

Essex Bio-Technology (1061.HK)

Results in the 1H16 Slightly Fell Short of Expectations

Hong Kong | Health & Personal care | Company report

21 September 2016

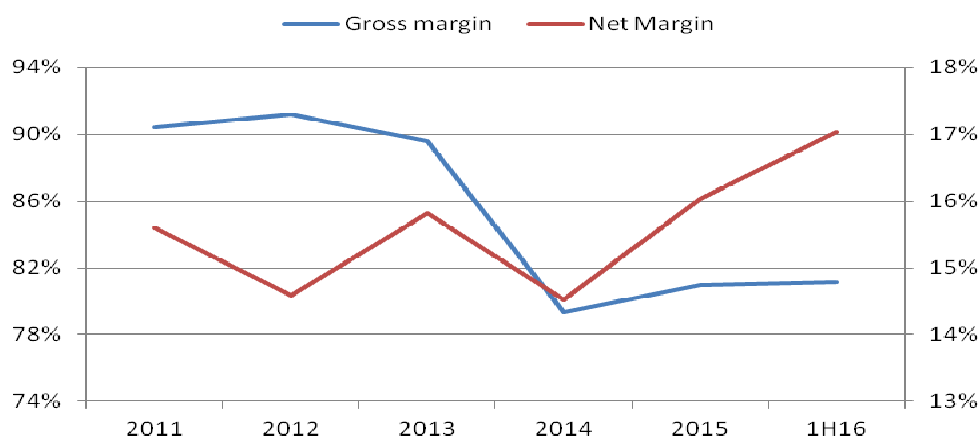
Results in the 1H16 Slightly Fell Short of Expectations

During the first half of the year, Essex Bio-Technology recorded a total revenue of HKD360 million, increased by 16.1% year on year. Meanwhile, the company achieved a net profit of HKD61.99 million, representing a year-on-year increase of 20.0% with a slowdown of growth rate. The EPS was 11.08 HK cents, increased by 19.4% on a year-on-year basis. Disregarding the RMB depreciation, the company achieved the revenue growth of over 20% and the profit growth approximately 30%, which were lower than the CAGR of 32.4% and 33.2% in the previous five years, respectively.

In the past, the company mainly depended on the Beifushu series products for the treatment of ocular wound healing and the Beifuji series products for the treatment and healing of surface wounds. In 2015, these two series products, respectively, contributed to 43% and 41% of the corporate revenue. During the first half of 2016, the company's surgical products realized a year-on-year revenue increase of 33.5%, wherein the Beifuji series products accounting for 93.4% the revenue of surgical products achieved a year-on-year increase of 24.8%. However, the revenue of ophthalmic products only increased by 0.6% Y-o-Y. In addition, the company was making adjustment to its sales system during the first half of the year and the growth rate of the product agent business fell short of the management's expectations put forward at the beginning of the year.

In terms of profitability, the company maintained a steady gross profit margin at 81%, down slightly by 1% on a year-on-year basis. At the same time, the company massively reduced administrative expenses by HKD5.4 million, contributed greatly to the increase of net profit margin. The decrease of administrative expenses was mainly due to the decrease of approximately HKD2.1 million in the equity-settled share-based payments to the employees and the decrease of approximately HKD2.4 million in research and development cost.

Earning capabilities of Essex Bio-Technology



Source: Company reports, Phillip Securities (HK) Research

Buy (Initially)

CMP: HKD 3.62

(Closing price as at 19 Sep 2016)

TARGET: HKD 4.52 (+24.8%)

COMPANY DATA

O/S SHARES (MN) :	560
MARKET CAP (HKDMN) :	2,026
52 - WK HI/LO (HKD):	5.08/ 3.35

SHARE HOLDING PATTERN, %

YAN Mingzhi:	53.42
--------------	-------

PRICE PERFORMANCE, %

	1M	3M	1Y
Essex Bio-Technology	-3.47	-9.27	-21.98
HSI	-5.32	-25.73	-28.21

PRICE VS. HSI



Source: Phillip Securities (HK) Research

KEY FINANCIALS

HK\$ mn	FY14	FY15	FY16E	FY17E
Net Sales	518	654	801	961
Net Profit	75	105	126	152
EPS, HK\$	0.14	0.19	0.23	0.27
PER, x	26.8	19.3	16.0	13.3
BVPS, HK\$	0.59	0.74	0.94	1.17
P/BV, x	6.09	4.91	3.86	3.09
ROE, %	25.7	28.2	26.9	25.8
Debt/Equity (%)	52.0	54.2	53.8	53.8

Source: Company reports, Phillip Securities Est.

Research Analyst
Fan Guohe
 (+ 86 21 51699400-110)
 fanguohe@phillip.com.cn

Sales Expansion may Contribute More Gradually

The surgical products were sold to 1900 hospitals, adding 135 new ones. Considering the brand awareness and the room for growth with respect to the number of hospitals, the surgical product is expected to maintain a comparatively rapid growth rate. Meanwhile, some of the company's ophthalmic products are planned to be launched in 2017. There are two ophthalmic products waiting for mass production. The therapeutic product using platelet-derived growth factor (PDGF) is still pending approval. Therefore, the ophthalmic business is expected to gradually recover.

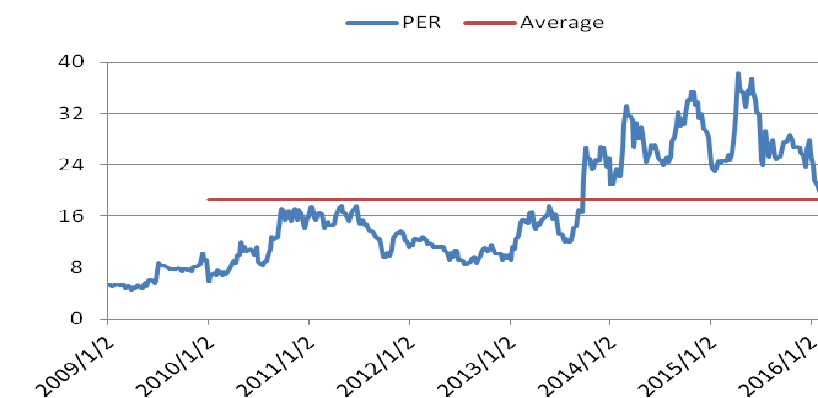
In 1H16, the sales team was expanded to currently 1255 members from the originally 910 members at the end of 2015. The newly added salesmen are mainly responsible for promoting new products. With time passing by, hopefully the new members will make significant contributions to the company's revenue and fully prepare for the agent business of an increasing number of third-party products in the future. In 1H16, the company recorded year-on-year increase of 84.6% with respect to the third-party products or services, which significantly outperformed the self-owned products in growth rate. Meanwhile, the revenue-contribution ratio was increased to 19%. It is regarded as a new aspect for business growth.

In spite of business growth due to internal adjustment, the company also emphasizes on expansion. It made investment in overseas enterprises in January, April and May 2016, respectively, aiming at product expansion in such fields as nerve regeneration, cancer treatment and ophthalmic devices in order to drive mid- and long-term development of the company.

Valuation

The company's surgical business is expected to maintain comparatively rapid growth. In addition, the gradual recovery of ophthalmic products and promotion of new products are likely to make significant contribution to the increment. We grant Essex Bio-Technology the "Buy" rating initially. The target price is HKD4.52, equivalent to 20x EPS in 2016. (Closing price as at 19 Sep 2016)

Historical P/E Valuation



Source: Bloomberg, Phillip Securities (HK) Research

Risks

Price drop of drugs exceeds expectation;
The time of launching of new products falls short of expectations;
Exchange rate volatility affects business performance.

Financials

FYE	2013	2014	2015	2016F	2017F
Valuation Ratios					
Price Earnings	36.57	26.81	19.26	16.02	13.33
Price to Book	7.93	6.09	4.91	3.86	3.09
Dividend Yield	0.5%	0.6%	0.7%	1.1%	1.4%
Per share data(HK\$)					
EPS Adjusted	0.10	0.14	0.19	0.23	0.27
Book Value Per Share	0.46	0.59	0.74	0.94	1.17
Dividends Per Share	0.02	0.02	0.03	0.04	0.05
Growth & Margin					
Revenue growth	-	49.3%	26.2%	22.4%	20.0%
Gross Profit growth	-	32.3%	28.8%	21.0%	20.0%
Net Profit growth	-	37.1%	39.4%	20.5%	20.3%
Profitability Ratios					
Gross Margin	89.6%	79.3%	81.0%	80.0%	80.0%
Net Profit Margin	15.8%	14.5%	16.0%	15.8%	15.8%
Dividend Payout Ratio %	18.2%	16.3%	13.3%	17.7%	18.4%
Key Ratios					
Return on Assets	15.3%	16.9%	18.4%	17.5%	16.7%
Return on Equity	24.4%	25.7%	28.2%	26.9%	25.8%
Effective Tax Rate					
Effective Tax Rate	24.9%	21.4%	19.7%	20.0%	20.0%
Liability ratio					
Liability ratio	34.4%	34.2%	35.1%	35.0%	35.0%
Income Statement(HK\$: mn)					
Revenue	347	518	654	801	961
- Cost of Goods Sold	36	107	124	160	192
Gross Income	311	411	530	641	769
- Selling, General & Admin Exp	239	313	398	484	581
Operating Income	73	100	138	165	197
Pretax Income	73	96	131	158	190
- Income Tax Expense	18	20	26	32	38
Income Before XO Items	55	75	105	126	152
Net Profit	55	75	105	126	152

Source: Company, Phillip Securities (HK) Research Estimates
(Financial figures as at 19 Sep 2016)

PHILLIP RESEARCH STOCK SELECTION SYSTEMS

Total Return	Recommendation	Rating	Remarks
>+20%	Buy	1	>20% upside from the current price
+5% to +20%	Accumulate	2	+5% to +20% upside from the current price
-5% to +5%	Neutral	3	Trade within $\pm 5\%$ from the current price
-5% to -20%	Reduce	4	-5% to -20% downside from the current price
<-20%	Sell	5	>20% downside from the current price

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

GENERAL DISCLAIMER

This publication is prepared by Phillip Securities (Hong Kong) Ltd ("Phillip Securities"). By receiving or reading this publication, you agree to be bound by the terms and limitations set out below.

This publication shall not be reproduced in whole or in part, distributed or published by you for any purpose. Phillip Securities shall not be liable for any direct or consequential loss arising from any use of material contained in this publication.

The information contained in this publication has been obtained from public sources which Phillip Securities has no reason to believe are unreliable and any analysis, forecasts, projections, expectations and opinions (collectively the "Research") contained in this publication are based on such information and are expressions of belief only. Phillip Securities has not verified this information and no representation or warranty, express or implied, is made that such information or Research is accurate, complete or verified or should be relied upon as such. Any such information or Research contained in this publication is subject to change, and Phillip Securities shall not have any responsibility to maintain the information or Research made available or to supply any corrections, updates or releases in connection therewith. In no event will Phillip Securities be liable for any special, indirect, incidental or consequential damages which may be incurred from the use of the information or Research made available, even if it has been advised of the possibility of such damages.

Any opinions, forecasts, assumptions, estimates, valuations and prices contained in this material are as of the date indicated and are subject to change at any time without prior notice.

This material is intended for general circulation only and does not take into account the specific investment objectives, financial situation or particular needs of any particular person. The products mentioned in this material may not be suitable for all investors and a person receiving or reading this material should seek advice from a financial adviser regarding the suitability of such products, taking into account the specific investment objectives, financial situation or particular needs of that person, before making a commitment to invest in any of such products.

This publication should not be relied upon as authoritative without further being subject to the recipient's own independent verification and exercise of judgment. The fact that this publication has been made available constitutes neither a recommendation to enter into a particular transaction nor a representation that any product described in this material is suitable or appropriate for the recipient. Recipients should be aware that many of the products which may be described in this publication involve significant risks and may not be suitable for all investors, and that any decision to enter into transactions involving such products should not be made unless all such risks are understood and an independent determination has been made that such transactions would be appropriate. Any discussion of the risks contained herein with respect to any product should not be considered to be a disclosure of all risks or a complete discussion of such risks.

Nothing in this report shall be construed to be an offer or solicitation for the purchase or sale of a security. Any decision to purchase securities mentioned in this research should take into account existing public information, including any registered prospectus in respect of such security.

Disclosure of Interest

Analyst Disclosure: Neither the analyst(s) preparing this report nor his associate has any financial interest in or serves as an officer of the listed corporation covered in this report.

Firm's Disclosure: Phillip Securities does not have any investment banking relationship with the listed corporation covered in this report nor any financial interest of 1% or more of the market capitalization in the listed corporation. In addition, no executive staff of Phillip Securities serves as an officer of the listed corporation.

Availability

The information, tools and material presented herein are not directed, intended for distribution to or use by, any person or entity in any jurisdiction or country where such distribution, publication, availability or use would be contrary to the applicable law or regulation or which would subject Phillip Securities to any registration or licensing or other requirement, or penalty for contravention of such requirements within such jurisdiction.

Information contained herein is based on sources that Phillip Securities (Hong Kong) Limited ("PSHK") believed to be accurate. PSHK does not bear responsibility for any loss occasioned by reliance placed upon the contents hereof. PSHK (or its affiliates or employees) may have positions in relevant investment products. For details of different product's risks, please visit the Risk Disclosures Statement on <http://www.phillip.com.hk>.

© 2016 Phillip Securities (Hong Kong) Limited

Contact Information (Regional Member Companies)

SINGAPORE**Phillip Securities Pte Ltd**

Raffles City Tower
250, North Bridge Road #06-00
Singapore 179101
Tel : (65) 6533 6001
Fax : (65) 6535 6631
Website: www.poems.com.sg

HONG KONG**Phillip Securities (HK) Ltd**

Exchange Participant of the Stock Exchange of Hong Kong
11/F United Centre 95 Queensway
Hong Kong
Tel (852) 22776600
Fax (852) 28685307
Websites: www.phillip.com.hk

INDONESIA**PT Phillip Securities Indonesia**

ANZ Tower Level 23B,
Jl Jend Sudirman Kav 33A
Jakarta 10220 – Indonesia
Tel (62-21) 57900800
Fax (62-21) 57900809
Website: www.phillip.co.id

THAILAND**Phillip Securities (Thailand) Public Co. Ltd**

15th Floor, Vorawat Building,
849 Silom Road, Silom, Bangrak,
Bangkok 10500 Thailand
Tel (66-2) 6351700 / 22680999
Fax (66-2) 22680921
Website: www.phillip.co.th

UNITED KINGDOM**King & Shaxson Capital Limited**

6th Floor, Candlewick House,
120 Cannon Street,
London, EC4N 6AS
Tel (44-20) 7426 5950
Fax (44-20) 7626 1757
Website: www.kingandshaxson.com

AUSTRALIA**PhillipCapital Australia**

Level 12, 15 William Street,
Melbourne, Victoria 3000, Australia
Tel (613) 96188238
Fax (613) 92002272
Website: www.phillipcapital.com.au

MALAYSIA**Phillip Capital Management Sdn Bhd**

B-3-6 Block B Level 3 Megan Avenue II,
No. 12, Jalan Yap Kwan Seng, 50450
Kuala Lumpur
Tel (603) 21628841
Fax (603) 21665099
Website: www.poems.com.my

JAPAN**PhillipCapital Japan K.K.**

Nagata-cho Bldg.,
8F, 2-4-3 Nagata-cho,
Chiyoda-ku, Tokyo 100-0014
Tel (81-3) 35953631
Fax (81-3) 35953630
Website: www.phillip.co.jp

CHINA**Phillip Financial Advisory (Shanghai) Co. Ltd**

No 436 Hengfeng Road,
Greentech Unit 604,
Postal code 200070
Tel (86-21) 51699400
Fax (86-21) 63532643
Website: www.phillip.com.cn

FRANCE**King & Shaxson Capital Limited**

3rd Floor, 35 Rue de la Bienfaisance 75008
Paris France
Tel (33-1) 45633100
Fax (33-1) 45636017
Website: www.kingandshaxson.com

UNITED STATES**Phillip Futures Inc**

141 W Jackson Blvd Ste 3050
The Chicago Board of Trade Building
Chicago, IL 60604 USA
Tel +1.312.356.9000
Fax +1.312.356.9005