

Ausnutria (1717.HK)

Own-branded goat milk powder business with fast growing trend; opening up elderly market with goat milk powder products
China | Dairy | Company report

25 September 2019

Investment Summary

Short seller Blue Orca has recently published reports about Ausnutria Dairy. The main allegations include overstating import data of infant milk formula, revenue and profits; understating its labor and staff costs; misleading Chinese consumers in relation to the ingredients of Kabrita infant goat milk formula; the acquisition of the 40% equity interest in Nutriunion HK was a sham transaction to unjustly enrich insiders, and the independence of the company's distributors. Apart from releasing voluntary announcement clarification, the independent review committee has been established and engaged the independent consultant to conduct the independent review.

In responding to the allegation of overstating import data of infant milk formula, revenue and profits, Ausnutria denied and pointed out that all import data are supported by documents. The report only counts the number of shipments of import agents. The estimation was arrived after deducting the company's inventory level. such estimation did not take into account the overhead costs incurred and value-added processes conducted by the company after the imported infant milk products arriving the Changsha, and did not take into account of the purchase of imported base powder (mainly New Zealand) from local importers. The independent consultant also noted that the import volume of goat milk in 2017 as per the customs' records was 154% higher than the annualised import volume as estimated by the short seller reports.

We are still optimistic about Ausnutria's medium and long-term business. Although China is facing a problem of declining birth rate, consumption upgrade continues in the infant milk industry. In 1H of 2019, the overall infant milk industry recorded a mid-single digit growth, which was mainly driven by ASP growth, and the trend is expected to continue. Ausnutria has conducted market research consistently with targeted consumers to raise the awareness of goat milk products. In view of the decline in birth rate, goat milk formula for kids has been launched. The company plans to also launch goat milk formula for the whole family, targeting adults and elderly. In 1H of 2019, in the imported formula milk powder market, Kabrita's market share in China reached 64.4%, accounting for 61.7% of the total imported goat milk powder. It is still the market leader.

Its interim revenue increased by 21.9% y.o.y. to RMB565 million. The growth of its own-branded formula cow milk powder recorded a slowdown but still with a 20.7% increase, among which organic formula milk powder increased by 52.3%. The proportion of overall own-branded formula milk powder business increased by 6.3 ppt to 86.7%. Benefiting from the increase in the proportion of its own brands, the gross profit margin increased by 5.7 ppt y.o.y. to 52.1%. The ratio of sales and distribution expenses to revenue was basically maintained at 27.4% y.o.y.. We expect overall revenue growth in 2H of the year to be faster than 1H. The slowdown in the growth of its own-branded formula cow milk powder business in 1H was mainly due to the high base in the same period last year and the delay in the approval of registration.

As for the private label and other business, the y.o.y. decline in 1H was mainly due to the strategic reorientation. As the new plant was completed, it is expected to gradually ease the problem of production capacity shortage. Ausnutria plans to terminate its butter business in the second quarter, and inventory will be cleared in 2H. We maintain buy rating, target price-earnings ratio 25 times, with target price HKD15.7. (current price as of September 23, 2019)

Buy

CMP HKD11

(Closing price at 23 September 2019)

TARGET HKD15.7 (+42.7%)

COMPANY DATA

O/S SHARES (MN)	1607
MARKET CAP (HKDBN)	17.688
52 - WK HI/LO (HKD)	6.78/16.68

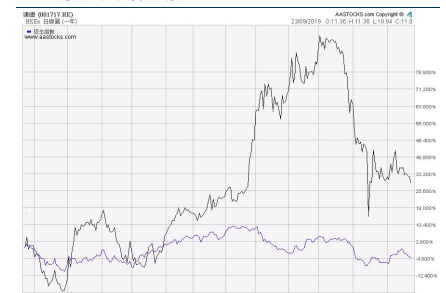
SHARE HOLDING PATTERN, %

CITIC	23.57%
Center Laboratories Inc.	23.38%

PRICE PERFORMANCE, %

	1 個月	3 個月	1 年
Ausnutria	-4.0	-27.9	29.7
HSI	0.2	-8.0	-4.6

RETURN VS. HSI



Source: Aastocks, Phillip Securities

KEY FINANCIALS

RMB mn	FY17	FY18	FY19E	FY20E
Net Sales	3926	5390	7006	8968
Net Profit	308	635	911	1243
EPS, RMB	0.24	0.47	0.57	0.77
PER, x	40.7	21.3	17.5	12.8
BVPS, RMB	1.5	2.5	2.3	2.5
P/BV, x	6.4	4.0	4.3	3.9
ROE, %	17.2%	19.0%	25.2%	31.1%

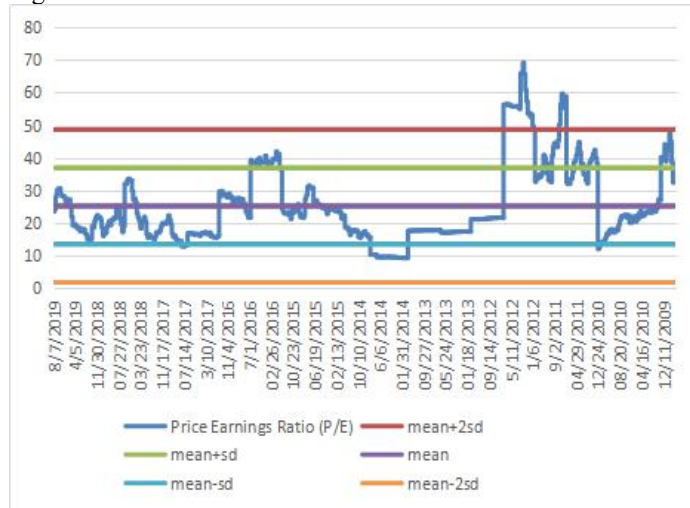
Source: Company, Phillip Securities Est.

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Investment Thesis & Valuation

We give buy rating, target price-earnings ratio 25 times, with target price HKD15.7. Potential investment risks include policy change, market competition deterioration, and raw milk cost with huge volatility. (current price as of September 23, 2019)

Figure: Historical PE Ratio



Source: Bloomberg, Phillip Securities

Financials

FYE	2016	2017	2018	2019E	2020E
Valuation Ratios					
Price to Earnings (P/E)	58.4	40.7	21.3	17.5	12.8
Price to Book (P/B)	7.8	6.4	4.0	4.3	3.9
Per Share Data (RMB)					
EPS	0.17	0.24	0.47	0.57	0.77
Book Value Per Share	1.27	1.54	2.49	2.28	2.52
Growth (%)					
Revenue	30.3%	43.3%	37.3%	30.0%	28.0%
Operating Income	2329.3%	45.2%	79.0%	42.5%	35.8%
Net Profit	319.9%	44.9%	106.1%	43.5%	36.4%
Margins (%)					
Gross Profit Margin	41.0%	43.0%	49.4%	51.4%	52.4%
Operating Profit Margin	11.4%	11.5%	15.0%	16.5%	17.5%
Net Profit Margin	8.5%	8.5%	12.0%	13.2%	14.1%
Key Ratios					
ROE (%)	14.7%	17.2%	19.0%	25.2%	31.1%
ROA (%)	6.0%	6.0%	9.4%	12.5%	15.5%
Income Statement (RMB)					
Revenue	2740	3926	5390	7006	8968
- Cost of Goods Sold	-1615	-2236	-2729	-3407	-4272
Gross Income	1125	1690	2661	3599	4696
-SG&A expenses	-862	-1267	-1906	-2443	-3127
Operating Income	311	452	809	1153	1567
Pretax Income	298	439	792	1136	1550
- Minority Interest	21	27	9	14	18
Net Profit	213	308	635	911	1243

Source: Company, Phillip Securities (HK) Research Estimates

Exchange rate (0.9025) is one year HKD/CNY forward contract price on 23th September from Wind

(Financial figures as at 23th September 2019)

PHILLIP RESEARCH STOCK SELECTION SYSTEMS

Total Return	Recommendation	Rating	Remarks
>+20%	Buy	1	>20% upside from the current price
+5% to +20%	Accumulate	2	+5% to +20% upside from the current price
-5% to +5%	Neutral	3	Trade within $\pm 5\%$ from the current price
-5% to -20%	Reduce	4	-5% to -20% downside from the current price
<-20%	Sell	5	>20% downside from the current price

We do not base our recommendations entirely on the above quantitative return bands. We consider qualitative factors like (but not limited to) a stock's risk reward profile, market sentiment, recent rate of share price appreciation, presence or absence of stock price catalysts, and speculative undertones surrounding the stock, before making our final recommendation

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