

Quintiles Transnational Holdings Inc.

First-Quarter Analysis; Another Great Quarter Driven by Strong Fundamentals; Guidance Increased

Conclusion

Quintiles reported better-than-expected first-quarter results and increased its 2014 guidance. While some of the guidance increase is due to one-time items in the quarter (\$0.08 of \$0.12 of outperformance) and a positive foreign-exchange impact, we are impressed with the solid bookings, record RFP environment, and deep client relationships that should insulate the company from sponsor consolidation relative to its peer group. Following the strong results and guidance revision for 2014, we are increasing our 2014 EPS estimate by \$0.12, to \$2.52 (up 19%, the midpoint of management's revised range). In 2015, we are increasing our estimate by \$0.10, to \$2.82 (up 12%), to reflect the one-time nature of a few of the earnings drivers this quarter. We reiterate our Outperform rating on Quintiles given the robust demand trends in both segments of the business.

Model Changes

For 2014 we now model revenue of \$4.14 billion, up \$29 million from our previous model and representing 8.7% growth (5.9% on an organic constant dollar basis). We now estimate operating margin of 13.5% (in line with our previous model). We model sequential margin reduction of 110 basis points as the company saw 110 basis points of positive foreign-exchange impact in the first quarter. Although foreign exchange should continue to be a benefit and we model some top-line lift as a result, we do not include a bottom-line benefit in our analysis given volatility in recent quarters. We now model EPS of \$2.52 (up 19% and \$0.12 above our prior \$2.40 target). In 2015 we model revenue growth of 7.8% (unchanged), operating margin of 13.8% (unchanged), and EPS of \$2.82 (up 12% and up 10 cents from our previous model).

Stock Thoughts and Valuation

Q shares trade at 17.3 times our updated 2015 EPS estimate, compared with its peer group of 16.7 times. We believe the company's scale, diverse client base, and lower risk profile justify a valuation slightly ahead of the group; therefore, we believe shares represent an attractive value at current levels. We reiterate our Outperform rating on Quintiles as we believe its industry-leading position should allow for more predictable revenue and better visibility to double-digit earnings growth potential relative to its peers. Our updated model is summarized in exhibit 1, on the following page.

Quintiles is the largest pharmaceutical outsourcing company in the world, with an annual revenue base approaching \$4 billion. Founded in 1982, the company is now a leader in both outsourced drug development and commercialization services. It operates in 100 countries, employs roughly 27,000 employees, and has generated double-digit revenue and EBITDA growth, on average, over the past decade.

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May 01, 2014

Stock Rating: **Outperform**
Company Profile: **Established Growth**

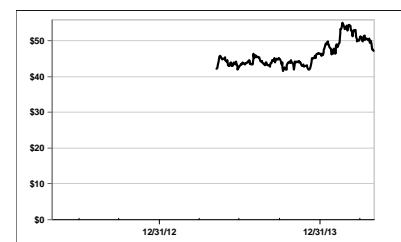
Symbol: Q (NYSE)
Price: \$48.76 (52-Wk.: \$40-\$55)
Market Value (mil.): \$6,129
Fiscal Year End: December
Long-Term EPS Growth Rate: 12%
Dividend/Yield: None

	2013A	2014E	2015E
Estimates			
EPS Q1	\$0.49	A\$0.68	NA
Q2	\$0.50	\$0.60	NA
Q3	\$0.54	\$0.61	NA
Q4	\$0.58	\$0.63	NA
FY	\$2.10	\$2.52	\$2.82
CY		\$2.52	\$2.82
Valuation			
FY P/E	23.2x	19.3x	17.3x
CY P/E		19.3x	17.3x

Trading Data (FactSet)	
Shares Outstanding (mil.)	129
Float (mil.)	58
Average Daily Volume	749,819

Financial Data (FactSet)	
Long-Term Debt/Total Capital (MRQ)	0.0
Book Value Per Share (MRQ)	-5.1
Return on Equity (TTM)	0.0

Two-Year Price Performance Chart



Sources: FactSet, William Blair & Company estimates

Exhibit 1: Updated Quintiles Income Statement Summary (2010-2015E)

	2010	2011	2012	2013	Q1'14	Q2'14E	Q3'14E	Q4'14E	2014E	2015E
Product Development Revenue	\$2,221.9	\$2,437.8	\$2,728.7	\$2,919.7	\$770.8	\$796.2	\$786.7	\$828.1	\$3,181.9	\$3,439.6
I.H.S. Revenue	\$774.8	\$857.1	\$963.7	\$888.6	\$234.5	\$235.1	\$238.8	\$247.9	\$956.3	\$1,023.2
Net revenue	\$2,996.8	\$3,294.9	\$3,692.4	\$3,808.3	\$1,005.3	\$1,031.3	\$1,025.5	\$1,076.0	\$4,138.1	\$4,462.8
Total Cost of revenue	1,925.0	\$2,153.0	\$2,459.4	\$2,471.4	\$643.7	\$667.7	\$661.8	\$696.4	\$2,669.6	\$2,867.3
Gross profit	1,071.8	\$1,142.0	\$1,233.0	\$1,336.9	\$361.6	\$363.6	\$363.7	\$379.7	\$1,468.6	\$1,595.5
Selling, general and administrative expense	608.9	\$651.7	\$687.3	\$725.3	\$190.2	\$199.2	\$197.0	\$205.9	\$792.2	\$845.8
EBITDA	462.9	\$490.3	\$545.7	\$611.6	\$171.4	\$164.4	\$166.7	\$173.8	\$676.3	\$749.7
Depreciation and amortization expense	84.6	\$91.9	\$100.3	\$107.5	\$29.1	\$29.1	\$30.0	\$31.1	\$119.2	\$135.3
Operating income (including options beg Q105)	378.3	\$398.4	\$445.4	\$504.1	\$142.324	\$135.4	\$136.7	\$142.7	\$557.1	\$614.4
Interest and other income (expense), net	(133.4)	(\$102.8)	(\$127.8)	(\$119.4)	(\$18.6)	(22.38)	(22.38)	(22.37)	(\$85.7)	(\$80.0)
Pretax income	245	\$295.6	\$317.6	\$384.7	\$123.7	112.98	114.36	120.31	\$471.4	\$534.4
Income tax expense	84.2	\$100.4	\$112.0	\$115.2	\$37.6	33.90	34.31	36.09	\$141.9	\$160.3
Equity investee earnings	1.11	(\$4.2)	\$3.0	(\$1.3)	\$4.9	0.48	0.37	(0.47)	\$5.3	\$0.0
Loss/(income) from Noncontrolling interests/minority interest	0.000	1.400	0.900	0.867	(0.0)	0.25	0.30	0.30	0.819	1.100
Net income (non-GAAP)	\$161.8	\$200.8	\$209.5	\$269.1	\$90.9	\$79.8	\$80.7	\$84.0	\$335.5	\$375.2
Nonrecurring items	(5.2)	(36.3)	(50.3)	(61.6)	(1.0)	(3.3)	(3.3)	(3.3)	(10.8)	(6.0)
Tax adjustment	1.8	87.1	18.9	19.2	0.2	1.0	1.0	1.0	3.2	2.0
Non controlling interest		(1.4)	0.0	0.0	0.0	(0.3)	(0.3)	(0.3)	(0.9)	(1.1)
Nonrecurring items (net of tax)	(3.4)	49.4	(31.5)	(42.3)	(0.8)	(2.5)	(2.6)	(2.6)	(8.4)	(5.1)
Net income (GAAP)	\$158	\$240.4	\$177.4	\$226.4	\$90.2	\$77.3	\$78.1	\$81.5	\$327.1	\$370.1
EPS (excl. nonrecurring items, incl. options beg Q105, diluted)	\$1.37	\$1.62	\$1.77	\$2.10	\$0.68	\$0.60	\$0.61	\$0.63	\$2.52	\$2.82
EPS (as reported)	\$1.34	\$2.04	\$1.51	\$1.77	\$0.68	\$0.58	\$0.59	\$0.61	\$2.46	\$2.78
Weighted average shares outstanding (basic)	116.4	116.2	115.7	124.1	129.9	129.6	129.4	129.1	129.5	129.8
Weighted average shares outstanding (diluted)	118.0	117.9	117.8	127.9	133.0	132.9	132.8	132.7	132.9	133.0
MARGIN ANALYSIS:										
Gross profit	35.8%	34.7%	33.4%	35.1%	36.0%	35.3%	35.5%	35.3%	35.5%	35.8%
SG&A	20.3%	19.8%	18.6%	19.0%	18.9%	19.3%	19.2%	19.1%	19.1%	19.0%
EBITDA	15.4%	14.9%	14.8%	16.1%	17.1%	15.9%	16.3%	16.2%	16.3%	16.8%
Depreciation & amortization	2.8%	2.8%	2.7%	2.8%	2.9%	2.8%	2.9%	2.9%	2.9%	3.0%
Operating income	12.62%	12.1%	12.1%	13.2%	14.2%	13.1%	13.3%	13.3%	13.5%	13.8%
Tax rate	34.4%	34.0%	35.3%	29.9%	30.4%	30.0%	30.0%	30.0%	30.1%	30.0%
Net income	5.4%	6.1%	5.7%	7.1%	9.0%	7.7%	7.9%	7.8%	8.1%	8.4%
GROWTH RATES:										
Revenue		9.9%	12.1%	3.1%	8.4%	9.2%	9.9%	7.2%	8.7%	7.8%
Revenue (excl. foreign exchange effect)					8.4%	8.8%	8.5%	6.7%	8.1%	
Revenue (organic)					3.4%	4.9%	5.6%	6.7%	5.9%	7.8%
Product Development Revenue (as reported)		9.7%	11.9%	7.0%	9%	10%	10%	7%	9.0%	8.1%
I.H.S. Revenue (as reported)		10.6%	12.4%	-7.8%	6%	7%	9%	8%	7.6%	7.0%
Gross profit		7%	8%	8.4%	14.3%	11.3%	9.5%	4.9%	9.8%	8.6%
SG&A		7%	5%	5.5%	9.7%	12.2%	14.4%	1.8%	9.2%	7%
EBITDA		6%	11%	12.1%	19.9%	10.3%	4.3%	8.8%	10.6%	11%
Operating income		5%	12%	13.2%	20.2%	9.1%	3.2%	10.4%	11%	10%
Net income (excl. non-recurring items)		24%	4%	28.4%	57.8%	26.9%	11.1%	11.2%	25%	12%
EPS (excl. non-recurring items, incl. options)		18%	10%	18.2%	40.9%	20.8%	11.5%	11.4%	20%	12%

E=William Blair & Company, L.L.C. estimate

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DOW JONES: 16,580.84

S&P 500: 1,883.95

NASDAQ: 4,114.56



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