

### SECTOR UPDATE

## Healthcare – Malaysia

Lacking Compelling Catalysts

We expect increased allocation to the MoH in Budget 2024 albeit at a tempered rate given other pressing priorities. Over the longer term, structural reforms as outlined by the HWP should significantly integrate both the private and public sectors, but it should not detrimentally affect the former's financial prospects. Sector earnings should recover in 2024 but there is a lack of compelling catalysts. Maintain MARKET WEIGHT. Top pick: KPJ Healthcare.

### WHAT'S NEW

- Budget review.** Budget 2023 saw an increased 12% yoy allocation to the Ministry of Health (MoH) at RM36.3b (Budget 2022: RM32.4b). It accounted for 9.4% of the total budget of RM388b and was the second-largest allocation in the federal budget. However, this would position public sector current health expenditure as a percentage of GDP at close to ~2.0%, which is relatively low compared to the 4.4% spent by upper-middle income countries (UMIC) and 6.4% of high-income countries (HIC).
- Budget 2024 likely tempered with cost-of-living priority.** Given the rising burden of non-communicable diseases and Malaysia increasingly becoming an ageing nation, there have been calls from various parties for an increased emphasis and budget allocation towards healthcare by drawing public sector health expenditure as a percentage of GDP closer to 5%. However, the government has highlighted that Budget 2024's priority is to address the cost of living. This may rein in public sector healthcare allocation, an increment but throttled down from the 12% yoy growth seen in 2023.
- Government contracts likely unaffected with bidding done on tender basis.** Development expenses may be at risk with core recurring operating expenses already accounting for 87% of 2023's public sector allocation. Of this, primary spending was for the procurement of medicines, vaccines and consumables. Naturally, the tender of government pharmaceutical contracts that expired on 30 Jun 23 is put into question. However, we highlight that these contracts are bid on an open tender basis and already extracting competitive rates for the government. Given this premise, there should not be increased risk for the likes of Duopharma. Government contract tenders are expected to be awarded in 4Q23.

### ACTION

- Maintain MARKET WEIGHT.** The hospital subsector's 2023 earnings are projected to contract by 1.1% following the moderation of COVID-19-related contributions. Growth should resume in 2024 with an earnings growth of 10.9%. This is against the backdrop of the subsector's valuations trading below -1.5SD to its five-year PE mean. However, the sector lacks compelling catalysts at this juncture, which underpins our MARKET WEIGHT on the sector. Our top pick is KPJ and we like it for its bargain valuations, its intention to divest its loss-making regional operations, and the conclusion of its greenfield expansion that allows for realisation of its positive operating leverage.

### REGIONAL PEER COMPARISON

Name	Ticker	Rec	Currency	Price @ 22 Sep 23 (lc)	Target Price (lc)	Mkt Cap (US\$m)	PE (x) 2023F	PE (x) 2024F	EV/EBITDA (x) 2023F	EV/EBITDA (x) 2024F	Div Yield (%) 2023F	P/B (x) 2023F
BKK. Dusit	BDMS TB	BUY	THB	26.25	33.00	11582	30.8	29.2	17.8	17.1	2.3	4.4
IHH Healthcare	IHH MK	HOLD	RM	5.96	6.40	11194	40.5	36.9	18.3	17.7	0.8	1.9
Bumrungrad Hosp	BH TB	HOLD	THB	265	235.00	5848	40.0	38.1	24.6	23.5	1.3	9.3
Raffles Medical	RFMD SP	BUY	SGD	1.24	1.70	1691	21.1	22.6	11.4	12.2	2.8	2.2
BKK. Chain Hosp.	BCH TB	HOLD	THB	19.6	17.30	1357	36.6	32.1	17.8	16.3	1.4	4.0
KPJ Healthcare	KPJ MK	BUY	RM	1.19	1.40	1108	22.2	19.0	8.4	7.7	2.2	2.3
<b>Regional hospitals avg</b>						<b>5463</b>	<b>31.9</b>	<b>29.7</b>	<b>16.4</b>	<b>15.8</b>	<b>1.8</b>	<b>4.0</b>
APEX Healthcare	APEX MK	NR	RM	2.50	n.a.	383	18.8	17.0	12.6	11.9	2.4	2.2
Duopharma	DBB MK	BUY	RM	1.20	1.59	246	17.2	12.6	10.8	8.2	1.7	1.6
Pharmaniaga	PHRM MK	NR	RM	0.45	n.a.	137	16.5	17.1	13.1	12.3	1.8	-4.0
<b>Malaysia pharma avg</b>						<b>255</b>	<b>17.5</b>	<b>15.6</b>	<b>12.2</b>	<b>10.8</b>	<b>2.0</b>	<b>-0.1</b>

Source: Bloomberg, UOB Kay Hian

## MARKETWEIGHT (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, Pharmaniaga, 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)
KPJ	BUY	1.19	1.40
Duopharma	BUY	1.20	1.59
IHH	HOLD	5.96	6.40

Source: UOB Kay Hian

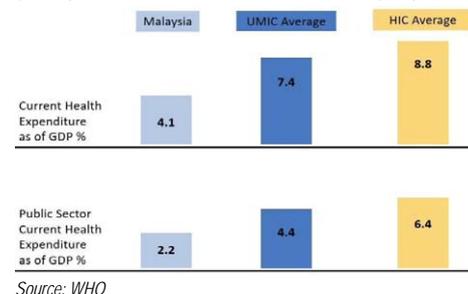
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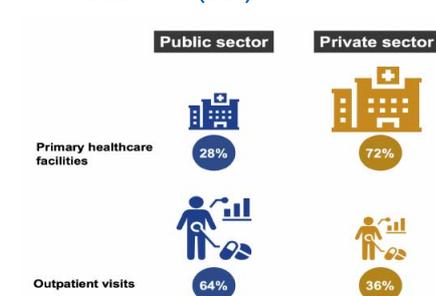
ESSENTIALS

- HWP implications for the private sector.** Recently, the MoH proposed a reform of the health system in Malaysia with its Health White Paper (HWP). This is to address the health system, particularly the public healthcare system that is overstretched, overburdened and dated. Among the comprehensive multi-pronged approach, we only highlight those relevant to the private sector, in the interest of IHH Healthcare and KPJ Healthcare. The HWP looks to enhance public and private partnerships to help balance resource utilisation across both sectors. Procurement of hospital care services from the private sector will be progressively and strategically implemented.
- Neutral to positive impact, depending on benefit package.** KPJ's Damansara Specialist Hospital 2 (DSH2) is an example, receiving decanted patients from the public sector for non-COVID-19-related operations. Expanding on this, HWP proposed to develop a benefit package that outlines a specific set of services and medications across primary healthcare up to hospital care for a standard set of affordable fees across both the public and private sectors. Indonesia had enacted a similar policy with its National Health Insurance to implement universal health coverage in 2014. Depending on the standardised rate, the impact is likely neutral to positive to the private hospitals in Malaysia and more so for the likes of KPJ which is geographically dispersed with ample capacity.
- Tangible effects of the HWP likely only to be realised at least five years from now** as the initial stage (1-5 years) is focused on pilot programmes and legislative amendments. Only over the medium- to long-term horizon will there be better coordination across the public and private sectors so that they are less fragmented, allowing service standards to achieve more balanced quality and performance levels.
- 1H23 results were largely disappointing but hospital operators should see a better 2H23.** Both IHH Healthcare (IHH) and Duopharma's 1H23 earnings have been curtailed by lower margins and normalising COVID-19 contributions which were also margin accretive weighed earnings. In addition, IHH's Acibadem operations were affected by the sharply depreciating Turkish lira. Meanwhile, KPJ's earnings came in broadly in line. Over 2H23, we expect for hospital operators' (IHH and KPJ) earnings to come in stronger vis-à-vis 1H23 following the full normalisation of the Turkish lira impact on Acibadem for the former and better gestation of hospitals for the latter. Contrastingly, headwinds are expected to persist for Duopharma with lacklustre public sector sales.
- Our preferred pick is KPJ Healthcare (KPJ MK/BUY/Target: RM1.40).** Our target price is based on 10.0x EV/EBITDA, a 30% discount to regional peers', and implies 22.4x 2024F PE. We are encouraged by KPJ's reorganisation of its loss-making regional operations, which paves the way for improved earnings visibility. In addition, KPJ has completed its greenfield expansion, which allows for a healthier balance sheet and realisation of its positive operating leverage. KPJ's valuations are also undemanding.

CURRENT HEALTH EXPENDITURE AS % OF GDP, MALAYSIA VS UPPER MIDDLE INCOME COUNTRIES (UMIC) AND HIGH INCOME COUNTRIES (HIC)



IMBALANCE OF FACILITIES RELATIVE TO OUTPATIENT VISITS BETWEEN THE PUBLIC AND PRIVATE SECTORS (2020)



KPJ: HISTORICAL PE BAND (PRE-PANDEMIC)



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