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KPJ Healthcare **Patients Flocking Back**

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KPJ expects the recovery in demand for its services, particularly non-Covid-related ones including elective surgeries, to extend into coming quarters which is also likely to surpass our expectation as the pandemic comes to an end. We raise our FY22-23F net profit by 5% each, lift our TP by 8% to RM1.16 (from RM1.02) and reiterate our **OUTPERFORM** call.

We came away from KPJ's 3QFY22 post-results briefing feeling positive. The key highlights are as follows:

1. KPJ expects the recovery in demand for its services to extend into coming quarters which is also likely to surpass our expectation as the pandemic comes to an end. There has been a strong return of domestic patients as well as foreign patients. The group is seeing pent-up demand for elective surgeries with both local and foreign patients returning.

To recap, key operating indicators showed mark improvement in both 9MFY22 and 3QFY22. 9MFY22 earnings were driven by higher patient throughput (+12%), bed occupancy rate (BOR) (of 55% compared to 41% in 9MFY21) and health tourism revenue (+53%) as the group saw a rebound in non-COVID related services including elective surgeries. Generally, its Malaysia operation (which anchors >96% of earnings) registered a higher BOR of 56% against 42% in 9MFY21 as surgeries rose 15%. QoQ, 3QFY22 earnings were driven by higher key operating indicators across the board including BOR (64% vs 43% in 2QFY22), number of surgeries (+22%), inpatients (+59%), outpatients (+13%) and operational beds (+3%).

2. The group is targeting FY22 EBITDA margin at 25% compared to 24% in 9MFY22 vs. our FY22 assumption of 22% and thereafter, 27% in FY23 (vs. our assumption of 22%). Due to better operational efficiencies and overhead absorption rate as a result of incremental revenue underpinned by higher patient throughput, the group expect hospitals under gestation namely KPJ Perlis, KPJ Bandar Dato' Onn and KPJ Batu Pahat to turn EBITDA positive in end 2022 compared to narrowing EBITDA losses in 9MFY22.
3. Damansara Specialist Hospital 2 (DSH2) has been successfully launched in Sept 2022 and is seeing gradual ramp-up in activities. The group aims to ramp up bed capacity from 60-123 beds in year 2023 to 205-265 beds in year 2025. The group is targeting DSH2 to be EBITDA-positive within 3 years by deploying 50% of capacity towards health tourism coupled with offering high revenue intensity services to reduce the gestation period including elective surgeries like neurosurgery, cardiac surgery, gastroenterology & endoscopy procedures and orthopaedics.

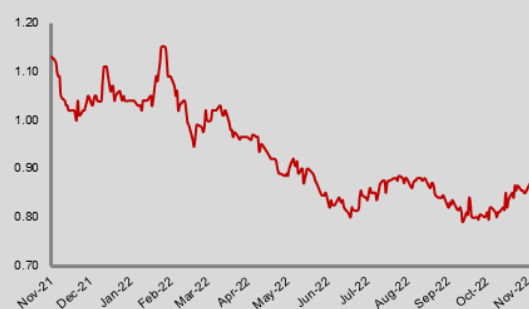
Forecasts. We raise our FY22F-FY23F net profit by 5% each (as we raise our assumption on respective patient throughput from 12-10% to 14-12% and EBITDA margin assumption from 22% to 23%).

We continue to like KPJ for: (i) the low "price elasticity of demand" for healthcare service, which mean players are less vulnerable to high inflation as they could pass on the higher cost, (ii) it being a reopening play, especially for elective surgeries, and (iii) its strong market position locally with the largest network of 28 private hospitals (vs. only 16 of IHH healthcare Malaysia operation in the second place).

OUTPERFORM ↔

Price: **RM0.975**
Target Price: **RM1.16** ↑

Share Price Performance



KLCI 1,486.54
YTD KLCI chg -5.2%
YTD stock price chg -12.2%

Stock Information

Shariah Compliant	Yes
Bloomberg Ticker	KPJ MK Equity
Market Cap (RM m)	4,234.6
Shares Outstanding	4,343.2
52-week range (H)	1.17
52-week range (L)	0.79
3-mth avg daily vol:	1,483,896
Free Float	29%
Beta	0.7

Major Shareholders

Johor Corporation	35.6%
Employees Provident Fund	13.5%
Waqaf An-Nur Corporation	7.1%

Summary Earnings Table

FY Dec (RM m)	2021A	2022F	2023F
Turnover	2,626.8	2,994.6	3,155.6
PBT	115.6	274.0	307.0
Net Profit (NP)	51.0	158.6	176.9
Core NP	51.0	158.6	176.9
Consensus (NP)	-	126.4	162.4
Earnings Revision	-	+5%	+5%
Core EPS (sen)	1.2	3.8	4.3
Core EPS growth (%)	(60.0)	205.7	11.4
NDPS (sen)	0.8	2.0	2.0
BVPS (RM)	0.51	0.53	0.55
PER (x)	78.1	25.8	23.1
Price/BVPS (x)	1.9	1.9	1.8
Net Gearing (%)	70.7	65.2	58.7
Dividend Yield (%)	0.8	2.1	2.1

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We raise our TP by 8% to RM1.16 (from RM1.02) based on 27x FY23F EPS, at a 10% discount to the average of its regional peers to reflect KPJ's smaller market capitalisation. We reduce the discount to 10% from 20% due to KPJ's improving earnings prospects. There is no adjustment to our TP based on ESG given a 3-star rating as appraised by us (see Page 4). **Reiterate OUTPERFORM.**

Key risks to our call are: (i) regulatory risk, (ii) the lack of political will to roll out a national health insurance scheme, and (iii) longer-than-expected gestation periods for its newer hospitals.

Income Statement						Financial Data & Ratios					
FY Dec (RM m)	2019A	2020A	2021A	2022F	2023F	FY Dec	2019A	2020A	2021A	2022F	2023F
Revenue	3,604.4	2,397.4	2,626.8	2,994.6	3,155.6	Growth					
EBITDA	640.6	538.9	529.5	688.8	725.8	Turnover	9.0%	-33.5%	9.6%	14.0%	5.4%
Dep & Amort	(216.2)	(223.3)	(255.3)	(268.3)	(276.3)	EBITDA	28.9%	-15.9%	-1.7%	30.1%	5.4%
Associates	43.9	16.9	25.9	28.6	30.9	Operating Profit	24.2%	-25.5%	-12.3%	69.3%	6.9%
PBT	278.8	150.8	115.6	274.0	307.0	PBT	24.2%	-25.5%	-12.3%	69.3%	6.9%
Taxation	(52.1)	(40.0)	(49.9)	(100.8)	(115.5)	Net Profit /(loss)	22.2%	-47.5%	-53.1%	205.7%	11.4%
MI	(15.3)	(0.4)	(14.6)	(14.6)	(14.6)	Profitability					
Net Profit	211.4	110.4	51.0	158.6	176.9	EBITDA Margin	17.8%	17.1%	19.5%	23.0%	23.0%
Balance Sheet						Operating Margin	13%	10.5%	11.8%	10.0%	14.0%
FY Dec (RM m)	2019A	2020A	2021A	2022F	2023F	PBT Margin	7.7%	6.3%	4.4%	9.1%	9.7%
Fixed Assets	2,598.7	2,863.6	2,676.2	2,708.0	2,731.6	Core Net Margin	5.9%	4.6%	1.9%	5.3%	5.6%
Int. Assets	235.4	235.8	220.0	220.0	220.0	Eff. Tax Rate	32.4%	30.0%	36.0%	37.0%	38.0%
Other FA	1,972.3	1,971.8	2,072.7	2,072.7	2,072.7	ROA	3.5%	1.8%	0.9%	2.6%	2.8%
Inventories	549.6	457.4	481.4	548.8	578.3	ROE	10.9%	5.6%	2.4%	7.3%	7.8%
Receivables	98.0	98.6	115.4	115.4	115.4	DuPont Analysis					
Other CA	478.3	462.2	318.0	387.1	476.1	Net Margin (%)	5.9%	4.6%	1.9%	5.3%	5.6%
Cash	-	-	250.2	250.2	250.2	Assets T/O (x)	1.7	2.6	2.4	2.1	2.1
Total Assets	5,985.8	6,141.4	6,187.6	6,363.4	6,508.8	Lev. Factor (x)	3.2	3.0	2.9	2.9	2.8
Payables	770.5	605.1	618.3	704.8	742.7	ROE (%)	10.9%	5.6%	2.4%	7.3%	7.8%
ST Borrowings	289.5	505.8	860.5	860.5	860.5	Leverage					
Ot. ST Liability	137.9	121.1	101.4	101.4	101.4	Debt/Asset (x)	0.3	0.3	0.3	0.3	0.3
LT Borrowings	1,473.8	1,449.2	968.0	968.0	968.0	Debt/Equity (x)	0.9	1.0	0.9	0.8	0.8
Ot. LT Liability	1,264.9	1,258.0	1,389.0	1,389.0	1,389.0	Valuations					
Minorities Int.	156.4	152.1	115.1	129.7	144.3	EPS (sen)	5.1	2.7	1.2	3.8	4.3
Net Assets	1,892.8	2,050.1	2,135.4	2,210.0	2,302.9	NDPS (sen)	1.83	2.00	0.75	2.00	2.00
Share Capital	906.7	909.5	959.5	959.5	959.5	BVPS (RM)	0.45	0.49	0.51	0.53	0.55
Treasury shares	-	(155.3)	(155.3)	(155.3)	(155.3)	PER (x)	19.2	36.6	78.1	25.8	23.1
Reserves	986.1	1,295.9	1,331.2	1,405.8	1,498.7	Net Div. Yield(%)	1.9	2.1	0.8	2.1	2.1
Equity	1,892.8	2,050.1	2,135.4	2,210.0	2,302.9	P/BV	2.2	2.0	1.9	1.9	1.9
Cashflow Statement						EV/EBITDA (x)	8.4	10.4	10.6	8.0	7.5
FY Dec (RM m)	2019A	2020A	2021A	2022F	2023F						
Operating CF	518.2	590.3	336.7	412.2	423.9						
Investing CF	(453.9)	(444.7)	(248.3)	37.8	(270.4)						
Financing CF	140.8	(310.0)	(134.1)	(393.8)	(36.4)						
Change In Cash	205.1	(164.4)	(45.7)	56.1	117.1						
Free CF	218.2	290.3	36.7	112.2	123.9						

Source: Kenanga Research, Bursa Malaysia

Peer Table Comparison

Name	Rating	Last Price (RM)	Target Price (RM)	Upside (%)	Market Cap (RM'm)	Shariah Compliant	Current FYE	Core EPS (sen)		Core EPS Growth		PER (x) - Core Earnings		PBV (x)	ROE (%)	Net Div. (sen)	Net Div Yld (%)
								1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	2-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.	1-Yr. Fwd.
Stocks Under Coverage																	
IHH HEALTHCARE BHD	OP	6.00	7.20	20.0%	52,836	Y	12/2022	18.6	20.5	2%	11%	32.3	29.2	2.2	7.1%	6.0	1.0%
KPJ HEALTHCARE BHD	OP	0.975	1.16	19.0%	4,235	Y	12/2022	3.8	4.2	211%	12%	25.8	23.1	1.9	7.3%	2.0	2.1%
MALAYSIAN GENOMICS	OP	0.750	1.07	42.7%	93	Y	06/2023	4.6	6.3	-14%	37%	16.4	11.9	2.0	13.9%	0.0	0.0%
RESOURCE CENTRE BHD																	
NOVA WELLNESS GROUP BHD	OP	0.890	1.09	22.5%	283	Y	06/2023	6.7	7.9	20%	18%	13.3	11.3	2.5	19.8%	3.0	3.4%
PHARMANIAGA BHD	MP	0.550	0.510	-7.3%	720	Y	12/2022	5.0	4.7	-62%	-6%	11.1	11.7	1.5	13.9%	2.3	4.2%
Simple Average																	

Source: Company, Bloomberg, Kenanga Research

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Stock ESG Ratings:

	Criterion	Rating				
GENERAL	Earnings Sustainability & Quality	★	★	☆		
	Corporate Social Responsibility	★	★	★		
	Management/Workforce Diversity	★	★	★		
	Accessibility & Transparency	★	★	★		
	Corruption-Free Pledge	★	★	★		
	Carbon-Neutral Initiatives	★	★	☆		
SPECIFIC	Medical waste disposal	★	★	★		
	Usage of biodegradable materials	★	★	★		
	Energy efficiency	★	★	★		
	Product safety	★	★	★	☆	
	Work site safety	★	★	★		
	Staff welfare	★	★	★		
OVERALL		★	★	★		

☆ denotes half-star
 ★ -10% discount to TP
 ★★ -5% discount to TP
 ★★★ TP unchanged
 ★★★★ +5% premium to TP
 ★★★★★ +10% premium to TP

Stock Ratings are defined as follows:

Stock Recommendations

OUTPERFORM : A particular stock's Expected Total Return is MORE than 10%
 MARKET PERFORM : A particular stock's Expected Total Return is WITHIN the range of -5% to 10%
 UNDERPERFORM : A particular stock's Expected Total Return is LESS than -5%

Sector Recommendations***

OVERWEIGHT : A particular sector's Expected Total Return is MORE than 10%
 NEUTRAL : A particular sector's Expected Total Return is WITHIN the range of -5% to 10%
 UNDERWEIGHT : A particular sector's Expected Total Return is LESS than -5%

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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