

PRA Health Sciences (PRAH) Playing Out as Expected...Positively

BUY

Price target \$46.00

Price \$40.61

Key Takeaway

From the IPO, we believed that '15 EPS could exceed our model, driven by margin. We are satisfied to see that playing out as expected. If not for FX headwind, revenue would outpace expectations as well. With bookings topping estimates for the 3 quarters since the IPO, revenue growth acceleration into 2016 seems realistic, as well. With PRAH up 40% just since the 1Q15 report (R2000 flat), we expect no better than a modest positive reaction to these results.

Solid Bookings, Remember 1.21x is Better than it Looks. PRAH now has exceeded our bookings estimate for 4Q14 (first reported Q after IPO) through 2Q15 by \$6-8M. The 1.21x book-to-bill is a solid result, and slightly better than a similar number from peers. Because management is booking Strategic Solutions on a rolling 4Q basis (add the quarter 1 year out, drop the quarter just reported), that segment tends to run about 1.05-1.1x. Thus, the other ~65% of the business generated a ~1.28x book-to-bill by our calculation.

Margin Ramping Quickly, Certainly Some FX Help. For the third consecutive quarter, EBITDA margin improved solidly. In 2Q, adjusted EBITDA margin increased 120 bps sequentially and ~350 YoY. Improving operating profitability is a minor contributor to that, but FX has been a major contributor. PRAH's higher cost exposure than revenue exposure to foreign currencies (primarily USD/EUR) is the widest spread among our covered CROs. Similar to ICLR in 1Q, PRAH has reached beyond the midpoint of its LT margin guidance range with the help of FX. We believe further operational improvements are available. Structural factors (QE in Europe, rate lift-off in the US) suggest that the strong dollar is unlikely to reverse, though a reversal clearly would be a risk to PRAH's margin performance.

Only Ding, Debt Extinguishment is Slow. Management had committed to paying down \$25M/quarter in debt post-IPO. So far, the pace has been \$15M/quarter. DSOs are inching up sequentially. Some of that is seasonality, and some is related to maturing relationships with larger customers (who are less willing to underwrite their vendors' working capital...industry trend). That could be causing management to walk the debt balance down more slowly. Nonetheless, the leverage ratio is actually dropping faster than anticipated because of the outperformance on EBITDA.

On the Call, Look for... 1) Client concentration metrics; 2) Mix of wins between large and SMID clients, and programmatic vs. Strategic Solutions business (might give indicators, but not hard numbers); 3) Sustainability of margin improvement; 4) Duration of backlog, and backlog coverage, and 5) Timing of data/IT initiative roll-out and anticipated impact.

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Chart 1: Summary of PRA's Results

PRA Health Sciences (PRAH)

2Q15 Earnings Summary

Sources: Company filings and Jefferies LLC

Reports 7/27/2015 AMC

FY ending December 31 in thousands except EPS	Reported		Estimate	Actual	Consensus	Percentage Change		Difference		
	2Q14	1Q15	2Q15	2Q15	2Q15	Seq	Y/Y	Seq	Y/Y	Est.
Net revenue	\$311,423	\$ 331,968	\$334,116	\$ 336,518	\$ 336,700	1.4%	8.1%	\$ 4,550	\$ 25,095	\$ 2,402
Direct costs	213,378	218,961	221,576	219,877		0.4%	3.0%	916	6,499	(1,699)
SG&A	53,758	58,686	58,010	57,489		(2.0%)	6.9%	(1,197)	3,731	(521)
FOREX	5,387	(9,066)	-	3,966		<u>(143.7%)</u>	<u>(26.4%)</u>	<u>13,032</u>	<u>(1,421)</u>	<u>3,966</u>
Adj EBITDA	38,900	63,387	54,530	55,186	55,400	(12.9%)	41.9%	(8,201)	16,286	656
Depreciation	4,910	5,128	5,325	5,085		<u>(0.8%)</u>	<u>3.6%</u>	<u>(43)</u>	<u>175</u>	<u>(240)</u>
Total expenses	277,433	273,709	284,911	286,417		4.6%	3.2%	12,708	8,984	1,506
Adj EBITA	33,990	58,259	49,205	50,101		(14.0%)	47.4%	(8,158)	16,111	896
Interest income (expense)	(19,359)	(13,744)	(13,541)	(13,779)		0.3%	(28.8%)	(35)	5,580	(238)
Other income (expense)	(116)	(464)	-	(96)		<u>(79.3%)</u>	<u>(17.2%)</u>	<u>368</u>	<u>20</u>	<u>(96)</u>
Pretax income	14,514	44,051	35,665	36,226		(17.8%)	149.6%	(7,825)	21,712	561
Taxes	4,354	13,215	10,699	10,868		<u>(17.8%)</u>	<u>149.6%</u>	<u>(2,347)</u>	<u>6,514</u>	<u>169</u>
Adj Net income	10,160	30,836	24,965	25,358		(17.8%)	149.6%	(5,478)	15,198	393
Adj EPS b/f charges	\$ 0.25	\$ 0.49	\$ 0.39	\$ 0.40	\$ 0.40	(18.6%)	60.0%	\$ (0.09)	\$ 0.15	\$ 0.01
Diluted shares	40,286	62,777	63,822	62,951		0.3%	56.3%	174	22,665	(871)
COMMON SIZE										
Net revenue	100.0%	100.0%	100.0%	100.0%				-	-	-
Direct costs	<u>68.5%</u>	<u>66.0%</u>	<u>66.3%</u>	<u>65.3%</u>				<u>(60)</u>	<u>(320)</u>	<u>(100)</u>
Gross margin	31.5%	34.0%	33.7%	34.7%				60	320	100
SG&A	<u>17.3%</u>	<u>17.7%</u>	<u>17.4%</u>	<u>17.1%</u>				<u>(60)</u>	<u>(20)</u>	<u>(30)</u>
Adj EBITDA	12.5%	19.1%	16.3%	16.4%				(270)	390	10
Adj EBITDA ex-FOREX	14.2%	16.4%	16.3%	17.6%						
Depreciation	<u>1.6%</u>	<u>1.5%</u>	<u>1.6%</u>	<u>1.5%</u>				-	(10)	(10)
Total expenses	89.1%	82.5%	85.3%	85.1%				270	(400)	(20)
Adj EBITA	10.9%	17.5%	14.7%	14.9%				(270)	400	20
Interest income (expense)	(6.2%)	(4.1%)	(4.1%)	(4.1%)				-	210	-
Other income (expense)	<u>(0.0%)</u>	<u>(0.1%)</u>	<u>0.0%</u>	<u>(0.0%)</u>				<u>10</u>	-	-
Pretax income	4.7%	13.3%	10.7%	10.8%				(250)	610	10
Taxes	<u>30.0%</u>	<u>30.0%</u>	<u>30.0%</u>	<u>30.0%</u>				-	-	-
Adjusted net income	3.3%	9.3%	7.5%	7.5%				(180)	430	10
Gross new busines	423,800		477,600							
Cancellations	(51,900)		(76,416)							
% of backlog	2.6%		3.5%							
Net new business	371,900	398,000	401,184	407,800				2.5%	9.7%	1.6%
Book-to-bill	1.19x	1.20x	1.20x	1.21x						

Source: Company data, FactSet, and Jefferies LLC

Company Description

PRA Health Sciences is a leading global contract research organization. The company provides outsourced clinical development services to the biotechnology and pharmaceutical industries. PRA's global clinical development platform spans 80 countries and employs more than 10,000 individuals worldwide. Since 2000, the company has performed approximately 2,300 clinical trials worldwide and has worked on more than 100 marketed drugs across several therapeutic areas.

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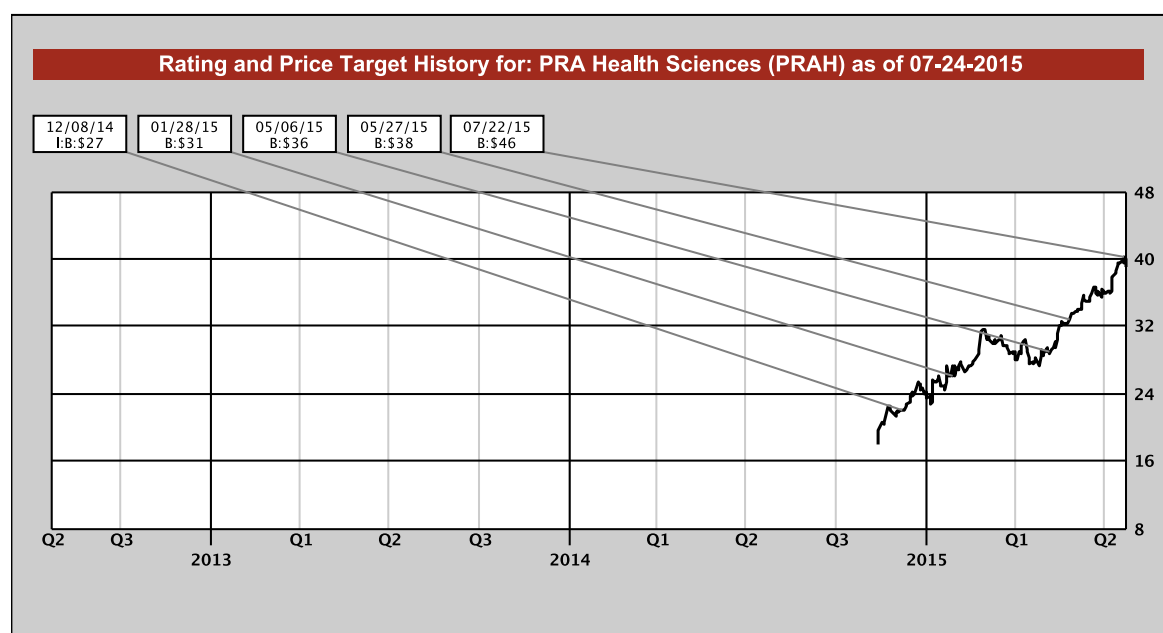
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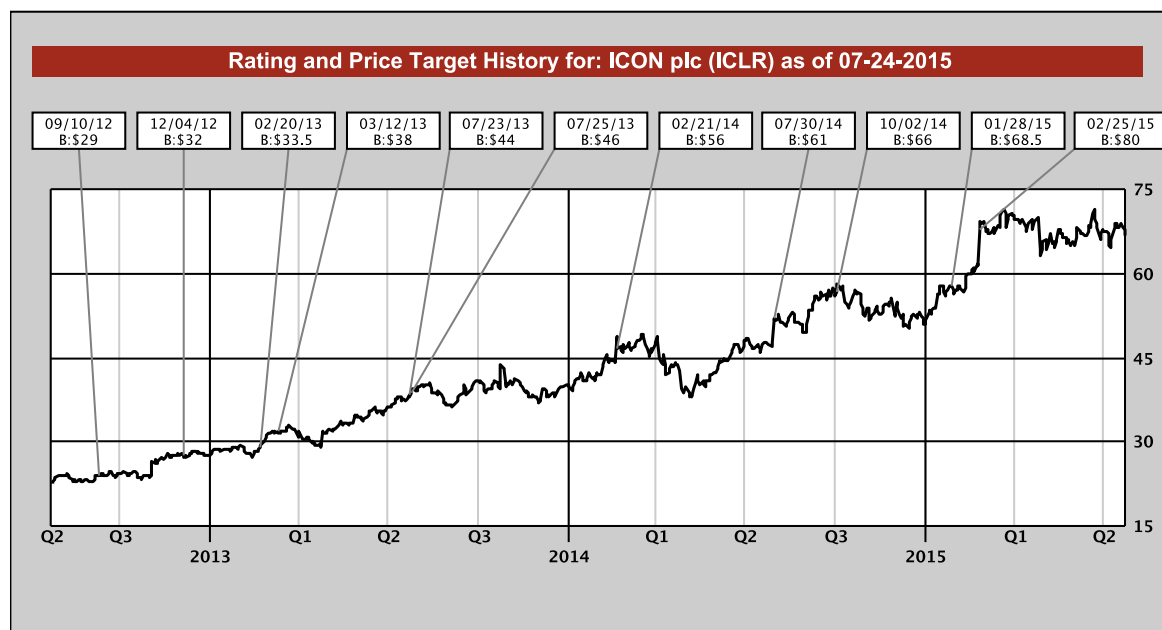
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- PRA Health Sciences (PRAH: \$40.61, BUY)





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			Count	Percent
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