Medicare Group (MCGS)

Recommendation	MARKET PERFORM	Risk Rating	R-3
Share Price	QR4.646	Target Price	QR5.524
Implied Upside	18.9%	Old Target Price	QR6.113

4Q2023 Misses Estimate As Staff Costs Bulge Despite In-Line Revenue; Lowering Price Target

- **Medicare Group (MCGS) 4Q2023 net profit fell 33.8% YoY but rose 9.0% to QR15.3mn and missed our estimate of QR25.8mn, even as the top-line came in-line with our expectations.** Bulk of the bottom-line miss was due to an unexpected spike in staff costs. While staff costs are usually the highest in 4Q, they still exceeded our model. **MCGS's 4Q2023 revenue rose 2.0%/18.9% YoY/QoQ to QR130.0mn, in-line with our forecast of QR129.6mn.** FY2023 EPS declined by 17.0% to QR0.23. Consequently, the board proposed a dividend of QR0.22/share for FY2023 down from QR0.2625 in FY2022, and lower than QR0.2476 we had forecasted.
- **The fourth quarter is traditionally MCGS's strongest, both at the top- and bottom-lines, other things being equal**. While 4Q2023 revenue was the highest quarter for 2023 as expected, it was the second-weakest earnings quarter for 2023 primarily due to staff costs-related margin pressure. **Staff costs spiked (+11.1% YoY; +13.2% for direct/line staff) in 4Q2023 likely to retain nurses, a trend that seems to have deepened from 3Q2023.** The higher-than-expected increase in staff costs account for more than 60% of the bottom-line miss. **Therefore, we trim our margins further in the model and revise out TP down as we believe that this likely represents a "new normal"–** we will try to get more color during the conference call later today. Even other costs that jumped, such as IT development (+94.1% YoY), security & cleaning (31.2% YoY) and maintenance & repairs (+25.6% YoY) generally have a significant labor cost component**.**
- **The GP margin came in lower at 33.0% compared with the 38.8% we had expected, and lower both sequentially (36.3%) and compared with 4Q2022 (39.2%).** Further to staff costs that were higher, medical & surgical costs and doctors' charges also printed ahead of our expectations, rising 10.7% and 12.8% YoY, respectively. Other operating costs including depreciation charges were largely in-line with estimates.
- **We cut our TP to QR5.524/share after adjusting margins and maintain our Market Perform rating even though there is an implied upside of 18.9%. The upside emanates primarily from the fact that MCGS now looks inexpensive relative to regional peers but we do not see any catalysts on the horizon to warrant a change in the rating.** We, however, note that MCGS could still 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) early last year.
- **MCGS was awarded a total of QR130.7mn (including additional QR16.6mn in damages/comprehensive compensation) on 24 January 2023 by the Court of Appeal in connection with the Seha receivable**. However, the Court of Cassation has since referred back the case to the Court of Appeal following Seha's challenge of the 24 January 2023 Court of Appeal judgement. This means the process will be drawn out and less certainty is now built in the quantum and timing of the payment. MCGS had written down QR76.3mn of the original QR114.1mn Seha receivable. We estimate a net positive impact of QR0.33/share but this is not in our base model. 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)** Recent addition to the FTSE Russell Micro Cap Index **(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 QR6.113 to QR5.524, which implies a 18.9% 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/offs 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	2023A	2024E	2025E	2026E	2027E
EPS (QR)	0.23	0.24	0.24	0.30	0.31
DPS (QR)	0.22	0.22	0.23	0.28	0.30
P/E (x)	19.9	19.6	19.1	15.7	14.8
EV/EBITDA (x)	16.5	15.8	14.9	13.6	11.9
DY (%)	4.7%	4.8%	4.9%	6.0%	6.3%

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	QR4.646
Dividend Yield (%)	4.7
P/E Ratio	19.9
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	QR4.412
3-m Average Vol. (mn)	0.8
Mkt. Cap. ($ bn/QR bn)	0.4/1.3
EV ($ bn/QR bn)	0.4/1.4
Shares O/S (mn)	281.4
FO Limit* (%)	100.0
FO (Institutional)* (%)	16.9
1-Year Total Return (%)	-20.4
Fiscal Year-End	December 31

Source: Bloomberg (as of February 20, 2024),*Qatar Exchange (as of February 20, 2024); Note: FO is foreign ownership

Phibion Makuwerere, CFA
+974 4476 6589
phibion.makuwerere@qnbfs.com.qa

Saugata Sarkar, CFA, CAIA
+974 4476 6534
saugata.sarkar@qnbfs.com.qa

Recommendations *Based on the range for the upside / downside offered by the 12-month target price of a stock versus the current market price*		Risk Ratings *Reflecting historic and expected price volatility versus the local market average and qualitative risk analysis of fundamentals*	
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

Contacts

QNB Financial Services Co. W.L.L.
Contact Center: (+974) 4476 6666
info@qnbfs.com.qa
Doha, Qatar

Saugata Sarkar, CFA, CAIA
Head of Research
saugata.sarkar@qnbfs.com.qa

Shahan Keushgerian
Senior Research Analyst
shahan.keushgerian@qnbfs.com.qa

Phibion Makuwerere, CFA
Senior Research Analyst
phibion.makuwerere@qnbfs.com.qa