

# Yili Industrial (600887 CH)

## 2Q rev/np +1%/3%; all eyes on cost savings

2Q results came in slightly below us, with revenue and net profits growing only 1%/3% (vs CMBle MSD growth for both), respectively. We attribute this to <1%/-9% growth/decline in liquid milk/milk powder revenue, when both exhibited slowdown from 1Q. Management did not explicitly revise down the 10% full year revenue guidance, and looks forward to seeing the below to help attain the target. These include 1) the continued double-digit growth in Satine, when premium room-temp milk remains popular among health-conscious consumers; 2) a recovery on 2C demand for cheese products, as initiatives taken for 2C (new launches) and 2B (consumer education) should start bearing fruit; 3) a gradual recovery on low-temp SKU along with the resumption of consumption habits post-pandemic; and 4) the resolution of patent bottleneck associated with Ausnutria. While these are legitimate to us, however, some of them might take further time to materialize, and the implied 15% 2H revenue growth looks to be quite challenging to achieve, in our view. On the contrary, cost efficiency could be the last resort to achieve a 9% net margins by 2025E, and the trajectory was well-tracked with a 0.6pp decrease in SG&A ratio in 1H. We remain buyer of Yili.

■ **Other call takeaway.** 1) **UHT yogurt** is undergoing a transition, when the sales of new SKU has not fully caught up with the obsolete. The decline has sequentially narrowed with momentum improving in July/August; 2) **Goodwill impairment on Ausnutria** could be detrimental, and Yili is striving its best to prevent this from happening. Excluding Ausnutria, Yili delivered 2% organic revenue growth for 1H; 3) **70% payout ratio** will be maintained as capex cycle has already peaked-out; 4) **raw material inventory write-off** of RMB400mn was a drag to 1H net profits, and the same could happen in 2H as the mismatch between demand and supply remains.

■ **Earnings change.** We lower our 2023-24E revenue by 3% each to reflect our concern. We also trim our gross margins by 0.4pp to reflect the destocking impact from smaller IMF brands upon the enactment of the new license legislation. These are partially mitigated by a 0.2pp lower in SG&A ratio, and result in a 2% cut in our 2023E net profits.

■ **Valuation.** Our new TP is based on an updated 21.0x (from previously 24.0x) roll-forwarded mid-24E PE, which benchmarks to -1sd below average (from previously at average). We now value both Mengniu (2319 HK, BUY), Yili (600887 CH, BUY) and Feihe (6186 HK, HOLD) at -1sd below average, in view of a lukewarm dairy demand amid a faltering consumption recovery.

### Earnings Summary

(YE 31 Dec)	FY21A	FY22A	FY23E	FY24E	FY25E
Revenue (RMB mn)	110,595	123,171	131,654	139,321	147,545
YoY growth (%)	14.2	11.4	6.9	5.8	5.9
Net profit (RMB mn)	8,704.9	9,431.1	10,676.9	11,959.2	13,367.7
YoY growth (%)	23.0	8.3	13.2	12.0	11.8
EPS (RMB)	1.4	1.5	1.7	1.9	2.1
Consensus EPS (RMB)	na	na	1.7	2.0	2.3
P/E (x)	29.1	23.9	15.9	14.2	12.7
P/B (x)	5.1	4.3	3.1	2.9	3.0
Yield (%)	2.4	2.9	4.8	5.4	6.1
ROE (%)	22.3	19.3	20.7	22.1	23.4
Net gearing (%)	Net cash	4.5	3.3	2.2	Net cash

Source: Company data, Bloomberg, CMBIGM estimates

### BUY (Maintain)

**Target Price** RMB36.5  
 (Previous TP RMB40.0)  
**Up/Downside** 29.2%  
**Current Price** RMB26.6

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### Stock Data

Mkt Cap (RMB mn) 169,462.9  
 Avg 3 mths t/o (RMB mn) 881.8  
 52w High/Low (RMB) 36.13/25.24  
 Total Issued Shares (mn) 6366.0  
 Source: FactSet

### Shareholding Structure

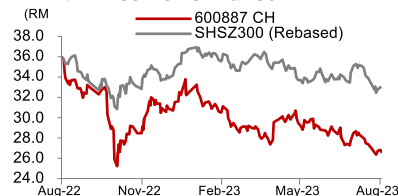
HKSCC 16.4%  
 Hohhot Investment Co. 8.5%  
 Source: HKEx

### Share Performance

	Absolute	Relative
1-mth	-6.5%	-0.6%
3-mth	-8.8%	-6.8%
6-mth	-12.6%	-5.2%

Source: FactSet

### 12-mth Price Performance



Source: FactSet

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5. [Yili Industrial \(600887 CH\) – Full-year guidance unchanged](#) – 20 Jul 2023

Figure 1: Earnings revision

RMB mn	New			Old			Diff (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	131,654	139,321	147,545	135,090	143,869	153,303	-2.5%	-3.2%	-3.8%
Gross Profit	41,926	44,722	47,735	43,523	46,685	50,099	-3.7%	-4.2%	-4.7%
EBITDA	15,149	17,071	19,138	15,262	16,972	18,958	-0.7%	0.6%	0.9%
Net profit	10,677	11,959	13,368	10,856	11,964	13,292	-1.7%	0.0%	0.6%
Gross Margin	31.8%	32.1%	32.4%	32.2%	32.4%	32.7%	-0.4ppt	-0.3ppt	-0.3ppt
EBITDA Margin	11.5%	12.3%	13.0%	11.3%	11.8%	12.4%	0.2ppt	0.5ppt	0.6ppt
Net Margin	8.1%	8.6%	9.1%	8.0%	8.3%	8.7%	0.1ppt	0.3ppt	0.4ppt

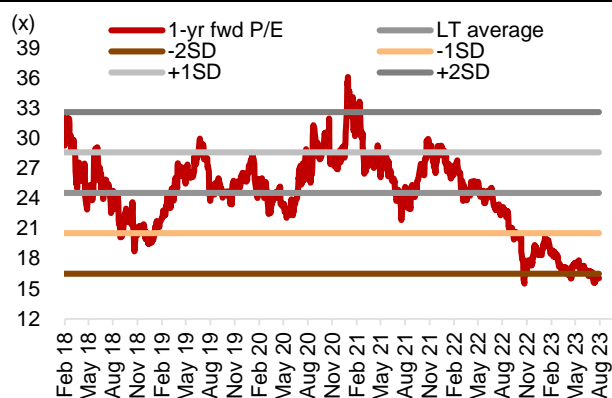
Source: CMBIGM estimates

Figure 2: CMBIGM estimates vs consensus

RMB mn	CMBIGM			Consensus			Diff (%)		
	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E	FY23E	FY24E	FY25E
Revenue	131,654	139,321	147,545	133,541	145,223	157,937	-1.4%	-4.1%	-6.6%
Gross Profit	41,926	44,722	47,735	43,717	48,094	52,830	-4.1%	-7.0%	-9.6%
EBITDA	15,149	17,071	19,138	16,616	19,190	21,433	-8.8%	-11.0%	-10.7%
Net profit	10,677	11,959	13,368	10,773	12,557	14,355	-0.9%	-4.8%	-6.9%
Gross Margin	31.8%	32.1%	32.4%	32.7%	33.1%	33.5%	-0.9ppt	-1ppt	-1.1ppt
EBITDA Margin	11.5%	12.3%	13.0%	12.4%	13.2%	13.6%	-0.9ppt	-1ppt	-0.6ppt
Net Margin	8.1%	8.6%	9.1%	8.1%	8.6%	9.1%	0ppt	-0.1ppt	0ppt

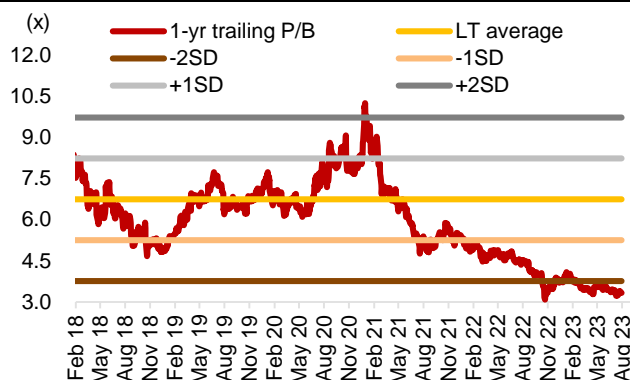
Source: Bloomberg, CMBIGM estimates

Figure 3: Yili - 12M forward P/E chart



Source: Bloomberg, CMBIGM estimates

Figure 4: Yili - 12M Trailing P/B chart



Source: Bloomberg, CMBIGM estimates

## Financial Summary

INCOME STATEMENT	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Revenue	96,886	110,595	123,171	131,654	139,321	147,545
Cost of goods sold	(67,453)	(76,417)	(83,119)	(88,935)	(93,760)	(98,921)
Others	(547)	(664)	(742)	(793)	(839)	(889)
Gross profit	28,886	33,515	39,311	41,926	44,722	47,735
Operating expenses	(20,923)	(24,584)	(29,914)	(31,003)	(32,341)	(33,761)
Selling expense	(16,884)	(19,315)	(22,908)	(24,356)	(25,217)	(26,263)
Admin expense	(3,883)	(4,828)	(6,164)	(5,924)	(6,269)	(6,640)
Others	(156)	(442)	(841)	(722)	(855)	(859)
Operating profit	7,963	8,930	9,397	10,923	12,381	13,974
Other income	7,963	8,930	9,397	10,923	12,381	13,974
EBITDA	10,406	11,919	13,484	15,149	17,071	19,138
Depreciation	(2,223)	(2,873)	(3,744)	(4,010)	(4,458)	(4,913)
Other amortisation	(220)	(115)	(343)	(216)	(232)	(250)
EBIT	7,963	8,930	9,397	10,923	12,381	13,974
Net Interest income/(expense)	(188)	29	255	685	714	754
Other income/expense	862	1,153	979	654	640	625
Pre-tax profit	8,150	10,112	10,630	12,263	13,736	15,353
Income tax	(1,051)	(1,380)	(1,312)	(1,513)	(1,695)	(1,895)
Minority interest	(21)	(27)	113	(72)	(81)	(91)
Net profit	7,078	8,705	9,431	10,677	11,959	13,368
Gross dividends	4,988	6,144	6,631	8,223	9,210	10,295

BALANCE SHEET	2020A	2021A	2022A	2023E	2024E	2025E
YE 31 Dec (RMB mn)						
Current assets	28,381	50,155	61,463	63,254	64,831	67,244
Cash & equivalents	11,695	31,742	33,853	34,368	34,869	36,131
Restricted cash	3	400	3	0	0	0
Account receivables	1,875	2,233	3,450	3,688	3,903	4,133
Inventories	7,545	8,917	14,836	15,874	16,736	17,657
Other current assets	7,263	6,862	9,321	9,324	9,324	9,324
Non-current assets	42,774	51,807	69,502	73,006	76,222	79,100
PP&E	28,768	29,379	33,735	36,174	38,231	39,974
Investment in JVs & assos	3,423	4,718	5,175	6,075	6,975	7,875
Intangibles	1,897	1,609	4,648	4,813	5,072	5,307
Other non-current assets	8,685	16,102	25,944	25,944	25,944	25,944
Total assets	71,154	101,962	130,965	136,259	141,052	146,344
Current liabilities	34,768	43,296	62,170	64,937	66,900	69,028
Short-term borrowings	6,957	12,596	26,799	26,799	26,799	26,799
Account payables	17,975	14,062	16,807	17,983	18,958	20,002
Other current liabilities	9,836	16,638	18,563	20,155	21,142	22,227
Non-current liabilities	5,853	9,875	14,653	14,653	14,653	14,653
Long-term borrowings	5,137	5,380	9,298	9,298	9,298	9,298
Other non-current liabilities	716	4,495	5,354	5,354	5,354	5,354
Total liabilities	40,622	53,171	76,822	79,590	81,553	83,681
Share capital	4,311	5,149	5,325	5,325	5,325	5,325
Retained earnings	23,541	24,298	27,587	30,041	32,790	35,862
Other reserves	2,532	18,262	17,356	17,356	17,356	17,356
Total shareholders equity	30,384	47,708	50,268	52,722	55,471	58,544
Minority interest	149	1,083	3,875	3,948	4,029	4,119
Total equity and liabilities	71,154	101,962	130,965	136,259	141,052	146,344

CASH FLOW	2020A	2021A	2022A	2023E	2024E	2025E
<b>YE 31 Dec (RMB mn)</b>						
<b>Operating</b>						
Profit before taxation	8,150	10,112	10,630	12,263	13,736	15,353
Depreciation & amortization	2,442	2,988	4,087	4,226	4,690	5,164
Change in working capital	4,684	(5,644)	(4,391)	(100)	(100)	(108)
Others	(5,425)	8,071	3,094	(1,513)	(1,695)	(1,895)
<b>Net cash from operations</b>	<b>9,852</b>	<b>15,528</b>	<b>13,420</b>	<b>14,875</b>	<b>16,630</b>	<b>18,514</b>
<b>Investing</b>						
Capital expenditure	(6,522)	(6,683)	(6,646)	(6,829)	(7,006)	(7,142)
Acquisition of subsidiaries/ investments	22	0	0	0	0	0
Others	(2,543)	(1,114)	(12,868)	(900)	(900)	(900)
<b>Net cash from investing</b>	<b>(9,043)</b>	<b>(7,797)</b>	<b>(19,514)</b>	<b>(7,729)</b>	<b>(7,906)</b>	<b>(8,042)</b>
<b>Financing</b>						
Dividend paid	(4,988)	(4,988)	(6,144)	(6,631)	(8,223)	(9,210)
Net borrowings	5,122	243	3,918	0	0	0
Share repurchases	248	16,047	(906)	0	0	0
Others	(428)	644	11,913	0	0	0
<b>Net cash from financing</b>	<b>(47)</b>	<b>11,945</b>	<b>8,781</b>	<b>(6,631)</b>	<b>(8,223)</b>	<b>(9,210)</b>
<b>Net change in cash</b>						
Cash at the beginning of the year	11,325	11,695	31,742	33,853	34,368	34,869
Exchange difference	(395)	(29)	(580)	0	0	0
<b>Cash at the end of the year</b>	<b>11,692</b>	<b>31,342</b>	<b>33,850</b>	<b>34,368</b>	<b>34,869</b>	<b>36,131</b>
GROWTH	2020A	2021A	2022A	2023E	2024E	2025E
<b>YE 31 Dec</b>						
Revenue	7.4%	14.2%	11.4%	6.9%	5.8%	5.9%
Gross profit	(13.1%)	16.0%	17.3%	6.7%	6.7%	6.7%
Operating profit	10.9%	12.1%	5.2%	16.2%	13.3%	12.9%
EBITDA	13.9%	14.5%	13.1%	12.3%	12.7%	12.1%
EBIT	10.9%	12.1%	5.2%	16.2%	13.3%	12.9%
Net profit	2.1%	23.0%	8.3%	13.2%	12.0%	11.8%
PROFITABILITY	2020A	2021A	2022A	2023E	2024E	2025E
<b>YE 31 Dec</b>						
Gross profit margin	29.8%	30.3%	31.9%	31.8%	32.1%	32.4%
Operating margin	8.2%	8.1%	7.6%	8.3%	8.9%	9.5%
EBITDA margin	10.7%	10.8%	10.9%	11.5%	12.3%	13.0%
Return on equity (ROE)	25.0%	22.3%	19.3%	20.7%	22.1%	23.4%
GEARING/LIQUIDITY/ACTIVITIES	2020A	2021A	2022A	2023E	2024E	2025E
<b>YE 31 Dec</b>						
Net debt to equity (x)	0.0	(0.3)	0.0	0.0	0.0	(0.0)
Current ratio (x)	0.8	1.2	1.0	1.0	1.0	1.0
Receivable turnover days	7.1	7.4	10.2	10.2	10.2	10.2
Inventory turnover days	40.8	42.6	65.2	65.2	65.2	65.2
Payable turnover days	97.3	67.2	73.8	73.8	73.8	73.8
VALUATION	2020A	2021A	2022A	2023E	2024E	2025E
<b>YE 31 Dec</b>						
P/E	29.5	29.1	23.9	15.9	14.2	12.7
P/E (diluted)	29.5	27.7	24.4	16.2	14.5	13.0
P/B	6.9	5.1	4.3	3.1	2.9	3.0
Div yield (%)	2.4	2.4	2.9	4.8	5.4	6.1

Source: Company data, CMBIGM estimates. Note: The calculation of net cash includes financial assets.

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