

# CSPC Pharmaceutical (1093 HK)

## Another solid quarter

CSPC announced 3Q19 results. Total revenue/ net profit was up 27.5% / 24.0% YoY in 9M19, reaching 70% / 69% of our full-year estimates.

- **3Q19 results in line.** 9M19/ 3Q19 revenue was up 27.5%/ 27.4% YoY. 9M19 innovative drug sales rallied 51.9% YoY, contributing 57% of total revenue. Strong innovative drug growth was still driven by strong momentum in NBP and oncology portfolio, up 35.7% YoY and 170.7% YoY, respectively. 9M19 GPM improved by 5.7ppts to 70.9% because high-margin innovative drugs contributing higher proportion to the total sales. Meanwhile, selling expense ratio rose 4.3ppts and R&D expense ratio increased 2.0ppts, offsetting the impact from gross margin improvement. Net profit margin was slightly down 0.5ppts to 16.8%.
- **NBP and oncology portfolio will maintain strong momentum.** In 9M19, sales of NBP reached RMB4.0bn, up 35.7% YoY. We think NBP will continue to grow fast on a high base thanks to further channel penetration into lower tier cities. CSPC aims to expand the sales force for NBP from c.2,400 people by end-19E to 2,700-2,800 people by end-20E. In addition, oncology drug sales force will expand fast from c.2,700 people by Sep 2019 to 4,500 people by end-20E. NBP and oncology portfolio are safe from "volume-based procurement" because these are either innovative drugs or generics with special dosage formulations.
- **Better efforts on R&D.** In 9M19, CSPC spent RMB1.5bn in R&D, accounting for 9.0% of total revenue. CSPC has built up a comprehensive R&D platform, covering small molecules, large molecules, specialty dosage formulations, etc. The Company now has above 300 drugs in pipeline, including 40 new small molecules, 50 new large molecules, 20 generics with special dosage formulations. CSPC has received approval for 5 generics YTD, while clopidogrel generic has won the tenders for "4+7" volume-based procurement in Sep 2019, bringing additional RMB400-500m sales to CSPC. We expect the blockbuster drug, Amphotericin B Colloidal Dispersion (ABCD) to receive NMPA's approval in 2020E and may realize RMB1bn sales within 3-year of commercialization.
- **Maintain BUY with new TP of HK\$23.80.** We expect revenue to grow 28%/ 22.3%/ 25.2% YoY in FY19/20/21E and net profit to grow 29.2%/ 22.8%/25.6% YoY in FY19/20/21E. CSPC trades at 29x 19E P/E and 23x 20E P/E. **Catalysts:** 1) earlier-than-expected launch of new products, and 2) stronger-than-expected product sales.

### Earnings Summary

(YE 31 Dec)	FY17A	FY18A	FY19E	FY20E	FY21E
Revenue (RMB mn)	13,409	17,751	22,723	27,798	34,799
YoY growth (%)	25	32	28	22	25
Net income (RMB mn)	2,403	3,087	3,984	4,893	6,146
EPS (RMB)	0.39	0.49	0.64	0.78	0.99
YoY growth (%)	25.0	25.4	29.2	22.8	25.6
P/E (x)	46.4	37.0	28.6	23.3	18.6
P/B (x)	8.3	7.4	6.2	5.3	4.4
Yield (%)	0.7	0.8	1.0	1.3	1.6
ROE (%)	18.1	20.5	22.3	23.0	24.0
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, CMBIS estimates; Note: Exchange rate of HK\$ against RMB at 0.897.

## BUY (Maintain)

Target Price	HK\$23.80
(Previous TP	HK\$20.62)
Up/Downside	+15.82%
Current Price	HK\$20.55

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### Stock Data

Mkt Cap (HK\$ mn)	128,157
Avg 3 mths t/o (HK\$ mn)	700.91
52w High/Low (HK\$)	21.65/ 9.90
Total Issued Shares (mn)	6,236

Source: Bloomberg

### Shareholding Structure

Management	29.94%
Citigroup Inc	5.87%
BlackRock	4.75%
Free float	59.44%

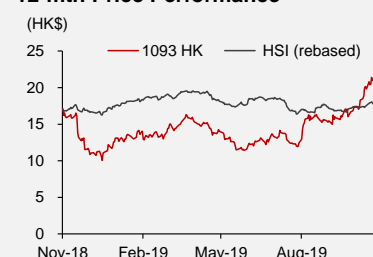
Source: HKEx

### Share Performance

	Absolute	Relative
1-mth	23.1%	25.5%
3-mth	67.2%	63.4%
6-mth	48.1%	57.3%

Source: Bloomberg

### 12-mth Price Performance



Source: Bloomberg

### Auditor: Deloitte

### Related Reports

1. The King is back – 20 Aug, 2019;
2. Growth prospects intact with encouraging margin performance- 22 May 19;
3. Results in-line; strong innovative drugs and intact generics –19 Mar 2019;

**Figure 1: 9M19 results changes**

	1Q18	1Q19	YoY	2Q18	2Q19	YoY	3Q18	3Q19	YoY
	RMB	RMB	Change	RMB	RMB	Change	RMB	RMB	Change
	mn	mn		mn	mn		mn	mn	
Innovative drugs	1,914	2,954	54.3%	2,044	3,195	56.3%	3,092	3,376	9.2%
Generics	1,261	1,291	2.4%	1,190	1,326	11.5%	1,193	1,245	4.3%
Antibiotics	321	347	8.1%	306	184	-39.7%	237	184	-22.5%
Vitamin C	548	524	-4.5%	503	634	26.1%	333	438	31.5%
Caffeine and Others	330	378	14.3%	343	345	0.5%	308	340	10.2%
<b>Total revenue</b>	<b>4,375</b>	<b>5,493</b>	<b>25.6%</b>	<b>4,385</b>	<b>5,685</b>	<b>29.6%</b>	<b>4,383</b>	<b>5,583</b>	<b>27.4%</b>
COGS	(1,563)	(1,652)	5.7%	(1,601)	(1,714)	7.0%	(1,409)	(1,508)	7.0%
<b>Gross profit</b>	<b>2,812</b>	<b>3,841</b>	<b>36.6%</b>	<b>2,784</b>	<b>3,971</b>	<b>42.6%</b>	<b>2,974</b>	<b>4,075</b>	<b>37.0%</b>
Other income and gains	39	32	-20.1%	71	68	-4.9%	96	116	20.3%
Distribution expenses	(1,477)	(2,064)	39.7%	(1,444)	(2,163)	49.8%	(1,575)	(2,231)	41.7%
Administrative expenses	(178)	(176)	-1.1%	(151)	(207)	37.7%	(171)	(200)	17.4%
Other expenses	(273)	(477)	74.6%	(296)	(484)	63.4%	(362)	(577)	59.5%
<b>Operating profit</b>	<b>922</b>	<b>1,156</b>	<b>25.3%</b>	<b>964</b>	<b>1,184</b>	<b>22.8%</b>	<b>963</b>	<b>1,183</b>	<b>22.8%</b>
Net finance costs	(9)	(14)	61.7%	(21)	(13)	-38.4%	(21)	(3)	-84.4%
Share of results of associates	8	16	92.5%	11	9	-19.7%	10	10	-2.1%
<b>Profit before tax</b>	<b>922</b>	<b>1,158</b>	<b>25.6%</b>	<b>954</b>	<b>1,180</b>	<b>23.6%</b>	<b>952</b>	<b>1,190</b>	<b>24.9%</b>
Income tax	(181)	(210)	16.0%	(199)	(239)	19.8%	(194)	(231)	19.4%
Minority interest	(2)	5	N/A	11	(15)	N/A	4	(26)	-742.3%
<b>Net profit</b>	<b>739</b>	<b>952</b>	<b>28.8%</b>	<b>766</b>	<b>926</b>	<b>21.0%</b>	<b>763</b>	<b>933</b>	<b>22.3%</b>
Gross margin	64.3%	69.9%	5.7ppt	63.5%	69.9%	6.4ppt	67.8%	73.0%	5.1ppt
Operating margin	21.1%	21.0%	-0.04ppt	22.0%	20.8%	-1.2ppt	22.0%	21.2%	-0.8ppt
Net margin	16.9%	17.3%	0.4ppt	17.5%	16.3%	-1.2ppt	17.4%	16.7%	-0.7ppt

Source: Company data

## Financial Summary

### Income statement

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
<b>Revenue</b>	<b>13,409</b>	<b>17,751</b>	<b>22,723</b>	<b>27,798</b>	<b>34,799</b>
Finished drug	9,864	13,758	18,612	23,568	30,446
Bulk medicines	3,545	3,994	4,111	4,230	4,354
Cost of sales	(5,304)	(5,991)	(6,483)	(7,228)	(8,700)
<b>Gross profit</b>	<b>8,105</b>	<b>11,761</b>	<b>16,241</b>	<b>20,571</b>	<b>26,100</b>
Other income and gains	52	296	337	413	520
Distribution expenses	(3,794)	(6,197)	(8,845)	(11,536)	(14,790)
Administrative expenses	(556)	(658)	(806)	(987)	(1,236)
R&D expenses	(707)	(1,345)	(1,981)	(2,391)	(2,958)
Other expenses	(81)	(26)	(40)	(49)	(61)
<b>Operating profit</b>	<b>3,019</b>	<b>3,831</b>	<b>4,905</b>	<b>6,021</b>	<b>7,575</b>
Share of profit of associate / JV	9	44	50	50	50
Net finance cost	(23)	(74)	(24)	(4)	(4)
Exceptional	-	-	-	-	-
Pre-tax profit	3,005	3,800	4,931	6,067	7,621
Profits tax	(594)	(736)	(955)	(1,183)	(1,486)
Minority interest	(8)	22	7	9	11
<b>Net profit</b>	<b>2,403</b>	<b>3,087</b>	<b>3,984</b>	<b>4,893</b>	<b>6,146</b>

### Cash flow summary

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
<b>EBIT</b>	<b>3,019</b>	<b>3,831</b>	<b>4,905</b>	<b>6,021</b>	<b>7,575</b>
Depreciation and amortization	621	630	2,006	2,635	2,519
Change in working capital	(234)	172	(607)	(666)	(687)
Income tax paid	(499)	(645)	(955)	(1,183)	(1,486)
Others	(57)	(250)	(1,350)	(1,959)	(1,843)
<b>Net cash from operating activities</b>	<b>2,851</b>	<b>3,738</b>	<b>3,999</b>	<b>4,848</b>	<b>6,078</b>
Capex	(1,021)	(1,644)	(1,500)	(1,500)	(1,500)
Placement of restricted bank deposits	(1,098)	(3,241)	-	-	-
Other	(732)	1,323	-	-	-
<b>Net cash from investing activities</b>	<b>(2,851)</b>	<b>(3,561)</b>	<b>(1,500)</b>	<b>(1,500)</b>	<b>(1,500)</b>
Change of Debts	(167)	(775)	-	-	-
Dividend paid	(630)	(791)	(1,195)	(1,468)	(1,844)
Other	2,212	1,414	(2)	(2)	(2)
<b>Net cash from financing activities</b>	<b>1,415</b>	<b>(151)</b>	<b>(1,197)</b>	<b>(1,470)</b>	<b>(1,846)</b>
<b>Net change in cash</b>	<b>1,415</b>	<b>26</b>	<b>1,302</b>	<b>1,878</b>	<b>2,732</b>
Cash at the beginning of the year	2,805	4,359	4,336	5,638	7,515
Exchange difference	257	(225)	-	-	-
Bank deposits with more than 3 months to maturity upon placement	65	177	-	-	-
<b>Cash at the end of the year</b>	<b>4,542</b>	<b>4,336</b>	<b>5,638</b>	<b>7,515</b>	<b>10,247</b>

### Balance sheet

YE 31 Dec (RMB mn)	FY17A	FY18A	FY19E	FY20E	FY21E
<b>Non-current assets</b>	<b>6,858</b>	<b>9,413</b>	<b>10,284</b>	<b>11,154</b>	<b>12,024</b>
Fixed asset	5,778	6,692	7,598	8,504	9,410
Goodwill	497	527	511	495	480
Intangible assets	89	807	787	767	747
Other non-current assets	494	1,387	1,387	1,387	1,387
<b>Current assets</b>	<b>11,824</b>	<b>13,803</b>	<b>15,994</b>	<b>19,285</b>	<b>24,181</b>
Cash	4,542	4,336	5,638	7,515	10,247
Account receivable	2,024	2,546	3,113	3,808	4,767
Inventories	2,516	3,045	3,108	3,465	4,171
Other current assets	2,742	3,877	4,135	4,497	4,996
<b>Current liabilities</b>	<b>4,995</b>	<b>7,247</b>	<b>7,528</b>	<b>8,276</b>	<b>9,753</b>
Borrowings	804	71	71	71	71
Trade and other payables	3,914	4,540	4,795	5,346	6,436
Other current liabilities	277	2,637	2,662	2,859	3,247
<b>Non-current liabilities</b>	<b>326</b>	<b>440</b>	<b>440</b>	<b>440</b>	<b>440</b>
Borrowings	52	-	-	-	-
Other non-current liabilities	274	440	440	440	440
<b>Total net assets</b>	<b>13,361</b>	<b>15,530</b>	<b>18,309</b>	<b>21,723</b>	<b>26,012</b>
<b>Minority interest</b>	<b>74</b>	<b>477</b>	<b>468</b>	<b>457</b>	<b>443</b>
<b>Shareholders' equity</b>	<b>13,288</b>	<b>15,052</b>	<b>17,841</b>	<b>21,266</b>	<b>25,569</b>

### Key ratios

YE 31 Dec	FY17A	FY18A	FY19E	FY20E	FY21E
<b>Sales mix (%)</b>					
Finished drugs	73.6	77.5	81.9	84.8	87.5
Bulk medicines	26.4	22.5	18.1	15.2	12.5
Total	100.0	100.0	100.0	100.0	100.0
<b>Profit &amp; loss ratios (%)</b>					
Gross margin	60.4	66.3	71.5	74.0	75.0
EBITDA margin	27.2	25.1	24.4	23.9	23.6
Pre-tax margin	22.4	21.4	21.7	21.8	21.9
Net margin	17.9	17.4	17.5	17.6	17.7
Effective tax rate	19.8	19.4	19.4	19.5	19.5
<b>Balance sheet ratios</b>					
Current ratio (x)	2.4	1.9	2.1	2.3	2.5
Trade receivables turnover days	92	77	76	76	76
Trade payables turnover days	273	361	366	366	366
Inventory turnover days	173	178	175	175	175
Net debt to total equity ratio (%)	Net cash	Net cash	Net cash	Net cash	Net cash
<b>Returns (%)</b>					
ROE	18.1	20.5	22.3	23.0	24.0
ROA	12.9	13.3	15.2	16.1	17.0
<b>Per share data</b>					
EPS (RMB)	0.39	0.49	0.64	0.78	0.99
DPS (RMB)	0.13	0.15	0.19	0.24	0.30
BVPS (RMB)	2.2	2.5	2.9	3.5	4.2

Source: Company data, CMBIS estimates; Note: Exchange rate of HK\$ against RMB at 0.897

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