

HealthEquity, Inc.(HQY)

\$52.65 (As of 04/27/20)

Price Target (6-12 Months): **\$55.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 02/04/20)

Prior Recommendation: Outperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:D

Value: D

Growth: B

Momentum: D

Summary

With solid HSA member growth, HealthEquity has gained from strong growth in Service and Custodial segments. Solid growth in HSAs and custodial assets bolstered the company's top line. Currently, HealthEquity is the second-largest HSA custodian by market share. Additionally, promising fiscal 2021 guidance instills optimism in the stock. HealthEquity exited fourth-quarter fiscal 2020 on an impressive note. However, a significant drop in operating and gross margin remains a concern. In fact, operating income plunged in the quarter. The company also faces stiff competition in the Medical Services market. HealthEquity is required to comply with the strict treasury regulations formulated by the Internal Revenue Service. The stock underperformed the industry in a year's time.

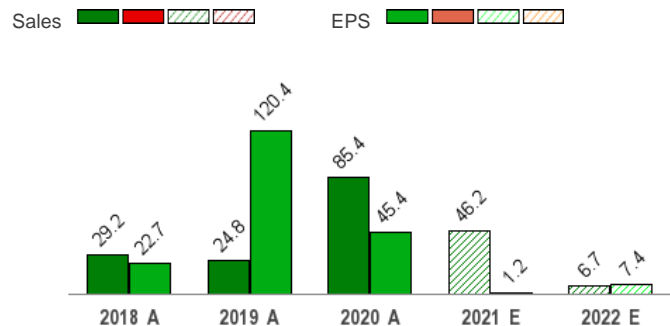
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$88.78 - \$34.40
20 Day Average Volume (sh)	966,563
Market Cap	\$3.7 B
YTD Price Change	-28.9%
Beta	1.57
Dividend / Div Yld	\$0.00 / 0.0%
Industry	<u>Medical Services</u>
Zacks Industry Rank	Top 30% (75 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	14.7%
Last Sales Surprise	1.4%
EPS F1 Est- 4 week change	-0.3%
Expected Report Date	06/02/2020
Earnings ESP	4.1%

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2022	201 E	199 E	206 E	224 E	830 E
2021	192 E	191 E	188 E	207 E	778 E
2020	87 A	87 A	157 A	201 A	532 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2022	\$0.46 E	\$0.45 E	\$0.49 E	\$0.50 E	\$1.88 E
2021	\$0.44 E	\$0.45 E	\$0.44 E	\$0.44 E	\$1.75 E
2020	\$0.41 A	\$0.45 A	\$0.47 A	\$0.39 A	\$1.73 A

*Quarterly figures may not add up to annual.

P/E TTM	30.6
P/E F1	30.1
PEG F1	1.3
P/S TTM	7.0

The data in the charts and tables, including the Zacks Consensus EPS and Sales estimates, is as of 04/27/2020. The reports text is as of 04/28/2020.

Overview

Headquartered in Draper, UT, HealthEquity provides integrated solutions for health-care account management, health reimbursement arrangement and flexible spending accounts for health plans, insurance companies and third-party administrators in the United States.

HealthEquity's flagship health savings account or HSA is a financial account through which consumers spend and save for the long term for healthcare on a tax-advantaged basis. This has provided the company with a competitive edge in the MedTech industry. Other than HSAs, the company offers Healthcare saving and spending platform, Investment platform and advisory services and Reimbursement arrangements.

In addition, HealthEquity offers health reimbursement and flexible spending arrangements solutions; Employee Retirement Income Security Act's plan administration and investment services.

The company operates through three revenue segments:

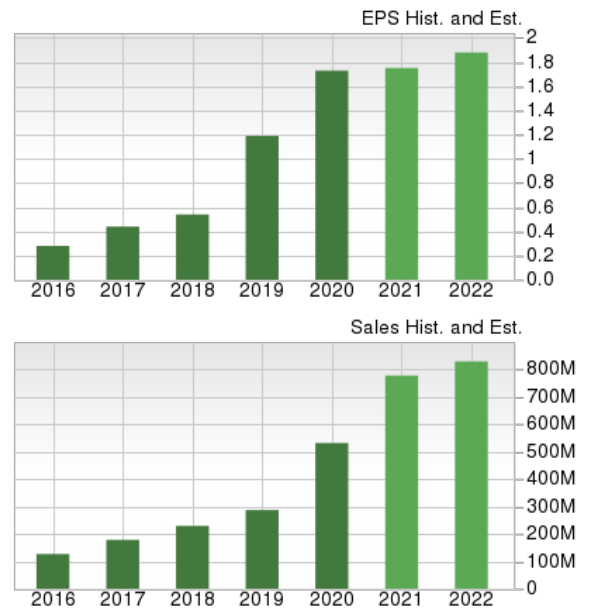
- Service revenues
- Custodial revenues
- Interchange revenues

FY20 at a Glance

In fiscal 2020, HealthEquity reported revenues of \$531.9 million, up 85.2% year over year. The top line also outpaced the Zacks Consensus Estimate by 0.2%.

The company reported adjusted net income of \$1.17 per share, down 9.3% year over year. The figure also missed the Zacks Consensus Estimate of \$1.67 by 29.9%.

While Service revenues accounted for 49% of net revenues, Custodial revenues contributed 31%. Meanwhile, Interchange revenues accounted for 16% of net revenues.



Reasons To Buy:

- ▲ **Health Savings Account (HSA):** HealthEquity is an Internal Revenue Service approved non-bank custodian of HSA, which is a medical savings account available to taxpayers in the United States who are enrolled in a high-deductible health plan (HDHP). The funds contributed to an account are not subject to federal income tax at the time of deposit. Addition to HSA, HealthEquity now offers FSA and HRA administration to regional employers.

As of Jan 31, 2020, the total number of Health Savings Accounts (HSA), for which HealthEquity served as a non-bank custodian (HSA members), was 5.3 million, up 34% year over year. Additionally, total Active HSA members were 4.3 million, up 34% year over year.

Total HSA Assets grossed \$11.5 billion, up 43% year over year.

- ▲ **Guidance Solid:** HealthEquity issued guidance for fiscal 2021.

The company expects revenues between \$770 million and \$790 million.

Adjusted net income is projected between \$124 million and \$132 million.

Adjusted EPS for fiscal 2021 is anticipated within \$1.70-\$1.81.

- ▲ **Unique Investment Platform:** It is encouraging to note that in addition to HSAs, HealthEquity offers a mutual fund investment platform and an online-only automated investment advisory service. The advisory service is delivered through a web-based tool, Advisor TM, which is offered and managed by HealthEquity Advisors, LLC. Its members pay huge fees, including all trading commissions and other expenses associated with transactions made through these online tools, for availing the above-mentioned services. Consequently, the company's operating profitability gets a boost.

There are three levels of service offered to investors. However, regardless of the level of service selected, members are responsible for the expenses payable.

- ▲ **Leadership Position:** HealthEquity clinched the top position in the HSA industry through its first-mover advantage, focus on innovation and differentiated capabilities.

The company's market share (measured by custodial assets) has literally tripled from 4% in December 2010 to 13% in December 2018, as noted by the 2018 Devenir HSA Research Report. Per the calendar 2019 Devenir HSA Research Report, Devenir projects that HSA assets grew 23%, while HealthEquity assets improved 29%. At calendar year end, HealthEquity came number one with market share of 19% with respect to HSAs and a close second by HSA assets at 16%.

According to the 2019 Midyear Devenir HSA Research Report, Devenir estimates that the HSA market will reach \$88 billion in HSA assets held over by 30 million accounts by the end of 2021.

- ▲ **Unique Suite of Advisory Services:** HealthEquity's automated investment advisory service are delivered through a web-based tool, AdvisorTM, which is offered and managed by HealthEquity Advisors, LLC. Notably, it is the company's SEC registered investment advisor subsidiary. Apart from this, HealthEquity offers 401(K) solution that can reduce the cost, risk and work of managing a retirement plan. In the third quarter of fiscal 2019, management at HealthEquity confirmed that it is doing an excellent job in selling a product in the retirement space and is also optimistic about it.

HealthEquity offers three levels of service to investors — Self-driven, GPS and Auto-pilot. For Self-driven services AdvisorTM provides a mutual fund investment platform to invest HSA balances. For GPS, AdvisorTM provides guidance and advice, but the member makes the final investment decisions and implements portfolio allocation and investment advice through the HealthEquity platform. For Auto-pilot, AdvisorTM manages the account and implements portfolio allocation as well as investment advice automatically for the member.

By the end of fiscal 2020, the company expects to add other administrative and retirement services for regional employers.

Solid HSA member growth is likely to boost HealthEquity's top line. The company now offers FSA and HRA administration to regional employers.

Reasons To Sell:

▼ **Shares Down:** Over the past year, shares of HealthEquity have declined 27.8% compared to the industry's fall of 25.2%. Intense competition and contraction in margins continue to weigh on the stock. Further, the ongoing economic volatility on account of the global coronavirus outbreak is hampering the stock.

▼ **Margins Fail to Impress:** In the fiscal fourth quarter, HealthEquity's gross margin was 56.5% of net revenues, down 220 bps year over year.

Operating income in the fiscal fourth quarter was \$14.5 million, down 12.3% year over year. Operating margin came in at 7.2% in the quarter, down significantly from the year-ago quarter's 21.9%.

▼ **Cutthroat Competition in the Medical Services Space:** HealthEquity faces stiff competition in the Medical Services markets. The company's direct competitors are HSA custodians that include state or federally chartered banks, such as Webster Bank and Optum Bank along with non-bank custodians approved by the U.S. Treasury, such as Payflex Systems USA, Inc. In the United States, the current top HSA custodians are Alliant Credit Union, Bank of America, BenefitWallet, HealthEquity, HealthSavings Administrators, HSA Bank, Optum Bank, SelectAccount, The HSA Authority and UMB Bank.

▼ **Data-security Issues:** HealthEquity deals with high level of sensitive personal data and information. Any form of security breaches might result in loss of sensitive information, theft or loss of actual funds, litigation, indemnity obligations to the customers. Notably, the company's online platform is hosted from two data centers that are located in Draper, UT and Austin, TX.

Per management, HealthEquity incurred significant costs to protect against security breaches in the fourth quarter of fiscal 2019. A similar trend in the coming quarters might keep its margins under pressure. In fact, there are high chances for the company to incur significant additional costs in the future to address problems caused by any actual or perceived security breaches.

▼ **Stiff Treasury Regulations:** As a non-bank custodian, HealthEquity is required to comply with Treasury Regulations Section 1.408-2(e) formulated by the IRS. The stiff regulatory environment has been a major dampener for HealthEquity. Notably, any failure to comply with the regulations adversely affect HealthEquity's ability to maintain current custodial accounts.

▼ **Weak Liquidity Position:** Cash and cash equivalents as of Jan 31, 2020, amounted to \$191.7 million, down from \$361.5 million in the prior-year quarter. Cumulative net cash provided by operating activities as of Jan 31, 2020, came in at \$105.4 million, compared with \$113.4 million reported in the year-ago quarter. However, the company's high level of debt on the balance sheet has pretty much to worry about, especially during the time when the coronavirus mayhem has forced the corporate sector halt their production and supply. The company's total debt came up to \$1.57 billion at the end of fiscal 2019. In fiscal 2019, the total debt-to-capital came in at 55.8%, compared to industry average of 27.2%, thereby indicating leveraged balance sheet.

HealthEquity faces stiff competition in the Medical Services markets. The company deals with high level of sensitive personal data. Any form of security breaches might hamper business prospects.

Last Earnings Report

HealthEquity Q4 Earnings and Revenues Top Estimates

HealthEquity, Inc. reported adjusted earnings per share of 39 cents in fourth-quarter fiscal 2020, which surpassed the Zacks Consensus Estimate of 34 cents by 14.7%. The bottom line also improved a significant 30% on a year-over-year basis.

For the full-year fiscal 2020, adjusted EPS came in at \$1.17, down 9.3% from the year-ago period. Further, the bottom line missed the consensus mark of \$1.67 per share by 29.9%.

Quarter Ending 01/2020

Report Date	Mar 16, 2020
Sales Surprise	1.36%
EPS Surprise	14.71%
Quarterly EPS	0.39
Annual EPS (TTM)	1.72

Revenues in Detail

The Zacks Rank #2 (Buy) company generated revenues of \$201.2 million outpacing the Zacks Consensus Estimate by 1.4%. Further, the figure soared 165.5% from the prior-year period.

For the full-year fiscal 2020, revenues came in at \$531.9, which soared 85.2% from the year-ago period and beat the consensus mark by 0.2%.

HSA Member Detail

As of Jan 31, 2020, the total number of Health Savings Accounts (HSA), for which HealthEquity served as a non-bank custodian (HSA members), was 5.3 million, up 34% year over year.

Additionally, total Active HSA members were 4.3 million, up 34% year over year.

Total Custodial Assets totaled \$11.5 billion, up 43% year over year.

Segmental Performance

Service Revenues: At this segment, revenues totaled \$122.2 million, up significantly from the year-ago quarter's \$25.8 million.

Custodial Revenues: At this segment, revenues grew 39.2% year over year to \$49.4 million, attributable to growth in HSA assets and 2.41% higher year-over-year annualized interest rate yield on HSA cash assets.

Interchange Revenues: At this segment, revenues skyrocketed 104% year over year to \$29.7 million. Per management, the upside was driven by increase in average total accounts.

Margin Details

HealthEquity generated gross profit of \$113.7 million, up significantly from the year-ago quarter's \$44.4 million. Gross margin was 56.5% of net revenues, down 220 bps year over year.

Sales and marketing expenses summed \$13.9 million, up 76.6% year over year. Technology and development expenses totaled \$31.5 million, up from \$10 million in year-ago quarter. General and administrative expenses amounted to \$23.4 million, up from the prior-year quarter's \$8.5 million.

Operating income in the fiscal fourth quarter was \$14.5 million, down 12.3% year over year. Operating margin totaled 7.2% in the quarter, down significantly from the year-ago quarter's 21.9%.

Guidance

HealthEquity issued its guidance for fiscal 2021.

The company expects revenues between \$770 million and \$790 million. The Zacks Consensus Estimate is pegged at \$822.4 million.

Adjusted net income is projected between \$124 million and \$132 million.

Adjusted EPS for fiscal 2021 is expected within \$1.70-\$1.81. The Zacks Consensus Estimate for earnings is pegged at \$1.81.

Valuation

HealthEquity's shares are down 29% and 27.8% in the year-to-date and trailing 12-month periods, respectively. Stocks in the Zacks sub-industry and Zacks Medical sector are down 13.7% and 3.4% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and sector are down 25.2% and up 1.3%, respectively.

The S&P 500 index is down 12% in the year-to-date period and 4.2% in the past year.

The stock is currently trading at 4.7X Forward 12-months sales, which compares to 4.1X for the Zacks sub-industry, 2.8X for the Zacks sector and 4.8X for the S&P 500 index.

Over the past five years, the stock has traded as high as 18.8X and as low as 3.4X, with a 5-year median of 11.3X.

Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$55 price target reflects 4.9X forward 12-months sales.

The table below shows summary valuation data for HQY.

Valuation Multiples - HQY					
		Stock	Sub-Industry	Sector	S&P 500
P/S F12M	Current	4.72	4.11	2.78	4.81
	5-Year High	18.84	4.11	3.84	4.81
	5-Year Low	3.43	1.98	2.25	2.54
	5-Year Median	11.30	2.52	2.96	3.01
EV/SALES TTM	Current	9.00	8.99	3.27	2.81
	5-Year High	22.21	10.64	4.19	3.45
	5-Year Low	6.24	2.30	2.62	2.16
	5-Year Median	13.48	3.48	3.43	2.82

As of 04/27/2020

Industry Analysis Zacks Industry Rank: Top 30% (75 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
BioTelemetry, Inc. (BEAT)	Neutral	3
Medpace Holdings, Inc. (MEDP)	Neutral	4
Natera, Inc. (NTRA)	Neutral	3
NovoCure Limited (NVCR)	Neutral	2
Progyny, Inc. (PGNY)	Neutral	3
So-Young International Inc. Sponsored ADR (SY)	Neutral	NA
Teladoc Health, Inc. (TDOC)	Neutral	2
Apollo Medical Holdings, Inc. (AMEH)	Underperform	5

Industry Comparison Industry: Medical Services				Industry Peers		
	HQY	X Industry	S&P 500	AMEH	BEAT	TDOC
Zacks Recommendation (Long Term)	Neutral	-	-	Underperform	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	5	3	2
VGM Score	D	-	-	D	C	B
Market Cap	3.73 B	214.66 M	19.77 B	522.30 M	1.59 B	14.23 B
# of Analysts	10	3	14	1	3	13
Dividend Yield	0.00%	0.00%	2.13%	0.00%	0.00%	0.00%
Value Score	D	-	-	F	D	F
Cash/Price	0.05	0.06	0.06	0.44	0.05	0.04
EV/EBITDA	38.85	-0.90	12.09	10.65	18.53	-1,407.87
PEG Ratio	1.37	1.52	2.36	4.99	2.22	NA
Price/Book (P/B)	3.62	3.11	2.70	2.72	4.30	13.91
Price/Cash Flow (P/CF)	24.88	13.07	10.70	14.34	13.81	NA
P/E (F1)	31.12	21.26	18.72	19.96	22.20	NA
Price/Sales (P/S)	7.01	2.65	2.12	0.93	3.61	25.72
Earnings Yield	3.32%	3.70%	5.19%	5.01%	4.51%	-0.57%
Debt/Equity	1.21	0.06	0.72	1.27	0.52	0.43
Cash Flow (\$/share)	2.12	-0.02	7.01	1.04	3.37	-0.50
Growth Score	B	-	-	D	B	A
Hist. EPS Growth (3-5 yrs)	47.17%	25.53%	10.88%	NA	56.71%	NA
Proj. EPS Growth (F1/F0)	1.27%	4.53%	-5.87%	74.42%	7.52%	19.46%
Curr. Cash Flow Growth	92.12%	5.01%	5.92%	7.37%	4.16%	-9.57%
Hist. Cash Flow Growth (3-5 yrs)	52.91%	14.98%	8.55%	NA	49.60%	NA
Current Ratio	1.96	1.44	1.23	3.12	3.02	6.52
Debt/Capital	54.81%	21.70%	43.90%	68.21%	34.25%	30.28%
Net Margin	7.46%	-3.05%	11.32%	2.52%	6.80%	-17.87%
Return on Equity	10.54%	-21.11%	16.60%	8.34%	20.23%	-10.65%
Sales/Assets	0.31	0.62	0.55	0.87	0.65	0.35
Proj. Sales Growth (F1/F0)	46.27%	1.69%	-1.15%	0.00%	10.30%	36.66%
Momentum Score	D	-	-	A	B	B
Daily Price Chg	2.55%	1.00%	2.63%	4.39%	5.58%	0.70%
1 Week Price Chg	9.91%	-0.18%	-1.74%	6.54%	-0.02%	11.69%
4 Week Price Chg	-0.27%	4.93%	8.71%	8.95%	17.82%	19.16%
12 Week Price Chg	-21.63%	-13.00%	-17.57%	-18.11%	-5.83%	91.09%
52 Week Price Chg	-27.81%	-27.81%	-11.60%	-24.01%	-16.71%	229.26%
20 Day Average Volume	966,563	210,540	2,734,148	44,693	321,415	2,794,812
(F1) EPS Est 1 week change	0.10%	0.00%	0.00%	0.00%	0.00%	0.00%
(F1) EPS Est 4 week change	-0.30%	-1.46%	-6.57%	0.00%	-1.10%	0.68%
(F1) EPS Est 12 week change	-4.28%	-11.29%	-12.64%	-40.95%	-0.04%	2.36%
(Q1) EPS Est Mthly Chg	-5.63%	-5.75%	-10.33%	NA	0.00%	-2.23%

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	D
Growth Score	B
Momentum Score	D
VGM Score	D

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.

Disclosures

This report contains independent commentary to be used for informational purposes only. The analysts contributing to this report do not hold any shares of this stock. The analysts contributing to this report do not serve on the board of the company that issued this stock. The EPS and revenue forecasts are the Zacks Consensus estimates, unless indicated otherwise on the reports first page. Additionally, the analysts contributing to this report certify that the views expressed herein accurately reflect the analysts personal views as to the subject securities and issuers. ZIR certifies that no part of the analysts compensation was, is, or will be, directly or indirectly, related to the specific recommendation or views expressed by the analyst in the report.

Additional information on the securities mentioned in this report is available upon request. This report is based on data obtained from sources we believe to be reliable, but is not guaranteed as to accuracy and does not purport to be complete. Any opinions expressed herein are subject to change.

ZIR is not an investment advisor and the report should not be construed as advice designed to meet the particular investment needs of any investor. Prior to making any investment decision, you are advised to consult with your broker, investment advisor, or other appropriate tax or financial professional to determine the suitability of any investment. This report and others like it are published regularly and not in response to episodic market activity or events affecting the securities industry.

This report is not to be construed as an offer or the solicitation of an offer to buy or sell the securities herein mentioned. ZIR or its officers, employees or customers may have a position long or short in the securities mentioned and buy or sell the securities from time to time. ZIR is not a broker-dealer. ZIR may enter into arms-length agreements with broker-dealers to provide this research to their clients. Zacks and its staff are not involved in investment banking activities for the stock issuer covered in this report.

ZIR uses the following rating system for the securities it covers. **Outperform-** ZIR expects that the subject company will outperform the broader U.S. equities markets over the next six to twelve months. **Neutral-** ZIR expects that the company will perform in line with the broader U.S. equities markets over the next six to twelve months. **Underperform-** ZIR expects the company will underperform the broader U.S. equities markets over the next six to twelve months.

No part of this report can be reprinted, republished or transmitted electronically without the prior written authorization of ZIR.