

DaVita Inc. (DVA)

\$82.92 (As of 08/05/20)

Price Target (6-12 Months): **\$95.00**

Long Term: 6-12 Months

Zacks Recommendation:
Outperform

(Since: 07/07/20)

Prior Recommendation: Neutral

Short Term: 1-3 Months

Zacks Rank: (1-5)

1-Strong Buy

Zacks Style Scores:

VGM:A

Value: A

Growth: B

Momentum: B

Summary

DaVita ended the second quarter on a mixed note as earnings beat but revenues missed estimates. The significant improvement in the bottom line is encouraging. Solid prospects in the Kidney Care wing aid the stock. Dialysis services in the United States showcased solid results during the quarter and improved overseas. The acquisition of several dialysis centers overseas is encouraging. Net dialysis and related lab patient service revenues saw an uptick in second quarter. A solid guidance for 2020 is another positive. The company continues gaining from the DaVita Venture Group. Over the past year, shares of DaVita have outperformed its industry. However, foreign exchange headwinds and stiff competition continue to weigh on the company. The declining profitability of calcimimetics is a dampener.

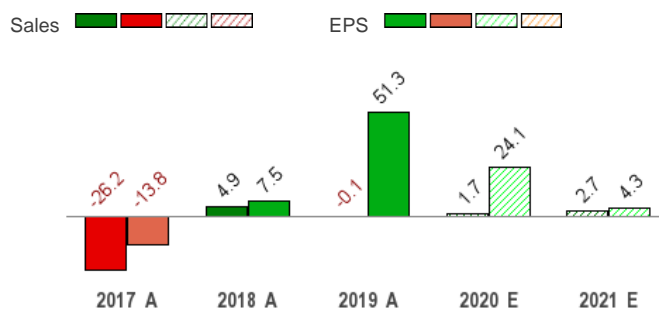
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$92.16 - \$53.51
20 Day Average Volume (sh)	836,750
Market Cap	\$10.1 B
YTD Price Change	10.5%
Beta	1.23
Dividend / Div Yld	\$0.00 / 0.0%
Industry	Medical - Outpatient and Home Healthcare
Zacks Industry Rank	Top 33% (84 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	51.2%
Last Sales Surprise	-1.1%
EPS F1 Est- 4 week change	9.2%
Expected Report Date	11/03/2020
Earnings ESP	0.0%
P/E TTM	11.6
P/E F1	12.4
PEG F1	0.6
P/S TTM	0.9

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021	2,886 E	2,930 E	2,998 E	3,011 E	11,891 E
2020	2,841 A	2,880 A	2,937 E	2,950 E	11,576 E
2019	2,743 A	2,843 A	2,904 A	2,899 A	11,388 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021	\$1.60 E	\$1.71 E	\$1.75 E	\$1.78 E	\$6.99 E
2020	\$1.83 A	\$1.95 A	\$1.42 E	\$1.51 E	\$6.70 E
2019	\$0.91 A	\$1.22 A	\$1.53 A	\$1.86 A	\$5.40 A

*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 08/05/2020. The reports text is as of 08/06/2020.

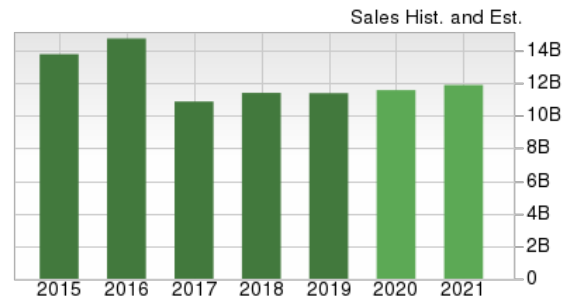
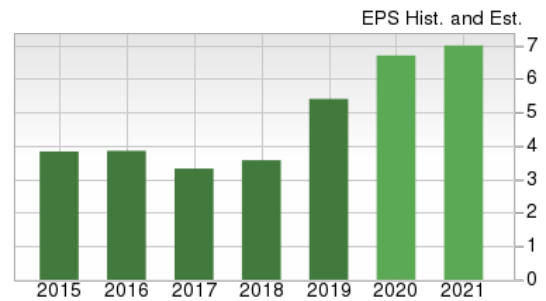
Overview

Founded in 1994 and headquartered in Denver, CO, **DaVita Inc.** is a leading provider of dialysis services in the U.S. to patients suffering from chronic kidney failure, also known as end stage renal disease (ESRD). The company operates kidney dialysis centers and provides related medical services primarily in dialysis centers and in contracted hospitals across the U.S. Its services include outpatient dialysis services, hospital inpatient dialysis services and ancillary services such as ESRD laboratory services and disease management services.

DaVita's Dialysis and related lab services business segment provides inpatient as well as outpatient dialysis services, routine laboratory testing for ESRD patients and management services to outpatient dialysis centers.

The company's other ancillary services and strategic initiatives segment includes its international dialysis services, pharmacy services, infusion therapy services, disease management services, vascular access services, ESRD clinical research programs and physician services.

For investors' notice, the company's major segment — DaVita Medical Group ("DMG") — has been divested to Optum, a subsidiary of UnitedHealth Group Inc. for a deal value of \$4.3 billion. The results of DMG business' operations have been reported as discontinued.



2019 at a Glance

The company's 2019 revenues totaled \$11.39 billion.

DaVita's Net Dialysis Services revenues for 2019 were \$10.90 billion (95.7% of net revenues), while Other revenues totaled \$491,773 (0.3%).



Reasons To Buy:

- ▲ **Shares Up:** Over the past year, shares of DaVita have rallied 38.8% compared with the industry's 3.7% rise. DaVita is set to gain significantly from dialysis services in 2020 and hence has maintained its impressive revenue guidance for the year. Also, solid prospects in the Kidney Care wing aids the stock.
- ▲ **DaVita Kidney Care:** DaVita Kidney Care, the major revenue-generating segment of DaVita, specializes in a broad array of dialysis services, thereby significantly contributing to the company's topline.

DaVita's incessant efforts to upgrade services, global expansion initiatives and active acquisitions remain impressive and are supported by the company's strong financial position.

As an operating division of DaVita, DaVita Kidney Care focuses on setting worldwide standards for clinical, social and operational practices in kidney care. DaVita saw solid results from the Kidney Care business. Of the major services that DaVita provides, the company's in-center hemodialysis, home hemodialysis, peritoneal dialysis, kidney transplant, urology, diabetology and vascular access surgery deserve a mention.

Net dialysis and related lab patient service revenues in the second quarter totaled \$2.76 billion, up 1.1% on a year-over-year basis. Per management, total U.S. dialysis treatments for the second quarter were 7,570,908, or an average 97,063 treatments per day. This represents a per-day increase of 0.7% on a year-over-year basis.

Through the second quarter, DaVita Kidney Care segment continued delivering strong performance beginning with treatment of Chronic Kidney Disease (CKD) all the way through End Stage Renal Disease (ESRD) and transplant.

In May 2020, DaVita launched the DaVita Venture Group (DVG), through which it plans to accelerate efforts to develop and deploy solutions aimed at improving the health care and quality of life for patients of kidney disease and related chronic conditions.

DaVita Kidney Care also provides support to nephrologist-led organizations like Nephrology Care Alliance (NCA) in their endeavor to treat patients of chronic kidney disease.

- ▲ **Guidance Impressive:** DaVita has reaffirmed the 2020 revenue range at between \$11.50 billion and \$11.70 billion. Adjusted EPS projection has been updated to the range of \$6.25-\$6.75 compared with the previously-issued \$5.75-\$6.25. Adjusted operating income margin is estimated in the band of 14-14.75% (up from the prior-guided range of 13-14%). This is likely to raise optimism in the stock and favor it in the near term.
- ▲ **DMG Divestment:** For investors' notice, DaVita recently completed the divestment of the DaVita Medical Group division to Optum, a subsidiary of UnitedHealth Group, for a deal value of \$4.34 billion. It is encouraging to note that the company used the full \$4.47 billion in preliminary net proceeds received at closing to repay its outstanding debt.
- ▲ **Acquisition of Dialysis Centers:** Acquiring dialysis centers and businesses that own and operate dialysis centers as well as other ancillary services is DaVita's preferred business strategy. These strategies have boosted the company's top line to a large extent.

DaVita's Kidney Care Business has opened a 150,000 square-foot campus for DaVita Labs, its diagnostic laboratory that serves DaVita dialysis clinics and their patients. In the recent past, DaVita HealthCare Partners also announced that HealthCare Partners, a unit within its medical group, has entered into a strategic partnership with Cigna, a global health insurance service company.

As of Jun 30, 2020 the company provided dialysis services to a total of approximately 236,800 patients at 3,082 outpatient dialysis centers, of which 2,795 centers were located in the United States and 287 centers in 10 other countries.

During the second quarter, DaVita opened a total of 28 new dialysis centers and acquired one in the country. It also took over three dialysis centers and opened two outside the United States.

- ▲ **Overseas Growth:** DaVita is steadily expanding in the international markets. In the past few years, the company has strengthened its position in the emerging and developing markets of Brazil, China, Colombia, Germany, India, Malaysia, Netherlands, Poland, Portugal and Saudi Arabia through strategic alliances as well as acquisitions of dialysis centers.

These are expected to help DaVita deliver more efficient patient care. Currently, DaVita is seeking to expand in major European and Asian countries via acquisitions and partnerships.

- ▲ **Stable Solvency Position:** DaVita exited the second quarter with cash and cash equivalents of \$3.19 billion, higher than \$1.49 billion in the preceding quarter. Meanwhile, the company's long-term debt totaled \$10.6 billion in the second quarter, down sequentially from \$11.18 billion. Although the quarter's long-term debt was much higher than the corresponding cash and cash equivalent level, the current debt level of \$2.27 billion, which is substantially higher than \$502 million in the preceding quarter, lags the company's short-term cash level. This is particularly good when it comes to the company's solvency position as at least during the year of economic downturn, the company has sufficient cash for debt repayment.

With respect to capital deployment, it is important to mention here that the company anticipates to be cautious regarding the same. Per management, the company's robust cash flow generation and solid balance sheet are likely to position it better to withstand any financial and operational obstacles due to the pandemic.

Risks

- **Calcimimetics Down:** Per management, the profitability of calcimimetics was on a declining trajectory by the end of the first quarter. In the second quarter, RPT from calcimimetics fell from \$9.55 to \$7, which is about a \$2.5 decline. Calcimimetics contributed approximately \$19 million to the company's operating income in the quarter. Also, due to unfavorable timing of calcimimetics and ballot-related costs, management expects some fluctuations in second-half 2020 earnings per share.

- **Strict Regulatory Environment:** DaVita's operations are subject to extensive federal, state and local government laws and regulations, such as Medicare and Medicaid payment rules and regulations, federal and state anti-kickback laws, the Stark Law and analogous state self-referral prohibition statutes, the False Claims Act (FCA), the Civil Monetary Penalty statute, the Foreign Corrupt Practices Act (FCPA) and federal and state laws regarding the collection, use and disclosure of patient health information. A violation or departure from any of these legal requirements may result in government audits, lower reimbursements, significant fines and penalties, the potential loss of certification, recoupment efforts or voluntary repayments, among other things.

In addition, failure to report and return overpayments within 60 days of when the overpayment is identified can lead to a violation of the FCA and associated penalties, as described in further detail below, and exclusion and penalties under the federal Civil Monetary Penalty statute, including civil monetary penalties of up to \$20,000 (adjusted for inflation) for each item or service for which a person received an identified overpayment and failed to report and return such overpayment.

- **Integration Risks:** DaVita's business strategy includes growth through acquisitions of dialysis centers and other businesses, as well as entry into joint ventures. The company may engage in acquisitions, mergers, joint ventures or dispositions or expand into new business models, which may affect its results of operations, debt-to-capital ratio, capital expenditures or other aspects of the business.

Per management, businesses that DaVita acquires may have unknown or contingent liabilities or liabilities that are in excess of the amounts that the company had originally estimated. Further DaVita can face other issues related to internal controls over financial reporting or issues that could affect the company's ability to comply with healthcare laws and regulations and other laws applicable to the company's expanded business.

- **Foreign Exchange Headwinds:** DaVita gains a significant part of its revenues from overseas operations and acquisition of dialysis centers abroad. However, a strengthening U.S. dollar is likely to impact the company's international sales. Notably, in the first quarter of 2020, the company saw a foreign exchange loss of about \$9 million associated with the international business operations. In the second quarter, there was a \$4-million foreign exchange loss associated with international business operations.

- **Dependence on Commercial Payers:** A significant portion of DaVita's dialysis and related lab services revenues are generated from patients who have commercial payers as the primary payers. The payments received from commercial payers are the primary generators of profit. However, there remains a risk of people shifting from commercial insurance schemes to government schemes due to the wide disparity in payment rates in case of a rise in unemployment. In fact, the mix of treatments reimbursed by non-government payers, as a percentage of total treatments, has been falling consistently over the years.

A large percentage of DaVita's patients already use Medicare or Medicaid programs. The overall increase in Medicare Advantage beneficiaries in the U.S. is likely to increase this percentage further, leading to additional pressure on the company's profitability, as inadequacy of government reimbursements could force it to close a number of centers.

- **Competition:** DaVita operates in a strictly competitive environment. Notably, the U.S. dialysis industry has a number of bigwigs operating, like, Baxter, Abbott, Boston Scientific which pose significant rivalry for DaVita.
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Last Earnings Report

DaVita Earnings Beat Estimates in Q2, Revenues Miss

DaVita Inc. reported second-quarter 2020 adjusted earnings per share of \$1.95, beating the Zacks Consensus Estimate of \$1.29 by 51%. The bottom line also reflects a significant 59.8% improvement from the year-ago quarter figure.

Total revenues in the quarter rose 1.4% year over year to \$2.88 billion, missing the Zacks Consensus Estimate by 1.1%.

Quarter Ending 06/2020

Report Date	Jul 30, 2020
Sales Surprise	-1.13%
EPS Surprise	51.16%
Quarterly EPS	1.95
Annual EPS (TTM)	7.17

Segment Details

Net dialysis and related lab patient service revenues in the second quarter totaled \$2.76 billion, up 1.1% on a year-over-year basis. Other revenues were \$121.8 million, up 2.4% from the year-ago quarter's figure.

Per management, total U.S. dialysis treatments for the second quarter were 7,570,908, or an average 97,063 treatments per day. This represents a per-day increase of 0.7% on a year-over-year basis.

Also, as of Jun 30, 2020 the company provided dialysis services to a total of approximately 236,800 patients at 3,082 outpatient dialysis centers, of which 2,795 centers were located in the United States and 287 centers in 10 other countries.

During the quarter, DaVita opened a total of 28 new dialysis centers and acquired one in the country. It also took over three dialysis centers and opened two outside of the United States. However, during the second quarter, the company also closed six dialysis centers in the United States.

Margin

Total operating expenses and charges amounted to \$2.47 billion, compared with \$2.38 billion in the year -ago period.

Adjusted operating income of \$461.2 million fell 0.9% from the prior-year quarter. Adjusted operating margin came in at 16%, down 20 basis points (bps) from the year-ago quarter.

Financial Condition

DaVita exited the second quarter with cumulative net cash from operating activities of \$1.01 billion compared with \$751.1 million in the year-ago quarter.

Guidance

DaVita has reaffirmed the 2020 revenue range between \$11.50 billion and \$11.70 billion. The Zacks Consensus Estimate for the same is pegged at \$11.68 billion.

Adjusted EPS projection has been updated to the range of \$6.25-\$6.75 compared with the previously-issued \$5.75-6.25. The Zacks Consensus Estimate for the same stands at \$6.13.

Adjusted operating income margin is estimated in the band of 14-14.75% (up from the prior-guided range of 13-14%).

Valuation

DaVita's shares are up 10.5% in the year-to-date period and up 38.8% in the trailing 12-month periods. Stocks in the Zacks sub-industry and the Zacks Medical sector are up 6.4% and up 1% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry is up 3.7% while sector is up 9.5%.

The S&P 500 index is down 2.6% in the year-to-date period and up 15% in the past year.

The stock is currently trading at 12.8X Forward 12-months earnings, which compares to 20.6X for the Zacks sub-industry, 22.6X for the Zacks sector and 22.6X for the S&P 500 index.

Over the past five years, the stock has traded as high as 22.9X and as low as 9.4X, with a 5-year median 15.4X.

Our Outperform recommendation indicates that the stock will perform above the market. Our \$95 price target reflects 14.7X forward 12-months earnings.

The table below shows summary valuation data for DVA.

Valuation Multiples -DVA					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	12.75	20.55	22.61	22.58
	5-Year High	22.86	22.66	23.16	22.58
	5-Year Low	9.37	14.49	15.89	15.25
	5-Year Median	15.42	17.67	18.90	17.55
P/S F12M	Current	0.86	2.63	2.82	3.61
	5-Year High	1.26	2.63	3.41	3.61
	5-Year Low	0.62	0.71	2.22	2.53
	5-Year Median	0.86	1.08	2.90	3.04
P/B TTM	Current	4.34	3.35	4.40	4.52
	5-Year High	5.04	4.00	5.07	4.56
	5-Year Low	1.77	1.91	2.94	2.83
	5-Year Median	2.71	2.49	4.29	3.73

As of 08/05/2020

Industry Analysis Zacks Industry Rank: Top 33% (84 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Fresenius Medical Care AGCo. KGaA (FMS)	Outperform	1
Amedisys, Inc. (AMED)	Neutral	3
Chemed Corporation (CHE)	Neutral	3
Quest Diagnostics Incorporated (DGX)	Neutral	3
Encompass Health Corporation (EHC)	Neutral	3
Elanco Animal Health Incorporated (ELAN)	Neutral	3
Hanger Inc. (HNGR)	Neutral	3
LHC Group, Inc. (LHCG)	Neutral	3

Industry Comparison

Industry: Medical - Outpatient And Home Healthcare

Industry Peers

	DVA	X Industry	S&P 500	DGX	EHC	ELAN
Zacks Recommendation (Long Term)	Outperform	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	1	-	-	3	3	3
VGM Score	A	-	-	A	B	F
Market Cap	10.12 B	793.97 M	22.93 B	17.06 B	6.77 B	10.08 B
# of Analysts	7	4	14	7	8	6
Dividend Yield	0.00%	0.00%	1.76%	1.76%	1.64%	0.00%
Value Score	A	-	-	A	B	D
Cash/Price	0.30	0.08	0.07	0.06	0.07	0.15
EV/EBITDA	9.68	11.90	13.16	12.72	10.66	22.72
PEG Ratio	0.56	3.29	2.99	0.96	5.45	4.70
Price/Book (P/B)	4.33	2.90	3.20	2.90	3.70	1.52
Price/Cash Flow (P/CF)	7.35	13.64	12.45	13.97	10.95	13.31
P/E (F1)	12.38	35.63	21.78	15.13	22.76	43.21
Price/Sales (P/S)	0.88	1.20	2.47	2.27	1.47	3.60
Earnings Yield	8.08%	2.16%	4.33%	6.61%	4.39%	2.29%
Debt/Equity	4.54	0.66	0.77	0.68	2.06	0.31
Cash Flow (\$/share)	11.28	1.90	6.94	9.09	6.22	1.90
Growth Score	B	-	-	B	C	D
Hist. EPS Growth (3-5 yrs)	8.21%	7.92%	10.46%	6.83%	13.25%	NA
Proj. EPS Growth (F1/F0)	23.99%	15.41%	-7.14%	28.05%	-23.47%	-44.81%
Curr. Cash Flow Growth	19.72%	6.12%	5.47%	10.66%	8.30%	-2.65%
Hist. Cash Flow Growth (3-5 yrs)	0.89%	13.00%	8.55%	6.08%	13.00%	NA
Current Ratio	1.35	1.29	1.32	1.29	1.66	3.82
Debt/Capital	83.54%	50.51%	44.59%	41.06%	67.57%	23.39%
Net Margin	7.20%	3.79%	10.15%	9.99%	6.21%	-3.63%
Return on Equity	40.78%	13.48%	14.46%	13.78%	16.89%	4.68%
Sales/Assets	0.64	0.82	0.51	0.60	0.73	0.30
Proj. Sales Growth (F1/F0)	2.08%	2.00%	-1.68%	12.80%	1.91%	-11.24%
Momentum Score	B	-	-	A	C	F
Daily Price Chg	-0.78%	0.13%	0.59%	-0.81%	0.13%	1.94%
1 Week Price Chg	0.07%	1.48%	0.14%	1.66%	3.09%	0.17%
4 Week Price Chg	1.23%	8.75%	5.31%	7.75%	10.87%	16.77%
12 Week Price Chg	4.98%	18.71%	19.84%	18.57%	7.07%	31.05%
52 Week Price Chg	38.78%	17.43%	2.73%	27.10%	7.75%	-19.67%
20 Day Average Volume	836,750	155,430	2,098,555	1,425,802	614,262	5,604,147
(F1) EPS Est 1 week change	9.18%	0.00%	0.00%	0.00%	0.00%	-5.39%
(F1) EPS Est 4 week change	9.18%	0.00%	1.10%	48.71%	-1.67%	-7.87%
(F1) EPS Est 12 week change	9.31%	0.27%	1.04%	91.44%	-4.10%	-41.25%
(Q1) EPS Est Mthly Chg	-2.70%	0.00%	0.39%	52.41%	6.63%	-19.49%

Zacks Stock Rating System

We offer two rating systems that take into account investors' holding horizons: Zacks Rank and Zacks Recommendation. Each provides valuable insights into the future profitability of the stock and can be used separately or in combination with each other depending on your investment style.

Zacks Recommendation

The Zacks Recommendation aims to predict performance over the next 6 to 12 months. The foundation for the quantitatively determined Zacks Recommendation is trends in the company's estimate revisions and earnings outlook. The Zacks Recommendation is broken down into 3 Levels; Outperform, Neutral and Underperform. Unlike many Wall Street firms, we have an excellent balance between the number of Outperform and Neutral recommendations. Our team of 70 analysts are fully versed in the benefits of earnings estimate revisions and how that is harnessed through the Zacks quantitative rating system. But we have given our analysts the ability to override the Zacks Recommendation for the 1200 stocks that they follow. The reason for the analyst over-rides is that there are often factors such as valuation, industry conditions and management effectiveness that a trained investment professional can spot better than a quantitative model.

Zacks Rank

The Zacks Rank is our short-term rating system that is most effective over the one- to three-month holding horizon. The underlying driver for the quantitatively-determined Zacks Rank is the same as the Zacks Recommendation, and reflects trends in earnings estimate revisions.

Zacks Style Scores

The Zacks Style Score is as a complementary indicator to the Zacks rating system, giving investors a way to focus on the highest rated stocks that best fit their own stock picking preferences.

Academic research has proven that stocks with the best Value, Growth and Momentum characteristics outperform the market. The Zacks Style Scores rate stocks on each of these individual styles and assigns a rating of A, B, C, D and F. We also produce the VGM Score (V for Value, G for Growth and M for Momentum), which combines the weighted average of the individual Style Scores into one score. This is perfectly suited for those who want their stocks to have the best scores across the board.

Value Score	A
Growth Score	B
Momentum Score	B
VGM Score	A

As an investor, you want to buy stocks with the highest probability of success. That means buying stocks with a Zacks Recommendation of Outperform, which also has a Style Score of an A or a B.

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