Kasthamandap Diagnostic and Medical Service Private Limited: Long-term rating upgraded and removed from 'Issuer not cooperating' category

June 03, 2024

Summary of rating action

Instrument (Amounts NPR in Million)	Last Rated Amount	Current Rated Amount	Rating Action
Long-term loans: fund based (Term loans)	560	546	**[ICRANP] LB+**; upgraded from [ICRANP] LB and removed from 'Issuer not cooperating' category
Total	**560**	**546**	

Rating action

ICRA Nepal has upgraded the long-term loan rating of Kasthamandap Diagnostic and Medical Service Private Limited (KDMS) to [ICRANP] LB+ (pronounced ICRA NP L B plus) from [ICRANP] LB (pronounced ICRA NP L B). The rating has also been removed from 'Issuer Not Cooperating' category.

Rationale

The rating action draws comfort from the experienced background of the company's promoter viz. Kathmandu Medical College Public Limited (KMC, with 100% stake), which has a long operational track record (since 2009) in medical education and healthcare sector. Further, the locational advantage of being adjacent to KMC (with sizeable patient flow) is likely to enhance the company's operational and financial profile. ICRA Nepal also takes positive note of the company's strategic importance to its parent company, since it has entirely outsourced its diagnostic services to KDMS, which is also reflected in adequate financial and operational support by KMC. Additionally, the rating also draws comfort from the company's improving trends in revenue and its healthy margins (albeit supported by operational support from KMC through leasing its equipment at nominal arbitrary fees/lease charges).

Nonetheless, the rating remains constrained by high project stabilization risks amid intense competition among diagnostic service providers in Kathmandu. Given the high debt funded capex (mostly land and building, through 80% debt), the company's debt service coverage indicators remain modest (DSCR of 0.9 times for FY2023), hence necessitating promoter support, while its gearing remains high at 4.4 times as of mid-July 2023 (against regulatory cap of 4.0 times). However, KMC with relatively better financial profile, has provided a corporate guarantee for KDMS's line of credit and provided promoter support for loan repayments and has charged low management fees which mitigates these concerns to an extent. However, any changes in management fee structure would have a bearing on KDMS's margins and ultimately its debt protection metrics. Incrementally, the company's ability to generate adequate revenues, margins and hence maintain comfortable debt coverage and capitalisation indicators, would remain the key rating sensitivities.

Key rating drivers

Credit strengths

Experienced promoter with established operational track record; synergies expected in operations – KMC, the sole promoter, began operations in 2009 as a medical college and teaching hospital, while KDMS has started operating on its own property adjacent to KMC from January, 2022. Initially, KDMS offered only CT scan services and gradually started adding other radiology services including MRI by leasing the equipment from KMC. The steady patient inflow at KMC supports KDMS's revenue generation prospects through referrals. KDMS is an integral part of KMC and the continuous support from promoters, as seen in past, is likely to create business and financial synergies.

Improving revenue trends and healthy margins – The company has been reporting steady growth in revenue after starting operations. KDMS began offering CT scan services in January 2022, followed by X-Ray, USG and MRI scans from the last quarter of FY2023. Since then, patient flow and revenues have increased in 9MFY2024 (annualized revenue growth of ~63%). The growing volume of scans and rising average realization indicate a positive revenue outlook for KDMS. Although revenue is closely tied to KMC's patient inflow, which has recently decreased, referrals from other hospitals amid the dense population density in the city could also aid the company's revenue profile. The company reported healthy operating profit margins on the backdrop of low lease rental and management fees charged by the promoter company. Nonetheless, the margins remain susceptible to any changes in the management fees/rental structure, which currently are charged on an arbitrary basis.

Credit challenges

Stretched financial profile in initial years of operations – The company underwent sizeable capex of ~NPR 704 million in FY2022 (mainly to acquire its current premises) which was funded through debt of ~80%. Despite reporting healthy margins, the company's revenue is yet to scale up vis-à-vis the debt burden as reflected in modest coverage indicators with DSCR of 0.9 times in FY2023 (0.3 times in FY2022). Hence, the shortfall necessitated promoter support from KMC for debt servicing so far. The capitalisation indicators of the company remain stretched with total debt to OPBITDA of 9.2 times and gearing of 4.4 times as of mid-July 2023.

Project stabilization risk amid intense competition in fragmented industry – KDMS faces intense competition from existing government and private hospitals as well as numerous diagnostic centers in the city. While patient flow from KMC offers some reassurance, KDMS's ability to generate sufficient revenue in this competitive landscape is yet to be proven, especially on the backdrop of reducing patient volume in KMC and low track record of KDMS so far.

Link to the previous rating rationale:
Rationale – Kasthamandap Diagnostic and Medical Services Private Limited INC-BLR November-2023

Analytical approach: For arriving at the ratings, ICRA Nepal has applied its rating methodology as indicated below**.**

Link to the applicable criteria:
Corporate Credit Rating Methodology

About the company

Incorporated in July 2021, Kasthamandap Diagnostic and Medical Service Private Limited (KDMS) runs a diagnostic centre located in Sinamangal, Kathmandu (adjacent to the parent company's hospital). It provides radiology services (CT scan, MRI, USG, and X-Ray). The company is promoted by Kathmandu Medical College Public Limited (100% stake) which has an operational track record of more than 15 years.

Key financial indicators (Standalone)

	FY2022 (Audited)	FY2023 (Audited)
Operating income-OI (Revenues in NPR million)	19	67
OPBDITA/OI (%)	80%	93%
Total debt/Tangible net-worth-TNW (times)	4.8	4.4
Total outside liabilities/TNW (times)	4.9	4.4
Total debt/OPBDITA (times)	13.9	9.2
Interest coverage (times)	0.3	1.0
DSCR (times)	0.3	0.9

Source: Company data

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