

QUALITY SYSTEMS INC. *Irvine, California*

Obama Stimulus Plan Encourages Paperless Health Care Records

BY MARILYN ALVA

INVESTOR'S BUSINESS DAILY

Government dollar signs for health care technology point straight ahead, though the road could stretch on for a while.

In his inaugural speech, President Obama pledged to harness technology to raise health care quality and lower its costs.

The \$819 billion stimulus package passed this week by the House includes \$20 billion for health care IT. Another \$1.5 billion is earmarked to modernize federal community health centers and Native-American health clinics.

The package, pending approval by the Senate, is seen as a stimulus for health care tech companies such as **Quality Systems**^{QSII}, which

sells software-based practice management and patient-records systems to doctor and dental practices.

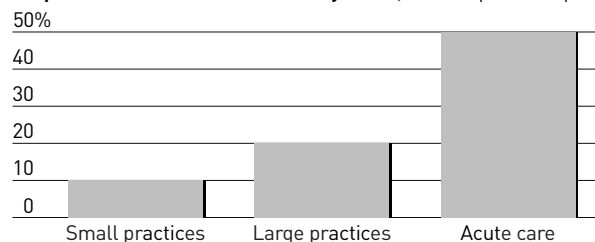
Irvine, Calif.-based Quality Systems also sells to federally sponsored health clinics and Indian health services.

"We think the best days are ahead, fueled by the Obama plan and by the continued promotion of electronic medical records and paperless health care," said Quality Systems' chief executive Steven Plochocki.

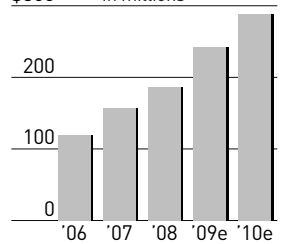
Healthy Pulse

Health care software vendor Quality Systems has been helping doctors modernize their practices. And there are still lots of doctors to convert.

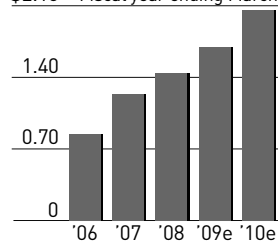
Adoption of electronic health care systems, includes partial adoption



Revenue, fiscal year ending March
\$300 In millions



Earnings per share
\$2.10 Fiscal year ending March



Sources: Company reports, BB&T Capital Markets, Thomson Reuters

But he and others don't expect the stimulus package to have an impact on health care vendors until 2010 at the earliest, and how it will actually trickle down to vendors is still unclear.

"What we do know is that doctors are continuing to look at these systems and are interested in buying them," said K. Newton Juhng, analyst with BB&T Capital Markets. "In some cases they will not be willing to wait that long. This stimulus package is really

gravy, the extra on top of the base."

Even without the extra push, Quality Systems' annual revenue has been growing about 26% on average the last couple of years.

On Thursday after the market close, the firm said third-fiscal-quarter sales ending Dec. 30 jumped 36% from the earlier year to \$65.5 million. Some of the growth came from two recent acquisitions.

Per-share earnings rose 15% to 46 cents a share, one

Quality Systems

qsii.com

Ticker	QSII
Share price	Near 37
12-month sales	\$231 mil
5-year profit growth rate	36%

IBD SmartSelect Corporate Ratings

Composite Rating	99
Earnings Per Share	90
Relative Price Strength	96
Industry Group Rank	3
Sales+Profit Margins+ROE	A
Accumulation/Distribution	C+

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cent above views. That was more than double the year-to-year growth rate in the second quarter, when execs noted expenses tied to a proxy fight with dissident shareholder Ahmed Hussein, which it won, reduced profit by 3 cents a share.

Plochocki says stimulus spending would likely trickle down to health-care tech vendors as a result of performance metrics doctors will be required to show.

Quality Systems is one of the top health care software vendors in the U.S., though with annual revenue at around \$200 million it's one of the smaller in the pack. The largest is **Allscripts-Misys Healthcare**^{MDRX}. Allscripts and Misys' recent merger has analysts calling it the giant in the space.

"Quality Systems should be able to hold its own and capture its share of new opportunities," said analyst Leo Carpio of Caris & Co.

(Continued)

Quality Systems has been on its own buying spree. Since May, it bought two companies — Healthcare Strategic Initiatives and Practice Management Partners.

The acquisitions added \$34 million in annualized revenue and new products in revenue cycle management. The figure is expected to rise as it sells new products to existing customers.

Quality Systems' chief rival in that field is **Athenahealth^{ATHN}**. Both now compete to sell doctors a new generation of revenue-management software and services.

"It's a big investment, but customers get it back quickly," Juhng said.

Quality Systems' executives have been gushing over the new systems, which can help doctors cut down on collection costs.

That's especially helpful in a recession and when unemployment rolls rise. The number of unpaid

patient bills typically goes up then. And it becomes tougher to collect.

"This has become more of a top-of-mind concern for doctors," Juhng said.

Meanwhile, some see plenty of room to grow the electronic medical records business, which would likely be the biggest beneficiary of the federal spending package. Only a small portion of doctors have switched from file folders to electronic patient records.

Quality Systems' electronic health records business is one of its main growth engines.

Systems are often sold along with its bread-and-butter practice-management software, which handles mundane tasks such as scheduling and billing.

About 75% of Quality Systems' new customers purchase practice management software in combination with electronic medical records systems,

which have higher margins.

"They tend to sell at a premium price," said Carpio, referring to electronic medical records products. One reason is that Quality Systems can customize products with templates for various types of practices, such as orthopedics and cardiology.

But the timid economy could make customers hold off on new purchases or pressure vendors for further discounts. And some observers worry that doctors will put off making new-tech buys in advance of incentives from the federal government.

"That's the risk," Carpio said. "There could be a short-term pause in sales. But at the end of the day, I think pressures for doctors to modernize are too great to wait."

Quality Systems' management said during a Friday conference call that some customers

have held off purchases due to confusion over the way the government would disburse funds.

Carpio says large-group practices with deep pockets would probably be more willing to buy sooner than single or small-group practices.

Quality Systems' customers are mostly mid- and large-sized group practices. Some budget-strapped hospitals that help affiliated physicians upgrade technology might hold off aid, observers say. Dental practices make up 10% of sales.

Management says customer financing hasn't been a problem. The firm's backlog stands at a record \$86 million. That's up just \$1 million from the previous quarter but \$10 million from the earlier year.

Analysts estimate Quality Systems' profit this fiscal year ending in March will grow 18% over the prior year to \$1.70 a share. They expect profit the next year to jump 21%.