

Salubris (002294.CH)

Growth Expected to Be Accelerated in 2017

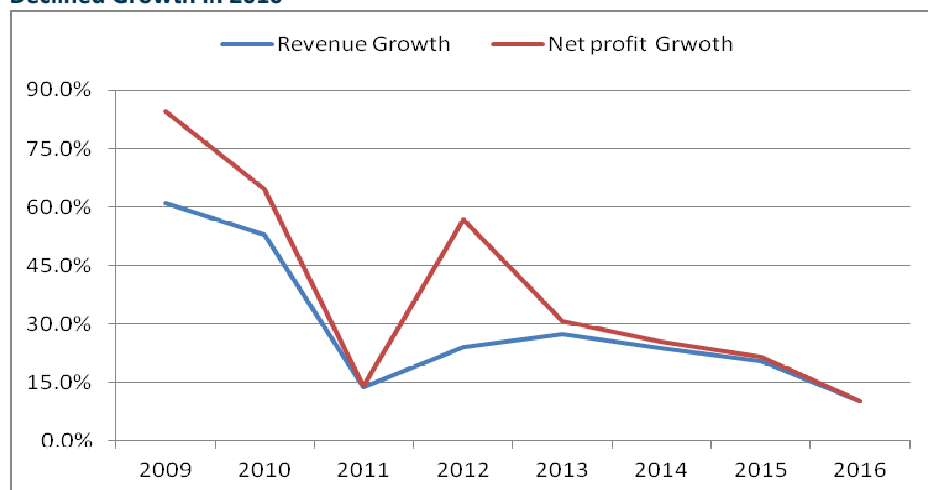
China | Pharmaceutical | Company report

10 February 2017

Growth Slowed Down in 2016

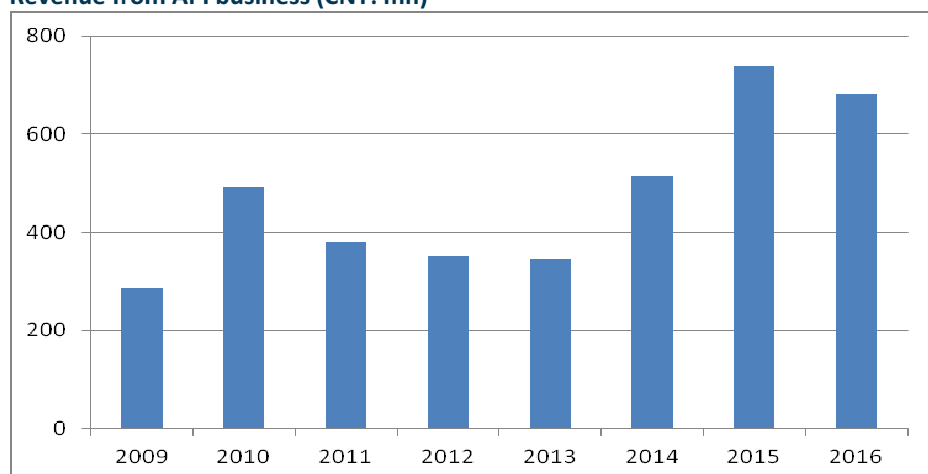
In 2016, Salubris recorded RMB3.83 billion in revenue, up 10.2% yoy; the net profit attributable to the parent company stood at RMB1.39 billion, up 10.2% yoy, with an EPS of RMB1.33. Overall speaking, the company experienced steady growth in 2016, but the growth rate slowed down, touching the lowest level since Salubris' IPO. As the main factor, the capacity was affected to a certain extent because the API business had been in the process of adjustment to production planning under the pressure from environmental protection. We expect that the API revenue in 2016 is less than RMB700 million, down to some extent compared to the previous year.

Declined Growth in 2016



Source: Company reports, Phillip Securities (HK) Research

Revenue from API business (CNY: mn)



Source: Company reports, Phillip Securities (HK) Research

However, the company's preparations business is still expected to achieve rapid growth, with the sales volume of competitive products Clopidogrel (Taijia) rising by around 15% to approximately RMB2.6 billion, and the revenue from second-line products, such as Bivalirudin, achieving rapid y-o-y growth at RMB120 million to RMB150 million.

BUY (Initially)

CMP: CNY 29.04

(Closing price as at 8 Feb 2017)

TARGET: CNY 36.70 (+26.4%)

COMPANY DATA

O/S SHARES (MN) :	1,046
MARKET CAP (CNYMN) :	30,376
52 - WK HI/LO (CNY):	31.13/24.81

SHARE HOLDING PATTERN, %

Salubris Pharmaceutical Co. Ltd. :	67.73
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PRICE PERFORMANCE, %

	1M	3M	1Y
Salubris	-1.39	-2.96	13.71
HS300	-1.35	-3.59	0.33

PRICE VS. HS300



Source: Phillip Securities (HK) Research

KEY FINANCIALS

CNY mn	FY14	FY15	FY16E	FY17E
Net Sales	2840	3427	3833	4363
Net Profit	1042	1266	1395	1600
EPS, CNY	0.99	1.21	1.33	1.53
PER, x	29.22	24.00	21.83	18.98
BVPS, CNY	3.61	4.39	5.12	5.99
P/BV, x	8.04	6.62	5.67	4.85
ROE, %	30.17	30.25	27.17	26.18
Debt/Equity (%)	21.86	14.72	14.29	14.29

Source: Company reports, Phillip Securities Est.

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Growth Expected to Be Accelerated in 2017

First, the company is one of the few local enterprises which has successfully operated high-end generic varieties, and its core variety, Taijia, has obtained the EU certification and becomes a typical example of high-quality homegrown generic drugs. Due to too many potential competitors, the market generally was not optimistic about the prospects of Taijia. But after the introduction of the consistency evaluation policy on generic drugs, medical policies have valued "improvement of quality standards, emphasis on cost performance", which will benefit high-quality generics in approval process, bidding and purchasing and other processes. Therefore, we expect Taijia's oligopoly to maintain. Furthermore, Interim Measures for Drug Trade of Medical Institutions in Guangdong Province took effect in September 2016, which means Taijia may participate in the tender through the non-base drug list and return to the Guangdong market in 2017. Therefore, we anticipate that Taijia will report more rapid growth.

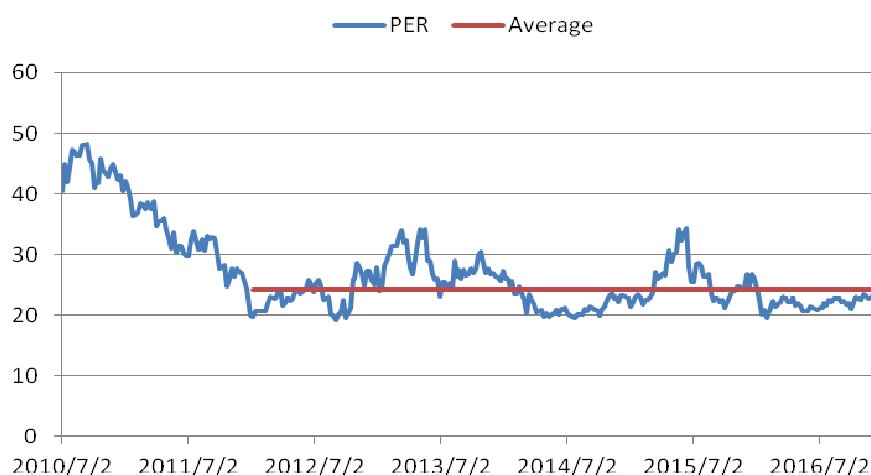
Second, the main second-line products are likely to enter the new Medical Insurance Drug Reimbursement List and sell quickly, which will mitigate the company's risk resulting from over-dependence on a single variety. Bivalirudin has become the preferred anti-coagulant drugs for PCI operations in the new version of guidelines, and its clinical status has exceeded heparin. Allisartan isoproxil, which belongs to New Drug Class 1.1, can be hydrolyzed into antihypertensive active substances in the gastrointestinal tract and absorbed without going through liver metabolism, thus imposing only small burden on liver and safer to the elderly. If Allisartan isoproxil makes the reimbursement list, its future revenue is likely to exceed RMB500 million.

In addition, the company accepted the assignment of 69.52% equity of Alain Medical for RMB129 million, for the improvement of its layout in cerebrovascular sector and peripheral vessel sector. The main products of Alain Medical are cerebral artery drug-eluting stent (in clinical follow-up stage) and lower limb arterial drug-eluting stent (in preclinical research stage), which possess optimistic market potential and is expected to become one of the growth points.

Valuation at Record Low

Generally, the company's growth hit the bottom in 2016, but will speed up in 2017 when the preparations business boosts. Meanwhile, the API business anticipates stable development. And the valuation of the company was only around 20x, at record low and the bottom of the industry counterparts. In light of the result improvement, we give an estimation of 24x EPS in 2017 with a target price of RMB36.70, with the "Buy" rating initially. (Closing price as at 8 Feb 2017)

Historical P/E Valuation



Source: Bloomberg, Phillip Securities (HK) Research

Peer Comparison

Stock code	Company	MV(CNY:mn)	PE-TTM	PE-2016F	PE-2017F	PB
002294.SZ	Salubris	30,376	21.78	20.77	17.92	6.07
600276.SH	Hengrui medicine	113,288	44.80	42.09	34.10	9.66
600521.SH	Huahai Pharma	22,634	45.97	41.92	32.54	5.61
000963.SZ	Huadong Pharma	37,043	27.14	26.42	21.61	5.27
002262.SZ	Nhwa-group	13,402	45.18	42.72	33.75	6.57
600196.SH	Fosun Pharma	60,971	22.43	21.27	17.76	3.14
	Average		37.10	34.88	27.95	6.78

Source: Wind, Phillip Securities (HK) Research

Risks

Persistent risk of single product;
Expansion of second-line market below expectations;
R&D progress of new products below expectations.

Financials

Periodicity:	2013	2014	2015	2016F	2017F
Valuation Ratios					
Price Earnings	36.59	29.22	24.00	21.83	18.98
Price to Book	9.71	8.04	6.62	5.67	4.85
Dividend Yield	1.63%	1.52%	1.71%	1.71%	1.71%
Per share data(CNY)					
EPS Adjusted	0.79	0.99	1.21	1.33	1.53
Book Value Per Share	2.99	3.61	4.39	5.12	5.99
Dividends Per Share	0.47	0.44	0.50	0.50	0.50
Growth & Margin					
Revenue growth	27.19%	23.92%	20.67%	11.85%	13.84%
Gross profit growth	29.17%	20.14%	21.19%	12.18%	12.76%
Net profit growth	30.71%	25.51%	21.45%	10.20%	14.22%
Gross Margin	75.36%	73.07%	73.38%	73.60%	73.85%
Operating Margin	41.39%	41.19%	42.36%	41.90%	42.25%
Net Profit Margin	36.23%	36.70%	36.94%	36.39%	36.67%
Dividend Payout Ratio %	47.24%	44.03%	49.59%	49.62%	49.68%
Key ratios					
Return on Assets	25.07%	25.24%	25.31%	23.73%	22.91%
Return on Equity	28.97%	30.17%	30.25%	27.17%	26.18%
Liability ratio	13.95%	17.94%	12.83%	12.50%	12.50%
Effective Tax Rate	14.66%	14.29%	14.87%	15.00%	15.00%
Income Statement(CNY: mn)					
Revenue	2,292	2,840	3,427	3,833	4,363
- Cost of Goods Sold	565	765	912	1,012	1,141
Gross Income	1,727	2,075	2,515	2,821	3,222
- Selling, General & Admin Expense	779	905	1,063	1,215	1,379
Operating Income	949	1,170	1,452	1,606	1,844
- Net Non-Operating Losses (Gain)	-29	-48	-38	-40	-45
Pretax Income	976	1,217	1,491	1,646	1,889
- Income Tax Expense	143	174	222	247	283
Income Before XO Items	833	1,043	1,270	1,399	1,605
- Minority Interests	3	1	4	4	5
Net Profit	830	1,042	1,266	1,395	1,600

Source: Company, Phillip Securities (HK) Research Estimates
(Financial figures as at 8 Feb 2017)

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

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