

Pharmaniaga Berhad

(7081 | PHRM MK) Health Care | Pharmaceuticals

Upgrade to BUY

(Previously NEUTRAL)

Expecting better earnings in subsequent quarters

Revised Target Price: RM2.35

(Previously RM2.27)

KEY INVESTMENT HIGHLIGHTS

- **4QFY19 normalised earnings came in at RM9.4m, which is above ours but lagged consensus expectations**
- **The quarterly performance was impacted by the full amortisation of Pharmacy Information System**
- **However, we expect the strong sales growth will contribute to improve earnings and cash position going forward**
- **Upgrade to BUY with a revised TP of RM2.35 per share**

4QFY19 performance impacted by a non-recurring item.

Pharmaniaga's recorded a loss of -RM178.6m in the 4QFY19. However, after exclusion of a non-recurring item, 4QFY19 normalised earnings increase more than two fold to RM9.4m on a year-over-year basis. This brings its full year FY19 normalised earnings to RM38.7m which was above ours but met consensus earnings estimates at 106.9% and 96.8% respectively.

Strong sales recorded during the quarter. Pharmaniaga reported solid 4QFY19 sales growth of +20.0%yoy to RM715.7m which was in line with the growth of logistics and distribution (L&D) division. During the quarter, revenue for the division grew by +23.8%yoy to RM508.2m driven by the stronger demand from the concession and non-concession businesses.

PhIS costs were fully amortised during the quarter. Following the new contract awarded by the Ministry of Health (MOH), the group has to revise the useful life of rights to supply. The rights to supply are expenses incurred for Pharmacy Information System (PhIS), being part and parcel of the ordinary contractual obligations under the Concession Agreement. With the new contract arrangement, the remaining unamortised rights to supply amounting to RM247.0m has been fully recognised during the quarter.

Expecting stronger cash flow position. The group's operating cash flow had turned positive at RM188.8m at the end of Q4FY19 (from -RM82.8m at the end of Q4FY18) due to the higher sales recorded and improved collection. The additional cash were used to pared down debt by RM81.4m or -12.2%yoy.

Impact to earnings. We are revising FY20F and FY21F earnings forecast upwards by +8.1% and +14.7% respectively to take into account: (i) stronger sales momentum and; (ii) lower amortisation rate as PhIS costs has been fully amortised.

Target price. We are revising our target price to **RM2.35** (previously RM2.27) per share. This is premised on pegging revised FY21F EPS of 19.6sen to target PER of 12.0x which is the average of its historical two-year rolling PER.

RETURN STATISTICS

Price @ 20 th February 2020 (RM)	2.04
Expected share price return (%)	+15.2
Expected dividend yield (%)	+5.3
Expected total return (%)	+20.5

SHARE PRICE CHART




Share price performance (%)	Absolute	Relative
1 month	-1.4	2.0
3 months	-1.0	-3.7
12 months	-25.2	-16.3

KEY STATISTICS

FBM KLCI	1534.98
Syariah compliant	Yes
Issue shares (m)	260.51
Estimated free float (%)	13.82
Market Capitalisation (RM'm)	532.91
52-wk price range	RM1.83 – RM2.88
Beta vs FBM KLCI (x)	0.87
Monthly velocity (%)	10.84
Monthly volatility (%)	19.42
3-mth average daily volume (m)	0.25
3-mth average daily value (RM'm)	0.53
Top Shareholders (%)	
Boustead Holdings Bhd	55.93
Lembaga Tabung Angkatan Tentera	11.20
Kamaruddin Lodin Bin Wok	4.79

ANALYST

NABIL Zainoodin, CFA, CA
nabil.zainoodin@midf.com.my
 03 -2772 1663

Upgrade to BUY. In November 2019, the government had extended Pharmaniaga's services for the provision of medicines and medical supplies to MOH facilities to the end of FY21 and provided them with a new contract to continue providing logistics and distribution services for MOH to over 148 government hospitals and 1,700 clinics nationwide until the end of FY24. Nonetheless, with the new contract arrangement, the group was significantly impacted by the recognition of the remaining unamortised PhIS of RM247.0m which caused the group to report a loss in 4QFY19. Moving forward, we expect strong sales growth from concession and non-concession businesses will contribute to an improvement in Pharmaniaga's earnings and cash position going forward. All things considered, we are upgrading our call recommendation to **BUY** from neutral previously, considering the stock is currently trading at an attractive forward PER of 10.4x (-1.5SD below its three year historical PER average) and dividend yield of about five percent. 

INVESTMENT STATISTICS

Financial year ending 31st December (in RM'm, unless otherwise stated)	2018	2019	2020E	2021F	2021F
Revenue	2,385.0	2,820.5	2,961.6	3,080.0	3,172.4
Cost of sales	(2,062.8)	(2,726.5)	(2,576.6)	(2,673.5)	(2,750.5)
Gross profit	322.1	94.0	385.0	406.6	421.9
Finance cost	(36.1)	(40.3)	(44.4)	(46.2)	(47.6)
Profit before tax and zakat	70.2	(191.9)	71.1	80.1	88.8
Income tax	(25.9)	42.4	(25.3)	(28.8)	(32.0)
Profit after tax	43.2	(149.4)	45.7	51.3	56.8
PATAMI	42.5	(149.2)	45.3	50.7	56.3
Normalised PATAMI	42.5	38.7	45.3	50.7	56.3
Normalised EPS (sen)	16.3	15.0	17.5	19.6	21.7
EPS growth (%)	-21.5	-8.4	16.9	12.0	10.9
PAT margin (%)	1.8	NA	1.5	1.7	1.8
Normalised PATAMI margin (%)	1.8	1.4	1.5	1.6	1.8
PER (x)	12.5	13.6	11.7	10.4	9.4
Dividend per share (sen)	16.0	8.5	9.6	10.8	12.0
Dividend yield (%)	7.8	4.2	4.7	5.3	5.9

Source: Company, MIDFR

PHARMANIAGA BHD: 4QFY19 RESULTS SUMMARY

FYE Dec (RM'm)	Quarterly results			Cumulative results	
	4QFY19	YoY (%)	QoQ (%)	FY19	YoY (%)
Revenue	715.7	20.0	(0.2)	2,820.5	18.3
Cost of sales	(869.6)	65.7	33.8	(2,726.5)	32.2
Gross Profit	(153.9)	nm	nm	94.0	(70.8)
Other income	0.2	>100	(24.2)	1.2	29.8
Operating expenses	(76.1)	50.0	23.5	(248.2)	14.0
EBIT	(229.8)	nm	nm	(153.0)	nm
Finance cost	(9.2)	(4.3)	(17.2)	(40.3)	11.6
Interest income	0.5	32.5	>100	1.4	54.8
Profit Before Tax and Zakat	(238.5)	(2,097.3)	>100	(191.9)	nm
Zakat	0.2	0.0	nm	(2.2)	>100
Income tax	59.6	nm	nm	44.7	(272.3)
Profit After Tax	(178.7)	nm	>100	(149.4)	(445.7)
Minority interest	(0.1)	nm	28.6	(0.2)	(129.9)
PATAMI	(178.6)	nm	nm	(149.2)	nm
Normalised PATAMI	9.4	>100	nm	38.7	(8.8)
GP margin (%)	-21.5%	nm	nm	3.3%	(75.3)
PBT margin (%)	-33.3%	nm	nm	-6.8%	nm
PATAMI margin (%)	-25.0%	nm	nm	-5.3%	nm
Normalised PATAMI	1.3%	76.0	nm	1.4%	(22.9)
Effective tax rate (%)	25.0%	(59.2)	nm	23.3%	(36.9)

Source: Company, MIDFR

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MIDF AMANAH INVESTMENT BANK : GUIDE TO RECOMMENDATIONS

STOCK RECOMMENDATIONS

BUY	Total return is expected to be >10% over the next 12 months.
TRADING BUY	Stock price is expected to <i>rise</i> by >10% within 3-months after a Trading Buy rating has been assigned due to positive newsflow.
NEUTRAL	Total return is expected to be between -10% and +10% over the next 12 months.
SELL	Total return is expected to be <10% over the next 12 months.
TRADING SELL	Stock price is expected to <i>fall</i> by >10% within 3-months after a Trading Sell rating has been assigned due to negative newsflow.

SECTOR RECOMMENDATIONS

POSITIVE	The sector is expected to outperform the overall market over the next 12 months.
NEUTRAL	The sector is to perform in line with the overall market over the next 12 months.
NEGATIVE	The sector is expected to underperform the overall market over the next 12 months.