

China Feihe (6186 HK)

2H sets to recover when channel restructuring completes as planned

We cut our 2022/23E revenue by 8.5%/3.0% to reflect the impact of Feihe's "freshness strategy" that has been ongoing since beginning of 2022. Feihe aims to clear up obsolete channel inventory to prepare for the enactment of the new national standards (early-2023) and to stabilize retail pricing. The restructuring also leads us to believe SG&A will surge in 1H22 and we have raise 2.3pp of our opex ratio accordingly. Meanwhile, we also lower our 2022/23E GPM by 2.5pp/2.9pp to reflect the potential dilution from a rising contribution of children/ adult IMF, which typically offers a lower GPM than infancy IMF. These changes result in a 11%/ 15% cut in our 2022/23E net profit, and hence our new TP of HK\$12.5. Other than these, management remains upbeat to look for a DD top line growth for 2H22 (subsequent to a SD decline for 1H) upon the completion of the channel restructuring, and we anticipate a clearer roadmap on how management will achieve its RMB35bn revenue target for 2023E. We remain buy-rated.

Our key NDR takeaway

- The key focus in 2022 is to clear up obsolete channel inventory and incentivize dealers to sell Feihe products. Management expected a slight revenue decline in 1H22 while maintained GPM/ NPM targets of 68-70% and 28-30%. Feihe also has a longer-term goal of RMB35bn revenue in 2023, 30% market share and 15% top line CAGR in 2023-28E.
- The company continued the efforts to develop its "2nd growth trajectory" after infancy IMF in 1H22, through launching higher-ended products and expanding into other milk powder segments, such as children and adult IMF.
- The super-premium brand Astrobaby Zhuorui launched in 4Q21 performed strongly in 1H22, according to management. Astrobaby products for the new national IMF standards, which will enter into force in Feb 2023, will be launched in 2023.
- Adult IMF performed in 1Q22 with the launch of its premium brand Aiben (爱本) in 4Q21 and a thorough upgrade of the core product "1962" in Jan.

Valuation. Our revised TP is based on 11.5x (from 13.0x) end-22E P/E, which still represents -1sd below its long term average of 16.7x. Our methodology reflects our vigilance in view of China's currently low birth rate and industry overhang.

(YE 31 Dec)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue (RMB mn)	18,592	22,776	25,413	31,562	36,862
YoY growth (%)	35.5	22.5	11.6	24.2	16.8
Net income (RMB mn)	7,437	6,959	7,236	8,865	10,117
EPS (RMB)	0.8	0.8	0.8	1.0	1.1
YoY growth (%)	69.8	(6.4)	4.0	22.5	14.1
Consensus EPS (RMB)	n.a	n.a	0.8	0.9	1.1
P/E (x)	n.a	n.a	9.4	7.7	6.7
P/B (x)	n.a	n.a	2.7	2.2	1.9
Yield (%)	n.a	n.a	4.5	5.5	6.3
ROE (%)	25.1	40.4	41.8	44.0	45.0
Net gearing (%)	net cash	net cash	net cash	net cash	net cash

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price	HK\$12.5
(Previous TP)	HK\$14.0)
Up/Downside	+40.4%
Current Price	HK\$8.9

China Consumer Sector

Joseph Wong
 (852) 3900 0838
 josephwong@cmbi.com.hk

Zheng Xiaohui
 zhengxiaohui@cmbi.com.hk



Stock Data

Mkt Cap (HK\$ mn)	79,256
Avg 3 mths t/o (HK\$ mn)	168.1
52w High/Low (HK\$)	18.3/ 6.8
Total Issued Shares (mn)	8,905

Source: Bloomberg

Shareholding Structure

Garland Glory Holdings	43.6%
Morgan Stanley	7.8%
Dasheng Ltd	4.5%

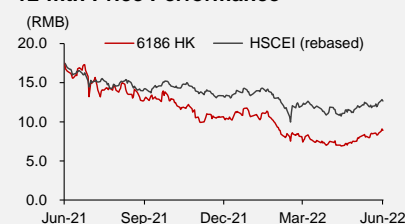
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	19.1%	8.5%
3-mth	19.9%	15.7%
6-mth	-14.8%	-11.4%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: Deloitte Related Reports

1. [China Cosmetics – The crown jewel of the consumption spectrum; initiate Botanee/ Proya/ Jahwa with Buy](#) – 21 Jun 2022
2. [2Q earnings risks look well-contained with refreshed expectation; top picks: CRB/ Smoore](#) - 15 Jun 2022

Figure 1: Earnings revision

RMB mn	New			Old			Diff (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	25,413	31,562	36,862	27,760	32,524	n.a	-8.5%	-3.0%	n.a
Gross profit	17,526	21,520	24,893	19,856	23,113	n.a	-11.7%	-6.8%	n.a
EBIT	10,093	12,371	14,122	11,034	12,940	n.a	-8.5%	-4.4%	n.a
Net profit	7,236	8,865	10,117	8,113	9,544	n.a	-10.8%	-14.9%	n.a
EPS (RMB)	0.8	1.0	1.1	0.9	1.0	n.a	-10.8%	-14.9%	n.a

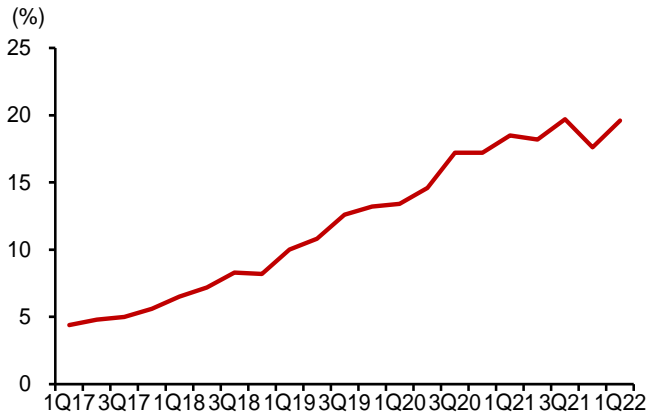
Source: Company data, CMBIGM estimates

Figure 2: CMBIGM estimates vs consensus

RMB mn	CMBIGM			Consensus			Diff (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	25,413	31,562	36,862	25,251	29,072	32,715	0.6%	8.6%	12.7%
Gross profit	17,526	21,520	24,893	17,190	19,756	22,102	2.0%	8.9%	12.6%
Operating profit	10,093	12,371	14,122	9,924	11,558	12,850	1.7%	7.0%	9.9%
Net profit	7,236	8,865	10,117	7,258	8,334	9,104	-0.3%	6.4%	11.1%
EPS (RMB)	0.8	1.0	1.1	0.8	0.9	1.1	-2.2%	4.2%	4.7%

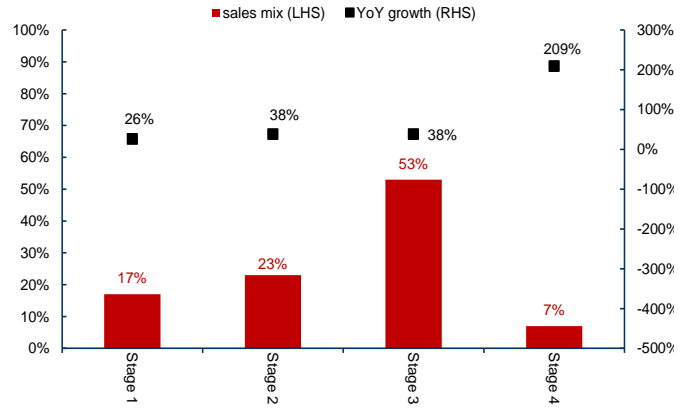
Source: Company data, CMBIGM estimates

Figure 3: Market share trend for Feihe



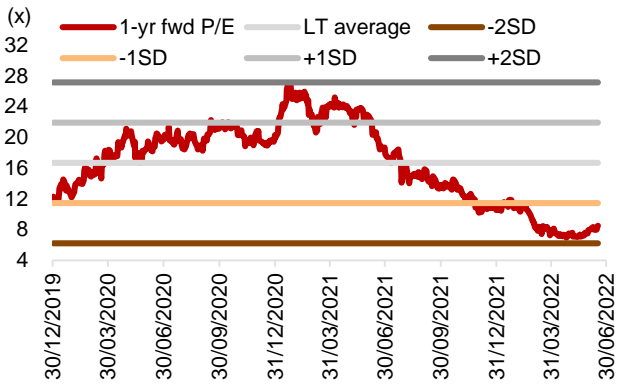
Source: Company data, CMBIS

Figure 4: Stage 3 IMF mix supports stage 4 expansion



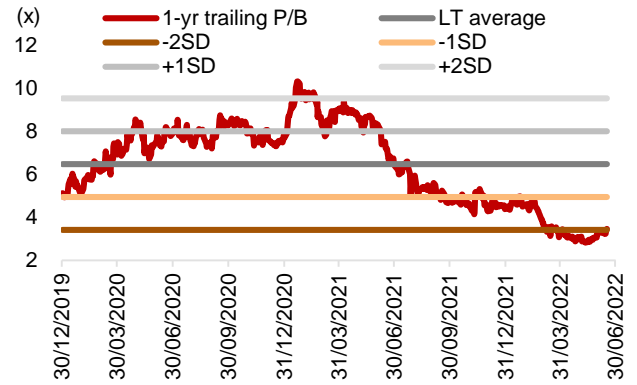
Source: Company data, CMBIS

Figure 5: 1-year forward P/E chart



Source: Bloomberg, CMBIS estimates

Figure 6: Trailing P/B chart



Source: Bloomberg, CMBIS estimates

Financial Summary

Income statement						Cash flow summary					
YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E	YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue	18,592	22,776	25,413	31,562	36,862	Net income	7,437	6,959	7,236	8,865	10,117
IMF	17,674	21,853	24,431	30,462	35,613	D&A	266	1,537	511	622	758
Others	919	923	981	1,099	1,249	Change in working capital	1,253	(827)	(120)	(266)	(234)
						Others	(1,205)	(854)	(30)	(30)	(30)
Gross profits	13,480	16,008	17,526	21,520	24,893	Net cash fr. operating act.	7,751	6,815	7,597	9,191	10,611
D&A	(266)	(1,537)	(275)	(302)	(333)	Capex & investments	(816)	(1,930)	(2,099)	(2,556)	(3,113)
Selling expense	(5,263)	(6,729)	(7,624)	(8,995)	(10,321)	Short term investment	-	-	-	-	1
Administration expenses	(1,161)	(1,208)	(1,423)	(1,767)	(2,064)	Others	(2,970)	(514)	-	-	(1)
Other income, gains	3,019	1,864	1,864	1,864	1,864	Net cash fr. investing act.	(3,786)	(2,444)	(2,099)	(2,556)	(3,113)
Other expense	(231)	(90)	(250)	(250)	(250)	Equity raised	-	(365)	-	-	-
EBIT	9,844	9,844	10,093	12,371	14,122	Change of Debts	(3,630)	(444)	-	-	-
						Dividend paid	(2,685)	(3,392)	(3,462)	(3,600)	(4,411)
EBITDA	10,110	11,382	10,367	12,674	14,454	Others	3,772	(44)	-	-	-
Finance costs, net	74	81	81	81	81	Net cash fr. financing act.	(2,543)	(4,245)	(3,462)	(3,600)	(4,411)
Non-operating	(18)	(253)	(116)	(116)	(116)	Net change in cash	1,421	125	2,036	3,035	3,087
Pre-tax profit	9,900	9,672	10,058	12,337	14,087	Cash at the beginning of the year	8,810	9,553	9,629	11,665	14,700
Income tax	(2,464)	(2,757)	(2,867)	(3,517)	(4,016)	Exchange difference	(173)	(49)	-	-	-
Less: Minority interests	0	44	46	46	46	Cash at the end of the year	10,059	9,629	11,665	14,700	17,787
Net profit	7,437	6,959	7,236	8,865	10,117	Less: pledged cash	-	-	-	-	-

Balance sheet						Key ratios					
YE 31 Dec (RMB mn)	FY20A	FY21A	FY22E	FY23E	FY24E	YE 31 Dec	FY20A	FY21A	FY22E	FY23E	FY24E
Non-current assets	9,778	11,512	13,084	15,002	17,342	Sales mix (%)					
PP&E/Fixed assets	7,197	8,437	10,018	11,950	14,304	IMF	95.1	95.9	96.1	96.5	96.6
Intangible assets	48	133	140	141	143	Others	4.9	4.1	3.9	3.5	3.4
Right of use assets, net	1,442	1,707	1,707	1,707	1,707	P&L ratios (%)					
Other non-current assets	1,091	1,234	1,219	1,203	1,188	Gross margin	72.5	70.3	69.0	68.2	67.5
Current assets	18,544	19,970	22,338	26,048	29,735	Operating margin	52.9	43.2	39.7	39.2	38.3
Cash	10,059	9,629	11,665	14,700	17,787	Pre-tax margin	53.3	42.5	39.6	39.1	38.2
Account receivable	289	477	525	652	762	Net margin	40.0	30.6	28.5	28.1	27.4
Inventories	557	576	576	576	576	Effective tax rate	(24.9)	(28.5)	(28.5)	(28.5)	(28.5)
Other current assets	7,640	9,287	9,572	10,120	10,610	Balance sheet analysis					
Current liabilities	7,107	6,942	7,154	7,563	7,928	Current ratio (x)	0.5	0.5	0.5	0.6	0.6
Borrowings	514	833	1,042	1,133	1,284	Net receivable days	5.6	7.5	7.5	7.5	7.5
Account payables	346	407	614	910	1,063	Inventory turnover days	80.9	69.2	69.2	69.2	69.2
Other payables	903	1,083	3,094	448	313	Net payable days	91.7	92.8	92.8	92.8	92.8
Rent payable	5,344	4,618	2,404	5,072	5,269	Net debt to equity (%)	net	net	net	net	net
Non-current liabilities	2,030	2,136	2,136	2,136	2,136	Returns (%)					
Borrowings	732	621	621	621	621	ROE	25.1	40.4	41.8	44.0	45.0
Deferred tax liabilities	139	115	115	115	115	Dividend yield	n.a	4.3	4.5	5.5	6.3
Other non-current liabilities	1,158	1,399	1,399	1,399	1,399	Per share					
Minority Interest	1,438	1,482	1,436	1,391	1,345	EPS (RMB)	0.8	0.8	0.8	1.0	1.1
						DPS (RMB)	0.3	0.4	0.4	0.5	0.6
Total net assets	19,186	22,403	26,132	31,352	37,012	BVPS (RMB)	2.0	2.3	2.8	3.4	4.0
Shareholders' equity	17,747	20,921	24,696	29,961	35,667	EV/ EBITDA (x)	n.a	5.3	5.7	4.2	3.5

Source: Company data, CMBIS estimates

Disclosures & Disclaimers

Analyst Certification

The research analyst who is primary responsible for the content of this research report, in whole or in part, certifies that with respect to the securities or issuer that the analyst covered in this report: (1) all of the views expressed accurately reflect his or her personal views about the subject securities or issuer; and (2) no part of his or her compensation was, is, or will be, directly or indirectly, related to the specific views expressed by that analyst in this report.

Besides, the analyst confirms that neither the analyst nor his/her associates (as defined in the code of conduct issued by The Hong Kong Securities and Futures Commission) (1) have dealt in or traded in the stock(s) covered in this research report within 30 calendar days prior to the date of issue of this report; (2) will deal in or trade in the stock(s) covered in this research report 3 business days after the date of issue of this report; (3) serve as an officer of any of the Hong Kong listed companies covered in this report; and (4) have any financial interests in the Hong Kong listed companies covered in this report.

CMBIGM Ratings

BUY : Stock with potential return of over 15% over next 12 months
HOLD : Stock with potential return of +15% to -10% over next 12 months
SELL : Stock with potential loss of over 10% over next 12 months
NOT RATED : Stock is not rated by CMBIGM

OUTPERFORM : Industry expected to outperform the relevant broad market benchmark over next 12 months
MARKET-PERFORM : Industry expected to perform in-line with the relevant broad market benchmark over next 12 months
UNDERPERFORM : Industry expected to underperform the relevant broad market benchmark over next 12 months

CMB International Global Markets Limited

Address: 45/F, Champion Tower, 3 Garden Road, Hong Kong, Tel: (852) 3900 0888 Fax: (852) 3900 0800

CMB International Global Markets Limited ("CMBIGM") is a wholly owned subsidiary of CMB International Capital Corporation Limited (a wholly owned subsidiary of China Merchants Bank)

Important Disclosures

There are risks involved in transacting in any securities. The information contained in this report may not be suitable for the purposes of all investors. CMBIGM does not provide individually tailored investment advice. This report has been prepared without regard to the individual investment objectives, financial position or special requirements. Past performance has no indication of future performance, and actual events may differ materially from that which is contained in the report. The value of, and returns from, any investments are uncertain and are not guaranteed and may fluctuate as a result of their dependence on the performance of underlying assets or other variable market factors. CMBIGM recommends that investors should independently evaluate particular investments and strategies, and encourages investors to consult with a professional financial advisor in order to make their own investment decisions.

This report or any information contained herein, have been prepared by the CMBIGM, solely for the purpose of supplying information to the clients of CMBIGM or its affiliate(s) to whom it is distributed. This report is not and should not be construed as an offer or solicitation to buy or sell any security or any interest in securities or enter into any transaction. Neither CMBIGM nor any of its affiliates, shareholders, agents, consultants, directors, officers or employees shall be liable for any loss, damage or expense whatsoever, whether direct or consequential, incurred in relying on the information contained in this report. Anyone making use of the information contained in this report does so entirely at their own risk.

The information and contents contained in this report are based on the analyses and interpretations of information believed to be publicly available and reliable. CMBIGM has exerted every effort in its capacity to ensure, but not to guarantee, their accuracy, completeness, timeliness or correctness. CMBIGM provides the information, advices and forecasts on an "AS IS" basis. The information and contents are subject to change without notice. CMBIGM may issue other publications having information and/ or conclusions different from this report. These publications reflect different assumption, point-of-view and analytical methods when compiling. CMBIGM may make investment decisions or take proprietary positions that are inconsistent with the recommendations or views in this report.

CMBIGM may have a position, make markets or act as principal or engage in transactions in securities of companies referred to in this report for itself and/or on behalf of its clients from time to time. Investors should assume that CMBIGM does or seeks to have investment banking or other business relationships with the companies in this report. As a result, recipients should be aware that CMBIGM may have a conflict of interest that could affect the objectivity of this report and CMBIGM will not assume any responsibility in respect thereof. This report is for the use of intended recipients only and this publication, may not be reproduced, reprinted, sold, redistributed or published in whole or in part for any purpose without prior written consent of CMBIGM.

Additional information on recommended securities is available upon request.

For recipients of this document in the United Kingdom

This report has been provided only to persons (I) falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005 (as amended from time to time) ("The Order") or (II) are persons falling within Article 49(2) (a) to (d) ("High Net Worth Companies, Unincorporated Associations, etc.") of the Order, and may not be provided to any other person without the prior written consent of CMBIGM.

For recipients of this document in the United States

CMBIGM is not a registered broker-dealer in the United States. As a result, CMBIGM is not subject to U.S. rules regarding the preparation of research reports and the independence of research analysts. The research analyst who is primary responsible for the content of this research report is not registered or qualified as a research analyst with the Financial Industry Regulatory Authority ("FINRA"). The analyst is not subject to applicable restrictions under FINRA Rules intended to ensure that the analyst is not affected by potential conflicts of interest that could bear upon the reliability of the research report. This report is intended for distribution in the United States solely to "major US institutional investors", as defined in Rule 15a-6 under the US, Securities Exchange Act of 1934, as amended, and may not be furnished to any other person in the United States. Each major US institutional investor that receives a copy of this report by its acceptance hereof represents and agrees that it shall not distribute or provide this report to any other person. Any U.S. recipient of this report wishing to effect any transaction to buy or sell securities based on the information provided in this report should do so only through a U.S.-registered broker-dealer.

For recipients of this document in Singapore

This report is distributed in Singapore by CMBI (Singapore) Pte. Limited (CMBIGMG) (Company Regn. No. 201731928D), an Exempt Financial Adviser as defined in the Financial Advisers Act (Cap. 110) of Singapore and regulated by the Monetary Authority of Singapore. CMBIGMG may distribute reports produced by its respective foreign entities, affiliates or other foreign research houses pursuant to an arrangement under Regulation 32C of the Financial Advisers Regulations. Where the report is distributed in Singapore to a person who is not an Accredited Investor, Expert Investor or an Institutional Investor, as defined in the Securities and Futures Act (Cap. 289) of Singapore, CMBIGMG accepts legal responsibility for the contents of the report to such persons only to the extent required by law. Singapore recipients should contact CMBIGMG at +65 6350 4400 for matters arising from, or in connection with the report.