



Mengniu (2319 HK)

Improved margins and decent growth in 1H19; maintain BUY

- 1H19 revenue grew 15.6% YoY, supported by liquid milk and milk formula segments revenue growth of 14.4% YoY and 45.1% YoY; GPM contracted to 39.1% in 1H19 while OPM and NPM (to owners of the Company) rose to 5.8% and 5.2%
- The Group's market share in multiple product segments remains dominant in 1H19
- Expect FY18-21E revenue CAGR to reach 12.3%; more challenges ahead due to the deteriorating macroeconomic environment and rising raw milk costs
- Maintain **BUY**; current TP represents 33.87x/25.75x 19E/20E P/E, and 4.48x/4.01x 19E/20E P/B

1H19 revenue grew 15.6% YoY. Revenue growth of liquid milk and milk formula segments reached 14.4% YoY and 45.1% YoY, but revenue from ice cream segment was down 2.4% YoY. 1H19 revenue growth was lower than that of 1H18 by 1.4ppt. We believe the weakened momentum reflects the general decline in retail sales and economic growth in China.

Mixed margin performance. GPM contracted slightly to 39.1% in 1H19 from 39.2% in 1H18. OPM and NPM (to owners of the Company), however, improved to 5.8% and 5.2% in 1H19 from 5.6% and 4.5% in 1H18. Higher OPM in 1H19 was mainly supported by the reduction in SG&A/revenue ratio; higher NPM (to owners of the Company) can be partially attributed to positive share of profit from associates, which was negative in 1H18.

Leading shares in product categories. The Group's market share in different product categories remains dominant. For the offline UHT product market and chilled yogurt product market, its market share edged up 0.2ppt YoY and 1.5ppt YoY to 28.5% and 34.5% in 1H19. For the online liquid milk product market, its market share increased by 2.5ppt YoY to 26.5% in 1H19. Market share of its newly-developed fresh milk product segment increased to 5.1% in 1H19, as compared with the top player's 39.1%.

FY18-21E revenue CAGR to reach 12.3%. We expect revenue growth would be mainly supported by the liquid milk and milk formula segments, whose revenue CAGRs are estimated to be 11.5% and 21.7% in FY18-21E. Slowdown in economic and consumption growth, strong competition in the domestic dairy market, and rising raw milk costs. Sales of Junlebao may suppress growth in the short term. Nonetheless, we expect GPM and NPM (to owners of the Company) would improve from 37.4% and 4.4% in FY18 to 39.0% and 5.7% in FY21E on enhancing economies of scale and stable SG&A expenses.

Maintain BUY; TP at HK\$ 34.6. The Group was able to maintain leading market shares in multiple product categories in 1H19, showing the resilience of the Group's business. However, the slowing growth rate and mixed profitability performance in 1H19 are causes for concern. Maintain **BUY**. Our DCF-derived TP represents 33.87x/25.75x 19E/20E P/E, and 4.48x/4.01x 19E/20E P/B.

Risk factors: 1) Macroeconomic risk; 2) Commodity price risk; 3) Food safety risk; 4) M&A risk, 5) Product concentration risk; 6) Product competitiveness risk; 7) Biological asset revaluation risk; 8) Currency exchange risk.

Results and Valuation

FY ended Dec 31	2017A	2018A	2019E	2020E	2021E
Revenue (RMB mn)	60,156	68,977	77,013	86,242	97,787
Chg (% YoY)	11.86	14.66	11.65	11.98	13.39
Net Profit (RMB mn)	2,048	3,043	3,645	4,798	5,603
Chg (% YoY)	N/A	48.60	19.80	31.61	16.79
Basic EPS (RMB)	0.53	0.78	0.93	1.22	1.42
Chg (% YoY)	N/A	48.10	19.08	31.52	16.79
P/E (x)	52.13	35.20	29.56	22.48	19.25
BVPS (RMB)	5.76	6.41	7.02	7.83	8.74
P/B (x)	4.76	4.28	3.91	3.50	3.14
DPS (RMB)	0.12	0.19	0.26	0.36	0.47
Yield (%)	0.44	0.69	0.95	1.32	1.72
ROAA (%)	3.82	4.88	5.17	6.06	6.16
ROAE (%)	9.43	12.73	13.78	16.37	17.13

Source(s): Bloomberg, ABCI Securities estimates

Company Report

Sep 11, 2019

Rating: BUY

TP: HK\$ 34.6

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Share price (HK\$)	30.20
52Wk H/L(HK\$)	34.6/21.105
Est. share price return	14.57%
Est. dividend yield	0.95%
Est. total return	15.52%
Previous Rating&TP	BUY;HK\$29.36
Previous report date	Apr 4, 2018

Source(s): Bloomberg, ABCI Securities

Key Data

Issued shares (mn)	3,932.44
Market cap (HK\$ mn)	118,759.75
3-mth ADT (HK\$ mn)	276.79

Major shareholders

	(%)
COFCO	31.39
Schroder	6.97
FIL Limited	6.54

Source(s): Bloomberg, HKEX

Revenue composition

	FY19E
Liquid milk	85.72
Ice cream	3.44
Milk formula	9.29

Source(s): ABCI Securities estimates

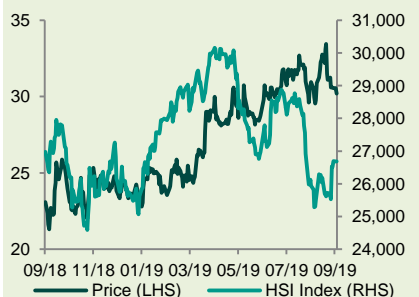
Sector Performance (%)

	Absolute	Relative*
1-mth	(2.42)	(5.92)
3-mth	(1.79)	0.81
6-mth	21.85	25.61

* Relative to HSI

Source(s): Bloomberg, ABCI Securities

1-Year price performance (HK\$)



Source(s): Bloomberg, ABCI Securities

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



Exhibit 1: 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): The Group

Exhibit 2: 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): The Group

Exhibit 3: 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): The Group

Exhibit 4: 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): The Group

Exhibit 5: Interim result comparison

	1H18	1H19
Growth (YoY %)		
Revenue	17.00	15.61
- Liquid milk	14.03	14.44
- Ice cream	12.82	(2.40)
- Milk formula	63.56	45.05
Gross profit	28.75	15.21
Operating profit	7.76	18.41
Net profit (to owners of the Company)	38.49	32.96
Margin (%)		
GPM	39.22	39.09
OPM	5.64	5.78
NPM (to owners of the Company)	4.53	5.21
Revenue composition (%)		
Liquid milk	83.92	83.07
Ice cream	6.50	5.48
Milk formula	8.48	10.63
Others	1.03	0.81

Source(s): The Group, ABCI Securities



Financial Statements

Consolidated income statement (2017A-2021E)

FY ends at Dec 31 (RMB mn, except per share data)	2017A	2018A	2019E	2020E	2021E
Revenue	60,156	68,977	77,013	86,242	97,787
- Liquid milk	53,015	59,389	66,019	72,989	82,240
- Ice cream	2,513	2,723	2,649	2,764	2,883
- Milk formula	4,042	6,017	7,152	8,846	10,857
- Other revenue	585	851	1,193	1,642	1,806
COGS	(38,973)	(43,193)	(47,201)	(52,589)	(59,676)
Gross profit	21,183	25,784	29,813	33,653	38,110
Other income	338	736	546	630	671
SG&A	(17,366)	(21,748)	(25,103)	(27,684)	(31,347)
Other expenses	(1,099)	(851)	(1,155)	(1,294)	(1,467)
EBIT	2,972	3,835	4,100	5,306	5,967
Net interest expense(-)/income(+)	184	318	654	1,306	1,754
Income from associate/JV	(532)	(300)	(39)	53	60
Profit before tax	2,625	3,853	4,715	6,664	7,781
Tax	(594)	(649)	(1,064)	(1,505)	(1,756)
Total net profit	2,031	3,204	3,651	5,159	6,025
- Profit to shareholders	2,048	3,043	3,645	4,798	5,603
- Minority interest	(17)	161	6	361	422
EPS (RMB)					
- Basic EPS	0.53	0.78	0.93	1.22	1.42
- Diluted EPS	0.53	0.78	0.93	1.21	1.42
DPS	0.12	0.19	0.26	0.36	0.47

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	5,959	7,298	19,973	23,212	31,754
Trade and bills receivable	2,647	2,892	3,334	3,655	4,288
Inventory	3,510	4,282	5,403	6,280	6,941
Others	13,902	15,269	7,673	8,391	8,830
Total current assets	26,018	29,741	36,383	41,538	51,812
PP&E and CIP	14,079	16,937	17,022	18,475	20,222
Goodwill	4,533	4,681	4,681	4,681	4,681
Other intangible assets	2,194	2,298	1,922	2,011	2,130
Others	11,315	12,799	14,632	16,870	19,525
Total non-current assets	32,121	36,716	38,258	42,038	46,559
Total assets	58,139	66,457	74,641	83,576	98,371
Trade and bills payable	6,342	7,022	7,359	8,564	9,357
ST borrowings	7,935	6,523	9,343	11,760	14,448
Others	8,289	11,565	13,166	14,347	15,110
Total current liabilities	22,566	25,109	29,868	34,670	38,915
LT Borrowings	6,015	8,192	6,640	6,658	6,677
Others	2,450	2,691	5,164	5,883	12,607
Total non-current liabilities	8,465	10,884	11,804	12,540	19,284
Shareholders' equity	22,604	25,212	27,713	30,918	34,499
Minority interest	4,503	5,252	5,255	5,448	5,673
Total equity	27,107	30,464	32,968	36,366	40,172
Total liabilities and equity	58,139	66,457	74,641	83,576	98,371

Source(s): Company, ABCI Securities estimates



Consolidated cash flow statement (2017A-2021E)

FY ends at Dec 31 (RMB mn)	2017A	2018A	2019E	2020E	2021E
Pretax profit	2,625	3,853	4,715	6,664	7,781
Depreciation and amortization	1,704	1,838	2,568	2,903	3,249
Change in working capital	1,229	1,637	1,113	1,222	1,108
Others	(52)	(965)	(1,718)	(2,984)	(4,310)
Cash flow from operating activities	5,505	6,363	6,679	7,805	7,828
Capex	(66,501)	(6,460)	(6,093)	(7,559)	(9,261)
Others	55,051	2,229	1,263	2,493	(2,318)
Cash flow from investing activities	(11,450)	(4,232)	(4,830)	(5,066)	(11,579)
Change in borrowings	4,479	(300)	1,268	2,434	2,707
Dividends paid	(399)	(526)	(818)	(1,025)	(1,594)
Others	1,668	(74)	9,972	(677)	11,103
Cash flow from financing activities	5,748	(900)	10,422	732	12,216
Net change in cash	(196)	1,231	12,271	3,471	8,464
Forex effect	(31)	10	(57)	(44)	(53)
Cash and cash equivalent - end	3,129	4,370	16,584	20,011	28,423

Source(s): Company, ABCI Securities estimates

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

FY ends at Dec 31	2017A	2018A	2019E	2020E	2021E
Growth (YoY %)					
Revenue	11.86	14.66	11.65	11.98	13.39
- Liquid milk	10.21	12.02	11.16	10.56	12.67
- Ice cream	15.28	8.37	(2.74)	4.35	4.32
- Milk powder	28.28	48.87	18.86	23.68	22.73
- Other products	69.40	45.30	40.21	37.65	10.00
Gross profit	20.11	21.72	15.63	12.88	13.24
Operating profit	N/A	29.02	6.91	29.40	12.47
Net profit (to owners of the Group)	N/A	48.60	19.80	31.61	16.79
Profitability ratios (%)					
GPM	35.21	37.38	38.71	39.02	38.97
OPM	4.94	5.56	5.32	6.15	6.10
EBITDA margin	6.89	8.23	8.66	9.52	9.42
NPM (to owners of the Group)	3.40	4.41	4.73	5.56	5.73
Return ratios (%)					
ROAA	3.82	4.88	5.17	6.06	6.16
ROAE	9.43	12.73	13.78	16.37	17.13
Liquidity ratio (x)					
Current ratio	1.15	1.18	1.22	1.20	1.33
Quick ratio	1.00	1.01	1.04	1.02	1.15
Cash ratio	0.28	0.32	0.69	0.69	0.84
Cash conversion cycle (days)					
Days of outstanding receivable	15.1	14.7	14.8	14.8	14.8
Days of inventory on hand	32.0	32.9	37.4	40.5	40.4
Days of outstanding payable	54.7	55.5	54.3	54.3	54.2
CCC	(7.7)	(7.9)	(2.1)	1.0	1.0
Leverage ratios (%)					
Total debt/Equity	51.46	48.30	48.89	51.02	52.95
Total debt/Total assets	23.99	22.14	21.41	22.04	21.47
Net debt/Equity	27.76	22.30	(14.18)	(15.26)	(28.53)
Net debt/Assets	12.94	10.22	(6.26)	(6.64)	(11.65)

Note: The Group recorded operating loss and net loss in FY16

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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