Dairy Products China News

Guaranteed Exclusive Analysis

Welcome to the December issue of Dairy Products China News.

Vol. 14 Issue 12 2022

There is no doubt that 2022 has been very challenging for dairy commodity exporters, underlined by GDT event 322 down 3.8% just before the Christmas holiday. Whilst some importing markets have upped their volume requirements, the reduced buying from China has remained the key factor overall. When we see major dairying businesses such as Modern Dairy recording growth in milk production of 57% in the H1 period this year, this is a clear pointer to one of the main causes of the lower demand (and the recent slippage in commodity prices). The country's milk production has been growing rapidly, despite challenging weather conditions. This fits the drive for national food security, understandable in a country which suffered famine in the 1950s and 1960s. This is why China is now the world's leading importer of cereals – and why it halted fertiliser exports back in October 2021.

Another major factor has been the slowing of the Chinese economy for a range of reasons, not least the property crisis: in 2022, JP Morgan estimates that this specific problem will have cost China's economy one point of growth – close to a third of the expected 3% or thereabouts. Housing costs have had their worst effects in Beijing and Shanghai too – areas which are key motors of local consumption.

November's economic indicators were very discouraging. Will next year prove any easier any will this hold for dairy? Whilst the pandemic situation has been one factor which has made it very difficult for the government to increase the role played in the economy by domestic demand, the rapid rollback of the zero-COVID policy now in place does suggest that 2023 could indeed see a return to moderate growth – the February to April period next year looks like being the time this recovery will be seen, if so. Local stocks have been significant for many dairy commodities, but trade contacts suggest that these are easing back in some cases; their expectation is that demand for dairy products will benefit across the various channels IF the levels of cases remain limited, which seems unlikely according to current reports. If not, the many recent GDP growth forecasts for China of between 4-5% in 2023 will almost certainly end up being far too high. For now, though, we hope for the best, of course – wishing all readers a very happy 2023!

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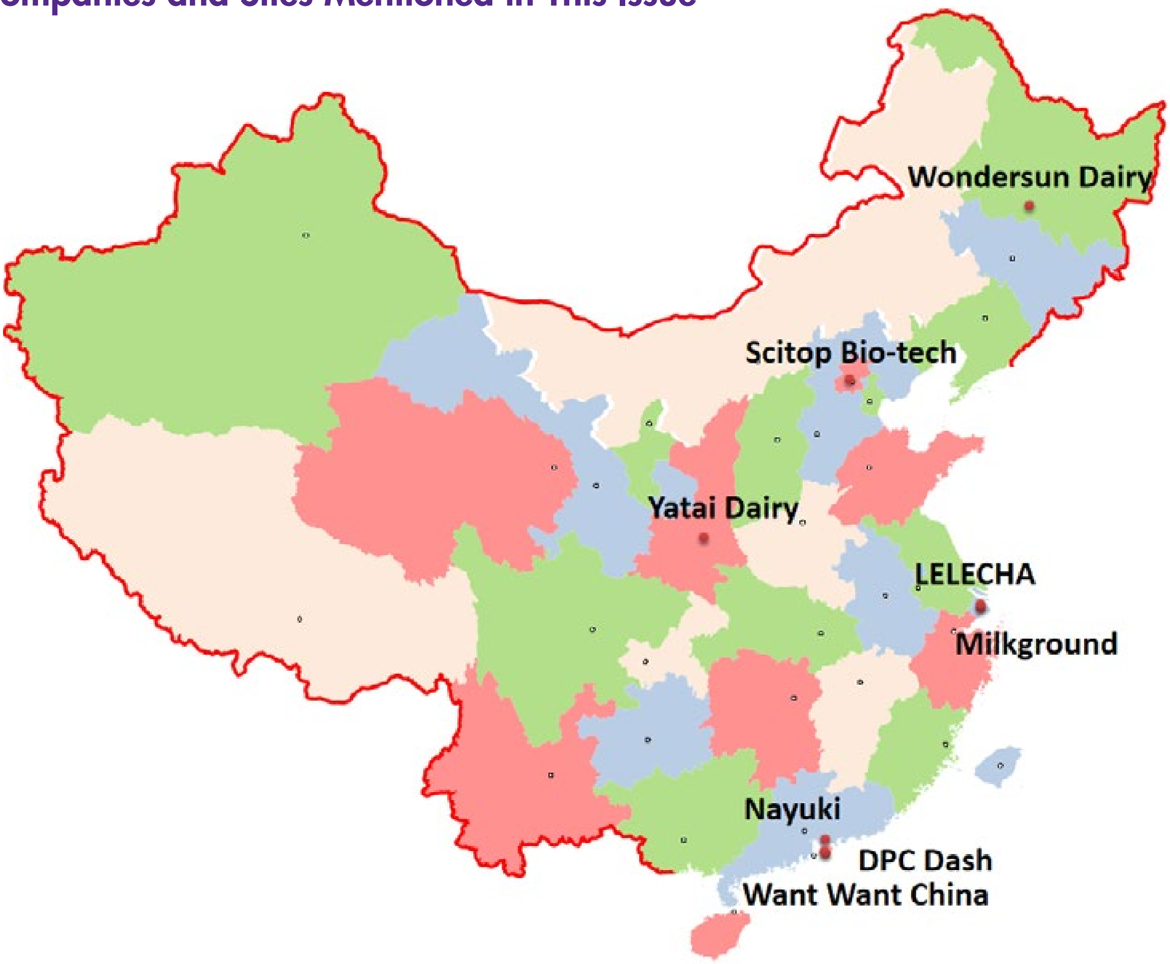
- In early Dec., details of 2 new dairy production projects were disclosed — Milkfly's 15,000 t/a cheese expansion project and Jiuding Food's 20 t/d AMF production project.
- In early Dec., the General Administration of Customs of China (GACC) posted a notice allowing camel dairy product imports from the United Arab Emirates (UAE), and announced the 2nd Russian dairy company approved for export to China in 2022.
- Want Want China announced 4.8% and 25.5% declines in revenue and profit in its report for April–Sept. 2022, with sales of dairy products and beverages down 13.2% YoY.
- On 5 Dec., Nayuki made a move to become the lead stakeholder in LELECHA with an agreement to acquire 43.64% of the business for USD73.7 million (RMB525 million).
- On 20 Nov., DPC Dash Ltd., Domino's Pizza China operator, passed the listing hearing of the Hong Kong Stock Exchange (HKEX). The company's sales have been growing over the past 3 years, but so have its net losses, even though these eased in H1 2022.
- Fonterra announces significant EBIT growth and resilient performance in China in Q1 FY2023.
- China's milk price has remained low in the last month of 2022, whilst reduced soybean meal prices have alleviated some of the cost-side pressures for producers who are hoping that the country's recent lifting of COVID restrictions may gradually revive dairy demand.

Major Companies and Sites Mentioned in This Issue



Market Analysis

Concentrating IMF Market in China

Summary: *In March-Nov., nearly 100 brands achieved re-registrations of infant formula products to conform to the new national standards in a process encouraging higher concentration in this market.*

Registration renewals for infant formula products have been continuing.In this transitional period to the new national standards for IMF – Infant Formula Foods (GB 10765-2021), Formula Foods for Older Infants (GB 10766-2021) and Formula Foods for Young Children (GB 10767-2021) – which all become effective on 22 Feb., 2023.

In March-Nov. this year, the State Administration for Market Regulation approved registrations of 274 formula products from 96 formula brands which were nearing the end of their registrations under the national standards in place since H2 2017, including:

- Most major domestic manufacturers such as Inner Mongolia Yili Industrial Group Co., Ltd. (Yili, Stock Code: 600887), China Feihe Limited (China Feihe, Stock Code: HK.06186), Beingmate Co., Ltd. (Beingmate, Stock Code: 002570) and Junlebao Dairy Group Co., Ltd. (Junlebao)
- SMEs such as Shaanxi Baiyue Youlishi Dairy Co., Ltd., Shanghai Newbaze Industrial Group Co., Ltd. Xi'an Yinqiao Dairy Industry (Group) Co., Ltd., Shaanxi Jinniu Dairy Co., Ltd., Guangzhou Meishuli Nutrition Co., Ltd., and Jiangxi New Born Dairy Nutrition Co., Ltd., in all accounting for 68 formula registrations
- Foreign players shown in published lists are Mead Johnson, Nestlé / Wyeth, Danone and Abbott Nutrition
- The 3 brands with most registrations are China Feihe (43), Junlebao (21) and Yili (18)

Raised Thresholds

The new national standards impose higher requirements for macro- and micro-nutrients in formula food for infants and young children, making it hard for some SMEs to secure renewal on even one product line.

- Registration costs: To meet the new national standards and re-registration rules, applicants should conduct and pass stability tests at least 3 times, each of 5 tonnes – products tested are not allowed for sales; it is estimated that each factory faces costs of at least USD1.4 million (RMB10 million) for re-registration
- Application limit: Each applicant can only apply for *"3 product lines (3 stages per product line)"* and each line needs to have a distinctive formulation

Accelerating Market Concentration

A more highly concentrated IMF market is a certainty. Compared with the 1,000+ formula products registered under the current standards, re-registration has led to a substantial decline in numbers, even though next year may see more foreign brand registrations, which generally take longer to process.(as foreign brands need registration approval in their countries before exporting to China, so face an extra step compared with to the domestic ones).

Trade sources indicate that many SME formula companies have prepared for the worst applying both for infant formula and adult formula registrations — if they pass they can push forward on IMF, if they fail they can shift to targeting the adult segment. Some have decided not to attempt re-registration or have only extended their registrations based on the existing standards. Once the new standards come into effect, products not conforming are barred from further production, so there are only 3 months left for those failed in re-registration to maximise their business from that last period.

The intention is that greater industry concentration will encourage higher quality from fewer businesses with more to lose if problems arise.

Liquid Dairy Trends Report

Summary: *In Q1-Q3 this year, China's sales of liquid dairy products grew in value terms, with the ambient segment growing whilst the fresh segment declined, according to a recent jointly published by the Economic Daily (a Chinese state-owned newspaper) and Yili on 5 Dec.*

On 5 Dec., the Economic Daily (a Chinese state-owned newspaper) and Yili jointly published its Q1-Q3 Dairy Products Consumption Trend Report, with analysis of consumer data from Kantar. This shows that China's sales of liquid dairy products (UHT/fresh milk, UHT/chilled yoghurt, milk beverages and lactobacillus drinks) grew over this period of 2022, and that ambient products grew fastest — premium pure milk in particular — whereas fresh products declined overall, as did sales of imported liquid dairy products.

The trends are provided in terms of value, but it is worth noting whilst many consumers' economic positions have been difficult, has inflation remained at a relatively moderate level. The country's CPI rose by 1.6% YoY in November, down from a 2.1% rise in October – after rising only 1.7% YoY in H1.

As a context for considering volumes, national milk production of 27.09 miilion tonnes in Q1-Q3 was up 7.7 YoY, whilst national dairy product output of 23.10 million tonnes in that period was up 2.6 YoY.

Sustained Growth in Liquid Dairy in Q1-Q3

Sales value was up by 1.7% YoY with 99.1% market penetration, due to higher sales volumes per order as people stocked up on food during the pandemic, and to higher demand in urban areas. However, consumers have been cutting back on the number of purchases and changing their buying channels and spending habits, becoming more sensitive to prices of liquid dairy products in general, limiting sales growth.

- Ambient liquid dairy: sales up 3.5% YoY, higher than the overall category average growth
- Chilled liquid dairy: sales continued to fall by 4.9% YoY, due to fewer consumer purchases; this followed the fall of -6.1% in 2021 (-5.2% in H1 2021)

Sales in upper-tier cities performed better: Beijing, Shanghai and Guangzhou saw 3.7% growth on average. In lower tier, county-level cities and counties, sales increased by only 0.8% YoY.

In distribution, as an extension of online to offline (O2O) retail, *"instant retail"* offering delivery within 30 minutes has grown and aided online sales overall, but at the same time squeezing business through the brick-and-mortar stores.

- Ambient liquid dairy: hypermarket sales down by 2.8% YoY vs. mini market and online sales up 10.1% and 6.3% YoY respectively
- Chilled liquid dairy: hypermarket sales down by 13.5% YoY vs. online sales up 17.3 YoY

TABLE 1: Retail Sales of Liquid Dairy Products, Q1-Q3 2022

Retail Channel	Market Share	YoY Change	Penetration
Hypermarkets	20.00%	-5.60%	45.6% (down)
Supermarkets	17.60%	-3.50%	47.2% (down)
Mini markets	/	7.80%	43.7% (flat)
Wholesale markets	/	10.20%	20.1% (flat)
Online retail	/	8.20%	/

Source: Q1-Q3 Dairy Products Consumption Trend Report

Growing Segments

Ambient dairy grew fastest, with functional and pure milks doing best due to consumers becoming increasingly health-conscious.

- Regular functional milk and pure milk: sales were up 15% YoY, averaging USD1.64/L (RMB11.7/L); market penetration reached 83.5%, an increase of 1.3 percentage points YoY
- Premium pure milk: sales were up 10%, averaging USD2.64/L (RMB18.8/L); market penetration was 77.1%, an increase of 2.1 percentage points YoY
- Mid-market products (high-quality functional milk and flavoured milk): sales were down 3%, averaging USD2.19/L (RMB15.6/L); market penetration was 54.3%.

Domestic Products Reinforce Their Position

As the competitiveness and brand reputations of Chinese products have continued to improve, their market share has risen at the expense of imported ones. This was especially the case in the ambient segment, whilst sales of domestic fresh dairy products fell much less than sales of the imported products as this segment slipped back.

TABLE 2: Sales of Domestic and Imported Liquid Dairy Products, Q1-Q3 2022

Item	Product Origin	Market Share	YoY Change in Market Share
Total	China	96.50%	2.60%
	Imported	3.50%	-5.80%
Ambient	China	95.70%	4.50%
	Imported	4.30%	-4.60%
Fresh	China	99.80%	-4.50%
	Imported	0.20%	-51.90%

Source: Q1-Q3 Dairy Products Consumption Trend Report

Two Powders Production Projects Approved in Dec.

Summary: *In Dec., 2 dairy powders production projects received environmental approval for construction start-up.*

On 5 Dec., 2 new dairy powder production projects received environmental approvals for construction start up, operated by Baotou Chevalese Dairy Group Co., Ltd. (Baotou Chevalese) and Xindongkang Nutrition Technology Co., Ltd. (Xindongkang Nutrition).

Baotou Chevalese

This company was founded in Nov. 2002 and is wholly owned by Inner Mongolia Chevalese Dairy Group Co., Ltd. It has a milk processing capacity of 150t/d and bulk milk powders production capacity of 6,200 t/a. The newly planned 2nd phase will expand the processing capacity to 500t/d.

2nd Phase Construction Details:

- Construction nature: Expansion
- Location: Tumd Right Banner Innovative Industrial Park, Baotou City, Inner Mongolia Autonomous Region
- Total investment: USD7.0 million (RMB50 million), including USD70,200 million (RMB500,000) for environmental protection
- Construction period: 6 months
- Construction content: 6-storey plant with 3,500 m^2 floor area, including production lines for bulk milk powders, sterilisation room, condensation room, feeding room, a cleaning-in-place (CIP) system for raw milk reception, along with the supporting equipment and facilities
- Processing capacity: 500 t/d of raw milk
- Product plan:
  - 17,000 t/a bulk milk powders (25kg/bag)
  - 13,000 t/a powders in 400g/bags, including 5,000 t/a IMF, 3,350 t/a powders for adults, 4,500 t/a sweetened powders and 150 t/a milk tea powder (made with 7,843 t/a bulk milk powders produced here and 5,157 t/a ingredients outsourced)
- Working system: 30 people in two 12-hour shifts for 276 days a year

Xindongkang Nutrition

This company was founded in Nov. 2005 with a registered capital of USD7.0 million (RMB64 million) and was previously known as Hebei Dongkang Dairy Co., Ltd. Its business includes dairy products (including milk powders), beverages, edible oil products, healthcare food, FSMPs, food additives and food flavours.

It has 4,800 t/a production capacity of formula powders for infants, school children, the middle-aged and elderly built in Sept. 2001, and 3,300 t/a demineralised whey powder capacity established in 2012 (reported as operational, whey origin unclear – local demineralisation is of course feasible but seems a precarious activity). Last month, it completed the construction work on a project to add 8,000 t/a capacity for polyunsaturated fatty acid (PUFA) microencapsulated powders.

Now it is to expand its dairy powders capacity.

Construction Details

- Construction nature: Expansion
- Location: Shijiazhuang Economic and Technological Development Zone, Hebei Province
- Total investment: USD1.7 million (RMB12 million), including USD2,808 (RMB20,000) for environmental protection
- Construction period: 2 months
- Production capacity:
  - Wet processing: 10,000 t/a of fat-filled demineralised whey powders, standard demineralised whey powder, modified milk powders, PUFA powder, etc
  - Dry processing: 10,000 t/a of formula powders for the middle-aged and elderly and other modified milk powders
- Working system: currently employing 166 people in three 8-hour shifts for 330 days a year

TABLE 3: Xindongkang Nutrition's Product Plan

No.	Product Item		Current Capacity, t/a	Planning Capacity, t/a	After Expansion, t/a
1	Demineralised Whey Powder		3,300	0	3,300
2	Dairy Powders for Wet Processing	Polyunsaturated Fatty Acid (PUFA) Microencapsulated Powder	8,000	-7,000	1,000
		Fat-filled Demineralised Whey Powders	0	5,000	5,000
		Demineralised Whey Powder	0	1,000	1,000
		Modified Milk Powders	0	3,000	3,000
3	Dairy Powders for Dry Processing		0	10,000	10,000

Source: Environment Impact Report

Progress on 2 Production Projects in Dec.

Summary: *In early Dec., details of 2 new dairy production projects were disclosed — Milkfly's 15,000 t/a cheese expansion project and Jiuding Food's 20 t/d AMF production project.*

In early Dec., a 15,000 t/a cheese expansion project for Miaofei Jiangsu Food & Technology Co., Ltd. (Milkfly) was announced on the official website of the Management Committee of the Economic and Technological Development Zone of Suqian City, Jiangsu Province.

Project Overview

- Construction nature: Expansion
- Total investment: USD5.3 million (RMB38 million), 7.11% (=USD0.4 million/RMB2.7 million) of which is for environmental protection
- Location: Economic and Technological Development Zone of Suqian City
- Site area: 7,000 m^2
- Construction period: 3 months
- Construction content: 42 new sets of production and auxiliary equipment including automatic filling equipment, sterilization equipment, laser coding machine, automatic packaging machine and intelligent storage shelves
- Designed capacity: 15,000 t/a of cheese products
- Working system: currently employing 40, to add 60 new workers in three 8-hour shifts for 300 days a year

Milkfly was established in July 2019 with a registered capital of USD10.3 million (RMB73.5 million). In Jan. 2021, it launched the *"O-sucrose"* cheese stick for children using monk fruit sweetener, a natural sugar substitute which is much sweeter than sugar and provides a point of differentiation in the category. The company received funding from Pantex China Ltd in a Series A funding round in June 2020 and another injection of USD14.0 million (RMB100 million) in a Series B round led by GL Ventures and followed by Eastern Bell Capital and Pantex China Ltd in Dec. of the same year.

TABLE 4: Product Plan for Milkfly's Expansion Project

Product	Current Capacity, t/a	Post-Expansion, t/a	Growth, t/a
Processed Cheese Sticks	3,000	13,000	10,000
Processed Mozzarella	7,000	7,000	0
Processed Cheese	0	5,000	5,000

Source: Miaofei Jiangsu Food & Technology Co., Ltd. (Milkfly)

Also this month a 20 t/d AMF production project by Inner Mongolia Jiuding Food Co., Ltd. (Jiuding Food)'s was approved by the Ecology and Environment Bureau of Hohhot City, Inner Mongolia Autonomous Region.

Project Overview

- Construction nature: New construction
- Total investment: USD1.4 million (RMB10.1 million), 1.09% (=USD15,444 million/RMB110,000) of which for environmental protection

- Location: The existing 90,576 m^2 plant area in Shengle Economy Park of Horinger County, Hohhot City, Inner Mongolia Autonomous Region
- Construction period: 6 months
- Product programme: 6,000 t/a or 20 t/d AMF, 10,500 t/a cheese (by-product); consumption: 16,500 t/a cream to produce AMF
- Working system: 10 people in three 8-hour shifts for 300 days a year

Jiuding Food was established in June 2007 with a registered capital of USD4.6 million (RMB33.0 million) and fixed assets worth USD8.4 million (RMB60 million). It produces ISO9000 certified AMF, premium edible linseed oil and purple perilla seed oil.

Governmental Direction

China Approves UAE Camel Dairy Imports and a Further Russian Dairy Exporter

Summary: *In early Dec., the General Administration of Customs of China (GACC) posted a notice allowing camel dairy product imports from the United Arab Emirates (UAE), and announced the 2nd Russian dairy company approved for export to China in 2022.*

On 8 March, China Customs published the Protocol of Inspection and Quarantine Requirements for the Imports of Dairy Products from United Arab Emirates (UAE) to China, confining the dairy products for entry to products made from camel milk as the main ingredient via proper heat treatment in UAE, including fermented dairy products and milk powders.

Related requirements:

Manufacturers

- The UAE manufacturers should be approved or registered with the authorities there, and also gain registration with GACC, subject to the animal health and public health regulations in both countries

Supplying Camel Farms

- No foot-and-mouth disease or suspected cases are reported at least one month before milk collection
- No clinical symptoms of anthrax are detected during milk collection
- No infection or suspected cases of Middle East respiratory syndrome coronavirus (MERS-CoV) are reported
- All farms are subject to the supervision of local competent departments
- All farms and their neighbouring regions are free from restriction relating to animal disease quarantine based on World Organisation for Animal Health's Terrestrial Animal Health Code or UAE's Animal Welfare Laws

Food Safety

- The imported dairy products comply with both countries' laws and regulations, and China's national food safety standards
- The production of the imported dairy products should use one of the processes below:
  - Ultra-high temperature sterilisation (UHT) at 13°C minimum for at least 1 second
  - High temperature short time pasteurisation (HTST) at 72°C minimum for15 – 240 seconds when pH in the products is below 7 (repeat HTST when pH in the products is 7 or above)

Packages and Labels

- The packages of the imported dairy products adopt materials that meet Chinese standards
- The registration number of the original manufacturer must be printed on the outer packaging; country of origin, product name, production date, shelf life, and manufacturer's registration number, name, address and contact number must to be displayed on inner packaging labels

Transportation / Storage Conditions:

- The imported products should be transported and stored under qualified sanitary conditions, free from poisonous and harmful substances. The shipping containers used should be sealed and numbered, with the seal number written on the product's sanitary certificates
- No damage or repacking of products occur during transportation.

2nd Russian Dairy Company Approved for Export to China in 2022

It was posted by Russia's Animal and Plant Inspection and Quarantine Service on 5 Dec. that the General Administration of Customs of China (GACC) has approved another Russian dairy company to export to China, the second this year, so there are now 54 Russian dairy processors approved to do so.

In March 2019, the Protocol on Veterinary and Public Health Conditions for Sino Russian Dairy Two-Way Trade was signed by the Chinese and Russian governments, facilitating dairy trade between two sides: dairy exports from Russia to China have increased from 2019 to 2021, notably for HS0401 (liquid milk/cream) from 93 tonnes to 707 tonnes and HS0404 (whey) from 5 tonnes to 1.532 tonnes. YTD, Russia's dairy exports to China have increased again dramatically, with additional export approvals believed to be likely in the coming years.

According to the agreement finally issued in 2020, the trade covers the following HS codes: 40110, 40120, 40140, 40150, 40210, 40221, 40291, 40229, 40299, 40310, 40390, 40410, 40490, 40510, 40520, 40590, 40610, 40630, 40640, 40690, 210500, 350110, 350220.

Company Dynamics

Want Want China Announces Mid-term Figures for FY2022

Summary: *Want Want China announced 4.8% and 25.5% declines in revenue and profit in its report for April–Sept. 2022, with sales of dairy products and beverages down 13.2% YoY.*

Want Want China Holdings Ltd. (Want Want China, HK. 00151), the local subsidiary of the Taiwanese Want Want Group, was established in 2007 and listed on the main board of Hong Kong Exchanges (HKES) in 2008. Its dairy product portfolio includes modified (reconstituted) milk – represented by its flagship *"Hot-Kid Milk"*, UHT/fresh milk and yoghurt, lactobacillus drinks, RTD coffee under the brand Mr. Bond Coffee, dairy candy, etc.

On 29 Nov., Want Want China announced its mid-term financial report for April–Sept. 2022 with key data as follows:

- Revenue: USD1.5 billion (RMB10.8 billion), down 4.8% YoY
- Operating profit: USD290.6 million (RMB2.1 billion), down 25.5% YoY
- Profit attributable to shareholders: USD224.1 million (RMB1.6 billion), slashed by 23.6% YoY

TABLE 5: Revenues by Category – Want Want China, April–Sept. 2022 vs 2021, USD million

Product category	April–Sept. 2021	April–Sept. 2022	Proportion	Trend
Rice crackers and extruded snacks	263.4	276.9	18.20%	5.10%
Dairy products and beverages (UHT/chilled flavoured milk and yoghurt, lactobacillus drinks, RTD coffee, juice drinks, sports drinks and Chinese herbal tea drinks)	921.3	799.3	52.60%	-13.20%
Leisure snacks (candy, ice cream & popsicle, biscuits, jellies, nuts, etc.)	403.5	432.3	28.40%	7.10%
Others (mainly alcohol)	9.9	12.5	0.80%	25.80%

Source: Mid-term Financial Report

Want Want China stressed the difficult market conditions due to the pandemic since April this year, hitting its whole supply chain and the market demand levels. Its profit and margins suffered as a result compounded by the rising material costs.

Costs & Profitability

- During the 6 months from April to Sept., its distribution costs rose by 2.2% YoY to USD869.7 million (RMB6.2 billion), pushing down its gross margin by 4 percentage points to 42.8% YoY (down 0.2 percentage poins vs. the second half of FY2021)
- Its margin on rice cracker and extruded snacks dropped by 3.8 percentage points to 37.2% YoY, due to rising costs for palm oil (40%+) and for energy
- On leisure snacks its margin was down by 2.4 percentage points to 42.2% YoY, primarily due to double-digit growth in costs of white granulated sugar, SMP and plastic packaging
- For dairy products and beverages the margin also fell 4.1 percentage points to 45.3% YoY, with the cost for WMP up 21% along with some rises in metal and paper packaging materials

Dairy Products and Beverages

- *"Hot-Kid Milk"*: This modified milk product made up over 90% of Want Want China's sales of dairy products and beverages, with sales down by 13.9% YoY, while dairy beverages saw sales decline by 2.1% YoY. Repeat COVID infections and increased control measures have affected the distribution and sales. As the backbone of the company's business, its sales rose to USD1.57 billion (RMB11.2 billion) in 2013 before shrinking to USD1.19 billion (RMB8.5 billion) in 2016. The latest annual date shows *"Hot-Kid Milk"* reach another sales record of above USD1.62 billion (RMB11.5 billion) in 2021. In 2017, *"Hot-Kid Milk"* represented nearly 60% of omni-channel sales in the children's dairy category (including pure/flavoured milk, UHT yoghurt, LAB drinks for children) in China, followed by Yili's *"QQ Star"* (2nd) and Mengniu's *"Future Star"* (3rd)
- To improve its product mix, *"Hot-Kid Milk"* has been relaunched in new packages (adding PET bottles to can, Tetra Pak briks and other specifications), aiming to take advantage of diverse consumption scenarios addressed through various retail formats; in addition, *"Nutty Milk"*, *"Everyday Milk"* and other new products with higher nutrition content and innovative flavours were also launched to meet the current market trends
- However, the reconstituted / modified milk market is under pressure from growing sales of fresh and ambient milk, especially in 3rd and 4th tier cities with improving cold chains

Overseas and China Operations

Overseas

- The group's revenues outside Taiwan and mainland China enjoyed double-digit growth as supply has picked up gradually to other regions such as the Americas, Asia Pacific, Southeast Asia and Oceania
- A Vietnamese factory also started up during the reporting period, providing a key production centre for its export business

Mainland China:

- Over 90% of its business is in mainland China
- The E-commerce distribution channels established rather recently accounted for sales of over USD14.4 million (RMB100.00 million), including online content platforms, social communities and fresh produce platforms, to be further explored to increase brand exposure online and drive overall sales
- Traditional wholesale channels were weakened by supply disruption, sales growth falling to single digits
- Approaching the year end, Want Want China said it is planning to update its instore displays and launch more snack combinations in preparation for shopping in the run-up to the Chinese Spring Festive, aiming to kick-start growth for the next 6 months of its FY2022.

Nayuki to Become the No.1 Stakeholder in LELECHA

Summary: *On 5 Dec., Nayuki made a move to become the lead stakeholder in LELECHA with an agreement to acquire 43.64% of the business for USD73.7 million (RMB525 million).*

On 5 Dec., the tea chain Nayuki Holdings Ltd. (Nayuki, Stock Code: 02150) announced a deal to invest USD73.7 million (RMB525 million) in acquiring 43.64% of Lelecha Group Ltd, owner of the new-style tea drink brand LELECHA – making it the lead shareholder in the business

Disclosed agreement details:

- LELECHA is one of the leading brands in China's freshly-made tea drinks industry, well recognised in the eastern parts of the country. This investment helps Nayuki strengthen its competitive position and reduce costs for further expansion
- LELECHA will remain an independent operation with no changes in brand strategy, staff composition and operations, but supported by Nayuki in store expansion, supply chain, internal management etc
- The terms include helping LELECHA go public if the brand meets the agreed performance targets for 2025-2027 and required conditions for listing on Nasdaq, NYSE, or the exchanges in China.

LELECHA was founded in Shanghai in 2016, operating a similar business to Nayuki, using a *"whole DTC + social commerce"* model, with a product range based on *"tea drinks + European-style soft bread"*. As of 3 Nov., LELECHA owns 140 physical stores in 21 cities across China, mainly located in the east – this is expected to rise to 158 before the lunar new year of 2023, and to 400 by the end of 2023.

LELECHA's net assets were USD27.2 million (RMB193.7 million) in 2020 and USD25.6 million (RMB182.4 million) in 2021, with turnovers of USD102.2 million (RMB727.6 million) in 2020 and USD122.1 million (RMB869.9 million) in 2021, but making losses after taxes of USD2.9 million (RMB20.6 million) and USD2.6 million (RMB18.2 million) for the two years.

It has completed 4 rounds of financing to date, a RMB200 million pre-A round in 2019 and three later strategic financings. The last of these, in July 2020, estimated the brand value at USD240.1 million (RMB1.7 billion) vs. the USD168.5 million (RMB1.2 billion) in this acquisition by Nayuki deal.

Nayuki, founded in Shenzhen in Nov. 2015, led the trend for such chains and now operates with 3 core product groups- *"freshly-made tea drinks"*, *"Nayuki Tea"* (bagged/loose tea) and *"RTD bottled fruit tea"*.

It went public on HKSE and became the first listed new-style tea drink brand on 30 June, 2021. In 2021, it reported annual revenues of USD603.7 million (RMB4.3 billion), with locations in 80 cities across China. YTD it has opened over 200 new physical stores, with 1,000 stores open in total by Nov. and many new openings expected in 2023.

Apart from this acquisition, it has also invested in emerging businesses like Cha's Mask (a tea drink chain), AOKKA and HUHU COFFEE (coffee chains), and He (Studio) (bakery brand) this year, although its investment in LELECHA is the largest such deal so far in 2022 for both Nayuki and the new-style tea drink sector overall.

Currently, HEYTEA, Nayuki and LELECHA are the top 3 brands in the premium tea drink segment in China, so competition will only intensify after this deal.

DPC Dash Passes HKEX Listing Hearing

Summary: *On 20 Nov., DPC Dash Ltd., Domino's Pizza China operator, passed the listing hearing of the Hong Kong Stock Exchange (HKEX). The company's sales have been growing over the past 3 years, but so have its net losses, even though these eased in H1 2022.*

On 20 Nov., Domino's Pizza Inc.'s local operator DPC Dash Ltd. (DPC Dash), passed the listing hearing of the Hong Kong Stock Exchange (HKSE) on its 2nd application on 14 Oct., after its first IPO application on 28 March was declared invalid.

Recent Financials of DPC Dash:

- Revenue:
  - 2019 – USD117.5 million (RMB836.6 million)
  - 2020 – USD155.0 million (RMB1,104.1 million)
  - 2021 – USD226.2 million (RMB1,611.3 million)
  - H1 2022 – USD127.6 million (RMB908.8 million), up 18.6% YoY
- Net loss:
  - 2019 – USD25.5 million (RMB181.6 million)
  - 2020 – USD38.5 million (RMB274.1 million)
  - 2021 – USD66.1 million (RMB471.1 million)
  - H1 2022 – USD13.4 million (RMB95.5 million), down 53.5% YoY
- Materials costs:
  - 2019 – USD32.0 million (RMB228.1 million) – 27.3% of revenue
  - 2020 – USD43.6 million (RMB310.5 million) – 28.1% of revenue
  - 2021 – USD59.8 million (RMB425.6 million) – 26.4% of revenue
  - H1 2022 – USD34.7 million (RMB247.2 million) – 27.2% of revenue
  - Meat (mainly pork and chicken), dairy products (mainly cheese) and sauces & seasonings collectively make up 65-70% of the total costs here
- DPC Dash explained that its substantial investment in market development including opening new locations and central kitchen units has been the primary cause for the consecutive net losses – also predicting another net loss for 2022 overall

The proceeds from this IPO are to be used in store network expansion, central kitchen production ramp-up, and in building technical competence to improve operations and service.

Fast Expanding

DPC Dash's stores are concentrated in 1st tier cities. As of June 2022, 77.56% were in Beijing, Shanghai, Shenzhen and Guangzhou, 56% in Beijing and Shanghai alone. Its store total grew at a CAGR of 35.53% from 188 to 465 in 2019-2021, and had reached 508 by 30 June 2022. The company's expansion plan envisages 120 new openings in 2022 and 180 in 2023.

Store operating margins also rose by 4.1%, 3.4%, 8.9%, and 9.2% from 2019 to 2021 and in H1 2022 respectively.

Labour Cost Pressure

Domino's 30 minutes delivery guarantee that differentiates it from competitors has brought forward great benefits. In 2021 and H1 2022, delivery orders accounted for 73.2% and 71.5% of its revenues; but does lead to high payroll costs at the same time. As of June 2022, DPC Dash has 3,199 full-time employees and 9,705 part-timers, 6,500 (=over 50%) of which are delivery staff. In 2019-2021, the annual wages for delivery staff and store staff amounted to USD47.2 million (RMB336 million), USD65.8 million (RMB469 million) and USD98.7 million (RMB703 million), representing 40.1%, 42.5%, and 43.7% of revenue in these years.

Central Kitchens

The company has 3 central kitchens in Shanghai (East China), Sanhe City of Hebei (North China) and Dongguan City of Guangdong (South China), offering semi-processed or processed food and ingredients for stores within a radius of 350 km in 12 cities. Demand from new stores could be met by ramping up production or storage capacity, so there are no plans for new central kitchens during 2023 at least.

DPC Dash was founded in 2008 and acquired Domino's Pizza's exclusive franchise in Beijing, Tianjin, Shanghai, Jiangsu and Zhejiang in 2010. In 2017, its franchise operations expanded to more inland regions as well as Hong Kong and Macau. In 2021 it accounted for 4.4% of China's pizza market, 3rd behind Pizza Hut (37.4%, entered China in 1990) and Champion Pizza (6.0%, a domestic brand founded in Hangzhou in 1998). The top two have 2,590 and 2,150 stores in China.

Fonterra Announces Significant Growth in Q1 FY2023

Summary: *Fonterra announces significant EBIT growth and resilient performance in China in Q1 FY2023.*

On 8 Dec., Fonterra issued its latest financial results, reporting substantial improvement in normalised earnings before interest and taxes (EBIT) and resilient growth in Greater China in Q1 FY2023 (three months ended 31 October).

Financial Summary in Q1 FY2023

- Normalised EBIT: up 94% YoY to USD237.3 million (NZD368 million)
- Normalised profit after tax: up 84% YoY to USD138.0 million (NZD214 million)
- Growth was primarily driven by continued strong margins in protein and cheese products, especially casein and caseinate used in food applications for medical nutrition and processed cheese
- Foodservice sector performance improved, but the high cost of milk continues to impact margins in both Consumer and Foodservice.
- It notes that global market volatility including changes in Greater China has depressed WMP demand; its milk reference collection price was lowered from USD5.48-6.45 (NZD8.50-10.00) per kgMS to USD5.48-6.13 (NZD8.50-9.50) per kgMS during the reporting period
- Total milk supply has returned to normal levels as a result of lower milk collections this season

Performance in Greater China

In this FY Q1, its business performance in Greater China has remained strong, said Dehan Zhou, CEO of Fonterra Greater China, adding that the company will continue to innovate and provide high value-added solutions to customers and partners, to help industry partners to address challenges while introducing New Zealand-sourced quality dairy products to Chinese consumers through various channels. In FY2022 ended on 31 July 2022, Greater China sales of USD4.29 billion (NZD6.66 billion) were up 6% and made up 1/3 of Fonterra's global revenue.

Sector Summary

- Dairy ingredients:
  - Protein ingredient sales saw good results, both WPC and MPC for ambient yoghurt
  - Sales of cheese products stayed high, as well as casein and other ingredients for processed cheese
  - Cooperation with Chinese dairy farms has been stepped up, including supply of grass-fed milk and application of New Zealand dairy ingredients
- Foodservice:
  - Anchor's milk fat products were selling in 445+ cities in China by the end of Q1 FY23, 14 of which are new markets penetrated in the quarter
  - More efforts will be directed to the bakery sector (an important user of products such as butter, AMF, cream etc
  - Sales of Anchor cream cheese used on new types of beverages in coffee stores have been very successful, and Fonterra has been in discussions with 100+ local boutique coffee chains in Nanjing, Hangzhou and Qingdao on dairy supply cooperation
- Innovations:
  - Product upgrade and premiumisation are being emphasized due to the rapid trend toward healthier and nutritional products, prompting new product launches such as Mainland Unsalted/Salted Butter
  - On the other hand, the impact of the pandemic controls has led to some restructuring of the cold chain for imported foods, and Fonterra has recently promoted ambient cream products to counter recent bottlenecks in cold chain logistics

In dairying, on 30 Nov., Fonterra launched a 5-year sustainable strategic development cooperation programme with Nestlé starting in Dec 2022, aiming to build a commercially-viable net-zero dairy farm that could cut 30% of carbon emissions by mid-2027 and reach zero emission in 10 years through increased use of technologies in farm management. The programme is also designed to benefit the local farming community, planning to commerce with around 50 farms and then scale up over the next three years.

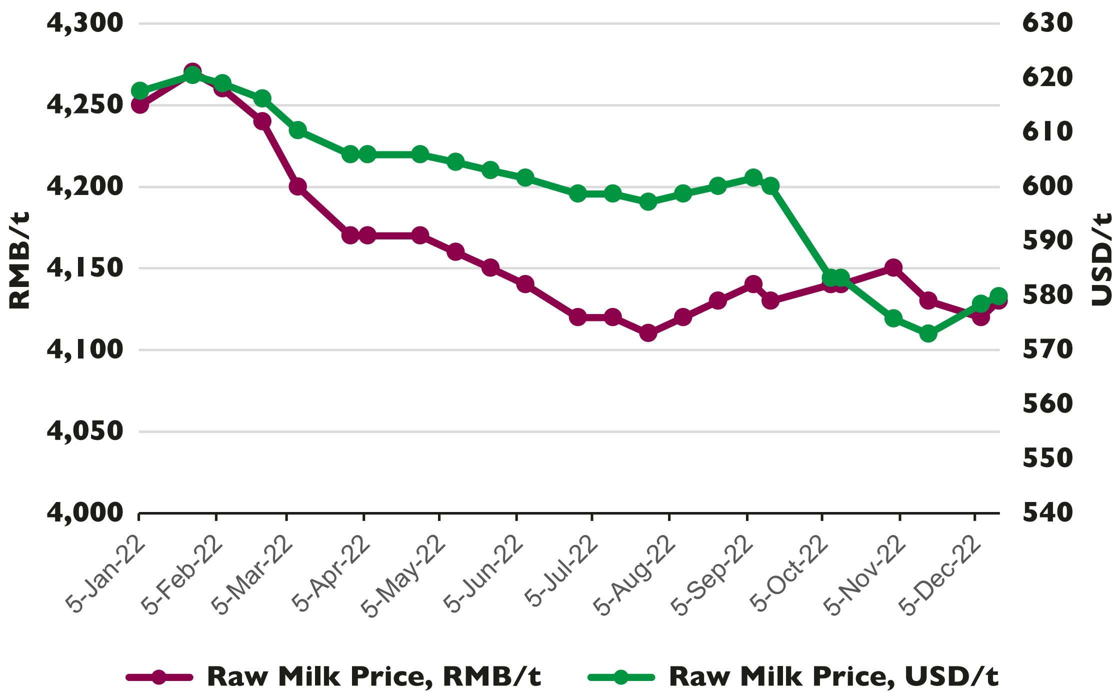
Raw Milk Price

Milk Price Ends Low in Dec.

Summary: *China's milk price has remained low in the last month of 2022, whilst reduced soybean meal prices have alleviated some of the cost-side pressures for producers who are hoping that the country's recent lifting of COVID restrictions may gradually revive dairy demand.*

As of 14 Dec., China's raw milk price averaged USD579.85/t (RMB4,130/t), up 0.2% MoM but still down 4.4% YoY. In Jan.-July, the price was falling, averaging USD577.75/t (RMB4,115/t) despite starting at USD598.81/t (RMB4,265/t) in Jan. In Aug.-Dec., the price has fluctuated in a range between USD578.45/t-USD582.66/t (RMB4,120/t-RMB4,150/t).

Figure I Trends in China's Raw Milk Price, Jan. 2022–Dec. 2022



Source: Ministry of Agriculture and Rural Affairs (MARA)

Post-pandemic Challenges and Opportunities

The sporadic COVID-19 outbreaks since March have meant repeated impacts on the production, transport and consumption of dairy products in China. The consequent lockdowns, reduced consumer demand and increased milk production (with more new farms coming online) have led to spray drying which has continued to this month. At present, some of the major dairy processors continue to sell powders at low prices, some are selling off farms at low prices, and some are discounting UHT milk to make this ever less attractive as an imported category.

China's *"20 Measures"* and *"10 New Measures"* released in Nov. and Dec. to address the pandemic situation aim to cancel temporary lockdowns and open full-scale dine-in restaurants and trans-regional transportation in steps. People's willingness to travel has increased and visits to foodservice outlets are gradually recovering.

The policy amendments and signs of recovering demand have boosted dairy stocks: on 22 Dec., Mengniu (Stock Code: HK.02319) led with a 4.59% increase in its share price, with Modern Dairy (Stock Code: HK.01117) enjoying a rise of 4.59% as well; other increases were China Feihe (Stock Code: HK.06186) up 1.93, Want Want China (Stock Code: 00151) up 1.75% and Ausnutria (Stock Code: HK.01717) up 0.48%.

Feed market

Data sourced on 14 Dec. by the Ministry of Agriculture and Rural Affairs (MARA) show:

- The national price of corn averaged USD431.03/t (RMB3,070/t), levelling off from the first week and up 5.9% YoY; the average in major production regions (Heilongjiang, Jilin and Liaoning) was USD395.93/t (RMB2,820/t) unchanged from the first week, while the price in the main demand area (Guangdong) was USD447.88/t (RMB3,190/t), up 0.3% from the first week
- The national price of soybean meal averaged USD731.48/t (RMB5,210/t), down 1.5% from the first week of the month and up 38.6% YoY. With imports of US soybeans arriving, factories have been running at pace increasing supply of soybean meal, meaning spot prices have fallen to the level of 2 months ago
- Meanwhile, data from the Feed Industry Association show the proportion of soybean meal used in feeds and concentrates was down by 0.6 percentage points MoM to 14.7% in Nov., in line with MARA's *Work Plan for the Reduction of Corn and Soybean Meal Substitution in Feed* issued in March 2021.

News in Brief

Dairy Imports in November 2022

November's import volumes present a very mixed bag – significant segments including cream, liquid milk, milk powders, cheese and lactose all show declines, whereas whey powders/permeate, butter, casein and whey proteins all grew. As expected, there is nothing here offering clarity on future trade prospects for individual segments – although the direction of travel appears relatively clear in overall terms. The revised COVID policy is already having an impact on demand, even though a difficult period with rising case numbers seems certain, but the fundamentals reflect the growing local milk production and evolving industry product mix.

TABLE 6: 2022 November Imports, tonnes

HS code	Product	202111	202210	202211	MOM	YOY
04011000	Milk & cream, fat ≤1%, not concentrated or sweetened	8,078.9	7,764.9	8,110.7	4.5%	0.4%
04012000	Milk & cream of >1% but ≤6% fat, not concentrated or sweetened	70,094.2	37,137.7	55,325.0	49.0%	-21.1%
04014000	Milk & cream, 6%	7.5	3.2	0.0	-100.0%	-100.0%
04015000	Milk & cream, fat >10%, not concentrated or sweetened	26,075.5	25,569.9	21,662.7	-15.3%	-16.9%
04021000	Milk & cream in solid forms,fat ≤1.5%, concentrated/sweetened	31,042.0	22,295.5	25,184.6	13.0%	-18.9%
04022100	Milk & cream in solid forms of >1.5% fat, concentrated, unsweetened	64,375.1	27,123.5	34,543.8	27.4%	-46.3%
04022900	Milk & cream in solid forms of >1.5% fat, concentrated, sweetened	189.6	307.5	69.5	-77.4%	-63.4%
04041000	Whey and modified whey	48,654.4	55,916.3	56,576.3	1.2%	16.3%
04049000	Products consisting of natural milk constituents, nes	464.1	240.0	440.0	83.3%	-5.2%
04051000	Butter	4,829.5	6,194.6	6,779.1	9.4%	40.4%
04059000	Other fats & oils derived from milk	1,445.1	3,961.3	3,829.5	-3.3%	165.0%
04061000	Fresh cheese, incl. whey cheese, curd	7,379.8	4,527.1	3,259.1	-28.0%	-55.8%
04062000	Grated or powdered cheese	4,352.0	2,442.1	3,653.9	49.6%	-16.0%
04063000	Processed cheese, not grated or powdered	1,726.2	1,459.6	1,375.6	-5.8%	-20.3%
04064000	Blue-veined cheese, other-veined cheese prod. by penicillium roqueforti	9.8	10.3	8.1	-21.2%	-17.2%
04069000	Cheese, nes	2,567.1	1,346.3	1,965.6	46.0%	-23.4%
17021100	Anhydrous lactose, lactose wt.≥99%	9,637.7	11,343.4	10,065.1	-11.3%	4.4%
17021900	Lactose syrup & other lactose	823.7	25.9	11.4	-56.1%	-98.6%
19011010	For infant food retail packaging formula,the defatted cocoa content < 5%	25,062.2	24,223.8	24,447.5	0.9%	-2.5%
35011000	Casein	982.8	1,209.3	1,980.1	63.7%	101.5%
35019000	Caseinates	2,396.5	1,764.5	2,118.3	20.0%	-11.6%
35022000	WPC80/WPI	3,180.5	2,563.2	3,462.8	35.1%	8.9%

Source: China Customs

China Bans Various Dairy Products from Entry in Oct.

On 24 Nov., the General Administration of Customs (GACC) released the October list of foods which were prevented from entering at the border, including various dairy products:

TABLE 7: China's Barred Dairy products in October 2022

HS code	Item	Place of origin	Manufacturer	Weight, kg	Reason of disqualification
1901101000	Nutrilon Growing Up Milk Formula, stage 4, 800g/can	Ireland	Nutricia Infant Nutrition Ltd.	3,328	Cu level not conforming the national standard
1901101000	Nutrilon Growing Up Milk Formula, stage 5, 800g/can	Ireland	Nutricia Infant Nutrition Ltd.	3,328	Vitamin D level not conforming the national standard
1901101000	Nutrilon Platinum Infant Milk Formula, stage 2, 800g/can	The Netherlands	Nutricia Cuijk B.V.	403	Protein level not conforming the national standard
2106909001	Nutrilon Pepti Baby Formula, stage 2, 800g/can	The Netherlands	Nutricia Cuijk B.V.	216	Vitamin D level not conforming the national standard
2106909001	Nutrilon Pepti Baby Formula, stage 2, 800g/can	The Netherlands	Nutricia Cuijk B.V.	864	Iron level not conforming the national standard
402210000	Camel Milk Formula with Probiotics (WMP)	Kazakhstan	VOSKHOD-2004LLP	799	Non-conforming labelling
404100090	Goat D90 (demineralised goat whey powder)	Spain	LACTEAS COBREROS S.A	100	Non-conforming packaging
2106100000	Myprotein Impact Whey Protein (vanilla flavour)	The UK	THEHUT.COMLTD	875	No proper certificates or required documents
2106100000	Myprotein Impact Whey Protein (milk tea flavour)	The UK	THEHUT.COMLTD	1,995	No proper certificates or required documents
2106100000	Myprotein Impact Whey Protein (strawberry flavour)	The UK	THEHUT.COMLTD	875	No proper certificates or required documents
1806200000	Myprotein Impact Whey Protein (chocolate flavour)	The UK	THEHUT.COMLTD	875	No proper certificates or required documents
406300000	Power Processed Red Cheddar Cheese	Taiwan, China	Samoa Power International Industrial Co., Ltd. (Taiwan Branch)	600	Excessive aerobic plate count

Source: General Administration of Customs (GACC)

Natural Dairy (NZ) Delisted from HKSE

Natural Dairy (NZ) Holdings Ltd (HK.00462) withdrew its request to resume listing on Hong Kong Exchanges (HKSE) on 24 Nov.

Before this, on 31 August 2021, the company submitted a new listing application which failed to complete within the required 6 months, lapsing on 28 February 2022. On 19 July 2022, it announced that the mandates of the professional parties involved in the resumption proposal (sponsor, legal advisers, auditors, property valuer etc) had not been renewed after expiry or would require further agreements before further work could commence. Thus the work for re-submitting the new application was halted, with no timeline set for re-submission, and to date the company remains unable to meet all the resumption conditions set by the Exchange. The company had sought a review of the Listing Committee's decision on 23 Aug., 2022, but then withdrew the review application on 11 Nov., 2022. The Listing Committee considered that Natural Dairy (NZ) had failed to make the resumption proposal within a reasonable period of time as required under under Practice Note 17 to the Listing Rules (PN17) and/or Rule 6.04. and had failed to take adequate action to meet all the resumption conditions – hence cancelling its listing from 28 Nov., 2022.

Natural Dairy (NZ), formerly China Jin Hui Mining Corporation, was registered in 2002 and listed on HKSE in June 2005. In 2009, it purchased 4 dairy farms from UBNZ Trustee Limited in New Zealand, shifting its business focus to dairy products from mining. Later on, it proposed to buy Crafar dairy farms, one of the biggest private dairy farms in New Zealand, only to find 3 board members of Crafar involved in serious fraud cases which meant the deal was off. As a consequence, Natural Dairy (NZ) was criticised by HKSE for failing to announce and obtain shareholders' approval in respect of a material change in the terms of a very substantial acquisition and suspended on 7 Sept., 2010. Its later application to HKSE on 31 Aug., 2021 to relist and change from being a dairy company into a real estate business lapsed on February 28, 2022 as it failed to meet the required conditions within six months.

Yatai Dairy Launches Upgraded Goat IMF

On 3 Dec., Shaanxi Yatai Dairy Co., Ltd. (Yatai Dairy) launched 3 upgraded goat milk formula ranges – *"Talent®"*, *"Joybast®"* and *"Xinbeibei®"* for infants from birth to 36 months. These products contain pure goat milk whey protein with improved nutritional formulations and are among the first batch approved as conforming to the new national standards.

- Talent:
  - Pure goat milk whey protein combined with 3rd-generation structured lipid OPO to augment absorption of nutrients
  - Lactoferrin content up to 180mg/100g, higher than the average level seen in 90% of the registered goat IMF
  - Including DHA, ARA and lutein, a combination of galacto-oligosaccharides (GOS) and fructo-oligosaccharide (FOS), and taurine, inositol, choline and other nutrient elements, to improve immunity, absorption, digestion, brain and bone development
- Joybast:
  - Adding lactoferrin, lutein, GOS, L-carnitineAdd and choline to the original formulation with DHA, ARA and probiotics, FOS and taurine; Lactoferrin content up to 92mg/100g, claiming functions in vision, immunity, absorption, digestion, brain and bone development
- Xinbeibei:
  - Lactoferrin content up to 92mg/100g
  - Including DHA, ARA, lutein, choline, GOS+FOS, and dual probiotics (Bifidobacterium animalis subsp. lactis HN019+Bifidobacterium animalis subsp. lactis Bb-12), to improve digestion and absorption.

Founded in 2004, Yatai Dairy has 80,000 goats and 4 automated production lines providing a processing capacity of 300 t/d raw milk and production capacity of 30,000 t/a dairy products.

PICTURE 1: Yatai Dairy's Upgraded Goat IMF Ranges

Source: Yatai Dairy

Wondersun Dairy Updates

Heilongjiang Wondersun Dairy Co., Ltd. (Wondersun Dairy, Stock Code: 600598) recently provided an update on its *"Golden Season"* formula range (for children above 3 years old, adults and the middle-aged and elderly) and on its premium IMF series *"Zhicai"*.

- *"Golden Season"*: The company now has 1,681 of its own *"Whole-family Nutrition (physical) Stores"* selling *"Golden Season"* formula series across the country – 14 flagship stores, 41 exclusively franchised stores and 1,626 standard stores. This network total 112% of its 2022 starting target of opening 1,500 such stores; its sales from these 1,681 stores have exceeded USD4.6 million (RMB33.0 million)
- "Zhicai": This range launched in late May 2022 now sells in some 5,000 physical stores, distributed via 400 dealers; a total of 1,111 *"Zhicai Exclusive (franchised) Stores"* and 400 of the company's own physical stores are in place; in Nov., the number of new customers and shelf sales ratio in these stores were up 24% and 53% MoM respectively

Earlier in 2019, Wondersun Dairy announced strategic development plan targeting revenue of USD1.4 billion (RMB10 billion) by 2025 and a market value after listing of above USD1.4 billion (RMB10 billion). To implement this plan, the company has put increasing efforts in brand building, product innovation, marketing and channel building and has earned first-mover advantage and recognition in the market as a result.

AustAsia Group Launches IPO on HKEX

On 16 Dec., the dairying business AustAsia Group Ltd. (AustAsia Stock Code: 2425.HK) launched an IPO on the Hong Kong Stock Exchange (HKEX), closing on 21 Dec. 2022, offering 3,064,000 shares at the price of USD0.74-USD0.90 (HKD5.79-HKD7.00) each, seeking up to USD27.54 million (HKD214.5 million). The company started trading shares on 30 Dec. 2022.

The proceeds from the IPO are to be used for the construction of *"Chunyuan"* No.4 Farm in Shandong and for the purchase of related equipment including 2 milking machines, 37 cattle feeders, cooling system, waste treatment facilities, testing and inspection devices, power generator, logistical support etc. The work on the new farm is expected to start in April 2023 and the farm is planned to reach full operation by Nov. 2024. Its capacity is 12,500 dairy cows (including 5,700 milking cows) with annual milk output close to 80,000 tonnes, representing a 13% increase in the company's total milk production.

The company is owned by the pan-Asian group Japfa Ltd. (62.5%), Meiji China (25%), Genki Forest (5%) through Plutus Taurus, New Hope Dairy (5%) through GGG Holdings Ltd, and Guangzhou Honest Dairy (Group) Co., Ltd. (2.5%). As of 30 June, 2022, AustAsia operated 10 standard dairy farms in China with a total of 111,424 dairy cows (57,383 adult milking cows).

Hyproca 1897 Pushes Upgraded A2 Milk Formula Products

Recently, Ausnutria has upgraded the *"Hyproca Hypure"* series (part of its premium IMF brand Hyproca 1897) with A2 β-casein and BB-12 probiotic (Bifidobacterium animalis subsp. lactis), FOS+GOS, indicating that this will make it easier to digest and ideal for the new-generation of parents' expectations of high quality. The company's fastest growing brand since 2019, Hyproca 1897 delivered annual revenues of USD446.8 million (RMB3.2 billion) last year, up by 17.9%, according to Ausnutria's financial report for 2021. In 2022, the company has launched 2 other new Hyproca 1897 products – *"Zhishu"* (lactose-free infant formula) and *"Hyproca 1897 Future Version"* (an HMO / Human Milk Oligosaccharides ultra-premium formula) – demonstrating its focus on high-end segments and the margins they can offer.

PICTURE 2: Hyproca 1897's Upgraded Fomula Hyproca Hypure

Source: Hyproca 1897

Scitop Bio-Tech Files Private Placement for Probiotics Capacity Improvement

In its registration statement on 1 Dec., Beijing Scitop Bio-tech Co., Ltd. (Scitop Bio, Stock Code: 300858.SZ) disclosed its plan to raise up to USD98.3 million (RMB700 million), of which USD87.0 million (RMB620 million) will be used for capacity improvement projects and USD11.2 million (RMB80 million) to supplement working capital.

At present, DuPont and Chr Hansen account for 80%+ of China's probiotic ingredients market, but Scitop Bio is building its position as the main domestic competitor.

The funding for a new probiotics factory in Horinger (Inner Mongolia) is to expand capacities of compound food additives, powdered probiotic strains and finished probiotic products x 3.86, x 14.33 and x 13.00 vs. their current levels, and to build additional capacities of 600 t/a for postbiotics and 100 t/a for fermentation agents for yoghurt. The facility is scheduled to start up in H2 2024 and reach full operation by 2017. If the demand is proven for these new lines, Scitop Bio expects its market shares in compound food additives and food-grade probiotic products (including probiotic materials, consumer products, fermentation agents for yoghurt, and probiotics) to rise to 13.33% and 28.38% from the current 5.26% and 4.02%.

Its plans will be supported by the company's recent gaining of international recognition – in late Oct., it signed a Probiotic License Agreement with Centro Sperimentale del Latte S.R.L. (CSL), an Italian culture producer, authorising CSL to manufacture and distribute Scitop Bio-tech's patented Lactobacillus Plantarum P-8 in Europe and North America exclusively.

TABLE 8: Capacity Planning for Scitop Bio-tech

Item	Compound food additives	Probiotic materials	Probiotic consumer products	Fermentation agents for yoghurt	Probiotics
Current capacity, t/a	3,500.00	30	100	–	–
Planning capacity, t/a	10,000.00	400	1,200.00	100	600
Total	**13,500.00**	**430**	**1,300.00**	**100**	**600**

Source: Scitop Bio-tech

Abbott Exiting Mainland China IMF Market

On 14 Dec., Abbott China announced it is halting production of all nutrition products for infant formula and children including Eleva, PediaSure and Similac in mainland China, a process to be managed in stages by next year, but gearing up for medical nutrition business in 2023. According to the announcement, its IMF products will still be available on online and offline stores during the transitional period. The cross-border E-commerce trade of Abbott infant and children nutrition products into China, as well as other Abbott operations in including diagnostics, medical devices and drugs in China remain unaffected.

In the face of fierce market competition over recent years, Abbott's retail IMF share in China has been falling according to Euromonitor, from 4.9% to 4.1% and then 3.6% over 2019-2021 and then to an estimated 3.1% in 2022 (vs. Feihe20.4%, Yili 14.4%, Danone 12%, Nestle 10%, Junlebao 10.5% and Biostime 3.5%).

Product quality issues have raised concerns. In May 2021, Abbott was fined USD1.3 million (RMB9.1 million) for excess vanillin in its stage 1 infant milk formula. In Feb. 2022, many Similac, Alimentum and EleCare IMF and FSMP made at its Sturgis, Michigan plant were recalled for potential exposure to Cronobacter sakazakii and Salmonella after two of the babies with Cronobacter infections died. After this, China Customs warned Chinese consumers to not purchase these products via any channels and stop using other IMF produced by Abbott.

Data from Abbott's report for Q3 2022 show sales down 4.8% YoY to USD10.4 billion and net profit slashed by 31.7% YoY to USD1.4 billion. Nutrition saw the biggest decline of its 4 main business operations, with sales down 14.9% YoY to USD1.8 billion, including a 24.8% drop in infant nutrition, accounting for sales of only USD827 million.

As China's IMF market becomes more concentrated, the exit of Abbott has only a minor impact on the overall market given its shrinking market share. It remains the case that international manufacturers still retain an edge in this market where technological innovation remains key for future development.

Milkground and Modern Dairy to Establish Dairy JV

On 13 Dec., Shanghai Milkground Food Tech Co., Ltd. (Milkground Food, Stock Code: 600882) published a proposal for a JV with China Modern Dairy Holdings Ltd. (Modern Dairy, Stock Code: HK.01117). Tentatively named Haoduoniu Animal Husbandry Technology Development Co., Ltd., this will have a registration capital of USD71.6 million (RMB510 million) – 40% from Milkground Food (USD28.6 million / RMB204 million) and 60% from Modern Dairy (USD43.0 million / RMB306 million).

Milkground Food said most of the raw materials for its cheese products are purchased internationally at present, but this JV could provide a strong local milk source by building or purchasing low-carbon, eco-friendly dairy farms, to some extent mitigating the vagaries of international procurement and improving the stability and safety of its supply chain.

As of 30 June, 2022, Modern Dairy owned 38 dairy farms with 383,000 cattle, up 52% YoY; in H1 its milk output hit a record 1.152 million tonnes, up 57% YoY, thanks to its larger farms and increasing milk yields per cow.

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