Initiating Coverage

Krishna Institute of Medical Sciences Ltd.

January 17, 2022

RETAILRESEARCH

Krishna Institute of Medical Sciences Ltd.

Industry	LTP	Recommendation	Base Case Fair Value	Bull Case Fair Value	Time Horizon
Healthcare Facilities	Rs 1442.1	Buy in the band of Rs 1438-1448 & add more on dips to Rs 1308-1312 band	Rs 1587	Rs 1709	2 quarters

HDFC Scrip Code	KRIINSEQNR
BSE Code	543308
NSE Code	KIMS
Bloomberg	KIMS IN
CMP Jan 14, 2022	1442.1
Equity Capital (Rs cr)	80.0
Face Value (Rs)	10
Equity Share O/S (cr)	8.0
Market Cap (Rs cr)	11,540.8
Book Value (Rs)	111.3
Avg. 52 Wk Volumes	447033
52 Week High	1565.0
52 Week Low	937.5

Share holding Pattern % (Dec 2021)	
Promoters	38.8
Institutions	29.3
Non Institutions	31.9
Total	100.0

HDFCsec Retail research stock rating meter

for details about the ratings, refer at the end of the report

* Refer at the end for explanation on Risk Ratings

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Our Take:

Krishna Institute of Medical Sciences (KIMS) Ltd is the largest corporate healthcare group in Andhra Pradesh (AP) and Telangana in terms of number of patients treated and treatments offered. The company is strategically focused on the southern India healthcare market where it has a strong understanding of regional nuances, customer culture and the mindset of medical professionals; and where there is growing need for quality and affordable healthcare services. It has expanded its hospital network in recent years through acquisitions; around 30% of the total bed capacity were added in the last three fiscals; adding over 880 beds. The company recently acquired 51.07% stake in Sunshine Hospitals. With this acquisition, KIMS will have a total of 12 hospitals, across 9 cities with 3666 beds (which is 1.9 times more beds than the second largest healthcare provider in AP and Telangana) and would further strengthen its presence in key home market.

KIMS has been delivering clinical excellence through quality healthcare services, supported by a combination of top medical talent and investments in new medical technology. The company is focused to offer quality healthcare services at affordable prices in their hospitals in both Tier 1 and Tier 2-3 markets, regardless of the market, specialty or service type. In Tier 1 cities, the company's prices across medical procedures are on average 20-30% lower than other private hospitals in India. Its ARPOB is significantly lower than its peers as it offers affordable quality healthcare service. There is a scope for improvement of its ARPOB given its clinical expertise, diversified specialties offerings and continuous improvement in patient management & discharge processes. Its occupancy rate (percentage of bed capacity) stands at 58% in FY21 (62.5% in H1FY22) implying a significant growth potential over a period of time which will further contribute to the company's overall growth.

Valuation & Recommendation:

KIMS has consistently delivered strong operational and financial performance through strong patient volumes, cost efficiency and diversified revenue streams across medical specialties. It reported healthy financials with revenue/EBITDA/PAT CAGR of 21%/28%/49.5% respectively over FY16-21. Doctor participation model, tight cost control coupled with prudent capital spending (low capex per bed compared to its peers) translated into healthy operating capabilities. Collaboration with doctors, which creates a culture of ownership, is one of KIMS' major strategies. Also, doctors' equity participation in the company keeps costs restricted. Strategy of acquiring land & constructing building and entering in long-term lease on low-cost terms has kept the rental expenses at minimal levels. KIMS is planning to add over 1600 beds over next three-four years with an approximate cost of Rs 9-11 million per bed marking a total outlay of Rs 1400-

1500cr (annual capex of Rs 300-400cr). While initial losses from newly set up hospitals are expected, operating margins may moderate over the medium term, but we expect margins to remain healthy.

To offer affordable healthcare service and improve its financials, KIMS is focused on improving its occupancy rates and maximizing operating efficiencies across its network. Around 15% of bed capacity is ready to get operational, supporting healthy topline growth. Strong brand reputation in South India, extensive experience of the promoters and association of renowned doctors & experienced consultants augurs well for the company's growth and margins. We expect KIMS to clock 22.7% revenue CAGR (including Sunshine Hospitals) on the back of better bed occupancy rate, increase in operational beds and improvement in ARPOB with superior clinical case mix over FY21-24E. On account of superior margin profile and operational efficiency due to healthy topline growth, we expect the company to deliver EBITDA/PAT CAGR of 20.1%/20.4% over FY21-24E. **We think the fair value of the stock is Rs 1587 (19x FY24 EV/EBITDA, 36x FY24E EPS) and the bull case fair value is Rs 1709 (20.5x FY24 EV/EBITDA, 39x FY24E EPS) over the next two quarters. Investors can buy the stock in the band of Rs 1438-1448 (17x FY24 EV/EBITDA, 32.8x FY24E EPS) and add on dips to Rs 1308-1312 band (15.5x FY24 EV/EBITDA, 29.8x FY24E EPS).**

Financial Summary

Particulars (Rs cr)	Q2FY22	Q2FY21	YoY-%	Q1FY22	QoQ-%	FY20	FY21	FY22E	FY23E	FY24E
Total Operating Income	411.7	409.6	0.5	473.2	-13.0	1,122.7	1,329.9	1,652.3	2,226.5	2,459.4
EBITDA	128.8	141.3	-8.8	143.7	-10.4	245.0	370.9	464.3	590.0	643.1
Depreciation	18.1	16.4	10.5	17.1	6.1	70.6	69.5	72.7	106.9	117.8
Other Income	5.4	1.5	255.9	4.3	25.8	6.1	10.2	13.2	16.7	24.6
Interest Cost	2.9	6.9	-58.1	6.3	-54.3	39.9	32.5	19.2	11.4	16.8
Tax	28.9	29.3	-1.4	32.5	-11.0	25.5	73.5	97.2	123.1	134.3
PAT	84.2	90.1	-6.5	92.1	-8.5	115.1	205.5	288.4	365.3	398.8
Adjusted PAT	81.7	83.5	-2.1	89.1	-8.3	115.1	201.2	292.3	323.6	351.5
EPS (Rs)	10.2	10.8	-5.1	11.1	-8.3	16.0	26.9	36.5	40.4	43.9
RoE-%						20.2	27.5	26.4	21.4	19.0
P/E (x)						90.1	53.7	39.5	35.7	32.8
EV/EBITDA						45.0	30.2	24.4	19.2	17.3

(Source: Company, HDFC sec)

Q2FY22 Result Review:

In Q2FY22, Krishna Institute of Medical Sciences (KIMS) Ltd reported decent revenue of Rs 411.7cr (+0.5%/-13% YoY/QoQ). Covid revenues in the base period impacted revenue growth. Overall, the business exhibited normalization as Covid-19 cases (~5-7% of revenue in Q2FY22) gradually declined across India and elective surgeries picked up. Increased patient flow, new doctor additions in existing specialties, increasing normalization of business to pre-covid levels contributed to the growth during the quarter. The company saw an improvement in its gross margins; up 277bps /297 bps YoY/QoQ to 79.2%, primarily due to favourable specialty mix. Tighter control on medical consumption cost and operational leverage (higher occupancy and robust IP/OP volume) supported healthy EBITDA margin of 31.3% as against 30.4% in Q1FY22 (34.5% in Q2FY22; mainly on account of high covid revenue share). The acquired asset reported significant improvement in EBITDA margin to 20.7% in H1FY22 (vs 16.8% in FY21). The company's EBITDA stood at Rs 128.8cr (-8.8%/-10.4% YoY/QoQ). KIMS reported PAT of Rs 81.7cr.

KIMS's occupancy stood at 59.8% in Q2FY22 as against 55.1% in Q2FY21 (62.2% in the previous quarter). The company's occupancy rate improved 470bps YoY due to pick up in elective surgeries. Average revenue per operating bed (ARPOB) improved to Rs 24,887 (down 5.8%/8.8% YoY/QoQ) compared to Rs 21,591 reported in Q4FY21 (similar period due to low covid revenue) due to increase in complex surgeries and procedures. Average length of stay (ALOS) improved from 5.06 days in Q4FY21 and 5.47 days in Q1FY22 to 4.61 days in Q2FY22. The company saw robust out-patient (OP) & in-patient (IP) growth across the hospitals during the quarter. IP discharged volume increased to 36,205 in Q2FY22 against 31,709 in the previous quarter. IP volume increased up 25.4% YoY as volume for major specialties has increased on account of normalization. OP consultation volume increased to 2.80 lakhs (+54.7%/53.6% YoY/QoQ).

	FY19	FY20	FY21
Revenue (Rs cr)	918.0	1,122.7	1,329.9
Revenue from inpatients (Rs cr)	717.7	879.9	1,048.1
Inpatient Volume	1,11,382	1,40,676	1,16,592
Revenue from outpatients (Rs cr)	195.6	238.8	280.0
Outpatient Volume	9,00,043	11,37,560	8,30,211

	FY19	FY20	FY21	H1FY22
Bed Capacity	2804	3004	3064	3064
Operating Beds	2209	2434	2590	-
Occupancy (% of Total Bed Capacity)	48.7%	55.7%	57.6%	62.50%
ARPOB (Rs)	18,334	18,307	20,609	25,406
ALOS (days)	4.47	4.34	5.53	-

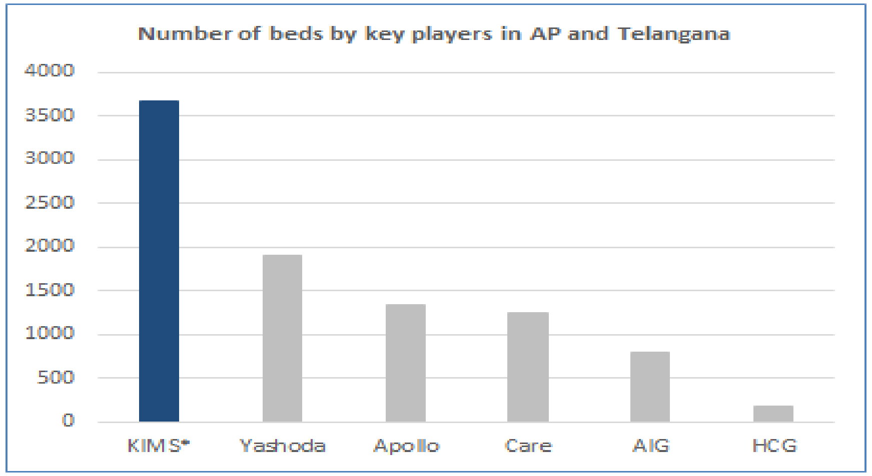
(Source: Company, HDFC sec)

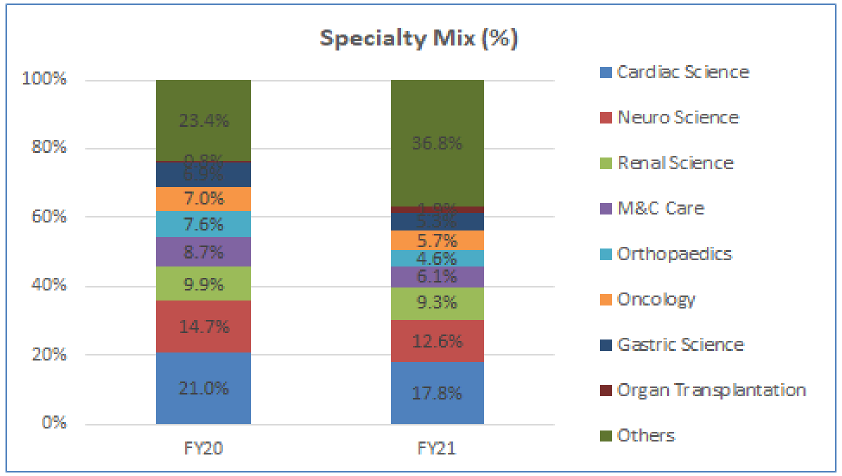
Key Triggers:

Established market position in Andhra Pradesh and Telangana:

KIMS through its network of 9 hospitals (3064 beds) under the "KIMS Hospital" brand has established a strong presence in the South Indian market. The group has a long operational track record of 16 years in the tertiary and the quaternary healthcare segments and also benefits from the strong brand reputation and extensive experience of the group's promoters. It enjoys leadership position in the region due to higher number of operational beds and proven quality services. KIMS has been delivering clinical excellence through quality healthcare services, supported by a combination of top medical talent and investments in new medical technology. KIMS is associated with renowned doctors in the region, it also collaborates with premier medical institutions to hire top talents.

KIMS is strategically focused on the healthcare market in South India where it has a deep understanding of regional nuances, customer culture and medical professionals. Also, there is supply-demand gap in quality and affordable healthcare services in AP and Telangana which provides KIMS with substantial growth opportunities in the regions. KIMS' hospitals at Secunderabad (Telangana), Rajahmundry (AP) and Kondapur (Telangana) are NABH accredited and many of its other hospitals are in the accreditation process. The group's Secunderabad facility is one of the largest single location hospitals with 1000 beds, offering multi-specialties. With recent acquisition of Sunshine Hospital, KIMS will have 12 hospitals across 9 cities with 3666 beds. The acquisition is further expected to enhance market presence in their core market - Hyderabad.





(*including Sunshine Hospitals)

(Source: Company, HDFC sec)

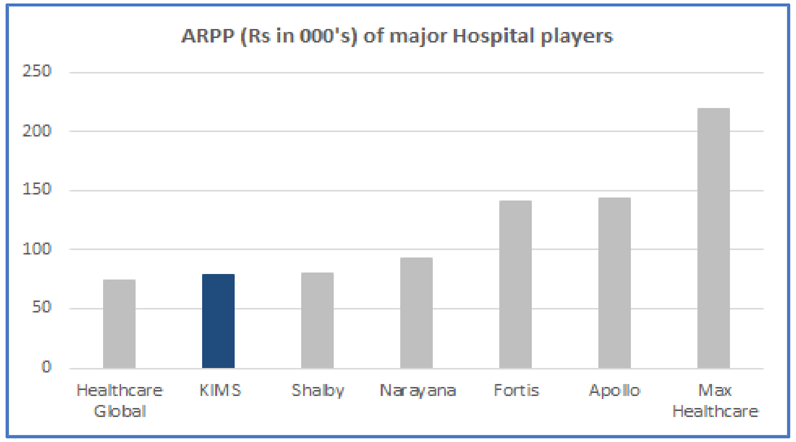
Comprehensive Range of Specialties and Clinical Excellence:

KIMS is focused on providing complex and advanced quaternary healthcare in various specialties. It offers comprehensive range of services across 25+ specialties and super-specialties using modern technology. These include cardiac sciences, oncology, neurosciences, gastric sciences, orthopaedics, organ transplantation, renal sciences and mother & child care. KIMS is running one of India's largest ECMO and Heart and Lung Transplant programs. It provides treatment for complex and chronic diseases covering primary, secondary, tertiary and quaternary healthcare. Offering multi-specialty treatments in the hospitals has improved the quality of care towards the patients. KIMS is focused on delivering clinical excellence through quality healthcare services, supported by a combination of top medical talent, strong clinical and patient safety protocols and investments in new medical technology. Its ability to attract, train and retain high quality doctors, consultants and medical support staff has helped the company to offer such quality services.

Multispecialty healthcare platform has resulted in diversified revenue streams, with no single specialty accounting for more than 25% of total income in the last three years. In terms of specialties, cardiac treatments account for the highest share of revenues at ~21% (FY20), followed by neuro sciences ~15% and renal sciences ~10%. The balance is spread across oncology, mother and child, gastric sciences, orthopaedics. KIMS is diversifying across clinical specialties and expanding its ability to provide complex and advanced quaternary healthcare in various specialties. The company is developing complicated specialist-skills in areas such as Organ Transplant, Mother & Child Care, and oncology. In the area of organ transplantation, the company recently expanded clinical team in Secunderabad (Telangana) to provide heart and lung transplants in addition to other organ transplant services (liver and kidney, among others). It also aims to strengthen oncology services by adding radiation and surgical services, and launch mother & child care services in more hospitals. The management has communicated their plans to add cancer centre in Vizag, Anantpur and Ongole. The company is also adding mother & child care unit in Anantpur. KIMS has a strong position established in the field of cardio, neuro, and renal care; with acquisition of Sunshine Hospitals, the company would see higher share of its revenue from the field of Orthopaedics (ex-Sunshine ~4.6% of revenue). Because of its diversified presence across major specialities, KIMS has managed to minimize revenue concentration risk.

Affordable pricing model - to support growth:

KIMS is focused to offer quality healthcare services at affordable prices in their hospitals in both Tier 1 and Tier 2-3 markets, regardless of the market, specialty or service type. In Tier 1 cities, the company's prices across medical procedures are on average 20-30% lower than other private hospitals in India. In FY20, KIMS' average revenue per patient (ARPP) stood at Rs 79,526, which is 41% lower than the industry average of Rs 112,000 (Crisil estimates). To maintain and improve its profitability with its affordable pricing model, the company rationalizes doctor, medical consumables & procurements and other administrative costs. Doctors' costs are a mix of fixed and variable arrangements based on patient volumes. Also, the company follows doctors' equity participation model; which keeps this expense at modest levels. KIMS' focus on teaching and research has helped it to attract and retain high quality doctors and healthcare professionals at an affordable cost. Also given that ~60% of hospital beds are in Tier 2-3 cities; doctor, nursing staff and other paramedical staff cost is relatively lower, which also justifies low ARPOB. The company has centralized supply chain operations, vendor management, compliance and administrative functions; which allows operational leverage and secure favourable pricing from vendors for medical equipment and consumables. The company secures land for long term on low-cost terms to avoid high fixed rentals. Due to its strong brand and two-decade experience in South Indian region; high percentage of walk-in patients & outpatient, aid in controlling operating costs. On the back of operating leverage derived from higher volume, it delivered highest EBITDA margins (28%+) as compared to average industry margins (<20%). The company achieved this by controlling capital and operating expenditure along with a multidisciplinary approach.



Hospitals	Ownership	Bed capacity	Owned or Lease
Secunderabad	100%	1000	Perpetual Lease
Nellore	100%	250	Part owned and part leased (30 years)
Rajahmundry	100%	180	Part owned and part leased
Srikakulam	57.83%	200	Owned
Kondapur	86.32%	200	Leased (10 years)
Ongole	100%	350	Owned
Vizag	51%	434	Operation & Management
Anantapur	80%	250	Owned
Kurnool	55%	200	Owned

(Source: Company, HDFC sec)

Ability to attract, and retain high quality doctors & Doctor Participation Model:

The company maintains standard of high-quality healthcare by consistently employing diverse pool of talented doctors, nurses and paramedical professionals. Multi-disciplinary approach, combined with affordable cost for treatment, a high-volume tertiary care model, and focus on teaching and research, has helped in attracting and retaining high quality doctors and other healthcare professionals. It also collaborates with premier medical institutions to hire top talents. KIMS has created a culture of ownership – its doctors actively participate in the equity ownership of the company and its subsidiaries and thus are involved in the company's growth. As of March 31, 2021, doctors (in the case of KIMS Anantapur, the management team of its predecessor), held stakes of 45%, 49%, 39%, 20% and 0.46%, in hospitals at Kurnool (AP), Vizag (AP), Srikakulam (AP), Anantapur (AP) and Kondapur (Telangana), respectively, which are the hospitals that KIMS hold through its subsidiaries. In addition to this, doctors held an aggregate stake of 6.92% of the company, which directly owns hospitals at Secunderabad (Telangana), Nellore (AP), Rajahmundry (AP) and Ongole (AP).

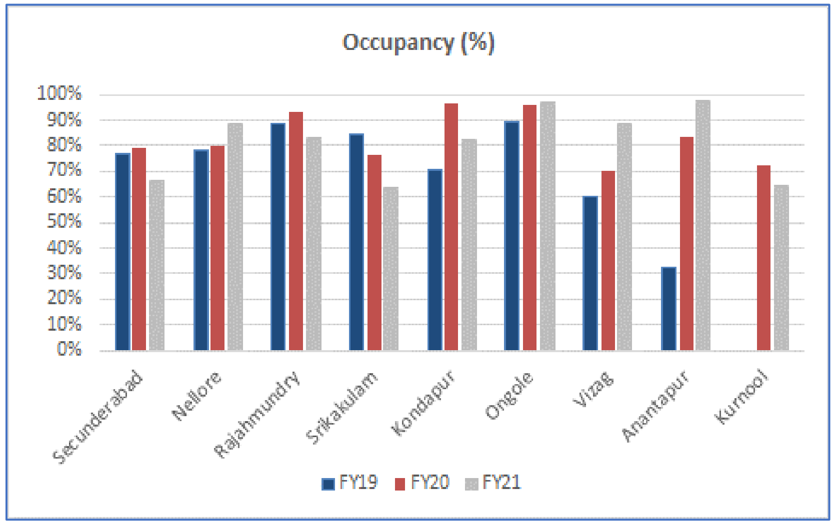
Doctors' ownership details

Name of company/ subsidiary	Hospital Name	Shareholding % of the company in the Subsidiary	Shareholding % of doctors in the company/subsidiary
KIMS	KIMS Secunderabad, KIMS Nellore, KIMS Rajahmundry and KIMS Ongole*	NA	6.92%
KHKPL	KIMS Kurnool	55.0%	45.0%
ICIMSPL	KIMS Vizag	51.0%	49.0%
AHPL	KIMS Srirakulam	57.83%	39.16%
SIMSPL	KIMS Anantapur	80.0%	20.0%^
KHEPL	KIMS Kondapur	86.32%	0.46%

(*owned directly by the company, ^ Includes the shareholding of the management team of the predecessor of KIMS Anantapur) (Source: Company, HDFC sec)

Improvement in occupancy levels – support healthy revenue growth and margin level:

The company reported strong revenue growth over FY18-21 due to its focus on improving average bed occupancy while decreasing average length of stay (ALOS) (as significant portion of in-patient revenues are derived from medical services in the initial 2-3 days). Over the last four years, KIMS has added ~30% of the total 3,064 beds on account of demand opportunities. Despite bed additions both through organic expansions as well as strategic acquisitions, occupancy levels have improved. Higher occupancy rates were due to its ability to recruit high-quality doctors and offer high quality care at affordable prices, while the decrease in ALOS was the product of adoption of improved medical technology, advancements in medical treatments and more efficient processes for patient diagnosis. To offer affordable healthcare service and improve its financials, KIMS is focused on improving its occupancy rates and maximizing operating efficiencies across its network. Around 15% of bed capacity is ready to get operational, supporting demand. Four facilities (Kondapur, Ongole, Vizag and Anantapur) currently operating at higher utilisation levels have around 25% of bed capacity ready to operationalise; adding incremental revenue without extra capex. The company is look to improve occupancy levels for three of its facilities (Secunderabad, Srikakulam and Kurnool). Sunshine Hospitals has reported poor occupancy levels of 40%, the management is confident of scaling it up substantially by adding specialties and its clinical team of doctors; thereby adding to the topline. In the short to medium term, additional capacities in AP and Telangana should drive growth for KIMS, while capex in other cities (Chennai and Bengaluru) should start yielding after FY24.



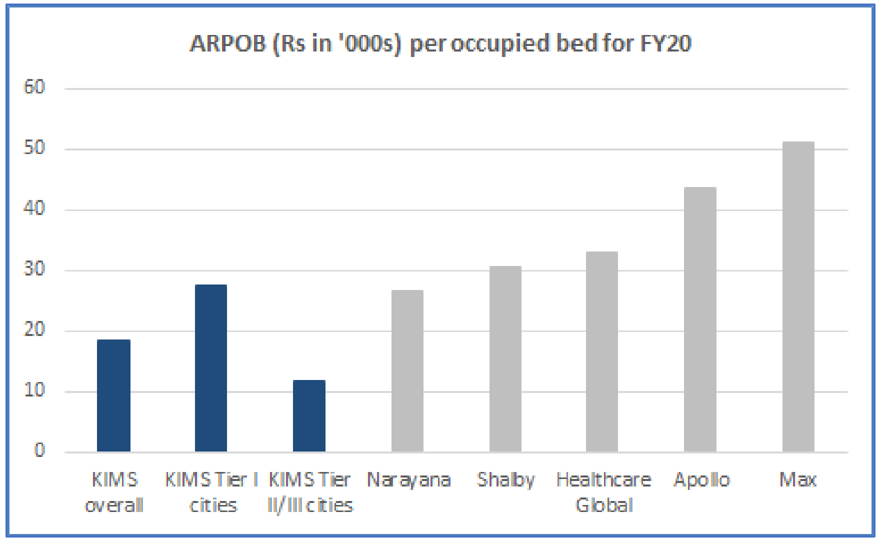
(Occupancy levels: Number of beds occupied divided by number of operational beds)

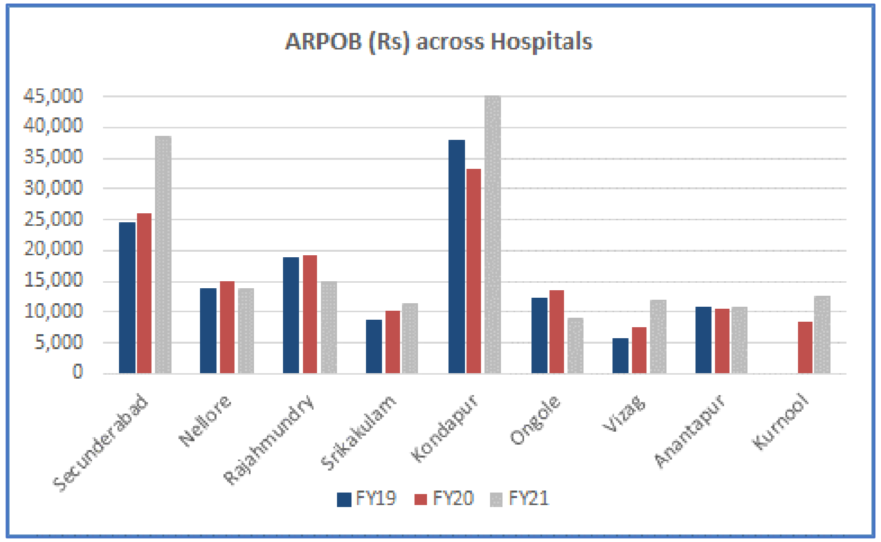
Hospital	Year	Ownership	Bed capacity	Operational beds	Tier 1 or Tier 2-3 cities
Secunderabad	2004	100%	1000	885	Tier 1
Nellore	2000	100%	250	250	Tier 2-3
Rajahmundry	2002	100%	180	180	Tier 2-3
Srikakulam	2014	57.83%	200	150	Tier 2-3
Kondapur	2014	86.32%	200	150	Tier 1
Ongole	2017	100%	350	246	Tier 2-3
Vizag	2019	51%	434	314	Tier 2-3
Anantapur	2019	80%	250	215	Tier 2-3
Kurnool	2020	55%	200	200	Tier 2-3

(Source: Company, HDFC sec)

Focus on improving realisations:

KIMS has consistently delivered strong operational and financial performance through strong patient volumes, cost efficiency and diversified revenue streams across medical specialties. Despite bed additions both through organic expansions as well as strategic acquisitions, its ARPOB increased to Rs. 20,609 (FY21) from Rs 16,775 (FY15) indicating improvement in services provided. Its ARPOB is significantly lower than its peers as it offers affordable quality healthcare service. There is a scope for improvement of its ARPOB given its clinical expertise, diversified specialties offerings and continuous improvement in patient management & discharge processes. Hospitals in Tier 1 markets provide higher margin services such as organ transplants, oncology and neuro-critical care, resulting in higher ARPOB (Rs 39,571 in FY21) and EBITDA. Hospitals operating in tier 2-3 cities (ARPOB of Rs 11,187 in FY21) have potential to improve ARPOB.





(Source: Company, HDFC sec)

Acquisition of Sarvejana Healthcare Private Limited (Sunshine Hospitals):

KIMS recently announced the acquisition of 51.07% stake in Sarvejana Healthcare Private Limited (SHPL) (Sunshine hospitals group) for a total cash consideration of Rs 362cr. The company will initially acquire 18.52% stake in SHPL, and up to 51.07% by March 31, 2022, when partly paid shares will be fully paid-up. SHPL will become a subsidiary of KIMS effective April 1, 2022. Sunshine Hospitals currently operates at three locations in Telangana, out of which two are in Hyderabad (Secunderabad and Gachibowli), and the third is in Karimnagar (Telangana), a fast-upcoming Tier 3 town. With total bed strength of 602, the acquisition will help KIMS Hospitals to consolidate its position as a leading provider of tertiary care services in its key markets and add a world-renowned orthopaedic surgical team led by Dr. A. V. Gurava Reddy. It is the No.1 player in the Joint replacement and Spine department with over 4,000 knee transplants a year. It would augment and complement KIMS Cardio, Neuro, Transplant, and Renal sciences team. The acquisition is expected to be EPS accretive immediately, as SHPL has an enterprise value of Rs 730cr; acquisition valued at 9.7x EV/EBITDA (FY21) (much lower than the industry).

Consolidated Financial Snapshot and operational parameters

	FY20	FY21
Bed Capacity (nos)	602	602
Occupancy %	39.60%	39.80%
IP Volume (nos)	21,970	17,515
ARPOB (Rs)	22,728	26,125
Revenue (Rs cr)	364.3	411.8
EBITDA (Rs cr)	33.1	75.2
EBITDA %	9.1%	18.3%
PBT (Rs cr)	-4.7	46.5
PAT (Rs cr)	-6	36.4

Hospital-wise key data

	Secunderabad		Gachibowli		Karimnagar	
	FY20	FY21	FY20	FY21	FY20	FY21
Revenue (Rs cr)	235	274	84.7	129	12.1	13.4
EBITDA (Rs cr)	32.3	53.4	5	28.1	1.4	1.9
EBITDA %	14%	20%	6%	22%	12%	14%
ARPOB (Rs)	33,651	43,683	29,324	35,697	13,205	16,451
ARPP (Rs in '000s)	136	218	113	197	46	53
ALOS (days)	4.1	5	3.9	5.5	3.5	3.2

(Source: Company, HDFC sec)

Sunshine Hospitals reported a revenue of Rs 411.8cr (revenue growth of 11.1% CAGR over the last two years) and healthy EBITDA margins of 18.3% in FY21. It reported operating EBITDA of Rs 75cr with 18% margin in FY21 (v/s 9% in FY20). It posted PAT of Rs 36cr in FY21 (vs net loss of Rs 6cr in FY20). Although SHPL is a profitable hospital, its operating margins are lower compared with KIMS. KIMS' management would start exploring cost and operational synergies. Adding new clinical specialties and strengthening existing ones could improve the current low occupancy level of 40%. Optimizing consumables costs given its scale benefits would help improve its margin. Margin levels of KIMS' matured units are unlikely to be reached as all three hospitals are on rented premises.

The acquisition of SHPL will enhance the presence of KIMS in Telangana with addition of 3 hospitals of SHPL in similar geographies, and also enable the company to benefit from expertise of orthopedic specialties, which SHPL is renowned for. Post-acquisition of majority stake in SHPL, KIMS will have a total of 12 hospitals, across 9 cities with 3666 bed capacity. We believe that the acquisition was at reasonable valuation and will accelerate the growth momentum for the company.

Disciplined inorganic growth:

KIMS, in the past, has a demonstrated track record of maintaining prudence in its expansion plans as indicated by its low dependence on external debt, despite steady organic and strategic inorganic expansions. Disciplined, low-leverage approach to acquisitions that enabled KIMS to maintain affordable pricing model as it enhances its presence in both Tier 1 and Tier 2-3 markets. Since FY17, the company has expanded its hospital network mainly through inorganic route. It acquired hospital in Ongole (AP), a 350-bed multispecialty hospital founded by local doctors, through a slump sale in FY17. It expanded its hospital network to add KIMS Vizag, a 434-bed multispecialty hospital in April 2018 by entering into a service agreement. It acquired a 250-bed hospital in Anantapur (AP) in October 2018 and a 200-bed hospital in Kurnool (AP) in April 2019, which solidified its presence in southern AP and adjoining areas of Karnataka. Strategy of acquiring land & construction building and entering in long-term lease on low-cost terms has kept the rental expenses at minimal levels. Low capex per bed in the past and limited rentals has been instrumental in improving its EBITDA margin level and achieving break-even at newer hospitals in lesser time period. In FY20, capex per bed was Rs 6.3 million for hospitals in Tier 1 cities and Rs 2.2 million for hospitals in Tier 2-3 cities; as against industry average of Rs 5-8 million in Tier 1 cities and Rs 1-5 million in Tier 2-3 cities (Crisil estimates). On the back of rich talent pool and affordable pricing due to its operational efficiency; occupancy levels of acquired assets have seen drastic improvement in short span of time.

Expansion Strategy – Consolidating position in existing markets & strategically increasing presence in the adjacent markets:
KIMS is focused on building multi-specialty facilities across its network. It plans to scale up its existing hospitals to add new clinical therapies such as Transplants, oncology, mother & child care. It is in talks to add cancer centre in Vizag, Anantpur and Ongole. The company is also adding mother & child care unit in Anantpur. The management is actively looking for greenfield and brownfield expansion opportunities and could further explore untapped geographies in existing markets of AP & Telangana; before setting its foot in adjacent regions. The company has identified new land parcel in Kondapur and have entered a long-term agreement.

Expansion Plan (Timeline, Additional beds and Capex)

Units	Current Beds	Incremental Beds	New Departments	Approx. Capex (Rs cr)	Approx. Timeline (Starting April 2021)
Kondapur	200	500	All Specialities	300	36-42 months
Vizag	434	50	Cancer Centre	15-20	24 months
Anantapur	250	150	Cancer Centre / Mother & Child	50-60	36-48 months
Ongole	350	-	Cancer Centre	15-20	36-42 months
Bangalore	-	350-400	All Specialities	300-330	36 months
Chennai	-	350-400	All Specialities	400	36 months
Western / Central India	-	250-300	All Specialities	300	24-36 months

(Source: Company, HDFC sec)

KIMS is planning to add over 1600 beds over next three-four years with an approximate cost of Rs 9-11 million per bed (much higher than its historical rate) marking a total outlay of Rs 1400-1500cr (annual capex of Rs 300-400cr). As part of its hospital development and acquisition strategy, KIMS has selected sites for its hospitals that have sufficient land area and basic infrastructure to support a flagship-sized hospital. KIMS is planning to expand its hospital network in adjacent regions. Initially, the company will focus on:

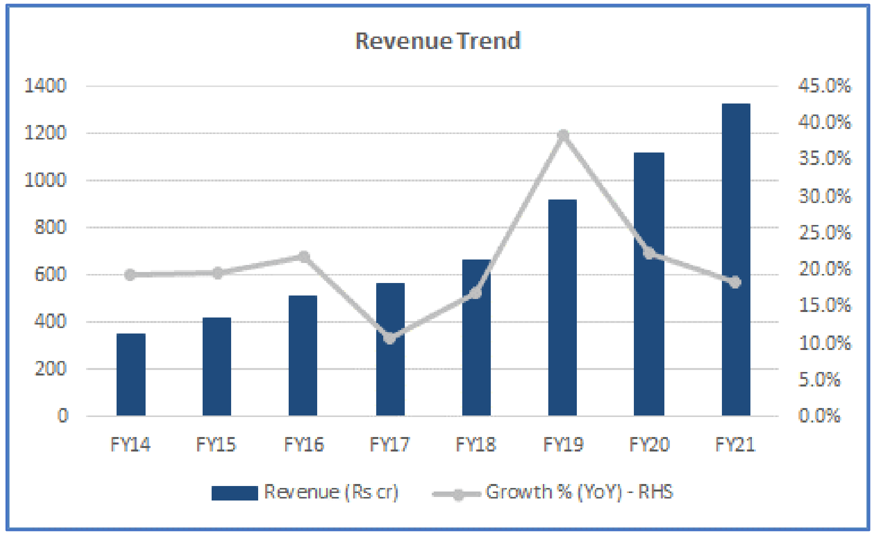
- Karnataka (Bangalore and greater Karnataka) as the region has the potential to support new hospitals that offer quality and affordable healthcare.
- Odisha (Bhubaneswar), which will be an extension of its existing hospital northward given the state's proximity to hospitals in Vizag and Srikakulam in AP (already serving significant number of patients traveling from south Odisha)
- Tamil Nadu (Chennai), where KIMS has acquired a land parcel for construction of a new facility in the future. A 400-bed facility with additional opportunity to scale is already in pipeline, the company has already procured land and is expected to receive necessary approvals in couple of months.
- Central & Western India (Indore, Aurangabad, Nagpur, and Raipur) where KIMS' brand awareness is strong and attract patients at their flagship hospital in Secunderabad for complex care. It provides KIMS with substantial growth opportunities in the region. KIMS is expected to announce expansion in Maharashtra (in Metro city).

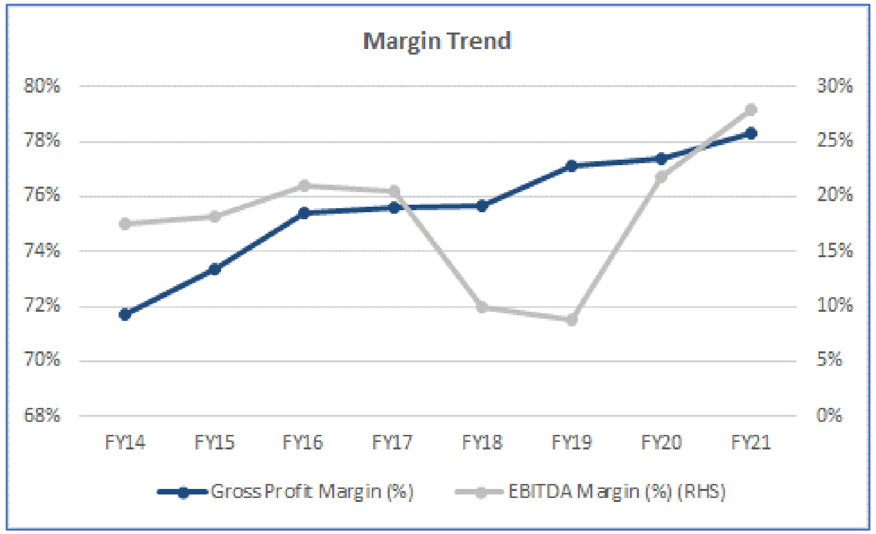
KIMS has successful history of sourcing, executing and integrating acquisitions. It intends to leverage its acquisition experience to successfully identify, execute and integrate new opportunities, including by entering into O&M arrangements with third party healthcare service providers. It also intends to explore opportunities for expansion via asset-light models. These may include revenue sharing arrangements, management fee-based arrangements or acquisition of other players in the healthcare sector undertaking operation and management of hospitals.

Robust operating & financial performance:

KIMS reported high operating profitability, despite constant capacity addition, mainly through acquisitions. The company has been maximizing its operating efficiencies across its network as it is critical for maintaining and improving the affordability of healthcare services and, profitability. The policy of providing equity partnership to its key doctors, have enabled the company to attract talent in Tier 2-3 locations and maintain low attrition levels and tight control over costs. These factors coupled with prudent capital spending (low capex per bed compared to its peers) has helped KIMS to turn around acquired hospitals as well as achieve break-even at newer hospitals in a short span of time, translating into healthy operating capabilities. Strategy of acquiring land & construction building and entering in long-term lease on low-cost terms has kept the rental expenses at minimal levels. KIMS has achieved the highest EBIT margins in the industry due to its unique business model - controlling doctors' costs (doctor participation model) and limited rental expenses.

KIMS has a demonstrated track record of maintaining prudence in its expansion plans as indicated by its low dependence on external debt, for organic and strategic inorganic expansions. Funds for recent acquisition of Sunshine Hospitals are met from cash surpluses and internal accruals. Additional capex spends of over Rs 1300-1400 crore spread over the next 3-4 years will involve partial debt funding. We expect debt levels to remain comfortable. Healthy profitability and increasing occupancy levels, have enabled a steady improvement in the company's return on capital employed (RoCE), which stood at ~27% in FY21, compared with ~13-17% in earlier years. While initial losses from newly set up hospitals is expected, operating margins may moderate over the medium term, but we expect margins to remain healthy. It aims to improve its occupancy rates and the utilization of key equipment and operating theatres by expanding delivery of tertiary care services, growing preventive healthcare and health screening programs and increasing community outreach programs.





(Note: Consolidated numbers; Source: Company, HDFC sec)

Industry Insights & Triggers:

Hospitals in India has long runway to growth with lower number of doctors/bed relative to total population, healthcare spends as percentage of GDP to the global averages. Low healthcare expenditure in India is primarily due to under-penetration of healthcare services and lower consumer spending on healthcare. This indicates that there is tremendous scope for enhancing healthcare services penetration in India and ample opportunity for the development of the healthcare industry as a whole. The demand outlook for healthcare services is positive in the long-run, due to growing awareness of healthcare issues, under-served nature of the sector, better affordability through increasing per capita income, and widening medical insurance coverage. India offers affordable healthcare treatment to many developing countries encouraging inbound medical tourism. Treatment for major surgeries in India costs approximately 1/5th of developed countries. A rare combination of world-class hospitals, equipped with best-in-class technology, skilled medical professionals, low treatment costs, and process improvements like e-medical visa, have made India a preferred destination for medical tourism.

The Indian healthcare delivery system has seen consolidation in recent years. A highly competitive industry, coupled with tightening of healthcare regulations, has made it difficult for smaller players in the industry to stay profitable. Larger hospital brands typically have stronger financial discipline and negotiating power with suppliers, better ability to attract medical talent, and greater capital and administrative resources to meet these needs over standalone hospitals. Many of the established players in the healthcare delivery industry follow inorganic growth to expand into the geographies where they have limited presence. In terms of supply creation major hospital chains have expanded into the next level of creamy tier 2 and 3 locations (with ~67% aggregate bed additions by 10 large hospitals players in the past four years being in these areas).

India's huge demand-supply gap, rising health insurance penetration, high out-of-pocket spends, increase in medical tourism provide compelling growth prospects for the industry. The adoption of asset-light models of expansion, enhanced focus on retail formats – pharmacy, diagnostics and digital initiatives – are expanding avenues of growth while keeping the balance sheet light. Private players remain the key growth contributors, around 68% of the treatments in value terms in FY20. The Indian healthcare delivery market at Rs 4.3 trillion in value terms (1.7 billion treatments in volume terms - inclusive of both in-patient and out-patient) in FY21 and is expected to increase at 17-18% CAGR to Rs 7.07 trillion by FY24E (Crisil estimates). In value terms, the IPD is expected to account for nearly 69%, while OPD is likely to account for the remaining. The share of IPD (in value terms) is expected to grow to nearly 74% in FY24.

Concerns:

Geographic concentration risk: The company has its operations in the states of Andhra Pradesh and Telengana. Economic slowdown in these regions or any new adverse regulation imposed by state authorities would impact its operations and profitability. Although, KIMS has taken steps to expand its presence in adjacent states, contribution from these states to topline and EBITDA would only happen after FY24/FY25 (unless KIMS opts for inorganic route for expansion prior to the said period).

High reliance on single facility: The company's flagship hospital in Secunderabad (~35% of total operational beds) contributes ~51% of the revenues and 63% of EBITDA in FY21. While contribution of Secunderabad unit has reduced in the recent years (55.8% in FY19); operationalizing existing bed capacity coupled with higher occupancy levels of acquired assets (existing for <4 fiscals) would reduce this concentration. Addition of 3 Sunshine hospitals would limit the dependence on their flagship 1000 bed hospital.

High competition: The healthcare sector is competitive, as increasing healthcare providers (newer and existing hospitals, low-cost nursing homes, etc) try to establish themselves among patients. Increasing subsidies from the government and improvement in services from the government hospitals may cause attrition in patients and disrupt business sustainability. With the advancing technology and newer medical interventions, several hospitals are evolving with their services as well.

Delay in project execution: The company has set timelines for increasing its bed capacity and its entry in new markets. As the company believed in procurement of land and construction of building; approvals regarding the same could take time. Delay in commissioning of these projects would impact its topline growth. Also, upfront capex for additional capacity is high due to land acquisition; debt funding would be required. Any higher-than-expected debt-funded capex would adversely impact coverage and leverage metrics.

Retention of doctors: Retaining doctors has always been a key challenge for the company and the healthcare industry due to high competition. Given its doctor participation model (senior doctors have stake in subsidiaries & company), KIMS has lower attrition compared to its peers.

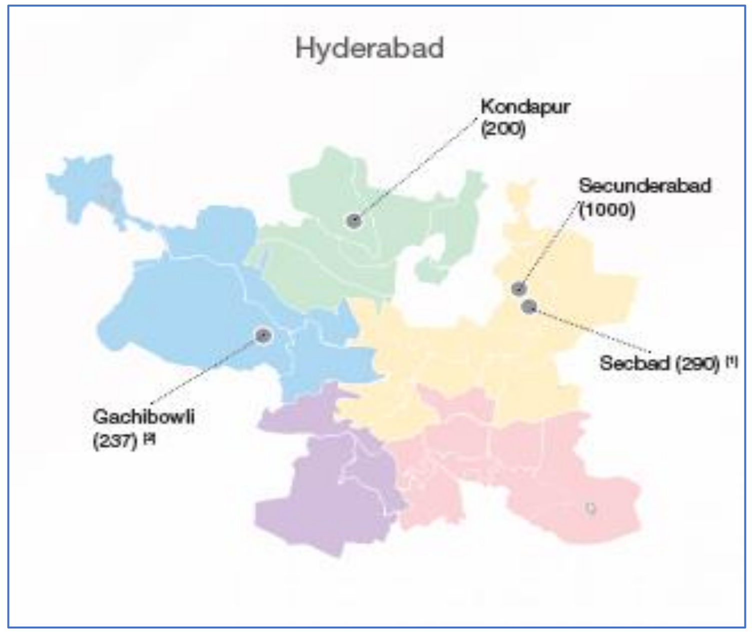
Price Regulation: The National Pharmaceutical Pricing Authority has in the past set ceilings ceiling on prices of cancer drugs, cardiac stents, drug eluting stents, condoms and intra-uterine devices. Government regulating prices for critical medical treatment which private hospital charges from patient remains a risk to revenues and margins.

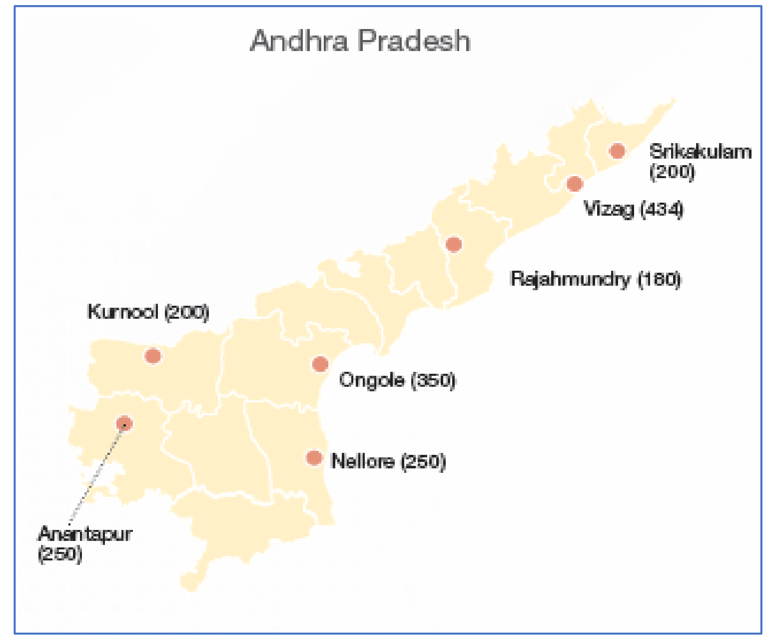
About the company:

Krishna Institute of Medical Sciences (KIMS) Ltd is the largest corporate healthcare group in Andhra Pradesh (AP) and Telangana in terms of number of patients treated and treatments offered. It provides multi-disciplinary integrated healthcare services, with a focus on primary secondary & tertiary care in Tier 2-3 cities and primary, secondary, tertiary and quaternary healthcare in Tier 1 cities. It offers a comprehensive range of healthcare services across 25+ specialties and super specialties, including cardiac sciences, oncology, neurosciences, gastric sciences, orthopedics, organ transplantation, renal sciences and mother & child care.

KIMS operates 9 multi-specialty hospitals spread across eight cities with an aggregate bed capacity of 3,064 with >2,500 operational beds. Its flagship hospital in Secunderabad has a capacity of 1,000 beds. It has expanded its hospital network in recent years through acquisition of hospitals; Ongole in FY17, Vizag and Anantapur in FY19 and Kurnool in FY20. Around 30% of the total bed capacities were added in the last three fiscals (adding over 880 beds). KIMS, in Oct 2021, has entered into definitive agreements with the shareholders of Sarvejara Healthcare Private Limited (Sunshine Hospitals) to acquire 51.07% stake for total cash consideration of Rs 362cr (as a combination of 18.52% stake through equity shares and the remainder through partly paid-up equity shares, which shall be fully paid up by April 2022). With this acquisition, KIMS will have a total of 12 hospitals, across 9 cities with 3666 beds (which is 1.9 times more beds than the second largest healthcare provider in AP and Telangana) and would further strengthen its presence in key home market. KIMS is strategically focused is on the southern India healthcare market where it has a strong understanding of regional nuances, customer culture and the mindset of medical professionals; and where there is growing need for quality and affordable healthcare services.

KIMS reported healthy financials with revenue/EBITDA/PAT CAGR of 21%/28%/49.5% over FY16-21 with average EBITDA margin of 18%+. It reported above average operating profitability, despite constant capacity additions, both organic and inorganic. Doctor participation model, tight cost control coupled with prudent capital spending translated into healthy operating capabilities. Despite bed additions both through organic expansions as well as strategic acquisitions, occupancy levels improved. ARPOB has also increased to Rs 20,609 in FY21 from Rs 16,775 in FY15 indicating improvement in services provided. Strong brand reputation in South India, extensive experience of the promoters and association of renowned doctors & experienced consultant's augurs well for the company's growth and superior margins.





(Note: The map plotting includes Sunshine Hospitals, there is one more Hospital of Sunshine group - Karimnagar (Telangana)) (Source: Company, HDFC sec)

Hospital-wise key financial and operational data

Hospital	Hospital revenue (Rs cr)	Revenue (2 years CAGR) (%)	Revenue from inpatients (Rs cr)	Revenue from outpatients (Rs cr)	EBITDA margin (%) FY20	EBITDA margin (%) FY21	Bed occupancy rate (%)	ARPOB (Rs) FY20	ARPOB (Rs) FY21	ALOS (days)
Secunderabad	684.5	16.9%	575.9	108.6	27.9%	34.8%	66.2%	26,225	38,478	5.0
Nellore	94.4	5.6%	60.2	34.2	25.2%	29.4%	88.7%	15,155	13,563	5.1
Rajahmundry	75.0	5.2%	47.5	27.4	22.7%	26.1%	82.8%	19,302	15,035	4.8
Srikakulam	36.0	-0.1%	23.8	12.1	18.5%	14.5%	63.8%	10,322	11,445	4.9
Kondapur	161.7	17.6%	132.3	29.6	24.7%	25.6%	82.2%	33,388	44,965	3.9
Ongole	72.7	22.7%	48.3	24.4	16.4%	31.6%	96.7%	13,548	8,915	8.2
Vizag	82.4	52.1%	66.1	16.2	-3.2%	16.7%	88.6%	7,622	11,897	6.2
Anantapur	69.2	74.0%	52.7	16.5	8.5%	8.7%	97.7%	10,621	10,785	6.0
Kurnool	52.1	28.0%	41.2	10.8	-2.5%	7.4%	64.0%	8,560	12,380	4.6

(Data: FY21, Source: Company, HDFC sec)

Peer Comparison:

	Mcap (Rs cr)	Revenue				EBITDA Margin (%)				APAT			
		FY21	FY22E	FY23E	FY24E	FY21	FY22E	FY23E	FY24E	FY21	FY22E	FY23E	FY24E
Krishna Institute of Medical Sciences	11,541	1,330	1,652	2,226	2,459	27.9	28.1	26.5	26.2	201	292	324	351
Narayana Hrudayalaya	12,779	2,582	3,657	4,161	4,577	7.1	16.5	17.6	18.0	-14	299	379	442
Fortis Healthcare	21,626	4,030	5,819	6,460	6,855	10.0	19.1	19.5	20.3	-111	390	524	597
Shalby	1,588	431	681	702	NA	20.1	17.2	18.7	NA	42	50	69	NA

	RoE (%)				P/E				EV/EBITDA			
	FY21	FY22E	FY23E	FY24E	FY21	FY22E	FY23E	FY24E	FY21	FY22E	FY23E	FY24E
Krishna Institute of Medical Sciences	27.5	26.4	21.4	19.0	53.7	39.5	35.7	32.8	30.2	24.4	19.2	17.3
Narayana Hrudayalaya	-1.3	22.7	23.2	22.9	negative	43.8	34.4	29.9	72.9	21.6	17.6	15.2
Fortis Healthcare	-1.7	6.7	7.3	7.0	negative	61.6	41.5	36.3	55.9	20.3	17.8	15.9
Shalby	5.2	5.8	7.2	NA	37.5	32.0	23.1	NA	17.9	13.6	12.5	NA

(Note: Consolidated numbers; Source: Bloomberg, Company, HDFC sec)

Financials – Consolidated

Income Statement

(Rs Cr)	FY20	FY21	FY22E	FY23E	FY24E
Net Revenues	**1122.7**	**1329.9**	**1652.3**	**2226.5**	**2459.4**
Growth (%)	**22.3**	**18.5**	**24.2**	**34.8**	**10.5**
Operating Expenses	877.7	959.1	1188.0	1636.5	1816.3
EBITDA	**245.0**	**370.9**	**464.3**	**590.0**	**643.1**
Growth (%)	**202.6**	**51.4**	**25.2**	**27.1**	**9.0**
EBITDA Margin (%)	**21.8**	**27.9**	**28.1**	**26.5**	**26.2**
Depreciation	70.6	69.5	72.7	106.9	117.8
EBIT	**174.4**	**301.4**	**391.6**	**483.1**	**525.3**
Other Income	6.1	10.2	13.2	16.7	24.6
Interest expenses	39.9	32.5	19.2	11.4	16.8
PBT	**140.5**	**279.0**	**385.6**	**488.4**	**533.1**
Tax	25.5	73.5	97.2	123.1	134.3
RPAT	115.1	205.5	288.4	365.3	398.8
APAT	**115.1**	**201.2**	**292.3**	**323.6**	**351.5**
Growth (%)	**-336.8**	**74.9**	**45.3**	**10.7**	**8.6**
EPS	16.0	26.9	36.5	40.4	43.9

Balance Sheet

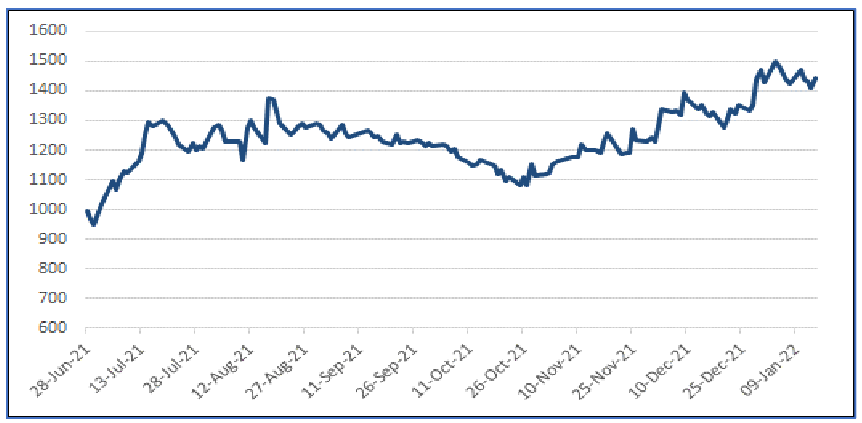
As at March (Rs Cr)	FY20	FY21	FY22E	FY23E	FY24E
SOURCE OF FUNDS					
Share Capital	74.5	77.6	80.0	80.0	80.0
Reserves	523.6	786.1	1267.7	1591.2	1942.7
Shareholders' Funds	**598.1**	**863.7**	**1347.7**	**1671.3**	**2022.7**
Minority's Interest	**13.3**	**12.5**	**18.7**	**60.5**	**107.8**
Long Term Debt	314.3	227.9	94.8	129.8	149.8
Net Deferred Taxes	34.3	32.9	27.9	27.9	27.9
Long Term Provisions & Others	15.7	17.9	22.2	29.9	32.2
Total Source of Funds	**975.7**	**1154.9**	**1511.3**	**1919.4**	**2340.5**
APPLICATION OF FUNDS					
Net Block & Goodwill	916.0	931.1	948.4	1503.5	1705.7
CWIP	2.2	9.2	9.2	9.2	9.2
Other Non-Current Assets	56.4	41.7	315.9	126.9	140.2
Total Non-Current Assets	**974.6**	**982.0**	**1273.5**	**1639.6**	**1855.1**
Current Investments	0.0	0.0	0.0	0.0	0.0
Inventories	30.4	24.1	40.7	54.9	60.6
Trade Receivables	132.3	109.8	153.9	195.2	215.6
Cash & Equivalents	45.7	284.4	324.3	413.4	640.9
Other Current Assets	11.5	32.9	52.1	57.9	64.0
Total Current Assets	**219.8**	**451.2**	**571.0**	**721.4**	**981.1**
Short-Term Borrowings	12.5	57.8	26.1	46.1	66.1
Trade Payables	123.4	131.9	181.1	231.8	256.0
Other Current Liab & Provisions	82.9	88.6	126.0	163.8	173.6
Total Current Liabilities	**218.8**	**278.3**	**333.2**	**441.6**	**495.7**
Net Current Assets	1.0	172.9	237.8	279.8	485.4
Total Application of Funds	**975.7**	**1154.9**	**1511.4**	**1919.4**	**2340.5**

Krishna Institute of Medical Sciences Ltd.

Cash Flow Statement

(Rs Cr)	FY20	FY21	FY22E	FY23E	FY24E
Reported PBT	140.5	279.0	385.6	488.4	533.1
Non-operating & EO items	5.2	4.3	-38.4	-40.1	-12.9
Interest Expenses	38.7	26.7	19.2	11.4	16.8
Depreciation	70.6	69.5	72.7	106.9	117.8
Working Capital Change	0.1	14.2	10.3	33.9	3.8
Tax Paid	-53.7	-37.7	-97.2	-123.1	-134.3
OPERATING CASH FLOW (a)	**201.5**	**356.0**	**352.3**	**477.4**	**524.3**
Capex	-51.5	-93.6	-90.0	-662.0	-320.0
Free Cash Flow	150.0	262.4	262.3	-184.6	204.3
Investments	0.0	0.0	-230.0	230.0	0.0
Non-operating income	-73.2	-260.6	0.0	0.0	0.0
INVESTING CASH FLOW (b)	**-124.7**	**-354.2**	**-320.0**	**-432.0**	**-320.0**
Debt Issuance / (Repaid)	-11.3	-58.0	-164.9	55.0	40.0
Interest Expenses	-33.0	-27.2	-19.2	-11.4	-16.8
FCFE	105.7	177.2	78.2	-141.0	227.5
Share Capital Issuance	0.0	95.0	191.7	0.0	0.0
Dividend	0.0	0.0	0.0	0.0	0.0
Others	0.0	0.0	0.0	0.0	0.0
FINANCING CASH FLOW (c)	**-44.3**	**9.8**	**7.6**	**43.6**	**23.2**
NET CASH FLOW (a+b+c)	**32.4**	**11.6**	**39.9**	**89.0**	**227.5**

One Year Price Chart



(Source: Company, HDFC sec)

Key Ratios

	FY20	FY21	FY22E	FY23E	FY24E
PROFITABILITY RATIOS (%)					
EBITDA Margin	21.8	27.9	28.1	26.5	26.2
EBIT Margin	16.1	23.4	24.5	22.4	22.4
APAT Margin	10.2	15.1	17.7	14.5	14.3
RoE	20.2	27.5	26.4	21.4	19.0
RoCE	20.3	30.0	30.9	30.1	26.9
SOLVENCY RATIO (x)					
Debt/EBITDA (x)	1.3	0.8	0.3	0.3	0.3
D/E	0.5	0.3	0.1	0.1	0.1
PER SHARE DATA (Rs)					
EPS	16.0	26.9	36.5	40.4	43.9
CEPS	24.9	34.9	45.6	53.8	58.6
Dividend	0.0	0.0	0.0	0.0	0.0
BVPS	80.3	111.3	168.4	208.8	252.8
TURNOVER RATIOS (days)					
Debtor days	41.5	33.2	29.1	28.6	30.5
Inventory days	9.3	7.5	7.2	7.8	8.6
Creditor days	37.0	35.0	34.6	33.8	36.2
VALUATION					
P/E (x)	90.1	53.7	39.5	35.7	32.8
P/BV (x)	18.0	13.0	8.6	6.9	5.7
EV/EBITDA (x)	45.0	30.2	24.4	19.2	17.3
EV/Revenues (x)	9.8	8.4	6.9	5.1	4.5
Dividend Yield (%)	0.0	0.0	0.0	0.0	0.0
Dividend Payout (%)	0.0	0.0	0.0	0.0	0.0

(Source: Company, HDFC sec)

HDFC Sec Retail Research Rating description

Green Rating stocks

This rating is given to stocks that represent large and established business having track record of decades and good reputation in the industry. They are industry leaders or have significant market share. They have multiple streams of cash flows and/or strong balance sheet to withstand downturn in economic cycle. These stocks offer moderate returns and at the same time are unlikely to suffer severe drawdown in their stock prices. These stocks can be kept as a part of long term portfolio holding, if so desired. This stocks offer low risk and lower reward and are suitable for beginners. They offer stability to the 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.

Red Rating stocks

This rating is given to emerging companies which are riskier than their established peers. Their share price tends to be volatile though they offer high growth potential. They are susceptible to severe downturn in their industry or in overall economy. Management of these companies need to prove their mettle in handling cyclicality of their business. If they are successful in navigating challenges, the market rewards their shareholders with handsome gains; otherwise their stock prices can take a severe beating. Overall these stocks offer high risk high return opportunities.

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