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CREDIT OPINION
24 November 2017

Update

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RATINGS

Yestar Healthcare Holdings Company Limited

Domicile	China
Long Term Rating	Ba3
Type	LT Corporate Family Ratings
Outlook	Stable

Please see the ratings section at the end of this report for more information. The ratings and outlook shown reflect information as of the publication date.

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Yestar Healthcare Holdings Company Limited

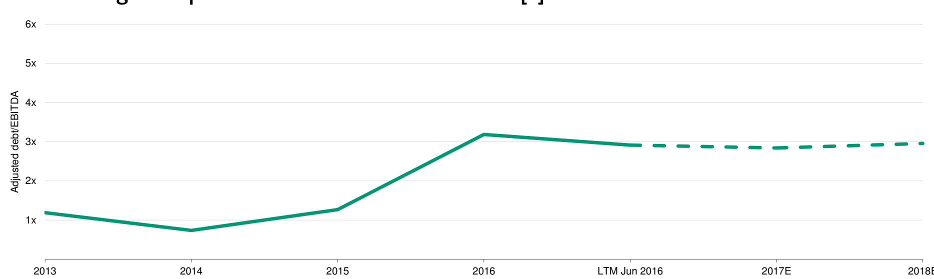
Update to credit analysis

Summary

Yestar Healthcare Holdings Company Limited's (Yestar) Ba3 corporate family rating reflects the company's (1) solid position in the distribution of medical consumable products in China, (2) strong and sustainable partnership with leading global companies, and (3) risk-controlled M&A strategy and prudent financial management.

At the same time, Yestar's rating is constrained by the company's (1) modest size and high supplier concentration, (2) relatively short operating history in distributing in vitro diagnostic (IVD) products, and (3) high cash investment requirements as it continues to pursue growth.

Exhibit 1
Debt leverage is expected to remain stable in 2018F [1]



[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations.
Sources: Moody's Financial Metrics™, Moody's Investors Service estimates

Credit strengths

» Beneficiary of growth in medical consumable products in China

» Stable film business, buttressed by a long relationship with FUJIFILM Holdings Corporation (Fujifilm, A1 negative) and proven film-processing capabilities

» Customer stickiness in IVD products, which offsets risk from a lack of long-term supplier contracts

Credit challenges

» Small scale with high supplier concentration

» M&A risks mitigated by prudent deal structures and financial management

» Solid operating cash flow, but major acquisitions, which will require additional funding

» Evolving regulatory landscape

Rating outlook

The stable outlook reflects our expectation that Yestar will maintain (1) its stable relationships with its key suppliers and customers; (2) a steady film business, while its IVD product consumable business continues to grow; (3) a prudent M&A strategy and financial management, including pre-funding of M&A and no change to the existing dividend policy; and (4) strong corporate governance.

Factors that could lead to an upgrade

» Given the short history of Yestar's IVD product business and the company's small scale, an upgrade is unlikely in the near term. Nevertheless, upward rating pressure could emerge if Yestar continues to build a strong M&A and execution track record, grows its scale and diversifies its key supplier relationships.

» Credit metrics indicative of upward rating pressure include adjusted debt/EBITDA below or around 2.0x, and retained cash flow/debt above 20% on a sustained basis.

Factors that could lead to a downgrade

» Downward rating pressure could emerge if Yestar's operating performance or financial profile, or both, deteriorate owing to (1) a weakening in key supplier relationships; (2) a decline in the company's competitiveness, or a significant change in the competitive landscape for the film or IVD product markets; (3) the pursuit of a more aggressive financial management policy, or (4) the failure to maintain sound corporate governance.

» Credit metrics indicative of downward rating pressure include adjusted debt/EBITDA above 3.0x-3.5x or retained cash flow/debt below 12%.

Key indicators

Exhibit 2

Yestar Healthcare Holdings Company Limited [1][2]

As adjusted	FYE Dec - 13	FYE Dec - 14	FYE Dec - 15	FYE Dec - 16	FYE Dec - 17 (f)	FYE Dec - 18 (f)
Revenue (RMB millions)	1,173	1,531	2,455	3,022	3,801	4,376
EBITA (RMB millions)	101	158	333	510	720	856
Reported operating margin	8.0%	9.7%	11.9%	14.0%	15.6%	16.3%
Debt / EBITDA	1.2x	0.7x	1.3x	3.2x	2.8x	3.0x
EBITA / interest	14.8x	22.1x	15.5x	8.6x	5.0x	4.9x
RCF / debt	-5.9%	81.2%	49.3%	17.0%	18.5%	17.3%

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. [2] Forecasts are Moody's opinion and do not represent the view of the issuer.
Sources: Moody's Financial Metrics™, Moody's Investors Service estimates

Profile

Yestar Healthcare Holdings Company Limited was established in 2000 and is headquartered in Shanghai. The company has been listed on the Hong Kong Stock Exchange since 2013. Yestar is one of the largest distributors of Roche Holding AG's (Roche, A1 stable) diagnostics products in China and the largest distributor of Fujifilm's film products in the mainland since 2014. Yestar is 63% owned by its founder, chairman and CEO, James Hartono and his siblings at end-June 2017.

Detailed credit considerations

Beneficiary of growth in medical consumable products in China

Yestar is well positioned in the medical consumable segment in China, amid an aging population and rising healthcare spending and investment. The company distributes IVD products by global diagnostics leader Roche, as well as by Thermo Fisher Scientific Inc. (Baa2 stable) and Becton, Dickinson and Company (Baa2 stable). Moreover, the company is the largest manufacturer and distributor of Fujfilm medical and dental films in China (A1 stable), producing under both the Fujifilm brand and its own Yes!Star brand for dental film.

We expect the company's medical consumable products sales to grow at a compound annual growth rate of more than 20% to around RMB4.4 billion in 2019 from that in 2016. The company's medical consumable products segment also enjoys higher gross margins versus other businesses segment.

Stable film business, buttressed by a long relationship with Fujifilm and proven film-processing capability

Yestar's mature film business will continue to generate steady revenue and cash flow, helped by the company's long-standing relationship with Fujifilm — which holds strong market positions — and its manufacturing capabilities. The company began purchasing color photographic paper and color film from Fujifilm in 2001, and it has been the exclusive distributor of Fujifilm color photographic paper in China since 2013. In addition, Yestar is the only processor Fujifilm has engaged in China for processing Fujifilm medical film and printed wiring board film sold on the mainland.

Yestar also makes industrial, non-destructive testing x-ray film, which is used for checking the structural integrity of machinery, as well as dental film under its own Yes!Star brand. All of the company's manufacturing and processing are done at its three factories in Nanning in Guangxi Province.

Customer stickiness in IVD products offsets risk from a lack of long-term supplier contracts

Yestar does not have long-term supplier contracts with Roche or the other IVD product suppliers. However, the business risk is mitigated by the company's access to, and long-term contracts with, its end customers. The company has also built a solid track record in its management of its relationship with Fujifilm, another company that does not usually offer long-term contracts or grant exclusivities.

IVD product manufacturers' distribution agreements are generally non-exclusive and need to be renewed annually. On the contrary, Yestar's contracts with hospitals and clinics can last from one to eight years, and those with local distributors can last from one to four years. Such long-term contracts provide stability and give suppliers an incentive to maintain the relationship with their distributors. Distributors also provide value-added services such as equipment installation, testing, maintenance, technical support, warehousing, customer service and receivable responsibilities.

In addition, once a hospital has signed to use a particular manufacturer's products, switching costs are high because it would have to change equipment and installations, and doctors also need to adjust to new data interpretation and analysis. As a result, there is high customer stickiness.

Small scale with high supplier concentration

Yestar is a small company (revenue of RMB1.8 billion in 1H2017) compared with its rated global healthcare peers. The company is also heavily dependent on two supplier relationships, with Fujifilm and Roche.

Substantial portion of Yestar's non-IVD related revenue in the first half of 2017 was derived from Fujifilm, including color photographic film, industrial film, and medical and dental films. However, this exposure was mitigated by the company being the sole manufacturer for Fujifilm in China in several product categories. The relationship also has a long history dating back to 1971 when the family of Yestar's founder, Hartono, first started distributing Fujifilm products in Indonesia.

Yestar derived around 63% of its revenue from its growing IVD product business, with Roche's products accounting for the vast majority of segment sales. The relationship only started in 2014, but Yestar has, through acquisitions and organic growth, already become one of Roche's largest IVD product distributors in China.

M&A risks mitigated by prudent deal structures and financial management

Yestar entered the IVD product distribution business through acquisitions. Since 2014, the company has completed six acquisitions: Jiangsu Uno in 2014; Shanghai Emphasis in 2015; and Guangzhou Hongen, Guangzhou Shengshiyuan, Shenzhen De Run Li Jia and Beijing Kaihongda in 2017. The company will make further acquisitions to supplement its organic business growth. Such a business strategy can be risky, but the company mitigates these risks by carefully structuring deals and maintaining prudent financial management.

In all of its IVD product acquisitions, Yestar buys a 70% stake upfront and acquires the remaining 30% after three-year profit guarantees have been achieved. Such a structure ensures that the acquired companies retain their value. This structure also gives Yestar time to adjust to running the new companies. The shareholders of the acquired companies are also required to enter non-compete agreements to prevent future competition.

Solid operating cash flow, but major acquisitions will require additional funding

Yestar generates solid cash flow from its operations. However, the company's working capital needs, dividends and acquisition payments will keep its free cash flow after acquisitions negative for the next 12-18 months. The company pre-funded for these needs with its $200 million bond issuance in 2016. However, if the company pursues a sizable acquisition, it will need additional funding.

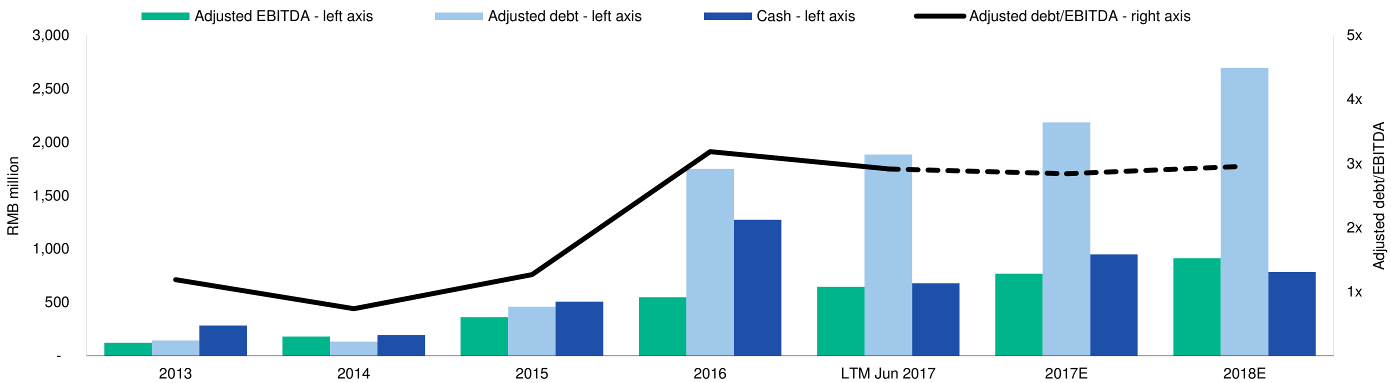
For its film business, Yestar generally receives 60-days of credit from Fujifilm and cash from its customers. However for IVD products, hospital payments can take as long as 240 days. As a result, as its IVD product business grows, Yestar's working capital will be a drag on operating cash flow. At the same time, while the company has low capital spending requirements, its main investment cash outflow will be acquisitions, including payments to buy out the remaining 30% of the acquired companies. Finally, the company plans to maintain 30%-50% dividend payouts.

As a result of the above-mentioned factors, although we expect Yestar's funds from operations to increase, free cash flow after acquisitions will remain negative in the next 12-18 months. The pre-funding of this negative free cash flow via a bond issuance drove the company's increase in total debt as of the end of June 2017 to around RMB1.9 billion from RMB458 million in 2015 (see Exhibit 3).

Yestar's adjusted debt/EBITDA rose to 2.9x as of the 12 months ending June 2017 from 1.3x in 2015. We expect leverage to remain steady in the next 12-18 months because further modest acquisitions could be funded by cash on hand, and revenue and adjusted

EBITDA could grow at around 20% during the same period. However, if the company pursues a significant transaction, additional funding will be required.

Exhibit 3
Yestar's debt pre-funding for its investment needs



Sources: Company's information, Moody's Investors Service estimates

Evolving regulatory landscape

Healthcare is a heavily regulated market in China, especially because most hospitals are run by the government, which on the one hand reduces bad debt risk but on the other hand raises reimbursement and other regulatory risks. Currently, there are no price controls on IVD products, and new products can also be introduced relatively easily by registration rather than by approval. However, this situation may change in the future with the increasing usage and costs of IVD products.

Moreover, the high-end IVD product segment in which Yestar operates is currently dominated by foreign suppliers — including Roche, Siemens Aktiengesellschaft (A1 stable), Abbott Laboratories (Baa3, stable) and Beckman Coulter, Inc. — and its margins are healthy. Local competitors do not yet pose significant competition, given their technological limitations. However, if the government decides to groom national champions like it has been doing in other industries (for example, telecom equipment, semiconductors and chemicals), the competitive landscape may change.

Liquidity analysis

Yestar's liquidity profile is sufficient. At end-June 2017, the company held RMB679 million in unrestricted cash, which, combined with expected cash flow from operations, will be sufficient to fund the Beijing Kaihongda acquisition announced in September 2017, as well as its RMB244 million in short-term debt and remaining payments for its previously announced acquisitions.

Structural considerations

Yestar's Ba3 senior unsecured bond rating is not affected by subordination to claims at the operating company level because the latter is not seen as material, especially because we expect the majority of claims to remain at the holding company.

Methodology and scorecard

The principal methodology used in these ratings was Distribution & Supply Chain Services Industry, published in December 2015. Our Ba3 rating is one notch below the 2017(F) grid outcome, reflecting Yestar's relatively recent entry into the IVD market and acquisition risks.

Exhibit 4

Rating factors

Yestar Healthcare Holdings Company Limited

Distribution and Supply Chain Services Industry Grid [1][2]				2017(F)				
Factor 1 : Scale (20%)	**Aaa**	**Aa**	**A**	**Baa**	**Ba**	**B**	**Caa**	**Ca**
a) Revenue (USD Billion)							X	
b) EBITA (USD Billion)						X		
Factor 2 : Business Profile (15%)								
a) Business Profile						X		
Factor 3 : Profitability & Efficiency (15%)								
a) Operating Margin				X				
b) Return on Invested Capital			X					
Factor 4 : Leverage & Coverage (35%)								
a) Debt / EBITDA				X				
b) EBITA / Interest				X				
c) RCF / Debt					X			
Factor 5 : Financial Policy (15%)								
a) Financial Policy					X			
Rating:								
a) Indicated Rating from Grid					Ba2			
b) Actual Rating Assigned					Ba3			

[1] All ratios are based on 'Adjusted' financial data and incorporate Moody's Global Standard Adjustments for Non-Financial Corporations. [2] 2017(F) represents Moody's forward view, not the view of the issuer.

Source: Moody's Investors Service estimates

Ratings

Exhibit 5

Category	Moody's Rating
YESTAR HEALTHCARE HOLDINGS COMPANY LIMITED	
Outlook	Stable
Corporate Family Rating	Ba3
Senior Unsecured	Ba3

Source: Moody's Investors Service

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