

# Biostime (1112 HK)

Share Price: HKD69.20

MCap (USD): 5.4B

Hong Kong

Target Price: HKD65.90(-5%)

ADTV (USD): 11M

Consumer Staples

# HOLD

(From BUY)

## Investment risk emerging; Take profit

- Downgrade to non-consensus HOLD from BUY, with a new TP of HKD65.90 (from HKD80.95) on more conservative sales/margin assumptions. TP multiple intact at 25x 14F PER.
- Channel checks suggest unsatisfactory end-point sales of ADIMIL series given unclear product positioning. Biostime also faces increasing competition from MNCs offering more discounts following sales slump in wake of scandals in 2H13.
- In addition, execution risk and OPEX burden mounting as Biostime introduces new business units and enters new product categories in future. Take profit on strength.

### What's New

Our discussions with retailers during our recent China trips suggested slow ADIMIL sales at end points. We also note MNCs such as Dumex and Abbott are now offering more discounts and incentives to distributors and customers to boost sales.

Industry sources also suggest Biostime is introducing new business units to manage the growing business portfolio; eg, separate teams will be responsible for ADIMIL and Biostime brands, etc.

Industry experts we talked to believe Biostime now has too many infant formula SKUs which are difficult to manage. The risk of product cannibalization is also on the rise.

We predict a sizable acquisition of an overseas branded manufacturer in the near future funded by its recent CB issue. On top of the recent diaper JV and in-house infant formula production investment, we await to see the execution progress.

### What's Our View

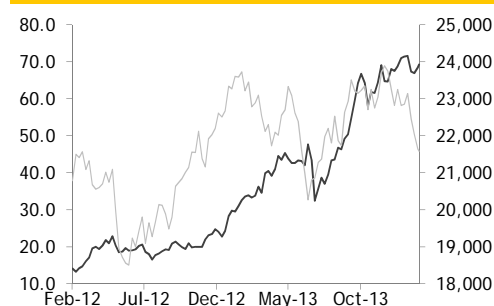
We lower our FY13/14/15 earnings forecasts by 9%/19%/20% as we adopt more conservative sales and margins assumptions. However, we have yet to factor in any earnings contributions/dilution from the recent acquisitions, the upcoming "ADISMART" launch in 2Q14 and OTO model (online to offline) into our forecasts.

FYE 31 Dec (CNY m)	FY11A	FY12A	FY13E	FY14E	FY15E
Revenue	2,189.0	3,381.9	4,788.7	6,281.0	8,007.1
EBITDA	709.6	1,031.9	1,441.2	1,717.8	2,197.1
Core net profit	527.4	743.1	1,024.9	1,290.5	1,688.1
Core EPS (CNY)	0.88	1.23	1.70	2.14	2.80
Core EPS growth (%)	50.3	40.9	37.9	25.9	30.8
Net DPS (CNY)	0.62	0.87	1.01	1.50	1.96
Core P/E (x)	61.7	43.8	31.8	25.2	19.3
P/BV (x)	16.5	14.0	11.6	9.5	7.8
Net dividend yield (%)	1.1	1.6	1.9	2.8	3.6
ROAE (%)	29.0	34.6	40.0	41.5	44.5
ROAA (%)	24.3	24.9	26.5	22.5	21.8
EV/EBITDA (x)	45.2	31.6	21.5	16.8	12.9
Net debt/equity (%)	net cash	net cash	net cash	net cash	net cash

### Key Data

52w high/low (HKD)	72.40/31.00
Free float (%)	25.2
Issued shares (m)	602
Market capitalization	HKD41.7B
Major shareholders:	
-Biostime Pharmaceuticals (China) Ltd.	75%
-Wasatch Advisors, Inc.	1%
-Thornburg Investment Management, Inc.	1%

### Share Price Performance



— Biostime (L) — Hang Seng Index (R)

	1 Mth	3 Mth	12 Mth
Absolute(%)	(3.1)	12.4	106.6
Relative to country (%)	2.6	18.5	122.2

### Maybank vs Market

	Positive	Neutral	Negative
Market Recs	7	4	0
	Maybank Consensus		% +/-
Target Price (HKD)	65.90	78.80	(16.4)
2013 PATMI(CNYm)	862	884	(2.4)
2014 PATMI(CNYm)	1,290	1,291	(0.0)

Source: FactSet; Maybank

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Figure 1: Sales estimates and assumptions

	FY11A	FY12A	FY13F	FY14F	FY15F
<b>Sales (CNY'000)</b>					
Probiotic supplements	331,962	379,203	507,471	583,591	659,458
Infant formula	1,684,655	2,715,291	3,919,765	5,265,252	6,830,067
Dried baby food	97,126	134,765	135,073	155,334	178,635
Baby care	47,845	105,989	164,897	206,122	257,652
Nutritional supplements	27,446	46,653	61,460	70,678	81,280
<b>Total</b>	<b>2,189,034</b>	<b>3,381,901</b>	<b>4,788,665</b>	<b>6,280,978</b>	<b>8,007,092</b>
<b>Growth rate (%)</b>					
Probiotic supplements	9.29	14.23	33.83	15.00	13.00
Infant formula	112.29	61.18	44.36	34.33	29.72
Dried baby food	(0.67)	38.75	0.23	15.00	15.00
Baby care	24.38	121.53	55.58	25.00	25.00
Nutritional supplements	N/A	69.98	31.74	30.00	28.00
<b>Total</b>	<b>77.46</b>	<b>54.49</b>	<b>41.60</b>	<b>31.16</b>	<b>27.48</b>

Source: Company data, Maybank Kim Eng estimates

Figure 2: Gross margin assumptions for different segments

Gross margin (%)	FY11A	FY12A	FY13F	FY14F	FY15F
Probiotic supplements	76.5	77.7	79.1	80.0	80.0
Infant formula	65.5	65.1	64.2	62.5	62.3
Dried baby food	57.3	56.9	56.9	56.0	55.0
Baby care	40.2	54.9	55.8	55.3	55.0
Nutritional supplements	70.3	65.4	64.1	64.0	64.0
<b>Total</b>	<b>66.5</b>	<b>65.9</b>	<b>65.2</b>	<b>63.7</b>	<b>63.4</b>

Source: Company data, Maybank Kim Eng estimates

Figure 3: OPEX assumptions

As % of sales	FY11A	FY12A	FY13F	FY14F	FY15F
S&D cost	32.37	31.87	31.21	32.00	31.80
Admin expense	3.75	3.46	3.81	4.00	3.90
Other expenses	1.07	1.14	1.26	1.30	1.30

Source: Company data, Maybank Kim Eng estimates

Figure 4: Mama100 membership system KPIs and POS coverage

	FY11A	FY12A	FY13F	FY14F	FY15F
Number of active members	825,230	1,400,781	2,093,038	2,818,259	3,543,480
Sales per active member (CNY)	2,069.1	2,044.9	2,085.8	2,044.1	2,044.1
Total POS	10,240	15,322	19,500	23,650	28,693
Active member per POS	80.6	91.4	107.3	119.2	123.5

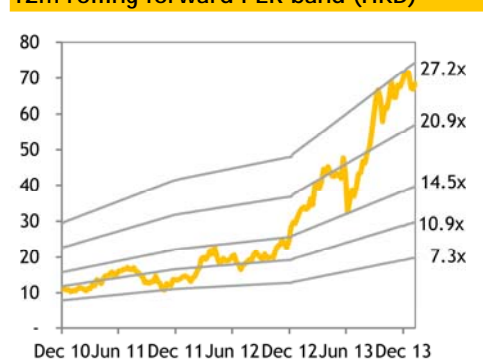
Source: Company data, Maybank Kim Eng estimates

12m rolling forward PER and +/-STD chart



Source: Bloomberg, Maybank Kim Eng

12m rolling forward PER band (HKD)



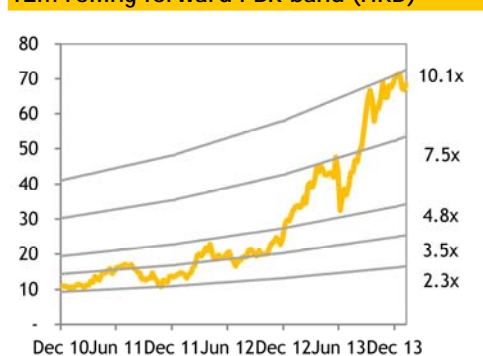
Source: Bloomberg, Maybank Kim Eng

12m rolling forward PBR and +/-STD chart



Source: Bloomberg, Maybank Kim Eng

12m rolling forward PBR band (HKD)



Source: Bloomberg, Maybank Kim Eng

FYE 31 Dec (CNY m)	FY11A	FY12A	FY13E	FY14E	FY15E
<b>Key Metrics</b>					
P/E (reported) (x)	61.7	43.8	37.8	25.2	19.3
Core P/E (x)	61.7	43.8	31.8	25.2	19.3
P/BV (x)	16.5	14.0	11.6	9.5	7.8
P/NTA (x)	16.5	14.0	11.6	9.5	7.8
Net dividend yield (%)	1.1	1.6	1.9	2.8	3.6
FCF yield (%)	1.5	2.3	2.0	4.0	4.2
EV/EBITDA (x)	45.2	31.6	21.5	16.8	12.9
EV/EBIT (x)	46.0	32.2	22.0	17.3	13.4
<b>Income Statement</b>					
Revenue	2,189.0	3,381.9	4,788.7	6,281.0	8,007.1
Gross profit	1,456.1	2,228.9	3,123.9	4,002.0	5,073.3
EBITDA	709.6	1,031.9	1,441.2	1,717.8	2,197.1
Depreciation	(12.8)	(21.8)	(32.4)	(54.5)	(82.3)
Amortisation	(0.1)	(0.3)	(0.3)	(0.2)	(0.2)
EBIT	696.6	1,009.3	1,408.5	1,663.1	2,114.6
Net interest income / (exp)	17.3	41.3	51.3	56.8	135.3
Associates & JV	0.0	0.0	0.3	0.7	0.9
Exceptionals	0.0	0.0	(162.9)	0.0	0.0
Other pretax income	0.0	0.0	0.0	0.0	0.0
Pretax profit	713.9	1,050.6	1,297.2	1,720.6	2,250.8
Income tax	(186.6)	(307.5)	(438.4)	(430.2)	(562.7)
Minorities	0.0	0.0	0.0	0.0	0.0
Reported net profit	527.4	743.1	862.0	1,290.5	1,688.1
Core net profit	527.4	743.1	1,024.9	1,290.5	1,688.1
<b>Balance Sheet</b>					
Cash & Short Term Investments	1,814.1	1,669.1	1,877.0	4,145.9	4,609.8
Property, Plant & Equip (net)	59.4	77.1	144.7	240.2	357.8
Intangible assets	1.4	1.2	0.9	0.6	0.5
Investment in Associates & JVs	0.0	0.0	8.0	398.7	399.6
Other assets	563.1	1,786.1	2,176.5	2,499.1	2,841.9
Total assets	2,438.1	3,533.4	4,207.0	7,284.5	8,209.6
ST interest bearing debt	0.0	270.5	338.2	372.0	297.6
LT interest bearing debt	0.0	0.0	0.0	0.0	0.0
Other liabilities	460.5	940.2	1,070.6	3,487.3	3,756.2
Total Liabilities	460.5	1,210.7	1,408.8	3,859.3	4,053.8
Shareholders Equity	1,977.6	2,322.7	2,798.2	3,425.2	4,155.9
Minority Interest	0.0	0.0	0.0	0.0	0.0
Total shareholders equity	1,977.6	2,322.7	2,798.2	3,425.2	4,155.9
<b>Cash Flow</b>					
Pretax profit	713.9	1,050.6	1,297.2	1,720.6	2,250.8
Depreciation & amortisation	13.0	22.6	32.7	54.7	82.5
Adj net interest (income)/exp	(17.3)	(43.4)	(58.4)	(65.7)	(145.1)
Change in working capital	(77.2)	101.5	(212.2)	157.1	(73.9)
Cash taxes paid	(123.0)	(307.5)	(438.4)	(430.2)	(562.7)
Other operating cash flow	43.3	79.0	79.0	78.9	78.8
Cash flow from operations	516.2	823.4	766.5	1,436.6	1,551.5
Capex	(38.8)	(60.7)	(100.0)	(150.0)	(200.0)
Free cash flow	477.4	762.7	666.5	1,286.6	1,351.5
Dividends paid	(180.5)	(406.0)	(533.4)	(664.2)	(958.2)
Equity raised / (purchased)	21.5	0.0	0.0	0.0	0.0
Change in Debt	0.0	270.5	67.6	2,066.3	(74.4)
OTH investing/financing cash flow	(490.5)	(738.7)	7.2	(29.8)	145.1
Effect of exch rate changes	(55.9)	0.0	0.0	0.0	0.0
Net cash flow	(168.8)	(135.5)	(513.6)	1,306.6	(1,032.6)

FYE 31 Dec (CNY m)	FY11A	FY12A	FY13E	FY14E	FY15E
<b>Key Ratios</b>					
<b>Growth ratios (%)</b>					
Revenue growth	77.5	54.5	41.6	31.2	27.5
EBITDA growth	109.4	45.4	39.7	19.2	27.9
EBIT growth	109.9	44.9	39.6	18.1	27.1
Pretax growth	113.7	47.2	23.5	32.6	30.8
Reported net profit growth	98.5	40.9	16.0	49.7	30.8
Core net profit growth	98.5	40.9	37.9	25.9	30.8
<b>Profitability ratios (%)</b>					
EBITDA margin	32.4	30.5	30.1	27.3	27.4
EBIT margin	31.8	29.8	29.4	26.5	26.4
Pretax profit margin	32.6	31.1	27.1	27.4	28.1
Payout ratio	70.6	70.9	70.2	70.0	70.0
<b>DuPont analysis</b>					
Net profit margin (%)	24.1	22.0	18.0	20.5	21.1
Revenue/Assets (x)	0.9	1.0	1.1	0.9	1.0
Assets/Equity (x)	1.2	1.5	1.5	2.1	2.0
ROAE (%)	29.0	34.6	40.0	41.5	44.5
ROAA (%)	24.3	24.9	26.5	22.5	21.8
<b>Liquidity &amp; Efficiency</b>					
Cash conversion cycle	67.7	77.1	93.3	98.6	96.5
Days receivable outstanding	1.2	0.5	1.8	2.8	2.4
Days inventory outstanding	99.1	128.1	141.2	138.3	136.8
Days payables outstanding	32.7	51.6	49.7	42.5	42.8
Dividend cover (x)	1.4	1.4	1.4	1.4	1.4
Current ratio (x)	5.2	2.0	2.1	3.1	3.2
<b>Leverage &amp; Expense Analysis</b>					
Asset/Liability (x)	5.3	2.9	3.0	1.9	2.0
Net debt/equity (%)	net cash	net cash	net cash	net cash	net cash
Net interest cover (x)	na	na	na	na	na
Debt/EBITDA (x)	0.0	0.3	0.2	0.2	0.1
Capex/revenue (%)	1.8	1.8	2.1	2.4	2.5
Net debt/ (net cash)	(1,814.1)	(1,398.5)	(1,538.8)	(3,773.9)	(4,312.2)

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