Dr Lal PathLabs

February 19, 2018

National Stock Exchange of India Limited
Exchange Plaza,
Plot No. C/1, G Block,
Bandra Kurla Complex
Bandra (E)
Mumbai – 400 051.

BSE Limited
Corporate Relationship Department
Phiroze Jeejeebhoy Towers
Dalal Street
Mumbai- 400001

**Subject: Financial Results Conference Call Transcript for Q3 9M FY18**

Dear Sir/Madam,

Pursuant to Reg. 30 of SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, please find attached herewith Financial Results Conference Call Transcript of the Company for Q3 9M FY18.

We request you to please take the same on record.

Thanking You,

Yours Faithfully,

For **Dr. Lal PathLabs Limited**

Dr Lal PathLabs Limited

**Rajat Kalra**
**Company Secretary & Legal Head**

Encl: As above

Dr. Lal PathLabs Limited (LPL)
Q3 & 9M FY18 Earning Conference Call Transcript

February 08, 2018

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| Call Duration | ▪ 59 minutes |
| Management Speakers | ▪ (Honorary) Brig. Dr. Arvind Lal - Chairman and Managing Director<br>▪ Dr. Om Prakash Manchanda - Whole-time Director and CEO<br>▪ Mr. Dilip Bidani – CFO<br>▪ Mr. Bharath - Chief Operating Officer<br>▪ Mr. Ved Goel - Deputy CFO<br>▪ Mr. Rajat Kalra - Company Secretary & Head of Investor Relations |
| Participants who asked questions | ▪ Abhishek Sharma from IIFL<br>▪ Alok Dalal from CLSA<br>▪ Anuj Gupta from Economic times<br>▪ Gagan Thareja from Kotak Investment<br>▪ Kislay Upadhyay from Ambit Capital<br>▪ Prakash Kapadia from Anived PMS<br>▪ Pratik Jain from Prabhudas Liladher<br>▪ Rohan Dalal from B&K Securities<br>▪ Shaleen Kumar from UBS<br>▪ Shivam Gupta from CWC Advisor<br>▪ Sreeram Rathi from ICICI Securities<br>▪ Varun Balchandran from Catamaran |

**Moderator:** Ladies and gentlemen, good day and welcome to Dr. Lal PathLabs Q3 FY18 Earning Conference Call. As a reminder, all participants' 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. Siddharth Rangnekar of CDR India. Thank you and over to you sir.

**Siddharth Rangnekar:** Thank you. Good evening, everyone, and welcome to Dr. Lal PathLabs Limited or LPL'ss Q3 & 9M FY18 Conference Call for Investors and Analysts. Joining us today are, (Honorary) Brig. Dr. Arvind Lal - Chairman and Managing Director of the company; Dr. Om Prakash Manchanda – Wholetime Director and CEO; Mr. Dilip Bidani – CFO; we also have with us Mr. Bharath - Chief Operating Officer; Mr. Ved Goel - Deputy CFO; and Mr. Rajat Kalra - Company Secretary & Head of Investor Relations.

I would like to highlight that some of the statements made on today's call could be forward-looking in nature. Actual results may vary significantly from those statements. A detailed disclosure in this regard is available in the 'Results Presentation', which was circulated to you earlier, and is also available on the exchange website.

I would now like to invite Dr. Lal to share his perspectives with you. Over to you, sir.

**Dr. Arvind Lal:** Thank you, Siddharth. Good Evening, everyone. It gives me immense pleasure to address you again in the Earnings Call of Q3 FY18.

At the outset, I am pleased to inform you that we have received all big required permissions to start operations in a much-awaited Kolkata Reference Lab, and we have commenced Lab Testing. Once the operations get stabilized, we will do a formal market launch later.

As I often mentioned, our business is built with the support of our customers and patients whom we have strived to provide high quality affordable service with improved accessibility. In order to achieve these goals, we continually focus to offer the latest and the best diagnostic testing platforms for rendering accurate and time-bound Diagnostic services to our patients' base.

The organized diagnostic space continues to witness close attention from various quarters which in our opinion bodes well for all the patients who will benefit from wider access to quality services. On our

part, we will continue to commit our commitment to drive scale on operations through an established brand franchise, the strength of our balance sheet and support from our patients and other stake holders.

With this, now I request Dr. Om to take this call forward by sharing his thoughts. Thank you very much.

**Dr. Om P Manchanda:** Thank you Dr. Lal. Thank you all for taking the time out and joining us for the call today. I will commence with the Highlights of Performance during Q3 & year to date Nine Months FY18 and share thoughts and Drivers of our Strategy." Later, Dilip will share the Details of Operating and Financial Progress achieved during this period.

I am glad to announce that during this quarter we achieved a revenue growth of 26.6% resulting into year-to-date nine months' growth of 14.1%, sharply up from what we had achieved in the first half, this is also in line with the guidance that I had given on the previous call. Of course, the current quarter performance had the advantage of favorable base primarily due to two variables - One is demonetization and other one is festival timings varying from quarter-to-quarter.

This growth was predominantly led by strong patient volume growth of 26.1% and this augurs well for the future of our business. This has been achieved through our ever-growing network reach and other initiatives to drive volumes.

Our efforts to drive growth through volumes and test mix rather than through upward revision of pricing is also paying off and will continue to do so in coming times to come. Last time I shared with you that we would be giving a renewed focus to the Wellness segment and bundled packages. I am glad to inform you that this initiative is gaining momentum, and we are aggressively pursuing this segment and we have seen an improvement in samples per patient as well.

As I move to Update our Strategic Initiatives, I am pleased to share that we received the final regulatory clearances in end December for our Kolkata Reference Lab Project, and we have started pilot test operations in that lab. Equipment stabilization is in progress, and we should see steady ramp up in the coming months. Based on our learning and experience from Kolkata Lab, we will then consider the timing from moving forward with Lucknow Reference Lab as well.

Overall with above backdrop, I am happy to share that we are on track to achieve around 15% revenue growth for the full year FY18.

With that I would request Dilip to continue.

**Dilip Bidani:** Thank you and good evening to all of you once again and thank you for your continued support and participation in our calls. I will run you through the Important Highlights.

I am glad to share that December quarter witnessed a strong revenue growth of 26.6% at Rs. 2,627 million, driven mainly by patient volume growth of 26.1%. With this, our nine months Year to date revenue stands at Rs. 7,901 million, growth of 14.1% on Year to date basis with YTD volume growth at 13.2%. The underlying patient volume growth of 26.1% for the quarter and 13.2% for the nine months' period from 3.03 million last year in Q3 to 3.82 million in Q3 this year.

We are also glad to mention that tests per patient have increased from 2.19 to 2.28 in Q3 this year. Revenue realization per patient at Rs. 688, was similar as Q3 last year which was then at Rs. 685. This reflects the price rationalization we have taken this year in select geographies and tests and partially offset by higher realizations of bundled tests.

Normalized EBITDA in Q3 at Rs. 596 million, after eliminating the impact of RSU and other stock-based remuneration charges grew at 22.5% over Q3 last year which was at Rs. 487 million. Cumulatively, EBITDA for the nine months period is Rs. 2,083 million is 8.6% higher than YTD last year, which was at Rs. 1,919 million. Normalized EBITDA margin for Q3 continued to be healthy at 22.7% and at 26.4% for YTD December. Other income includes dividend from liquid funds and interest from FD. Cash and liquid funds balance as at end December is Rs. 4,903 million. PBT is Rs. 555 million in Q3 Vs. Rs. 472 million in the previous year, a growth of 17.6%. YTD nine months PBT grew 6% to Rs. 1,993 million from Rs. 1,880 million last year. PAT at Rs. 364 million in Q3 grew 17.7% Vs. Rs. 309 million in Q3 last year. YTD nine months PAT grew 6.7% to Rs. 1,319 million from Rs. 1,237 million last year. Q3 FY18 EPS diluted is Rs. 4.40 Vs. Rs. 3.75 in the previous year.

We are continuing to pursue our strategies outlined earlier and focus on expansion through franchising our collection network and building scale in the markets where we operate. Focus will continue on cost and productivity improvement to protect margins and reinvest in the business.

This brings me to the conclusion of my opening remarks and I would like the moderator to take queries from the participants. Thank you.

**Moderator:** Thank you very much. Ladies and gentlemen, we will now begin with the Q&A Session. The first question is from the line of Sreeram Rathi from ICICI Securities. Please go ahead.

**Sreeram Rathi:** Two questions; one, on the volume growth this quarter it was 26% significantly higher of course also benefited from the low base, at the same time in Q4 also we had a low base last year. So you are guiding for 15% growth and looking at the nine months number, you already had 14% revenue growth. So is there a possibility that you can surpass your guidance because last year Q4 was also low base, so is it a conservative guidance or something like that?

**Dr. Om P Manchanda:** Little early for us to comment on this, but you are probably right because Feb, March are two key months, so hopefully we should surpass this 15% as well.

**Sreeram Rathi:** Like 15% growth for FY'18, first half being impacted by the high base and second half benefited from the low base. So going forward from next year onwards, should we assume that mid-teens is something that is comfortable for achieving the growth is what we are looking at, most part of that will be volume growth only?

**Dr. Om P Manchanda:** I think that is fair assumption. Yes, that we have continuously been saying that given the pricing pressure and competitive intensity, we want to stay focused on volume as much as possible, So we right now do not foresee any price increase, so we will continue to drive growth through volumes.

**Sreeram Rathi:** The other expenses for the quarter has been significantly higher in absolute amount sequentially as well as YoY basis to Rs.71 crore. So any particular reason for that or it also include some additional expenses which would have started for Kolkata?

**Dilip Bidani:** Sriram, hi, Dilip here. The cost for this quarter specifically we have increased expenditure bit on A&P, there has been an impact on repairs and maintenance which we have undertaken, some other initiatives and infrastructure costs that we have taken and little bit contributed by Kolkata as well, but not so significant yet.

**Sreeram Rathi:** So I can assume that probably this would have been specific this quarter part of it like repairs, maintenance and A&P which may not be recurring every quarter?

**Dilip Bidani:** Yes, but I do not think we can be very specific about that because there could be some costs which will come in, in the next quarter as well, which would be higher on Kolkata side. Also what is happening is that there is a profile of the channel margins, which is changing with relatively higher growth in the other regions outside of Delhi, where the channel margins are higher. So that is also taking shape now.

**Sreeram Rathi:** So sir, we stick to our guidance of around (+25%) kind of EBITDA margin going forward?

**Dilip Bidani:** That is what we are maintaining that we should be in a position to be above 25% EBITDA margins.

**Moderator:** Thank you. We will take the next question from the line of Shalin Kumar from UBS. Please go ahead.

**Shalin Kumar:** Continuing on questions of the previous participants, we already are close to 25% if I average out for our nine months and if I look at this quarter EBITDA margin they are close to 22%. So we are basically saying that for this quarter we should have close to 25% kind of EBITDA margin for a year?

**Dilip Bidani:** Yes, in fact, the normalized margins on YTD basis is 26.4%.

**Shalin Kumar:** When we get 25%, it is normalized margin we are talking about or…?

**Dilip Bidani:** Yes, we are talking about normalized margins… even the 22.7% I spoke about is a normalized margin.

**Shalin Kumar:** Can you tell us about your bundle test and health and wellness, the first brand which you had earlier discussed. How much are they contributing, what kind of growth are you seeing over there?

**Dr. Om P Manchanda:** We are seeing a very good growth there, but I would not say, the growth is entirely due to Wellness segment, there could also been upselling or cannibalization from existing portfolio. So, we have to sort that as to what extent it is preventive and to what extent it is not preventive. But definitely, we are getting good traction there because we did launch a new mix where we had completely new packages and price points, and we also opened it up to not only our lab but also collection network. So it has given us good growth, and partly that is also showing up in volume growth that we see in this quarter. It is little early for us to share these numbers because we need to do a little bit of deep dive as to what the breakup is but on balance I can say it is giving a good response.

**Shalin Kumar:** The volume growth was pretty impressive, I agree that we had low base and your realization also are holding up. So can we think like competition is not increasing here or what is happening in the size over there?

**Dr. Om P Manchanda:** I think in the previous calls I have mentioned many times that one should not read too much into this wild swing in volume growth, because many times depending on the type of sort of infection,

sometimes one patient may have frequent testing over a short period of time, especially when the infections like dengue, etc., are higher lot of the platelets count come in and that tend to really give a very high volume growth. So I believe we would not unnecessarily jump to conclusion that 26% growth is going to be sustainable. Overall, all I can say is that it is volume-led growth which is very important for us rather than price-led. So that is one trend that we see, and second, what we are seeing is not only patient volume, but also test per patient as a contribution of some of these bundled packages move up, it will also drive up the test per patient, and that will further help us to have higher realization per patient as we go forward. So this particular quarter 26% volume growth also may have come because of certain tests like platelets, etc., been much more than the usual quarter we see.

**Shalin Kumar:** One thing which I was trying to understand is about the competitive intensity, if you can highlight about it? Last bit is basically there has always been worry about price capping which we hear and which is a worry about. So if you will be sharing anything or you have any view on that?

**Dr. Om P Manchanda:** That is an external variable, I think, internally what we can do is that continuously focus on cost of doing business and stay productive in relation to competition, I think, our internal focus has been to drive productivity and focus on model where the cost of goods is lower than competition. So that is the focus that will continue for us. On the price regulation piece, because it is an external variable, one cannot comment about this. I think, internally, we need to stay prepared for that if that happens.

**Moderator:** Thank you. We will take the next question from the line of Prakash Kapadiya from Anived PMS. Please go ahead.

**Prakash Kapadiya:** Sir, two questions from my side; typically on the Delhi NCR region, some thoughts on using technology especially to upscale, cross-sell to family members increasing ARPU given that northern region we have leadership to grow the market share more than double digit. So small things like sending a reminder for diabetes or vitamin kind of level or selling swasth as a package and you know communicating the value proposition because if one has to look at just the small test or two tests will cost Rs. 1,200-1,500 while a package might cost Rs. 2,200. So some thoughts on that and is that an option to grow the NCR in the northern market faster than what we were historically at?

**Dr. Om P Manchanda:** I will break your question in two parts -- One is that we neither do or nor want to be seen as pushing sales of these tests for even if they are not required, we do not want to get ourselves into a position where pushing

these tests unnecessarily, that is not our intent, we won't do that. Probably what we try to do is create healthcare awareness and make people aware about their health needs so that they are little more conscious about that, and we make our offerings of preventive health checkups. This entire wellness product that we have which is 'Swasth', is available to patients, and we make them aware about various wellness packages, and if they want to avail these kind of packages not only for themselves but for other family members, they are most welcome to do that. But you are probably right that we have a good sort of brand equity in Northern India, and we are seeing clearly being a preferred brand people do not mind paying slightly higher premium to quality and brand, and that traction we have seen. So this wellness growth also has come from not only Delhi NCR but other parts of North India as well.

**Prakash Kapadiya:** Any thoughts or anything working on say once a loyal customer specifically this is more from the Northern region customer repeats himself, so tapping family members or getting more into tapping other family members, is that a possibility we are thinking, is it possible, not possible?

**Dr. Om P Manchanda:** I will actually sum this up in a sort of marketing initiative where we move away from a transaction model to an engagement model, engagement will not only extend to the same patient coming to us for multiple visits, but also will extend to the family members. We have launched a facility where patients can access all their earlier reports, not only for himself/herself, but also for the family members, which becomes all records in one place, which is bringing in the feeling of one definition for all the healthcare needs of the family. We are moving in that direction. With a lot of our digital initiatives, this will become much easier for us to engage with that customer at a family level rather than at individual level.

**Prakash Kapadiya:** If that translates that NCR and the northern market, that is the biggest market, if that can grow bit faster, that can really help achieve overall growth relatively better than what we have been doing?

**Dr. Om P Manchanda:** Absolutely, thanks for your inputs as well.

**Prakash Kapadiya:** On the Eastern region, if you could give us some sense, more like higher volume, lower ticket size, what kind of test do we think will sell more typical diabetes, blood test, thyroid.. how do we look at cost because I guess cost, also would be relatively lower which should lead to normalized sort of margins as the Kolkata scale comes in. What point of inflection does the hockey stick kind of volume come in – is it year two onwards from our experience in Delhi once the reference lab was set up, would give some sense that will be helpful?

**Dr. Om P Manchanda:** I think that is a very good question and internally we are working on that. There are two curves in our revenue graph -- One is the curve which is of high end test, other is routine test. Since this lab is central lab, it is going to have lot of high end test, I think the first initial kicker will come from high end test. Normally these are those tests which are outsourced by other healthcare institutions like hospitals and smaller independent labs. What it does is that the growth is going to be widespread from the entire region rather than from one or two cities. So I see that first six months to may be one year we will see growth coming from higher end tests or complex tests. As the brand equity tends to trickle down, and that will have a positive rub off on building up of infrastructure, because more and more collection centers and franchisees, they will come forward, want to become associated with Dr. Lal PathLabs, and then from that infrastructure, comes a business for routine tests. That is where the next layer of expansion will fall in place where we start building centralized lab network. That according to me should start happening after about one and half or two years. So there is going to be gradual ramp up of this, and I think the question that you have inflection point or a tipping point, that should happen may be after one and half years to two years. That is how my experience is, I do not know how it pans out, and we will have to see. Quarter-after-quarter we will have to see, but that is the way I would see.

**Prakash Kapadiya:** Directionally this is what at least we also internally feel how we would...

**Dr. Om P Manchanda:** That is what we have also seen at a smaller scale level when we look at centralized lab in a smaller town. So, initially it is high end testgrowth and then comes routine.

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

**Rohan Dalal:** I have two questions: The first one pertaining to your volume growth. I wanted to know what was the split, where did the growth really come from – from B2C or B2B volumes for this quarter, was it more walk-ins?

**Dr. Om P Manchanda:** It was uniformly spread across, initially as we mentioned this year, festivals were more in September month, so, usually festivals are in October or early November, so we had that advantage, all that flow which should have happened in September actually happened in October, so that is one thing. Second is also last year base was low. So I think the growth is uniform. So there is no particular outlier sort of variable that I can talk about which led to growth in a particular area or a particular segment.

**Rohan Dalal:** I was wondering regarding the operational profit for the quarter. There was from other expenditures, if I have seen it right, the cost of material consumed also went up by about 29% and your employee benefit expenses also went up as well along with the fees to collection centers. So could you shed some light on that?

**Dilip Bidani:** Basically if you look at this quarter and this year, the volume growth itself leads to a higher material cost, so that is fully reflective of the volume growth that has taken place, plus there has been some cost escalation due to GST and all, so this had impact on that as well, that is one item. Other item you mentioned was on personnel cost and people cost. This includes cost of RSU which is also there in the cost base, so that has also been adding to the overall cost growth plus the headcount cost which has increased over last year The head count numbers plus typical annual increment takes place would add to the people cost of last year versus this year. These are the two, three main reasons.

**Moderator:** Thank you. We will take the next question from the line of Gagan Thareja from Kotak Investment. Please go ahead.

**Gagan Thareja:** Is it possible to understand what portion of the RSU is still to be expensed out and what timeframe will it happen?

**Dilip Bidani:** Basically this RSU charge will be over the life of the RSU, which is four years and is calculated as per the Black-Scholes formula. So therefore, there is a very complex formula which typically results in bulk of the charge being taken in the first year itself, and then it goes on over the remaining life of the vesting period. But one thing you must note is that this is the cashless charge, it is not a cash outflow, it is Black-Scholes formula which is a charge to P&L and typically it results in hit in the first year of the grant and then gradually tapers off. Other thing you must recall is that this is not dilutive any further right now, because if you recall, these are all going to be issued out from the old ESOP trust which is already holding the shares. So there is no further dilution which is taking place.

**Gagan Thareja:** What could be the fixed cost for the Kolkata Lab?

**Dilip Bidani:** Fixed cost for the Kolkata Lab on a full year basis annualized going forward will be in the range of Rs.6 to 8 crore is what we estimate excluding the material cost.

**Gagan Thareja:** To a previous question, you did point out in the affirmative that 15% volume growth for the next financial year is sustainable. If that is the case, then I am just trying to understand what is the contribution from Kolkata for that?

**Dilip Bidani:** If you look at the way we are looking at it is that Kolkata should give us from the company average a significantly higher growth. So the way we are looking at it is at least 10% to 12% points higher than the company growth is what we need to work towards, because that is what is then going to drive the overall volumes. Let us wait and see, because unless we do that knowing fully well that more than half of the volume is from the northern region, and part of it is Delhi NCR may not grow at the same rate in order to get weighted average of 15%-odd, we will need to grow the eastern market much faster, but more so with the heavy investment coming in.

**Gagan Thareja:** Currently, a lot of tests pertaining to the Eastern region would have been executed at the Delhi lab. So once you shift up to the Kolkata Lab which you will in the coming times, what impact could it have on the Delhi labs here?

**Dr. Om P Manchanda:** Dependence from Kolkata region on Delhi is not that high as one would tend to think. I think the dependence is in the range of 10% to 15%. While we are looking at this investment in the region to stimulate demand rather than impact supplies, I think to the extent of 10% to 15% reduction in Delhi testing would take place. But in any case, that would help to serve the northern region from whatever we are expecting for us required to grow in this market, would come from NRL Delhi.

**Gagan Thareja:** Your thoughts on your business in the western and southern region. Currently what proportion of your sales from these two regions and how do you strategize for these two regions in the coming two, three years?

**Dr. Om P Manchanda:** As we outlined earlier also, we continue to look at that way, so there are two focus cities we have in South and West, in South it is Bangalore and in West it is Pune. Both these cities we continue to aggressively market and build B2C business. Thesis there is that once we create these clusters, on back of that we can grow the region, the way we did in Delhi. So once we reach the critical mass of Rs.30-40-50 crore in a city and then it is set for expansion in the region. So, that is one element of the strategy. Second is we continue to market pan India our high end and complex tests and we are investing behind building specialty sales force and bringing in lot of focus on high end test like genetics, etc., and also going to look at creating certain divisions which are going to focus on things like oncology, etc., and that we will continue to market to all healthcare institutions and focus on B2B segment, and as I mentioned earlier it does help us in building B2C at a later stage, while parallel efforts on M&A would continue, that is the way we would look at South and West.

**Gagan Thareja:** Would it be fair to presume that in the coming three, four years or rather two, three years, in these two regions you might see an inflection point just as you might reach in the Eastern region post the Kolkata lab gets executed?

**Dr. Om P Manchanda:** If we actually track three of our growth, that is what one tend to assume in absence of any inorganic happening, the organic way of growing business is actually the same way. So you keep on seeding the newer markets for future growth and while we build today, let us say, eastern region is expected to become star while these regions could be our future stars as well. We are not leaving these regions untapped but we are investing in a couple of focus cities and see how it turns out to be.

**Moderator:** Thank you. We will take the next question from the line of Anuj Gupta from Economic Times. Please go ahead.

**Anuj Gupta:** All I want to know is can you give a color on the revenue as well as the volume? Northern is supposed to be the strongest market but you have had fair share of competition from the South and West. So any comments on that?

**Dr. Om P Manchanda:** Competition is uniform all across, it is not that North has higher competition or lower competition, and I think that is uniformly distributed. Only thing is, since our dependence on North is high, so we tend to feel it more, so that is question #1.

**Dilip Bidani:** To your other question, revenue split is still continuing at the earlier level, so we have about 70-72% coming from North, 12-13% is East, and about the same 13-14% in south and west combined. The value share is this, but the volume share may be slightly lower in the north and higher in the other three combined, because the value realization is a bit higher coming from the north.

**Anuj Gupta:** You just talked about your plans of marketing in the south and the west regions. So are you planning to take people onboard or is it going to be via specialist vendor or something of that?

**Dr. Om P Manchanda;** These people are on our payroll.

**Moderator:** Thank you. We will take the next question from the line of Alok Dalal from CLSA. Please go ahead.

**Alok Dalal:** Recent economic survey for the first time mentioned about discrepancy in prices for diagnostic test. So sir what signals are you getting through at this kind of survey, is that finally this unregulated to regulated going to take place and how are you positioning for that?

**Dr. Om P Manchanda:** My take on that comment is that prices do vary mainly because these labs have various quality standards, #1 is going to be a clinical establishment act coming in where these labs are being run, what are the quality standards. So that should try and convert and create a level playing field as far as the quality is concerned. As far as pricing is concerned, we are probably not at the lower end, but we are definitely not at the top end as well, so we are anything somewhere in the middle, or even probably lower than that. I think the earlier question that was asked is that regulation is an external variable, and what we need to prepare internally is the cost of doing business has to be very efficient and competitive, and make sure that quality standards are at par with the world standard, what NABL and CAP requirements are. We are very sure at that quality our price is competitive and let us see how it works out.

**Alok Dalal:** There could be a regulator for diagnostic service. Is that what the survey may indicate?

**Dr. Arvind Lal:** Alok, this is Dr. Lal here. This has happened previously also during epidemics, or endemics, swine flu and dengue fever, etc., etc., where the government has stepped into regulate the price, but to be fair to the government, after the epidemic was over, they took away that price control. Right now too much should not be looked into it, and the industry in which it has happened, cardiology, etc., that is a far cry from the diagnostics industry and in diagnostics industry the variables are not that much. Of course, the quality standards are too many, there are 100,000 labs in India, so that way it is different kind of a playing field. But to be fair to the industry, as such there is not much of difference in the prices of the organized players.

**Dr. Om P Manchanda:** I think, Alok, the general reading is that one is the variation but think the cost inflation or medical inflation, pathology test in general over a longer period is not that high. While the variation may probably explained due to differential quality standards, but in general I do not see pricing of test actually is going southwards rather than upwards.

**Moderator:** Thank you. We will take the next question from the line of Pratik Jain from Prabhudas Lilladher. Please go ahead.

**Pratik Jain:** I wanted to ask, what were the employee cost look like after Kolkata reference lab comes into operation or have we already factored in increase in the employees, is it already reflecting in this number, and also the impact on margins from the eastern region after Kolkata reference lab comes in?

**Dilip Bidani:** As far as people cost is concerned, right now it is not yet fully loaded, there are some people who are already recruited and have been there on the rolls, but not for the full quarter. So, the first full quarter will probably be Q1 of next year, not even March '18. So as we go forward that will get fully loaded. Kolkata expenses will be in the range of Rs.6–8 crore kind of thing to start with including people cost.

**Pratik Jain:** When do we expect the commercialization of the lab -- Q1 FY'19?

**Dr. Om P Manchanda:** Testing work has begun, we have not done a market launch, so for that we will formally do in Q1. We just want to see that entire operation is fully stabilized before we open it up to full market.

**Pratik Jain:** Gross margins from the Eastern region would be in after the lab comes into operation?

**Dr. Om P Manchanda:** I do not see any change in that, it should be in line with what we have always been doing, and relatively gross margins from East region are lower than Northern region, as we explained earlier, that the brand premium, etc., is much more there compared to East. Rightnow, we are looking at volume growth rather than growth in margin.

**Moderator:** Thank you. We will take the next question from the line of Shivam Gupta from CWC Advisor. Please go ahead.

**Shivam Gupta:** I just want to do a follow up to a comment that was earlier made. In quarters where you see such stupendous volume growth, why should not your gross margins correspondingly expand because logically you should have consumed more reagent, right?

**Dilip Bidani:** Yes, it is a good question, basically during this quarter there has also been an investment in additional A&P and other fixed cost which dilutes the margin to that extent.

**Shivam Gupta:** So that would not be in your cost of reagents, right?

**Dilip Bidani:** It is not in the cost of reagents.

**Shivam Gupta:** I am just only focusing on the cost of reagent line item. At least on that portion, you should have seen expansion. So what math am I missing there?

**Dilip Bidani:** I think you would be having the full impact of GST which has come in, in this quarter, because in September quarter we did not have the full impact, we had stocked up a little in advance and all of that.

**Shivam Gupta:** So effectively when your model of higher volume growth plays out and since you are saying that full GST gets normalized here. So then from FY'19 you should see a reasonable expansion on a gross level, is that correct?

**Dr. Om P Manchanda:** If I understood your question correctly, if we get a volume growth which is very high from tests which are automated, centralized, then you see a huge expansion of gross margin, but if you get lot of tests which are very local in nature, routine in nature, where high manpower cost is required, and whatever reagents, so you do not see expansion of gross margin then, so, for example, if Vitamin D volumes grow then our gross margins also tend to go up, but if tests like dengue or some of these infectious diseases go up, then our gross margins do not, and also mix impact, sometimes, when there is a spike in volume, one normally tends to see volume growth of those tests which are low in gross margins, because they are very routine or there could be some epidemic where government intervention is there on pricing, etc., On this particular quarter, we do not have that analysis, but probably we will take that input and see deeper into it, but I think that will be my general comment on the gross margin.

**Shivam Gupta:** The second question I had was that around this budget apart from the usual noise around the healthcare capping, there was also talk of government starting like free diagnostics. So hypothetically if that gets floated on a PPP basis, would the Dr. Lal be keen to look at that proposition?

**Dr. Om P Manchanda:** Yes, many times this question tends to come on free diagnostics. India, is a very large country, diverse sort of segments, we are still about at current volume base, we are very-very small compared to what the market size is, and we cater to a different kind of segment, it is not that segment which is extremely price conscious. So, some of the initiatives of free diagnostics will not affect us. That is my thesis that we are not going to get impacted negatively. Now next question of yours would be we want to participate in such ventures. Obviously yes, at one level other than commercial, our mission is to create sort of a healthcare accessible as well as affordable. So, in whatever way we can help as an enterprise without diluting our stakeholders' interest, we would definitely want to participate.

**Moderator:** Thank you. We will take the next question from the line of Kislay Upadhyay from Ambit Capital. Please go ahead.

**Kislay Upadhyay:** Sir, I understand going ahead, revenues will almost entirely be driven by volumes. One part of that would be increase in market size due to increasing healthcare awareness. The other part I guess would be

gaining market share from standalone diagnostics, regional chains of hospitals. Can I get your views on what would be the biggest revenue for you given your strength?

**Dr. Om P Manchanda:** I think the real lever for us is cost of doing business. We want to make sure that scale plays to our advantage, and as the scale picks up, per unit cost of doing business for us should become competitive, compared to let us say standalone players, and we are also seeing as our strategy of holding onto current prices pans out for a few years, I have a feeling that would put pressure on the unorganized players, and similarly as clinical establishment act gets more sort of a compliance issue start building up, people have to invest behind quality, people will have to invest behind some of the standards related to waste management, etc., So overall the cost structure of unorganized space, I have a sense over a period of time will move. Once that start setting then obviously the shifts should become much more than what we are seeing from unorganized to organized.

**Kislay Upadhyay:** What do you think would be the biggest gainers of the factors you mentioned, other cost for the unorganized – would it be the hospitals or the regional chains or the top four branded players?

**Dr. Om P Manchanda:** Biggest gainer in this is going to be the patient, patient is going to get test of a great quality at the most competitive price. So the players who can actually give that would be benefitted, I think the players who are aiming for scale are the ones should be benefitted, people who can build good quality network should be the beneficiary according to me.

**Kislay Upadhyay:** Given that the prices we would not be increasing our prices, maybe not even at CPI, would it be right to assume that at least the cost of the reagents and other costs would be growing at CPI, if that is the case, to what extent would our scale benefits prevent margin erosions and to what year do you expect that to happen?

**Dr. Om P Manchanda:** This whole dodging inflation, this is not a strategy we are saying for life, we are right now as much as possible we want to resist the price increase, and beyond a point we cannot absorb this increase, we will have to revisit this whole idea, but we are taking it quarter-by-quarter, year-by-year. I think the last price increase that we took was in 2016, we want to attempt the same in 2019, let us see how we succeed, but otherwise, as we promote this whole bundle tests, where the price per test may come down but the realization per patient will go up, because you are selling more tests per patient and that combination should help us, where we have a very combination of business coming from wellness and business coming from illness segment.

**Moderator:** Thank you. We will take the next question from the line of Varun Balchandran from Catamaran. Please go ahead.

**V Balachandran:** I just had one question on the Wellness business. I think in the last call you mentioned you have a senior person now heading that particular segment and driving that separately. So if you could give us some sense of the plan going forward for that segment in terms of how you plan to roll it out across the branches, at home testing as well as to aggregators, how do you see that gaining traction in the next year or so?

**Dr. Om P Manchanda:** So, that is right, idea is to give sharp focus to this, we just created two verticals where we start looking at the entire piece of wellness separately. Right now it is our existing channel that we are looking at, it is not something new we are doing, we already were doing at a small scale in Delhi NCR, we just have stepped up the efforts in this direction.

**V Balachandran:** Just if you could give us some sense of how you are thinking about rolling this out across branches, would you start let us say with the North region first within the top cities and then sort of roll it out gradually across places and in parallel what is the bottom that you have enrolled to serve the home testing demand, if you could give some sense of that, it will be helpful?

**Dr. Om P Manchanda:** It has been rolled out across the country, it is just that value for the patient has gone up very sharply because now patient is able to get much larger number of tests at a great price, so that has been rolled out across the country in our channel. In addition to that as you all know that online channel is also growing significantly. So, we will look at that channel as well. So idea is to reach out as many patients as possible and create awareness about healthcare per se.

**V Balachandran:** On that point, do you have A&P number in mind that will sort of create awareness thing, that this particular new package or the services available across country, any kind of A&P in mind and thereafter a year or two or medium term how big do you think wellness would be as a part of your own revenue base?

**Dr. Om P Manchanda:** It is still early right now, as I mentioned that we cannot say whatever growth is coming in this segment is coming only because of wellness. Wellness, according to me is that patient has no prescription, it is self-driven kind of test, as you know lot of promotion is going on by lot of competition, so we have just seen this new segment that is emerging, but it is not that any sale that is coming on account of these packages is due to wellness only, because there is a lot of interaction between illness or sickness segment to wellness. So we do not know whether the patient completely came for preventive test or not.

**V Balachandran:** I was wondering as you set up this as a separate vertical, and you drive efforts on that, how do you measure the impact of that particular focus in terms of what that is bringing in?

**Dr. Om P Manchanda:** We have to figure that out, we are probably learning, and we do not want to mislead first ourselves that this entire business is from wellness, so we need to understand little deeper under this before we start hearing to the market.

**Moderator:** Thank you. We will take the next question from the line of Abhishek Sharma from India Infoline. Please go ahead.

**Abhishek Sharma:** Let us suppose if price control does come, I am presuming that it will be easier to impose on individual test. In which case would company such as yours which are more focused on individual test rather than bundle test would be at a disadvantage as compared to companies who are bundling their tests?

**Dr. Om P Manchanda:** I do not know. First of all, this price control itself at this stage is hypothetical. Second is, you also should remember that if the price table comes down, and then your volumes will tend to go up for the brand… our brand is the preferred brand, so we do expect with low pricing our volume should multiply, we have seen that a couple of times in the past as well. So I do not know whether that will be to our advantage or disadvantage, but as I mentioned that we have to make sure that our cost of doing business is competitive compared to any other player for a given quality and I think if that control happens, I am sure regulator will also try to ensure that there is a level playing field on quality. I think for a given quality, if we are very competitive in cost of doing business, then advantage should flow to us.

**Abhishek Sharma:** The question is not so much about quality. Assuming that there is parity on that, but more about whether bundling of tests could help some of the other diagnostic players escape price control if it comes… it is still hypothetical but just on that?

**Dr. Om P Manchanda:** We also have bundled tests, it is not that we only sell individual tests, so bundling was always happening, now we are talking about this "Swasth" package, and you have knowledge of medical field, so, all these tests, LFT, KFT, CPCs they are all panels, right, they are all bundled tests.

**Moderator:** Thank you. We will take the next question from the line of Gagan Thareja from Kotak Investments. Please go ahead.

**Gagan Thareja:** You just mentioned that the initial ramp up in Kolkata will happen through high end test and then over a period of time it is the routine

test which will pick up. Given that high end test I presume would have better margins, would it then help you absorb the fixed cost in the ramp up phase to a very good extent and therefore is it even possible that in a year, year and a half time, when the scale up has happened we could even look at some scope for margin improvements there?

**Dr. Om P Manchanda:** Actually, high end test, somehow tends to convey that it will have better profitability, that is not true, these are complex tests, also B2B where you are competing with fewer players, but there is a fierce competition, because everybody is knocking the same door. So some of these high end tests need not necessarily give us higher gross margins, I think that is first point to be noted. What it does is that, it positions you as a quality player because your contact with the medical fraternity at top end is very high, it also helps your brand to travel to longer distances, much more higher level of involvement of patient as well as the family to the brand compared to routine tests, I think those are the big pluses of having higher market share in high end test, need not necessarily translate higher gross margin, I just want to highlight that.

**Gagan Thareja:** In North, you point out is around 70-72% of your sales. Is it possible to split it further down Delhi NCR and rest of North and also give an idea of how the North and within North Delhi, NCR and the rest of North is growing in volume terms?

**Dr. Om P Manchanda:** We have not shared this information in public forum right now because of competitive reasons, so I would not like to delve further on this.

**Moderator:** Thank you. That was the last question. I now hand the floor back to the management for their closing comments.

**Dilip Bidani:** Thank you everyone. We look forward to seeing you again next quarter. Good Bye.

**Moderator:** Thank you very much, ladies and gentlemen. On behalf of Dr. Lal PathLabs, that concludes this conference. Thank you all for joining us and you may disconnect your lines now.

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