

Q & M Dental Group

Back to core business post spin-offs

SINGAPORE | HEALTHCARE | RESULTS

- FY2016 Revenue missed our FY2016 estimate by 7% due to lower-than-expected 4Q16 clinic turnover
- FY2016 Core PATMI missed our FY2016 estimates by 27% due to higher-than-expected margin compression
- Proposed final dividend of 0.7 cents; FY2016 dividend of 1.12 cents (31% payout ratio)
- More aggressive in expanding its clinics network to support growth post spin-offs
- On track to spin-off listing of Aoxin on the SGX-Catalist Board by 2Q FY2017

S\$' mn	FY16	FY15	y-y (%)	Comments
Dental and Medical Clinics	118.7	97.8	21.4%	Higher revenue from organic and inorganic growth in both SG and CN
Dental Equipment & Supplies Distribution	13.7	9.6	43.5%	Acquisition of Shenyang Maotai Quanmin Medical Equipment Leasing Co., Ltd in CN (Jan-16)
Dental Supplies Manufacturing	22.5	16.7	35.0%	Increased sales from new factory with higher production capacity
Revenue	154.9	124.0	25.0%	
Gross	126.2	103.6	21.8%	Margin compression due to higher costs of sales Pro-rate gross margin fell 2.1pps to 78.9%
EBITDA	43.0	23.2	85.4%	Exclude impairment and spin-off related costs and gain, FY16 EBITDA would have +15.9% yoy
EBIT	38.6	19.2	100.8%	
PATMI	28.3	11.4	148.2%	
DPS (S\$ cents)	1.12	0.84	32.9%	Payout ratio: 31% (FY16) vs 57% (FY15)

Source: Company, PSR est.

Listing gain to lift FY17F EPS but recurring profit from Aoxin and Aidite to shrunk c.26% post spin-offs. After spin-off listings, its China subsidiaries will be reclassified as Q&M's associates. Instead of receiving 60% of Aoxin's profit and 51% of Aidite's, Q&M will now recognise c.44% of Aoxin's profit and subsequently c.38% of Aidite's profit.

Clinic business is the sole growth engine post spin-offs. Management noted that it will step up its expansion plan for Clinic business, given the headwinds in its Distribution business in Malaysia. Distribution business in Malaysia was hit by lower demand and weakening MYR, which lifted its costs of sales. The Group recorded c.S\$2mn impairment of Goodwill in view of the slowdown in its Distribution business in Malaysia.

Focus on organic growth in its Clinic business. Investment thesis of low dentist-to-population ratio in Singapore remains intact. Key under-served areas identified are West and North areas of Singapore. It targets to open three new clinics in Singapore by 1H FY2017. However, patient demand under CHAS and Pioneer Generation subsidies could be dampened by government's tighter claim limits this year. Q&M had been a beneficiary of this government initiative.

Q&M is in a net debt position of S\$40.4mn, and 18.4% of its total debt (amounting to S\$15.5mn) will be expiring in FY2017. While the Group has S\$44.1mn cash as at 31 December 2016, it intends to refinance these loans to fund its accelerated expansion.

Downgrade to 'Reduce' rating with lower TP of \$0.65 (previously S\$0.89) based on unchanged 38.2x FY17F PER. We adjusted our forecast FY17 EPS lower by c.28% to 1.69 Singapore cents after accounting for (i) lower FY17F revenue growth expectation, and (ii) c.26% loss of profit from Aoxin and Aidite. Our FY17F EPS excludes gain on spin-off of Aoxin and spin-off listing cots. **Potential re-rating catalysts** would be (i) the Group stepping up its pace of acquisitions or picking up favourable deals; and (ii) to revive its businesses in Malaysia.

6 March 2017

Reduce (Downgrade)

LAST CLOSE PRICE	SGD 0.705
FORECAST DIV	SGD 0.010
TARGET PRICE	SGD 0.650
TOTAL RETURN	-6.4%

COMPANY DATA

O/S SHARES (MN) :	797
MARKET CAP (USD mn / SGD mn) :	398 / 562
52 - WK HI/LO (SGD) :	0.81 / 0.66
3M Average Daily T/O (mn) :	121

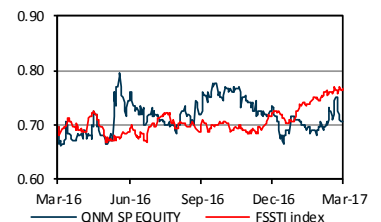
MAJOR SHAREHOLDERS (%)

Quan M in Holdings Pte Ltd	48.06%
Heritas Helios Investmetns Pte Ltd	8.04%
Koh ShunJie, Kelvin	4.63%
Dr Ng Chin Siau	14.2%

PRICE PERFORMANCE (%)

	1M TH	3M TH	1Y R
COMPANY	14	(2.8)	4.2
STI RETURN	2.70	7.48	16.45

PRICE VS. STI



Source: Bloomberg, PSR

KEY FINANCIALS

Y/E Dec	FY 15	FY 16 F	FY 17 F	FY 18 F
Revenue (SGD mn)	124	155	124	137
EBITDA (SGD mn)	23	43	17	17
NPAT, adj. (SGD mn)	11	28	14	14
EPS (S Cents)	15	3.6	17	17
PER, adj. (x)	47.2	19.7	41.7	40.9
P/BV, (x)	5.8	4.9	4.7	4.6
DPS (S Cents)	0.8	1.1	1.0	1.0
Div Yield (%)	1%	2%	1%	1%
ROE (%)	13.5%	27.4%	11.6%	11.5%

Source: Company Data, PSR est.

Valuation Method

P/E Multiple @ 38.2x

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Spin-offs and listing of Aidite and Aoxin

(i) Received approval for the quotation of the shares of Qinghuangdao Aidite High Technical Ceramic Co., Ltd. (“Aidite”) on the National Equities Exchange and Quotations System (NEEQ, a.k.a. the New Third Board) in China on 1 December 2016. Q&M’s effective interest in Aidite has decreased to 38.17% post spin-off and restructuring.

Valuation of Aidite doubled. The 51% stake in Aidite was acquired at an implied PER of 10x. The 12.83% stake was spun-off with \$521.327mn gain, implying 21.1x PER based on Aidite’s \$7.882mn FY2016 profit.

(ii) Proposed spin-off listing of Aoxin Q&M Dental Group Pte. Ltd. (Aoxin) on SGX-Catalist Board is expected to be completed in 2Q FY2017. Q&M is expected to hold a controlling interest of 43.92% in Aoxin after spin-off.

The 60% stakes of Aoxin was acquired with an implied PER of 11x, and we expect the higher valuation of Aoxin post spin-off listing. The recent listing of healthcare service providers on SGX-Catalist Board are Singapore O&G Ltd. and HC Surgical Specialists Ltd. They were listed at a valuation of 12.8x and 12.5x PER, respectively.

The successful spin-offs of Aidite and soon, Aoxin, will be a testament of the Group’s strategy of identifying, acquiring and realising value from business with great potential. Management shared their intention to replicate such model, which would add new growth driver to the Group before spinning it off and unlocking value to Q&M’s shareholders.

Unlikely to see higher dividend payout ratio or special dividend in FY17F.

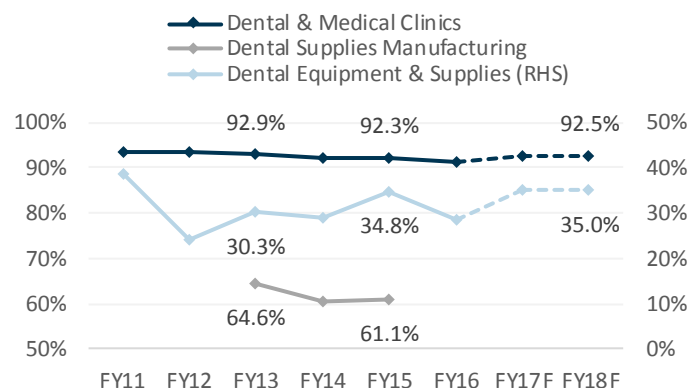
FY2016 payout ratio was 31% as compared to FY2015’s 57%. We expect the Group to reinvest most of the gains from spin-off listing into its robust expansion projects. We maintained our assumption that the Group will payout 60% of its FY17F earnings (exclude gains from spin-off).

Margins to return to pre-FY2014 level, i.e. before acquisition of Aidite and Aoxin.

FY2016 Distribution gross profit margin was compressed by higher cost of sales for Shenyang Maotai. Distribution margin shed 6.1 percentage points (“pps”) to 28.7% in FY2016 compared to a year ago. We think it could stabilise at c.35% after the spin-off listing of Aoxin.

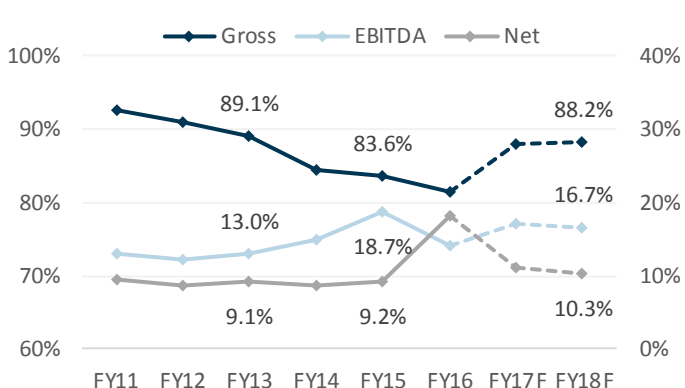
Figure 2 & 3:

Segment Gross Margin



Source: Company, PSR est.

Margins



Source: Company, PSR est.

FY2015: Full year contribution from Aidite and Aoxin (both acquired in mid-FY2014)

FY17F onwards: Higher gross profit margin without adverse impact from China’s cost pressure and better procurement process, as well as improved economies of scale

Valuations

Q&M Dental Group is currently trading at 20.1x trailing PER, which is below the peers' average PER at 37.3x. It also has higher than peers' average return on equity (ROE). These are distorted by the S\$21.2mn gain from spin-off of Aidite, the S\$1.1mn spin-off related costs and the S\$4.1mn impairment of Goodwill.

Excluding all non-recurring items, FY16F EPS would have been 1.53 cents, implying TTM PE multiple of 46.2x. A high c.24% premium to peers' 37.3x PER.

Q&M has been trading on a high PER (5-year average PER at 41.8x) as it had been gaining ground in China dental market via acquisitions. However, we think that such high premium to its peers are now unjustifiable after Q&M spin-off listing its China businesses and no longer have significant control over them.

As such we maintained PER multiple at 38.2x FY17F PER, which is in line with peers' average FY17F PER of 38.4x.

Figure 4: Peers Comparison

Company	Mkt Cap (SGD mn)	P/E TTM	P/E FY1	P/E FY2	Net D/E (%)	ROA (%)	ROE (%)	P/B
Q & M Dental Group	562	20.1	19.7	30.1	13.5	5.7	14.0	5.8
Singapore								
Raffles Medical Group Ltd	2,475	35.1	32.9	28.9	Net Cash	8.2	11.1	3.7
Talkmed Group Ltd	979	26.2	24.8	21.6	Net Cash	51.6	62.4	15.4
IHH Healthcare Bhd	15,558	N/A	45.1	36.1	21.1	1.7	2.8	N/A
Healthway Medical Corp Ltd	103	N/A	N/A	N/A	8.2	-0.1	-0.1	0.5
Cordlife Group Ltd	280	N/A	N/A	N/A	Net Cash	-2.8	-5.3	2.3
ISEC Healthcare Ltd	147	21.9	N/A	N/A	Net Cash	9.7	10.4	2.5
AsiaMedic Ltd	29	N/A	N/A	N/A	Net Cash	-9.7	-15.7	1.7
Singapore O&G Ltd	294	33.1	27.4	22.5	Net Cash	21.5	26.8	7.1
Average		29.1	32.6	27.3	14.7	10.0	11.5	4.7
China								
Aier Eye Hospital Group Co	6,207	55.3	51.6	38.9	Net Cash	15.5	21.6	11.3
Topchoice Medical Invs Corp	1,893	47.3	47.4	37.3	Net Cash	16.8	22.8	9.8
Average		51.3	49.5	38.1	N/A	16.1	22.2	10.5
India								
Apollo Hospitals Enterprise Ltd	3,670	52.4	60.4	42.0	62.1	4.7	10.0	5.0
Hong Kong								
Phoenix Healthcare Group Co. Ltd	2,376	37.3	33.0	26.8	Net Cash	9.0	10.9	3.9
Thailand								
Bumrungrad Hospital Public Co Ltd	5,128	35.0	33.9	30.9	Net Cash	17.0	26.7	8.8
Malaysia								
KPJ Healthcare Bhd	1,335	29.3	28.0	24.0	72.2	3.8	9.7	2.6
US								
Concord Medical Services Holdings Ltd.	306	N/A	N/A	N/A	68.1	-5.9	-12.0	1.1
Simple Average (Excl. QNM)		37.3	38.4	30.9	46.3	9.4	12.1	5.4

Source: Bloomberg, Phillip Securities Research (Singapore) Estimates

Financials

Income Statement

Y/E Dec, SGD mn	FY14	FY15	FY16	FY17F	FY18F
Revenue	100.3	124.0	154.9	124.0	137.2
EBITDA	15.1	23.2	43.0	16.5	17.2
Depreciation & Amortisation	(2.8)	(4.0)	(4.5)	(3.3)	(3.7)
EBIT	12.2	19.2	38.6	13.2	13.5
Share of profit from assoc. & JVs	0.0	0.0	0.0	4.8	5.5
Net Finance Inc/(Exp)	(0.5)	(2.4)	(3.0)	(3.2)	(3.7)
Profit before tax	11.8	16.8	35.5	14.7	15.2
Taxation	(1.3)	(2.0)	(2.2)	(1.0)	(1.1)
Net profit, reported	10.5	14.8	33.3	13.7	14.2
Non-controlling interest	(1.9)	(3.4)	(5.0)	(0.0)	(0.0)
PATMI, reported	8.6	11.4	28.3	13.6	14.1
Non-recurring items	0.0	1.8	16.1	0.0	0.0

Per share data (SGD Cents)

Y/E Dec	FY14	FY15	FY16	FY17F	FY18F
EPS, reported	1.20	1.46	3.55	1.69	1.73
DPS	0.73	0.84	1.12	1.01	1.04
BVPS	10.72	11.81	14.40	14.88	15.36

Cash Flow

Y/E Dec, SGD mn	FY14	FY15	FY16	FY17F	FY18F
CFO					
Profit before tax	11.8	16.8	35.5	14.7	15.2
Adjustments	3.7	4.2	(9.5)	1.8	2.0
WC changes	(4.3)	(5.2)	(6.1)	(2.6)	(1.6)
Cash generated from ops	11.2	15.9	19.9	14.0	15.6
Others	(0.6)	(2.6)	(2.8)	(1.0)	(1.1)
Cashflow from ops	10.6	13.3	17.1	12.9	14.5
CFI					
CAPEX, net	(17.3)	1.5	(5.9)	(11.6)	(11.4)
Others	(21.6)	(21.0)	(14.5)	0.3	0.2
Cashflow from investments	(38.8)	(19.6)	(20.4)	(11.4)	(11.2)
CFF					
Share issuance, net	12.9	(0.8)	(5.4)	0.0	0.0
Loans, net of repayments	29.2	(12.5)	(0.3)	0.0	0.0
Dividends	(6.5)	(5.8)	(6.7)	(8.2)	(8.5)
Others	(0.4)	54.5	(5.1)	(3.5)	(3.9)
Cashflow from financing	35.1	35.5	(17.5)	(11.7)	(12.4)
Net change in cash	6.9	29.2	(20.8)	(10.1)	(9.1)
CCE, end	35.6	64.9	44.1	34.0	24.9

Source: Company, Phillip Securities Research (Singapore) Estimates

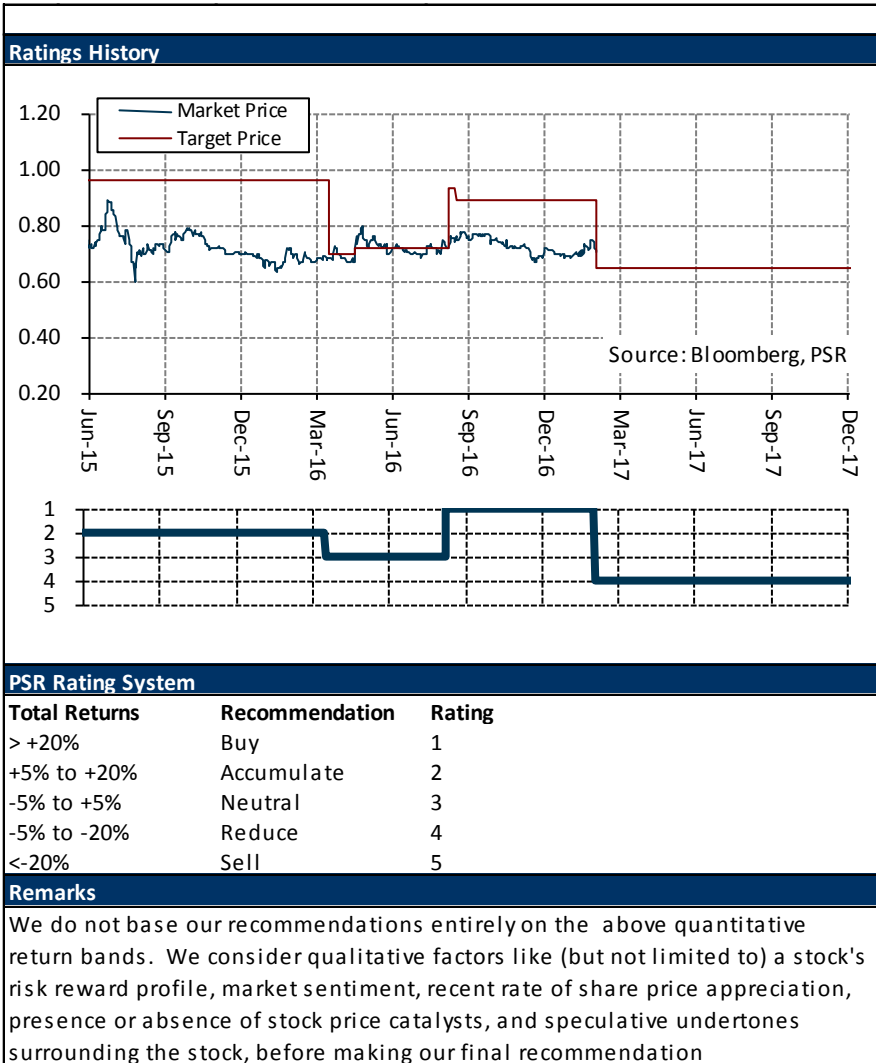
*Forward multiples & yields based on current market price; historical multiples & yields based on historical market price.

Balance Sheet

Y/E Dec, SGD mn	FY14	FY15	FY16	FY17F	FY18F
ASSETS					
PPE	37.4	34.3	27.4	35.7	43.3
Associates & JVs	0.0	0.0	39.8	44.6	50.1
Intangibles	35.3	76.9	75.2	75.2	75.2
Others	1.1	1.1	6.7	6.7	6.7
Total non-current assets	73.8	112.3	149.1	162.1	175.2
Accounts receivables	16.3	22.8	23.8	21.2	23.4
Cash	35.7	64.9	44.1	34.0	24.9
Inventories	8.6	11.2	7.6	4.6	5.0
Others	6.2	4.7	4.6	4.6	4.6
Total current assets	66.9	103.6	80.1	64.3	57.9
Total Assets	140.7	215.9	229.1	226.5	233.1
LIABILITIES					
Accounts payables	21.0	25.7	21.0	12.8	13.8
Short term loans	3.8	15.7	15.5	15.5	15.5
Others	1.0	0.6	0.0	0.0	0.0
Total current liabilities	25.8	42.0	36.5	28.3	29.3
Long term loans	28.5	63.8	68.9	68.9	68.9
Others	1.3	1.8	1.7	1.7	1.7
Total non-current liabilities	29.8	65.6	70.6	70.6	70.6
Total Liabilities	55.6	107.7	107.1	98.9	99.9
EQUITY					
Non-controlling interests	8.4	16.1	7.4	7.4	7.4
Shareholder Equity	76.6	92.1	114.7	120.1	125.8

Valuation Ratios

Y/E Dec	FY14	FY15	FY16	FY17F	FY18F
P/E (X), adj.	39.9	47.2	19.7	41.7	40.9
P/B (X)	4.5	5.8	4.9	4.7	4.6
EV/EBITDA (X), adj.	22.7	23.2	12.9	34.5	33.5
Dividend Yield (%)	1.5%	1.2%	1.6%	1.4%	1.5%
Growth & Margins (%)					
Growth					
Revenue	40.9%	23.6%	25.0%	-20.0%	10.7%
EBITDA	65.8%	54.1%	85.4%	-61.6%	4.2%
EBIT	72.3%	56.9%	100.8%	-65.8%	2.5%
Net profit, adj.	32.6%	33.1%	148.2%	-51.8%	3.5%
Margins					
EBITDA margin	15.0%	18.7%	27.8%	13.3%	12.5%
EBIT margin	12.2%	15.5%	24.9%	10.6%	9.8%
Net profit margin	8.5%	9.2%	18.3%	11.0%	10.3%
Key Ratios					
ROE (%)	14.0%	13.5%	27.4%	11.6%	11.5%
ROA (%)	8.2%	6.4%	12.7%	6.0%	6.1%
Net Debt / (Cash)	(3.3)	14.6	40.4	50.5	59.5
Net Gearing (X)	Net Cash	13.5%	33.1%	39.6%	44.7%



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