雅士利

Yashili International Holdings Ltd

雅士利國際控股有限公司

(Incorporated in the Cayman Islands with limited liability)

(Stock Code: 1230)

ANNOUNCEMENT OF INTERIM RESULTS FOR THE SIX MONTHS ENDED 30 JUNE 2017

FINANCIAL HIGHLIGHTS

	For the six months ended 30 June		
	2017	2016	Percentage
	RMB million	*RMB million*	change
Revenue	**966.7**	1,146.5	(15.7%)
Gross profit	**447.6**	580.5	(22.9%)
Profit attributable to equity holders of the parent	**(121.9)**	15.1	(907.3%)
Earnings per share (RMB cents)			
— Basic and diluted	**(2.6)**	0.3	(966.7%)

For the six months ended 30 June 2017, the revenue of the Group amounted to RMB966.7 million (same period of 2016: RMB1,146.5 million), representing a decrease of 15.7% from the same period of 2016. The decrease in revenue of the Group was mainly due to: (1) the accelerated shrinking of the modern and traditional channels compromised the Group's existing competitive advantages in these channels and the Group withdrew from some inefficient stores of such modern and traditional channels; (2) during the first half of 2017, the Group continued to deal with the sales model transformation of the mother-and-baby store channel and the e-commerce channel whereby the implementation and effect of the new marketing strategies require time and cost input; (3) the Group increased its promotion efforts during the first half of 2017 to cope with the intensified market competition; and (4) the Group was proactively consolidating its product lines in response to the impact brought by the Administrative Measures for the Registration of Recipes of Infant Formula Milk Powder Products (the "Recipe Registration Requirement"), and such consolidation may affect the sales of some products to a certain extent.

The board of directors (the "**Board**") of Yashili International Holdings Ltd (the "**Company**") is pleased to announce the unaudited consolidated results of the Company and its subsidiaries (the "**Group**") for the interim period ended 30 June 2017 together with the comparative figures for the same period of 2016 as follows.

UNAUDITED INTERIM CONDENSED CONSOLIDATED STATEMENT OF PROFIT OR LOSS

		Unaudited	
		For the six months ended 30 June	
		2017	2016
	Notes	***RMB'000***	*RMB'000*
Revenue	*3*	**966,694**	1,146,511
Cost of sales	*4*	**(519,103)**	(566,042)
Gross profit		**447,591**	580,469
Other income and gains	*3*	**52,152**	39,414
Selling and distribution expenses		**(490,667)**	(493,429)
Administrative expenses		**(113,972)**	(159,886)
Other expenses		**(109,243)**	(50,075)
Loss from operations		**(214,139)**	(83,507)
Finance income	*4*	**64,825**	77,032
Finance costs		**(10,366)**	(6,188)
Net finance income		**54,459**	70,844
Loss before tax		**(159,680)**	(12,663)
Income tax credit	*5*	**37,742**	27,736
(Loss)/profit for the period		**(121,938)**	15,073
Attributable to:			
Owners of the parent	*6*	**(121,938)**	15,073
		RMB cents	*RMB cents*
(Loss)/earnings per share attributable to ordinary equity holders of the parent			
Basic and diluted	*6*	**(2.6)**	0.3

UNAUDITED INTERIM CONDENSED CONSOLIDATED STATEMENT OF COMPREHENSIVE INCOME

	Unaudited	
	For the six months ended 30 June	
	2017	2016
	RMB'000	*RMB'000*
(Loss)/profit for the period	**(121,938)**	15,073
Other comprehensive income		
Exchange differences on translation of financial statements of overseas subsidiaries	**40,508**	65,897
Other comprehensive income for the period	**40,508**	65,897
Total comprehensive (loss)/income for the period	**(81,430)**	80,970
Attributable to:		
Owners of the parent	**(81,430)**	80,970

UNAUDITED INTERIM CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION

	Notes	**Unaudited 30 June 2017** *RMB'000*	Audited 31 December 2016 *RMB'000*
NON-CURRENT ASSETS			
Property, plant and equipment		**1,758,391**	1,788,658
Construction in progress		**52,895**	38,812
Investment properties		**30,629**	67,486
Land use rights		**88,928**	93,734
Intangible assets		**297,289**	297,801
Goodwill		**991,236**	991,236
Deferred tax assets		**249,872**	202,950
Long-term bank deposits		**—**	379,927
Prepayments, deposits and other receivables		**4,116**	5,496
Total non-current assets		**3,473,356**	3,866,100
CURRENT ASSETS			
Inventories	*7*	**678,576**	619,876
Trade and bills receivables	*8*	**161,956**	161,391
Prepayments, deposits and other receivables	*9*	**227,938**	191,230
Other financial assets		**413,706**	476,994
Pledged deposits	*10*	**833,030**	803,123
Cash and bank balances	*10*	**1,922,190**	1,642,818
		4,237,396	3,895,432
Assets of a disposal group classified as held for sale		**203,891**	204,459
Total current assets		**4,441,287**	4,099,891
CURRENT LIABILITIES			
Trade payables	*11*	**337,479**	237,621
Other payables and accruals		**821,294**	862,233
Interest-bearing bank loans	*13*	**1,115,761**	1,143,091
Tax payable		**3,192**	5,602
		2,277,726	2,248,547
Liabilities directly associated with assets classified as held for sale		**4,345**	4,988
Total current liabilities		**2,282,071**	2,253,535
NET CURRENT ASSETS		**2,159,216**	1,846,356
TOTAL ASSETS LESS CURRENT LIABILITIES		**5,632,572**	5,712,456

UNAUDITED INTERIM CONDENSED CONSOLIDATED STATEMENT OF FINANCIAL POSITION (Continued)

	Unaudited 30 June 2017	Audited 31 December 2016
	RMB'000	*RMB'000*
NON-CURRENT LIABILITIES		
Deferred income	**2,787**	3,329
Deferred tax liabilities	**9,601**	7,513
Total non-current liabilities	**12,388**	10,842
NET ASSETS	**5,620,184**	5,701,614
EQUITY		
Equity attributable to owners of the parent		
Share capital	**399,352**	399,352
Reserves	**5,220,832**	5,302,262
TOTAL EQUITY	**5,620,184**	5,701,614

NOTES TO THE UNAUDITED INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

1. BASIS OF PREPARATION AND CHANGES IN THE GROUP'S ACCOUNTING POLICIES

1.1 Basis of preparation

The interim condensed consolidated financial statements for the six months ended 30 June 2017 have been prepared in accordance with IAS 34 Interim Financial Reporting issued by the International Accounting Standards Board (the IASB) and the disclosure requirements of the Rules Governing the Listing of Securities on the Stock Exchange of Hong Kong Limited.

The interim condensed consolidated financial statements do not include all the information and disclosures required in the annual financial statements, and should be read in conjunction with the Group's annual financial statements for the year ended 31 December 2016.

1.2 New standards and amendments adopted by the Group

The accounting policies adopted in the preparation of these interim condensed consolidated financial statements are consistent with those followed in the Group's annual financial statements for the year ended 31 December 2016, except for the adoption of new standards effective as of 1 January 2017.

The nature and the effect of those new standards are disclosed below. Although these amendments apply for the first time in 2017, they do not have a material impact on the annual consolidated financial statements of the Group or the interim unaudited condensed consolidated financial statements of the Group. The nature and the impact of each amendment is described below:

Amendments to IAS 7 Statement of Cash Flows: Disclosure Initiative

The amendments require entities to provide disclosures about changes in their liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes (such as foreign exchange gains or losses). On initial application of the amendments, entities are not required to provide comparative information for preceding periods. The Group is not required to provide additional disclosures in its condensed interim consolidated financial statements, but will disclose additional information in its annual consolidated financial statements for the year ending 31 December 2017.

1. BASIS OF PREPARATION AND CHANGES IN THE GROUP'S ACCOUNTING POLICIES (Continued)

1.2 New standards and amendments adopted by the Group (Continued)

Amendments to IAS 12 Income Taxes: Recognition of Deferred Tax Assets for Unrealised Losses

The amendments clarify that an entity needs to consider whether tax law restricts the sources of taxable profits against which it may make deductions on the reversal of that deductible temporary difference. Furthermore, the amendments provide guidance on how an entity should determine future taxable profits and explain the circumstances in which taxable profit may include the recovery of some assets for more than their carrying amount.

Entities are required to apply the amendments retrospectively. However, on initial application of the amendments, the change in the opening equity of the earliest comparative period may be recognised in opening retained earnings (or in another component of equity, as appropriate), without allocating the change between opening retained earnings and other components of equity. Entities applying this relief must disclose that fact.

The Group applied the amendments retrospectively. However, their application has no effect on the Group's financial position and performance as the Group has no deductible temporary differences or assets that are in the scope of the amendments.

Annual Improvements Cycle — 2014–2016
Amendments to IFRS 12 Disclosure of Interests in Other Entities: Clarification of the scope of disclosure requirements in IFRS 12

The amendments clarify that the disclosure requirements in IFRS 12, other than those in paragraphs B10–B16, apply to an entity's interest in a subsidiary, a joint venture or an associate (or a portion of its interest in a joint venture or an associate) that is classified (or included in a disposal group that is classified) as held for sale.

The Group has adopted the amendments retrospectively. As the disclosure requirements in IFRS 12 do not specifically apply to the interim condensed consolidated financial statements, the Group did not provide these disclosures for its interest in Scient (China) Baby Nourishment Co., Ltd., a wholly owned subsidiary that was classified as held for sale as at 30 June 2017. The Group will disclose the required information in its annual consolidated financial statements for the year ending 31 December 2017.

2. OPERATING SEGMENT INFORMATION

Since the acquisition of Oushi Mengniu (Inner Mongolia) Dairy Products Co., Ltd ("Oushi Mengniu") and Dumex Baby Food Co., Ltd. ("Dumex China") in 2015 and 2016, respectively, and the operation of Yashili New Zealand Dairy Co., Limited ("Yashili New Zealand") at the end of 2015, the Group underwent various group reorganisation, including the purchase, production and sales functions.

From the second half of 2016, the Group is reorganised into business units based on their products and services and has three reportable operating segments as follows:

(a) Production and sale of infant milk formula products — this segment includes the development, manufacture and sale of infant milk formula products in the PRC and overseas.

(b) Production and sale of nutrition products — this segment includes the development, manufacture and sale of milk powder for adults and teenagers, soymilk powder, rice flour and cereal products in the PRC and overseas.

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

(c) Other operations mainly include the sale of surplus raw materials and the production and the sale of base-powder, and the results of these operations are included in the "others" column.

The change was made to improve the way in which the business units can be managed. Comparative figures of the operating segment information have been adjusted retrospectively.

For the purpose of assessing segment performance and allocating resources among segments, the senior executive management team assesses the performance of the operating segments based on a measure of "reportable segment profit", i.e., "revenue less cost of sales and selling and distribution expenses". The Group does not allocate other income and gains, net finance costs, expenses other than certain selling and distribution expenses to its segments, as the senior executive management does not use this information to allocate resources to or evaluate the performance of the operating segments. Segment assets and liabilities are not regularly reported to the Group's senior executive management and therefore information of reportable segment assets and liabilities is not presented in these condensed consolidated financial statements.

Intersegment sales and transfers are transacted with reference to the selling prices used for sales made to third parties at the then prevailing market prices.

	For the six months ended 30 June 2017 (Unaudited)			
	Infant milk formula products *RMB'000*	**Nutrition products** *RMB'000*	**Others** *RMB'000*	**Total** *RMB'000*
Segment revenue:				
Sales to external customers	**673,884**	**246,650**	**46,160**	**966,694**
Intersegment sales	**3,948**	**4,748**	**—**	**8,696**
	677,832	**251,398**	**46,160**	**975,390**
Reconciliation:				
Elimination of intersegment sales	**(3,948)**	**(4,748)**	**—**	**(8,696)**
Total revenue				**966,694**
Segment results	**(11,750)**	**(32,458)**	**2,469**	**(41,739)**
Reconciliation:				
Finance income				**64,825**
Finance costs				**(10,366)**
Other income and gains				**52,152**
Unallocated other expenses				**(224,552)**
Loss before tax				**(159,680)**

2. OPERATING SEGMENT INFORMATION (Continued)

	For the six months ended 30 June 2016 (Unaudited)			
	Infant milk formula products *RMB'000* Restated	Nutrition products *RMB'000* Restated	Others *RMB'000* Restated	Total *RMB'000* Restated
Segment revenue:				
Sales to external customers	825,210	312,204	9,097	1,146,511
Intersegment sales	16,327	7,844	—	24,171
	841,537	320,048	9,097	1,170,682
Reconciliation:				
Elimination of intersegment sales	(16,327)	(7,844)	—	(24,171)
Total revenue				1,146,511
Segment results	65,888	31,972	(1,012)	96,848
Reconciliation:				
Finance income				77,032
Finance costs				(6,188)
Other income and gains				39,414
Unallocated other expenses				(219,769)
Loss before tax				(12,663)

3. REVENUE, OTHER INCOME AND GAINS

An analysis of the Group's revenue, other income and gains is as follows:

		Unaudited For the six months ended 30 June	
		2017	2016
	Notes	***RMB'000***	*RMB'000*
Revenue			
Sales of goods	*(a)*	**966,694**	1,146,511
Other income and gains			
Government grants related to			
— expenses incurred		**30**	555
— assets		**542**	542
Other income			
— fines	*(b)*	**100**	735
— consigned processing operation	*(c)*	**32,503**	22,591
Foreign exchange gains		**10,200**	11,546
Gain on disposal of items of property, plant and equipment		**2,881**	—
Others		**5,896**	3,445
		52,152	39,414

Notes:

(a) Revenue represented the net invoiced value of goods sold, after allowance for returns (if any) and trade discounts.

(b) Income related to fines mainly represented amounts received from distributors for cross territorial sales that breached the terms of distribution agreements during the period.

(c) This mainly represented consigned processing income from processing raw milk powder for Inner Mongolia Mengniu (Group) Dairy Company Limited, a fellow subsidiary of the Company.

4. LOSS BEFORE TAX

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

	Unaudited For the six months ended 30 June	
	2017	2016
	RMB'000	*RMB'000*
Cost of goods sold	**519,103**	566,042
Depreciation of items of property, plant and equipment*	**79,248**	81,917
Depreciation of investment properties	**1,293**	2,474
Amortisation of prepaid land lease payments*	**2,260**	767
Amortisation of other non-current assets*	**2,107**	1,477
Amortisation of intangible assets*	**1,300**	1,362
Total depreciation and amortisation	**86,208**	87,997
Minimum lease payments under operating leases of buildings	**9,613**	5,166
Employee benefit expense* (excluding directors' and chief executive's remuneration):		
Wages, salaries and allowances	**226,681**	192,213
Termination benefits	**26,778**	1,414
Pension scheme contributions (defined contribution schemes)	**18,517**	16,042
	271,976	209,669
Interest income	**(58,195)**	(57,352)
Gain on other financial assets	**(6,630)**	(19,680)
Total finance income	**(64,825)**	(77,032)

* Part of these costs and expenses were included in "Costs of goods sold" as disclosed above.

5. INCOME TAX CREDIT

The major components of income tax credit in the unaudited interim condensed consolidated statement of profit or loss are:

	Unaudited	
	For the six months ended 30 June	
	2017	2016
	RMB'000	*RMB'000*
Current tax		
Provision for the period	**1,155**	15,471
Adjustments recognised in the period for current tax of prior years	**4,794**	1,697
Deferred tax	**(43,691)**	(44,904)
Total income tax credit	**(37,742)**	(27,736)

Pursuant to the Corporate Income Tax Law of the PRC passed by the Tenth National People's Congress on 16 March 2007 (the "Income Tax Law"), the statutory income tax rate of the Group's subsidiaries located in Mainland of PRC is 25%, except for Oushi Mengniu which is subject to a preferential tax rate of 15%, in accordance with "The notice of tax policies relating to the implementation of Western China Development Strategy".

Pursuant to the rules and regulations of the Cayman Islands and the British Virgin Islands (the "BVI"), the Group is not subject to any income tax in the Cayman Islands and the BVI.

The provision for Hong Kong profits tax for the six months ended 30 June 2017 is calculated at 16.5% (six months ended 30 June 2016: 16.5%) of the assessable profit for the period.

Pursuant to the rules and regulations of New Zealand, the Group's subsidiary located in New Zealand is subject to income tax at a rate of 28% during the six months ended 30 June 2017 (six months ended 30 June 2016: 28%).

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

The basic (loss)/earnings per share amount for the period is calculated by dividing the (loss)/profit for the period attributable to ordinary equity holders of the parent by the weighted average number of ordinary shares outstanding during the period.

The parent has no dilutive potential shares during the period.

The calculations of basic and diluted (loss)/earnings per share are based on:

	Unaudited For the six months ended 30 June **2017** ***RMB'000***	 2016 *RMB'000*
(Loss)/earnings:		
(Loss)/profit attributable to ordinary equity holders of the parent, used in the (loss)/earnings per share calculations	**(121,938)**	15,073
	Number of shares ***(in thousand)***	 *(in thousand)*
Shares:		
Weighted average number of ordinary shares for the purpose of the basic (loss)/earnings per share calculations	**4,745,560**	4,745,560

7. INVENTORIES

	Unaudited **30 June** **2017** ***RMB'000***	Audited 31 December 2016 *RMB'000*
Raw materials	**178,042**	208,030
Finished goods	**255,307**	232,761
Work in progress	**252,642**	180,259
Packing materials	**33,781**	29,297
Low value consumables	**920**	893
	720,692	651,240
Provisions	**(42,116)**	(31,364)
	678,576	619,876

8. TRADE AND BILLS RECEIVABLES

	Unaudited 30 June 2017 *RMB'000*	Audited 31 December 2016 *RMB'000*
Trade and bills receivables	**162,571**	162,138
Provision for impairment	**(615)**	(747)
	161,956	161,391

The Group normally allows a credit limit and credit term to its customers which is adjustable in certain circumstances. In view of the aforementioned and the fact that the Group's trade and bills receivables relate to a large number of diversified customers, there is no significant concentration of credit risk. Trade and bills receivables are non-interest-bearing.

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

	Unaudited 30 June 2017 *RMB'000*	Audited 31 December 2016 *RMB'000*
Within 3 months	**94,666**	117,057
3 to 6 months	**14,147**	38,521
More than 6 months	**53,143**	5,813
	161,956	161,391

Trade and bills receivables that were past due but not impaired relate to a number of independent customers that have a good track record with the Group. Based on past experience, the directors are of the opinion that no provision for impairment is necessary in respect of these balances as there has not been a significant change in credit quality and the balances are still considered fully recoverable.

As at 30 June 2017, all the assets of Yashili New Zealand including trade receivables of RMB29,478,986 were collateralized for a bank loan of RMB97,825,000 under a general security agreement.

The amounts due from related parties of the Group included in the trade receivables are as follows:

	Unaudited 30 June 2017 *RMB'000*	Audited 31 December 2016 *RMB'000*
Subsidiaries of the ultimate holding company	**38,090**	9,953
A substantial shareholder and its subsidiaries	**18,987**	—
	57,077	9,953

The above amounts are unsecured, non-interest-bearing and repayable on credit terms similar to those offered to the major customers of the Group.

9. PREPAYMENTS, DEPOSITS AND OTHER RECEIVABLES

	Unaudited 30 June 2017 ***RMB'000***	Audited 31 December 2016 *RMB'000*
Interest receivable	**64,105**	10,796
Other receivables arising from promotion services	**63,755**	91,999
Value-added tax recoverable	**34,477**	35,098
Prepayments for purchase of raw materials	**21,570**	10,886
Prepayments for purchase of advertising services	**—**	2,802
Others	**48,147**	45,145
	232,054	196,726
Less: Non-current prepayments	**4,116**	5,496
	227,938	191,230

The amounts due from related parties included in prepayments, deposits and other receivables are as follows:

	Unaudited 30 June 2017 ***RMB'000***	Audited 31 December 2016 *RMB'000*
Subsidiaries of the ultimate holding company	**3,677**	3,600
A substantial shareholder and its subsidiaries	**66,858**	70,296
	70,535	73,896

The above amounts are unsecured, non-interest-bearing and have no fixed terms of repayment.

10. CASH AND BANK BALANCES AND LONG-TERM BANK DEPOSITS AND PLEDGED DEPOSITS

	Note	Unaudited 30 June 2017 RMB'000	Audited 31 December 2016 RMB'000
Cash and cash equivalents		**433,864**	581,491
Pledged deposits with banks		**833,030**	803,123
Time deposits with maturity of more than 3 months		**1,488,326**	1,441,254
		2,755,220	2,825,868
Less: Pledged deposits with banks	*(a)*	**833,030**	803,123
Less: Long-term bank deposits		**—**	379,927
Cash and bank balances		**1,922,190**	1,642,818

Note:

(a) As at 30 June 2017, other than certain bank loans secured by time deposits amounting to RMB802,927,000 (31 December 2016: RMB798,905,000), a deposit of RMB30,103,000 was secured for documentary credit (31 December 2016: RMB4,218,000 was pledged for letters of credit).

11. TRADE PAYABLES

An aged analysis of the Group's trade payables, based on the invoice date, as at the reporting date is as follows:

	Unaudited 30 June 2017 RMB'000	Audited 31 December 2016 RMB'000
Within 3 months	**283,324**	222,504
3 to 6 months	**26,474**	12,356
More than 6 months	**27,681**	2,761
	337,479	237,621

11. TRADE PAYABLES (Continued)

The amounts due to related parties included in trade payables are as follows:

	Unaudited 30 June 2017	Audited 31 December 2016
	RMB'000	*RMB'000*
Subsidiaries of the ultimate holding company	**33,603**	2,997
The subsidiaries of a substantial shareholder of the ultimate holding company	**11,216**	9,758
A subsidiary of a substantial shareholder	**229**	—
	45,048	12,755

Trade payables, including amounts due to related parties, are non-interest-bearing and are normally settled within one month to three months.

12. DIVIDENDS

The directors do not recommend the payment of an interim dividend for the six months ended 30 June 2017 (for the six months ended 30 June 2016: Nil).

During the six months ended 30 June 2017, the Company didn't declare and pay dividend to the shareholders of the Company (six months ended 30 June 2016: the Company declared and paid a final dividend of approximately RMB0.75 cents per share as an appropriation of share premium for the year ended 31 December 2015 to the shareholders of the Company).

13. INTEREST-BEARING BANK LOANS

		Unaudited As at 30 June 2017			Audited As at 31 December 2016		
	Notes	**Effective interest rate (%)**	**Maturity**	**RMB'000**	Effective interest rate (%)	Maturity	RMB'000
Current							
Short-term bank loans:							
— Pledged loans	(a)	**LIBOR+0.9/ HIBOR+0.9/ EURIBOR*+0.9**	**2017**	**717,936**	LIBOR+0.9/ HIBOR+0.9	2017	743,091
— Guaranteed loans	(b)	**1.47**	**2017**	**200,000**	1.47 to 3.915	2017	300,000
— Pledged and guaranteed loans	(c)	**BKBM**+0.85**	**2017**	**97,825**	—	—	—
— Credit loans		**3.915**	**2017**	**100,000**	3.915	2017	100,000
				1,115,761			1,143,091

13. INTEREST-BEARING BANK LOANS (Continued)

	Unaudited 30 June 2017 *RMB'000*	Audited 31 December 2016 *RMB'000*
Bank loans denominated in		
— USD	**20,355**	673,767
— RMB	**300,000**	400,000
— HKD	**694,184**	69,324
— EUR	**14,682**	—
— NZD	**86,540**	—
	1,115,761	1,143,091

Notes:

(a) As at 30 June 2017, certain bank loans with an aggregate amount of approximately RMB717,936,000 (31 December 2016: RMB743,091,000) were secured by bank balances amounting to RMB802,927,000 (31 December 2016: RMB798,905,000).

(b) As at 30 June 2017, a bank loan amounting to RMB200,000,000 (31 December 2016: RMB200,000,000) was guaranteed by Yashili International Group Ltd. ("Yashili (Guangdong)"). As at 30 June 2017, no bank loan (31 December 2016: RMB100,000,000) was guaranteed by Shanxi Yashili Dairy Co., Ltd.

(c) As at 30 June 2017, a bank loan of RMB97,825,000 (31 December 2016: Nil) was guaranteed by Yashili (Guangdong) and was also secured over all the assets of Yashili New Zealand by a general security agreement. As at 30 June 2017, the carrying amount of the total assets of Yashili New Zealand amounted to RMB1,543,216,000.

* EURIBOR: The Euro Interbank Offered Rate (Euribor) is a daily reference rate, published by the European Money Markets Institute for Eurozone banks.

** BKBM: The New Zealand Bank Bill Benchmark Rate (BKBM) is a base rate in New Zealand.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Industry Review

During the first half of 2017, the global economy continued to improve. Developed economies recovered steadily, while among the emerging economies, China and India continued driving the economic growth. However, the world's economy still faced risks and uncertainties as its recovery was not balanced and there hadn't yet been a structural strong growth.

China's economy operated within an appropriate range with more visible good momentum, and was in good shape featuring steady growth, upbeat employment, stable price, rising income and structural improvement. The economic development has become more stable, sustainable and better coordinated. According to the preliminary statistics published by the National Bureau of Statistics of China, the gross domestic products for the first half of the year reached RMB38,149 billion, representing an increase of 6.9% from the previous year based on comparable prices. The annual national disposable income per capita was RMB12,932, representing a nominal growth of 8.8% from the same period of 2016 and a real growth of 7.3% after excluding price factors. The annual national consumption expenditure per capita amounted to RMB8,834, representing a nominal growth of 7.6% and a real growth of 6.1% after excluding price factors.

On 1 October 2016, The *Administrative Measures for the Registration of Recipes of Infant Formula Milk Powder Products* ("Recipe Registration Requirement") came into effect. Recipe Registration Requirement requires that every enterprise, in principle, shall not have more than three product series or nine product recipes, and when enterprises apply for recipe registration, product claims related to the product recipe in the product label and the instruction manual will also be reviewed, in order to ensure the authenticity, accuracy and scientificalness of the labels and instructions of infant formula milk powder and to prevent enterprises from over-advertising and misleading consumers via labels and instructions. 1 January 2018 is the deadline for registering the existing products and brands. Against this backdrop, mother-and-baby chain store systems were more prudent in brand selection with more attention paid to the overall strength of producers, such as brand, supply chain, management, support and service. With regards to population policy, the demographic dividend from the nationwide two-child policy was gradually reflected in the first half of 2017, which drove the infant formula industry and presented new development opportunities for relevant enterprises and markets.

The domestic infant formula market size during the first half of the year 2017 increased 7% as compared to the same period of 2016, with increased sales volumes and prices. The mother-and-baby store channel maintained stronger growth with increased sales volumes and price and was the largest market channel with 54% market share. The Internet continued to affect consumers' behavior and buying habits. The growth in the e-commerce channel had stopped, and the development of overseas online shopping, overseas intermediate purchase and cross-border e-commerce underwent inspection and standardization. Affected by the new policy of milk powder, some products were sold at low price online, which influenced consumer perception. The modern trade channel continued to shrink with price recovering, and domestic brands relying on this channel speed up the shift to the mother-and-baby store channel under huge competition pressure.

Business Review

In 2013, Mengniu Group entered into strategic cooperation with the Group by way of a general offer, thereby becoming the Group's controlling shareholder. In 2014, the Group, China Mengniu International Company Limited ("Mengniu International") and Danone Asia Baby Nutrition Pte. Ltd. ("Danone Asia") entered into a share subscription agreement. As the deal closed in February 2015, Danone Asia officially became the Group's second largest shareholder. In December 2015, the Group completed the acquisition of the entire equity interest in Oushi Mengniu, a member of Mengniu Group, and officially became the sole milk powder business platform under Mengniu Group. In May 2016, the Group completed the acquisition of the entire equity interest in Dumex China, a member of Danone Group, and initially completed its brand consolidation and domestic capacity expansion.

The Group is committed to developing reliable nutrition products for consumers, including the branded product series for promoting healthy growth of infants and toddlers such as Yashili, Reeborne, Dumex, Arla and Scient, as well as those designed to meet the nutritional needs of adults such as Youyi, Huanqing and Zhengwei. The Group's business model incorporates such key factors as premium imported dairy raw materials, premium imported original infant formula milk powder products, self-developed recipes, advanced manufacturing system and professional marketing teams with sufficient knowledge on local consumer markets, which enables us to offer trustworthy products to consumers.

Introduction of Product Categories

Infant formula products

The infant milk formula products developed by the Group are mainly aimed at satisfying the health and nutritional needs of infants and toddlers during daily feeding, and can serve as a major source of nutrition for infants and toddlers supplementary to breast milk. All of the Group's branded infant milk formula products are produced using premium imported raw materials. The Group is striving to develop infant formula with the most ideal nutrition composition to well cater to the needs of infants and toddlers during different stages of growth and development.

The Group has established different infant milk formula product lines targeting customers at different consumption levels. The originally canned and packaged imported organic "Baby & Me" introduced by the Group through partnership with Arla Foods is originated from Denmark and targets the ultra-high-end market. The upgraded "Diamor" and "Precinutri" of Dumex are mainly aimed at creating integrated solutions for babies. Mengniu's "Reeborne" as a strategic brand of the Group mainly targets the high-end customers, under which organic series products are launched as key ones. The Group is committed to establishing "Reeborne" as a leading and professional brand in organic products market. Mengniu's "Platinum Jiazhi" mainly focuses on mid-end consumers which provides infants with comprehensive nutrition. Products under "Meileizi" and "Meimengyi" also mainly focus on mid-end consumer groups to achieve finer market segment in the mother-and-baby store channel. Yashily's "Super α-Golden", originally canned and imported from New Zealand, targets mid- to high-end customer groups, and gathers global resources. Its vigor system enhances the growth of babies' own probiotic group, releasing internal intestinal vitality. Yashily's "α-Golden", originally canned and imported from New Zealand, targets mid-end customer groups. Products of this series contain the 1+1 nutrition mix to supply key nutrition for physique and intelligence growth. Yashily's "Super Golden" targets mid-end customers. Infant formula milk powder of this series is elaborately developed by the Yashili R&D team based on the growth characteristics and nutritional needs of infants and toddlers so as to provide them with necessary and balanced nutrition for healthy growth. Yashily's "Golden" targets low- to mid-end customers, focusing on nutrition provision to facilitate the healthy growth of infants. Yashily's "New Formula" facilitates intellectual development and stimulates immune cells, mainly targeting low- to mid-end customers.

Tailored infant formula products

The accelerating modernization and industrialization process, and the changing environment, lifestyles and diets in China pose increasing health challenges to Chinese infants and toddlers. As an infant nutrition expert, the Group not only endeavors to satisfy the nutritional needs of infants and toddlers, but also has professional formula products under Dumex to meet the special nutritional needs of special infants and toddlers. At present, the Group has three series of professional formula products under Dumex:

— Products for Allergy: this category includes products for prevention of allergy (HA) and treatment of allergy (PEPTI). HA products can effectively guard infants and toddlers exposing to high risk of allergy against such risk through semi-hydrolyzing techniques. PEPTI products serve as an effective remedy to the allergy to protein in food of infants and toddlers through deeply hydrolyzing techniques.

— Products for Digestion: this category includes lactose-free formula products (LF) which would effectively avoid the vicious circle of diarrhoea due to hypolactasia.

— Products for Under-weight Newborn: this category includes formula for low-birth-weight newborn babies (LBW) which would cater to their needs for catching up with standards of growth.

Nutrition food

The Group also produces and sells various types of nutrition food, including: nutritional milk powder for adult family members — adult milk powder under the "Mengniu" brand and adult milk powder under the "Youyi" brand; high-end functional milk powder for mid- and old-age people — milk powder for the middle-aged and elderly people under the "Huanqing" brand; nutritional milk powder for children — "Future Star" milk powder; healthy and delicious dissolvable products — cereal under the "Zhengwei" brand; and infant complementary food — nutritional rice cereal for infants and toddlers under the "Yashily" brand. Such a portfolio comprises products with differentiated nutritional mixes designed for consumers with special needs as well as those suitable for general consumers.

"Mengniu"-branded adult milk powder targets customers demanding daily nutritional supplements, such as the middle-aged and elderly people, students and women. Leveraging on 100% premium milk source, technologies from Northern Europe, scientific formula and under stringent supervision and control, the products provide consumers in China with milk power of international quality.

"Youyi"-branded adult milk powder, with a track record of 17 years, focuses on consumers including the middle-aged and elderly people, students and women. It contains calcium, vitamin A/D/E, dietary fiber and other beneficial elements. Produced in compliance with international standards, products of this series are reliable.

"Huanqing"-branded milk powder for the middle-aged and elderly people addressing their needs for strong bones and cardiovascular system. Products of this series are developed with recipes beneficial to bones, including colostrum basic protein, vitamin D and rich calcium, and to cardiovascular system, including phytosterol esters, linoleic acid (ω -3), linolenic acid (ω -6). The products use 100% imported milk sources. They are sugar-free and added with inulin. The healthy and fat-free milk powder agrees with the constitution of the middle-aged and elderly people.

"Future Star" milk powder for children growth contains 58 dietary mixes, including 28 fruit-vegetable powders, probiotics + prebiotics and DHA. The products are applicable to babies who are slow or picky eater, or eat little.

"Zhengwei"-branded cereal is positioned to provide consumers with premium nutrition mix. Being of natural and pure flavor, the cereal products supplement daily dietary fiber and are suitable for the whole family members for daily drinking.

"Yashily"-branded nutritious milk rice cereal for infants and toddlers are developed for Chinese babies based on their characteristics of growth and development. Products of this series mainly use rice of premium quality as raw materials, and are processed with high-speed production line, sealed equipment and fine packaging process so as to ensure stable quality and safety.

Brand Strategies

The first half of 2017 was crucial for the brands of the Group. Each department has made steady progress in implementing the differentiated business models and branding portfolios established between late 2016 and early 2017 as follows: "Yashily" brand focuses on basic nutrition; "Reeborne" under the Mengniu brand is committed to differentiated competition, mainly for the organic market; "Dumex" is positioned to build up a professional image and dedicated to discovering pediatric solutions; Arla as a strategic brand of shareholders will highlight its privilege of serving royal families. Among them, "Baby & Me" covers the ultra-high-end market; "Dumex" and "Reeborne" under Mengniu brand cover the mid- to high-end market, and "Yashily" covers the mid-end market. Products of each series enjoy competitive advantages as compared with that of other series in terms of price range. On regional strategies, "Baby & Me" and "Dumex" focus on first- and second-tier cities, while penetrating into the eastern region; "Yashily" and "Reeborne" under Mengniu brand focus on third- and fourth-tier cities, while penetrating into the central region. With such coordination, the Group has established a tight brand matrix with its products covering the whole market network, which lays a solid foundation for coping with the fierce competition in infant formula market which will offer high-end and branded products in the future.

The consumption habits of consumers indicated an evident consumption upgrading. According to the data from a third party, the volume of the ultra-high-end market (RMB430 per kilogram) recorded a significant growth as compared to that of the same period of 2016. Price is no longer the only factor to be considered by consumers born after 1985 to 1990. They are inclined to buy more specialized products with better quality, and that is also the case in third- and fourth-tier cities. Hence, the high-end market of milk powder has experienced significant growth in recent years as consumers are willing to pay more money for products with specialized formula and of reliable quality from country of origin. Therefore, it is the best time for the Group to develop the high-end market.

In addition, change in media form of external communication is underway. When purchasing and collecting products, many consumers choose to search the internet and check comments from the users in addition to considering recommendations made by friends, while traditional media have an increasingly insignificant influence on consumers. Therefore, the Group mainly applied media budget to digital marketing as a way to attract purchasers. The Group hopes to have its roots in domestic market and thoroughly examine consumer insights. It aims to influence consumers by producing such contents as may strike a responsive chord in the hearts of target groups. Based on such contents, the Group explores ways of targeted marketing, seeking to reach consumers effectively. Membership promotion and community marketing are also highly valued to allow consumers to become spokesmen, thus spontaneously spreading positive comments.

Product R&D

In 2017, as infant formula producers are gearing up for the Recipe Registration Requirement, the Group is no exception. During the year, the key task of the Group's R&D management center is to smooth the recipe registration of infant products, submit the scientific development processes of safe and nutritional infant formula to the China Food and Drug Administration ("CFDA") and actively coordinate with experts for the review process. Thanks to the active cooperation of the Group's relevant departments, several factories under the Group have submitted filing applications for the recipe registration of series products, and these applications were accepted by CFDA. In August, the Group was listed among the first batch of enterprises granted recipe registration by CFDA. A total of 7 series and 21 recipes of the Group were approved for registration and record, which indicated the Group had the most approved recipes on the list.

On product packaging, the R&D team of the Group is actively improving the lid design for existing canned products, making them more novel and practical, and prepares to apply for patent protection in this regard.

For adult products, the Group's R&D team developed the organic modified milk powder for pregnant and lying-in women. Currently, it comes to the final preparation stage to launch the products.

In 2017, the Group's R&D center puts a lot of efforts in basic nutrition research. It has applied jointly with the National Institute for Nutrition and Health of the Chinese Center for Disease Control and Prevention for a national 13th Five-Year Plan project titled "Development of Special Dairy Products based on China's Breastmilk Components and Research on Key Generic Technology (基於我國母乳組分的特需乳製品創製及共性關鍵技術研究)". Oushi Mengniu under the Group, acting as the leading unit, undertakes the research assignment in respect of Task Five of the project, titled A New Generation of Infant Dairy Products and Development of Dairy Based Foodstuffs for Special Medical Purpose (《新一代嬰幼兒乳製品和乳基特殊醫學用途食品的創製》).

Sales Channels

During the first half of 2017, the Group rapidly increased the contribution of the mother-and-baby store channel and developed the e-commerce business by further advancing channel transformation and innovation activities. According to statistical analysis (not financial data) by the channel management department of the Group based on membership loyalty systems and actual sales from point of sales machines at stores, the mother-and-baby store channel accounted for 76% of terminal sales of infant formula in June 2017, modern trade 20% and e-commerce 4% (Beginning of 2017: mother-and-baby store channel 64%, modern trade 35% and e-commerce 1%). To this end, the original marketing organizational structure consisting of brand divisions was restructured into a system comprising CBUs set up by channel and product category, where the "maternity CBU" is in charge of the strategic objective of brand upgrading and channel transformation; the "modern trade CBU" strives to tackle the problem of "channel, product category and price declines"; the "high-end maternity CBU" is positioned to restore Dumex's position as one of the top four foreign brands again and help Arla stand out among a long list of brands; the "innovation CBU" is to expand community marketing, integrate internal market resources and develop TP business in a bid to capture new consumers based on the existing e-commerce network; and the Scient Project Department was established for new business development jointly by the brand business, distributors and sales teams.

The "maternity CBU" established by the Group unleashed its team potential and accelerated the exploration of mother-and-baby chain stores through a partnership and push money based incentive mechanism. During the first half of the year, the contribution of the mother-and-baby store channel recorded a significant double-digit growth on year-on-year basis, with its results up by over 50% year-on-year. The "high-end maternity CBU" strictly controlled costs in the supermarket channel (inefficient and ineffective shopping guide and contract expenses, etc.) and strengthened mother-and-baby chain stores expansion as a way to stabilize sales volume. The "modern trade CBU" completed partial transformation by advancing direct supply to mother-and-baby-stores, and fruitful results were achieved in reducing losses by KAs. As for e-commerce sales of "innovation CBU". Online business layout has been fully developed, thus laying a solid foundation for the development of the second half of the year. On innovation activities, the Group rationalized the business model of joyful-shopping developed for employees, which recorded profit as a separate account. All of the three brand-new business activities consisting of new media, communities and TP operation were launched and reached the scheduled goal, making a good start to the development of new competence in the Internet field.

In terms of internal marketing management, the Group has established the marketing support department with great attention paid to channel management, inspection and anti-cross management and membership system. The Group rationalized marketing mechanisms and procedures and the matrix of powers and responsibilities, and set up a strong inspection system to inspect and review market costs in an effort to improve cost efficiency. It cracked down on goods fleeing and price undercutting to maintain market order. The Group participated in solving and optimizing SAP related problems and built up a membership management system connecting with Outworker Assistant (外勤助手) to achieve information-based management on all procedures, from purchase, production, warehousing, delivery, entry into store, sales to interaction with consumers. This system is able to achieve such integrated functions as comprehensive budget management, targeted use of expenses, efficient business operation, purchase-sales-inventory management, anti-cross management and instant interaction with consumers. Moreover, the membership management system also achieves order processing and settlement functions for directly-managed mother-and-baby stores. Market BP was established to support each CBU to perform brand promotion and sales campaign. Thanks to the above efforts, a well-established and efficient marketing management system has come into being.

Quality Control

Quality is the lifeblood of an enterprise and the only way for an enterprise to capture the market. The Group is continuously dedicated to building up a comprehensive quality management system covering the entire value chain from supplier quality management to consumer services.

The Group selects and manages suppliers with stringent standards from the beginning of the supply chain. During the first half of 2017, the review process for all suppliers was unified and the Group reviewed and examined suppliers regularly to ensure the audit of suppliers is complete and comprehensive. Moreover, in accordance with the national standards newly issued in respect of raw materials and packaging materials as well as new risk control requirements, the Group has updated the standards of raw and auxiliary materials and carried out strict incoming inspection as a way to ensure the high quality and standards of materials purchased.

During the first half of the year, the Group established a new quality center in a bid to optimize resources of the Group and offer guidance on achieving quality excellence at all levels.

On laboratory test, laboratories in all factories purchased advanced test and analysis equipment based on test requirements, including inductively coupled plasma mass spectrometer, ultra-performance liquid chromatography-tandem mass spectrometer, gas chromatograph-mass spectrometer, high performance liquid chromatograph, atomic absorption spectrometer and gas chromatograph. During the first half of the year, the Horinger factory completed relevant resource allocation and conducted full analysis for finished products. All analysis and test results of the products of the Group's factories were in compliance with relevant national standards. In the strict national sampling campaign conducted in the first half of the year, the pass rate of products under "Yashily", "Mengniu", "Dumex" and "Scient" was 100%, which further boosted consumers' confidence for the products of the Group.

The Group's factories constantly upgraded and transferred their infrastructure so as to ensure compliance with requirements specified by the production license for infant formula milk powder. This included separation of drying and concentration zones, upgrading the entrance of air-conditioned changing rooms of the dryer, adding air shower facilities for ton bags and packaging materials, and building a stripping room and an unloading awning in the raw material warehouse in the Horinger factory; upgrade of stick pack production workshop in the Shanxi factory; and upgrade of changing rooms in the Shanghai factory. The upgrading tasks have been basically completed. In order to improve the quality traceability system, the Group has carried out the upgrade and transformation of equipment for the GBT product quality traceability project, starting with the Chaozhou factory during the first half of the year.

The Group's factories passed the supervisory accreditation or re-assessment of such management systems as ISO9001, HACCP, FSSC22000, Integrity and CNAS in accordance with the requirements of audit plans, and accomplished such tasks as are required to obtain the production license as a way to ensure a sound operation of the quality system and lay a solid foundation for producing quality products.

The Group's quality center has developed its product risk control plan in response to the national risk control plan and hot issues in the market. This plan involves testing 32 batches of products including infant formula milk powder, modified milk powder and milk rice cereal. Results indicated a satisfactory condition.

The Group's factories have prepared and submitted relevant quality files in accordance with the requirements of recipe registration for infant formula to ensure the recipe registration goes smoothly.

In terms of application system, the Shanghai factory successfully switched to the Mengniu LIMS system, and the Group's factories started using the Mengniu SAP system to ensure a sound operation of quality related work as well as the effectiveness of product traceability through quality modules of such systems.

Resource Integration

During the first half of 2017, the supply chain management center was further integrated and reorganized based on the Group's overall deployment and future business needs.

As for strategies, the Group divested itself of the Longjiang factory and the Guangzhou factory as a way to make good use of fixed assets and improve utilisation rate; focused on main business, i.e. infant formula milk powder, and outsourced non-core businesses to specialized companies for supply; and improved efficiency and cut labor cost through delayering of organization structure.

As for planning, a specialized planning management department was established independent of the original planning and logistics department to strengthen central S&OP coordination, develop the demand forecasting model and increase the order fulfillment rate.

As for procurement, the Group has improved the procurement bidding system and procedure based on business functions, thus realizing significant savings. As to raw material procurement, the Group drew on Mengniu's strength in centralized procurement of bulk materials and monitored market opportunities to lock purchase prices or stock up, thus avoiding the impact of price fluctuations on the costs. As to procurement of key materials, the Group screened the suppliers and selected strategic suppliers, and carried out direct procurement from manufacturers to establish long-term relations with suppliers. As to procurement of packaging materials, the Group will conduct benchmarking within the Group for the major packaging materials and concentrate the demands for materials with uniform specifications to organize procurement bidding, so as to reduce costs and improve efficiency. As to market procurement, the Group screened and slashed suppliers considering their prices, services and quality, in order to motivate suppliers, cut costs, improve service and reduce daily management costs by leveraging on economy of the scale of centralized procurement. As to fixed asset procurement and comprehensive procurement, the Group set up and promoted the working procedures for comprehensive procurement and provided professional supplier sourcing, bidding, price bargaining and contract services for various departments with purchasing needs. The Group conducted benchmarking by reducing the items to be purchased, screened and reduced suppliers, and optimized and shared the supplier resources within the Group to reduce purchasing and operating costs.

As for manufacturing, the Group has established an engineering committee and a safety committee consisting of specialized staff from all the factories. The engineering committee focuses on budget control and feasibility of construction projects as well as in-depth communication in respect of technical proposals so as to achieve connectivity among resources, information and technologies and further improve the management of capital expenditure projects. The safety committee identifies risk sources and formulates specific solutions leveraging on guiding tools for safety assessment; shares various tools, concepts and methods with respect to daily safety management. Each factory reviews and shares cases on a regular basis so as to carry out safety related work in a deeper and more professional way, enhance the safety awareness of factory personnel, identify and eliminate the potential safety hazards. Thanks to these efforts, no major safety accident occurred in the first half of the year.

As for logistics, the Group selected appropriate re-distribution centers based on the sales concentration areas to improve the overall distribution efficiency and reduce transportation costs. The logistics service model and the existing carrier network were optimized to improve the capacity and efficiency of their support for business, thus simultaneously reducing sales logistics cost and production logistics cost.

Financial Review

Revenue

For the six months ended 30 June 2017, the revenue of the Group amounted to RMB966.7 million (same period of 2016: RMB1,146.5million), representing a decrease of 15.7% from the same period of 2016.

Revenue by product category

	For the six months ended 30 June		
	2017	2016	Percentage
	RMB million	*RMB million*	change
By product category			
Infant formula products	**673.9**	825.2	(18.3%)
Nutrition food products	**246.6**	312.2	(21.0%)
Others	**46.2**	9.1	407.7%
Total	**966.7**	1,146.5	(15.7%)

For the six months ended 30 June 2017, revenue realized by infant formula products amounted to RMB673.9 million (same period of 2016: RMB825.2 million), representing a decrease of 18.3% from same period of 2016 while the sales proportion of high-end infant formula products (include Reeborne and Arla Organic) is growing from 9.4% for the first half of 2016, 13.3% for the second half of 2016 to 22.5% for first half of 2017, and revenue realized by nutrition food products amounted to RMB246.6 million (same period of 2016: RMB312.2 million), representing a decrease of 21.0% from same period of 2016, and revenue realized by other products amounted to RMB46.2 million (same period of 2016: RMB9.1 million), representing an increase of 407.7% from same period of 2016, which was mainly derived from the base powder sold by the subsidiary, Yashili New Zealand to members of the Danone Group.

The decrease in the Group's revenue was mainly due to: (1) the accelerated shrinking of the modern and traditional channels compromised the Group's existing competitive advantages in these channels and the Group withdrew from some inefficient stores of such modern and traditional channels; (2) during the first half of 2017, the Group continued to deal with the sales model transformation of the mother-and-baby store channel and the e-commerce channel whereby the implementation and effect of the new marketing strategies require time and cost input; (3) the Group increased its promotion efforts during the first half of 2017 to cope with the intensified market competition; and (4) the Group was proactively consolidating its product lines in response to the impact brought by the Recipe Registration Requirement, and such consolidation may affect the sales of some products to a certain extent.

During the first half of the year, the Group introduced an experienced marketing management team which accelerated the integration process and adopted proactive initiatives, including reinforcement of internal marketing management, optimization of sales model, channels transformation and continuous focus on targeted products. At the same time, the Group also achieved progress in the integration of back office management and supply chain of the Group. It is anticipated that the effectiveness and benefits of such integration will be gradually realized during the second half of the year.

Gross profit

For the six months ended 30 June 2017, the Group recorded a gross profit of RMB447.6 million (same period of 2016: RMB580.5 million), representing a decrease of 22.9% from the same period of 2016. The gross profit margin was 46.3%, representing a decrease of 4.33% from the same period of 2016, which was due to more gift products offered during the period.

Selling and distribution expenses

For the six months ended 30 June 2017, the Group generated selling and distribution expenses of RMB490.7 million (same period of 2016: RMB493.4 million), representing a decrease of 0.5% from the same period of 2016; In terms of the percentage of revenue, selling and distribution expense was 50.8% (same period of 2016: 43.0%) for the first half of 2017, representing an increase of 7.8% from the same period of 2016. The increase was mainly because some fixed expense such as labor cost and marketing cost did not decrease while revenue dropping down.

Administrative expenses

For the six months ended 30 June 2017, administrative expenses amounted to RMB114.0 million (same period of 2016: RMB159.9 million), representing a decrease of 28.7% from the same period of 2016, mainly attributable to the decrease in the downtime losses in the first half of 2017 of RMB34.0 million as compared to the same period of 2016.

Net finance income

For the six months ended 30 June 2017, net finance income amounted to RMB54.5 million (same period of 2016: RMB70.8 million). The decrease in net finance income of 23.0% was mainly attributable to acquisition of Dumex China (completed in May 2016) which led to the decrease of working capital available for investment.

Income tax credit

For the six months ended 30 June 2017, the income tax credit of the Group amounted to RMB37.7 million (same period of 2016: RMB27.7 million), and the effective income tax rate was –23.6% (same period of 2016: –218.1%). The increase in income tax credit was mainly because the income tax expense arising from a profit-making subsidiary same period of 2016 affected the deferred income tax expense.

Inventory

As at 30 June 2017, the balance of inventory of the Group amounted to RMB678.6 million (31 December 2016: RMB619.9 million), and the increase in inventory was mainly attributable to an increase in work in progress stocked up in preparation for sales in the second half of the year.

Other financial assets

As at 30 June 2017, other financial assets included wealth management products of RMB50.8 million, which were principal guaranteed and with an anticipated annualized yield of 3.1% (31 December 2016: 3.1%), and wealth management products of RMB362.9 million, which were of floating proceeds and with anticipated annualized yields of 3.55% to 4.65% (31 December 2016: 3.50% to 4.00%).

Trade and bills receivables

As at 30 June 2017, the Group's trade and bills receivables amounted to RMB162.0 million (31 December 2016: RMB161.4 million). During the first half of 2017, the trade receivables turnover days were 30 days (same period of 2016: 25 days), representing an increase of 5 days as compared to the same period of 2016, mainly attributable to the consolidation of Dumex China since June 2016, which had a longer turnover days.

Human resources and employees' remuneration

As at 30 June 2017, the Group had a total of 2,634 full-time employees (30 June 2016: 4,362). The total staff cost for the first half of 2017 was approximately RMB272.0 million (same period of 2016: RMB209.7 million). The increase in total staff cost was mainly because only one month's salary cost of Dumex China was included during the same period of 2016 as Dumex China was consolidated since June 2016. In addition, the increase of termination benefits also cause the increase in staff cost.

Contingent liabilities

As at 30 June 2017, the Group had no material contingent liabilities (31 December 2016: Nil).

Capital commitment

As at 30 June 2017, the Group's capital commitment was RMB24.2 million (31 December 2016: RMB36.3 million) which is mainly related to the rectification project for the Recipe Registration Requirement and purchase of milk powder production equipment.

Use of net proceeds from Initial Public Offering

The Company's net proceeds from Initial Public Offering amounted to approximately RMB1,965.8 million after deduction of relevant expenses. The Company had applied these net proceeds as disclosed in the section "Future Plans and Use of Proceeds" in the prospectus dated 30 October 2010. Therefore, the use of net proceeds as of 30 June 2017 is set out as below:

Items	**Available at the end of 2016**	**Applied during the six months ended 30 June 2017**	**Pending for application during the six months ended 30 June 2017**
	RMB'000	*RMB'000*	*RMB'000*
Expansion of production capacity for infant formula and nutrition food products	150,271	27,456	122,815
Acquisition of integrated dairy companies engaged in the production of raw milk and raw milk powder and establishment of vertically-integrated production facilities overseas	—	—	—
Promotional activities in television networks and websites of popular baby nursing forums as well as major magazines, newspapers and other printing media	—	—	—
Enhancement on the Group's research and development capabilities	14,356	7,660	6,696
Total	164,627	35,116	129,511

HUMAN RESOURCES

During the first half of 2017, the human resources management center of the Group closely centered on the strategic plan and the must-win battles for 2017 to carry out work in the following aspects as a way to reorganize its resources, regenerate to shine and seize opportunities in industrial competition:

I. For organizational transformation, as the Group implemented the marketing structure consisting of four CBUs and rationalized the supply chain, it actively drove to complete the integration of middle and back office, effectively rationalize resources for optimal allocation, integrate the original Yashili with Oushi Mengniu and Dumex in an effective way. That is how the Group realized the entire chain integration from the supply chain to marketing, human resources, finance, legal affairs and audit, established such a structure as was applicable to milk powder business segment and accomplished talents allotment under the new circumstances so as to ensure its positive operation.

II. For improving the incentive mechanism, position ranking, remuneration and welfare and performance were consolidated, laying a sound foundation for centralized management. The Group adjusted the salary for high-performance employees and carried out retention plan for high-potential employees as a way to motivate them. Multi-level incentive schemes were designed covering all employees, among which the distinctive sales incentive policy effectively inspired employees and boosted business development. Welfare projects were optimized and improved for full coverage and care delivery so as to enhance their own well-being.

III. For talent pool construction, a series of talent and organizational development projects were carried out, such as identifying high-potential personnel through organization and talent filtration in a bid to improve the development and training plan for high-potential personnel, thus supporting future business development with talent reserves. Moreover, the Group increased the investment in training resources in an effort to develop high-potential personnel, enhance the capability of the marketing team and train new staff. Various activities were carried out, such as new staff training camp, marketing training and internal marketing trainer cultivation so as to build learning organizations and enhance professional skills of marketing personnel.

IV. Streamline organization. The Group rationalized and optimized procedures, issued the first-level and second-level matrix of powers and responsibilities for the entire group and each center, and sped up decentralization to improve the efficiency of business decision-making.

V. For cultural construction, the Group held strategy consensus meetings to strengthen the promotion of strategies and improve the consensus on strategies, so as to unite all personnel for cohesion. The cultural construction focused on two important values, i.e. "passion" and "openness". The Group organized distinctive staff activities on an annual and quarterly basis to better promote its corporate culture's core values, and continuously maintained communication and exchanges with employees to strengthen the cultural characteristics of the Group, in an effort to improve cohesion with culture and build a passionate team of officers and executives. Meanwhile, the Group set up, improved and implemented culture-related rules, and developed uniform culture and awareness, so as to foster corporate culture featuring passion, teamwork and responsibility.

SOCIAL RESPONSIBILITY

In 2017, the Group made persistent efforts in social welfare activities and extensively spread love.

In March, the Group donated milk powder valued approximately RMB419,000 to the Overseas Chinese Charity Foundation of China, and these products were delivered to poor people in need of love and care across the country in a bid to help children living in poverty; the Group donated milk powder valued approximately RMB56,000 to the Guangdong Branch of Red Cross Society of China. Through the Guangdong Branch of Red Cross Society of China and the Red Cross of Heyuan City, these products were distributed to children from the impoverished families in Heyuan. Most children involved in this activity were left in their grandparents' or other relatives' care, while their parents worked away in the cities. While bringing food to these children, this activity was also expected to spread warmth and social care.

In April, a blind mother insisted on giving up treatment to save her unborn fetus which made her family face a dilemma. After a short pleasant for having a new baby, the poverty-stricken family faced another predicament that the mother receiving chemotherapy could not feed breast milk to the baby, but the family could not even afford milk powder. Upon receipt of such information, the Company donated milk powder to the blind mother through the Red Cross in an effort to help the family living in distressed circumstances.

In July, the Group donated milk powder to the poverty-stricken families living in such mountainous areas as Chongqing, Hongya County in Meishan City of Sichuan, Luding County in Garze Tibetan Autonomous Prefecture of Sichuan, Ma'erkang County in Ngawa Tibetan and Qiang Autonomous Prefecture of Sichuan and Xuzhou City of Jiangsu, hoping that these children will enhance their physical quality in the future to have a stronger physique, be energetic and grow up healthily and happily.

PUBLIC RELATIONS AND CRISIS MANAGEMENT

The Group maintains active and effective publicity means and communicates relevant information to external parties in an open and transparent manner. The Group also maintains good communication with all publicity departments and institutions, publishes the Company's latest information on a timely basis, and takes an active part in various social welfare and charitable activities.

The Group has developed a complete set of internal crisis management systems and response mechanisms, and addresses complaints from consumers and issues of the media's concern via its crisis management center in a timely and accurate manner. Meanwhile, the Group is highly concerned with potential problems reflected by the market, and provides good services for consumers in advance to prevent the occurrence of crisis. The Group has established a news center to pay close attention to the trends and news of the industry and monitor public opinions, in order to make timely response to any incidents in the industry. The Group eliminates negative impacts and maintains a good reputation in the industry through effective communication and disclosure of information to the public and the media.

INVESTOR RELATIONS

The Group believes that effective communication with shareholders, investors and prospective investors is essential for enhancing investor relations and enabling investors to understand the business performance and strategies of the Group. The Group conducts communication and exchanges with investors through various channels and means such as on-site receptions, telephone conferences, non-deal roadshows and investment summits of securities companies.

To facilitate effective communication, the Group has set up a website (www.yashili.hk) to post the latest information on its financial information, corporate governance practices and other data available for public inspection.

FUTURE PROSPECT

Policy Implications

Recipe Registration Requirement officially came into force on 1 October 2016, which will have profound impacts on the industry. After 1 January 2018, only infant milk powder brands at home and abroad that have obtained the registration certificate are allowed to carry out domestic production, sales and imports activities. The number of infant milk powder brands will decrease from 2,000 to 500, over 70% of which are estimated to be eliminated. Less known, inferior and small brands are likely to be phased out, making some market space of third-tier and below cities available.

The effect of the nationwide two-child policy are becoming more visible, the period from 2017 to 2019 may be a domestic baby boom. According to the data from the National Bureau of Statistics of China, the number of newborns during 2016 increased by 17.86 million, representing a high growth of 7.6%. The National Health and Family Planning Commission estimates that the number of newborns will range from 17.5 million to 21 million each year during the 13th Five-Year Plan period. From a macro perspective, the number of newborns in 2017 is estimated to be approximately 20 million, with a growth rate of around 10% during the period from 2017 to 2019.

As the nationwide two-child policy plays its role over time, the third- and fourth-tier cities and townships with relatively low life stress are likely to create a baby boom and boost local milk powder demands, which will then shore up the sales of domestic milk powder brands with competitive strength in the modern trade channel in these areas.

Industry Trend

In the second half of 2017, China's infant formula market will continue to recover and take on an increasingly consolidated trend, featuring quick reshuffle of domestic brands, integration of online and offline channels, and a growing fleet of high-end products and normalized prices. The entire infant formula industry would be in a critical period for reform and transformation.

With the implementation of Recipe Registration Requirement going further, those brands failing in recipe registration have gone for clearance sale in the first half of the year. Distributors will choose brands for partnership more prudently. Those brands that have national or even global presence, sound brand strategy planning and channel strategy planning will be advantaged.

International brands are extending business channels to wider areas while enhancing the advantages of their strong brands. Domestic brands are drawing on their well-established channels, coupled with brand promotion that well serves the national conditions, to gradually enhance their brand images and consumer loyalty. Brands mainly leveraging on the mother-and-baby store channel are becoming the most competitive ones by virtue of their innovative partnership models. The e-commerce channel is still dominated by international brands, but such brands and channels are undermined by market disorder due to the lack of online and offline price control. Domestic brands are exploring the online and offline combination model for consumer experience and brand promotion.

The high-level price of international raw milk powder will lead to general price increase by enterprises. However, the hiking channel costs and brand promotion costs will continue squeezing profit margin of enterprises. With the need for brand upgrading and differentiated competition being further highlighted, high-end functional products, organic infant formula and especially infant formula containing pure goat milk protein will become new favorites of the market because of their technical barriers and resource scarcity.

The entire industry is in urgent need of making good use of existing resources by virtue of innovative models in a bid to provide a role model for manufacturer supply and create a healthier market atmosphere.

Company Strategies

Brand strategies

In the second half of 2017, the Group will follow the brand strategies established in the first half of the year: "Yashily" will focus on basic nutrition; "Reeborne" under the Mengniu brand is committed to differentiated competition, mainly the organic market; "Dumex" is positioned to build up a professional image and dedicated to discovering pediatric solutions; Arla as a strategic brand of shareholders will highlight its privilege of serving royal families to provide comprehensive nutritional solutions for Chinese babies.

As there has been an obviously growing trend towards consumption upgrading, the Group will speed up efforts to introduce Mengniu's "Reeborne" and Arla "Baby & Me" to target consumer groups. For example, since mid-2017, Mengniu's "Reeborne" has launched large-scale roadshows covering third- and fourth-tier cities and combining trial of products and sales promotion, to rapidly enhance brand recognition and trial rates in short term, thus driving sales volume. Arla will further increase its penetration in first-tier cities by devoting greater effort to display and promotion. It is expected that the sales growth for the second half of the year will be faster than that of the first half. Upon elimination of some less-productive stores in the modern trade channel in the first half of the year, resources of "Yashily" and "Dumex" will be allocated more precisely, thus enhancing the output efficiency. With overall adjustment and more investment being made, the Group's sales target for the second half of the year will be more aggressive.

The Group's overall media communication strategy for 2017 is based upon the model of "Reeborne" to conduct online brand communication and offline brand promotion to approach mothers and ensure targeted spending of brand costs, so as to generate cost effectiveness and achieve the dual goals of brand growth and corporate profits. Meanwhile, the Group will leverage on Danone, Arla and Yashili New Zealand to further strengthen its international brand image. The Group will continue to carry out the research program on nutritional composition of breast milk from eight major domestic cities, in an attempt to showcase its ongoing effort in Chinese breast milk study via such public welfare activity, and to convey its sense of social responsibility and care for consumers, so as to enhance its brand reputation in an all-round manner.

Product R&D

In the second half of 2017, the Group's R&D center will actively promote the development of other new series of infant formula products and prepare the materials required in accordance with the Recipe Registration Requirement, with focus on goat milk-based infant formula. Goat milk powder, as an emerging milk powder, becomes increasingly popular in the market, making China a large consumer market. Besides, enterprises involved in goat milk powder have been thriving in recent years. As the market keeps growing, numbers of dairy enterprises target goat milk powder. The official implementation of the Recipe Registration Requirement will also speed up the reshuffle of domestic goat milk powder market and offer development opportunities for new brands and well-established brands. The Group will seize such opportunities to develop goat milk infant formula products and enter the goat milk infant formula market, so as to expand its product lines, create new opportunities for profit growth and provide consumers with a greater variety of products and more choices.

The R&D center will continue to uphold the product innovation concept, expand the Group's product lines, and select foreign premium organic raw materials to develop not only domestic organic products but also organic products originally packaged and imported from other countries. The product category involves infant complementary food and children products.

Sales channels

In the second half of 2017, in response to the industry changes brought by the new policy on milk powder, the Group will leverage on its strength in the global supply chain and multi-brand network established in the first half of the year, coupled with the successful CBUs business structure, to firmly promote channel transformation.

The "maternity CBU" assumes the strategic objective of brand upgrading and channel transformation. "Reeborne", as a strategic brand, will target medium and large mother-and-baby chain stores and high-end market, while tactical brands will strive for fast and sustained growth and continue leveraging on their strengths of being fast and flexible to seize small and medium mother-and-baby chain stores and individual weighted stores. While expanding channels, the Group will pay greater attention to enhancing the quality, average sales per point of sale and new consumer accumulation of these stores.

The "modern trade CBU" will completely withdraw from chain stores with negative contribution margin. For KAs with profit contribution, the Group will boost sales volume with special offer for hot selling products and special shelves in the second half of the year when consumers stock up for the Mid-Autumn Festival, the National Day and the Spring Festival. The Group will vigorously expand to small chain stores and single mother-and-baby stores with "Super α Golden" produced in New Zealand and Yashily's "New Formula" to further advance partial transformation. Distribution of adult milk powder and dissolvable products to retail stores will be increased, and there will be foretaste in school districts in autumn and order-placing meetings prior to the Mid-Autumn Festival.

The "high-end maternity CBU" is still positioned to regain leadership of "Dumex" as one of the top four foreign brands and help Arla stand out among a long list of brands. In the second half of the year, the Group will continue strengthening sales teams to make them closer to frontline sales and acquire stronger execution capacity. The Group will constantly advance downward development of the sales channels of existing products (from first- and second-tier cities to third- and fourth-tier cities), and strengthen control over channels by introducing system platform, using costs in a targeted way, improving cost efficiency, and achieving sound anti-goods-fleeing and price-control management. "Dumex" and Arla will duplicate the superior channel operation capacity of domestic brands, which, coupled with their strong brand influence as foreign brands, can create strong competitive strength.

The "innovation CBU" continues to explore innovative businesses and form models based on the steadily improving e-commerce network. Actions to be taken include expanding community marketing, integrating internal market resources, developing official accounts operation and promoting fans-to-member conversion. It will continue to explore Internet-based new business models to lay a foundation for developing the Group's future business models.

Supply chain

In the second half of 2017 and the foreseeable future for 2 to 3 years, the overall supply chain of the Group will be operated in line with its existing central strategies, i.e. "to develop an end-to-end, performance-driven new supply chain management model of Yashili that is oriented toward meeting customers' demands and aims to reduce total costs of the supply chain through specialized functional divisions, teamwork and continuous improvement".

The Group will further rationalize the supply chain management structure to precisely control the whole end-to-end process starting with customers' demands and ended with demands satisfaction. It involves five specialized functions including strategy, planning, procurement, manufacture and logistics, and four fundamental tasks including: team and talent development; operational management excellence, and concepts, methods and tools for constant improvement; EQSA (environment, quality, safety and audit) redlines and risk control; CAPEX on continuous hardware and capital investment and improvement.

The Group will design the supply chain organizational structure as required to get the right person in the right place and let professional persons do professional things. Performance indicators are provided with clear definition, seeking to drive improvement by performance. The performance is designed with three parts including sharing indicators, specialization indicators and redline indicators, among which, sharing highlights teamwork; specialization emphasizes specialized management and division; and redline reflects bottom line awareness where violation can be the overriding reason for disqualifying an employee. The Group will develop specific improvement projects and action plans to ensure goals are achieved and followed up.

While strictly strengthening the management, the Group also adopts an incentive system for the team. The supply chain management center of the Group is working with the human resource department to formulate incentive schemes for the team, in order to boost them to deliver good results and make continuous improvement as a way to achieve excellence in performance.

Human resources

The human resources management center will support the Group in stabilizing sales and improving efficiency in the second half of 2017 in multiple aspects:

I. Sustain transformation and streamline the organization. The center will continue advancing organizational transformation to rationalize resources and optimize allocation based on business activities, improve the supply chain system and speed up the transformation. The center will strengthen efforts to unify working standards, speed up process optimization, carry out relevant training and workshops, and assist business tackling and streamlining as a way to improve operating efficiency of the entire organization. Meanwhile, it will constantly conduct benchmarking between internal and external organization, reduce costs, perform downsizing and streamline administration to build efficient teams.

II. Implement the incentive system which is performance-oriented. The center will implement short and long-term incentive plans featuring more passion of entrepreneurship and distinctive special incentive systems, both of which are performance-oriented, so as to inspire employees with effective mechanism and thus boost businesses. The center will further integrate and improve the Group's remuneration and welfare system to cover all employees, thus enhancing staff's satisfaction and their own well-being.

III. Construct talent pool and strengthen capability. More efforts will be made to train high-potential talent, improve the capability of marketing teams and train new employees. Targeted training will be carried out based on the competence map of the high-potential talent to improve talent pool construction. Targeted professional training, especially a series of marketing trainings, will be conducted to improve the capability of marketing teams and enhance the marketing and promotion capability of the front-line personnel, seeking to build a team of internal marketing trainers, construct learning organizations and boost marketing businesses.

IV. Strengthen cultural construction to improve cohesion. The center will organize distinctive staff activities on quarterly and annual bases to constantly promote and propagandize corporate culture's core values, and maintain communication with employees in various forms and through multiple channels to foster a cultural atmosphere focusing on the values of "passion" and "openness". It will also carry out cultural workshops and team building activities in a bid to strengthen the integration of corporate cultures, thus improving cohesion and fostering a distinctive Yashili culture.

INTERIM DIVIDENDS

The Board does not recommend an interim dividend for the six months ended 30 June 2017 (for the six months ended 30 June 2016: Nil).

DIRECTORS' AND CHIEF EXECUTIVES' INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES AS AT 30 JUNE 2017

As at 30 June 2017, none of the Directors or chief executives of the Company or their respective associates had or was deemed to have any interests or short positions in the shares, underlying shares or debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (Chapter 571 of the Laws of Hong Kong) ("SFO"), which have been notified to the Company and the Stock Exchange of Hong Kong Limited (the "Stock Exchange") pursuant to Division 7 and 8 of Part XV of the SFO, including interests or short positions which the Directors and the chief executives of the Company are taken or deemed to have under such provisions of the SFO, or which are required to be and are recorded in the register required to be kept under section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") as set out in Appendix 10 to the Rules Governing the Listing of Securities (the "Listing Rules").

Furthermore, at no time during the six months ended 30 June 2017 was the Company, its holding company or any of its subsidiaries a party to any arrangements to enable the Directors and chief executives of the Company (including their spouse and children under 18 years of age) to hold any interest or short positions in the shares or underlying shares in, or debentures of, the Company or its associated corporations (within the meaning of Part XV of the SFO).

SUBSTANTIAL SHAREHOLDERS' INTERESTS AND SHORT POSITIONS IN SHARES AND UNDERLYING SHARES AS AT 30 JUNE 2017

To the best of knowledge of any Director or chief executive of the Company, as at 30 June 2017, the persons or corporations (other than Directors or chief executives of the Company) who had interest or short positions in the shares and underlying shares of the Company or its associated corporation(s) which were required to be disclosed to the Company under the provisions of Divisions 2 and 3 of Part XV of the SFO, or which were required to be entered in the register required to be kept under section 336 of the SFO were as follows:

Name of substantial shareholder	Capacity/Nature of interest	Number of shares	Approximate percentage to the issued share capital[7]
Mengniu Dairy[1]	Interests in a controlled corporation	2,422,150,437[6]	51.04%
Mengniu International[2]	Beneficial owner	2,422,150,437[6]	51.04%
Danone SA[3]	Interests in a controlled corporation	1,186,390,074[6]	25.00%
Danone Baby and Medical Holding[3]	Interests in a controlled corporation	1,186,390,074[6]	25.00%
Danone Baby and Medical Nutrition BV[3]	Interests in a controlled corporation	1,186,390,074[6]	25.00%
Nutricia International BV[3]	Interests in a controlled corporation	1,186,390,074[6]	25.00%
Danone Asia[4]	Beneficial owner	1,186,390,074[6]	25.00%
Zhang International Investment Limited[5]	Beneficial owner	303,462,119[6]	6.39%

Notes:

(1) As at 30 June 2017, Mengniu Dairy held 99.95% interest in Mengniu International.

(2) As at 30 June 2017, Mengniu International directly held the relevant shares.

(3) As at 30 June 2017, Danone SA held 100% interest in Danone Baby and Medical Holding. Danone Baby and Medical Holding held 100% interest in Danone Baby and Medical Nutrition BV. Danone Baby and Medical Nutrition BV held 100% interest in Nutricia International BV. Nutricia International BV held 100% interest in Danone Asia.

(4) As at 30 June 2017, Danone Asia directly held the relevant shares.

(5) Zhang International Investment Ltd. is held by Mr. Zhang Lihui, Mr. Zhang Likun, Mr. Zhang Liming, Mr. Zhang Lidian, Mr. Zhang Libo and Ms. She Lifang as their wholly-owned investment holding company to hold their shares in the Company.

(6) All the above shares are held in long position (as defined under Part XV of the SFO).

(7) The total number of issued shares of the Company as at 30 June 2017 was 4,745,560,296.

Save as disclosed above, as at 30 June 2017, the Directors of the Company were not aware of any other person or corporation having an interest or short position in shares and underlying shares of the Company or its associated corporation(s) which were required to be recorded in the register required to be kept by the Company pursuant to Section 336 of the SFO.

SHARE OPTION SCHEME

The Company adopted a share option scheme (the "Pre-IPO Share Option Scheme") on 8 October 2010, and adopted a share option scheme (the "Share Option Scheme") on 8 October 2010. On 23 July 2013, Mengniu International made a voluntary general offer to option holders of the Company ("Option Offer"), to cancel the outstanding options granted under the Pre-IPO Share Option Scheme and the Share Option Scheme. On 13 August 2013 (being the final closing date of the Option Offer), the Option Offer was accepted in respect of 52,088,266 options. The underlying options together with all the rights attached thereto were cancelled and given up and all the outstanding options automatically lapsed upon acceptance of the Option Offer.

No option was granted by the Company nor was there any outstanding option granted by the Company from 1 January 2017 to 30 June 2017.

FOREIGN CURRENCY RISK

The Group is exposed to foreign currency risk primarily from bank deposits, other receivables and bank loans, denominated in foreign currencies, that are currencies other than the functional currencies of the operations to which the transactions relate. The currencies giving rise to this risk are primarily Hong Kong dollars, US dollars and New Zealand dollars.

PLEDGED ASSETS

As at 30 June 2017, the Group has pledged bank deposits, other financial assets and non-current assets in an aggregate of approximately RMB2,337.9 million (31 December 2016: RMB803.1 million).

LIQUIDITY AND CAPITAL RESOURCES

As at 30 June 2017, the liquidity of the Group was comprised of cash and cash equivalents, pledged deposits to be released within one year, long-term bank deposits and other financial assets amounted to RMB3,168.9 million in aggregate (31 December 2016: RMB3,302.9 million), representing a decrease of 4.08%. The decrease was mainly due to a net cash outflow of RMB119.1 million from operating activities.

OPERATING ACTIVITIES

For the six months ended 30 June 2017, the Group's net cash outflows from operating activities amounted to RMB119.1 million (six months ended 30 June 2016: net outflows of RMB107.5 million). Net cash outflow from operating activities increased from that of the same period of 2016, which was mainly due to capital being occupied as a result of the increase in the value of work in progress stocked up.

INVESTING ACTIVITIES

For the six months ended 30 June 2017, the net cash outflow used in investing activities amounted to RMB13.5 million (six months ended 30 June 2016: net outflows of RMB353.0 million), mainly arising from the payment for acquisition of a subsidiary same period of 2016 and the maturity of wealth management products.

FINANCING ACTIVITIES

For the six months ended 30 June 2017, the net cash outflows generated from financing activities amounted to RMB20.8 million (six months ended 30 June 2016: net outflows of RMB107.4 million). The decrease in net cash outflows from financing activities as compared to the same period of 2016 was mainly attributable to the increase in proceeds from bank loans and the decrease in dividend payment.

LOANS AND BORROWINGS

As at 30 June 2017, the Group's bank loans amounted to RMB1,115.8 million (31 December 2016: RMB1,143.1 million), which was repayable on demand.

As at 30 June 2017, the total equity of the Group amounted to RMB5,620.2 million (31 December 2016: RMB5,701.6 million), debt to assets ratio (total bank loans at period end divided by total assets) was 14.1% (31 December 2016: 14.3%).

The capital structure of the Group is reviewed by the Board annually, including the dividend policy and share repurchase activities of the Group.

CORPORATE GOVERNANCE

The Group is dedicated to ensuring high standards of corporate governance with an emphasis on the building up of a diligent and dedicated Board, a sound internal control system, with a view to enhancing its transparency and accountability to shareholders. The Board acknowledges that good corporate governance practices and procedures are beneficial to the Group and its shareholders.

During the period from 1 January 2017 to 30 June 2017, the Company has adopted and complied with all code provisions of the Corporate Governance Code as set out in Appendix 14 to the Listing Rules.

BOARD OF DIRECTORS

For the six months ended 30 June 2017, the Board's composition had undergone the following changes:

(1) Mr. Huang Xiaojun resigned as a non-executive Director with effect from 5 June 2017; and

(2) Ms. Lam Pik Po, Katty was appointed as a non-executive Director with effect from 5 June 2017.

As at 30 June 2017, the Board was comprised of four non-executive Directors, two executive Directors, and three independent non-executive Directors. The non-executive Directors were Mr. Jeffrey, Minfang Lu (Chairman), Mr. Qin Peng, Mr. Zhang Ping and Ms. Lam Pik Po, Katty; the executive Directors were Mr. Chopin Zhang and Mr. Hua Li; and the independent non-executive Directors were Mr. Mok Wai Bun Ben, Mr. Cheng Shoutai and Mr. Lee Kong Wai Conway.

INDEPENDENT NON-EXECUTIVE DIRECTORS

Pursuant to Rule 3.10A of the Listing Rules, independent non-executive Directors shall represent at least one-third of the board. During the period from 1 January 2017 to 30 June 2017, the Board of the Company comprises nine members, three of whom are independent non-executive Directors. Therefore, Rule 3.10A has been duly complied with by the Company during the said period.

DISCLOSURE OF INFORMATION OF DIRECTORS UNDER RULES 13.51(2) AND 13.51(B)(1) OF THE LISTING RULES

Save as disclosed in the announcement of the Company dated 1 June 2017, there are no changes in the directors' biographical details since the date of the 2016 annual report of the Company, which are required to be disclosed pursuant to Rules 13.51(2) and 13.51(B)(1) of the Listing Rules.

SECURITIES TRANSACTIONS OF DIRECTORS

The Board has adopted the Model Code as the Company's code of conduct and rules governing dealings by all Directors in the securities of the Company.

The Directors have confirmed, following specific enquiries by the Company, that they have complied with the required standards set out in the Model Code throughout the six months ended 30 June 2017.

PURCHASE, SALE OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES

Neither the Company nor any of its subsidiaries purchased, redeemed or sold any of the Company's listed securities during the six months ended 30 June 2017.

COMPANY SECRETARY

Mr. Li Yuejin and Ms. Ho Siu Pik are the joint company secretaries of the Company following the appointment of Mr. Li Yuejin as a joint company secretary on 11 October 2016. Following the resignation of Mr. Li Yuejin as the joint company secretary of the Company on 6 July 2017, Ms. Ho Siu Pik became the sole company secretary of the Company. Ms. Ho is a director of the Corporate Services Department of Tricor Services Limited and is not an employee of the Company. During the interim period prior to the appointment of a new joint company secretary, Ms. Ho Siu Pik will contact the management of the Company and report to the chairman of the Board and/or the chief executive officer of the Company through Mr. Eric Fang of Investment Management Division of the Company when necessary in accordance with the code provisions set out in the Corporate Governance Code in Appendix 14 of the Listing Rules.

AUDIT COMMITTEE

As at 29 August 2017, the Audit Committee consists of two independent non-executive Directors, namely Mr. Lee Kong Wai Conway (Chairman), Mr. Mok Wai Bun Ben and one non-executive Director, namely Mr. Zhang Ping (including one independent non-executive Director who possesses the appropriate professional qualifications or accounting or related financial management expertise).

The audit committee has reviewed together with the management, the accounting principles and policies adopted by the Group and the Group's unaudited interim results for the six months ended 30 June 2017, and was of the opinion that the preparation of such interim results complied with the applicable accounting standards and requirements and that adequate disclosures have been made.

In addition, the independent auditors of the Company, Ernst & Young, have reviewed unaudited interim results for the six months ended 30 June 2017 in accordance with Hong Kong Standard on Review Engagements 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Hong Kong Institute of Certified Public Accountants.

SCOPE OF WORK OF ERNST & YOUNG

The financial figures set out in the announcement of interim results for the year ended 30 June 2017 have been agreed by the Group's auditor, Ernst & Young, to the amounts set out in the Group's draft condensed consolidated financial statements for the current period. The work performed by Ernst & Young in this respect did not constitute an assurance engagement in accordance with Hong Kong Standards on Auditing, Hong Kong Standards on Review Engagements or Hong Kong Standards on Assurance Engagements issued by the Hong Kong Institute of Certified Public Accountants and consequently no assurance has been expressed by Ernst & Young on the announcement of interim results.

PUBLICATION OF INTERIM REPORT

The interim report of the Company for the six months ended 30 June 2017 containing all the applicable information required by the Listing Rules will be dispatched to the shareholders of the Company and made available for review on the websites of The Stock Exchange of Hong Kong Limited (www.hkexnews.hk) and the Company (www.yashili.hk) in due course.

By order of the Board
Yashili International Holdings Ltd
雅士利國際控股有限公司
Jeffrey, Minfang Lu
Chairman

Hong Kong, 29 August 2017

As at the date of this announcement, the board of directors of the Company comprises: Mr. Jeffrey, Minfang Lu (Chairman), Mr. Qin Peng, Mr. Zhang Ping and Ms. Lam Pik Po, Katty as non-executive directors; Mr. Chopin Zhang and Mr. Hua Li as executive directors; and Mr. Mok Wai Bun Ben, Mr. Cheng Shoutai and Mr. Lee Kong Wai Conway as independent non-executive directors.