

Equities

Hong Kong/China

Company Update

## Company Report

# Phoenix Healthcare (1515 HK)

19 March 2015

## Establish General Clinic Network, Explore Profit Model of Medical Care Insurance

The company signed a framework agreement with UMP Healthcare Holdings Limited (UMP) to acquire its 20% stake at 15x PE. The two agreed to form and hold 50/50% equity interest in UMP Phoenix Healthcare Limited (the "JV Company"), which may develop the general clinic business in Beijing. Ten general clinic networks are expected to be established in Beijing in the coming three years.

- General clinic is a new business model to be explored.** Apart from setting up community general clinic network, the JV Company will also launch health care management plan (the "Plan") for companies and individuals in China with reference to UMP's existing business model. The Plan provides employees or individuals with year-round free-of-charge outpatient services after charging a certain amount of fixed annual fee, targeting mid to high-end customers by providing them with basic health insurance. This model is similar to commercial health insurance plans offered by those health care providers, which is in line with China's promotion of the development of medical care insurance as well as the establishment of multi-level healthcare systems under the healthcare reform, and is of smaller risk and greater sustainability. If the demonstration project in Beijing is successful, it can be replicated nationwide.
- General clinic creates synergies with existing business.** The integration of hospital groups with commercial medical care insurance abroad has proved to be successful with great synergies. For Phoenix Healthcare, community general clinics serve as grass-roots outpatient medical network to meet patients' demand for consultation, chronic disease and other health care issues, while transferring critically ill patients to the company's existing grade II and III hospitals to increase the number of visits of its traditional business. The Plan will also bring in advance premiums for the company to boost its operating cash flow and reduce its financial cost, which is conducive to the company's future expansion.
- Earnings forecast and valuation:** As the company is still in talks with UMP regarding the cooperation agreement, we would exclude the agreement from our forecast model. We estimate the company's 2014-16E EPS to be Rmb0.24, Rmb0.31 and Rmb0.37. Once the deal is clinched, we will adjust our earnings forecasts correspondingly. We give the company a 2015E EPS of 45x, corresponding to a target price of Rmb17.2. Reiterate "Buy".
- Risk factors:** The growth of the number of general clinic patients is slower than expected. Insufficient and inaccurate data provided by participants under the Plan.

### Investment Summary

Year ended 31 Dec	2012	2013	2014E	2015E	2016E
Turnover (Rmb m)	758	887	1,026	1,164	1,316
Growth (%)	49	17	16	13	13
Net profit (Rmb m)	101	139	204	257	310
Growth (%)	110	37	47	26	21
EPS (Rmb)	-	0.24	0.24	0.31	0.37
Growth (%)	-	-	1	26	21
PE (x)	-	47	46	37	30
EBITDA	200	240	284	357	432
Growth (%)	81	20	18	26	21
EV/EBITDA (x)	-	36	32	25	21
DPS (Rmb)	-	-	0.055	0.068	0.083
Yield (%)	-	-	0.49	0.61	0.74

Note: 2013 data excludes one-off IPO-related cost

Sources: Company, CER estimates

China / Biomedical / Medical Services

## BUY

Share Price	Target Price	Upside
HK\$13.02	HK\$17.20	32%

(As of 18 March 2015)

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52-wk Range (HK\$)

10.06 – 16.26

DVD yield (%)

0.49

### Latest Key Data

FF no of shares (m)	833,763
FF (%)	54.9
FF market cap (HK\$ m)	10,850
12M daily turnover (HK\$ m)	6,365
12M volatility (%)	-1.7
PEG FY14-16E (x)	2.0
ROE FY14-16E (%)	11.69
P/B FY14 (x)	4.7
Net debt/equity FY14 (%)	ND

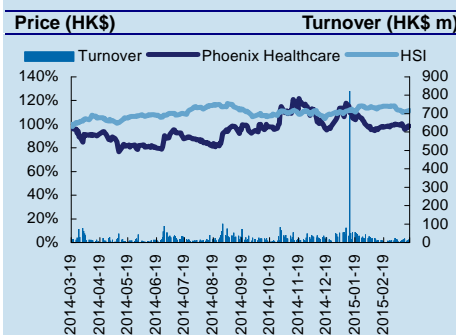
### Performance (%)

	1 个月	本年
Absolute	1.1	(9.0)
Relative to HSCEI	4.0	(11.1)

### Shareholding Structure (%)

Speed Key Limited	33.27
Senmart Investments	17.50
Hyde Intl. Investment	7.48

### Price Chart



Sources: Bloomberg, CER estimates

## Several thoughts on the establishment of general clinics

### 1. How to resolve the issue of doctor resources?

There is no training system for general doctors in China, and it will be too costly to introduce experts from Hong Kong or overseas. The company will establish the (general doctor) Professional and Training committee jointly with UMP Healthcare Holdings, and it will pick some medical personnel from its existing hospital network to attend training. In the next three years, 10 general clinics are expected to be opened, each with three general doctors. We estimate it will not be difficult to pick 30 medical personnel to receive training.

### 2. How to expand customer base of the health management scheme?

Two issues are crucial to future development of the general clinic + health management scheme: First, the number of members participating in the health plan should be large enough to diversify risks and create profit through growing economies of scale. Second, doctors should gain access to members' health data in a bid to launch targeted health products. Below is our understanding to these two issues.

- Recruitment of health management members will be mainly dependent on UMP's brand effect, as it has developed long-term cooperative relationship in Hong Kong with a number of multinational enterprises, government bodies and institutions under the model of general clinics. General clinics in Beijing will try to develop business relationship with UMP's existing customers with branches in Beijing, before they market to other enterprises or individuals with help of the demonstration effect of the first batch of customers. We expect the number of members for the health management scheme will witness swift growth in the first three years.
- Comprehensiveness and accuracy of customers' health data represent a bottleneck hindering the development of commercial health insurance plans. The company has done some research in this respect previously, and it will work to resolve this problem through shared commercial health insurance data. However, we are convinced the JV Company will not be able to fully break this bottleneck from data at the initial stage, which means general clinic products could face certain risks at the early stage, but considering the clinics will only provide outpatient service, the risks will be generally under control. With the development of this business, the combination of hospital services institutions and health insurance will enjoy genuine advantages in terms of collection and analysis of customer data, so the company will hopefully gain distinct competitive edges leveraging on comprehensive and accurate data. Membership recruitment -> medical services -> data collection and analysis -> more-targeted health management plan -> membership expansion is a self-reinforcing closed loop. At present, there are only a handful of medical services institutions conducting commercial health insurance business in China, and Phoenix Healthcare is likely to enjoy first-mover advantage in this area.

### 3. Any impact on company profitability?

Over 2015-16, the general clinic business in Beijing is expected to make only limited contribution to the company's profit as it will be at the introduction stage. The valuation of UMP Healthcare is currently HK\$900m, corresponding to 15x PE given approximately HK\$60m in annual profit, and 18% interest corresponds to profit of around HK\$10.80m. Taking into account Phoenix Healthcare is expected to post net profit of Rmb257m in 2015, the UMP interest should not have material impact on its profitability.

## Company Description

Phoenix Healthcare is the largest private hospital group in China. Since 2007, it has participated in public hospitals and now has 11 general hospitals, one traditional Chinese medicine hospital and 28 community clinics under the IOT model. We are optimistic about the company given its extensive experience in investment and management of hospitals with state-backed policies. It will expand hospital network in the short term, thus giving it an unparallel edge.

## Income Statement (Consolidated)

Year to 31 Dec (Rmb m)	2012	2013	2014E	2015E	2016E
Operating income	758	887	1,026	1,164	1,316
Operating cost	(573)	(675)	(774)	(873)	(980)
Gross profit	185	213	252	291	336
Other profits & losses	30	60	85	138	187
Operating expenses	(51)	(99)	(92)	(113)	(131)
Operating profit	163	204	245	317	392
Finance cost	(16)	(12)	39	41	41
Pre-tax profit	147	192	284	358	432
Income tax expenses	(37)	(47)	(71)	(90)	(108)
After-tax operating profit	111	145	213	269	324
Minorities	(10)	(6)	(9)	(11)	(14)
Net profit	101	139	204	257	310
EBITDA	200	240	284	357	432
EBIT	163	204	245	317	392
EPS (Rmb)	0.19	0.24	0.24	0.31	0.37
DPS (Rmb)	-	-	0.055	0.068	0.083

Note: 2013 data excludes one-off IPO-related fees

Sources: Company, CER estimates

## Cash Flow Statement (Consolidated)

Year to 31 Dec (Rmb m)	2012	2013	2014E	2015E	2016E
Operating cash flow	166	170	188	264	325
Net profit	101	90	204	257	310
Depreciation & amortization	36	37	39	40	40
Change in working capital	(6)	0	(46)	(16)	(11)
Others	35	44	(9)	(16)	(14)
Investing cash flow	(102)	(842)	18	17	16
Net capex	(28)	(21)	(24)	(25)	(25)
Disposal of assets	0	0	0	0	0
Change in LT investment	(37)	(820)	0	0	0
Change in other assets	(37)	(1)	42	41	41
Financing cash flow	(282)	971	364	(58)	(69)
Change in share capital	(200)	1,542	0	0	0
Net change in debt	33	(42)	410	0	0
Bonus payment	0	0	(46)	(58)	(69)
Change in other LT debts	(115)	(530)	0	0	0
Net impact of changes in foreign exchange rate	0	(11)	0	0	0
Net cash flow	(218)	289	570	223	272

Sources: Company, CER estimates

## Balance Sheet (Consolidated)

Year to 31 Dec (Rmb m)	2012	2013	2014E	2015E	2016E
Total assets	1,021	2,124	2,704	2,949	3,240
Current assets	365	1,473	2,075	2,340	2,650
Cash & cash equivalents	113	402	972	1,195	1,467
Marketable securities & ST investment	60	176	176	176	176
Accounts receivables	83	84	101	128	151
Inventories	35	31	36	40	45
Others	74	781	789	800	811
Non-current assets	656	651	630	610	590
Goodwill and intangible assets	323	317	303	289	274
Net fixed assets	122	123	126	129	131
Others	211	210	201	193	185
Total liabilities	443	408	821	855	891
Current liabilities	202	403	207	242	279
Accounts payable	122	124	100	116	132
ST borrowings	7	200	0	0	0
Others	73	79	107	127	147
LT liabilities	241	5	614	613	612
LT debts	232	0	610	610	610
Others	9	5	4	3	2
Total equities	578	1,716	1,883	2,094	2,349
Shareholders' equity	485	1,617	1,775	1,975	2,216
Minorities	93	99	108	119	133
Total liabilities + SH equities	1,021	2,124	2,704	2,949	3,240
Net cash / (debt)	(126)	202	362	585	857
Net gearing (%)	ND	ND	ND	ND	ND

Sources: Company, CER estimates

## Financial Summary

Year to 31 Dec	2012	2013	2014E	2015E	2016E
Growth (%)					
Revenue	49	17	16	13	13
EBITDA	81	20	18	26	21
EBIT	81	25	20	30	24
Net profit	110	37	47	26	21
Margins (%)					
Gross	24	24	25	25	25
EBITDA	26	27	28	31	33
EBIT	22	23	24	27	30
Net margins	13	16	20	22	24
Others (%)					
Effective tax rate	25	24	25	25	25
Payout ratio	0.00	0.00	0.49	0.61	0.74
ROIC	35	15	17	19	21
Average ROE	15	12	11	13	13
Average ROA	9	9	8	9	10
ICR (x)	ND	ND	ND	ND	ND

Note: 2013 data excludes one-off IPO-related fees

Sources: Company, CER estimates

## China Everbright Research Limited Rating System

Buy	Expected to outperform the benchmark index by >15% over the next six months
Accumulate	Expected to outperform the benchmark index by 5 - 15% over the next six months
Hold	Expected to outperform or underperform the benchmark index by <5% over the next six months
Reduce	Expected to underperform the benchmark index by 5 - 15% over the next six months
Sell	Expected to underperform the benchmark index by >15% over the next six months

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