

Quipt Home Medical Corp.

(QIPT-TSXX: C\$8.00) (QIPT-NASDAQ: US\$6.06) *intraday*

May 16, 2023

BUY

Target: C\$13.50

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Solid Q2/F23; Index Inclusion a Potential NT Catalyst

Key metrics (all in USD):

- **Sales** of \$58.1 MM were slightly better than our estimate of \$56.8 MM and consensus of \$57.1 MM, and grew by 73% y/y. We note that Q2/F23 included nearly a full-quarter's contribution from Great Elm Healthcare, QIPT's largest-ever acquisition that added \$60 MM of annual sales and \$13 MM of adj. EBITDA. Organic growth was 2.5% q/q, of which approximately 2% was due to Medicare pricing adjustments. The Company remains on track to meet or exceed its historic 8-10% organic growth rates, driven by CPI-based adjustments to Medicare reimbursement rates, the amelioration of recent supply chain issues, and baseline demand growth for respiratory products. Recurring revenue ticked up slightly to 78% of sales (Q1/F23 - 77%), which we attribute to the inclusion of Great Elm.
- **Adj. EBITDA** of \$13.1 MM (22.5% margin) was in-line with our estimate but topped consensus (range: \$11.7 - \$13.6 MM), growing by 86% y/y. Margin rate improved by 50 bps sequentially and ~150 bps y/y as the business continued to realize scale benefits. The Company also achieved \$2 MM in synergies from the Great Elm acquisition ahead of schedule, contributing to the margin lift. Bad debt expense improved to 4.2% of sales from 5.6% in the prior quarter and 9.4% in the prior year period, reflecting the quality of QIPT's growth.
- **Balance sheet and cash flow:** Pro forma for the Company's April equity financing, QIPT currently has \$18 MM of cash on hand plus \$41 MM available on its senior credit facility. QIPT ended the quarter with \$91 MM of debt (\$107 MM including leases), but we estimate that it paid down ~\$13 MM subsequent to quarter end, bringing net leverage to 1.5x run-rate EBITDA. Management does not plan to pay down additional debt, preferring to keep cash on hand for potential M&A. Operating cash flow in Q1 was \$10 MM and capex was \$3.6 MM. The Company announced that it initiated an at-the-market (ATM) equity program, to provide balance sheet flexibility for future M&A, though it does not currently have plans to use it.

Outlook: Management is optimistic that QIPT can outpace its historic organic growth rate of 8-10% as it works to expand its sales team, acquire new payor contracts, and take advantage of highly favourable regulatory developments. Margins are expected to remain strong as the business continues to realize scale benefits, supported by a continued focus on operating efficiency, cost control, and technology implementation. The integration of Great Elm is progressing ahead of schedule, and management remains focused on executing additional M&A, with the potential for another large acquisition vs. exclusively tuck-ins. The Company believes there are still 12 - 15 states outside of its existing footprint that would represent attractive expansion markets, based on its criteria, that include a high prevalence of respiratory illness and aging populations.

Figure 1: Summary Results

QIPT-CA	Q2/F23 (Mar. '23)					Prior Quarter	Q/Q Change	Prior Year	Y/Y Change
	Actual	Eight Capital	Variance	Consensus Estimate	Variance				
Sales	\$58.1	\$56.8	2%	\$57.1	2%	\$40.8	42%	\$33.6	73%
Gross Profit	\$43.2	\$43.3	(0%)	\$43.8	(1%)	\$30.7	41%	\$26.2	65%
<i>Gross Profit %</i>	74%	76%	-191 bps	77%	-236 bps	75%	-97 bps	78%	-373 bps
Adj. EBITDA	\$13.1	\$12.9	1%	\$12.6	4%	\$9.0	46%	\$7.0	86%
<i>Adj. EBITDA %</i>	22.5%	22.8%	-22 bps	22.1%	47 bps	22.0%	50 bps	21.0%	153 bps

Amounts in USD millions

Source: Company reports, Factset, Eight Capital

Valuation: QIPT currently trades at 5.4x F2024E EV/EBITDA (Figure 5) vs. Healthcare Supplies and Services peers at 11x. Our \$13.50 target price is based on 11x EV/2023E EBITDA.

Russell 2000 Index Inclusion Could Create 4 MM+ Shares Worth of Buying Demand

New Index Additions Begin to be Announced this Friday, May 19

We believe that QIPT is a likely candidate to be added to the Russell 2000 Index during its annual reconstitution process, based on the substantial increase in its market cap compared to last year. New additions to the index begin to be announced publicly on May 19 (this Friday; see Figure 3). With \$275 B of passive index funds tracking the index, we estimate that QIPT's inclusion could create 4.4 MM shares (22 trading days) worth of demand based on QIPT's estimated weighting in the index (Figure 2). Relatively thin trading volume in QIPT shares has the potential to exacerbate a supply/demand imbalance. This catalyst dovetails with QIPT's announcement this month that it received conditional approval to graduate from the TSXV to the TSX, which could likewise improve liquidity and institutional participation.

The Russell 3000 index is a market-cap-weighted index that contains the largest 3000 U.S. public companies, representing 96% of the investible U.S. equity market. The index is subdivided into the Russell 1000 (largest 1000 stocks) and the Russell 2000 (smallest 2000 of the Russell 3000). Every year in May/June the index undertakes a reconstitution process whereby it replaces companies that have fallen outside of the top 3000 with larger ones not currently in the index. We note that the lower market cap bound of the Russell 2000 last year was US\$240 MM, with the index falling by ~5% in the interim, whereas QIPT's market cap was US\$250 MM on April 28, 2023 (the index's ranking day).

Figure 2: Inclusion in Russell 2000 Index Could Create 21 Days' Worth of Demand for QIPT Shares

<i>All in US\$</i>		
QIPT Market Cap		\$250 Million
Russell 2000 Market Cap	÷	\$2.6 Trillion
QIPT Weighting in Russell 2000		0.0096%
AUM of Passive Index Funds Tracking Russell 2000 ⁽¹⁾	x	\$275 Billion
Implied Value of QIPT Shares to be Purchased by Passive Funds		\$26 Million
QIPT Share Price (US\$)	÷	\$6.06
Implied # of QIPT Shares to be Purchased by Passive Funds		4,363,417
Average Daily Volume (TSX + NASDAQ, 90d)	÷	195,000
Days to Cover	=	22.4

1) As of June 30, 2022. Includes funds tracking the Russell 2000 Index and Russell 2000 Value Index.

Source: Russell, Factset, Eight Capital

Figure 3: Key Dates for Russell Index Annual Reconstitution Process

Date	Event
April 28, 2023	"Ranking Day": U.S. public companies are ranked in order of size
May 19, 2023	Preliminary lists of reconstituted index constituents are communicated to the marketplace
May 26, June 2, June 9, June 16, June 23	Updates are provided on these dates
June 23, 2023	Newly reconstituted indexes take effect after market closes this date

Source: Russell, Eight Capital

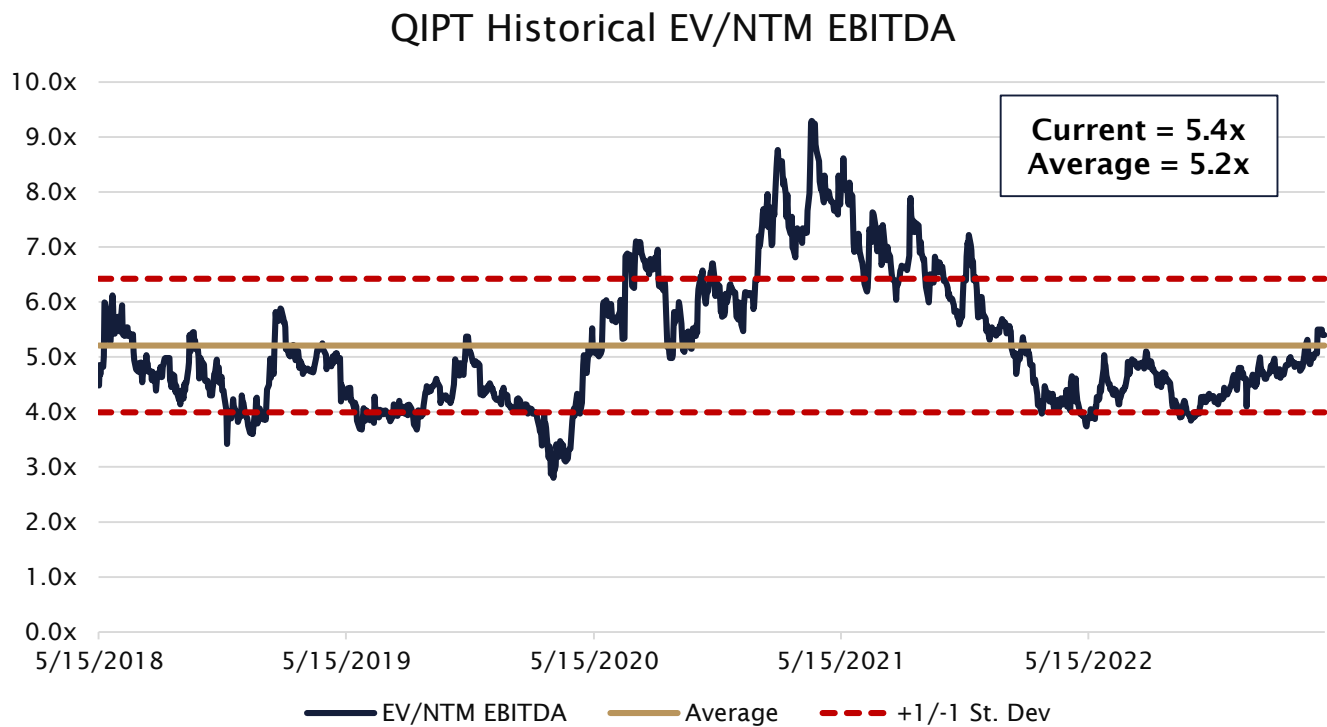
Figure 4: Estimate Revisions

QIPT-CA	June-23 Q3/F23E		Sept-23 Q4/F23E		Sept-23 F2023E		Sept-24 F2024E	
	Old	New	Old	New	Old	New	Old	New
Revenue	\$58.5	\$59.6	\$61.1	\$62.3	\$217.2	\$220.8	\$257.4	\$262.1
Adj. EBITDA	\$13.7	\$13.7	\$14.7	\$15.1	\$50.3	\$50.9	\$59.2	\$61.2
Adj. EBITDA Margin	23.4%	23.0%	24.0%	24.3%	23.1%	23.1%	23.0%	23.4%
Diluted EPS	\$0.02	\$0.00	\$0.03	\$0.03	\$0.09	\$0.03	\$0.26	\$0.19

(US \$MM, unless otherwise noted)

Source: Eight Capital

Figure 5: Historical Valuation



Source: Factset, Eight Capital

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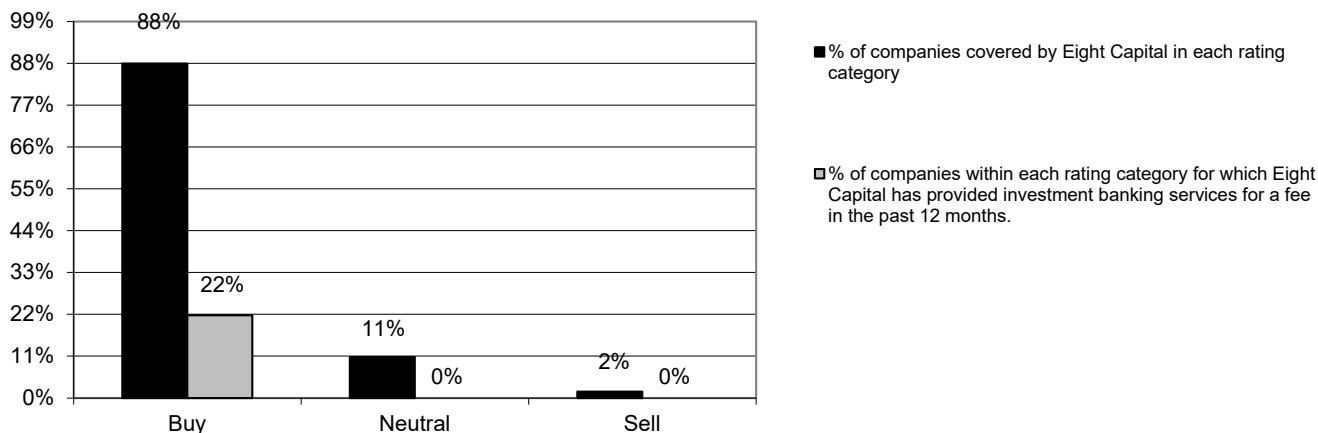
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