

Shandong Weigao

Defensive player

to summarize...

- Revenue increased 30.1% YoY to RMB513.0m with net profit up 33.5% YoY to RMB141.0m for 1Q FY12/10A.
- Sales of consumable product increased 30.0% YoY while the sales of blood purification kits increased 160.4% YoY and orthopaedic product increased 20.6% YoY.
- New JV with Nikkiso will start manufacturing at the end of 2010.
- The contribution from JWMS is beyond the expectation with 57.9% YoY growth.
- Although Medtronic JV contribution increased 60.9% YoY, the contribution would not be significant in short term.
- Target price of HK\$32.58 is unchanged. Maintain HOLD.

1Q FY12/10A results. Weigao's results were in line with our estimate for 1Q FY12/09A. Revenue increased 30.1% YoY to RMB513.0m while net profit increased 33.5% YoY to RMB141.0m. The gross margin improved 2.6 pcp YoY to 50.7% while the net profit margin widened 0.7 pcp YoY to 27.5%. The distribution cost increased 51.4% YoY mainly because of free training to the staff in some hospitals and increasing its own sales training. The administrative expenses increased 42.6% YoY mainly because of 42.0% increase in R&D expenditure and RMB5.4m bad debt provision. However, the contribution from DES JV and Medtronic JV increased 57.8% YoY and 60.8% YoY, which offset some effect from increase of distribution cost and administrative expenses.

Table 1.1Q FY12/10A results

3 months to Mar	Turnover (RMBm)	Gross Profit (RMBm)	Gross margin (%)	Pre-tax profit (RMBm)	Tax rate (%)	Net profit (RMBm)
1Q FY10	513.0	260.0	50.7	154.7	8.7	141.0
4Q FY09	500.2	311.1	62.2	215.9	11.6	189.8
QoQ(%)	2.6	(16.4)		(28.3)		(25.7)
1Q FY09	394.3	189.5	48.1	116.3	10.1	105.6
YoY (%)	30.1	37.2		33.0		33.5

Source: Company data

Growth Driver. For 1Q FY12/10A, the sales of medical consumable product increased 30.0% YoY growth to RMB423.4m, which was mainly driven by 43.8% YoY growth to RMB153.2m, 91.7% YoY growth to RMB18.3m in pre-filled syringes and 41.5% YoY growth to RMB31.3m in other consumables. The sales of blood purification kits were growing quicker than expectation with 160.4% YoY growth to RMB25.8m. The sales of orthopaedic product increased 20.6% YoY to RMB34.7m, which would expect to grow faster in the following quarters in 2010.

JV with Nikkiso. Weigao announced in April 2010 to form a JV in manufacturing and sales of hemodialysis machines in China. Weigao Blood (70.0% hold by Weigao) will hold 51.0% of the JV. Weigao will benefit from the JV by: 1) contribution from the JV by manufacturing and sales of hemodialysis machine; 2) contribution from distribution of hemodialysis machine by Weigao's distribution network. The management said that the JV is expected to start manufacturing at the end of 2010, but the contribution for the company in 2010 would be small. The accounting method for the JV is now under the discussing.

JWMS and Medtronic JV performance were better than expectation. In 1Q FY12/10A, the contribution from JWMS increased 57.9% YoY to RMB34.9m, which was mainly driven by the volume growth. The market has been expected that the price pressure and vicious competition in Chinese DES market would slow down the

Ticker	8199 HK
Rating	HOLD(Unchanged)
Price (HK\$)	33.50
Target Price (HK\$)	32.58(-3%)
12m Price Range (HK\$)	16.00-39.80
Market cap. (US\$m)	4,622.5
Daily t/o (US\$m)	3.4
Free float (%)	30.7

Financial summary

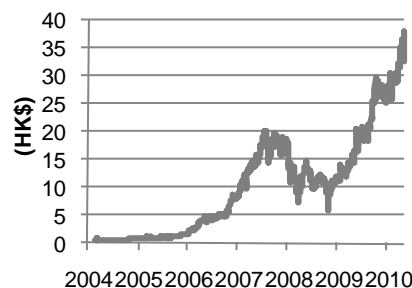
Year to Dec	08A	09A	10F	11F	12F
Turnover (RMBm)	1,514.4	1,878.5	2,503.9	3,255.0	4,231.5
Net Profit (RMBm)	482.4	633.9	853.9	1,079.0	1,413.0
EPS (RMB)	0.485	0.589	0.793	1.003	1.313
P/E (x)	60.8	50.1	37.2	29.4	22.5
P/B (x)	13.2	11.2	9.4	7.5	5.9
EV/EBITDA (x)	52.6	41.4	30.0	23.6	17.4
Yield (%)	0.5	0.5	0.8	1.0	1.3
ROE (%)	25.4	23.4	26.5	27.4	28.5
ROCE (%)	25.3	24.6	28.4	29.7	31.8
N. Gear. (%)	Cash	Cash	Cash	Cash	Cash

Source: SBI/Bloomberg

	10F	11F	12F
Consensus EPS (RMB)	0.792	1.030	1.280
Previous earnings (RMBm)	853.8	1,092.1	1,374.4
Previous EPS (RMB)	0.793	1.015	1.277

Price performance

Year to Dec	1m	3m	12m
Relative to HSI (%)	+12.5	+15.6	+75.4
Actual price changes (%)	+2.9	+15.3	+107.8



Source: Bloomberg

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growth of JWMS. The better than expected results show that the demand for DES product in China is still strong. The Medtronic JV contribution increased 60.9% YoY to RMB10.3m mainly because the JV sold some its inventories. We think that Medtronic JV contribution would still not be significant in short term as Weigao still need time to work with Medtronic to make each other corporate better.

Table 2. 4Q FY12/09A revenue breakdown and 2010 growth guidance

3months to Dec	1Q FY10 (RMBm)	YoY (%)	% of total (%)	2010 growth Guidance(%)	Notes
Self-produced products					
Consumables					
Infusion sets	153.2	43.8	29.9	40	2010 full year guidance unchanged
Syringes	91.4	22.9	17.8	20	2010 full year guidance unchanged
Needles	84.1	20.8	16.4	25	2010 full year guidance unchanged
Blood bags	35.3	9.5	6.9	15	Production staff shortage, 2010 full year guidance unchanged
Blood sampling products	9.8	(13.5)	1.9	40	Some export order cancelled, 2010 full year guidance revise down
Pre-filled syringes	18.3	91.7	3.6	50	2009 delayed order achieved in 1Q, 2010 full year guidance unchanged
Other consumables	31.3	41.5	6.0	40	2010 full year guidance unchanged
Subtotal for consumables	423.4	30.0	82.5		
Orthopaedic products	34.7	20.6	6.8	30	2010 full year guidance unchanged
Blood Purification consumable	25.8	160.4	5.0	100	2010 full year guidance unchanged
PVC granules	13.3	17.5	2.6	35	2010 full year guidance unchanged
Subtotal for self-produced product	497.2	32.3	96.9		
Trading					
Medical instruments	8.0	(41.6)	1.6	35	Stop sale of Gambro machine, 2010 full year guidance revised down
Other products	7.8	63.9	1.5	35	2010 full year guidance unchanged
Subtotal for trading product	15.8	(15.1)	3.1		
Total	513.0	30.1	100.0		

Source: Company data

Valuation. We maintain our target price of HK\$32.58, representing 36.1x FY12/10F and 29.6x FY12/11F P/E based on our estimate. We think that the solid fundamental and strong growth potential make Weigao a defensive choice in the volatile market. We recommend to HOLD.

Table 3: P & L

Year to Dec (RMBm)	08A	09A	10F	11F	12F
Turnover	1,514.4	1,878.5	2,503.9	3,255.0	4,231.5
Cost of sales	(756.1)	(877.2)	(1,155.3)	(1,488.9)	(1,918.6)
Gross profit	758.2	1,001.3	1,348.5	1,766.1	2,312.9
Other net (loss)/income	78.1	69.0	107.8	51.8	56.3
Selling and distribution costs	(208.7)	(321.3)	(443.6)	(544.2)	(665.1)
Administrative expenses	(137.7)	(180.9)	(242.8)	(296.2)	(359.6)
Operating profit	489.9	568.0	769.9	977.6	1,344.4
Financial costs	(30.2)	(4.0)	(4.2)	(4.0)	(4.0)
Share of loss of a jointly controlled entity	56.0	109.4	140.8	147.9	155.2
Share of loss of an associate	8.4	31.6	50.4	75.6	105.8
Pre-tax profit	524.1	705.0	956.9	1,197.0	1,601.5
Tax	(39.0)	(71.8)	(95.5)	(107.1)	(174.3)
Minority interests	(2.7)	0.7	(7.2)	(10.9)	(14.3)
Net profit	482.4	633.9	854.2	1,079.0	1,413.0

Source: Company data and SBI E2-Capital

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