

## Pharmaniaga

Recommendation: **HOLD**

Stock Code: 7081

Bloomberg: PHRM MK

Price: MYR4.42

12-Month Target Price: MYR4.60

Date: November 16, 2009

Board: Main

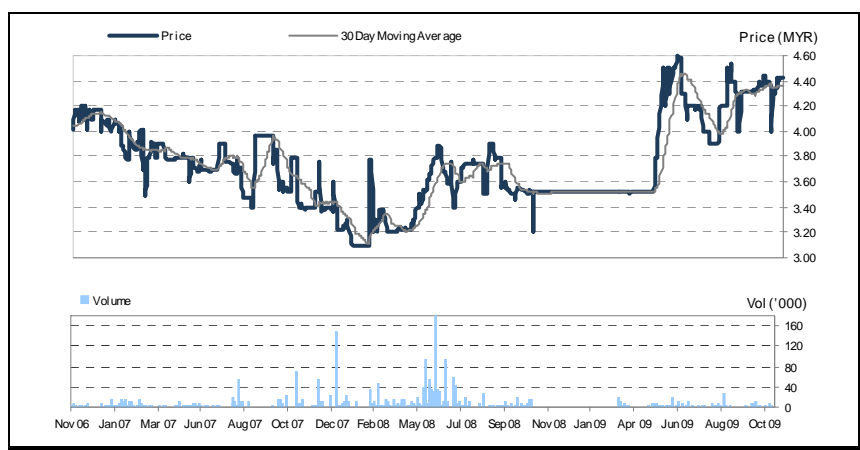
Sector: Trading/Services

GICS: Health Care/Pharmaceuticals

Market Value - Total: MYR472.8 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 &amp; Earnings Outlook

- Pharmaniaga's 3Q09 results were surprisingly weak, with a larger-than-expected 65.8% QoQ decline in net profit to MYR6.1mln. 9M net profit was MYR38.3 mln, down 9.4% YoY and accounted for 58.4% of our original full-year forecast.
- The manufacturing division posted a pre-tax loss of MYR1.2 mln in 3Q vs a profit of MYR9.7 mln in 2Q. The loss was not expected and was partly due to higher-than-projected start-up expenses for the new manufacturing plant in Puchong. A slowdown in concession sales, expiry of some tender sales, and higher sales volume of lower-margin products contributed to a 26.1% QoQ drop in pre-tax profit for the trading and distribution division. Effective tax rate for 3Q was also higher at 32.2% vs our estimate of 25%.
- We cut our 2009 net profit forecast by 20% to MYR52.4 mln but maintain a 2010 net profit estimate of MYR66.0 mln. Going forward, we still expect government orders to pick up. Margins could fluctuate depending on the types of medicine but given the more positive economic environment, we expect the demand for higher-priced products to increase, supporting an improvement in margins. The soon-to-commence Puchong plant, which focuses on higher-margin small volume injectable products, will be another growth driver for 2010.

## Recommendation &amp; Investment Risks

- Despite the 3Q earnings setback, we maintain our Hold recommendation and 12-month target price of MYR4.60 for Pharmaniaga.
- Government spending on pharmaceuticals will continue to grow given, among others, the rising prevalence of chronic diseases (as a consequence of rising affluence and unhealthy living habits) and emergence of new epidemic diseases (such as H1N1). Pharmaniaga will be one of the main beneficiaries to the increased spending, in our opinion. A bigger catalyst for the stock would be a confirmation of a renewal of the pharmaceutical supply contract. We believe chances of the contract being re-awarded to Pharmaniaga are high given its established network and long relationship with the Government. In the meantime, the share price should be supported by its attractive dividend yield.
- The target price is based on a PER of 7x, which is the average one-year forward multiple for the stock, on projected earnings for 2010 and includes our projected dividend of 27 sen.
- Risks to our recommendation and target price include Pharmaniaga not successfully renewing its concession or renewing it on less favorable terms. Slower-than-expected economic recovery could cause the government to reduce healthcare spending and request for lower product pricing.

## Key Stock Statistics

FY Dec.	2008	2009E
Reported EPS (sen)	56.1	49.0
PER (x)	7.9	9.0
Dividend/Share (sen)	27.0	27.0
NTA/Share (MYR)	3.30	3.60
Book Value/Share (MYR)	3.63	3.91
No. of Outstanding Shares (mln)	107.0	
52-week Share Price Range (MYR)	3.50 - 4.60	
Major Shareholders:	%	
UEM Group Berhad	86.8	

\* Stock deemed Shariah compliant by the Securities Commission.

## Per Share Data

FY Dec.	2006	2007	2008	2009E
Book Value (MYR)	2.96	3.27	3.63	3.91
Cash Flow (sen)	32.5	62.6	69.9	63.5
Reported Earnings (sen)	11.7	46.8	56.1	49.0
Dividend (sen)	15.0	18.0	27.0	27.0
Payout Ratio (%)	60.1	38.4	36.1	43.2
PER (x)	37.9	9.4	7.9	9.0
P/Cash Flow (x)	13.6	7.1	6.3	7.0
P/Book Value (x)	1.5	1.4	1.2	1.1
Dividend Yield (%)	3.4	4.1	6.1	6.1
ROE (%)	8.5	15.0	16.3	12.4
Net Gearing (%)	60.4	49.2	8.3	11.1

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**Quarterly Performance**

FY Dec. / MYR mln	3Q09	3Q08	% Change
Reported Revenue	330.0	314.3	5.0
Reported Operating Profit	10.6	20.0	-46.7
Depreciation & Amortization	NA	NA	NA
Net Interest Income / (Expense)	-0.9	-1.6	-41.6
Reported Pre-tax Profit	9.4	17.6	-46.6
Reported Net Profit	6.1	10.6	-42.8
Reported Operating Margin (%)	3.2	6.4	-
Reported Pre-tax Margin (%)	2.9	5.6	-
Reported Net Margin (%)	1.8	3.4	-

Source: Company data

**Profit & Loss**

FY Dec. / MYR mln	2007	2008	2009E	2010E
Reported Revenue	1,184.0	1,305.6	1,365.8	1,454.8
Reported Operating Profit	86.7	95.1	78.0	93.6
Depreciation & Amortization	-17.6	-15.5	-16.2	-17.2
Net Interest Income / (Expense)	-9.0	-5.5	-3.1	-2.5
Reported Pre-tax Profit	77.9	90.6	74.4	91.5
Effective Tax Rate (%)	33.6	32.2	26.2	25.0
Reported Net Profit	50.1	60.0	52.4	66.0
Reported Operating Margin (%)	7.3	7.3	5.7	6.4
Reported Pre-tax Margin (%)	6.6	6.9	5.4	6.3
Reported Net Margin (%)	4.2	4.6	3.8	4.5

Source: Company data, S&amp;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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**Shariah-compliant stock** - As defined by the Shariah Advisory Council of Malaysia's Securities Commission

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Recommendation and Target Price History

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

