

4 September 2023

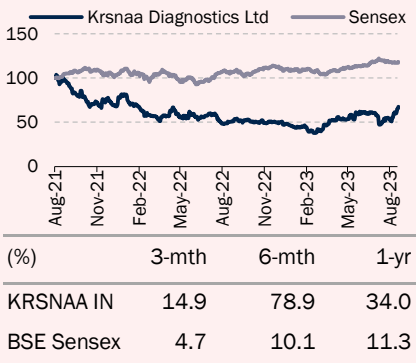
BSE Sensex: 65387

Sector: Hospitals

Stock data

| | |
|-------------------------------|-----------|
| CMP (Rs) | 645 |
| Mkt Cap (Rs bn/USD m) | 20.3 /245 |
| Target Price (Rs) | - |
| Change in TP (%) | NA |
| Potential from CMP (%) | NA |
| Earnings change (%) | |
| FY24E | NA |
| FY25E | NA |
| Bloomberg code | KRSNAA IN |
| 1-yr high/low (Rs) | 649/353 |
| 6-mth avg. daily volumes (m) | 0.2 |
| 6-mth avg. daily traded value | |
| (Rsm/USDm) | 82.1/1 |
| Shares outstanding (m) | 31.4 |
| Free float (%) | 72.2 |
| Promoter holding (%) | 27.8 |

Price performance – relative & absolute



- Krsnaa Diagnostics (KDL) is a unique diagnostic service provider with a strong focus on the B2G (Business to Government/PPP) and radiology segments in contrast to its peers that are predominantly B2C-focused pathology players. In PPP model, KDL collaborates with government-owned healthcare facilities for deployment/operation of its centres, based on successful tender wins.
- Most PPP contracts have a term range of 5-10 years and typically have a high renewal rate. Under this arrangement, the winner of the tender gets immediate access to a large pool of captive customers at the facility and a space to set up the centre at no additional cost, which enables disruptive pricing. When executed well, this structure results in a business that generates high ROCEs of 30%+ over a period of 2-3 year, even for capital-intensive businesses such as radiology.
- Increasingly, PPP tender processes are managed by large private entities in a fairly transparent manner. Further, there has been a progressive improvement on the govt receivables front, as reflected in a sharp reduction in KDL's receivable days – 56 days as of FY23 vs 97-98 days in FY18/19.
- The PPP model is potentially the most effective model catering to the underserved and high growth 'bottom of pyramid' healthcare opportunity in India. Driven by programs including Free Diagnostic Services and PPP models, the government's share in the diagnostics industry is expected to grow at a 14-17% CAGR from the current Rs135bn – representing a large opportunity for private players.
- With its demonstrated ability to win/operate PPP centres on a pan-India basis and a win rate of ~78%, KDL is a dominant player in this space. Over the last five years, the company has delivered a revenue/EBITDA CAGR of 35/33% with a steady-state EBITDAM of 25-30%, far eclipsing growth of its listed peers.
- In the last 12 months, KDL has won multiple large pathology tenders, which when combined will have a peak revenue potential of at least Rs5bn (1x FY23 revenue), providing robust growth visibility. It will also create a more balanced revenue mix across asset-heavy radiology and pathology segments. Its recent strategic foray into the B2C space could create an interesting growth engine in the medium-long term.
- Scale-up of recently won contracts should drive revenue/EBITDA/PAT CAGR of 31%/34%/40% over FY23-FY26E with 20%/15% RoCE/RoE. Faster scale-up in existing contracts, along with new tender wins, could add to the upsides.

Key valuation metrics

| Year to 31 Mar | FY22 | FY23 | FY24E | FY25E | FY26E |
|------------------------|---------|-------|-------|-------|--------|
| Net sales (Rs m) | 4,555 | 4,871 | 6,176 | 8,664 | 10,999 |
| Adj. net profit (Rs m) | 684 | 621 | 743 | 1,258 | 1,706 |
| Shares in issue (m) | 31 | 31 | 31 | 31 | 31 |
| Adj. EPS (Rs) | 21.8 | 19.8 | 23.7 | 40.1 | 50.1 |
| % change | (141.7) | (9.2) | 19.6 | 69.3 | 25.1 |
| PE (x) | 26.9 | 29.6 | 24.8 | 14.6 | 11.7 |
| Price/ Book (x) | 2.7 | 2.5 | 2.3 | 2.0 | 1.7 |
| EV/ EBITDA (x) | 12.4 | 14.3 | 11.7 | 7.8 | 5.2 |
| RoE (%) | 14.9 | 8.7 | 9.6 | 14.4 | 15.4 |
| RoCE (%) | 15.2 | 8.9 | 10.2 | 15.6 | 17.7 |

Source: Company, DAM Capital Research

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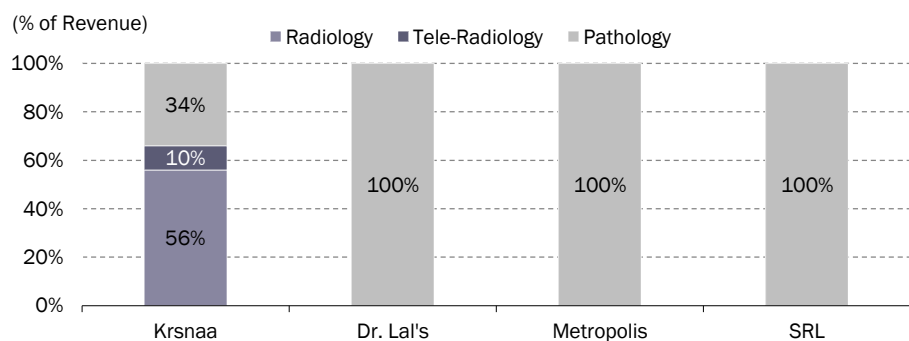
KEY HIGHLIGHTS

- A unique diagnostics company, catering to the high growth, underserved, 'bottom of pyramid' healthcare services segment through PPP contracts.
- Superior cost structure enabled by PPP contracts, combined with operational efficiency, enables disruptive pricing (50-60% discount) without compromising on profitability.
- Exceptional tender win rate of ~78% due to tailored business model, large scale of operations and managerial expertise. High probability of tender renewal due to a large existing infrastructure base.
- High growth visibility with robust tender wins last year expected to drive 31%/34%/40% revenue/EBITDA/PAT CAGR over FY23-26E.
- Better profitability and strong net cash balance sheet expected to lead to ROCE/ROE inching up to 20%/15% by FY26E.

Krsnaa Diagnostics: A Unique Business Model

Krsnaa Diagnostics (KDL) is a differentiated diagnostic service provider, offering radiology (66% of revenue) and pathology (34% of revenue) testing services at affordable prices (typically 50-60% discount compared to peers). The company has a strong presence in the PPP (B2G) space, in contrast to its listed peers that are predominantly B2C/B2B pathology players.

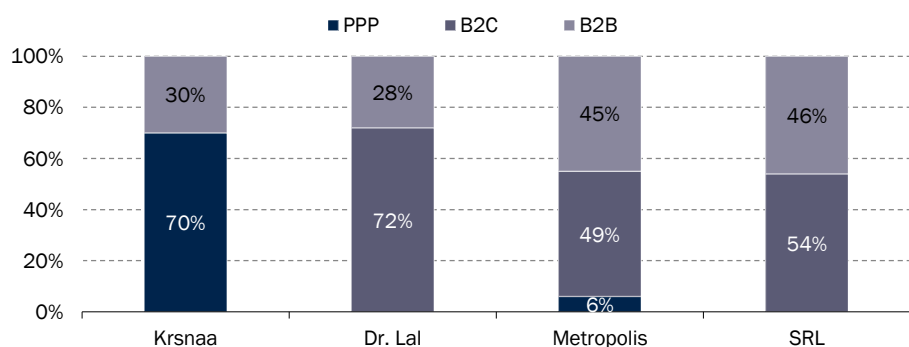
Exhibit 1: Peers are pathology focused...



Source: Company, DAM Capital Research

In the PPP segment, Krsnaa collaborates with central, state, and municipal government-operated health and medical facilities for the deployment and operation of its diagnostic centres, based on successful tender wins. A similar setup is also used for partnerships with private hospitals.

Exhibit 2: ...and largely B2C focused

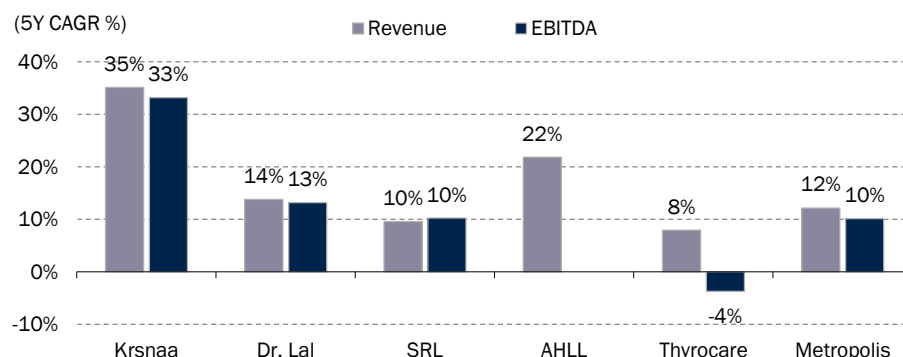


Source: Company, DAM Capital Research

□ Fastest-growing diagnostics company

For FY23, KDL recorded revenue/EBITDA of Rs4.9bn/1.2bn with EBITDAM of 25.1% — making it the fastest-growing diagnostics provider among its peers by a substantial margin over a five-year period.

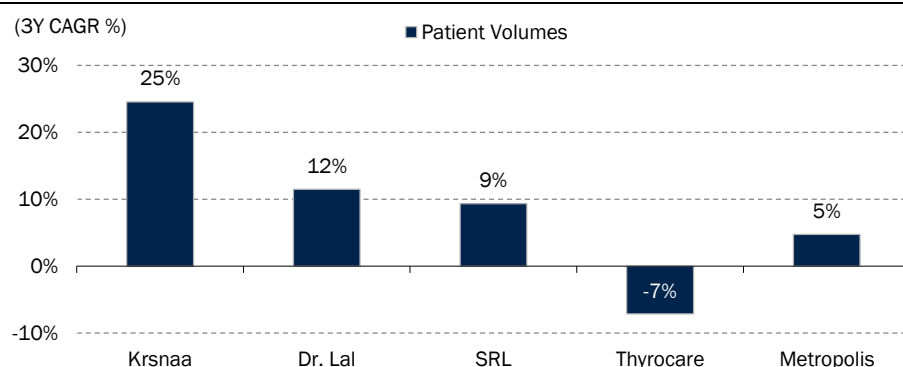
Exhibit 3: 5Y CAGR - peer comparison



Source: Company, DAM Capital Research

A similar trend is visible in-patient volumes, where Krsnaa has delivered a CAGR of 25% between FY20 and FY23, far outpacing its listed peers.

Exhibit 4: 3Y patient volume CAGR – peer comparison



Source: Company, DAM Capital Research

□ Disruptive pricing

In line with its aim of making reliable healthcare services available to all, KDL offers tests at 60-80% lower prices as compared to market rates. This makes KDL possibly the best proxy for 'bottom of pyramid' healthcare growth opportunity in India.

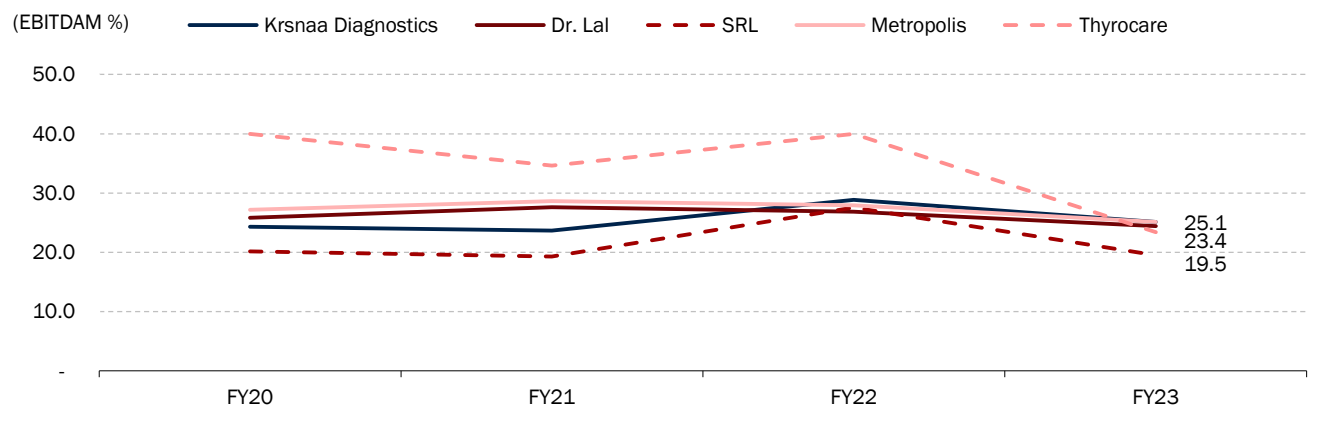
Exhibit 5: Krsnaa offers tests at 60-80% lower than market rates

| Segment | Test (Price in Rs) | Peer 1 | Peer 2 | Peer 3 | Krsnaa | % Δ from min. price |
|-----------|--------------------|--------|--------|--------|--------|---------------------|
| Radiology | CT Brain | 4,500 | 4,500 | 3,500 | 973 | -72% |
| Radiology | MRI Brain | 8,000 | 8,250 | 7,000 | 2,209 | -68% |
| Pathology | CBC | 250 | 250 | 200 | 146 | -27% |
| Pathology | Blood Sugar | 85 | 80 | 70 | 26 | -63% |
| Pathology | Thyroid | 500 | 550 | 550 | 216 | -57% |
| Pathology | Vitamin D | 1,500 | 1,250 | 1,450 | 595 | -52% |
| Pathology | Vitamin B12 | 1,000 | 1,100 | 1,300 | 243 | -76% |
| Pathology | HbA1C | 550 | 440 | 400 | 141 | -65% |

Source: Company, DAM Capital Research

Despite charging sharply lower prices for its services, the company maintains a healthy level of profitability when compared to its peers. This is enabled by its superior cost structure owing to the PPP model, as well as a high level of operational efficiency.

Exhibit 6: KDL's EBITDA margins are comparable to peers, despite the sharp difference in pricing



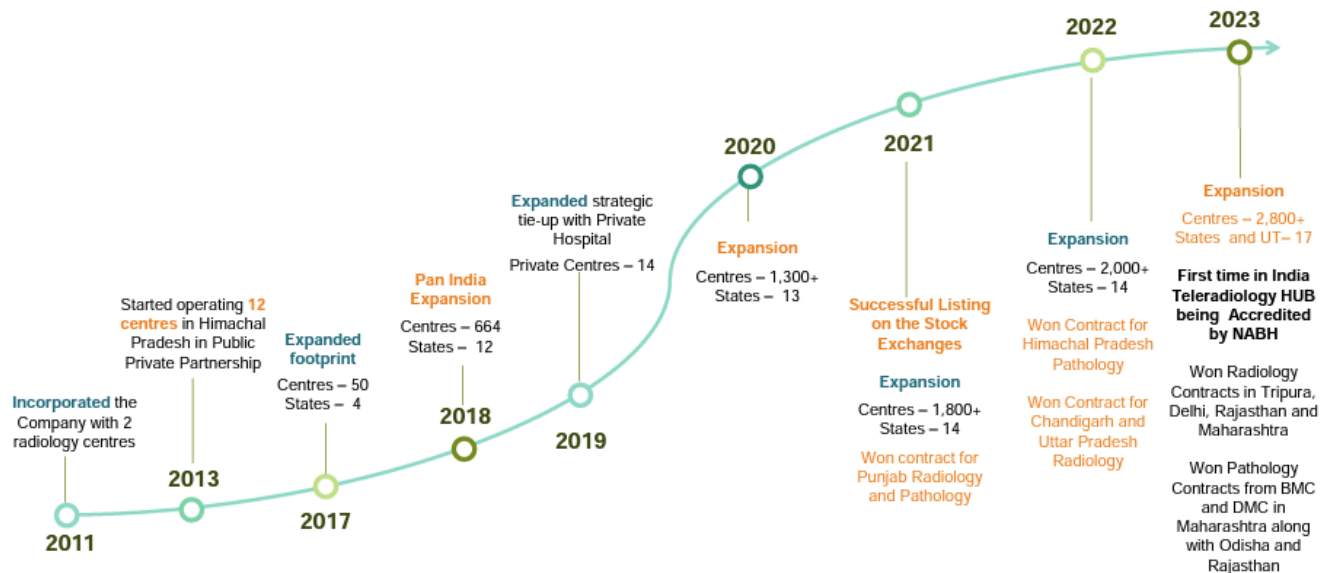
Source: Company, DAM Capital Research

The company has undergone a tremendous scale up, establishing itself as one of the fastest growing diagnostic chains in the country...

Company background

Krsnaa was established at Pune, Maharashtra, in December 2010 by first generation entrepreneur Mr. Rajendra Mutha. Since then, the company has undergone a tremendous scale up, establishing itself as one of the fastest growing diagnostic chains in the country with a particular focus on PPP contracts for providing pathology and radiology services.

Exhibit 7: A snapshot of Krsnaa's journey



Source: Company, DAM Capital Research

As of FY23, Krsnaa operates over 133 CT/MRI centres, 1,090 pathology collection centres, 99 pathology processing labs and 1,528 tele-reporting centres across 17+ states and union territories.

Exhibit 8: Geographical overview

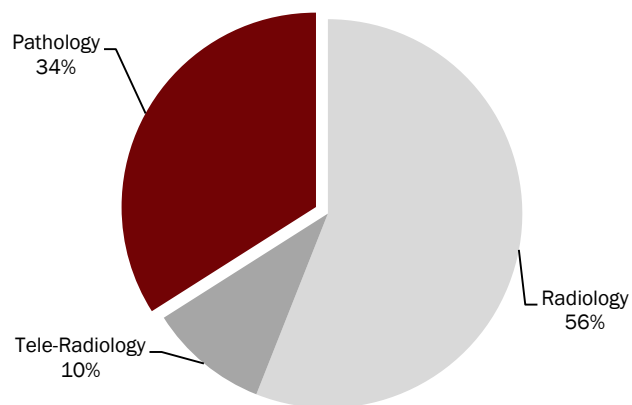


Source: Company, DAM Capital Research

➤ Business mix

KDL offers a range of diagnostics imaging services and clinical laboratory tests that include both routine and specialised tests/studies and profiles, which are used for prediction, early detection, diagnostic screening, confirmation and/or monitoring of diseases.

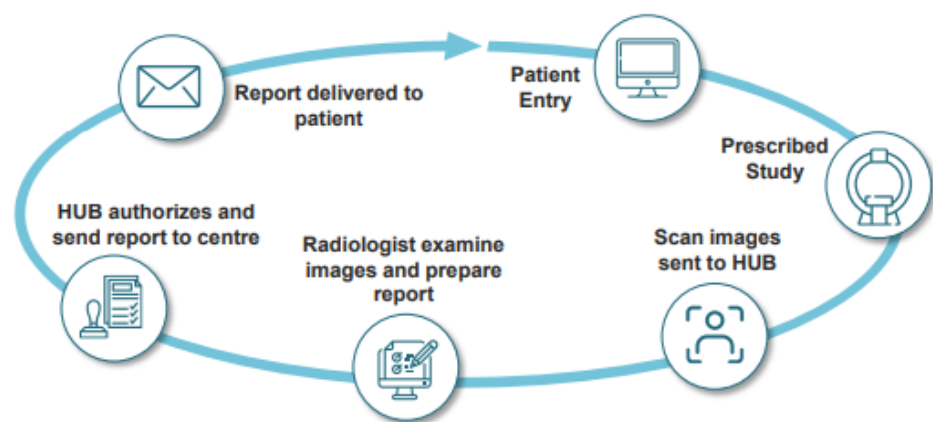
Exhibit 9: Krsnaa's revenue mix (%)



Source: Company, DAM Capital Research

- **Radiology:** KDL is a large radiology chain, having a pan-India presence across 17 states with 1,661 radiology-focused centres, as of FY23. These centres provide MRI, CT scans, X-rays, mammography, ultrasound, colour doppler and bone densitometry services. The segment is subject to high capital requirements, given the high equipment cost. Therefore, while segmental fixed costs are typically higher than pathology, thereby leading to a stretched breakeven timeline, a ramp up in new centres will likely lead to the realisation of major operating leverage benefits. Mature margins for the segment range from 35% to 40%.
- **Tele-radiology:** Krsnaa's NABH certified tele-reporting hub at Pune is the largest of its kind in India, employing over 220 radiologists who can service patients 24/7. Under this model, the analogue image from the test conducted at a centre is converted into a digital format using a CR machine. This digital image is then transferred to Krsnaa's Pune hub via a direct line where its team of specialists evaluate the image and prepare the report.

Exhibit 10: Tele-reporting process



Source: Company, DAM Capital Research

KDL offers a comprehensive test menu covering the key disciplines of conventional and specialised lab services

- Krsnaa operates ~1,500 such centres across the country. Under this arrangement, the machines are usually owned by the government and Krsnaa only provides reporting for the tests.
- Initially, tele-reporting was a cost centre for KDL which the management turned into a profit centre by providing this service to various other operators – indicating the ingenuity of the management team. Today, tele-reporting contributes ~10% to the overall revenues.
- Recently, the company has also started receiving requests for tele-reporting from private operators who would be able to save on the fixed cost of having a radiologist at their centres and would only have to pay a certain amount per scan to KDL.
- This is a high-return low-capital business and would add a potentially interesting growth lever to KDL in the future.
- **Pathology:** KDL offers a comprehensive test menu covering the key disciplines of conventional and specialised lab services — its offerings encompass a wide range of investigations, from routine tests to highly specialised ones. It has top of the line fully automated analysers and a team of highly skilled and trained technical staff to undertake these investigations.
- As of FY23, Krsnaa operates over 1,090 collection centres and 99 pathology processing labs across the country. Given the lower capital outlay required for a collection centre, ramp up timelines are typically shorter when compared to the radiology segment. EBITDA margins for the segment range between 25% and 35%.

□ Management team

One of Krsnaa's defining factors is the management team's hands-on experience with managing the tender bidding and implementation process, as well as working directly with government agents. This contrasts with Krsnaa's peers who have built larger B2C franchises.

Exhibit 11: An overview of Krsnaa's senior management team

| Manager | Designation | Comments |
|---------------------|----------------|--|
| Mr. Rajendra Mutha | Exec. Chairman | Mr. Rajendra Mutha is the founder and executive chairman of the company. He has over 10 years of experience in the field of pharmacy and diagnostics. He is a registered pharmacist certified by the Maharashtra State Pharmacy Council. |
| Ms. Pallavi Jain | MD | Ms. Pallavi Jain has been part of Krsnaa Diagnostics since its inception and has played a crucial role in development of the organisation. She has been catalyst in the expansion and growth of Krsnaa Diagnostics from the tendering process to implementation and execution of the projects. |
| Mr. Yash Mutha (CA) | ED | Mr. Yash Mutha is a chartered accountant by qualification and has over 15+ years of experience working with the Big Four audit firms and industry. He has worked with Credit Suisse as well as other MNC companies. |
| Mr. Pawan Daga (CA) | CFO | Mr. Pawan Daga has 10+ years of experience in mergers and acquisitions, treasury and funding, investor relations, cost management, financial operations, legal, taxation, financial accounting, and reporting. He is a chartered accountant and has a Master of Commerce degree from Pune University. |
| Mr. Rupesh Dagar | CBO | Mr. Rupesh Dagar has been a veteran in the diagnostics sector for more than 25 years and is currently the chief business officer at Krsnaa Diagnostics. His achievements include developing the organisation's core strengths, mergers & acquisition, creating marketing, social media, digital marketing strategies, reinventing the lab, and network expansion pan-India. He is known for his teamwork and creating a highly motivated team. Network expansion, mergers and acquisitions, managing rapid growth, marketing, and team building are among his areas of competence in the industry. |

Source: Company, DAM Capital Research

PPP Diagnostics: A Large Underserved Opportunity

□ Overview

Notably, KDL hasn't had any write-offs in its >10 years of business with various government entities.

In the PPP segment, KDL collaborates with central, state and municipal government-operated health and medical facilities for the deployment and operation of its diagnostic centres.

PPP agreements (based on successful tender wins) to deploy diagnostic centres for the radiology and pathology services are typically long-term contracts (with annual price escalation provisions) that ensure visibility of revenues for its operations. The term of a contract ranges between 2 and 10 years and typically includes a term extension clause based on performance/mutual agreement.

Increasingly, PPP tender processes are managed by entities such as Big 4 firms and are conducted online in a fairly professional manner with significant transparency. Also, there has been a progressive improvement on the government receivables front, as reflected in a sharp reduction in KDL's receivable days — 56 days as of FY23 vs 97-98 days in FY18/19. Notably, KDL hasn't had any write-offs in its >10 years of business with various government entities.

Exhibit 12: Tender process overview



Source: Company, DAM Capital Research

KDL has a win rate of ~78% on its tender submissions since its existence. In most cases, KDL's primary competition in tenders is from regional players, including local diagnostic chains.

➤ How does the model work?

Typically, patients referred by government institutes to PPP centres are provided with diagnostics services free of charge. The cost of tests provided to patients is reimbursed to the service provider by the authorities.

However, private patients/walk-ins are usually charged as per the rate quoted by the service provider. In terms of services offered, essential diagnostic tests and their charges to respective patients are predetermined by the authority.

With regard to any additional services, the charges are mutually agreed upon between the authority and the concessionaire. These user charges have escalation clauses and hence, they increase over the course of the concession period. These covenants are mentioned in the agreement and have to be abided by.

➤ PPP model aims to expand reach of services

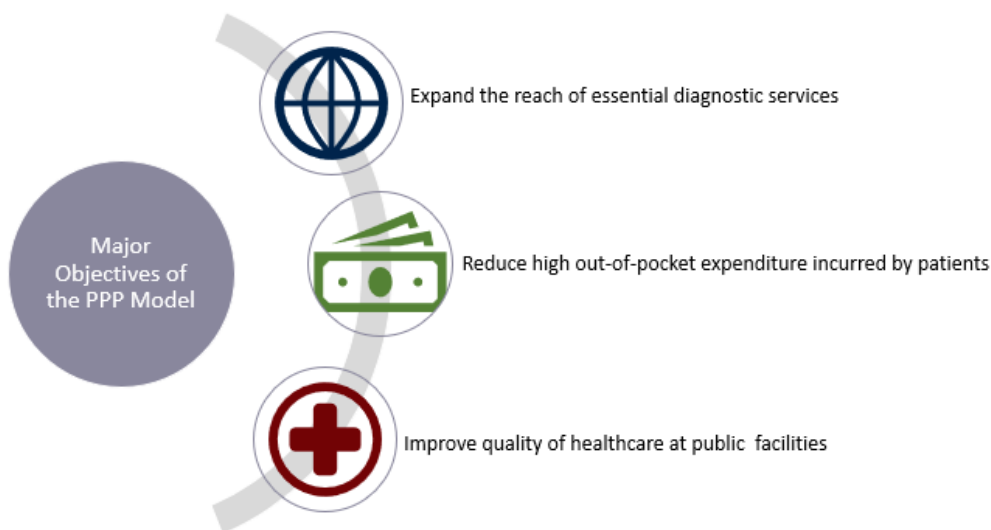
In 2015, the Government of India under the National Health Mission launched the Free Essential Diagnostics Initiative to address the high out-of-pocket expenditure on diagnostics (10% OOPE on cost of diagnostics – 11% in OPD and 9.6% in IPD as per NSSO's 71st round) and improve the quality of healthcare services.

The objective of the Free Diagnostic Services Initiative program is to ensure availability and access to essential diagnostic tests at public health facilities to reduce direct costs and out-of-pocket expenditure incurred by economically weak patients.

One aspect of this mission envisages outsourcing of high cost, technologically demanding and lower frequency diagnostic services to private service providers, while high-volume, low-cost tests not requiring highly skilled manpower are undertaken by public health facilities.

This aspect has been the primary growth driver for the PPP model in provision of radiology services.

Exhibit 13: Major objectives of the PPP model



Source: Company, DAM Capital Research

As per the NSS report, the percentage of cases receiving free medicines in urban areas is 14.4% and stands at 13.8% in rural areas.

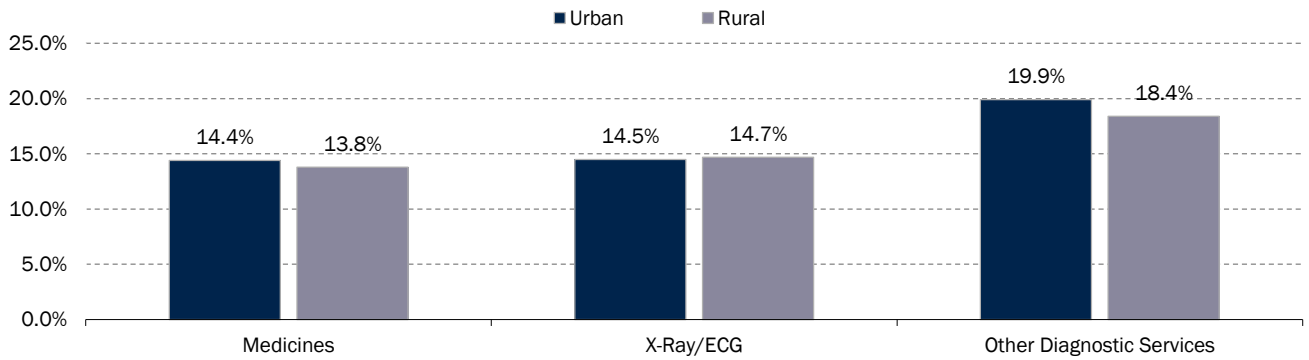
□ Massive potential for PPP model diagnostics

The National Sample Survey ("NSS") data on the percentage of cases that receive free medicines and diagnostic services reveals that the statistics do not vary significantly between urban and rural areas.

As per the NSS report, the percentage of cases receiving free medicines in urban areas is 14.4% and stands at 13.8% for rural areas. However, the trend differs slightly for other diagnostic services as the percentage is higher for urban areas (19.9%) as compared with rural areas (18.4%).

This can be attributed to low penetration of diagnostic services in rural India. This offers a huge potential for the government to get into partnerships with diagnostic players in order to tap into the highly under-penetrated rural areas of India.

Exhibit 14: Percentage of cases receiving free medicines, x-ray/ESG and other diagnostic tests



Source: Company, DAM Capital Research

Almost all existing listed healthcare companies (diagnostics/hospitals) are effectively a play on “top of the pyramid” healthcare opportunity.

➤ **Proxy for ‘bottom of the pyramid’ healthcare growth**

The Indian healthcare system can be broadly split into ‘top of the pyramid’ and ‘bottom of the pyramid’, which represent two segments with widely divergent status of healthcare services. While ‘top of the pyramid’ continues to represent the more profitable part of the Indian healthcare opportunity, the significantly underserved ‘bottom of the pyramid’ offers substantially better growth opportunities.

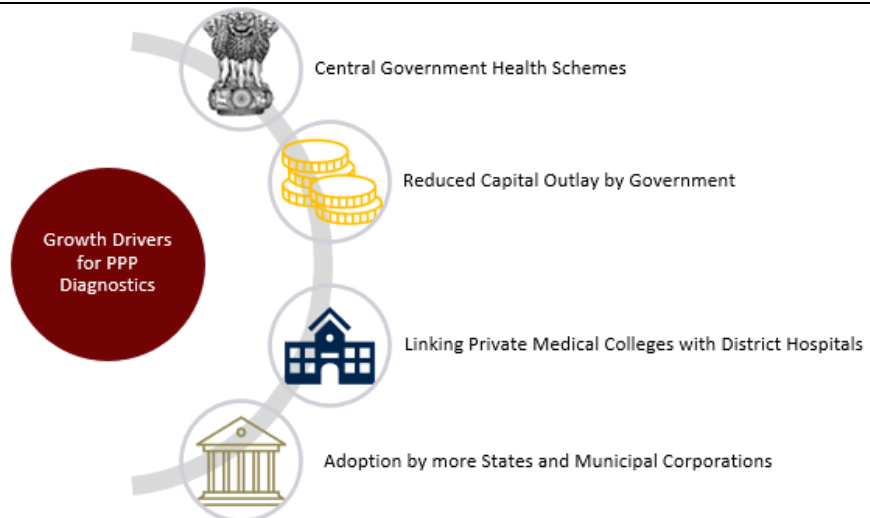
Almost all existing listed healthcare companies (diagnostics/hospitals) are effectively a play on ‘top of the pyramid’ healthcare opportunity with limited participation in the other segment. These companies have, in general, struggled to create viable models to cater to ‘bottom of the pyramid’ healthcare opportunity, e.g., hospitals in Tier 2/3 towns.

PPP diagnostics is effectively a play on the ‘bottom of the pyramid’ opportunity as most of the PPP spends are directed towards smaller urban locations and rural areas. It offers a unique and profitable opportunity to participate in the long-term growth opportunity in the Indian healthcare industry.

➤ **Growth drivers for the PPP model**

Apart from the fundamental factors, such as conducive government policies and rising non communicable diseases in the country, that drive the healthcare delivery market, an increasing share of the aged population, along with other growth drivers such as rising health awareness, growing health insurance coverage and improving affordability, also plays a crucial role.

Exhibit 15: Growth drivers for PPP diagnostics



Source: Company, DAM Capital Research

Increasing prevalence of central healthcare-related schemes

With the rising prevalence of central schemes including Ayushman Bharat, the shift seems likely, which will boost the PPP model in the diagnostic industry. The Prime Minister has also voiced his support for private sector participation in creating a network of public health laboratories under the AB-PMJAY scheme. The NITI Aayog has also come up with draft guidelines for a PPP model in healthcare that involve private players designing, building, financing, operating and maintaining medical colleges and also upgrading, operating and maintaining the associated district hospitals.

The model helps reduce capital outlay by the government

As per obligations usually cited in PPP concession agreements, the private player has to procure, finance and undertake planning, design, development, operation and maintenance of the diagnostic centre. It also involves gaining appropriate proprietary rights, licences, agreements and permissions for materials, methods, processes, and systems which are to be incorporated at the centre, at the expense of the private player. The PPP model defers immediate capital expenditure on the part of the government, and hence, the authorities can manage their budgetary allocations more effectively. The private player gets reimbursed on a timely basis as per its performance over the course of the concession period.

Adoption by more states and municipal corporations

Health comes under the state list and hence, most of the development in the PPP model of diagnostic has been through state government initiatives. The PPP model has gained traction with the pushing of NHM's Free Diagnostic Initiative. The scheme involves strengthening the diagnostic capabilities and enhancing the reach of government facilities via the PPP model or in-house. Either way, the private player is involved in the process. Not only states but also municipal corporations are taking advantage of the PPP model to boost their healthcare goals.

PPP model to link new or existing private medical colleges with functional district hospitals

To address the shortage of qualified doctors and improve the medical education infrastructure, NITI Aayog has proposed the PPP model linking new or existing private medical colleges with functional district hospitals, and thereby augmenting medical seats. Under this envisioned model, a concessionaire will design, build, finance, operate and maintain the medical college and also upgrade, operate and maintain the associated district hospital with a minimum annual student intake of 150 MBBS seats. The concessionaire will provide all healthcare services to patients free of cost after the beneficiaries pay the registration fee of ₹10. The scheme, if implemented, will further boost opportunities for diagnostic service providers to facilitate required services under the PPP model. This is because the model concession agreement also aims to provide free/cheap diagnostic services to patients covered under the Ayushman Bharat Yojana or any other state insurance scheme.

□ Advantage of PPP model for private operators

Apart from having a positive impact on public healthcare and lowering government expenditure associated with this, the PPP model offers multiple advantages to the private sector.

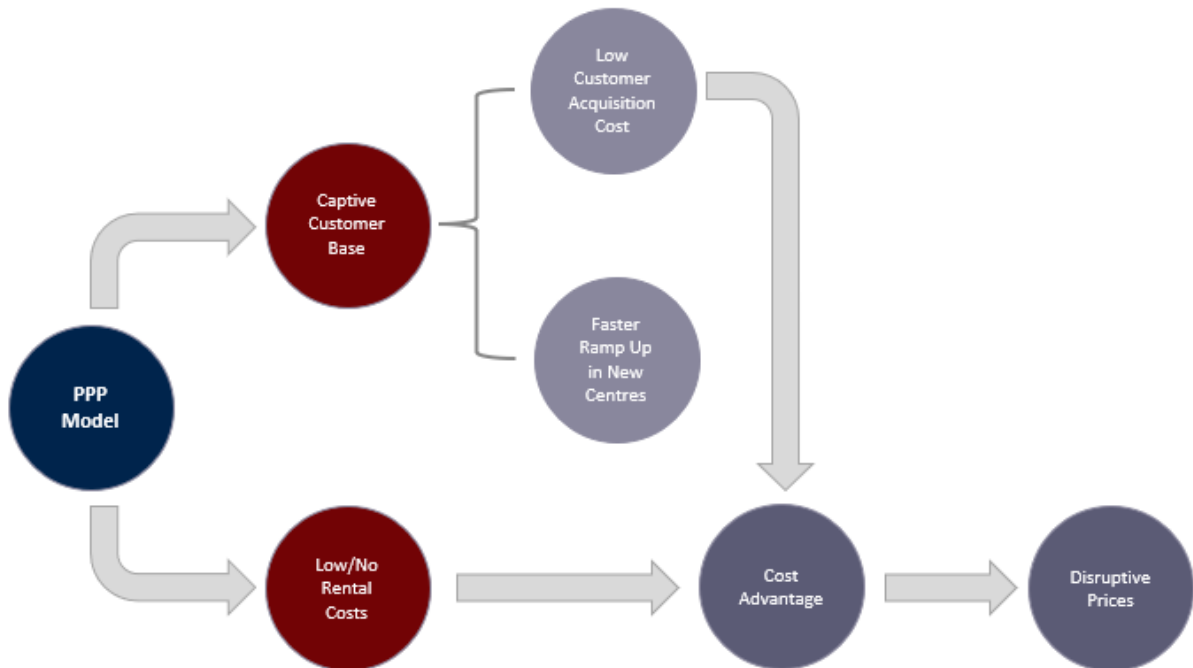
The shop-in-shop model followed under the PPP structure allows a private diagnostic operator to leverage a large base of captive patients, implying limited/no outgo on marketing/customer acquisition costs.

This, combined with negligible rental costs and large patient volumes, substantially lowers the operating cost base and significantly accelerates the breakeven timeline, as compared to a standalone private centre.

Health comes under the state list and hence, most of the development in the PPP model of diagnostic has been through state government initiatives.

As a result, the operator of the PPP centre is able to provide extremely disruptive pricing and capture market share.

Exhibit 16: Advantages of PPP diagnostics business model



Source: Company, DAM Capital Research

□ What is KDL's right to win in the segment?

Typically, in PPP tenders, players with an established track record and most competitive prices win the contract. In most cases, KDL's primary competition in tenders comprises regional players, including local diagnostic chains which operate at a substantially lower scale.

A business model that is specifically tailored for PPP contracts, large-scale operations, operational efficiency, and an existing infrastructure base makes Krsnaa a dominant player in this segment. This is evident from the company's tender win rate of ~78%.

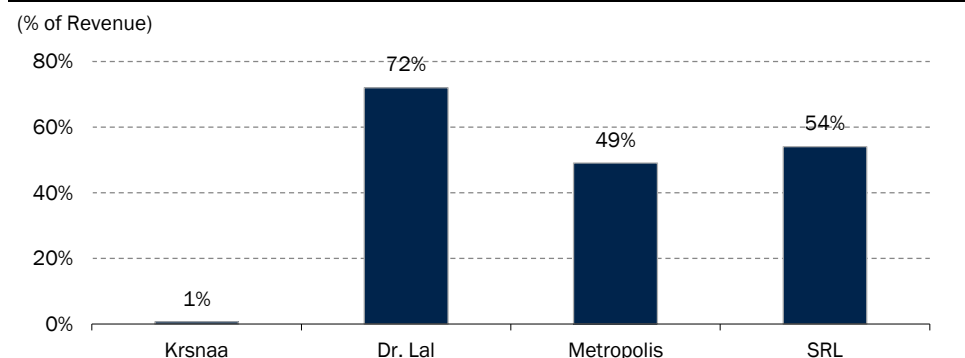
➤ Lower contribution from franchise B2C stores

Unlike its peers, Krsnaa derives negligible revenues from franchise B2C stores. This allows the company to place highly competitive bids for PPP contracts.

In case of peers, the cost of tests at franchise stores effectively acts as a floor price to ensure uniformity in pricing across outlets, when placing tender bids.

As a result, competition for tenders is usually limited to smaller regional players.

Exhibit 17: Krsnaa has the lowest revenue contribution from B2C



Source: Company, DAM Capital Research

➤ **Larger scale of operations**

Krsnaa operates over 133 CT/MRI centres, 1,090 pathology centres and 99 pathology processing labs across the country, serving over 10mn patients in FY23. The company's scale of operations, combined with strong vendor relationships, allows it to negotiate favourable terms for machines and equipment which places it in an advantageous position as compared to its smaller competitors.

➤ **Operational efficiency**

Backing the company's large scale of operations is its state-of-the-art tele-reporting hub in Pune which employs over 220 radiologists. Under this arrangement, the test image is transferred to the hub for the preparation of the final report, allowing Krsnaa to operate its outlets without requiring the presence of individual radiologists at each location.

Given that the hub has sufficient capacity for processing up to ~13x of FY23 test volumes, Krsnaa should be able to add new stores without the need to hire additional individual radiologists at each location, lowering the marginal cost of adding an outlet.

A PPP contract is usually valid for a term of 2-10 years with a built-in term extension clause which can be activated contingent on performance and mutual agreement

Exhibit 18: Large capacity headroom

| Test | Monthly Capacity | FY23 Annual Volumes | Headroom |
|----------------|------------------|---------------------|----------|
| CT Scans | 2,00,000 | 9,17,666 | 7.8x |
| MRIs | 41,000 | 3,82,553 | 3.9x |
| Tele-Reporting | 20,00,000 | 55,60,646 | 12.8x |

Source: Company, DAM Capital Research

Additionally, this model also allows the cost of radiologists at the Pune hub to be spread over a larger volume of tests, leading to operating leverage benefits.

➤ **Existing investment in infra leads to high renewal percentage**

A PPP contract is usually valid for a term of 2-10 years with a built-in term extension clause which can be activated contingent on performance and mutual agreement. Further, considering its services at competitive rates, public health agencies have often expanded the coverage of the scope of its services to additional centres without any additional bidding process.

Notably, in recent quarters, the competition for tenders has shifted increasingly towards smaller regional players. Given Krsnaa's large base of existing infrastructure from PPP contracts, operational efficiency and cost competitiveness driven by scale, the company enjoys a high probability of tender renewals.

Exhibit 19: Virtuous cycle of tender wins



Source: Company, DAM Capital Research

Strategic Foray into B2C Pathology Space

While B2G remains the mainstay of KDL's growth plans, the company has recently undertaken a strategic foray into the highly competitive B2C pathology testing business.

In order to build this business, management intends to leverage the existing base of PPP radiology centres in a region to build a funnel of customers to nearby franchisee-owned B2C pathology centres, which would limit marketing spends. This would enable the company to offer holistic diagnostic services to the patient under one umbrella.

The company would require franchisees to make upfront deposits against the fees payable to it (80% of revenues).

Since B2C franchise stores would charge 20% higher prices for pathology tests as compared to a typical PPP store, they would be retained by the franchisee to compensate for operating the store. Despite the 20% delta, KDL's B2C offering would still charge prices which are substantially lower than its competitors.

To this end, the company has recently introduced affordable wellness packages. Further, given the fixed cost nature of operations, KDL's margins in the segment are expected to be similar to those at the corporate level (~25-30%).

Currently, the company has 42 live franchise locations across Maharashtra and Punjab.

Robust Growth Visibility Supported by New Tenders

□ Strong tender wins

Based on disclosures filed on the exchanges, the cumulative peak revenue potential of tenders awarded to Krsnaa over the last year amounts to Rs5bn, which is ~1x of FY23 revenues. Notably, the rollout of a tender after signing the contract typically requires a period of 6-12 months. The length of a tender usually ranges between 7 and 10 years.

Exhibit 20: Potential for almost 2.5x revenues over the next 4-5 years based on disclosed tender pipeline

| Region | Date | Details | Peak Revenue (Rs m) |
|-------------------------------------|--------|--------------------------------------|---------------------|
| Maharashtra | Jul'22 | 39 CT scans | 500 |
| BMC | Jan'23 | 600 Collection Centres | 400 |
| Odisha | Feb'23 | 5 Hub Labs & 386 Collection Centres | 500 |
| Rajasthan | Mar'23 | Free Diagnostic Services (Pathology) | 3,000 |
| Assam | May'23 | | 600 |
| Total (A) | | | 5,000 |
| FY23 Revenue (B) | | | 4,871 |
| Potential Growth (1+(A)/(B)) | | | 2.0 |

Source: Company, DAM Capital Research

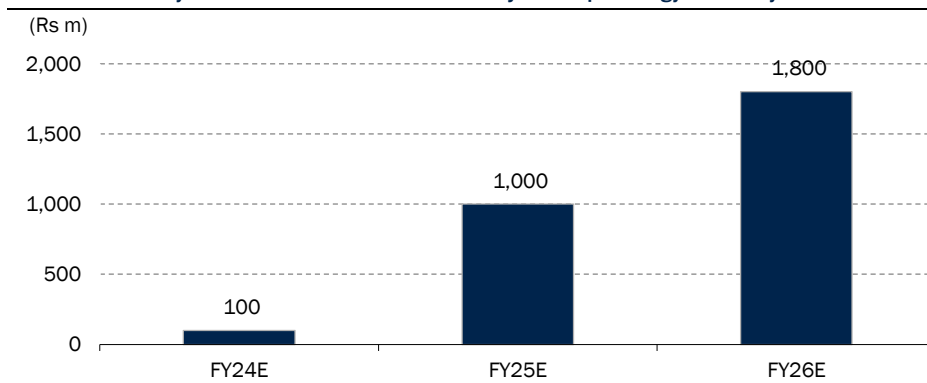
Rajasthan pathology tender: In May 2023, the company received a letter of acceptance from the National Health Mission, Rajasthan. As part of the tender requirements, the company was required to provide additional performance security to Krsnaa.

In July 2023, owing to disagreements over the provision of additional performance security, the authorities decided to cancel the letter of acceptance. In light of this situation, the company in collaboration with Telecommunication Consultants India Ltd, 'TCIL', (GOI-owned consortium partner) took legal recourse and approached the Rajasthan High Court.

In August 2023, the court ruled in favour of the company and directed the company to fulfill the conditions pertaining to the additional performance security. In line with this judgement, the authorities are also willing to go ahead with the agreement and execute the project with no contest remaining between the parties.

Revenues from the contract are expected to start accruing in CY24/FY25. Given that this is a tender for 1,300 collection centres across the state which would entail significant logistics costs, management expects EBITDAM of 25% on the tender – expected from the first year itself. We estimate yearly revenues of Rs1.8bn from the contract by FY26E. Notably, management estimates are significantly more aggressive than our estimates.

Exhibit 21: Yearly revenue run rate of Rs2bn for Rajasthan pathology tender by FY26E



Source: Company, DAM Capital Research

□ Scale-up in ongoing tenders

Among the ongoing tenders, the Punjab Radiology/Pathology and Himachal Pradesh Pathology tenders present large opportunities. Apart from the new tenders, scaling up of ongoing tenders is expected to be a major growth driver for Krsnaa.

Exhibit 22: Major ongoing new tenders to deliver a revenue CAGR of 40% between FY23 and FY26E

| Tender (Rs m) | FY23 | FY24E | FY25E | FY26E | CAGR (%) |
|------------------------------|------------|--------------|--------------|--------------|------------|
| Punjab PPP | 390 | 650 | 800 | 1,000 | 37% |
| Himachal Pradesh (Pathology) | 290 | 600 | 750 | 850 | 43% |
| Total | 680 | 1,250 | 1,550 | 1,850 | 40% |

Source: Company, DAM Capital Research

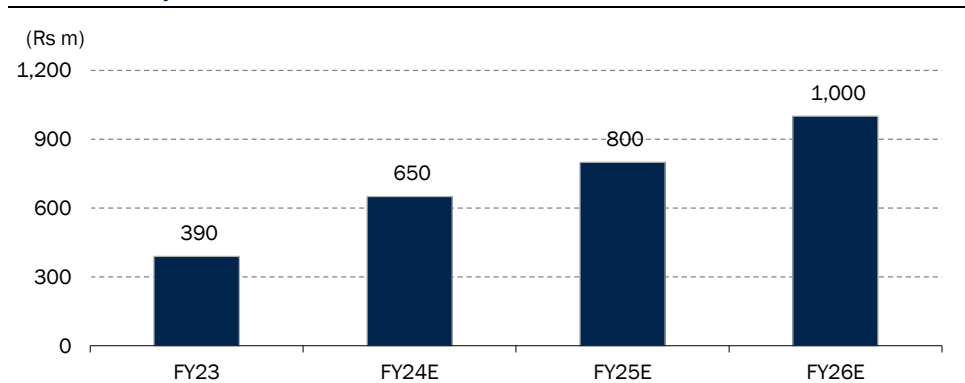
Combined, the two tenders are expected to deliver a revenue CAGR of 40% between FY23 and FY26E and contribute Rs1.9bn to revenues by FY26E.

Punjab: Implementation of the tender got delayed by ~6 months owing to delays in land allotment from the government, driven by a regime change post the state elections. As of Q4FY23, the company had operationalised all 25 radiology centres, 30 hub labs and 95 collection centres. As per initial estimates, the tender was estimated to ramp up to Rs1bn annual revenues by FY25E. However, we estimate the company to reach this run rate by FY26E.

The disparity from original estimates is largely due to the State Government's decision to not offer free diagnostic services, which has been seen in other states. The revenues would be 50/50 between radiology and pathology. Both segments are growing at a similar trend.

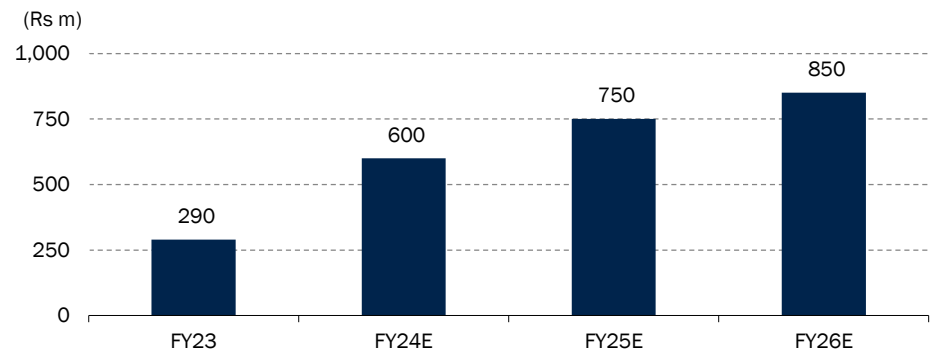
Since the tender is not covered under FDS (Free Diagnostic Services), Punjab PPP is purely a cash business. From a working capital perspective, we note that a cash business is superior to FDS, albeit the revenue ramp up is gradual.

Exhibit 23: Punjab PPP revenue CAGR of 37% between FY23 and FY26E



Source: Company, DAM Capital Research

Himachal Pradesh: Tests under this tender are covered by FDS, which should lead to a healthy scale up. Management indicated that roll out of the tender is complete. An annual revenue run rate of Rs850mn is expected from the tender by FY26E.

Exhibit 24: HP tender estimated to deliver revenue CAGR of 43% between FY23 and FY26E

Source: Company, DAM Capital Research

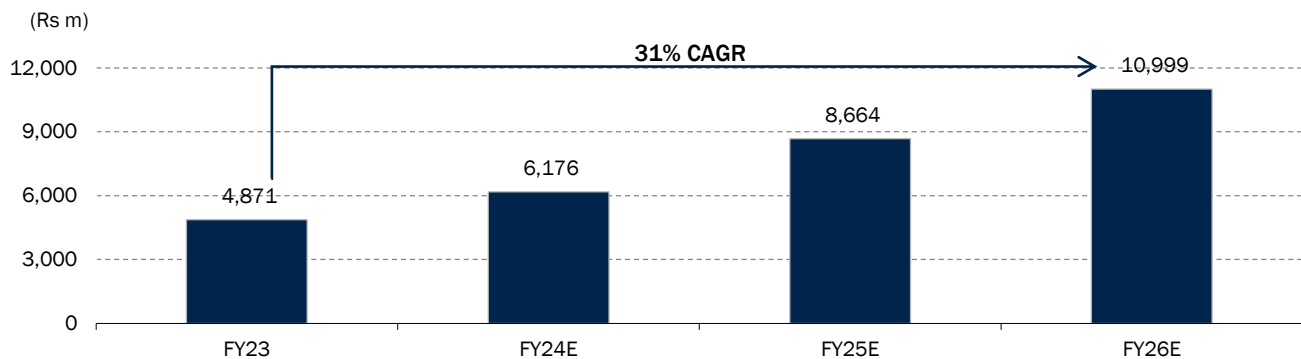
Financial Projections

Increasing contribution from the recently won tenders, combined with a scale up in the base business on the back of price escalation clauses in existing contracts, is expected to drive revenue/EBITDA/PAT CAGR of 31%/34%/40% between FY23 and FY26E, with ROCE/ROE inching up to 20%/15% respectively.

□ Recent tender wins to drive 31% revenue CAGR between FY23 and FY26E

Between FY23 and FY26E, we project Krsnaa's revenues to deliver a CAGR of 31%, largely driven by the new tenders. Considering that all the major tenders awarded to Krsnaa over the last year are in the Pathology segment, we expect a relatively short ramp up timeline after the commencement of operations at these centres.

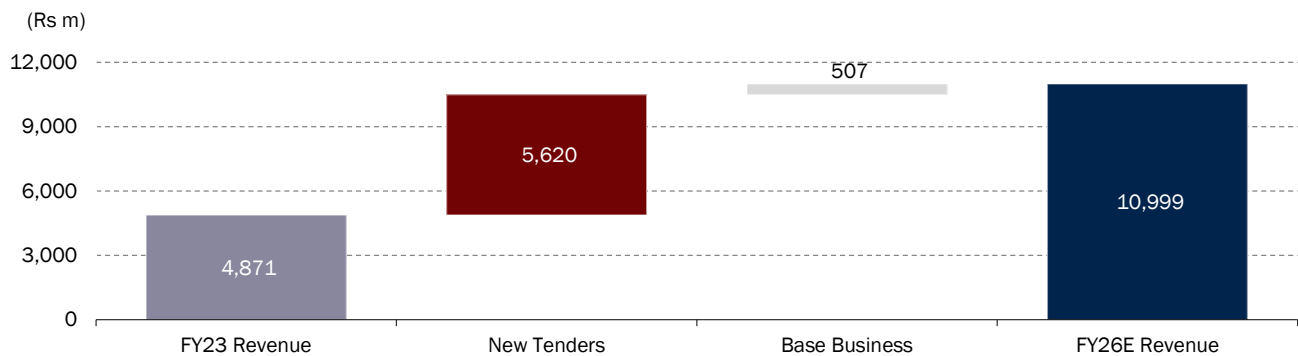
Exhibit 25: We estimate a revenue CAGR of 31% between FY23-26E



Source: Company, DAM Capital Research

Notably, 92% of the incremental revenue for FY26E over FY23 is expected to be driven by new tenders, while the remaining is expected to be driven by a steady scale up in existing contract revenues on the back of price escalation clauses.

Exhibit 26: FY26E revenue bridge



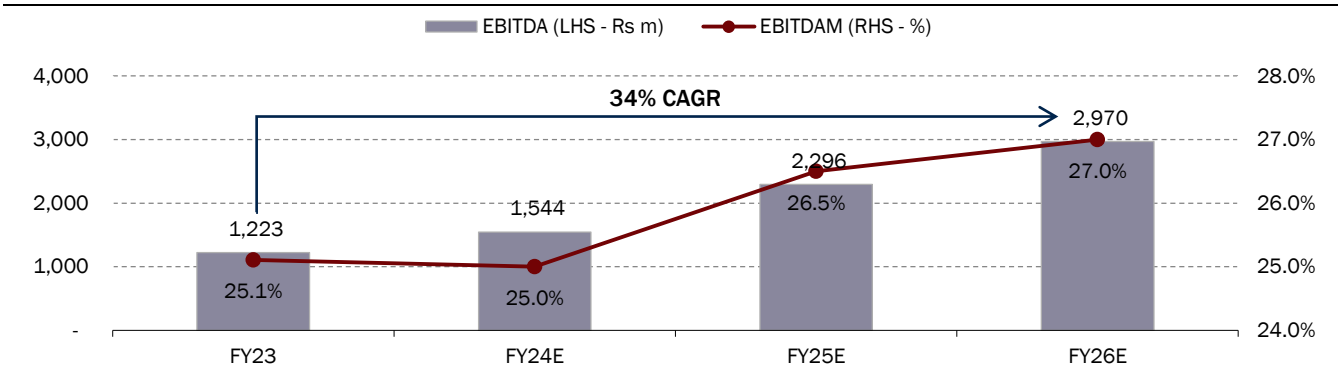
Source: Company, DAM Capital Research

□ EBITDAM expansion to be driven by ramp up in new centres/op. leverage

In FY23, Krsnaa's EBITDAM declined on a YoY basis, largely due to implementation of various tenders. The new centres established in this process are yet to mature in terms of revenues but have already added to the operating cost base. We expect these centres to ramp up FY24E onwards, which is expected to lead to a jump in EBITDAM from FY25E.

We project Krsnaa to deliver an EBITDA CAGR of 34% between FY23 and FY26E, with EBITDAM inching up to 27% (+200 bps) over this period driven by operating leverage and ramp up in new centres.

Exhibit 27: KRSNAA is expected to deliver an EBITDA CAGR of 34% between FY23-26E

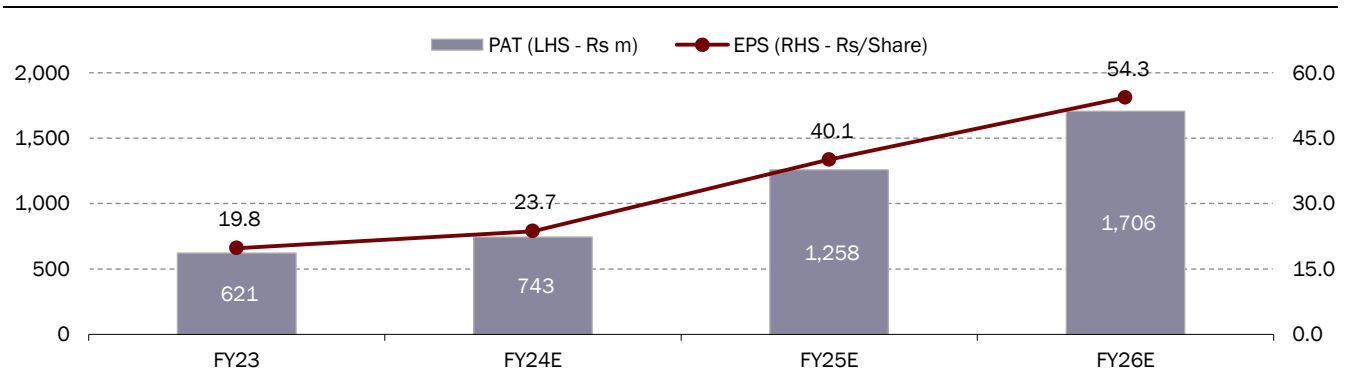


Source: Company, DAM Capital Research

Higher EBITDA to drive PAT/EPS growth

We estimate a CAGR of 40% in PAT/EPS between FY23 and FY26E, driven by healthy EBITDA growth on a stable fixed cost base. Tax rate over this period is expected to remain at ~25%.

Exhibit 28: PAT/EPS CAGR of 40% between FY23 and FY26E



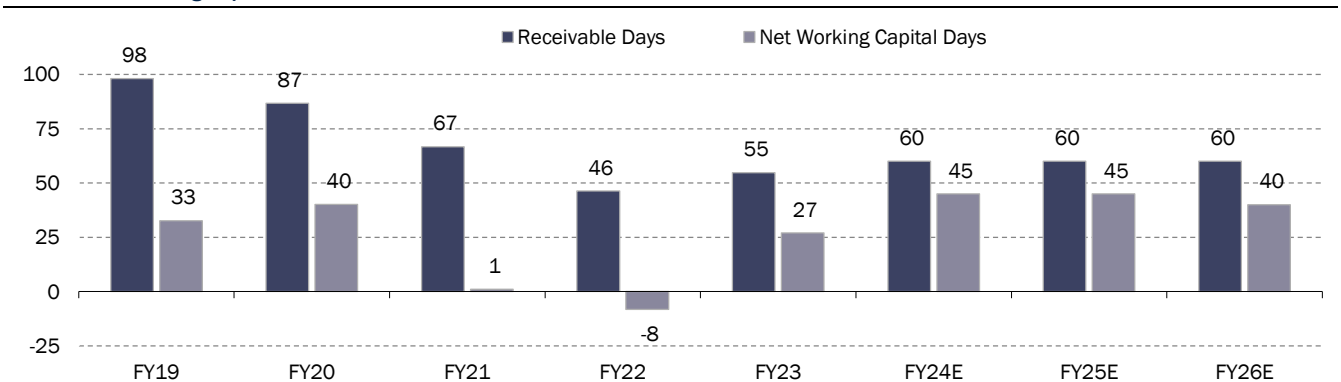
Source: Company, DAM Capital Research

Cash/net debt

Working capital to remain in a comfortable position

There has been a progressive improvement on the government receivables front as reflected in a sharp reduction in KDL's receivable/NWC days. Notably, KDL hasn't had any write-offs in its >10 years of business with various government entities. We expect the company to maintain NWC of 40-45 days going forward.

Exhibit 29: Working capital trends

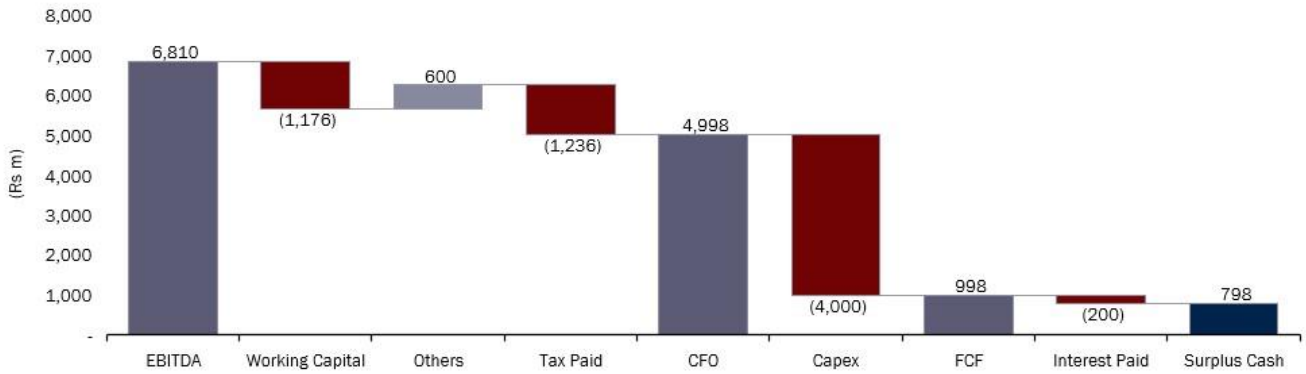


Source: Company, DAM Capital Research

➤ **Sturdy CFO generation to support growth capex...**

Robust EBITDAM, combined with calibrated working capital requirements, is expected to result in Krsnaa generating a cumulative CFO of ~Rs5bn between FY24E and FY26E (73% CFO/EBITDA). Capex spends during this period are expected to remain elevated at Rs4bn on the back of execution of recently won tenders.

Exhibit 30: Cumulative cash flow (FY24-26E)



Source: Company, DAM Capital Research

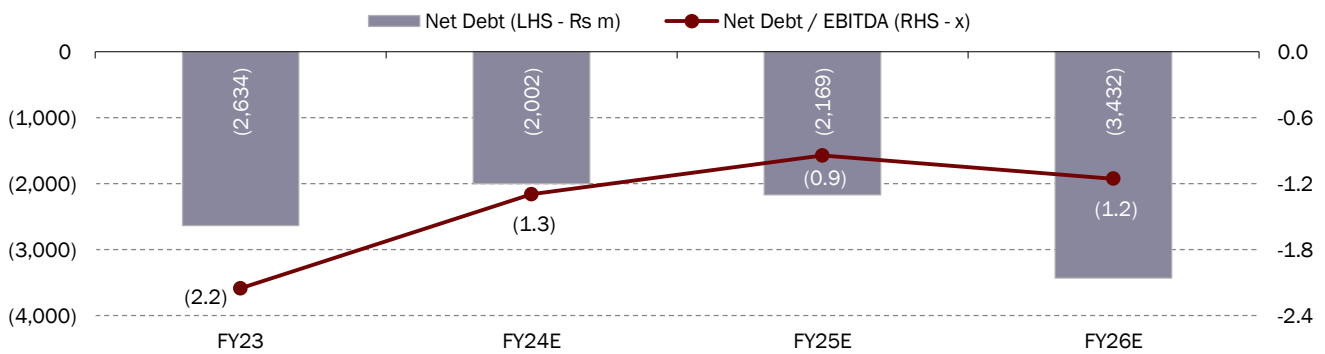
Given the strong CFO generation, we expect Krsnaa to be able to comfortably fund its capex requirements through internal accruals.

After interest expenses, we expect the company to be left with a cash surplus of ~Rs800 for FY24-26E.

➤ **...and improve cash position**

As a result, we estimate the company’s net cash balance to increase by ~Rs800mn. M&A action could lead to a change in the leverage metrics.

Exhibit 31: Projected to maintain a net cash balance sheet

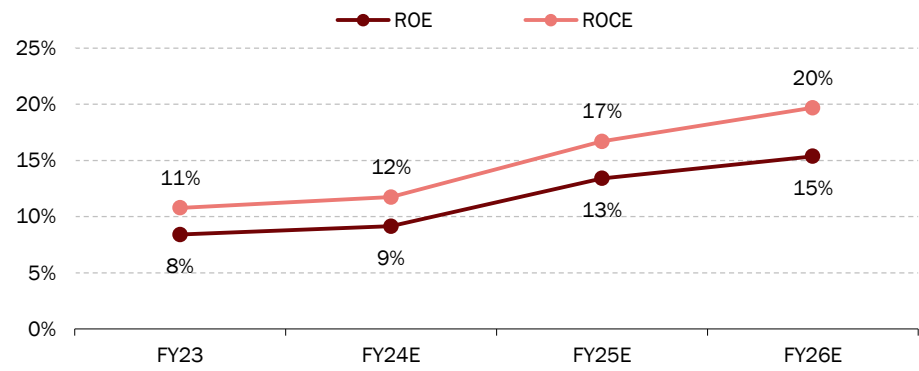


Source: Company, DAM Capital Research

❑ **Scale up in return ratios**

The combination of improving profitability and a healthy balance sheet should enable the company to showcase a steady improvement in its return ratios. We estimate ROCE/ROE to inch up to 20%/15% by FY26E.

Exhibit 32: ROCE/ROE to inch up to 20%/15% by FY26E respectively



Source: Company, DAM Capital Research

Key Risks

- **Dependence on government policies/regimes**

KDL is focused on operating diagnostic centres in existing facilities of public healthcare agencies. Its future operations are dependent on the policies and budgetary allocations available to such public healthcare agencies to deploy diagnostic centres within their existing facilities. Any change in the policy by the state or central government or a change in the regime could have an adverse impact on its business, financial condition and results of operation, as in the case of the Punjab tender.

- **Payments dependent on contracts with public agencies**

Over the last few years, a majority of the company's revenue from operations has been generated from contracts with public health agencies. Its future success is to a large extent dependent on its ability to maintain good relationships with public health agencies. If its relationship with these entities deteriorates or if it is unable to fulfil its contractual obligations, the contracts may be terminated and these entities may form contracts with other providers, as was the case initially with the Rajasthan tender. This would materially impact KDL's business.

- **Diagnostics industry in India is highly competitive**

The diagnostics industry in India is highly competitive with several companies present in the market, and therefore it is challenging to improve market share and profitability. The company competes on the breadth of its test offerings, the geographical reach of its network, its ability to accurately undertake scans or process specimens and report data in a timely manner, as well as on its patient relationships.

Also, the pricing-related competition may intensify in the near future which may have an adverse impact on the results of its operations, including profit margins.

- **Higher competition when bidding for tenders**

KDL's larger competitors may modify their business model to benefit from increased cost efficiencies and bid for tenders at a significant discount to its prices. If KDL is unable to compete effectively, its future growth could be impacted.

Income statement

| Year to 31 Mar (Rs m) | FY22 | FY23 | FY24E | FY25E | FY26E |
|----------------------------|--------------|--------------|--------------|--------------|---------------|
| Net sales | 4,555 | 4,871 | 6,176 | 8,664 | 10,999 |
| % growth | 14.9 | 7.0 | 26.8 | 40.3 | 26.9 |
| Operating expenses | 3,240 | 3,648 | 4,632 | 6,368 | 8,029 |
| EBITDA | 1,315 | 1,223 | 1,544 | 2,296 | 2,970 |
| % change | 40.1 | (7.0) | 26.2 | 48.7 | 29.3 |
| Other income | 149 | 194 | 200 | 200 | 200 |
| Net interest cost | 185 | 77 | 100 | 50 | 50 |
| Depreciation | 414 | 538 | 653 | 769 | 846 |
| Pre-tax profit | 865 | 802 | 991 | 1,677 | 2,274 |
| Deferred tax | 6 | 31 | 0 | 0 | 0 |
| Current tax | 175 | 150 | 248 | 419 | 569 |
| Profit after tax | 684 | 621 | 743 | 1,258 | 1,706 |
| Preference dividend | 0 | 0 | 0 | 0 | 0 |
| Minorities | 0 | 0 | 0 | 0 | 0 |
| Adjusted net profit | 684 | 621 | 743 | 1,258 | 1,706 |
| Non-recurring items | 0 | 0 | 0 | 0 | 0 |
| Reported net profit | 684 | 621 | 743 | 1,258 | 1,706 |
| % change | (63.0) | (9.2) | 19.6 | 69.3 | 35.6 |

Balance sheet

| As on 31 Mar (Rs m) | FY22 | FY23 | FY24E | FY25E | FY26E |
|---------------------------------------|--------------|--------------|--------------|---------------|---------------|
| Paid-up capital | 157 | 157 | 157 | 157 | 157 |
| Preference capital | 0 | 0 | 0 | 0 | 0 |
| Reserves & surplus | 6,687 | 7,230 | 7,973 | 9,232 | 10,937 |
| Shareholders' equity | 6,844 | 7,387 | 8,130 | 9,389 | 11,094 |
| Total current liabilities | 1,428 | 937 | 508 | 582 | 701 |
| Total debt | 256 | 165 | 565 | 365 | 115 |
| Deferred tax liabilities | 70 | 114 | 114 | 114 | 114 |
| Other non-current liabilities | 155 | 482 | 482 | 482 | 482 |
| Total liabilities | 1,910 | 1,698 | 1,669 | 1,542 | 1,412 |
| Total equity & liabilities | 8,754 | 9,085 | 9,799 | 10,931 | 12,506 |
| Net fixed assets | 4,116 | 4,933 | 5,780 | 6,511 | 6,666 |
| Investments | 3 | 3 | 3 | 3 | 3 |
| Cash | 2,419 | 1,088 | 856 | 823 | 1,836 |
| Other current assets | 923 | 1,170 | 1,269 | 1,702 | 2,110 |
| Deferred tax assets | 0 | 0 | 0 | 0 | 0 |
| Other non-current assets | 1,293 | 1,891 | 1,891 | 1,891 | 1,891 |
| Net working capital | 1,914 | 1,321 | 1,617 | 1,944 | 3,245 |
| Total assets | 8,754 | 9,085 | 9,799 | 10,931 | 12,506 |

Cash flow

| Year to 31 Mar (Rs m) | FY22 | FY23 | FY24E | FY25E | FY26E |
|-----------------------------|--------------|----------------|--------------|--------------|--------------|
| Pre-tax profit | 865 | 802 | 991 | 1,677 | 2,274 |
| Depreciation | 414 | 538 | 653 | 769 | 846 |
| Chg in Working capital | (33) | (738) | (528) | (360) | (288) |
| Total tax paid | (181) | (181) | (248) | (419) | (569) |
| Net Interest | 185 | 77 | 100 | 50 | 50 |
| Others | 0 | 0 | 0 | 0 | 0 |
| Operating cash flow | 1,250 | 498 | 968 | 1,717 | 2,313 |
| Capital expenditure | (1,431) | (1,360) | (1,500) | (1,500) | (1,000) |
| Free cash flow (a+b) | (182) | (862) | (532) | 217 | 1,313 |
| Chg in investments | 0 | 0 | 0 | 0 | 0 |
| Debt raised/(repaid) | (1,771) | (91) | 400 | (200) | (250) |
| Net interest | (185) | (77) | (100) | (50) | (50) |
| Capital raised/(repaid) | 92 | 0 | 0 | 0 | 0 |
| Dividend (incl. tax) | 0 | 0 | 0 | 0 | 0 |
| Other items | 0 | 0 | 0 | 0 | 0 |
| Net chg in cash | 890 | (1,331) | (232) | (33) | 1,013 |

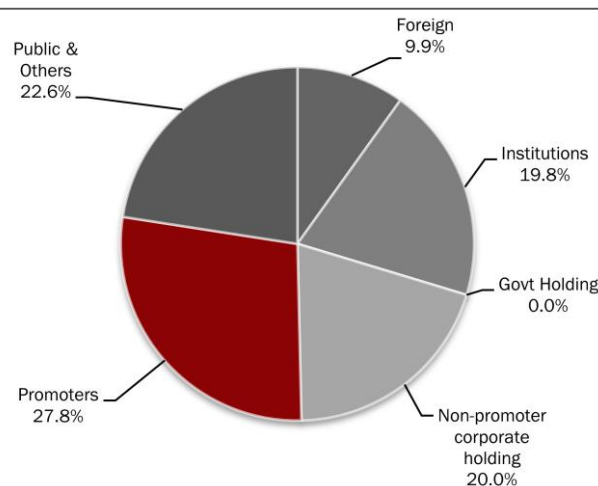
Key ratios

| Year to 31 Mar | FY22 | FY23 | FY24E | FY25E | FY26E |
|----------------------|-------|-------|-------|-------|-------|
| EBITDA margin (%) | 28.9 | 25.1 | 25.0 | 26.5 | 27.0 |
| EBIT margin (%) | 19.8 | 14.1 | 14.4 | 17.6 | 19.3 |
| PAT margin (%) | 15.0 | 12.8 | 12.0 | 14.5 | 15.5 |
| RoE (%) | 14.9 | 8.7 | 9.6 | 14.4 | 15.4 |
| RoCE (%) | 15.2 | 8.9 | 10.2 | 15.6 | 17.7 |
| Gearing (x) | (0.3) | (0.1) | 0.0 | 0.0 | (0.2) |
| Net debt/ EBITDA (x) | (1.6) | (0.8) | (0.2) | (0.2) | (0.6) |
| FCF yield (%) | (1.0) | (4.7) | (2.9) | 1.2 | 7.1 |
| Dividend yield (%) | 0.0 | 0.0 | 0.0 | 0.0 | 0.0 |

Valuations

| Year to 31 Mar | FY22 | FY23 | FY24E | FY25E | FY26E |
|--------------------------|-------------|-------------|-------------|-------------|-------------|
| Reported EPS (Rs) | 21.8 | 19.8 | 23.7 | 40.1 | 50.1 |
| Adj. EPS (Rs) | 21.8 | 19.8 | 23.7 | 40.1 | 50.1 |
| PE (x) | 26.9 | 29.6 | 24.8 | 14.6 | 11.7 |
| Price/ Book (x) | 2.7 | 2.5 | 2.3 | 2.0 | 1.7 |
| EV/ Net sales (x) | 3.6 | 3.6 | 2.9 | 2.1 | 1.4 |
| EV/ EBITDA (x) | 12.4 | 14.3 | 11.7 | 7.8 | 5.2 |
| EV/ CE (x) | 2.2 | 2.1 | 1.9 | 1.7 | 1.4 |

Shareholding pattern



As of Jun-23

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