% in FY2019. Hence, the coverage ratios remain adequate with interest cover at 2.9 times and DSCR at 1.3 times in FY2020, while the total debt/OPBDITA improved to 4.0 times (~5.2 times for FY2019). The company's ability to maintain/improve the revenue trajectory and the coverage indicators, amid increasing term debts alongside capex plans, would remain a key monitorable.

Full enrolment across major courses – Given the healthy demand outlook for medical education in Nepal, GMC has been able to report full enrolment for all major courses, i.e. MBBS and postgraduate (PG) course. Although other paramedical courses like BDS, BSC Nursing and BPH have reported lower enrolment in the recent years, their contribution in overall medical college revenues remain low (~7% for FY2020). MBBS course, the key revenue driver accounting for ~82% of the medical college's income, has consistently reported 100% enrolment. Further, increment of sanctioned seats for PG to 33 in AY[1]2020 against 22 in AY2019 remains a positive for the enrolment outlook over the medium term.

Positive demand outlook for medical education and healthcare services in Nepal – Factors such as better affordability through increasing per capita income and growing medical insurance coverage, rising healthcare awareness, technological improvements in early diagnosis and treatment, and higher incidence of lifestyle diseases support the industry's prospects. This, in turn, will boost demand for medical education as well as healthcare services.

Credit challenges

Weak capitalisation due to negative net worth – In FY2019, the company rectified the major prior-period accounting errors (booking of course fee income on cash basis) through retained earnings. This resulted in a negative net worth of ~NPR 436 million as of mid-July 2019 after the unearned revenues of NPR 731 million were removed from the retained earnings. The net worth (excluding revaluation reserve of NPR 793 million) continues to be negative (negative NPR 385 million as of mid-July 2020) and is expected to remain so over the medium term as the rate of net profit generation remains moderate. The company's ability to gradually recover the accumulated losses and improve the capitalisation would remain critical for its financial profile.

Weak current ratio and risk of asset liability and cash flow mismatches – The company is exposed to risks of cash flow mismatch as the course fees are collected in advance and restricted funds are not created for the same. The company's current ratio (excluding student advances) was weak at 0.28 times as of mid-July 2020. GMC's ability to reduce the funding mismatch would remain a key monitorable.

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 for the national quota as well as uncertainty over the year-on-year (YoY) seat allocation for the MBBS course. Though medical colleges have flexibility in determining the fees for the foreign seat quota, GMC has not enrolled any foreign student till date. This has impacted its margins compared to its competitors. The seat allocation for the company has gradually reduced over the years (95 seats in AY2020 from 110 in AY2017). Any further regulatory changes impacting the seat allocation and fees ceiling would impact the company's revenue stream and financial profile.

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

[1] *Academic Year generally refers to the period from April-May.*

About the company

Gandaki Medical College Teaching Hospital and Research Centre Pvt Ltd (GMC) was established in 2007 A.D in Pokhara and is affiliated to Tribhuvan University – Institute of Medicine (IOM) for medical and allied health sciences. GMC offers courses such as MBBS, BDS, B.Sc. Nursing, BNS, BSc. MIT, BSc. MLT, BPH, B-Pharma programme and postgraduate programmes as well. It had more than 600 students enrolled (in total) in the last academic year.

Key financial indicators

	FY2017 (Audited)	FY2018 (Audited)	FY2019 (Audited)	FY2020 (Audited)
Operating income (OI; NPR million)	846	892	888	970
OPBDITA/OI (%)	31%	28%	20%	25%
Total debt/Tangible net-worth (TNW; times)	2.1	1.7	(2.1)*	(2.5)*
Total outside liabilities/ TNW (times)	2.7	2.3	(4.2)*	(4.7)*
Total debt/OPBDITA (times)	3.9	3.9	5.1	4.0
Interest coverage (times)	3.0	2.8	2.2	2.9
DSCR (times)	2.1	1.8	1.3	1.3
Current ratio (excluding student advances)	1.1	1.2	0.2	0.3

** TNW excludes the revaluation reserves created by revaluation of land in FY2019.*
Source: Company data

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About ICRA Nepal Limited:

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