

# Feihe (6186 HK) Pandemic-induced headwinds persist; downgrade to HOLD

- New COVID-19 cases in northeastern China, where the Group's production facilities and raw milk supplier are located, imply potential disruption
- Delayed commencement of the Kingston plant in Canada means that the launch of premium goat milk IMF products will be deferred
- Consumer behavior has turned conservative and may switch to lower-priced alternatives
- Downgrade to **HOLD**; current TP implies 24.21x/19.47x 20E/21E P/E, or 6.71x/4.99x 20E/21E P/B

**New COVID-19 cases may hamper production capability.** Though the COVID-19 outbreak is largely contained in China, a small no. of new cases have been reported in Wuhan and northeastern China, where the Group's production facilities are located (Helongjiang and Jilin provinces). In addition, YST Dairy, which supplies 68.7% of raw milk purchased by the Group in 2018 according to our calculation, also has its production facilities located in northeastern China and may face potential production disruption. In Canada, the no. of new cases is still above 1000 per day. According to the Group, its new plant located in Kingston, Ontario, is tasked to produce its new goat milk IMF products for the North America and Southeast Asia markets. The Ontario government has not specified the timeline for reopening manufacturing plants; therefore, production of the Kingston Plant will be affected. We believe challenges brought by production disruptions would add to uncertainty in its growth outlook and product launch schedule.

**Consumer behavior likely to turn conservative.** According to NBS, the national per capita disposable income growth was only at 0.8% YoY (1Q19: 8.8% YoY); the median figure declined by 0.7% YoY (1Q19: 8.7% YoY). In addition, for items under the national per capita expenditure, only "Food, tobacco & alcohol" and "Residence" grew by 2.1% YoY while all other items declined. The low or negative growth of per capita disposable income has resulted in reduced consumer spending and we expect consumer behavior to remain conservative amid economic uncertainties. As the Group focuses mainly on high-end products, sales can be affected since consumers may switch to cheaper alternatives.

**Downgrade to HOLD; TP at HK\$ 14.8.** Due to the delayed commencement of the Kingston plant, which will subsequently defer the launch of its premium goat milk IMF products, we lower our revenue forecast. FY19-22E revenue CAGR would be 20.5% (previous: 21.4%). Downgrade to **HOLD** amid possible production disruption, delays in new product launch, and potential impacts of reduced consumer spending. Our DCF-derived TP represents 24.21x/19.47x 20E/21E P/E, or 6.71x/4.99x 20E/21E P/B.

**Risk factors:** 1) Macroeconomic risk; 2) Demographic risk; 3) Product quality risk; 4) Supplier concentration risk; 5) Raw material cost risk; 6) Interest rate risk; 7) Foreign currency risk; 8) Product development risk; 9) Prolonged pandemic risk; 10) Production disruption risk.

## Results and Valuation

FY ended Dec 31	FY17A	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	5,887	10,392	13,722	17,521	20,438	23,514
Chg (YoY %)	58.07	76.52	32.04	27.69	16.65	15.05
Net Profit – to owners of the Company (RMB mn)	1,160	2,242	3,935	5,000	6,217	7,204
Chg (% YoY)	178.24	93.26	75.47	27.07	24.35	15.87
Basic EPS (RMB)	0.14	0.28	0.48	0.56	0.70	0.81
Chg (YoY %)	180.00	100.00	71.43	16.60	24.35	15.87
P/E (x)	113.94	56.97	33.23	28.50	22.92	19.78
BVPS (RMB)	0.43	0.72	1.46	2.02	2.71	3.52
P/B (x)	36.87	22.07	10.94	7.90	5.88	4.53
Dividend (HK\$)	N/A	N/A	0.19	0.20	0.25	0.29
Dividend yield	N/A	N/A	1.33	1.36	1.69	1.96
ROAA (%)	19.82	23.76	22.57	21.98	23.48	21.67
ROAE (%)	38.92	47.85	41.82	32.20	29.41	25.87

Source(s): The Group, ABCI Securities estimates

## Company Report May 12, 2020 Rating: HOLD TP: HK\$ 14.8

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Share price (HK\$)	14.44
52WK H/L (HK\$)	16.5/6.26
Est. share price return	2.23%
Est. dividend yield	1.38%
Est. total returns	3.61%
Previous rating/TP	BUY/HK\$16.0
Previous report date	Mar 31, 2020

Source(s): Bloomberg, ABCI Securities estimates

### Key data

Issued shares (mn)	8,933.34
Mkt cap (HK\$ mn)	128,997.43
ADT since IPO (HK\$mn)	274.91
Shareholding (%)	
Garland Glory Holdings	43.32
North Haven Private Equity Asia	18.59
Dasheng LTD	4.45

Source(s): Bloomberg, the Group

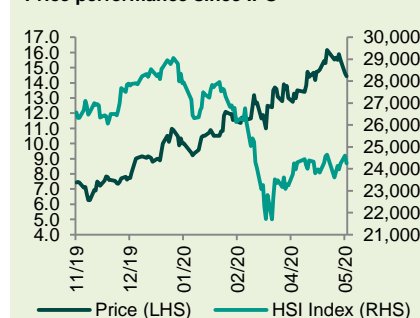
### Price performance (%)

	Absolute	Relative*
1-mth	6.96	7.07
3-mth	34.70	47.30
6-mth	92.53	102.59

\* Relative to HSI

Source(s): Bloomberg

### Price performance since IPO



Source(s): Bloomberg, ABCI Securities

Note: Market data as of May 12, 2020  
RMB/HKD: 1.0896



**Exhibit 1: Change in assumptions, projections, and valuations**

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FY ends at Dec 31	Current report		Previous report		Rationale
	FY20E	FY21E	FY20E	FY21E	
<b>Assumptions</b>					
GPM (%)	70.5	71.4	70.5	71.4	
Pretax margin (%)	40.5	43.2	40.5	43.1	N/A
NPM (to shareholders of the Company) (%)	28.5	30.4	28.5	30.4	
D/E (%)	0.0	0.0	0.0	0.0	N/A
D/A (%)	0.0	0.0	0.0	0.0	
Tax rate (%)	29.5	29.5	29.5	29.5	N/A
Revenue growth (YoY %)	27.7	16.6	27.7	19.7	
- High-end product series	31.6	15.1	31.6	16.4	Lower growth projections caused by expected delay of product launch for goat milk IMF
- Regular product series	20.8	13.5	20.8	13.5	
- Other dairy products	14.2	8.4	14.2	8.4	
- Other	15.0	17.0	15.0	17.0	
<b>Projections</b>					
DRO (days)	12.8	12.8	12.8	12.8	
DIH (days)	60.5	60.1	60.5	60.1	Adjusted based on the performance in FY19
DPO (days)	82.0	82.6	82.0	82.6	
CCC (days)	(8.8)	(9.6)	(8.8)	(9.6)	
ROAA (%)	22.0	23.5	22.0	23.9	Lower growth contributed to the lower returns
ROAE (%)	32.2	29.4	32.2	30.0	
<b>Valuations</b>					
TP (HK\$)	14.8		16.0		
P/E	24.21	19.47	26.22	20.58	Lower growth projections lead to lower valuation and TP
P/B	6.71	4.99	7.27	5.37	

Note: 1) Other products include nutritional supplement and baby & toddler food products; 2) Previous report was published on Mar 31, 2020

Source(s): The Group, ABCI Securities estimates

**Exhibit 2: Major forecast changes**

FY ends at Dec 31	Current report			Previous report			Change (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue (RMB mn)	17,521	20,438	23,514	17,521	20,967	24,569	0.00	(2.52)	(4.29)
Net profit (to owners of the Company)	5,000	6,217	7,204	5,000	6,371	7,528	0.00	(2.42)	(4.30)
EPS (RMB)	0.56	0.70	0.81	0.56	0.71	0.84	0.00	(1.41)	(3.57)

Note: Previous report was published on Mar 31, 2020

Source(s): The Group, ABCI Securities estimates



## Financial statement of the Group

### Consolidated income statement

FY ends at Dec 31 (RMB mn)	FY17A	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Revenue</b>	<b>5,887</b>	<b>10,392</b>	<b>13,722</b>	<b>17,521</b>	<b>20,438</b>	<b>23,514</b>
- COW Milk - IMF	5,417	9,199	12,538	16,165	18,545	20,366
- High-end IMF product series	3,795	6,658	9,411	12,387	14,257	15,617
- Regular IMF product series	1,621	2,542	3,127	3,778	4,288	4,748
- GOAT Milk - IMF	0	0	0	0	366	1,381
- Other dairy products	471	550	605	691	749	834
- Other products	0	642	578	665	778	934
Cost of sales	(2,097)	(3,373)	(4,112)	(5,168)	(5,838)	(6,716)
<b>Gross profit</b>	<b>3,790</b>	<b>7,019</b>	<b>9,610</b>	<b>12,353</b>	<b>14,600</b>	<b>16,798</b>
- COW Milk - IMF	3,761	6,684	9,081	11,966	13,913	15,381
- High-end IMF product series	2,814	5,091	7,141	9,526	11,116	12,259
- Regular IMF product series	947	1,593	1,940	2,440	2,797	3,122
- GOAT Milk - IMF	0	0	0	0	236	876
- Other dairy products	29	104	210	132	150	177
- Other products	0	231	319	256	300	364
Admin expenses	(361)	(580)	(913)	(1,115)	(1,103)	(1,294)
Selling expenses	(2,139)	(3,661)	(3,848)	(4,829)	(5,260)	(6,012)
Net finance costs	(21)	(59)	(73)	(103)	0	0
Others	0	0	1	1	1	1
<b>Pretax profit</b>	<b>1,651</b>	<b>3,189</b>	<b>5,683</b>	<b>7,091</b>	<b>8,822</b>	<b>10,212</b>
Tax	(491)	(946)	(1,748)	(2,092)	(2,605)	(3,008)
<b>Net profit</b>	<b>1,160</b>	<b>2,242</b>	<b>3,935</b>	<b>5,000</b>	<b>6,217</b>	<b>7,204</b>
- Owners	1,160	2,242	3,935	5,000	6,217	7,204
- MI	0	0	0	0	0	0
<b>Dividend</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>1,500</b>	<b>1,865</b>	<b>2,161</b>
<b>EPS (RMB)</b>						
- Basic	0.14	0.28	0.48	0.56	0.70	0.81
- Diluted	0.14	0.28	0.48	0.55	0.68	0.79
<b>DPS (HK\$)</b>	<b>0.00</b>	<b>0.00</b>	<b>0.19</b>	<b>0.20</b>	<b>0.25</b>	<b>0.29</b>

Note: Other products include nutritional supplement and baby & toddler food products

Source(s): The Group, ABCI Securities estimates

### Consolidated balance sheet

FY ends at Dec 31 (RMB mn)	FY17A	FY18A	FY19A	FY20E	FY21E	FY22E
Bank balances and cash	2,771	3,641	7,377	9,344	14,704	17,679
Trade and bills receivables	175	513	314	911	527	1,031
Inventory	395	660	686	1,028	895	1,282
Others	1,082	2,481	8,911	4,565	7,393	8,371
<b>Current assets</b>	<b>4,423</b>	<b>7,295</b>	<b>17,289</b>	<b>15,848</b>	<b>23,519</b>	<b>28,363</b>
PP&E	1,431	2,555	3,971	4,556	5,062	5,435
Land use rights	119	306	377	192	164	147
Investment in an associates	143	143	143	143	143	143
Others	899	1,559	1,224	1,760	1,573	1,939
<b>Non-current assets</b>	<b>2,591</b>	<b>4,563</b>	<b>5,715</b>	<b>6,651</b>	<b>6,941</b>	<b>7,664</b>
<b>Total assets</b>	<b>7,014</b>	<b>11,857</b>	<b>23,004</b>	<b>22,499</b>	<b>30,461</b>	<b>36,027</b>
Trade and bills payable	514	833	1,042	1,282	1,359	1,711
ST borrowings	903	1,083	3,094	0	0	0
Others	1,672	2,944	3,303	2,782	3,425	2,406
<b>Current liabilities</b>	<b>3,089</b>	<b>4,860</b>	<b>7,439</b>	<b>4,064</b>	<b>4,784</b>	<b>4,117</b>
LT Borrowing	64	657	1,716	0	0	0
Others	275	552	820	405	1,430	458
<b>Non-current liabilities</b>	<b>339</b>	<b>1,210</b>	<b>2,536</b>	<b>405</b>	<b>1,430</b>	<b>458</b>
Shareholders' capital	3,585	5,787	13,030	18,029	24,247	31,451
MI	0	0	0	0	0	0
<b>Total equity</b>	<b>3,585</b>	<b>5,787</b>	<b>13,030</b>	<b>18,029</b>	<b>24,247</b>	<b>31,451</b>
<b>Total liabilities and equity</b>	<b>7,014</b>	<b>11,857</b>	<b>23,004</b>	<b>22,499</b>	<b>30,461</b>	<b>36,027</b>

Source(s): The Group, ABCI Securities estimates



### Consolidated cash flow statement

FY ends at Dec 31 (RMB mn)	FY17A	FY18A	FY19A	FY20E	FY21E	FY22E
Profit before tax	1,651	3,189	5,683	7,091	8,822	10,212
Depreciation and amortization	98	162	181	168	154	145
Change in working capital	1,174	659	607	(1,771)	1,594	(2,073)
Others	(699)	(888)	(1,290)	(690)	(3,705)	(2,801)
<b>Cash flow from operating activities</b>	<b>2,224</b>	<b>3,121</b>	<b>5,181</b>	<b>4,798</b>	<b>6,865</b>	<b>5,484</b>
PP&E and right-of-use assets	(406)	(1,083)	(1,349)	(539)	(476)	(356)
Structured deposits & time deposits	(1,145)	(1,857)	(4,606)	2,243	(2,036)	(1,187)
Others	(128)	(332)	440	131	(347)	(170)
<b>Cash flow from investing activities</b>	<b>(1,680)</b>	<b>(3,272)</b>	<b>(5,515)</b>	<b>1,835</b>	<b>(2,859)</b>	<b>(1,712)</b>
Change in borrowing	465	752	3,070	(4,810)	0	0
Placement of pledged bank deposits	(243)	(1,200)	(12)	(84)	(88)	(92)
Others	0	(61)	1,065	(145)	(30)	(22)
<b>Cash flow from financing activities</b>	<b>222</b>	<b>(509)</b>	<b>4,123</b>	<b>(5,039)</b>	<b>(118)</b>	<b>(115)</b>
<b>Net change in cash</b>	<b>766</b>	<b>(660)</b>	<b>3,789</b>	<b>1,594</b>	<b>3,888</b>	<b>3,656</b>
Cash and cash equivalent - beg	817	1,566	896	4,659	6,245	10,108
ForEx Impact	1	(9)	(26)	(8)	(25)	50
<b>Cash and cash equivalent - end</b>	<b>1,584</b>	<b>896</b>	<b>4,659</b>	<b>6,245</b>	<b>10,108</b>	<b>13,815</b>

Source(s): The Group, ABCI Securities estimates

### Key operating and financial ratios

FY ends at Dec 31	FY17A	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Growth (YoY %)</b>						
Revenue	58.1	76.5	32.0	27.7	16.6	15.0
Cow - IMF	70.3	69.8	36.3	28.9	14.7	9.8
Goat - IMF	N/A	N/A	N/A	N/A	N/A	277.0
Other dairy products	(13.4)	16.9	10.0	14.2	8.4	11.3
Other products	N/A	N/A	(10.0)	15.0	17.0	20.0
Gross profit	86.4	85.2	36.9	28.5	18.2	15.1
Pretax profit	177.5	93.1	78.2	24.8	24.4	15.8
Net profit (to shareholders of the Company)	178.2	93.3	75.5	27.1	24.4	15.9
<b>Profitability ratios (%)</b>						
GPM	64.4	67.5	70.0	70.5	71.4	71.4
Cow - IMF	69.4	72.7	72.4	74.0	75.0	75.5
Goat - IMF	N/A	N/A	N/A	N/A	64.5	63.4
Other dairy products	6.2	18.9	34.7	19.0	20.1	21.2
Other products	N/A	35.9	55.1	38.5	38.6	39.0
Pretax margin	28.0	30.7	41.4	40.5	43.2	43.4
NPM (to shareholders of the Company)	19.7	21.6	28.7	28.5	30.4	30.6
<b>Return ratios (%)</b>						
ROAA	19.8	23.8	22.6	22.0	23.5	21.7
ROAE	38.9	47.8	41.8	32.2	29.4	25.9
<b>Liquidity ratio (x)</b>						
Current ratio	1.4	1.5	2.3	3.9	4.9	6.9
Quick ratio	1.3	1.4	2.2	3.6	4.7	6.6
Cash ratio	0.9	0.9	1.4	2.5	3.5	4.7
<b>Working capital turnover (days)</b>						
Receivable turnover	8.3	12.1	11.0	12.8	12.8	12.1
Inventory turnover	59.9	57.1	59.7	60.5	60.1	59.2
Payable turnover	76.1	72.9	83.2	82.0	82.6	83.4
Cash conversion cycle	(7.9)	(3.8)	(12.5)	(8.8)	(9.6)	(12.2)
<b>Leverage ratios (%)</b>						
Total debt to Equity	27.0	30.1	36.9	0.0	0.0	0.0
Total debt to Total assets	13.8	14.7	20.9	0.0	0.0	0.0
Net debt to Equity	(68.1)	(65.4)	(77.5)	(68.4)	(84.4)	(77.4)
Net debt to Total assets	(34.8)	(31.9)	(43.9)	(54.8)	(67.2)	(67.6)

Note:1) Other products include nutritional supplement and baby & toddler food products

Source(s): The Group, ABCI Securities estimates

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Rating	Definition
Buy	Stock return rate $\geq$ Market return rate (10%)
Hold	- Market return rate (-10%) $\leq$ Stock return rate < Market return rate (+10%)
Sell	Stock return < - Market return (-10%)

Notes: Stock return rate: expected percentage change of share price plus gross dividend yield over the next 12 months  
Market return rate: average market return rate since 2005 (HSI total return index 2005-17 CAGR at 10%)

Time horizon of share price target: 12-month

Stock rating, however, may vary from the stated framework due to factors including but not limited to: corporate governance, market capitalization, historical price volatility relative to corresponding benchmark index, average daily turnover of the stock relative to market capitalization of the stock, competitive advantages in corresponding industry, etc.

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