



COMPUGROUP MEDICAL (COP) OVERWEIGHT

FAVORABLE LEGISLATION; GLOBAL
EXPANSION; INITIATE BUY & TARGET €90

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THESIS

We are initiating an overweight rating on CompuGroup Medical following strong Q4 and FY 20 results. We value it at 59.86x P/E with a target price of €90 based on TTM EPS of 1.51, representing a 17% upside as of February 21st, 2021. We believe that with the recent passage of the German digital healthcare act that is expected to take effect this year, coupled with recent acquisitions that CompuGroup Medical has made, there is a large opportunity for future growth.

KEY DRIVERS

Passage of the German Digital Healthcare Act. In the back half of 2019, the German parliament voted on and passed a €4.3 Billion package aimed at increasing the rate of hospital digitization in Germany. Given the large upfront cost of implementing digital health services, this act provides hospitals and patients with reimbursements from insurers to lower the cost burden and increase adoption. With CompuGroup Medical's strong presence in Germany and across the EU and the broad suite of eHealth products CompuGroup offers we expect to see revenue realization from this act to pick up around the second quarter and continue over the next few years.

Commercialization of recently launched telemedicine platform. CompuGroup Medical Launched Clickdoc, a telemedicine platform, in the back half of 2018. This product serves as a way for CompuGroup Medical to capture a portion of the telehealth market that has seen impressive growth over the past few years. The Coronavirus pandemic has sped up the adoption rate of telehealth platforms and CompuGroup Medical was well-positioned to meet this increased demand, especially in European markets. CompuGroup has drastically increased spend in the last few quarters and has offered free or discounted sign up for doctors in order to increase product awareness and drive user growth. As of May 2020, the Clickdoc platform has 80,000 registered users, and as of November 2020, the platform has 8,000 paying customers. Further commercialization of the Clickdoc platform should provide strong organic revenue growth moving into the next few quarters.

Expansion into US markets with targeted acquisitions. CompuGroup Medical has made it a priority to increase their footprint within the highly digitized US healthcare market. In the most recent quarter CompuGroup Acquired eMDs an electronic medical records software company and Schuyler House a Physician office lab company to boost their market share in the United States. These two acquisitions make CompuGroup Medical the number two player in the United States for Physician lab information systems and number four player in the Ambulatory Information systems market based on market share.

European markets remain an area of opportunity moving forward. Continued digitization efforts in the European region have been enhanced by the pandemic as healthcare systems have had to adapt to the changing environment.

PRICE:
EUR €77.00
(Reflects price on 02/21/21)

TARGET:
EUR €90

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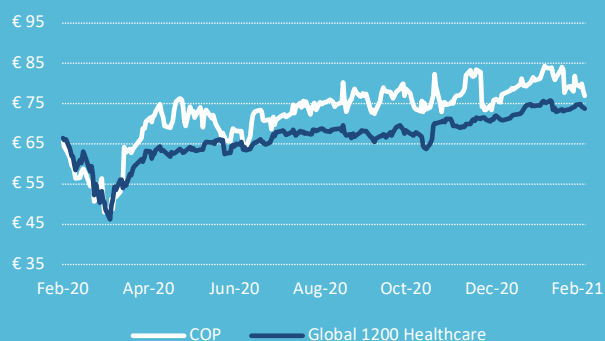
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SUMMARY

Rating	Buy
Price Target	EUR
FY20E Rev (mil)	EUR €837.26
FY20E EPS	EUR €1.88
52-Week High/Low	EUR €46.50 / EUR €85.40
Shares Out (mil)	53.7
Market cap. (mil)	EUR €4,135
Net Cash/Share	2.24
Price/Earnings	49.2
Price/Book	16.7
Price/Sales	4.9
Price/Cash Flow	30.8
EV/EBITDA	21.4
Quick ratio	0.9
Current ratio	1.0
Dividend	0.6%

COP Performance (1Y)



COMPANY OVERVIEW

CompuGroup Medical SE & Co. is a German software and information technology company that operates within the healthcare sector. Their software offerings assist physicians, dentists, pharmacists, nurses, laboratory and administrative professionals in both their medical and organizational functions. The company's information technology builds the communication infrastructure between insurance providers, pharmacies, and physicians for the safe delivery of information. They currently provide their services to clients in Germany, key European countries, Canada, and the United States. CompuGroup is headquartered in Koblenz, Germany, has offices in 18 countries, and employs more than 5,600 employees across 56 countries.

MANAGEMENT OVERVIEW

In the last few weeks, CompuGroup medical recently announced the appointment of Derek Pickell as the Chief Executive Officer for the entire CompuGroup Medical US operation, including the newly acquired eMDs and Aria Health Services business. Pickell boasts over 37 years of experience in the US Healthcare IT and technology-enabled market, bringing a wealth of knowledge and success to CompuGroup's ambitions and acquisitions in the United States. In the past, Mr. Pickell has been the CEO of eMDs, Inc overseeing significant revenue and client growth at an over 30% CAGR, positioning eMDs as a top 5 company for ambulatory software and solutions. Before joining eMDs, he was CEO of Convergent Revenue Cycle Management, Inc. where he managed the strategic direction, financial and operational performance, as well as the sales and marketing for the Healthcare Division.

Another recent addition to the CompuGroup Medical team was a new CEO Dr. Dirk Wössner, who joined CGM at the beginning of the year due to CGM's after a career in McKinsey and Deutsche Telekom. Going forward, he plans to continue the CompuGroup Medical strategy of aggressive M&A for continued market share growth and value creation in the company's core industry, stepping up R&D expenses (i.e., platform modernization and user experience) from 168 million Euros in 2020 to 200 million Euros in 2021, continuously emphasizing customer experience, and growing the company's US foothold, and strengthening marketing and distribution capabilities.

FAVORABLE INDUSTRY TRENDS

The global eHealth market is expected to grow to USD 310.09 billion by 2027, driven by the growing usage of big data, an emphasis on patient-centric healthcare delivery, an increase in government initiatives supporting the use of eHealth solutions, and the ongoing demands of the coronavirus pandemic in Europe. The EHR market size accumulated \$11.2 billion in revenue at an annual growth rate of 3% for the next 7 years and a profit margin of 15.5%. Overall the growing market possesses a high barrier to entry, low volatility, high revenue growth, and a high amount of competition.

The North America region is expected to continue to dominate the global market during the forecast period driven by rising spending on healthcare, the presence of large healthcare

companies like Cerner, a growing population of individuals with chronic disease and a high rate of hospital digitization.

Asian markets highlighted by China are expected to have the fastest rate of growth due to higher government spending to implement EHR systems in healthcare facilities, rising medical tourism, increasing per capita income, and a robust hospital network.

European markets are also expected to expand substantially in the near future due to the rising adoption of EHR systems for ambulatory care by government organizations. Looking specifically at the European market CompuGroup Medical clearly has a large area of opportunity in the EU moving forward.

The EU poses a unique opportunity for CompuGroup Medical because of the lagging ENRAM score in the EU, which measures the share of digitized hospitals in the region compared to other industrialized nations. The ENRAM score ranks hospitals from 7 or a paperless building to a 0 or a building with no digitization. As of 2017, Germany only had 1-2% of its hospitals holding an ENRAM score of 6 or 7 compared to the United States' 73%. This represents a large market for CompuGroup Medical to expand their market share. Regulatory tailwind, for example, from the Hospital Future Act in Germany that designates €4.3 billion to the digitization of German hospitals in the years to come is expected to support this measure and speed up eHealth spend.

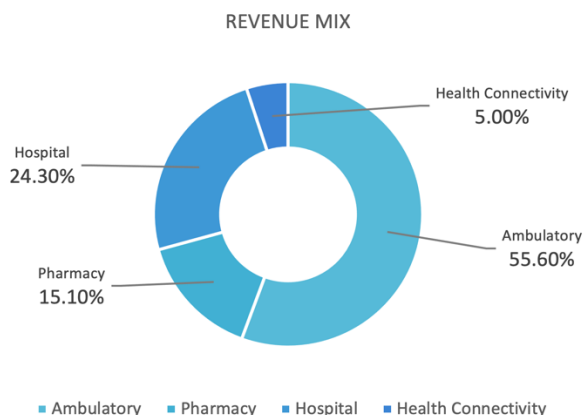
SOLID Q4 & FY 20 RESULTS; RAISED GUIDANCE

CompuGroup Medical reported Q4 and FY 20 results on February 4th. In the fourth quarter, CompuGroup Medical saw revenue increase from €231m to €243m, representing growth of 5% QoQ. Recurring revenue also saw impressive growth of 7%, increasing from €133.98m in Q3 to €143.37m in Q4. CompuGroup also saw double-digit growth in three out of its four revenue segments. The health connectivity segment saw quarterly revenue growth of 29%, the pharmacy information systems saw quarterly growth of 17%, and the pharmacy information systems grew 12% QoQ.

In the most recent quarterly conference, call management raised guidance for the upcoming year, citing tailwinds in their Ambulatory information systems and Hospital information systems segments. Management expects total revenue in 2021 to range from €1 Billion to €1,040 Billion and adjusted EBITDA to range from €210 Million to €230 Million. This guidance would represent 20% YoY revenue growth and adjusted EBITDA growth of around 5% YoY. Management reaffirmed that the revenue realization potential from the monetization of the Clickdoc platform would begin to kick in during the middle half of 2021, and revenue from the German Digital Healthcare will be realized in the back half of 2021. Management has noted that both of these should drive double-digit organic growth levels this year. This guidance confirms that the initiatives that CompuGroup Medical is undertaking have positioned them well for sustained growth for years to come.

DIVERSE REVENUE STREAMS

CompuGroup's revenue is generated from the creation and sales of information technology services to the healthcare sector and is categorized into the Ambulatory Information Systems (AIS), Hospital Information Systems (HIS), Pharmacy Information Systems (PCS), and Health Connectivity Services (CHS) segments. The firm reported €837M in sales in FY20 of which AIS makes up the largest segment followed by HIS, PCS, and HCS.

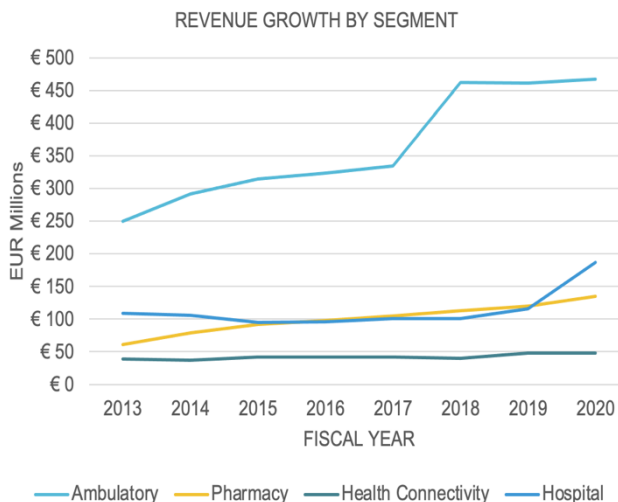


The AIS revenue segment focuses on providing management software and electronic billing services to primary care physicians throughout the healthcare field. The provided services encompass the entire patient cycle from administrative and clinical needs to the billing process through their MEDEDI, Medistar, XDENT, Practice Perfect, and Professional Medical Office (PMO) software. Each of their platforms caters to a different area within healthcare such as PMO focusing on specialty physicians and XDENT focusing on dentists. This segment has seen a revenue increase of 87% from FY13 to FY20, raising it from €250M to €467M. This rise is expected to increase in the next few quarters as the recent acquisition of MDeverywhere Midco Inc., U.S. information systems platform, has increased the firm's market penetration into the largest healthcare sector providing a large upside opportunity. Continued digitization efforts throughout Europe will also be a large area for organic revenue growth.

The HIS revenue segment caters to secondary care institutions with inpatients that require extended periods of care. Services range from planning, administrative, clinical, and billing needs for rehabilitation centers, hospitals, regional care, and social services. HIS has grown 71.19% from FY13 to FY20 and makes up the second largest segment of CMG's revenue mix. This is its first year as the second largest segment with it experiencing 60.86% revenue growth this fiscal year. This significant growth level is largely driven by the firm's acquisition of the IT Healthcare portfolio from Cerner Corporation. Also, the Hospital future Act, a €4B healthcare digitization investment in Germany, is expected to further boost revenue growth in the near future. The recent acquisition of U.S. based Schuyler House has positioned the company as the number one laboratory information systems provider in the United States and is expected to further boost revenue growth.

The PCS segment specifically caters to the clinical, administrative, and billing needs of pharmacies. Their services increase the internal and external communication processes of pharmacies enabling them to optimize their supply chain, medical dispensement, and cost structures. The pharmacy Telematics Infrastructure (IT) system which provides fast and safe information between pharmacies and physicians has been aggressively expanded to increase market share and the subsequent network effect. The firm has also begun working with IhreApotheken.de, a German pharmacy portal, to connect with their own CLICKDOC software to allow patients to rapidly redeem pharmacy prescriptions at their desired location. This segment has experienced a 122% increase in revenue from FY13 to FY20 and makes up the third largest revenue source.

CHS focuses on non-healthcare providing clients such as pharmaceutical firms, insurance providers, and individual consumers. CHS creates the reliable and safe communication channel between pharmaceutical firms, insurance providers, and doctors while also providing market study and clinical trial information. This segment also provides record-keeping services to other information technology companies in the form of health records and access portals. The company has seen growing success with their CLICKDOC system which provides video consultation services and information transfer between consumers and physicians. As the smallest revenue segment, CHS has seen a 23% growth in sales from FY13 to FY20.

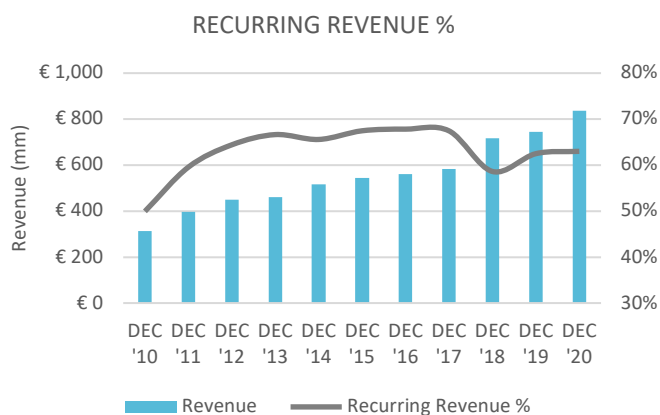


COMMITMENT TO GROWING RECURRING REVENUE BASE

Management has made it a priority to increase the amount of recurring revenue as a percent of total sales. Over the past decade, recurring revenue has grown at a CAGR of 11.78% and currently makes up 63% of total revenue, up from 50% of total revenue a decade ago.

The eHealth industry that CompuGroup operates in is software and services that are critical for healthcare providers. The critical nature of these software and services leads to a sticky customer base as the ease of switching between software providers is limited. When hospitals, pharmacies, and physicians implement CompuGroup products, they are incentivized to continue using its whole suite of products.

CompuGroup Medical has made several acquisitions in recent years to transition its business towards being a software and eHealth services company instead of a hardware and IT services company. As a result, CompuGroup has seen an improvement in margins and an increase in the percent of recurring revenue. As shown in the chart below, recurring revenue as a % of total revenue has increased gradually over the years along with revenue, and management expects this trend to continue over the next few years.



SHIFT TOWARDS CLOUD AND SAAS PRODUCTS

With the eHealth and healthcare industry continually evolving and innovating, software providers must also continue to innovate by introducing new products and services. CompuGroup Medicals' first SaaS offering is the Clickdoc telemedicine platform that was launched in late 2018. This product serves as an opportunity to connect doctors with patients globally and on-demand. In addition to this, the company also announced planned partnership cooperation with NOWEDA, operator of the online portal IhreApotheken.de. The goal is the further joint digitalization of the patient journey. By combining IhreApotheken.de and CompuGroup Medical's CLICKDOC system, it is theorized to be possible in the future to order drugs in local pharmacies where it is legally allowed. The planned cooperation will enable ordering medicines and the redemption of prescriptions via CLICKDOC in the chosen pharmacy.

In CompuGroup Medicals most recent quarterly conference call management team has reaffirmed its ambitions to bolster its product offerings in the SaaS and cloud space. Management expects to roll out more product offerings towards the back half of 2021 and realize revenue from this initiative by the second quarter of 2022.

DCF MODEL BREAKDOWN

Impressive Revenue Growth

Our model includes managements guidance for a large increase in revenue growth into the next year. Based on management's guidance we project revenue growth of 20% for next year would mean an increase from €837 Million to €1 Billion. Our model assumes modest revenue growth into 2022 that eventually stabilizes at around 4% in the terminal year. We

are projecting a short-term annual growth rate of around 9% which would be slightly lower than CompuGroup Medicals five-year average. As CompuGroup makes a shift to SaaS and cloud-based healthcare products we should expect to see higher margins and an increase in the percent of recurring revenue that the firm generates.

Despite our long-term optimism on higher operating margins, in the short term we expect a slight decline in margins over the next few quarters as CompuGroup intensifies marketing surrounding the Clickdoc platform. Management also expects operating margin pressures as they continue to build out their Telematics infrastructure.

WACC LONG-TERM GROWTH RATE & TAX RATE

Our valuation model uses a 6.5% weighted average cost of capital that was referenced from the FactSet database. While this WACC may seem aggressive, we feel that given the dominant position within its industry, high recurring revenue rate, and stable business model, this weighted average cost of capital is warranted. Our long-term growth rate of 3% was calculated based on our belief that CompuGroup will be able to grow in line with the average global GDP growth rate in perpetuity.

The tax rate assumption in our model is based on management's guidance that the firms tax rate will remain in line with previous years. Therefore, our tax rate assumption is the 5Y average tax rate of CompuGroup which stands at 37%.

A VALUE-DRIVEN APPROACH

Our base case valuation for CompuGroup Medical stands at €90, representing a price to value of 0.85. This base case valuation is based on a perpetuity growth rate of 3% and a weighted average cost of capital of 6.5%. This assumes a short-term decrease in operating margins as management ramps up selling expenses and top-line growth numbers that are in line with management's expectations.

Our upside valuation case of €105.36 represents quicker than expected revenue recognition from the Clickdoc platform and from product orders relating to the German digital healthcare act. This upside case also assumes higher than expected operating margins based on lower costs from the telematics infrastructure upgrade.

Our downside valuation of €68.72 reflects higher than expected costs associated with the telematics infrastructure upgrade and the Clickdoc platform. This assumption also recognizes softer than expected revenue from the recently acquired US based units.



COMPETITIVE LANDSCAPE

The electronic medical records system industry is characterized by a medium to high level of market share concentration and a high degree of internal competition from established brands. While many industry operators control a large share of either the ambulatory or inpatient software market, few companies command a large share of the electronic health record (EHR) software market. All of these companies have access to a highly skilled digital workforce, an established brand name in data security, compliance with government regulation, and access to vast R&D funding.

One of COP's biggest global competitors is Cegedim, an innovative technology and services company in the field of digital data flow management for healthcare ecosystems. The company reports a lower price of 23.50 euros per share, a smaller market cap of 326 million Euros (COP's market cap is 4295 million Euros), and an EBIT of 27.9 million Euros.

Another competitor to consider, especially considering COP's expansion into the US is Cerner, one of the foremost suppliers of health information technology services, devices, and hardware in the United States, commanding a market share of 20%. Cerner boasts a share price of 79.82 dollars, a market capitalization of 25 billion dollars, and an EBIT of 834 million dollars. Furthermore, while most industry operators only operate domestically, Cerner Corporation operates globally in over 25,000 facilities worldwide. Unfortunately, the company's industry-relevant operating income has not performed as well as its revenue, declining over the past five years and by 15% in 2020.

Another major competitor is Epic Systems Corporation, a private leading software provider for midsize to large medical organizations specializing in developing, installing, supporting software to over 4.6 million patients. The company controls a market share of 24.2% and its EpicCare Ambulatory Electronic Medical Record product is highly rated by clinical and technical staff alike, which has led to significant adoption across the ambulance sector. In terms of revenue, Epic Systems has risen at an annual rate of 9.8% to 2.7 billion dollars due to federal incentives to adapt EHR systems and winning contracts with major hospitals.

The last major competitor is Allscripts Healthcare Solutions Inc., a provider of clinical, financial, data analytics solutions to numerous healthcare providers with major clients including North Shore LIJ Health System, Memorial Sloan Kettering Cancer Center, Orlando Health and Children's Hospital of Wisconsin in Milwaukee. The company's industry-relevant revenue has grown at an annualized rate of 9.0% to \$1.6 billion over the five years to 2020, has amassed a market share of 14.1%, and has a market cap of 2.7 billion.

RISK FACTORS

One of the risks facing CompuGroup medical is potential currency headwinds due to the two acquisitions that were made over the last two quarters. The acquisitions of eMDs and Schuyler House increases CompuGroup Medicals' exposure to the United States market. Currently, 93% of revenue comes from European regions while only 7% comes from United States markets. We expect CompuGroup to continue to increase its exposure in US markets which could increase potential foreign currency exchange risk. We believe that this risk is the least probable in the short term and would not have a great deal of impact on operations.

Another potential risk is concern surrounding valuation. Although we believe that CompuGroup Medical deserves to trade at a premium relative to its peers, there is a chance that the market could derate the company in the short term.

Given the acquisition-based nature of CompuGroup, there is a clear risk of overpaying for an acquisition. A rise in rates could also limit CompuGroup Medicals ability to obtain reasonable financing to complete an acquisition. This risk is the most highly probable and would likely present the most significant risk.

The final risk is a risk of increased competition in the eHealth space. As discussed earlier in the report, given the critical nature of the software and services that CompuGroup Medical provides hospitals, physicians, and pharmacies, we believe they have a sticky customer base.

RISK SCORECARD

