Middle East Healthcare Co.

Investment Update

Sector-wide competition pressures seen in last two quarters prompts forecast revision; we remain "Overweight" on the back of MEH's turnaround potential

Middle East Healthcare (MEH, Saudi German Hospitals) reported a net income of SAR 160.1mn (up 263.9% Y/Y, and 49.5% Q/Q) driven by a SAR 114mn capital gain on its Riyadh land recorded during the quarter. Adjusted net income would have stood at an estimated SAR 46.1mn, to record a normalized 4.9% Y/Y growth, and down 33.8% Q/Q. Pressures were seen in the top line from Ramadan seasonality as well as price competition in Jeddah from new facilities in the region. Increasing OPEX likely from Makkah and Dammam operational expansion hires further added pressures to the bottom line. GPMs remained resilient, underscoring the firm's operational initiatives which they are undergoing now that the bulk of MEH's expansions are behind it. We expect the firm to continue its turnaround initiatives amid the focus shifted from expansions to 1) operations, 2) lower finance expenses amid partial sukuk callback and financial restructuring, 3) enhance its top line, 4) costs efficiencies, and 4) DRG premium initiatives, to support its profitability metrics to tend towards industry averages. We downgrade FY25 & FY26 net income forecasts by 16.3% & 6.4% to SAR 262.2mn & SAR 348.9mn (normalized), at a revised FY24-29E CAGR extending to 17.9%, amid more apparent competitive pressures across the sector. We revise down our TP to 77.2/share, while remaining "Overweight" on the stock which trades at an adjusted FY25E forward PE of 18x.

Capital gain of SAR 114mn from land sale supported Q1-25 results; seasonality and Jeddah facility performance pressured top line: MEH recorded a one-off driven bottom line of SAR 160.1mn (up 263.9% Y/Y and 49.5% Q/Q), supported by the Riyadh land sale capital gain of SAR 114mn. Normalized net income would have stood at an estimated SAR 46.1mn at a 4.9% Y/Y growth (down 33.8% Q/Q from a normalized Q4-24). Ramadan seasonality taking place entirely in Q1-25 (almost 7 days more Y/Y), and Jeddah facility performance added top line pressures on the quarterly revenue reaching SAR 733.7mn (up 6.5% Y/Y and down 2.0% Q/Q). Jeddah's facility being a mostly outpatient faced sensitivity to seasonal effects of Ramadan, while the facility also faces pricing competition from new hospitals in the region. While gross profit margin rose to 38.7% (up 100bps Y/Y and Q/Q), SG&As rose 28% Y/Y and 1% Q/Q likely due to hirings for Makkah facility additional capacity ahead of Hajj, as well as for the increase in licensed capacity at Dammam facility (to 300 beds). Q2-25 is expected to display a turnaround from Q1-25 from a less seasonally burdened quarter, as well as an expected stronger contribution from the Makkah facility during Hajj season.

Quarterly revenue slowdowns display competitive pressures; we revise our forecasts from previous estimates to reflect increased competition while maintaining GPM resilience at MEH: Softer Q4-24 and Q1-25 revenue growth displayed the theme of increased competition. While flat patient volume growth (Y/Y) in Q1-25 was lead by Ramadan, we consider the effect of increasing competition in Jeddah adding onto that. Furthermore, while the Riyadh facility continues to ramp up, its newly opened neighbor hospital run by Sulaiman AlHabib (HMG) will continue to be a source of competition over patient volumes. Our net income forecasts are revised down by 16.3% and 6.4% for FY25 & FY26 to reach SAR 262.2mn & SAR 348.9mn (normalized) amid competitive pressures in Riyadh and Jeddah. Revenue & net income CAGR forecasts to reach 7.5% and 17.9% through FY24-29E; we maintain our view on MEH's GPM resilience, as the firm leads value based healthcare in the Kingdom, with advanced cost control measures, as well as initiatives on staff retention for long term cost saving. With little expansion ahead for the firm our forecasted GPM expands from 38.6% in FY24 to 38.9% by FY28E, while dipping 80bps Y/Y in FY26E due to the 194 bed brownfield expansion in Jeddah. Cost efficiencies amid little expansions, as well as decreasing finance costs as a result of the gradual callback of the Sukuk and financial restructuring plan further improves the bottom line growth in the coming years for the firm which has had the bulk of its expansions already behind it.

Recommendation	Overweight
Target Price (SAR)	77.2
Upside / (Downside)*	49.6%

Source: Tadawul *prices as of 19th of June 2025

Key Financials

in SAR mn, (unless specified)	FY24	FY25E	FY26E	FY27E
Revenue	2,883	3,090	3,525	3,771
Growth %	8.7%	7.2%	14.1%	7.0%
Gross Profit	1,114	1,216	1,356	1,470
EBIT	441	468	525	593
Net Income*	282	376*	349	446
Growth %	HIGH	33.4%	-7.3%	27.7%
EPS	3.06	4.09	3.79	4.84
DPS	0.0	0.0	0.0	1.0

Source: Company reports, Aljazira Capital *Includes SAR 114mn income from land sale

Key Ratios

	FY24	FY25E	FY26E	FY27E
Gross Margin	38.6%	39.3%	38.5%	39.0%
OP Margin	15.30%	15.15%	14.88%	15.73%
Net Margin	9.8%	12.2%	9.9%	11.8%
EBITDA Margin	22.8%	22.2%	21.5%	22.4%
RoE	18.6%	20.2%	15.7%	17.0%
RoA	5.5%	7.1%	6.2%	7.7%
P/E	22.4	12.6	13.6	10.7
P/B	3.9	2.4	2.0	1.7
EV/EBITDA	13.6	10.7	9.6	8.2
Dividend Yield	0.0%	0.0%	0.0%	1.9%

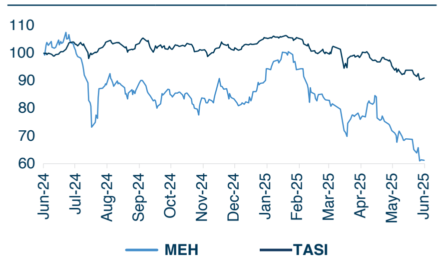
Source: Company reports, Aljazira Capital Research

Key Market Data

Market Cap (SAR bn)	4.7
YTD%	-25.9%
52 weeks (High)/(Low)	91.6/49.7
Share Outstanding (mn)	92.0

Source: Company reports, Aljazira Capital Research

Price Performance



Source: Tadawul, AlJazira Capital Research

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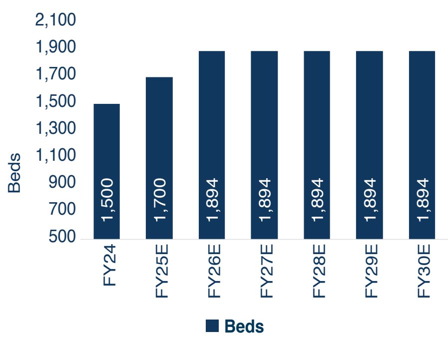
Gradual Sukuk callback towards financial restructuring, and continued improved working capital to aid improvement in financial position and bottom line growth: MEH approved a partial gradual callback of its SAR1bn sukuk which we expect the firm to continue doing so as the economic cycle tends towards a lower rate environment in the coming years. Large receivables payments from MoH in Q4-24's end and Q1-25, as well as continuous reconciliation with insurance clients further aided working capital improvements for the firm which management expects to continue. Net receivables reached SAR 1.8bn, down from SAR 2.3bn at the start of FY24; we expect receivables to rise in proportion to revenues though at slight improved collection durations. We forecast improved operating cash generation to aid in gradually deleveraging the firm, where we expect current D/E levels of 1.4x to wind down to 0.9x by FY26E, post expansion, and ROAA and net margin reaching 6.2% and 9.9% up from a normalized 4.2% and 7.5% in FY24. Due to restructured financials from partial Sukuk callback and ahead of lower interest rate environment, we expect finance costs coming down 56% from FY24-28E to support long term net income growth. We estimate that MEH could potentially start to pay dividends of SAR 1.0/share from FY27, post Jeddah expansion.

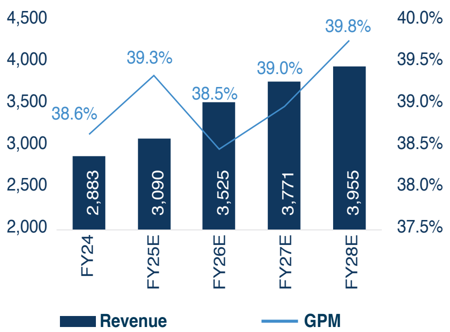
Breathing room for MEH to focus on operational initiatives, and reducing finance costs, underscore its expected turnaround story after expanding at an estimated 50% to c. 1,500 beds through FY19-24: We consider MEH to be out of the woods from expansionary pressures and volatility, as only a 194 bed brownfield expansion remains ahead of it; giving the firm the headroom to focus on patient attraction, ramp ups and efficiency initiatives. In doing so, MEH has increased its specialized and sub specialized medical staff by almost 30% from FY23 to reach 356 by FY24 to enhance case mix and improve DRG positioning. Its breathing room found from post expansions also enabled the firm to expand in medical education initiatives to benefit from the financial incentives from talent breeding, and potential DRG premiums. Furthermore, MEH's turnover rates improved from 14.8% in FY23 to 12.7% in FY24, with initiatives towards further improvement. MEH aims to further increase its retention rate initiatives after the firm was also able to receive the highly accredited Magnet nursing accreditation, which facilities with the accreditation are usually at 16% lower turnover rates than non-Magnet hospitals. The firm is also a leader and an early adaptor in the value based healthcare model in the Kingdom. These operational initiatives summarize the direction of the focus at MEH post-expansions, and the driver behind MEH being the second highest GPMs in the sector. While the firm sits subpar to industry profitability metrics (FY24 ROAA and net margin at 5.5% & 9.8%, compared to sector averages of 9.7% & 18.3%, respectively), the firm's scale and no expansion burdens sets MEH to turnaround towards industry figures, and driven by lesser financial costs expected.

Fig 1: Increasing operational beds through a brownfield expansion in Jeddah



Source: Company presentations, Aljazira Capital Research *FY25 increase includes operational beds licensed for Dammam, and Makkah increase

Fig 2: GPM trajectory aided by cost efficiency initiatives and challenged by FY26 expansion



Source: Company Financials, Aljazira Capital Research

AJC view and valuation: MEH has scaled up to be a c. 1,500 bed strong healthcare provider, with more headroom for growth from increasing operational beds at Dammam, Makkah, and the new Jeddah expansion. While major expansions are behind the firm, MEH is able to focus on operational initiatives, where we believe its turnaround potential lies. Furthermore, decrease in finance cost can streamline performance to bottom line, which we expect to contribute to bottom line growth in the coming years. As the firm currently sits at sub-par profitability metrics, it still recorded the third largest revenues in FY24 among its peers, and second highest GPMs in FY24, highlighting its profitability potentials post deleveraging and operational efficiencies post ramp ups. Efficiencies and reduction in finance costs are expected to drive long term performance; while FY25E to post a normalized 20.7% Y/Y growth at SAR 262.2mn vs SAR 217.2mn in FY24 (excluding one offs) with support of Dammam and Makkah increased capacities as well as resilience in GPMs. We downgrade our TP to **SAR 77.2 /share**, remaining "**Overweight**" on the stock trading at a FY25E forward P/E of 18x (normalized). We value the stock by way of 50% PE (25x on FY26E earnings, discounted) and 50% on DCF (9.3% WACC and 2.5% terminal growth rate).

Valuation Summary

	Target Price	Weight	Weighted TP
PE (25x on FY26E, discounted)	83.6	50%	41.8
DCF	70.8	50%	35.5
Target Price (SAR/Share):			**77.2**
Up/Downside (%)			**49.6%**

Source: AlJazira Capital Research, prices as of 19th June 2025

Upside risks to valuation:

- GPMs returning back to 50%s range
- More net income margin accretive Vision 2030 projects
- More geographically strategic expansions
- Favorable DRG premiums

Downside risks to valuation:

- Increased competitive pressures from neighboring facilities
- Slower than expected deleveraging

Key Financial Data

Amount in SARmn, unless otherwise specified	FY23	FY24E	FY25E	FY26E	FY27E	FY28E	FY29E	FY30E
Income statement								
Revenues	2,653	2,883	3,090	3,525	3,771	3,955	4,137	4,308.1
Y/Y	**23.3%**	**8.7%**	**7.2%**	**14.1%**	**7.0%**	**4.9%**	**4.6%**	**4.1%**
Cost	(1,638.8)	(1,768.9)	(1,874.0)	(2,169.3)	(2,301.0)	(2,382.3)	(2,465.9)	(2,540.2)
Gross profit	**1,014.4**	**1,113.9**	**1,215.8**	**1,356.0**	**1,469.8**	**1,572.7**	**1,671.5**	**1,767.9**
Gross profit Margin	**38.23%**	**38.64%**	**39.35%**	**38.47%**	**38.98%**	**39.76%**	**40.40%**	**41.04%**
Selling & distribution expense	(51.1)	(73.2)	(77.9)	(88.9)	(95.0)	(99.6)	(104.2)	(108.5)
General & administration expense	(639.4)	(599.8)	(669.2)	(742.6)	(782.3)	(812.7)	(839.8)	(863.7)
Share from associates			(0.6)	0.0	0.8	1.4	2.0	2.3
Operating profit	**324.0**	**440.9**	**468.1**	**524.6**	**593.3**	**661.8**	**729.5**	**798.0**
Y/Y	**130.8%**	**36.1%**	**6.2%**	**12.1%**	**13.1%**	**11.5%**	**10.2%**	**9.4%**
OP Margin	**12.21%**	**15.30%**	**15.15%**	**14.88%**	**15.73%**	**16.73%**	**17.63%**	**18.52%**
Other income	22.5	91.0	141.1	30.7	31.8	32.9	33.9	34.8
Financial charges	(155.6)	(221.8)	(196.8)	(168.8)	(134.8)	(97.2)	(58.0)	(45.7)
Profit before zakat & minority interest	**190.9**	**310.2**	**412.3**	**386.5**	**490.4**	**597.5**	**705.4**	**787.1**
Non-controlling interest	3.5	1.9	4.8	4.7	3.1	1.6	1.4	1.0
Profit before zakat	**20.5**	**283.9**	**380.9**	**353.6**	**448.7**	**546.7**	**645.4**	**720.2**
Zakat	(170.4)	(26.3)	(31.4)	(32.9)	(41.7)	(50.8)	(60.0)	(66.9)
Net income	**17.0**	**282.0**	**376.2**	**348.9**	**445.6**	**545.1**	**644.0**	**719.1**
Y/Y	**-77.3%**	**1555.1%**	**33.4%**	**-7.3%**	**27.7%**	**22.3%**	**18.1%**	**11.7%**
EPS (SAR)	**0.19**	**3.06**	**4.09**	**3.79**	**4.84**	**5.92**	**7.00**	**7.81**
DPS (SAR)	**0.00**	**0.00**	**0.00**	**0.00**	**1.00**	**1.50**	**1.50**	**1.75**
Balance sheet								
Assets								
Cash & bank balance	44	52	77	42	52	112	101	334
Receivables	2,301	1,946	2,191	2,452	2,571	2,642	2,708	2,760
Other current assets	191	175	187	211	198	201	205	208
Property & Equipment	2,502	2,767	2,862	2,880	2,872	2,864	2,853	2,833
Other non-current assets	96	185	141	158	170	177	177	170
Total assets	**5,135**	**5,125**	**5,458**	**5,743**	**5,863**	**5,997**	**6,044**	**6,305**
Liabilities & owners' equity								
Payables	559	322	346	406	437	459	482	504
Non-current debt	1,116	640	640	734	663	524	461	452
Total current liabilities	460	300	231	221	238	253	268	280
Long-term loans	1,310	753	863	779	617	543	531	180
Sukuk		989	879	729	579	429	-	-
Total other non-current liabilities	324	447	447	473	482	487	494	501
Non-controlling interest	46	48	49	49	50	51	52	52
Paid -up capital	920	920	920	920	920	920	920	920
Statutory reserves	219	219	219	219	219	219	219	219
Retained earnings	178	478	854	1,203	1,649	2,102	2,608	3,189
Total owners' equity	1,320	1,626	2,002	2,351	2,797	3,250	3,756	4,337
Total equity & liabilities	**5,135**	**5,125**	**5,458**	**5,743**	**5,863**	**5,997**	**6,044**	**6,305**
Cashflow statement								
Operating activities	191	766	312	392	658	787	909	1,010
Investing activities	(242)	(509)	(271)	(269)	(255)	(266)	(273)	(274)
Financing activities	80	(249)	(16)	(157)	(393)	(461)	(647)	(503)
Change in cash	29	8	25	(35)	10	59	(10)	233
Ending cash balance	**44**	**52**	**77**	**42**	**52**	**112**	**101**	**334**
Key fundamental ratios								
Liquidity ratios								
Current ratio (x)	1.2	1.7	2.0	2.0	2.1	2.4	2.5	2.7
Quick ratio (x)	1.2	1.7	2.0	1.9	2.0	2.3	2.4	2.6
Profitability ratios								
GP Margin	38.2%	38.6%	39.3%	38.5%	39.0%	39.8%	40.4%	41.0%
Operating Margins	12.2%	15.3%	15.1%	14.9%	15.7%	16.7%	17.6%	18.5%
EBITDA Margin	19.4%	22.8%	22.2%	21.5%	22.4%	23.5%	24.5%	25.5%
Net Margin	0.6%	9.8%	12.2%	9.9%	11.8%	13.8%	15.6%	16.7%
Return on assets	0.4%	5.5%	7.1%	6.2%	7.7%	9.2%	10.7%	11.6%
Return on equity	1.2%	18.6%	20.2%	15.7%	17.0%	17.7%	18.1%	17.5%
Leverage ratio								
Debt / equity (x)	1.8	1.4	1.2	0.9	0.7	0.5	0.3	0.1
Market/valuation ratios								
EV/sales (x)	3.8	3.0	2.3	2.0	1.8	1.6	1.4	1.2
EV/EBITDA (x)	20.2	13.6	10.7	9.6	8.2	7.0	5.9	4.9
EPS (SAR)	0.2	3.1	4.1	3.8	4.8	5.9	7.0	7.8
BVPS (SAR)	14.3	17.7	21.8	25.5	30.4	35.3	40.8	47.1
Market price (SAR)	83.3	68.7	51.6	51.6	51.6	51.6	51.6	51.6
Market-Cap (SAR mn)	7,667	6,323	4,749	4,749	4,749	4,749	4,749	4,749
Dividend yield	0.0%	0.0%	0.0%	0.0%	1.9%	2.9%	2.9%	3.4%
P/E ratio (x)	450.0	22.4	12.6	13.6	10.7	8.7	7.4	6.6
P/BV ratio (x)	5.8	3.9	2.4	2.0	1.7	1.5	1.3	1.1

Sources: AlJazira Capital, Company Financials *Prices as of 19th June 2025

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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