

SECTOR UPDATE

Healthcare – Malaysia

Defensive Position Is Unappealing For Now

Maintain MARKET WEIGHT on the healthcare sector. Despite tepid inpatient volume growth, hospitals' positive operating leverage is expected to boost earnings by 12.4% and 10.9% in 2024-25 respectively, though current valuations are lofty at 32.5x PE. Alpha IVF, with its impressive regional expansion, and Duopharma, poised for recovery after a challenging 2023, present more alluring prospects. However, amid a risk-on environment, we TACTICALLY UNDERWEIGHT healthcare, anticipating relative underperformance. Our top picks are Alpha IVF and Duopharma.

WHAT'S NEW

- **Structural uptrend in margins as expansion approach shifts to brownfield.** Both IHH Healthcare (IHH) and KPJ Healthcare (KPJ) are largely pursuing a brownfield approach to their expansions ahead, a shift from their greenfield expansions in the past. Brownfield expansions typically reach breakeven in half the time required for greenfield expansions. There is also significantly less risk as a brownfield expansion is merely an extension of a proven fully-gestated hospital as opposed to venturing into a new catchment area. For example, KPJ's four loss-making hospitals (Bandar Dato's Onn, Miri, Batu Pahat, Perlis) have been incurring losses for more than three years. As IHH and KPJ undergo the shift, their margins should see a structural uptrend. KPJ has indicated that its five-year EBITDA target is 28% vs 2023's 22%. IHH's blended hospital EBITDA margin is 22%, which should improve to the likes of its more mature markets, Malaysia or Singapore operations, which command 26% and 29% respectively.
- **Alpha IVF: From breakeven to profitability with Alhaya.** Alpha IVF's new facility, Alhaya, is situated within KPJ's flagship, the premium health tourism-oriented Damansara Specialist Hospital 2. Early signs are promising, with Alhaya already breaking even within its first month of operations and has continued its momentum since. At this juncture, we have conservatively assumed for Alhaya to contribute 0.5% and 4.1% of Alpha IVF's total group patient volume for FY24-25 respectively. Alhaya's contribution may currently be small but it is reflective of Alpha IVF's group fertilisation and pregnancy rates (proven true thus far).

ACTION

- **Maintain MARKET WEIGHT on the healthcare sector.** While domestic inpatient volume growth is not particularly exciting, the impact to earnings is meaningful given hospitals' positive operating leverage. In view of this and KPJ's corporate restructuring and turnaround efforts, the hospital segment is expected to grow earnings by 12.4%/10.9% in 2024-25 respectively. However, valuations are trading at 32.5x, close to the five-year mean PE. Alpha IVF and Duopharma offer more appealing opportunities. Alpha IVF has exhibited high levels of proven execution and is undertaking exciting regional expansions while Duopharma is expected to see a recovery following a challenging 2023.

Given that the hospitals are the heavyweights in the sector, they anchor our MARKET WEIGHT on the healthcare sector but we TACTICALLY UNDERWEIGHT it as amid an anticipated risk-on environment, interest may swing towards higher beta sectors or other deep value sectors and the healthcare sector is likely to underperform on a relative basis. Alpha IVF and Duopharma are our top picks for the sector.

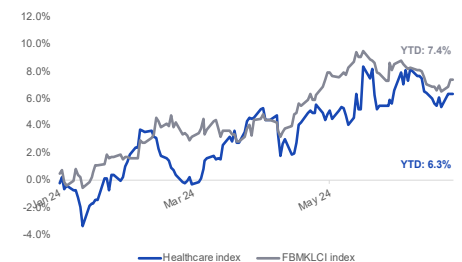
REGIONAL PEER COMPARISON

Name	Ticker	Rec	Currency	Price @ 3 Jul 24 (Icl)	Target Price (Icl)	Mkt Cap (US\$m)	----- PE (x) -----	--- EV/EBITDA (x) ---	Div Yield (%)	P/B (x)		
							2024F	2025F	2024F	2024F		
BKK. Dusit	BDMS TB	BUY	THB	26.00	32.00	11251	24.2	22.8	15.1	14.3	3.2	4.2
IHH Healthcare	IHH MK	HOLD	RM	6.33	6.40	11771	39.0	35.2	19.4	18.5	0.8	1.8
Bumrungrad Hosp	BH TB	HOLD	THB	246.00	235.00	5429	35.6	33.9	21.8	20.8	1.5	8.3
Raffles Medical	RFMD SP	HOLD	SGD	1.02	1.15	1341	23.8	22.1	10.3	9.7	2.0	1.7
BKK. Chain Hosp.	BCH TB	HOLD	THB	17.00	17.30	1161	28.0	24.9	14.1	12.9	1.8	3.2
KPJ Healthcare	KPJ MK	HOLD	RM	1.93	1.78	1796	30.4	27.4	11.0	10.4	1.6	3.5
Regional hospitals avg						5463	30.2	27.7	15.3	14.4	1.8	3.8
APEX Healthcare	APEX MK	NR	RM	2.84	n.a.	432	23.6	17.4	13.5	12.9	2.0	2.4
Alpha IVF	ALPHA MK	BUY	RM	0.31	0.40	320	23.5	21.3	14.3	12.4	2.6	7.0
Duopharma	DBB MK	BUY	RM	1.25	1.39	255	15.4	13.1	9.3	8.3	2.6	1.6
Malaysia healthcare avg						336	20.8	17.3	12.4	11.2	2.4	3.7

Source: Bloomberg, UOB Kay Hian

MARKET WEIGHT (Maintained)

HEALTHCARE INDEX VS FBMKLCI INDEX



Source: Bloomberg, UOB Kay Hian
Healthcare Index is an equal weighted index consisting of IHH Healthcare, KPJ Healthcare, Duopharma Biotech, Pharmanlaga, Apex Healthcare, Kotra Industries, Optimax, Cengild Medical and DC Healthcare, YSP Southeast Asia, TMC Life Sciences

SECTOR PICKS

Company	Rec	Share Price (RM)	Target Price (RM)
Alpha IVF	BUY	0.31	0.40
Duopharma	BUY	1.25	1.39
KPJ	HOLD	1.94	1.78
IHH	HOLD	6.33	6.40

Source: UOB Kay Hian

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ESSENTIALS

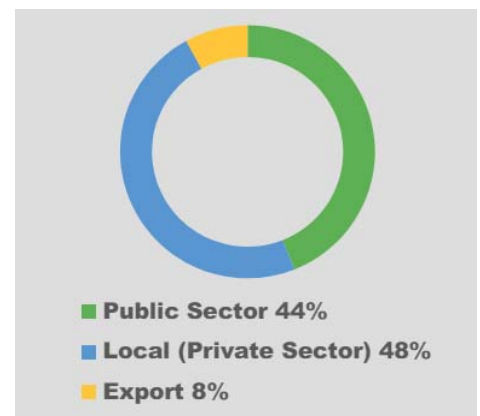
- KPJ is embarking on a foreign patient recruitment drive.** KPJ generated RM200m from foreign patients in 2023. Healthcare tourists and foreign expatriates made equal contributions. The latter is due to see exponential growth with management targeting an ambitious 50-75% yoy growth for 2024. KPJ looks to engage agencies in Indonesia and Bangladesh to drive health tourism. It carries limited risk seeing that these agencies are compensated based on a finder's fee. A relatively weak ringgit has also shifted some preference to Malaysia vis-à-vis Singapore and has thereby aided the gestation of the likes of KPJ Bandar Dato' Onn. KPJ had also appointed Sherene Azli as the group's new Chief Marketing Officer in Nov 23. She was previously the CEO of the Malaysia Healthcare Travel Council (MHTC) for six years. MHTC is the national agency under the purview of the Ministry of Health, tasked to promote Malaysia's healthcare travel industry.
- Carving out own niche, easing perception of heightened competition.** Sunway Healthcare appears relatively aggressive with its hospital rollout. However, we note that: a) the catchment area of Sunway Healthcare's hospitals does not coincide with a KPJ hospital (Seberang Jaya and Ayer Itam in Penang), or b) the catchment area is well populated to be supportive of new hospitals (Ipoh). Furthermore, locations such as Kota Bharu (Kelantan) that fall beyond the aforementioned categories would coincide with KPJ's mature hospitals that typically retain habitual or repeat patients. In addition, Sunway Healthcare's positioning could appeal to a different segment of patients. Given these factors, the ramp-up of Sunway Healthcare's hospitals is unlikely to significantly disrupt the landscape for IHH and KPJ.
- Duopharma unaffected by Pharmaniaga's PN17 status.** Pharmaniaga was classified under Practice Note 17 of the Main Market Listing Requirements of Bursa Malaysia in Feb 23. This was due to its core business' failure to meet the minimum requirements for capital or equity and its shareholders' funds. Positively, its financial status has not impacted Pharmaniaga's logistics and distribution role for the government. Neither the government's reordering of pharmaceutical supplies nor payments has been affected, as reaffirmed by Duopharma as a supplier of pharmaceuticals to the government through Pharmaniaga. Duopharma has taken proactive measures, securing sufficient borrowing facilities to cover three months' worth of working capital tied to Pharmaniaga, in the event payments are deferred (public sector sales account close to 50% of Duopharma's revenue).
- Our preferred pick is Alpha IVF (ALPHA MK/BUY/ RM0.40).** We like Alpha IVF for its: a) superior three-year earnings CAGR (FY23-26) outlook of 19.0%, ahead of its peers' average of 13.4%; b) attractive growth and palatable valuations, as well as leading clinical success rates in the region; and c) far superior average profit margin of 32.0% for FY24-26, which is more than double the average of its regional peers (15.3%) and well ahead of the next highest margin (23.7%). Alpha IVF's new fertility clinic launched in April has already broken even and achieved similar fertility success rates as the group's, reflecting Alpha IVF's ability to replicate its successes with its expansions. Our target price is pegged to 28.0x FY25F PE, a 20% premium to its peers trading at a historical 22.8x 2025F PE.
- IHH Healthcare and Sunway Healthcare vying for hospital in Penang.** Based on a media report, Island Hospital in Penang is said to have attracted IHH Healthcare and Sunway Healthcare as potential buyers. Island Hospital is a mere 2km away from IHH's Gleneagles Hospital in Penang. Both are fully mature hospitals, but they appear to serve distinct segments of the market. Based on the reported price tag of RM4b and an EBITDA of RM200m, it could enhance IHH's 2025 EBITDA by 5.7%. However, its PAT margins are unknown. Factoring in forgone interest income and/or additional incurred interest cost to fund the RM4b, the overall impact on IHH's 2025 earnings appears insignificant by our estimates.

LITTLE OVERLAP IN CAPTIVE AREAS OF SUNWAY HEALTHCARE'S HOSPITALS VS IHH AND KPJ

Sunway Healthcare's hospitals (existing and new)	within 5km proximity
Sunway City (Selangor)	
Sunway Velocity (Kuala Lumpur)	IHH
Seberang Jaya (Penang)	
Kota Damansara (Kuala Lumpur)	
Paya Terubong (Penang)	
Ipoh (Perak)	Possible KPJ
Kota Bharu (Kelantan)	Possible KPJ
Iskandar Puteri (Johor)	

Source: Sunway Healthcare, IHH, KPJ

DUOPHARMA'S REVENUE BREAKDOWN. PUBLIC SECTOR SALES COLLECTIONS ARE DEPENDENT ON PHARMANIAGA.



Source: Duopharma

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