CONCORD MEDICAL SERVICES HOLDINGS LIMITED

Concord Medical Services Has All The Metrics Of A Value Stock

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SEEKING ALPHA

Concord Medical Services (CCM) is *almost a* classic deep value stock. Let me give you the rundown, then get to the 'almost.'

CCM stock IPO'ed at eleven dollars on the NYSE in December 2009. Since IPO, the company has dropped to three dollars and change, despite slowly but surely executing its intended business plan to operate a network of radiotherapy and diagnostic imaging centers (and soon to be hospitals).

Basically, CCM leases expensive medical equipment and provides management services to its hospital partners. From its 20-F:

... we receive a contracted percentage of each center's revenue net of specified operating expenses. Each center is located on the premises of our hospital partners and is typically equipped with a primary unit of advanced radiotherapy or diagnostic imaging equipment, such as a linear accelerator, head gamma knife system, body gamma knife system, positron emission tomography-computed tomography scanner, or PET-CT scanner, or magnetic resonance imaging scanner, or MRI scanner. We provide clinical support services to doctors who work in the centers in our network, which include developing treatment protocols for doctors and organizing joint diagnosis between doctors in our network and clinical research. In addition, we help recruit and determine the compensation of doctors and other medical personnel in our network and are typically in charge of most of the non-clinical aspects of the centers' daily operations, including marketing, training and administrative duties. Our hospital partners are responsible for the centers' clinical activities, the medical decisions made by doctors, and the employment of the doctors in accordance with regulations.

With a PE of just over 7, a forward PE of just over 6, and a price to book of < 0.5, the stock has all the metrics of a value stock. What's more, the company just paid a 0.19 special dividend and approved a $20 million share buyback -- at current prices that is roughly 13% of the market cap and 1/3 (!) of the free float.

Now that I hopefully have you interested, here is the negative part, and it is important. The company operates in China and was cited by its auditor Ernst and Young for a lack of appropriate staff with US accounting knowledge. Given all the reverse merger scams, I would not blame you for running for the hills, but there are several reasons for why I think this stock is different:

1. CCM was a sponsored IPO with top-tier lead underwriters JP Morgan and Morgan Stanley, who did due diligence on the company. It was NOT formed from a reverse merger, and it is still listed on the NYSE.
2. Unlike the problematic Chinese reverse mergers, short interest on CCM is basically nil. This means that the (usually) smart money is not betting against the company. While this does not guarantee legitimacy, it at least indicates that no one has been able to establish fraud to the extent they are willing to bet on it.
3. In a similar vein, the company is getting very little interest overall right now. I like that. There have been no substantive articles in the past 6 months. The time to buy value stocks is when nobody is paying attention. Although I suppose this post invalidates that argument to a certain extent, at least people can evaluate the stock near its lows with very little current interest aside from this post.
4. Money talks. The company bought back 1.7 million shares last year, just paid a 0.18 special dividend this year, and just announced a $20 million stock buyback. A clear warning sign that a company is a potential fraud is that it does not buy back stock despite "no-brainer" value metrics. On the other hand, if a company is not legitimate, why waste money on its shareholders rather than siphoning it off to employees? That the company is willing to intelligently spend substantial cash on its shareholders provides me an indication that it is legitimate.

Assuming the company is legitimate, I think a bet on private healthcare for Chinese citizens is not the worst place to be. Many Chinese are getting richer and will be expected to consume more healthcare, although there are the usual emerging market investment issues including regulatory and other risks. And with the valuation as low as it is, there is some margin of safety (again assuming the company is legitimate).

Net net, I believe (but am not certain) that the company is legitimate and, more than that, I believe that it is run in the best interests of its shareholders with a business model that seems reasonable. I have made an investment in the firm, but certainly understand why many would choose not to. It is not a "widows and orphans" stock, and I doubt that even the classic value investor Benjamin Graham would invest due to the risks of investing in smallcap Chinese companies. For Graham, the threat of bad financials would ensure that no smallcap Chinese company could have enough margin of safety. In Graham's terminology, I would call this a speculation that is grounded on principles of value, but nevertheless a speculation.

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