# Lanzhou Zhuangyuan Pasture Co., Ltd.*
# 蘭州莊園牧場股份有限公司

*(a joint stock limited liability company incorporated in the People's Republic of China)*

**(Stock Code: 1533)**

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

**FINANCIAL HIGHLIGHTS**

**Results**

| | Six months ended 30 June | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Revenue | **291,675** | 322,214 |
| Gross profit | **93,096** | 111,578 |
| Profit for the period attributable to equity shareholders of the Company | **37,742** | 37,625 |
| Earnings per share (RMB)[1] | **0.27** | 0.27 |

- Revenue decreased by 9.5% as compared to the corresponding period in 2016.
- Gross profit decreased by 16.6% as compared to the corresponding period in 2016.
- Profit for the period attributable to equity shareholders of the Company increased by 0.3% as compared to the corresponding period in 2016.

(1) The calculation of earnings per share is based on the profit attributable to ordinary equity shareholders of the Company and the weighted average of ordinary shares in issue during the interim periods.

The board (the "**Board**") of directors (the "**Directors**") of Lanzhou Zhuangyuan Pasture Co., Ltd.*蘭州莊園牧場股份有限公司 (the "**Company**") is pleased to present the unaudited consolidated interim results (the "**Interim Results**") of the Company and its subsidiaries (the "**Group**") for the six months ended 30 June 2017 (the "**Reporting Period**"), together with the comparative figures for the corresponding period in 2016.

The Interim Results and the unaudited condensed consolidated interim financial statements have been reviewed by the audit committee of the Company (the "**Audit Committee**") and the external auditor of the Company.

**CONSOLIDATED STATEMENT OF PROFIT OR LOSS**
*for the six months ended 30 June 2017 – unaudited*
*(Expressed in RMB)*

| | | Six months ended 30 June | |
|---|---|---|---|
| | | **2017** | 2016 |
| | *Note* | ***RMB'000*** | *RMB'000* |
| **Revenue** | *3* | **291,675** | 322,214 |
| Cost of sales | | **(198,579)** | (210,636) |
| **Gross profit** | | **93,096** | 111,578 |
| Gain arising on initial recognition of agricultural produce at fair value less costs to sell at the point of harvest | | **7,179** | 4,900 |
| Loss arising from changes in fair value less costs to sell of biological assets | | **(6,894)** | (28,281) |
| Other net income | *4* | **21,086** | 18,509 |
| Distribution costs | | **(33,469)** | (26,247) |
| Administrative expenses | | **(29,906)** | (25,405) |
| **Profit from operations** | | **51,092** | 55,054 |
| Net finance costs | *5(a)* | **(9,835)** | (8,246) |
| **Profit before taxation** | *3, 5* | **41,257** | 46,808 |
| Income tax | *6* | **(3,515)** | (9,183) |
| **Profit for the period** | | **37,742** | 37,625 |
| **Attributable to:** | | | |
| Equity shareholders of the Company | | **37,742** | 37,625 |
| **Earnings per share** | | | |
| – Basic and diluted (RMB) | *7* | **0.27** | 0.27 |

Details of dividends payable to equity shareholders of the Company are set out in note 11 on page 13.

**CONSOLIDATED STATEMENT OF PROFIT OR LOSS AND OTHER COMPREHENSIVE INCOME**
*for the six months ended 30 June 2017 – unaudited*
*(Expressed in RMB)*

| | Six months ended 30 June | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| **Profit for the period** | **37,742** | 37,625 |
| **Total comprehensive income for the period** | **37,742** | 37,625 |
| **Attributable to:** | | |
| Equity shareholders of the Company | **37,742** | 37,625 |
| **Total comprehensive income for the period** | **37,742** | 37,625 |

## CONSOLIDATED STATEMENT OF FINANCIAL POSITION

*at 30 June 2017 – unaudited*
*(Expressed in RMB)*

| | Note | At 30 June 2017 RMB'000 | At 31 December 2016 RMB'000 |
|---|---|---|---|
| **Non-current assets** | | | |
| Property, plant and equipment | | **669,078** | 684,354 |
| Available-for-sale financial assets | | **33,720** | 33,720 |
| Lease prepayments | | **18,450** | 18,832 |
| Biological assets | *8* | **128,515** | 126,289 |
| Deferred tax assets | | **3,955** | 4,108 |
| Other non-current assets | | **81,456** | 90,743 |
| | | **935,174** | 958,046 |
| **Current assets** | | | |
| Inventories | | **54,567** | 75,056 |
| Trade receivables | *9* | **23,324** | 14,036 |
| Deposits, prepayments and other receivables | | **15,123** | 17,097 |
| Pledged deposit | | **14,248** | 4,000 |
| Cash and cash equivalents | | **394,359** | 273,352 |
| | | **501,621** | 383,541 |
| **Current liabilities** | | | |
| Trade and bills payables | *10* | **102,955** | 84,168 |
| Receipts in advance | | **4,108** | 20,290 |
| Accrued expenses and other payables | | **57,075** | 54,552 |
| Non-current liabilities due within one year | | **5,064** | 6,151 |
| Bank loans | | **399,563** | 307,000 |
| Current taxation | | **7,461** | 15,133 |
| | | **576,226** | 487,294 |
| **Net current liabilities** | | **(74,605)** | (103,753) |
| **Total assets less current liabilities** | | **860,569** | 854,293 |

| | At 30 June 2017 *RMB'000* | At 31 December 2016 *RMB'000* |
|---|---|---|
| **Non-current liabilities** | | |
| Bank loans | **29,634** | 44,500 |
| Deferred income | **41,009** | 46,256 |
| Obligations under finance leases | **2,375** | 3,303 |
| | **73,018** | 94,059 |
| **NET ASSETS** | **787,551** | 760,234 |
| **CAPITAL AND RESERVES** | | |
| Share capital | **140,500** | 140,500 |
| Reserves | **647,051** | 619,734 |
| **Total equity attributable to equity shareholders of the Company** | **787,551** | 760,234 |
| **TOTAL EQUITY** | **787,551** | 760,234 |

## NOTES:

*(Expressed in RMB unless otherwise indicated)*

### 1 BASIS OF PREPARATION

The interim financial report has been prepared in accordance with the applicable disclosure provisions of the Rules Governing the Listing of Securities on The Stock Exchange of Hong Kong Limited, including compliance with International Accounting Standard (the "IAS") 34, *Interim financial reporting*, issued by the International Accounting Standards Board (the "IASB"). It was authorised for issue on 21 August 2017.

The interim financial report has been prepared in accordance with the same accounting policies adopted in the 2016 annual financial statements, except for the accounting policy changes that are expected to be reflected in the 2017 annual financial statements. Details of any changes in accounting policies are set out in note 2.

The interim financial report has been prepared assuming the Group will continue as a going concern notwithstanding the net current liabilities of the Group at 30 June 2017. The Directors are of opinion that, based on the working capital forecast of the Group, the Group will have necessary liquid funds to finance its working capital expenditure requirements for a reasonable period of time.

The preparation of an interim financial report in conformity with IAS34 requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses on a year to date basis. Actual results may differ from these estimates.

The interim financial report contains condensed consolidated financial statements and selected explanatory notes. The notes include an explanation of events and transactions that are significant to an understanding of the changes in financial position and performance of the Group since the 2016 annual financial statements. The condensed consolidated interim financial statements and notes thereon do not include all of the information required for full set of financial statements prepared in accordance with IFRSs.

The interim financial report is unaudited, but has been reviewed by KPMG 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 HKICPA.

### 2 CHANGES IN ACCOUNTING POLICIES

The IASB has issued several amendments to IFRSs that are first effective for the current accounting period of the Group. None of these developments has had a material effect on how the Group's results and financial position for the current or prior periods have been prepared or presented in the interim financial report.

The Group has not applied any new standard or interpretation that is not yet effective for the current accounting period.

## 3 SEGMENT REPORTING

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 for the purposes of resource allocation and performance assessment, the Group has presented the following two reportable segments, which are Dairy farming and Dairy products production. 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 management to make decisions about resources to be allocated to each segment and assess its performance.

– Dairy farming – breeding dairy cows to produce and sell raw milk.

– Dairy products production – producing and selling Pasteurised Milk, Ultra High Temperature Milk ("UHT Milk"), Modified Milk, Yogurt and Other Dairy Products.

### (a) Segment results, assets and liabilities

For the purposes of assessing segment performance and allocating resources between segments, the Group's most senior executive management monitors the results, assets and liabilities attributable to each reportable segment on the bases as they are presented in the Group's financial statements.

Information regarding the Group's reportable segments as provided to the Group's most senior executive management for the purposes of resource allocation and assessment of segment performance for the period is set out below:

| | **Six months ended 30 June 2017** | | |
|---|---|---|---|
| | **Dairy farming** | **Dairy products production** | **Total** |
| | *RMB'000* | *RMB'000* | *RMB'000* |
| **Revenue** | | | |
| Revenue from external customers | **90** | **291,585** | **291,675** |
| Inter-segment revenue | **75,778** | **–** | **75,778** |
| **Reportable segment revenue** | **75,868** | **291,585** | **367,453** |
| **Reportable segment profit (adjusted EBITDA)** | **28,047** | **53,055** | **81,102** |

| | **At 30 June 2017** | | |
|---|---|---|---|
| | **Dairy farming** | **Dairy products production** | **Total** |
| | *RMB'000* | *RMB'000* | *RMB'000* |
| **Reportable segment assets** | **692,657** | **1,214,861** | **1,907,518** |
| **Reportable segment liabilities** | **499,551** | **624,371** | **1,123,922** |

| | Six months ended 30 June 2016 | | |
|---|---|---|---|
| | **Dairy farming** | **Dairy products production** | **Total** |
| | *RMB'000* | *RMB'000* | *RMB'000* |
| **Revenue** | | | |
| Revenue from external customers | 78 | 322,136 | 322,214 |
| Inter-segment revenue | 54,071 | – | 54,071 |
| **Reportable segment revenue** | 54,149 | 322,136 | 376,285 |
| **Reportable segment profit (adjusted EBITDA)** | 13,588 | 88,210 | 101,798 |

| | At 31 December 2016 | | |
|---|---|---|---|
| | **Dairy farming** | **Dairy products production** | **Total** |
| | *RMB'000* | *RMB'000* | *RMB'000* |
| **Reportable segment assets** | 668,598 | 1,108,100 | 1,776,698 |
| **Reportable segment liabilities** | 489,215 | 531,357 | 1,020,572 |

**(b) Reconciliations of reportable segment profit or loss**

| | Six months ended 30 June | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Reportable segment profit | **81,102** | 101,798 |
| Net finance costs | **(9,835)** | (8,246) |
| Depreciation and amortisation | **(23,116)** | (18,463) |
| Loss arising from changes in fair value less costs to sell of biological assets | **(6,894)** | (28,281) |
| Consolidated profit before taxation | **41,257** | 46,808 |

## 4 OTHER NET INCOME

| | Six months ended 30 June | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Government grants | **15,666** | 11,307 |
| Net income from sales of materials | **3,579** | 4,956 |
| Others | **1,841** | 2,246 |
| Total | **21,086** | 18,509 |

## 5 PROFIT BEFORE TAXATION

Profit before taxation is arrived at after charging/(crediting):

### (a) Net finance costs

| | Six months ended 30 June | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Interest income | **(824)** | (1,131) |
| Interest expenses on bank loans | **9,920** | 9,710 |
| Finance charges on obligations under finance leases | **291** | 116 |
| Net foreign exchange loss/(gain) | **448** | (449) |
| Total | **9,835** | 8,246 |

### (b) Other items

| | Six months ended 30 June | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Staff costs | **25,456** | 23,402 |
| Depreciation and amortisation | **23,116** | 18,463 |

## 6 INCOME TAX

Income tax in the consolidated statement of profit or loss represents:

| | Six months ended 30 June | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| **Current taxation** | | |
| PRC income tax | **3,362** | 7,817 |
| **Deferred taxation** | | |
| Origination and reversal of temporary difference | **153** | 1,366 |
| Total | **3,515** | 9,183 |

*Notes:*

(i) The Company and its subsidiaries are subject to the PRC Enterprise Income Tax statutory rate of 25% for the six months ended 30 June 2017.

(ii) Pursuant to the Announcement of the State Administration of Taxation on Issues of Enterprise Income Tax Concerning In-depth Implementation of Western Region Development Strategy (《國家稅務總局關於深入實施西部大開發戰略有關企業所得稅問題的公告》) promulgated by the State Administration of Taxation on 6 April 2012 and effective on 1 January 2011, from 1 January 2011 to 31 December 2020, the Company and its subsidiaries established in the Western Region of the PRC are entitled to the preferential income tax rate of 15%.

(iii) According to the PRC Enterprise Income Tax Law and the Implementation Rules, the Group's income arising from certain agricultural activities is exempted from Enterprise Income Tax.

## 7 BASIC AND DILUTED EARNINGS PER SHARE

The calculation of basic earnings per share is based on the profit attributable to ordinary equity shareholders of the Company of RMB37,742,000 (six months ended 30 June 2016: RMB37,625,000) and the weighted average of 140,500,000 ordinary shares (2016: 140,500,000 ordinary shares) in issue during the interim period.

There was no difference between basic and diluted earnings per share as there were no dilutive potential shares outstanding during the six months ended 30 June 2017 and 2016.

## 8 BIOLOGICAL ASSETS

### (a) Nature of the Group's agricultural activities

Biological assets of the Group are dairy cows held to produce raw milk.

The quantity of the dairy cows owned by the Group as at 30 June 2017 and 31 December 2016 is shown below. The Group's dairy cows are milkable cows held for raw milk production and heifers and calves that have not reached the age to produce raw milk.

| | **At 30 June 2017** | At 31 December 2016 |
|---|---|---|
| | ***Heads*** | *Heads* |
| Milkable cows | **2,853** | 2,560 |
| Heifers | **1,583** | 1,534 |
| Calves | **644** | 1,008 |
| Total | **5,080** | 5,102 |

In general, the heifers are inseminated when they reach approximately 14 months old. After a gestation period of approximately 10 months, a calf is born and the heifers begin to produce raw milk and the lactation periods begin. The heifers, at this time, will be transferred to the group of milkable cows. A milkable cow is typically milked for approximately 300 days in each lactation period and has as many as 6 lactation periods. The male calves newly born are sold while the female calves are bred for 6 months and then transferred to the group of heifers for preparation of insemination.

### (b) Value of the Group's biological assets

The amounts of the dairy cows are as below:

| | At 30 June 2017 *RMB'000* | At 31 December 2016 *RMB'000* |
|---|---|---|
| Milkable cows | **86,988** | 80,869 |
| Heifers | **32,709** | 32,914 |
| Calves | **8,818** | 12,506 |
| Total | **128,515** | 126,289 |

The fair value of the Group's dairy cows as at 30 June 2017 were estimated by using the same valuation techniques as adopted in the consolidated financial statements of the Group for the year ended 31 December 2016.

## 9 TRADE RECEIVABLES

| | At 30 June 2017 *RMB'000* | At 31 December 2016 *RMB'000* |
|---|---|---|
| Trade receivables due from third parties | **23,389** | 14,149 |
| Less: allowance for impairment of doubtful debts | **(65)** | (113) |
| Total | **23,324** | 14,036 |

### (a) Ageing analysis

As of the end of the reporting period, the ageing analysis of trade receivables, based on the invoice date and net of allowance for doubtful debts, is as follows:

| | At 30 June 2017 *RMB'000* | At 31 December 2016 *RMB'000* |
|---|---|---|
| Less than 3 months | **19,812** | 11,799 |
| More than 3 months but less than 6 months | **2,589** | 1,730 |
| More than 6 months but less than 12 months | **881** | 434 |
| More than 1 year but less than 2 years | **5** | 58 |
| More than 2 years but less than 3 years | **37** | 15 |
| Total | **23,324** | 14,036 |

**(b) Impairment of trade receivables**

Impairment losses in respect of trade receivables are recorded using an allowance account unless the Group is satisfied that recovery of the amount is remote, in which case the impairment loss is written off against trade receivables directly.

The movement in the allowance for doubtful debts during the period, including both specific and collective loss component, is as follows:

| | **At 30 June 2017** *RMB'000* | At 31 December 2016 *RMB'000* |
|---|---|---|
| At 1 January | **113** | 668 |
| Impairment losses recognised | **42** | 170 |
| Impairment losses reversed | **(90)** | (318) |
| Uncollectible amounts written off | **–** | (407) |
| At 30 June/31 December | **65** | 113 |

At 30 June 2017, the Group's trade receivable of RMB65,000 (31 December 2016: RMB113,000) were individually or collectively determined to be impaired. Consequently, specific allowances for doubtful debts were recognised. The Group does not hold any collateral over these balances.

**(c) Trade receivables that are not impaired**

The ageing analysis of trade receivables that are neither individually nor collectively considered to be impaired are as follows:

| | **At 30 June 2017** *RMB'000* | At 31 December 2016 *RMB'000* |
|---|---|---|
| Neither past due nor impaired | **22,741** | 13,450 |
| Past due but not impaired | **583** | 586 |
| Total | **23,324** | 14,036 |

Receivables that were neither past due nor impaired relate to a wide range of customers for whom there was no recent history of default.

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

## 10 TRADE AND BILLS PAYABLES

| | At 30 June 2017 *RMB'000* | At 31 December 2016 *RMB'000* |
|---|---|---|
| Trade payable for purchase of raw milk, packing material and auxiliary material | **55,072** | 60,755 |
| Trade payable for purchase of forage and veterinary medicine | **19,388** | 19,413 |
| Bills payable | **28,495** | 4,000 |
| Total | **102,955** | 84,168 |

All of the trade and bills payables of the Group are expected to be settled within one year.

As of the end of the reporting period, the ageing analysis of trade and bills payables is as follows:

| | At 30 June 2017 *RMB'000* | At 31 December 2016 *RMB'000* |
|---|---|---|
| Less than 3 months | **53,234** | 72,378 |
| More than 3 months but less than 6 months | **41,921** | 4,562 |
| More than 6 months but less than 12 months | **5,262** | 5,257 |
| More than 1 year but less than 2 years | **998** | 725 |
| More than 2 years | **1,540** | 1,246 |
| Total | **102,955** | 84,168 |

## 11 DIVIDENDS

(i) The board of directors of the Company has resolved not to declare an interim dividend for the six months ended 30 June 2017.

(ii) Dividends payable to equity shareholders attributable to the previous financial year, approved during the interim period

| | **Six months ended 30 June** 2017 *RMB'000* | 2016 *RMB'000* |
|---|---|---|
| Final dividend in respect of the previous financial year, approved during the following interim period, of RMB7.42 cents per share (six months ended 30 June 2016: RMB7.12 cents per share) | **10,425** | 10,004 |
| Total | **10,425** | 10,004 |

The dividends have been substantially paid out upon the approval of the interim financial report.

## MANAGEMENT DISCUSSION AND ANALYSIS

### Business Overview

We are one of the leading dairy companies in Gansu and Qinghai where our operations and sales are primarily located and we operate a vertically integrated business model. Our vertically integrated business model covers the critical stages of the dairy industry value chain, from dairy farming, to manufacturing, and then to marketing and sales of dairy products. Our dairy farming operations aim to ensure stable supply of high quality raw milk for our dairy products manufacturing. We owned and operated four dairy farms and collectively operated four dairy farms through cooperation with local dairy farmers. Our strategy is to expand the herd size of dairy cows in our self-operated dairy farms and existing collectively-operated dairy farms so as to maintain approximately 60% of our raw milk requirement that could be sourced internally in the near future, which will enable us to achieve balanced, complementary yet diverse sources of raw milk supply to satisfy our dairy product manufacturing need. We believe our vertically integrated business model allows stringent control over each important process of dairy production and thereby guarantees the high quality and safety of our dairy products.

We offer a broad range of dairy products tailored to the needs and taste preferences of different consumer groups. Our principal products sold to retail consumers, mainly through distributors and sales agents, include (i) liquid milk products, which comprise pasteurised milk (i.e., fresh milk), UHT milk, modified milk and yogurt, and (ii) milk beverages. We place strong emphasis on our product development to continuously develop new products that meet the evolving tastes and preference of our consumers, which differentiates us from our competitors in the region.

We are a major player on the sale of "Cold Chain Liquid Milk Products" (i.e., liquid milk products that have a short shelf life between 3 days to 21 days and need to be stored at low temperature of 2°C – 6°C, which include pasteurised milk and yogurt products) in the Gansu and Qinghai regional market. We believe that we are well positioned to compete in the Cold Chain Liquid Milk Product market in Gansu and Qinghai due to our close proximity to the local market and our established local distribution network. We plan to continue to expand our cold chain production capacity and distribution network to increase the sales of Cold Chain Liquid Milk Products in the Gansu and Qinghai regional market and then further expand into other provinces in the northwestern China market.

While focusing on the Cold Chain Liquid Milk Product market, we also leveraged on our strong brand recognition in the regional market to continue to strengthen the sales of our popular UHT milk and modified milk products, thereby maintaining our diversified product offerings. Going forward, we intend to continue our efforts in the sales of our UHT milk and modified milk products that are popular among local customers to maintain our diversified product offerings.

***Dairy Farming***

- *Number of dairy cows*

During the Reporting Period, our biological assets comprised dairy cows. Dairy cows are further categorised into calves, heifers and milkable cows. The following table sets out the number of our dairy cows as at 30 June 2017 and 31 December 2016:

| | **At 30 June 2017** *Heads* | At 31 December 2016 *Heads* |
|---|---|---|
| Milkable cows | **2,853** | 2,560 |
| Heifers | **1,583** | 1,534 |
| Calves | **644** | 1,008 |
| **Total** | **5,080** | 5,102 |

- *Milk yield*

We produced approximately 12,820 tonnes of raw milk for the Reporting Period, representing an increase of approximately 25.6% from about 10,209 tonnes in the corresponding period in 2016. The improved results were mainly attributable to the increase in average milk yield per milkable cow per annum.

Our average milk yield per milkable cow per annum increased from 6.0~7.4 tonnes during the six months ended 30 June 2016 to 6.4~8.6 tonnes during the Reporting Period.

***Dairy Products Production***

During the Reporting Period, the level of competition in the market of domestic dairy products, especially liquid milk products, continuously increased. In response to these market conditions, we continuously optimized our product mix using our advantages of milk sources produced by our own dairy farms and quality dairy products with high protein and fresh dairy milk products, thus strengthening our differentiated competitiveness, and focused on developing the northwestern China market.

- *Optimizing Liquid Milk Product Mix*

Product mix has affected our revenue, gross profit and gross profit margin in the past. We continued to place effort to increase the proportion of sales of Cold Chain Liquid Milk Products, which we believe will represent the consumer preferences in the near future and will provide higher selling prices and higher gross profit margin to us compared to other dairy products. We have established an extensive distribution network for our Cold Chain Liquid Milk Products in the Gansu and Qinghai regional market and purchased additional package lines which are designed for packaging of pateurised milk and yogurt products to expand our production and increase the sales of Cold Chain Liquid Milk Products.

We plan to further increase the sales of Cold Chain Liquid Milk Products and other high margin products. We plan to further expand our cold chain production facilities and distribution network in Gansu and Qinghai by purchasing additional packaging lines, constructing additional cold warehouses and vending machines. We expect sales of our Cold Chain Liquid Milk Products and high-margin products will continue to increase in the foreseeable future.

- *Expansion of our Distribution Network*

  We rely on our distribution network to sell our dairy products to end consumers. The effectiveness and geographic reach of our distribution network and sales force directly impact our sales. We have established a distribution network comprising various sales channels covering most of the local markets in Gansu and Qinghai. As at 30 June 2017, we had entered into distribution agreements with 305 distributors and 144 sales agents, as compared to 303 distributors and 168 sales agents as at 31 December 2016. To further promote our branded dairy products across the region, we aim to enhance our distribution network to deepen our regional sales and distribution network and solidify our established position in our primary markets. Furthermore, we are also expanding our distribution network into the China national market, especially in the northwestern China region.

- *Average Selling Price of our Liquid Milk Products*

  Our revenue and profitability are affected by the average selling price of our liquid milk products, which in turn, is determined by prevailing market conditions, cost of raw materials, production costs and competition. The average selling price of our liquid milk products decreased slightly from RMB9,527 per tonne in the six months ended 30 June 2016 to RMB9,462 per tonne in the Reporting Period. We believe our ability to maintain a relatively high average selling price for our liquid milk products was primarily due to the high quality of our products and our ability to develop and launch new products catered to the evolving tastes and preferences of local consumers, as well as our success in changing the product mix of our liquid milk products to focus on marketing and sales of Cold Chain Liquid Milk Products and other high margin products.

***Quality Control***

Product safety management and quality control are our core values and of paramount importance to our business. We implement stringent quality control and production safety management measures throughout our production process from the procurement of feeds, dairy farming, raw milk sourcing and processing to production, packaging, storage and delivery of our products.

Our quality control system is designed based on the Good Manufacturing Practices (GMPs), the Hazard Analysis and Critical Control Points (HACCP) and the Sanitation Standard Operating Procedures (SSOPs).

GMPs are the foundation for our milk safety and milk quality programme. GMPs are implemented in four main areas of our dairy processing, specifying control measures in respect of (i) personnel hygiene; (ii) building and facilities; (iii) equipment and utensils; and (iv) production and process control.

In addition, we have also applied the principles of HACCP in the management of our milk safety. Our HACCP plan focuses on areas where problems potentially may occur and requires that production facilities be prepared to deal with problems immediately if they occur. Under our HACCP plan, we conducted a hazard analysis in order to identify any hazardous biological, chemical or physical properties in raw materials and processing steps. Based on the analysis, we identified the critical control points and establish monitoring procedures and use the monitoring results to streamline processes on a continuous basis. As a testament of our efforts in complying with HACCP, our production plants in Gansu and Qinghai received the HACCP Certification issued by the China Quality Certification Centre and Beijing Continental Hengtong Certification Co. Ltd., respectively.

Furthermore, we have also implemented the SSOP specifying step-by-step procedures needed for processes related to sanitation. Following the SSOP, we focus on key sanitation conditions and requirements, such as the safety of water that comes into contact with dairy products, condition and cleanliness of contact surfaces, prevention of cross-contamination from insanitary objects to dairy product, protection of dairy products and packaging materials, labelling, storage, and use of cleaning solutions and pesticides, control of employee health conditions, and exclusion of pests from the production plant.

Our quality control system is divided into six stages: (i) control over the quality of feeds; (ii) control over the quality of dairy cows; (iii) control over sourcing and processing of raw milk; (iv) control over raw materials and suppliers; (v) control over production process; and (vi) control over storage and delivery of finished products.

***Brand Building***

The liquid milk product industry in China, including Gansu and Qinghai, our major markets, is highly concentrated. The competitive landscape of the dairy product industry in China can be split into three categories: (1) national brands; (2) regional brands; and (3) foreign brands. As a regional brand, we are located near to the market with shorter transportation time that guarantees better freshness. Our products are also more tailored to the taste and spending habits of end consumers. Compared with our competitors, we benefited from a stable supply of raw milk from our suppliers with whom we have developed good relationship over the years.

We believe the demand for premium Cold Chain Liquid Milk Products will continue to rise along with the increased awareness of the importance of nutritional products to the health and well-being of consumers. To capture the increasing demand for Cold Chain Liquid Milk Products, we plan to continue to expand our cold chain distribution network in Gansu and Qinghai and further in northwestern China. We believe that one of the key factors to a successful cold chain distribution network is the strategic location of cold warehouses outside of our production plants as it allows our products to reach local markets within 300 kilometers radius of our cold warehouses and also allows us to have better control over the quality of the Cold Chain Liquid Milk Products during the distribution process.

We also seek to expand our third party distributors to deepen our regional sales and distribution network and solidify our established position in Gansu and Qinghai, our primary markets. We will also continue to develop the e-commerce sales channels and satisfy the demands and preferences of different consumer groups through the internet direct sales portal to reach a wider customer base and to adapt to consumers' purchase preference.

## Financial Overview

### *Revenue*

The following table sets out the breakdown of sales amount, sales volume and average selling price by product types for the six months ended 30 June 2017 and 2016:

| | **Six months ended 30 June** | | | | | |
|---|---|---|---|---|---|---|
| | **2017** | | | 2016 | | |
| | **Sales Amount** *RMB'000* | **Sales Volume** *Tonne* | **Average Selling Price** *RMB/Tonne* | Sales Amount *RMB'000* | Sales Volume *Tonne* | Average Selling Price *RMB/Tonne* |
| **Liquid Milk Products** | | | | | | |
| Pasteurised Milk | **9,690** | **1,121** | **8,644** | 9,572 | 1,131 | 8,463 |
| UHT Milk | **54,215** | **8,253** | **6,569** | 51,109 | 8,132 | 6,285 |
| Modified Milk | **102,194** | **11,555** | **8,844** | 107,215 | 12,073 | 8,881 |
| Yogurt | **122,571** | **9,580** | **12,794** | 151,212 | 12,159 | 12,436 |
| **Subtotal** | **288,670** | **30,509** | **9,462** | 319,108 | 33,495 | 9,527 |
| **Milk Beverage** | **1,975** | **454** | **4,350** | 2,075 | 428 | 4,848 |
| **Other Dairy Products** | **1,030** | **22** | **46,818** | 1,031 | 36 | 28,639 |
| **Total** | **291,675** | **30,985** | **9,413** | 322,214 | 33,959 | 9,488 |

Our revenue decreased by 9.5% from RMB322.2 million for the six months ended 30 June 2016 to RMB291.7 million for the Reporting Period, primarily due to the decrease in our sales of liquid milk products, particularly the yogurt products.

The decrease of our liquid milk business was due to the decrease in the total volume of liquid milk products sold in Qinghai and fierce competition from national brands. During the Reporting Period, the total volume of dairy products sold decreased by 8.8% from approximately 33,959 tonnes for the six months ended 30 June 2016 to approximately 30,985 tonnes for the Reporting Period, primarily due to the decrease in the sales volume of yogurt products.

*Gross profit and gross profit margin*

The following table sets forth the breakdown of our cost of sales and gross profit by our product types, as well as their respective gross profit margin after biological assets fair value adjustments, for the periods indicated:

| | Six months ended 30 June | | | | | |
|---|---|---|---|---|---|---|
| | **2017** | | | 2016 | | |
| | **Cost of sales** *RMB'000* | **Gross Profit** *RMB'000* | **Gross profit margin** % | Cost of sales *RMB'000* | Gross Profit *RMB'000* | Gross profit margin % |
| **Liquid Milk Products** | | | | | | |
| Pasteurised Milk | **5,406** | **4,284** | **44.2** | 5,072 | 4,500 | 47.0 |
| UHT Milk | **44,767** | **9,448** | **17.4** | 38,735 | 12,374 | 24.2 |
| Modified Milk | **66,771** | **35,423** | **34.7** | 70,119 | 37,096 | 34.6 |
| Yogurt | **79,507** | **43,064** | **35.1** | 94,128 | 57,084 | 37.8 |
| **Subtotal** | **196,451** | **92,219** | **31.9** | 208,054 | 111,054 | 34.8 |
| **Milk Beverage** | **1,467** | **508** | **25.7** | 1,478 | 597 | 28.8 |
| **Other Dairy Products** | **661** | **369** | **35.8** | 1,104 | -73 | -7.1 |
| **Total cost of sales/Total gross profit/ Overall gross profit margin** | **198,579** | **93,096** | **31.9** | 210,636 | 111,578 | 34.6 |

Our overall gross profit margin of our dairy products after taking into account biological assets fair value adjustments was 31.9% for the Reporting Period and 34.6% for the corresponding period in 2016. The decrease in the overall gross profit margin during the Reporting Period was primarily due to the increase of purchase price of raw milk. The average raw milk purchase price increased by about 6.9% from RMB3.60/kg for the six months ended 30 June 2016 to RMB3.85/kg for the Reporting Period.

*Gain arising on initial recognition of agricultural produce at fair value less costs to sell at the point of harvest*

Our gain arising from initial recognition of agricultural produce at fair value less costs to sell at the point of harvest increased from RMB4.9 million for the six months ended 30 June 2016 to RMB7.2 million for the Reporting Period. The increase was mainly due to the increase of milk yield during the Reporting Period compared to the corresponding period in 2016.

*Loss arising from changes in fair value less costs to sell of biological assets*

We recorded loss arising from changes in fair value less costs to sell of biological assets amounted to RMB6.9 million for the Reporting Period, which decreased by 75.6% from RMB28.3 million for the corresponding period in 2016, primarily contributable to the improved milk yield and the fluctuation of raw milk price compared with the corresponding period of last year.

***Other net income***

Other net income includes government grants, net income from sales of materials and other income. Government grants are generally obtained from our agricultural activities. For the six months ended 30 June 2017 and 2016, government grants we recognized amounted to RMB15.7 million and RMB11.3 million, and net income from sales of materials we recognized amounted to RMB3.6 million and RMB5.0 million, respectively.

***Operating expenses***

| | **Six months ended 30 June** | |
|---|---|---|
| | **2017** | 2016 |
| | ***RMB'000*** | *RMB'000* |
| Distribution costs | **33,469** | 26,247 |
| Administrative expenses | **29,906** | 25,405 |
| Total operating expenses | **63,375** | 51,652 |

Our operating expenses increased from RMB51.7 million for the six months ended 30 June 2016 to RMB63.4 million for the Reporting Period.

The increase in distribution costs during the Reporting Period was mainly due to: (1) the increase in transportation cost and staff cost to promote sales in the fierce market competition; (2) the increase in the marketing expenses for the purpose of securing higher sales growth and gaining larger market shares in regional key market and further exploring the national market for our Cold Chain Liquid Milk Products.

The administrative expenses increased primarily because there was cost incurred relating to the proposed A Shares offering during the Reporting Period.

***Net finance costs***

Our net finance costs increased by 19.5% from RMB8.2 million for the six months ended 30 June 2016 to RMB9.8 million for the Reporting Period, primarily due to increased interest expenses resulting from increased average bank loans utilized during the Reporting Period.

***Current ratio and net gearing ratio***

As at 30 June 2017, our current ratio (current assets/current liabilities) was approximately 0.87 compared to 0.79 as at 31 December 2016. As at 30 June 2017, the net gearing ratio was 5.0% compared to 11.1% as at 31 December 2016. Net gearing ratio was calculated by net debt (aggregated bank loans and obligations under finance leases net of cash and cash equivalents as at the ending of the period/year) over total equity attributable to equity shareholders of the Company.

*Liquidity and capital resources*

During the Reporting Period, we financed our operations primarily through net cash inflows from our daily operations and proceeds from bank loans. As at 30 June 2017 and 31 December 2016, we had RMB394.4 million and RMB273.4 million in cash and cash equivalents, respectively, which was mainly denominated in Renminbi and primarily consisted of cash on hand and bank deposits.

*Capital expenditures*

We had capital expenditures of RMB10.2 million and RMB72.3 million for the six months ended 30 June 2017 and 2016, respectively, which were primarily used in purchasing property, plant and equipment, procuring dairy cows  and settling land leases.

*Working capital*

As at 30 June 2017, we had net current liabilities of RMB74.6 million (31 December 2016: net current liabilities of RMB103.8 million).

*Indebtedness*

During the Reporting Period, our borrowings were denominated in Renminbi. As at 30 June 2017, our outstanding short-term bank loans, including long-term loans due within one year, amounted to RMB399.6 million at interest rates ranging from 4.35%~8.00% per annum. As at 30 June 2017, our outstanding long-term bank loans, net of amount due within one year, amounted to RMB29.6 million at interest rates ranging from 5.39%~5.488% per annum.

The management believes that the existing financing resources will be sufficient to meet current operations, current and future expansion plans and, if necessary, we will be able to obtain additional financing with favorable terms. There is no material effect of seasonality on our borrowing requirements.

For the Reporting Period, we were not subject to significant exposure to interest rate risk. Hence, no financial instrument for hedging was employed.

*Contingent liabilities*

As at 30 June 2017 and 31 December 2016, we did not have significant contingent liabilities.

*Use of Proceeds from Listing*

The Company was listed on the Main Board of the Stock Exchange on 15 October 2015 (the "**Listing**"). Net proceeds from the Listing amounted to approximately RMB116.0 million.

We set out below the status of the application of the net proceeds from the issue of shares in connection with the Listing:

| | As of 30 June 2017 | |
|---|---|---|
| | **Actual amount used** | **Intended amount to be used** |
| | *RMB'000 (%)* | *RMB'000 (%)* |
| Financing a portion of the funds required to import approximately 5,000 dairy cows from Australia or New Zealand | 81,222 (70.0%) | 81,222 (70.0%) |
| Promoting our brands | 9,275 (8.0%) | 23,206 (20.0%) |
| Working capital and other general corporate purposes | 11,603 (10.0%) | 11,603 (10.0%) |
| IPO proceeds not utilized | 13,931 (12.0%) | N/A |
| **Total** | **116,031 (100%)** | **116,031 (100%)** |

*Note:* The Board resolved to reallocate the net proceeds which were no longer needed for the originally designed purpose to support other purposes of use of proceeds. For details, please refer to the announcement of the Company dated 26 October 2016.

**Human Resources**

We had 712 employees in Mainland China and Hong Kong as at 30 June 2017 (31 December 2016: 748 employees). During the Reporting Period, total staff costs, including the portion accounted for in the profit and loss statement and capitalised to assets but excluding independent non-executive Directors' fees, were approximately RMB26.2 million (the corresponding period in 2016: RMB23.9 million).

Our remuneration policies aim to attract, retain and incentivize talents to ensure competency of our team in implementing our business strategies and to maximize shareholder value. We will regularly review our remuneration policies and employee benefits with reference to market practices and performance of individual employees.

For the employees in the PRC, we have participated in defined contribution retirement plans and social insurance plans organised by the relevant local governmental authorities. For the employees in Hong Kong, we participate in the mandatory provident fund scheme with contributions calculated in accordance with the provisions under the Mandatory Provident Fund Schemes Ordinance (Chapter 485 of the Laws of Hong Kong).

### Corporate Social Responsibility

We believe that social responsibility is the foundation for the development of an enterprise. In our opinion, taking part in social welfare activities is an important method for an enterprise to give back to the society, as well as a key way for an enterprise to achieve mutual development and advancement with the society.

## OUTLOOK

Our goal is to further strengthen our regional market leading position and brand recognition in Gansu and Qinghai. To achieve this goal, we plan to implement the following strategies:

- Pursue our branding strategies to strengthen our branding positions under our different brands, increase our market shares and enhance consumer loyalty;

- Upgrade our cold chain distribution facilities to strengthen our regional market leader position in Gansu and Qinghai and expand our sales and distribution network;

- Improve our raw milk production capacity and quality to satisfy the needs of our fast growing business; and

- Enrich our product portfolio to address changing consumer preferences and offer new tasting experience to inspire demands for our products through our continuous product development efforts.

## IMPORTANT EVENTS THAT HAVE OCCURRED SINCE 30 JUNE 2017

Subsequent to 30 June 2017, there had been no significant change in our principal business, pricing policy and costs structure.

On 3 August 2017, the Board passed the resolutions regarding the proposal on the extension of the validity period of the Shareholders' approval for the proposed initial public offering of not more than 46,840,000 A Shares in the PRC on the Shenzhen Stock Exchange, which is subject to approval of extraordinary general meeting and class meetings to be held on 29 September 2017. For further details, please refer to the announcement of the Company dated 3 August 2017, the notice of extraordinary general meeting of the Company, the notice of domestic Shareholders' class meeting and H Shareholders' class meeting, all dated 14 August 2017.

## CORPORATE GOVERNANCE

We are committed to ensuring high standards of corporate governance at all times and in all aspects of our operations. The Board believes that good corporate governance is an essential element in enhancing the confidence of current and potential shareholders, investors, employees, business partners and the community as a whole. The Board strives to adhere to the principles of corporate governance and has further strengthened and improved its internal controls in order to undertake sound corporate governance code provisions and practices to meet the relevant statutory and commercial standards by focusing on internal control, fair disclosure and accountability to all shareholders.

Pursuant to code provision (the "**Code Provision**") A.2.1 of the Corporate Governance Code, the responsibilities between the chairman and the chief executive officer should be segregated and should not be performed by the same individual. However, the Company does not have a separate chairman and chief executive officer and Mr. Ma Hongfu currently performs both roles. The Board believes that vesting the roles of both chairman and chief executive officer in the same person has the benefit of ensuring consistent leadership within the Group and enables more effective and efficient overall strategic planning for the Group. The Board considers that the balance of power and authority for the present arrangement will not be impaired and this structure will enable the Company to make and implement decisions promptly and effectively. The Board will continue to review and consider splitting the roles of chairman of the Board and chief executive officer of the Company at a time when it is appropriate and suitable by taking into account the circumstances of the Group as a whole.

Save for the above, the Company has complied with all applicable Code Provisions of the Corporate Governance Code and Corporate Governance Report as set out in Appendix 14 to the Listing Rules for the Reporting Period since the Company was listed on the Stock Exchange.

## SECURITIES TRANSACTIONS BY DIRECTORS AND SUPERVISORS

The Company has adopted the Model Code for Securities Transactions by Directors of Listed Issuers (the "**Model Code**") as set out in Appendix 10 to the Listing Rules regarding directors' securities transactions. Having made specific enquiry of all Directors and the supervisors of the Company (the "**Supervisors**"), all the Directors and Supervisors confirm that they have complied with the required standards of the Model Code during the Reporting Period.

## PURCHASE, REDEMPTION OR SALE OF LISTED SECURITIES OF THE COMPANY

During the Reporting Period, there was no repurchase, sale or redemption by the Company, or any of its subsidiaries, of any listed securities of the Company.

## MATERIAL LITIGATION AND ARBITRATION PROCEEDINGS

The Group has no material litigation or arbitration proceedings during the Reporting Period.

## SHARE OPTION SCHEME

There is no Share Option Scheme adopted for the Company during the Reporting Period.

## REVIEW OF INTERIM RESULTS

The Company has established the audit committee (the "**Audit Committee**") with written terms of reference in compliance with the Listing Rules. The Audit Committee comprises three independent non-executive Directors, namely Ms. Liu Zhijun, Ms. Xin Shihua and Mr. Wong Cho Hang Stanley. Ms. Liu Zhijun is the chairman of the Audit Committee. The Audit Committee is responsible for, amongst other matters, reviewing and supervising the Group's financial reporting process and internal control system and providing advice and recommendations to the Board. The Audit Committee has amongst others, reviewed and discussed with the management the accounting principles and practices adopted by the Group and the Group's internal controls and financial reporting matters, including the review of the unaudited interim results of the Group for the Reporting Period.

## DIVIDEND

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

## PUBLICATION OF INTERIM RESULTS ANNOUNCEMENT AND INTERIM REPORT

The interim results announcement is published on the Company's website (http://www.lzzhuangyuan.com/) and the Stock Exchange's website (http://www.hkexnews.hk). The interim report of the Company for the Reporting Period will be despatched to the Shareholders and will be made available on the websites of the Company and the Stock Exchange in due course.

By order of the Board
**Lanzhou Zhuangyuan Pasture Co., Ltd.***
**Ma Hongfu**
*Chairman*

Lanzhou, the PRC, 21 August 2017

*As at the date of this announcement, the executive directors of the Company are Mr. Ma Hongfu, Mr. Wang Guofu, Mr. Chen Yuhai and Mr. Yan Bin; the non-executive directors of the Company are Mr. Yap Kean Chong and Mr. Song Xiaopeng; and the independent non-executive directors of the Company are Ms. Liu Zhijun, Ms. Xin Shihua and Mr. Wong Cho Hang Stanley.*

* *For identification purpose only*