



Dr. Lal PathLabs Limited (LPL)
Q2 & H1 FY19 Earnings Conference Call Transcript
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Call Duration	▪ 1 hour 3 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 Goel – CFO▪ Mr. Bharath Uppiliappan - Chief Operating Officer▪ Mr. Rajat Kalra - Company Secretary & Head of Investor Relations
Participants who asked questions	<ul style="list-style-type: none">▪ Ashish Thavkar from Motilal Oswal Asset Management▪ Bharat Celly from Equirus Securities▪ Chandramouli from Goldman Sachs▪ Harith Ahamed from Spark Capital▪ Imran Khan from Ratnatraya Capital▪ Nikunj Doshi from Bay Capital▪ Prakash Kapadia from Anived Portfolio Management▪ Prashant Nair from Citigroup▪ Rohan Dalal from B&K Securities▪ Saion Mukherjee from Nomura▪ Sameer Baisiwala from Morgan Stanley▪ Shaleen Kumar from UBS Securities▪ Sriraam Rathi from ICICI Securities▪ Tushar Manudhane from Motilal Oswal Securities

Moderator: Ladies and Gentlemen, Good day and Welcome to Dr. Lal PathLabs' Q2 & H1 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 "*" then "0" on your touchtone telephone. Please note that this conference is being recorded. I would now like to hand the conference over to Mr. Nishid Solanki from CDR India. Thank you and over to you, Sir.

Nishid Solanki: Thank you. Good Afternoon, everyone and welcome to Dr. Lal PathLabs' Q2 & H1 FY19 Earnings Conference Call. Joining us today are (Hony) Brig. Dr. Arvind Lal - Chairman and Managing Director of the Company, Dr. Om Prakash Manchanda – Whole-time Director and CEO, Mr. Ved Prakash Goel – CFO. We also have with us Mr. Bharath Uppiliappan – Chief Operating Officer and Mr. Rajat Kalra -- Company Secretary & Head of Investor Relations.

I would like to highlight that some of the statements made on the call today could be forward-looking in nature. Actual results may vary significantly from these forward-looking 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. Over to you, Sir.

(Hony) Brig. Dr. Arvind Lal Good evening, everyone. I am delighted to address you all on our Q2 & H1 FY19 results. In my address today, I would like to talk to you about the company's strategic vision.

Dr. Lal PathLabs' brand stands for putting the patient first and is unmatched in its ability to offer precise diagnostic services, delivered through our network that is powered by a technology enabled platform. We have a higher than average share of walk-in patients on account of the trust that the patients and healthcare providers have restored on us and the quality of infrastructure that we have created around it.

At the organization level, we are happy with how our strategic business plan is shaping up. Together with the projected growth in our network reach across East and Central regions pivoted around the commissioning of our reference laboratory at Kolkata, we are also working at improving patient and sample volumes in the region. This would be further bolstered with the renewed focus on SwasthFit, our preventive health packages. Our hub-and-spoke model is designed to draw incremental volumes quickly with the non-linear increase in CAPEX. The growth will continue to be realized as we continue to strengthen our network especially in the under-represented areas. Therefore, the improvement we see in our earnings profile is also expected to be sustainable over the long-term.

With that, I would like to hand over the forum to Dr. Om to share his thoughts and updates on the "Operational Performance."

Dr. Om P Manchanda:

Thank you, Dr. Lal. I am pleased to inform you that our Revenue for Q2 FY19 improved by 14.1% to Rs. 317.5 crore. It was driven by volume growth of 18.8% which has trended largely as per our expectations.

We are seeing good progress in 'bundled test packages' under the name SwasthFit. This is gaining further momentum and hence has helped us to increase our samples per patient from 2.28 in Q1 of FY18 to 2.34 in Q2 of FY19. Our strategic focus remains on further deepening our network footprint through additional franchisee collection centers, for scaling up in the markets where we are already a very strong player. While we do that, we are also cognizant of supporting our existing partners to grow and our effort is to help PSCs, i.e., Patient Service Centers to expand their scope and scale wherever possible.

Our plan for Western and Southern zone is centered around the focus cities. We are looking at building clusters around Pune and Bangalore and enhancing the coverage out there. From a capacity building perspective, we are open to explore opportunities for inorganic growth through mergers and acquisitions in these markets.

We are also able to maintain our EBITDA margins despite inflation and some cost elements by renewed focus on cost optimization and productivity enhancements. For the year FY19 ahead, we are looking at maintaining the current trend in volume growth by leveraging technology and our network to grow patient volumes and continued focus on improving the test mix.

With that, now I request Ved to give us an update on the "Financial Performance."

Ved P Goel:

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

The underlying patient volume for Q2 FY19 stood at 4.8 million as compared to 4 million in the same period last year. The samples per patient has also increased to 2.34 from 2.28 in Q2 last year same period. Revenue realization per patient for Q2 stood at Rs. 669 which is marginally lower as against Rs. 691 for Q2 last year. Normalized EBITDA after eliminating the impact of RSU, other stock-based charges and CSR expense in Q2 stood at Rs. 905 million as compared to Rs. 808 million reported in Q2 FY18, representing a growth of 12.1% YoY.

Normalized EBITDA margin for Q2 stood at 28.5%. Other income includes dividend from liquid funds and interest on deposits. Cash and liquid funds at the end of Q2 FY19 stood at Rs. 6,332 million. PBT came in at Rs. 881 million in Q2 FY19 versus Rs. 778 million in the same period of previous year, a growth of 13.2% YoY. PAT grew by 12.8% to Rs. 574 million in Q2 FY19 as compared to Rs. 509 million in Q2 of last year. EPS for Q2 FY19 is Rs. 6.92 versus Rs. 6.19 in the same quarter last year.

I am happy to inform that Board has approved an interim dividend of Rs. 2.5 per share.

With a strong financial performance, coupled with an integrated network and trust of patients and healthcare providers, we are well poised to benefit from the emerging opportunities in the Diagnostics sector.

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. Ladies and gentlemen, we will now begin the question-and-answer session. We will take the first question from the line of Saion Mukherjee from Nomura.

Saion Mukherjee: My first question is regarding the volume growth you mentioned, the trajectory will remain strong but we are now having a higher base as you go into the second half of this fiscal year. How sustainable you think and if you can guide on the volume growth?

Dr. Om P Manchanda: This volume growth actually is a function of at times a seasonality of fever incidents. This year definitely we have seen bit of a subdued seasonality. We are currently in the middle of that. The clarity on the volume growth for this quarter will probably emerge by end of this month. But as we have always said in the past also that there is a renewed thrust in the company to drive volumes as much as possible and that is why we have been also very competitive on pricing. That is where we are seeing the benefit of that. I think we are still fairly comfortable on this number as of now. I know that you are probably referring to higher base due to higher growth in the second half but on a sequential basis the base is not that high. So, we are still very confident as of now.

Saion Mukherjee: On the pricing front, I see the realization per patient has come down marginally, it is a function of probably mix and pricing. So, particularly on pricing how you are seeing and what is the environment like and are we at a stage where the pricing can go up anytime soon?

Dr. Om P Manchanda: I think if you really want to do that, you can always do that but consciously we have decided to stay competitive on that, get higher throughput through volumes. As of now, we will stick to that strategy what we have outlined in the past plus this realization is not entirely due to price, it is slightly also we have had few promotions last quarter to drive new customer acquisitions, that also has impacted realization. We hope to recover maybe in the next two quarters. So, it is not entirely due to price drop itself or price rationalization, it is also impacted by some kind of promotion schemes that we ran in this quarter.

Moderator: Thank you. We will take the next question from the line of Rohan Dalal from B&K Securities.

Rohan Dalal: I just wanted to understand just in line with what the last participant was asking, with regards to the realizations, I think the fall has been little bit larger than usual with the sales per patient falling by about 5% and so that was something I thought that was a little concerning if you can throw some color on that maybe how exactly we see this panning out in the next half year that would be great?

My second question is in regards to the cost structure. So, we have been optimizing the cost at a pretty strong rate; we are already at 27% normalized EBITDA margin. I was wondering if that seems to be sustainable and if we should build that in as a steady state rate?

Dr. Om P Manchanda: So, let me take the last question first. So, we are fairly confident of having this kind of margin sustained at least for the year. I think that confidence is fairly high. As far as the revenue per patient part is concerned, I think I agree with you that the gap between volume and value growth has widened. We have studied the reasons behind that. In addition to mix change, I think one of the reasons has been that because we are driving certain volume growth especially in the East region, we ran a scheme where we did a lot of free testing for patients, where the volumes got counted but revenue was not there, so that impacted revenue per patient. We believe that is not the entire reason, it is to the extent of about 2%, balance is due to price and mix change. So, we will still continue to do these schemes maybe next three, four months, maybe next quarter where revenue per patient may again be little bit impacted but we hope to recover back to a normal sort of a thing. So, probably my sense of forecast on that would be it will be nearly flat rather than declining over previous years.

Rohan Dalal: With regards to the realizations, is there any rise in competition or this is just because of our expansion to the East, so has the competitive landscape really resolved from last two years actually?

Dr. Om P Manchanda: I think as I mentioned even in the previous quarter's call also that intensity of competition is not as much as what one used to see. It is a bit of deliberate attempt on our side to drive traffic and volumes so that we build scale, and as I mentioned earlier as well that lot of our infrastructure still has a scope to serve larger number of volumes and we have potential to really benefit from the scale. So, that is why we are driving volumes especially in our rest of India territories.

Moderator: Thank you. We will take the next question from the line of Shaleen Kumar from UBS Securities.

Shaleen Kumar: Just want to understand you have said that this is a deliberate attempt over on our side. So, is there a volume growth or volume size in our mind post which we would like to increase or beyond which we want to see a price increase, or there is a timeline thing in your mind that we want to keep it at this level for some time?

Dr. Om P Manchanda: Around 17-18% volume growth if we can sustain over a period of time and I think that is a number which I should keep in mind.

- Shaleen Kumar:** Beyond that you would like to take price increase?
- Dr. Om P Manchanda:** Yes, the price increase is driven because if the cost rise then we cannot help it, then we will have to do it in any case, but if we can push it without diluting the margins and volume growth of 17-18% is where I would be more comfortable with.
- Shaleen Kumar:** Can you give some update on the competition per se specifically in B2B space and also an update on the Kolkata Lab, how it has been running, if we can get something like how much revenue it has started contributing?
- Dr. Om P Manchanda:** Our East region growth has been 23% which is higher than of course our overall business growth. So, we continue to see a good traction. State wise I think Bihar, Jharkhand, Odisha, these markets are seeing much better growth than other parts, so we definitely see much more potential to grow here. It has been now close to six, seven months. Ideally I would have loved to see little higher growth from East than what we have experienced, but let us see how it goes; West Bengal and North East can do better.
- On the competition, there is nothing much which one is seeing. So, it is pretty much the same. Relatively that aggressiveness what one used to see on pricing is slightly mellowing down. As far as three or four large players, I think these companies numbers are public and you must be seeing those numbers, they have had their results declared last week, another competitor has filed for DRHP again you will be aware about that. The competition at the regional level is much more muted than what it used to be earlier. So, I think it is pretty much stable scenario, there is no change one has seen. I really do not have any fresh update on the competition side unless Bharath, do you want to add something to it?
- Bharath Uppiliappan:** I think the other fact is we also have been responding at the localized level where competition is coming from. We are effectively able to control the market scenario from our strength perspective. So, we have also become sharp and nimble in terms of responding back where required, it is not a broad spectrum.
- Dr. Om P Manchanda:** Actually, competition was at two level; one was in the last two years where we have seen a lot of these bundle packages being promoted by many companies, sending SMSs etc., I think we have responded very well to that. Second level of competition has been in institutional segment where lot of undercutting was happening on pricing, that we have responded now fairly well. Third element was lot of these hospital lab management, there also lot of discounting was happening. I think to some extent we have realized that, potential has large opportunity but may not be a very viable opportunity so we sort of recalibrated our approach to hospital lab. So, there is no fresh update than what we have been saying in the last two quarters on competition.
- Shaleen Kumar:** For your Kolkata lab, is there an operating metric which you are gauging and when will you call it as success and if you like to repeat this in Lucknow?

Dr. Om P Manchanda: Internal sort of benchmark for us is if we can grow that region twice the growth rate of the company, let us say if I grow 15-16% the company, then I should really touch 30% in the East region, is the way I would like to look at it.

Secondly, I know that purchasing power of East is not that high as let us say as other parts of India. So, I really would like to drive scale, more volumes so that we can probably protect our margins even at a lower realization is what I would like to see. So, actually I would like to chase more volumes there and slightly better average between lab to CC ratio so that my cost overhead structure is lower.

Lucknow, as of now we are just putting it on the backburner because that market we believe can be easily serviced from Delhi and we have equally large operations out of Kanpur. So, as of now we are putting Lucknow on the back burner.

Moderator: Thank you. We will take the next question from the line of Prakash Kapadia from Anived PMS.

Prakash Kapadia: About the sustainability of volume growth if I look at this quarter also has been good, what are we doing to sustain the volume momentum, especially in NCR, because that still accounts for a larger portion of our Revenues, so some value addition with technology like say a reminder for tests or archives of key parameters of some trend analysis for the patients, something which we are doing additional specially in NCR if you could highlight that will be helpful?

Bharath Uppiliappan: NCR still has a lot of opportunity and room to grow and that will come once again from geographic expansion on one side, second is service level enhancement. Even the current outlets which we have we can significantly improve the service component, third is there is a lot of work happening around response time to turn around time, saying when do you pick up a sample, how do we kind of track his progress, and how do we kind of deliver reports faster and more accurately. The last component lies obviously like you said in getting more and more technology involved for example in home collection, there is a lot of work happening on that side in NCR. So, it is a key focus and yes, we will build on the citadel we have.

Prakash Kapadia: So, that is work in progress. And geographical expansion you mentioned.

Bharath Uppiliappan: It is work in deployment, so it is already in the market and it is getting strengthened every day.

Prakash Kapadia: On Kolkata, what has been the response from the hospital segment in terms of acceptance of Dr. Lal because this is where we were initially focusing on and then we were expecting the B2C to scale, so what has been the share of response from hospitals and next year do we expect hockey stick kind of growth, obviously the intention is there but the confidence of 2x growth of the company growth is what we were targeting.

So, is the visibility, confidence, learnings in Kolkata now showing us the bigger picture or not?

Dr. Om P Manchanda: Let me set the expectation. I think in our space one does not see a hockey stick kind of curve. So, it is not that one is expected to see overnight jump in growth rates. I am fairly confident that the region is very large as awareness builds up, as our service level builds up, we just got accredited by NABL because that is also very important element for many of these hospitals because they are looking for accredited lab, next stage for us maybe after few quarters we may even go for cap accreditation. All this will add to the credibility of our offering. So, to me it is going to be a steady curve rather than hockey stick curve. I am fairly confident even now also if I look at, if the company has grown at 14.1%, our East region is still at 23%, so we are there in terms of growth rates being much higher than overall company average. So, I am fairly confident that it will grow but yes, West Bengal and Northeast regions could have done better compared to Bihar, Jharkhand, Odisha, that is what we have seen. I think in next six to nine months, we will see much better performance. So, I am fairly confident about this lab doing well in this region.

Prakash Kapadia: If I look at the share of our daily dividend plans that has increased to total investments of cash and liquid. So, that should lead to a lower tax rate going forward because they are more tax efficient investments, right, because I see the current tax rate is full tax paying, that should overall reduce our tax rate going forward, right?

Ved P Goel: No, these investments we generally do in FDs where the interest is subject to same tax rate and there is no differential tax rate.

Prakash Kapadia: Daily dividend plan, so the yields are net of tax and the DDT is deducted, so overall the tax rate should come down, right, if we look at the balance sheet, DDR is almost 28-30% of our investments?

Ved P Goel: Not really because we have growth option as well as DDR option. So, this is not making any difference overall as a percentage.

Dr. Om P Manchanda: Ved, you may not have readily available data for this, but why don't you check this?

Prakash Kapadia: Yes, please, you can check. Any thoughts of parking more funds to FMPs or more tax efficient instruments going forward as we generate cash assuming there is no M&A or inorganic opportunity which we close, given the cash flows which we have, any thoughts on deployment on more tax efficient instruments?

Dr. Om P Manchanda: No, I think our audit committee is very particular on this. So, we are taking a little conservative approach on this rather than putting it to higher risk. So, our investment policy is more driven by board decisions.

- Prakash Kapadia:** I was not referring to more yields, I was referring to more tax efficiency in terms of these things here, DDR or FMP which should be far more tax efficient?
- Ved P Goel:** We are keeping this money mainly for some strategic acquisition and all that. So, we do not want to lock in any money in these long-term investments, like FMP and all that structured products but it is a good suggestion.
- Moderator:** Thank you. We will take the next question from the line of Sriraam Rathi from ICICI Securities.
- Sriraam Rathi:** A few questions: Firstly, you mentioned that current level of margin should be maintained which is around 27- 27.5%. Generally, I believe that Q2 is one of the best quarters?
- Dr. Om P Manchanda:** Sorry, when I meant current level of margins, I do not mean Q2 margins, I meant the year margins. So, as you rightly said, Q2 is the highest. So, this is not the representative margin for the year.
- Sriraam Rathi:** Last year, we had 25% margin on reported basis.
- Dr. Om P Manchanda:** 25% after ESOP charge, right. I think that is what we should maintain.
- Sriraam Rathi:** Secondly, you mentioned that the growth rate on volumes should be around 18-20%, that should be maintained in the near-term and the realization should be flattish going forward compared to the previous quarters correspondingly. So, are we indicating that the revenue growth rate in that case could be in highest double digit?
- Dr. Om P Manchanda:** No-no, the volume growth, we are aiming for 18%, I think we have achieved in the last two quarters the same number. We are hopeful that we will be able to maintain this in the next two quarters as well. Actually, if you look at our tests growth it is even higher than volumes. So, I will rather stay at volumes right now about 18%-odd but our value growth is definitely going to be lower than 18% because of mix change, because of price rationalization, because of promotions, etc., our Revenue per patient is likely to be lower, hence our value growth would be lower than the volume growth. So far, we have done first half about 15.8%, so we are confident that for the year we should be around 15% in terms of value.
- Sriraam Rathi:** Just some more details on the realization part. So, this decline in realization is primarily because of the promotions and mix or we have also taken some price cuts?
- Dr. Om P Manchanda:** It is a mix of both. So, I think it is a little bit of detail answer, Sriraam, we can take it offline because we are just trying to decompose the impact of each of these variables, but all the three variables have contributed to this; one is price rationalization, yes, in some places we have taken downward correction, we have also run some promotional activities as I mentioned

earlier and third is also mix change. So, we are just trying to decompose the impact of each of these variables and we can probably take it offline and talk about it.

Sriraam Rathi: How much of our Revenues coming from franchisee in this quarter?

Dr. Om P Manchanda: Directionally, relative contribution of franchisee is growing faster than other segments. It would not have materially changed in one quarter. So, it remains at 35%-odd.

Sriraam Rathi: In the initial remarks, you mentioned that you are looking to open clusters in Pune and Bangalore. So, what does this cluster exactly mean, how should we look at that?

Dr. Om P Manchanda: Cluster essentially means that since our presence in South and West is weak and in absence of any M&A deal materializing, so we are looking at two cities where we want to gain critical mass and these two cities are the largest cities right now, I think around Rs. 20 crore plus kind of revenue. Our intention is to see if we can take it to Rs. 40, 50 crore so that from there the region can grow further. So, as we had articulated this many quarters back, our strategy is to build clusters and then grow in contiguous markets, for us the nucleus of South and West region is Pune and Bangalore. So, that is what we keep saying, we just deepen our presence in these markets.

Sriraam Rathi: This does not mean opening a new reference lab or something?

Dr. Om P Manchanda: No, it is mainly disproportionate efforts in these markets.

Sriraam Rathi: So, more focus on these markets?

Dr. Om P Manchanda: Yes.

Moderator: Thank you. We will take the next question from the line of Chandramouli from Goldman Sachs.

Chandramouli: First question is on the SwasthFit packages that you mentioned earlier in your opening remarks. Can you give us a little bit of color and some of the initiatives that you have taken in this as well as little bit of detail on what proportion of the total revenue in this quarter is coming from here?

Dr. Om P Manchanda: I will give you some information, it is a bit of competitive information, so I do not want to tell everything. Close to about 13%-odd of our contribution is now coming from Swasth packages.

Chandramouli: Some of the initiatives that you have taken there, is there something that one can do on the corporate segment because as I understand most of the business right now is retail if not B2B, so is there something going on in the corporate segment, because SwasthFit kind of fits well in that segment?

- Bharath Uppiliappan:** Yes, corporate remains a key focus segment for us and we are building good propositions for our corporate customers and that is something which we are going to deploy in a phased manner in the market. Yes, So, corporate will remain a key market and we are addressing that.
- Chandramouli:** Just in order to understand this a little bit, could you give us a little bit of color on maybe what percentage of total business is exposed to corporates right now if we can understand?
- Bharath Uppiliappan:** We do not discuss segment wise detail as it is competitive information by nature, so we would refrain from getting into specifics on that count.
- Chandramouli:** Second question is on utilization. You mentioned earlier in the call that lot of focus is to drive more volumes through your infrastructure and you are taking that approach. So, can you give us some color on what levels of utilization your infrastructure is at, at the moment to understand how much more we can grow on the volume?
- Dr. Om P Manchanda:** I think easily our current infrastructure can take the twice of volumes of what we are doing including Kolkata reference lab. So, we have fairly lot of capacity to take care of the volumes right now.
- Chandramouli:** Final question is on Ayushman Bharat as the scheme was launched in late September, it has been more than a month. Are you seeing any early signs of benefit, opportunities arise out of this scheme?
- Dr. Arvind Lal:** Ayushman Bharat is more tertiary kind of a scheme. Right now, the way it has been introduced, not all healthcare providers have jumped on to the bandwagon. So, it is not for people like us right now which are purely diagnostics. What you are asking is not applicable to us right now.
- Chandramouli:** I am just trying to understand, there are some hospital lab management contracts that you do and there will be some contracts that you have with the Government as well. So, just trying to understand if you have seen any uptick in volumes as a result of Ayushman Bharat?
- Dr. Om P Manchanda:** Not really, I do not see Ayushman Bharat in current shape and form directly impacting us as of now.
- Moderator:** Thank you. We will take the next question from the line of Ashish Thavkar from Motilal Oswal Asset Management.
- Ashish Thavkar:** On Kolkata, can you share some more information as to how many labs we have connected to our reference lab and what are the kind of tests that we are doing now?
- Bharath Uppiliappan:** Close to about 20-odd satellite labs stay connected apart from direct servicing of West Bengal market. That is what is spread into Kolkata every day. From a tests view perspective, Kolkata is really self-sufficient, so their outsource to our main reference lab at Delhi is very small. So, practically all

the tests acquired from the region gets conducted over there. From a departmental perspective, apart from the routine Biochemistry, Immunoassay and Hemat we also now do molecular, we also do microbiology, histopathology and also high end test like karyotyping, etc., on premise in Kolkata. So, it is a pretty good set up and self-sufficient to meet the needs of the eastern region currently. We also keep on adding new tests and new equipment so there is a periodic review of what is required and that keeps getting added.

Ashish Thavkar: Vis-à-vis the NCR region, just broadly in terms of percentages if you do not want to share the absolute numbers, so in terms of percentages if I try to compare with the NCR region, what could be the difference between the number of tests per month and the pricing, what is the percentage difference between NCR and Kolkata?

Dr. Om P Manchanda: I think if Delhi NCR is 100 realization, then East would be about 65-70 and that maybe due to many factors, not just the pricing because the mix itself would be very different in East then what we have in North.

Ashish Thavkar: So, when you say that you want to penetrate deeper into existing regions, so is this something you would like to disturb the pricing model in Delhi, so is it something which is at the back of your mind?

Dr. Om P Manchanda: No, when we say go deeper essentially there are a lot of Tier-2, Tier-3 towns, we are yet to go there, towns like if you say Mathura, Bulandshahar, Saharanpur if you are familiar with these towns, they are Tier-2, Tier-3 towns in these regions. In entire UP states, there are a lot of towns down the pop strata. So, we want to get deeper into these places. I do not think it is something to do with the pricing, yes, I know the affordability factor would come in but we are fairly affordable brand, it is not that we are a premium, premium brand.

Moderator: Thank you. We will take the next question from the line of Nikunj Doshi from Bay Capital.

Nikunj Doshi: Just wanted to understand in terms of capabilities say local lab vis-à-vis regional players, vis-à-vis players like us, what is the capability difference in terms of tests to be carried out and what kind of business are we getting from the other labs in that sense?

Dr. Om P Manchanda: I think one key capability difference is that our ability to build scale. So, lot of these regional players or single unit player, they come under lot of top line growth because they do not know how to really build within their infrastructure and build scale. And that scale gives you huge advantage in terms of, obviously on one side you are building overheads structure because you have corporate structure but it also gives you advantage of lower cost of reagents, etc., So, I think that is one big capability difference because for us the entire market is open, we do not need patient, we need only patient sample and our ability to transport these samples, build collection network is one big difference compared to these local players. I think the other big difference is brand itself which is technically the entire

experience of turnaround time, quality or trust in the report, etc., all that when the brand becomes bigger and that is the real differentiator over all these smaller players. So, technically it boils down to two parameters which is quality and service.

Dr. Arvind Lal: And the third parameter, Nikunj, is that these smaller labs are not capable of carrying out the high-ended test, the most sophisticated test for which we are well known, so they cannot do those, so our is like a one stop shop, whereas the others are not and this also works to our advantage.

Nikunj Doshi: I just wanted to understand that aspect in greater depth, in terms of the number of test or in terms of percentage of revenue perspective, there will be tests which a regional lab or perhaps the local lab may not be able to do it and it will be perhaps be done at your end, so you would be sourcing lot of business from the regional labs or perhaps standalone labs, so just wanted to understand what percentage of business are we getting from such kind of high end tests which others are not able to do?

Dr. Om P Manchanda: Yes, so that is called institutional business of B2B, so one-third of our business comes from this channel which is outsourced by these guys to us which includes hospital labs, also includes smaller private independent labs.

Nikunj Doshi: Regional players would also be giving business to us or they have their own capability for such high-end test also?

Dr. Om P Manchanda: Yes, now they will also outsource, so there is no lab which will stay the entire test menu, there are only one or two central labs in the country which will do that.

Nikunj Doshi: Do we have pricing power there in such kind of environment or we still have to maintain some kind of competitiveness?

Dr. Om P Manchanda: Because lot of people are knocking the same door, pricing has to be competitive, but I think in this business pricing alone is not the real reason why somebody will outsource to you and most of these tests have sort of bearing on the diagnosis which is in a bit of gray zone, so quality is also an important aspect of this.

Nikunj Doshi: On data analytics side, what are the efforts that we are making and what can be done going forward?

Dr. Om P Manchanda: So, I think on data analytics a lot of discussions do take place but we are also acutely aware about some regulatory aspect of confidentiality, etc., So, as of now we are not into this monetizing data, so we do not do any of these things, it is completely with us. Whatever little bit internal analysis we do that but I do not think right now there is any plan till there is a clarity on the regulatory aspect.

- Nikunj Doshi:** But going forward, do you see that area emerging as a great opportunity for business like us?
- Dr. Om P Manchanda:** I am not too clear right now. First of all as of now my immediate response is, I doubt, because unless it is married to the other two dots which is pharmaceuticals as well as clinicians, you cannot really establish cause and effect. So, I think my reaction immediate would be as of now I am not too clear about it. There is also a layer of confidentiality and security, etc., So, we are staying away from this as of now.
- Moderator:** Thank you. We will take the next question from the line of Prashant Nair from Citigroup.
- Prashant Nair:** Just on the realization side, you mentioned part of this is mix related and partly the entry strategy in the East and then maybe some pricing. So, would the mix kind of normalize through the year or is the mix change also part of you having gone to a new market and the tests there are different or is it more to just do with the season?
- Dr. Om P Manchanda:** I think it is a new market as well because lot of volume growth is coming from rest of India where the realization is probably lower than North. So, I think it will probably remain to some extent right through future as well.
- Prashant Nair:** You are talking both in terms of the kind of test as well as the geographies from where you are getting your volumes and the former may normalize but the latter is likely to continue, is that a fair way of looking at it?
- Dr. Om P Manchanda:** Season is one but let us say everything else remaining the same, the revenue per patient will be impacted by the weightage from rest of India being higher than let us say from Delhi NCR.
- Moderator:** Thank you. We will take the next question from the line of Sameer Baisiwala from Morgan Stanley.
- Sameer Baisiwala:** Can you update us on your plans to deploy cash for M&A activities? I think you have been looking out for long but nothing has fructified.
- Dr. Om P Manchanda:** I think there are only two uses of cash; one is either we pay it off as dividend, other is we deploy into some businesses. So, our efforts on M&A continue and we believe that an industry like ours which is highly fragmented there is definitely a roadmap for inorganic growth, if nothing new, globally also one has seen that, efforts are on, we do not have anything specific to share but all we can say at this stage is that we are continuously putting efforts in this direction.
- Sameer Baisiwala:** You are not getting good candidates or is valuation of pricing is an issue?
- Dr. Om P Manchanda:** I think it is the quality of assets which is a bigger issue because we are a little bit finicky about the quality of business here.

- Sameer Baisiwala:** The second question is can you just talk a bit more about your expansion to South and West other than you mentioned about Bangalore and Pune clusters, what kind of effort you plan to put over next 12-18 months in terms of opening new clinical labs or any other infrastructure that you have in mind?
- Dr. Om P Manchanda:** I think it is a good question. Some good suggestion came from some of you guys in the last call as well. While we continue to try inorganic piece, it may be taking little bit of time. As a group, we will review this and probably look at going beyond Pune and Bangalore and see what we can do to aggressively focus on organic side as well. So, I think we are currently deliberating that. My sense is, given that we have now done East infrastructure, maybe focus has to now aggressively shift to south and west also. We will plan it out maybe next five, six months we will unfold our plan for South and West as well.
- Sameer Baisiwala:** Any thoughts on your digital efforts? Second is what kind of cost pressure are you seeing in the business?
- Dr. Om P Manchanda:** Great question. I think it has become very clear that technology has to become part of our DNA and we have been continuously investing behind this. As I mentioned earlier, we have created separate digital group. We need to do more of this and behavior of buying diagnostics online also one is seeing initial change in that. So, going forward we will have disproportionate investment in this area.
- We are using technology in many ways; right now it is more in the area of customer services and also in these health packages. We will definitely see that the proportion of digital investments and sales from online channel will grow as time goes.
- Sameer Baisiwala:** What more can you do? You are looking at payments and report keeping and all of that stuff or something beyond that?
- Dr. Om P Manchanda:** That is already happening, people can now download reports not only for immediate visits but even for previous visits, they can see graphical representation of various values, they can reach out to us through chatbot, get queries answered, they can pay online, they can book online, all that is happening, but I think the real stuff would be when we start getting leads from online sales. Then our whole channel of collection center shifts from offline to online model, so I think that is where we will see a big change and can probably integrate all the Phlebotomists through loosely called Uberization model, etc., I think that is where the big step jump would come, but there is some way to go there because in our business, quality is very-very important, it is not just the physical delivery of a product, here the integrity of the sample is very-very critical, so the customer experience is very important and so far we are managing the entire sort of value chain ourselves. Very little dependence is on the franchisee. The moment franchising of this collection through online channel happens and probably it will open up, but I get a sense that it will take little bit of time for us to standardize all the processes, but definitely digital online is here to stay.

On the cost pressure in the business, when we open labs, lab overheads actually add to the cost. To that extent we have been very efficient now in the last few quarters, we are improving our ratio from collection centers to labs. Other cost pressure has been the dollar which I think we have managed it very well, it has not impacted us that much, right. We have also renegotiated some rents. So, I think overall in all areas, so far as we have been saying we are not taking price increase, so we manage our cost very well without diluting the margins. So, we are hopeful that we will manage it for some more time.

Sameer Baisiwala: Employees and salaries?

Dr. Om P Manchanda: I think our last year increment was about 8-9%.

Bharath Uppiliappan: Our numbers reflect that our employee cost growth is lower than sales growth this quarter. So, we are fairly under control.

Dr. Om P Manchanda: It is not growing beyond top line growth. There is no deleveraging.

Moderator: Thank you. We will take the next question from the line of Dr. Harith Ahamed from Spark Capital.

Dr. Harith Ahamed: Can you give some sense of your collection center to lab ratio in different geographies maybe North and East, at the network level it is roughly 9 in FY18, so just trying to understand the difference between mature cluster and cluster that is ramping up?

Bharath Uppiliappan: We may not have region wise information to share but our efficiency ratio has gone up by about 30%-odd between Q4 FY17 to where we are now. So, our ratio has improved by 30%-odd is what I would like to say between collection center per lab to what it was in the past to what it is currently today.

Dr. Harith Ahamed: This is for the overall network?

Dr. Om P Manchanda: Overall network, yes.

Dr. Harith Ahamed: Second question is regarding volumes that come through your pick-up point network. How much lower is the pricing versus your typical B2C pricing or maybe what percentage of the price charged to the end customer or the patient is your share in volumes that come through the pickup point network?

Dr. Om P Manchanda: First of all, I think the profile of test that we get through pick up point is very different from what we get through B2C. So, it may not be a straight like-to-like comparison but let us say assuming there is a test which we sell through pick up point versus B2C, if B2C is 100, then pick up would be close to 65.

- Moderator:** Thank you. We will take the next question from the line of Bharat Celly from Equirus Securities.
- Bharat Celly:** Our realizations have come down by almost 4-5% but our gross margins have stood up sequentially as well as year-on-year. So, what is the reading there?
- Dr. Om P Manchanda:** I think reagent cost as a percentage of total is very low and many of these promotion stuff that we talked about, they are test like glucose and consumption cost is very low there. So, that is why it is not impacting gross margin that much.
- Bharat Celly:** When we talk that we are focusing on Bangalore and Pune for the West and South zones, so just wanted to understand what exactly we are trying to do there to get higher market share over there?
- Dr. Om P Manchanda:** Technically, we are just trying to make the brand more visible; we are increasing especially in Bangalore because it is a little bit of IT savvy city, we are trying to do home collections and digital initiatives. So, it is basically that sort of activities which are very B2C activities.
- Bharat Celly:** What has been the growth over there let us say this quarter?
- Dr. Om P Manchanda:** So, we would like to restrain in sharing those numbers right now.
- Moderator:** Thank you. We will take the next question from the line of Tushar Manudhane from Motilal Oswal Securities.
- Tushar Manudhane:** Just with respect to this price rationalization which has also impacted the realization year-on-year as well as quarter-on-quarter, just to understand is this for some set of tests and in some particular region where you have taken this price cuts?
- Dr. Om P Manchanda:** Yes.
- Tushar Manudhane:** So, is this like a response to the industry or this is on the proactive basis?
- Dr. Om P Manchanda:** No, actually we are basically trying to simplify pricing structure in our system.
- Tushar Manudhane:** So, industry has not?
- Dr. Om P Manchanda:** No, we are not targeting any competitor or something. We operate in a very unorganized set up. So, each lab is having its own pricing structure. So, as you expand it tends to become a barrier to scale if you are too customised. So, we are just trying to simplify this and in some places you lose, some places you gain, net-net effect we lost little bit and we are seeing favorable volume impact. So, that is what we are trying to do. I do not think it is a response to competition.

- Tushar Manudhane:** This is fully reflected in this quarter or there is some impact to come in the coming quarters?
- Dr. Om P Manchanda:** I think it is pretty much settled.
- Moderator:** Thank you. We will take the next question from the line of Imran Khan from Ratnatraya Capital.
- Imran Khan:** In the last 1.5 years, we have added some 400 patient service centers. So, can you please guide us on this for the future?
- Dr. Om P Manchanda:** So, on an average, this translates to about 15%-odd of our infrastructure which will continue to grow and that will keep coming from this collection center network.
- Imran Khan:** If you can share this, what percentage of our new PSC's got converted from non-national players i.e. regional players or let us say pathology labs to our brand basically?
- Bharath Uppiliappan:** As a policy, we do not encourage labs to take on our collection centres, we prefer for them to be standalone retail spaces.
- Imran Khan:** What I actually mean is, there are one or two centers who collect the samples and then send it to some bigger regional labs, I am asking about the touch points converted to our brand.
- Dr. Om P Manchanda:** Many of these regional players do not operate through a collection center network. So, technically they are all new centers which we would make, they are not posh guys.
- Moderator:** Thank you. We will take the next question from the line of Shaleen Kumar from UBS Securities.
- Shaleen Kumar:** Any update on this pricing cap list of essential tests which we were hearing like two quarters back from the Government or Government agency?
- Dr. Om P Manchanda:** We never heard it from the Government agencies, it was only what we picked up in the media but there is no update on that.
- Shaleen Kumar:** So, you do not see any upcoming risk on that front?
- Dr. Om P Manchanda:** That risk will always exist, so I do not think I can say yes or no for that because your knowledge is as good as mine as of now. So, we do not have any formal communication on that. That is something I can share with you.
- Moderator:** Thank you. We will take the next question from the line of Sriraam Rathi from ICICI Securities.

- Sriraam Rathi:** How had been the flu season this quarter and what would have been the impact on the volume and value growth?
- Dr. Om P Manchanda:** It is quite subdued compared to earlier years. I think it is a fairly good news because we are not dependent on seasonal spikes at least this year.
- Sriraam Rathi:** So, the volume and value would have been lower than the last year in this quarter particularly for flu related?
- Dr. Om P Manchanda:** Yes, I am not playing that up, but actually contribution from seasonal flu is much less this year than what one has seen in the past. But last quarter also had favorable base as well, because lot of festivals were in Q2, this time they are in Q3, so it is bit offset by that as well.
- Moderator:** Thank you. Ladies and Gentlemen, that was the last question for today. I would now like to hand the conference over to the management for their closing comments.
- Dr. Om P Manchanda:** Thank you very much for joining us today on this call and on behalf of Dr. Lal PathLabs, I wish you and your family a very Happy Diwali and we will talk to you next year in February.
- Dr. Arvind Lal:** Thank you.
- Ved P Goel:** Thank you.
- Moderator:** Thank you very much. Ladies and Gentlemen, on behalf of Dr. Lal PathLabs, we conclude today's conference. Thank you for joining. You may disconnect the lines now.

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