October 23, 2020 Revised

Rainbow Children's Medicare Private Limited: Rating upgraded and Outlook revised to Stable

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-Convertible Debentures	100.00	50.00	[ICRA]AA-(Stable); upgraded from [ICRA]A+(Positive)
Total	**100.00**	**50.00**	

**Instrument details are provided in Annexure-1*

Rationale

For arriving at the rating, ICRA has considered the consolidated business and financial risk profiles of Rainbow Children's Medicare Private Limited (RCMPL) and its subsidiaries, which is collectively referred as the Rainbow Group.

The rating upgrade takes into consideration the Rainbow Group's strong operational and financial performance over the years, which is expected to be sustained over the medium term. Its operating income (OI) witnessed a CAGR of 34% between FY2015 and FY2020 on the back of increase in bed capacity to 1,105 by FY2020 from 330 in FY2015, coupled with improved average revenue per occupied bed (ARPOB). The Group had undertaken ~Rs. 300.00-crore capex during the last three years, mainly towards addition of hospitals in Hyderabad, Chennai and Delhi. All these new hospitals had achieved breakeven with the Chennai hospital achieving its breakeven in Q2 FY2021. The OI and margins are likely to decline marginally in FY2021 owing to the impact of the Covid-19 pandemic. However, the Group is expected to report healthy revenue growth and increased margins from FY2022 onwards with improving occupancy at the existing hospitals, along with addition of three new hospitals. Moreover, the liquidity position remains strong with unencumbered cash and liquid investments of Rs. 112.62 crore as on September 30, 2020.

The rating factors in the established track record of the Rainbow Group in paediatrics and obstetrics healthcare segment through its network of fourteen hospitals in Hyderabad, Vijayawada, Bangalore, Delhi and Chennai. The rating factors in its healthy capital structure and coverage indicators with adjusted interest coverage of 18.6 times and adjusted total Debt/OPBDITA of 0.35 times in FY2020 owing to its low debt levels. ICRA notes the favourable demand outlook for the healthcare services in the country, due to factors such as better affordability through increasing per capita income and widening medical insurance coverage, growing awareness for healthcare and under-penetration of healthcare services.

The Group has moderate capex plans of adding 300 beds in Hyderabad, Bangalore and Vishakhapatnam at an estimated cost of Rs. 120 crore, of which Rs. 50 crore was incurred till FY2020. It expects to incur the pending cost of Rs. 70 crore in FY2021, primarily funded by internal accruals and existing cash balances. Further, the Group has deferred the other capex plans at present due to the pandemic, which is likely to improve its free cash flows over the medium term. The rating is constrained by the high regional concentration of revenues and profits with Hyderabad accounting for 61% of the total revenues and most of its operating profits in FY2020. However, with expected improvement in Bangalore, Chennai and Delhi hospitals, the dependence on Hyderabad will reduce over the medium term. Further, it faces stiff competition from established hospitals in Bangalore, Delhi and Chennai, wherein it has limited brand recognition. Moreover, retention of the doctors remains a key challenge for the company, considering the competition in the healthcare industry. ICRA also notes the exposure of hospitals to regulatory risks in terms of any restrictive pricing regulations instated by the Central and state governments.

The Stable outlook on [ICRA]AA- rating reflects ICRA's opinion that the Rainbow Group would benefit from its established track record in the paediatrics and obstetrics healthcare segment, maintain stable occupancy levels and healthy average revenue per occupied bed (ARPOB) levels. Further, the capital structure and coverage indicators are expected to be comfortable with moderate capex plans.

Key rating drivers and their description

Credit strengths

Established operational track record of over two decades – The Rainbow Group started the first hospital in 1999 at Banjara Hills, Hyderabad. Over the years, it has expanded operations to seven paediatric hospitals in Hyderabad, two in Vijayawada, two in Bangalore, two in Delhi and one in Chennai with a total bed strength of 1,299 (and operational beds of 1,105) as on September 30, 2020. Out of the fourteen hospitals, two are out-patient clinics, eight hospitals are operational for more than three years and remaining four hospitals are less than three years old. RCMPL operates its hospitals under the name Rainbow Children's Hospital & Birthright by Rainbow. The maternity centre acquired in Delhi is operated under the name Rosewalk.

Comfortable financial risk profile and liquidity position: The adjusted gearing (for lease liability) of RCMPL is low at 0.13 times as on March 31, 2020 (actual gearing is 1.19 times as on March 31,2020 owing to lease liability of Rs.432.55 crore as on March 31,2020 due to application of IND AS 116 on leases). The adjusted interest coverage is healthy at 18 times and adjusted Debt/OPBDIT at 0.35 times for FY2020 (actual interest coverage and Debt/OPBDIT is 4.2 and 2.4 times respectively due to IND AS 116). The liquidity profile is strong with cash and liquid investments of Rs 112.62 crore as on September 30,2020 owing to healthy accruals despite capex incurred during the period and low working capital intensity of the hospital business.

Favourable demand outlook for healthcare services – The demand outlook for the healthcare services is favourable due to factors such as better affordability through increasing per capita income, widening medical insurance coverage, growing awareness for healthcare, under-penetration of healthcare services and technological improvements in early diagnosis and treatment.

Credit challenges

High concentration of revenues and operating profits – The Hyderabad hospitals together contributed to 61% and 59% of its total revenues in FY2020 and H1 FY2021, which declined from ~82% in FY2016. Going forward, with ramp-up of operations in other cities, the dependence on Hyderabad will reduce over the medium term. Although most of its operating profits are derived from the Hyderabad hospitals, the expected improvement in margins from Bangalore and Delhi hospitals and breakeven of operations at Chennai will reduce the concentration of profits on Hyderabad in the medium term. The average period for a new hospital to breakeven for the Group is generally ranges 18-36 months.

Moderate capex plans – The Group is planning to add 300 beds during the next six months at an estimated cost of Rs. 120 crore. The pending cost of Rs. 70 crore in FY2021 is expected to be funded by its existing cash balances and internal accruals. The company is setting up a new 150-bed hospital in Vishakhapatnam, shifting operations of the existing 70-bed hospital in Vikrampuri, Hyderabad to a new 100-bed hospital and a new hospital with 50 beds in Hebbal, Bangalore. Further, the Group has deferred the other capex plans at present due to the pandemic, which is likely to improve its free cash flows.

Significant competition – The Rainbow Group remains dependent on the paediatrics and obstetrics specialties for its revenues and faces stiff competition from established hospitals in Chennai, Delhi and Bangalore, wherein it is a recent entrant and has limited brand recognition. The retention of the doctors remains a key challenge for the company, given the competition in the healthcare industry. However, the attrition of key consultants has been low for the Group since its inception.

Liquidity position: Strong

RCMPL's liquidity position is **strong** with expected cash flow from operations of nearly Rs. 100 crore for FY2021, cash and liquid investments of Rs. 112.62 crore and undrawn working capital limits of Rs. 19 crore as on September 30, 2020. In relation to these sources of cash, it has capex commitment of Rs. 70 crore for FY2021 with repayment obligations of Rs. 5.0 crore in FY2021. Overall, ICRA expects that RCMPL would be able to meet its near-term commitments through internal sources of cash and generate sufficient cash surpluses.

Rating sensitivities

Positive triggers – A further upgrade in the near term looks unlikely. However, ICRA may upgrade RCMPL's rating if there is a significant diversification of revenue profile while increasing scale of operations and sustaining the operating margins.

Negative triggers – The rating may witness a downward pressure if there is a large debt-funded capex or if there is a material decline in operational performance resulting in adjusted RoCE (to lease liability on account of IND AS 116) below 15% on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Hospitals
Parent/Group Support	Not Applicable
Consolidation / Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of Rainbow Children's Medicare Private Limited. As on March 31, 2020, the company had four subsidiaries that are enlisted in Annexure-2.

About the company

Rainbow Children's Medicare Private Limited (RCMPL) operates a chain of paediatric hospitals with pre-natal centres founded by Dr. Ramesh Kancharla in 1999 at Hyderabad, Telangana with main focus towards child and women health care. The Rainbow Group has seven hospitals in Hyderabad, two hospitals in Bangalore, two in Vijayawada, two in Delhi and one in Chennai. RCMPL operates its hospitals under the name Rainbow Children's Hospital & Birthright by Rainbow. RCMPL has two operational subsidiaries 1) Rainbow Speciality Hospitals Private Limited (RSHPL) and 2) Rosewalk Healthcare Private Limited (RWHPL). RSHPL operates a paediatric cardiac hospital in Hyderabad, whereas RWHPL operates a boutique maternity hospital under the name *Rosewalk* in Delhi. The Group has a total capacity of 1,299 beds, of which 1,105 beds are operational as on September 30, 2020. As on September 30, 2020 on a fully diluted basis, the promoter and promoter group holds 57.6% stake and CDC group[1] holds 31.7% and the remaining 10.7% stake is held by minority shareholders.

[1] CDC is UK's Development Finance Institution (DFI) wholly owned by the UK Government. It generally invests patient capital and acts as a long term investor

Key financial indicators

	FY2018	FY2019	FY2020*
Operating Income (Rs. crore)	401.8	542.8	719.4
PAT (Rs. crore)	36.3	57.9	55.3
OPBDIT/ OI (%)	17.27%	20.61%	27.90%
PAT/OI(%)	9.03%	10.67%	7.69%
Total Outside Liabilities/ Tangible Net Worth (times)	0.2	0.3	1.5
Total Debt/ OPBDIT (times)	0.2	0.5	2.4
Interest Coverage (times)	16.3	19.7	4.2

*Source: Annual reports and ICRA research; * RCMPL has adopted Ind AS 116 for leases which created lease liability and impacted the leverage and coverage metrics in FY2020; However, the adjusted numbers remain healthy.*

Status of non-cooperation with previous CRA: Not Applicable

Any other information: None

Rating history for last three years

	Instrument	Current Rating (FY2021)				Chronology of Rating History for the past 3 years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2020	Date & Rating in FY2019	Date & Rating in FY2018	
					23-Oct-20	11-Dec-19	29-Nov-18	16-Oct-17	20-Jun-17
1	Non-Convertible Debentures	Long Term	50.00	45.00	[ICRA]AA-(Stable)	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	
2	Bank Loan Ratings-Unallocated Limits	Short Term/Long Term	50.00	NA	NA	NA	NA		[ICRA]A+ (Stable)/ [ICRA]A2+ withdrawn

Amount in Rs. crore

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
INE961O07021	Non-Convertible Debentures	Aug-16	9.50%	Aug-24	50.00	[ICRA]AA-(Stable)

Source: Rainbow Children's Medicare Private Limited

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Rainbow Children's Hospital Private Limited	99.99%	Full Consolidation
Rainbow Women & Children's Hospitals Private Limited	99.99%	Full Consolidation
Rosewalk Healthcare Private Limited	99.99%	Full Consolidation
Rainbow Speciality Hospitals Private Limited	76.11%	Full Consolidation

Source: Rainbow Children's Medicare Private Limited

Corrigendum

Document dated October 23, 2020 has been corrected with revisions as detailed below:

- In the 'About the Company' section on page 3, the latest shareholding pattern was added.

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