

CHINA XIANGTAI FOOD CO., LTD.

Raising Forecasts Following Acquisition and New Joint Venture Price Target Upgrade Under Review

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CHINA XIANGTAI FOOD CO., LTD. (NASDAQ – PLIN - \$1.70)

Industry: Consumer Goods/Defensive

Price Target: \$6.70

COMPANY SNAPSHOT

Headquartered in Chongqing, China Xiangtai Food Co., Ltd, is a food company primarily engaged in pork processing. The Company's operations span key sections of the pork processing value chain, including slaughtering, packing, distribution, and wholesale of a variety of fresh pork meat and parts. Primarily focused on pork products, PLIN also offers other fresh and processed products, including beef, lamb and poultry.

KEY STATISTICS

Price as of 5/5/20	\$1.70
52 Week High – Low	\$6.00 - \$1.30
Est. Shares Outstanding	22.0M
Market Capitalization	\$37.4M
Average Volume	182,169
Exchange	NASDAQ

COMPANY INFORMATION

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INVESTMENT HIGHLIGHTS

Conclusion: PLIN has announced major initiatives which should substantially increase the Company's financial performance and drive the stock toward our \$6.70 price target, which reflects 13x our upwardly revised FY21 operating income forecast in our basic (non-roll up) P&L model.

PLIN closes accretive, complementary acquisition. In a matter of weeks, PLIN not only executed a highly profitable and accretive complementary business acquisition but closed on a major joint venture which provides the Company with unrivalled positioning through vertical integration. The acquisition in particular enables PLIN to expand the southwest market in China but also add roughly \$70 million, or a 70% rise in annualized sales.

New, 10-year JV bolsters integration. Meanwhile, the recently announced a 10-year joint venture with Chongqing Fengjie County Rural Ecological Agriculture Development Co., Ltd. ("FEA") increases PLIN's vertical integration by immediately adding hog breeding capabilities. Pork is a major food staple in China and PLIN is a leading provider throughout the food chain.

New forecasts, price target under review, more deals in the offing. Given the recent events, we have raised key forecasts and our price target is under review for a potential upgrade as well. Plus, it appears additional business development opportunities are in the offing later this year, enabling PLIN to establish a stronghold in this sector. Publicly traded pork companies such as Hormel are near year highs as this category serves as a popular defensive group during these difficult economic and market conditions. As a US-traded pure play on this sector in China, PLIN could follow a similar path.

COMPANY BACKGROUND

Headquartered in Chongqing, NASDAQ-listed **China Xiangtai Food Co., Ltd. (NASDAQ – PLIN)** is a leading player in the pork processing industry

that has unique, vertically integrated operations across key sections of the industry value chain in China, including slaughtering, packing, distribution, and the wholesale of fresh pork meat and parts. As such, the Company offers processed and fresh products which are primarily sold through farmer's markets and supermarkets/grocery stores via local distributors, small wholesalers and retail vendors. The main products from the processed series include shredded meat, sliced meat, meat stuffing, pickled meat, lamb and offal, sausage, bacon, steamed meat, breaded chicken and spicy meat.

Interestingly, 70-80% of sales are derived from the distribution of fresh pork. However, a shift and interest in ready-to-eat processed pork (such as sausages) and interest in frozen pork which is available for sale in the supermarket/grocery store channel is on the rise. Plus, the Company can offer frozen pork imported from other countries. Not only does this aid in revenue for the company but raises gross profit as well. The greater the processed pork comprises sales the greater the profit. Moreover, production capacity for the Company's high quality and broad offering slate, coupled with its diversified sales channels positions PLIN in rare company. We would not be surprised to see PLIN emerge as the "Hormel Foods" (NYSE – HRL - \$48.27) of China in the coming years.

Pork is a key staple of the protein diet in China and strong demand exists with upside potential in the form of fast-growing product categories such as processed/ready-to-eat and frozen (domestic and imported) along with new channels such as online order and delivery. According to a report by China-Industrial Research Institute, frozen pork sales are expected to grow by 62% from 2015 to 2020, with 60 million tons consumed. Plus, the channels in which product is sold is clearly moving toward supermarkets and even restaurants and hotels—with the growth rate expected to reach around 27% from 2015 to 2020.

China is the largest pork production and consumption market in the world, comprising 49.25% and 50.2% of the global production and consumption markets respectively in 2015. Pork is deeply rooted in Chinese culture and diet and comprised 61.9% of China's meat consumption in 2015. The growing demand for fresh pork and packaged pork products is attributable to the rise in disposable income and living standards, continuing urbanization, expansion of middle class, the important role of animal protein in food consumption, the importance of pork as a source of animal protein and increasing demand for high quality and safe products, such as those produced by PLIN.

RECENT EVENTS

The Acquisition

On April 3, 2020, PLIN announced that the Company, through its subsidiary Chongqing Jinghuangtai Enterprise Management Consulting Co., Ltd., entered into a definitive agreement to acquire a 51% controlling interest in Chongqing Ji Mao Cang Feed Co., Ltd. ("JMC"). Founded in 2012, Chongqing Ji Mao Cang Feed Co., Ltd (JMC). is a private enterprise specializing in feed raw material sales and feed formula solutions. JMC

has entered strategic alliances with large grain and oil companies such as Sinograin, COFCO, Cargill, Good Ocean, and Louis Dreyfus, and has obtained general distributorship in Chongqing, Sichuan and other places. JMC has more than 200 customers in the farm industry and nearly 100 customers in the feed production industry. In addition to adding an estimated \$70M in annualized revenue, including the sale of more than 200,000 tons of soybean meal, the acquisition is expected to help the Company expand its market in Southwest China.

Pursuant to the Agreement, subject to certain milestones to be achieved by JMC, the Company agreed to issue to JMC a total of 2,000,000 shares of the Company's ordinary share for consideration equal to \$7,420,000 over the next two years. Management believes that business and profitability will benefit from this expanded vertical integration of the industry supply chain and network.

The Joint Venture

In late April, PLIN announced that through its primary operating subsidiary Chongqing Penglin Food Co., Ltd, the Company has entered into a joint venture framework agreement with Chongqing Fengjie County Rural Ecological Agriculture Development Co., Ltd. (FEA), a private enterprise specializing in hog breeding business. Pursuant to the ten-year agreement, the Company and FEA have agreed to jointly establish a hog breeding farm, thus enabling the Company to secure its own supply chain.

Management believes that the expansion into the breeding business demonstrates its confidence in the pork market in China. Moreover, the joint venture will enable the Company to control the supply end of its products and proudly offer 'from farm to supermarket' service. The company will have the entire integrated product chain, including breeding, producing, butchering, packaging and selling and will have a favorable impact on profit margins. The JV leadership plans to purchase up to 300 breeding hogs by the end of September and PLIN expects to start producing its own pigs in February 2021. Once in full operation, the JV expects to produce 7500 hogs annually, with approximately 100 kg to 150 kg per hog. We believe that the sales from producing hogs would be millions of dollars per year.

NEW FORECASTS

As noted above, the aforementioned major business initiatives should substantially increase the Company's financial performance and raise its overall profile. As a result, we are raising key line items in the FY20 and FY21 forecasts found in our basic model. It should be noted that our forecasts are produced on our own without direct guidance from the Company. In our original report, we posited that in a non-roll up scenario, PLIN would generate \$102M in revenue for FY20 versus \$102.5M in FY19. With the new information in hand, we have made upward revisions to our forecasts.

Our new FY20 top-line projection of \$119.5M reflects our original basic model revenue plus one quarter's worth of revenue from the (51%) JMC acquisition, as PLIN can now consolidate results. With a boost in gross profit we project operating income of \$6.9M, versus \$5.5M in the year-ago period. For FY21 we now estimate revenue of \$179M, reflecting the core business, the JMC contribution, and revenue from the FEA JV. Improved margins should drive operating profit to \$13M, nearly a doubling of our estimates for FY20. With potential

guidance for line items below the operating line and balance sheet (i.e., minority interest), we plan to update our net income, comprehensive income and EPS forecasts in the coming weeks.

Since future revenue and margins now appear to be higher than originally forecast, our price target is under review for a potential upgrade. In the meantime, our current \$6.70 target reflects 13x our operating income estimate for FY21, using a share count of 23M shares to represent the 2M shares in the JMC deal and other items. It should be noted that as management continues to seek out ways to capture market share and as these deals close, the value of PLINs shares will be driven higher as well.

It should be noted that publicly traded pork companies in the US such as Hormel are near 52-week highs and 26x estimated FY21 EPS as this category serves as a popular defensive group during these difficult economic and market conditions. As a US-traded pure play on this sector in China, PLIN could follow a similar path.

RECENT TRADING HISTORY FOR PLIN

(Source: www.StockCharts.com)





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Rob Goldman founded Goldman Small Cap Research in 2009 and has over 25 years of investment and company research experience as a senior research analyst and as a portfolio and mutual fund manager. During his tenure as a sell side analyst, Rob was a senior member of Piper Jaffray's Technology and Communications teams. Prior to joining Piper, Rob led Josephthal & Co.'s Washington-based Emerging Growth Research Group. In addition to his sell-side experience Rob served as Chief Investment Officer of a boutique investment management firm and Blue and White Investment Management, where he managed Small Cap Growth portfolios and *The Blue and White Fund*.

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