# 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 31 DECEMBER 2020

### FINANCIAL HIGHLIGHTS

| | For the year ended 31 December | | |
|---|---|---|---|
| | **2020** | 2019 | **Movements** |
| | **RMB'000** | RMB'000 | |
| Operating income(1) | **2,779,148** | 2,640,920 | **5.2%** |
| Revenue(2) | **2,660,823** | 2,539,567 | **4.8%** |
| Gross profit(2) | **1,025,118** | 937,149 | **9.4%** |
| Profit for the year | **460,969** | 135,696 | **239.7%** |
| Profit attributable to owners of the parent | **406,680** | 27,742 | **1,365.9%** |
| Basic earnings per share (RMB) | **0.0535** | 0.0044 | **0.0491** |
| Return on net assets | **13.5%** | 5.6% | **7.9%** |

(1) Operating income is calculated based on revenue plus other income, and does not include disposal of biological assets of RMB330 million;

(2) It represents revenue and gross profit of continuing operations.

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).

The board (the "**Board**") of directors (the "**Directors**") of China Shengmu Organic Milk Limited (the "**Company**" or "**China Shengmu**") hereby to announce the consolidated financial results of the Company and its subsidiaries (the "**Group**" or "**Shengmu**") for the year ended 31 December 2020 together with the comparative figures for the year ended 31 December 2019.

## CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME

| | Notes | For the year ended 31 December **2020** RMB'000 | 2019 RMB'000 |
|---|---|---|---|
| **CONTINUING OPERATIONS** | | | |
| REVENUE | 3 | **2,660,823** | 2,539,567 |
| Cost of sales | | **(1,635,705)** | (1,602,418) |
| Gross profit | | **1,025,118** | 937,149 |
| Loss arising from changes in fair value less costs to sell of biological assets | | **(224,237)** | (284,896) |
| Other income and gains/(losses) | 3 | **(44,457)** | 2,999 |
| Selling and distribution expenses | | **(32,084)** | (30,704) |
| Administrative expenses | | **(111,718)** | (131,257) |
| Impairment losses on financial and contract assets, net | | **1,683** | (13,622) |
| Other expenses | | **(997)** | (163) |
| Finance costs | 5 | **(116,788)** | (225,239) |
| Share of losses of associates | | **(35,551)** | (64,953) |
| **PROFIT BEFORE TAX FROM CONTINUING OPERATIONS** | 4 | **460,969** | 189,314 |
| Income tax expense | 6 | **—** | (410) |
| **PROFIT FOR THE YEAR FROM CONTINUING OPERATIONS** | | **460,969** | 188,904 |
| **DISCONTINUED OPERATION** | | | |
| Loss for the year from a discontinued operation | | **—** | (53,208) |
| PROFIT FOR THE YEAR | | **460,969** | 135,696 |
| Profit attributable to: | | | |
| Owners of the parent | | **406,680** | 27,742 |
| Non-controlling interests | | **54,289** | 107,954 |
| | | **460,969** | 135,696 |

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

| | Note | For the year ended 31 December<br>2020<br>RMB'000 | 2019<br>RMB'000 |
|---|---|---|---|
| EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT | 8 | | |
| Basic | | | |
| – For profit for the year | | **RMB0.0535** | RMB0.0044 |
| – For profit from continuing operations | | **RMB0.0535** | RMB0.0127 |
| Diluted | | | |
| – For profit for the year | | **RMB0.0535** | RMB0.0044 |
| – For profit from continuing operations | | **RMB0.0535** | RMB0.0127 |
| **OTHER COMPREHENSIVE INCOME/ (LOSS)** | | | |
| Exchange differences on translation of foreign operations | | **2,013** | (2,598) |
| Net other comprehensive income/(loss) that may not be reclassified to profit or loss in subsequent periods | | **2,013** | (2,598) |
| **OTHER COMPREHENSIVE INCOME/ (LOSS) FOR THE YEAR, NET OF TAX** | | **2,013** | (2,598) |
| **TOTAL COMPREHENSIVE INCOME FOR THE YEAR** | | **462,982** | 133,098 |
| Attributable to: | | | |
| Owners of the parent | | **408,693** | 25,144 |
| Non-controlling interests | | **54,289** | 107,954 |
| | | **462,982** | 133,098 |

## CONSOLIDATED STATEMENT OF FINANCIAL POSITION

| | Notes | As at 31 December 2020 RMB'000 | 31 December 2019 RMB'000 |
|---|---|---|---|
| **NON-CURRENT ASSETS** | | | |
| Property, plant and equipment | | **1,772,651** | 2,043,525 |
| Right-of-use assets | | **45,100** | 54,272 |
| Other intangible assets | | **6,242** | 11,254 |
| Investments in associates | | **122,255** | 150,413 |
| Biological assets | | **2,572,102** | 2,531,188 |
| Long term receivables | | **10,498** | 14,505 |
| Other non-current assets | | **—** | 11,843 |
| Total non-current assets | | **4,528,848** | 4,817,000 |
| **CURRENT ASSETS** | | | |
| Inventories | | **715,078** | 678,054 |
| Biological assets | | **15,008** | 13,799 |
| Trade and bills receivables | 9 | **136,611** | 167,118 |
| Prepayments, other receivables and other assets | | **614,578** | 614,130 |
| Pledged deposits | | **387,452** | 177,516 |
| Cash and bank balances | | **327,651** | 132,636 |
| Total current assets | | **2,196,378** | 1,783,253 |
| **CURRENT LIABILITIES** | | | |
| Trade and bills payables | 10 | **1,699,448** | 1,365,884 |
| Other payables and accruals | | **239,981** | 574,772 |
| Derivative financial instruments | | **—** | 3,267 |
| Interest-bearing bank and other borrowings | | **1,335,873** | 2,144,832 |
| Lease liabilities | | **—** | 32,287 |
| Total current liabilities | | **3,275,302** | 4,121,042 |
| **NET CURRENT LIABILITIES** | | **(1,078,924)** | (2,337,789) |
| **TOTAL ASSETS LESS CURRENT LIABILITIES** | | **3,449,924** | 2,479,211 |

## CONSOLIDATED STATEMENT OF FINANCIAL POSITION (CONTINUED)

| | As at | |
|---|---|---|
| | **31 December 2020** | 31 December 2019 |
| | **RMB'000** | RMB'000 |
| **NON-CURRENT LIABILITIES** | | |
| Interest-bearing bank and other borrowings | **30,398** | 39,443 |
| Long term payables | **—** | 28,940 |
| Total non-current liabilities | **30,398** | 68,383 |
| Net assets | **3,419,526** | 2,410,828 |
| **EQUITY** | | |
| **Equity attributable to owners of the parent** | | |
| Share capital | **69** | 50 |
| Reserves | **3,196,663** | 2,186,371 |
| | **3,196,732** | 2,186,421 |
| **Non-controlling interests** | **222,794** | 224,407 |
| **Total equity** | **3,419,526** | 2,410,828 |

**NOTES**

**1. CORPORATE AND GROUP 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 in the People's Republic of China (the "**PRC**").

**2. BASIS OF PREPARATION AND CHANGES IN ACCOUNTING POLICES OF THE GROUP**

**Basis of Preparation**

The financial statements have been prepared in accordance with International Financial Reporting Standards ("**IFRSs**") (which include all International Financial Reporting 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, agricultural produce and derivative financial liabilities. 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 (collectively referred to as the "**Group**") for the year ended 31 December 2020. A subsidiary is an entity (including a structured entity), directly or indirectly, controlled by the Company. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee (i.e., existing rights that give the Group the current ability to direct the relevant activities of the investee).

## 2. BASIS OF PREPARATION AND CHANGES IN ACCOUNTING POLICES OF THE GROUP (CONTINUED)

### Basis of Preparation (continued)

Basis of consolidation (continued)

When the Company has, directly or indirectly, less than a majority of the voting or similar rights of an investee, the Group considers all relevant facts and circumstances in assessing whether it has power over an investee, including:

(a) the contractual arrangement with the other vote holders of the investee;

(b) rights arising from other contractual arrangements; and

(c) the Group's voting rights and potential voting rights.

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.

Profit or loss and each component of other comprehensive income are attributed to the owners of the parent of the Group and to the non-controlling interests, even if this results in the non-controlling interests having a deficit balance. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

The Group reassesses whether or not it controls an investee if facts and circumstances indicate that there are changes to one or more of the three elements of control described above. A change in the ownership interest of a subsidiary, without a loss of control, is accounted for as an equity transaction.

If the Group loses control over a subsidiary, it derecognises (i) the assets (including goodwill) and liabilities of the subsidiary, (ii) the carrying amount of any non-controlling interest and (iii) the cumulative translation differences recorded in equity; and recognises (i) the fair value of the consideration received, (ii) the fair value of any investment retained and (iii) any resulting surplus or deficit in profit or loss. The Group's share of components previously recognised in other comprehensive income is reclassified to profit or loss or retained profits, as appropriate, on the same basis as would be required if the Group had directly disposed of the related assets or liabilities.

## 2. BASIS OF PREPARATION AND CHANGES IN ACCOUNTING POLICES OF THE GROUP (CONTINUED)

**Basis of Preparation (continued)**

Going concern

The Group had net current liabilities of RMB1,078,924,000 as at 31 December 2020 (2019: net current liabilities of RMB2,337,789,000). In view of the net current liabilities position, the board of directors has 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 RMB1,949,798,000, the unutilised entrusted loan facility of RMB1,600,000,000 granted by China Mengniu Dairy Co., Ltd as at the date of this report and cash flow projections for the year ending 31 December 2021, the directors are satisfied that the Group is able to meet in full its financial obligations as they fall due for the foreseeable future. Accordingly, the directors have prepared the consolidated financial statements on a going concern basis.

**Changes in Accounting Policies and Disclosures**

The Group has adopted the *Conceptual Framework for Financial Reporting 2018 and the* following revised IFRSs for the first time for the current year's financial statements.

| | |
|---|---|
| Amendments to IFRS 3 | *Definition of a Business* |
| Amendments to IFRS 9, IAS 39 and IFRS 7 | *Interest Rate Benchmark Reform* |
| Amendments to IFRS 16 | *Covid-19-Related Rent Concessions (early adopted)* |
| Amendments to IAS 1 and IAS 8 | *Definition of Material* |

## 2. BASIS OF PREPARATION AND CHANGES IN ACCOUNTING POLICES OF THE GROUP (CONTINUED)

### Changes in Accounting Policies and Disclosures (Continued)

The nature and the impact of the *Conceptual Framework for Financial Reporting 2018* and the revised IFRSs are described below:

(a) *Conceptual Framework for Financial Reporting 2018* (the "**Conceptual Framework**") sets out a comprehensive set of concepts for financial reporting and standard setting, and provides guidance for preparers of financial statements in developing consistent accounting policies and assistance to all parties to understand and interpret the standards. The Conceptual Framework includes new chapters on measurement and reporting financial performance, new guidance on the derecognition of assets and liabilities, and updated definitions and recognition criteria for assets and liabilities. It also clarifies the roles of stewardship, prudence and measurement uncertainty in financial reporting. The Conceptual Framework is not a standard, and none of the concepts contained therein override the concepts or requirements in any standard. The Conceptual Framework did not have any significant impact on the financial position and performance of the Group.

(b) Amendments to IFRS 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 has applied the amendments prospectively to transactions or other events that occurred on or after 1 January 2020. The amendments did not have any impact on the financial position and performance of the Group.

## 2. BASIS OF PREPARATION AND CHANGES IN ACCOUNTING POLICES OF THE GROUP (CONTINUED)

**Changes in Accounting Policies and Disclosures (Continued)**

(c) Amendments to IFRS 9, IAS 39 and IFRS 7 address issues affecting financial reporting in the period before the replacement of an existing interest rate benchmark with an alternative risk-free rate ("**RFR**"). The amendments provide temporary reliefs which enable hedge accounting to continue during the period of uncertainty before the introduction of the alternative RFR. 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 hedging relationships.

(d) Amendment to IFRS 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 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 for annual periods beginning on or after 1 June 2020 with earlier application permitted and shall be applied retrospectively.

During the year ended 31 December 2020, no leases of the Group have been reduced or waived by the lessors as a result of the covid-19 pandemic. The amendment did not have any impact on the financial position and performance of the Group.

## 2. BASIS OF PREPARATION AND CHANGES IN ACCOUNTING POLICES OF THE GROUP (CONTINUED)

**Changes in Accounting Policies and Disclosures (Continued)**

(e) Amendments to IAS 1 and IAS 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, or both. The amendments did not have any significant impact on the financial position and performance of the Group.

## 3. REVENUE, OTHER INCOME AND GAINS/(LOSSES)

An analysis of revenue, other income and gains/(losses) from continuing operations is as follows:

| | For the year ended 31 December | |
|---|---|---|
| | **2020** | 2019 |
| | **RMB'000** | RMB'000 |
| Revenue from contracts with customers | **2,660,823** | 2,539,567 |

## 3. REVENUE, OTHER INCOME AND GAINS/(LOSSES) (CONTINUED)

Disaggregated revenue information for revenue from contracts with customers

| | For the year ended 31 December | |
|---|---|---|
| | **2020** | 2019 |
| | **RMB'000** | RMB'000 |
| **Type of goods** | | |
| Sale of products | **2,660,823** | 2,539,567 |
| **Geographical market** | | |
| Mainland China | **2,660,823** | 2,539,567 |
| **Timing of revenue recognition** | | |
| Goods transferred at a point in time | **2,660,823** | 2,539,567 |
| **Other income and gains/(losses)** | | |
| Other income | | |
| Beef cattle | **113,080** | 98,723 |
| Raw materials | **5,245** | 2,630 |
| | **118,325** | 101,353 |
| Other costs | | |
| Beef cattle | **(113,080)** | (98,723) |
| Raw materials | **(3,889)** | (7,027) |
| | **(116,969)** | (105,750) |
| Government grants | **4,088** | 17,678 |
| Bank interest income | **7,651** | 5,735 |
| Foreign exchange differences, net | **(4,966)** | (1,952) |
| Loss on disposal of items of property, plant and equipment | **(11,947)** | (7,561) |
| Impairment loss of investment in an associate | **—** | (5,111) |
| Impairment loss of items of property plant and equipment | **(60,470)** | — |
| Impairment loss of intangible assets | **(8,250)** | — |
| Gain on partial disposal of an associate | **23,144** | — |
| Gain on disposal of a subsidiary | **845** | — |
| Fair value gains, net: | | |
| Derivative financial instruments | **—** | 849 |
| Others | **4,092** | (2,242) |
| | **(44,457)** | 2,999 |

## 4. PROFIT BEFORE TAX

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

| | For the year ended 31 December | |
|---|---|---|
| | **2020** | 2019 |
| | **RMB'000** | RMB'000 |
| Cost of inventories sold | **1,635,705** | 1,602,418 |
| Loss arising from changes in fair value less costs to sell of biological assets | **224,237** | 284,896 |
| Depreciation of property plant and equipment | **154,715** | 153,412 |
| Less: Capitalised in biological assets | **46,237** | 41,948 |
| Depreciation recognised in the consolidated statement of profit or loss and other comprehensive income | **108,478** | 111,464 |
| Depreciation of right-of-use assets | **3,061** | 1,741 |
| Less: Capitalised in biological assets | **1,016** | 476 |
| Depreciation recognised in the consolidated statement of profit or loss and other comprehensive income | **2,045** | 1,265 |
| Amortisation of other intangible assets | **1,028** | 1,285 |
| Less: Capitalised in biological assets | **341** | 354 |
| Amortisation recognised in the consolidated statement of profit or loss and other comprehensive income | **687** | 931 |
| Research and development costs | **5,696** | 4,791 |
| Lease payments not included in the lease | **8,035** | 7,370 |
| Auditor's remuneration | **2,680** | 3,060 |
| Impairment on financial and contract assets, net | **(1,683)** | 13,622 |
| Write-down of inventories to net realisable value | **1,458** | 2,849 |
| Gain on partial disposal of an associate | **(23,144)** | — |
| Gain on disposal of a subsidiary | **(845)** | — |
| Loss on disposal of items of property, plant and equipment | **11,947** | 7,561 |
| Employee benefit expense (including directors' and chief executive's remuneration): | | |
| Wages, salaries, bonuses and allowances | **251,574** | 227,918 |
| Other social insurances and benefits | **7,424** | 13,327 |
| Pension scheme contributions | **4,590** | 9,565 |
| | **263,588** | 250,810 |

## 5. FINANCE COSTS

| | For the year ended 31 December | |
|---|---|---|
| | **2020** | 2019 |
| | **RMB'000** | RMB'000 |
| Interest on bank loans and other loans | **115,436** | 209,933 |
| Interest on corporate bonds | **—** | 12,665 |
| Interest on long term payables | **1,352** | 2,641 |
| | **116,788** | 225,239 |

## 6. INCOME TAX

| | For the year ended 31 December | |
|---|---|---|
| | **2020** | 2019 |
| | **RMB'000** | RMB'000 |
| Current - PRC | **—** | — |
| Deferred | **—** | 410 |
| Total tax charge/(credit) for the year from continuing operations | **—** | 410 |
| Current - PRC | **—** | — |
| Deferred | **—** | 217 |
| Total tax charge for the year from a discontinued operation | **—** | 217 |
| | **—** | 627 |

## 7. DIVIDENDS

The directors do not recommend the payment of any dividend for the year ended 31 December 2020 (2019: Nil).

## 8. EARNINGS PER SHARE ATTRIBUTABLE TO ORDINARY EQUITY HOLDERS OF THE PARENT

The basic earnings per share amounts are calculated by dividing the profit for the year attributable to ordinary equity holders of the parent, by the weighted average number of ordinary shares of 7,605,396,000 (2019: 6,354,400,000) in issue during the year.

The calculation of the diluted earnings per share amounts is based on the profit for the year attributable to ordinary equity holders of the parent of RMB406,680,000 (2019: RMB27,742,000). The weighted average number of ordinary shares used in the calculation is the number of ordinary shares in issue during the year, as used in the basic earnings per share calculation of 7,605,396,000 (2019: 6,354,400,000) shares, plus the weighted average number of ordinary shares assumed to have been issued at no consideration on the deemed exercise of warrants and dilutive potential ordinary shares.

No adjustment has been made to the basic earnings per share amounts presented for the year ended 31 December 2020 in respect of a dilution because the impact of the warrants and dilutive potential ordinary shares had an anti-dilutive effect on the basic earnings per share amounts presented.

The Group had no potentially dilutive ordinary shares in issue during the year ended 31 December 2020 (2019: Nil).

| | **Number of shares** | |
|---|---|---|
| | **For the year ended 31 December** | |
| | **2020** | 2019 |
| Weighted average number of ordinary shares in issue during the year used in the basic earnings per share calculation | **7,605,396,000** | 6,354,400,000 |
| Weighted average number of ordinary shares in issue during the year used in the diluted earnings per share calculation | **7,605,396,000** | 6,354,400,000 |

## 9. TRADE AND BILLS RECEIVABLES

| | As at 31 December 2020 RMB'000 | As at 31 December 2019 RMB'000 |
|---|---|---|
| Bills receivables | — | 450 |
| Trade receivables | **136,611** | 167,840 |
| Impairment | — | (1,172) |
| | **136,611** | 167,118 |

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:

| | As at 31 December 2020 RMB'000 | As at 31 December 2019 RMB'000 |
|---|---|---|
| Within 3 months | **136,611** | 164,346 |
| 4 to 6 months | — | 185 |
| 7 months to 1 year | — | 1,718 |
| Over 1 year | — | 869 |
| | **136,611** | 167,118 |

## 10. TRADE AND BILLS PAYABLES

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

| | As at | |
|---|---|---|
| | **31 December 2020** | 31 December 2019 |
| | **RMB'000** | RMB'000 |
| Within 3 months | **1,014,154** | 1,008,135 |
| 4 to 6 months | **512,573** | 294,595 |
| 7 to 12 months | **157,604** | 49,967 |
| 1 to 2 years | **9,466** | 5,961 |
| 2 to 3 years | **1,501** | 2,409 |
| Over 3 years | **4,150** | 4,817 |
| | **1,699,448** | 1,365,884 |

## MANAGEMENT DISCUSSION AND ANALYSIS

## INDUSTRIAL OVERVIEW

In 2020, China made remarkable achievements in overcoming the impact of COVID-19, coordinating epidemic prevention and control, and realizing economic and social development. Following the successful conclusion of the 13th Five-Year Plan, the 14th Five-Year Plan has been comprehensively rolled out. China witnessed accelerated establishment of a new development pattern, and implemented high-quality development. China took the lead in achieving positive growth among major economies in the world.

COVID-19 has not only brought challenges to the dairy industry, but also quietly changed the public's awareness of drinking milk. On the eve of the World Milk Day 2020, FrieslandCampina, China Dairy Industry Association and China International Exchange and Promotion Association for Medical and Healthcare jointly organized an online live forum on health protection in China, and published the "Chinese Milk Quotient Report 2020". The report showed that Chinese Milk Quotient (the "**Milk Quotient**") in 2020 was 62.7 points, 2 points higher than the previous year, and the improvement of people's milk drinking behavior contributed the most to the improvement of the Milk Quotient. The National Health Commission has issued dietary guidelines for COVID-19, suggesting that the general population should drink and eat 300g of dairy products every day.

On 21 February 2021, Document No. 1 of the Central Committee, *Certain Opinions of Central Committee of the Communist Party of China and the State Council on Comprehensively Promoting Rural Revitalization and Accelerating Agricultural and Rural Modernization*, was published. The document again emphasized "actively developing the cattle and sheep industry and continuing to implement the revitalization action of the dairy industry". Dairy industry is an important industry to implement "Healthy China" initiative, a representative industry of food safety, and a landmark industry of agricultural modernization. It can play a leading role in industrial integration and development. Inner Mongolia, located in 45 degrees north latitude, which is a high-quality golden milk source belt, is the country's largest dairy production area, with advantaged resources to develop diary industry.

To promote the national strategy of dairy industry revitalization, Inner Mongolia Autonomous Region made a target of reaching 3.5 million dairy stocks and 10 million tonnes of dairy production by 2025. Therefore, the Inner Mongolia Autonomous Region Government introduced relevant supporting policies, including increasing support for the combination of planting and breeding, increasing subsidies for dairy and livestock breeding facilities and equipment, strengthening the construction of milk source bases, promoting the transformation and upgrading of small and medium-sized farms, supporting dairy food processing with ethnic characteristics, providing land use policy support, and strengthening financial policy support to provide a strong boost to the development of the dairy industry.

At the 2020 CHINA DAIRY 20 SUMMIT, China Shengmu launched the three-year action plan of "Enabling Industrial Chain, Supply Chain Stability and Competitiveness". In the future, the dairy enterprises will continue to improve the industry through strong and practical actions, leading the development of the dairy industry to facilitate the revitalization of the dairy industry throughout the country, deliver the social responsibility of dairy enterprises and make efforts to protect the nutrition and health of the people in our country.

## PERFORMANCE OVERVIEW

As of 31 December 2020, the principal business of the Group was dairy farming business, production and sales of high-end desert-based organic raw milk and quality non-organic raw milk. The Group has committed to concentrating its resources on the production and sales of desert-based organic milk. At the same time, based on the diversified demand of customers for quality raw milk, the Company continued to develop functional raw milk to improve the profitability of the Company.

The Group adopted lean operation, had an insight into market demand, and timely transformed the conventional farms to organic ones to increasing the sales volume of organic milk. By implementing several management measures, such as enhancing per unit yield, decreasing cost and increasing efficiency, and expanding moderately, during the reporting period, the Group recorded after-tax profits of about RMB461.0 million (2019: RMB 135.7 million), an increase of RMB325.3 million over the last year. The Company ranked second in terms of market value growth rate among the 26 listed dairy enterprises in China in 2020.

On 31 July 2020, Start Great Holdings Limited (a wholly-owned subsidiary of China Mengniu) exercised its warrants and became the largest shareholder of the Company. In the future, the Group will further deepen the cooperation with China Mengniu and its subsidiaries (the "**Mengniu Group**"), optimize the layout of quality raw milk, strengthen the coordination of supply chain management, and achieve better operating results.

## BUSINESS REVIEW

As at 31 December 2020, the Group had 14 organic farms and 19 non-organic farms, including a fattening cattle farm. The Group had a total of 110,735 cows, including 58,889 organic cows and 51,846 non-organic cows. The Group continued to optimize the structure of cows by eliminating inefficient and ineffective cows, and improving the efficiency and self-reproduction rate of cows. The Company's cow structure is more reasonable, the reserve of cows is sufficient, and the size of cows has shown positive growth for the first time in the past three years.

### *Size of Herd*

Unit: Head

| | **As at 31 December** | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | **2020** | | | | | 2019 | | | | |
| | **Number of Farms** | **Milkable Cows** | **Calves and Heifers** | **Fattening Cattle (1)** | **Subtotal** | Number of Farms | Milkable Cows | Calves and Heifers | Fattening Cattle (1) | Sub-total |
| **Organic** | **14** | **32,309** | **26,580** | **—** | **58,889** | 11 | 24,459 | 20,343 | — | 44,802 |
| **Non-organic** | **19** | **25,349** | **24,036** | **2,461** | **51,846** | 23 | 34,966 | 26,306 | — | 61,272 |
| **Total** | **33** | **57,658** | **50,616** | **2,461** | **110,735** | 34 | 59,425 | 46,649 | — | 106,074 |

(1) For the data in this table for the current and previous years, the number of fattening cattle refers only to the cattle raised on a fattening cattle farm.

In 2020, the Group's key operating objectives were achieved better than expected. The annualized milk yield per milkable cow increased by 0.72 tonnes to 10.34 tonnes (2019: 9.62 tonnes), and the sales volume of organic milk was 285,000 tonnes, increasing by 10.4% over the previous year. The average external selling price of raw milk was RMB4,513/tonne (2019: RMB4,183/tonne), with a year-on-year increase of 7.9%. The gross profit of the dairy business amounted to RMB1,025.1 million (2019: RMB885.5 million), and the gross profit rate was 38.5% (2019: 35.5%).

## ORGANIC FORAGE

Through many years of dedicated investment in the Ulan Buh Desert, Bayannur Shengmu High-tech Ecological Forage Co., Ltd. ("**Shengmu Forage**") has currently built an organic forage base of over 220,000 mu. Shengmu Forage has built an organic fertilizer processing plant with an annual capacity of 70,000 tonnes and 7 liquid fertilizer plants. It has installed 328 fertilizing systems of organic liquid fertilizer for the planting base and built 9 cow dung processing plants with annual capacity of 250,000 cubic meters for the farms. Shengmu Forage is currently capable of satisfying the demand of organic forage planting for fertilizer. It has established a complete management system for planting organic forage, paving solid foundation for the development model of organic industry chain.

Shengmu Forage has established and fully implemented the corporate standard quality management systems of "Organic Forage" and "Organic Grass" to further establish an industrial standard. Through standardization of planting management, grass-to-glass organic tracking and organic product quality, Shengmu Forage has passed organic certification from authorized institutions within and outside the country for ten years consecutively and become the demonstration base for domestic large-scale organic planting industry.

## ORGANIC FARMING

In September 2020, Shengmu won the three-year "Demonstration Base of Asian Organic Agriculture Research and Development Center" jointly presented by Asia Organic Agriculture Research and Development Center and Beijing Continental Hengtong Certification Co., Ltd. (CHTC) for its unique organic breeding mode and excellent operation ability, which enhanced the brand influence of Shengmu.

## NUTRITION AND FEEDING WITH SCIENTIFIC FORMULATION

In respect of nutrition and feeding, the Group improved the production performance of dairy cows mainly through planting silage corn, alfalfa and other high-quality roughage in its own forage bases, and enhanced feed conversion efficiency through internally produced biological fermented forage. All kinds of premium feedstuff were fed through the "TMR Watch", a TMR monitoring system, to ensure balanced ration nutrition and healthy and high-yield dairy cows. At the same time, the Group introduced the world's latest feeding concept, established the Shengmu Research Institute with the team led by Li Shengli, the chief scientist of the National Dairy Industry and Technology System, and published the "three-year action implementation plan" of Shengmu High-Tech. The Group enhanced its core competitiveness by introducing the advanced feeding technology and feeding concept.

## SCIENTIFIC BREEDING AND HEALTHCARE

In respect of breeding, the Group conducted strategic cooperation with top three cow genetic breeding companies in the world. By selecting genetic materials of premium cows and applying genome detection techniques, the Group wanted to complete a 3-5 year herd genetic improvement plan, accelerate genetic progress, shorten generation interval, and breed Holstein cows with high quality and output. The Group built two national core breeding farms, in which it optimized the breeding process, introduced industry senior experts, strengthened the training of breeding technology, and improved the breeding index.

The Group joined the Calf and Heifer Organization, established an external think tank, closely connected with senior experts in the industry, and raised calves with the latest technology and the highest standard. In this year, the Group attached great importance to improving the welfare of calves and strengthening the comfort construction of calves, by providing sunshade and ventilation in summer, preventing wind and keeping warm in winter, and adding warm vests to each calf, which significantly increased the survival rate of calves, and dramatically strengthened the reserve of calves and heifers.

In respect of healthcare, the Group adopted many measures, such as optimization of daily food formula for dairy cows, emphasis on adjustment of rumen health, improvement of comfort of cowsheds, and enhancement of healthcare management process of dairy farms. Meanwhile, the Group worked together with top five global animal protection companies and top two domestic vaccine companies to make the animal benefit plan with the highest standard and the prevention and control of epidemic plan for dairy farms. As such, the Group can improve the positive immunity mechanism of herds and enhance the self immunity of dairy cows so as to control the culling rate of the dairy farms. Through cooperation with excellent animal protection companies, the Group actively carried out training and on site practical study and formulated a special subject on control of mastitis and a plan for prevention and control of limping disease, enhancing the healthcare effect and decreasing disease occurring rate, and effectively improving the body health of dairy cows and decreasing the culling rate. In 2020, the passive culling rate of the Group decreased by 6.0% over last year.

## CLIENT-ORINTED AND PRODUCT INNOVATION

In terms of product research and development, to meet the demand of domestic market consumption upgrade and dairy industry customers, the Group conducted independent research and development in the field of production, constantly broke through technology bottlenecks, and improved the fine forage processing and feeding technology. The Group has successfully developed DHA raw milk by self-transformation and metabolism of dairy cows fed DHA forage. The content of DHA in raw milk was above 15mg/100g. The DHA content of milk produced by biological enrichment is stable, which is easier for the absorption by human body. Innovations in the development of DHA natural functional milk have further improved the profitability of the Company.

## QUALITY AND SAFETY MANAGEMENT

Based on the concept of "providing globally most premium desert-based organic milk" as its mission, making reference to ten international and domestic standards such as AQ, Arlagarden, ISO9000, ISO22000 and ISO22002 as well as 52 laws and regulations and standards related to animal husbandry and breeding, China Shengmu has formulated a standard of "Shengmu Quality and Safety Management System for Dairy Industry and Farms" to cover dairy farm management and key parts in entirety. The standard involves management of 93 key control points in 4 categories including quality management of source of raw and auxiliary materials, health benefit of dairy cows, guarantee of milk quality and operating support, realizing an improving total quality management model based on clients with all staff engaged.

In respect of raw milk quality management, leveraging on the unique farming environment in the Ulan Buh Desert and the hardware configuration and management level in the dairy farms with large size, the Group formulated QP, QA, QC and QS management standards. With reference to GB13078 forage hygiene standard, the Group strictly assessed the source suppliers and checked for every batch of raw and auxiliary materials in dairy farms in order to guarantee the quality and prohibited entry of unqualified raw and auxiliary materials, ensuring that premium forage is supplied for dairy cows and improving the comfort of dairy cows to produce healthy and premium raw milk. The Group placed an emphasis on improving central inspection room in 2020, while increasing the frequency and tightening the standards of inspection, the Group had fully complied with the comprehensive internal risk investigation and prevention plan to completely eliminate quality risk and guarantee the quality of raw milk. The Group set an internal target to achieve the best quality of raw milk, improving quality of raw milk to Level S qualification rate (TBC≤30,000, SCC≤200,000)>92%. In 2020, with the average TBC of 10,000 and the average SCC of 150,000, the annual qualification rate reached 95%, far higher than the current EU standard and ranking a leading position at home and abroad.

## DIGITAL-BASED DEVELOPMENT AND INTERNAL MANAGEMENT UPGRADE

In July 2020, the Company concluded a cooperation agreement with UniDairy on the herd management system, and officially launched the UniDairy herd information system in September, which further upgraded the digital management of herd and improved the level of information management of the farms. In September 2020, the Company inked a strategic agreement with SAP, the world's top software service provider, to jointly build a digital platform for the whole industry chain of animal husbandry. After 119 days, SAP-ERP project of China Shengmu has been fully put into operation at the end of the year. The successful launch of the SAP-ERP project has improved the Company's overall management and control ability, process standardization ability, fine management ability and industrial collaboration ability, and opened a new digital chapter of building intelligent farms and enabling China's organic dairy industry.

## PRACTICE GOING GREEN AND ENVIRONMENTAL PROTECTION TO SUPPORT CIRCULAR AND ECOLOGICAL DEVELOPMENT

In 2020, the Group took initiative to conduct energy saving, consumption reduction and environmental protection. It replaced the fuel of heating boilers from coal to electricity to reduce carbon dioxide emissions, and removed original coal-fired boilers in 16 farms and used air source heat pumps for heating instead. By heat source transformation, the Group has reduced coal consumption by around 1,800 tonnes and carbon dioxide emissions by around 3,200 tonnes each year. In addition, the Group cooperated with suppliers of silage corn in terms of cow dung processing of farms. The cow dungs were supplied to its own organic fertilizer farms and silage corn suppliers. The Group adopted various cooperation modes to form a reasonable and sustainable planting-feeding integration agricultural production system with cow dung returning to the farm and forage grass feeding cows.

## FINANCIAL REVIEW

Immediately after the battle against COVID-19 began, the Group established a pandemic prevention and control group led by the senior management team, forming an internal top-down & bottom-up system characterized by timely decision making and rapid response. Combined with relevant government policies, the Group made full use of the advantages of centralized farms for materials dispatch and allocation and operational efficiency adjustment. As such, apart from the slight initial impact on transport and logistics, the Group's dairy farms generally maintained normal operation, with stable raw milk production and sales. The Group's cows, employees and operating results were not materially affected.

In 2020, the Group's revenue amounted to RMB2,660.8 million. The Group's gross profit margin increased by 1.9% from 36.6% in 2019 to 38.5% in 2020. The Group's profit after income tax increased by RMB325.3 million from RMB135.7 million in 2019 to RMB461.0 million in 2020, among which, profit attributable to owners of the parent company increased from RMB27.7 million in 2019 to RMB406.7 million in 2020, representing a net increase of RMB379.0 million or a growth rate of 1,365.9%.

## 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[2] | | | | |
|---|---|---|---|---|---|---|---|---|---|
| For the year ended 31 December | Segment revenue | Inter-segment sales | External sales | External sales as % of total revenue | Segment revenue | Inter-segment sales | External sales | External sales as % of total revenue | Total revenue |
| **2020** | **2,660,823** | **—** | **2,660,823** | **100.0%** | **—** | **—** | **—** | **—** | **2,660,823** |
| 2019 | 2,609,337 | 111,577 | 2,497,760 | 90.5% | 261,609 | — | 261,609 | 9.5% | 2,759,369 |

(1) Liquid milk business from January to April is included in the previous year in this table and tables below and related analysis throughout this section. Such presentation can reflect and analyze the operating condition and changes of the Group for the previous year more reasonably;

(2) Liquid milk business includes the discontinued liquid milk business. The figures for the previous year include figures of January to April before disposal of the liquid milk business.

In 2020, the Company's operating results were generally improved leveraging on the Group's well-stablished strategic partnership with Mengniu Group during the outbreak of pandemic, as well as various measures taken by the Group after the pandemic was alleviated, such as raising the raw milk price and adjusting the weight of the sales of organic milk upon a rapid recovery of dairy products market. The external sales of raw milk business of the Group increased from RMB2,497.8 million in 2019 to RMB2,660.8 million in 2020, representing an increase of 6.5% as compared to last year.

### *Dairy Farming Business*

| | For the year ended 31 December | | | | | | | |
|---|---|---|---|---|---|---|---|---|
| | **2020** | | | | 2019 | | | |
| | **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 | **1,459,267** | **285,073** | **5,119** | **54.8%** | 1,151,442 | 239,177 | 4,814 | 44.1% |
| Inter-segment sales[1] | **—** | **—** | **—** | **—** | 98,291 | 19,024 | 5,167 | 3.8% |
| Subtotal | **1,459,267** | **285,073** | **5,119** | **54.8%** | 1,249,733 | 258,201 | 4,840 | 47.9% |
| **Premium non-organic raw milk[2]** | | | | | | | | |
| External sales | **1,201,556** | **304,548** | **3,945** | **45.2%** | 1,346,318 | 362,072 | 3,718 | 51.6% |
| Inter-segment sales[3] | **—** | **—** | **—** | **—** | 13,286 | 3,585 | 3,706 | 0.5% |
| Subtotal | **1,201,556** | **304,548** | **3,945** | **45.2%** | 1,359,604 | 365,657 | 3,718 | 52.1% |
| **Dairy farming segment** | | | | | | | | |
| External sales | **2,660,823** | **589,621** | **4,513** | **100%** | 2,497,760 | 601,249 | 4,154 | 95.7% |
| Inter-segment sales | **—** | **—** | **—** | **—** | 111,577 | 22,609 | 4,935 | 4.3% |
| **Total** | **2,660,823** | **589,621** | **4,513** | **100.0%** | 2,609,337 | 623,858 | 4,183 | 100.0% |

(1) Represents self-produced organic raw milk sold to the Group's organic liquid milk business during the period from January to April 2019.

(2) The average selling price includes natively functional DHA milk.

(3) Represents self-produced premium non-organic raw milk sold to the Group's high-end non-organic liquid milk business during the period from January to April 2019.

In 2020, following the market development trend, the Group focused on its organic milk business and changed three dairy farms into organic farms during the year. Sales volume of raw milk increased from 258,201 tonnes in 2019 to 285,073 tonnes in 2020, representing an increase of 10.4%. Sales volume of non-organic milk in 2020 was 304,548 tonnes, including natively functional DHA milk of 12,784 tonnes.

In 2020, the average selling price of the Group's raw milk was RMB4,513/tonne, representing an increase of 7.9% as compared to that of last year. The average selling price of organic raw milk was RMB5,119/tonne, increasing by 5.8% as compared to last year; the average selling price of non-organic raw milk was RMB3,945/tonne, increasing by 6.1% as compared to last year.

*Cost of Sales, Gross Profit and Gross Profit Margin*

Unit: RMB in thousands, except percentages

| | For the year ended 31 December | | | | | |
|---|---|---|---|---|---|---|
| | **2020** | | | 2019 | | |
| | **Cost of sales Amount** | **Gross profit Amount** | **Gross profit margin** | Cost of sales Amount | Gross profit Amount | Gross profit margin |
| **Dairy farming business** | | | | | | |
| **Organic raw milk** | | | | | | |
| Before elimination | **800,699** | **658,568** | **45.1%** | 718,645 | 531,088 | 42.5% |
| After elimination (1) | **800,699** | **658,568** | **45.1%** | 665,391 | 486,051 | 42.2% |
| **Premium non-organic raw milk** | | | | | | |
| Before elimination | **835,006** | **366,550** | **30.5%** | 956,036 | 403,568 | 29.7% |
| After elimination (3) | **835,006** | **366,550** | **30.5%** | 946,866 | 399,452 | 29.7% |
| Subtotal | | | | | | |
| Before elimination | **1,635,705** | **1,025,118** | **38.5%** | 1,674,681 | 934,656 | 35.8% |
| After elimination | **1,635,705** | **1,025,118** | **38.5%** | 1,612,257 | 885,503 | 35.5% |
| **Liquid milk business** | | | | | | |
| **Organic liquid milk** | | | | | | |
| Before elimination | **—** | **—** | **—** | 167,728 | 71,339 | 29.8% |
| After elimination (2) | **—** | **—** | **—** | 120,868 | 118,199 | 49.4% |
| **Premium non-organic liquid milk** | | | | | | |
| Before elimination | **—** | **—** | **—** | 20,405 | 2,137 | 9.5% |
| After elimination(3) | **—** | **—** | **—** | 16,276 | 6,266 | 27.8% |
| **Subtotal** | | | | | | |
| Before elimination | **—** | **—** | **—** | 188,133 | 73,476 | 28.1% |
| After elimination | **—** | **—** | **—** | 137,144 | 124,465 | 47.6% |
| **Total after elimination** | **1,635,705** | **1,025,118** | **38.5%** | 1,749,401 | 1,009,968 | 36.6% |

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

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

In 2020, the gross profit margin of the Group's dairy farming business after elimination increased from 35.5% in 2019 to 38.5% in 2020, of which, the gross profit margin of organic raw milk business was 45.1%, increasing by 2.9% as compared to last year, and the gross profit margin of non-organic raw milk business was 30.5%, increasing by 0.8% as compared to last year. The increase was primarily due to: (1) the increase in the sales volume and adjustment to the structure of organic milk; and (2) the higher selling price of raw milk as compared to last year.

***Other Gains and Losses, Net***

In 2020, net losses generating from the Group's other gains and losses amounted to RMB44.5 million (2019: net gains of RMB69.3 million), mainly due to the inclusion of investment income of RMB85.8 million from the disposal of Shengmu Dairy in 2019.

***Selling and Distribution Expenses***

The Group's selling and distribution expenses primarily include logistics and transportation expenses and employees' remunerations. In 2020 and 2019, the Group's selling and distribution expenses amounted to RMB32.1 million and RMB131.1 million, respective. The significant decrease in 2020 as compared to 2019 was mainly due to the inclusion of January to April figures of the dairy company disposed of in previous year figures.

### *Administrative Expenses*

Administrative expenses mainly include salary and welfare, travel expenses and transportation expenses of management and administrative employees, as well as administrative expenses including attorney and audit fees. In 2020 and 2019, the Group's administrative expenses amounted to RMB111.7 million and RMB141.3 million, representing a decrease of approximately 20.9% as compared to last year, mainly due to the inclusion of audit and other intermediary fees incurred in respect of the disposal of dairy company last year and the administrative expenses incurred by the dairy company disposed of from January to April last year. In 2020 and 2019, administrative expenses accounted for 4.2% and 5.1% of revenue, respectively.

### *Finance Costs*

In 2020, the Group's finance costs amounted to RMB116.8 million (2019: RMB229.2 million), the decrease was mainly attributable to the facts that the Company repaid the entrusted loans of RMB1,370.0 million from Mengniu while further optimizing its debt structure by obtaining loans with low interest rates, which has led to a reduction in both the interest-bearing liabilities and the interest rates.

### *Loss Arising from Changes in Fair Value Less Costs to Sell of Biological Assets*

Loss arising from changes in fair value less costs to sell 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, the value of a heifer increases when it grows up to a milkable cow, 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 2020 and 2019, the Group's loss arising from changes in fair value less costs to sell of biological assets were RMB224.2 million and RMB284.9 million, respectively. Loss arising from changes in fair value less costs to sell of biological assets of the Group decreased in 2020 as compared to 2019, which was mainly due to the facts that great achievements have been made in the efforts of pandemic prevention and healthcare for herbs during the year, that the culling rate decreased as compared to last year and that some of the non-organic farms were changed to organic farms.

***Share of Losses of Associates***

The Group's associates include (a) Inner Mongolia Mengniu Shengmu High-tech Dairy Products Co., Ltd. (內蒙古蒙牛聖牧高科乳品有限公司) ("**Mengniu Dairy Company**") invested and owned as to 49% by the Group, which is primarily engaged in the operating and selling of Shengmu organic liquid milk brand; (b) Shengmu Forage in which the Group invested and held minority interests, and its subsidiary; (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, producing dairy products with the raw milk purchased from the Group; and (d) Inner Mongolia Yiyingmei Dairy Co., Ltd. (內蒙古益嬰美乳業有限公司) ("**Yiyingmei**"), in which the Group invested and held minority interests, producing high-end organic infant milk powder with the raw milk purchased from the Group in the future. It was originally a wholly-owned subsidiary of the Group and was owned as to a minority interest of 20% to the Group subsequent to the entering into of an equity transfer and unilateral capital increase agreement with Dabeinong Group on 11 September 2020. The Group recorded a share of the losses of the abovementioned associates for 2020 and 2019 of RMB35.6 million and RMB65.2 million, respectively.

***Income Tax Expense***

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.

The Group had no income tax expense in 2020, and the income tax expense in 2019 was RMB0.6 million.

***Profit Attributable to Owners of the Parent Company and Profit Attributable to Non-Controlling Interests***

In 2020, profit attributable to owners of the parent company of the Group was RMB406.7 million, representing a net increase of RMB379.0 million or a growth rate of 1,365.9% from a profit of RMB27.7 million in 2019, which was mainly attributable to (1) the stable increase in the selling price of the Group's raw milk as compared to last year; (2) the increase in the sales volume of organic milk as compared to last year due to the adjustment made to the structure of organic milk; (3) the significantly improved profitability of the Company through internal management upgrade and improvement of operating effectiveness; and (4) the Group completed the acquisition of minority interests in 12 joint venture farms by the end of 2019.

Profit attributable to non-controlling interests mainly represents the profit for the period attributable to dairy farmers with whom we cooperate in relation to dairy farm management in our farms. In 2020 and 2019, profit attributable to non-controlling interests was RMB54.3 million and RMB108.0 million, respectively.

## ANALYSIS ON CONSOLIDATED STATEMENT OF FINANCIAL POSITION

***Current Assets***

As at 31 December 2020, total current assets of the Group were RMB2,196.4 million (as at 31 December 2019: RMB1,783.3 million), primarily consisting of inventory of RMB715.1 million (as at 31 December 2019: RMB678.1 million), trade and bills receivables of RMB136.6 million (as at 31 December 2019: RMB167.1 million), prepayments, deposits and other receivables of RMB614.6 million (as at 31 December 2019: RMB614.1 million), cash and bank balances of RMB715.1 million (as at 31 December 2019: RMB310.2 million), and consumable biological assets of RMB15.0 million (as at 31 December 2019: RMB13.8 million). There was an increase in the Group's current assets as at 31 December 2020 as compared with that of 31 December 2019, which was mainly attributable to the increase of RMB404.9 million in the Group's cash and bank balances as compared with that at the beginning of the year due to the continued improvement of the Company's operating results.

### *Current Liabilities*

As at 31 December 2020, total current liabilities of the Group amounted to RMB3,275.3 million (as at 31 December 2019: RMB4,121.0 million), primarily consisting of trade and bills payables of RMB1,699.4 million (as at 31 December 2019: RMB1,365.8 million), other payables and accruals of RMB240.0 million (as at 31 December 2019: RMB574.8 million), interest-bearing bank and other borrowings and lease liabilities of RMB1,335.9 million (as at 31 December 2019: RMB2,177.1 million), and derivative financial instruments of nil (as at 31 December 2019: RMB3.3 million). The significant decrease in the Group's current liabilities as at 31 December 2020 compared to that as at 31 December 2019, was mainly due to the repayment of entrusted loans of RMB1,370.0 million from Mengniu in 2020, the decrease in interest-bearing liabilities as compared to last year and the receipt of a short-term borrowing (equivalent to RMB228.4 million) from J.P. Morgan at the end of the year.

### *Foreign Exchange Risk*

The Group's businesses are principally located in the mainland China and most transactions are conducted in RMB. As at 31 December 2020, the Group did not have significant foreign currency exposure from its operations, except for cash balances equivalent to approximately RMB228.4 million, RMB2.5 million and RMB0.1 million which were denominated in United States dollars, Hong Kong dollars and Euro, respectively. As at 31 December 2020, 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. Credit risk related to the Group's other financial assets arises from default of the counterparty with a maximum exposure equal to the carrying amounts of these instruments. Since the Group trades only with recognized and creditworthy third parties, collateral is generally not required.

***Charge on Assets***

As at 31 December 2020, the Group had pledged deposits of approximately RMB387.5 million (as at 31 December 2019: RMB177.5 million) in total to banks as deposits for the issuance of letters of credit and bank drafts. As at 31 December 2020, there was no pledge with the Group's entrusted loans (as at 31 December 2019: biological assets with fair value of approximately RMB945.7 million and partial interests in 13 wholly-owned subsidiaries and 2 non-wholly-owned subsidiaries with an aggregate net assets of RMB2,393.9 million were used as collaterals for the entrusted loans of the Group amounting to RMB1,370.0 million).

***Liquidity, Financial Resources and Capital Structure***

In 2020, the Group financed its daily operations mainly from internally generated cash flows and bank borrowings. In 2020, the Group had (a) cash and bank balances of RMB327.7 million (as at 31 December 2019: RMB132.6 million), and (b) interest-bearing bank and other borrowings of RMB1,366.3 million (as at 31 December 2019: RMB2,184.3 million), all denominated in RMB, of which, RMB30.4 million were repayable within one to five years, while the remaining interest-bearing bank and other borrowings were repayable within one year. Except bank and other borrowings equivalent to RMB41.7 million which are denominated in Euros, RMB228.4 million which are denominated in United State dollars and bear fixed interest rates, the Group's remaining bank and other borrowings are denominated in RMB and bear fixed interest rates. For the year ended 31 December 2020, the annual interest rate of bank loans ranged from 1.55% to 6.53% (for the year ended 31 December 2019: 1.55% to 12.97%).

### *Interest-Bearing Borrowings*

| | As at 31 December | | | |
|---|---|---|---|---|
| | **2020** | | 2019 | |
| | **Effective interest rate (%)** | **RMB'000** | Effective interest rate (%) | RMB'000 |
| **Current** | | | | |
| Bank loans – unsecured | **2.90-5.22** | **1,324,561** | 4.35-6.26 | 763,650 |
| Bank loans – secured | **—** | **—** | 5.66-6.09 | 1,370,000 |
| Current portion of long term bank and other borrowings – unsecured | **1.55** | **11,312** | 1.55 | 11,182 |
| | | **1,335,873** | | 2,144,832 |
| **Non-current** | | | | |
| Bank loans – unsecured | **1.55** | **30,398** | 1.55 | 39,443 |
| | | **1,366,271** | | 2,184,275 |

In 2020, with the constantly improved operating results, the increasingly adequate operating cash flow and the continuously improved external financing environment, the Company has proactively conducted debt restructuring and prepaid its entrusted loans of RMB1,370.0 million during the year. As a result, the Group's interest-bearing liabilities decreased to a reasonable level with significant reduction in the cost of fund seen, and the debt-to-asset ratio decreased from 63.5% in 2019 to 49.2% in 2020, thus bettering the assets and liabilities structure.

## ENVIRONMENTAL POLICIES AND PERFORMANCE

In 2020, 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.

## CAPITAL COMMITMENTS

As at 31 December 2020, the Group has no capital commitments in respect of the acquisition of property, plant and equipment (as at 31 December 2019: RMB81.1 million), which was mainly due to the inclusion of the data of the disposed Yiyingmei in that of 2019.

## HUMAN RESOURCES

As at 31 December 2020, the Group had a total of 2,589 employees (as at 31 December 2019: 2,668 employees). Total staff costs in 2020 (including the emoluments of Directors and senior management of the Company) amounted to RMB263.6 million (2019: RMB270.5 million).

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 and efficiency incentive 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.

## CONTINGENT LIABILITIES

As at 31 December 2020, the Group provided guarantees with amount of RMB94.6 million (31 December 2019: RMB80.0 million) and RMB14.5 million (31 December 2019: RMB65.4 million) for the bank borrowings of Shengmu Forage and Food Union Shengmu, respectively. The external guarantees provided by the Group were recognised in the financial statements on the basis of the valuation of the guarantees provided by the independent professional valuer regarded as the best estimates required to pay for the performance of the relevant current obligations in accordance with the requirements of IFRSs.

**Material Acquisitions and Disposals**

In 2020, (1) Shengmu Dairy, an associate in which the Group held a 49% equity interest, split its dairy product sales business into a newly established entity named Mengniu Dairy Company, which was owned as to 51% by the Mengniu Group and 49% by the Group. The Group has disposed of all its 49% equity interests (excluding the sales business) held in Shengmu Dairy, the original joint venture, to Mengniu Group; (2) the Group disposed of the 5.38% equity interest held in Food Union Shengmu to Food Union (Dairy) Hong Kong Limited; (3) on 29 May 2020, the Group completed the issuance of 688,705,234 shares at an issue price of HK$0.33 to pay the non-cash consideration for the acquisition of minority interests in 12 joint venture farms; and (4) on 11 September 2020 (after trading hours), the Group and Dabeinong Group entered into an equity transfer and capital increase agreement, pursuant to which, the Group would own 20% passively diluted minority interests in Yiyingmei upon its disposed of 70% equity interests in Yiyingmei, a wholly-owned subsidiary, to Dabeinong Group and upon Dabeinong Group unilaterally contributed additional capital to Yiyingmei. Except the above, the Company did not have any other significant acquisition and disposal of subsidiaries and associates.

The Group received the exercise notices from Start Great Holdings Limited (a wholly-owned subsidiary of China Mengniu) and Greenbelt Global Limited on 27 July and 31 July 2020, respectively, to subscribe for 1,197,327,890 shares and 140,862,105 shares at an exercise price of HK$0.33 per share. Upon subscription and issuance of the above-mentioned share, the total number of issued shares of the Company was 8,381,295,229. China Mengniu, through Star Great Holdings Limited, became the largest shareholder of the Company, holding 17.51% of issued shares of the Company.

**Future Plans for Material Investments or Acquisition of Capital Assets and Expected Source of Funding**

Save as disclosed above in "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

### *FOCUS ON CORE BUSINESSES TO REALIZE INNOVATION-DRIVEN DEVELOPMENT*

The Company will grasp the market opportunity, follow the consumption upgrading trend, and actively expand the overseas organic forage grass cooperation and certification business. It will bring together the global high-quality resources, strengthen its organic control ability, combine its own unique desert environment advantages, focus on the development of organic dairy industry, and continue to increase the output of high-end desert-based organic milk. In 2021, The Company plans to build 4 more organic farms to consolidate the absolute leading position of the Group in the organic field. According to the market demand, it will increase the input and conversion of DHA in farms, and plan to build 3 more DHA natural functional milk farms in 2021. At the same time, the Company will continue to develop and innovate functional milk through cutting-edge technology to meet customers' growing demand for high-end functional milk. The Company will plan to produce A2 milk containing rich A2- β -casein through genomic screening of herd through A2- β -casein gene, and further increase the profit contribution from scientific innovation.

### *CONTINUE TO ADOPT LEAN OPERATION AND COMPREHENSIVELY IMPROVE EFFICIENCY*

Upholding the management philosophy of "Cows First", and leveraging on the prenium resources of the Ulan Buh Desert, the Company will comprehensively improve the comfort level of dairy cows, improve the health level of dairy cows at all stages, and effectively extend the life of natural lactation of dairy cows. Through precise nutrition and feeding, the Company will strenghten fine welfare of dairy cows, and continue to improve the parity yield of dairy cows, thus, realizing increase in both the annual per unit yield and gross production.

The Company will continue to attach importance to the genetic improvement, and optimize the breeding system. By implementing the 3-5 year genetic improvement plan, the Company will breed core and high-quality herds, and realize the high-quality growth of the herd size.

## ***BUILD INTELLIGENT FARMS AND UPGRADE PRODUCTION EFFICIENCY***

The Company will continue to promote the Intelligent Shengmu strategy. Through SAP system and company information construction, the Company will improve the overall risk control ability, process standardization ability, fine management ability and industrial collaboration ability. It will establish the whole-process intelligent dairy farming system of the animal husbandry industry chain, and realize the standardized, data-oriented, informationized and intelligent management of the production process of dairy farming through digital information technologies, such as sharing and co-construction, interconnection and ecological development of animal husbandry, so as to improve the efficiency of cows, the production capacity of farms and the profitability of the Group.

## ***REALIZE BRANDING OF RAW MILK AND TAKE "SHENGMU INSIDE" AS A PROUD***

Leveraging on the innate advantages of "Being Natural, Pure and Healthy", the Group launched landmark certification and GAP certification, to create a strong brand value of "Desert-Based Organic Milk", and to make domestic high-end dairy products using Shengmu organic raw milk proud of "Shengmu Inside".

## ***PROMOTE THE CULTURE PLATFORM STRATEGY AND STIMULATE THE ENDOGENOUS DRIVING FORCE OF ENTERPRISE***

The Group makes constant efforts to promote the construction of corporate culture, consolidate the cultural foundation, sublimate the promotion and implementation of culture, and effectively promote the implementation of cultural values. In addition, the Group further promotes the three-level (the company, system and department) talent training system. The Group will continue to build a talent training platform and carry out high-quality training projects. It will improve the joint development mechanism, provide a solid talent guarantee for the fulfillment of corporate vision and strategic goals, and dig out the endogenous driving force for enterprise development.

## *ESTABLISH COOPERATION AND PARTNERSHIP TO BOOST SUSTAINABLE DEVELOPMENT*

In 2020, the Group submitted an application for its accession to The United Nations Global Compact (UNGC). In high recognition of the ten principles initiated by the UNGC covering issues such as human rights, labor standards, environment and anti-corruption, Shengmu has undertaken to fully response to the Sustainable Development Goals (SDG) of the United Nations during the process of strategy making and operation, so as to contribute to sustainable development worldwide in an cooperative, creative and innovative manner.

## 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 Company and its 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 31 December 2020.

## 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 31 December 2020.

## PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

For the year ended 31 December 2020, neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's shares.

## AUDIT COMMITTEE

The Company established the Audit Committee on 18 June 2014 in compliance with the Code. The Audit Committee was established with written terms of reference in compliance with the 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 9 April 2019. As at 31 December 2020, the Audit Committee comprised three independent non-executive Directors (Mr. WANG Liyan, Mr. FU Wenge and Mr. WU Liang) and was chaired by Mr. WANG Liyan.

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 2020.

## SCOPE OF WORK OF ERNST & YOUNG

The financial information in respect of the announcement of the Group's results for the year ended 31 December 2020 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 31 December 2020 (2019: Nil).

## ANNUAL GENERAL MEETING

The 2021 annual general meeting will be held on or before 30 June 2021. A notice convening the 2021 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 2020 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, 22 March 2021

*As at the date of this announcement, the executive directors of the Company are Mr. Yao Tongshan and Mr. Zhang Jiawang; the non-executive directors of the Company are Mr. Shao Genhuo, Mr. Zhao Jiejun, Mr. Sun Qian and Mr. Zhang Ping; and the independent non-executive directors of the Company are Mr. Fu Wenge, Mr. Wang Liyan and Mr. Wu Liang.*