



# Yili (600887 CH)

## Defensive amid challenges; maintain BUY

- Revenue growth slowed in 1H19 to 12.8% YoY; GPM, OPM, and NPM (to owners of the Company) declined to 38.7%, 8.7% and 8.4% in 1H19
- Remained dominant in the offline UHT products and fresh milk product markets in 1H19
- Expect revenue CAGR of 13.4% in FY18-21E; we expect growth to fluctuate in coming years amid challenge
- Rising raw material and operating costs is a concern going forward
- Maintain **BUY**; current TP represents 31.13x/29.48x 19E/20E P/E or 7.26x/6.19x 19E/20E P/B

**Revenue growth was 12.8% YoY in 1H19.** Revenue growth in liquid milk, chilled products, and milk formula product segments were 13.2% YoY, 15.4% YoY, and 13.4% YoY in 1H19. Revenue growth in 1H19 dropped noticeably from 1H18, which was mainly due to the revenue growth declining to 8.7% YoY in 2Q19 from 17.1% YoY in 1Q19. We believe that the faltering economic growth and declining retail sales growth are starting to impact the Group's performance. However, we still believe the Group would achieve its FY19 revenue target of RMB 90bn, based on the 1H19 performance.

**Margins contracted in 1H19.** GPM, OPM, and NPM (to owners of the Company) declined to 38.7%, 8.7% and 8.4% in 1H19 from 39.2%, 9.5%, and 8.6% in 1H18. Core GPM was stable at ~ 38.6%. The 1H19 margin deterioration was mainly attributable to the 2Q19 margins being lower than those of 1Q19. GPM, OPM and NPM (to owners of the Company) dropped from 40.1%, 10.8%, and 9.8% in 1Q19 to 37.3%, 6.4%, and 6.9% in 2Q19. The Group is facing higher raw material costs and operating costs, which we believe would pose challenges for the Group to achieve its FY19 net profit target of RMB 7.6bn.

**Staying strong in offline UHT products and offline fresh milk products.** The Group's offline UHT product market share increased by 2.4ppt to 38.8% in 1H19; its share in offline fresh milk market share edged down by 1.9ppt to 39.1% in 1H19. Yili is catching up quickly in the online liquid milk product segment – its share rose to 24.3% in 1H19 from 21.4% in 1H18, whereas Mengniu's rose to 26.5% in 1H19 from 24.0% in 1H18.

**Expect revenue CAGR of 13.4% in FY18-21E.** We expect total revenue would rise by 13.8% YoY to reach RMB 90.6bn in FY19E, although slowdown can be expected in FY20E due to a weakened consumer market. Revenue CAGRs of liquid milk, chilled product, and milk formula segments are expected to reach 12.4%, 12.5%, and 19.0% in FY18-21E. We expect margins would also fall in FY20E due to the rising raw material and operating costs. Our current NP for FY19 is 9.6% lower than the Group's target.

**TP at RMB 34.9; maintain BUY.** The Group recently announced a new share award scheme for its management (152,428k shares would be granted to certain management members at RMB 15.46/shr), which suppress share price in the short term. We remain positive on the Group's overall performance and its defensiveness in the challenging environment. Nonetheless, we lower TP to reflect the lower growth rates in coming years. Our DCF-derived TP represents 31.13x/29.48x 19E/20E P/E or 7.26x/6.19x 19E/20E P/B.

**Risk factors:** 1) Macroeconomic risk; 2) Commodity price risk; 3) Food safety risk; 4) M&A risk; 5) Investment risk; 6) Currency exchange risk

### Results and Valuation

FY ended Dec 31	2017A	2018A	2019E	2020E	2021E
Revenue (RMB mn)	68,058	79,553	90,563	102,567	116,040
Chg (% YoY)	12.29	16.89	13.84	13.26	13.14
Net Profit (to owners of the Company) (RMB mn)	6,001	6,440	6,835	7,218	8,386
Chg (% YoY)	5.99	7.31	6.13	5.61	16.18
Basic EPS (RMB)	0.99	1.06	1.12	1.18	1.38
Chg (% YoY)	6.45	7.07	5.75	5.61	16.18
P/E (x)	30.36	28.36	26.82	25.39	21.86
BVPS (RMB)	4.13	4.59	4.81	5.63	6.52
P/B (x)	7.28	6.55	6.26	5.34	4.61
DPS (RMB)	0.62	0.68	0.72	0.79	0.92
Yield (%)	2.07	2.25	2.38	2.61	3.06
ROAA (%)	13.56	13.29	13.05	11.95	13.63
ROAE (%)	24.91	24.29	23.89	22.68	22.63

Source(s): Bloomberg, ABCI Securities estimates

## Company Report

### Sep 11, 2019

### Rating: BUY

### TP: RMB 34.9

Analyst: Paul Pan  
Tel: (852) 2147 8829  
Email: paulpan@abci.com.hk

Share price (RMB)	30.06
52Wk H/L (RMB)	34.66/20.6
Est. share price return	16.10%
Est. dividend yield	2.38%
Est. total return	18.48%
Previous Rating&TP	BUY;RMB35.2
Previous report date	Nov 20, 2017

Source(s): Bloomberg, ABCI Securities

### Key Data

Issued shares (mn)	6,097.13
Market cap (RMB mn)	183,279.58
3-mth ADT (RMB mn)	1,739.48

### Major shareholders (%)

HK Securities Clearing Co	13.04
Hohhot Investment Co Ltd	8.83
Pan Gang	3.87
China Securities Finance Co	2.99
Sunshine Insurance	1.79

Source(s): , Bloomberg, Company

### % of core revenue

	FY19E
Liquid milk	82.89
Chilled product	6.28
Milk formula	10.83

Source(s): ABCI Securities estimates

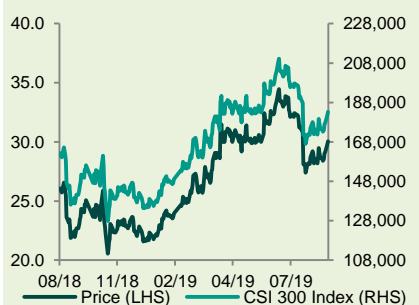
### Sector Performance (%)

	Absolute	Relative*
1-mth	9.71	0.55
3-mth	(7.31)	(15.44)
6-mth	14.86	6.37

\* Relative to CSI 300 Index

Source(s): Bloomberg, ABCI Securities

### 1-Year price performance (RMB)



Source(s): Bloomberg, ABCI Securities

\* All pricing and market data as of closing of Sep 10, 2019



**Exhibit 1: Quarterly financial performance**

	1Q18	2Q18	3Q18	4Q18	1Q19	2Q19
<b>Growth (YoY %)</b>						
Total revenue	25.10	14.05	12.68	16.93	17.10	8.67
Total gross profit	29.77	14.01	6.96	26.82	19.28	3.66
Operating profit	24.06	(23.60)	(7.08)	44.54	5.14	(1.66)
Pretax profit	22.10	(4.34)	0.47	31.60	9.08	8.38
Net profit (to owners of the company)	21.15	(17.47)	1.83	30.87	8.36	11.83
<b>Margins</b>						
GPM	39.35	39.08	36.02	38.85	40.09	37.28
OPM	12.05	7.05	7.49	7.31	10.82	6.38
Pretax margin	12.66	7.96	8.73	8.79	11.80	7.94
NPM (to owners of the Company)	10.63	6.66	7.49	7.64	9.84	6.86

Source(s): The Group, ABCI Securities

**Exhibit 2: Interim financial performance**

	1H18	1H19
<b>Growth (YoY %)</b>		
Total revenue	19.26	12.84
- Liquid milk	20.50	13.23
- Chilled products	14.89	15.43
- Milk formula	27.26	13.36
Total gross profit	21.32	11.41
- Liquid milk	20.57	13.03
- Chilled products	20.70	18.46
- Milk formula	20.27	9.96
Operating profit	2.79	2.60
EBITDA	1.54	4.90
Pretax profit	12.64	8.80
Net profit (to owners of the company)	2.43	9.71
<b>Margins</b>		
GPM	39.21	38.72
- Liquid milk	35.95	35.88
- Chilled products	46.14	47.35
- Milk formula	53.63	52.01
OPM	9.52	8.66
EBITDA margin	11.57	10.76
Pretax margin	10.29	9.92
NPM (to owners of the Company)	8.63	8.39

Source(s): The Group, ABCI Securities

**Exhibit 3: UHT product market share (%)**

Company	Market share	
	1H18	1H19
Mengniu	28.3	28.5
Yili	36.4	38.8
Company A	7.2	6.8
Company B	5.4	5.2
Others	22.7	20.7

Note: Nielsen offline retail data  
Source(s): Mengniu

**Exhibit 4: Chilled yogurt market share (%)**

Company	Market share	
	1H18	1H19
Mengniu	33.0	34.5
Yili	21.7	20.2
Company A	10.1	10.0
Company B	4.4	4.7
Others	30.8	30.1

Note: Nielsen offline retail data  
Source(s): Mengniu

**Exhibit 5: Fresh milk market share (%)**

Company	Market share	
	1H18	1H19
Mengniu	2.4	5.1
Yili	41.0	39.1
Company A	8.8	8.8
Company B	4.0	4.1
Others	43.8	42.9

Note: Nielsen offline retail data  
Source(s): Mengniu

**Exhibit 6: E-commerce - liquid milk (%)**

Company	Market share	
	1H18	1H19
Mengniu	24.0	26.5
Yili	21.4	24.3
Company A	6.3	5.7
Company B	5.4	3.0
Others	42.9	40.5

Note: Nielsen online retail research  
Source(s): Mengniu



## Financial Statements

### Consolidated income statement (2017A-2021E)

FY ends at Dec 31 (RMB mn, except per share data)	2017A	2018A	2019E	2020E	2021E
<b>Revenue</b>	<b>68,058</b>	<b>79,553</b>	<b>90,563</b>	<b>102,567</b>	<b>116,040</b>
- Core revenue	66,801	78,721	89,173	100,646	114,040
- Liquid milk	55,766	65,679	73,915	82,963	93,373
- Chilled product	4,606	4,997	5,598	6,235	7,113
- Milk formula	6,428	8,045	9,660	11,447	13,554
- Non-core revenue	747	256	862	1,169	1,383
- Interest income	511	577	528	752	617
COGS	(42,363)	(49,106)	(55,777)	(64,030)	(71,571)
<b>Gross profit</b>	<b>25,696</b>	<b>30,447</b>	<b>34,786</b>	<b>38,537</b>	<b>44,469</b>
- Core gross profit	25,063	29,785	34,116	37,590	43,622
- Liquid milk	19,611	23,126	26,311	28,488	32,889
- Chilled product	1,984	2,252	2,730	3,023	3,586
- Milk formula	3,468	4,406	5,074	6,079	7,148
- Non-core gross profit	122	86	142	195	229
- Gross profit on interest income	511	577	528	752	617
Business tax and levies	(512)	(531)	(626)	0	0
S&D expenses	(15,522)	(19,773)	(22,575)	(25,976)	(30,051)
Admin expenses	(3,108)	(2,980)	(3,998)	(4,511)	(5,094)
R&D expenses	(209)	(427)	(329)	(384)	(409)
<b>Operating profit</b>	<b>6,345</b>	<b>6,737</b>	<b>7,259</b>	<b>7,666</b>	<b>8,915</b>
Finance costs	(113)	60	14	22	13
Others	842	780	810	821	943
<b>Pretax profit</b>	<b>7,074</b>	<b>7,578</b>	<b>8,082</b>	<b>8,509</b>	<b>9,870</b>
Tax	(1,071)	(1,126)	(1,239)	(1,282)	(1,474)
<b>Net profit</b>	<b>6,003</b>	<b>6,452</b>	<b>6,843</b>	<b>7,227</b>	<b>8,396</b>
- Profit attributable to shareholders	6,001	6,440	6,835	7,218	8,386
- Minority interest	2	12	9	9	11
Cash dividend	3,792	4,110	4,360	4,790	5,607
<b>EPS (RMB)</b>					
- Basic	0.99	1.06	1.12	1.18	1.38
- Diluted	0.99	1.06	1.12	1.18	1.38
<b>Cash DPS (RMB)</b>	<b>0.62</b>	<b>0.68</b>	<b>0.72</b>	<b>0.79</b>	<b>0.92</b>

Source(s): Company, ABCI Securities estimates



**Consolidated balance sheet (2017A-2021E)**

FY ends at Dec 31 (RMB mn)	2017A	2018A	2019E	2020E	2021E
Cash and cash equivalent	21,823	11,051	19,103	21,549	10,108
Trade and bills receivable	950	1,282	1,376	1,667	1,980
Inventory	4,640	5,507	7,453	7,177	8,788
Others	2,433	6,615	2,532	2,651	3,342
<b>Total current assets</b>	<b>29,846</b>	<b>24,455</b>	<b>30,463</b>	<b>33,045</b>	<b>24,218</b>
PP&E	13,256	14,688	17,218	18,874	20,069
Goodwill	11	11	11	11	11
AFS investment	652	831	914	1,006	1,106
LT equity investment	1,765	1,909	2,218	2,586	2,922
Others	3,771	5,712	6,345	8,126	11,091
<b>Total non-current assets</b>	<b>19,455</b>	<b>23,151</b>	<b>26,707</b>	<b>30,602</b>	<b>35,199</b>
<b>Total assets</b>	<b>49,300</b>	<b>47,606</b>	<b>57,170</b>	<b>63,646</b>	<b>59,417</b>
Trade and bills payable	7,469	9,116	11,123	553	848
ST borrowings	7,860	1,523	1,964	2,066	1,997
Others	8,521	8,532	13,296	24,723	14,802
<b>Total current liabilities</b>	<b>23,850</b>	<b>19,171</b>	<b>26,383</b>	<b>27,342</b>	<b>17,647</b>
LT Borrowings	0	0	8	8	8
Others	210	398	1,242	1,671	1,694
<b>Total non-current liabilities</b>	<b>211</b>	<b>398</b>	<b>1,250</b>	<b>1,678</b>	<b>1,701</b>
Shareholders' equity	25,103	27,916	29,300	34,349	39,748
Minority interest	136	122	237	278	321
<b>Total equity</b>	<b>25,240</b>	<b>28,037</b>	<b>29,537</b>	<b>34,627</b>	<b>40,069</b>
<b>Total liabilities and equity</b>	<b>49,300</b>	<b>47,606</b>	<b>57,170</b>	<b>63,646</b>	<b>59,417</b>

Source(s): Company, ABCI Securities estimates

**Consolidated cash flow statement (2017A-2021E)**

FY ends at Dec 31 (RMB mn)	2017A	2018A	2019E	2020E	2021E
Net profit	6,003	6,452	6,843	7,227	8,396
Depreciation and amortization	1,495	1,684	1,928	2,176	2,434
Change in working capital	(613)	530	1,670	1,578	118
Others	121	(42)	134	222	80
<b>Cash flow from operating activities</b>	<b>7,006</b>	<b>8,625</b>	<b>10,576</b>	<b>11,202</b>	<b>11,028</b>
Change in PP&E, intangible assets, and other non-current assets	(3,279)	(5,043)	(7,292)	(9,523)	(13,647)
Others	162	(331)	(90)	(187)	(127)
<b>Cash flow from investing activities</b>	<b>(3,117)</b>	<b>(5,374)</b>	<b>(7,382)</b>	<b>(9,709)</b>	<b>(13,775)</b>
Change in borrowings	7,710	(6,337)	449	102	(69)
Cash flow related to dividend payment, interest payment, or profit distribution	(3,845)	(4,393)	(4,051)	(4,399)	(4,808)
Others	188	(19)	0	0	0
<b>Cash flow from financing activities</b>	<b>4,053</b>	<b>(10,749)</b>	<b>(3,602)</b>	<b>(4,297)</b>	<b>(4,878)</b>
<b>Net change in cash</b>	<b>7,942</b>	<b>(7,498)</b>	<b>(409)</b>	<b>(2,804)</b>	<b>(7,624)</b>
ForEx effect	(398)	307	33	44	(3)
<b>Cash and cash equivalent - end</b>	<b>20,756</b>	<b>13,565</b>	<b>13,188</b>	<b>10,429</b>	<b>2,802</b>

Source(s): Company, ABCI Securities estimates



**Key operating and financial ratios (2017A-2021E)**

FY ends at Dec 31	2017A	2018A	2019E	2020E	2021E
<b>Growth (YoY %)</b>					
Revenue	12.29	16.89	13.84	13.26	13.14
Core revenue	12.06	17.84	13.28	12.87	13.31
- Liquid milk	12.61	17.78	12.54	12.24	12.55
- Chilled products	9.82	8.49	12.03	11.37	14.08
- Milk formula	17.83	25.14	20.08	18.50	18.40
Non-core revenue	6.92	(65.74)	236.79	35.68	18.29
Gross profit	10.84	18.49	14.25	10.78	15.39
Core gross profit	9.87	18.84	14.54	10.18	16.05
- Liquid milk	10.12	17.93	13.77	8.27	15.45
- Chilled products	9.89	13.48	21.26	10.72	18.61
- Milk formula	13.17	27.05	15.16	19.80	17.58
Non-core gross profit	69.56	(29.64)	66.27	36.62	17.88
Operating profit	22.24	6.18	7.74	5.61	16.30
EBITDA	14.50	7.15	8.99	7.08	15.55
Pretax Profit	6.66	7.12	6.66	5.28	15.99
Net profit (to owners of the Company)	5.99	7.31	6.13	5.61	16.18
<b>Profitability ratios (%)</b>					
GPM	37.76	38.27	38.41	37.57	38.32
Core-GPM	37.52	37.84	38.26	37.35	38.25
- Liquid milk	35.17	35.21	35.60	34.34	35.22
- Chilled products	43.08	45.06	48.77	48.48	50.41
- Milk formula	53.95	54.78	52.53	53.11	52.74
Non-core GPM	16.30	33.49	16.53	16.65	16.59
OPM	9.32	8.47	8.02	7.47	7.68
EBITDA margin	11.44	10.49	10.04	9.50	9.70
Pretax margin	10.39	9.53	8.92	8.30	8.51
NPM (to owners of the Group)	8.82	8.09	7.55	7.04	7.23
<b>Revenue contribution (%)</b>					
Core revenue/ total revenue	98.15	98.95	98.47	98.13	98.28
Non-core revenue/ total revenue	1.10	0.32	0.95	1.14	1.19
Interest income/ total revenue	0.75	0.73	0.58	0.73	0.53
<b>Core revenue composition</b>					
- Liquid milk	83.48	83.43	82.89	82.43	81.88
- Chilled products	6.90	6.35	6.28	6.20	6.24
- Milk formula	9.62	10.22	10.83	11.37	11.89
<b>Return ratios (%)</b>					
ROAA	13.56	13.29	13.05	11.95	13.63
ROAE	24.91	24.29	23.89	22.68	22.63
<b>Liquidity ratio (x)</b>					
Current ratio	1.25	1.28	1.15	1.21	1.37
Quick ratio	1.06	0.99	0.87	0.95	0.87
Cash ratio	0.92	0.58	0.72	0.79	0.57
<b>Cash conversion cycle (days)</b>					
Days of outstanding receivable	3.6	4.3	4.6	4.6	4.9
Days of inventory on hand	39.2	37.8	43.0	42.3	41.4
Days of outstanding payable	60.8	59.0	61.3	63.4	61.7
CCC	(17.9)	(16.8)	(13.8)	(16.4)	(15.4)
<b>Leverage ratios (%)</b>					
Total debt/Equity	31.14	5.43	6.68	5.99	5.00
Total debt/Total assets	15.94	3.20	3.45	3.26	3.37

Source(s): Company, ABCI Securities estimates



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Rating	Definition
Buy	Stock return $\geq$ Market return rate (10%)
Hold	- Market return (-10%) $\leq$ Stock return < 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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Office address: ABCI Securities Company Limited, 13/F Fairmont House, 8 Cotton Tree Drive, Central, Hong Kong.  
Tel: 852) 2868 2183