

# Quintiles Transnational Holdings Inc.

## Fourth-Quarter Analysis; Strong Market Commentary and IHS Recovery Underpin Impressive Guidance for 2014

### Conclusion

- Quintiles reported better-than-expected fourth-quarter results and 2014 guidance on Thursday, February 13. We believe the company's commentary on the robust RFP environment (the greatest value of outstanding work available in the last three years) should allow for strong bookings and improved revenue growth throughout 2014. Two consecutive quarters of much improved awards for the IHS segment should also allow that business to return to growth after declining in 2013. Following the strong results and guidance for 2014, we are increasing our 2014 EPS estimate by \$0.07, to \$2.40 (up 14%). We reiterate our Outperform rating on Quintiles given the robust demand trends in both product development and IHS and an attractive valuation relative to its peers.

### Model Changes

- For 2014, we now project revenue of \$4.11 billion, up \$81 million from our previous model and representing 7.9% growth (5.7% on an organic constant dollar basis). We now estimate operating margin of 13.5% (down from 13.9% previously) and EPS of \$2.40 (up 14% and \$0.07 above our prior \$2.33 target). In 2015, we project revenue growth of 7.9% (up from 7.8%), operating margin of 13.8% (down from 14.2% previously), and EPS of \$2.72 (up 14% and up \$0.03 from our previous model).
- The stand-out in the quarterly results, from our perspective, was the strong new business for both segments (1.24 times for product development and 1.46 times for IHS.). Given the company's size, we are impressed by its ability to consistently book more than \$1 billion of new business and deepen its relationships with clients (the company reported increasing the scope of its relationship with two key partners this quarter). As we move into 2014 and see these bookings translate into revenue, we believe burn rates remain consistent with recent levels, which would lead to revenue growth closer to the double-digit level absent the winding down of two large projects in 2013. These projects—which include the largest clinical trial ever managed by Quintiles—create a revenue growth headwind of 390 basis points this year. We project a book-to-bill ratio of 1.18 times in 2014 in both product development and IHS, although awards for IHS will likely be skewed to the second half of any given year. Thus we expect IHS's book-to-bill ratio to dip below 1.0 for the next one to two quarters, before rebounding again in the third quarter.

*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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February 13, 2014

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

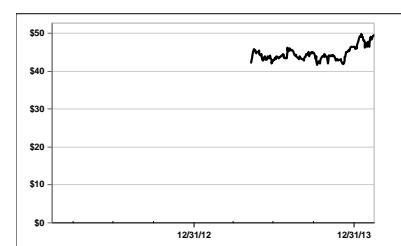
Symbol: Q (NYSE)  
Price: \$52.20 (52-Wk.: \$40-\$52)  
Market Value (mil.): \$6,374  
Fiscal Year End: December  
Long-Term EPS Growth Rate: 12%  
Dividend/Yield: None

	2012A	2013A	2014E
<b>Estimates</b>			
EPS FY	\$1.77	\$2.10	\$2.40
CY		\$2.10	\$2.40
<b>Valuation</b>			
FY P/E	29.5x	24.8x	21.8x
CY P/E		24.8x	21.8x

<b>Trading Data (FactSet)</b>	
Shares Outstanding (mil.)	129
Float (mil.)	42
Average Daily Volume	472,004

<b>Financial Data (FactSet)</b>	
Long-Term Debt/Total Capital (MRQ)	0.0
Book Value Per Share (MRQ)	-5.5
Enterprise Value (mil.)	8,021.8
EBITDA (TTM)	0.0
Enterprise Value/EBITDA (TTM)	0.0x
Return on Equity (TTM)	0.0

### Two-Year Price Performance Chart



Sources: FactSet, William Blair & Company estimates

## Stock Thoughts and Valuation

- During the day on Thursday, Quintiles traded at 21.8 times our updated 2014 EPS estimate of \$2.40, compared with its peer group of 23.2 times (24.6 times excluding Charles River [CRL \$58.80; Market Perform]). Given Quintiles's 6% discount relative to its peer group, we believe the stock is positioned to perform well during 2014. We believe the company's scale and lower risk profile justify a valuation more in line with or even slightly ahead of the group. We reiterate our Outperform rating on Quintiles as we believe that 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 below in exhibit 1, on the following page.

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

	2010	2011	2012	2013	Q1'14E	Q2'14E	Q3'14E	Q4'14E	2014E	2015E
Product Development Revenue	\$2,221.9	\$2,437.8	\$2,728.7	\$2,919.7	\$766.1	\$784.8	\$782.6	\$843.1	\$3,176.6	\$3,433.9
I.H.S. Revenue	\$774.8	\$857.1	\$963.7	\$888.6	\$227.4	\$230.7	\$233.3	\$241.1	\$932.5	\$997.8
Net revenue	\$2,996.8	\$3,294.9	\$3,692.4	\$3,808.3	\$993.5	\$1,015.4	\$1,015.9	\$1,084.2	\$4,109.1	\$4,431.7
Total Cost of revenue	1,925.0	\$2,153.0	\$2,459.4	\$2,471.4	\$641.8	\$657.2	\$652.2	\$699.8	\$2,651.1	\$2,846.7
Gross profit	1,071.8	\$1,142.0	\$1,233.0	\$1,336.9	\$351.7	\$358.2	\$363.7	\$384.4	\$1,458.0	\$1,585.0
Selling, general and administrative expense	608.9	\$651.7	\$687.3	\$725.3	\$190.2	\$196.1	\$191.5	\$207.6	\$785.4	\$840.9
EBITDA	462.9	\$490.3	\$545.7	\$611.6	\$161.5	\$162.1	\$172.2	\$176.8	\$672.6	\$744.0
Depreciation and amortization expense	84.6	\$91.9	\$100.3	\$107.5	\$27.2	\$28.9	\$29.7	\$31.3	\$117.2	\$134.4
Operating income (including options beg Q105)	378.3	\$398.4	\$445.4	\$504.1	\$134.3	\$133.2	\$142.5	\$145.5	\$555.4	\$609.6
Interest and other income (expense), net	(133.4)	(\$102.8)	(\$127.8)	(\$119.4)	(25.00)	(24.81)	(24.81)	(24.81)	(\$99.4)	(\$91.8)
Pretax income	245	\$295.6	\$317.6	\$384.7	109.27	108.40	117.66	120.65	\$456.0	\$517.9
Income tax expense	84.2	\$100.4	\$112.0	\$115.2	32.78	32.52	35.30	36.19	\$136.8	\$155.4
Equity investee earnings	1.11	(\$4.2)	\$3.0	(\$1.3)	(1.70)	0.48	0.37	(0.47)	(\$1.3)	(\$1.4)
Loss/(income) from Noncontrolling interests/minority interest	0.000	1.400	0.900	0.867	0.25	0.25	0.30	0.30	1.100	1.100
Net income (non-GAAP)	\$161.8	\$191.0	\$208.6	\$268.2	\$74.8	\$76.4	\$82.7	\$84.0	\$317.9	\$361.1
Nonrecurring items	(5.2)	(36.3)	(50.3)	(61.6)	(3.3)	(3.3)	(3.3)	(3.3)	(13.0)	(6.0)
Tax adjustment	1.8	87.1	18.9	19.2	1.0	1.0	1.0	1.0	3.9	2.0
Non controlling interest		(1.4)	(0.9)	(0.6)	(0.3)	(0.3)	(0.3)	(0.3)	(1.1)	(1.1)
Nonrecurring items (net of tax)	(3.4)	49.4	(32.3)	(42.9)	(2.5)	(2.5)	(2.6)	(2.6)	(10.2)	(5.1)
Net income (GAAP)	\$158	\$240.4	\$174.8	\$226.0	\$72.3	\$73.8	\$80.2	\$81.4	\$307.7	\$356.0
EPS (excl. nonrecurring items, incl. options beg Q105, diluted)	\$1.37	\$1.62	\$1.76	\$2.10	\$0.56	\$0.58	\$0.62	\$0.63	\$2.40	\$2.72
EPS (as reported)	\$1.34	\$2.04	\$1.48	\$1.76	\$0.54	\$0.56	\$0.60	\$0.61	\$2.32	\$2.68
Weighted average shares outstanding (basic)	116.4	116.2	115.7	124.1	128.9	128.6	128.4	128.1	128.5	128.8
Weighted average shares outstanding (diluted)	118.0	117.9	117.8	127.9	132.8	132.7	132.6	132.5	132.7	132.8
<b>MARGIN ANALYSIS:</b>										
Gross profit	35.8%	34.7%	33.4%	35.1%	35.4%	35.3%	35.8%	35.5%	35.5%	35.8%
SG&A	20.3%	19.8%	18.6%	19.0%	19.1%	19.3%	18.9%	19.1%	19.1%	19.0%
EBITDA	15.4%	14.9%	14.8%	16.1%	16.3%	16.0%	16.9%	16.3%	16.4%	16.8%
Depreciation & amortization	2.8%	2.8%	2.7%	2.8%	2.7%	2.8%	2.9%	2.9%	2.9%	3.0%
Operating income	12.62%	12.1%	12.1%	13.2%	13.5%	13.1%	14.0%	13.4%	13.5%	13.8%
Tax rate	34.4%	34.0%	35.3%	29.9%	30.0%	30.0%	30.0%	30.0%	30.0%	30.0%
Net income	5.4%	5.8%	5.6%	7.0%	7.5%	7.5%	8.1%	7.7%	7.7%	8.1%
<b>GROWTH RATES:</b>										
Revenue		9.9%	12.1%	3.1%	7.1%	7.5%	8.9%	8.0%	7.9%	7.9%
Revenue (excl. foreign exchange effect)				3.8%	7.2%	7.6%	8.0%	8.1%	7.8%	
Revenue (organic)				3.4%	4.0%	4.5%	5.9%	8.1%	5.7%	7.9%
Product Development Revenue (as reported)		9.7%	11.9%	7.0%	8%	8%	10%	9%	8.8%	8.1%
I.H.S. Revenue (as reported)		10.6%	12.4%	-7.8%	3%	5%	7%	5%	4.9%	7.0%
Gross profit		7%	8%	8.4%	11.2%	9.7%	9.5%	6.2%	9.1%	8.7%
SG&A		7%	5%	5.5%	9.8%	10.5%	11.2%	2.7%	8.3%	7%
EBITDA		6%	11%	12.1%	12.9%	8.8%	7.7%	10.7%	10.0%	11%
Operating income		5%	12%	13.2%	13.4%	7.3%	7.6%	12.6%	10%	10%
Net income (excl. non-recurring items)		18%	9%	28.6%	29.8%	21.4%	15.0%	9.8%	19%	14%
EPS (excl. non-recurring items, incl. options)		18%	9%	19.3%	16.1%	15.8%	15.6%	10.2%	14%	14%

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

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DOW JONES: 15,963.94

S&P 500: 1,819.26

NASDAQ: 4,201.29



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Underperform (Sell)	1	Underperform (Sell)	0

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