

Analyst: Sabina Cheng

Main Board Listing – Research

澳優乳業股份有限公司
Ausnutria Dairy Corporation Limited [Stock Code: 01717]
Joint Global Coordinators, Joint
Sponsors, Joint Bookrunners and Joint
Lead Managers
: Macquarie Capital Securities Limited

BOC International Limited

Sector : Food and Beverage

Business : A leading paediatric milk formula company in the PRC market

Total share offer: <u>300,000,000</u> shares (30.0% of the enlarged share capital) Public Offer: 30,00,000 shares (10%) Placing: 270,000,000 shares (90%)	<u>Business of Ausnutria Dairy (“The Group”)</u> <p>The Group is a leading paediatric milk formula company in the PRC market. It is principally engaged in the production, distribution and sale of high-priced and premium-priced paediatric milk formula products in the PRC market. Its paediatric milk formula products are produced from milk powder imported from Australia.</p> <p>The Group’s principal supply relationships are with the Australian-based dairy producers, namely Tatura and Murray Goulburn in Australia. The Group currently imports all of its products from its trading companies in the PRC. At present, it sells three different series of paediatric milk formula products, namely, A-choice Series, Best-choice Series and Allnutria Series.</p> <p>The Group has obtained Hazard Analysis and Critical Control Points and ISO 9000 certifications for its production process. In addition, the milk powder that it imports from Australian dairy producers is recognised by Australian Quarantine and Inspection Service in Australia and General Administration of Quality Supervision in the PRC, to be in compliance with the relevant requirements for exporting from Australia and importing into the PRC respectively.</p>
Price: HK\$3.60 – HK\$5.10 per share Market Cap: HK\$3.6 billion – HK\$5.1 billion Pro forma fully diluted FY09 P/E: 17.6x – 25.0x Adjusted NTA per share: HK\$0.76 – HK\$1.06 Staffing: 272 (as of 30 th June 2009)	
HK Public Offer period: 24 th Sep 2009 – 29 th Sep 2009 noon Receiving bankers: Bank of China (Hong Kong) Limited Hong Kong Share registrar: Computershare Hong Kong Investor Services Listing date: 8 th October 2009	

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Shareholders after Listing (Assuming the over-allotment option is not exercised)

All Harmony - Mr Chen Yuanrong owned 49.22% of the company, an executive director and CEO of the Group. The remaining portion is owned by 20 former and present employees of the Group.	20.00%
Brave Leader - Mr Wu Yueshi (59.57%), chairman and executive director of the Group. Ms X Wu (30.67%), the elder sister of Mr Wu Yueshi, and Mr Yan Weibin (9.76%), an executive director of the Group	6.00%
Silver Castle - Mr Wu Yueshi (59.57%), Ms X Wu (30.67%), and Mr Yan Weibin (9.76%)	33.30%
Ausnutria BVI - Mr Wu Yueshi (59.57%), Ms X Wu (30.67%), and Mr Yan Weibin (9.76%)	10.70%
Public Shareholders	30.00%
	100.00%

Use of Proceeds

Net proceeds from the offer are estimated to be HK\$833.5 million (based on an offer price of HK\$4.35, being the mid-point of the indicative price range and assuming the over-allotment option is not exercised)

	HK\$ million
To explore and undertake potential investment opportunities for investing in or acquiring upstream milk powder related assets and/or operations	250
To expand the Group's distribution network and strengthen its brand building, marketing and promotional initiatives	250
For enhancing the Group's research and development efforts	83.3
For complementing the Group's efforts in introducing its new series of organic paediatric nutrition products (including organic paediatric milk formula and organic infant supplements) and new products, and further expanding the range and quality of this series of products	83.3
To establish two new production lines for the production of the Group's paediatric milk formula products and to construct a new storage warehouse adjacent to the Group's existing production plant to cater for its anticipated business expansion, as well as other supporting facilities	83.3
For general working capital purposes	~ 83.6

Financial Highlights

	Year ended 31 st December			Six months ended	
	2006	2007	2008	30 th June 2008	30 th June 2009
	RMB '000	RMB '000	RMB '000	RMB '000	RMB '000
Revenue	93,716	186,526	405,166	174,634	320,972
Gross profit	45,273	78,797	146,003	66,376	136,261
Operating profit	15,425	28,234	80,354	34,549	91,250
Profit attributable to shareholders	11,853	22,373	70,529	30,179	65,161
Gross profit margin	48.3%	42.2%	36.0%	38.0%	42.5%
Operating profit margin	16.5%	15.1%	19.8%	19.8%	28.4%
Net profit margin	12.6%	12.0%	17.4%	17.3%	20.3%

Revenues Breakdown

	Year ended 31 st December						Six months ended			
	2006		2007		2008		2008		2009	
	(RMB '000)	%	(RMB '000)	%	(RMB '000)	%	(RMB '000)	%	(RMB '000)	%
A-choice Series	42,934	45.8	38,187	20.5	59,336	14.6	26,382	15.1	33,833	10.5
Best-choice Series	44,728	47.7	106,809	57.3	173,920	42.9	78,740	45.1	137,088	42.7
Allnutria Series	2,942	3.2	36,531	19.5	161,042	39.8	65,428	37.5	143,847	44.8
Others	3,112	3.3	4,999	2.7	10,868	2.7	4,084	2.3	6,204	2.0
Total	93,716	100.0	186,526	100.0	405,166	100.0	174,634	100.0	320,972	100.0



Strengths/Opportunities

- ✓ Targeting the high-end segment, we believe the Group can benefit from the sustainable increase in paediatric milk consumption given the increasing awareness of product quality and safety issues.
- ✓ The Group's income is expected to increase following the increase in its product mix. While Ausnutria explores new areas of the paediatric milk formula and rice cereal in 4Q 2009, more new products will also be launched shortly, as the Group is actively sourcing quality overseas suppliers.
- ✓ Driven by the increasing urbanization and affluence in China, the Group should have more opportunities to expand its premium brand in second and third-tier cities where foreign brands have little market presence.

Peer valuation comparison

	Ausnutria		Yili Industrial (A shares)		Mengniu Dairy (H shares)		American Dairy (US shares)		Synutra (US shares)	
	FY2009E	FY2010E	FY2009E	FY2010E	FY2009E	FY2010E	FY2010E	FY2009E	FY2010E	FY2009E
P/E ratio	16.1x*	20.9x*	33.4x	25.8x	26.1x	21.9x	10.6x	8.7x	68.6x	13.2x

Remark: (*) based on the mid- point of the indicative price range

Weaknesses/Threats

- × The Group depends on two Australian dairy producers, namely Tatura and Murray Goulburn, as its main suppliers of milk powder. Any shortage or suspension of milk powder from them could result in reduced production and revenue for the Group.
- × The Group once suffered from an incident called "Enterbacter Sakazaki Incident" in June 2008. Its milk powder was reported to be contaminated during the transportation process from its supplier to the PRC. The Group said the contaminated milk powder did not reach its plant nor was it offered for sale by the Group or its distributors to the public in the PRC. No penalties were imposed on the Group for this incident and its results of operations were not affected. Nevertheless, the Group, like its peers, is exposed to risk of contingent liability for any potential defective products.
- × For the respective periods ended as at 31st December 2006, 2007 and 2008, and the six months ended 30th June 2009, sales of the Group's top five distributors remained high, representing 25.1%, 37.9%, 27.5% and 28.2%, respectively, of its total revenue, whilst sales of the largest distributor represented 7.1%, 13.2%, 8.7% and 9.0%, respectively, of its total revenue. Any negative changes in its relationships with these distributors would have significant impacts on business operation results.

Recommendation: Trading Buy

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