July 2019

Dallah Healthcare Co.

Result Flash Note 2Q-19

Dallah posted a disappointing set of result in Q2-19 with net profit of SAR 15.3mn, significantly below AJC's and the market consensus estimates. The result was mainly affected by higher than expected COGS, finance expenses, and OPEX. Higher COGS was largely due to the increase in startup OPEX for Namar Hospital, which started operations in Q2-18. The rise in OPEX was due to higher depreciation expenses and operating cost related to the hike in operating levels at Namar Hospital. The increase in financing cost due to greater operating leverage for Namar Hospital and larger company investments also adversely impacted the results. Revenue was in line with our estimates. "**Neutral**" recommendation on the stock with a TP at SAR 54.20/share.

- Dallah posted net income of SAR 15.3mn in Q2-19 (EPS of SAR 0.13), missing AJC's and the market consensus estimates of SAR 31.5mn and SAR 32.8mn, respectively. The deviation of Q2-19 net income from our estimates is mainly ascribed to a lower than expected gross margin owing to higher startup operating expenses at Namar Hospital. The rise in operating levels at Namar Hospital led to higher OPEX. Financing costs also increased on account of increased operating leverage for the hospital. Pre-operating costs increased at Dr. Mohammed Alfagih Hospital in which the company holds a stake.
- Dallah's sales in Q2-19 stood at SAR 286.0mn, reflecting an increase of 4.7% Y/Y, in line with our estimate of SAR 286.3mn.
- Gross profit stood at SAR 92.5mn, indicating a rise of 0.1% Y/Y. The GP Margin further declined to 32.3% in Q2-19 from 33.8% in Q2-18 against our estimate of 36.0%. Operations at Namar Hospital, which commenced in Q2-18, continue to have an impact on the margin.
- Operating profit stood at SAR 18.1mn, depicting a decline of 8.1% Y/Y. The company witnessed an increase of 2.3% Y/Y in OPEX (SG&A) to record SAR 74.4mn compared to our estimates of SAR 70.2mn and SAR 72.7mn posted in Q2-18.

AJC view: We believe the operations at Namar Hospital, which commenced in Q2-18, continue to have an adverse impact on the company's profit. We believe it would take a couple of years for margins to increase as full capacity expansion would take effect by FY-21. Increased capacity utilization at Namar Hospital and the new hospital opening at Al-Nakheel would constitute key revenue growth drivers. The company's retail-based model places it in a favorable position over its peer set with respect to receivables. However, Dallah needs to make prudent capital allocation decisions while executing its expansion plans due to a high net debt/EBITDA ratio of 3.5x. We lower EPS for FY19 to SAR 1.51 compared to our previous estimate of SAR 1.91. "**Neutral**" recommendation on Dallah with a TP at **SAR 54.20/share.**

Results Summary

SARmn (unless specified)	Q2-18	Q1-19	Q2-19	Change Y/Y	Change Q/Q	Deviation from AJC Estimates
Revenue	**273.1**	**321.1**	**286.0**	4.7%	-10.9%	-0.1%
Gross Profit	92.4	120.3	92.5	0.1%	-23.1%	-10.3%
Gross Margin	*33.83%*	*37.46%*	*32.34%*	-	-	-
EBIT	19.7	41.2	18.1	-8.1%	-56.1%	-45.0%
Net Profit	18.7	35.2	15.3	-18.2%	-56.5%	-51.4%
EPS	0.16	0.29	0.13	-	-	-

Source: Company Reports, AlJazira Capital *NM: Not meaningful

Neutral

Target Price (SAR)	**54.20**
Upside / (Downside)*	**-2.2%**

Source: Tadawul *prices as of 28rd of July 2019

Key Financials

SARmn (unless specified)	FY17	FY18	FY19E
Revenues	1,212.1	1,180.9	1,226.9
Growth %	4.2%	-2.6%	3.9%
Net Income	295.0	141.8	113.2
Growth %	31.3%	-51.9%	-20.2%
EPS	5.00	1.89	1.51

Source: Company reports, Aljazira Capital

Key Ratios

SARmn (unless specified)	FY17	FY18	FY19E
Gross Margin	46.0%	36.9%	35.0%
Net Margin	24.3%	12.0%	9.2%
P/E	20.2x	23.4x	36.7x
P/B	3.5x	2.0x	3.7x
EV/EBITDA (x)	17.5x	18.2x	24.1x

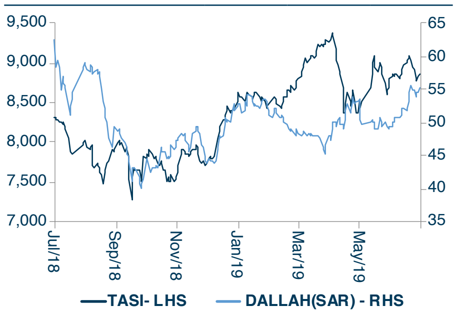
Source: Company reports, Aljazira Capital

Key Market Data

Market Cap (bn)	4.1
YTD %	+17.8%
52 Week High/ Low	59.77/39.40
Shares Outstanding (mn)	75

Source: Company reports, Aljazira Capital

Price Performance



Source: Tadawul, Aljazira Capital

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RATING TERMINOLOGY

1. Overweight: This rating implies that the stock is currently trading at a discount to its 12 months price target. Stocks rated "Overweight" will typically provide an upside potential of over 10% from the current price levels over next twelve months.
2. Underweight: This rating implies that the stock is currently trading at a premium to its 12 months price target. Stocks rated "Underweight" would typically decline by over 10% from the current price levels over next twelve months.
3. Neutral: The rating implies that the stock is trading in the proximate range of its 12 months price target. Stocks rated "Neutral" is expected to stagnate within +/- 10% range from the current price levels over next twelve months.
4. Suspension of rating or rating on hold (SR/RH): This basically implies suspension of a rating pending further analysis of a material change in the fundamentals of the company.

Disclaimer