

SINOPHARM ACCORD (000028.SZ)

Distribution Business Exceeds Expectations, Retail Stores Continue Expanding

China | Pharmaceuticals | Company Update

September 3, 2019

Company Update

As of 30 June 2019, the company's revenue was RMB 25.228 billion, representing an increase of 21.42% YoY; net profit attributable to shareholders was RMB 651 million, with a YoY increase of 1.42%. Revenue from pharmaceutical distribution business was RMB 19.477 billion, representing an increase of 22.66% YoY; segment net profit attributable to shareholders was RMB 382 million, representing an increase of 15.41% YoY. Revenue from Guoda Drugstore was RMB 6.108 billion, representing an increase of 18.75% YoY; segment net profit attributable to shareholders was RMB 150 million, representing an increase of 7.81% YoY. Basic earnings per share was RMB 1.52 (corresponding period in 2018: RMB 1.50). The company's performance of core business is basically consistent with our forecast, in the first half of 2019, the company expanded the scale, and growth rate was better than the overall level of the industry, and achieved steady and rapid growth in performance; related performance increase in total revenue was mainly contributed by the acceleration of the company resource integration and expansion of store network layout. As of the first half of 2019, the company had a total of 107 subsidiaries, and the number of retail outlets of Guoda Drugstore was 4,593, with a net increase of 318 stores, 228 of which was direct-sales shops. During the reporting period, the company invested in the establishment of the Sinopharm Guoda Drugstore Bayannao'er Co., Ltd., Inner Mongolia Guoda Pharmaceuticals Co., Ltd., and Sinopharm Guoda Drugstore Yongxingtang Chain (Chaoyang) Co., Ltd.

Investment Highlights

Distribution business continues to integrate and promote the synergy of wholesale and retail

In the pharmaceutical distribution field, the company continues to integrate the distribution and logistics business, deeply penetrates into the end markets, improves the multistep distribution network, creates intelligent supply chain, developed a clustered and large-scale industrial advantages, and commit to becoming a leading provider of medical health products and services in Southern China. In the first half of 2019, the distribution launched the logistics planning of wholesale and retail integration, and the sales of wholesale and retail synergies increased by 54% YoY, and the part outside of Guangdong and Guangxi provinces increased by 64% YoY. In the first half of 2019, the hospital direct selling market distributed in 30 cities at prefecture level and above in Guangdong and Guangxi ranked the top three; the distribution of customers was mainly including retail medical treatment, grass-root medical institutions, and small-scale social medical services: 1,804 medical institutions at the first level or above, 3,783 primary care customers (excluding 836 first-level hospitals), and 1,587 retail terminal customers (chain drugstores, single stores). The company has complete pharmaceutical distribution networks in Guangdong and Guangxi, achieve comprehensive coverage of the second and third-level medical institutions in Guangdong and Guangxi, scale and growth rate have achieved rapid growth. In the first half of 2019, traditional business grew by 22% YoY, retail direct sales increased by 30% YoY, equipment consumables increased by 52% YoY, retail medical treatment increased by 80% YoY, and primary care increased by 34% YoY.

Retail business's performance stably increased, store network gradually expanded

In the pharmaceutical retail field, Guoda Drugstore is a pharmaceutical retail enterprise that ranks the first in the sales volume throughout the country, and is one of the few enterprises in China with national direct sales drug retail network. As of the end of June 2019, Guoda Drugstore had established 28 regional chain enterprises, had 4,593 stores, covering 19 provinces, autonomous regions, and municipalities directly under the central government, which formed a network of pharmacies covering the urban agglomerations of East China, North China, and coastal region of South China, and gradually spread into the Northwest, Central Plains, and inland city clusters; 3,470 direct-operated stores, with sales revenue of RMB 5.381 billion, a YoY growth of 11.82%; 1,123 franchise stores with distribution revenue of RMB 622 million, an increase of 7.64% YoY. The "New Concept" pilot pharmacy jointly launched by Guoda Drugstore and

ACCUMULATE

CMP RMB 47.56

(Closing price at 30 August 2019)

TARGET RMB 54.12 (+13.79%)

COMPANY DATA

O/S SHARES (MN)	428.13
MARKET CAP (RMBMN)	20,362
52 - WK HI/LO (RMB):	37.79/52.75

SHARE HOLDING PATTERN

Sinopharm Group Co., Ltd	56.06%
HK Securities Clearing Company Ltd	4.33%

PRICE PERFORMANCE

	1M	3M	1Y
SINOPHARM ACCORD	14.87%	12.45%	3.19%
CSI300	-0.93%	4.68%	13.95%

RETURN & CSI300



Source: Phillip Securities (HK) Research

KEY FINANCIALS

mn RMB	FY17 A	FY18 A	FY19 E	FY20 E	FY21 E
Revenue	41,263	43,122	50,456	55,051	60,101
NP for Owners	1,058	1,211	1,266	1,483	1,730
EPS RMB	2.47	2.83	2.96	3.46	4.04
P/E	19.25	16.82	16.08	13.73	11.77
BVPS RMB	21.95	27.14	29.68	32.65	36.12
P/B	2.17	1.75	1.60	1.46	1.32
ROE	11.85%	11.52%	10.41%	11.12%	11.75%

Source: Company reports, Phillip Securities Est.

Research Analyst
Leon Duan (+852 2277 6515)
 leonduan@phillip.com.hk

Walgreens Boots Alliance opened on January 20th at Shangnan Road, Pudong New District of Shanghai. Up to now, sales have increased by 34.8% YoY, and the number of transactions has increased by 31.5% YoY. In addition, Guoda Drugstore built an Internet + medical e-commerce model, improved the value-added service system, optimized the self-operated OTO platforms such as WeChat Mall and APP, created a pharmacy + Internet O2O model, enhanced the front-end customer experience, and launched the e-commerce national customer service. In the first half of 2019, the number of effective members nationwide was 11.436 million, an increase of 8% YoY. In 2019, the company promoted brand upgrade, implemented the new brand strategy, successively completed the "Guoda" upgrades and "Guozhi" brand integration plan, and continue to promote brand upgrades in the second half of the year. The leading scale of Guoda Drugstore was one of the core competitiveness, and the scale advantage reduced the company's procurement cost and enhanced the company's bargaining ability.

Financial Forecast and Valuation

Financial Performance

In the first half of 2019, the company realized gross profit of RMB 2.81 billion, representing an increase of 21.41% YoY as compared to RMB 2.41 billion in 2018. The increase in gross profit was mainly attributable to the increase of distribution and retail businesses. Gross profit margin of the company decreased from 11.61% in 2018 to 11.15% in 2019. The decrease was mainly due to the larger proportion of distribution business.

Figure-1: Profitability level

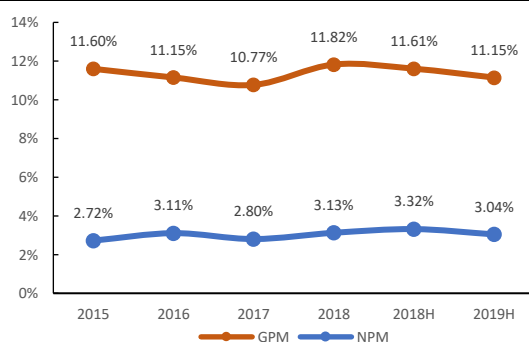
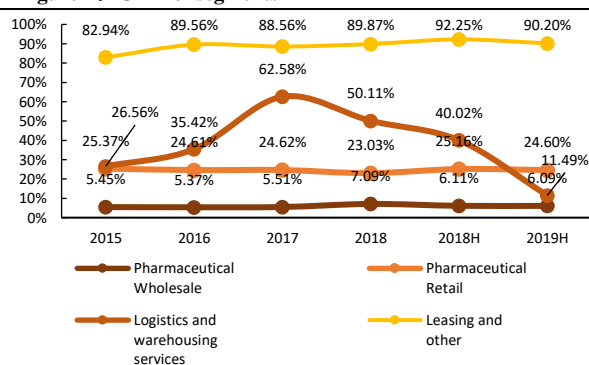


Figure-2: GPM of segments



Source: Phillip Securities (HK) Research, Company Report

Figure-3: Liability-to-asset ratio

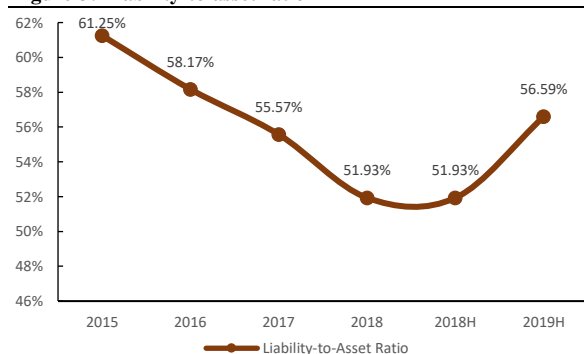
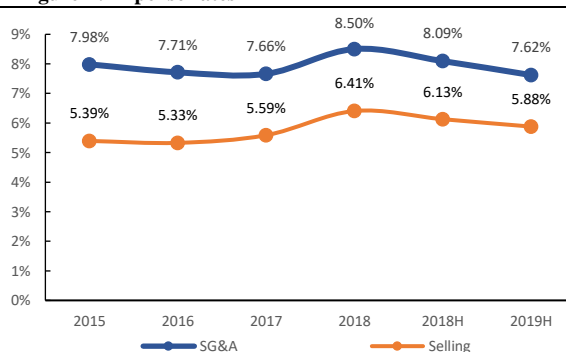


Figure-4: Expense rates



Source: Phillip Securities (HK) Research, Company Report

Table-1: Financial performance of last three years

RMB in million		FY2016	FY2017	FY2018	FY2018H	FY2019H
Pharmaceutical Wholesale	Revenue	30,982.39	31,022.97	31,866.75	15,430.41	18,998.36
	YoY	8.89%	0.13%	2.72%		23.12%
	GP	1,662.47	1,707.94	2,260.68	942.70	1,157.34
Pharmaceutical Retail	GPM	5.37%	5.51%	7.09%	6.11%	6.09%
	Revenue	8,761.10	9,892.84	10,873.16	5,153.49	5,986.43
	YoY	18.68%	12.92%	9.91%		16.16%
	GP	2,156.05	2,435.74	2,504.26	1,296.79	1,472.66
	GPM	24.61%	24.62%	23.03%	25.16%	24.60%

Logistics and warehousing services	Revenue	20.55	29.57	26.11	15.53	46.84
	YoY	16.25%	43.88%	-11.70%		201.66%
	GP	7.28	18.50	13.08	6.21	5.38
Leasing and other	GPM	35.42%	62.58%	50.11%	40.02%	11.49%
	Revenue	310.05	318.02	356.36	179.75	196.51
	YoY	-8.48%	2.57%	12.06%		9.33%
Total	GP	277.69	281.65	320.26	165.82	177.25
	GPM	89.56%	88.56%	89.87%	92.25%	90.20%
	Revenue	41,248.34	41,263.39	43,122.39	20,779.17	25,228.15
Total	YoY	9.07%	0.04%	4.51%		21.41%
	GP	4,600.18	4,443.84	5,098.28	2,411.52	2,812.63
	GPM	11.15%	10.77%	11.82%	11.61%	11.15%

Source: Phillip Securities (HK) Research, Company Report

Financial Forecast and Valuation

We adjust the company's revenue in FY19/FY20/FY21 to be RMB 50.5/55.1/60.1 billion, representing increases of 17.01%/9.11%/9.17% YoY; gross profit will be RMB 5.7/6.3/7.0 billion, representing increases of 11.89%/10.44%/10.57% YoY; net profit attributable to shareholders will be RMB 1.3/1.5/1.7 billion, representing increases of 4.59%/17.12%/16.62% YoY; corresponding EPSs are RMB2.958/3.646/4.040. Based on our residual income valuation model, we adjust a TP of RMB 54.12, corresponding to FY19/FY20/FY21 18.30x/15.62x/13.40x PE with a +13.79% potential upside compared with CP of RMB 47.56 as of August 30, 2019, we give "ACCUMULATE" investment rating.

Table-2: Key Actual Figures and Forecast

mn RMB	2019H	Previous 2019 Forecast	% of Completion
Revenue	25,228.15	45,989.45	54.9%
GP	2,812.63	5,894.83	47.7%
Operating Profit	889.94	1,901.02	46.8%
EBT	960.34	1,922.43	50.0%
NP attributable to shareholders	650.83	1,334.72	48.8%

Source: Phillip Securities (HK) Research, Company Report

Table-3: Key Forecast and Target Price Revision

mn RMB		Old	New	% Change
Revenue	FY2019E	45,989.45	50,456.29	9.7%
	FY2020E	49,718.17	55,051.50	10.7%
	FY2021E	53,366.27	60,101.20	12.6%
GP	FY2019E	5,894.83	5,704.65	-3.2%
	FY2020E	6,739.18	6,300.47	-6.5%
	FY2021E	7,603.86	6,966.23	-8.4%
Operating Profit	FY2019E	1,901.02	1,703.32	-10.4%
	FY2020E	2,173.32	1,934.72	-11.0%
	FY2021E	2,452.17	2,200.03	-10.3%
NP attributable to shareholders	FY2019E	1,334.72	1,266.31	-5.1%
	FY2020E	1,525.90	1,483.08	-2.8%
	FY2021E	1,721.68	1,729.61	0.5%
RI TP		50.29	54.12	7.6%

Source: Phillip Securities (HK) Research, Company Report

Risk

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

Financials

Table-4: Financial data

FYE DEC	FY17A	FY18A	FY19E	FY20E	FY21E
Valuation Ratios					
P/E	19.25	16.82	16.08	13.73	11.77
P/B	2.17	1.75	1.60	1.46	1.32
Dividend Yield	0.63%	0.84%	0.88%	1.03%	1.20%
Per Share Data in RMB					
EPS	2.47	2.83	2.96	3.46	4.04
DPS	0.30	0.40	0.42	0.49	0.57
BVPS	21.95	27.14	29.68	32.65	36.12
Growth & Margins (%)					
Growth					
Revenue	0.04%	4.51%	17.01%	9.11%	9.17%
Operating Profit	-9.58%	11.63%	19.02%	13.59%	13.71%
Net Profit	-9.75%	16.57%	10.83%	17.12%	16.62%
Margins					
Gross Margin	10.77%	11.82%	11.31%	11.44%	11.59%
Operating Profit Margin	3.11%	3.32%	3.38%	3.51%	3.66%
Net Profit Margin	2.80%	3.13%	2.96%	3.18%	3.40%
Key Ratios					
ROA	4.85%	4.72%	4.03%	4.29%	4.81%
ROE	11.85%	11.52%	10.41%	11.12%	11.75%
Income Statement in mn RMB					
Revenue	41,263.39	43,122.39	50,456.29	55,051.50	60,101.20
Gross Profit	4,443.84	5,098.28	5,704.65	6,300.47	6,966.23
EBIT	1,576.39	1,791.79	2,063.89	2,369.51	2,717.63
EBT	1,466.03	1,678.93	1,870.34	2,190.52	2,554.65
Net Profit	1,156.74	1,348.43	1,494.45	1,750.28	2,041.23
Net Profit for Owners	1,057.79	1,210.74	1,266.31	1,483.08	1,729.61

Source: Company, Phillip Securities (HK) Research
(Financial data as of August 30)

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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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