

SINOPHARM ACCORD (000028.SZ)

Leading Company in Pharmaceutical Industry, “Wholesale and Retail Integration” Boost Growth

China | Pharmaceuticals | Company Report

26 June 2019

Investment Summary

Leading enterprise in pharmaceutical industry, continue to promote the “Wholesale and Retail integration” strategy

The company is a comprehensive pharmaceutical listed company under the China National Pharmaceutical Group and Sinopharm Group, and it is the leading enterprise in pharmaceutical industry of the country. After the completion of major asset restructuring in 2016, the company actively promoted the “wholesale and retail integration” strategy, made full use of the commercial platform with mature distribution and the terminal advantageous network with wide retail sales to extend the commodity to the retail terminal through effective resource integration means and give play to the scale effect so as to achieve the synergistic interaction between distribution and retail, continue to further promote the distribution business in Guangdong and Guangxi, and expand the layout of retail pharmacies. In 2018, the sales revenue of wholesale and retail synergy was RMB590 million, a YoY increase of 75%.

Improve distribution network, transformation and innovation of distribution business

The company’s distribution business is concentrated in the Guangdong and Guangxi provinces, with Sinopharm Group Guangzhou/Guangxi companies as the core companies, ranking the first in the two markets, comprehensively covering the Grade-III and Grade-II medical institutions and retail chain terminals in Guangdong and Guangxi, covering more than 4,000 medical institutions. With the changes in the market environment, the company has transformed and innovated in the distribution field, and actively expanded its business development areas, clearly focused on the development of four business directions including retail direct sales, equipment consumables, retail diagnosis and treatment, and primary care. The company has improved supply chain management efficiency and reduced operating costs to ensure that earnings are growing through informatization reform. In 2018, the retail direct sales increased by 34% YoY, equipment consumables increased by 29% YoY, retail diagnosis and treatment increased by 49% YoY, and primary care increased by 17% YoY.

Build a “new Guoda”, continue to promote internationalization

As a large-scale pharmaceutical retail enterprise in China, Guoda Drugstore has 28 regional chain companies and established the logistics and distribution network including Shanghai National Logistics Center and 23 provincial and municipal distribution centers. Guoda Drugstore ranked the first among the China pharmaceutical retailers for seven consecutive years since 2011. According to the “Statistical Analysis Report on the Operation of Drug Circulation Industry in 2017” by the Ministry of Commerce, the total sales of Guoda Drugstore in 2017 was RMB11.08 billion, a YoY increase of 7.48%, leading 21.49% to second-class Beijing Tongrentang (RMB9.12 billion). As of drug retail market of RMB400.3 billion in 2017, the market share of Guoda Drugstore was 2.8%, which was the same as in previous years. In July 2018, Guoda Drugstore completed the introduction of Walgreens Boots Alliance (WBA), and became a Chinese-foreign joint venture after the equity transfer.

Initial coverage with TP of RMB 50.29 and investment rating of “BUY”

Based on our SOTP valuation model, we initiate coverage on Sinopharm Accord with 16.13x/14.11x/12.50x FY19/FY20/FY21 PER, corresponding to TP RMB 50.29 with a 21.0% potential upside compared with current price RMB 41.56 as of June 24, 2019, and recommend “BUY” investment rating.

BUY (Initial)

CMP RMB 41.56

(Closing price at 24 June 2019)

TARGET RMB 50.29 (+21.0%)

COMPANY DATA

O/S SHARES (MN)	428
MARKET CAP (RMBMN)	17,793
52 - WK HI/LO (RMB):	52.70/37.79

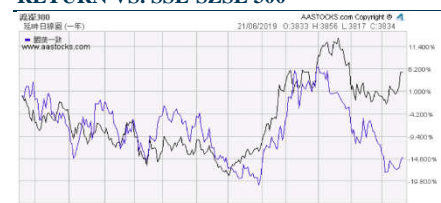
SHARE HOLDING PATTERN , %

Sinopharm Group Co., Ltd.	56.06
HK Securities Clearing Company Ltd	3.39

PRICE PERFORMANCE , %

	1M	3M	1Y
SINOPHARM	-6.42	-16.88	-15.39
ACCORD			
SSE-SZSE 300	6.88	2.63	7.89

RETURN VS. SSE-SZSE 300



Source: Phillip Securities (HK), aastocks

KEY FINANCIALS

RMB mn	FY 17	FY 18	FY 19E	FY 20E	FY 21E
Revenue	41,263	43,122	45,989	49,718	53,122
Net Profit for owners	1,058	1,211	1,335	1,526	1,711
EPS, RMB	2.47	2.83	3.12	3.56	4.00
PER, x	16.82	14.70	13.33	11.66	10.14
BVPS, RMB	21.95	27.14	29.84	32.92	36.11
P/BV, x	1.89	1.53	1.39	1.26	1.15
ROE, %	11.26%	10.42%	10.45%	10.83%	11.36%

Source: Company reports, Phillip Securities Est.

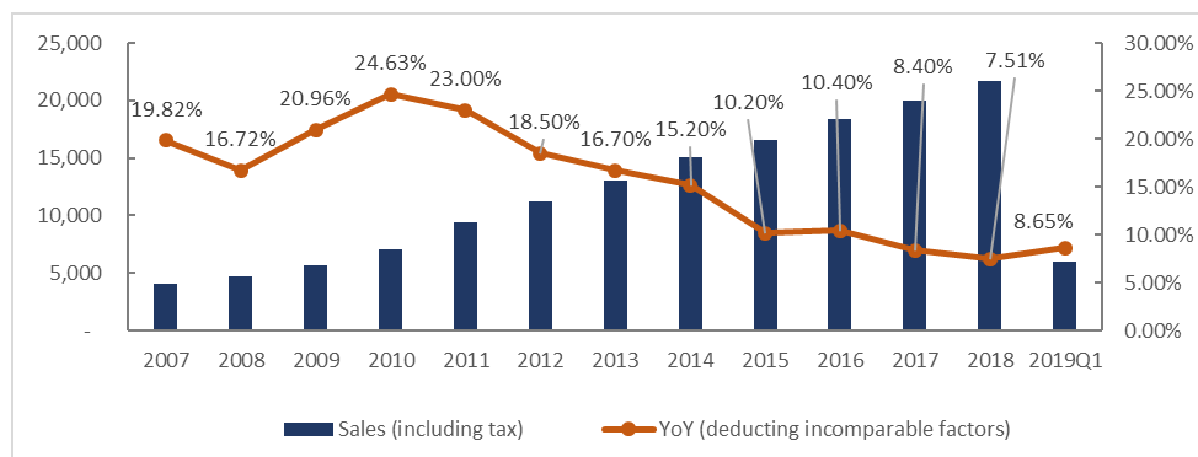
Research Analyst
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Industry Analysis

The scale of the pharmaceutical circulation market has grown steadily

According to the Ministry of Commerce's Drug Circulation Statistics System, the total sales of the seven major categories of pharmaceutical products in the first quarter of 2019 was 596.6 billion RMB (including tax), showing an increase of 8.65% YoY deducting incomparable factors, and the growth rate was 0.72% higher than the same period of last year. The sales of retail market was 119.3 billion RMB, a YoY increase of 9.70%, growth rate increased by 0.6%. Among them, the income of pharmaceutical circulation direct reporting enterprises (total 1071 enterprises) was 426.8 billion RMB (excluding tax), after deducting incomparable factors, the growth rate was 9.63% YoY, growth rate increased by 0.93%; the profit was 7.3 billion RMB, representing an increase of 8.84% YoY deducting incomparable factors, growth rate increased by 5.62%; the average gross profit margin was about 8.45%, an increase of 1.07%; the average expense rate was 6.88%, increasing by 0.71% YoY; the average profit rate was about 1.71%, remaining the same with last year. In 2018, the total sales of seven major categories of pharmaceutical products was 2,168.8 billion RMB (including tax), representing an increase of 7.51% YoY deducting incomparable factors, growth rate decreased by 1.03%. The pharmaceutical retail market's sales were 433.8 billion RMB, a YoY increase of 8.88%, growth rate dropped by 0.07%. Overall, the scale of the pharmaceutical circulation market maintained steady growth. From 2007 to 2018, the compound annual growth rate of the market scale reached 16.54%. Although the growth rate has declined slightly in recent years, the overall growth trend remains stable.

Figure-1: The Scale of Pharmaceutical Circulation Market (in `00 mn RMB) and Growth Rate



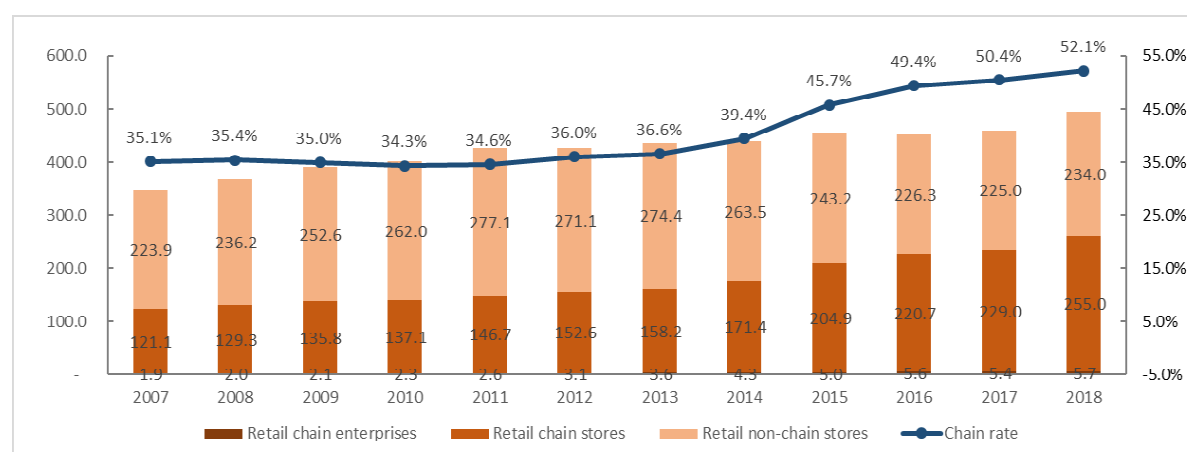
Source: Phillip Securities (HK) Research, Ministry of Commerce, "Statistical Analysis Report on the Operation of Drug Circulation Industry";

Industry concentration has a large room for improvement

According to the overall goal of the National Drug Circulation Industry Development Plan (2016-2020), by 2020 there will be a number of intensive, informatized and large-scale drug circulation enterprises with a network coverage of the whole country: the annual sales of the top 100 wholesale enterprises will account for more than 90% of the total pharmaceutical wholesale market, the annual sales of the top 100 pharmaceutical retailers will account for more than 40% of the total retail market, and the retail chain rate will exceed 50%. This plan also encourages the implementation of wholesale and retail integration, chain management and multi-business mixed operations. At present, the target of the drug retail chain rate has been completed ahead of schedule. According to the "Food and Drug Regulatory Statistics Annual Report" issued by the CFDA, as of the end of November 2018, there were 5,671 drug

retail chain enterprises nationwide, an increase of 262 compared with last year; 2.55 million retail chain stores, an increase of 26 thousand stores compared with last year; 234 thousand retail pharmacies, an increase of 9 thousand pharmacies compared with last year; the retail chain rate of pharmacies is 52.1%, an increase of 1.7% compared with last year. It is expected that in the situation of pharmaceutical circulation management becoming stricter, the scale effect gradually becoming prominent and the industry's normative improvement, the pharmacy retail chain rate will continue to rise.

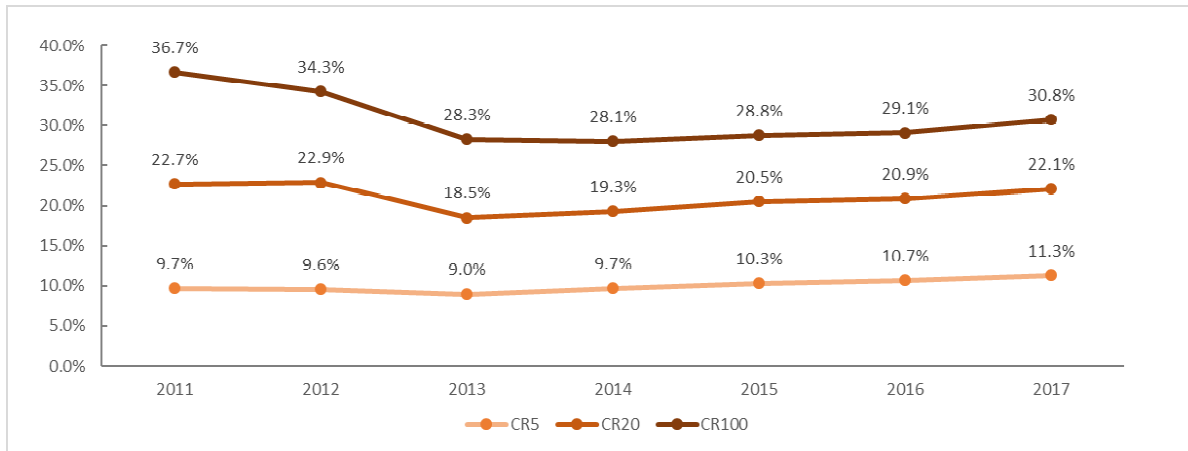
Figure-2: The Number of Retail Drug Stores (in thousand) and Chain Rate



Source: Phillip Securities (HK) Research, CFDA 2007-2018 Annual Reports on Food and Drug Administration Statistics;

According to the “Statistical Analysis Report on the Operation of Drug Circulation Industry in 2017” issued by the Department of Market Supervision of the Ministry of Commerce, the retail pharmaceuticals industry is still relatively fragmented. In the top 100 pharmaceutical retailers ranking by sales in 2017, there were a total of 58,355 retail stores, accounting for 12.9% of the market. The total sales were 123.2 billion RMB, accounting for 30.75% of the whole retail market, increasing by 15.04% YoY and exceeding 30% for the first time. The industry's leading Sinopharm Group Guoda Drugstore's sales in 2017 was 11.08 billion RMB, based on the total estimate of 2017 drug retail market 400.3 billion RMB, the industry's leading enterprise's market share was only 2.8%. Combined analysis with the pharmacy chain rate, since 2015, the retail pharmacy chain rate has increased rapidly, and in 2017 it broke through 50% for the first time. We believe that chain pharmacies have scale effect and management advantages, especially in terms of procurement costs, expense control, personnel management, overall planning and city coverage rate. Compared with the chain rate of US retail pharmacy market, CVS, Walgreens and Rite Aid - three chain drugstore giants account for more than 75% of the US market share, while in 2017 China's pharmaceutical retail industry CR5 is only 11.3%, the scale of leading enterprises is relatively small. It is expected that there will be large room for improvement in the chain rate and concentration of retail pharmacies in China in the future.

Figure-3: 2011-2017 Pharmaceuticals Retail Concentration of China

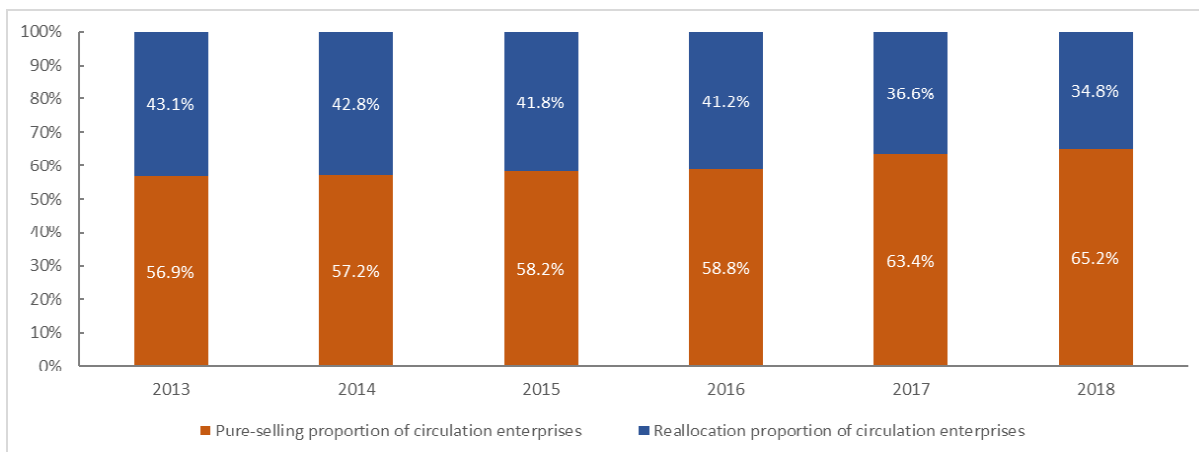


Source: Phillip Securities (HK) Research, "Statistical Analysis Report on the Operation of Drug Circulation Industry in 2017";

Two-vote system promotes industry integration

The "two-vote system" in the field of pharmaceutical circulation means that the pharmaceutical production enterprises directly invoice to the circulation enterprise, and the circulation enterprise re-invoices (delivery) to the hospital, and invoices are issued twice. Under the influence of the "two-vote system", the pure-selling and reallocation business have polarized. The pure-selling business grows rapidly due to the "two-vote" medical reform policy, and the reallocation business, in which the intermediaries transfer inventories to the sub-distributors, has a smaller proportion of business, leading to a further decline in industry sales growth. In addition, as the "two-vote system" brings greater capital turnover pressure to enterprises, M&A integration in the pharmaceutical commerce sector will become a new development trend. We believe that with the implementation of the national health reform policy and the enhancement of capital, the concentration and chain rate of the pharmaceutical circulation industry will further increase in the future.

Figure-4: 2013-2018 the Proportion of Pure-Selling and Reallocation Businesses of Circulation Market



Source: Phillip Securities (HK) Research, Qianzhan industrial research;

Company Analysis

Company Profile

The company is a comprehensive pharmaceutical listed company under the China National Pharmaceutical Group and Sinopharm Group (stock code: 000028, 200028), which has a national cross-regional pharmaceutical retail chain brand “Guoda Drugstore”. The company has established 29 regional chain companies in 19 provinces, autonomous regions and municipalities in China, covering nearly 70 large- and medium-sized cities with over 4,000 retail pharmacies. In 2019Q1, the revenue was RMB11.879 billion, with a YoY increase of 15.82%; net profit contributed to owners was RMB300 million, an increase of 2.53% YoY; net profit contributed to owners after deduction of non-recurring profit or loss was RMB297 million, an increase of 4.36% YoY. In 2018, the revenue was RMB43.122 billion, with a YoY increase of 4.51%; net profit contributed to owners was RMB1.211 billion, an increase of 14.46% YoY.

Since 2016, the company has located as the national pharmaceutical retail integration platform under the China National Pharmaceutical Group. It has completed the integration and reorganization with the Guoda Drugstore and realized the strategic transformation and upgrade of “National Retail + Guangdong-Guangxi Distribution + Industrial Investment”. The company’s distribution is willing to create “the leading pharmaceutical distribution and supply chain service provider in Southern China”, relying on the deep distribution and delivery network of the Southern Region. The company is the manufacturer and supplier of domestic and foreign pharmaceuticals, medical devices, consumables and other health care products. And it also provides comprehensive distribution, logistics and other value-added services to downstream hospitals, other distributors, retail pharmacies, primary care providers and other customers. At the same time, the company has transformed itself into a leading provider of pharmaceutical supply chain solutions, integrating innovation in the supply chain and the Internet in health-related industries such as medicine and medical care, and exploring the coordinated development of diversified businesses. At present, the network of professional prescription chain pharmacies has been managed in a direct manner in major cities in Guangxi and Guangdong Province, and new drug special drugs, chronic disease drugs and large health products have been sold to terminal consumers. Meanwhile, Guoda Drugstore actively carried out chronic disease management services such as diabetes and high blood pressure and actively docked the “Internet +” service, initiating the health service APP and the construction of online health community. In the past seven years, Guoda Drugstore constantly ranked the first in the pharmaceutical retail industry in China.

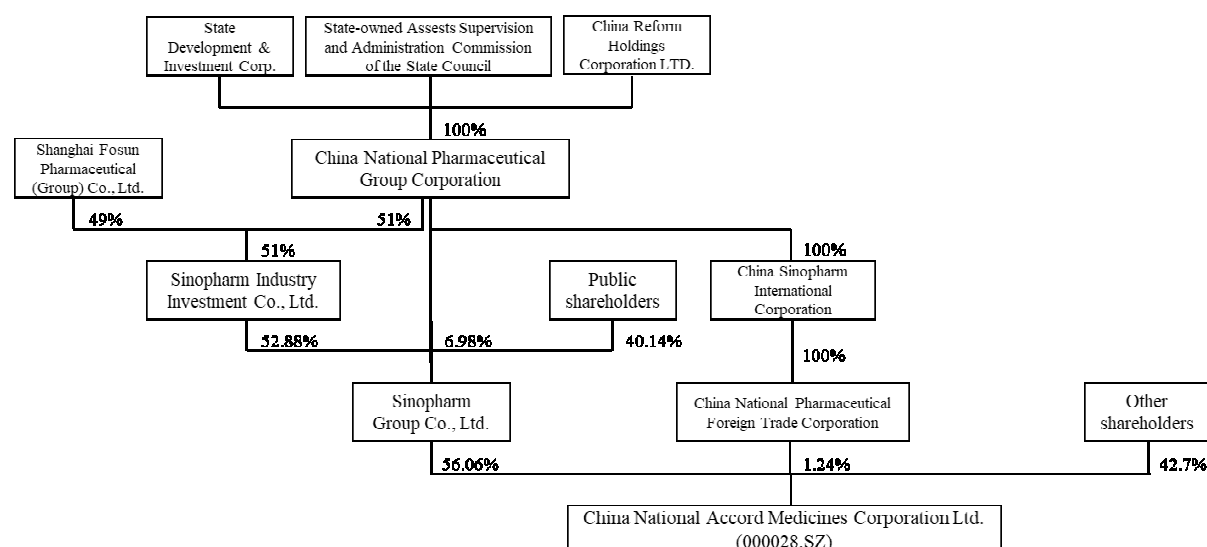
Table-1: Key Milestones

Year	Milestones
1985	Establishment of the company’s predecessor, Shenzhen Medicine Production & Supplies Head Company Inc.
2000	Rename as Shenzhen Accord Pharmaceutical Co., Ltd. after restructured listed
2004	Sinopharm Group has a 43.33% stake and has become the company’s largest shareholder
2006	Acquisition of 90% equity of Sinopharm Group Guangzhou Co., Ltd. to form the Southern distribution network as the core enterprise
2007	Establishment of Guangdong Accord Drugstore Co., Ltd. to form an integrated operation system for cross-regional retail chains
2008	Establishment of Sinopharm Group Foshan Co., Ltd. Awarded as the Guangdong Pharmaceutical Industry Innovation Enterprise Award and the Guangdong Pharmaceutical Industry Outstanding Contribution Enterprise Award for 30 years of Reform and Opening
2009	Acquisition of 75% equity of Suzhou Wanqing Pharmaceutical Co., Ltd. with RMB100 million Use of Guangzhou Logistics Center, which was invested RMB140 million, and became the first third-party pharmaceutical logistics company in Southern China

	Completion of acquisition of equity of Sinopharm Group Nanning Co., Ltd.
2010	Awarded as "Top 100 Chinese Pharmaceutical Industry" Acquisition of 52.61% equity of Sinopharm Group Shenzhen Chinese Medicine Co., Ltd., which became a wholly-owned subsidiary of the company
2012	"Accord" was recognized as a famous trademark in Guangdong Province Use of Sinopharm Group Guangxi Co., Ltd. Modern Medicine Logistics Center, the first modern pharmaceutical logistics center in Guangxi, which was invested RMB155 million Sinopharm Group Guangzhou Co., Ltd. won the "Internet Drug Trading Service Qualification Certificate", entered the field of pharmaceutical e-commerce Establishment of Sinopharm Group Shaoguan Co., Ltd., further improved the strategic layout of the distribution in the Northern Guangdong and strengthen the dominant position of the Guangdong-Guangxi distribution network
2013	Operation of Sinopharm Group Guangzhou Drugstore, the first professional prescription retail pharmacy in Guangdong of the company
2016	Approval of restructuring project by the CSRC unconditionally, and injection of Guoda Drugstore as a whole
2017	Establishment of the sales center of Sinopharm Group Guangzhou Co., Ltd. to deepen the chain terminal network business in Southern China Operation of Sinopharm Group Guangzhou Medical Supply Chain Service Co., Ltd. to provide intensive integration services for medical inspection products for medical institutions Introduction of Walgreens Boots Alliance, overseas pharmaceutical retail giant in the world
2018	Establishment of Sinopharm Group Guoda Drugstore Co., Ltd. with Walgreens Boots Alliance

Source: Phillip Securities (HK) Research, Wind

Figure-5: Shareholding Structure of Company (as of 2018 Annual Report)



Source: Phillip Securities (HK) Research, company Report

Key Business Analysis

The company is a comprehensive pharmaceutical listed company under the China National Pharmaceutical Group and Sinopharm Group. After the reorganization, all of the businesses are related to pharmaceutical business, including pharmaceutical distribution and pharmaceutical retail. The business of the company is mainly divided into the following two sections:

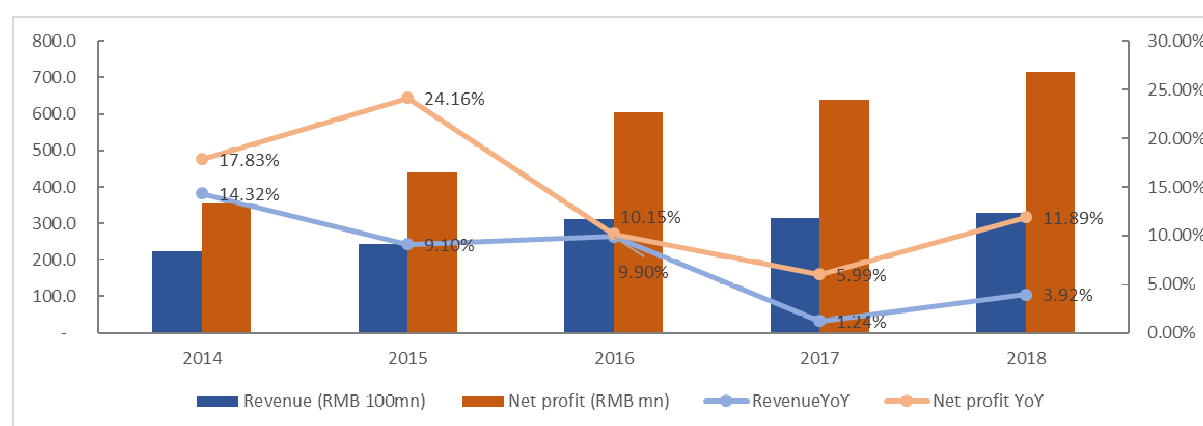
1. Pharmaceutical distribution business

The company's pharmaceutical distribution business is established in Guangdong and Guangxi, the company has completed the network construction of Guangdong and Guangxi in 2013, and the business has extended to the county-level regions; in 2014, the company has accelerated

the integration of three-tier companies and achieved an operation all over the network in 2015; moreover, the distribution network has further expanded in 2018 and main development direction is retail terminals, including: 982 secondary and tertiary medical institutions, 4,996 primary medical customers and 1,947 retail terminal customers (chain drugstores and single store). The company's pharmaceutical distribution business has achieved the first scale in Guangdong and Guangxi and the leading position in market segment of Guangdong and Guangxi, and has obtained the relatively leading position in vaccine, instrument, and e-commerce industries.

In 2018, the revenue of pharmaceutical distribution business was RMB32.757 billion, representing a YoY increase of 3.92%, the net profit was RMB716 million, a YoY increase of 11.89%. From 2014 to 2018, the distribution business maintained steady growth. The compound annual growth rate of revenue reached 10.1%, and the compound annual growth rate of net profit reached 19.26%.

Figure-6: Revenue and Net Profit of Distribution Business

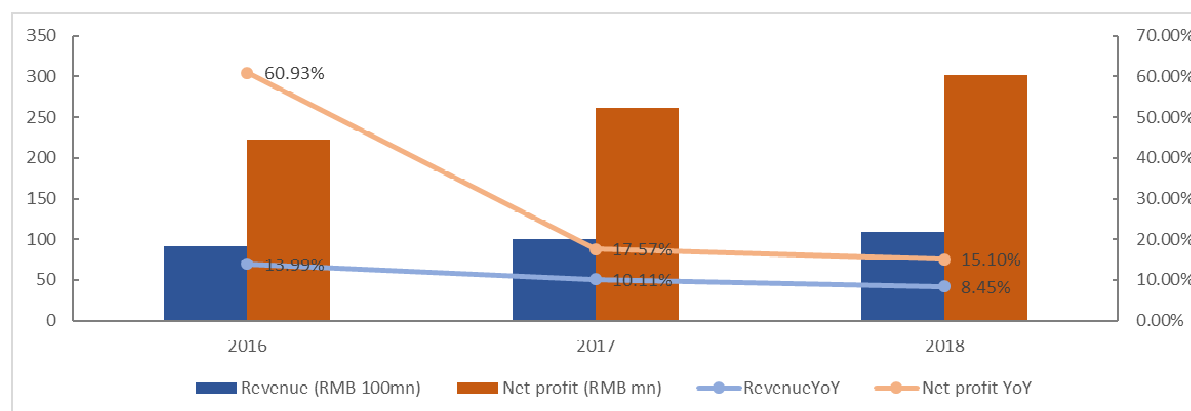


Source: Phillip Securities (HK) Research, Company Report

2. Pharmaceutical retail business

Guoda Drugstore, which was reorganized into the company in 2016, is a pharmaceutical retail enterprise that ranks the first in the sales volume throughout the country, and is one of the enterprises in China with national direct sales drug retail network. By the end of 2018, Guoda Drugstore has operated 4,275 stores, with a YoY increase of 441 stores compared with 2017. Among them, there are 361 hospital-side stores, increased 58 new ones; 1,213 national chronic disease stores, increased 302 new ones; 2,670 medical insurance stores of direct sales; covering 19 provinces, autonomous regions and municipalities, entering nearly 70 large and medium sized cities, which has formed a drugstore networks covering eastern and northern China, southern coastal cities, and gradually expanded into northeast, central plains and inland cities, the sales scale of which has exceeded 10 billion, ranking the first within industry.

In 2018, the revenue of Guoda Drugstore was RMB10.878 billion, a YoY increase of 8.45%, the net profit was RMB302 million, a YoY increase of 15.10%. From 2016, the compound annual growth rate of revenue of Guoda Drugstore was 9.28%, and the compound annual growth rate of net profit was 16.37%, which showed a steady growth of the retail business.

Figure-7: Revenue and Net Profit of Retail Business of Guoda Drugstore

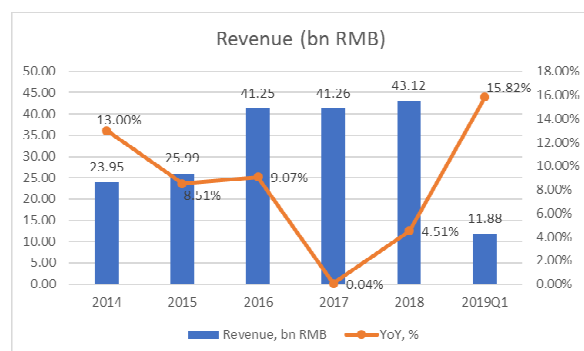
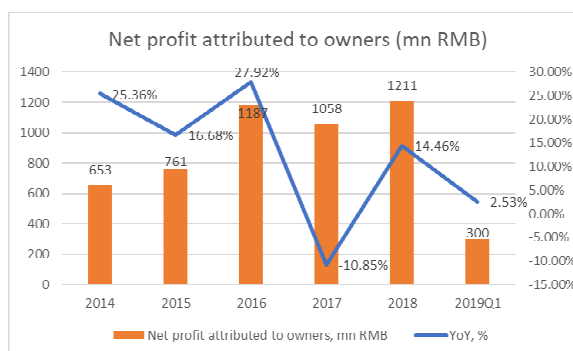
Source: Phillip Securities (HK) Research, Company Report

Investing Highlights

Leading enterprise in pharmaceutical industry, continue to promote the “wholesale and retail integration” strategy

The company is a comprehensive pharmaceutical listed company under the China National Pharmaceutical Group and Sinopharm Group, and it is the leading enterprise in pharmaceutical industry of the country. After the completion of major asset restructuring in 2016, the company actively promoted the “wholesale and retail integration” strategy, made full use of the commercial platform with mature distribution and the terminal advantageous network with wide retail sales to extend the commodity to the retail terminal through effective resource integration means and give play to the scale effect so as to achieve the synergistic interaction between distribution and retail, continue to further promote the distribution business in Guangdong and Guangxi, and expand the layout of retail pharmacies.

Despite the influence of factors such as “two-vote system”, GPO, price reduction and post-restructuring operation integration in the past two years, wholesale and retail synergy has achieved initial success, in 2018, the sales revenue of wholesale and retail synergy was RMB590 million, a YoY increase of 75%. At the same time, the company created the new model of distribution-Guoda wholesale and retail “member store”, and gave play to the advantages of commercial distribution center in variety, background connection, and delivery, combined with Guangdong Guoda retail network, developed member stores in Guangdong and Guangxi, and the members increased to 86 stores throughout the year. We believe that the continually promotion of wholesale and retail integration, integration of distribution and retail strategy varieties, category planning and resource sharing, will benefit to the company to build a more complete operating system, play the synergy effect of wholesale and retail, and enhance the comprehensive competitiveness of the company.

Figure-8: Turnover and Growth Rate**Figure-9: Net Profit Attributed to Owners**

Source: Phillip Securities (HK) Research, Company Report

Improve distribution network, transformation and innovation of distribution business

The company's distribution business is concentrated in the Guangdong and Guangxi provinces, with Sinopharm Group Guangzhou Co., Ltd. and Sinopharm Group Guangxi Co., Ltd. as the core companies, ranking the first in the Guangdong and Guangxi, comprehensively covering the Grade-III and Grade-II medical institutions and retail chain terminals in Guangdong and Guangxi, covering more than 4,000 medical institutions. In 2018, through investment in mergers and acquisitions and new establishments, Sinopharm Holding Guangxi Hezhou Co., Ltd., Sinopharm Holding Guangxi Qinzhou Co., Ltd., Sinopharm Holding Guangxi Hechi Co., Ltd., Sinopharm Holding Guorun Medical Supply Chain Service (Guangxi) Co., Ltd., and Sinopharm Holding Baiyi Pharmacy Guangxi Co., Ltd. have been established, which has further strengthened the layout of the distribution business of Guangdong and Guangxi.

Affected by the policies of the Guangdong medical reform system such as "two-vote system", GPO and second bargaining, the growth rate of the entire pharmaceutical industry slowed down and the company's distribution business was affected accordingly. However, with the changes in the market environment, the company has transformed and innovated in the distribution field, and actively expanded its business development areas, clearly focused on the development of four business directions including retail direct sales, equipment consumables, retail diagnosis and treatment, and primary care. The company has improved supply chain management efficiency and reduced operating costs to ensure that earnings are growing through informatization reform. In 2018, the retail direct sales increased by 34% YoY, equipment consumables increased by 29% YoY, retail diagnosis and treatment increased by 49% YoY, and primary care increased by 17% YoY. The company has promoted the implementation of 131 key cooperation projects of two vote system, the income of Guangdong's pure sales business increased by RMB958 million; accelerated the stationing of distribution and retail, there were 61 open drugstores throughout the year, including 23 drugstores newly opened in 2018 (12 cooperative drugstores in the hospitals, 6 drugstores near the hospitals, and 5 DTP pharmacies), the quality of the drugstores was gradually improved, and the sales revenue increased by 36% YoY. We expect that the company's distribution business will continue to grow steadily as the distribution business transforms and innovates.

Build a "new Guoda", continue to promote internationalization

As a large-scale pharmaceutical retail enterprise in China, Guoda Drugstore has 28 regional chain companies and established the logistics and distribution network including Shanghai National Logistics Center and 23 provincial and municipal

distribution centers. Guoda Drugstore ranked the first among the China pharmaceutical retailers for seven consecutive years since 2011. According to the “Statistical Analysis Report on the Operation of Drug Circulation Industry in 2017” by the Ministry of Commerce, the total sales of Guoda Drugstore in 2017 was RMB11.08 billion, a YoY increase of 7.48%, leading 21.49% to second-class Beijing Tongrentang (RMB9.12 billion). As of drug retail market of RMB400.3 billion in 2017, the market share of Guoda Drugstore was 2.8%, which was the same as in previous years.

Table-2: The Top 10 of Retail Pharmacies in 2017

Rank	Name	Sales (in ¥`00 mn)
1	國藥控股國大藥房有限公司 Guoda Drugstore	110.80
2	中國北京同仁堂（集團）有限責任公司 Beijing Tongrentang Group Co., Ltd.	91.20
3	雲南鴻翔一心堂藥業（集團）股份有限公司 Yunnan Hongxiang Yixintang Pharmaceutical Co., Ltd.	85.09
4	老百姓大藥房連鎖股份有限公司 Lbx Pharmacy Chain Joint Stock Company	83.33
5	大參林醫藥集團股份有限公司 DaShenLin Pharmaceutical Group Co., Ltd.	83.08
6	重慶桐君閣大藥房連鎖有限責任公司 Chongqing Tongjunge Pharmacy Franchises Co., Ltd.	72.50
7	益豐大藥房連鎖股份有限公司 Yifeng Pharmacy Chain Co., Ltd.	56.01
8	上海華氏大藥房有限公司 Shanghai Huashi Pharmacy Co., Ltd.	41.66
9	湖北同濟堂藥房有限公司 Ready Medicine Co., Ltd.	38.21
10	遼寧成大方圓醫藥連鎖有限公司 Liaoning Chengda Fangyuan Pharmacy Chains Co., Ltd.	36.26

Source: Phillip Securities (HK) Research, Company Report

Based on the retail business developed in nearly 70 cities in 19 provinces and autonomous regions, Guoda Drugstore expanded their retail scale advantage with the “self-opening + M&A” model; meanwhile, it completed the investment in newly establishing Fujian Guoda Medicine Co., Ltd., Shanghai Guoda Ruijing Pharmacy Co., Ltd., Sinopharm Holding Guoda Drugstore Zhengzhou Chain Co., Ltd. and Inner Mongolia Guoda Drugstore Pharmaceutical Co., Ltd., and the acquisition of 100% equity of Shanxi Zhongao Pharmaceutical Co., Ltd., the acquisition of relevant retail business and assets of Inner Mongolia Tongren Pharmacy Chain Co., Ltd., and the acquisition of 100% equity of Shanxi Yixintang Pharmacy Co., Ltd. At the end of 2018, the total number of Guoda Drugstore reached 4,275 stores, a net increase of 441 stores, including 3,202 direct stores, with sales revenue of RMB10.02 billion, up 9.87% YoY; 1,073 franchise stores, distribution revenue of RMB1.183 billion, an increase of 6.25% YoY.

Figure-10: Composition of Guoda Drugstore

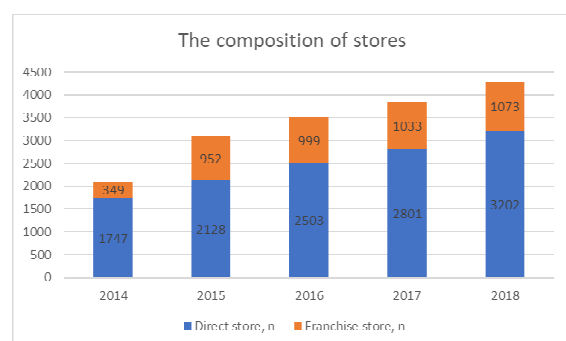
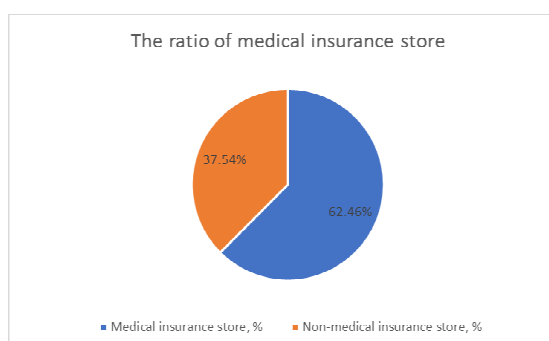


Figure-11: Ratio of Medical Insurance Direct Store



Source: Phillip Securities (HK) Research, Company Report

In July 2018, Guoda Drugstore completed the introduction of Walgreens Boots Alliance (WBA), and became a Sino-foreign joint venture after the equity transfer. WBA is the world's largest drugstore retailer that provides health care services through the operation of pharmaceutical wholesale and community pharmacies. At the

same time, it also has advanced chain pharmacy management experience and DTP pharmacy operation experience. In 2018, the revenue of WBA was US131.5 billion and net profit attributed to owners was US5.024 billion. We believe that through the cooperation with WBA with introducing internationally advanced management concepts, information technology and product supply chain management, the company could improve the operational efficiency, pharmaceutical service capabilities, etc. of Guoda Drugstore, and enhance the gross profit rate, thereby strengthening the company's profitability, and accelerating the internationalization process to lead the development of China's pharmaceutical retail industry.

Financial Forecast and Valuation

Financial Performance

The company's gross profit in 2018 was 5.098 billion RMB, representing an increase of 14.73% YoY; gross profit margin was 11.82%, increasing by 1.05%; net profit attributable to shareholders was 1.211 billion RMB, increasing by 14.46% YoY; net profit attributable to shareholders margin was 2.81%, increasing by 0.25%. It is expected that as Guoda Drugstore completes the introduction of WBA, the store expansion and operation efficiency will gradually improve, and more profits will be released in 2019.

Table-3: Financial Performance of Last Three Years

	Unit: RMB mn	Medicine wholesale		Medicine retail		Logistic & storage service		Lease and other		Medicine manufacturing		Total		
		Amount	YoY	Amount	YoY	Amount	YoY	Amount	YoY	Amount	YoY	Amount	YoY	
2018	Revenue	31,866.75	2.72%	10,873.16	9.91%	26.11	-11.70%	356.36	12.06%	0.00	0.00%	43,122.39	4.51%	
	Cost	29,606.07	0.99%	8,368.91	12.23%	13.03	-17.71%	36.1	-0.73%	0.00	0.00%	38,024.11	3.27%	
	Gross profit	2,260.68	32.36%	2,504.26	2.81%	13.08	-29.28%	320.26	13.71%	0.00	0.00%	5,098.28	14.73%	
	Gross profit ratio	7.09%		23.03%		50.11%		89.87%			0.00%		11.82%	
	Net profit contributed to owners												1,210.74	14.46%
	Net profit ratio contributed to owners												2.81%	
2017	Revenue	31,022.97	0.13%	9,892.84	12.92%	29.57	43.88%	318.02	2.57%	0.00	-100.00%	41,263.39	0.04%	
	Cost	29,315.03	-0.02%	7,457.09	12.90%	11.07	-16.62%	36.37	12.37%	0.00	-100.00%	36,819.55	0.47%	
	Gross profit	1,707.94	2.73%	2,435.74	12.97%	18.5	154.18%	281.65	1.43%	0.00	-100.00%	4,443.84	-3.40%	
	Gross profit ratio	5.51%		24.62%		62.58%		88.56%			0.00%		10.77%	
	Net profit contributed to owners												1,057.79	-10.85%
	Net profit ratio contributed to owners												2.56%	
2016	Revenue	30,982.39	8.89%	8,761.10	18.68%	20.55	16.25%	310.05	-8.48%	1,174.24	-27.89%	41,248.34	9.07%	
	Cost	29,319.92	8.99%	6,605.05	19.89%	13.27	2.21%	32.36	-44.01%	677.55	-28.77%	36,648.16	9.62%	
	Gross profit	1,662.47	7.23%	2,156.05	15.10%	7.28	55.05%	277.69	-1.17%	496.69	-26.66%	4,600.18	4.87%	
	Gross profit ratio	5.37%		24.61%		35.42%		89.56%		42.30%			11.15%	
	Net profit contributed to owners												1,186.54	27.91%
	Net profit ratio contributed to owners												2.88%	

Source: Phillip Securities (HK) Research, Company Report

Financial Forecast

It is estimated that the company's revenue in FY19/FY20/FY21 will be RMB 45.99/49.72/53.37 billion, representing increases of 6.65%/8.11%/7.34% YoY; net profit attributable to shareholders will be RMB 1.34/1.53/1.72 billion, representing increases of 10.24%/14.32%/12.83% YoY; corresponding EPSs are RMB 3.12/3.56/4.02. The company continues to promote the integration of wholesale and retail, exerts the synergy effect. At the same time, it further enhances the transformation and innovation of the circulation business and builds up a new Guoda Drugstore. We are optimistic about the future development of the company.

Table-4: Financial Forecast

RMB in million	2016A	2017A	2018A	2019E	2020E	2021E
Revenue	41,248.34	41,263.39	43,122.39	45,989.45	49,718.17	53,366.27
YoY%	9.07%	0.04%	4.51%	6.65%	8.11%	7.34%
GP	4,600.18	4,443.84	5,098.28	5,894.83	6,739.18	7,603.86
YoY%	4.87%	-3.40%	14.73%	15.62%	14.32%	12.83%
GPM	11.15%	10.77%	11.82%	12.82%	13.55%	14.25%
PBT	1,600.15	1,466.03	1,678.93	1,922.43	2,197.79	2,479.78
NP	1,281.78	1,156.74	1,348.43	1,532.47	1,751.98	1,976.77
YoY%	24.45%	-9.75%	16.57%	13.65%	14.32%	12.83%
NPM	3.11%	2.80%	3.13%	3.33%	3.52%	3.70%
NP attributable to shareholders	1,186.54	1,057.79	1,210.74	1,334.72	1,525.90	1,721.68
EPS (Basic, RMB)	2.80	2.47	2.83	3.12	3.56	4.02

Source: Phillip Securities (HK) Research, Company Report

Valuation

Based on our SOTP valuation model, we initiate coverage on Sinopharm Accord with 16.13x/14.11x/12.50x FY19/FY20/FY21 PER, corresponding to TP RMB 50.29 with a 21.0% potential upside compared with current price RMB 41.56 as of June 24, 2019, and recommend “BUY” investment rating.

Table-5: Peers Comparison

Ticker	Name	Closing Price RMB	Market Cap RMB bn	PE (TTM)	PE (2019E)	PE (2020E)
000028.SZ	國藥一致	41.47	17.75	14.57	13.05	11.49
Retail Peers						
603939.SH	益豐藥房	63.40	23.89	51.64	42.10	31.73
603233.SH	大參林	41.98	21.83	38.39	33.80	27.84
603883.SH	老百姓	56.20	16.10	34.71	30.07	24.62
002727.SZ	一心堂	27.39	15.55	27.52	23.61	19.14
600085.SH	同仁堂	28.67	39.32	33.71	32.49	29.59
Average				37.19	32.41	26.58
Distribution Peers						
600511.SH	國藥股份	22.61	17.28	12.04	11.60	10.26
603368.SH	柳藥股份	33.43	8.66	15.05	12.78	10.29
600713.SH	南京醫藥	4.57	4.76	17.51	15.06	12.96
002462.SZ	嘉事堂	15.27	3.83	11.30	9.43	7.74
Average				13.98	12.22	10.31

Source: Phillip Securities (HK) Research, Wind, Prices are as of June 21, 2019.

Risk

1. Industry policy risk
2. Guoda Drugstore`s business fails expectations
3. Distribution business transformation fails expectations

Financials

FYE	FY17	FY18	FY19E	FY20E	FY21E
Valuation Ratios					
P/E	16.82	14.70	13.33	11.66	10.33
P/B	1.89	1.53	1.39	1.26	1.14
Dividend Yield (%)	0.72%	0.96%	1.01%	1.15%	1.30%
Per share data (RMB)					
EPS	2.47	2.83	3.12	3.56	4.02
DPS	0.30	0.40	0.42	0.48	0.54
BVPS	21.95	27.14	29.84	32.92	36.41
Growth & Margins (%)					
Growth					
Revenue	0.04%	4.51%	6.65%	8.11%	7.34%
Operating profit	-5.99%	14.15%	13.77%	14.32%	12.83%
Net Profit	-9.75%	16.57%	13.65%	14.32%	12.83%
Margins					
Gross margin	10.77%	11.82%	12.82%	13.55%	14.25%
Operating profit margin	3.55%	3.87%	4.13%	4.37%	4.59%
Net Profit Margin	2.80%	3.13%	3.33%	3.52%	3.70%
Key Ratios					
ROA	5.18%	4.66%	5.09%	5.58%	6.01%
ROE	11.26%	10.42%	10.45%	10.83%	11.05%
Income statement (RMB mn)					
Revenue	41,263.39	43,122.39	45,989.45	49,718.17	53,366.27
Gross Profit	4,443.84	5,098.28	5,894.83	6,739.18	7,603.86
EBT	1,466.03	1,678.93	1,922.43	2,197.79	2,479.78
Net profit	1,156.74	1,348.43	1,532.47	1,751.98	1,976.77
Minority Interest	98.95	137.69	197.76	226.08	255.09
Net profit for owners	1,057.79	1,210.74	1,334.72	1,525.90	1,721.68

Source: Company, Phillip Securities (HK) Research Estimates
Financials as of 24 June, 2019.

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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