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# Kalbe Farma

## Update on recent issue: drugs price reduction

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We upgrade our call on KLBF to Neutral with similar TP of Rp 1,200. Our target on KLBF has pierced through and we view the negative sentiment already reflected in current price. Government's plan to push down branded drugs price has been a major issue lately, but we expect the real implementation would rather be difficult. Although we still wait for further KPPU's info regarding this issue, which will resolve next Monday based on our channel check, but we expect there are 2 ways of reducing drugs price: (1) through price ceiling system, or (2) removing tax from drugs. In addition, in any case that Government opens foreign exposure in pharma industry to 100%, we view that pharma company as big as KLBF will not be affected much as the business, in particular the distribution, is not easy to replicate.

### Price ceiling system: slowly kill pharma industry

We've checked on numerous drugs price control in India, Canada, China, and USA. The impact, though it can reduce drugs price, will cut R&D budget even further hence number of new drugs (we're talking about social welfare in the long run). We view that through this price ceiling system, Government would kill pharma industry, in contradiction with Government's plan to promote this industry. We, however, have done sensitivity analysis towards KLBF in case the regulation is applied. We ended with TP of Rp 500-850 if no ASP hikes or ASP reduction by 6% in 2016-20F.

### Removing tax from drugs

Another way is to eliminate tax from drugs just like Malaysian Government do. In Indonesia, on the other hand, Government applies 10% tax for drugs. We view it is very unlikely for Government to eliminate tax from drugs considering that our tax revenue is always below target. Per Nov'15, we note that our tax income only reached 59.8% from target of Rp 1.3trn.

### Valuation: NEUTRAL with TP of Rp 1,200

We reiterate KLBF at Rp 1,200 using DCF method (WACC of 13%, LTG of 5%). We do not change our numbers as we view it is very unlikely for Government to apply both methods we analyzed. Our TP implies 2016-17F P/E of 27.5x and 24.0x.



Kalbe Farma is the largest publicly-listed pharmaceuticals company in Southeast Asia.

**Neutral**      **Rp 1,200**

### Company Update

Share Price	Rp 1,185
Sector	Healthcare
Price Target	Rp 1,200 (+1%)

### Stock Data

Reuters Code	KLBF.JK
Bloomberg Code	KLBF.IJ
Issued Shares	46,875
Mkt Cap. (Rpbn)	55,547
Avg. Value Daily 6 Month (Rpbn)	63.2
52-Wk range	1915 / 1135

### Major Shareholders

PT. Gira Sole Prima	10.2%
Others	46.5%
Public	43.3%

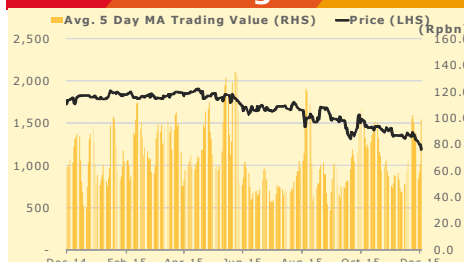
### Consensus

<b>Core EPS</b>	<b>15F</b>	<b>16F</b>
Consensus (Rp)	45	50
TRIM vs Cons. (%)	-5.8	-12.7

### Companies Data

Year end Dec	2013	2014	2015F	2016F	2017F
Sales (Rp bn)	16,002	17,369	17,727	18,918	21,394
EBITDA (Rp bn)	2,736	2,998	2,993	3,140	3,581
Net Profit (Rp bn)	1,971	2,121	2,024	2,104	2,401
EPS (Rp)	41	44	42	44	50
EPS Growth (%)	11%	8%	-5%	4%	15%
DPS (Rp)	19	17	18	20	23
BVPS (Rp)	173	200	223	247	275
EV/EBITDA (x)	20.0	18.0	18.0	17.0	14.9
P/E (x)	28.9	26.9	28.2	27.1	23.7
Div Yield (%)	1.6	1.4	1.5	1.7	1.9

### Stock Price & Avg. Trade Value



## Sensitivity analysis

We conduct sensitivity analysis to determine KLBF's TP in case Government applies price ceiling system to reduce branded drugs price. In our assumption, we assume 3 scenarios: (1) company could not raise its ASP by 2% as historical, (2) company would require to tweak down their ASP by 2% in 2016-20F, and (3) company reduce their ASP further by 6% in 2016-20F.

**Figure 1. Could not raise ASP by 2%**

	2017F	2018F	2019F	2020F	2021F	2022F	2023F	2024F	2025F	2026F
EBIT	2,935	3,263	3,640	4,075	4,816	5,698	6,751	8,008	9,512	11,310
EBIT (1-T)	2,231	2,480	2,766	3,097	3,660	4,331	5,131	6,086	7,229	8,596
Capex	-1,077	-1,238	-1,139	-1,276	-1,429	-1,334	-1,467	-1,291	-1,395	-1,506
Changes in	-529	-655	-758	-878	-1,105	-1,291	-1,511	-1,771	-2,078	-2,441
Depreciation	457	519	576	640	711	778	851	916	986	1,061
FCFF (Rp bn)	1,082	1,105	1,445	1,583	1,837	2,483	3,004	3,940	4,742	5,710
Discounted FCFF	1,082	976	1,128	1,091	1,118	1,335	1,426	1,652	1,757	1,868
Terminal value	72,975									
PV of terminal	23,879									
Total company	37,313									
Net debt	-2,146									
NAV	39,459									
NAV / share	<b>842</b>									

Source: TRIM Research

In our first scenario, there is probability that Government will not push company to reduce their ASP, but instead limit their ASP hikes. Historically, KLBF managed to up its ASP by 2%, except in 2015. Hence, in this scenario, we assume there is no ASP hikes in our calculation. As the impact, we obtained KLBF TP at Rp 850, with EPS growth 2016-17F of 11% YoY. KLBF net income in 2016F down by 6% YoY.

**Figure 2. Reduce ASP by 2% in 2016-20F**

	2017F	2018F	2019F	2020F	2021F	2022F	2023F	2024F	2025F	2026F
EBIT	2,751	2,961	3,202	3,478	4,147	4,949	5,913	7,069	8,460	10,132
EBIT (1-T)	2,090	2,251	2,433	2,644	3,152	3,762	4,494	5,372	6,430	7,701
Capex	-1,077	-1,238	-1,139	-1,276	-1,429	-1,334	-1,467	-1,291	-1,395	-1,506
Changes in working capital	-515	-639	-739	-857	-1,095	-1,280	-1,499	-1,757	-2,062	-2,423
Depreciation	457	519	576	640	711	778	851	916	986	1,061
FCFF (Rp bn)	955	892	1,131	1,151	1,339	1,925	2,379	3,240	3,958	4,832
Discounted FCFF	955	788	882	793	815	1,035	1,130	1,359	1,466	1,581
Terminal value	61,755									
PV of terminal value	20,207									
Total company value	31,012									
Net debt	-2,054									
NAV	33,066									
NAV / share	<b>705</b>									

Source: TRIM Research

In second scenario, we assume that Government will opted to push company in reducing its ASP, by 2% as historical increase. However, we assume the price decline to be in 2016-20F only, given limited operational cost. We reach KLBF TP at Rp 700 with EPS growth 2016-17F of -3% YoY. In this scenario, KLBF net profit in 2016F decline by 9% YoY.

**Figure 3. Reduce ASP by 6% in 2016-20F**

	2017F	2018F	2019F	2020F	2021F	2022F	2023F	2024F	2025F	2026F
EBIT	2,392	2,394	2,402	2,422	2,965	3,625	4,429	5,407	6,599	8,048
EBIT (1-T)	1,818	1,819	1,826	1,841	2,253	2,755	3,366	4,110	5,015	6,117
Capex	-1,077	-1,238	-1,139	-1,276	-1,429	-1,334	-1,467	-1,291	-1,395	-1,506
Changes in	-490	-611	-707	-822	-1,078	-1,261	-1,477	-1,733	-2,035	-2,393
Depreciation	457	519	576	640	711	778	851	916	986	1,061
FCFF (Rp bn)	709	489	555	383	458	938	1,273	2,001	2,571	3,278
Discounted FCFF	709	432	433	264	279	504	604	839	953	1,073
Terminal value	41,900									
PV of terminal	13,710									
Total company	19,800									
Net debt	-1,874									
NAV	21,674									
NAV / share	<b>462</b>									

Source: TRIM Research

Our last scenario, we assume Government will push KLBF further in terms of selling price, hence -6% in 2016-20F (margin of branded drugs becomes similar with margin of generic drugs at 12%). Again, we limit our ASP reduction in 5 years only. As the result, KLBF TP reached Rp 500 with EPS growth 2016-17F of -10% YoY and net income of -15% YoY in 2016F.

### Income Statement (Rpbn)

Year end Dec	2013	2014	2015F	2016F	2017F
Revenue	16,002	17,369	17,727	18,918	21,394
Revenue Growth	17.3%	8.5%	2.1%	6.7%	13.1%
Gross Profit	7,679	8,476	8,613	9,200	10,486
Opr. Profit	2,551	2,752	2,640	2,737	3,124
EBITDA	2,736	2,998	2,993	3,140	3,581
EBITDA Growth (%)	15.4%	9.6%	-0.2%	4.9%	14.0%
Net Int Inc/(Exp)	22	11	23	31	35
Gain/(loss) Forex	1	14	14	14	14
Other Inc/(Exp)	4	(20)	(9)	(9)	(9)
Pre-tax Profit	2,573	2,764	2,663	2,768	3,159
Tax	(602)	(643)	(639)	(664)	(758)
Minority Int.	51	56	56	56	56
Extra. Items	-	-	-	-	-
Reported Net Profit	1,971	2,121	2,024	2,104	2,401
Core Net Profit	1,920	2,065	1,968	2,047	2,344
Growth (%)	10.7%	7.6%	-4.7%	4.0%	14.5%
Dividend per share	19	17	18	20	23
growth (%)	0.0%	-10.5%	6.2%	8.9%	14.5%
Dividend payout	47%	39%	43%	45%	45%

### Cash Flow (Rpbn)

Year end Dec	2013	2014	2015F	2016F	2017F
Net Profit	1,920	2,065	1,968	2,047	2,344
Depr / Amort	185	246	353	403	457
Chg in Working Cap	(1,177)	6	8	(267)	(543)
Others	(6)	72	-	-	-
CF's from oprs	927	2,316	2,329	2,183	2,258
Capex	(971)	(821)	(900)	(1,000)	(1,077)
Others	104	144	59	66	70
CF's from investing	(867)	(677)	(841)	(934)	(1,007)
Dividend	(901)	(810)	(846)	(921)	(1,055)
Others	287	(368)	100	(35)	(35)
CF's from financing	(613)	(1,177)	(746)	(956)	(1,090)
Net cash flow	(554)	462	741	293	161
Cash at BoY	1,829	1,371	1,474	2,215	2,508
Cash at EoY	1,371	1,834	2,215	2,508	2,670
Free Cashflow	(10)	1,543	1,468	1,217	1,211

### Interim Result (Rpbn)

	3Q14	4Q14	1Q15	2Q15	3Q15
Sales	4,379	4,610	4,247	4,473	4,408
Gross Profit	2,119	2,345	2,102	2,196	2,113
EBITDA	729	829	757	776	667
Opr. Profit	667	769	682	704	593
Net profit	507	598	537	547	450
Core profit	494	578	529	534	436
Gross Margins (%)	48.4%	50.9%	49.5%	49.1%	47.9%
EBITDA Margins (%)	16.7%	18.0%	17.8%	17.3%	15.1%
Opr Margins (%)	15.2%	16.7%	16.1%	15.7%	13.5%
Net Margins (%)	11.6%	13.0%	12.7%	12.2%	10.2%
Core Margins (%)	11.3%	12.5%	12.4%	11.9%	9.9%

### Balance Sheet (Rpbn)

Year end Dec	2013	2014	2015F	2016F	2017F
Cash and equivalents	1,426	1,895	2,215	2,508	2,670
Other curr asset	6,071	6,226	6,237	6,608	7,357
Net fixed asset	2,926	3,404	3,951	4,548	5,168
Other asset	892	900	875	875	875
Total asset	11,315	12,425	13,279	14,540	16,070
ST debt	584	252	344	344	344
Other curr liab	2,057	2,134	2,153	2,258	2,463
LT debt	-	44	87	87	87
Other LT Liab	175	177	177	177	177
Minority interest	392	435	63	94	129
Total Liabilities	2,815	2,608	2,762	2,866	3,072
Shareholders Equity	8,108	9,382	10,454	11,580	12,869
Net debt / (cash)	(843)	(1,598)	(1,784)	(2,077)	(2,239)
Total cap employed	8,674	10,039	10,782	11,938	13,262
Net Working capital	4,857	5,735	5,955	6,515	7,219
Debt	584	296	431	431	431

### Key Ratio Analysis

Year end Dec	2013	2014	2015F	2016F	2017F
<b>Profitability</b>					
Gross Margin (%)	48.0%	48.8%	48.6%	48.6%	49.0%
Opr Margin (%)	15.9%	15.8%	14.9%	14.5%	14.6%
EBITDA Margin (%)	17.1%	17.3%	16.9%	16.6%	16.7%
Core Net Margin (%)	12.0%	11.9%	11.1%	10.8%	11.0%
ROAE (%)	25.3%	23.6%	19.8%	18.6%	19.2%
ROAA (%)	18.5%	17.4%	15.3%	14.7%	15.3%
<b>Stability</b>					
Current ratio (x)	2.8	3.4	3.4	3.5	3.6
Net Debt to Equity (x)	(0.1)	(0.2)	(0.2)	(0.2)	(0.2)
Net Debt to EBITDA (x)	(0.3)	(0.5)	(0.6)	(0.7)	(0.6)
Interest Coverage (x)	89.1	52.9	75.1	77.8	88.8
<b>Efficiency</b>					
A/P (days)	52	63	62	60	57
A/R (days)	48	50	50	48	47
Inventory (days)	113	126	125	122	119

### Capital History

Date	
30-Jul-91	IPO@Rp7,800
08-Oct-12	Stock split 1:5
13-Dec-13	Decrease in issued and fully paid shares

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