

China Feihe (6186 HK)

Completion of channel restructuring continues to drive a steady 2H recovery

We moderately trim our 2022/23E earnings by 6-7% p.a as we now attempt to factor-in 1) a lower GPM (by average 0.8pp) due to higher non-infant milk formula contribution and 2) a 1.5pp higher selling expense. Our forecast in general is at the low end/ slightly below management guidance, as we believe a low birth rate could compound with an intensifying competition to weigh on margins and drive up promotion expenses. Despite this, Feihe's sequential sales recovery sustains our BUY rating.

- **Guidance maintained.** Management targets DD HoH revenue growth in 2H and LSD revenue decline for 2022E (1H22: -16.2% YoY). Margin-wise, Feihe indicated that 2H GPM and NPM will improve HoH, with full year GPM and NPM standing at 66-68% (1H22: 68%, 2021: 70.3%) and c.26% (1H22: 23.3%, 2021: 30.2%), respectively. With that, this implies selling expense ratio to stabilise at c.30% in longer term (1H22: 32.5%).
- **Sales mix upgrade has been an important topline support.** While China's IMF market has been under pressure in recent three years, super premium and super premium+ (teens of growth YoY in 1H22) segments maintained a steadily upward momentum, according to management. Feihe would be a major beneficiary from this trend, given a heavy weight (c.59% in 1H) of these segments in its revenue structure.
- **New health and nutrition related product categories could become important topline drivers in longer term.** New product categories, including children milk powder (stage 4 products accounted for c.12% of infant milk powder revenue in 1H) and adult milk powder (still small revenue contribution), are making increasing revenue contribution (in % terms). The company is also looking at opportunities for expanding into other categories, such as cheese and infant complementary food. Margins could still trend down in longer term with increasing contribution from children (GPM c.60%) and adult milk powder (GPM of premium SKUs c.50%).
- **Valuation.** Our new TP is based on an unchanged 11.5x end-22E P/E which still represents -1sd below its long term average. In our view, the low earnings visibility of the IMF industry has not convinced us of a valuation roll-over at the moment.

Earnings Summary

(YE 31 Dec)	FY20A	FY21A	FY22E	FY23E	FY24E
Revenue (RMB mn)	18,592	22,776	21,177	23,536	25,851
YoY growth (%)	35.5	22.5	(7.0)	11.1	9.8
Net profit (RMB mn)	7,436.9	6,871.0	5,228.9	6,112.1	6,672.2
EPS (Basic) (RMB)	0.83	0.77	0.59	0.68	0.75
YoY growth (%)	72.6	(7.5)	(23.9)	16.9	9.2
Consensus EPS (RMB)	na	na	0.68	0.77	0.86
P/E (x)	15.9	18.6	9.3	8.0	7.3
P/B (x)	6.6	6.1	2.1	1.8	1.6
Yield (%)	1.9	2.7	4.3	5.0	5.5
ROE (%)	48.3	35.5	24.0	24.7	23.1
Net gearing (%)	Net cash	Net cash	Net cash	Net cash	Net cash

Source: Company data, Bloomberg, CMBIGM estimates

BUY (Maintain)

Target Price	HK\$7.60
(Previous TP)	HK\$8.40)
Up/Downside	28.3%
Current Price	HK\$5.92

China Consumer Staples-Food and beverages

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Stock Data

Mkt Cap (HK\$ mn)	54,248.6
Avg 3 mths t/o (HK\$ mn)	7.2
52w High/Low (HK\$)	13.96/5.80
Total Issued Shares (mn)	8,893.2

Source: FactSet

Shareholding Structure

Garland Glory Holdings Limited	43.6%
North Haven Private Equity	7.8%
Asia IMF Hold	

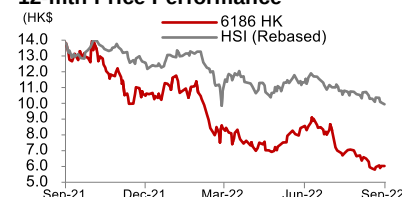
Source: HKEx

Share Performance

	Absolute	Relative
1-mth	-8.3%	-3.4%
3-mth	-28.8%	-19.8%
6-mth	-27.8%	-22.8%

Source: FactSet

12-mth Price Performance



Source: FactSet

Related Reports

1. [China Feihe \(6186 HK\) – 1H softer than expected: a lower 2022E despite a sequentially better 2H – 25 Jul 2022](#)
2. [China Feihe - 2H sets to recover when channel restructuring completes as planned – 30 Jun 2022](#)

Figure 1: Earnings revision

RMB mn	New			Old			Diff (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	21,177	23,536	25,851	21,156	23,593	26,009	0.1%	-0.2%	-0.6%
Gross Profit	14,116	15,821	17,484	14,400	15,931	17,400	-2.0%	-0.7%	0.5%
EBIT	7,389	8,621	9,405	7,763	9,169	9,911	-4.8%	-6.0%	-5.1%
Net profit	5,229	6,112	6,672	5,564	6,572	7,103	-6.0%	-7.0%	-6.1%
EPS (RMB)	0.57	0.67	0.73	0.61	0.72	0.78	-6.0%	-7.0%	-6.1%
Gross Margin	66.7%	67.2%	67.6%	68.1%	67.5%	66.9%	-1.4ppt	-0.3ppt	0.7ppt
EBIT Margin	34.9%	36.6%	36.4%	36.7%	38.9%	38.1%	-1.8ppt	-2.2ppt	-1.7ppt
Net Margin	24.7%	26.0%	25.8%	26.3%	27.9%	27.3%	-1.6ppt	-1.9ppt	-1.5ppt

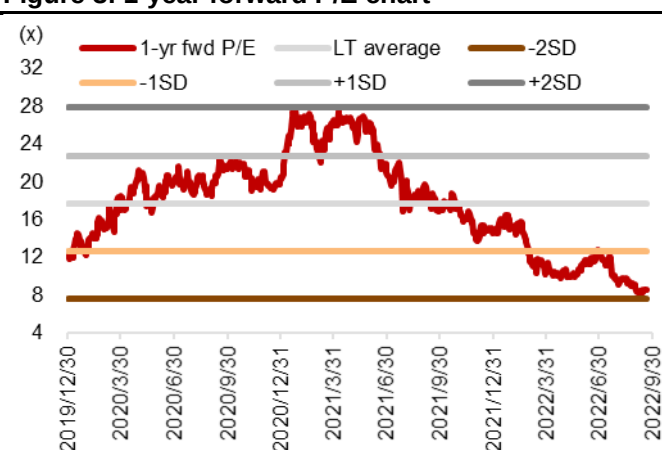
Source: Company data, CMBIGM estimates

Figure 2: CMBIGM estimates vs consensus

RMB mn	CMBIGM			Consensus			Diff (%)		
	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E	FY22E	FY23E	FY24E
Revenue	21,177	23,536	25,851	22,631	25,313	28,120	-6.4%	-7.0%	-8.1%
Gross Profit	14,116	15,821	17,484	15,239	17,075	18,894	-7.4%	-7.3%	-7.5%
Operating Profit	7,389	8,621	9,405	7,608	9,661	10,661	-2.9%	-10.8%	-11.8%
Net profit	5,229	6,112	6,672	6,200	7,011	7,761	-15.7%	-12.8%	-14.0%
EPS (RMB)	0.57	0.67	0.73	0.68	0.77	0.86	-15.3%	-12.4%	-14.3%
Gross Margin	66.7%	67.2%	67.6%	67.3%	67.5%	67.2%	-0.7ppt	-0.2ppt	0.4ppt
EBIT Margin	34.9%	36.6%	36.4%	33.6%	38.2%	37.9%	1.3ppt	-1.5ppt	-1.5ppt
Net Margin	24.7%	26.0%	25.8%	27.4%	27.7%	27.6%	-2.7ppt	-1.7ppt	-1.8ppt

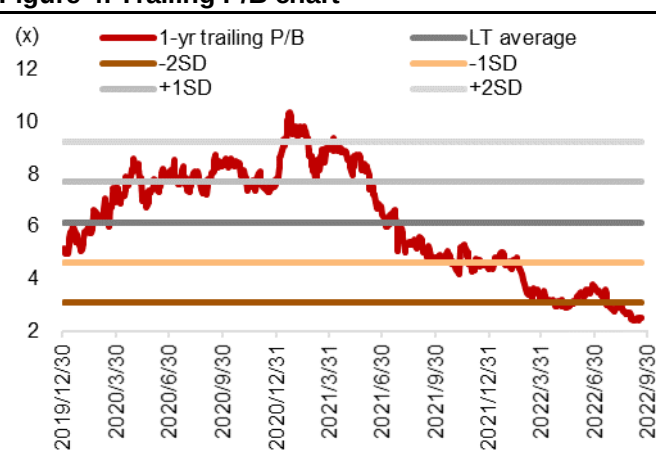
Source: Company data, CMBIGM estimate

Figure 3: 1-year forward P/E chart



Source: Bloomberg, CMBIGM estimates

Figure 4: Trailing P/B chart



Source: Bloomberg, CMBIGM estimates

Financial Summary

INCOME STATEMENT	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec (RMB mn)						
Revenue	13,722	18,592	22,776	21,177	23,536	25,851
Cost of goods sold	(4,112)	(5,112)	(6,769)	(7,061)	(7,715)	(8,367)
Gross profit	9,610	13,480	16,008	14,116	15,821	17,484
Selling expense	(3,848)	(5,263)	(6,729)	(7,200)	(7,532)	(8,272)
Admin expense	(913)	(1,161)	(1,208)	(1,271)	(1,412)	(1,551)
Others	819	2,788	1,774	1,744	1,744	1,744
Operating profit	5,668	9,844	9,844	7,389	8,621	9,405
EBITDA	5,849	10,110	10,288	7,899	9,222	10,089
Depreciation	(181)	(266)	(442)	(510)	(601)	(684)
Other amortisation	(0)	(0)	(1)	0	0	0
Net Interest income/(expense)	15	74	81	87	91	91
Other income/expense	0	(18)	(253)	(116)	(116)	(116)
Pre-tax profit	5,683	9,900	9,672	7,361	8,596	9,380
Income tax	(1,748)	(2,464)	(2,757)	(2,098)	(2,451)	(2,674)
After tax profit	3,935	7,437	6,915	5,262	6,145	6,706
Minority interest	0	0	(44)	(33)	(33)	(33)
Net profit	3,935	7,437	6,871	5,229	6,112	6,672
Core net profit	4,072	6,046	6,871	5,229	6,112	6,672
Net dividends	1,574	2,287	3,462	2,092	2,445	2,669

BALANCE SHEET	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec (RMB mn)						
Current assets	17,289	18,544	19,970	20,128	23,075	26,416
Cash & equivalents	7,377	10,059	9,629	9,753	12,484	15,613
Account receivables	314	289	477	438	487	534
Inventories	686	1,284	1,722	1,796	1,963	2,128
Prepayment	571	557	576	576	576	576
ST bank deposits	5,390	6,331	7,540	7,540	7,540	7,540
Other current assets	2,949	24	26	26	26	26
Non-current assets	5,715	9,778	11,512	13,009	14,141	15,183
PP&E	3,971	7,197	8,437	9,944	11,091	12,149
Right-of-use assets	377	366	428	428	428	428
Deferred income tax	209	376	474	474	474	474
Investment in JVs & assos	143	143	128	112	96	81
Intangibles	48	48	133	139	139	139
Other non-current assets	18,256	20,192	21,882	22,041	24,987	28,329
Total assets	23,004	28,323	31,481	33,137	37,215	41,599
Current liabilities	7,439	7,107	6,942	6,898	7,022	7,145
Short-term borrowings	3,094	448	313	213	213	213
Account payables	1,042	1,133	1,284	1,339	1,464	1,587
Tax payable	614	910	1,063	1,063	1,063	1,063
Other current liabilities	2,631	4,518	4,221	4,221	4,221	4,221
Lease liabilities	57	98	62	62	62	62
Non-current liabilities	2,536	2,030	2,136	2,036	1,936	1,936
Long-term borrowings	1,716	732	621	521	421	421
Obligations under finance leases	128	139	115	115	115	115
Other non-current liabilities	691	1,158	1,399	1,399	1,399	1,399
Total liabilities	9,974	9,137	9,078	8,933	8,958	9,081
Share capital	0	0	0	0	0	0
Retained earnings	13,030	17,747	20,921	22,688	26,709	30,936
Other reserves	0	0	0	0	0	0
Total shareholders equity	13,030	17,747	20,921	22,688	26,709	30,936
Minority interest	0	1,438	1,482	1,515	1,549	1,582
Total equity and liabilities	23,004	28,323	31,481	33,137	37,215	41,599

CASH FLOW	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec (RMB mn)						
Operating						
Profit before taxation	5,683	9,900	9,672	7,361	8,596	9,380
Depreciation & amortization	181	266	443	510	601	684
Tax paid	(1,748)	(2,464)	(2,757)	(2,098)	(2,451)	(2,674)
Change in working capital	562	1,253	(827)	21	(91)	(90)
Others	503	(1,204)	284	16	16	16
Net cash from operations	5,181	7,751	6,815	5,809	6,671	7,316
Investing						
Capital expenditure	(1,401)	(816)	(1,930)	(2,023)	(1,748)	(1,742)
Acquisition of subsidiaries/ investments	0	(757)	(286)	0	0	0
Net proceeds from disposal of short-term investments	0	0	16	16	16	16
Others	(4,114)	(2,213)	(244)	(16)	(16)	(16)
Net cash from investing	(5,515)	(3,786)	(2,444)	(2,023)	(1,748)	(1,742)
Financing						
Dividend paid	(2,704)	(2,685)	(3,392)	(3,462)	(2,092)	(2,445)
Net borrowings	3,070	(3,630)	(444)	(200)	(100)	0
Proceeds from share issues	5,984	0	(365)	0	0	0
Others	(2,226)	3,772	(44)	0	0	0
Net cash from financing	4,123	(2,543)	(4,245)	(3,662)	(2,192)	(2,445)
Net change in cash						
Cash at the beginning of the year	3,641	7,377	10,059	9,629	9,753	12,484
Exchange difference	(18)	(173)	(49)	0	0	0
Others	(34)	1,433	(506)	0	0	0
Cash at the end of the year	7,377	10,059	9,629	9,753	12,484	15,613
GROWTH	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec						
Revenue	na	35.5%	22.5%	(7.0%)	11.1%	9.8%
Gross profit	na	40.3%	18.7%	(11.8%)	12.1%	10.5%
Operating profit	na	73.7%	0.0%	(24.9%)	16.7%	9.1%
EBITDA	na	72.9%	1.8%	(23.2%)	16.7%	9.4%
Net profit	na	89.0%	(7.6%)	(23.9%)	16.9%	9.2%
PROFITABILITY	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec						
Gross profit margin	70.0%	72.5%	70.3%	66.7%	67.2%	67.6%
Operating margin	41.3%	52.9%	43.2%	34.9%	36.6%	36.4%
EBITDA margin	42.6%	54.4%	45.2%	37.3%	39.2%	39.0%
Return on equity (ROE)	na	48.3%	35.5%	24.0%	24.7%	23.1%
GEARING/LIQUIDITY/ACTIVITIES	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec						
Net debt to equity (x)	0.2	(0.1)	(0.0)	(0.0)	(0.1)	(0.2)
Current ratio (x)	2.3	2.6	2.9	2.9	3.3	3.7
Receivable turnover days	8.2	5.6	7.5	7.5	7.5	7.5
Inventory turnover days	60.9	91.7	92.8	92.8	92.8	92.8
Payable turnover days	92.5	80.9	69.2	69.2	69.2	69.2
VALUATION	2019A	2020A	2021A	2022E	2023E	2024E
YE 31 Dec						
P/E	14.1	15.9	18.6	9.3	8.0	7.3
P/E (diluted)	14.2	16.2	19.0	9.5	8.1	7.4
P/B	4.3	6.6	6.1	2.1	1.8	1.6
Div yield (%)	2.8	1.9	2.7	4.3	5.0	5.5

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

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