Yili (600887 CH)

2Q20 strongly beat; TP lifted to RMB45.90

2Q20 NP +72% YoY, strongly beat expectation on better GPM and selling expenses ratio. FY20E adj. NP growth is on track to meet share award scheme requirement. We raised FY20-22E NP by 7-13% and lifted TP from RMB33.10 to RMB45.90, based on 32x FY21E P/E (vs 28x avg. FY20E and 21E EPS previously), which is the avg. of mid-point (28x) and peak (32x) 1-yr forward P/E range since A-share was announced to be included in MSCI Emerging Markets Index on 21 Jun 2017. FY19-22E EPS CAGR is improved from 10% to 13%. We expect Yili would continue to benefit from industry consolidation. Maintain Buy.

- **2Q20 results strongly beat on better margins.** 1H20 NP fell 1% to RMB3,781mn (equivalent to 60% of our FY20E NP est. vs 54-56% in 1H17-1H19). 2Q20 NP jumped 72%. Revenue rose 22% led by liquid milk (+17%) and milk powder (+86%). By key products, Satine rose 25% (vs Milk Deluxe 30%+) and Pro-Kido rose 40%. Ambrosial rose 10% in 2Q20 but still fell 5% in 1H20 as consumption pattern shifted from yogurt to milk. 2Q20 GPM widened 1.6ppt to 38.7% on reduced promotions and better product mix. NP jumped 72% on operating leverage and GPM expansion.
- **Grabbed more market share.** According to Nielsen data, retail sales of ambient liquid milk and chilled liquid milk decreased by 5.1% and 7.8%, respectively, while retail sales of IMF increased by 4.9% in 1H20. Organic liquid milk, chilled fresh milk and UHT milk outperformed the market by growing 12.6%, 12.3% and 7.5%, respectively, in terms of retail sales. During the period, Yili's market share of ambient products/chilled products increased by 3.2/0.3ppt to 38.8%/15.3%, but market share of IMF fell 0.2ppt to 5.8%.
- **2H20E outlook.** Yili maintained its 2020 target of RMB97bn total revenue (+8% YoY). 1H20 adj. NP growth was 14.6% (on share award scheme benchmark), on track to meet 10% growth target in FY20E. Though raw milk cost is expected to increase in 2H20E, Yili expects this trend would limit industry's promotion activities in 2H. For selling expenses ratio, Yili expects a slight YoY decline trend on precise spending.
- **New businesses development. (1) Chilled fresh milk:** Current market size is >RMB10bn. Yili recorded around RMB300mn sales in 1H20. Sector growth depends on ongoing consumer education and cold chain development. Management expects ambient milk remains the key growth driver. **(2) Cheese:** Market size of B2C is around RMB3bn and B2B's size could be 2-3x of B2C. Yili recorded >RMB200m sales in 1H20 (vs MN's RMB457mn).
- **Maintain Buy.** We lifted FY20/21/22E NP by 13%/7%/9% to mainly factor in lower selling expenses ratio. **Catalysts:** better-than-expected revenue and margins. **Risks:** Raw milk cost pressure, food safety issues.

Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	78,976	90,009	97,286	108,915	119,932
YoY growth (%)	17	14	8	12	10
Net profit (RMB mn)	6,440	6,934	7,107	8,745	10,124
EPS (RMB)	1.060	1.150	1.166	1.435	1.661
YoY growth (%)	7	8	1	23	16
Consensus EPS (RMB)	na	na	1.054	1.328	1.530
P/E (x)	38.3	35.3	34.8	28.3	24.4
P/B (x)	8.8	9.5	8.7	7.7	6.9
Yield (%)	1.7	2.0	2.0	2.5	2.9

Source: Company data, Bloomberg, CMBIS estimates

BUY (Maintain)

Target Price	**RMB45.90**
(Previous TP	RMB33.10)
Up/Downside	**+13%**
Current Price	**RMB40.59**

China F&B Sector

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Stock Data

Mkt Cap (HK$ mn)	246,918
Avg 3 mths t/o (HK$ mn)	2,513.66
52w High/Low (HK$)	40.59/ 26.89
Total Issued Shares (mn)	5,907.5

Source: Bloomberg

Shareholding Structure

Huhhot Investment	8.88%

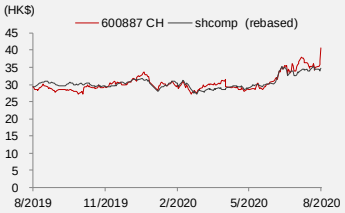
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	8.8%	4.1%
3-mth	28.4%	8.8%
6-mth	23.2%	10.0%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Da Hua

Related reports

1. "Yili – Expect full recovery of sales by Jun" – 4 May 2020
2. "China Dairy Sector - Multiple growth drivers ahead; sector consolidation to continue" – 19 Nov 2019

Figure 1: 1H20 results review

Y/E Dec (RMB mn)	2Q20	2Q19	change (%)	1Q20	1Q19	change (%)	1H20	1H19	change (%)	Remarks
Revenue	**26,800**	**21,888**	**22%**	**20,544**	**23,077**	**-11%**	**47,344**	**44,965**	**5%**	**Sales of key products Satine, Ambrosial, Changqing, Pro-Kido, Chocliz and others grew by 4%**
Cost of sales	(16,427)	(13,761)	19%	(12,848)	(13,858)	-7%	(29,275)	(27,620)	6%	
Gross profit	10,373	8,127	28%	7,696	9,219	-17%	18,069	17,346	4%	
Other income and gains/(losses)	305	378	-19%	222	168	32%	526	546	-4%	
Selling and distribution expenses	(6,115)	(5,536)	10%	(5,203)	(5,566)	-7%	(11,318)	(11,102)	2%	A&P exp +2%
Administrative expenses	(1,203)	(973)	24%	(915)	(943)	-3%	(2,119)	(1,916)	11%	driven by share award exp
R&D expenses	(120)	(109)	10%	(84)	(92)	-9%	(203)	(201)	1%	
Tax & surcharges	(165)	(163)	1%	(125)	(168)	-25%	(290)	(330)	-12%	
Other expenses	(38)	(25)	52%	60	(30)	-305%	22	(55)	-140%	
Operating profit	3,036	1,699	79%	1,651	2,588	-36%	4,687	4,287	9%	
Finance income, net	(17)	40	-142%	(67)	105	-163%	(84)	145	-158%	
Other gains/(losses)	(86)	(63)	37%	(334)	(10)	3115%	(421)	(73)	473%	donation exp increased by RMB276mn
Share of profit from JV/associate	98	66	47%	81	46	76%	179	112	59%	borrowings jumped due to high capex plan
Profit before tax	3,030	1,742	74%	1,332	2,728	-51%	4,361	4,471	-2%	
Tax expense	(425)	(224)	89%	(179)	(448)	-60%	(604)	(672)	-10%	
Profit after tax	2,605	1,518	72%	1,152	2,280	-49%	3,757	3,798	-1%	
Non-controlling interests	(12)	(13)	-7%	(9)	(5)	100%	(22)	(18)	21%	
Net profit	**2,592**	**1,505**	**72%**	**1,143**	**2,276**	**-50%**	**3,735**	**3,781**	**-1%**	
Margin & Ratio (%)										
Gross margin	38.7	37.1	1.6	37.5	39.9	(2.5)	38.2	38.6	(0.4)	
Operating margin	11.3	7.8	3.6	8.0	11.2	(3.2)	9.9	9.5	0.4	
Selling expenses expenses ratio	22.8	25.3	(2.5)	25.3	24.1	1.2	23.9	24.7	(0.8)	
Administrateive expenses ratio	4.5	4.4	0.1	4.5	4.1	0.4	4.5	4.3	0.2	
R&D expenses ratio	0.4	0.5	(0.1)	0.4	0.4	0.0	0.4	0.4	0.0	
Net margin	9.7	6.9	2.8	5.6	9.9	(4.3)	7.9	8.4	(0.5)	
Effective tax rate	14.0	12.9	1.2	13.5	16.4	(3.1)	13.9	15.0	(1.1)	

Source: Company, CMBIS

Figure 2: Earnings revision

	New			Old			Diff (%)		
US$ mn	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	97,286	108,915	119,932	97,074	109,902	120,994	0%	-1%	-1%
Gross Profit	36,235	41,195	45,721	36,053	41,452	45,906	1%	-1%	0%
Operating Profit	8,585	10,126	11,560	7,361	9,602	10,845	17%	5%	7%
Net Profit	7,107	8,745	10,124	6,264	8,155	9,305	13%	7%	9%
Gross Margin	37.2%	37.8%	38.1%	37.1%	37.7%	37.9%	+0.1ppt	+0.1ppt	+0.2ppt
Operating Margin	8.8%	9.3%	9.6%	7.6%	8.7%	9.0%	+1.2ppt	+0.6ppt	+0.6ppt
Net Margin	7.4%	7.9%	8.2%	6.4%	7.3%	7.5%	+1.0ppt	+0.6ppt	+0.7ppt

Source: Company data, CMBIS estimates

Figure 3: CMBIS estimates vs consensus

	CMBIS			Consensus			Diff (%)		
US$ mn	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	97,286	108,915	119,932	98,201	110,544	122,822	-1%	-1%	-2%
Gross Profit	36,235	41,195	45,721	36,364	41,442	46,207	0%	-1%	-1%
Operating Profit	8,585	10,126	11,560	7,571	9,468	10,855	13%	7%	6%
Net profit	7,107	8,745	10,124	6,513	8,401	9,425	9%	4%	7%
Gross Margin	37.2%	37.8%	38.1%	37.0%	37.5%	37.6%	+0.2ppt	+0.3ppt	+0.5ppt
Operating Margin	8.8%	9.3%	9.6%	7.7%	8.6%	8.8%	+1.1ppt	+0.7ppt	+0.8ppt
Net Margin	7.4%	7.9%	8.2%	6.6%	7.6%	7.7%	+0.8ppt	+0.3ppt	+0.5ppt

Source: Bloomberg, CMBIS estimates

Figure 4: P/E band chart



Source: CMBIS estimates, Bloomberg, Company data

Financial Summary

Income statement

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue	**78,976**	**90,009**	**97,286**	**108,915**	**119,932**
Liquid milk	65,679	73,761	77,043	86,456	95,409
Milk powder	8,045	10,055	13,245	14,818	16,308
Ice-cream	4,997	5,631	6,262	6,834	7,317
Others	833	776	1,036	1,107	1,198
Cost of sales	(49,106)	(56,392)	(61,051)	(67,720)	(74,212)
Gross profit	29,870	33,617	36,235	41,195	45,721
Other income	1,402	1,125	1,111	1,009	1,034
Selling expenses	(19,773)	(21,070)	(22,473)	(25,159)	(27,704)
Admin expenses	(2,980)	(4,285)	(4,864)	(5,228)	(5,637)
Other op expenses	(1,033)	(1,314)	(1,423)	(1,691)	(1,853)
EBIT	7,486	8,075	8,585	10,126	11,560
Finance income, net	60	(8)	(121)	(94)	18
Other gains/(losses)	(113)	(86)	(420)	(86)	(86)
JV & associates	144	214	296	371	446
Pre-tax profit	7,578	8,194	8,341	10,316	11,938
Income tax	(1,126)	(1,243)	(1,215)	(1,552)	(1,793)
Less: Minority interests	(12)	(17)	(19)	(19)	(20)
Net profit	**6,440**	**6,934**	**7,107**	**8,745**	**10,124**

Cash flow summary

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Profit before tax	7,578	8,194	8,341	10,316	11,938
JV & associates	(144)	(214)	(296)	(371)	(446)
D&A	1,598	1,891	2,373	2,903	3,183
Net finance income	(60)	8	121	94	(18)
Change in working capital	313	3,312	742	1,022	1,019
Others	(660)	(4,736)	(726)	(1,343)	(1,556)
Operating cash flow	**8,625**	**8,455**	**10,554**	**12,622**	**14,119**
Capex	(5,091)	(9,243)	(10,000)	(4,000)	(3,000)
Acquisitions	0	(1,617)	0	0	0
Others	(284)	861	(828)	138	138
Investing cash flow	**(5,375)**	**(9,999)**	**(10,828)**	**(3,862)**	**(2,862)**
Change of debt	(6,337)	6,633	8,431	(3,000)	(2,500)
Dividend and interest paid	(4,393)	(4,406)	(5,486)	(5,465)	(6,527)
Others	(19)	(3,244)	0	0	0
Financing cash flow	**(10,749)**	**(1,016)**	**2,945**	**(8,465)**	**(9,027)**
Net change in cash	(7,499)	(2,560)	2,672	295	2,230
Cash at the beginning	20,756	13,564	11,066	13,738	14,033
Exchange difference	307	62	0	0	0
Cash at the end	**13,564**	**11,066**	**13,738**	**14,033**	**16,263**

Balance sheet

YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
Non-current assets	**23,151**	**34,755**	**42,728**	**44,244**	**44,556**
Fixed asset	17,374	24,461	32,138	33,283	33,149
Prepaid lease payments	650	1,936	1,936	1,936	1,936
Interest in JV	1,909	1,961	2,257	2,628	3,073
Other non-current assets	3,217	6,397	6,397	6,397	6,397
Current assets	**24,455**	**25,706**	**29,998**	**31,592**	**35,077**
Inventories	5,507	7,715	8,352	9,265	10,153
Account receivables	1,282	1,837	1,986	2,223	2,448
Prepayments	1,614	1,352	1,445	1,595	1,737
Others	5,001	3,476	4,476	4,476	4,476
Cash	11,051	11,325	13,738	14,033	16,263
Current liabilities	**19,171**	**31,432**	**37,484**	**38,305**	**38,079**
Account payables	9,116	10,801	11,694	12,971	14,214
Other payables	8,135	12,262	12,991	14,035	15,065
Borrowings	1,556	4,866	9,366	9,866	8,366
Tax payables	353	397	397	397	397
Others	10	3,106	3,037	1,037	37
Non-current liabilities	**398**	**2,755**	**6,755**	**5,255**	**5,255**
Borrowings	0	1,971	5,971	4,471	4,471
Others	398	784	784	784	784
Total net assets	**28,037**	**26,274**	**28,487**	**32,277**	**36,300**
Shareholders' equity	**27,916**	**26,131**	**28,325**	**32,096**	**36,098**
Non-controlling interests	**122**	**143**	**162**	**181**	**202**

Key ratios

YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
Sales mix (%)					
Liquid milk	83.2	81.9	79.2	79.4	79.6
Milk powder	10.2	11.2	13.6	13.6	13.6
Ice-cream	6.3	6.3	6.4	6.3	6.1
Others	1.1	0.8	0.8	0.7	0.7
P&L ratios (%)					
Gross margin	37.8	37.3	37.2	37.8	38.1
EBIT margin	9.5	9.0	8.8	9.3	9.6
Net margin	8.2	7.7	7.3	8.0	8.4
Payout ratio	66.1	70.9	70.0	70.0	70.0
Balance sheet ratios					
Current ratio (x)	1.3	0.8	0.8	0.8	0.9
Quick ratio (x)	1.0	0.6	0.6	0.6	0.7
A/C receivables days	5	6	7	7	7
A/C payables days	62	64	67	66	67
Inventory days	38	43	48	47	48
Net cash (RMB mn)	9,495	4,488	(4,599)	(1,304)	3,426
Returns (%)					
ROAE	24.3	25.7	26.1	28.9	29.7
ROAA	13.3	12.8	10.7	11.8	13.1
Per share					
EPS (RMB)	1.06	1.15	1.17	1.43	1.66
DPS (RMB)	0.70	0.81	0.82	1.00	1.16
BVPS (RMB)	4.59	4.29	4.65	5.26	5.92

Source: Company data, CMBIS estimates

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