

# China / Hong Kong Company Flash Note

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DBS Group Research . Equity

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## Yestar International (2393 HK)

BUY; HK\$2.20  
HK\$4.27 (94% upside)

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### Shanghai IVD distribution business to be largest earnings driver in 2016/17

- Expect in-vitro diagnostic (IVD) device distribution business in Shanghai to be the largest earnings driver, making up 16-38% of 15F-17F earnings
- The growth of the Shanghai IVD business itself will be mainly driven by hospitals' determination to increase medical service offerings, sales network & product portfolio expansion
- Yestar is believed to be in talks with other M&A targets. Successful M&A will accelerate EPS CAGR in 2014-17F (current estimates: 43%)
- Maintain BUY. TP at HK\$4.27

In 2Q 2015, Yestar announced its acquisitions of 70% stakes in five companies engaging in the distribution of Roche (ROG VX) IVD products (Shanghai Emphasis, Shanghai Chaolian, Shanghai Jianchu, Shanghai Haole, Shanghai Dingpei) for Rmb910m. Shanghai Emphasis holds the distribution rights of Roche IVD products in China and the other four companies are distributors for Shanghai Emphasis. There is an aggregate guaranteed profit by the vendor Mr. Li Bin in the acquisition (see the following table). Thanks to the guaranteed profit, the newly acquired Shanghai IVD companies will be a major earnings contributor for Yestar. We estimate it will account for 16%/38%/37% of Yestar's earnings in 15F / 16F / 17F.

#### Earnings growth of Yestar's IVD business in Shanghai

Profit after tax (Rmb m)		Change %
2012 actual	58	
2013 actual	84	45%
2014 actual	97	16%
2015 guaranteed*	156	60%
2016 guaranteed*	187	20%
2017 guaranteed*	225	20%

Source: company, DBS Vickers

\*The earnings are guaranteed by Mr. Li Bin. If they are not achieved, he has to compensate the difference to Yestar.

We discussed with the head of Yestar's IVD business in Shanghai (also the vendor of the above-mentioned acquisition), Mr. Li Bin, to learn more about the growth drivers of Yestar's IVD business in Shanghai.

Shanghai IVD business earnings to grow by 60% in FY15F. We believe there are two drivers for the growth:

- 1) **Increase in IVD machines installed.** The sales of IVD devices consist of two parts: IVD machines and IVD consumables. To provide IVD services, hospitals need to continuously renew IVD consumables used in the IVD machines. Thus, once the IVD machines are installed, there will be stable demand for IVD consumables. In Shanghai region, the number of the company's IVD machines installed and in service has been growing (see the following table), and creates increasing demand for IVD consumables.

#### IVD machines in service

2011	c.265
2012	c.385
2013	c.505
2014	c.600
Jun-15	c.650
Dec-15	c.700

Source: company, DBS Vickers

- 2) **Rebates offered by Roche.** The Shanghai IVD division mainly distributes Roche (ROG VX) IVD products. Once the sales exceeds the target set by Roche, it will offer a rebate. We estimate the sales target to be c.Rmb700m in 2015. Judging from the number of IVD machines installed, the actual sales could exceed Rmb900m in 2015 which could generate rebates of Rmb20m – 30m from Roche.

Flash Note

Shanghai IVD business earnings to grow by 20% in 2016F/17F, boosted by four drivers:

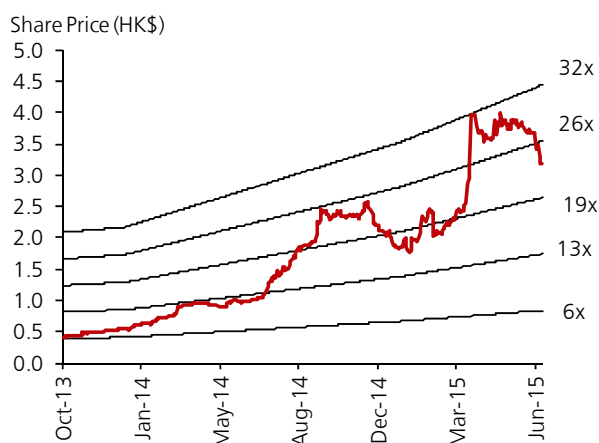
- 1) **Public hospitals' determination to increase their medical service offerings.** Drug sales make up c.46% of Shanghai's public hospitals' revenue. We estimate that it accounts for >50% of their net income as hospitals are allowed to mark up 15% over their procurement cost when selling the drugs. However, the Central government is gradually removing the mark-up. By 2017, all public hospitals will not be allowed to mark up prices when selling drugs and drug sales can only account for 30% of total public hospitals' revenue. In view of these changes, the net income of public hospitals in Shanghai will be negatively impacted. They need to look for other revenue sources to compensate, such as increasing medical service offerings. IVD devices are necessary for providing medical services. Thus, we believe the demand for IVD devices in Shanghai will increase.
- 2) **Penetration into 3<sup>rd</sup> tier hospitals.** The Shanghai division covers over 90% of top and 2<sup>nd</sup> tier hospitals in Shanghai. The division is now penetrating into 3<sup>rd</sup> tier hospitals, which provide diagnostic services to the masses. They have demand for IVD products but compared to top and 2<sup>nd</sup> tier hospitals, their financial resources are relatively limited. So, instead of selling IVD machines & consumables directly to them, the Shanghai division would co-develop testing centers with them. Those centers would procure IVD machines through a financial

leasing arrangement. As for the procurement of IVD consumables, they will be paid with the revenue from IVD services provided to the masses. This strategy can attract 3<sup>rd</sup> tier hospitals to become customers without requiring them to commit any capital. Also, as these hospitals are involved in the establishment and development of the testing centers, they would have higher confidence on the quality of the IVD service.

- 3) **Penetration into regions other than Shanghai.** The Shanghai division is already selling IVD products in Jiangsu, Jiangxi and Henan provinces. By co-operating with large hospital groups that have a nationwide hospital network, the division will further expand its presence in other regions.
- 4) **Product portfolio expansion.** The Shanghai division mainly distributes Roche IVD products, and a minority of revenue is contributed by Thermo Fisher's (TMO US) products. Those products are for diagnosis of immune system, cancer, bacteria, and bio-chemical index. The division is now expanding into other areas (e.g. measure of clotting activation) to expand revenue sources.

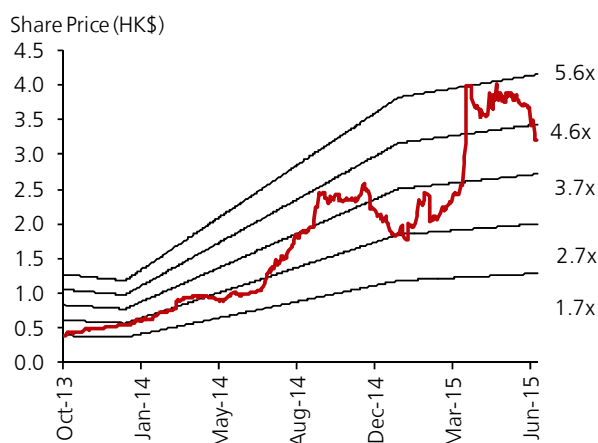
Driven by the Shanghai IVD business, Yestar's EPS CAGR in 2014-17F is expected to be 43% with potential upside should future M&A materialized. We believe Yestar is in talks with several M&A targets. After the new share issuance in Jun, Yestar's balance sheet has become much stronger (estimated net cash as of Dec-15: Rmb29m), putting it in a good position to capitalize on future M&A opportunity. Maintain BUY with TP unchanged at HK\$4.27.

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 %	
<b>Medical imaging</b>														
Yestar Int'l*	2393 HK	HKD	2.2	530	20.0	13.3	2.3	3.8	3.2	2.8	15.1	9.7	23.6	22.4
Mindray Med.Intl	MR US	USD	28.13	3,329	17.0	15.2	1.5	1.7	1.9	1.7	11.6	10.6	11.3	11.4
CR Wandong Medical 'A'	600055 CH	CNY	37.6	1,312	166.4	105.3	0.0	0.0	11.5	10.3	n.a.	n.a.	5.9	9.9
Edan Instruments 'A'	300206 CH	CNY	21.02	793	91.4	59.5	0.4	0.8	4.1	3.9	n.a.	n.a.	3.5	5.1
Wuhan Guide Infrared 'A' Su:	002414 CH	CNY	39.36	3,806	152.0	103.6	n.a.	n.a.	9.2	8.6	n.a.	n.a.	5.8	8.3
<b>Medical Devices</b>														
Andon Health 'A'	002432 CH	CNY	21.87	1,311	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	28.87	680	73.6	55.2	0.4	n.a.	9.4	8.2	n.a.	n.a.	9.8	11.8
CR Wandong Medical 'A'	600055 CH	CNY	37.6	1,312	166.4	105.3	0.0	0.0	11.5	10.3	n.a.	n.a.	5.9	9.9
Edan Instruments 'A'	300206 CH	CNY	21.02	793	91.4	59.5	0.4	0.8	4.1	3.9	n.a.	n.a.	3.5	5.1
Shenzhen Glory Med.'A'	002551 CH	CNY	28.55	1,670	64.2	44.4	n.a.	n.a.	6.7	5.7	n.a.	n.a.	11.4	14.7
Beijing Bohui Innovation 'A'	300318 CH	CNY	32	845	84.9	84.2	n.a.	n.a.	n.a.	n.a.	315.0	147.8	3.4	5.1
JS Yuyue Mdeqt.& Supp.'A'	002223 CH	CNY	67.2	6,333	101.1	79.0	0.2	0.2	18.7	15.2	82.0	64.6	18.4	19.7
Zhuhai Hokai Med.Insts. 'A'	300273 CH	CNY	24.49	2,935	51.0	35.6	0.2	0.3	11.6	9.0	45.0	30.9	23.8	26.4
Truiking Technology 'A'	300358 CH	CNY	35.35	1,331	46.6	32.3	0.4	0.5	6.6	4.5	n.a.	n.a.	20.6	21.6
Shinva Med.Instm. 'A'	600587 CH	CNY	47.42	3,106	44.9	34.9	0.2	0.3	5.7	5.0	32.4	27.3	12.9	14.6
Sinocare 'A'	300298 CH	CNY	31.61	1,329	34.1	27.1	1.0	1.2	5.9	5.2	33.0	32.2	18.2	19.0
Shanghai Tofflon Sctc. 'A'	300171 CH	CNY	20.87	2,135	31.0	25.5	1.2	1.6	4.3	3.7	48.9	40.8	14.3	15.2
Pw Medtech Group	1358 HK	HKD	2.33	503	12.4	9.8	0.8	1.1	1.3	1.2	n.a.	n.a.	11.9	13.2
Microport Scientific*	853 HK	HKD	3.34	613	n.a.	79.7	0.0	0.0	1.9	1.9	101.4	20.0	(7.5)	2.4
Shandong Weigao*	1066 HK	HKD	4.96	2,864	16.0	14.2	1.9	2.1	1.7	1.5	11.0	9.6	10.8	11.3
Lifetech Scientific	1302 HK	HKD	1.48	764	54.8	29.6	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	49.2	56.1
<b>China in-vitro diagnostic industry players</b>														
ZJ Da Diagnostics 'A'	300244 CH	CNY	82.55	3,589	120.3	84.3	0.2	0.3	21.2	16.7	n.a.	n.a.	22.5	24.7
GZ Improve Medical 'A'	300030 CH	CNY	19.94	951	73.6	62.3	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Sinocare 'A'	300298 CH	CNY	31.61	1,329	34.1	27.1	1.0	1.2	5.9	5.2	33.0	32.2	18.2	19.0
Beijing Bohui Innovation 'A'	300318 CH	CNY	32	845	84.9	84.2	n.a.	n.a.	n.a.	n.a.	315.0	147.8	3.4	5.1
Beijing Leadman Bcm.'A'	300289 CH	CNY	37.8	961	36.6	32.1	0.7	0.6	5.3	4.6	n.a.	n.a.	13.8	14.7
Dirui Industrial 'A'	300396 CH	CNY	46.61	1,152	55.5	43.6	n.a.	n.a.	7.0	6.0	n.a.	n.a.	12.7	13.9
Da An Gene Of Sun Yat 'A'	002030 CH	CNY	29.06	3,086	99.9	80.5	0.1	0.1	18.5	15.1	n.a.	n.a.	18.4	18.9
Shanghai Kehua Bio 'A'	002022 CH	CNY	28.39	2,345	38.8	32.0	1.1	1.4	8.8	7.2	54.6	46.4	23.4	23.5
Wuhan Humanwell 'A'	600079 CH	CNY	34.49	3,574	33.0	26.1	0.8	1.0	3.3	2.8	15.1	13.3	10.4	11.7
Shinva Medical 'A'	600587 CH	CNY	47.42	3,106	44.9	34.9	0.2	0.3	5.7	5.0	32.4	27.3	12.9	14.6
Biosino Biotech 'H'	8247 HK	HKD	3.66	62	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.

# FY15: FY16; FY16: FY17

Source: Thomson Reuters, \*DBS Vickers

### Flash Note

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**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)

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