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CHINA SHENGMU ORGANIC MILK LIMITED

中國聖牧有機奶業有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 1432)

RENEWAL OF CONTINUING CONNECTED TRANSACTION

Raw Fresh Milk Supply Framework Agreement

RAW FRESH MILK SUPPLY FRAMEWORK AGREEMENT

The Company announces that on 17 November 2022, Shengmu High-tech (for itself and on behalf of its subsidiaries), an indirect wholly-owned subsidiary of the Company, entered into the Raw Fresh Milk Supply Framework Agreement with Inner Mongolia Mengniu (for itself and on behalf of its subsidiaries) in relation to the purchase of raw fresh milk by China Mengniu Group from the Group for a term of three years commencing from 1 January 2023 to 31 December 2025.

LISTING RULES IMPLICATIONS

As at the date of this announcement, Shengmu High-tech is an indirect wholly-owned subsidiary of the Company and Inner Mongolia Mengniu is a non-wholly owned subsidiary of China Mengniu.

As at the date of this announcement, to the best of the Directors' knowledge, information and belief having made all reasonable enquiry, China Mengniu holds 100% equity interest in Start Great, which in turn holds approximately 29.99% equity interest in the Company. Accordingly, each of Start Great, China Mengniu and Inner Mongolia Mengniu is a connected person of the Company.

As one or more applicable percentage ratios under the Listing Rules in respect of the highest proposed annual cap under the Raw Fresh Milk Supply Framework Agreement exceed 5%, the entering into of the Raw Fresh Milk Supply Framework Agreement and the transactions contemplated thereunder are subject to the reporting, announcement and independent shareholders' approval requirements under Chapter 14A of the Listing Rules. Start Great will be required to abstain from voting at the EGM in relation to the Raw Fresh Milk Supply Framework Agreement and the transactions contemplated under such agreement. Save as disclosed above, to the best of the Directors' knowledge, information and belief having made all reasonable enquiry, no Shareholder is required to abstain from voting at the EGM in relation to the Raw Fresh Milk Supply Framework Agreement and the transactions contemplated under such agreement.

GENERAL

An Independent Board Committee has been established to advise the Independent Shareholders in respect of the Raw Fresh Milk Supply Framework Agreement, the transactions contemplated under such agreement and the proposed annual caps for such transaction for the three years ending 31 December 2023, 2024 and 2025.

The Board has appointed Somerley as the Independent Financial Advisor to advise the Independent Board Committee and the Independent Shareholders in this regard.

A circular containing, among other things, (1) details of the Raw Fresh Milk Supply Framework Agreement and the proposed annual caps; (2) a letter of advice from the Independent Financial Advisor to the Independent Board Committee and Independent Shareholders; (3) a letter from the Independent Board Committee in relation to the Raw Fresh Milk Supply Framework Agreement and the proposed annual caps, and (4) the notice convening the EGM is expected to be dispatched to the Shareholders before 8 December 2022 (and currently expected to be on or around 5 December 2022), so that the Company could have sufficient time to prepare information for inclusion in the circular.

Reference is made to the announcement of the Company dated 30 December 2019 and the circular of the Company dated 6 March 2020 in relation to, among other things, the raw fresh milk supply framework agreement dated 30 December 2019 and entered into between Shengmu High-tech and Inner Mongolia Mengniu in relation to the purchase of raw fresh milk by China Mengniu Group from the Group for a three-year term from 1 January 2020 to 31 December 2022.

The Company announces that on 17 November 2022, Shengmu High-tech (for itself and on behalf of its subsidiaries), an indirect wholly-owned subsidiary of the Company, entered into the Raw Fresh Milk Supply Framework Agreement with Inner Mongolia Mengniu (for itself and on behalf of its subsidiaries) in relation to the purchase of raw fresh milk by China Mengniu Group from the Group for a term of three years commencing from 1 January 2023 to 31 December 2025.

RAW FRESH MILK SUPPLY FRAMEWORK AGREEMENT

Principal Terms

The principal terms of the Raw Fresh Milk Supply Framework Agreement are summarised as follows:

- Date: 17 November 2022
- Parties: Shengmu High-tech (for itself and on behalf of its subsidiaries) and Inner Mongolia Mengniu (for itself and on behalf of its subsidiaries)
- Term: From 1 January 2023 to 31 December 2025
- Principal terms: The Group shall sell raw fresh milk which meets China Mengniu Group’s purchasing standard and quality requirements to China Mengniu Group on a daily basis in accordance with the monthly milk supply plan to be agreed between the Group and China Mengniu Group, and the Group shall ensure that on average more than 80% of the raw fresh milk it produces in each year will be sold to China Mengniu Group. The specific amount to be purchased shall be the amount as confirmed by the Group and China Mengniu Group. The daily delivery amount is determined by the amount as weighted by China Mengniu Group.
- Delivery: The Group shall be responsible for delivering raw fresh milk to the locations designated by China Mengniu Group. If the Group is unable to deliver milk in a timely manner, the Group shall notify China Mengniu Group at least 24 hours prior to the scheduled delivery and the Group shall bear related losses suffered by China Mengniu Group.
- Payment terms: China Mengniu Group shall pay monthly in accordance with the purchase amount of raw fresh milk, and payment for raw fresh milk purchased in any month shall be settled by the end of the following month. The monthly payment date shall be before the 30th calendar day of each month (or the 28th calendar day for February). If the monthly payment date falls on a statutory holiday, the payment date will be postponed to the first working day after the statutory holiday.

Purchase Price and Pricing Mechanism

The purchase price of raw fresh milk to be sold by the Group to China Mengniu Group under the Raw Fresh Milk Supply Framework Agreement shall be determined and adjusted in accordance with the following pricing mechanism:

- (a) the base price (the “**Base Price**”) shall be determined based on market conditions, seasonal factors and sales price of raw fresh milk in the region, as agreed between Shengmu High-tech and Inner Mongolia Mengniu;
- (b) the logistics subsidy as agreed between Shengmu High-tech and Inner Mongolia Mengniu based on the prevailing logistics costs incurred by the dairy farming industry and the distance between the customer’s location and Shengmu High-tech’s dairy farm(s); and
- (c) adjustments as agreed between Shengmu High-tech and Inner Mongolia Mengniu based on the quality and rating of raw fresh milk, taking into account various milk quality indicators, such as level of protein, fat content, somatic cell count, microorganism count and freezing point etc. (together with the logistics subsidy referred to in paragraph (b) above, the “**Adjustments**”).

Internal Control Mechanism

Timely Delivery of Raw Fresh Milk

The Group has established an internal control mechanism to ensure the timely delivery of raw fresh milk. The Group maintains a three-month rolling plan for the herd and milk production to ensure that the Group has sufficient milk production capacity to meet the monthly supply plans for raw fresh milk. In addition, the dairy farms of the Group and the dairy products manufacturing facilities of China Mengniu Group are located in the same region. The maximum transportation distance for the supply of raw fresh milk from the dairy farms of the Group to the manufacturing facilities of China Mengniu Group is less than 110 kilometres and the transportation time is generally less than two hours. Given the close proximity, the Group is able to coordinate additional resources to meet the monthly supply plans if there is any emergency situation.

To the best of the Directors’ knowledge, information and belief having made all reasonable enquiry, the term in the Raw Fresh Milk Supply Framework Agreement that the Group shall bear the losses suffered by China Mengniu Group if the Group fails to deliver raw fresh milk in a timely manner is a common term in similar agreements between China Mengniu Group and its suppliers of raw fresh milk which

are independent from China Mengniu Group. Therefore, the Board considers that such term is on normal commercial terms and in the interest of the Company. The Group endeavors to deliver its products in a timely manner, and as at the date of this announcement, the Group has not incurred any penalty due to late delivery of raw fresh milk to China Mengniu Group historically.

Referencing Market Prices

The Group formulates an annual supply plan for raw fresh milk, which is then divided into monthly supply plans taking into account the volume required by China Mengniu Group. The unit price of raw fresh milk, which comprises the Base Price and the Adjustments, is determined on a monthly basis. The Sales Team will review on a monthly basis the actual volume of raw fresh milk supplied. The Sales Team will also evaluate the fairness of the unit price by examining and considering the quantitative data from the test results of the milk quality indicators and checking whether the unit price has correctly reflected the test results of the raw fresh milk.

The Group's pricing mechanism with its customers (including China Mengniu Group and other independent third party customers) is generally the same and therefore the selling price of raw fresh milk to be sold by the Group to China Mengniu Group under the Raw Fresh Milk Supply Framework Agreement would be comparable to that of the other independent third party customers. The Group has established the following internal control measures to ensure that the purchase price and other terms of the sale of raw fresh milk by the Group to China Mengniu Group contemplated under the Raw Fresh Milk Supply Framework Agreement are no less favourable than the terms offered to independent third party customers, where the Sales Team has been tasked with:

- (a) considering and comparing prices and terms of similar products offered by the Group to other purchasers every month;
- (b) conducting market research every month and comparing the selling price of similar products offered by three other raw fresh milk producers when determining the Base Price for each month;
- (c) reviewing other terms of orders received from China Mengniu Group and other independent third party customers to ensure that the other terms offered by the Group to China Mengniu Group are no less favourable to those offered to independent third party customers; and
- (d) ensuring that each sale is executed at a purchase price determined in accordance with the relevant pricing mechanism as set out above in this announcement.

General

The Company has also implemented internal control procedures and policies led by the Group's compliance team to monitor connected transactions with an emphasis on, among others, (1) maintenance of a list of connected persons and connected transactions; (2) identifying connected transactions with the assistance of various departments and external legal advisors; (3) analysis on aggregating connected transactions and managing any aggregated transaction amounts; and (4) monitoring utilization of annual caps of continuing connected transactions on a monthly basis.

The Group's compliance team will conduct an annual review to verify if the continuing connected transactions are conducted in compliance with the terms of the Raw Fresh Milk Supply Framework Agreement and Chapter 14A of the Listing Rules. The compliance team will prepare and submit a report of its findings to the management and Audit Committee of the Company.

The Group's external auditors and independent non-executive Directors shall conduct an annual review and confirm whether the transactions have been entered into in accordance with the terms of the Raw Fresh Milk Supply Framework Agreement in the Company's annual report in accordance with the Listing Rules.

Reasons for and Benefits of Entering into the Raw Fresh Milk Supply Framework Agreement

As one of the leading dairy product manufacturers in the PRC, China Mengniu Group is equipped with a strong management team and a solid dairy product distribution network, offering diversified products including liquid milk products, ice cream, milk formula and cheese. The Company believes that a raw fresh milk supply relationship with China Mengniu Group (taking into account, among other things, the Group's commitment to supply on average more than 80% of the raw fresh milk it produces in each year to China Mengniu Group) will help to stabilise the price and sales volume of raw fresh milk and generate stable income and cash flow for the Group.

The dairy farms of the Group are mainly located in the regions of Hohhot and Bayannur, and China Mengniu Group has sufficient raw fresh milk processing capacity in these regions. The short transportation distance ensures the freshness of raw fresh milk supplied by the Group, which in turn contributes to the high quality of milk products manufactured by China Mengniu Group. It also lowers the Group's costs of transportation and preservation, which makes the price of raw fresh milk supplied by the Group more competitive as compared to other suppliers of raw fresh milk.

Whilst focusing on the production and sale of desert-based organic milk, the Group also endeavors to satisfy customers' diversified needs for quality raw milk and continues to develop a variety of functional raw milk to enhance the Group's product mix and profitability.

The collaboration between the Group and China Mengniu Group, which eventually leads to the growth of demand of desert-based organic milk through channels such as marketing and distribution, would enhance the awareness of the Group's milk products and in turn promote the Group's sales growth, thereby achieving a win-win outcome for both groups. Therefore, the Board expects the likelihood of a significant adverse change to the business relationship with China Mengniu Group to be relatively low.

In the unlikely event of any change to the business relationship between the Group and China Mengniu Group, the Board believes that the raw fresh milk produced by the Group can be sold to other major customers in the region, and such change will not have a material impact on the financial position of the Group. In particular,

- (a) the Group has been actively expanding its sales team and looking for new customers. The Sales Team regularly arranges meetings and dairy farm visits with target customers. The Sales Team also attends industry events to explore more diversified sales opportunities. The Group believes that its outstanding achievements in carbon neutrality and desert circulation agriculture system will attract customers;
- (b) the Group is constantly seeking to diversify its product portfolio and develop new products based on market needs as part of the Group's effort to enhance its sales and marketing;
- (c) as the environmental and industry regulations become increasingly stringent, some small farm operators have withdrawn from the market due to increased operating costs and non-compliance as a result of substandard supervision, and such changes are conducive to the healthy development of large-scale dairy farms in the future;
- (d) with the impact of consumption upgrade, urban citizens have a growing demand of high quality organic milk. The Board expects that the Group will benefit from the upward trend of the organic dairy industry and have a relatively high growth rate; and

- (e) the high quality of the Group's milk products (in terms of purity and freshness), in particular its organic raw milk, is well recognized both in the market and by relevant authorities (as evidenced by various product certifications). Apart from China Mengniu Group, the Group also supplies raw fresh milk to other independent third party dairy product manufacturers in the PRC.

In light of the factors mentioned above, the Directors (excluding the independent non-executive Directors) are of the view that the Raw Fresh Milk Supply Framework Agreement is entered into on normal commercial terms and in the ordinary course of business of the Group, are in the interests of the Company and the Shareholders as a whole, and the terms of the Raw Fresh Milk Supply Framework Agreement (including the proposed annual caps) are fair and reasonable.

Historical Transaction Amounts

The raw fresh milk sold by the Group to China Mengniu Group for the three years ended 31 December 2019, 2020 and 2021 and the nine months ended 30 September 2022 amounted to RMB2,350,989,496, RMB2,504,619,468, RMB2,621,629,144 and RMB2,171,776,462, respectively.

Proposed Annual Caps

The Directors propose that the total annual sales amount by the Group to China Mengniu Group under the Raw Fresh Milk Supply Framework Agreement shall not exceed RMB3,400 million, RMB4,300 million and RMB5,000 million for the three years ending 31 December 2023, 2024 and 2025, respectively.

As disclosed in the interim report of the Company for the six months ended 30 June 2022, in order to realise the Group's strategic plans to grow its organic milk sales, the Group commenced the construction of a dairy farming demonstration zone at its base in the Ulan Buh Desert earlier this year. The Group plans to build a 10,000-head dairy farm and an organic demonstration farm in the demonstration zone, the construction of which is expected to be completed in 2023. When the demonstration zone commences full operation, it is expected the 10,000-head dairy farm will produce approximately 80,000 tonnes of high quality organic milk per year whilst the organic demonstration farm will produce an average of approximately 20,000 tonnes of fresh milk per year. The newly built demonstration zone will significantly enhance the production capacity of the Group, bolstering its ability to satisfy orders for raw fresh milk from the Group's customers, including orders from China Mengniu Group. For the six months ended 30 June 2022, the Group sold a total of 311,565 tonnes of raw milk and, as at the end of that period, had a total of 130,802 cows in stock, of

which 86,578 were organic cows. In addition, in determining such annual caps, the Directors have also considered the following factors:

- (a) the expected number of milkable cows of the Group (taking into account anticipated purchases and improvement in dairy cow breeding capacity, etc.) and the expected increase in the overall sales volume of raw fresh milk by the Group for the three years ending 31 December 2023, 2024 and 2025;
- (b) the expected increase in sales volume of raw fresh milk to China Mengniu Group taking into account, among other things, the Group's commitment to supply on average more than 80% of the raw fresh milk it produces in each year to China Mengniu Group;
- (c) the potential increase in price of dairy products in China;
- (d) the historical and prevailing purchase price for raw fresh milk paid by China Mengniu Group; and
- (e) the historical transaction amounts of raw fresh milk sold by the Group to China Mengniu Group for the three years ended 31 December 2019, 2020 and 2021 and the nine months ended 30 September 2022 respectively, as mentioned above.

LISTING RULES IMPLICATIONS

As at the date of this announcement, Shengmu High-tech is an indirect wholly-owned subsidiary of the Company and Inner Mongolia Mengniu is a non-wholly owned subsidiary of China Mengniu.

As at the date of this announcement, to the best of the Directors' knowledge, information and belief having made all reasonable enquiry, China Mengniu holds 100% equity interest in Start Great, which in turn holds approximately 29.99% equity interest in the Company. Accordingly, each of Start Great, China Mengniu and Inner Mongolia Mengniu is a connected person of the Company.

As one or more applicable percentage ratios under the Listing Rules in respect of the highest proposed annual cap under the Raw Fresh Milk Supply Framework Agreement exceed 5%, the entering into of the Raw Fresh Milk Supply Framework Agreement and the transactions contemplated thereunder are subject to the reporting, announcement and independent shareholders' approval requirements under Chapter 14A of the Listing Rules. Start Great will be required to abstain from voting at the EGM in relation to the Raw Fresh Milk Supply Framework Agreement and the transactions contemplated under such agreement. Save as disclosed above, to the best

of the Directors' knowledge, information and belief having made all reasonable enquiry, no Shareholder is required to abstain from voting at the EGM in relation to the Raw Fresh Milk Supply Framework Agreement and the transactions contemplated under such agreement.

Mr. Lu Minfang, a non-executive Director and chairman of the Board, is also an executive director and chief executive officer of China Mengniu. Mr. Zhang Ping, a non-executive Director, is also an executive director, vice president and chief financial officer of China Mengniu. Mr. Lu and Mr. Zhang have abstained from voting on the resolutions of the Directors approving the Raw Fresh Milk Supply Framework Agreement and the transactions contemplated thereunder. Other than Mr. Lu and Mr. Zhang, no Director is materially interested in the transactions contemplated under the Raw Fresh Milk Supply Framework Agreement and no Director is required to abstain from voting on the resolutions of the Directors to approve the Raw Fresh Milk Supply Framework Agreement and the transactions contemplated under such agreement.

The independent non-executive Directors will set out in the circular to be dispatched to the Shareholders their views in respect of the Raw Fresh Milk Supply Agreement, the transactions contemplated under such agreement and the proposed annual caps for the three years ending 31 December 2023, 2024 and 2025, which will be formed after taking into account the advice to be provided by Somerley, the Independent Financial Advisor.

INFORMATION ON THE PARTIES

The Company is an investment holding company. The Group is principally engaged in dairy farming business.

Shengmu High-tech is an indirect wholly-owned subsidiary of the Company and is principally engaged in dairy farming and the sale of raw milk.

Inner Mongolia Mengniu is a non-wholly owned subsidiary of China Mengniu and is principally engaged in the business of manufacture and sale of dairy products.

China Mengniu is a company listed on the Stock Exchange and is one of the leading dairy product manufacturers in the PRC. China Mengniu Group is principally engaged in manufacturing and distribution of quality dairy products including liquid milk, ice-cream, milk formula and other dairy products.

GENERAL

An Independent Board Committee has been established to advise the Independent Shareholders in respect of the Raw Fresh Milk Supply Framework Agreement, the transactions contemplated under such agreement and the proposed annual caps for such transaction for the three years ending 31 December 2023, 2024 and 2025.

The Board has appointed Somerley as the Independent Financial Advisor to advise the Independent Board Committee and the Independent Shareholders in this regard.

A circular containing, among other things, (1) details of the Raw Fresh Milk Supply Framework Agreement and the proposed annual caps; (2) a letter of advice from the Independent Financial Advisor to the Independent Board Committee and Independent Shareholders; (3) a letter from the Independent Board Committee in relation to the Raw Fresh Milk Supply Framework Agreement and the proposed annual caps, and (4) the notice convening the EGM is expected to be dispatched to the Shareholders before 8 December 2022 (and currently expected to be on or around 5 December 2022), so that the Company could have sufficient time to prepare information for inclusion in the circular.

DEFINITIONS

In this announcement, unless the context otherwise requires, the following terms shall have the following meanings:

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| “Board” | the board of Directors |
| “China Mengniu” | China Mengniu Dairy Company Limited (中國蒙牛乳業有限公司), a company incorporated in Cayman Islands with limited liability, the shares of which are listed on the Stock Exchange (stock code: 2319) |
| “China Mengniu Group” | Inner Mongolia Mengniu and its subsidiaries from time to time |
| “Company” | China Shengmu Organic Milk Limited (中國聖牧有機奶業有限公司), a company incorporated in the Cayman Islands with limited liability, the shares of which are listed on the Stock Exchange (stock code: 1432) |
| “connected person(s)” | has the meaning ascribed to it under the Listing Rules |
| “Director(s)” | the director(s) of the Company |

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| “EGM” | the extraordinary general meeting of the Company to be convened for the purpose of considering and, if thought fit, approving, among other things, the Raw Fresh Milk Supply Framework Agreement (including the proposed annual caps) and the transactions contemplated under such agreement |
| “Group” | the Company and its subsidiaries from time to time |
| “Hong Kong” | Hong Kong Special Administrative Region of the PRC |
| “Independent Board Committee” | a committee of the Board comprising all the independent non-executive Directors, namely, Mr. Wang Liyan, Mr. Wu Liang and Mr. Sun Yansheng |
| “Independent Financial Advisor” or “Somerley” | Somerley Capital Limited, a corporation licensed by the Securities and Futures Commission to conduct Type 1 (dealing in securities) and Type 6 (advising on corporate finance) regulated activities under the Securities and Futures Ordinance, who is appointed to advise the Independent Board Committee and the Independent Shareholders in respect of the Raw Fresh Milk Supply Framework Agreement and the transactions contemplated under such agreement |
| “Independent Shareholder(s)” | Shareholders other than Start Great and its associates |
| “Inner Mongolia Mengniu” | Inner Mongolia Mengniu Dairy (Group) Company Limited (內蒙古蒙牛乳業(集團)股份有限公司), a company established in the PRC with limited liability and a non-wholly owned subsidiary (as to 99.99%) of China Mengniu |
| “Listing Rules” | the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited |
| “PRC” | the People’s Republic of China and for the purpose of this announcement, does not include Hong Kong, Macao Special Administrative Region and Taiwan |

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| “Raw Fresh Milk Supply Framework Agreement” | the raw fresh milk supply framework agreement dated 17 November 2022, entered into between Shengmu High-tech (for itself and on behalf of its subsidiaries) and Inner Mongolia Mengniu (for itself and on behalf of its subsidiaries), in relation to the purchase of raw fresh milk by China Mengniu Group from the Group for a three-year term from 1 January 2023 to 31 December 2025 |
| “RMB” | Renminbi, the lawful currency of the PRC |
| “Sales Team” | the sales team of the Group |
| “Shareholder(s)” | holder(s) of the Shares |
| “Shares” | ordinary share(s) of par value HK\$0.00001 each in the issued share capital of the Company |
| “Shengmu High-tech” | Inner Mongolia Shengmu High-tech Farming Co., Ltd. (內蒙古聖牧高科牧業有限公司), a company established in the PRC and an indirect wholly-owned subsidiary of the Company |
| “Start Great” | Start Great Holdings Limited, a company established in the British Virgin Islands with its registered office at Vistra Corporate Services Centre, Wickhams Cay II, Road Town, Tortola, VG1110, British Virgin Islands, which is a direct wholly-owned subsidiary of China Mengniu |
| “Stock Exchange” | The Stock Exchange of Hong Kong Limited |

By Order of the Board
China Shengmu Organic Milk Limited
Lu Minfang
Chairman

Hong Kong, 17 November 2022

As at the date of this announcement, the executive Director of the Company is Mr. Zhang Jiawang; the non-executive Directors of the Company are Mr. Lu Minfang, Mr. Sun Qian, Mr. Zhang Ping, Mr. Zhao Jiejun, Ms. Shao Lijun; and the independent non-executive Directors of the Company are Mr. Wang Liyan, Mr. Wu Liang and Mr. Sun Yansheng.