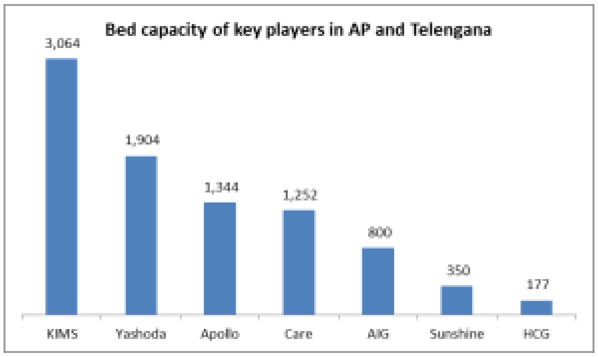
Krishna Institute of Medical Sciences Ltd

Key Details	
CMP (Rs)	1,116
52 week H/L (Rs)	1,394/938
Market Cap (Rs. Bn)	89.5
Adj. Book Value (Rs) (FY21)	113.7
FV (Rs)	10.0
P/E (X) (TTM)	44.2
Dividend Yield (%) (FY21)	-

Shareholding Pattern (%) as of September 30, 2021	
Promoter and Promoter Group	38.8
Public	61.2
Total	100.0

Background



Source: Company Reports

Krishna Institute of Medical Sciences Limited ("KIMS" or "the Company"), operates 9 multi-speciality hospitals under the "KIMS Hospital" Brand, with and aggregate bed capacity of 3,064, including over 2,500 operational beds as of June 30, 2021. KIMS is a dominant player in the states of Andhra Pradesh (AP) and Telangana ("core markets"), having 1.6x bed capacity compared to the next largest player in the core markets. KIMS' flagship hospital at Secunderabad (Telangana) has a capacity of 1,000 beds as of June 30, 2021. In Q1 FY22, KIMS' overall occupancy rate stood at ~58%. The company has added over 940 beds, in aggregate, in its hospitals in Vizag, Anantapur, Rajamundry and Kurnool between FY19-21 and the overall bed occupancy in these hospitals has increased from 71.83% to 78.60% in this period. The company has positioned itself as an affordable health service provider in Tier-II and Tier-III cities and has an Average Revenue per Occupied bed (ARPOB) of ~Rs. 27,000, which is ~25% lower than its peers.

Key Management personnel

Name	Designation	Qualification
Dr. Bhaskara Rao Bollineni	Managing Director	MBBS, MS, DNB (CT Surgery)
Dr. Abhinay Bollineni	CEO	Bachelor degree in medicine and surgery

Earnings Summary – Consolidated

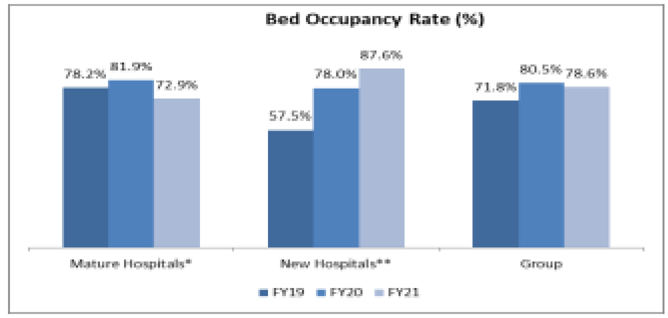
Rs. In Bn	FY18	FY19	FY20	FY21	Q1 FY22
Revenue from Operations	6.64	9.18	11.22	13.30	4.77
EBITDA	1.03	0.87	2.51	3.81	1.48
EBITDA Margin	*15.5%*	*9.5%*	*22.4%*	*27.9%*	*31.0%*
PBT	1.02	0.84	1.41	2.79	1.24
Adjusted PAT	0.76	0.50	1.15	2.02	0.92
Adjusted PAT Margin	*11.4%*	*5.4%*	*10.2%*	*15.2%*	*19.3%*
EPS(Rs)	(9.4)	(6.9)	16.0	26.1	11.5
RoCE (%)	NA	4.0%	18.5%	26.9%	29.8%
ROE (%)	NA	(8.8%)	19.2%	23.8%	25.2%

Source: Company Annual report, Capitaline; Note: CMP and Mkt Cap as on 29 October 2021

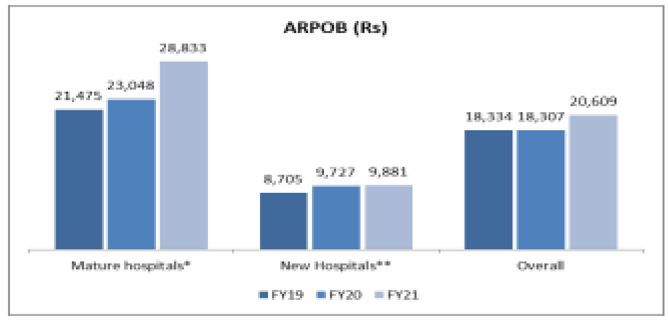
Investment rationale

Focused on affordable healthcare in underpenetrated markets

KIMS is focused on providing affordable healthcare in Tier-II and Tier-III cities and it has been able to achieve profitability in these cities by identifying markets with significantly underserved healthcare demand and delivery quality healthcare services at affordable prices. The bed occupancy levels for the recently acquired hospitals have seen a steady increment in the last 4 years. The bed occupancy rates for mature hospitals were impacted due to COVID-19 in FY21. We expect the occupancy rates for new hospitals sustain at similar rates to mature hospitals, which is expected to drive growth in future revenue.



In FY21, the company's ARPOB per day stood at Rs. 39,571 in Tier-I markets and Rs. 11,187 in Tier-II and III markets. The company's ARPOB per day is approximately 25% lower than its peers. In FY21, the overall ARPOB per day stood at Rs. 20,609 and it was Rs. 27,289 in Q1 FY22. Management believes its daily sustainable ARPOB to be in the range of Rs. 21,000 – 22,000, in the near future. The company aims to undertake initiatives to improve its daily ARPOB and minimize Average Length of Stay (ALOS) at its hospitals in order to increase patient turnover to drive revenue growth.



Source: RHP

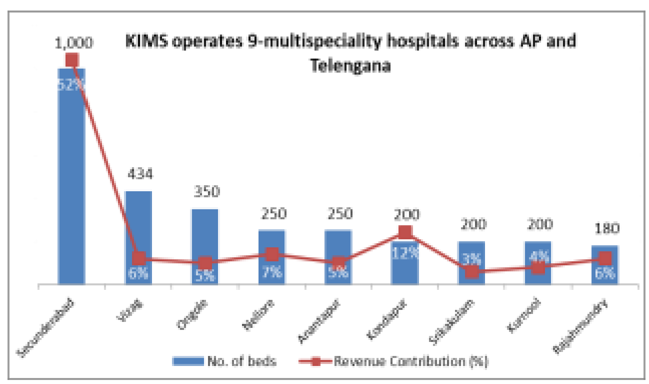
Bed Occupancy Rate – Number of bed occupied divided by number of operational census beds (i.e. excluding day care beds like dialysis, endoscopy, emergency etc.) as of the last day of the relevant year.

**Mature hospitals – Established/Operational for more than 4 years*

***New hospitals – Established/Operational for less than 4 years*

Strong regional presence and Cluster-based expansion to drive revenue growth

KIMS is the market leader in AP and Telangana in terms of number of patients treated and treatments offered. The company has grown strategically in these markets where they have a strong understanding of regional nuances, customer culture and the mindset of medical professionals. KIMS plans to add capacity of approximately 1,500 beds over the next 3-4 years, of which 500 beds will be in its existing hospitals and the remaining 1,000 beds will be added in the new geographies, through a mixture of green-field and brown-field expansions. KIMS has already entered into a land leasing agreement for expansion of KIMS Kondapur, where it will add around 250 beds to its existing capacity. In FY21, capital expenditure per bed for the company was Rs. 6.9 mn in Tier-1 cities and Rs. 2.2 mn for Tier-II and Tier-III cities, one of the lowest in the peer group. The company expects blended capex per bed to be around Rs. 9.0 -10.0 mn, going forward as the company looks to expand into metro cities. However, this is expected to be offset by higher ARPOB per day and hence, we expect the company to sustain its current returns.



Source: RHP, Company Reports

For future expansion, the company intends to focus on large geographies that can help achieve scale as they did in AP and Telangana. Karnataka, Tamil Nadu, Central India and Maharashtra have been identified as potential markets for expansion. The company has identified land parcels in Bangalore, Chennai and Maharashtra for green-field expansion. **Addition in existing bed capacity and strategic geographical expansion is expected to drive future topline growth.**

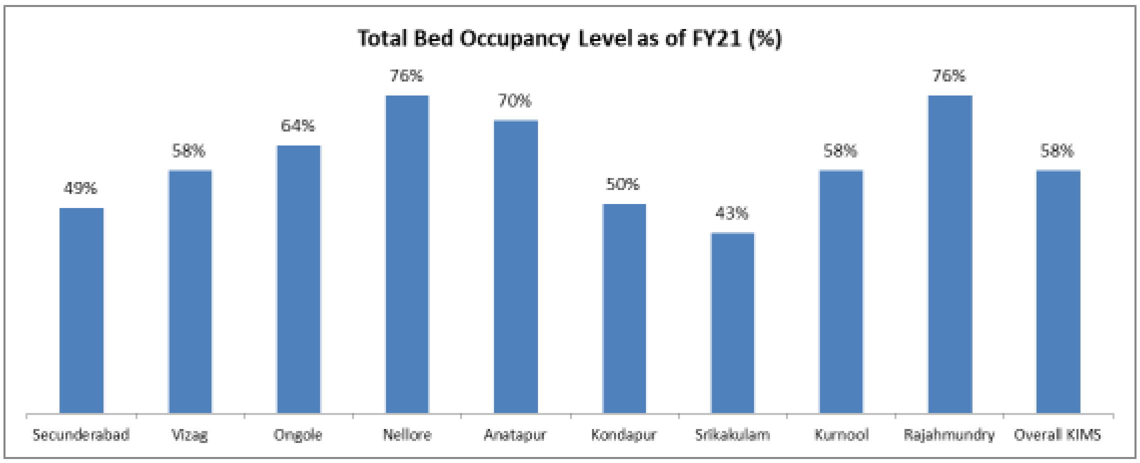
Unique model for doctor retention and fixed pay-out delivering volume growth and cost efficiency

The company follows a unique business model of doctor retention through equity participation. As a result, it has been able to retain over 80% of its doctors since its inception in 2000. This network of top quality doctors has helped the company build the "KIMS hospital" brand, which has driven volume growth. In FY21, its top 10 doctors contributed 21.8% of its total income and top 25 doctors contributed 36.1% of its total income. The company continues to focus on doctor acquisition and retention through training, research and equity participation, in order to leverage its doctor network to provide quality services at affordable costs.

Moreover, the pay-outs for the doctors are fixed with about 50% fixed pay-outs in Tier-I city and about 95% fixed pay-outs in Tier-II and Tier-III cities. As a result, the company has been able to historically maintain its doctor's cost as a percentage of revenue in the range of 19% - 21%, which it expects to sustain going forward. This has helped the company to control its costs and thus, deliver superior margins.

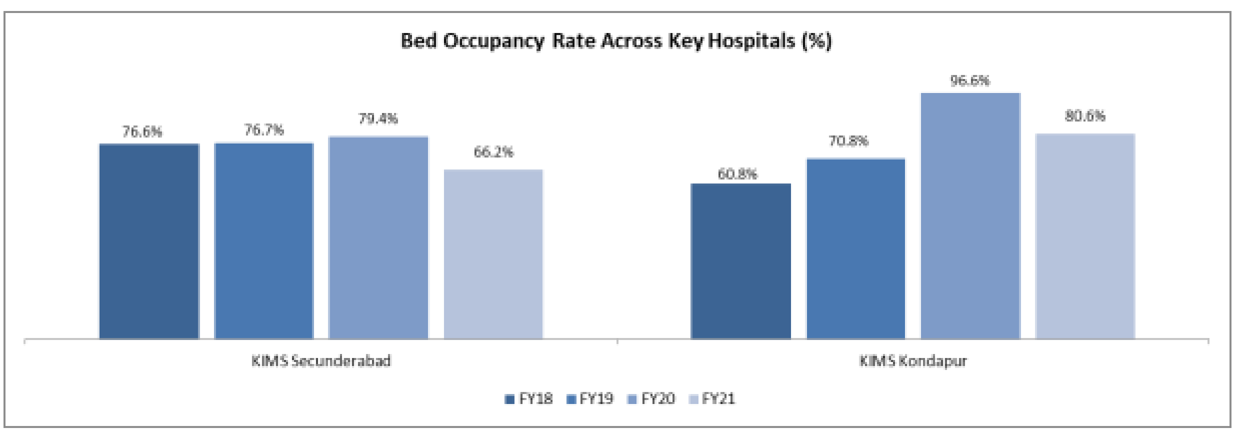
Increase in occupancy levels to drive future growth

The company had an overall occupancy level (based on total bed capacity) of 58% as of March 31, 2021. This was impacted significantly due to COVID-19, especially in the months of April and May 2020 as people chose to defer their elective surgeries due to nationwide lockdowns. The overall occupancy levels for the company are expected to normalize as impact of COVID-19 wanes out. Also, as new hospitals mature and by implementing measures to reduce its ALOS, the company aims to increase its overall occupancy levels through improved efficiency, resulting in volume and revenue growth. Historically, for the past 7-8 years, matured assets have grown at the rate of 10% - 12% per year in terms of revenue, whereas in the last 4 years, newly acquired assets have delivered revenue growth in the range of 15% -20%. As new assets mature, its occupancy rates are expected to improve. As a result, the management expects a blended topline growth in the range of 10% - 13%, going forward.



Source: Company Presentation

The overall impact of the pandemic was also visible in the company's key hospitals of KIMS Secunderabad and KIMS Kondapur, which contributed to more than 64% of the company's total revenue as of FY21. The bed occupancy rates in KIMS Secunderabad and KIMS Kondapur declined to 66.2% and 80.6% in FY21 from 79.4% and 96.6% in FY20, respectively. However, for KIMS Secunderabad, the company has been able to increase its ARPOB from Rs. 26,225 per bed in FY20 to Rs. 38,478 in FY21 by adding complex procedures such as heart, lung and liver transplants. This has resulted in improved ARPOB per day and EBITDA margins. As occupancy levels normalize, we expect the company to sustain the current ARPOB levels, which will help drive revenue growth for these two as well as other hospitals of the company.



Bed Occupancy Rate – Number of bed occupied divided by number of operational census beds (i.e. excluding day care beds like dialysis, endoscopy, emergency etc.) as of the last day of the relevant year.
Source: RHP

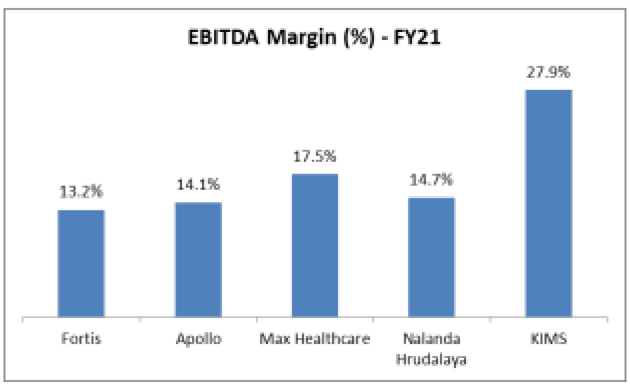
Track record of strong financial performance

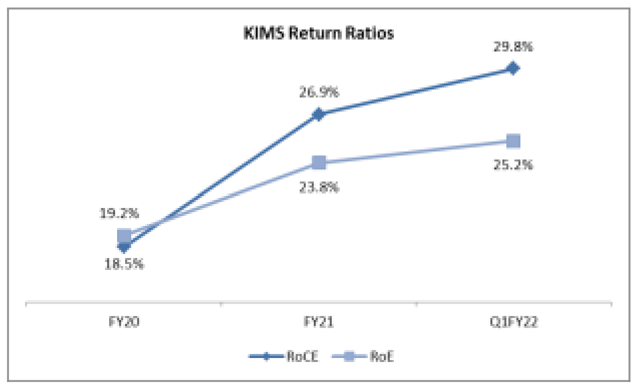
KIMS has delivered revenue CAGR of 26.0% between FY17-20. Whereas its revenue CAGR between FY19-21 was approximately 20.6%. The management expects its revenue to grow in the range of 10% - 13% sustainably. The company has one of the highest EBITDA margin amongst its peers at ~31.0% in Q1 FY22. However, this was positively impacted due to the second wave of COVID-19 and related services during the quarter. The management expects margins to normalize at its Q4 FY21 levels of c. 29%, which is still one of the highest in the industry. One of the lowest operating costs in the industry and superior margin offerings like heart, liver and lung transplant, has resulted into high margins for the company.

The major reasons for the company to be able to optimize its costs are:

- Leveraging its KIMS brand name to attract and retain doctors with fixed pay-outs, resulting in a sticky doctor's cost to revenue ratio despite revenue growth
- Able to avoid high rental costs by leasing land parcels and building its own facility for several of its hospitals

As the company achieves scale, we expect it to deliver consistent top line and bottom line growth. Despite the addition 4 new units in the last 4 years, the company was able to increase its asset turnover ratio from 1.30x in FY19 to 1.71x in FY21. The company also had one of the highest RoCE in the industry of 26.9% in FY21. The company has been able to achieve higher than industry returns due to its ability to put up a bed at lower capex per bed as compared to its peers. **Given the company's track record of adding new hospitals at lower capex as compared to its peers, we expect higher return ratios to sustain going forward. The company is currently net debt free and is well capitalized for its expansion plans. Given the favorable liquidity position and growth from future expansion, we believe that the return ratios are sustainable at the current levels.**



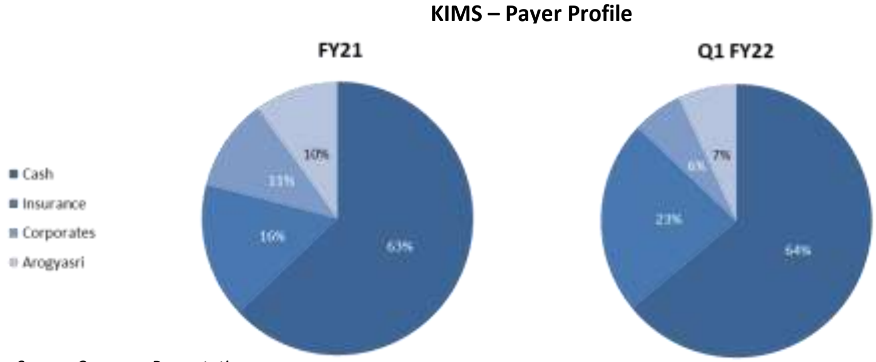


Source: Annual Reports, Company Presentations

Improving payer profile

The company has a well-diversified payer profile and is focused on further increasing the share of insurance and cash in its payer profile which are high margin contributors. In Q1 FY22, due to the impact COVID-19, there has been an increase in cash and insurance payers. However, there has been a sequential decline in in-patient and out-patient volumes due to the second wave of COVID-19 of about 3% and 30%, respectively. **As the in-patient and out-patient volumes normalize and with the company's focus on improving patient turnover through efficiency, we expect the company to sustain current levels of cash and insurance payers (Q1 FY22), which may result in improved margins.**

KIMS – Payer Profile



Source: Company Presentation

Sarvejana Healthcare Private Limited (Sunshine Hospitals) acquisition:

On October 27 2021, KIMS announced acquisition of 51.07% equity stake in Sarvejana Healthcare Private Limited, which owns and operates hospitals in and around Hyderabad, Telangana under the brand 'Sunshine Hospitals'. Sunshine Hospitals was started in May 2009 by Dr. A.V. Gurava Reddy. It currently operates across 3 locations in Telangana, out of which two are in Hyderabad - Secunderabad and Gachibowli, and the 3rd is in Karimnagar, a fast upcoming Tier 3 town. Sunshine Hospitals have combined bed strength of more than 600 beds across these 3 locations.

KIMS made this acquisition at an Enterprise value of Rs. 7.3 bn, implying an EV/EBITDA ratio of 9.7x based on Sunshine's FY21 operating EBITDA of Rs. 0.75 bn. This acquisition is in-line with the company's strategy to strengthen its presence in key markets of Hyderabad and Secunderabad. Following is a brief snapshot of Sunshine Hospital's consolidated Income Statement:

Particulars (Rs. Mn)	FY21	FY20	Growth (YoY)
Revenue	4,118	3,643	*13.0%*
EBITDA	752	331	*127%*
EBITDA Margin	18%	9%	--
PBT	465	-47	*NM*
PAT	364	-60	*NM*

Source: Company Press Release

Key Risks

- The company's revenues are highly concentrated in terms of geography as well as units. AP and Telangana are two key markets from where it derives its revenues. Also, about 52% of its revenue mix is from its flagship facility in Secunderabad. Hence, the company may face concentration risk and any negative impact on these may impact its revenues significantly.
- The company has been positively impacted due to COVID-19 outbreak. However, it might face challenges to sustain its volume and margins as the COVID-19 related cases reduces drastically.
- The company is dependent on its top-25 doctors for more than 35% of its overall revenue. Hence, doctor retention and acquisition plays a key role in sustaining its volume and revenue growth performance.
- Increase in government efforts for affordable health through various low insurance schemes such as Arogyasri has driven higher volumes for the company. Any changes in government policies or schemes may result in lower volumes though Arogyasri channel.
- Ability to replicate its business model beyond AP and Telangana possesses an important challenge for potential future growth.

Overall View

KIMS has successfully grown from a single unit in 2000 to 9 multi-specialty hospitals and is a dominant player in AP and Telangana, offering healthcare services across more than 25 specialties and super specialties. It has been able to add capacity at a significant pace, adding 940 beds in the last 4 years through organic and inorganic growth. The company follows a cluster based approach and a unique doctor retention model, which has helped achieve industry leading margins and profitability while continuing its growth momentum. KIMS has plans to add an additional capacity to the tune of about 50% in the next 3 to 4 years and as its newly acquired units mature over the next few years, its occupancy levels are also expected to improve. These two factors are expected to drive a double-digit topline growth for the company in the next 3-4 years. High margin offerings such as heart, liver and lung transplant are expected to sustain its margins despite addition of new units in the medium term. The company is trading at an EV/EBITDA of 27.2x, which seems to be much lower than comparable peers and hence the risk reward seems favorable. We initiate with a Buy rating on the stock with the target price of Rs.1,500 using EV/EBITDA multiple of 21x on FY23E EBITDA of Rs. 5.28 bn. Any earnings/target price revision would depend on the recovery in overall economic scenario, execution of expansion plans, increase in market share across services and geographies, overall occupancy levels and changes in general business momentum.

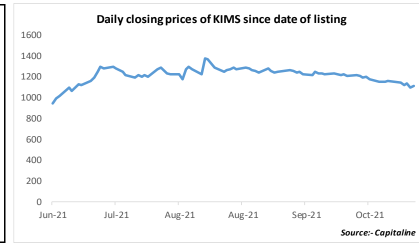
Earnings Summary

Y/E	Sales	Growth	EBITDA	Margin	Net Profit	EPS	Growth
31-Mar	**Rs Mn**	**(%)**	**Rs Mn**	**(%)**	**Rs Mn**	**Rs**	**%**
19A	9,180	38.3%	868	9.5%	503	(6.91)	NM
20A	11,226	22.3%	2,511	22.4%	1,150	16.0	NM
21A	13,299	18.5%	3,810	27.9%	2,055	26.9	68.1%
22E	15,693	18.0%	4,551	29.0%	2,646	33.1	22.9%
23E	18,204	16.0%	5,279	29.0%	3,198	40.0	20.8%

Note: Prices and Market Cap as of 29 October 2021. Source: Company Annual Reports

**Please refer to Disclaimer on the next page*

Rating Interpretation	
Rating	**Expected to**
Buy	Appreciate more than 10% over 12-18 month period
Hold	Appreciate below 10% over 12-18 months period
Under Review	Rating under Review
Exit	Exited out of model portfolio



Yellow Rating stocks

This rating is given to stocks that have strong balance sheet and are from relatively stable industries which are likely to remain relevant for long time and unlikely to be affected much by economic or technological disruptions. These stocks have emerged stronger over time but are yet to reach the level of green rating stocks. They offer medium risk, medium return opportunities. Some of these have the potential to attain green rating over time.

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