

PRA Health Sciences, Inc.

PRAH: Raising Numbers on Strong 2Q15 Bookings and Ongoing Efficiency Gains

We reiterate our **Sector Weight** rating on PRA Health Sciences, Inc. (PRAH) on valuation with the stock up 130% since its successful late-2014 IPO (vs. S&P up 3%) and now trading at a premium multiple of 13.0x our upwardly revised 2016 EBITDA estimate (peer group: 12.6x). Also, elevated balance sheet debt (~4.5x EBITDA) may relatively limit the Company's strategic flexibility vs. the other publicly traded CROs. A refinancing might help improve PRAH's investment profile given the low interest rate environment and elevated equity valuations, in our opinion.

Key Investment Points

We are increasing our forward model estimates for revenues, adjusted EBITDA and adjusted EPS based on strong 2Q15 results. Specifically, PRAH generated net bookings of \$408M, calculating to a net book-to-bill of 1.21x. This is particularly impressive given PRAH's large functional outsourcing business, for which mgmt only books NTM revenue. Adjusted EPS totaled \$0.47, above consensus of \$0.40, inclusive of a ~\$0.05 YOY currency benefit on gross margins. SG&A expenses were also lower than expected at \$59M (KBCM: \$63M) due to ongoing efficiency gains and modest synergies from prior acquisitions.

Looking ahead, we model revenues of **\$1.383B at the high end of mgmt's guidance range of \$1.34B-\$1.39B (~10.5% constant currency organic)**. Our outlook for 2H15 is well supported by \$2.262B of backlog at the end of June, which should also support double-digit growth through 1H16 as well. RFP volumes remain at record levels, and the mix of programmatic and functional projects in backlog has remained stable. Mgmt referenced some early cross-selling interest from clients across the legacy PRA and RPS services, but revenue impact to date still appears to be limited.

PRAH formally launched its **Predictivv informatics platform in June**, with an initial focus on internal efficiencies. The first client-facing application (*Predictivv Connect*) is about to be piloted on its first clinical study. Over time, mgmt will be launching applications in site selection, patient enrollment and investigator engagement.

The major risk for PRAH remains its **elevated indebtedness**. PRAH paid down ~\$15M of bank debt in 2Q15. However, the Company remains the most financially leveraged CRO with a debt ratio (net debt-to-EBITDA) of 4.5x. We anticipate no near-term liquidity issues given its strong cash flow profile and the structure of its loan agreements (e.g., no principal payments until 2020). Nonetheless, from a relative strategic standpoint, PRA may have less financial flexibility than other publicly traded CROs.

Estimates

FY ends 12/31	F2014A	1Q15A	2Q15A	3Q15E	4Q15E	F2015E	F2016E
EPS (Net)	\$1.26	\$0.41	\$0.47	\$0.47	\$0.49	\$1.84	\$2.19
Cons. EPS	--	\$0.41	\$0.40	\$0.43	\$0.43	\$1.73	\$2.03
Previous	--	--	\$0.40	\$0.43	\$0.44	\$1.69	\$1.99
Valuation							
P/E	33.1x	--	--	--	--	22.7x	19.1x

Sources: Company reports, FactSet, KeyBanc Capital Markets Inc.

For analyst certification and important disclosures, please refer to the Disclosure Appendix.

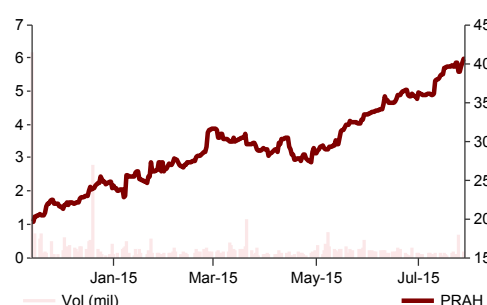
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NASDAQ: PRAH

Rating: **Sector Weight**
Price Target: **NA**
Price: **\$41.74**



Sources: Company reports, FactSet, KeyBanc Capital Markets Inc.

Company Data

52-week range	\$18 - \$41
Market Cap. (M)	\$2,620.4
Shares Out. (M)	62.78
Enterprise Value (M)	\$3,490.2
Avg. Daily Volume (30D)	152,913.0
SI as % of Float	6.9%
SI % Chg. from Last Per.	109.8%

Sources: Company reports, FactSet, KeyBanc Capital Markets Inc.

Valuation

PRAH's current trading price implies a 13.0x multiple on our 2016 adjusted EBITDA estimate of \$271M [consensus (pre 2Q15): \$249M], which is roughly in line with the CRO group average (12.6x). We believe PRAH is nicely set up for ~10% growth in the near/mid-term. However, elevated indebtedness may limit the Company's strategic flexibility with regard to acquisitions and reinvestments.

Investment Risks

PRAH operates in a competitive industry against other providers that have similar services. Also, the Company's ability to generate revenue and earnings growth is contingent on trends in global biopharmaceutical R&D spending and the propensity of biopharmaceutical firms to outsource R&D and sales activities to third parties. Finally, PRAH has an elevated level of indebtedness, so it is important for the Company to reduce debt.

PRAH is, by far, the most financially leveraged CRO with a debt ratio (net debt-to-EBITDA) of 4.5x. This is almost six times the average of its publicly traded, late-stage CRO peers at 0.8x. We anticipate no liquidity issues given the Company's strong cash flow and the structure of its loan agreements, including no principal payments until 2020 and loose covenants (in our view). Nonetheless, from a relative strategic standpoint, mgmt will have limited financial flexibility for opportunistic acquisitions and/or reinvestment projects in the business.

FINANCIAL MODELS

Figure 1: Projected Income Statements

PRAH -- GAAP Income Statement (in millions)	Fiscal Year End, December 2014					Fiscal Year End, December 2015					2015E	2016E
	2013A	1QA	2QA	3QA	4QA	2014A	1QA	2QA	3QE	4QE		
Net Service Revenues	832.9	311.4	311.4	320.1	323.8	1,266.6	332.0	336.5	355.3	359.4	1,383.1	1,510.7
Reimbursement Revenues	158.4	43.4	46.1	57.3	46.2	193.0	56.6	56.3	58.6	58.1	229.6	249.1
Total Revenues	\$991.3	\$354.7	\$357.5	\$377.3	\$370.0	\$1,459.6	\$388.6	\$392.8	\$413.9	\$417.4	\$1,612.7	\$1,759.8
Y-O-Y Growth %	39.5%	87.0%	73.5%	70.1%	8.4%	52.1%	6.6%	8.1%	11.0%	11.0%	9.2%	9.2%
less: Direct Costs	(526.9)	(215.2)	(213.2)	(215.6)	(214.9)	(859.2)	(219.0)	(219.9)	(233.4)	(235.7)	(908.0)	(988.0)
less: Reimbursement Revenues	(158.4)	(43.4)	(46.1)	(57.3)	(46.2)	(193.0)	(56.6)	(56.3)	(58.6)	(58.1)	(229.6)	(249.1)
Gross Income	\$306.0	\$96.2	\$98.2	\$104.5	\$108.8	\$407.4	\$113.0	\$116.6	\$121.9	\$123.6	\$475.1	\$522.7
Gross Margin, % of service revenue	36.7%	30.9%	31.5%	32.6%	33.6%	32.2%	34.0%	34.7%	34.3%	34.4%	34.4%	34.6%
less: Selling, General, and Admin.	(212.6)	(60.8)	(56.2)	(63.6)	(73.7)	(254.0)	(60.8)	(58.9)	(62.2)	(62.2)	(244.1)	(256.8)
less: Depreciation and Amortization	(50.5)	(24.6)	(24.6)	(23.9)	(23.4)	(96.6)	(19.2)	(19.2)	(19.8)	(19.9)	(78.2)	(83.2)
less: Other	(76.9)	-	-	(0.0)	0.0	(0.0)	-	(0.2)	-	-	(0.2)	-
Operating Income	(\$34.0)	\$10.7	\$17.4	\$17.0	\$11.7	\$56.8	\$32.9	\$38.3	\$39.9	\$41.6	\$152.7	\$182.7
plus: Interest Income (Expense)	(56.4)	(21.8)	(20.8)	(21.0)	(18.3)	(81.9)	(15.4)	(15.4)	(15.4)	(15.3)	(61.5)	(57.6)
plus: FX Gains (Losses)	(7.8)	(3.7)	(5.4)	10.7	9.0	10.5	9.1	(4.0)	-	-	5.1	-
plus: Other, Net	(28.2)	(1.4)	(0.1)	(0.1)	(25.7)	(27.3)	(0.5)	(0.1)	(0.1)	(0.1)	(0.8)	-
Pretax Income	(126.4)	(16.2)	(8.9)	6.5	(23.3)	(41.9)	26.1	18.8	24.4	26.2	95.5	125.1
less: Provision For Taxes	39.3	6.3	5.2	(4.9)	1.5	8.2	(8.0)	(5.6)	(7.3)	(7.9)	(28.8)	(36.3)
Net Income Before Unconsolidated Equ	(87.1)	(9.9)	(3.7)	1.6	(21.8)	(33.7)	18.1	13.2	17.1	18.3	66.7	88.8
plus: Gains From Unconsolidated JV	(1.2)	(0.2)	(0.4)	(0.5)	(1.0)	(2.0)	(0.9)	(0.8)	(0.8)	(0.8)	(3.4)	-
Net Income	(88.3)	(10.0)	(4.1)	1.2	(22.8)	(35.7)	17.2	12.4	16.2	17.5	63.4	88.8
Diluted EPS (GAAP)	(\$2.23)	(\$0.25)	(\$0.10)	\$0.03	(\$0.45)	(\$0.83)	\$0.27	\$0.20	\$0.26	\$0.28	\$1.01	\$1.41
Diluted Share Count	39.6	40.3	40.6	39.2	50.7	42.9	62.8	63.0	63.0	63.0	62.9	63.0
Non-GAAP Metrics												
Net Revenues	\$832.9	\$311.4	\$311.4	\$320.1	\$323.8	\$1,266.6	\$332.0	\$336.5	\$355.3	\$359.4	\$1,383.1	\$1,510.7
Year-Over-Year Growth (%)	39.5%	87.0%	73.5%	70.1%	8.4%	52.1%	6.6%	8.1%	11.0%	11.0%	9.2%	9.2%
Adjusted EBITDA	\$130.6	\$39.7	\$45.5	\$47.0	\$50.6	\$182.8	\$55.7	\$61.3	\$61.8	\$63.6	\$242.4	\$271.5
Adjusted EBITDA Margin	15.7%	12.8%	14.6%	14.7%	15.6%	14.4%	16.8%	18.2%	17.4%	17.7%	17.5%	18.0%
Adjusted Earnings Per Share	\$0.61	\$0.22	n/a	n/a	\$0.35	\$1.26	\$0.41	\$0.47	\$0.47	\$0.49	\$1.84	\$2.19
Year-Over-Year Growth (%)	-21.3%	n/a	n/a	n/a	30.0%	105.6%	85.9%	n/a	n/a	38.6%	45.7%	18.9%

Source: Company reports and KeyBanc Capital Markets Inc.

Disclosure Appendix

PRA Health Sciences, Inc. - PRAH

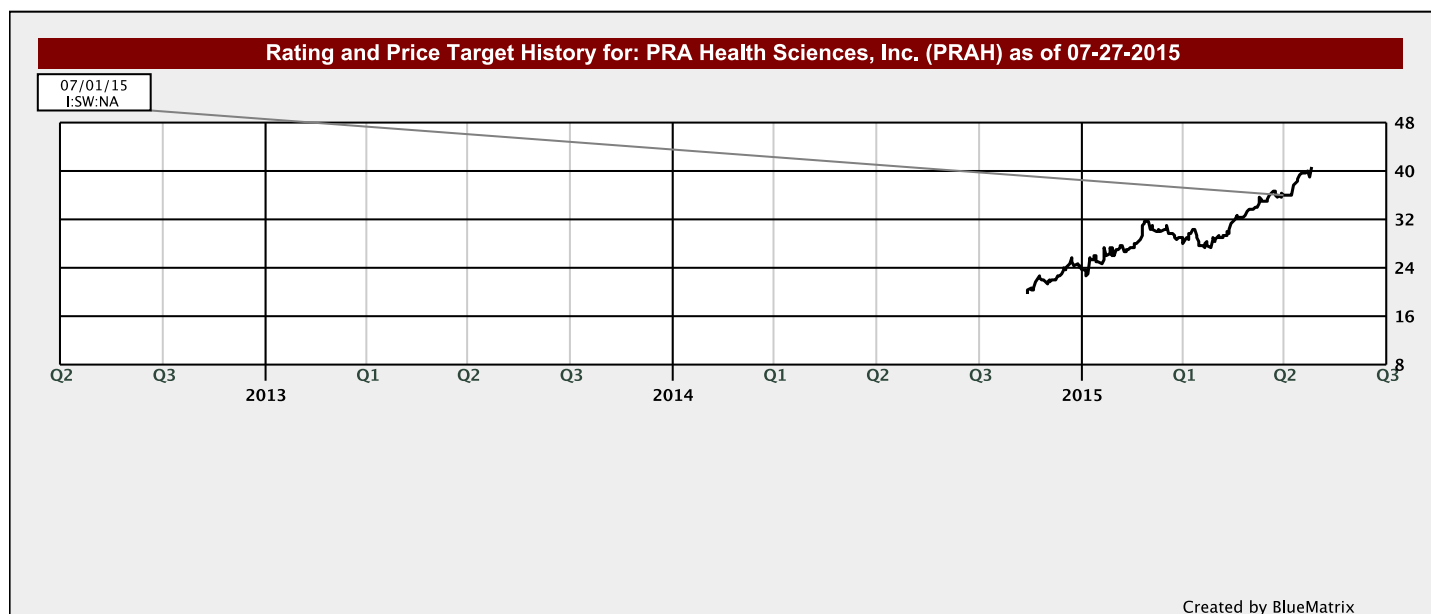
We expect to receive or intend to seek compensation for investment banking services from PRA Health Sciences, Inc. within the next three months.

As of the date of this report, we make a market in PRA Health Sciences, Inc..

Reg A/C Certification

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Three-Year Rating and Price Target History



Rating Disclosures

Distribution of Ratings/IB Services Firmwide and by Sector									
KeyBanc Capital Markets					HEALTHCARE				
Rating	Count	Percent	IB Serv/Past 12 Mos.		Rating	Count	Percent	IB Serv/Past 12 Mos.	
			Count	Percent				Count	Percent
Overweight [OW]	357	45.83	84	23.53	Overweight [OW]	19	44.19	3	15.79
Sector Weight [SW]	406	52.12	66	16.26	Sector Weight [SW]	22	51.16	5	22.73
Underweight [UW]	16	2.05	0	0.00	Underweight [UW]	2	4.65	0	0.00

Disclosure Appendix (cont'd)

Rating System

Overweight - We expect the stock to outperform the analyst's coverage sector over the coming 6-12 months.

Sector Weight - We expect the stock to perform in line with the analyst's coverage sector over the coming 6-12 months.

Underweight - We expect the stock to underperform the analyst's coverage sector over the coming 6-12 months.

Note: KeyBanc Capital Markets changed its rating system after market close on February 27, 2015. The previous ratings were Buy, Hold and Underweight. Additionally, Pacific Crest Securities changed its rating system to match KeyBanc Capital Markets' rating system after market close on April 10, 2015, in conjunction with the merger of the broker dealers. The previous ratings were Outperform, Sector Perform and Underperform.

Other Disclosures

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