

Record high results supported by patient volumes and recent expansions. Expansion campaign to define next chapters in HMG's performance

HMG recorded record high quarterly results with a bottom line of SAR 555.0mn (up 14.0% Y/Y and 0.7% Q/Q) and top line of SAR 2,573.6mn (up 13.3% Y/Y, and 2.1% Q/Q). GP margins remained flat Y/Y at 34.1% while decreasing 70bps Q/Q, though we expect a more pronounced negative effect on GP margins from expansions going forward as HMG schedules a 78% expansion in built up bed capacities for FY24 over FY23 beds. Its expansion campaign, stretching to FY27, looks to expand its capacity by c. 90% of FY23 capacities, and it is this campaign which we see will define HMG's coming periods. We estimate an FY23-28E revenue CAGR of 13.8% and a bottom line CAGR of 13.9% for the same period. We value the stock at an upward revised TP of SAR 266.0 per share, while retaining our "Neutral" recommendation. Potential downside risks to our valuation stem mainly from project delays and higher than expected contraction on gross margins, while key favorable specifications at HMG over its peers warrant a premium over the sector.

Q2-24 results reached record highs as patient volumes and recent expansions supported the period: HMG in Q2-24 reached a bottom line of SAR 555.0mn (up 14.0% Y/Y and 0.7% Q/Q) to record its highest ever quarterly net income to date. HMG also recorded its highest quarterly top line, in line with our forecast, at SAR 2,573.6mn (up 13.3% Y/Y, and 2.1% Q/Q), despite the seasonally down-quarter, due to higher patient volumes at HMG- likely as a result of expansions in the past two quarters. All segments experienced growth with the Hospitals segment and the Pharmacies segment growing 13.0% Y/Y and 12.0% Y/Y, respectively, as patient volumes increase. The Solutions segment also grew 32.8% Y/Y. Despite two major expansions coming in during H1-24 (Sahafa and South West Jeddah), HMG recorded a GP Margin of 34.1% (flat Y/Y, and down 70bps Q/Q). The Sahafa expansion, however, only partially took place during this quarter, opening in early June, and will likely have a more pronounced effect on margins in the next quarter. Operating income of SAR 551.7mn displayed a growth of 10.6% Y/Y, (down 0.8% Q/Q) as OPEX to revenue rose 60bps Y/Y. Net non-operating income (excl non-controlling interests) reached SAR 22.6mn (up 68.5x Y/Y, and 41% Q/Q) to support the bottom line of SAR 555.0mn during the quarter.

636 beds capacity expansions scheduled for the year to define the next chapters of HMG's upcoming future performance: HMG looks to expand its built-up beds capacity to reach an estimated 3,414 beds by FY24's end, a 78% increase over its estimated beds capacity of 1,913 during FY23's end. In the pipeline- North Jeddah (350 beds), Takhasusi (145 beds), and AlKharj are scheduled by EOY, while management indicates that the AlKharj and Takhasusi expansions are ahead of schedule. These expansions come in atop the Sahafa (500 beds) and South West Jeddah (330 beds) expansions seen during H1-24, and a minor Qassim expansion. Operational beds, however, are expected to roll out gradually, as per patient volumes, as HMG tends to initially begin operating at 30% of a facility's capacity during kick off. The expansions scheduled during this year, and ahead (90 beds in Hamra, 2025, and 140 beds in Tabuk, 2027) are the major drivers for our expected FY23-28E CAGR of 13.8%, while we see the effects of adverse quarterly seasonality on the top line to be mitigated by ramp ups in the medium term. We estimate a bottom line growth of an FY23-28E CAGR of 13.9% driven by a 90% beds expansion over FY23 capacities, and favorable demographics and regulatory initiatives.

Margins expected to scale back as a result of expansion campaign: Gross margins are expected to be pressurized during FY24-25, as we expect GPMs to wind down by 100bps by FY25 while recent expansions ramp up. Our reason for modest GPM declines are twofold 1) Recent ramp up in Jeddah has been successful with its first seven weeks of operations surpassing Khobar's ramp up by nearly double. We take that as a sign of good demand for expansions in Jeddah and other areas with a lack of presence of premium private healthcare providers. 2) HMG at its scale and size would be able to mitigate the effects of major expansions more than smaller providers. We expect a similar trajectory for its operating margins, reaching 20.9% in FY25E, from 22.0% in FY23, before improving from FY26 onwards.

Recommendation	Neutral
Target Price (SAR)	266.0
Upside / (Downside)*	-5.9%

Source: Tadawul *prices as of 28th of July 2024

Key Financials

SARmn (unless specified)	FY22	FY23	FY24E	FY25E
Revenues	8,311	9,508	11,139	13,393
Growth %	14.6%	14.4%	17.1%	20.2%
Net Income	1,651	2,046	2,196	2,572
Growth %	19.9%	23.9%	7.3%	17.1%
EPS	4.72	5.85	6.28	7.35
DPS	3.48	4.32	4.70	5.50

Source: Company reports, Aljazira Capital

Key Ratios

	FY22	FY23	FY24E	FY25E
Gross Margin	33.1%	34.4%	33.9%	33.4%
OP Margin	20.5%	22.0%	21.2%	20.9%
Net Margin	19.9%	21.5%	19.7%	19.2%
EBITDA Margin	24.2%	25.3%	27.8%	27.1%
RoE	29.4%	33.1%	32.5%	34.9%
P/E (x)	60.2	48.3	45.0	38.5
P/B (x)	16.9	15.3	14.1	12.9
EV/EBITDA (x)	49.8	42.0	33.0	28.2
Dividend Yield	1.2%	1.5%	1.7%	1.9%

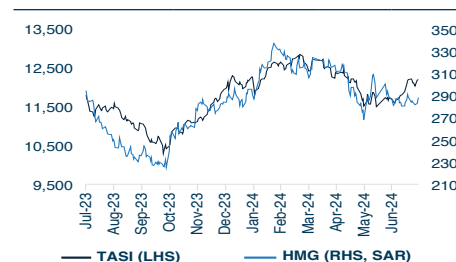
Source: Company reports, Aljazira Capital

Key Market Data

Market Cap (SAR bn)	99.5
YTD%	-0.5%
52 weeks (High)/(Low)	346.8/223.2
Share Outstanding (bn)	350.0

Source: Company reports, Aljazira Capital

Price Performance



Source: Tadawul, Aljazira Capital

Equity Analyst

Ibrahim Elaiwat

+966 11 2256115

i.elaiwat@Aljaziracapital.com.sa



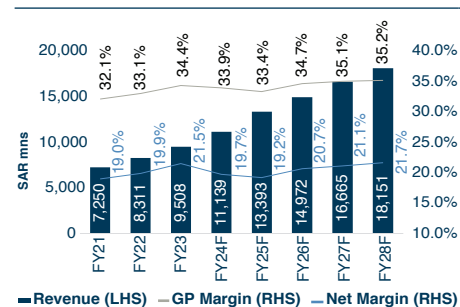


Estimated CAPEX of c. SAR 7bn (FY24-28E) is expected to reshape capital profile towards more debt: D/E for the firm increased over 20 percentage points from 63.0% to 83.7% Y/Y by Q1-24 as scheduled expansion pile on and long term debt increases 51% Y/Y from SAR 3.65bn to SAR 5.52bn in Q1-24. Going forward, we expect HMG's D/E to reach 0.9x by FY24 before winding down amid repayments from operating cash flows. In turn, we expect the charges on the relevant debts to be shown at the P&L level once facilities are online. Finance charges from the latest commercialized facilities are expected to begin appearing this year. In effect we estimate that HMG's net other income-less-finance charges, which was shrinking in the past two years, to turn negative amid more expansions coming online, as out of HMG's cash holding of 2.52bn, 2.02bn are in estimated income earning deposits at near 6%; lower than its finance charges at SAIBOR+ a premium. We forecast finance charges to peak by FY24E's at SAR 204.6mn end before showing improvement in charges by FY26E. We do not see this as a risk, however, to HMG's expected future dividend payouts of above 70%.

Competitive advantages at HMG to deem it a sector leader among peers: HMG possesses leading specifications among its peers, starting with its brand equity among the Saudi Arabian market. Furthermore, its corporate social responsibility (CSR) initiatives, education & research initiatives as well as its efficient pricing strategy is likely to fare well for its DRG multiples once the DRG (diagnosis-related group pricing) system is in effect. Multiples, and DRG bases are however still not announced, though we expect HMG's efficiency and social initiatives to mitigate any negative effects on pricing multiples in urban areas, and should benefit its pricing multiples for facilities in rural areas. Furthermore, HMG's size as the largest publically listed private healthcare provider, and more so after its 90% capacity expansions, should unlock more potentials for efficiency and value in the long run as it also becomes a household name across other regions it is tapping into. We see the stock as one with a fundamental moat around its business for the long term with a solid basis for a premium among its peers.

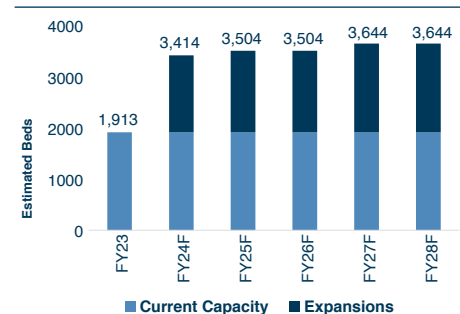
AJC view and valuation: HMG ended Q2-24 with record high results for its bottom line of SAR 550.0mn (up 14.0% Y/Y and 0.7% Q/Q) and top line of SAR 2,573.6mn (up 13.3% Y/Y, and 2.1% Q/Q) while gross margins contract Q/Q but remain flat Y/Y at 34.1%. The period saw a brief operation of the newly opened Sahafa facility, as well as a quarter of the newly opened South West Jeddah facility, which likely supported patient volumes and pressurized margins slightly. Going forward, we expect the additional expansions to define the next chapters of HMG's performance, as HMG braces for planned expansions that can host 90% more beds than its FY23 capacity. In effect we expect an FY23-28E revenue CAGR of 13.8%, as gross profit margin pressurize over FY24-25 to reach 33.4% before improving thereafter. We expect minimal contractionary effects on GP margins from the FY27 Tabuk expansion, at HMG's scale. We expect operating margins at a similar trajectory as gross profit margins, to reach 20.9% in FY25 and improve thereafter. Our forecasts punctuate at a bottom line FY23-28E CAGR of 13.95%. We see that HMG's next periods come with several risks to our valuation: 1) Development risks and delays could reshape the expected timeline of HMG's growth, 2) Staffing challenges could delay expansion licensing from MoH, 3) Slower ramp ups, particularly at the Riyadh facility, and 4) Changes in revenue structure from DRG pricing after the shadow billing period. However, we see that HMG possess many key advantages to the stock granting it a premium over its peers from its brand equity, partnership with government initiatives (NEOM, sporting events, medical centers in tourist areas), scale and size, and efficiency & CSR and their potential effects on DRG multiples. We value the stock using a blended, 50% DCF valuation (WACC = 7.8% and terminal growth rate = 3.0%) and 50% on PE valuations (36.0x on FY25E estimates) to arrive at a revised TP of **SAR 266.0 per share**, while retaining our **"Neutral"** recommendation on the stock, as it trades at a FY25E forward P/E of 38.5x.

Fig 1. Performance to be supported by expansions underway and future expansions from FY24-27



Sources: ALJazira Capital, Company Financials

Fig 2. Significant expansion campaign to set HMG as the largest listed private healthcare provider



Sources: ALJazira Capital, Company Disclosures *Representing facility capacities. Operational capacities are rolled out gradually for new facilities. **Labels representing total capacities





Fig 4. Key Financials

Amount in SAR mn, unless otherwise specified	FY21	FY22	FY23	FY24E	FY25E	FY26E	FY27E	FY28E
Income statement								
Revenues	7,250	8,311	9,508	11,139	13,393	14,972	16,665	18,151
Y/Y	23.7%	14.6%	14.4%	17.1%	20.2%	11.8%	11.3%	8.9%
Gross profit	2,330	2,748	3,270	3,781	4,470	5,194	5,844	6,392
OPEX	(379.4)	(398.1)	(369.0)	(419.6)	(550.5)	(615.3)	(684.6)	(745.4)
Operating profit	1,466	1,700	2,096	2,367	2,798	3,325	3,763	4,198
Y/Y	31.5%	16.0%	23.2%	12.9%	18.2%	18.8%	13.2%	11.6%
Financial charges	(37.9)	(49.4)	(70.1)	(204.6)	(198.4)	(162.8)	(137.6)	(124.3)
Other income/income from associates	73.1	145.5	144.4	195.4	185.6	184.0	178.6	166.7
Profit before zakat & minority interest	1,501	1,797	2,170	2,357	2,785	3,346	3,804	4,240
Zakat and minority interest	(114.1)	(107.7)	(68.5)	(89.3)	(139.3)	(167.3)	(190.2)	(212.0)
Net income	1,377	1,651	2,046	2,196	2,572	3,096	3,523	3,931
Y/Y	30.4%	19.9%	23.9%	7.3%	17.1%	20.4%	13.8%	11.6%
EPS	3.93	4.72	5.85	6.28	7.35	8.85	10.07	11.23
DPS	2.8	3.48	4.32	4.70	5.50	6.55	7.55	8.42
Balance sheet								
Assets								
Cash & bank balance	2,644	2,747	2,620	3,005	2,223	2,313	3,596	5,084
Other current assets	1,490	1,413	1,517	1,621	1,902	2,043	2,198	2,367
Property & Equipment	6,653	7,937	11,163	12,884	14,393	15,064	14,754	14,316
Other non-current assets	41	487	498	498	498	498	498	498
Total assets	10,827	12,584	15,798	18,008	19,015	19,918	21,046	22,264
Liabilities & owners' equity								
Total current liabilities	2,048	2,590	3,299	4,448	5,137	5,526	5,968	6,346
Long-term loans	2,445	3,033	4,810	5,214	4,660	4,188	3,785	3,441
Total other non-current liabilities	808	856	922	957	1,110	1,210	1,328	1,433
Non-controlling interest	188	227	281	352	425	507	596	692
Total owners' equity	5,339	5,879	6,485	7,037	7,682	8,487	9,368	10,351
Total equity & liabilities	10,827	12,584	15,798	18,008	19,015	19,918	21,046	22,264
Cashflow statement								
Operating activities	2,183	2,844	3,244	3,408	4,104	4,476	4,983	5,318
Investing activities	(1,248)	(1,939)	(3,487)	(2,451)	(2,344)	(1,576)	(624)	(519)
Financing activities	(631)	(801)	116	(573)	(2,543)	(2,809)	(3,076)	(3,312)
Change in cash	305	103	(127)	385	(783)	91	1,283	1,488
Ending cash balance	2,644	2,747	2,620	3,005	2,223	2,313	3,596	5,084
Key fundamental ratios								
Liquidity ratios								
Current ratio (x)	2.0	1.6	1.3	1.0	0.8	0.8	1.0	1.2
Quick ratio (x)	1.8	1.4	1.1	0.9	0.7	0.6	0.8	1.0
Profitability ratios								
Gross profit margin	32.1%	33.1%	34.4%	33.9%	33.4%	34.7%	35.1%	35.2%
Operating margin	20.2%	20.5%	22.0%	21.2%	20.9%	22.2%	22.6%	23.1%
EBITDA margin	24.6%	24.2%	25.3%	27.8%	27.1%	28.3%	28.2%	28.4%
Net profit margin	19.0%	19.9%	21.5%	19.7%	19.2%	20.7%	21.1%	21.7%
Return on assets	13.6%	14.1%	14.4%	13.0%	13.9%	15.9%	17.2%	18.2%
Return on equity	26.9%	29.4%	33.1%	32.5%	34.9%	38.3%	39.5%	39.9%
Leverage ratio								
Debt / equity (x)	0.6	0.6	0.8	0.9	0.7	0.6	0.5	0.4
Market/valuation ratios								
EV/sales (x)	7.8	12.1	10.6	9.2	7.6	6.8	6.0	5.4
EV/EBITDA (x)	31.9	49.8	42.0	33.0	28.2	24.0	21.3	19.0
EPS (SAR)	3.93	4.72	5.85	6.28	7.35	8.85	10.07	11.23
Market price (SAR)*	161.40	284.00	284.00	282.60	282.60	282.60	282.60	282.60
Market-Cap (SAR mn)	56,490	99,400	98,910	98,910	98,910	98,910	98,910	98,910
Dividend yield	1.7%	1.2%	1.5%	1.7%	1.9%	2.3%	2.7%	3.0%
P/E ratio (x)	41.0	60.2	48.3	45.0	38.5	31.9	28.1	25.2
P/B ratio (x)	10.6	16.9	15.3	14.1	12.9	11.7	10.6	9.6

Sources: AlJazira Capital, Company Financials





RESEARCH DIVISION

Head of Sell-Side Research - AGM
Jassim Al-Jubran
+966 11 2256248
j.aljabran@aljaziracapital.com.sa

RESEARCH
DIVISION

AlJazira Capital, the investment arm of Bank AlJazira, is a Shariaa Compliant Saudi Closed Joint Stock company and operating under the regulatory supervision of the Capital Market Authority. AlJazira Capital is licensed to conduct securities business in all securities business as authorized by CMA, including dealing, managing, arranging, advisory, and custody. AlJazira Capital is the continuation of a long success story in the Saudi Tadawul market, having occupied the market leadership position for several years. With an objective to maintain its market leadership position, AlJazira Capital is expanding its brokerage capabilities to offer further value-added services, brokerage across MENA and International markets, as well as offering a full suite of securities business.

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

The purpose of producing this report is to present a general view on the company/economic sector/economic subject under research, and not to recommend a buy/sell/hold for any security or any other assets. Based on that, this report does not take into consideration the specific financial position of every investor and/or his/her risk appetite in relation to investing in the security or any other assets, and hence, may not be suitable for all clients depending on their financial position and their ability and willingness to undertake risks. It is advised that every potential investor seek professional advice from several sources concerning investment decision and should study the impact of such decisions on his/her financial/legal/tax position and other concerns before getting into such investments or liquidate them partially or fully. The market of stocks, bonds, macroeconomic or microeconomic variables are of a volatile nature and could witness sudden changes without any prior warning, therefore, the investor in securities or other assets might face some unexpected risks and fluctuations. All the information, views and expectations and fair values or target prices contained in this report have been compiled or arrived at by Al-Jazira Capital from sources believed to be reliable, but Al-Jazira Capital has not independently verified the contents obtained from these sources and such information may be condensed or incomplete. Accordingly, no representation or warranty, express or implied, is made as to, and no reliance should be placed on the fairness, accuracy, completeness or correctness of the information and opinions contained in this report. Al-Jazira Capital shall not be liable for any loss as that may arise from the use of this report or its contents or otherwise arising in connection therewith. The past performance of any investment is not an indicator of future performance. Any financial projections, fair value estimates or price targets and statements regarding future prospects contained in this document may not be realized. The value of the security or any other assets or the return from them might increase or decrease. Any change in currency rates may have a positive or negative impact on the value/return on the stock or securities mentioned in the report. The investor might get an amount less than the amount invested in some cases. Some stocks or securities maybe, by nature, of low volume/trades or may become like that unexpectedly in special circumstances and this might increase the risk on the investor. Some fees might be levied on some investments in securities. This report has been written by professional employees in Al-Jazira Capital, and they undertake that neither them, nor their wives or children hold positions directly in any listed shares or securities contained in this report during the time of publication of this report, however, The authors and/or their wives/children of this document may own securities in funds open to the public that invest in the securities mentioned in this document as part of a diversified portfolio over which they have no discretion. This report has been produced independently and separately by the Research Division at Al-Jazira Capital and no party (in-house or outside) who might have interest whether direct or indirect have seen the contents of this report before its publishing, except for those whom corporate positions allow them to do so, and/or third-party persons/institutions who signed a non-disclosure agreement with Al-Jazira Capital. Funds managed by Al-Jazira Capital and its subsidiaries for third parties may own the securities that are the subject of this document. Al-Jazira Capital or its subsidiaries may own securities in one or more of the aforementioned companies, and/or indirectly through funds managed by third parties. The Investment Banking division of Al-Jazira Capital maybe in the process of soliciting or executing fee earning mandates for companies that is either the subject of this document or is mentioned in this document. One or more of Al-Jazira Capital board members or executive managers could be also a board member or member of the executive management at the company or companies mentioned in this report, or their associated companies. No part of this report may be reproduced whether inside or outside the Kingdom of Saudi Arabia without the written permission of Al-Jazira Capital. Persons who receive this report should make themselves aware, of and adhere to, any such restrictions. By accepting this report, the recipient agrees to be bound by the foregoing limitations.

Asset Management | Brokerage | Investment Banking | Custody | Advisory

Head Office: King Fahad Road, P.O. Box: 20438, Riyadh 11455, Saudi Arabia, Tel: 011 2256000 - Fax: 011 2256068