

Jiwa Bio-Pharm Holdings

Timing for profit jump

to summarize...

- The healthcare industry increased 25.3% in net profit for first 11m of 2009 and outlook is positive.
- Jiwa's 1H FY03/10A results is impressive with 36.8% YoY growth in bottom line mainly driven by specialized drugs.
- "Song Taisi 松泰斯" and "Gluthion 古拉定" is a leading market players, taking 24.9% market share with total sales of HK\$130.0 in 1H FY03/10A, which shows Jiwa's capability in ramping up blockbuster drugs.
- Edaravone injections (依达拉奉注射液) - "Jiwa Youmin 积华尤敏" was launched in 2009 and has won the bid in 17 provinces.
- "Transton 同息通" accounted for 10.9% market share, showing solid growth.
- "Jida Bente 积大本特" increased 126.4% YoY in FY03/09A and 120.0% YoY
- Other specialized drugs show good potential as well.
- Mr. Lau and his family is holding 71.1% of the listco and dividend payout ratio between 25.0% and 35.0%
- It is currently trading at 16.1x FY03/10F P/E and 11.8x FY03/11F P/E based on our back of pad estimate

Company Background. Jiwa is mainly engaged in the manufacture, trading and distribution of specialized drugs and anti-infectious drugs. The company was started in 1994 and listed in HKEx Main Board in 2003. The listco hold 70.0% of Jida while the other 30.0% was owned by Yunan Pharmaceutical, the main pharmaceutical distributor in Yunan Province. Jida is now the fifth biggest pharmaceutical company in Yunan Province.

Favorable industry environment. The healthcare industry is developing quickly after SFDA and NDRC's effort in restructuring and cleaning up the industry throughout 2005-2007. The industry growth rates rebounded to 24.9% in 2007 with net profit growth of 55.6%. The sales kept increasing 28.1% while net profit was up 28.3% in 2008. For first 11 months of 2009, sales increased 21.3% YoY to RMB991.2b while the net profit increased 25.3% for first 11 month. The government expenditure as a percentage of total expenditure increased from 18.0% in 2006 to 24.7% in 2008. However, the medical expenditure level is still very low in China comparing to other countries in the world. According to WHO's 2005 statistics, China's expenditure on health as percentage of GDP was only 4.7%, ranking 153 in 192 countries in the world. The percentage increased to 4.8% in 2008, but it was still in the low level in the world. With China's growing economy, the government is increasing its effort in health expenditure: 1) In 2009, the government said that it will invest RMB850b in following 3 years in health expenditure; 2) medical insurance to cover all residence with the coverage ratio of 85.6% by April 2009; 3) widen and strengthen healthcare network by building up community healthcare centers and healthcare service point. We think that the increasing government effort in improving the healthcare standard in China would encourage the development of the industry.

Jiwa's impressive 1H FY03/10A results. The sales increased 75.3% YoY to HK\$326.7m while the net profit increased 36.8% YoY to HK\$32.0m. The sales of finished drugs increased 20.7% YoY to HK\$178.3m, accounting for 54.6% of total sales, while the operating profit increased 54.7% YoY to HK\$39.3m, accounting for 79.8% of total operating profit. The pharmaceutical trading business increased 19.0% YoY to HK\$45.2m, accounting for 13.8% YoY to HK\$13.0m, while the operating profit increased 25.8% YoY to HK\$13.0. The new injected distribution business made revenue of HK\$101.2m with operating profit of HK\$1.8m.

| Ticker | 2327HK |
|------------------------|-----------|
| Rating | Not Rated |
| Price (HK\$) | 0.64 |
| Target Price (HK\$) | N.A. |
| 12m Price Range (HK\$) | 0.17-0.78 |
| Market cap. (US\$m) | 132.2 |
| Daily t/o (US\$m) | 0.7 |
| Free float (%) | 28.9 |

Financial summary

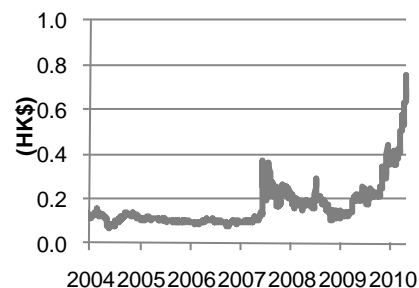
| Year to Mar | 07A | 08A | 09A |
|--------------------|-------|-------|-------|
| Turnover (HK\$m) | 206.6 | 317.4 | 472.1 |
| Net Profit (HK\$m) | 21.1 | 48.3 | 51.2 |
| EPS (HK\$) | 0.014 | 0.031 | 0.032 |
| P/E (x) | 45.6 | 20.8 | 20.1 |
| P/B (x) | 4.2 | 3.4 | 3.1 |
| EV/EBITDA (x) | 21.6 | 12.1 | 13.0 |
| Yield (%) | 0.6 | 1.6 | 1.6 |
| ROE (%) | 9.7 | 18.5 | 16.2 |
| ROCE (%) | 7.5 | 12.8 | 10.5 |
| N. Gear. (%) | 11.4 | 23.3 | 29.7 |

Source: SBI/Bloomberg

| | 10F | 11F | 12F |
|---------------------------|-----|-----|-----|
| Consensus EPS (HK\$) | - | - | - |
| Previous earnings (HK\$m) | - | - | - |
| Previous EPS (HK\$) | - | - | - |

Price performance

| Year to Dec | 1m | 3m | 12m |
|--------------------------|-------|-------|--------|
| Relative to HSI (%) | +12.8 | +63.1 | +145.0 |
| Actual price changes (%) | +10.3 | +68.4 | +240.4 |



Source: Bloomberg

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Table 1. 1HFY03/10A results

| 6 months to Sep | Turnover (HK\$m) | Gross Profit (HK\$m) | Gross margin (%) | Pre-tax profit (HK\$m) | Tax rate (%) | Net profit (HK\$m) |
|-----------------|------------------|----------------------|------------------|------------------------|--------------|--------------------|
| 1H FY03/10A | 326.7 | 145.4 | 44.5 | 46.8 | 10.7 | 32.0 |
| 1H FY03/09A | 186.4 | 79.3 | 42.5 | 30.7 | 1.6 | 23.4 |
| YoY | 75.3 | 83.4 | | 52.4 | | 36.8 |

Source: Company data

Table 2. 1HFY03/10A segment breakdown

| 6 months to September (HK\$m) | Revenue | YoY change (%) | % of total | Operating profit | YoY change (%) | % of total |
|---------------------------------|---------|----------------|------------|------------------|----------------|------------|
| Finished drugs | 178.3 | 20.7 | 54.6 | 39.3 | 54.7 | 79.8 |
| Trading and healthcare products | 45.2 | 19.0 | 13.8 | 13.0 | 25.8 | 26.4 |
| Distribution business | 101.2 | - | 31.0 | 1.8 | - | 3.7 |
| Pharmaceutical bulk material | 2.1 | 188.1 | 0.6 | (4.9) | - | (9.9) |
| Total | 326.7 | 75.3 | 100.0 | 49.2 | 51.3 | 100.0 |

Source: Company data

Leader in domestic glutathione product (谷胱甘肽) market. Reduced glutathione sodium for injection (注射用还原型谷胱甘肽钠) is used for treatment of liver impairment of different origins, auxiliary treatment for radiotherapy, chemotherapy, hypoxemia and hepatitis disease. Jiwa was the leader in this market, accounting for 29.0% market share in China. It has been the exclusive distributor in China for “Gluthion 古拉定” reduced glutathione sodium for injection (注射用还原型谷胱甘肽钠) manufactured by Italia Laboratorio Farmaceutico C.T. since 1996. Jiwa also launched its own reduced glutathione sodium for injection (注射用还原型谷胱甘肽钠)- “Song Taisi 松泰斯” in 2003. In FY03/09, the sales of “Gluthion 古拉定” was HK\$149.0m and “Song Taisi 松泰斯” was HK\$71m., which shows Jiwa’s capability in handling blockbuster drugs. The sales were affected in 2H 2009 because of the temporary shortage of raw material. The company has expects that two products could keep a 30.0%+ growth in coming years because of its strong demand.

Edaravone Injection is expected to ramp up quickly. Jiwa launched its Edaravone injections (依达拉奉注射液) - “Jiwa Youmin 积华尤敏” in 2009. Edaravone injection(依达拉奉注射液) is mainly used for improving nerve syndromes, and daily activity capacity and function impairment caused by acute stroke. Edaravone injections (依达拉奉注射液) is now in the regional medicine insurance list of 22 provinces and cities in China. There were only five approved manufacturers in China. Simcere (SCR US) owns two manufacturers, accounting for 92.7% market share. Simcere’s total sales of Edaravone injections (依达拉奉注射液) in FY12/09A was RMB745.4m. Jiwa has a vertically integrated production line for Edaravone injection(依达拉奉注射液) from raw material to finished product, which allow it to have around 80.0% gross margin. The company found that “Jiwa Youmin 积华尤敏” was accepted well in the first year of launch and has won the bid in 17 provinces. Jiwa will further widen its distribution channel and increasing its sales effort in this product to ramp up “Jiwa Youmin 积华尤敏” quickly to be a key blockbuster drugs for the company

“Transton 同息通” is a solid growth driver and profit contributor. Triamcinolone Acetonide Injection (曲安奈德注射液) is used for rheumatoid arthritis, bronchial asthma, allergic rhinitis, acute sprain, frozen shoulder, chronic limb ache and different kind of skin diseases. Jiwas launched Triamcinolone Acetonide Injection (曲安奈德注射液)-“Transton 同息通” in 2002. “Transton 同息通” accounted for 10.9% of Triamcinolone Acetonide product market. The sales of this product increased 18.6% YoY in FY03/09 to HK\$70m and 23.1% YoY in 1H FY03/10 to HK\$48m with gross margin of around 60.0%. Jiwa expects that the product could keep a solid growth in coming years driven by the increasing market demand and potential to be listed in regional EDL list.

“Jida Bente 积大本特” is in high growth. Tamsulosin Hydrochloride (盐酸坦洛新) is mainly used for benign prostatic hyperplasia. Jiwa’s Tamsulosin Hydrochloride (盐酸坦洛新) “Jida Bente 积大本特” was launched in 2006. It is easy to take, even elderly patients with swallowing difficulty could take it as well. It currently accounted for 4.8% of the market share. The key competitor was Astellas Pharma Inc. (4503 JP), which had 81.1%+ market share. Jiwa’s product has won the tender in cities, such as Beijing, Guangzhou, Xian and Zhejiang. The product is currently in high growth stage. Its sales increased 126.4% YoY to HK\$12.0m in FY03/09A and 120.0% YoY to HK\$11.0m in 1HFY03/10A.

Table 3. key products performance and outlook

| | FY03/08A | FY03/09A | YoY | 1HFY03/09A | 1H FY03/10A | YoY(%) | GP Margin | FY03/11F |
|--------------------|----------|----------|-------|------------|-------------|--------|-----------|----------|
| | HK\$m | HK\$m | (%) | HK\$m | HK\$m | | % | Outlook |
| “Gluthion 古拉定” | 126 | 149.0 | 18.3 | 58.0 | 84.0 | 44.8 | 60.0 | 30.0%+ |
| “Song Taisi 松泰斯” | 46.0 | 71.0 | 54.3 | 37.0 | 46.0 | 24.3 | 45.0 | 30.0%+ |
| “Jiwa Youmin 积华尤敏” | - | 2.7 | - | - | 9.0 | - | 80.0+ | 50.0%+ |
| “Transton 同息通” | 59.0 | 70.0 | 18.6 | 39.0 | 48.0 | 23.1 | 60.0 | 20.0%+ |
| “Jida Bente 积大本特” | 5.3 | 12.0 | 126.4 | 5.0 | 11.0 | 120.0 | 80.0+ | 50.0%+ |

Source: Company data&SBI E2Capital

Table 4. Key products industry info.

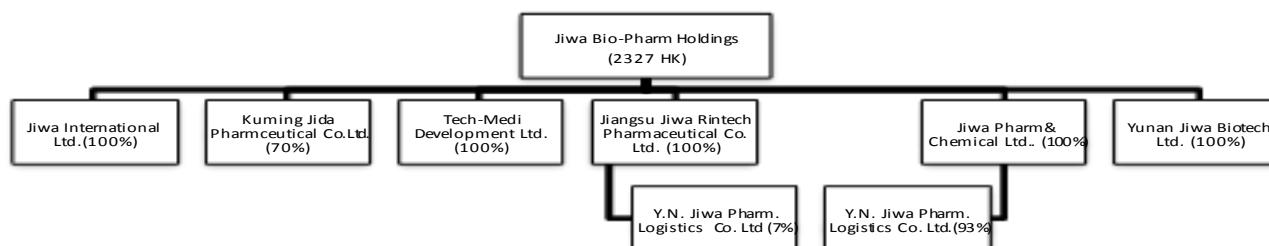
| | Market share (%) | Market Ranking | National Medical Insurance | Local EDL | Medical insurance refund rate |
|--------------------|------------------|----------------|----------------------------|-----------|-------------------------------|
| “Gluthion 古拉定” | 17.2 | Second | Catalogue II | | Up to 90% |
| “Song Taisi 松泰斯” | 7.7 | Fifth | Catalogue II | Potential | Up to 90% |
| “Jiwa Youmin 积华尤敏” | 1.6 | Fourth | Catalogue II | | Up to 90% |
| “Transton 同息通” | 10.9 | Fourth | Catalogue II | Potential | Up to 90% |
| “Jida Bente 积大本特” | 4.8 | Third | Catalogue II | | Up to 90% |

Source: Company data & SBI E2Capital

Highlight of other drugs. Other potential drug development is as follows: 1) “Artrodar 安必丁” (exclusively distribution agreement in China with Swiss company-TRB Chemedica) launched in FY03/06A, which is for treatment of degenerative joint disease, is now developing quickly with 160.0% YoY growth to HK\$13.0m in 1HFY03/10A; 2) “Shi Si Tai 时士太” (treatment of a variety of neoplasms, giantism and acromegaly) and “Huo Duo Shi 活多史” (good antithrombotic effect) were launched in FY03/06A, which shows positive market acceptance; 3) vertically integrated production line for Citalopram Hydrobromide (antidepressant drug); 4) expects to launch 2-5 new product per year.

Corporate governance. Mr. Lau and his family started international drug trading in China since 1987. Mr. Lau started Kuming Jida Pharm in 1993, which finished registration in 1994. Jiwa set up Jiangsu Jiwa Rintech, which is engaged in pharmaceutical bulk material in November 2004. Jiwa acquired Jiwa Pharm and Chemical at price of HK\$9.7m in October 2008. Mr. Lau is the founder and Chairman of the company and his son is the founder, Vice Chairman and CEO. Currently, Mr. Lau and his family are holding 71.1% of the listco. The company has paid dividend every year with dividend payout ratio between 25.0% and 35.0%.

Chart 1. Key holding companies



Source: Company data

Risks. 1) Government regulation risk; 2) risk from unexpected accident; 3) market liquidity.

Peers comparison and valuation. Our back of pad estimate shows that the counter is currently trading at 16.1x FY03/10F P/E and 11.8x FY03/11F P/E. We think that Jiwa's business model is close to Sino Biopharmaceutical (1177 HK) and Lee's Pharm (8221 HK). After comparison, we find that: 1) Jiwa is currently trading at 43.7% discount to Sino Bio-pharm and 23.3% discount to Lee's Pharm in terms of 1-Yr forward P/E; 2) Jiwa's growth potential and dividend yield is similar to Sino-Biopharm; 3) dividend yield is better than Lee's Pharm; but 3) Jiwa's gross margin is lower than other two companies because of its lower margin business from anti-infection drugs. In our view, we think Jiwa is undervalued because: 1) Strong growth potential with its specialized drugs; 2) start of profit jumping stage because several specialized drugs start to show scale effect; 3) rich product development pipeline.

Table 5. Peers comparison

| | Fiscal Year | Turnover (HK\$m) | Gross Margin (%) | Net profit (HK\$m) | Mkt. Cap (US\$m) | 1-Yr P/E (x) | 2-Yr P/E (x) | Yield (%) | YoY Guidance For net profit(%) |
|---------------------------|-------------|---------------------|---------------------|-----------------------|---------------------|-----------------|-----------------|--------------|-----------------------------------|
| Jiwa (2327 HK)* | FY03/09 | 472.1 | 44.0 | 51.2 | 132.2 | 16.1 | 11.8 | 1.6 | 30.0 + |
| Sino Bio-pharm (1177 HK)* | FY12/09 | 3,243.6 | 80.3 | 397.0 | 1897.6 | 28.6 | 24.0 | 1.6 | 30.0+ |
| Lee's Pharm (8221 HK)** | FY12/09 | 173.8 | 71.7 | 46.4 | 194.1 | 21.0 | 15.3 | 0.7 | - |

*the P/E is based our estimate ** the P/E is based on market consensus

Source: Company data, SBI E2Capital & Bloomberg

Table 6. P&L

| Year to Mar (HK\$m) | 07A | 08A | 09A | 1H09A | 1H10A |
|-----------------------------------|---------|---------|---------|---------|---------|
| Revenue | 206.6 | 317.4 | 472.1 | 186.4 | 326.7 |
| Cost of sales | (109.3) | (171.4) | (263.9) | (107.0) | (181.3) |
| Gross profit | 97.3 | 146.0 | 208.2 | 79.3 | 145.4 |
| Other income | 3.7 | 21.9 | 7.9 | 3.7 | 3.1 |
| Selling expenses | (23.7) | (39.5) | (78.1) | (21.3) | (68.3) |
| Administrative expenses | (39.6) | (51.6) | (59.7) | (26.6) | (30.1) |
| Share-based employee compensation | | | | (1.3) | - |
| Other operating expenses | (2.6) | (2.6) | (4.6) | (0.9) | (0.8) |
| Profit from operation | 35.2 | 74.2 | 73.7 | 32.9 | 49.4 |
| Finance costs | (2.3) | (4.6) | (4.5) | (2.2) | (2.5) |
| Share of results of associates | | (0.0) | (0.1) | (0.1) | (0.1) |
| Profit before taxation | 32.8 | 69.6 | 69.0 | 30.7 | 46.8 |
| Income tax expenses | (5.8) | (11.5) | (5.7) | (0.5) | (5.0) |
| Profit for the period | 27.1 | 58.1 | 63.3 | 30.2 | 41.8 |
| Attributable to: | | | | | |
| Equity holders of the Company | 21.1 | 48.3 | 51.2 | 23.4 | 32.0 |
| Minority interests | 6.0 | 9.9 | 11.8 | 6.8 | 9.9 |
| Dividend (HK\$m) | 6.0 | 16.1 | 16.1 | | |

Source: Company data

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BUY : absolute upside of >10% over the next six months

HOLD : absolute return of -10% to +10% over the next six months

SELL : absolute downside of >10% over the next six months

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