Company Initiation

HAITONG 海通國際

November 2, 2014

Yestar International 2393 HK

BUY	TP: HK$ 11.00

Rating: **New** TP: **New** EPS: **New**

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Ride on momentum

Transforming into a pharmaceutical play; initiate at BUY

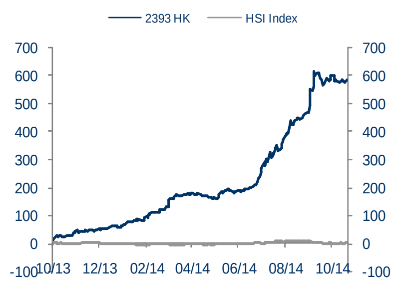
Largest partner of Fujifilm in the PRC. Listed in October 2013, Yestar is an important business partner of Fujifilm Group in the PRC, undertaking the processing, sales and marketing of Fujifilm medical imaging products, color photographic papers and industrial imaging products.

Transforming to pharmaceutical-focused business model. Results for the company demonstrated strong growth in 1H14, with revenue up 35% YoY to RMB694mn and net profit up 31% YoY to RMB37mn, buoyed by +55% revenue growth in the medical imaging segment amid high demand in the booming pharmaceutical industry. To further take advantage of the growing pharmaceutical industry, in September 2014, Yestar acquired 70% equity interest of Nanjing Uno, a medical equipment and consumables distributor in the PRC for a consideration of RMB245mn. With the acquisition, Yestar obtained the distribution rights of Roche Diagnostics Products and BD Diagnostics Products.

Solid earnings growth potential. We forecast Yestar to record FY13-16E revenue and net profit CAGR of 32% and 44% respectively, as it continues to strengthen sales its imaging product business, while we also factor in full-year contribution from the new acquisition beginning from FY15E. From FY14-16E, we expect gross margins of 16.8-19.1%, and net margin to rise from 6.3-7.3%, also benefiting from contributions from new medical device distribution business, which have approximately 30% blended gross margin. In FY15E, we forecast revenue contribution from the new medical device business to account for 17% of revenue, up from 3% in FY14E.

Initiate with BUY and TP of HK$11.00. Yestar's share price is +323% YTD, and has re-rated consistently as it transforms from a traditional imaging company to one with a pharmaceutical theme. Currently trading at a valuation of 20.9x FY15E P/E, Yestar is trading at significantly above its own historic forward P/E of 13.0x and comparable to pharmaceutical peers. We value Yestar at 24x FY15E P/E, representing ~0.6x PEG, and derive a target price of HK$11.00, implying 17% upside. The company has high ROE (>25%), and also offers a strong balance sheet, being in a net cash position, putting it in a good position for further M&A opportunities and higher dividend payout (currently 50%). We initiate coverage on the company with a BUY rating. Risks include: 1) non-synergy in new business; 3) price pressure on products; and 3) PRC government policies may affect the pharmaceutical industry.

Relative performance (%)



	12/12A	12/13A	12/14E	12/15E	12/16E
Revenue (RMB mn)	956	1,173	1,507	2,173	2,671
EBITDA (RMB mn)	86	106	146	233	285
Net profit, pre-exceptional (RMB mn)	57	65	95	157	194
EPS (RMB cents)	16.75	17.80	20.38	33.68	41.56
- % change from prev. EPS	-	-	-	-	-
- % vs. Consensus EPS	-	-	-0.6	5.2	6.6
EPS growth (%)	0.0	6.3	14.5	65.3	23.4
ROE (%)	37.9	27.5	26.7	37.5	38.2
Net debt (cash)/equity (%)	net cash	net cash	net cash	net cash	net cash
P/E (X)	42.0	39.5	34.5	20.9	16.9
P/B (X)	16.9	7.7	8.6	7.2	5.9
EV/EBITDA (X)	26.3	22.8	21.0	12.8	10.0
Dividend yield (%)	0.0	0.0	1.4	2.4	3.0

Source: Company data, HTI

Rating/Prev. Rating	**Buy/(N/A)**
TP/Prev. TP (HK$)	**11.00/(N/A)**
Price (Oct. 31, 2014, HK$)	9.38
% Upside/Downside	17%
Market Cap (USDmn)	565
Free float (%)	28.7
Daily vol - 6M avg (mn)	2.7
Daily val - 6M avg (US$mn)	2.2
Major shareholder/%	Hartono/71.1%

Financials

Income Statement

(RMB mn except otherwise indicated)	2012	2013	2014E	2015E	2016E
Revenue (net of business tax)	**956**	**1,173**	**1,507**	**2,173**	**2,671**
YoY growth	*-2.2%*	*22.8%*	*28.4%*	*44.2%*	*22.9%*
COGS	(789)	(964)	(1,253)	(1,760)	(2,161)
Gross profit	**167**	**209**	**254**	**414**	**510**
YoY growth	*2.4%*	*25.2%*	*21.2%*	*63.0%*	*23.3%*
Gross profit margin	*17.5%*	*17.8%*	*16.8%*	*19.0%*	*19.1%*
SG&A expenses	(91)	(115)	(121)	(193)	(238)
R&D expenses	-	-	-	-	-
Other operating income/loss	(1)	(2)	(2)	(3)	(4)
EBITDA	**86**	**106**	**146**	**233**	**285**
YoY growth	*19.5%*	*22.8%*	*37.9%*	*60.0%*	*22.3%*
EBITDA margin	*9.0%*	*9.0%*	*9.7%*	*10.7%*	*10.7%*
Depreciation	(10)	(13)	(15)	(16)	(17)
Amortization	-	-	-	-	-
EBIT	**76**	**92**	**131**	**217**	**268**
YoY growth	*22.5%*	*21.4%*	*42.1%*	*65.8%*	*23.5%*
EBIT margin	*7.9%*	*7.9%*	*8.7%*	*10.0%*	*10.1%*
Interest income	4	1	1	1	1
Interest expense	(3)	(6)	(6)	(6)	(6)
Profit/loss from associates	-	-	-	-	-
Profit/loss from acquisition/disposal	-	-	-	-	-
Other non-operating income/loss	5	6	6	6	6
Pretax income	**82**	**94**	**132**	**219**	**270**
YoY growth	*17.7%*	*14.8%*	*41.4%*	*65.1%*	*23.4%*
PBT margin	*8.5%*	*8.0%*	*8.8%*	*10.1%*	*10.1%*
Income tax	(24)	(28)	(37)	(61)	(76)
Effective tax rate	*28.9%*	*30.2%*	*28.0%*	*28.0%*	*28.0%*
					-
Minority interest (I/S item)	(2)	(0)	(0)	(0)	(0)
Net income, post-exceptionals	**57**	**65**	**95**	**157**	**194**
YoY growth	*19.5%*	*15.1%*	*46.2%*	*65.3%*	*23.4%*
Net margin	*5.9%*	*5.5%*	*6.3%*	*7.2%*	*7.3%*
Post-exceptional items - gain/(loss)	-	-	-	-	-
Net income, pre-exceptionals	**57**	**65**	**95**	**157**	**194**
YoY growth	*19.5%*	*15.1%*	*46.2%*	*65.3%*	*23.4%*
Net margin	*5.9%*	*5.5%*	*6.3%*	*7.2%*	*7.3%*

Balance Sheet

(RMB mn except otherwise indicated)	2012	2013	2014E	2015E	2016E
Assets					
Cash and cash equivalents	160	283	345	432	547
Pledged deposits	-	-	-	-	-
Bill and trade receivables	101	17	22	31	38
Inventories	178	273	267	262	257
Other receivables	24	29	29	29	29
Other current assets	4	3	3	3	3
Total current assets	**468**	**605**	**666**	**758**	**875**
Net PP&E (including AUC)	**96**	**104**	**114**	**123**	**130**
Net intangibles	**3**	**3**	**3**	**3**	**3**
Equity investments	-	-	-	-	-
Investments in securities or other	6	8	8	8	8
Total investments	6	8	8	8	8
LT deferred tax assets	-	-	-	-	-
LT trade and bills receivables	-	-	-	-	-
Other long term assets	15	16	19	26	30
Total assets	**587**	**736**	**810**	**917**	**1,046**
Liabilities					
Accounts payable	376	263	289	318	350
Short-term debt	25	117	117	117	117
Other current liabilities	7	-	-	-	-
Total current liabilities	**408**	**380**	**407**	**436**	**467**
Long-term debt	20	-	-	-	-
LT trade and bills payable	-	-	-	-	-
Deferred tax liabilities	-	-	-	-	-
Other LT liabilities	10	13	13	13	13
Total non-current liabilities	**30**	**13**	**13**	**13**	**13**
Total liabilities	**438**	**394**	**420**	**449**	**481**
Common shareholders' equity					
Issued capital	-	37	37	37	37
Reserves	140	296	343	422	519
Common shareholders' equity	**140**	**333**	**380**	**459**	**556**
Minority interests	9	9	9	9	9
Total liabilities and equity	**587**	**736**	**810**	**917**	**1,046**

Cash Flow Statement

(RMB mn except otherwise indicated)	2012	2013	2014E	2015E	2016E
Operating activities					
Profit before taxes	57	65	95	157	194
Depreciation and amortization	10	13	15	16	17
Net profit/loss on asset sales	-	-	-	-	-
Increase/decrease in working capital	93	(135)	27	25	30
Other operating cash flow items	-	-	-	-	-
Net CF flow from operating activities	**159**	**(56)**	**137**	**198**	**241**
Investing activities					
Capital expenditure	(53)	(22)	(24)	(25)	(24)
Acquisition/divesture	(3)	(2)	-	-	-
Proceeds from disposal of assets	-	-	-	-	-
Other investment cash flow items	0	(0)	(3)	(7)	(4)
Net CF flow from investing activities	**(55)**	**(25)**	**(27)**	**(32)**	**(29)**
Financing					
Dividends paid	-	-	(48)	(79)	(97)
Share repurchase/issue	-	-	-	-	-
Increase/decrease in debt&notes payable	(2)	72	-	-	-
Change in Minority interests	-	-	-	-	-
Other financing cash flow items	(84)	131	-	-	-
Net CF flow from financing activities	**(86)**	**203**	**(48)**	**(79)**	**(97)**
	-	-	-	-	-
Total cash flow	**18**	**123**	**62**	**87**	**115**

Ratio Analysis

	2012	2013	2014E	2015E	2016E
Valuation					
P/E (x)	42.0	39.5	34.5	20.9	16.9
P/B (X)	16.9	7.7	8.6	7.2	5.9
EV/EBITDA (X)	26.3	22.8	21.0	12.8	10.0
Dividend yield(%)	0.0	0.0	1.4	2.4	3.0
FCF yield (%)	1.9	-1.2	1.2	1.1	1.1
Profitablity					
Gross margin (%)	17.5	17.8	16.8	19.0	19.1
EBIT margin (%)	7.9	7.9	8.7	10.0	10.1
Net margin (%)	5.9	5.5	6.3	7.2	7.3
SG&A/revenue (%)	9.5	9.8	8.0	8.9	8.9
ROE (%)	37.9	27.5	26.7	37.5	38.2
ROA (%)	10.6	9.8	12.3	18.2	19.8
Liquidity & Leverage					
Current Ratio (X)	1.1	1.6	1.6	1.7	1.9
Quick Ratio (X)	0.7	0.9	1.0	1.1	1.3
Net debt/equity (%)	-82.3	-49.8	-59.8	-68.5	-77.3
Total debt/equity (%)	32.1	35.2	30.8	25.5	21.1
Total liabilities/total assets (%)	74.6	53.5	51.9	49.0	46.0
EBIT interest coverage ration (x)	26.4	16.0	22.7	37.7	46.5
Efficiency					
Inventory days	71.9	85.3	78.7	54.9	43.8
A/R days	26.3	18.3	4.7	4.4	4.8
A/P days	143.2	121.1	80.5	63.0	56.5

Company background

Listed on the Hong Kong Stock Exchange in October 2013, Yestar International (Yestar) is one of the leading providers of color photographic paper and a provider of a broad range of imaging products with strong sales platform across the PRC. It processes color photographic paper, various image printing films and medical imaging films into ready-to-use form by cutting and slitting master rolls into customized sizes and packaging the products under precisely controlled processing conditions.

Yestar is an important business partner of Fujifilm Group in the PRC. As the largest authorized distributor and processor of the aforesaid products in the PRC since June 2009, Yestar undertake the processing, sales and marketing of Fujifilm medical imaging products, color photographic papers and industrial imaging products. Other photo related and document printing products of Fujifilm Group are also under Yestar's distribution.

In September 2014, Yestar acquired 70% equity interest of Nanjing Uno, a medical equipment and consumables distributor in the PRC for a consideration of RMB245mn. With the acquisition, Yestar obtained the distribution rights of Roche Diagnostics Products and BD Diagnostics Products.

Business model

The Company converts master rolls of color photographic paper, image printing film and medical film which are directly purchased from Fujifilm Group into sheets customized ready-to-use sizes and package under the Fujifilm and Yestar brand for sale in the PRC.

With an extensive sales and marketing network in the PRC, Yestar's end markets include a variety of retailers, healthcare clinics and industrial manufacturers. Sales to end users allow the company to obtain feedback on product quality, whereas the wholesalers sales channels can help expand the Company's geographic coverage and accelerate sales growth at lower costs by leveraging on the wholesalers' local market knowledge and sales network.

In terms of products, Yestar diversified its portfolio and tapped into the medical imaging industry by processing and selling Fujifilm medical dry film and medical wet film to Fujifilm Group in the PRC. Leveraging on its capability to process and sell imaging products, the Company further diversified into the processing of dental film and industrial NDT x-ray film and sold them under its own Yes!Star brand. As of 1H14, the company's portfolio are mainly categorized into three segments, namely (1) medical image printing products and (2) color photographic papers and (3) industrial imaging products.

Going forward, after the Nanjing Uno acquisition, Yestar will continue to venture into the medical device industry by means of mergers and acquisitions and further develop its medical consumable business, as well as actively explore more business opportunities with Fujifilm.

Products by segment

Image printing products segment

Category	Description	Brands
Color photographic paper	• Sales and processing of Fujifilm minilab color photographic paper (smaller than 12 inches in size) and professional color photographic paper (normally no less than 12 inches in size)	Fujifilm
Industrial imaging products	• Sales of Fujifilm industrial NDT x-ray film	Fujifilm
	• Sales and processing of Yes!Star industrial NDT x-ray film	Yes!Star
	• Sales and processing of Fujifilm PWB film	Fujifilm
Other image printing products	• Sales and/or processing of other photo-related products of Fujifilm Group (including sale and processing of color film, sales of photofinishing equipment and consumables, mini instant cameras and other photo-related products)	Fujifilm
	• Sales of Fujifilm Group's document printing equipment and consumables	Fuji Xerox, Acuity

Medical imaging products segment

Category	Description	Brands
Medical imaging products	• Sales and processing of Fujifilm medical dry film	Fujifilm
	• Sales and processing of Fujifilm medical wet film	Fujifilm
	• Sales and processing of Yes!Star dental film	Yes!Star

Source: Company data, HTI

What Yestar gains in the medical industry from the Nanjing Uno acquisition

Roche	BD (Becton Dickinson)
A leader in research-focused health care: • Founded in 1896 in Basel, Switzerland. • Combined strengths in pharmaceuticals and diagnostics.	**A leading global medical technology company:** • Founded in 1897 and headquartered in the US. • Manufactures and sells a broad range of medical supplies, devices, laboratory equipment and diagnostic products.
The global market leader in vitro diagnostics & tissue-based cancer diagnostics etc, with a broad range of innovative diagnostic tests and systems: • Integrated heathcare solutions. • Early detection. • Targeted screening, evaluation. • Monitoring of disease.	**BD Diagnostics:** • A leading provider of products for the safe collection and transport of diagnostic specimens. • Instruments and reagent systems to accurately detect a broad range of infectious diseases, heathcare associated infections and cancers.
Roche Diagnostics in the PRC: • Largest IVD products provider in the world. • No.1 market share in the PRC.	**BD in the PRC:** • BD Medical. • BD Biosciences. • BD Diagnostics.

Source: Company data, HTI

Future growth strategies

We list below some of the growth strategies of the company going forward.

Venture into the medical device business and further develop the medical consumable business

- By means of mergers and acquisitions to venture into the medical device industry.
- Actively explore more business opportunities with Fujifilm with an aim to co-develop the medical industry in the PRC.
- Employ technological know-how to launch Fujifilm branded dental film in the 2H14.
- Aim to become a key player in the PRC's expanding medical industry.

Target to launch new medical consumer products under the Yes!Star brand in 2H14

- Introduce another medical thermal-dry film product line under its house brand Yes!Star to satisfy the mass market.
- Together with the new consumable line, launch Yes!Star branded medical dry-films and medical dry film printers.

Launch a professional color photographic paper product under the Yes!Star brand

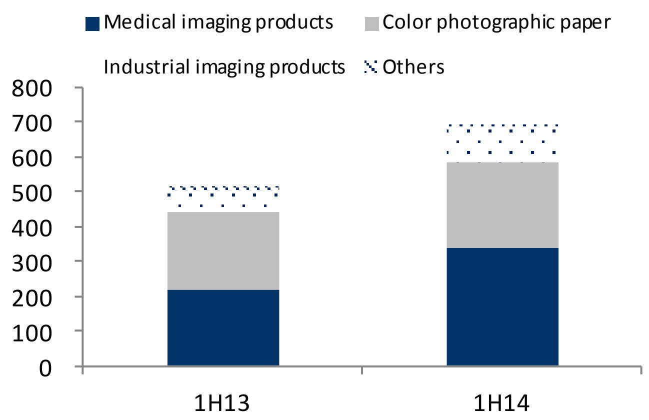
- Successfully launch in June 2014, expect to make substantial contribution in 2H14.
- Targeting the mass market and act as a complement to the Group's mid to high-end focused Fujifilm products.

Financials: We forecast 32% and 44% revenue and net profit CAGR from FY13-16E

Robust top-line growth in 1H14: In 1H14, Yestar reported a solid 34.7% growth in revenue to RMB694mn versus RMB515mn in 1H13. Through increase in helath consciousness and increase in market share, medical imaging products (48.6% of revenue) and industrial imaging products (14.4% of revenue) segments both saw strong YoY growth of 55.2% and 55.5% respectively, while color photographic paper segment (35.6% of revenue) saw 10.7% YoY growth.

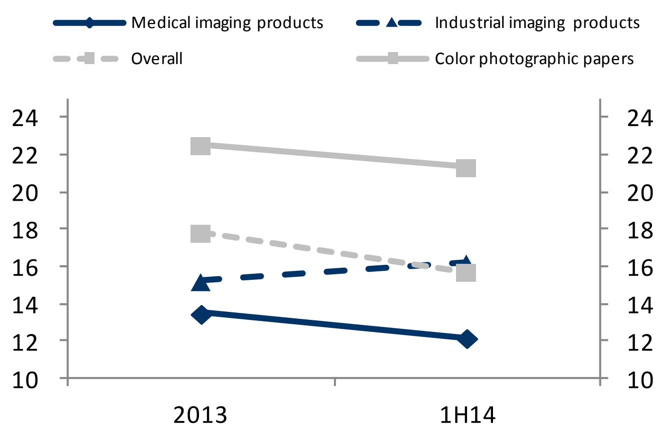
Slight decrease in gross margins in 1H14 due to higher contributions of medical film: Gross margin in 1H14 fell to 15.7% from 17.3% in 1H13 as a result of increased contribution of medical imaging products, which has a relatively lower gross margin (1H14: 12.2%), compared to color photographic paper (1H14: 21.3%) and industrial imaging film (1H14: 16.2%)

Revenue by products categories (RMB mn)



Source : Company Data, HTI

Gross profit margin (%) by products categories



Source : Company Data, HTI

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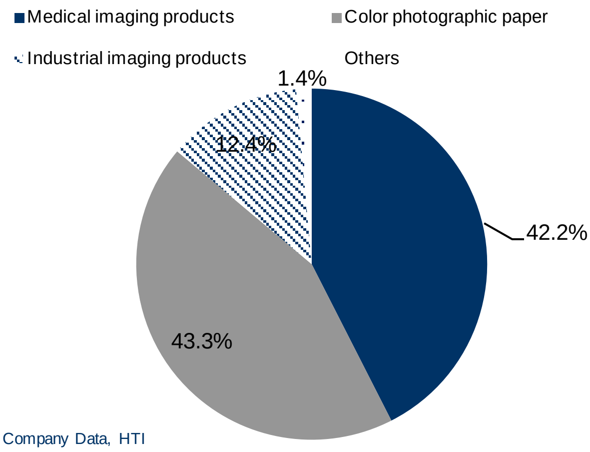
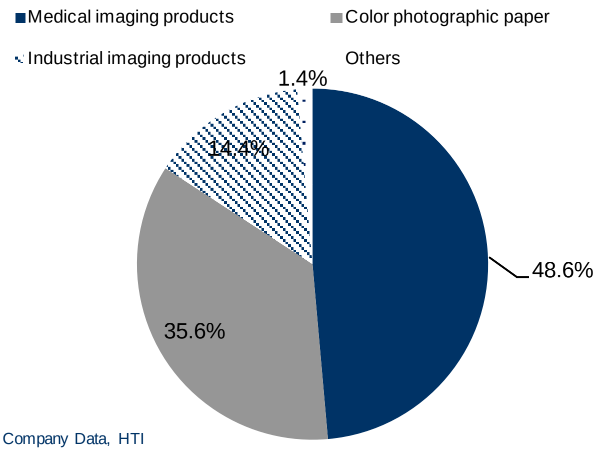
Revenue breakdown by products categories, 1H13



Source : Company Data, HTI

Revenue breakdown by products categories, 1H14



Source : Company Data, HTI

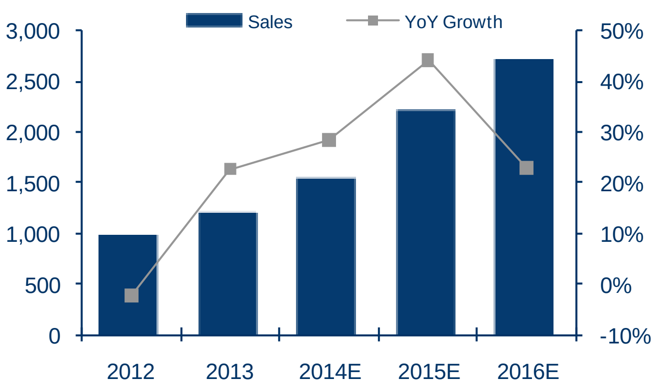
Solid net profit growth in 1H14: Net profit in 1H14 rose strongly by 31% to RMB37mn, with net margin remaining stable at 5.4% (1H13: 5.5%). While the company did not declare an interim dividend, similar to 1H13, management guided that full-year payout is expected to be no less than 35%, and likely comparable to the 50% level for FY13. Capex for the next two years is expected to be RMB20mn/year, and with RMB208mn as of end-1H14, the company may look to make one more acquisition before the end of 2014.

Results review (RMB mn)	1H14	1H13	YoY
Sales	694	515	34.7%
Gross profit	109	89	22.5%
Gross margin	15.7%	17.3%	
Operating profit	54	41	33.3%
Operating margin	7.8%	7.9%	
Net profit	37	29	30.7%
Net margin	5.4%	5.5%	

Source: Company data, HTI

Future revenue growth to come from expanding product line and contributions from medical device segment: For 2H14 through 2016, we expect the company to continue to record strong revenue and net profit growth as it continues to expand through further optimizing product mix driven by expanding product lines in its film products, especially on the medical film segment where there continues to be high demand and growth potential, as well as significant contributions from its medical device business, which will begin to have full-year contributions from FY15 onwards.

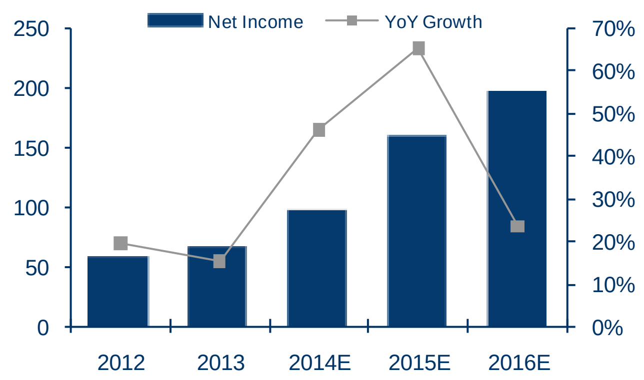
Sales (RMB mn) and YoY growth (2012-2016E)



Source : Company Data, HTI

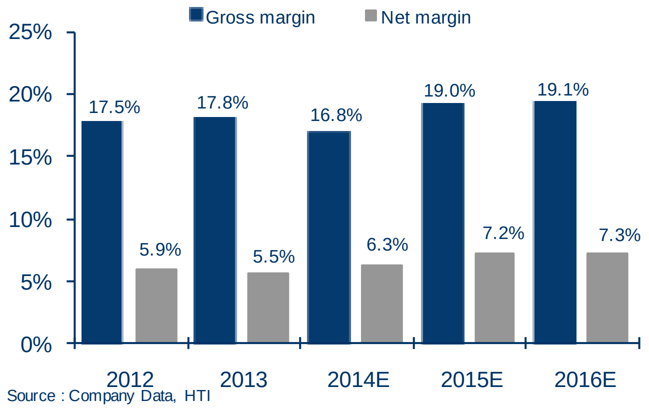
We forecast strong revenue and net profit growth for FY13-16E: With the assumption of revenue CAGR of 24% and 20% for the film/imaging and medical device segments respectively, overall, we forecast FY13-16E revenue and net profit CAGR of 31.6% and 43.9%. Overall revenue CAGR is higher than the segmental breakdown due to the fact that the medical device segment (from the acquisition of Nanjing Uno) will only begin to have full-year contribution in FY15E onwards, hence pulling up the total revenue growth figure. From FY14E, we expect gross margins to come in at 16.8%, before rising to 19.0%/19.1% in FY15E and FY16E as a result of contributions from the medical device segment, which we expect to have gross margins of 30%. For FY14E, we anticipate net margin to be at 6.3%, and rising to to 7.2% and 7.3% in FY15E and FY16E respectively.

Net income (Rmb mn) and YoY growth (2012-2016E)



Source : Company Data , HTI

Gross and net margins (2012-2016E)



Source : Company Data, HTI

Valuations: Benefiting from strong growth profile and positive investor sentiment in the pharmaceutical sector. Initiate with BUY rating with TP of HK$11.00.

Yestar's share price has shown extremely strong performance, and is +323% YTD and +580% since listing, and has re-rated consistently as it transforms from a traditional imaging company to one with a pharmaceutical theme.

In our view, Yestar's most direct comparables listed in Hong Kong would be pharmaceutical equipment/medical device retail and distribution players such as China Pioneer Pharma (1345 HK, BUY), PW Medtech (1358 HK, BUY), Shandong Weigao (1066 HK), China Medical System (0867 HK), and Microport (0853 HK). Collectively, this peer group is trading at 21.1x FY15E P/E respectively.

Currently trading at a valuation of 20.9x FY15E P/E, Yestar is trading at significantly above its own historic forward P/E of 13.0x and comparable to pharmaceutical peers. While we would not say Yestar's valuations are undemanding, we do expect the company to benefit from the sector re-rating trend which is set to continue with positive investor sentiment in the pharmaceutical sector supported by strong sector earnings growth.

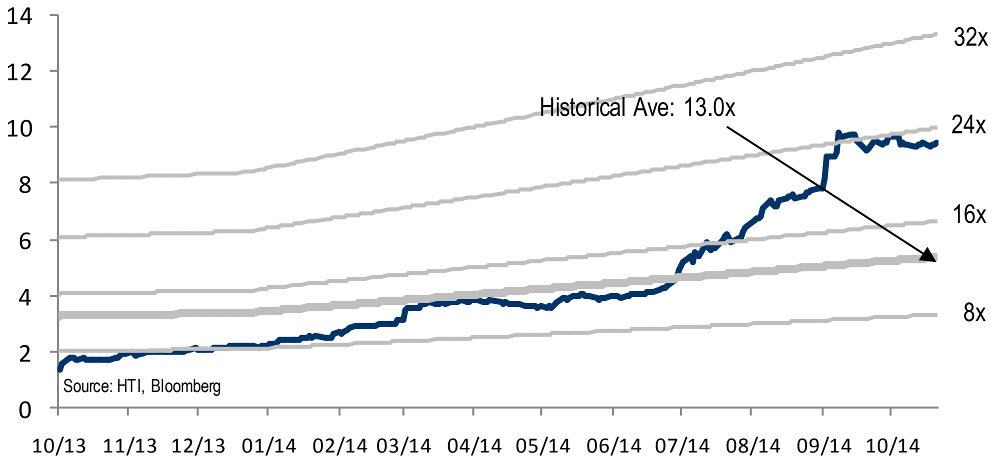
We value Yestar at 24x FY15E P/E, representing ~0.6x PEG, and derive a target price of HK$11.00, implying 17% upside. The company has high ROE (>25%), and also offers a strong balance sheet, being in a net cash position, putting it in a good position for further M&A opportunities and higher dividend payout (currently 50%). We initiate coverage on Yestar with a BUY rating.

Comps table

Company	Stock Code	Market Cap (US$bn)	Price (LC) (Oct 31, 2014)	Target price (HK$)	Rating	PER (x) 14E	PER (x) 15E	PER (x) 16E	PBR (x) 14E	PBR (x) 15E	PBR (x) 16E	Dividend yield (%) 14E	Dividend yield (%) 15E	Dividend yield (%) 16E	ROE (%) 14E	ROE (%) 15E	ROE (%) 16E
YESTAR INTL	2393 HK	0.6	9.38	11.00	BUY	34.5	20.9	16.9	8.6	7.2	5.9	1.4	2.4	3.0	26.7	37.5	38.2
HK listed peers																	
CHINA PIONEER PHARMA	1345 HK	1.3	6.76	8.20	BUY	25.0	18.7	14.4	6.3	5.7	5.1	2.8	3.7	4.9	26.1	31.9	37.3
PW MEDTECH	1358 HK	1.1	4.49	5.60	BUY	34.3	20.3	16.6	3.4	3.0	2.6	0.0	1.0	1.2	10.4	15.7	16.9
CHINA MEDICAL SYSTEMS	0867 HK	4.5	14.30	N/A	N/A	37.3	25.6	20.3	7.4	6.1	5.1	1.1	1.4	1.7	22.3	24.5	25.1
SHANDONG WEIGAO	1066 HK	4.5	7.82	N/A	N/A	27.0	22.4	20.0	2.8	2.6	2.3	1.0	1.2	1.3	11.1	12.1	12.8
MICROPORT	0853 HK	0.7	3.92	N/A	N/A	34.7	18.3	15.8	1.8	1.7	1.5	1.6	2.0	1.2	4.6	10.0	11.5
CHINA HK PHOTO P	1123 HK	0.1	0.52	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A	N/A
Global peers																	
SHINVA MEDICAL INSTRUMENT	600587 CH	2.4	36.98	N/A	N/A	43.8	31.6	24.2	4.2	4.5	3.7	0.3	0.3	0.4	12.7	15.4	16.7
LUCKY FILM CO - A	600135 CH	0.7	13.03	N/A	N/A	100.2	72.4	33.4	N/A	N/A	N/A	N/A	N/A	N/A	3.9	5.2	9.0
FUJIFILM HOLDING	4901 JP	17.0	3687.00	N/A	N/A	22.4	20.0	18.4	0.9	0.8	0.8	1.3	1.4	1.5	4.1	4.2	4.5
KONICA MINOLTA	4902 JP	5.6	1214.00	N/A	N/A	31.2	19.0	14.7	1.3	1.2	1.2	1.4	1.6	1.9	4.2	6.7	8.5
AGFA - GEVAET NV	000919 CH	1.3	15.73	N/A	N/A	38.8	32.1	26.3	3.4	3.2	3.0	1.3	1.6	1.9	9.1	10.4	11.5

Source: HTI, Bloomberg

Yestar International Price (HKD, LHS) vs Forward PE (x)



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	Rating	Remark
Stock (9 - 12 months)	Buy	Target price +15% or more above the current price
	Hold	Target price within 0% to +15% of the current price
	Sell	Target price below the current price
Sector	Overweight	Relative performance over Hang Seng Index ≥10%
	Neutral	Relative performance within Hang Seng Index -10% to +10%
	Underweight	Relative performance below Hang Seng Index ≤-10%

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