Fresenius Medical Care (FMS)

$37.60 (As of 01/20/20)

Price Target (6-12 Months): **$40.00**

Long Term: 6-12 Months	**Zacks Recommendation:** (Since: 12/16/19) Prior Recommendation: Outperform	**Neutral**
Short Term: 1-3 Months	**Zacks Rank:** (1-5)	**4-Sell**
	Zacks Style Scores:	VGM:B
	Value: A | Growth: C | Momentum: C	

Summary

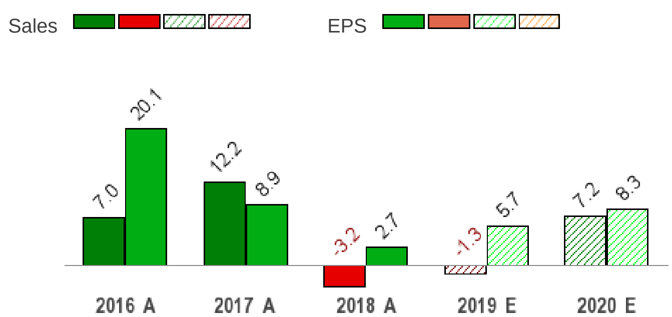
Fresenius Medical continues to gain from core Health Care Products and Services segments. Revenues in the North American, EMEA and Asia-Pacific regions also improved. In fact, management remains optimistic about the buyouts of Sound Physicians and NxStage Medical. Furthermore, strong view for 2019 and 2020 paints a brighter picture. A wide range of dialysis products and services instills optimism in the stock. Management expects to undertake meaningful investments in 2019 to capitalize on opportunities and optimize cost base. Fresenius Medical reported strong results in the third quarter. However, an intensely competitive dialysis products market adds to woes. The stock has underperformed the industry in a year's time.

Price, Consensus & Surprise

Data Overview

52 Week High-Low	$42.75 - $31.63
20 Day Average Volume (sh)	372,425
Market Cap	$22.8 B
YTD Price Change	2.1%
Beta	1.45
Dividend / Div Yld	$0.45 / 1.2%
Industry	[Medical - Instruments]
Zacks Industry Rank	Bottom 39% (155 out of 254)
Last EPS Surprise	13.6%
Last Sales Surprise	4.1%
EPS F1 Est- 4 week change	-0.2%
Expected Report Date	02/19/2020
Earnings ESP	0.0%
P/E TTM	15.4
P/E F1	14.5
PEG F1	2.5
P/S TTM	1.2

Sales and EPS Growth Rates (Y/Y %)



Sales Estimates (millions of $)

	Q1	Q2	Q3	Q4	Annual*
2020	4,892 E	5,056 E	5,085 E	5,168 E	20,575 E
2019	4,694 A	4,883 A	4,913 A	4,772 E	19,192 E
2018	4,885 A	5,028 A	4,718 A	4,909 A	19,443 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2020	$0.62 E	$0.65 E	$0.66 E	$0.70 E	$2.60 E
2019	$0.59 A	$0.52 A	$0.67 A	$0.68 A	$2.40 E
2018	$0.49 A	$0.54 A	$0.69 A	$0.66 A	$2.27 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 01/20/2020. The reports text is as of 01/21/2020.

Overview

Based in Bad Homburg, Germany, Fresenius Medical Care AG & Co. KGaA (FMS) is one of the largest integrated providers of products and services for individuals undergoing dialysis following chronic kidney failure.

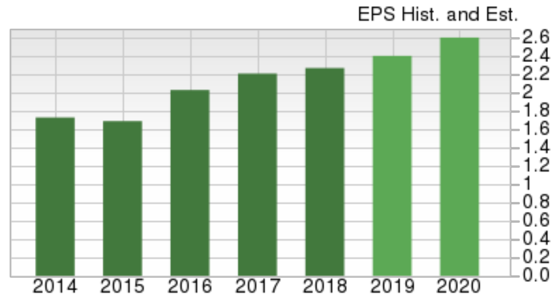
Formed in 1996 following the merger of the dialysis business of Fresenius AG and the U. S. dialysis service provider, National Medical Care, Fresenius Medical provides products and services across the entire dialysis value chain throughout the World.

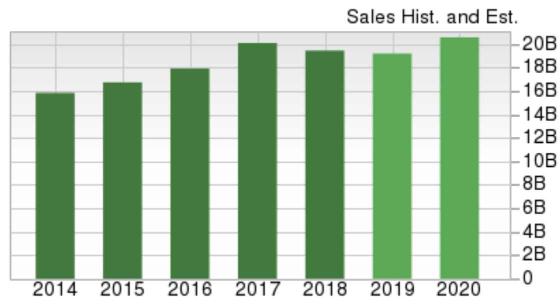
Through its network of over 3,600 dialysis clinics across the world, the company offers dialysis services and products in more than 120 countries and employs over 109,000 staffs in more than 50 countries.

Fresenius Medical manufactures a variety of durable medical devices used in the treatment of End Stage Renal Disease (ESRD). Devices like Hemodialysis Machines, Peritoneal Dialysis Machines, Granuflo Concentrate Mixing Tanks and monitoring devices like the Crit-line platform are included in the company's product pipeline.

The company primarily operates in two revenue segments.

The Health Care Services segment: This segment consists of the company's Dialysis Services and the Care-Coordination (non-dialysis laboratory services), which accounted 81.7% of net revenues in full year 2018.





The Health Care Products segment: This segment comprises of the company's Dialysis machines, dialyzers, dialysis solutions, hemodialysis concentrates, bloodline systems, water treatment systems, dialysis drugs and other medical products. The segment accounted for 18.3% of net revenues in full year 2018.

Fresenius Medical derives its revenues majorly from four geographical locations - North America, EMEA, Asia-Pacific and Latin America.

Reasons To Buy:

Global Efficiency Program Phase II on Track: Fresenius Medical has launched the second phase of its Global Efficiency Program (GEP II) in 2018. The program's aim is to identify and realize further efficiency potential and enhance the overall competitiveness of Fresenius Medical. Starting in 2018, GEP II targets to achieve sustained cost improvements of EUR 150 to 200 million per annum by 2020. Per management, the GEP program continues to progress in line with its plans over the course of 2019.

Wide range of dialysis products, deliberate initiatives for attaining market traction, solid international foothold, strategic acquisitions & divestments are the major growth catalysts

2019 Guidance & Cost-Optimization Program: For 2019, Fresenius Medical continues to expect adjusted revenue growth between 3% and 7%. Adjusted net income is anticipated to grow in the range of (2%) to 2%. For 2020, adjusted revenues and adjusted net income are estimated to grow at mid-to-high single digits.

In 2019, Fresenius Medical is likely to invest around EUR 100 million to sustainably improve cost base in addition to the GEP II program. Notably, the 2019 cost-optimization program is expected to be accretive to net income from 2020.

Wide Range of Dialysis Products & Services: The company provides a wide range of Dialysis products in its own dialysis clinics and to third-party clinics. These include modular machine components, dialyzers, bloodline systems, HD (hemodialysis) solutions, concentrates and water treatment systems.

Fresenius Medical offers a wide array of Hemodyalisis, Peritoneal dialysis and Acute Dialysis products as well. Earlier, the company sold more than 48,000 dialysis machines worldwide, in addition to 130 million dialyzers. Till date, the company has accounted for almost half of global sales of dialysis products. Around 3 million patients, worldwide, regularly undergo dialysis treatment.

In September 2019, the company achieved another milestone in China, with the introduction of the 4,008A dialysis machine. This is a significant step in the market with the largest dialysis patient population in the world.

Favorable Tiding on the Regulatory Front: Fresenius Medical recently announced the FDA device approval for its computer-assisted ultrafiltration control software, which aims to improve fluid management during hemodialysis (HD). This further fortifies Fresenius Medical's foothold in the global renal medical devices and services space.

The ultrafiltration control software is designed to work with its newer HD machines and provide computer-assisted diagnosis. Notably, effective fluid management is critical about creating the best HD treatment.

Growth Strategy 2020: Fresenius Medical has set up a strong long-term objective called the 'Growth Strategy 2020', to chalk out a few strategic initiatives for attaining solid market traction.

Per the postulates of the 'Growth Strategy 2020', Fresenius Medical aims to boost revenues to $28 billion by 2020, corresponding to an average annual growth rate of around 10%. In this regard revenues increased 7% on a year-over-year basis and reached $17.9 billion in recent past, driven by strong performance in Health Care Services. Furthermore, management forecasts an increase in revenues in tune with organic growth and acquisitions. At the same time, the company expects high single-digit annual growth in net income by 2020.

In addition to the stock's strong performance in its core dialysis business, Fresenius Medical intends to achieve the 2020 targets by expanding its Care Coordination (non-dialysis segment) as well. The company reconfirmed the mid-term outlook of its 'Growth Strategy 2020' in 2018.

Huge Investments in China & India: Fresenius Medical plans to invest in designing training facilities, training courses and optimizing facilities to meet increasing demand for home dialysis products and services in the developing economies.

In 2019, the company is likely to make huge investments in China. On the product side, Fresenius Medical has 15 years of experience in China. Now, it is trying to leverage on the chronic diseases and the current development of the Chinese healthcare market. Precisely, Fresenius Medical is expected to form a network of more than 100 clinics and invest in home dialysis in China during the upcoming years.

The company's second focus is likely to be on the Indian market, where it has just launched the 4008A machine.

Strong Global Foothold: Fresenius Medical has a solid market hold in the regions of North America, Europe (EMEA), Asia Pacific and Latin America. To strengthen its market position, the company is resorting to various approaches like enhancing its organic growth and making strategic and suitable acquisitions. The company also aims at aligning its business activities through public-private partnerships in the dialysis business for tapping into new markets in the coming quarters.

In recent past, the company entered the dialysis services market in Israel. Fresenius Medical also expanded its dialysis services business in India by acquiring an 85% stake in Sandor Nephro Services, a dialysis group, offering dialysis treatment and other associated services such as laboratory tests to 308,471 patients in 3,624 dialysis clinics worldwide.

In third-quarter 2019, the company witnessed revenue growth across all its geographical zones, viz, Asia-Pacific, North America, Latin America and EMEA.

Strategic Acquisitions & Partnerships: Acquisitions have been a key catalyst for the company. In an initiative to boost its long-term strategy or the 'Growth-Strategy 2020', Fresenius Medical already acquired all outstanding shares of NxStage Medical for $30 a share. Fresenius Medical expects the acquisition to prove accretive to earnings within three years from deal closure. Furthermore, the deal is expected to provide annual pre-tax cost savings of $80 million to $100 million over the next three to five years. Fresenius Medical also expects integration costs of about $150 million over the next three years from the time of announcement last year.

Lately, the company has also entered into a strategic agreement with Humacyte, Inc., a medical research, discovery and development company and a $150 million equity investment. This agreement will further provide Fresenius Medical to obtain exclusive global rights to commercialize HUMACYL, Humacyte's investigational human acellular vessel.

▲ **Divestments:** In an initiative to optimize its portfolio, Fresenius Medical recently sold the majority of its shareholding in Sound Inpatient Physicians Holdings for $2.15 billion to an investment consortium led by private equity firm Summit Partners. Notably, the sale is likely to close late in 2018 and bring a gain of about $983 million for the company.

Earlier, the company announced the divestiture of its Shiel Medical unit to Quest Diagnostics. Notably, Shiel is a clinical laboratory provider primarily focusing on non-renal lab services. The lab specifically serves in the New York-New Jersey metropolitan area. Post the deal closure, Quest Diagnostics and Fresenius Medical will jointly work on identifying patients with early-stage chronic kidney disease, with potential to benefit from treatment to slow progression to end-stage renal disease (ESRD), based on the former's laboratory data analytics.

▲ **Distribution Agreement:** Recently, RenalSense has entered into an agreement with Fresenius Medical Care (Bad Homburg) for distribution of its Clarity RMS critical care urine monitoring system in Europe, the Middle East, and Africa (EMEA).

Fresenius Medical Care will market the company's products in 85 EMEA countries through its acute care division.

Reasons To Sell:

Unfavorable price performance, tough regulatory environment, difficulties in collecting trade receivables in foreign legal-paradigms & competition in the niche markets are the headwinds

- **Shares Lack Luster:** Shares of Fresenius Medical gained 7.6% compared to the industry's rally of 14.9% in a year's time. The current level fell short of the S&P 500 index's growth of 25.6% over the same time frame.

  Soft peritoneal dialysis revenues and an intensely competitive dialysis market, limit the company's prospects.

- **Tough Regulatory Environment:** Fresenius Medical faces a highly regulated environment in almost every country in which it operates. Furthermore, the company has to fulfill specific legal requirements everywhere that includes the tough antitrust regulations. Violating healthcare or other regulations under public law can result in extensive legal repercussions. These include the dismissal of important federal certifications, penalties, fines, recalls, increased costs (for fulfilling regulatory requirements), exclusion from reimbursement programs of the respective government health care system, or even a total or partial ban on business operations.

  Adding to the concerns, changes in the law (especially relating to reimbursement) in such a difficult regulatory environment can also impact the company's fundamental business model and the implementation of strategy. Because of the company's significant international exposure, Fresenius Medical is likely to face difficulties while enforcing and collecting trade receivables in foreign legal paradigms. In fact, the inability of certain countries to service their national debt might hamper the company's interests. Notably, concerns associated with the regulatory environment present a low risk to the company in the short-term, and in the mid-term, they present a medium risk to the company.

- **Cutthroat Market Competition:** Fresenius Medical has numerous competitors in the field of health care services as well as the sale of dialysis products. Tough competition in the niche markets is likely to impede the company's sales opportunities and lose market share. However, per management, concerns that arise due to competition represent low risk for the company in the short-term, as well as in the mid-term. The company faces aggressive rivalry from HCA Holdings, DaVita HealthCare and Baxter International.

  The problem of competitors copying patents of Fresenius Medical is an added concern, which might arise from inadequate protection for technologies and products developed by the company. This might affect the company's bottom line in the long term.

Last Earnings Report

Fresenius Medical Q3 Earnings & Revenues Top Estimates

Quarter Ending	09/2019
Report Date	Oct 29, 2019
Sales Surprise	4.05%
EPS Surprise	13.56%
Quarterly EPS	0.67
Annual EPS (TTM)	2.44

Fresenius Medical Care AG & Co. KGaA reported adjusted earnings per share of 67 cents in the third quarter of 2019, which beat the Zacks Consensus Estimate of 59 cents by 13.6%. However, the bottom line declined 2.9% year over year.

Revenues rose 4.1% year over year to $4.91 billion and surpassed the Zacks Consensus Estimate of $4.72 billion by 4%.

Segmental Details

In the third quarter, Fresenius Medical reported through two segments — Health Care Services and Health Care Products.

Health Care Services revenues improved 7% on a year-over-year basis and 4% at cc. The improvement came on the back of growth in same market treatments, acquisitions, and increase in dialysis days. However, the effect of sold or closed clinics and a revenue recognition adjustment for accounts receivable in legal dispute partially offset the improvement.

Health Care Products revenues climbed 16% year over year and 13% at cc. The upside was mainly driven by higher sales of home hemodialysis products, primarily as a result of the effective roll-out of the NxStage product range, dialyzers, hemodialysis solutions and concentrates. Lower volume of sales of machines partially offset the upside.

Geographical Growth

North America

Revenues in the region grew 8% year over year and 3% at cc. On organic basis, sales in the region improved 3%.

EMEA

Revenues in this region increased 10% year over year and 9% cc in the quarter. On organic basis, sales in the region improved 9%. Per management, the performance was impacted by favorable business development in Health Care Services and Health Care Products.

Asia-Pacific

Revenues in this region improved 13% year over year and 9% at cc in the reported quarter. Per management, positive business development in both Health Care Services and Health Care Products led to the upside.

Latin America

Revenues in Latin America rose 7% year over year and 20% at cc. Organic growth in region was 15%.

Guidance Reiterated

For 2019, Fresenius Medical expects adjusted revenues to grow between 3% and 7%, and adjusted net income to develop in the range of a (2%) to 2%.

For 2020, this Zacks Rank #1 (Strong Buy) company expects adjusted revenues and adjusted net income to grow at a mid to high-single digit rate.

Valuation

Fresenius Medical's shares are up 2.1% and 7% in the year-to-date period and trailing 12-month periods, respectively. Stocks in the Zacks sub-industry and Zacks Medical sector are up 3.2% and 3.2% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are up 14.9% and 5.6%.

The S&P 500 index is up 26% in the year-to-date period and 26.2% in the past year.

The stock is currently trading at 14.33X Forward 12-months earnings, which compares to 34.51X for the Zacks sub-industry, 21.79X for the Zacks sector and 19.2X for the S&P 500 index.

Over the past five years, the stock has traded as high as 23.09X and as low as 11.91X, with a 5-year median 19.11X.

Our Neutral recommendation indicates that the stock will perform in-line with the market. Our $40 price target reflects 15.4X forward 12-months earnings.

The table below shows summary valuation data for FMS.

Valuation Multiples - FMS

		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	14.33	34.51	21.79	19.2
	5-Year High	23.09	34.51	21.79	19.34
	5-Year Low	11.91	23.22	15.85	15.17
	5-Year Median	19.11	27.4	18.91	17.44
P/S F12M	Current	1.1	3.69	2.88	3.57
	5-Year High	1.59	3.69	3.82	3.57
	5-Year Low	0.94	2.16	2.43	2.54
	5-Year Median	1.36	2.51	2.94	3
P/B TTM	Current	4.23	4.23	4.61	4.55
	5-Year High	2.88	4.23	5.02	4.55
	5-Year Low	1.25	2.54	3.43	2.85
	5-Year Median	2.31	3.3	4.29	3.61

As of 01/20/2020

Industry Analysis **Zacks Industry Rank:** Bottom 39% (155 out of 254)

Top Peers

STERIS plc **(STE)**	Outperform
Edwards Lifesciences Corporation **(EW)**	Neutral
Hologic, Inc. **(HOLX)**	Neutral
Intuitive Surgical, Inc. **(ISRG)**	Neutral
Olympus Corp. **(OCPNY)**	Neutral
SONOVA HOLDING **(SONVY)**	Neutral
Thermo Fisher Scientific Inc. **(TMO)**	Neutral
Varian Medical Systems, Inc. **(VAR)**	Neutral

Industry Comparison Industry: Medical - Instruments

Industry Peers

	FMS Neutral	X Industry	S&P 500	BAX Neutral	DVA Neutral	MDT Neutral
VGM Score	B	-	-	B	A	B
Market Cap	22.77 B	117.51 M	24.65 B	45.81 B	10.18 B	159.55 B
# of Analysts	3	2	13	10	6	13
Dividend Yield	1.20%	0.00%	1.73%	0.98%	0.00%	1.81%
Value Score	A	-	-	C	A	B
Cash/Price	0.05	0.09	0.04	0.07	0.15	0.07
EV/EBITDA	7.14	-0.57	14.11	19.24	11.84	18.70
PEG Ratio	2.53	2.68	2.08	2.09	0.62	2.89
Price/Book (P/B)	1.51	4.68	3.39	5.85	5.07	3.15
Price/Cash Flow (P/CF)	10.26	23.53	13.81	19.48	10.93	16.38
P/E (F1)	14.88	30.51	19.19	23.98	14.29	21.25
Price/Sales (P/S)	1.17	3.37	2.69	4.10	0.90	5.16
Earnings Yield	6.91%	-0.67%	5.21%	4.17%	7.00%	4.70%
Debt/Equity	0.75	0.10	0.72	0.72	4.26	0.49
Cash Flow ($/share)	3.66	-0.06	6.94	4.61	7.27	7.27
Growth Score	C	-	-	B	A	C
Hist. EPS Growth (3-5 yrs)	9.67%	13.24%	10.56%	NA	-0.06%	6.06%
Proj. EPS Growth (F1/F0)	6.80%	20.35%	7.57%	10.80%	4.83%	7.30%
Curr. Cash Flow Growth	2.60%	9.84%	14.73%	14.69%	-14.54%	6.26%
Hist. Cash Flow Growth (3-5 yrs)	5.04%	8.78%	9.00%	-5.21%	-2.15%	15.58%
Current Ratio	0.98	2.68	1.24	2.78	1.81	2.77
Debt/Capital	42.79%	17.32%	42.99%	41.88%	82.68%	32.80%
Net Margin	7.47%	-15.15%	11.14%	13.80%	3.68%	15.11%
Return on Equity	9.92%	-17.95%	17.16%	22.99%	19.95%	14.52%
Sales/Assets	0.55	0.60	0.55	0.68	0.57	0.34
Proj. Sales Growth (F1/F0)	6.07%	11.70%	4.16%	4.52%	0.63%	3.17%
Momentum Score	C	-	-	A	C	B
Daily Price Chg	0.08%	0.00%	0.27%	-0.29%	0.61%	0.14%
1 Week Price Chg	0.71%	0.68%	0.39%	0.47%	1.16%	4.18%
4 Week Price Chg	4.04%	3.23%	2.95%	9.13%	7.76%	4.88%
12 Week Price Chg	14.74%	4.59%	7.76%	13.47%	36.90%	13.05%
52 Week Price Chg	7.86%	-8.30%	22.29%	29.82%	40.11%	35.88%
20 Day Average Volume	372,425	117,754	1,536,375	2,305,422	1,011,500	3,533,057
(F1) EPS Est 1 week change	-0.19%	0.00%	0.00%	0.34%	0.00%	0.00%
(F1) EPS Est 4 week change	-0.19%	0.00%	0.00%	0.48%	0.00%	0.00%
(F1) EPS Est 12 week change	0.19%	0.09%	-0.40%	-0.94%	4.15%	0.69%
(Q1) EPS Est Mthly Chg	0.00%	0.00%	0.00%	0.00%	0.00%	-0.03%

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	C
Momentum Score	C
VGM Score	B

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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