

19 May 2015

Pharmaniaga

1Q15 Inline but Rich Valuations

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Period	1Q15
Actual vs. Expectations	<ul style="list-style-type: none"> 1Q15 PATAMI of RM31.8m (+21% YoY) came in at 32% and 31% of our and market consensus full-year forecast, respectively. We consider the results to be within expectations because subsequent quarters earnings growth rates are expected to taper off as the recognition of deferred tax assets for some of the subsidiaries are expected to be fully utilised. We estimate the sustainable effective tax rate to be between 28% and 33%.
Dividends	<ul style="list-style-type: none"> A first interim single tier DPS of 7.0 sen was declared, which came in within our expectation.
Key Result Highlights	<ul style="list-style-type: none"> QoQ, 1Q15 revenue fell 24% due to lower off-take from government hospitals. However, PBT rose slightly mainly due to improved manufacturing margin contributions that offset the lower revenue. Manufacturing PBT margin interestingly rose to 33% in 1Q15 compared to 17% in 4Q14 as a result of efficiency improvement. 1Q15 PATAMI fell 13% to RM31.8m due to lower effective tax rate of 17% compared to 3% in 4Q14. Note that the lower effective tax rate was due to recognition of deferred tax assets for some of the subsidiaries but it was expected to be fully utilised. Hence, we expect the effective tax rate to elevate back to between 28% and 33%. YoY, 1Q15 net profit rose 21% to RM31.8m due largely to lower effective tax rate of 17% compared to 30% in 1Q14. PBT rose slightly by 1.3% due to margin improvement in the manufacturing division. PBT margin rose to 33% in 1Q15 from 26% in 1Q14. This was primarily attributable to the higher profit margin from manufacturing division as a result of improved operational efficiencies, which directly reduced its manufacturing costs. Some of the efficiency improvement initiatives were manufacturing batch consolidation and enhanced procurement exercise.
Outlook	<ul style="list-style-type: none"> Pharmaniaga is a prime beneficiary of being the sole concession holder to purchase, store, supply and distribute approved drugs and medical products to 148 government hospitals and 1,400 clinics and district offices nationwide. The concession agreement ends in 2019 and allows for upwards revision in prices every three years. Note that Pharmaniaga Logistics had on 16 Mar 2012 entered into a 10-year concession agreement with the Malaysian government to purchase, store, supply, and distribute drugs and medical products.
Change to Forecasts	<ul style="list-style-type: none"> No changes to our earnings forecasts.
Rating & Valuation	<ul style="list-style-type: none"> Downgrade to MARKET PERFORM from OUTPERFORM. The stock has risen by >50% since our initiating coverage report back in Nov 2014. Due to the strong share price performance and rich FY15 and FY16 PER valuations of 17.9x compared to an average net profit growth of 7.9%, coupled with lack near-term catalyst, we downgrade the stock from Outperform to Market Perform. The saving grace is a decent dividend yield of 4.3%. Our RM6.95 target price is based on unchanged 16.5x FY16 EPS.
Risks to Our Call	<ul style="list-style-type: none"> Better-than-expected volume sales.

MARKET PERFORM

Price: **RM6.91**
Target Price: **RM6.95**

Share Price Performance



KLCI	1,823.50
YTD KLCI chg	3.5%
YTD stock price chg	50.9%

Stock Information

Bloomberg Ticker	PHRM MK Equity
Market Cap (RM m)	1,788.9
Issued shares	258.9
52-week range (H)	7.53
52-week range (L)	4.10
3-mth avg daily vol:	295,430
Free Float	28%
Beta	0.8

Major Shareholders

BOUSTEAD HOLDINGS BH	56.4%
LEMBAGA TABUNG ANGKA	10.1%
VALUECAP SDN BHD	5.4%

Summary Earnings Table

FYE Dec (RM m)	2014A	2015E	2016E
Turnover	2122.9	2324.6	2545.4
EBIT	140.2	155.2	176.2
PBT	125.5	145.6	163.4
Net Profit (NP)	93.8	100.0	109.0
Core NP	93.8	100.0	109.0
Consensus (NP)	-	102.1	107.0
Earnings Revision	-	-	-
Core EPS (sen)	36.2	38.6	42.1
Core EPS growth (%)	69.9	6.7	9.0
NDPS (sen)	28.0	29.9	29.5
BVPS (RM)	2.03	2.12	2.25
PER (x)	19.1	17.9	16.4
Price/Book (x)	3.4	3.3	3.1
Net Gearing (%)	32.1	39.9	41.6
Net Div Yield (%)	4.1	4.3	4.3

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Result Highlight

	1Q	4Q	1Q	Q-o-Q	Y-o-Y
FY Dec (RM'm)	FY14	FY14	FY15	Chg (%)	Chg (%)
Turnover	468.7	627.1	471.9	(24.7)	0.7
EBITDA	53.5	57.7	54.5	(5.6)	1.8
PBT	38.1	37.9	38.6	2.0	1.3
PATAMI (NP)	26.2	36.7	31.8	(13.4)	21.3
EPS (sen)	10.13	14.2	12.3	(13.4)	21.2
EBITDA margin	11%	9%	12%		
PBT margin	8%	6%	8%		
Effective tax rate	30%	3%	17%		

Source: Bursa Malaysia, Kenanga Research

Quarterly segmental breakdown

	3Q13	4Q13	1Q14	2Q14	3Q14	4Q14	1Q15	QoQ chg %	YoY chg %
Revenue									
Logistics and Distribution	440.9	568.2	468.9	521.4	496.4	622.3	470.0	(24.5)	0.2
Manufacturing	75.2	95.2	90.8	95.6	90.0	93.7	97.5	4.1	7.3
Eliminations	(75.3)	(95.5)	(91.1)	(92.0)	(84.3)	(88.9)	(95.5)	7.5	4.9
TOTAL	440.8	567.9	468.7	525.1	502.1	627.1	471.9	(24.7)	0.7
PBT									
Logistics and Distribution	(3.4)	10.7	14.8	1.5	4.9	18.9	10.8	(42.8)	(27.0)
Manufacturing	15.0	24.7	25.4	28.6	22.7	17.0	32.2	89.8	26.5
Eliminations	1.9 S	(2.4)	(2.1)	(5.5)	(2.7)	2.0	(4.4)	(315.5)	110.2
TOTAL	13.5	33.0	38.2	24.6	24.9	37.9	38.6	2.0	1.2
PBT Margins (%)									
Logistics and Distribution	(0.8)	1.9	3.2	0.3	1.0	3.0	2.3		
Manufacturing	19.9	26.0	28.0	29.9	25.2	18.1	33.0		
TOTAL	3.1	5.8	8.1	4.7	5.0	6.0	8.2		

Source: Bursa Malaysia, Kenanga Research

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Income Statement

FY Dec (RM m)	2012A	2013A	2014A	2015E	2016E
Revenue	1812.3	1946.6	2122.9	2324.6	2545.4
EBITDA	160.3	160.4	189.9	209.2	229.1
Depreciation	-44.1	-54.5	-49.7	-54.0	-52.9
Operating profit	116.3	105.8	140.2	155.2	176.2
Other income	1.1	1.3	1.3	3.3	4.2
Interest Exp	-15.0	-14.7	-16.8	-13.8	-17.8
Associate	0.0	0.0	0.0	0.0	0.0
PBT	103.3	93.0	125.5	145.6	163.4
Taxation	-40.1	-36.2	-31.4	-45.1	-53.9
Minority Interest	-1.5	-1.6	-0.4	-0.4	-0.5
Net Profit	61.7	55.2	93.8	100.0	109.0

Balance Sheet

FY Dec (RM m)	2012A	2013A	2014A	2015E	2016E
Fixed Assets	339.7	353.4	369.8	410.2	451.6
Intangible Assets	149.5	124.5	233.0	233.0	233.0
Other FA	10.3	18.7	35.7	35.7	35.7
Inventories	464.9	410.5	427.0	490.2	536.8
Receivables	199.5	132.4	142.9	156.5	171.4
Other CA	24.4	38.6	2.3	2.3	2.3
Cash	34.6	32.9	32.0	87.1	109.8
Total Assets	1,222.8	1,111.0	1,242.7	1,415.0	1,540.6
Payables	306.2	337.4	448.6	491.2	537.8
ST Borrowings	341.0	199.6	200.1	260.0	300.0
Other ST Liability	76.6	52.9	6.5	8.1	8.1
LT Borrowings	0.1	0.3	1.1	46.2	51.9
Other LT Liability	11.2	17.6	34.5	34.5	34.5
Minorities Int.	15.8	15.6	25.5	25.9	26.4
Net Assets	472.0	487.6	526.5	549.1	581.9
Share Capital	117.7	129.4	129.4	129.4	129.4
Reserves	354.3	358.2	397.1	419.7	452.4
Equity	472.0	487.6	526.5	549.1	581.8

Cashflow Statement

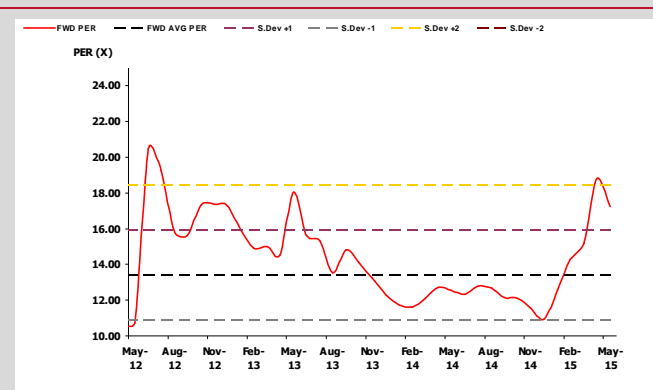
FY Dec (RM m)	2012A	2013A	2014A	2015E	2016E
Operating CF	16.7	254.9	213.5	120.3	147.5
Investing CF	(127.3)	(84.0)	(154.5)	(60.0)	(60.0)
Financing CF	89.5	(171.3)	(60.1)	(5.1)	(64.9)
Change In Cash	(21.1)	(0.4)	(1.2)	55.1	22.6
Free CF	(5.8)	211.4	123.5	60.3	87.5

Source: Bursa Malaysia, Kenanga Research

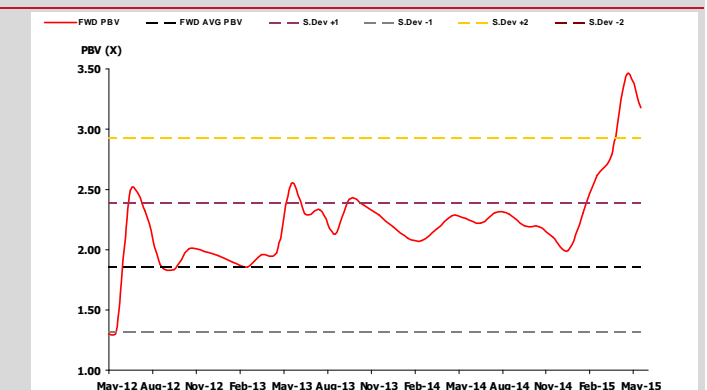
Financial Data & Ratios

FY Dec (RM m)	2012A	2013A	2014A	2015E	2016E
Growth					
Turnover (%)	19.2%	7.4%	9.1%	9.5%	9.5%
EBITDA (%)	39.9%	0.0%	18.4%	10.2%	9.5%
Operating Profit (%)	56.4%	-9.0%	32.5%	10.7%	13.5%
PBT (%)	41.2%	-10.0%	35.0%	16.0%	12.2%
Core Net Profit (%)	18.3%	-10.5%	69.9%	6.7%	9.0%
Profitability (%)					
EBITDA Margin	8.8%	8.2%	8.9%	9.0%	9.0%
Operating Margin	6.4%	5.4%	6.6%	6.7%	6.9%
PBT Margin	5.7%	4.8%	5.9%	6.3%	6.4%
Core Net Margin	5.50%	8.10%	8.50%	6.60%	6.50%
Effective Tax Rate	38.8%	39.0%	33.0%	31.0%	33.0%
ROA	5.0%	5.0%	7.5%	7.1%	7.1%
ROE	13.1%	11.3%	17.8%	18.2%	18.7%
DuPont Analysis					
Net Margin (%)	3.4%	2.8%	4.4%	4.3%	4.3%
Assets Turnover (x)	0.7	0.6	0.6	0.6	0.6
Leverage factor (x)	2.6	2.3	2.4	2.6	2.6
ROE (%)	13.1%	11.3%	17.8%	18.2%	18.7%
Leverage					
Debt/Asset (x)	0.3	0.2	0.2	0.2	0.2
Debt/Equity (x)	0.7	0.4	0.4	0.6	0.6
Net Cash/(Debt)	-306.5	-167.0	-169.2	-219.1	-242.1
Net Debt/Equity (x)	0.6	0.3	0.3	0.4	0.4
Valuations					
EPS (sen)	23.8	21.3	36.2	38.6	42.1
NDPS (sen)	6.3	16.0	28.0	29.9	29.5
BVPS (RM)	1.82	1.88	2.03	2.12	2.25
PER (x)	29.0	32.4	19.1	17.9	16.4
Net Div. Yield (%)	0.9	2.3	4.1	4.3	4.3
P/BV (x)	3.8	3.7	3.4	3.3	3.1

Fwd PER Band



Fwd PBV Band



Source: Bloomberg, Kenanga Research

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Peer Comparison															
NAME	Price	Mkt Cap	PER (x)			Est. Div. Yld.	Est. ROE	P/BV	Net Profit (RMm)			1 Yr Fwd NP Growth	2 Yr Fwd NP Growth	Target Price	Rating
	(RM)	(RMm)	Actual	1 Yr Fwd	2 Yr Fwd	(%)	(%)	(x)	Actual	1 Yr Fwd	2 Yr Fwd	(%)	(%)	(RM)	
IHH HEALTHCARE BHD	5.99	49207.0	65.2	56.8	51.6	0.5	4.2	2.4	754.3	867.0	954.0	14.9	10.0	5.00	Underperform
KPJ HEALTHCARE BERHAD	4.24	4393.1	30.7	35.1	33.0	0.0	9.0	3.2	143.0	125.0	133.0	-12.6	6.4	3.54	Underperform
PHARMANIAGA BERHAD	6.91	1788.9	19.1	17.9	16.4	0.0	18.2	3.3	93.8	100.0	109.0	6.6	9.0	6.95	Outperform

Source: Bloomberg, Kenanga Research

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Stock Ratings are defined as follows:**Stock Recommendations**

OUTPERFORM	: A particular stock's Expected Total Return is MORE than 10% (an approximation to the 5-year annualised Total Return of FBMKLCI of 10.2%).
MARKET PERFORM	: A particular stock's Expected Total Return is WITHIN the range of 3% to 10%.
UNDERPERFORM	: A particular stock's Expected Total Return is LESS than 3% (an approximation to the 12-month Fixed Deposit Rate of 3.15% as a proxy to Risk-Free Rate).

Sector Recommendations***

OVERWEIGHT	: A particular sector's Expected Total Return is MORE than 10% (an approximation to the 5-year annualised Total Return of FBMKLCI of 10.2%).
NEUTRAL	: A particular sector's Expected Total Return is WITHIN the range of 3% to 10%.
UNDERWEIGHT	: A particular sector's Expected Total Return is LESS than 3% (an approximation to the 12-month Fixed Deposit Rate of 3.15% as a proxy to Risk-Free Rate).

*****Sector recommendations are defined based on market capitalisation weighted average expected total return for stocks under our coverage.**

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