



MONARCH
NETWORTH CAPITAL

Update Note – Q2FY22

SHALBY LTD

Growth Ready!

November 8th, 2021

BUY

TP INR 280

Upside 81%

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INVESTMENT THESIS



Shalby Ltd ('Shalby') came out with its Q2FY22 results which reported sequential margin degrowth on the back of implants businesses losses and reduced covid related tailwinds (16.2% vs 25.5% for Q2FY21 vs 20% for Q1FY22). Implant business reported USD 1mn revenue in Q2FY22, guidance for FY22E and FY23E at INR 50crs and INR 100crs respectively. First Ortho Franchise started in Udaipur, expected to open 50 franchises across India over medium term. The newer hospitals (892 beds) reported ~12% EBITDA margins with 37% revenue contribution while mature hospitals (228 beds) reported ~37% EBITDA margins with 29% revenue contribution. Ramp-up of occupancy in newer hospitals will improve the overall EBITDA margin profile. Key optionalities including the Implants business and the franchisee business are yet to play out. We retain a BUY on Shalby with a target price of Rs280, which is 81% upside on CMP. At our target price, Shalby is available at 28x FY23E PER; on the CMP it trades at 16x FY23E PER.

BBG code	SHALBY IN
Mcap(Crs)	INR 1675
CMP	INR 155
52 W (H/L)	INR 214 / 90
Target Price	INR 280
Upside	81%

SHALBY
MULTI-SPECIALTY
HOSPITALS

Source: Company, MNCL Research

Q2FY22 performance led by strong momentum in non-covid surgeries; Implants losses drag bottom line

- Q2FY22 performance was led by higher non-covid surgery counts (~6190 vs 5000 pre-covid levels). Arthroplasty and Orthopedics contributed to ~55% of total sales. This may have an element of bulking up, being elective surgeries.
- Consolidated margins impacted on account of Implants business losses which is likely to continue in H2FY22 and reduced covid related tailwinds. Higher share of Arthroplasty and Orthopedics surgery remains key for better margins.

Implant business scale-up key for medium term profit growth

- Implant business reported sales of USD 1mn in Q2FY22 with an EBT loss of USD 0.7mn. With scale up of volumes on account of core markets including North America, Japan and Latam markets and entry into high growth markets in Asia will lead to better margins driven by operating leverage.
- Guidance:** Revenue target for FY23E is INR 100crs and INR 45 to INR 50crs for FY22E

Multiple optionalities and attractive valuations

- We believe key optionalities including the Implants business and the franchisee business are yet to play out. Implants to be a significant contributor to the earnings growth with new strategy and leadership team in place.
- We retain a BUY on Shalby with a target price of Rs280, which is 81% upside on CMP, which has been reduced from INR 320 on account of estimate revision. At our target price, Shalby is available at 28x FY23E PER; on the CMP Shalby trades at 16x FY23E PER

Particulars(INR in Crs)	Q2FY22	Q1FY22	QoQ%	Q2FY21	YoY%
Revenue	1,816	1,924	-6%	1,156	57%
EBITDA	294	382.9	-23%	295	0%
EBITDA Margin%	16%	20%	-369bps	26%	-929bps
EBIT	180	293	-39%	203	-11%
EBIT Margin%	10%	15%	-534 bps	18%	-766 bps
PAT	108	205	-47%	245	-56%
PAT Margin%	6%	11%	-473bps	21%	-1524bps
EPS	1.0	1.9	-47%	2.3	-56%

Source: Company, MNCL Research

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REVENUE

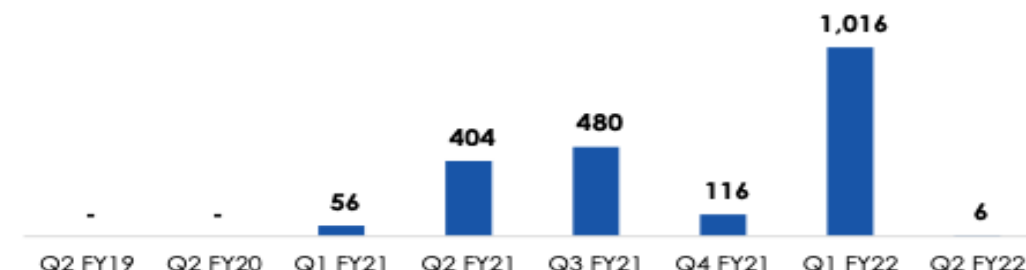


Non-Covid Total Patients Count



Source: Company Presentation

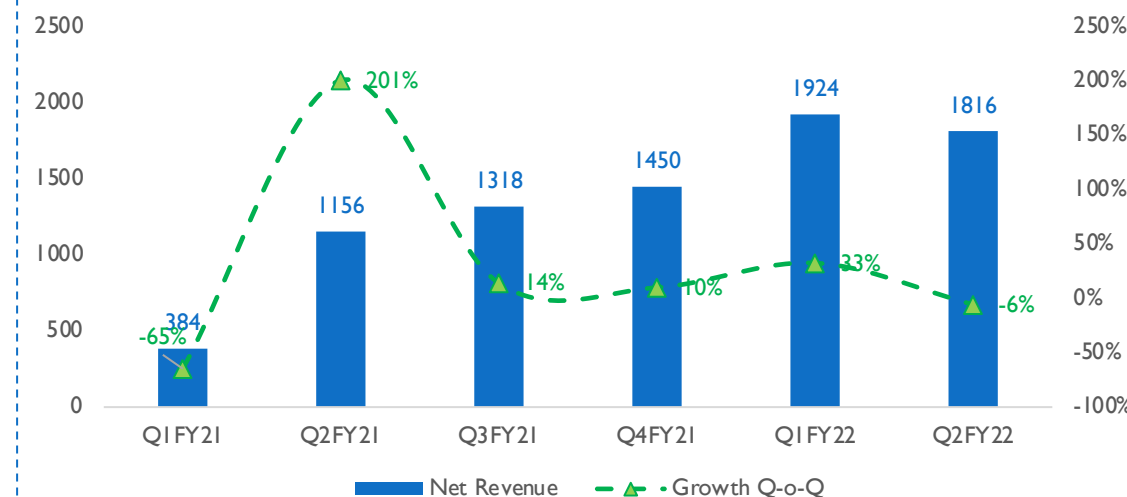
Covid Revenues (Rs mn)



Source: Company Presentation

Q2FY22 sales reflected normalized base

- Q2FY22 sales had hardly 14 covid patient count vs 5361 in Q1FY22 and thus the revenues on account of Covid related tailwinds reduced.
- At the same time, non-covid surgeries made a come back with ~6190 surgery count led by elective surgeries including Arthroplasty and Orthopedic (~55% of total revenues)
- We thus consider Q2FY22 to be a normalized base for the hospital business. However, Q2FY22 surgery count momentum may not continue on account of bulking up of surgeries post covid.



Source: Company, MNCL Research



SHALBY CONSENSUS – IMPLANTS BUSINESS

Details of the Acquisition

- Shalby acquired certain assets from Consensus Orthopaedics (Consensus), headquartered in California.
- The acquired assets primarily comprise of inventory and plant & equipment. Product inventory includes knee systems, mobile bearing knee systems, hip systems and revision knee systems.
- The manufacturing site as well as the products are USFDA approved. Further, a team of over 40 Consensus employees will be joining Shalby as part of this transaction.
- Consideration:** USD 11.45mn to be funded by USD 3.35mn in cash and USD 8.45mn in bank borrowings.
- Management:** Appointed Mr. Sushobhan Dasgupta as Vice Chairman and Global President of Shalby Limited and Mr. Daniel Hayes as the Chief Executive Officer of Shalby Advanced Technologies.

Current Status

- EBITDA loss has reduced from INR 38 million in last quarter of operations which was 45 days to INR 15.4 million in first full quarter for the year on account of higher operational efficiencies
- Engaging with existing customers through regular management field meetings while the back orders are being serviced gradually as per arrival of raw materials has supported the ramping up of the sales as the implant business during the quarter, recorded total revenues of USD 1mn and YTD revenue is USD 1.6mn.
- Re-establishing market presence and revenue base in core markets of US, Japan and Latin America while entering high growth markets of Middle East and Asia, particularly India, Indonesia, Vietnam and Bangladesh will help increase the margins as the business reaches higher operational efficiencies on account of volume growth
- Guidance:** Revenue target for FY23E is INR 100crs and INR 45 to INR 50crs for FY22E

Q2FY22 Performance	USD ('000)	INR (In Crs)
Revenue From Operations	1,000	7.38
Gross Profit	470	3.47
GP Margin (%)	49%	49%
EBITDA	-209	-1.54
EBIT	-562	-4.1
EBT	-679	-5.0

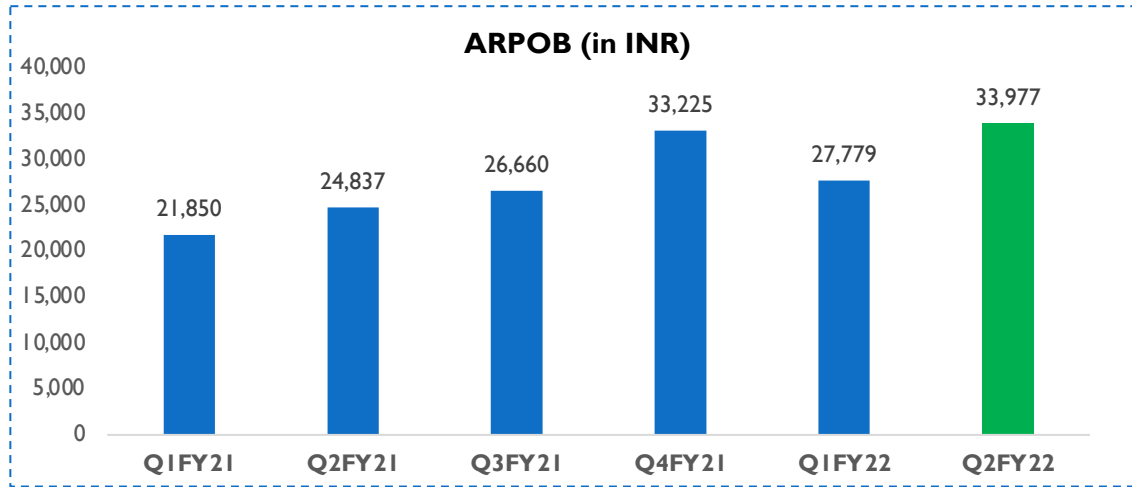
Source: Company, MNCL Research

Particulars	FY22E	FY23E	FY24E
Revenues (Rs cr)	56.3	112.5	168.8
Revenues (USD mn)	7.6	15.2	22.8
Gross Profit (Rs cr)	27.6	61.9	101.3
Gross Margins (%)	49%	55%	60%
Opex (Rs Cr)	38	50.6	67.5
EBITDA (Rs cr)	(10.4)	11.3	33.8
EBITDA Margins (%)	-19%	10%	20%

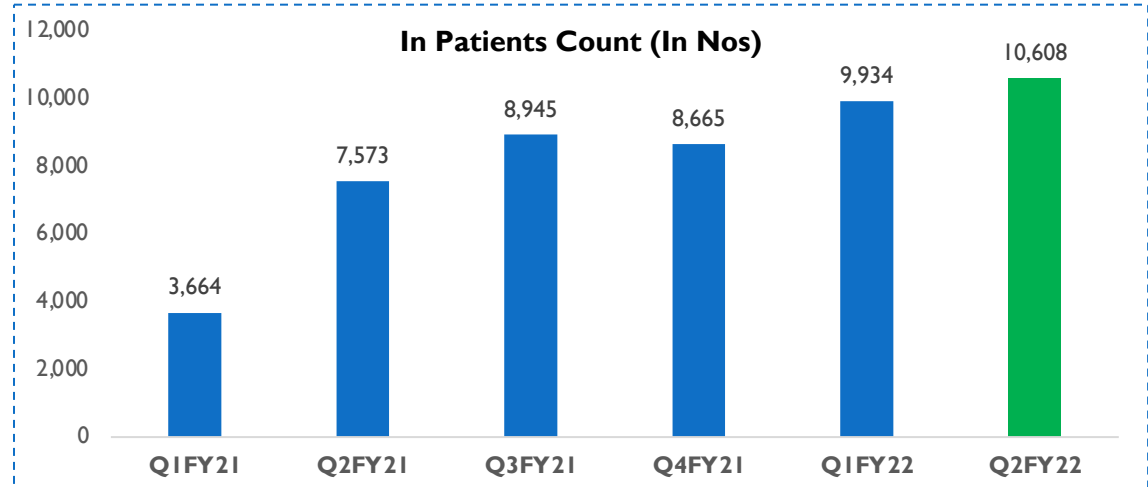
Source: MNCL Research



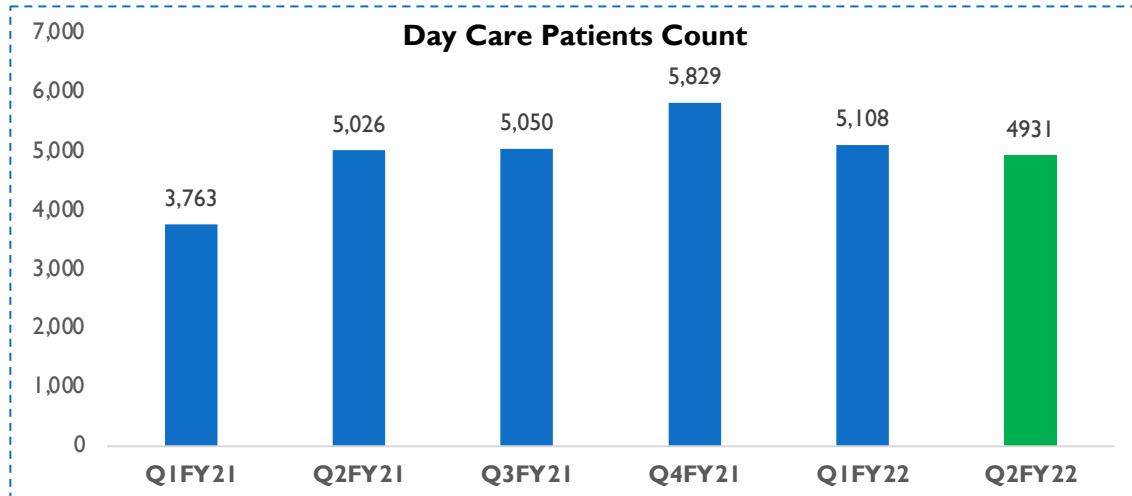
QUARTERLY OPERATIONAL METRICS



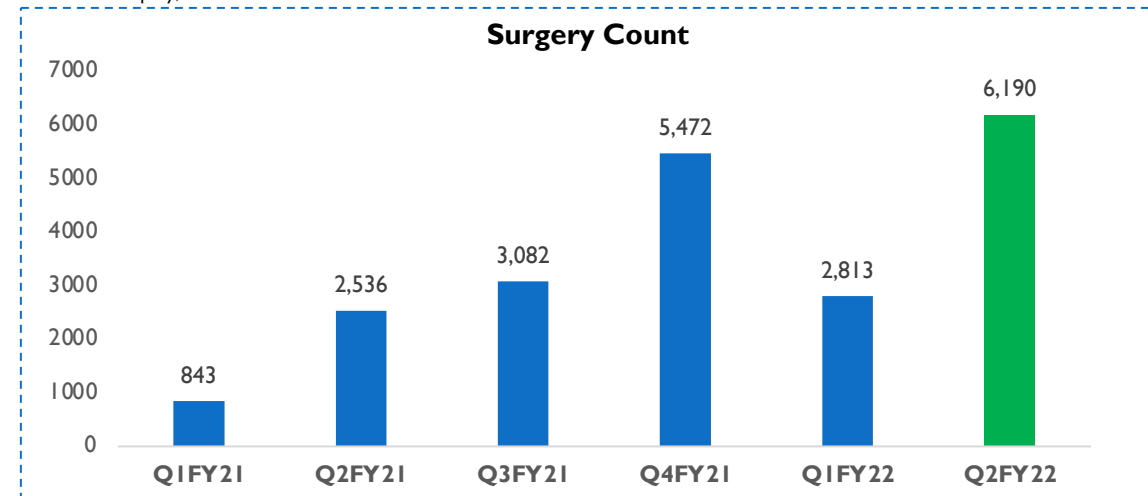
Source: Company, MNCL Research



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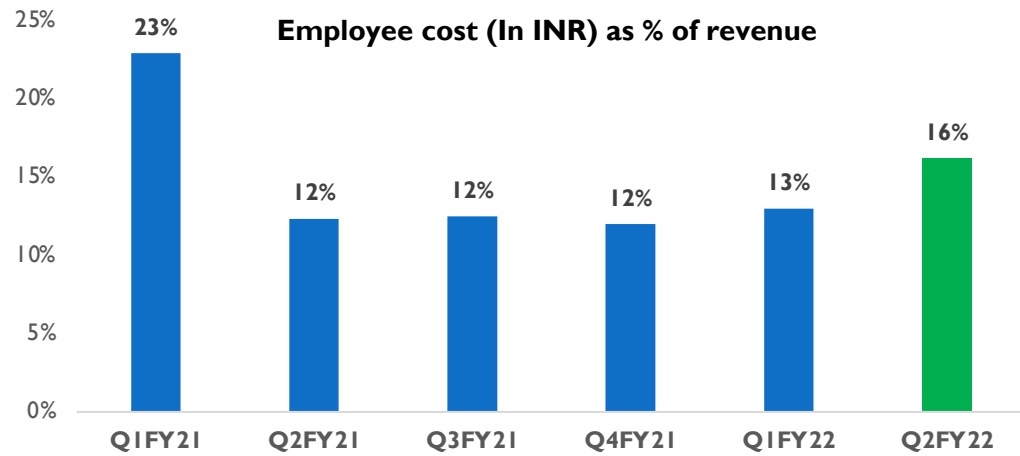
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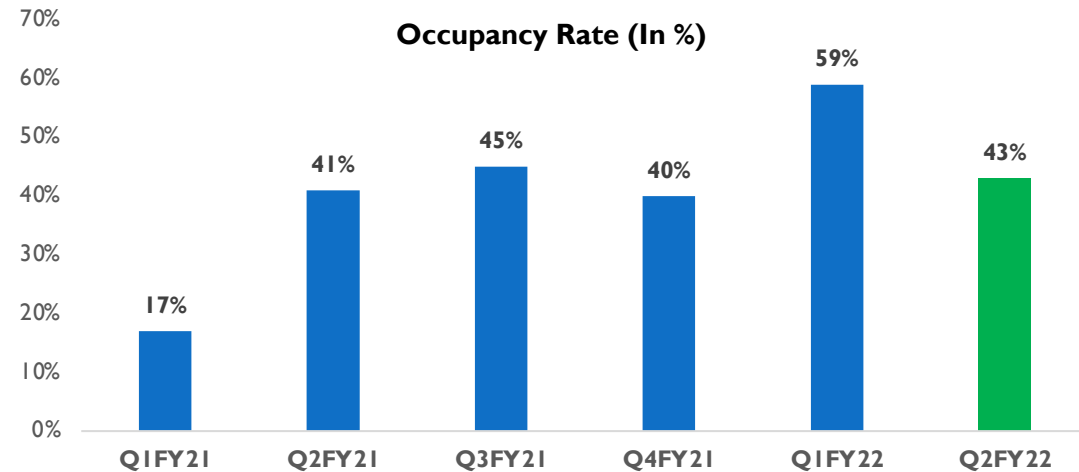
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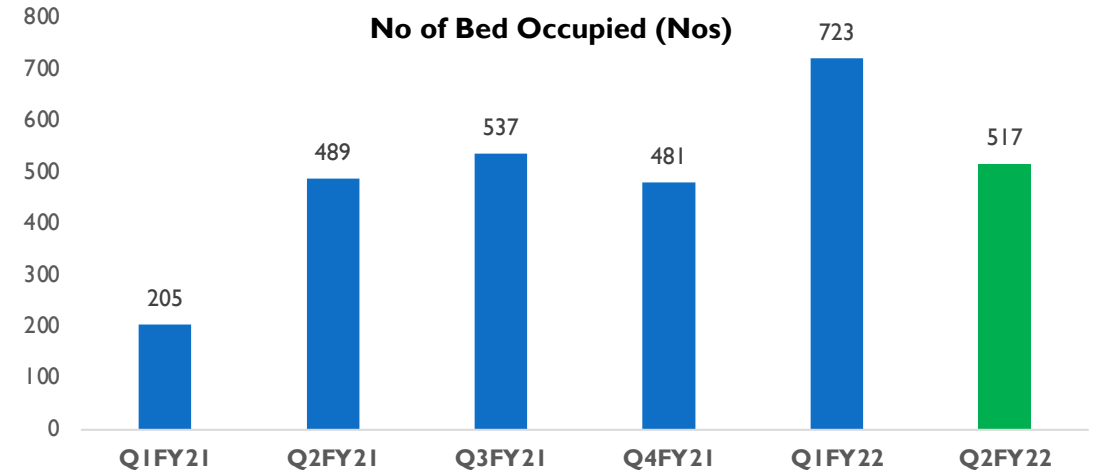
QUARTERLY OPERATIONAL METRICS



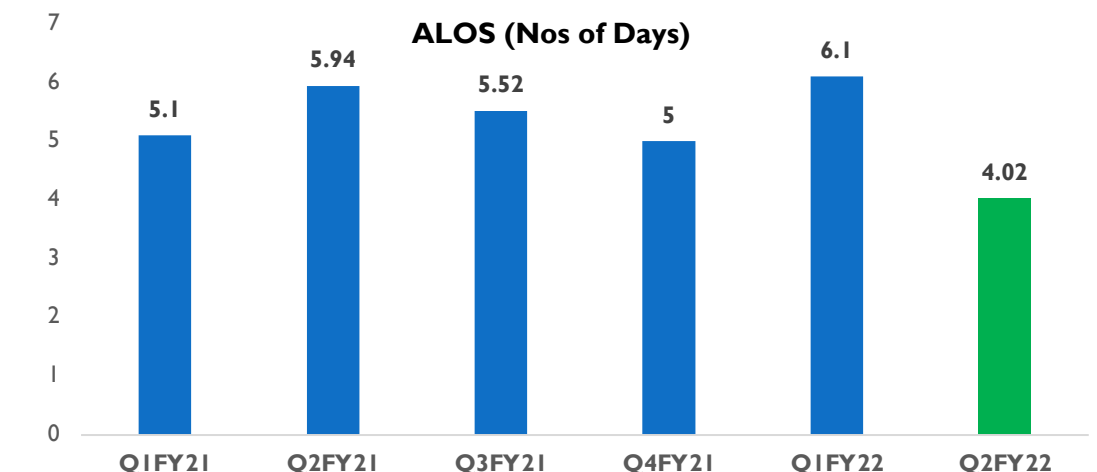
Source: Company, MNCL Research



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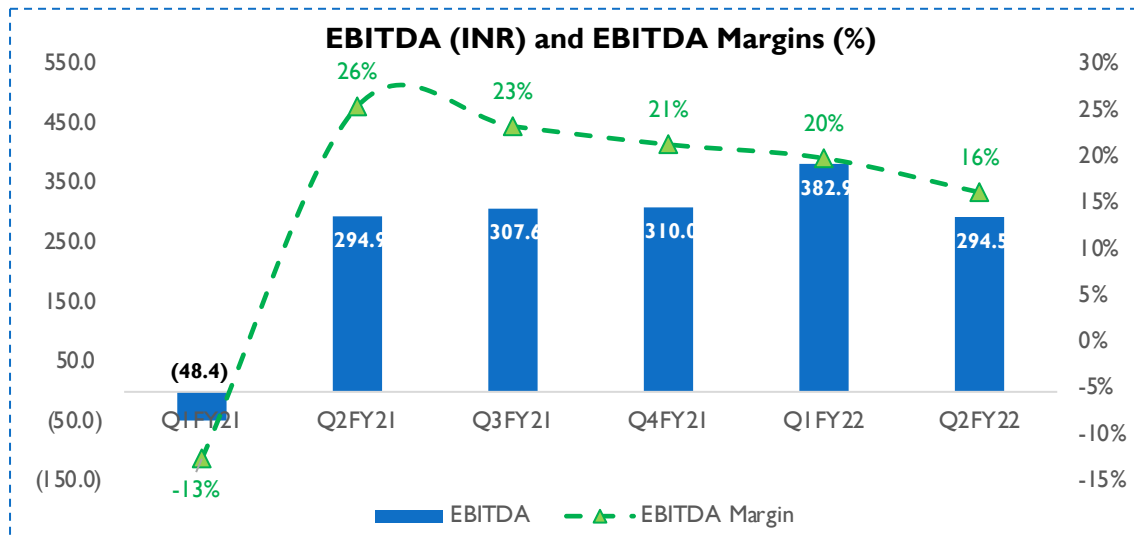


Source: Company, MNCL Research

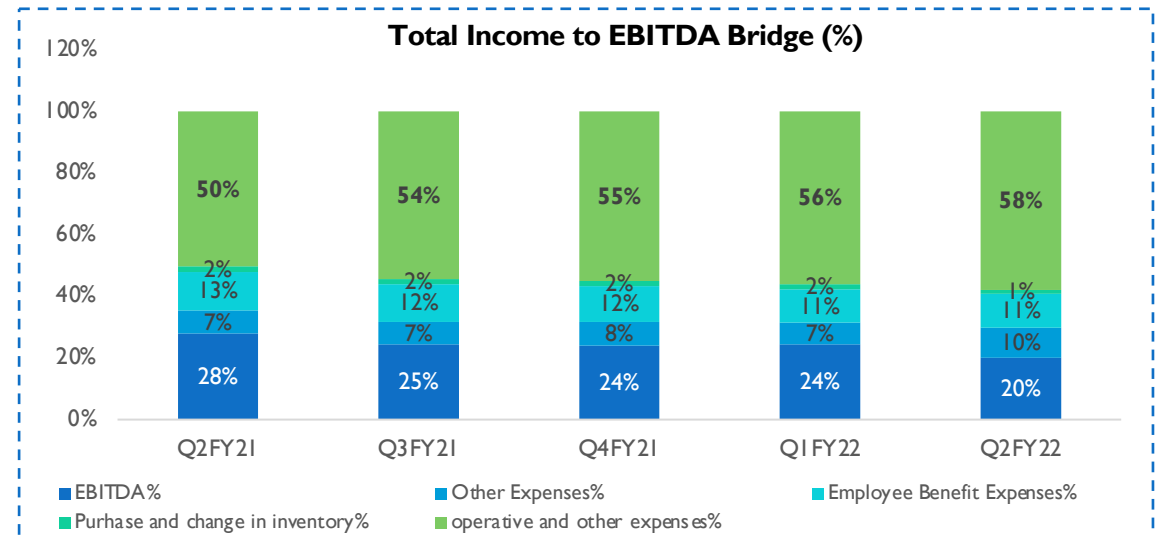


Source: Company, MNCL Research

MARGINS



Source: Company, MNCL Research



Source: Company, MNCL Research

Consolidated EBITDA margins reducing on account of Implant business

- EBITDA margins have reduced in H1 FY22 vs prior period on account of reducing Covid related tailwind and losses on account of Implants business.
- Implants business posted ~50% gross margins, however on account of higher opex remains loss making. The consolidated numbers are impacted to the extent of higher employee costs and other expenses.
- Higher Arthroplasty surgeries, reducing losses from Implants business and franchisee revenues should lead to much better EBITDA margins over medium term.

Q2FY22 CONCALL KTA'S



Operational Performance

- In patients count increased 40% y-o-y led by non-covid patients. Covid patients drop to 14 vs 5350 in Q1FY22
- Surgery count at 6190 in Q2FY22 vs pre-covid run-rate of ~5000 surgeries
- ARPOB at INR 33,977; ALOS at 4.02 days and occupancy at 43% for Q2FY22
- Non-Covid patient count at 121,829 in Q2FY22; higher than pre-covid levels.

Shalby Consensus – Implants business

- Revenue target for FY23E is INR 100crs and INR 45 to INR 50crs for FY22E
- Re-establishing market presence and revenue base in core markets of US, Japan and Latin America. Plans to enter high growth markets of Middle East and Asia, particularly India, Indonesia, Vietnam and Bangladesh
- FDA approval in US and Japan. 80% documentation done for India, other countries of south east Asia and row. On track to get the approvals in next 6-8 months.
- Gross margins at ~49%; efficiency in GMs to be led by higher volumes
- New product launches expected in November
- Company performed roughly for past 5 years due to lack of funding hence supply issues to market.

Hospital Business

- Arthroplasty and Orthopedics in total contributed ~54% of total surgeries
- Standalone Hospital Margins at 20% vs 24.4% in Q1FY22 which had significant Covid related tailwind.
- Total vaccinations done is 1 lakhs plus from which revenues earned is INR 10crs
- Capex plans: INR 160 cr in Santacruz Hospital Mumbai (175 beds) and INR 31crs in Nashik (146 beds)

Orthopedic Franchise Business

- First orthopedic franchise launched in Udaipur; to add another franchise in Jaipur
- Plan to add 50 Franchise in next 3 years; most of the hospitals to be 30-60 bed Arthroplasty super specialty
- Can potentially add INR 800 to 1,000 crs in revenue from franchise operations with potential EBITDA margin of 20%
- Margins depends on franchise model. In FOFO all revenues will hit the margins directly and In FOSO model-revenues will split and expenses will be deducted.

OPTIONALITY



Optionality

Implant Business synergies

Franchisee Model

2 new hospitals

Ramp-up of Implant business faster than estimated

- As per the management during the concall, Consensus did USD 7.5mn sales in the last fiscal operating at 15% utilization i.e. 3,000 implants. This would mean a realisation of appx. USD 2500 per Implant for the company. With its internal consumption requirement of ~10,000 implants, it can lead to potential synergies of Rs 1 Cr per annum.
- We have assumed Implants business to do USD8mn in FY22 and USD 15mn in FY23E which is in line with the management. Any upside from internal consumption is not included.

Upside from Franchisee model haven't been incorporated

- It recently launched its first Ortho Franchise in Udaipur and plan on launching 1 more in Jaipur by end of FY22. Medium term plan is to ramp up franchise count to 50. Profitability in franchise business is expected to be in-line with the hospital business and potentially can do revenues of INR 1,000crs on 50 franchise.
- However, given the nascent stage at which project is operating, we haven't incorporated any upside from this initiative.

Nashik and Asha Parekh Hospital commercialized post FY23E

- Nashik Hospital commercialization is expected to happen in H2FY23E, While Asha Parekh Hospital by FY24E on account of Covid related disruptions
- We thus have considered both the hospitals to be commercialized post FY23E. Early commercialization may debt EBITDA on account of upfronted opex.

SOTP VALUATIONS



Hospital Business

FY23E
EBITDA

Rs 166cr

EV/EBITDA (x)

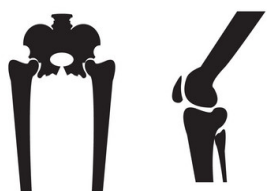
16x

EV

INR 2,656cr

Rationale for multiples

- We believe, FY23E EBITDA is still not reflective of the overall potential of the business on account of 33% of operating beds still in the early stages of maturity.
- Shalby has enough capacity to grow over medium to long term without the need of any specific capacity. **Further, we have not incorporated any upsides from the franchise business.**
- Given the specialty focus and earnings expansion potential, we thus value hospital assets at 16x FY23E EV/ EBITDA.



Implant Business

Rs 11.3cr

20x

INR 225cr

- At the outset, we have revised our EBITDA assumptions for the business from INR 12.5crs FY23E EBITDA earlier to INR 11.3crs on the back of management commentary in Q2FY22 concall.
- Implants business profitability is expected to improve at a faster clip post FY23 on account of opex leverage. We have assumed ~10% EBITDA margins while peers operate at 23%+ EBITDA margins.
- Given this, we have valued this at an elevated multiple of 20x FY23E EV/EBITDA.



INR 177 crs

16.2x

INR 2881crs

- **Given the derived EV of INR 2881cr; we have arrived at a revised target price of INR 280 per share, which is 81% above the current market price of INR 155.**

VALUATIONS



Target price Rs280, Upside 81%

- Shalby's best in class EBITDA margins even with lower occupancy and lower Capex/bed is a testimony of its cost and capital efficient operations.
- The newer hospitals (33% of operating beds) to lead EBITDA expansion on account of increased occupancies and asset maturity.
- We believe key optionalities including the Implants business and the franchisee business are yet to play out. Implants to be a significant contributor to the earnings growth with new strategy and leadership team in place. Synergies to be massive for Shalby given the internal consumptions.
- We thus Retain a BUY on Shalby with a target price of Rs280, which is 81% upside on CMP, which has been reduced from INR 320 on account of estimate revision. At our target price, Shalby is available at 28x FY23E PER; on the CMP Shalby trades at 16x FY23E PER

Key Risks

Inability to ramp-up occupancies in new hospitals : Impact **High**

- Bulk of the EBITDA expansion in our projections are contributed from the new hospital portfolio
- Inability to turnaround these assets will significantly impact the earnings growth and overall re-rating potential of the company

Keyman Risk – Arthroplasty & Dr Vikram Shah : Impact **High**

- Dr Vikram Shah remains a key pull behind Shalby's Arthroplasty practice especially in SG Highway Hospital in Ahmedabad and hence there is significant Keyman Risk involved
- Further, Arthroplasty penetration into non-Gujarat Hospitals remain a key trigger for overall increase in ARPOBs and EBITDA profile of these units.

New Capex : Impact **Medium to High**

- Given the occupancy levels and lower utilisation of the maturing hospitals; Adding new Hospitals without sufficiently maturing the existing ones would be RoE dilutive

PEER COMPARISON



Peer comparison of valuations

Particulars	CMP	Mcap	PAT (FY23E)	PEx (FY23E)	EV (FY23E)	EV /EBITDA (FY23E)
Shalby	154	1,675	111	15.0	1,532.24	8.6
Avg Peers						
Apollo Hospitals	4434	63,820	1,128	56.8	64,384.40	25.7
Max Healthcare	339	33,494	951	34.6	32,583.20	22.7
Fortis Healthcare	251	19,051	434	42.6	19,496.10	17.1
Narayana Hrudayalaya	540	11,119	321	34.4	11,339.80	16.5
Aster DM	194	9,678	566	17.0	12,521.00	7.8
Healthcare Global	247	3,028	25	137.4	3,394.30	13.0

Source: Company, MNCL Research

- Shalby available at a discount to peers:** On all the valuation parameters, Shalby trades at a discount to peers. Further, Net cash position, Rich ARPOBS and Margin profile and earnings expansion potential makes Shalby worthy of better multiples.

Key Triggers for Re-rating

- Management Bench strength:** With Mr Shushobhan Dasgupta appointed as the Vice Chairman and Global President of Shalby, the management bench strength has been further strengthened. Mr Dasgupta was the Vice President at Johnson & Johnson Medical Asia Pacific thus bringing rich expertise in Implants business which is the new growth area for Shalby.
- Implants Business:** With backward integrating into Implants manufacturing provides significant synergies to Shalby. Further, potential to market the products in US and Asia - pacific can be a significant growth driver.
- Hospital Earnings growth:** Growth drivers are in place for Shalby to increase its current EBITDA base by 2x on the back of maturity of new hospitals. Medium term earnings growth can be another re-rating trigger for Shalby. Further, upside from franchise business remain key optionality.

FINANCIALS



Profit and Loss Account

Y/E March (Rs Crs)	FY16	FY17	FY18	FY19	FY20	FY21	FY22E	FY23E
Net Sales	290	324	378	462	487	431	674	847
% growth	5%	11%	17%	22%	5%	-11%	15%	14%
Cost of Consumables	4	37	40	40	53	34	54	42
% of sales	2%	11%	10%	9%	11%	8%	8%	5%
Hospital Operation Expenses	178	150	181	240	241	215	323	398
% of sales	61%	46%	48%	52%	49%	50%	48%	47%
Personnel	29	39	45	65	66	57	74	93
% of sales	10%	12%	12%	14%	13%	13%	11%	11%
EBITDA	56	71	79	83	83	86	113	177
EBITDA Margin (%)	19%	22%	21%	18%	17%	20%	17%	21%
Depreciation	11	17	23	33	36	37	41	42
EBIT	44	55	56	50	47	49	77	146
Interest Expenses	10	11	12	9	7	4	2	2
PBT From Operations	34	44	44	41	39	46	75	145
Other Income	2	7	10	9	17	9	13	13
PBT	36	51	54	50	57	55	88	158
Exceptionals	-	-	-	-	-	-	-	-
PBT after Exceptional	36	51	54	50	57	55	88	158
Tax-Total	-	0.4	21.8	14.6	18.7	12.7	21.2	37.8
Effective Tax Rate (%)	-1%	43%	27%	37%	51%	23%	24%	24%
Reported PAT	36	29	39	32	28	42	67	120
Extraord. items -Adj.	-	-	-	-	-	-	-	1
Adjusted PAT	36	29	39	32	28	42	67	120
PAT Margin	13%	9%	10%	7%	6%	10%	9%	14%
% Growth	12.5%	8.9%	10.4%	6.9%	5.7%	9.8%	9.2%	13.6%

Source: Company, MNCL Research

Balance Sheet

Y/E March (Rs Crs)	FY16	FY17	FY18	FY19	FY20	FY21	FY22E	FY23E
SOURCES OF FUNDS								
Capital	88	88	108	108	108	108	108	108
Reserves & Surplus	117	164	643	672	691	727	794	913
Shareholders' Funds	205	251	752	780	799	835	902	1,021
Minority Interest	0	(1)	0	0	0	0	0	0
Total Loan Funds	210	311	91	57	49	36	29	29
Total Liabilities	422	568	907	910	944	915	976	1,095
APPLICATION OF FUNDS								
Gross Block	428	341	692	766	782	781	864	895
Accumulated Dep.	109	18	41	74	110	121	158	199
Capital WIP	82	221	46	2	3	4	35	84
Net Fixed Assets	401	544	697	695	679	667	745	784
Investments	0	0	0	0	0	0	0	0
Other non-current assets	38	38	97	106	114	58	30	42
Goodwill	-	-	-	-	-	-	-	-
Inventories	7	8	12	13	15	23	30	44
Sundry Debtors	31	34	51	81	95	88	142	172
Other Current Assets	1	12	16	12	20	21	21	21
Cash & Cash Equivalent	16	16	116	36	57	99	85	132
Loans and Advances	8	12	17	55	47	40	40	40
Total Current Assets	64	159	236	197	234	271	318	409
Trade Payables	47	39	49	56	60	58	91	111
Other Current Liabilities	35	63	49	31	22	24	26	29
Provisions	0	71	25	1	1	1	1	1
Total Current Liab. & Prov.	82	173	123	88	83	82	118	140
Net Current Assets	(18)	(15)	113	109	150	189	201	270
Total Assets	422	568	907	910	944	915	976	1,095

Source: Company, MNCL Research

FINANCIALS



Ratios

Y/E March	FY16	FY17	FY18	FY19	FY20	FY21E	FY22E	FY23E
Growth ratios (%)								
Net sales	5.4	11.5	16.7	22.3	5.3	-11.5	15.2	14.0
EBITDA	-17.7	28.6	10.4	5.8	-0.9	4.3	36.3	60.3
Adjusted Net Profit	12.5	8.9	10.4	6.9	5.7	9.8	9.2	13.6
Margin Ratio (%)								
EBITDA Margin	19.1	22.1	20.9	18.1	17.0	20.0	16.1	21.3
EBIT Margin	15.2	16.9	14.8	10.9	9.6	11.5	10.5	16.6
PBT Margins	12.4	15.6	14.2	10.9	11.7	12.8	12.1	17.8
PAT Margin	12.5	8.9	10.4	6.9	5.7	9.8	9.2	13.6
Return Ratio (%)								
ROE	17.7	11.4	5.2	4.1	3.5	5.1	7.4	11.7
ROCE	11.3	6.1	5.6	3.8	3.3	4.9	7.4	12.1
ROIC	11.2	10.9	7.8	7.1	7.6	6.7	9.7	15.2
Turnover Ratio days (days)								
Fixed Asset Turnover Ratio	0.9	0.7	0.6	0.7	0.7	0.6	1.0	1.2
Inventory Period	9	9	12	10	11	20	15	18
Debtors Period	40	38	49	64	71	74	70	70
Creditors Period	59	44	47	44	45	49	45	45
Net Working Capital Days	(10)	2	13	30	37	45	40	43
Solvency Ratio (%)								
Net Debt-equity (x)	1.0	1.2	0.1	0.1	0.1	0.0	0.0	0.0
O/s Shares	8.7	8.7	10.8	10.8	10.8	10.8	10.8	10.8
Fully Diluted Shares	8.7	8.7	10.8	10.8	10.8	10.8	10.8	10.8
Per share (Rs)								
Basic EPS (reported)	4.3	3.4	3.6	2.9	2.6	3.9	6.2	11.1
CEPS	5.5	5.2	5.7	6.0	5.9	7.3	10.0	15.0
Book value	23.5	28.7	69.6	72.2	74.0	77.3	83.5	94.6
Valuation								
P/E			56.75	44.08	18.07	25.75	26.75	14.96
P/BV			2.97	1.79	0.62	1.30	1.99	1.76
EV/EBITDA			27.78	16.32	5.36	11.42	14.43	8.75
EV/Sales			5.80	2.95	0.91	2.29	2.33	1.87

Source: Company, MNCL Research

Cash Flows

Y/E March (Rs mn)	FY16	FY17	FY18	FY19	FY20	FY21	FY22E	FY23E
Pre-tax profit	36	51	54	50	57	55	88	158
Net chg in working capital	(19)	83	(19)	(100)	(18)	(52)	(25)	(22)
Cash flow from operating activities (a)	4	60	14	43	55	84	126	146
Capital expenditure	(119)	(51)	(177)	(31)	(19)	(0)	(114)	(80)
Adjusted FCF	123	112	191	75	74	84	240	226
Cash flow from investing activities (b)	(98)	(154)	(237)	1	(31)	(57)	(132)	(98)
Debt raised/(repaid)	125	93	(203)	(24)	(5)	(9)	(6)	-
Dividend (incl. tax)	-	-	-	-	-	-	-	-
Cash flow from financing activities (c)	110	109	339	(19)	(22)	(29)	(8)	(2)
Net chg in cash (a+b+c)	16	16	116	25	3	(2)	(14)	47

Source: Company, MNCL Research

Thank You!

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Analyst holding in stock: **NO**

Key to MNCL Investment Rankings

Buy: Upside by >15%, Accumulate: Upside by 5% to 15%, Hold: Downside/Upside by -5% to +5%, Reduce: Downside by 5% to 15%, Sell: Downside by >15%

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