

Equity Research

Quintiles Transnational Holdings, Inc.

Q: Q1 2014 Earnings First Look

- **Bottom line.** Quintiles reported a strong quarter, beating revenue, EPS, and bookings estimates and raising 2014 guidance. The revenue beat was attributable to slightly better-than-expected performance in both segments. The strong EPS beat was mostly due to very strong margin performance in the PDEV segment, though we caution that most of the outperformance appears to be due to FX. Much like its CRO peers, Quintiles could face the risk of some disruption from large pharma M&A (Quintiles is AstraZeneca's preferred partner for Phase 1), which could overshadow some of the strong operational performance.
- **Revenue.** \$1,005MM vs. \$1,001MM (Wells Fargo) and \$997MM (consensus).
- **EPS.** \$0.68 vs. \$0.57 (Wells Fargo) and \$0.55 (consensus). A gain on sales of marketing securities contributed ~\$0.03.
- **Operating margin.** 14.2% vs. 13.4% (Wells Fargo) and 13.1% (consensus).
- **Segments.** PDEV revenue of \$771MM vs. \$773MM (Wells Fargo) and \$767MM (consensus). PDEV operating margin of 20.8% vs. 19.4% (Wells Fargo) and 19.2% (consensus). IHS revenue of \$234MM vs. \$228MM (Wells Fargo) and \$231MM (consensus). IHS operating margin of 3.8% vs. 5.6% (Wells Fargo) and 5.2% (consensus). Corporate overhead was 2.7% of revenue versus our expectation of 2.9%.
- **Bookings.** Book-to-bill of 1.27 vs. 1.21 (Wells Fargo). Net bookings were \$1,274B vs. \$1,215B (Wells Fargo) and \$1,190 (consensus). PDEV book-to-bill was 1.30, while IHS book-to-bill was 1.15.
- **2014 Guidance.** Raised 2014 EPS guidance to \$2.45-2.58 from \$2.33-2.46 previously. Raised 2014 revenue guidance to \$4.13-4.19B from \$4.09-4.15B previously. Current 2014 consensus stands at EPS of \$2.42 on revenue of \$4.20B.
- **Conference call.** 8:00 a.m. ET. 855.484.7367.

Valuation Range: \$56.00 to \$60.00

Our valuation range is DCF-based (WACC = 8.0%; terminal NOPLAT growth = 2%) and represents 24x our 2014 EPS estimate. Risks include: (1) project cancellations or delays due to client M&A, economic weakness, pipeline reprioritization, or compound failure; (2) a reversal in the trend toward increased outsourcing; (3) lack of improvement in the IHS segment; (4) margin pressure from strategic relationships; (5) foreign exchange volatility; and (6) large insider ownership.

Investment Thesis:

We believe Quintiles is a leader in several capacities (size, operational efficiency, strategic savvy) in a secular growth industry, creating a favorable risk/reward profile for long-term holders.

Outperform / V

Sector: Pharmaceutical Services

Market Weight

Earnings Reported - First Look

	2013A	2014E	2015E	
EPS		Curr. Prior	Curr. Prior	
Q1 (Mar.)	\$0.49	\$0.68 A 0.57	\$0.65	NC
Q2 (June)	0.50	0.59 NC	0.67	NC
Q3 (Sep.)	0.54	0.61 NC	0.68	NC
Q4 (Dec.)	0.58	0.61 NC	0.69	NC
FY	\$2.10	\$2.39 NC	\$2.68	NC
CY	\$2.10	\$2.39	\$2.68	
FY P/E	22.4x	19.7x	17.6x	
Rev.(MM)	\$3,808	\$4,123	\$4,418	

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters
 NA = Not Available, NC = No Change, NE = No Estimate, NM = Not Meaningful
 V = Volatile, * = Company is on the Priority Stock List

Ticker	Q
Price (04/30/2014)	\$47.13
52-Week Range:	\$40-55
Shares Outstanding: (MM)	128.9
Market Cap.: (MM)	\$6,075.1
S&P 500:	1,883.95
Avg. Daily Vol.:	620,896
Dividend/Yield:	\$0.00/0.0%
LT Debt: (MM)	\$2,046.0
LT Debt/Total Cap.:	NM
ROE:	NM
3-5 Yr. Est. Growth Rate:	11.0%
CY 2014 Est. P/E-to-Growth:	1.8x
Last Reporting Date:	05/01/2014

Source: Company Data, Wells Fargo Securities, LLC estimates, and Reuters

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Please see page 3 for rating definitions, important disclosures and required analyst certifications

All estimates/forecasts are as of 05/01/14 unless otherwise stated.

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Together we'll go far



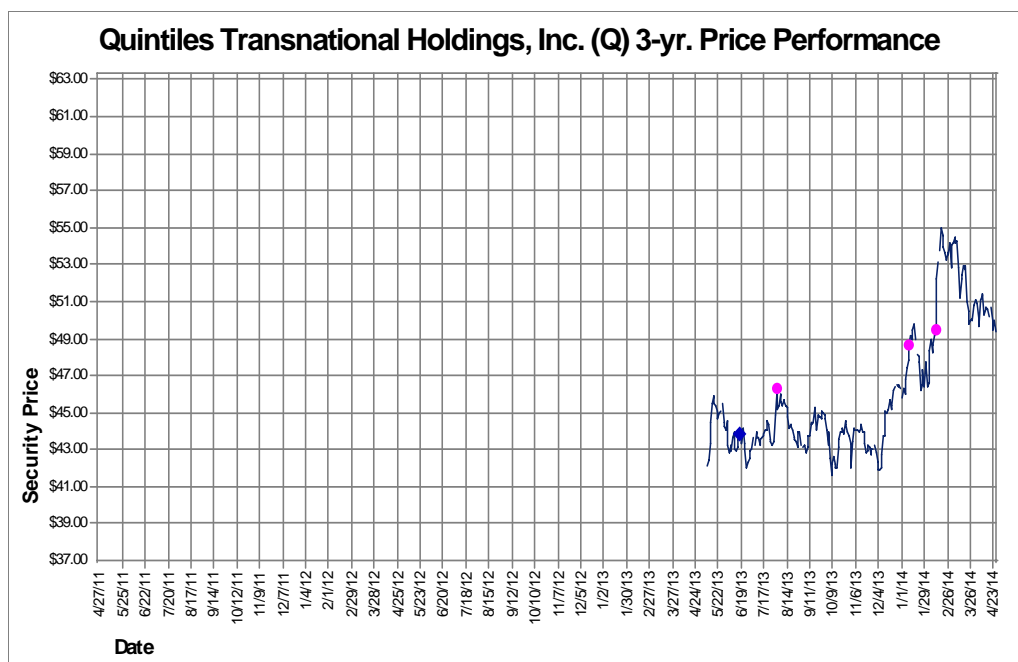
Company Description:

Based in Durham, North Carolina, Quintiles Transnational Holdings, Inc. is the largest contract research organization by revenue, providing both clinical trial management services and contract sales services to pharmaceutical and biotechnology clients. The company operates in two segments: Product Development (PDEV) and Integrated Health Services (IHS). PDEV provides a range of clinical trial services including study design, investigator recruitment, site start-up, patient recruitment, clinical monitoring, project management, phase I, bioanalytical services, biostatistics, central lab, genomics services, strategic planning, and a range of consulting services. The vast majority of the IHS business consists of contract sales and related commercial services, but the segment also contains peri-approval clinical trial services as well as services provided to payers and healthcare providers. In addition to being the industry's largest CRO, Quintiles is differentiated from peers by its exposure to the contract sales business.

FY ending December In millions except EPS	Actual		Est	Actual	Cons	Yr / Yr	Seq
	Q1 2013	Q4 2013	Q1 2014	Q1 2014	Q1 2014	change	change
Total revenue	927	\$ 1,004	\$ 1,001	\$ 1,005	\$ 997	8.4%	0.1%
Cost of products and services	611	642	644	644		5.3%	0.3%
Gross profit	316	362	357	362		14.3%	(0.1%)
Selling, general & administrative	198	233	224	219		10.7%	(5.8%)
Operating income	118	129	134	142	131	20.2%	10.2%
Interest expense (income)	36	25	24	23		(34.1%)	(7.1%)
Other expense (income)	(2)	(2)	-	(5)			
Pretax income	85	106	109	124		45.3%	17.3%
Taxes	26	30	33	38		44.8%	27.3%
Income before equity earnings	59	76	76	86		45.5%	13.4%
Equity earnings	(2)	0	-	5			
Net income (continuing ops)	57	76	76	91		58.3%	19.1%
Noncont. interests income (loss)	0	0	-	0			
NI to common	\$ 58	\$ 76	\$ 76	\$ 91		57.8%	18.9%
Non-GAAP EPS	\$ 0.49	\$0.58	\$0.57	\$ 0.68	\$ 0.55	40.9%	18.8%
Diluted shares outstanding	119	133	133	133		12.0%	0.1%
EBITDA	\$ 143	\$ 160	\$ 162	\$ 171		19.9%	7.3%
MARGIN ANALYSIS						Yr / Yr	Seq
Cost of sales / net revenue	65.9%	63.9%	64.3%	64.0%		(190) bps	10 bps
Gross margin	34.1%	36.1%	35.7%	36.0%		190 bps	(10) bps
SG&A / net revenue	21.3%	23.2%	22.3%	21.8%		50 bps	(140) bps
EBIT margin	12.8%	12.9%	13.4%	14.2%	13.1%	140 bps	130 bps
Pretax margin	9.2%	10.5%	10.9%	12.3%		310 bps	180 bps
Tax rate	30.5%	28.0%	30.0%	30.4%		(10) bps	240 bps
Net margin from continuing ops	6.2%	7.6%	7.6%	9.0%		280 bps	140 bps
EBITDA margin	15.4%	15.9%	16.1%	17.1%		160 bps	110 bps
SEGMENT ANALYSIS						Yr / Yr	Seq
PDEV Segment Revenue	\$ 706	\$ 775	\$ 773	\$ 771	\$ 767	9.1%	(0.5%)
Growth: core	7.8%	6.1%	5.0%	5.1%			
Growth: FX	(1.0%)	(0.4%)	(0.1%)	(0.5%)			
Growth: acq/div/other	0.9%	4.6%	4.5%	4.5%			
Revenue growth: total	7.6%	10.2%	9.4%	9.1%			
Gross profit	\$ 277	\$ 319	313	\$ 320		15.5%	0.4%
Gross margin	39.3%	41.2%	40.5%	41.6%		230 bps	40 bps
Operating income	\$ 133	\$ 153	\$ 150	\$ 161	\$ 147	21.1%	5.1%
Operating margin	18.8%	19.7%	19.4%	20.8%	19.2%	210 bps	110 bps
IHS Segment Revenue	\$ 221	\$ 229	\$ 228	\$ 234	\$ 231	6.0%	2.4%
Growth: core	(0.3%)	(1.0%)	4.0%	7.9%			
Growth: FX	(4.2%)	(4.7%)	(0.7%)	(1.9%)			
Growth: acq/div/other	0.0%	0.0%	0.0%	0.0%			
Revenue growth: total	(4.6%)	(5.7%)	3.3%	6.0%			
Gross profit	\$ 39	\$ 43	\$ 44	\$ 41		5.6%	(3.6%)
Gross margin	17.6%	18.7%	19.4%	17.6%		(10) bps	(110) bps
Operating income	\$ 6	\$ 12	\$ 13	\$ 9	\$ 12	44.1%	(23.1%)
Operating margin	2.8%	5.1%	5.6%	3.8%	5.2%	100 bps	(130) bps
Consolidated Revenue	\$ 927	\$ 1,004	\$ 1,001	\$ 1,005	\$ 997	8.4%	0.1%
Growth: core	5.7%	4.3%	4.8%	4.9%			
Growth: FX	(1.9%)	(1.5%)	(0.3%)	0.0%			
Growth: acq/div/other	0.6%	3.4%	3.5%	3.5%			
Revenue growth: total	4.4%	6.2%	7.9%	8.4%			
Corp. overhead, non-GAAP	\$ (22)	\$ (35)	\$ (29)	\$ (27)		24.8%	(22.8%)
% of total revenue	(2.4%)	(3.5%)	(2.9%)	(2.7%)		40 bps	(80) bps
BOOKINGS & BACKLOG						Yr / Yr	Seq
Ending backlog	\$ 9,000	\$ 9,855	\$ 10,069	\$ 10,100	\$ 1,004	12.2%	2.5%
PDEV net bookings	\$ 1,075	\$ 964	\$ 968	\$ 1,005		(6.5%)	4.3%
IHS net bookings	\$ 170	\$ 335	\$ 247	\$ 269		57.9%	(19.7%)
Total net bookings	\$ 1,246	\$ 1,299	\$ 1,215	\$ 1,274	\$ 1,190	2.3%	(1.9%)
PDEV book-to-bill	1.52	1.24	1.25	1.30			
IHS book-to-bill	0.77	1.46	1.08	1.15			
Total net book-to-bill	1.34	1.29	1.21	1.27	1.19		

Source: FactSet (consensus); Company data; Wells Fargo Securities, LLC estimates

Required Disclosures



	Date	Publication Price (\$)	Rating Code	Val. Rng. Low	Val. Rng. High	Close Price (\$)
	6/18/2013		Evans			
◆	6/18/2013	43.53	1	48.00	50.00	43.89
▲	8/1/2013	46.29	1	50.00	52.00	46.29
●	1/10/2014	47.84	1	52.00	54.00	48.61
■	2/12/2014	51.55	1	56.00	60.00	49.44

Source: Wells Fargo Securities, LLC estimates and Reuters data

Symbol Key

▼ Rating Downgrade

▲ Rating Upgrade

● Valuation Range Change

◆ Initiation, Resumption, Drop or Suspend

■ Analyst Change

□ Split Adjustment

Rating Code Key

1 Outperform/Buy

2 Market Perform/Hold

3 Underperform/Sell

SR Suspended

NR Not Rated

NE No Estimate

Additional Information Available Upon Request

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2=Market Perform: The stock appears appropriately valued, and we believe the stock's total return will be in line with the market over the next 12 months. HOLD

3=Underperform: The stock appears overvalued, and we believe the stock's total return will be below the market over the next 12 months. SELL

SECTOR RATING

O=Overweight: Industry expected to outperform the relevant broad market benchmark over the next 12 months.

M=Market Weight: Industry expected to perform in-line with the relevant broad market benchmark over the next 12 months.

U=Underweight: Industry expected to underperform the relevant broad market benchmark over the next 12 months.

VOLATILITY RATING

V = A stock is defined as volatile if the stock price has fluctuated by +/-20% or greater in at least 8 of the past 24 months or if the analyst expects significant volatility. All IPO stocks are automatically rated volatile within the first 24 months of trading.

As of: May 1, 2014

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