



Flat like Y/Y net income growth in Q2-24 due to margins at lowest in c. 5 years; 39% capacity expansion to drive future growth

Mouwasat reported its Q2-24 results at a net income of SAR 152.7mn (up 1.4% Y/Y, and down 11.0% Q/Q). Its results were burdened by a contraction in GP margins which reached 44.5% (down 210bps Y/Y, and 330bps Q/Q), as a result of its recent Madinah Long Term Care Hospital (100 beds) which became operational by H1-24, as well as investments in specialized services. OPEX-to-revenue at 19.5% improved slightly by 30bps Y/Y while contracting 170bps Q/Q. We see its upcoming expansions scheduled for H2-25 in the Western region in Jeddah (300 beds) and Yanbu (200 beds) a driver for its short term performance; driving our FY23-26E CAGR estimate to 13.9%. Its minimal Riyadh expansion of 120 beds, expected by FY28E, is forecasted to extend its longer term revenue growth estimates to an FY23-28E CAGR of 11.4%. We see its c. 39% beds capacity expansion a catalyst to further GP margin decline, estimated to reach 46.0% by FY25, down c. 250bps from FY23 levels. Our forecasts punctuate at a FY23-FY28E NI CAGR of 15.3%, in support by OPEX efficiencies. We revise our TP for the firm to **SAR 110.0 per share** at a “Neutral” recommendation.

Top line growth and lower OPEX in Q2-24 came head-to-head with lowest GP Margins in five years to record a net income of SAR 152.7mn: Mouwasat ended Q2-24 to record bottom line of SAR 152.7mn at a lackluster growth of 1.4% Y/Y (down 11.0% Q/Q). Results were supported by revenues reaching SAR 690.3mn (up 10.0% Y/Y, and down 4.5% Q/Q); driven by the recent operation, and ramping up, of the Madina Long Term Care Hospital (100 beds) which came online in H1-24. Management reported improved contractual terms with their customers which likely also supported revenue growth for the quarter. The firm’s Madinah expansion, along with investments in service specializations, pressured quarterly gross profit margins to 2019 levels to reach 44.5% in Q2-24 (down 210bps Y/Y, and 330bps Q/Q). OPEX-to-revenue at 19.5% rose slightly by 30bps Y/Y (down 170bps Q/Q), yet operational income was likely supported by increase in other income to record SAR 176.2mn in OP income (down 0.7% Y/Y and 9.8% Q/Q).

Expansion campaign (620 beds) of 39% of current capacity to drive our FY23-28E revenue CAGR estimate of 11.4% at the cost of GP margins: Mouwasat seeks to increase its foothold in the Western region via a 500 bed expansion in the region by FY25. Jeddah’s 300 bed expansion, at a 51% stake, is scheduled to be operational by Q2-25; with Yanbu’s expansion following right after in Q3-25. We expect the pressures of the c. 31% capacity expansions to contract margins to 46.0% by FY25E’s end, at a 250bps decline from FY23. In return, the H2-25 expansions are expected to carry the revenue growth from FY23-26E at a CAGR of 13.9%. At a longer term, Mouwasat’s Riyadh expansion in the Qadisiya district at 120 beds increases its consolidated beds capacity to 2,220 beds expected by FY28E; a c. 39% capacity increase from its current 1,600. Mouwasat’s expansion campaign is the chief driver to our estimated FY23-28E revenue CAGR of 11.4%. We do see the current pressures on GP margins to carry on for a year and a half, as seen in similar cases across other providers with a similar profile. Current pressures on GP margins are likely to coincide with FY25’s 500 bed expansions to reach 46.0% (250bps less than FY23 levels), before improving to 46.6% in FY28; while facing slight pressures during FY28 from the c. 5% capacity expansion from its future capacity levels. Current GP margins for H1-24 sit at 46.2%. We estimate operating margins at a similar trajectory, reaching 27.5% (down 50bps from FY23) while facing the effects of the expansions along the way. Our estimates punctuate at a FY23-28E net income CAGR of 15.3%.

AJC view and valuation: Our main takeaway from Mouwasat’s recent results were the display of margin contractions post an only 6% expansion in its capacity, as it was also coupled by investments in specialized services. However, we estimate the potentials going forward for further GP margin declines as it faces an upcoming 31% capacity expansion by FY25E. Furthermore, while Mouwasat enjoys the highest GP margins among its peers (TTM), its net income margin at 23.5% sits neck-to-neck with the top four providers’ net margins, which average at 22.7%. We do, however, forecast net margins for the firm to wither down from FY23’s NI margin of 24.6% to 24.1% by FY25E amid expansionary pressures. While downside risks from further margin pressures are present, we see that the firm’s minimal net D/E at 0.15x, which sits at its lowest among its peers, provides the firm with a healthy headroom to raise debt to support any shortfalls in cash needs from any potential contracting operational cashflows; while also supporting its dividend payouts. Upsides to our valuation are present in the potential success of its four-clinics pipeline which are under design and licensing. We value the stock at a blended 50% DCF (WACC=9.5%, and terminal growth=2.5%) and 50% PE (32x on FY24-25E averages) to arrive at a revised TP of **SAR 110.0 per share**, at a “Neutral” recommendation.

Recommendation	Neutral
Target Price (SAR)	110.0
Upside / (Downside)*	6.4%

Source: Tadawul *prices as of 8th of Aug 2024

Key Financials

in SAR mn, (unless specified)	FY22	FY23	FY24E	FY25E
Revenue	2,334	2,706	2,937	3,393
Growth %	8.9%	15.9%	8.6%	15.5%
Net Income	599.3	666.4	730.2	818.7
Growth %	3.7%	11.2%	9.6%	12.1%
EPS	3.00	3.33	3.65	4.09
DPS	1.50	1.75	1.90	2.50

Source: Company reports, Aljazira Capital

Key Ratios

	FY22	FY23	FY24E	FY25E
Gross Margin	47.1%	48.5%	46.7%	46.0%
OP Margin	28.4%	28.0%	28.8%	27.5%
Net Margin	25.7%	24.6%	24.9%	24.1%
EBITDA Margin	36.3%	36.1%	36.5%	34.9%
RoE	21.7%	21.5%	21.1%	21.4%
P/E (x)	69.7	33.6	28.3	25.3
P/B (x)	7.2	6.8	5.7	5.2
EV/EBITDA (x)	50.1	23.6	20.0	18.1
Dividend Yield	0.7%	1.4%	1.7%	1.8%

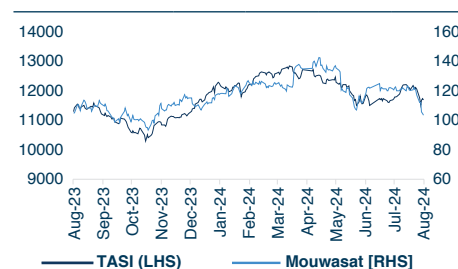
Source: Company reports, Aljazira Capital

Key Market Data

Market Cap (SAR bn)	20.8
YTD%	-7.5%
52 weeks (High)/(Low)	144.0/92.5
Share Outstanding (bn)	200

Source: Company reports, Aljazira Capital

Price Performance



Source: Tadawul, Aljazira Capital

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Key Financials

Amount in USD mn, unless otherwise specified	FY20	FY21	FY22	FY23	FY24E	FY25E	FY26E	FY27E	FY28E
Income statement									
Revenues	2,045.0	2,144.1	2,334.1	2,705.5	2,936.9	3,393.3	3,996.8	4,241.4	4,647.5
Y/Y	10.1%	4.8%	8.9%	15.9%	8.6%	15.5%	17.8%	6.1%	9.6%
Cost	(1,084.7)	(1,148.4)	(1,235.2)	(1,392.4)	(1,564.9)	(1,833.4)	(2,136.1)	(2,258.2)	(2,481.9)
Gross profit	960.3	995.8	1,098.9	1,313.1	1,372.0	1,559.8	1,860.7	1,983.2	2,165.5
Selling & distribution expense	(124.2)	(98.9)	(117.3)	(110.2)	(104.9)	(138.7)	(145.5)	(150.1)	(155.2)
General & administration expense	(258.2)	(275.0)	(318.5)	(337.4)	(363.6)	(428.6)	(435.6)	(441.1)	(459.3)
Amortization of intangible assets	-	-	-	-	-	-	-	-	-
Operating profit	577.8	621.9	663.1	865.4	903.5	992.5	1,279.7	1,392.0	1,551.0
Y/Y	22.8%	7.6%	6.6%	30.5%	4.4%	9.9%	28.9%	8.8%	11.4%
Other income	13.1	18.5	20.1	18.9	22.6	22.3	21.8	23.2	25.5
Financial charges	(14.0)	(8.2)	(22.9)	(46.5)	(56.0)	(48.0)	(46.5)	(41.7)	(32.0)
Profit before zakat & minority interest	576.9	632.2	660.3	837.9	870.0	966.8	1,255.0	1,373.5	1,544.6
Non-controlling interest	(33.5)	(32.3)	(33.4)	(30.7)	(30.5)	(39.1)	(48.1)	(51.3)	(56.1)
Profit before zakat	543.4	599.9	626.9	807.2	839.6	927.7	1,206.9	1,322.3	1,488.5
Zakat	(15.2)	(21.7)	(27.6)	(38.7)	(50.5)	(50.6)	(65.8)	(72.1)	(81.1)
Net income	528.2	578.2	599.3	768.5	789.1	877.1	1,141.1	1,250.2	1,407.3
Y/Y	25.4%	9.5%	3.7%	28.2%	2.7%	11.2%	30.1%	9.6%	12.6%
EPS	2.64	2.89	3.00	3.33	3.65	4.09	5.46	6.00	6.79
DPS	1.25	1.38	1.50	1.75	1.90	2.50	3.30	3.90	4.40
Balance sheet									
Assets									
Cash & bank balance	160	157	144	49	153	335	601	916	1,169
Other current assets	1,035	1,158	1,430	1,550	1,645	1,764	1,903	1,886	1,990
Property & Equipment	2,203	2,419	2,808	3,046	3,364	3,595	3,638	3,625	3,565
Other non-current assets	250	325	280	301	284	318	401	423	459
Total assets	3,649	4,059	4,662	4,946	5,446	6,012	6,543	6,850	7,183
Liabilities & owners' equity									
Total current liabilities	551	640	767	831	752	929	1,054	1,091	1,142
Long-term loans	575	564	628	500	753	811	761	622	412
Total other non-current liabilities	143	153	162	173	134	134	148	129	139
Non-controlling interest	101	98	153	150	153	158	164	170	177
Paid-up capital	1,000	1,000	1,000	2,000	2,000	2,000	2,000	2,000	2,000
Statutory reserves	300	300	300	366	439	521	630	630	630
Other reserve	-	-	-	-	-	-	-	-	-
Dividend	-	-	-	-	-	-	-	-	-
Retained earnings	979	1,304	1,623	911	1,214	1,460	1,788	2,208	2,683
Total owners' equity	2,279	2,604	2,923	3,277	3,653	3,981	4,417	4,838	5,313
Total equity & liabilities	3,649	4,059	4,634	4,930	5,446	6,012	6,543	6,850	7,183
Cashflow statement									
Operating activities	483	683	707	814	932	1,046	1,328	1,545	1,650
Investing activities	(319)	(446)	(473)	(475)	(525)	(513)	(399)	(296)	(274)
Financing activities	(208)	(240)	(247)	(434)	(302)	(353)	(663)	(934)	(1,123)
Change in cash	(44)	(3)	(13)	(95)	104	181	267	315	253
Ending cash balance	160	157	144	49	153	335	601	916	1,169
Key fundamental ratios									
Liquidity ratios									
Current ratio (x)	2.2	2.1	2.1	1.9	2.4	2.3	2.4	2.6	2.8
Quick ratio (x)	1.8	1.8	1.8	1.7	2.1	2.0	2.1	2.3	2.5
Profitability ratios									
Gross profit margin	47.0%	46.4%	47.1%	48.5%	46.7%	46.0%	46.6%	46.8%	46.6%
Operating margin	28.3%	29.0%	28.4%	28.0%	28.8%	27.5%	30.8%	31.7%	32.3%
EBITDA margin	35.3%	36.2%	36.3%	36.1%	36.5%	34.9%	37.7%	38.5%	38.8%
Net profit margin	25.8%	27.0%	25.7%	24.6%	24.9%	24.1%	27.3%	28.3%	29.2%
Return on assets	15.1%	15.0%	13.7%	13.8%	14.0%	14.3%	17.4%	17.9%	19.4%
Return on equity	24.9%	23.7%	21.7%	21.5%	21.1%	21.4%	26.0%	25.9%	26.8%
Leverage ratio									
Debt / equity (x)	0.3	0.3	0.3	0.2	0.2	0.2	0.2	0.2	0.1
Market/valuation ratios									
EV/sales (x)	13.8	16.5	18.2	8.5	7.3	6.3	5.3	5.0	4.4
EV/EBITDA (x)	39.0	45.6	50.1	23.6	20.0	18.1	14.2	12.9	11.4
EPS (SAR)	2.64	2.89	3.00	3.33	3.65	4.09	5.46	6.00	6.79
BVPS (SAR)	22.8	26.0	29.2	16.4	18.3	19.9	22.1	24.2	26.6
Market price (SAR)*	138.0	173.8	209.0	111.8	103.4	103.4	103.4	103.4	103.4
Market-Cap (SAR mn)	27,600	34,760	41,800	22,360	20,680	20,680	20,680	20,680	20,680
Dividend yield	0.7%	0.7%	0.7%	1.3%	1.7%	1.8%	2.4%	3.2%	3.8%
P/E ratio (x)	52.3	60.1	69.7	33.6	28.3	25.3	18.9	17.2	15.2
P/BV ratio (x)	6.1	6.7	7.2	6.8	5.7	5.2	4.7	4.3	3.9

Sources: Aljazira Capital, Company Financials





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TERMINOLOGY

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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.

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