Hau Giang Pharmaceutical (HOSE: DHG)

Deserving Of Its Valuation Premium

February 25th, 2009

An industry leading franchise..

A powerful consumer-driven franchise built around a number of unique advantages within the industry supply chain, DHG has grown to be the largest and most dominant publicly-listed pharmaceutical company in Vietnam - ranked by sales, total output, distribution capability and market capitalization. DHG remains one of the TVS “high conviction buys”.

With a solid earnings outlook and high margins…

Core earnings have been growing at a healthy 29% from 2005-2008 (although 2007 after tax earnings were signfincantly down due to a large share issuance and a new tax rate.) Back on a positive track in 2008, EPS was up 11% to VND6,793, and we are projecting 11% growth in 2009 to VND7,548. Underpinning this growth are hefty 51 percent gross margins, which have remained stable in the past four years. With a new plant coming on line in 2011, and a new emphasis on distributing products from foreign firms, the firm is well positioned for future growth.

The current valuation premium is justified and consistent with other regional markets …

Although the current PE ratio of 13.6 times 2009 earnings represents a premium to the current market PE multiple (about 10x 2009 earnings) we believe that this is justified. Sales are more defensive than most other sectors and we maintain that DHG offers relatively more certainty in earnings during the current downcycle. It is also worth noting that this valuation premium is entirely consistent with comparable companies in other regional markets. Typically these are trading at between a 40% to 100% premium to their broader indices.

With earnings volatility expected to be less than the market due to product portfolio…

In the long run, we expect macroeconomic strength to boost the earnings and share price of DHG due to the fact that consumer purchasing of pharmaceuticals in Vietnam is more discretionary than in developed economies that have better public or private health insurance systems, or higher disposable income. We view the company therefore as a hybrid consumer cyclical/staple opportunity, with significant upside in a strengthening economy, and recommend aggressively building positions in the event of either price weakness or signs of expansion in sales growth.

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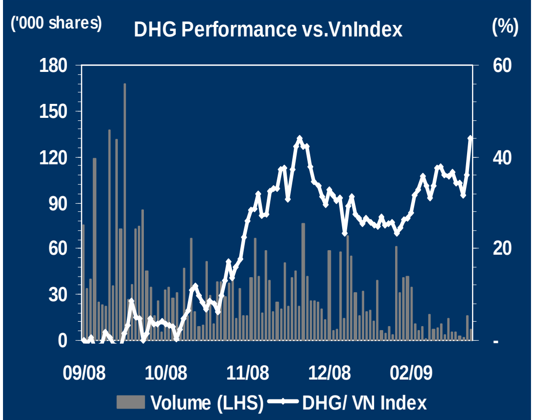


Symbol/Exchange	DHG/HOSE
Market Capitalization	USD117.5m
Average daily value	USD72k
2009 EPS	7,548
2009 PE	13.6x
2009 PB	2.5x
Dividend yield	2.4%
3-yrs CAGR EPS ('06-'08)	7%
3-yrs Avg ROE ('06-'08)	35%
Most recent price (as of 24/02/09)	VND103k/USD5.9
52W High/Low	VND183k/94.5k
Foreign ownership	44%

Analyst: Nguyen Trong Khiem

This report is written based on carefully selected information and should only be used for reference. TVS is not responsible for any investors' buy/sell decision. For further information, please mail TVS at info@tvs.vn.

FINANCIAL HIGHLIGHTS

Income Statement (VND bn)	FY06	FY07	FY08	FY09E	FY10E	FY11E
Sale revenue	868	1,269	1,513	1,689	1,900	2,318
Cost of good solds	403	601	718	821	927	1,131
Sell & Administration expenses	368	529	629	689	769	939
EBITDA	111	170	187	219	253	313
Depreciation	13	24	29	26	37	51
EBIT	98	146	158	193	216	262
Interest expense	11	17	5	25	28	35
EBT	87	128	153	168	188	227
Taxes	0	13	16	17	19	23
NPAT	87	115	137	151	169	204
Balance Sheet (VND bn)	**FY06**	**FY07**	**FY08**	**FY09E**	**FY10E**	**FY11E**
Cash	35	130	212	220	225	197
ST Investment	0	52	2	3	3	4
Account Receivable	166	257	310	347	390	571
Inventory	121	230	308	292	317	434
Other current assets	7	4	6	7	9	10
Tangible fixed assets	81	111	107	81	201	185
Intangible fixed assets	62	105	117	118	118	118
Total Assets	483	942	1,133	1,177	1,346	1,599
Short-term debts and loans	168	43	8	51	57	70
Equity	170	652	753	854	973	1,127
Free Cash Flows (VND bn)	**FY06**	**FY07**	**FY08**	**FY09E**	**FY10E**	**FY11E**
NPAT for Corporate	87	115	136	151	169	204
Depreciation	13	24	29	26	37	51
Interest expense after tax	11	16	5	23	26	31
Changes in WC	(76)	(74)	(26)	(115)	(32)	(215)
CFO	36	81	143	85	200	72
Net investment	(63)	(53)	(21)	0	(158)	(35)
FCFF	(27)	28	122	85	42	37
Ratios	**FY06**	**FY07**	**FY08**	**FY09E**	**FY10E**	**FY11E**
SR Growth	57%	46%	19%	12%	13%	22%
EBITDA Growth	54%	52%	10%	17%	16%	23%
EBIT Growth	61%	48%	9%	22%	12%	21%
EBT Growth	57%	47%	19%	10%	12%	21%
EBITDA Margin	13%	13%	12%	13%	13%	13%
Net debt/Equity	90%	-13%	-25%	-19%	-16%	-10%
ROE	58%	28%	19%	19%	18%	19%
ROA	18%	12%	12%	13%	13%	13%
EPS (VND)	10,882	6,130	6,793	7,548	8,438	10,209
BV/Share (VND)	21,305	34,585	37,665	42,713	48,651	56,361
Cash/share (VND)	4,375	6,898	10,587	10,996	11,263	9,867

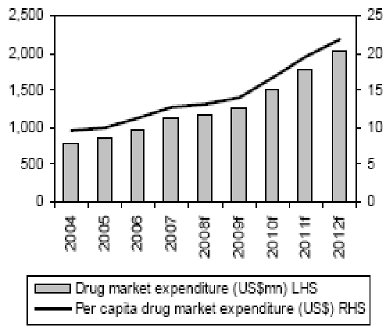
COMPANY SUMMARY

DHG pharmaceutical manufactures, trades, and markets pharmaceutical products and trades in drug raw materials and equipment. DHG has a strong competitive position in an otherwise highly- fragmented, heavily-regulated, strongly-protected Vietnamese drug industry. DHG accounts for nearly 7% of the 2008 total drug market share (both imported and domestic producers) and 13% of the domestic manufactured medicines. The company's degree of vertical integration is unmatched in the industry, given its both cost protection on the supply side and revenue and profit opportunities on the demand side. Because of the scale of its production, its leadership in important therapeutic categories, its access to raw materials, and its proprietary distribution system, DHG is well positioned to sustain its leadership in the industry.

INDUSTRY OVERVIEW BACKGROUND

Drug Market Trends

(2004-2012)



f = forecast. Source: Drug Administration of Vietnam, Vietnam Ministry of Health, General Statistics Office of Vietnam, Vietnam Pharmaceutical Companies Association, BMI

Small Industry. The pharmaceutical industry in Vietnam generates about $1.3 billion in sales per year (2008), comprising less than one half of one percent of GDP, which is quite low compared to developed and other developing countries. The health sector overall in Vietnam is very small, both as a percentage of GDP, and in terms of total market capitalization. Per capita pharmaceutical expenditure is low at about USD13, however the opportunity stems from expected growth.

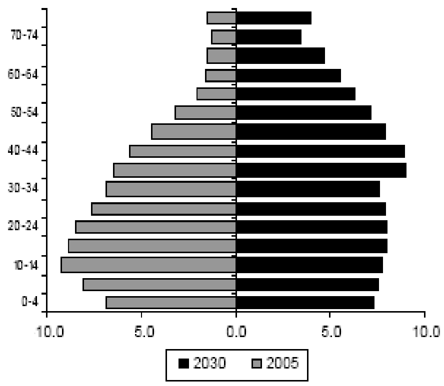
Unit and Price Trends. The industry itself grew 18% in 2008 (15% annually on average), according to the Ministry of Health. Of that, unit growth is estimated to be about 9%; the main drivers of which are the availability of new drugs coming to market, rising consumer incomes, increased education about the benefits of medication, and lower prices from higher competition. Price inflation in the drug industry has been rampant for many years, therefore in 2007, the government introduced price controls at both state and private companies. After some success in lowering prices, in June 2008, the government lifted the restrictions, and drug price increases stabilized at 9% for 2008.

Reduction of Trade and Tariff Barriers. The Vietnamese pharma industry has been highly protected for many years. Local producers, accounting for only 51% of domestic supply in total, have enjoyed protective tariffs on imports, restrictions on the ability of foreign-owned companies to distribute products, lax enforcement of intellectual property (IP) rights concerning patented drugs, and the abilty to sell prescription medication over the counter. However, the industry will experience dramatic upheaval in the coming years due to increasing competition from foreign companies with newly granted market access from the WTO agreement. As a part of the WTO deal, foreign firms will see their import tariffs decline from on average about 10% to circa 2.5%, which will aggravate price competition.

Drug Expenditure Forecast 2006 - 2012

	2006	2007	2008e	2009e	2010e	2011e	2012e
Drug market expenditure (US$ mm)	956	1,114	1,220	1,336	1,463	1,602	1,754
Drug market expenditure (VND bn)	15,313	17,879	19,519	21,181	22,845	24,640	26,577
Per-capital drug market expenditure (US$)	11.20	12.90	13.90	15.00	16.20	17.50	18.90
Drug expenditure % GDP	1.58	1.59	1.50	1.42	1.36	1.30	1.23

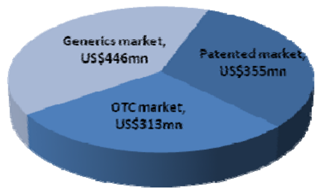
Population By Age, 2005 And 2030 (mn, total)



Top Ten Drug Manufacturing Companies in Vietnam 2007

Rank	Company Name	Revenue (bil. VND)
1	Hau Giang Pharmaceutical	1,269
2	Mekophar	540
3	Sanofi-Synthelabo	466
4	Imexpharm	430
5	Domesco	420
6	Binh Dinh Pharmaceutical	400
7	Cuu Long Pharmaceutical	350
8	Ha Tay Pharmaceutical	320
9	Traphaco	305
10	Thanh Hoa Pharmaceutical	207
		4,708

Vietnam's Pharmaceutical Market 2007



Source: UN Ministry of Health, PAD, GSO of VN, BMI

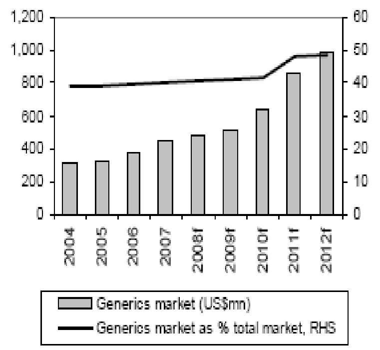
Increased imports and local production from foreign branch offices. Until recently, foreign companies have not been able to import drugs directly, being forced to rely instead on local drug import/export agents who carry out local distribution. (Or in some cases, on their own domestic production.) Under the WTO, however, foreign companies will be able to both import products through a wholly-owned local subsidiary ("branch") and also engage in local distribution, though on a limited basis. However, foreign firms are expected to target the high end of the pharmaceutical market, categories where drugs are currently not available, and treat serious diseases. As a result, the new companies are expected to increase the overall share of the market, rather than taking share from local competitors.

Locally-controlled wholesale distribution. There are estimated to be over 700 drug distributors in Vietnam, 50 of which are controlled by the government, and the rest split between distribution systems of pharmaceutical companies (such as DHG) and independent (third party) distributors. In recent years, the government has had to impose price controls to check the business activities of many drug distributors, some of whom are known for arbitrary price hikes, kickbacks and other forms of price manipulation. The degree to which companies can establish their own distribution systems improves their price position and marketing power in the long run as these companies' products aren't marked up by middle men.

Retail distribution system. The main type of retail sale to consumers is through pharmacies, and represents about 70% of industry sales. There are approximately 57,000 pharmacies in Vietnam, although there is a shortage of pharmacists. Pharmaceutical companies ship products from their own warehouses and distribution centers directly to the retailer, or rely on an independent distributor to reach more remote retailers. In the second channel, known as the treatment channel (consisting of 30% of industry sales), drugs are sold to consumers from hospitals, doctor's offices, and medical centers. This channel is smaller because most Vietnamese consumers have a habit for self-treatment using drugs from pharmacies before going to the hospital.

Generics Expenditure (US$mn) And As % Of Total Market

(2004-2012)



f = forecast. Source: Drug Administration of Vietnam, Vietnam Ministry of Health, General Statistics Office of Vietnam, Vietnam Pharmaceutical Companies Association, BMI

Product Segments: The Prescription Market. The prescription market stands at around USD947m in 2008 sales, and is projected to grow at about 12% per year until 2011. Of that, 56% consists of generic drugs (USD496m), and the remainder of patented drugs (USD385m), although in practice most "patented" drugs are frequently copied – and often counterfeited. In Vietnam, by far the largest category of prescription drug is antibiotics (32%) and DHG is the market share leader in this segment with 13%. The high number of antiobiotics is a function of the popularity among doctors of the medication in treating a wide range of ailments. (It has also resulted in worrying levels of antibiotic resistance. For example, nearly 70% of bacteria carried by people living in urban parts of Vietnam are resistant to penicillin.)

Product Segments: OTC Market. The OTC market, the second of the two main product segments, stands at USD363m in sales, or about 28% of the total market. The OTC market is growing at about 9% annually, but is projected to be a smaller percentage of the total market in 2012 than it is today because of the rapid growth of the prescription segment. The largest segments are analgesics (30.7%), cough and cold (15.2%) and digestives (23.7%).

DHG's BUSINESS TODAY

Pharmaceutical Production

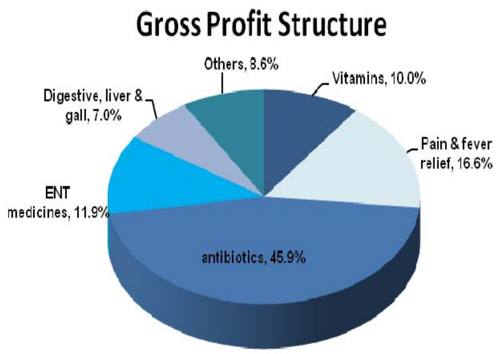
In the last five years, DHG revenue has been growing at a pace significantly higher than the industry. For example, in 2008, DHG sales were up 19.2% compared to the industry growth of 18%. In years prior to that, the differential was much higher. Average growth rate from 2004 to 2007 was 42% compared to just 12% of the total market. In the coming year of 2009, we expect DHG's sales to be more in line with projected industry growth of 10-12% as top line growth has slowed down throughout the 2008 year.

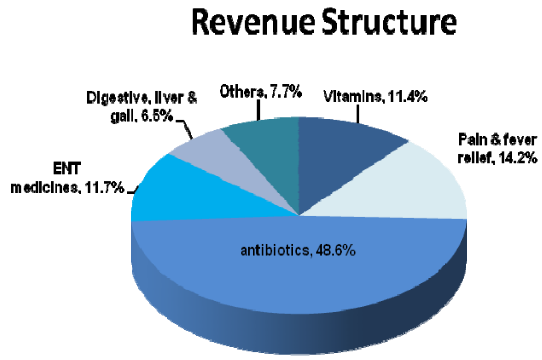
DHG competes in three main lines of business: prescription medications (50% of sales), OTC medications (41% of sales), raw materials and commercial trading (9% of sales).

Prescription Sales. DHG prescription sales are estimated to be growing at 13% per annum. The main product segment within prescription sales is antibiotics, which are key drivers of the company's revenue and earnings, contributing to 48.6% and 45.9% respectively. (They represent about 85% of prescription sales.) Some popular names for this type of products are Aticef, Calbact, and Hacefa. The growth rate for the antibiotic segment is slowing down in 2008. Growth estimation for 2009 of this group is only 8% compared to the previous average of 31% (from 2006 to 2008). However, we expect this to be offset by high growth rates in other prescription categories such as central nervous system (20%), cardio-vascular (35%), muscular skeletal (40%) and sensory organs (60%) for 2009.

***OTC sales*. DHG's OTC growth is estimated at 12% per annum from 2009 onward. The main category is pain and fever relief, which contributes about 14.2% of revenue and 16.6% of net income from the company's manufactured products (not including trading). The growth rate for this group should be a modest 6% in 2009. DHG's most famous brand name is Hapacol (known as paracetamol in Europe and acetaminophen in the U.S.) which generated 13% of total revenue in 2007. People perceive Hapacol to be a high quality product at a good price as similar imported products sell at a considerable premium.

Also in OTC, vitamins contribute to 11% of revenue and 10% of gross profits (for manufactured goods). Though this segment has been growing rapidly at about 40% a year, we expect this rate to slow to about 20% in the coming year. Rising income and better understanding of vitamins' importance promise high growth rate will persist in the future.





The last major OTC segment for DHG is ear, nose and throat medicines (ENT or sometimes referred to as cough and cold medicines). Unlike most of DHG's products, the company does not rely entirely on imported materials for this group. Instead, DHG uses local sources of raw materials (herbal) as they are available at cheaper prices than imported sources. This group contributes 11.7% of revenue and 11.9% of gross profit (for manufactured goods). In 2007, this group generated 54% more revenue than the previous year. We expect the high growth rate to continue due to the local preference of herbal products over occidental medicines. Main products are Eugica, Pamin, Clanoz.

Other important product categories include eyes, muscle, bone & joint medicines, nerve, digestive systems, diabetes, and heart disease. Together they contribute 7.7% of revenue and 8.6% of net income. These high end categories will be the target of many foreign companies entering the market.

International sales. DHG exports 77 products to seven international markets (Russia, Ukraine, Mongolia, Moldova, Romania, Cambodia and Myanmar). However, revenue from exporting products is still modest at 1.1% of total 2007 revenue. DHG will try to push export growth for generic products to 15% annually as well as expanding to other new markets.

Important Therapeutic Categories in Vietnam - Size, Growth and DHG Sales

	Industry Categories USD (mln)	DHG 2007 USD	DHG 2008 USD	DHG Growth 2008 %	Projected 2009-2010 Growth	Projected 2009 value USD	Projected 2010 value USD
Prescription - Patended & Generic (12% growth)							
Antibiotics	**284**	34,470,320	36,524,333	6.0%	8%	39,446,280	42,601,982
Alimentary	**213**	3,107,552	3,346,957	7.7%	6%	3,547,775	3,760,641
Central Nervous System	**100**	303,486	385,050	26.9%	20%	462,059	554,471
Respiratory	**88**	n.a	n.a.	n.a	n.a		
Cardiovascular	**85**	988,093	1,385,770	40.2%	35%	1,870,789	2,525,566
Muscular-skeletal	**43**	1,475,081	2,083,640	41.3%	40%	2,917,096	4,083,934
Oncology	**43**	n.a	n.a.	n.a	n.a		
Sensory organs	**13**	529,335	2,395,250	352.5%	60%	3,832,400	6,131,840
Subtotal	**869**	40,873,866	46,121,000	11.8%		52,076,399	59,658,434
Over the Counter (9% growth)							
Analgesics	**97**	10,657,286	10,999,083	3.2%	6%	11,659,028	12,358,570
Cough and Cold	**48**	8,561,118	9,026,132	5.4%	10%	9,928,745	10,921,619
Digestives	**75**	1,091,842	1,175,958	7.7%	6%	1,246,516	1,321,306
Skin Treatments	**48**	839,879	674,390	-19.7%	0%	674,390	674,390
Vitamins	**48**	7,537,736	10,348,094	37.3%	4%	10,762,017	11,192,498
Diabetes	**n.a**	141,156	216,394	53.3%	30%	281,312	365,705
Cosmetic products	**n.a**	882,226	850714	-3.6%	2%	867,729	885,083
Subtotal	**316**	**29,711,242**	**33,290,765**	12%		**35,419,737**	**37,719,173**
Total Sales	**1185**	**70,585,108**	**79,411,765**			**87,496,136**	**97,377,607**

Sources: BMI Research, TVS Research and Analysis, DHG Financial Statements. All figures are estimates.

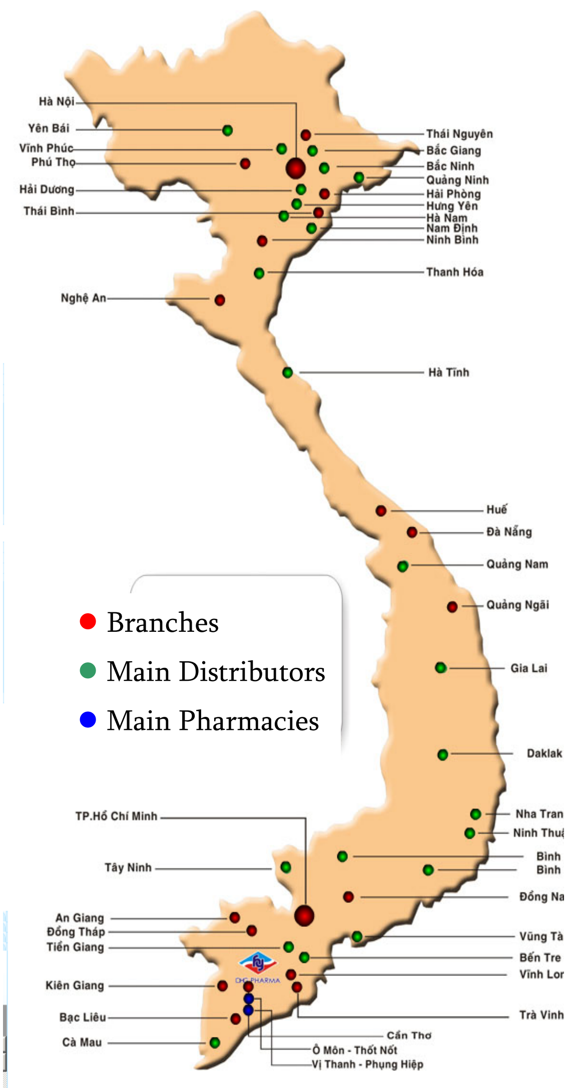
DHG Trading: Raw Material Sales and Other Pharmaceuticals

In recent years, DHG has been striving to decrease its dependence on imported raw materials. The company is targeting a lower ratio of 70% by 2012 (from the current level of 85%), and is creating a new production subsidiary (DHG Nature) to produce raw materials for oriental medicines. It also sells raw materials from its own inventory when market conditions are right.

DHG's position compares favorably with the industry as a whole which on average imports 90% of active pharmaceutical ingredients (APIs) used in production (mostly antibiotics and vitamins ingredients), creating significant exposure to both increases in raw material costs and to currency fluctuations. In the past two years, drug companies in Vietnam have been hit hard by rising raw material costs driving down margins significantly. DHG's position as a large bulk buyer of API's is one of its unique advantages in the industry.

Another advantage DHG enjoys in the area of purchasing is that it uses its large GSP warehouses to engage in more active inventory control as a means to reduce risk from import price fluctuations. It also creates another source of revenue as DHG will sell some its inventory to other pharmaceutical companies when prices increase.

DHG'S Distribution Network



DHG Distribution Sales

DHG's products go through two main channels: commercial and treatment. DHG's commercial network is the largest in the country, reaching to more than 20,000 customers in all 64 provinces (including supermarkets, doctor's offices, wholesales distributors and pharmacies). Seventy percent of DHG's sales are through this channel. The company has 17 branches and 18 distribution centers. The company's large share issuance in 2007 was made to develop the distribution network and invest in the fixed assets needed to be an industry leader.

In the treatment channel, DHG's network reaches 98% of the total 978 hospitals in Vietnam. To win this business, DHG and its competitors must engage in a bidding competition on contracts. DHG has successfully introduced many of its own developed prescription drugs such as Apitim (high blood-pressure and chest pain) and Lipvar (high cholesterol) through this channel.

DHG has turned five of its distribution branches into subsidiaries to compete for contracts with importers and foreign companies producing locally. Many international counterparts have already asked DHG to become their distributor but so far DHG has not accepted any bids.

Also, DHG has finished building a new central warehouse at Tan Tao Industrial Zone (total capex of more than VND25bn). The new warehouse starts operating in the beginning of 2009, improving transportation in the South. Furthermore, Tan Tao warehouse can be utilized for trading other companies' products if DHG decides to engage in partnerships with foreign counterparts. We expect a higher percentage of trading products from 2009 as foreign companies have to look for local distributors (regulations only allow foreign companies to set up one trading point, therefore they must rely on local distributors to market drugs).

Operations

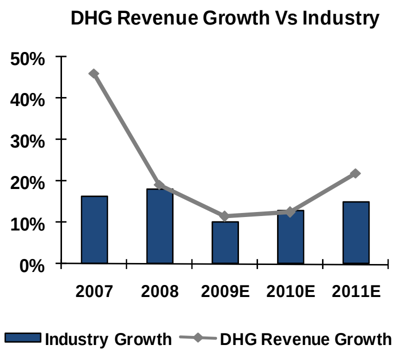
DHG Research and Development. Based on most recent data DHG has an R and D fund of about USD1.2m which is insignificant even by local industry standards (Publicly-listed pharmaceutical companies are not currently reporting R and D expense as a separate line item, even though they do report the total size of their "R and D fund" as a balance sheet item). The company introduced 144 new products in 2007, 38 in 2008, most of which were part of the oriental medicine business.

Production. DHG is currently the largest domestic producer in terms of capacity (total capacity of 3 billion units/year). The company's facilities include four processing factories, one substance extracting facility, and one packaging plant. Operating efficiency remained at more than 90% all year. DHG will begin construction on a new factory in 2009 at Tra Noc Industrial Zone. Capex for this project is estimated at VND158bn (including VND20bn for machinery) bringing DHG's total capacity up to 5 billion units/year (from the current level of 3 billion units/year). The factory will be completed by the end of 2010 and is expected to boost revenue starting in 2011.

The Vietnamese government will begin to enforce newly announced quality standards (for production, storage, laboratory and pharmacy practices) that could put half of the local companies out of business and exacerbate rapid industry consolidation. The new regulations require pharmaceutical producers to have GMP (Good Manufacturing Practices) in order to continue operating. Out of the nearly 180 local drug manufacturers, there are only 86 that satisfy GMP standard. By 2010, firms will also need to meet standards for GSP (Good Storage Practice) and GLP (Good Laboratory Practice). DHG currently meets all of these specifications.

Management. For 20 years, general director and chairwoman Pham Thi Viet Nga has led DHG as it has grown from a small and unprofitable firm to a successful, well known brand name in the pharmaceutical industry. The management's dedication and ability have led DHG to the first position in generic products (in term of value) and many awards such as the Vietnamese top quality products (for 12 years consecutively), top 100 strong brand name etc.

FINANCIAL ANALYSIS



2008 Results: The company's annual results for 2008 were strong with operating profit growing at 17.7% YoY even though this was down from on average 50% earnings growth in the previous three years. However, the economic slowdown has taken its toll as *fourth quarter 2008* results were disappointing with the top line growing at a weak 3%, gross profit 6% *less* than the previous year, and after tax profit down 8% over the previous year. From our vantage point, it appears these results are being driven by an industry wide slowdown rather than events related specifically to DHG's core business as top line growth at the next two largest publicly traded pharmaceutical companies (Imexpharm and Domesco) was also weak.

Revenue growth

Due to the difficulty of the economy in general, limited capacity and higher competition from foreign companies, we estimate revenue growth for 2009 will slow to nearly 12%. This is very modest compared to the historic growth rate of 36.3% annually from 2004 to 2008. However in the long run, we expect revenue growth to improve to 16.4% per annum (from 2010 onwards) when DHG introduces its new factory and economic conditions improve. Increasing capacity from the new factory in Tra Noc Industrial zone is the primary reason for high revenue growth in 2012 and 2013. The removal of price restrictions, an expanding distribution network, trading revenue from other companies' products, and new oriental medicines will be other factors contributing to revenue growth.

Income Statement (VND bn)	FY07	FY08	FY09E	FY10E	FY11E
Sale revenue	1,269	1,513	1,689	1,900	2,318
Cost of good solds	601	718	821	927	1,131
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EBITDA	170	187	219	253	313
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Interest expense	17	5	25	28	35
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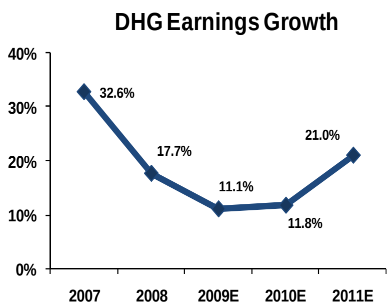
Gross, net margin and earnings growth



In general, DHG is a highly profitable company with 51% gross margin, a function of the economics of the generic drug business: low costs of goods sold and attractive pricing relative to costs. Margins have held firm through the slowdown in sales. In 2007, the company began paying a new tax rate of 10% (instead of 0% previously), which also cut into growth in after tax earnings. Also in 2007, the company floated almost 10,000,000 new shares, more than doubling shares outstanding. The combination of the two meant 2007 EPS was down about 44% for the year. However even though DHG issued more than one million shares additionally in 2008, EPS for this year is up by 11% compared to 2007. Future EPS is estimated to grow at 16% on average from 2009 to 2013, with the tax rate and shares outstanding holding constant.

BALANCE SHEET ANALYSIS

Balance Sheet (VND bn)	FY07	FY08	FY09E	FY10E	FY11E
Cash	130	212	220	225	197
ST Investment	52	2	3	3	4
Account Receivable	257	310	347	390	571
Inventory	230	308	292	317	434
Other current assets	4	6	7	9	10
Tangible fixed assets	111	107	81	201	185
Intangible fixed assets	105	117	118	118	118
Total Assets	942	1,133	1,177	1,346	1,599
Short-term debts and loans	43	8	51	57	70
Equity	652	753	854	973	1,127

Strong Balance Sheet

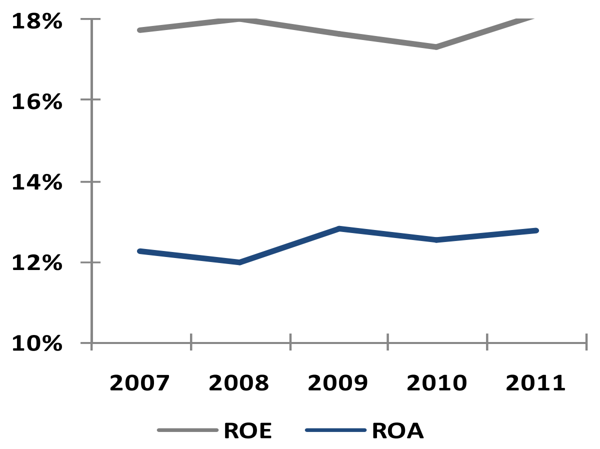
Borrowing is minimal at DHG, with the debt projected to remain at about 40% of equity. DHG has an excellent cash position as well as significant receivables outstanding, making their working capital overall quite strong with the ratio of current assets to current liabilities at 2.7x by the end of 2008. Healthy constant cash flow and extremely low short-term liabilities should keep the ratio in a range from 2.6x to 2.8x until 2013.

Inventory

We expect inventory turnover to fall from 3.4x in 2007 to an average of 2.9x, starting from 2008. This falling trend is consistent with DHG's strategy of reserving large amounts of raw materials to reduce input cost fluctuations as well as selling them to local companies when opportunities exist. As a result, inventory holding periods will be longer (at 137 days) compared to that of 2007 (at 107 days). Such long holding periods should not reflect problems but seen as rather a conservative strategy to improve flexibility of raw materials sources.

ROE and ROA

DHG's ROE fell to 19% by the end of 2008 compared to 31% in 2007. The combination of share issuances (to increase chartered capital from VND80bn to VND200bn) and the new tax rate of 10% in 2007 were two main reasons for the decline. The large equity base should keep average ROE at 20.7% until 2013. On the other hand, ROA only declined slightly to 12.8% by the end of 2008 (from 13.6% in 2007) due to smaller earnings growth compared to that of assets. Average ROA from 2009 to 2013 should stay constant at 13%.



VALUATION

Our valuation analysis results in a one year target price range for DHG between VND116,610 to VND126,057. The valuation is a mix between P/E, P/B and discounted cashflow analysis.

P/E valuation

P/E	2009	2010	2011	2012	2013
13	99,352	111,062	134,371	165,550	186,233
14	106,901	119,501	144,580	178,128	200,383
15	114,449	127,939	154,789	190,706	214,532
16	121,998	136,377	164,998	203,284	228,682
17	129,546	144,815	175,207	215,862	242,831

DHG's closing price on February 25th, 2009 was VND103,000 or 13.6x FY2009 EPS, about a 40% premium to the market. Applying a range of PE multiple from 14x to 16x to our projected 2009 earnings, the result is between VND106,901 to VND121,998 year end 2009 target. In terms of peer comparison, DHG's current price on 2008 EPS is 15.2x compared to 7.4x for DMC and 10.1x for IMP, reflective of DHG's dominant market position. Both DMC and IMP experienced negative EPS growth in FY2008 while DHG had a positive 11% growth.

P/B valuation

P/BV	2009	2010	2011	2012	2013
2.3	99,721	113,584	131,582	155,111	182,308
2.5	108,263	123,314	142,854	168,399	197,926
2.7	116,806	133,045	154,127	181,686	213,544
2.9	125,349	142,775	165,399	194,974	229,161
3.1	133,891	152,505	176,671	208,262	244,779

DHG is trading at 2.7x its book value, 60% lower than FY2007 figure. As the leading company in this industry, DHG has always traded at a premium P/B compared to other listed firms. We expect 2009FY PB should be in a range from 2.5x to 2.9x. As a result, our P/B valuation gave DHG's 2009 target price range of VND108,263 to VND125,349.

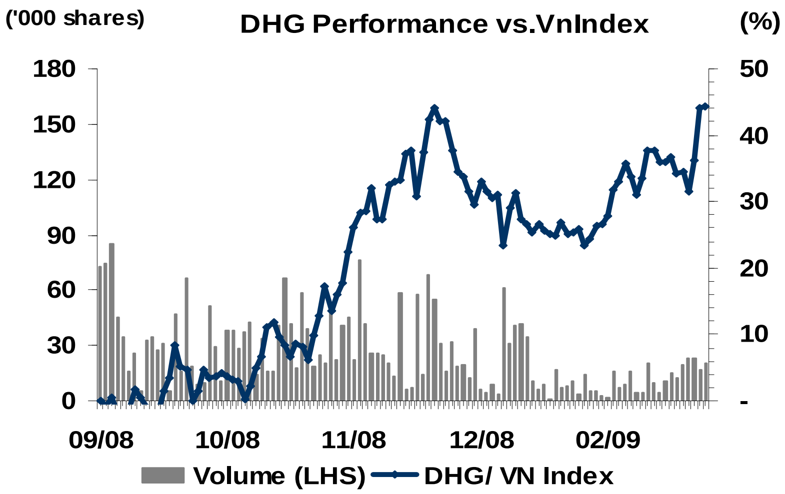
Discounted Cashflow

Free Cash Flows (VND bn)	FY07	FY08	FY09E	FY10E	FY11E	FY12E
NPAT for Corporate	115	136	151	169	204	252
Depreciation	24	29	26	37	51	56
Interest expense after tax	16	5	23	26	31	33
Changes in WC	(74)	(26)	(115)	(32)	(215)	(132)
CFO	81	143	85	200	72	209
Net investment	(53)	(21)	0	(158)	(35)	(38)
FCFF	28	122	85	42	37	170

We assumed a weighted average cost of capital (WACC) of 14.7%. Average growth rate of 9%. The result from this valuation gave DHG's FY2009 price of VND130,470.

Recent Stock Performance and Liquidity

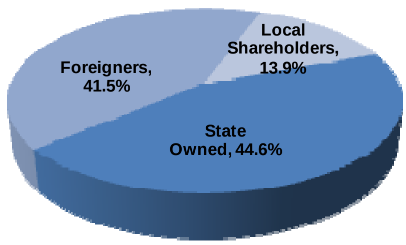
DHG's market capitalization of USD117.5m accounted for 1.5% of the total HOSE market capitalization. Average trading value came close to 0.8% of the total market steadily holding at USD72k/day during last month. The stock has outperformed the VNIndex by 44% during the last 6 months.



Shareholding Structure

The government is the largest shareholder for DHG with a 44.61% holding. This stock is also very popular with foreigners as they hold 41.5% of the total outstanding shares (Indochina Capital at 4.5%, Dragon Capital at 4% and Vinacapital at 2%). The remaining percentages belonged to domestic investors. At the time of the publication of this report, remaining room for foreign purchases was USD9.1m.

Shareholders Structure



RISKS

The Vietnamese Pharmaceutical industry will experience great changes this year when WTO commitments start to take effect. We expect a shift of market share to leading companies within the industry and many foreign entries in 2009. Although DHG might take benefit through gaining market share, investors should notice fluctuation in material prices and currency risk. In addition, new foreign entries will create more pressure on DHG.

WTO impact

According to WTO commitments, 100% foreign owned distribution companies are allowed to operate in Vietnam from 2009. The new entries will provide stronger competition compared to local firms due to their financial and product development strengths. DHG will still have an edge in its primary, generic products (antibiotics, vitamins) and oriental medicines since they do not require high R&D spending. On the other hand, patented products will face stronger competition and limit DHG's long term growth.

Currency risks and fluctuation in raw material prices

Since 85% of DHG raw materials are imported (mostly from EU countries), the company is highly exposed to currency risk which could negatively effect profit margins if the price for imported inputs increase significantly. Currently, DHG is using longer inventory periods to minimize sudden increases of inputs prices.

General risks from economic recession

The Vietnamese economy is facing many difficulties from the global recession. Reduction in consumers' purchasing power will affect demand for the whole industry although the negative impact on DHG's products may be limited due to the necessesity of their purchases for health purposes.

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