



## Sector Report: Consumer Sector - Food & Beverage

行业报告：消费行业 - 食品饮料

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# Striving for Growth During Unprecedented Changes in 2020

2020年在前所未见的变局中求发展

- The food and beverage (F&B) industry is undergoing unprecedented changes.** The demographics, occupational structure and geographical distribution of consumers in China are undergoing fundamental changes. Due to the rise in new distribution channels, China's FMCG channels have become more fragmented than ever. Due to the emergence of new media, the forms of communication with consumers are also undergoing huge changes. The rise of new consumer brands is changing the industry landscape. In addition, the NCP epidemic will have significant impact in the short term.
- Consumption upgrade is the major driving force for industry growth.** Except for coffee, fresh milk, bottled water and other sub-categories, the sales volume of most food & beverage products have reached saturation. Consumption upgrade which promotes product mix improvement is the major growth driver of the F&B industry. As consumption upgrade continues, high-quality consumer products and catering companies which can meet consumer demand for convenience, enjoyment and health, will further grow. Moreover, specialization, industrialization, branding and differentiation can create added value for F&B companies.
- Maintain "Outperform" rating for the sector.** In the current economic downturn, we believe that food and beverage consumption will play a more vital role. We expect that the concentration of the catering category will continue to rise. We are optimistic about growth and product mix upgrade of dairy category. Sparkling products become more diversified, providing more opportunities for leading companies. Top picks of the sector are Mengniu Dairy (02319 HK) and China Foods (00506 HK).
- 食品饮料行业迎来前所未有之变局。**中国消费者的年龄结构、职业结构、地理分布正在发生根本性的变动。由于新分销渠道的崛起，中国的快消品渠道变得前所未有的撕裂。因为新媒体的出现，与消费者沟通的形式也在发生重大变动。大量的新消费品牌的兴起正在改变行业格局。而新冠肺炎疫情有着强烈的短期影响。
- 消费升级成为行业增长的最重要动力。**除咖啡、鲜奶、瓶装水等若干子品类外，大部分的食品饮料产品的销量已经趋于饱和。消费升级带来产品结构改善，是食品饮料行业的主要增长动力。随着消费升级的继续，可以满足消费者方便需求、享乐需求和健康需求的优质消费品和餐饮企业还会得到进一步增长。而专业化、工业化、品牌化和差异化可以为食品饮料企业创造更多附加值。
- 维持行业“跑赢大市”评级。**在当前经济下行的局面下，我们认为食品饮料消费将起到压舱石的作用。我们预计餐饮行业集中度将继续提升。我们看好乳制品行业的增长空间和产品结构升级空间。汽水产品更加多元化，为汽水龙头提供了新的增长机会。行业首选为蒙牛乳业(02319 HK)和中国食品(00506 HK)。

Rating:

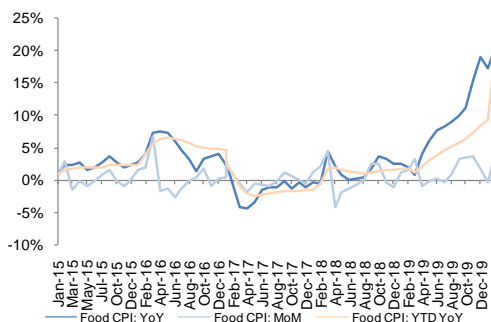
**Outperform**  
Maintained

评级:

**跑赢大市** (维持)

CPI: Food

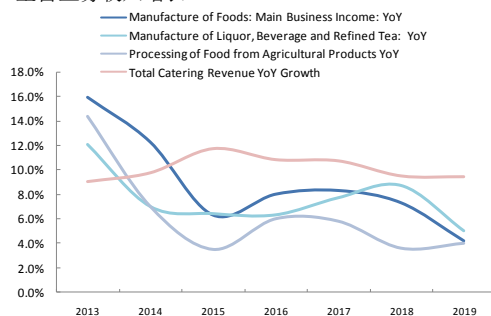
食品价格指数



Source: National Statistics Bureau of the PRC.

YoY Growth of Main Business Income

主营业务收入增长



Source: National Statistics Bureau of the PRC.

Company Name	Code	Price	Rating	19PER	20PER	21PER	19ROE	19P/B	19Yield
公司名称	编号	股价(HKS)	投资评级	市盈率(x)	市盈率(x)	市盈率(x)	净资产收益率(%)	市净率(x)	股息率(%)
Uni-President China	00220 HK	8.700	Neutral	24.3	23.1	21.9	10.4	2.5	2.1
China Resources Beer	00291 HK	37.950	Neutral	83.1	42.4	30.7	6.9	5.6	0.5
Tingyi	00322 HK	14.600	Neutral	27.8	25.4	23.4	13.4	3.7	2.7
Café de Coral	00341 HK	17.560	Accumulate	17.3	24.5	22.2	18.3	3.6	4.8
Vitasoy International	00345 HK	29.950	Accumulate	45.7	44.2	39.7	22.9	10.0	1.4
China Foods	00506 HK	3.000	Buy	17.1	15.1	13.4	10.1	1.7	1.7
Mengniu Dairy	02319 HK	29.550	Accumulate	15.5	22.2	19.4	25.0	3.6	1.5
Dali Foods	03799 HK	5.650	Buy	18.0	16.5	15.7	23.6	4.0	5.6
Tianyun International	06836 HK	0.930	Buy	5.0	4.2	3.6	19.7	0.9	5.4
Weighted Average.									
市值加权平均				37.7	28.3	23.8	16.6	4.5	2.2

Source: the Companies, Bloomberg, Guotai Junan International.

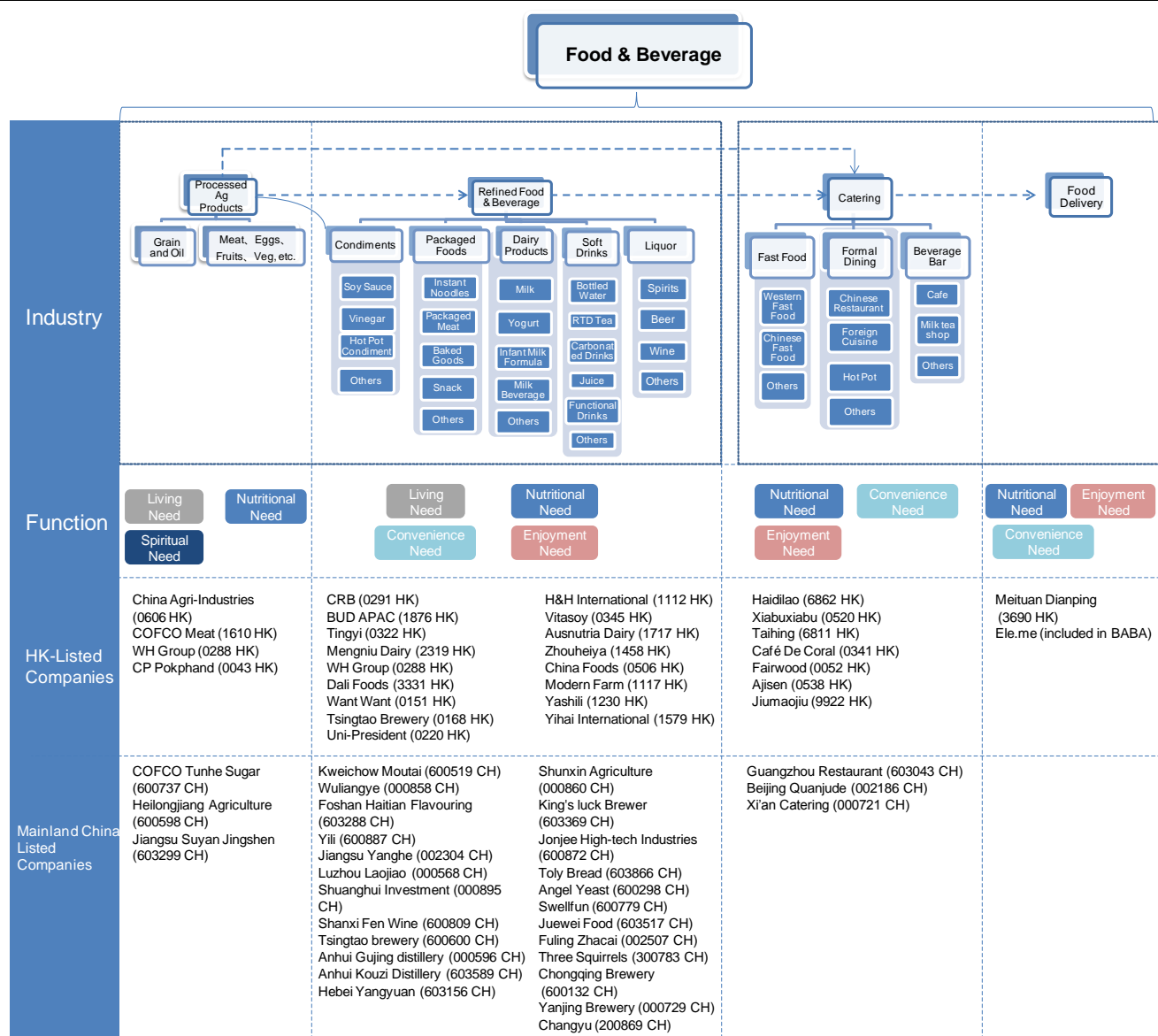
## TABLE OF CONTENTS

Overview .....	3
Industry Analysis .....	10
Dairy Products Category .....	10
Soft Drinks.....	16
Beer.....	21
Packaged Food .....	26
Catering.....	32
Food Delivery .....	42
Hong Kong Catering Industry .....	45
How Ongoing Structural Changes of Chinese Consumers Impact on Consumption.....	46
How Changes in Demographics Impact Consumption .....	46
How Changes in Occupation Structure and Income Impact Consumption .....	48
How Changes in Consumer Geographic Distribution Impact Consumption .....	53
How Changes in Sales Distribution Channels Impact Consumption .....	55
How Changes in Media Impact Consumption .....	63
The Opportunities and Challenges Brought by the Rise of New Consumer Brands .....	68
Valuation .....	71
Conclusion .....	76

## Overview

**The food & beverage industry is extremely rational and highly stable.** The food & beverage industry includes the processing of agricultural products (the output is fresh foods), the manufacturing industry (the output is packaged food, liquor, soft drinks, condiments, etc.), and the catering category (including food delivery). Fresh foods have always been the largest component of food consumption. The main consumption form is fresh foods from supermarkets or wet markets as ingredients to cook, which meets basic living and nutritional needs. The food & beverage manufacturing industry has been a rapidly-rising industry after the reform and opening up of China's markets. It mainly meets consumer demand for more nutritional foods such as milk, yogurt, etc., and demand for convenience in food consumption, such as instant noodles and packaged meat. The existence of liquor and soft drinks is to make consumers have a happy mood and meet the enjoyment needs of consumers. Furthermore, with disposal income rapidly growing and less available time to cook by themselves, Chinese consumers are more willing to dine in restaurants as they deem dining in fine restaurants as a reward to their hard work and a comfortable way to feed themselves. The catering category can at the same time meet consumer convenience/ nutritional/enjoyment needs. The emergence of O2O food delivery has further satisfied consumer need for convenience. Buying foods from markets and cooking for the family can sometimes achieve a high level of self-realization. As eating and drinking is fundamental to human beings, the food & beverage industry has strong rationality, and its existence is almost irreplaceable, which also will not disappear due to technological advances. Furthermore, food & beverage consumption frequency tops all consumption categories. Despite the fluctuation in the macro economy, consumers will hardly reduce consumption of 3 meals per day. The food & beverage industry shows extremely high stability.

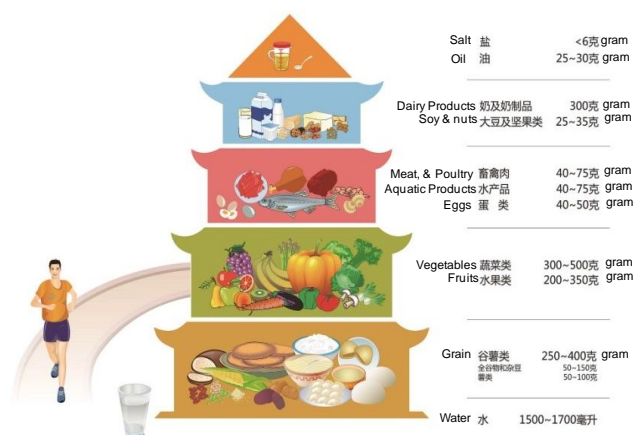
**Figure-1: Food & Beverage Industry Landscape**



Source: Guotai Junan International.

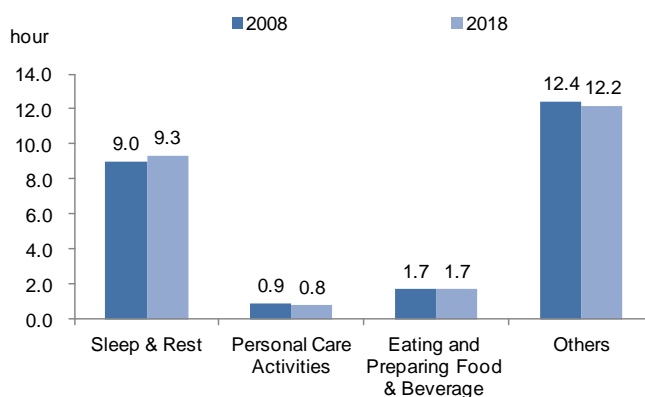
**Food & beverage companies and catering companies essentially compete for daily food intake and daily time allocation of consumers.** As each consumer has limited daily consumption of energy and nutrition, theoretically all food & beverage companies and catering companies are competing for the limited daily food intake of consumers. According to food intake recommendations from the China Nutrition Society (CNS), Chinese consumption of cereals and meats have reached the standards recommended by the CNS, but the per capita consumption of dairy products is far from the recommended value. With consumers' limited daily food intake, many seemingly unrelated categories may also be competing. For example, eating too much snack foods (biscuits, small bread, nuts, etc.) will affect the consumption of dining out. During the Novel Coronavirus Pneumonia (NCP) epidemic, residents cannot dine out and they have to cook at home every day, so demand for fresh foods and convenient foods surged significantly. Compared to food, consumption of beverages (liquor and soft drinks) is more flexible as people can metabolize water faster. For example, at dinner, one person can drink more than 10 bottles of beer, but it is impossible to eat more than ten roasted chickens. Relatively speaking, beverage consumption is not limited by stomach space but liquor consumption can be limited by the potential intake of each person. All alcoholic beverages including spirits, wine and beers, etc, compete with each other. On the other hand, in 2018, Chinese people spent an hour and 44 minutes on dietary activities per day, only 4 minutes more than in 2008. As the rhythm of life quickens, consumers inevitably reduce food preparation time in the limited time of dietary activities, which is reflected in the rapid development of the convenience foods and the catering category.

Figure-2: Chinese Dietary Guidelines



Source: Chinese Nutrition Society.

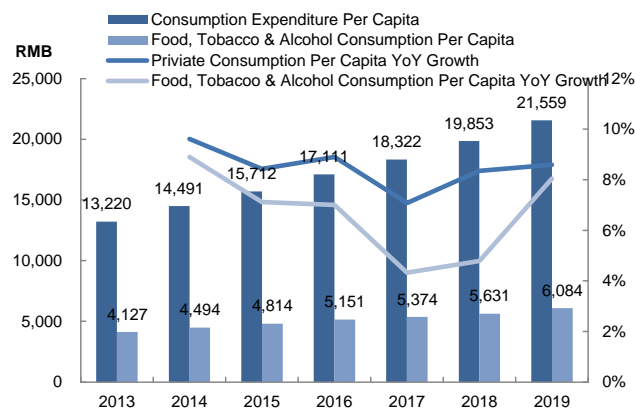
Figure-3: Average Time Distribution of Per Person Per Day



Source: National Bureau of Statistics of the PRC, Guotai Junan International.

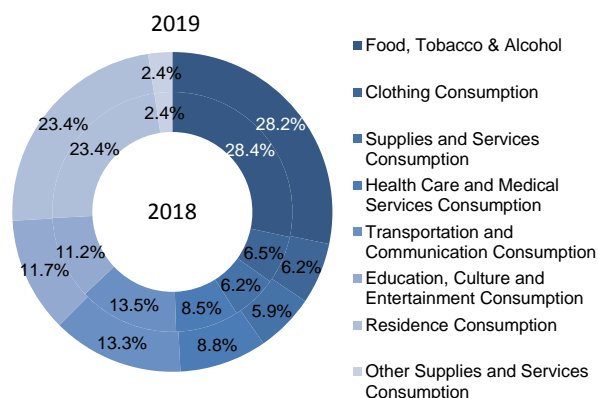
**Food is still the largest consumption expenditure of Chinese citizens, but the proportion is decreasing year by year.** Due to the rapid development of the China's economy, Chinese consumer demand for food has been largely satisfied, as a result, the growth rate of food consumption (including food & beverage and tobacco & liquor) per capita over recent years has been notably slower than consumption expenditure per capita. As consumers spend more on discretionary consumer goods and services, food consumption mix of consumption expenditure per capita has continuously declined to 28.2% in 2019 from 55% in 1990. Food consumption expenditure growth has picked up in 2019 as increasing pork prices drove up food CPI. Though China's food consumption is still the highest contribution to private consumption expenditure, with reference to developed East Asian countries and areas such as Japan, South Korea, China Taiwan and China Hong Kong, China's food consumption growth is expected to underperform private consumption growth but food consumption mix may stabilize at 20%-25%, still the highest among all consumption categories.

**Figure-4: Consumption Expenditure Per Capita and Food, Tobacco & Alcohol Consumption Per Capita in China**



Source: National Bureau of Statistics of the PRC, Guotai Junan International.

**Figure-5: Mix of Consumption Expenditure Per Capita in China**

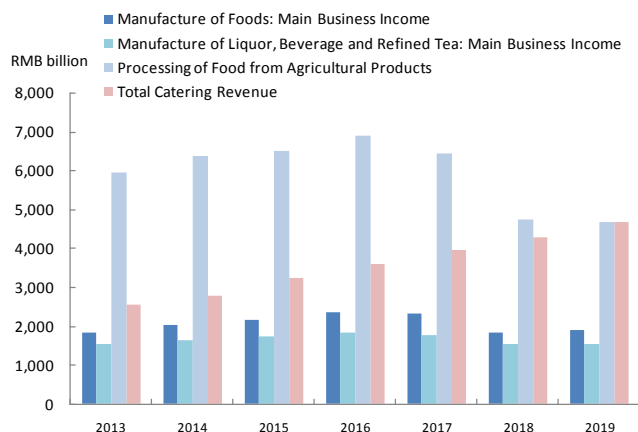


Source: National Bureau of Statistics of the PRC, Guotai Junan International.

**What are the growth drivers of the seemingly saturated food & beverage industry?** China's food consumption is still the highest contribution to private consumption expenditure. Three meals per day is a strong human nature demand, which indicates that 1,095 meals are needed for every person each year. Together with snacks, brunch, soft drinks, liquor and late-night snacks, food consumption has the highest consumption frequency among all consumption categories. The growth drivers of the food & beverage industry will mainly come from specialization, industrialization, branding and differentiation, which can create more added value for the food & beverage industry. In addition, food & beverage consumption not only meets the basic living needs and nutritional needs of people, but also meets the enjoyment needs of people, such as liquor, soft drinks, snack foods and high-end catering. And as work becomes more stressful and the pace of living quickens, consumers' demand for conveniently intaking food is increasing gradually, which benefits convenience foods and meal replacement foods producers. Although consumers' needs for nutrition have been basically met, consumers' demand for health is endless, which benefits organic food producers. As the consumption upgrade continues, high-quality consumer products which can meet consumer convenience needs, enjoyment needs and health needs which will further grow.

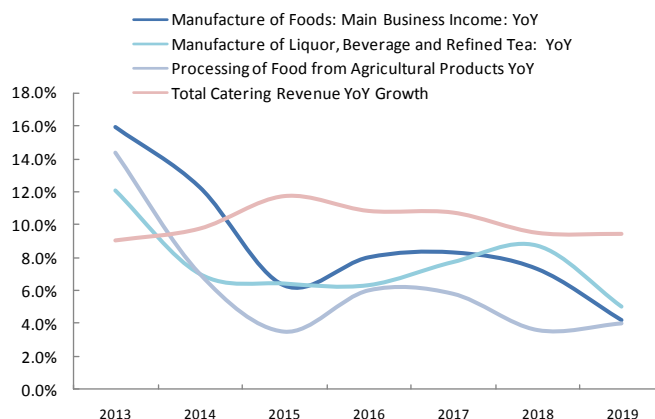
**The supply of food & beverage has become more specialized.** The proportion of consumers who still cook at home is rapidly declining. As consumers' income increases, disposable time decreases, as well as young people lacking cooking skills, more consumers are willing to go to restaurants to order food delivery or to eat convenience foods. The manufacture of food and manufacture of liquor, beverages and refined tea notably outperformed that of processing of agricultural food products. The catering category, which is more specialized compared to cooking at home, reported stronger growth than retail sales growth and GDP growth over recent years. Furthermore, from 2015 onwards, on-demand food delivery, which roots into the catering category with the help of intelligent dispatch systems, brought great changes to China's food industry. On-demand food delivery is the highest efficiency method of food consumption so far and a prime example of specialization and social division. And the rise of fresh food e-commerce and community group buying is mainly attributing to consumers' needs to reduce time on purchasing fresh food. The specialization of food & beverage supply also further meet the diversified needs of consumers for food & beverage products. The rise of catering supply chain companies and FMCG B2B e-commerce also made the distribution of food & beverage products more efficient.

**Figure-6: Main Business Income of Manufacture of Foods and Liquor, Beverage and Refined Tea, Processing of Food from Agricultural Products and Total Catering Revenue.**



Source: National Bureau of Statistics of the PRC, Guotai Junan International.  
Note: According to the statistical standard of National Bureau of Statistics, the scope of investigation of industrial enterprises above designated size was adjusted regularly every year.

**Figure-7: YoY Growth of Main Business Income of Manufacture of Foods and Liquor, Beverage and Refined Tea, and Processing of Food from Agricultural Products and YoY Growth of Total Catering Revenue.**

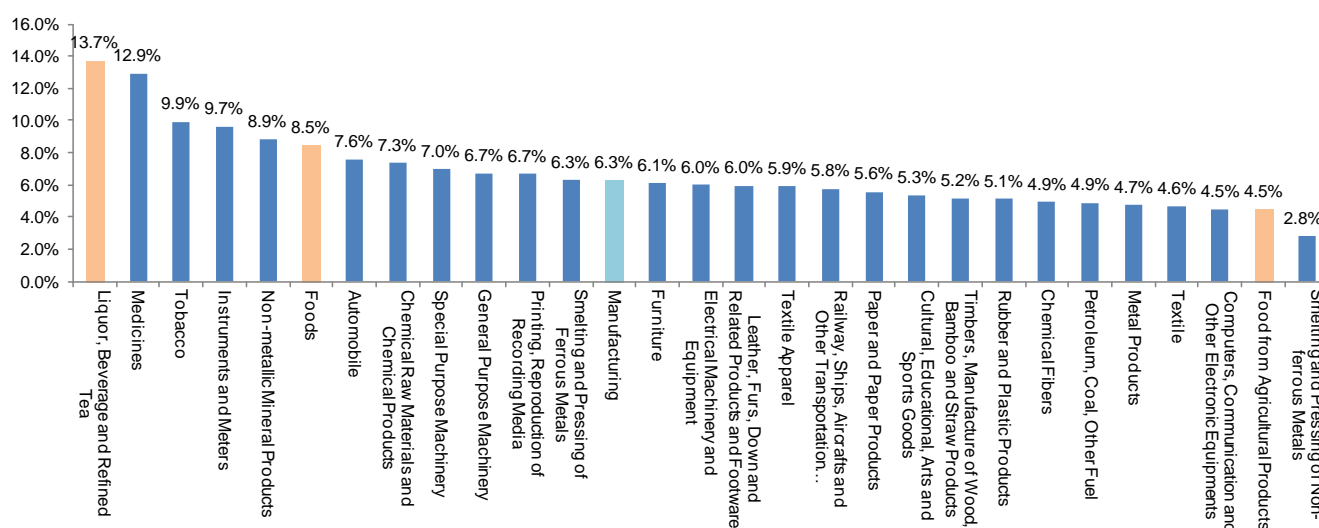


Source: National Bureau of Statistics of the PRC, Guotai Junan International.  
Note: The growth rates are calculated according to comparable caliber.

**The industrialization of food & beverages has created great value.** Although the agricultural products processing industry and catering category have large sales scale, in Hong Kong stock market and China stock market, most of the listed food & beverage companies are in the manufacturing industry, mainly because compared to the processing industry, the manufacturing industry has a more complicated production process, which created higher value. In addition, the finished products of the food & beverage manufacturing industry are highly standardized, which enables leading companies to rapidly expand and achieve scale effects. Although agricultural products processing industry has large sales scale, its added value and profit margin are not high enough to generate more listed companies. The catering category (except hot pot and fast food) is less standardized and less automated, and it is difficult to rapidly expand and generate scale effects. Taking the advantage of industrialization, the food & beverage manufacturing industry produces food and beverage products safely, efficiently, and on a large scale, which has given food and beverages new attributes. Controlling fermentation has become one of the most important processes in food and beverage manufacturing. Fermentation includes food fermentation (such as yogurt, cheese, bread, pickle, fermented bean curd, fermented meat and fish, etc.) and brewing (liquor such as beer, spirits, wine and condiments such as soy sauce and vinegar). Compared with ordinary fermentation, industrial fermentation has stricter control over the fermentation process, more advanced fermentation technology, and can achieve large-scale mass production. Furthermore, the industrialization of food and beverages solves the problem of preservation of food and beverages by sterilizing and sealing under the premise of destroying nutritional components as little as possible, which greatly extends the shelf life of food and beverages, and improves the sales radius and economic value of food and beverages. In addition, the food and beverage manufacturing industry has made food and beverage consumption more flexible by designing portable packaging, which meets consumers' convenience needs for food and beverages. Comparing the average profit margin of the manufacturing industry, we find that the food manufacturing industry and the liquor, beverage, and refined tea manufacturing industries have higher profit margins. And the profit margin of the liquor, beverages, and refined tea manufacturing industries is the highest among all manufacturing industries as liquor, beverages and refined tea have the longest manufacturing period and unique flavor.



**Figure-8: Sales Margins of Manufacturing Sectors**



Source: National Bureau of Statistics of the PRC, Guotai Junan International.

**Product homogeneity and concerns about food safety are important factors in increasing market concentration.** Product homogeneity within categories means that there is no essential difference in the products produced by different companies, and consumers have no special preference for products of certain companies. In short, even loyal consumers who close their eyes can't tell the difference between different companies' products. With high product homogeneity categories, leading players can produce on a large scale to minimize costs, but small brands cannot achieve large scale sales, resulting in high unit production costs, so small brands are struggling to compete with leading brands. In categories where it is difficult to achieve differentiation, it is challenging for small brands to convince consumers to pay a premium for special taste, concepts or packaging. For example, bottled water, instant noodles and milk are highly homogenous, where it is difficult for companies to create novel products, so brand influence and distribution layout have become the most important factors influencing consumer choice, however, they happened to be the strengths of leading brands. According to Nielsen, the top 2 companies in the bottled water market in 2018 had market share of 51.2%, the top 2 companies in the instant noodles market had market share of 61.2%, and the top 2 companies in the UHT milk market had market share of 67.3%. On the other hand, under China's current development situation, food safety issues are still an important factor influencing consumer choice, especially in food for infants such as milk powder, milk and candy. Consumers generally believe that the quality of top brands' products is better, which also have fewer food safety risks, resulting in high market concentration.

**Homogeneity is also a double-edged sword.** In highly homogenous categories, although leading companies maintain a high market share, they usually have to maintain a low profitability level to prevent new entrants from entering the market and the competition among leading companies is intense as well. If products are highly differentiated within categories, such as liquor, condiments, etc., the taste of different brands' products have significant differentiation. Different brands can own a group of different loyal consumers, therefore leading brands struggle to increase their market share. The same truth is in the catering category. But the advantage of differentiation is that companies can make consumers loyal to their products and achieve premium margins. We have noticed that many new consumer brands (such as Simple Love, Liziqi, Saturn Bird and Yuanqi Senlin) established and gained a firm foothold in the market over recent years, challenging the position of leading brands which have dominated the market for a long time. These new brands seized the opportunity of consumption upgrade, launched differentiated products, distributed in new channels and communicated with consumers through new media channels. For specific analysis, please refer to the chapter 'The Opportunities and Challenges Brought by the Rise of New Consumer Brands' in this report.

**Categories with a short transport radius are likely to form a regional market, which hinders the improvement in national market concentration to some extent.** Fresh milk, chilled yoghurt, and short shelf-life bread have a short shipping radius due to their short shelf life, while beer has a short shipping radius due to low unit value with the need to recycle empty bottles. Categories with a short shipping radius are naturally easy for regional brands to operate, as regional brands have factories, distribution channels, and loyal local consumers. Fresh milk and chilled yoghurt shows more regional characteristics due to restrictions on the procurement of raw milk and shipping radius, especially fresh milk, as the shelf life of fresh milk (7-14 days) is shorter than chilled yogurt (21 days). It is relatively easier for national players to break through the regional restrictions in the short shelf-life bread

market and beer market, as they can achieve outbound expansion by building additional factories. Leading companies of beer and short shelf-life bread have complete national operations. Within these markets, the main factor limiting the outbound expansion of national players is that strong local brands may fight back with a price war, which leads to a delays in profitability. As the short shelf-life bread category has a relatively shorter history with less strong regional players, both Toly and Dali have the chance to dominate the market. As leading dairy players such as Mengniu and Yili have controlled more upstream raw milk sources as well as raw milk sources near urban areas which continued to shrink due to the influence of environmental protection policies, the strength of regional dairy companies has been weakened. In addition, due to the improvement in transportation and advanced preservation technology, the shipment radius of leading dairy companies lengthened. We expect that the market concentration of fresh milk and chilled yogurt will continue to rise.

**Inimitable products and brands create economic moats for companies.** Among all Hong Kong and A-share listed companies, baijiu companies show the highest gross margin and net margin, mainly because high-end baijiu products have unique flavors and tastes that cannot be perfectly imitated by competitors. The unique flavors and taste of baijiu are generated through fermentation, blending and long-term storage. There are too many microorganisms participating in the fermentation process, and long-term storage brings about great changes, therefore each baijiu product has distinctive flavor and taste, which are impossible to be perfectly replicated. For food and beverage companies, distinct and inimitable products is the most cost-efficient way to form differentiation, which is why high-end spirits companies and condiment companies can achieve a premium margin. In addition, some addictive drinks such as Coca-Cola and Vita Lemon Tea can win loyal consumers with their distinctive taste. Once a distinctive product gains a first-mover advantage, it will firmly occupy the minds of consumers, making the brand a representative of a certain category. For example, Maotai represents sauce-flavored baijiu, Liuge Hetao represents walnut milk, Coca Cola represents carbonated drinks and Vita represents lemon tea. Without inimitable products, companies can only create differentiation by reinforcing brand power, but this method is relatively expensive and requires continuous investment. Most FMCG companies have to spend lots of expenses on advertisement and promotion, which erodes a large proportion of margin.

**Table-1: Profitability of Listed Food & Beverage Companies in China**















































































































Ticker	English Name	Company			Gross margin%		Net margin%	
		Chinese Name	Sector	Market Cap	2018A	2019F	2018A	2019F
600519 CH	KWEICHOW MOUTAI CO LTD-A	贵州茅台	Spirits	1,396,547	91.4%	91.9%	45.6%	46.5%
603589 CH	ANHUI KOUZI DISTILLERY CO -A	口子窖	Spirits	30,497	74.4%	75.6%	35.9%	37.6%
603156 CH	HEBEI YANGYUAN ZHIHUI BEVE-A	养元饮品	Beverage	30,118	50.0%	52.1%	32.9%	35.9%
000858 CH	WULIANGYE YIBIN CO LTD-A	五粮液	Spirits	488,044	73.8%	72.9%	33.4%	34.8%
002507 CH	CHONGQING FULING ZHACAI-A	涪陵榨菜	Foods	19,362	55.8%	58.2%	34.6%	34.0%
002304 CH	JIANGSU YANGHE BREWERY -A	洋河股份	Spirits	161,041	73.7%	71.4%	33.6%	33.4%
603369 CH	JIANGSU KING'S LUCK BREWER-A	今世缘	Spirits	38,578	72.9%	74.2%	30.8%	29.8%
000568 CH	LUZHOU LAOJIAO CO LTD-A	泸州老窖	Spirits	120,664	77.5%	78.8%	26.7%	29.1%
002714 CH	MUYUAN FOODSTUFF CO LTD-A	牧原股份	Agriculture	179,683	9.8%	31.8%	3.9%	28.5%
603288 CH	FOSHAN HAITIAN FLAVOURING -A	海天味业	Condiments	304,507	46.5%	46.2%	25.6%	26.6%
6186 HK	CHINA FEIHE LTD	中国飞鹤	Dairy Products	84,599	67.5%	69.0%	21.6%	25.8%
603198 CH	ANHUI YINGJIA DISTILLERY C-A	迎驾贡酒	Spirits	14,874	60.9%	61.4%	22.3%	22.8%
600779 CH	SICHUAN SWELLFUN CO LTD-A	水井坊	Spirits	25,022	81.9%	82.6%	20.6%	22.5%
000596 CH	ANHUI GUJING DISTILLERY CO-A	古井贡酒	Spirits	63,118	77.8%	78.4%	19.5%	21.2%
200869 CH	YANTAI CHANGYU PIONEER-B	张裕	Wine	15,651	63.0%	59.4%	20.3%	20.4%
002568 CH	SHANGHAI BAIRUN INVESTMENT-A	百润股份	Liquor	14,068	68.7%	66.9%	10.1%	19.9%
600197 CH	XINJIANG YILITE INDUSTRY-A	伊力特	Spirits	6,474	49.0%	51.3%	20.1%	19.6%
000848 CH	HEBEI CHENGDE LOLO CO-A	承德露露	Beverage	7,185	50.8%	50.8%	19.5%	19.4%
300498 CH	WENS FOODSTUFFS GROUP CO - A	温氏股份	Agriculture	172,986	16.9%	28.4%	6.9%	19.0%
000799 CH	JIUGUI LIQUOR CO LTD-A	酒鬼酒	Spirits	11,989	78.8%	79.6%	18.8%	18.6%

Source: Bloomberg, Guotai Junan International.



**Each food & beverage sub-sector shows different characteristics.** The food and beverage industry is a huge market in China, including many sub-sectors, such as packaged food (packaged meat, instant noodles, baked food and leisure foods, etc.), liquor (baijiu, beer, wine, etc.), soft drinks (bottled water, carbonated drinks, RTD tea, etc.), dairy products (milk, yoghurt, milk powder, etc.) and service-oriented catering industries (hot pot and fast food, etc.). These sub-sectors have different characteristics and growth trends. We rate these industries on the basis of rationality, growth potential, nationalization, concentration, and rational competition. In essence, we aim to analyze whether the growth potential and competition environment of certain sub-sectors are friendly enough for listed companies (usually leading companies) to grow. For example, the dairy products category shows high rationality, growth potential and high concentration, but due to high homogenization in the category, intense price competition occurs from time to time, resulting in a low rating for rational competition. Therefore, we should mainly focus on the marginal changes on competition of the dairy products market. As far as fresh milk is concerned, it is worth noting whether the product can break through regional restrictions. Beer, packaged meat, and instant noodles all struggle to grow and have less intense competition, so we need to pay close attention to whether their rationality has changed and whether consumers still need these products. The good news is that consumption upgrades have reinforced their rationality. The catering category has a strong rationality, but market concentration is still low, so we need to figure out how much potential room there is in the market .

**Figure-9: Review of Food & Beverage Sub-Sectors.**

Sub-Sector	Market Size (RMB Billion)	Rationality	Growth Potential	Nationalization	Concentration	Rational Competition
<b>Fresh Foods</b>	<b>4,738</b>	 <b>5</b>	 <b>3</b>	 <b>3</b>	 <b>1</b>	 <b>4</b>
<b>Dairy Products</b>	<b>388</b>	 <b>5</b>	 <b>4</b>	 <b>4.5</b>	 <b>5</b>	 <b>3</b>
Room Temperature Yogurt	134*	 <b>3</b>	 <b>4</b>	 <b>5</b>	 <b>5</b>	 <b>2</b>
Chilled Yogurt		 <b>4</b>	 <b>4</b>	 <b>3</b>	 <b>3.5</b>	 <b>4</b>
UHT Milk	92	 <b>5</b>	 <b>4</b>	 <b>5</b>	 <b>5</b>	 <b>2</b>
Fresh Milk	31	 <b>5</b>	 <b>5</b>	 <b>2</b>	 <b>2</b>	 <b>4</b>
Powder Milk	18	 <b>5</b>	 <b>3</b>	 <b>5</b>	 <b>3</b>	 <b>4</b>
Soy Drinks	11	 <b>3</b>	 <b>5</b>	 <b>5</b>	 <b>4</b>	 <b>4</b>
<b>Soft Drinks</b>	<b>549</b>	 <b>4</b>	 <b>4</b>	 <b>5</b>	 <b>3</b>	 <b>3.5</b>
Bottled Water	183	 <b>4</b>	 <b>5</b>	 <b>4.5</b>	 <b>5</b>	 <b>3</b>
Carbonated Drinks	84	 <b>3.5</b>	 <b>4</b>	 <b>5</b>	 <b>5</b>	 <b>5</b>
RTD Tea	120	 <b>3.5</b>	 <b>4</b>	 <b>5</b>	 <b>5</b>	 <b>3</b>
Juice	89	 <b>3.5</b>	 <b>4</b>	 <b>5</b>	 <b>5</b>	 <b>4</b>
Energy Drinks	41	 <b>5</b>	 <b>5</b>	 <b>5</b>	 <b>5</b>	 <b>4</b>
<b>Beer</b>	<b>614</b>	 <b>4</b>	 <b>3</b>	 <b>4</b>	 <b>5</b>	 <b>3</b>
<b>Spirits</b>	<b>1,247</b>	 <b>4</b>	 <b>4</b>	 <b>4</b>	 <b>1</b>	 <b>4.5</b>
<b>Condiments</b>	<b>1,188</b>	 <b>5</b>	 <b>4</b>	 <b>4</b>	 <b>2</b>	 <b>4</b>
<b>Instant Noodles</b>	<b>91</b>	 <b>4</b>	 <b>2.5</b>	 <b>5</b>	 <b>5</b>	 <b>2</b>
<b>Packaged Meat</b>	<b>79</b>	 <b>3.5</b>	 <b>2.5</b>	 <b>4.5</b>	 <b>5</b>	 <b>4.5</b>
<b>Catering</b>	<b>4,271</b>	 <b>5</b>	 <b>5</b>	 <b>3</b>	 <b>1</b>	 <b>3.5</b>
Hotpot	481	 <b>4</b>	 <b>5</b>	 <b>4</b>	 <b>1</b>	 <b>4</b>
Fast Food		 <b>5</b>	 <b>4</b>	 <b>5</b>	 <b>3</b>	 <b>4</b>

Source: Euromonitor, Guotai Junan International.

Note: Including room temperature yogurt and chilled yogurt.

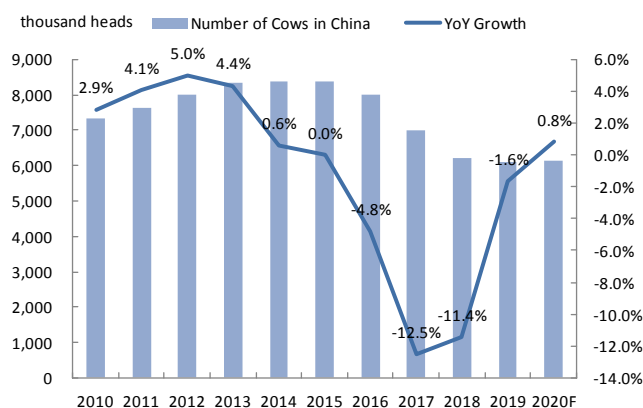
**The food & beverage industry is undergoing unprecedented changes.** Chinese customer demographics, occupational structure and geographical distribution are undergoing fundamental changes. Due to the rise in new distribution channels, China's FMCG channels have become more fragmented than ever. And due to the emergence of new media channels, the form of brands communicating with consumers is also undergoing huge changes. In addition, we have also seen that the rise new consumer brands is changing the industry landscape. These unprecedented changes will bring different opportunities and challenges to different sub-sectors of the food & beverage industry and listed companies in the industry. We will conduct relevant discussions in the following chapters.

## Industry Analysis

### Dairy Products Category

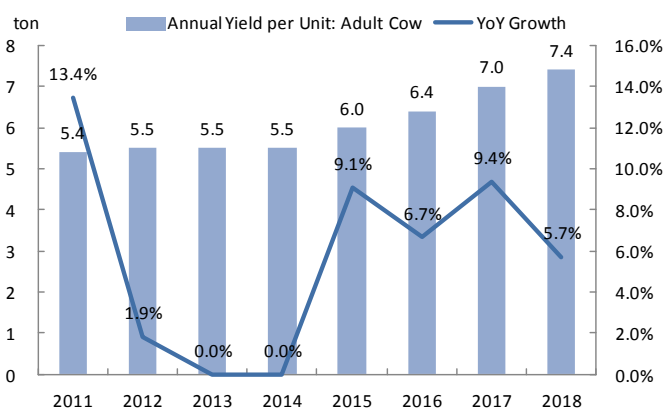
**It will take time for domestic raw milk production capacity to recover.** Due to the supply shortage brought by the decline in number of cows and strong demand for dairy products, China's raw milk price continued to rise in 2H2019. As at Feb. 12, 2020, raw milk price in China was RMB3.81/kg, up 5.2% YoY. Due to stricter environmental protection regulation and lower profitability over the last several years, a large number of small-scale dairy farms with less than 300 cows have been phasing out. De-capacity of cow breeding around southern cities went even further. In addition, driven by the rapid rise in pork prices, beef prices have also seen notable growth, as a result, dairy farmers were willing to slaughter low-efficient cows for sale as beef. United States Department of Agriculture (USDA) data shows that from 2015 to 2019, China's domestic cow inventory has continued to decline for five consecutive years. In 2018, there were 6.2 million cows which declined to 6.1 million in 2019. In the context of the continuous decline in cow inventory, domestic raw milk has remained stable, mainly thanks to the significant increase in annualized yield per milkable cow and the increase in the proportion of milkable cows. According to China Milk Industry Statistics, the annualized yield of milkable cows in China increased to 7.4 tons in 2018. Most Large-scale dairy farms can achieve annualized yield of milkable cows of more than 10 tons due to high-quality dairy cow populations and more optimized feeding methods. Due to the substantial increase in profitability of dairy farming, large-scale dairy farmers have begun to expand cow population in an orderly manner. It is expected that dairy cow inventory will stabilize and recover in 2020. However, it takes 2-3 years from expansion of dairy cow population to the increase in raw milk output. Raw milk price is expected to maintain a slight upward trend in the next 2-3 years. We expect raw milk price to maintain mid-single-digit percentage increase in 2020. Under pressure of increasing raw milk price, leading dairy players forced upstream dairy farmers to accelerate their pace of expansion. Due to the tight supply of raw milk, China's imports of bulk milk powder have increased significantly over the past five years. According to USDA data, China's imported bulk milk powder in 2019 increased by 22.3% YoY to 980,000 tons, exceeding the 2014 level. Imported bulk milk powder is an important source of milk powder supply in China, accounting for more than 40% in 2019. The price change of bulk milk powder can have considerable impact on the input costs of dairy products in China. Whole milk price of GDT, the benchmark for global milk powder price, has been relatively stable over recent years, which had not recurred significant changes like that in 2013.

**Figure-10: Number of Cows in China & YoY Growth**



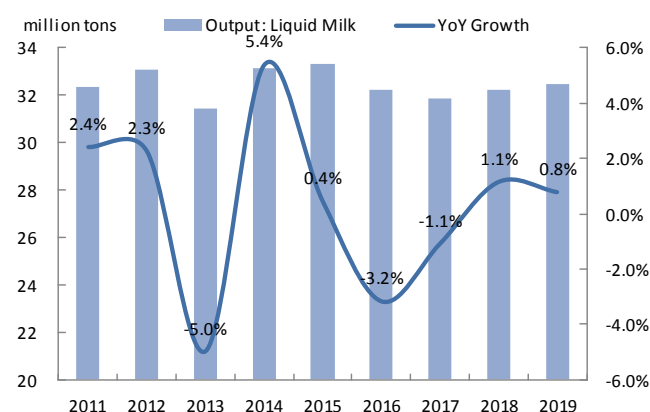
Source: USDA, Guotai Junan International.

**Figure-11: Annual Yield per Unit: Adult Cows**



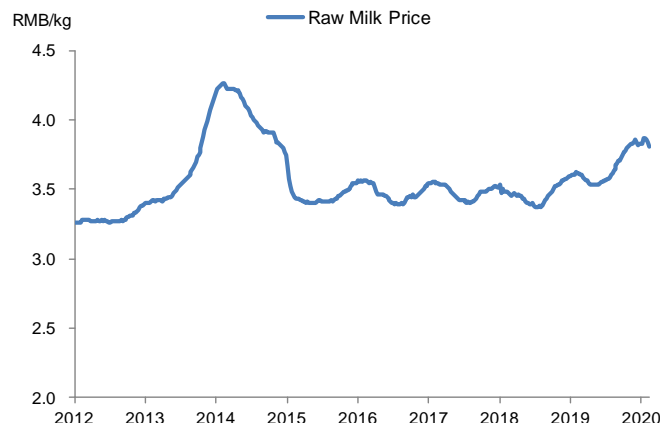
Source: China Milk Industry Statistics, Guotai Junan International.

Figure-12: Liquid Milk Output in China & YoY Growth



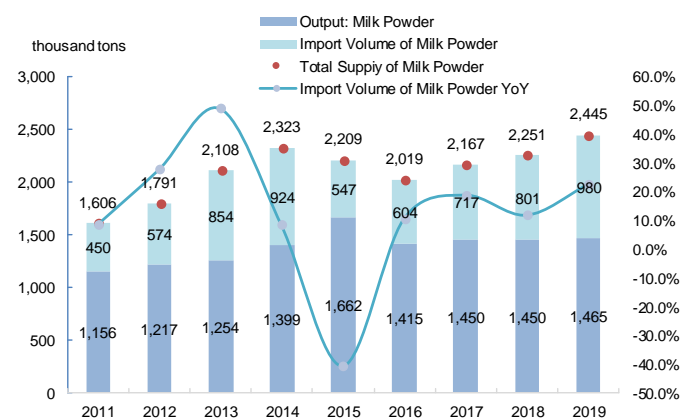
Source: USDA, Guotai Junan International.

Figure-13: Raw Milk Price in China



Source: National Bureau of Statistics of the PRC, Guotai Junan International.

Figure-14: Milk Powder Output in China and Import  
Volume of Milk Powder



Source: USDA, Guotai Junan International.

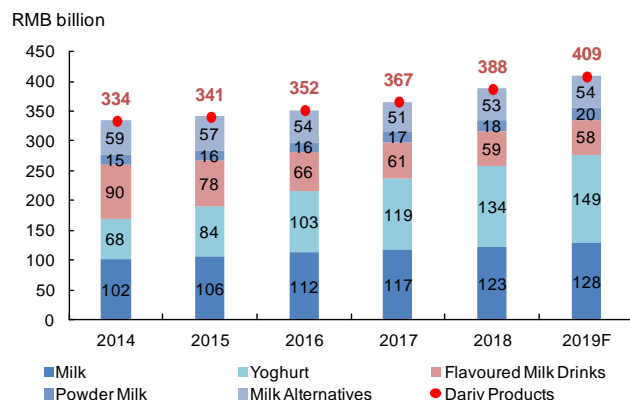
Figure-15: Whole Milk Price of GDT



Source: GDT, Guotai Junan International.

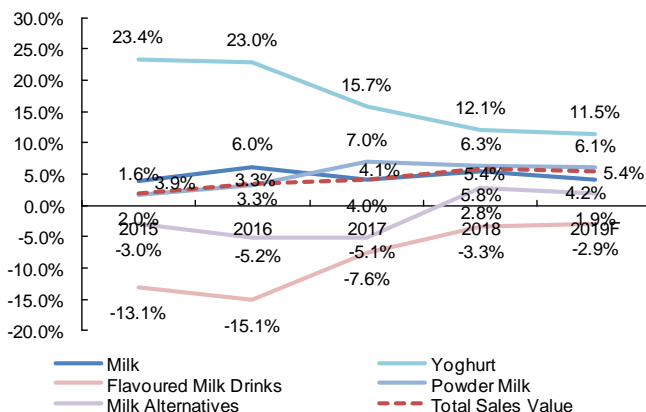
**Room temperature yogurt has become the most important growth driver for the dairy products category over recent years.** In 2009, Bright launched a room temperature yogurt product called Momchilovtsi (莫斯利安), which became the most important driving force for Bright's rapid growth before 2014. In 2013, Yili and Mengniu entered the room temperature yogurt market by launching Ambrosial (安慕希) and Just Yogurt (纯甄), respectively. As Yili and Mengniu have strong distribution advantages, especially Yili, they could distribute their products to every corner of China fairly rapidly, which could gradually squeeze the market share of Bright's Momchilovtsi. As room temperature yogurt has a long shelf life and a large distribution radius, it can penetrate into low-tier cities, resulting in rapid increase in penetration rate. Since its introduction, room temperature yogurt has maintained rapid growth and has become the most critical growth driver of the dairy products category over recent years. The product category of room temperature yogurt has evolved greatly; with more new flavors to attract new consumers. Moreover, the consumption scenario of room temperature yogurt is more comprehensive, including gift packaging for holidays, at-home consumption and ready-to-drink consumption, etc. However, the rapid growth of room temperature yogurt has suppressed growth of chilled yogurt to a certain extent, whose growth has not exceeded low single-digit percentage over recent years. In the future, with the development of cold chain construction and the popularity of health concepts, we believe that chilled yogurt consumption in low-tier cities will gradually increase. In 2017, the market size of yogurt (including room temperature yogurt and chilled yogurt) surpassed that of milk. China's milk market has grown slowly over recent years due to its high penetration rate. The main growth driver is product mix upgrade.

Figure-16: Sales Value of Dairy Products in China



Source: Euromonitor, Guotai Junan International.

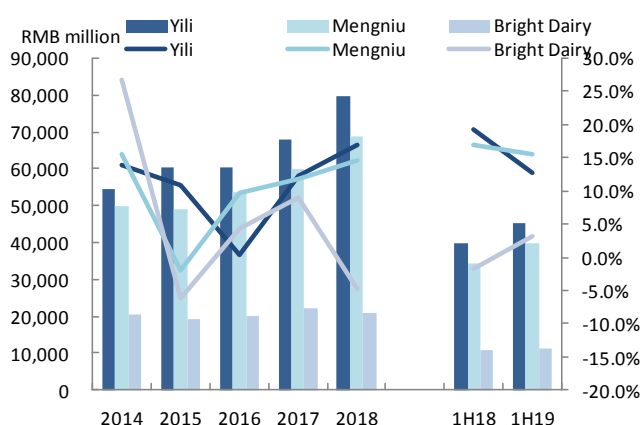
Figure-17: Dairy Products Sales YoY Growth in China



Source: Euromonitor, Guotai Junan International.

A duopoly market has been formed; the further increase in concentration depends on the progress of leading players occupying the chilled dairy products market. As Yili has adopted a deep distribution model which has strong control over its distribution channels, making new products can smoothly penetrating into low-tier cities, allowing Ambrosial to be quickly introduced to the national market. In 2019, Ambrosial's sales (factory price including tax) are expected to exceed RMB20 billion. Driven by Ambrosial, Yili's revenue and market share have continued to grow. Although Mengniu's room temperature yogurt sales are lower than that of Yili, it is rapidly improving its weakness in distribution. Over recent years, Mengniu's Just Yogurt has also achieved rapid growth. In addition, Mengniu has been leading in the high-end milk market, and Milk Deluxe has always maintained the top position in the high-end milk market because UHT dairy products have less differentiation. Leading dairy companies have greater advantages in terms of distribution, brand influence and upstream procurement, resulting in a continuous increase in market concentration. Due to Bright's slow movement in establishing national distribution, Yili and Mengniu have grasped more market share. In 1H2019, Mengniu and Yili's total market share of UHT dairy products was 67.3%, and their total market share of chilled dairy products was 54.7%. The chilled dairy products market, especially fresh milk market, has obvious regional characteristics due to restrictions on raw milk procurement. However, as regional restrictions of fresh milk have been overcome by better transportation and storage technology, Mengniu and Yili have placed more emphasis on the fresh milk market, and we expect market concentration of chilled dairy products to also increase.

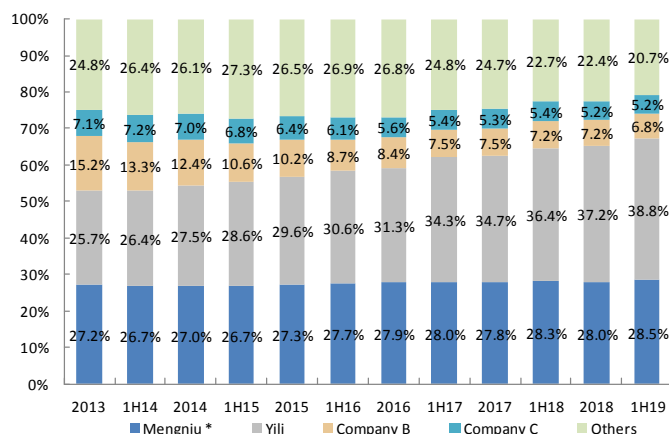
Figure-18: Sales of Leading Dairy Product Companies



Source: the Companies, Guotai Junan International.

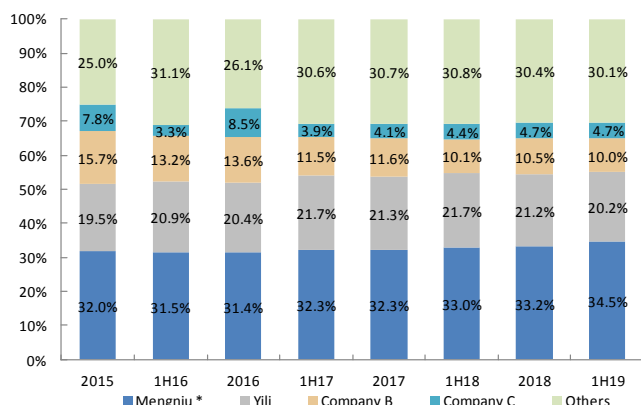
Note: Mengniu's revenue included sales generated from Junlebao which has been disposed of.

Figure-19: Market Share of UHT Dairy Products



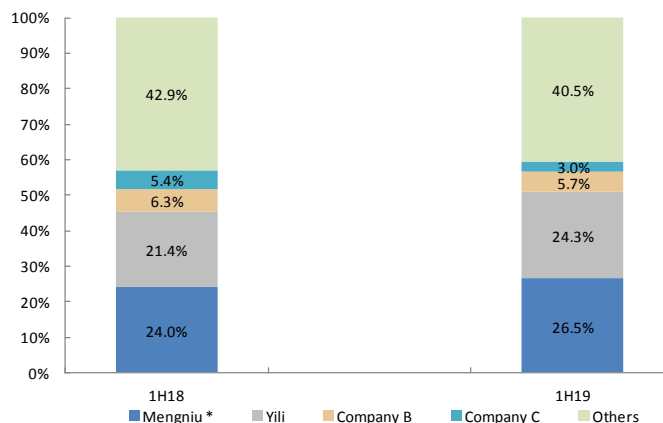
Source: Nielsen, Guotai Junan International.

Figure-20: Market Share of Chilled Yogurt



Source: Nielsen, Guotai Junan International.

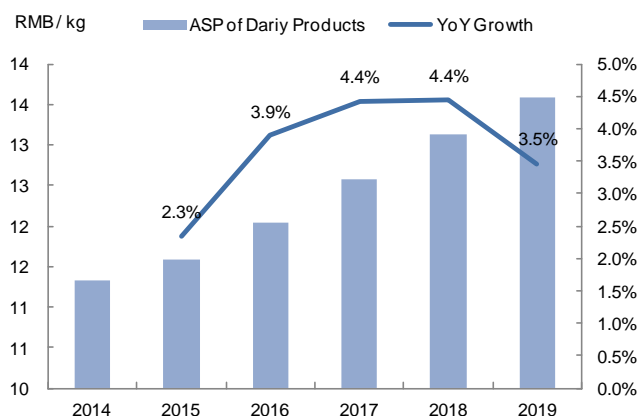
Figure-21: Market Share of Liquid Milk in E-commerce



Source: Nielsen, Guotai Junan International.

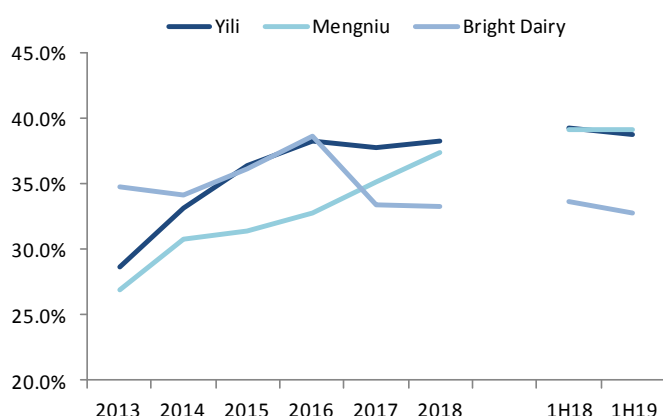
**The dairy product mix continued to upgrade; leading players' profitability continued to improve.** Due to the increasing mix of room temperature yogurt and high-end milk, the ASP of dairy products in China has increased year by year. We have seen that the gross margins of Yili and Mengniu have improved significantly since 2013. The gross margin of dairy companies in 2019 declined slightly, mainly due to the rapid rise in raw milk prices. Leading companies have actively hedged the impact of rising raw material prices through product mix upgrade. For example, Mengniu launched the Dream Cap Milk Dextru to upgrade its products, and Yili also followed up on its own version of Dream Cap. Dairy companies have also upgraded their products by using imported milk sources and organic milk sources. In 2019, dairy companies also introduced more packaging and flavors of room temperature yogurt products to meet the different needs of consumers. In 3Q2019, Yili's revenue increased by 11.2% YoY, slowing, but its high-end star products such as Ambrosial, Satine, and Meiyitian, etc., maintained rapid growth. Mengniu's revenue growth in the 2H2019 is also expected to be slower than 1H2019, but sales growth of Milk Deluxe in 3Q19 is estimated to be more than 25%, and the growth rate of Just Yogurt is estimated to be around 28%.

Figure-22: ASP of Dairy Products in China



Source: Euromonitor, Guotai Junan International.

Figure-23: Gross Margin of Leading Dairy Product Companies



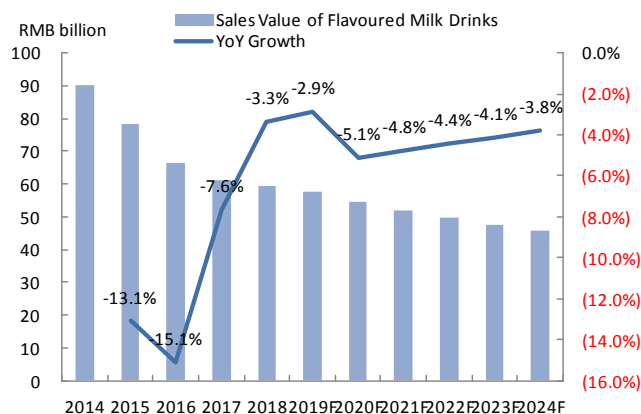
Source: the Companies, Guotai Junan International.

**Increased health consciousness benefits fresh milk but hurts milk drinks.** With the improvement of consumers' living standards and health consciousness, consumers have higher demand for fresh milk, and the construction of cold chains in China has been accelerating, which strongly promotes sales of fresh milk. According to Euromonitor, China's fresh milk sales in 2019 is expected to increase by 11.6% YoY to RMB34.3 billion. China's dairy giants such as Yili and Mengniu, global giants such as Anchor, or e-commerce giants such as Alibaba, all have tapped into the mid-to-high-end fresh milk market. In the past, restricted by transportation radius, the fresh milk market used to be dominated by local brands. However, due to environmental restrictions in recent years, some milk sources around urban areas were eliminated, while national dairy companies such as Mengniu have enhanced their control over milk sources, which is more beneficial to the supply of fresh milk. Local dairy brands such as Yantang and Sanyuan are expected to face greater pressure. On the flip side, flavored milk drinks have suffered from perceptions that such products contain too many sugar and additives. Consequently, health-conscious parents have increasingly turned to purchase room temperature yoghurt and fresh milk for their children instead. Flavored milk drinks saw continued decline in both volume and



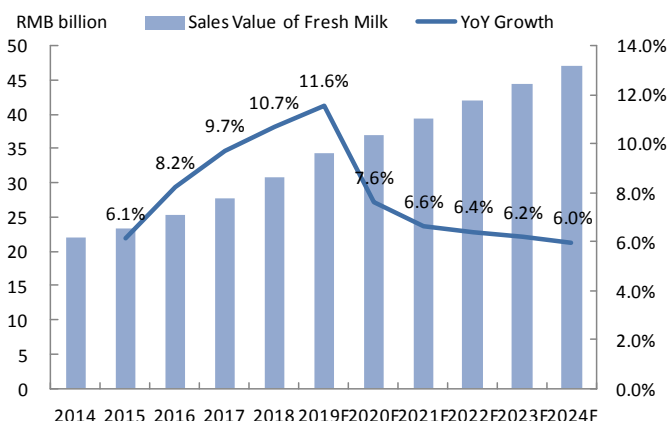
value terms in 2019. Major players' flavored milk drinks all reported sluggish sales.

Figure-24: Sales Value of Flavored Milk Drinks



Source: Euromonitor, Guotai Junan International.

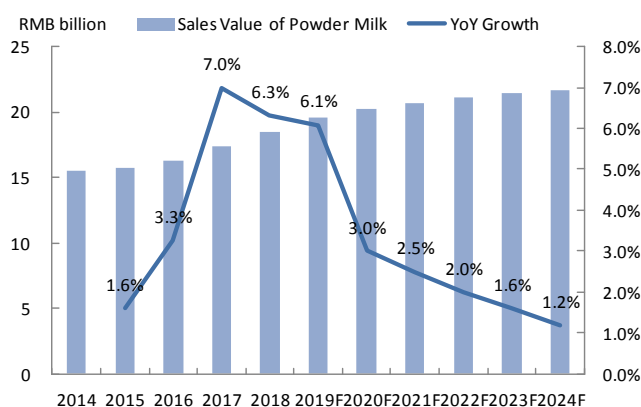
Figure-25: Sales Value of Fresh Milk in China



Source: Euromonitor, Guotai Junan International.

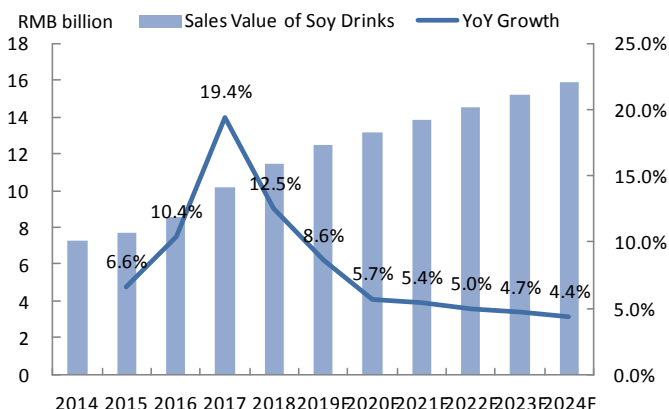
**The infant milk formula (IMF) industry is under pressure; soy milk growth is slowing but potential is still huge.** The decrease in number of newborn babies in China has weighed on IMF sales. As the increase in newborns effect brought by the universal two-child policy has subsided and one-child families and the population of women in childbearing age have declined, the number of newborn babies in China decreased by 3.8% YoY to 14.65 million in 2019. Sales of phase-one IMF has declined considerably in 2019. As time goes by, phase-two and phase-three IMF will also show decline. IMF companies will continue to promote their product structure. Organic IMF and goat IMF are promising products for IMF. On the other hand, after years of rapid growth, the growth of the soymilk industry has slowed. We believe that the growth potential of soymilk is still huge, and its growth rate depends on consumer education. In developed countries and regions, soy milk has become an important alternative to milk due to its health concept and environmental friendliness. Although soy milk brands such as Vitasoy, DoubenDou and Plant Selected are still facing issues including pricing, taste and consumer education, we expect that there is still huge growth potential for packaged soy milk in China.

Figure-26: Sales Value of Powder Milk



Source: Euromonitor, Guotai Junan International.

Figure-27: Sales Value of Soy Milk



Source: Euromonitor, Guotai Junan International.

**Per capita consumption of dairy products still has room to rise.** Dairy products mainly meet consumers' nutritional needs, and at the same time meets enjoyment needs and convenience needs. Dairy products are rich in nutrients such as proteins, minerals and vitamins, which are extremely beneficial for the nutritional needs of infants and young children. Yogurt, especially room temperature yogurt, has a rich and attractive taste, which meets consumers' enjoyment needs, a little bit like beverages. The popularity of Tetra Pak packaging makes the consumption of dairy products more convenient, coupled with the rich nutrition, dairy products can meet consumer demand for meal replacements to a certain extent. Compared with developed countries and regions in Asia, such as Japan, South Korea, China Taiwan and China Hong Kong, etc., the per capita consumption of dairy products in mainland China has large room for growth, especially when per capita GDP increasing from US\$10,000 dollars to US\$20,000 dollars. As the proportion of young customers who have formed consumption habits of dairy products increases, there is still much room for growth in China's dairy consumption market. The dairy products category shows high rationality, growth potential, high

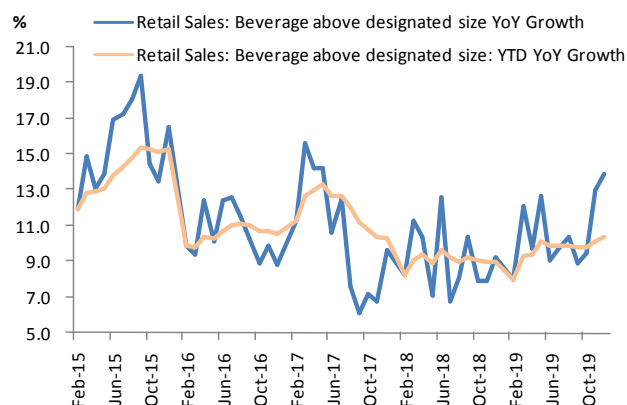
concentration, and national reach, but due to high homogenization in the category, intense price competition occurs from time to time, resulting in a low amount of rational competition. Therefore, we should mainly focus on the marginal changes in competition in the dairy products market. We expect that with the achievement of the RMB100 billion sales target in 2020 and pressure from high raw milk costs, competition between Yili and Mengniu will become less intense, but we need to pay attention to the short-term impact of the NCP epidemic on the industry.

**The dairy products category has been affected by the NCP epidemic.** For dairy products, consumption during the Spring Festival period accounts for a large proportion of annual sales. For manufacturers, the products prepared for the Spring Festival have generally been shipments to distributors in the fourth quarter of last year, and they have relatively less inventory pressure. Before January 23, distributors also delivered a considerable portion of their products to retail selling points. After January 23, the Chinese government called on residents to not go outside if not necessary and not to visit other people, resulting in a sharp decline in demand for products prepared for the Spring Festival. After the first 2-3 months of its shelf life, dairy products can only be sold at discount. At present, retailers and distributors are under great pressure, and manufacturers will be impacted in 1Q2020 and 2Q2020. After the epidemic, manufacturers need to help destocking in channels. Manufacturers may experience loss in sales and share more promotion expenses with distributors and retailers. During the current special period, manufacturers are also doing their best to help distributors through difficulties. For example, Mengniu recycled the goods of its distributors then donated them to stricken civilians, which not only sends important nutritional supplements to doctors, patients and people in stricken areas, but also lowers distributors' inventory level. As milk is an important nutritional supplement, and some studies indicate that milk is favorable for enhancing people's immune system. After the epidemic outbreak, consumer demand for milk even increased. Fortunately, dairy companies can sell products to consumers through online channels including e-commerce and fresh foods e-commerce, which have not been shut down by the government. After the epidemic ends, accumulated channel inventory needs discounts to clear out; market competition may increase in the short term. In the long run, the dairy products market still has promising prospects, as consumers fully realize the benefits to their immune system and health during the epidemic.

## Soft Drinks

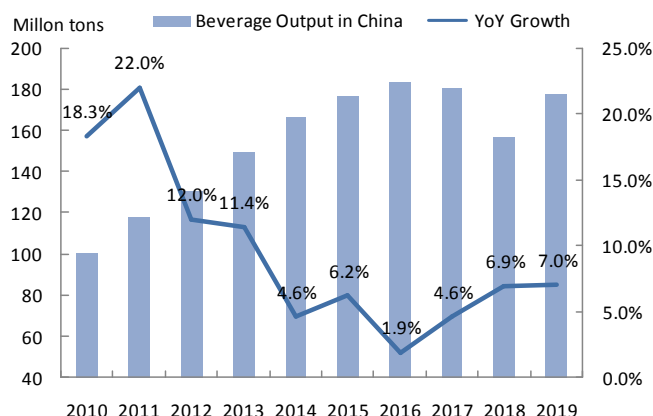
**China's soft drinks market maintained growth momentum in 2019.** According to the National Bureau of Statistics, in 2019, China's beverage output increased by 7.0% YoY, maintaining the momentum of recovery growth. In 2019, China's retail sales of beverages above designated size rose by 10.4% YoY, which notably outgrew total retail sales of enterprises above designated size. The essence of beverages is to satisfy consumer enjoyment, convenience needs (convenience to quench thirst) and functional needs (functional drinks and coffee, etc.). Due to richer consumption scenarios and improved consumer health awareness, bottled water has not only become the largest drinks category, but has also maintained a rapid growth rate. Except for bottled water, soft drinks generally contain sugar and food additives, which can generate a pleasant feeling to consumers and make them addictive. Although the preference for sugar is an evolved preference, consumers generally realize that excessive consumption of sugary soft drinks is not good for their health, so no sugar and small packaging have become a new trend. However, because consumers have both rational and emotional thinking, it is often challenging to balance long-term benefits with short-term benefits. Therefore, sugary soft drinks will not be completely abandoned, as the pleasure generated by sugar intake is an important reason and motivation (consumers may not even realize) for consumers to buy soft drinks repeatedly. Sugar-free beverages have to include unique flavors and mouth feelings (such as bubble taste), otherwise they are no different from drinking bottled water. Adding sugar substitutes has become the best choice for many beverage products to satisfy both health and taste concerns. Impulse consumption of soft drinks accounts for a large proportion, so small retail selling points (convenience stores and grocery stores, etc.) will continue to be important sales channels for soft drinks. Consumers, especially in high-tier cities, have shown more preference for fresh products and convenience stores with sophisticated cold-chain transportation is increasingly expanding and chilled tea, milk tea, and coffee products are becoming more popular.

**Figure-28: Retail Sales: Beverages Above Designated Size YoY Growth**



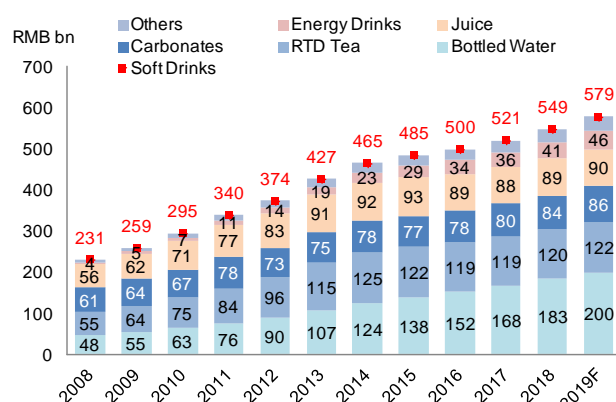
Source: National Bureau of Statistics of the PRC, Guotai Junan International.

**Figure-29: Beverage Output in China & YoY Growth**



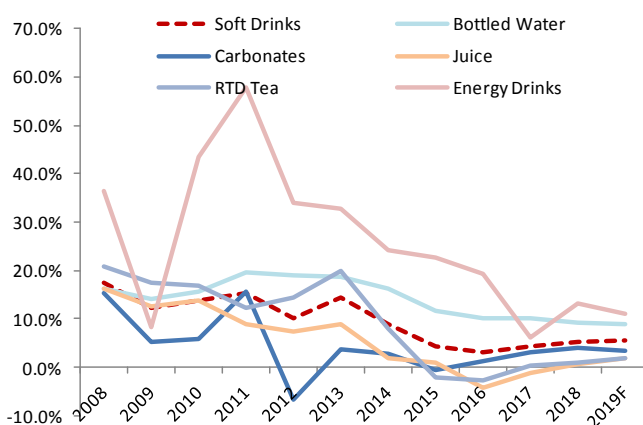
Source: National Bureau of Statistics of the PRC, Guotai Junan International.  
Note: According to National Bureau of Statistics in China, the statistical standard of output may change. The growth rates are calculated according to comparable caliber.

**Figure-30: Retail Sales Value of Soft Drinks in China**



Source: Euromonitor, Guotai Junan International.

**Figure-31: Retail Sales Value Growth of Soft Drinks in China**



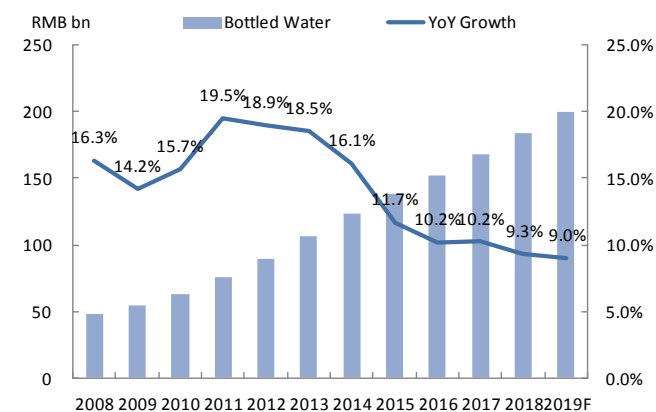
Source: Euromonitor, Guotai Junan International.

**Market concentration of the overall soft drinks market is low, but concentrations in sub-sectors are high.** Due to many sub-sectors in the soft category, there are basically no companies leading in every sub-sector of soft drinks in China, mainly due to differences in capabilities and fixing consumer brand recognition, results in relatively low concentration of the soft drinks industry. However, in each sub-sector, due to the obvious homogeneity, the degree of concentration is high. At present, China's soft drinks consumption has reached a relatively high level, and per capita consumption is expected to rise slowly, mainly driven by bottled water. The growth drivers of enjoyment drinks such as carbonated drinks, fruit juices and RTD tea mainly come from product mix upgrades. Although the number of consumers aged 10-20 is declining, the retention of soft drinks consumption habits among consumers aged 20-30 will underpin the development of the soft drinks industry.

## Bottled Water

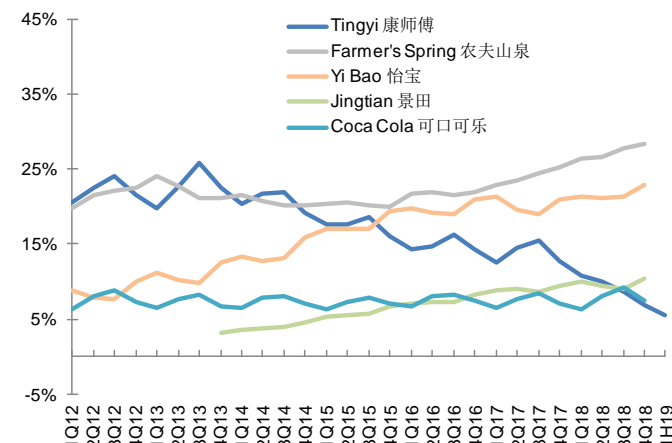
**Bottled water is expected to maintain rapid growth.** Bottled water has become the biggest product in the soft drinks category, and its market size is expected to reach RMB200 billion in 2019. Bottled water meets consumer convenience and health needs. Due to the accelerated pace of life and concerns about water quality, bottled water has gradually become the main drinking water for many households, and even the source of water for cooking. Bottled water priced at RMB2 has replaced bottled water price at RMB1 and has become mainstream in the bottled water market. Nongfu Spring and Yibao have dominated the bottled water priced at RMB2 market, as a result, other manufacturers are trying to continue to upgrade to RMB3. In order to make consumers accept the premium bottled water priced at RMB3, most bottled water priced at RMB3 is mineral water, which is extracted from famous mountains or lakes in China, such as Tingyi's Hanyangquan (涵养泉) and Yili's Inikin. We have noticed that consumers are paying more attention to water quality, and online sales of high-end foreign bottled water such as Perrier and S.Pellegrino have experienced explosive growth. Near-water drinks such as sparkling water and soda water in 2019 performed well. In 2020, more manufacturers have paid attention to sparkling water and soda water. We expect that China's bottled water will maintain a rapid growth rate, and the proportion of high-end water will continue to increase.

Figure-32: Sales Value of Bottled Water in China



Source: Euromonitor, Guotai Junan International.

Figure-33: Bottled Water Market Share by Volume



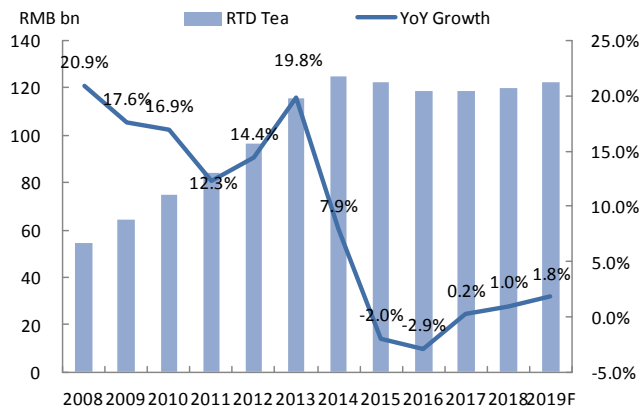
Source: Nielsen, Guotai Junan International.

## RTD Tea

**The new categories growth made up for the retreat of old categories.** In terms of sales value, RTD tea is still the second largest category in the soft drinks market. Herbal tea category sales continued to decline after reaching its peak, dragging down overall performance of RTD tea. However, RTD tea excluding herbal tea and milk tea maintained a high growth trend in 2019, mainly due to the rise of new categories. We have noticed that lemon tea and juice tea maintained strong growth in 2019 and became larger categories. Driven by Vita Lemon Tea, the growth rate of the lemon tea significantly outperformed other RTD tea categories. Encouraged by the great success of Vita Lemon Tea and its high profit margin, many brands launched their own lemon tea products, hoping to gain more market share of RTD tea and to follow the trend of consumption upgrade. We believe that due to its strong brand power and product power, Vitasoy will maintain its leading position in the lemon tea market. Juice tea is also growing rapidly. For example, Meco Juice Tea launched by Xiangpiaopiao achieved sales of RMB770 million in 3Q2019, up more than 1000% YoY. Sugar-free has also been an important trend in RTD tea, and major brands have launched sugar-free products. Ran Tea (燃茶) of the emerging brand Yuanqi Senlin mainly launched healthy sugar-free products and has won many consumers.

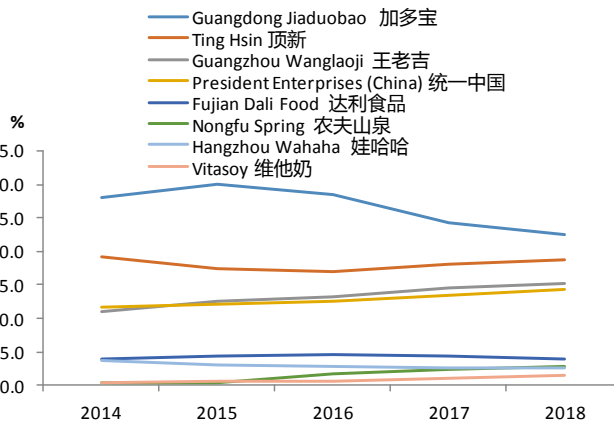
For now, new-style tea shops (such as Hey Tea and Nayuki) have limited the impact on RTD tea as their price discretion is large. We have also noticed that there is a large gap in the market between RTD tea priced at RMB3-6 and freshly-made tea priced at RMB15-30. UPC has launched chilled RTD tea, Refreshing Tea. In the market of RTD tea, excluding herbal tea, Tingyi and UPC are the leading brands, but under the challenge of Nongfu Spring's Tea π, their market share has shrunk significantly.

Figure-34: Sales Value of RTD Tea in China



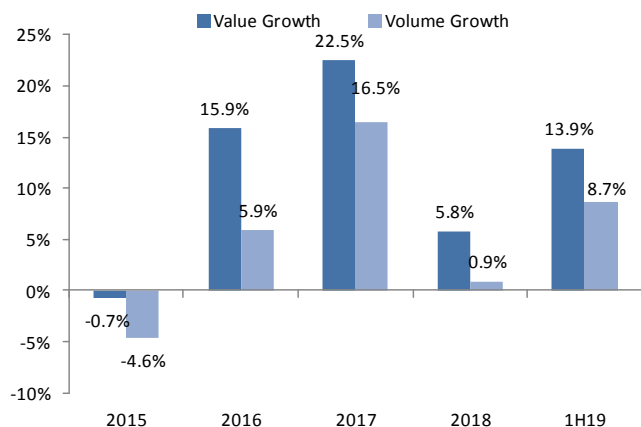
Source: Euromonitor, Guotai Junan International.

Figure-35: RTD Tea Market Share by Value



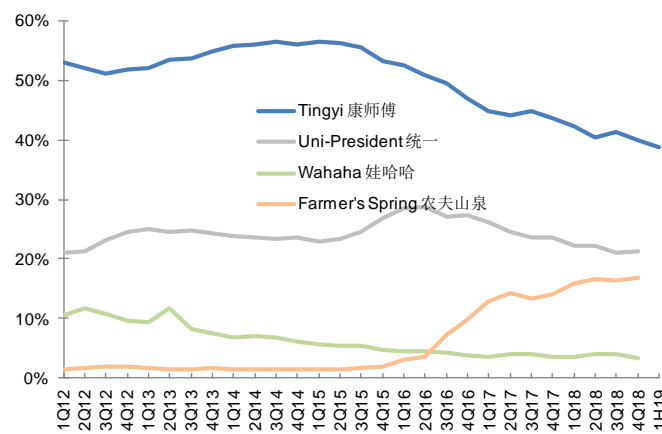
Source: Euromonitor, Guotai Junan International.

Figure-36: Sales Volume Growth and Sales Value Growth of RTD Tea (excluding Traditional Chinese Herbal Tea Drinks and Milk Tea)



Source: Nielsen, Guotai Junan International.

Figure-37: RTD Tea (excluding Traditional Chinese Drinks and Milk tea) Market Share by Value



Source: Nielsen, Guotai Junan International.

## Carbonated Drinks

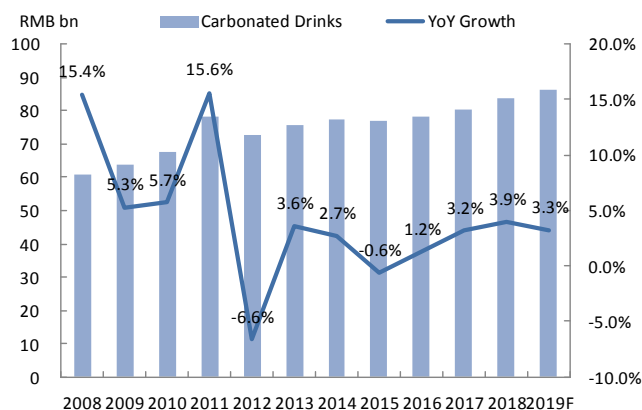
**The mature but growing carbonated drinks market has become more dynamic.** More customers have reaccepted carbonated drinks with the launch of more low-sugar products and small packaged products; carbonated drinks have maintained a momentum of recovery in 2019. The carbonated drinks market is basically monopolized by Coca-Cola and Pepsi, and Coca-Cola has an obvious leading advantage. The carbonated drinks market has rational competition, and basically no large-scale price wars have happened over last few years. Both Coca-Cola and Pepsi have good profitability. As the leader of China's carbonated drinks market, Coca-Cola is committed to leading the consumption upgrade of the industry by introducing more low-sugar products and small packaged products. Where China Foods is responsible for the sales of Coca-Cola's products, slim cans account for 17% of its total sparkling products sales, and PET 500ml has replaced 90% of PET 600ml sales, resulting in indirect price hikes. In addition, its sugar-free series and fiber + series performed well and contributed more sales. The recovering carbonated drinks market has attracted new entrants to cut into the market. The cutting-edge domestic brand Yuanqi Senlin (元气森林) tapped into the market with its diversified sugar-free products, which achieved rapid market share expansion by penetrating into convenience store channels first. "Hankou No. 2 Factory" re-emerged from the popularization of Guochao (literally the "national hip"), with soft drinks



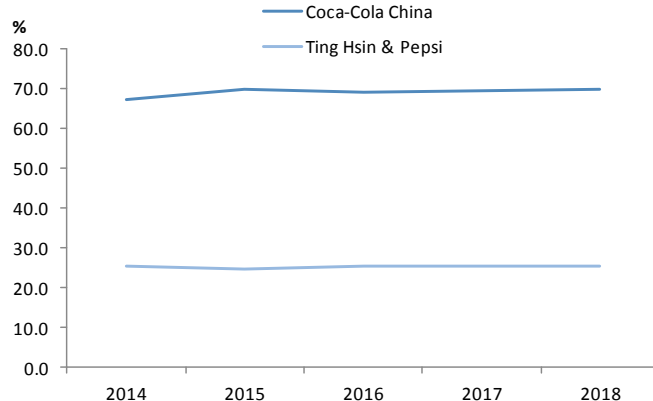
launched by them having become new trendy products. We believe that carbonated drinks have a unique bubble taste. This category is difficult to be replaced, and the product has large extension potential. Coca-Cola has strong advantages of R&D, marketing and distribution, which can seize the opportunity of consumption upgrade in the carbonated drinks industry.

**Figure-38: Sales Value of Carbonated Drinks in China**

**Figure-39: Market Share by Value in Carbonated Drinks Market**



Source: Euromonitor, Guotai Junan International.



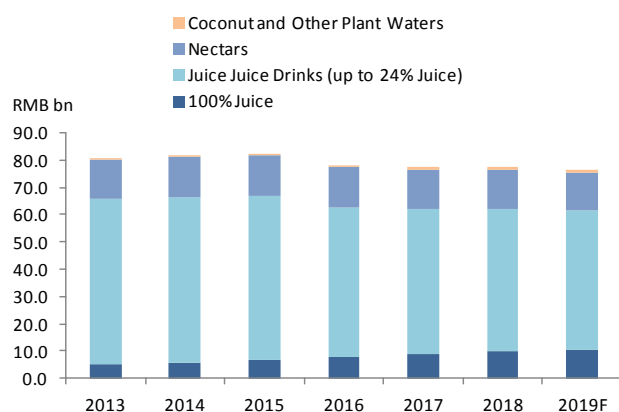
Source: Euromonitor, Guotai Junan International.

## Juice

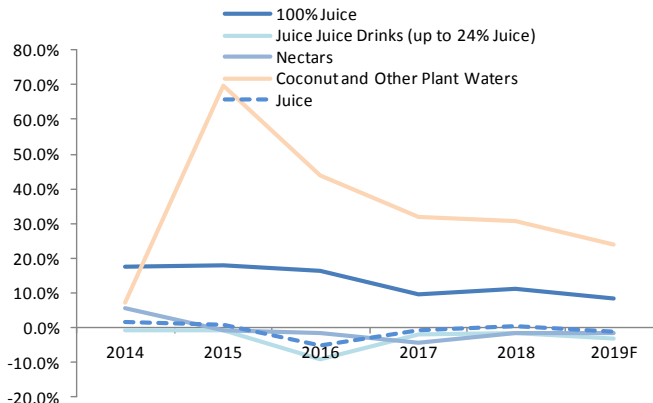
**Growth of the juice market remained relatively weak, and concentrated juice has become a trend.** According to Euromonitor, juice is still the third largest soft drinks category in China, and diluted fruit took the most share. However, because diluted juice includes added sugar and food additives, they are gradually being abandoned by consumers. In recent years, diluted juice sales have continued to decline, but the healthier 100% fruit juice drinks including Not From Concentrate (NFC) and From Concentrate (FC) have seen much stronger growth. The diluted fruit juice market is basically monopolized by Coca-Cola, Tingyi and UPC, but their diluted juice sales all met headwinds. But in 2019, Nongfu Spring's NFC juice achieved good sales performance. Coca-Cola's Minute Maid will also upgrade towards high-concentration juice drinks. In addition, due to the short shelf life of NFC juice, many small regional brands have seized the opportunity to tap into the NFC juice market. The juice market is not only upgrading toward NFC, but even to High Pressure Processing (HPP) juice. HPP juice undergoes a non-thermal process that allows fruits and vegetables to attain longer shelf life while preserving nutrients at a maximum level. Overall, rationality in juice is weaker than other soft drink categories, which is more likely to be replaced.

**Figure-40: Sales Value of Juice in China**

**Figure-41: Sales Value Growth of Juice in China**



Source: Euromonitor, Guotai Junan International.

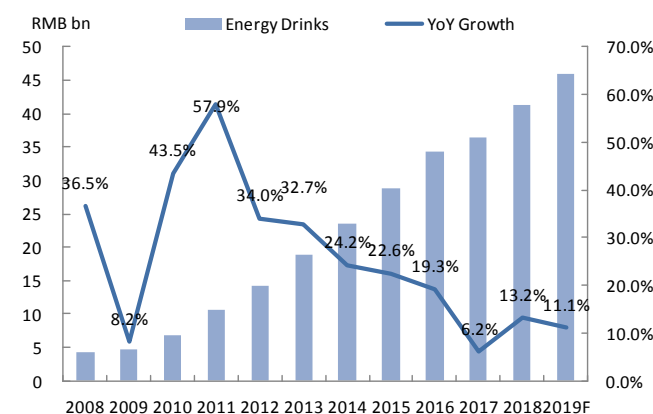


Source: Euromonitor, Guotai Junan International.

## Energy Drinks

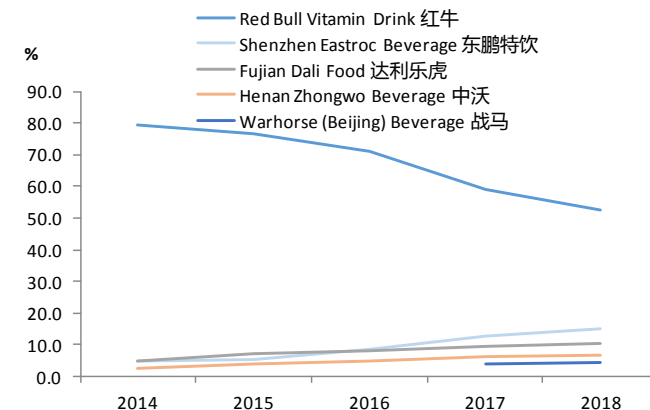
Energy drinks has been the fastest growing category, but competition has become more fierce. Benefiting from rapidly increasing market penetration, increasing private car population and sports activities, energy drinks have become China's fastest-growing beverage category over recent years. However, as the penetration rate has gradually become saturated, the growth rate of energy drinks has slowed down. In the past, China Red Bull dominated energy drinks market, but with the dispute over the trademark of Red Bull between China Red Bull (Reignwood Group) and Thailand Red Bull, sales of Red Bull in China were greatly affected, leaving more market share for other domestic energy drinks brands. The domestic energy drinks brands represented by Estroc Beverage (东鹏特饮) and Dali Hi-Tiger (达利乐虎) have already grasped a considerable part of market share originally owned by China Red Bull. Reignwood Group has also launched its own brand of energy drinks, War Horse, as a plan B. Energy drinks products are impressively profitable due to its strong functionality and high entry barriers (health care product license). Hi-Tiger has also been the main driving force for Dali's sales for the last several years. Competition in the energy drinks market has become more intense, which is reflected in competition for channel resources and advertising resources. Energy drinks brands sponsored more sports events and e-sports championships. In the future, due to the limited consumption scenarios of energy drinks which can be replaced by other refreshing beverages such as coffee, sports drinks and tea, we expect growth of energy drinks to further slow down.

Figure-42: Sales Value of Energy Drinks in China



Source: Euromonitor, Guotai Junan International.

Figure-43: Market Share by Value in Energy Drinks Market



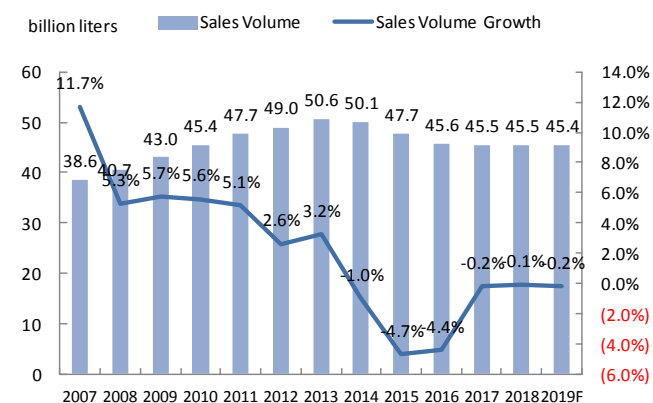
Source: Euromonitor, Guotai Junan International.

The NCP epidemic has affected outdoor consumption, which will weigh on soft drinks sales in 1H2020. After the novel coronavirus outbreak, the Chinese government called on civilians to not go outside if not necessary, which significantly hurt outdoor consumption of soft drinks. In addition, soft drinks consumption for dinners and parties during the Spring Festival fell sharply. Although, generally, the first quarter is the off-season for soft drinks, if the epidemic lasts longer, channel inventory may pile up with older shelf life products, and inventory pressure will be gradually transferred to upstream manufacturers, who may need to pay more towards promotion expenses to help channel destocking. However, referring to the experience during SARS, the epidemic is likely to end before summer and this will not affect the peak season sales of soft drinks.

## Beer

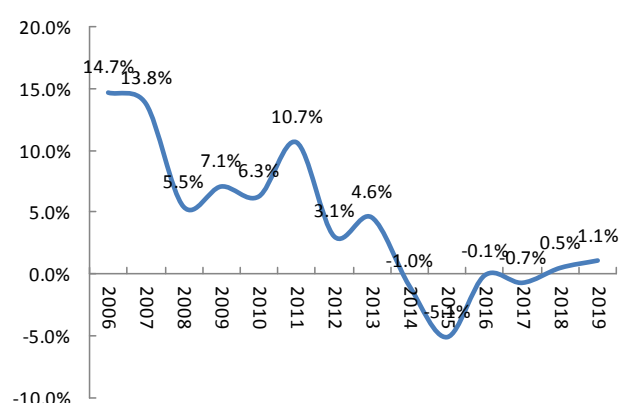
**Per capita consumption of beer will struggle to recover.** Beer is essentially to satisfy consumers' enjoyment and social needs. In terms of sales volume, beer is China's largest alcoholic beverage. In terms of sales value, it is lower only to baijiu. Chinese beer consumption continued to decline after reaching its peak in 2013. In 2017, it reached bottom, with the annual change not exceeding 1%. The decline in beer consumption in China has mainly been due to the aging population, fewer consumption scenarios, stricter punishment on drink driving, baijiu substitutes and fewer migrant rural workers. China's per capita consumption of beer has currently stayed at 32.6 liters/year, which is far behind the traditional beer consumption rate of European countries and the United States, but it is higher than the world average. Generally speaking, per capita beer consumption does not have much correlation with the level of economic development. For example, per capita beer consumption in Vietnam and Laos, which have a poor economic development level, is also higher than that in China. The main factors that determine the per capita consumption of beer are consumption habits and consumption scenarios. Unlike soft drinks, the per capita beer consumption of young people has not exceeded that of their parents when they were young. With the continued deterioration of aging, China's per capita beer consumption will struggle to pick up again.

**Figure-44: Retail Sales Volume& YoY Growth of Beer in China**



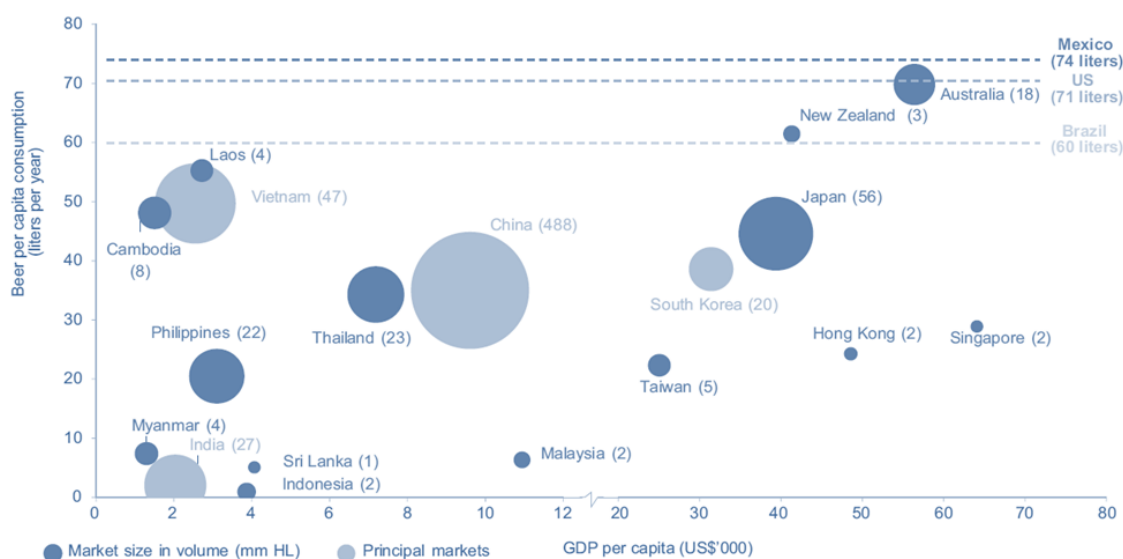
Source: Euromonitor, Guotai Junan International.

**Figure-45: YoY Growth of Production Volume in China**



Source: National Bureau of Statistics of the PRC, Guotai Junan International.  
Note: YoY Growth of production volume of brewers above a designated size.

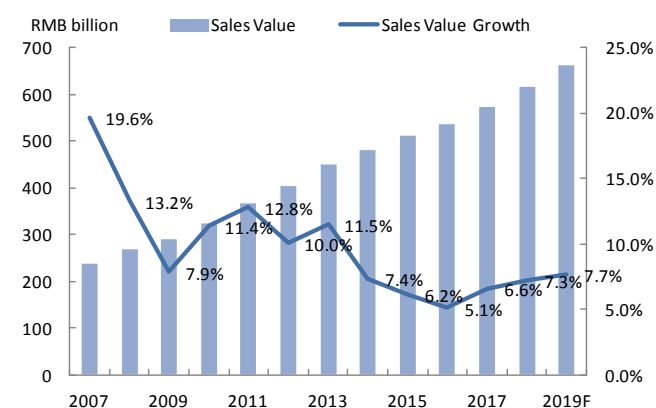
**Figure-46: Per Capita Consumption of Beer**



Source: GlobalData.

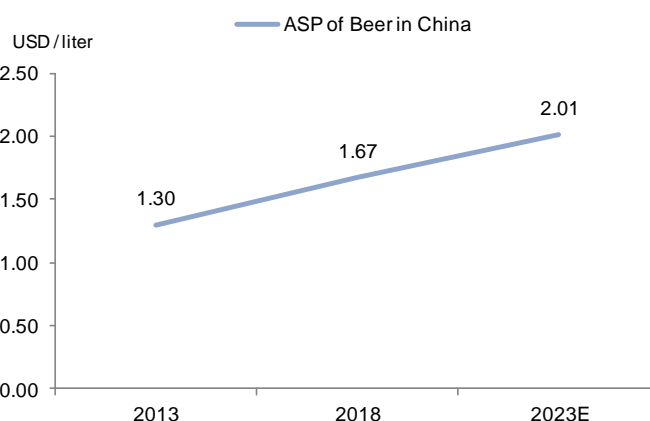
**Product structure upgrade has become the main driving force for the beer industry.** From 2013 to the present, the main driving force for the beer industry is the increase in ASP underpinned by the improvement in product structure and price lift. According to GlobalData, from 2013 to 2018, the ASP of beer in China increased by 28.5% and the growth rate of beer price outperformed corresponding CPI. In 2018, due to the significant increase in raw material costs, the beer industry has witnessed widespread price hikes, but we believe that due to perfect market competition, the beer market has less chance to raise price directly, and product structure improvement will become the major driver for growth of ASP. With the new generation of consumers becoming mainstream consumers of beer, low-priced beers with a light taste cannot meet their needs. High-end beer can satisfy the diversified needs of customers for taste, concentration and variety. Today in China, there are fewer scenarios where people compete through drinking beer, and drinking better has become the consensus. High-end beer can adapt to more consumption scenarios. According to GlobalData, the volume contribution of China's premium and super premium beer sales rose from 10.9% to 16.4%, and it is expected to continue to rise to 19.9% by 2023. The value contribution of China's premium and super premium beer sales exceeded 51% in 2018, and it is expected to increase to 60.9% in 2023. The ASP of China's major beer brands has increased significantly, becoming the main driver of for revenue growth. The critical sales channel of high-end beer is nightlife channels, but in 2019, the Chinese government's anti-pornography and anti-criminal movement weighed on nightlife channels, and it also affected sales of beer in nightlife channels. The ASP of beer in China is much lower than the world average and significantly lower than countries with similar GDP per capita. In the long run, the increase in ASP is still the main driving force for future industry growth.

**Figure-47: Retail Sales Value & YoY Growth of Beer in China**



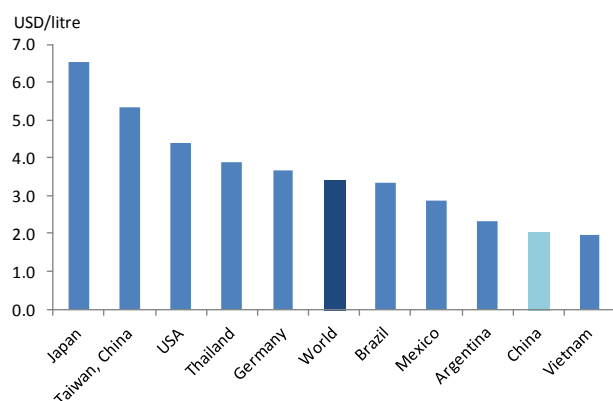
Source: Euromonitor, Guotai Junan International.

**Figure-48: ASP of Beer in China**



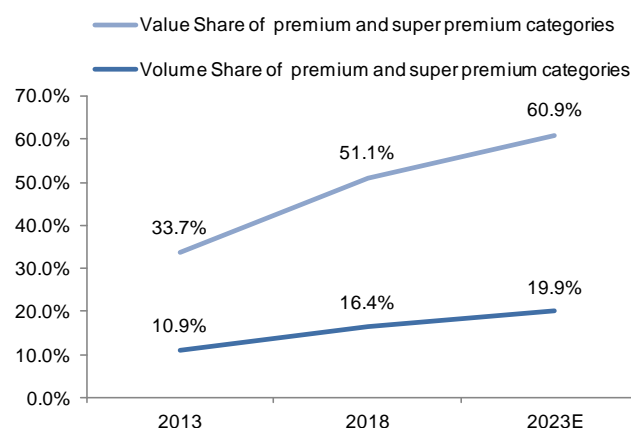
Source: GlobalData, Guotai Junan International.

**Figure-49: ASP of Beer in the Different Countries**



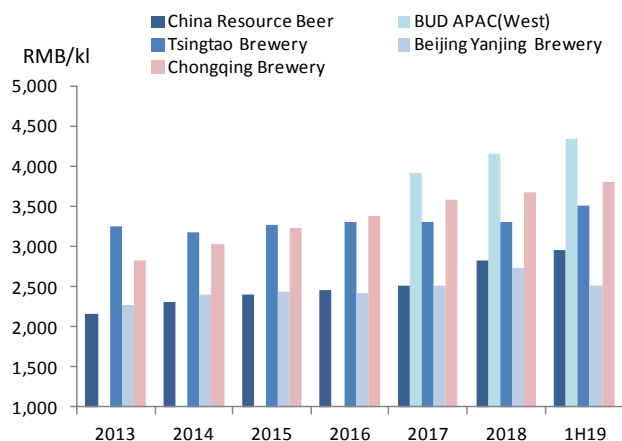
Source: Euromonitor, Guotai Junan International.

**Figure-50: Share of Premium and Super Premium Categories in China**



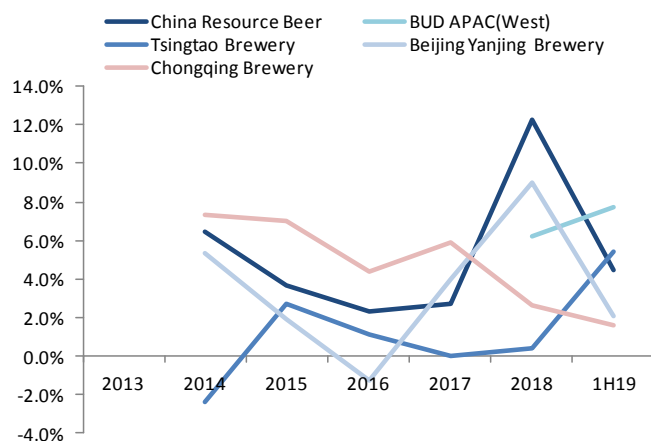
Source: GlobalData, Guotai Junan International.

Figure-51: ASP of Leading Beer Players



Source: the Companies, Guotai Junan International.  
Note: BUD APAC (West)'s revenue is mostly generated from China.

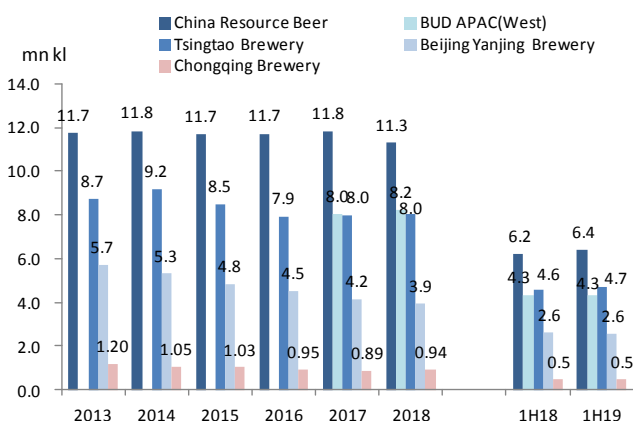
Figure-52: ASP Growth of Leading Beer Players



Source: the Companies, Guotai Junan International.  
Note: BUD APAC (West)'s revenue is mostly generated from China.

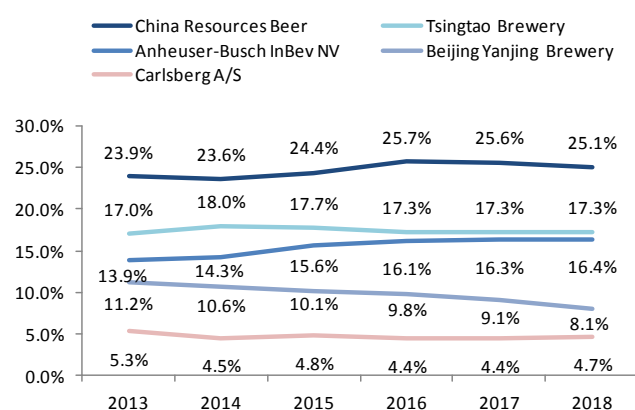
**The beer market is highly concentrated.** As the beer industry is an asset-heavy and capital-heavy industry, the integration of China's beer market was completed through acquisitions many years ago. Due to the homogenization of beer products and the obvious scale effect, in China where lager beer is the mainstream, small beer manufacturers are struggling to survive. In terms of sales, China Resources Beer (CRB) firmly maintained the top position in China's beer industry, followed by Tsingtao Beer and Anheuser-Busch InBev ("AB InBev" or "BUD"). According to Euromonitor, in terms of sales volume, the top 3 companies in China's beer market have market share of 58.8% in 2018. As AB InBev's ASP is higher, in terms of sales value, AB InBev's market share exceeds that of CRB. Due to the short distribution radius of the beer products and historical evolution, the competition landscape in each province is different, and the leading manufacturers are also different. For example, CRB dominates in Liaoning, Sichuan, Anhui and other provinces, Tsingtao dominates in Shandong, Shaanxi and other provinces, AB InBev dominates in Jiangxi and Fujian and other provinces, and Yanjing leads in Beijing and Guangxi. Generally speaking, competition intensity in provinces with single monopoly is relatively low, while competition is more intensified in provinces where market share of leading brands is close. The base market is also the main profit-generating source for beer manufacturers and the pioneering place for upgrading product structure. In the future, we don't think the industry landscape will change much, but brand influence of premium beer brands and the longer shipment radius will make it easier to break through regional restrictions. And market concentration will be more difficult to increase in the future, as the remaining small manufacturers mainly operate differentiated non-lager beer.

Figure-53: Sales Volume of Leading Beer Players



Source: the Companies, Guotai Junan International.  
Note: BUD APAC (West)'s revenue mostly generated from China.

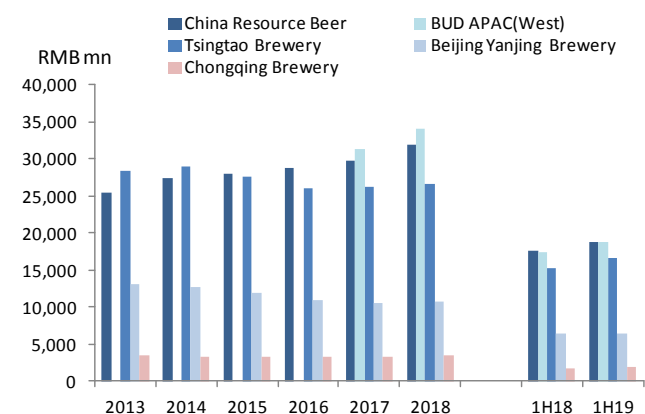
Figure-54: Market Share in terms of Sales Volume in the Beer Market



Source: Euromonitor, Guotai Junan International.



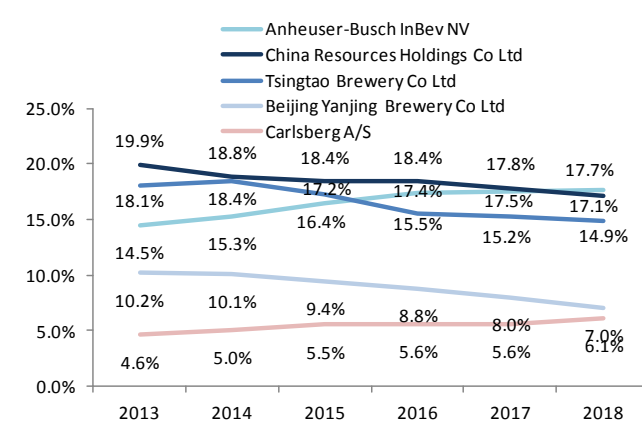
Figure-55: Revenues of Leading Beer Players



Source: the Companies, Guotai Junan International.

Note: BUD APAC (West)'s revenue mostly generated from China.

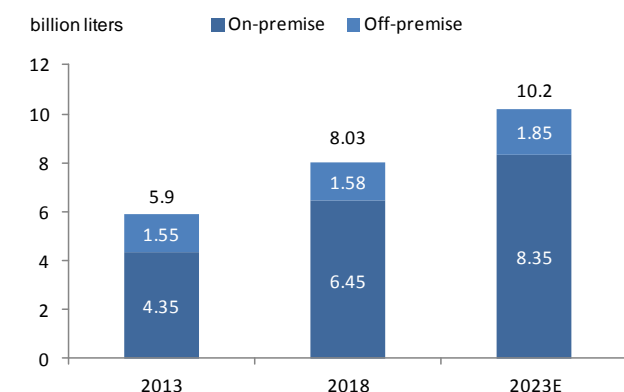
Figure-56: Market Share in terms of Sales Value in Beer Market



Source: Euromonitor, Guotai Junan International.

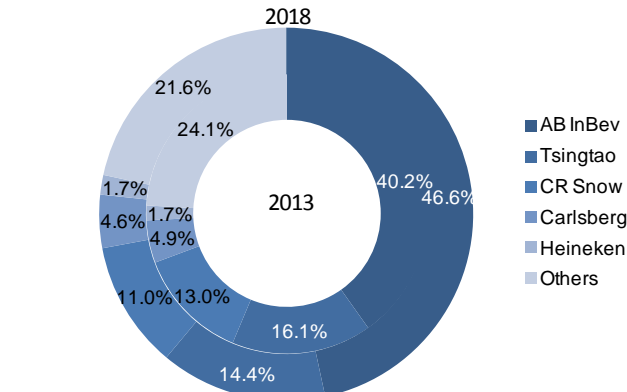
**Competition in the premium beer market will be more intense.** As beer is a typical imported product with notable characteristics of western culture, consumers are more inclined to choose international brands when consuming premium beer, resulting in foreign brands occupying a dominant position in the premium beer market in China. According to GlobalData, AB InBev grasped 46.6% market share in the premium beer market in 2018, maintaining an absolute leading position. The main brand products of Tsingtao Brewery have a premium position than the main brand products of CRB, mainly because Tsingtao Brewery originated from a brewery set up by westerners, and it is now recognized by consumers as a premium Chinese beer. Over the years, CRB's premiumization has made a slow progress as consumers have lower acceptance of its newly launched high-end sub-brands. However, as CRB has completed the acquisition of Heineken's China business, competition in China's premium beer industry will become more intense. On-premise channels (restaurants, nightlife, etc.) are the main sales channels for premium beer, accounting for 80% of premium beer sales in 2018. Sales of mainstream beer in on-premise channels accounted for only 43%. Therefore, to launch into the premium beer market, beer companies need to establish a sophisticated distribution and sales team to ensure that they can touch the relevant sales points. CRB has kicked off its 3-year plan for Heineken to fully launch in China. In order to enhance its distribution ability in the high-end market, CRB plans to raise its distributors' sales scale by (1) training existing distributors, (2) developing new distributors, and (3) recruiting other companies' distributors. Heineken will first tap into newly established selling points and avoid to head-to-head competition with existing brands in mature channels. But with sales scale expansion, head-to-head competition is unavoidable, especially during the adjustment period in nightlife channels. We believe that in the high-end market in the future, competition for distributors and sales points will become more intense.

Figure-57: Channel Breakdown of Premium and Super Premium Beer Market



Source: Global Data, Guotai Junan International.

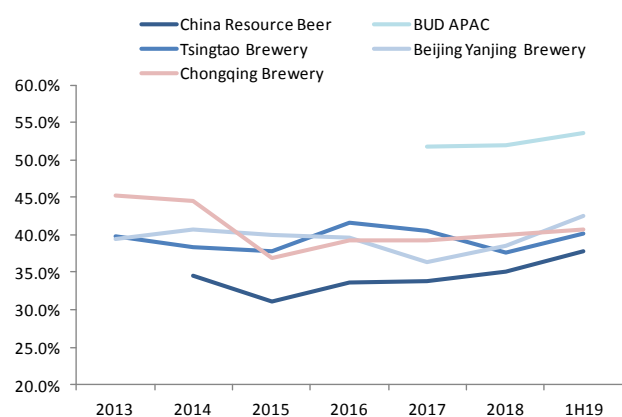
Figure-58: Market Share in terms of Sales Value in Premium and Super Premium Beer Market



Source: Global Data, Guotai Junan International.

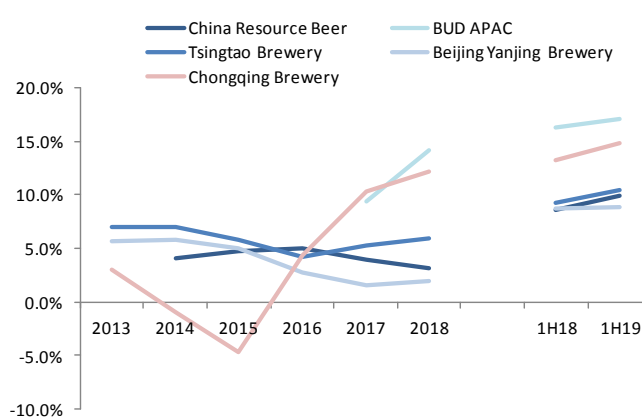
**Domestic brands have promising prospects on profitability improvement.** AB InBev's product structure shows more premium than domestic brands, reflected in the higher ASP and gross margin in its financial reports. In addition, AB InBev, as a foreign-owned beer company, has a more advanced management system and simpler government-business relations. It has advantages over state-owned beer companies in terms of integrating factories and improving production efficiency. As beer sales growth is stagnant, the main development direction for domestic brands is to improve their product structure and production efficiency, closing the discrepancy with AB InBev. CRB closed 5 breweries in 2017 and 13 breweries in 2018. We expect CRB to further close breweries in the mid-single digits in 2H2019. The number of staff in CRB has decreased from 45,600 in 2017 to 35,000 in 1H2019. Although the progress of Tsingtao in closing breweries is slower than CRB, it is also moving toward the right direction. Due to increasingly intense competition in the premium beer market, brand building has become even more critical, and we believe that beer companies have less room to save in marketing expense. But we believe that the improvement in product structure and production efficiency can greatly improve profitability of domestic beer companies. Although domestic beer companies have potential in doubling their earnings, their valuation has fully reflected that expectation. The beer industry is struggling to grow and the market is highly concentrated with relatively low intense competition, so we need to pay more attention to whether their rationality has changed significantly and whether customers have abandoned them. The good news is that consumption upgrades have reinforced their rationality.

**Figure-59: Gross Margin of Leading Beer Players**



Source: the Companies, Guotai Junan International.

**Figure-60: PAT Margin of Leading Beer Players**



Source: the Companies, Guotai Junan International.

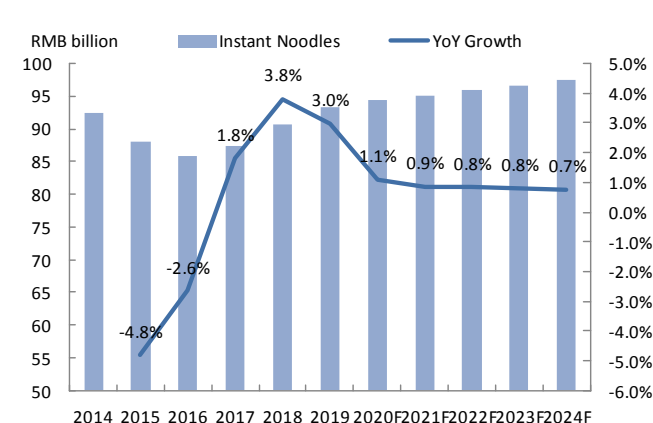
**The NCP epidemic significantly hurt the catering industry, which has weighed on beer sales in 1H2020.** After the novel coronavirus outbreak, most restaurants and bars in China have closed at their own discretion or by government instruction. On-premise channels contribute more than 50% of beer sales, which were significantly affected by the epidemic. And residents avoid going out, which lowered the purchase volume of beer. Although, generally, the first quarter is the off-season for beer, if the epidemic lasts longer, the channels inventory will pile up with older shelf-life products, and inventory pressure will be gradually transmitted to upstream manufacturers, who may need to pay more promotion expenses to help channels destock. However, referring to the experience of SARS, the epidemic is likely to end before summer and will not affect peak season sales of beer.

## Packaged Food

### Instant Foods

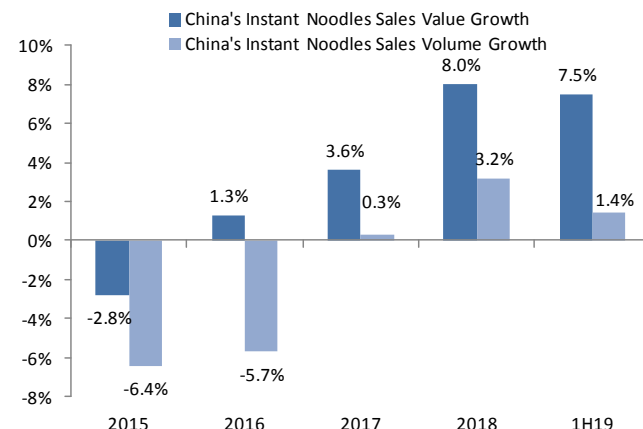
**The instant noodles industry has maintained recovery momentum with notable consumption upgrade.** Consumption of instant noodles continued to decline after 2013, due to less migrant rural workers, the increase in high-speed trains and impact of food delivery. From 2013 to 2017, the sales volume of instant noodles continuously declined, but it was bottomed out during 2018 and 2019. The expansion of student groups and the increase in the population of singles have become important forces in driving instant noodles sales. According to Nielsen data, in 1H2019, the sales volume and sales value of instant noodles in China increased by 1.4% YoY and 7.5% YoY, respectively, with an obvious trend of consumption upgrade. According to Euromonitor's forecast, instant noodles will achieve sales growth in 2019 and maintain recovery momentum, with sales reaching RMB154.1 billion. High-end and medium-end instant noodles products have performed strongly in satisfying consumers' pursuit of health and high quality, supporting the growth of instant noodles sales. In 1H2019, revenue of Tingyi and UPC in instant noodles increased by 3.7% YoY and 2.8% YoY, respectively. In 1-3Q2019, Nissin Foods' revenue in China increased 12.5% YoY (net of exchange rate effects). In 3Q2019, UPC's Soup Daren continued to achieve double-digit growth. Tingyi's market share stopped falling in 3Q2019 due to its competitive strategy against Jinmailang through price reduction in the low-end instant noodles market. In 2H2019, competition between Tingyi and Jinmailang in the low-end instant noodles market became less intense. Instant noodles manufacturers pay more attention to the layout of high-end instant noodles and have begun to test markets above RMB10. The highly monopolized instant noodle market has seen new domestic entrants, such as Lamianshuo, which has achieved rapid growth mainly because it has accurately entered the high-end instant noodles market. Tingyi's Express priced at RMB20 achieved breakthrough growth by using industry-leading low-temperature vacuum tumbling and fresh-locking technology. Instant noodles manufacturers pay more attention to container noodles to meet the convenience needs of busy consumers in cities. According to Nielsen's data, it can be seen that sales growth of container noodles is much higher than that of bagged noodles. Per capita consumption of instant noodles is not significantly correlated with the level of economic development. According to data from the World Instant Noodles Association, per capita sales of instant noodles in economically developed South Korea and economically underdeveloped Vietnam are significantly higher than those in China. The main factors that determine the per capita consumption of instant noodles are consumption habits and consumption scenarios. We believe that the growth potential of per capita consumption of instant noodles in China is limited.

**Figure-61: Retail Sales Value & YoY Growth of Instant Noodles in China**



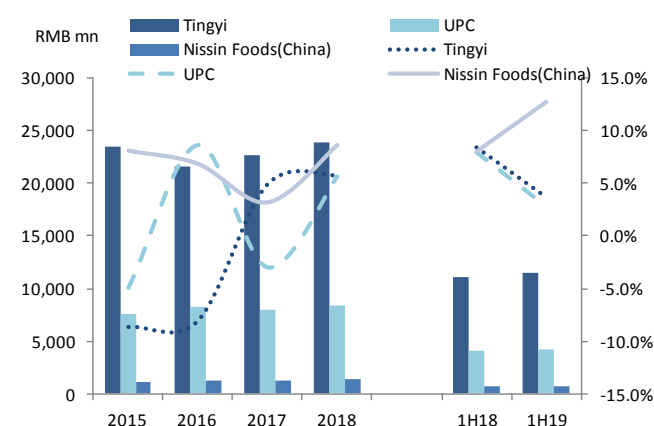
Source: Euromonitor, Guotai Junan International.

**Figure-62: Retail Sales Value Growth and Retail Sales Volume Growth**



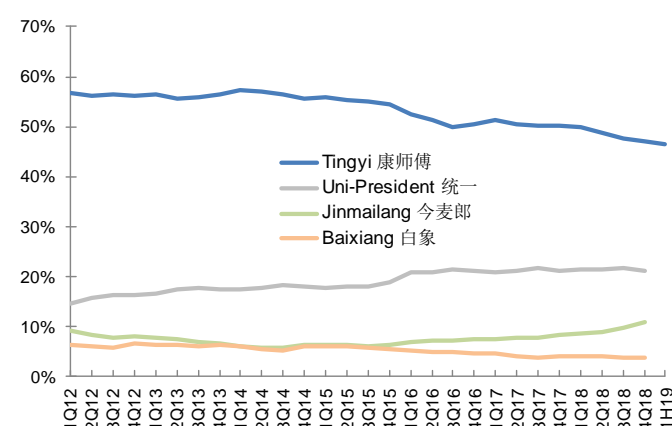
Source: Nielsen, Guotai Junan International.

Figure-63: Revenue of Tingyi, UPC & Nissin in Instant Noodles



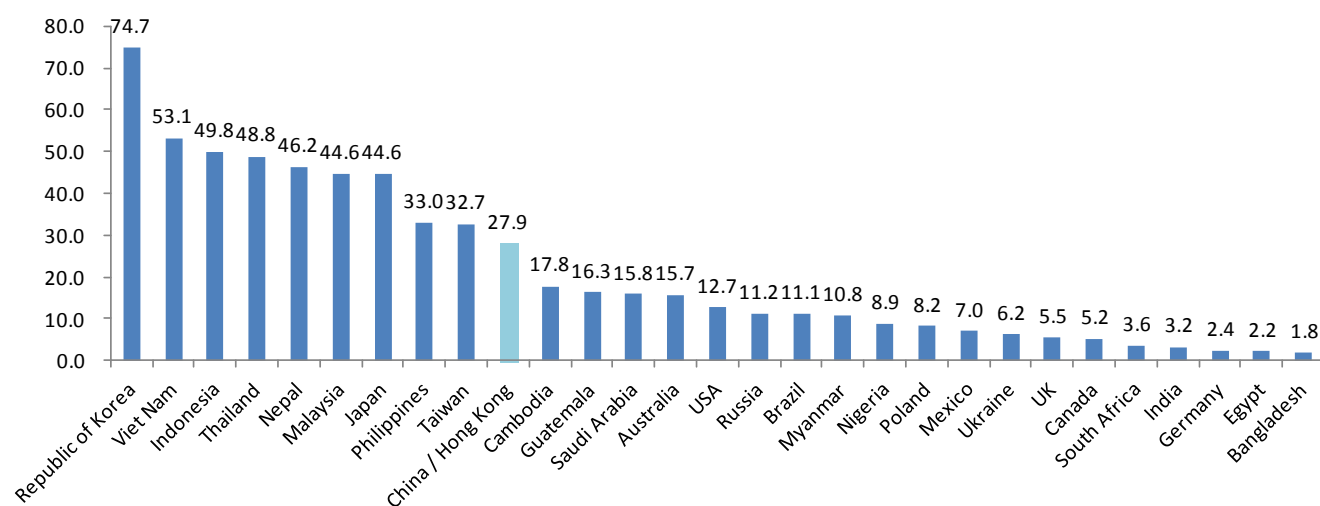
Source: Nielsen, Guotai Junan International.

Figure-64: Market Share in the Instant Noodles Market



Source: Nielsen, Guotai Junan International.

Figure-65: Per Capita Consumption of Instant Noodles



Source: World Instant Noodles Association, Guotai Junan International.

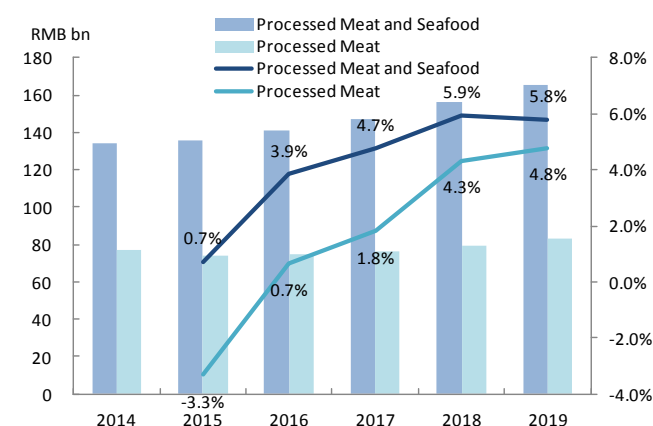
**Race track of convenience foods becomes wider.** In the past, instant noodles basically represented convenience foods, but we have seen that due to technological progress and changes in consumer taste, the race track of convenience foods has become significantly wider. 2019 was an breakthrough year of the self-heating hot pot category. Not only did companies that produce convenience foods introduce self-heating hot pot products, so did catering enterprises such as Haidilao and Xiaolongkan. Self-heating food was derived from self-heating hot pot, leading to self-heating noodles, self-heating rice, etc. Other local special flavor products have been modernized, and have won favor with many consumers. Chongqing hot and sour rice noodles and Liuzhou river snails rice noodles instant rice noodles have seen rapid growth in online sales. China's food culture has a long history. Every place has some special foods, such as Rougamo in northwest China and hot noodles with sesame paste in Wuhan. These delicious local foods will become the development direction of the convenience food industry in the future. We believe that after the end of the large-scale subsidy for food delivery, the marginal impact of food delivery on convenience foods has become smaller. As food delivery is constrained by cost, the price gap between food delivery and convenience foods will continue to widen. Moreover, the consumption scenarios of convenience foods are more diversified, and their rationality has not been greatly affected. The recent outbreak of the NCP epidemic has made the value of convenience food more prominent. With the shortage of foods after the closure of cities, convenience foods have become an important food source. Consumption upgrades in the convenience food industry will continue in the future.

## Packaged Meat

**High-temperature meat products finished bottom.** The essence of packaged meat products is to meet demand from consumers to conveniently eat meat. In China, where meat consumption is fully satisfied, the convenience attribute of packaged meat products is more prominent. High-temperature meat products (shelf stable meat) are the largest component of the packaged meat market in China. As a partner of instant noodles, high-temperature meat products and instant noodles share, to a large proportion, consumption scenarios. Packaged meat products and instant noodles experienced a period of rapid growth before 2013, but they continued to decline in the following years, mainly due to the decrease in the number of migrant rural workers and the rise in high-speed and booming food delivery. Similarly, consumers who are more health conscious have concerns about high-temperature meat products. From 2013 to 2017, the sales volume of high-temperature meat products continuously declined, which bottomed out during 2018 and 2019. The expansion of the student population and the increase in population of singles have become important driving forces for high-temperature meat product sales.

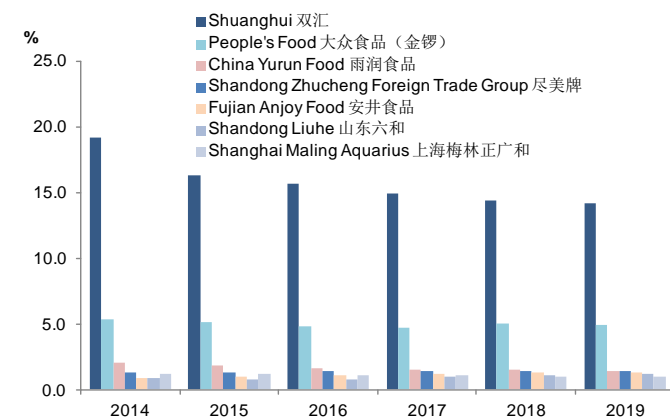
**The growth of meat products has been driven by the improvement of product structure.** Low-temperature meat products (chilled processed meat and frozen processed meat) have achieved faster growth than high-temperature meat products, mainly because low-temperature meat products retain more nutrients and less additives and win favor of the middle class, as well as low-temperature meat products having low penetration. In 2019, due to the influence of the African swine fever, the price of pork in China increased significantly, resulting in a substantial increase in the cost of meat products. We can see that under the leadership of Shuanghui, packaged meat producers have shifted the cost of raw materials downstream through price lifts. Referring to the last round of pork price cycle, Shuanghui raised the ex-factory price when pork price reached the then high point in 2016, but when pork price declined in 2016 to 2018, the price of Shuanghui's meat products was not revised down. The meat product market is basically dominated by Shuanghui which is far ahead of the second-ranked meat product brand, mainly because Shuanghui's global industrial chain layout fully mobilizes upstream and downstream resources to form a larger advantage. Looking forward to the future, we expect that the quantity of low temperature meat products will achieve moderate growth, but high-temperature meat products sales volume will struggle to regain growth. Its sales value growth is mainly driven by price increase and product structure improvement.

**Figure-66: Retail Sales Value of Packaged Meat and Seafood and Retail Sales Value of Packaged Meat in China**



Source: Euromonitor, Guotai Junan International.

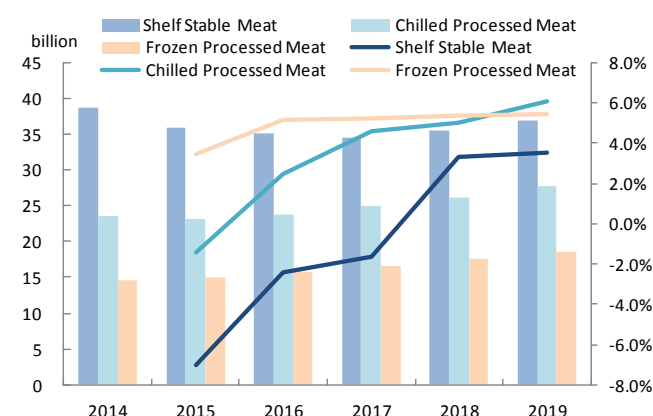
**Figure-67: Market Share in Packaged Meat and Seafood in China**



Source: Euromonitor, Guotai Junan International.

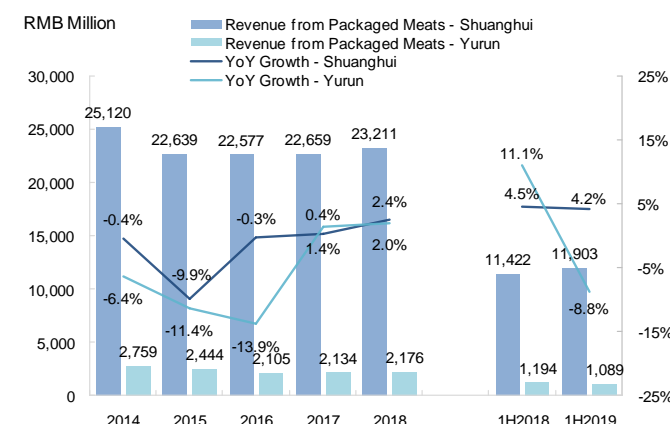


Figure-68: Retail Sales Value of Packaged Meat in China



Source: Euromonitor, Guotai Junan International.

Figure-69: Revenue of Shuanghui, and Yurun in Packaged Meat

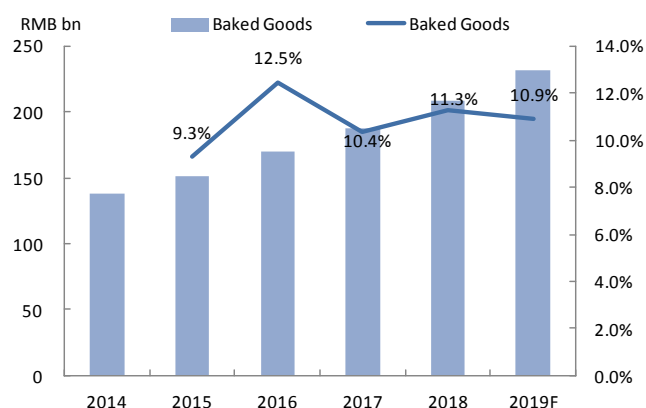


Source: the Companies, Guotai Junan International.

## Baked Foods

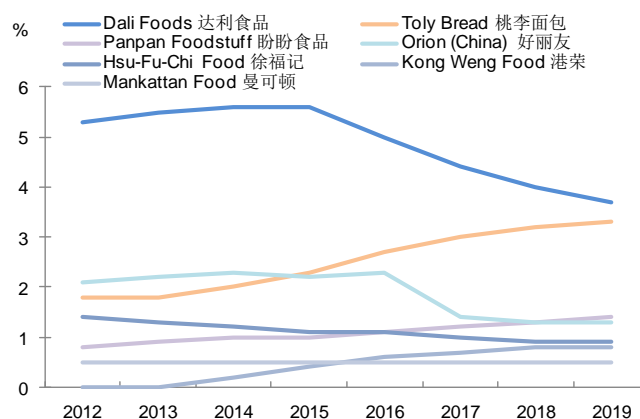
**Two business models of baked foods coexist; packaged baked food and short shelf life food.** Baked foods include a variety of products, such as bread, cakes, pastry and pies. The history of baked goods can be traced back to ancient Egyptian times and has evolved along with human history. In the west, baked food plays an important role in food and beverages, usually as a staple food. But in China, baked foods are usually eaten by consumers as snacks or for breakfast. There are two main business models in the baked food market: packaged baked food and freshly baked food. Packaged bread products are usually sold through retail channels and have the advantage of convenience. Freshly baked bread products are usually sold in bakeries and are relatively fresh and tasty. In 2018, the retail scale of China's baking industry was RMB208.9 billion, of which 73.9% was freshly made baked foods and 26.1% was the packaged baked foods. The freshly made bread industry has a large scale market, but due to the low threshold, the market is extremely fragmented and there is no national leading company. Relatively speaking, the concentration of packaged baked goods is relatively high, due to high homogeneity in packaged baked foods, which is good for the layout of national companies. Dali food has always been a leading enterprise in packaged baked foods in China, and its main product has been long shelf life bread. However, as the taste and health association of long shelf life bread is not as good as that of short shelf life bread, it is obvious that short shelf life bread is grasping market share from long shelf life bread. Toly is China's largest short shelf life bread producer, and its sales scale is gradually catching up with Dali. In order to reverse the unfavorable situation, Dali also launched its own short shelf life bread brand Meibeichen. With the help of channel advantages, Dali's short shelf life bread has grown rapidly in a short time. However, due to intensified competition in the short shelf life market, we have seen that the profitability of Toly and Dali in the short shelf life market has been affected. We also see that domestic and foreign companies have introduced more innovative baked goods, especially through online channels. In addition, the consumption of baked goods other than for breakfast is expanding. The baked food market is expected to maintain high single-digit percentage growth.

Figure-70: Retail Sales Value & YoY Growth of Baked Food



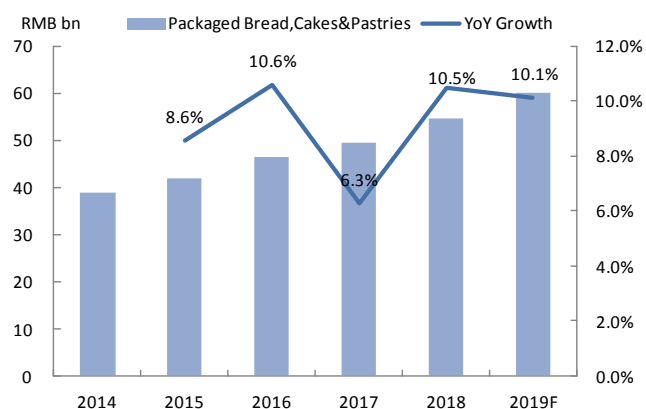
Source: Euromonitor, Guotai Junan International.

Figure-71: Market Share of Baked Food Category



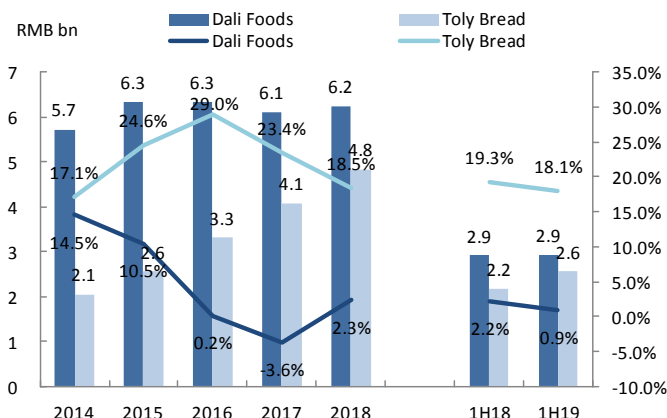
Source: Euromonitor, Guotai Junan International.

Figure-72: Retail Sales Value & YoY Growth of Packaged Bread, Cakes & Pastries



Source: Euromonitor, Guotai Junan International.

Figure-73: Revenue of Dali and Toly in Packaged Bread, Cakes & Pastries



Source: the Companies, Guotai Junan International.

21 February 2020

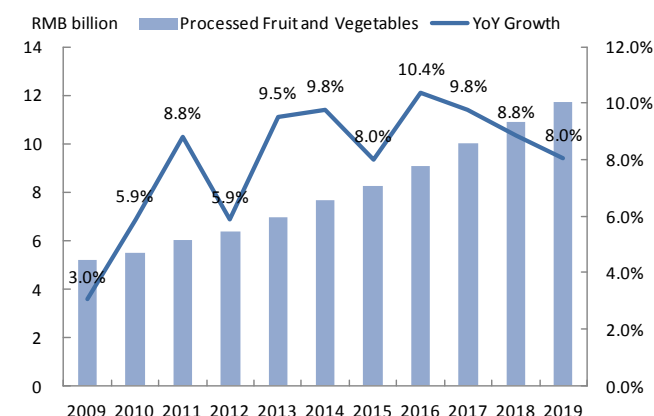
Consumer Sector-Food & Beverage 消费行业-食品饮料

Sector Report

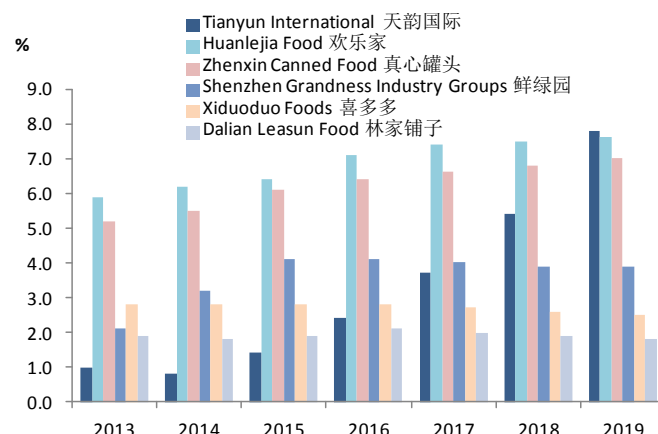
## Packaged Fruit and Vegetables

**The fresh fruit substitution effect has forced processed fruits to transition to snack foods.** With the improvement of fresh fruit distribution network and the enhancement of consumer health awareness, consumers have greater demand for fresh fruit. The substitution effect of fresh fruits on processed fruits is obviously strengthened. In addition, consumers still have misunderstandings about processed fruit products. Many consumers think that canned fruits must contain preservatives to preserve them. In fact, canned fruit products can be stored for a long time through proper sterilization and sealing. In order to cope with the substitution competition of fresh fruits, the processed fruit industry has introduced new types of fruit processed products and is striving to broaden the consumption scenarios of processed fruits. For example, Tianyun International introduced fruit ice cream and Lin Jia Pu Zi launched yellow peaches, coconut, yoghurt and sago products. Compared with staple foods such as rice, processed fruits have lower calorie content, which can attract female consumer groups with a sense of body management. China's processed fruit and vegetable industry is relatively low in concentration. With the advantages of the Hong Kong stock listing and product research and development, Tianyun International ranked first in the industry in terms of retail sales in 2019. In 1H2019, Tianyun International's private label product revenue increased by 23.2% to RMB258 million, mainly due to its expanding sales network and production capacity. Tianyun's number of distributors increased from 210 in 2018 to 277 in 1H2019. Tianyun's private label products have been listed in well-known supermarket chains, such as Auchan, RT-Mart, China Resources Vanguard, AEON, Beijing Jingkelong, Wal-Mart and Jinan Hualian. We believe that in the future, the processed fruit industry will mainly develop in the direction toward snack foods, so as to increase consumer consumption frequency and get rid of competition with fresh fruits.

**Figure-74: Retail Sales Value & YoY Growth of Packaged Fruit and Vegetables in China** **Figure-75: Market Share of Packaged Fruit and Vegetables**



Source: Euromonitor, Guotai Junan International.

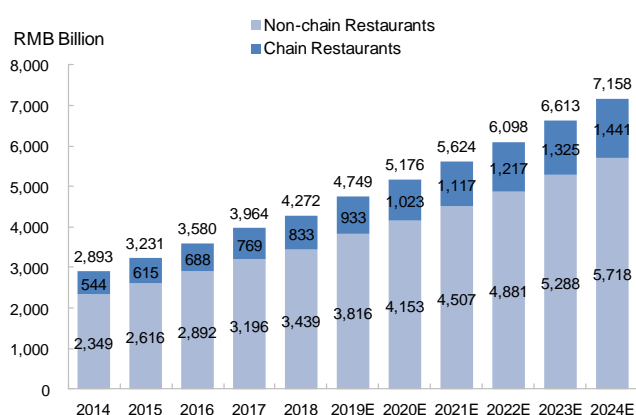


Source: Euromonitor, Guotai Junan International.

## Catering

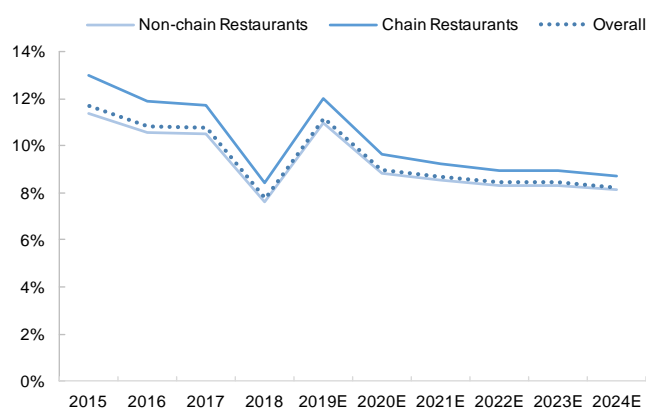
**The catering industry is improving steadily.** The catering industry integrates three formats: food, retail and service. It not only has fast food that can meet the living and nutritional needs of consumers, but also has high-grade restaurants that can meet the enjoyment and social needs of consumers. According to trends of developed countries, the catering industry will benefit most from growth of per capita disposable income. Going to a favorite restaurant has become an important way for office workers to reward their hard work. China's catering revenue increased by 9.4% YoY to RMB4,672 billion in 2019, higher than the corresponding total retail sales growth rate. Catering revenue accounted for 11.3% of total retail sales in the same period in 2019. The offline retail industry is greatly impacted by e-commerce, while the catering industry is basically unaffected, so it is popular with retail formats like shopping malls.

**Figure-76: Total Catering Revenue in China**



Source: National Bureau of Statistics of PRC, Frost & Sullivan, Guotai Junan International.

**Figure-77: YoY Growth of Catering Revenue in China**



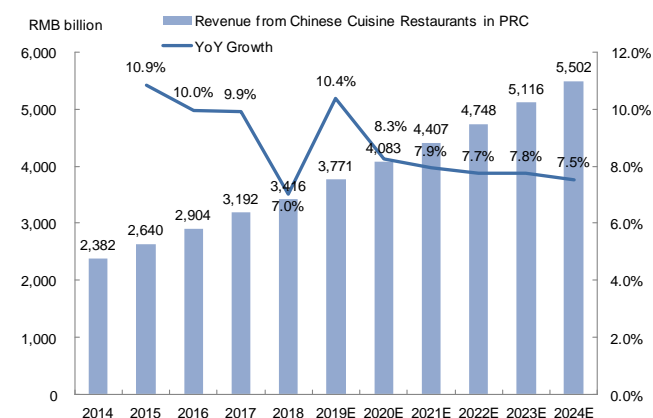
Source: National Bureau of Statistics of PRC, Frost & Sullivan, Guotai Junan International.

**Proportion of chain restaurants is expected to rise.** The catering industry has a low threshold, resulting in many participants. China has more than 10 million restaurants and about 6 million active ones, with more than 3 million restaurants opening and nearly 3 million restaurants closing every year. The proportion of chain restaurants in China is relatively low, which only accounted for 19.5% of total catering revenue in 2018. Most independent restaurants have relatively low tolerance to risk and are easily eliminated by the market. As the standardization of Chinese restaurants and supply chains become more professional, we can see that the overall size of large-scale catering enterprises continues to expand. According to Meituan Dianping, the growth rate of chain restaurants in China is significantly higher than the overall growth rate of catering revenue. The concentration of the catering industry is continuously increasing, and the influence of major catering enterprises is continuously expanding, creating a group of competitive catering giants. Emerging strong performing catering brands are also welcomed through accessible capital, with many financing channels from the primary market, and the number of successful listings of catering enterprises continues to grow. Since Xiabuxiabu and Haidilao have been listed in the Hong Kong market, Jiumaojiu (TaiEr's parent company) was also listed successfully on January 15, 2020, and has been popular in market trading.

**Chinese cuisine restaurants are the mainstream form of catering in China, but western-style fast food companies have a larger scale.** According to Frost & Sullivan, revenue of Chinese cuisine restaurants in 2018 was RMB3,450 billion, accounting for 80.0% of China's total catering revenue, and it is the mainstream form of catering in China. Although western-style fast food accounted for a relatively small amount of revenue, it has fostered China's largest catering group, Yum China. According to the Chinese Culinary Association, Yum China's revenue ranks first among all catering companies in China. As at September 30, 2019, Yum China had a total of 8,917 restaurants, of which 6,324 were KFC restaurants and 2,255 Pizza Hut restaurants. In 1-3Q2019, Yum China's revenue recorded US\$6,747 million, roughly equal to RMB46,220 million, maintaining its leading position. All top restaurants in terms of number of restaurants are western fast food brands, such as Zhengxin Chicken Steak (15,059), Wallace (12,102), McDonald's (4,256), mainly as Western fast food has a high degree of standardization, which enables restaurants to rapidly expand. Chinese cuisine is the opposite. Chinese food has rich cuisines and unique designs. It is difficult to establish uniform standards. Chinese restaurants are often too dependent on chefs, which often leads to a lack of experienced chefs in new stores, resulting in lower quality of dishes. In the future, with the more professional supply chain and the application of compound condiments, casual dining can get rid of dependence on chefs. Tai Er is the typical example. Chinese fast food standardization has

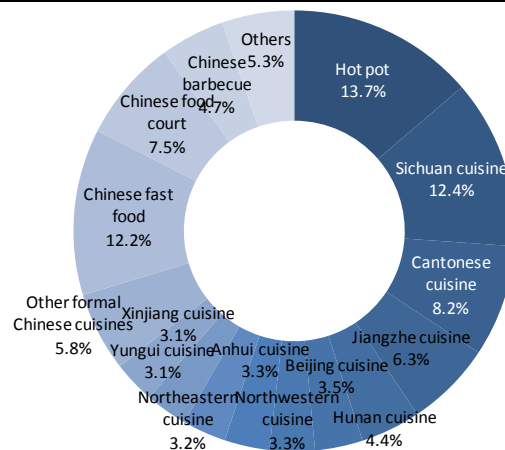
been achieved through a central kitchen. But we have not seen a national leading Chinese fast food company like KFC yet, mainly because Chinese fast food restaurants have limited dishes with specific taste, and it is easy to fall into the dilemma of expansion in other places. And as the catering industry has extremely low thresholds, Chinese fast food restaurant chains are facing competition from countless small restaurants. What is more critical is that there is a large gap regarding management capability between domestic fast food restaurants and international fast food giants. According to data from China Hospitality Association, the top five Chinese fast food restaurants are Laoxiangji (老乡鸡), Yang Guofu Spicy Hot Pot (杨国福麻辣烫), Zhang Liang Spicy Hot Pot (张亮麻辣烫), Ajisen (味千) and Kung Fu (真功夫), and their numbers of stores are still far from Western fast food brands. With the improvement of management capability, the more specialized supply chains and the application of compound condiment, we believe that the scale of Chinese restaurant companies will gradually increase.

**Figure-78: Revenue from Chinese Cuisine Restaurants in China**



Source: Frost & Sullivan, Guotai Junan International.

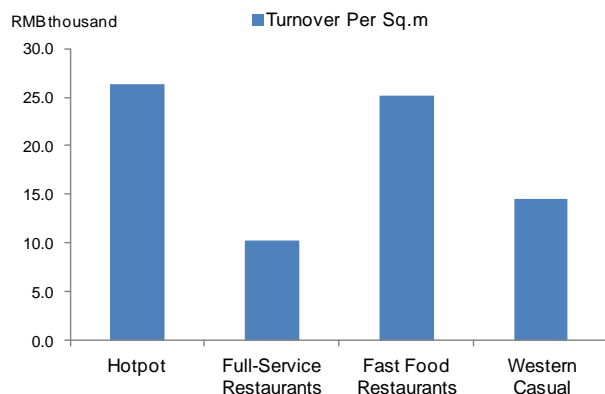
**Figure-79: Market Share among All Chinese Cuisine Styles**



Source: Frost & Sullivan, Guotai Junan International.

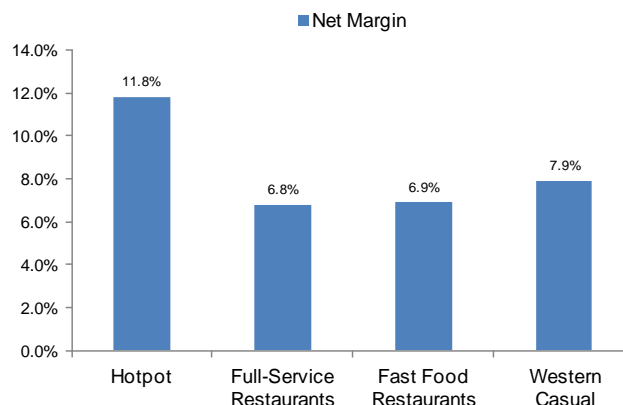
**Hot pot is king of Chinese restaurant cuisines.** According to Frost & Sullivan, in 2017, hotpot revenue accounted for 13.7% of revenue of Chinese restaurants, followed by Sichuan, Cantonese and Jiangzhe style cuisines, accounting for 12.4%, 8.2% and 6.3%, respectively. According to Meituan, hot pot was the hottest category in 2018, with the number of orders and the total consumption amount ranking first in all catering categories. According to the 2019 Chinese Catering Report, the proportion of hot pot orders increased from 15.9% in 2017 to 20.3% in 2018. In the eyes of consumers, hot pot is also a type of Chinese dinner. In 2018, per capita consumption of hot pot was RMB49, significantly higher than that of fast food, which is consistent with dinner, but hot pot is actually different from other Chinese cuisines. On the one hand, hot pot avoids dependence on chefs, has a lower technical threshold and higher gross margins, making hot pot the first choice for many entrepreneurs to tap into the catering industry. According to data from the 2019 Chinese Catering Report, revenue per sq.m and net profit margin for hot pot restaurants topped amongst all catering categories. On the other hand, the high standardization and easy-to-replicate business model of hot pot makes hot pot brands expand rapidly. Leading hot pot brands such as Haidilao and Xiabuxiabu have already controlled the upstream supply chain, and their capacity can even serve other catering companies. Xiabuxiabu, Morals Village (德庄) and Xiaolongkan are not inferior to other Chinese fast food brands in terms of number of stores. Hotpot has high per capita consumption like dinner and standardization like fast food, making it the best option in the Chinese catering industry.

Figure-80: Turnover per Sq.m of Restaurants



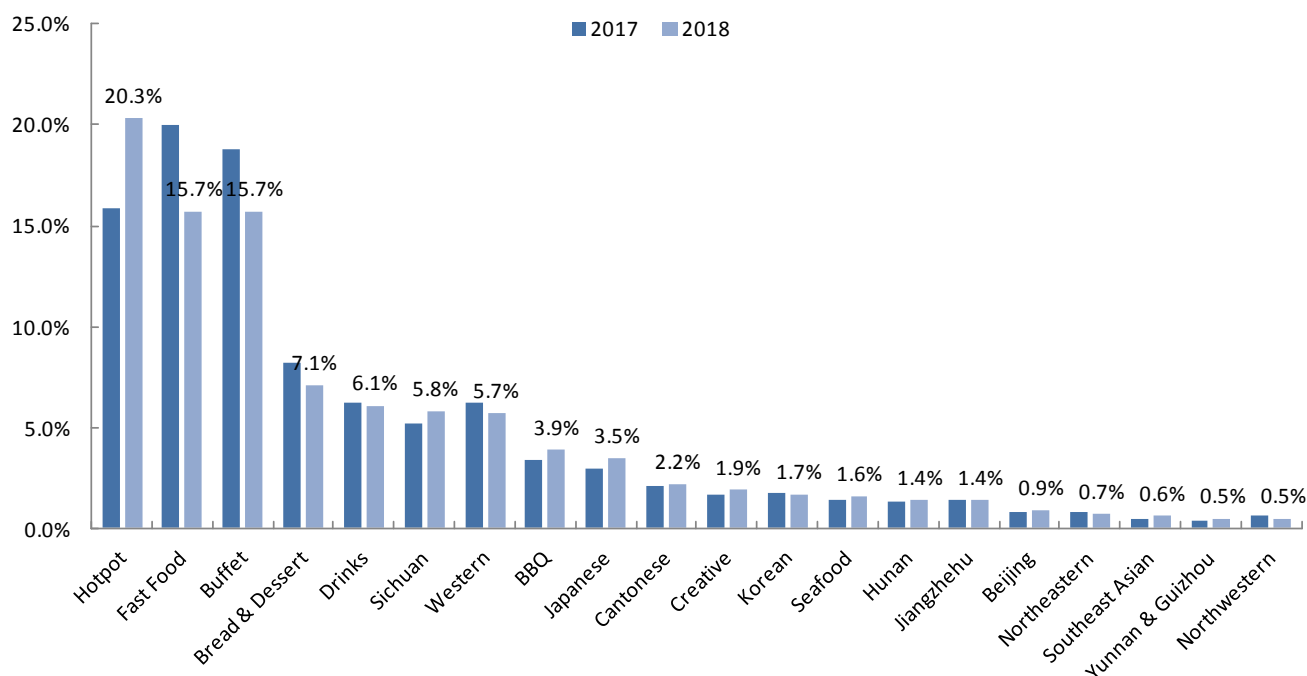
Source: 2019 Chinese Catering Report, Guotai Junan International.

Figure-81: Net Margin of Restaurants



Source: 2019 Chinese Catering Report, Guotai Junan International.

Figure-82: Order Volume Breakdown by Catering Category



Source: 2019 Chinese Catering Report.

**Reviews of restaurants in lifestyle service platforms have a huge influence on customer choice.** Currently, the value of group buying is gradually fading, but the value of user generated content (UGC) is increasingly becoming outstanding, as restaurant reputation is the primary consideration of 80.7% of customers in choosing restaurants, and 72.3% of consumers learn about restaurants from lifestyle service platforms. Promotion activities can attract customers to try once, but without good reputation and quality, customers will not come again. This is also the reason why group buying has lost popularity. There are two major user reviewing platforms, Dianping.com (Meituan) and Koubai (Alibaba). Dianping.com has a dominating position as it has 15 years of experience in building a rich UGC database, which Koubai cannot accumulate in a short period. In addition, the industry follows the 'winner takes all' rule, customers will only refer to the ratings from platforms with most users and comments. We believe that user review services is critical for life service platforms, because 1) merchants are willing to cooperate with the platform with the most influence on customers, which lays a solid foundation for other related businesses (food delivery and B2B business); 2) the high quality of UGC increases customer loyalty and attracts traffic.

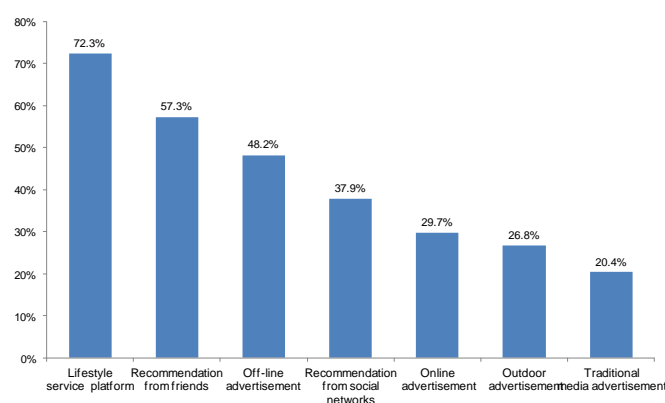


**Figure-83: Chinese Consumers' Major Considerations in Choosing Restaurants**



Source: iResearch Report, Guotai Junan International.

**Figure-84: Major Methods Used to Discover Restaurants**



Source: iResearch, Guotai Junan International.

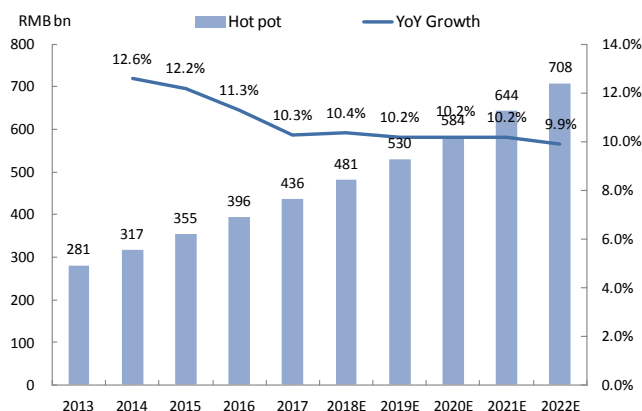
### The catering industry has borne the brunt of the NCP epidemic, and we expect that the industry reshuffle may accelerate.

Since the novel coronavirus outbreak in China first occurred, the epidemic has continued to escalate. The situation entered into a new stage after Wuhan announced a transportation lockdown on 23 January 2020. As dining together is a very likely way for the virus to spread from person to person, most restaurants in mainland China have closed at their own discretion or by government instruction. Restaurants, especially large Chinese restaurants, usually peak during the Spring Festival period, but their revenues have almost been zero this year. For fast food restaurants and casual dining restaurants, sales can also be generated by food delivery, but on a relatively small scale. Meanwhile, restaurants still face a large sum of ongoing expenses, including rental, labor and employee resettlement costs, putting tremendous pressure on their cash flows. In comparison to the SARS epidemic, the NCP epidemic has so far been more difficult to deal with in terms of the spreading of the virus, which is expected to last longer. An optimistic estimate is that the NCP epidemic may end by May 2020. In this regard, such a negative impact on China's catering industry would last until July 2020. Xibei Xiaomiancun, a well-known Chinese restaurant brand, predicted that it will run out of cash within three months. Leading restaurants may survive by acquiring capital through financing from the primary market or secondary market, or bank loans. However, smaller restaurants may face an even worse situation. We forecast that China's catering industry will face an intensified reshuffle this year. Upon the termination of the NCP epidemic, large-scale catering companies will recover first and expansion will be favorable as many outlets in good locations may be available due to the closure of small restaurants.

### Hot Pot

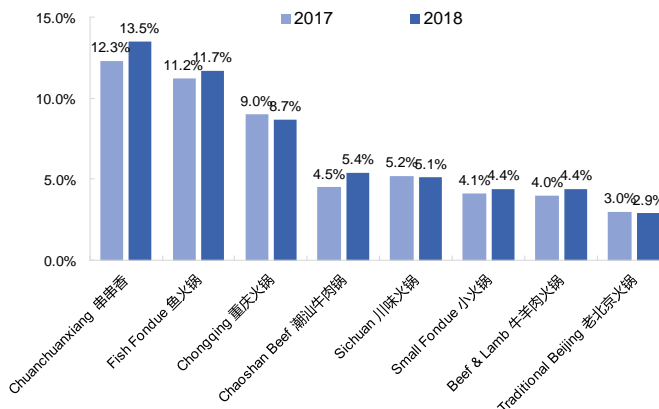
**Hotpot is highly inclusive, and there is still huge room for future growth.** The hot pot industry has grown rapidly in recent years, with an average annual growth rate of more than 10%, because on the one hand, the supply of hot pot has increased significantly, and on the other hand, hot pot has been widely accepted by consumers. After years of development, hot pot has achieved universality and inclusiveness, laying the foundation for the expansion of hot pot chain enterprises. The taste of hot pot can be spicy or light, and the dishes of hot pot can be meat or vegetables, or others. The nutritional balance can maximize customer needs. At present, there are many types of hotpots in China, which can be divided into Sichuan hotpot, northern mutton hotpot, Taiwan small hotpot, Cantonese hotpot, and Yungui hotpot. Sichuan-style hotpots (chuanchuanxiang, Chongqing hotpot, Sichuan-style hotpot, etc.) have produced the largest number of chain hotpot companies, such as Xiaolongkan, Dalongyi, Morals Village, etc. However, Haidilao and Xiabuxiabu deliberately downplayed the categories they operated to achieve full category coverage, to meet the needs of the largest consumer population, and achieve national expansion. Due to the maximum taste choice of hot pot, it is very likely to become top pick for dining together. According to a survey by 36Kr, the first reason for consumers choosing to eat hot pot is that they want to get together with friends.

Figure-85: Hot Pot Revenue & YoY Growth in China



Source: Frost & Sullivan, Guotai Junan International.

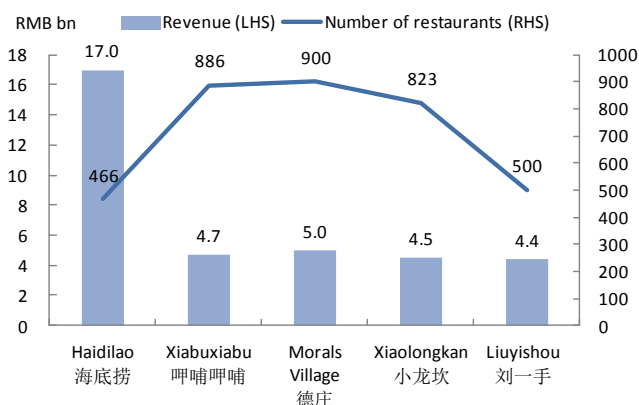
Figure-86: Share of Hot Pot Types



Source: 2019 Chinese Catering Report, Guotai Junan International.

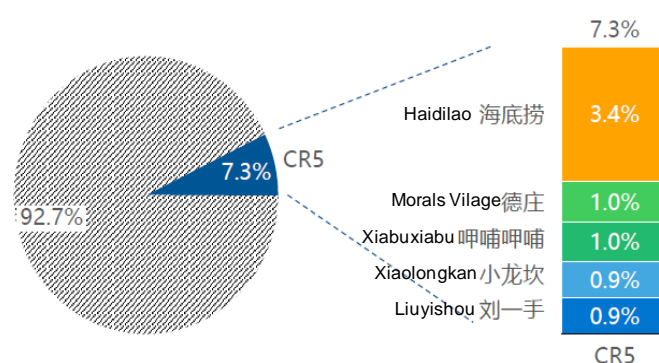
**There is a plenty of room for improvement for market concentration of hotpot.** Due to high profit margin and low barriers, the hot pot cuisine has attracted many participants, resulting in a highly fragmented market. In 2018, top 5 companies in the hot pot industry had market share of 7.3%, and individual stores accounted for 75%. Compared with individual stores, chain brands have greater advantages in upstream supply chain, systematic operations management mechanisms and brand influence. In the hot pot industry, Haidilao stands out. In 2018, Haidilao's revenue was RMB16.97 billion, which is expected to maintain rapid growth in 2019. The company had a total of 466 stores in 2018, and is expected to have added 300 in 2019. Upstream, Haidilao has Jarud Banner Haidilao to supply ingredients, and has the Shuhai responsible for procurement, warehousing, and logistics of the ingredients. Downstream, Shuyun Dongfang is responsible for the decoration of Haidilao stores, and Weihai Consulting is responsible for related human resources and services. After more than 20 years of development, Haidilao has concluded a scientific and effective hot pot methodology that can support the expansion of its business scale. Haidilao has unique experience in decentralization and centralization, as well as incentivizing employees. In the eyes of consumers, Haidilao has become synonymous with good service. This kind of competitive advantage is not easy to be abandoned by consumers over time. Xiabuxiabu launched small hot pot firstly in mainland China, which became popular during the SARS period and gradually expanded in scale. Xiabuxiabu launched Coucou in 2016, and began to explore the high-end market. Large-scale comprehensive hot pot companies are not easily affected by changes in consumer preferences. We believe that leading hot pot companies still have a lot of room to continue to penetrate low-tier cities.

Figure-87: Revenue and Number of Restaurants of Leading Hot Pot Players in 2018



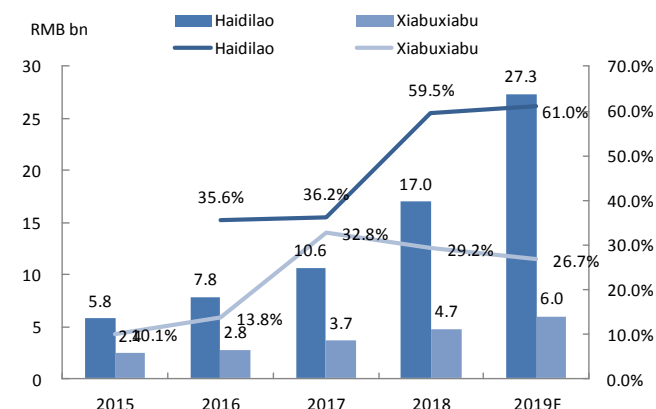
Source: 36Kr, the Companies, Guotai Junan International.

Figure-88: Market Share of Top 5 in Hot Pot Industry in 2018



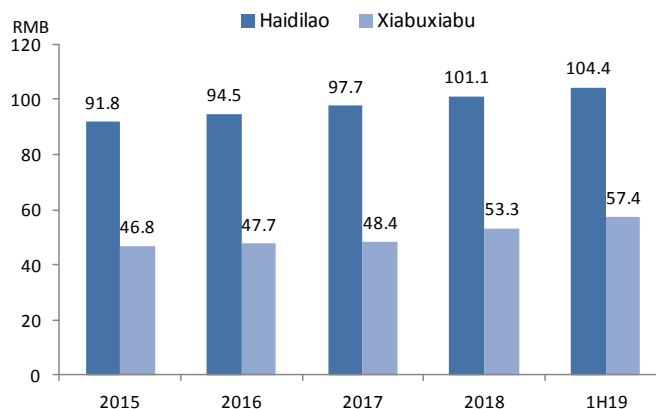
Source: 36Kr, the Companies, Frost & Sullivan, Guotai Junan International.

Figure-89: Revenue of Haidilao and Xiabuxiabu



Source: the Companies, Bloomberg, Guotai Junan International.

Figure-90: Average Spending per Guest

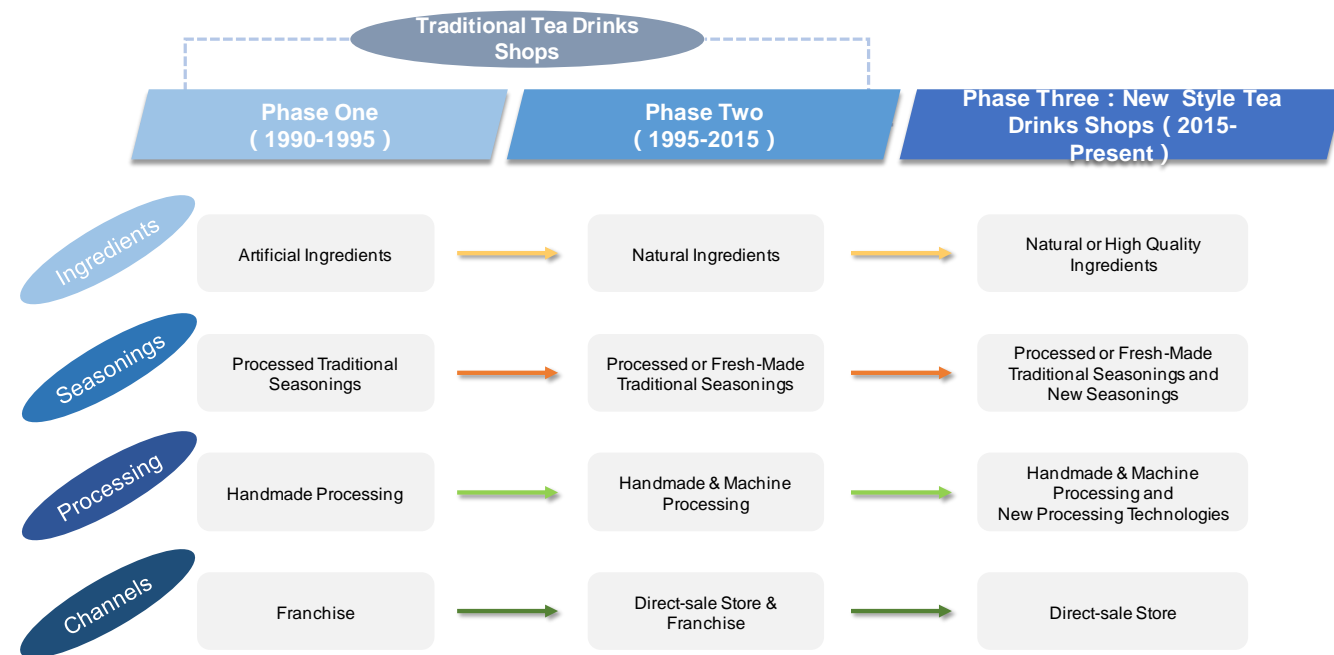


Source: the Companies, Bloomberg, Guotai Junan International.

## New-style Tea Drinks

The love from young women towards tea drinks has promoted the vigorous development of the new-style tea drinks industry. The development of China's freshly-made tea drinks industry has gone through three stages: stage 1) tea powder blended with cream to make milk tea, stage 2) upgrade to tea and fresh milk as raw materials. Five years ago, new-style tea drinks, represented by Heytea and Nayuki, began to rise, leading to stage 3) compared with traditional tea drinks, new-style tea drinks emphasize more on the selection of ingredients, production process, store operation and product innovation. For example, in the selection of raw materials, the new-style tea drinks brands use natural and high-quality food materials such as high-quality tea, fresh milk, cane sugar and fresh fruits, etc., to replace tea bags, creamers, saccharin, canned fruits and the like, which are commonly used in traditional tea drinks. In addition, new-style tea drinks are also more diversified in the selection of tea bases and ingredients, developing a variety of fruit teas to break the shackles of traditional tea drinking concepts. In addition, the new-style tea and beverage industry pays more attention to the appearance and packaging of products, and has also makes corresponding improvements to store decoration. Therefore, we can see that five years ago, Heytea and Nakuyi's products were labeled "Insta-famous". Many consumers waited in long lines just to take pictures and post them on their WeChat Moments. The vigorous development of new-style tea drinks has been partly due to their good-looking appearance and addictive taste (high sweetness) which attracts young women. According to 36Kr, the post-90s generation (21-30 years old) has become the mainstream consumer of new-style tea drinks, accounting for 50% of the total number of consumers, while the post-80s generation accounts for 37%. According to the gender distribution, 70% of the new-style tea consumers are women. Head brands such as Heytea and Nayuki have obviously been speeding up their expansion in 2018 and 2019 due to their good cash flow and favorable capital. Up to now, Heytea and Nayuki has already got rid of the label of "Insta-famous " and has become an indispensable part of young people's lives.

Figure-91: Evolution of Tea Drinks Stores



Source: 36 Kr, Guotai Junan International.

Table-2: Leading Tea Drink Brand in China

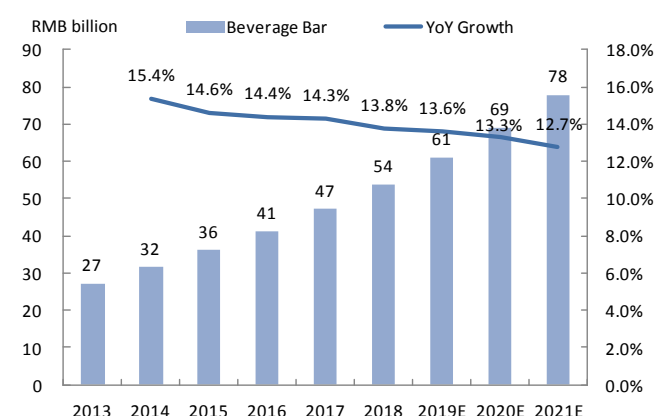
	Heytea (喜茶)	Nayuki (奈雪的茶)	Cha Yan Yue Se (茶颜悦色)	Lele Tea (乐乐茶)
<b>Year of Foundation</b>	2012	2015	2015	2016
<b>Place of Birth</b>	Jiangmen	Shenzhen	Changsha	Shanghai
<b>No of Stores*</b>	390	323	100+	54
<b>Main Products</b>	Tea Drinks	Tea Drinks & Soft French Bread	Tea Drinks	Tea Drinks & Soft French Bread
<b>Price Range (RMB Yuan)</b>	22-32	19-33	11-22	19-29
<b>Floor Area Per Store (sq.m)</b>	100-400	200-400	15+	50-400
<b>Offline Sales Channel</b>	Regular	Regular	Regular & Franchise	Regular
<b>Online Sales Channel</b>	Takeaway & Mini-Program	Takeaway & Mini-Program	Takeaway	Takeaway
<b>Latest Status of Funding</b>	Round C by Tencent & Sequoia Time: Jul 2019 Est. Value: RMB9 Billion	Round A+ by Tiantu Capital Time: Mar 2018 Consideration: Hundreds of Million Est. Value: RMB6 Billion	Round A by GC Funds & Source Code Capital Time: Aug 2019	Round Pre-A by Vertex Ventures, Ruchuan, Z&H, Hina, Prometheus, etc. Time: Apr 2019 Consideration: RMB200 Million

Source: 36 Kr, Guotai Junan International.

Note: As at the end of 2019.

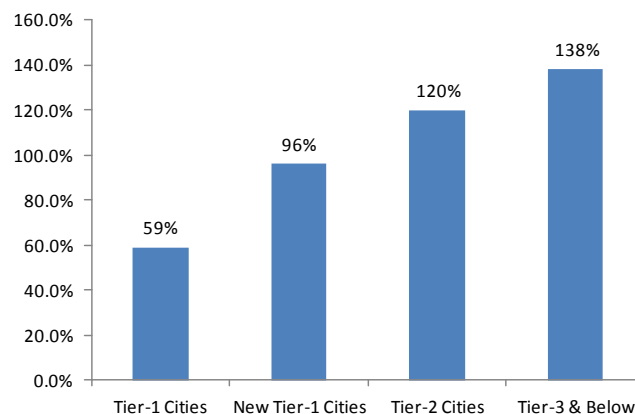
**The growth potential of the new-style Chinese tea drinks industry is huge, and cross-border competition will be significantly strengthened.** The head brands of the new-style tea drinks have already occupied a relatively good competitive position. They have strengths in store location, consumer awareness and product research and development. In 2019, Heytea introduced 240 new products all year round, in order to consolidate its economic moat and prevent new brands from overtaking by introducing new amazing products. Heytea revealed that it will open another 400 stores in 2020 and will continue to focus on first-tier cities and provincial capitals. Regarding Nayuki's development plan for the next two years, Peng Xin, the founder of Nayuki, disclosed that she planned to deepen operations in first-tier and second-tier cities in the domestic market, including provincial capitals and municipalities directly under the central government, to increase the density of store layout. Cha Yan Yue Se used to operate only in Changsha. It is also planning to expand in other markets in 2020. Starbucks has nearly 4,100 stores in China and plans to expand the number of stores nationwide to 6,000 by 2022. Peng Xin expects that it is possible for Nakuyi to reach the same number of stores. Compared with coffee, Chinese tea drinks have stronger leisure properties, more consumption scenarios, and higher growth potential in the industry. At present, the new-style tea drinks have not set foot in third-tier or fourth-tier cities. Entering the low-tier market and overseas markets will be the new direction for the new-style tea drinks brands to expand. We also see that cross-border competition in the current beverage industry is constantly emerging. The business scope of Heytea includes not only milk tea and fruit tea, but also coffee, dessert, bread, etc. In November 2019, Nayuki opened a "Nayuki Dream Factory" with an area of 1,000 square meters in Shenzhen, which integrates different formats such as tea drinking, baking, retail, wine house, steak house, and so on, including more than 1,000 SKUs. On the other hand, Starbucks has already launched a series of tea drinks. Luckin has introduced an independent brand of tea drinks, "Fawn Tea". We believe that China's new-style tea drinks brands have sufficient management capability, product innovation capability and brand marketing capability, and is not inferior to international coffee giants such as Starbucks and Costa.

**Figure-92: Revenue of Beverage Bars (excluding cafés)**



Source: 36Kr, the Companies, Guotai Junan International.

**Figure-93: Growth of Number of New Tea Drinks Shops**



Source: 36Kr, Meituan Dianping, Guotai Junan International.

## Cafés/Coffee

**The development of an intellectual society strongly promotes coffee consumption.** China's coffee market has been undergoing significant growth over recent years. According to a Frost & Sullivan report, China's market size of coffee increased from RMB15.6 billion in 2013 to RMB56.8 billion in 2018, with a CAGR of 29.5%. The per capita consumption of coffee in China was 3.2 cups in 2013 and nearly doubled to 6.2 cups by 2018. The main reason for the rapid growth in China's coffee market is that rapid economic growth has created many intellectual economic industries, such as finance, IT, and creative industries, etc. White collar workers in these industries are under great pressure and work long hours. They need caffeine in coffee to refresh themselves and have a certain dependence on coffee. Besides this, coffee also represents a more modern lifestyle. The increase in urbanization rate also promotes growth of coffee sales. Countries and regions in East Asia such as Japan, South Korea, China Taiwan and China Hong Kong were not used to the consumption of coffee in the past, but they have all experienced a rapid increase in coffee consumption per capita due to the rapid development of an intellectual society. In 2018, per capita consumption of coffee in Japan, Hong Kong and Taiwan was 279 cups, 250 cups and 209 cups of coffee, respectively, and South Korea even exceeded 300 cups. Coffee has a higher refreshing effect than tea, and less young people have a habit of drinking hot tea compared to the previous generation. As the urbanization rate continues to rise, the number of white-collar workers continues to grow and young consumers become mainstream, the certainty of sustained growth in China's coffee consumption in the future is promising.

Figure-94: Market Size of Coffee in China

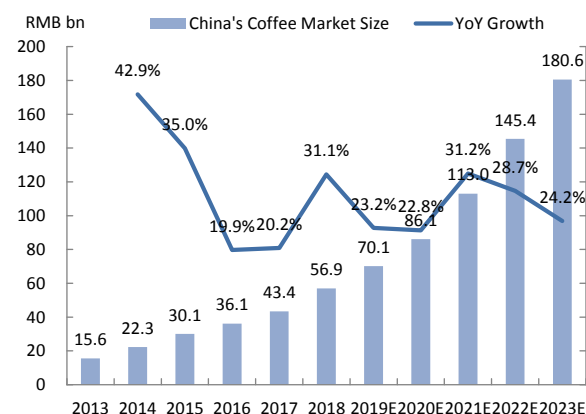
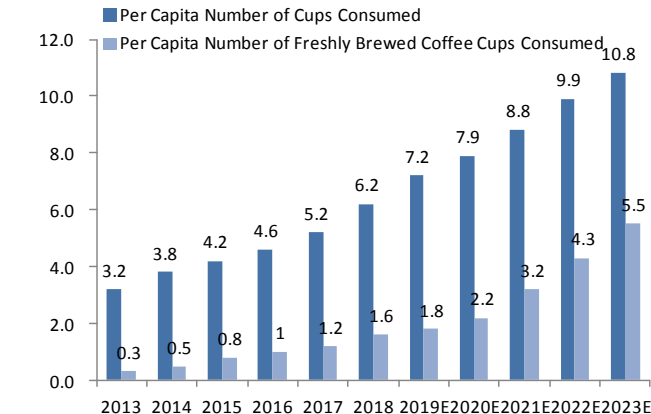


Figure-95: Per Consumption of Coffee



Source: Frost & Sullivan, Prospectus of Luckin Coffee, Guotai Junan International.

Source: Frost & Sullivan, Prospectus of Luckin Coffee, Guotai Junan International.

**Different types of coffee are priced differently, covering many brands from different sectors.** Coffee consumption scenarios, purchasing methods and price bands are the most abundant and varied in the consumer sector. Consumers can choose from RMB1 to RMB50. At RMB1, consumers can choose low-end instant coffee and at RMB3-5 consumers can choose low-end RTD coffee. At RMB5-10, consumers can choose medium-high RTD coffee or high-end instant coffee, such as Saturn Bird Coffee. At the price band of RMB10-15, consumers can buy freshly brewed coffee at Family Mart/ 7-11 convenience stores, self-service coffee machines, and discounted Luckin coffee. At RMB15-20, customers can drink a cup of freshly brewed coffee provided by McDonald's and KFC as well as discounted Luckin coffee. In the RMB20-30 price range, there is mainly Luckin coffee at original price and Coffee Box. In the RMB30-40 price range, there are the major international chain café brands such as Starbucks, Costa and Pacific Coffee. Higher than RMB40, there is mainly high-end premium café brands. Due to the relatively long price band of coffee, many companies from different industries have launched coffee products, including international food giant Nestlé, beverage giant such as Coca-Cola, UPC, Tingyi, Nongfu Spring as well as international café giant chains, Starbucks and emerging domestic café brand, Luckin. Due to rapid growth, the Chinese coffee market is becoming more crowded than ever before. Whether it is instant, ready-to-drink or freshly brewed coffee, companies are vigorously opening out in the coffee industry. We saw the explosive growth of Internet coffee represented by Luckin, which to some extent squeezed the growth space of other traditional café brands. And Luckin's price band can even reach the price range of RTD coffee, attracting a wider range of consumers. At present, China's coffee market is still in a stage of rapid development. Competition across the price bands is not fierce except for Luckin, but competition within the price bands may become more intense.



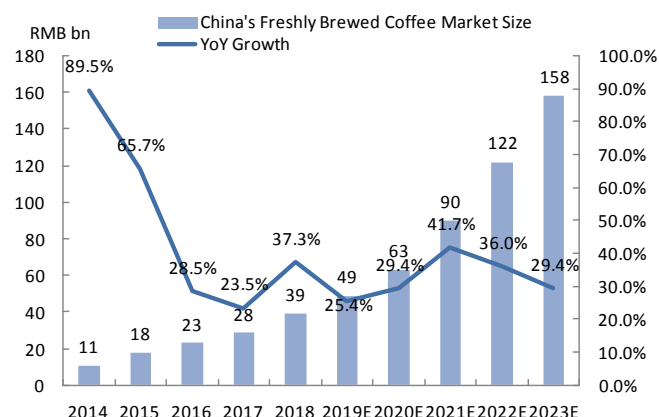
21 February 2020

Consumer Sector-Food & Beverage 消费行业-食品饮料

Sector Report

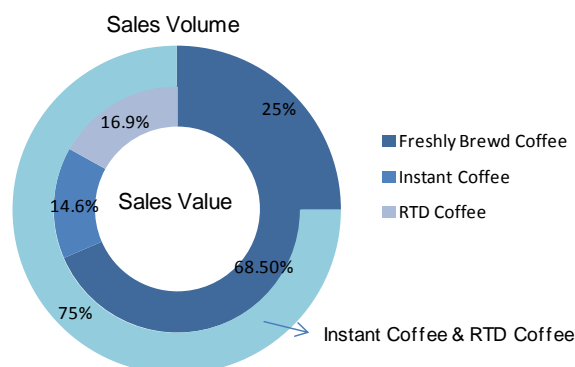
*See the last page for disclaimer*

Figure-97: Market Size of Freshly Brewed Coffee in China



Source: Frost & Sullivan, Prospectus of Luckin Coffee, Guotai Junan International.

Figure-98: Share of Coffee Market

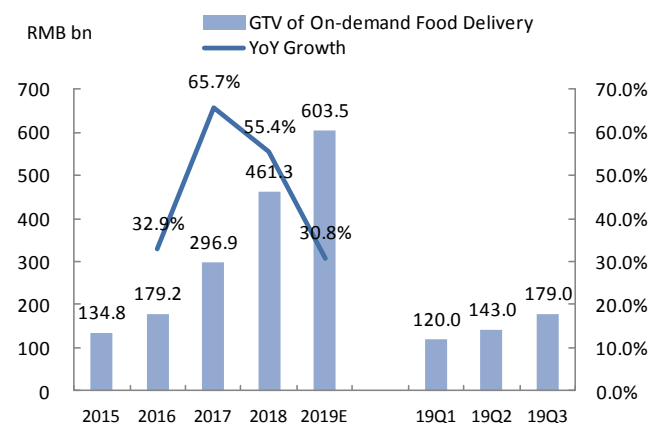


Source: Frost & Sullivan, Prospectus of Luckin Coffee, Euromonitor, Guotai Junan International.

## Food Delivery

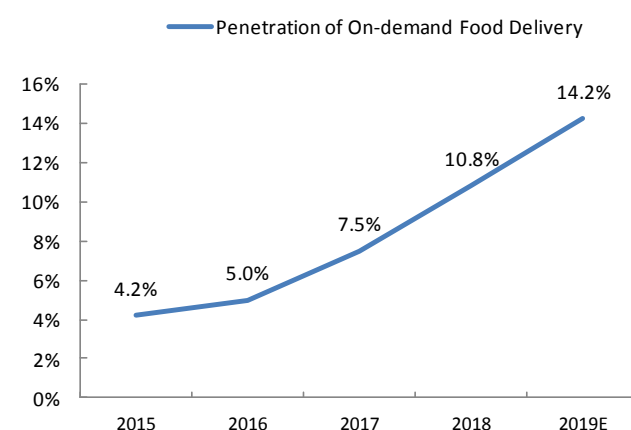
**Less discretionary time, shorter delivery times and low cost of delivery are driving food delivery to grow robustly.** China's on-demand food delivery GTV increased 55.4% YoY from RMB296.9 billion in 2017 to RMB461.3 billion in 2018, which accounted for 10.8% of total catering revenue. Trustdata expects that on-demand food delivery GTV will continue to grow 30.8% YoY to RMB603.5 billion in 2019, representing 14.2% of total catering revenue. The strong growth of food delivery in China has been driven by three growth pillars. (1) Chinese people have less discretionary time compared to other countries due to longer average working hours and higher female labor participation rate (62%), which reduces available time for cooking at home. (2) Population density in urban cities in China was 2,426 people per square kilometer in 2017, over seven times that of the U.S. As a result, it takes 35 minutes for each delivery order in China compared to 75 minutes in the US. (3) Low cost of delivery is a unique advantage for China's food delivery industry compared to developed east Asian countries and areas which actually also have high demand for food delivery due to less discretionary time and high population density of consumers. Due to China's family planning policy over last 30 years and weakening desire towards childbirth, China's labor supply has been declining since 2013 and is expected to continue decreasing. But the services industry in China is burgeoning and the post-1990s generation has been the main labor force, who are less willing and lack ability to work mechanically and painstakingly in manufacturing factories and construction sites; we noticed that China's labor force is continuously shifting from the industrial industry to services industry, which provides enough labor force for the on-demand delivery industry. Compared to developed countries, the driver cost for each food delivery order in China is around US\$1, much lower than US\$5 in the US. Moreover, the widespread use of electric bicycles in China has greatly improved the transportation efficiency of food delivery in intricate intra-city road conditions, which significantly lowers the cost of delivery.

**Figure-99: On-demand Food Delivery GTV & Growth in China**



Source: Trustdata, Guotai Junan International.

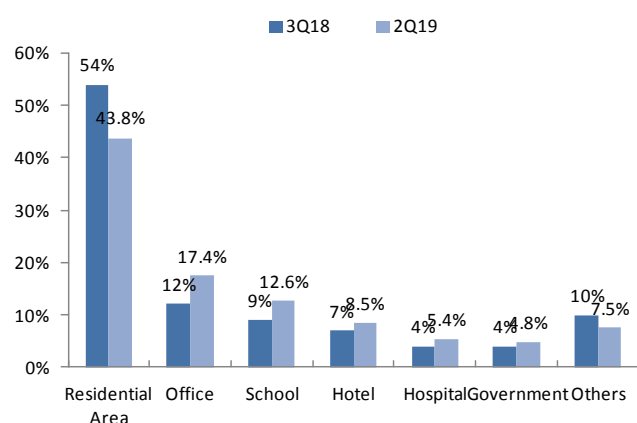
**Figure-100: On-demand Food Delivery Penetration of Total Catering Revenue**



Source: Trustdata, Guotai Junan International.

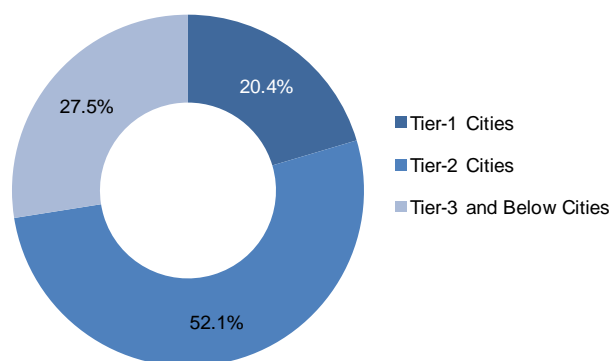
**Food delivery consumption has still got great potential to grow with consumption scenarios further enriching and penetration increasing.** On-demand food delivery platforms have successfully helped consumers to develop a habit of ordering food delivery through lots of subsidies. In 2Q19, about 43.8% of food deliveries were ordered from residential areas, indicating that most food deliveries were ordered to replace cooking at home. We believe that consumption habit can be relatively smoothly extended to more dining scenarios, once laziness habits are formed, which cannot be given up easily. Customers under 30 are the major consumer base of food delivery, and we expect a considerable portion of them will keep their food ordering delivery habit after starting families due to laziness and lack of cooking skills. Nevertheless, based on Meituan's number of food delivery transactions (6,393 million) and market share in 2018, we figure out the number of total food delivery transactions in China in 2018 was around 10,909 million, representing 7.8 transactions per person each year, which only accounts for 0.7% of the total annual number of meals per person ( $3 \times 365$ ). We believe that food delivery penetration has great room to grow as consumption frequency increases and more new users are included, especially in lower-tier cities. In 1H19, according to Trustdata, only 27.5% of food delivery orders were generated in tier-3 and below cities.

**Figure-101: Food Delivery Orders Breakdown by Place**



Source: Trustdata, Guotai Junan International.

**Figure-102: Food Delivery Order Distribution in 1H19**

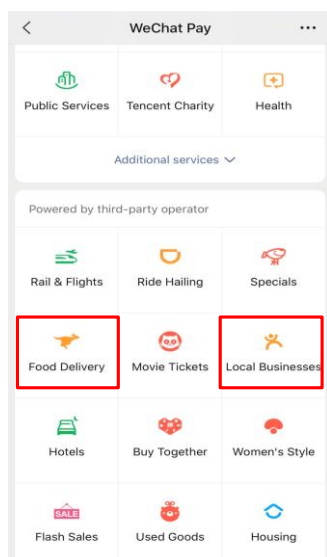


Source: Trustdata, Guotai Junan International.

**Meituan roots deeper and has support from Tencent while Ele.me has strong synergy effects with Alibaba's other business.** Meituan has a key edge as they have a stronger connection with merchants, wider city layout and Tencent's support. Meituan works with 5.1 million annual active merchants across 2,800 cities, much higher than Ele.me and Koubei's 3.5 million annual active merchants across 676 cities. Meituan has a much stronger presence in lower-tier cities than Ele.me and Koubei as Meituan has started working with merchants across the country since competition in group buying started in 2010. Since then, Meituan has trained a group of experienced business developers (BD) with strong execution capabilities. In addition, Tencent, as Meituan's substantial shareholder, has provided Meituan two different entry points (previously three) in WeChat Pay. Around one tenth of Meituan's transactions were generated through Tencent's Weixin and QQ. On the other hand, Ele.me and Koubei served 3.5 million annual active merchants across 676 cities, lower than Meituan. But after Alibaba's takeover, Ele.me has been strengthening its connections with merchants, and Ele.me and Koubei can share merchant resources with each other after the

merger. And with Alibaba's technical support, Ele.me has accelerated product iterations and improved its dispatch system. Moreover, Alibaba has a firm base of technologies in cloud services, SaaS and finance, which can efficiently empower merchants. On top of all that, Alibaba has integrated its membership program with Ele.me by launching its 88 VIP. Based its integrated membership program, Alibaba knows more about its consumers with all-around detailed data, which enables it to market precisely. Within Alibaba's ecosystem, Ele.me and Alibaba's other business can provide traffic to each other, creating a huge synergy effect.

Figure-103: WeChat Pay



Source: WeChat.

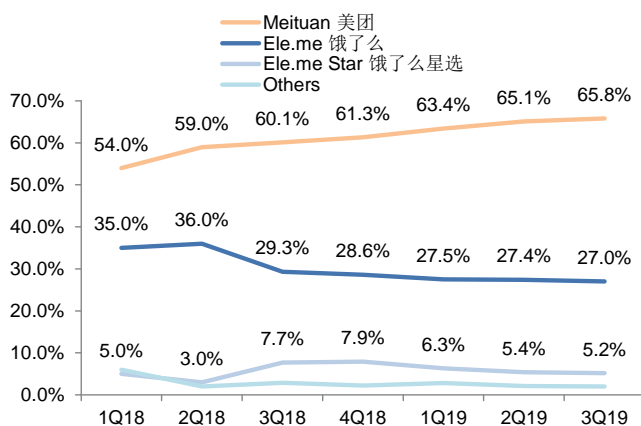
Figure-104: Alibaba's 88 VIP



Source: Alibaba.

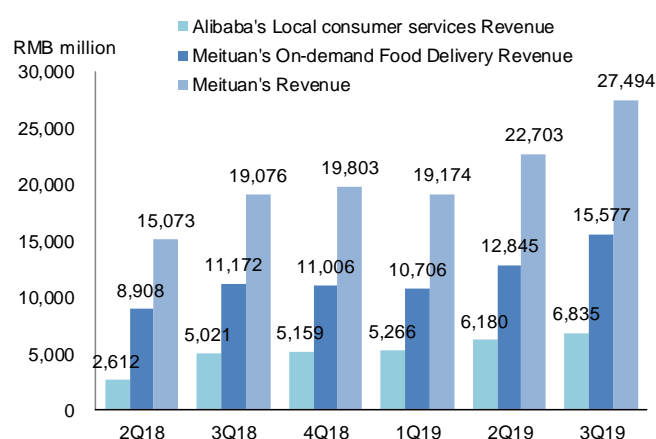
**Meituan maintains leadership but intense competition may continue.** Since Meituan's GTV surpassed Ele.me in 2016, the Company has maintained No.1 position in the food delivery market. According Trustdata, Meituan grasped 65.8% market share in 3Q19, notably higher than Ele.me's 32.2%. And Meituan Waimai's MAU was also considerably higher than Ele.me. According to Alibaba's financial results, its revenue from local consumer services including Ele.me and Koubei in 3Q19 achieved RMB6,835 million, notably lower than Meituan's revenue (RMB27,494 million) and Meituan's on-demand food delivery revenue (RMB15,577 million). The duopoly competition has been fully entrenched in the food delivery market where small players hardly survive and Meituan's leading position has strengthened. As Alibaba's new local service company has Alibaba's financial support, we expect that the intense competition between Meituan and Alibaba will not end in the short term. The market may maintain the landscape of 7 vs. 3 to 6 vs. 4.

Figure-105: Competitive Landscape of China Online On-Demand Delivery Industry (Based on GTV)



Source: Trustdata, Guotai Junan International.

Figure-106: Revenue of Meituan and Alibaba's Local Consumer Services Revenue

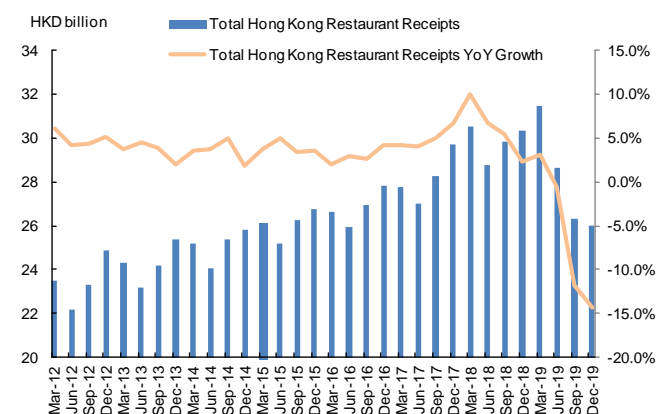


Source: Alibaba, Meituan, Guotai Junan International.

## Hong Kong Catering Industry

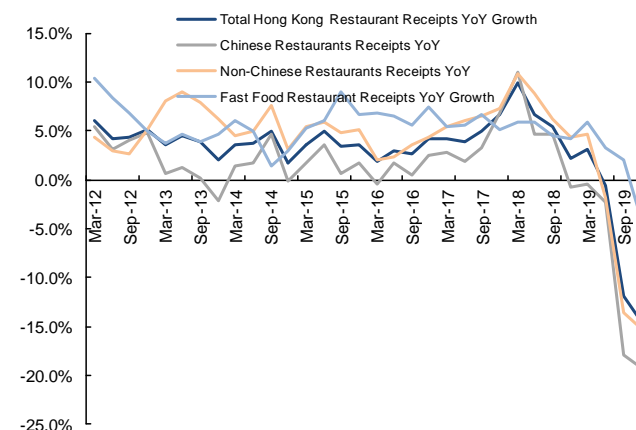
The challenging external environment has severely affected the catering industry in Hong Kong. Demonstrations in Hong Kong have severely impacted the catering industry. According to the Census and Statistics Department of Hong Kong, total Hong Kong restaurant receipts in 3Q2019 and 4Q2019 decreased by 11.8% YoY and 14.3% YoY, respectively. In 4Q2019, Chinese restaurant receipts and non-Chinese restaurant receipt fell by 19.2% YoY and 15.1% YoY, respectively. The demonstrations have recently shown signs of easing in 1Q2020, but the slightly recovered Hong Kong catering industry was hit hard again by the NCP epidemic, which significantly reduced the number of tourists arriving Hong Kong and significantly lowered residents' desire to eat out. Relatively speaking, fast food restaurants are less affected than other catering types, but the challenging external environment is unavoidable. Leading Chinese fast food giants such as Café de Coral have also been impacted by the external environment, but relatively speaking, due to their stable consumer group, their revenue has been affected less than other full-service restaurants. However, due to the need to launch more discounted packages and promotions, Café de Coral's gross margin was considerably affected.

**Figure-107: Total Hong Kong Restaurant Receipts & YoY Growth**



Source: Census and Statistics Department of Hong Kong, Guotai Junan International.

**Figure-108: Total Restaurants, Chinese Restaurants, Non-Chinese Restaurants and Fast Food Restaurant Receipts & YoY Change**



Source: Census and Statistics Department of Hong Kong, Guotai Junan International.

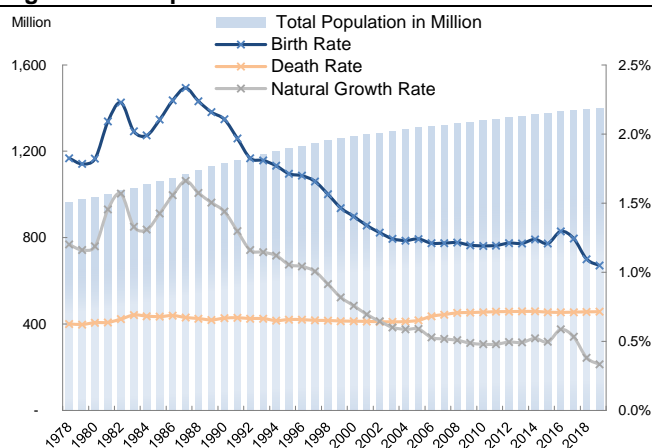
## How Ongoing Structural Changes of Chinese Consumers Impact on Consumption

**Structural changes of consumers have a substantial impact on food and beverage consumption; the driving force for consumption upgrade comes from the significant optimization of labor force structure.** All consumer goods are born to meet consumer needs, and consumers of all ages and income groups have huge differences in demand for consumer goods. If we can understand the ongoing structural changes of Chinese consumers, we can better understand the current consumer goods market and predict the future development of consumer goods. With the spiraling decline of the number of newborn babies, the aging trend of China's population will be difficult to reverse in the future. It is clear that the size of young consumer groups has begun to shrink, which also explains why per capita consumption of many consumer products such as beer, instant noodles and ham sausage have been weak since 2013. In addition, the decline in childbirth directly poses a challenge to growth of the diaper and IMF industries. However, we can see that Chinese occupation structure is continuously improving. With the rapid development of China's tertiary industry, especially industries incorporating intelligence and creativity (IT, finance, culture, education, health and other industries), more and more people are becoming middle class, growing in quantity and quality, and has become the biggest driving force of China's consumption upgrade. The proportion of college students in the newly employed population each year has exceeded 60%. Income and standard of taste of the newly employed population have greatly improved. Their demand for higher quality lives will drive the consumption industry to continue to develop. Along with the steady progress of urbanization, Chinese consumers' pursuit of a better life will drive the food and beverage industry towards a higher level. Moreover, the fight against poverty has led by the Chinese government has greatly reduced the number of poor people and increased demand for daily consumer goods.

## How Changes in Demographics Impact Consumption

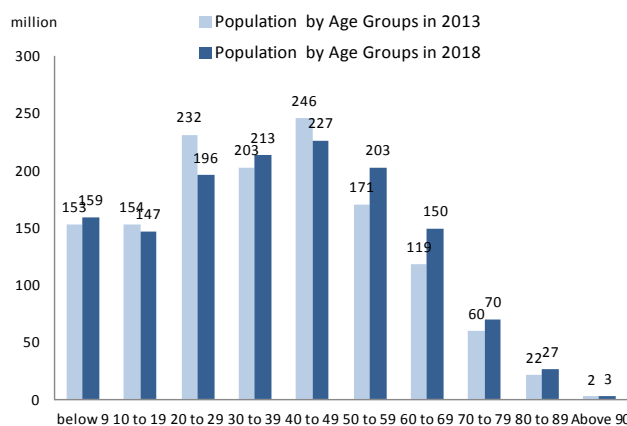
**China's demographic is undergoing structural change.** With the passing of the baby boom, China's newborn population has shown a gradual decline. Judging from the population structure, the number of young people aged between 10-29 years in China has shrunk significantly in the past five years. According to a sample survey data from the National Bureau of Statistics of China, China's population aged between 10-29 years was about 385 million in 2013, but fell to 343 million in 2018. This also explains why the per capita consumption of many consumer products such as beer, beverages, instant noodles and high-temperature meat products has been sluggish since 2013. Looking ahead, as the number of newborn babies continues to decline, we estimate that the average age in China will further increase. In the next 5-10 years, judging from the current population of 0-19 year olds, the proportion of the young population aged between 10-29 years will continue to show a significant downward trend, which will exert significant pressure on the growth of consumption in beer, beverages, instant noodles and high-temperature meat products and other industries. However, we also see that the generation post 1990 and post 1980 that grew up after the reform and opening up of China are becoming the main force of China's consumption, which will greatly change the structure of food and beverage consumption.

Figure-109: Population Growth in China



Source: National Bureau of Statistics of the PRC, Guotai Junan International.

Figure-110: Population Structure 2013 vs. 2018



Source: National Bureau of Statistics of the PRC, Guotai Junan International.



**The number of newborn babies is expected to inevitably decline due to lower fertility rate and less women of reproductive age.** Following the limited two-child policy and universal two-child policy implemented in 2013 and 2015, respectively, China's population growth temporarily went up in 2014 and 2016. But as the universal two-child policy has been taking less effect in 2019, the birth rate fell to 1.05% with 14.65 million newborn babies, the lowest number since 1949. According to the World Bank, births per woman (also known as the total fertility rate) in 2017 was 1.68 in mainland China, less than 1.77 in the United States and 2.24 in India. Except for family-planning policy, lower child-bearing willingness and declining marriage rates put more pressure on fertility. Over the past few decades, Chinese women's desire for motherhood drastically changed from 'eager to give birth' to 'don't want to' or 'can't afford to give birth'. And late marriage age (or even resistance to marriage) has become more common than ever before in China as young people start careers later due to longer education period and inability to afford a houses in tier-1/tier-2 cities. We noticed that in developed urban areas, marriage rate has also stayed low. On the other hand, as the second generation of Chinese baby boomers, born between 1982 and 1992, is aging, the population within reproductive age will continue to shrink in the next ten years. As the number of newborn babies decreases continually, sales of IMF and diapers have been affected. However, it is worth noting that the new generation of young parents with stronger purchasing power will promote consumption upgrade of diapers and IMF.

Figure-111: Number of Newborn Babies in China

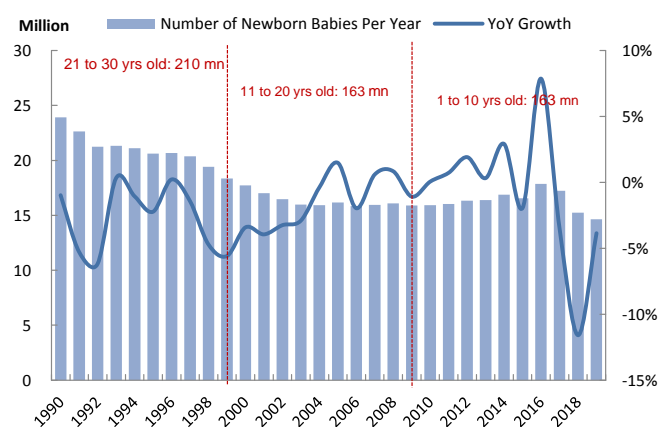
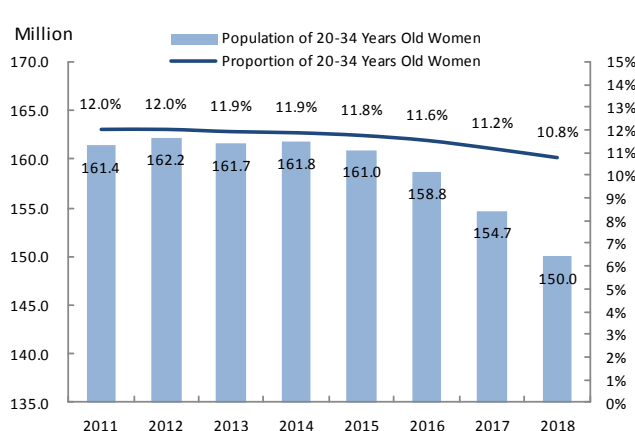


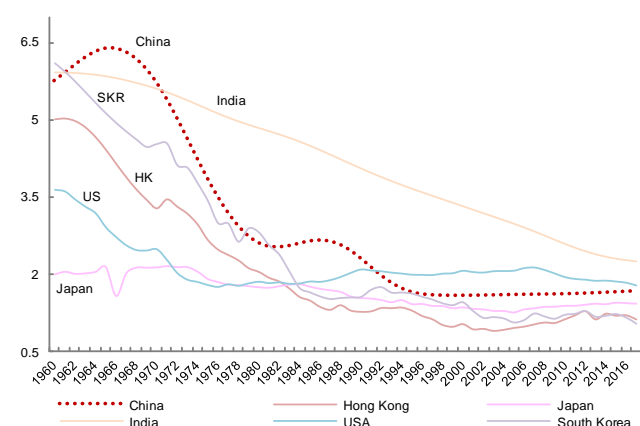
Figure-112: Population of Women Aged 20 to 24 in China



Source: National Bureau of Statistics of the PRC, Guotai Junan International.

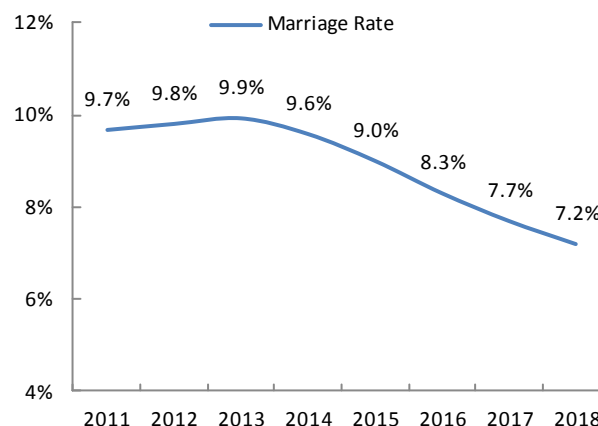
Source: National Bureau of Statistics of the PRC, Guotai Junan International.

Figure-113: Births Per Woman by Region



Source: World Bank, Guotai Junan International.

Figure-114: Marriage Rate

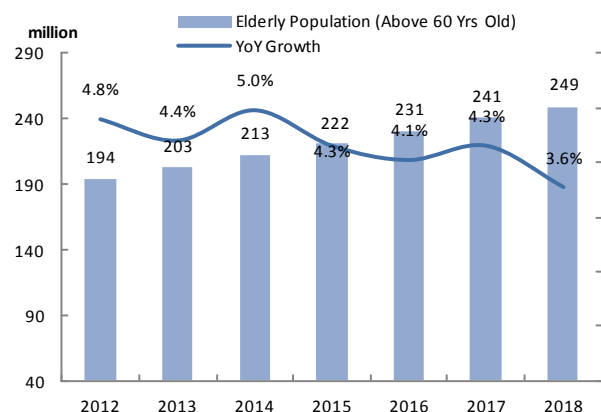


Source: Ministry of Civil Affairs of the PRC, Guotai Junan International.

**An ageing problem has fully emerged.** In 1990, China's average life expectancy was only 68.6 years, which remarkably increased to 76.3 years by 2015. The upward trend has not slowed down up to now. The proportion of the elderly over 60 years old has continued to increase from 13.7% in 2011 to 17.9% in 2018. The population of the elderly over 60 years reached 249 million in 2018. The elderly population has been growing faster than that of the total population in China. According to the United Nations, the proportion of the elderly over 60 years old in China will reach 25.3% in 2030. The elderly dependency ratio has increased from 10.7% in 2004 to 16.8% in 2018, which is expected to further increase, which may mitigate the consumption power of working people. China's demographic dividend has been disappearing and may turn to population burden. According to the Ministry of Human Resources and Social Security of the PRC, in 2018, around 159 million retirees were receiving pensions from the social security fund. And the number is expected to significantly enlarge as the first generation of baby boomers, born between 1962 to

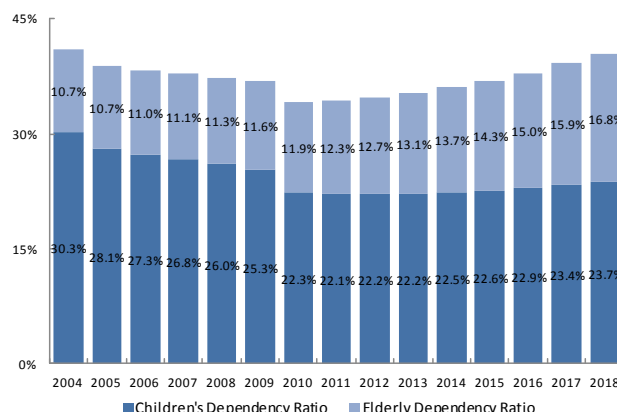
1973, is retiring. The increase in social security expenditure will, to a certain extent, lead to an increase in social security payment pressure of the current working population. And with the increase of dependency ratio, the pressure on young people to support the elderly will become even greater. In the past, the consumption rate of the generation of the elderly was extremely low, but the consumption of the new generation of elderly will be more normal and will not be too conservative in consumption. Moreover, the accumulation of houses as wealth and the improvement of the social security system will ensure spending power of retired people. With the increase of the elderly population, the consumption of health care products and nursing supplies for the elderly is expected to increase simultaneously.

**Figure-115: Elderly Population in China**



Source: National Bureau of Statistics of the PRC, Guotai Junan International.

**Figure-116: Dependency Ratio**

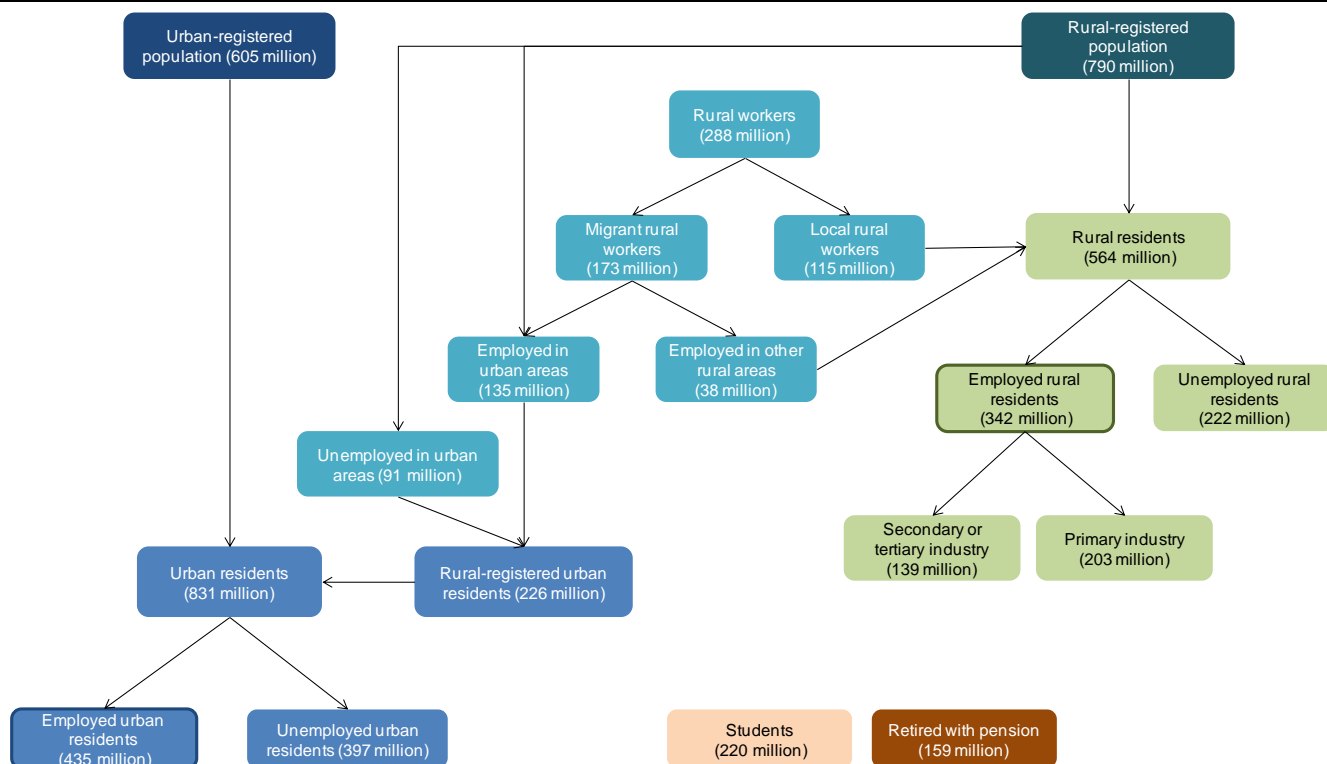


Source: Minister of Human Resources and Social Security, CEIC, Guotai Junan International.

## How Changes in Occupation Structure and Income Impact Consumption

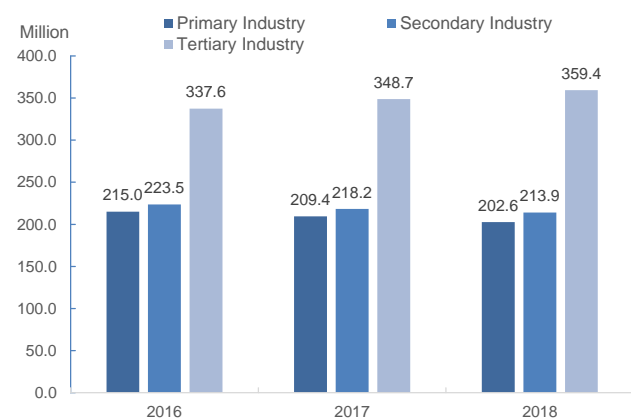
**The transfer of the employed population in the secondary industry to the tertiary industry stimulates the growth of consumption.** In order to predict the changes in future consumption, we think it is very important to study the occupation composition of consumers, because occupation generally reflects the income level of consumers. The occupation and income level of consumers determine their consumption habits and consumption level at the same time. In the process of China's primary industry population transferring to the secondary industry/tertiary industry, a large number of working class have been generated, with both income level and consumption expenditure increasing greatly, which has become one of the main driving forces supporting the rapid growth of consumption in the past few decades. In 2018, China's rural-registered population was 790 million, while the rural resident population was 564 million, with 226 million farmers entering the city (135 million were migrant rural workers working in the city and others don't have jobs). Of the 342 million employed people who stayed in the countryside in 2018, only 203 million were engaged in the primary industry, down from 2016. In recent years, due to the impact of capacity reduction, employees in the secondary industry have obviously begun to transfer to the tertiary industry. According to data from the National Bureau of Statistics, the number of migrant rural workers engaged in manufacturing and construction decreased by 2.0% YoY and 0.3% YoY, respectively, in 2018, while the number of migrant workers engaged in catering and residential services increased by 0.9% YoY and 0.8% YoY, respectively. The tertiary industry absorbed 359 million employees in 2018, an increase of 21.8 million compared with 2016. As the tertiary industry is closely related to urbanization, the consumption habits of the rural-registered population engaged in the tertiary industry are similar to those of the urban-registered population, unlike those migrant workers engaged in manufacturing and construction industries, staying in a closed environment and not affected by urban consumerism. The new generation of young migrant workers is relatively more inclined to engage in the tertiary industry, as the awakening of young migrant workers' self-awareness has lowered their willingness to engage in heavy work, and the tertiary industry has become their first choice. Relatively speaking, the marginal consumption tendency of the tertiary industry population is greater, and with the increase in number of people, it will become a favorable support for the growth of consumption.

Figure-117: Chinese Occupation Landscape in 2018



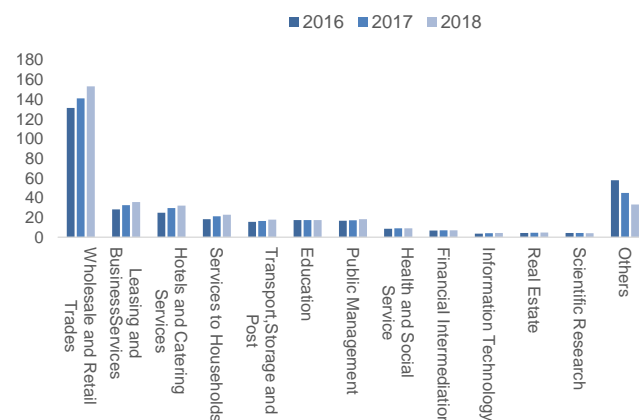
Source: National Bureau of Statistics of the PRC, Guotai Junan International.

Figure-118: Number of Employed Persons in China



Source: National Bureau of Statistics of PRC, Guotai Junan International.

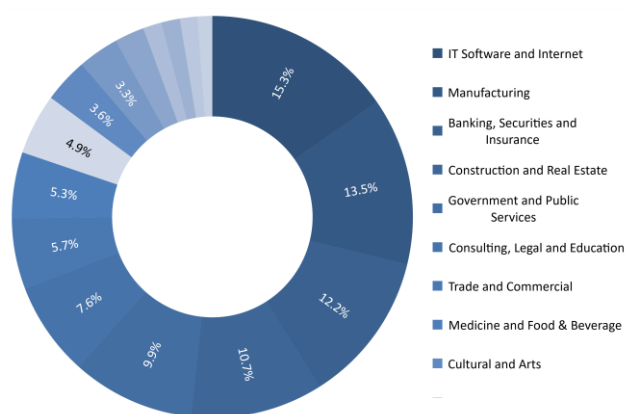
Figure-119: Number of Employed Persons in Tertiary Industry



Source: National Bureau of Statistics of PRC, Guotai Junan International.

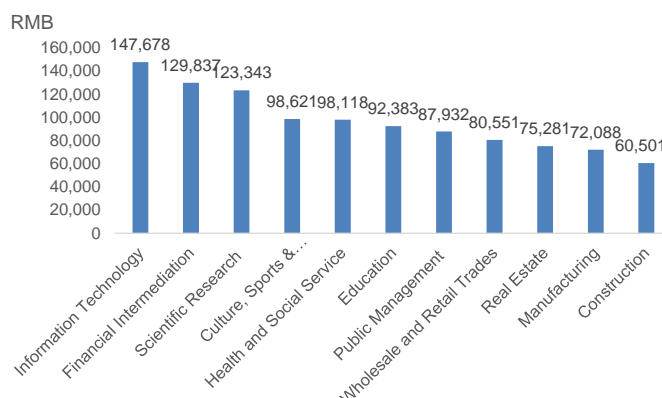
**The expansion of the middle class has become the most important support for consumption upgrading.** Due to the relatively low added value of the primary and secondary industries, only a small number of people can be promoted to middle class. According to the definition of the "2019 White Paper of the New Middle Class", the annual income of middle-class families is RMB200,000 to RMB1 million, and their occupations are 1) professional white-collar workers or middle and senior managers of enterprises; 2) educators, media personnel, scholars and other cultural and educational professionals; and 3) civil servants and government staff or affiliated institutions. The middle class needs higher education levels or have corresponding scientific qualities. According to the "2019 White Paper of New Middle Class", IT, manufacturing and finance have created the largest proportion of middle class. The total number of employees in the IT industry and financial industry is lower than that in the manufacturing industry, but due to their high-income level, IT industry and financial industry employees have great probability of entering the middle class. According to the "2019 White Paper of New Middle Class", except for manufacturing and construction, the middle class comes from the tertiary industry. With GDP per capita exceeding US\$10,000, China's tertiary industry, especially those highly related to intelligence and creativity (IT, finance, culture, education and health, etc.) will surely continue to develop, giving birth to an increasingly large middle class, whose quantity and quality are increasing day by day, becoming the biggest driving force for China's consumption upgrade.

Figure-120: Occupation Structure of Middle Class



Source: 2019 White Paper of New Middle Class, Guotai Junan International.

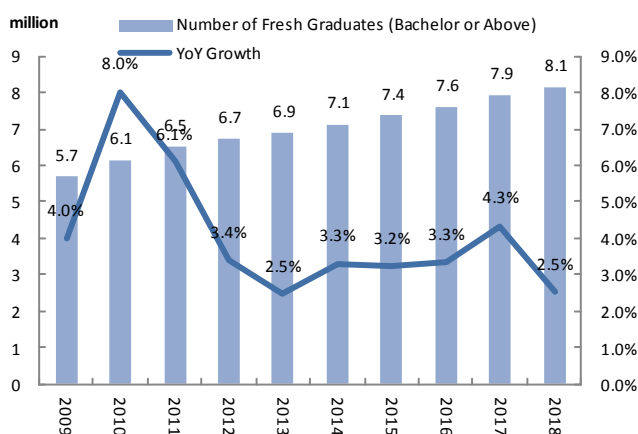
Figure-121: Average Wage of Employed Persons in Urban Non-Private Units by Sector



Source: National Bureau of Statistics of the PRC, Guotai Junan International.

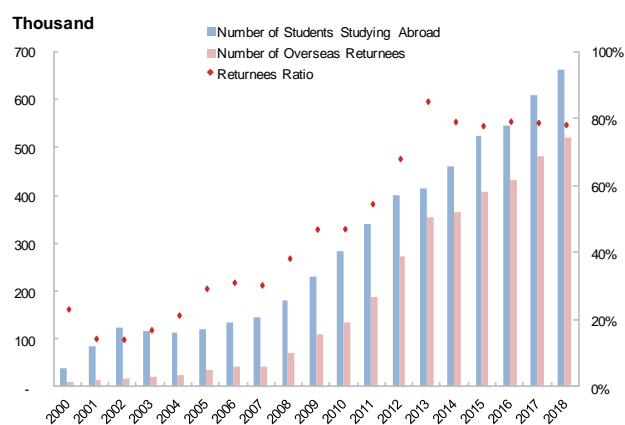
The proportion of well-educated newly employed in the labor force increased considerably, which lays a solid foundation for the expansion of middle class and consumption upgrade. According to the National Bureau of Statistics, the number of fresh college graduates per year in China increased from 3.4 million in 2005 to 8.2 million in 2018. According to the National Bureau of Statistics, the number of overseas returnees reached 519,000 in 2018 and is expected to rise tremendously. Shanghai, Beijing, Shenzhen, Hangzhou and Guangzhou are the top five cities of choice for overseas talent. In 2018, the number of newly employed labor force in China was 13.61 million, of which the number of well-educated labor force (bachelors, masters, doctors and returning students) was 8.7 million, accounting for more than 63%. Because of China's long-term one-child policy, parents have the ability and willingness to invest in their children's education, and China's higher education has made significant progress, and has greater ability to train more high-quality talent. The newly employed labor force with higher education is generally engaged in white-collar jobs and has a higher chance of being promoted to the middle class. The development and growth of China's middle class will become the foundation of China's continued prosperity of consumption. Not only that, the quality of China's new blue-collar labor force has also been greatly improved. Facilitated by the implementation of a 9-year compulsory education program, the educational attainment composition of China's general population has been improving dramatically and learning levels are shifting rapidly upward. By 2018, around one-third of China's population had attained upper secondary or above education. Illiteracy rates also dropped significantly. With reference to neighboring countries in APAC, such as South Korea and Japan, we expect that in China the average years of education will continue to add up along with the ongoing economic and social development. As income and consumer taste of the newly employed labor force have improved significantly, their demand for higher quality consumption will drive the industry to continue to develop. China is bound to have a group of world-class consumer brands.

Figure-122: Fresh College Graduates (Bachelors or Above)



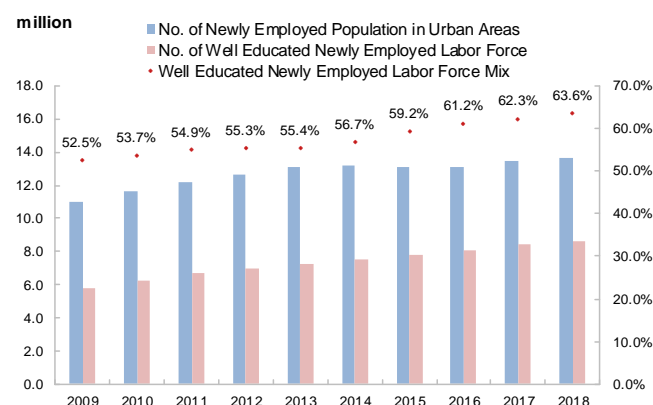
Source: National Bureau of Statistics of the PRC, Guotai Junan International.

Figure-123: Number of Overseas Returnees



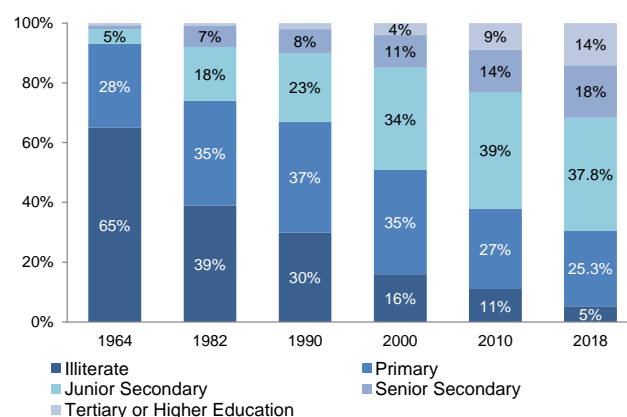
Source: Minister of Human Resources and Social Security, CEIC, Guotai Junan International.

**Figure-124: Percentage of Well-Educated Labor Force in New Employed Population**



Source: National Bureau of Statistics of the PRC, Guotai Junan International.

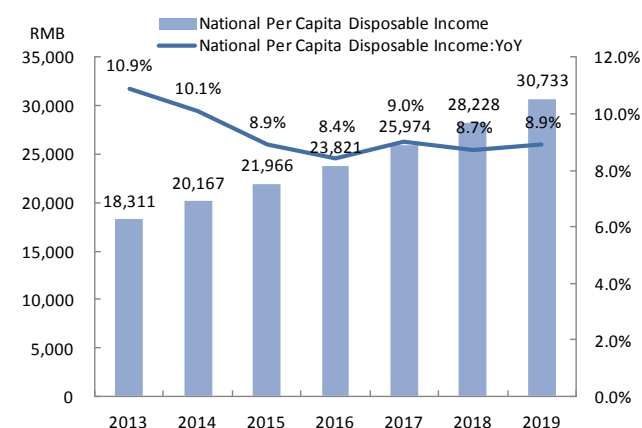
**Figure-125: Population by Educational Attainment**



Source: Conference Board, National Bureau of Statistics of the PRC, Guotai Junan International.

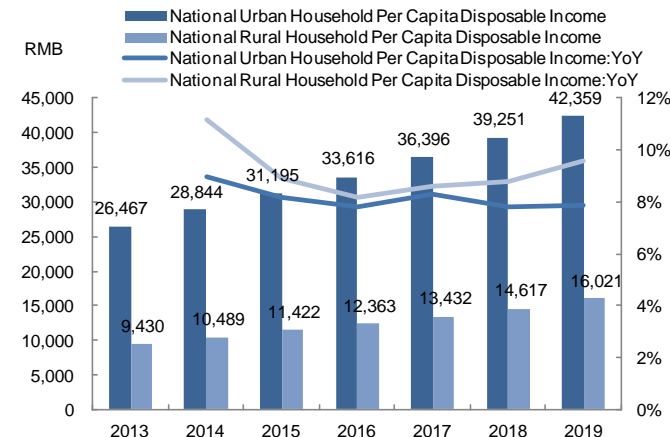
**Nowadays, China's individuals of working age have higher disposable incomes than their parents did.** Chinese consumers' income is rising rapidly, as a result, they have the potential to reshape global consumption as the baby boomer generation did in the West – the richest generation in history. The growth of per capita disposable income has long been faster than GDP growth in China. China's national per capita disposable income increased by 8.9% YoY in 2019 to RMB30,733, up 0.2 ppt YoY from 8.7% in 2018, according to the National Bureau of Statistics of PRC. Per capita disposable income has added up in both urban and rural areas, while the rural/urban ratio peaked in 2010 and reduced afterwards due to stronger rural income growth. We estimate that these trends will continue, in which urban consumers will spend a much greater share of their income on premium consumer goods and rural consumers will buy more consumer goods to meet their needs.

**Figure-126: China's National Per Capita Disposable Income & Growth**



Source: National Bureau of Statistics of China, Guotai Junan International.

**Figure-127: National Urban Household Per Capita Disposable Income & Growth and National Rural Household Per Capita Disposable Income & Growth**



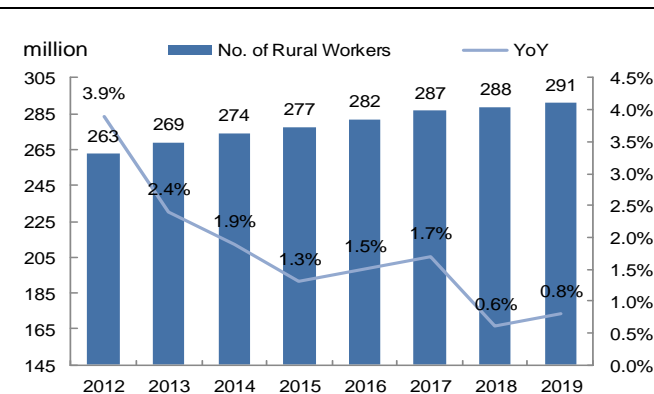
Source: National Bureau of Statistics of China, Guotai Junan International.

**The number of migrant rural workers in urban areas has decreased, but wages of rural workers continue to increase.** "The Report on Monitoring and Investigation of Rural Workers in 2018" showed that the total number of rural workers in China in 2018 was 288.36 million, up 0.6% YoY, but among rural workers, 135.06 million were employed in urban areas, down 2.04 million or 1.5% YoY. The main reason is that the first generation of migrant workers are getting older. If they cannot settle down in the city, they have to return to their hometown. According to statistics, the proportion of rural workers over 50 is 22.4%, up 1.1 ppts YoY. With the aging of the population, the average age of rural workers is also gradually increasing. The average age of rural workers was 38.6 years old in 2015 and reached 40.2 years old in 2018. In addition, the slowdown of the investment in infrastructure facilities and fixed assets has lead to reduced demand for labor. Due to the irreversible aging trend, the number of the working-age population will decrease in the future, and the increment of rural workers will also continue to decline. Due to the de-capacity of the manufacturing industry, rural workers in the secondary industry are gradually transferring to the tertiary industry. The proportion of the employed population of rural workers in the tertiary industry has exceeded 50%, with an increase



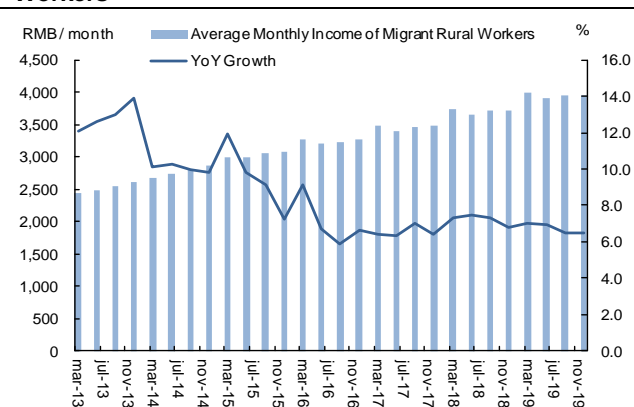
of 2.5% in 2018. The growth rate in catering, residential services, repair and other services, public management, social security and social organizations is especially fast. The new economy represented by e-commerce and lifestyle service e-commerce is booming in China, and the demand for the labor force is increasingly growing. In 2018, Meituan created 2.7 million delivery jobs and took over the jobs transferred from manufacturing. According to the 2018 "Express Team Insight Report", the total number of express delivery workers in China reached 3 million, absorbing many industrial workers. The income of migrant rural workers continued to rise; the average monthly income of migrant rural workers in 2019 rose 6.3% YoY.

Figure-128: No. of Rural Workers



Source: National Bureau of Statistics of the PRC, Guotai Junan International.

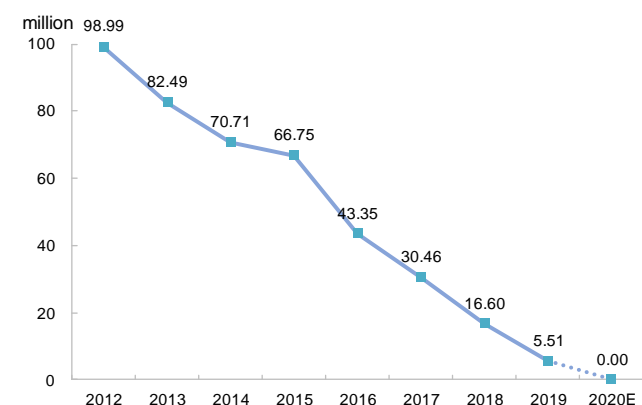
Figure-129: Average Monthly Income of Migrant Rural Workers



Source: National Bureau of Statistics of the PRC, Guotai Junan International.

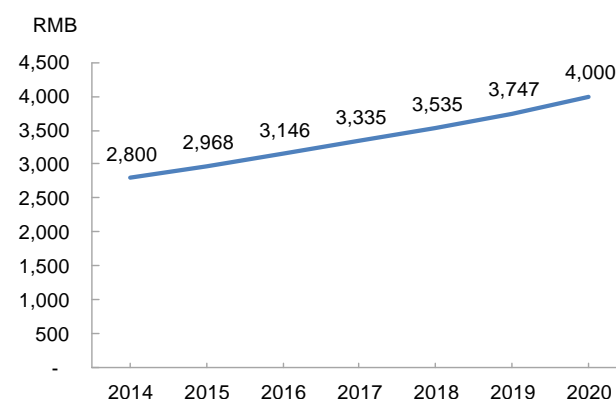
**China has achieved tremendous achievements in the fight against poverty, which has developed a new driving force for consumption growth.** The Chinese government defined the poverty standard as at RMB2,300 (at constant prices) of per capita annual income in 2011, which is equivalent to a nominal level of RMB3,747 in 2019. In this regard, a total of 93.48 million people have been lifted out of poverty since the fight against poverty was initiated in 2012. Only 5.51 million people in China still lived in poverty in 2019. The government expects to lift the whole population out of poverty, and plans to establish a well-off society. Per capita disposable income of rural residents in poor areas was RMB10,371 in 2018, up 10.6% YoY, while per capita consumption of these residents was RMB8,956 in 2018, up 9.3% YoY. Increasing purchasing power of low-income people is essential for boosting the demand for daily consumer goods. Such a target of poverty alleviation does not mean the end of improvement of undeveloped areas in China. The government has improved the living quality of low-income groups by raising minimum subsistence allowances and by expanding the coverage of rural endowment insurance. In terms of healthcare services, China has strived to offer essential medical services for poor people. Nowadays the rate of reimbursement of hospitalization for serious illnesses in rural areas has reached 90%. As absolute poverty gradually disappears, China enters into a new phase to overcome relative poverty. We anticipate that the goals of the next phase of China's poverty relief will include reducing the income gap between urban and rural areas and between the east and west. With the advancement of urbanization and the development of the western regions, the income of low-income groups is expected to increase, boosting consumption upgrade.

Figure-130: Population in Poverty



Source: National Bureau of Statistics of the PRC, the State Council Leading Group Office of Poverty Alleviation and Development, Guotai Junan International.

Figure-131: China's Poverty Standard



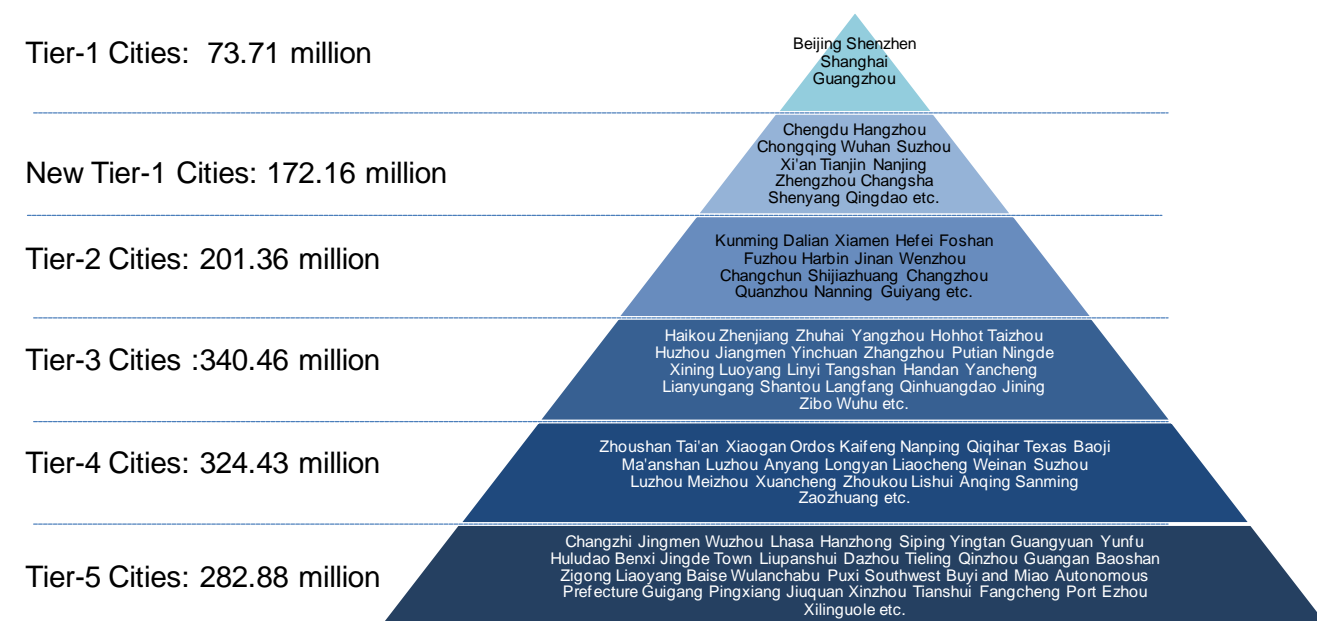
Source: National Bureau of Statistics of the PRC, the State Council Leading Group Office of Poverty Alleviation and Development, Guotai Junan International.



## How Changes in Consumer Geographic Distribution Impact Consumption

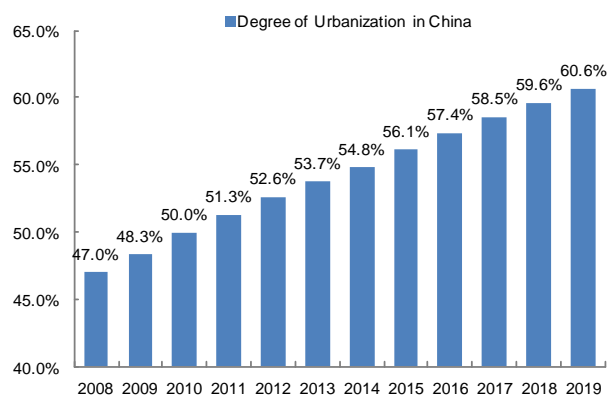
The urbanization rate is steadily advancing, which benefits consumption upgrade and the development of new consumption patterns. In 2019, the urbanization rate of China continued to increase steadily by 1.02 ppts YoY to 60.6%, but the level of urbanization rate of China's registered population is still low, only 43.37% in 2018. Among tier-one cities, Beijing and Shanghai still implement strict household registration policies, but Guangzhou and Shenzhen are already implementing looser settlement policies. In order to promote the urbanization rate of the registered population, the State Council proposed that all restrictions on household registration will be removed in smaller cities with an urban residential population of less than 3 million. Residency limits will be completely relaxed in cities with populations between 3 million and 5 million, while for cities home to more than 5 million, the household registration system will be simplified. Just like in hukou, new residents will be entitled to the same treatment in terms of education opportunities, employment and entrepreneurship, healthcare and social insurance, and housing scheme. Relaxing the restrictions in hukou has enabled more people from rural or undeveloped areas to migrate to larger cities, speeding up urbanization in China. Benefitting from the increasing size of population, new tier-1 and tier-2/tier-3 cities will reap demographic dividend over the next decade, therefore stimulating consumer demand and regional economic growth. Generally speaking, cities with higher per capita income and population density are the ideal places for the development of new consumption patterns. For example, on-demand food delivery, fresh food e-commerce, community group-buying, shopping malls, etc. are now rapidly developing in tier-1/tier-2 cities. Population density in urban cities in China was 2,426 people per square kilometer in 2017, over seven times that of the US. As a result, it takes 35 minutes for each delivery order in China compared to 75 minutes in the US. China's urbanization is far from over, especially that the urbanization level of the registered population has a lot of room for improvement. China's new consumption patterns will also develop even better.

Figure-132: Number of Residents in Different Tier Cities



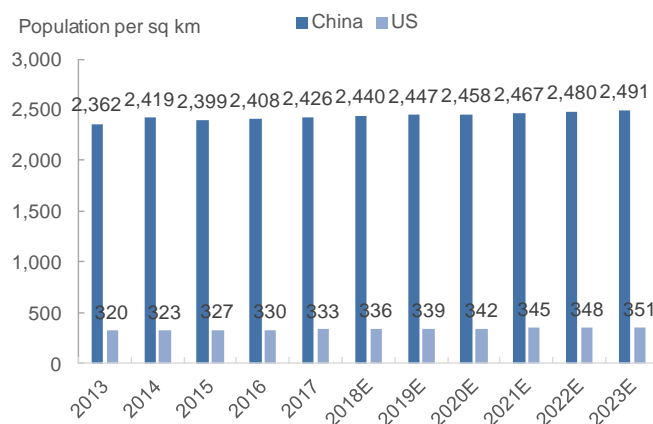
Source: National Bureau of Statistics of the PRC, Guotai Junan International.

**Figure-133: Degree of Urbanization in China**



Source: National Bureau of Statistics of the PRC, Guotai Junan International.

**Figure-134: Population Density in Urban Cities in China and the US**



Source: iResearch.

21 February 2020

Consumer Sector-Food & Beverage 消费行业-食品饮料

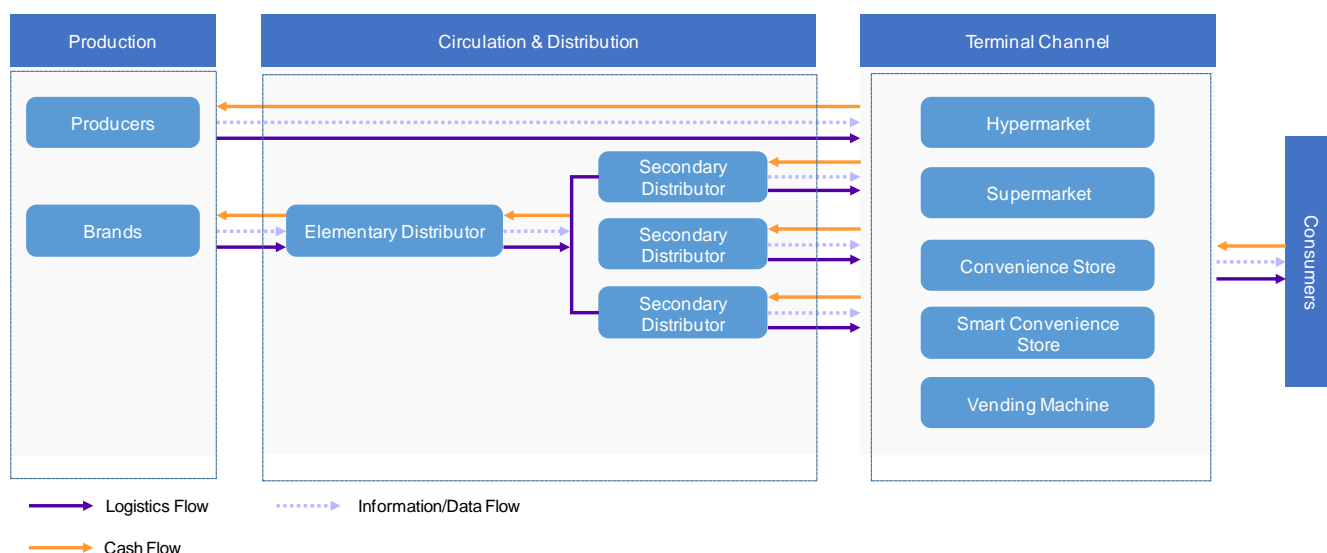
Sector Report

## How Changes in Sales Distribution Channels Impact Consumption

**China's vast territory and multi-tiered cities have made distribution channels of consumer products very complex.** According to the National Bureau of Statistics, in 2019, China's population was 1.40 billion, spread over an area of 9.60 million square kilometers. Tier-1, new tier-1, and tier-2 cities, with robust spending power of residents and well-developed distribution channels, amounted to 49 cities and 450 million people. However, 360 cities, 2,800 counties, 40,000 towns, and 600,000 villages in China's lower-tier cities still contain another 950 million people. In tier-1 and tier-2 cities, the local market is dominated by modern trade (such as supermarkets, supermarket chains and convenience stores) as shopping experience in modern trade is more comfortable, despite the fact that the operating cost of modern trade is higher. High-tier cities are densely populated, and the stronger purchasing power can offset the higher operating cost of modern trade. In addition, for brand owners, high entry cost into modern trade (e.g. various fees paid to retailers) results in lower profitability. However, modern trade has the function of exhibitions, advertising and promotion, which are also essential for brand owners. China has 6 million traditional small mom and pop stores, with 93% opened in tier-3 and tier-4 cities, towns and villages. Due to the scattered distribution of residential population in low-tier cities in China, traditional channels are able to conduct multi-level and low-cost distribution, which can be vital for FMCG companies. Even in high-tier cities, there are still a variety of small stores to be connected through traditional channels.

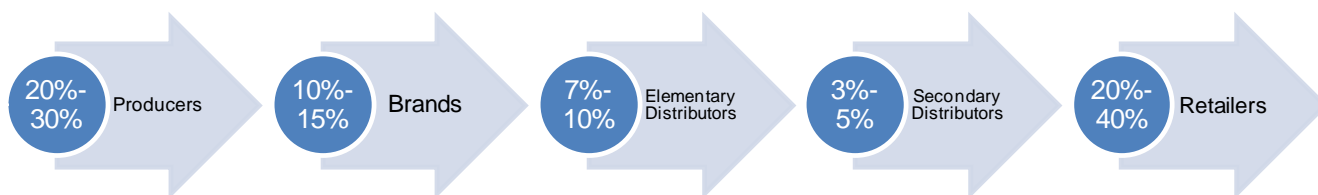
**Channel advantages is an economic moat of leading enterprises, but it is now being challenged.** In the past, the rapid growth of leading FMCG companies was driven by large-scale production and large-scale distribution helped by distributors, which enable FMCG companies to reach consumers by offering the lowest prices. Traditional channels are usually the profit-generating sources for brand owners. Leading companies, such as Coca-Cola, Tingyi, and Yili, manage thousands of first-level distributors, hundreds of thousands of second-level distributors, and millions of retail outlets. Such a channel advantage is undoubtedly an economic moat that other competitors can hardly achieve in the short run. Consumers used to have lower self awareness and be easily influenced. Therefore, in the past, the FMCG industry was dominated by the winners in these channels. Traditional channels, at their peak, accounted for over 50% in sales of dairy products and 40% in sales of packaged foods and soft drinks. Drastic channel changes over the past decade have reduced the proportion of traditional channels. Traditional channels involve multi-level distribution, which is inefficient and relies too heavily on the low-cost operation of secondary distributors. However, with rises in labor costs, storage and transportation costs, the gross profits earned by secondary distributors could no longer cover their costs. The decline in revenue and sales growth, together with the elimination of old distributors, has weakened the role offered through traditional channels.

Figure-135: Distribution Chain in the FMCG Industry



Source: JINGDATA, Guotai Junan International.

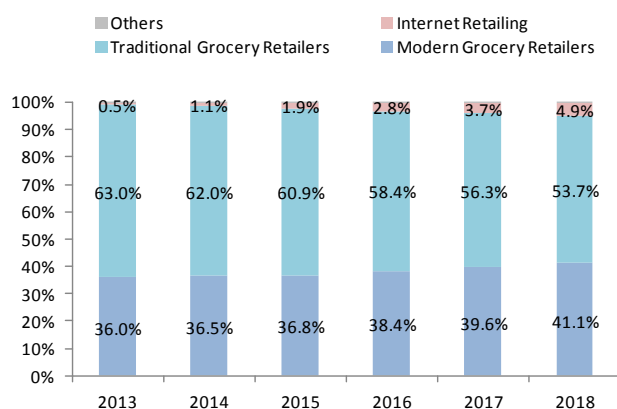
Figure-136: Value Chain of FMCG (Gross Margin Gained by Each Participant)



Source: JINGDATA, Guotai Junan International.

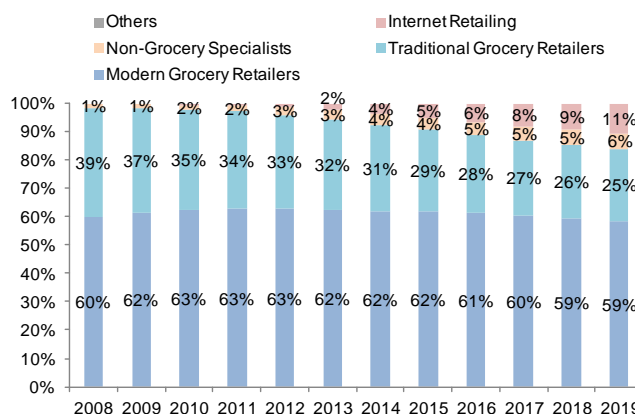
**The rise in new retail has built more fragmented channels.** In the past decade, distribution channels in China have experienced drastic changes. The main reason is that post 1980 and post 1990 had consumer habits change. Traditional channels were less attractive because of the uncomfortable shopping experience. With the acceleration in urbanization progressing and the continuous enhancement of infrastructure, the layout of modern trade has become wider. We observe that modern trade is increasingly replacing traditional channels. However, the rise of e-commerce channels eroded market share of modern trade. Different from other sectors such as clothing or electronics, the F&B sector basically has lower online penetration rate, especially for impulsive-consumption sub-sectors such as beer and soft drinks. But online penetration of food & beverage has started to go up in recent years, especially for those packaged foods and dairy products, and even fresh food, achieving rapid growth and online presence. Fresh food e-commerce platforms with on-demand delivery, such as Missfresh, Ding-Dong Maicai, and Hema, have attracted a large number of new clients due to the fast and convenient experience, although their operations are quite costly. Specifically, during the outbreak of the NCP epidemic, online shopping of fresh food has become the first choice for many consumers. The rise of new retail, represented by Hema, Ding-Dong and Missfresh, further weakened traditional supermarkets, represented by RT-Mart and Wal-Mart, in terms of revenue growth and profitability. To meet these rapidly-changing consumer needs, RT-Mart and Wal-Mart begun to cooperate with companies having strong O2O distribution capabilities, such as Alibaba and Meituan, and have strived to survive the new-retail shock. However, we see that convenience stores and community fresh supermarkets, operating purely offline, have greatly satisfied consumers' daily needs and reported rapid growth as well. The transformation of traditional channels is also underway. FMCG B2B platforms, including Alibaba LST and JD XTL, are optimizing the existing system of distributors in traditional channels. These platforms use advanced data management technology to improve efficiency and shorten the layers of distribution.

Figure-137: Fresh Food Sales Breakdown by Channel in China



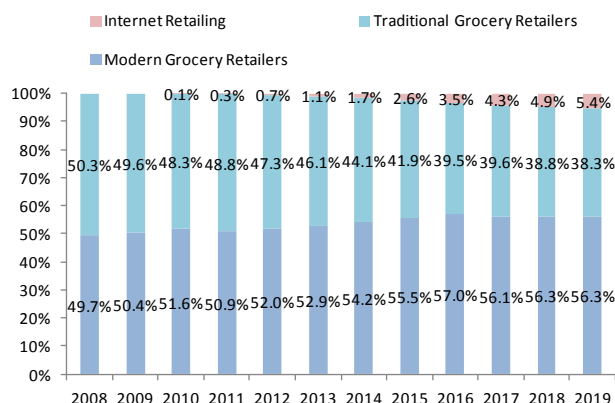
Source: Euromonitor, Guotai Junan International.

Figure-138: Packaged Food Sales Breakdown by Channel in China



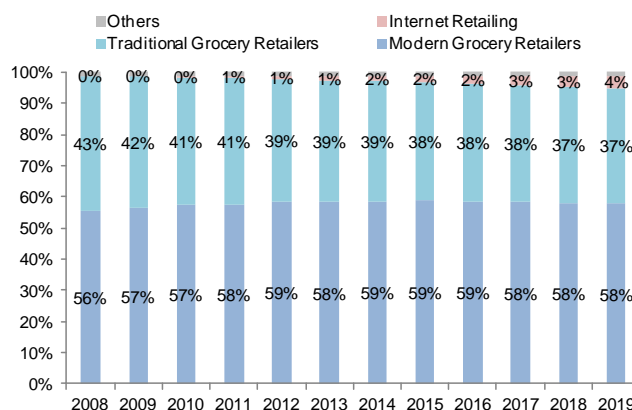
Source: Euromonitor, Guotai Junan International.

**Figure-139: Drinking Milk Sales Breakdown by Channel in China**



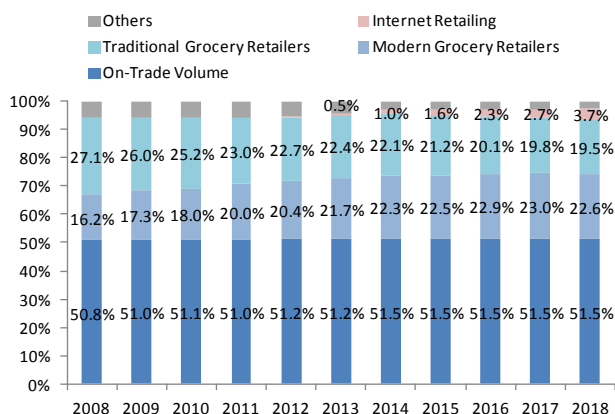
Source: Euromonitor, Guotai Junan International.

**Figure-140: Soft Drinks Sales Breakdown by Channel in China**



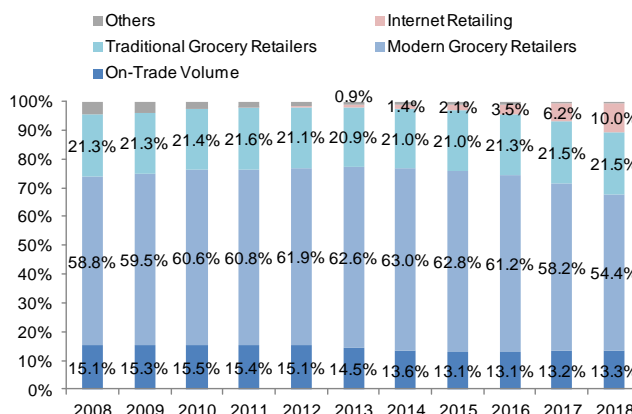
Source: Euromonitor, Guotai Junan International.

**Figure-141: Beer Sales Breakdown by Channel in China**



Source: Euromonitor, Guotai Junan International.

**Figure-142: Spirits Milk Sales Breakdown by Channel in China**



Source: Euromonitor, Guotai Junan International.

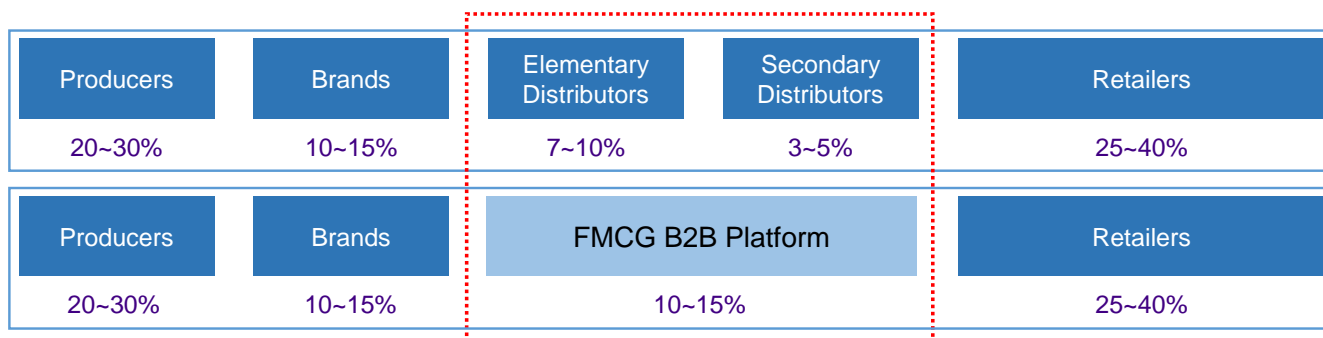
**Diversification of channels is not a bad thing for brand owners, but needs to be fully adapted.** We expect that China's distribution channels will become more diversified with the proportion of e-commerce expected to further increase; the development of new retail cannot be stopped. Diversification of channels is not a bad thing for brand owners as they can have a wider range of choices for distribution. Many emerging channels also hope to being backed by influential brands. The more fragmented the channel, the lower the concentration and thereby the greater the bargaining power of brand owners. In the United States, due to the higher concentration of retailers, the bargaining power of brand owners is relatively low, making it difficult for small brands to survive. Besides supermarkets, more and more new business models in modern channels have emerged, further reducing the concentration of the retail sector and hence benefitting brand owners. Despite the increasing expensive traffic costs and marketing expenses via online channels, new online platforms like Pinduoduo may still be an alternative for brand owners. On the other hand, newly-emerged channels also weakened the channel advantages of leading companies to some extent, giving smaller brands more opportunities to reach consumers. Given that different channels may require different ways of operation, brand owners, especially leading companies, need to improve their operating capabilities within multi-channels.

## FMCG B2B E-Commerce Platform

**The internet has empowered the transformation of traditional channels.** FMCG B2B e-commerce platforms that emerged in 2016, such as Alibaba LST, JD XTL, and many other smaller-sized platforms, have had a profound impact on China's traditional channels. The goal of these platforms is to become a direct bridge between FMCG brands and retail points, and to improve distribution efficiency by reducing the number of layers of the previous multi-layer distribution system. These FMCG B2B e-commerce platforms can provide integrated services for retail stores by distributing multiple categories of goods at one time, which will greatly improve distribution efficiency and eliminate unnecessary labor costs. As China's FMCG market is huge and traditional channels have great room to optimize, a large number of enterprises have started their own FMCG B2B e-commerce platforms, including 1) platforms built by internet giants, e.g. Alibaba LST, JD XTL; 2) platforms built by start-ups, e.g. Jiuxian.com, and Yijiupi (易久批); 3) platforms built by brand owners, e.g. Xiaokang Buy (Haitian), Cola GO; and 4) platforms built by retailers and B2B distributors, e.g. RT-Mart e-Lufa. In 2016, hundreds of FMCG B2B platforms started their business by raising capital and expanded rapidly via extensive subsidies. The market in lower-tier cities involves more than 360 cities, 2800 counties, 40,000 towns, and 600,000 villages, and covers more than 900 million people in China. To cover all users in China, FMCG B2B platforms need tens of thousands of warehouses, hundreds of thousands of vehicles for distribution, and millions of workers in relevant areas. Self-operated platforms may also need a large sum of money for purchases at the very beginning. In addition, they have to use low-pricing strategies to attract new users. Due to homogeneity and fierce market competition, FMCG B2B e-commerce platforms failed to maintain their profitability and to attract external investors.

**The concentration of FMCG B2B platforms will increase, which is a mixed sign for brand owners.** According to Linkshop's data, the number of financings in the field of FMCG B2B has dropped since 2016, and the entire market has encountered a 'capital winter' since 2019. The intensified market competition and the difficulty in acquiring funds have led to a reshuffle of the industry. Many FMCG B2B platforms went bankrupt, including Hui Xiadan (invested in by Tencent). Overall, the FMCG B2B platform's transformation from traditional channels was worse than previously expected, mainly because the compliance costs of FMCG B2B firms are higher than those of traditional distributors. Without the help of brand owners, platforms are faced with higher procurement costs of goods. The reshuffle of the industry is undoubtedly good for the giant firms, because FMCG B2B is an industry with significant scale effect. Large-scale firms have greater bargaining power upstream and downstream. The B2B e-commerce platforms, represented by JD XTL, bypass distributors and set up an independent warehouse logistics system to deliver goods to retail points. The B2B e-commerce platforms, represented by Alibaba LST, choose to cooperate with distributors to integrate warehousing and logistics systems so that the unified system can schedule to achieve rapid business expansion. However, in this way, distributors may be downgraded to logistics partners for FMCG B2B e-commerce platforms. Many brand owners, with solid distribution systems, may refuse to cooperate with FMCG B2B e-commerce platforms due to cost-benefit analysis. If the FMCG B2B industry is monopolized by one or two players, which may weaken channel strength of leading brand owners. Other brand owners, without solid distribution systems, are actively cooperating with FMCG B2B e-commerce platforms in the hope to distribute their products to more offline stores, and brand owners can effectively control marketing expenses and enhance the 'know-your-customer' processes on the basis of instant data and feedback from FMCG B2B e-commerce platforms.

**Figure-143: Value Chain of FMCG B2B Platform**



Source: JINGDATA, Guotai Junan International.

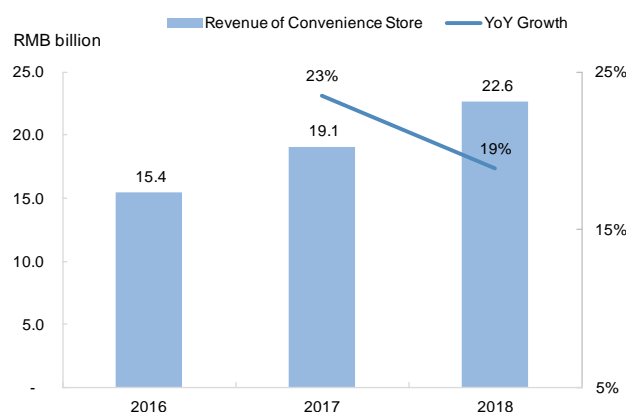


## Convenience Stores

**Convenience stores have been a critical channel for new consumer brands.** According to the China Chain Store & Franchise Association's report, in 2018, revenue of China's convenience stores reached RMB226.4 billion, up 19% YoY; the number of stores reached 120,000. Average sales of a single store per day is now around RMB5,300, up 7% YoY. Profitability improved slightly in 2018, but operational capability and supply chain efficiency still needs to be strengthened. We see that the product mix of convenience stores was optimized and that the proportion of self-owned brands largely increased. In terms of the supply side, despite rapid growth of the industry scale of China's convenience stores, its market share is relatively low as compared to other retailing channels. Meanwhile, the number of residents per store in mainland China is far lower than that in Japan/ Taiwan/ South Korea (2,200 persons per store in coverage). In terms of the demand side, with the advancement of urbanization, the accumulated density of urban population has formed a huge consumer base and demand potential. We forecast that the convenience store industry will be boosted in China's tier-4 and above cities. Thanks to the rapid growth of per capita income, the per customer transaction continues to rise. The increasing popularity of convenience stores benefits the development of new consumer brands, as the average age of convenience stores' major customers is relatively young, which has higher acceptance toward fancy new consumer brands. The new beverage brand, Yuanqi Senlin (元气森林), achieved robust sales growth with the help of mass distribution in the convenience store channel.

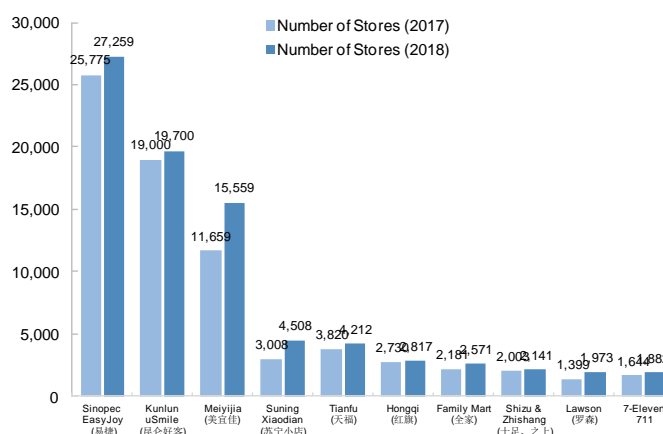
**The number of convenience stores from petroleum companies lead; Franchise has become the mainstream.** According to a report by the China Chain Store & Franchise Association, Sinopec Easy Joy, Kunlun uSmile, and Meiyijia, ranking as top three, which owned 27,259, 19,700, 15,559 stores by the end of 2018, respectively. Suning Group, as one of the new entrants, accelerated the expansion of Suning Xiaodian stores since 2017. Family Mart, Lawson, and 7-Eleven raised the number of their stores by 18%, 41% and 14% to 2,571, 1,973 and 1,882, respectively. Key drivers include: 1) wider acceptance of the convenience store franchise system; 2) strengthened business localization, e.g., cooperation with mainstream e-commerce/ distribution platforms such as Meituan; and 3) implementation of new-retailing models, including AI services, deformed shelves, online-to-offline sales, and brand intellectual properties. The franchise system has been widely enhanced and the business trend has been led by top players in China's convenience store sector. We expect an ongoing increase in concentration ratio of China's convenience store market. Major participants in regional markets, such as Tianfu, Hongqi, and Quik slowed down their expansion of stores in 2018.

**Figure-144: Revenue of Convenience Stores & YoY Growth**



Source: China Chain Store & Franchise Association, Guotai Junan International.

**Figure-145: Number of Stores by Convenience Store Brand**



Source: China Chain Store & Franchise Association, Guotai Junan International.

## Chain Community Fresh Foods Supermarket

**Chain community fresh foods supermarkets have an edge: strong connection with consumers and standardized management.** Its further developments rely on the supply chain integration. Compared with traditional supermarkets, chain community fresh foods supermarkets are usually located within communities, providing the most convenient shopping experience for consumers. Compared with local fresh food stores, chain community fresh foods supermarkets have an edge of standardized management and large-scale procurement. The operating area of community fresh foods supermarkets are usually around 400-600 square meters, and fresh foods account for over 60% of sales. Since chain community fresh food stores rely on the expansion of physical stores, this business model usually has high rental costs and store operating expenses. Moreover, in order to achieve higher profit margin and sustainable growth, players need to get access to upstream agricultural products procurement. This requires more on supply chain integration capability.

**Qian Dama, Yipin Shengxian and Shengxian Chuanqi have tapped into community fresh foods supermarkets.** Qian Dama opened its first store in Dongguan in 2012. Benefitting from its efficient franchise and sales competence, Qian Dama has opened more than 1,600 stores as at September 2019. Yipin Shengxian was first established in Hefei in July 2017, and then expanded mainly in Hefei and Chongqing. As at the end of 2018, Yipin Shengxian had 610 stores with more than 18,000 employees. In March 2019, the company finished its RMB2 billion fund raising, which was led by Tencent, with a total estimated value of RMB20 billion. Since then, the company accelerated its nationwide expansion. Shengxian Chuanqi was founded in 2015 and is geographically concentrated in Hefei. As at April 2019, it had 107 stores in Hefei and announced that over 500 stores would be opened in the coming future. On October 10, 2018, Shengxian Chuanqi completed its series B fund raising and had a total estimated value of over RMB3 billion. After completing its B+ round of financing led by Jiashi Investments in July 2019, the company strengthened its store network and supply chains and looked forward to the new shares listing for the next step. In view of product categories, Yipin Shengxian and Shengxian Chuanqi's products primarily contain fruits, vegetables, meat and eggs, which in total account for over 70% of all categories, while Qian Dama focuses on meat and vegetables. Meanwhile, the three players have built sound supply chain systems, and are able to access upstream channels for procurement to some extent. In addition, with its further standardization of branding and operational capacity, the companies tend to accelerate expansion driven by capital.

## Fresh Foods E-Commerce Platforms with Pre-positioned Warehouses

**During the NCP epidemic, fresh foods e-commerce platforms grew explosively.** Fresh foods e-commerce platforms set up pre-positioned warehouses within communities and had their own delivery riders, which enabled them to reach customers efficiently, since products are able to be delivered directly from pre-positioned warehouses to customers' homes within 30 minutes to one hour. On one hand, the pre-positioned warehouse model enjoys low rental costs, low store operating expenses and low decoration costs as the expansion does not depend on physical stores. In addition, benefitting from high efficiency of inter-warehouse transportation, pre-positioned warehouses can reduce transportation breakdowns during cold chain transportation, helping food remain fresh. High efficiency in cold chain transportation and fast delivery are the strengths for fresh foods e-commerce. However, players adopting pre-positioned warehouses generally suffer from high delivery costs and marketing expenses. Due to the low transaction value per order and low gross margin of fresh foods, players in the field so far had difficulty to earn profit. However, just as investors have begun to have doubts about the fresh e-commerce model, the outbreak of the NCP epidemic has resulted in the explosive growth of fresh e-commerce. For example, in January, the GMV of Ding Dong Maicai increased 8-10 times YoY, and value per order increased from RMB60 to RMB100. After the NCP epidemic outbreak, residents have been restricted from going out, and fresh e-commerce has become the most convenient and safest way to buy fresh foods. Just as the SARS epidemic promoted e-commerce growth, this NCP epidemic will also accelerate the acceptance of consumers toward buying fresh food online.

**Missfresh, Ding Dong Maicai and Pupu Mall are three leading fresh foods e-commerce players.** Established in November 2014, Missfresh is an early player using pre-positioned warehouses. Its logistic system includes city sorting center and community pre-positioned warehouses. Currently, Missfresh has more than 1,500 pre-positioned warehouses and its quick delivery service has covered more than 20 cities (mainly high-tier cities). Missfresh has optimized its location and improved penetration via cooperation with Tencent Smart Retail. And intelligent sorting and distribution orders help it achieve average delivery time of less than 36 minutes. Different from Missfresh, Ding Dong Maicai, established in April 2017, has adopted a model of "local procurement + pre-positioned warehouses". As at November 2019, Ding Dong Maicai had 345 pre-positioned warehouses. Pupu Mall was founded in June 2016 in Fuzhou. Pupu Mall covers most areas of Fuzhou and its neighboring city, Xiamen. Next, it will focus on expanding in the Shenzhen market where 1-2 new warehouses will be established per week. Missfresh, Ding Dong and Pupu Mall have experienced 8, 9 and 4 rounds of funding since establishment, respectively. In common, the three players have pre-positioned warehouses concentrated in the tier-1/tier-2 cities. Regarding expansion, they choose to root deeper and gain competitive advantages in mature markets first before expanding other new cities.

### Supermarkets with On-demand Delivery Ability.

**Supermarkets with delivery ability have advantages and disadvantages of community fresh foods supermarkets and fresh foods e-commerce.** In such a model, supermarkets can function as pre-positioned warehouses which satisfy customers' 'delivery to home' demand. In the meantime, supermarkets are able to not only satisfy customers' in-store experience which strengthens branding, but also guarantee a high retention rate by converting offline traffic to online platforms. Usually, supermarkets with delivery ability have a larger area and provide more SKU compared with the community supermarket model or pre-positioned warehouses model. However, the integrated model has common disadvantages from community supermarkets and fresh foods e-commerce platforms. In general, supermarkets with delivery ability model are the most comprehensive model in new retail business, but it faces challenges from both store operations and logistics.

**Hema supermarket is a representative of supermarkets with delivery ability model.** Supported by Alibaba's strategic investment, Hema accelerated its development in China. As at December 12, 2019, Hema had 200 stores. Besides expansion of its own brand, Hema jointly operated with Sanjiang Shopping, New Huadu and RT-Mart. In June 2018, Hema also accelerated expansion by leasing Shirble's 12 supermarkets in Shenzhen. Hema is remarkable for its outstanding operating efficiency and high technology, but due to high store operating costs, it still suffers from loss to some extent and can only claim breakeven for some of its mature supermarkets in tier-1/tier-2 cities. From 2019, Hema has gradually slowed down expansion, while 7 Fresh, Xiaoxiang Shengxian experienced stagnation of expansion. more refined operating capability would be the key to achieve profitability.

### Community Group Buying

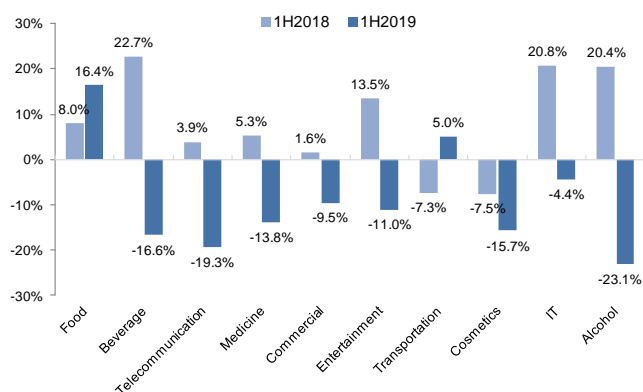
**Community Group-buying is a retail model that relies on social networks.** Every community is an independent unit for community group buying, where group representatives (usually a housewife or the owner of grocery shop in the neighborhood) establish WeChat groups for customers to place orders and take care of the last kilometer of delivery, while products, logistics, storage and after-sales services are provided by community group-buying platforms. In community group buying, customer acquisition costs are low due to sales that are based on network of acquaintances. Meanwhile, distribution costs remains low due to order concentration, and low store operating costs can be achieved without physical stores. However, this model is highly dependent on group representatives, resulted in low scale effect. Besides, community group-buying platforms in this model also have problems regarding limited SKU and inefficiency of supply chain management. Hence, community group buying may gradually adopt community supermarkets or pre-positioned warehouses in the future instead of being an independent business format. On the other hand, the players in community supermarkets or fresh foods e-commerce might also develop their group-buying business.

**With the rapid development of community group-buying business, e-commerce giants have begun to tap in.** Xingsheng Youxuan (兴盛优选) was founded by Furong Xingsheng (芙蓉兴盛) which is a famous convenience store brand in Hunan. Xingsheng Youxuan initiated the model of "small online shopping platform + community convenience stores" in June 2016. Its GMV in 2019 is expected to reach RMB10 billion. Since Meijia Youxuan's (美家优选) establishment in June 2018, it quickly expanded to 40 cities and has developed to have nearly 10,000 group representatives within 3 months. After transforming and upgrading to Meijia-Maica (美家买菜), the company announced the "Spark Fire for Million Dollar Plan" so as to quickly improve its presence in the local communities. As the development of community group buying, a situation of housewives as group representatives gradually vanished due to the instability of housewives as group representatives. Instead, players in the field began to root in community convenience stores and establish their reliable training system for group representatives. On the other hand, e-commerce giants also have seen the opportunities and launched their community group-buying services. In January 2019, Taobao launched "Yizhan Group-buying" (驿站团购) as a mobile app; Suning launched "Suxiaotuan" (苏小团), and aggressively recruited group representatives; in February 2019, Missfresh launched "Meiri Pinpin" (每日拼拼). In December 2019, JD joined hands with the Guangdong retail giant, Tianfu, to enter the community grouping-buying market.

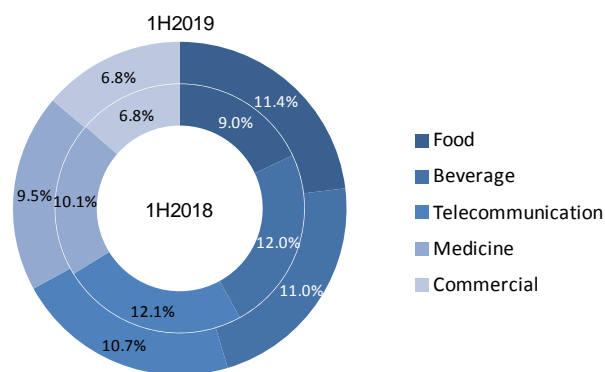
## How Changes in Media Impact Consumption

**Brand building has become more critical.** Although a number of industries are cutting their advertising expenses as a response to the slowdown in economic growth, food and beverage sectors have bucked this trend. According to CTR data, in 1H2019, food and beverage sectors contributed 11.4% and 11.0%, respectively, of total advertising expenses, which ranked top 2 among all sectors. As food and beverage sectors are featured by higher frequency of consumption, brand owners need to continually use advertisements to influence consumer behavior. Over the past decade, consumers are becoming strong-minded in making buying decisions so that retailers have become an increasingly unimportant role in product recommendations. Influential brands, such as Moutai, Haitian, Yili and Mengniu, Coca-cola, Tingyi and Shuanghui, are highly valued among consumers so that these brands can generate more sales without the help of retailers. Given the ever-changing landscape of distribution channels, many food and beverage brands have been aware of the importance of brand building as a tool to raise their bargaining power over various distribution channels. Also, they have to enhance their communication with consumers to consolidate their brand values. Although brand value may not be fully reflected on their financial statements, it is a most important asset for FMCG companies, which can be monetized in the future. Most of the HK-listed F&B companies we cover are allocating more resources towards brand building and marketing instead of promotion in channels.

**Figure-146: Advertising Spending YoY Change of Top 10 Industries in 1H2018 and 1H2019** **Figure-147: Advertising Spending Breakdown by Industry**



Source: CTR, Guotai Junan International.



Source: CTR, Guotai Junan International.

**Table-3: Brand Value of Chinese Food & Beverage Brands**

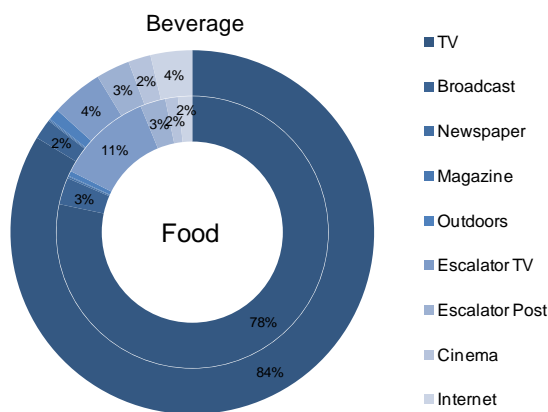
Rank in F&B	Rank	Brand	Category	Brand Value (USD Million)	% Brand Value Change
1	5	Moutai (茅台)	Alcohol	36,555	58%
2	13	Meituan (美团)	Internet Services	19,918	n.a.
3	22	Yili (伊利)	Food & Dairy	9,068	19%
4	24	Ele.me (饿了么)	Internet Services	7,269	n.a.
5	27	Mengniu (蒙牛)	Food & Dairy	6,760	26%
6	37	Dianping (大众点评)	Internet Services	3,846	n.a.
7	40	Wuliangye (五粮液)	Alcohol	3,715	69%
8	48	Yanghe (洋河)	Alcohol	2,864	41%
9	49	Shuanghui (双汇)	Food & Dairy	2,829	9%
10	62	Snowbeer (雪花)	Alcohol	1,818	53%
11	64	Luzhou Laojiao (泸州老窖)	Alcohol	1,644	-7%
12	67	National Cellar 1573 (国窖 1573)	Alcohol	1,426	40%
13	69	Tsingtao Brewery (青岛啤酒)	Alcohol	1,341	5%
14	75	Harbin Beer (哈尔滨啤酒)	Alcohol	1,141	-9%
15	88	Changyu (张裕)	Alcohol	885	-7%
16	91	Gujing Distillery (古井贡酒)	Alcohol	802	33%
17	99	By-Health (汤臣倍健)	Healthcare	694	17%

Source: Kantar, Guotai Junan International.

**Diversified advertising media channels have challenged national brands.** Given that the whole population is the potential market for food & beverage, national brands used to advertise their products to consumers via CCTV TV channel and local TV channels. Given the lowest unit cost, TV advertisements were widely used by leading FMCG companies over the past decades and still play a relatively large part in today's food & beverage advertisement. According to CTR data, in 1H2019, TV advertisement spend in China's food & beverage industry accounted for more than 75% of total advertising spent, far exceeding the percentages in other industries. However, with the fast development of the Internet and mobile Internet, media channels have become more fragmented, and attention of consumers has been dispersed, reducing the size of TV viewers and weakening the effectiveness of TV (as a conventional advertising way) for leading food & beverage companies. We see that food & beverage companies have spent more on advertising, especially through many other new media channels. However, fragmented media is detrimental to leading F&B companies' advertising activities. Since media fragmentation has narrowed the social circle of their clients, national food and beverage brands find it necessary to launch advertisements through every media channel in order to reach more people, instead of communicating with consumers only through TV just like in the past. As a result, advertising expenses of food & beverage companies have surged. And, some well-developed brand owners are less aware of the rise in new media channels so that there may be a gap between these brands and the young customers. Nevertheless, diversified advertising media channels also can be beneficial for many leading brand owners to promote their new and innovative products by precisely targeting potential consumer groups. We noticed that many leading brands achieved huge success by sponsoring hot reality shows and sports TV programs, but it is difficult to predict the audience ratings of TV programs before sponsoring.

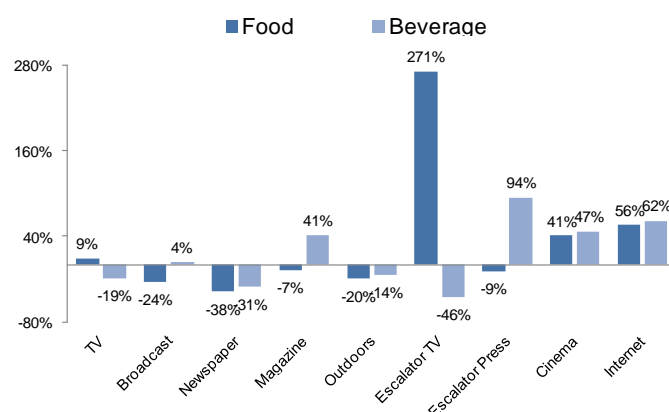


**Figure-148: Advertising Spending of Food & Beverage Industry Breakdown by Media**



Source: CTR, Guotai Junan International.

**Figure-149: Advertising Spending YoY Change of Food & Beverage Industry in 1H2019**



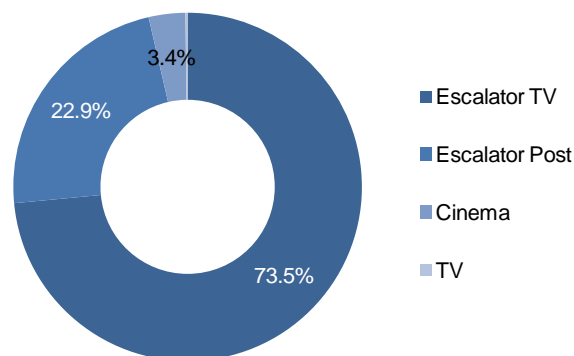
Source: CTR, Guotai Junan International.

**Figure-150: Brand's Advertisement Expenditure Rank in CCTV**

Brand	Category	YoY Growth
Feihe 飞鹤	Food & Dairy	297.3%
Zulijian 足力健	Apparel	-24.9%
Xiaoguantea 小罐茶	Tea	-6.6%
Tongyitang 同溢堂	Medicine	131.0%
Junlebao 君乐宝	Food & Dairy	8.9%
Mengniu 蒙牛	Food & Dairy	87.1%
Yili 伊利	Food & Dairy	43.3%
Luhua 鲁花	Food	3.7%
Huawei 华为	Technology	8.9%
Changlong 长隆	Entertainment	544.9%

Source: CTR, Guotai Junan International.

**Figure-151: Luckin's Advertisement Expenditure Breakdown**



Source: CTR, Guotai Junan International.

**Diversification of media channels has provided opportunities to new consumer brands.** In the era of TV advertising, national brands monopolized TV advertising resources because new consumer brands could hardly afford high advertising costs on CCTV. However, the rise in new media channels has greatly benefited new consumer brands. Now they can reach their consumer groups through low-cost and customized advertising. Unlike national brands, new consumer brands do not need to advertise to the mass of public at higher costs, but instead, they only need to reach a few of targeted consumer groups. Given that consumers' entertainment time has become fragmented, a lot of new advertising types are emerging, from elevator ads and search engines to short videos, live streaming e-commerce, Xiaohongshu and personal IP brands. Diversification of media channels enables new consumer brands to stay much closer to their potential customers and away from competition with large national brands. But as cheap traffic from new media channels gradually disappear, new media channels may be subject to the 'head effect', which means the market will be dominated by those top brand owners with abundant resources.

### Live streaming E-commerce

**Live Streaming e-commerce has strong selling ability as well as excellent promotion ability.** Since 2016, leading internet platforms, such as Taobao, JD.com, Dou Yin (Tic Tok), Kuai Shou, launched their live streaming functions, generating additional traffic and revenue through live streaming sessions. According to Alibaba, in 2019, the daily average number of Taobao live streaming sessions reached 60,000. The total GMV reached RMB100 billion in 2019 and is expected to exceed RMB250 billion in 2020. In 2019, 81 live streaming hosts each created more than RMB100 million in sales, and the sales conversion rate was higher than 60%. Taobao's top-selling live streaming host, Viya generated a GMV of more than RMB2.7 billion in 2018. During the 2019 Double-Eleven shopping festival, Viya herself promoted RMB267 million in sales for the first two hours, and attracted nearly 40 million viewers in total. Revenue generated by another popular host Li Jiaqi (李佳琦) also exceeded RMB1 billion on that day. On 5 January 2020, Li, his live streaming session attracted 16.77 million viewers and sold 100,000 packets of Jinzi Ham's spicy

sausages within 5 minutes. Thanks to the broader influence of KOLs over their audience as well as the immersive experience by content marketing, live streaming e-commerce has a clear advantage over the traditional one in terms of the traffic density. Live streaming not only helps build brand awareness, but in turn brings lower cost of goods purchased and builds a positive reputation for head hosts. Live streaming has taken an increasingly important part in consumers' shopping activities. We estimate that live streaming will continue to be included in traditional e-commerce channels as well as social networking, short video and life services platforms. Eventually, live streaming e-commerce will act as an essential role in introducing new products for well-known brands and also promoting niche products for emerging brands. For brand owners, their profit from selling products during live streams cannot cover the cost paid to the host, but live streaming plays a very effective promotion role as a large number of viewers watch, making brand owners willing to pay high sponsorship fees.

Figure-152: Live streaming Channel of Lijiaqi (李佳琦)



Source: Taobao, Guotai Junan International.

Figure-153: Live Streaming Channel of Viya (薇娅)



Source: Taobao, Guotai Junan International.

## Xiaohongshu

**The shares of KOL in Xiaohongshu has shortened the time for consumers to trust its new brands and new products.**

Xiaohongshu, also known as RED, is a social media and e-commerce platform created in 2013, allowing users to create wish lists, shop online, and post product reviews and lifestyle stories. Xiaohongshu presents user-created content via short videos and photos, and the number of times of content is presented per day exceeds 4.5 billion. According to Xiaohongshu, RED community had more than 300 million registered users by July 2019, of which most are post-1990 females, and MAUs reached 85 million. Consumers with similar needs and buying habits are gathered in RED communities, where they are able to use their fragmented time to browse reviews and share stories. By inserting purchase links into RED posts, Xiaohongshu successfully converts the consumer's interests into sales. More and more consumers agree with Xiaohongshu's unique value in improving decision-making and providing emotional resonance. KOLs from RED communities not only reflect the current changes in consumer attitudes, but creates fashion trends. In recent years, Xiaohongshu has helped build a large number of new brands, including Chicecream, Perfect Diary, Grain Rain, Judy Doll, Maia Active, etc. Thanks to the rise of Guochao (the "national hip"), domestic consumer brands are quickly gaining market share and popularity (e.g. new releases, search clicks). In our view, this trend will continue, and an increasing number of new products and brands customized for Chinese consumers will emerge, especially in consumer sectors.

## Personal IP Brand

Li Ziqi (李子柒), one of China's most popular video bloggers, focuses mainly on traditional Chinese food culture where she traces the roots of diet and food ingredients, and fully demonstrates the Chinese pastoral lifestyle. Over 22 million, 35 million, and 8 million followers (subscribers) on Sina Weibo, Dou Yin, and YouTube, respectively, have watched her videos. Noticeably, the number of times each of Li's 103 videos on YouTube have been viewed exceeds 5 million. In 2016, Li registered "Li Ziqi", "Qi", and "Gourmet & Life Stylist" as trademarks, and after two years of shooting videos, in 2018 Li Ziqi launched her flagship store on Taobao, where most of the food and condiments that appeared in her videos are available for sale. Li Ziqi's Taobao store generated a GMV of RMB80 million during the past Double Eleven festival, hitting a record high. The success of Li Ziqi has mainly been attributable to high quality content and strong personalized identity. We estimate that personal IP brands are being valued as one of the most efficient marketing channels for today's consumer sectors, which can smoothly turn viewers' traffic into sales. In this respect, in China's consumer sector, a larger number of personal IP brands will rise, while existing brands are actively seeking for cooperation with IP creators. In particular, we expect that for food and beverage sectors, personal IP creators will place more emphasis on quality cuisine ingredients, food processing techniques, healthy lifestyle brand positioning, and cultural and spiritual value. The most important thing is that the personal IP brands make a strong emotional link between the consumer and the brand, similar to the relationship between fans and idols, making the purchase of the product itself a way to strengthen their connection with their idols.

**Figure-154: Li Ziqi's Video**



Source: Li Ziqi, Guotai Junan International.

**Figure-155: Li Ziqi's Product**



Source: Li Ziqi, Guotai Junan International.



## The Opportunities and Challenges Brought by the Rise of New Consumer Brands

**New consumer brands have sprung up with the help of capital resources.** Since 2015, a large number of high-quality domestic brands emerged, such as Hi Tea, Nayuki's Tea, Luckin Coffee, Yuanqi Senlin, Chicecream, Saturn Bird Coffee, Li Ziqi, Le Chun, Simple Love Yoghurt, RYYTN, Mo Xiaoxian, and Ramen Tale, etc., competing with existing brands to some extent. The rise of these new consumer brands was mainly because they cater to the trend of consumption upgrade and the ever-changing tastes of the young people. New media and new distribution channels put new and old brands on the same starting line. Thanks to rapid growth of Chinese economy over the past 40 years, people have become more confident in Chinese traditional culture and they are more willing to choose domestic brands than ever before. In the process of economic transformation, China has witnessed an increasing amount of capital invested in the consumer sector. Brand owners have to pay attention to innovation and optimization of their products. Unlike gaming and social networking services, consumer products are feature with longer product cycles and slower business expansion. But more and more investors become interested in the consumer business because of its stable profitability and cash flow. For new consumer brand owners, China's well-developed manufacturing capacity and supply chain greatly support the supply side of high-quality products. Most importantly, unlike Taobao store owners, founders of new consumer brands have become able to successfully operate their brands based on their in-depth understanding of the internet mindset and younger generations' consumption habits.

**Figure-156: Yuanqi Senlin (元气森林) and Saturn Bird Coffee(三顿半)**



**Figure-157: Simple Love (简爱) and Chicecream (钟薛高)**



Source: Euromonitor, Guotai Junan International.

Source: Euromonitor, Guotai Junan International.

**Upgraded products can create new unique selling points.** The development of each new brand is to deal with the strong pain point of a certain group of customers. Although that user base is relatively small, the potential market size may be quite large because most customers are willing to pay to deal with their pain points. Many new brands have to earn market share in niche markets, instead of red sea markets. For example, Yuanqi Senlin has created a fashion of 'Zero-Sugar Health' product by promoting its sugar-free sparkling water to solidify its 'fashionable health' positioning and seize new market opportunities. With the help of convenience stores and e-commerce channels, Yuanqi Senlin's products can rapidly reach its consumers. Yuanqi Senlin has had a wide spectrum of beverage products, including tea, yoghurt, and energy drinks. According to Foodplus' data, in 2019, the retail sales of Yuanqi Senlin amounted to RMB1.5-2.0 billion, and Yuanqi Senlin's revenue is expected to reach RMB600-700 million. By 2H2019, Yuanqi Senlin was valued at nearly RMB4 billion. In addition, on the 2019 Double Eleven festival, the new coffee brand, Saturn Bird won the top spot in the coffee sector. Saturn Bird uses cold extraction technology to extract coffee powder, which can better retain the taste and flavor of coffee beans. Such a formula can be dissolved in cold water within only 3 seconds and is believed to be healthier as it does not contain any sucrose, fat, and artificial flavors. Saturn Bird Coffee focuses on the post-1990s generation since they are often under heavy work pressure and more addicted to coffee drinks of higher quality, better taste and nicer packaging. And cheap Nestlé Instant Coffee no longer meets their needs, unless restricted by budget, they cannot consume expensive freshly brewed coffee every day. Therefore upgraded instant coffee can be a good choice for refreshment needs. In recent years, Simple Love Yoghurt has become popular among post 1985 young mothers and ladies, who

have stronger purchasing power and are eager to select high-quality family-use products. Simple Love has dealt with their pain point of getting rid of food additives by launching pure yogurt products.

**The emergence of new media platforms brought about traffic dividend.** The rapidly developing new media platforms such as RED, live streaming e-commerce, Douyin, and Kuaishou, have created huge pools of traffic and become important marketing channels for new consumer brands. New consumer brands promote their products and services via new media platforms, instead of the traditional ones where leading brands dominate. In the past, media strived to cover a wider range of customers at lower cost. However, nowadays different new media mainly focus on specific groups of clients. New media channels can precisely push advertisements and promote advertisers' products to targeted customer groups. Different channels attract users with different identities and backgrounds. For example, most users of Douyin and RED communities are young people living in China's higher-tier cities. Yuanqi Senlin impressed potential consumers by inviting popular stars and internet celebrities to advertise its products. Perfect Diary invested heavily in both intermediate-level KOLs and WeChat private traffic so as to fully utilize its brand popularity and reputation. RYYTN has fully utilized online resources to avoid direct offline competition against giants such as Mengniu and Yili. In short, new media can quickly and unobtrusively make consumers familiar with new brands. People are willing to disseminate and share the above-mentioned brand products because of their creative and attracting packaging designs, further reducing the overall marketing expenses. Besides, new consumer brands are more flexible in R&D and strategic marketing. Chicecream's Duanpian Liquor ice cream and Ecuador Pink-Diamond ice cream are good examples.

**The rise of new channels has made new consumer brands much closer to consumers.** In the past, China's leading FMCG companies relied heavily on a well-established distributor systems to carry out large-scale production and distribution, and reach consumers at lower cost. They carried out in-depth distribution and firmly controlled thousands of primary distributors, hundreds of thousands of secondary distributors and millions of retail outlets. Hypermarkets and supermarkets mainly attract elder customers and have high barrier for brands. Therefore, new consumer brands cannot be rapidly distributed in these conventional channels. By contrast, e-commerce platforms enable new consumer brands to achieve nationwide coverage without establishing offline distribution channels. Young people are not only the targeted consumers of new consumer brands, but also of e-commerce, convenience stores and other new distribution channels. Hence, new channels are very suitable to distribute products of new consumer brands. In addition, new consumer brands mainly drive sales by introducing trendy products and building brands. The proportion of their active sales is relatively large, which is also conducive to sales on e-commerce platforms. The proportion of e-commerce channels for distribution of new consumer brands is much higher than that of traditional brands. New media platforms such as RED, WeChat, live streaming e-commerce, Douyin and Kuaishou, can help new consumer brands monetize their online traffic and achieve integration of advertisements and sales.

**The rise of Guochao (literally the "national hip") has driven growth of domestic brands.** Before this word appeared, the expression of "national style" or "retro" was more common, and the appearance of Guochao narrowed the gap between the latest fashion and traditional culture of China. Guochao is not only an element of traditional Chinese culture, but also a mix of traditional culture and current trends to make products more fashionable. For example, the Palace Museum attracts the younger generation by recreating a self-image and making creative products. Li Ning printed the logo "China Li Ning" on the clothing chest as a tag during the New York Fashion Week, reflecting their confidence of the Chinese culture. The rapid development of China's economy and great improvement of people's living standards have awakened patriotism and generated a sense of self-pride. The return of traditional culture and the growing awareness of cultural self-confidence combined resulted in the rise of Guochao. China's post 1990s and post 2000s, born and raised up in a prosperous and peaceful era, are much prouder of the country's great leap and unprecedented prosperity. Compared to their previous generations, they typically have more interest and confidence in domestic products. Growing up with the internet, the youngsters wear Guochao as a badge of pride as well as a fashionable icon. The Han Chinese clothing was once controversial but has gradually become a new pursuit of youngsters. More and more domestic brands have seized the great opportunity of the rise in Guochao by launching new products containing Chinese-featured elements. Benefiting from this rise, new brands also emerged, including Li Ziqi and Chicecream. According to data jointly published by Baidu and People.cn Research Institute, from 2009 to 2019, the popularity index of Chinese domestic brands surged from 38% to 70%. During the past year, the cumulative search volume of key words related to domestic product brands exceeded 12.6 billion (times) on Alibaba platforms.

**New consumer brands not only cater to consumption upgrade but also inspire leading brands to catch up.** Many new consumer brands essentially cater to growing demand for premium products of young consumers with stronger purchasing power and unique taste. Most new brands are positioned to provide higher quality, but more expensive products. In our view, thanks to the ongoing consumption upgrade, the proportion of higher quality consumer goods will continue to rise. Leading FMCG companies used to respond slowly to new demand of young consumers, leaving some markets to new consumer brands. Moreover, as new consumer brand products are usually positioned as premium products, the price war which is often used by leading companies does not work. Nevertheless, the rise in new consumer brands encourages China's leading FMCG companies to improve their products and optimize business operations. Inspired by new brands, leading FMCG companies are expected to develop popular products for young people. Some leading FMCG companies might lose their market share in the long term, if they fail to catch up with consumption upgrading trends. We believe that leading companies will maintain their existing advantages, especially in distribution channels and brand building, which will provide more time for them to transform. We are more optimistic about companies that have organizational structure advantages and can take the initiative to lead consumption upgrades.

21 February 2020

Consumer Sector-Food &amp; Beverage 消费行业-食品饮料

Sector Report



## Valuation

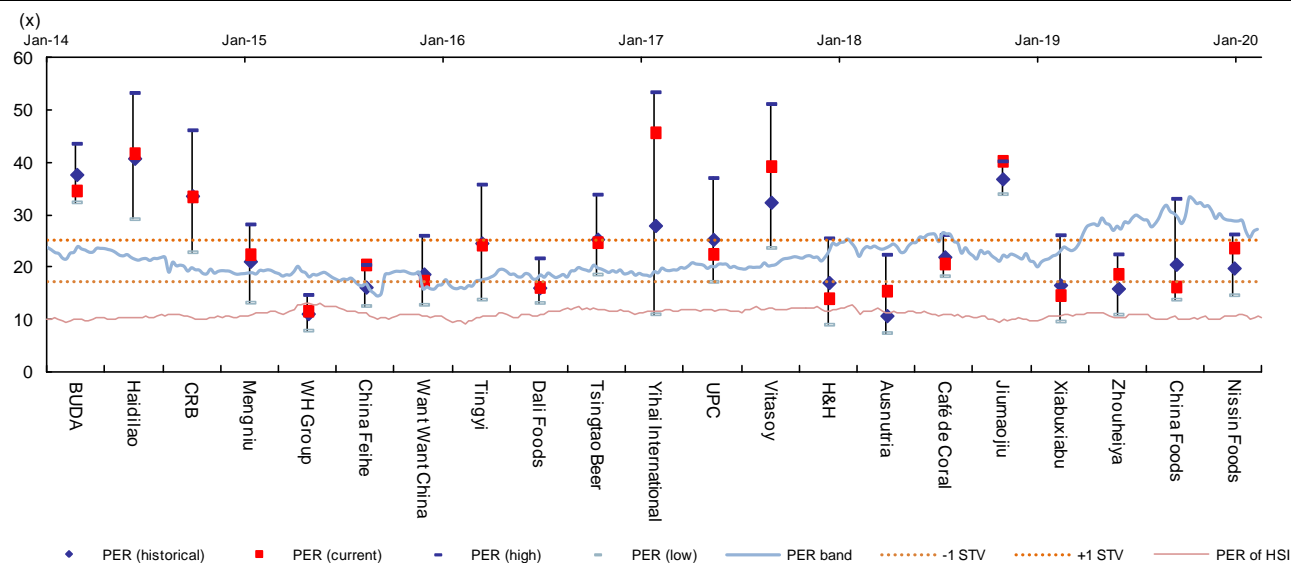
**Valuation of the broadly defined food & beverage sector of the Hong Kong market is trending up.** We have calculated the weighted average forward PER of the broadly defined food & beverage sector, which includes major food & beverage manufacturers (food & beverage, dairy products, beer, etc) and catering companies. We have witnessed that more and more dominating and rapidly-growing consumer companies have been listed in the Hong Kong market over recent years, such as Yihai, Haidilao, BUDA, China Feihe, Jiumaojiu, etc. In addition, leading consumer companies which have stable profitability, strong cash flow, healthy financial condition and promising growth potential have increasingly been welcomed by the market during economic downturns. Therefore, the valuation of the F&B sector is trending up and running north of +1 standard deviation over recent months. Generally, leading consumer companies have enjoyed valuation premium in the Hong Kong market. As at 21 February, 2020, the weighted average forward PER of the F&B sector traded at 35.9x 2019F PER, 28.5x 2020F PER and 23.6x 2021F PER, significantly higher than the forward PER of HSI. As the valuation of F&B companies with differed growth rate spreads over a wide range, sometimes, it is reasonable to value companies by PEG. It is worth noting that Hong Kong listed major food & beverage companies have no major difference with mainland China-listed companies, but small-scaled Hong Kong listed food & beverage trade at notable discounts compared to leading HK-listed companies and same-scale mainland China-listed companies due to low liquidity and low visibility.

**Table-4: Peers Table of Broadly Defined Food & Beverage Companies (Leading F&B Manufacturers & Catering Companies)**

Company				Market Cap	PER(x)				PBR(x)				Gross	Net	ROE	DY(%)
	Stock Code	Currency	Last price		18A	19F	20F	21F	18A	19F	20F	21F	Margin(%)	Margin(%)	(%)	
													19F	19F	19F	19F
Hong Kong Listed Food & Beverage Companies (including catering companies)																
Budweiser Brewing Apac	1876 HK	HKD	24.6	325,788	43.4	43.8	35.8	29.8	n.a.	3.9	3.6	3.3	53.1	14.2	9.1	1.4
Haidilao International	6862 HK	HKD	33.15	175,695	90.0	62.8	43.2	33.2	17.9	14.3	11.3	8.7	58.9	9.0	24.7	0.3
China Resources Beer	291 HK	HKD	37.95	123,117	106.3	50.6	34.5	27.4	5.7	5.5	5.1	4.6	37.0	6.2	10.4	0.6
China Mengniu Dairy	2319 HK	HKD	29.55	116,299	32.2	21.9	22.9	19.2	4.0	3.6	3.2	2.8	37.7	5.6	17.7	1.0
Wh Group	288 HK	HKD	8.53	125,626	17.0	13.3	11.6	11.0	2.1	1.9	1.7	1.6	19.8	5.1	15.0	3.3
China Feihe Ltd	6186 HK	HKD	12.1	108,093	40.7	27.3	21.0	17.0	n.a.	7.5	5.9	4.7	69.0	25.8	33.6	2.4
Want Want China	151 HK	HKD	6.25	77,595	19.1	18.2	17.1	16.2	4.3	4.3	4.0	3.9	48.1	18.3	23.9	4.1
Dali Foods Group	3799 HK	HKD	5.65	77,372	17.6	17.7	16.2	15.2	4.4	4.2	3.9	3.7	40.2	18.2	24.5	4.4
Tingyi	322 HK	HKD	14.6	82,107	28.1	27.6	24.5	22.4	3.7	3.6	3.4	3.3	31.5	4.4	13.5	3.1
Tsingtao Brewery	168 HK	HKD	43.85	64,332	38.1	29.1	25.2	21.6	2.9	2.8	2.6	2.5	38.6	6.6	9.4	1.5
Yihai International	1579 HK	HKD	51.2	53,601	87.3	64.2	47.4	36.5	23.5	17.9	13.6	10.4	39.1	17.9	30.1	0.4
Uni-President China	220 HK	HKD	8.7	37,578	30.8	24.9	22.7	20.9	2.5	2.5	2.5	2.5	36.0	6.2	10.4	4.0
Vitasoy Intl	345 HK	HKD	29.95	31,860	45.7	44.6	38.7	34.0	10.0	9.2	8.5	7.8	54.2	9.0	21.7	1.4
Health And Happiness	1112 HK	HKD	35.35	22,751	22.8	17.1	14.1	12.6	4.3	3.6	3.0	2.7	66.5	11.1	23.0	1.5
Ausnutria Dairy	1717 HK	HKD	12.9	20,816	27.6	21.0	15.9	12.5	5.5	4.8	4.0	3.3	52.6	13.1	22.3	1.5
Cafe De Coral	341 HK	HKD	17.56	10,285	22.5	17.4	24.2	18.1	2.9	3.0	3.0	3.1	13.4	6.9	16.9	4.2
Jiumaojiu	9922 HK	HKD	9.6	13,281	160.8	61.5	44.2	25.2	n.a.	4.5	4.2	3.7	63.8	6.9	30.4	0.5
Xiabuxiabu	520 HK	HKD	8.21	8,880	16.2	19.3	15.0	12.1	3.4	3.2	2.9	2.6	62.7	7.0	17.9	2.2
Zhou Hei Ya	1458 HK	HKD	4.59	10,939	17.1	22.6	18.5	18.7	2.3	2.3	2.0	1.9	55.6	13.4	10.5	2.0
China Foods	506 HK	HKD	3	8,392	22.1	18.9	16.3	14.2	1.7	1.7	1.6	1.5	35.9	2.3	9.1	1.8
Nissin Foods	1475 HK	HKD	7.08	7,606	37.0	28.1	24.1	21.3	2.2	2.1	2.0	1.9	33.1	8.6	7.4	1.6
Yashili International	1230 HK	HKD	0.62	2,942	47.5	23.0	27.0	20.0	0.5	0.5	0.5	0.5	42.1	3.5	2.2	0.0
Midpoint					31.5	23.9	23.5	19.6	3.7	3.6	3.3	3.2	41.1	7.8	17.3	1.6
Simple Average					44.1	30.7	25.5	20.9	5.5	4.9	4.2	3.7	45.0	10.0	17.4	2.0
Weighted Average					48.2	35.9	28.5	23.6	7.3	5.8	5.0	4.2	45.9	11.4	17.5	1.9

Source: Bloomberg, Guotai Junan International.

**Figure-158: Forward PER of Broadly Defined Food & Beverage Sector (Including F&B Manufacturers & Catering Companies)**



Source: Bloomberg, Guotai Junan International.

**Valuation of sub-sectors in the F&B industry showed slightly different numbers.** Based on the operations scope, we have divided major food & beverage companies into four groups, narrowly conceived food & beverage sub-sector, dairy products sub-sector, beer sub-sector and catering sub-sector. Based on our calculation, the valuation of the catering sector ranked first (43.6x/34.1x/28.2x 19F/20F/21F PER, see Table-8), successively followed by beer (43.6x/34.1x/28.2x 19F/20F/21F PER, see Table-7), narrowly conceived F&B (28.3x/24.3x/21.5x 19F/20F/21F PER, see Table-5) and dairy products (23.6x/20.9x/17.3x 19F/20F/21F PER, see Table-6). The lead of the catering sector was primarily due to the extremely high valuation of Haidilao and Jiumaojiu, as they have promising growth potential due to high visibility in opening new restaurants. If excluding Haidilao and Jiumaojiu, the valuation of the catering sector (18.4x/17.1x/14.1x 19F/20F/21F PER) would fall behind the dairy products sector as most Hong Kong focused catering companies have limited growth potential. The beer sector trades at a premium as beer companies have high certainty in earnings growth (as discussed above). Comparing each sub-sector in the Hong Kong market with those in the mainland China market and global market, we found no major differences in valuation, but mainland China may trade at a little bit of a premium due to its stronger liquidity. In the terms of individual stocks, we believe that China Foods has the most attractive valuation, and Mengniu has the safest valuation compared to other leading F&B companies and promising earnings growth.

**Table-5: Peers Table of Narrowly Conceived Food & Beverage Companies**

Company	Stock Code	Currency	Last price	Market Cap HKD mn	PER(x)				PBR(x)				Gross Margin(%)	Net Margin(%)	ROE (%)	DY(%)
					18A	19F	20F	21F	18A	19F	20F	21F	19F	19F	19F	19F
Hong Kong Listed Food & Beverage Companies																
Want Want China Holdings	151 HK	HKD	6.25	77,595	19.1	18.2	17.1	16.2	4.3	4.3	4.0	3.9	48.1	18.3	23.9	4.1
Dali Foods Group	3799 HK	HKD	5.65	77,372	17.6	17.7	16.2	15.2	4.4	4.2	3.9	3.7	40.2	18.2	24.5	4.4
Tingyi (Cayman Isl'n)	322 HK	HKD	14.6	82,107	28.1	27.6	24.5	22.4	3.7	3.6	3.4	3.3	31.5	4.4	13.5	3.1
Yihai International	1579 HK	HKD	51.2	53,601	87.3	64.2	47.4	36.5	23.5	17.9	13.6	10.4	39.1	17.9	30.1	0.4
Uni-President China	220 HK	HKD	8.7	37,578	30.8	24.9	22.7	20.9	2.5	2.5	2.5	2.5	36.0	6.2	10.4	4.0
Vitasoy Intl Holdings	345 HK	HKD	29.95	31,860	45.7	44.6	38.7	34.0	10.0	9.2	8.5	7.8	54.2	9.0	21.7	1.4
Zhou Hei Ya International	1458 HK	HKD	4.59	10,939	17.1	22.6	18.5	18.7	2.3	2.3	2.0	1.9	55.6	13.4	10.5	2.0
China Foods	506 HK	HKD	3	8,392	22.1	18.9	16.3	14.2	1.7	1.7	1.6	1.5	35.9	2.3	9.1	1.8
Nissin Foods	1475 HK	HKD	7.08	7,606	37.0	28.1	24.1	21.3	2.2	2.1	2.0	1.9	33.1	8.6	7.4	1.6
Simple Average					32.7	28.5	24.2	21.4	5.8	5.1	4.4	3.9	41.5	10.9	16.8	2.6
Weighted Average					32.3	28.3	24.3	21.5	6.6	5.8	5.0	4.5	40.8	12.7	20.2	3.1
Mainland China Listed F&B Companies																
Foshan Haitian Flavouring -A	603288 CH	CNY	104.87	313,488	60.6	53.8	44.9	37.8	20.4	16.8	13.9	12.0	46.1	26.6	32.6	1.1
Henan Shuanghui	000895 CH	CNY	35.09	128,936	22.1	21.7	20.0	18.2	8.9	7.3	6.6	5.7	20.0	9.7	35.6	4.2
Hebei Yangyuan Zhihui	603156 CH	CNY	27.84	32,501	10.2	10.4	9.7	8.9	1.8	2.1	1.9	1.8	52.1	35.9	23.1	9.2
Toly Bread Co Ltd-A	603866 CH	CNY	40.89	29,824	39.2	37.1	30.9	26.3	5.6	6.8	6.2	5.5	39.8	12.6	18.6	1.2
Angel Yeast Co Ltd-A	600298 CH	CNY	28.61	26,100	25.7	25.3	21.5	18.6	5.5	4.7	4.0	3.5	36.2	12.2	18.7	1.3
Juewei Food Co Ltd-A	603517 CH	CNY	40.69	27,415	36.1	29.8	24.2	20.6	5.5	6.4	5.3	4.4	34.8	15.7	22.0	1.3
Chongqing Fuling Zhacai-A	002507 CH	CNY	27.05	23,637	30.1	30.3	26.2	23.6	8.6	7.2	5.9	4.9	58.2	34.0	23.1	0.9
Three Squirrels Inc-A	300783 CH	CNY	68.63	30,465	84.6	72.0	56.8	47.1	22.2	15.9	13.1	10.6	28.3	3.7	20.8	0.4
Sichuan Teway Food	603317 CH	CNY	40.8	18,660	59.0	50.4	39.8	32.6	13.3	9.8	8.1	6.6	39.5	17.9	20.3	0.4
Xiangpiaopiao Food Co Ltd-A	603711 CH	CNY	23.75	10,994	29.5	26.1	20.4	16.2	4.3	4.0	3.5	3.0	39.9	9.2	15.4	1.2
Chacha Food Co Ltd-A	002557 CH	CNY	40.9	22,955	44.7	38.5	32.6	27.8	6.2	5.6	5.0	4.5	32.5	11.4	14.9	1.2
Fu Jian Anjoy Foods Co	603345 CH	CNY	61.17	16,006	49.9	43.5	35.9	27.8	6.5	6.1	5.4	4.7	25.8	6.4	14.0	0.7
Simple Average					41.0	36.6	30.2	25.5	9.1	7.7	6.6	5.6	37.8	16.3	21.6	1.9
Weighted Average					46.3	41.6	34.9	29.6	13.9	11.6	9.7	8.4	38.7	20.0	28.6	2.0
Global Listed F&B Companies																
Companies																
Nestle Sa-Reg	NESN SW	CHF	109.76	2,592,229	31.9	25.5	23.7	22.0	5.7	6.1	6.4	6.1	49.8	13.6	23.1	2.6
Coca-Cola Co/The	KO US	USD	59.72	1,992,586	39.5	28.6	26.5	24.4	15.0	13.5	12.6	11.8	60.8	23.9	49.6	2.9
Pepsico Inc	PEP US	USD	145.16	1,570,788	16.0	27.8	24.6	22.9	14.1	13.7	13.1	12.1	55.1	10.9	49.9	2.8
Mondelez International Inc-A	MDLZ US	USD	59.04	658,830	24.9	22.0	22.2	20.4	3.3	3.1	3.0	2.9	40.0	15.0	14.6	2.0
Danone	BN FP	EUR	71.34	412,362	19.0	18.7	17.0	16.0	2.8	2.7	2.5	2.3	48.9	9.8	14.6	2.9
Reckitt Benckiser Group Plc	RB/ LN	GBp	6442	459,818	20.3	19.4	19.8	18.9	3.1	3.0	2.8	2.6	60.3	18.3	15.3	2.6
Keurig Dr Pepper Inc	KDP US	USD	29.3	320,992	69.9	24.0	20.9	18.7	1.8	1.8	1.7	1.6	57.0	15.5	7.5	2.0
Kraft Heinz Co/The	KHC US	USD	27.42	260,809	n.a.	17.2	12.0	11.6	0.6	0.6	0.6	0.6	32.6	7.7	3.7	5.1
General Mills Inc	GIS US	USD	54.13	254,953	18.5	16.0	15.7	15.5	4.6	4.0	3.6	3.4	35.0	12.0	25.7	3.6
Hershey Co/The	HSY US	USD	160.11	261,528	28.3	29.3	25.9	24.5	24.0	19.2	14.4	12.5	45.4	14.4	73.1	2.1
Monster Beverage Corp	MNST US	USD	70.4	294,779	37.9	34.5	31.0	28.2	10.6	9.1	7.8	6.6	59.9	26.6	28.6	0.0
Associated British Foods Plc	ABF LN	GBp	2617	208,454	19.6	23.6	17.8	16.4	2.2	2.2	2.0	1.9	23.0	5.5	9.4	2.0
Hormel Foods Corp	HRL US	USD	45.53	189,599	23.9	24.9	25.8	24.6	4.3	4.1	3.9	3.7	19.8	10.3	17.0	2.1
Coca-Cola European Partners	CCEP US	USD	55.91	203,188	24.1	21.3	18.6	17.1	3.5	3.8	4.0	3.9	38.2	9.1	17.1	2.7
Mccormick & Co-Non	MKC US	USD	163.83	169,500	23.2	30.9	31.2	29.0	6.8	6.3	5.8	5.3	40.1	13.1	21.2	1.3
Kellogg Co	K US	USD	65.67	174,437	16.7	23.4	17.1	16.4	8.7	8.2	6.5	5.8	32.3	7.1	35.9	3.3
Chocoladefabriken	LISN SW	CHF	93000	173,584	44.7	43.5	40.4	37.2	5.1	5.6	5.2	4.9	63.0	11.4	11.7	1.0
Simple Average					28.7	25.3	23.0	21.4	6.8	6.3	5.6	5.2	44.8	13.2	24.6	2.4
Weighted Average					29.6	25.8	23.6	22.0	8.7	8.2	7.8	7.3	50.6	15.1	31.2	2.6

Source: Bloomberg, Guotai Junan International.

**Table-6: Peers Table of Dairy Companies**

Company	Stock Code	Currency	Last price	Market	PER(x)				PBR(x)				Gross	Net	ROE	DY(%)
				Cap	18A	19F	20F	21F	18A	19F	20F	21F	Margin (%)	Margin (%)	(%)	
				HKD mn									19F	19F	19F	19F
<b>Hong Kong Listed Dairy Companies</b>																
China Mengniu Dairy	2319 HK	HKD	29.55	116,299	32.2	21.9	22.9	19.2	4.0	3.6	3.2	2.8	37.7	5.6	17.7	1.0
China Feihe	6186 HK	HKD	12.1	108,093	40.7	27.3	21.0	17.0	n.a.	7.5	5.9	4.7	69.0	25.8	33.6	2.4
Health And Happiness	1112 HK	HKD	35.35	22,751	22.8	17.1	14.1	12.6	4.3	3.6	3.0	2.7	66.5	11.1	23.0	1.5
Ausuntria Dairy	1717 HK	HKD	12.9	20,816	27.6	21.0	15.9	12.5	5.5	4.8	4.0	3.3	52.6	13.1	22.3	1.5
Yashili International	1230 HK	HKD	0.62	2,942	47.5	23.0	27.0	20.0	0.5	0.5	0.5	0.5	42.1	3.5	2.2	0.0
<b>Simple Average</b>					<b>34.1</b>	<b>22.0</b>	<b>20.2</b>	<b>16.3</b>	<b>3.6</b>	<b>4.0</b>	<b>3.3</b>	<b>2.8</b>	<b>53.6</b>	<b>11.8</b>	<b>19.8</b>	<b>1.3</b>
<b>Weighted Average</b>					<b>34.6</b>	<b>23.6</b>	<b>20.9</b>	<b>17.3</b>	<b>4.2</b>	<b>5.2</b>	<b>4.3</b>	<b>3.6</b>	<b>53.8</b>	<b>14.7</b>	<b>24.7</b>	<b>1.6</b>
<b>Mainland China Listed Beer Companies</b>																
Inner Mongolia Yili	600887 CH	CNY	30.71	207,252	27.1	26.4	24.4	20.9	6.7	6.2	5.6	5.0	38.0	7.9	23.5	2.5
Bright Dairy & Food	600597 CH	CNY	11.72	15,887	39.2	30.0	26.8	24.0	2.7	2.5	2.4	2.2	32.9	2.2	8.6	1.2
New Hope Dairy	002946 CH	CNY	11.48	10,849	37.7	38.7	30.8	25.5	6.0	4.7	4.1	3.6	33.7	4.4	12.1	n.a.
Beijing Sanyuan	600429 CH	CNY	5.08	8,422	39.4	n.a.	n.a.	n.a.	1.5	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.	n.a.
Beingmate	002570 CH	CNY	6.47	7,324	150.2	n.a.	43.1	23.1	3.6	n.a.	43.1	23.1	52.0	0.2	n.a.	n.a.
Xinjiang Tianrun	600419 CH	CNY	11.96	3,556	26.3	21.5	18.2	16.1	2.7	2.8	2.5	2.3	27.4	7.9	12.8	1.5
<b>Simple Average</b>					<b>53.3</b>	<b>29.1</b>	<b>28.7</b>	<b>21.9</b>	<b>3.9</b>	<b>4.1</b>	<b>11.6</b>	<b>7.2</b>	<b>36.8</b>	<b>4.5</b>	<b>14.3</b>	<b>1.7</b>
<b>Weighted Average</b>					<b>32.3</b>	<b>27.1</b>	<b>25.3</b>	<b>21.3</b>	<b>6.1</b>	<b>5.8</b>	<b>6.4</b>	<b>5.3</b>	<b>37.7</b>	<b>7.1</b>	<b>21.8</b>	<b>2.4</b>
<b>Global Listed Dairy Companies</b>																
Nestle Sa-Reg	NESN SW	CHF	109.76	2,592,229	31.9	25.5	23.7	22.0	5.7	6.1	6.4	6.1	49.8	13.6	23.1	2.6
Danone	BN FP	EUR	71.34	412,362	19.0	18.7	17.0	16.0	2.8	2.7	2.5	2.3	48.9	9.8	14.6	2.9
Saputo Inc	SAP CN	CAD	41.27	98,940	21.3	23.3	20.9	n.a.	3.0	2.7	2.5	n.a.	30.0	4.7	11.9	1.6
Meiji Holdings Co Ltd	2269 JP	JPY	7040	74,933	16.5	15.4	14.8	14.3	1.9	1.8	1.7	1.6	37.1	5.2	12.2	2.0
<b>Simple Average</b>					<b>22.2</b>	<b>20.7</b>	<b>19.1</b>	<b>17.5</b>	<b>3.4</b>	<b>3.3</b>	<b>3.3</b>	<b>3.3</b>	<b>41.5</b>	<b>8.3</b>	<b>15.4</b>	<b>2.3</b>
<b>Weighted Average</b>					<b>29.5</b>	<b>24.3</b>	<b>22.5</b>	<b>21.0</b>	<b>5.1</b>	<b>5.4</b>	<b>5.6</b>	<b>5.5</b>	<b>48.7</b>	<b>12.6</b>	<b>21.3</b>	<b>2.6</b>

Source: Bloomberg, Guotai Junan International.

21 February 2020

Consumer Sector-Food &amp; Beverage 消费行业-食品饮料

Sector Report

**Table-7: Peers Table of Beer Companies**

Table 1: Performance Data of Beer Companies																	
Company		Stock Code	Currency	Last price	Market Cap	PER(x)				EV/EBITDA				Gross	Net Margin	ROE(%)	DY(%)
						18A	19F	20F	21F	18A	19F	20F	21F	Margin (%)	(%)	19F	19F
Hong Kong Listed Beer Companies																	
Budweiser Brewing	1876 HK	HKD	24.60	325,788	43.4	43.8	35.8	29.8	n.a.	19.3	17.7	15.6	53.1	14.2	9.1	1.4	
Apac																	
China Resources Beer	291 HK	HKD	37.95	123,117	106.3	50.6	34.5	27.4	24.6	22.7	17.7	14.9	37.0	6.2	10.4	0.6	
Tsingtao Brewery	168 HK	HKD	43.85	64,332	38.1	29.1	25.2	21.6	10.0	12.8	11.6	10.2	38.6	6.6	9.4	1.5	
Simple Average					62.6	41.1	31.8	26.3	17.3	18.3	15.7	13.6	42.9	9.0	9.6	1.2	
Weighted Average					57.8	43.6	34.1	28.2	19.6	19.3	17.0	14.8	47.5	11.3	9.4	1.2	
Mainland China Listed Beer Companies																	
Companies																	
Tsingtao Brewery	600600 CH	CNY	46.22	64,331	38.1	34.6	29.4	25.2	10.0	13.0	11.7	10.2	38.4	6.4	9.5	1.2	
Chongqing Brewery	600132 CH	CNY	48.39	25,925	54.1	40.5	41.2	35.3	23.6	29.1	26.9	23.4	39.9	16.2	45.3	1.9	
Beijing Yanjing Brewery	000729 CH	CNY	6.38	19,906	93.3	82.9	70.1	58.0	12.5	13.3	12.8	10.9	37.0	1.9	1.7	0.3	
Zhujiang Brewery	002461 CH	CNY	7.01	17,176	39.5	31.0	28.5	24.0	10.5	15.5	13.8	12.4	44.1	12.2	6.0	1.6	
Simple Average					56.3	47.2	42.3	35.6	14.1	17.7	16.3	14.2	39.8	9.2	15.6	1.3	
Weighted Average					50.2	42.9	38.0	32.2	13.2	16.7	15.2	13.3	39.2	8.5	15.1	1.3	
Global Listed Beer Companies																	
Anheuser-Busch Inbev	ABI BB	EUR	66.96	1,138,896	33.3	16.4	16.3	14.7	11.2	11.9	11.3	10.8	61.8	16.6	13.6	2.7	
Ambev Sa	ABEV3 BZ	BRL	16.17	450,864	19.0	21.2	19.9	17.7	11.2	11.3	10.6	9.8	59.2	22.7	20.3	3.7	
Heineken Nv	HEIA NA	EUR	103.9	504,179	28.6	27.5	22.1	20.4	11.9	12.7	12.6	12.0	47.6	9.0	14.2	1.8	
Constellation Brands	STZ US	USD	208.34	310,672	11.6	23.9	22.6	19.4	16.1	18.0	17.1	16.0	51.5	20.6	13.7	1.4	
Asahi Group Holdings	2502 JP	JPY	4800	161,816	15.1	15.5	13.5	12.4	9.2	9.9	8.9	8.4	37.9	6.8	11.9	2.0	
Carlsberg As-B	CARLB DC	DKK	1017	175,142	26.6	23.3	22.1	20.0	9.6	11.4	11.4	10.8	49.5	10.0	14.8	2.1	
Kirin Holdings	2503 JP	JPY	2235	142,406	12.2	32.9	13.9	12.7	9.8	11.5	10.2	9.3	43.7	3.1	6.5	2.7	
Molson Coors Beverage	TAP US	USD	55.41	94,128	10.8	49.5	14.2	13.6	8.8	12.2	9.5	9.5	39.7	2.3	1.8	3.6	
Simple Average					19.6	26.3	18.1	16.4	11.0	12.4	11.5	10.8	48.9	11.4	12.1	2.5	
Weighted Average					24.9	22.0	18.5	16.7	11.5	12.4	11.8	11.2	54.3	14.6	14.0	2.5	

Source: Bloomberg, Guotai Junan International.

**Table-8: Peers Table of Catering Companies**

Table of P/E Ratio Table of Catering Companies																	
Company	Stock Code	Currency	Last price	Market Cap	PER(x)					PBR(x)				Gross	Net	ROE	DY(%)
					HKD mn	18A	19F	20F	21F	18A	19F	20F	21F	Margin (%)	Margin (%)	(%)	)
Hong Kong Listed Catering Companies																	
Haidilao International	6862 HK	HKD	33.15	175,695	90.0	62.8	43.2	33.2	17.9	14.3	11.3	8.7	58.9	9.0	24.7	0.3	
Cafe De Coral Holdings	341 HK	HKD	17.56	10,285	22.5	17.4	24.2	18.1	2.9	3.0	3.0	3.1	13.4	6.9	16.9	4.2	
Xiabuxiabu	520 HK	HKD	8.21	8,880	16.2	19.3	15.0	12.1	3.4	3.2	2.9	2.6	62.7	7.0	17.9	2.2	
Jiumaojiu International Hold	9922 HK	HKD	9.6	13,281	160.8	61.5	44.2	25.2	n.a.	4.5	4.2	3.7	63.8	6.9	30.4	0.5	
Fairwood Holdings Ltd	52 HK	HKD	19.42	2,516	11.6	13.9	11.4	14.5	3.3	3.2	3.3	3.1	12.9	6.1	23.4	4.3	
Ajisen China Holdings Ltd	538 HK	HKD	2.04	2,227	3.4	10.0	10.3	7.2	0.6	n.a.	n.a.	n.a.	n.a.	8.0	5.9	5.2	
Tang Palace China Holdings	1181 HK	HKD	1.05	1,130	8.3	6.8	6.3	n.a.	2.0	n.a.	n.a.	n.a.	n.a.	n.a.	24.6	n.a.	
Tai Hing Group Holdings Ltd	6811 HK	HKD	1.31	1,310	4.3	10.9	8.7	7.1	n.a.	1.2	2.2	2.1	71.0	3.6	15.6	4.4	
Tsui Wah Holdings Ltd	1314 HK	HKD	0.4	564	7.0	117.6	n.a.	n.a.	0.5	0.5	n.a.	n.a.	72.2	0.3	0.4	2.5	
Simple Average						36.0	35.6	20.4	16.8	4.4	4.3	4.5	3.9	50.7	6.0	17.7	2.9
Weighted Average						85.1	57.2	40.1	30.4	16.0	12.5	9.9	7.7	56.8	8.6	24.0	0.7
Mainland China Listed Catering Companies																	
Guangzhou Restaurant Group	603043 CH	CNY	28.75	12,858	28.2	26.7	22.0	18.3	6.0	5.2	4.4	3.7	54.2	14.6	19.5	1.4	
China Qianjude Group	002186 CH	CNY	9.65	3,295	38.0	35.7	33.3	31.1	2.0	n.a.	n.a.	n.a.	n.a.	n.a.	5.5	n.a.	
Simple Average						33.1	31.2	27.6	24.7	4.0	n.a.	n.a.	n.a.	n.a.	n.a.	5.5	n.a.
Weighted Average						30.2	28.5	24.3	20.9	5.1	5.2	4.4	3.7	54.2	14.6	16.6	1.4
Global Listed Catering Companies																	
Mcdonald'S Corp	MCD US	USD	215.08	1,261,383	27.2	27.3	25.2	21.4	n.a.	n.a.	n.a.	n.a.	52.7	28.6	n.a.	2.4	
Starbucks Corp	SBUX US	USD	88.6	809,821	22.9	30.0	29.5	23.2	99.2	n.a.	n.a.	n.a.	28.2	13.6	n.a.	1.7	
Yum! Brands Inc	YUM US	USD	103.87	243,331	20.1	24.6	26.5	23.2	n.a.	n.a.	n.a.	n.a.	50.3	23.1	n.a.	1.7	
Restaurant Brands Intern	QSR US	USD	66.31	240,470	50.1	27.6	22.5	20.6	10.4	7.9	9.0	8.2	58.0	11.5	31.4	3.1	
Chipotle Mexican Grill Inc	CMG US	USD	927.59	200,585	145.0	73.5	50.7	40.3	17.8	15.3	12.5	10.1	20.5	6.3	22.4	0.0	
Yum China Holdings Inc	YUMC US	USD	46.05	134,839	24.3	24.4	48.6	23.2	6.1	5.6	5.4	4.6	23.3	8.1	24.0	1.0	
Simple Average						48.3	34.6	33.8	25.3	33.4	9.6	8.9	7.7	38.8	15.2	25.9	1.7
Weighted Average						35.3	30.9	29.2	23.4	62.9	10.0	9.3	8.0	42.5	20.0	26.5	2.0

Source: Bloomberg, Guotai Junan International.

## Conclusion

**Maintain "Outperform" rating for the sector.** In the current economic downturn, we believe that food and beverage consumption will play a more vital role. In 2020, the growth trend of leading food and beverage companies will remain unchanged. We believe that there is huge growth potential of catering consumption which will meet the enjoyment needs of consumers, and there is still much room for improvement in the market concentration within the catering industry. We are optimistic about the future growth of leading catering companies, especially leading hot pot companies. Relatively speaking, the rationality and growth potential of the dairy industry are the best among all food and beverage sub-sectors, and due to the homogeneity of products and the limitations of raw milk procurement, the concentration of the industry should continue to improve. As a leader in the industry, Mengniu initiated the launch of DreamCap products and fresh milk products, leading the industry to continue to upgrade, and Mengniu promoted high scale of sales and enhanced its global operations capabilities through outbound M&As. Competition in the sparkling drinks category is relatively healthy, and industry leaders are leading the industry to upgrade through small packaging and less sugar. Consumers' acceptance of soda beverages has further promoted diversification of sparkling drinks products and has provided new growth opportunities. The top picks in the Consumer Sector - Food & Beverage are Mengniu Dairy (02319 HK, Accumulate, TP of HK\$33.5) and China Foods (00506 HK, Buy, TP of HK\$4.30).



**Company Rating Definition**

The Benchmark: Hong Kong Hang Seng Index

Time Horizon: 6 to 18 months

Rating		Definition
Buy	买入	Relative Performance >15%; or the fundamental outlook of the company or sector is favorable.
Accumulate	收集	Relative Performance is 5% to 15%; or the fundamental outlook of the company or sector is favorable.
Neutral	中性	Relative Performance is -5% to 5%; or the fundamental outlook of the company or sector is neutral.
Reduce	减持	Relative Performance is -5% to -15%; or the fundamental outlook of the company or sector is unfavorable.
Sell	卖出	Relative Performance <-15%; or the fundamental outlook of the company or sector is unfavorable.

**Sector Rating Definition**

The Benchmark: Hong Kong Hang Seng Index

Time Horizon: 6 to 18 months

Rating		Definition
Outperform	跑赢大市	Relative Performance >5%; or the fundamental outlook of the sector is favorable.
Neutral	中性	Relative Performance is -5% to 5%; or the fundamental outlook of the sector is neutral.
Underperform	跑输大市	Relative Performance <-5%; Or the fundamental outlook of the sector is unfavorable.

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