Pharmaniaga Berhad

(7081 | PHRM MK) Health Care | Pharmaceuticals

Downgrade to NEUTRAL

(from BUY)

Pharmaniaga falls into PN17

***Revised* Target Price: RM0.48**

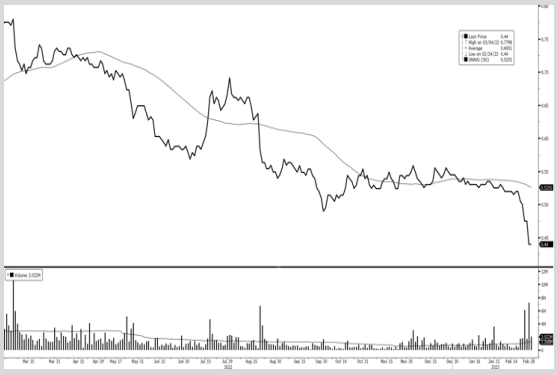
(previously RM0.77)

KEY INVESTMENT HIGHLIGHTS

- **Pharmaniaga's FY22 net earnings tumbled into a deficit of -RM607; below yearly earnings forecast**
- **Earnings loss due to vaccine impairment and high operating cost**
- **FY22 revenue reduced by -27%**
- **Revise FY23-24 earnings forecast down -79% and -83%**
- **Downgrade to NEUTRAL with revised TP of RM0.48**

RETURN STATISTICS	
Price @ 27th February 2023	0.44
Expected share price return (%)	+9.1
Expected dividend yield (%)	-0.3
Expected total return (%)	**+8.8**

SHARE PRICE CHART



Share price performance (%)	Absolute	Relative
1 month	-17.8	-15.4
3 months	-19.3	-18.3
12 months	-47.6	-42.7

KEY STATISTICS	
FBM KLCI	1,455.50
Syariah compliant	Yes
F4GBM Index	Yes
ESG Grading Band	☆
Issue shares (m)	1309.96
Estimated free float (%)	34.84
Market Capitalisation (RM'm)	576.49
52-wk price range	RM0.43 - RM0.86
Beta vs FBM KLCI (x)	1.19
3-mth average daily volume (m)	1.25
3-mth average daily value (RM'm)	0.65
Top Shareholders (%)	0
Boustead Holdings Bhd	51.84
Lembaga Tabung Angkatan Tentera	8.62
UBS AG	1.44

Earnings tumbled into a deficit. In 4QFY22, Pharmaniaga Berhad (Pharmaniaga) earnings tumbled into a deficit of -RM644.4m, from RM85.5m in 4QFY21 and RM8.6m in 3QFY22. For FY22, earnings slumped into a deficit of -RM607.3m; which came in **below** our and consensus' expectations. Meanwhile, the group's revenue rose by +21.2%yoy but slipped -6.7%qoq to RM862.7m in 4QFY22. For FY22, revenue slipped -27.1%yoy to RM3.51b. The lower demand for Covid-19 vaccines (which resulted in inventory write-off) had dragged both revenue and earnings for FY22, as well as higher travelling cost, repair and maintenance, and rental of warehouses. This was however offset by: (i) growth in the concession business as additional products were added into the concession list, (ii) improved contribution from the private sector by approximately 50% as a result of aggressive sales efforts, and (iii) new products launched to the market.

Logistics and Distribution. Revenue rose by +31.9%yoy but dropped -8%qoq to RM609.6m, while earnings slipped to a deficit of -RM7.1m from RM18.6m in 4QFY21 and RM37m in 3QFY22. For FY22, revenue rose by +10.5%yoy to RM2.52b, while earnings declined -3.4%yoy to RM50.1m. Lower FY22 earnings were due to lower distribution income on Covid-19 vaccines and higher operating costs of opening 3 new warehouses for the volume increase; offset by stronger contribution from the concession business and improved contribution from the private sector.

Manufacturing. Revenue added +17.1%yoy and +14.2%qoq to RM102.6m, while earnings declined to -RM562m, from RM4m in 4QFY21 and RM28.9m in 3QFY22. For FY22, revenue dropped -82.5%yoy to RM326.3m, and earnings declined to a deficit of -RM520.1m from RM126.1m in FY21. The earnings deficit was due to the provision for slow moving inventories on Covid-19 vaccines in adherence to the requirement of MFRS102 Inventories.

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Indonesia. Revenue was up by +15.9%yoy but dropped -3.4%qoq to RM251.3m in 4QFY22. Earnings recorded a deficit of -RM44.5m from a deficit of -RM2.6m in 4QFY21 and RM18.9m in 3QFY22. For FY22, revenue jumped +10.1%yoy to RM983.2m, but earnings slipped into a deficit of -RM21.7m from -RM1.4m in FY21. The lower FY22 earnings was due to impairment of goodwill of the Indonesia manufacturing cash-generating unit of RM50.3m. Nevertheless, improved operational efficiency include among others stock optimisation and aggressive collection effort as well as digitalisation in its business processes mitigated the losses.

Vaccines in slow demand. Despite the RM552.3m provisions on slow-moving inventories for the Covid-19 vaccine, we believe that Pharmaniaga's performance will see improvement in FY23. The group will keep working to negotiate the sale of the vaccinations with other parties. Additionally, the Government has postponed the concession agreement negotiations with the group until June CY23. While Pharmaniaga is engaged in final talks, business as usual continues to be conducted. In the meantime, the group's +50%yoy increase in the private market was reported, and it aims to maintain the uptrend in CY23. We believe the group will continue to concentrate on entering the Indonesian market for its future growth.

Moving forward. Pharmaniaga will continue to actively enhance the division's operational efficiency and will build on its growing portfolio of products to broaden its global presence, as well as leverage on its increased capacity utilisation via its contract manufacturing business. With continued expansion of the group's new product portfolio coupled with sustained demand, the long-term prospects for its manufacturing division remain optimistic. Stripping the impairment, the group made about RM15m in core net profit in FY22. Similarly, barring unforeseen circumstances, we believe Pharmaniaga will continue to leverage on its capacity and capability in drug manufacturing and distribution.

PN17 announced. Pharmaniaga announced that the recent results had triggered the PN17 prescribed criteria; on the basis that Paragraph 2.1(a) of Practice Notes 17.

Revised FY23-24 earnings estimates. In consideration of Pharmaniaga's FY22 earnings coming in below our expectations, we revise our earnings estimates for FY23 and FY24 downwards by -79% and -87% respectively. As such, we **revise our target price to RM0.48** (previously RM0.77), by pegging a PER of 20x to a revised EPS23 of 2.4 sen. The PER is based on the pharmaceutical industry's 5-year average.

Revised to NEUTRAL. All in all, we downgrade our recommendation from BUY to **NEUTRAL** with **revised target price of RM0.48.** Nevertheless, we maintain a positive view on the group on the basis of its: (i) large portfolio of pharmaceutical products in line with growing demand, (ii) halal market penetration, and (iii) long-term marketing plan for international sales. We also remain cautious on Pharmaniaga's future performance pending the sale of its Covid-19 vaccines.

INVESTMENT STATISTICS

Financial year ending 31st December (in RM'm, unless otherwise stated)	2020A	2021A	2022E	2023F	2024F
Revenue	2,725.1	4,815.0	3,848.5	4,419.1	5,182.0
Cost of sales	(2,726.5)	(4,185.0)	(3,425.2)	(3,955.1)	(4,637.9)
Gross profit	(1.5)	630.0	**423.3**	**464.0**	**544.1**
Profit after tax	**(270.4)**	**172.2**	**56.7**	**67.9**	**87.7**
Normalised PATAMI	**(81.5)**	**172.2**	**58.43**	**71.32**	**92.08**
Normalised EPS (sen)	2.1	13.1	4.5	5.4	7.0
EPS growth (%)	-86.0	526.0	23.2	157.3	158.2
PAT margin (%)	-9.9	3.6	1.5	1.5	1.7
Normalised PATAMI margin (%)	-3.0	3.6	1.5	1.6	1.8
PER (x)	46.3	7.8	17.3	14.1	11.0
Dividend per share (sen)	0.0	5.0	4.0	5.0	6.7
Dividend yield (%)	0.0	4.9	5.2	6.5	8.7

Source: Company, MIDFR

Table 1: Pharmaniaga's quarterly earnings review

Financial year ending 31st December (in RM'm unless otherwise stated)	Quarterly results					Cumulative results		
	4QFY21	3QFY22	4QFY22	QoQ (%)	YoY (%)	FY21	FY22	YoY (%)
Revenue	711.7	924.7	862.7	(6.7)	21.2	4,815.0	3,510.7	(27.1)
Cost of sales	(554.6)	(825.6)	(790.0)	(4.3)	42.4	(4,185.0)	(3,138.2)	(25.0)
Gross Profit	**157.1**	**99.1**	**72.7**	(26.6)	(53.7)	**630.0**	**372.5**	(40.9)
Other income	0.9	0.1	2.7	2,000.0	213.1	1.5	3.1	107.5
Operating expenses	(25.5)	(74.0)	(701.6)	847.9	2,648.4	(322.6)	(917.3)	184.3
EBIT	**132.4**	**25.2**	**(626.1)**	(2,584.5)	(572.8)	**308.9**	**(541.7)**	(275.4)
Finance cost	(7.9)	(9.7)	(12.5)	28.6	58.6	(33.3)	(40.0)	20.1
Interest income	0.6	0.1	0.2	88.9	(57.7)	1.5	0.9	(40.2)
Profit Before Tax and Zakat	**125.1**	**15.6**	**(638.4)**	(4,195.2)	(610.4)	**277.1**	**(580.8)**	(309.6)
Zakat	(12.3)	(0.6)	(12.3)	1,945.5	0.0	(24.1)	(0.2)	(99.1)
Income tax	(27.7)	(5.6)	(7.4)	31.7	(73.3)	(80.8)	(24.0)	(70.3)
Profit After Tax	**85.2**	**9.4**	**(644.2)**	(6,970.0)	(856.4)	**172.2**	**(605.1)**	(451.4)
Minority interest	(0.3)	0.8	0.2	(74.6)	(162.3)	0.1	2.3	4,021.8
PATAMI	**85.5**	**8.6**	**(644.4)**	(7,578.1)	(853.9)	**172.2**	**(607.3)**	(452.8)
Normalised PATAMI	**85.5**	**8.6**	**(644.4)**	(7,578.1)	(853.9)	**172.2**	**(607.3)**	(452.8)
Basic EPS (sen)	6.5	0.7	(49.2)	(7,553.0)	(853.3)	20.2	(48.5)	(339.9)
Diluted EPS (sen)	6.5	0.7	(49.2)	(7,553.0)	(853.3)	208.2	(48.5)	(123.3)
DPS (sen)	4.3	9.3	9.3	0.0	116.3	12.0	9.3	(22.5)
				+/-ppts				*+/-ppts*
GP margin (%)	22.1%	10.7%	8.4%	(0.0)	(0.1)	13.1%	10.6%	(0.0)
PBT margin (%)	17.6%	1.7%	-74.0%	(0.8)	(0.9)	5.8%	-16.5%	(0.2)
PATAMI margin (%)	12.0%	0.9%	-74.7%	(0.8)	(0.9)	3.6%	-17.3%	(0.2)
Normalised PATAMI margin (%)	12.0%	0.9%	-74.7%	(0.8)	(0.9)	3.6%	-17.3%	(0.2)
Effective tax rate (%)	22.1%	36.0%	-1.2%	(0.4)	(0.2)	29.2%	-4.1%	(0.3)
Segmental								
Revenue								
Logistics & Distribution	462.1	662.9	609.6	(8.0)	31.9	2,276.2	2,514.6	10.5
Manufacturing	87.6	89.8	102.6	14.2	17.1	1,865.3	326.3	(82.5)
Indonesia	216.9	260.0	251.3	(3.4)	15.9	893.1	983.2	10.1
Net Profit								
Logistics & Distribution	18.6	37.0	(7.1)	(119.2)	(138.1)	51.8	50.1	(3.4)
Manufacturing	4.0	28.9	(562.0)	(2,045.3)	(14,250.1)	126.1	(520.1)	(512.5)
Indonesia	(2.6)	18.9	(44.5)	(335.0)	1,599.5	(1.4)	(21.7)	1,502.3

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 *rise* 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 *fall* 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.
ESG RECOMMENDATIONS* - source Bursa Malaysia and FTSE Russell	
☆☆☆☆	Top 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆☆	Top 26-50% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆☆	Top 51%- 75% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell
☆	Bottom 25% by ESG Ratings amongst PLCs in FBM EMAS that have been assessed by FTSE Russell

* ESG Ratings of PLCs in FBM EMAS that have been assessed by FTSE Russell in accordance with FTSE Russell ESG Ratings Methodology