

# HAU GIANG PHARMACEUTICAL JSC (DHG)

RECOMMENDATION: BUY

September 22, 2009

## GENERAL INFORMATION

Industry	Pharmaceutical
Listed	HOSE
Ticker	DHG
Charter Capital (VND bn)	200
52-week high	166,000
52-week low	91,580
Avg 10 day trading volume	92,690

On September 4, DHG official announced its profit revision to VND 280bn PBT for the whole year 2009 and also the share bonus scheme. Accordingly, profit will increase 70 percent compare to initial target and 100 percent year over year.

**We like the company growth story** which has consistently proves sustainable over the years. In 2008, the most painful year of pharma industry, DHG still manage to come up on top with more than 15 percent profit yoy increase. This year, when the market turns favorable, again DHG stands out by doubling its 2008 net income.

**With high returns, DHG is absolutely a powerhouse.** For most companies, growth and returns for most of the time are mutually exclusive. But for the past 3 years, average ROE of DHG is more than 20 percent. This year, we expect ROE to soar up to 30 percent.

## VALUATION MEASURES

Price (Sep. 22, 2009)	149,000
Market Cap. (VND bn)	2,980
P/E trailing (x)	18.7
P/B trailing (x)	3.8
P/E forward 2009 (x)	11.1
P/B forward 2009 (x)	3.2
ROE trailing (%)	20.4
ROA trailing (%)	12.7
EV/EBITDA 2008 (x)	15.6

## 1H 2009 PERFORMANCE REVIEW

**Robust sale growth, improved gross margin, and better cost management are the key drivers behind impressive 1H earning performance**

DHG's 1H financial statements demonstrated better than expected performance when earnings before tax reached VND101 bn, increasing 36% half over half and fulfilling 67% whole year target. This achievement was supported by two key engines – robust revenue growth and improvement in profit margin. However, both of these two drivers could not be seen simply by analyzing financial statements.

The change in the methodology of recording selling expense, in which sale discounts were now deducted right from the topline instead of being recorded as a separate item, has deflated the actual revenue that should be recorded and subsequently reduced the amount of selling expenses. In fact, rather than only growing 3% as shown in 1H2009 report, sales maintained its robust growth of roughly 15%.

In the mean time, under the old method of recording revenue, gross margin should have increased from 52.49% of 1H 2008 to roughly 56.65% in 1H 2009, and selling expenses should have decreased from 35.6% in 1H 2008 to 34.8% in 1H 2009. Enhancement in gross margin could be attributed to the drop in material price in Q1, the increase in proportional sales of higher margin products. Meanwhile, the reduction of selling expenses clearly demonstrates better cost management and changes in sale incentive policy which resulted from the company's effort to control cost in the tough time of 2008.

In light of stronger than expected 1H performance, DHG revised its full-year PBT targets from VND150 bn to VND280 bn in which the reverse in provisions for account receivable and losses in long-term investment was VND57 bn.

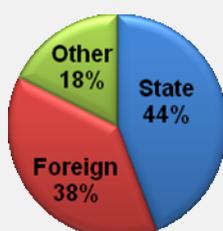
**Provision expenses will be reversed in 2<sup>nd</sup> Quarter FS, lifting profit before tax of 1<sup>st</sup> Half to VND158 bn**

The write-off of VND57 bn provisions will be recorded in Q2 2009 audited report. These include VND 45 bn in account receivable provision and VND 12 bn in investment provision. Previously the company made provisions for its receivable since its customers, mostly hospitals, were late in making payments. Nevertheless, credit quality of these receivables remains good and therefore DHG has decided to write off those provisions lately. As a result, administration expense in which account receivable provision is recorded, and financial expense where investment provision is booked will reduce in audited FS of Q2 as compared to unaudited report. These revised cost accounts will bring revised earnings before tax in 1H to around VND158bn.

## FINANCIAL PERFORMANCE 1H 2009

Revenue (VND bn)	791.4
Profit after tax (VND bn)	92.4
Gross margin (%)	52.5
Net margin (%)	11.7
Debt/Equity (%)	13.0

## OWNERSHIP STRUCTURE



Source:DHG

## OPERATING RESULTS



Source: DHG

## 2H 2009 LOOKING FORWARD: Momentum is expected high on both top line and bottom line

By lifting year-end target for profit before tax up from VND 150bn to VND 280 bn, in which profit before reversion of provision is VND 223bn, DHG implies that their core business will perform much better in the second half than in the first half. In fact, empirical analysis demonstrated that except for 2008 when the industry encountered many difficulties, 2H revenue is usually 20 - 30 percent higher than that of 1H. Consequently, we expect the company's sale and subsequently earning in Q3 and Q4 to surpass Q2 by approximately 15 percent and 40 percent respectively. In other word, we expect 2H earning to reach VND 142 bn, finishing the year with a total of VND 300 bn profit before tax.

## FUTURE PROJECT

The construction of the VND 200bn factory to expand capacity and manufacturing new products will start in early 2010. Currently the project has received permission from the Minister of Health and is completing its final stage of preparation. Located in a 22ha factory in Tra Noc industrial zone, the factory can produce 3 billion units annually (an increase of 75% in capacity from the current factory). The factory is expected to operate in Q2 2011 with tax exemptions that DHG can enjoy.

## SENTIMENT ANALYSIS AND RECOMMENDATIONS

At the current price, DHG is trading at 11x its 2009 earning, which is equal to industry average, while previously DHG was always traded at a premium compared to other pharmaceutical companies as a market leader. We think the reason lies in investors' sentiment. First, although DHG is cheaper from a relative valuation, its absolute value is more than twice that of its peers, making it a bit "heavy" to move on. Second, the share splitting event is still weeks ahead, which make it less attractive. As we observe, market sentiment is high when the news is about to come, rallies when news come out, but drops in the gap between the day of news announcement and the ex-right day.

From a more fundamental point of view, we value the company at 180,000 per share price, equivalent to PE 2009 13x. Since the stock is currently traded at good discount, we see a good opportunity for both long and short term investors to start accumulating. All in all, we do not think DHG merely a defensive stock, which generates stable cash flow. We see it as one of the growing stock in the current market.

## SHARE PERFORMANCE



Source: Reuters

## PEER COMPARISON

DESCRIPTIONS	DHG	DMC	IMP	DCL	OPC	TRA
Chartered capital (VND bn)	200.0	179.0	116.6	97.2	81.9	80.0
Share Price (VND) Sep.1, 2009	149,000	58,500	72,500	68,000	51,000	78,000
Market capital (VND bn)	2,980.0	1,047.2	845.3	660.9	417.7	624.0
Revenue 1H 2009	791.4	490.5	311.0	250.7	137.9	345.5
Increase yoy (%)	3.7	9.9	11.5	(2.6)	14.7	(10.8)
Profit after tax 1H 2009	92.4	42.4	33.9	28.3	21.8	25.8
Increase yoy (%)	35.7	37.7	6.5	14.1	33.4	17.0
Total Asset Q2/2009	1,262.8	675.9	632.8	602.4	291.0	404.8
Total Equity Q2/2009	783.6	486.5	527.3	284.5	258.9	277.9
Debt/Equity Q2/2009 (%)	13.0	17.1	5.2	83.3	4.0	17.3
P/E trailing (x)	18.7	14.0	13.5	12.1	11.6	12.5
P/B trailing (x)	3.8	2.3	1.6	2.3	1.6	2.2
ROA trailing (%)	12.7	11.7	10.2	9.1	12.4	12.3
ROE trailing (%)	20.4	16.2	12.2	19.2	14.0	17.9
Profit after tax 2009 (VCSC)	268.8	89.5	71.3	62.4	54.1	55.2
P/E 2009 (VCSC)	11.1	11.7	11.9	10.6	7.7	11.3

## SUMMARY OF HISTORICAL AND PROJECTED FINANCIAL STATEMENTS

INCOME STATEMENT (VND Bn)	2007A	2008A	1H 2009	1H 2009 R	2009F
Revenue	1,269	1,485	791.0	791.4	1,634.0
COGS	600.8	694.4	375.6	375.6	778.9
Gross Profit	668.5	791	415.8	415.8	855.1
Selling Expenses	469.3	521.5	226.4	226.4	467.3
Administrative Expenses	59.8	103.9	69.7	24.7	78.4
Operating Profit	139.4	165.6	119.8	164.8	309.3
Profit before tax	128.3	145.0	101.1	158.1	300.0
Profit after tax	115.1	130.0	93.5	145.3	270.0
Minority Interest	-	1.1	1.0	1.0	1.2
<b>PAT to the Company's shareholders</b>	<b>115.1</b>	<b>128.9</b>	<b>92.4</b>	<b>144.2</b>	<b>268.8</b>
BALANCE SHEET (VND Bn)	2007A	2008A	1H 2009		2009F
Cash	135.0	211.7	424.8		326.8
Short term investment	52.0	2.3	16.1		190.2
Short term receivable	257.4	255.1	229.1		288.4
Inventory	230.3	308.2	300.6		303.0
Other current asset	4.2	6.2	10.2		12.4
Fixed asset	216.6	224.0	238.8		227.9
Construction in process	12.2	2.0	4.4		9.4
Long term investment	35.7	66.8	30.3		45.6
Other long term assets	1.4	5.5	8.4		5.4
<b>TOTAL ASSET</b>	<b>944.7</b>	<b>1,081.8</b>	<b>1,262.8</b>		<b>1,409.2</b>
Short term loans	43.4	8.5	102.0		56.1
Payables	259.6	359.0	358.7		402.2
Long term debt	0.8	15.2	14.5		15.2
Chartered capital	200.0	200.0	200.0		200.0
Capital Surplus	378.8	378.8	378.8		378.8
Treasury Stock	-	(0.3)	(0.3)		(0.3)
Retain earnings	1.2	62.2	95.9		235.0
Other funds	58.4	55.2	109.3		122.2
Minority Interest	2.5	3.2	4.0		4.1
<b>TOTAL CAPITAL</b>	<b>944.7</b>	<b>1,081.8</b>	<b>1,262.8</b>		<b>1,409.2</b>
CASH FLOW STATEMENT	2007A	2008A	1H 2009		
CF from Operating Activities	51.3	177.7	146.1		
CF from Investing Activities	(191.6)	(13.2)	(26.6)		
CF from Financing Activities	235.3	(82.8)	93.5		
<b>Net cash flow</b>	<b>94.9</b>	<b>81.8</b>	<b>213.1</b>		
Beginning Cash Balance	35.0	130.0	211.7		
<b>Ending Cash Balance</b>	<b>130.0</b>	<b>211.7</b>	<b>424.8</b>		
FINANCIAL RATIOS	2007A	2008A	1H 2009	1H 2009 R	2009F
Revenue growth (%)	46.2	17.0	3.7	3.7	10.0
Gross profit margin (%)	52.7	53.3	52.5	52.5	52.3
Operating profit/sales (%)	11.0	11.1	15.1	20.8	18.9
ROA trailing (%)	12.2	12.0	12.8	16.1	19.2
ROE trailing (%)	18.0	18.7	20.6	25.3	28.9
ROIC trailing (%)	16.9	18.5	18.3	23.9	27.2
EPS trailing (VND)	5,757	6,500	8,086	10,578	13,500
EPS growth (%)	(47.1)	12.9	n/a	n/a	107.7

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