

Analyst: Anita Hwang

Main Board Listing – Research

United Laboratories International Holdings Limited [Stock Code: 3933]

(聯邦制藥國際控股有限公司)

**Sole Global Coordinator, Bookrunner,
Lead manager and Sponsor**

: HSBC

Sector : Pharmaceuticals

Business : Manufacture and sale of antibiotics products

Total share offer: <u>300,000,000</u> shares (25 % of the enlarged share capital) Public Offer: 30,000,000 shares (10%) Placing: 270,000,000 shares (90%) Greenshoe: 45,000,000 shares Price: HK\$2.25 – HK\$2.75 per share Market Cap: HK\$2,700 – HK\$3,300 million FY06 PER: 11.84X – 14.47X Adjusted NTA per share: HK\$1.59 – HK\$1.71 Staffing: 3,845	<u>Business of United Laboratories</u> United Laboratories principally engages in the manufacture and sale of antibiotics finished products and the bulk medicine and intermediate products used to produce them. It also produces and sells smaller amounts of cough syrup, anti-allergy medicine and capsule casings. According to information published by Southern Medical Economic Research Centre (南方醫藥經濟研究所), United Laboratories ranked amongst the top 20 chemical pharmaceutical industry enterprises (化學製藥工業企業) in the PRC in 2005 in terms of revenue. Key customers of finished products include distributors of pharmaceutical products in the PRC. For sales of intermediate products and bulk medicine outside the PRC, its customers include major pharmaceutical manufacturers and distributors. Three key categories of antibiotics finished products are produced, namely semi-synthetic penicillin, cephalosporins and beta-lactamase inhibitors. These products are mainly used for the treatment of microbial infections including respiratory infections, digestive system infections, urinary system infections and skin and soft tissue infections.
HK Public Offer period: 4 th June 07 – 7 th June 07 noon Receiving bank: HSBC Share registrar: Computershare Hong Kong Investor Services Limited Listing date: 15 th June 2007	

Major Shareholders after Listing (Assuming the over-allotment option is not exercised)

The Choy Family Trust

(a discretionary trust of which the objects include Mrs. Choy, Ms. Choy, Mr. Tsoi and Ms. Shum)

75.0%

Mrs. Choy is the spouse of Mr. Choy Kam Kok, the Chairman and executive director

Ms. Choy Siu Chit, a non-executive director, the daughter of Mr. Choy and Mrs. Choy

Mr. Tsoi Hoi Shan, the son of Mr. Choy and Mrs. Choy

Ms. Shum Fun, the spouse of Mr. Tsoi

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**Use of Proceeds**

Net proceeds from the offer are estimated to be HK\$672.2 million. *(Being the mid-point of the offer price range [HK\$2.50 per share] and assuming the over-allotment option is not exercised)*

	HK\$ million
For expansion and upgrading of production facilities	294.0
For market development and expansion of sales and marketing network	106.9
For strengthening research and development capabilities by setting up additional R&D facilities	73.5
For the partial repayment of two of the outstanding loan facilities	180.4
For general working capital	17.4

Financial Highlights

HK\$ million	Year ended 31 Dec		
	2004	2005	2006
Revenue	1,200.1	1,720.4	2,080.5
Gross profit	398.5	599.8	736.3
EBITDA	282.2	337.7	501.3
Operating profit	176.3	175.5	221.8
Net profit	149.4	132.9	173.8
Gross margin	33.2%	34.9%	35.4%
Operating margin	14.7%	10.2%	10.7%
Net margin	12.4%	7.7%	8.4%

Revenue Breakdown by business activities (% of Total revenue)

Year ended 31 Dec	2004		2005		2006	
	HK\$ million	%	HK\$ million	%	HK\$ million	%
Intermediate products	0.0	-	53.9	3.1	197.4	9.5
Bulk medicine	639.9	53.3	896.4	52.1	1,077.3	51.8
Finished products and capsule casings	560.2	46.7	770.1	44.8	805.8	38.7
Total	1,200.1	100.0	1,720.4	100.0	2,080.5	100.0

Strengths/Opportunities

- ✓ United Laboratories has vertically integrated production operation that supplies the intermediate products required for its mid-stream production of bulk medicine. This should allow the company to enjoy the benefits of lower production costs and better quality control.
- ✓ United Laboratories did not give profit forecast for FY07. Based on the offer price range and FY06 EPS, the historic PER is 11.84X – 14.47X. Several close peers engaged in similar business (bulk medicine and intermediate products) include China Pharmaceutical (1093), Lijun International Pharmaceutical (2005), Dawnray Pharmaceutical (2348) and Wuyi Pharmaceutical (1889). The average FY06 PER is 23X but at a wide range from 9X to over 50X. China Pharmaceutical is the most direct comparable in terms of product mix, but it trails United Laboratories in profit margins. In all, the valuation of United Laboratories is attractive.



Weaknesses/Threats

- × **Pricing of products:** The Government has imposed price control on all medicine listed in the Insurance Catalogue by fixing a retail ceiling price for each product. The price control has been on a wide range of pharmaceutical products, with antibiotics finished products being one of the key targets. The intention is to reduce irregularities in pricing medicinal products in China and to make health expenses more affordable to the public. There have been over 20 price adjustments for various categories of drugs since 1998.

During the Track Record Period, the PRC Government reduced the prescribed retail ceiling prices of a wide range of products that were subject to government-mandated price controls on three occasions.

Sales of United Laboratories' finished products whose retail ceiling prices were reduced accounted for approximately 24.8%, 2.1% and 12.3% of the total turnover in the 3 years ended 31 December 2004, 2005 and 2006, respectively. Any further reduction in the price ceilings would pose high risk in increasing the volatility in revenue of United Laboratories.

- × Generic antibiotics products are generally less-differentiated homogenous products. Price sensitivity of consumers in the PRC is general high. If the products are not included in the Insurance Catalogue, consumers may not be able to get reimbursement. The company's turnover and financial performance may be adversely affected if the existing or new products are not included in the Insurance Catalogue.

Recommendation: Trading Buy



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