

Magellan Health, Inc. (MGLN)

\$57.72 (As of 05/06/20)

Price Target (6-12 Months): **\$61.00**

Long Term: 6-12 Months

Zacks Recommendation:

Neutral

(Since: 01/31/20)

Prior Recommendation: Underperform

Short Term: 1-3 Months

Zacks Rank: (1-5)

3-Hold

Zacks Style Scores:

VGM:B

Value: B

Growth: C

Momentum: C

Summary

Magellan Health's shares have underperformed its industry in a year's time. Strategic acquisitions and alliances over the years in both its segments, namely Healthcare and Pharmacy Management, led to a healthy inorganic profile through business expansion in different markets, products and service verticals. Nevertheless, its revenues are under pressure due to weak Behavioral & Specialty Healthcare and Pharmacy Management businesses. The company expects its 2020 revenues to soften due to poor contribution from its Behavioral and Specialty Healthcare business. The company's low return on equity compared with the industry average adds to the stock's unattractiveness. Suspension of share buybacks and dividend payments also makes investors shy away from parking their money in the stock.

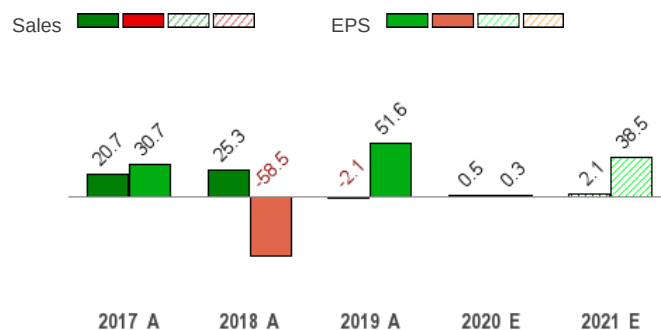
Price, Consensus & Surprise



Data Overview

52 Week High-Low	\$81.04 - \$30.60
20 Day Average Volume (sh)	185,973
Market Cap	\$1.4 B
YTD Price Change	-26.2%
Beta	1.14
Dividend / Div Yld	\$0.00 / 0.0%
Industry	<u>Medical - HMOs</u>
Zacks Industry Rank	Top 15% (39 out of 253)

Sales and EPS Growth Rates (Y/Y %)



Last EPS Surprise	29.2%
Last Sales Surprise	0.5%
EPS F1 Est- 4 week change	-1.0%
Expected Report Date	05/11/2020
Earnings ESP	39.3%
P/E TTM	15.5
P/E F1	15.4
PEG F1	0.7
P/S TTM	0.2

Sales Estimates (millions of \$)

	Q1	Q2	Q3	Q4	Annual*
2021					7,343 E
2020	1,766 E	1,790 E	1,833 E	1,807 E	7,195 E
2019	1,739 A	1,788 A	1,829 A	1,803 A	7,159 A

EPS Estimates

	Q1	Q2	Q3	Q4	Annual*
2021					\$5.18 E
2020	\$0.68 E	\$0.86 E	\$1.13 E	\$1.39 E	\$3.74 E
2019	\$0.40 A	\$0.86 A	\$1.23 A	\$1.24 A	\$3.73 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 05/06/2020. The reports text is as of 05/07/2020.

Overview

Founded in 1969, Magellan Health offers healthcare management services in the United States. It is headquartered in Scottsdale, AZ.

The company has two segments, namely, **Healthcare** (contributed 71% of the company's total 2019 revenues) and **Pharmacy Management** segments (39%).

The Healthcare segment is further broken into two reporting units — Behavioral & Specialty Health and Magellan Complete Care (MCC)

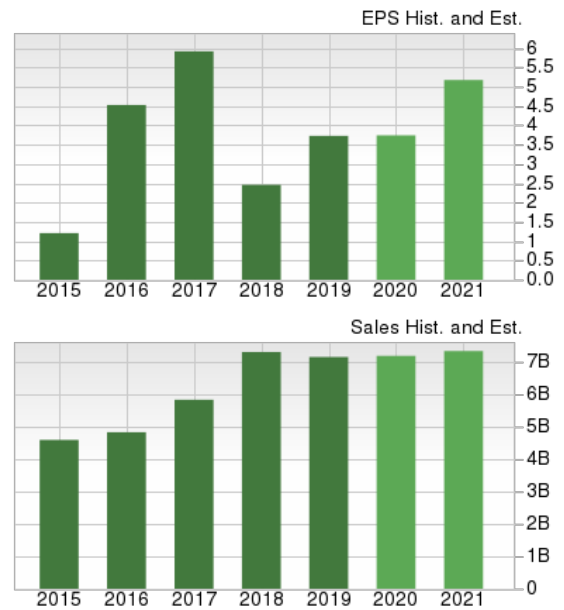
The **Behavioral & Specialty Health** reporting unit's customers include health plans, accountable care organizations, employers, state Medicaid agencies, the United States military and various federal government agencies for which Magellan provides carve-out management services for behavioral health, employee assistance plans (EAPs) and other areas of specialty healthcare including diagnostic imaging, musculoskeletal management, cardiac and physical medicine.

MCC largely focuses on managing care for special populations including individuals with serious mental illness (SMI), dual eligibles, the aged, blind and the disabled (ABD) and other populations with unique and often complex healthcare needs.

The **Pharmacy Management** segment consists of products and solutions, which provide financial and clinical management of pharmaceuticals. It offers pharmacy benefit management services, pharmacy benefit administration for state Medicaid and other government sponsored programs, pharmaceutical dispensing services, clinical and formulary management programs, medical pharmacy management programs and programs for the integrated management of specialty drugs that treat complex conditions.

These services are available individually, in combination or on a fully integrated manner. The company markets its pharmacy management services to health plans, employers, third-party administrators, state governments, Medicare Part D beneficiaries, government agencies, exchanges, brokers and consultants.

Pharmacy Management enter into contracts with its customers for services using risk-based, gain share or ASO arrangements. In addition, the Pharmacy Management segment provides services to the MCC reporting unit within the Healthcare segment.



Reasons To Buy:

▲ **Strategic Acquisitions:** Over the years, the company has expanded its capabilities through a series of acquisitions. In Healthcare segment, a number of acquisition from 2013-2017 expanded the company's MCC reporting unit. Magellan also increased its presence within the federal marketplace through the acquisition of Armed Forces Services Corporation ("AFSC") in 2016, which falls under the Behavioral & Specialty Health reporting unit. Notably, in pharmacy management, buyouts from 2013-2016 expanded the company's presence in the Pharmacy benefit management market. These transactions expanded its business portfolio, leading to long-term growth.

Magellan Health growth initiatives and strategic buyouts poise the company well for long-term growth.

▲ **Business Streamlining:** Magellan Health has entered into a definitive agreement to sell its Magellan Complete Care (MCC) business to Molina Healthcare for \$850 million. The sale eliminates the risk of Magellan's ability to execute on its MCC profitability improvement initiatives and allows the leadership team to focus on the remaining businesses which provides high returns. The transaction is expected to be completed by the end of the first quarter of 2021.

▲ **Operational Efficiency Improve:** The company continues to progress well on its operational efficiency improvements. It is working to achieve a more industry competitive administrative cost structure in 2020 and beyond. These initiatives are expected to result in cost improvement of nearly \$30 million by 2021 and nearly \$75 million by 2022. We believe these initiatives will drive margin recovery. The company targets a long-term goal of at least 2% adjusted net income margin (by 2021).

▲ **Low Debt:** The company's debt-to-equity ratio declined in 2019, strengthening its balance sheet. Its debt-to-equity ratio of 48.6% is lower than the industry average of 64%, which reduces its financial risk. Also its interest expense rose 2.1% at a much lower rate than 36.3% in 2018. This reflects the company's improved financial flexibility.

▲ **Share Price Performance:** In a year's time, the stock has underperformed its industry. Nevertheless, the company's progress on fundamentals should further aid its stock price. The company's long-term earnings growth rate of 18.6% is higher than the industry's growth rate of 13.2%.

Reasons To Sell:

- ▼ **Decline in Revenue Growth:** The company witnessed steady top-line improvement over the years, which is evident from its six-year CAGR of 14.7% (2012-2018). However, for 2019, the same was down 2% year over year. Revenues suffered decline led by loss of a health plan PBM customer due to an acquisition and the planned reduction in the geographic scope of the Company's PartD pharmacy plan. The company expects total revenues in the band of \$7 billion to \$7.4 billion for 2020, implying that revenues will remain at levels consistent with the figure reported in 2019.
- ▼ **Increase in Cost of Care and Low Profitability:** The company experienced a 4.7% increase in cost of care during 2019, which weighed on its margins due to 2.1% revenue dip. Also return on equity (ROE) undermines its growth potential. Its trailing 12-month ROE of 6.8% compares unfavorably with the industry average of 23.6%, suggesting that it is less efficient in using shareholders' funds.
- ▼ **Tepid Guidance:** Adjusted earnings per share of \$3.34 to \$4.14 are expected. The mid-point of the guidance indicates that earnings will remain flat year over year. The company also anticipates 2020 segment profit in the range of \$250 million to \$280 million, and revenues for the year in the range of \$7 billion to \$7.4 billion. The mid-point of revenue guidance also suggests no growth year over year.
- ▼ **Absence of Share Buyback and Dividends:** The company made no share repurchases during the fourth quarter of 2019 and in the first quarter of 2020. It also does not expect to pay any dividend in 2020. We perceive this suspension of share buyback and dividend payout not bode well with investors as the concerns about revenue decline and cost escalation persist.

Declining revenues, decline in earnings in Pharmacy business, low profitability makes the stock look unattractive.

Last Earnings Report

Magellan Health Q4 Earnings Beat Estimates, Rise Y/Y

Magellan Health's fourth-quarter 2019 earnings per share of \$1.24 beat the Zacks Consensus Estimate by 29.2%. Moreover, the bottom line came in against the year-ago reported loss of 77 cents per share.

Revenues of \$1.81 billion were down 2.3% year over year due to lower contribution from Managed Care and other. However, the top line beat the Zacks Consensus Estimate by 0.5%.

Segment profit of the company soared 354.4% year over year. Total costs and expenses rose 5.6% year over year due to higher cost of goods sold, and depreciation and amortization.

Full-Year Highlights

For 2019, net revenues came in at \$7.3 billion, up 2.2% year over year. Adjusted net income for the year was \$91.7 per share, surging 48.7% year over year.

Segmental profit increased 10.8% year over year to \$252.7 million. This upside can be attributable to solid contributions by Healthcare segment and Pharmacy Management segment.

For the entire year, unrestricted cash and investments totaled \$195.4 million, up 49.8% from the level at 2018 end.

Capital Position

Cash flow from operations for the year ended 2019 was \$164.8 million, up 42.3% year over year.

As of Dec 31, 2019, the company's cash and cash equivalents totaled \$272.3 million, down 16.3% from the level on Dec 31, 2018.

As of Dec 31 2019, total assets of the company dipped 3.7% to \$2.9 billion from the figure at 2018 end.

Total stockholder's equity decreased 8% year over year to \$1.3 billion at 2019 end.

2020 Guidance

For 2020, the company expects its net revenues in the band of \$7-\$7.4 billion. While adjusted net income is anticipated in the range of \$83-\$103 million, segment profit for the full year is projected from \$250 million to \$280 million.

Quarter Ending 12/2019

Report Date	Feb 28, 2020
Sales Surprise	0.50%
EPS Surprise	29.17%
Quarterly EPS	1.24
Annual EPS (TTM)	3.73

Recent News

Magellan Health Expands Telehealth Services Amid COVID-19 Outbreak — Mar 20, 2020

Magellan Healthcare, the behavioral and specialty healthcare segment of the company, expanded telehealth services and implemented additional initiatives to support clients during the novel coronavirus (COVID-19) pandemic.

Magellan Healthcare revised its operations to permit all credentialed and contracted behavioral health providers to conduct telehealth video sessions for all routine services and certain psychological testing, applied behavior analysis (ABA), intensive outpatient programs (IOP) and partial hospitalization program (PHP) services. Providers are able to use a number of HHS OCR-approved platforms to perform their telehealth video sessions. Magellan is also allowing telephone-only sessions when a member has no access to a video platform. These alternative approaches will ensure members that they get proper care in times of urgency.

Magellan Health's Arizona Unit Provides Medicare Advantage D-SNP Plan — Jan 7, 2020

Magellan Health's unit Magellan Complete Care of Arizona has enhanced its current offerings and now provides a new Medicare Advantage Dual Special Needs Plan (D-SNP) for 2020.

Magellan Health's Virginia Arm Offers Medicare Advantage D-SNP Plan — Jan 2, 2020

Magellan Health's subsidiary Magellan Complete Care of Virginia has expanded its range of current offerings and now renders a Medicare Advantage Dual Special Needs Plan (D-SNP) for 2020.

Magellan Rx Management's New Launch Provides Integrated Care Management — Nov 25, 2019

Magellan Rx Management has launched MRx Navigate, a comprehensive care management program that provides comprehensive, high-touch and high-tech solutions catering to patient wellness and simplifying member healthcare experience.

Valuation

Magellan Health shares are down 24.4% and 15.7% in the year-to-date period, and over the trailing 12-month period. Stocks in the Zacks sub-industry and the Zacks Medical sector are down 5.8% and 3.6% in the year-to-date period, respectively. Over the past year, the Zacks sub-industry and the sector is up 15.5% and 1.5%, respectively.

The S&P 500 index is down 10.9% in the year-to-date period and down 0.8% in the past year.

The stock is currently trading at 13.61x trailing a forward 12-month earnings, which compares with 15.33x for the Zacks sub-industry, 22.06x for the Zacks sector and 20.52x for the S&P 500 Index.

Over the past five years, the stock has traded as high as 44.59x and as low as 8x with a 5-year median of 16.77x. Our Neutral recommendation indicates that the stock will perform in-line with the market. Our \$61 price target reflects 14.29x forward earnings.

The table below shows summary valuation data for MGLN

Valuation Multiples - MGLN					
		Stock	Sub-Industry	Sector	S&P 500
P/E F12M	Current	13.61	15.33	22.06	20.52
	5-Year High	44.59	20.58	22.06	20.52
	5-Year Low	8	12.48	15.81	15.18
	5-Year Median	16.77	16.1	18.81	17.45
P/S F12M	Current	0.18	0.37	2.53	3.07
	5-Year High	0.41	0.84	3.84	3.44
	5-Year Low	0.11	0.33	2.25	2.54
	5-Year Median	0.28	0.53	2.95	3.01
P/B TTM	Current	0.95	3.44	4.49	4.44
	5-Year High	2.1	4.07	5.03	4.54
	5-Year Low	0.57	2.46	3.43	2.85
	5-Year Median	1.41	3.1	4.29	3.62

As of 05/06/2020

Industry Analysis Zacks Industry Rank: Top 15% (39 out of 253)



Top Peers

Company (Ticker)	Rec	Rank
Anthem Inc (ANTM)	Neutral	3
Cigna Corporation (CI)	Neutral	3
Centene Corporation (CNC)	Neutral	3
Humana Inc (HUM)	Neutral	2
The Joint Corp (JYNT)	Neutral	3
Molina Healthcare Inc (MOH)	Neutral	2
Select Medical Holdings Corporation (SEM)	Neutral	3
UnitedHealth Group Incorporated (UNH)	Neutral	3

Industry Comparison Industry: Medical - Hmos				Industry Peers		
	MGLN	X Industry	S&P 500	CI	CNC	UNH
Zacks Recommendation (Long Term)	Neutral	-	-	Neutral	Neutral	Neutral
Zacks Rank (Short Term)	3	-	-	3	3	3
VGM Score	B	-	-	A	C	C
Market Cap	1.44 B	1.67 B	19.11 B	68.22 B	37.93 B	273.59 B
# of Analysts	3	4.5	14	13	11	12
Dividend Yield	0.00%	0.00%	2.2%	0.02%	0.00%	1.50%
Value Score	B	-	-	A	B	C
Cash/Price	0.39	0.29	0.06	0.08	0.28	0.09
EV/EBITDA	5.89	8.41	11.69	7.98	14.28	12.72
PEG Ratio	0.65	0.96	2.48	0.90	0.94	1.42
Price/Book (P/B)	1.01	2.05	2.58	1.51	1.60	4.57
Price/Cash Flow (P/CF)	6.34	11.08	10.40	6.76	9.81	15.80
P/E (F1)	15.48	15.26	18.81	10.00	13.82	17.78
Price/Sales (P/S)	0.20	0.62	1.97	0.44	0.46	1.11
Earnings Yield	6.48%	6.52%	4.99%	10.00%	7.24%	5.62%
Debt/Equity	0.49	0.60	0.75	0.71	0.72	0.60
Cash Flow (\$/share)	9.10	6.68	7.01	27.12	6.68	18.28
Growth Score	C	-	-	B	D	C
Hist. EPS Growth (3-5 yrs)	-0.44%	19.97%	10.87%	19.22%	29.09%	24.13%
Proj. EPS Growth (F1/F0)	0.36%	5.42%	-9.86%	7.58%	7.26%	7.50%
Curr. Cash Flow Growth	14.08%	14.42%	5.88%	138.17%	45.38%	14.76%
Hist. Cash Flow Growth (3-5 yrs)	3.37%	13.62%	8.55%	31.41%	49.67%	19.53%
Current Ratio	1.84	1.36	1.25	0.67	1.14	0.75
Debt/Capital	32.70%	38.01%	44.23%	41.65%	42.08%	38.53%
Net Margin	0.78%	3.86%	10.87%	3.19%	1.03%	5.59%
Return on Equity	6.81%	17.56%	16.36%	15.05%	11.47%	24.86%
Sales/Assets	2.31	1.40	0.55	0.99	1.87	1.40
Proj. Sales Growth (F1/F0)	0.50%	12.88%	-2.18%	10.22%	48.48%	7.00%
Momentum Score	C	-	-	A	C	D
Daily Price Chg	-5.62%	-2.10%	-1.27%	-3.66%	-4.17%	-1.46%
1 Week Price Chg	26.04%	1.46%	0.53%	-0.59%	-7.95%	-2.33%
4 Week Price Chg	11.58%	6.82%	0.68%	-1.50%	0.54%	7.82%
12 Week Price Chg	-22.13%	-7.91%	-22.30%	-17.58%	-1.49%	-4.85%
52 Week Price Chg	-18.77%	-0.48%	-11.55%	17.20%	15.68%	20.75%
20 Day Average Volume	185,973	260,271	2,470,143	1,832,127	4,418,283	4,223,405
(F1) EPS Est 1 week change	0.00%	0.00%	0.00%	0.48%	-0.11%	-0.23%
(F1) EPS Est 4 week change	-0.97%	-1.05%	-6.52%	-0.30%	-1.56%	-1.78%
(F1) EPS Est 12 week change	-20.41%	-1.45%	-14.84%	-0.59%	-2.08%	-1.45%
(Q1) EPS Est Mthly Chg	0.00%	3.87%	-12.48%	3.68%	14.38%	3.87%

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	B
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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