

# Yili (600887 CH)

## Expect full recovery of sales by Jun

FY19 NP +8% to RMB6,934mn, in line with our estimates and consensus. 1Q20 NP was down 50% due to COVID-19 impact. That said, management said sales recovered 90% currently and expects a full recovery by Jun 2020. We cut our FY20/21E net profit estimates by 17%/5% mainly to reflect lower revenue and GPM. Our TP is revised from RMB34.04 to RMB33.10, based on 28.0x average FY20E and FY21E EPS. We expect Yili would benefit from industry consolidation, reflected by market share gain in 1Q20. Maintain Buy.

- FY19 results in line.** Revenue rose 14%, in line, led by liquid milk (+12%) and milk powder (+25%). Key products like Satine and Ambrosial grew by 17-18%, behind MN's Milk Deluxe and Just Yoghurt's 20%+ growth. Market share of UHT milk and IMF rose 1.4ppt and 0.4ppt to 37.7% and 6.0%, respectively, in 2019. GPM fell 0.5ppt to 37.3%, slight below our expectation of 37.8%, led by 6.7ppt reduction in GPM of milk powder segment mainly due to margin dilution from the acquisition of Westland Co-operative Dairy. SG&A expenses ratio dropped 0.6ppt to 28.2%, led by 1.6ppt reduction in A&P expenses.
- 1Q20 hit by COVID-19.** Revenue dropped 11% led by 19% decline of liquid milk sales as sales affected by COVID-19. Market share of UHT milk and chilled milk up 1.1ppt and 0.3ppt YoY. GPM squeezed by 2.4ppt to 37.5% on more promotion to destock old inventories. SG&A expenses ratio increased 1.6ppt due to operating deleverage. Yili reported RMB67mn net finance cost (vs RMB105 net income) as total borrowing increased from RMB6.8bn in Dec 2019 to RMB12bn in Mar 2020. NP fell 50% to RMB1,143mn.
- FY20E guidance.** Yili sets its total revenue and PBT target at RMB97bn and RMB6.1bn in FY20E, representing 7.5% YoY growth and 26% YoY decrease, respectively. This implies 14% YoY growth/13% YoY decline for total revenue/PBT, respectively, during 2-4Q20. That said, excluding government grant and share award expenses, management expects adj. NP to resume growth in 2-4Q20. Going forward, while Yili still focuses on domestic dairy business, it will develop Southeast Asia market and develop healthy drinks business.
- Maintain Buy.** Our new TP of RMB33.10 is based on 28.0x average FY20E and FY21E EPS. Our target P/E multiple is unchanged as we expect Yili to resume double-digit revenue growth beginning 2H20E. **Catalysts:** better-than-expected revenue and margins. **Risks:** recovery slower-than-expected, raw milk cost pressure, food safety issues.

### Earnings Summary

(YE 31 Dec)	FY18A	FY19A	FY20E	FY21E	FY22E
Revenue (RMB mn)	78,976	90,009	97,074	109,902	120,994
YoY growth (%)	17	14	8	13	10
Net profit (RMB mn)	6,440	6,934	6,264	8,155	9,305
EPS (RMB)	1.060	1.150	1.027	1.338	1.526
YoY growth (%)	7	8	(11)	30	14
Consensus EPS (RMB)	na	na	1.088	1.361	1.559
P/E (x)	27.6	25.4	28.5	21.9	19.2
P/B (x)	6.4	6.8	6.5	5.7	5.1
Yield (%)	2.4	2.8	2.5	3.2	3.7

Source: Company data, Bloomberg, CMBIS estimates

**BUY (Maintain)**

Target Price **RMB33.10**  
 (Previous TP **RMB34.04**)  
 Up/Downside **+13%**  
 Current Price **RMB29.24**

### China F&B Sector

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### Stock Data

Mkt Cap (HK\$ mn)	177,367
Avg 3 mths t/o (HK\$ mn)	1,723.43
52w High/Low (HK\$)	34.66/ 26.88
Total Issued Shares (mn)	5,907.5

Source: Bloomberg

### Shareholding Structure

Huhhot Investment	8.88%
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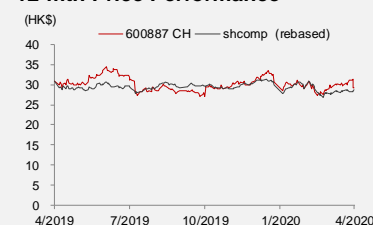
Source: HKEx

### Share Performance

	Absolute	Relative
1-mth	2.1%	0.3%
3-mth	-4.4%	0.8%
6-mth	4.6%	9.5%

Source: Bloomberg

### 12-mth Price Performance



Source: Bloomberg

**Auditor: Da Hua**

### Related reports

"China Dairy Sector - Multiple growth drivers ahead; sector consolidation to continue" - 19 Nov 2019

Figure 1: FY19 and 1Q20 results review

Y/E Dec (RMB mn)	FY19	FY18	change (%)	Remarks	1Q20	1Q19	change (%)
<b>Revenue</b>	<b>90,009</b>	<b>78,976</b>	<b>14%</b>	<b>Key products like Satine, Ambrosial and plain milk saw 17-18% growth according to Nielsen data</b>	<b>20,544</b>	<b>23,077</b>	<b>-11%</b>
Cost of sales	(56,392)	(49,106)	15%		(12,848)	(13,858)	-7%
Gross profit	33,617	29,870	13%		7,696	9,219	-17%
Other income and gains/(losses)	1,125	1,402	-20%		289	139	109%
Selling and distribution expenses	(21,070)	(19,773)	7%		(5,203)	(5,566)	-7%
Administrative expenses	(4,285)	(2,980)	44%	increased due to acquisition of new businesses, set up of new business units, salary increase and share award exp	(915)	(943)	-3%
R&D expenses	(495)	(427)	16%		(84)	(92)	-9%
Tax & surcharges	(577)	(531)	9%		(125)	(168)	-25%
Other expenses	(241)	(76)	219%		(7)	0	-29467%
Operating profit	8,075	7,486	8%		1,651	2,588	-36%
Finance income, net	(8)	60	-113%	total borrowing jumped from RMB1.56bn to RMB6.84bn	(67)	105	-163%
Other gains/(losses)	(86)	(113)	-24%		(334)	(10)	3115%
Share of profit from JV/associate	214	144	48%		81	46	76%
Profit before tax	8,194	7,578	8%		1,332	2,728	-51%
Tax expense	(1,243)	(1,126)	10%		(179)	(448)	-60%
Profit after tax	6,951	6,452	8%		1,152	2,280	-49%
Non-controlling interests	17	12	38%		9	5	100%
<b>Net profit</b>	<b>6,934</b>	<b>6,440</b>	<b>8%</b>		<b>1,143</b>	<b>2,276</b>	<b>-50%</b>
<b>Margin &amp; Ratio (%)</b>							
Gross margin	37.3	37.8	(0.5)	raw milk cost +6.7%, dilution from acquisition of Westland Co-operative Dairy	37.5	39.9	(2.4)
Operating margin	9.0	9.5	(0.5)		8.0	11.2	(3.2)
Selling expenses ratio	23.4	25.0	(1.6)	A&P exp ratio fell 1.6ppt to 12.3%	25.3	24.1	1.2
Administrative expenses ratio	4.8	3.8	1.0		4.5	4.1	0.4
R&D expenses ratio	0.6	0.5	0.1		0.4	0.4	0.0
Net margin	7.7	8.2	(0.5)		5.6	9.9	(4.3)
Effective tax rate	15.2	14.9	0.3		13.5	16.4	(2.9)
	<b>FY19</b>	<b>FY18</b>	<b>change</b>				
Inventory days	43	38	5				
A/C receivables days	6	5	1				
A/C payable days	64	62	2				

Source: Company, CMBIS

**Figure 2: Earnings revision**

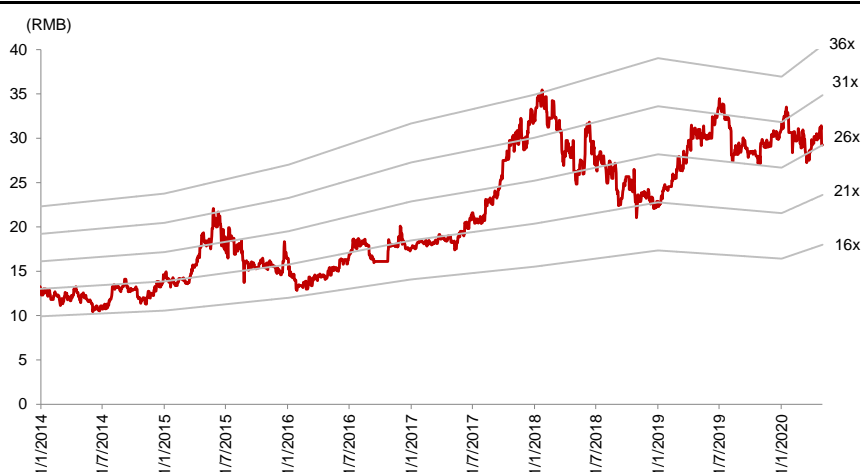
US\$ mn	New			Old			Diff (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	97,074	109,902	120,994	100,972	110,638	na	-4%	-1%	na
Gross Profit	36,053	41,452	45,906	38,443	42,307	na	-6%	-2%	na
Operating Profit	7,361	9,602	10,845	8,632	9,884	na	-15%	-3%	na
Net Profit	6,264	8,155	9,305	7,508	8,607	na	-17%	-5%	na
Gross Margin	37.1%	37.7%	37.9%	38.1%	38.2%	na	-0.4ppt	-0.5ppt	na
Operating Margin	7.6%	8.7%	9.0%	8.5%	8.9%	na	-0.9ppt	-0.2ppt	na
Net Margin	6.4%	7.3%	7.5%	7.4%	7.8%	na	-1.0ppt	-0.5ppt	na

Source: Company data, CMBIS estimates

**Figure 3: CMBIS estimates vs consensus**

US\$ mn	CMBIS			Consensus			Diff (%)		
	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E	FY20E	FY21E	FY22E
Revenue	97,074	109,902	120,994	97,554	109,517	119,431	0%	0%	1%
Gross Profit	36,053	41,452	45,906	36,231	41,570	45,177	0%	0%	2%
Operating Profit	7,361	9,602	10,845	7,038	9,155	10,762	5%	5%	1%
Net profit	6,264	8,155	9,305	6,513	8,401	9,425	-4%	-3%	-1%
Gross Margin	37.1%	37.7%	37.9%	37.1%	38.0%	37.8%	flat	-0.3ppt	+0.1ppt
Operating Margin	7.6%	8.7%	9.0%	7.2%	8.4%	9.0%	+0.4ppt	+0.3ppt	flat
Net Margin	6.4%	7.3%	7.5%	6.7%	7.7%	7.9%	-0.3ppt	-0.4ppt	-0.4ppt

Source: Bloomberg, CMBIS estimates

**Figure 4: P/E band chart**

Source: CMBIS estimates, Bloomberg, Company data

## Financial Summary

Income statement						Cash flow summary					
YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E	YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Revenue</b>	<b>78,976</b>	<b>90,009</b>	<b>97,074</b>	<b>109,902</b>	<b>120,994</b>	Profit before tax	7,578	8,194	7,401	9,636	10,994
Liquid milk	65,679	73,761	77,378	88,315	97,467	JV & associates	(144)	(214)	(216)	(249)	(274)
Milk powder	8,045	10,055	12,614	13,752	14,999	D&A	1,598	1,891	2,373	2,903	3,183
Ice-cream	4,997	5,631	6,501	7,230	7,892	Net finance income	(60)	8	89	129	39
Others	833	776	795	819	850	Change in working capital	313	3,312	733	1,104	1,029
Cost of sales	(49,106)	(56,392)	(61,021)	(68,450)	(75,088)	Others	(660)	(4,736)	(741)	(1,322)	(1,475)
Gross profit	29,870	33,617	36,053	41,452	45,906	<b>Operating cash flow</b>	<b>8,625</b>	<b>8,455</b>	<b>9,639</b>	<b>12,201</b>	<b>13,496</b>
Other income	1,402	1,125	879	902	927	Capex	(5,091)	(9,243)	(10,000)	(4,000)	(3,000)
Selling expenses	(19,773)	(21,070)	(23,298)	(25,772)	(28,313)	Acquisitions	0	(1,617)	0	0	0
Admin expenses	(2,980)	(4,285)	(4,854)	(5,275)	(5,808)	Others	(284)	861	115	115	115
Other op expenses	(1,033)	(1,314)	(1,420)	(1,706)	(1,868)	<b>Investing cash flow</b>	<b>(5,375)</b>	<b>(9,999)</b>	<b>(9,885)</b>	<b>(3,885)</b>	<b>(2,885)</b>
EBIT	7,486	8,075	7,361	9,602	10,845	Change of debt	(6,337)	6,633	5,441	(1,000)	(1,510)
Finance income, net	60	(8)	(89)	(129)	(39)	Dividend and interest paid	(4,393)	(4,406)	(5,287)	(4,820)	(6,109)
Other gains/(losses)	(113)	(86)	(86)	(86)	(86)	Others	(19)	(3,244)	0	0	0
JV & associates	144	214	216	249	274	<b>Financing cash flow</b>	<b>(10,749)</b>	<b>(1,016)</b>	<b>154</b>	<b>(5,820)</b>	<b>(7,619)</b>
Pre-tax profit	7,578	8,194	7,401	9,636	10,994	Net change in cash	(7,499)	(2,560)	(92)	2,496	2,992
Income tax	(1,126)	(1,243)	(1,121)	(1,464)	(1,672)	Cash at the beginning	20,756	13,564	11,066	10,974	13,470
Less: Minority interests	(12)	(17)	(17)	(17)	(17)	Exchange difference	307	62	0	0	0
<b>Net profit</b>	<b>6,440</b>	<b>6,934</b>	<b>6,264</b>	<b>8,155</b>	<b>9,305</b>	<b>Cash at the end</b>	<b>13,564</b>	<b>11,066</b>	<b>10,974</b>	<b>13,470</b>	<b>16,462</b>

Balance sheet						Key ratios					
YE 31 Dec (RMB mn)	FY18A	FY19A	FY20E	FY21E	FY22E	YE 31 Dec	FY18A	FY19A	FY20E	FY21E	FY22E
<b>Non-current assets</b>	<b>23,151</b>	<b>34,755</b>	<b>42,648</b>	<b>44,043</b>	<b>44,183</b>	<b>Sales mix (%)</b>					
Fixed asset	17,374	24,461	32,138	33,283	33,149	Liquid milk	83.2	81.9	79.7	80.4	80.6
Prepaid lease payments	650	1,936	1,936	1,936	1,936	Milk powder	10.2	11.2	13.0	12.5	12.4
Interest in JV	1,909	1,961	2,177	2,426	2,701	Ice-cream	6.3	6.3	6.7	6.6	6.5
Other non-current assets	3,217	6,397	6,397	6,397	6,397	Others	1.1	0.8	0.7	0.6	0.6
<b>Current assets</b>	<b>24,455</b>	<b>25,706</b>	<b>26,223</b>	<b>30,162</b>	<b>34,431</b>	<b>P&amp;L ratios (%)</b>					
Inventories	5,507	7,715	8,348	9,365	10,273	Gross margin	37.8	37.3	37.1	37.7	37.9
Account receivables	1,282	1,837	1,981	2,243	2,470	EBIT margin	9.5	9.0	7.6	8.7	9.0
Prepayments	1,614	1,352	1,443	1,608	1,750	Net margin	8.2	7.7	6.5	7.4	7.7
Others	5,001	3,476	3,476	3,476	3,476	Payout ratio	66.1	70.9	70.0	70.0	70.0
Cash	11,051	11,325	10,974	13,470	16,462	<b>Balance sheet ratios</b>					
<b>Current liabilities</b>	<b>19,171</b>	<b>31,432</b>	<b>34,474</b>	<b>37,522</b>	<b>38,317</b>	Current ratio (x)	1.3	0.8	0.8	0.8	0.9
Account payables	9,116	10,801	11,688	13,111	14,382	Quick ratio (x)	1.0	0.6	0.5	0.6	0.6
Other payables	8,135	12,262	12,977	14,101	15,136	A/C receivables days	5	6	7	7	7
Borrowings	1,556	4,866	9,366	9,866	8,366	A/C payables days	62	64	67	66	67
Tax payables	353	397	397	397	397	Inventory days	38	43	48	47	48
Others	10	3,106	47	47	37	Net cash (RMB mn)	9,495	4,488	(4,363)	(867)	3,625
<b>Non-current liabilities</b>	<b>398</b>	<b>2,755</b>	<b>6,755</b>	<b>5,255</b>	<b>5,255</b>	<b>Returns (%)</b>					
Borrowings	0	1,971	5,971	4,471	4,471	ROAE	24.3	25.7	23.4	27.8	28.2
Others	398	784	784	784	784	ROAA	13.3	12.8	9.7	11.4	12.2
<b>Total net assets</b>	<b>28,037</b>	<b>26,274</b>	<b>27,641</b>	<b>31,428</b>	<b>35,042</b>	<b>Per share</b>					
<b>Shareholders' equity</b>	<b>27,916</b>	<b>26,131</b>	<b>27,481</b>	<b>31,251</b>	<b>34,848</b>	EPS (RMB)	1.06	1.15	1.03	1.34	1.53
<b>Non-controlling interests</b>	<b>122</b>	<b>143</b>	<b>160</b>	<b>177</b>	<b>194</b>	DPS (RMB)	0.70	0.81	0.72	0.94	1.07
						BVPS (RMB)	4.59	4.29	4.51	5.13	5.72

Source: Company data, CMBIS estimates

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