Lumbini Medical College and Teaching Hospital Limited: Ratings downgraded to [ICRANP] LBB+/A4+

January 09, 2023

Summary of rating action:

Instrument* (Amounts in NPR Million)	Last rated limits	Current rated limits	Rating Action
Long-term loan limits	470	378	**[ICRANP] LBB+**; downgraded from [ICRANP] LBBB
Short-term loan limits	180	231	**[ICRANP] A4+**; downgraded from [ICRANP] A3+
Total	**650**	**608**	

** Instrument details are provided in Annexure-1*

Rating action

ICRA Nepal has downgraded the rating assigned to the long-term loan limits of Lumbini Medical College and Teaching Hospital Limited (LMC or the company) to **[ICRANP] LBB+** (pronounced ICRA NP L double B plus) from [ICRANP] LBBB (pronounced ICRA NP L triple B). ICRA Nepal has also downgraded the company's short-term loan rating to **[ICRANP] A4+** (pronounced ICRA NP A four plus) from [ICRANP] A3+ (pronounced ICRA NP A three plus).

Rationale

The downward revision in ratings mainly factors in the sharp decline in LMC's operating profit margins (OPM) in FY2022, which along with the rising debt levels have led to a steep deterioration in the company's financial and liquidity profile. The decline in OPM was mainly due to reduced share of income from high-margin medical college segment (amid the deferrals in intakes after the outbreak of Covid-19 pandemic) and steadily rising share of revenue under low-margin government-sponsored 'health insurance' segment. The company has also incurred higher than anticipated investments in group companies, including another medical college viz. Devdaha Medical College, which have relatively weaker financial profile. The increased investments, revenue moderation and delayed reimbursement under the 'health insurance' segment have impacted LMC's liquidity profile and increased its reliance on external debt funding. This, along with the rising borrowing rates, have caused significant deterioration in LMC's debt coverage/servicing indicators, which is expected to persist over the medium term. The ratings are also tempered by the restrictive regulatory environment for medical colleges in Nepal with capped fees for the MBBS course, which has historically been the major driver of medical college revenues and profitability.

Nonetheless, the ratings continue to take comfort from LMC's established operational track record (since 2008), its experienced promoter/management team along with the healthy occupancy across all the major courses in the medical college, supported by the favourable demand-supply scenario for medical education in Nepal. The ratings also take positive note of LMC's improving brand position supported by added hospital facilities, thereby resulting in improving per patient revenue metrices, which has partly compensated for the reduced patient flow. Going forward, LMC's ability to improve its margins will have a direct bearing on its liquidity and financial profile and will remain a key rating sensitivity. Continued pressure on margin and liquidity could warrant further rating action.

Key rating drivers

Credit strengths

Experienced promoters/management team and established operational track record – Incorporated in 2005, LMC started enrolling students to the MBBS course from August 2008. With increasing track record over the years along with the presence of experienced promoters/management team, LMC has improved its market position over the years. With year-on-year added facilities and services, LMC has been able to improve its brand image thereby leading to an increased per patient revenue in recent years, which remains a positive amid recovering patient inflows after the pandemic.

Full enrolment across major courses – LMC offers four medical and paramedical courses, viz. MBBS, PG, BSc. Nursing and PCL Nursing. Given the healthy demand outlook for medical education in Nepal, LMC has been able to report good enrolment for these courses. The MBBS course fees is the key revenue driver, accounting for ~80% of the medical college's income and this course has consistently reported 100% enrolment (for 100 seats allocated herein) over the years. The seats sanctioned for PG has also increased to 33 from AY2020-21 onwards from 9 in AY2019-20, which has supported the college income. Further, LMC's brand positioning has been improving, given the sizeable patient flows (notwithstanding post-pandemic decline) which is expected to contribute to good enrolment level and stable hospital revenues, going forward.

Credit challenges

Increased margin pressures – The company's operating profitability remains mainly supported by the medical college segment while the hospital segment offers much lower margins, acting as a support unit for medical college. LMC has been facing a year's college income loss from FY2021 onwards following delayed intake of a batch of students after the pandemic outbreak which has impacted its OPM levels (~11% for FY2022 from ~17% in FY2021 and ~16% in FY2020). LMC has also reported steady increase in revenues pertaining to the Government's health insurance scheme (37% of FY2022 revenues as against 23% in FY2020) which offer lower margins. The company's ability to recoup its margins amid the necessity to continue health insurance scheme remains to be seen.

Stressed liquidity and financial profile – Medical colleges collect fees upfront in three equal instalments in the first three years of studies for MBBS, the major revenue driver and cash inflow source for LMC. However, with the Covid induced yearly delays in admissions, LMC has been losing income related to one batch of students, which has also added to the liquidity stress. This, coupled with delayed recovery of amount under health insurance scheme has further pressurized the company's liquidity profile, thereby leading to a steady increase in utilization of short-term debt in FY2021 and FY2022. This has led to stretched debt coverage indicator with total debt to OPBDITA of ~6.6 times for FY2022 (1.6 times for FY2020) and deteriorated debt servicing indicators (DSCR of 1.1 times, sharply moderating from ~3.1 times in FY2020). Going forward, LMC's ability to maintain a comfortable liquidity profile and debt service/coverage indicators will remain a key rating monitorable/sensitivity.

Increasing investments in group/associate companies – LMC has made higher than anticipated investments in subsidiaries as well as associates, and also acquired ~17% stake in another medical college viz. Devdaha Medical College and Research Institute (Devdaha) located at Rupandehi district. Devdaha is a 400-bed capacity teaching hospital with sanctioned intake of 50 students in MBBS. The acquisition was made by purchasing shares from its existing shareholders at a premium. Moreover, LMC has also injected additional funds in its subsidiary, Lumbini International Hospital (LIH) and a few associate companies with under-construction projects. These units could require additional funding support going forward, which could strain LMC's liquidity profile. LMC has also advanced corporate guarantee for credit facilities availed by LIH, with similar possibility for other entities, which could further stretch its liquidity profile, in case of exigencies at investee companies.

Links to previous rating rationale
Rationale_LMC_Fresh BLR - June 2021

Analytical approach: For arriving at the ratings, ICRA Nepal has considered LMC's consolidated financials and applied its rating methodology as indicated below**.**

Links to applicable criteria:
Corporate Credit Rating Methodology

About the company

Lumbini Medical College and Teaching Hospital Limited (LMC) was established in year 2005. Initially, the college was registered as a private limited company on December 11, 2005, and was converted to public limited company on April 16, 2014. LMC offers medical courses such as MBBS, PCL, BSC and PG in affiliation with Kathmandu University and Council for Technical and Vocational Training (CTEVT).

Key financial indicators

	FY2019 (Audited)	FY2020 (Audited)	FY2021 (Audited)	FY2022 (Provisional)
Operating income (OI; NPR million)	1,346	1,540	1,411	1,570
OPBDITA/OI (%)	22%	16%	17%	11%
Total debt/Tangible net worth (TNW; times)	0.55	0.60	1.50	1.57
Total outside liabilities/ TNW (times)	2.30	2.27	2.89	3.15
Total debt/OPBDITA (times)	1.07	1.67	4.91	6.57
Interest coverage (times)	9.07	7.01	5.13	1.70
DSCR (times)	3.53	3.11	2.18	1.13
Current ratio (times)	0.43	0.60	0.71	0.61

Source: Company data

Standalone figures for FY2019 and consolidated figures (Including holding company LMC and subsidiaries LIH, Lumbini Wami Hospital, United Public Lumbini Hospital Pvt. Ltd.)

Annexure-1: Instrument details

Instrument (Amounts in NPR Million)	Last rated limits	Current rated limits	Rating action
Long-term loan limits (A)	**470**	**378**	**[ICRANP] LBB+**; downgraded from [ICRANP] LBBB
Term loans	454	367	
Hire purchase loans	16	10	
Short-term loan limits (B)	**180**	**230**	**[ICRANP] A4+**; downgraded from [ICRANP] A3+
Non-fund based (Bank guarantee)	1	1	
Fund based (Demand loans and Overdraft)	180	230	
Grand total (A+B)	**650**	**608**	

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About ICRA Nepal Limited:

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