Monday, August 29, 2022

Company Report

China Merchants Securities (HK) Co., Ltd.
Hong Kong Equity Research

Hansoh (3692 HK)

Soft 1H22; portfolio upgrades on pace

- **1H22 revenue/attributable NP were flat, falling short CMS est. by 9%/3%; due to COVID disruption and VBP headwinds**
- **Co. guided low-single digit growth for full year FY22E; and expected almonertinib to achieve RMB3.3bn in FY22E**
- **We revised down SOTP-based TP to HKD23.1. Maintain BUY on Co.'s enhancing pipeline and well-capitalized position in BD front**

Flat results in 1H22; balance sheet remained robust

1H22 total revenue was flat at RMB4,434mn (+0.7% yoy), primarily caused by Omicron disruption and ongoing VBP pressures, partly offsetting by new innovative products (+85% yoy to RMB2,319mn). Co. expects sales from innovative drugs will continue to increase to 55% of total revenue in FY22E (vs 46%/52% in FY21/1H22). Co. guided its flagship drug almonertinib will reach RMB3.3bn sales in FY22E and is well position to attend the upcoming 2022 NRDL negotiation for addition of 1L NSCLC indication. Meanwhile, ongoing generic GPO continued to weigh heavily on its generic portfolio (down 33% yoy to RMB2,115mn). We anticipate the generic sales downtrend to continue amid deepening national and regional VBPs. Co. placed more efforts on its pipeline upgrades, with R&D expense ratio further expanded by 1.1ppt to 16.7%. We expect Co. to maintain 15.5%-16% of R&D ratio (o/w 14.5% R&D ratio should be associated with in-house R&D). OCF grew 64% yoy to RMB1,774mn reflecting sound A/R management (A/R down to RMB3bn in 1H22 vs. RMB3.2bn/3.7bn at end of 1H21/YE21). Net cash remained strong at ~RMB15bn, reflecting a healthy B/S in our view.

BD activities on good footing

Co. announced three in-licensing BD deals YTD 2022, including 1) NKT2152 (HIF-2α inhibitor) from NiKang Therapeutics for RCC in May, 2) TU2670 (an orally active non-peptide GnRH antagonist) from TiumBio for the treatment of endometriosis and uterine fibroids in Aug; and 3) GDI-4405 (3CL protease inhibitor) from Beijing Huayi Health for COVID treatment in Aug. We believe these licensing deals should further enrich Co.'s innovative pipeline and add supports to Co.'s efforts to achieve pipeline upgrades.

Maintain BUY, SOTP-based TP cut to HKD23.1

We revised down FY22E/23E adj. NP by 8%/7% to reflect lower-than-expected 1H22 growth and ongoing VBP headwinds. We cut SOTP-based TP to HKD23.1 from HKD30.4. We identify continued pipeline upgrades will be the major rerate catalysts. **Investment risk**: clinical delay/failure, lower-than-expected sales, regulatory risks, NRDL-driven price cut risk.

RMB mn	2019	2020	2021	2022E	2023E
Consolidated revenue	8,683	8,690	9,935	10,155	11,457
yoy change	12%	0%	14%	2%	13%
Adjusted net profit	2,574	2,597	2,738	2,795	3,182
yoy change	35%	1%	5%	2%	14%
EPS Fully diluted (HKD)	0.53	0.53	0.60	0.55	0.64
PER adj (x)	29.1	29.1	25.9	28.2	24.4
PBR (x)	6.1	4.5	4.0	3.7	3.2

Sources: Company data, CMS (HK) estimates

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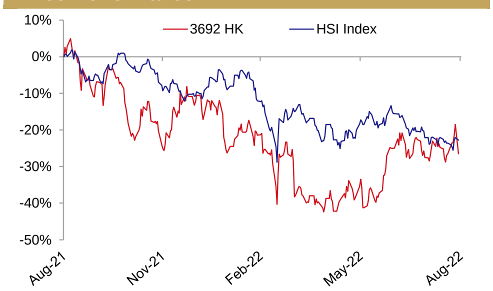
WHAT'S NEW

1H22 earnings update; TP revision

BUY

Previous	BUY
Price (Aug 29, 2022)	HKD15.5
12-month Target Price (Potential up/downside)	HKD23.1 (+49%)
Previous	HKD30.4

Price Performance



Source: Bloomberg

%	1m	6m	12m
3692 HK	1.4	(0.1)	(26.5)
HSI	(0.9)	(10.6)	(22.8)

Sector: Pharmaceutical & Healthcare	
Hang Seng Index (Aug 29, 2022)	20,023
HSCEI (Aug 29, 2022)	6,872
Key Data	
52-week range (HKD)	12.0-22.6
Market cap (HKD mn)	91,915
Avg. daily traded value (HKD mn)	62.7
BVPS (HKD)	4.8
Shareholding Structure	
Founding members	65.9%
Cen Junda	16.0%
Free float	18.1%

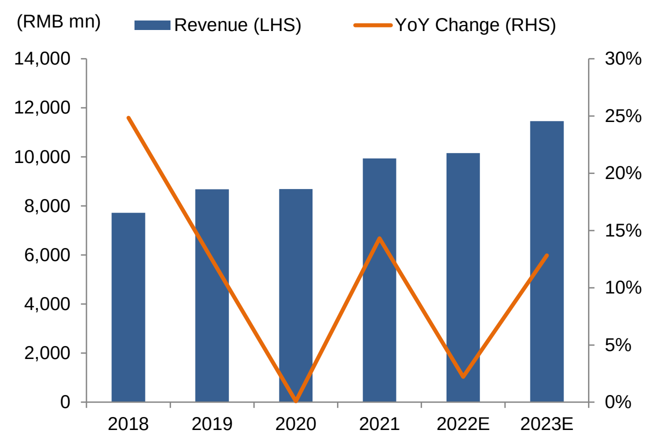
Source: Bloomberg

Related Research

1. HANSOH PHARMA (3692 HK) - Continued portfolio upgrade amid VBP headwind (BUY) (Apr 6, 2022)
2. HANSOH PHARMA (3692 HK) - Continued efforts in improving pipeline (BUY) (Oct 19, 2021)
3. HANSOH PHARMA (3692 HK) - Soft 1H21 results; strong B/S support pipeline upgrades (BUY) (Sep 7, 2021)
4. HANSOH PHARMA (3692 HK) - FY20 results in line; new products to drive LT growth (BUY) (Mar 30, 2021)

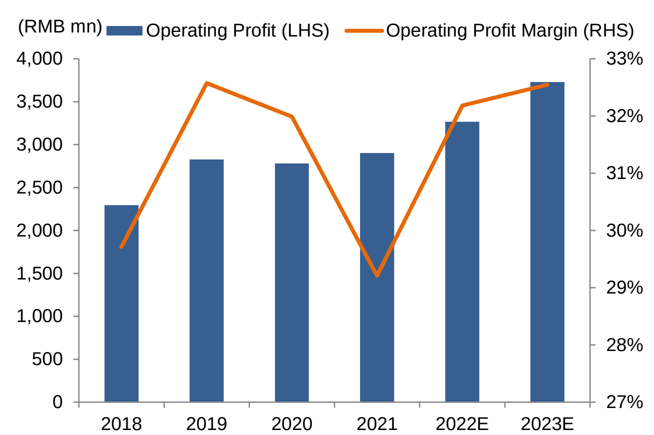
Focus charts

Figure 1: Total revenue and growth forecast



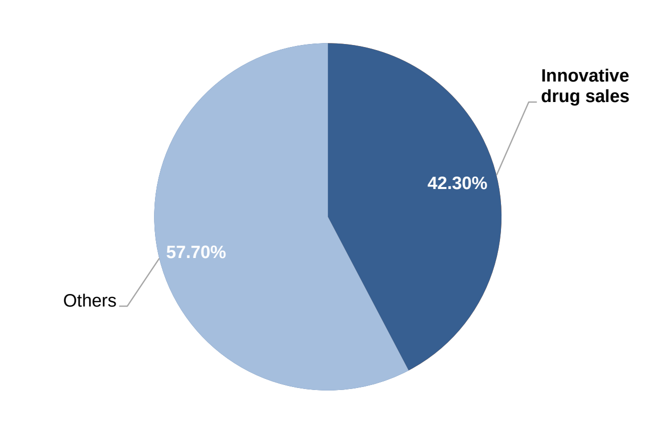
Sources: Company, CMS (HK) estimates

Figure 2: Operating profit and OP margin forecast



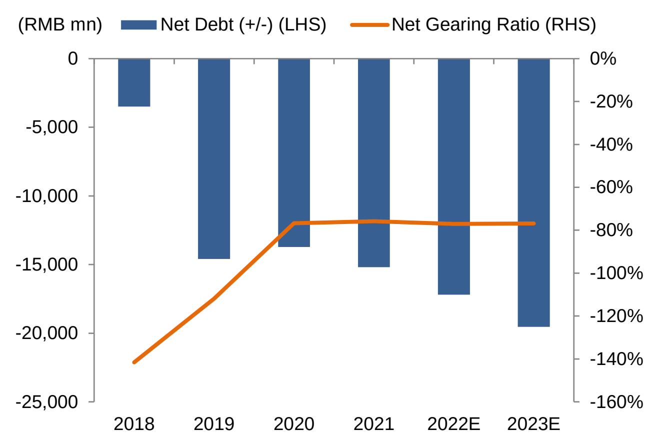
Sources: Company, CMS (HK) estimates

Figure 3: Hansoh's innovative drug sales achieved fast uptake in FY21



Source: Company

Figure 4: Net gearing position and net gearing trend



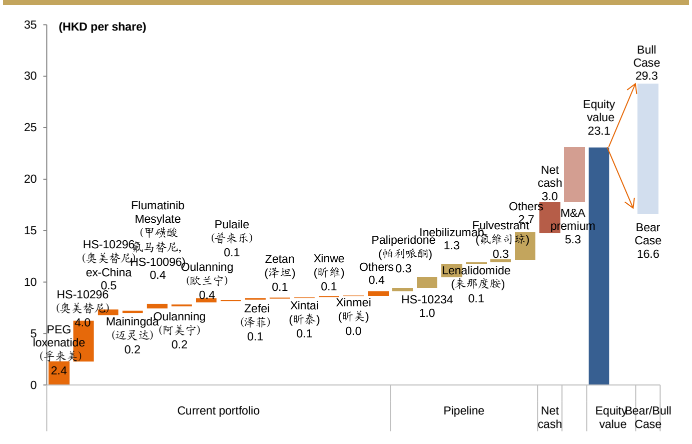
Source: Company, CMS (HK) estimates

Figure 5: Comparison between two approved 3rd-Gen EGFR TKI in China

Drug	Aumolertinib	Osimertinib
Company	Hansoh	AZ
Trial	APOLLO	AURA3 (treatment arm)
No. of patients	244	279 (treatment arm)
Indications	2L NSCLC (EGFR T790M+)	2L NSCLC (EGFR T790M+)
Phase	Phase 2	Phase 3
ORR (CR)	68.9% (0%)	70.6% (9.7%)
DCR	93.4%	93.2%
mDOR (mon)	12.4	9.7
mPFS (mon)	12.3	10.1
mOS (mon)	30.2	26.8
Safety	AE Grade ≥3 20.9% SAE 10.2% Death 1.6%	AE Grade ≥3 9% SAE 30.1% Death 0.7%

Sources: Company, ESMO, AACR

Figure 6: Valuation bridges



Source: CMS (HK) estimates

Figure 7: Financials revision

(RMB mn)	2022E			2023E		
	OLD	NEW	Chg	OLD	NEW	Chg
Consolidated revenue	**10,793**	**10,155**	**(5.9%)**	**12,226**	**11,457**	**(6.3%)**
Cost of goods sold	(971)	(914)	(5.9%)	(1,100)	(1,088)	(1.1%)
Gross profit	**9,821**	**9,241**	**(5.9%)**	**11,126**	**10,369**	**(6.8%)**
Total SG&A and other expenses	(4,695)	(4,468)	(4.8%)	(5,318)	(4,984)	(6.3%)
Administrative expenses	(971)	(812)	(16.4%)	(1,100)	(974)	(11.5%)
Selling and distribution costs	(3,723)	(3,656)	(1.8%)	(4,218)	(4,010)	(4.9%)
R&D expenses	(1,673)	(1,625)	(2.9%)	(1,895)	(1,776)	(6.3%)
Other income, gains and losses	120	120	-	120	120	-
EBITDA	**3,955**	**3,650**	**(7.7%)**	**4,467**	**4,163**	**(6.8%)**
Total depreciation and amortisation	(382)	(382)	-	(434)	(434)	-
Depreciation expense	(361)	(361)	-	(413)	(413)	-
Amortisation expenses	(21)	(21)	-	(21)	(21)	-
EBIT (incl. associate)	**3,574**	**3,268**	**(8.6%)**	**4,032**	**3,729**	**(7.5%)**
Associates	-	-	-	-	-	-
Financial income (expense)	31	31	-	41	41	(0.2%)
Interest income	87	87	-	97	97	(0.1%)
Interest expense	(56)	(56)	-	(56)	(56)	-
Forex gain (loss)	-	-	-	-	-	-
Others	-	-	-	-	-	-
Non-operating profit (loss)	30	30	-	30	30	-
Pretax profit	**3,635**	**3,329**	**(8.4%)**	**4,104**	**3,800**	**(7.4%)**
Tax	(654)	(599)	(8.4%)	(739)	(684)	(7.4%)
Minority interest	-	-	-	-	-	-
NP attributable to shareholders	**2,980**	**2,730**	**(8.4%)**	**3,365**	**3,116**	**(7.4%)**
Adjusted net profit	**3,046**	**2,795**	**(8.2%)**	**3,430**	**3,182**	**(7.3%)**
			-			-
EPS Fully diluted (RMB)	**0.51**	**0.47**	**(8.2%)**	**0.57**	**0.53**	**(7.3%)**
Growth (%)			**p.p.**			**p.p.**
Consolidated revenue	9%	2%	-6	13%	13%	0
Gross profit	8%	2%	-6	13%	12%	-1
Adjusted net profit	11%	2%	-9	13%	14%	1
Profitability (%)						
Gross margin (%)	91.0%	91.0%	0	91.0%	90.5%	-1
Adj. net profit margin (%)	28.2%	27.5%	-1	28.1%	27.8%	0

Source: CMS (HK) estimates

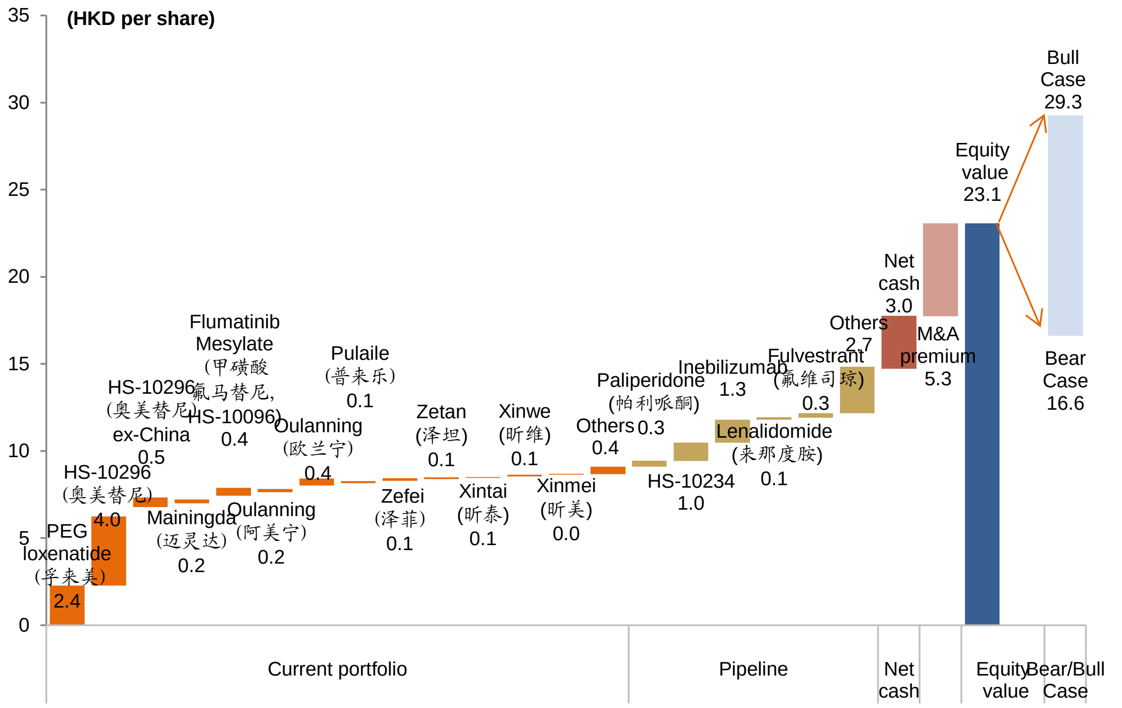
Valuation summary

Figure 8: Valuation summary

	Previous	Revised	Change
Portfolio (RMB mn)			
PEG loxenatide (孚来美 GLP-1 / PEX168)	12,068	11,399	-6%
HS-10296 (奥美替尼)	27,683	19,952	-28%
HS-10296 (奥美替尼) ex-China	4,522	2,734	-40%
Mainingda (迈灵达)	1,149	1,083	-6%
Flumatinib Mesylate (甲磺酸氟马替尼, HS-10096)	2,326	2,205	-5%
Ameining (阿美宁)	1,060	951	-10%
Oulanning (欧兰宁)	1,981	1,981	0%
Pulaile (普来乐)	759	630	-17%
Zefei (泽菲)	824	727	-12%
Zetan(泽坦)	509	509	0%
Xintai (昕泰)	679	270	-60%
Xinwe (昕维)	475	473	0%
Xinmei (昕美)	263	232	-12%
Apixaban (阿哌沙班)	371	367	-1%
Vildagliptin (维格列汀)	321	317	-1%
Canagliflozin (卡格列净)	383	379	-1%
Prucalopride succinate (琥珀酸普卡必利)	194	193	-1%
Others	1,347	892	-34%
Pipeline (RMB mn)			
Paliperidone (帕利哌酮)	1,654	1,632	-1%
HS-10234	9,499	5,268	-45%
Inebilizumab	7,206	6,583	-9%
Lenalidomide (来那度胺)	628	620	-1%
Rivaroxaban (利伐沙班)	1,281	1,263	-1%
Fulvestrant (氟维司琼)	550	544	-1%
Lurasidone hydrochloride (盐酸鲁拉西酮)	445	439	-1%
Dexlansoprazole （右兰索拉唑)	371	367	-1%
Dabigatran etexilate (甲磺酸达比加群酯)	270	267	-1%
HS-10342	2,906	2,721	-6%
Others	22,539	9,016	-60%
Add: Net cash	15,190	15,190	0%
Equity valuation	**119,450**	**89,204**	**-25%**
Equity valuation after M&A premium at 30%	**155,285**	**115,966**	**-25%**
No. of shares (mn)	5,878	5,878	0%
TP (HKD)	**30.4**	**23.1**	**-24%**

Source: CMS (HK) estimates

Figure 9: Co.'s risk-adjusted NPV summary



Source: CMS (HK) estimates

Financial Summary

Balance Sheet

RMB mn	2019	2020	2021	2022E	2023E
Non-current assets	**2,127**	**3,506**	**3,981**	**4,307**	**4,581**
PP&E	1,741	2,039	3,225	3,564	3,851
Lease prepayment for LUR	187	264	251	230	208
Intangible assets	5	10	17	25	33
Others	195	1,192	488	488	488
Current assets	**17,448**	**17,286**	**23,179**	**25,061**	**27,938**
Inventories	414	299	410	411	490
Trade receivables	2,246	3,127	3,676	3,554	4,010
Other receivables	194	142	160	160	160
Financial assets	6,355	9,433	4,231	4,231	4,231
Total cash and cash equivalents	8,238	4,285	14,702	16,704	19,047
Total assets	**19,575**	**20,792**	**27,160**	**29,368**	**32,519**
Current liabilities	**6,240**	**2,690**	**3,024**	**2,958**	**2,993**
Trade and bills payables	193	124	248	183	218
Other payables	6,007	2,554	2,641	2,641	2,641
Income tax payable	41	11	134	134	134
ST bank debt	-	-	-	-	-
Non-current liabilities	**291**	**227**	**365**	**365**	**365**
Deferred government grants	-	-	-	-	-
Deferred tax liabilities	285	122	267	267	267
LT bank loans	-	-	-	-	-
Shareholders' funds	**13,044**	**17,876**	**20,029**	**22,302**	**25,418**
Minorities	**-**	**-**	**-**	**-**	**-**
Total liability and equity	**19,575**	**20,792**	**27,160**	**29,368**	**32,519**

Profit & Loss Statement

RMB mn	2019	2020	2021	2022E	2023E
Consolidated revenue	**8,683**	**8,690**	**9,935**	**10,155**	**11,457**
Cost of goods sold	(730)	(802)	(870)	(914)	(1,088)
Gross profit	**7,953**	**7,889**	**9,065**	**9,241**	**10,369**
(–) Total SG&A expense	**(4,044)**	**(3,862)**	**(4,371)**	**(4,468)**	**(4,984)**
Administrative expenses	(778)	(759)	(943)	(812)	(974)
Selling costs	(3,266)	(3,103)	(3,428)	(3,656)	(4,010)
(–) R&D expenses	**(1,121)**	**(1,252)**	**(1,797)**	**(1,625)**	**(1,776)**
(+/–) Other income, net	**40**	**5**	**5**	**120**	**120**
EBITDA	**3,030**	**3,013**	**3,181**	**3,650**	**4,163**
Total Dep. & amort.	(202)	(233)	(278)	(382)	(434)
EBIT	**2,828**	**2,780**	**2,902**	**3,268**	**3,729**
(+/–) Finance income, net	164	155	103	31	41
(+/–) Profit from JV & Asso.	-	-	-	-	-
(+/–) Other income, net	9	163	295	30	30
Profit before tax	**3,001**	**3,098**	**3,300**	**3,329**	**3,800**
(–) Tax	(444)	(529)	(587)	(599)	(684)
Net Profit	**2,557**	**2,569**	**2,713**	**2,730**	**3,116**
(+/–) Minority interest	-	-	-	-	-
Net profit attri to shareholders	**2,557**	**2,569**	**2,713**	**2,730**	**3,116**
Adjusted net profit	**2,574**	**2,597**	**2,738**	**2,795**	**3,182**
EPS Fully diluted (RMB)	**0.47**	**0.47**	**0.50**	**0.47**	**0.53**
EPS Fully diluted (HKD)	**0.53**	**0.53**	**0.60**	**0.55**	**0.64**

Cashflow Statement

RMB mn	2019	2020	2021	2022E	2023E
CF from operating	**3,330**	**2,206**	**2,393**	**3,080**	**2,954**
Pretax profit	3,001	3,098	3,300	3,329	3,800
OP before WC chgs	3,039	3,570	3,569	3,680	4,193
Net WC chgs	832	(834)	(536)	55	(499)
Income tax paid	(541)	(529)	(587)	(599)	(684)
Interest paid	-	-	(53)	(56)	(56)
CF from investing	**(7,076)**	**(3,543)**	**(2,143)**	**(621)**	**(611)**
Purchase of PPE	(581)	(627)	(1,400)	(700)	(700)
Purchase of land use right	-	-	-	-	-
Purchase of intangible assets	(5)	(8)	(8)	(8)	(8)
Purchases of ST investment, net	(6,658)	-	-	-	-
Interest received	108	92	92	87	97
Others	62	(3,000)	(827)	-	-
CF from financing	**7,993**	**(945)**	**3,406**	**(457)**	**-**
Issuance of equity shares	9,534	3,161	-	-	-
Dividends	(1,500)	(4,200)	(381)	(457)	-
Others	(42)	94	-	-	-
Beginning cash	**965**	**5,345**	**3,063**	**6,719**	**8,721**
Forex	*133*	-	-	-	-
End cash	**5,345**	**3,063**	**6,719**	**8,721**	**11,064**

Sources: Company data, CMS (HK) estimates

Financial Ratios

	2019	2020	2021	2022E	2023E
Growth					
Consolidated revenue	12%	0%	14%	2%	13%
Gross profit	12%	-1%	15%	2%	12%
Adjusted net profit	35%	1%	5%	2%	14%
Profitability					
Gross margin	92%	91%	91%	91%	91%
Adj. net profit margin	30%	30%	28%	28%	28%
ROE	20%	15%	14%	13%	13%
ROA	13%	12%	10%	9%	10%
Efficiency					
Inventory days	221	160	147	162	149
Accounts receivable days	101	111	123	128	119
Accounts payable days	87	71	77	85	66
Cash cycle days	235	200	193	205	202
Liquidity					
FCF (RMB mn)	2,851	1,663	1,077	2,459	2,343
Net gearing (%)	(112)	(77)	(76)	(77)	(77)

Investment Ratings

Industry Rating	Definition
OVERWEIGHT	Expect sector to outperform the market over the next 12 months
NEUTRAL	Expect sector to perform in-line with the market over the next 12 months
UNDERWEIGHT	Expect sector to underperform the market over the next 12 months

Company Rating	Definition
BUY	Expect stock to generate 10%+ return over the next 12 months
HOLD	Expect stock to generate +10% to -10% over the next 12 months
SELL	Expect stock to generate loss of 10%+ over the next 12 months

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