

Middle East Healthcare Co. (Saudi German) posted net income of SAR 28.5mn (SAR 0.31 EPS), below our and the consensus estimate of SAR 39.2mn and SAR 38.1mn, respectively. The decline in net income was driven by 240bps contraction in the GP Margin and increase in OPEX. The increase in inpatient traffic spurred growth in revenue. We maintain our recommendation of **“Neutral”** on the stock with a TP of **SAR 31.90/share**.

- Saudi German posted net income of SAR 28.5mn in Q4-20 (EPS of SAR 0.31), below AJC's and the market consensus estimate of SAR 39.2mn and SAR 38.1mn, respectively. The deviation of Q4-20 net income from our estimate is mainly ascribed to a lower-than-expected GP Margin. Dammam hospital, which commenced operations in February-2020, incurred losses of SAR 19.4mn during the quarter.
- Saudi German's sales in Q4-20 stood at SAR 470.5mn, up 15.7% Y/Y, in-line our estimate of SAR 492.1mn. We attribute the increase in revenue to higher inpatient traffic. The company hired new caregivers and key management professionals in Q2-19 to boost revenue and operational efficiency, which could be one of the key reasons for the rise in patients.
- Gross profit was recorded at SAR 160.7mn, indicating a rise of 8.2% Y/Y. The GP Margin contracted to 34.2% in Q4-20 from 36.6% in Q4-19 against our estimate of 35.9%. We expect margins to be under pressure in the near term.
- Operating profit stood at SAR 31.1mn, relatively unchanged compared to SAR 31.0mn in Q4-19. As operating expense increased 10.2% Y/Y, the operating margin declined to 27.5% in Q4-20 from 28.9% in Q4-19.

AJC view: Saudi German's overall results were below our expectations. We expect margins to remain under pressure in the near-term due to the commencement of operations at Dammam hospital. We will revisit our FY21 estimates, once the detailed financials are available.

The company's receivables stood at 1,471mn in Q3-20, translating to receivable days of 314. Saudi German's average receivable days increased steadily from 156 days in FY14 to 254 days in FY19. We believe this is a major cause for concern, leading to an unfavorable working capital cycle and adversely impacting liquidity. It is imperative that the company addresses issue to avoid liquidity issues in the long term.

Saudi German Hospitals has witnessed growth in revenue, improvement in margins and net income for the last four quarters, which is a very encouraging sign from a LT perspective. However, most of the positives appear to be priced at current levels.

We value Saudi German on 50% weight for DCF (3.0% terminal growth and 6.0% average WACC), and 25% weight each for relative valuation based on P/E (24.4x FY21 EPS) and EV/EBITDA (16.1x FY21 EBITDA). These yield a TP of SAR 31.9/share, implying a 4.8% downside from the current levels. The stock is currently trading at a P/E of 29.3x based on our FY21 EPS estimate. We maintain our recommendation of **“Neutral”** on Saudi German with a TP of **SAR 31.9/share**.

Results Summary

SARmn	Q4-19	Q3-20	Q4-20	Change Y/Y	Change Q/Q	Deviation from AJC Estimates
Revenue	406.5	492.1	470.5	15.7%	-4.4%	-4.4%
Gross Profit	148.6	171.9	160.7	8.2%	-6.5%	-9.0%
Gross Margin	36.6%	34.9%	34.2%	-	-	-
EBIT	31.0	43.3	31.1	0.4%	-28.1%	-34.7%
Net Profit	37.5	34.9	28.5	-23.9%	-18.3%	-27.2%
EPS	0.41	0.38	0.31	-	-	-

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

Neutral

Target Price (SAR) **31.90**

Upside / (Downside)* **-4.8%**

Source: Tadawul *prices as of 25th of February 2021

Key Financials

(in SAR mn, unless specified)	FY19	FY20	FY21E
Revenue	1,496.6	1,772.2	1,836.1
Growth %	7.6%	18.4%	3.6%
Net Income	97.6	101.0	105.1
Growth %	-43.3%	3.5%	4.1%
EPS	1.06	1.10	1.14

Source: Company reports, Aljazira Capital

Key Ratios

	FY19	FY20	FY21E
Gross Margin	31.6%	33.9%	32.5%
Net Margin	6.5%	5.7%	5.7%
P/E (x)	28.0	31.9	29.3
P/B (x)	1.8	2.0	1.9
EV/EBITDA (x)	18.9	18.6	16.2

Source: Company reports, Aljazira Capital

Key Market Data

Market Cap(bn)	3.1
YTD%	-4.4%
52 week (High)/(Low)	39.2/23.9
Share Outstanding (mn)	92.0

Source: Company reports, Aljazira Capital

Price Performance



Source: Tadawul, Aljazira Capital

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- 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.
- 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.
- 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.

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