

# China / Hong Kong Flash Note

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DBS Group Research . Equity

16 Aug 2017

## Yestar International (2393 HK) : HOLD (Downgrade from BUY)

Mkt. Cap: US\$1,048m | 3m Avg. Daily Val: US\$1.2m

Last Traded Price ( 15 Aug 2017): HK\$3.77

Price Target 12-mth: HK\$3.40 (10% downside) (Prev HK\$4.60)

### Analyst

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## Company Guide

[Yestar International](#)



Summary of our point of view, and highlights the relevant data points, which are actively tracked

## Stretched valuation

- Sharp moderation in earnings growth to 0.5% y-o-y in 1H17 from 24% in 2016 mainly due to surge in operating & finance costs
- Cut FY17F/18F earnings by 11%/14% to reflect weak performance of imaging products, higher operating cost, and tax rate
- Expect consensus to cut earnings estimates substantially which should trigger share price correction
- Downgrade to HOLD on stretched valuations and currency risk; TP lowered to HK\$3.4

### Forecasts and Valuation

FY Dec (RMB m)	2016A	2017F	2018F	2019F
Turnover	3,022	3,741	4,261	4,909
EBITDA	536	741	866	1,022
Pre-tax Profit	384	486	606	762
Net Profit	201	233	292	375
Net Pft (Pre Ex) (core profit)	201	233	292	375
Net Profit Gth (Pre-ex) (%)	23.5	15.7	25.6	28.2
EPS (RMB)	0.09	0.11	0.13	0.17
EPS (HK\$)	0.11	0.13	0.16	0.20
EPS Gth (%)	14.2	15.7	25.6	28.2
Diluted EPS (HK\$)	0.11	0.13	0.16	0.20
DPS (HK\$)	0.05	0.05	0.06	0.08
BV Per Share (HK\$)	0.51	0.59	0.69	0.83
PE (X)	34.8	30.1	23.9	18.7
P/Cash Flow (X)	23.6	18.4	12.2	11.4
P/Free CF (X)	24.5	19.4	12.7	11.8
EV/EBITDA (X)	13.8	11.1	9.2	7.6
Net Div Yield (%)	1.2	1.3	1.7	2.1
P/Book Value (X)	7.4	6.4	5.4	4.5
Net Debt/Equity (X)	0.4	1.0	0.5	0.2
ROAE (%)	21.7	22.9	24.6	26.4

Earnings Rev (%)	(11)	(14)	New
Consensus EPS (RMB)	0.15	0.19	0.24
Other Broker Recs:	B: 4	S: 0	H: 0

Source: Company, DBS Vickers, Thomson Reuters

### What's New

Earnings growth moderated sharply to 0.5% y-o-y in 1H17 from 24% in 2016 due to surge in operating & financial costs.

Even though Yestar's revenue in 1H17 grew 23% y-o-y driven by in-vitro diagnostic (IVD) segment which made up 63% of total sales, earnings growth was only 0.5%. This was due to:

- 1) Increase in selling & admin costs as a percentage of sales of 1.6ppt y-o-y to 12.5% due to surge in amortization of intangible assets resulting from acquisition of in-vitro diagnostic (IVD) device distributors in Guangdong last year, and an increase in selling expenses to further penetrate into the hospital market;
- 2) Surge in interest cost by 218% to Rmb62m after issuance of senior notes to raise US\$200m (coupon rate: 6.9%) in 2H16; and
- 3) Increase in effective tax rate by 5ppts to 34%, as interest expense from the senior notes mentioned above cannot be deducted for tax calculation purposes.

Cut 17F/18F earnings by 11%/14% to reflect weak performance of imaging products, higher admin & selling costs, and higher tax rate. We revised down the earnings estimates in 17F/18F to reflect the following:

- 1) Weak performance of Imaging products (e.g. color photographic paper). This segment made up 37% of 1H17

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sales, and its revenue dropped by 13% y-o-y due to competition and shrinking demand resulting from digitalization of photos and films. This trend should continue. Thus, we lowered FY17F/18F sales of this segment by 15%/19%;

- 2) We revised up FY17F/18F selling & admin costs as percentage of sales by 0.7ppt p.a. to reflect expenses from acquiring new customers in the hospital segment;
- 3) We have revised up the effective tax rate in 17F/18F by 4ppts p.a. as the interest expense of the senior notes cannot be used to deduct tax.

**Expect consensus to cut earnings estimates substantially which may trigger share price correction.**

As at 15 Aug 2017, the consensus is projecting Yestar to earn Rmb303m in FY17F. Stripping out 1H17 earnings of Rmb107m from this figure, the consensus is projecting Yestar to earn Rmb196m in 2H17F, implying y-o-y earnings growth of 107%. We do not think Yestar can achieve this. The cut in consensus' estimate is inevitable and that should likely trigger a share price correction.

**Downgrade to HOLD with TP lowered to HK\$3.4.** The stock is now trading at 30x FY17F PE. This valuation should have already priced in the projected earnings CAGR of 27% in 17F-19F. We believe there is not much room for Yestar to accelerate its

earnings growth. It has been relying on M&As to grow since 2014. However, as of Jun 17, its net debt to equity ratio already reached 161% (Dec 16: 43%), hence making it difficult to raise further debt for more M&As. Meanwhile, it also faces currency risk. The majority of its revenue is dominated in Rmb. But c.70% of its total debt as of Jun 17 is dominated in US\$ and it is paying interest in US\$ semi-annually (US\$7m each time) until 2021. Depreciation of Rmb against US\$ would increase Yestar's financial burden. Thus, we downgrade the stock from BUY to HOLD. Our previous TP is based on 34x FY17F PE (10% premium over healthcare sector's sector average in HK & Mainland China). To better reflect its earnings growth outlook, we changed our valuation methodology to 1x PEG (FY17F PE / EPS CAGR in FY17F-19F). Based on 1x PEG, the stock should trade at an implied 27x FY17F PE which results in a lower TP of HK\$3.4.

**Interim Income Statement (RMBm)**

FY Dec	1H2016	2H2016	1H2017	% chg yoy	% chg hoh
Revenue	1,437	1,585	1,763	22.7	11.2
Cost of Goods Sold	(1,081)	(1,175)	(1,268)	17.3	7.9
<b>Gross Profit</b>	<b>356</b>	<b>410</b>	<b>495</b>	<b>38.9</b>	<b>20.6</b>
Other Oper. (Exp)/Inc	(141)	(183)	(211)	50.2	15.7
<b>Operating Profit</b>	<b>216</b>	<b>228</b>	<b>284</b>	<b>31.5</b>	<b>24.6</b>
Other Non Opg (Exp)/Inc	0.0	0.0	0.0	nm	nm
Associates & JV Inc	0.0	0.0	0.0	nm	nm
Net Interest (Exp)/Inc	(17.8)	(41.6)	(59.5)	(234.3)	(43.1)
Exceptional Gain/(Loss)	0.0	0.0	0.0	nm	nm
<b>Pre-tax Profit</b>	<b>198</b>	<b>186</b>	<b>224</b>	<b>13.3</b>	<b>20.5</b>
Tax	(56.9)	(57.0)	(76.1)	33.8	33.6
Minority Interest	(34.6)	(34.3)	(41.1)	(18.7)	19.8
<b>Net Profit</b>	<b>106</b>	<b>94.7</b>	<b>107</b>	<b>0.5</b>	<b>12.9</b>
Net profit bef Except.	106	94.7	107	0.5	12.9
EBITDA	216	228	284	31.5	24.6
<b>Margins (%)</b>					
Gross Margins	24.8	25.9	28.1		
Opg Profit Margins	15.0	14.4	16.1		
Net Profit Margins	7.4	6.0	6.1		

Source: Company, DBS Vickers

DBSVHK recommendations are based on an Absolute Total Return\* Rating system, defined as follows:

**STRONG BUY** (>20% total return over the next 3 months, with identifiable share price catalysts within this time frame)

**BUY** (>15% total return over the next 12 months for small caps, >10% for large caps)

**HOLD** (-10% to +15% total return over the next 12 months for small caps, -10% to +10% for large caps)

**FULLY VALUED** (negative total return i.e. > -10% over the next 12 months)

**SELL** (negative total return of > -20% over the next 3 months, with identifiable catalysts within this time frame)

*Share price appreciation + dividends*

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