

## Select Medical Corp.

## Spin-off could unlock Concentra's value

Reiterate Rating: BUY | PO: 29.00 USD | Price: 25.78 USD

## The spin off not a complete surprise; goal to unlock value

SEM announced plans to spin off Concentra into a publicly traded company, which is not a complete surprise to us as the company previously indicated it believes the asset is undervalued. We do not expect this to be a deleveraging event (SEM is levered at 5x) but rather a way to make it easier for the market to value Concentra. While there are no direct comps, health care services companies with similar margins and payor mix trade at a premium to SEM (10x+ vs SEM at 8x EBITDA). We reiterate our Buy rating on SEM as we see the improvement in labor combined with commercial re-pricing as drivers of upside over time.

## Concentra has healthy margins, commercial payor mix

Concentra is the largest provider of occupational medicine providing occupational health, urgent care, physical therapy, drug screening, and physical exams through 540 medical centers and 140 onsite clinics at employer locations as well as telemedicine. With payor mix heavily weighted towards commercial payors (Workers' comp is 59% of Concentra's revs), segment margins are well above average, at 20% for Concentra (16% after allocating corporate overhead) vs SEM consolidated margin at 12%. Concentra accounts for 27% of SEM's revenues and 44% of Adj EBITDA given the depressed margins at Critical Illness Recovery Hospital segment. SEM would exit the occupational business after owning it for 9 years with margins improved from 8-9% before the acquisition from Humana (HUM) in 2015.

## Indirect peers trade at 10x+ EBITDA multiple

With no other publicly traded occupational therapy company, we point to a pure-play rehab therapy provider, USPH, as a close comp given its 21% EBITDA margin, payor mix skewed towards commercial (47% of revenues, workers comp 10%), and a consolidation opportunity. USPH is trading at 10x 2023E EBITDA. However, it is not clear what leverage the standalone Concentra would have while USPH has a below average leverage (3x). Other potential comps would be ACHC (margins in the 20% range) – trading at 12x, and SGRY (payor mix skewed towards commercial payors) – trading at 14x.

04 January 2024

## Equity

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## Stock Data

Price	25.78 USD
Price Objective	29.00 USD
Date Established	3-Nov-2023
Investment Opinion	B-1-7
52-Week Range	21.28 USD - 33.51 USD
Mrkt Val (mn) / Shares Out (mn)	3,299 USD / 128.0
Free Float	82.0%
Average Daily Value (mn)	14.55 USD
BofA Ticker / Exchange	SEM / NYS
Bloomberg / Reuters	SEM US / SEM.N
ROE (2023E)	17.4%
Net Dbt to Eqty (Dec-2022A)	274.2%
ESGMeter™	Medium

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SEM = Select Medical

USPH = US Physical Therapy

ACHC = Acadia Healthcare

SGRY = Surgery Partners

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Timestamp: 04 January 2024 10:33AM EST

## Price objective basis & risk

### Select Medical Corp. (SEM)

Our \$29 PO is based on 8.9x our 2024E Adjusted EBITDA less Non-Controlling Interest estimate, towards the middle of its historical 7.5-10x range, which we think is justified given the strong performance in outpatient businesses offsetting weaker inpatient margins.

Upside risks to our PO are outperformance in CIRH and IRF segments, better-than-expected Medicare rates, faster rebound to volumes, or larger-than-expected cost offsets (especially in labor).

Downside risks to our PO are: continued labor disruption, COVID disruption, Medicare rate pressure, lower-than-expected cost saves from labor during a recession, a recession impacting growth, high leverage and execution risk on deals.

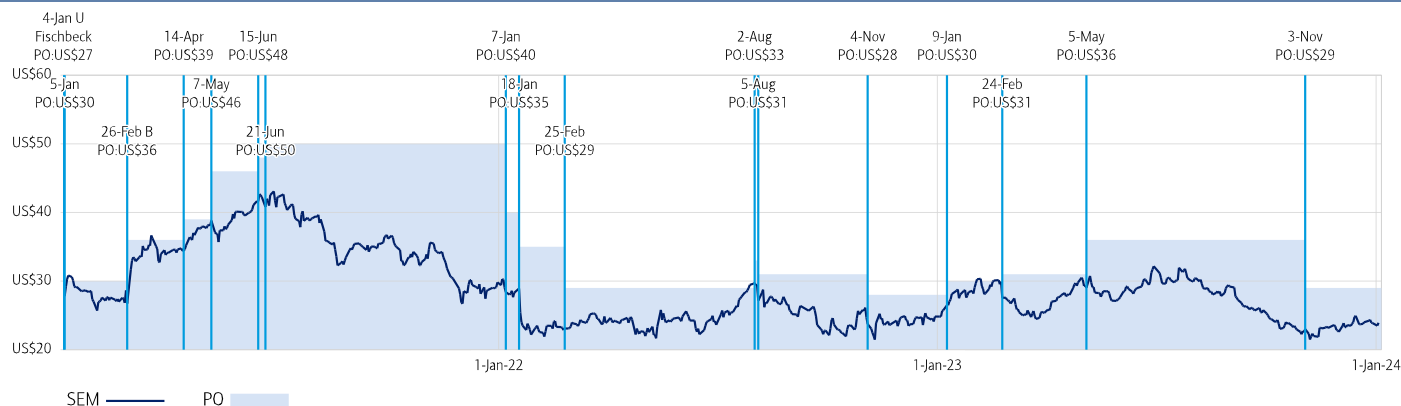
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### Select Medical (SEM) Price Chart



SEM — PO

B: Buy, N: Neutral, U: Underperform, PO: Price Objective, NA: No longer valid, NR: No Rating

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### Equity Investment Rating Distribution: Health Care Group (as of 31 Dec 2023)

Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	234	60.94%	Buy	115	49.15%
Hold	80	20.83%	Hold	36	45.00%
Sell	70	18.23%	Sell	29	41.43%

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Coverage Universe	Count	Percent	Inv. Banking Relationships <sup>R1</sup>	Count	Percent
Buy	1895	53.62%	Buy	1083	57.15%
Hold	832	23.54%	Hold	454	54.57%
Sell	807	22.84%	Sell	383	47.46%

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Neutral	≥ 0%	≤ 30%
Underperform	N/A	≥ 20%

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