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UPDATES & IDEAS

• One clue to the growth potential still up ahead for **Hutchison China Meditech** (HCM;245p) is the fact that in the last two decades the disposable income of China's urban and rural residents grew close to 20 times. With that has come a demand for better medicines but the problem has been that average medical costs during this time has soared more than 130 times.

In April '09, the Chinese government launched their three-year plan for medical reform which is intended to provide access to essential health care for everyone in China by 2020 and followed this up in August with their "essential medicines list" of 307 medicines - those that satisfy priority health needs and which are to be shortly made available to 30% of state-owned healthcare institutions.

HCM has found itself with 17 of its drugs on the list. Even if the majority of these are generic drugs (that are manufactured by multiple manufacturers in China) and the government are now intending to use the list as a mechanism for price control, it is clearly good news for HCM, which has been growing very quickly anyway.

Although still small, at a market cap of £125m, Hutchison has powerful backers in the form of Hutchison Whampoa, which in turn is owned by Asia's richest man, Li Ka Shing.

The largest part of the business – US\$102m of the US\$111m sales in the year to 31 December – is the sale of such prescription and over the counter drugs. Much of what the company does is based on traditional Chinese medicines, or botanicals, which the company says has an advantage over new western drugs because their use for hundreds of years suggests they are both effective and safe. But the drugs tend to be complex, each involving up to six active compounds and many western doctors are skeptical. The two main ones are *She Xiang Bao Xin*, which are pills for treating cardiovascular conditions (50% of group sales) and *Dan Ning tablets*, for gallbladder conditions (8%). Sales of each grew by 41% and 29% respectively. Alongside that there are also a range of OTC medicines such as *Fu Fu Dan Shen* (angina) and

Ban Lan Gen (colds), which are amongst the top OTC brands in China.

In addition, HCM has been using the cash from prescription products to develop proprietary drugs, the main one being *HMPL-004*, based on a Chinese herb to treat Crohn's disease and ulcerative colitis. Trials are presently in phase 2.

There is a third business involved in rolling out health shops in fashionable parts of London under the Sen brand as well as distributing infant nutritional products in China. Both these are small but making progress.

HCM's profitability is being suppressed by the R&D side so it is expected to be only marginally profitable this year but the business looks exciting. *One to watch.*