

Sino Biopharma



Margins shrink, top line still strong

HOLD (from BUY)

Key points:

- 3Q revenue rose 74.3% YoY to HK\$584.6m and net profit 6.8% YoY to HK\$66.6m. Pre-tax profit was up 41.5% YoY at HK\$138.8m
- New blockbuster drugs, such as Mingzheng capsules, helped sustain high top line growth
- R&D costs surge 143.9% as drug projects enter trials
- No short term re-rating catalysts, but SB's strong drug pipeline puts it ahead of cash-rich peers such as Shineway (2877 HK) and Wuyi (1889 HK)
- Downgrade to HOLD, target price of HK\$1.10, representing 8.0x FY12/09F P/E

3Q top line growth offsets margin squeeze. Sino Biopharmaceutical's (SB) 3Q FY12/08A's top line beat our expectations with revenue growth of 74.3% YoY to HK\$584.6m and a net profit increase 6.8% to HK\$66.6m. However, its gross margin shrunk 3.5 pcp YoY to 77.9% and net margin 7.2 pcp YoY to 11.4%, mainly because of increasing R&D expenses (up 143.9% YoY) and a higher effective tax rate (from 8% in 3Q FY12/07A to 27.7% in 3Q FY12/08A), eroding net profit. Pre-tax profit increased 41.5% YoY to HK\$138.8m.

More drugs enter trials. Management explained that the surge in R&D costs was mainly due to a high number of drug projects entering the trial stage. In 3Q FY12/08A, R&D expenses accounted for 4.5% of revenue (3Q FY12/07A: 3.2%). The increase in the company's effective tax rate was expected.

New blockbuster drugs bring high growth. Besides contributions from new assets acquired in 2007, new blockbuster drugs continue to keep SB's top line growth high. In 3Q FY12/08A, sales of Mingzheng capsules grew 113.6% YoY to HK\$121.3m, Tianqing Ganping capsules 89.3% YoY to HK\$38.3m and Tianqing Ganmei injections 197.8% YoY to HK\$49.4m. Among key legacy drugs, Kaishi injections' growth slowed to 26.9% YoY to HK\$159.2m (2Q FY12/08A: 45.5%), while revenue from Ganlixin dropped 2.0% YoY to HK\$71.6m.

Downgrade to HOLD, revised target price to HK\$1.10. We have cut our earnings forecast to HK\$253.2m for FY12/08F and HK\$313.0m (from HK\$278.2m and HK\$335.8m, respectively) to incorporate the company's higher cost structure. While we acknowledge that the stock may lack near-term catalysts, we believe its solid drug pipeline puts it ahead of cash-rich peers such as Shineway (2877 HK, HK\$3.50) and Wuyi (1889 HK, HK\$0.77). Downgrade to HOLD, with a revised target price of HK\$1.10, representing 8.0x FY12/09F P/E.

China Pharmaceuticals

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Stock data

Price	HK\$1.03
Target price	HK\$1.10 (+7%)
12 mth range	HK\$0.70-1.88
Market cap.	US\$299.2m
Daily t/o, 3 mth	US\$0.2m
Free float %	44.6%
Ticker	1177.HK/1177 HK

Financial summary

Year to Dec	06A	07A	08F	09F	10F
Turnover (HK\$m)	734.71	1,164.32	1,059.72	689.23	237.6
Net Profit (HKm)	141.2	224.4	253.2	313.0	368.4
EPS (HK)	0.062	0.099	0.112	0.138	0.163
EPS Δ%	(91.3)	58.9	12.9	23.6	17.7
P/E (x)	16.5	10.4	9.2	7.5	6.3
P/B (x)	1.22	1.15	0.96	0.86	0.77
EV/EBITDA (x)	6.1	2.3	0.9	0.4	(0.1)
Yield (%)	4.9	5.8	6.5	8.1	9.5
ROE (%)	7.5	11.4	11.4	12.1	12.8
ROCE (%)	6.3	12.3	19.4	20.0	21.5
N. Gear. (%)	Cash	Cash	Cash	Cash	Cash

Price Performance

	1 mth	3 mth	12 mth
Relative to HSI (%)	60.4	31.8	47.2
Actual price changes (%)	28.8	-22.6	-34.8

	08F	09F	10F
Consensus EPS (HK\$)	0.130	0.160	0.201
Previous forecasts (HK\$m)	278.2	335.8	400.0
Previous EPS (HK\$)	0.123	0.148	0.177

Price Chart



Table 1: 3Q FY12/08A results summary

3 months to Sep.	Turnover (HK\$m)	Gross profit (HK\$m)	Gross margin (%)	Pre-tax profit (HK\$m)	Tax rate (%)	Net profit (HK\$m)	EPS (HK\$)	DPS (HK\$)
3Q FY08	584.6	455.4	77.9	138.8	27.7	66.6	0.029	0.010
3Q FY07	335.5	272.9	81.4	98.1	8.0	62.4	0.028	0.015
YoY (%)	74.3	66.9	-	41.5	-	6.8	6.8	-

Source: Company data

Table 2: 3Q FY12/08A revenue breakdown

3 months to Sep (HK\$m)	Revenue	YoY change (%)	% of turnover
Cardio-cerebral medicines	114.6	59.2	19.6
Hepatitis medicines	314.8	63.2	53.9
Oncology medicines	47.0	130.4	8.0
Others	108.2	115.4	18.5
Total	584.6	74.3	100.0

Source: Company data

Table 3: P&L

Year to Dec (HK\$m)	06A	07A	08F	09F	10F
Turnover	734.7	1,164.3	2,059.7	2,689.2	3,237.6
Cost of sales	(138.8)	(205.8)	(463.0)	(645.4)	(783.5)
Gross profit	595.9	958.5	1,596.6	2,043.8	2,454.1
Other income and gains	91.5	98.4	77.8	55.0	57.5
Selling and distribution costs	(327.7)	(503.8)	(809.1)	(1,075.7)	(1,278.9)
Administrative expenses	(121.8)	(154.7)	(226.8)	(271.6)	(340.0)
Other operating expenses	(31.3)	(53.7)	(124.0)	(161.9)	(194.9)
Operating profit	206.6	344.7	514.5	589.8	707.8
Finance costs, net	(2.2)	(2.6)	(9.1)	(5.4)	(6.5)
Share of profits of an associated	0.7	0.2	-	-	-
Exceptionals	-	-	-	-	-
Profit before taxation	205.1	342.3	505.4	584.3	691.5
Taxation	(22.1)	(34.0)	(126.3)	(146.1)	(172.9)
Profit after tax	183.0	308.3	379.1	438.2	518.6
Minority interests	(41.8)	(84.0)	(125.9)	(125.2)	(150.2)
Profit attributable to shareholders	141.2	224.4	253.2	313.0	368.4
% chg	-	58.9	12.9	23.6	18.0
Dividends	(113.2)	(135.8)	(151.9)	(187.8)	(221.0)

Source: Company data

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