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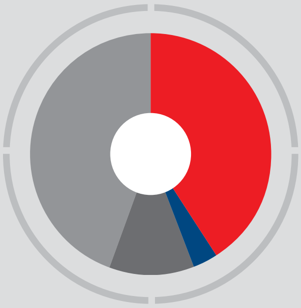
Medplus Health Services Ltd.

CMP: Rs 1,032	Rating: BUY	Target: Rs 1,320

Company Information

BSE Code	543427
NSE Code	MEDPLUS
Bloomberg Code	MEDPLUS IN
ISIN	INE804L01022
Market Cap (Rs. Cr)	12,340
Outstanding shares(Cr)	11.93
52-wk Hi/Lo (Rs.)	1143.10/993.35
Avg. daily volume (1yr. on NSE)	6,276,730
Face Value(Rs.)	2
Book Value (Rs)	131

Shareholding Pattern as on 20 Dec'2021



Company overview

Medplus Health Services Limited ("Medplus") is the 2nd largest pharmacy retailer in India, in terms of (i) revenue from operations for the financial year 2021, and (ii) number of stores as of March 31, 2021. Medplus offers a wide range of products, including (i) pharmaceutical and wellness products, including medicines, vitamins, medical devices and test kits, and (ii) fast-moving consumer goods, such as home and personal care products, including toiletries, baby care products, soaps and detergents, and sanitizers. Medplus has 3 manufacturing plants in Telangana, manufacturing range of plastic products, optical frames, spectacles and liquid disinfectants etc. Medplus holds strong market share in Chennai, Bangalore, Hyderabad and Kolkata of approximately 30%, 29%, 30% and 22%, respectively in organized pharmacy retail market. As of Sep'21, the company operated 2326 stores across Karnataka (546), Tamil Nadu (475), Telangana (474), Andhra Pradesh (297), West Bengal (224), Maharashtra (221) and Odisha (89). In 2020 company started focusing on online sales, by virtue of which company was able to deliver their online purchases customers within 2 hours of purchase in select cities of Hyderabad, Bangalore, Kolkata, Pune and Nagpur. Medplus employs a data analytics driven cluster-based approach to their store network expansion. A strong omni channel platform (store, website, app, telephone ordering, order online, pick physically) which enables it to leverage the strong offline presence to establish and grow its online channel.

Investment Rationale

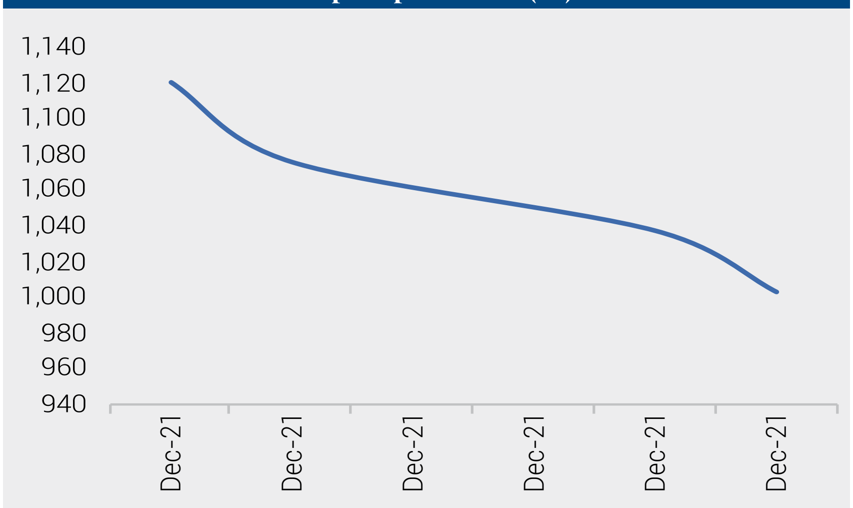
Medplus major beneficiary of increasing share for E-commerce channel

While traditional retail channels continue to constitute mammoth share (89% as of FY21) of pharmacy retail market in India, there has been a recent shift towards modern retail channels such as e-commerce and brick & mortar (B&M). The share of the modern retail (e-commerce and B&M) is expected to inch higher on the back of 27% CAGR between FY21 and FY25 vs 8% for traditional channel. Courtesy of high growth, traditional retail channels' share is expected to come down to 80% by FY25. Within modern retail, e-commerce (together with omni-retail channel) is expected to grow at a robust CAGR of 42% between the same period. The shift is expected to be driven by change in consumer perception who are now inclined to purchase regular prescription drugs and other wellness products from modern organized pharmacy retail outlets that offer the benefit of an enhanced retail environment, the assurance of authentic drugs, transparent discounts and a wide variety of products. This trend has been further accelerated by the outbreak of the COVID-19 pandemic. Medplus with (i) well-established brand, (ii) genuine and good quality pharmaceutical products offering, (iii) wide product offering, (iv) ability to achieve high fulfilment rates, (v) offering of neighbourhood convenience with large store footprint, and (vi) ability to offer competitive pricing to the customers, is likely to continue the gains in market share. The company was the first to operate as an omni channel platform and wants to further increase online sales revenue contribution to total revenues leveraging store expansion and faster delivery. Over the last two years, revenue from online sales channel has steadily increased and for the financial years 2020 and 2021 and the six months ended September 30, 2021 accounted for 6.99%, 8.98%, and 8.44% of total revenue from operations, respectively.

Apt store expansion with improving per store dynamics from matured stores

Medplus streamlined and methodical store opening process along with focus on the sustainability and profitability of each store, has allowed company to maintain healthy store level economics. Between FY19-21, Medplus opened new stores at a CAGR of more than 12% and as of FY21, 53% of the stores are located in Metro cities, 26% in Tier-1, 17% in Tier 2 and only 4% in Tier 3, hence there is immense scope of growth. Medplus has a higher average revenue per store of Rs 1.59 cr being more present in metro and tier 1 cities. Medplus employs a data analytics driven cluster-based approach to store network expansion, whereby the company first achieve high store density in a densely-populated residential area within a target city before expanding store network in the surrounding areas within that city, followed by expansion into other adjacent cities. Hence, it has higher store concentration in Chennai, Bangalore, Hyderabad and Kolkata. Medplus' typical store comprises of 550 to 600 square feet with capex of Rs 0.60 million. Moreover, over 95% of company's stores are operated and managed exclusively by the company thus bearing the capex. As of FY21, over 60% and 75% of the new stores achieved a positive store level operating EBITDA within the first three months and first six months of operations, respectively. Further, as of H2FY22, the mature stores had a median payback period of less than 3 years and demonstrated a compounded average same store sales growth of 8.3% on MRP from FY19 to FY21. As of September 30, 2021, Medplus store network comprised of 2,326 stores, of which 55.25% of the total number of stores have been opened since FY18. The company has an operating EBITDA margin of 5.74% as of Sep'21 while the store level operating EBITDA margin stands at 10.26%. More importantly, store level operating EBITDA margin for matured stores stands at 11.58% vs 8.59% for non-matured stores as of Sep'21. Hence, there is likelihood of increased contribution from such stores as they mature and gradually achieve higher growth rates and improved profitability.

Medplus price chart (Rs)



Fully integrated across value chain driven by inhouse technology

Medplus' business operations across the entire value chain are backward integrated and are wholly-managed and operated by the company. Company's entire business value chain, from sourcing of products, to warehousing, to distribution to stores, to store operations and interfacing with customers, and to last mile delivery, is supported by integrated technology infrastructure, which has been developed in-house. As of September 30, 2021, company has 18 primary warehouses in total with each in Bangalore, Chennai, Hyderabad, Vijayawada, Kolkata, Pune, Bhubaneshwar, Mumbai and Nagpur. These warehouses are supported by smaller warehouses in cities where Medplus has higher store density. These technologically enabled warehouses form hubs for company's stores, and stores' inventories are replenished through centralized inventory management system, which is capable of tracking the sales and inventory levels at stores and warehouses in real-time. Company's supply chain is supported by an algorithm driven automated replenishment and stock picking system that is driven by a real time inventory analytics platform, which again has been developed in-house and refined over the last ten years. The company aims to enhance its delivery infrastructure and achieve a higher rate of online delivery purchases by reaching customers within two hours. The 2-hour delivery services were started in FY21, and recent pilots in July 2021 have showed promising results where 93% of online delivery purchases were delivered within two hours in select micro-markets of Hyderabad. The company expects to expand its ability to deliver online purchases within two hours of purchase in big cities such as Mumbai by December 31, 2021.

Increase in share of private label products will lead to improvement in profit margins

For FY21 and H1FY22, Medplus' product mix primarily comprised of branded pharmaceutical products (76.8% and 74.9%, respectively), private label pharmaceutical products (5.6% and 6.7%, respectively), branded fast-moving consumer goods (12.9% and 11.6%, respectively) and private label consumer goods (4.8% and 6.9%, respectively). Percentage of store revenues from private label pharmaceutical products and private label consumer goods together have increased from 4.48% in FY19 to 10.36% in FY21 and further to 13.54% in H1FY22. This has helped to improve gross margins from 18.86% in FY19 to 21.02% in FY21 and further to 21.3% in H1FY22. Company has stated that 1% increase in private label share will increase the margins by 0.5%. Company intends to (i) increase the penetration of private label pharmaceutical products by introducing private label products for more therapeutic areas, in particular for sub-chronic and chronic ailments and (ii) introduce new private label products for FMCG in particular, in the consumer categories of nutrition and wellness. Besides, the company also plans to spend on advertising for private label products and train staff to push for more private label products particularly for stores where share of revenue is less from private label products. Besides, Medplus aims to keep a tight control over costs through inhouse management of all supply chain and infrastructure and logistics and also has inhouse technology team. Besides, pharmaceutical products are also procured directly from pharmaceutical companies or their carry forward agents, which helps to keep costs under check. Besides, as store matures, albeit absolute costs increase, as % of revenue, store EBITDA margins improve. On financial front, during FY19-21, Medplus' revenue and EBITDA grew at a CAGR of 16.2% (to Rs. 3069 cr) and 34.9% (to Rs. 217), respectively, while PAT grew at a CAGR of 130% to Rs. 63 cr. EBITDA margins improved by 182bps to 7.1%, while PAT margins improved by 153bps to 2.1%. EBITDA and PAT margins have further increased to 8.4% and 3.5% respectively in H1FY22.

Key risks

- Increase in competitive intensity from online players
- Delay in EBITDA break-even at new stores

Valuation

Medplus Health Services Limited ("Medplus") is the 2nd largest pharmacy retailer in India, in terms of (i) revenue from operations for the financial year 2021, and (ii) number of stores as of March 31, 2021. The share of the modern retail (e-commerce and B&M) is expected to inch higher to 20% vs (11% as of FY21) driven by 27% CAGR between FY21 and FY25 vs 8% for traditional channel. Medplus has been growing its stores at a CAGR of more than 12% and presently holds 2326 stores. 53% of the stores are located in Metro cities, 26% in Tier-1, 17% in Tier 2 and only 4% in Tier 3, hence there is immense scope of growth. Medplus has a higher average revenue per store of Rs 1.59 cr being more present in metro and tier 1 cities. Medplus employs a data analytics driven cluster-based approach to store network expansion, whereby the company first achieve high store density in a densely-populated residential area within a target city before expanding store network in the surrounding areas within that city, followed by expansion into other adjacent cities. Hence, it has higher store concentration in Chennai, Bangalore, Hyderabad and Kolkata. Moreover, over 95% of company's stores are operated and managed exclusively by the company and 55.25% of the total number of stores have been opened since FY18 and hence are not matured. Store level operating EBITDA margin for matured stores stands at 11.58% vs 8.59% for non-matured stores as of Sep'21. Hence, there is likelihood of increased contribution from such stores as they mature and gradually achieve higher growth rates and improved profitability. Besides, the company has been gradually increasing share of private label products from 4.48% in FY19 to 10.36% in FY21 and further to 13.54% in H1FY22. This has helped to improve gross margins from 18.86% in FY19 to 21.02% in FY21 and further to 21.3% in H1FY22. Company has stated that 1% increase in private label share will increase the margins by 0.5%. Company's entire business value chain, from sourcing of products, to warehousing, to distribution to stores, to store operations and interfacing with customers, and to last mile delivery, is supported by integrated technology infrastructure, which has been developed in-house. These strategies helped the company to contain costs and as more stores matures and the company exploits economies of scale, EBITDA margins will expand. Medplus also sources pharmaceutical products directly from pharmaceutical companies or their carry forward agents, which helps to keep costs under check. Thus, given industry dynamics and company positioning, we expect Medplus to reap benefits from this shift towards modern retail. At the CMP, the scrip trades at EV/EBITDA of 34.16x FY23E EBITDA. Investors are advised to 'BUY' the scrip for a target price of Rs 1320 at a target EV/EBITDA of 42x FY23E EBITDA.

Particulars (in Rs Cr)	FY20	FY21	FY22E	FY23E
Revenue	2,871	3,069	3,888	4,570
Growth (%)	26%	7%	27%	18%
EBITDA	134	217	307	370
EBITDA Margin (%)	4.7%	7.1%	7.9%	8.1%
Net Profit	2	63	113	142
Net Profit Margin (%)	0.1%	2.1%	2.9%	3.1%
EPS (Rs)	0.2	5.3	9.5	11.9

Source: Ashika Research

Ashika Stock Broking Ltd.

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