

Medplus Health Services Ltd

Recommendation	Subscribe for Long Term		BACKGROUND				
Price Band	Rs 780-796		Company Overview				
Bidding Date	13-15 December		Medplus Health Service Ltd. (Medplus) is the second largest pharmacy retailer in India, in terms of (i) revenue from operations for the FY21, and (ii) number of stores as of March 31, 2021. The company offers a wide range of products, including (i) pharmaceutical and wellness products, 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. The company was founded in 2006 by Gangadi Madhukar Reddy to reduce the problem of fake medicines in the system.				
Book Running Lead Manager	Axis, Credit Suisse, Edelweiss, Normura		Medplus has maintained a strong focus on scaling up its store network, having grown from operating the initial 48 stores in Hyderabad at the conception of the business to operating India's second largest pharmacy retail network of over 2,000 stores distributed across Tamil Nadu, Andhra Pradesh, Telangana, Karnataka, Odisha, West Bengal and Maharashtra.				
Registrar	KFintech		Objects of the Issue				
Sector	Pharmacy		The issue of Rs 1398 cr includes offer for sale of Rs 793 cr and Rs 600 cr fresh issue which would be utilized for investment into its material subsidiary, Optival for funding working capital requirements				
Minimum Retail Application – Details at Cut off Price							
Number of Shares	18		Investment Rationale				
Application Money	14328		<ul style="list-style-type: none"> Established Brand and Value Proposition to Customers Omni-Channel Model Cluster Based Expansion Increased share of Private Labels Continued Improvement in Operational Efficiency 				
Discount to retail	NIL		Valuation and Recommendation				
Payment Mode	ASBA, UPI		The company has been opening stores at CAGR of 12% since FY10 which has skewed towards the end of the decade at 17.2% between FY20-1HFY22. However, due to increased leverage on account of omni-channel and higher share of private label sales, profitability has grown at much higher rate. Gross margins have grown at a CAGR of 22.7% between FY19 to FY21 and EBITDA at 63.2% during the same period. The cluster-based strategy gives higher penetration in the selected regions. We believe that Medplus is a well-established brand among its clusters and has positioned itself as a genuine and good quality pharmaceutical products supplier through its omni-channels, which will continue to drive its gains in market share. We recommend "Subscribe for Long Term" .				
Consolidated Financials (Rs Cr)	FY20	FY21	Financial Snapshot				
Total Income	2,871	3,069	FY19	FY20	FY21	H2FY22	
EBITDA	166	217	Revenues	2273	2871	3069	1880
PAT	2	63	%growth			7%	29%
Valuations*	Lower Band	Upper Band	EBIDTA	119	166	217	159
Market Cap (Rs cr)	9305	9496	% Margins	5.2%	5.8%	7.1%	8.4%
EPS	5.3	5.3	Adj. PAT	12	2	63	66
BV/share	61	61	EV/EBIDTA @ Rs 796			43.9	29.8
P/BV	12.7	13.0	PE @ Rs 796			150.5	71.5
PE	147.4	150.5	P/BV @ Rs 796			13.0	11.9
*FY21 numbers, diluted equity							
Post Issue Shareholding Pattern							
Promoters	40.4%						
Public	59.6%						
Offer structure for different categories							
QIB (Including Mutual Fund)	50%						
Non-Institutional	15%						
Retail	35%						
Post Issue Equity Capital (Rs cr)	23.9						
Issue Size (Rs cr)	1370-1398						
Face Value (Rs)	2						
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*Annualised							



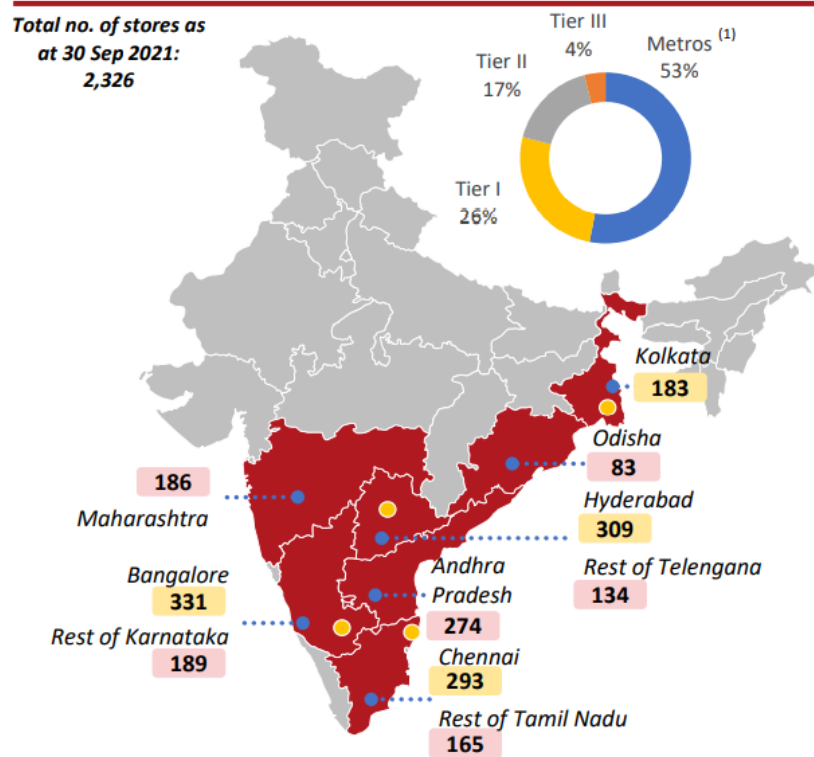
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Company Overview

Medplus Health Service Ltd. (Medplus) is the second largest pharmacy retailer in India, in terms of (i) revenue from operations for the FY21, and (ii) number of stores as of March 31, 2021. The company offers a wide range of products, including (i) pharmaceutical and wellness products, 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. The company was founded in 2006 by Gangadi Madhukar Reddy to reduce the problem of fake medicines in the system.

Medplus has maintained a strong focus on scaling up its store network, having grown from operating the initial 48 stores in Hyderabad at the conception of the business to operating India's second largest pharmacy retail network of over 2,000 stores distributed across Tamil Nadu, Andhra Pradesh, Telangana, Karnataka, Odisha, West Bengal and Maharashtra, as of March 31, 2021

Present in seven states in India, evenly distributed across metros and other cities



It is the first pharmacy retailer in India to offer an omni-channel platform. The customers of the company have multiple options to transact, including (a) purchasing products at one of the stores, or (b) placing an order through a telephone call to receive delivery of their purchased products, or (c) placing an order online to receive delivery of their purchased products, or (d) "Click and Pick", by placing an order online and picking up their purchased products from one of the stores. The business operations across the entire value chain are backward integrated and are wholly-managed and operated by the company. The entire business value chain, from sourcing of products, to warehousing, distribution to stores, store operations, interfacing with customers, and to last mile delivery, is supported by the integrated technology infrastructure, which Medplus has developed in-house.



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Investment Rationale

Established Brand and Value Proposition to Customers

Medplus is the second largest pharmacy retailer in India, in terms of (i) revenue from operations, and (ii) number of stores as of March 31, 2021. It operates 2,326 stores distributed across Tamil Nadu, Andhra Pradesh, Telangana, Karnataka, Odisha, West Bengal and Maharashtra. “MedPlus” brand has a history and track record of over 15 years, and has been positioned to stand for genuine and good quality pharmaceutical products that are offered at affordable prices.

Value Pricing – Mr Reddy started the company with an objective to cut inefficiencies in the supply chain using technology to deliver better value to the customers. Over a period of time, as the company has built scale, it has continued to further reduce its costs that has allowed it to deliver more value to customer in the form of discounts that have increased from up to 10% to up to 20%. The stores present a consistent and uniform customer experience of offering genuine and good quality pharmaceutical products and fast-moving consumer goods at affordable prices.

Average Order Value (excl. GST)	Discounts on Pharma Products	Discounts on FMCG Products ⁽⁴⁾
> INR 1000	Upto 20% ⁽³⁾	Upto 5%
INR 200 -1000	Upto 10%	Upto 5%
< INR 200 ⁽⁵⁾	0%	0%

Omni-Channel Model

Medplus is the first pharmacy retailer in India to offer an omni-channel platform, according to the Technopak Report. Commencing in 2015, the customers could either visit the stores or access the offerings online, through its website and mobile application. The customers have multiple options, including (i) purchasing products at one of the stores, or (ii) placing an order through a telephone call to receive delivery of their purchased products, or (iii) placing an order online to receive delivery of their purchased products, or (iv) “Click and Pick”, by placing an order online and picking up their purchased products from one of the stores.

The omni-channel proposition of the company leverages its existing store networks and supply chain and distribution network to offer a differentiated offering to the customers. It allows it to (i) deepen and extend the customer reach from, and expand the total addressable market for, each of the stores, (ii) further enhance “convenience” as one of its core customer value propositions, (iii) lower incremental cost of operations for online deliveries (as the stores act as branding sites and lower cost of online customer acquisition), and (iv) retain offline and online customers within its customer ecosystem.

Cluster Based Expansion

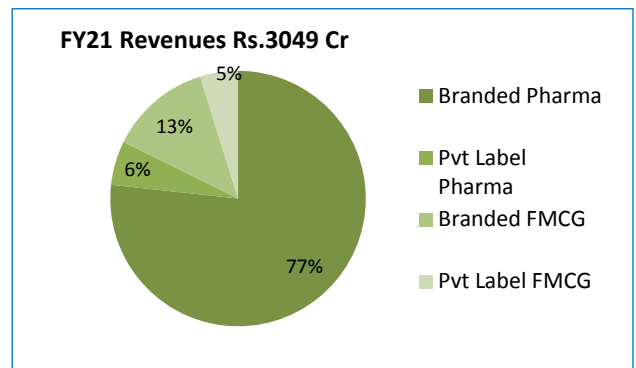
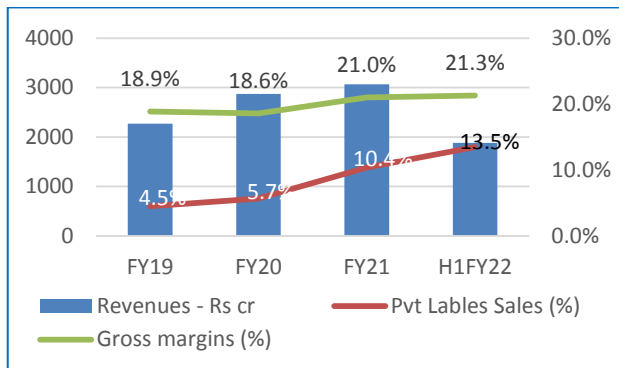
The company employs a data analytics driven cluster-based approach to its store network expansion, whereby it first achieves high store density in a densely-populated residential area within a target city before expanding the store network in the surrounding areas within that city, followed by expansion into other adjacent cities. This approach allows the company to (i) create brand visibility within the cities where they operate, through focused implementation of marketing and advertising initiatives, (ii) increase its market share in the cities where it operates, (iii) replicate the growth model in adjacent underserved cities and towns, as it develops its presence in those clusters, and (iv) generate cost efficiencies due to operating leverage achieved in the supply chain and inventory management. The cluster-based

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expansion approach and replicable store roll-out strategy have allowed Medplus to achieve and maintain attractive and healthy store level economics. **The company is looking to enter into one to two new states every year.**

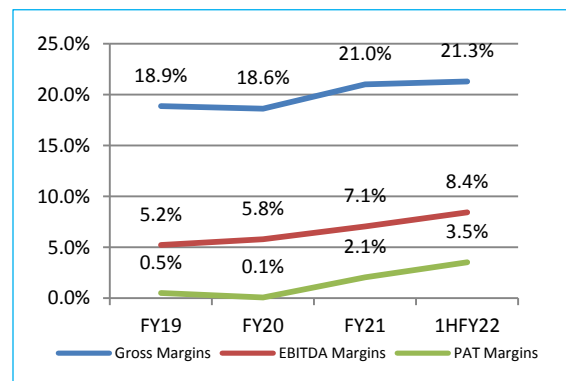
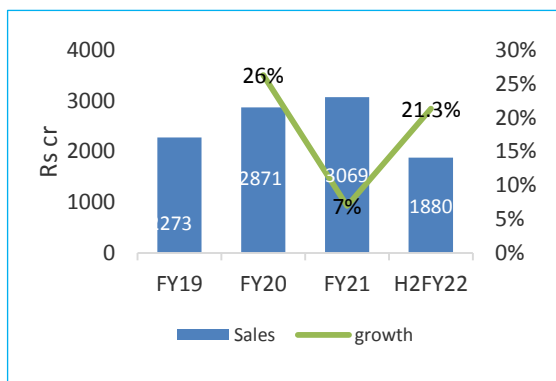
Increased share of Private Labels

The company generally derives higher gross margins from sales of private label products and aims to increase the range of private label products. Due to the scale of purchases, the company is less constrained by minimum order quantity requirements imposed by suppliers which in turn, allow it to offer a wider range of private label products to its customers.



Continued Improvement in Operational Efficiency

The company is continuously improving its supply chain and distribution infrastructure to increase its operating efficiency and to enhance the supply chain management. With omni-channel leverage, the company is able to increase profitability. Further, to increase operating efficiency, the company is planning to increase automation at the warehouses, for processes such as sorting, labelling and packaging. It also plan to increase the proportion of the product procurement conducted directly through pharmaceutical companies or their carry forward agents, as it is expected to increase the gross margins.



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Risks and Concerns

1. **Pledging by one of the promoter companies:** One of the corporate promoters, Lone Furrow had pledged 1,676,418 Series B2 CCPS held by it in favour of Zash Traders aggregating to 7.64% of the pre-Offer equity share capital of the Company, on a fully diluted basis which have since been converted into 8,543,340 Equity Shares.
2. **Higher competition:** The COVID-19 pandemic has changed consumer behaviours and accelerated the advancement of disruptive technologies that has resulted in a significant increase in e-commerce competition. Disruptive innovation by existing or new competitors potentially in the nature of a more user-friendly, innovative online channel or other such sales channel could significantly alter the competitive landscape in the future.

Valuation and Recommendation

India's pharmacy retail market is expected to grow at a CAGR of approximately 11% between FY21 to FY25, from Rs 1,81,125 cr to Rs 2,72,500 cr, in terms of revenue. According to the Technopak Report, the organized pharmacy retail market's share of India's pharmacy retail market, in terms of revenue, increased from approximately 5% in the FY15 to approximately 11% for the FY21. The organized pharmacy retail market is expected to grow at a CAGR of approximately 27% between FY21 to FY25, from Rs 20,475 cr to Rs 53,500 cr, in terms of revenue, primarily through a combination of structural growth in underlying market and gaining market share from the unorganized pharmacy retailers.

The company has been opening stores at CAGR of 12% since FY10 which has skewed towards the end of the decade at 17.2% between FY20-1HFY22. However, due to increased leverage on account of omni-channel and higher share of private label sales, profitability has grown at much higher rate. Gross margins have grown at a CAGR of 22.7% between FY19 to FY21 and EBITDA at 63.2% during the same period. The cluster-based strategy gives higher penetration in the selected regions.

In organized segment, Apollo Pharmacy is the largest player however it is part of Apollo Hospitals and separate numbers are not available. There is no other pure play pharmacy listed hence it is not possible to compare Medplus with peers.

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FINANCIALS

P&L (Rs. Cr)	FY19	FY20	FY21	H2FY22	H2FY21	Balance Sheet (Rs. Cr)	FY19	FY20	FY21	H2FY22	H2FY21
Net Revenue	2,273	2,871	3,069	1,880	1,463	Share Capital	0	0	0	6	0
% Growth		26%	7%	29%		Reserve & Surplus	291	528	730	795	590
COGS	1,844	2,337	2,424	1,479	1,144	Non Controlling Int	0	1	1	0	1
GM %	18.9%	18.6%	21.0%	21.3%	21.8%	Networth	291	529	731	801	591
Employee Cost	211	272	339	180	180	Total Loans	104	105	135	57	86
% of Revenues	9.3%	9.5%	11.0%	9.6%	12.3%	Lease Liabilities	324	372	455	544	405
Other expenses	98	96	90	62	40	Trade payable	158	234	148	224	181
% of Revenues	4.3%	3.3%	2.9%	3.3%	2.8%	Other Current Liab	61	73	58	84	82
EBITDA	119	166	217	159	98	Total provisions	20	35	38	36	39
EBITDA Margin	5.2%	5.8%	7.1%	8.4%	6.7%	Total Current Liab.	239	342	244	344	303
						Total Equity & Liab.	959	1,349	1,566	1,746	1,385
Depreciation	59	75	88	55	42	Fixed Assets & CWIP	48	67	97	120	68
Other Income	12	17	22	11	8	Right of use assets	288	316	385	464	339
Interest	50	47	55	31	27	Goodwill	41	41	41	41	41
						Deferred Tax Assets	50	40	39	41	39
Exceptional gain	-	(32)	-	-	-	Other non Curr. assets	60	68	81	91	69
PBT	23	29	95	84	37	Cash	50	141	119	96	72
Tax	11	28	32	17	15	Inventories	394	644	750	810	685
Tax rate	48%	94%	34%	21%	40%	Debtors	9	6	5	7	4
PAT	12	2	63	66	22	Other Current assets	18	25	49	74	67
% Growth						Total Assets	959	1,349	1,566	1,746	1,385
EPS (Post Issue)	1.0	0.2	5.3	5.6	1.9	Cash Flow (Rs. Cr)	FY19	FY20	FY21	H2FY22	H2FY21
Performance Ratios	FY19	FY20	FY21	H2FY22	H2FY21	EBITDA	119	166	217	159	98
EBITDA Margin (%)	5.2%	5.8%	7.1%	8.4%	6.7%	Provisions & Others	21	19	56	15	52
PAT Margin (%)	0.5%	0.1%	2.1%	3.5%	1.5%	Op. profit before WC	140	185	273	174	150
ROE (%)	4.1%	0.3%	8.6%	16.6%	7.5%	Change in WC	19	(176)	(241)	(1)	(136)
ROCE (%)	18.4%	12.0%	17.3%	26.8%	19.0%	Less: Tax	(13)	(15)	(29)	(16)	(9)
Net D/E (x)	0.2	-0.1	0.0	0.0	0.0	CF from operations	147	(7)	3	157	6
Turnover Ratios	FY19	FY20	FY21	H2FY22	H2FY21	Addition to assets	(22)	(30)	(54)	(42)	(10)
Debtors Days	1	1	1	1	1	(Purchase)/Sale of invst.	(1)	(3)	15	(59)	(3)
Inventory Days	62	81	88	78	84	Div/Int Received	4	5	4	2	2
Creditor Days	25	29	17	21	22	CF from Investing	(19)	(28)	(35)	(99)	(11)
Asset Turnover (x)	5.7	4.5	3.5	4.4	4.3	Loans	(69)	(108)	(95)	(58)	(43)
Valuation Ratios	FY19	FY20	FY21	H2FY22	H2FY21	CCPS	-	204	98	-	-
Price/Earnings (x)			150.5	71.5	213.2	Interest paid	(14)	(7)	(8)	(3)	(5)
EV/EBITDA (x)		57.0	43.9	29.8	48.4	Equity	-	1	-	0	-
Price/BV (x)			13.0	11.9	16.1	CF from Financing	(83)	90	(6)	(61)	(48)
Mkt cap/Sales (x)			3.1	2.5	3.2	Net Change in cash	45	56	(37)	(3)	(53)
EV/Sales (x)			3.1	2.5	3.3	Cash at beginning	(91)	(47)	9	(28)	9
						Exchange difference					
						Cash at end	(47)	9	(28)	(31)	(45)

Source: Company Data, NBRR

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