

20 August 2018 | 2QFY18 Results Review

## Pharmaniaga Berhad

*Earnings impacted by rising tax expense*

### INVESTMENT HIGHLIGHTS

- 2QFY18 earnings lagged estimates
- Increased in revenue contribution from L&D
- Operating profit dragged by high operating expenses & tax
- Declared a second interim dividend of 4.0sen
- Maintain NEUTRAL with revised TP of RM3.00 per share

**2QFY18 earnings lagged estimates.** Pharmaniaga's 2QFY18 earnings came in at RM5.4m which lagged our and consensus earnings estimates at 42.6% and 37.8% respectively. Revenue for the quarter rose by +12.5%yoy but earnings declined by -43.8%yoy on a year-over-year basis respectively.

**Increased in revenue contribution from L&D.** In 2QFY18, Pharmaniaga's higher revenue of RM582.7m (from RM518.0m in 2QFY17) was mainly due to the higher revenue contribution coming from logistic and distribution (L&D) division. The L&D segment revenue contribution rose by +21.3%yoy mainly attributable to the increase demand from government hospitals. This was partially mitigated by a lower revenue from its Indonesian division which dipped by -4.8%yoy. The reasons for the dipped were because of the depreciation of the Malaysian Ringgit against the Indonesian Rupiah and increased in finance costs.

**High operating expenses and tax dragged operating profit.** Despite the higher revenue during the quarter, Pharmaniaga recorded earnings of RM5.4m in 2QFY18 which is -43.8%yoy lower than 2QFY17's earnings. This was mainly due to the decline in operating profit of L&D division by -45.9%yoy as operating expenses increased. This was due to the higher provision for stock obsolescence and receivables which increased by two-fold and five-fold respectively. Meanwhile, effective tax rate rose to 43.3% in 2QFY18 from 29.4% in the previous year corresponding quarter as a result of increased profitability of certain subsidiaries and non-deductible expenses.


**Second interim dividend declared.** Pharmaniaga declared a second interim dividend of 4.0sen per share for the quarter under review.

**Maintain NEUTRAL**  
**Revised Target Price: RM3.00**  
*(Previously RM4.20)*

RETURN STATS	
Price (17 <sup>th</sup> August 2018)	RM3.11
Target Price	RM3.00
Expected Share Price Return	-3.5%
Expected Dividend Yield	+2.0%
<b>Expected Total Return</b>	<b>-1.5%</b>

STOCK INFO	
KLCI	1,783.47
Bursa / Bloomberg	7081 / PHRM MK
Board / Sector	Main / Trading Services
Syariah Compliant	YES
Issued shares (mil)	260.51
Market cap. (RM'm)	810.17
Price over NA	1.54
52-wk price Range	RM2.86-RM4.65
Beta (against KLCI)	0.64
3-mth Avg Daily Vol	0.09m
3-mth Avg Daily Value	RM0.32m
Major Shareholders (%)	
Boustead Holding Bhd	56.09
LTAT	11.23
Kamaruddin Lodin	4.80

**Downward revision in earnings forecasts.** Following the earnings announcement, we are revising down our earnings forecasts for FY18F and FY19F by -13.5%yoy and -9.8%yoy respectively. We are inputting a higher effective tax rate and rising operating expenses going forward due to challenging business environment. Key rerating catalysts to our earnings forecasts would be: (i) better-than-expected government concession orders and; (ii) better-than-expected cost reduction.

**Maintain NEUTRAL with a revised TP of RM3.00.** All in, we are maintaining our **NEUTRAL** recommendation on Pharmaniaga with a revised TP of **RM3.00** (from RM4.20 per share previously) post earnings revision. Our TP is derived via pegging our FY19F EPS of 21sen to FY19F target PER of 14.3x which is -1SD lower than the average of its historical five-year rolling PER. We believe that the future procurement of drugs and medical supplies from the Ministry of Health will continue to be moderate as it tries to manage the escalating healthcare costs in the public hospitals. That said, we take comfort in the fact that both its private sector business as well as Indonesian operation have been contributing well to the group's overall earnings which we think will bode well for the company. 

**Table 1: Pharmaniaga's quarterly earnings review**

FYE Dec (RM'm)	Quarterly results				Cummulative results			
	2QFY17	1QFY18	2QFY18	QoQ (%)	YoY (%)	1HFY17	1HFY18	YoY (%)
Revenue	518.0	617.9	582.7	(5.7)	12.5	1,136.3	1,200.7	5.7
Cost of sales	(450.3)	(526.0)	(500.3)	(4.9)	11.1	(974.2)	(1,026.3)	5.4
<b>Gross Profit</b>	<b>67.7</b>	<b>91.9</b>	<b>82.4</b>	(10.3)	21.7	<b>162.1</b>	<b>174.3</b>	7.5
Other income	0.0	0.7	0.2	(76.5)	nm	0.0	0.9	nm
Operating expenses	(51.2)	(56.4)	(62.3)	10.5	21.8	(111.5)	(118.7)	6.5
<b>EBIT</b>	<b>16.5</b>	<b>36.2</b>	<b>20.2</b>	(44.0)	22.7	<b>50.6</b>	<b>56.4</b>	11.5
Finance cost	(6.4)	(7.6)	(8.5)	12.4	32.6	(12.8)	(16.0)	25.3
Interest income	0.1	0.1	0.2	160.0	108.0	0.2	0.3	44.0
<b>Profit Before Tax and Zakat</b>	<b>10.2</b>	<b>28.7</b>	<b>12.0</b>	(58.3)	17.4	<b>38.0</b>	<b>40.7</b>	7.0
Zakat	(0.1)	(0.1)	(0.1)	nm	nm	(0.1)	(1.0)	881.0
Income tax	(0.3)	(0.3)	(5.2)	1,641.0	1,641.0	(8.8)	(16.3)	85.3
<b>Profit After Tax</b>	<b>9.8</b>	<b>17.6</b>	<b>5.8</b>	(67.2)	(41.2)	<b>29.1</b>	<b>23.4</b>	(5.7)
Minority interest	(0.2)	0.0	0.4	nm	(286.0)	(0.5)	0.4	0.9
<b>PATAMI</b>	<b>9.6</b>	<b>17.6</b>	<b>5.4</b>	(69.3)	(43.8)	<b>28.5</b>	<b>23.0</b>	(5.6)

Source: Company, MIDFR

**Table 2: Pharmaniaga's quarterly segmental breakdown**

Segmental Breakdown	Quarterly results				Cumulative results			
	2QFY17	1QFY17	2QFY18	QoQ (%)	YoY (%)	1HFY17	1HFY18	YoY (%)
<b>Revenue</b>								
Logistics & Distribution	343.2	455.0	416.3	(8.5)	21.3	783.7	871.3	11.2
Manufacturing	0.7	0.6	0.7	22.8	0.8	1.5	1.3	(9.8)
Indonesia	174.0	162.4	165.7	2.1	(4.8)	351.1	328.1	(6.6)
<b>Total Revenue</b>	<b>518.0</b>	<b>617.9</b>	<b>582.7</b>	(5.7)	12.5	<b>1,136.3</b>	<b>1,200.7</b>	5.7
<b>EBIT</b>								
Logistics & Distribution	5.9	14.1	3.2	(77.3)	(45.9)	12.3	17.4	41.4
Manufacturing	8.3	20.0	16.1	(19.4)	93.4	34.7	36.0	4.0
Indonesia	2.9	2.1	4.2	101.0	41.9	5.8	6.2	8.4
<b>Total EBIT</b>	<b>17.2</b>	<b>36.2</b>	<b>23.5</b>	(35.2)	36.6	<b>52.7</b>	<b>59.6</b>	13.2

Source: Company, MIDFR

## INVESTMENT STATISTICS

FYE Dec (RM'm)	FY2015	FY2016	FY2017	FY2018F	FY2019F
Revenue	2,189.3	2,189.0	2,324.0	2,364.0	2,437.5
Cost of sales	(1,836.5)	(1,845.8)	(1,988.8)	(2,033.0)	(2,097.5)
<b>Gross profit</b>	<b>352.9</b>	<b>343.2</b>	<b>335.2</b>	<b>331.0</b>	<b>340.0</b>
Finance cost	(15.1)	(33.7)	(28.8)	(25.0)	(26.2)
<b>Profit Before Tax and Zakat</b>	<b>112.7</b>	<b>72.0</b>	<b>73.1</b>	<b>72.7</b>	<b>75.7</b>
Income tax	(27.4)	(25.9)	(17.4)	(25.4)	(21.2)
<b>Profit After Tax</b>	<b>84.6</b>	<b>45.9</b>	<b>55.1</b>	<b>46.6</b>	<b>54.9</b>
EPS (sen)	0.32	0.18	0.21	0.18	0.21
EPS Growth (%)	-10.4	-43.9	15.5	-13.3	17.2
PER (x)	9.7	17.3	15.0	17.3	14.7
Dividend Per Share (sen)	0.30	0.16	0.19	0.13	0.06
Dividend yield (%)	4.7	5.1	6.1	4.1	2.0

Source: Company, MIDFR

## DAILY PRICE CHART



Noor Athila Mohd Razali  
noor.athila@midf.com.my  
03-2772 1679

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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.