

03 January 2018 | Corporate Update

KPJ Healthcare Berhad

Poised to benefit from realignment of business operation

Maintain BUY

Unchanged Target Price: RM1.06

INVESTMENT HIGHLIGHTS

- **Exiting Jeta Garden**
- **Expansion plans on track**
- **Going big in Indonesia**
- **No new greenfield injection into Al-Aqar REIT until FY19**
- **Earnings forecasts maintained**
- **Maintain BUY with an unchanged TP of RM1.06 per share**

Exiting Jeta Garden. KPJ Healthcare disclosed in our recent meeting with the management that it is in an advance stage of disposing Jeta Garden, its aged care center in Australia. According to management, it is currently in the midst realigning its operation to focus on delivering medical services. Jeta Garden will be sold at net tangible asset (NTA) value and the proceeds will be recognised as a gain on disposal. We understand that the disposal will only be completed by first half of FY18 following an EGM in February 2018. Therefore, Jeta Garden will still be consolidated in FY17.

Expansion plan on track. We understand from the management that KPJ Perlis which is slated to be completed in December 2017 is now waiting for the clearance from Ministry of Health (MOH). It will be ready for operation sometime in January 2018. As for the rest of its expansion plan, the hospitals that are expected to be opened after KPJ Perlis in FY18-19 would be KPJ Bandar Dato' Onn (BDO) in Johor, KPJ Kuching, KPJ Miri and expansion of KPJ Sabah.

Going big in Indonesia. Despite the intricacies of operating in the Indonesian market, management of KPJ is planning to expand its footprint in Indonesia in the medium to long term. Management believes that there is still value in Indonesia which is home to 255m population as its gross margins in Indonesia remains high at 45% when compared against gross margins in Malaysia which tend to be in the tune of about 38-40%. Indonesia remains in KPJ's interest due to its lower labour costs and plenty of underserved areas. Also, by targeting to operate in cities outside of Jakarta which are underserved it will also avoid from competing head-on with Indonesia's private healthcare service providers such as: Mitra Keluarga Karyasehat (NR) and Siloam Hospitals (NR) in terms of getting medical doctors to practise in the hospital.

RETURN STATS	
Price (2 January 2018)	RM0.98
Target Price	RM1.06
Expected Share Price Return	+8.2%
Expected Dividend Yield	+2.0%
Expected Total Return	+10.2%

STOCK INFO	
KLCI	1,782.7
Bursa / Bloomberg	5878 / KPJ MK
Board / Sector	Main / Trading Services
Syariah Compliant	YES
Issued shares (mil)	4,264.73
Market cap. (RM'm)	4,179.43
Price over NA	2.49
52-wk price Range	RM0.90 – RM1.14
Beta (against KLCI)	0.45
3-mth Avg Daily Vol	1.15m
3-mth Avg Daily Value	RM1.15m
Major Shareholders (%)	
Johor Corporation	43.61
EPF	12.69
Waqaf An-Nur Corp	7.14

No new greenfield injection into Al-Aqar REIT until FY19. We understand from the management that there will be no new injection of greenfield hospitals into Al-Aqar REIT until FY19 as the company is trying to exhaust its reinvestment allowance tax on newly built greenfield hospitals. However, management mentioned that there is potential that KPJ will inject the expansions on matured existing hospitals that have been completed instead from FY18 onwards.

Table 1: Potential injection into Al-Aqar REIT

FY18 onwards	FY19 onwards
KPJ Selangor (Carpark)	KPJ Pasir Gudang
KPJ Seremban (Extension)	KPJ Sabah
	KPJ Bandar Maharani
	KPJ Rawang
	KPJ Selangor (Consultant Suite)

Source: Company, Forecasts by MIDFR

Earnings forecast. We are making no changes to our forecasts at this juncture as we opine that KPJ is on track to meet our earnings projections.

Maintain BUY with an unchanged Target Price (TP) of RM1.06. All factors considered, we reiterate our **BUY** recommendation on KPJ with a SOP-based TP of **RM1.06** per share (TG: 3.0%, WACC: 7.84%) per share. We are positive on the fact that KPJ has decided to exit Jeta Garden as we opine that the business has remained loss making since it was acquired back in 2010 and is showing no sign of turning around anytime soon. This is despite the continuous effort by the Management to turn around the operation including adding more capacity to the facility in 2015. Furthermore, we believe that the Management will be able to use the proceeds from the disposal to pare down debts (c.0.71x) and reinvest in expanding existing hospitals which will benefit KPJ in the future.

Going forward, we opine that growth will continue to be driven by higher contribution from newly opened hospitals as well as improvements in contribution coming from its more matured hospitals. We also view that the improving Ringgit against USD will bode well for KPJ as it will reduce the volatility and the cost of medical consumables which in turn will result in higher profitability. Furthermore, we opine that there will be a new round of price revision exercise that will take place early next year which will assist in revenue growth for FY18 given the absence of price revisions this year. 

Table 2: KPJ Healthcare's capacity expansion plan (Greenfield)

Project	Location	Total Capacity (beds)	First Phase (beds)	Completion	Opening
Perlis	Perlis	90	60	3Q2017	4Q2017
Kuching	Sarawak	150	114	2Q2018	3Q2018
Miri	Sarawak	96	61	1Q2018	2Q2018
Bandar Dato' Onn	Johor	150	90	1Q2018	2Q2018
UTM	Johor	150	90		TBA
Nilai	Negeri Sembilan	96	61		TBA
Bayuemas, Klang	Selangor	90	90		TBA

Source: Company

Table 3: KPJ Healthcare's SOP valuation

Items	RM'm	Remarks
KPJ Enterprise value	5,328.7	DCF method, WACC: 8.32%, TG: 3%
Net debt FY18	1,103.4	
KPJ firm value	4,225.3	
KPJ Al-Aqar REIT	470.4	Based on KPJ's 38% stake and consensus TP: RM1.70
Total KPJ firm value	4,695.7	
Proceeds from warrants	355.8	
Cash proceeds from rights and warrants	5,051.6	
No.of shares (m)	4,760.0	
KPJ value per share	1.06	

Source: Forecasts by MIDFR

INVESTMENT STATISTICS

FYE Dec (RM'm)	FY2014	FY2015	FY2016	FY2017F	FY2018F
Revenue	2,639.1	2,847.6	3,021.1	3,533.0	3,882.8
Cost of sales	(1,869.7)	(2,021.2)	(2,123.1)	(2,433.5)	(2,646.1)
Gross profit	769.4	826.4	898.0	1,099.5	1,236.7
Finance costs	(42.9)	(50.4)	(83.1)	(72.9)	(77.2)
Profit before tax and zakat	218.1	209.6	210.2	223.1	288.5
Income tax expense	(68.6)	(62.2)	(50.5)	(61.7)	(84.0)
Net Profit	147.3	145.1	155.9	149.7	189.6
PBT Margin (%)	8.3	7.4	7.0	6.3	7.4
Net Profit Margin (%)	5.6	5.1	5.2	4.2	4.9
EPS (sen)	3.5	3.2	3.3	3.1	4.0
EPS Growth (%)	33.9	-9.1	2.5	-4.0	26.7
PER (x)	27.9	30.7	29.9	31.2	24.6
Dividend per share (sen)	4.9	7.9	1.6	1.6	2.0
Dividend yield (%)	5.0	8.0	1.6	1.6	2.0
Tax rate (%)	31.4	29.7	24.0	27.7	29.1

Source: Company, Forecasts by MIDFR

DAILY PRICE CHART



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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <10% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.