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YuanShengTai Dairy Farm Limited **原生态牧业有限公司**

(Incorporated in Bermuda with limited liability)

(Stock Code: 1431)

REVISION OF ANNUAL CAPS FOR CONTINUING CONNECTED TRANSACTIONS UNDER THE 2020 FEIHE MASTER AGREEMENT

**Independent Financial Adviser to the Independent Board Committee
and the Independent Shareholders**



A letter from the Board is set out on pages 6 to 20 of this circular. A letter from the Independent Board Committee containing its recommendation to the Independent Shareholders is set out on pages 21 to 22 of this circular. A letter from Gram Capital, the Independent Financial Adviser, containing its advice to the Independent Board Committee and the Independent Shareholders is set out on pages 23 to 40 of this circular.

A notice convening the SGM of YuanShengTai Dairy Farm Limited to be held at EAST Beijing, Workshop 2, No. 22, Jiuxianqiao Road, Chaoyang District, Beijing, the PRC on Wednesday, 15 December 2021 at 10:00 a.m. is set out on pages 45 to 47 of this circular. Whether or not you are able to attend and vote at the meeting, you are requested to complete the accompanying form of proxy in accordance with the instructions printed thereon and return it to the branch share registrar and transfer office of the Company in Hong Kong, Computershare Hong Kong Investor Services Limited, at 17M Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, as soon as possible and in any event no later than 48 hours before the time appointed for the holding of the meeting (i.e. no later than 10:00 a.m. (Hong Kong time) on Monday, 13 December 2021) or any adjournment thereof. Completion and return of the form of proxy as instructed will not preclude you from subsequently attending and voting at the meeting or any adjourned meeting if you so wish.

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This circular is prepared in both English and Chinese. In the event of inconsistency, the English text of this circular will prevail.

DEFINITIONS

In this circular, unless the context otherwise requires, the following expressions have the following meanings:

“2013 Feihe Master Agreement”	a master agreement dated 1 November 2013 entered into between (a) Ruixinda and Ruixincheng on the one part and (b) Feihe Dairy HLJ (for itself and on behalf of its subsidiaries) in relation to the supply of raw milk
“2014 Announcement”	announcement of the Company dated 31 October 2014 in relation to, among others, the revision of the annual caps for the transactions contemplated under the 2013 Feihe Master Agreement
“2014 Circular”	circular of the Company dated 21 November 2014 in relation to, among others, the revision of the annual caps for the transactions contemplated under the 2013 Feihe Master Agreement
“2015 Announcement”	announcement of the Company dated 14 December 2015 in relation to, among others, the renewal of the 2013 Feihe Master Agreement and the proposed annual caps for the transactions contemplated under the 2015 Feihe Master Agreement
“2015 Circular”	circular of the Company dated 31 December 2015 in relation to, among others, the renewal of the 2013 Feihe Master Agreement and the proposed annual caps for the transactions contemplated under the 2015 Feihe Master Agreement
“2015 Feihe Master Agreement”	a master agreement dated 14 December 2015 entered into between (a) Ruixinda and Ruixincheng (for themselves and on behalf of their subsidiaries) on the one part and (b) Feihe Dairy HLJ and Feihe Gannan (for themselves and on behalf of their subsidiaries) in relation to the supply of raw milk
“2017 Announcement”	announcement of the Company dated 12 May 2017 in relation to, among others, the renewal of the 2015 Feihe Master Agreement and the proposed annual caps for the transactions contemplated under the 2017 Feihe Master Agreement
“2017 Circular”	circular of the Company dated 30 June 2017 in relation to, among others, the renewal of the 2015 Feihe Master Agreement and the proposed annual caps for the transactions contemplated under the 2017 Feihe Master Agreement

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“2017 Feihe Master Agreement”	a master agreement dated 12 May 2017 entered into between (a) the Company (for itself and on behalf of its subsidiaries) and (b) China Feihe (for itself and on behalf of its subsidiaries) in relation to the supply of raw milk
“2019 Announcement”	announcement of the Company dated 23 September 2019 in relation to, among others, the entering into of the 2020 Feihe Master Agreement and the proposed annual caps for the transactions contemplated under the 2020 Feihe Master Agreement
“2019 Circular”	circular of the Company dated 16 October 2019 in relation to, among others, the entering into of the 2020 Feihe Master Agreement and the proposed annual caps for the transactions contemplated under the 2020 Feihe Master Agreement
“2020 Feihe Master Agreement”	a master agreement dated 23 September 2019 entered into between (a) the Company (for itself and on behalf of its subsidiaries) and (b) China Feihe (for itself and on behalf of its subsidiaries) in relation to the supply of raw milk
“associate(s)”	has the same meaning ascribed to it under the Listing Rules
“Board”	board of Directors of the Company
“China Feihe”	China Feihe Limited (中國飛鶴有限公司), an exempted company incorporated in the Cayman Islands with limited liability on 26 October 2012, the ordinary shares of which are listed on the main board of the Stock Exchange
“Commencement Date”	the date on which the condition precedent to the 2020 Feihe Master Agreement is satisfied
“Company”	YuanShengTai Dairy Farm Limited (原生態牧業有限公司), an exempted company incorporated with limited liability under Bermuda Law on 1 May 2012, the ordinary shares of which are listed on the Main Board of the Stock Exchange
“connected person”	has the same meaning ascribed to it under the Listing Rules
“Director(s)”	director(s) of the Company
“Feihe Dairy Group”	the group of companies comprising China Feihe and its subsidiaries

DEFINITIONS

“Feihe Dairy HLJ”	Heilongjiang Feihe Dairy Co., Ltd.* (黑龍江飛鶴乳業有限公司), a company incorporated in the PRC, which is a wholly owned subsidiary of China Feihe
“Feihe Dairy International”	Feihe International, Inc., currently known as Flying Crane International Inc., an Independent Third Party and a company incorporated in the United States, whose securities were previously listed on the New York Stock Exchange
“Feihe Gannan”	Feihe (Gannan) Dairy Farm Limited* (飛鶴(甘南)乳品有限公司), a company incorporated in the PRC, which is a member of Feihe Dairy Group
“Feihe Master Agreements”	collectively, the 2013 Feihe Master Agreement, the 2015 Feihe Master Agreement and the 2017 Feihe Master Agreement
“Gram Capital” or “Independent Financial Adviser”	Gram Capital Limited, a licensed corporation to carry out Type 6 (advising on corporate finance) regulated activity under the SFO, being the independent financial adviser to the Independent Board Committee and the Independent Shareholders in respect of the transactions contemplated under the 2020 Feihe Master Agreement and the Proposed New Annual Caps
“Group”	the Company together with its subsidiaries
“HK\$”	Hong Kong dollars, the lawful currency of Hong Kong
“Hong Kong”	Hong Kong Special Administrative Region of the PRC
“Independent Board Committee”	the independent board committee of the Company formed to consider the transactions contemplated under the 2020 Feihe Master Agreement and the Proposed New Annual Caps
“Independent Shareholders”	Shareholders who are not required to abstain from voting at the SGM to approve the continuing connected transactions
“Independent Third Parties”	an individual(s) or a company(ies) who or which is/are not connected (within the meaning of the Listing Rules) with any Directors, chief executive or substantial Shareholders (within the meaning of the Listing Rules) of the Company, its subsidiaries or any of their respective associates

DEFINITIONS

“Indicative Price”	the latest indicative milk price determined quarterly by the Heilongjiang Fresh Milk Price Coordination Committee* (黑龍江省生鮮乳價格協調委員會)
“Latest Practicable Date”	22 November 2021, being the latest practicable date prior to the printing of this circular for ascertaining certain information in this circular
“Listing Date”	26 November 2013, being the date where dealings in the Shares first commence on the Main Board of the Stock Exchange
“Listing Rules”	Rules Governing the Listing of Securities on the Stock Exchange
“Original Annual Caps”	original annual caps in respect of the transactions contemplated under the 2020 Feihe Master Agreement for each of the three years ending 31 December 2022 as set out in the 2019 Circular
“PRC”	the People’s Republic of China, which for the purposes of this circular only, excludes Hong Kong, Macao Special Administrative Region and Taiwan
“Proposed New Annual Caps”	the proposed new annual caps in respect of the transactions contemplated under the 2020 Feihe Master Agreement for the two years ending 31 December 2021 and 31 December 2022 (including the 90% Limit)
“Prospectus”	prospectus of the Company dated 14 November 2013
“Ruixincheng”	Harbin Ruixincheng Commercial Trade Co., Ltd.* (哈爾濱市瑞信誠商貿有限公司), a wholly foreign owned enterprise incorporated in the PRC on 3 May 2013 and an indirect wholly owned subsidiary of the Company
“Ruixinda”	Harbin Ruixinda Dairy Farming Co., Ltd.* (哈爾濱市瑞信達牧業有限公司), a wholly foreign owned enterprise incorporated in the PRC on 9 December 2010 and an indirect wholly owned subsidiary of the Company
“SFO”	Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong)

DEFINITIONS

“SGM”	a special general meeting of the Company to be convened on 15 December 2021 to consider and approve the transactions contemplated under the 2020 Feihe Master Agreement and the Proposed New Annual Caps
“Share(s)”	ordinary share(s) of HK\$0.01 each in the capital of the Company
“Shareholder(s)”	registered holder(s) of ordinary share(s) of HK\$0.01 each in the capital of the Company
“Stock Exchange”	The Stock Exchange of Hong Kong Limited
“subsidiary(ies)”	has the same meaning ascribed to it under the Listing Rules

* *For identification purposes only*

LETTER FROM THE BOARD



YuanShengTai Dairy Farm Limited 原生態牧業有限公司

(Incorporated in Bermuda with limited liability)

(Stock Code: 1431)

Executive Directors:

Mr. Zhao Hongliang (趙洪亮)
Mr. Fu Wenguo (付文國)
Mr. Chen Xiangqing (陳祥慶)
Mr. Liu Gang (劉剛)

Non-executive Directors:

Mr. Leng Youbin (冷友斌)
Mr. Liu Hua (劉華)
Mr. Cai Fangliang (蔡方良)

Independent non-executive Directors:

Mr. Meng Jingzong (蒙靜宗)
Mr. Zhang Yuezhou (張月周)
Mr. Zhu Zhanbo (朱戰波)
Ms. Lin Jinping (劉晉萍)

Registered office:

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Hamilton HM 11
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*Head office and Principal Place of Business
in the PRC:*

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Kedong, Qiqihar
Heilongjiang Province
PRC

*Principal place of business
in Hong Kong:*

31/F, 148 Electric Road
North Point
Hong Kong

25 November 2021

To the Shareholders

Dear Sir or Madam,

REVISION OF ANNUAL CAPS FOR CONTINUING CONNECTED TRANSACTIONS UNDER THE 2020 FEIHE MASTER AGREEMENT

INTRODUCTION

We refer to the Prospectus, the 2014 Announcement, the 2014 Circular, the 2015 Announcement, the 2015 Circular, the 2017 Announcement, the 2017 Circular, the 2019 Announcement and the 2019 Circular, in relation to, among others, the continuing connected transactions under the Feihe Master Agreements and the 2020 Feihe Master Agreement, and the announcement of the Company dated 4 November 2021 in relation to the revision of annual caps under the 2020 Feihe Master Agreement.

LETTER FROM THE BOARD

The transactions contemplated under the 2020 Feihe Master Agreement constitute continuing connected transactions of the Company, and are subject to the reporting, announcement, annual review and independent shareholders' approval requirements under Chapter 14A of the Listing Rules.

The purpose of this circular is to provide you with (i) further information on the details of the 2020 Feihe Master Agreement, the transactions contemplated thereunder and the Proposed New Annual Caps; (ii) the letter of recommendation from the Independent Board Committee to the Independent Shareholders; (iii) the letter of advice from the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders; (iv) the notice of the SGM; and (v) other information as required under the Listing Rules.

PRINCIPAL TERMS OF THE 2020 FEIHE MASTER AGREEMENT

On 23 September 2019, the Company entered into the 2020 Feihe Master Agreement with China Feihe, a member of Feihe Dairy Group, to confirm the Group's supply of raw milk to Feihe Dairy Group for a term commencing from the Commencement Date and ending on 31 December 2022, subject to the terms and conditions contained therein. Other than the Proposed New Annual Caps, the principal terms of the 2020 Feihe Master Agreement remain the same as those disclosed in the 2019 Circular, which are summarised as follows:

- Date: 23 September 2019
- Parties: (a) the Company (for itself and on behalf of its subsidiaries); and
(b) China Feihe (for itself and on behalf of its subsidiaries).
- Contract period: The initial term of the 2020 Feihe Master Agreement shall commence from the Commencement Date and shall end on 31 December 2022. The 2020 Feihe Master Agreement may be extended for a period of three years after the expiry of the initial term, subject to approval of such extension and the transactions contemplated thereunder (including the related annual caps) by the Independent Shareholders (if required) in accordance with the Listing Rules.
- Condition precedent: The 2020 Feihe Master Agreement has become effective upon the approval of the 2020 Feihe Master Agreement and the transactions contemplated thereunder (including the Original Annual Caps relating thereto) by the Independent Shareholders in accordance with the provisions of the Listing Rules.
- Subject matter: Supply of raw milk by the Group to Feihe Dairy Group.

LETTER FROM THE BOARD

- Pricing term:** For each calendar year during the term of the 2020 Feihe Master Agreement, the Group and Feihe Dairy Group will enter into an annual sale contract specifying, among others, the pricing mechanism, the quantity and quality of raw milk expected to be purchased by Feihe Dairy Group during the calendar year and payment terms. The unit selling price of raw milk generally comprises two elements, being (i) the unit base price; and (ii) certain price adjustment factors including, among others, the microbe count, the level of protein content and fat content and the freezing point of raw milk. The unit selling price of raw milk will be negotiated by the parties on arm's length basis and in good faith with reference to the Indicative Price, the aforesaid adjustment factors and the prevailing market prices offered by the Group to its Independent Third Parties customers for products of similar quality. The terms and purchase prices offered by the Group to Feihe Dairy Group shall be no more favourable than those available to other Independent Third Parties customers.
- Priority:** In the event that the Group receives purchase orders from Feihe Dairy Group and other purchasers concurrently, the Group shall give priority to Feihe Dairy Group for purchase of raw milk on terms and conditions no less favourable to the Group than that offered by the other purchasers.
- Payment term:** Generally, to be settled on accrual basis, with a credit term of no more than one month, during which no interest will accrue.
- Early termination:** Both parties may, at any time during the continuance of the 2020 Feihe Master Agreement, give the other not less than three months' prior written notice to terminate the 2020 Feihe Master Agreement.

PRICING METHOD AND PROCEDURES

Under the 2020 Feihe Master Agreement, the Group will, by the end of each calendar year during the term, enter into an annual sales contract agreement (“**Sales Contract**”) with the Feihe Dairy Group to agree on, among others, the pricing mechanism of raw milk for the next calendar year.

The unit selling price for the raw milk sold by the Group is determined by the formula below:

$$\begin{array}{l} \text{Unit selling price of} \\ \text{raw milk} \end{array} = \begin{array}{l} \text{Base price of} \\ \text{raw milk (Note 1)} \end{array} + \begin{array}{l} \text{Adjustments taking into account} \\ \text{certain safety and} \\ \text{quality standards (Note 2)} \end{array}$$

Notes:

1. In determining the base price of raw milk, the parties to the Sales Contract take into account the Indicative Price determined quarterly by the Heilongjiang Fresh Milk Price Coordination Committee* (黑龍江省生鮮乳價格協調委員會).
2. The adjustment factors included, among others, the microbe count, the level of protein content and fat content and the freezing point of raw milk.

LETTER FROM THE BOARD

The Group's pricing mechanism with its customers (including Feihe Dairy Group and other Independent Third Party customers of the Group) are generally the same, and therefore the selling price of the raw milk contemplated under the 2020 Feihe Master Agreement would be no less favourable than that of the other Independent Third Party customers of the Group.

In order to ensure that the terms of sales of raw milk to Feihe Dairy Group (including the unit selling price) would be on normal commercial terms and on terms no less favourable to the Group than those offered to Independent Third Party customers, the Group has adopted the following pricing procedures:

- (1) the Group will check the latest Indicative Price on a quarterly basis;
- (2) due to the super premium quality of the Group's raw milk and the resulting demand from the Group's customers for the production of their high-end dairy products, the Group has been able to charge raw milk prices that are higher than the Indicative Price. In determining the unit base price of the raw milk to be sold, the Group will take into account the correlation between and trends of the historical and latest Indicative Prices and unit base prices of raw milk to the Feihe Dairy Group and the Group's other Independent Third Party customers;
- (3) the Group will check with laboratories of the Group to ascertain the actual safety and quality standard of the raw milk of the Group to be sold, such as the microbe count, the level of protein content and fat content and the freezing point of raw milk. In determining the extent of adjustment to the unit base price attributable to these adjustment factors, the Group will take into account the correlation between and trends of the historical selling prices of raw milk of comparable safety and quality standard to the Feihe Dairy Group and the Group's other Independent Third Party customers;
- (4) similar to other customers of the Group, Feihe Dairy Group may, from time to time after noting any change in the market conditions and the demand and supply of raw milk, issue a price adjustment notice to the sales department of the Group to request for adjustment to the unit selling price of raw milk. Upon receiving such notice, the sales department of the Group shall seek approval from both of the deputy general manager in charge and the general manager of the Group for the relevant price adjustment. For the purpose of determining whether the price adjustment request is justifiable, the deputy general manager in charge and the general manager of the Group, who are experienced in the dairy farming industry, will, among others, (i) take into account the correlation between and trends of the historical and latest Indicative Prices and selling prices of raw milk to the Feihe Dairy Group and Independent Third Party customers; and (ii) check with laboratories of the Group to ascertain the actual quality of the raw milk of the Group to be supplied, and will take into account the correlation between and trends of the historical selling prices of raw milk of comparable safety and quality standard to the Feihe Dairy Group and the Group's other Independent Third Party customers. Subject to obtaining of such approval, the price of the raw milk sold by the Group to Feihe Dairy Group may be adjusted.

LETTER FROM THE BOARD

Apart from the price adjustment controls as stated above, designated members of the Group's senior management, namely deputy general manager in charge of sales department and general manager, will (i) review the raw milk price agreed between the Group and Feihe Dairy Group on a monthly basis, and compare it with the raw milk prices (of similar quality and during the same period of time) being agreed between the Group and other Independent Third Party customers, and (ii) review other trading terms of purchase orders received from Feihe Dairy Group and other Independent Third Party customers, to ensure that (a) the unit selling prices of raw milk for all of the Group's customers remain comparable, (b) other trading terms offered by Feihe Dairy Group, such as base price, adjustment factor, payment term and driving distance, are no less favourable to the Group than that offered by the other Independent Third Party customers; and (c) the contemplated transactions between the Feihe Dairy Group and our Group are conducted on normal commercial terms.

Taking into account that (i) the Group's pricing mechanism with its customers (including Feihe Dairy Group and other Independent Third Party customers of the Group) are generally the same, and that the selling price of the raw milk contemplated under the 2020 Feihe Master Agreement would be no less favourable than that of the other Independent Third Party customers of the Group; and (ii) the Group's policy on review of raw milk prices agreed between the Group and its customers (including Feihe Dairy Group) as mentioned above, the Directors consider such pricing mechanism will be able to ensure the transactions contemplated under the 2020 Feihe Master Agreement be conducted on normal commercial terms and on terms no less favourable to the Company than terms available to Independent Third Parties.

REVISION OF ANNUAL CAPS

The Company currently estimates that given the expected increase in the overall sales volume of Feihe Dairy Group and the expected increase in demand from Feihe Dairy Group in respect of the purchase of raw milk from the Group, the annual transaction amounts under the 2020 Feihe Master Agreement for the years ending 31 December 2021 and 31 December 2022 are expected to exceed the Original Annual Caps. As such, the Company intends to revise the annual caps for the years ending 31 December 2021 and 31 December 2022 under the 2020 Feihe Master Agreement in respect of the sale of raw milk by the Group to Feihe Dairy Group.

The historical transaction amounts contemplated under the 2020 Feihe Master Agreement accounted for 83.6% and 89.3% of the revenue of the Group for the year ended 31 December 2020 and for the nine months ended 30 September 2021, respectively. As of the Latest Practicable Date, the transaction amounts of the continuing connected transactions under the 2020 Feihe Master Agreement have not exceeded the Original Annual Caps for the year ending 31 December 2021 as disclosed in the 2019 Circular.

LETTER FROM THE BOARD

The Original Annual Caps

The following table sets out the Original Annual Caps set out in the 2019 Circular and the historical transaction amount in respect of the transactions contemplated under the 2020 Feihe Master Agreement for the year ended 31 December 2020 and the nine months ended 30 September 2021:

	Original annual caps <i>(RMB million)</i>	Historical transaction amount <i>(RMB million)</i>	Utilisation rate of original annual caps
Year ended 31 December 2020	1,300	1,299	99.9%
Year ending 31 December 2021	1,400	1,162 <i>(note)</i>	83.0%
Year ending 31 December 2022	1,500	–	–

Note: Unaudited figure for the nine months ended 30 September 2021

The Proposed New Annual Caps

The following table sets out the Proposed New Annual Caps in respect of the transactions contemplated under the 2020 Feihe Master Agreement for each of the two years ending 31 December 2022, which represent 103.0% and 128.7% of the actual revenue of the Company for the year ended 31 December 2020, respectively:

Year ending 31 December	Annual cap for the sales of raw milk to Feihe Dairy Group pursuant to the 2020 Feihe Master Agreement <i>(RMB million)</i>
2021	1,600
2022	2,000

The Proposed New Annual Caps in respect of the transactions contemplated under the 2020 Feihe Master Agreement have been determined with reference to:

- the historical sales volume in respect of the sales of raw milk contemplated under the 2020 Feihe Master Agreement for the year ended 31 December 2020 and the six months ended 30 June 2021, which are approximately 299,854 tonnes and 176,015 tonnes, respectively;
- the projected sales volume of raw milk by the Group to Feihe Dairy Group for each of two years ending 31 December 2022, which are currently expected to be approximately 324,000 tonnes and 396,000 tonnes, respectively;

LETTER FROM THE BOARD

- c) the prospect of the PRC domestic dairy industry following the introduction of the three-child policy by the PRC government and Action Plan for the Promotion of Domestic Infant Milk Formula (國產嬰幼兒配方乳粉提升行動方案) unveiled by the National Development and Reform Commission of China, aiming to increase the portion of domestically manufactured infant milk formula in China with a target to remain a 60% self-sufficient level in the industry, and to encourage the use of fresh milk in the production of infant milk formula;
- d) the prevailing and expected future market price of raw milk. The average Indicative Price increased by approximately 6.85% during the first two quarters of 2021 when compared to the corresponding period in 2020. According to the research reports issued by China International Capital Corporation Limited in February 2021 and August 2021, it is expected that the shortage of raw milk supply will last till 2022 and the price of raw milk will continue to increase in 2022. Therefore, the Company expects that the price of raw milk will continue to increase steadily during each of the two years ending 31 December 2022 which is currently expected to be around RMB4,700 and RMB4,850 per tonne, respectively; and
- e) a buffer of around 5% to cover any unforeseen circumstances, for instance, the unexpected increment of the market price of raw milk, the inflation rate in the PRC and unexpected substantial increase in demand of raw milk by Feihe Dairy Group.

Level of Contribution

Based on the Proposed New Annual Caps, it is expected that the revenue contribution from Feihe Dairy Group as a percentage of the Group's total revenue may reach around 90% for the two years ending 31 December 2021 and 2022. The Company undertakes not to generate more than 90% of its annual revenue in 2021 and 2022 from China Feihe (the "90% Limit"), such that this 90% Limit shall form part of the Proposed New Annual Caps in addition to the numerical figures.

The Company will closely monitor the transaction amounts in respect of the transactions contemplated under the 2020 Feihe Master Agreement through the following measures:

- a) the Company will have designated personnel from the relevant departments to monitor the actual transaction amounts and report to the management team on a monthly basis in relation to the transactions to ensure that the Proposed New Annual Caps are not exceeded;
- b) The finance department of the Company will perform half-yearly reporting of the actual transaction amounts; and
- c) The auditors and the independent non-executive Directors of the Company will conduct annual review on the connected transactions in accordance with the Listing Rules.

LETTER FROM THE BOARD

Meanwhile, the finance department of Company has also been collecting and preparing the management account of the Company on a monthly basis to keep track of its total revenue. The management team of the Company will compare the transaction amount with China Feihe with the total revenue of the Company every month to get to know the revenue contribution of China Feihe. The Company's internal control measures, including the monitoring on the revenue from Feihe Dairy Group, have been working effectively. The Company was fully aware of the amount and contribution of the revenue generated from China Feihe in 2020. However, given the Company was of the view that its annual cap for 2020 was RMB1,300 million while the 70% level was only an expectation of the Board based on the information it had as of the date of the 2019 Circular, the Company decided to increase its raw milk supply to China Feihe to above 70% of its revenue due to (i) the unstable and unpredictable market environment caused by COVID-19 in 2020, (ii) the strong demand of China Feihe; (iii) normal commercial terms offered by China Feihe, and (4) limited useful life of our raw milk. Accordingly, it is believed that the Company's internal control measures will continue to work effectively and ensure that the revenue contribution from Feihe Dairy Group will not exceed 90% for the years ending 31 December 2021 and 2022.

The Company also undertakes that if the actual revenue for 2021 and 2022 fail to reach the expected level, it will correspondingly reduce or suspend the transactions with China Feihe and supply the remaining raw milk to third party customers to ensure that the 90% Limited is fully complied with. As the sale amount of raw milk for the last quarter of each year could generally take up more than 20% of the total sale amount for each year, the Company plans to review the percentage of revenue contribution from China Feihe and the Group's actual revenue for the first three quarters in early October in each year. If the revenue contribution from China Feihe exceeds 90%, the Company will adjust its sale strategy for the last quarter and reduce or suspend the transactions with China Feihe to ensure that the 90% Limited is fully complied with. Based on the review conducted for the year of 2021, the revenue from Feihe Dairy Group accounted for 89.3% of the Group's total revenue for the first three quarters of 2021. The Company will keep monitoring the sales of raw milk to Feihe Dairy Group for the last quarter of 2021.

REASONS AND BENEFITS FOR THE CONTINUING CONNECTED TRANSACTIONS

Feihe Dairy Group has been the Group's largest customer for five consecutive years since 2017, and it has experienced sustainable and fast growth in recent years. Along with Feihe Dairy Group's fast business growth, its demand for raw materials such as raw milk has also been increasing over the years and the Proposed New Annual Caps are in line with the fast business growth of Feihe Dairy Group. The Board believes that the sales of raw milk to Feihe Dairy Group is important to the business of the Group. It is expected that the long-term and continuing supply of raw milk products to Feihe Dairy Group will further enhance the stability of the Group's customer base and ensure future demand for the Group's raw milk product.

LETTER FROM THE BOARD

The Board considers that, by adopting the Proposed New Annual Caps, the Group is not unduly reliant on the Feihe Dairy Group for the following reasons:

(a) Mutually beneficial and complementary relationship

The Group is the largest supplier of raw milk for Feihe Dairy Group in 2020, offering excellent geographical advantages given the Group's farms are in close proximity of Feihe Dairy Group's downstream processing plants, which enables the freshness of the fresh milk supplied to be optimally preserved. For the year ended 31 December 2020 and the nine months ended 30 September 2021, the raw milk purchased by Feihe Dairy Group from the Group accounted for 92.4% and 89.6% of the total amount of raw milk purchased by Feihe Dairy Group. At the same time, Feihe Dairy Group is also the largest customer of the Group in 2020, providing a stable source of revenue for the Group. For the year ended 31 December 2020 and the nine months ended 30 September 2021, Feihe Dairy Group contributed approximately 83.6% and 89.3% of the Group's total revenue, respectively.

As the largest and leading infant milk formula manufacturer in the PRC, Feihe Dairy Group has stringent quality control requirements in respect of, among others, the hygiene and safety conditions of the dairy cows of its suppliers and requires the raw milk supplied by its suppliers to meet high quality standards. Besides, given the perishable nature of raw milk, in order to maintain its freshness and to minimise the risk of contamination, it is not feasible for Feihe Dairy Group to either keep significant inventory of raw milk, or to procure raw milk from suppliers which are too far away. It will also cause substantial costs for Feihe Dairy Group to communicate and purchase raw milk from a large number of mid to small size dairy farms. In terms of herd size and production volume, the Company is one of the leading dairy farming companies in the PRC and it has a strong supply capacity in high-quality raw milk. As of 30 June 2021, the Group had 7 dairy farms in operation with 72,321 dairy cows, and for the year ended 31 December 2020, the total sales volume of raw milk of the Group amounted to 355,599 tonnes. As the Group is one of the limited number of raw milk suppliers in Heilongjiang, the PRC with over 70,000 dairy cows and the capability of producing super premium raw milk and considering the long-term and close relationship with the Group, it is natural and advisable for Feihe Dairy Group to choose to procure more raw milk from the Group to meet its strong and increasing demand. For the year ended 31 December 2020 and the nine months ended 30 September 2021, Feihe Dairy Group's purchases from the Group amounted to RMB1,299 million and RMB1,162 million, respectively.

Based on the above-mentioned reasons, it is believed that the business relationship between Feihe Dairy Group and the Group is mutually beneficial and Feihe Dairy Group and the Group are mutually reliant on each other. It is beneficial to the Group in securing stable and long-term demand from Feihe Dairy Group, a high-quality customer and leading player in China's infant formula industry, and also strategically important to Feihe Dairy Group by ensuring a source of high-quality raw milk for producing high-end infant formula products.

LETTER FROM THE BOARD

(b) Solid long-term relationship and extremely low risk of termination

Feihe Dairy Group has maintained solid and long-term business relationship with the Group in order to ensure the security of the raw milk supplies. Since the Group started to supply super premium raw milk in 2010, Feihe Dairy Group has been the Group's major customer for more than ten years.

High quality and stable fresh milk supply is essential to the continued success of Feihe Dairy Group's infant milk formula products. In order to further strengthen Feihe Dairy Group's leading position in high-end infant milk formula market and provide enhanced protection and security on the future raw milk supplies, Feihe Dairy Group acquired 3,342,320,920 Shares of the Company through a conditional voluntary general offer in 2020, representing approximately 71.26% of the total issued share capital of the Company.

Taking into consideration the above-mentioned factors, it is highly certain that Feihe Dairy Group and the Group will maintain a stable and long-term business relationship, and there is an extremely low risk that the relationship between Feihe Dairy Group and the Group will materially adversely change or terminate.

(c) In line with the fast business growth of Feihe Dairy Group

Feihe Dairy Group has experienced sustainable and fast growth in the recent years. For the year ended 31 December 2019, Feihe Dairy Group's total revenue was RMB13,721.5 million, representing an increase of 32.0% as compared to last year. For the year ended 31 December 2020, Feihe Dairy Group's total revenue was RMB18,592.5 million, representing an increase of 35.5% as compared to last year. For the six months ended 30 June 2021, Feihe Dairy Group's revenue was RMB11,543.8 million, representing an increase of 32.6% as compared to the same period last year. Along with Feihe Dairy Group's fast growth in sales of infant milk formula products, its demand for raw materials such as raw milk has also been increasing over the years. For the year ended 31 December 2020, Feihe Dairy Group's total purchase of raw milk amounted to RMB1,406 million, representing an increase of 41.3% as compared to last year. For the six months ended 30 June 2021, Feihe Dairy Group's total purchase of raw milk amounted to RMB903 million, representing an increase of 29.4% as compared to the same period last year.

Therefore, the Proposed New Annual Caps are also in line with the fast business growth of Feihe Dairy Group. Upon the approval of the Proposed New Annual Caps, Feihe Dairy Group could benefit from more transactions under the 2020 Feihe Master Agreement to satisfy its increasing demand for high quality raw milk and secure a stable supply, and the Group could also benefit from a stable and strong source of revenue.

LETTER FROM THE BOARD

(d) Strong capability to develop dairy farms

Thanks to the long-term operation experience in the dairy market and good leadership skills of the management team, the Company has developed a strong capability to develop its own dairy farms. Other than Gannan Farm and Kedong Heping Farm which were acquired from China Feihe in 2011, the Company has developed all the remaining five dairy farms in operation by itself.

The table below sets out the percentage of total sale volume of raw milk produced by the dairy farms acquired from China Feihe to the total sale volume of raw milk produced by the Group for each of the three years ended 31 December 2020 and the six months ended 30 June 2021:

	Total sale volume of raw milk produced by the two dairy farms acquired from China Feihe (tonnes)	Total sale volume of raw milk produced by the Group (tonnes)	Percentage
Year ended 31 December 2018	62,722	282,261	22.2%
Year ended 31 December 2019	67,685	334,424	20.2%
Year ended 31 December 2020	87,967	355,599	24.7%
Six months ended 30 June 2021	53,451	179,824	29.7%

(e) Limited priority arrangement

The change in relationship with China Feihe has not and would not result in material impact to the Company. The Company is still able to maintain and develop its business relationship with other customers other than China Feihe, and the Company could sell its raw milk to other customers other than China Feihe who offered better terms. Under the priority arrangement, the Group will only give priority to Feihe Dairy Group for purchase of raw milk when the terms and conditions offered by Feihe Dairy Group are no less favourable than that offered by the other purchasers. In addition, China Feihe has undertaken to the Company that the Company is allowed to suspend the priority arrangement when it needs to sell more raw milk to third party customers for the purpose of complying with the 90% Limit.

LETTER FROM THE BOARD

(f) Reduction of reliance

It is also believed that the Company is able to reduce the percentage of revenue contribution from China Feihe for the following reasons:

- (i) regardless of the increase in the sales of raw milk to China Feihe, the Company will still maintain and develop its business relationship with other customers other than China Feihe;
- (ii) due to the strong demand for high quality raw milk in the PRC market over the years, it is relatively easy for the Company to find alternative customers for its raw milk if it wants to reduce the sales of raw milk to China Feihe;
- (iii) the actual designed capacity of the seven dairy farms currently operated by the Group is 90,000 dairy cows. Driven by the advanced management model of our farms, the number of dairy cows of the Group's dairy farms increased from 65,886 heads as of 30 June 2020 to 72,321 heads as of 30 June 2021. There is still considerable potential for the Company to further increase the number of dairy cows in the existing seven farms, which will help increase the raw milk production; and
- (iv) in order to seize the market opportunities, the Company is planning the construction of two new farms with a total designed capacity of 22,000 dairy cows to further expand the Company's production and overall scale of operation. In addition, the Company has entered into two agreements to acquire a dairy farm with around 1,500 dairy cows and a dairy farm (without any dairy cows) with a designed capacity of 10,000 dairy cows, respectively. Upon the further expansion of its production capacity, it is believed that the Company will be able to not only satisfy the demand from China Feihe but also increase its supply of raw milk to other customers who are also in need of high quality raw milk, which will naturally elevate the percentage of revenue contribution from other customers and reduce the percentage of revenue contribution from China Feihe.

(g) Common market practice in the dairy industry

The upstream and downstream industry players in China's dairy industry are highly interdependent. On the one hand, as the competitive landscape in the downstream market of China's dairy industry has been increasingly concentrated, raw milk suppliers mainly sell their products to a limited number of top dairy products manufacturers in the downstream. On the other hand, large-scale dairy products manufacturers generally incline to establish long-term and stable relationships with trustful raw milk suppliers in the upstream to secure stable supply and product safety and quality. It is a common market practice in the dairy industry in China for a dairy farming company to have a high customer concentration.

The Directors (including the independent non-executive Directors after having considered the Independent Financial Adviser's advice, and excluding Mr. Leng Youbin, Mr. Liu Hua, Mr. Cai Fangliang, Mr. Liu Gang and Ms. Liu Jinping) consider that the 2020 Feihe Master Agreement are on normal commercial terms, fair and reasonable and in the interests of the Company and the shareholders as a whole, and that the Proposed New Annual Caps are fair and reasonable and in the interests of the Company and the shareholders as a whole.

LETTER FROM THE BOARD

Each of Mr. Leng Youbin, Mr. Liu Hua and Mr. Cai Fangliang has abstained from voting at the relevant Board meeting for the approval of the 2020 Feihe Master Agreement (including the Proposed New Annual Caps) due to their positions as executive director of China Feihe and their shareholding in China Feihe. Mr. Liu Gang, being a younger brother of Mr. Liu Hua, has abstained from voting at the relevant Board meeting for the approval of the 2020 Feihe Master Agreement (including the Proposed New Annual Caps) to avoid any potential conflicts of interest. Ms. Liu Jinping, being an independent non-executive Director, is also an independent non-executive director of China Feihe and has abstained from voting at the relevant Board meeting for the approval of the 2020 Feihe Master Agreement (including the Proposed New Annual Caps) to avoid any potential conflicts of interest. Save as disclosed above, none of the other Directors has a material interest in the transactions contemplated under the 2020 Feihe Master Agreement or is required to abstain from voting on the relevant resolutions of the Board.

IMPLICATIONS OF THE LISTING RULES

As of the date of this announcement, China Feihe holds approximately 71.26% of the total issued share capital of the Company. Therefore, China Feihe is the controlling shareholder of the Company and hence a connected person of the Company. Thus, the transactions contemplated under the 2020 Feihe Master Agreement constitute connected transactions of the Company pursuant to Chapter 14A of the Listing Rules.

As the applicable percentage ratios under the Listing Rules in respect of the highest Proposed New Annual Caps under the 2020 Feihe Master Agreement will exceed 25%, the 2020 Feihe Master Agreement and the transactions contemplated thereunder are subject to the reporting, announcement and the independent shareholders' approval requirement under Chapter 14A of the Listing Rules.

The Company will convene a SGM to seek approval from the Independent Shareholders in respect of the continuing connected transactions under the 2020 Feihe Master Agreement (including the Proposed New Annual Caps). An Independent Board Committee has been formed to advise the Independent Shareholders on the proposed revision of the annual caps. The Independent Board Committee has also approved the appointment of Gram Capital as the independent financial adviser to advise the Independent Board Committee and Independent Shareholders in this regard.

The Company will continue to monitor the Group's actual amount of sales to Feihe Dairy Group under the 2020 Feihe Master Agreement against the Original Annual Caps to ensure it will not be exceeded before the relevant Independent Shareholders' approval could be obtained at the proposed SGM.

LETTER FROM THE BOARD

GENERAL INFORMATION

The Company

The Company is a dairy farming company in the PRC dedicated to the production of super premium raw milk. The ordinary shares of the Company are listed on the main board of the Stock Exchange.

Feihe Dairy Group

Feihe Dairy Group is based in Heilongjiang province and is principally engaged in the production and sale of infant formula products in the PRC. The ordinary shares of China Feihe are listed on the main board of the Stock Exchange. As of the date of this announcement, China Feihe holds approximately 71.26% of the total issued share capital of the Company. Therefore, China Feihe is the controlling shareholder of the Company and hence a connected person of the Company.

SGM

A resolution approving the transactions contemplated under the 2020 Feihe Master Agreement and the Proposed New Annual Caps relating thereto shall be proposed at the SGM.

A notice convening the SGM to be held at EAST Beijing, Workshop 2, No. 22, Jiuxianqiao Road, Chaoyang District, Beijing, the PRC on Wednesday, 15 December 2021 at 10:00 a.m. is set out on pages 45 to 47 of this circular.

In accordance with the Listing Rules, any connected person or Shareholder and its associates with a material interest in the 2020 Feihe Master Agreement and the transactions contemplated thereunder must abstain from voting on the resolution to approve the revision of the annual caps for the years ending 31 December 2021 and 31 December 2022 for the continuing connected transactions contemplated under the 2020 Feihe Master Agreement at the SGM.

China Feihe, being a connected person of the Company with material interests in the 2020 Feihe Master Agreement, will abstain from voting at the SGM on the ordinary resolution to approve the transactions (together with the Proposed New Annual Caps thereof) contemplated under the 2020 Feihe Master Agreement. The Board confirms that China Feihe, who will abstain from voting on the resolution approving the transactions contemplated under the 2020 Feihe Master Agreement, controls the voting rights in respect of its Shares of the Company.

The voting of the SGM will be taken by poll.

A form of proxy for the SGM is enclosed herewith. Whether or not Shareholders are able to attend and vote at the SGM, they are requested to complete the enclosed form of proxy and return the same to the branch share registrar and transfer office of the Company in Hong Kong, Computershare Hong Kong Investor Services Limited, at 17M Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong in accordance with the instructions printed thereon as soon as possible and in any event no later than 48 hours before the time appointed for the holding of the SGM (i.e. no later than 10:00 a.m. (Hong Kong time) on Monday, 13 December 2021) or any adjournment thereof. Completion and return of the form of proxy as instructed will not prevent Shareholders from subsequently attending and voting at the SGM or any adjourned meeting if they so wish.

LETTER FROM THE BOARD

RECOMMENDATION

The Board considers that the transactions contemplated under the 2020 Feihe Master Agreement will be conducted by the Group in its ordinary and usual course of business, on normal commercial terms, are fair and reasonable and in the interests of the Company and the Shareholders as a whole, and that the Proposed New Annual Caps are fair and reasonable. The Board therefore recommends the Independent Shareholders to vote in favour of the relevant resolution set out in the notice of the SGM.

FURTHER INFORMATION

The Independent Board Committee comprising three independent non-executive Directors has been appointed to recommend the Independent Shareholders in respect of the transactions contemplated under the 2020 Feihe Master Agreement and the Proposed New Annual Caps. Gram Capital has been appointed as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in such regard.

Accordingly, your attention is drawn to (i) the letter of recommendation from the Independent Board Committee to the Independent Shareholders set out on pages 21 to 22 of this circular, which contains its recommendation to the Independent Shareholders; (ii) the letter of advice from Gram Capital set out on pages 23 to 40 of this circular, which contains its advice to the Independent Board Committee and the Independent Shareholders; (iii) the general information set out in the Appendix to this circular; and (iv) the notice of the SGM.

Yours faithfully
For and on behalf of the Board of
YuanShengTai Dairy Farm Limited
Zhao Hongliang
Executive Director and Chairman

LETTER FROM THE INDEPENDENT BOARD COMMITTEE



YuanShengTai Dairy Farm Limited **原生態牧業有限公司**

(Incorporated in Bermuda with limited liability)

(Stock Code: 1431)

25 November 2021

To the Independent Shareholders

Dear Sir or Madam,

REVISION OF ANNUAL CAPS FOR CONTINUING CONNECTED TRANSACTIONS UNDER THE 2020 FEIHE MASTER AGREEMENT

We refer to the circular of the Company dated 25 November 2021 (the “**Circular**”) to the Shareholders, of which this letter forms part. Terms defined in the Circular have the same meanings in this letter unless the context otherwise requires.

In compliance with the Listing Rules, we have been appointed by the Board to form the Independent Board Committee and advise the Independent Shareholders as to whether, in our opinion, the transactions contemplated under the 2020 Feihe Master Agreement and the Proposed New Annual Caps will be conducted by the Group in its ordinary and usual course of business, are on normal commercial terms and in the interests of the Company and the Shareholders as a whole and are fair and reasonable so far as the Independent Shareholders are concerned. In this connection, Gram Capital has been appointed as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in respect of the transactions contemplated under the 2020 Feihe Master Agreement and the Proposed New Annual Caps.

We wish to draw your attention to the letter from the Board set out on pages 6 to 20 of the Circular, and the letter from Gram Capital to the Independent Board Committee and the Independent Shareholders set out on pages 23 to 40 of the Circular which contains its opinion in respect of the transactions contemplated under the 2020 Feihe Master Agreement and the Proposed New Annual Caps.

LETTER FROM THE INDEPENDENT BOARD COMMITTEE

Having taken into account the advice of Gram Capital and its recommendation in relation thereto, we consider that the transactions contemplated under the 2020 Feihe Master Agreement are conducted by the Group in its ordinary and usual course of business, are on normal commercial terms and in the interests of the Company and the Shareholders as a whole and are fair and reasonable so far as the Independent Shareholders are concerned, and the Proposed New Annual Caps are fair and reasonable and are in the interests of the Company and the Shareholders as a whole. Accordingly, we recommend that you vote in favour of the relevant resolution set out in the notice of the SGM.

Yours faithfully,
Independent Board Committee of
YuanShengTai Dairy Farm Limited

Meng Jingzong

Zhang Yuezhou

Zhu Zhanbo

LETTER FROM GRAM CAPITAL

Set out below is the text of a letter received from Gram Capital, the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders in respect of the Transactions for the purpose of inclusion in this circular.



Room 1209, 12/F.
Nan Fung Tower
88 Connaught Road Central/
173 Des Voeux Road Central
Hong Kong

25 November 2021

*To: The independent board committee and the independent shareholders
of YuanShengTai Dairy Farm Limited*

Dear Sir/Madam,

CONTINUING CONNECTED TRANSACTIONS

We refer to our appointment as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in respect of the revision of annual caps for the year ending 31 December 2021 and 2022 under the 2020 Feihe Master Agreement and the transactions contemplated thereunder (the “**Transactions**”), details of which are set out in the letter from the Board (the “**Board Letter**”) contained in the circular dated 25 November 2021 issued by the Company to the Shareholders (the “**Circular**”), of which this letter forms part. Terms used in this letter shall have the same meanings as defined in the Circular unless the context requires otherwise.

On 23 September 2019, the Company entered into the 2020 Feihe Master Agreement with China Feihe, a member of Feihe Dairy Group, to confirm the Group’s supply of raw milk to Feihe Dairy Group for a term commencing from the Commencement Date and ending on 31 December 2022, subject to the terms and conditions contained therein.

With reference to the Board Letter, the Company currently estimates that given the expected increase in the overall sales volume of Feihe Dairy Group and the expected increase in demand from Feihe Dairy Group in respect of the purchase of raw milk from the Group, the annual transaction amounts under the 2020 Feihe Master Agreement for the year ending 31 December 2021 and 31 December 2022 are expected to exceed the Original Annual Caps. As such, the Company intends to revise the annual caps for the year ending 31 December 2021 and 31 December 2022 under the 2020 Feihe Master Agreement in respect of the sale of raw milk by the Group to Feihe Dairy Group.

With reference to the Board Letter, the Transactions constitute continuing connected transactions of the Company, and are subject to the reporting, annual review, announcement and Independent Shareholders’ approval requirement pursuant to Chapter 14A of the Listing Rules.

LETTER FROM GRAM CAPITAL

The Independent Board Committee comprising Mr. Meng Jingzong (alias Owens Meng), Mr. Zhang Yuezhou and Mr. Zhu Zhanbo (all being independent non-executive Directors) has been established to advise the Independent Shareholders on (i) whether the terms of the Transactions are on normal commercial terms and are fair and reasonable; (ii) whether the Transactions are in the interests of the Company and the Shareholders as a whole and are conducted in the ordinary and usual course of business of the Group; and (iii) how the Independent Shareholders should vote in respect of the resolution(s) to approve the Transactions at the SGM. We, Gram Capital Limited, have been appointed as the Independent Financial Adviser to advise the Independent Board Committee and the Independent Shareholders in this respect.

INDEPENDENCE

We were not aware of (i) any relationships or interests between Gram Capital and the Company; or (ii) any services provided by Gram Capital to the Company, during the past two years immediately preceding the Latest Practicable Date, or any other parties that could be reasonably regarded as hindrance to Gram Capital's independence to act as the Independent Financial Adviser to the Independent Board Committee and the Independent Shareholders.

BASIS OF OUR OPINION

In formulating our opinion to the Independent Board Committee and the Independent Shareholders, we have relied on the statements, information, opinions and representations contained or referred to in the Circular and the information and representations as provided to us by the Directors. We have assumed that all information and representations that have been provided by the Directors, for which they are solely and wholly responsible, are true and accurate at the time when they were made and continue to be so as at the Latest Practicable Date. We have also assumed that all statements of belief, opinion, expectation and intention made by the Directors in the Circular were reasonably made after due enquiry and careful consideration. We have no reason to suspect that any material facts or information have been withheld or to doubt the truth, accuracy and completeness of the information and facts contained in the Circular, or the reasonableness of the opinions expressed by the Company, its advisers and/or the Directors, which have been provided to us. Our opinion is based on the Directors' representation and confirmation that there is no undisclosed private agreements/arrangements or implied understanding with anyone concerning the 2020 Feihe Master Agreement and the Transactions. We consider that we have taken sufficient and necessary steps on which to form a reasonable basis and an informed view for our opinion in compliance with Rule 13.80 of the Listing Rules.

The Circular, for which the Directors collectively and individually accept full responsibility, includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Company. The Directors, having made all reasonable enquiries, confirm that to the best of their knowledge and belief the information contained in the Circular is accurate and complete in all material respects and not misleading or deceptive, and there are no other matters the omission of which would make any statement as contained in the Circular or the Circular misleading. We, as the Independent Financial Adviser, take no responsibility for the contents of any part of the Circular, save and except for this letter of advice.

LETTER FROM GRAM CAPITAL

We consider that we have been provided with sufficient information to reach an informed view and to provide a reasonable basis for our opinion. We have not, however, conducted any independent in-depth investigation into the business and affairs of the Company, Feihe Dairy Group and each of their respective subsidiaries or associates, nor have we considered the taxation implication on the Group or the Shareholders as a result of the Transactions. Our opinion is necessarily based on the financial, economic, market and other conditions in effect and the information made available to us as at the Latest Practicable Date. Shareholders should note that subsequent developments (including any material change in market and economic conditions) may affect and/or change our opinion and we have no obligation to update this opinion to take into account events occurring after the Latest Practicable Date or to update, revise or reaffirm our opinion. In addition, nothing contained in this letter should be construed as a recommendation to hold, sell or buy any Shares or any other securities of the Company.

Lastly, where information in this letter has been extracted from published or otherwise publicly available sources, it is the responsibility of Gram Capital to ensure that such information has been correctly extracted from the relevant sources while we are not obligated to conduct any independent in-depth investigation into the accuracy and completeness of those information.

PRINCIPAL FACTORS AND REASONS CONSIDERED

In arriving at our opinion in respect of the Transactions, we have taken into consideration the following principal factors and reasons:

Information on the Company

With reference to the Board Letter, the Company is a dairy farming company in the PRC dedicated to the production of super premium raw milk.

As at 30 June 2021, the Group had six farms in Heilongjiang Province, the PRC and one farm in Jilin Province, the PRC, respectively. Each farm has an actual designed capacity ranging from 6,000 to 18,000 dairy cows, and the total site area of the seven farms amounted to approximately 5,909,000 m².

Information on Feihe Dairy Group

With reference to the Board Letter, Feihe Dairy Group is based in Heilongjiang province and is principally engaged in the production and sale of infant formula products in the PRC. The ordinary shares of China Feihe are listed on the main board of the Stock Exchange. As of the Latest Practicable Date, China Feihe holds approximately 71.26% of the total issued share capital of the Company. Therefore, China Feihe is the controlling shareholder of the Company and hence a connected person of the Company.

As advised by the Directors, Feihe Dairy Group was one of the Group's top five customers since the shares of which were listed on the Main Board of the Stock Exchange in November 2013.

LETTER FROM GRAM CAPITAL

Reasons for the Transactions

As disclosed in the prospectus of the Company dated 14 November 2013, when the Group was in its initial stage of commercial production in 2010, Feihe Dairy Group accounted for all of the Group's revenue. Throughout years of the Group's development, Feihe Dairy Group remained as one of the top five customers of the Group for the recent years. As confirmed by the Directors, the Board believes the sales of raw milk to the Feihe Dairy Group is important to the business of the Group. It is expected that for the long term, the Group's continuing supply of raw milk products to the Feihe Dairy Group will further enhance the stability of the Group's customer base and ensure future demand for the Group's raw milk.

As confirmed by the Directors, as the supply of raw milks by the Group to the Feihe Dairy Group are conducted in the ordinary and usual course of business of the Group and on a frequent and regular basis, it would be costly and impractical to make regular disclosure of each of the relevant transactions and obtain the prior approval from the Independent Shareholders as required by the Listing Rules, if necessary. Accordingly, the Directors are of the view that the supply of raw milks by the Group to the Feihe Dairy Group, being revenue in nature, will be beneficial to the Company and the Shareholders as a whole.

With reference to the Board Letter, the Company currently estimates that given the expected increase in the overall sales volume of Feihe Dairy Group and the expected increase in demand from Feihe Dairy Group in respect of the purchase of raw milk from the Group, the annual transaction amounts under the 2020 Feihe Master Agreement for the year ending 31 December 2021 and 31 December 2022 are expected to exceed the Original Annual Caps. As such, the Company intends to revise the annual caps for the year ending 31 December 2021 and 31 December 2022 under the 2020 Feihe Master Agreement in respect of the sale of raw milk by the Group to Feihe Dairy Group.

In light of (i) the revenue contribution from Feihe Dairy Group, being one of the top five customers of the Group for the recent years; (ii) the long-term business relationship between the Group and the Feihe Dairy Group; (iii) it would be costly and impractical to make regular disclosure of each of the relevant transactions and obtain the prior approval from the Independent Shareholders as required by the Listing Rules, if necessary; and (iv) the annual transaction amounts under the 2020 Feihe Master Agreement for the year ending 31 December 2021 and 31 December 2022 are expected to exceed the Original Annual Caps, we consider that the supply of raw milks by the Group to the Feihe Dairy Group are conducted in the ordinary and usual course of business of the Group and the Transactions are in the interests of the Company and the Shareholders as a whole.

LETTER FROM GRAM CAPITAL

1. Principal terms of the Transactions

Set out below are the principal terms of the Transactions, details of which are set out under the section headed “PRINCIPAL TERMS OF THE 2020 FEIHE MASTER AGREEMENT” in the Board Letter.

Date:	23 September 2019
Parties:	(a) the Company (for itself and on behalf of its subsidiaries); and (b) China Feihe (for itself and on behalf of its subsidiaries).
Contract period:	The initial term of the 2020 Feihe Master Agreement shall commence from the Commencement Date and shall end on 31 December 2022. The 2020 Feihe Master Agreement may be extended for a period of three years after the expiry of the initial term, subject to approval of such extension and the transactions contemplated thereunder (including the related annual caps) by the Independent Shareholders (if required) in accordance with the Listing Rules.
Subject matter:	Supply of raw milk by the Group to Feihe Dairy Group.
Pricing term:	For each calendar year during the term of the 2020 Feihe Master Agreement, the Group and Feihe Dairy Group will enter into an annual sale contract specifying, among others, the pricing mechanism, the quantity and quality of raw milk expected to be purchased by Feihe Dairy Group during the calendar year and payment terms. The unit selling price of raw milk generally comprises two elements, being (i) the unit base price; and (ii) certain price adjustment factors including, among others, the microbe count, the level of protein content and fat content and the freezing point of raw milk. The unit selling price of raw milk will be negotiated by the parties on arm’s length basis and in good faith with reference to the Indicative Price, the aforesaid adjustment factors and the prevailing market prices offered by the Group to its Independent Third Parties customers for products of similar quality. The terms and purchase prices offered by the Group to Feihe Dairy Group shall be no more favourable than those available to other Independent Third Parties customers.
Priority:	In the event that the Group receives purchase orders from Feihe Dairy Group and other purchasers concurrently, the Group shall give priority to Feihe Dairy Group for purchase of raw milk on terms and conditions no less favourable to the Group than that offered by the other purchasers.
Payment term:	Generally, to be settled on accrual basis, with a credit term of no more than one month, during which no interest will accrue.

LETTER FROM GRAM CAPITAL

Pricing method and procedures

Under the 2020 Feihe Master Agreement, the Group will, by the end of each calendar year during the term, enter into the Sales Contract with the Feihe Dairy Group to agree on, among others, the pricing mechanism of raw milk for the next calendar year.

The Group generally negotiates the unit selling pricing for the raw milk with its customers (including both Feihe Dairy Group and its Independent Third Party customers) based on the latest Indicative Price determined quarterly by the Heilongjiang Fresh Milk Price Coordination Committee* (黑龍江省生鮮乳價格協調委員會) and taking into account certain adjustment factors. The Group's pricing mechanism with its customers (including Feihe Dairy Group and other Independent Third Party customers of the Group) are generally the same, and therefore the selling price of the raw milk contemplated under the 2020 Feihe Master Agreement would be no less favourable than that of the other Independent Third Party customers of the Group. We understood that the Group will check the latest Indicative Price on a quarterly basis.

In order to ensure that the terms of sales of raw milk to Feihe Dairy Group (including the unit selling price) would be on normal commercial terms and on terms no less favourable to the Group than those offered to Independent Third Party customers, the Group adopted certain pricing procedures (the "**Pricing Procedures**"). Details of the pricing procedures are set out under the sub-section headed "Pricing method and procedures" in the Board Letter.

Apart from the price adjustment controls as stated above, designated members of the Group's senior management namely deputy general manager in charge of sales department and general manager will (i) review the raw milk price agreed between the Group and Feihe Dairy Group on a monthly basis, and compare it with the raw milk prices (of similar quality and during the same period of time) being agreed between the Group and other Independent Third Party customers; and (ii) review other trading terms of purchase orders received from Feihe Dairy Group and other Independent Third Party customers, to ensure that (a) the unit selling prices of raw milk for all of the Group's customers remain comparable; (b) other trading terms offered by Feihe Dairy Group (e.g. base price, adjustment factor, payment term and driving distance) are no less favourable to the Group than that offered by the other Independent Third Party customers; and (c) the contemplated transactions between the Feihe Dairy Group and the Group are conducted on normal commercial terms.

Having considered the aforesaid measures, we consider that the effective implementation of the aforesaid measures would help to ensure the fair pricing under the 2020 Feihe Master Agreement.

To assess the effectiveness of the implementation of the aforesaid measures, we requested the Company to provide us invoices issued by the Group to (i) Feihe Dairy Group; and (ii) Independent Third Party customers during each quarter of 2020 and during first three quarters of 2021. As advised by the Directors, the Company provided us the invoices (the "**Price Documents**") on a quarterly and random basis. We noted from the Price Documents that the unit prices of the raw milk supplied by the Group to Feihe Dairy Group were not lower than those supplied to the Independent Third Party customers in similar period.

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We further requested the Company to provide documents in respect of the Group's review on unit base price for the relevant months of the Price Documents. We obtained documents showing the Group's review on the unit base price agreed between the Group and (i) Feihe Dairy Group; and (ii) other Independent Third Party customers during each quarter of 2020 and during first three quarters of 2021. According to the aforesaid documents, the aforesaid documents were prepared by sales department's staff, reviewed by sale department's manager-level staff and approved by deputy general manager in charge of sales department.

With reference to Rule 14A.56 of the Listing Rules, among other things, the auditors of the Company must provide a letter to the Board confirming whether anything has come to their attention that causes them to believe that the continuing connected transactions were not, in all material respects, in accordance with the pricing policies of the listed issuer's group if the transactions involve the provision of goods or services by the listed issuer's group. We obtained the letter from the Company's auditors, showing their confirmation that, among other things, nothing has come to their attention that causes them to believe that the continuing connected transactions regarding the supply of raw milk by the Group to the Feihe Dairy Group for the year ended 31 December 2020 was not, in all material respects, in accordance with the pricing policies of Group.

Having considered (i) our findings on (a) Price Documents; and (b) documents showing the Group's review on the unit base price as mentioned above; and (ii) the confirmation letter from Company's auditors, we do not doubt the effectiveness of the implementation of the aforesaid measures.

We also noted that the Company will closely monitor the transaction amounts (including the percentage amount) in respect of the transactions contemplated under the 2020 Feihe Master Agreement through certain measures, details of which are set out under the section headed "Level of Contribution" of the Board Letter.

Payment term

Pursuant to the 2020 Feihe Master Agreement, payment term will generally be settled on accrual basis, with a credit term of no more than one month, during which no interest will accrue.

For our due diligence purpose, we further searched for companies listed in Hong Kong which are engaged in similar line of business as the Group, being production and sale of raw milk in the PRC and derived a majority of their turnover from such business, based on their respective latest published financial information. Set out below are our findings on credit period of comparable listed companies, which are exhaustive as far as we were aware of:

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Company	Principal business	Credit Period
China Modern Dairy Holdings Limited (1117)	The company is an investment holding company principally engaged in the production and sales of milk. The company operates through two business segments. The Dairy Farming segment is engaged in the breeding of dairy cows to produce raw milk. The Liquid Milk Products Production segment is engaged in the production and sales of processed liquid milk. The company is also involved in the production of fodder and the sales of feeds through its subsidiaries.	The group allows a credit period of 30 days to its customers.
China Shengmu Organic Milk Limited (1432)	The company is a China-based investment holding company principally engaged in the production and distribution of raw milk and dairy products. The company operates through two business segments. The Farming segment is engaged in the breeding of dairy cows to produce and distribute raw milk. The Liquid Milk Products segment is engaged in the production and distribution of organic ultra-heat treated liquid milk and organic yogurt.	In 2020, the credit period is generally one month, extending up to three months for major customers. However, the group normally allows a credit limit or offer to its customers credit terms which are adjustable in certain circumstances and closely monitors overdue balances.
China ZhongDi Dairy Holdings Company Limited (1492) <i>Note:</i> the company was privatised and delisted in June 2021	The group is principally engaged in business operations including raising and breeding dairy cows, producing and selling premium raw milk, importing and selling dairy cows of quality breeds and breeding stock, and import trading business in cows, alfalfa hay and other animal husbandry-related products.	The group normally allows a credit period of 30 days to its customers for sales of raw milk.

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Company	Principal business	Credit Period
China Youran Dairy Group Ltd. (9858)	<p>The company is a China-based investment holding company principally engaged in the production and sales of raw milk, as well as the trading, production and sales of dairy farming products. The company mainly conducts its businesses through two segments. The Raw Milk segment provides raw milk to large-scale dairy manufacturers for further processing into premium dairy products. The Comprehensive Ruminant Farming Solutions segment includes feed business, breeding business and ruminant farming products marketplace business. The company provides nutritious concentrated feed, forage grass and ancillary ruminant farming support services for dairy farms. The company also provides dairy farms with access to high-quality frozen bovine semen for dairy cattle and beef cattle, as well as ruminant farming products.</p>	<p>As at 31 December 2020 and 30 June 2021, trade receivables from related parties are aged within 3 months based on the month of delivery.</p>

Source: financial reports of the comparable listed companies and the Stock Exchange's website.

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We noted from the above table that the credit periods of the comparable listed companies were generally approximate one month.

Based on the above, we consider the payment term under the 2020 Feihe Master Agreement to be fair and reasonable.

Priority

Pursuant to the 2020 Feihe Master Agreement, in the event that the Group receives purchase orders from Feihe Dairy Group and other purchasers concurrently, the Group shall give priority to Feihe Dairy Group for purchase of raw milk on terms and conditions no less favourable to the Group than that offered by the other purchasers.

As confirmed by the Directors, designated members of the Group's senior management namely deputy general manager in charge of sales department and general manager will review other trading terms of purchase orders received from Feihe Dairy Group and other Independent Third Party customers, to ensure that other trading terms offered by Feihe Dairy Group are no less favourable to the Group than that offered by the other Independent Third Party customers before giving priority rights to Feihe Dairy Group. As there will be other trading terms comparison procedures before giving priority rights to Feihe Dairy Group, we consider that such procedures are sufficient to ensure the priority rights will be given to Feihe Dairy Group under the circumstances that terms and conditions are no less favourable to the Group than that offered by the other Independent Third Party customer.

Upon our request, the Directors advised us that Feihe Dairy Group has been a customer of the Group since 2008. To the best of the Directors knowledge, the Directors were not aware of any breach of individual contracts (i.e. delayed payment) under the Feihe Master Agreements regarding supply of raw milk by the Group or any order as placed by Feihe Dairy Group for recent three years.

We noted that China Shengmu Organic Milk Limited ("**China Shengmu**", stock code: 1432, together with its subsidiaries, the "**Shengmu Group**") despatched a circular to its shareholders on 6 March 2020, among other things, China Shengmu entered into priority supply agreements with Inner Mongolia Shengmu High-tech Dairy Co., Ltd. and Huhehaote Mengniu Shengmu High-tech Dairy Co., Ltd (呼和浩特市蒙牛聖牧高科乳品有限公司) respectively on 23 December 2018. Pursuant to the priority supply agreements, China Shengmu agreed that it will, and it will also procure its subsidiaries to, provide raw fresh milk to the aforesaid companies with priority under the same conditions.

In addition, we also noted that China Shengmu entered into a milk supply framework agreement (the "**Shengmu Agreement**") with its connected person (i.e. a non-wholly owned subsidiary) in relation to the purchase of organic raw milk by the Shengmu Group on 22 November 2016. Pursuant to the milk supply framework agreement, among other things, Shenmu Group's connected person shall sell all organic raw milk it produces to the Shengmu Group on a priority basis to satisfy the demand of the Shengmu Group.

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To further assess whether the Priority Rights is a normal commercial term, after taking into the consideration that the supply of raw milk by the Group to Feihe Dairy Group is by nature supplying/purchasing goods or services, we remove the industry restriction.

Based on our research, we noted more than five transactions regarding Hong Kong listed companies supplying/purchasing goods or services to/from connected persons with a priority supply/purchasing right. Despite that our findings may not be exhaustive, having considered (i) our research purpose is to identify if there are Hong Kong listed companies supplying/purchasing goods or services to/from connected persons with a priority supply/purchasing right, therefore it is not necessary to identify all similar transactions with priority; (ii) the number of sample transactions are sufficient to demonstrate the situation, we are of the view that the sample transactions as listed out below are fair and representative. Set out below are all our findings with announcement dates falling within one year prior to the date of 2020 Feihe Master Agreement for the Independent Shareholders' information purposes only.

Announcement date	Company name	Nature of transactions	Priority term
23 August 2018	China Datang Corporation Renewable Power Co., Limited (1798)	The group and connected person group mutually provide the counterparty with the goods and services.	If the terms and conditions of similar products and services offered by one of the parties are no less favourable than those offered by an independent third party, the counterparty shall give such party the priority in sourcing of the requisite products and services.
13 December 2018	China Railway Construction Corporation Limited (1186)	Connected person and its related parties/ connected persons/ associates provide services to the group.	Under the same or less favourable conditions of purchase from third parties, connected person shall give priority to providing services to the company.
30 April 2019	Kunming Dianchi Water Treatment Co., Ltd. (3768)	The group provides operation and management services to connected person group.	Connected person group shall give priority to the operation and management services provided by the group when the service terms offered and fees quoted by third parties are the same.

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Announcement date	Company name	Nature of transactions	Priority term
24 May 2019	Culturecom Holdings Limited (343)	The company's subsidiary provides services to connected person.	The company's subsidiary will be given priority by connected person in the procurement of the services to connected person provided that the material terms offered by the company's subsidiary are comparable to those offered by independent third parties.
14 June 2019	CGN mining Company Limited (1164)	The group supplies goods to connected person group by the group.	The group shall have the right of first offer to supply natural uranium demanded by connected person group during the effective period.

As the purpose of aforesaid searching is to find out whether the priority supply arrangements exist among the Hong Kong listed companies, the industries in which the transactions involved are irrelevant.

Having considered (i) there were Hong Kong listed companies supplying/purchasing goods or services to/from connected persons with a priority supply/purchasing right; (ii) supplying/purchasing goods or services to/from connected persons with a priority supply/purchasing right to be acceptable; (iii) the Group will give priority to Feihe Dairy Group for purchase of raw milk on terms and conditions being no less favourable to the Group than those offered by other Independent Third Party customers; (iv) the Group adopted internal control procedures to ensure other trading terms offered by Feihe Dairy Group are no less favourable to the Group than those offered by other Independent Third Party customers; (v) as Feihe Dairy Group is the Group's largest customer, the priority arrangement could reinforce the business relationship with China Feihe Group (which has been one of the Group's most important business partner); (vi) the Company could sell its raw milk to other customers other than China Feihe who offered better terms; and (vii) the grant of priority arrangement encourages competitions among the Group's customers in offering the best purchase price to the Group in order to procure raw milk from the Group, particularly when there is a strong demand or insufficient supply of raw milk in the market, we are of the view that the priority terms to be normal commercial terms.

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2. The revised annual caps under the 2020 Feihe Master Agreement

Set out below are (i) the historical transactions amounts of the transactions and existing annual caps regarding supply of raw milk to Feihe Dairy Group for the year ended 31 December 2020 and 31 June 2021 respectively; (ii) the existing annual caps for the three years ending 31 December 2022; and (iii) the revised annual caps for the two years ending 31 December 2022 (the “**Revised Annual Caps**”):

	For the year ended 31 December 2020 (“FY2020”) RMB’million	For the year ending 31 December 2021 (“FY2021”) RMB’million	For the year ending 31 December 2022 (“FY2022”) RMB’million
Historical transactions amount	1,299	1,162 ^(Note 1)	N/A
Existing annual caps	1,300	1,400	1,500
Utilisation rate	99.9%	N/A	N/A
		For the year ending 31 December 2021 RMB’million	For the year ending 31 December 2022 RMB’million
Revised Annual Caps		1,600	2,000

Note:

1. The figure is for the nine months ended 30 September 2021 and is unaudited.
2. The Company undertakes not to generate more than 90% of its annual revenue in 2021 and 2022 from China Feihe.

With reference to the Board Letter, the Revised Annual Caps were determined with various factors, details of which are set out under the sub-section headed “The Proposed New Annual Caps” in the Board Letter.

We noted that the existing annual cap for the year ended 31 December 2020 was almost fully utilized. The annualised amounts based on the historical transaction amounts for the nine months ended 30 September 2021 would exceed the existing annual cap for FY2021. The Revised Annual Cap for FY2021 represents a substantial increase of approximately 14% to the existing annual cap for FY2021; and the Revised Annual Cap for FY2022 represents a substantial increase of 25% to the Revised Annual Cap for FY2021.

To assess the fairness and reasonableness of the Revised Annual Caps for the two years ending 31 December 2022, we obtained and reviewed the calculation of the Revised Annual Caps (the “**Calculation**”). We noted that the Revised Annual Caps were arrived by (i) the estimated quantity of raw milk (in tonne) to be supplied by the Group to the Feihe Dairy Group for the two years ending 31 December 2022; (ii) the estimated selling price of raw milk for the two years ending 31 December 2022; and (iii) buffers of around 5% on the estimated demand of raw milk (in RMB) for the two years ending 31 December 2022, which were arrived by (i) and (ii).

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Estimated quantity of raw milk (in tonne)

Upon our request, the Directors advised us the estimated demand of raw milk (in tonne) for FY2021 (the “**2021 Feihe Volume**”)/FY2022 (the “**2022 Feihe Volume**”) was determined based on (i) the estimated quantity of raw milk to be supplied by the Group to all customers for the year ending 31 December 2021 (the “**2021 Total Volume**”)/for the year ending 31 December 2022 (the “**2022 Total Volume**”); (ii) a maximum of 90% of the aforesaid volume (in tonne) to be supplied by the Group to the Feihe Dairy Group.

As (i) the 2021 Total Volume is in line with the actual quantity of raw milk supplied by the Group to all customers for the year ended 31 December 2020; and (ii) there is no material difference (with difference of less than 5%) between the 2021 Total Volume as compared to the annualized quantity of raw milk supplied by the Group to all customers for the first nine months ended 30 September 2021, we consider the 2021 Total Volume to be justifiable.

With reference to the Board Letter, the Company undertakes not to generate more than 90% of its annual revenue in 2021 and 2022 from China Feihe (the “**Percentage Limits**”). Having considered the proportion of revenue (generated from raw milk supply segment) attributable by single largest customers to all relevant customers as recorded by the Comparable Companies as follows, we consider the Percentage Limits to be fair and reasonable.

	Proportion of revenue (generated from raw milk supply segment) attributable by single largest customers to all relevant customers		
Company name	For the year ended 31 December 2020	For the year ended 31 December 2019	For the year ended 31 December 2018
China Modern Dairy Holdings Limited (1117)	82.0%	85.3%	90.0%
China Shengmu Organic Milk Limited (1432)	94.1%	92.6%	42.7%
China ZhongDi Dairy Holdings Company Limited (1492)	77.6%	90.9%	46.9%
<i>Note:</i> the company was privatised and delisted in June 2021			
China Youran Dairy Group Ltd. (9858)	95.8% <i>(Note)</i>	92.9% <i>(Note)</i>	91.7% <i>(Note)</i>

Note: % to the revenue generated from raw milk supply segment in total

Source: financial reports of the comparable listed companies.

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Having considered that (i) the Company undertakes not to generate more than 90% of its annual revenue in 2021 and 2022 from China Feihe and the Percentage Limit is justifiable; and (ii) purchase prices offered by the Group to Feihe Dairy Group shall be no more favourable than those available to other Independent Third Parties customers, we are of the view that the Company adopted 90% of 2021 Total Volume as the estimated quantity of raw milk (in tonne) to be supplied by the Group to the Feihe Dairy Group to be reasonable.

Based on the above factors, we consider the 2021 Feihe Volume to be reasonable.

We further noted that the estimated quantity of the 2022 Total Volume represented an increase of approximately 22% (the “**2022 Increase**”) as compared to the 2021 Total Volume.

To assess the fairness and the reasonableness of the 2022 Increase, we conducted the following analyses:

- We noted that the Group recorded an increase of approximately 18% in the quantity of raw milk supplied by the Group to all customers for the year ended 31 December 2019 as compared to that for the year ended 31 December 2018.

According to the Company’s annual report for the year ended 31 December 2019, as at 31 December 2019, the Group had 33,716 matured milkable cows, which represented a slight increase of 1,291 matured milkable cows or approximately 4.0% to the number of matured milkable cows as at 31 December 2018.

As advised by the Directors, by strategically increasing the number of matured milkable cows, improving the operational efficiency of the farms and feeding formula for the cow, and optimizing the age structure of herds and herd structure, the Group can further improve the overall milk yield and the average milk yield per cow so as to cater for the market demand of the Group’s raw milk.

- According to the Company’s interim report, as at 30 June 2021, the Group had seven farms in total, with total actual designed capacity of 90,000 dairy cows. As at 30 June 2021, the Group had 72,321 number of dairy cows, including 35,057 matured milkable cows and 37,264 heifers and calves. If the Group is to increase 22% of number of matured milkable cows (i.e. 7,713 heads), the total number of dairy cows would increase to 80,034 heads, which is still within the actual designed capacity of 90,000 dairy cows.
- Upon our request, we understood that in general, the heifers are inseminated with semen when they reach approximately 13 months old. After approximately nine months following a successful insemination, a calf is born and the dairy cow begins to produce raw milk and the lactation period begins. Therefore, the calves will grow to milkable cows, which will further increase in the Group’s raw milk supply capacity.

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- In order to seize the market opportunities, the Company is planning the construction of two new farms with a total designed capacity of 22,000 dairy cows to further expand the Company's production and overall scale of operation. In addition, the Company has entered into two agreements to acquire a dairy farm with around 1,500 dairy cows and a dairy farm (without any dairy cows) with a designed capacity of 10,000 dairy cows, respectively.

Based on the above, we consider that the Group could be able reach the raw milk supply capacity. In addition, as the Company undertakes not to generate more than 90% of its annual revenue in 2021 and 2022 from China Feihe and the Percentage Limit is justifiable, we are of the view that the 2022 Feihe Volume to be reasonable.

Estimated selling price

We noted from the Calculation that the Directors applied estimated selling price of RMB4.70 per kilogram for FY2021, which is close to the average selling price of approximately RMB4.66 per kilogram for the six months ended 30 June 2021 with difference of less than 1%.

In addition, the estimated selling price for FY2022 represented a slight increase of approximately 3% as compared to the estimated selling price for FY2021. Having considered that the average selling price for the six months ended 30 June 2021 represented an increase of approximately 7% as compared to that for FY2020; the average selling price for FY2020 represented an increase of approximately 5% as compared to that for FY2019; and the average selling price for FY2019 represented an increase of approximately 7% as compared to that for FY2018, we are of the view that the slight increase of approximately 3% to be justifiable. Accordingly, we consider the estimated selling price for FY2022 to be reasonable.

Having considered the above factors, we are of the view that the estimated amounts of raw milk to be supplied by the Group to the Feihe Dairy Group for FY2021 and FY2022 to be fair and reasonable.

Buffers

We noted that buffers of approximately 5% were applied as assumptions for the determination of the Revised Annual Caps. Having considered that the additional buffer (which forms approximately 5% of the Revised Annual Caps for each of the two years ending 31 December 2022) were applied for unforeseeable circumstances, for instance, (a) the unpredictable increase in selling price of raw milk; and (b) the unexpected substantial increase in demand of raw milk by the Feihe Dairy Group, we consider that the buffers to be acceptable.

In light of that the above factors, we are of the view that the Revised Annual Caps for the two years ending 31 December 2022 are fair and reasonable.

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Shareholders should note that as the Revised Annual Caps (including the Percentage Limits) for the two years ending 31 December 2022 are relating to future events and were estimated based on assumptions which may or may not remain valid for the entire period up to 31 December 2022, and they do not represent forecasts of cost to be incurred from the transactions contemplated under the 2020 Feihe Master Agreement. Consequently, we express no opinion as to how closely the actual revenue/income/cost to be generated/incurred from the transactions contemplated under the 2020 Feihe Master Agreement will correspond with the Revised Annual Caps (including the Percentage Limits).

3. Listing Rules implication

The Directors confirmed that the Company shall comply with the requirements of Rules 14A.53 to 14A.59 of the Listing Rules pursuant to which (i) the values of the transactions contemplated under the 2020 Feihe Master Agreement must be restricted by their respective annual caps for the period concerned under the 2020 Feihe Master Agreement; (ii) the terms of the transactions contemplated under the 2020 Feihe Master Agreement (including their respective annual caps) must be reviewed by the independent non-executive Directors annually; (iii) details of independent non-executive Directors' annual review on the terms of the transactions contemplated under the 2020 Feihe Master Agreement must be included in the Company's subsequent published annual reports.

Furthermore, it is also required by the Listing Rules that the auditors of the Company must provide a letter to the Board confirming, among other things, whether anything has come to their attention that causes them to believe that the transactions contemplated under the 2020 Feihe Master Agreement (i) have not been approved by the Board; (ii) were not, in all material respects, in accordance with the pricing policies of the Group if the transactions involve the provision of goods or services by the listed issuer's group; (iii) were not entered into, in all material respects, in accordance with the relevant agreement governing the transactions; and (iv) have exceeded their respective annual caps.

In the event that the total amounts of the transactions contemplated under the 2020 Feihe Master Agreement or its percentage to the Group's total revenue are anticipated to exceed their respective annual caps or the Percentage Limits, or that there is any proposed material amendment to the terms of the 2020 Feihe Master Agreement, as confirmed by the Directors, the Company shall comply with the applicable provisions of the Listing Rules governing continuing connected transaction.

Given the above stipulated requirements for continuing connected transactions pursuant to the Listing Rules, we are of the view that there are adequate measures in place to monitor the transactions contemplated under the 2020 Feihe Master Agreement and thus the interest of the Independent Shareholders would be safeguarded.

LETTER FROM GRAM CAPITAL

RECOMMENDATION

Having taken into consideration the factors and reasons as stated above, we are of the opinion that (i) the terms of the Transactions are on normal commercial terms and are fair and reasonable; and (ii) the transactions contemplated under the 2020 Feihe Master Agreement are conducted in the ordinary and usual course of business of the Group and the Transactions are in the interests of the Company and the Shareholders as a whole. Accordingly, we recommend the Independent Board Committee to advise the Independent Shareholders to vote in favour of the resolution(s) to be proposed at the SGM to approve the Transactions and we recommend the Independent Shareholders to vote in favour of the resolution(s) in this regard.

Yours faithfully,
For and on behalf of
Gram Capital Limited
Graham Lam
Managing Director

Mr. Graham Lam is a licensed person registered with the Securities and Futures Commission and a responsible officer of Gram Capital Limited to carry out Type 6 (advising on corporate finance) regulated activity under the SFO. He has over 25 years of experience in investment banking industry.

* *For identification purpose only*

1. RESPONSIBILITY STATEMENT

This circular, for which the Directors collectively and individually accept full responsibility, includes particulars given in compliance with the Listing Rules for the purpose of giving information with regard to the Company. The Directors having made all reasonable enquiries, confirm that to the best of their knowledge and belief the information contained in this circular is accurate and complete in all material respects and not misleading or deceptive, and there are no other matters the omission of which would make any statement herein or this circular misleading.

2. INTEREST IN SECURITIES

Save as disclosed below, as at the Latest Practicable Date, none of the Directors and chief executives of the Company had any interest or short position in the Shares, underlying Shares and debt securities of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) nor had any interest in the right to subscribe for Shares in the Company which had to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they were taken or deemed to have under such provisions of the SFO) or which were required, pursuant to section 352 of the SFO, to be entered in the register of the Company referred to therein or which were required, pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers contained in the Listing Rules, to be notified to the Company and the Stock Exchange.

(i) Long Positions in the Shares

Name of Director	Capacity/Nature of interests	Number of Shares held	Approximate percentage of issued Shares
Mr. Leng Youbin ("Mr. Leng") <i>(Note)</i>	Interest in a controlled corporation and founder of a discretionary trust/ Corporate and other interest	3,342,320,920	71.26%

Note: 3,342,320,920 Shares were beneficially owned by China Feihe which is owned as to 50.22% by Mr. Leng, a non-executive Director. Therefore, Mr. Leng is deemed or taken to be interested in 3,342,320,920 Shares beneficially owned by China Feihe by virtue of the SFO.

(ii) Long Positions in the shares of China Feihe – an associated corporation of the Company

Name of Directors	Capacity/Nature of interests	Number of Shares held	Approximate percentage of issued Shares
Mr. Leng ^(Note 1)	Interest in a controlled corporation and founder of a discretionary trust/ corporate and other interest	4,457,428,339	50.22%
Mr. Liu Hua (“Mr. Liu”) ^(Note 2)	Interest in a controlled corporation and founder of a discretionary trust/ corporate and other interest	933,198,378	10.47%
Mr. Cai Fangliang (“Mr. Cai”) ^(Note 3)	Interest in a controlled corporation	101,647,734	1.14%
Mr. Liu Gang ^(Note 4)	Beneficial owner, interest in a controlled corporation and spouse’s interest	1,694,000	0.02%

Notes:

- 587,516,458 shares were held by Mr. Leng through his controlled corporation – Dasheng Limited (“Dasheng”). 33.33% of the equity interests in Dasheng were held directly by Mr. Leng. 3,889,911,881 shares were held by Harneys Trustees Limited (“Harneys”) as the trustee of Leng Family Trust, which in its capacity as trustee holds the entire issued share capital of LYB International Holding Limited (“LYB”), which in turn holds the entire issued share capital of Garland Glory Holdings Limited (“Garland Glory”). Leng Family Trust was established by Mr. Leng as the settlor and the only discretionary object.
- 587,516,458 shares were held by Mr. Liu through his controlled corporation – Dasheng. 33.33% of the equity interests in Dasheng were held directly by Mr. Liu. 345,681,920 shares were held by Harneys as the trustee of LH Family Trust, which in its capacity as trustee holds the entire issued share capital of LH Capital Holding Limited, which in turn holds the entire issued share capital of LH Financial Holding Limited, LH Family Trust was established by Mr. Liu as the settlor and the only discretionary object.
- 101,647,734 shares were held by Mr. Cai through his controlled corporation – Adroit Shipping Limited. Adroit Shipping Limited is directly wholly owned by Mr. Cai.
- 464,000 shares were directly held by Mr. Liu Gang. 677,000 shares were held by Mr. Liu Gang through his controlled corporation – Thyme Fair Limited. Thyme Fair Limited is directly wholly owned by Mr. Liu Gang. 553,000 shares are held by Ms. Guan Shijing, the spouse of Mr. Liu Gang, Mr. Liu Gang is deemed to be interested in these shares.

Save as disclosed above and so far as is known to the Directors, as at the Latest Practicable Date, none of the Directors and the chief executive of the Company had or was deemed to have any other interests or short positions in the Shares, underlying Shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO), which were required: (a) to be notified to the Company and the Stock Exchange pursuant to Divisions 7 and 8 of Part XV of the SFO (including interests and short positions which they were taken or deemed to have under such provisions of the SFO); or (b) pursuant to section 352 of the SFO, to be entered in the register as referred to therein; or (c) to be notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers contained in the Listing Rules.

3. DIRECTORS' SERVICE CONTRACTS

As at the Latest Practicable Date, none of the Directors had or was proposed to have a service contract with the Company or any of our subsidiaries other than contracts expiring or determinable by the employer within one year without the payment of compensation (other than statutory compensation).

4. COMPETING INTERESTS

As at the Latest Practicable Date, none of the Directors and their respective associates was interested in any business apart from the business of the Group, which competes or is likely to compete, either directly or indirectly, with the business of the Group.

5. OTHER ARRANGEMENTS INVOLVING DIRECTORS

As at the Latest Practicable Date:

- (a) none of the Directors was materially interested in any contract or arrangement entered into by any member of the Group subsisting at the Latest Practicable Date and which was significant in relation to the business of the Group; and
- (b) none of the Directors had any direct or indirect interest in any assets which had been since 31 December 2020 (the date to which the latest published audited consolidated financial statements of the Company were made up), (i) acquired or disposed of by; (ii) leased to; or (iii) are proposed to be acquired or disposed of by; or (iv) are proposed to be leased to, any member of the Group.

6. MATERIAL ADVERSE CHANGES

The Directors are not aware of any material change in the financial or trading position of the Group since 31 December 2020, the date to which the latest published audited accounts of the Group were made up.

7. EXPERT

The following is the qualification of the expert who has given its opinions or advice, which are contained or referred to in this circular:

Name	Qualification
Gram Capital Limited	a licensed corporation to carry out Type 6 (advising on corporate finance) regulated activity under the SFO

As at the Latest Practicable Date, Gram Capital:

- (a) has given and has not withdrawn its written consent to the issue of this circular with the inclusion of its letter and references to its name, in the form and context in which it appears;
- (b) did not have any shareholding in any member of the Group or the right (whether legally enforceable or not) to subscribe for or to nominate persons to subscribe for securities in any member of the Group; and
- (c) did not have any direct or indirect interest in any assets which had been since 31 December 2020 (the date to which the latest published audited consolidated financial statements of the Company were made up), acquired, disposed of by, or leased to any member of the Group or were proposed to be acquired or disposed of by, or leased to, any member of the Group.

The letter from the Independent Financial Adviser dated 25 November 2021 is set out on pages 23 to 40 in this circular and was given for incorporation in this circular.

8. GENERAL

In the event of inconsistency, the English text of this circular shall prevail over the Chinese text.

9. DOCUMENTS ON DISPLAY

The 2020 Feihe Master Agreement will be available on (i) the website of the Company (www.ystdfarm.com) and (ii) the website of the Stock Exchange (www.hkex.com) during the period of 14 days from the date of this circular.

NOTICE OF THE SPECIAL GENERAL MEETING



YuanShengTai Dairy Farm Limited 原生态牧业有限公司

(Incorporated in Bermuda with limited liability)

(Stock Code: 1431)

NOTICE OF THE SPECIAL GENERAL MEETING

NOTICE IS HEREBY GIVEN that the special general meeting of YuanShengTai Dairy Farm Limited (“**Company**”) will be held at EAST Beijing, Workshop 2, No. 22, Jiuxianqiao Road, Chaoyang District, Beijing, the PRC on Wednesday, 15 December 2021 at 10:00 a.m. to consider and, if thought fit, pass, with or without modifications, the following resolution as ordinary resolution of the Company:

ORDINARY RESOLUTION

1. “**THAT:**
 - (a) the transactions contemplated under the 2020 Feihe Master Agreement (a copy of which has been produced to the meeting marked “A” and signed by the Chairman of the meeting for the purpose of identification) and the Proposed New Annual Caps be and are hereby approved, ratified and confirmed; and

NOTICE OF THE SPECIAL GENERAL MEETING

- (b) the directors of the Company or any other person authorised by the directors of the Company be and are hereby authorised to sign, execute, perfect and deliver all such documents and do all such deeds, acts, matters and things as they may in their absolute discretion consider necessary or desirable for the purpose of or in connection with the implementation of the 2020 Feihe Master Agreement and all transactions and the Proposed New Annual Caps and other matters contemplated thereunder or ancillary thereto, to waive compliance from and/or agree to any amendment or supplement to any of the provisions of the 2020 Feihe Master Agreement and the Proposed New Annual Caps which in their opinion is not of a material nature and to effect or implement any other matters referred to in this resolution.”

For and on behalf of the Board of
YuanShengTai Dairy Farm Limited
Zhao Hongliang
Executive Director and Chairman

Hong Kong, 25 November 2021

<i>Registered office:</i>	<i>Head office and Principal Place of Business in the PRC:</i>	<i>Principal place of business in Hong Kong:</i>
Clarendon House	Qingxiang Street	31/F, 148 Electric Road
2 Church Street	Kedong, Qiqihar	North Point
Hamilton HM 11	Heilongjiang Province	Hong Kong
Bermuda	PRC	

Notes:

1. The register of members of the Company will be closed from Friday, 10 December 2021 to Wednesday, 15 December 2021, both days inclusive, during which period no transfer of shares of the Company will be registered. In order to qualify for voting at the special general meeting of the Company, all transfers of shares of the Company accompanied by the relevant share certificates must be lodged for registration with the Company's branch share registrar in Hong Kong, Computershare Hong Kong Investor Services Limited at Shops 1712-1716, 17th Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong, no later than 4:30 p.m. on Thursday, 9 December 2021.
2. Any member of the Company (the “**Member**”) entitled to attend and vote at the SGM convened by the Notice or its adjourned meeting (as the case may be) is entitled to appoint one (or, if he/she/it holds two or more shares in the Company, more than one) proxy to attend and, on a poll, vote on his/her/its behalf subject to the provisions of the By-laws of the Company. A proxy need not be a Member but must be present in person at the SGM to represent the Member. If more than one proxy is so appointed, the appointment shall specify the number and class of shares in respect of which such proxy is so appointed.
3. In order to be valid, the form of proxy must be deposited together with a power of attorney or other authority, if any, under which it is signed or a notarially certified copy of that power or authority, at the offices of the Company's branch share registrar and transfer office in Hong Kong, Computershare Hong Kong Investor Services Limited, at 17M Floor, Hopewell Centre, 183 Queen's Road East, Wanchai, Hong Kong not less than 48 hours before the time for holding the SGM (i.e. no later than 10:00 a.m. (Hong Kong time) on Monday, 13 December 2021) or adjourned meeting. completion and return of a form of proxy will not preclude a Member from attending in person and voting at the SGM or any adjournment thereof should he/she so wish.

NOTICE OF THE SPECIAL GENERAL MEETING

4. Where there are joint holders of any ordinary share of the Company, any one of such holders may vote at the meeting, either personally or by proxy, in respect of such share as if he were solely entitled thereto, but if more than one of such holders be present at the meeting personally or by proxy, that one of such holders so present whose name stands first on the register of members of the Company in respect of such share shall alone be entitled to vote in respect thereof.
5. Voting of the ordinary resolution set out in this notice will be by way of poll.
6. Unless the context otherwise requires, terms used in this notice shall have the same meanings as those defined in the circular to the shareholders of the Company dated 25 November 2021.

As at the date of this notice, the Board comprises four executive Directors, namely Mr. Zhao Hongliang (Chairman), Mr. Fu Wenguo (Chief Executive Officer), Mr. Chen Xiangqing (Chief Financial Officer) and Mr. Liu Gang; three non-executive Directors, namely Mr. Leng Youbin, Mr. Liu Hua and Mr. Cai Fangliang; and four independent non-executive Directors, namely Mr. Meng Jingzong (alias Owens Meng), Mr. Zhang Yuezhou, Mr. Zhu Zhanbo and Ms. Liu Jinping.