

# China Resources Sanjiu (000999.CH)

## Outward Expansion Will Drive New Growth Points

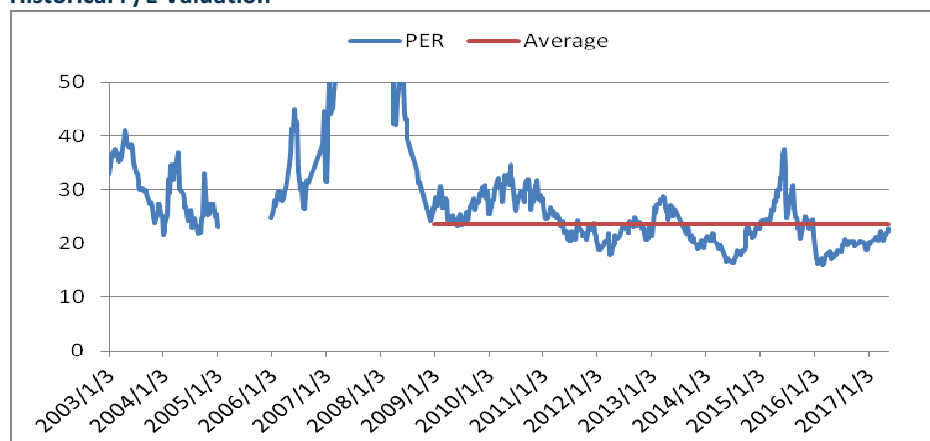
China | Pharmaceutical | Company report

17 May 2017

### Investment Summary

China Resources Sanjiu (CR Sanjiu) is a leader in domestic OTC field with certain brand bargaining power. In the future, the company intends to provide more plentiful products to raise prices moderately and enhance brand positioning. Meanwhile, the company has successfully finished the adjustment of product structure. The proportion of prescription drugs has continued to increase, and TCM formula granules and Xuesaitong soft capsule will have sound development prospect. With strong channels and terminal resources, the cooperation with Sanofi is expected to bring new growth point for the company, and the future M&A expansion in the field of big health is also worth the wait. We give the company an estimation of 24x EPS in 2017, with a target price of MRB35.38 and "Accumulate" rating initially. (Closing price as at 15 May 2017)

### Historical P/E Valuation



Source: Bloomberg, Phillip Securities (HK) Research

### Peer Comparison

Ticker	Company	MV (CNY: mn)	PE-2017F	PE-2018F	PB
600276.SH	Hengrui Medicine	132,631	42.15	34.79	10.05
600518.SH	Kangmei Pharmaceutical	103,595	25.05	20.44	3.44
600196.SH	Fosun Pharma	73,924	23.46	20.06	3.33
002411.SZ	Bocon Pharmaceutical	41,372	31.75	24.41	4.88
600332.SH	Baiyunshan	42,724	24.48	20.61	2.50
000538.SZ	Yunnan Baiyao	91,383	26.90	23.40	5.55
600535.SH	Tasly	43,878	28.85	24.39	5.30
600085.SH	Tongrentang	43,215	41.00	36.32	5.35
	<b>Average</b>		<b>30.46</b>	<b>25.55</b>	<b>5.05</b>
<b>000999.SZ</b>	<b>CR Sanjiu</b>	<b>29,083</b>	<b>20.16</b>	<b>17.01</b>	<b>3.38</b>

Source: Wind, Phillip Securities (HK) Research

### First Quarter Results Benefited from Outward M&A

The revenue and net profit attributable to shareholders of the company in the first quarter of 2017 were RMB24.6 and RMB370 million, respectively, up 15.2 and 20% yoy, equivalent to earnings per share of MRB0.38, which is in line with expectations.

### Accumulate (Initially)

CMP: CNY 29.71

(Closing price as at 15 May 2017)

TARGET: CNY 35.38 (+19.1%)

### COMPANY DATA

O/S SHARES (MN) :	979
MARKET CAP (CNYMN) :	29,083
52 - WK HI/LO (CNY):	29.88/21.67

### SHARE HOLDING PATTERN, %

CR Pharmaceutical :	63.60
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### PRICE PERFORMANCE, %

	1M	3M	1Y
CR Sanjiu	6.10	12.64	29.65
HS300	11.92	16.18	20.92

### PRICE VS. HS300



Source: Phillip Securities (HK) Research

### KEY FINANCIALS

CNY mn	FY15	FY16	FY17E	FY18E
Net Sales	7790	8831	10309	11762
Net Profit	1249	1198	1443	1710
EPS, CNY	1.28	1.22	1.47	1.75
PER, x	23.21	24.35	20.16	17.01
BVPS, CNY	7.73	8.80	10.11	11.68
P/BV, x	3.84	3.38	2.94	2.54
ROE, %	17.43	14.80	15.41	15.87
Debt/Equity (%)	56.6	55.4	56.3	56.3

Source: Company reports, Phillip Securities Est.

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The results of the first quarter significantly outperformed the negative growth in 2016, mainly attributable to Shenghuo Pharmaceutical's inclusion into the consolidated statements in September 2016. In addition, the company has achieved steady growth in original business such as TCM granules and OTC business. Moreover, the cost control of the company was effective. The marketing expense and administrative expense ratio were 35.9% and 6.9%, respectively, down 0.6 percentage point and 2.9 percentage points compared to those in 2016. On the whole, the company's profitability remained stable, with the gross margin and the net profit margin maintaining at approximately 62% and 15%, respectively.

## Outward Expansion Will Drive New Growth Points

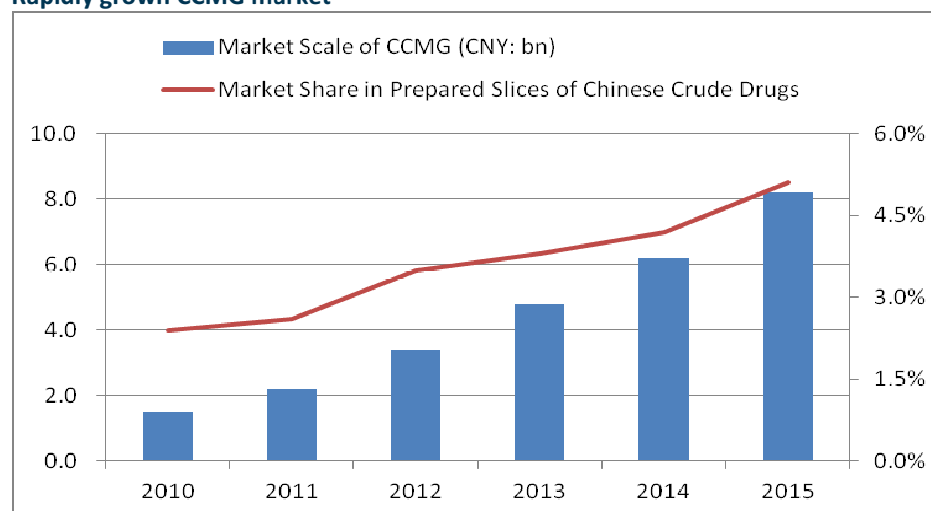
In 2016, the company completed 100% stake acquisition of Kunming Shenghuo Pharmaceutical which specializes in cardiovascular and cerebrovascular drugs. The main products of Shenghuo Pharmaceuticals include Xuesaitong soft capsules and Huangtengsu soft capsules, forming a complementation with Shenfu injection of the company. It is worth noting that its main product "Lixuwang" Xuesaitong soft capsules was included into 2017 NDRL, so the sales expansion in the future is expected to be accelerated.

The company also signed the Framework Agreement of Cooperation in China to Carry out Consumer Healthcare Business with Sanofi to jointly develop the health consumer goods market in China and set up a joint venture specializing in pediatric and gynecological non-prescription products in China. In addition, the company is selling Sanofi products as a sales agent. Since the beginning of January, the company has become an omni-channel agent of Sanofi's liver product Yishanfu that ranks the forefront in the world, and will gradually introduce its global OTC varieties in the near future. It is believed that Sanofi's pediatric drug brand "Goodbaby", gynecological drug brand "Kangfute" and liver medicine "Yishanfu" will form a good complementation with the company's OTC products and channels, and bring new growth point for the company.

## TCM Formula Granules Business Will Grow Rapidly

At present, the domestic business of TCM formula granules only accounts for 5.1% of Chinese herbal pieces business, far behind the rest of the Asia-Pacific region. In addition, TCM granules will extend to secondary hospitals and grassroots hospitals, therefore the prospects for development is broad. At present, CR Sanjiu is approximately occupying a market share of 14%, ranking second in the market. The company is capable of producing about 640 kinds of single-flavor dispensing granules, possessing a certain competitive advantage. The company will also utilize the Chinese intelligent pharmacy and actively promote the sale of TCM formula granules. This business is expected to maintain a growth rate of more than 20%, being one of the main driving forces for prescription drugs.

### Rapidly grown CCMG market



Source: Phillip Securities (HK) Research

## Risks

The pace of M&A integration was not optimistic as expected;  
The business of traditional Chinese medicine injection has continued to decline.

## Financials

Periodicity:	2014	2015	2016	2017F	2018F
<b>Valuation Ratios</b>					
Price Earnings	28.03	23.21	24.35	20.16	17.01
Price to Book	4.30	3.84	3.38	2.94	2.54
Dividend Yield	1.37%	0.50%	0.54%	0.61%	0.71%
<b>Per share data(CNY)</b>					
EPS Adjusted	1.06	1.28	1.22	1.47	1.75
Book Value Per Share	6.91	7.73	8.80	10.11	11.68
Dividends Per Share	0.41	0.15	0.16	0.18	0.21
<b>Growth &amp; Margin</b>					
Revenue growth	-	8.54%	13.36%	16.74%	14.09%
Gross profit growth	-	8.20%	15.78%	18.01%	12.87%
Net profit growth	-	20.59%	-4.11%	20.46%	14.82%
Gross Margin	60.82%	60.63%	61.93%	62.60%	63.00%
Operating Margin	16.55%	16.08%	14.48%	15.10%	16.00%
Net Profit Margin	14.43%	16.04%	13.56%	14.00%	14.54%
Dividend Payout Ratio %	38.49%	11.72%	13.11%	12.21%	12.02%
<b>Key ratios</b>					
Return on Assets	10.04%	11.01%	9.37%	9.89%	10.16%
Return on Equity	16.26%	17.43%	14.80%	15.41%	15.87%
Liability ratio	34.42%	36.15%	35.64%	36.00%	36.00%
Effective Tax Rate	14.88%	16.63%	16.89%	16.80%	16.80%
<b>Income Statement(CNY: mn)</b>					
<b>Revenue</b>	<b>7,177</b>	<b>7,790</b>	<b>8,831</b>	<b>10,309</b>	<b>11,762</b>
- Cost of Goods Sold	2,812	3,067	3,362	3,856	4,352
<b>Gross Income</b>	<b>4,365</b>	<b>4,723</b>	<b>5,469</b>	<b>6,454</b>	<b>7,410</b>
- Selling, General & Admin Expenses	3,177	3,471	4,190	4,897	5,528
<b>Operating Income</b>	<b>1,188</b>	<b>1,253</b>	<b>1,279</b>	<b>1,557</b>	<b>1,882</b>
- Interest Expense	28	28	28	30	32
- Net Non-Operating Losses (Gains)	-102	-302	-200	-220	-220
Pretax Income	1,260	1,529	1,453	1,749	2,072
- Income Tax Expense	187	254	245	294	348
Income Before XO Items	1,072	1,275	1,208	1,455	1,724
- Minority Interests	36	25	10	12	14
<b>Net Profit</b>	<b>1,036</b>	<b>1,249</b>	<b>1,198</b>	<b>1,443</b>	<b>1,710</b>

Source: Company, Phillip Securities (HK) Research Estimates

(Financial figures as at 15 May 2017)

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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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