BIDV securities company

Pharmaceutical sector - ICB 4577
March, 4th, 2014

# CORPORATION ANALYSIS REPORT
## Cuu Long Pharmaceutical Joint Stock Corporation (DCL)

### TRADING GRAPH

Đồ thị vẽ theo giá điều chỉnh đv KLg: 10,000cp

### RECOMMENDATION

| | |
|---|---|
| Investment view | **Strong buy** |
| Target price | 46.9 |
| Current price (March, 4th 2014) | 30.5 |
| Prospect in 3 month | Increase |
| Prospect in 6 month | Increase |
| Prospect in 12 month | Increase |

### TRADING INFORMATION

| | |
|---|---|
| Outstanding shares(million shares) | **9.91** |
| Market Cap (billion) | 306.81 |
| Total book value (billion) | 285.37 |
| Foreign ownership (%) | 19.78% |
| Current price (dong/share) March, 4th 2014 | 30.5 |
| Average trading volume in 10 days (share) | 58.47 |
| Lowest price 52 wks (dong) | 11.9 |
| Highest price 52wks (dong) | 33.5 |
| +/- 7 days | -3.60% |
| +/- 1 month | 4.09% |

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### INVESTMENT HIGHLIGHT

**Vietnam pharmaceutical market retained a high and stable growth**: Vietnam ranked 13th out of 137 countries having highest pharmaceutical growth in the world. The compound annual growth rate (CAGR) of 2009-2013 is 24.83%. According to BMI, Vietnam market value 2014 was estimated at 80.193 billion dongs, up 15.72% compared to 2013.

**DCL's revenue includes** 52.21% of pharmaceutical; 28.61% of capsule 10.01% of Vikimco and 9.17% of goods for resale.

**Effective restructuring:** Since 2012, DCL's leaderships have actively reformed, in which they have mainly focused on sales and marketing strategy, policy for company's receivables and liabilities, product restructuring in oder to improve DCL's revenue and its cash flow.

**Company's performance was flourished from 2011 to 2013**: In 2011, the company lost nearly 31 billion dongs. Due to effective restructuring, up to Q2/2013, DCL had removed its accumulated losses. In 2013, the firm gained 36 billion dongs, up 86.32% over 2012, in which, its revenue increased 14.27%, its gross margin rose to 29.73% from 27.94%, its interest expense decreased 41% compared to 2012.

**DCL's expected performance in 2014:** We expect that its revenue will reach 750 billion dongs, up 7.28% over 2013. Gross profit margin is predicted to rise from 29.73% to 31.74% due to selling higher profit products. Financial expense reduced also push the increase in net income. We hope that the firm will reach 42 billion dongs of net income, equivalent to 4.201 dongs of EPS, up 18.98% compared to 2013.

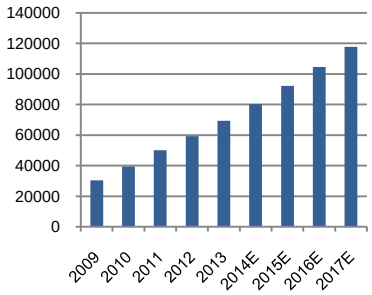
**Investment points:** DCL is a defensive stock with its beta less than 1, low liquidity so it is suitable for long-term investment. Its performance is improved because of effective restructuring and it is one of a few company that have P/B of 1.1 and P/E of 8. We recommend buying DCL with expected price next 12 months is 46.900 dongs per share.

| Financial information | 2009 | 2010 | 2011 | 2012 | 2013 |
|---|---|---|---|---|---|
| Net revenue (Bil.VND) | 576 | 558 | 630 | 612 | 699 |
| % y-o-y | | -3.11% | 12.99% | -2.89% | 14.27% |
| Total assets (Bil.VND) | 641 | 792 | 875 | 666 | 613 |
| Equity (Bil.VND) | 300 | 280 | 267 | 250 | 285 |
| Capital charter (Bil. VND) | 99.14 | 100 | 100 | 100.59 | 101.08 |
| Outstanding shares (Mil.) | 9.7 | 9.9 | 9.9 | 9.9 | 9.9 |
| Profit after tax (Bil.VND) | 56.5 | 11.7 | -30.8 | 19.2 | 35.7 |
| % y-o-y | | -79.21% | -362.20% | -162.22% | 85.93% |
| EPS (dongs/share) | 5812 | 1184 | -3106 | 1932 | 3600 |
| Book value (dongs/share) | 30,918 | 28,221 | 26,974 | 25,186 | 28,786 |
| Gross profit margin | 24.22% | 26.45% | 25.98% | 27.94% | 29.73% |
| ROS | 9.81% | 2.11% | -4.89% | 3.13% | 5.11% |
| ROE | 19.68% | 4.05% | -11.25% | 7.41% | 13.34% |
| ROA | 9.47% | 1.64% | -3.69% | 2.49% | 5.58% |

*Sources: DCL*

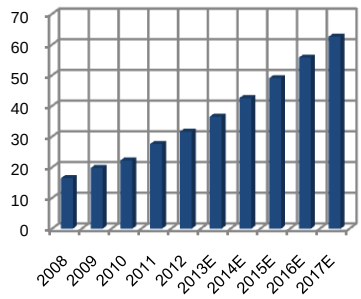
## INDUSTRY OVERVIEW

***Vietnam pharmaceutical market value***




*(Sources: Drug Administration of Vietnam, BMI)*

**Pharmaceutical expenditure per capita *(USD)***




*(Sources: Drug Administration of Vietnam, BMI)*

**Vietnam pharmaceutical market retained a high and stable growth**: Vietnam ranked 13th out of 137 countries having highest pharmaceutical growth in the world. The compound annual growth rate of 2009-2013 is 24.83%. According to BMI, Vietnam market value 2014 was estimated at 80.193 billion dongs, up 15.72% compared to 2013.

**Pharmaceutical expenditure per capita is still low and will continue to increase** creating opportunities for pharmaceutical companies: pharmaceutical expenditure per capita 2012 was USD31.63, lower than other countries in region (in 2011, this figure in Asia was 45USD per capita). BMI forecasted that the expenditure would be around USD62.59 per capita in 2017, corresponding to CAGR of 14.63% from 2012 to 2017 due to the appreciation of income, life expectancy and awareness of health care.

**Domestic producers are less competitive in Vietnam:** Foregin manufaures dominate the market with market share of over 50% in production and of 70% of value. Domestic manufacturers mainly focus on producing generics for common treatment, at low price, lack of specific drugs, still does not update high technology and well production standards. (Only one-third firms have been conforming to the GMP standard). In 2013, Vietnam pharmaceutical imported value was USD1,790 million, an increase of 3.18% compared to 2012.

**Dependence on foreign raw materials**: 90% of raw materials are imported from abroad, mainly from the Chinese, India, Austria, Spain,... because of unstable domestic suppliers and of low manufacturing technology. 11M2013, Vietnam imported USD274.7 million of raw materials, up 14.05% year on year.

**Prescription drug revenue of domestic producers decreased because of joint Circular No. 01/2012/TTLT-BYT-BTC** guilding bidding drugs procurement in the medical facilities**.** The cicular divided the bidding packages into 8 packages. However, domestic manufacturers could not bid on some packages because they did not meet these criteria; they also could not compete with Indian's, Pakistan's, China's companies on price for the other packages. **The joint cicular No. 36/2013/TTLT-BYT-BTC** going into force on January, 1st 2014 amended and supplemented a number of acticles of the joint cicular No. 01/TTLT-BYT-BTC. We expect that the rate of domestic drugs winning will increase because this cicular creates opportunity for domestic companies of high qualify to bid on WHO-GMP, EU-GMP and PIC/s-GMP packages with foreign manufacturers coming from ICH.

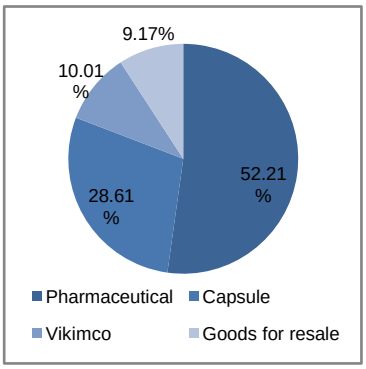
**Price control:** Drug price increases must be approved by the Drug Administration of Vietnam while the raw materials prices subject to global price and to exchange rate fluctuations.

**Domestic pharmaceutical companies are permited to spend 15% of total input cost on advertising and brokage** instead of 10% before. This is the content of the law No. 32/2013/QH13 amending and supplementing a number of acticle of Coporate Income Tax law.

**High barriers to entry:** The companies have to meet GPs requirements, to build strong distribution system and good relationships with pharmacies, hospitals to compete with businesses in sectors.

## COMPANY OVERVIEW

**Revenue breakdown 2013**



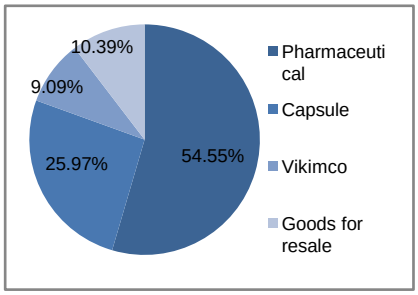

*(Sources: DCL)*

**Biên lợi nhuận gộp các nhóm hàng**

| Products | Design capacity (mil. units per year) | Gross profit margin |
|---|---|---|
| Pharmaceutical | 600 | 30-40% |
| Antibiotics | 1,000 | 20-30% |
| Capsule | 5,000 | 45% |
| Vikimco | 100 | 20% |
| Goods for resale | | 5-8% |

*(Sources: DCL)*

**Revenue plan 2014**




*(Sources: DCL)*

**Company's performance is improved**: In 2011, the company lost nearly 31 billion dongs. Because of effective restructuring, up to Q2/2013, DCL had removed its accumulated losses. In 2013, the firm gained 36 billion dongs, up 86.32% over 2012, in which, its revenue increased 14.27%, its gross margin rose to 29.73% from 27.94%, its interest expense decreased 41% compared to 2012.

**Business plan in 2014:** Its target revenue and net income are 770 billion dongs (up 10.14%) and 42 billion dongs (up 17.67%), respectively. In a prudent manner, we expect its revenue will reach 750 billion dongs of revenue and 42 billion dongs of net income.

DCL's revenue includes 52.21% of pharmaceutical; 28.61% of capsule 10.01% of medical equipment (Vikimco) and 9.17% of goods for resale.

**DCL is the only business own Capsule factory with total capacity of 5 billion units per year.** Capsules has high gross profit margin of 45%. The demand for DCL is high. 30% of drugs which is produced in Vietnam are in hard capsules, in which, there are over 60% capsules imported. Because DCL's capsules have many designs, sizes, easy to print logo or company name and flexible delivery time, it is popular to domestic pharmaceutical firms and its price is higher 10-15% than imported products.

**Prescription drug sale increased:** Prescription drugs account for 30% of pharmaceutical revenue. In 2013, although prescription drug revenue of many pharmaceutical firms decreased under the effect of Joint cicular No. 01/2012/TTLT-BYT-BTC, DCL's prescription drug revenue still rose because of its lower price.

**Effective restructuring:** Since 2012, DCL's leaderships have actively reformed, in which they have mainly focused on sales and marketing strategy, policy for company's receivables and liabilities.

- **Restructuring product portfolio**: Reducing the proportion of goods for resale because of low margins (5-8%), promoting the production and consumption of antibiotics and pharmaceutical (especially for Non-betalactam groups), in long term, increasing the proportion of this group up to 60-70% of revenue, maintaining the output of capsules and Vikimco. The proportion of self-produced goods increased from 81.89% in 2012 to more than 90% in 2013, and is expected to continue increasing in the next years.
- **Focusing on selling policies**: Restructing the organization and operation of departments in specialization, establishing a separate marketing department, chaging packaging designs in order to increase consumption and to raise DCL's brand recognition.
- **Rising accounts receivable turnover**: In the past, accounting department has reponsibilty of money collection. Since the beginning of 2013, salespeople are responsible for collecting money from theirs customers. As a result, short -term receivable account fell from 250 billion dongs in 2012 to 195 billion dongs in 2013, the number of receivable day decreased correspondly from 178 days to 114 days. Q4/2013, the firm is no longer required to make additional provision for doubtful receivable.
- **Reducing debt**: The effective performance and the increase in cash flow supported positively DCL in reducing debt. Compared with 2012, debt

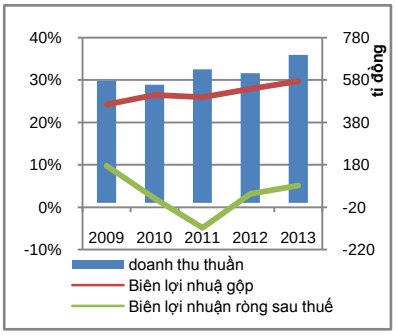
decreased by 21.35% to 252 billion, the company has no long-term debt.

**Risk analysis:**

- **High level of competition**: There are more than 170 domestic pharmaceutical companies producing generic drugs which are duplicated. The foreign enterprises have advantages in brand, quality and a higher discount rate. In addition, the entry of new foreign businesses and opening up the market for foreign manufacturers under WTO and TTP commitment make the market more intense competition.
- **Risk of fluctuations in raw materials price and exchange rate**: The companies imports about 90% of raw material.
- **Interest rate risk**: Debt accounts for over 41% of the total assets of the DCL. By the end of Q4/2013, the company's debt decreased by 21.35%, the company has no long-term debt. In addition, the State Bank has planed to cut interest rates by 1-2% in 2014.

## FINANCIAL ANALYSIS

**Revenue and net income**




*(Sources: DCL)*

In 2013, the DCL's financial situation was improved, in which, its accounts receivable turnover increased, its debt reduced and its profit margin rose rapidly. DCL's performace was also improved.

- **Growth analysis:**

In 2013 the revenue rebounded, increased 14.27% compared to 2012, reached 699 billion dongs. This is a high growth rate after the period of 2009-2012 in which the revenue almost unchanged (with CAGR of 2.06%).

- **Capital and asset structures:**

**DCL's debt downed:** compared with 2012, the debt decreased by 21.35% to 252 billion dongs, the firm has no long-term debt.

**DCL's receivable account and its inventory reclined strongly which improved its financial situation:** Its receivable account and its inventory account decreased by 22.16% and by 31.39%, respectively, because of its renovation in selling policy.

- **Its liquidity was improved**: Its current ratio and its quick ratio rose from 1.1 and 1.06 in 2012 to 1.23 and 1.19 in 2013, respectively.
- **Operational capacity:** Its accounts receivable days and days in inventory went downed from 178 days and 164 days in 2012 to 114 days and 125 days in 2013, respectively. However, they are still higher than DCL's rivals. As we forecaste, DCL's accounts receivable turnover and its inventory turnover will be better due to its positive renovation in selling policy.
- **Profitability**: was improved. Net profit margin increased from -0.89% in 2011 to 3.13% in 2012 and to 5.11% in 2013. In which:

  **Gross profit margin rose** from 27.94% in 2012 to 29.73% in 2013 because of its product restructuring.

  **Interest expense decreased**: by 41% because the debt and interest rate fell**.**

  **However, the selling and administration expense rose** because of its stronger marketing activities, stronger selling policy and its more effective wages, salaries and incentives. We evaluate that they are DCL's positive points.

| Fundermantal ratios | DCL | | | DHT | DBT | LDP | SPM |
|---|---|---|---|---|---|---|---|
| | 2011 | 2012 | 2013 | | | | |
| **Capital sructure** | | | | | | | |
| Debt to equity | 2.27 | 1.67 | 1.15 | 1.27 | 2.67 | 1.31 | 0.67 |
| Total asset to total equity | 3.27 | 2.67 | 2.15 | 2.27 | 3.77 | 2.31 | 1.67 |
| **Asset structure** | | | | | | | |
| Long-term asset to total assets | 0.29 | 34.43% | 34.73% | 21.25% | 15.80% | 17.21% | 42.44% |
| Short- term asset to total assets | 0.71 | 65.57% | 65.27% | 78.75% | 84.20% | 82.79% | 57.56% |
| **Liquidity ratios** | | | | | | | |
| Quick ratios | 1.10 | 1.06 | 1.19 | 0.55 | 0.61 | 0.90 | 2.67 |
| Current ratios | 1.12 | 1.10 | 1.23 | 1.42 | 1.21 | 1.53 | 2.81 |
| **Operational capacity (number of days)** | | | | | | | |
| Accounts receivable days | 186.48 | 177.93 | 114 | 35 | 69 | 38 | 378 |
| Days in inventory | 166.33 | 163.85 | 125 | 89 | 103 | 67 | 40 |
| Accounts payable days | 110.63 | 129.27 | 68 | 46 | 101 | 118 | 58 |
| **Profitable ability** | | | | | | | |
| Gross profit margin | 25.98% | 27.94% | 29.73% | 15.02% | 20.14% | 19.03% | 21.76% |
| ROS | -4.89% | 3.13% | 5.11% | 2.69% | 2.10% | 3.67% | 8.13% |
| ROE | -11.25% | 7.41% | 13.34% | 13.95% | 14.14% | 25.20% | 5.19% |
| ROA | -3.69% | 2.49% | 5.58% | 6.23% | 3.76% | 10.88% | 6.06% |

*(Sources: BSC' collection)*

## INVESTMENT VIEW

| Weighted average cost of capital | |
|---|---|
| Risk free rate | 9.20% |
| Market rate | 16.19% |
| Beta | 0.835 |
| **Cost of equity** | **15.04%** |
| **Cost of debt** | **12.69%** |
| Market value of debt (million dongs) | 251,651 |
| Market value of equity (million dongs) | 324,178 |
| **Weighted average cost of capital** | **12.79%** |

*(Sources: Bloomberg, BSC's collection)*

**Valuation result**

| | Price | Proportion |
|---|---|---|
| **FCFF** | 40,883 | 50% |
| **P/E** | 49,066 | 30% |
| **P/B** | 58,616 | 20% |
| **Price** | **46,900** | |

*(Nguồn: BSC tổng hợp)*

This report use FCFF, P/E and P/B to evaluate the market value of DCL.

**The free cash flow to firm FCFF**

This method is suitable for DCL because it takes in consider the time value of money and the company has large debt and its proportion of debt is reducing.

**We apply FCFF 2 stages**, including: (1) stage 1: from 2014 to 2018, Antibiotics factory was reduced 50% of coporate income tax; (2) stage 2: long–term growth.

- ***Stage 1***:

***DCL's revenue***: we forecast that the CAGR of its revenue is 5.29% during the period of 2013-2018, in which, its revenue in 2014 was estimated at 750 billion dongs, up 7.28% compared to 2013.

**Gross profit margin*:*** is forecasted to rise from 29.73% in 2013 to 31.74**%** because the company has promoted manufacturing and selling products which have high profit margin.

***Net profit margin:*** We predicted that the CAGR of net income is 18.83% during the period of 2013-2018. Net profit margin rise from 5.11% in 2013 to 9.35% in 2018 because of the increase in gross profit margin and the reduce in interest expense. In 2014, the neet income is estimated at 42 billion dongs, euivalent to 4.201 dongs of EPS, up 18.98% over 2013.

***Free cash flow to firm:*** is pedicted to rise by 4.5% of CAGR from 2014 to 2018, in which, its fixed asset consumption and depreciation is forecasted not to have large changes because the company still do not have any expanding plan.

- ***Stage 2***: We expect that the FCFF will rise by 3% in long-term.

***The weighted avegage cost of capital:*** The Cost of Equity was calculated by the

CAPM model, using the 10-year government bond risk-free rate of 9.2%, the expected market return of Vnindex of 16.19% and the adjusted beta of 0.835 collected from Bloomberg to reflect the Cost of Equity of 15.04%. The cost of debt was computed from DCL's financial report of 12.69%. The coprorate income tax is 22% after 2014.

***The estimated price of DCL under this method is 40.883 dongs.***

- **Multiple valuation- P/E**:

The industry P/E is 11.68

EPS 2014 is expected at 4.201 dongs per share.

***The estimated price of DCL under this method is 49.066 dongs.***

- **Multiple valuation-P/B**:

The industry P/B is 2.04

DCL's book value is 27,786 dongs per share.

***The estimated price of DCL under this method is 58.616 dongs***

**Valuation result**

| | Price | Proporion |
|---|---|---|
| **FCFF** | 40,883 | 50% |
| **P/E** | 49,066 | 30% |
| **P/B** | 58,616 | 20% |
| **Price** | **46,900** | |

**Investment points:** DCL is a defensive stock with its beta less than 1, low liquidity so it is suitable for long-term investment. Its performance is improved because of effective restructuring and it is one of a few company that have P/B of 1.1 and P/E of 8. We recommend buying DCL with expected price next 12 months is 46.900 dongs per share.

| Stocks | Market value (million dongs) | Revenue (TTM) | Gross profit margin | Net profit margin | ROA (%) | ROE (%) | P/E | P/B | EV/EBITDA |
|---|---|---|---|---|---|---|---|---|---|
| **DCL** | 324,178 | 652,678,496,256 | 31.01% | 5.71% | 5.56 | 14.49 | 8.74 | 1.17 | 5.81 |
| **DHG** | 8,497,619 | 3,527,357,300,736 | 46.51% | 16.71% | 21.62 | 32.12 | 14.42 | 8.58 | 11.55 |
| **TRA** | 2,146,577 | 1,683,232,423,936 | 42.18% | 9.08% | 15.14 | 27.17 | 15.87 | 3.16 | 8.15 |
| **DMC** | 1,276,929 | 1,429,614,821,376 | 28.83% | 7.43% | 11.62 | 17.74 | 12.02 | 2.04 | 8.19 |
| **IMP** | 918,725 | 842,107,846,656 | 46.24% | 7.13% | 6.94 | 8.33 | 15.41 | 1.27 | 5.46 |
| **DHT** | 162,052 | 669,615,865,856 | 15.02% | 2.69% | 6.23 | 13.95 | 9.01 | 1.24 | 6.31 |
| **DBT** | 81,084 | 580,075,667,456 | 20.14% | 2.10% | 3.76 | 14.14 | 6.54 | 0.91 | 7.94 |
| **OPC** | 784,268 | 563,818,692,608 | 49.37% | 9.98% | 13.20 | 18.13 | 11.68 | 2.04 | 7.25 |
| **LDP** | 190,738 | 462,894,678,016 | 19.03% | 3.67% | 10.88 | 25.20 | 9.60 | 2.55 | 5.85 |
| **SPM** | 330,480 | 447,507,283,968 | 21.76% | 8.13% | 6.06 | 5.19 | 9.56 | 0.48 | 8.56 |
| **PMC** | 447,964 | 357,361,786,880 | 38.98% | 15.60% | 29.86 | 38.05 | 6.80 | 3.06 | 5.29 |
| **PPP** | 37,250 | 101,344,468,992 | 9.63% | -3.86% | 2.14 | 6.57 | 17.62 | 1.95 | 26.39 |
| **Median** | | | | | | | 11.68 | 2.04 | 7.94 |

*(Sources: Bloomberg, BSC's collection)*

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