

12 June 2024

Healthcare

OVERWEIGHT

1QCY24 Report Card: Private Hospitals Stand Out



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The recently concluded 1QCY24 results saw stable sequential earnings delivery (against our expectations) by the sector. Generally, private hospitals under our coverage were in a seasonally low quarter due to the festive holidays. Both IHH (OP; TP: RM7.00) and KPJ (MP; TP: RM1.95) expect patients to return in subsequent quarters. Despite PHARMA's results beating our forecast, it guided for orders to moderate at its medical supply unit in subsequent quarters. Meanwhile, health supplement manufacturers KOTRA and NOVA disappointed as consumers temporarily cut down on purchases amidst weak spending sentiment. Reiterate OVERWEIGHT. Our Top pick for the sector is IHH (OP; TP: RM7.00).

Private hospitals stood out, pharmaceutical players fell behind. This quarter marked a stable sequential earnings delivery against our expectations with 50%/50% coming in within/below our forecasts compared to 20%/80% above/below against the preceding quarter (see table on Page 2). The disappointment came largely from pharmaceutical players. Out of the five companies under our coverage, only **PHARMA (UP; TP: RM0.34)** beat expectation. As for the other four: **IHH** and **KPJ (MP; TP: RM1.95)** met expectations while conversely, **NOVA (OP; TP: RM0.70)** and **KOTRA (OP; TP: RM5.35)** came in below.

- **Private Hospitals**

Seasonally weaker 1QCY24 for private healthcare operators, but generally healthy. Generally, private healthcare players in 1QCY24 under our coverage including **KPJ** and **IHH** were in a seasonally low quarter due to the festive holidays. Both players expect patients to return in subsequent quarters as already seen starting from Apr CY24. **KPJ's** 1QFY24 results met expectations despite the slower festive period that led to patients delaying treatment. 1QFY24 earnings were driven by higher inpatient throughput (+4%), bed capacity (+8%), average revenue per inpatient (+11%) and outpatient (+8%), and surgeries (+1%) despite a lower bed occupancy rate (BOR) of 65% compared to 70% in 1QFY23 and outpatient throughput (-2%). Losses from KPJ's five new hospitals narrowed 30% YoY in 1QFY24. It is optimistic that these hospitals will halve their losses in FY24, driven by incremental revenues from higher patient throughput.

Separately, IHH's 1QFY24 results met expectations with core net profit rising 22% YoY driven largely by lower tax. Its EBITDA eased 2% despite a 16% growth in its top line suggesting that price hikes were outpaced by cost inflation. It has pegged its charges to patients to consumer price index (CPI) across all its key markets. It expects strong patient throughput in Turkey, Singapore and Malaysia after the festive season in 1QFY24.

Outlook. Global healthcare expenditures are projected to reach a total of USD10t by 2026, increasing from USD8.4t in 2022, representing a CAGR of 3.5% during the five-year period (see chart on next page). Amplifying the demand for private healthcare are rising chronic diseases across the globe. Specifically, the WHO reported that almost half of the global healthcare expenditures (USD4t) will be spent on three leading causes of death: (i) cardiovascular diseases, (ii) cancer, and (iii) respiratory diseases.

In 2024, we expect **IHH's** revenue per inpatient growth of 12% to 16% (vs. an estimated 19% in 2023 due to low base effect in 2022), inpatient throughput growth of 9%–12% (vs. an estimated 7% in 2023) and bed occupancy rate (BOR) of 65%–73% (vs. an estimated averaging 65% in 2023) for its hospitals in Malaysia, Singapore, India and Türkiye. IHH expects its earnings momentum to accelerate, underpinned by revenue intensity and rising demand in 2HFY24. It has pegged its charges to patients to consumer price index (CPI) across all its key markets. It expects strong patient throughput in Turkey, Singapore and Malaysia after the festive season in 1QFY24.

We like **IHH** for its pricing power as the inelastic demand for private healthcare services allows providers such as **IHH** to pass on the higher cost amidst rising inflation, and its presence in multiple markets, i.e. Malaysia, Singapore, Türkiye and Greater China.

Similarly, in 2024, we expect **KPJ's** patient throughput to grow at 9% (vs. an estimated 7% in FY23) with BOR at 72% (vs. 67% in FY23), driven by revenue intensity emanating from the recovery in demand for elective surgeries.

We also like **KPJ** for its pricing power as a private healthcare provider and its strong market position locally with the largest network of 28 private hospitals (vs. 16 of the next largest player **IHH**). However, the fundamentals have priced-in the recent run-up in its share price.

• Health Supplements and OTC Drugs

Both KOTRA and NOVA's results missed expectations, while earnings remain resilient. Both KOTRA and NOVA's 9MFY24 results missed expectations: (i) as consumers temporarily held back purchases on weak spending sentiment, and (ii) due to the resulting deterioration of operating scale.

Outlook. Independent market researcher Statista in its consumer market outlook projects the OTC pharmaceuticals market in Malaysia to grow at a CAGR of 6% to an estimated USD715m (RM3.2b) by 2027 as consumers take a more proactive stance towards their health and well-being (including taking health supplements on a regular basis), especially in the aftermath of the Covid-19 pandemic.

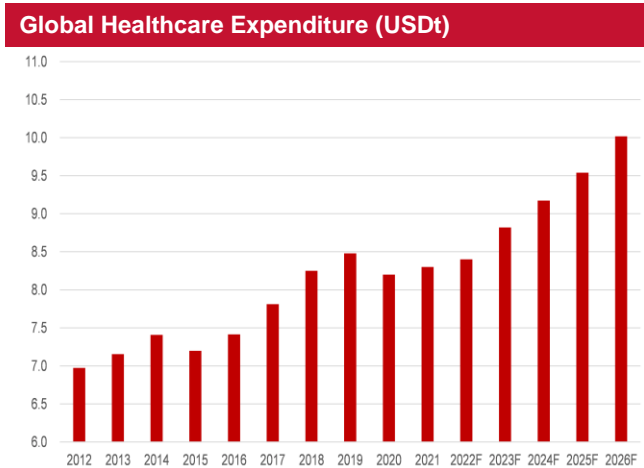
The trend augurs well for **KOTRA** which manufactures and sells OTC supplements and nutritional and pharmaceutical products under key flagship household brands such as *Appeton*, *Axcel* and *Vaxcel*. We also like **KOTRA** for: (i) its integrated business model encompassing the entire spectrum of the pharmaceutical value chain from R&D, product conceptualisation to manufacturing and sales, and (ii) the superior margins of its original brand manufacturing (OBM) business model (vs. low-margin contract manufacturing).

Meanwhile, **NOVA** is ramping up production at its new plant during the year. There is also earnings impact from the introduction of 15-20 new SKUs in FY23 (in addition to 35 in FY22) including skincare products, health supplements, and Activmax and Sustinex range of functional food products such as plant-based protein including specialty Activmax for hospitals. We also like **NOVA** for its business model which encompasses the entire spectrum of value chain from product conceptualisation starting from R&D to manufacturing.

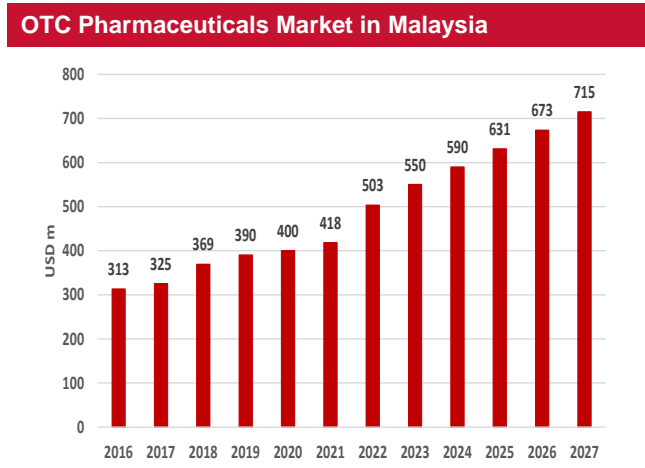
However, the same cannot be said for **PHARMA (UP; TP: RM0.34)** which is still under PN17 status. **PHARMA's** 1QFY24 results beat our forecast. Its 1QFY24 core net profit jumped almost 10-fold on improved sales, efficiency gains and cessation of non-core units. **PHARMA** guided for sustained profitability (after an earnings spike in 1QFY24) with moderate orders for medical supplies under the concession, impact from a price hike in 1QFY24 and better inventory management. Its near-term profitability will be driven by: (i) closure of non-core and non-performing businesses involved in producing supplements and nutraceuticals products, and (ii) efficiency gain through on-going inventory optimisation efforts and aggressive payment collection.

| Quarterly Results Performance | | | | | | | | | | | | | |
|-------------------------------|----------|-----------|-----------|-----------|-----------|-----------|-----------|----------|-----------|-----------|----------|-----------|-----------|
| | 4QCY23 | | | | | | 3QCY23 | | | | | | |
| | KENANGA | | | CONSENSUS | | | KENANGA | | | CONSENSUS | | | |
| | Above | Within | Below | Above | Within | Below | Above | Within | Below | Above | Within | Below | |
| IHH | | 1 | | | 1 | | | | 1 | | | | 1 |
| KPJ | | 1 | | | 1 | | 1 | | | | 1 | | |
| NOVA | | | | 1 | | | | | | 1 | | | 1 |
| KOTRA | | | | 1 | | 1 | | | | 1 | | | 1 |
| PHARMA | 1 | | | | | | | | | 1 | | | 1 |
| Total | 0 | 2 | 2 | 0 | 2 | 1 | 1 | 0 | 4 | 1 | 0 | 4 | 4 |
| Total (%) | 0 | 50 | 50 | 0 | 67 | 33 | 20 | 0 | 80 | 20 | 0 | 80 | 80 |

Source: Kenanga Research, companies quarterly results,



Source: Kenanga Research, WHO, various



Source: Kenanga Research, various

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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. | | | | |
| Stocks Under Coverage | | | | | | | | | | | | | | | | | |
| IHH HEALTHCARE BHD | OP | 6.25 | 7.00 | 12% | 55,044 | Y | 12/2024 | 20.6 | 21.6 | 42% | 5% | 30.3 | 28.9 | 1.8 | 6.1% | 7.0 | 1.1% |
| KOTRA INDUSTRIES BHD | OP | 4.27 | 5.35 | 25% | 633 | Y | 06/2024 | 29.5 | 35.6 | -33% | 21% | 14.5 | 12.0 | 2.0 | 14.9% | 26.0 | 6.1% |
| KPJ HEALTHCARE BHD | MP | 1.96 | 1.95 | -1% | 8,872 | Y | 12/2024 | 6.2 | 6.9 | 7% | 12% | 31.8 | 28.4 | 3.5 | 11.2% | 3.4 | 1.7% |
| NOVA WELLNESS GROUP BHD | OP | 0.535 | 0.700 | 31% | 171 | Y | 06/2024 | 4.1 | 4.7 | -8% | 13% | 13.0 | 11.5 | 1.5 | 11.9% | 3.3 | 6.2% |
| PHARMANIAGA | UP | 0.380 | 0.340 | -11% | 548 | Y | 12/2024 | 3.5 | 3.4 | -35% | -4% | 10.8 | 11.2 | (2.2) | -18.7% | 0.0 | 0.0% |

Source: Company, Bloomberg, Kenanga Research

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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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