

## Medicare Group (MCGS)

Recommendation	MARKET PERFORM	Risk Rating	R-3
Share Price	QR6.900	Target Price	QR7.144
Implied Upside	3.5%	Old Target Price	QR7.191

### Trimming Estimates & Price Target But Defensive Attributes Support Our Market Perform Rating

We have marginally trimmed our top-line growth estimates for Medicare after a below-forecast FY2022 even as 1Q2023 revenue came marginally above estimates. We maintain our Market Perform rating as the slight downgrade in growth expectations were marginally offset by the improving cost of capital outlook. Moreover, changes in peer multiples had a net marginal positive effect. Also, we trimmed our margins, after they came under pressure during 1Q2023 primarily due to imported inflation in medications and surgical costs. Management contends that these cost pressures will normalize in the near future, however. We note the stock price has had huge swings since our [initiation](#) note in November, in line with general market gyrations, but has recovered nicely in the last couple weeks and is now trading within our estimated fair value range. Our overall thesis remains: Prevailing tailwinds and headwinds combine for a balanced/neutral outlook in the short- to medium-term for Medicare. In the medium- to longer-term, it is likely that tailwinds, primarily due to positive demographics, become dominant. While Medicare has proven to be an attractive dividend play over the years, this yield allure is being weighed down by improving cross asset yields. Nonetheless, MCGS is a cash-cow, with a high cash conversion ratio. The board and management have been generous, with most of the bottom-line paid to shareholders as dividends. The stock boasts a LTM dividend yield of 3.8% (QSE: 4.7%) on the back of an 93% payout ratio. We also like its lower risk profile owing to its product offering and strong balance sheet, which in turn, supports a continued stable dividend flow. However, the forecast period looks rather pedestrian due to competition dynamics and limited fruition of previously-announced expansion plans.

### Highlights

- Medicare Group's 1Q2023 net profit rose 9.4% to QR18.8mn YoY but declined 18.7% QoQ, missing our estimate of QR22.3mn by 16.0%. A jump in cost of sales by 11.5% YoY (6.8% sequentially) to QR82.8mn, primarily driven by an unanticipated 18.3% YoY (18.4% QoQ) spike in medications and surgical costs, saw its GP margin shrinking to 35.3% from 36.7% in 1Q2022 (4Q2022: 39.2%); gross margin came in lower than our modeled estimate. This was due to inflationary pressures that have been pervasive globally – management reckons that this will normalize soon. MCGS had averaged a GP margin of 38.0% for the past eight quarters.
- MCGS's revenue rose 9.1% YoY and 0.5% QoQ to QR128.1mn, largely in line with our expectations of QR126.3mn. While 1Q is traditionally weaker than the preceding 4Q, the sequential 0.5% marginal increase in revenue registered in 1Q2023 was due to demand – primarily elective procedures as per management's guidance – that was pushed out from 4Q2022 during the World Cup into 1Q2023. All else being equal, we do not see this repeating in future.
- We have revised down marginally our revenue projection for FY2023 to QR505.0mn from QR511.1mn. Similarly, our net profit forecast is now lower at QR79.5mn from QR96.7mn, weighed down further by increased cost pressures as we trim our gross margin expectations to 38.2% from 40.1%.
- We reiterate our Market Perform rating. Meanwhile, 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.

### 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 update our weighted 12-month TP to QR7.144 from QR7.191, which implies a 3.5% 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/off 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

### Key Data

Current Market Price	QR6.900
Dividend Yield (%)	3.8
P/E Ratio	24.5
Bloomberg Ticker	MCGS QD
ADR/GDR Ticker	N/A
Reuters Ticker	MCGS.QA
ISIN	QA0006929754
Sector*	Healthcare
52wk Share Price High	QR7.695
52wk Share Price Low	QR5.505
3-m Average Vol. (mn)	0.2
Mkt. Cap. (\$ bn/QR bn)	0.5/1.9
Shares O/S (mn)	281.4
FO Limit* (%)	100.0
FO (Institutional)* (%)	20.2
1-Year Total Return (%)	5.81
Fiscal Year-End	December 31

Source: Bloomberg (as of May 24, 2023),\*Qatar Exchange (as of May 24, 2023); Note: FO is foreign ownership

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**Valuation Summary**
**Weighted Valuation**

Methodology	Weight in Valuation	Upside/Downside Potential
DCF	35.0%	-16.2%
EEM	30.0%	22.9%
Dividend Discount Model	5.0%	-41.0%
Relative Valuation	30.0%	
International Sector Peers	20.0%	
P/E, FY2023e	5.0%	13.4%
P/FCF, FY2022	5.0%	-32.6%
P/BV, FY2022	5.0%	94.4%
LTM Div. Yield	5.0%	86.6%
Local Comparisons	10.0%	
DSM Index P/E @ 12.1x, FY2023e	5.0%	-51.6%
DSM Index LTM Div. Yield @ 4.7%	5.0%	-23.1%
<b>Weighted Average Upside Potential</b>		<b>3.5%</b>

Source: QNB FS Research

**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
<b>PROFIT FOR THE PERIOD</b>	<b>79,164,805</b>	<b>79,463,949</b>	<b>92,157,234</b>	<b>104,157,085</b>	<b>114,287,492</b>

Source: Company data, QNB FS Research

**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
<b>Total Non-Current Assets</b>	<b>1,166,268,803</b>	<b>1,178,374,217</b>	<b>1,157,936,078</b>	<b>1,138,015,486</b>	<b>1,118,480,159</b>
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
<b>Total Current Assets</b>	<b>190,799,872</b>	<b>160,203,856</b>	<b>180,615,242</b>	<b>206,225,108</b>	<b>235,374,379</b>
<b>Total Assets</b>	<b>1,357,068,675</b>	<b>1,338,578,072</b>	<b>1,338,551,320</b>	<b>1,344,240,595</b>	<b>1,353,854,538</b>
<b>EQUITY AND LIABILITIES</b>					
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
<b>Total Equity</b>	<b>1,040,198,982</b>	<b>1,041,406,405</b>	<b>1,059,742,154</b>	<b>1,078,353,801</b>	<b>1,096,042,730</b>
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
<b>Total Non-Current Liabilities</b>	<b>172,381,617</b>	<b>156,090,729</b>	<b>142,729,081</b>	<b>130,957,816</b>	<b>122,523,009</b>
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
<b>Total Current Liabilities</b>	<b>144,488,076</b>	<b>141,080,939</b>	<b>136,080,084</b>	<b>134,928,977</b>	<b>135,288,800</b>
<b>Total Liabilities</b>	<b>316,869,693</b>	<b>297,171,667</b>	<b>278,809,165</b>	<b>265,886,793</b>	<b>257,811,809</b>
<b>Total Equity and Liabilities</b>	<b>1,357,068,675</b>	<b>1,338,578,072</b>	<b>1,338,551,320</b>	<b>1,344,240,595</b>	<b>1,353,854,538</b>

Source: Company data, QNB FS Research

**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

**Key Ratios**

MCGS RATIOS	2022A	2023E	2024E	2025E	2026E
<b>GROWTH METRICS</b>					
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%
<b>OPERATING RATIOS</b>					
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%
<b>RETURN RATIOS</b>					
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%
<b>VALUATION RATIOS</b>					
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%
<b>LEVERAGE RATIOS</b>					
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
<b>LIQUIDITY RATIOS</b>					
Current Ratio	1.3	1.1	1.3	1.5	1.7
Quick Ratio	1.1	0.9	1.1	1.3	1.5
<b>WORKING CAPITAL DAYS</b>					
Inventory Days	157	157	157	157	157
Average Collection Period	110	110	110	110	110
Payables Days	143	143	143	143	143

Source: Company data, QNB FS Research

**Price Multiple Valuation Analysis**

	Country	Market Cap US\$'mn	P/E Earnings	P/FCF Cashflow	P/BV Book Value	D/P DY (%)	EV/EBITDA EBITDA
AADC AB Equity	Saudi Arabia	504.2	N/A	N/A	2.0	N/A	N/A
ALHAMMAD AB Equity	Saudi Arabia	1,835.3	28.2	33.4	4.9	2.4	19.7
DALLAH AB Equity	Saudi Arabia	4,222.3	42.4	55.7	7.7	1.2	29.6
GMPC UH Equity	UAE	334.6	N/A	16.4	1.2	5.6	N/A
LHC SJ Equity	South Africa	2,200.6	15.2	24.5	1.6	1.9	6.9
MIDAN KK Equity	Kuwait	370.7	N/A	14.9	2.5	1.5	N/A
MOUWASAT AB Equity	Saudi Arabia	5,269.1	33.6	41.7	7.3	1.3	21.9
NAHDI AB Equity	Saudi Arabia	6,667.6	23.3	15.6	10.8	3.1	12.8
NTC SJ Equity	South Africa	1,852.2	11.1	30.9	1.9	4.1	7.0
SULAIMAN AB Equity	Saudi Arabia	20,799.5	49.6	79.6	16.2	1.3	39.2
<b>Peer Group Median</b>		<b>2,026.4</b>	<b>28.2</b>	<b>30.9</b>	<b>3.7</b>	<b>1.9</b>	<b>19.7</b>
<b>Peer Group Average</b>		<b>4,405.6</b>	<b>29.1</b>	<b>34.8</b>	<b>5.6</b>	<b>2.5</b>	<b>19.6</b>
<b>MCGS QD Equity</b>	<b>Qatar</b>	<b>510.4</b>	<b>24.4</b>	<b>35.0</b>	<b>1.8</b>	<b>3.8</b>	<b>18.7</b>

Source: Bloomberg, QNBFS Research

[Ends]

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>	
<b>OUTPERFORM</b>	Greater than +20%	<b>R-1</b>	Significantly lower than average
<b>ACCUMULATE</b>	Between +10% to +20%	<b>R-2</b>	Lower than average
<b>MARKET PERFORM</b>	Between -10% to +10%	<b>R-3</b>	Medium / In-line with the average
<b>REDUCE</b>	Between -10% to -20%	<b>R-4</b>	Above average
<b>UNDERPERFORM</b>	Lower than -20%	<b>R-5</b>	Significantly above average



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