

Kingworld Medicines

(01110.HK/1110 HK)

Not rated

Price as of January 2 (HK\$)	0.96
12M target price (HK\$)	N/A
Previous target price (HK\$)	N/A
Unchanged / Revised up (down) (%)	N/A
Upside/downside (%)	N/A

Key message

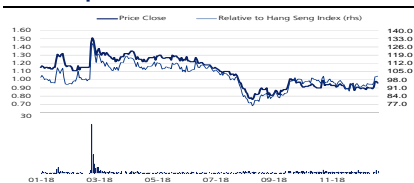
We had a company visit at Kingworld and met the IR Director. Overall sales rose 9.3% YoY in 1H18, driven by a 38% sales surge from Nin Jiom Chuan Bei Pei Pa Koa. After completion of the channel reform, management expects to see double-digit growth in 2H18. The star product remained the Culturelle probiotics product series in the healthcare product segment. Sales in Hong Kong and Macau were promising, while sales in China were disrupted by a supply shortage. Management is confident in achieving double-digit Culturelle's sales growth in the local market in 2H18 and 2019. The counter is trading at 10.5x 2017 historical PE. We do not offer a rating on it.

Trading data

Mkt cap (HK\$bn/US\$m)	0.598 / 76.29
Outstanding shares (mn)	623
Free Float (%)	31.4
3M avg. daily trading (mn)	0.60
52-week trading range (HK\$)	0.760 -1.51

Performance	3M	6M	12M
Absolute (%)	-3	-18.7	-16.5
Relative (%)	4.4	-5.5	1.2

Share price chart



Source: TEJ

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See the last page for important disclosures.

Improving outlook in 2019

Event

We had a company visit at Kingworld's office in Hong Kong and met its IR Director.

Impact

1H18 sales rose 9.3% YoY to Rmb556mn, in which sales from Nin Jiom Chuan Bei Pei Pa Koa surged 38% YoY, mainly due to Nin Jiom Chuan Bei Pei Pa Koa gaining recognition over the internet from an American's speedy recovery from his cough in February of 2018. Together with the completion of the channel reform initiated in 2H17 to standardize channel management, the company expects sales to grow by double digits in 2H18 via strengthening cooperation with regional chain stores, expanding distribution coverage to lower tier cities, and further leveraging brand recognition.

Due to the sales disruption from the channel reform in 1H18, sales of Taiko Seirogan products saw a 12.6% YoY decline in 1H18. According to management, the reform will be completed in early 2019. Taiko Seirogan revenue is forecasted to recover to positive growth upon the completion of the restructuring.

Regarding the healthcare product segment, the star product remained the Culturelle probiotics product series. Culturelle's sales in Hong Kong and Macau surged 63.7% YoY in 1H18. That said, sales in China were negatively affected by a supply shortage, leading to a sales decrease of 25.8% YoY. Thanks to the high brand recognition of Culturelle probiotics in Hong Kong, management is confident in achieving double-digit sales growth in the local market in 2H18 and 2019. However, it may take longer to smooth out the supply side in China.

Valuation & Action

Closing at HK\$0.96, the counter is trading at 10.5x 2017 historical PE. As Kingworld is an under-covered company with a small market capitalization without market consensus, there is no forward PE as a reference. We will keep an eye on its future plans for collaborations with well-established pharmaceutical companies in China. We currently do not offer a rating on Kingworld.

Risks

Heavy reliance on a single product; ability to identify products with potential in China; risk in expanding its distribution network.

Key financials and valuations

	Dec-15A	Dec-16A	Dec-17A
Revenue (RMBmn)	714	1,054	1,031
Gross profit (RMBmn)	227	324	323
Operating profit (RMBmn)	49	96	96
Net profit (RMBmn)	39	47	51
EPS (RMB)	0.06	0.07	0.08
DPS (RMB)	0.01	0.03	0.03
EPS growth (%)	0.0	22.3	14.0
PE (x)	14.7	12.0	10.5
PB (x)	1.0	1.1	1.0
EV/EBITDA (x)	11.2	6.6	6.8
Net debt to equity (%)	4.0	12.7	28.1
Dividend yield (%)	1.4	3.0	3.4
Return on average equity (%)	0.0	8.4	9.5

Source: Company data, KGI Research estimates

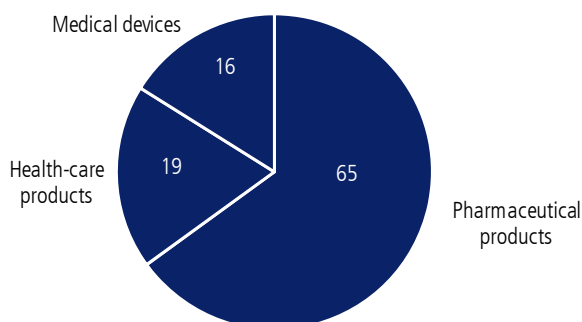
Figure 1: Interim results highlights

YE 31 Dec. (Rmb mn)	1H18	1H17	Remarks
Turnover	556.5	509.1	Sales of pharmaceutical products grew 29.5% YoY, while sales of healthcare products and medical devices declined by 18.9% YoY and 16.1% YoY, respectively.
% chg	9.3%	-	
COGS	(382.3)	(360.5)	
Gross profit	174.3	148.6	
Gross margin %	31.3%	29.2%	
Other revenue	8.0	12.9	
Admin. expenses	(41.5)	(33.7)	
Distribution and selling expenses	(89.0)	(71.7)	
Amortization of intangible assets	(9.4)	(9.4)	
Operating profit	42.4	46.7	
Operating margin %	7.6%	9.2%	
Finance costs	(8.0)	(12.7)	
Share of results of joint ventures	7.9	3.7	
Profit before tax	42.2	37.8	
Tax	(10.0)	(8.7)	
MI	(4.6)	(6.9)	
Net profit	27.5	22.1	
% chg	24.4%	-	
Net margin %	12.1%	17.1%	
EPS (Rmb)	0.044	0.034	

Source: Company data; KGI Research

Figure 2: Pharmaceutical products accounted for 65% of total sales

Sales weighting in 1H18 by product, percent



Source: Company data; KGI Research

Figure 3: Peer comparison – Valuations

Name	Bloomberg Code	Mkt. Cap. (US\$ mn)	Price (2/1) (LCY)	PE (x)				PB (x)		ROE (%)		Dividend yield (%)	
				2017A	2018F	2019F	2020F	2018F	2019F	2018F	2019F	2018F	2019F
Kingworld	1110 HK	77	0.96	9.3	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
China Medical System	867 HK	2,194	6.90	8.2	7.7	6.8	6.1	1.8	1.5	24.2	22.4	4.1	4.8
Hin Sang Group	6893 HK	128	0.91	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Besunyen Holdings	926 HK	76	0.37	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Sinopharm Group	1099 HK	11,829	31.05	14.4	13.3	11.7	10.4	1.9	1.7	15.5	15.5	2.0	2.3
H&H	1112 HK	3,472	42.30	25.8	18.7	14.6	11.6	4.4	3.5	24.5	26.4	0.6	0.9
Shanghai Pharmaceuticals	2607 HK	6,485	15.84	10.6	9.3	8.3	7.5	1.0	0.9	11.4	11.3	2.9	3.1
Average				13.6	12.2	10.4	8.9	2.3	1.9	18.9	18.9	2.4	2.8

Source: Bloomberg; KGI Research

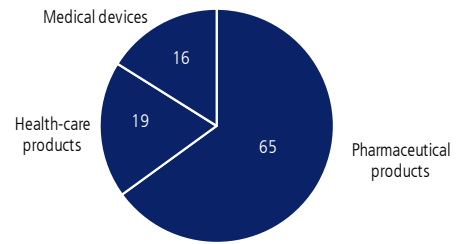
Figure 4: Company profile

Established in 1996, Kingworld is engaged in the distribution of branded imported pharmaceutical and health-care products in China. It distributes more than 60 products, mostly with exclusive distribution rights in China, Hong Kong, and Macau. The Nin Jiom series has been the key product line for the company, contributing 47% of total sales in 2017. In 2014, the company introduced the Culturelle probiotics product line to Hong Kong, Macau, and China. Sales of this line accounted for 19% of the total in 2017. The company was listed in 2010 at HK\$1.6 per share.

Source: KGI Research

Figure 5: Company overview

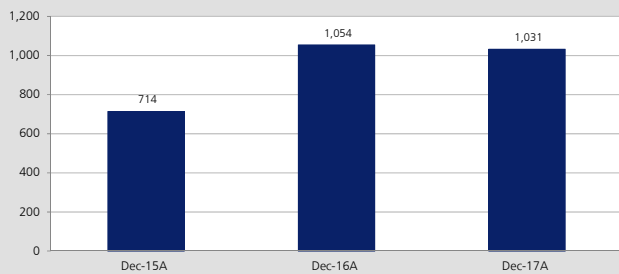
Revenue weighting in 1H18, percent



Source: KGI Research

Figure 6: Sales

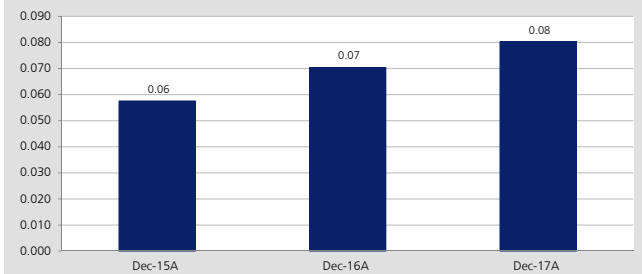
Sales, RMBmn



Source: KGI Research

Figure 7: EPS

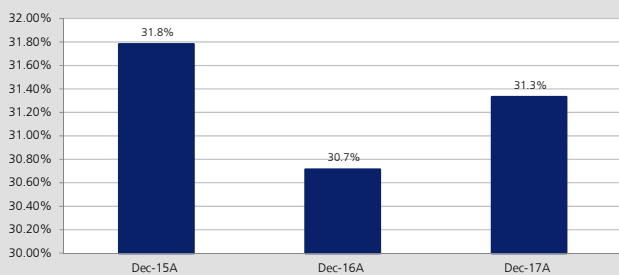
EPS, RMB



Source: KGI Research

Figure 8: Gross Margin

Gross margin, percent



Source: KGI Research

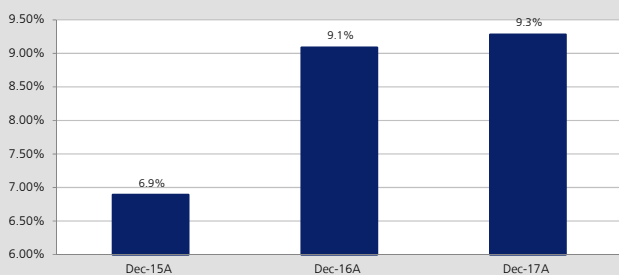
Figure 9: Rolling PE



Source: KGI Research

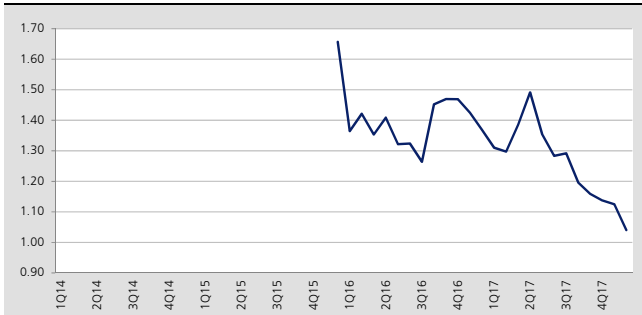
Figure 10: Operating Margin

Operating Margin, percent



Source: KGI Research

Figure 11: Rolling PB



Source: KGI Research

Balance sheet			
RMBmn	Dec-15A	Dec-16A	Dec-17A
Total assets	1,089	1,394	1,332
Current assets	611	888	839
Cash & ST securities	140	230	233
Inventory	79	128	149
Accounts receivable	287	438	413
Other current assets	105	92	44
Non-current assets	478	506	493
LT investments	108	108	113
Net fixed assets	16	23	57
Total other assets	354	375	323
Total liabilities	402	755	691
Current liabilities	372	727	665
Accounts payable	167	272	242
Interest bearing ST liabilities	168	311	413
Other current liabilities	38	144	10
Non-current liabilities	30	28	26
Long-term debt	-	-	-
Other L-T liabilities	30	28	26
Total equity	687	639	642
Shareholders' funds	591	524	553
Minority interests	96	115	89
Preferred shareholders funds	-	-	-
Key ratios			
	Dec-15A	Dec-16A	Dec-17A
Growth			
Revenue growth		47.6%	(2.1%)
Operating profit growth		94.8%	(0.0%)
EBITDA growth		88.7%	2.7%
Net profit growth		19.3%	8.7%
EPS growth		22.3%	14.0%
Profitability			
Gross profit margin	31.8%	30.7%	31.3%
Operating margin	6.9%	9.1%	9.3%
EBITDA margin	7.4%	9.5%	10.0%
Net profit margin	5.5%	4.5%	5.0%
Return on average assets		3.8%	3.7%
Return on average equity		8.4%	9.5%
Stability			
Gross debt to equity	24.4%	48.7%	64.4%
Net debt to equity	4.0%	12.7%	28.1%
Interest coverage (x)	4.3	7.9	4.2
Interest & ST debt coverage (x)	0.2	0.2	0.1
Cash flow interest coverage(x)	6.5	(0.3)	2.8
Cash flow/int. & ST debt (x)	0.6	(0.0)	0.2
Current ratio (x)	1.6	1.2	1.3
Quick ratio (x)	1.4	1.0	1.0
Net debt (RMBmn)	27	81	180
Per share data			
EPS (RMB)	0.06	0.07	0.08
CFPS (RMB)	0.15	(0.01)	0.11
BVPS (RMB)	0.86	0.80	0.89
SPS (RMB)	1.04	1.58	1.62
EBITDA/share (RMB)	0.08	0.15	0.16
DPS (RMB)	0.01	0.03	0.03
Activity			
Sales / avg assets		0.85	0.76
Days receivable	146.9	152.1	146.1
Days inventory	59.2	64.0	76.7
Days payable	125.0	136.2	124.8
Cash cycle	81.1	79.9	98.1

Source: Company data, KGI Research estimates

Profit & loss			
RMBmn	Dec-15A	Dec-16A	Dec-17A
Revenue	714	1,054	1,031
Cost of goods sold	(487)	(730)	(708)
Gross profit	227	324	323
Other operating income	(7)	(3)	24
Operating expenses	(171)	(225)	(251)
Operating profit	49	96	96
Other exceptional items	-	-	-
Income from associates	18	6	14
Interest expense	(16)	(13)	(26)
Pre-tax profit	51	89	83
Current taxation	(12)	(22)	(17)
Minorities	(8)	(20)	(15)
Extraordinary items	8	-	-
Net profit	39	47	51
EBITDA	53	100	103
EPS (RMB)	0.06	0.07	0.08

Cash flow			
RMBmn	Dec-15A	Dec-16A	Dec-17A
Operations cash flow	103	(4)	72
Operating profit	49	96	96
Depreciation & amortisation	4	4	7
Decrease in working capital	61	25	(112)
Other operating cashflow	16	(94)	125
Interest paid	(16)	(13)	(26)
Tax paid	(12)	(22)	(17)
Investing cash flow	(168)	(18)	24
Sale of ST investment	-	84	65
New investments	-	-	-
Capital expenditure	(6)	(11)	(40)
Others investing cashflow	(162)	(90)	(1)
Free cash flow	96	90	(70)
Financing cash flow	(1)	121	(83)
Increase in short term debt	(61)	144	112
Increase in long term loans	-	-	-
New ordinary shares issued	-	-	-
Ordinary dividends paid	-	(8)	(16)
Other financing cashflow	60	(15)	(179)
Total cash generated	(66)	99	13

ROIC			
	Dec-15A	Dec-16A	Dec-17A
1 - COGS/revenue	31.8%	30.7%	31.3%
- Operating exp./revenue	23.9%	21.3%	24.4%
= Operating margin	6.9%	9.1%	9.3%
1 / (Working capital/revenue	0.4	0.2	0.3
+ Net PPE/revenue	0.0	0.0	0.1
+ Other assets/revenue)	0.5	0.4	0.3
= Capital turnover	1.1	1.6	1.4
Operating margin	6.9%	9.1%	9.3%
x Capital turnover	1.1	1.6	1.4
x (1 - tax rate)	76.7%	75.7%	79.8%
= After-tax ROIC	5.9%	11.3%	10.4%

Source: Company data, KGI Research estimates

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	Not Rated (NR)	The stock is not rated by KGI Securities.
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