Zydus Foundation

August 28, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Non-convertible debentures	145.00 (Reduced from 160.00)	CARE A-; Stable	Revised from CARE BBB+; Stable

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

The revision in the rating assigned to the non-convertible debenture (NCD) issue of Zydus Foundation (ZF) factors in strengthening of its business risk profile as reflected by significant growth in the total operating income (TOI), profitability and cash accruals during FY23 (refers to the period April 1 to March 31) backed by continued high enrolment ratio along with rationalisation of employee cost on a larger student base. The revision in the rating also takes into account better-than-envisaged profitability in FY23 which is also expected to remain better than the earlier envisaged level in FY24 followed by introduction of post-graduation course (Doctor of Medicine; MD). With higher-than-envisaged profitability and cash accruals, the company prepaid the NCDs amounting to ₹40 crore in FY23.

The rating continues to derive strength from its strong parentage of Zydus Lifesciences Limited (ZLL; previously known as Cadila Healthcare Limited) by virtue of being its wholly-owned subsidiary. CARE ratings Limited (CARE Ratings) observes that majority of ZLL's corporate social responsibility (CSR) spend is being done through ZF and expects the same to continue. The rating also suitably factors in ZLL's need-based support to ZF as a parent, since it is strategically important to the Zydus Cadila group which already has vast experience in the pharmaceutical and healthcare sectors. Through ZF, the group has forayed into the field of medical college. The rating also favourably factors in completion of capex for building a new super-speciality hospital-cum-medical college, benefits available under various government schemes for its hospital and good growth prospects for the higher education sector.

The rating of ZF, however, remains constrained on account of the upcoming large schedule bullet repayment of NCDs of ₹145 crore (due in March 2025); thereby expected to require reliance on the Zydus Cadila group for its servicing. The rating is further constrained on account of the limited track record of operation of the existing medical college and susceptibility to regulatory changes in the higher education and healthcare sectors. CARE Ratings also takes cognisance of the on-going Public Interest Litigation (PIL) filed against ZLL in the Honourable Gujarat High Court wherein the Court has asked ZLL not to charge any fees from patients for medical treatment until the case is disposed-off. Furthermore, CARE Ratings takes note of ZF's formation under Section 8 of the Companies Act, 2013 with the objective of promotion of education, research or charity; and profit, if any, is to be utilised for promoting these objectives thereby limiting net surplus and cash flow.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Self-sustainable generation of sufficient cash flows for meeting ZF's debt servicing requirements without any reliance on group support.
- Significant improvement in its debt coverage indicators.

Negative factors

- Material reduction in enrolment of students with sharp decline in income on a sustained basis.
- Any change in the extent of shareholding of the parent (ZLL) or deterioration in the credit profile of ZLL or lower-than-envisaged support from ZLL/ Zydus Cadila group.

Analytical approach: Standalone along with factoring managerial and financial linkages with its parent, ZLL. On account of having a strong credit risk profile, ZLL is capable of providing need-based support to ZF in a timely manner. Furthermore, the management of ZLL has also strongly articulated their willingness to extend any need-based support to ZF.

Outlook: Stable

CARE Ratings believes that ZF shall continue to benefit from its strengthening infrastructure leading to steady growth in student enrolment while it shall continue to receive need-based support from the Zydus Cadila group.

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

Detailed description of the key rating drivers

Key strengths

Strengthening of business risk profile

The company posted its first-ever net profit during FY23 which remained significantly better than envisaged. During FY23, the company earned strong operating profit of ₹31.51 crore as compared with ₹6.27 crore in FY22, mainly due to increase in college fee income on account of continuous increase in the number of students along with rationalisation of employee cost on a larger student base and improvement in bed occupancy at the hospital. As against its aggressive hiring plan, the company had been able to manage its operations efficiently by optimising the hiring process, to fill the vacancies for the position of teachers & para medical staff. With higher-than-envisaged profitability, the company has prepaid the NCDs of ₹40 crore in FY23. Furthermore, CARE Ratings expects the company to improve its operating profitability during FY24-FY26 with introduction of post graduate course (MD). The company has received requisite approvals from Medical Council of India (MCI) and All India Council for Technical Education (AICTE) to introduce post-graduation course with its first academic year starting from 2023-2024.

Strong parentage of ZLL providing financial flexibility

ZF is a 100% subsidiary of ZLL, the flagship company of the Zydus Cadila group. ZLL is the fifth-largest pharmaceutical company in India as well as the fifth-biggest generic-pharmaceutical company in the United States of America (USA) based on prescription (Source: ZLL's Annual report for FY23). According to the management, ZLL is the domestic market leader in the Oncology segment and was ranked amongst the top five companies in cardiology, respiratory, gynaecology and pain management segments during FY23. Furthermore, 12 of the company's brands were amongst the top 300 brands of Indian Pharmaceutical Market (IPM) during the year. Moreover, the financial risk profile of ZLL is very strong marked by large net worth base and minimum reliance on external debt resulting into healthy capital structure and strong debt protection indicators. During FY23, ZLL reported a net profit of ₹2,097 crore and gross cash accruals (GCA) of around ₹2,712 crore. ZLL, on an average, spends nearly ₹25-30 crore annually towards CSR primarily in the education and healthcare sectors. During FY23, ZLL provided funds of ₹6.30 crore (P.Y.: ₹17.00 crore) in the form of CSR contribution to ZF. Due to its strong financial profile, ZLL is capable of providing any need-based assistance to ZF. Furthermore, the management of ZLL has also indicated their willingness to extend any need-based support to ZF.

Managerial linkages with the resourceful promoter group, Zydus Cadila, which has wide experience in pharmaceutical and healthcare sectors

ZF is a part of the Zydus Cadila group promoted by Ahmedabad-based Pankaj Patel and his family. Pankaj Patel, the Chairman of ZLL, and Sharvil Patel, Managing Director of ZLL and Chairman of Zydus Wellness Limited (ZWL), act as Directors in ZF thereby demonstrating strong managerial linkages with the Zydus Cadila group. Furthermore, the promoter group has significant experience of more than six decades in the pharmaceutical and healthcare industry. The major group companies are Zydus Healthcare Limited, Zydus Wellness Limited, Cliantha Research Ltd, Zydus Hospira Oncology Private Limited, Zydus Technologies Limited, etc.

Zydus Cadila group currently manages and operates four hospitals in Gujarat including two in Ahmedabad, one in Anand and one in the Suzuki Motor Gujarat Township at Becharaji Village. Over the period of last four years ended FY23, the Zydus Cadila group has demonstrated strong financial support to ZF by infusing fund to support its operations as well to fund the on-going capex requirement.

Benefits available from state government

Under the health policy 2016, introduced by GoG, "Zydus Medical College and Hospital" is eligible for receiving various incentives as follows: (1) Assistance of ₹7.5 lakh per seat for M.B.B.S. course for a maximum period of five years. (2) Reimbursement of electricity duty in the electricity bill of medical college and attached hospital for five years. (3) Annual grant from the government which was received by the Civil hospital before the transfer of operations to ZF. (4) Other government incentives related to construction of hospital building, purchase of equipment, under Health Policy 2016 and under Pradhan Mantri Jan Arogya Yojana (PMJAY). However, certain state government assistance and incentives which were available for the period of five years only, got exhausted by the end of FY23. ZF has received a total government grant of ₹105.25 crore up to March 31, 2023.

Continued high enrolment ratio in light of limited availability of medical seats in the state with overall favourable growth prospects for the education as well as healthcare sectors

Since its first year of operation in 2019, ZF was able to maintain the enrolment level at 100% due to the limited seats available for medical education in Gujarat. The total seats available for M.B.B.S. course in Gujarat is nearly 6,400-6,500 as against more than 75,000 students who registered for National Eligibility-cum-Entrance Test (NEET) annually. Hence, CARE Ratings expects that ZF would continue to receive 100% enrolment going forward. Moreover, the outlook for overall education sector remains favourable in light of growing middle-class population with rising income levels, increasing enrolment of students in colleges and universities, emphasis on girls' education, increasing private spend on education, wider variety of courses offered by colleges and universities, etc. However, challenges relating to access to education, quality of education imparted, governance and management, and financial commitment to education development continue to persist.

At present, the rising incidences of lifestyle diseases, the rising demand for affordable healthcare, the emergence of technologies like telemedicine, and the increased role of government in healthcare investment space are the major driving factors in Indian healthcare industry. The Indian government has remained very active through its various initiatives such as Ayushman Bharat, Amrutam Yojana and other schemes.

Healthy net worth base on the back of continued receipt of corpus fund

During FY23, ZF received donation for special purpose amounting to ₹15.25 crore which was directly credited to the corpus fund under balance sheet leading to further strengthening of net worth base of an entity as on March 31, 2023. Moreover, ZF has prepaid part NCD of ₹40 crore during FY23 leading to reduction in the debt level to ₹145 crore as on March 31, 2023. Thus, the overall gearing ratio of the company improved from 0.97x as on March 31, 2022, to 0.65x as on March 31, 2023. As informed by the management, ZF does not have plan to raise any debt in the medium term which will lead to improvement in the overall gearing over a period of FY24-FY26.

Strengthening infrastructure

The entity has completed the project to build additional bed capacity along with college facility/ infrastructure and incurred an aggregate cost of around ₹430 crore by March 31, 2023. As on March 31, 2023, the entity has fully achieved its planned bed capacity of 750 beds. Furthermore, the entity has built additional infrastructure for Post Graduate course. The entire capex of around ₹430 crore is being funded through NCD of ₹185 crore (of which the entity has prepaid ₹40 crore) and balance through CSR contribution received from Zydus group entities.

Liquidity: Adequate

The liquidity of ZF over next one year is expected to remain adequate in the absence of any long-term debt repayment obligation during this period as well as due to nominal interest rate charged on the existing NCDs. The liquidity of ZF is largely underpinned from the expectation of its access to timely need-based support from its parent (ZLL) and Zydus Cadila group. ZF being part of the large-size Zydus Cadila group enjoys strong financial flexibility.

Key weaknesses

Limited track record of operations with the medical college being first venture of the promoter group in the higher education sector

ZF has a limited track record of operation as it had taken over the operation of the medical college at Dahod (Gujarat) in January 2019. Although Zydus Cadila group has vast experience in the healthcare and pharmaceutical industries, the promoter group has ventured into the higher education sector by taking over the operations of the medical college at Dahod. By virtue of being the group's first venture in higher education sector, the operations may be impacted if not managed successfully. With the successful operations and 100% enrolment in M.B.B.S course, the company has recently introduced M.D. (post-graduation) course with its first academic year started from the year 2023-2024. CARE Ratings observes that maintaining healthy enrolment ratio and generating sufficient cash flows by way of charging of adequate tuition fees over a long period of time and thereby becoming self-sufficient would be crucial for its prospects.

Challenges of attracting and retaining quality doctors and medical professionals

Undertaking new project and expanding existing facilities require trained doctors and medical personnel. Scarcity of trained medical persons (including doctors) owing to better alternatives available with them, makes it relatively difficult to attract and retain skilled pool of medical personnel, especially in the tribal area of Dahod.

Envisaged limited operating cash flows for the foreseeable future

ZF has a scheduled bullet repayment obligation of ₹145 crore of NCD on March 25, 2025, i.e., FY25. ZF's cash accruals are envisaged to be limited during FY25, thereby necessitating need-based support from ZLL/ Zydus Cadila group for its timely servicing (including through refinancing). Considering bullet repayment of the existing NCDs in FY25, there exists refinancing risk. However, CARE Ratings notes and envisages that ZF being part of the Zydus Cadila group and a 100% subsidiary of ZLL, should be able to service/refinance its debt in a timely manner.

Presence in a regulated higher education sector

Higher education sector is one of the regulated sectors with both state and central governments regulating the industry directly and/or indirectly through various bodies including University Grants Commission (UGC), Medical Council of India (MCI) and All India Council for Technical Education (AICTE). The scope of government regulations is wide, starting from establishment of course/institute, seat sharing, fee fixation and periodical review of the standards followed by the institute. These factors have significant impact on the revenues and profitability of the institutions. Also, risk related to non-renewal of courses along with any adverse changes in regulatory guideline persists as the university needs to follow the same from time to time.

On-going PIL in Honourable Gujarat High Court for operating the hospital
The Honourable Gujarat High Court has directed ZLL not to charge any fees from patients visiting its hospital (erstwhile Dahod General Civil hospital) for treatment. The decision came after a PIL was filed by four residents of Dahod stating that the hospital management had started charging the poor patients for medical services which were given free till 2017 and urged the court to put a break on the practice. Presently, ZF is not charging any fees for medical treatment in its existing hospital. The matter is sub-judice and its outcome and impact on ZF will be closely monitored by CARE Ratings.

Applicable criteria

Policy on default recognition
Consolidation
Financial Ratios – Non financial Sector
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Credit Watch
Education
Hospital
Policy on Withdrawal of Ratings

About the company and industry

Industry classification

Macro-Economic Indicator	Sector	Industry	Basic Industry
Consumer Discretionary	Consumer Services	Other Consumer Services	Education

ZF, a 100% subsidiary of ZLL, was incorporated in January 2019, under Section 8 of the Companies Act, 2013. ZF is headed by Pankaj Patel and family who also own and run ZLL, ZWL and various other companies. ZF had taken over the running operations of 363-bed Civil Hospital Dahod from Government of Gujarat (GoG) under Brown Field (Scheme for establishment of new self-financed medical college at government hospitals) Scheme of Health Policy, 2016 and obtained permission from GoG and MCI to commence Medical College at Dahod. This initiative is under the PPP model initiated by GoG. ZF now manages the Zydus Medical College and Hospital (ZMCH) at Dahod, and the college is affiliated to Shri Govind Guru University, Godhra. ZMCH is providing tertiary health care services to the tribal population of eastern Gujarat and adjacent districts of Madhya Pradesh and Rajasthan states and runs the college offering M.B.B.S. and M.D. courses.

Brief Financials (₹ crore)	FY22 (A)	FY23 (A)	Q1FY24 (UA)
Total operating income	64.48	108.15	26.28
PBILDT	6.27	31.51	3.76
PAT	(4.81)	15.05	(0.66)
Overall gearing (times)	0.97	0.65	NA
Interest coverage (times)	NM	175.06	NM

A: Audited; UA: Unaudited; NM: Not Meaningful; NA: Not Available; Note: 'the above results are latest financial results available'

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating history for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Debentures-Non-convertible debentures	INE04VY08012	24-03-2020	0.10%	March 2025	145.00	CARE A-; Stable

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/ Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021
1	Debentures-Non-convertible debentures	LT*	145.00	CARE A-; Stable	-	1)CARE BBB+; Stable (30-Aug-22)	1)CARE BBB+; Stable (02-Sep-21)	1)CARE BBB+; Stable (29-Sep-20)
2	Debentures-Non-convertible debentures	LT*	-	-	-	-	1)Withdrawn (02-Sep-21)	1)CARE BBB+; Stable (29-Sep-20)

*Long term

Annexure-3: Detailed explanation of covenants of the rated instruments/facilities

NCDs	Covenants
Financial covenants and non-financial covenants	1) In the event there is a downgrade in the Credit Rating of the Debentures or the Issuer below 'BBB+' by the Rating Agency having an outstanding rating on the Debentures or the Issuer, the Coupon for the Debentures shall be revised upwards by 0.05% for each notch of such downgrade, from the date of such downgrade and shall be payable on the immediately next Coupon Payment Date. 2) In case of default in payment of any monies accruing due on the respective due dates or in creation of Security Interest within the stipulated timelines, the entire outstanding amount thereof shall carry default interest, which shall be a rate of 2% p. a. over and above the applicable Coupon Rate in respect of all outstanding amounts for the period of default or delay until (and incl.) date on which such failure is rectified or waived off, as the case may be, by the Debenture Trustee. 3) The Debenture holders shall have a right to call upon the Issuer to mandatorily redeem the Debentures, upon the occurrence of any of the following events (each a "Mandatory Redemption Event" and collectively "Mandatory Redemption Events"): (a) In the event, the Credit Rating of the Debentures or Issuer is downgraded to or below 'B-' by the Rating Agency having an outstanding rating of the Debentures or Issuer or a new rating of B- or lower is assigned. (b) In the event the Debentures are not listed on the wholesale debt market segment of the Stock Exchange within 15 (fifteen) days from the Deemed Date of Allotment or within such period as permitted under Applicable Law.

Annexure-4: Complexity level of the various instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Debentures-Non Convertible Debentures	Complex

Annexure-5: Lender details: Not Applicable

Note on the complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About us:

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