DaVita Inc. (DVA)

$75.95 (As of 03/13/20)

Price Target (6-12 Months): **$87.00**

Long Term: 6-12 Months	**Zacks Recommendation:**	**Outperform**
	(Since: 02/11/20)	
	Prior Recommendation: Neutral	
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**1-Strong Buy**
	Zacks Style Scores:	VGM:A
	Value: B | Growth: A	Momentum: D

Summary

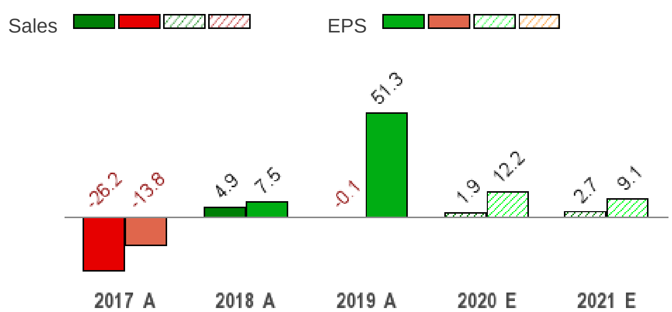
DaVita ended the fourth quarter on a tepid note. However, the massive surge in the quarterly bottom line is encouraging. Dialysis services in the United States showcased solid results during the quarter. Also, dialysis activities ramped up overseas. Further, the company is on track to acquire more dialysis centers in the United States. The recent divestment of the DMG unit to Optum is likely to enable the company to clear debt. A solid guidance for 2020 is an added positive. The stock has outperformed the industry in a year's time. On the flip side, the company witnessed softness in calcimimetics in the quarter, which impacted annual sales. Also, ballot-related costs are expcted to impact the bottom line in the second half of 2020. DaVita is currently exposed to foreign exchange headwinds.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	**$90.15 - $43.40**
20 Day Average Volume (sh)	**1,754,141**
Market Cap	**$9.5 B**
YTD Price Change	**1.2%**
Beta	**1.61**
Dividend / Div Yld	**$0.00 / 0.0%**
Industry	**Medical - Outpatient and Home Healthcare**
Zacks Industry Rank	**Top 19% (47 out of 253)**
Last EPS Surprise	**12.1%**
Last Sales Surprise	**-0.6%**
EPS F1 Est- 4 week change	**0.0%**
Expected Report Date	**05/05/2020**
Earnings ESP	**0.0%**
P/E TTM	**13.8**
P/E F1	**12.5**
PEG F1	**0.6**
P/S TTM	**0.8**

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2021	2,876 E	2,955 E	3,007 E	3,003 E	11,921 E
2020	2,836 E	2,901 E	2,940 E	2,929 E	11,606 E
2019	2,743 A	2,843 A	2,904 A	2,899 A	11,388 A

EPS Estimates

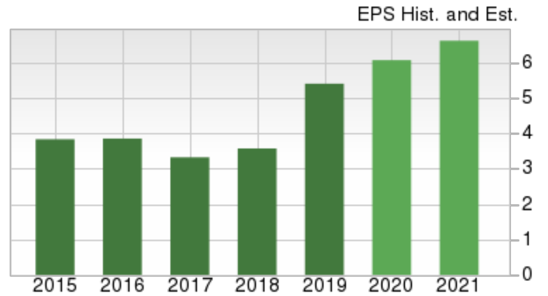
	Q1	Q2	Q3	Q4	Annual*
2021	$1.56 E	$1.67 E	$1.65 E	$1.70 E	$6.61 E
2020	$1.47 E	$1.60 E	$1.49 E	$1.51 E	$6.06 E
2019	$0.91 A	$1.22 A	$1.53 A	$1.86 A	$5.40 A

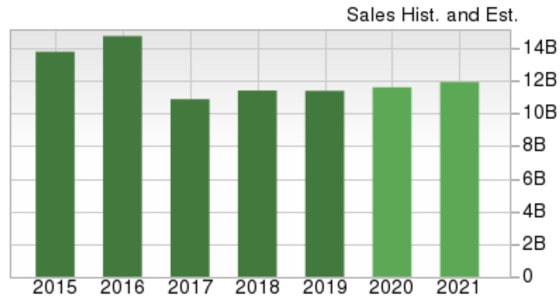
*Quarterly figures may not add up to annual.

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 03/13/2020. The reports text is as of 03/16/2020.

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:

> 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.

▲ **Shares Up:** Over the past year, shares of DaVita have rallied 45.9% against the industry's 6.1% rally. The current level outpaced the S&P 500 index's 5.3% decline.

DaVita is set to gain significantly from dialysis services in 2020 and hence has issued an impressive 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, specalizes in a broad array of dialysis services, thereby significantly contributing to the company's topline.

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.

Notably, fourth-quarter U.S. dialysis and related lab services revenues grossed $2.77 billion, up 1.8% on a year-over-year basis.

▲ **Guidance Impressive:** DaVita raised its earnings per share (EPS) guidance for 2020.

Notably, the company now expects adjusted EPS between $5.75 and $6.25. This compares to the earlier projected band of $5.25-$5.75.

DaVita expects 2020 revenues between $11.50 billion and $11.70 billion.
Operating income margin is estimated in the band of 13-14%.

Free cash flow from continuing operations is projected between $600 million and $800 million.

▲ **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.

In the fourth quarter of 2019, the company provided dialysis services to a total of approximately 235,500 patients at 3,012 outpatient dialysis centers, of which 2,753 centers were located in the United States and 259 centers in 10 countries outside the United States.

During the quarter, DaVita opened a total of 31 new dialysis centers in the country. Outside the United States, the company launched three new dialysis centers and acquired seven dialysis centers.

▲ **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.

DaVita realized around $2 million of operating income from its international operations in the fourth quarter.

Risks

- **Calcimimetics Down:** Per management, DaVita witnessed a drop in calcimimetics revenues in the fourth quarter, which impacted its annual sales. Resultantly, DaVita's 2019 revenues fell 0.1% from 2018. For 2020, DaVita now expects $40-$70 million of operating income from calcimimetics. Also, due to unfavorable timing of calcimimetics and ballot-related costs, management expects some fluctuations in second-half 2020 EPS.

- **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 fourth quarter of 2019, the company witnessed a loss of $4 million in international operating income owing to unfavorable currency movements. For 2019, the company incurred a loss of $2 million in international operating income.

- **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.

Last Earnings Report

DaVita Earnings Beat Estimates in Q4, Guidance Impressive

Quarter Ending	12/2019
Report Date	Feb 10, 2020
Sales Surprise	-0.61%
EPS Surprise	12.05%
Quarterly EPS	1.86
Annual EPS (TTM)	5.52

DaVita reported fourth-quarter 2019 adjusted EPS of $1.86, beating the Zacks Consensus Estimate of $1.66. The bottom line indicates a massive surge from the year-ago quarter's 90 cents.

Total revenues in the quarter moved up 2.7% year over year to $2.90 billion, which also lagged the Zacks Consensus Estimate of $2.92 billion.

Fourth-quarter adjusted operating income totaled $463 million, up 25.1% year over year.

Segment Details

Net dialysis and related lab patient service revenues in the fourth quarter totaled $2.77 billion, up 1.8% on a year-over-year basis. Other revenues were $132,575, up 26.2% from the year-ago quarter's figure.

Per management, total U.S. dialysis treatments for the fourth quarter were 7,681,462, or an average of 96,744 treatments per day. The figure represents a per-day increase of 1.7% on a year-over-year basis.

Per management, DaVita witnessed lower calcimimetics revenue in the quarter, which impacted its annual sales.

Also, the company provided dialysis services to a total of approximately 235,500 patients at 3,012 outpatient dialysis centers, of which 2,753 centers were located in the United States and 259 centers were in 10 countries outside the United States. During the quarter, DaVita opened a total of 31 new dialysis centers in the country. Outside the United States, the company launched three new dialysis centers and acquired seven dialysis centers.

Financial Condition

DaVita exited the fourth quarter with operating cash flow of $678 million.

Guidance

DaVita expects 2020 revenues between $11.50 billion and $11.70 billion.
Adjusted EPS is projected between $5.75 and $6.25. This compares to the earlier projected band of $5.25-$5.75.

Operating income margin is estimated in the band of 13-14%.

Free cash flow from continuing operations is projected between $600 million and $800 million.

Valuation

DaVita's shares are up 1.2% in the year-to-date period and up 45.8% in the trailing 12-month periods. Stocks in the Zacks sub-industry are down 11.4% while the Zacks Medical Sector is 12.8% in the year-to-date period. Over the past year, stocks in the Zacks sub-industry are down 6.1% while that in the sector are down 13.8%.

The S&P 500 index is down 15.8% in the past six months period and down 5.3% in the past year.

The stock is currently trading at 12.3X Forward 12-months earnings, which compares to 17.44X for the Zacks sub-industry, 17.95X for the Zacks sector and 15.72X for the S&P 500 index.

Over the past five years, the stock has traded as high as 22.86X and as low as 9.37X, with a 5-year median 16X.

Our Outperform recommendation indicates that the stock will perform better than the market. Our $87 price target reflects 14X 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	12.3	17.44	17.95	15.72
	5-Year High	22.86	21.46	21.08	19.34
	5-Year Low	9.37	14.49	15.82	15.18
	5-Year Median	16	17.61	18.74	17.42
P/S F12M	Current	0.82	2.11	2.44	2.9
	5-Year High	1.3	2.45	3.84	3.44
	5-Year Low	0.62	0.71	2.44	2.54
	5-Year Median	0.89	1	2.96	3
P/B TTM	Current	4.2	2.79	4	3.65
	5-Year High	4.89	3.74	4.05	4.56
	5-Year Low	1.77	1.91	3.45	2.85
	5-Year Median	2.71	2.47	4.32	3.63

As of 03/13/2020

Industry Analysis **Zacks Industry Rank:** Top 19% (47 out of 253)

Top Peers

Amedisys, Inc. **(AMED)**	Neutral
Chemed Corporation **(CHE)**	Neutral
Quest Diagnostics Incorporated **(DGX)**	Neutral
Encompass Health Corporation **(EHC)**	Neutral
Fresenius Medical Care AG & Co. KGaA **(FMS)**	Neutral
Hanger Inc. **(HNGR)**	Neutral
LHC Group, Inc. **(LHCG)**	Neutral
Elanco Animal Health Incorporated **(ELAN)**	Underperform

Industry Comparison Industry: Medical - Outpatient And Home Healthcare

Industry Peers

	DVA Outperform	X Industry	S&P 500	DGX Neutral	EHC Neutral	ELAN Underperform
VGM Score	A	-	-	C	B	D
Market Cap	9.54 B	698.22 M	19.05 B	12.91 B	6.29 B	8.94 B
# of Analysts	7	2.5	13	8	9	5
Dividend Yield	0.00%	0.00%	2.31%	2.19%	1.75%	0.00%
Value Score	B	-	-	C	B	C
Cash/Price	0.12	0.06	0.05	0.08	0.02	0.03
EV/EBITDA	10.51	10.87	11.57	9.93	9.95	23.16
PEG Ratio	0.57	2.21	1.68	2.18	3.06	1.49
Price/Book (P/B)	4.20	3.25	2.56	2.29	3.72	1.51
Price/Cash Flow (P/CF)	6.73	10.46	10.18	10.64	10.27	11.81
P/E (F1)	12.53	21.75	14.94	14.56	17.60	20.06
Price/Sales (P/S)	0.84	1.03	2.02	1.67	1.37	2.91
Earnings Yield	7.98%	3.77%	6.67%	6.87%	5.68%	4.99%
Debt/Equity	4.61	0.58	0.70	0.70	1.93	0.42
Cash Flow ($/share)	11.28	1.93	7.01	9.09	6.22	1.90
Growth Score	A	-	-	B	B	D
Hist. EPS Growth (3-5 yrs)	2.09%	12.31%	10.85%	8.95%	16.11%	NA
Proj. EPS Growth (F1/F0)	12.30%	14.23%	5.99%	1.31%	-7.13%	5.47%
Curr. Cash Flow Growth	19.72%	6.70%	6.15%	10.66%	8.30%	-2.65%
Hist. Cash Flow Growth (3-5 yrs)	0.89%	7.93%	8.52%	6.08%	13.00%	NA
Current Ratio	1.56	1.23	1.24	1.25	1.05	2.90
Debt/Capital	83.67%	55.12%	42.57%	41.55%	67.44%	29.58%
Net Margin	7.12%	2.93%	11.64%	11.10%	7.79%	2.21%
Return on Equity	25.18%	13.50%	16.74%	16.15%	23.68%	7.33%
Sales/Assets	0.59	0.87	0.54	0.64	0.77	0.35
Proj. Sales Growth (F1/F0)	1.91%	5.14%	3.54%	2.06%	6.21%	0.34%
Momentum Score	D	-	-	F	C	C
Daily Price Chg	11.28%	4.51%	8.21%	7.03%	8.32%	5.11%
1 Week Price Chg	5.44%	0.17%	-0.67%	5.62%	3.23%	-7.34%
4 Week Price Chg	-11.93%	-22.45%	-22.67%	-13.72%	-22.45%	-27.92%
12 Week Price Chg	2.98%	-17.60%	-20.46%	-10.39%	-8.82%	-22.52%
52 Week Price Chg	41.75%	-3.89%	-10.79%	10.09%	6.50%	-26.00%
20 Day Average Volume	1,754,141	150,782	3,061,271	1,831,211	889,781	6,340,389
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	-0.11%	-0.11%	0.00%
(F1) EPS Est 4 week change	0.00%	-0.11%	-0.32%	-0.11%	-0.11%	-1.06%
(F1) EPS Est 12 week change	9.01%	-1.56%	-0.65%	-1.39%	-2.48%	-8.11%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	-0.62%	-0.34%	-0.70%	4.17%

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	B
Growth Score	A
Momentum Score	D
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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