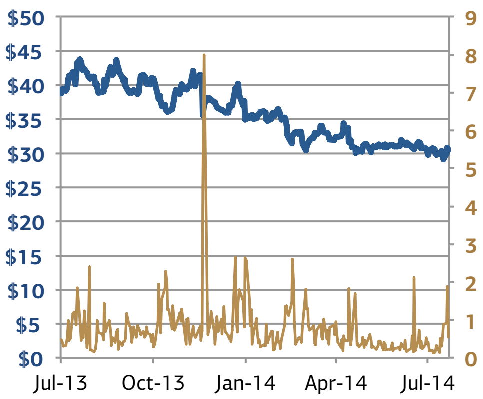
August 14, 2014

Anne Stevenson-Yang
+86 139 1082 0535
anne@jcapitalresearch.com

Mindray Medical Intl. (MR US) one-year share price in USD (blue) and volume (gold, in mln shares)



Source: Bloomberg, August 14, 2014

Mindray Medical Intl. (MR US)

Price	USD 30.50
Rating	**SELL**
Price target	**USD 16.04**
Difference	**47%**
Market Cap	USD 3.60 bln
Simple Moving Avg.	0.47 mln
P/E	16.7x

Source: Bloomberg, August 14, 2014

China | Medical Supplies

Mindray Medical International (MR US)

Not getting better

+ Ugly quarter

Mindray's Q2 results revealed a China business that has hardly a heartbeat, with 3.4% top-line growth, even as the industry reported 15% growth. Overseas, it was all about Zonare. Management lowered guidance from "high teens" to 10%. Board member Chen Qingtai resigned—something that, given the company's other problems, should also be viewed as a negative.

+ Dwindling cash

The company has warned that it will "speed up investments" to improve competitiveness, meaning that the fast-disappearing cash resources will continue dropping. The repurchases of stock dwindled in Q2 to a mere USD 51,000 despite the low share price.

+ SELL; PT USD 16.04

We are lowering our price target to USD 16.04 per share for Mindray, based on a DCF model with a terminal growth rate of 2% and a WACC of 7.5%. We assume 10% top-line growth in 2014 at constant gross margins, deteriorating to 7% in 2015 and 5% thereafter.

Anne Stevenson-Yang +86 139 1082 0535 anne@jcapitalresearch.com

Faltering

Without any new ideas, Mindray reported another weakening quarter in August 12, lowering guidance for the year from "high teens" to 10%. And yet that guidance is premised on a pick-up from the 3.4% growth reported in China to at least 15%. Yet we see China slowing even more dramatically.

China sales weakening.

Our research in China indicates that Mindray has lost what small footing it had gained a couple of years ago in the higher-tier hospitals, which now say they no longer purchase Chinese-made equipment. Mindray's market is at the county level. But the governments that build those hospitals have run short of cash, and no one seems to be buying equipment. The July numbers on all sources of finance—dramatically down—indicate that credit is not moving to borrowers, and that means Mindray's customers will not be making purchases.

Chemicals

Management touted its growing installed base in the IVD business and claims that reagent sales will be driving Mindray's growth. The Q2 report hangs on the reagents.

Mindray provides little disclosure on the IVD business. The company has said that it had six IVD products available in 2013 and was expanding that range in 2014. The company sells reagents, or chemicals to be used in the IVD analyzers, and Mindray discloses that the reagent sales comprised 10.7% of sales in 2013 and 41.2% of total IVD sales in Q2. The reagent sales provided China's growth.

To make the Chinese growth target in 2014, Mindray would need a sequential improvement of 25% in the second half in China. Given management's explanation that a larger installed IVD base will drive that growth, the 10% of revenues that represent the reagents would need to quadruple.

But our research indicates that the IVD equipment sales represent a small portion of the market and of ongoing sales. Furthermore, the county and village hospitals that are Mindray's core market tend to prefer generic IVD machines that can use commodity reagents sold cheaply by a number of vendors. We believe it possible that Mindray may be selling low-value, commodity reagents. If so, that would undermine Mindray's argument that it is

Anne Stevenson-Yang +86 139 1082 0535 anne@jcapitalresearch.com

building a foundation for high-margin sales in the IVD business.

And Mindray does not seem to believe that in any case. Management has warned that the company will be investing in its future and will not be expanding margins for the foreseeable future.

Where's the cash going?

Mindray's cash resources are dwindling, down 11% QoQ in Q2 after dropping 15% QoQ in Q1. Granted, the company paid down debt in the quarter. But Mindray also continued spending heavily on plant and equipment in spite of what we have verified is excess holdings of land, R&D facilities, and productive capacity within China. Spending on R&D has failed to generate tangible benefit for the company. The 1.4% calculated yield on Mindray's cash, restricted cash, and short-term investments seems light in an environment where an office secretary can get 4% in an Alipay money market fund. We continue to have reservations about the quality of cash that Mindray reports and the need for its capital expenditures.

Valuation

We believe Mindray's business is deteriorating and the company is underperforming peers.

We believe that Mindray's China business is deteriorating and that the company is under-performing peers. Overseas, we are skeptical that it can continue to outperform its peer group in Europe when we cannot validate superiority of brand or service offering. We have therefore adjusted down our estimates of Mindray's earnings and lower our target price.

Risks

The Chinese government could provide significant stimulus to local governments to complete the hospital plans they have already approved. Mindray has said it will win new tenders in the second half of the year, and government stimulus could make this wish come true.

Anne Stevenson-Yang +86 139 1082 0535 anne@jcapitalresearch.com

Disclaimer

This publication is issued by J Capital Research ("J Capital"). This publication has been prepared for the general use of the clients of J Capital and unauthorized copying or distribution is prohibited. Nothing in this document shall be construed as a solicitation to buy or sell any security or product. In preparing this document, J Capital did not take into account the investment objectives, financial situation and particular needs of the reader. Before making an investment decision, the reader needs to consider, with or without the assistance of an adviser, whether the advice is appropriate in light of their particular investment needs, objectives and financial circumstances. J Capital accepts no liability whatsoever for any direct, indirect, consequential or other loss arising from any use of this publication and/or further communication in relation to this document.