

China / Hong Kong Company Flash Note

Refer to important disclosures at the end of this report

DBS Group Research . Equity

17 November 2015

Yestar International (2393 HK)

BUY; HK\$2.98

Price Target: HK\$4.27 (43% upside)

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Key takeaways from meeting with Yestar's major supplier Roche Diagnostic

- Distribution of Roche (ROG VX) in-vitro diagnostic (IVD) devices is projected to contribute over 50% of Yestar's earnings in 2016 and 2017
- To drive the growth of IVD sales, Roche and Yestar are penetrating into top tier hospitals in inner provinces and Tier2/3 hospitals in developed regions
- To accelerate earnings growth, we believe Yestar is in talks with at least one M&A target
- Re-iterate BUY with TP unchanged at HK\$4.27. Chairman's buyback of 6.6m shares (0.3% stake) for HK\$19.9m at average price of HK\$3 in last one month echoes our positive view

We project that distribution of Roche (ROG VX) in-vitro diagnostic (IVD) devices will contribute c.37%/ 55%/ 55% of Yestar earnings in 15F/16F/17F. Roche is the largest IVD brand in China with 18% market share in 2014 (in terms of revenue). The second and third largest brands are Beckman and Sysmex (6869 JT) with 9% and 8% market share respectively. Roche's attitude towards the IVD business in China, and its strategy to grow its operations are crucial to Yestar's earnings growth going forward. Recently, we met the General Manager of Roche Diagnostic (Shanghai), Mr. Wong Fatt Heng, to discuss the above topics. Here are the key takeaways:

For Roche, IVD business in China is attractive and increasingly important. Diagnostic devices contributed 22-23% of Roche's total revenue in 2013/14. The contribution from IVD business in China to this segment has been increasing from close to 9% in 2013 to close to 10% in 2014. In 2015, it is likely to break through 11%. China's IVD business is increasingly attractive and important to Roche because:

1) In developed countries, IVD expenditure per capita is over US\$25 whereas in China, it is less than US\$3. There is huge room to grow.

2) Sales of IVD devices consist of two parts: equipment and consumables. Once the equipment is installed for service, there will be regular demand for relevant consumables for 5-10 years. This increases the visibility of future earnings.

3) Unlike many other medical devices which have to go through provincial tenders before selling to hospitals, IVD devices can be sold directly to individual hospitals. Thanks to this, IVD devices can avoid the price cut imposed by provincial governments for provincial tenders.

Currently, Roche is importing the majority of its IVD equipment and consumables from overseas. To optimise its operations in China, it is constructing a production plant in Suzhou (Jiangsu province) for IVD products. Roche plans to commence operations of that plant in 2016.

Penetration into Tier2/3 regions to drive strong sales growth.

In 2000-14, CAGR of Roche's IVD devices sales in China was 32%. In 2014-19, Roche targets to achieve annual revenue growth of 20.6% through two ways:

1) Further penetration into top tier hospitals in provinces with large population but are at the mid-level phases in terms of economic development. For example, Anhui province has a population of over 69m (ranked no.15 in 2014) and per capita GDP of around Rmb11,180 (ranked no. 28 in 2014).

2) Tier2/3 hospitals. Those are hospitals operating at a smaller scale relative to top tier hospitals. According to "Guideline on Promoting a Tiered-Diagnosis & Treatment System" released by the State Council in Sep 2015, China will strengthen the medical capabilities of Tier2/3 hospitals.

Flash Note

Distributors like Yestar play an important role to the growth of Roche IVD business in China. We estimate distributors contributed over 50% of Roche's IVD sales in China while the major four distributors: Yestar, Beijing Baron (a subsidiary under Humanwell 600079 CH), Zhejiang Dian (300244 CH) and Ningbo Medical (300439 CH) contributed over 15% of Roche IVD sales in China in 2014. Based on our discussions with Roche Diagnostic (Shanghai), we believe the abovementioned distributors are very important to Roche in growing its business because:

1. China is a big market. For Roche, to penetrate into this market, the cost of relying on distributors is much lower than building its own marketing team;
2. Most of the IVD consumables are a reagent in liquid form. There are special logistic requirements for them (for example, the products must be kept at a certain temperature). Distributors will take care of such requirements, which helps Roche to save cost;
3. As a supplier, Roche grants 2 months of credit terms to distributors. However, it normally takes over 5 months for distributors to collect money from customers (hospitals). Hence, distributors are a big help to Roche in terms of account receivables management;

On the back of IVD distribution business, we project Yestar's earnings will grow at 76% / 63% / 19% in 15F / 16F / 17F.

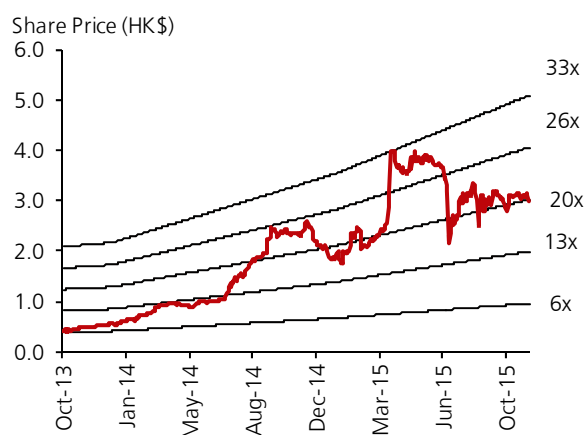
Potential M&A to accelerate earnings growth. We believe Yestar is in talks with at least one M&A target which is engaged in medical device business. Successful M&As would accelerate earnings growth.

As of Oct 2015, we estimate Yestar had total bank loans of around Rmb450m and cash of around Rmb300m which implies net debt of approximately Rmb150m. In 2Q15, Yestar announced the acquisition of a distributor of Roche IVD devices in Shanghai for a total consideration of Rmb910m, and 80% of this has been paid. Assuming Yestar raises debt to pay the balance, total net debt of Yestar could increase to Rmb330m and net debt to equity could increase to 28%.

Assuming the cap of net debt to equity ratio for Yestar is 50% and total consideration for the next M&A target is around Rmb270m, we believe Yestar's current balance will be able to fund this.

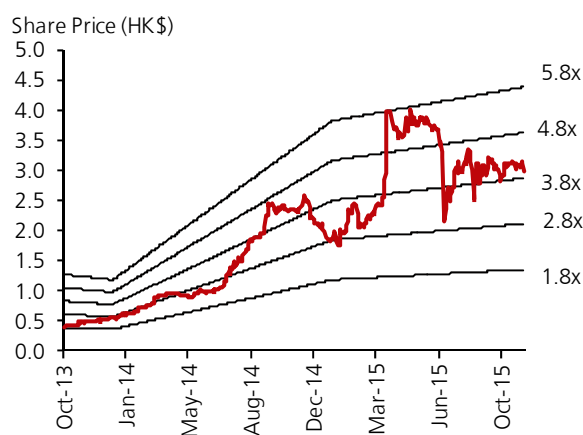
Reiterate BUY. In view of strong earnings growth ahead and potential M&A opportunity, we re-iterate BUY with TP unchanged at HK\$4.27. From 12 Oct 15 to 13 Nov 2015, Chairman of Yestar, James Hartono spent HK\$19.9m to buy 6.6m shares of Yestar (0.3% stake) at average price of HK\$3.00ps. The Chairman's move echoes with our positive view on Yestar.

PE band chart



Source: Thomson Reuters, DBS Vickers

PB band chart



Source: Thomson Reuters, DBS Vickers

Peers valuation

Company Name	Currency Code	Price Local\$	Mkt Cap US\$m	PE	PE	Yield	Yield	P/Bk	P/Bk	EV/EBITDA	ROE	ROE		
				15F x	16F x	15F %	16F %	15F x	16F x	15F x	16F x	15F %	16F %	
Medical imaging														
Yestar Int'l*	2393 HK	HKD	2.98	836	27.6	18.3	1.7	2.7	4.4	3.8	14.5	9.3	23.6	22.4
Mindray Med.Intl	MR US	USD	26.65	2,349	17.9	15.5	1.5	1.7	1.8	1.6	11.1	10.0	10.1	10.5
CR Wandong Medical 'A'	600055 CH	CNY	37.68	1,313	188.4	96.6	0.0	0.0	11.5	10.3	n.a.	n.a.	6.3	11.0
Edan Instruments 'A'	300206 CH	CNY	27.17	1,024	94.7	63.3	0.2	0.5	5.2	5.1	n.a.	n.a.	2.5	4.2
Wuhan Guide Infrared 'A'	002414 CH	CNY	29.97	2,895	156.1	111.0	0.1	0.1	7.1	6.7	n.a.	n.a.	4.9	6.7
Medical Devices														
Andon Health 'A'	002432 CH	CNY	30.85	1,848	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
GD Biolight Meditech 'A'	300246 CH	CNY	38.58	908	109.0	85.9	0.3	n.a.	12.5	11.1	n.a.	n.a.	8.9	10.5
CR Wandong Medical 'A'	600055 CH	CNY	37.68	1,313	188.4	96.6	0.0	0.0	11.5	10.3	n.a.	n.a.	6.3	11.0
Edan Instruments 'A'	300206 CH	CNY	27.17	1,024	94.7	63.3	0.2	0.5	5.2	5.1	n.a.	n.a.	2.5	4.2
Shenzhen Glory Med.'A'	002551 CH	CNY	30.92	2,169	84.7	57.5	n.a.	n.a.	9.1	7.9	n.a.	n.a.	10.1	13.3
Beijing Bohui Innovation 'A'	300318 CH	CNY	23.58	1,553	196.5	124.1	n.a.	n.a.	5.0	4.5	212.6	122.2	6.5	9.4
JS Yuyue Mdeqt.& Supp.'A'	002223 CH	CNY	43.6	4,105	64.9	49.9	0.6	0.7	11.7	9.7	52.8	41.1	18.8	20.5
Zhuhai Hokai Med.Insts. 'A'	300273 CH	CNY	23.53	2,985	58.8	41.1	0.4	0.5	10.9	8.9	50.9	34.4	20.4	23.0
TruKing Technology 'A'	300358 CH	CNY	41.82	1,870	58.6	40.0	0.3	0.4	12.6	9.6	n.a.	n.a.	21.0	21.2
Shinva Med.Instm. 'A'	600587 CH	CNY	37.25	2,438	38.6	30.2	0.3	0.4	4.6	4.1	20.2	17.0	11.4	13.0
Sinocare 'A'	300298 CH	CNY	37.9	1,593	45.9	36.1	0.8	0.6	7.2	6.1	n.a.	n.a.	16.5	18.0
Shanghai Tofflon Sctc. 'A'	300171 CH	CNY	26.59	2,718	39.9	32.7	0.9	1.1	5.4	4.7	43.9	35.7	13.9	14.8
Pw Medtech Group	1358 HK	HKD	1.76	380	10.1	8.6	0.7	0.7	1.2	1.1	n.a.	n.a.	12.0	13.4
Microport Scientific*	853 HK	HKD	3.19	586	n.a.	72.2	0.0	0.0	1.7	1.7	28.5	17.2	(2.1)	2.4
Shandong Weigao*	1066 HK	HKD	5.77	3,332	19.2	17.0	1.6	1.8	2.0	1.8	12.4	10.9	10.8	11.3
Lifetech Scientific	1302 HK	HKD	1.48	764	56.9	40.0	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	41.3	47.9
China in-vitro diagnostic industry players														
ZJ Da Diagnostics 'A'	300244 CH	CNY	83.1	3,610	126.5	89.0	0.2	0.3	23.2	18.9	n.a.	n.a.	18.0	20.5
GZ Improve Medical 'A'	300030 CH	CNY	18.82	936	71.3	58.8	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Sinocare 'A'	300298 CH	CNY	37.9	1,593	45.9	36.1	0.8	0.6	7.2	6.1	n.a.	n.a.	16.5	18.0
Beijing Bohui Innovation 'A'	300318 CH	CNY	23.58	1,553	196.5	124.1	n.a.	n.a.	5.0	4.5	212.6	122.2	6.5	9.4
Beijing Leadman Bcm.'A'	300289 CH	CNY	21.18	1,450	51.9	47.5	0.5	0.4	7.6	6.6	n.a.	n.a.	14.2	14.8
Dirui Industrial 'A'	300396 CH	CNY	52.35	1,293	68.9	52.1	0.2	0.2	7.9	6.8	n.a.	n.a.	11.7	14.3
Da An Gene Of Sun Yat 'A'	002030 CH	CNY	45.81	4,861	152.2	124.5	n.a.	n.a.	24.6	20.5	n.a.	n.a.	16.5	16.7
Shanghai Kehua Bio 'A'	002022 CH	CNY	29.75	2,455	47.2	38.3	0.8	0.9	9.5	7.9	28.9	23.1	20.0	20.4
Wuhan Humanwell 'A'	600079 CH	CNY	19.07	3,949	39.2	26.7	0.5	0.9	3.6	2.8	14.3	12.3	9.7	10.8
Shinva Medical 'A'	600587 CH	CNY	37.25	2,438	38.6	30.2	0.3	0.4	4.6	4.1	20.2	17.0	11.4	13.0
Biosino Biotech 'H'	8247 HK	HKD	3	51	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

Source: Thomson Reuters, *DBS Vickers

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Share price appreciation + dividends

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