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SHENGUAN HOLDINGS (GROUP) LIMITED

神冠控股(集團)有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 00829)

2020 INTERIM RESULTS ANNOUNCEMENT

FINANCIAL AND OPERATING SUMMARY

	For the six months ended 30 June		
	2020	2019	Change
Revenue (<i>RMB million</i>)	364.1	386.8	-5.9%
Profit Attributable to Owners of the Company (<i>RMB million</i>)	27.1	31.4	-13.5%
Basic Earnings Per Share (<i>RMB cents</i>)	0.84	0.97	-13.4%
Interim Dividend Per Share (<i>HK cents</i>)	–	–	N/A
Cash Inflow from Operating Activities (<i>RMB million</i>)	109.3	104.7	+4.4%
	1H 2020	FY 2019	1H 2019
Total Assets (<i>RMB million</i>)	3,089.2	3,083.5	3,012.3
Inventory Turnover Day			
– Raw Materials (<i>days</i>)*	48.4	28.7	34.7
Inventory Turnover Day			
– Finished Goods & Work in Progress (<i>days</i>)*	296.9	228.7	357.0
Trade Receivables Turnover Day (<i>days</i>)*	110.8	93.6	99.7
Trade Payables Turnover Day (<i>days</i>)*	96.7	87.6	68.5

* Calculated based on the average value between the beginning of the period and the end of the period.

The board (the “Board”) of directors (the “Directors”) of Shenguan Holdings (Group) Limited (the “Company”) is pleased to announce the unaudited condensed consolidated interim results of the Company and its subsidiaries (collectively, the “Group”) for the six months ended 30 June 2020 (the “Period”), which have been prepared in accordance with the Hong Kong Accounting Standard 34 *Interim Financial Reporting* issued by Hong Kong Institute of Certified Public Accountants. The 2020 condensed consolidated interim results of the Group have been reviewed by the audit committee and auditors of the Company, and approved by the Board on 28 August 2020.

CONDENSED CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

For the six months ended 30 June 2020

		Six months ended 30 June	
		2020	2019
	<i>Notes</i>	RMB'000	RMB'000
		(Unaudited)	(Unaudited)
REVENUE	4	364,087	386,764
Cost of sales		<u>(267,755)</u>	<u>(284,310)</u>
Gross profit		96,332	102,454
Other income and gains, net	5	37,364	21,920
Selling and distribution expenses		(12,074)	(14,223)
Administrative expenses		(85,721)	(75,466)
Finance costs	6	(1,295)	(383)
Share of loss of an associate		<u>(2,100)</u>	<u>(1,854)</u>
PROFIT BEFORE TAX	7	32,506	32,448
Income tax expense	8	<u>(9,681)</u>	<u>(5,563)</u>
PROFIT FOR THE PERIOD		<u>22,825</u>	<u>26,885</u>

		Six months ended 30 June	
		2020	2019
	Note	RMB'000	RMB'000
		(Unaudited)	(Unaudited)
OTHER COMPREHENSIVE INCOME			
<i>Other comprehensive income that may be reclassified to profit or loss in subsequent periods:</i>			
Exchange differences on translation of foreign operations		<u>(4,503)</u>	<u>2,212</u>
NET OTHER COMPREHENSIVE INCOME THAT MAY BE RECLASSIFIED TO PROFIT OR LOSS IN SUBSEQUENT PERIODS AND OTHER COMPREHENSIVE INCOME FOR THE PERIOD, NET OF TAX		<u>(4,503)</u>	<u>2,212</u>
TOTAL COMPREHENSIVE INCOME FOR THE PERIOD		<u><u>18,322</u></u>	<u><u>29,097</u></u>
Profit attributable to:			
Owners of the Company		27,147	31,394
Non-controlling interests		<u>(4,322)</u>	<u>(4,509)</u>
		<u><u>22,825</u></u>	<u><u>26,885</u></u>
Total comprehensive income attributable to:			
Owners of the Company		22,644	33,606
Non-controlling interests		<u>(4,322)</u>	<u>(4,509)</u>
		<u><u>18,322</u></u>	<u><u>29,097</u></u>
EARNINGS PER SHARE ATTRIBUTABLE TO OWNERS OF THE COMPANY			
	10		
Basic and diluted (RMB cents per share)		<u><u>0.84</u></u>	<u><u>0.97</u></u>

CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

30 June 2020

		30 June 2020 <i>RMB'000</i> (Unaudited)	31 December 2019 <i>RMB'000</i> (Audited)
	<i>Notes</i>		
NON-CURRENT ASSETS			
Property, plant and equipment		1,102,001	1,125,619
Investment properties		7,901	7,901
Right-of-use assets		116,448	116,090
Other intangible assets		10,473	36,104
Investment in an associate		26,866	28,965
Deferred tax assets		18,571	19,660
Long term prepayments and other receivables		13,790	8,410
Pledged deposits		80,000	50,000
Time deposits		130,000	220,000
Total non-current assets		1,506,050	1,612,749
CURRENT ASSETS			
Inventories		540,837	472,411
Trade and bills receivables	11	167,173	275,071
Prepayments, other receivables and other assets		81,776	69,069
Financial asset at fair value through profit or assets		–	10,139
Pledged deposits		55,000	45,000
Cash and cash equivalents		738,361	599,063
Total current assets		1,583,147	1,470,753
CURRENT LIABILITIES			
Trade and bills payables	12	69,717	78,553
Other payables and accruals		70,478	76,446
Dividend payable		105,973	–
Interest-bearing bank borrowings		155,613	89,578
Lease liabilities		1,411	1,010
Tax payable		18,491	7,192
Total current liabilities		421,683	252,779
NET CURRENT ASSETS			
		1,161,464	1,217,974
TOTAL ASSETS LESS CURRENT LIABILITIES			
		2,667,514	2,830,723

		30 June 2020	31 December 2019
	<i>Note</i>	<i>RMB'000</i>	<i>RMB'000</i>
		(Unaudited)	(Audited)
NON-CURRENT LIABILITIES			
Lease liabilities		1,915	392
Deferred income		29,786	31,574
Deferred tax liabilities		18,148	22,330
Total non-current liabilities		49,849	54,296
Net assets		2,617,665	2,776,427
EQUITY			
Equity attributable to owners of the Company			
Issued capital	13	27,807	27,807
Reserves		2,590,195	2,744,635
		2,618,002	2,772,442
Non-controlling interests		(337)	3,985
Total equity		2,617,665	2,776,427

NOTES TO CONDENSED INTERIM FINANCIAL INFORMATION

30 June 2020

1. CORPORATE INFORMATION

Shenguan Holdings (Group) Limited (the “Company”) was incorporated in the Cayman Islands as an exempted company with limited liability under the Companies Law, Cap 22 of the Cayman Islands.

The Company and its subsidiaries (collectively referred to as the “Group”) are principally engaged in the manufacture and sale of edible collagen sausage casing products, pharmaceutical products, food products, skin care and health care products and bioactive collagen products.

2. BASIS OF PREPARATION AND ACCOUNTING POLICIES

The unaudited condensed interim financial information of the Group has been prepared in accordance with Hong Kong Accounting Standard (“HKAS”) 34 *Interim Financial Reporting* issued by the Hong Kong Institute of Certified Public Accountants (the “HKICPA”) and the applicable disclosure requirements of Appendix 16 of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (the “Listing Rules”).

The unaudited condensed interim financial information does not include all the information and disclosures required in the annual consolidated financial statements, and should be read in conjunction with the Group’s annual consolidated financial statements for the year ended 31 December 2019.

The accounting policies adopted in the preparation of the unaudited condensed interim financial information are consistent with those applied in the preparation of the Group’s annual consolidated financial statements for the year ended 31 December 2019 which have been prepared in accordance with Hong Kong Financial Reporting Standards (“HKFRSs”) (which include all Hong Kong Financial Reporting Standards, HKASs and Interpretations) issued by the HKICPA, except for the adoption of the following revised HKFRSs for the first time for the current period’s financial information.

Amendments to HKFRS 3	<i>Definition of a Business</i>
Amendments to HKAS 39, HKFRS 7 and HKFRS 9	<i>Interest Rate Benchmark Reform</i>
Amendment to HKFRS 16	<i>Covid-19-Related Rent Concessions (early adopted)</i>
Amendments to HKAS 1 and HKAS 8	<i>Definition of Material</i>

The nature and impact of the revised HKFRSs are described below:

- (a) Amendments to HKFRS 3 clarify and provide additional guidance on the definition of a business. The amendments clarify that for an integrated set of activities and assets to be considered a business, it must include, at a minimum, an input and a substantive process that together significantly contribute to the ability to create output. A business can exist without including all of the inputs and processes needed to create outputs. The amendments remove the assessment of whether market participants are capable of acquiring the business and continue to produce outputs. Instead, the focus is on whether acquired inputs and acquired substantive processes together significantly contribute to the ability to create outputs. The amendments have also narrowed the definition of outputs to focus on goods or services provided to customers, investment income or other income from ordinary activities. Furthermore, the amendments provide guidance to assess whether an acquired process is substantive and introduce an optional fair value concentration test to permit a simplified assessment of whether an acquired set of activities and assets is not a business. The Group does not has significant change on its ordinary activities or has any transaction upon adoption of the amendments on 1 January 2020 and accordingly, the amendments did not have any impact on the Group’s condensed Interim financial information.

- (b) Amendments to HKAS 39, HKFRS 7 and HKFRS 9 address the effects of interbank offered rate reform on financial reporting. The amendments provide temporary reliefs which enable hedge accounting to continue during the period of uncertainty before the replacement of an existing interest rate benchmark. In addition, the amendments require companies to provide additional information to investors about their hedging relationships which are directly affected by these uncertainties. The amendments did not have any impact on the financial position and performance of the Group as the Group does not have any interest rate hedge relationships.
- (c) Amendment to HKFRS 16 provides a practical expedient for lessees to elect not to apply lease modification accounting for rent concessions arising as a direct consequence of the covid-19 pandemic. The practical expedient applies only to rent concessions occurring as a direct consequence of the covid-19 pandemic and only if (i) the change in lease payments results in revised consideration for the lease that is substantially the same as, or less than, the consideration for the lease immediately preceding the change; (ii) any reduction in lease payments affects only payments originally due on or before 30 June 2021; and (iii) there is no substantive change to other terms and conditions of the lease. The amendment is effective retrospectively for annual periods beginning on or after 1 June 2020 with earlier application permitted. The Group does not has any rent concessions granted by lessor as a result of the covid-19 pandemic during the period ended 30 June 2020 and accordingly, the amendments did not have any impact on the Group's condensed interim financial information.
- (d) Amendments to HKAS 1 and HKAS 8 provide a new definition of material. The new definition states that information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements. The amendments clarify that materiality will depend on the nature or magnitude of information. The amendments did not have any impact on the Group's unaudited condensed interim financial information.

3. OPERATING SEGMENT INFORMATION

The Group is engaged in the principal business of manufacture and sale of edible collagen sausage casing products. The Group also involves in the manufacture and sale of pharmaceutical products, food products, skin care and health care products and bioactive collagen products.

Since over 90% of the Group's revenue is generated by its edible collagen sausage casing products, no operating segments have been aggregated to form the above reportable operating segment.

Geographical information is not presented since over 90% of the Group's revenue is derived from external customers based in the PRC and over 90% of the Group's non-current assets are located in the PRC. Accordingly, in the opinion of directors of the Company, the presentation of geographical information would provide no additional useful information to the users of this unaudited condensed interim financial information.

Revenue from major customers of the Group, excluding value added tax, which individually accounted for 10% or more of the Group's revenue for the year is set out below:

	Six months ended 30 June	
	2020	2019
	RMB'000	RMB'000
	(Unaudited)	(Unaudited)
Customer 1	57,275	51,941
Customer 2	45,612	69,167
Customer 3	43,198	47,459

4. REVENUE

Set out below is the disaggregation of the Group's revenue:

	Six months ended 30 June	
	2020	2019
	<i>RMB'000</i>	<i>RMB'000</i>
	(Unaudited)	(Unaudited)
Revenue from contracts with customers		
Goods transferred at point in time	363,993	386,699
Service transferred over time	94	65
	<u>364,087</u>	<u>386,764</u>

5. OTHER INCOME AND GAINS, NET

An analysis of other income and gains, net is as follows:

	Six months ended 30 June	
	2020	2019
	<i>RMB'000</i>	<i>RMB'000</i>
	(Unaudited)	(Unaudited)
Bank interest income	15,682	12,194
Other interest income	192	–
Foreign exchange gain, net	1,441	392
Net changes to financial assets at fair value through profit or loss	1,986	1,268
Gain on disposal of right-of-use assets	–	3,841
Government grants	16,280	2,622
Sales of dried meat products	419	312
Others	1,364	1,291
	<u>37,364</u>	<u>21,920</u>

6. FINANCE COSTS

	Six months ended 30 June	
	2020	2019
	<i>RMB'000</i>	<i>RMB'000</i>
	(Unaudited)	(Unaudited)
Interest on bank loans	1,255	370
Interest on lease liabilities	40	13
	<u>1,295</u>	<u>383</u>

7. PROFIT BEFORE TAX

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

	Six months ended 30 June	
	2020 RMB'000 (Unaudited)	2019 RMB'000 (Unaudited)
Depreciation of property, plant and equipment	47,220	47,158
Depreciation of right-of-use assets	2,190	1,843
Amortisation of other intangible assets	25,630	25,852
Impairment/(reversal of impairment) of trade receivables	3,532	(1,539)
Loss on disposal of items of property, plant and equipment	312	1,018
Write-off of inventories	5,658	1,371
Provision against obsolete and slow-moving inventories	9,526	14,095
Foreign exchange differences, net	(1,441)	(392)
	<u>47,220</u>	<u>47,158</u>

8. INCOME TAX EXPENSE

The Group is subject to income tax on an entity basis on profits arising in or derived from the jurisdictions in which members of the Group domiciled and operate.

Hong Kong profits tax has been provided at the rate of 16.5% on the estimated assessable profits arising in Hong Kong during the period, except for one subsidiary of the Group which is a qualifying entity under the two-tiered profits tax rates regime. The first HK\$2,000,000 (2019: HK\$2,000,000) of assessable profits of this subsidiary are taxed at 8.25% and the remaining assessable profits are taxed at 16.5%.

A subsidiary located in Wuzhou, Guangxi in the Western Region of China and is subject to the region's preferential corporate income tax rate of 15% as set out in Notice of the Ministry of Finance, the General Administration of Custom and the State Administration of Taxation on Tax Policy Issues Concerning Further Implementing the Western China Development Strategy (Cai Shui [2011] No. 58).

Taxes on profits assessable elsewhere have been calculated at the rates of tax prevailing in the jurisdictions in which the Group operates.

	Six months ended 30 June	
	2020 RMB'000 (Unaudited)	2019 RMB'000 (Unaudited)
Current tax charge for the period		
– PRC	12,223	6,836
– Hong Kong	553	537
Deferred tax	(3,095)	(1,810)
	<u>9,681</u>	<u>5,563</u>
Total tax charge for the period	<u>9,681</u>	<u>5,563</u>

9. DIVIDENDS

	Six months ended 30 June	
	2020	2019
	<i>RMB'000</i>	<i>RMB'000</i>
	(Unaudited)	(Unaudited)
Final dividend declared and paid for 2019 – HK2.0 cents (2018: HK2.0 cents) per ordinary share	59,028	56,974
Special dividend declared and paid for 2019 – HK4.0 cents (2018: HK1.6 cents) per ordinary share	118,056	45,580
	177,084	102,554

The directors of the Company did not propose any interim dividend in respect of the reporting period (2019: Nil).

10. EARNINGS PER SHARE ATTRIBUTABLE TO OWNERS OF THE COMPANY

The calculation of basic earnings per share amount for the period ended 30 June 2020 is based on the profit for the period attributable to owners of the Company of RMB27,147,000 (2019: RMB31,394,000) and the weighted average number of ordinary shares of 3,230,480,000 (2019: 3,231,046,000) in issue during the period ended 30 June 2020.

The Group had no potentially dilutive ordinary shares in issue during the period ended 30 June 2020 (2019: Nil).

11. TRADE AND BILLS RECEIVABLES

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

	30 June 2020	31 December 2019
	<i>RMB'000</i>	<i>RMB'000</i>
	(Unaudited)	(Audited)
Within 6 months	146,833	269,909
6 months to 1 year	18,006	2,322
Over 1 year	2,334	2,840
	167,173	275,071

The Group's trading terms with its customers are mainly on credit. The credit period is generally for a period of one month, extending up to three months for certain customers.

12. TRADE AND BILLS PAYABLES

An ageing analysis of the trade and bills payables as at the end of the reporting period, based on the invoice date, is as follows:

	30 June 2020 <i>RMB'000</i> (Unaudited)	31 December 2019 <i>RMB'000</i> (Audited)
Within 1 month	35,425	37,162
1 to 2 months	18,637	1,981
2 to 3 months	8,076	7,044
Over 3 months	7,579	32,366
	<u>69,717</u>	<u>78,553</u>

The trade payables are non-interest-bearing and are normally settled on terms of range from 60 days to 180 days.

13. SHARE CAPITAL

Shares

	30 June 2020 <i>HK\$'000</i> (Unaudited)	31 December 2019 <i>HK\$'000</i> (Audited)
Authorised:		
20,000,000,000 ordinary shares of HK\$0.01 each	<u>200,000</u>	<u>200,000</u>
Issued and fully paid:		
3,230,480,000 (31 December 2019: 3,230,480,000) ordinary shares of HK\$0.01 each	<u>32,305</u>	<u>32,305</u>
	<i>RMB'000</i>	<i>RMB'000</i>
Equivalent to	<u>27,807</u>	<u>27,807</u>

MANAGEMENT DISCUSSION AND ANALYSIS

Market Review

During the six months ended 30 June 2020 (the “Period”), as bombarded by the COVID-19 epidemic, the economy of the People’s Republic of China (the “PRC” or “China”) experienced a year-on-year decline. Following the outbreak gradually under control, full resumption of work and production in China were taken place, the domestic economy recovered rapidly in the second quarter, and major macroeconomic indicators were operated within a reasonable range. With the implementation of the “creating an enabling environment” policy and various policies to stimulate consumption, China’s economy is gradually returning to the normal status.

According to the National Bureau of Statistics of the PRC from January to June 2020, China’s gross domestic product dropped by 1.6% year-on-year; total retail sales of consumer goods decreased by 11.4% for the Period, representing a narrow down of 7.6 percentage points as compared with the decrease in the first quarter. The total output of pork, beef, mutton and poultry was approximately 34.89 million tons for the Period, down by 10.8% year-on-year. Among which, pork output decreased by 19.1% year-on-year. During the Period, owing to the greater impact of the COVID-19 epidemic on China’s economy, the sales volume of the domestic meat product industry decreased significantly. Under the context of oversupply of collagen sausage casings, the market competition became more and more intense.

Catalyzing by the COVID-19 epidemic, the great health industry ushered in an explosive opportunity. The Group will ride on the opportunities to respond to the changes of external market in a proactive manner. Based on the principal business of collagen sausage casings, the Group accelerated the production and operation of medicinal products, expanded the sales channels of medical collagen raw materials and type I and type II medical device products and extended its reach to the great health industry. At the same time, the Group also launched new businesses such as collagen food products and skincare products and expanded the layouts of collagen applications. By centering on the theme of “stabilizing quality, stabilizing market, prudent investment”, the Group vigorously explored new markets and made continuous adjustments to foster the overall positive improvement of the Group’s production and operation conditions, thereby generating better returns for the shareholders.

Business Review

Thanks to the joint efforts of its employees, the Group maintained the leading position in the domestic collagen sausage casing market. Since the fourth quarter of 2018, raw material prices have risen due to the continuously improved environmental protection requirements in China. Since 2019, the Group’s high-end collagen sausage casings trial products suitable for high-end sausage markets have been basically determined and have entered the stage of bulk trial production and customer trial use and achieved certain results. The Group has actively taken effective measures to control production costs, accelerated the automation and intelligent transformation of machinery to improve production efficiency.

Owing to fierce market competition, customers' demand for high-end products also increased. The Group strengthened the communication with customers and improved the provision of services to ensure the stability of high-end product quality of key customers, so as to promote the sales of high-end products. In addition, with the support of the government, the Group strengthened the research and development of new products and scientific research projects and had actively participated in public welfare undertakings such as student aid and poverty alleviation.

During the Period, with the joint efforts of all employees, the Group kept on improving product quality, continued to deepen and optimize performance management, added performance evaluation indicators for various departments, further perfected performance management systems, and enhanced food safety, environmental protection and also production safety management. At the same time, to promote the development of new industries and new products, the Group strengthened the construction of corporate research and development platforms, in which a group of highly-educated technical personnel are gathered together.

Industrial Layout and Technological Research & Development

The Group is committed to stepping up the development of its collagen technologies, with an aim to establishing a safe, reliable and standardized great health industry. Such move will also upgrade and transform the collagen industry and proactively promote the application of collagen in the great health industry. The Group is striving to promote new technologies and new products in various segments covering collagen food products, healthcare products, skincare products and medicinal products. The sales of some new products have increased significantly as compared with the same period of last year, but as these new product sales are just getting started, they have yet to make significant contribution to the Group's sales.

During the Period, the Group gained recognition for its outstanding performance, including the titles of "Cluster of Excellent Talents at Autonomous Region Level in Guangxi" (廣西優秀等次自治區級人才小高地), "Guangxi Top 100 Private Enterprises" (廣西民營企業100強), "Guangxi Top 100 Private Manufacturers" (廣西民營企業製造業100強), "Guangxi Most Competitive Private Enterprise" (廣西最具競爭力民營企業) and "Guangxi Leading Industrial Enterprise" (廣西工業龍頭企業). After re-assessment, Wuzhou Shenguan Protein Casing Co., Ltd. ("Wuzhou Shenguan"), a wholly-owned subsidiary of the Company, maintained the titles as "National High-Tech Enterprise" (國家高新技術企業), "China's Leading Intellectual Property Enterprise" (國家知識產權優勢企業) and "The Secondary Enterprise of Safety Production Standardization in Guangxi" (廣西安全生產標準化二級企業).

During the Period, the Group achieved outstanding results in new product research and development. For collagen food products, the collagen rice noodles, bovine collagen and collagen drinks developed by the Group have achieved initial market launch and promotion through the short live-video broadcasts on WeChat Store and Taobao flagship store. For collagen skincare products, new products such as new collagen masks, collagen extracts and collagen superior were already under sales online and offline and have achieved certain results. In addition, the Group is also actively making use of the resources generated in the production process for comprehensive application, and carry out the research and development works of skin soap series products and natural liquid soap products.

For collagen medical materials, Guangdong Victory Biotech Co., Ltd. (“Guangdong Victory”) has filed to the Guangdong provincial authorities regarding the corporate standards on six products including Fibrous Type I Collagen (Q/SCSW2-2017), Medical Soluble Type I Collagen (Q/SCSW3-2017) and Collagen Wound Dressing (Q/SCSW4-2017), and these products have obtained the dual certification of ISO13485 and ISO22442 from the European Union and are launched for sale on the market. The Group’s new product, the highly reactive collagen-based bone repairing biomaterials (高活性膠原基骨修復生物材料), is at its testing stage for its product technical indicators, and it is expected that the testing report will be completed by the end of the year, then follow by the application for clinical trial approval. The band-aids and liquid dressing products produced in Wuzhou have obtained the production permits for type I medical device products, and the production equipment is at the installation and trial production stage, the mass production of which can be expected in 2020.

Ferguson (Wuhan) Biotech Company Limited (“Ferguson Wuhan”) is striving the research and development works of three types of products, namely health food, general food and food for special dietary users. Of which, the glucosamine tablets are going through product registration material declaration, the DHA soft capsules and foods for special medical purposes, namely, children’s whole nutrition formula powder and methyl tetrahydrofolic acid tablets are undergoing or have completed the technical review, and the products that have completed technical review are currently under administrative review.

As at 30 June 2020, the Group had the following patents:

	Granted and still effective	Accepted and pending for approval
National Intellectual Property Administration of the PRC	69	20
Taiwan Intellectual Property Office	2	–
United States Patent and Trademark Office	1	–

Collagen Sausage Casings

One of the Group's principal businesses is the manufacture and sale of edible collagen sausage casings, most of which are used for the production of western sausages. Sausage manufacturers made product innovation and diversification to continue to research and develop high-end sausages, and the demand includes imitated pork castings and other high-end products.

In order to keep pace with the new trend of the domestic meat product industry, the Group launched new products that can be applied to more types of sausages fillings to cater for the market. These new products are gradually marketed and adopted. At the same time, the Group also made great efforts in enhancing internal management, increasing the level of automation, streamlining production processes and improving efficiency.

With respect to the supply of raw materials, cattle's inner skin is a major raw material for collagen sausage casing production. The supply of cattle's inner skin remained stable over the past few years and such situation is expected to remain unchanged in the coming years. Guangxi Zhiguan Industrial Development Co., Limited ("Guangxi Zhiguan"), one of the Group's substantial cattle inner skin providers, applied for the Food Production Licence under the Measures for the Administration of Food Production Licensing and Food Safety Law of the PRC on a voluntary basis and was granted such licence, effective until November 2022, by the Wuzhou Bureau for Administrative Examination and Approval, the local issuing authority of the China Food and Drug Administration where Guangxi Zhiguan is located.

Quality Control

The Group strictly controls each production step to ensure that its products are of the best quality and comply with all safety requirements. The Group's production and manufacturing of collagen sausage casings has passed the certification of ISO9001 Quality Management System, ISO22000 Food Safety Management System, ISO10012 Measurement Management System and ISO14000 Environmental Management System, and has obtained the Food Production Permit and the Filing of Export Food Manufacturers (出口食品生產企業備案證). The Group has also registered with the U.S. Food and Drug Administration for export of sausage casing products to the United States. In addition, the production of all of the Group's sausage casing products have strictly complied with the PRC's national standards (GB14967-94), sausage casing manufacturing industry standards (SB/T10373-2012) and the filed corporate standards (Q/WZSG0001S-2012). All these certifications are the recognition of the Group as a trustworthy product supplier to its customers.

Guangxi Wuzhou Zhongguan Testing Technology Services Co., Ltd. (“Wuzhou Zhongguan”), a subsidiary of the Group, is able to examine over 800 indicators, including the physicochemical indicators such as heavy metals and microelements, pesticide residues, microorganisms and proteins. Currently, Wuzhou Zhongguan continues to independently undertake third-party inspection assignments, undertake various food and relevant product testing services and issue officially-recognized testing reports, thus generating external sales revenue. Such qualification is going to lay a solid foundation for the Group to develop into a collagen materials base, thereby facilitating the development of high-end foods, healthcare products and medicines in the health industry.

Customer Relationship

The Group is committed to developing long-term mutual trust cooperation relationships with its business partners and has already built a sophisticated customer network. The Group has established its closely-knit yet extensive network of leading manufacturers of processed meat products and sausages, which is not only for the cooperation with enterprises in the PRC, but also with those in various overseas markets, such as South America, Southeast Asia and the United States. During the Period, the Group continued to supply high-quality sausage casing products to a number of renowned food suppliers in the PRC. The number of domestic customers remained stable.

Financial Analysis

Revenue

Revenue decreased by approximately 5.9% to approximately RMB364.1 million for the Period from approximately RMB386.8 million for the six months ended 30 June 2019 (the “Prior Period”). Owing to the impact of the COVID-19 epidemic, some customers delayed the resumption of work after Chinese New Year during the Period, which resulted a decrease in products demand.

Cost of sales

Cost of sales decreased by approximately 5.8% to approximately RMB267.8 million for the Period from approximately RMB284.3 million for the Prior Period, including the provision and write-off of inventory of approximately RMB15.2 million, as compared to the provision and write-off of approximately RMB15.5 million for the Prior Period. Excluding such items, the cost of sales for the Period decreased by approximately 6.0% as compared to the Prior Period. The costs of raw materials for the Period slightly decreased by approximately 2.8% to approximately RMB106.3 million as compared with that of the Prior Period. In addition, the charges for energy slightly increased by approximately 0.7% to approximately RMB55.4 million. The direct labor costs slightly decreased by approximately 0.5% to approximately RMB43.3 million.

Gross profit

Gross profit margin maintained at 26.5%, while the gross profit decreased by approximately 6.0% to approximately RMB96.3 million for the Period from approximately RMB102.5 million for the Prior Period.

Other income and gains

Other income and gains increased by approximately 70.5% to approximately RMB37.4 million for the Period from approximately RMB21.9 million for the Prior Period. In addition to the increase in bank interest income, the Group received government subsidies of approximately RMB16.3 million during the Period, representing an increase of approximately RMB13.7 million over the Prior Period, the reason of which was that, during the period of the COVID-19 epidemic, the Group received employment stabilization subsidies for continuing the production during Chinese New Year and obtained unemployment insurance emergency rebates to stabilize employment. The subsidiaries and rebates were received from the PRC government.

Selling and distribution expenses

Selling and distribution expenses as a percentage of revenue decreased to approximately 3.3% for the Period from approximately 3.7% for the Prior Period. Selling and distribution expenses decreased by approximately 15.1% to approximately RMB12.1 million for the Period from approximately RMB14.2 million for the Prior Period.

Administrative expenses

Administrative expenses increased by approximately 13.6% to approximately RMB85.7 million for the Period from approximately RMB75.5 million for the Prior Period. The Group made charitable donations of approximately RMB8.2 million during the Period, representing an increase of approximately RMB8.0 million from the Prior Period, mainly to support the fight against the COVID-19 epidemic.

For the technologies acquired by the Group through the acquisition of Guangdong Victory, the intangible assets are amortized over five years (these intangible assets will be fully amortized in the third quarter of this year). The related amortization expense was approximately RMB25.4 million for the Period and for the Prior Period. After deducting the non-controlling interests and deferred tax of Guangdong Victory, the effect of the related amortization expense on the net profit of the Group was approximately RMB15.2 million. The item above that exerted a relatively material impact on the net profit for the Period and for the Prior Period was non-cash items and hence the cash flow of the Group was not affected.

Finance costs

Finance costs increased by approximately 238.1% to approximately RMB1.3 million for the Period from approximately RMB383,000 for the Prior Period, mainly attributable to the increase in bank borrowings.

Share of loss of an associate

The share of loss of an associate for the Period amounted to approximately RMB2.1 million, which was mainly due to the share of loss of Ferguson Wuhan during the Period. The production of Ferguson Wuhan was suspended for some time during the Period due to COVID-19 epidemic.

Income tax expenses

Income tax expenses were approximately RMB9.7 million for the Period, as compared to approximately RMB5.6 million for the Prior Period. The Company's major operating subsidiary, Wuzhou Shenguan enjoyed a preferential tax treatment due to its location in western China and fall into the industry category encouraged by government policies. The applicable tax rate for Wuzhou Shenguan is 15%.

The effective tax rates applied to the Group were approximately 17.1% and approximately 29.8% of profit before tax, respectively for the Prior Period and for the Period. The higher effective tax rates for the Period was mainly due to the provision of dividend withholding tax.

Loss attributable to non-controlling interests

The loss attributable to non-controlling interests for the Period was approximately RMB4.3 million, which mainly represented the amortization expense of technology intangible assets attributable to the non-controlling interests in Guangdong Victory.

Profit attributable to owners of the Company

As stipulated in the aforesaid reasons, profit attributable to owners of the Company decreased by approximately 13.5% to approximately RMB27.1 million for the Period from approximately RMB31.4 million for the Prior Period.

LIQUIDITY AND CAPITAL RESOURCES

Cash and bank borrowings

The Group generally finances its business operations and capital expenditure with internally generated cash flows as well as the bank borrowings provided by its principal banks.

As at 30 June 2020, the cash and cash equivalents together with pledged and time deposits amounted to approximately RMB1,003.4 million and amounted to RMB897.4 million after deducting part of the 2019 dividends by bank transfer that was completed in early July 2020, representing a decrease of approximately RMB16.7 million from the end of 2019. Among these balances, approximately 93.7% was denominated in Renminbi, and the remaining 6.3% was denominated in Hong Kong dollars, Singapore dollars and U.S. dollars.

As at 30 June 2020, the total bank borrowings of the Group amounted to approximately RMB155.6 million, increased by approximately RMB66.0 million (as at 31 December 2019: approximately RMB89.6 million), and all bank borrowings were wholly repayable within one year. Total bank borrowings denominated in RMB was approximately RMB65 million, and total bank borrowings denominated in U.S. dollars was approximately US\$12.8 million (equivalent to approximately RMB90.6 million).

The Group was in a net cash position (cash and cash equivalents together with the pledged and time deposits less total bank borrowings) of approximately RMB847.8 million as at 30 June 2020, and amounted to RMB741.8 million after deducting the dividends by bank transfer that was completed in early July 2020, representing a decrease of approximately RMB82.7 million as compared to that as at the end of 2019. The debt-to-equity ratio was 5.9% as at 30 June 2020 (as at 31 December 2019: 3.2%). The debt-to-equity ratio was calculated by dividing total bank borrowings by total equity.

Cash flows

During the Period, the net cash inflow of approximately RMB109.3 million was generated from operating activities, while investing activities and financing activities utilized approximately RMB158.9 million and RMB8.8 million, respectively. The net cash outflow from investing activities was mainly attributable to the cash outflow from increase in non-pledged time deposits with original maturity of over three months and the increase in pledged deposits. The net cash outflow from financing activities was mainly attributable to the combined effects of the repayment of bank borrowings and the new bank borrowings and the payment of 2019 final dividends.

Exposure to exchange risks

The Group mainly operates in the PRC with most of its transactions settled in Renminbi. The assets and liabilities, and transactions arising from the operations are mainly denominated in Renminbi. Although the Group may be exposed to foreign currency exchange risks, the Board believes that the future currency fluctuations will not have any material impact on the Group's operations. The Group had not adopted any formal hedging policies.

Capital expenditure

The capital expenditure of the Group during the Period amounted to approximately RMB25.7 million, which was mainly used for the acquisition of property, plant and equipment, and the capital commitments as at 30 June 2020 amounted to approximately RMB119.0 million, which were mainly related to the improvement and upgrades of production facilities.

The estimated capital expenditure of the Group for 2020 amounted to approximately RMB80.0 million, which will be used for the upgrade and intellectualization of production facilities for sausage casing business, as well as the expansion of production facilities of the new businesses in progress, and the renovation and addition of equipment for the research and development center in Singapore.

Pledge of assets

As at 30 June 2020, pledged bank deposits amounted to approximately RMB135.0 million in total.

Contingent liabilities

As at 30 June 2020 and up to the date of this announcement, the Group was not aware of any material contingent liabilities.

SIGNIFICANT INVESTMENTS, MATERIAL ACQUISITIONS AND DISPOSALS OF SUBSIDIARIES, ASSOCIATED COMPANIES AND JOINT VENTURES

The Group had no significant investments, material acquisitions or disposals of subsidiaries, associated companies and joint ventures during the Period.

EVENTS AFTER THE PERIOD

There were no important events affecting the Group that have occurred since 30 June 2020.

HUMAN RESOURCES

As at 30 June 2020, the Group hired a total of approximately 2,600 contract employees (as at 30 June 2019: 2,500). During the Period, the total remuneration and employees' benefit expenses charged to profit or loss were approximately RMB73.7 million (first half of 2019: approximately RMB81.2 million). In order to attract and retain high quality talents to ensure smooth business operation and to cope with the need of the Group's continuing expansion, the Group offers competitive remuneration packages with reference to the market conditions as well as individual qualifications and experience.

PROSPECTS AND STRATEGIES

China's economy has experienced a decline in the first half of 2020 due to the impact of the COVID-19 epidemic. Thanks to the effective prevention and control measures taken nationwide, the epidemic in China has been further brought under control with work and production in different industries resumed, and China's economy has recovered significantly in the second quarter. The hidden worries of the COVID-19 epidemic have not completely dissipated, the Sino-US economic and trade relations have shown signs of deterioration during the Period and China's economy is still facing tremendous challenges. Looking forward to the second half of 2020, the domestic economic situation will continue to remain acute. However, with the PRC government emphasizing on the keynotes of "Six Stabilities" and "Six Guarantees", together with the introduction of a number of policies to stimulate the domestic economy, the domestic economy is not expected to encounter significant fluctuations.

The back and forth COVID-19 epidemic situation overseas has greatly affected the global meat product industry and blocked the import of meat products, but this presents an opportunity for domestic meat products enterprises. Facing such complicated economic environment, opportunities and challenges coexist for the Group's production and operation, thus creating and seizing opportunities is the key for the Group in the second half of the year. 2020 is going to be the final year for the Group to implement the "Thirteenth Five-Year Plan". However, the Group exposed to threats from external factors such as global oversupply of collagen sausage casings, increasingly fierce market competition, negative growth in the meat industry, customer products transformation and upgrading, and higher requirements for product applicability. However, as nutritional high-end sausages are gradually available for household and group consumption, while the price of natural sausage casings is high, the demand for high-end collagen sausage casings to replace pig sausage casings will further increase, in which it will bring opportunities to the Group to a certain extent.

In 2020, the production and operation of the Group will mainly focus on "stabilizing quality, stabilizing market, prudent investment" to speed up the implementation of product diversification strategies, increase efforts to develop new products and expand new markets while stabilizing its existing principal businesses and improving product quality. In the second half of 2020, the Group will accelerate the implementation of product diversification strategies and put efforts in the research and development of new collagen-based food products, healthcare products, cosmetics and medical materials. The Group will utilize automation and intellectualization as the means to achieve product diversification and extend its reach to the great health industry as well as the strategic emerging industries, so as to build itself into a world-class supplier of collagen raw materials.

In terms of the sausage casing industry, there will be three focuses, namely, enhance product quality, improve the support of various production lines and comprehensively promote the technological transformation of mechanized, automated and intelligent production. While intensifying the development of new products and expanding the market, and further improving the ancillary facilities of production lines to fully utilize production capacity, the Group will carry out intelligent technological transformation to reduce production costs, and will also transform the environmental protection facilities to enhance its environmental protection processing capabilities, thereby strengthening food safety and production safety to strictly prevent illegal operations and achieve the goal of reducing safety risks.

For collagen food products, the Group plans to expand its production capacity of collagen rice noodles, collagen drinks and bovine collagen ingredients. While accelerating the preliminary works of constructing rice noodle production workshops and equipment selection, the Group will also put more efforts in advertising and sales planning, and fully promote online e-commerce, micro commerce and offline agency sales, so as to realize more significant growth in sales revenue. For collagen skincare products, the Group will strengthen the construction of “Luxianna” product chain and the development of “COLL-FULL” new products, and accelerate the construction of the base in Singapore and put it into operation, so as to complement the facilitation of the sales planning of the product series such as collagen extracts and collagen superior under the “collagen product family”.

The Group will further intensify the research on medical collagen, and strive to obtain the production permits for a number of collagen medical device products during 2020, and also strive to obtain the certification of ISO13485 and ISO22442 from the European Union in 2020 for the medical collagen products in Wuzhou. In addition, the Group will also expand the sales channels of medical collagen raw materials and medical device products, so as to generate economic benefits for the Group as soon as possible.

Finally, the Shenguan team will continue to endeavour and propel the continuous business growth and further broaden the application of collagen technology to generate better returns for the shareholders.

OTHER INFORMATION

SHARE OPTION SCHEME

In order to attract and retain the eligible persons, provide additional incentive to them and promote the success of the business of the Group, the Company adopted a share option scheme (the “Scheme”) on 29 May 2020 (the “Adoption Date”) whereby the Board are authorised, at their absolute discretion and subject to the terms of the Scheme, to grant options to subscribe the share(s) of the Company (the “Share(s)”) to, inter alia, any employees (full-time or part-time), directors, consultants and advisors of the Group or any substantial shareholder, distributors, contractors, suppliers, agents, customers, business partners or service providers of the Group. The Scheme shall be valid and effective for a period of ten years commencing on 29 May 2020, subject to the early termination provisions contained in the Scheme.

An offer for the grant of options must be accepted within seven days inclusive of the day on which such offer was made. The amount payable by the grantee of an option to the Company on acceptance of the offer for the grant of an option is HK\$1.00. The subscription price of a Share in respect of any particular option granted under the Scheme shall be a price solely determined by the Board and notified to a participant and shall be at least the highest of: (i) the closing price of the Shares as stated in the Stock Exchange's daily quotations sheet on the date of grant of the option; (ii) the average of the closing prices of the Shares as stated in the Stock Exchange's daily quotations sheets for the five trading days immediately preceding the date of grant of the option; and (iii) the nominal value of a Share on the date of grant of the option.

The Company shall be entitled to issue options, provided that the total number of Shares which may be issued upon exercise of all options to be granted under the Scheme does not exceed 10% of the Shares in issue on the Adoption Date. The Company may at any time refresh such limit, subject to the shareholders' approval and issue of a circular in compliance with the Listing Rules, provided that the total number of Shares which may be issued upon exercise of all outstanding options granted and yet to be exercised under all the share option schemes of the Company does not exceed 30% of the Shares in issue at any time.

The total number of securities available for issue under the Scheme as at the date of this announcement was 323,048,000 Shares, which represented 10% of the total number of issued Shares as at the Adoption Date. The total number of Shares issued and to be issued upon exercise of options granted to any grantee (including both exercised and outstanding options) under the Scheme, in any 12-month period up to the date of grant shall not exceed 1% of the Shares in issue.

An option may be exercised in accordance with the terms of the Scheme at any time during a period as the Board may determine, which shall not exceed ten years from the date of grant subject to the provisions of early termination thereof.

At no time during the Period were rights to acquire benefits by means of the acquisition of shares in or debentures of the Company granted to any of the Directors or their respective spouses or minor children, or were any such rights exercised by them; nor was the Company, its holding company, or any of its subsidiaries or fellow subsidiaries a party to any arrangement to enable the Directors to acquire such rights in any other body corporate.

There is no share option outstanding, granted, cancelled or lapsed under the Scheme during the six months ended 30 June 2020.

PAYMENT OF INTERIM DIVIDENDS

In view of the capital expenditure to be incurred by the Group and market expansion in the foreseeable future, no interim dividend was proposed by the Board in respect of the Period (Prior Period: Nil).

PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

Neither the Company, nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities during the Period.

UPDATE ON DIRECTOR AND SENIOR MANAGEMENT INFORMATION

Changes in the information of Directors and senior management of the Company since the disclosure made in the 2019 annual report of the Company, that are required to be disclosed pursuant to Rule 13.51B(1) of the Listing Rules, are set out below:

Mr. Ng Yuk Yeung (being the company secretary of the Company) has resigned as an independent non-executive director of BGMC International Limited, a listed company in Hong Kong (stock code: 1693), on 3 July 2020.

CORPORATE GOVERNANCE CODE

Save as disclosed below, the Company had complied with all the code provisions as set out in the Corporate Governance Code (the "Code") contained in Appendix 14 to the Listing Rules during the Period.

Under code provision A.2.1 of the Code, the roles of chairman and the chief executive should be separate and should not be performed by the same individual.

Ms. Zhou Yaxian, who acts as the chairman (the "Chairman") and the president of the Company, is also responsible for overseeing the general operations of the Group. The Board will meet regularly to consider major matters affecting the operations of the Group. The Board considers that this structure will not impair the balance of power and authority between the Board and the management of the Company. The roles of the respective executive Directors and senior management, who are in charge of different functions complement the role of the chairman and chief executive. The Board believes that this structure is conducive to strong and consistent leadership which enables the Group to operate efficiently.

The Company understands the importance to comply with code provision A.2.1 of the Code and will continue to consider the feasibility of appointing a separate chief executive. The Company will make timely announcement if the chief executive has been appointed.

The Chairman takes the lead to ensure that the Board acts in the best interests of the Company, that there is effective communication with the shareholders and that their views are communicated to the Board as a whole. The Chairman meets at least annually with the non-executive Directors without the executive Directors being present.

MODEL CODE TO THE LISTING RULES

The Company has adopted the Model Code as set out in Appendix 10 to the Listing Rules as its own code of conduct regarding Directors' securities transactions. The Company has also adopted the Model Code for the members of senior management of the Group.

The Company has made specific enquiry with all the Directors and all the Directors have confirmed that they had complied with the Model Code during the Period. Moreover, no incident of non-compliance of the Model Code by the senior management was noted by the Company.

AUDIT COMMITTEE

The audit committee of the Board comprises of three independent non-executive Directors, namely Mr. Tsui Yung Kwok, Mr. Meng Qinguo and Mr. Yang Xiaohu. Mr. Tsui Yung Kwok, who possesses professional accounting qualification and relevant accounting experience, is the chairman of the audit committee.

The audit committee has reviewed the unaudited condensed consolidated interim results of the Group for the Period and considered that the interim results had complied with all applicable accounting standards and the Listing Rules. The audit committee has also reviewed this report.

The unaudited condensed consolidated interim results of the Group for the Period have been reviewed by the Company's auditor, Ernst & Young.

By order of the Board
Shenguan Holdings (Group) Limited
Zhou Yaxian
Chairman

Hong Kong, 28 August 2020

As at the date of this announcement, the executive Directors are Ms. Zhou Yaxian, Mr. Shi Guicheng, Mr. Ru Xiquan and Mr. Mo Yunxi; the non-executive Director is Dato' Sri Low Jee Keong; and the independent non-executive Directors are Mr. Tsui Yung Kwok, Mr. Meng Qinguo and Mr. Yang Xiaohu.