

Pharmaniaga

Recommendation: **HOLD**

Stock Code: 7081

Bloomberg: PHRM MK

Price: MYR5.44

12-Month Target Price: MYR5.50

Date: August 12, 2010

Board: Main

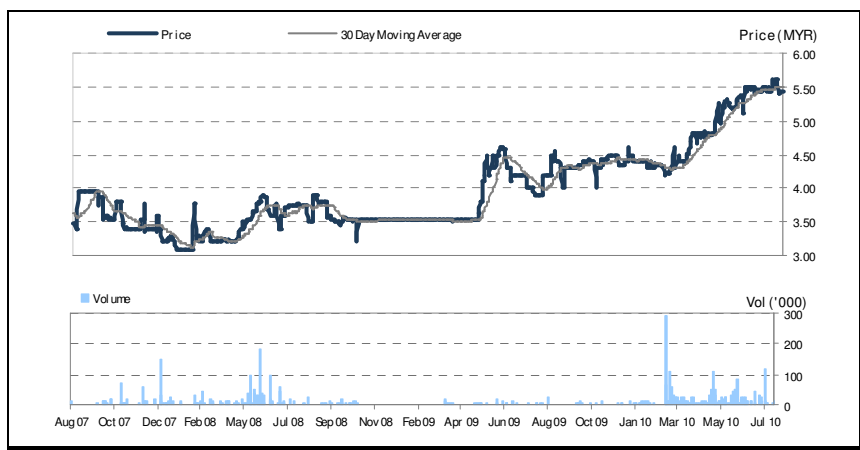
Sector: Trading/Services

GICS: Health Care/Pharmaceuticals

Market Value - Total: MYR582.0 mln

Summary: Pharmaniaga holds the sole concession for the supply of pharmaceuticals to government hospitals. The group also manufactures generic pharmaceuticals and supplies medical products and equipment in Malaysia and Indonesia.

Analyst: Siti Rudziah Salikin



Results Review & Earnings Outlook

- Pharmaniaga's 2Q10 net profit grew 58.5% QoQ to MYR14.7 mln. The results were behind our expectations because of weaker-than-expected contribution from the trading and distribution division. YTD net profit was MYR24.1 mln and accounted for 28.5% of our original full-year forecast.
- The manufacturing segment, which incurred a loss in 1Q partly because of the plant closure in March, turned around with an operating profit of MYR8.7 mln. The trading and distribution division revenue was boosted by higher sales to the government and the growing demand for generic drugs. Operating profit, however, fell 33% QoQ as margin dropped to 2.7% (1Q: 4.8%) due to sales of lower margin products and the competitive environment in the generic market. Higher selling expenses and personnel costs also contributed to the weaker-than-expected results.
- We reduce our projected net profit for 2010 by 7.7% after lowering margins for the trading and distribution division. We maintain our 2011 forecast. The growth prospect remains positive, in our opinion, driven by: (i) rising healthcare spending, (ii) the increasing demand for generics and impending expiry of patented drugs globally, and (iii) the growth in medical tourism in Malaysia. Margins, however, could continue to be pressured by competition from cheaper imports. We expect meaningful contributions from higher-margin small volume injectables to start flowing in 2011 and help to improve margins.

Recommendation & Investment Risks

- We maintain our Hold recommendation with an unchanged 12-month target price of MYR5.50.
- We continue to view Pharmaniaga as a defensive stock with decent prospects and respectable dividend yields. The emergence of Boustead Holdings (BOUS MK, MYR4.25, Buy) as a new controlling shareholder would be good for Pharmaniaga, as we expect Boustead to turn more aggressive in its effort to expand its pharmaceutical businesses into the Asean region in a big way. Boustead is acquiring UEM Group's entire 86.8% stake in Pharmaniaga for MYR5.75 per share. Boustead will make an MGO for the remaining shares but intends to maintain Pharmaniaga's listing status.
- The target price is based on PER of 8x and includes our projected dividend. The assigned valuation is at a premium to the stock's two-year average forward PER of 6.5x, given greater certainty following the renewal of the group's concession (for another 10 years).
- Risks to our recommendation and target price include: (i) slower-than-expected economic growth, which could cause the government to reduce healthcare spending and request for lower product pricing; and (ii) an adverse outcome from negotiations of the new terms of the concessions with the MOH.

Key Stock Statistics

FY Dec.	2009	2010E
Reported EPS (sen)	56.3	53.9
PER (x)	9.7	10.1
Dividend/Share (sen)	37.0	30.0
NTA/Share (MYR)	3.72	4.04
Book Value/Share (MYR)	4.03	4.34
No. of Outstanding Shares (mln)	107.0	
52-week Share Price Range (MYR)	4.00 - 5.61	
Major Shareholders:	%	
UEM Group Berhad	86.8	

* Stock deemed Shariah compliant by the Securities Commission.

Per Share Data

FY Dec.	2007	2008	2009	2010E
Book Value (MYR)	3.27	3.63	4.03	4.34
Cash Flow (sen)	62.6	69.9	69.2	67.4
Reported Earnings (sen)	46.8	56.1	56.3	53.9
Dividend (sen)	18.0	27.0	37.0	30.0
Payout Ratio (%)	38.4	36.1	58.6	41.8
PER (x)	11.6	9.7	9.7	10.1
P/Cash Flow (x)	8.7	7.8	7.9	8.1
P/Book Value (x)	1.7	1.5	1.4	1.3
Dividend Yield (%)	3.3	5.0	6.8	5.5
ROE (%)	15.0	16.3	12.4	12.9
Net Gearing (%)	49.2	8.7	0.0	13.9

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Pharmaniaga

Recommendation: **HOLD**Stock Code: **7081**Bloomberg: **PHRM MK**Price: **MYR5.44**12-Month Target Price: **MYR5.50**Date: **August 12, 2010****Quarterly Performance**

FY Dec. / MYR mln	2Q10	2Q09	% Change
Reported Revenue	350.3	333.2	5.1
Reported Operating Profit	20.8	25.5	-18.7
Depreciation & Amortization	NA	NA	NA
Net Interest Income / (Expense)	-0.3	-0.9	-66.4
Reported Pre-tax Profit	20.3	24.3	-16.5
Reported Net Profit	14.7	17.7	-16.7
Reported Operating Margin (%)	5.9	7.7	-
Reported Pre-tax Margin (%)	5.8	7.3	-
Reported Net Margin (%)	4.2	5.3	-

Source: Company data

Profit & Loss

FY Dec. / MYR mln	2008	2009	2010E	2011E
Reported Revenue	1,305.6	1,300.8	1,355.9	1,491.2
Reported Operating Profit	95.1	85.9	80.6	95.6
Depreciation & Amortization	-15.5	-14.7	-15.3	-16.7
Net Interest Income / (Expense)	-5.5	-3.6	-1.8	-1.4
Reported Pre-tax Profit	90.6	81.4	79.3	94.7
Effective Tax Rate (%)	32.2	24.2	26.0	25.0
Reported Net Profit	60.0	60.2	57.7	69.5
Reported Operating Margin (%)	7.3	6.6	5.9	6.4
Reported Pre-tax Margin (%)	6.9	6.3	5.8	6.3
Reported Net Margin (%)	4.6	4.6	4.3	4.7

Source: Company data, S&P Equity Research

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Strong Buy: Total return is expected to outperform the total return of the KLCI or KL Emas Index respectively, by a wide margin over the coming 12 months, with shares rising in price on an absolute basis.

Buy: Total return is expected to outperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months, with shares rising in price on an absolute basis.

Hold: Total return is expected to closely approximate the total return of the KLCI or KL Emas Index respectively, over the coming 12 months with shares generally rising in price on an absolute basis.

Sell: Total return is expected to underperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months and share price is not anticipated to show a gain.

Strong Sell: Total return is expected to underperform the total return of the KLCI or KL Emas Index respectively, over the coming 12 months by a wide margin, with shares falling in price on an absolute basis.

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Recommendation and Target Price History

Date	Recommendation	Target Price
27-May-10	Hold	5.50
25-Aug-09	Hold	4.60
11-May-09	Hold	4.20
25-Nov-08	Hold	3.70
26-Jun-08	Hold	4.05

