

June 9, 2014 Company Report Rating: BUY TP: HK\$ 1.84

Share price (HK\$)	1.40
Est. share price return	31.43%
Est. dividend yield	-
Est. total return	31.43%

Previous Rating & TP	(Initiation)
Previous Report Date	N/A

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Key Data

52Wk H/L (HK\$)	2.71 / 1.23
Issued shares (mn)	3,909
Market cap (HK\$ mn)	5,473
3-mth avg daily turnover (HK\$ mn)	18.9
Major shareholder(s):	
Zhao Hongliang	34.12
Mengniu Group	4.41

Source(s): Company, Bloomberg, ABCI Securities

Key operating data in 2013

Number of dairy cows (head)	40,396
Milkable cows	21,544
Calves and heifers	18,852
Total sales volume (tonnes)	183,702
Milk yield (tonnes)	9.0
Average selling price (RMB / kg)	4.79

Source(s): Company, ABCI Securities

Share performance (%)

	Absolute	Relative*
1-mth	3.73	(1.25)
3-mth	(23.20)	(24.62)
6-mth	(44.62)	(43.12)

*Relative to HSI

Source(s): Bloomberg, ABCI Securities

Stock performance



Source(s): Bloomberg, ABCI Securities

YST Dairy (1431 HK)

A rising star in China's dairy industry

YST Dairy is one of the leading raw milk producers with large-scale dairy farms (individual herd sizes in 3 out of the 4 existing dairy farms exceed 10,000 head). Under the highly fragmented dairy farming industry in China (~5% of raw milk production volume comes from large dairy farms with herd sizes of over 5,000 dairy cows), YST Dairy, as a large dairy farmer, is able to charge a premium for its quality products based on the economies of scale and advanced farm management techniques. Furthermore, the market consolidation underway encouraged by the Chinese government would enable YST Dairy to gain additional market share. Recent dumping of dairy stocks triggered by the weak domestic milk prices has provided a good opportunity for investors to accumulate. The counter is trading at book value and we believe its valuation is undemanding. Initiate BUY with TP at HK\$ 1.84

Strong dairy farming know-how. YST Dairy has a better milk yield compared to its HK-listed peers and the national average in China. In 2013, its average milk yield was 9.0 tonnes (5.88% higher than Modern Dairy; 4.65% higher than Huishan Dairy; and 63.64% higher than the average of dairy farms in China) The figure reflects the Group's superior breeding and farm management skills. As its existing dairy farms in operation and under construction (except the one for educational use) are large in scale with individual capacities of over 6,000 cows, we believe the Group would be able to maintain its high milk yield in the future.

Premium product quality. The Group is able to charge a premium for raw milk due to its finer quality. It supplies premium raw milk to leading dairy products manufacturers, such as Mengniu Group and Feihe Dairy Group, for the production of high-end products, e.g. Mengniu's Milk Deluxe (特仑苏) and Feihe's AstroBaby (星飞帆). In 2013, the ASP of the Group was RMB 4,795 per tonne, 32.73% higher than the raw milk ASP in China during the year.

Strong growth in premium milk market expected in China. Due to the growing health awareness among the public and surging household income, it is expected the premium milk market will expand at 17.5% CAGR over 2012-17E. Moreover, we expect large dairy farmers would gain additional market share by eliminating the small players as the market consolidation continues. All these would benefit the Group in the future.

Initiate with BUY with TP at HK\$1.84. Our target valuation at 13.94x of FY14E P/E reflects a 20% discount to the lower quartile of Modern Dairy's historical P/E since 2012. The discount is justified by its relatively shorter listing history and lower ROAE compared to those of Modern Dairy. Based on the Group's expansion plan and the growth in downstream premium liquid milk market, we estimate net income to surge by 90.67% YoY to RMB 415mn in FY14E, translating into an EPS of RMB 0.106 (HK\$ 0.131). Initiate BUY on YST Dairy with TP at HK\$ 1.84

Risk factors: 1) High customer concentration; 2) Animal risk arising from outbreak of disease epidemic; 3) Fluctuation in beef price affecting the raw milk price; 4) Fluctuation in fair value gain or loss of biological assets; 5) No dividend payout record.

Results and Valuation

FY ended Dec 31	2012A	2013A	2014E	2015E	2016E
Revenue (RMB mn)	689	881	1,160	1,692	2,463
Chg (% YoY)	363.16	27.81	31.67	45.92	45.54
Net Income (RMB mn)	210	218	415	600	874
Chg (% YoY)	10.48	3.81	90.67	44.45	45.67
EPS (RMB)	0.054	0.056	0.106	0.153	0.223
P/E (x)	-	20.27	10.63	7.36	5.05
BVPS (RMB)	0.151	1.001	1.107	1.260	1.484
P/B (x)	-	1.13	1.02	0.90	0.76
DPS (RMB)	-	-	-	-	-
Yield (%)	-	-	-	-	-
ROAE (%)	43.19	9.67	10.08	12.96	16.29
Net gearing (%)	77.43	Net Cash	Net Cash	Net Cash	Net Cash

*Net gearing=Net debt/Total equity

Source(s): Bloomberg, ABCI Securities estimates

Valuation analysis

In our evaluation of YST Dairy, we apply the comparative valuation method with reference to the market valuation of Modern Dairy because of their similarities in revenue composition. YST Dairy's business mainly focuses on the upstream raw milk farming with all of its revenue coming from raw milk sales, while ~90% Modern Dairy's revenue was contributed by its upstream raw milk production in FY13.

Market valuation of Modern Dairy

Modern Dairy is trading at 14.90x FY14E P/E, below the lower quartile of its historical P/E since 2012 at 17.42x. We believe the undemanding valuation primarily reflects the concern on tumbling raw milk selling price in 2014 after it had rallied by over 25% in 2013. According to weekly survey of raw milk prices by the Ministry of Agriculture, raw milk ASP among 10 major raw milk production provinces, including Inner Mongolia, Heilongjiang, Xinjiang, etc., has been declining since Feb 2014.

Since milk yield usually peaks in spring, hence we expect raw milk prices to stay weak on the increased supply in short run. However, if demand for raw milk remains at recent levels, raw milk price is likely to stabilize when milk yield falls in summer, the conventionally low-yield season. We believe the market sentiment would improve by then.

BUY YST Dairy, but should be in discount with Modern Dairy

Valuation of dairy sector should be bottoming out since milk price is expected to stabilize. Our target P/E for YST Dairy at 13.94x represents a 20% discount to the lower quartile of Modern Dairy's historical P/E since 2012 (the previous dairy cycle). We believe the YST Dairy's discount to Modern Dairy is justified based on the following factors:

1. A relatively short listing history. YST Dairy has been listed since Nov 2013, while Modern Dairy has been listed since Nov 2010.
2. A lower return ratio. FY14E ROAE for YST Dairy is 10.08%, vs. Modern Dairy's 15.13%.

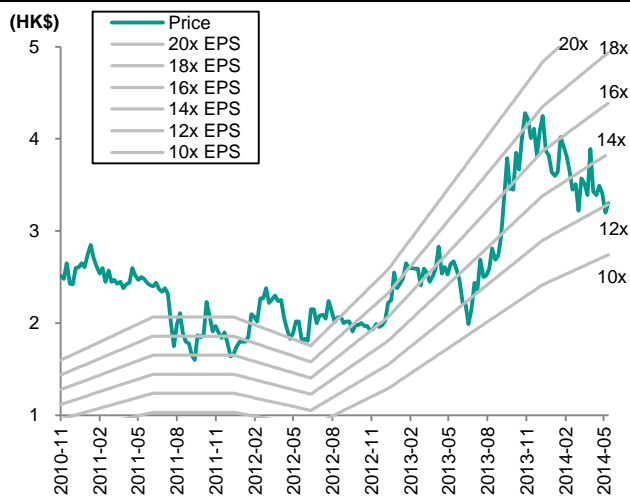
Based on the target FY14E P/E, we initiate our coverage on YST with a **BUY** rating with TP at HK\$ 1.84, representing an upside of 31.43% from the current trading price.

Sector valuation

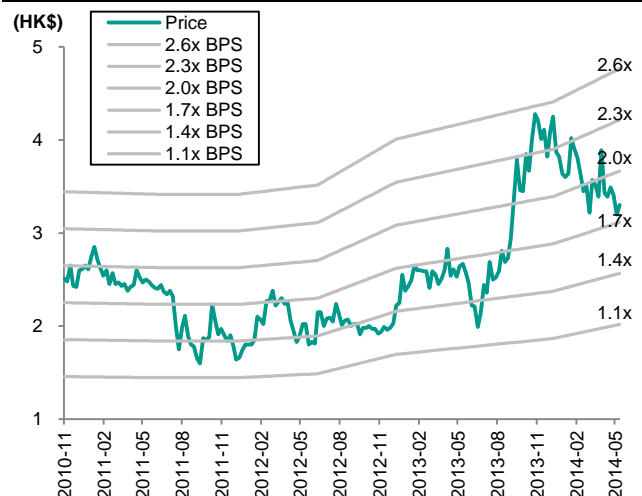
Exhibit 1: Peer valuation table for F&B sector & dairy industries

Company	Ticker	Mkt cap (HK\$ mn)	As of 6/6/2014 CRY	Share Price	P/E (x)		EPS (%YoY)		P/B (x)		ROAE (%)	
					FY14E	FY15E	FY14E	FY15E	FY14E	FY15E	FY14E	FY15E
Large-cap F&B stocks in Hang Seng Index												
WANT WANT CHINA	151 HK	137,407	HKD	10.40	23.13	19.73	11.54	17.24	7.89	6.74	36.95	37.26
TINGYI	322 HK	121,742	HKD	21.75	29.53	24.40	30.14	21.05	4.96	4.45	16.02	16.59
CHINA MENGNIU DA	2319 HK	73,331	HKD	37.45	27.31	21.79	22.79	25.41	3.00	2.67	12.00	12.40
CHINA RES ENTERP	291 HK	51,206	HKD	21.30	28.10	23.77	(4.05)	18.21	1.11	1.06	3.50	3.57
Sector Weighted Average					26.62	22.14	17.51	20.14	5.12	4.48	21.08	21.46
HK-listed dairy stocks												
CHINA MENGNIU DA	2319 HK	73,331	HKD	37.45	27.31	21.79	22.79	25.41	3.00	2.67	12.00	12.40
HUIZHAN DAIRY	6863 HK	26,510	HKD	1.84	15.96	11.41	39.68	38.30	1.56	1.39	13.71	13.44
CHINA MODERN DAI	1117 HK	16,316	HKD	3.38	14.90	11.31	91.16	31.72	1.98	1.69	15.13	16.94
YUANSHENGTAI DAI	1431 HK	5,473	HKD	1.40	10.63	7.36	90.67	44.45	1.02	0.90	10.08	12.96
BIOSTIME INTERNA	1112 HK	29,549	HKD	48.95	21.30	17.08	35.26	24.72	8.01	6.58	45.21	52.35
YASHILI INTERNAT	1230 HK	10,927	HKD	3.07	17.56	14.07	19.51	27.89	2.66	2.46	15.67	18.15
Sector Weighted Average					21.89	17.17	36.78	28.83	3.48	3.00	18.83	20.71
A-share market dairy stocks												
INNER MONG YIL-A	600887 CH	80,963	RMB	31.95	17.61	14.39	9.94	22.44	3.48	2.88	21.91	22.64
BRIGHT DAIRY-A	600597 CH	25,031	RMB	16.48	30.24	21.51	65.15	40.55	4.28	3.75	15.00	18.57
GUANGXI ROYAL-A	002329 CH	4,197	RMB	15.81	57.70	41.39	44.12	37.96	4.14	3.86	6.03	8.31
BEINGMATE BABY-A	002570 CH	16,679	RMB	13.15	16.71	13.66	11.43	22.36	2.95	2.55	17.87	19.31
Sector Weighted Average					21.31	16.59	22.16	26.51	3.59	3.04	19.49	20.93
International dairy product producers with business in China												
NESTLE SA-REG	NESN VX	1,927,517	CHF	68.85	19.77	18.45	11.08	7.17	3.24	3.14	16.68	16.36
ABBOTT LABS	ABT US	467,504	USD	40.15	18.13	16.10	34.70	12.58	2.47	2.30	13.74	15.06
DANONE	BN FP	364,917	EUR	53.68	19.56	17.74	14.50	10.21	2.65	2.51	14.30	14.45
MEAD JOHNSON	MJN US	139,447	USD	89.00	24.24	21.70	15.78	11.74	29.03	17.91	158.40	100.54
FONTERRA-SHAR FD	FSF NZ	62,833	NZD	5.95	41.82	20.27	(67.50)	106.29	1.61	1.56	3.61	7.18
Sector Weighted Average					20.16	18.18	13.79	10.72	4.23	3.59	22.32	19.69
Overall Weighted Average					20.96	18.50	15.50	13.07	4.26	3.64	21.93	19.96

Source(s): Bloomberg, ABCI Securities estimates

Exhibit 2: Historical forward P/E of Modern Dairy in Nov 2010 – Jun 2014


Source(s): Bloomberg, ABCI Securities

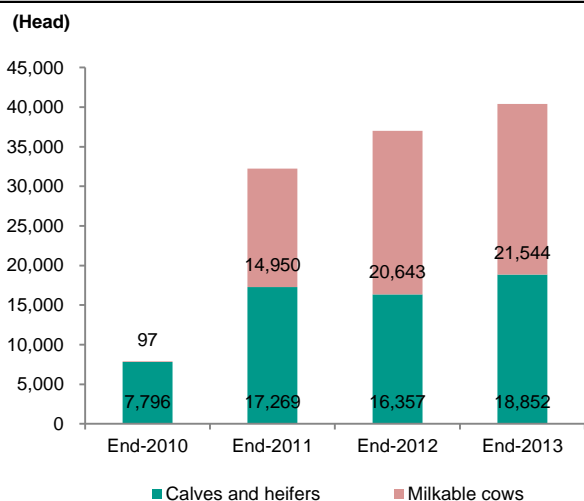
Exhibit 3: Historical forward P/B of Modern Dairy in Nov 2010 – Jun 2014


Source(s): Bloomberg, ABCI Securities

Strong dairy farming know-how

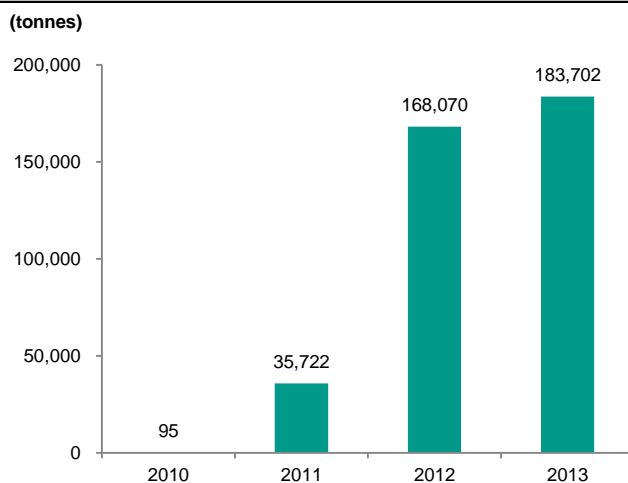
We see the factor of know-how, which is the technical skills and practical knowledge required to do something correctly, is crucial in differentiating the winners from the losers in the dairy industry. YST's dairy cows have the highest milk yield (9.0 tonnes p.a./milkable cow) among the HK-listed raw milk producers. Its number of milkable cows grew 4.36% YoY to 21,544 at end-2013 while raw milk sales volume was up 9.30% YoY to 183,702 tonnes. Milk yield is expected to improve further on a more balanced age group of the herd and more self-breed dairy cows become milkable.

Exhibit 4: Number of dairy cow of the Group, at end-2010 to end-2013



Source(s): The Company, ABCI Securities

Exhibit 5: Sales volume of raw milk of YST Dairy, FY10-13



Source(s): The Company, ABCI Securities

The average milk yield per cow was substantially influenced by the herd structure. The increases in the percentage of dry cows (milkable cows that are in the 60-day dry period of a 400-day lactation cycle during which they do not produce any raw milk) lowered the average milk yield per cow during FY10-12. However, with percentage of milking cow rose in FY13, milk yield edged up from 8.9 tonnes in FY12 to 9.0 tonnes in FY13. Furthermore, with a larger number of milkable cows going into the 3rd and 4th lactation during which the milkable cows are expected to increase their raw milk production, we expect the overall milk yield of YST Dairy to rise further in 2014-15.

Exhibit 6: Number of dairy cow of the Group at end-2010 to end-2013

	FY10	FY11	FY12	FY13
Number of milkable cow at period-end (head)	97	14,950	20,643	21,544
Effective milking cow during the period (head)	9	3,883	18,884	20,411
Sales volume of raw milk (tonnes)	95	35,722	168,070	183,702
Milk yield (tonnes/head)	10.7	9.2	8.9	9.0

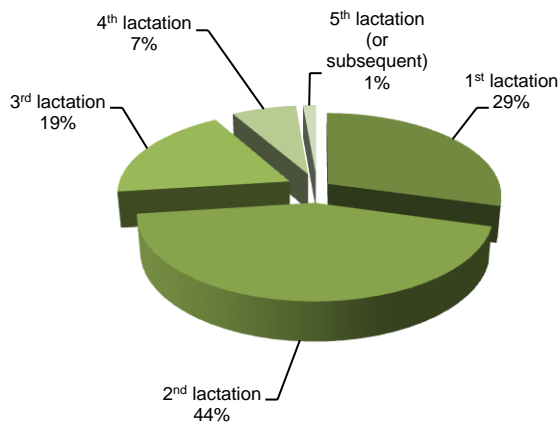
Source(s): The Company, ABCI Securities

Higher milk yield than peers

The Group had a better milk yield than its HK-listed peers and the national average in China. Average milk yield in 2013 was 9.0 tonnes for the Group, higher than Modern Dairy's 8.5 tonnes. The milk yield of Huishan Dairy during the 6 months ended on 30 Sep, 2013 was 8.6 tonnes, and the average milk yield, in China in 2012 was 5.5 tonnes according to China Dairy Yearbook.

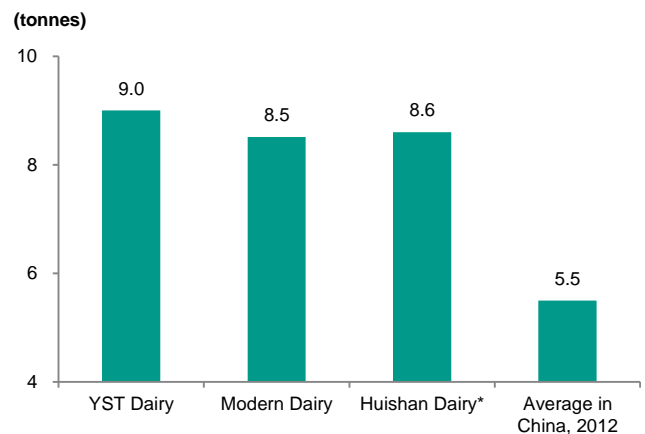
We believe YST Dairy's milk yield was higher because of its standardized operating procedures and management expertise in operating their large farms. As of 31 Dec 2013, the Group owned four large farms located in Heilongjiang and Jilin of China. The designed capacity of the farms ranges from 6,000 - 18,000 head of dairy cows. Currently, the raw milk industry is dominated by small dairy farms with less than 1,000 head of dairy cows. Based on its economics of scale and standardized operating management, we believe YST Dairy's relatively higher efficiency will continue to support its milk yield will sustain in the future.

Exhibit 7: Breakdown of milkable cows of YST Dairy by lactation cycle, FY13



Source(s): The Company, ABCI Securities

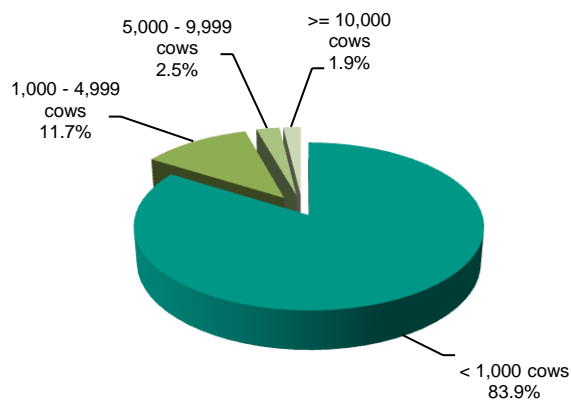
Exhibit 8: Milk yield comparison on YST Dairy and peers'



*: The milk yield of Huishan Dairy during the six months ended on 30 September

Source(s): The Companies, China Dairy Yearbook, ABCI Securities

Exhibit 9: Production of raw milk in China by size of dairy farm, 2012

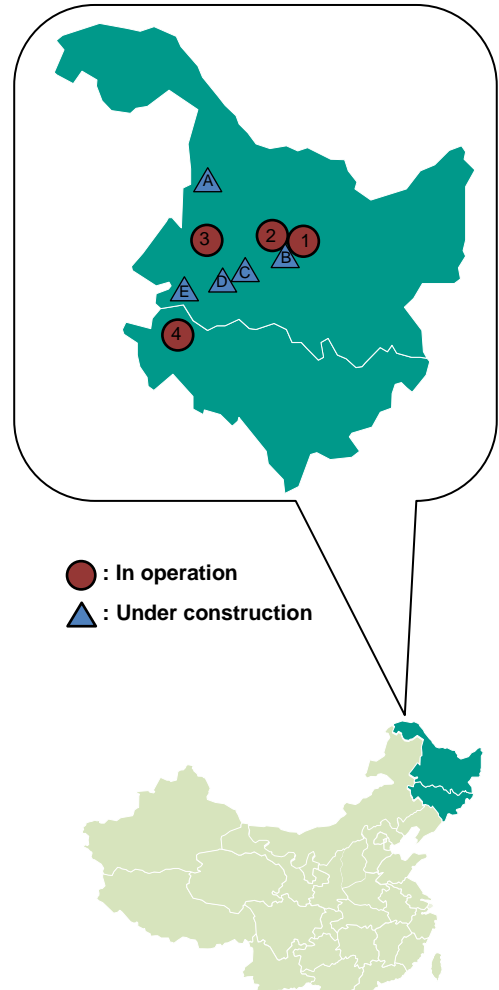


Source(s): Euromonitor International, ABCI Securities

Exhibit 10: Dairy farms of YST Dairy

- 1. Kedong YST Farm:**
Designed Capacity: 18,000 heads of dairy cow
Site area: 784,333 m²
- 2. Kedong Oumei Farm:**
Designed Capacity: 6,000 heads of dairy cow
Site area: 384,000 m²
- 3. Gannan Oumei Farm:**
Designed Capacity: 12,000 heads of dairy cow
Site area: 986,333 m²
- 4. Zhenlai Farm Phase I:**
Designed Capacity: 15,000 heads of dairy cow
Site area: 1,066,667 m²

- A. Baiquan (under construction):**
Designed Capacity: 15,000 heads of dairy cow
Site area: 994,000 m²
Expected completion: 2Q15
- B. Kedong Yongjin Farm (under construction):**
Designed Capacity: 12,000 heads of dairy cow
Site area: 714,000 m²
Expected completion: 4Q14
- C. Honghai Farm (under construction):**
Designed Capacity: 15,000 heads of dairy cow
Site area: 1,000,000 m²
Expected completion: 4Q15
- D. Sifang Farm (under construction):**
Designed Capacity: 15,000 heads of dairy cow
Site area: 673,333 m²
Expected completion: 4Q15
- E. Teifeng Farm (under construction):**
Designed Capacity: 400 heads of dairy cow
Site area: 200,010 m²
Expected completion: 4Q14
(It is for education tours)



All of the dairy farms the Group owns and in operation are located within the Songnen Plain (松嫩平原), comprised of parts of Heilongjiang and Jilin, the two most northeastern provinces in China.

Source(s): The Company, ABCI Securities

YST Dairy plans to build 5 additional farms in the Songnen Plain by 2016, including one for education and tourism, one for raising reserve cows and 3 for commercial production. It aims to attain a total herd size of 100,000 in 2017. Based on our projection, its herd size would reach 100,000 by 2016E- a year earlier than its targeted time frame.

High quality products

The Group is able to charge a premium for raw milk due to its quality. It supplies premium raw milk to leading dairy products manufacturers, such as Mengniu Group and Feihe Dairy Group for their high-end products, named Milk Deluxe (特仑苏) and AstroBaby (星飞帆), respectively.

According to Euromonitor International, the raw milk produced by YST Dairy is of the highest quality in China's dairy market by safety standard (measured by microbe and somatic cells) and nutritional standard (measured by the level of protein and fat). Thanks to the advanced breeding techniques and dairy farm management, we believe the Group would be able to maintain its premium quality in the future.

Exhibit 11: Key quality indicators of raw milk in each dairy farm in 2013

	Gannan Oumei Farm	Kedong Oumei Farm	Kedong YST Farm	Zhenlai Farm Phase I
Safety Standard (CFU/mL)				
Microbe count	2,300	2,100	2,600	3,100
Somatic Cell Count	119,000	126,000	143,000	164,000
Nutritional Standard (%)				
Protein	3.8	3.6	3.5	3.4
Fat	4.8	4.5	4.3	4.3

Source(s): The Company, ABCI Securities

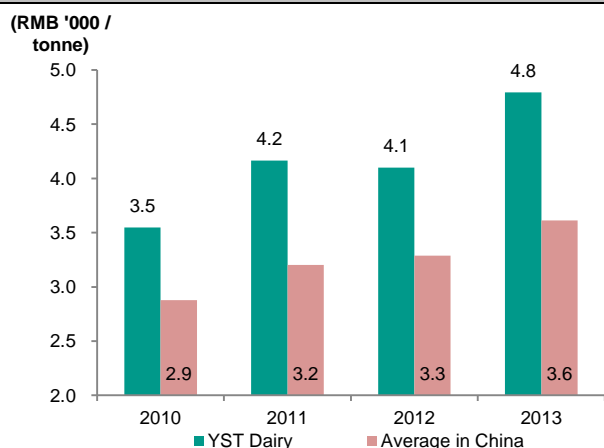
Exhibit 12: Key quality indicators of raw milk by domestic and international standards

	PRC Standard	E.U. Standard	U.S. Standard
Safety Standard (CFU/mL)			
Microbe count	$\leq 2,000,000$	$< 100,000$	$< 100,000$
Somatic Cell Count	N/A	$< 400,000$	$< 750,000$
Nutritional Standard (%)			
Protein	≥ 2.8	N/A	≥ 3.2
Fat	≥ 3.1	N/A	≥ 3.5

Source(s): Ministry of Health of the PRC, EUR-Lex, a database of EU Law and Euromonitor International, YST's Prospectus, ABCI Securities

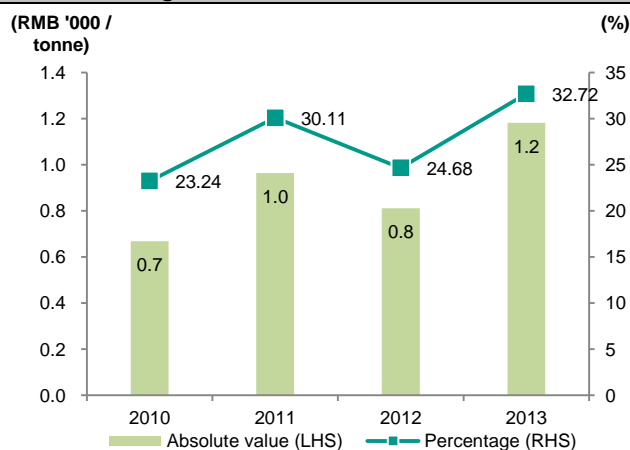
In 2013, the average selling price of the Group was RMB 4,795 per tonne, 32.73% higher than the average price of raw milk in China during the year.

Exhibit 13: Raw milk ASP of YST Dairy and China in 2010-13



Source(s): The Company, Ministry of Agriculture, ABCI Securities

Exhibit 14: Price Premium of YST Dairy's raw milk to China's average in 2010-13

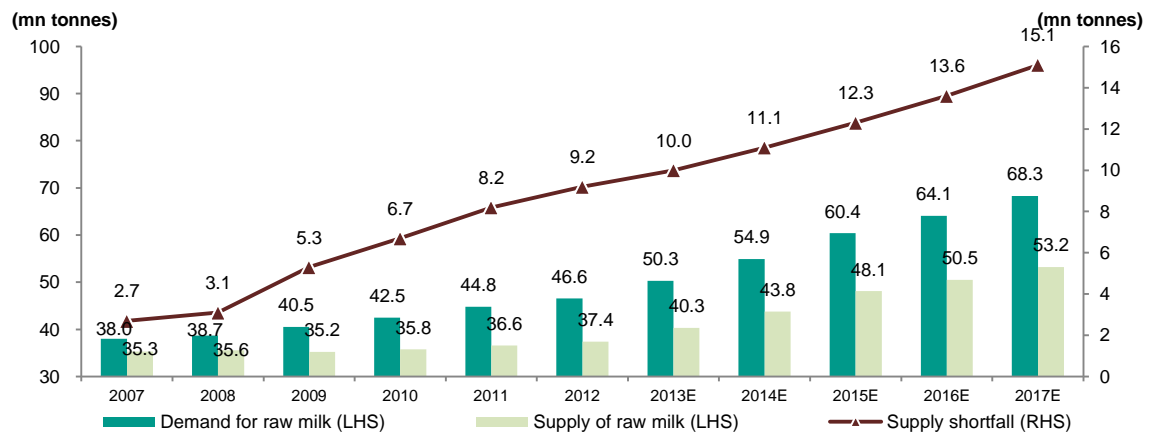


Source(s): The Company, Ministry of Agriculture, ABCI Securities

Earnings outlook

China's raw milk demand increased at a 4.2% CAGR o from 38.0mn tonnes in 2007 to 46.6mn tonnes in 2012. As growth in raw milk supply lags behind that of the demand, the supply shortfall widened from 2.7mn tonnes in 2007 to 9.2mn tonnes in 2012. It is expected that the supply shortfall would reach 15.1mn tonnes in 2017. The increasing divergence between demand and supply is beneficial to the entire dairy farming industry.

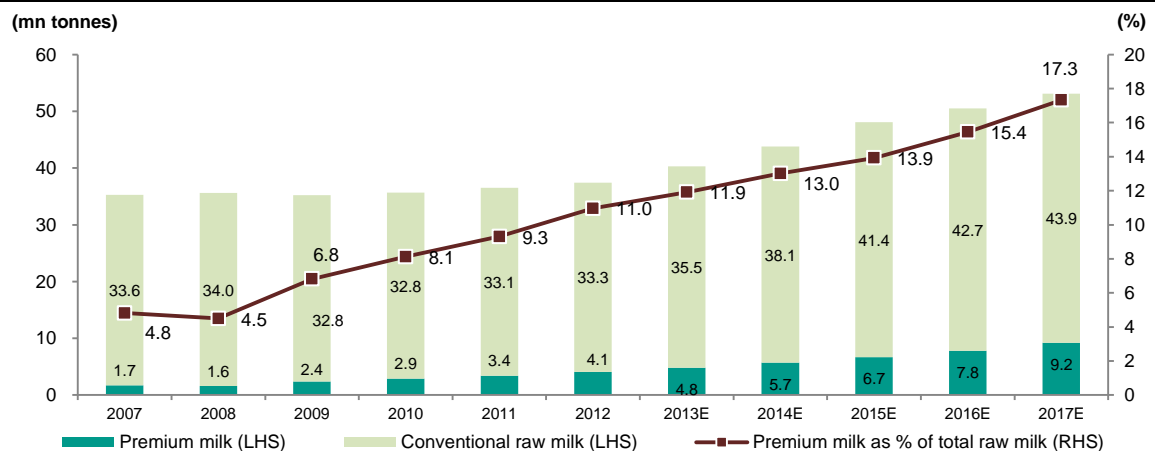
Exhibit 15: Demand for and supply of raw milk in China, 2007-17E



Source(s): Prospectus of Huishan Dairy, NBS, ABCI Securities

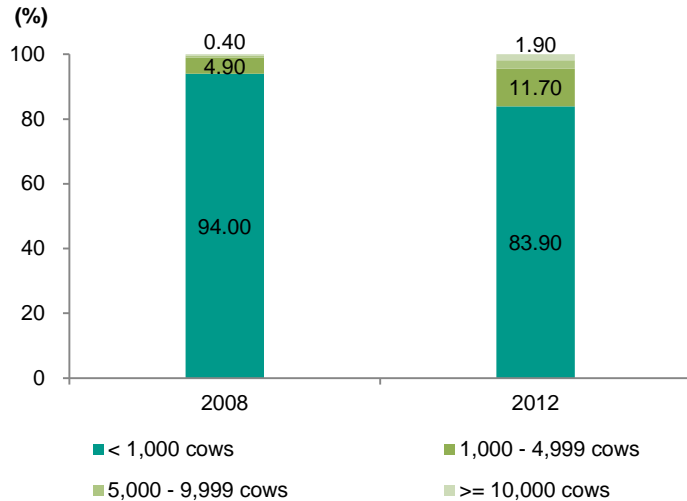
Furthermore, driven by the growing health awareness among the public and surging household income over the past few years, demand growth for premium milk outpaced that of the raw milk. Production volume of premium milk grew at 19.25% CAGR from 1.7mn tonnes in 2007 to 4.1mn tonnes in 2012. The growth of demand is expected to stay high over 2012-17. It is expected that the production volume of premium milk is estimated to increase at 17.54% CAGR from 4.1mn tonnes in 2012 to 9.2mn tonnes in 2017, which is beneficial to premium milk producers.

Exhibit 16: Production volume of premium milk and conventional raw milk in China, 2007-17E



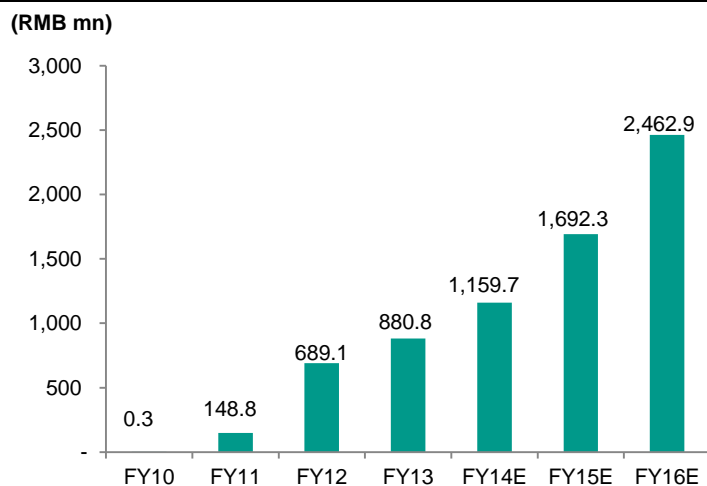
Source(s): Prospectus of Huishan Dairy, NBS, ABCI Securities

Based on its advanced dairy farm management and premium dairy cow breeds generating premium raw milk, we expect the Group, as one of the leading premium milk players, can capture the growth of sector more fully than its peers. Moreover, under the market consolidation, the large dairy farmers can earn an extra growth from eliminating the small players.

Exhibit 17: Breakdown of dairy farms in China by herd size, 2008 and 2012


Source(s): Euromonitor International, ABCI Securities

The Group's revenue jumped from RMB 0.3mn in 2010 to RMB 881mn in 2013. Looking forward, based on the growing downstream liquid milk industry and its expanding herd size, we expect the Group's revenue to increase to RMB 2,463mn in 2016E, representing a 40.88% CAGR over 2013-16E.

Exhibit 18: Revenue of YST Dairy in FY10-16E


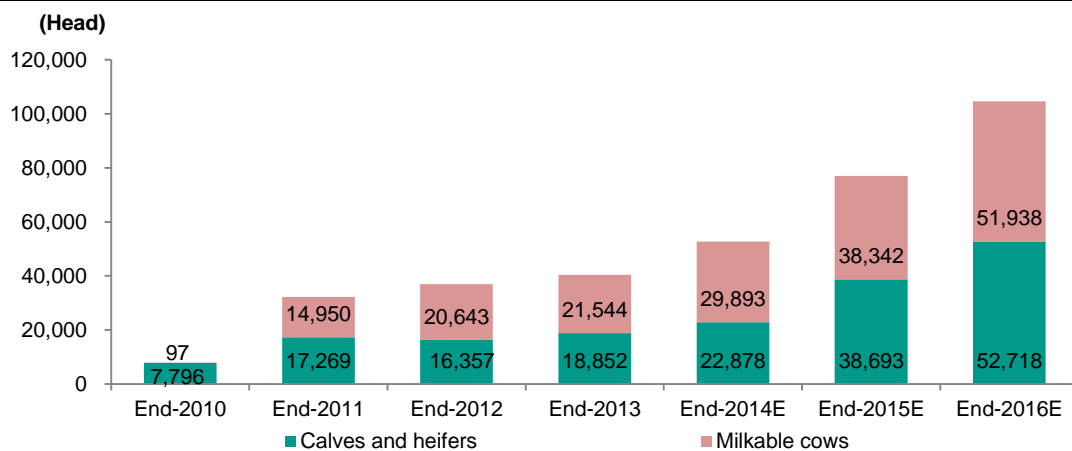
Source(s): The Company, ABCI Securities estimates

Growth in herd size

We expect the herd size of YST Dairy to surge in FY14E-16E after its capital has been fueled by its IPO proceeds of HK\$ 2.56bn in 2013. The Group would invest HK\$ 1.97bn (or 75% of the net proceeds from IPO) on construction of new dairy farms. According to the Group's plan, five new dairy farms would be completed by 2017, and 20,000 heifers would be procured from third parties to expand its herd size.

We estimate that the number of milkable cow would increase from 21,544 at end-2013 to 51,938 heads at end-2016E, and the total herd size would increase from 40,396 at end-2013 to 104,656 at end-2016.

Exhibit 19: Milkable cows of YST Dairy at period-end (2010-16E)



Source(s): The Company, ABCI Securities estimates

Positive surprise may come from demand for milk beverage

Raw milk demand may be boosted by the unexpected growth in demand for milk beverage products. In general, raw milk demand is largely determined by the liquid milk production industry.

Liquid milk products include white milk, flavored milk drinks and yogurt. However, the market may have underestimated the raw milk demand by the milk beverage industry. Milk beverage products is a new product segment that has been growing rapidly in the recent years.

So far, liquid milk market in China is dominated by Mengniu Dairy, Yili Dairy and Bright Dairy. Whereas the local milk beverage market is dominated by Wa Ha Ha, Want Want, Uni-President. The financial statements of Want Want indicate its milk beverage products segment has been growing in a fast lane for the last several years.

However, due to lack of information to quantify the growth driven by the milk beverage sector, our earnings projections for YST Dairy do not include such positive factor.

Profitability and net profit projections

Exhibit 20: Breakdown of cost of sales

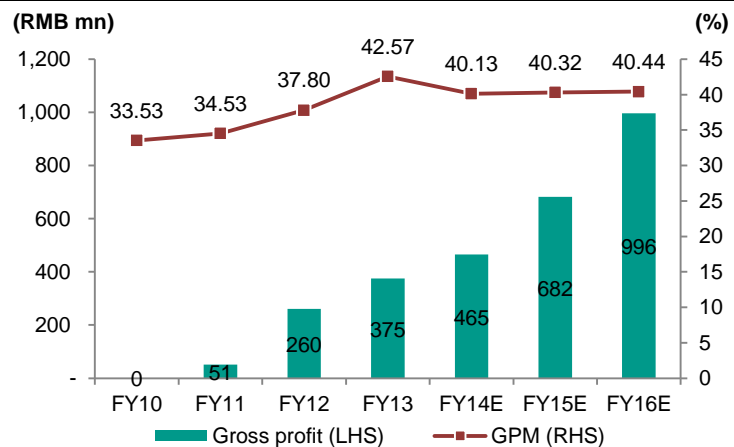
	(RMB mn)	FY12 (%)	(RMB mn)	FY13 (%)
Feed	339	79.17	395	78.06
Staff cost	18	4.12	23	4.51
Depreciation	23	5.46	33	6.54
Veterinary cost	13	3.10	16	3.15
Utility	19	4.52	20	3.87
Other costs	16	3.64	20	3.87
Total	429	100.00	506	100.00

Based on our sensitivity analysis, for a 10% increase (decrease) in average feeding cost, net profit would decrease (increase) by 18% FY13.

Source(s): The Company, ABCI Securities

Expected growth in feeding cost

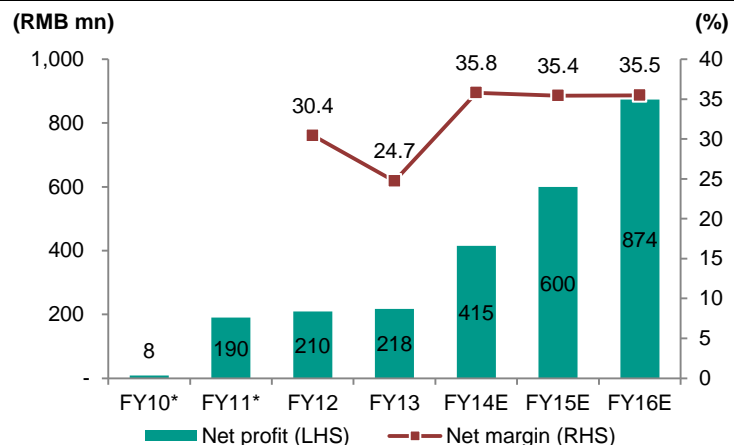
The breeding cost of the Group for milkable cow was RMB 395mn in FY13. We estimate that the average daily breeding cost for milkable cow was RMB 51.29 during the period. In order to maintain the nutrition quality of the raw milk, we expect the daily breeding cost to increase to RMB 60 in FY14, which will narrow the Group's profit margin in the short term. Thanks to the higher ASP for premium milk, the Group's GMP is expected to be higher than peers.

Exhibit 21: Gross profit and GPM of YST Dairy in FY10-16E


Source(s): The Company, ABCI Securities estimates

Gearing improvement

Thanks to the IPO in 4Q13, the Group is currently in a net cash position as compared to a net gearing of 77.43% at end-2012. With the improved gearing in 2014, we expect interest expenses to reduce from RMB 135mn in FY13 to RMB 15mn in FY14E. Under this backdrop, we estimate net profit to grow at 58.9% CAGR over FY13-16E to RMB 874mn in FY16E. Our net profit projection for FY14E-16E is accounted for the net profit from core operation only, and fair value gain (or loss) from biological assets is excluded.

Exhibit 22: Net profit and net margin of YST Dairy, FY10-16E


*: The net margin in FY10 and FY11 were distorted by fair value gain on dairy cows
 Source(s): The Company, ABCI Securities estimates



Risk Factors

High customer concentration

YST Dairy has a high customer concentration with only 5 customers. Sales attributable to the Group's largest customers accounted for ~36% of the Group's total revenue in FY13. The Group's customers are Yili Group, Mengniu Group, Feihe Dairy Group (飞鹤乳业集团), Bright Dairy Group (光明乳业集团), and Aibeite Dairy (吉林艾倍特乳业).

Animal risk

A major outbreak of any illnesses or diseases at any of the Group's dairy farms could have significant adverse impacts on raw milk production capacity and volume.

Food safety risks

Product safety and quality is critical for dairy production industry. Sales volume and financial condition could be adversely affected by product contamination, which may lead to product liability claims or other regulatory action.

Fluctuation in beef prices

Beef prices were highly correlated with raw milk prices. The upsurge in beef prices in 2012-2013 motivated farmers to sell their dairy cows and cash out. Subsequently, raw milk prices surged in 2013 due to reduced supply. We believe the upsurge of raw milk and beef prices in 4Q13 will motivate farmers to raise dairy cows again. Considering the two-year growing period from calves to heifers and milkable cows, we expect a surge in new raw milk supply is unlikely in 2014-15. However, a drastic decline in raw milk supply is unlikely to repeat in 2013-14 unless major disease outbreaks threatening the cattle occurs.

Fluctuation in biological value

The fair value of dairy cows is determined based on two criteria:

1. The market prices at year-end is adjusted with reference to the age and cost of the dairy cows to reflect differences in characteristics and stages of growth of the dairy cows; or
2. The present value of expected net cash flows from the dairy cows discounted at a current market rate when market prices are unavailable.

For a 10% increase (decrease) in average feeding cost, net profit would decrease (increase) by 18% FY13. For a 10% increase (decrease) raw milk ASP, net profit would increase (decrease) by 40% in FY13.



Comparison of the Group and its major peers

Exhibit 23: Comparison of segmental financial data among the Group and its major peers

YST Dairy (1431 HK)				China Modern Dairy (1117 HK)			
FY ended	Dec			FY ended	Dec*		
Reported currency	RMB			Reported currency	RMB		
FY	2011	2012	2013	FY	2011*	2012*	2013*
Revenue (RMB mn)	149	689	881	Revenue (RMB mn)	1,392	2,035	3,289
Net profit (RMB mn)	190	210	218	Net profit (RMB mn)	314	408	481
Total assets (RMB mn)	2,387	2,593	4,968	Total assets	7,917	10,159	12,494
Total equity (RMB mn)	381	590	3,911	Total equity	4,889	5,329	5,861
Total equity/total assets (%)	15.96	22.75	78.72	Total equity/total assets	61.75	52.46	46.91
Revenue composition (RMB mn)				Revenue composition (RMB mn)			
Sales of raw milk	149	689	881	Sales of raw milk	1,392	2,005	2,911
				Sales of processed milk	-	86	321
Revenue composition (%)				Revenue composition (%)			
Sales of raw milk	100.00	100.00	100.00	Sales of raw milk	100.00	98.54	88.51
				Sales of processed milk	-	4.23	9.76
Herd size and milk yield				Herd size and milk yield			
Milkable cows (Head)	14,950	20,643	21,544	Milkable cows (Head)	54,338	77,953	98,791
Heifers and calves (Head)	17,269	16,357	18,852	Heifers and calves (Head)	74,421	98,311	88,047
Total dairy cows (Head)	32,219	37,000	40,396	Total dairy cows (Head)	128,759	176,264	186,838
Total sales volume (tonnes)	35,722	168,070	183,702	Total sales volume (tonnes)	366,656	496,979	678,762
Total Sales volume per dairy cows (tonnes/head)	1.11	4.54	4.55	Total Sales volume per dairy cows (tonnes/head)	2.85	2.82	3.63
Milk yield for milkable cows (tonnes)	8.80	8.90	9.00	Milk yield for milkable cows (tonnes)	7.80	7.94	8.51
Profitability (%)				Profitability (%)			
Gross profit margin	34.53	37.80	42.57	Gross profit margin	31.20	32.08	38.19
ROAA		8.42	5.76	ROAA		4.51	4.25
ROAE		43.20	9.67	ROAE		8.11	8.76

*The year end of the reporting period of China Modern Dairy change from June to Dec in 2013. The financial data for the company above was adjusted by ABCI Securities

Source(s): Companies, Bloomberg, ABCI Securities



Exhibit 24: Comparison of segmental financial data among the Group and its major international peers (cont'd)

Huishan Dairy (6863 HK)			
FY ended	Mar		
Reported currency	RMB		
FY	<u>2012</u>	<u>2013</u>	<u>1H14</u>
Revenue (RMB mn)	1,333	2,552	1,534
Net profit (RMB mn)	450	945	516
Total assets	7,190	10,511	17,930
Total equity	882	5,883	12,438
Total equity/total assets	12.27	55.97	69.37
Revenue composition (RMB mn)			
Sales of raw milk	672	681	424
Liquid milk business	564	1,707	1,002
Others	97	164	108
Revenue composition (%)			
Sales of raw milk	50.42	26.68	27.64
Liquid milk business	42.32	66.88	65.32
Others	7.26	6.44	7.04
Herd size and milk yield			
Milkable cows (Head)	31,221	49,889	57,040
Heifers and calves (Head)	59,033	62,962	71,312
Total dairy cows (Head)	90,254	112,851	128,352
Total sales volume (tonnes)	236,190	397,593	227,117
Total Sales volume per dairy cows (tonnes/head)	2.62	3.52	1.77
Milk yield for milkable cows (tonnes)	8.60	9.10	8.60
Profitability (%)			
Gross profit margin	6.90	17.32	16.23
ROAA		10.68	7.26
ROAE		27.95	11.27

Source(s): Companies, Bloomberg, ABCI Securities



Financial Statements of the Group

Consolidated income statement (2012A-2016E)

FY Ended Dec 31 (RMB mn)	2012A	2013A	2014E	2015E	2016E
Revenue	689	881	1,160	1,692	2,463
Raw milk	689	881	1,160	1,692	2,463
COGS	(429)	(506)	(694)	(1,010)	(1,467)
Gross profit	260	375	465	682	996
SG&A	(40)	(59)	(92)	(116)	(143)
Other income (loss)	(11)	(97)	42	34	23
Pre-tax profit	210	218	416	601	875
Income tax	-	(0)	(1)	(1)	(2)
Net profit*	210	218	415	600	874
Profit attributable to:					
Minority interests	-	-	-	-	-
Equity shareholders of the Company	210	218	415	600	874
EPS (RMB)	0.054	0.056	0.106	0.153	0.223
DPS (RMB)	-	-	-	-	-
EBIT	263	353	431	621	906
EBITDA	274	382	486	690	988

*: Our net profit projection refers to net profit from the core operation only, and it is excluding fair value change of biological assets

Source(s): Company, ABCI Securities estimates

Consolidated balance sheet (2012A-2016E)

As of Dec 31 (RMB mn)	2012A	2013A	2014E	2015E	2016E
Current assets	233	2,319	2,177	1,849	1,932
Cash and equivalent	8	2,026	1,538	1,152	950
Trade and bill receivables	71	65	126	152	253
Inventories	139	201	484	512	693
Other current assets	15	27	30	32	36
Non-current assets	2,360	2,649	3,400	4,506	5,808
Property, plant and equipment	1,299	1,341	1,786	2,218	2,636
Intangible assets	118	-	1	1	2
Long term investments	-	-	-	-	-
Biological assets	942	1,088	1,365	2,016	2,874
Other non-current assets	2	219	249	271	297
Total assets	2,593	4,968	5,577	6,355	7,740
Current liabilities	1,704	816	987	1,138	1,620
Trade and bill payables	208	212	244	254	389
Receipts in advance	-	-	-	-	-
Short term borrowings	166	220	320	420	720
Other current liabilities	1,330	384	422	465	511
Non-current liabilities	298	241	265	291	320
Long-term payables	-	-	-	-	-
Long-term borrowings	298	-	-	-	-
Other non-current liabilities	-	241	265	291	320
Total liabilities	2,003	1,057	1,252	1,430	1,941
Minority interests	-	-	-	-	-
Shareholders' equities	590	3,911	4,326	4,926	5,799
BVPS (RMB)	0.151	1.001	1.107	1.260	1.484

Source(s): Company, ABCI Securities estimates



Consolidated cash flow statement (2012A-2016E)

FY ended Dec 31 (RMB mn)	2012A	2013A	2014E	2015E	2016E
Profit before tax	210	218	416	601	875
Changes in depreciation and amortization	36	51	55	69	82
Changes in working capital	(149)	(295)	(312)	(58)	(155)
Financial cost	46	51	15	20	31
Income tax paid	-	(0)	(1)	(1)	(2)
Others	(14)	52	-	-	-
CF Operating	129	77	174	630	831
Increase in PP&E	(98)	(161)	(500)	(500)	(500)
Increase in intangible assets	-	(4)	(1)	(1)	(1)
Increase in biological assets	(119)	(160)	(241)	(563)	(781)
Others	(2)	(44)	-	-	-
CF Investing	(219)	(369)	(741)	(1,064)	(1,282)
Capital injection	-	3,011	-	-	-
Net debt financing	(26)	(245)	100	100	300
Dividend payout	(45)	(195)	-	-	-
Interest paid	(24)	(23)	(15)	(20)	(31)
Others	176	(236)	(6)	(31)	(20)
CF Financing	81	2,311	79	49	249
Net change in cash	(10)	2,018	(489)	(385)	(202)
Cash at the beginning	17	8	2,026	1,538	1,152
Adjustment (Time deposit & FX effect)	-	(0)	-	-	-
Cash at the end	8	2,026	1,538	1,152	950

Source(s): Company, ABCI Securities estimates

Key operating and financial ratios (2012A-2016E)

FY ended Dec 31	2012A	2013A	2014E	2015E	2016E
Sales mixed (%)					
Raw milk	100.00	100.00	100.00	100.00	100.00
Profit & loss ratios (%)					
Gross margin	37.80	42.57	40.13	40.32	40.44
Net profit margin	30.44	24.72	35.80	35.44	35.47
Effective tax rate	-	0.18	0.18	0.18	0.18
Growth (%)					
Revenue	363.16	27.81	31.67	45.92	45.54
Gross profit	406.96	43.93	24.13	46.60	45.98
EBIT	16.96	34.53	21.93	44.19	45.95
EBITDA	20.56	39.39	27.17	41.92	43.26
Net profit	10.48	3.81	90.67	44.45	45.67
Balance sheet ratios					
Current ratio (x)	0.14	2.84	2.21	1.62	1.19
Quick ratio (x)	0.06	2.60	1.72	1.17	0.76
Cash ratio (x)	0.00	2.48	1.56	1.01	0.59
Trade and bill receivables days	31.05	28.08	30.00	30.00	30.00
Trade and bill payables turnover days	149.12	151.44	120.00	90.00	80.00
Inventory turnover days	112.48	122.67	180.00	180.00	150.00
Total debt / equity ratio (%)	78.75	5.63	7.40	8.53	12.42
Net debt / equity ratio (%)	77.43	Net Cash	Net Cash	Net Cash	Net Cash
Returns (%)					
ROAE	43.19	9.67	10.08	12.96	16.29
ROAA	8.42	5.76	7.87	10.05	12.40
Payout ratio	-	-	-	-	-

Source(s): Company, ABCI Securities estimates

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Rating	Definition
Buy	Stock return \geq Market return rate
Hold	Market return $- 6\% \leq$ Stock return $<$ Market return rate
Sell	Stock return $<$ Market return $- 6\%$

Stock return is defined as the expected % change of share price plus gross dividend yield over the next 12 months

Market return: 5-year average market return rate from 2007-2011

Time horizon of share price target: 12-month

Definition of share price risk

Rating	Definition
Very high	$2.6 \leq$ 180 day volatility/180 day benchmark index volatility
High	$1.5 \leq$ 180 day volatility/180 day benchmark index volatility $<$ 2.6
Medium	$1.0 \leq$ 180 day volatility/180 day benchmark index volatility $<$ 1.5
Low	180 day volatility/180 day benchmark index volatility $<$ 1.0

We measure share price risk by its volatility relative to volatility of benchmark index. Benchmark index: Hang Seng Index.

Volatility is calculated from the standard deviation of day to day logarithmic historic price change. The 180-day price volatility equals the annualized standard deviation of the relative price change for the 180 most recent trading days closing price.

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