

# Yunkang Group (2325 HK)

## Strong growth driven by continued expansion of medical institution alliance network

Yunkang's revenue increased 82% YoY to RMB1.38bn in 1H22, primarily attributable to the rapid growth of diagnostic testing services driven by COVID-19 under the dynamic zero-Covid policy in China. The overall gross margin decreased to 47.2% in 1H22 (50.9% in 1H21, 53.0% in FY21), mainly due to the decrease of the average unit price of Covid-19 tests regulated by the government. With relatively stable SG&A expense ratio, the net profit margin in 1H22 decreased from 20.6% in 1H21 (or 23.9% in 2021) to 17.0% in 1H22. In 1H22, Yunkang generated RMB234.4mn attributable net profit (+50% YoY), and the Company has declared an interim dividend of HK\$0.088 per share (c. 20% payout ratio). Trade and other receivables expanded to RMB1.57bn as of Jun 2022 from RMB886.9mn in end-2021 due to increased service orders and long settlement duration of revenue from public hospitals and China CDC.

■ **Strong growth in the core business of diagnostic testing services for medical institution alliances.** The revenue from diagnostic outsourcing services (ICL business) increased 41% YoY to RMB680.4mn, while the revenue from the core business, on-site diagnostic services for medical institution alliances, increased more significantly by 166% YoY to RMB650.7mn. In 1H22, diagnostic testing services for medical institution alliances accounted for 47% of the total revenue (vs 32% in 1H21). The growth of the core business was mainly driven by the increased number of on-site diagnostic centres and improved average revenue per centre. As of Jun 2022, Yunkang assisted in establishing and operating 350 on-site diagnostic centres, with nearly 90 additional centres under development. The semi-annual average revenue from each centre was RMB1.9mn in 1H22 (vs a full-year average revenue of RMB2.2mn in FY21).

■ **Continue to expand the medical institution alliance network and to enhance operational capabilities.** The Company plans to primarily focus on pathology, genetic and infectious disease laboratories while rapidly expanding its on-site diagnostic services for medical institution alliances. Yunkang also targets to develop small-scale self-operated ICLs to provide timely services for customers, and aims to digitalise its testing services by developing technical and operating systems to support its operations. Yunkang is open to acquire or invest in companies with potential business synergies.

■ **Maintain BUY.** We revised our DCF-based target price from HK\$23.44 to HK\$23.21 (WACC: 11.9%, terminal growth rate: 2.0%).

### Earnings Summary

(YE 31 Dec)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue (RMB mn)	1,200.3	1,696.7	2,719.2	2,686.7	2,750.3
YoY growth (%)	77.1%	41.4%	60.3%	(1.2%)	2.4%
Net profit (RMB mn)	260.2	381.9	601.9	605.8	658.8
YoY growth (%)	(924.8%)	46.8%	57.6%	0.6%	8.8%
EPS (Reported)(RMB)	na	na	0.97	0.98	1.06
YoY growth (%)	na	na	na	0.6%	8.8%
P/E (x)	na	na	16.6	16.5	15.2
Net gearing (%)	11.4%	(32.4%)	(36.2%)	(36.8%)	(37.8%)

Source: Company data, Bloomberg, CMBIGM estimates

**BUY (Maintain)**

**Target Price** HK\$23.21

(Previous TP) HK\$23.44

**Up/Downside** 23.9%

**Current Price** HK\$18.74

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### Stock Data

Mkt Cap (HK\$ mn)	11,642.2
Avg 3 mths t/o (HK\$ mn)	NA
52w High/Low (HK\$)	19.18/6.60
Total Issued Shares (mn)	621.3

Source: FactSet

### Shareholding Structure

YK Development	40.3%
Daan International	33.8%

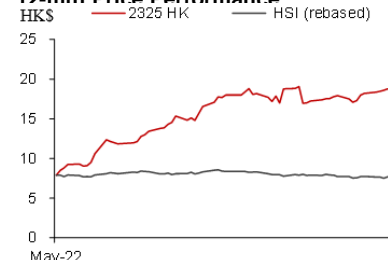
Source: HKEx

### Share Performance

	Absolute	Relative
1-mth	4.8%	8.0%
3-mth	NA	NA
6-mth	NA	NA

Source: FactSet

### 12-mth Price Performance



Source: FactSet

**Auditor:** PWC

**Website:** www.yunkanghealth.com

### Related report:

1. A leading medical operation service provider with strong operation capabilities – 27 Jun 2022

Figure 1: Risk-adjusted DCF valuation

DCF Valuation (in RMB mn)	2022E	2023E	2024E	2025E	2026E	2027E	2028E	2029E	2030E
EBIT	736	741	805	896	1,224	1,594	2,020	2,449	2,879
Tax rate	17.0%	17.0%	17.0%	17.0%	17.0%	17.0%	17.0%	17.0%	17.0%
EBIT*(1-tax rate)	611	615	668	744	1,016	1,323	1,677	2,033	2,389
+ D&A	80	102	121	139	160	178	195	211	225
- Change in working capital	(330)	31	(7)	(37)	(206)	(236)	(265)	(280)	(280)
- Capex	(300)	(300)	(300)	(300)	(350)	(350)	(350)	(350)	(350)
FCFF	61	448	482	546	619	915	1,257	1,613	1,984
Terminal value									20,469
Terminal growth rate	2.0%								
WACC	11.9%								
Cost of Equity	16.0%								
Cost of Debt	5.0%								
Equity Beta	1.3								
Risk Free Rate	3.0%								
Market Risk Premium	10.0%								
Target Debt to Asset ratio	35.0%								
Effective Corporate Tax Rate	15.0%								
Terminal value (RMB mn)	7,449								
Total PV (RMB mn)	11,324								
Net debt (RMB mn)	-932								
Minority interest (RMB mn)	-0								
Equity value (RMB mn)	12,256								
# of shares (mn)	621								
Price per share (RMB per share)	19.73								
Price per share (HK\$ per share)	23.21								

Source: CMBIGM estimates

Figure 2: Sensitivity analysis (HK\$)

		10.9%	11.4%	WACC 11.9%	12.4%	12.9%
Terminal growth rate	3.0%	28.87	26.79	24.95	23.32	21.87
	2.5%	27.63	25.72	24.03	22.53	21.17
	2.0%	26.53	24.77	23.21	21.81	20.54
	1.5%	25.54	23.92	22.46	21.15	19.97
	1.0%	24.66	23.15	21.79	20.56	19.44

Source: Company data, CMBIGM estimates

Figure 3: CMBIGM estimates revision

	New			Old			Diff(%)		
RMB mn	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	2,719	2,687	2,750	2,719	2,734	2,815	0.0%	-1.7%	-2.3%
Gross profit	1,355	1,317	1,383	1,343	1,338	1,414	0.9%	-1.6%	-2.1%
Operating profit	725	730	794	728	747	816	-0.4%	-2.3%	-2.8%
Net profit	602	606	659	604	620	678	-0.4%	-2.3%	-2.8%
EPS (RMB)	0.97	0.98	1.06	0.97	1.00	1.09	-0.4%	-2.3%	-2.8%
Gross margin	49.82%	49.00%	50.30%	49.39%	48.95%	50.21%	+0.43 ppt	+0.06 ppt	+0.09 ppt

Source: Company data, CMBIGM estimates

Figure 4: CMBIGM estimates vs consensus

	CMBIGM			Consensus			Diff(%)		
RMB mn	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	2,719	2,687	2,750	2,399	2,760	2,940	13.3%	-2.7%	-6.5%
Gross profit	1,355	1,317	1,383	1,207	1,380	1,504	12.2%	-4.6%	-8.0%
Operating profit	725	730	794	977	1,136	898	-25.8%	-35.8%	-11.6%
Net profit	602	606	659	542	631	731	11.1%	-4.0%	-9.9%
EPS (RMB)	0.97	0.98	1.06	0.88	1.02	1.18	10.5%	-4.4%	-9.7%
Gross margin	49.82%	49.00%	50.30%	50.33%	50.00%	51.15%	-0.52 ppt	-1.00 ppt	-0.85 ppt

Source: Company data, Bloomberg, CMBIGM estimates

## Financial Summary

INCOME STATEMENT	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec (RMB mn)						
Revenue	678	1,200	1,697	2,719	2,687	2,750
Cost of goods sold	(379)	(544)	(798)	(1,365)	(1,370)	(1,367)
Gross profit	299	656	899	1,355	1,317	1,383
Operating expenses	(310)	(333)	(448)	(629)	(587)	(590)
Selling expense	(193)	(219)	(273)	(402)	(398)	(402)
Admin expense	(113)	(105)	(152)	(204)	(188)	(187)
Others	(4)	(9)	(23)	(23)	(1)	(1)
Pre-tax profit	(11)	323	451	725	730	794
Income tax	(1)	(53)	(79)	(123)	(124)	(135)
Others	(20)	(10)	9	0	0	0
Net profit	(32)	260	382	602	606	659
Minority interest	(1)	5	1	0	0	0
Net profit to shareholders	(31)	255	381	602	606	659
BALANCE SHEET	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec (RMB mn)						
Current assets	419	1,435	1,743	2,434	2,531	2,703
Cash & equivalents	64	336	801	1,262	1,388	1,555
Account receivables	260	485	825	1,043	1,016	1,025
Inventories	15	25	42	53	51	48
Prepayment	49	351	44	44	44	44
Financial assets at FVTPL	0	150	0	0	0	0
Other current assets	30	89	31	31	31	31
Non-current assets	851	522	712	1,040	1,249	1,438
PP&E	103	277	485	709	911	1,094
Deferred income tax	26	40	36	36	36	36
Investment in JVs & assos	22	20	0	0	0	0
Intangibles	55	7	6	12	18	24
Financial assets at FVTPL	57	59	58	178	178	178
Other non-current assets	588	119	127	105	105	105
Total assets	1,269	1,957	2,455	3,475	3,779	4,141
Current liabilities	412	819	871	770	772	771
Short-term borrowings	137	421	208	208	208	208
Account payables	258	329	557	456	458	457
Tax payable	1	33	72	72	72	72
Other current liabilities	16	36	34	34	34	34
Non-current liabilities	67	71	133	133	133	133
Long-term borrowings	50	51	82	82	82	82
Obligations under finance leases	6	9	44	44	44	44
Deferred income	6	0	0	0	0	0
Other non-current liabilities	5	11	6	6	6	6
Total liabilities	479	890	1,004	903	905	904
Share capital	0	1	21	21	21	21
Capital surplus	939	955	955	1,654	1,654	1,654
Retained earnings	(164)	92	475	897	1,199	1,562
Total shareholders equity	776	1,048	1,452	2,571	2,874	3,237
Minority interest	15	18	(0)	(0)	(0)	(0)
Total equity and liabilities	1,269	1,957	2,455	3,475	3,779	4,141
CASH FLOW	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec (RMB mn)						
Operating						

<b>Profit before taxation</b>	<b>(11)</b>	<b>323</b>	<b>451</b>	<b>725</b>	<b>730</b>	<b>794</b>
Depreciation & amortization	26	33	52	76	98	117
Change in working capital	(13)	(152)	(133)	(330)	31	(7)
Others	2	(0)	(1)	(87)	(109)	(120)
<b>Net cash from operations</b>	<b>5</b>	<b>203</b>	<b>369</b>	<b>385</b>	<b>750</b>	<b>784</b>
<b>Investing</b>						
Capital expenditure	(27)	(45)	(223)	(300)	(300)	(300)
Acquisition of subsidiaries/ investments	(20)	0	0	0	0	0
Net proceeds from disposal of short-term investments	(118)	(50)	174	(120)	0	0
Others	(157)	(96)	359	(8)	(8)	(8)
<b>Net cash from investing</b>	<b>(323)</b>	<b>(191)</b>	<b>311</b>	<b>(428)</b>	<b>(308)</b>	<b>(308)</b>
<b>Financing</b>						
Dividend paid	0	0	0	(181)	(303)	(296)
Net borrowings	(1)	286	(181)	0	0	0
Proceeds from share issues	0	(1)	(6)	698	0	0
Others	(18)	(24)	(28)	(13)	(13)	(13)
<b>Net cash from financing</b>	<b>(18)</b>	<b>261</b>	<b>(215)</b>	<b>505</b>	<b>(316)</b>	<b>(310)</b>
<b>Net change in cash</b>						
Cash at the beginning of the year	400	64	336	801	1,262	1,388
Exchange difference	0	(1)	0	0	0	0
<b>Cash at the end of the year</b>	<b>64</b>	<b>336</b>	<b>801</b>	<b>1,262</b>	<b>1,388</b>	<b>1,555</b>
<b>GROWTH</b>	<b>2019A</b>	<b>2020A</b>	<b>2021A</b>	<b>2022E</b>	<b>2023E</b>	<b>2024E</b>
<b>YE 31 Dec</b>						
Revenue	13.7%	77.1%	41.4%	60.3%	(1.2%)	2.4%
Gross profit	24.5%	119.2%	37.1%	50.7%	(2.8%)	5.1%
Net profit	(37.3%)	(924.8%)	46.8%	57.6%	0.6%	8.8%
<b>PROFITABILITY</b>	<b>2019A</b>	<b>2020A</b>	<b>2021A</b>	<b>2022E</b>	<b>2023E</b>	<b>2024E</b>
<b>YE 31 Dec</b>						
Gross profit margin	44.1%	54.6%	53.0%	49.8%	49.0%	50.3%
Net profit margin	(4.6%)	21.3%	22.5%	22.1%	22.5%	24.0%
Return on assets (ROA)	n/m	13.0%	15.5%	17.3%	16.0%	15.9%
Return on equity (ROE)	(4.0%)	24.4%	26.2%	23.4%	21.1%	20.4%
<b>GEARING/LIQUIDITY/ACTIVITIES</b>	<b>2019A</b>	<b>2020A</b>	<b>2021A</b>	<b>2022E</b>	<b>2023E</b>	<b>2024E</b>
<b>YE 31 Dec</b>						
Net debt to equity (x)	0.1	0.1	(0.3)	(0.4)	(0.4)	(0.4)
Current ratio (x)	1.0	1.8	2.0	3.2	3.3	3.5
Receivable turnover days	132.2	113.3	138.0	135.0	135.0	135.0
Inventory turnover days	15.0	13.0	13.5	11.6	11.0	10.5
Payable turnover days	120.0	106.0	122.0	122.0	122.0	122.0
<b>VALUATION</b>	<b>2019A</b>	<b>2020A</b>	<b>2021A</b>	<b>2022E</b>	<b>2023E</b>	<b>2024E</b>
<b>YE 31 Dec</b>						
P/E	na	na	na	16.6	16.5	15.2

Note: The calculation of net cash includes financial assets. Source: Company data, CMBIGM estimates

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