



## Mengniu (2319 HK) Margin profile to improve

- Revenue growth trajectory would continue to be affected by the challenging consumer market ; meanwhile, milk formula and cheese segments are still exploring new growth strategies
- Margins will expand on the Group's ability to enhance cost efficiency and the favorable price trend for raw milk
- Maintain **BUY**; current TP implies 22.67x/19.44x 23E/24E P/E, or 2.82x/2.56x 23E/24E P/B

**Growth trajectory to be affected by challenging consumer market recovery.** 1H23 headline revenue growth was 7.1% YoY. Excluding the cheese product segment affected by the Group's acquisition of Milkground (600882 CH), 1H23 revenue growth was 3.6% YoY. In 1H23, revenue of liquid milk and ice cream products grew 5.0% YoY and 10.4% YoY, while revenue growth in the milk powder segment was flat. The weakened consumer market in 1H23 was a major cause for the low organic revenue growth. Unremarkable performance of the milk powder segment shows the Group is still finding its footing in the consumer market. While consolidation impact in the cheese segment helped boost headline revenue growth, Milkground's 1H23 revenue actually declined 20.4% YoY to RMB 2,065.98mn. If its results further deteriorate, the Group's overall revenue would be adversely affected. Since improvement in the consumer market hinges on the macroeconomic recovery, we believe gains in 2H23 will likely be gradual. We project revenue growth in FY23E to reach 8.1% YoY; revenue of liquid milk, ice cream, and milk formula segments would grow by 5.2% YoY, 10.0% YoY, and 5.1% YoY. FY22-25E revenue CAGR is projected at 8.8%.

**Margin profile to improve.** In 1H23, GPM and OPM rose to 38.4% and 6.4% vs. 36.6% and 5.3% in 1H22, while NPM (to shareholders of the Company) declined to 5.9% from 7.9% in 1H22. The lower NPM can be attributed to the lower share of profit gained from associates and higher effected tax rate in 1H23. Improvement in GPM and OPM shows better cost efficiency and the Group's ability to capture the opportunity of declining raw milk price. We expect GPM, OPM, NPM (to shareholders of the Company) to reach 36.1%, 6.3%, and 5.5% in FY23E.

**Maintain BUY; TP at HK\$ 34.0.** We expect cost-control measures would support further margin expansion. Maintain **BUY**. We lower our DCF-derived TP to reflect the lower revenue and profit projections. Current TP represents 22.67x/19.44x 23E/24E P/E, or 2.82x/2.56x 23E/24E P/B.

**Risk factors:** 1) Macroeconomic risk; 2) Raw material cost risk; 3) Regulation risk; 4) Food safety risk; 5) Business acquisition risk; 6) Product concentration risk; 7) Uneven growth among product categories; 8) High financial leverage; 9) Acquisition risk.

### Results and Valuation

FY ended Dec 31	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue (RMB mn)	88,141	92,593	100,072	108,125	116,696
Chg (% YoY)	15.9	5.1	8.1	8.0	7.9
Net Profit (RMB mn)	5,026	5,303	5,517	6,432	7,545
Chg (% YoY)	42.6	5.5	4.0	16.6	17.3
Basic EPS (RMB)	1.27	1.34	1.40	1.63	1.91
Chg (% YoY)	42.0	5.3	4.3	16.6	17.3
P/E (x)	19.46	18.48	17.71	15.19	12.95
BVPS (RMB)	9.32	10.14	11.27	12.39	13.70
P/B (x)	2.66	2.45	2.20	2.00	1.81
DPS(RMB)	0.38	0.40	0.41	0.48	0.56
Yield (%)	1.5	1.6	1.7	1.9	2.3
ROAA (%)	5.6	4.8	4.4	4.9	5.6
ROAE (%)	14.4	13.8	13.1	13.8	14.7

Source(s): Bloomberg, ABCI Securities estimates

## Company Report

Sep 11, 2023

Rating: **BUY**

TP: HK\$ 34.0

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Share price (HK\$)	26.6
52Wk H/L(HK\$)	40.15/24.3
Est. share price return	27.8%
Est. dividend yield	1.7%
Est. total return	29.5%
Previous Rating&TP	BUY; HK\$44.3
Previous report date	Apr 4, 2023

Source(s): Bloomberg, ABCI Securities estimates

### Key Data

Issued shares (bn)	3.94
Market cap (HK\$ bn)	104.8
3-mth ADT (HK\$ mn)	293.0

### Major shareholders

	(%)
COFCO	24.1
FIL Limited	8.0

Source(s): Bloomberg, HKEX, ABCI Securities

### Sector Performance (%)

	Absolute	Relative*
1-mth	(4.57)	2.2
3-mth	(13.2)	(8.5)
6-mth	(25.1)	(13.4)

\* Relative to HSI

Source(s): Bloomberg, ABCI Securities

### 1-Year price performance (HK\$)



Source(s): Bloomberg, ABCI Securities

Note:

- All pricing and market data as of Sep 7, 2023;
- RMB/HKD: 1.0728

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

FY ends at Dec 31	Current report		Previous report		Rationale
	FY23E	FY24E	FY23E	FY24E	
<b>Assumptions</b>					
D/E (%)	86.3	74.6	59.9	46.4	Adjusted based on 1H23 company release
D/A (%)	35.8	31.9	27.6	22.9	
Tax rate (%)	20.2	20.2	17.8	17.9	
<b>Valuations</b>					
TP (HK\$)	34.0		44.3		Slashed TP due to lower revenue and profit forecasts
P/E (x)	22.67	19.44	26.73	23.78	
P/B (x)	2.82	2.56	3.49	3.17	

Note: Previous report was published on Apr 4, 2022

Source(s): The Company, ABCI Securities estimates

**Exhibit 2: Changes in major forecasts**

As of Dec 31	Current report			Previous report			Change (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue (RMB mn)	100,072	108,125	116,696	100,158	109,676	121,910	(0.1)	(1.4)	(4.3)
Net profit (to shareholders of the Company) (RMB mn)	5,517	6,432	7,545	5,749	6,463	7,722	(4.0)	(0.5)	(2.3)
EPS (RMB)	1.40	1.63	1.91	1.45	1.64	1.95	(3.7)	(0.2)	(2.0)

Source(s): ABCI Securities estimates



## Financial Statements

### Consolidated income statement

FY ends at Dec 31 (RMB mn, except per share data)	FY21A	FY22A	FY23E	FY24E	FY25E
<b>Revenue</b>	<b>88,141</b>	<b>92,593</b>	<b>100,072</b>	<b>108,125</b>	<b>116,696</b>
- Liquid milk	76,514	78,269	82,314	88,930	95,891
- Ice cream	4,240	5,652	6,216	6,902	7,544
- Milk formula	4,949	3,862	4,060	4,455	4,874
- Other revenue	2,438	4,810	7,483	7,838	8,387
COGS	(55,752)	(59,904)	(63,931)	(68,393)	(73,151)
<b>Gross profit</b>	<b>32,390</b>	<b>32,690</b>	<b>36,141</b>	<b>39,732</b>	<b>43,546</b>
S&D expenses	(23,488)	(22,347)	(25,147)	(27,530)	(29,870)
Admin expenses	(3,524)	(4,442)	(4,205)	(4,558)	(5,032)
Other operating expenses	(516)	(477)	(523)	(544)	(600)
<b>EBIT</b>	<b>4,862</b>	<b>5,423</b>	<b>6,266</b>	<b>7,100</b>	<b>8,044</b>
Net interest expense /income	284	260	189	666	927
Other gains/(losses)	693	819	286	105	260
<b>Profit before tax</b>	<b>5,868</b>	<b>6,502</b>	<b>6,741</b>	<b>7,872</b>	<b>9,231</b>
Tax	(905)	(1,318)	(1,359)	(1,591)	(1,863)
<b>Total net profit</b>	<b>4,964</b>	<b>5,185</b>	<b>5,382</b>	<b>6,281</b>	<b>7,368</b>
- Profit to shareholders	5,026	5,303	5,517	6,432	7,545
- Minority interest	(62)	(118)	(135)	(151)	(177)
<b>Dividend</b>	<b>1,506</b>	<b>1,590</b>	<b>1,613</b>	<b>1,883</b>	<b>2,209</b>
<b>EPS (RMB)</b>					
- Basic EPS	1.27	1.34	1.40	1.63	1.91
- Diluted EPS	1.27	1.34	1.30	1.52	1.78
<b>DPS (RMB)</b>	<b>0.38</b>	<b>0.40</b>	<b>0.41</b>	<b>0.48</b>	<b>0.56</b>

Note: items may not sum up due to rounding

Source(s): The Group, ABCI Securities estimates

### Consolidated balance sheet

FY ends at Dec 31 (RMB mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Cash and cash equivalent	11,217	12,766	19,544	23,783	19,858
Trade and bills receivable	4,160	3,660	4,843	3,377	4,351
Inventory	6,485	8,073	6,664	8,314	6,905
Others	9,158	12,278	11,545	13,673	8,157
<b>Total current assets</b>	<b>31,020</b>	<b>36,777</b>	<b>42,597</b>	<b>49,147</b>	<b>39,272</b>
PP&E and CIP	19,955	23,764	24,001	26,470	31,267
Goodwill	4,858	8,888	8,888	8,888	8,888
Other intangible assets	7,999	12,374	12,993	13,643	14,325
Others	34,270	36,010	37,851	34,486	38,200
<b>Total non-current assets</b>	<b>67,081</b>	<b>81,036</b>	<b>83,733</b>	<b>83,486</b>	<b>92,680</b>
<b>Total assets</b>	<b>98,101</b>	<b>117,813</b>	<b>126,330</b>	<b>132,633</b>	<b>131,952</b>
Trade and bills payable	8,804	10,201	10,707	11,401	12,796
ST borrowings	4,265	9,095	11,845	11,440	10,067
Others	16,003	13,858	13,752	18,423	15,727
<b>Total current liabilities</b>	<b>29,072</b>	<b>33,153</b>	<b>36,304</b>	<b>41,264</b>	<b>38,591</b>
LT Borrowings	18,786	26,106	29,485	26,962	23,951
Convertible bonds	3,981	3,908	3,908	3,869	3,830
Others	4,262	4,594	4,189	3,848	3,908
<b>Total non-current liabilities</b>	<b>27,030</b>	<b>34,608</b>	<b>37,582</b>	<b>34,678</b>	<b>31,688</b>
Shareholders' equity	36,826	40,099	44,412	48,810	53,969
Minority interest	5,174	9,953	8,032	7,881	7,704
<b>Total equity</b>	<b>41,999</b>	<b>50,052</b>	<b>52,444</b>	<b>56,691</b>	<b>61,673</b>
<b>Total liabilities and equity</b>	<b>98,101</b>	<b>117,813</b>	<b>126,330</b>	<b>132,633</b>	<b>131,952</b>

Note: items may not sum up due to rounding

Source(s): The Group, ABCI Securities estimates



**Consolidated cash flow statement**

FY ends at Dec 31 (RMB mn)	FY21A	FY22A	FY23E	FY24E	FY25E
Pretax profit	5,868	6,502	6,741	7,872	9,231
Depreciation and amortization	2,396	2,878	2,036	2,329	2,868
Change in working capital	1,459	932	2,536	2,774	4,848
Others	(2,179)	(1,980)	(2,993)	(3,465)	(4,202)
<b>Cash flow from operating activities</b>	<b>7,545</b>	<b>8,333</b>	<b>8,320</b>	<b>9,509</b>	<b>12,745</b>
Change in PP&E and CIP	(5,992)	(4,723)	(6,157)	(7,061)	(8,819)
Others	(9,448)	(10,139)	13,177	11,036	10,344
<b>Cash flow from investing activities</b>	<b>(15,440)</b>	<b>(14,862)</b>	<b>7,020</b>	<b>3,975</b>	<b>1,526</b>
Change in borrowings	8,089	12,076	6,129	(2,968)	(4,422)
Others	(1,316)	(7,929)	(18,231)	(8,718)	(11,586)
<b>Cash flow from financing activities</b>	<b>6,773</b>	<b>4,147</b>	<b>(12,102)</b>	<b>(11,685)</b>	<b>(16,008)</b>
<b>Cash at bank and on hand classified as held for sale</b>	<b>0</b>	<b>(59)</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>Net change in cash</b>	<b>(1,123)</b>	<b>(2,441)</b>	<b>3,238</b>	<b>1,799</b>	<b>(1,737)</b>
Forex effect	(11)	43	(52)	(7)	(5)
<b>Cash and cash equivalent - end</b>	<b>8,092</b>	<b>5,693</b>	<b>8,879</b>	<b>10,671</b>	<b>8,929</b>

Note: items may not sum up due to rounding

Source(s): The Group, ABCI Securities estimates

**Key operating and financial ratios**

FY ends at Dec 31	FY21A	FY22A	FY23E	FY24E	FY25E
<b>Growth (YoY %)</b>					
Revenue	15.9	5.1	8.1	8.0	7.9
- Liquid milk	12.9	2.3	5.2	8.0	7.8
- Ice cream	61.0	33.3	10.0	11.0	9.3
- Milk powder	8.2	(22.0)	5.1	9.7	9.4
- Other products	126.3	97.3	55.6	4.7	7.0
Gross profit	13.1	0.9	10.6	9.9	9.6
Operating profit	39.6	11.6	15.5	13.3	13.3
Pretax profit	41.2	10.8	3.7	16.8	17.3
Net profit (to shareholders of the Company)	42.6	5.5	4.0	16.6	17.3
<b>Profitability ratios (%)</b>					
GPM	36.7	35.3	36.1	36.7	37.3
OPM	5.5	5.9	6.3	6.6	6.9
Pretax margin	6.7	7.0	6.7	7.3	7.9
NPM (to shareholders of the Company)	5.7	5.7	5.5	5.9	6.5
<b>Return ratios (%)</b>					
ROAA	5.6	4.8	4.4	4.9	5.6
ROAE	14.4	13.8	13.1	13.8	14.7
<b>Liquidity ratio (x)</b>					
Current ratio	1.1	1.1	1.2	1.2	1.0
Quick ratio	2.5	2.3	2.2	2.4	2.9
Cash ratio	1.7	1.7	1.7	1.7	1.9
<b>Cash conversion cycle (days)</b>					
Days of outstanding receivable	15	15	16	14	12
Days of inventory on hand	39	44	42	40	38
Days of outstanding payable	55	58	60	59	60
CCC	(1)	2	(2)	(5)	(10)
<b>Leverage ratios (%)</b>					
Total debt/Equity	64.4	78.1	86.3	74.6	61.4
Total debt/Total assets	27.6	33.2	35.8	31.9	28.7
Net debt/Equity	37.7	52.6	49.0	32.6	29.2
Net debt/Assets	16.1	22.4	20.3	13.9	13.6

Note: items may not sum up due to rounding

Source(s): The Group, ABCI Securities estimates

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Rating	Definition
Buy	Stock return rate $\geq$ Market return rate ( $\sim 9\%$ )
Hold	- Market return rate ( $\sim 9\%$ ) $\leq$ Stock return rate $<$ Market return rate ( $\sim +9\%$ )
Sell	Stock return $<$ - Market return ( $\sim -9\%$ )

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 2006 (HSI total return index 2006-22 averaged at 8.4%)

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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