You should read the following discussion and analysis of our financial condition and results of operations together with our combined financial statements as of and for each of the years ended December 31, 2011, 2012 and 2013 and the accompanying notes included in the accountants' report set out in Appendix I to this [REDACTED]. Our combined financial statements have been prepared in accordance with IFRS. Potential investors should read the accountants' report in Appendix I in its entirety and not rely merely on the information contained in this section. The following discussion and analysis contains forward-looking statements that involve risks and uncertainties. For additional information regarding these risks and uncertainties, please refer to the section headed "Risk Factors" in this [REDACTED].

OVERVIEW

We are the largest organic dairy company in China and the only vertically integrated organic dairy company in China that meets E.U. organic standards, according to the F&S Report. We have a 54.2% market share in China based on 2013 organic raw milk production volume, according to the F&S Report. Together with our associate, Shengmu Forage, our unique vertically integrated "grass-to-glass" organic ("全程有機") production model covers the entire dairy industry value chain, meeting E.U. organic standards for all major stages of the dairy production process: forage growing, dairy farming to produce raw milk, and processing to produce liquid milk products. We are also a major player in premium non-organic raw milk market in China based on 2013 production volume, also according to the F&S Report.

We classify our businesses into the following two segments:

- *Dairy farming*. This segment consists of (i) sales of organic raw milk which accounted for 45.3% of our total raw milk sales volume in 2013. Out of the organic raw milk sales volume in 2013, 74.2% was sold to external customers including Mengniu Group, while the remaining 25.8% was used for downstream processing into our "Shengmu 圣牧" branded organic liquid milk products; (ii) sales of premium non-organic raw milk which accounted for 54.7% of total raw milk sales volume in 2013.

- *Liquid milk*. This segment engages in (i) processing our organic raw milk into packaged organic whole milk, low fat milk, and children's milk which are marketed under our own "Shengmu 圣牧" brand; (ii) selling our organic dairy products to consumers in China primarily through distributors.

As of December 31, 2013, we had a total of 30,621 organic dairy cows and 29,836 non-organic dairy cows. As of that date, all of our 13 organic dairy farms were located in the Ulan Buh desert while all of our 12 non-organic dairy farms were located in Hohhot, Inner Mongolia. A majority of our farms have a capacity to house between 2,500 to 4,500 cows. Our average annual milk yield in 2013 was 8.5 tonnes.

We have experienced rapid growth over the Track Record Period. Our revenue increased from RMB389.4 million in 2011 to RMB1,143.7 million in 2013, or a CAGR of 71.4%. Our profit for the year before biological fair value adjustments increased from RMB106.1 million in 2011 to RMB365.0 million in 2013, or a CAGR of 85.5%. Our gross margin was 29.4%, 33.4% and 42.9% in 2011, 2012 and 2013, respectively.

FACTORS AFFECTING OUR RESULTS OF OPERATIONS AND FINANCIAL CONDITION

Our financial condition, results of operations and the period-to-period comparability of our financial results are principally affected by the following factors:

- *Production volume of raw milk.* In line with our strategy to focus on expanding our organic raw milk and liquid milk businesses, we expect that our production volume of organic raw milk will grow significantly while our production volume of premium non-organic raw milk will increase at a slower pace. Our production volume is primarily driven by the size of our cow herd. As of December 31, 2011, 2012 and 2013, we had four, seven and 13 organic dairy farms, respectively, and 8,982, 14,111 and 30,621 organic dairy cows, respectively. We plan to build an additional 18 organic dairy farms by 2016 and grow our herd of organic dairy cows to approximately 120,000 organic dairy cows by that time. Production volume of raw milk is also affected by average annual milk yield, which we intend to increase by continuing to improve the animal welfare of our cows and operational efficiencies. The growth of our herd of dairy cows is affected by the availability of feed at commercially acceptable prices. As part of our strategic cooperation agreement with Shengmu Forage, our primary supplier of organic forage, Shengmu Forage, has agreed to supply organic forage to us on an exclusive basis, and plans to develop at least approximately 60,000, 65,000, and 65,000 mu of additional growing fields of organic forage in 2014, 2015 and 2016, respectively, to support the growth of our cow herd. See "Business — Suppliers and Procurement — Organic Feed."

- *Production of liquid milk products.* The production volume of our organic liquid milk products significantly depends on our processing capacity. We currently have three production lines in our organic liquid milk processing facility with a maximum daily processing capacity of 330 tonnes of organic liquid milk. We plan to increase our daily liquid milk processing capacity to 1,150 tonnes, including 380 tonnes of yogurt and 440 tonnes of other liquid milk products in addition to our current 330-tonne capacity, by the end of 2016. Expansion of processing capacity is capital intensive. We currently plan to allocate an aggregate of RMB360 million from 2014 to 2016 towards expansion of our processing capacity. See "Business — Business Strategy."

- *Average selling price.* The price of milk products is market driven. Currently there is a significant shortage in the supply of raw milk, particularly organic raw milk, in China, according to the F&S Report. Market demand for organic milk products has increased continually, driven by a combination of the growing concern for food safety and rising disposable income in China. The growth of organic milk supply, however, has significantly lagged the growth of demand, due to a combination of factors such as an often long and stringent organic product certification process and relatively large capital expenditures required for establishing large scale organic dairy farms. In addition, the average selling price of our organic milk products is affected by the dynamics between our pricing power and our efforts to increase market penetration through more flexible pricing policies. Our pricing power depends on our ability to maintain and improve the recognition of our "Shengmu 圣牧" brand (which we introduced only recently in June 2012) and educate consumers on the benefits of our "grass-to-glass" organic milk products.

- *Distribution network.* We began building our distribution network of liquid milk products in 2011 and generating revenue from liquid milk products in 2012. In 2013, 26.5% of our revenue was derived from sales of liquid milk products. We plan to focus on increasing sales of liquid milk products going forward and expanding our distribution network is a key component of our plan. As of December 31, 2012 and 2013, our distribution network had 108 and 316 distributors, respectively, which we plan to increase to over 400 by the end of 2014. Furthermore, our distribution network currently reaches mostly tier one and tier two cities, and we will seek to penetrate further into tier three and tier four cities. We intend to continue to focus on expanding sales channels such as supermarket chains, department stores, and convenience store chains. The level of success we experience in implementing these expansion strategies will significantly affect our revenue growth.

- *Product mix.* Product mix may affect our revenue, gross and net margins. In 2013, sales of premium non-organic raw milk and organic milk products, including organic raw milk and liquid milk products, constituted 42.7% and 57.3% of our total revenue, respectively. Sales of raw milk, including premium non-organic raw milk and organic raw milk, and liquid milk products constituted 73.5% and 26.5% of our total revenue, respectively. We expect that our future revenue growth will primarily be driven by increases in sales of organic raw milk and liquid milk products. In 2013, after elimination of internal profit from inter-segment sales, our gross margin of liquid milk products was 54.0%, as compared to 43.0% for organic raw milk and 35.9% for premium non-organic raw milk. The gross margin of our liquid milk products has been increasing as a result of the increase in our production scale. We expect our gross margin of liquid milk products to increase further as our production scale continues to increase. In addition, we expect sales of liquid milk products to increase as a percentage of our total sales. Both of these trends would positively impact our overall gross margin. On the other hand, our selling and distribution expenses have also increased primarily due to our increased sales of liquid milk products (particularly expenses to promote our "Shengmu 圣牧" brand and our products), representing 1.6%, 3.3% and 6.3% of our total revenue in 2011, 2012 and 2013, respectively. In terms of our product mix, we plan to offer yogurt in the third quarter of 2014 and develop and market additional new liquid milk products in the longer term. New products will generate additional revenue, but the profit margins of new products will likely be relatively low when we first market them, and increase if sales of these products become successful.

- *Cost of sales.* Feed is the largest component of our cost of sales, representing 78.4%, 76.3% and 78.4% of the total cost of sales for our dairy farming business in 2011, 2012 and 2013, respectively. Our feed primarily consists of forages and concentrated feed. Currently, we source our organic forages and principal raw materials (in terms of volume) for concentrated feed for our organic cows substantially from Shengmu Forage, with which we have an exclusive supply arrangement. The prices of these organic forages and principal raw materials are determined with reference to market price. See "Continuing Connected Transactions — Non-Exempt Continuing Connected Transactions — Continuing Connected Transactions with Shengmu Forage" for more details. Historically, these prices have not fluctuated significantly. Shengmu Forage has agreed to plant and supply sufficient organic forages to us to support our future expansion plans. But if Shengmu Forage fails to supply sufficient organic forages to us, we will have to purchase from third parties which may be more expensive or even to develop our own forage growing business as supply of organic forages is limited in China. Our feeds for non-organic dairy cows are purchased from third parties. Compared to organic feeds, non-organic feeds are more widely available on the market, and market prices have historically not fluctuated significantly. Any significant change in feed price will have a significant impact on our cost of sales and profit margins. In addition, we will continuously improve our feed formulae for our dairy cows to receive better nutrition which may lead to an increase in our average feed costs.

- *Availability of capital.* A majority of our dairy farms are designed to house 2,500 to 4,500 dairy cows, which cost approximately RMB50 million to RMB90 million to purchase based on the current market prices of domestic and imported dairy cows in China. A dairy farm requires additional investments of approximately RMB30 million to RMB55 million for construction and purchase of equipment and approximately six to eight months between commencement and completion of construction. Therefore, dairy farming is capital intensive and the growth of our herd size and hence production volume will depend on availability and cost of funding.

- *Change in fair value of biological assets*. Our results of operations are affected by changes in fair value less cost to sell of biological assets in respect of our dairy cows. We are required under IFRS to recognize such changes under "Gain/(loss) arising from changes in fair value less cost to sell of biological assets." "Gain/(loss) arising from changes in fair value less costs to sell of biological assets" represents fair value changes on our dairy cows due to the changes in physical attributes and market prices of and discounted future cash flow to be generated by those cows. In general, when a heifer becomes a milkable cow, its value increases as the discounted cash flow from milking is higher than the selling price of heifer. Further, when a milkable cow is culled and sold, its value decreases. During the Track Record Period, our biological assets were revalued at each reporting date. We recorded net gains arising from changes in fair value less costs to sell of biological assets totaling RMB117.1 million, RMB4.4 million and RMB9.5 million in 2011, 2012 and 2013, respectively. The fair value of the heifers and calves is determined with reference to their market prices and breeding costs, while the fair value of milkable cows represents the present value of expected net cash flows from such milkable cows discounted at a current market rate. In applying these valuation methods, our independent qualified professional valuer has relied on a number of assumptions related to, among other things, raw milk prices, milk yield, culling rates, feed costs and discount rates. Therefore, the fair value of our dairy cows could be affected by, among other things, the accuracy of these assumptions. Any changes in the estimates may affect the fair value of the dairy cows significantly. Upward adjustments do not generate any cash inflow for our operations. The independent qualified professional valuer and our management review the assumptions and estimates periodically to identify any significant changes in fair value of dairy cows. We expect that our results will continue to be affected by changes in the fair value of our cow herd. For more information about the valuation methods applied in valuing our dairy cows, see Note 18 of the Accountants' Report included as Appendix I to this [REDACTED].

CRITICAL ACCOUNTING POLICIES AND ESTIMATES

We have identified certain accounting policies that are significant to the preparation of our financial statements. Our significant accounting policies, which are important for an understanding of our financial condition and results of operations are set forth in details in Note 3 to the Accountants' Report included in Appendix I to this [REDACTED]. Some of our accounting policies involve subjective assumptions and estimates, as well as complex judgment relating to accounting items. In each case, the determination of these items requires management judgment based on information and financial data that may change in future periods. When reviewing our financial statements, you should consider (i) our selection of critical accounting policies; (ii) the judgment and other uncertainties affecting the application of such policies; and (iii) the sensitivity of reported results to changes in conditions and assumptions. We set forth below the accounting policies that we believe involve the most significant estimates and judgment used in the preparation of our financial statements.

Withholding Taxes Arising From the Distribution of Dividends

Our determination as to whether to accrue for withholding taxes arising from the distributions of dividends from certain subsidiaries according to the relevant tax jurisdictions is subject to judgment on the timing of the payment of the dividends or the amount of profits to be retained by the relevant subsidiaries. During the Track Record Period, we did not incur any deferred tax liabilities arising thereon.

Fair Value of Dairy Cows

Our dairy cows are valued at fair value less costs to sell. The fair value of dairy cows is determined based on either the market-determined prices as of the end of 2011, 2012 and 2013 adjusted with reference to the species, age, growing condition, cost incurred and expected yield of the milk to reflect differences in characteristic and/or stages of growth of dairy cows; or the present value of expected net cash flows from the dairy cows discounted at a current market-determined rate, when market-determined prices are unavailable. Any changes in the estimates may affect the fair value of the dairy cows significantly. The independent qualified professional valuer and our management review the assumptions and estimates periodically to identify any significant changes in fair value of dairy cows. Further details are given in note 18 to the Accountants' report.

Impairment of Receivables

We assess doubtful accounts for estimated losses resulting from the inability of the debtors to make the required payments. We base the estimates on the assessment of recoverability of individual receivable balance, customer credit-worthiness, and historical write-off experience. If the financial condition of the debtors were to deteriorate, actual write-offs would be higher than estimated.

Impairment of Non-financial Assets (Other than Goodwill)

We assess whether there are any indicators of impairment for all non-financial assets at the end of each reporting period. Indefinite life intangible assets are tested for impairment annually and at other times when such an impairment indicator exists. Other non-financial assets are tested for impairment when there are indicators that the carrying amounts may not be recoverable. An impairment exists when the carrying value of an asset or a cash-generating unit exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The calculation of the fair value less costs to sell is based on available data from binding sales transactions in an arm’s length transaction of similar assets or observable market prices less incremental costs for disposing of the asset. When value in use calculations are undertaken, management must estimate the expected future cash flows from the asset or cash-generating unit and choose a suitable discount rate in order to calculate the present value of those cash flows.

Depreciation

Property, plant and equipment are depreciated on a straight-line basis over the estimated useful lives of the assets, after taking into account the estimated residual values. We review the estimated useful lives and residual values of the assets regularly in order to determine the amount of depreciation expense to be recorded during any reporting period. The determination of the useful lives and residual values are based on the historical experience with similar assets and taking into account anticipated technological changes. The depreciation expense for future periods is adjusted if there are significant changes from previous estimates.

PRINCIPAL STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME COMPONENTS

The following table sets forth a summary of our combined results of operations for the period indicated. Our historical results presented below are not necessarily indicative of the results that may be expected for any future period.

	For the year ended December 31,					
	2011		2012		2013	
	Amount	% of revenue	Amount	% of revenue	Amount	% of revenue
	(RMB in thousands, except percentages)					
Revenue	389,417	100.0%	700,763	100.0%	1,143,709	100.0%
Cost of sales	(274,816)	(70.6)%	(466,704)	(66.6)%	(653,284)	(57.1)%
Gross profit.	114,601	29.4%	234,059	33.4%	490,425	42.9%
Gain/(loss) arising from changes in fair value less costs to sell of biological assets	117,139	30.1%	4,406	0.6%	9,484	0.8%
Other income and gains	10,854	2.8%	7,939	1.1%	6,868	0.6%
Selling and distribution expenses	(6,395)	(1.6)%	(22,869)	(3.3)%	(71,821)	(6.3)%
Administrative expenses	(7,845)	(2.0)%	(12,563)	(1.8)%	(25,436)	(2.2)%
Loss on disposal of a subsidiary	(444)	(0.1)%	—	—	—	—
Finance costs	(4,669)	(1.2)%	(12,389)	(1.8)%	(32,821)	(2.9)%
Share of profits and losses of associates	—	—	320	0.0%	(1,349)	(0.1)%
Profit before tax	223,241	57.3%	198,903	28.4%	375,350	32.8%
Income tax expense	—	—	—	—	(852)	(0.1)%
Profit and total comprehensive income for the year	223,241	57.3%	198,903	28.4%	374,498	32.7%
Attributable to:						
Owners of parent	223,268	57.3%	195,782	27.9%	327,309	28.6%
Non-controlling interests	(27)	0.0%	3,121	0.4%	47,189	4.1%
Other financial data:						
Adjusted EBITDA[(1)]/Adjusted EBITDA margin[(2)]	113,669	29.2%	218,458	31.2%	427,590	37.4%
Profit and total comprehensive income for the year before biological asset fair value adjustments[(3)]	106,102	27.2%	194,497	27.8%	365,014	31.9%

(1) Adjusted EBITDA refers to our profit and total comprehensive income for the year before income tax expense, finance costs, depreciation of items of property, plant and equipment, amortisation of prepaid land lease payments, amortisation

of other intangible assets and gain arising from changes in fair value less costs to sell of biological assets. Adjusted EBITDA is not a standard measure under IFRS. Adjusted EBITDA is a widely used financial indicator of a company's ability to service and incur debt. Adjusted EBITDA should not be considered in isolation or construed as an alternative to cash flows, net income or any other measure of financial performance or as an indicator of our operating performance, liquidity, profitability or cash flows generated by operating, investing or financing activities. In evaluating adjusted EBITDA, we believe that investors should consider, among other things, the components of adjusted EBITDA such as selling and distribution expenses and administrative expenses and the amount by which adjusted EBITDA exceeds capital expenditures and other charges. We have included adjusted EBITDA because we believe it is a useful supplement to cash flow data as a measure of our performance and our ability to generate cash flow from operations to cover debt service and taxes. Adjusted EBITDA presented herein may not be comparable to similarly titled measures presented by other companies. Investors should not compare our adjusted EBITDA to adjusted EBITDA presented by other companies because not all companies use the same definition.

The following table reconciles our profit and other comprehensive income for the year under IFRS to our definition of adjusted EBITDA for the period indicated:

	For the year ended December 31,		
	2011	2012	2013
	(RMB in thousands)		
Profit and total comprehensive income for the year	223,241	198,903	374,498
Gain arising from changes in fair value less costs to sell of biological assets	(117,139)	(4,406)	(9,484)
Income tax expense	—	—	852
Finance costs	4,669	12,389	32,821
Depreciation of items of property, plant and equipment	2,486	10,736	28,003
Amortisation of prepaid land lease payments	—	35	71
Amortisation of other intangible assets	412	801	829
Adjusted EBITDA	113,669	218,458	427,590

(2) Adjusted EBITDA margin is calculated by dividing adjusted EBITDA by revenue.

(3) Represents profit and total comprehensive income for the year minus gain/(loss) arising from changes in the fair value less costs to sell of biological assets, which is not a standard measure under the IFRS.

Revenue

During the Track Record Period, our revenue was generated from two operating segments: (i) dairy farming business, under which we produce and sell raw milk, both organic and premium non-organic; and (ii) liquid milk business, under which we produce and sell liquid milk products under the "Shengmu 圣牧" brand. All of our liquid milk products are produced from organic raw milk supplied internally by our organic dairy farms. Our total revenue is presented after elimination of inter-segment sales.

The following table sets forth the components of our revenue by operating segments for the period indicated.

	Dairy farming business				Liquid milk business				
For the year ended December 31,	**Segment revenue**	**Inter-segment sales(1)**	**External sales**	**External sales as % of total revenue**	**Segment revenue**	**Inter-segment sales**	**External sales**	**External sales as % of total revenue**	**Total revenue (after elimination of inter-segment sales(1))**
	(RMB in thousands, except percentages)								
2011	389,417	—	389,417	100.0%	—	—	—	—	389,417
2012	682,179	15,345	666,834	95.2%	33,929	—	33,929	4.8%	700,763
2013	972,308	131,561	840,747	73.5%	302,962	—	302,962	26.5%	1,143,709

(1) Represents internally produced organic raw milk sold to our liquid milk business.

Our business began in the dairy farming business, and expanded into the liquid milk business in 2012. Our liquid milk business has grown rapidly since then, representing 26.5% of our total revenue in 2013. We expect revenue from our liquid milk business to increase both in absolute amounts and as a percentage of our total revenue for the foreseeable future.

Dairy farming business

The following table sets forth the sales amount, sales volume and average selling price per tonne of our raw milk for the period indicated.

	For the year ended December 31,								
	2011			2012			2013		
	Sales amount	Sales volume	Average selling price	Sales amount	Sales volume	Average selling price	Sales amount	Sales volume	Average selling price
	RMB	Tonnes	RMB/ tonne	RMB	Tonnes	RMB/ tonne	RMB	Tonnes	RMB/ tonne
	(in thousands except sales volume and average selling price)								
Organic raw milk									
External sales	82,774	21,484	3,853	168,096	33,397	5,033	352,918	68,518	5,151
Inter-segment sales[(1)]	—	—	—	15,345	2,708	5,667	131,561	23,813	5,525
Subtotal	82,774	21,484	3,853	183,441	36,105	5,081	484,479	92,331	5,247
Premium non-organic raw milk									
External sales	306,643	81,165	3,778	498,738	121,300	4,112	487,829	111,465	4,377
Total	389,417	102,649	3,794	682,179	157,405	4,334	972,308	203,796	4,771

(1) Represents internally produced organic raw milk sold to our liquid milk business.

Sales volume of both organic raw milk and premium non-organic raw milk increased significantly throughout the Track Record Period primarily due to increases in the number of our dairy cows and average annual milk yield. The number of dairy cows at our organic dairy farms increased from 8,982 as of December 31, 2011 to 30,621 as of December 31, 2013.

The average selling prices of both organic raw milk and premium non-organic raw milk also increased throughout most of the Track Record Period. Our selling prices of organic raw milk for inter-segment sales are set with reference to our selling prices for external sales.

Liquid milk business

The following table sets forth the sales amount, sales volume and average selling price per tonne of our liquid milk products for the period indicated.

	For the year ended December 31,		
	2011	**2012**	**2013**
Sales amount *(RMB in thousands)*	—	33,929	302,962
Sales volume *(Tonnes)*	—	2,246	20,715
Average selling price *(RMB/tonne)*	—	15,106	14,625

We began to offer organic whole-milk products in gift pack and environmentally friendly pack in June 2012 and further added organic low-fat milk and organic milk for children products in 2013. Sales volume of liquid milk products increased significantly during the Track Record Period due to our increased organic raw milk production volume, our continued efforts to expand our liquid milk business and increased market recognition of our "Shengmu 圣牧" brand. The average selling price of our liquid milk products decreased from 2012 to 2013 primarily due to a combination of (i) our efforts to incentivize distributors to drive sales and increase market penetration through more flexible pricing policies; and (ii) changes in product mix, as we introduced organic milk for children and sales of environmentally friendly packed whole milk as a percentage of our total sales increased significantly in 2013, both of which had lower selling prices as a result of lower packaging cost.

Cost of Sales and Gross Margin

The following table sets forth our gross profit and gross margin for each of our segments both before and after the elimination of internal profit from inter-segment sales for the period indicated. We use a portion of our organic raw milk to produce our liquid milk products. Such internal supply of organic raw milk is recorded as revenue under our dairy farming business and cost of sales under our liquid milk business with a reference to the price of organic raw milk sold to our external customers in the same period. These inter-segment sales were eliminated during consolidation of our results of operations.

	For the year ended December 31,								
	2011			2012			2013		
	Cost of sales	Gross profit	Gross margin	Cost of sales	Gross profit	Gross margin	Cost of sales	Gross profit	Gross margin
	Amount	Amount	%	Amount	Amount	%	Amount	Amount	%
	(RMB in thousands, except percentages)								
Dairy farming business									
Organic raw milk									
Before elimination	64,829	17,945	21.7%	125,144	58,297	31.8%	271,176	213,303	44.0%
After elimination(1)	64,829	17,945	21.7%	115,758	52,338	31.1%	201,237	151,681	43.0%
Premium non-organic raw milk	209,987	96,656	31.5%	331,712	167,026	33.5%	312,670	175,160	35.9%
Subtotal:									
Before elimination	274,816	114,601	29.4%	456,856	225,323	33.0%	583,846	388,462	40.0%
After elimination(1)	274,816	114,601	29.4%	447,470	219,364	32.9%	513,907	326,841	38.9%
Liquid milk business									
Before elimination	—	—	N/A	25,193	8,736	25.7%	200,998	101,964	33.7%
After elimination(2)	—	—	N/A	19,235	14,694	43.3%	139,377	163,585	54.0%

(1) Represents gross profit after elimination of internal profit attributable to inter-segment sales of organic raw milk. Such internal profit is calculated as the difference of (i) the inter-segment sales of organic raw milk used in our liquid milk business and (ii) the production costs for such organic raw milk calculated as the product of (a) total cost of sales of organic raw milk and (b) the volume of organic raw milk sold to our liquid milk business divided by total sales volume of organic raw milk.

(2) Represents gross profit after adding back the internal profit attributable to inter-segment sales of organic raw milk. Such internal profit is calculated as the difference of (i) the inter-segment sales of organic raw milk used in this segment and (ii) the production costs for such organic raw milk calculated using the formula in note (1) above.

Dairy farming business

The following table sets forth the major components of our cost of sales (before elimination of related costs of inter-segment sales) both in absolute terms and as a percentage of our cost of sales for the period indicated.

	For the year ended December 31,					
	2011		2012		2013	
	Amount	% of total	Amount	% of total	Amount	% of total
	(RMB in thousands, except percentages)					
Feeds	215,533	78.4%	348,606	76.3%	457,817	78.4%
Salary, welfare and social insurance	21,707	7.9%	34,579	7.6%	49,321	8.4%
Others[1]	37,576	13.7%	73,671	16.1%	76,708	13.2%
Total	274,816	100.0%	456,856	100.0%	583,846	100.0%

(1) Consists primarily of veterinary cost, frozen semen, depreciation, utilities, repairs and maintenance, rental expenses and consumables.

Feed costs for milkable cows account for the majority of costs for our dairy farming business. In 2011, 2012 and 2013, feed costs accounted for 78.4%, 76.3% and 78.4%, respectively, of the cost of sales of our dairy farming business. We feed our cows forages including corn silage, alfalfa and guinea grass, and concentrated feed.

The cost of sales related to inter-segment sales of organic raw milk was nil, RMB9.4 million and RMB69.9 million in 2011, 2012 and 2013, respectively, which accounted for nil, 2.1% and 12.0% of our cost of sales.

The following table sets forth the gross profit and gross margin of our organic raw milk by product type both before and after elimination of internal profit from inter-segment sales and premium non-organic raw milk for the period indicated.

	For the year ended December 31,								
	2011			2012			2013		
	Cost of sales	Gross profit	Gross margin	Cost of sales	Gross profit	Gross margin	Cost of sales	Gross profit	Gross margin
	Amount	Amount	%	Amount	Amount	%	Amount	Amount	%
	(RMB in thousands, except percentages)								
Organic raw milk									
Before elimination	64,829	17,945	21.7%	125,144	58,297	31.8%	271,176	213,303	44.0%
After elimination[1]	64,829	17,945	21.7%	115,758	52,338	31.1%	201,237	151,681	43.0%
Premium non-organic raw milk	209,987	96,656	31.5%	331,712	167,026	33.5%	312,670	175,160	35.9%

(1) Represents gross profit after elimination of internal profit attributable to inter-segment sales of organic raw milk. Such internal profit is calculated as the difference of (i) the inter-segment sales of organic raw milk used in our liquid milk business and (ii) the production costs for such organic raw milk calculated as the product of (a) total cost of sales of organic raw milk and (b) the volume of organic raw milk sold to our liquid milk business divided by total sales volume of organic raw milk.

Gross margin of our organic raw milk business has increased significantly during the Track Record Period primarily due to the continuing increase in the average selling price of organic raw milk. The increase in gross margin of our premium non-organic raw milk business was primarily due to the continuing increase in the average selling price of premium non-organic raw milk.

Liquid milk business

Cost of sales of our liquid milk products primarily consists of costs of procurement of raw milk, costs of packaging and auxiliary materials, salary and welfare of employees directly involved in production activities and other costs.

The following table sets forth the major components of our cost of sales both in absolute terms and as a percentage of our cost of sales for the period indicated.

	For the year ended December 31,					
	2011		2012		2013	
	Amount	% of total	Amount	% of total	Amount	% of total
	(RMB in thousands, except percentages)					
Raw milk[1]	—	—	12,846	51.0%	115,951	57.7%
Packages	—	—	7,383	29.3%	62,559	31.1%
Salary, welfare and social insurance	—	—	1,373	5.4%	3,836	1.9%
Others[2]	—	—	3,591	14.3%	18,652	9.3%
Total	—	—	25,193	100.0%	200,998	100.0%

(1) Before elimination of internal profit generated from inter-segment sales to liquid milk business.

(2) Consists primarily of other raw materials, depreciation, utilities, repairs and maintenance, consumables and service fee.

We began sale of our liquid milk products in June 2012. Cost for internal procurement of organic raw milk and cost of packaging materials historically represented a substantial majority of our cost of sales in the liquid milk business.

The gross margin of our liquid milk business increased significantly in 2013 from 2012, primarily due to an increase in our production scale and efficiency.

Gain Arising from Changes in Fair Value Less Costs to Sell of Biological Assets

Gain/(loss) arising from changes in fair value less costs to sell of biological assets represents fair value changes in our dairy cows, due to the changes in physical attributes and market prices of and discounted future cash flow to be generated by those cows. In general, when a heifer becomes a milkable cow, its value increases as the discounted cash flow from milking is higher than the selling price of heifers. Further, when a milkable cow is culled and sold, its value decreases. During the Track Record Period, the biological assets were revalued at each reporting date.

During the Track Record Period, the valuer for dairy cows has adopted the following principal valuation assumptions:

- *Calves and heifers*. The fair value of the heifers purchased within six month prior to each reporting date is determined with reference to the actual purchase price, with adjustment by adding the feed costs from the purchase date to the reporting date. For the remaining heifers, the fair value of 14-month-old heifers is determined by referring to the market price of the actively traded market and adjusted by the potential milk yield. The fair value of heifers older than 14 months is determined by adding the breeding costs required to raise the heifers from 14 months of age to their respective ages plus the estimated margins that would be required by a raiser. The fair value of the calves and heifers younger than 14 months of age and the fair value of the calves is determined by subtracting the breeding costs required to raise the calves or heifers from their respective ages to 14 months of age and the estimated margins required by a raiser.

- *Milkable cows*. The fair value of milkable cows is determined using the multi-period excess earnings method, which is based on the discounted future cash flows to be generated by such milkable cows.

We recorded net gains arising from changes in fair value less costs to sell of biological assets of RMB117.1 million, RMB4.4 million and RMB9.5 million in 2011, 2012 and 2013, respectively. See "— Results of Operations" for analyses on the fluctuation of the gains arising from changes in fair value less costs to sell of biological assets.

When disposing of our dairy cows, we write off the carrying amount of the dairy cows from our biological assets, and the difference between the carrying amount of the dairy cows disposed and the proceeds from the disposal is recorded as change in fair value less costs to sell of our biological assets. The cash proceeds are recorded under investment cash inflow. The cash proceeds from disposal of biological assets amounted to RMB22.9 million, RMB39.0 million and RMB159.6 million in 2011, 2012 and 2013, respectively.

For more information, see "— Discussion of Certain Statements of Financial Position Items — Biological Assets."

Other Income and Gains

Other income and gains include government grants, bank interest income and other income. Government grants, which totaled RMB6.3 million, RMB3.7 million and RMB5.5 million in 2011, 2012 and 2013, respectively, are unconditional grants and subsidies and are a part of PRC government's policy to support China's dairy farming business.

Selling and Distribution Expenses

The following table sets forth our selling and distribution expenses by business segment for the period indicated.

	For the year ended December 31,								
	2011			2012			2013		
	Amount	% of total revenue	% of segment revenue	Amount	% of total revenue	% of segment revenue	Amount	% of total revenue	% of segment revenue
	(RMB in thousands, except percentages)								
Dairy farming business	6,183	1.6%	1.6%	9,007	1.3%	1.3%	11,157	1.0%	1.1%
Liquid milk business	212	—	N/A	13,862	2.0%	40.9%	60,664	5.3%	20.0%
Total	6,395	1.6%	N/A	22,869	3.3%	N/A	71,821	6.3%	N/A

Dairy farming business

Substantially all of the selling and distribution expenses of our dairy farming business consisted of transportation and logistics expenses associated with the delivery of raw milk to our customers.

Liquid milk business

The following table sets forth the components of the selling and distribution expenses of our liquid milk business as a percentage of segment revenue for the period indicated.

	For the year ended December 31,					
	2011		2012		2013	
	Amount	% of segment revenue	Amount	% of segment revenue	Amount	% of segment revenue
	(RMB in thousands, except percentages)					
Promotion and advertisement	212	N/A	5,213	15.4%	20,625	6.8%
Logistics	—	—	1,782	5.3%	18,752	6.2%
Salary and welfare	—	—	3,847	11.3%	11,811	3.9%
Consumables, travel and others	—	—	3,020	8.9%	9,476	3.1%
Total	212	N/A	13,862	40.9%	60,664	20.0%

Selling and distribution expenses of our liquid milk business increased significantly in 2013 primarily due to the significant increase in our sales of liquid milk products and expansion of distribution network. Promotion and advertisement expenses increased significantly in 2013 primarily due to our advertising campaign launched at China Central Television, or CCTV, to promote our products. Logistics expenses increased in 2013 primarily due to our increased sales volume.

Administrative Expenses

Our administrative expenses primarily consist of salary and welfare of management and administrative employees. During the Track Record Period, administrative expenses as a percentage of revenue were 2.0%, 1.8% and 2.2% in 2011, 2012 and 2013, respectively.

Loss on Deemed Disposal of a Subsidiary

We recorded a loss on deemed disposal of a subsidiary of RMB0.4 million in 2011 primarily due to the discontinued consolidation of Shengmu Forage as a result of investments by third party investors, and the resulting loss arising from the deemed disposal of Shengmu Forage. We did not record any loss on disposal of a subsidiary in 2012 and 2013.

Finance Costs

Our finance costs represent interest expenses on bank borrowings less interest expenses capitalized into biological assets. Our net finance costs are primarily affected by the outstanding amount of borrowings and applicable interest rates.

Share of Profits and Losses of Associates

Share of profits and losses of associates represent our interest in Shanghai Saihan and Beijing Shengmu, which are distributors of our liquid milk products in these regions, and in which we have 41.67% and 30% shareholding, respectively, as well as Shengmu Forage in which we have an 8.6% shareholding. Shengmu Forage is accounted for as an associate of our Group because we control more than 20% effective voting power of Shengmu Forage due to the acting-in-concert arrangement among Shengmu Holding and two of our Ultimate Controlling Shareholders. For details, please refer to "Relationship with Controlling Shareholders — Major Retained Businesses of Our Ultimate Controlling Shareholders — Shengmu Forage."

We recorded share of profits and losses of associates of nil, profits of RMB0.3 million and losses of RMB1.3 million in 2011, 2012 and 2013, respectively. The profits in 2012 were primarily due to the profits generated by Shengmu Forage from which we purchased our organic forages. The losses in 2013 were primarily due to the losses of Shanghai Saihan and Beijing Shengmu, which were in the early stages of developing a market for our liquid milk products that we introduced in June 2012.

Income Tax Expense

Under the current laws of the Cayman Islands and the British Virgin Islands, we are not subject to income tax or capital gains tax in the Cayman Islands and the British Virgin Islands. Additionally, dividend payments made by us are not subject to withholding tax in the Cayman Islands and the British Virgin Islands.

No provision has been made for Hong Kong profits as we did not earn income that is subject to Hong Kong profits tax in 2011, 2012 and 2013. There is no withholding tax on the dividends distributed from our Hong Kong subsidiary.

Our subsidiaries in the PRC are generally subject to PRC Enterprise Income Tax rate of 25% for each of the years ended December 31, 2011, 2012 and 2013. According to the Enterprise Income Tax Law of the PRC (the "EIT Law"), our income arising from agricultural activities, such as dairy farming and processing of primary agricultural products, is exempt from income tax. Under the PRC tax laws and regulations, there is no statutory time limit for us to enjoy such tax exemption as long as our relevant PRC subsidiaries complete filings with the relevant competent tax authorities as required.

In accordance with "The notice of tax policies relating to the implementation of the Western China Development Strategy" (財政部、海關總署、國家稅務總局《關於深入實施西部大開發戰略有關稅收政策問題的通知》(財稅[2011]58號), our taxable income arising from processing of non-primary agricultural products is subject to preferential tax rate of 15% from 2013 to 2020.

Our income tax expenses were nil, nil and RMB0.9 million in 2011, 2012 and 2013, respectively, and our effective income tax rate was nil, nil and 0.2%. As of the Latest Practicable Date and during the Track Record Period, we had fulfilled all our tax obligations and did not have any unresolved tax disputes with the applicable tax authorities.

Profit For the Year

As a result of the foregoing, our profit for the year was RMB223.2 million, RMB198.9 million and RMB374.5 million in 2011, 2012 and 2013, respectively. By comparison, our profit for the year before biological assets fair value adjustments was RMB106.1 million, RMB194.5 million and RMB365.0 million during the same periods.

Profit Attributable to Non-controlling Interest

We recorded profit/(loss) attributable to non-controlling interest of (RMB27,000), RMB3.1 million and RMB47.2 million in 2011, 2012 and 2013, respectively. Non-controlling interest during the Track Record Period primarily represented the minority interests in our dairy farms held by dairy farmers with whom we work in managing our farms.

RESULTS OF OPERATIONS

Year Ended December 31, 2012 Compared to Year Ended December 31, 2013

Revenue

Our revenue increased by 63.2% from RMB700.8 million in 2012 to RMB1,143.7 million in 2013, reflecting (i) a 42.5% increase in revenue from our dairy farming business; and (ii) a 793.8% increase in revenue from our liquid milk business.

Dairy farming business

Revenue from our dairy farming business increased by 42.5% from RMB682.2 million to RMB972.3 million, primarily reflecting the following factors:

- *Organic raw milk*. Total revenue from sales of organic raw milk (before elimination of inter-segment sales) increased from RMB183.4 million to RMB484.5 million, consisting of (i) an increase in external sales by 109.9% from RMB168.1 million to RMB352.9 million; and (ii) an increase in inter-segment sales to our liquid milk business from RMB15.3 million in 2012 to RMB131.6 million. From 2012 to 2013, as a result of our continuing investment in organic dairy farms, the number of our organic dairy cows increased from

14,111 as of December 31, 2012 to 30,621 as of December 31, 2013. As a result, total sales volume of organic raw milk increased from 36,105 tonnes in 2012 to 92,331 tonnes in 2013. In addition, the average selling price of our organic raw milk increased from RMB5,081 per tonne to RMB5,247 per tonne due to continuing strong demand.

- *Premium non-organic raw milk*. Revenue of premium non-organic raw milk remained relatively stable at RMB498.7 million and RMB487.8 million in 2012 and 2013, respectively, reflecting an increase in the average selling price from RMB4,112 per tonne to RMB4,377 per tonne as demand continues to rise, offset by a decrease in our external sales volume from 121,300 tonnes to 111,465 tonnes reflecting our strategy to shift focus to organic raw milk and liquid milk businesses.

Liquid milk business

We began selling our liquid milk products in June 2012. Revenue from sales of our liquid milk products increased by 793.8% from RMB33.9 million in 2012 to RMB303.0 million in 2013 as our sales volume increased from 2,246 tonnes in 2012 to 20,715 tonnes in 2013. The substantial increase primarily reflected a combination of (i) the first full-year sales of our liquid milk products after commencing sales in June 2012; (ii) continuing expansion of our distribution network, which totaled 108 and 316 distributors as of December 31, 2012 and 2013, respectively; (iii) continued rising demand for organic milk products in China generally as a result of factors such as consumers' continued focus on food safety and a general rise in disposable income; (iv) increased recognition of our brand as a result of increased advertising and promotional efforts such as those on CCTV and Air China flights. The increase in sales volume was partially offset by a decrease in the average selling price of our liquid milk products by 3.2% from RMB15,106 per tonne in 2012 to RMB14,625 per tonne in 2013 primarily due to a combination of (i) our efforts to incentivize distributors to drive sales and increase market penetration through more flexible pricing policies; and (ii) changes in our product mix as we introduced environmentally-friendly packaged whole milk product series and children's series which have lower selling prices as a result of lower packaging cost.

Cost of sales

Our cost of sales increased by 40.0% from RMB466.7 million in 2012 to RMB653.3 million in 2013, primarily as a result of a substantial increase in the production and sales volume of both raw milk from our dairy farming business and liquid milk products.

- *Dairy farming business*. Cost of sales of our dairy farming business increased by 27.8% from RMB456.9 million in 2012 to RMB583.8 million in 2013. Cost of sales of our dairy farming business (after elimination of related cost of inter-segment sales) increased by 14.8% from RMB447.5 million in 2012 to RMB513.9 million in 2013. The increase was primarily due to an increase in the production volume of raw milk. Feed costs remained the major component for the costs of sales of our raw milk.

- *Liquid milk business.* Cost of sales of our liquid milk products increased by 697.6% from RMB25.2 million in 2012 to RMB201.0 million in 2013. Cost of sales of our liquid milk products (after elimination of internal profit from inter-segment sales) increased by 626.0% from RMB19.2 million in 2012 to RMB139.4 million in 2013, primarily as a result of a significant increase in our production volume. The cost of internal procurement of organic raw milk remained the major component for the costs of sales of our liquid milk products.

Gross profit and gross margin

As a result of the foregoing, our gross profit increased by 109.5% from RMB234.1 million in 2012 to RMB490.4 million in 2013, and our gross margin increased from 33.4% in 2012 to 42.9% in 2013.

- *Dairy farming business.* The gross profit of our dairy farming business increased from RMB225.3 million in 2012 to RMB388.5 million in 2013. By comparison, after elimination of internal profit from inter-segment sales, the gross profit of our dairy farming business increased from RMB219.4 million in 2012 to RMB326.8 million in 2013. Gross margin of our dairy farming business increased from 33.0% in 2012 to 40.0% in 2013, or 32.9% in 2012 to 38.9% in 2013 (after elimination of internal profit from inter-segment sales), reflecting:

  (i) an increase in gross margin from 31.8% to 44.0% for our organic raw milk, or 31.1% to 43.0% (after elimination of internal profit from inter-segment sales) primarily due to (a) an increase in average milk yield (b) increased production scale and efficiency, and (c) and our increased average selling price as discussed above under "— Revenue;" and

  (ii) an increase in gross margin from 33.5% to 35.9% for our premium non-organic raw milk primarily due to our increased average selling price as discussed above under "— Revenue."

- *Liquid milk business.* The gross profit of our liquid milk business increased from RMB8.7 million in 2012 to RMB102.0 million in 2013, and the gross margin of our liquid milk business was 25.7% and 33.7%. By comparison, after elimination of internal profit from inter-segment sales, the gross profit of our liquid milk business increased from RMB14.7 million in 2012 to RMB163.6 million in 2013, and the gross margin of our liquid milk business was 43.3% and 54.0%. The increase in gross margin was primarily due to an increase in our production scale and efficiency. The increase in gross margin was partially offset by a decrease in the average selling price of our liquid milk products as discussed above under "— Revenue."

Gain arising from changes in fair value less costs to sell of biological assets

We recorded a gain arising from changes in fair value less costs to sell of biological assets of RMB4.4 million in 2012, as compared to a gain arising from changes in fair value less costs to sell of biological assets of RMB9.5 million in 2013. The higher gain in 2013 compared to 2012 was primarily due to an increase in the average selling price of non-organic raw milk, an increase in average milk yield, an increase in the number of our milkable cows, and change in the composition of cow herd. The gain in 2012 was primarily due to increases in the number of our milkable cows, milk yield and market price of raw milk.

Other income and gains

Our other income and gains decreased by 12.7% from RMB7.9 million in 2012 to RMB6.9 million in 2013, primarily due to a decrease in bank interest income. The decrease in bank interest income was primarily due to a decrease in the average balance of bank deposits as a result of increasing expenditures in dairy farm construction in 2013.

Selling and distribution expenses

Selling and distribution expenses increased by 213.5% from RMB22.9 million in 2012 to RMB71.8 million in 2013, and as a percentage of revenue, increased from 3.3% in 2012 to 6.3% in 2013. Selling and distribution expenses of our dairy farming business increased by 24.4% from RMB9.0 million in 2012 to RMB11.2 million in 2013, primarily due to increased transportation and logistics expenses as a result of the increase in sales volume of our organic raw milk. Selling and distribution expenses of our liquid milk business increased significantly from RMB13.9 million in 2012 to RMB60.7 million in 2013, primarily due to (i) increased logistics services as our sales volume increased; (ii) increases in salary and welfare of our employees engaging in sales, marketing and distribution; and (iii) an increase in promotional and advertising expenses as we increased efforts and resources in promoting our "Shengmu 圣牧" brand and our liquid milk products, which we introduced in June 2012.

Administrative expenses

Our administrative expenses increased by 101.6% from RMB12.6 million in 2012 to RMB25.4 million in 2013, and as a percentage of revenue, increased from 1.8% in 2012 to 2.2% in 2013. The increase primarily reflected an increase in employee headcount as our operations expanded significantly and an increase in average employee compensation.

Finance costs

Our finance costs increased by 164.5% from RMB12.4 million in 2012 to RMB32.8 million in 2013 due to our increased interest expenses on bank loans, which in turn was due to an increase in the average balance of our bank loans to fund our continuing investment in the construction of dairy farms and purchase of dairy cows.

Share of profits and losses of associates

We recorded share of profits of associates of RMB0.3 million in 2012 and share of losses of associates of RMB1.3 million in 2013. The profits in 2012 were primarily due to the profits of our associate, Shengmu Forage. The share of losses of associate in 2013 was primarily due to the losses of our associates, Shanghai Saihan and Beijing Shengmu, which distributed our liquid milk products, and in which we owned 41.7% and 30.0% interest, respectively. These distributors incurred losses in 2013 because they were still in the early stages of developing a market for our liquid milk products, which we introduced in June 2012.

Income tax expense

Our income tax expense increased from nil in 2012 to RMB0.9 million in 2013, respectively, primarily as a result of commencement of sales of liquid milk products subject to income tax in 2013.

Profit for the year

As a result of the foregoing, our profit for the year increased by 88.3% from RMB198.9 million in 2012 to RMB374.5 million in 2013, and our profit margin increased from 28.4% in 2012 to 32.7% in 2013. By comparison, our profit for the year before biological asset fair value adjustments increased by 87.7% from RMB194.5 million in 2012 to RMB365.0 million in 2013, and our profit margin before biological asset fair value adjustments increased from 27.8% in 2012 to 31.9% in 2013.

Profit attributable to non-controlling interests

Profit attributable to non-controlling interests totaled RMB3.1 million in 2012 and RMB47.2 million in 2013. The increase was primarily due to an increase in the number of our non-wholly owned subsidiaries, primarily dairy farms, and business expansion of existing dairy farms.

Year Ended December 31, 2011 Compared to Year Ended December 31, 2012

Revenue

Our revenue increased by 80.0% from RMB389.4 million in 2011 to RMB700.8 million in 2012, reflecting (i) a 75.2% increase in revenue from our dairy farming business; and (ii) the launching of our liquid milk business.

Dairy farming business

Revenue from our dairy farming business increased by 75.2% from RMB389.4 million to RMB682.2 million, primarily reflecting the following factors:

- *Organic raw milk*. Total revenue from sales of organic raw milk (before elimination of inter-segment sales) increased from RMB82.8 million to RMB183.4 million, consisting of (i) a 103.0% increase in external sales from RMB82.8 million to RMB168.1 million; and (ii) an increase in internal sales to our liquid milk business from nil in 2011 to RMB15.3

million in 2012. From 2011 to 2012, as a result of our continuing investment in organic dairy farms, the number of our organic dairy cows increased from 8,982 as of December 31, 2011 to 14,111 as of December 31, 2012. As a result, total sales volume of organic raw milk increased from 21,484 tonnes in 2011 to 36,105 tonnes in 2012. The average selling price increased significantly from RMB3,853 per tonne in 2011 to RMB5,081 per tonne in 2012, primarily due to increased market acceptance of organic milk that contributed to higher selling prices of organic raw milk.

- *Premium non-organic raw milk*. Revenue of premium non-organic raw milk increased from RMB306.6 million in 2011 to RMB498.7 million in 2012, reflecting an increase in the average selling price from RMB3,778 per tonne to RMB4,112 per tonne as demand continued to rise.

Liquid milk business

We began selling liquid milk products in June 2012 and generated a total revenue of RMB33.9 million and a sales volume of 2,246 tonnes in 2012. Our liquid milk products were produced solely from the organic raw milk we produced internally.

Cost of sales

Our cost of sales increased by 69.8% from RMB274.8 million in 2011 to RMB466.7 million in 2012. The increase was primarily due to a substantial increase in the production and sales volume of our raw milk in our dairy farming business.

- *Dairy farming business*. Cost of sales of our dairy farming business increased by 66.2% from RMB274.8 million in 2011 to RMB456.9 million in 2012. By comparison, after elimination of related cost of inter-segment sales, cost of sales of our dairy farming business increased from RMB274.8 million in 2011 to RMB447.5 million in 2012. The increase was primarily due to an increase in our sales volume as a result of stronger market demand, which was met by an increase of our dairy cows. Feed costs remained the major component for the costs of sales of our raw milk.

- *Liquid milk business*. We recorded cost of sales of RMB25.2 million for sales of liquid milk products in 2012 which began in June 2012. By comparison, cost of sales of our liquid milk products (after elimination of internal profit from inter-segment sales) was RMB19.2 million in the same year. Cost of internal procurement of organic raw milk from our dairy farming business was the major component for the costs of sales of our liquid milk products.

Gross profit and gross margin

As a result of the foregoing, our gross profit increased significantly from RMB114.6 million in 2011 to RMB234.1 million in 2012.

- *Dairy farming business*. The gross profit of our dairy farming business increased by 96.6% from RMB114.6 million in 2011 to RMB225.3 million in 2012. By comparison, after elimination of internal profit from inter-segment sales, the gross profit of our dairy farming business increased by 91.4% from RMB114.6 million in 2011 to RMB219.4 million in 2012. Gross margin of our dairy farming business increased from 29.4% in 2011 to 33.0% in 2012, or 29.4% to 32.9% (after elimination of internal profit from inter-segment sales) reflecting (i) an increase in gross margin from 21.7% to 31.8%, or from 21.7% to 31.1% (after elimination of internal profit from inter-segment sales), for our organic raw milk business and an increase in gross margin from 31.5% to 33.5% for our premium non-organic raw milk business. The increase in gross margin for organic raw milk business was primarily due to the increase in average selling price as discussed under "— Revenue" above and our increased average annual milk yield.

- *Liquid milk business*. We began selling liquid milk products under the "Shengmu 圣牧" brand in June 2012. We recorded a gross profit of RMB8.7 million of our liquid milk business and our gross margin was 25.7%. By comparison, after elimination of internal profit from inter-segment sales, our gross profit of liquid milk business was RMB14.7 million, and our gross margin was 43.3%.

Gain arising from changes in fair value less costs to sell of biological assets

Our gain arising from changes in fair value less costs to sell of biological assets decreased significantly from RMB117.1 million in 2011 to RMB4.4 million in 2012. In 2010, we purchased our dairy cows at a lower market price in the aftermath of the melamine incidents in China in 2008, which resulted in a relatively higher gain from the changes in fair value of our dairy cows in 2011 compared to 2012.

Other income and gains

Our other income and gains decreased by 27.5% from RMB10.9 million in 2011 to RMB7.9 million in 2012, primarily due to a decrease in the government grants received by us and bank interest income.

Selling and distribution expenses

Selling and distribution expenses increased by 257.8% from RMB6.4 million in 2011 to RMB22.9 million in 2012, and as a percentage of revenue, increased from 1.6% in 2011 to 3.3% in 2012. Selling and distribution expenses of our dairy farming business increased by 45.2% from RMB6.2 million in 2011 to RMB9.0 million in 2012, primarily due to increased transportation and logistics expenses as a result of increased sales volume of raw milk. Selling and distribution expenses of our liquid milk business increased significantly from RMB0.2 million to RMB13.9 million, primarily due to (i) increased logistics services as our sales volume increased; (ii) increases in salary and welfare of our employees engaging in sales, marketing and distribution; and (iii) an increase in promotional and advertisement expenses as we increased efforts and resources in promoting our "Shengmu 圣牧" brand and our liquid milk products, which we introduced in June 2012.

Administrative expenses

Our administrative expenses increased by 61.5% from RMB7.8 million in 2011 to RMB12.6 million in 2012, and as a percentage of revenue, decreased from 2.0% in 2011 to 1.8% in 2012. The increase in absolute amounts primarily reflected an increase in our employee headcount as our operations expanded significantly and an increase in average employee compensation.

Loss on deemed disposal of a subsidiary

We recorded a loss on deemed disposal of a subsidiary of RMB0.4 million in 2011 primarily due to the discontinued consolidation of Shengmu Forage as it received investments by third party investors, and as a result of which, we no longer consolidated the financial results of Shengmu Forage.

Finance costs

Our finance costs increased significantly from RMB4.7 million in 2011 to RMB12.4 million in 2012, primarily due to our increased interest expenses on bank loans, which in turn was due to an increase in the average balance of our bank loans to fund our continuing investment in the construction of dairy farms and purchase of dairy cows.

Share of profits and losses of associates

We did not record any share of profits and losses of associates in 2011 and recorded share of profits of associates of RMB0.3 million in 2012. The profits in 2012 was primarily due to the profits of our associate, Shengmu Forage, from which we purchased our organic forages.

Income tax expense

We did not have any income tax expense in 2011 and 2012. In 2011, profits from our dairy farming business were considered income arising from agricultural activities and were therefore exempt from income taxation under PRC tax laws and regulations. Our liquid milk products business did not have any taxable income in 2012.

Profit for the year

As a result of the foregoing, our profit for the year decreased by 10.9% from RMB223.2 million in 2011 to RMB198.9 million in 2012, and our profit margin decreased from 57.3% in 2011 to 28.4% in 2012. By comparison, our profit for the year before biological asset fair value adjustments increased by 83.3% from RMB106.1 million in 2011 to RMB194.5 million in 2012, and our profit margin before biological asset fair value adjustments increased from 27.2% in 2011 to 27.8% in 2012.

Profit attributable to non-controlling interests

We recorded profit/(loss) attributable to non-controlling interests of (RMB27,000) in 2011 and RMB3.1 million in 2012. The increase was primarily due to an increase in the number of our non-wholly owned subsidiaries, primarily our dairy farms, and business expansion of existing dairy farms.

DISCUSSION OF CERTAIN STATEMENTS OF FINANCIAL POSITION ITEMS

The following table sets forth our summary combined statement of financial position as of the date indicated. This information should be read together with our combined financial information included in Appendix I—"Accountants' Report" to this [REDACTED].

	As of December 31,		
	2011	2012	2013
	(RMB in thousands)		
Non-current assets			
Property, plant and equipment	194,875	450,249	922,764
Prepaid land lease payments	—	3,452	3,381
Other intangible assets	15,021	14,466	14,192
Investments in associates	14,756	17,576	17,727
Biological assets	713,826	1,029,541	1,510,160
Prepayments for property, plant and equipment and biological assets	14,101	26	9,043
Deferred income tax assets	—	—	187
Total non-current assets	952,579	1,515,310	2,477,454
Current assets			
Inventories	103,881	204,243	335,218
Trade and bill receivables	10,043	24,510	63,470
Prepayments, deposits and other receivables	15,893	30,030	94,377
Pledged deposits	29,224	12,797	15,030
Cash and cash equivalents	69,550	29,838	127,059
Total current assets	228,591	301,418	635,154
Current liabilities			
Trade and bills payables	83,963	132,151	191,037
Receipts in advance	15,473	17,527	82,481
Other payables and accruals	82,468	124,581	198,565
Interest-bearing bank borrowings	75,000	324,000	932,000
Tax payable	—	—	633

	As of December 31,		
	2011	2012	2013
	(RMB in thousands)		
Total current liabilities	256,904	598,259	1,404,716
Net current liabilities	(28,313)	(296,841)	(769,562)
Total assets less current liabilities	924,266	1,218,469	1,707,892
Non-current liabilities			
Interest-bearing bank borrowings	49,000	—	—
Total non-current liabilities	49,000	—	—
Net assets	875,266	1,218,469	1,707,892

Property, Plant and Equipment

Our property, plant and equipment primarily consist of buildings, machinery and equipment, office and other equipment, motor vehicles and construction in progress. We had property, plant and equipment in the amount of RMB194.9 million, RMB450.2 million and RMB922.8 million as of December 31, 2011, 2012 and 2013, respectively. The continued increase in our property, plant and equipment during the Track Record Period primarily reflected our continuing investment in dairy farms, which totaled 17, 21 and 25 as of December 31, 2011, 2012 and 2013, respectively, including four, seven and 13 organic dairy farms, respectively.

Prepaid Land Lease Payments

Our prepaid land lease payments represent prepaid operating lease payments for a parcel of land located in China and used primarily for liquid milk production purposes. We had prepaid land lease payments in the amount of nil, RMB3.5 million and RMB3.4 million as of December 31, 2011, 2012 and 2013, respectively.

Other Intangible Assets

Our intangible assets primarily consist of technical know-how contributed by IMU to our subsidiary IMU-Shengmu Dairy and computer software. We had other intangible assets in the amount of RMB15.0 million, RMB14.5 million and RMB14.2 million as of December 31, 2011, 2012 and 2013, respectively.

Investments in Associates

Our investments in associates represent our equity interest in Shanghai Saihan and Beijing Shengmu, which are distributors of our liquid milk products in Shanghai and Beijing, as well as in Shengmu Forage. We had investments in associates in the amount of RMB14.8 million, RMB17.6 million and RMB17.7 million as of December 31, 2011, 2012 and 2013, respectively. The year-on-year increase during the Track Record Period in our investments in associates primarily reflected the continuing growth of Shengmu Forage.

Biological Assets

Our biological assets consist of dairy cows, which are further categorized into calves, heifers and milkable cows. The following table sets forth the number of our biological assets as of the date indicated.

	As of December 31,					
	2011		2012		2013	
	Head	% of total	Head	% of total	Head	% of total
Calves and heifers	11,828	33.7%	21,747	44.0%	24,607	40.7%
Milkable cows	23,288	66.3%	27,636	56.0%	35,850	59.3%
Total	35,116	100.0%	49,383	100.0%	60,457	100.0%

The following table sets forth the fair value of our biological assets as of the date indicated.

	As of December 31,					
	2011		2012		2013	
	(RMB in thousands, except percentages)					
Calves and heifers	185,125	25.9%	353,443	34.3%	424,699	28.1%
Milkable cows	528,701	74.1%	676,098	65.7%	1,085,461	71.9%
Total	713,826	100.0%	1,029,541	100.0%	1,510,160	100.0%

The fair value of our biological assets increased by 46.7% from RMB1,029.5 million as of December 31, 2012 to RMB1,510.2 million as of December 31, 2013. The fair value of our biological assets increased by 44.2% from RMB713.8 million as of December 31, 2011 to RMB1,029.5 million as of December 31, 2012. The increase in the fair value of our biological assets during the Track Record Period was primarily due to a combination of (i) continuing increase in the fair value of milkable cows as a result of a combination of increases in the number of cows, average milk yield and raw milk price; and (ii) continuing increase in the fair value of calves and heifers as a result of increase in the number of heifers.

Valuation of dairy cows

Our dairy cows were independently valued by Jones Lang LaSalle, a firm of independent qualified professional valuers not connected with us, which has appropriate qualifications and experiences in valuation of biological assets. The following table sets forth the fair value of our dairy cow herd as of the date indicated.

	As of December 31,								
	2011			2012			2013		
	Herd value	Herd size	Average value	Herd value	Herd size	Average value	Herd value	Herd size	Average value
	RMB'000	Head	RMB	RMB'000	Head	RMB	RMB'000	Head	RMB
Calves and heifers	185,125	11,828	15,651	353,443	21,747	16,252	424,699	24,607	17,259
Milkable cows	528,701	23,288	22,703	676,098	27,636	24,464	1,085,461	35,850	30,278
Total	713,826	35,116	NM(1)	1,029,541	49,383	NM(1)	1,510,160	60,457	NM(1)

(1) NM means not meaningful.

Set forth below are the key assumptions and inputs adopted in the valuation process of our dairy cows. According to IFRS13.89, an entity shall develop unobservable inputs using the best information available in the circumstances, which might include the entity's own data. In developing unobservable inputs, an entity may begin with its own data, but it shall adjust those data if reasonably available information indicates that other market participants would use different data or there is something particular to the entity that is not available to other market participants. Based on the above standard, Jones Lang LaSalle has applied certain assumptions based on the actual data of our Company, by making appropriate adjustments in consideration of industry practice and market conditions. Jones Lang LaSalle advised us that it has adopted consistent approach in deriving relevant assumptions in the valuation of comparable listed dairy companies.

		As of and for the year ended December 31,		
		2011	**2012**	**2013**
Milkable cows				
Valuation approach for milkable cows[(1)]				
Raw milk prices (RMB/kilogram)[(2)]	Assumption used	3.88	4.50	5.00
	Actual	3.79	4.33	4.77
Feed costs (RMB/kilogram of raw milk)[(3)]	Assumption used	2.22	2.48	2.49
	Actual	2.10	2.21	2.25
Culling rate[(4)]	Assumption used	20.5	20.0	20.5
	Actual	12.5	15.6	24.8
Projected lactation periods[(5)]	Assumption used	6	6	6
Milk yield per head per lactation period (tonne)[(6)]	Assumption used	6-8	6-8	7-9
	Actual	7.6	7.8	8.5
Discount rate (%)[(7)]	Assumption used	15.34	14.00	14.50
Calves and heifers				
Valuation approach for calves and heifers[(8)]				
Per head market price of 14 month-old heifers (RMB)[(9)]	Assumption used	16,195	17,306	18,315
	Actual	N/A	N/A	N/A

(1) Valuation approach for milkable cows

The fair value of the milkable cows is developed through the application of income approach technique known as multi-period excess earnings method (MEEM). MEEM is a derivative of the discounted cash flow (DCF) method. Using this technique, we estimate the direct economic benefits attributed to the milkable cows. Such economic benefits are then capitalized at a rate which reflects all business risks including intrinsic and extrinsic uncertainties in relation to the subject assets. To estimate the economic benefit, the revenues for the milkable cows are projected over their remaining useful lives. Based on the projected revenues, the costs associated with supporting the milkable cows are net off. The net income projection is then adjusted by economic capital charges.

The capital charges include returns on the assets that are used or used up in the generation of the subject biological assets income projection. Examples of such assets include fixed asset, assembled workforce and working capital. Key assumptions for the MEEM include the following:

Components of Cash Inflow:
— Revenue from raw milk sales
— Revenue from female and male calves born
— Revenue from sales of culled cows

Components of Cash outflow:
— Feeds
— Salary, welfare and social insurance
— Others

(2) Raw milk prices

The raw milk prices used as an assumption in the valuation process are based on our historical average selling prices, prospects of demand and supply of raw milk, as well as the analysis of prices obtained from the markets where we operate as of the end of each reporting periods. The estimated fair value of milkable cows increases when the raw milk price increases.

Actual raw milk prices represent average selling prices for the period. As raw milk prices have generally been rising, the actual price for a given period is lower than the prices used in the assumption.

(3) Feed costs

The feed costs used as an assumption in the valuation process are based on our historical average feed costs per kilogram of raw milk at the end of each reporting periods. The estimated fair value of milkable cows decreases when the feed costs per kilogram of raw milk increases.

The feed costs used in the assumption are a fraction of (i) all feed costs occurred in a lactation cycle, as the numerator; and (ii) the volume of raw milk produced in a lactation cycle, as the denominator. The lactation cycle used in the valuation is assumed to be 400 days (i.e. each milkable cow is expected to give birth every 400 days).

The actual feed costs are a fraction of (i) the feed costs that were accounted under cost of sales of raw milk, for each of the year ended December 31 2011, 2012 and 2013 respectively, as the numerator; and (ii) the volume of raw milk produced for 2011, 2012 and 2013 respectively, as the denominator.

(4) Culling rate

It is normally assumed that the number of milkable cows at the end of each reporting period will decrease in the projection period at certain culling rates due to natural or unnatural factors, including illness, difficult birth, low milk production or completion of all lactation periods. We also choose to proactively cull the cows to improve the genetics of the next generations of cows.

The culling rate adopted as a valuation assumption assumed all milkable cows will be culled within six lactations, without taking into consideration the heifers that had given birth and became milkable cows during the Track Record Period which the actual culling rate did.

(5) Projected lactation periods

The projected lactation periods used as an assumption in the valuation are assumed to be six to seven lactation periods depending on the individual physical condition of the milkable cows. Typically, a milkable cow can be milked for six lactation periods. The estimated fair value of milkable cows increases when they have longer economic useful lives.

(6) Milk yield

The milk yield used as an assumption in the valuation process is based on historical milk yield, health conditions of cows, and management and operation of the dairy farms. Milk yield is expected to increase during the third to fourth lactation periods, and then decrease in the following lactation periods.

(7) Discount rate

Weighted Average Cost of Capital is applied in the determination of the discount rate. The discount rate reflects the time value of money and a risk premium, representing compensation for the risk inherent in the future cash flow that is uncertain. The estimated fair value of milkable cows decreases when discount rate increases.

(8)	Valuation approach for calves and heifers	The fair value of the heifers purchased within six month prior to each reporting date is determined with reference to the actual purchase price, with adjustment by adding the feed costs from the purchase date to the reporting date. For the calves and the rest heifers, the fair value of 14 months old heifers is determined by referring to the market price of the actively traded market and adjusted by the potential milking yield. The fair values of the heifers older than 14 months old are determined by adding the breeding costs required to raise the heifers from 14 months old to the respective specific ages plus the estimated margins that would be required by a raiser. The fair values of the heifers younger than 14 months old and the fair values of the calves are determined by subtracting the breeding costs required to raise the calves or heifers from the respective specific ages to 14 months old and the margins that would be required by a raiser.
(9)	Market price of 14 months old heifers	The fair values of 14 months old heifers are determined using the average market price at the actively traded markets as reference, and adjusted by the potential milking yield. As heifers of 14 months old are regularly traded and an actively traded market has been developed, Jones Lang LaSalle advised us that using their market price as reference in determining the fair values of calves and heifers is fair and reasonable and also in line with the market practice. We purchase heifers of different ages and therefore our actual purchase prices are not comparable to the prices of 14 months old heifers used in the assumption.

Prepayments for Property, Plant and Equipment and Biological Assets

See "— Discussion of Certain Statements of Financial Position Items — Prepayments, Deposits and Other Receivables" below.

Inventories

Our inventories primarily consist of raw materials, finished goods and consumables. Inventories of our dairy farming business primarily consist of feeds. Inventories of our liquid milk business primarily consist of packaging materials and finished goods. The following table sets forth the components of our inventories as of the date indicated and our turnover of inventories for the period indicated.

	As of December 31,		
	2011	**2012**	**2013**
	(RMB in thousands, except turnover days)		
Raw materials	98,383	194,462	319,525
Finished goods	—	—	832
Consumables	5,498	9,781	14,861
Total	103,881	204,243	335,218
Inventory turnover days(1)	80	84	100

(1) Inventory turnover days are calculated using the average of opening balance and closing balance of inventory for a year divided by the sum of cost of sales and breeding costs of calves and heifers that were capitalized and multiplied by 365 days.

Our inventories totaled RMB103.9 million, RMB204.2 million and RMB335.2 million as of December 31, 2011, 2012 and 2013, respectively. The increase during the Track Record Period was primarily due to a combination of (i) an increase in forages and other feeds which totaled RMB96.3 million, RMB188.9 million and RMB305.2 million as of December 31, 2011, 2012 and 2013, respectively, as we continued to increase our herd size; (ii) an increase in packaging materials which totaled nil, RMB1.7 million and RMB4.6 million as of December 31, 2011, 2012 and 2013, respectively, as a result of our expansion into the liquid milk business.

During the Track Record Period, our inventory turnover days increased from 80 days in 2011 to 84 days in 2012 and 100 days in 2013. The increase was primarily due to increasing storage of forages in anticipation of increase in number of dairy cows as new dairy farms commenced operations.

As of April 30, 2014, RMB188.3 million, or 56.2% of our inventories as of December 31, 2013 were used.

Trade and Bills Receivables

Our trade receivable balances represent the outstanding amounts receivable by us from our customers. The table below sets forth the components of our trade receivable balances as of the date indicated.

	As of December 31,		
	2011	2012	2013
	(RMB in thousands)		
Trade receivables			
- Dairy farming business	10,043	22,284	35,074
- Liquid milk business	—	2,226	28,396
Subtotal	10,043	24,510	63,470
Impairment	—	—	—
Total	10,043	24,510	63,470

As a result of the increase in our sales, our trade receivables increased from RMB10.0 million as of December 31, 2011, to RMB24.5 million as of December 31, 2012 and further to RMB63.5 million as of December 31, 2013. For our dairy farming business, we typically require our customers to make payments each month for raw milk purchased in the previous month. For the sales of our liquid milk products to our distributors, we typically require them to pay the entire purchase price of our products before delivery. We occasionally grant credit limits to distributor customers on a case-by-case basis.

The table below sets forth the aging analysis of our trade receivable balances as of the date indicated, as well as the trade receivable turnover days for the period indicated.

	As of and for the year ended December 31,		
	2011	2012	2013
	(RMB in thousands, except turnover days)		
Within three months	10,043	24,510	63,470
Trade receivable turnover days[1]	14	9	14

(1) Average trade receivables equal trade receivables at the beginning of the period plus trade receivables at the end of the period, divided by two. Trade receivables turnover days equals average trade receivables divided by revenue and then multiplied by 365.

During the Track Record Period, our trade receivables turnover days remained relatively short. During the same period, no impairment or provision of trade receivables had been provided because as of December 31, 2011, 2012 and 2013, none of our trade receivables were past due.

As of April 30, 2014, RMB63.1 million, or 99.4% of our trade receivables outstanding as of December 31, 2013 were settled.

Prepayments, Deposits and Other Receivables

Prepayments, deposits and other receivables primarily consist of prepayments. Our prepayments mainly consist of prepayments for forages, concentrated feed, dairy cows and packaging materials. Our prepayments totaled RMB19.1 million, RMB9.2 million and RMB83.8 million as of December 31, 2011, 2012 and 2013, respectively. Our prepayments increased significantly from RMB9.2 million as of December 31, 2012 to RMB83.8 million as of December 31, 2013, primarily due to prepayments paid to for purchase of dairy cows, to Shengmu Forage to secure the supply of forages and to Tetra Pak for packaging materials.

Trade and Bills Payables

Our trade and bills payables primarily relate to purchases of feed as well as packaging material and spare parts. Our trade and bills payables totaled RMB84.0 million, RMB132.2 million and RMB191.0 million as of December 31, 2011, 2012 and 2013, respectively. The increase in our trade payables during the Track Record Period primarily reflected an increase in the purchase of feeds and packaging materials as our business continued to expand.

The table below sets forth the aging analysis of our trade payables as of the date indicated as well as the trade payable turnover days for the period indicated.

	As of and for the year ended December 31,		
	2011	2012	2013
	(RMB in thousands, except turnover days)		
Less than one year	81,579	131,850	190,561
One to two years	2,384	292	359
Two to three years	—	9	117
	83,963	132,151	191,037
Trade payables turnover days[(1)]	55	59	60

(1) Trade payables turnover days are calculated using the average of opening balance and closing balance of trade payables for a year divided by the sum of cost of sales and breeding costs of calves and heifers that were capitalized and multiplied by 365 days.

Our trade payable turnover days increased from 55 days in 2011 to 59 days in 2012 and 60 days in 2013, which primarily reflected our increasing bargaining power against our suppliers as our purchase volume increased as a result of our business expansion.

As of April 30, 2014, RMB189.1 million, or 99.0% of our trade payables outstanding as of December 31, 2013 were paid.

Other Payables and Accruals

The table below sets forth the components of our other payables and accruals as of the date indicated.

	As of December 31,		
	2011	2012	2013
	(RMB in thousands)		
Payables for acquisition of property, plant and equipment	12,569	28,053	87,416
Payables for purchase of dairy cows	5,139	17,877	18,959
Payables for third parties' deposits	2,248	10,597	20,194
Salary and welfare payables	5,453	10,162	20,060
Advances from related parties	47,272	38,263	7,609
Payables for purchase of transportation services	901	1,931	8,217
Others	8,886	17,698	36,110
Total	82,468	124,581	198,565

Principal components of "other payables and accruals" include the following:

- *Payables for acquisition of property, plant and equipment*. These payables increased significantly during the Track Record Period as we expanded significantly our herd size, number of our dairy farms as well as production facilities.

- *Payables for purchase of dairy cows*. The increase in these payables was primarily due to the increase in purchase of dairy cows.

- *Payables for third parties' deposits*. These payables primarily represented deposits from (i) suppliers in our dairy farming business and (ii) distributors in our liquid milk products business. These payables increased as a result of the increase in herd size from our dairy farming business, coupled with our entry into the liquid milk products business.

- *Salary and welfare payables*. These payables increased primarily due to the expansion of our staff size to support our expanded operations.

- *Advances from related parties*. We had certain advances from related parties during the Track Record Period, all of which were settled as of March 29, 2014.

LIQUIDITY AND CAPITAL RESOURCES

Overview

To date, we have financed our operations primarily through cash from our operations, proceeds from bank loans, and to a lesser extent, through investments from equity investors and advances from related parties. As of December 31, 2013, we had RMB127.1 million in cash and cash equivalents, substantially all of which were denominated in Renminbi. Our cash and cash equivalents primarily consist of cash on hand and demand deposits.

The following table sets forth a summary of our cash flows for the period indicated.

	For the year ended December 31,		
	2011	2012	2013
	(RMB in thousands)		
Net cash generated from operating activities	141,204	177,942	363,630
Net cash used in investing activities	(408,376)	(535,215)	(934,299)
Net cash generated from financing activities	269,550	317,427	667,890
Net (decrease)/increase in cash and cash equivalents	2,378	(39,846)	97,221
Cash and cash equivalents at the beginning of the year	67,980	69,550	29,838
Effect of foreign exchange rate changes	(808)	134	—
Cash and cash equivalents at the end of the year	69,550	29,838	127,059

Operating Activities

Net cash generated from operating activities in 2013 was RMB363.6 million, which was primarily attributable to our profit before taxation of RMB375.4 million, an increase in trade and bills payables of RMB58.9 million and an increase in other payables and accruals of RMB110.0 million, and partially offset by non-cash net gains arising from the changes in fair value less costs to sell of biological assets of RMB9.5 million, an increase in inventories of RMB131.0 million, a decrease in trade and bills receivables of RMB39.0 million and an increase in prepayments, deposits and other receivables of RMB55.4 million.

Net cash generated from operating activities in 2012 was RMB177.9 million, which was primarily attributable to our profit before taxation of RMB198.9 million, an increase in trade and bills payables of RMB44.3 million and an increase in other payables and accruals of RMB23.3 million, and partially offset by non-cash net gains arising from the changes in fair value less costs to sell of biological assets of RMB4.4 million, an increase in inventories of RMB100.4 million and an increase in trade and bills receivables of RMB14.5 million.

Net cash generated from operating activities in 2011 was RMB141.2 million, which was primarily attributable to our profit before taxation of RMB223.2 million, an increase in trade and bills payables of RMB48.8 million and an increase in other payables and accruals of RMB23.9 million, and partially offset by non-cash net gains arising from the changes in fair value less costs to sell of biological assets of RMB117.1 million, an increase in inventories of RMB33.4 million and an increase in pledged deposits of RMB17.5 million.

Investing Activities

Net cash used in investing activities in 2013 was RMB934.3 million, which was attributable to (i) payments for breeding calves and heifers of RMB332.8 million; (ii) payment for the purchase of property, plant and equipment of RMB442.5 million in connection with additional dairy farms; and (iii) payment for the purchase of dairy cows of RMB316.5 million. The amount was partially offset by proceeds from disposal of dairy cows of RMB159.6 million.

Net cash used in investing activities in 2012 was RMB535.2 million, which was attributable to (i) payments for breeding calves and heifers of RMB200.1 million; (ii) payment for the purchase of property, plant and equipment of RMB243.6 million in connection with additional dairy farms; and (iii) payment for the purchase of dairy cows of RMB124.3 million. The amount was partially offset by proceeds from disposal of dairy cows of RMB39.0 million.

Net cash used in investing activities in 2011 was RMB408.4 million, which was attributable to (i) payments for breeding calves and heifers of RMB122.7 million; (ii) payment for the purchase of property, plant and equipment of RMB132.0 million in connection with additional dairy farms; and (iii) payment for the purchase of dairy cows of RMB175.9 million. The amount was partially offset by proceeds from disposal of dairy cows of RMB22.9 million.

Financing Activities

Net cash generated from financing activities in 2013 was RMB667.9 million, which was primarily attributable to (i) proceeds from new bank loans and new other loans of RMB959.8 million; (ii) capital injection by non-controlling interest of RMB114.9 million. The amount was partially offset by (i) repayment of bank and other loans of RMB374.2 million; and (ii) interest payment of RMB32.7 million.

Net cash generated from financing activities in 2012 was RMB317.4 million, which was primarily attributable to (i) proceeds from new bank loans and new other loans of RMB351.5 million; (ii) proceeds from issue of equity instruments and capital injection by non-controlling interest of RMB144.3 million. The amount was partially offset by (i) repayment of bank and other loans of RMB164.0 million; and (ii) interest payment of RMB14.4 million.

Net cash generated from financing activities in 2011 was RMB270.0 million, which was primarily attributable to (i) proceeds from new bank loans and new other loans of RMB84.5 million; (ii) proceeds from issue of equity instruments and capital injection by non-controlling interest of RMB243.0 million. The amount was partially offset by (i) repayment of bank loans of RMB50.0 million; and (ii) interest payment of RMB8.0 million.

INDEBTEDNESS

As of April 30, 2014, the latest practicable date for the purpose of the indebtedness statements, we had total indebtedness of approximately RMB880.0 million. The table below sets forth the components of our indebtedness as of the date indicated.

	As of December 31,			As of April 30,
	2011	2012	2013	2014
	(RMB in thousands)			
Current				
-unsecured bank and other borrowings (unguaranteed)	—	145,000	782,000	880,000
-guaranteed bank and other borrowings (unsecured)	75,000	130,000	150,000	—
-current portion of guaranteed long-term bank and other borrowings (unsecured)	—	49,000	—	—
	75,000	324,000	932,000	880,000
Non-current				
-guaranteed long-term bank and other borrowings (unsecured)	49,000	—	—	—
Total	124,000	324,000	932,000	880,000

The table below sets forth the effective interest rates of our borrowings as of the date indicated.

	As of December 31,			As of April 30,
	2011	2012	2013	2014
	(In percentages)			
Current				
-Unsecured bank and other borrowings (unguaranteed)	—	6.31%	6.00%	6.00%
-Guaranteed bank and other borrowings (unsecured)	5.47-5.81%	6.00-6.56%	6.00%	—
-Current portion of guaranteed long-term bank and other borrowings (unsecured)	—	5.60%	—	—
Non-current				
-Guaranteed long-term bank and other borrowings (unsecured)	5.60%	—	—	—

Bank and other borrowings — guaranteed (unsecured)

The following table sets forth details of our guaranteed bank and other borrowings as of April 30, 2014.

	Outstanding as of December 31, 2013			Outstanding amount as of April 30, 2014
	Amount	Interest rate	Term/ maturity date	
	(RMB in thousands)			(RMB in thousands)
China Merchant Bank	100,000	6.0%	One year/between February 27 and November 19, 2014	—
Inner Mongolia Bank	50,000	6.0%	One year/February 5, 2014	—
	150,000			—

These loans contain customary covenants and restrictions for facilities of this type in the PRC, including restrictions on disposal of the borrower's material assets through assignment, leasing or providing guarantee unless otherwise agreed by the lender in writing and obligations to make timely notice to the lender for any material development of the borrower's operations. These loans were guaranteed by Mr. YAO Tongshan and certain other shareholders, and the guarantees were released by February 28, 2014.

Bank and other borrowings — unsecured (unguaranteed)

The following table sets forth details of our unsecured bank and other borrowings as of April 30, 2014.

	Outstanding as of December 31, 2013			Outstanding amount as of April 30, 2014
	Amount	Interest rate	Term/ maturity date	
	(RMB in thousands)			(RMB in thousands)
Bank of China	297,000	6.0%	One year/between July 22, 2014 and December 12, 2014	345,000
Agricultural Bank of China	178,000	6.0%	One year/between February 27 and July 1, 2014	158,000
Huaxin International Trust	30,000	6.0%	One year/April 14, 2014	—
Bank of Communication	137,000	6.0%	One year/between May 23 and October 30, 2014	137,000
China Minsheng Bank	80,000	6.0%	One year/between July 29 and August 28, 2014	80,000
China Merchant Bank	60,000	6.0%	One year/between November 17 and December 23, 2014	160,000
	782,000			880,000

These loans contain customary covenants and restrictions for facilities of this type in the PRC, including restrictions on disposal of the borrower's material assets through assignment, leasing or providing guarantee unless otherwise agreed by the lender in writing and obligations to make timely notice to the lender for any material development of the borrower's operations.

During the Track Record Period and up to the Latest Practicable Date, our Directors confirm that they are not aware of any material defaults in payment of our trade and non-trade payables and bank borrowing. Other than otherwise disclosed in this [REDACTED], the agreements under our bank borrowings do not contain any material covenants that will have a material adverse effect on our ability to make additional borrowings or issue debt or equity securities in the future.

Save as disclosed herein, we did not have any other material borrowings, indebtedness, facilities, hire purchase commitments, mortgages and charges, or other material contingent liabilities as of April 30, 2014.

Our Directors confirm that we did not have any material default in payment of trade or other payables or bank borrowings, nor did we breach any material financial covenants during the Track Record Period. Except short-term notes and refinancing of and drawdown under facilities as described under "— Working Capital," our Directors have confirmed that we do not have any plan to raise additional external debt financing as of the Latest Practicable Date.

We do not anticipate any changes to the availability of bank financing to finance our operations in the future, although there is no assurance that we will be able to access bank financing on favorable terms or at all.

Statement of Indebtedness

Save as disclosed in this [REDACTED], we did not have outstanding indebtedness or any loan capital issued and outstanding or agreed to be issued, bank overdrafts, loans or similar indebtedness, liabilities under acceptance (other than normal trade bills), acceptance credits, debentures, mortgages, charges, finance leases or hire purchase commitments, guarantees or other contingent liabilities as of April 30, 2014, being the latest practicable date for our indebtedness statement. Our Directors confirm that, as of the Latest Practicable Date, there is no material change in the Company's indebtedness since April 30, 2014.

COMMITMENTS

Capital Commitments

The table below sets forth details of our capital commitments as of the date indicated.

	As of December 31,		
	2011	2012	2013
	(RMB in thousands)		
Contracted but not provided for:			
-Land and buildings	78,510	57,703	48,501
-Plant and machinery	14,850	4,065	37,641
	93,360	61,768	86,142

Operating Lease Commitments

We lease a number of dairy farms including building structures and equipment, and office properties, under non-cancellable operating lease arrangements. The table below sets forth our future minimum rental payments under non-cancellable operating lease agreements as of the date indicated.

	As of December 31,		
	2011	2012	2013
	(RMB in thousands)		
Within one year	10,247	9,668	8,949
Later than one year and no later than five years	28,523	28,170	24,859
After five years	10,043	5,022	—
	48,813	42,860	33,808

CAPITAL EXPENDITURES

Our capital expenditures totaled RMB452.0 million, RMB625.5 million and RMB1,135.1 million in 2011, 2012 and 2013, respectively. Our capital expenditures during the Track Record Period primarily related to acquisitions of property, plant and equipment, prepaid land lease payments, acquisitions of other intangible assets and biological assets as our business expanded as well as an increase in investments in associates.

Following the completion of the [REDACTED], we will continue to incur capital expenditures to grow our business. We expect our capital expenditures to total RMB1,040.4 million in 2014 and RMB734.0 million in 2015. Our planned future capital expenditures in the foreseeable future primarily relate to purchase of dairy cows and construction of additional organic dairy farms. See also "Future Plans and [REDACTED]."

WORKING CAPITAL

The table below sets forth the details of our current assets and liability as of the date indicated.

	As of December 31,			As of April 30,
	2011	2012	2013	2014
	(RMB in thousands)			
Current assets				
Inventories	103,881	204,243	335,218	261,805
Trade and bill receivables	10,043	24,510	63,470	139,657
Prepayments, deposits and other receivables	15,893	30,030	94,377	185,781
Pledged deposits	29,224	12,797	15,030	8,989
Cash and cash equivalents	69,550	29,838	127,059	368,517
Total current assets	228,591	301,418	635,154	964,749
Current liabilities				
Trade and bills payables	83,963	132,151	191,037	130,795
Receipts in advance	15,473	17,527	82,481	59,282
Other payables and accruals	82,468	124,581	198,565	194,657
Interest-bearing bank borrowings	75,000	324,000	932,000	880,000
Tax payable	—	—	633	529
Total current liabilities	256,904	598,259	1,404,716	1,265,263
Net current liabilities	(28,313)	(296,841)	(769,562)	(300,514)

Our net current liabilities increased from RMB 28.3 million as of December 31, 2011 to RMB296.8 million as of December 31, 2012, and to RMB769.6 million as of December 31, 2013. The increase in our net current liabilities during the Track Record Period primarily reflected our funding needs to purchase and breeding of dairy cows and to support our continuing investment in property, plant and equipment related to dairy farms and processing facilities to expand our business, which was primarily financed through short-term bank loans, which increased significantly, totaling RMB75 million, RMB324 million and RMB932 million as of December 31, 2011, 2012 and 2013, respectively.

Since December 31, 2013, our net current liabilities has decreased significantly due to the pre-[REDACTED] investments in our company in February 2014, as a result of which we received an additional RMB683.3 million in shareholders' equity, and a corresponding increase in cash and cash equivalents. As of the Latest Practicable Date, we had credit facilities of an aggregate amount of RMB1,317.0 million, for RMB1,272.0 million of which we have obtained pre-approval letters from the relevant banks (stating that the banks will grant new facilities to us upon expiration of the current term and repayment of existing facilities), and of which RMB428.0 million have not been utilized. In addition, we were approved in March 2014 to issue short-term notes of up to RMB200 million and we have not issued any such notes as of the Latest Practicable Date.

Our Directors confirm that, taking into account the above sources of funding, as well as our current cash and cash equivalents, anticipated cash flow from operations and proceeds from the [REDACTED], we will have sufficient working capital to meet our anticipated cash needs, including our working capital and capital expenditures requirements for at least the next 12 months from the date of this [REDACTED].

After due consideration and discussion with the Company's management and based on the above, the Joint Sponsors have no reason to believe that the Company cannot meet the working capital requirements for the 12 month period from the date of this [REDACTED].

Our future cash requirements will depend on many factors, including our operating income, costs to establish additional dairy farms, market acceptance of our products and services or other changing business conditions and future developments, including any investments or acquisitions we may decide to pursue. We may require additional cash to repay existing debt obligations or to re-finance our existing debts due to changing business conditions or other future developments. If our existing cash is insufficient to meet our requirements, we may seek to sell additional equity securities, debt securities or borrow from lending institutions. We cannot assure you that financing will be available in the amounts we need or on terms acceptable to us, if at all. The sale of additional equity securities, including convertible debt securities, would dilute our Shareholders' interests in our Company. The incurrence of debt would divert cash for working capital and capital expenditures to service debt obligations and could result in operating and financial covenants that restrict our operations and our ability to pay dividends to our Shareholders. If we are unable to obtain additional equity or debt financing as required, our business operations and prospects may suffer.

CONTINGENT LIABILITIES

As of the Latest Practicable Date, we did not have significant contingent liabilities.

RELATED PARTY TRANSACTIONS

It is the view of our Directors that each of the related party transactions set out in note 32 to the Accountants' Report set forth in Appendix I to this [REDACTED] were conducted in the ordinary and usual course of business and on normal commercial terms between the relevant parties. See the section headed "Continuing Connected Transactions" for more details.

The following table sets forth the outstanding balances with related parties as of the date indicated.

	As of December 31,		
	2011	2012	2013
	(RMB in thousands)		
Amounts due from associates			
included in			
- Accounts receivable	—	—	1,386
- Prepayments, deposits and other receivables(1)	—	—	57,501
Amounts due to associates			
included in			
- Receipts in advance	—	200	—
- Trade payables(1)	—	12,039	2,963
- Other payables and accruals(1)	3,272	38,263	—
Amounts owed by/(owed to) certain shareholders			
included in:			
− Other payables and accruals(2)	(44,000)	—	(6,880)

(1) Primarily relating to purchases of forages and advances from Shengmu Forage.

(2) Primarily relating to purchases of dairy cows.

Other than the accounts receivable and trade payables due from/to related parties, the above transactions with related parties are unsecured, interest-free and have no fixed terms of repayment. Accounts receivable and trade payables with related parties have similar credit terms to those offered by/to independent third parties. All balances from our non-trade related party transactions outstanding as of December 31, 2013 (consisting of RMB6.9 million in amounts owed to Shareholders) have been settled as of March 29, 2014.

During the Track Record Period, Shengmu Forage provided free biowaste (i.e., cow dung) cleaning services to our organic dairy farms. Such services include collecting and cleaning unprocessed biowaste from our farms. In return, Shengmu Forage acquired such unprocessed biowaste from our farms at no cost. After the [REDACTED], we expect to continue to receive such biowaste cleaning services from Shengmu Forage.

In 2011, we also sold our raw milk with an aggregate amount of RMB 46.8 million to Mengniu Group, which is principally engaged in the production of dairy products in the PRC and is [REDACTED] on the Main Board of the Hong Kong Stock Exchange, through two individuals, who were the then directors of Shengmu Holding.

OFF-BALANCE SHEET ARRANGEMENTS

We have not entered into any off-balance sheet arrangements or commitments to guarantee the payment obligations of any third parties. We do not have any variable interest in any uncombined entity that provides financing, liquidity, market risk or credit support to us or engages in leasing or hedging or research and development services with us.

QUALITATIVE AND QUANTITATIVE DISCLOSURE ABOUT MARKET RISK

We are exposed to various types of market risks in the ordinary course of our business. The main risks arising from our financial instruments are interest rate risk, foreign currency risk, credit risk and liquidity risk. We manage our exposure to these risks through regular operating and financial activities. The Board regularly reviews these risks and our financial risk management policy seeks to ensure that adequate resources are available to manage the market risks summarized below and to create value for our Shareholders.

Interest Rate Risk

We are exposed to cash flow interest rate risk due to fluctuations in the prevailing market interest rates on cash and cash equivalents and pledged bank deposits. We consider that these bank balances are not sensitive to fluctuation in interest rate. Our fair value interest rate risk relates primarily to fixed-rate bank borrowings. We currently do not have an interest rate hedging policy. However, we monitor interest rate exposure and will consider hedging significant interest rate exposure should the need arises.

Foreign Currency Risk

Our businesses are principally located in the PRC and substantially all transactions are conducted in Renminbi, except for the purchases of imported biological assets, machinery and equipment. During the Track Record Period, substantially all of our assets and liabilities were denominated in Renminbi, except that as of December 31, 2011, cash and bank balances of approximately RMB11.2 million were denominated in U.S. dollars. The fluctuation of the exchange rates of Renminbi against foreign currencies could slightly affect our results of operations. We do not hedge against any fluctuation in foreign currency. We have conducted a sensitivity analysis to determine our exposure to changes in foreign currency exchange rates. Our profit before tax would have increased by RMB0.8 million, RMB0.1 million and nil, respectively, if U.S. dollars had strengthened by 5.0% against Renminbi with all other variables held constant in 2011, 2012 and 2013, respectively.

Credit Risk

We trade only with recognized and creditworthy third parties. It is our policy that all customers who wish to trade on credit terms are subject to credit verification procedures. In addition, receivable balances are monitored on an on-going basis and our exposure to bad debts is not significant. Credit risk relating to our other financial assets, which comprise cash and bank balances and other receivables, arises from the default of the counterparty with a maximum exposure equal to the carrying amounts of these instruments. Since we trade only with recognized and creditworthy third parties, there is no requirement for collateral.

We have concentration of credit risk as 99%, 89% and 51% of total trade receivables as of December 31, 2011, 2012 and 2013, respectively, which was due from our top two customers, namely, Mengniu Group and Yili Group, which are principally engaged in milk processing industry in the PRC and listed in the main board of the Stock Exchange and Shanghai Stock Exchange, respectively.

Liquidity Risk

Our objective is to maintain a balance between continuity of funding and flexibility through the use of bank loans and projected cash flows from operations. Based on contractual undiscounted payments, our financial liabilities were RMB292.0 million, RMB581.6 million and RMB1,328.7 million as of December 31, 2011, 2012 and 2013, respectively. We believe there is no significant liquidity risk as we have sufficient committed facilities to fund our operations.

We expect to fund our future cash flow needs through primarily internally generated cash flows from operations, bank borrowings, the [REDACTED] from the [REDACTED], as well as any equity and debt offerings after the [REDACTED].

Capital Management

The primary objectives of our capital management are to safeguard our ability to continue as a going concern and to maintain healthy capital ratios in order to support its business and maximize shareholders' value. We manage our capital structure and make adjustment to it in light of changes in economic conditions and the risk characteristics of the underlying assets. In order to maintain or adjust the capital structure, we may adjust the amount of dividends paid to Shareholders, return capital to Shareholders or issue new [REDACTED]. No changes were made to the objectives, policies or processes for managing capital during the Track Record Period. Consistent with others in the industry, we monitor capital on the basis of the gearing ratio. This ratio is calculated as net debt divided by total capital. Our policy is to maintain a healthy gearing ratio. Our gearing ratio was 14.2%, 26.6% and 54.6% as of December 31, 2011, 2012 and 2013, respectively.

KEY FINANCIAL RATIOS

The following table sets forth our certain key financial ratios for the period indicated or as of the date indicated.

	As of and for the period ended December 31,		
	2011	2012	2013
Return on equity(1)	26.1%	16.8%	21.9%
Return on assets(2)	18.9%	10.9%	12.0%
Current ratio(3)	0.89	0.50	0.45
Quick ratio(4)	0.49	0.16	0.21
Gearing ratio(5)	14.2%	26.6%	54.6%

(1) Calculated as net profit attributable to owners of the Company for the period divided by total equity attributable to owners of the Company at the end of the period, then multiplied by 100%.

(2) Calculated as net profit for the period divided by total assets at the end of the period, then multiplied by 100%.

(3) Calculated as current assets divided by current liabilities.

(4) Calculated as current assets less inventory divided by current liabilities.

(5) Calculated as bank borrowings divided by total equity, then multiplied by 100%.

Our return on equity, or ROE, decreased from 26.1% in 2011 to 16.8% in 2012 primarily due to a significant decrease in our gain arising from changes in fair value less costs to sell of biological assets in 2012, which decreased from RMB117.1 million in 2011 to RMB4.4 million. In 2010, we purchased our dairy cows at a lower market price due to the melamine incidents in China in 2008, which resulted in a relatively high gain from the changes in fair value of our dairy cows in 2011 compared to 2012. Our net profit before biological asset fair value adjustments, representing the difference of our net profit and gain/(loss) arising from changes in the fair value less costs to sell of biological assets, increased from RMB106.1 million in 2011 to RMB194.5 million in 2012. Our ROE increased from 16.8% in 2012 to 21.9% in 2013 primarily due to a significant increase in our net profit, partially offset by an increase in our total equity.

Similar to ROE, our return on assets, or ROA, decreased from 18.9% in 2011 to 10.9% in 2012 primarily due to the significant decrease in our gain arising from changes in fair value less costs to sell of biological assets in 2012. Our ROA increased from 10.9% in 2012 to 12.0% in 2013 primarily due to a significant increase in our net profit, partially offset by an increase in our total assets.

Our current ratio decreased from 0.89 as of December 31, 2011 to 0.50 as of December 31, 2012 and further to 0.45 as of December 31, 2013, primarily due to increases in our current liabilities in connection with our business growth. To support our growth, we used significant cash generated from our operations and from bank borrowings to fund our capital expenditures for purchases of dairy cows and construction of our dairy farms and liquid milk processing plant, which contributed to the increase in our current liabilities and partially offset the increase in our current assets.

Similar to the decrease in our current ratio, our quick ratio decreased from 0.49 as of December 31, 2011 to 0.16 as of December 31, 2012, primarily due to increases in our current liabilities in connection with our business growth. Our quick ratio increased from 0.16 as of December 31, 2012 to 0.21 as of December 31, 2013, primarily because our current assets excluding inventory increased by a higher rate than our current liabilities.

Our gearing ratio increased from 14.2% as of December 31, 2011 to 26.6% as of December 31, 2012 and further to 54.6% as of December 31, 2013, primarily due to increases in our bank borrowings in connection with our business growth. To support our growth, we borrowed significant bank loans to fund our capital expenditures for purchases of dairy cows and construction of our dairy farms and liquid milk processing plant.

VALUATION OF BIOLOGICAL ASSETS

We have engaged Jones Lang LaSalle, a firm of independent qualified professional valuers, to determine the fair value of our dairy cows as of December 31, 2011, 2012 and 2013, respectively. The key members of the Jones Lang LaSalle valuers include Mr. Simon Chan and Professor T.Y. GAO.

Mr. Simon Chan, regional director at Jones Lang LaSalle, is a Fellow of the Hong Kong Institute of Certified Public Accountants (HKICPA) and a Fellow of CPA Australia. He is also a Certified Valuation Analyst (CVA), a member of The International Association of Consultants, Valuers and Analysts (IACVA), a member of Canadian Institute of Mining, Metallurgy and Petroleum (CIM), and a member of the Australasian Institute of Mining and Metallurgy (AusIMM). Simon oversees the business valuation services of Jones Lang LaSalle and has over 15 years of accounting, auditing, corporate advisory and valuation experiences. He has provided a wide range of valuation services to numerous listed and listing companies of different industries in China, Hong Kong, Singapore and the United States. Simon oversaw the valuation of biological assets for the initial public offerings and subsequent financial reports of China Modern Dairy Holdings Ltd (1117.HK), China Huishan Dairy Holdings Company Limited (6863.HK), and YuanShengTai Dairy Farm Limited (1431.HK). He also led the valuation of other biological assets, such as hogs, trees, rabbits and chickens, for financial reporting purpose of Hong Kong listed companies including Chenming Paper (1812.HK), China Mengniu Dairy Company Limited (2319.HK) and Kandda Food (834.HK), as well as numerous private companies.

Prof. T.Y. GAO, a professor of Henan Agricultural University (Animal Science), and an independent biological asset valuation expert, is a council member of the China Animal Husbandry and Veterinary Association Cattle Branch, an executive director of the China Animal Husbandry and Veterinary Association Animal Ecology Branch, an executive director of the Animal Husbandry Engineering Branch of the Agricultural Engineering Society, an executive director of the China Scalper Breeding Committee, a deputy secretary of the Straw Utilization Branch of China Agricultural Society and an executive director of the Grass Fodder Branch of the Animal Husbandry and Veterinary Institute. He has extensive experience in the area of cow breeding and is mainly engaged in the study of the utilization of local feeds resources for feeding cattle, environment management of dairy cows and livestock ecology. Professor GAO has published 23 books, has won 15 prizes of scientific achievements and has published more than 200 academic papers in different journals, most of which are on the research and study of dairy cows and dairy production. He participated in the valuation of biological assets for the [REDACTED] and subsequent financial reports of China Modern Dairy Holdings Ltd (1117.HK), China Huishan Dairy Holdings Company Limited (6863.HK), and YuanShengTai Dairy Farm Limited (1431.HK).

Based on market reputation and relevant background research, our Directors and the Joint Sponsors are satisfied that Jones Lang LaSalle is independent from us and is competent in conducting a valuation on our biological assets.

Valuation Method

Dairy cows

Calves and heifers

A market-based approach is adopted by Jones Lang LaSalle to value our calves and heifers, because recent market-based prices for heifers at a certain age exist near each reporting date and therefore the fair value of the calves and heifers is developed through the application of the market approach with reasonable adjustments to reflect age and potential milk yield differences.

Milkable Cows

An income-based approach is adopted by Jones Lang LaSalle to value our milkable cows, primarily because there is no reliable market-based price for dairy cow at this stage. In general, raisers of dairy cows do not sell dairy cows that are milkable, as milking generate more profits in the long run than the sales of dairy cows. As a result, the fair value of the milkable cows is developed through the application of an income approach technique known as multi-period excess earnings method ("MEEM"). MEEM is a derivative of the discounted cash flow ("DCF") method. Using this technique, Jones Lang LaSalle estimates the direct economic benefits attributed to the milkable cows. Such economic benefits are then capitalized at a rate which reflects all business risks including intrinsic and extrinsic uncertainties in relation to the subject assets. To estimate the economic benefit, the revenues for the milkable cows are projected over their remaining useful lives. Based on the projected revenues, the costs associated with supporting the milkable cows are offset. The net income projection is then adjusted by certain economical capital charges. The capital charges include returns on the assets that are used or used up in the generation of the subject biological assets income projection. Examples of such assets include fixed assets, assembled workforce and working capital.

Our Directors and the Joint Sponsors held various discussions with Jones Lang LaSalle in relation to their methodologies and procedures required to prepare their valuation report. Our Directors and the Joint Sponsors further compared the valuation methodologies chosen with those used by the industry peers. Our Directors, the Joint Sponsors are satisfied that the valuation methodologies chosen are appropriate and reasonable.

Key Assumptions and Inputs

Dairy cows

Key inputs for valuing our dairy cows are the number and classification of dairy cows. Based on maturity stages, our dairy cows are classified into calves and heifers and milkable cows. Different valuation approaches are adopted for calves and heifers and milkable cows.

Calves and heifers

The key inputs and assumptions for valuing our calves and heifers are the per head market price for 14 months old heifers, which were RMB 16,195, RMB17,306 and RMB18,315 as of December 31, 2011, 2012 and 2013, respectively.

Milkable cows

The key assumptions and inputs include the revenues from milking the dairy cows and the costs associated with the milkable cows. Jones Lang LaSalle also assumes that there will be no material change in the existing political, legal, technological, fiscal or economic condition which may adversely affect our business. In deriving the residual cash flow of the milkable cows, Jones Lang LaSalle has deducted returns on contributory assets, which represent charges for the use of contributory assets employed to support the milkable cows and help generate revenue. Our Directors confirmed, and the Joint Sponsors concurred, that the key bases and assumptions used by Jones Lang LaSalle in the valuation process are consistent with those used by the industry peers and are appropriate and reasonable.

The key assumptions and inputs for calculating the revenues from milking include the following:

- The number of and the respective estimated culling rates and calf birth rates for, milkable cows at different lactation stages.
- The milk yield rate as adjusted by an estimated spoilage rate at different lactation stages.
- The prices for raw milk produced by, and female and male calves given birth by, milkable cows at different lactation stages.

Based on the above assumptions, the total revenue from our milkable cows as forecasted in the valuation process as of December 31, 2013 is approximately RMB4.8 billion.

The key assumptions and inputs for calculating the costs associated with raising the milkable cows include the following:

- feeds;
- salary, welfare and social insurance; and
- others.

Based on the above assumptions, the total costs in relation to our milkable cows as forecasted in the valuation process as of December 31, 2013 is approximately RMB3.3 billion.

The Directors and the Joint Sponsors discussed with Jones Lang LaSalle in relation to their methodologies, procedures, key bases and assumptions and understand that Jones Lang LaSalle has conducted the biological asset valuation in accordance with International Accounting Standard 41 - Agriculture, issued by the International Accounting Standards Board and with reference to the International Valuation Standards, issued by the International Valuation Standards Council. The key assumptions, as detailed above, are made based on the historical actual operation performance of the Company. Jones Lang LaSalle has obtained and discussed with us regarding the historical actual operation data from us, and considered and reviewed whether they are appropriate and reasonable to be used in the valuation. Jones Lang LaSalle confirmed that their valuation procedures provide a reasonable basis for their opinion, the inputs used in the valuation technique are appropriate and reasonable. Our Directors and the Joint Sponsors confirm that the key bases and assumptions adopted are consistent with industry practice and in line with the actual figures during the Track Record Period.

Sensitivity Analysis

The following table illustrates the sensitivity of the estimated fair value of milkable cows that would arise if the key inputs had changed as of 31 December 2013, assuming all other variables remained constant.

Milk price sensitivity

Assumed Milk Price:	5.00	RMB/kg						
% Change in Milk Price	10.00%	5.00%	2.00%	1.00%	-1.00%	-2.00%	-5.00%	-10.00%
Corresponding Valuation Result (RMB'000)	1,377,168	1,232,007	1,144,913	1,115,885	1,057,819	1,028,790	941,696	796,545
Change in Valuation Result (RMB'000)	291,707	146,546	59,452	30,424	-27,642	-56,671	-143,765	-288,916
% Change in Valuation Result	*26.87%*	*13.50%*	*5.48%*	*2.80%*	*-2.55%*	*-5.22%*	*-13.24%*	*-26.62%*

The estimated fair value of milkable cows increases when the milk price increases, and decreases when the milk price decreases.

Discount rate sensitivity

Assumed Discount Rate:	14.50%					
% Change in Discount Rate	1.50%	1.00%	0.50%	-0.50%	-1.00%	-1.50%
Corresponding Valuation Result (RMB'000)	1,057,798	1,066,859	1,076,076	1,094,994	1,104,708	1,114,586
Change in Valuation Result (RMB'000)	-27,663	-18,602	-9,385	9,533	19,247	29,125
% Change in Valuation Result	-2.55%	-1.71%	-0.86%	0.88%	1.77%	2.68%

The estimated fair value of milkable cows increases when the discount rate decreases, and decreases when the discount rate increases.

Milk yield sensitivity

Assumed Milk Yield:	20.84	kg/head/day						
% Change in Milk Yield	10.00%	5.00%	2.00%	1.00%	-1.00%	-2.00%	-5.00%	-10.00%
Corresponding Valuation Result (RMB'000)	1,218,592	1,152,021	1,112,079	1,098,775	1,072,146	1,058,832	1,018,890	952,319
Change in Valuation Result (RMB'000)	133,131	66,560	26,618	13,314	-13,315	-26,629	-66,571	-133,142
% Change in Valuation Result	12.26%	6.13%	2.45%	1.23%	-1.23%	-2.45%	-6.13%	-12.27%

The estimated fair value of the milkable cows increases when the milk yield increases, and decreases when the milk yield decreases.

Feed cost sensitivity

Assumed Feed Costs:	2.49	RMB/kg						
% Change in Feed Costs	10.00%	5.00%	2.00%	1.00%	-1.00%	-2.00%	-5.00%	-10.00%
Corresponding Valuation Result (RMB'000)	931,759	1,008,605	1,054,720	1,070,085	1,100,826	1,116,201	1,162,306	1,239,162
Change in Valuation Result (RMB'000)	-153,702	-76,856	-30,741	-15,376	15,365	30,740	76,845	153,701
% Change in Valuation Result	-14.16%	-7.08%	-2.83%	-1.42%	1.42%	2.83%	7.08%	14.16%

The estimated fair value of the milkable cows increases when the feed costs decrease, and decreases when the feed costs increase.

Heifer price sensitivity

Assumed Heifer Price:	18,315	RMB						
% Change in Heifer Price	10.00%	5.00%	2.00%	1.00%	-1.00%	-2.00%	-5.00%	-10.00%
Corresponding Valuation Result (RMB'000)	1,132,388	1,108,919	1,094,846	1,090,148	1,080,763	1,076,075	1,061,992	1,038,523
Change in Valuation Result (RMB'000)	46,927	23,458	9,385	4,687	-4,698	-9,386	-23,469	-46,938
% Change in Valuation Result	4.32%	2.16%	0.86%	0.43%	-0.43%	-0.86%	-2.16%	-4.32%

The estimated fair value of the milkable cows increases when the price of heifers increases, and decreases when the price of heifers decreases.

Stock-take and Internal Control

Stock-take

We have established a standard protocol for stock take consisting of periodic and random stock take to ensure the physical existence of our biological assets and accuracy of relevant data and information. Each of our dairy farms is required to perform a full stock take on a quarterly basis to ensure the relevant information such as headcount and, age-grouping are accurately reflected in our dairy farm information management system and submit a detailed report to the record keeping department at our headquarters. The dairy cow officers, staff of finance department, staff of record keeping department and the heads of relevant departments are required to confirm the result of the quarterly full stock take in writing. Our finance department also performs stock-take when dairy farm manager or dairy cow officer resigns or is replaced.

Internal Control and Management System

We have devised a comprehensive policy for biological asset management. Our biological asset management policy covers among other things, the relevant accounting policies, transferring among age groups, purchase and disposal of dairy cows, breeding, record keeping and stock take. To facilitate the implementation of our biological asset management policy, we employ the dairy farm information management system developed by a third-party developer, in collaboration with the accounting system, to keep comprehensive record of our dairy cows herd.

[REDACTED]

The following [REDACTED] of our Group prepared in accordance with Rule 4.29 of the Listing Rules is for illustrative purposes only, and is set out below to illustrate the effect of the [REDACTED] on the net tangible assets of our Group attributable to the equity holders of our Company as of December 31, 2013 as if the [REDACTED] had taken place on December 31, 2013 assuming none of the [REDACTED] and options that have been granted under the Pre-[REDACTED] Share Option Scheme or may be granted under the Share Option Scheme has been exercised.

This [REDACTED] has been prepared for illustrative purposes only and because of its hypothetical nature, it may not give a true picture of the combined net tangible assets of our Group as of December 31, 2013 or at any future dates following the [REDACTED]. It is prepared based on the combined net assets of our Group as of December 31, 2013 as set out in the Accountant's Report of our Group, the text of which is set out in Appendix I to this [REDACTED], and adjusted as described below.

	Combined net tangible assets attributable to the owners of the Company as of December 31, 2013	Estimated net [REDACTED]	[REDACTED]	[REDACTED] per Share	[REDACTED] per Share
	RMB'000	RMB'000	RMB'000	RMB	HK$
Based on an [REDACTED] of HK$[REDACTED] per Share	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]
Based on an [REDACTED] of HK$[REDACTED] per Share	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]	[REDACTED]

DISTRIBUTABLE RESERVES

The Company was only incorporated on December 11, 2013. The Company did not have any distributable reserves as of December 31, 2013 and as of the Latest Practicable Date.

DISCLOSURE PURSUANT TO RULES 13.13 TO 13.19 OF THE LISTING RULES

Except as otherwise disclosed in this [REDACTED], we confirm that, as of the Latest Practicable Date, we were not aware of any circumstances that would give rise to a disclosure requirement under Rules 13.13 to Rules 13.19 of the Listing Rules.

DIVIDEND POLICY

We have not declared any dividends during the Track Record Period. Our Board at its discretion may declare dividends in the future after taking into account our operations, earnings, financial condition, cash requirements and availability and other factors as it may deem relevant at such time. The payment of any dividends will also be subject to our articles of association, the Companies Law, applicable laws and other relevant factors.

[REDACTED]

We incurred [REDACTED] (excluding [REDACTED]) of RMB2.1 million during the Track Record Period, of which RMB1.8 million was recognized as administrative expenses and RMB0.3 million was capitalized as deferred [REDACTED] that are expected to be charged against equity upon successful [REDACTED] under the relevant accounting standards. We expect to incur further [REDACTED] (excluding [REDACTED]) of approximately RMB28.3 million, of which RMB22.8 million will be recognized as administrative expenses and RMB5.5 million will be charged against equity. We do not believe the remaining expenses will have a material impact on our results of operations for 2014.

DIRECTORS' CONFIRMATION ON NO MATERIAL ADVERSE CHANGE

Our Directors confirm that they have performed sufficient due diligence on our Company to ensure that, up to the date of this [REDACTED], there has been no material adverse change in our financial or trading position or prospects since December 31, 2013 (being the date to which our Company's latest combined audited financial results were prepared), and there has been no events since December 31, 2013 which would materially affect the information shown in the Accountants' Report, the text of which is set out in Appendix I to this [REDACTED].