# Dallah Healthcare Co.

## Investment Update



## 91% capacity increase in major-stake hospital beds by FY28 drives long term performance; margins under pressure by upcoming two-hospital acquisition

**Dallah is maintaining its momentum into H1-24, where it recorded a bottom line of SAR 231.1mn (up 56.5% Y/Y) and a top line reaching SAR 1,549.2mn (up 11.7%). Its recent performance has been attributed to a mix of improvements- starting with a top line supported by patient volume increases and minor price hikes, as well as margin expansions, operational capacity increases, and also increased income from associates which have already recorded a SAR 20.6mn for the half as compared to a loss of SAR 1.9mn in all of FY23. Going forward, Dallah seeks to finalize a two-hospital acquisition (AlAhsa at 205 beds, and AlSalam at 495 beds, both in the Eastern Region) via a share swap funded by a 3.99% capital increase. While AlSalam is a loss making hospital, as it was recently established, and AlAhsa's estimated revenue generation per bed at less than Dallah's, we expect Dallah to be able to immediately recognize synergies with the two hospitals via its economies of scale on cost controls, improving quality and sourcing medical talent, and potentially negotiating towards corporate contract clients. Furthermore, Dallah is expected to load up nearly SAR 764.0mn in Ayyan's total debt- though we expect Dallah's scale and more favorable credit rating to potentially open opportunities to refinance the debt at better terms. Along with an expansion in the up-and-coming district of AlArid expected in FY28, we estimate an FY23-28E revenue and net income CAGR of 12.7% and 20.4%, respectively; also supported by improvement in its associate companies. We revise our TP up to SAR 172.0 per share, at a "Neutral" recommendation.**

**Increase in patient volume, operational capacity, performance of associate hospitals, and slight price hikes enhancing margins categorized healthy H1-24 results:** Dallah's H1-24 results reached a bottom line of SAR 231.1mn (up 56.5% Y/Y), while also recording a top line for the half reaching SAR 1,549.2mn (up 11.7% Y/Y). The double digit revenue growth came as a result of patients increasing by 1% Y/Y, and likely due to the 50 bed operational addition at Kingdom Hospital taking place towards the end of the period; in addition to favorable case mixes also supporting the period's revenues, price increases on insurance clients across mature and new facilities to match inflation (and higher for newly operated facilities) were also in effect. As a result of the cases mixes and price adjustments, GP margins for H1-24 reached 38.2%, with Q2-24's margins reaching its highest levels since 2018. Furthermore, contributions from its associate hospitals reached SAR 20.6mn in H1-24 as compared to an SAR 8mn loss Y/Y. Notably, Mohammed Al-Faqih hospital (currently 350 beds, and a 31.21% stake) recorded losses for Dallah at SAR 23.0mn in FY23, but decreased its loss contribution to just SAR 1.0mn throughout H1-24. Also, while increasing its stake in Jeddah's International Medical Center during FY23 (now at a 27.18% stake, currently hosting 300 beds), the associate hospital contributed SAR 15.1mn to the bottom line in H1-24 as compared to SAR 6.1mn throughout all of FY23. Dallah's H1-24 bottom line then reaches its highest net income for a first-half to date.

**Upcoming major transaction to acquire AlSalam Hospital and AlAhsa Hospital circumvents development risks and increases beds capacity by c. 63% over FY23 levels:** Dallah seeks to finalize its agreement by end of year to acquire 97.4% of AlAhsa Hospital, and 100% of Al Salaam Hospital from Ayyan Investment Co. via a share swap funded by a 3.99% capital increase, raising Dallah's number of shares to 101.57mn. Both hospitals are in the Eastern Region. AlAhsa hospital established in 1999 in Hofouf, has an estimated building capacity to host 205 beds and is a class B hospital in terms of insurance classifications. Al Salaam hospital, established in 2022 in AlKhobar, has a building capacity of 495 beds and is a class A/VIP hospital. The net equity value for the 100% and 97.41% acquisitions was reached at a total of SAR 660mn; with an acquired net book value of 218.3mn for AlAhsa, and a SAR -131.14mn for AlSalam. We estimate Dallah to load up nearly SAR 764.0mn of the acquirees' debt, though we expect that Dallah's financial profile, scale, and credit rating to be able to mitigate the acquires' finance cost (estimated at an annualized c. 8% as of H1-24) should Dallah decide to refinance. Furthermore, at an estimated current EV for the deal at SAR 1.4bn (excluding lease liabilities), implies a cost of SAR 2.0mn per bed, below the average starting range of nearly SAR 2.5mn per-bed for a greenfield premium hospital project.

**Potentials from AlSalam and AlAhsa acquisition expected to be realized by medium term after a 410bps pressure on margins by FY25E over H1-24 levels:** We estimate both hospitals to generate a lesser total revenue to utilized beds than Dallah's. We do, however, expect Dallah to be able to enhance its acquirees' revenue generation via more specialized services, patient attraction, and possibly contract clients as a part of its initiatives post acquisition. However, with AlAhsa being a class B hospital, we expect more headroom for revenue enhancement from the newly established AlSalam hospital. We estimate a four year FY25-30E revenue CAGR from both hospitals reaching 17.0% on the back improved utilization rates and revenue enhancement post acquisition. AlSalam is currently a loss making hospital, as it is a new hospital; and while ramp ups towards break even could take up to three years for a new hospital, we expect the hospital to reach its breakeven point during FY26E. Competition in that region, however, is a risk on its ramp up time. The hospitals would be able to benefit by Dallah's brand equity, economies of scale on its costs, quality of doctors and sourcing talent, gaining accreditations, as well as its relationship with insurance clients and the ability to negotiate corporate client contracts. We expect the Ayyan acquisitions to pressure Dallah's recently heightened GP margins, to reach 34.1% in FY25 (down c. 410bps from H1-24 levels), as the hospitals ramp up. We forecast, however, for GP margins to recover to 37.0% by FY27E before facing some pressures from the FY28E AlArid expansion. At Dallah's scale and existing operational network, we expect immediate synergies to take place for the OPEX required to run the AlAhsa and AlSalam hospitals; pressuring operating margins by only 180bps, from FY23 levels, during their first full year, before gradually improving after. Going forward, we forecast a five year FY23-28E revenue and net income CAGR of 12.7% and 20.4%, respectively- mainly driven by the consolidation and ramping up of the upcoming acquirees.

| | |
|---|---|
| **Recommendation** | **Neutral** |
| **Target Price (SAR)** | **172.0** |
| **Upside / (Downside)*** | **7.0%** |

Source: Tadawul *prices as of 17th of Sept 2024

### Key Financials

| in SAR mn, (unless specified) | FY22 | FY23 | FY24E | FY25E |
|---|---|---|---|---|
| Revenues | 2,488 | 2,943 | 3,256 | 3,987 |
| Growth % | 18.2% | 18.3% | 10.6% | 22.5% |
| Net Income | 274.5 | 360.1 | 463.1 | 430.4 |
| Growth % | 6.1% | 31.2% | 28.6% | -7.1% |
| EPS | 2.70 | 3.70 | 4.56 | 4.24 |
| DPS | 2.00 | 2.00 | 2.00 | 2.0 |

Source: Company reports, Aljazira Capital Research

### Key Ratios

| | FY22 | FY23 | FY24E | FY25E |
|---|---|---|---|---|
| Gross Margin | 36.0% | 36.7% | 37.9% | 34.1% |
| OP Margin | 17.0% | 17.2% | 18.4% | 15.4% |
| Net Margin | 11.0% | 12.2% | 14.2% | 10.8% |
| EBITDA Margin | 21.6% | 21.5% | 23.3% | 20.6% |
| RoE | 14.2% | 13.9% | 12.6% | 10.2% |
| P/E (x) | 54.8 | 46.4 | 35.3x | 37.9x |
| P/B (x) | 6.7 | 5.2 | 4.0x | 3.8x |
| EV/EBITDA (x) | 31.2 | 30.4 | 24.9x | 23.1x |
| Dividend Yield | 1.4% | 1.2% | 1.2% | 1.2% |

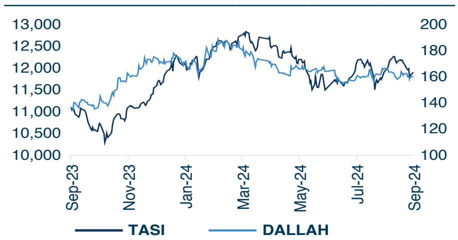
Source: Company reports, Aljazira Capital Research

### Key Market Data

| | |
|---|---|
| Market Cap (SAR bn) | 15.7 |
| YTD% | -6.4% |
| 52 weeks (High)/(Low) | 194.0/131.4 |
| Share Outstanding (mn) | 101.6 |

Source: Company reports, Aljazira Capital Research *Post Acquisition

### Price Performance




Source: Tadawul, Aljazira Capital Research

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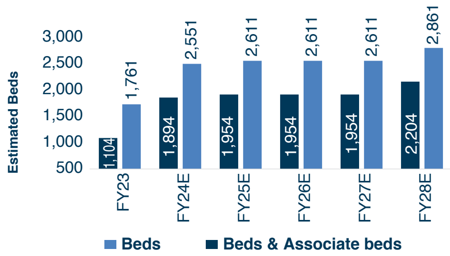
**Total expansions to extend capacity by c. 91% over the current, post the FY28E AlArid expansion, driving long term performance for the stock:** On the immediate term, Dallah is set to gradually extend its Namar inpatient capacity by 100 beds per the need. We expect that utilization at Namar is near 70% or above, potentially warranting rolling out some of the 100 by the end of the year, and stretching onto FY25E. Furthermore, post the Ayyan acquisitions taking place by end of FY24, Dallah is expected to open up a 250 bed hospital in the up-and-coming AlArid district in Riyadh by FY28E. Dallah Clinics are also expected to open two clinics by H2-24E which are currently under refurbishment. We expect the expansion campaign underway to extend Dallah's capacity from the current estimated 1,154 beds to 2,204 beds (91% increase) by FY28E. The bottom line is expected to be supported by Dallah's portfolio of associates, which have already recorded a net contribution of SAR 20.6mn, as compared to a loss of SAR 1.9mn for all of FY23. Its associate, and premium provider, IMC, is also undergoing an expansion in Jeddah to potentially expand Dallah's income from associates, though we await further details on the expansion.

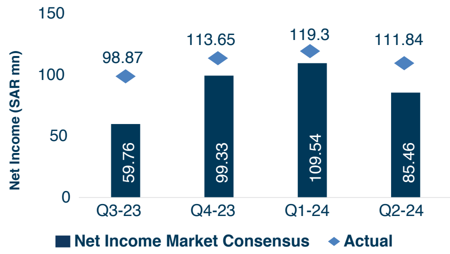
**AJC view and valuation:** Dallah possesses various growth drivers found in its upcoming Ayyan acquisition, AlArid expansion, its performance of its invested associates, as well as a potential expansion under study for its AlNakheel land. While the acquisition will load up Dallah's balance sheet with an estimated SAR 762.3mn in debt (which Ayyan pays an estimated annualized EIR of c. 8% as for H1-24), we expect that Dallah's credit rating and scale is able to mitigate the interest paid on the acquired interest bearing debts should Dallah refinance them. Furthermore, while AlSalam is a loss making hospital, which we forecast that Dallah's initiatives and synergies with the hospital to expedite the ramp up at the hospital. Our estimates on all the developments ongoing at Dallah punctuate at a FY23-28E revenue and net income CAGR of 12.7% and 20.4%, respectively. We do however expect that that intensified competition in the region to be a potential downside risk to the expected ramp up of AlSalam. Further downsides are present from longer than expected delays in expansions, which have happened at Dallah previously. While upsides are found in the success of materializing the AlNakheel land into an expansion, or higher than expected patient volumes or price hikes, as well as a quicker than expected ramp up at AlSalam. We value the stock at 50% DCF (terminal growth rate = 2.5%) and 50% PE (42x over FY25E earnings, based on a three year forward CAGR of 21.0%) to upwardly revise our TP to **SAR 172.0 per share,** at a "**Neutral**" recommendation.

**Fig. 1: Ayyan acquisition, AlArid, and Namar expansions to extend expected capacity by 91% over current**




Source: Company Presentations, AlJazira Capital Research

**Fig. 2: Average positive deviation of 22.4mn (TTM) driven by revenue and margin performance as well as associate income**




Sources: Company Financials, AlJazira Capital Research, Argaam

**Valuation Summary:**

| DCF | FY24E | FY25E | FY26E | FY27E | FY28E | FY29E | FY30E |
|---|---|---|---|---|---|---|---|
| Operating Profit | 598.2 | 613.2 | 808.6 | 951.9 | 1,061.8 | 1,174.8 | 1,287.4 |
| Depreciation & Amortization | 130.4 | 172.5 | 186.0 | 191.6 | 221.3 | 225.1 | 228.4 |
| Working capital chg | -132.8 | -56.4 | -47.5 | -36.4 | -73.5 | -31.6 | -19.5 |
| **CFO** | **595.8** | **729.4** | **947.1** | **1,107.1** | **1,209.6** | **1,368.2** | **1,496.4** |
| Capex | (1,267.3) | (462.4) | (481.8) | (326.9) | (252.4) | (258.3) | (255.6) |
| FCFF | -671.5 | 266.9 | 465.3 | 780.2 | 957.3 | 1,109.9 | 1,240.7 |
| **Present value of FCFF** | **-657.6** | **244.2** | **396.7** | **620.4** | **709.0** | **760.6** | **785.9** |
| Sum of the PV | | | | | | | 2,859.2 |
| PV of terminal value | | | | | | | 16,008.4 |
| **Enterprise Value** | | | | | | | **18,867.5** |
| Cash | | | | | | | 143.0 |
| Debt | | | | | | | 1,782.6 |
| Non-Controlling Interest | | | | | | | 280.0 |
| FV | | | | | | | 16,947.9 |
| **Fair value per share*** | | | | | | | **SAR 166.9** |

Source: Company reports, AlJazira Capital Research *Over post-acquisition number of shares

**Blended Valuation**

| | Fair value | Weights | Weighted average |
|---|---|---|---|
| DCF based value | 166.9 | **50%** | 83.4 |
| Relative Valuation - P/E (42x - FY25E) | 178.0 | **50%** | 89.0 |
| **Weighted average 12-month price target** | | | **172.0** |
| **Expected Capital Gain** | | | **7.0%** |

Source: Company reports, AlJazira Capital Research

## Fig 4. Key Financials

| Amount in SAR mn, unless otherwise specified | FY22 | FY23 | FY24E | FY25E | FY26E | FY27E | FY28E |
|---|---|---|---|---|---|---|---|
| **Income statement** | | | | | | | |
| Revenues | 2,488.0 | 2,942.9 | 3,255.8 | 3,987.3 | 4,399.3 | 4,760.3 | 5,369.2 |
| **Y/Y** | **18.2%** | **18.3%** | **10.6%** | **22.5%** | **10.3%** | **8.2%** | **12.8%** |
| Cost | (1,592.9) | (1,864.2) | (2,021.2) | (2,628.0) | (2,818.0) | (2,999.1) | (3,425.9) |
| **Gross profit** | **895.1** | **1,078.7** | **1,234.5** | **1,359.3** | **1,581.3** | **1,761.3** | **1,943.3** |
| Selling & distribution expense | (45.0) | (59.8) | (66.9) | (77.2) | (88.8) | (97.0) | (111.2) |
| General & administration expense | (429.8) | (517.1) | (569.2) | (664.0) | (677.3) | (703.7) | (761.2) |
| Expected credit loss provision | (27.8) | (30.2) | (32.2) | (36.9) | (41.7) | (46.8) | (52.0) |
| **Operating profit** | **392.5** | **471.6** | **566.3** | **581.3** | **773.4** | **913.8** | **1,018.8** |
| **Y/Y** | **19.7%** | **20.2%** | **20.1%** | **2.7%** | **33.0%** | **18.2%** | **11.5%** |
| Other income | 30.0 | 34.7 | 31.9 | 31.9 | 35.2 | 38.1 | 43.0 |
| Financial charges | (70.5) | (104.1) | (114.0) | (157.4) | (137.1) | (126.3) | (106.2) |
| Other adjustments | (22.8) | (1.9) | 35.9 | 36.6 | 39.5 | 41.2 | 45.7 |
| **Income before zakat** | **329.1** | **400.3** | **520.1** | **492.5** | **710.9** | **866.7** | **1,001.3** |
| Zakat | (33.7) | (14.9) | (21.7) | (24.6) | (35.5) | (37.8) | (50.1) |
| Non-controlling interest | (21.0) | (25.3) | (35.3) | (37.5) | (38.1) | (38.5) | (39.0) |
| **Net income** | **274.5** | **360.1** | **463.1** | **430.4** | **637.3** | **790.4** | **912.2** |
| **Y/Y** | **6.1%** | **31.2%** | **28.6%** | **-7.1%** | **48.1%** | **24.0%** | **15.4%** |
| **EPS** | **2.70** | **3.70** | **4.56** | **4.24** | **6.27** | **7.78** | **8.98** |
| **DPS** | **2.00** | **2.00** | **2.00** | **2.00** | **3.25** | **4.00** | **5.00** |
| **Balance sheet** | | | | | | | |
| **Assets** | | | | | | | |
| Cash & equivalent | 238 | 235 | 72 | 204 | 281 | 151 | 223 |
| Other current assets | 1,066 | 1,110 | 1,291 | 1,492 | 1,599 | 1,686 | 1,871 |
| Property plant & equipment | 2,847 | 3,040 | 4,103 | 4,367 | 4,633 | 4,736 | 4,730 |
| Other non-current assets | 769 | 1,858 | 2,479 | 2,488 | 2,495 | 2,500 | 2,504 |
| **Total assets** | **4,920** | **6,243** | **7,945** | **8,551** | **9,008** | **9,073** | **9,328** |
| **Liabilities & owners' equity** | | | | | | | |
| Total current liabilities | 885 | 1,163 | 1,299 | 1,231 | 1,284 | 1,275 | 1,334 |
| Long-term loans | 1,529 | 1,288 | 1,717 | 2,097 | 2,178 | 1,846 | 1,564 |
| Total other non-current liabilities | 274 | 319 | 501 | 529 | 508 | 491 | 526 |
| Paid -up capital | 900 | 977 | 1,016 | 1,016 | 1,016 | 1,016 | 1,016 |
| Statutory reserves | 155 | 1,121 | 1,742 | 1,742 | 1,742 | 1,742 | 1,742 |
| Fair value adjustment | 14 | (2) | (2) | (2) | (2) | (2) | (2) |
| Retained earnings | 921 | 1,108 | 1,368 | 1,595 | 1,902 | 2,286 | 2,691 |
| Treasury shares | - | - | - | - | - | - | - |
| Non-controlling interest | 242 | 269 | 305 | 342 | 380 | 419 | 458 |
| Total owners' equity | 2,232 | 3,473 | 4,428 | 4,693 | 5,038 | 5,461 | 5,904 |
| **Total equity & liabilities** | **4,920** | **6,243** | **7,945** | **8,551** | **9,008** | **9,073** | **9,328** |
| **Cashflow statement** | | | | | | | |
| Operating activities | 442 | 626 | 600 | 649 | 899 | 1,067 | 1,215 |
| Investing activities | (226) | (294) | (1,845) | (478) | (498) | (343) | (269) |
| Financing activities | (186) | (335) | 1,081 | (39) | (324) | (855) | (874) |
| Change in cash | 30 | (3) | (163) | 132 | 78 | (131) | 72 |
| **Ending cash balance** | **238** | **235** | **72** | **204** | **281** | **151** | **223** |
| **Key fundamental ratios** | | | | | | | |
| **Liquidity ratios** | | | | | | | |
| Current ratio (x) | 1.3 | 1.5 | 1.2 | 1.0 | 1.4 | 1.5 | 1.4 |
| Quick ratio (x) | 1.2 | 1.0 | 0.8 | 1.1 | 1.2 | 1.2 | 1.3 |
| **Profitability ratios** | | | | | | | |
| Gross profit margin | 36.0% | 36.7% | 37.9% | 34.1% | 35.9% | 37.0% | 36.2% |
| Operating margin | 15.8% | 16.0% | 17.4% | 14.6% | 17.6% | 19.2% | 19.0% |
| EBITDA margin | 21.6% | 21.5% | 23.3% | 20.6% | 23.5% | 24.9% | 24.8% |
| Net profit margin | 11.0% | 12.2% | 14.2% | 10.8% | 14.5% | 16.6% | 17.0% |
| Return on assets | 5.7% | 6.5% | 6.5% | 5.2% | 7.3% | 8.7% | 9.9% |
| Return on equity | 14.2% | 13.9% | 12.6% | 10.2% | 14.1% | 16.3% | 17.4% |
| **Leverage ratio** | | | | | | | |
| Debt / equity (x) | 0.99 | 0.62 | 0.63 | 0.63 | 0.59 | 0.46 | 0.36 |
| **Market/valuation ratios** | | | | | | | |
| EV/sales (x) | 6.7 | 6.5 | 5.8 | 4.7 | 4.3 | 3.9 | 3.4 |
| EV/EBITDA (x) | 31.2 | 30.4 | 24.9 | 23.1 | 18.2 | 15.6 | 13.6 |
| EPS (SAR) | 2.7 | 3.7 | 4.6 | 4.2 | 6.3 | 7.8 | 9.0 |
| BVPS (SAR) - Adjusted | 22.11 | 32.79 | 40.59 | 42.83 | 45.86 | 49.64 | 53.62 |
| Market price (SAR)* | 148.00 | 171.80 | 160.80 | 160.80 | 160.80 | 160.80 | 160.80 |
| Market-Cap (SAR mn) | 15,032 | 17,450 | 16,332 | 16,332 | 16,332 | 16,332 | 16,332 |
| Dividend yield | 1.4% | 1.2% | 1.2% | 1.2% | 2.0% | 2.5% | 3.1% |
| P/E ratio (x) | 54.8 | 46.4 | 35.3 | 37.9 | 25.6 | 20.7 | 17.9 |
| P/BV ratio (x) | 6.7 | 5.2 | 4.0 | 3.8 | 3.5 | 3.2 | 3.0 |

Sources: AlJazira Capital, Company Financials

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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