

China Medical System (867.HK)

Introducing Six Injection Products and Acquiring Elcitonin Rights

30 July 2018

Hong Kong | Pharmaceutical | Company report

Investment Summary

We see stock price decreasing during recent market fluctuation. Expect for market factors, we partly attribute price volatility to unfavorable test results of one key pipeline product (Traumakine). However, we emphasize that R&D will not affect the growth momentum of current portfolio and introduction of new drugs. We maintain previous EPS forecast of RMB0.77/0.86 and TP HKD21, and suggest buying around price bottom. (Closing price at 26 July 2018)

BUY

CMP HKD13.9

(Closing price at 26 July 2018)

TARGET HKD21.0 (+51%)

Introducing of Six Injection Products

On 20 July, CMS entered into an agreement with Venus Pharma to acquire all assets of Venus Pharma's current product portfolio related to China market (involving know-how, all intellectual property or the right of application for the intellectual property, and other rights to commercialize the products in China). There are six main products and all included in Class B content of NDRL, commonly used drugs for clinical anti-tumor therapy and recommended by guidelines. Other two drugs belong to carbapenem antibiotics, having a wide range of antibacterial effects and being used to treat a variety of infections. We know from our checks that these drugs may attain drug import registration certificate within 1 to 1.5 years, and we regard these mid-term drivers for company development.

COMPANY DATA

O/S SHARES (MN)	2,487
MARKET CAP (HKMDN)	34,573
52 - WK HI/LO (HKD)	20.0 / 12.46

SHARE HOLDING PATTERN, %

Director Lam Kong	43.53
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PRICE PERFORMANCE, %

	1M	3M	1Y
CMS	-19.47	-26.72	3.78
HIS	26.86	-4.95	6.83

Figure: Six New Injections

Drugs	Function	2017 Market Size in China
Gemcitabine	Non-small cell lung cancer,	>RMB2bn
Docetaxel	pancreatic cancer, breast cancer,	>RMB3bn
Pemetrexed	prostate cancer, etc	>RMB3bn
Bortezomib		>RMB0.6bn
Meropenem	Antibacterial	>RMB4bn
Imipenem		>RMB2.5bn

Source: Company, Phillip Securities

RETURN VS. HSI



Source: Aastocks, Phillip Securities (HK) Research

Acquiring Promotion Rights of Elcitonin

CMS gained exclusive promotion rights of Elcitonin (Elcatonin Injection, an original synthetic calcitonin derivative), dated from Aug 2018. Elcitonin, originally developed by a Japanese pharmaceutical firm Asahi Kasei Pharma, is commonly used anti-osteoporosis drug and also recommended by "Primary Osteoporosis Diagnose and Treatment Guideline (2017)". It has been marketed in China for several years and categorized as Class B of NDRL. Now the number of osteoporosis patients in China exceeds 70mn which means great market potential for development. Asahi Kasei Pharma, headquartered in Tokyo, is a research-based healthcare innovator that discovers, develops, manufactures, and markets pharmaceuticals and diagnostic products that address unmet medical needs. We highlight this cooperation will underpin way for further collaboration between CMS and Asahi Kasei.

KEY FINANCIALS

RMB mn	FY16	FY17	FY18E	FY19E
Net Sales	4,90.8	5,348.8	6,039.8	6,794.2
Net Profit	1,375.9	1,674.8	1,903.6	2,141.3
EPS, RMB	0.55	0.67	0.77	0.86
PER, x	21.84	18.02	15.81	14.06
BVPS, RMB	2.50	2.95	3.41	3.92
P/BV, x	4.84	4.11	3.55	03.08
ROE, %	22.16	22.79	22.47	21.95

Source: Company, Phillip Securities Est.

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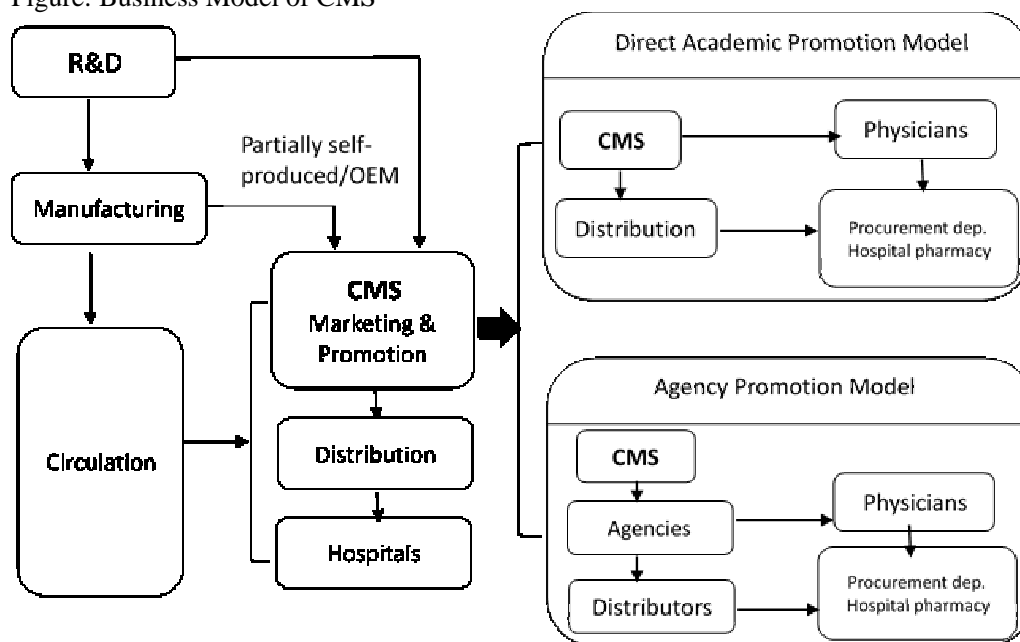
FY17 Results

In 2017, excluding Two-invoice System effect, CMS reported revenue of RMB5578.6mn, +21.2% YoY, GPM saw 1ppt decrease due to ASP down by 1.9pp. We highlight efficient cost control measures, given EBITDA margin increased by 0.7ppt, with percentage of selling/administrative expenses in revenue dropping by 0.8pp. And NPM kept stable. Its payout ratio maintained around 40% intact.

Figure: CMS Product Mix under Direct Academic Promotion Network

Drugs	Function	Year of Introduction	Hospital Coverage	% in Sales	NDRL
Plendil	Hypertension and stable angina pectoris	2016	26,000	24.1%	Yes
Deanxit	Mild to moderate depression and anxiety	1997	21,000	17.7%	Yes
Ursofalk	Cholesterol gallstones in the gallbladder, cholestatic liver disease and biliary reflux gastritis	1998	9,400	17.9%	Yes
XinHuoSu	Acute heart failure	2008	1,900	7.7%	Yes
Salofalk	Ulcerative Colitis and Crohn's disease	2008	3,900	5.5%	Yes
Bioflor	Diarrhea in adults and children	2010	3,000	4.9%	-
Stulln	Senile macula degeneration and asthenopia	2007	7,000	4.1%	-
DanShen-Tong	Antisepsis and anti-inflammation	2015	4,000	2.8%	Yes
Hirudoid	Blunt traumata	2015	6,000	2.4%	PDRL
NuoDiKang	Activating blood circulation, freeing blood vessels, alleviating pain, Coronary heart disease and angina	2015	3,700	1.9%	Yes
Combizym	Dyspepsia	2015	1,300	1.3%	Yes
GanFuLe	Liver cancer, cirrhosis and liver fibrosis	2008	-	0.8%	Yes
Imdur	Anti-ischemic	2016	8,000	0.7%	Yes
Parlodel	Hyperprolactinaemia	2014	1,300	-	Yes
Lamisil	Superficial fungal infection	-	-	-	Yes
Movicol	Constipation	-	-	-	-
Total	-	-	-	92.4%	-

Figure: Business Model of CMS



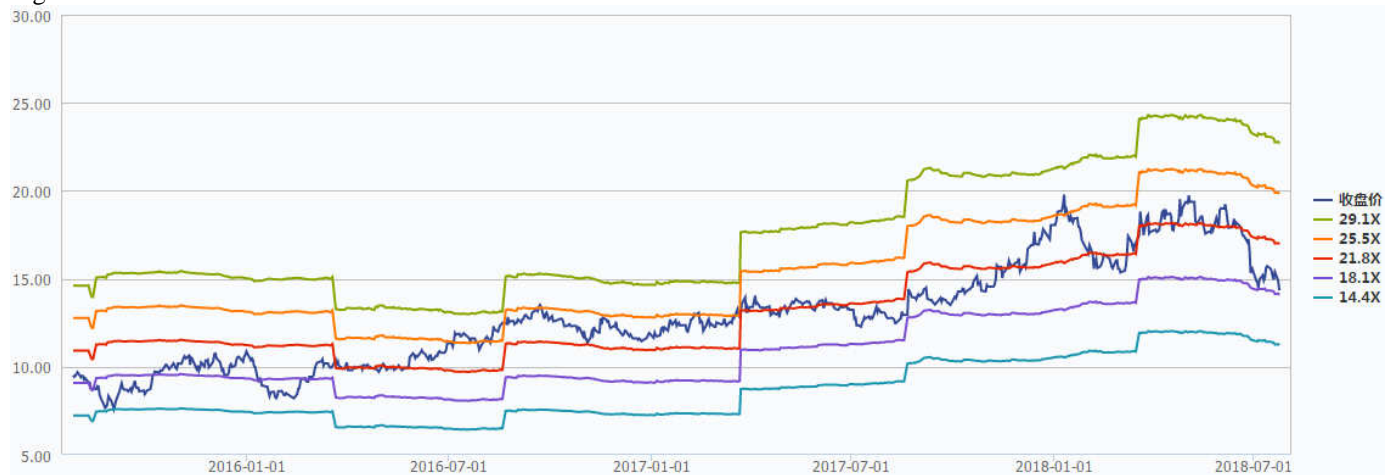
Source: Company, Phillip Securities

Investment Thesis, Valuation & Risk

Our valuation model gives target price of HK\$21.0. We highlight future growth momentum coming from increasing penetration of current hospital coverage and introduction of new drugs. Excluding possible pipeline contribution and new introduction, we assume relatively stable expenses ratios and predict 18E/19E EPS to be RMB0.77/0.86, based on current product mix potential. Thus we give target price of HKD21.0, BUY recommendation. (Exchange rate= 0.8706 RMB/HKD)

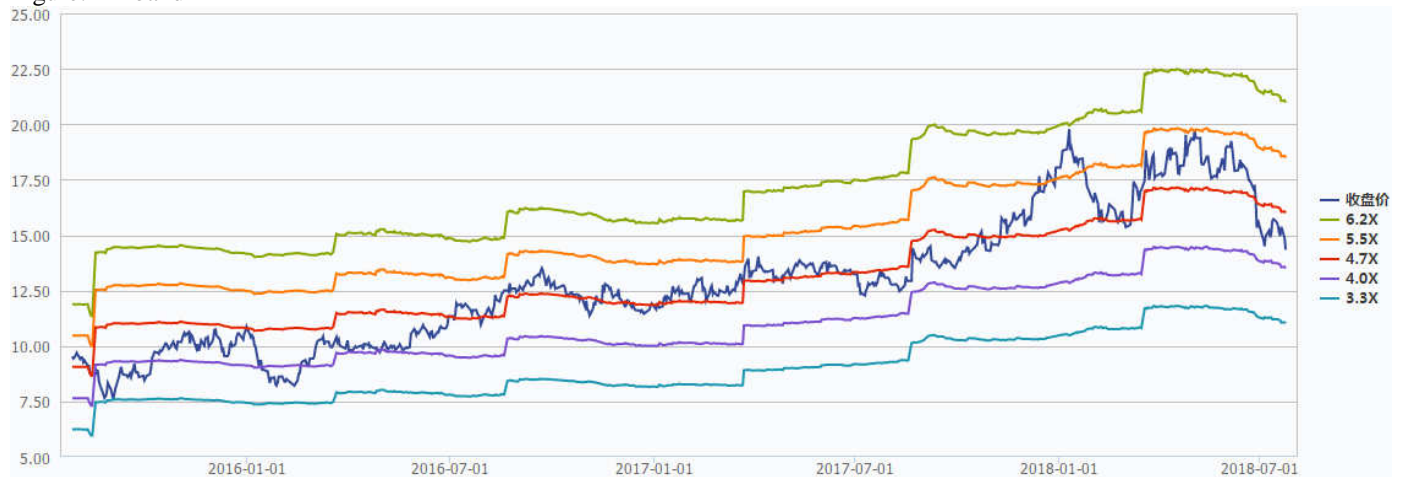
Risks include: R&D fails expectations; Policy risks; Exchange risk; New introduction fails expectation.

Figure: PE band



Source: Wind (as at July 25), Phillip Securities

Figure: PB band



Source: Wind (as at July 25), Phillip Securities

Figure: HK Peers

Code	Firm	Mkt Cap /HKD mn	GPM		NPM		2017 ROE (%)	PE			EPS		
			FY17	FY16	FY17	FY16		TTM	18E	19E	17A	18E	19E
0867.HK	康哲藥業	35580.35	65.03	59.42	31.22	28.1	24.84	17.8	15.72	13.35	0.78	0.91	1.07
	Max	139433.90	88.99	92.52	53.61	52.13	64.2	561.33	41.76	33.41	9.33	2.17	2.58
	Medium	13755.17	60.44	56.55	19.51	18.83	17.02	21.61	18.38	16.12	0.34	0.49	0.55
	Average	32154.94	57.83	56.23	17.17	14.57	18.72	56.94	21.93	18.28	0.9	0.77	0.91
1177.HK	中國生物製藥	139433.90	79.14	79.2	24.59	20.09	26.1	47.4	41.76	33.41	0.34	0.26	0.33
1093.HK	石藥集團	130784.41	60.44	51	17.82	16.94	21.79	43.09	36.11	28.38	0.44	0.58	0.74
2196.HK	復星醫藥	109026.97	58.56	53.68	19.51	22.17	13.18	24.89	22.54	18.76	1.46	1.7	2.05
3320.HK	華潤醫藥	72221.37	16.39	15.39	3.95	3.78	8.76	20.79	17.72	15.35	0.53	0.65	0.75
1513.HK	麗珠醫藥	35033.64	63.31	63.52	52.83	11.02	51.26	4.9	22.27	19.32	9.33	1.71	1.97
2005.HK	石四藥集團	22941.06	58.74	51.56	21.58	20.76	21.61	34.6	26.19	20.7	0.23	0.29	0.37
1558.HK	東陽光藥	17991.83	82.49	77.25	39.1	40.42	24.58	23.3	18.38	15.42	1.65	2.17	2.58
0512.HK	遠大醫藥	15124.61	51.97	46.87	10.16	7.27	23.41	32.9	23.43	18.71	0.2	0.23	0.28
0460.HK	四環醫藥	14833.42	72.36	68.71	53.61	52.13	13.2	8.58	8.74	8.05	0.18	0.18	0.19
3933.HK	聯邦製藥	12676.92	36.6	35.63	1.19	-4.39	1.57	129.93	16.72	16.12	0.06	0.46	0.48
0940.HK	中國動物保健品	10198.27	--	62.34	--	7.77	--	561.33	--	--	--	--	--
0950.HK	李氏大藥廠	5191.28	67.66	71.87	19.91	24.19	13.66	20.3	18.01	15.92	0.38	0.49	0.55
0719.HK	新華製藥股份	5028.37	27.1	23.99	4.97	3.36	9.38	11.35	--	--	0.52	--	--
2348.HK	東瑞製藥	3616.06	63.63	62.05	33.05	32.23	17.02	10.34	--	--	0.42	--	--
1061.HK	億勝生物科技	3605.70	81.99	80.32	18.6	17.57	25.81	21.61	17.5	14.1	0.29	0.36	0.45
1349.HK	復旦張江	3406.79	88.99	92.52	12.06	20.87	8.78	37.92	--	--	0.09	--	--
2633.HK	雅各臣科研製藥	3260.17	39.88	44.34	13.22	14.42	10.86	16.16	--	--	0.1	--	--
1652.HK	福森藥業	1699.85	55.67	50.27	21.33	21.53	64.2	14.71	--	--	0.18	--	--
8037.HK	中國生物科技服務	1443.74	28.73	34.71	-72.55	-68.86	-24.23	--	--	--	-0.08	--	--

Source: Wind (as at July 25), Phillip Securities

Financials

FYE	FY2015	FY2016	FY2017	FY2018E	FY2019E
Valuation Ratios					
Price to Earnings (P/E)	29.97	21.84	18.02	15.81	14.06
Price to Book (P/B)	5.68	4.84	4.11	3.55	3.08
Per Share Data					
EPS (RMB Cents)	40.37	55.40	67.14	76.53	86.09
Book Value Per Share (RMB)	2.13	2.50	2.95	3.41	3.92
Dividend Per Share (RMB Cents)	16.16	22.43	26.86	30.61	34.44
Growth (%)					
Revenue	20.65	37.92	9.14	12.92	12.49
Operating Income	21.32	48.11	24.72	9.85	12.49
Net Profit	-4.46	38.28	21.19	13.99	12.49
Margins (%)					
Gross Profit Margin	57.58	59.42	65.03	64.50	64.00
Operating Profit Margin	29.74	31.93	36.49	35.50	35.50
Net Profit Margin	28.04	28.12	31.22	31.52	31.52
Key Ratios					
ROE (%)	18.95	22.16	22.79	22.47	21.95
ROA (%)	17.62	16.99	16.45	15.73	15.36
Income Statement (RMB Mn)					
Revenue	3,553.4	4,900.8	5,348.8	6,039.8	6,794.2
- Cost of Goods Sold	1,507.3	1,988.9	1,870.5	2,144.1	2,445.9
Gross Income	2,046.1	2,911.9	3,478.3	3,895.7	4,348.3
- Operating Expenses	989.4	1,346.9	1,604.1	1,751.5	1,936.3
Operating Income	1,056.7	1,565.0	1,951.9	2,144.1	2,411.9
+ Net Non-Operating Gain/Loss	7.4	(64.6)	82.3	75.0	84.4
Pretax Income	1,064.1	1,500.4	1,808.4	2,069.1	2,327.5
- Income Tax Expenses	(67.6)	(122.5)	(138.5)	(165.5)	(186.2)
Net Profit	995.9	1,375.9	1,674.8	1,903.6	2,141.3

Source: Wind, Phillip Securities (HK) Research Estimates

Exchange rate is 0.8706 RMB/HKD (1YHKDRMB future price on July 26).

(Financial figures as at 26 July 2018)

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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