

# SH Pharma (2607.HK)

Rapid growth in core segments, promising in innovation transformations

Hong Kong | Pharmaceuticals | Company Update

January 3, 2020

## Result Update

For the nine months ended September 30, 2019, the company recorded operating income of RMB 146.617 billion, an increase of 19.57% YoY, and its main business continued to grow rapidly. Of which, the pharmaceutical manufacturing sector realized revenue of RMB 17.682 billion, a YoY increase of 24.05%. The pharmaceutical business realized revenue of RMB 129.235 billion, an increase of 18.95% YoY (among which, the pharmaceutical distribution business achieved sales revenue of RMB 121.218 billion, an increase of 18.56% YoY; the pharmaceutical retail business achieved sales revenue of RMB 5.908 billion, an increase of 15.94% YoY). The company realized a net profit attributable to shareholders of listed companies of RMB 3.399 billion, a YoY increase of 0.80%; the main business of the pharmaceutical manufacturing sector contributed a profit of RMB 1.540 billion, a YoY increase of 20.56%; the main business of the pharmaceutical business contributed a profit of RMB 1.526 billion, a YoY increase increased by 15.73%; the participating companies contributed profits of RMB 804 million, an increase of 48.13% YoY. The company's comprehensive gross profit margin was 13.70%, a decrease of 0.11 percentage point compared with the same period last year; the gross profit margin of the pharmaceutical manufacturing sector was 57.54%, a decrease of 0.10 percentage point compared with the same period last year, and the average gross profit margin of 60 key varieties was 71.71%; the gross profit margin of pharmaceutical distribution was 6.40%, a YoY decrease of 0.27 percentage points; the gross profit margin of pharmaceutical retail was 14.10%, a YoY decrease of 1.02 percentage points.

## Continue to deepen one product one policy, accelerate innovation transformations

In the pharmaceutical manufacturing sector, the company focuses on key products and continuously increases its market share, such as tanshinone IIA sodium sulfonate injection. From January to September 2019, it realized sales revenue of RMB 1.14 billion, a YoY increase of 76.39%. According to the life cycle of different products, the company has formulated a differentiated terminal strategy, and the promotion effect is significant. In January-September 2019, Ulinastatin for injection achieved sales income of RMB 673 million, a YoY increase of 32.91%; hydroxychloroquine sulfate tablets achieved sales income of RMB 587 million, a YoY increase of 20.56%; Hongyuanda achieved sales income was 366 million yuan, a YoY increase of 31.75%. Eureka for injection achieved sales of 275 million yuan, a YoY increase of 20.85%.

In addition, the company continued to accelerate innovation transformation. From January to September 2019, R & D expenditure was RMB 860 million, an increase of 13.74% YoY; 73 invention patent applications were completed, 24 invention patent authorizations, and 20 utility model authorizations, totaling 117 patents. On September 17, the company signed a joint venture agreement with BIOCAD, the largest biopharmaceutical company in Russia, to introduce adalimumab biosimilars, trastuzumab biosimilars, bevacizumab biosimilars, and PD-1 products. Permanent and exclusive R & D, production, sales and other commercialization rights of the six blockbuster biopharmaceuticals in Greater China, including the joint venture company, will be the sole platform for BIOCAD in Greater China.

## Accumulate

CMP HKD 15.16

(Closing price at 31 December 2019)

TARGET HKD 18.06 (+19.14%)

### COMPANY DATA

|                      |            |
|----------------------|------------|
| O/S SHARES (MN)      | 919        |
| MARKET CAP (HKDMN)   | 53,310     |
| 52 - WK HI/LO (HKD): | 18.5/13.04 |

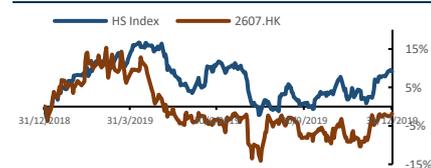
### SHARE HOLDING PATTERN

|   |        |
|---|--------|
| Shanghai Pharmaceutical (Group) Co., Ltd. | 25.21% |
| Shanghai Shangshi (Group) Co., Ltd.       | 8.39%  |

### PRICE PERFORMANCE

|     | 1M    | 3M    | 1Y     |
|-----|-------|-------|--------|
| SHP | 7.98% | 5.72% | -1.81% |
| HSI | 7.00% | 8.25% | 9.07%  |

### RETURN & HSI



Source: Phillip Securities (HK) Research

### KEY FINANCIALS

| mn RMB                          | FY17A  | FY18A  | FY19E  | FY20E  | FY21E  |
|---------------------------------|--------|--------|--------|--------|--------|
| Revenue                         | 130.8  | 159.0  | 187.5  | 205.5  | 225.4  |
| NP attributable to shareholders | 47     | 84     | 76     | 97     | 45     |
| EPS RMB                         | 1.31   | 1.37   | 1.54   | 1.74   | 1.98   |
| P/E                             | 11.58  | 11.05  | 9.86   | 8.70   | 7.67   |
| BVPS RMB                        | 12.66  | 13.79  | 14.86  | 16.07  | 17.45  |
| P/B                             | 1.20   | 1.10   | 1.02   | 0.94   | 0.87   |
| ROE                             | 10.72% | 10.63% | 10.74% | 11.26% | 11.80% |

Source: Company, Phillip Securities (HK) Research

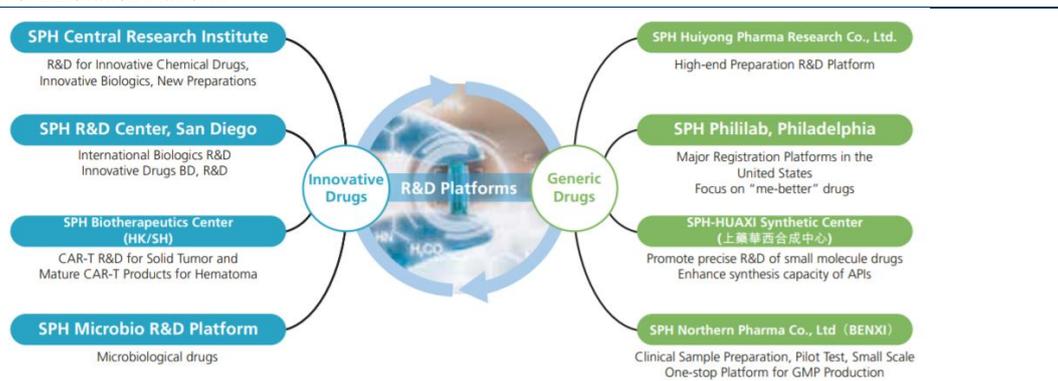
Research Analyst  
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The company continued to advance the consistency evaluation of the quality and efficacy of generic drugs, further improved the production process and the quality of medicines. As of the end of September, the company has completed more than 40 product specifications for BE testing and application, of which 6 varieties have passed the consistency evaluation. Two varieties of ceftriaxone sodium for injection and lansoprazole for injection have completed a BE test and declared to CDE. Beclometasone propionate inhalation aerosol has been approved for supplementary application, 3 specifications of rosuvastatin calcium tablets have been declared for production, and lenalidomide capsules and rivaroxaban tablets have been completed for BE filing. Capsaicin, a commonly used drug for clinical chemotherapy, has been completed. Tabin has also officially started the BE trial.

**Pharmaceuticals services continue promoting, expand the terminal market**

In November 2019, the company continued to promote the implementation of new distribution and new retail development strategies, promote the rapid development of advantageous and innovative services, clarify the regional development strategies of key provinces, and continue to promote key provinces such as Guangdong, Shandong, Heilongjiang, Jilin, and Liaoning. The platform construction utilizes the policy opportunities brought by the two-vote system and volume purchase, integrates market resources, and strictly controls the accounts receivable, while quickly seizing the pure-sale terminal market. Among the large varieties, Pfizer's Peer vaccine market has been rapidly expanding, which has led to rapid increase in distribution revenue. During the reporting period, the company achieved 2.122 billion in distribution revenue from vaccine business, a YoY increase of 92.33%. The company has launched a new business, providing efficient and compliant sales channels for imported drugs and new special drugs that are not covered by medical insurance, and after the corresponding products enter the medical insurance, the company's distribution network will be used to provide hospital services. The one-stop service chain of innovative pharmaceutical companies has joined forces to win the general distribution rights for new varieties of large pharmaceuticals.

**Figure-1: Layout of Innovation Platform**



Source: Phillip Securities (HK) Research, Company Report

**Table-1: Development Pipeline for Innovative Drugs**

| Therapeutic Area | Item                    | Registration Class                         | R&D Stage        | Project Description  |
|------------------|-------------------------|--|------------------|--|
| Anti-tumor       | SPH1188-11              | Innovative drug under type 1 chemical drug | Clinical phase I | New generation of target-oriented lung cancer drug. Effective for EGFR sensitive mutations, drug resistance mutations, some rare mutations and wild type, with the high concentration in lung tissues and brain tissues. |
|                  | Humanized CD20 antibody | Class 2 of biological drugs for treatment  |                  | Humanized antibody drugs with independent rights. More effective and safer than foreign drugs with the same target.  |

|   |  |  |                     |  |
|---|--|--|---------------------|--|
|   |  |  |                     | Used to treat hematological tumors and certain rare autoimmune diseases. Expected to remedy the current situation in China where this rare disease has no treatment, and become the first-tier standard therapeutic drug for the disease.  |
|   | Her2 compound antibody drugs for treatment | Class 1 of biological drugs for treatment  |                     | China's first compound antibody drug. Superior to foreign antibody drugs with the same target in terms of single drug efficacy. Has an unparalleled practical advantage compared with combined pharmacotherapy. After going to the market, it has an edge in market competition with antibody drugs with the same target whether in monotherapy or in combined pharmacotherapy |
|   | T-DM1                                      | Class 2 of biological drugs for treatment  |                     | An antibody coupling drugs used in the anti-tumor field, targeting patients with refractory/recurrent tumors which develop antibody resistance during treatment. Its action mechanism determines that it will not cause secondary drug resistance. Expected to become a second-tier standard therapeutic drug.   |
|   | SPH3348                                    | Innovative drug under type 1 chemical drug |                     | New target-oriented lung cancer and gastric cancer drug. With best activity among the same kind, wide treatment window, and low toxicity.  |
|   | CD30-DM1                                   | Class 1 of biological drugs for treatment  |                     | Antibody coupling drugs with independent intellectual property rights. Used in the field of hematology. With significant effect on rare diseases in the field. No similar product marketed in China.   |
| <b>Digestive metabolism</b>               | SPH4480                                    | Innovative drug under type 1 chemical drug | Clinical acceptance | A new diabetes drug. Can reduce weight, lower blood sugar, increase sensitivity to insulin, and improve diabetes triad. No drugs for this target marketed in the world.  |
| <b>Immunosuppressant</b>                  | Lei Teng Shu                               | Innovative drug under type 1 chemical drug | Clinical phase II   | In respect of immune indication of rheumatoid arthritis and AIDS patients, studies of the same kind, either domestic or overseas, all stay in the clinical trial stage   |
| <b>Cardiovascular and cerebrovascular</b> | Salvianolic acid A for injection           | Chinese medicine of class A new drug       | Clinical phase I    | A Chinese medicine of class A new drug. Preclinical pharmacology and toxicology studies show a broad and significant pharmacological effect. Notably superior to similar products in terms of safety range and the onset time.   |
|   | SPH3127                                    | Innovative drug under type 1 chemical drug | Clinical phase II   | A new antihypertensive drug. Significantly superior to others product with the same target in  |

terms of efficacy, bioavailability and safety window. Shows good tolerance in phase I clinical trial. With potential to be best in class.

Source: Phillip Securities (HK) Research, Company Report

### Financial Forecast and Valuation

We forecast that the company's FY19/FY20/FY21 income will be RMB 187.58/205.60/225.44 billion, representing an increase of 17.91%/9.61%/9.65% YoY; net profit attributable to shareholders will be RMB 4.35/4.93/5.60 billion, increasing 12.12%/13.24%/13.56% YoY; corresponding EPS will be RMB 1.54/1.74/1.98. We use DCF model and residual income model to value the company. Assuming equity cost is 10.49%, debt cost is 2.33%, and WACC is 7.19%. We get PT of HKD 18.06 and HKD 20.48 respectively. The lower valuation result corresponds to FY19/FY20/FY21 10.57x/9.33x/8.22x PE, which has an increase of +19.14% compared to the current price (HKD 15.16 as of December 31, 2019), giving an "Accumulate" rating.

Figure-2: Profit margin keep increasing

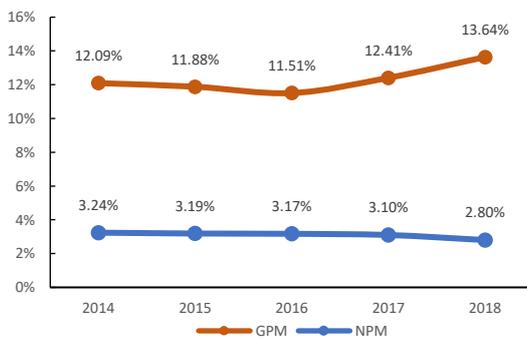
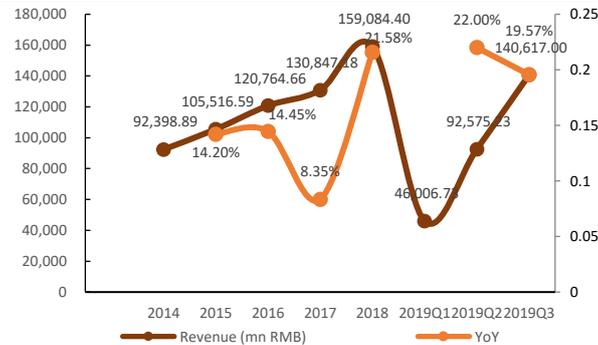


Figure-3: Growth rate of revenue



Source: Phillip Securities (HK) Research, Company Report

Figure-4: Gearing ratio

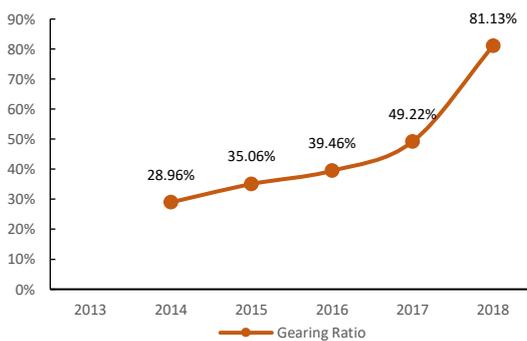
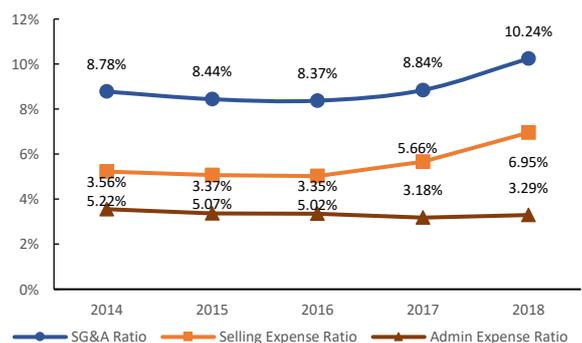


Figure-5: Expense rate



Source: Phillip Securities (HK) Research, Company Report

Table-2: Financial forecast

| RMB in million                  | FY2014A   | FY2015A    | FY2016A    | FY2017A    | FY2018A    | FY2019E    | FY2020E    | FY2021E    |
|---------------------------------|-----------|------------|------------|------------|------------|------------|------------|------------|
| Revenue                         | 92,398.89 | 105,516.59 | 120,764.66 | 130,847.18 | 159,084.40 | 187,576.04 | 205,596.74 | 225,445.32 |
| COS                             | 81,223.39 | 92,979.05  | 106,867.75 | 114,607.85 | 137,390.36 | 168,920.34 | 184,729.05 | 202,071.60 |
| GP                              | 11,175.50 | 12,537.54  | 13,896.91  | 16,239.33  | 21,694.04  | 25,450.33  | 28,600.04  | 32,163.76  |
| Operating Profit                | 3,063.30  | 3,631.16   | 3,784.56   | 4,665.95   | 5,401.60   | 6,128.39   | 7,141.17   | 8,162.61   |
| EBIT                            | 4,195.93  | 4,680.46   | 5,164.48   | 5,873.12   | 6,351.16   | 7,350.47   | 8,236.45   | 9,257.89   |
| EBT                             | 3,799.73  | 4,171.85   | 4,639.00   | 5,204.81   | 5,343.38   | 6,292.30   | 7,125.36   | 8,091.25   |
| NP                              | 2,992.02  | 3,364.37   | 3,829.71   | 4,057.78   | 4,456.26   | 5,084.81   | 5,758.01   | 6,538.55   |
| NP attributable to shareholders | 2,591.13  | 2,876.99   | 3,196.39   | 3,520.64   | 3,881.06   | 4,351.53   | 4,927.65   | 5,595.63   |
| EPS (Basic)                     | 0.96      | 1.07       | 1.19       | 1.31       | 1.37       | 1.54       | 1.74       | 1.98       |

Source: Phillip Securities (HK) Research, Company Report

**Table-3: DCF model**

| RMB in million       | FY2019            | FY2020   | FY2021   | FY2022   | FY2023    |
|----------------------|-------------------|----------|----------|----------|-----------|
| FCFF                 | 876.17            | 1,309.36 | 1,675.31 | 2,064.75 | 2,453.93  |
| Terminal Value       |                   |          |          |          | 78,073.50 |
| Discount factor      | 0.93              | 0.87     | 0.81     | 0.76     | 0.71      |
| PV                   | 817.40            | 1,139.60 | 1,360.31 | 1,564.07 | 56,908.85 |
| EV                   | 61,790.23         |          |          |          |           |
| Debt value           | 33,234.24         |          |          |          |           |
| Cash                 | 17,435.83         |          |          |          |           |
| Equity value         | 45,991.82         |          |          |          |           |
| Equity value in RMB  | 45,991,821,509.50 |          |          |          |           |
| Number of shares     | 2,829,324,000.00  |          |          |          |           |
| Value per share RMB  | 16.26             |          |          |          |           |
| Currency rate        | 0.90              |          |          |          |           |
| Value per share HKD  | 18.06             |          |          |          |           |
|                      | 2.33%             |          |          |          |           |
| Cost of debt         | 40.5%             |          |          |          |           |
| Debt weights         | 0.85              |          |          |          |           |
| Adjusted beta        | 3.15%             |          |          |          |           |
| Risk-free rate       | 11.79%            |          |          |          |           |
| Market return        | 10.49%            |          |          |          |           |
| Cost of equity       | 59.53%            |          |          |          |           |
| Equity weights       | 7.19%             |          |          |          |           |
| WACC                 | 3.50%             |          |          |          |           |
| Terminal growth rate | 17,435.83         |          |          |          |           |

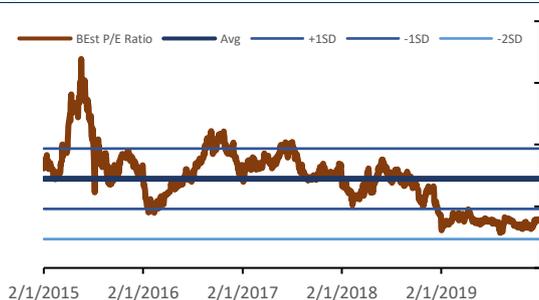
Source: Phillip Securities (HK) Research, Company Report

**Table-4: RI model**

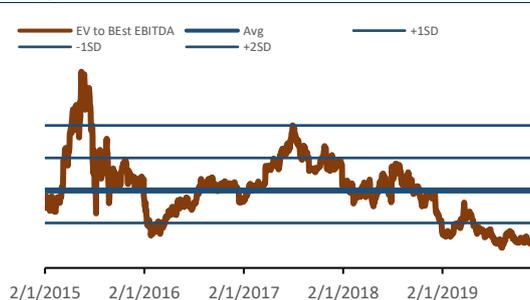
| RMB               | FY2019 | FY2020 | FY2021 | FY2022 | FY2023 | FY2024 | FY2025 | FY2026 | FY2027 | FY2028 |
|-------------------|--------|--------|--------|--------|--------|--------|--------|--------|--------|--------|
| EPS               | 1.54   | 1.74   | 1.98   | 2.04   | 2.21   | 2.39   | 2.84   | 3.40   | 4.11   | 5.01   |
| DPR               | 30.38% | 30.38% | 30.38% | 30.38% | 30.38% | 30.38% | 30.38% | 30.38% | 30.38% | 30.38% |
| DPS               | 0.47   | 0.53   | 0.60   | 0.62   | 0.67   | 0.72   | 0.86   | 1.03   | 1.25   | 1.52   |
| Add R/E PS        | 1.07   | 1.21   | 1.38   | 1.42   | 1.54   | 1.66   | 1.98   | 2.37   | 2.86   | 3.49   |
| BPSt              | 14.86  | 16.07  | 17.45  | 18.87  | 20.40  | 22.07  | 24.04  | 26.41  | 29.27  | 32.76  |
| BPS0              | 13.79  | 14.86  | 16.07  | 17.45  | 18.87  | 20.40  | 22.07  | 24.04  | 26.41  | 29.27  |
| ROEO              | 11.15% | 11.72% | 12.31% | 11.69% | 11.69% | 11.69% | 12.86% | 14.14% | 15.56% | 17.12% |
| Re                | 10.49% | 10.49% | 10.49% | 10.49% | 10.49% | 10.49% | 10.49% | 10.49% | 10.49% | 10.49% |
| RI                | 0.09   | 0.18   | 0.29   | 0.21   | 0.23   | 0.24   | 0.52   | 0.88   | 1.34   | 1.94   |
| Persistent factor | 0.80   |        |        |        |        |        |        |        |        |        |
| Terminal Vaue     | 5.08   |        |        |        |        |        |        |        |        |        |
| PV                | 0.08   | 0.15   | 0.22   | 0.14   | 0.14   | 0.13   | 0.26   | 0.40   | 0.54   | 2.59   |
| BPS0              | 13.79  |        |        |        |        |        |        |        |        |        |
| TP                | 18.44  |        |        |        |        |        |        |        |        |        |
| Currency rate     | 0.9    |        |        |        |        |        |        |        |        |        |
| TP in HKD         | 20.48  |        |        |        |        |        |        |        |        |        |

Source: Phillip Securities (HK) Research, Company Report

**Figure-6: Forward P/E Band**



**Figure-7: Forward P/B Band**



Source: Phillip Securities (HK) Research, Bloomberg

**Table-5: Comparable peers**

| Ticker   | Ticker | Mkt Cap      | EV           | EV/TTM EBITDA | EV/EBITDA FY1 | EV/EBITDA FY2 | P/E          | P/E FY1      | P/E FY2      | P/FCF        | Dividend    |
|--|--------|--------------|--------------|---------------|---------------|---------------|--------------|--------------|--------------|--------------|-------------|
| SHANGHAI PHARMACEUTICALS-H CNY (16 securities) | 2607   | 68.62        | 105.72       | N.A.          | 8.96          | 8.53          | 9.36         | 8.85         | 7.95         | 35.24        | 3.08        |
| <b>Median</b>                                  |        | <b>23.17</b> | <b>26.88</b> | <b>12.21</b>  | <b>14.20</b>  | <b>11.95</b>  | <b>16.13</b> | <b>18.34</b> | <b>15.44</b> | <b>21.45</b> | <b>1.26</b> |
| <b>Average</b>                                 |        | <b>31.81</b> | <b>37.72</b> | <b>16.51</b>  | <b>17.47</b>  | <b>14.10</b>  | <b>21.52</b> | <b>20.77</b> | <b>17.12</b> | <b>50.26</b> | <b>1.88</b> |
| CHONGQING ZHIFEI BIOLOGICA-A                   | 300122 | 113.91       | 115.87       | 34.32         | 25.91         | 18.25         | 37.32        | 32.02        | 22.93        | 106.02       | 1.01        |
| SHANGHAI FOSUN PHARMACEUTI-A                   | 600196 | 93.42        | 122.07       | 20.70         | 20.92         | 17.63         | 25.27        | 21.14        | 18.24        | N.A.         | 1.20        |

|                                |        |              |              |             |             |             |              |              |              |              |             |
|--------------------------------|--------|--------------|--------------|-------------|-------------|-------------|--------------|--------------|--------------|--------------|-------------|
| YIFENG PHARMACY CHAIN CO L-A   | 603939 | 39.79        | 41.16        | 42.78       | 31.87       | 24.77       | 52.17        | 48.80        | 37.27        | 124.06       | 0.41        |
| LIVZON PHARMACEUTICAL GROU-A   | 000513 | 39.47        | 31.83        | 10.76       | 12.86       | 11.15       | 26.43        | 24.61        | 21.12        | 10.92        | 2.76        |
| JOINTOWN PHARMACEUTICAL-A      | 600998 | 37.57        | 68.94        | 15.90       | 14.20       | 11.95       | 16.50        | 15.53        | 12.64        | 49.61        | 0.72        |
| CHINA NATIONAL MEDICINES-A     | 600511 | 29.45        | 27.39        | 9.00        | 8.18        | 7.42        | 13.59        | 2.00         | 1.78         | 21.45        | 1.47        |
| HUBEI JUMPCAN PHARMACEUT-A     | 600566 | 28.23        | 26.38        | 9.98        | N.A.        | N.A.        | 11.67        | 9.58         | 7.89         | 8.60         | 5.09        |
| LAOBAIXING PHARMACY CHAIN-A    | 603883 | 26.38        | 29.70        | 28.78       | 23.11       | 19.09       | 36.23        | 34.43        | 27.94        | 152.41       | 0.78        |
| CHINA MEHECO CO LTD -A         | 600056 | 19.96        | 24.06        | 7.81        | N.A.        | N.A.        | 10.93        | 9.90         | 9.57         | 34.09        | 3.33        |
| GUIZHOU BAILING GROUP PHAR-A   | 002424 | 17.63        | 20.33        | 21.08       | N.A.        | N.A.        | 25.77        | 27.22        | 26.39        | N.A.         | 0.92        |
| REALCAN PHARMACEUTICAL GRO-A   | 002589 | 16.56        | 31.04        | 7.17        | 8.82        | 7.50        | 22.96        | 11.66        | 9.76         | 7.43         | 0.68        |
| CQ PHARMACEUTICAL HOLDING-A    | 000950 | 14.25        | 24.51        | 15.22       | N.A.        | N.A.        | 11.22        | N.A.         | N.A.         | N.A.         | N.A.        |
| GUANGXI LIUZHOU PHARMACEUT-A   | 603368 | 12.49        | 16.77        | 12.55       | 11.36       | 9.18        | 12.61        | 12.33        | 9.87         | N.A.         | 1.84        |
| XIN JIANG READY HEALTH IND-A   | 600090 | 8.63         | 8.96         | 6.64        | N.A.        | N.A.        | 11.02        | N.A.         | N.A.         | 16.85        | 4.78        |
| HPGC RENMINTONGTAI PHARMAC-A   | 600829 | 5.68         | 7.15         | 11.87       | N.A.        | N.A.        | 14.93        | N.A.         | N.A.         | 21.39        | N.A.        |
| SHANDONG XINHUA PHARM CO-A     | 000756 | 5.57         | 7.31         | --          | N.A.        | N.A.        | 15.76        | N.A.         | N.A.         | N.A.         | 1.33        |
| <b>HKD (18 securities)</b>     |        |              |              |             |             |             |              |              |              |              |             |
| <b>Median</b>                  |        | <b>24.57</b> | <b>26.05</b> | <b>7.81</b> | <b>8.86</b> | <b>7.48</b> | <b>12.14</b> | <b>11.65</b> | <b>10.05</b> | <b>14.29</b> | <b>2.33</b> |
| <b>Average</b>                 |        | <b>45.05</b> | <b>54.72</b> | <b>9.40</b> | <b>9.54</b> | <b>8.11</b> | <b>13.44</b> | <b>13.95</b> | <b>11.40</b> | <b>22.13</b> | <b>2.80</b> |
| SINO BIOPHARMACEUTICAL CSPC    | 1177   | 176.22       | 179.67       | 19.26       | 18.76       | 16.47       | 3.22         | 37.53        | 32.21        | N.A.         | 0.73        |
| PHARMACEUTICAL GROUP LT        | 1093   | 148.81       | 142.86       | 20.33       | 17.12       | 14.12       | 30.02        | 26.03        | 21.16        | 66.00        | 0.97        |
| SINOPHARM GROUP CO-H           | 1099   | 108.58       | 207.33       | 7.49        | 7.62        | 6.75        | 12.77        | 11.76        | 10.37        | N.A.         | 2.35        |
| GUANGZHOU BAIYUNSHAN PHARM-H   | 874    | 79.40        | 74.34        | N.A.        | 12.30       | 9.46        | 12.20        | 12.20        | 10.24        | 47.15        | 1.81        |
| CHINA RESOURCES PHARMACEUTIC   | 3320   | 58.35        | 116.71       | 6.82        | 6.02        | 5.38        | 9.46         | 9.51         | 8.69         | 10.67        | 1.80        |
| CHINA MEDICAL SYSTEM HOLDING   | 867    | 35.74        | 35.52        | 10.68       | 9.73        | 8.84        | 12.09        | 11.31        | 10.28        | 11.98        | 3.33        |
| 3SBIO INC                      | 1530   | 32.95        | 35.76        | 18.31       | 13.03       | 10.30       | 21.03        | 17.94        | 13.30        | 20.41        | N.A.        |
| YICHANG HEC                    | 1558   | 25.51        | 25.75        | 10.35       | 8.76        | 7.60        | 13.99        | 11.54        | 9.93         | 29.19        | 4.04        |
| CHANGJIANG PHA-H SSY GROUP LTD | 2005   | 24.57        | 26.05        | 13.18       | 12.33       | 10.32       | 18.76        | 17.01        | 14.12        | N.A.         | 1.58        |
| LUYE PHARMA GROUP LTD          | 2186   | 24.52        | 25.95        | 8.15        | 7.88        | 7.37        | 11.12        | 10.74        | 9.45         | N.A.         | 2.21        |
| CHINA TRADITIONAL CHINESE ME   | 570    | 24.32        | 30.83        | 7.81        | 6.77        | 5.87        | 11.03        | 9.87         | 8.17         | N.A.         | 2.99        |
| TONG REN TANG TECHNOLOGIES-H   | 1666   | 12.60        | 11.74        | 6.54        | 6.53        | 6.24        | 13.95        | 12.82        | 12.18        | 10.08        | 2.66        |
| SIHUAN PHARMACEUTICAL HLDGS    | 460    | 11.31        | 4.66         | 1.51        | N.A.        | N.A.        | N.A.         | N.A.         | 4.27         | 4.37         | 2.06        |
| CHINA SHINWAY PHARMACEUTICA    | 2877   | 7.84         | 2.68         | 2.56        | 2.53        | 2.20        | 9.90         | 9.53         | 8.31         | 14.29        | 4.87        |
| SHANGHAI FUDAN-ZHANGJIANG-H    | 1349   | 5.29         | 4.80         | 15.03       | N.A.        | N.A.        | 19.58        | 19.01        | 15.97        | 17.27        | 1.83        |
| CONSUN PHARMACEUTICAL GROUP    | 1681   | 5.16         | 4.64         | 4.28        | 4.33        | 3.91        | 7.15         | 7.01         | 6.20         | 11.96        | 6.47        |
| LEE'S PHARMACEUTICAL HLDGS     | 950    | 3.34         | 2.78         | 4.03        | 9.91        | 6.34        | 7.91         | 13.68        | 10.05        | N.A.         | 2.31        |
| DAWNRAYS PHARMACEUTICAL HOLD   | 2348   | 2.86         | 1.90         | 3.51        | N.A.        | N.A.        | 8.38         | 4.74         | 3.66         | 9.07         | 5.24        |

Source: Phillip Securities (HK) Research, Bloomberg

## Risk

The launch of new products fails expectations; Industry policy risk.

## Financials

**Table-6: Financial data**

| FYE DEC                             | FY17A      | FY18A      | FY19E      | FY20E      | FY21E      |
|-------------------------------------|------------|------------|------------|------------|------------|
| <b>Valuation Ratios</b>             |            |            |            |            |            |
| P/E                                 | 11.58      | 11.05      | 9.86       | 8.70       | 7.67       |
| P/B                                 | 1.20       | 1.10       | 1.02       | 0.94       | 0.87       |
| Dividend Yield                      | 2.65%      | 2.72%      | 3.08%      | 3.49%      | 3.96%      |
| <b>Per Share Data in RMB</b>        |            |            |            |            |            |
| EPS                                 | 1.31       | 1.37       | 1.54       | 1.74       | 1.98       |
| DPS                                 | 0.40       | 0.41       | 0.47       | 0.53       | 0.60       |
| BVPS                                | 12.66      | 13.79      | 14.86      | 16.07      | 17.45      |
| <b>Growth &amp; Margins (%)</b>     |            |            |            |            |            |
| <b>Growth</b>                       |            |            |            |            |            |
| Revenue                             | 8.35%      | 21.58%     | 17.91%     | 9.61%      | 9.65%      |
| Operating Profit                    | 23.29%     | 15.77%     | 13.46%     | 16.53%     | 14.30%     |
| Net Profit                          | 5.96%      | 9.82%      | 14.10%     | 13.24%     | 13.56%     |
| <b>Margins</b>                      |            |            |            |            |            |
| Gross Margin                        | 12.41%     | 13.64%     | 13.57%     | 13.91%     | 14.27%     |
| Operating Profit Margin             | 3.57%      | 3.40%      | 3.27%      | 3.47%      | 3.62%      |
| Net Profit Margin                   | 3.10%      | 2.80%      | 2.71%      | 2.80%      | 2.90%      |
| <b>Key Ratios</b>                   |            |            |            |            |            |
| ROA                                 | 3.98%      | 3.51%      | 3.24%      | 3.34%      | 3.53%      |
| ROE                                 | 10.72%     | 10.63%     | 10.74%     | 11.26%     | 11.80%     |
| <b>Income Statement in mn RMB</b>   |            |            |            |            |            |
| Revenue                             | 130,847.18 | 159,084.40 | 187,576.04 | 205,596.74 | 225,445.32 |
| GP                                  | 16,239.33  | 21,694.04  | 25,450.33  | 28,600.04  | 32,163.76  |
| EBIT                                | 5,873.12   | 6,351.16   | 7,350.47   | 8,236.45   | 9,257.89   |
| Profit before tax                   | 5,204.81   | 5,343.38   | 6,292.30   | 7,125.36   | 8,091.25   |
| NP                                  | 4,057.78   | 4,456.26   | 5,084.81   | 5,758.01   | 6,538.55   |
| Minority Interest                   | 537.14     | 575.20     | 733.28     | 830.36     | 942.92     |
| NP attributable to shareholders     | 3,520.64   | 3,881.06   | 4,351.53   | 4,927.65   | 5,595.63   |
| <b>Balance Sheet in mn RMB</b>      |            |            |            |            |            |
| Cash and equivalents                | 13,569.41  | 16,605.56  | 17,435.83  | 18,307.62  | 19,223.01  |
| Inventories                         | 17,269.96  | 25,024.01  | 29,505.75  | 32,340.41  | 35,462.60  |
| Account Receivable                  | 36,529.58  | 48,014.84  | 56,614.19  | 62,053.19  | 68,043.89  |
| Others                              | 1,273.31   | 3,627.17   | 3,808.53   | 3,998.95   | 4,198.90   |
| Assets classified as held for sale  |            | 6.30       | -          | -          | -          |
| Total Current Assets                | 68,642.68  | 93,278.35  | 107,364.60 | 116,700.49 | 126,928.70 |
| PP&E                                | 9,386.26   | 11,007.63  | 11,951.00  | 12,975.23  | 14,087.23  |
| Intangible Assets                   | 8,092.08   | 14,199.10  | 14,341.09  | 14,484.50  | 14,629.35  |
| Others                              | 8,223.88   | 8,394.72   | 8,478.67   | 8,563.46   | 8,649.09   |
| Total Non-current Assets            | 25,702.22  | 33,601.45  | 34,770.76  | 36,023.19  | 37,365.67  |
| Total Assets                        | 94,344.90  | 126,879.80 | 142,135.37 | 152,723.68 | 164,294.37 |
| Account Payable                     | 35,115.29  | 44,587.92  | 54,820.48  | 59,950.95  | 65,579.21  |
| Short-term Debt                     | 13,791.68  | 22,031.36  | 23,132.93  | 24,289.58  | 25,504.05  |
| Others                              | 724.53     | 2,090.16   | 2,111.07   | 2,132.18   | 2,153.50   |
| Total Current Liabilities           | 49,631.81  | 68,709.76  | 80,064.47  | 86,372.70  | 93,236.76  |
| Long-term Debt                      | 2,958.80   | 9,620.30   | 10,101.31  | 10,606.38  | 11,136.70  |
| Others                              | 2,078.02   | 2,116.00   | 2,137.16   | 2,158.53   | 2,180.12   |
| Total Non-current Liabilities       | 5,036.82   | 11,736.30  | 12,238.47  | 12,764.91  | 13,316.81  |
| Total Liability                     | 54,668.63  | 80,446.06  | 92,302.95  | 99,137.61  | 106,553.57 |
| Shareholders' Equity                | 34,030.84  | 39,013.58  | 42,042.92  | 45,473.34  | 49,368.78  |
| Minority Interests                  | 5,645.01   | 7,419.70   | 7,789.50   | 8,112.72   | 8,372.02   |
| Total Equity                        | 39,675.85  | 46,433.27  | 49,832.42  | 53,586.06  | 57,740.79  |
| <b>Cashflow Statement in mn RMB</b> |            |            |            |            |            |
| Profit before tax                   | 5,204.81   | 5,343.38   | 6,292.30   | 7,125.36   | 8,091.25   |
| Depreciation&Amortization           | 934.37     | 1,302.21   | 1,386.08   | 1,476.87   | 1,575.16   |
| Depreciation                        | 721.30     | 935.97     | 1,016.18   | 1,103.27   | 1,197.83   |
| Amortization                        | 213.07     | 366.24     | 369.90     | 373.60     | 377.33     |
| minus Change in Working Capital     | 1,418.57   | 10,761.26  | 3,002.83   | 3,312.51   | 3,663.25   |
| minus Income tax paid               | 904.10     | 1,371.42   | 1,207.49   | 1,367.35   | 1,552.71   |
| Others                              | -2,175.20  | 7,083.18   | -119.26    | -119.26    | -119.26    |
| OCF                                 | 1,641.31   | 1,596.08   | 3,348.80   | 3,803.11   | 4,331.19   |
| Capex                               | -2,735.24  | -2,049.29  | -2,224.92  | -2,415.60  | -2,622.62  |
| Change in other assets              | 541.41     | -5,441.61  | -601.78    | -607.80    | -613.88    |
| ICF                                 | -2,193.83  | -7,490.90  | -2,826.71  | -3,023.40  | -3,236.50  |
| Net change in debt                  | 4,273.43   | 14,901.18  | 1,582.58   | 1,661.71   | 1,744.80   |
| Others                              | -1,112.46  | -6,037.66  | -1,686.31  | -1,703.17  | -1,720.20  |
| FCF                                 | 3,160.97   | 8,863.52   | -103.73    | -41.46     | 24.59      |
| Cash flow (net)                     | 2,608.45   | 2,968.70   | 418.37     | 738.25     | 1,119.28   |

Source: Company, Phillip Securities (HK) Research  
(Financial data as of December 31, 2019)

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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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