

Company Name : Pharmaniaga Berhad  
Date : 17 April 2017  
Source : The Star

## CIMB Research Upgrades Pharmaniaga To Hold



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KUALA LUMPUR: CIMB Equities Research has upgraded Pharmaniaga from Reduce to Hold with a target price of RM4.90 as the recent underperformance of share price have more than reflected the weak earnings in 2016.

It said on Monday it reduced the target price from RM5 to RM4.90 based on 18.7 times CY18 price-to-earnings, which is in line with its five-year average.

“We have also cut our FY17-19F EPS by 19.3-30.3% to account for weaker Ministry of Health (MOH) orders and higher operating costs. We would turn positive on the stock in the event of a significant increase in the MOH’s budget for drug purchases,” it said.

CIMB Research said Pharmaniaga's net profit dropped 45.7% on-year to RM45.6mil in FY16, despite flattish revenue.

The company's logistics & distribution (L&D) segment incurred pretax loss of RM14.8mil in FY16 (vs. pretax profit of RM12.3m in FY15) mainly due to cutbacks of government orders and sharp increase in finance cost to RM33.7mil (122.5% on-year).

Furthermore, the group's manufacturing EBIT contracted to 23.2% in FY16 (-5.9 percentage points on-year) on the back of lower offtake of in-house products from the government.

"Although government orders are likely to be weak in 2017F, we expect an improvement in the L&D division through better inventory management.

"Management began reducing orders placed with suppliers since early part of 2H16 which should translate to lower borrowings needed to fund the required working capital. Orders are placed six months in advance and the improvement will only be reflected in 1Q17. Management aims to reduce total borrowings by RM100mil to RM120mil in FY17F, which would lower finance costs," it said.

CIMB Research also noted that Pharmaniaga's management stated that it is in the process of finalising the extension of its concession agreement with the MOH, which is due to expire by 2019.

"The group is confident of obtaining a 10-year extension, given its proven track record and extensive L&D network. The extension would be positive for earnings as it would lengthen the amortisation period for the Pharmacy Information System (PhIS) from four years to 14 years, which would lead to lower annual amortisation costs.

Pharmaniaga is looking to expand its product portfolio by introducing 250 new products over the next 10 years. Although the research house believes that it is unlikely to reach this target in the slated time frame, it concurs that product launches are essential to support earnings growth for the manufacturing segment.

“The group’s manufacturing arm is also set to benefit from more product tender wins and higher selling prices from the Approved Product Purchase List (APPL for 2017-2019F) e-tender exercise in January 2017,” said the research house.