

Hong Kong

**ADD** (no change)

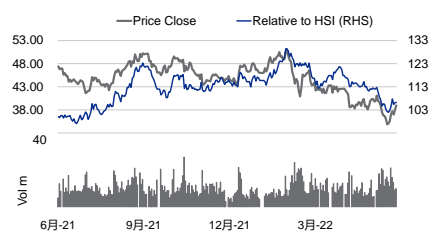
Consensus ratings\*: Buy 34 Hold 2 Sell 1

Current price:	HK\$38.95
Target price:	HK\$52.30
Previous target:	HK\$54.40
Up/downside:	34.3%
CGI / Consensus:	-2.4%
Reuters:	2319.HK
Bloomberg:	2319 HK
Market cap:	US\$19,623m
	HK\$154,025m
Average daily turnover:	US\$57.79m
	HK\$452.9m
Current shares o/s:	3,945m
Free float:	68.7%

\*Source: Bloomberg

**Key changes in this note**

- FY22F EPS decreased by 7.95%.
- FY23F EPS decreased by 6.50%.
- FY24F EPS decreased by 5.33%.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	0.4	-11.8	-18.5
Relative (%)	-7	-15.7	5.6

**Major shareholders**

	% held
COFCO	16.3
Danone	9.9
Arla	5.3

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# China Mengniu Dairy

## 1H22F weak sales due to the pandemic impact

- We now expect the top line to grow by 5% yoy in 1H22F and 10.9% yoy in FY22F.
- We expect to see a yoy improvement in Mengniu's OPM in 2H22F after a yoy decline in 1H22F.
- Sales growth of mass market white milk products was 17–18% yoy in 5M22F, and the growth of fresh milk and high-end Milk Deluxe was 25–26% yoy and in the double digits yoy.
- If the pandemic situation stabilizes in 2H22F, we expect Mengniu to continue its new product launches and promotion campaigns.
- Reiterate Add with a new DCF-based TP of HK\$52.3 because of mild sales growth in 1H22F.

### Mild 1H22F outlook because of the pandemic rebound

In Mar–May, the pandemic rebound hit multiple cities in China. According to our channel check, while demand and sales in Shanghai was satisfactory, it was negatively affected in some other cities, as distributors maintained a cautious attitude toward stocking amid the pandemic fluctuations, and the product mix shifted to mass market white milk products. If the pandemic situation stabilizes in 2H22F, we are still confident that Mengniu will make up some sales. We now expect its top line to grow by 5% yoy in 1H22F and 10.9% yoy in FY22F. Because of weak sales, a high base and a poor product mix amid the pandemic, the 1H22F margin is under pressure. In addition, although the domestic raw milk price has been stable in 1H22F, the price of some other raw materials, such as milk powder, packaging materials and palm oil, have risen significantly, negatively affecting the gross margin in 1H22F. We expect the 2H22F raw milk price to remain stable. On the bright side, because of the weak macro, we expect Mengniu to continue to cut its selling and marketing expenses for the rest of the year. We now expect its OPM to decline by 0.3% pts yoy in 1H22F, but to be flat yoy in 2H22F.

### Liquid milk products outperform

According to our channel check, sales growth of mass market white milk products was 17–18% yoy in 5M22F, and the growth of fresh milk and high-end Milk Deluxe was 25–26% yoy and in the double digits yoy. Sales growth of cheese and ice-cream products was also positive. However, sales of room temperature yogurt and dairy drinks were affected, as outdoor consumption was significantly affected by the pandemic rebound. If the pandemic situation stabilizes in 2H22F, we expect Mengniu to continue its new product launches and promotion campaigns. It already started some promotion campaigns for room temperature yogurt and dairy drinks in Jun.

### Restructuring the milk powder business

Mengniu's milk powder business underperformed that of its peers in 1H22F. We expect Mengniu to privatize Yashili (1230 HK, Not rated) and to restructure its milk powder business. By privatizing Yashili, we expect Mengniu to better allocate resources internally for its milk powder business and generate more synergy. Going forward, Mengniu will focus more on Mengniu branded milk powder products to strengthen its brand image and improve sales growth according to the management.

### Reiterate Add with new DCF-based TP of HK\$52.3

We cut our FY22F–24F EPS forecasts by 7.95%, 6.50% and 5.33%, respectively. We adjusted down our DCF-based TP to HK\$52.3 (risk free rate: 4.0%, beta: 0.95, WACC: 8.8%) because of mild sales growth in 1H22F. We reiterate our Add rating as we still see large growth potential from a mix upgrade, distribution channel reforms and global expansion. Positive catalysts include better margin improvement and stronger sales growth. The main risks are stronger price competition and a higher raw milk price that hurt revenue growth and margin of Mengniu.

Financial Summary	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Revenue (Rmbm)	76,035	88,141	97,784	109,304	120,639
Operating EBITDA (Rmbm)	4,883	6,149	6,725	8,179	9,345
Net Profit (Rmbm)	3,525	5,026	5,393	6,571	7,573
Core EPS (Rmb)	0.89	1.27	1.37	1.67	1.93
Core EPS Growth	(11.1%)	42.8%	7.8%	21.8%	15.3%
FD Core P/E (x)	37.25	26.08	24.20	19.86	17.23
DPS (Rmb)	0.27	0.38	0.41	0.50	0.58
Dividend Yield	0.81%	1.15%	1.24%	1.51%	1.74%
EV/EBITDA (x)	27.44	22.37	19.71	15.58	13.02
P/FCFE (x)	21.03	NA	26.11	21.75	18.25
Net Gearing	20.3%	40.7%	27.4%	15.0%	3.8%
P/BV (x)	3.96	3.56	3.14	2.78	2.46
ROE	11.4%	14.4%	13.8%	14.8%	15.1%
% Change In Core EPS Estimates			(7.95%)	(6.50%)	(5.33%)
CGI/consensus EPS (x)			0.90	0.92	0.91

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

# 1H22F weak sales due the pandemic impact

**Figure 1: Mengniu earnings revision**

Key assumptions	FY22F			FY23F			FY24F		
	Old	New	% change	Old	New	% change	Old	New	% change
Sales (Rmbm)	99,262	97,784	-1.5%	109,056	109,304	0.2%	119,690	120,639	0.8%
Overall gross margin	36.6%	36.4%	-0.2%	37.2%	37.0%	-0.2%	37.4%	37.2%	-0.2%
-Mengniu standalone	36.6%	36.4%	-0.2%	37.1%	36.9%	-0.2%	37.3%	37.1%	-0.2%
-Yashili	37.6%	37.6%	0.0%	38.1%	38.1%	0.0%	39.1%	39.1%	0.0%
Overall operating margin	5.8%	5.4%	-0.5%	6.4%	5.9%	-0.5%	6.7%	6.2%	-0.5%
-Mengniu standalone	6.0%	5.5%	-0.5%	6.7%	6.1%	-0.5%	6.9%	6.4%	-0.5%
-Yashili	2.5%	2.5%	0.0%	3.0%	3.0%	0.0%	3.5%	3.5%	0.0%
Mengniu's standalone net profit	5,103	4,637	-9.1%	6,129	5,672	-7.5%	6,925	6,499	-6.2%
Share of profits from CMD	647	647	0.0%	764	764	0.0%	891	891	0.0%
Yashili's profit attributable to Mengniu	109	109	0.0%	134	134	0.0%	182	182	0.0%
Overall reported net profit	5,859	5,393	-7.9%	7,028	6,571	-6.5%	7,999	7,573	-5.3%
Core earnings	5,859	5,393	-7.9%	7,028	6,571	-6.5%	7,999	7,573	-5.3%

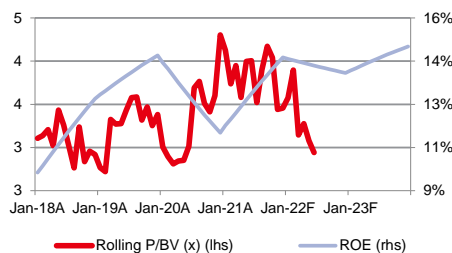
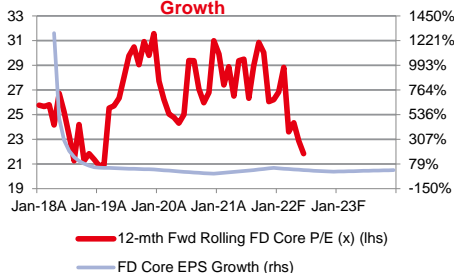
SOURCES: CGIS RESEARCH ESTIMATES

**Figure 2: Mengniu DCF valuation**

DCF valuation (Rmb m)	FY22F	FY23F	FY24F	FY25F	FY26F	FY27F	FY28F	FY29F	FY30F	FY31F	FY32F	FY33F	FY34F
<b>EBIT</b>	<b>5,237.2</b>	<b>6,477.7</b>	<b>7,518.3</b>	<b>8,747.4</b>	<b>10,193.9</b>	<b>11,898.6</b>	<b>13,910.7</b>	<b>16,289.2</b>	<b>19,104.9</b>	<b>22,443.0</b>	<b>26,406.5</b>	<b>31,119.3</b>	<b>36,731.7</b>
Taxes	-1,013.1	-1,234.5	-1,427.7	-1,661.1	-1,935.7	-2,259.5	-2,641.5	-3,093.2	-3,627.9	-4,261.8	-5,014.4	-5,909.3	-6,975.1
<b>NOPAT</b>	<b>4,224.1</b>	<b>5,243.2</b>	<b>6,090.6</b>	<b>7,086.3</b>	<b>8,258.1</b>	<b>9,639.2</b>	<b>11,269.2</b>	<b>13,196.0</b>	<b>15,477.0</b>	<b>18,181.2</b>	<b>21,392.1</b>	<b>25,210.0</b>	<b>29,756.6</b>
<b>NOPAT growth</b>	<b>6.3%</b>	<b>24.1%</b>	<b>16.2%</b>	<b>16.3%</b>	<b>16.5%</b>	<b>16.7%</b>	<b>16.9%</b>	<b>17.1%</b>	<b>17.3%</b>	<b>17.5%</b>	<b>17.7%</b>	<b>17.8%</b>	<b>18.0%</b>
D&A	1,487.6	1,701.2	1,826.2	1,844.5	1,862.9	1,881.6	1,900.4	1,919.4	1,938.6	1,958.0	1,977.5	1,997.3	2,017.3
<b>Funds from operation</b>	<b>5,711.7</b>	<b>6,944.5</b>	<b>7,916.8</b>	<b>8,930.8</b>	<b>10,121.1</b>	<b>11,520.7</b>	<b>13,169.6</b>	<b>15,115.4</b>	<b>17,415.6</b>	<b>20,139.2</b>	<b>23,369.6</b>	<b>27,207.3</b>	<b>31,773.9</b>
Change in net working Capital	685.4	322.0	358.3	361.9	365.5	369.2	372.9	376.6	380.4	384.2	388.0	391.9	395.8
<b>Cash flow from operation</b>	<b>6,397.1</b>	<b>7,266.5</b>	<b>8,275.2</b>	<b>9,292.7</b>	<b>10,486.6</b>	<b>11,889.9</b>	<b>13,542.5</b>	<b>15,492.0</b>	<b>17,795.9</b>	<b>20,523.4</b>	<b>23,757.6</b>	<b>27,599.2</b>	<b>32,169.7</b>
Capex	-2,500.0	-2,500.0	-2,500.0	-2,525.0	-2,550.3	-2,575.8	-2,601.5	-2,627.5	-2,653.8	-2,680.3	-2,707.1	-2,734.2	-2,761.6
<b>Free cash flow from operation</b>	<b>3,897.1</b>	<b>4,766.5</b>	<b>5,775.2</b>	<b>6,767.7</b>	<b>7,936.3</b>	<b>9,314.2</b>	<b>10,941.0</b>	<b>12,864.5</b>	<b>15,142.1</b>	<b>17,843.0</b>	<b>21,050.5</b>	<b>24,865.0</b>	<b>29,408.2</b>
<b>FCF growth</b>	<b>1034.8%</b>	<b>22.3%</b>	<b>21.2%</b>	<b>17.2%</b>	<b>17.3%</b>	<b>17.4%</b>	<b>17.5%</b>	<b>17.6%</b>	<b>17.7%</b>	<b>17.8%</b>	<b>18.0%</b>	<b>18.1%</b>	<b>18.3%</b>
Terminal free cash flow	520,702.3	<b>Assumptions</b>											
Total discounted free cash flow	83,603.7	Equity Beta 0.95											
Present value of terminal free cash flow	176,546.8	Risk Free Rate 4.0%											
		Market Risk Premium 6.8%											
<b>Total present value of forecasted free cash flows</b>	<b>260,150.5</b>	<b>Cost of Equity 10.5%</b>											
Less: Net Debt / (Cash)	12,822.3	Cost of Debt 3.0%											
<b>Equity Value</b>	<b>247,328.2</b>	Effective Tax Rate 24.5%											
No. of outstanding shares (millions)	3,927.4	Target Gearing 20.0%											
<b>Per share Equity Value (Rmb)</b>	<b>63.0</b>	<b>WACC 8.8%</b>											
Exchange rate	0.8	<b>Terminal growth rate 3.0%</b>											
<b>Target price (HK\$)</b>	<b>52.30</b>												

SOURCES: CGS-CIMB RESEARCH ESTIMATES, COMPANY REPORTS, BLOOMBERG

## BY THE NUMBERS

**P/BV vs ROE**

**12-mth Fwd FD Core P/E vs FD Core EPS Growth**


### Profit & Loss

(Rmbm)	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
<b>Total Net Revenues</b>	<b>76,035</b>	<b>88,141</b>	<b>97,784</b>	<b>109,304</b>	<b>120,639</b>
<b>Gross Profit</b>	<b>28,629</b>	<b>32,390</b>	<b>35,629</b>	<b>40,422</b>	<b>44,909</b>
<b>Operating EBITDA</b>	<b>4,883</b>	<b>6,149</b>	<b>6,725</b>	<b>8,179</b>	<b>9,345</b>
Depreciation And Amortisation	-1,667	-1,259	-1,488	-1,701	-1,826
<b>Operating EBIT</b>	<b>3,216</b>	<b>4,891</b>	<b>5,237</b>	<b>6,478</b>	<b>7,518</b>
Financial Income/(Expense)	512	284	381	396	412
Pretax Income/(Loss) from Assoc.	426	693	871	1,032	1,213
Non-Operating Income/(Expense)	0	0	0	0	0
<b>Profit Before Tax (pre-EI)</b>	<b>4,155</b>	<b>5,868</b>	<b>6,489</b>	<b>7,906</b>	<b>9,144</b>
Exceptional Items					
<b>Pre-tax Profit</b>	<b>4,155</b>	<b>5,868</b>	<b>6,489</b>	<b>7,906</b>	<b>9,144</b>
Taxation	-653	-905	-1,013	-1,234	-1,428
Exceptional Income - post-tax					
<b>Profit After Tax</b>	<b>3,502</b>	<b>4,964</b>	<b>5,476</b>	<b>6,672</b>	<b>7,716</b>
Minority Interests	23	62	-82	-101	-143
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
<b>Net Profit</b>	<b>3,525</b>	<b>5,026</b>	<b>5,393</b>	<b>6,571</b>	<b>7,573</b>
Recurring Net Profit	3,525	5,026	5,393	6,571	7,573
<b>Fully Diluted Recurring Net Profit</b>	<b>3,525</b>	<b>5,026</b>	<b>5,393</b>	<b>6,571</b>	<b>7,573</b>

### Cash Flow

(Rmbm)	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
<b>EBITDA</b>	<b>4,883</b>	<b>6,149</b>	<b>6,725</b>	<b>8,179</b>	<b>9,345</b>
Cash Flow from Invt. & Assoc.					
Change In Working Capital	967	1,158	685	322	358
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	830	-5	720	837	964
Net Interest (Paid)/Received	-580	-644	-780	-819	-860
Tax Paid	-753	-1,310	-1,013	-1,234	-1,428
<b>Cashflow From Operations</b>	<b>5,348</b>	<b>5,348</b>	<b>6,337</b>	<b>7,284</b>	<b>8,379</b>
Capex	-4,414	-6,047	-2,500	-2,500	-2,500
Disposals Of FAs/subsidiaries	126	0	0	0	0
Acq. Of Subsidiaries/investments	-1,224	-6,667	0	0	-0
Other Investing Cashflow	10,334	-5,439	1,161	1,216	1,273
<b>Cash Flow From Investing</b>	<b>4,822</b>	<b>-18,153</b>	<b>-1,339</b>	<b>-1,284</b>	<b>-1,227</b>
Debt Raised/(repaid)	-3,926	4,108	0	0	0
Proceeds From Issue Of Shares	257	0	0	0	0
Shares Repurchased					
Dividends Paid	-785	-1,058	-712	-1,058	-1,506
Preferred Dividends					
Other Financing Cashflow	-116	-11	0	0	0
<b>Cash Flow From Financing</b>	<b>-4,571</b>	<b>3,038</b>	<b>-712</b>	<b>-1,058</b>	<b>-1,506</b>
Total Cash Generated	5,599	-9,767	4,286	4,942	5,646
<b>Free Cashflow To Equity</b>	<b>6,244</b>	<b>-8,697</b>	<b>4,998</b>	<b>6,000</b>	<b>7,152</b>
<b>Free Cashflow To Firm</b>	<b>10,750</b>	<b>-12,161</b>	<b>5,778</b>	<b>6,819</b>	<b>8,012</b>

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

## BY THE NUMBERS... cont'd

### Balance Sheet

(Rmbm)	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Total Cash And Equivalents	11,397	11,217	15,503	20,445	26,090
Total Debtors	2,991	4,162	4,290	4,825	5,359
Inventories	5,512	6,485	7,121	7,986	8,884
Total Other Current Assets	11,606	9,156	10,173	12,493	15,304
<b>Total Current Assets</b>	<b>31,507</b>	<b>31,020</b>	<b>37,087</b>	<b>45,749</b>	<b>55,637</b>
Fixed Assets	15,276	19,955	20,967	21,766	22,440
Total Investments	16,878	30,092	30,315	30,583	30,905
Intangible Assets	12,601	12,857	12,784	12,711	12,639
Total Other Non-Current Assets	3,885	4,178	4,178	4,178	4,178
<b>Total Non-current Assets</b>	<b>48,640</b>	<b>67,081</b>	<b>68,244</b>	<b>69,238</b>	<b>70,161</b>
Short-term Debt	4,924	4,265	4,265	4,265	4,265
Current Portion of Long-Term Debt					
Total Creditors	7,969	8,804	9,812	10,969	12,163
Other Current Liabilities	13,251	16,003	17,460	20,347	23,753
<b>Total Current Liabilities</b>	<b>26,144</b>	<b>29,072</b>	<b>31,538</b>	<b>35,581</b>	<b>40,181</b>
Total Long-term Debt	14,020	24,060	24,060	24,060	24,060
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	2,734	2,970	2,970	2,970	2,970
<b>Total Non-current Liabilities</b>	<b>16,754</b>	<b>27,030</b>	<b>27,030</b>	<b>27,030</b>	<b>27,030</b>
Total Provisions	0	0	0	0	0
<b>Total Liabilities</b>	<b>42,899</b>	<b>56,102</b>	<b>58,568</b>	<b>62,611</b>	<b>67,211</b>
Shareholders' Equity	32,983	36,826	41,507	47,019	53,086
Minority Interests	4,265	5,174	5,256	5,357	5,501
<b>Total Equity</b>	<b>37,248</b>	<b>41,999</b>	<b>46,763</b>	<b>52,377</b>	<b>58,586</b>

### Key Ratios

	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Revenue Growth	(3.8%)	15.9%	10.9%	11.8%	10.4%
Operating EBITDA Growth	(3.8%)	25.9%	9.4%	21.6%	14.3%
Operating EBITDA Margin	6.42%	6.98%	6.88%	7.48%	7.75%
Net Cash Per Share (Rmb)	-1.92	-4.34	-3.26	-2.01	-0.57
BVPS (Rmb)	8.39	9.34	10.57	11.97	13.52
Gross Interest Cover	5.62	6.58	6.71	7.91	8.74
Effective Tax Rate	15.7%	15.4%	15.6%	15.6%	15.6%
Net Dividend Payout Ratio	25.3%	25.4%	25.3%	25.3%	25.2%
Accounts Receivables Days	15.86	14.81	15.77	15.22	15.45
Inventory Days	40.93	39.27	39.95	40.02	40.76
Accounts Payables Days	56.78	54.91	54.66	55.06	55.90
ROIC (%)	6.5%	13.5%	12.8%	15.7%	18.0%
ROCE (%)	7.6%	9.4%	8.8%	9.9%	10.5%
Return On Average Assets	4.69%	6.32%	6.09%	6.90%	7.33%

### Key Drivers

	Dec-20A	Dec-21A	Dec-22F	Dec-23F	Dec-24F
Total sales volume growth (%)	-7.4%	14.0%	5.7%	6.2%	6.1%
Overall average selling price growth (%)	3.4%	1.5%	4.4%	4.8%	4.1%

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

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Distribution of stock ratings and investment banking clients for quarter ended on 31 Mar 2022		
632 companies under coverage for quarter ended on 31 Mar 2022		
	Rating Distribution (%)	Investment Banking clients (%)
Add	70.3%	0.8%
Hold	22.0%	0.0%
Reduce	7.8%	0.2%

**Spitzer Chart for stock being researched ( 2 year data )**

**China Mengniu Dairy (2319 HK)**

## RECOMMENDATION FRAMEWORK

### Stock Ratings Definition:

Add	The stock's total return is expected to reach 15% or higher over the next 12 months.
Hold	The stock's total return is expected to be between negative 10% and positive 15% over the next 12 months.
Reduce	The stock's total return is expected to fall below negative 10% over the next 12 months.

*The total expected return of a stock is defined as the sum of the: (i) percentage difference between the target price and the current price and (ii) the forward net dividend yields of the stock. Stock price targets have an investment horizon of 12 months.*

### Sector Ratings Definition:

Overweight	An Overweight rating means stocks in the sector have, on a market cap-weighted basis, a positive absolute recommendation.
Neutral	A Neutral rating means stocks in the sector have, on a market cap-weighted basis, a neutral absolute recommendation.
Underweight	An Underweight rating means stocks in the sector have, on a market cap-weighted basis, a negative absolute recommendation.

### Country Ratings Definition:

Overweight	An Overweight rating means investors should be positioned with an above-market weight in this country relative to benchmark.
Neutral	A Neutral rating means investors should be positioned with a neutral weight in this country relative to benchmark.
Underweight	An Underweight rating means investors should be positioned with a below-market weight in this country relative to benchmark.

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