

Medicare Group (MCGS)

Recommendation	MARKET PERFORM	Risk Rating	R-3
Share Price	QR5.494	Target Price	QR6.072
Implied Upside	10.5%	Old Target Price	QR7.144

3Q2023 Miss As Revenue Disappoints and Margins Shrink; Reducing Price Target

- Medicare Group (MCGS) 3Q2023 net profit fell 31.8%/19.9% YoY/QoQ to QR14.0mn, and missed our estimate of QR20.5mn.** We attribute about 91% of the miss to lower-than-expected revenue and the other 9% to lower-than-modeled margins due to both higher cost of sales and operating costs.
- MCGS's 3Q2023 revenue declined 4.2%/8.1% YoY/QoQ to QR109.3mn, below our expectations of QR113.6mn.** While we adjudge the miss at the top-line of 3.8% to be within a reasonable forecast deviation range, it had an outsized impact on the bottom-line miss. We reckon Qatar's average population (per PSA data) during 3Q2023 actually increased by 1.7% YoY, and it is possible that increased bed supply by competitors toward the end of last year is beginning to take a toll.
- The GP margin came in lower at 36.3% compared with the 39.5% we had expected, and lower both sequentially (37.7%) and compared with 2Q2022, which printed at 39.6%.** While the biggest cost of sales elements, staff costs and medical & surgical costs, came largely in-line, community doctor expenses were significantly above forecast. Other operating costs came in 4.7% above our estimates.
- We again expect to trim our FY2023 estimates of net profit by between 5-8%, and we lower our price target to reflect 3Q2023 performance.** Assuming an 8% cut to 2023 EPS, the stock is trading at a 2023 P/E of ~21.2x and DY of ~4.3%, which is attractive relative to its historical five-year median of 25.9x and 3.8%, respectively. It is also attractive relative to its regional peers trading at a median 2023 P/E of 25.9. However, cross asset yields are much more appealing and this could keep the stock under pressure.
- We reiterate our Market Perform rating. We also note that MCGS could get a boost once there is more clarity on when it will receive a cash windfall following the Court of Appeal judgement in its favor against the National Health Insurance Company (Seha) on 24 January.** MCGS was awarded a total of QR130.7mn. It had written down QR76.2mn of the original QR114.1mn Seha receivable but the court ruling implies that MCGS will receive an additional QR16.6mn of damages/comprehensive compensation. We estimate a net positive impact of QR0.33/share but this is not in our base model. Recent newsflow where the Court of Cassation referred back the case to the Court of Appeal – following Seha's challenge of the January 24 Court of Appeal judgement – means the process will be drawn out and less certainty is now built in the quantum and timing of the payment. We estimate a net impact of QR0.13/share should MCGS decide to completely write-off the Seha receivable.
- We see several tailwinds and headwinds canceling out each other to render a relatively neutral prognosis on MCGS's near-term outlook.** In the short- to medium-term, we see the following variables driving the outlook: muted bed growth due to suspended bed-expansion plans, superior service level & product quality, favorable public health policy, increased healthcare spend, low beta, tariff controls, and increasing competition. In the medium- to longer-term, things are looking up with some of the following factors expected to become more dominant in shaping prospects: an above-average population growth, disease burden and expected change in the composition of expats (to a more white-collar workforce).

Catalysts

- Catalysts: (1) Phased rollout of the "new" Seha/health insurance policy (2) Initiative by the QIA to increase market liquidity (3) Increase in FOL to 100% from 49% (4) Inpatient beds expansion plans, though drawn-out than initially planned (5) Contingent receivable cash windfall from Medicare's court case (vs. the government on "old" Seha).**

Recommendation, Valuation and Risks

- Recommendation and Valuation: We maintain our Market Perform rating and lower our weighted 12-month TP from QR7.144 to QR6.072, which implies a 10.5% upside potential. Our TP is a weighted average of various valuation models: DCF, EBITDA Exit Multiple and Relative-Valuation methodologies.** Several macro and micro themes cancel out each other to render a relatively neutral prognosis on MCGS's near-term outlook. In the short- to medium-term, we see the following variables driving the outlook: bed capacity & occupancy levels, service level & product quality, public health policy, increased healthcare spend, low beta, tariff controls and competition from both the private and public players. In the medium- to longer-term, above-average population growth, disease burden and expected change in the composition of expats (to a more white-collar workforce), will become more dominant in shaping prospects.
- Key risks: (1) Further delays to planned bed-expansion plans (2) Further write-downs/offsets of the Seha receivable (3) Escalating competitive pressure as both private and public bed-count increases (4) Low stock liquidity (5) Rising global/local yields (6) Global disease outbreak.**

Key Financial Data and Estimates

Medicare Group	2022A	2023E	2024E	2025E	2026E
EPS (QR)	0.28	0.28	0.33	0.37	0.41
DPS (QR)	0.26	0.25	0.29	0.33	0.37
P/E (x)	24.5	24.4	21.1	18.6	17.0
EV/EBITDA (x)	19.8	19.3	17.0	15.4	14.0
DY (%)	3.8%	3.7%	4.3%	4.8%	5.3%

Source: Company data, QNB FS Research; Note: All data based on current number of shares; These estimates may not reflect the most recent quarter

Key Data

Current Market Price	QR5.494
Dividend Yield (%)	4.8
P/E Ratio	21.0
Bloomberg Ticker	MCGS QD
ADR/GDR Ticker	N/A
Reuters Ticker	MCGS.QA
ISIN	QA0006929754
Sector*	Healthcare
52wk Share Price High	QR7.600
52wk Share Price Low	QR5.151
3-m Average Vol. (mn)	0.2
Mkt. Cap. (\$ bn/QR bn)	0.4/1.5
EV (\$ bn/QR bn)	0.5/1.7
Shares O/S (mn)	281.4
FO Limit* (%)	100.0
FO (Institutional)* (%)	18.1
1-Year Total Return (%)	-16.6
Fiscal Year-End	December 31

Source: Bloomberg (as of October 23, 2023); *Qatar Exchange (as of October 23, 2023); Note: FO is foreign ownership

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Condensed Financial Statements & Forecasts
Income Statement (QR)

MCGS INCOME STATEMENT	2022A	2023E	2024E	2025E	2026E
REVENUE	487,165,561	504,900,286	518,832,833	543,692,419	569,372,264
GROSS PROFIT	185,409,085	192,731,318	203,565,728	217,213,637	231,474,251
EBITDA	102,150,287	105,464,920	116,851,483	126,698,925	137,092,300
OPERATING PROFIT	73,704,284	77,060,354	88,754,344	98,752,355	109,151,910
PROFIT FOR THE PERIOD	79,164,805	79,463,949	92,157,234	104,157,085	114,287,492

Source: Company data, QNB FS Research; Note: All data based on current number of shares; These estimates may not reflect the most recent quarter

Balance Sheet (QR)

MCGS BALANCE SHEET	2022A	2023E	2024E	2025E	2026E
Property, Plant and Equipment	1,032,712,543	1,047,435,968	1,029,615,840	1,012,313,259	995,395,943
Right-of-Use Assets	37,592,055	34,974,044	32,356,033	29,738,022	27,120,011
Financial Investments at FVTOCI	69,730,395	69,730,395	69,730,395	69,730,395	69,730,395
Investment Properties	26,233,810	26,233,810	26,233,810	26,233,810	26,233,810
Total Non-Current Assets	1,166,268,803	1,178,374,217	1,157,936,078	1,138,015,486	1,118,480,159
Inventories	30,586,104	32,625,153	33,525,433	35,131,785	36,791,140
Accounts Receivable and Prepayments	118,063,533	120,635,440	122,655,951	126,261,111	129,985,227
Cash and Bank Balances	42,150,235	6,943,263	24,433,858	44,832,212	68,598,012
Total Current Assets	190,799,872	160,203,856	180,615,242	206,225,108	235,374,379
Total Assets	1,357,068,675	1,338,578,072	1,338,551,320	1,344,240,595	1,353,854,538
EQUITY AND LIABILITIES					
Share Capital	281,441,000	281,441,000	281,441,000	281,441,000	281,441,000
Legal Reserve	116,010,669	123,957,063	133,172,787	143,588,495	155,017,244
Fair Value Reserve	18,365,451	18,365,451	18,365,451	18,365,451	18,365,451
Revaluations Surplus	549,025,726	549,025,726	549,025,726	549,025,726	549,025,726
Retained Earnings	75,356,136	68,617,165	77,737,191	85,933,129	92,193,308
Total Equity	1,040,198,982	1,041,406,405	1,059,742,154	1,078,353,801	1,096,042,730
Interest Bearing Loans	54,396,528	37,575,275	23,642,683	11,206,931	2,001,087
Lease Liabilities	40,692,837	39,407,796	38,163,336	36,958,175	35,791,071
Employees' End of Service Benefits	77,292,252	79,107,657	80,923,062	82,792,710	84,730,850
Total Non-Current Liabilities	172,381,617	156,090,729	142,729,081	130,957,816	122,523,009
Accounts Payables & Accruals	118,503,116	122,592,217	123,808,890	128,211,840	132,696,298
Interest Bearing Loans	24,043,006	16,608,093	10,449,953	4,953,410	884,471
Lease Liabilities	1,941,954	1,880,629	1,821,241	1,763,727	1,708,031
Total Current Liabilities	144,488,076	141,080,939	136,080,084	134,928,977	135,288,800
Total Liabilities	316,869,693	297,171,667	278,809,165	265,886,793	257,811,809
Total Equity and Liabilities	1,357,068,675	1,338,578,072	1,338,551,320	1,344,240,595	1,353,854,538

Source: Company data, QNB FS Research; Note: All data based on current number of shares; These estimates may not reflect the most recent quarter

Cash Flow Statement (QR)

MCGS CASH FLOW STATEMENT	2022A	2023E	2024E	2025E	2026E
Cash Flow from Operating Activities	102,928,555	88,117,472	117,348,986	128,598,137	139,442,775
Cash Flow from Investing Activities	(59,721,426)	(37,618,379)	(5,014,561)	(4,192,608)	(5,626,395)
Cash Flow from Financing Activities	(53,303,967)	(95,802,903)	(94,843,830)	(104,007,175)	(110,050,580)
Change in Cash	(10,096,838)	(45,303,810)	17,490,595	20,398,354	23,765,800
Opening Cash	52,247,073	52,247,073	6,943,263	24,433,858	44,832,212
Cash End of Period	42,150,235	6,943,263	24,433,858	44,832,212	68,598,012

Source: Company data, QNB FS Research; Note: All data based on current number of shares; These estimates may not reflect the most recent quarter

Key Ratios

MCGS RATIOS	2022A	2023E	2024E	2025E	2026E
GROWTH METRICS					
Revenue	0.7%	3.6%	2.8%	4.8%	4.7%
Gross Profit	0.4%	3.9%	5.6%	6.7%	6.6%
EBITDA	-2.0%	3.2%	10.8%	8.4%	8.2%
Operating Profit	-3.2%	4.6%	15.2%	11.3%	10.5%
Net Profit	0.1%	0.4%	16.0%	13.0%	9.7%
OPERATING RATIOS					
Gross Margin	38.1%	38.2%	39.2%	40.0%	40.7%
EBITDA Margin	21.0%	20.9%	22.5%	23.3%	24.1%
EBIT Margin	15.1%	15.3%	17.1%	18.2%	19.2%
Net Profit Margin	16.3%	15.7%	17.8%	19.2%	20.1%
RETURN RATIOS					
RoE	7.6%	7.6%	8.7%	9.7%	10.4%
RoIC	6.6%	6.8%	8.0%	9.1%	10.2%
RoA	5.4%	5.8%	6.6%	7.3%	8.1%
VALUATION RATIOS					
EV/Sales	4.1	4.0	3.8	3.6	3.4
EV/EBITDA	19.8	19.3	17.0	15.4	14.0
EV/EBIT	27.4	26.3	22.4	19.8	17.5
PE Ratio	24.5	24.4	21.1	18.6	17.0
PEG Ratio	2.6	1.9	1.5	1.6	1.6
P/CF	18.9	22.0	16.5	15.1	13.9
P/B	1.9	1.9	1.8	1.8	1.8
Dividend Yield	3.8%	3.7%	4.3%	4.8%	5.3%
FCF Yield	3.0%	2.5%	5.6%	6.2%	6.7%
LEVERAGE RATIOS					
Debt/Equity Ratio	11.6%	9.2%	7.0%	5.1%	3.7%
Net Debt/Equity Ratio	7.6%	8.5%	4.7%	0.9%	-2.6%
Net Debt/Capital Ratio	7.9%	8.6%	4.8%	1.0%	-2.7%
Net Debt/EBITDA	77.3%	83.9%	42.5%	7.9%	-20.6%
Interest coverage	35.8	17.0	24.5	35.4	51.5
LIQUIDITY RATIOS					
Current Ratio	1.3	1.1	1.3	1.5	1.7
Quick Ratio	1.1	0.9	1.1	1.3	1.5
WORKING CAPITAL DAYS					
Inventory Days	88	88	89	90	91
Average Collection Period	110	110	110	110	110
Payables Days	143	143	143	143	143

Source: Company data, QNB FS Research

Recommendations		Risk Ratings	
<i>Based on the range for the upside / downside offered by the 12-month target price of a stock versus the current market price</i>		<i>Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals</i>	
OUTPERFORM	Greater than +20%	R-1	Significantly lower than average
ACCUMULATE	Between +10% to +20%	R-2	Lower than average
MARKET PERFORM	Between -10% to +10%	R-3	Medium / In-line with the average
REDUCE	Between -10% to -20%	R-4	Above average
UNDERPERFORM	Lower than -20%	R-5	Significantly above average

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