

Hong Kong

ADD (no change)

Consensus ratings*: Buy 11 Hold 0 Sell 0

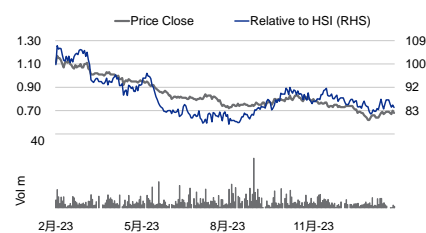
Current price:	HK\$0.68
Target price:	HK\$0.89
Previous target:	HK\$1.01
Up/downside:	30.9%
CGI / Consensus:	-27.6%

Reuters:	1117.HK
Bloomberg:	1117 HK
Market cap:	US\$688.3m
	HK\$5,383m
Average daily turnover:	US\$0.25m
	HK\$1.93m
Current shares o/s:	7,859m
Free float:	39.0%

*Source: Bloomberg

Key changes in this note

- FY23F EPS decreased by 68.3%.
- FY24F EPS decreased by 45.0%.
- FY25F EPS decreased by 38.7%.



Source: Bloomberg

Price performance	1M	3M	12M
Absolute (%)	6.3	-16.1	-40.4
Relative (%)	0.8	-8.7	-18.4

Major shareholders	% held
China Mengniu	52.4
Xinmu	4.3
Yinmu	4.3

Analyst(s)

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China Modern Dairy Holdings

Falling feed costs to benefit margins

- China Modern Dairy (CMD) has issued a profit warning for FY23F, guiding that net profit likely fell 66-72% yoy to Rmb160m-200m due to weak raw milk selling prices.
- We now estimate revenue climbed 12.2% yoy to Rmb13.8bn in FY23F but net profit plunged 67.7% yoy to Rmb181.5m.
- For FY24F, we expect feed costs to decrease and raw milk price to slide 2% yoy, narrowing from a 5.5% yoy fall in FY23F, leading to margin improvement.
- Reiterate Add with lower DCF-based TP of HK\$0.89.

Raw milk price decreased by a greater quantum in 2H23F vs. 1H23

CMD's raw milk selling price fell 4.4% yoy in 1H23 and we estimate it decreased 5.5% in FY23F, likely leading to hoh margin contraction in 2H23F, we believe. The company said in the call that raw milk segment GPM fell 3% pts yoy to 28.1% in FY23F (vs. 28.3% in 1H23), and we forecast overall GPM to be 22.1% and 21.3% for FY23F and 2H23F (1H23: 22.9%), respectively, mainly due to the lower raw milk selling price. For FY24F, we expect raw milk selling price to dip 2% yoy before increasing in FY25F. For FY24F, the US Department of Agriculture (USDA) forecasts total cow herd size in China to decrease yoy. Hence, production volume is likely to stay low, resulting in an improved supply and demand situation in FY25F, in our view. According to China's Statistics Bureau, China dairy output increased by 1.6% yoy and 3.1% in Dec and 2023, respectively, due to a low base in 2022. CMD announced its herd size expanded 11% yoy to 450,000 heads by end-FY23F, with milk yield of 12.6 tonnes, up 3% yoy. The company targets to achieve 13 tonnes milk yield p.a. by 2025F.

Falling feed costs likely to benefit margins in FY24F

In 2H23F, domestic corn, soybean meal and alfalfa prices fell by 3%, 13% and 44% yoy, respectively, according to financial data provider Wind. CMD's feed costs increased 5.8% yoy in 1H23 but stayed yoy flattish in FY23F. We expect CMD's feed costs to stay on its downward trend in FY24F, which should boost its margins. We now expect CMD's GPM to expand by 1.8% pts yoy to 23.9% in FY24F, leading to net profit growth of 206% yoy to Rmb556m. Capex for FY24F should be similar to that in FY23F at roughly Rmb3bn, to be used mainly for the maintenance of farms and milkable cows, according to management. Management also guided for capex to decrease from FY25F due to less investments.

Solid growth of new business

CMD also said in its announcement that its new businesses (mainly the feed business) achieved revenue of Rmb3.3bn in FY23F, up 40% yoy, and recorded a net profit. The company's feed business posted GPM of 10% and NPM of c.1-2% in 1H23. CMD targets to increase its feed business's contribution to 30% of total revenue in FY24F (c.24% in FY23F, based on our forecasts) and expects its NPM to expand to mid-single-digits in the medium-to-long term. The feed business has an asset-light operation and no need for fixed asset investment.

Reiterate Add with a lower DCF-based TP of HK\$0.89

We cut our FY23F-25F EPS forecasts by 38.7-68.3% to reflect the lower-than-expected raw milk selling price. This pushes down our DCF-based TP to HK\$0.89 (WACC: 9.9%, terminal growth rate: 1%, Beta: 0.95). However, we reiterate Add as we believe falling feed costs should benefit CMD's margin expansion in FY24F. The key re-rating catalysts are lower-than-expected feed costs and better margin improvement in 1H24F; while key downside risks are 1) weaker-than-expected raw milk selling price, affecting margins, and 2) higher-than-expected feed costs.

Financial Summary

	Dec-21A	Dec-22A	Dec-23F	Dec-24F	Dec-25F
Revenue (Rmbm)	7,078	12,295	13,794	15,010	16,320
Operating EBITDA (Rmbm)	2,397	2,827	2,582	3,042	3,329
Net Profit (Rmbm)	1,019	562	181	555	779
Core EPS (Rmb)	0.14	0.07	0.02	0.07	0.10
Core EPS Growth	20%	(50%)	(68%)	206%	40%
FD Core P/E (x)	4.35	8.77	27.19	8.88	6.33
DPS (Rmb)	-	-	-	-	-
Dividend Yield	0%	0%	0%	0%	0%
EV/EBITDA (x)	4.27	5.17	4.76	3.98	3.50
P/FCFE (x)	NA	1.99	2.57	8.52	5.70
Net Gearing	53.3%	83.9%	63.0%	58.7%	51.8%
P/BV (x)	0.41	0.44	0.43	0.41	0.38
ROE	10.9%	5.1%	1.6%	4.7%	6.3%
% Change In Core EPS Estimates			(68.3%)	(45.0%)	(38.7%)
CGI/consensus EPS (x)			0.42	0.45	0.44

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

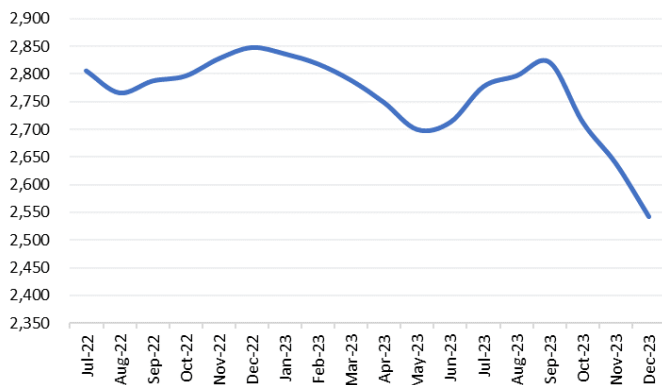
Falling feed costs to benefit margins

Figure 1: Financial results

(Rmb m)	2H22	2H23F	yoy	FY22	FY23F	yoy
Sales	6,663.0	7,160.7	7.5%	12,295.1	13,794.1	12.2%
Farm operating expenses	(5,050.8)	(5,636.5)	11.6%	(9,028.1)	(10,749.2)	19.1%
Gross profit	1,612.2	1,524.2	-5.5%	3,267.0	3,045.0	-6.8%
Gross margin	24.2%	21.3%	-2.9%	26.6%	22.1%	-4.5%
Gain arising from changes in fair value	(650.6)	(602.2)	-7.4%	(988.2)	(1,136.4)	15.0%
Other income	120.3	62.4	-48.1%	201.6	181.4	-10.0%
SG&A expenses	(616.1)	(597.5)	-3.0%	(1,100.1)	(1,149.9)	4.5%
% of sales	9.2%	8.3%	-0.9%	8.9%	8.3%	-0.6%
Other expenses	(38.9)	(23.8)	-38.8%	(42.4)	(42.4)	0.0%
% of sales	0.6%	0.3%	-0.3%	0.3%	0.3%	0.0%
Operating profit	426.9	363.1	-15.0%	1,337.8	897.7	-32.9%
Operating margin	6.4%	5.1%	-1.3%	10.9%	6.5%	-4.4%
Share of profit (loss) of an associate	12.4	14.6	17.5%	15.4	20.0	29.8%
Other gains and losses	(153.2)	(256.6)	67.5%	(378.7)	(302.9)	-20.0%
Profit before finance costs and tax	286.1	121.0	-57.7%	974.6	614.7	-36.9%
Finance costs	(225.7)	(149.9)	-33.6%	(379.6)	(410.4)	8.1%
Profit before tax	60.4	(28.9)	NA	595.0	204.4	-65.7%
Income tax expenses	(11.2)	10.3	NA	(14.8)	(5.1)	-65.4%
Non-controlling interests	5.7	(9.1)	NA	(17.8)	(17.8)	0.0%
Net profit	54.8	(27.8)	NA	562.5	181.5	-67.7%
Pre-tax margin	0.9%	-0.4%	-1.3%	4.6%	1.5%	-3.4%
Net margin	0.8%	-0.4%	-1.2%	4.6%	1.3%	-3.3%

SOURCES: CGSI RESEARCH ESTIMATES, COMPANY DATA

Figure 2: China domestic corn price (Rmb/tonne)



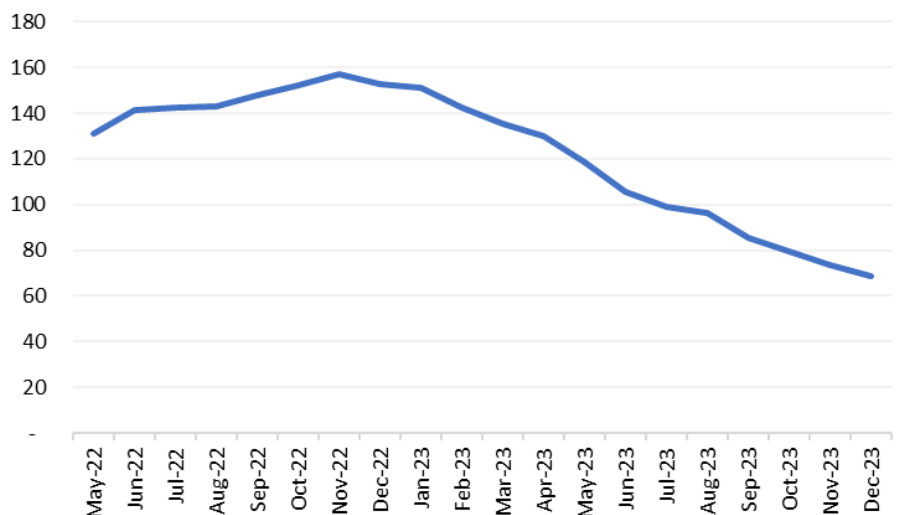
SOURCES: CGSI RESEARCH, COMPANY DATA, WIND

Figure 3: China domestic soybean meal price (Rmb/tonne)



SOURCES: CGSI RESEARCH, COMPANY DATA, WIND

Figure 4: Alfalfa price index



SOURCES: CGSI RESEARCH, COMPANY DATA, WIND

Figure 5: Earnings revision

	FY23F			FY24F			FY25F		
	Old	New	% chg.	Old	New	% chg.	Old	New	% chg.
Sales (Rmb m)	13,967	13,794	-1.2%	15,552	15,010	-3.5%	16,907	16,320	-3.5%
Operating profit	1,298	898	-30.9%	1,767	1,302	-26.4%	2,036	1,531	-24.8%
Operating margin	9.3%	6.5%	-2.8ppts	11.4%	8.7%	-2.7ppts	12.0%	9.4%	-2.7ppts
Reported net profit (Rmb m)	572	181	-68.3%	1,010	555	-45.0%	1,271	779	-38.7%
Net margin	4.1%	1.3%	-2.8ppts	6.5%	3.7%	-2.8ppts	7.5%	4.8%	-2.7ppts
EPS (Rmb)	0.07	0.02	-68.3%	0.13	0.07	-45.0%	0.16	0.10	-38.7%

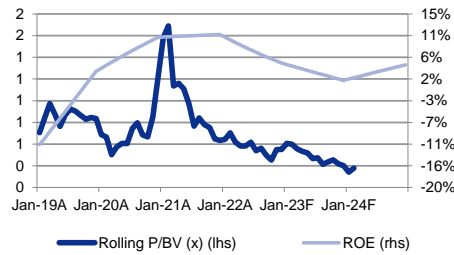
SOURCES: CGSI RESEARCH ESTIMATES, COMPANY DATA

Figure 6: DCF valuation

DCF valuation (Rmb m)	FY22	FY23F	FY24F	FY25F	FY26F	FY27F	FY28F	FY29F	FY30F	FY31F	FY32F	FY33F	FY34F
EBIT	1,353.3	917.7	1,331.5	1,561.0	1,795.1	2,064.4	2,374.0	2,730.1	3,139.6	3,610.6	4,152.2	4,775.0	5,491.3
Taxes	-14.8	-5.1	-14.7	-20.4	-23.5	-27.0	-31.1	-35.7	-41.1	-47.3	-54.4	-62.5	-71.9
NOPAT	1,338.5	912.5	1,316.8	1,540.5	1,771.6	2,037.3	2,342.9	2,694.4	3,098.5	3,563.3	4,097.8	4,712.5	5,419.4
NOPAT growth	13.4%	-31.8%	44.3%	17.0%	15.0%	15.0%	15.0%	15.0%	15.0%	15.0%	15.0%	15.0%	15.0%
D&A	1,132.3	1,456.8	1,478.8	1,539.4	1,585.6	1,633.2	1,682.2	1,732.6	1,784.6	1,838.2	1,893.3	1,950.1	2,008.6
Funds from operation	2,470.7	2,369.3	2,795.6	3,080.0	3,357.2	3,670.5	4,025.1	4,427.0	4,883.2	5,401.5	5,991.1	6,662.6	7,428.0
Change in net working Capital	-1,971.1	1,726.4	-51.1	-47.5	-48.9	-50.4	-51.9	-53.5	-55.1	-56.7	-58.4	-60.2	-62.0
Cash flow from operation	484.8	4,090.6	2,729.8	3,012.0	3,308.3	3,620.1	3,973.2	4,373.6	4,828.1	5,344.8	5,932.7	6,602.4	7,366.0
Capex	-2,248.4	-2,248.4	-2,248.4	-2,248.4	-2,473.2	-2,720.6	-2,992.6	-3,291.9	-3,621.1	-3,983.2	-4,381.5	-4,819.6	-5,301.6
Free cash flow from operation	-1,763.6	1,842.2	481.4	763.6	835.1	899.6	980.6	1,081.7	1,207.0	1,361.6	1,551.2	1,782.8	2,064.4
FCF growth	-365.1%	-204.5%	-73.9%	58.6%	9.4%	7.7%	9.0%	10.3%	11.6%	12.8%	13.9%	14.9%	15.8%
Terminal free cash flow	23,382.0			Assumptions									
Total discounted free cash flow	8,092.1			Risk free									
Present value of terminal free cash flow	7,661.2			Market risk premium									
				Beta									
Total present value of forecasted free cash flows	15,753.4			Cost of equity									
Less: Net Debt	9,951.0			Cost of debt									
Equity Value	5,802.4			Cost of debt (after tax)									
No. of outstanding shares (millions)	7,884.3			Target gearing ratio									
Per share Equity Value (Rmb)	0.7			WACC									
Exchange rate	0.8			Terminal growth rate									
Target price (HK\$)	0.89												

SOURCES: CGSI RESEARCH ESTIMATES, COMPANY DATA

BY THE NUMBERS

P/BV vs ROE

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


Profit & Loss

(Rmbm)	Dec-21A	Dec-22A	Dec-23F	Dec-24F	Dec-25F
Total Net Revenues	7,078	12,295	13,794	15,010	16,320
Gross Profit	2,549	3,267	3,045	3,581	3,948
Operating EBITDA	2,397	2,827	2,582	3,042	3,329
Depreciation And Amortisation	(1,252)	(1,489)	(1,685)	(1,741)	(1,798)
Operating EBIT	1,146	1,338	898	1,302	1,531
Financial Income/(Expense)	(198)	(380)	(410)	(410)	(410)
Pretax Income/(Loss) from Assoc.	37	15	20	30	30
Non-Operating Income/(Expense)	51	(379)	(303)	(333)	(333)
Profit Before Tax (pre-EI)	1,035	595	204	588	817
Exceptional Items					
Pre-tax Profit	1,035	595	204	588	817
Taxation	(2)	(15)	(5)	(15)	(20)
Exceptional Income - post-tax					
Profit After Tax	1,033	580	199	573	797
Minority Interests	(14)	(18)	(18)	(18)	(18)
Preferred Dividends					
FX Gain/(Loss) - post tax					
Other Adjustments - post-tax					
Net Profit	1,019	562	181	555	779
Recurring Net Profit	1,019	562	181	555	779
Fully Diluted Recurring Net Profit	1,019	562	181	555	779

Cash Flow

(Rmbm)	Dec-21A	Dec-22A	Dec-23F	Dec-24F	Dec-25F
EBITDA	2,397	2,827	2,582	3,042	3,329
Cash Flow from Inv. & Assoc.	(37)	(15)	(20)	(30)	(30)
Change In Working Capital	(457)	(1,971)	1,726	(51)	(47)
(Incr)/Decr in Total Provisions					
Other Non-Cash (Income)/Expense					
Other Operating Cashflow	123	(22)	207	184	181
Net Interest (Paid)/Received	(155)	(319)	(400)	(400)	(400)
Tax Paid	(2)	(15)	(5)	(15)	(20)
Cashflow From Operations	1,869	485	4,091	2,730	3,012
Capex	(1,993)	(2,248)	(2,248)	(2,248)	(2,248)
Disposals Of FAs/subsidiaries	789	0	0	0	0
Acq. Of Subsidiaries/investments					
Other Investing Cashflow	(1,670)	25	79	98	102
Cash Flow From Investing	(2,874)	(2,224)	(2,170)	(2,151)	(2,147)
Debt Raised/(repaid)	735	4,219	0	0	0
Proceeds From Issue Of Shares	(56)	44	779	0	0
Shares Repurchased					
Dividends Paid					
Preferred Dividends					
Other Financing Cashflow	961	(380)	(410)	(410)	(410)
Cash Flow From Financing	1,640	3,883	368	(410)	(410)
Total Cash Generated	635	2,144	2,289	169	455
Free Cashflow To Equity	(270)	2,480	1,921	579	865
Free Cashflow To Firm	(807)	(1,359)	2,331	989	1,276

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

BY THE NUMBERS... cont'd

Balance Sheet

(Rmbm)	Dec-21A	Dec-22A	Dec-23F	Dec-24F	Dec-25F
Total Cash And Equivalents	1,929	2,313	4,615	4,783	5,238
Total Debtors	1,222	2,184	2,144	2,367	2,575
Inventories	2,191	3,379	2,202	2,431	2,644
Total Other Current Assets	0	51	51	51	51
Total Current Assets	5,343	7,927	9,012	9,633	10,508
Fixed Assets	14,718	16,334	15,667	15,990	16,255
Total Investments	353	459	479	509	539
Intangible Assets	2,076	2,407	2,407	2,407	2,407
Total Other Non-Current Assets	1,185	1,695	1,695	1,695	1,695
Total Non-current Assets	18,331	20,894	20,247	20,601	20,895
Short-term Debt	2,413	4,866	4,866	4,866	4,866
Current Portion of Long-Term Debt					
Total Creditors	3,169	3,348	3,857	4,259	4,632
Other Current Liabilities	484	254	254	254	254
Total Current Liabilities	6,066	8,468	8,977	9,379	9,752
Total Long-term Debt	5,445	7,210	7,210	7,210	7,210
Hybrid Debt - Debt Component					
Total Other Non-Current Liabilities	1,048	1,499	1,228	1,228	1,228
Total Non-current Liabilities	6,493	8,710	8,439	8,439	8,439
Total Provisions	0	0	0	0	0
Total Liabilities	12,559	17,178	17,416	17,817	18,191
Shareholders' Equity	10,865	11,264	11,446	12,001	12,780
Minority Interests	250	379	397	415	432
Total Equity	11,115	11,643	11,843	12,416	13,213

Key Ratios

	Dec-21A	Dec-22A	Dec-23F	Dec-24F	Dec-25F
Revenue Growth	17.6%	73.7%	12.2%	8.8%	8.7%
Operating EBITDA Growth	7.3%	17.9%	(8.7%)	17.8%	9.4%
Operating EBITDA Margin	33.9%	23.0%	18.7%	20.3%	20.4%
Net Cash Per Share (Rmb)	(0.84)	(1.24)	(0.95)	(0.93)	(0.87)
BVPS (Rmb)	1.54	1.43	1.46	1.53	1.63
Gross Interest Cover	5.78	3.52	2.19	3.17	3.73
Effective Tax Rate	0.20%	2.48%	2.50%	2.50%	2.50%
Net Dividend Payout Ratio	NA	NA	NA	NA	NA
Accounts Receivables Days	51.01	50.55	57.26	55.01	55.27
Inventory Days	135.0	112.6	94.8	74.2	74.9
Accounts Payables Days	186.9	131.7	122.3	129.9	131.1
ROIC (%)	9.04%	7.35%	3.90%	6.33%	7.31%
ROCE (%)	7.02%	6.27%	3.77%	5.38%	6.15%
Return On Average Assets	6.27%	3.62%	2.06%	3.27%	3.88%

Key Drivers

	Dec-21A	Dec-22A	Dec-23F	Dec-24F	Dec-25F
Avg. milk yield per milkable cow (ton/p.a.)	11.3	12.2	12.6	12.9	13.3
ASP for raw milk (Rmb/kg) - external	4.4	4.3	4.0	4.0	4.0
Number of dairy cows	353,793.0	405,358.0	419,898.4	454,443.7	478,652.2

SOURCES: CGIS RESEARCH, COMPANY DATA, BLOOMBERG

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Description:	Excellent	Very Good	Good	N/A	N/A

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Distribution of stock ratings and investment banking clients for quarter ended on 31 Dec 2023		
636 companies under coverage for quarter ended on 31 Dec 2023		
	Rating Distribution (%)	Investment Banking clients (%)
Add	67.5%	1.3%
Hold	22.5%	0.0%
Reduce	10.1%	0.2%

Spitzer Chart for stock being researched (2 year data)

China Modern Dairy Holdings (1117 HK)

— Price Close



Recommendation Framework

Stock Ratings Definition:

Add	The stock's total return is expected to exceed 10% over the next 12 months.
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