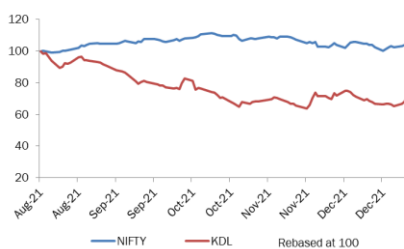


Sunshine acquisition and organic expansion are key value drivers

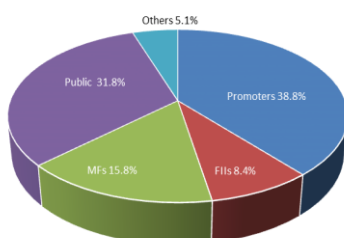
BUY

Sector	: Healthcare - Hospitals
Target Price	: ₹ 1,776
Last Closing Price	: ₹ 1,381
Market Cap	: ₹ 11,052 crore
52-week High/Low	: ₹ 1,532/938
Daily Avg Vol (12M)	: 411,081
Face Value	: ₹ 10
Beta	: 0.57
Pledged Shares	: 5.22%
Year End	: March
BSE Scrip Code	: 543308
NSE Scrip Code	: KIMS
Bloomberg Code	: KIMS IN
Reuters Code	: KRIL.NS
NSE Nifty	: 16,871
BSE Sensex	: 56,486
Analyst	: Research Team

Price Performance



Shareholding Pattern



Initiating Coverage

Investment Summary

- Founded by renowned cardiothoracic surgeon Dr. B Bhaskara Rao and headquartered in Hyderabad, Krishna Institute of Medical Sciences (KIMS) is one of the largest corporate healthcare groups operating in Andhra Pradesh and Telangana. KIMS has grown from a single 200-bed hospital at Nellore in 2000 to a multi-disciplinary healthcare service provider with 9 multi-specialty hospitals and over 3,000 beds today.
- KIMS focuses on offering quality healthcare services at affordable prices, regardless of the market, specialty or service type. It has successfully implemented affordable pricing model in all its hospitals across Tier 1 and Tier 2-3 markets.
- KIMS has consistently delivered strong operational and financial performance through robust patient volumes, cost efficiency and diversified revenue streams across medical specialties.
- A disciplined, low-leverage approach to acquisitions enables KIMS to maintain its affordable pricing model and expand its hospital network.
- KIMS is set to acquire a 51.07% equity stake in Sunshine Hospitals which will help it to consolidate its position as a leading provider of tertiary care services in its key markets and bring on board an orthopaedic surgical team led by Dr. AV Gurava Reddy.
- KIMS's plan to add ~1,700 incremental beds over a span of 24-48 months provide further revenue visibility.
- We expect robust revenue growth in FY22, followed by acceleration in FY23, with contributions from Sunshine Hospitals and new beds. The KIMS stock currently trades at an attractive forward P/E of 21.8x FY24E EPS. Based on a target P/E multiple of 28.0x, we initiate coverage on KIMS with a BUY rating, based on a price target of ₹ 1,776 and an upside potential of 29%.

Key Financial Metrics (Consolidated)

₹ crores	FY19A	FY20A	FY21A	FY22E	FY23E	FY24E
Total income	923.7	1,128.7	1,340.1	1,715.7	2,348.5	2,898.2
Growth		22.2%	18.7%	28.0%	36.9%	23.4%
EBITDA	81.3	251.1	381.0	534.9	697.3	860.1
EBITDA margin	8.9%	22.4%	28.7%	31.4%	29.9%	29.9%
PAT	(47.5)	114.1	205.0	328.9	399.5	492.1
PAT margin	-5.2%	10.2%	15.4%	19.3%	17.1%	17.1%
Diluted EPS (₹)	(6.71)	15.87	26.42	42.39	51.49	63.43

Source: Company data; Khambatta Research.

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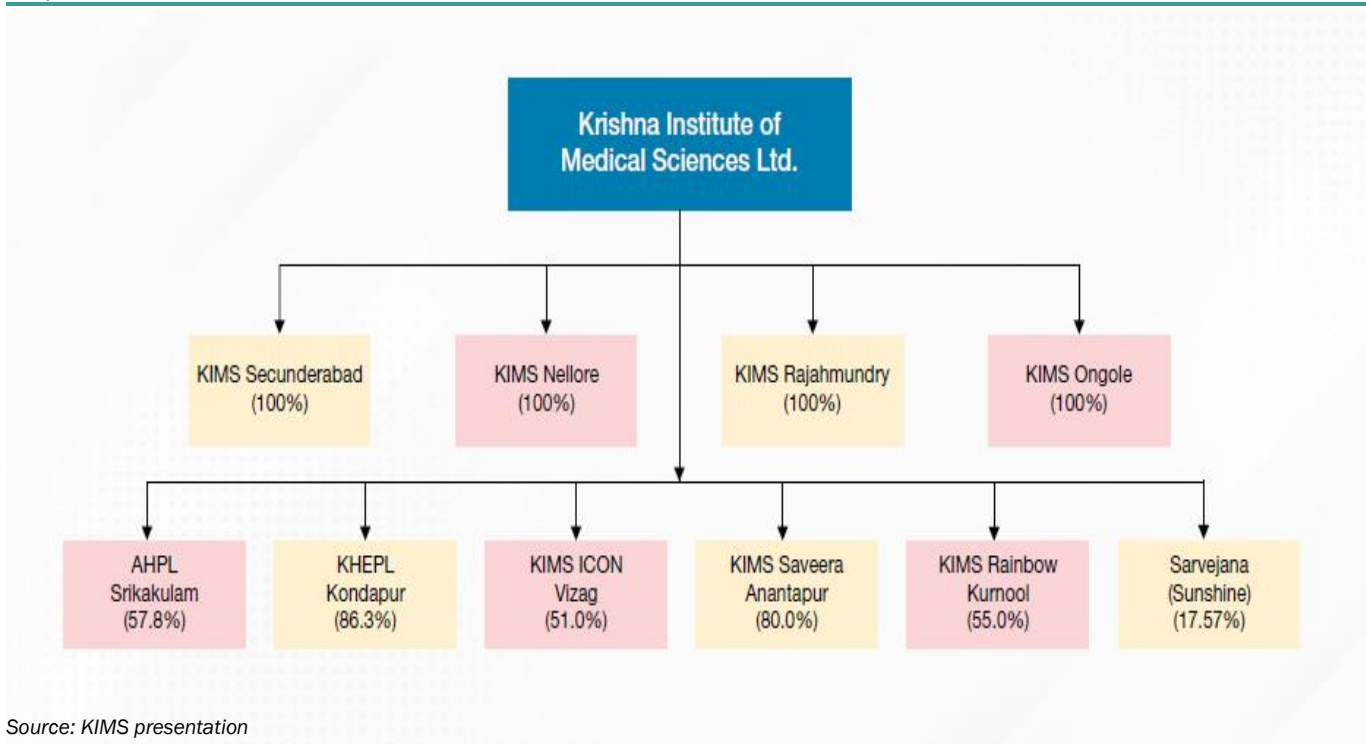
Company Profile

KIMS is one of the largest healthcare groups in AP and Telangana, providing integrated multi-disciplinary healthcare services

Krishna Institute of Medical Sciences (KIMS) is one of the largest corporate healthcare groups 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 and tertiary care in Tier 2-3 cities, and primary, secondary, tertiary and quaternary healthcare in Tier 1 cities. The company operates 9 multi-specialty hospitals under the “KIMS Hospitals” brand, with an aggregate bed capacity of 3,064 and over 2,500 operational beds as of 31 December 2020, which is 2.2x more beds than the second largest provider in AP and Telangana, according to a CRISIL report. KIMS offers a comprehensive range of healthcare services across more than 25 specialties and super specialties including cardiac sciences, oncology, neurosciences, gastric sciences, orthopaedics, organ transplantation, renal sciences and mother & child care.

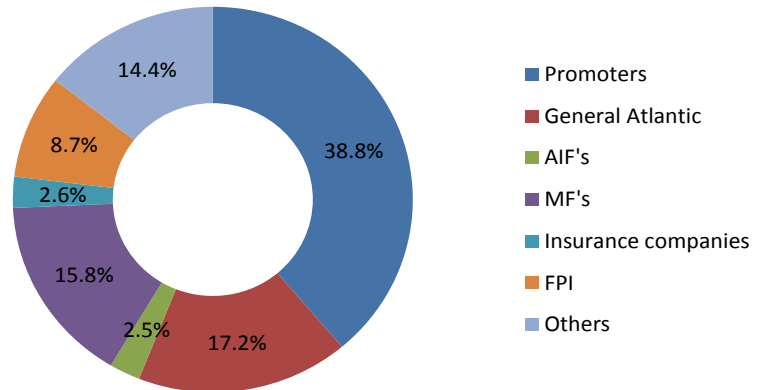
KIMS has grown from a single hospital to a chain of multi-speciality hospitals through organic growth and strategic acquisitions under the leadership of renowned cardiothoracic surgeon Dr. Bhaskara Rao Bollineni, who is the group’s Founder and Managing Director, and Dr. Abhinay Bollineni, Executive Director and CEO.

Corporate structure



Source: KIMS presentation

Shareholding pattern



Source: KIMS presentation, Khambatta Research

Investment Thesis

Robust growth driven by expansion and consolidation in the Indian hospitals sector. The Indian healthcare delivery industry is expected to grow at a 17-18% CAGR from 2020 to reach ₹ 7.07 trillion by 2024. In FY20, 68% of hospital treatments, in terms of the treatment value, were carried out in private hospitals, with the number expected to reach 72% by FY24. Demand from patients and doctors for high-quality facilities, modern technologies, and multidisciplinary care are the key factors driving consolidation in the healthcare industry. Larger hospital brands typically have stronger financial disciplines and negotiating power with suppliers, better ability to attract medical talent, and greater capital and administrative resources to meet these needs compared to standalone hospitals. In addition, the consolidation of hospital brands in India’s Tier 2-3 cities in the last few years have formed regional clusters that provide a base for further expansion and consolidation. (Source: CRISIL report).

Leading player in South India with a strategic regional focus. KIMS has over 20 years of expertise in AP and Telangana since it began its operations in Nellore in 2000. It strategically focuses on the southern Indian healthcare market where it has a strong understanding of regional nuances, customer culture and the mindset of medical professionals with a significant and growing need for quality and affordable healthcare services.

In FY20, AP was amongst the top-ranking states in terms of GSDP growth. AP and Telangana also ranked amongst the top three states in terms of overall health index score. AP was also a leading state in terms of doctors per 1,000 people in 2018 and has been attracting doctors and patients seeking treatments from all over the country. AP and Telangana also have strong health insurance coverage with penetration rates of 4% and 12%,

KIMS has over two decades of expertise in the Southern Indian healthcare market

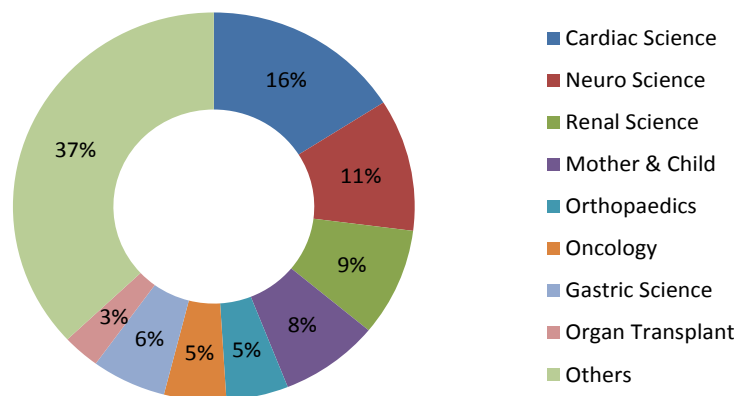
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respectively (as of FY20). Government-backed schemes in AP and Telangana have helped to set the stage for future growth. (Source: CRISIL report).

Given the leading position held by KIMS in AP and Telangana as a provider of quality and affordable healthcare services, as well as its track record of growth, KIMS is well positioned to be a consolidator in the region. It has grown from a single 200-bed hospital at Nellore in 2000 to a leading multi-disciplinary integrated private healthcare services provider with nine multi-specialty hospitals with over 3,000 beds today.

Speciality mix, 9M FY22



Source: KIMS presentation, Khambatta Research

Low-cost and affordable pricing model. KIMS focuses on offering quality healthcare services at affordable prices, regardless of the market, speciality or service type. It has successfully implemented affordable pricing model in all hospitals in both Tier 1 and Tier 2-3 markets, although it faces different competitive landscapes and pricing pressures, serve patients from different economic backgrounds and offer a different mix of specialty offerings in different markets.

KIMS has been successful in adopting the affordable pricing model through control over its capex and opex

Its control over capex and opex has enabled KIMS to successfully adopt the affordable pricing model. In FY20, capex per bed was ₹ 6.35 mn for hospitals in Tier 1 cities and ₹ 2.21 mn for hospitals in Tier 2-3 cities, compared to an industry average of ₹ 5-8 mn in Tier 1 cities and ₹ 1-5 mn in Tier 2-3 cities. KIMS's prices across medical procedures in Tier 1 cities are on average 20% to 30% lower than other private hospitals in India (source: CRISIL report). Following the disciplined approach, KIMS manages its capital expenditures according to the needs of each market. Its hospitals are located in markets that have been able to support high patient volumes, which are vital to the success of the affordable pricing model. KIMS purchases land at attractive rates by entering markets early. It acquires land on a long-term basis and enters into lease agreements on low-cost terms to avoid high fixed rental costs, such as the land for its hospital in Secunderabad, which is held on a

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perpetual lease basis. KIMS Vizag's real estate is under an operation and maintenance arrangement without traditional lease rentals. With only one hospital (KIMS Kondapur) on traditional lease, it has minimised lease expenses and lease renewal risks that often drive up costs. KIMS reported an ROCE of 22.3% in 9M FY20 from its overall operations across high-priced Tier 1 markets and lower priced Tier 2-3 markets.

To sustain affordable pricing while still generating strong returns, KIMS streamlines its doctor, procurement and other administrative costs. It manages doctor costs by employing a mix of fixed and variable compensation arrangements, based on patient volumes, costs and other factors at each hospital. KIMS has standardized protocols for medical and operating procedures to ensure an optimal number of employees and medical support staff per bed and achieve optimal utilization of resources. It has also streamlined and centralized supply chain operations, vendor management, compliance and administrative functions. This allows KIMS to leverage its scale and secure favourable pricing from vendors for medical equipment and consumables.

Ability to attract, train and retain high quality doctors, consultants and medical support staff. KIMS has maintained its standard of high quality healthcare by consistently employing a diverse pool of talented doctors, nurses and paramedical professionals. Its multi-disciplinary approach, combined with affordable cost for treatment, a high-volume tertiary care model, and focus on teaching and research, has helped KIMS to attract and retain high quality doctors and other healthcare professionals.

KIMS has taken significant efforts to create a culture that nurtures medical talents and encourages its doctors to become stakeholders in the hospitals where they work. This culture of empowerment and ownership has encouraged learning and training at its hospitals, and led to good talent retention and allowed patients to create long-term relationships with the doctors. KIMS has retained over 80% of its doctors since its inception in 2000.

KIMS is accredited by the National Board of Examination to enroll students in a number of specialty specific DNB courses, which serves as a training ground for a number of its doctors and medical support staff and helps them contribute to the availability of skilled doctors for recruitment. As of December 31, 2020, KIMS had 208 doctors in DNB and post-doctoral fellowship programs. KIMS continuously endeavors to undertake initiatives to ensure that the attrition rates for its doctors remain low.

Strong operational and financial performance. KIMS has consistently delivered strong operational and financial performance through strong patient volumes, cost efficiency and diversified revenue streams across medical specialties. It has achieved healthy profitability in both Tier 1 and Tier 2-3 markets by identifying markets with significant underserved healthcare demand and delivering quality healthcare services at affordable

KIMS encourages its doctors to become stakeholders in the company, which aids in improving retention

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KIMS is one of the only three hospitals in India with a “AA” rating by Crisil

prices, which in turn drives patient volumes. The company’s hospitals in Tier 1 markets generate higher margins from services such as organ transplants, oncology and neuro-critical care, resulting in higher ARPOB and EBITDA. The multispecialty healthcare platform has resulted in diversified revenue streams, with no single specialty accounting for more than 25% of the total income in any of the last three years. KIMS is one of only three hospitals in India that are rated AA by CRISIL.

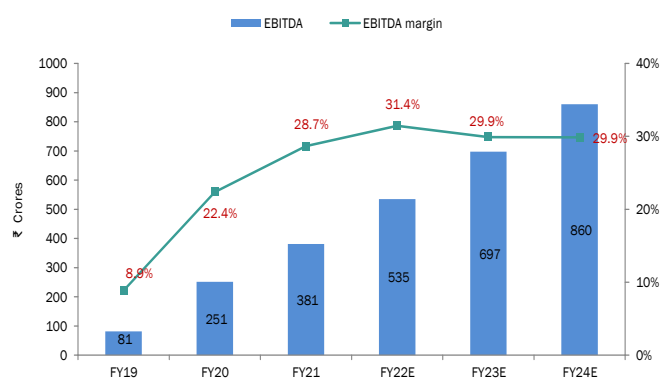
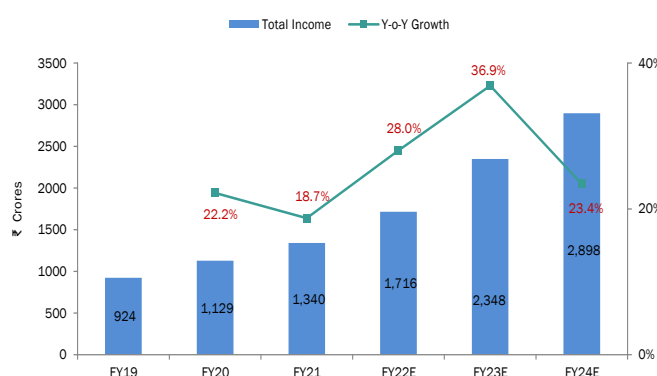
Operating performance

Particulars	FY19	FY20	FY21	FY22 9M
Bed Capacity	2,804	3,004	3,064	3,064
Occupancy	49%	56%	58%	63%
IP volume	111,382	140,676	116,592	104,143
OP volume	900,043	1,137,560	830,211	742,862
ARPOB	18,334	18,307	20,609	24,186
ARPP	81,995	79,526	113,904	123,089
ALOS	4.47	4.34	5.53	5.09
Revenue	9,239	11,287	13,401	12,906
EBITDA	1,740	2,511	3,810	4,143
EBITDA %	19%	22%	28%	32%

Source: KIMS presentation

Total income and growth

EBITDA and EBITDA margin



Source: KIMS presentation, Khambatta Research

Inorganic growth strategy and expansion plans will aid future growth: A disciplined, low-leverage approach to acquisitions has enabled KIMS to maintain its affordable pricing model as it has grown across both Tier 1 and Tier 2-3 markets. Since FY17, KIMS has expanded its hospital network primarily through acquisition of other hospitals. In FY17, it acquired a

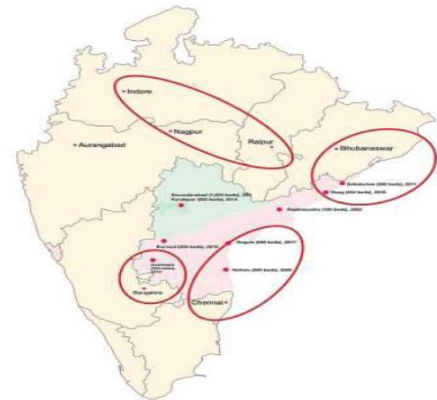
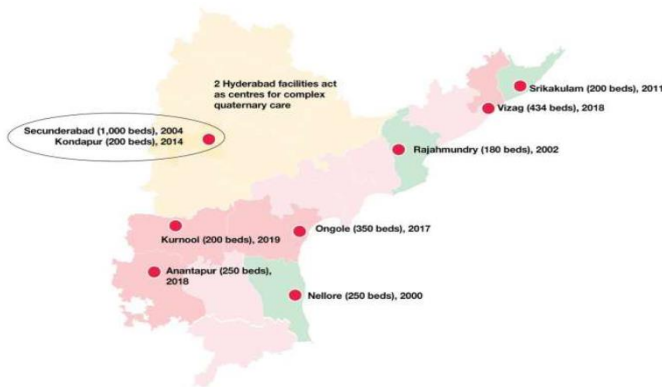
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hospital in Ongole, a 350-bed multispecialty hospital. The company acquired KIMS Vizag, a 434-bed multispecialty hospital in April 2018. It further acquired a 250-bed hospital in Anantapur in October 2018 and a 200-bed hospital in Kurnool in April 2019 that solidified its presence in southern AP and adjoining areas of Karnataka. KIMS aims to strengthen its existing hospitals and specialities and also to strategically grow its presence in the adjacent markets of Karnataka, Odisha, Tamil Nadu and central India.

Location of KIMS Hospitals in AP and Telangana

Potential target markets



Source: KIMS presentation

KIMS plans to add ~1,700 incremental beds at a total estimated capex of ~₹ 1,400 crores over a span of 24-48 months provide further revenue visibility.

Expansion plan

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

Source: KIMS presentation

Acquisiton of a majority stake in Sunshine Hospitals will help KIMS consolidate its leading position in Southern India. KIMS will acquire a 51.07% equity stake in private equity firm InvAscent-backed Sunshine Hospitals for ~ ₹ 362 crores, of which ₹ 270 crores have already been paid out. The acquisition will help KIMS to consolidate its position as a leading

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KIMS is set to acquire 51.07% in Sunshine Hospitals for ₹ 362 crores

provider of tertiary care services in its key markets and bring onboard an orthopaedic surgical team led by Dr. AV Gurava Reddy. 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, a fast-upcoming Tier 3 town. With a total bed strength of over 600, it is a leading player in the joint replacement and spine specialities with over 4,000 knee transplants conducted in a year. It is the first hospital in India with ISOC membership. More than 10,000 surgeries are conducted annually across all the orthopaedic sub-specialities at Sunshine with more than 700 robotic knee replacements done in less than 18 months, the fastest in the world.

The Sunshine deal is expected to be EPS-accretive and provides an enhanced platform for KIMS to further strengthen its presence in the key home markets of Hyderabad and Secunderabad. The combined entity will have 12 hospitals across 9 cities with 3,666 beds and over 1,200 doctors and 12,000 employees. Sunshine Hospitals is a natural fit, clinically and strategically, to KIMS's vision of providing clinical excellence at an affordable cost. It will also allow KIMS to consolidate its position in Hyderabad, which is its core market.

Peer Comparison

We compare KIMS with the following listed hospitals and healthcare facilities.

Peer comparison: Key financials metrics, FY21

₹ Crore	KIMS	Apollo Hospitals Enterprise	*Fortis Healthcare	*Narayana Hrudayalaya	*Max Healthcare Institute
Total income	1,340.1	10,605.0	4,685.0	3,151.6	1,107.1
EBITDA	381.0	1,137.4	609.5	422.9	93.6
EBITDA margin	28.7%	10.7%	13.0%	7.0%	8.5%
PAT	205.0	150.4	57.9	118.9	59.0
PAT margin	15.4%	1.4%	1.2%	3.8%	1.2%
EPS (Rs)	26.4	10.7	0.8	5.9	1.0
ROE	23.4%	3.3%	0.9%	10.5%	2.3%
ARPOB (₹ in 000' for FY20)	18.3	37.4	43.6	26.6	51
ARPP (₹ in 000' for FY20)	79	144	141	93	219
Current market cap	11,121	69,779	19,765	14,355	34,130

Source: Bloomberg, company data, Khambatta Research * Reported financials for FY20 as losses were reported in FY21

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Valuation

The KIMS stock currently trades at an attractive forward P/E of 21.8x FY24E EPS

At 28.0x FY24E EPS, we initiate coverage on KIMS with a BUY rating, based on a price target of Rs 1,776 and an upside potential of 29%. KIMS reported 18.7% and 32% y-o-y growth in total income in FY21 and 9M FY22, respectively. We expect revenue growth to be robust for the full year, followed by acceleration in FY23, aided by consolidation of Sunshine Hospitals and addition of beds. We expect EBITDA margins over the forecast period to be marginally lower than the current levels as guided by management. The KIMS stock currently trades at an attractive forward P/E level of 21.8x FY24E EPS. Based on a target P/E multiple of 28.0x, we initiate coverage on KIMS with a BUY rating, based on a price target of ₹ 1,776 and an upside potential of 29%.

Profit & Loss Account (Consolidated)

₹ crore	FY19A	FY20A	FY21A	FY22E	FY23E	FY24E
Total income	923.7	1,128.7	1,340.1	1,715.7	2,348.5	2,898.2
Growth		22.2%	18.7%	28.0%	36.9%	23.4%
Cost of service & operations	842.5	877.7	959.1	1,180.8	1,651.2	2,038.1
EBITDA	81.3	251.1	381.0	534.9	697.3	860.1
EBITDA margin	8.9%	22.4%	28.7%	31.4%	29.9%	29.9%
Depreciation & amortization	52.1	70.6	69.5	73.5	102.9	137.9
EBIT	27.9	179.5	311.0	460.1	594.3	722.2
PBT	(12.9)	139.5	278.6	446.9	542.8	668.7
Tax expense	(34.7)	(25.5)	(73.5)	(118.0)	(143.3)	(176.5)
PAT	(47.5)	114.1	205.0	328.9	399.5	492.1
PAT margin	-5.2%	10.2%	15.4%	19.3%	17.1%	17.1%
Diluted EPS (₹)	(6.71)	15.87	26.42	42.39	51.49	63.43

Source: Company data, Khambatta Research.

Key Balance Sheet Items (Consolidated)

₹ Crore	FY19A	FY20A	FY21A	FY22E	FY23E	FY24E
Total shareholders' equity	569.4	611.4	876.2	1,205.7	1,605.2	2,097.3
Total debt	261.3	278.8	239.9	335.3	515.3	535.3
PPE	721.7	748.9	770.6	970.6	1,470.6	1,970.6

Source: Company data, Khambatta Research

Ratio Analysis

	FY19A	FY20A	FY21A	FY22E	FY23E	FY24E
ROE	-8.3%	18.7%	23.4%	27.3%	24.9%	23.5%
Total D/E ratio	0.46x	0.46x	0.27x	0.28x	0.32x	0.26x

Source: Company data, Khambatta Research

Krishna Institute of Medical Sciences Limited**14 March 2022****Key Risks**

- KIMS is exposed to geographical concentration risks as all its hospitals are located in AP and Telangana.
- Further severe and/or prolonged waves of covid-19 can potentially have a negative impact on KIMS's revenues and profits due to the postponement of non-emergency treatment by patients as well as possible delays in the execution of planned capacity expansions.

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Guide to Khambatta's research approach

Valuation methodologies

We apply the following absolute/relative valuation methodologies to derive the 'fair value' of the stock as a part of our fundamental research:

DCF: The Discounted Cash Flow (DCF) method values an estimated stream of future free cash flows discounted to the present day, using a company's WACC or cost of equity. This method is used to estimate the attractiveness of an investment opportunity and as such provides a good measure of the company's value in absolute terms. There are several approaches to discounted cash flow analysis, including Free Cash Flow to Firm (FCFF), Free Cash Flow to Equity (FCFE) and the Dividend Discount Model (DDM). The selection of a particular approach depends on the particular company being researched and valued.

ERE: The Excess Return to Equity (ERE) method takes into consideration the absolute value of a company's return to equity in excess of its cost of equity discounted to the present day using the cost of equity. This methodology is more appropriate for valuing banking stocks than FCFF or FCFE methodologies.

Relative valuation: In relative valuation, various comparative multiples or ratios including Price/Earnings, Price/Sales, EV/Sales, EV/EBITDA, Price/Book Value are used to assess the relative worth of companies which operate in the same industry/industries and are thereby in the same peer group. Generally our approach involves the use of two multiples to estimate the relative valuation of a stock.

Other methodologies such as DuPont Analysis, CFROI, NAV and Sum-of-the-Parts (SOTP) are applied where appropriate.

Stock ratings

Buy recommendations are expected to improve, based on consideration of the fundamental view and the currency impact (where applicable) by at least 15%.

Hold recommendations are expected to improve, based on consideration of the fundamental view and the currency impact (where applicable) between 5% and 15%.

Sell recommendations are expected to improve up to 5% or deteriorate, based on consideration of the fundamental view and the currency impact (where applicable).

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Krishna Institute of Medical Sciences Limited**14 March 2022**

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