CHINA SHENGMU ORGANIC MILK LIMITED
中國聖牧有機奶業有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 1432)

FINAL RESULTS ANNOUNCEMENT
FOR THE YEAR ENDED DECEMBER 31, 2017

FINANCIAL HIGHLIGHTS

	For the year ended December 31,		
	2017	2016	**Movements**
	RMB'000	RMB'000	
Revenue	**2,706,842**	3,466,544	**(21.9%)**
Gross profit	**1,084,368**	1,675,411	**(35.3%)**
(Loss)/profit for the year before fair value adjustment of biological assets	**(228,834)**	972,537	**(123.5%)**
(Loss)/profit for the year	**(824,313)**	956,808	**(186.2%)**
(Loss)/profit attributable to the owners of the parent	**(985,789)**	680,615	**(244.8%)**

In this announcement "**we**", "**us**" and "**our**" refer to the Company (as defined below) and where the context otherwise requires, the Group (as defined below).

Translated English names of Chinese natural persons, legal persons, governmental authorities, institutions or other entities for which no official English translation exists are unofficial translations for identification purpose only.

The board (the "**Board**") of directors (the "**Directors**") of China Shengmu Organic Milk Limited (the "**Company**" or "**China Shengmu**") hereby announces the consolidated financial results of the Company and its subsidiaries (the "**Group**" or "**Shengmu**") for the year ended December 31, 2017, together with the comparative figures for the year ended December 31, 2016.

CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

	Notes	**For the year ended December 31, 2017**	2016
		RMB'000	RMB'000
REVENUE	4	**2,706,842**	3,466,544
Cost of sales		**(1,622,474)**	(1,791,133)
Gross profit		**1,084,368**	1,675,411
Loss arising from changes in fair value less costs to sell of biological assets		**(595,479)**	(15,729)
Other income and losses	4	**(732,855)**	(87,146)
Selling and distribution expenses		**(317,400)**	(287,949)
Administrative expenses		**(102,487)**	(141,714)
Other expenses	6	**(10,595)**	(56,233)
Finance costs	7	**(150,531)**	(124,667)
Share of profits and losses of associates		**(6,874)**	(16,242)
(LOSS)/PROFIT BEFORE TAX	5	**(831,853)**	945,731
Income tax credit	8	**7,540**	11,077
(LOSS)/PROFIT FOR THE YEAR		**(824,313)**	956,808

CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME (CONTINUED)

	Notes	For the year ended December 31, 2017	2016
		RMB'000	RMB'000
OTHER COMPREHENSIVE INCOME			
Exchange differences on translation of foreign operations		**3,081**	12,158
Net other comprehensive income to be reclassified to profit or loss in subsequent periods		**3,081**	12,158
TOTAL COMPREHENSIVE (LOSS)/ INCOME FOR THE YEAR		**(821,232)**	968,966
(Loss)/profit attributable to:			
Owners of the parent		**(985,789)**	680,615
Non-controlling interests		**161,476**	276,193
		(824,313)	956,808
Total comprehensive (loss)/income attributable to:			
Owners of the parent		**(982,708)**	692,773
Non-controlling interests		**161,476**	276,193
		(821,232)	968,966
(Loss)/earnings per share attributable to ordinary equity holders of the parent:	10		
Basic		**(RMB0.155)**	RMB0.107
Diluted		**(RMB0.155)**	RMB0.106

CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Notes	As at December 31, 2017 RMB'000	December 31, 2016 RMB'000
NON-CURRENT ASSETS			
Property, plant and equipment		**2,798,328**	2,710,368
Prepaid land lease payments		**36,550**	37,566
Other intangible assets		**13,611**	14,847
Investments in associates		**105,784**	112,658
Available-for-sale investments		**2,007**	1,427
Biological assets	11	**3,867,389**	3,884,257
Prepayments for property, plant and equipment and biological assets		**6,209**	11,963
Long term receivables		**14,059**	19,684
Deferred tax assets		**32,197**	24,634
Other non-current assets		**39,212**	16,565
Total non-current assets		**6,915,346**	6,833,969
CURRENT ASSETS			
Inventories		**860,828**	928,816
Biological assets	11	**33,511**	—
Trade and bills receivables	12	**1,100,006**	1,108,787
Prepayments, deposits and other receivables		**898,837**	393,550
Pledged deposits		**128,884**	66,791
Available-for-sale investments		**—**	120,000
Cash and bank balances		**582,283**	1,047,382
Total current assets		**3,604,349**	3,665,326

CONSOLIDATED STATEMENT OF FINANCIAL POSITION (CONTINUED)

	Notes	**As at December 31, 2017**	As at December 31, 2016
		RMB'000	RMB'000
CURRENT LIABILITIES			
Trade and bills payables	13	**1,188,964**	920,631
Receipts in advance		**14,700**	13,152
Other payables and accruals		**441,718**	438,550
Interest-bearing bank and other borrowings		**2,654,046**	918,404
Income tax payable		**1,455**	1,581
Total current liabilities		**4,300,883**	2,292,318
NET CURRENT (LIABILITIES)/ASSETS		**(696,534)**	1,373,008
TOTAL ASSETS LESS CURRENT LIABILITIES		**6,218,812**	8,206,977
NON-CURRENT LIABILITIES			
Interest-bearing bank and other borrowings		**720,201**	1,751,950
Long term payables		**82,829**	107,900
Total non-current liabilities		**803,030**	1,859,850
Net assets		**5,415,782**	6,347,127
EQUITY			
Equity attributable to owners of the parent			
Share capital	14	**50**	50
Reserves		**4,356,281**	5,338,989
		4,356,331	5,339,039
Non-controlling interests		**1,059,451**	1,008,088
Total equity		**5,415,782**	6,347,127

CONSOLIDATED STATEMENT OF CASH FLOWS

	For the year ended December 31, 2017 RMB'000	2016 RMB'000
Net cash flows (used in)/from operating activities	**(113,158)**	942,225
Net cash flows used in investing activities	**(947,725)**	(1,233,968)
Net cash flows from/(used in) financing activities	**453,788**	(191,498)
NET DECREASE IN CASH AND CASH EQUIVALENTS	**(607,095)**	(483,241)
Cash and cash equivalents at beginning of year	**932,382**	1,411,499
Effect of foreign exchange rate changes, net	**(27,615)**	4,124
CASH AND CASH EQUIVALENTS AT END OF YEAR	**297,672**	932,382

NOTES

1. CORPORATE INFORMATION

The Company is an exempted company incorporated in the Cayman Islands with limited liability. The registered office address of the Company is P.O. Box 309, Ugland House, Grand Cayman, KY1-1104, Cayman Islands.

The Company is an investment holding company. During the year, the Company's subsidiaries were primarily engaged in the production and distribution of raw milk and dairy products in the People's Republic of China (the "**PRC**").

2. BASIS OF PREPARATION AND CHANGES TO THE GROUP'S ACCOUNTING POLICIES

Basis of Preparation

The financial statements have been prepared in accordance with International Financial Reporting Standards ("**IFRSs**") (which include all International Financial Report Standards, International Accounting standards ("**IASs**") and Interpretations) issued by the International Accounting Standards Board ("**IASB**") and the disclosure requirements of the Hong Kong Companies Ordinance. They have been prepared under the historical cost convention, except for certain biological assets and agricultural produce which have been measured at fair value less costs to sell. These financial statements are presented in Renminbi ("**RMB**") and all values are rounded to the nearest thousand except when otherwise indicated.

Basis of Consolidation

The consolidated financial statements include the financial statements of the Company and its subsidiaries for the year ended December 31, 2017.

The financial statements of the subsidiaries are prepared for the same reporting period as the Company, using consistent accounting policies. The results of subsidiaries are consolidated from the date on which the Group obtains control, and continue to be consolidated until the date that such control ceases.

2. BASIS OF PREPARATION AND CHANGES TO THE GROUP'S ACCOUNTING POLICIES (Continued)

Going concern

The Group had net current liabilities of RMB696,534,000 as at December 31, 2017 (2016: net current assets of RMB1,373,008,000). In view of the net current liabilities position, the board (the "**Board**") of directors (the "**Directors**") have given careful consideration to the future liquidity and performance of the Group and its available sources of finance in assessing whether the Group will have sufficient financial resources to continue as a going concern.

Having considered the unutilised banking facilities of RMB1,764,404,000 and unused credit facility of super short-term notes of RMB1,300,000,000 and unused credit facility of medium-term notes of RMB300,000,000 available as at December 31, 2017 and cash flow projections for the year ended December 31, 2018, the Directors are satisfied that the Group is able to meet in full its financial obligations as they fall due for the foreseeable future. To mitigate any liquidity issues that might be faced by the Group, the Group may curtail or defer its expansion plans based on the availability of sufficient funds. Accordingly, the Directors have prepared the consolidated financial statements on a going concern basis.

Should the Group be unable to continue in business as a going concern, adjustments would have to be made to restate the values of assets to their recoverable amounts, to provide for any further liabilities which might arise and to reclassify non-current assets as current assets. The financial statements do not include any adjustments that would result from the failure of the Group to continue in business as a going concern.

Changes in Accounting Policies and Disclosures

The Group has adopted the following revised IFRSs for the first time for the current year's financial statements.

Amendments to IAS 7	*Disclosure Initiative*
Amendments to IAS 12	*Recognition of Deferred Tax Assets for Unrealised Losses*
Amendments to IFRS 12 included in Annual Improvements to IFRSs 2014-2016 Cycle	Disclosure of Interests in Other Entities: Clarification of the Scope of IFRS 12

2. BASIS OF PREPARATION AND CHANGES TO THE GROUP'S ACCOUNTING POLICIES (Continued)

Changes in Accounting Policies and Disclosures (Continued)

The nature and the impact of the above amendments to IFRSs are described below:

(a) Amendments to IAS 7 require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes. The amendments have had no significant impact on the financial position and performance of the Group.

(b) Amendments to IAS 12 clarify that an entity, when assessing whether taxable profits will be available against which it can utilise a deductible temporary difference, needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference. Furthermore, the amendments provide guidance on how an entity should determine future taxable profits and explain the circumstances in which taxable profit may include the recovery of some assets for more than their carrying amount. The amendments have had no impact on the financial position and performance of the Group.

(c) Amendments to IFRS 12 clarify that the disclosure requirements in IFRS 12, other than those disclosure requirements in paragraphs B10 to B16 of IFRS 12, apply to an entity's interest in a subsidiary, a joint venture or an associate, or a portion of its interest in a joint venture or an associate that is classified as held for sale or included in a disposal group classified as held for sale. The amendments have had no impact on the Group's financial statements as none of the Group's subsidiaries were classified as a disposal group held for sale as at December 31, 2017 and so no additional information is required to be disclosed.

3. OPERATING SEGMENT INFORMATION

For management purposes, the Group is organised into business units based on their products and services and has two reportable operating segments as follows:

(a) Dairy farming — breeding dairy cows to produce and distribute raw milk; and

(b) Liquid milk products — producing and distributing self-owned brand ultra-heat treated liquid milk, organic yogurt and other dairy products.

Management monitors the results of the Group's operating segments separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on reportable segment profit/loss, which is a measure of adjusted profit/loss for the year. The adjusted profit/loss for the year is measured consistently with the Group's profit/loss after tax except that loss arising from fair value less costs to sell of biological assets is excluded from this measurement as management believes that such adjusted information is most relevant in evaluating the results of the dairy farming segment as compared to the results of other entities that operate within the dairy farming industry.

Segment assets exclude unallocated head office and corporate assets as these assets are managed on a group basis.

Segment liabilities exclude unallocated head office and corporate liabilities as these liabilities are managed on a group basis.

3. **OPERATING SEGMENT INFORMATION (Continued)**

Intersegment sales and transfers are transacted with references to the prices internally agreed between dairy farming segment and liquid milk products segment.

For the year ended December 31, 2017	**Dairy farming**	**Liquid milk products**	**Total**
	RMB'000	**RMB'000**	**RMB'000**
Segment revenue			
Sales to external customers	**1,279,190**	**1,427,652**	**2,706,842**
Intersegment sales	**1,223,040**	**11,520**	**1,234,560**
	2,502,230	**1,439,172**	**3,941,402**
Reconciliation:			
Elimination of intersegment sales			**(1,234,560)**
Revenue			**2,706,842**
Segment results	**847,088**	**(1,047,798)**	**(200,710)**
Reconciliation:			
Elimination of intersegment results			**13,737**
Loss arising from changes in fair value less costs to sell of biological assets			**(595,479)**
Corporate and other unallocated expenses			**(41,861)**
Loss for the year			**(824,313)**
As at December 31, 2017			
Segment assets	**9,993,243**	**2,437,525**	**12,430,768**
Reconciliation:			
Elimination of intersegment receivables			**(2,212,939)**
Corporate and other unallocated assets			**301,866**
Total assets			**10,519,695**
Segment liabilities	**4,250,247**	**2,741,230**	**6,991,477**
Reconciliation:			
Elimination of intersegment payables			**(2,212,939)**
Corporate and other unallocated liabilities			**325,375**
Total liabilities			**5,103,913**

3. **OPERATING SEGMENT INFORMATION (Continued)**

For the year ended December 31, 2016	Dairy farming	Liquid milk products	Total
	RMB'000	RMB'000	RMB'000
Segment revenue			
Sales to external customers	1,360,401	2,106,143	3,466,544
Intersegment sales	1,302,553	—	1,302,553
	2,662,954	2,106,143	4,769,097
Reconciliation:			
Elimination of intersegment sales			(1,302,553)
Revenue			3,466,544
Segment results	1,018,835	(5,145)	1,013,690
Reconciliation:			
Elimination of intersegment results			(25,995)
Loss arising from changes in fair value less costs to sell of biological assets			(15,729)
Corporate and other unallocated expenses			(15,158)
Profit for the year			956,808
As at December 31, 2016			
Segment assets	9,098,425	2,189,724	11,288,149
Reconciliation:			
Elimination of intersegment receivables			(919,698)
Corporate and other unallocated assets			130,844
Total assets			10,499,295
Segment liabilities	3,488,046	1,512,368	5,000,414
Reconciliation:			
Elimination of intersegment payables			(919,698)
Corporate and other unallocated liabilities			71,452
Total liabilities			4,152,168

4. REVENUE, OTHER INCOME AND LOSSES

Revenue represents the net invoiced value of goods sold, after allowances for returns and trade discounts.

An analysis of revenue, other income and losses is as follows:

	For the year ended December 31,	
	2017	2016
	RMB'000	RMB'000
Revenue		
– Sales of raw milk	**1,279,190**	1,360,401
– Sales of liquid milk products	**1,427,652**	2,106,143
	2,706,842	3,466,544
Other income and losses		
– Government grants	**312**	7,924
– Bank interest income	**8,739**	3,953
– Foreign exchange differences, net	**(27,967)**	(4,662)
– Loss on disposal of items of property, plant and equipment	**(2,402)**	(14,677)
– Impairment of trade receivables	**(656,054)**	(86,310)
– Impairment of milk powder	**(17,283)**	—
– Others	**(38,200)**	6,626
	(732,855)	(87,146)
	1,973,987	3,379,398

5. **(LOSS)/PROFIT BEFORE TAX**

The Group's (loss)/profit before tax is arrived at after charging/(crediting):

	For the year ended December 31,	
	2017	2016
	RMB'000	RMB'000
Cost of inventories sold	**1,622,474**	1,791,133
Loss arising from changes in fair value less costs to sell of biological assets	**595,479**	15,729
Depreciation of items of property, plant and equipment	**187,250**	146,783
Amortisation of prepaid land lease payments	**2,251**	266
Amortisation of other intangible assets	**1,395**	1,434
Research and development costs	**11,639**	11,662
Minimum lease payments under operating leases	**1,200**	1,200
Auditor's remuneration	**3,090**	2,700
Employee benefit expense (including directors' and chief executive's remuneration):		
Wages, salaries, bonuses and allowances	**248,363**	241,272
Other social insurances and benefits	**22,855**	27,411
Pension scheme contributions	**14,666**	11,506
Equity-settled share option expenses	**—**	45,151
	285,884	325,340

6. **OTHER EXPENSES**

The Group made donations with a total amount of RMB10,595,000 during the year of 2017 (2016: RMB56,233,000).

7. FINANCE COSTS

	For the year ended December 31,	
	2017	2016
	RMB'000	RMB'000
Interest on bank loans	**64,749**	61,373
Interest on short-term notes	**14,300**	5,730
Interest on corporate bonds	**77,052**	64,299
Interest on long term payables	**5,040**	6,157
Less: Interest capitalised	**(10,610)**	(12,892)
	150,531	124,667

8. INCOME TAX CREDIT

	For the year ended December 31,	
	2017	2016
	RMB'000	RMB'000
Current — PRC	**24**	12,481
Deferred	**(7,564)**	(23,558)
	(7,540)	(11,077)

9. DIVIDENDS

The directors do not recommend the payment of any dividend for the year ended December 31, 2017 (2016: Nil).

10. (LOSS)/EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT

The basic (loss)/earnings per share amount is calculated by dividing the (loss)/profit for the year attributable to ordinary equity holders of the Company, by the weighted average number of ordinary shares of 6,354,400,000 (2016: 6,354,400,000) in issue during the year.

The diluted (loss)/earnings per share amount is calculated by dividing the (loss)/profit for the year attributable to ordinary equity holders of the parent, by the weighted average number of ordinary shares used in the calculation of the basic (loss)/earnings per share calculation, and the weighted average number of ordinary shares assumed to have been issued at no consideration on the deemed exercise or conversion of all dilutive potential ordinary shares into ordinary shares.

The Group had no potentially dilutive ordinary shares in issue during the year of 2017 (2016: 57,439,740).

	Number of shares For the year ended December 31,	
	2017	2016
Weighted average number of ordinary shares in issue during the year used in the basic (loss)/earnings per share calculation	**6,354,400,000**	6,354,400,000
Effect of dilution of share options	**—**	57,439,740
Weighted average number of ordinary shares in issue during the year used in the diluted (loss)/earnings per share calculation	**6,354,400,000**	6,411,839,740

11. BIOLOGICAL ASSETS

The biological assets of the Group comprise primarily dairy cows held to produce raw milk and beef cattle raised for sale.

(A) Quantity of biological assets

The quantity of biological assets owned by the Group as at December 31, 2017 and December 31, 2016 is shown below. The Group's biological assets include heifers and calves, milkable cows, beef cattle. Heifers and calves are dairy cows that have not had their first calves. The Group's beef cattle are raised for sale.

11. **BIOLOGICAL ASSETS (Continued)**

(A) Quantity of biological assets (Continued)

	As at	
	December 31, 2017	December 31, 2016
	Head	Head
Dairy cows		
Heifers and calves	**51,383**	59,442
Milkable cows	**72,959**	69,887
Beef cattle	**7,675**	—
Total quantity of biological assets	**132,017**	129,329

(B) Value of biological assets

The value of Group's biological assets as at December 31, 2017 and 2016 is as follows:

	As at	
	December 31, 2017	December 31, 2016
	RMB'000	RMB'000
Dairy cows		
Heifers and calves	**1,146,523**	1,252,248
Milkable cows	**2,720,866**	2,632,009
Beef cattle	**33,511**	—
Total value of biological assets	**3,900,900**	3,884,257

The Group's biological assets in the PRC were independently valued by Jones Lang LaSalle Corporate Appraisal and Advisory Limited ("**JLL**"), a firm of independent professional qualified valuers not connected with the Group, which has appropriate qualifications and recent experience in the valuation of biological assets.

12. TRADE AND BILLS RECEIVABLES

	As at December 31, 2017 RMB'000	As at December 31, 2016 RMB'000
Trade and bills receivables	**1,840,492**	1,194,299
Impairment	**(740,486)**	(85,512)
	1,100,006	1,108,787

The Group normally allows a credit limit or offer to its customers credit terms which are adjustable in certain circumstances. The Group closely monitors overdue balances. In view of the aforementioned and the fact that the Group's trade receivables relate to a large number of diversified customers, there is no significant concentration of credit risk. The Group does not hold any collateral or other credit enhancements over its trade receivables. The trade and bills receivables are non-interest-bearing.

An aging analysis of the trade and bills receivables as at the end of the reporting period, based on the invoice date and net of provision, is as follows:

	As at December 31, 2017 RMB'000	As at December 31, 2016 RMB'000
Within 3 months	**550,907**	484,116
4 to 6 months	**269,445**	331,798
7 to 12 months	**272,596**	268,863
Over 1 year	**7,058**	24,010
	1,100,006	1,108,787

13. TRADE AND BILLS PAYABLES

An aging analysis of the trade payables of the Group, based on the invoice date, is as follows:

	As at	
	December 31, 2017	December 31, 2016
	RMB'000	RMB'000
1 to 3 months	**967,986**	895,338
4 to 6 months	**138,930**	14,790
7 to 12 months	**69,365**	5,120
1 to 2 years	**12,255**	3,297
2 to 3 years	**351**	2,086
Over 3 years	**77**	—
	1,188,964	920,631

14. ISSUED CAPITAL

The Company was incorporated in the Cayman Islands on December 11, 2013. As at December 31, 2017 and December 31, 2016, the Company has authorized share capital of HK$300,000, divided into 30,000,000,000 shares with a par value of HK$0.00001 each.

As at December 31, 2017 and December 31, 2016, the Company's share capital was HK$63,544 with 6,354,400,000 shares in issuance.

MANAGEMENT DISCUSSION AND ANALYSIS

MARKET OVERVIEW

With the improvement of people's income and living standard, consumers have higher standards on the healthiness, safety and nutrition of food. In particular, due to the heavily polluted environment and rising incidence of serious diseases, consumers have become increasingly concerned about food safety. By contrast with developed countries, organic food takes few shares in domestic market, representing a good opportunity as well as vast potential for the development of the industry.

This dairy products industry in the PRC is still in the stage of rapid development in view of its later start. In recent years, the increasing per capita income of the PRC has laid foundations for upgrading the consumption in this industry. The consumers' consumption custom about dairy products has gradually matured. The general consumption volume of dairy products in the PRC will maintain an increasing trend in the future years.

China's No.1 Central Document in 2017 specifies that the government shall guide companies to strive for international organic certification of agricultural products and improve the authority and influence of domestic green and organic certification. Given the rising popularity of nutritious and healthy food, the organic food sector is expected to be a "sunrise industry" in China.

On January 9, 2017, five ministries and commissions including the Ministry of Agriculture, the National Development and Reform Commission, the Ministry of Industry and Information Technology, the Ministry of Commerce, and China Food and Drug Administration jointly issued the "National Development Plan for Dairy Industry (2016-2020)" (《全國奶業發展規劃 (2016-2020年)》(the "**13th Five-Year Plan for Dairy Industry**"). The Plan explicitly states that it will accelerate the transforming of production model in the dairy industry and enhance integrated development of the dairy industry so that the dairy industry will make an obvious progress in the modernization and enter the global advanced ranks in its entirety by 2020.

Yu Kangzhen (于康震), vice minister of the Ministry of Agriculture, said that parties including the government, the associations and enterprises shall collaborate sufficiently with each other to proactively respond to and resolve the issue. First, "grow good forage", to enhance the supply of premium forage for dairy cows; second, "raise good cows", to enhance the standardized farming of scale for dairy cows; third, "produce premium milk", to improve the quality safety of dairy products; fourth, "procure integration", to enhance the integrated development of the dairy industry; and fifth, "strengthen promotion", to enhance the influence of China's dairy industry.

The dairy industry in the PRC is experiencing a special period of comprehensively transforming from a traditional industry to a modern one and from a weak industry to an efficient one. At such point of transforming and upgrading, the dairy industry in the PRC will certainly obtain trust in the wave of upgrading consumption and expand broader development space by grasping the trend of consumers' demand, providing high-value consumption experience, implementing deep layout of industry chain, and possessing capacity and strength to make the products differential against the backdrop of upgrading consumption.

BUSINESS REVIEW

China Shengmu is the largest organic dairy company in the PRC in terms of the herd size of organic dairy cows and the production volume of organic raw milk for the year ended December 31, 2017. China Shengmu is the only vertically integrated grass-to-glass organic dairy company in the PRC that meets the E.U. organic standards. It is also the only dairy company in the PRC that offers branded organic dairy products that are 100% processed from raw milk produced by self-owned certified organic dairy farms and the only sizeable dairy company in the PRC to operate the "desert-based grass-to-glass organic production model"(沙漠全程有機產業體系). Starting with the selection of milk sources, Shengmu has created a grass-to-glass organic production model from forage planting to herd farming, then to product processing and finally to market for sales. It has created the first complete desert-based revolving industry chain for organic milk in the world. The entire five processes including organic environment, organic planting, organic farming, organic processing, and organic market are all controllable and form Shengmu's unique complete revolving organic ecological circle.

In response to the rising competition in the dairy market, the Group established a development strategy of "brand upgrade, price stabilization, channel expansion and innovative development", under which, the Group heightened the expansion of new channels while focusing on the key markets for efficient operation. In 2017, the revenue of the Group amounted to RMB2,706.8 million and its gross profit amounted to RMB1,084.4 million, of which the revenue of grass-to-glass organic liquid milk under its self-owned brand amounted to RMB1,400.3 million, accounting for 51.8% of the total revenue of the Group.

In 2017, the Group has determined to carry out its new strategic approach, which delivered an excellent brand image, market recognition and reputation of "Shengmu" brand among consumers, paving a solid foundation for the Group to "battle 2018". The employees in China Shengmu are confident in the future development prospects.

Stabilize Price, Expand Channels, Explore New Marketing Models, and Create High-end Brand

Despite the fierce market competition in 2017, China Shengmu explicitly defined its market position as a supplier of high-end and premium products with high value. Being committed to maintaining a good brand image, the Group has proactively optimized its product structure and improved the price of its end products.

For the development of channels, the Group continued to give strong support to its distributors and sub-distributors. A modern supermarket (stores in class A) channel plan has been implemented in the national market. By the end of 2017, its products have been introduced to approximately 4,300 modern supermarkets, with Shengmu organic liquid milk products covering various large-scale chain supermarkets, such as RT-Mart and Auchan. On the other hand, under the "blue ocean" channel strategy, the Group has established 120,000 super-community stores, which were categorized into class B and class C and each under separate management. These super community stores enabled the Group to narrow its distance with consumers and be close to the people's life.

The Group made great progress in the field of e-commerce, which achieved 100% sales growth in 2017. By immediately following the development trend of e-commerce, the proportion of Shengmu organic milk's sales through the channel of e-commerce has increased in a stable way, currently outperforming its peers. In July 2017, China Shengmu and Suning Commerce Group Co., Ltd. signed a strategic cooperative agreement by which Shengmu officially participated in the Suning 818 shopping gala. During the year, Shengmu has established a proprietary farm for Suning whose members are specially provided with dairy products produced from such farm. Thus, Suning has become the first e-commerce platform owning a proprietary farm. Moreover, China Shengmu and Suning will cooperate deeply in many aspects such as marketing resources, brand reactivity and diversified cooperation. They will also cooperate in public welfare. They plan to carry out a crowdfunding activity to green desert through purchasing of Shengmu's products together with "11 Sunning" activity of Suning. The upgraded cooperation between China Shengmu and Suning aims to meet consumers' demands and produce organic milk beneficial for the health of people.

In 2017, China Shengmu started cooperation with Yunji, an emerging e-commerce company, and made remarkable achievements. With the established platform of Yunji, the largest and leading social marketing enterprise in China, Shengmu interacted with its customers through diversified marketing activities and invited popular on-line shop-owners to visit its industrial chain base, which, unlike the traditional sales channels, impressed the wide consumers greatly. An aggregate revenue of RMB100 million was recorded through Yunji in 2017.

In respect of special sales activities, China Shengmu and Easy Joy at gas stations of Sinopec have cooperated in 2017 and achieved excellent performance during the year. Various promotion and marketing activities were organized and attracted over two million fans. Such frequent promotion and marketing activities increase the number of re-purchases and effectively boosted product sales.

Creating a Green GDP Model to Control Desertification by "Industry" is beneficial to the Country and the People and has Won Recognition among Professionals at Home and Abroad

Shengmu has established a complete revolving organic ecological circle in the hinterland of Ulan Buh Desert through unremitting efforts for many years, providing a new sample and creating a new model for desertification control. Shengmu has planted tens of millions of sandy trees in Ulan Buh Desert and made desert reclamation of over 400,000 mu. In the future, pursuing a model of desert control through industry development, the Group will prevent and control desertification while developing its business, aiming to turn a desert of 1,000 square kilometers into oasis during the course of creating a global-leading organic dairy brand.

In 2017, Shengmu put more efforts in organizing the special mega-event "Shengmu Desert Organic Journey". The number of visitors increased by nearly one time compared with that of 2016. Shengmu invited numbers of consumers from all over the country to visit Ulan Buh Desert and the organic farm base and experience the mode of desert control through organic industry development, enabling them to understand the safety of Shengmu's products, so as to enhance the reputation and brand awareness of Shengmu.

Shengmu's grass-to-glass organic liquid milk products have received wide recognition and popularity. In the BIOFACH CHINA Organic Trade Fair (中國國際有機食品博覽會) held in May 2017, China Shengmu was awarded Gold Medal jointly by the China Green Food Development Center (中國綠色食品發展中心) and the NürnbergMesse Group for the seventh time. And at the 18th China Green Food Exposition in August 2017, Shengmu's grass-to-glass organic milk won the gold prize due to its "zero pollution", "zero addition" and "complete nature".

"Organic" Dairy Farms, Adhere to Sustainable Development and Produce Premium Milk in the Desert

Premium milk derives from good planting. Starting with the source, Shengmu has created a grass-to-glass organic production model from grass-planing to dairy-farming, then to dairy-processing, and finally to the dining tables of consumers.

Farming Business

In order to establish safe base for milk sources, organic dairy farms are essential. The Ulan Buh Desert is a natural isolation area free from epidemics, and the sand beds in the desert provide dairy cows with comfortable living conditions. Sufficient sunlight provides guarantee for dairy cows' synthesis of calcium. Free sand baths make every dairy cow own lustrous and shiny fur. Bright sands can prevent dairy cows from suffering from mastitis. High comfort can allow dairy cows to produce healthy milk.

Shengmu owns 23 organic dairy farms. With sufficient living space of an average of 60 square meters for each cow, standard nutrition formulation management and professional healthcare system, as well as the unique environmental system, all dairy cows can enjoy cozy living conditions. Advanced facilities and standard milking process ensure high quality raw milk with better nutritive and hygienic index than its peers. Besides, established quality tracking system is also in place, with unique identity code on the ear of each cow, which ensures that the entire process can be traceable.

Herd Size and Production

As at December 31, 2017, the Group had 23 organic dairy farms in operation, and 12 non-organic farms in operation. The organic and non-organic herd size of the Group have changed from 94,815 and 34,514 dairy cows as at December 31, 2016 to 95,181 and 29,161 dairy cows as at December 31, 2017, respectively.

	As at December 31,									
	2017					2016				
	Number of dairy farms	**Calves and heifers**	**Milkable cows**	**Beef cattle**	**Subtotal**	Number of dairy farms	Calves and heifers	Milkable cows	Beef cattle	Subtotal
Organic	**23**	**41,247**	**53,934**	**6,944**	**102,125**	23	45,534	49,281	—	94,815
Non-organic	**12**	**10,136**	**19,025**	**731**	**29,892**	12	13,908	20,606	—	34,514
Total	**35**	**51,383**	**72,959**	**7,675**	**132,017**	35	59,442	69,887	—	129,329

The Group produced 452,857 tonnes of organic raw milk and 156,328 tonnes of premium non-organic raw milk in 2017, and produced 421,023 tonnes of organic raw milk and 177,356 tonnes of premium non-organic raw milk in 2016.

Organic Forage Planting

Forage is an essential raw material in organic dairy farming. Pursuant to a long-term strategic cooperation agreement entered into with us, Shengmu Forage continues to supply organic forage to us. Currently, Shengmu Forage owns developed grassland of over 200,000 mu. Abundant organic manure from organic farming and mature management model for standard organic planting facilitate alfalfa and corn planting in the desert.

Legume forage, such as medicago, can facilitate effective circulation of substances. A large number of creatures living in the soil under a corn can increase organic matter of the soil and prevent the soil from hardening. Corn's abundant roots can fix surface soil to avoid loss of topsoil and enhance soil's capability to keep water and fertility. Therefore, a sustainable green ecological cycle is formed. As a portion of the cycle, quality organic forage improves the quality of dairy, thus playing a key rule in the process of dairy farming in organic dairy farms.

Liquid Milk Business

All the raw milk of Shengmu used to produce self-owned brand grass-to-glass organic liquid milk is resourced from self-owned organic dairy farms of Shengmu. The Group has invested heavily to construct world-leading A3 aseptic filling equipment imported from Sweden. At the same time, it introduced the most advanced Tetra Pak production system worldwide to follow the processing flow of organic milk, which has no chemical additives such as preservatives, colorants, etc. and thus is natural and healthy. Every bag of the organic milk is stamped with spray code, the organic traceability code authorized by CNCA.

The formation of comprehensive organic milk model by Shengmu also marks the progress made in industrial technology capability in dairy industry in China, which effectively promoted the supply capability of domestic organic dairy products, satisfied the needs of Chinese people for high-quality diary milk, embarked on a new milestone of domestic grass-to-glass organic traceable liquid milk, and improved the product quality in the industry and market competitiveness, thus enabling dairy industry to achieve sustainability in a real sense.

There is an aggregate of 16 production lines of liquid milk operated by the Group during the year, and the production volume of organic liquid milk products under its self-owned brand which were entirely processed from raw milk produced by self-owned certified organic dairy farms stood at 151,070 tonnes as compared to 197,276 tonnes for the year of 2016.

FINANCIAL REVIEW

In 2017, the Group's revenue decreased by 21.9% from RMB3,466.5 million in 2016 to RMB2,706.8 million. Gross profit of the Group decreased by 35.3% from RMB1,675.4 million in 2016 to RMB1,084.4 million in 2017. (Loss)/profit attributable to owners of the parent decreased by 244.8% from profit attributable to owners of the parent of RMB680.6 million in 2016 to loss attributable to owners of the parent of RMB985.8 million in 2017.

Analysis on Consolidated Statement of Profit or Loss and Other Comprehensive Income

Revenue

Unit: RMB in thousands, except percentages

	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
2017	**2,502,230**	**1,223,040**	**1,279,190**	**47.3%**	**1,439,172**	**11,520**	**1,427,652**	**52.7%**	**2,706,842**
2016	2,662,954	1,302,553	1,360,401	39.2%	2,106,143	—	2,106,143	60.8%	3,466,544

(1) Represents self-produced raw milk sold to the Group's liquid milk business.

Given the rising competition existing in the dairy market, the Group required the market terminals to stabilize prices globally to improve the brand image of Shengmu. In 2017, the sales volume of the Group's own organic liquid milk products decreased by approximately 21.7%. Meanwhile, the Group strengthened its support to distributors and sub-distributors by reducing the price of liquid milk products moderately. The revenue of the Group's own organic liquid milk products in 2017 was affected by the price stabilization actions of the Group, and amounted to RMB1,400.3 million, representing a decrease of approximately 31.8% against 2016. Further, the selling price of raw milk in 2017 significantly decreased against last year due to market competition, which was another main reason for the decrease in the Group's revenue against 2016.

Dairy Farming Business

	For the year ended December 31,							
	2017				2016			
	Revenue (RMB'000)	**Sales volume (Tonnes)**	**Average selling price (RMB/ Tonne)**	**Revenue as % of dairy farming segment revenue**	Revenue (RMB'000)	Sales volume (Tonnes)	Average selling price (RMB/ Tonne)	Revenue as % of dairy farming segment revenue
Organic raw milk								
External sales	**815,492**	**211,027**	**3,864**	**32.6%**	784,631	166,986	4,699	29.5%
Inter-segment sales(1)	**1,167,334**	**222,755**	**5,240**	**46.6%**	1,222,020	228,761	5,342	45.9%
Subtotal	**1,982,826**	**433,782**	**4,571**	**79.2%**	2,006,651	395,747	5,071	75.4%
Premium non-organic raw milk								
External sales	**463,698**	**137,412**	**3,375**	**18.6%**	575,770	156,455	3,680	21.6%
Inter-segment sales(2)	**55,706**	**14,736**	**3,780**	**2.2%**	80,533	18,765	4,292	3.0%
Subtotal	**519,404**	**152,148**	**3,414**	**20.8%**	656,303	175,220	3,746	24.6%
Dairy farming segment	**2,502,230**	**585,930**	**4,271**	**100.0%**	2,662,954	570,967	4,664	100.0%

(1) Represents self-produced organic raw milk sold to the Group's organic liquid milk business.

(2) Represents self-produced premium non-organic raw milk sold to the Group's high-end non-organic liquid milk business.

In 2017, total sales volume of the Group's raw milk increased slightly relative to 2016. However, affected by the current condition of domestic dairy industry, the selling price of raw milk dropped significantly relative to 2016, which led to a decrease in revenue from the dairy farming segment from RMB2,663.0 million in 2016 to RMB2,502.2 million in 2017. The inter-segment sales volume to organic liquid milk processing plant maintained a high proportion over the total sales volume of organic raw milk, enabling the Group to develop the dairy farming business in a sustainable manner through the development, construction and consolidation of the market of its own liquid dairy products from "grass-to-glass organic production model" amid the prolonged "chill" of the dairy industry.

Liquid milk business

In 2017, affected by the increase in price of the market terminals, the sales in the market decreased significantly and revenue from liquid milk business of the Group decreased by 32.2% from RMB2,106.1 million in 2016 to RMB1,427.7 million. Revenue from liquid milk business maintained at a high level in 2017, accounting for 52.7% of total revenue of the Group. In addition, revenue from organic business (comprising organic raw milk business and organic liquid milk business) accounted for 81.9% of total revenue of the Group in 2017.

Organic liquid milk business

	For the year ended December 31,		
	2017	2016	Decrease
Revenue (RMB'000)	**1,400,277**	2,054,292	(31.8%)
Sales volume (Tonnes)	**145,949**	186,393	(21.7%)
Average selling price (RMB/Tonne)	**9,594**	11,021	(12.9%)

Revenue From Organic/Non-Organic Business And Percentages

Unit: RMB in thousands, except percentages

	For the year ended December 31,			
	2017		2016	
	Amount	**Percentage**	Amount	Percentage
Organic products				
Organic liquid milk	**1,400,277**	**51.8%**	2,054,292	59.3%
Organic raw milk	**815,492**	**30.1%**	784,631	22.6%
Subtotal of organic products	**2,215,769**	**81.9%**	2,838,923	81.9%
Non-organic products				
Premium non-organic raw milk	**463,698**	**17.1%**	575,770	16.6%
High-end non-organic liquid milk	**27,375**	**1.0%**	51,851	1.5%
Subtotal of non-organic products	**491,073**	**18.1%**	627,621	18.1%
Total	**2,706,842**	**100.0%**	3,466,544	100.0%

Cost of Sales, Gross Profit and Gross Margin

	For the year ended December 31,					
	2017			2016		
	Cost of sales Amount	**Gross profit Amount**	**Gross margin**	Cost of sales Amount	Gross profit Amount	Gross margin
	(RMB in thousands, except percentages)					
Dairy farming business						
Organic raw milk						
Before elimination	**1,056,926**	**925,900**	**46.7%**	965,276	1,041,375	51.9%
After elimination(1)	**513,155**	**302,337**	**37.1%**	407,299	377,332	48.1%
Premium non-organic raw milk						
Before elimination	**375,463**	**143,941**	**27.7%**	434,862	221,441	33.7%
After elimination(3)	**338,055**	**125,643**	**27.1%**	388,292	187,478	32.6%
Subtotal of dairy farming business						
Before elimination	**1,432,389**	**1,069,841**	**42.8%**	1,400,138	1,262,816	47.4%
After elimination	**851,210**	**427,980**	**33.5%**	795,591	564,810	41.5%
Liquid milk business						
Organic liquid milk business						
Before elimination	**1,287,657**	**124,140**	**8.8%**	1,615,850	438,442	21.3%
After elimination(2)	**748,783**	**651,494**	**46.5%**	969,298	1,084,994	52.8%
High-end non-organic liquid milk business						
Before elimination	**27,552**	**(177)**	**(0.6%)**	51,702	149	0.3%
After elimination(3)	**22,481**	**4,894**	**17.9%**	26,244	25,607	49.4%
Subtotal of liquid milk business						
Before elimination	**1,315,209**	**123,963**	**8.6%**	1,667,552	438,591	20.8%
After elimination	**771,264**	**656,388**	**46.0%**	995,542	1,110,601	52.7%
Total	**1,622,474**	**1,084,368**	**40.1%**	1,791,133	1,675,411	48.3%

(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 plus (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 arrived at by calculating 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.

(3) Premium non-organic raw milk after elimination is calculated using the formula in note (1) above, and the premium non-organic liquid milk after elimination is calculated using the formula in note (2) above.

Cost of sales of the Group decreased from RMB1,791.1 million in 2016 to RMB1,622.5 million in 2017. Gross profit decreased from RMB1,675.4 million in 2016 to RMB1,084.4 million in 2017. Gross profit margin decreased from 48.3% in 2016 to 40.1% in 2017.

Cost of sales of the Group decreased by 9.4% in 2017 against 2016. Such decrease in cost of sales was mainly attributable to reduced sales volume of the Group. Gross profit of the Group decreased by 35.3% in 2017 against 2016, higher than the decrease of revenue of the Group, primarily because (1) the Group required the market terminals to stabilize prices globally to improve the brand image of Shengmu, given the rising competition existing in the dairy market. In 2017, the Group's own organic liquid milk products decreased significantly in sales volume; (2) the Group increased its support to distributors and sub-distributors by reducing the price of liquid milk products appropriately in 2017; and (3) the significant decrease in the production of organic liquid milk products in 2017 against 2016 led to a higher unit price of the organic liquid milk products than 2016.

Overall, against the backdrop of unfavourable conditions of and fierce competition in the dairy industry, the Group's overall gross margin declined significantly, while gross margin of the organic business on the whole remained high.

Other Income and Losses

Other income and losses of the Group increased from RMB87.1 million in 2016 to RMB732.9 million in 2017, mainly attributable to the provision for impairment of trade receivables referring to the recoverability of individual account receivables and aging analysis by the Group.

Selling and Distribution Expenses

Selling and distribution expenses of the Group primarily include logistics and transportation expenses, warehouse fees and relevant employees' remunerations. In 2017 and 2016, selling and distribution expenses of the Group amounted to RMB317.4 million and RMB287.9 million, accounting for 11.7% and 8.3% of revenue, respectively. The much higher cost of sales to revenue ratio against last year was mainly attributable to the significant decrease in revenue in 2017 relative to 2016 and the Group's stronger support to the promotion expenses incurred by the distributors and sub-distributor.

Administrative Expenses

Administrative expenses mainly include salary and welfare, travel expenses and transportation expenses of management and administrative employees. In 2017 and 2016, administrative expenses of the Group were RMB102.5 million and RMB141.7 million, accounting for 3.8% and 4.1% of revenue, respectively. The lower administrative expense to revenue ratio in 2017 against 2016 was mainly due to the equity-settled share option expense included in the administrative expenses in 2016. Excluding this, administrative expenses in 2017 and 2016 accounted for 3.8% and 2.8% of revenue respectively. Such higher ratio was mainly attributable to the significant decrease in revenue in 2017 against 2016.

Losses Arising from Changes in Fair Value Less Cost of Sales of Biological Assets

Losses arising from changes in fair value less cost of sales of biological assets represents fair value changes in the dairy cows, due to the changes in physical attributes and market prices of the dairy cows 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 milkable cow is higher than the selling price of heifer. Further, when a milkable cow is ousted and sold, its value decreases.

In 2017 and 2016, the Group recorded losses arising from changes in fair value less cost of sales of biological assets of RMB595.5 million and RMB15.7 million. The significant increase in losses arising from changes in fair value less cost of sales of biological assets in 2017 against 2016 was mainly attributable to the facts that (i) the Group controlled the numbers of its dairy cows, given the weak demand of raw milk in the market; and (ii) the price of raw milk dropped.

Share of Profits and Losses of Associates

The Group's associates include (a) the companies that were jointly established by the Group and its premium distributors in its key distribution cities to distribute the liquid milk products with the Group's self-owned brand; (b) Bayannur Shengmu High-tech Ecological Forage Co., Ltd. (巴彥淖爾市聖牧高科生態草業有限公司) and its subsidiary ("**Shengmu Forage**") in which the Group invested and held minority interests; and (c) Food Union Shengmu and Inner Mongolia Shengmu Low Temperature Dairy Product Company Limited (內蒙古聖牧低溫乳品有限公司) in which the Group invested and held minority interests and which produces dairy products with the raw milk to be purchased by it from the Group. In 2017 and 2016, the Group recorded share of losses of associates of RMB6.9 million and RMB16.2 million respectively.

Income Tax Credit

All profits of the Group were derived from its operations in the PRC. According to the Enterprise Income Tax Law of the PRC (the "**EIT Law**"), the Group's subsidiaries in the PRC are generally subject to a corporate income tax at a rate of 25%. According to the preferential provisions of the EIT Law, the Group's income arising from agricultural activities, such as dairy farming and processing of raw agricultural products, is exempted from enterprise income tax. Under the PRC tax laws and regulations, there is no statutory time limit for such tax exemption as long as the relevant PRC subsidiaries of the Group complete filings with the relevant tax authorities as required.

In accordance with "The Notice of Tax Policies Relating to the Implementation of the Western China Development Strategy" jointly issued by Ministry of Finance, General Administration of Customs and State Administration of Taxation (Cai Shui [2011] No.58) (財政部、海關總署、國家税務總局《關於深入實施西部大開發戰略有關税收政策問題的通知》 (財税[2011]58號)), the Group's taxable income arising from processing of non-raw agricultural products is subject to preferential tax rate of 15% from 2013 to 2020.

Income tax credit of the Group was RMB7.5 million and RMB11.1 million in 2017 and 2016 respectively. Income tax credit of the Group in 2017 was due to the provision of deferred income tax assets for net loss of the liquid milk business and unrealised profit or loss from internal sales.

(Loss)/Profit Attributable to Owners of the Parent and Profit Attributable to Non-Controlling Interests

Profit attributable to non-controlling interests mainly represents the profit attributable to the non-controlling interests in the Group's dairy farms held by the dairy farmers with whom we cooperate in relation to dairy farm management. In 2017, loss attributable to owners of the parent was RMB985.8 million, compared with profit attributable to owners of the parent of RMB680.6 million in 2016. Profit attributable to non-controlling interests in 2017 and 2016 was RMB161.5 million and RMB276.2 million respectively.

(Loss)/profit attributable to owners of the parent in 2017 decreased greatly as compared to 2016 and recorded a substantial loss, which was mainly due to the following reasons: (1) pursuant to the provision policy for asset impairment established by the Group based on its actual production and operation conditions, the Group determined the receivable group by using aging as a credit risk characteristic and, by aging analysis, made provisions for bad debts in respect of account and other receivables, and also estimated the provisions for asset impairment with reference to the recoverability of individual account receivables and customer creditworthiness on a prudent basis, which was RMB657.3 million in 2017; (2) affected by ① the Group's control over the number of dairy cows in response to week demand for raw milk in the market; and ② drop of the price of raw milk, changes in the Group's fair value less cost of sales of biological assets recorded a great loss of RMB595.5 million in 2017; and (3) due to intensified competition in domestic dairy market, both sales volume and selling price of the Group's own liquid milk products decreased greatly against last year, and the average price of raw milk also recorded a large decline against last year.

Analysis On Consolidated Statement Of Financial Position

Current Assets

As at December 31, 2017, the total current assets of the Group were RMB3,604.3 million (RMB3,665.3 million as at December 31, 2016), primarily consisting of inventories of RMB860.8 million (RMB928.8 million as at December 31, 2016), biological assets of RMB33.5 million, trade and bills receivables of RMB1,100.0 million (RMB1,108.7 million as at December 31, 2016), prepayments, deposits and other receivables of RMB898.8 million (RMB393.6 million as at December 31, 2016) and cash and bank balances, available for sale investments and pledged deposits of RMB711.2 million (RMB1,234.2 million as at December 31, 2016).

Trade and Bills Receivable

Unit: RMB in thousands, except percentages

	As at	
	December 31, 2017	December 31, 2016
Trade and bills receivables	**1,840,492**	1,194,299
Impairment	**(740,486)**	(85,512)
Total	**1,100,006**	1,108,787

	As at			
Aging	**December 31, 2017**		December 31, 2016	
	Amount	**Percentage**	Amount	Percentage
Within 6 months	**820,352**	**74.6%**	815,914	73.6%
7 to 12 months	**272,596**	**24.8%**	268,863	24.2%
Over 1 year	**7,058**	**0.6%**	24,010	2.2%
Total	**1,100,006**	**100.0%**	1,108,787	100.0%

Original value of trade and bills receivables of the Group increased substantially against last year, mainly attributable to the Group's stronger support to the sales of the self-owned brand liquid milk products, taking into consideration the recovery days of the receivables from terminal supermarkets and department stores and aiming to increase and consolidate its share in organic liquid milk market.

Pursuant to the provision policy for asset impairment established by the Group based on its actual production and operation conditions, the Group determined the receivable group by using aging as a credit risk characteristic and, by aging analysis, made provisions for bad debts in respect of account and other receivables, and also estimated the provisions for asset impairment with reference to the recoverability of individual account receivables and customer creditworthiness. In 2017, the Group made a total provision of RMB657.3 million for the impairment of account receivables.

Current Liabilities

As at December 31, 2017, total current liabilities of the Group amounted to RMB4,300.9 million (RMB2,292.3 million as at December 31, 2016), primarily consisting of trade and bills payables of RMB1,189.0 million (RMB920.6 million as at December 31, 2016), receipts in advance of RMB14.7 million (RMB13.2 million as at December 31, 2016), other payables and accruals of RMB441.7 million (RMB438.5 million as at December 31, 2016), interest-bearing bank and other borrowings of RMB2,654.0 million (RMB918.4 million as at December 31, 2016), and income tax payable of RMB1.5 million (RMB1.6 million as at December 31, 2016). The large increase in current liabilities as at December 31, 2017 relative to December 31, 2016 was mainly because the rights attached to the corporate bonds in a principal of RMB1,000.0 million issued by the Group on cum-right basis in 2015 may be exercised by the creditors by the end of the third year (i.e. end of 2018), such corporate bonds were accounted as non-current liabilities due within one year. Besides, the Group issued super short-term notes in a principal of RMB400.0 million in 2017.

Non-Current Liabilities

As at December 31, 2017, the total non-current liabilities of the Group amounted to RMB803.0 million (RMB1,859.9 million as at December 31, 2016), primarily consisting of interest-bearing bank and other borrowings of RMB720.2 million (RMB1,752.0 million as at December 31, 2016) and long-term payables of RMB82.8 million (RMB107.9 million as at December 31, 2016).

Foreign Exchange Risk

The Group's businesses are principally located in the mainland China and substantially all transactions are conducted in RMB. As at December 31, 2017, the Group did not have significant foreign currency exposure from its operations, except interest-bearing bank borrowings equivalent to approximately RMB322.9 million which were denominated in Euros, bank balances equivalent to approximately RMB5.4 million, RMB174.9 million and RMB4.5 million which were denominated in Hong Kong dollars, United States dollars and Euro, respectively. In 2017, the Group did not enter into any arrangements to hedge against any fluctuation in foreign exchange.

Credit Risk

The Group only trades with recognized and creditworthy third parties. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures. As the Group's trade receivables relate to a large number of diversified customers, there is no significant concentration of credit risk. Since the Group trades only with recognized and creditworthy third parties, collateral is generally not required.

Charge on Assets

As at December 31, 2017, the Group had pledged deposits of approximately RMB128.9 million (RMB66.8 million as at December 31, 2016) to banks in the PRC as deposits for the issuance of letters of credit and bank drafts.

Liquidity, Financial Resources and Capital Structure

In 2017, the Group financed its daily operations mainly from internally generated cash flows and bank and other borrowings. As at December 31, 2017, the Group had (a) cash and bank balances of RMB582.3 million (RMB1,047.4 million as at December 31, 2016), and (b) interest-bearing bank and other borrowings of RMB3,374.2 million (RMB2,670.4 million as at December 31, 2016), of which, RMB656.7 million were repayable within one to five years and RMB63.5 million repayable within five to eight years, while the remaining interest-bearing bank and other borrowings were repayable within one year. The gearing ratio (calculated as total debt (total interest-bearing bank and other borrowings) divided by total equity) was 62.3% as at December 31, 2017 (42.1% as at December 31, 2016). Except bank and other borrowings equivalent to RMB322.9 million which are denominated in Euros and bear fixed interest rates, the Group's remaining bank and other borrowings are denominated in RMB and bear fixed interest rates. In 2017, the annual interest rate of bank and other borrowings was 1.55% to 6.98% (2016: 1.55% to 5.87%).

Environmental Policies and Performance

The Group's operations were in compliance in all material respects with currently applicable national and local environmental protection laws and regulations in the PRC in 2017.

Capital Commitments

As at December 31, 2017, the Group's capital commitments amounted to RMB214.6 million (RMB352.6 million as at December 31, 2016). The Group has sufficient internal and financial resources to fund its capital expenditures.

HUMAN RESOURCES

As at December 31, 2017, the Group had a total of 3,803 employees (3,849 employees as at December 31, 2016). Total staff costs in 2017 (including the emoluments of Directors and senior management of the Company) amounted to RMB285.9 million (excluding equity-settled share option expenses) (RMB280.2 million in 2016).

The Group believes that the dedicated efforts of all of its employees are the very essence of the Group's rapid development and success in the future. The Group provides management personnel and employees with on-the-job education, training and other opportunities to improve their skills and knowledge. In general, the Group determines employee compensation based on each employee's performance, qualifications, position and seniority. The Group has made contributions to the social security funds and housing reserve for its employees in accordance with the relevant national and local social welfare laws and regulations.

The Group has also approved and adopted a pre-IPO share option scheme (the "**Pre-IPO Share Option Scheme**") and a share option scheme (the "**Share Option Scheme**"). The purpose of the Pre-IPO Share Option Scheme and the Share Option Scheme is to attract, retain and motivate the Directors, senior management and employees of the Group and other participants.

Contingent Liabilities

As at December 31, 2017, the Group provided guarantees with amount of RMB160,000,000 (2016: RMB300,000,000) and RMB102,880,000 (2016: RMB51,450,000) for the bank borrowings of Shengmu Forage and Food Union Shengmu, respectively.

Material Acquisitions And Disposals

The Company did not make any material acquisitions and disposals of subsidiaries and associated companies in 2017.

Future Plans For Material Investments Or Acquisition Of Capital Assets And Expected Source Of Funding

Save as disclosed above in connection with capital commitments under the paragraph headed "Capital Commitments" and in the prospectus under the section headed "Future Plans and Use of Proceeds", the Group does not have any plan for material investments or acquisition of capital assets as at the date of this announcement.

OUTLOOK

The Group's long-term objective is to become a leading organic dairy company in the world.

Build Garden-like Organic Dairy Farms to Produce Milk of Best-Quality

The Group endeavors to build world-class comfortable garden-like organic dairy farms, so as to further improve the herd growing environment and staff working environment and the whole environment of the dairy farms, striking to provide the organic dairy cows in the desert with the best living welfare, and turn them into "happy cows and healthy cows", thus ensuring the producing of milk with best quality.

Increase Investment in Research and Development to Improve Research and Development Capability

For the purpose of improving its research and development ability, the Group proactively explores the establishment of a diversified investment mechanism for research and development. Next, the Group will establish Shengmu Research Institute (聖牧研究院) in cooperation with international and domestic leading scientific research institutes and agricultural colleges, and increase investment in research and development to improve its research and development capability in developing new products and technologies leading the market.

Improve Business Capability of Its Partners

The Group cannot make success without the success of its partners. In 2018, the Group will bring its partners into the group cadre echelon by establishing the Partner Training Institute (事業夥伴培訓學院) and providing them opportunities to study in Tsinghua University and Zhejiang University systematically, aiming to improve their business capability in the aspects of business skills, operating management and entrepreneurship, and build a well disciplined partner team with great mission and vision and strong capability.

Strengthen Brand Building

Brand is deemed as the most valuable wealth of Shengmu organic milk undertakings. In 2018, the Group will continue to firmly build brand awareness through the following three aspects: (1) delivering Shengmu's commitments to top quality, high-end position and ecological welfare to consumers in an omnibearing three-dimensional manner; (2) believing that the Ulan Buh Desert is the best billboard, and bringing the desert scenario to the market and consumers to desert and Shengmu's organic base; and (3) designing and implementing shopping guides, KA counters and display environment in favor of brand image building, so as to fully enhance the brand image of Shengmu.

Intensify Hit Products and Exploit Innovative Channels

In 2018, the Group will carry out all-around product planning, optimize product structure, and upgrade product quality and package. Besides, the Group will mainly engaged in hit products such as gift pack, business pack and children's pack both online and offline. Meanwhile, the Group will exploit innovative sales channels by focusing on the development of new mode channels such as supermarkets and department stores.

Root the Concept of "Great 2B" in Mind

By fully consolidating superior resources, the Group will share its organic achievements with platform such as Tmall, JD.COM, Suning.com, Yunji, as well as enterprises such as PetroChina, Starbucks, Holiland and Xibei, etc. in the form of strategic cooperation and customizing exclusive products flexibly.

Establish "Base" Market to Realize Market Transformation Quickly

In 2018, the Group will centralize superior resources and delegate regional responsibility-owner to establish the "base" market and benchmarking market for the output of "model, sales, talents, efficiency and brand" to generate returns quickly.

Conform to International Standards to Build International Brand Image

Food Union Shengmu Dairy Co., Ltd. ("**Food Union Shengmu**"), a company jointly established by the Group and Food Union (Dairy) Hong Kong Limited ("**Food Union**"), is expected to commence production in the second half of 2018, which will further enrich Shengmu series products. Targeting at children, high-end low temperature liquid milk products that are suitable for children will be launched to satisfy internationalized and popular demand, so as to facilitate China Shengmu's interconnecting with the international communities. This strategic cooperation, by introducing global-leading process, will accelerate the Company's internationalization and create an international brand image.

CORPORATE GOVERNANCE PRACTICES

The Company ensures that the Company and its subsidiaries are committed to achieving and maintaining high standards of corporate governance. The Board understands the influence and importance of high standards of corporate governance on the value of the Company, and that good corporate governance is in the interest of the Group and shareholders as a whole.

We have adopted, applied and complied with the code provisions contained in the Code on Corporate Governance and Corporate Governance Report (the "**Code**") as set out in Appendix 14 to the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited (the "**Listing Rules**") (as amended from time to time) for the year ended December 31, 2017, except for provision A2.1 of the Corporate Governance Code as disclosed below.

Pursuant to provision A2.1 of the Corporate Governance Code, the roles of chairman and chief executive officer should be separate and should not be performed by the same individual. However, the Company does not have a separate chairman and chief executive officer and Mr. SHAO Genhuo currently performs these two roles (chairman and chief executive officer). The Board believes that vesting the roles of both chairman and chief executive officer in the same person has the benefit of ensuring the consistent leadership within the Group and enables more effective and efficient overall strategic planning and implementation for the Group. The Board considers that the balance of power and authority for the present arrangement will not be impaired and this structure will enable the Company to make and implement decisions promptly and effectively. The Board will continue to review and consider splitting the roles of chairman of the Board and chief executive officer of the Company at a time when it is appropriate and suitable by taking into account the circumstances of the Group as a whole.

MODEL CODE FOR DIRECTORS' SECURITIES TRANSACTIONS

The Company has adopted a code of conduct regarding securities transactions on terms no less exacting than the required standard of dealings set out in the Model Code for Securities Transactions by Directors of Listed Issuers (the "**Model Code**") as set out in Appendix 10 to the Listing Rules. Having made specific queries to the Directors, all Directors have confirmed that they have complied with the required standards as set out in the Model Code for the year ended December 31, 2017.

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

For the year ended December 31, 2017, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's shares.

USE OF NET PROCEEDS FROM THE GLOBAL OFFERING

The net proceeds from the Global Offering of the Company were approximately RMB801.2 million. The relevant net proceeds are intended to be or have been used in accordance with the proposed usages as set out in the section headed "Future Plans and Use of Proceeds" in the Prospectus of the Company dated June 30, 2014.

As at December 31, 2017, the net proceeds were applied as follows:

	Funds utilized as at December 31, 2017 RMB'000
Constructing six additional organic dairy farms	182,525
Acquiring dairy cows domestically and from overseas	145,644
Sales and marketing activities and expansion of distribution network	40,102
Expanding the Group's liquid milk production capacity	120,306
Repayment of loans	120,306
Additional working capital and general corporate purposes	80,204
Total:	689,087

AUDIT COMMITTEE

The Company established the Audit Committee on June 18, 2014 in compliance with the Corporate Governance Code set out in Appendix 14 to the Listing Rules. The Audit Committee was established with written terms of reference in compliance with the Corporate Governance Code. The primary duties of the Audit Committee are to review and supervise the financial reporting process and internal control system of the Group. The Company modified the terms of reference of the Audit Committee on January 1, 2016. As at December 31, 2017, the Audit Committee comprised three independent non-executive Directors (Ms. GE Xiaoping, Mr. LI Changqing and Mr. WANG Liyan) and was chaired by Ms. GE Xiaoping.

The Audit Committee has reviewed the accounting standards and practices adopted by the Group and discussed with the management on the internal control and financial reporting matters, including the review of the annual results for 2017.

SCOPE OF WORK OF ERNST & YOUNG

The financial information in respect of the announcement of the Group's results for the year ended December 31, 2017 have been agreed by the Group's auditors, Ernst & Young, to the amounts set out in the Group's draft consolidated financial statements for the year. The work performed by Ernst & Young in this respect did not constitute an assurance engagement in accordance with Hong Kong Standards on Auditing, Hong Kong Standards on Review Engagements or Hong Kong Standards on Assurance Engagements issued by the Hong Kong Institute of Certified Public Accountants and consequently no assurance has been expressed by Ernst & Young on the results announcement.

DIVIDEND DISTRIBUTION

The Board does not recommend the payment of final dividend for the year ended December 31, 2017 (2016: Nil).

ANNUAL GENERAL MEETING

The 2018 annual general meeting will be held on or before June 30, 2018. A notice convening the 2018 annual general meeting will be published on the website of the Stock Exchange and the Company and dispatched to the Shareholders in due course.

PUBLICATION OF ANNUAL RESULTS ANNOUNCEMENT AND ANNUAL REPORT

This annual results announcement is published on the website of the Hong Kong Stock Exchange at www.hkexnews.hk and on the website of the Company at www.youjimilk.com. The annual report of the Company for the year of 2017 containing all the information required by the Listing Rules will be dispatched to Shareholders and published on the above websites in due course.

By Order of the Board
China Shengmu Organic Milk Limited
Shao Genhuo
Chairman

Hong Kong, March 29, 2018

As at the date of this announcement, the executive directors of the Company are Mr. Yao Tongshan, Mr. Wu Jianye, Ms. Gao Lingfeng and Mr. Cui Ruicheng; and the non-executive directors of the Company are Mr. Wen Yongping, Mr. Fan Xiang, Mr. Cui Guiyong, Mr. Sun Qian, Mr. Shao Genhuo and Mr. Zhang Jiawang; and the independent non-executive directors of the Company are Mr. Li Changqing, Ms. Ge Xiaoping, Mr. Fu Wenge, Mr. Wang Liyan and Mr. Li Xuan.