

EARNINGS REVIEW

Sinopharm Group (1099.HK)

Neutral

Equity Research

In line with expectations: Operating efficiency drives solid growth**What surprised us**

Sinopharm FY14 results saw revenue of Rmb200.1bn, +20% yoy (organic/M&A: 17.5%/2.5%), and NPAT of Rmb2.88bn, +28% yoy and 1% above our estimates. Its bottom line outpaced top line growth for the first time thanks to increasing hospital sales and operating efficiency. GP margin sequentially improved to 8.42% (from 7.78% in 3Q) as a result of a higher contribution of sales of domestic products. 2H14 adjusted EBIT margin of 3.64% was 40bps lower than 1H14 on higher admin costs, yet 29bps up vs 2H13. Mgmt. said centralized procurement (less than 10% for now) would help improve GP margin. Finance cost ratio of 1.16% was higher than 1.10% in 2013 as a result of higher hospital direct sales that had higher AR days.

What to do with the stock

We are positive on the company's execution and above industry average revenue growth. Management guided for 3-5% higher than the industry revenue growth of c.12-14% in 2015 and continues to believe operating efficiency will drive earnings growth and market share gains. However, it said finance cost might be a big uncertainty due to sustained working capital requirements due to delayed cash payments from hospitals. As such, we maintain our Neutral rating as we think its current valuation fairly prices in the risk/reward with 1% TP downside. We raise our 2015-17 revenue forecasts by 2%/3%/5% and adjust EPS by -2%/-1%/+1% to reflect a slightly higher top line offset by enlarged share capital due to the secondary placement completed in 4Q14. **Valuation:** We keep our 12-m TP (based on 2015E-17E EV/GCI vs CROCI/WACC; 1.22x val ratio) of HK\$29.1, implying 17X/14X 2015E/16E P/E. **Risks:** (-): Higher finance costs and lower margin. (+): Further operational leverage.

Sinopharm FY14 results financial summary

(Rmb mn)	4Q13	4Q14	YoY %	2013A	2014		YoY %		
					Prior E	Actual	Chg%	Old	New
Revenue	44,514	53,556	20.3%	166,866	199,525	200,131	0.3%	20%	20%
NPAT	532	726	36.6%	2,250	2,843	2,875	1.1%	26%	28%
GP margin	8.39%	8.42%	0.03%	8.02%	8.33%	8.16%	(0.17%)	0.31%	0.14%
OP margin	2.92%	3.46%	0.53%	3.48%	3.98%	3.83%	(0.15%)	0.50%	0.34%
NP margin	1.19%	1.36%	0.16%	1.35%	1.44%	1.44%	(0.00%)	0.09%	0.09%

Source: Company data, Gao Hua Securities Research

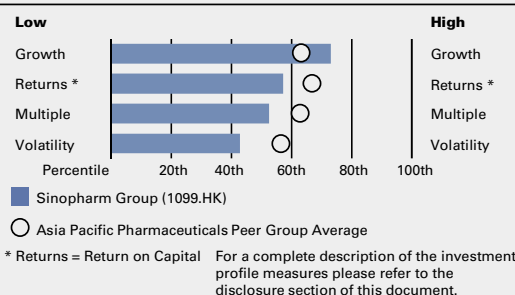
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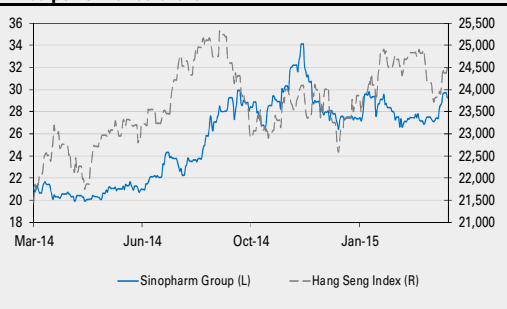
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Investment Profile

Key data	Current
Price (HK\$)	29.25
12 month price target (HK\$)	29.10
Market cap (HK\$ mn / US\$ mn)	80,937.5 / 10,431.1
Foreign ownership (%)	--

	12/14	12/15E	12/16E	12/17E
EPS (Rmb) New	1.04	1.33	1.63	1.99
EPS revision (%)	(6.2)	(2.3)	(0.7)	0.6
EPS growth (%)	18.6	27.6	23.2	21.8
EPS (dil) (Rmb) New	1.04	1.33	1.63	1.99
P/E (X)	18.5	17.6	14.3	11.8
P/B (X)	1.9	2.1	1.9	1.7
EV/EBITDA (X)	8.8	8.7	7.8	7.1
Dividend yield (%)	1.6	1.7	2.1	2.5
ROE (%)	11.7	12.7	14.2	15.4
CROCI (%)	32.6	15.3	15.7	15.7

Price performance chart

Share price performance (%)	3 month	6 month	12 month
Absolute	6.9	2.5	38.6
Rel. to Hang Seng Index	1.9	(0.3)	21.3

Source: Company data, Goldman Sachs Research estimates, FactSet. Price as of 3/23/2015 close.

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Sinopharm Group: Summary Financials

Profit model (Rmb mn)	12/14	12/15E	12/16E	12/17E	Balance sheet (Rmb mn)	12/14	12/15E	12/16E	12/17E
Total revenue	200,131.3	235,893.6	277,001.6	324,048.9	Cash & equivalents	15,232.4	15,201.8	12,111.7	8,765.1
Cost of goods sold	(183,803.0)	(216,720.4)	(254,621.3)	(297,983.6)	Accounts receivable	70,579.6	80,785.5	94,863.6	110,975.7
SG&A	(8,670.3)	(10,030.9)	(11,668.2)	(13,520.3)	Inventory	20,308.6	23,945.6	28,133.3	32,924.5
R&D	--	--	--	--	Other current assets	4,151.9	4,151.9	4,151.9	4,151.9
Other operating profit/(expense)	204.0	240.5	282.4	330.3	Total current assets	110,272.5	124,084.8	139,260.6	156,817.1
EBITDA	8,645.6	10,317.2	12,161.1	14,305.1	Net PP&E	6,348.0	9,092.8	12,202.2	15,731.1
Depreciation & amortization	(783.7)	(934.6)	(1,166.5)	(1,429.8)	Net intangibles	7,102.3	6,846.0	6,589.8	6,333.6
EBIT	7,861.9	9,382.7	10,994.5	12,875.3	Total investments	1,639.9	1,826.5	2,040.7	2,286.7
Interest income	187.9	292.0	291.4	232.2	Other long-term assets	3,293.1	3,293.1	3,293.1	3,293.1
Interest expense	(2,316.6)	(2,537.9)	(2,699.8)	(2,885.1)	Total assets	128,655.7	145,143.2	163,386.4	184,461.5
Income/(loss) from uncons. subs.	162.6	186.6	214.2	245.9	Accounts payable	60,142.7	71,844.3	84,408.7	98,783.6
Others	38.7	39.9	39.9	39.9	Short-term debt	25,232.9	25,232.9	25,232.9	25,232.9
Pretax profits	5,934.6	7,363.3	8,840.3	10,508.3	Other current liabilities	644.3	644.3	644.3	644.3
Income tax	(1,383.0)	(1,719.6)	(2,066.9)	(2,459.0)	Total current liabilities	86,019.8	97,721.4	110,285.8	124,660.7
Minorities	(1,676.8)	(1,975.1)	(2,252.0)	(2,542.4)	Long-term debt	4,222.6	4,222.6	4,222.6	4,222.6
Net income pre-preferred dividends	2,874.8	3,668.6	4,521.4	5,507.0	Other long-term liabilities	2,123.7	2,123.7	2,123.7	2,123.7
Preferred dividends	0.0	0.0	0.0	0.0	Total long-term liabilities	6,346.3	6,346.3	6,346.3	6,346.3
Net income (pre-exceptionals)	2,874.8	3,668.6	4,521.4	5,507.0	Total liabilities	92,366.1	104,067.7	116,632.1	131,007.0
Post-tax exceptionals	0.0	0.0	0.0	0.0	Preferred shares	0.0	0.0	0.0	0.0
Net income	2,874.8	3,668.6	4,521.4	5,507.0	Total common equity	27,381.9	30,192.6	33,619.4	37,777.3
EPS (basic, pre-exception) (Rmb)	1.04	1.33	1.63	1.99	Minority interest	8,907.8	10,882.9	13,134.8	15,677.2
EPS (basic, post-exception) (Rmb)	1.04	1.33	1.63	1.99	Total liabilities & equity	128,655.7	145,143.2	163,386.4	184,461.5
EPS (diluted, post-exception) (Rmb)	1.04	1.33	1.63	1.99	BVPS (Rmb)	9.90	10.91	12.15	13.65
DPS (Rmb)	0.31	0.40	0.49	0.59	Ratios	12/14	12/15E	12/16E	12/17E
Dividend payout ratio (%)	29.8	29.8	29.8	29.8	CROCI (%)	32.6	15.3	15.7	15.7
Free cash flow yield (%)	4.3	1.1	(2.6)	(2.5)	ROE (%)	11.7	12.7	14.2	15.4
Growth & margins (%)	12/14	12/15E	12/16E	12/17E	ROA (%)	2.5	2.7	2.9	3.2
Sales growth	19.9	17.9	17.4	17.0	ROACE (%)	13.7	13.9	14.4	14.6
EBITDA growth	28.5	19.3	17.9	17.6	Inventory days	36.7	37.3	37.3	37.4
EBIT growth	28.8	19.3	17.2	17.1	Receivables days	115.4	117.1	115.7	115.9
Net income growth	27.8	27.6	23.2	21.8	Payable days	108.7	111.1	112.0	112.2
EPS growth	18.6	27.6	23.2	21.8	Net debt/equity (%)	39.2	34.7	37.1	38.7
Gross margin	8.2	8.1	8.1	8.0	Interest cover - EBIT (X)	3.7	4.2	4.6	4.9
EBITDA margin	4.3	4.4	4.4	4.4	Valuation	12/14	12/15E	12/16E	12/17E
EBIT margin	3.9	4.0	4.0	4.0	P/E (analyst) (X)	18.5	17.6	14.3	11.8
Cash flow statement (Rmb mn)	12/14	12/15E	12/16E	12/17E	P/B (X)	1.9	2.1	1.9	1.7
Net income pre-preferred dividends	2,874.8	3,668.6	4,521.4	5,507.0	EV/EBITDA (X)	8.8	8.7	7.8	7.1
D&A add-back	783.7	934.6	1,166.5	1,429.8	EV/GCI (X)	1.5	1.6	1.4	1.3
Minorities interests add-back	1,676.8	1,975.1	2,252.0	2,542.4	Dividend yield (%)	1.6	1.7	2.1	2.5
Net (inc)/dec working capital	(7,448.7)	(2,141.3)	(5,701.4)	(6,528.3)					
Other operating cash flow	7,674.3	(186.6)	(214.2)	(245.9)					
Cash flow from operations	5,560.8	4,250.3	2,024.3	2,704.8					
Capital expenditures	(2,904.2)	(3,423.1)	(4,019.7)	(4,702.4)					
Acquisitions	(616.5)	0.0	0.0	0.0					
Divestitures	0.0	0.0	0.0	0.0					
Others	(836.9)	0.0	0.0	0.0					
Cash flow from investments	(4,357.6)	(3,423.1)	(4,019.7)	(4,702.4)					
Dividends paid (common & pref)	(667.8)	(857.8)	(1,094.6)	(1,349.1)					
Inc/(dec) in debt	3,000.0	0.0	0.0	0.0					
Common stock issuance (repurchase)	0.0	0.0	0.0	0.0					
Other financing cash flows	(2,305.1)	0.0	0.0	0.0					
Cash flow from financing	27.1	(857.8)	(1,094.6)	(1,349.1)					
Total cash flow	1,230.4	(30.6)	(3,090.0)	(3,346.7)					

Note: Last actual year may include reported and estimated data.
Source: Company data, Goldman Sachs Research estimates.

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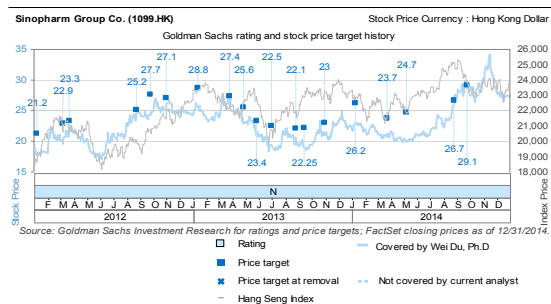
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