Medical Facilities Corporation (TSX: DR) Initial Screen

High-quality, specialty surgery hospital operator trading at 7.5x FCF with significant upside optionality

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Key Ratio and Statistics (CAD)

Recommendation	**Buy**	TEV/Revenue	0.7x
Market Cap	222.2mm	TEV/EBITDA	3.5x
52-Week Low	7.80	P/E	32.6x
52-Week High	10.15	Total Debt/EBITDA	1.5x
Share Price	9.03	Date	5/10/2024

Executive Summary:

Medical Facilities is a small-cap Canadian listed owner and operator of five specialty surgery hospitals (SSHs) across the mid-west. These surgical hospitals are exclusively focused on orthopedic and spinal surgery and are some of the best hospitals in the respective states in which they operate. All of MFC's hospitals have minority physician ownership, which creates a robust regional moat with minimal physician churn. MFC's poor performance stems from financial challenges that started in Q12019 after a poor acquisition. In response to these challenges, MFC underwent a strategic shift. Following the divestiture of non-core assets, the company suspended acquisitions, reduced overhead costs, and initiated share buybacks and debt repayments. Our investment thesis revolves around the imminent sale of MFC's remaining core SSHs. This strategic move aligns with the company's commitment to wind down the business and return capital to shareholders.

Business Overview:

Medical Facilities Corporation (MFC), in partnership with physicians, owns a diverse portfolio of highly rated, high-quality surgical facilities in the United States through its wholly owned US-based subsidiaries. MFC's ownership includes controlling interest in four specialty surgical hospitals (SSH) in Arkansas, Oklahoma, and South Dakota and an ambulatory surgery center (ASC) in California.

Summary of Facility Information as of September 30, 2023	Arkansas Surgical Hospital (ASH)	Oklahoma Spine Hospital (OSH)	Black Hills Surgical Hospital (BHSH)	Sioux Falls Specialty Hospital (SFSH)	Surgery Center of Newport Coast (SCNC)
Location	North Little Rock	Oklahoma City	Rapid City	Sioux Falls	Newport Beach
Year Opened	2005	1999	1997	1985	2004
Year Acquired by the Corporation	2012	2005	2004	2004	2008
Ownership Interest	51.00%	64.00%	54.20%	51.00%	51.00%
Non-controlling Interest	49.00%	36.00%	45.80%	49.00%	49.00%
Exchangeable Interest	5.00%	1.00%	10.80%	14.00%	-
Size (sq ft)	126000	61000	86000	76000	7000
Operating/Procedure Rooms	13/2	7/2	11/1	15/1	2/1
Overnight Rooms	41	25	26	33	-

Figure 1: Summary of MFC Facilities

Non-controlling interests in the facilities are indirectly owned, primarily by physicians practicing at the facilities. Upon MFC's acquisition of indirect controlling interests in the SSHs located in Arkansas, Oklahoma, and South Dakota, the non-controlling interest shareholders were granted the right to exchange between 1.00% to 14.00% of the ownership interest in their respective facilities for common shares of the corporation. The liability associated with this derivative instrument is recorded on the consolidated balance sheet.

Figure 2 below provides a more comprehensive breakdown of the revenue contribution by facility.

Revenue Contribution By Facility (In thousands of U.S. dollars)	Nine Months Ended September 30,				% of revenue
	2023	2022	$ Change	% Change	(2023)
ASH	66,623	56,240	10,383	18.46%	20.61%
OSH	58,461	56,319	2,142	3.80%	18.08%
BHSH	75,825	71,308	4,517	6.33%	23.45%
SFSH	103,537	96,963	6,574	6.78%	32.02%
SCNC	7,223	8,226	(1,003)	-12.19%	2.23%
MFC Nueterra ASCs	11,648	18,234	(6,586)	-36.12%	3.60%
Total revenue and other income	**323,317**	**307,290**	**16,027**	**5.22%**	

Figure 2: Revenue Contribution by Facility FY2022 – FY2023 (9M)

Summary of Exited Assets as of Septmeber 30, 2023	Date Exited	C.O.I (%) Prior to Sale	Sale Proceeds ($, mm)	Pre-tax Gain on Sale	Notes
Eastwind Surgical	5/5/23	N/A	-	-	Permanently Closed
Riverview Ambulatory Surgical Center	6/30/23	N/A	-	-	Permanently Closed
City Place Surgery & St. Luke's Surgery Center	7/1/23	30.30%	1.40	1.10	Buyer Assumed debt of $5mm
Miracle Hills Surgery Center	7/31/23	58.70%	1	0.6	-
Brookside Surgery Center	8/25/23	49.60%	1.1	0.8	-

Figure 3: Summary of Exited MFC Facilities

In addition, through a partnership with NueHealth LLC MFC used to own controlling interest in four ASCs located in Michigan, Missouri, Nebraska, and Pennsylvania. This has been part of a strategy to divest non-core assets that were not efficiently run and profitable. Figure 2 summarizes the assets that were divested during FY2023.

The SSHs perform scheduled surgical, imaging, diagnostic, and other procedures, including primary and urgent care, and derive their revenue from the fees charged for the use of their facilities. The ASCs specialize in outpatient surgical procedures, with patient stays of less than 24 hours, whereas SSHs are licensed for both inpatient and outpatient surgeries. The facilities mainly focus on limited clinical specialties, such as orthopedics, neurosurgery, pain management, and other non-emergency elective procedures. In addition to this, two of the SSHs provide urgent care services.

What Went Wrong at MFC?

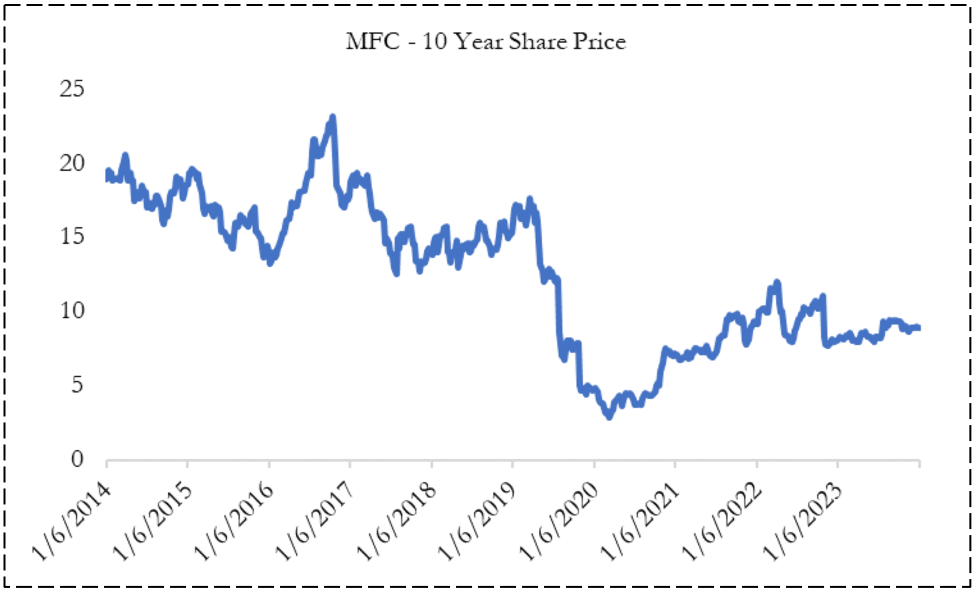

Figure 4: MFC 10 Year Share Price

To better understand MFC's lackluster performance over the last ten years, a period where the share price has slumped over 50%, it is very important to understand MFC's history to explain what has led to such immense value destruction for shareholders.

MFC was listed on the 29th of March 2004. They did not do a vanilla equity issuance; rather, they issued income-participating (IPS) securities. So, when investors bought one IPS, they bought both one common share and a C$5.90 aggregate principal amount of 12.5% subordinated notes. Only in May of 2011 did MFC convert to the traditional common share structure from the original IPS structure.

MFC's historical strategy has been to use debt to fund acquisitions of both ASCs and SSHs. Everything was going relatively smoothly for the company until Q1 of 2019. This is where we start to see the first issues with their strategy.

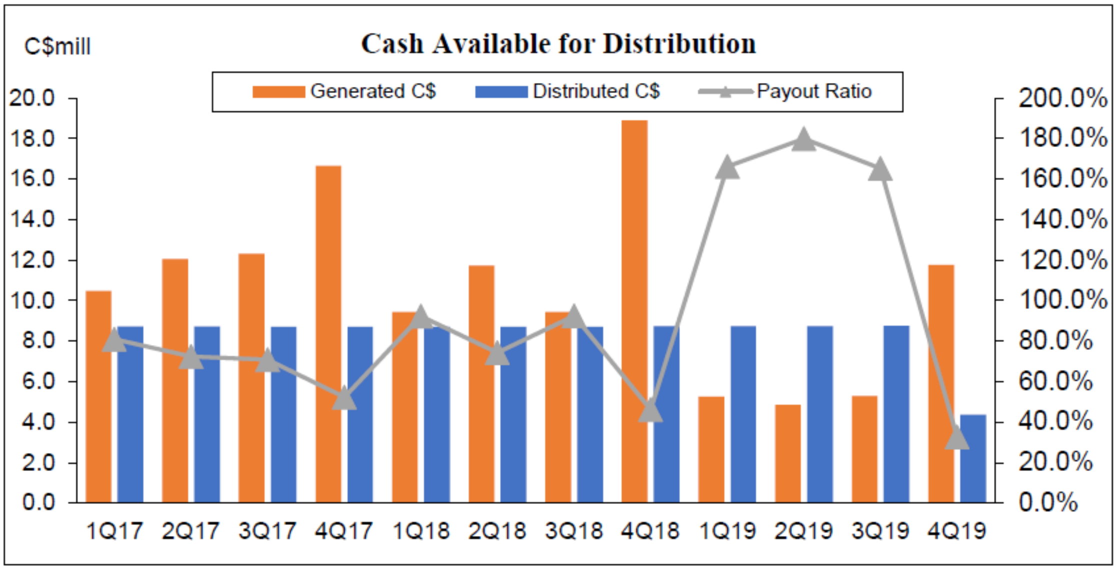

Figure 5: MFC CAFD 1Q2017 – 4Q2019 from 2020 MDA

Also, in regard to the graph above, which shows 'CAFD.' This is a non-GAAP/non-IFRS measure, and I explain this more in my section on covering MFC's financials.

In MFC's Q1 2019 call, management mentioned that income from operations was down 14.1mm from Q1 of 2018 to 10.2mm in Q1 of 2019. They associated the decrease with the lower EBITDA from a few facilities, but most notably from Unity Medical and Surgical Hospital (UMASH). They associated the lower EBITDA as being primarily a result of a payor mix with a higher proportion of governmental payors as well as an increased proportion of lower-acuity cases.

This also marked the first quarter, where MFC's cash available for distribution was less than the payout that they had made. This resulted in a payout ratio of 166.3% for 1Q2019 compared to 92.2% for 1Q2018. This can be seen in Figure 5. Management then went on to say that going back as far as 2013, the first quarter has typically been MFC's weakest quarter.

I also think it's worth highlighting some of the most poignant questions from the 1Q2019 Earnings Call that analysts asked, as it serves to provide a clearer picture of effectively what went wrong and how management was so blindsided by what was to come.

Question 1: Regarding UMASH, is there any demographic or any other sort of structural changes in UMASH's markets that might explain the increase we saw in the government pay on the quarter. Also leading on from that as you look at the payor mix that we saw in the quarter, is that indicative of what we may see in coming quarters?	**Answer 1:** We saw overall volume growth at Unity. The issue is that we had a lower acuity of those surgeries. And what we see from fourth quarter to first quarter, we generally have a higher commercial payor mix in the fourth quarter of the year so that we typically see more governmental payors in the first quarter as a result of those compressions.
Question 2: Did what we see in the quarter in terms of lower-acuity cases indicative of what we might see in additional quarters?	**Answer 2:** Well, we think it's more of an anomaly when we are talking about a higher case mix. Higher level of acute surgeries, those take a while to source, to preauthorize through insurance and so forth. So we think there has been no trend, no demographic change, nothing that would indicate that it would be a continuing issue.
Question 3: Just from everything you have been talking about, it sounds like there's really nothing to be read into the	**Answer 3:** I would think that's correct. There is nothing. We are not seeing anything in any of our markets that would

activities, the payor mix, the case volume, that would necessarily reflect any kind of changes through the rest of this year or into next year from normal patterns.	show a change to just kind of the normal progression. So I think, the first quarter we have a lot more Medicare patients than we do in the fourth quarter, and that trend every year in US health care continues to kind of keep going that way.
Question 4: Are there going to be any changes in the position of the dividend going forward?	**Answer 4:** We have no plans to change the dividend.

Between Q1 and Q2 of 2019, MFC's CFO changed from Tyler Murphy to David Watson, and MFC's poor performance continued into 2Q2019. The issues mentioned in the 1Q2019 call continued, and management had no reasonable answers other than that they were disappointed.

By 3Q2019, Management realized that the monthly dividend they had been paying out historically was no longer sustainable. So, in 3Q2019, it was announced that the dividend payment schedule had been changed from monthly to quarterly, at an annual rate of C$0.28 per share versus the prior annual rate of C$1.125 per share. Then CEO Robert Horrar said, "The challenges we have been facing this year at Unity Medical and Surgical Hospital, or UMASH, continued to affect our results in the third quarter. We are disappointed in the results over the past few quarters, resulting in a payout ratio of over 100%."

Additionally, MFC recorded a $22mm goodwill impairment charge related to the MFC Nueterra ASCs. The impairment charge was largely due to challenges at one of the larger ASCs in the group.

The monthly dividends were something that was core to MFC's shareholder base. Once the monthly dividend was gone, many retail dividend investors left, meaning MFC had no natural shareholder base.

In 2020, the COVID pandemic worsened MFC's financial situation, which led to MFC's share price hitting a low of C$2.86. In February 2020, it was announced that MFC had sold most of its interest in UMASH, and its ownership interest decreased from 87.6% to 31.7%. MFC received $1.1mm in cash consideration for its equity interests. Furthermore, UMASH's debt obligation to MFC was reduced by $3mm, with the remaining $20mm being structured on a five-year term. MFC also announced that they would sell the real estate assets underlying UMASH, consisting of land and buildings, for approximately $25mm.

What has changed?

Since the divestiture of UMASH, MFC has adopted a change in corporate strategy. This was announced in a press release shared on September 13th, 2022. They announced that they were in constructive discussions with Converium Capital, a company shareholder, and other shareholders to gather feedback on MFC's strategic direction.

As part of this change in corporate strategy, it was announced that the following would be done:

- MFC would suspend all acquisitions
- Divest all non-core assets
- Pursue overhead cost reductions
- Evaluate and implement strategies to return capital to its shareholders

As part of this change in strategy, MFC added Adina Storch and Yanick Blanchard as independent directors of the company, replacing Stephen Dineley and Lois Cormack, who resigned from the board. Alongside changes in the board, Jason Redman was appointed interim CEO and has since become the permanent CEO.

As was mentioned in the Business Overview section at the start of the report, MFC disposed of five of their ASCs throughout FY2023, which were all non-core assets.

MFC has also aggressively bought back its shares since September 2022. It did this via a modified Dutch auction for up to $34.5mm, which was announced alongside the change in corporate strategy.

QoQ Change in DSO						
	Q2 2022	Q3 2022	Q4 2022	Q1 2023	Q2 2023	Q3 2023
DSO	**30,196,779**	**29,554,010**	**29,366,985**	**25,702,096**	**25,345,146**	**25,066,567**
Nominal Change		(642,769)	(187,025)	(3,664,889)	(356,950)	(278,579)
%change YoY		*-2.13%*	*-0.63%*	*-12.48%*	*-1.39%*	*-1.10%*

Figure 6: MFC Common Shares Outstanding Table & YoY Change

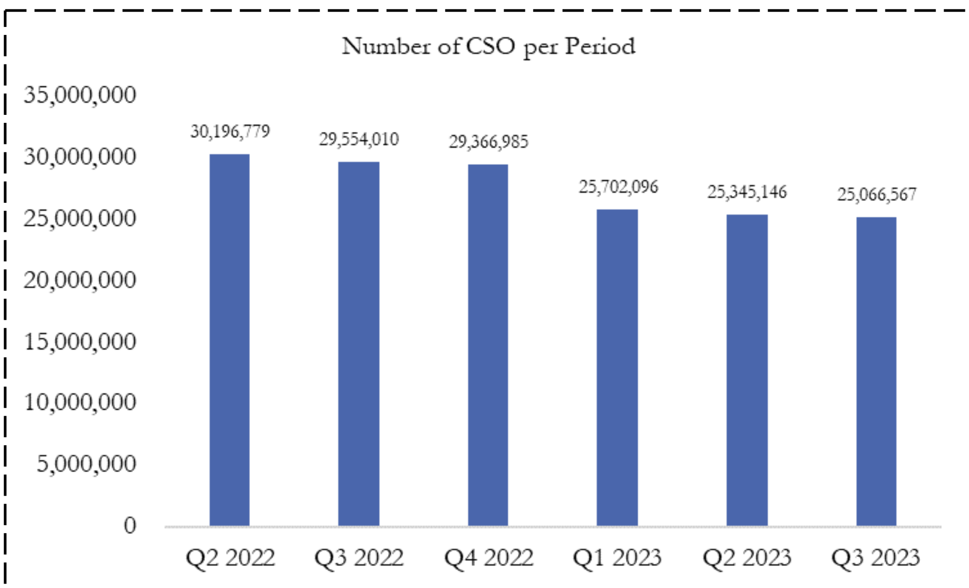

Figure 7: MFC Common Shares Outstanding Per Period

Since then, they have continued to buy back shares and pay off debt. During FY2023, $12mm of repayments were made against their corporate credit facility.

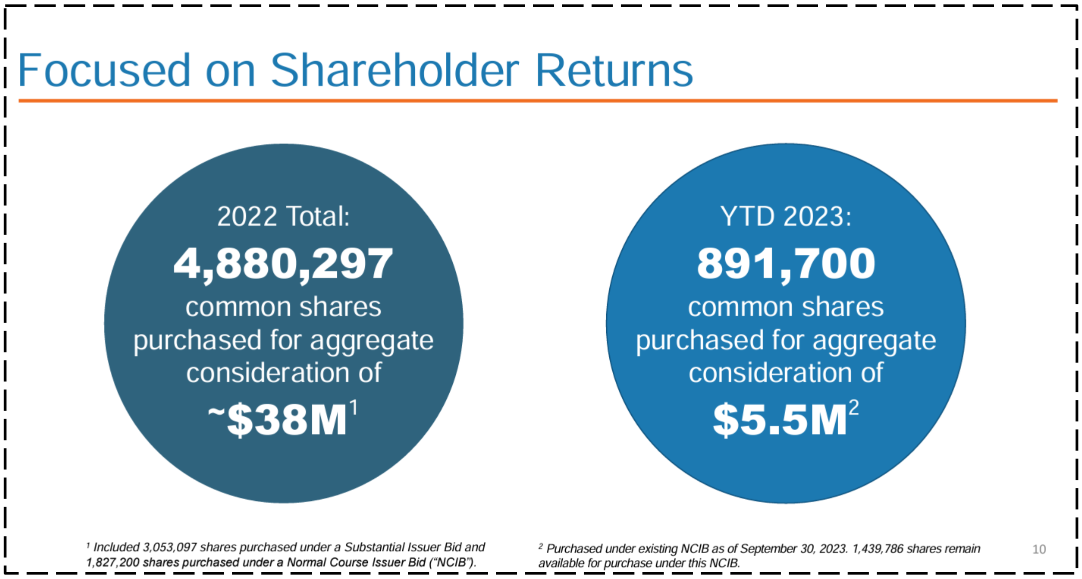

Figure 8: MFC Investor Relations Presentation from December 2023

It is also extremely important to focus on reducing corporate overheads at the MFC Canada level of the structure. Before Jason Redman's arrival, corporate costs had been on an upward trajectory for a couple of years, doubling from just under \$6mm to over \$12mm. In addition, prior management had granted themselves significant stock options.

\$12mm in corporate expenses is somewhat unacceptable, and it looks like management was trying to line their pockets instead of having the shareholder's best interest at heart. Since Jason has come in as the CEO, management has made multiple decisions to help reduce corporate overheads. For example, last year, they replaced KPMG with Grant Thornton as their auditor, which brought significant cost savings. Management has guided that their strategy of cutting overhead costs should increase the cashflows attributable to shareholders in the range of \$5mm.

Cash Available for Distribution (In thousands of U.S. dollars)	2022	2021
Cash available for distribution at Facility level	70,195	85,576
Non-controlling interest in cash available for distribution at Facility level	(33,110)	(40,489)
Corporation's share of cash available for distribution at Facility level	**37,085**	**45,087**
Corporate expenses	(12,054)	(12,021)
%of corporation's share of CAFH @ Facility level	*32.50%*	*26.66%*
Interest on corporate credit facility	(789)	(568)
Recovers of (provision for) current income taxes	(3,082)	(2,623)
Cash available for distribution	**21,160**	**29,875**

Figure 9: Cash Available for Distribution: Corporate Expenses

To further validate our thesis, we talked to Michael from Converium Capital. Michael confirmed that Converium, in September of 2022, had replaced four of six directors on the board. They also replaced the CEO and set out a strategy to a) cut down overhead costs, b) sell all the facilities, and c) use the proceeds as if it were going to be a piecemeal sale and buyback stock.

Valuation:

DCF Build

Operating Build	21A	22A	23E	24E	25E	26E	27E	28E
Facility Service Revenue	398,633.0	424,551.0	445,778.55	459,151.91	472,926.46	487,114.26	501,727.69	516,779.52
%growth YoY		*6.50%*	*5.00%*	*3.00%*	*3.00%*	*3.00%*	*3.00%*	*3.00%*
Government Stimulus Income	13,099.0	(10,162.0)	0	0	0	0	0	0
Total Revenue	**411,732.0**	**414,389.1**	**445,778.6**	**459,151.9**	**472,926.5**	**487,114.3**	**501,727.7**	**516,779.5**
EBIT	**77,358.0**	**34,939.0**	**66,866.8**	**75,760.1**	**78,032.9**	**80,373.9**	**82,785.1**	**85,268.6**
%operating margin	*19.41%*	*8.23%*	*15.00%*	*16.50%*	*16.50%*	*16.50%*	*16.50%*	*16.50%*

DCF	21A	22A	23E	24E	25E	26E	27E	28E
Period				1	2	3	4	5
EBIT	**77,358.0**	**34,939.0**	**66,866.8**	**77,047.3**	**80,707.0**	**84,540.6**	**88,556.3**	**92,762.7**
Tax Rate	20%	20%	20%	20%	20%	20%	20%	20%
EBIAT	**61,886.40**	**27,951.20**	**53,493.43**	**60,608.06**	**62,426.30**	**64,299.09**	**66,228.06**	**68,214.90**
D&A				9,500.00	9,500.00	9,500.00	9,500.00	9,500.00
Change in Net Working Capital				350.00	344.36	354.69	365.34	376.30
%of Sales				*2.50%*	*2.50%*	*2.50%*	*2.50%*	*2.50%*
CAPEX				8,500.00	8,500.00	8,500.00	8,500.00	8,500.00
Minority Interest Deduction				29,097.58	29,963.92	30,848.59	31,759.79	32,698.34
Unlevered Free Cash Flows				**32,160.48**	**33,118.01**	**34,095.81**	**35,102.93**	**36,140.27**
Discount Rate				9.50%	9.50%	9.50%	9.50%	9.50%
PV of FCF				29,370.30	27,620.79	25,969.20	24,416.70	22,957.30
PV of Stage 1	**130,334.28**							

EV to EQ Bridge	
Final-Year FCF	36,140.27
Exit Multiple	9x
Terminal Value	325,262.41
PV of TV	**206,615.68**
Enterprise Value	336,949.96
less Debt	52,603.00
plus Cash & Cash Equivalents	26,979.00
Equity Value	311,325.96
DSO	25,066,567
Equity Value per Share (USD)	12.42
Equity Value per Share (CAD)	**16.77**
Upside	**82.45%**

Assumptions for DCF	
Discount Rate	9.50%
Share Price	9.19
DSO	25,066,567

Multiples Valuation

Medical Facilities Corporation		Ending Period:
Multiples Valuation		**9/30/2023**
Hospital Asset, EBITDA		EBITDA Annualized
ASH		16,000,000
OSH		5,900,000
BHSH		18,500,000
SFSH		34,200,000
Hospital EBITDA, Total		74,600,000
Hospital EBITDA, DR's Share		39,180,602
EBITDA:FCF Conversion		52%
Corporate Expenses, Annualized		(8,700,000)
Net Debt Calculation		Amount
Cash & Equivalents		22,356,222
Debt, Current Portion		16,004,000
Debt, Non-Current Portion		36,515,000
Corporate Credit Facility		24,000,000
Lease Liabilities, Current Portion		10,127,000
Lease Liabilities, Non-Current Portion		40,625,000
Net Hospital Debt		52,519,000
Hospital Asset, Sale Multiples		EV/EBITDA Multiple
ASH		9.3x
OSH		9.3x
BHSH		11.0x
SFSH		10.5x
Hospital Asset, Sale Values		Sale EV
ASH		148,000,000
OSH		54,575,000
BHSH		203,500,000
SFSH		359,100,000
Sum		765,175,000
Valuation		
Enterprise Value		765,175,000
Less: Net Debt (Hospital Level)		(52,519,000)
Equity Value, USD, Total		712,656,000
Equity Value, USD, DR's Proportional Share		374,293,443
Less: DR Corporate Credit Facility		(24,000,000)
Years Until All Asset Sales Complete		2.00
Less: Capitalized Corporate Overhead Costs Until Wind-Down		(17,400,000)
Equity Value, USD, DR's Proportional Share		332,893,443
FX CAD/USD		1.32
Equity Value, CAD, DR's Proportional Share		439,419,345
Diluted Shares Outstanding		25,500,473
Intrinsic Value per Share	**CAD**	**17.23**
Current Price per Share	CAD	9.19
Upside		88%

Appendix:

Payor Mix

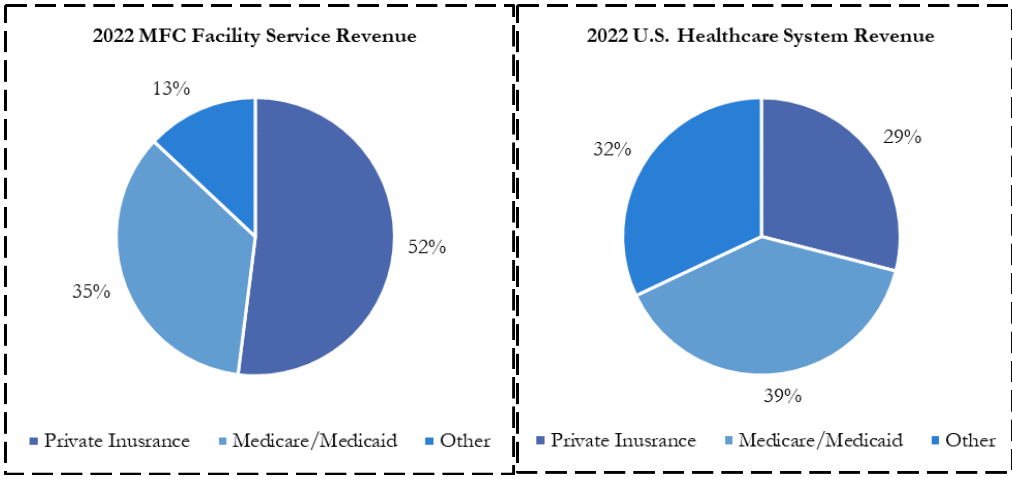

Exhibit 1: MFC vs. US Healthcare System Payor Mix

Operating Income

Operating Income								
Hospital Asset	2022, 4Q	2023, 1Q	2023, 2Q	2023, 3Q	TTM	MR TTM	DR % Own	TTM to DR
ASH	3,476,000	4,127,000	4,417,000	4,791,000	16,811,000	13,493,341	51%	8,573,610
OSH	2,143,000	1,408,000	957,000	36,000	4,544,000	5,222,452	64%	2,908,160
BHSH	4,983,000	2,955,000	4,940,000	2,701,000	15,579,000	16,177,043	54%	8,443,818
SFSH	12,756,000	7,583,000	7,417,000	6,928,000	34,684,000	29,028,330	51%	17,688,840
SCNC	(75,000)	310,000	378,000	59,000	672,000		51%	342,720
MFC Nuterra ASCs	320,000	11,000	10,000	202,000	543,000		50%	271,500
Total	**23,603,000**	**16,394,000**	**18,119,000**	**14,717,000**	**72,833,000**	**63,921,167**	52.5%	**38,228,648**

Exhibit 2: Operating Income

Equity Level Cashflows

Medical Facilities Equity Level	
Operating Income	38,228,648
Interest Expense	(3,943,540)
Tax Expense	(10,130,592)
Net Income	24,154,517
Depreciation & Amortization	5,700,206
Capital Expenditures	(9,616,579)
"Maintenance" Capital Expenditures	(5,252,091)
Free Cash Flow	20,238,144
"Steady State" Free Cash Flow	24,602,632
Share Price (CAD)	8.94
Market Capitalization (USD)	166,530,000
P / FCF	**8.2x**
P / Steady State FCF	6.8x
S/O	25,500,473

Exhibit 3: Equity Level Cashflows

Black Hills Surgical Hospital Quality

BLACK HILLS

SURGICAL HOSPITAL

Proudly owned by physicians

Year after year, BHSH has consistently ranked among the top 1% of hospitals in the nation for providing quality care and service out of nearly 5,000 hospitals.

Medical Excellence 2021-2022 (CareChex by Quantros)		
#1 in State	**#1 in Market**	**Top 100 in Nation**
Overall Hospital Care	Overall Hospital Care	Overall Hospital Care
Overall Surgical Care	Overall Surgical Care	Overall Surgical Care
Joint Replacement	General Surgery	Joint Replacement
Neurological Care	Joint Replacement	Major Orthopedic Surgery
Major Orthopedic Surgery	Neurological Care	Spinal Fusion
	Major Orthopedic Surgery	Spinal Surgery

Exhibit 4: CareChex Medical Excellence Ranking 2021-2022

Patient Safety 2021-2022 (CareChex by Quantros)		
#1 in State	**#1 in Market**	**Top 100 in Nation**
Overall Hospital Care	Overall Hospital Care	Overall Hospital Care
Overall Surgical Care	Overall Surgical Care	Overall Surgical Care
Joint Replacement	Joint Replacement	Joint Replacement
Major Orthopedic Surgery	Neurological Care	Major Orthopedic Surgery
	Major Orthopedic Surgery	

Exhibit 5: CareChex Patient Safety Ranking 2021-2022

BHSH also won the award from CareChex for the best hospital overall in South Dakota in 2022.

BHSH has received numerous awards from Healthgrades, another site that ranks hospitals. Their surveys found that 93% of patients would recommend BHSH, which is 23% higher than the national average. From 2017 through 2019, patients treated in hospitals receiving the America's 100 Best Hospitals for Joint Replacement Award have, an average, a 64.5 percent lower risk of experiencing a complication while in the hospital than if they were treated in hospitals that did not receive the award. Additionally, patients treated at hospitals that did not receive the award were 2.82 times more likely to experience a complication in the hospital than if they were treated at hospitals that received the award.

Exhibit 6: Healthgrades Awards for BHSH

BHSH was also ranked among the top 10 hospitals in the nation for orthopedic and spine care based on HCAHPS patient survey data. HCAHPS is the Hospital Consumer Assessment of Healthcare Providers and Systems. It is the first national, standardized, publicly reported survey of patients' perspectives of hospital care administered by the government. These results are available for patients to check at http://www.medicare.gov/care-compare and are frequently checked.

Exhibit 7: HCAHPS Survey Results for BHSH

I also think that Google Reviews are worth looking at, given that these would probably be some of the first things customers look at when considering a hospital.

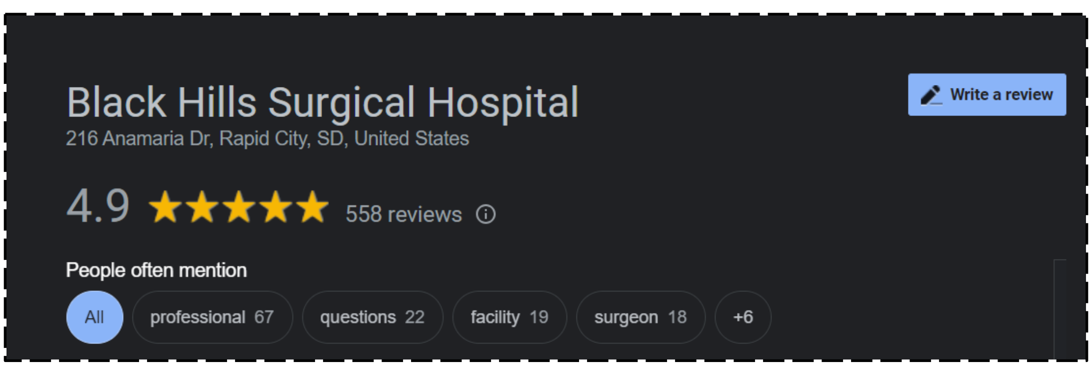

Exhibit 8: Google Reviews of BHSH

<u>Sioux Falls Specialty Hospital Quality</u>

Exhibit 9: Healthgrades Awards for SFSH

Exhibit 10: HCAHPS Survey Results for SFSH

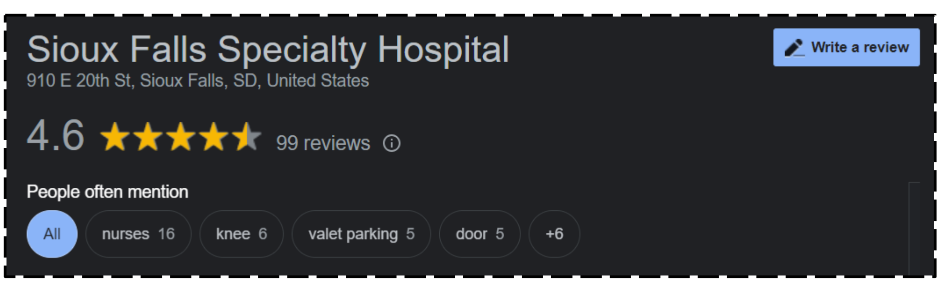

Exhibit 11: Google Reviews of SFSH

<u>Arkansas Surgical Hospital Quality</u>

ARKANSAS
SURGICAL HOSPITAL
PHYSICIAN OWNED

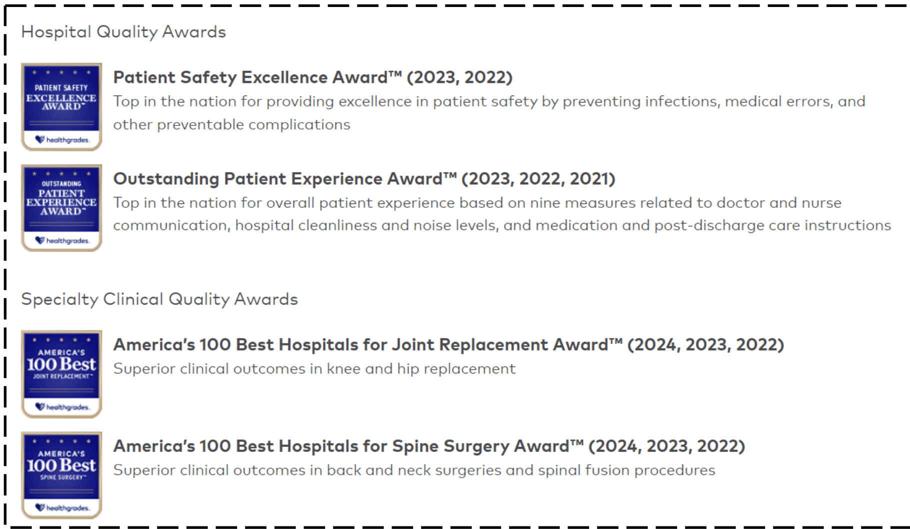

Exhibit 12: Healthgrades Awards for ASH

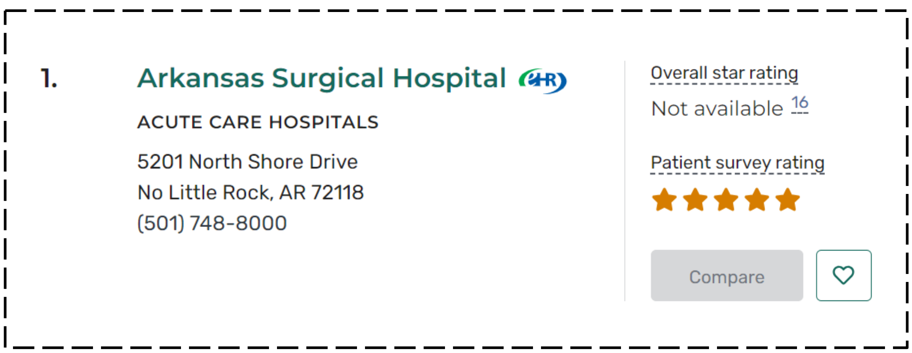

Exhibit 13: HCAHPS Survey Results for ASH

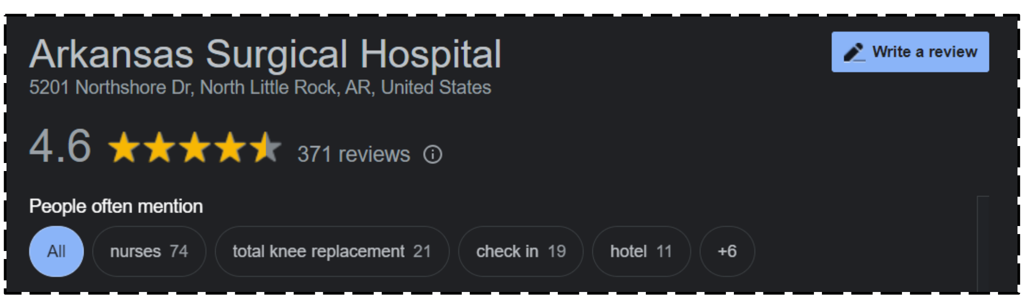

Exhibit 14: Google Reviews of ASH

<u>Oklahoma Spine Hospital Quality</u>

Of all the specialty surgical hospitals that MFC owns, Oklahoma Spine Hospital is of the lowest quality.

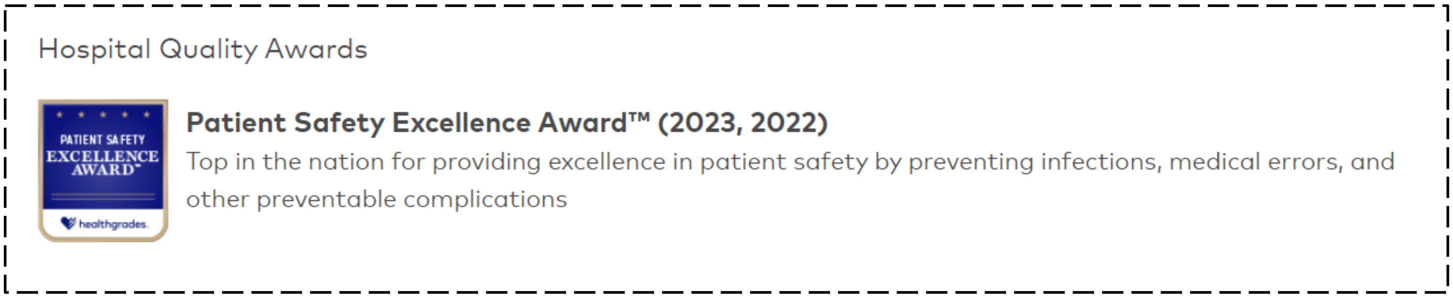

Exhibit 15: Healthgrades Awards for OSH

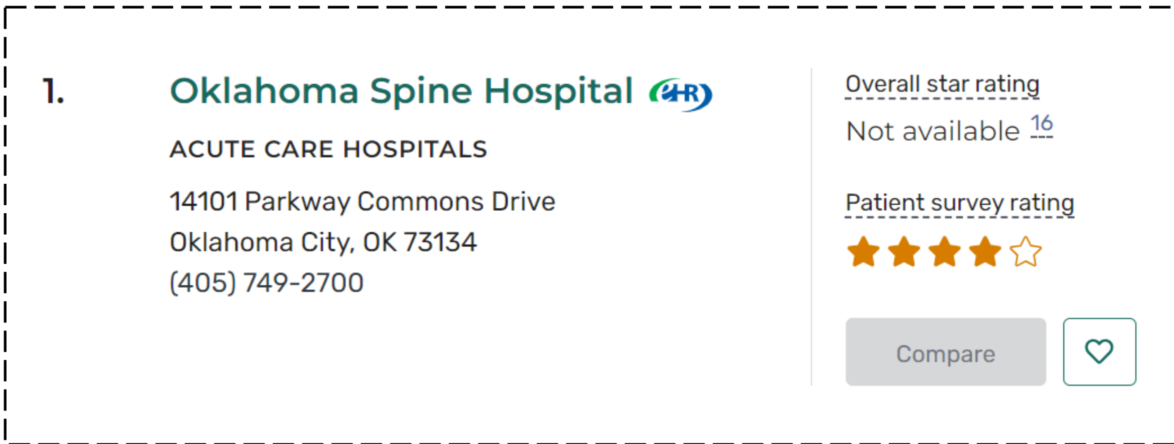

Exhibit 16: HCAHPS Survey Results for OSH

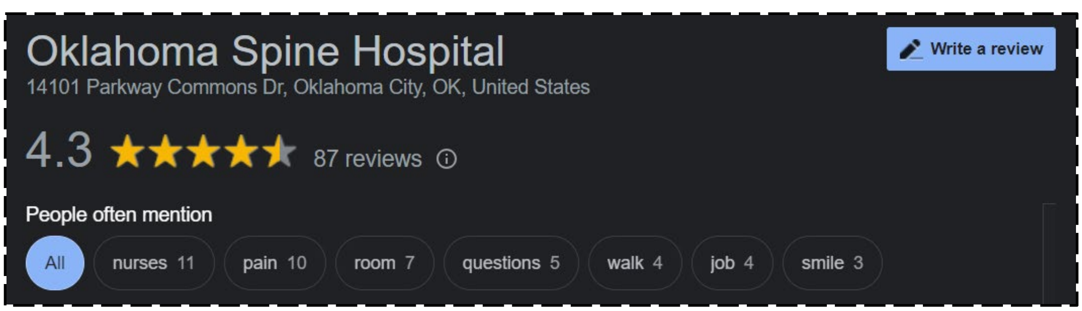

Exhibit 17: Google Reviews of OSH

<u>MFC Topline</u>

Understanding MFC's financials is somewhat complicated because there are so many NCIs in their operating assets. But to better understand why this opportunity exists, understanding the financials of MFC is essential. The first thing to note is that even though MFC is listed in Canada, all their earnings are reported in US Dollars. Therefore, any financials used throughout this report will be in US Dollars.

The third line item in Figure 12, 'Government Stimulus income (costs),' oscillates between positive in FY2020, then negative in FY2021, and completely disappears in FY2023. To clarify this, one must understand the litany of COVID-19 relief programs the government runs. The Coronavirus Aid, Relief and Economic Security (CARES) Act was signed into law on March 7th, 2020. The CARES Act included provisions for financial assistance to hospitals, surgery centers, and healthcare providers. These funds were made available via the Public Health and Social Services Emergency Fund (PHSSEF), the Paycheck Protection Program (PPP), and the Employee Retention Credit (ERC).

The PHSSEF was administered by the Department of Health and Human Services (HHS) to provide eligible healthcare providers with relief funds to cover non-reimbursable expenses, including lost revenue, attributable to COVID-19. Funds not utilized for eligible costs and not applied to lost revenues must be returned.

MFC recognized income for the loans received under the PPP during prior periods based on management's assumption that they had met the requirements for forgiveness. However, given the denial and additional review of certain loan forgiveness applications by the SBA in 2022, MFC management no longer had reasonable assurance of meeting the forgiveness requirements for loans of $12.34mm. This $12.34mm comprises all PPP loan balances for facilities whose forgiveness applications have been denied or are under review. Therefore, we see the reversal of $12.34mm from FY2022's revenue. Management is still trying to pursue loan forgiveness, and if this does occur in the future, income will be recognized. All these expenses and income are one-time effects due to COVID-19, and thus, as Christian from Trident Opportunities suggests, it makes more sense to deduct the positive stimulus income from 2021, and the negative income from 2022 should be added back on top of revenues. This effectively smoothens the revenue and somewhat adjusts for the impacts of COVID-19. Exhibit 18 below shows this.

(In thousands of U.S. dollars)	Year Ended December 31,		
	2022	2021	2020
HHS	1,434	9,724	11,514
PPP	(12,335)	1,479	12,226
ERC	608	192	-
FFCRA	-	52	1,288
Other	131	1,652	980
Government Stimulus Income (Costs)	**(10,162)**	**13,099**	**26,008**

Exhibit 18: Government Stimulus Income Impact on I/S for FY2021 - FY2022

Revenues Without Adjustment (In thousands of U.S. dollars)			
	9M 2023	2022	2021
Facility service revenue	323,317	424,551	398,633
Government stimulus income (costs)	-	(10,162)	13,099
Total Revenue	**323,317**	**414,389**	**411,732**
YoY Growth %		*0.65%*	
Revenues With Adjustment (In thousands of U.S. dollars)			
	9M 2023	2022	2021
Facility service revenue	323,317	424,551	398,633
Government stimulus income (costs)	-	10,162	(13,099)
Total Revenue	**323,317**	**434,713**	**385,534**
YoY Growth %		*12.76%*	

Exhibit 19: Revenue With & Without Adjustments for FY2021 – 9M2023

MFC EBIT

Perhaps somewhat more concerning is that even though we see adjusted revenue growth of 12.76% there is a 54.8% decline in EBIT. This is shown below in Figure 5. The important thing to note here is that there was a one-time noncash expense in the 'Impairment of goodwill, other intangibles and equipment' line item, which was a $16.55mm drag on EBIT. MFC recorded an impairment loss in the MFC Nueterra ASCs cash-generating unit (CGU). These were the ASCs that were divested of in FY2023. While I am always weary of adjusting as management and investors too often classify otherwise recurring expenditures as one-time expenditures, I think here it is fair to make this adjustment. Thus, we can see below in Exhibit 20 that once we make this adjustment, the actual decline in EBIT improves from 54.5% to only 4%. While a 4% decline in EBIT is not great, it is significantly better than a 54.8% decline. Furthermore, I think there is a strong case to be made that the decline in EBIT is due to transitory issues, which I do not believe will last.

EBIT	9M 2023	2022	2021
Facility service revenue	323,317	424,551	398,633
Government stimulus income (costs)	-	(10,162)	13,099
Total Revenue	**323,317**	**414,389**	**411,732**
EBIT	**41,599**	**34,939**	**77,358**
YoY Growth %		*-54.83%*	

Adjusted EBIT	9M 2023	2022	2021
Facility service revenue	323,317	424,551	398,633
Government stimulus income (costs)	-	10,162	(13,099)
Total Revenue	**323,317**	**434,713**	**385,534**
EBIT	**41,599**	**45,101**	**64,259**
+ Impairment of goodwill, other intangibles and equipment		16,549	
Adjusted EBIT	**41,599**	**61,650**	**64,259**
YoY Growth %		*-4.06%*	

Exhibit 20: Adjusted EBIT for FY2021 – 9M2023

Exchangeable Interest Liability:

On the income statement, we see that in the 'Finance costs' segment, there is this change in the value of exchangeable interest liability, which crops up somewhat randomly, either positively or negatively impacting MFC's bottom line. There is also the line item underneath, which is the interest expense on exchangeable interest liability. Both of these are shown in the exhibits below.

	9M 2023	2022	2021
Finance costs			
Change in value of exchangeable interest liability	4,010	(8,224)	11,539
Interest expense on exchangeable interest liability	5,226	7,362	8,707
Interest expense, net of interest income	4,651	5,731	6,064
Impairment loss on loan receivable	786	11,990	-
Loss on foreign currency	42	3	34
	14,715	**16,862**	**26,344**

Exhibit 21: Finance Costs on MFC Income Statement

As a result of MFC's acquisition of its interests in ASH, BHSH, SFSH, and OSH, MFC entered into exchange agreements with the owners, who initially retained a 49% non-controlling interest in these facilities. The terms that MFC agreed to allow the non-controlling interest holders in each facility the right to exchange a portion of their interest in their respective facilities for common shares of MFC. The outstanding exchangeable interest for each facility is detailed below.

Summary of Facility Information as of September 30, 2023	Arkansas Surgical Hospital (ASH)	Oklahoma Spine Hospital (OSH)	Black Hills Surgical Hospital (BHSH)	Sioux Falls Specialty Hospital (SFSH)	Surgery Center of Newport Coast (SCNC)
Exchangeable Interest	5.00%	1.00%	10.80%	14.00%	-

Exhibit 22: Exchangeable Interest by Facility

The exchangeable interests are subject to certain limitations, such as the exchange can only occur quarterly, and the NCIs are not allowed to exchange more than 3% per quarter. The exchangeable interest liability is carried at fair value. It is determined at each reporting date by multiplying the closing share price by the total number of common shares issuable under the exchangeable interest. Each facility's distributions in excess of what the company does not own but would own if the interest exchange was effective are recorded as interest expense. Each facility's distributions are treated as interest expenses but are non-cash expenses.

EIL Maths (In thousands of U.S. dollars)	September 30, 2023	June 30, 2023	Change
Shares to be issued for EIL	5,937,372	6,082,735	(145,363)
MFC's closing share price	CAD 9.46	CAD 8.29	CAD 1.17
Closing USD/CAD exchange rate	$1.3579	$1.3247	$0.0332
Exchangeable Interest Liability	**41,364**	**38,066**	**3,298**

Exhibit 23: Change in Value of EIL Exemplified

The figure above demonstrates the change in the value of the exchangeable interest liability. If MFC's share price increases in any given period, then the EIL on MFC's balance sheet increases, negatively impacting MFC's bottom line. However, since it is a non-cash expense, it is added to the cash-flow statement under finance income.