

# China Modern Dairy Holdings Ltd. 中國現代牧業控股有限公司

(Incorporated in the Cayman Islands with limited liability)

Stock Code: 1117



INTERIM REPORT  
2014

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# Corporate Information

## BOARD OF DIRECTORS

### Executive Directors

Ms. GAO Lina (Deputy Chairman and Chief Executive Officer)  
Mr. HAN Chunlin (Chief Operation Officer)  
Mr. SUN Yugang (Chief Financial Officer)

### Non-Executive Directors

Mr. YU Xubo (Chairman)  
Mr. WOLHARDT Julian Juul  
Mr. HUI Chi Kin, Max  
Mr. WU Jing Shui

### Independent Non-Executive Directors

Mr. LI Shengli  
Mr. LEE Kong Wai, Conway  
Mr. KANG Yan  
Mr. ZOU Fei (appointed on 25 August 2014)  
Mr. LIU Fuchun (resignation with effect from 25 August 2014)

## AUDIT COMMITTEE

Mr. LEE Kong Wai, Conway (Chairman)  
Mr. HUI Chi Kin, Max  
Mr. ZOU Fei (appointed on 25 August 2014)  
Mr. LIU Fuchun (resignation with effect from 25 August 2014)

## REMUNERATION COMMITTEE

Mr. LI Shengli (Chairman)  
Mr. WOLHARDT Julian Juul  
Mr. ZOU Fei (appointed on 25 August 2014)  
Mr. LIU Fuchun (resignation with effect from 25 August 2014)

## NOMINATION COMMITTEE

Mr. KANG Yan (Chairman)  
Mr. LI Shengli  
Mr. LEE Kong Wai, Conway

## AUTHORISED REPRESENTATIVES

Ms. GAO Lina  
Mr. WONG Kai Hing

## COMPANY SECRETARY

Mr. WONG Kai Hing

## HEADQUARTERS

Economic and Technological Development Zone  
Maanshan City, Anhui Province,  
PRC

## REGISTERED OFFICE

Maples Corporate Services Limited  
PO Box 309  
Ugland House  
Grand Cayman, KY1-1104, Cayman Islands

## HONG KONG OFFICE

Unit 2402, 24/F,  
Alliance Building 130-136  
Connaught Road Central Sheung Wan  
Hong Kong

## PRINCIPAL SHARE REGISTRAR AND TRANSFER OFFICE

Maples Finance Limited  
PO Box 1093,  
Queensgate House  
Grand Cayman, KY1-1102  
Cayman Islands

## HONG KONG BRANCH SHARE REGISTRAR AND TRANSFER OFFICE

Computershare Hong Kong Investor Services Limited  
Shops 1712-1716, 17/F, Hopewell Centre  
183 Queen's Road East Wanchai  
Hong Kong

## LEGAL ADVISORS

### As to Hong Kong Law

Cleary Gottlieb Steen & Hamilton (Hong Kong)

### As to PRC Law

Commerce & Finance Law Offices

### As to Cayman Islands Law

Maples and Calder

## AUDITOR

Deloitte Touche Tohmatsu  
Certified Public Accountants

## PRINCIPAL BANKERS

Agricultural Development Bank of China Maanshan Branch  
China  
Construction Bank Maanshan Branch  
Bank of Communication Maanshan Branch  
Citibank N.A. Hong Kong

## STOCK CODE

The Stock Exchange of Hong Kong Limited: 1117

## WEBSITE

<http://www.moderndairyir.com>

# Financial Highlights

## RESULTS

	Six months ended 30 June		
	2014 RMB'000	2013 RMB'000	Changes %
Turnover	2,584,535	1,388,033	86.2%
Earnings before finance costs and tax	686,867	263,311	160.9%
Cash EBITDA*	981,897	408,213	140.5%
Cash EBITDA margin	38.0%	29.4%	8.6%
Net profit	545,377	163,737	233.1%

## FINANCIAL POSITION

	As at		
	30 June 2014 RMB'000	31 December 2013 RMB'000	Changes %
Biological assets	6,297,959	5,954,363	5.8%
Cash and cash equivalents	457,837	369,041	24.1%
Total assets	13,179,089	12,493,821	5.5%
Total borrowing (includes short-term debenture)	5,125,277	4,948,666	3.6%
Gearing ratio (Total borrowing/Total assets)	38.9%	39.6%	-0.7%

\* Cash EBITDA represents EBITDA before loss arising from changes in fair values less costs to sell of dairy cows, loss arising from financial liabilities designated at fair value through profit or loss (FVTPL), gain arising from financial assets designated at FVTPL, net loss on disposal of property, plant and equipment and realised changes in fair values of dairy cows recognised in costs of sales.

# Management Discussion and Analysis

## BUSINESS REVIEW

The Group is primarily engaged in two principal business segments: (i) dairy farming business, under which we mainly produce and sell raw milk to customers for processing into dairy products and sell self-breeding dairy cows; and (ii) liquid milk products business, under which we mainly produce and sell liquid milk products. The demand for high-end dairy products has continued to grow at a rapid pace in the PRC due to various factors in the PRC market, including the rising per capita disposable income and the increasing awareness of food safety. This is a key driver for the demand for our quality raw milk products. Since the dairy farming industry in China is largely fragmented and the supply of high-end quality raw milk is very limited, we believe there are significant growth opportunities for the Group to expand its market share in China.

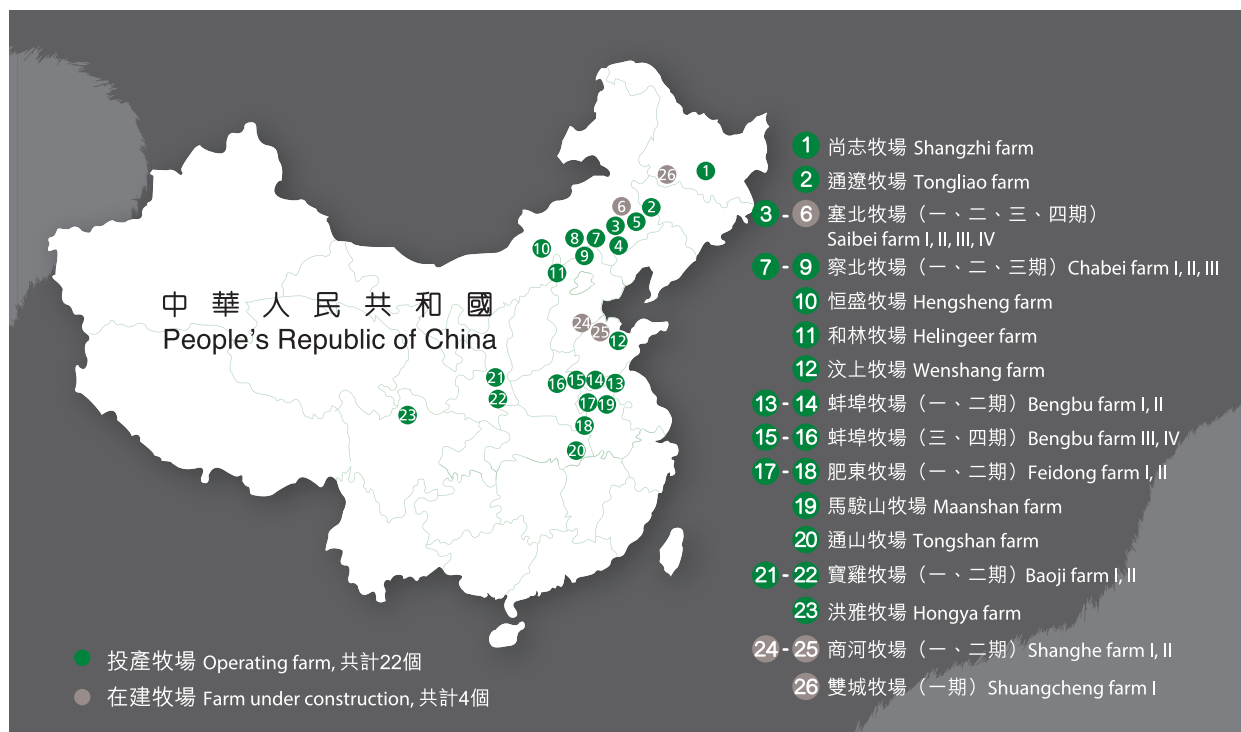
We are the largest dairy farming company in terms of herd size as well as the largest raw milk producer in China. During the six months ended 30 June 2014, the Group's operating results reached a historical high due to increases in productivity and the increased demand for high-end dairy products in the PRC. As of 30 June 2014, the Group had 22 farms operating, 2 farms under construction invested through the joint venture and 2 farms under construction by the Group in the PRC with approximately 190,027 dairy cows in total. Our farms are situated across the PRC in strategic geographical locations that are close to downstream dairy product processing plants and feed supply sources. Sales of milk produced for the Group amounted to 463,991 tons for the six months ended 30 June 2014. This represents an increase of 51.6% from 306,115 tons in the corresponding period of 2013 and indicates that the Group has established a stable and leading market position in China's raw milk market. In terms of production, the Group accounted for more than 70% of the milk source supply of Milk Deluxe, Mengniu Group's premium brand of milk. For other independent third parties, our raw milk is also used for the production of premium milk. The sales volume of premium milk in the PRC has increased consistently for more than 15% in recent years. Looking ahead, the Group's emphasis on quality and premium milk sales remains the growth engine of the future.

Turnover of the Group reached RMB2,585 million for the six months ended 30 June 2014, representing a growth of 86.2% from RMB1,388 million in the corresponding period of 2013. This was primarily attributable to significant increase of sales volume of our products during the reporting period.

Cash EBITDA (earnings before loss arising from changes in fair values less costs to sell of dairy cows, loss arising on financial liabilities designated as at FVTPL, gain arising on financial assets designated at FVTPL, net loss on disposal of property, plant and equipment, realised changes in fair value of dairy cows recognised in cost of sales, interest, taxes, depreciation and amortization) increased by 140.5% from RMB408.2 million in the corresponding period last year to RMB981.9 million for the six months ended 30 June 2014. Cash EBITDA margin increased from 29.4% in the corresponding period last year to 38.0% for the six months ended 30 June 2014. The Company considers that such increase for the six months ended 30 June 2014 was mainly due to (i) the expansion of the number of milkable cows and continuous improvement in the milk yield per milkable cow, (ii) an increase in sales of our branded milk, (iii) persistent increase in both the production volume and the unit price of raw milk, and (iv) effective control of costs and expenses.

During the period, the Group's own brand of milk was awarded gold prize in the food category by Monde Selection, the International Institute for Quality Selections. As an independent international organization jointly established by the European Community (EC) and the Ministry of Foreign Affairs and Trade of Belgium (比利時經貿部) in 1961, the International Institute for Quality Selections is currently the oldest, the most representative and the most authoritative food quality testing organization in the world. Its prizes are awarded for the purpose of monitoring food quality and are regarded as the "Nobel Prize" in the international food sector. The contest awards prizes after conducting strict reviews and inspections of the safety, taste, packaging and raw materials of food products. This gold prize further proves that the Group's own brand of milk has won international recognition for its high quality in purity and freshness, and adds confidence and momentum to the future development of the PRC dairy industry.

Our Farms



As of 30 June 2014, the Group had 22 farms operating, 2 farms under construction invested through the joint venture and 2 farms under construction by the Group in the PRC with approximately 190,027 dairy cows in own farms in total. There are approximately 2,544 dairy cows in total through the joint venture.

Herd size

	As of	
	30 June 2014 Heads	31 December 2013 Heads
<b>Dairy cows</b>		
Milkable cows	107,516	98,791
Heifers and calves	82,511	88,047
<b>Total dairy cows</b>	<b>190,027</b>	<b>186,838</b>

As at 30 June 2014, we are the largest dairy farming company in terms of herd size as well as the largest raw milk producer in the PRC. As at 30 June 2014, the current herd size is 190,027 compared to 186,838 as at 31 December 2013.

## Milk Yield

Our financial results are directly affected by our milk yield per cow. In general, as milk yield per cow improves, the costs of production of a unit of milk decreases. Milk yield per cow is affected by a number of factors, including a cow's stage of lactation, breed, genetics and feed mix. We have achieved an average annual milk yield of 9.0 tons for the six months ended 30 June 2014, representing an increase of 7.1% from 8.4 tons for last corresponding period. Such results are attributable to effective herd management, genetic improvement of our cows through generations and increase in number of cows reaching the peak stage of lactation.

## Financial Overview

### Turnover

The following table sets out the breakdown of our consolidated turnover by our two operating segments for the six months ended 30 June 2014 and 30 June 2013:

	Six months ended 30 June					
	External Sales RMB'000	2014 Internal Supplies RMB'000	Subtotal RMB'000	External Sales RMB'000	2013 Internal Supplies RMB'000	Subtotal RMB'000
Sales of raw milk business	2,250,575	169,746	2,420,321	1,271,031	47,309	1,318,340
Liquid milk products business	284,639	—	284,639	117,002	—	117,002
Sales of dairy cow business	49,321	—	49,321	—	—	—
Consolidated turnover	2,584,535	169,746	2,754,281	1,388,033	47,309	1,435,342

Our turnover increased by 86.2% from RMB1,388 million for the six months ended 30 June 2013 to RMB2,585 million for the six months ended 30 June 2014 primarily due to significant increase in our sales of raw milk and liquid milk products.

- *Dairy farming business*

Turnover from our dairy farming business increased substantially primarily due to growth of our cow herd and increase in average selling price of our quality raw milk as a result of the shortage of raw milk in the market.

The following table sets out the sales amount, sales volume and average selling price (ASP) per tonne of our raw milk for the periods indicated:

	Six months ended 30 June					
	2014			2013		
	Sales Amount RMB'000	Sales Volume Tonne	ASP RMB'000/ Tonne	Sales Amount RMB'000	Sales Volume Tonne	ASP RMB'000/ Tonne
<b>Raw Milk</b>						
External Sales	2,250,575	438,142	5.14	1,271,031	295,746	4.30
Internal Supplies	169,746	31,387	5.41	47,309	10,696	4.42
Subtotal	2,420,321	469,529	5.15	1,318,340	306,442	4.30

Turnover attributable to the internal use of raw milk increased substantially due to strong growth of our liquid milk business. As the processing plant for producing liquid milk is currently located in southern area where milk price is generally higher than that in northern area, the selling price of raw milk for internal supplies is higher than the average selling price for external sales of national farms.

	Six months ended 30 June					
	2014			2013		
	Sales Amount RMB'000	Sales Volume Heads	ASP RMB'000/ Head	Sales Amount RMB'000	Sales Volume Heads	ASP RMB'000/ Head
Dairy cows	49,321	2,549	19.3	—	—	—

- *Liquid milk products business*

Turnover from our liquid milk products business increased by 143.2% from RMB117.0 million for the six months ended 30 June 2013 to RMB284.6 million for the six months ended 30 June 2014, which accounted for 11.0% and 8.4% of our consolidated turnover for the six months ended 30 June 2014 and 2013, respectively.

The strong growth of our liquid milk products business was a result of strong market demand for our liquid milk products. The total volume of liquid milk sold increased by 149.3% from 10,369 tonnes for the six ended 30 June 2013 to 25,849 tonnes for the six months ended 30 June 2014. The following table sets out the breakdown of sales amount, sales volume and average selling price per tonne of our liquid milk products for the periods indicated:

	Six months ended 30 June					
	2014			2013		
	Sales Amount RMB'000	Sales Volume Tonne	ASP RMB'000/ Tonne	Sales Amount RMB'000	Sales Volume Tonne	ASP RMB'000/ Tonne
Liquid Milk Products	284,639	25,849	11.01	117,002	10,369	11.28



**Cost of sales**

Our cost of sales primarily consisted of dairy farming cost and liquid milk products cost. Costs of sales of dairy farming business include feeds cost, labor cost, utilities, depreciation and other costs of farms. Costs of sales of liquid milk products business include raw materials, labor cost, depreciation, utilities and other processing costs. The following table sets forth a breakdown of our cost of sales for our products for the periods indicated:

**Costs of sales of dairy farming business**

	Six months ended 30 June			
	2014		2013	
	RMB'000	%	RMB'000	%
<b>Costs of sales of raw milk business:</b>				
Feeds cost	1,152,786	78.0%	759,432	77.2%
Labor cost	80,890	5.5%	51,637	5.2%
Utilities	34,996	2.4%	28,076	2.9%
Depreciation	84,447	5.7%	57,135	5.8%
Other costs of farms	125,404	8.4%	87,704	8.9%
Subtotal of costs of sales of raw milk business	1,478,523	100%	983,984	100%
Inter-segment cost	(165,137)		(47,309)	
<b>Costs of sales of raw milk external, net</b>	<b>1,313,386</b>		<b>936,675</b>	
<b>Dairy cow business</b>	<b>49,321</b>		<b>—</b>	
<b>Total cost of sales of dairy farming business</b>	<b>1,362,707</b>		<b>936,675</b>	

With the expansion of our herd size and general increase in market price of feeds, total feed costs (before offsetting the internal relative costs of sales of the supply of raw milk) for the six months ended 30 June 2014 increased to RMB1,152.8 million from RMB759.4 million for the same period last year, representing an increase of 51.8%. Sales of raw milk (before offsetting the internal relative sales income from the supply of raw milk) increased by 83.6% to RMB2,420.3 million for the six months ended 30 June 2014 from RMB1,318.3 million for the same period last year.

Meanwhile, cost (excluding depreciation) per ton of raw milk sold (before offsetting the internal relative costs of sales of the supply of raw milk) decreased by 1.9% from RMB3,025 for the same period last year to RMB2,969 for the six months ended 30 June 2014, mainly due to the increase in the annual milk yield per cow by 7.1% from 8.4 tons for the same period last year to 9.0 tons for the six months ended 30 June 2014.

**Costs of sales of liquid milk product business**

	Six months ended 30 June			
	2014		2013	
	RMB'000	%	RMB'000	%
Raw materials	189,630	87.6%	66,663	76.6%
Labor cost	6,891	3.2%	5,394	6.2%
Depreciation	9,095	4.2%	9,602	11.0%
Utilities	4,447	2.1%	2,257	2.6%
Other processing costs	6,415	2.9%	3,089	3.6%
	<b>216,478</b>	<b>100%</b>	<b>87,005</b>	<b>100%</b>

With the increase in sales volume of liquid milk and the price hike of raw milk, raw material cost for the six months ended 30 June 2014 increased from RMB66.7 million for the same period last year to RMB189.6 million, representing an increase of 184.3%. Sales of liquid milk increased by 143.2% to RMB284.6 million for the six months ended 30 June 2014 from RMB117.0 million for the same period last year.

Due to the price hike of raw milk, cost (excluding depreciation) per ton of liquid milk sold increased by 7.5% from RMB7,465 for the same period last year to RMB8,023 for the six months ended 30 June 2014.

**Gross profit and gross margin**

The following table sets forth the breakdown of our gross profit by our two operating segments as well as their respective gross margin, for the years indicated:

	Six months ended 30 June			
	2014		2013	
	Gross Profit RMB'000	Gross Margin	Gross Profit RMB'000	Gross Margin
<b>Dairy farming business</b>				
Before offsetting	941,798	38.1%	334,356	25.4%
After offsetting	937,189	40.7%	334,356	26.3%
<b>Liquid milk products business</b>	68,161	23.9%	29,997	25.6%

- *Dairy farming business*

Gross profit of our dairy farming business (before offsetting the internal relative costs of sales of the supply of raw milk) increased by 181.7% from RMB334.3 million for the six months ended 30 June 2013 to RMB941.8 million for the six months ended 30 June 2014. The increase was primarily due to the substantial increase in the sales volume and the average selling price of our raw milk.

Gross margin of our dairy farming business (before offsetting the internal relative costs of sales of the supply of raw milk) remained at a high level at 38.1% for the six months ended 30 June 2014 compared to 25.4% for the six months ended 30 June 2013, primarily due to increase of average selling price of raw milk and milk yield per cow.

## Management Discussion and Analysis

- *Liquid milk products business*

Gross profit of our liquid milk products business increased by 127.3% from RMB30.0 million for the six months ended 30 June 2013 to RMB68.2 million for the six months ended 30 June 2014. The increase was primarily due to the increase in sales volume our branded milk products.

Gross margin of our liquid milk products business decreased from 25.6% for the six months ended 30 June 2013 to 23.9%, mainly due to the increase of market price of raw milk.

### Loss arising from changes in the fair value less costs to sell of dairy cows

The Group's dairy cows were fair valued by the directors of the Company at 30 June 2014 while the fair value of the Group's dairy cows at 31 December 2013 has been arrived at on the basis of a valuation carried out by independent qualified professional valuer. Loss arising from changes in the fair value of biological assets was RMB84.6 million for the six months ended 30 June 2014 (six months ended 30 June 2013: loss of RMB66.3 million). This was mainly attributable to the increase in ratio of milkable cows among our herd across generations, and after producing milk of milkable cows and along with increase of lactation period, impairment will be occurred as cash flow generated in the future will be reduced.

### Other Income

For the six months ended 30 June 2014, other income amounted to RMB 19.9 million (six months ended 30 June 2013: RMB 53.6 million). Other income mainly consisted of government grants and interest income, among others, interest income for the six months ended 30 June 2014 amounted to RMB 11.3 million (six months ended 30 June 2013: RMB 6.4 million), in which government grants for the six months ended 30 June 2014 amounted to RMB6.3 million (six months ended 30 June 2013: RMB44.4 million). Government grants mainly consisted of subsidies for agricultural projects (for example: circulation economic subsidy, agricultural integrated development subsidy, straw utilization subsidy and sizable farm subsidy, etc.).

### Operating expenses

	Six months ended 30 June,	
	2014 RMB'000	2013 RMB'000
Selling and distribution expenses	49,217	23,250
Administrative expenses	106,806	67,142
Total operating expenses	156,023	90,392

Our operating expenses increased from RMB90.4 million for the six months ended 30 June 2013 to RMB156.0 million for the six months ended 30 June 2014. Selling and distribution expenses mainly consisted of transportation costs from sales of milk, salaries of sales personnel and daily expenses, among others, transportation costs was increased from RMB 19.6 million in the corresponding period last year to RMB 44.0 million for the six months ended 30 June 2014, mainly due to increase in sales volume of raw milk and liquid milk products.

Administrative expenses mainly consisted of salaries of management and other administrative employees (including equity-based share option expenses), and depreciation of office building, staff quarters and equipments, among others, salaries (excluding equity-based share option expenses) of management was increased from RMB30.8 million in the corresponding period last year to RMB42.8 million for the six months ended 30 June 2014.

Equity-based share option expenses included in the administrative expenses for the period increased from RMB3.4 million for the corresponding period last year to RMB17.0 million for the six months ended 30 June 2014, mainly due to the granting of 80 million options to employees pursuant to the employee share option incentive scheme on 6 June 2014.

#### ***Other Gains and Losses***

Losses arising from other gains and losses amounted to RMB99.6 million (for the six months ended 30 June 2013: gains arising from other gains and losses amounted to RMB3.6 million). This is mainly due to a loss of RMB84.7 million arising from an one-off measurement at fair value accounted in the current loss in respect of the transaction cost payable to investing shareholders anticipated upon the exercise of put options and call options in future period as assessed during the period. Those two types options were the put options granted to Success Dairy II Limited by the Company and the call options granted to the Company by the Success Dairy II Limited pursuant to the agreement entered into between the Company and Success Dairy II Limited for the establishment of two joint venture companies on 23 September 2013. Details are set out in note 12 to the unaudited interim condensed consolidated financial statements.

#### **Finance costs**

Finance costs increased from RMB94.9 million for the last corresponding period to RMB134.9 million for the six months ended 30 June 2014. This was mainly attributable to the increase in bank loans and interest expense no longer being capitalized following the transfer of construction in progress to property, plant and equipment.

#### **Profit Attributable to the Owners of the Company**

Taking into account of all the above factors, the Group's profit attributable to the owners of the Company was RMB523.2 million for the six months ended 30 June 2014. This represents an increase of 240.6% from RMB153.6 million for corresponding period last year.

Basic earnings per share were approximately RMB10.84 cents (six months ended 30 June 2013: RMB3.19 cents).

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

For the six months ended 30 June 2014, the Group's cash flow from operating activities amounted to RMB1,037.1 million, as compared to RMB368.2 million in the corresponding period last year.

As at 30 June 2014, the Group's available and unutilised banking facilities amounted to approximately RMB7,565.3 million (31 December 2013: RMB3,668.1 million). The Group's management are of the opinion that the working capital available to the Group is sufficient for its present needs.

## Management Discussion and Analysis

The table below sets forth our short-term and long-term borrowings as at the dates indicated below.

	As at	
	30 June 2014 RMB'000 (Unaudited)	31 December 2013 RMB'000 (Audited)
Bank borrowings	4,025,277	3,748,666
Unsecured borrowings	1,950,102	1,533,139
Secured borrowings	1,814,175	1,964,527
Guaranteed borrowings	261,000	251,000
	4,025,277	3,748,666
<b>Carrying amount repayable:</b>		
Within one year	2,641,122	1,788,799
Between one to two years	714,825	1,042,337
Between two to five years	669,330	917,530
	4,025,277	3,748,666
Less: Amounts due within one year shown under current liabilities	(2,641,122)	(1,788,799)
	1,384,155	1,959,867

As at 30 June 2014, the gearing ratio, being the ratio of total borrowings (including short-term debenture) to total assets was 38.9% (31 December 2013: 39.6%). The annual interest rate of the banks and other borrowings for the six months ended 30 June 2014 varied from 1.73% to 7.05% (six months ended 30 June 2013: 1.78% to 7.05%, six months ended 31 December 2013: 2.00% to 7.05%). As at 30 June 2014, all borrowings were denominated in Renminbi and United States Dollar ("US\$").

### PLEDGE OF ASSETS

As at 30 June 2014, land use rights, buildings and equipment, and biological assets with carrying value of RMB10.0 million (31 December 2013: RMB10.2 million), RMB56.9 million (31 December 2013: RMB59.2 million) and RMB4,250.9 million (31 December 2013: RMB4,014.2 million), respectively, were pledged as security for bank borrowings.

### CAPITAL COMMITMENTS AND CONTINGENCIES

As at 30 June 2014, the Group had capital commitments of RMB299.5 million related to acquisition of property, plant and equipment and capital contribution to joint ventures.

The Group did not have any significant contingent liabilities as at 30 June 2014.

### FINANCIAL MANAGEMENT POLICIES

The Group continues to closely manage financial risks to safeguard the interests of the shareholders of the Company. The Group applies its cash flows generated from operation and bank loans to its operational and investment needs.

The Group's management consider that the Group has limited foreign currency exposure in respect of its operations since its operations are mainly conducted in the PRC. Sales and purchases are mainly denominated in Renminbi and the foreign currency risks associated with concentrated feeds and farm facilities are not material. In view of the minimal foreign currency exchange risk related to its operations, the Group currently does not use any derivative contracts to hedge against its exposure to foreign currency risks.

## **HUMAN RESOURCES AND REMUNERATION OF EMPLOYEES**

The Group had approximately 5,129 employees (31 December 2013: 5,288) in mainland China and Hong Kong as at 30 June 2014. Total staff costs (including staff compensation capitalized to unmatured dairy cows) for the six months ended 30 June 2014 were approximately RMB199.3 million (six months ended 30 June 2013: RMB137.0 million).

The Group values recruiting, training and retaining quality personnel. We recruit talented employees from local universities, vocational schools and other technical schools, and we provide these employees with various pre-employment and on-the-job training. The Group also offers remuneration at competitive rates with the aim of retaining quality personnel and two share option schemes to encourage and reward employees to contribute in terms of company performance.

## **PROSPECTS**

Looking ahead, with the continued increase in the consumption standard of residents in the PRC and their increasing health awareness, it is expected that the demand for high-end premium raw milk will continue to increase. The per capita milk consumption by residents in the PRC is still far lower than the world average level. It is anticipated that there is still much room for an increase in the demand for raw milk in the PRC. All these factors have contributed to a favourable external environment for the further development of the modern animal husbandry industry.

The Group's own brand of milk has undergone stringent reviews and was awarded gold prize in the food category by Monde Selection, the International Institute for Quality Selections, out of various products from all over the world in the competition. This entails the Group's own brand of milk has gained recognition and praise from countries around the world, including developed countries in food. Joseph Bessemans, President of Monde Selection, fully recognized and commended the Group's own brand of milk at the prize presentation ceremony. By leveraging on the momentum resulting from being awarded the gold prize at Monde Selection, the Group will step up its marketing efforts. It is expected that the sales of the Group's own brand of milk will experience noticeable growth.

In view of the increasing awareness of health quality and safety, the Group has strived to maintain good product quality control while actively developing the downstream business. During the period, the Group established a dedicated team which was mainly responsible for the sales of its own brand of milk and the Group planned to gradually expand its existing sales network from East China and North China to most regions of the PRC. With the continued expansion of the sales network, it is expected that the sales of the Group will continue to increase, generating considerable income for the Group.

In addition, the Group will establish a company to sell low-temperature branded milk using the pasteurized processing technology to develop a sales network for low-temperature branded milk.

The Group has been actively improving the structure of the herd of cows. So far, the Group has 190,027 dairy cows. It is expected that the average milk yield for the year can reach 8.7 tons (six months ended 31 December 2013: 8.5 tons). With the increasing yield per milkable cow and growth of our cow herd, the Group is confident that the annual milk volume for 2015 will reach 1 million tons.

# Other Information

## DIRECTORS' AND CHIEF EXECUTIVE'S INTERESTS AND SHORT POSITIONS IN SHARES, UNDERLYING SHARES AND DEBENTURES

As at 30 June 2014, the interests and short positions of the directors of the Company (the "Directors") in the shares, underlying shares and debentures of the Company and its associated corporations (within the meaning of Part XV of the Securities and Futures Ordinance (Chapter 571 of the laws of Hong Kong) (the "SFO")) as recorded in the register required to be kept by the Company under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code for Securities Transactions by Directors of Listed Issuers (the "Model Code") were as follows:

Name of Director	Nature of interest	Number of Shares or underlying Shares	Approximate percentage of shareholding interest
Ms. GAO Lina <sup>(1)</sup>	Interest in controlled corporation	219,581,733	4.55%
	Beneficial owner	40,756,516 <sup>(3)</sup>	0.84%
Mr. HAN Chunlin	Beneficial owner	28,554,583 <sup>(2)</sup>	0.59%
Mr. SUN Yugang	Beneficial owner	16,064,990 <sup>(2)</sup>	0.33%
Mr. LIU Fuchun	Spouse	170,000	0.00%

(1) Ms. Gao holds approximately 49.12% of the interests in Jinmu Holdings Co. Ltd ("Jinmu"). Ms. Gao is deemed to be interested in the 219,581,733 shares held by Jinmu under the SFO.

(2) These represent interest in underlying shares of the Management Options and share options granted by the Company, details of which are set out in the section "Management Options" and "Share Option Scheme" below.

(3) This represent 1,600,000 ordinary shares and 39,156,516 share options in underlying shares of the Management Options and share options.

Saved as disclosed above, as at 30 June 2014, none of the Directors and the chief executive of the Company and their respective associates had any interests or short positions in the shares, underlying shares and debentures of the Company or any of its associated corporations (within the meaning of Part XV of the SFO) as recorded in the register of the Company required to be kept under Section 352 of the SFO or as otherwise notified to the Company and the Stock Exchange pursuant to the Model Code.

## SUBSTANTIAL SHAREHOLDERS' INTERESTS

As at 30 June 2014, the interests or short positions of substantial shareholders, other than the Directors or the chief executive of the Company whose interests and short positions in the shares of the Company and of its associated corporations (within the meaning of Part XV of the SFO) as set out above, in the shares and underlying shares of the Company as recorded in the register required to be maintained under Section 336 of the SFO were as follows:

Name	Capacity/ Nature of interest	Number of Shares	Approximate percentage of shareholding interest
China Mengniu Dairy Company Ltd	Beneficial interest	1,347,903,000	27.92%
Xinmu Holdings Co Ltd.	Beneficial interest	671,021,025	13.90%
Yinmu Holdings Co Ltd.	Beneficial interest	446,465,419	9.25%

Save as disclosed above, the Company had not been notified of any other interests or short positions in the shares or underlying shares representing 5% or more of the issued share capital of the Company or as recorded in the register required to be maintained under section 336 of the SFO as at 30 June 2014.

## MANAGEMENT OPTIONS

The Company granted share options to certain Directors and chief executives for the purpose of providing incentives and rewards to their contributions to the success of the Group's operations. The following Management Options were outstanding during the period:

Name of grantee	Date of grant	Number of underlying shares which may be issued pursuant to the Management Options				
		As at 1 January 2014	Granted during the period	Exercised during the period	Lapsed during the period	As at 30 June 2014
Ms. GAO Lina	31 October 2010	29,276,916	—	—	—	29,276,916
Mr. HAN Chunlin	31 October 2010	21,653,916	—	—	—	21,653,916
Mr. SUN Yugang	31 October 2010	9,142,924	—	—	—	9,142,924
		60,073,756	—	—	—	60,073,756

These options are exercisable during the period commencing from the Listing Date (26 November 2010) until 10 years from the date of offer.

As at 30 June 2014, the number of shares to be issued upon the exercise of the outstanding options is 60,073,756 shares, representing 1.24% of the issued share capital of the Company as at that date.



## SHARE OPTIONS

### Share Option Scheme Adopted on 17 November 2011 (“Share Option Scheme I”)

The Company unconditionally adopted a share option scheme on 17 November 2011. The following share options were outstanding under the Share Option Scheme I during the Review Period:

Name or category of participant	Number of shares which may be issued pursuant to the Share Options Scheme I					As at 30 June 2014	Option period
	As at 1 January 2014	Granted during the period	Exercised during the period	Cancelled and lapsed during the period	As at 30 June 2014		
<b>Directors</b>							
Ms. GAO Lina	2,879,600	—	—	—	2,879,600	12.12.2012-30.6.2020	
Mr. HAN Chunlin	1,900,667	—	—	—	1,900,667	12.12.2012-30.6.2020	
Mr. SUN Yugang	1,922,066	—	—	—	1,922,066	12.12.2012-30.6.2020	
Subtotal	6,702,333	—	—	—	6,702,333		
<b>Other employees</b>							
In aggregate	26,925,440	—	—	(598,718)	26,326,722	12.12.2012-30.6.2020	
Total	33,627,773	—	—	(598,718)	33,029,055		

Notes:

- All the share options were granted on 12 December 2012 and the exercise price is HK\$2.89.
- The share options granted (the “Scheme I Granted Options”) to each grantee under the Share Option Scheme I (the “Scheme I Grantee”) are deemed to be divided into three tranches, each of which consists of one third of the Scheme I Granted Options and will be associated with a performance target within a specific financial period (the “Scheme I Performance Target”). The Scheme I Performance Target has been determined by the board of directors of the Company (“Board”) and specified in the offer letter to each Scheme I Grantee. The financial period for the first tranche is the twelve months ended 30 June 2013; the financial period for the second tranche is the twelve months ended 30 June 2014; and the financial period for the third tranche will be the twelve months ending 30 June 2015. The corresponding tranche will accrue if the Scheme I Performance Target set for the relevant financial period is met.
- The Scheme I Granted Options accrued in accordance with the above paragraph shall vest on a one-off basis within 30 days after the date of publication of the results announcement for the six months ending 30 June 2015. Any Scheme I Granted Options not accrued as a result of non-fulfillment of any Scheme I Performance Target shall automatically lapse.
- The share options represent personal interest held by the relevant Directors as beneficial owners.

### Share Option Scheme Adopted on 5 June 2014 (“Share Option Scheme II”)

The Company unconditionally adopted a share option scheme on 5 June 2014. The following share options were outstanding under the Share Option Scheme II during the Review Period:

Name or category of participant	Number of shares which may be issued pursuant to the Share Options Scheme II					As at 30 June 2014	Option period
	As at 1 January 2014	Granted during the period	Exercised during the period	Cancelled and lapsed during the period	As at 30 June 2014		
<b>Directors</b>							
Ms. GAO Lina	—	7,000,000	—	—	7,000,000	6.6.2014-29.4.2022	
Mr. HAN Chunlin	—	5,000,000	—	—	5,000,000	6.6.2014-29.4.2022	
Mr. SUN Yugang	—	5,000,000	—	—	5,000,000	6.6.2014-29.4.2022	
Subtotal	—	17,000,000	—	—	17,000,000		
<b>Other employees</b>							
In aggregate	—	63,000,000	—	—	63,000,000	9.6.2014-29.4.2022	
Total	—	80,000,000	—	—	80,000,000		

Notes:

- All the share options were granted on 6 June 2014 and the exercise price is HK\$3.38.
- The share options granted (the “Scheme II Granted Options”) to each grantee under the Share Scheme II (the “Scheme II Grantees”) are deemed to be divided into three tranches, each of which consists of one third of the Scheme II Granted Options and will be associated with a performance target within a specific financial period (the “Scheme II Performance Target”). The Scheme II Performance Target has been determined by the Board and specified in the offer letter to each Scheme II Grantee. The financial period for the first tranche will be the 2014 financial year; the financial period for the second tranche will be the 2015 financial year; and the financial period for the third tranche will be the 2016 financial year. The corresponding tranche will accrue if the Scheme II Performance Target set for the relevant financial period is met.
- The Scheme II Granted Options accrued in accordance with the above paragraph shall vest on a one-off basis within 30 days after the date of publication of the results announcement for the 2016 financial year. Any Scheme II Granted Options not accrued as a result of non-fulfillment of any Scheme II Performance Target shall automatically lapse.
- The share options represent personal interest held by the relevant Directors as beneficial owners.

For more details of the share option schemes adopted by the Company, please refer to Note 18 to the Condensed Consolidated Financial Statements.

Save as disclosed above, during the Review Period, the Company or any of its subsidiaries was not a party to any arrangements whose objects are, or one of whose objects is, to enable the Directors to acquire benefits by means of the acquisition of shares in, or debentures of, the Company or any other body corporate. Save for those disclosed above, during the six months ended June 30, 2014, none of the Directors (including their spouses and children under the age of 18) held any interests in or was granted any right to subscribe for the securities of the Company or its associated corporations (within the meaning of Part XV of the SFO), or had exercised any such rights.

## CORPORATE GOVERNANCE

The Company has adopted the code provisions set out in the Corporate Governance Code and Corporate Governance Report (“CG Code”) as set out in Appendix 14 to the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited (“Listing Rules”). The Company has, throughout the six months ended 30 June 2014 complied with the code provisions set out in the CG Code, except for the deviations from code provision A.6.7 which is explained below.

## Other Information

Code provision A.6.7 of the CG Code provides, among other things, that independent non-executive Directors and other non-executive Directors should attend general meetings and develop a balanced understanding of the views of shareholders. Mr. Han Chunlin, the executive Director, Mr. Hui Chi Kin Max and Mr. Ding Sheng, the non-executive Directors and Mr. Liu Fu Chun, the independent non-executive Director, were not able to attend the annual general meeting of the Company held on 5 June 2014 due to other business engagements.

## MODEL CODE FOR SECURITIES TRANSACTIONS BY DIRECTORS

The Company has adopted the Model Code as set out in Appendix 10 to the Listing Rules as the Company's code of conduct regarding securities transactions by Directors. Following specific enquiring by the Company, all Directors confirmed that they have complied with the required standards set out in the Model Code throughout the six months ended 30 June 2014.

## CHANGE OF DIRECTOR AND CHANGES OF DIRECTOR'S INFORMATION

Pursuant to rule 13.51B(1) of the Listing Rules, the change of directors' information of the Company since the date of the 2013 Annual Report are as follows:

Mr. DING Sheng tendered his resignation as non-executive Director of the Company effective from 26 June 2014.

Mr. LIU Fu Chun tendered his resignation as an independent non-executive Director of the Company, a member of the audit committee and the remuneration committee of the Company with effect from each of 25 August 2014.

### Mr. WU Jingshui (吳景水)

Mr. WU Jingshui ("Mr. Wu") has been appointed as a non-executive Director of the Company with effect from 26 June 2014.

Mr. Wu Jingshui, aged 48, graduated from Inner Mongolia Light Industry Institute majoring in industrial enterprise financial accounting. Mr. Wu also holds a Master's degree from Inner Mongolia Agricultural University and a Master of Business Administration degree from China Europe International Business School. He also holds a PRC senior accountant qualification and has extensive experience in financial management.

Mr. Wu served as executive director of China Mengniu Dairy Company Limited ("Mengniu"), a company listed on the Stock Exchange (stock code: 2319), from March 2010 to March 2014, and also served as Chief Financial Officer of Mengniu from March 2010 to August 2013. Mr. Wu was appointed Vice President (Finance) of Inner Mongolia Mengniu Dairy (Group) Co., Ltd ("Inner Mongolia Mengniu") in April 2008, and before that served as the Financial General Manager of the liquid milk division and the Chief Financial Officer of Inner Mongolia Mengniu. In 2010, Mr. Wu was honoured as a "Labour Model (Progressive Staff) of Hohhot." Mr. Wu is currently a non-executive director of Yashili International Holdings Ltd., a company listed on the Stock Exchange.

In connection with his appointment as Director, Mr. Wu entered into a letter of appointment with the Company for a term of three years commencing from 26 June 2014 and is subject to retirement by rotation and re-election at annual general meetings in accordance with the Company's Articles of Association. Mr. Wu is not entitled to any remuneration.

Save as disclosed above, Mr. Wu does not have relationships with any Directors, senior management or substantial or controlling shareholders of the Company. He has not held any other directorships in any public companies the securities of which are listed on the Stock Exchange or overseas in the last three years or any other positions in the Company or any of its subsidiaries, and he does not have any other interests in the shares of the Company within the meaning of Part XV of the SFO.

### Mr. ZOU Fei (鄒飛)

Mr. ZOU Fei ("Mr. Zou") has been appointed as an independent non-executive Director of the Company and also a member of each of the audit committee and remuneration committee of the Company with effect from 25 August 2014.

Mr. Zou, aged 41, holds a master's degree in economics and a doctor's degree in finance from University of Texas of the United States of America. He is also a chartered financial analyst, a member of Chinese Finance Association of America and one of the experts listed in "Thousand Talents Program" launched by the PRC.

Mr. Zou previously served in various positions such as a fund manager of American Century Investments, a managing director of special investment department of China Investment Corporation, the former chairman of the board of Chinese Finance Association of America and the board observer of Noble Group in Singapore. He is currently serving in positions such as the president of Synergy Capital and is an independent director of Delta Dunia Makmur TBK PT in Indonesia, senior consultant of Louis Dreyfus Commodities in France.

In connection with his appointment as Director, Mr. Zou entered into a letter of appointment with the Company for a term of three years commencing from 25 August 2014 and is subject to retirement by rotation and re-election at annual general meetings of the Company in accordance with the Company's articles of association. Mr. Zou is entitled to an annual remuneration of RMB200,000.

Save as disclosed above, Mr. Zou does not have any relationship with any other Directors, senior management or substantial or controlling shareholders of the Company. He has not held any other directorships in any public companies the securities of which are listed on the Stock Exchange or overseas in the last three years or any other positions in the Company or any of its subsidiaries, and he does not have any other interests in the shares of the Company within the meaning of Part XV of the SFO.

#### **Mr. LEE Kong Wai, Conway**

The Company was informed by Mr. LEE Kong Wai, Conway that after the Company's last published 2013 Annual Report, the changes in his biographical details are as follows:

Mr. LEE Kong Wai, Conway was appointed as an independent non-executive director of GSL New Energy Holdings Limited, a company listed on the Stock Exchange (stock code: 451), commencing from 9 May 2014. Mr. Lee was appointed as a non-executive Director and the Deputy Chairman of Merry Garden Holdings Limited, a company listed on the Stock Exchange (Stock code: 1237), commencing from 16 July 2014. Mr. Lee was appointed as an independent non-executive director of WH Group Limited, a company listed on the Stock Exchange (stock code: 288), commencing from 5 August 2014. Mr. Lee was appointed as an independent non-executive director of China Rundong Auto Group Limited, a company listed on the Stock Exchange (Stock code: 1365), commencing from 12 August 2014.

Save for the information disclosed above, there is no other information required to be disclosed pursuant to Rule 13.51B(1) of the Listing Rules.

## **PURCHASE, SALES OR REDEMPTION OF THE COMPANY'S LISTED SECURITIES**

Neither the Company nor any of its subsidiaries has purchased, sold or redeemed any of the Company's listed securities during the six months ended 30 June 2014.

## **THE BOARD'S DIVERSITY POLICY**

The Board has adopted the Diversity Policy, which sets out the approach to diversity of Board members. In determining the Board composition, the Company considers a range of diversity elements, including but not limited to gender, age, cultural and education background, professional experience, skills and knowledge. All appointments of the Board will be made based on merit and objective criteria while taking into full account of the interest of Board's diversity.

The selection of candidate will be based on a range of diversity elements. The final decision will be made according to the strengths of the candidate and his/her contribution that would bring to the Board.

## **REVIEW OF INTERIM RESULTS**

The condensed consolidated financial statements of the Group for the six months ended 30 June 2014 have been reviewed by the Group's auditor, Deloitte Touche Tohmatsu, in accordance with Hong Kong Standard on Review Engagements 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Hong Kong Institute of Certified Public Accountants and the audit committee of the Company (the "Audit Committee").

The Audit Committee comprises Mr. LEE Kong Wai, Conway, Mr. HUI Chi Kin, Max and Mr. ZOU Fei.

On behalf of the Board  
**China Modern Dairy Holdings Ltd.**  
**Ms. GAO Lina**

*Deputy Chairman, Chief Executive Officer and Executive Director*

Hong Kong, 25 August 2014

# Report on Review of Condensed Consolidated Financial Statements



TO THE BOARD OF DIRECTORS OF CHINA MODERN DAIRY HOLDINGS LTD.  
(Incorporated in the Cayman Islands with limited liability)

## INTRODUCTION

We have reviewed the condensed consolidated financial statements of China Modern Dairy Holdings Ltd. (the "Company") and its subsidiaries (collectively referred to as the "Group") set out on pages 21 to 48, which comprise the condensed consolidated statement of financial position as of 30 June 2014 and the related condensed consolidated statement of profit or loss and other comprehensive income, condensed consolidated statement of changes in equity and condensed consolidated statement of cash flows for the six months then ended, and certain explanatory notes. The Main Board Listing Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited require the preparation of a report on interim financial information to be in compliance with the relevant provisions thereof and International Accounting Standard 34 "Interim Financial Reporting" ("IAS 34") issued by the International Accounting Standards Board. The directors of the Company are responsible for the preparation and presentation of these condensed consolidated financial statements in accordance with IAS 34. Our responsibility is to express a conclusion on these condensed consolidated financial statements based on our review, and to report our conclusion solely to you, as a body, in accordance with our agreed terms of engagement, and for no other purpose. We do not assume responsibility towards or accept liability to any other person for the contents of this report.

## SCOPE OF REVIEW

We conducted our review in accordance with Hong Kong Standard on Review Engagements 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity" issued by the Hong Kong Institute of Certified Public Accountants. A review of these condensed consolidated financial statements consists of making inquiries, primarily of persons responsible for financial and accounting matters, and applying analytical and other review procedures. A review is substantially less in scope than an audit conducted in accordance with Hong Kong Standards on Auditing and consequently does not enable us to obtain assurance that we would become aware of all significant matters that might be identified in an audit. Accordingly we do not express an audit opinion.

## CONCLUSION

Based on our review, nothing has come to our attention that causes us to believe that these condensed consolidated financial statements for the six months ended 30 June 2014 are not prepared, in all material respects, in accordance with IAS 34.

Without qualifying our review conclusion, we draw attention to the fact that the comparative condensed consolidated statement of profit or loss and other comprehensive income, condensed consolidated statement of changes in equity and condensed consolidated statement of cash flows for the six months ended 30 June 2013, and the relevant explanatory notes included in these condensed consolidated financial statements have not been reviewed in accordance with Hong Kong Standard on Review Engagements 2410 "Review of Interim Financial Information Performed by the Independent Auditor of the Entity".

**Deloitte Touche Tohmatsu**

*Certified Public Accountants*

Hong Kong

25 August 2014

# Condensed Consolidated Statement of Profit or Loss and Other Comprehensive Income

For the six months ended 30 June 2014

		Six months ended 30 June	
NOTES		2014 RMB'000 (Unaudited)	2013 RMB'000 (Unaudited)
Turnover	4	2,584,535	1,388,033
Cost of sales		(1,579,185)	(1,023,680)
Gross profit		1,005,350	364,353
Loss arising from changes in fair value less costs to sell of dairy cows	13	(84,559)	(66,343)
Other income	5	19,925	53,603
Selling and distribution expenses		(49,217)	(23,250)
Administrative expenses		(106,806)	(67,142)
Share of profit of an associate		2,796	847
Share of profit of joint ventures		1,943	—
Other gains and losses		(99,641)	3,622
Other expenses		(2,924)	(2,379)
Profit before finance costs and tax	6	686,867	263,311
Finance costs	7	(134,892)	(94,878)
Profit before tax		551,975	168,433
Income tax charge	8	(6,598)	(4,696)
Profit and total comprehensive income for the period		545,377	163,737
Profit and total comprehensive income attributable to:			
Owners of the Company		523,163	153,563
Non-controlling interests		22,214	10,174
		545,377	163,737
Earnings per share (RMB)	10		
Basic		10.84 cents	3.19 cents
Diluted		10.72 cents	3.16 cents

# Condensed Consolidated Statement of Financial Position

As at 30 June 2014

	NOTES	30 June 2014 RMB'000 (Unaudited)	31 December 2013 RMB'000 (Audited)
<b>NON-CURRENT ASSETS</b>			
Property, plant and equipment	11	4,113,612	4,032,642
Land use rights		65,496	66,261
Goodwill		310,426	310,426
Interest in an associate		28,517	25,722
Interest in joint ventures		90,148	32,829
Deposit for acquisition of biological assets		5,463	—
Biological assets	13	6,297,959	5,954,363
Other financial assets	12	92,822	34,517
		<b>11,004,443</b>	<b>10,456,760</b>
<b>CURRENT ASSETS</b>			
Inventories		558,286	691,108
Trade and other receivables	14	599,709	544,710
Land use rights		1,667	1,667
Pledged bank balances		557,147	430,535
Bank balances and cash		457,837	369,041
		<b>2,174,646</b>	<b>2,037,061</b>
<b>CURRENT LIABILITIES</b>			
Trade and other payables	15	1,161,229	1,386,430
Amount due to an associate	21(b)	114,791	87,820
Tax payable		9,927	9,161
Borrowings - due within one year	16	2,641,122	1,788,799
Short-term debenture	17	1,100,000	1,200,000
Deferred income		11,302	10,913
		<b>5,038,371</b>	<b>4,483,123</b>
<b>NET CURRENT LIABILITIES</b>		<b>(2,863,725)</b>	<b>(2,446,062)</b>
<b>TOTAL ASSETS LESS CURRENT LIABILITIES</b>		<b>8,140,718</b>	<b>8,010,698</b>

Condensed Consolidated Statement of Financial Position

As at 30 June 2014

	NOTES	30 June 2014 RMB'000 (Unaudited)	31 December 2013 RMB'000 (Audited)
<b>CAPITAL AND RESERVES</b>			
Share capital		415,261	415,261
Reserves		5,867,894	5,327,763
Equity attributable to owners of the Company		6,283,155	5,743,024
Non-controlling interests		139,924	117,710
		6,423,079	5,860,734
<b>NON-CURRENT LIABILITIES</b>			
Borrowings - due after one year	16	1,384,155	1,959,867
Deferred income		114,311	113,949
Other financial liabilities	12	219,173	76,148
		1,717,639	2,149,964
		8,140,718	8,010,698



# Condensed Consolidated Statement of Changes in Equity

For the six months ended 30 June 2014

	Attributable to owners of the Company							
	Share capital RMB'000	Share premium RMB'000	Other reserve RMB'000 (Note)	Share options reserve RMB'000	Retained earnings RMB'000	Total RMB'000	Non-controlling interests RMB'000	Total RMB'000
Balance at 1 January 2013 (Unaudited)	413,075	2,390,483	1,585,752	9,298	838,377	5,236,985	91,766	5,328,751
Profit and total comprehensive income for the period	—	—	—	—	153,563	153,563	10,174	163,737
Recognition of equity-settled share-based payment (Note 18(a))	—	—	—	3,424	—	3,424	—	3,424
Exercise of share options (Note 18(c))	1,489	13,247	—	(1,924)	—	12,812	—	12,812
Balance at 30 June 2013 (Audited)	414,564	2,403,730	1,585,752	10,798	991,940	5,406,784	101,940	5,508,724
Balance at 1 January 2014 (Audited)	415,261	2,409,936	1,585,752	12,648	1,319,427	5,743,024	117,710	5,860,734
Profit and total comprehensive income for the period	—	—	—	—	523,163	523,163	22,214	545,377
Recognition of equity-settled share-based payment (note 18 (a) (b))	—	—	—	16,968	—	16,968	—	16,968
Balance at 30 June 2014 (Unaudited)	415,261	2,409,936	1,585,752	29,616	1,842,590	6,283,155	139,924	6,423,079

Note: Other reserve balance represented the contribution from the owners for the operation of the Group.

# Condensed Consolidated Statement of Cash Flows

For the six months ended 30 June 2014

	Six months ended 30 June	
	2014 RMB'000 (Unaudited)	2013 RMB'000 (Unaudited)
Net cash generated from operating activities	1,037,102	368,203
Net cash used in investing activities		
Purchases of property, plant and equipment	(375,837)	(417,344)
Addition in biological assets	(551,168)	(611,075)
Addition in pledged bank balances	(302,843)	(442,747)
Release of pledged bank balances	176,231	193,435
Proceeds on disposal of dairy cows	141,854	128,572
Investment in joint ventures	(55,375)	—
Other investing cash flows	12,539	12,801
	(954,599)	(1,136,358)
Net cash generated from financing activities		
Interest paid	(166,318)	(112,110)
New bank borrowings raised	1,874,341	1,155,985
Repayment of bank borrowings	(1,597,730)	(884,352)
Proceeds from issue of short-term debenture	1,100,000	700,000
Repayment of short-term debenture	(1,200,000)	—
Other financing cash flows	(4,000)	10,012
	6,293	869,535
Net increase in cash and cash equivalents	88,796	101,380
Cash and cash equivalents at 1 January	369,041	276,650
Cash and cash equivalents at 30 June, represented by bank balances and cash	457,837	378,030

# Notes to the Condensed Consolidated Financial Statements

For the six months ended 30 June 2014

## 1. GENERAL INFORMATION

China Modern Dairy Holdings Ltd. (the “Company”) is a public limited liability company and its shares are listed on the Main Board of The Stock Exchange of Hong Kong Limited (the “Stock Exchange”) since 26 November 2010. The registered office of the Company is Maples Corporate Services Limited, PO Box 309, Ugland House, Grand Cayman, KYI-1104, Cayman Islands and its principal place of business is located in Economic and Technological Development Zone, Maanshan City, Anhui Province, the People’s Republic of China (the “PRC”).

The principal activity of the Company is investment holding and its subsidiaries are mainly engaged in production and sales of milk and breeding and sales of dairy cow. The Company and its subsidiaries are hereinafter collectively referred to as the “Group”. The condensed consolidated financial statements are presented in Renminbi (“RMB”), the currency of the primary economic environment in which the principal subsidiaries of the Group operate (the “functional currency”).

## 2. BASIS OF PREPARATION

In preparing the condensed consolidated financial statements for the six months ended 30 June 2014, the directors of the Company have given careful consideration to the future liquidity of the Group in light of its net current liabilities of approximately RMB2,863,725,000 as at 30 June 2014 (31 December 2013: net current liabilities of RMB2,446,062,000). Having considered the credit facilities of approximately RMB7,565,266,000 which remains unutilised as at 30 June 2014, the directors of the Company are satisfied that the Group will be able to meet in full its financial obligations as they fall due for the foreseeable future. Accordingly, the condensed consolidated financial statements have been prepared on a going concern basis.

In preparation of the interim condensed consolidated statement of profit or loss and other comprehensive income for the six months ended 30 June 2014, management of the Company has changed the analysis and presentation of expenses recognised in profit or loss from using the classification by nature to using the classification by function. Comparative information for the six months ended 30 June 2013 has been presented on the same basis.

The condensed consolidated financial statements of the Group have been prepared in accordance with the applicable disclosure requirements of Appendix 16 to the Rules Governing the Listing of Securities on the Stock Exchange and with International Accounting Standard 34 “Interim Financial Reporting”.

## 3. PRINCIPAL ACCOUNTING POLICIES

The condensed consolidated financial statements have been prepared on the historical cost basis except for: (i) the biological assets, which are measured at fair value less costs to sell; and (ii) other financial assets and other financial liabilities (derivative financial instruments), which are measured at fair value. Except as described below, the accounting policies and methods of computation used in the condensed consolidated financial statements for the six months ended 30 June 2014 are consistent with those followed in the preparation of the Group’s consolidated financial statements for the year ended 31 December 2013.

In the current interim period, the Group has applied, for the first time, a new Interpretation and certain amendments to International Financial Reporting Standards (“IFRSs”) issued by International Accounting Standards Board (“IASB”) that are mandatorily effective for the current interim period.

The application of the above new Interpretation and amendment to IFRSs in the current interim period has had no material effect on the amounts reported in the condensed consolidated financial statements and/or disclosures set out in the condensed consolidated financial statements.

#### **4. SEGMENT INFORMATION**

The Group manages its business by lines of products. In a manner consistent with the way in which information is reported internally to the Group's most senior executive management, being the chief operating decision maker (the "CODM") of the Group, for the purposes of resource allocation and performance assessment. The Group has presented the following two reportable segments, which are Dairy Farming and Liquid Milk Products. Each reportable segment is a separate business unit which offers different products, and is managed separately because they require different technology and marketing strategies. The financial information of the different segments is regularly reviewed by the Group's CODM to make decisions about resources to be allocated to each segment and assess its performance.

- Dairy farming: breeding dairy cows to produce and distribute raw milk and selling self-breeding dairy cows;
- Liquid milk products: producing and distributing processed liquid milk.

Sales of milk produced of RMB 1,623,312,000 is from a single external customer (six months ended 30 June 2013: RMB1,014,847,000) for the six months ended 30 June 2014.

##### **Segment revenue, results, assets and liabilities**

For the purposes of assessing segment performance and allocating resources between segments, the Group's CODM monitors the results, assets and liabilities attributable to each reportable segment on the following bases:

Segment assets include all assets with the exception of goodwill, other financial assets and other headoffice or corporate assets. Segment liabilities include all current and non-current liabilities with the exception of other financial liability and other headoffice or corporate liabilities.

Revenue and expenses are allocated to the reportable segments with reference to sales generated by those segments and the expenses incurred by those segments.

Unallocated expense consists of selling and distribution expenses, administrative expenses of headoffice and other non-operating segment.

## Notes to the Condensed Consolidated Financial Statements

For the six months ended 30 June 2014

### 4. SEGMENT INFORMATION *(continued)*

#### Segment revenue, results, assets and liabilities *(continued)*

The following is an analysis of the Group's revenue and results by reportable segment:

	Dairy farming RMB'000	Liquid milk products RMB'000	Total RMB'000
<b>For the six months ended 30 June 2014 (unaudited)</b>			
Segment revenue from sales of			
– Milk produced	2,420,321	284,639	2,704,960
– Dairy cows	49,321	—	49,321
Less: Inter-segment revenue	(169,746)	—	(169,746)
Net external revenue	2,299,896	284,639	2,584,535
Segment cost of sales of			
– Milk produced	1,478,523	216,478	1,695,001
– Dairy cows	49,321	—	49,321
Less: Inter-segment cost of sales	(165,137)	—	(165,137)
Net external cost of sales	1,362,707	216,478	1,579,185
Reportable segment profit	722,117	47,079	769,196
Loss arising from changes in fair value less costs to sell of dairy cows			(84,559)
Unallocated share of profit of an associate			2,796
Unallocated share of profit of joint ventures			1,943
Unallocated other income			2,684
Unallocated other gains and losses			(84,952)
Unallocated expense			(55,133)
Profit before tax			551,975
<b>As at 30 June 2014 (unaudited)</b>			
Segment assets	11,405,998	620,055	12,026,053
Elimination of inter-segment receivables			(344,158)
Unallocated assets			1,497,194
Consolidated assets			13,179,089
Segment liabilities	6,425,635	479,581	6,905,216
Elimination of inter-segment payables			(344,158)
Unallocated liabilities			194,952
Consolidated liabilities			6,756,010

**4. SEGMENT INFORMATION** *(continued)***Segment revenue, results, assets and liabilities** *(continued)*

	Dairy farming RMB'000	Liquid milk products RMB'000	Total RMB'000
<b>For the six months ended 30 June 2013 (unaudited)</b>			
Segment revenue from sales of			
– Milk produced	1,318,340	117,002	1,435,342
Less: Inter-segment revenue	(47,309)	—	(47,309)
Net external revenue	1,271,031	117,002	1,388,033
Segment cost of sales of			
– Milk produced	983,984	87,005	1,070,989
Less: Inter-segment cost of sales	(47,309)	—	(47,309)
Net external cost of sales	936,675	87,005	1,023,680
Reportable segment profit	223,801	25,324	249,125
Loss arising from changes in fair value less costs to sell of dairy cows			(66,343)
Unallocated share of profit of an associate			847
Unallocated other income			7,637
Unallocated expense			(22,833)
Profit before tax			168,433
<b>As at 31 December 2013 (audited)</b>			
Segment assets	11,085,279	446,997	11,532,276
Elimination of inter-segment receivables			(216,470)
Unallocated assets			1,178,015
Consolidated assets			12,493,821
Segment liabilities	6,433,677	347,004	6,780,681
Elimination of inter-segment payables			(216,470)
Unallocated liabilities			68,876
Consolidated liabilities			6,633,087

## Notes to the Condensed Consolidated Financial Statements

For the six months ended 30 June 2014

### 4. SEGMENT INFORMATION *(continued)*

#### Geographic information

Since all the revenue from external customers is derived from the customers located in mainland China and all the non-current assets are obtained and located in mainland China while all the segments are managed on a nationwide basis because of the similarity of the type or class of the customers and the similarity of the regulatory environment in the whole region, there is no information separated by different geographical locations within mainland China provided to the Group's management.

### 5. OTHER INCOME

	Six months ended 30 June	
	2014 RMB'000 (Unaudited)	2013 RMB'000 (Unaudited)
Government grants related to		
– Other assets	5,689	4,744
– Income (Note i)	656	7,193
– Biological assets (Note ii)	—	32,489
Bank interest income	11,317	6,416
Others	2,263	2,761
	<b>19,925</b>	<b>53,603</b>

Notes:

- i. These government grants are unconditional government subsidies received by the Group from relevant government bodies for the purpose of giving financial support to the Group's operation.
- ii. These government grants are unconditional government subsidies received by the Group from relevant government bodies for the purpose of supporting the Group to purchase dairy cows.

**6. PROFIT BEFORE FINANCE COSTS AND TAX**

Profit before finance costs and tax is arrived at after charging (crediting):

	Six months ended 30 June	
	2014 RMB'000 (Unaudited)	2013 RMB'000 (Unaudited)
Cost of sales:		
Planation and breeding costs to produce raw milk	1,313,386	936,675
Production costs for liquid milk products	216,478	87,005
Costs of sales of dairy cows*	49,321	—
	<b>1,579,185</b>	<b>1,023,680</b>
Other gains and losses:		
Gain arising on financial assets designated at fair value through profit or loss (FVTPL)	(58,305)	—
Loss arising on financial liabilities designated at FVTPL	143,025	—
	<b>84,720</b>	<b>—</b>
Net foreign exchange loss (gain)	12,009	(4,801)
Loss on disposal of property, plant and equipment, net	2,912	1,179
	<b>99,641</b>	<b>(3,622)</b>
Depreciation of property, plant and equipment	107,632	77,380
Employee benefits expenses	149,804	93,142
Auditor's remuneration	600	2,021
Release of land use rights	766	825

\* Among the cost of sales of dairy cows, the feeding cost of dairy cows is RMB34,114,000.



## Notes to the Condensed Consolidated Financial Statements

For the six months ended 30 June 2014

### 7. FINANCE COSTS

	Six months ended 30 June	
	2014	2013
	RMB'000	RMB'000
	(Unaudited)	(Unaudited)
Interest expenses on:		
Bank borrowings wholly repayable within five years	119,529	106,316
Bank borrowings wholly repayable after five years	—	2,392
Short-term debenture repayable within five years	30,366	9,121
Total borrowing cost	149,895	117,829
Less: capitalised amount for construction of property, plant and equipment	(15,003)	(22,951)
	134,892	94,878

The borrowing costs was capitalised based on the terms of the specific bank borrowings in respect of construction in progress.

### 8. INCOME TAX CHARGE

	Six months ended 30 June	
	2014	2013
	RMB'000	RMB'000
	(Unaudited)	(Unaudited)
The charge comprises:		
Current tax:		
PRC enterprise income tax	6,598	4,696

The tax charge for the period under review represents income tax in the PRC which is calculated at the prevailing tax rate on the taxable income of the subsidiaries established in the PRC.

According to the prevailing tax rules and regulation in the PRC, certain entities of the Group operating in agricultural business are exempted from enterprise income tax.

As at 30 June 2014, no liability has been recognised in respect of these differences because the Group is in a position to control the timing of the reversal of the temporary differences and it is probable that such differences will not be reversed in the foreseeable future. The aggregate amount of temporary differences associated with undistributed earnings of PRC subsidiaries for which deferred tax liabilities have not been recognised was approximately RMB2,196,440,000 (31 December 2013: RMB1,609,717,000) as at 30 June 2014.

### 9. DIVIDEND

No dividends were paid, declared or proposed during the current reporting period (six months ended 30 June 2013: Nil)  
The Directors do not recommend the payment of an interim dividend for the six months ended 30 June 2014.

## 10. EARNINGS PER SHARE

The calculation of the basic and diluted earnings per share attributable to owners of the Company is based on the following data:

	Six months ended 30 June	
	2014 RMB'000 (Unaudited)	2013 RMB'000 (Unaudited)
<b>Earnings</b>		
Earnings for the purpose of basic earnings per share (profit for the period attributable to owners of the Company)	523,163	153,563

	Six months ended 30 June	
	2014 (Unaudited)	2013 (Unaudited)
<b>Number of shares</b>		
Weighted average number of ordinary shares for the purpose of basic and diluted earnings per share	4,827,338,751	4,808,746,000
Effect of dilutive potential ordinary shares option	51,903,704	51,758,234
Weighted average number of ordinary shares for the purpose of diluted earnings per share	4,879,242,455	4,860,504,234

## 11. PROPERTY, PLANT AND EQUIPMENT

During the six months ended 30 June 2014, the Group acquired property, plant and equipment amounted to RMB268,308,000 (six months ended 30 June 2013: RMB338,271,000) in order to increase its production capacity.

## 12. OTHER FINANCIAL ASSETS AND LIABILITIES

	30 June 2014 RMB'000 (Unaudited)	31 December 2013 RMB'000 (Audited)
	Financial assets carried at FVTPL	
Derivative financial instruments	92,822	34,517
Financial liabilities carried at FVTPL		
Derivative financial instruments	219,173	76,148

## 12. OTHER FINANCIAL ASSETS AND LIABILITIES *(continued)*

Financial assets carried at FVTPL represent fair value of the Call Option (as defined below) granted to the Company at the reporting date. Financial liabilities carried at FVTPL represent fair value of the Put Option (as defined below) granted by the Company to a joint venture investor at the reporting date. The fair value of the Call Option and the Put Option was independently valued by Jones Lang LaSalle Corporate Appraisal And Advisory Limited (the "JLL"), a firm of independent qualified professional valuers.

On 23 September 2013, the Company entered into two agreements (the "JV Agreement I" and "JV Agreement II") with Success Dairy II Limited ("Success Dairy"), a third party investor, to incorporate Asia Dairy Holdings (the "JV Company I") and Asia Dairy Holdings II (the "JV Company II"). JV Company I and JV Company II respectively owns a PRC subsidiary, Modern Farm Shanghe Ltd. ("現代牧業(商河)有限公司") and Modern Farm Jinan Ltd. ("現代牧業(濟南)有限公司"). The principal activities of JV Company I, JV Company II and their subsidiaries include to design, construct and operate a dairy farm ("Dairy Farm") in the PRC for the purpose of, amongst others, breeding, raising and sale of dairy cattle, production, processing and sale of raw milk, production of processed milk under OEM contracts for other processors and the sale of fertilizers. The Company owns as to 18% equity interests and Success Dairy owns as to the remaining 82% equity interests in the JV Company I and JV Company II, respectively.

Pursuant to Joint Venture Agreement I and Joint Venture Agreement II, the Company has granted a put option (the "Put Option") to Success Dairy, exercisable at any time between the third year to the seventh year after the first day on which the Dairy Farm produces milk for sales ("Commencement of Operation"). Success Dairy is entitled to require the Company to purchase back up to all of its equity interests in the JV Company I and JV Company II and all loans or borrowings owed by the JV Company I and JV Company II to Success Dairy at the put option exercise price determined in accordance with the Joint Venture Agreement I and Joint Venture Agreement II, respectively.

Pursuant to Joint Venture Agreement I and Joint Venture Agreement II, Success Dairy has granted the Company a call option (the "Call Option"), exercisable at any time between the third to the seventh year after the Commencement of Operation. The Company is entitled to require Success Dairy to sell up to all of its equity interests in the JV Company I and the JV Company II and all loans or borrowings owed by the JV Company I and the JV Company II to Success Dairy at the call option exercise price determined in accordance with the Joint Venture Agreement I and Joint Venture Agreement II, respectively.

**12. OTHER FINANCIAL ASSETS AND LIABILITIES** (continued)

The fair values of the Put Option and Call Option as at 30 June 2014 have been determined by using a Binominal Option Pricing Model with the following assumptions:

	JV Agreement I US\$'000	JV Agreement II US\$'000
Price of investing capital	41,000	24,600
Exercise price	43,184	25,911
Expected volatility	39.66%	43.85%
Risk-free interest rate	1.09%	1.50%
Dividend yield	—	—
Return Rate	7.00%	7.00%

For the fair value measurements of the Group's Put Option and Call Option, any change in the significant unobservable inputs might result in a significantly higher or lower fair value measurement.

**13. BIOLOGICAL ASSETS**

The Group's dairy cows were fair valued by the directors of the Company at 30 June 2014 while the fair value of the Group's dairy cows at 31 December 2013 has been arrived at on the basis of a valuation carried out by independent qualified professional valuer. As at 30 June 2014 the fair value less costs to sell of heifers and calves are determined with reference to the market-determined prices of items with similar age, breed and genetic merit, if the market-determined prices are available. Due to the fact that the market-determined prices for milkable cows are not available, the directors of the company have applied net present value approach to calculate the fair value less cost to sell of these items. The resulting loss arising from changes in fair value less costs to sell of dairy cows of RMB84,559,000 (six months ended 30 June 2013: loss of RMB66,343,000) has been recognised directly in profit or loss for the six months ended 30 June 2014.

The principal valuation assumptions affecting the estimation of the fair value of dairy cows by applying the net present value approach are the same as those set out in note 23 of Group's consolidated financial statements for the year ended 31 December 2013.

For the fair value measurements of the Group's calves, heifers and milkable cows, any change in the significant unobservable inputs might result in a significantly higher or lower fair value measurement.

## Notes to the Condensed Consolidated Financial Statements

For the six months ended 30 June 2014

### 14. TRADE AND OTHER RECEIVABLES

The Group allows credit period of 60 to 120 days to its trade customers.

The following is an analysis of trade receivables at the end of respective reporting periods:

	30 June 2014 RMB'000 (Unaudited)	31 December 2013 RMB'000 (Audited)
Trade receivables		
– within 120 days based on invoice date	512,788	462,775
Advances to suppliers	62,511	69,464
Others	24,410	12,471
	<b>599,709</b>	<b>544,710</b>

### 15. TRADE AND OTHER PAYABLES

The credit period taken for the settlement of trade purchases is 60 days. The following is an aged analysis of trade and bills payables at the end of the reporting period:

	30 June 2014 RMB'000 (Unaudited)	31 December 2013 RMB'000 (Audited)
Trade and bills payables		
Within 60 days based on invoice date	588,880	682,985
Over 60 days based on invoice date	51,297	42,379
	<b>640,177</b>	<b>725,364</b>
Payable for acquisition of property, plant and equipment	356,786	479,318
Accrued staff costs	52,301	45,321
Advance payment from customers	41,504	55,949
Interest payable	17,980	35,447
Others	52,481	45,031
	<b>521,052</b>	<b>661,066</b>
	<b>1,161,229</b>	<b>1,386,430</b>

## 16. BORROWINGS

During the current period, the Group obtained new bank borrowings amounting to RMB1,874,341,000 (six months ended 30 June 2013 RMB1,155,985,000) and repaid RMB1,597,730,000 (six months ended 30 June 2013: RMB884,352,000).

The annual interest rate of the bank borrowings during the period ranged from 1.73 % to 7.05% (six months ended 30 June 2013: 1.78% to 7.05%). As at 30 June 2014, the Group's interest-bearing bank borrowings were denominated in RMB and United States Dollar ("US\$").

## 17. SHORT-TERM DEBENTURE

	30 June 2014 RMB'000 (Unaudited)	31 December 2013 RMB'000 (Audited)
Short term debenture - unsecured (Notes)	1,100,000	1,200,000

Notes:

- i. On 27 March 2013, the Company issued short-term debenture with a principal amount of RMB700,000,000 through China Merchants Bank Co., Ltd., the leading underwriter, with maturity of one year. The short term debenture bears a fixed interest rate of 4.99% per annum and its effective interest rate is 5.41% per annum after considering the effect of issue costs and has been repaid on 28 March 2014.
- ii. On 6 December 2013, the Company issued short-term debenture with a principal amount of RMB500,000,000 through China Construction Bank Co., Ltd., the leading underwriter, with maturity of six months. The short term debenture bears a fixed interest rate of 6.90% per annum and has been repaid on 28 April 2014.
- iii. On 24 April 2014, the Company issued short-term debenture with a principal amount of RMB700,000,000 through China Merchants Bank Co., Ltd., the leading underwriter, with maturity of one year. The short term debenture bears a fixed interest rate of 6.00% per annum and its effective interest rate is 6.43% per annum after considering the effect of issue costs.
- iv. On 21 May 2014, the Company issued short-term debenture with a principal amount of RMB400,000,000 through CITIC Securities Co., Ltd., the leading underwriter, with maturity of one year. The short term debenture bears a fixed interest rate of 6.00% per annum and its effective interest rate is 6.32% per annum after considering the effect of issue costs.

## 18. SHARE-BASED PAYMENT TRANSACTIONS

### (a) The Company's Share Option Scheme I

The Company's Share Option Scheme I was adopted pursuant to a resolution passed on 17 November 2011 for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. The maximum number of shares that may be granted under the Share Option Scheme I and other share option schemes shall not exceed 20% of the number of issued shares of the Company from time to time. Unless approved by the shareholders of the Company in general meeting in the manner prescribed in the Rules Governing the Listing of Securities on the Stock Exchange, the board of directors of the Company (the "Board") shall not grant options to any grantee if the acceptance of those options would result in the total number of shares issued and to be issued to that grantee on exercise of his options during any 12-month period exceeding 1% of the total shares of the Company (or its subsidiary) then in issue.

On 12 December 2012, the Company announced that a total of 40,000,000 share options (the "Scheme I Share Options") to subscribe for shares of HK\$0.10 each in the capital of the Company (the "Scheme I Shares") were granted by the Company to two directors and 128 eligible employees of the Company (collectively, the "Scheme I Grantees"), subject to acceptance of the Scheme I Grantees, under the Company's Share Option Scheme I adopted by the Company on 17 November 2011.

The Share Options shall entitle the Scheme I Grantees to subscribe for an aggregate of 40,000,000 new shares upon the exercise of the Scheme I Share Options in full at an exercise price of HK\$2.89 per share. Out of the aggregate of 40,000,000 Scheme I Share Options, 3,000,000 and 2,000,000 Scheme I Share Options were granted to Ms. GAO Lina and Mr. HAN Chunlin, directors of the Company, respectively. 2,000,000 Scheme I Share Options were granted to Mr. SUN Yugang, who was appointed as a director of the Company with effect from 28 June 2013.

Pursuant to the rules of the Share Option Scheme I, the Scheme I Share Options granted to each of the Scheme I Grantees (the "Scheme I Granted Options") are deemed to be divided into three tranches, each of which consists of one third of the Scheme I Granted Options and will be associated with a performance target within a specific financial period (the "Scheme I Performance Target"). The non-market based Scheme I Performance Target has been determined by the Board and specified in the offer letter to each of the Scheme I Grantees. The financial period for the first tranche is the twelve months ended 30 June 2013; the financial period for the second tranche is the twelve months ended 30 June 2014; and the financial period for the third tranche will be the twelve months ending 30 June 2015. Each tranche of the Scheme I Granted Options after meeting the respective Scheme I Target Performance shall vest on a one-off basis within 30 days after the date of publication of the results announcement for the six months ending 30 June 2015. Any of the Scheme I Granted Options not vested as a result of non-fulfillment of the Scheme I Performance Target at the end of the respective specific financial period shall automatically lapse.

**18. SHARE-BASED PAYMENT TRANSACTIONS** (continued)**(a) The Company's Share Option Scheme I** (continued)

Other information of the Scheme I Granted Options is set out below:

Exercise price of the Scheme I Share Options:	HK\$2.89
Closing price of the Shares immediately before the date of grant:	HK\$1.98
Validity period of the Scheme I Share Options:	Five (5) years on the date when the Scheme I Options became vested

The following table discloses movements of the Scheme I Share Options during the reporting period:

Category	Outstanding as at 1 January 2014	Granted during the period	Exercised during the period	Lapsed* during the period	Cancelled** during the period	Outstanding as at 30 June 2014
Share Option A	4,780,267	—	—	—	—	4,780,267
Share Option B	28,847,506	—	—	—	(598,718)	28,248,788
	33,627,773	—	—	—	(598,718)	33,029,055

Category	Outstanding as at 1 January 2013	Granted during the period	Exercised during the period	Lapsed* during the period	Cancelled** during the period	Outstanding as at 30 June 2013
Share Option A	5,000,000	—	—	(219,733)	—	4,780,267
Share Option B	35,000,000	—	—	(503,615)	(3,166,667)	31,329,718
	40,000,000	—	—	(723,348)	(3,166,667)	36,109,985

\* Share Options lapsed due to non-fulfillment of the Scheme I Performance Target during the related period.

\*\* Share Options were cancelled due to the relevant Scheme I Grantees' resignation from the Group.

Out of the aggregate of 40,000,000 Scheme I Share Options, 5,000,000 Scheme I Share Options were granted to two directors of the Company ("Share Option A") and the remaining Share Options were granted to 128 eligible employees ("Share Option B"), respectively. Mr. SUN Yugang awarded under Share Option B was appointed as a director with effect from 28 June 2013.

The fair values of Share Option A and Share Option B determined at the dates of grant using the Binomial Option Pricing Model were HK\$3,322,000 (equivalent to RMB2,696,000) and HK\$21,626,000 (equivalent to RMB17,547,000) respectively.



## 18. SHARE-BASED PAYMENT TRANSACTIONS (continued)

### (a) The Company's Share Option Scheme I (continued)

The following assumptions were used to calculate the fair values of share options:

	Share Options A	Share Options B
Grant date share price	HK\$1.97	HK\$1.97
Exercise price	HK\$2.89	HK\$2.89
Expected volatility	41.79%	41.79%
Option life	Five years	Five years
Dividend yield	—	—
Risk-free interest rate	0.4%	0.4%
Sub-optional factor	2.8	2.2

The Binomial Option Pricing Model has been used to estimate the fair value of the options. The variables and assumptions used in computing the fair value of the Scheme I Share Options are based on the directors' best estimate. Changes in variables and assumptions may result in changes in the fair value of the Scheme I Share Options.

The Company recognised a share option expense of RMB3,584,000 during the current period (six months ended 30 June 2013: RMB3,424,000). None of the Scheme I Share Options was exercisable as at 30 June 2014.

### (b) The Company's Share Option Scheme II

The Company's Share Option scheme II was adopted pursuant to a resolution passed on 5 June 2014 for the purpose of providing incentives and rewards to eligible participants who contribute to the success of the Group's operations. The maximum number of shares that may be granted under the Share Option Scheme II and other share option schemes shall not exceed 20% of the number of issued shares of the Company as at the date of 5 June 2014. Unless approved by the shareholders of the Company in general meeting in the manner prescribed in the Rules Governing the Listing of Securities on the Stock Exchange, the Board shall not grant options to any grantee if the acceptance of those options would result in the total number of shares issued and to be issued to that grantee on exercise of his options during any 12-month period exceeding 1% of the total shares of the Company (or its subsidiary) then in issue.

On 6 June 2014, the Company announced that a total of 80,000,000 share options (the "Scheme II Share Options") to subscribe for Shares were granted by the Company to three directors and 148 eligible employees of the Company (collectively, the "Scheme II Grantees"), subject to acceptance of the Scheme II Grantees, under the Company's Share Option Scheme II adopted by the Company on 5 June 2014.

The Scheme II Share Options shall entitle the Scheme II Grantees to subscribe for an aggregate of 80,000,000 new shares upon the exercise of the Scheme II Share Options in full at an exercise price of HK\$3.38 per Share. Out of the aggregate of 80,000,000 Scheme II Share Options, 7,000,000, 5,000,000 and 5,000,000 Scheme II Share Options were granted to Ms. GAO Lina Mr. HAN Chunlin and Mr. SUN Yugang, directors of the Company, respectively.

**18. SHARE-BASED PAYMENT TRANSACTIONS** *(continued)***(b) The Company's Share Option Scheme II** *(continued)*

Pursuant to the rules of the Share Option Scheme II, the Scheme II Share Options granted to each of the Scheme II Grantees (the "Scheme II Granted Options") are deemed to be divided into three tranches, each of which consists of one third of the Scheme II Granted Options and will be associated with a performance target within a specific financial period (the "Scheme II Performance Target"). The non-market based Scheme II Performance Target has been determined by the Board and specified in the offer letter to each of the Scheme II Grantees. The financial period for the first tranche is the financial year ending 31 December 2014; the financial period for the second tranche will be the financial year ending 31 December 2015; and the financial period for the third tranche will be the financial year ending 31 December 2016. Each tranche of the Scheme II Granted Options after meeting the respective Scheme II Target Performance shall vest on a one-off basis within 30 days after the date of publication of the results announcement for the financial year ending 31 December 2016. Any of the Scheme II Granted Options not vested as a result of non-fulfillment of the Scheme II Performance Target at the end of the respective specific financial period shall automatically lapse.

Other information of the Scheme II Granted Options is set out below:

Exercise price of the Scheme II Share Options:	HK\$3.38
Closing price of the Shares	
immediately before the date of grant:	HK\$3.38
	Five (5) years on the date when the Scheme II Options
Validity period of the Scheme II Share Options:	became vested

The following table discloses movements of the Scheme II Share Options during the reporting period:

Category	Outstanding					Outstanding as at 30 June 2014
	as at 1 January 2014	Granted during the period	Exercised during the period	Lapsed during the period	Cancelled during the period	
Share Option C	—	17,000,000	—	—	—	17,000,000
Share Option D	—	63,000,000	—	—	—	63,000,000
	—	80,000,000	—	—	—	80,000,000

Out of the aggregate of 80,000,000 Scheme II Share Options, 17,000,000 Scheme II Share Options were granted to three directors of the Company ("Share Option C") and the remaining Scheme II Share Options were granted to 148 eligible employees ("Share Option D"), respectively.

The fair values of Share Option C and Share Option D determined at the dates of grant using the Binomial Option Pricing Model were HK\$25,827,000 (equivalent to RMB20,530,000) and HK\$83,969,000 (equivalent to RMB66,747,000) respectively.

## 18. SHARE-BASED PAYMENT TRANSACTIONS (continued)

### (b) The Company's Share Option Scheme II (continued)

The following assumptions were used to calculate the fair values of share options:

	Share Options C	Share Options D
Grant date share price	HK\$3.38	HK\$3.38
Exercise price	HK\$3.38	HK\$3.38
Expected volatility	43.55%	43.55%
Option life	Five years	Five years
Dividend yield	—	—
Risk-free interest rate	1.75%	1.75%
Sub-optional factor	2.2	1.6

The Binomial Model option pricing model has been used to estimate the fair value of the options. The variables and assumptions used in computing the fair value of the Scheme II Share Options are based on the directors' best estimate. Changes in variables and assumptions may result in changes in the fair value of the Scheme II Share Options.

The Company recognised a share option expense of RMB13,384,000 during the current period (six months ended 30 June 2013: nil). None of the Scheme II Share Options was exercisable as at 30 June 2014.

### (c) Modern Farm Option Scheme

The option scheme of Modern Farming Group Co., Ltd. ("Modern Farm") (the "Modern Farm Scheme") was adopted pursuant to agreement dated 9 June 2009 for the primary purpose of providing incentives to directors and eligible employees of Modern Farm and its subsidiaries, and will expire on 8 June 2019. Under the Modern Farm Scheme, Modern Farm granted options to two directors and one top management of Modern Farm (the "MF Grantees") to subscribe for a total of RMB10,821,069 paid-in capital (the "MF Options") and each MF option has an exercise price of RMB5.9883 per RMB1 paid-in capital on 17 June 2009.

At 30 June 2010, the amount of paid-in capital in respect of which MF Grantees can subscribe for and remained outstanding under the Modern Farm Scheme was RMB10,821,069, representing 2.09% of the paid-in capital of Modern Farm at that date.

On 31 October 2010, the Company granted to the MF Grantees a total of 87,412,507 share options of the Company for nil consideration and each with an exercise price of HK\$0.86 (HK\$1 = RMB0.74) per share (the "Management Options") to replace the MF Options which lapsed and ceased to have effect at the same time. The Company's management considers that the Management Options granted is a replacement of the MF Options granted and the incremental fair value caused by the replacement of the MF Options with the Management Options is insignificant. The following table discloses movements of the Management Options during the current period:

Category	Outstanding as at 1 January 2014	Granted during the period	Exercised during the period	Lapsed during the period	Cancelled during the period	Outstanding as at 30 June 2014
Management Options	60,073,756	—	—	—	—	60,073,756

**18. SHARE-BASED PAYMENT TRANSACTIONS** (continued)**(c) Modern Farm Option Scheme** (continued)

Category	Outstanding as at 1 January 2013	Granted during the period	Exercised* during the period	Lapsed during the period	Cancelled during the period	Outstanding as at 30 June 2013
Management Options	87,412,507	—	(18,535,733)	—	—	68,876,774

\* 18,535,733 share options of the Management Options were exercised during the six months ended 30 June 2013. Share options reserve of RMB1,924,000 in relation to the 18,535,733 share options was reclassified to share premium as a result of the exercise.

**19. OPERATING LEASE COMMITMENTS****The Group as lessee**

At the end of each reporting period, the Group was committed to make future minimum lease payments in respect of plant and vehicles rented under non-cancellable operating leases which fall due as follows:

	30 June 2014 RMB'000 (Unaudited)	31 December 2013 RMB'000 (Audited)
Within one year	718	579
In the second to fifth year inclusive	365	364
Over five years	697	748
	<b>1,780</b>	<b>1,691</b>

**20. CAPITAL COMMITMENTS**

	30 June 2014 RMB'000 (Unaudited)	31 December 2013 RMB'000 (Audited)
Capital expenditure contracted but not provided for, in respect of acquisition of property, plant and equipment	175,144	78,527
in respect of acquisition of biological assets	57,864	—
in respect of capital contribution to joint ventures	66,450	120,719
	<b>299,458</b>	<b>199,246</b>

## 21. RELATED PARTY TRANSACTIONS

### a. Name and relationship with related parties are as follows:

Name	Relationship
Qishi Grass Co., Ltd (“Qishi”)	An associate of the Group
Modern Farm (Shanghe) Co., Ltd	A subsidiary of a joint venture
China Mengniu Dairy Co., Ltd (“Mengniu Company”)*	A shareholder with significant influence over the Company
Inner Mongolia Mengniu Dairy (Group) Company Limited **	A subsidiary of Mengniu Company
Inner Mongolia Mengniu Dairy Keerqin Co., Ltd. **	A subsidiary of Mengniu Company
Mengniu Dairy Taian Co., Ltd. **	A subsidiary of Mengniu Company
Mengniu Dairy (Maanshan) Co., Ltd. **	A subsidiary of Mengniu Company
Hubei Frealth Dairy Co., Ltd. **	A subsidiary of Mengniu Company
Mengniu Dairy (Shangzhi) Co., Ltd. **	A subsidiary of Mengniu Company
Mengniu Dairy (Chabei) Co., Ltd. **	A subsidiary of Mengniu Company
Mengniu Dairy (Baoji) Co., Ltd. **	A subsidiary of Mengniu Company
Mengniu Dairy Meishan Co., Ltd. **	A subsidiary of Mengniu Company
Mengniu Saibei Dairy Co., Ltd. **	A subsidiary of Mengniu Company
Mengniu Dairy (Suqian) Co., Ltd. **	A subsidiary of Mengniu Company
Inner Mongolia Mengniu Hi-tech Dairy Co., Ltd. **	A subsidiary of Mengniu Company
Shijiazhuang Junlebao Dairy Co., Ltd. **	A subsidiary of Mengniu Company

\* Mengniu Company became a substantial shareholder of the Company and was able to exercise significant influence over the Group from 22 May 2013. Mengniu Company is principally engaged in milk processing industry in the PRC and listed on the Main Board of the Stock Exchange. The related party transaction disclosures with Mengniu Group (defined as below) only take into account transactions with Mengniu Group since 22 May 2013.

\*\* These entities are subsidiaries of Mengniu Company (collectively referred to as the “Mengniu Group”).

**21. RELATED PARTY TRANSACTIONS** (continued)

- b. At the end of the reporting period, the Group had the following balances with related parties:

**Amount due from**

	30 June 2014 RMB'000 (Unaudited)	31 December 2013 RMB'000 (Audited)
<b>Mengniu Group</b>		
Trade receivable		
Within 120 days based on invoice date	211,760	215,356
<b>Modern Farm (Shanghe) Co., Ltd</b>		
Other receivable	10,961	—

**Amount due to**

	30 June 2014 RMB'000 (Unaudited)	31 December 2013 RMB'000 (Audited)
<b>Qiushi</b>		
Trade payable		
Within 60 days based on invoice date	94,291	37,820
Over 60 days based on invoice date	20,500	50,000
	114,791	87,820
<b>Mengniu Group</b>		
Advance from customer	34,721	46,101

## 21. RELATED PARTY TRANSACTIONS *(continued)*

- b. At the end of the reporting period, the Group had the following balances with related parties: *(continued)***

During the current period, the Group entered into the following transactions with related parties:

	Six months ended 30 June	
	2014 RMB'000 (Unaudited)	2013 RMB'000 (Unaudited)
Sales of raw milk to the Mengniu Group	1,623,312	237,479
Processing liquid milk products for the Mengniu Group	—	1,169
	<b>1,623,312</b>	<b>238,648</b>
Sales of dairy cows to Modern Farm (Shanghe) Co., Ltd	49,321	—
Purchase of raw material from Qiushi	135,537	98,345

- c. Remuneration of key managements personnel**

The remuneration of directors of the Company and other members of key management during the period were as follows:

	Six months ended 30 June	
	2014 RMB'000 (Unaudited)	2013 RMB'000 (Unaudited)
Salaries and other benefits	3,707	2,891
Recognition of equity-settled share-based payment	4,970	852
Retirement benefits scheme contributions	81	132
	<b>8,758</b>	<b>3,875</b>

## 22. FAIR VALUE MEASUREMENTS

Fair value of the Group's assets and liabilities that are measured at fair value on a recurring basis

The Group's biological assets, other financial assets and other financial liabilities are measured at fair value at the end of each reporting period. The following table gives information about how the fair values of these financial assets and financial liabilities are determined (in particular, the valuation technique(s) and inputs used), as well as the level of the fair value hierarchy into which the fair value measurements are categorized (levels 1 to 3) based on the degree to which the inputs to the fair value measurements is observable.

Level 1: fair values measured based on quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: fair values measured based on valuation techniques for which all inputs which have a significant effect on the recorded fair value are observable, either directly or indirectly.

Level 3: fair values measured based on valuation techniques for which any inputs which have a significant effect on the recorded fair value are not based on observable market data. (unobservable inputs)

Fair value of the Group's assets and financial liabilities that are measured at fair value on a recurring basis is set out below:

Assets/(liabilities)	Fair value as at 30 June 2014	Fair value as at 31 December 2013	Fair value hierarchy	Valuation techniques and key inputs
Biological assets	6,297,959	5,954,363	level 3	Refer to note 13
Other financial assets	92,822	34,517	level 3	Refer to note 12
Other financial liabilities	(219,173)	(76,148)	level 3	Refer to note 12

The directors of the Company consider that the carrying amounts of financial statements approximate their fair values.

Reconciliation of Level 3 fair value measurements of derivative financial instruments.

	Call Option RMB'000 (Unaudited)	Put Option RMB'000 (Unaudited)
At 1 January 2014	34,517	(76,148)
Gain (loss) in profit or loss	58,305	(143,025)
At 30 June 2014	92,822	(219,173)

\* There is no Call Option and Put Option for the six months ended 30 June 2013

The gain (loss) for the period in the profit or loss related to derivative financial instruments held at the end of the reporting period. Fair value losses on the derivative financial instruments are presented as "other gain and loss" in condensed consolidated statement of profit or loss and other comprehensive income.



## **22. FAIR VALUE MEASUREMENTS** *(continued)*

### **Fair value measurements and valuation processes**

The management has set up a valuation team, which is headed up by the Chief Financial Officer of the Company, to determine the appropriate valuation techniques and inputs for fair value measurements.

In estimating the fair value of an asset or a liability, the Group uses market-observable data to the extent it is available. Where Level 1 inputs are not available, the Group engages third party qualified valuers or use internal resources to perform the valuation depending on the complexity and significance of the valuation. The valuation team works closely with the qualified external valuers to establish the appropriate valuation techniques and inputs to the model as appropriate. The Chief Financial Officer reports the valuation committee's findings to the board of directors of the Company regularly to explain the cause of fluctuations in the fair value of the assets and liabilities.

Information about the valuation techniques and inputs used in determining the fair value of various assets and liabilities are disclosed above.

## **23. EVENTS AFTER THE REPORTING PERIOD**

There is no material event after the reporting period.