

SOPHARMA TRADING

INDUSTRY: PHARMACEUTICAL WHOLESALE

BOUND TO HEALTHY GROWTH

11.8% CAGR FOR THE LAST SEVEN YEARS; 7.15% AVERAGE DIVIDEND YIELD IN THE LAST FIVE YEARS. SOPHARMA TRADING FIRMLY LEADS THE BULGARIAN PHARMACEUTICALS WHOLESALE MARKET. STABLE MARKET GROWTH OF 3-5% TO SUPPORT THE COMPANY'S TOP LINE WHILE THE EXPECTED 80% INCREASE IN GOVERNMENT HEALTHCARE SPENDING AND THE HOSPITALS' NEED TO INVEST IN NEW EQUIPMENT TO FURTHER BOOST GROWTH AND OFFER HIGHER PROFITABILITY.

FULL-VALUE HEALTHCARE SOLUTIONS PROVIDER

Undisputable Bulgarian pharmaceutical wholesale market leader with a 23% market share, Sopharma Trading provides full-value healthcare solutions to 3000+ customers. Offers diversified portfolio of 10K+ products – medicines, consumables, medical equipment and devices. Excellent network with 400 domestic and international partners, including exclusive partnerships with global leaders like GE Healthcare, Abbott, Carl Zeiss, etc. Profiting on both high-growth pharmacy market and high margin hospital market.

VERTICALLY INTEGRATED WITH A LEADING MEDICINE PRODUCER

Sopharma Trading is part of one of the biggest pharmaceutical groups in Bulgaria – Sopharma (3JR BU), with the latter second biggest generics producer in Bulgaria. Benefits from the synergies of the vertical integration i.e. easy access to low cost financing, thus having a unique position to further penetrate the hospital market.

WIDE DISTRIBUTION NETWORK ACROSS BULGARIA

17,500 sq. m. of warehouse space; 130 vehicles fleet; Full country coverage with five modern regional distribution centers in the major cities of Sofia, Varna, Burgas, Plovdiv and Veliko Turnovo.

STATE-OF-THE-ART WAREHOUSE MANAGEMENT SYSTEM

Operates a state-of-the-art warehouse management system. Integrated fully automated management system in its biggest and newest warehouse in Sofia (10,000 sq. m) in 2008. In 2014, implemented the latest generation of the system in the Varna hub; Modernization in other regional centers to follow. The Company is the first in Bulgaria certified with the international Good Distribution Practice (GDP) standards. With the latest innovations in its warehouses, the Company already meets the GDP's requirements to be introduced in 2017.

GOOD CORPORATE GOVERNANCE AND STABLE DIVIDENDS

Following Sopharma's example, Sopharma Trading has good corporate governance and is among the highest dividend paying companies in Bulgaria with a 5YR average dividend yield of 7% and dividend payout of above 70%.

VALUATION/RISKS

VALUATION: Our BGN 6.47 per share target price is derived by discounting the company's cash flows. **RISKS:** Local healthcare system imbalances; Overregulated healthcare market with imminent regulations reshuffle.

in '000 BGN, excl. ratios	2013	2014F	2015F	2016F
Revenues	507,027	583,081	641,389	692,700
EBITDA	12,770	16,123	19,160	24,033
EBIT	10,548	13,323	15,953	20,223
Net profit	9,490	12,481	15,090	19,272
Equity	59,369	62,489	66,262	71,080
ROE	15.98%	19.97%	22.77%	27.11%
Gross Profit Margin	7.11%	7.20%	7.50%	8.00%
EBITDA margin	2.52%	2.77%	2.99%	3.47%
Net profit margin	1.87%	2.14%	2.35%	2.78%
EPS	0.29	0.38	0.46	0.59
Debt/equity	1.66	1.99	2.09	2.02
P/E	11.10	14.76	12.21	9.56
P/B	1.77	2.95	2.78	2.59
EV/EBITDA	8.25	11.44	9.62	7.67
Payout ratio	80%	75%	75%	75%
Dividend yield	7.19%	5.08%	6.14%	7.84%

BUY
ONE YEAR PRICE TARGET: BGN 6.47
CURRENT PRICE: BGN 5.60

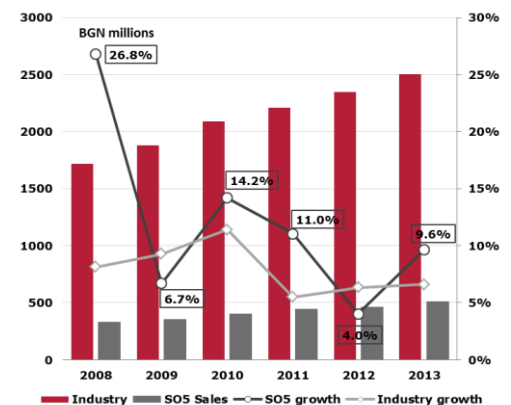
EXCHANGE RATES

EUR/BGN (FIXED): 1.95583
USD/BGN: 1.59555

MARKET DATA

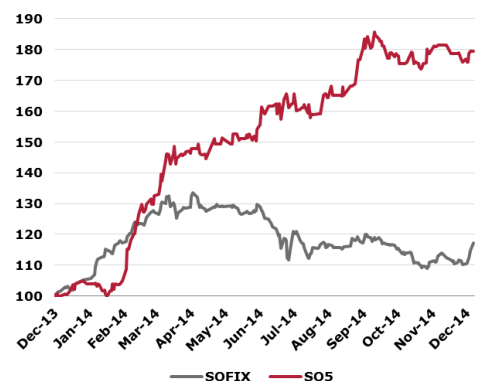
Shares Outstanding:	32.9 m
Share Capital:	32.9 m
Free-float:	28%
Treasury Shares	n/a
Market Cap.:	BGN 184.3 m
Avg. Daily Vol.:	BGN 128,600
52 Weeks Range:	BGN 2.94-5.73
BSE Ticker	S05
Bloomberg Ticker	S05 BU

OUTPACING THE INDUSTRY



Source: Company data

PRICE PERFORMANCE VS. THE MARKET



Source: Bloomberg

EXECUTIVE SUMMARY

WE CONFIRM THE BUY RATING OF SOPHARMA TRADING WITH ONE YEAR PRICE TARGET OF BGN 6.47 WHICH PROVIDES FOR A 15% UPSIDE IN THE NEXT 12 MONTHS.

THE COMPANY

Sopharma Trading (the Company) is the biggest pharmaceuticals wholesaler in Bulgaria. It is part of the local pharmaceutical group – Sopharma (3JR BU), with the latter being one of the leading local generics producer.

Sopharma Trading was established from the merger of five regional wholesalers in Bulgaria in 2007. Since then the Company has doubled its revenue and tripled its net profit. It has also built up its market presence from a cumulative 16% market share in 2007 up to the leading position with a 23% market share.

Diversification: During the last five years, the Company has successfully diversified its operations from being a simple medicine distributor to a full service healthcare provider offering 10,000+ products - medicines, consumables, medical equipment and devices. It also provides turnkey hospitals re-equipment services as well as complete logistics solutions for import, storage and distribution to end customers together with marketing and advertising services for market penetration.

The Company services 3,000+ customers in Bulgaria and has an excellent partnership network with 400 local and international partners, including exclusive contracts with global leaders such as GE Healthcare, Abbott, Carl Zeiss, Eucerin, etc. Such partnerships help the Company diversify its operations, thus tapping on significant profitability as medical equipment, consumables, devices and non-medicine products offer double digit profitability margins compared to the overregulated medicine distribution.

Operations: The Company **works with both pharmacies and hospitals**, with the former generating 54% of revenues in 2013 and the latter – 46%. The pharmacy segment contributes the most to the Company's top line but offers little margins as this part of the healthcare system is overregulated and distributors' markups are limited by law. Local regulations limit wholesalers' margins to 7% max (one of the lowest margins in the EU according to IMS Health) and with the fierce competition on the market it is a margin that is hardly, if at all, achievable. Profitability on the pharmacy segment comes from exclusive product placement.

The hospitals' segment, on the other hand, is divided into four subgroups: medicines, wholesale, medical consumables and devices, and medical equipment. The latter two subgroups i.e. **medical consumables and equipment provide both high growth and high margin potential**, especially when the Company has exclusivity for Bulgaria over certain equipment and consumables manufacturers such as GE Healthcare. Sopharma Trading has exclusive contract with GE in supplying the latter's imaging equipment e.g. MRIs, ultrasound equipment, etc. Therefore, to tap on this potential the Company is focusing on diversifying its product portfolio and further penetrating into these subgroups of the hospital market. During the last five years, it managed to increase its gross profit margin from 6.6% to 7.14% by selling those high margin medical equipment and consumables. Currently, these subgroups still generate less than 5% of the Company's sales but are on the rise.

Nevertheless, working with Bulgarian hospitals has significant shortcomings. Due to the chronic liquidity problems in the Bulgarian healthcare system, hospitals delay their payments with 200, sometimes even 300 days, thus urging pharmaceutical wholesalers to indirectly provide for the financial gap in the system. As a result, few wholesalers have the potential to work on the market unless they have access to cheap financing. Sopharma Trading's vertical integration with Sopharma provides it exactly this – the ability to get better-than-the-market financing terms because domestic banks have high confidence in the group's credit quality. Sopharma Trading is even able to profit from the hospitals' inability to meet payments on time as the Company charges interest on all delayed payments and thus, sometimes financial revenues offset financial expenses.

Corporate Governance: Sopharma Trading has an excellent management team and good corporate governance. It is among the top 10 best dividend paying companies on the market with an average five year dividend yield and dividend payout of 7.15% and 70%+, respectively. The Company is also among the most liquid stocks on the Bulgarian Stock Exchange and as such is part of the BGBX40 index that tracks the 40 most liquid stocks on the market.

THE COUNTRY AND THE MARKET

The country is under a Currency board and the Bulgarian lev is pegged to the Euro at 1.95583.

In 2014, we expect a modest economic growth (approx. 1.4%) as political and financial uncertainty during the summer have depressed business activity and put serious pressure on the state budget and public debt. Nevertheless, with the new government taking cabinet in November, imminent reforms in major sectors as the judiciary, energy and healthcare will support economic growth in the mid- to long term.

We expect the Bulgarian pharmaceutical industry to grow at an accelerating 2 to 5% in the next few years due to the aging population and the hospitals' need to invest in new equipment and complementary consumables. We also expect to see government spending on healthcare increase as it is way below EU average and the healthcare system is regularly underfunded.

THE VALUATION

We use the discounted cash flow method to value Sopharma Trading and provide relative peer valuation only for comparison.

We value the stock of the Company at BGN 6.47 per share or 15% above the current market price.

SOME RISKS

Overregulation due to government's attempts to artificially lower medicine prices; Significant market imbalances due to lack of healthcare reform, incl. inefficient state institutions; Imminent budget deficits may lead to temporarily lower healthcare spending, thus further increasing state hospitals' indebtedness and rising hospitals' insolvency potential;

Fierce pharmaceutical market rivalry; Limited market due to population size; Slow economic growth and lower disposable income for high value medical products.

COMPANY OVERVIEW

Sopharma Trading is the leading pharmaceutical wholesaler in Bulgaria. Established in 2007 from the merger of five regional distributors, the Company has doubled revenues and tripled net profits during the last six years.

It distributes a wide range of healthcare products, 10,000+ items, from basic medicine to special medical cosmetics, medical consumables, equipment and devices. Additionally, it offers pre-wholesale services to other distributors and/or pharmaceutical producers.

Sopharma Trading operates 17,500 sq. m. of warehouse space in five of the major cities in Bulgaria – Sofia, Varna, Burgas, Plovdiv and Veliko Turnovo. The majority of its warehouse space (75%) operates under an innovative state-of-the-art fully automated warehouse management system, implemented from the specialized Austrian company KNAPP. The modern technology limits human mistakes and allows faster customer order processing. A robot collects and compiles orders with human personnel responsible for double checking and special orders only.

The innovative warehouse management system was first introduced in the regional distribution center of the Company in Sofia (10,000 sq. m.) in 2008. In 2014, Sopharma Trading finished the modernization of its second largest warehouse in Varna (3,000 sq. m.) introducing the latest KNAPP warehouse management technology.

Sopharma Trading is the first Bulgarian company to be certified as per ISO 9001:2008 for international Good Distribution Practice (GDP) standard. The standard provides for the best practices in storing, transporting, selling and reporting the distribution of medical products. With the latest innovations in its warehouses, the Company already meets the international GDP's requirements to be introduced in 2017.

*Supplies more than 10,000
medical products*

*Operates state-of-the-art ware-
house management system*

SHAREHOLDERS' STRUCTURE

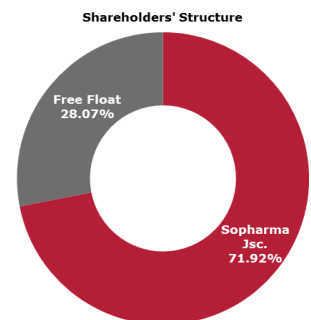
Sopharma Trading is part of the one of the biggest Bulgarian pharmaceutical groups – the Sopharma Group. Its registered capital is BGN 32.905m distributed in 32 905 009 number of outstanding shares.

Sopharma owns 71.92% of the Company's outstanding shares. The rest is free float, traded on the local market and distributed among many institutional and individual investors. The Company has 25,000 small individual investors.

The Company's Chairman of the Board, Mr. Ognyan Donev, is also Sopharma's leading shareholder together with his partner -the Bulgarian lawyer Mr. Ventsislav Stoev. Despite the fact that Mr. Donev is the leading controlling shareholder, his management role in Sopharma Trading's operations is more of a supervisory type rather than executive.

Sopharma Trading's chief executive officer is Mr. Dimitar Dimitrov.

of shares outstanding 32.9 m



POTENTIAL CATALYSTS

GROWING DOMESTIC MARKET: First, aging population will support 2-5% growth of the market over the next couple of years. Second, healthcare costs as a percentage of the state budget are still well below EU average i.e. 4% vs. 7%, respectively. So far, the healthcare system has been chronically underfunded. Thus, imminent sector reform should increase healthcare spending to reach EU average. And third, out-of-dated hospital equipment will be replaced with newer one, thus demand for the latter and the accompanying consumables and devices will further boost growth and offer higher profitability.

PORTFOLIO DIVERSIFICATION: Sopharma Trading's focus on diversification, its exclusive contracts with leading medical product manufacturers and its developed partnerships with local hospitals will help the Company tap on the expected market growth.

SOLID MARKET POSITION: The Company's leading market position, its access to cheap financing and its vertical integration to the group of Sopharma are other competitive advantages providing a gateway to growth and profitability improvement.

HEALTHCARE SECTOR OVERVIEW

GLOBAL & CEE PHARMACEUTICAL SECTOR

The global pharmaceutical market is expected to grow with an accelerating rate of 4 to 7% per year and reach USD 1.2 trillion in 2017 and USD 1.5 trillion in 2020, according an IMS Health research. Emerging markets will be the driving force with an expected annual growth of 10-13%. Eastern Europe is expected to grow at 5-8%.

The aging populations will be the growth engine in rich countries, while in developing countries the population will become wealthier. Therefore, the latter is expected to experience

*Global market expected to grow
at 4-7% until 2017*

chronic diseases, typical of wealthier societies (such as hypertension and diabetes). Besides growth in demand, we expect to witness an increased pressure on drug prices as governments are struggling to narrow budget deficits.

Growth in Eastern Europe will also come from the region's need to renew its old medical equipment. The region has already started the process as post-socialist health care systems are adjusting to rising demand and enriching population and are taking advantage of the targeted healthcare funding from the European Union's Structural Funds. For example, the CEE countries, especially Romania and Bulgaria, have been the "best buyers" of new medical imaging equipment in Europe in the last couple of years. But the region is still lagging behind Western Europe in terms of new devices installed per a million inhabitants, according to a 2013 analysis, conducted by the European Coordination Committee of the Radiological, Electromedical and Healthcare IT Industry. The renewal of medical devices will also be accompanied with an increased demand for the proper complementary consumables, thus providing an additional niche for growth on the market.

Eastern Europe expected to grow at 5-8%

LOCAL PHARMACEUTICAL & PHARMACEUTICAL WHOLESALE SECTOR

The pharmaceutical industry has been one of the fastest growing sectors the Bulgaria over the last decade with 8% CAGR during the last five years. IMS Health expects a modest growth over the next couple of years of 2-5% due to the growing imbalances in the healthcare system (i.e. chronic underfunding and reduced hospital solvency) and lower disposable income due to the economic crisis. Nevertheless, healthcare reform is imminent and is expected to establish efficient healthcare and hospital management and better drug and wholesale regulation.

Market expected to grow 2-5% until 2017

Currently, Bulgaria spends 4% of the state budget on health compared to the EU average of 7.3%. At the same time due to chronic underfunding hospitals significantly delay payments to suppliers. Additionally, due to budget deficits the state often tries to lower drug prices even though drug prices are well below EU average and smaller domestic wholesalers find it profitable to re-export imported drugs. At the same time whole parts of the industry are almost unregulated i.e. no central tendering for special medical consumables, devices and equipment thus offering profitability potential.

According to IMS Health, Bulgaria has the highest VAT on drugs (20%) while regulated wholesale markup capped at 7% for drugs covered by the public funds is one of the lowest in the EU.

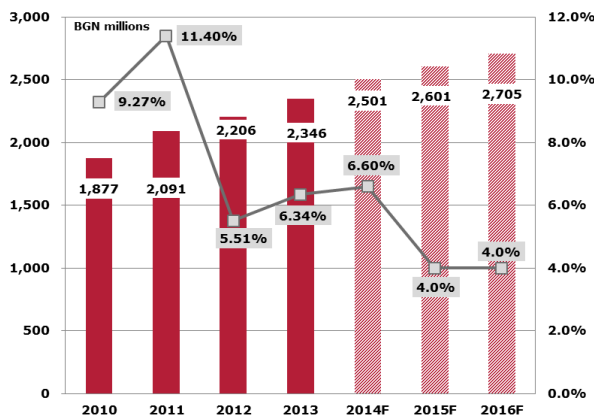
Four major players dominated the wholesale market

Currently, roughly 80% of the market is dominated by international drugs with the rest locally produced by the two leading generic manufacturers – Sopharma and Actavis. However, it is difficult for international players to gain significant part of the wholesale market.

The wholesale is dominated by four players with Sopharma Trading on the lead. Second largest, both in terms of volumes and value, is the ex-Actavis wholesaler Pharmnet that is currently owned and run by the local businessman Veselin Mareshki. The latter also controls the biggest pharmacy chain in the country but has been often accused of improper market practices by competitors. Third in place is again a locally owned distributor - Sting, while the fourth place is for the German Libra-Phoenix wholesaler. All four account for 82% of the market.

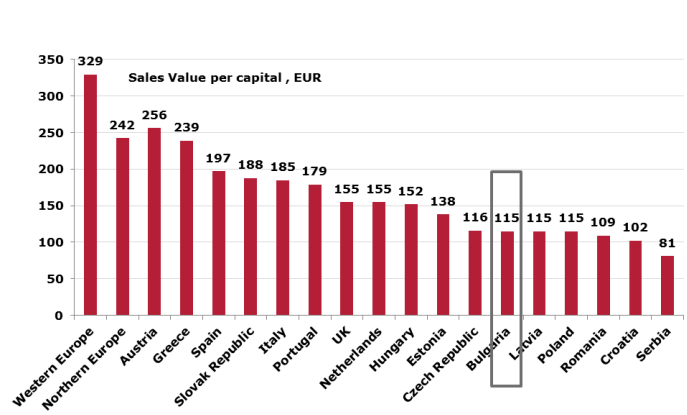
Competition is fierce with Pharmnet dominating the pharmacy market. Sopharma Trading dominates the hospitals market with its easy access to cheap financing. As a result to get margins distributors rely on income from other activities such as marketing, services, exclusive partnerships, and etc.

Exhibit 2: The local market is expected to grow modestly



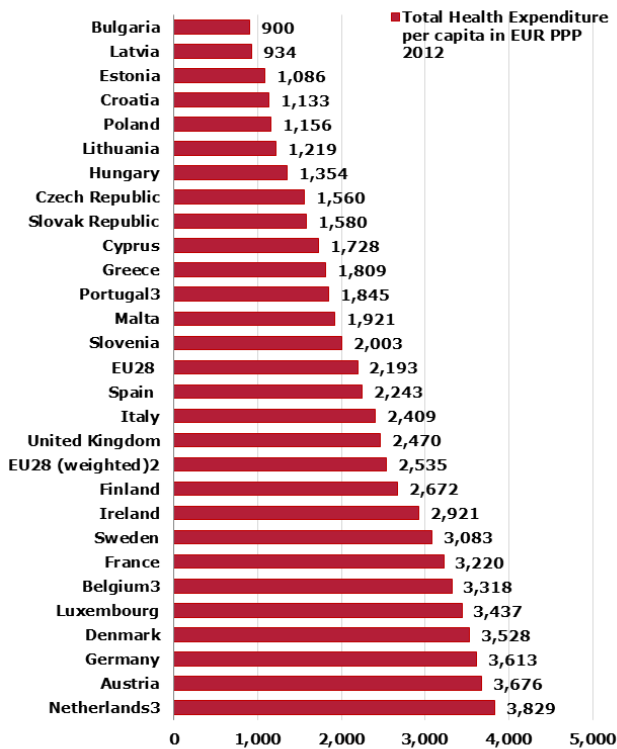
Source: IMS Health

Exhibit 3: Sales value per capita close to CEE average



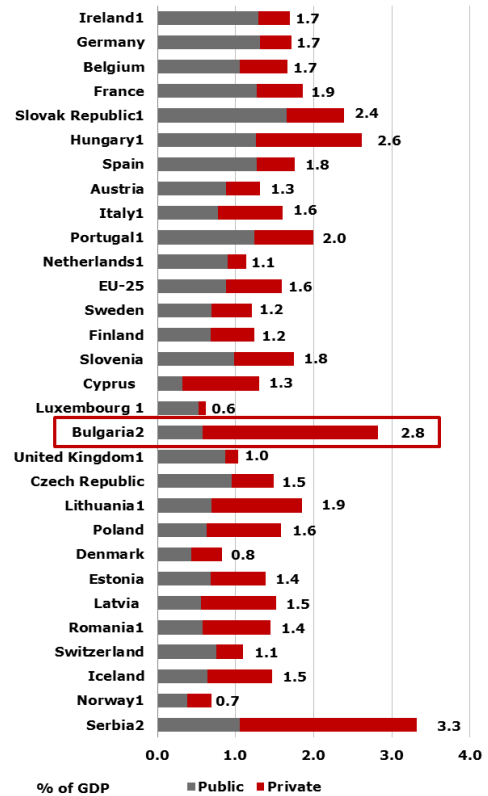
Source: IMS Health; Company data; Q3 2014

Exhibit 4: Total health care expenditures per capita in Bulgaria lowest in EU...



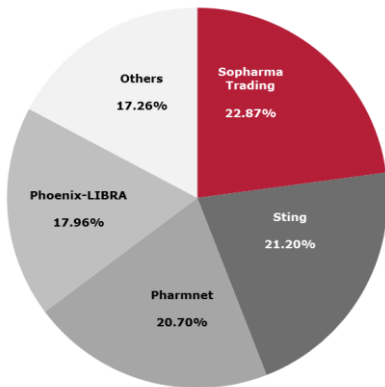
Source: OECD Health Data 2012; Eurostat Statistics Database

Exhibit 5: ... with private spending on prescribed and OTC medicine among the highest in Europe



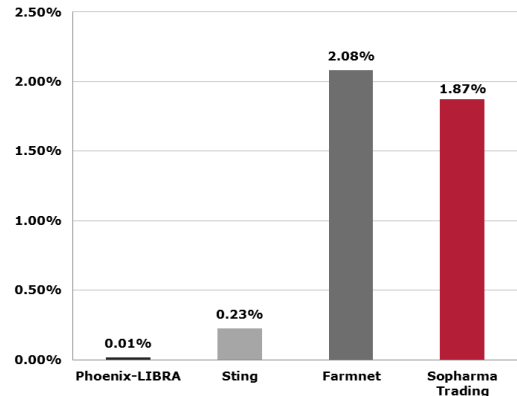
Source: OECD Health Data 2012; Eurostat Statistics Database (1. Includes medical non-durables. 2. Total medical goods)

Exhibit 6: Fierce rivalry, but Sopharma Trading on the lead ...



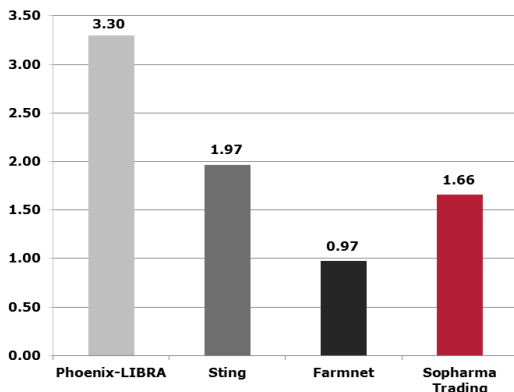
Source: Companies financial statements; FY 2013

Exhibit 7: ... delivering high net profit margins ...



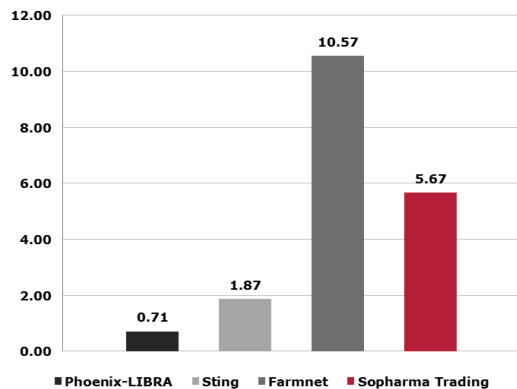
Source: Companies financial statements; FY 2013

Exhibit 8: ... better leverage levels...



Source: Companies financial statements; FY 2013

Exhibit 9: ... and good interest coverage abilities.



Source: Companies financial statements; FY 2013

SOPHARMA TRADING MARKET PRESENCE

Sopharma Trading is the leading pharmaceutical wholesaler in Bulgaria with a 23% market share. It has kept this position during the last five years with solid market presence and diversified portfolio of products and services.

Diversification – Sopharma Trading’s gateway to growth

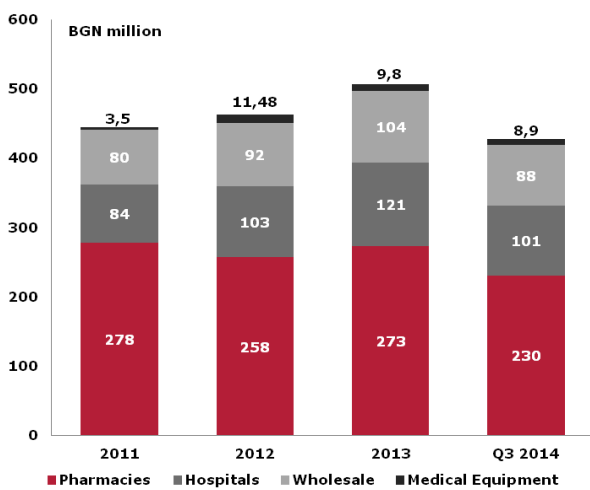
The Company works with both pharmacies and hospitals, with the former generating 54% of revenues in 2013 and the latter – 46%. The hospitals’ segment is divided into four subgroups: medicines, wholesale, medical consumables and devices, and medical equipment. The pharmacy segment and the medicine subgroup of the hospital market contribute the most to the Company’s top line but offer little margins due to overregulation of drug prices and tough competition.

The latter two subgroups in the hospital segment i.e. medical consumables and equipment, however, provide both high growth and high margin potential, especially when the Company has exclusivity over the marketing in Bulgaria of certain products, incl. nonmedicine, such as GE Healthcare devices, for example. Currently, these subgroups generate less than 5% of the Company’s sales. However, Sopharma Trading’s target is to quadruple this part of its business in the mid- to long term tapping on its solid financial position and easy access to cheap financing due to its synergy with the mother company Sopharma.

The Company’s business with related parties, however, represents less than 15% of sales in 2013 and is declining. According to Sopharma Trading’s management, in terms of transfer pricing Sopharma treats its wholesale subsidiary as any other wholesaler it works with i.e. it sells to Sopharma Trading at prevailing wholesale prices set for all the market participants. Additionally, Sopharma Group offers Sopharma Trading slightly longer trade receivables repayment schedules compared to other suppliers to the wholesaler.

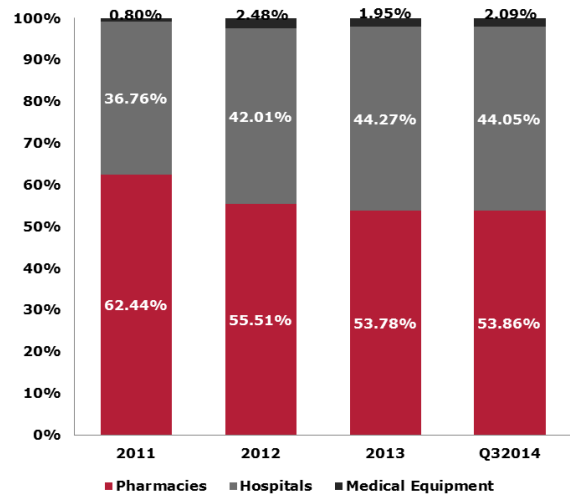
Lastly, more than 80% of the products Sopharma Trading sells are imported.

Exhibit 10: Revenue breakdown by segments, nominal



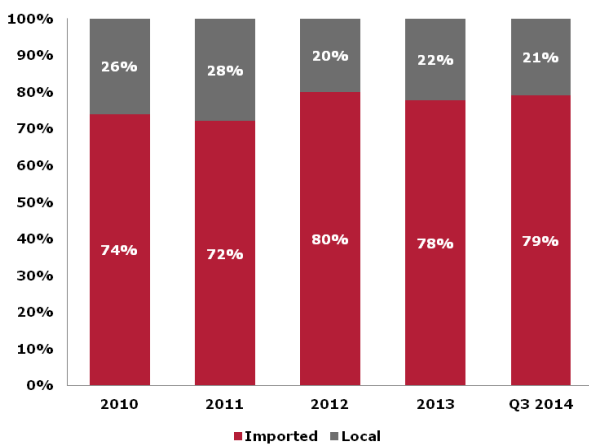
Source: Company data

Exhibit 11: Revenue breakdown by segments, % of sales



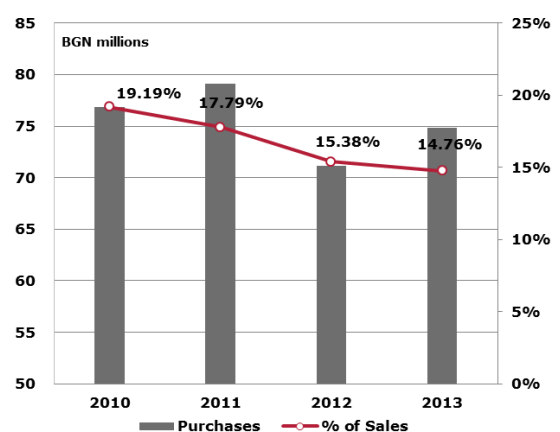
Source: Company data

Exhibit 12: Revenue breakdown by product place of origin



Source: Company data

Exhibit 13: Purchases from related parties



Source: Company data

FINANCIAL ANALYSIS AND VALUATION

Sopharma Trading is a solid company with excellent presence on the Bulgarian pharmaceutical market. The Company's vertical integration to the Sopharma Group adds positively to its ability to get cheaper debt financing. Nevertheless, we consider Sopharma Trading's ability to generate free cash flow fairly independent of the mother company. Therefore, we use the discounted cash flow model to value the Company's intrinsic value and present peer's relative valuation for comparison only.

Stable performance, expected to further improve

	2012	2013	12M	2014E
Current Price	1.78	3.2	5.6	5.6
Number of Shares	32,905	32,905	32,905	32,905
Market Capitalization	58,571	105,296	184,268	184,268
Net Profit	7,349	9,490	11,267	12,481
P/E	7.97	11.10	16.35	14.76
Equity	58,702	59,369	61,761	62,489
P/B	1.00	1.77	1.88	1.90
Sales	466,635	510,342	569,920	587,629
P/S	0.13	0.21	0.32	0.31
EV	58,620	105,391	184,369	184,386
EBITDA	11,052	12,770	15,776	16,123
EV/EBITDA	5.30	8.25	11.69	11.44
ROE	12.52%	15.98%	18.24%	19.97%
ROA	3.39%	4.05%	4.29%	4.45%

SOPHARMA TRADING PERFORMANCE ANALYSIS

Sopharma Trading has doubled its revenues in seven years (11.8% CAGR) and tripled its profits over the same period. The Company has been outpacing the overall market in five of these seven years. In 2014, the trend continues with growth in revenues accelerating to 16% in Q3 2014 due to double digit growth both on the pharmacy and the hospital segments. By the end of the year we expect growth to stabilize at 15% and then gradually decline to a long term growth of 3%.

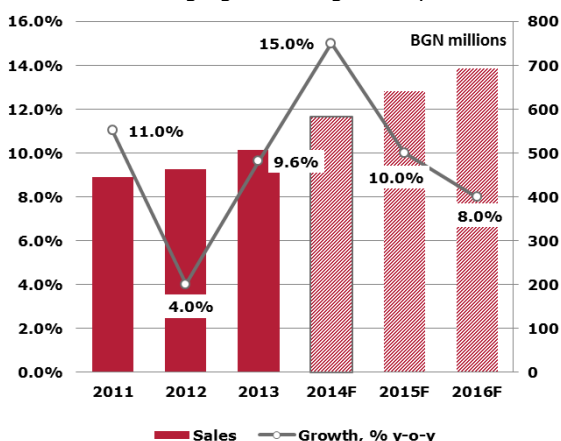
Hospital segment to bring profitability

The Company's portfolio diversification has helped it improve profitability despite the eroded regulative wholesale markup. With fierce rivalry, diversification and excellent partner relationships are the gateways to growth and higher profits.

Gross profit has registered 8% CAGR over the last four years to BGN 36m in 2013. In Q3, 2014 it has added another 14.4% and increased from BGN 26.5m to BGN 30.4m. Additionally, after several years of working below 7% gross profit margin, thanks to diversification, in 2013 the Company surpassed the 7% barrier and in Q3 2014 has reached 7.14%. We expect this positive trend to continue and with rising demand for new medical devices and consumables gross profit to reach 8% of sales by 2016.

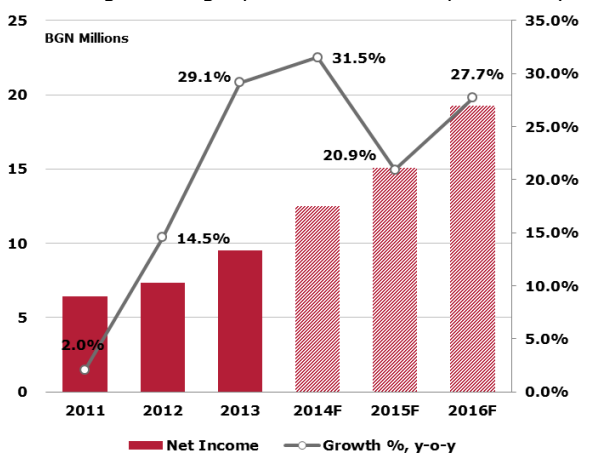
EBIT has also improved registering 31% rise y-o-y in Q3 2014 to BGN 10.8m while net income rose 22% to BGN 9.96m despite rising interest expense.

Exhibit 14: Double digit growth to gradually stabilize to 3%



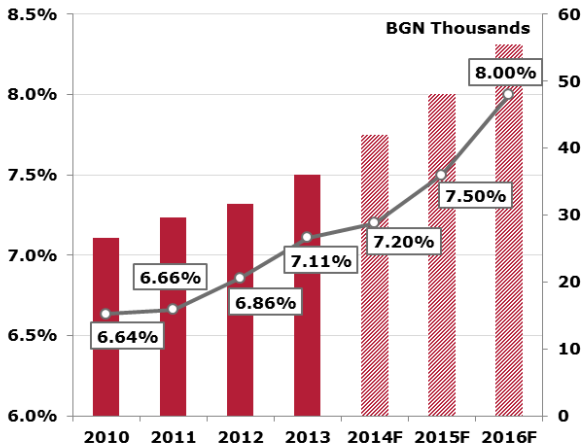
Source: Elana Trading estimates, company data

Exhibit 15: Higher margin products to add to profitability



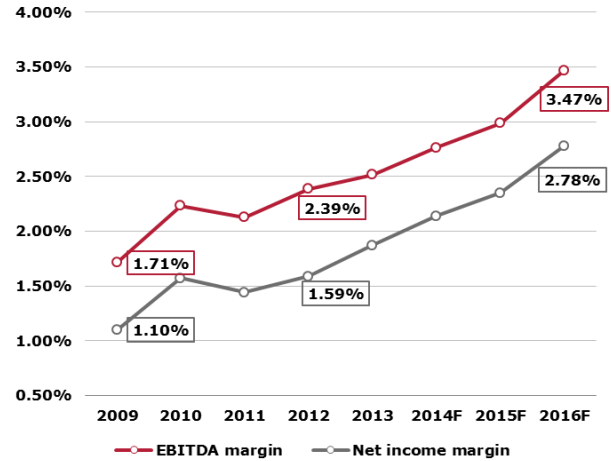
Source: Company data

Exhibit 16: Gross profit margin to further improve ...



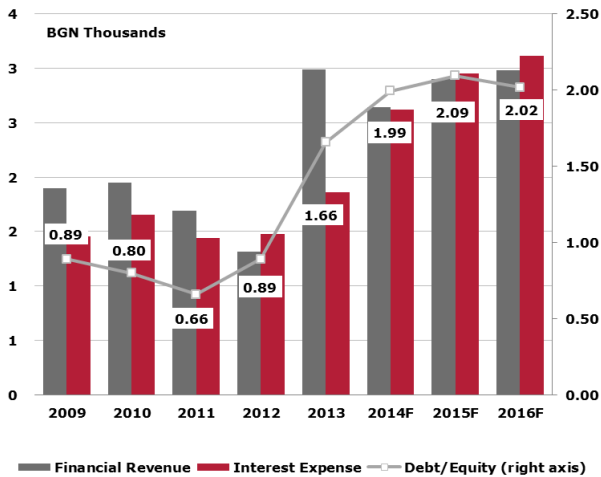
Source: Elana Trading estimates, Company data

Exhibit 17: ... EBITDA and net profit margins to follow...



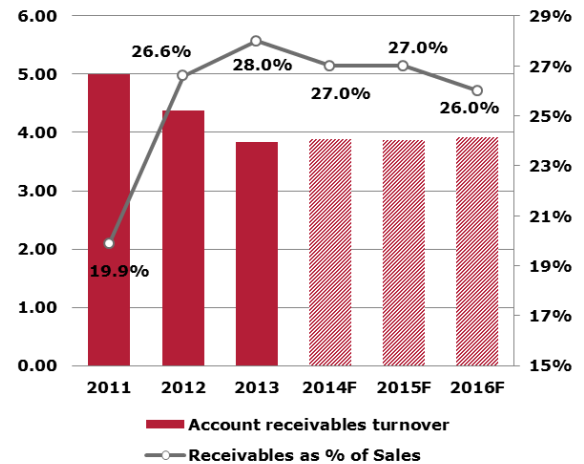
Source: Elana Trading estimates, company data

Exhibit 16: ... even despite rising debt as revenue growth will outpace interest expense growth



Source: Elana Trading estimates, Company data

Exhibit 17: Receivables turnover to stabilize due to flexible collection mechanisms



Source: Elana Trading estimates, company data

Working with hospitals in Bulgaria has its shortcomings. In this case Sopharma Trading is trading off higher revenue and margins with higher debt level. Leverage has doubled in 2013 for two reasons. First, the Company is basically financing delayed payments by hospitals and in a way financing hospitals themselves. Second, up to 2012 some of this financing has been co-shared with the mother company Sopharma, but since the wholesaler is the hospital's supplier in 2013 Sopharma stepped aside and Sopharma Trading is currently dealing with the market specifics independently. It is, however, greatly benefiting from the synergies of the vertical integration with Sopharma, in this case from the group's excellent credit quality and thus access to cheap debt financing. Currently, Sopharma Trading's debt costs are averaging at approx. 2-2.3%.

Debt levels to follow Company's revenue growth

Going forward we expect debt levels growth to stay in line with the Company's pace of growth and any general Bulgarian economy trends. At the same time, we expect to see higher interest expenses to be compensated with reciprocal financial income stemming from hospitals' delayed payments collections.

We also expect CAPEX investments to stay at the current levels. The Company is planning no major investments in new equipment except upgrades of the smaller regional distribution centers in the country with newer warehouse management technology and additional investments in newer operation management systems (e.g. CRMs, etc.).

SOPHARMA TRADING VALUATION

We use the discounted cash flow model to value Sopharma Trading's intrinsic value and it returns a BGN 6.47 per share.

We value Sopharma Trading's at BGN 6.47 per share

When valuing the Company we incorporate a steadily declining revenue growth from 15% in 2014 to a sustainable 3% growth rate 2019 going forward. We expect profit margins to

increase to an EBIT margin above 3% of sales while CAPEX expenses and depreciation to follow the general growth of the Company.

When calculating the Company's weighted average cost of capital we foresee a gradual increase in the risk free rate as Bulgaria's cost of financing will rise with continuing budget deficits. This will translate into higher corporate debt cost as well, but we expect Sopharma Trading to continue to get favorite debt financing terms due to its vertical integration with Sopharma.

ASSUMPTIONS

BGN'000	2012	2013	2014F	2015F	2016F	2017F	2018F	2019F	TERMINAL YEAR
Sales	462,529	507,027	583,081	641,389	692,700	734,262	763,633	786,542	810,138
<i>Growth</i>	<i>4.03%</i>	<i>9.62%</i>	<i>15.00%</i>	<i>10.00%</i>	<i>8.00%</i>	<i>6.00%</i>	<i>4.00%</i>	<i>3.00%</i>	<i>3.00%</i>
EBITDA	11,052	12,770	16,123	19,160	24,033	27,519	29,176	34,200	19,443
<i>EBITDA margin</i>	<i>2.39%</i>	<i>2.52%</i>	<i>2.77%</i>	<i>2.99%</i>	<i>3.47%</i>	<i>3.75%</i>	<i>3.82%</i>	<i>4.35%</i>	<i>2.40%</i>
D&A	2,400	2,222	2,800	3,207	3,810	4,038	3,971	3,933	3,646
<i>% of Sales</i>	<i>0.52%</i>	<i>0.44%</i>	<i>0.48%</i>	<i>0.50%</i>	<i>0.55%</i>	<i>0.55%</i>	<i>0.52%</i>	<i>0.50%</i>	<i>0.45%</i>
Investments	1,964	8,273	5,831	5,773	4,156	4,406	4,582	4,719	5,266
<i>% of Sales</i>	<i>0.42%</i>	<i>1.63%</i>	<i>1.00%</i>	<i>0.90%</i>	<i>0.60%</i>	<i>0.60%</i>	<i>0.60%</i>	<i>0.60%</i>	<i>0.65%</i>
EBIT	8,652	10,548	13,323	15,953	20,223	23,481	25,205	30,267	15,798
<i>EBIT margin</i>	<i>1.87%</i>	<i>2.08%</i>	<i>2.28%</i>	<i>2.49%</i>	<i>2.92%</i>	<i>3.20%</i>	<i>3.30%</i>	<i>3.85%</i>	<i>1.95%</i>
NWC	38,595	37,871	27,988	29,247	24,660	26,140	27,185	28,001	28,355
<i>% of Sales</i>	<i>8.34%</i>	<i>7.47%</i>	<i>4.80%</i>	<i>4.56%</i>	<i>3.56%</i>	<i>3.56%</i>	<i>3.56%</i>	<i>3.56%</i>	<i>3.50%</i>
Change NWC	1,070	-724	-9,883	1,259	-4,587	1,480	1,046	816	354

WACC CALCULATION

	2014	2015	2016	2017	2018	2019	TERMINAL YEAR
RISK FREE RATE	2.50%	3.00%	3.00%	3.50%	3.50%	4.00%	4.00%
EQUITY RISK PREMIUM	12.00%	12.00%	12.00%	12.00%	12.00%	12.00%	12.00%
BETA	0.48	0.55	0.66	0.77	0.80	0.80	0.80
COST OF EQUITY	8.26%	9.60%	10.92%	12.74%	13.10%	13.60%	13.60%
COST OF DEBT	2.75%	3.00%	3.25%	3.25%	3.50%	4.25%	4.25%
EFFECTIVE TAX RATE	10%	10%	10%	10%	10%	10%	10%
AFTER-TAX COST OF DEBT	2.48%	2.70%	2.93%	2.93%	3.15%	3.83%	3.83%
WEIGHT OF EQUITY	33%	32%	33%	34%	35%	37%	37%
WACC	4.41%	4.93%	5.57%	6.24%	6.63%	7.44%	7.44%

DISCOUNTED CASH FLOWS

BGN'000	2014	2015	2016	2017	2018	2019	TERMINAL YEAR
EBIT	13,323	15,953	20,223	23,481	25,205	30,267	15,798
EBIT(1-T)	11,991	14,357	18,201	21,133	22,684	27,240	14,218
ADD: D&A	2,800	3,207	3,810	4,038	3,971	3,933	3,646
LESS: INVESTMENTS	5,831	5,773	4,156	4,406	4,582	4,719	5,266
LESS: CHANGE NWC	-9,883	1,259	-4,587	1,480	1,046	816	354
FCF	18,843	10,532	22,442	19,286	21,028	25,638	12,244
PV FCF	18,641	9,918	19,863	15,843	16,005	17,591	
SUM OF PV FCF	97,861						
PV OF CONTINUING VALUE	210,019						
TOTAL PV FREE CASH FLOWS	307,880						
LESS: OUTSTANDING DEBT	98,475						
PLUS: FINANCIAL ASSETS	3,395						
PV OF EQUITY	212,800						
NUMBER OF SHARES	32,905						
PRICE PER SHARE	6.47						

SENSITIVITY ANALYSIS

Exhibit 18: Terminal growth

	1%	2%	3%	4%	5%
WACC 5.5%	5.76	7.38	10.30	17.10	51.15
WACC 6.0%	5.19	6.47	8.59	12.85	25.61
WACC 7.0%	4.34	5.19	6.47	8.59	12.85
WACC 8.0%	3.73	4.34	5.19	6.47	8.59
WACC 9.0%	3.28	3.73	4.34	5.19	6.47

Source: Elana Trading estimates

Exhibit 19: Terminal EBIT margin

	1.0%	1.5%	2.0%	2.5%	3.0%
WACC 5.0%	5.63	9.43	12.85	17.03	20.83
WACC 6.0%	3.78	6.31	8.59	11.38	13.92
WACC 7.0%	2.86	4.76	6.47	8.56	10.46
WACC 8.0%	2.30	3.82	5.19	6.86	8.38
WACC 9.0%	1.93	3.20	4.34	5.73	7.00

Source: Elana Trading estimates

CENTRAL AND EASTERN EUROPE PEER COMPARISON

Company	Country	Mkt Cap (BGN m)	P/E	ROE	Dvd Yld*
SOPHARMA TRADING	Bulgaria	185	16.35	18.24%	4.51%
MEDIKA DD	Croatia	92	9.54	8.98%	n/a
PELION SA	Poland	366	13.48	12.31%	4.1%
NEUCA SA	Poland	480	14.13	17.55%	1.7%
FARMACOL SA	Poland	526	10.49	10.14%	0%
SALUS DD	Slovenia	70	16.01	5.20%	n/a
		Average	13.33	12.07%	

* Price per share @ ex div day

Source: Bloomberg, Warsaw Stock Exchange

RECOMMENDATION AND PRICE TARGET

The intrinsic value of Sopharma Trading's stock is higher than current the market prices despite the stock's appreciation over the last year. The favorable market and the Company's position on that market are some of the factors to contribute to Sopharma Trading's management efforts to increase shareholders' value.

Recommendation: BUY

Target Price: BGN 6.47

Increase: 15%

We maintain our **BUY** recommendation with price target that offers 15% upside potential to current quotes.

In terms of significant investors involved in our stock market, we share the following observations:

- Bulgarian institutional investors prefer Sopharma Trading's stock due to solid market position and stable dividend policy. They are expected to increase their portfolio positions if the price consolidates below current levels and sustain positions at current price levels.
- Domestic private investors view the stock as stable and perspective for longer-term holding.
- Foreign investors are opening up to Sopharma Trading due to higher liquidity and stable dividend policy.

STOCK PRICE DYNAMICS



ANNUAL FINANCIAL DATA (AUDITED, EXCL. FORECASTS)

INCOME STATEMENT (IN '000 BGN)	2011	2012	2013	TTM	2014F	2015F
Sales	444,616	462,529	507,027	565,593	583,081	641,389
Other operating income	2,577	4,106	3,315	4,327	4,548	5,003
Cost of Materials	2,717	3,127	2,973	3,301	3,498	3,848
Cost of External Services	4,248	5,790	5,962	7,137	6,967	7,971
Cost of Labor	12,540	12,715	13,685	15,042	15,743	17,318
Other operating expenses	4,877	4,131	6,030	4,092	4,198	4,810
COGS	414,990	430,800	470,987	525,731	541,099	593,285
Total Operating Expenses	439,981	457,983	499,794	556,825	574,306	630,439
EBITDA	9,468	11,052	12,770	15,776	16,123	19,160
Depreciation and Amortization	2,256	2,400	2,222	2,681	2,800	3,207
EBIT	7,212	8,652	10,548	13,095	13,323	15,953
Financial revenue	1,692	1,317	2,987	2,529	2,640	2,904
Financial expense	1,754	1,788	2,955	3,267	2,740	2,950
Interest Expense	1,444	1,479	1,861	2,839	2,624	2,950
EBT	7,150	8,181	10,580	12,357	13,223	15,907
Income Taxes	734	832	1,090	1,090	742	816
Net Income	6,416	7,349	9,490	11,267	12,481	15,090
BALANCE SHEET (IN '000 BGN)	2011	2012	2013	TTM	2014F	2015F
Inventories	56,132	55,458	55,039	52,056	64,139	70,553
Receivables from related parties	425	838	2,620	2,237	2,332	1,924
Trade Receivables	88,359	123,025	141,889	158,170	157,432	173,175
Other receivables and prepaid expenses	17,148	9,046	2,816	15,368	8,746	9,621
Cash& Cash Equivalents	5,998	3,507	3,395	5,008	6,997	7,697
CURRENT ASSETS	168,062	191,874	205,759	232,839	239,646	262,970
Property, Plant & Equipment	19,794	20,744	25,322	24,786	29,154	38,483
Intangibles	943	773	920	2,471	1,166	1,283
Investments available for sale	0	3,102	2,256	2,256	4,665	5,131
Other receivables	0	0	306	205	350	385
NON-CURRENT ASSETS	20,737	24,619	28,804	29,718	40,816	45,282
TOTAL ASSETS	188,799	216,493	234,563	262,557	280,462	308,252
Share Capital	32,905	32,905	32,905	32,905	32,905	32,905
Reserves	17,169	18,244	16,691	18,526	17,939	19,448
Retained Earnings	6,502	7,553	9,773	10,330	11,645	13,909
SHAREHOLDERS' EQUITY	56,576	58,702	59,369	61,761	62,489	66,262
Short-term Bank Loans	35,778	47,066	89,573	98,138	116,616	128,278
Current Portion of Long Term Bank Loans	374	1,194	1,865	2,378	2,332	2,566
Liabilities to Related Parties	54,794	67,710	31,895	46,602	44,314	48,746
Account Payables	34,835	34,000	39,493	41,273	42,565	47,463
Tax Liabilities	1,434	1,154	1,559	3,652	1,749	1,924
Liabilities to Employees & Social Security	1,040	1,011	1,169	1,258	1,749	1,924
Other Current Liabilities	2,282	1,144	2,334	1,439	2,332	2,822
CURRENT LIABILITIES	130,537	153,279	167,888	194,740	211,658	233,722
Long Term Bank Loans	1,113	3,976	7,037	5,794	5,615	7,915
Deferred Taxes	398	320	0	0	408	289
OTHER LONG TERM LIABILITIES	175	216	269	262	292	64
NON-CURRENT LIABILITIES	1,686	4,512	7,306	6,056	6,314	8,268
Total Liabilities	132,223	157,791	175,194	200,796	217,973	241,990
Shareholders' Equity and Liabilities	188,799	216,493	234,563	262,557	280,462	308,252
NUMBER OF SHARES:	32,905,009	32,905,009	32,905,009	32,905,009	32,905,009	32,905,009
PRICE IN BGN - PERIOD END:	1.66	1.78	3.2	5.6	5.6	5.6
MARKET CAP IN BGN - PERIOD END:	54,622,315	58,570,916	105,296,029	184,268,050	184,268,050	184,268,050

QUARTERLY FINANCIAL DATA (UNAUDITED)

INCOME STATEMENT ('000 BGN)	Q1 2013	Q2 2013	Q3 2013	Q4 2013	Q1 2014	Q2 2014	Q3 2014
Sales	122,331	120,669	126,106	137,921	143,998	141,903	141,771
Other operating income	1,163	1,698	(409)	863	1,254	1,053	1,157
Cost of Materials	752	724	718	779	818	879	825
Cost of External Services	1,469	1,532	1,456	1,505	2,075	1,442	2,115
Cost of Labor	3,183	3,681	3,339	3,482	3,525	4,226	3,809
Other operating expenses	435	1,230	1,466	2,899	317	632	244
COGS	114,796	112,183	115,578	128,430	141,517	131,168	132,024
Total Operating Expenses	121,280	119,685	122,376	136,453	141,517	139,072	139,783
EBITDA	2,859	3,388	3,675	2,848	4,408	4,609	3,911
Depreciation and Amortization	645	706	354	517	673	725	766
EBIT	2,214	2,682	3,321	2,331	3,735	3,884	3,145
Financial revenue	720	1,045	393	829	510	619	571
Financial expense	466	1,185	541	763	852	847	805
Interest Expense	397	394	413	657	747	728	707
EBT	2,468	2,542	3,173	2,397	3,393	3,656	2,911
Income Taxes	0	0	0	1,090	0	0	0
Net Income	2,468	2,542	3,173	1,307	3,393	3,656	2,911

BALANCE SHEET ('000 BGN)	Q1 2013	Q2 2013	Q3 2013	Q4 2013	Q1 2014	Q2 2014	Q3 2014
Inventories	55,458	44,896	45,820	41,583	55,039	51,931	53,596
Receivables from related parties	838	977	804	907	2,620	2,428	2,321
Trade Receivables	123,025	140,375	140,784	137,846	141,889	144,739	150,729
Other receivables and prepaid expenses	9,046	10,845	9,990	14,484	2,816	9,720	14,726
Cash & Cash Equivalents	3,507	5,253	9,085	6,894	3,395	6,824	4,344
CURRENT ASSETS	191,874	202,346	206,483	201,714	205,759	215,642	225,716
Property, Plant & Equipment	20,744	22,347	22,280	21,725	25,322	24,787	24,618
Intangibles	773	782	639	522	920	987	1,697
Investments available for sale	3,102	0	0	0	2,256	2,256	2,256
Other receivables	0	0	0	0	306	271	248
NON-CURRENT ASSETS	24,619	23,129	22,919	22,247	28,804	28,301	28,819
TOTAL ASSETS	216,493	225,475	229,402	226,056	234,563	243,943	254,535
Share Capital	32,905	32,905	32,905	32,905	32,905	32,905	32,905
Reserves	18,244	18,178	18,516	18,446	16,691	16,691	18,530
Retained Earnings	7,553	10,022	5,233	8,467	9,773	13,166	7,415
SHAREHOLDERS' EQUITY	58,702	61,105	56,654	59,818	59,369	62,762	58,850
Short-term Bank Loans	47,066	50,082	48,622	89,803	89,573	93,686	91,402
Current Portion of Long Term Bank Loans	1,194	1,232	1,519	1,097	1,865	1,854	2,277
Liabilities to Related Parties	67,710	70,744	75,259	28,565	31,895	33,912	45,248
Account Payables	34,000	31,691	35,485	35,249	39,493	39,027	36,792
Tax Liabilities	1,154	2,356	1,838	2,602	1,559	2,767	3,187
Liabilities to Employees & Social Security	1,011	1,026	1,041	1,122	1,169	1,220	1,261
Other Current Liabilities	1,144	1,431	2,722	1,726	2,334	1,735	9,277
CURRENT LIABILITIES	153,279	158,562	166,486	160,164	167,888	174,201	189,444
Long Term Bank Loans	3,976	5,274	5,731	5,545	7,037	6,713	5,977
Deferred Taxes	320	320	320	320	0	0	0
OTHER LONG TERM LIABILITIES	216	214	211	209	269	267	264
NON-CURRENT LIABILITIES	4,512	5,808	6,262	6,074	7,306	6,980	6,241
Total Liabilities	157,791	164,370	172,748	166,238	175,194	181,181	195,685
Shareholders' Equity and Liabilities	216,493	225,475	229,402	226,056	234,563	243,943	254,535

Financial and Performance Indicators	2012	2013	TTM	2014F	2015F
Valuation					
Price/Earnings (P/E)	7.97	11.10	16.35	14.76	12.21
Price/Book (P/B)	1.00	1.77	2.98	2.95	2.78
Price/Sales (P/S)	0.13	0.21	0.32	0.31	0.29
EV (`000 BGN)	58,620	105,391	184,369	184,386	184,399
EV/EBITDA	5.30	8.25	11.69	11.44	9.62
Profitability					
Return on common equity	12.52%	15.98%	18.24%	19.97%	22.77%
Return on assets	3.39%	4.05%	4.29%	4.45%	4.90%
Return on invested capital	1.23%	2.89%	n/a	4.58%	5.09%
EBITDA margin	2.39%	2.52%	2.79%	2.77%	2.99%
EBIT margin	1.87%	2.08%	2.32%	2.28%	2.49%
Net income margin	1.59%	1.87%	1.99%	2.14%	2.35%
Dividend					
Dividend yield	11.24%	7.19%	4.11%	5.08%	6.14%
Dividend per share (BGN)	0.20	0.23	n/a	0.28	0.34
Liquidity					
Current ratio	1.25	1.23	1.20	1.13	1.13
Quick ratio	0.89	0.90	0.93	0.83	0.82
Credit					
LT debt/equity	0.07	0.12	0.09	0.09	0.12
Total debt/equity	0.89	1.66	1.72	1.99	2.09
Total debt/total assets	0.73	0.75	0.76	0.78	0.79

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BUY	Target price is more than 10% above current quotes
HOLD	Target price in +/-10% range of the current quotes
SELL	Target price is more than 10% below the current quotes

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